

**Mongolia**

**Mongolia**  
**Project for Capacity Building of**  
**Capital Market in Mongolia**

**Technical Assistance Materials**

**January 2018**

**Japan International Corporation Agency**  
**(JICA)**

**Daiwa Institute of Research Ltd.**  
**Japan Economic Research Institute Inc.**

IL
JR
18-009



**【 Reports】**

Sr.	No.	Date	Title	Document	In charge
3	3	2015/4/4	Report on the current status of Mongolian capital market	Word	consultants
8	8	2016/12/15	Concept paper on Self Regulatory Organization (SRO)	Presentation	consultants
9	9	2017/1/30	Concept paper on Policy Committee	Word	consultants

**【 Training in UB (SOEs): 31 March 2015】**

Sr.	No.	Date	Title	Document	In charge
16	2	2015/3/31	Consulting approach for initial public offering (IPO) & dual listing	Presentation	consultants

**【 Training in UB (Regulatory authority): 27 April - 1 May 2015】**

Sr.	No.	Date	Title	Document	In charge
17	1	2015/4/27	Organizational structure of Financial Services Agency (FSA) and framework of regulation and supervision for securities sector in Japan	Presentation	FSA
18	2		Supervision of securities firms in Japan	Presentation	FSA
19	3		Off-site monitoring	Presentation	FSA
20	4	2015/4/28	An overview of securities inspection	Presentation	FSA/SESC
21	5		Risk evaluation and key indicators in inspection process	Presentation	FSA
22	6		The role of securities firms and the implications	Presentation	consultants
23	7	2015/4/29	Investor's roles	Presentation	consultants
24	8		Stock markets in Asia	Presentation	consultants
25	9		Corporate finance basics	Presentation	consultants
26	10	2015/4/30	Financial analysis basics	Presentation	consultants
27	11		Financials for securities companies	Presentation	consultants
28	12	2015/5/1	Case study - BDSec's annual financial summary	Presentation	consultants

**【 Training in UB (Securities companies): 20&23 May 2016】**

Sr.	No.	Date	Title	Document	In charge
30	2	2016/5/20	IPO & Dual-listing (1): Scheduling	Presentation	consultants
32	4		IPO & Dual-listing (3): Capital policy	Presentation	consultants
33	5	2016/5/23	Business promotion - How to approach potential clients	Presentation	consultants
34	6		Investor education	Presentation	consultants
35	7		Business ethics for securities companies	Presentation	consultants

**【 IPO&DL Seminar No.1 (23 June 2015)】**

Sr.	No.	Date	Title	Document	In charge
37	2	2015/6/23	Costs and benefits of initial public offering (IPO)	Presentation	consultants
38	3		Dual listing: Benefits and introduction of Asian major stock exchanges	Presentation	Daiwa CM HK
39	4		Privatizing state-owned corporations (SOCs) - Lessons from Japanese experiences	Presentation	consultants
41	6		Opportunities for Mongolian companies to IPO in Japan	Presentation	JPX

**【 IPO&DL Seminar No.2 (18 March 2016)】**

Sr.	No.	Date	Title	Document	In charge
44	2	2016/3/18	Innovative thinking in Investor Relations and Corporate Governance	Presentation	Mr. Tatsuya Imade
45	3		Optimizing capital markets through innovations - Lessons from the past & on-going initiatives in foreign markets	Presentation	Prof. Seiji Adachi

**【 IPO&DL Seminar No.3 (12 May 2017)】**

Sr.	No.	Date	Title	Document	In charge
46	1	2017/5/12	Progress of JICA's Technical Assistance Project	Presentation	consultants
47	2		Redesigning Mongolian capital market: Rationale and technical issues	Presentation	consultants
48	3		Opportunities for Mongolian companies to raise capital in Japan	Presentation	JPX

**【Investor Week Seminar (27 October 2016)】**

Sr.	No.	Date	Title	Document	In charge
49	1	2016/10/27	How to activate equity trading - Lessons from Japanese experiences	Presentation	Prof. Seiji Adachi

**【Training in Tokyo No.1 (October 2015)】**

Sr.	No.	Date	Title	Document	In charge
50	1	2015/10/1	Overview of Japan Exchange Group (JPX) and recent developments in Japanese capital market	Presentation	JPX
51	2		Listing examination	Presentation	JPX
52	3		Listed company regulation & supervision - Maintaining & enhancing the quality of financial products	Presentation	JPX
53	4		Corporate governance and disclosure	Presentation	JPX
54	5	2015/10/2	A brief explanation of market surveillance at Japan Exchange Regulation	Presentation	JPX
55	6		Inspection on trading participants	Presentation	JPX
56	7	2015/10/5	Self regulatory function of Japan Securities Dealers Association (JSDA)	Presentation	JSDA
57	8		JSDA rules for initial public offerings (IPOs)	Presentation	JSDA
58	9		The role of an underwriter in an IPO	Presentation	consultants
59	10		Investor relations	Presentation	Daiwa Securities
60	11	2015/10/6	Listing standards and underwriters	Presentation	consultants
61	12		Audit and internal control report system under the Financial Instruments and Exchange Act	Presentation	FSA
62	13	2015/10/7	Supervision of large securities firms in Japan	Presentation	FSA
63	14		An overview of the Securities and Exchange Surveillance Commission (SESC)	Presentation	FSA/SESC
64	15		The inspection policy and inspection program	Presentation	FSA/SESC
65	16		Financial analysis	Presentation	FSA/SESC

**【Training in Tokyo No.2 (April 2016)】**

Sr.	No.	Date	Title	Document	In charge
66	1	2016/4/11	Listing requirements in Asia	Presentation	consultants
67	2		Stock exchange in Asia	Presentation	consultants
68	3	2016/4/12	Japan Exchange Group and recent developments in Japanese securities markets	Presentation	JPX
69	4		International cooperation of Japan Exchange Group	Presentation	JPX
70	5		Disclosure and corporate governance	Presentation	JPX
71	6	2016/4/13	Listed company regulation & supervision - Maintaining and enhancing the quality of financial products	Presentation	JPX
72	7		Inspection on trading participants	Presentation	JPX
73	8		A brief explanation of market surveillance at Japan Exchange Regulation	Presentation	JPX
74	9		Listed companies' disclosure for investors	Presentation	consultants
75	10		Accounting scandals and false reports	Presentation	consultants
76	11		Self regulatory function of Japan Securities Dealers Association (JSDA)	Presentation	JSDA
77	12	2016/4/14	Outline of qualification examinations, etc., implemented by JSDA	Presentation	JSDA
78	13		Case studies: Discoveries by recent member firm inspections	Presentation	JSDA
79	14		Disciplinary actions of JSDA	Presentation	JSDA
80	15	2016/4/15	Supervision of authorized financial instruments firms association	Presentation	FSA
81	16		Supervision systems of financial instruments markets	Presentation	FSA
82	17		Cooperation with self regulatory organizations (SROs)	Presentation	FSA/SESC
83	18		Capital market development in Myanmar	Presentation	consultants



**【Training in Tokyo No.3 (May 2017)】**

Sr.	No.	Date	Title	Document	In charge
84	1	2017/5/18	Eligibility for dual listing	Presentation	consultants
85	2		What we need for bond market	Presentation	Daiwa Securities
86	3		Introduction to Japan Commodity Clearing House (JCCH)	Presentation	JCCH
87	4		Introduction to Tokyo Commodity Exchange (TOCOM) Group	Presentation	TOCOM
88	5	2017/5/19	Overview of Japan Exchange Group	Presentation	JPX
89	6		Listed company regulation & supervision - Maintaining and enhancing the quality of financial products	Presentation	JPX
90	7		Overview of Tokyo Stock Exchange (TSE) equity market	Presentation	JPX
91	8		Overview of Japan Securities Clearing Corporation (JSCC)	Presentation	JSCC
92	9	2017/5/22	Self regulatory rules of JSDA	Presentation	JSDA
93	10		JSDA rules for IPOs	Presentation	JSDA
94	11	2017/5/23	Outline of the regulations on securities companies in Japan	Presentation	FSA/SESC
95	12		A summary of Japanese government bond (JGB) debt management	Presentation	Ministry of Finance

**【Other lecture materials and presentations】**

Sr.	No.	Date	Title	Document	In charge
98	3	2015/5/19	Lecture on Self Regulatory Organization (SRO) at Financial Regulatory Commission (FRC)	Presentation	consultants
99	4	2015/5/21	Lecture on Self Regulatory Organization (SRO) at Mongolian Stock Exchange (MSE)	Presentation	consultants
100	5	2015/6/9	Lecture on improving financial literacy	Presentation	consultants
101	6	2015/6/30	Listing rules	Presentation	consultants
102	7	2015/9/8	Introduction of the Project for capacity development	Presentation	consultants
103	8	2015/11/23	Requirements for listing and disclosure	Presentation	consultants
104	9	2016/1/15	Financial Market - New investment environment: Challenges for potential issuers and intermediaries	Presentation	consultants
106	11	2016/6/2	Japanese experience on financial literacy	Presentation	consultants
107	12	2016/6/28	Lecture on investor education	Presentation	consultants
108	13	2016/7/7	Introduction to listing management	Presentation	consultants
109	15	2016/11/1	Policy Committee	Presentation	consultants
110	14	2016/11/9	Lecture for FRC Management Team (1)	Presentation	consultants
111	16	2016/11/9	Lecture for FRC Management Team (2)	Presentation	consultants
112	17	2016/11/14	Lecture for FRC Management Team (3)	Presentation	consultants
114	19	2017/2/20	Privatization and IPO (1)	Presentation	consultants
115	20	2017/2/23	Privatization and IPO (2)	Presentation	consultants
116	21	2018/4/13	Investor Protection Fund	Presentation	consultants



# **Report on the Current Status of Mongolian Capital Market**

**April 2015**

**JICA Consultant Team**

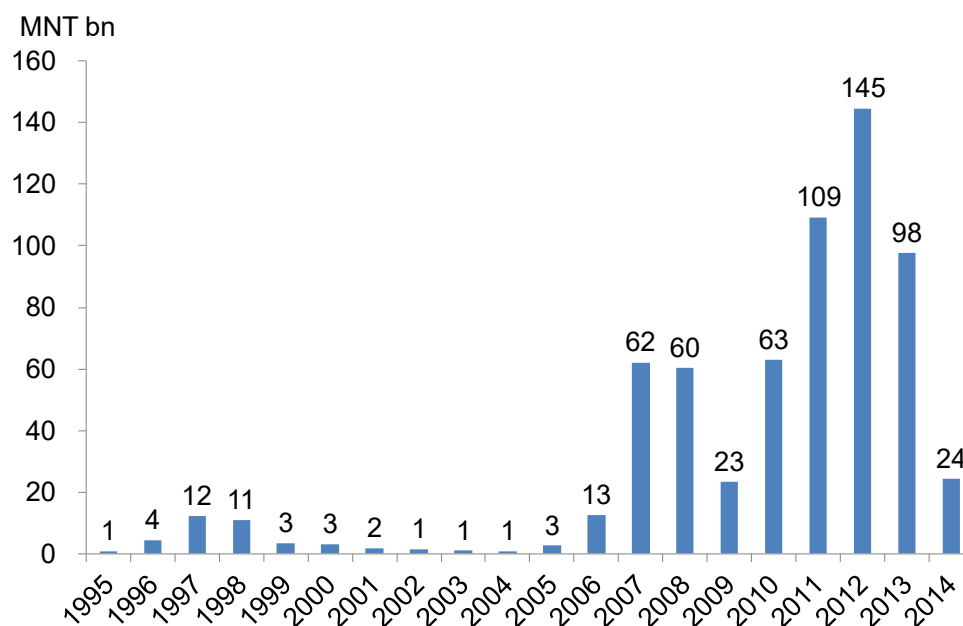
## **Contents**

<b>I. Overview of the Mongolian Capital Market.....</b>	<b>2</b>
<b>II. Five expected outcomes and JICA Consultant team's cooperation.....</b>	<b>9</b>
1. <b>Effective Policy Committee for vitalization of the capital markets.....</b>	<b>9</b>
2. <b>Improving FRC's capacity for regulation and supervision of capital markets.....</b>	<b>19</b>
3. <b>Writing a concept paper on self-regulatory organization.....</b>	<b>24</b>
4. <b>Increasing IPO and promoting dual-listing of Mongolian companies.....</b>	<b>26</b>
5. <b>Enhancing financial literacy for general public.....</b>	<b>53</b>

## I. Overview of the Mongolian Capital Market

MSE faced another tough year in 2014. Trading value declined to MNT 24bn, down 75% from MNT 98bn for 2013. Market capitalization fell to MNT 1.4tn (US\$764m), which is **equivalent to 7% of Mongolia's GDP** at the end of Dec14. 7% to GDP is the second lowest in North and Southeast Asia, after Cambodia. By counter, APU is the largest in market capitalization at MNT 279bn (US\$150m), followed by Tavantolgoi's MNT 232bn.

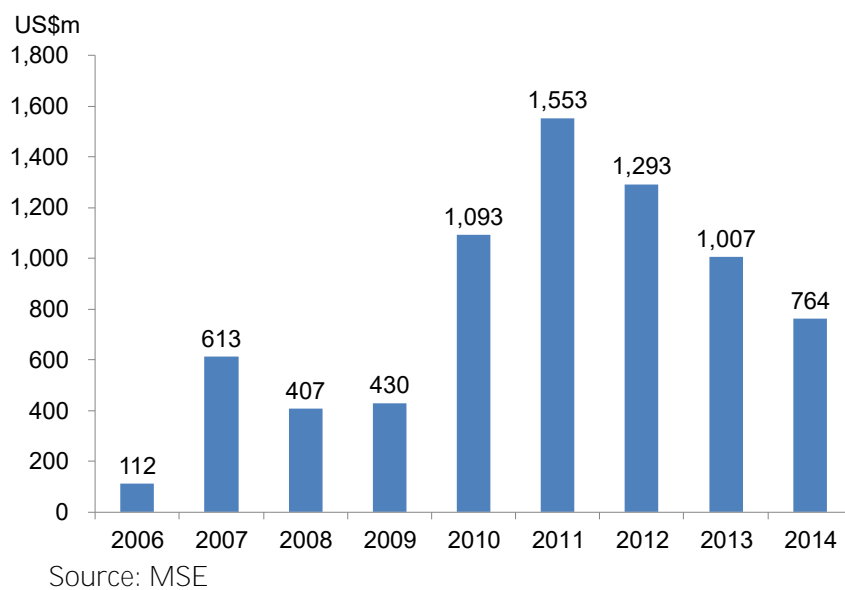
**Figure 1-1 Trading value at MSE**



Source: MSE

MSE's slow trading activities are attributed to structural issues as well as economic downturn. MSE is lack of blue chips. Floating rates for most of MSE stocks are too low at a single digit. Financial reports are sometimes not reliable. Disclosure is not favorable for investors for many cases. General public is not familiar with the stock market. In addition, Mongolia's economy has been hit by weak natural resource prices. Interest rates were raised to fight import inflation.

**Figure 1-2 MSE's Market capitalization**



**Table 1-1 Top10 companies by market capitalization, end-Dec14**

MNT bn

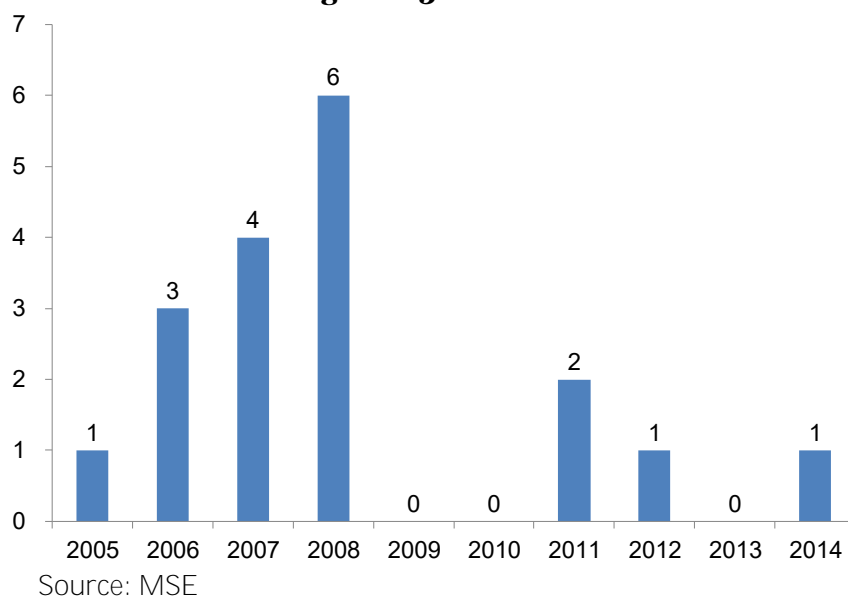
Market cap		2014
1	APU	279
2	Tavantolgoi	232
3	Berkh Uul	68
4	Shivee Ovoo	67
5	Sharyn Gol	62
6	Baganuur	61
7	Gobi	58
8	UB Buk	48
9	Suu	41
10	Mongol Securities	40

Source: MSE

### **(1) Listed companies**

No of listed companies at MSE further decreased by 24 to 237 in 2014. The JICA Consultant team (the team) believes that delisting companies that do not meet listing requirements is a right action for MSE. Given that there have been only 18 IPO in the past, number of listed companies can potentially drop to less than 100, in our view.

**Figure 1-3 No of IPO**



Quite a few listed companies do not comply with corporate responsibility. Some of them even do not submit financial reports, according to a survey by FRC. There are some that do not hold an annual shareholders' meeting. Financial numbers are sometimes not reliable, according to accountants. There are only 10 or less listed companies that are audited by the big four international accounting firms. No of listed companies paying dividends are ranging from 15 to 40, depending on a year. The team believes that these facts definitely dampen market confidence, especially from overseas investors.

**Table 1-2 No of listed companies with corporate responsibility, 2013**

	# out of listed companies
Paid dividends	30
Submitted financial reports	204
Renewed company charter	161
Appointed independent directors	122
Held annual shareholders' meetings	150

Source: FRC

In fact, many of major Mongolian corporate group of companies are unlisted. There are roughly 50 overseas-listed companies with Mongolian assets, mainly in Toronto, Australia and Hong Kong. The team also believes that promoting IPO for unlisted Mongolian companies with sound fundamentals and making dual-listing for Mongolian-related companies at TSX/TSV, ASX, HKEx, LSE etc. will be necessary for more active market. Privatization including ETT can be also a driver for MSE, in our view.

## **(2) Securities companies**

The team thinks that securities industry needs further development. It is quite obvious that there are too many small-sized securities companies. According to FRC, there are some that even do not own office space. No of licensees for brokers and dealers declined to 62 from 83 in the past one year, which the team believes is a right action. The team also expects a further decline in no of securities companies after Jul15, when minimum paid-up capital requirements for licenses will be raised.

**Table 1-3 No of licensees**

	Broker, dealer	Underwriter	Investment advisory
<b>Dec-13</b>	83	25	16
<b>Jan-14</b>	79	25	16
<b>Feb-14</b>	79	25	16
<b>Mar-14</b>	79	25	16
<b>Apr-14</b>	79	25	16
<b>May-14</b>	79	25	16
<b>Jun-14</b>	79	25	16
<b>Jul-14</b>	71	25	16
<b>Aug-14</b>	71	25	16
<b>Sep-14</b>	71	25	16
<b>Oct-14</b>	65	25	16
<b>Nov-14</b>	65	25	16
<b>Dec-14</b>	62	25	16

Source: MSE

BDSec is the largest securities company in Mongolia, with a brokerage market share of 32% for 2014. The company is also known as a major underwriter in Mongolia, which has a track record of 11 IPO out of 18.

**Table 1-4 Brokerage share by securities companies, 2014**

	2014
<b>1 BDSEC</b>	32%
<b>2 TDB CAPITAL</b>	20%
<b>3 TULGAT CHANDMANI BAYAN</b>	8%
<b>4 TENGER CAPITAL</b>	7%
<b>5 GOLOMT SECURITIES</b>	6%
<b>6 DELGERKHANGAI SECURITIES</b>	4%
<b>7 STANDARD INVESTMENT</b>	3%
<b>8 MONSEC</b>	3%
<b>9 GENDEX</b>	3%
<b>10 ASIA PACIFIC SECURITIES</b>	2%
<b>Top10 total</b>	89%

Source: MSE

Nevertheless BDBSec is considered to be a small-sized securities company with employees of 50. Operating revenues for 2012 and 2013 were MNT 5.9bn and MNT 2.6bn, which are translated into US\$4.4m and US\$1.7m, respectively.

**Table 1-5 Summary of BDBSec's financial data**



	MNT m	
	2012	2013
Cash and equivalents	661	858
Short-term investments	3,801	3,684
Total assets	9,750	9,750
Liabilities	281	832
Shareholders' equity	9,469	8,918

Operating income	5,952	2,636
Gross profit	4,859	1,986
Income before tax	1,666	323
Net income	1,491	288

Source: BDSec

**Table 1-6 List of IPO**

			MNT m	
Ticker	Listed company	Listing date	IPO amount	Underwriter
MSH	Hotel Mongolia JSC	25-May-05	800	BDSec
JTB	Genco Tour Bureau JSC	17-Jan-06	8,259	BDSec
520	Zoos Bank JSC	2006	2,023	Ace and T Capital (Worldkey)
BDS	BDSec JSC	22-Jun-06	750	BDSec
MIB	Moninjbar JSC	2007	1,000	BDSec
HBO	HBOil JSC	2-May-07	400	BDSec
OLL	Olloo JSC	12-Sep-07	582	n.a.
MDR	Mongolian Development Resources	Dec-07	13,200	BDSec
HRM	Hermes Centre JSC	16-May-08	2,356	Bats Invest
529	Anod Bank JSC	2008	20,171	without underwriter
RMC	Remicon JSC	19-May-08	5,049	Gauli (DCF)
NKT	Nako Fuel JSC	24-Jun-08	900	BDSec
HGN	Khuh Gan JSC	30-Jul-08	3,195	BDSec
533	Mon Fresh JSC	2008	-	MICC (cancelled)
SIL	Silicat JSC	1-Aug-11	3,650	BDSec
SHG	Sharyn Gol JSC	2011	18,300	BDSec
ETR	E-Trans logistics JSC	9-Apr-12	924	BDSec
MRX	Merex JSC	14-Jan-14	2,600	Standard Investment

Note: Zoos Bank and Anod Bank were delisted

Source: BDSEc, MSEC etc.

The team thinks that industry consolidation is necessary for Mongolia's securities industry. Current average size of securities companies is too small for operation, including investor education. Potential leaders in the industry are those under banking groups, in our opinion. Figure 7 shows that securities companies under banking groups ranked #2, #4 and #5 in the brokerage market share. The team also observes that there are attempts by bank-related

securities companies for expansion.

**Table 1-7 Mongolia's big four banks and securities business**

	Khan Bank	Golomt Bank	Trade Development Bank	Xac Bank
<b>Total assets, 2013</b>	MNT 4.8tn	MNT 3.7tn	MNT 5.1tn	MNT 1.8tn
<b>Securities subsidiary</b>	-	Golomt Securities (subsidiary)	TDB Capital (subsidiary)	Tenger Capital (sister company)
<b>Securities license</b>	Underwriting (Khan Bank)	Brokerage (Golomt Sec) Underwriting (Golomt Bank)	Underwriting (TDB Capital)	Underwriting (Tenger Capital)

Source: Khan Bank, Golomt Bank, Trade Development Bank, Xac Bank

Bank-related securities companies are also major players in the retail government bond market. Tenger Capital gains 68% of share in accumulated amount for the period of 23 Dec-24Feb. TDB Capital and Golomt Securities are ranked #3 and #4, respectively.

**Table 1-8 Trading value of retail government bonds, 23 Dec 14-24 Mar 15**

	Sales	M/S
<b>Tenger Capital</b>	75,937	64%
<b>TDB Capital</b>	17,735	15%
<b>Ard Capital</b>	10,004	8%
<b>Golomt Securities</b>	7,820	7%
<b>BDSec</b>	4,106	3%

Source: MSE

### **(3) Investors**

Activities by Mongolian investors were slower for 2014. Although there are around 780,000 accounts at MSCH&CD, most of them are account holders that are allocated ETT shares, in our understanding. There are roughly 20,000 retail investors, but only 10,000 active investors, according to Mongolian Association of Securities Dealers.

There are almost no domestic institutional investors in Mongolia. Potential domestic institutional investors are insurance companies, but insurance companies do not have any exposure to shares so far. US-based Firebird is known as one of major overseas institutional investors in Mongolia, but overseas investors activities are also limited, due mainly to the current inactive market.

### **(4) MSE**

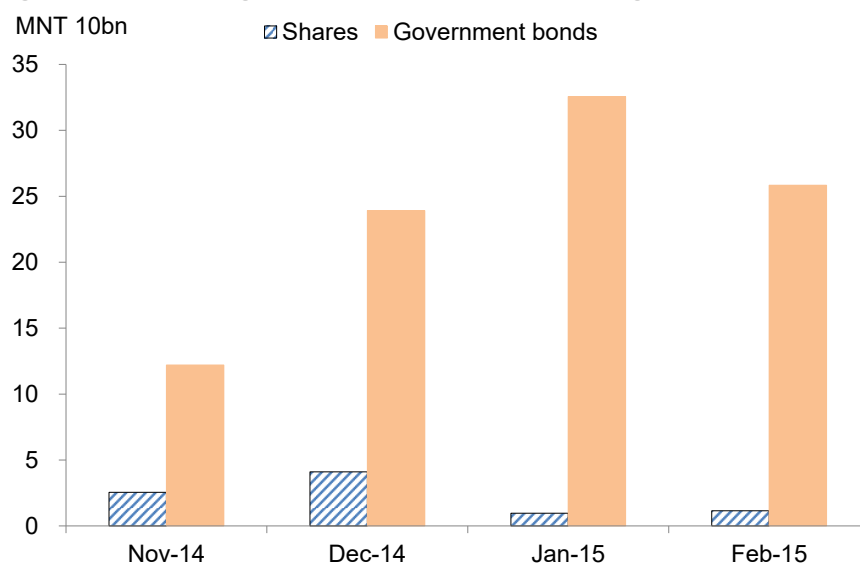
Since Jun14, MOF becomes controls MSE as its sole shareholder, replacing SPC. MOF and MSE appear to have discussions closely for revitalization of MSE. For 2014, the team forecasts that MSE incurred loss for the third consecutive year, as a result of weak market sentiment.

MSE has taken a couple of new measures in the past year, in an effort to reform the market. First, MSE categorized all listed stocks in three groups. Companies under Classification 1 will be regarded as globally-comparable quality stocks. Those under Classification 2 are mid-sized stocks, while stocks under Classification 3 are small cap counters and companies that do not meet requirements. There is none for Classification 1, 89 for Classification 2 and 148 for Classification 3.

Second, retail government bonds are now sold and traded at MSE. Government bonds which are auctioned in a preceding week, are sold at MSE for retail investors since Nov14. Secondary trading of retail government bonds started in Jan15. Currently there are three

maturities of 12, 28 and 52 weeks for retail government bonds, and they attract retail investors with a high-yield of 14-16%, which is sometimes slightly higher than bank deposit rates. In fact, amount of retail government bond sales exceeds that of shares in the past four months.

**Figure 1-4 Trading value of shares and retail government bonds**



Source: MSE

MSE is considering commodity futures and currency futures as new products. MSE apparently thinks that Commodity futures have potential, given relatively active Mongolia Agriculture Commodity Exchange. For currency futures, the team has impression that MSE studies Kazakhstan Stock Exchange's experiences. KASE's trading value for 1Q14 reached US\$65bn, 74% out of which was derived by currency futures, according to KASE.

**Table 1-9 Mongolian Agriculture Commodity Exchange**

Description	
Established	2013
Trading value, 1H14	MNT 450bn
Products	Cashmere (90% of total), wool, oilseeds
Responsible agencies	Ministry of Industry and Agriculture, FRC

Source: various

**Table 1-10 Breakdown of trading value at Kazakhstan Stock Exchange, 1Q14**

Currency	74%
Shares	0%
Corporate bonds	0%
Government securities	2%
Repo (corporate securities)	1%
Repo (government securities)	24%
Total	100%

Source: Kazakhstan Stock Exchange

## II. Five expected outcomes and JICA Consultant team's cooperation

### 1. Effective Policy Committee for vitalization of the capital markets

#### (1) Review on the current situation in Mongolia

FRC has established the Non-standing Policy Committee in September 2014 by the order of the Chairman of FRC as shown in the below. Main role of the Non-standing Policy Committee is to have deliberation on important issues on the capital market development, policy, regulations and other related matters, and to issue recommendation on such issues.

There are thirteen members in the Committee. According to what we heard in January 2015, Vice Chairman of the FRC took a role as the Head of the Committee. Senior Supervisor of the Securities Market Department and the head of Capital Market Policy Planning Division, was the secretary of the Committee. The members were assigned by FRC Chairman's order as shown below.

#### **Order of the FRC Chairman. About establishing the Policy Committee:**

According to the items 3.2, 4.2 of the Charter of FRC, approved by the Parliament Resolution #45 of 2006, it is ORDERED that:

1. In order to discuss the issues on capital market development, policy, regulations and other related matters, to elaborate recommendation and comments on necessary issues, establish the non-standing Policy Committee for Capital markets with below persons:

Head of the Policy Committee: Daajamba B. FRC Commissioner and Vice Director  
Members of the Policy Committee:

Jambaajamts T.	Acting head of the Securities department of FRC
Ganbat D.	Head of the Supervision Department, Bank of Mongolia
Nyamaa B.	Head of the Capital markets and insurance policy department, MoF
Angar D.	Acting CEO of MSE
Gandulam T.	CEO of MSCH &CD
Ulziibayar B.	Board member of MASD
Burenjargal Ts.	CEO of MASD
Lkhagvadorj B.	Board Chairman of BDSec
Altantsetseg B.	Economics teacher of Economics School, National University of Mongolia
Ganzorig A.	Economics teacher of Economics School, National University of Mongolia
Unenbat J.	CEO of Corporate Governance Development Center
Ganzorig U.	President of the Capital Markets Association

Secretary: Tumenbayar Sh., Senior Supervisor, CM Policy and Planning Division, Securities Department of FRC

2. Assign the Head of the Policy Committee /Daajamba B./ to take necessary measure for establishing and enacting the committee.
3. Assign the Head of the Policy Committee /Daajamba B./ to provide guidance and supervision on the committee activities and report and present the necessary issues to FRC Meeting.

By Chairman of FRC

Mr. Bayarsaikhan D.

Although the team does not have the latest member list of Policy Committee, the new responsible department for the committee is Market Development Department.

By January 2015, four meetings have been held since the establishment of the Committee. The first meeting was to make an introduction of members and role of the Committee to all members. The other three meetings were held on ad-hoc basis, depending on the current and urgent issues which FRC thought should be discussed among the major stakeholders and the academic experts. The topics of discussion and recommendation in the Committee are: split of function of CSD, tax policy to promote the capital market, privatization of state owned companies listed in MSE, private pension funds, etc. (see Appendix 1)

According to a member of the Committee, a couple days before the meeting being held, related documents for discussion are sent to each member by FRC. Summary of the meetings is disclosed on the FRC website in Mongolian but not in English<sup>1</sup>.

Although FRC submitted recommendations of the Committee to the Parliament and the Government, it seems that these recommendations are not considered very seriously by them, and none of these recommendations has come into effect up to now. This is because the Policy Committee is regarded as non-standing and is not officially institutionalized yet, and also, perhaps more importantly, thorough discussion with a wide range of viewpoints has not been made within a very short time-frame of the past meetings.

Hence, it will be very important for FRC to formalize the Policy Committee as an influential advisory institution in the capital market and to improve operation of the Committee in more effective manner.

## **(2) Possible solutions**

Taking into account the fact that the capital market in Mongolia is at a very early stage of development and a wide variety of issues needs to be discussed and resolved by only a limited number of people who have sufficient knowledge and experience on the capital market, the team has to say it would be difficult for FRC to emulate the structure and operations of the Financial System Council in Japan (described in Appendix 2) entirely. However, in order for FRC to strengthen the authority of the Policy Committee and to **improve the Committee's operation**, the team believes the following measures should be considered to be taken in the near future.

### **a) To institutionalize the Policy Committee as a formal and independent advisory body for the FRC**

Firstly, it is important to institutionalize the Policy Committee as a standing body, and some type of rules or regulations on roles & functions of the Committee should be issued when necessary. As illustrated in the case of Financial System Council in Japan, such rules or regulations should stipulates major tasks, organization, appointment of members, etc. of the Committee.

Also, such Committee should be regarded as an independent body which would make recommendation to the government from the perspective of the third party. In this regard, it would be desirable that the head of the Policy Committee be a person with an independent standpoint.

---

<sup>1</sup> Bank of Mongolia (BOM) has Monetary Policy Committee consisted of 14 members including 7 BOM management people, 3 academic experts and 1 MOF official and 3 from the financial industry associations. Monetary Policy Committee was held four times in 2014, and "statement" or decision in the Committee is disclosed on BOM's website both in Mongolia and in English.

**b) To set up an appropriate meeting schedule which enables the members to analyze a specific issue and deliberate it thoroughly**

As indicated in the current operations of the Financial System Council, its Sectional Committees and several Working Groups in Japan, the team supposes that members of the Policy Committee need to have more time and wider-ranging viewpoints to make thorough discussion and deliver an opinion which is effective and constructive for the development of the capital market in Mongolia. In other words, the Policy Committee needs to have sufficient consensus building process, especially for important issues which are very new to the Mongolian capital market or which could have large influence on the current and future market players. For a certain type of issue, it would be more effective to invite industry professionals who make presentation or explanation on the current situation of the issue, in order for the members to have better understanding on the issue. Each issue should be discussed in the Committee at least [three] times within a certain time frame before submitting a recommendation or a report to the Chairmen of FRC.

**c) To enlarge the members of the Policy Committee**

It would be difficult for each member of the Committee to have thorough understanding and give an independent opinion of all the issues discussed in the Committee. At the same time, considering a limited number of professional people and academic experts of the capital market in Mongolia at this stage, it would not be realistic to have Sub Committee or Working Group for each of a specific issue.

Hence, the team believe that it would be important to enlarge the members of the Committee so that at least some member(s) could have profound knowledge and actual business experience (either in Mongolia or abroad) on an issue. Inviting more professionals from the private sector including large companies listed at MSE or at overseas stock exchange, institutional investors, banks, law firms, etc. could be an option. Also, including expatriates or foreign professionals working in Ulaanbaatar could be considered to learn from experiences abroad.

**d) To disclose minutes of the Policy Committee both in Mongolian and in English**

It will get more and more important for FRC as a regulator to earn stronger trust from the financial industry and the public. In order to achieve that, FRC needs to be more transparent when making an important decision which affects the current and future businesses of players in the capital market. Sharing information on the current progress of a specific issue could also be helpful to enhance knowledge level of professionals in the capital market.

In this regard, the team believes that it would be important to disclose information of the Policy Committee as much as possible, including minutes and relevant documents of meetings, both in Mongolian and in English.

**(3) Probable technical cooperation activities under JICA program**

In this JICA project, a FSA person, who is in charge of the Financial System Council in Japan, will be able to provide helpful information to FRC on its experiences and efforts in operating the Council since 1998.

In addition, depending on a specific topic discussed in the Policy Committee, FSA, an industry professional or an academic expert will be sent from Japan as an outside lecturer (or as a non-standing member) of the Committee.

The JICA consulting team will help FRC to institutionalize the Policy Committee as an independent advisory body, give advice on appropriate and effective operation of the Policy

Committee and suggest possible outside lecturer from Japan.

Based on discussions with FRC, MSE and the market participants, possible issues to be discussed further in the Policy Committee are:

- Taxation related to the securities market
- Introduction of derivative products in MSE

Enhancing research and planning capability at Market Development Department is an additional request that FRC expects support from the team. The team will discuss with JICA on this matter.

## **Appendix 1: Recommendations by the Policy Committee in the past meetings**

### **Recommendation #1**

In regard to the Government Resolution # 292, dated on September 18, 2014, **about the measures to be taken for the “MSCH & CD” LLC.**, the Policy Committee recommends following:

1. **Separating some of the functions of the “MSCH & CD”, and transferring them** to the new entity will bring significant changes in the securities clearing, settlement and deposit in the country, and the impact on the overall market infrastructure may be significant. Therefore, in order to avoid any systemic risk, any distortion or confusion in the market, and any damage to clients and investors, it is recommended that there should be a Working Group established and shall be composed of the representatives from the professional institutions and all other market participants, and the implementation of the resolution shall be conducted based on the comments and conclusions of that Working Group, and if deemed necessary, the implementation shall be done by stages/phases.
2. **The “MSCH & CD” is a special object that contains secret and confidential** information of the State as well as individuals and thus it is under the protection of State security guards. It is recommended that the Government shall resolve the due care issues to make sure there is no leakage of any confidential information to any third party during the process of transferring some of its functions to the new entity.
3. Although it is appropriate to separate the securities settlement function as an independent entity as stated in the item 4 of the abovementioned resolution, it is not appropriate to have it under 100% control of a securities trading organization. Instead, the Government and Ministry of Finance should own its shares, and coordinate and direct those three companies of securities trading, central depository of securities and securities settlements. Because, the securities settlement entity will not only conduct MSE trading settlements, but also the settlements for other trades that are conducted on the Commodity exchange and OTC market. Therefore it is inappropriate to have the MSE own all of its shares.
4. To ensure that there is no increase in the fees charged from market participants, investors and clients due to shifting the securities settlement function to a separate entity.
5. Keeping its main activities (settlement, title registration, safekeeping of securities) that require a lot of work to transfer at the current company, and separate other activities by shifting them to the new entity is the key leverage for maintaining the normal flow of the company and also avoid any potential systemic risk. In other words, the current company shall continue to undertake the safekeeping of securities, registration of titles to the securities, and the securities settlement function shall be transferred to the new entity. This will be the optimal solution for the time being, and if necessary, the relevant decisions should be altered accordingly.

### **Recommendation #2**

In order to stimulate the capital market development, the Government should



implement a policy on increasing the demand and supply in the capital market products, and in this regard, the Policy Committee is recommending the followings to the Parliament and the Government:

**One: Promoting supply and demand in the market through tax/fiscal policy**

It is recommended to offer tax credits or discounts for IPO companies.

1.1. For the Issuing company:

- 1.1.1. To offer a corporate income tax discount or scaled tax rate for an IPO company depending on its trading volume during the first 3 years since IPO. Example: for a company that raised 10 billion by issuing securities (either IPO or bond), a 5% corporate income tax can be levied during the first 3 years, and if the raised fund exceeds 10 billion, then the tax is waived during the first 3 years. Or, for new securities offering, a discount tax rate for the first 3 years, and furthermore, the current 10% and 25% rates can be lowered to 5% and 10%.
- 1.1.2. For businesses that are based on public interests (i.e. banks, mining companies, telecommunication companies), if they become a listed company, a tax waive can be applied for certain period of time.
- 1.1.3. The current 10% **tax on capital gain is discouraging the investors' interest** in this type of financial products. Thus, the tax on capital gain shall be waived until January 1<sup>st</sup> of 2021, or for capital gains earned over up to 2 years of holding period, the tax rate should be 5%, and for capital gains earned over 2 and more years of holding period, the tax should be waived, or the rate should be lowered depending on the length of holding period.
- 1.1.4. For companies, the tax on dividend income earned by investing in a public company shares should be waived until January 1<sup>st</sup> 2021.

1.2. For Individual Investors:

- 1.2.1. The capital gain tax for individual investors shall be waived until January 1<sup>st</sup> of 2021, or for capital gains earned over up to 2 years of holding period, the tax rate should be 5%, and for capital gains earned over 2 and more years of holding period, the tax should be waived, or the rate should be lowered depending on the length of holding period.
- 1.2.2. For individual investors, the tax on dividend income earned by investing in a public company shares should be waived until January 1<sup>st</sup> 2021.

**Two: Trading of the shares of State Owned Companies that are listed on MSE**

According to an official survey, there are 1,965,759,932 shares of 21 companies that are 100% State owned; and 72,552,967 shares of 16 companies that have state ownership to some degree. However, there is no market capitalization calculated for the 100% state owned companies. The State ownership portion in those partially state-owned companies constitutes 31% of the total market capitalization of the securities market. This is something we need to pay attention to.

Although abovementioned companies are listed on the MSE, their shares are not traded. The actions to start trading these shares need to be taken. By trading the

shares owned by the State, the total trading volume of the market, investment activities and the number of investors in the market will increase, and it will enable an environment for determining more accurate market value of the securities, and thus furthermore lead to better corporate governance practices, and evolvement of large national companies.

### **Three: Use of the securities market infrastructure and ensuring higher valuation of the shares when conducting the privatization activities of the State owned companies**

The development of the securities market is related to the privatization program of the country. Conducting the privatization of the state owned companies through MSE, using its infrastructure and systems will enable significant fund raising by attracting many investors. Moreover, it will help stimulating the market activities and thus contribute to the economy.

It is not sufficient to privatize only 4 companies out of the 22 state-owned companies included in the privatization list submitted by the Government to the Parliament. It is recommended to increase the number of state-owned companies to be privatized.

It is resolved to trade the Government bonds via MSE, and offering the shares of the state-owned companies in the same manner will help boosting the investor confidence.

### **Four: About Private Pension Fund activities**

It is an international common practice to put the idle funds of pension funds into the securities market. We need to do the same, by moving some of the idle fund of the pension fund that are invested as deposits at commercial banks and earning less return. We need to do this urgently. For this, it is recommended to modify the investment policy of the fund, stating specifically that the fund should invest only in the shares of those companies that have stable operations and are in compliance with the international standards of corporate governance. Pension funds are usually the biggest investors and also they monitor the company operations well. With the presence of this type of large investors, confidence of the minority shareholders can be increased and thus stimulate the market activities and improve the liquidity of the shares.

On the other side, the need to adopt a law on private pension fund arises along with the capital market development. Establishing the ground for private pension funds will enable the evolvement of large, sophisticated investors. Promoting the presence of large professional / sophisticated investors in the market will bring in a lot of progress in the development of the market.

### **Five: Ensuring the sustainability of the macro-economy**

It is considered that macro-economic situation is the key indicator of the state of a **country's financial sector. Mongolian economy is facing a slowdown during last year, double digit inflation, MNT depreciation and these factors are increasing the investment risks.**

The development and stability of the securities market help addressing the financial matters of the businesses in real sector and also attract foreign investors. These will, in turn, contribute to the sustainability and the long-term growth of the economy.

The Policy Committee hopes that the Government will take actions according to

these recommendations.

## Appendix 2: Financial System Council under FSA in Japan

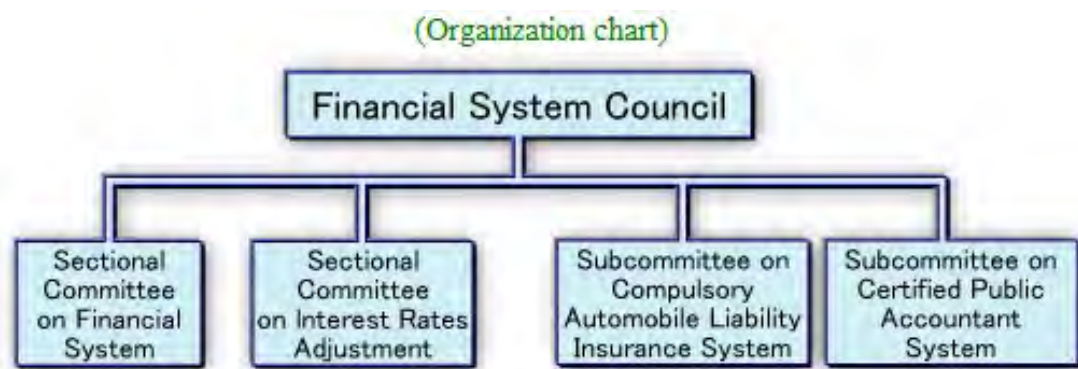
### Overview of Financial System Council

Financial System Council was established in 1998 based on Financial Services Agency Establishment Act.

According to Article 7 of the Act, main role and functions of Financial System Council is (1) to have deliberation on important issues related to financial system improvement, etc. based on a request from the Prime Minister, the Commissioner of FSA or the Minister of Finance, (2) to deliver an opinion on the above issues to the Prime Minister, the Commissioner of FSA or the Minister of Finance, and (3) to have deliberation on important issues related to Compulsory Automobile Liability Insurance System with request from the **Prime Minister or the Commissioner of FSA. In addition, the Council's role is to deliver an opinion** on interest rate adjustment to the Prime Minister, the Commissioner of FSA, the Minister of Finance or Policy Board of the Bank of Japan, and to have deliberation on issues related to Certified Public Accountant System with request from Prime Minister or the Commissioner of FSA.

Members of the Financial System Council are appointed by the Prime Minister with approval from the both houses of the Diet, and the members should exercise their authorities independently from major stakeholders, and each member must not be a board member of any political organizations. Term of the members is three years. Deliberation process should be disclosed annually.

The following is an organization chart of Financial System Council, and there are four sectional committees, each focusing on different and specific issues.



Source: FSA's website

### Financial System Council Order

Under Article 7 of the Financial Services Agency Establishment Act, there is Financial System Council Order which stipulates organization, appointment of members, etc. of the Financial System Council.

According to the Order, the Financial System Council should be organized with less than thirty members, and an ad hoc member or an expert member could be included in the Council when needed.

Chairman of the Council should be chosen by the members of the Council. Term of

members is two years. Also, Chairman of the Sectional Committee on Financial System and on Interest Rate Adjustment should be chosen by the members of the Sectional Committee. Working Group could be organized under the Council or the Sectional Committee. Members of the Working Group should be chosen by the Chairman of the Council or the Sectional Committee.

The Financial System Council cannot hold a meeting and make a decision without majority of the members.

In order to carry out its task, the Council is able to request cooperation to the top of related governmental organization for submitting documents, providing a relevant explanation, etc.

### **Current operation of the Financial System Council**

Currently, there are seventeen members in the Financial System Council. Professor Naoyuki Yoshino of Keio University Economics Department is the Chairman of the Council. Ten members including Professor Yoshino are academic experts, two from consulting companies (Boston Consulting Group and Nomura Research Institute), two from private companies (Mitsui Sumitomo Insurance and Mitsubishi Corp), one lawyer, one from Japanese Trade Union Confederation, and one from voluntary consumer organization. The Financial System Council and the Sectional Committee of Financial System are held twice or three times a year. Recently, the Council and the Sectional Committee have been held concurrently. As of January 2015, there has been thirty-three meetings for the Financial System Council and twenty-one meetings for the Sectional Committee of Financial System. Minutes and **discussion materials of meeting are disclosed on FSA's website.**

There are several Working Groups under the Financial System Council or Sectional Committees, including Working Group on Investment Management, Working Group on Sophistication of Payment and Settlement Operations, Working Group on the Mid- and Long-Term Roadmap of the Financial Industry in Japan, Working Group on the Provision of Risk Money to Emerging and Growing Companies, Working Group on the Provision of Insurance Products/Services, etc. Generally, such working groups are held more frequently compared to the Financial System Council. For example, Working Group on Investment Management which started October 2014 has been held five times in three months. Also, in case of the Working Group on the Provision of Risk Money to Emerging and Growing Companies, before finalizing the draft report, eleven meetings were held within six months. Similar with the Financial System Council, minutes and discussion materials of every meeting are disclosed.

The chart below is a summary of operations of the recent Working Groups.

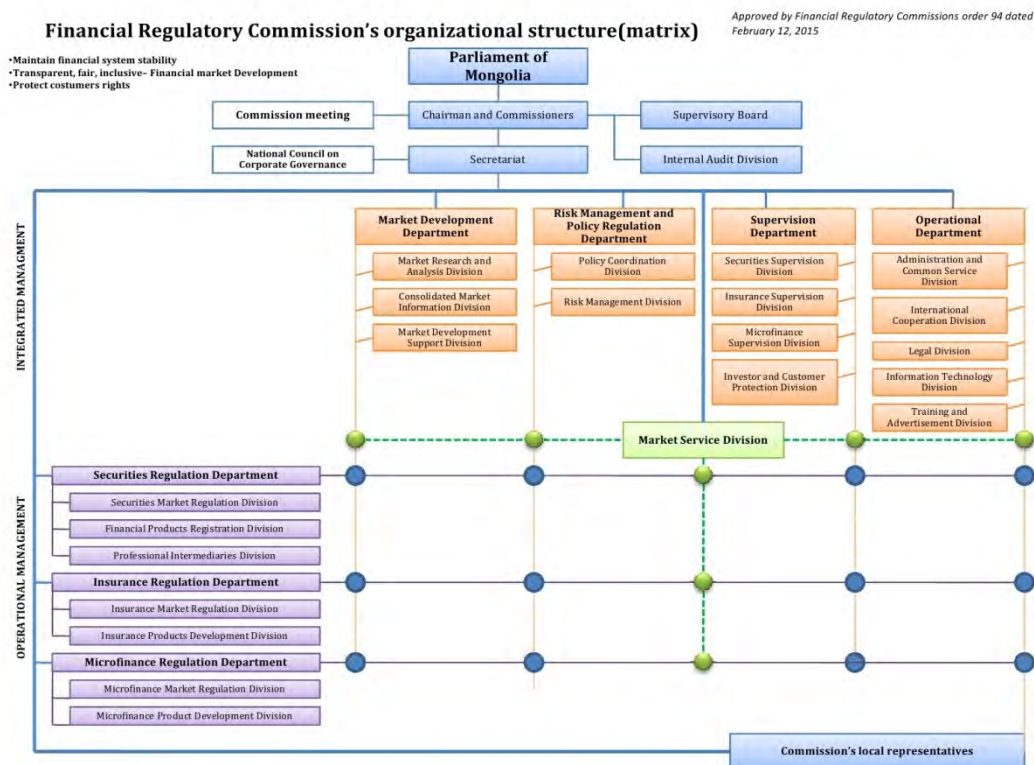
<b>Name of the Working Group (WG)</b>	<b>Term / # of meetings</b>	<b># of members / Head of the Group</b>	<b>examples of outside lecturers</b>
<b>WG: Investment Management</b>	Oct 2014 - / 6	17 / Mr. Kanda, prof., Univ. of Tokyo, Graduate school of law and politics	Nomura Institute of Capital Markets Research, SESC, National Consumer Affairs Center, Nippon Technology Venture Partners, The Japan Academic Society for Ventures and Entrepreneurs, Japan Federation of Bar Associations, Japan Venture Capital Assoc., etc.

<b>WG: Sophistication of Payment and Settlement Operations</b>	Oct 2014- / 10	23 / Mr. Iwahara, prof., Waseda Univ. Law School	NTT Data Group, Japan Bankers Assoc., The Japan Research Institute, Fujitsu, Bank of Japan (BoJ), Deloitte Tomatsu Consulting, JCCI, National Consumer Affairs Center, The Center for Financial Industry Information Systems, etc.
<b>WG: Mid- and Long-Term Roadmap of the Financial Industry in Japan</b>	Jun 2011 – May 2012 / 14	21 / Mr. Yoshino, prof., Keio Univ. Economics Dept.	Bank of Tokyo-Mitsubishi UFJ, Tokio Marine Holdings, Daiwa Securities, Japan Center for Int'l Finance, Sumitomo Chemical, Mitsubishi Corp., HSBC, JPMorgan, Goldman Sachs, Citigroup, BoJ, Dogan Advisors, The Kagoshima Bank, Sumitomo Mitsui Asset Management, Japan Assoc. for Financial Planners, MorningStar, Carlyle Japan, A.T.Kearney, Nomura Research Institute, etc.
<b>WG: Regulation on Insider Trading</b>	Jul 2011– Dec 201 / 5	16 / Mr. Kanda, prof., Univ. of Tokyo, Graduate school of law and politics	Tokyo Stock Exchange, Tokio Marine Holdings, JX Holdings, Keidanren, etc.
<b>WG: Regulation on Investment Trust and Investment Corporation</b>	Mar 2012-Dec 2012 / 13	18 / Mr. Kanda, prof., Univ. of Tokyo, Graduate school of law and politics	NRI, Nomura Institute of Capital Markets Research, Deutsche Bank Group, Assoc. for Real Estate Securitization, SMBC Nikko, etc.

## 2. Improving FRC's capacity for regulation and supervision of capital markets

### (1) Review on the current situation in Mongolia

Regulation and supervision for market intermediaries, including securities brokers/dealers, underwriters, investment funds etc., used to be covered by FRC's Capital Market Intermediaries Division under Securities Department, but now its responsible department is newly-established Supervision Department. Capital market intermediaries are to be supervised by Securities Supervision Division (SSD) under Supervision Department.



SSD conducts on-site monitoring for major intermediaries, from time to time. It appears that frequency of on-site monitoring is not fixed, typically once in a couple of years. Main purpose of on-site monitoring is to inspect capital market intermediaries if they comply with laws, rules and regulations.

Financial data is not scrutinized by its off-site monitoring. SSD does not have access to capital **market intermediaries'** financial data, except for semi-annual/annual financial reports submitted by intermediaries. Resolution No.457, issued in November 2013, defines data that securities companies need to submit on a monthly basis, but it is mostly trading data and does not key financial numbers.

Moreover, no of staff in SSD is only 9, compared to 62 brokers/dealers, 25 underwriters and 16 investment advisory companies. In addition, SSD is also responsible for supervision of around 300 listed companies, in addition to intermediaries including securities companies, custodian banks, commodity brokers, MSE and MSCH&CD.

### (2) Possible solutions

For better results by its limited staff count at SSD, FRC plans to change its supervision to risk-based supervision from compliance-based. Risk-based supervision is increasingly

common for financial regulators globally, and the team thinks that FRC's attempt to implement risk-based supervision is a positive move. By risk-based supervision, regulators are supposed to supervise high risk-profiled targets (securities companies, for instance) more than those who are low risk-profiled. Although FRC received some support from World Bank for risk-based supervision in the past, that was more or less theoretical inputs, and the team observes that SSD needs further support for what to do in implementing risk-based supervision.

### **(3) Probable technical cooperation activities under JICA program**

The team suggests that a training course will be necessary for FRC to understand basics for risk-based supervision. The team believes that it will be a simple formula for the time-being, given that Mongolian securities companies' operations are mostly brokerage of shares and sales of government bonds, while underwriting and dealing activities are limited.

The team proposes that the first training course on this matter should include the basic framework of risk-based supervision, what kind of data and materials FRC needs to collect from securities companies, and basic financial data analysis. Eventually manuals on risk-based supervision will be necessary. The team understands that a manual for on-site supervision is being developed by Risk Management and Policy Regulation Department.

The team believes that FSA will dispatch its experts for a training course on risk-based supervision to share knowledge and their experiences with FRC. The first training course in Mongolia is tentatively scheduled for 27 April to 1 May 2015. The team proposes that the course will consist of three topics: a) basic framework of risk-based supervision and FSA's experiences; 2) data/materials collection from capital market intermediaries; and 3) introduction to financial data analysis of capital market intermediaries.

In addition, technical cooperation by the team, FSA and other Japanese experts is expected in the area of the following issues:

- a) Rules and guidelines under Securities Market Law and Investment Fund Law
- b) Law enforcement
- c) New financial products
- d) Supervision of custodian banks
- e) Implementing alternative dispute resolution
- f) Improving disclosure for listed companies
- g) Better quality of client services by securities companies

## **Appendix: Guidelines for on-site inspection/supervision of securities firms (brokerage and dealer firms)**

1. General
  - 1.1. The purpose of the supervision is to ensure the compliance of the regulated entities to the Securities market law and other related laws and regulations, and to assess and correct any incompliance if any.
  - 1.2. Inspection has to be conducted by the inspectors in accordance with this guideline.  
Inspection team:  
Head of the team:  
Members of the team:  
  
The time period covered by the inspection:  
The dates/period of the inspection to be conducted:
  - 1.3. The head of the team will be in charge of organizing the team (working group), ensuring the coverage of all the aspects stated in the guideline, conducting the inspection well, and timely reporting the results to FRC.
  - 1.4. The management of the regulated entity will let the inspection team to conduct the inspection, and provide the necessary information in a timely and complete manner.
2. Preparation of the inspection
  - 2.1. Prior to the inspection, the person in charge of the company shall provide following documents to the inspection team:
    - 2.1.1. Company charter **and operation's manual**
    - 2.1.2. Findings on off-site supervision on the company
    - 2.1.3. Any petition, complaints received from clients about the damages they incurred due to the wrongdoings of the company and/or its employees.
    - 2.1.4. Previous feedbacks **and responses given from FRC to the company's financial statements and filings.**
3. The scope of the inspection activity
  - 3.1. Regarding the enforced rules and regulations
    - 3.1.1. Check whether the company charter is registered at the state registration and any amendments are approved by the relevant authority, and the version that is kept at the company is the same as the one kept at FRC (shall have no discrepancy between those copies).
    - 3.1.2. Check whether the internal rule and code of the company that are required by FRC are in compliance with the relevant laws and regulations, and are followed/ enforced accordingly in its operations.
    - 3.1.3. Check whether the internal audit function of the company is efficient and in accordance with the relevant regulations.
    - 3.1.4. Check whether the company paid the required fees
    - 3.1.5. Check whether the company adopted a rule on Anti-money-laundering, and is complying with the rule in its operations.
    - 3.1.6. Check whether the company is reporting to the Financial Information office in **accordance with the FRC regulation on "Client identification Process and reporting of suspicious transactions" which was approved by the FRC resolution # 253, dated on November 23, 2009, and amended by the FRC resolution # 272 of 2010.**
    - 3.1.7. If the inspection was being conducted due to any issue reporting to FRC, the scope of the inspection should be determined, and the inspection shall be conducted accordingly.



- 3.1.8. The inspection team shall advise and inform the company management about any updates or amendments on relevant laws, regulations and also new rules and regulations.
- 3.2. Regarding the main activities / operations
  - 3.2.1. Check whether the company is in compliance with the documentation requirements of all the processes that range from receiving client orders to recording and accounting of the securities transactions, set by FRC, and properly kept and secured the risk of loss and damage to those documents/files.
  - 3.2.2. Check whether the activities such as receiving orders, conducting and canceling of orders are in compliance with the relevant laws and regulations, and there is a daily internal control function on monitoring the orders received/given during the trading process, the price of the securities etc.
  - 3.2.3. Check whether the company provided information about its employees and related parties to the database of the FRC, and whether the company conducts any control and monitoring on the use of inside information, and prevents any exploitation of such information.
  - 3.2.4. Check whether the company ensures the safety and confidentiality of information.
  - 3.2.5. **Check whether the company is submitting the required information to the FRC's** information database, and keeping the required forms and records.
  - 3.2.6. Check whether the company is providing the clients with necessary information, whether the company is doing any activities to help the clients have better understanding of the market.
  - 3.2.7. Check whether the company is providing any services for organizing the shareholder meeting, dividend distribution, share repurchases,/if so, the content of that service agreement is in compliance with the relevant laws and regulations/
  - 3.2.8. Check whether the company is addressing the complaints from the clients
  - 3.2.9. Check how the company is keeping the record of “power of attorney”, and check **whether the time period and the scope of all the “power of attorney” are still valid.**
  - 3.2.10. Check whether the company is providing the information stated in the Article 57 of the Securities Law to FRC and the clients.
  - 3.2.11. In terms of publicly disclosed information, check whether the company is in **compliance with the FRC regulation on “Marketing activities of a regulated entity”,** approved by the FRC resolution # 370 of 2013.
  - 3.2.12. In terms of archiving of accounting and bookkeeping records, check whether the company is in compliance with the clause 52.2 of the Securities Law.
  - 3.2.13. Check whether the company has a contract with an audit firm that is registered at FRC according to the clause 53.1 of Securities Law, and whether the audit firm is in compliance with the clause 53.2 of the Securities Law.
  - 3.2.14. Check whether the information disclosed to public is proper, accurate, and the resource and distribution channels are in compliance with the RC regulation.
  - 3.2.15. Inform and warn the company about the amendment in the Criminal Law about imposing criminal sanction on actions such as trading on the insider information, market manipulation, initiating transactions with no change of owners, providing fake information, starting from February 09, 2014.
- 3.3. Regarding Financing, Equipment and HR matters
  - 3.3.1. Check whether the company is in compliance with the prudential ratio criteria
  - 3.3.2. Check whether the loss reserve/provision is sufficient to the level set by FRC, and whether the company rule on compensating any damage to the clients from the loss reserve is effectively enforced.
  - 3.3.3. Check whether the management, internal audit personnel, and employees of the company are licensed by FRC and obtained the professional indemnity insurances.
  - 3.3.4. Check whether the workplace, equipment, software meet the standard/requirement **set by the regulation on “Licensing of regulated entity”, approved by FRC resolution**

- #506 of 2013, and the **regulation on “Operations of a regulated entity”**, approved by the FRC resolution #7 of 2014.
- 3.3.5. Check whether the documentation of accounting and bookkeeping activities are in compliance with the relevant laws, regulations, and IFRS standards.
  - 3.3.6. Check whether the company regularly submitted its financial statements in a timely manner in accordance with the regulation approved by FRC resolution #454 of 2013.
  - 3.3.7. If the regulated entity is undertaking other types of regulated activities, check whether the other activities meet the requirements set by the Securities law, and FRC regulations.
4. Reporting the result of the inspection
- 4.1. The report of the inspection shall be finalized within 10 working days since the end of the inspection and be presented to the Head of the Securities Department.
  - 4.2. Recommendations on correcting any incompliance revealed during the inspection shall be given to the company with a specified timeframe to correct. This recommendation shall be attached to the inspection report. The head of the inspection team will report the fulfillment of the recommended actions given with the specified timeframe to the Head of the Securities Department in a consolidated manner.
  - 4.3. The reports of inspections made in 2014 shall be presented to FRC.

#### SECURITIES DEPARTMENT

### **3. Writing a concept paper on self-regulatory organization**

#### **(1) Review on the current situation in Mongolia**

Under the Securities Market Law, MSE is designated as one of the SRO; however, the actual transformation process of MSE as an organization into SRO has not yet started.

There are differences in how the stock exchanges act as a self-regulatory body depending on the country, but generally can be classified into two groups: 1) regulation on listing, and 2) regulation on trading.

The first classification involves activities related to listing probation and activities related to examine the adequacy of those companies listed. The activities related to listing probation for instance in JPX is rather a ceremonial event where final screenings take place including official meeting with management of soon-to-be-listed companies since most of the necessary check-ups regarding listing requirements are conducted by underwriters. It will also be ideal for MSE to act such way given its capacity; however, the current surrounding situations such as the limited capacities on the securities houses and limited staff count in MSE are the bottlenecks. On the other hand, the activities concerning verification of the adequacy of those already listed companies should be conducted effectively by the MSE with reasonable responsibility, it can be achieved via modifying and/or implementing its mandates stipulated on the relevant law.

Activities regarding regulation on trading include monitoring activities towards member **securities companies' financial** soundness and whether they are complying with laws, rules **and regulations, as well as checking investors' wrong**-doings. It is advisable to demarcate the actual details during the monitoring process of securities companies with those of FRC. Monitoring of investors has been enhanced via the MIT surveillance system which was implemented in 2012.

In addition to MSE, Mongolian Association of Securities Dealers (MASD) is expected to play a major role in regulating the market as an SRO. The team understands that MASD is preparing rules and regulations as an SRO. Given that MASD is an association of securities companies, the team expects for MASD to self-regulate member companies' behavior, especially that of sales representatives. Sharing ethics with securities sales representatives is important to improve investors' confidence.

#### **(2) Possible solution**

The team thinks that the first step should be building consensus for SRO among Mongolia's stakeholders. Setting up a working group is a good idea to discuss roles of each regulatory organization – FRC, MSE and MASD. FRC is a regulator, MSE and MASD are SROs. A concept paper on SRO will be prepared and shared by stakeholders, when the working group reaches consensus.

#### **(3) Probable technical cooperation activities under JICA program**

After assisting the working group for SRO and writing the concept paper, the team plans to hold a training course in Mongolia as well as in Japan for relevant stakeholders. Main beneficiaries will be MSE, MASD and FRC, but the team believes that other stakeholders including listed companies also need to learn about the new regulatory framework for the capital market. The team also plans to host a seminar on SRO.

The team expects supports by experts from Japan Exchange Group (JPX) and Japan Securities Dealers' Association (JASD). JPX separated its SRO function to another organization called Japan Exchange Regulation (JPX-Regulation) in 2008 (then called Tokyo Stock Exchange Regulation) and the team believe that it will be helpful for MSE to learn from JPX-Regulation how the company managed to enhance its SRO function. The

team also thinks that JASD will be able to provide plenty of useful knowledge and experiences as an SRO, which continues to enhance its function in light of variable securities market.

#### 4. Increasing IPO and promoting dual-listing of Mongolian companies

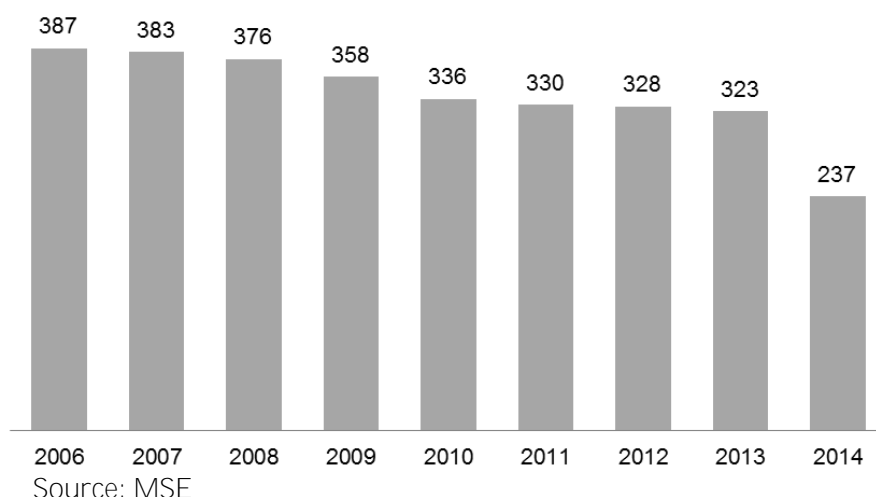
##### (1) Review on the current situation in Mongolia

Equity financing activities through MSE have been stagnant in recent years and there seems to be almost no immediate deals in the pipeline, even after the introduction of the new Securities Market Law in January 2014. This is due not only to the macroeconomic momentum affecting the investor sentiment, but also to several fundamental issues inherent in the current capital markets in Mongolia. In this section, observations by JICA Consultant team (**hereafter** ‘the team’) on the current situation of equity financing in the Mongolian are introduced from five perspectives --- security issuers (listed companies and potential issuers), investors (institutional and retail), intermediaries (brokerage firms and underwriters), stock exchange (MSE) and the regulator (FRC).

##### a) Listed companies

As of the end of 2014, there are 237 listed companies at MSE, 150 less than the end of 2006 (Figure 2-1). The decrease is due largely to the recent effort by FRC and MSE to delist the companies which failed to fulfill the legal requirements to stay listed. In 2013 and 2014, 68 and 25 companies were delisted, respectively. (See also Table 2-1 and 2-2 for the complete list of the companies listed at, and delisted from, MSE. Definitions of three classifications in Table 2-1 are detailed in (d) MSE, later in this section.)

**Figure 2-1 Number of companies listed at MSE**



**Table 2-1 Listed companies by classification (as of February 20, 2015)**

<b>I Classification</b>								
<b>№</b>	<b>Symbol</b>	<b>Company name</b>						
		(None)						
<b>II Classification</b>								
<b>№</b>	<b>Symbol</b>	<b>Company name</b>						
1	AAR	Autozam	79	HHN	Kharkhorin	68	JGV	Juulchin Gobi
2	AOI	Autoimpex	80	HSR	Khasu Mandal	69	BLG	Zavkhan Bayalag
3	ATI	Agrotechimpex	81	HSX	Khishig Uul	70	ZVH	Zavkhan teever
4	ADL	Aduunchuluun	82	AHH	Khorin Khoyordugaar Baaz	71	ORG	Zavkhan teekh
5	APP	Asia Pacific Properties	83	HGN	Khukh gan	72	ZSB	Zoos bank
6	APU	APU	84	TSA	Tsagaantolgoi	73	ZOO	Zoos goyol
7	EER	Arig gal	85	SHG	Sharyn Gol	74	INT	Ingettolgoi
8	ATR	Atar-Urguu	86	SHV	Shivee Ovoo	75	IHN	Ikh nuur
9	BAN	Baganuur	87	ETR	E Trans logistics	76	IHU	Ikh uusgel
10	BNG	Bayangol Hotel	88	IND	Erdenet-Zandan	77	MNG	Mandalgobi impex
11	BTG	Bayanteeg	89	SVR	Erdenet Suvarga	78	MMH	Machine mechanism
12	BDS	B D Sec	<b>III Classification</b>			79	MNB	Mon Nab
13	HHC	Bishrelt Industrial	<b>№</b>	<b>Symbol</b>	<b>Company name</b>	80	MDZ	Mongol diesel
14	BHL	Buunii hudalmaa	1	AZZ	AZZAN	81	MSR	Mongol Shir
15	BHG	Bukhug	2	ERD	Ajlyn Khuvsas	82	MEG	Mongol EEG
16	GTJ	Guril tejeel Bulgan	3	ALD	Azyk	83	MTZ	Mongolian railway
17	BEU	Berkh Uul	4	ALM	Almaas	84	HAM	Mongolian khugijl undesnii negdel
18	SUL	Gazar Suljmel	5	ALA	Altai	85	HBJ	Mongolyn hurungiin birj
19	GHC	Gan khiits	6	AZH	Altan zam	86	MSV	Monsav
20	HZB	Gan Kherlen	7	ANO	Anod bank	87	AZA	Munkh Jim
21	HRM	Hermes centre	8	ABH	Ar Bayankhangai	88	NDS	Nalaikhyn dulaany stants
22	GOV	Gobi	9	ART	Ar tarkhi	89	NIE	Noyot Khaikhan
23	GTL	Gutal	10	ARJ	Arvijikh	90	TGS	Nomin Khishig
24	DZG	Darkhan Hotel	11	ALI	Arljiaa Impex	91	ORI	Orgil Gobi-Altai
25	NEH	Darkhan Nekhi	12	CND	ASBI	92	UAA	Uv-Uujuulagch
26	DHU	Darkhan Khuns	13	NOG	Achit alkaby	93	ULZ	Ulzii-Dundgobi
27	DRN	Dornod	14	ARG	Aerogeodezi	94	ONH	Undurkhaan
28	DES	Dornod Khudakdaa	15	BZO	Baganuur, zuun umnut busiin	95	OEE	Urgun Khereglee
29	SOI	Eurofeu Asia			tsakhilgaan tugeekh suljee	96	GTU	Sav shim
30	JTB	Genco tour bureau	16	BRC	Barilga Corporation	97	ARH	Selenge Ar D'huvch
31	IBA	Ikh Barilga	17	BNB	Bayalag Nalaikh	98	DLH	Selenge Dulaankhaan
32	MIE	Materialimpex	18	BLS	Bayalag Shar. Gol	99	SEM	Selenge Impex
33	MMX	Makhimpex	19	BAJ	Bayalag Sumber	100	SES	Selenge sureg
34	MRX	Merex JSC	20	VIK	Bayan Aldar	101	TVL	Tavilga
35	BDL	Mogoin gol	21	BBD	Bayanbogd	102	TAL	Talyn Gal
36	ASA	Mon-Asar	22	BTL	Bayantalbai	103	UST	Tuv Us
37	MBG	Mon It Buligar	23	BAL	Bayantolgoi	104	TLP	Tulpar
38	MOG	Mongeo	24	BTR	Bayantooroi	105	ACL	Teever-Achlal
39	ERS	Mongol Alt	25	BHR	Binse	106	HUN	Uvs Khuns
40	KEK	Mongol Keramik	26	BSKY	Bluesky Securities	107	UDS	Ulaanbaatar dulaany suljee
41	DLG	Mongol makh expo	27	BOR	Bornuur	108	UTS	Ulaanbaatar tsakhilgaan tugeekh
42	MNH	Mongol nekhmel	28	BRO	Boroogijn Uildver			suljee
43	UYN	Mongol savkhi	29	BUN	Bulgan Undarga	109	UNS	Ulaansan
44	MSC	Mongol Securities	30	CCA	Buudain Tsatsal	110	LJA	Uliastai tegsh
45	MVO	Mongol shevro	31	BYN	Buyan	111	UND	Undarga Umnugobi
46	MSH	Mongol shiltgeen	32	BUT	Buteel	112	UBA	Uran Barilga
47	MDR	Mongolia development resources	33	BLC	Buteelch Uils	113	CMD	Usjuulakh
48	GGE	Mongolyn Gegee	34	BRM	Beren mining	114	SOH	Uujim Khangai
49	MCH	Telecom Mongolia	35	GTR	Gan teerem	115	HBZ	KHAABZ
50	MIB	Moninjbar	36	DLA	Gantumurt	116	HGL	Khangal
51	MNS	Monnoos	37	HML	Global mongolia holdings	117	AVH	Kharshiin Gegee
52	MUDX	MUDIX	38	JGL	Govin Undur	118	CHE	Khorgo Kharkhan
53	NKT	Naco tulsh	39	GFG	Gobi Financial Group	119	SDT	Khot development
54	NUR	Niislel Urguu	40	GNR	Gonir	120	ADU	Khuvsulgal altan duulga
55	NXE	Nekheesgui Edlel	41	GUR	Guril	121	HUV	Khuvsulgal Geology
56	OLL	Olloo	42	DBL	Davaanbulag	122	HUZ	Khuvsulgal usan zam
57	ORD	Orkhondalai	43	DZS	Dalanzadgad DTsS	123	HVL	Khuvsulgal
58	PMC	Remicon	44	DAR	Darkhan guril tejeel	124	HHS	Khuvsulgal khuns
59	SIL	Silicate	45	HSB	Darkhan makh-expo	125	HUT	Khuduugiin Teever
60	SSG	Songolon Barmat	46	DSS	Darkhan Selengiin tsakhilgaan	126	HBT	Khungun beton
61	SOR	Sor			tugeekh suljee	127	HSG	Khusug Trade
62	SUU	Suu	47	DTU	Darkhan Metallurgical Plant	128	HTS	Khutulim cement shokhoi
63	TAV	Tav	48	DUS	Darkhan us suvag	129	DAO	Khurtai
64	TTL	Tavantolgoi	49	DAH	Darkhan Khuvun	130	HAH	Khuns-Arkhangai
65	TCK	Talkh-Chikher	50	DDS	Darkhany dulaany suljee	131	HRD	Khurd
66	TAH	Takhi Ko	51	DAS	Darkhan dulaany tsakhilgaan stants	132	HRL	Kherlen Khivs
67	TEX	Technicimport	52	DZU	DZUZG	133	HLG	Khyalganat
68	TMZ	Tumriin Zavod	53	BAZ	Digital catalyst	134	HJL	Tsuutaj
69	TUS	Tushig Uul	54	DZD	Dornod autozam	135	CDU	Chandmani dundgobi
70	TEE	Teever Darkhan	55	DIM	Dornod Impex	136	CAD	Chandmani uul
71	BUK	UB-BUK	56	DOT	Dornod Teever	137	SIM	Shim
72	CHR	Uvs Chatsargana	57	DHS	Dornod Khuns	138	AMT	Shimtleeg
73	UBH	Ulaanbaatar khivs	58	DRU	Durvon-Uul	139	NRS	Shinest
74	UID	Ulsyn ikh delguur	59	DSH	Dulaan sharyn gol	140	SCL	Shinechlel Invest
75	HBO	HBOil	60	DKS	Dulaany tsakhilgaan stants II	141	JRG	Evlel
76	HMK	Khanyin Material	61	DGS	Dulaany tsakhilgaan stants III	142	EAZ	Erdenet Autozam
77	TVT	Khar tarvagatai	62	DSD	Dulaany tsakhilgaan stants IV	143	EUD	Erdenet us, dulaan tugeekh suljee
78	HAG	Khargia	63	DMA	Devshil Mandal	144	TAS	Erdenet Khuns
			64	SUN	Euroasia Capital Holding JSC	145	EDS	Erdenetiin dulaany tsakhilgaan stants
			65	JLT	Jargalant uils	146	BOE	Erchim Bayan-Ulgii
			66	JST	Jinst	147	ECV	Ereentsav
			67	JIV	Jinst-Uvs	148	ESG	Esgii Gutal

Source: MSE

**Table 2-2 Companies delisted from MSE**

№	Symbol	Company name	Date delisted	№	Symbol	Company name	Date delisted	№	Symbol	Company name	Date delisted
1	ULN	Ulaanbaatar Hotel	2014/11/24	53	HNG	Khangai	2013/8/23	105	IAR	Ilch-Arkhangai	2010/7/9
2	CSU	TSaSTU	2014/11/24	54	HUJ	Khujirt Urguu	2013/8/23	106	ERH	Erdenet khivs	2010/6/24
3	MEL	Monel	2014/11/24	55	SHR	Shar Khooloi	2013/8/23	107	NIC	NIC	2010/5/27
4	RIN	RIN	2014/11/24	56	ETL	Erdenetolgoi tuv	2013/8/23	108	ATK	Avto kombinat	2010/5/19
5	BNT	Tuul bayan	2014/11/24	57	JIM	Urgun Jim	2013/8/23	109	AVT	Khorinnaimdugaar Baaz	2010/4/22
6	DLM	Modlog	2014/11/24	58	MAN	Mandal	2013/8/23	110	SBB	Spirit Bal Buram	2010/4/16
7	CHI	Chimbai	2014/11/24	59	ZOS	Zoos trade	2013/8/23	111	HOR	Khash Ord	2010/4/16
8	OTL	Orkhon bulag	2014/10/3	60	OZT	Shakhait khairkhan	2013/8/23	112	OGU	Uguuj-Sumber	2010/4/8
9	OZM	Uguumur uul	2014/9/4	61	BNR	Bayankhongor	2013/8/23	113	NHT	Khotgor	2010/3/5
10	HAL	Tegsh	2014/6/13	62	SAI	Sainshand	2013/8/23	114	MNF	Monfresh Juice	2010/3/4
11	ALT	Altan Taria	2014/5/21	63	UVN	Uvs	2013/8/23	115	BJT	Buyant	2010/2/26
12	DRI	Darkhan Impex	2014/5/9	64	ASG	Asgat	2013/8/23	116	CCL	Tsatsral Mon	2010/2/24
13	MTS	Khorol-Erdene	2014/1/24	65	JRT	Jargalant Tuv	2013/8/23	117	UDV	Undur Dov	2010/2/23
14	DNU	Dornod noos	2014/1/14	66	BBS	Bayanbulag	2013/8/23	118	AYN	Ayanchin	2010/2/23
15	IBU	Torgon ur	2014/1/14	67	MER	Merei	2013/8/23	119	EHB	EKHBUT	2010/2/23
16	ULH	Ulaan khotgor	2014/1/14	68	HBB	Buyantbulag	2013/8/23	120	SHO	Shoroon ord	2010/2/23
17	TEV	Teever tuv	2014/1/14	69	HDS	Selenge Khurd	2013/8/23	121	MZR	Manzushir	2010/2/23
18	ARI	Arijaa	2014/1/14	70	BUR	Ij Buren	2013/8/23	122	KER	Ceramzit	2010/2/23
19	DRZ	Dar Zam	2014/1/14	71	OBL	Ikha daats	2013/8/23	123	BUL	Bayan-Uul	2010/2/23
20	JNN	Jinchin	2014/1/14	72	CNR	Teever tsagaannuur	2013/8/23	124	DTT	Mon khulug	2009/12/18
21	ULB	Ulbaa	2014/1/14	73	AHD	Autoteever-27	2013/8/23	125	SBU	Bilgekh bayanburd	2009/11/12
22	AHM	Altai khanyin material	2014/1/14	74	ADC	Autodaats	2013/8/23	126	DEE	Deej	2009/11/12
23	OZH	Mandal Orgil	2014/1/14	75	HII	Khiits-Uvs	2013/8/23	127	DLB	Delgertrade	2009/11/12
24	SUO	Sumber-Ulzii	2014/1/14	76	TBE	Jonshit teeveer	2013/8/23	128	BUS	Baruun-Urt Us	2009/11/12
25	GOS	Gobi sumber	2014/1/14	77	TRN	Turuun	2013/8/23	129	SVN	Savan trade	2009/9/4
26	HIE	Khereglee-impex	2013/12/16	78	MED	Mongol Ed Impex	2013/8/23	130	ZMS	ZGMS	2009/9/2
27	UGT	Ugtaal tuv	2013/8/23	79	DDL	Khalkh buudai	2013/8/23	131	ORL	Tuv orgil	2009/7/1
28	AGA	Agro-Amgalan	2013/8/23	80	ATA	Atar tuv	2013/8/23	132	SNH	Shankh	2009/6/8
29	CHA	Chandgan	2013/8/23	81	NUL	Khangain Tsaram	2013/8/23	133	NDR	Naid	2009/6/8
30	THA	Takhilgat	2013/8/23	82	GGL	Gun Galuut	2013/8/23	134	ARL	Darkhan khudaladaa	2009/6/8
31	SNO	Shine Urguu	2013/8/23	83	UAR	Us-Arkhangai	2013/8/23	135	EHT	Ed khereglegchdiin tuv	2009/6/8
32	NLO	Nalaikh Ugruu	2013/8/23	84	ASH	Asralt khairkhan	2013/8/19	136	TGD	Zurkh uul	2009/6/8
33	ARZ	Ardyn Zorig	2013/8/23	85	SHS	Shines	2013/8/19	137	UUG	Jirmen suljee	2009/6/8
34	BNM	Bayanmod-Uul	2013/8/23	86	MSD	Mongol Shudenz	2013/7/25	138	SSR	Munkhsansar	2009/6/8
35	BNH	Bayankhan	2013/8/23	87	HCH	Javkhant kharaa	2013/7/25	139	URC	Mon Urgats	2009/6/8
36	ZES	Bat Khiits	2013/8/23	88	OJN	Orkhon jims nogoo	2013/7/25	140	MGG	Magsarjav	2009/6/8
37	BND	Bayandukhum	2013/8/23	89	ERZ	Erdene zam	2013/7/25	141	URT	Ikha Urguu	2009/3/10
38	JMT	Jimst	2013/8/23	90	DHM	Deed Buyan	2013/7/25	142	ATG	Altan joloogobi	2009/1/24
39	CGC	Tsagaanchuluut	2013/8/23	91	ITL	Bayan-Itgelt	2013/6/21	143	BNZ	Urgats uguuj	2008/12/26
40	BRD	Gobi shand	2013/8/23	92	TLG	Tulga	2013/5/6	144	HHB	Dornin bers	2008/12/12
41	BBG	Del Bayanbulag	2013/8/23	93	MEI	Mongol Em Impex	2013/4/22	145	SIT	Dornod SiTo	2008/10/29
42	TSN	Tsagaannuur	2013/8/23	94	HRH	Khurkh gol	2012/12/27	146	GNL	Gan negdel	2008/10/14
43	AYG	Altan Useg	2013/8/23	95	DHO	Delgerekh khuns	2012/12/14	147	DER	Darkhan urguu	2008/9/4
44	HTO	Khuns Tuv	2013/8/23	96	BGL	Baiguulamj	2012/7/17	148	ACH	Atar chandgan	2008/8/26
45	HRA	Altanduulga	2013/8/23	97	MEZ	Monenzim	2012/4/9	149	ATE	Achaa teeveer	2008/8/26
46	SGT	Selenge Guril Tejeel	2013/8/23	98	JOL	Jol	2011/11/30	150	BLA	Monmoid	2008/7/4
47	UDR	Undram	2013/8/23	99	CNT	Chandmani tal	2011/11/9	151	ENT	Emnelgin Technique	2008/6/6
48	ZNR	Zuunkharaa-Urguu	2013/8/23	100	OHR	Ord kharsh	2011/6/16	152	MSL	Suljee	2008/4/24
49	NSD	Noyon Shand	2013/8/23	101	MNM	Mongol Nom	2011/5/12	153	DBZ	Damjlaga baaz	2008/3/31
50	BBH	Bayanbadrakh	2013/8/23	102	BRL	Khash urguu	2011/5/5	154	LZB	Janna D Ark	2008/2/26
51	ORH	Orkhon	2013/8/23	103	HST	Khailaast	2010/9/23	155	TNV	Tenkheg-Us	2008/2/22
52	ZAL	Zaluuchuud	2013/8/23	104	ARX	Ardiin erkha	2010/9/21	156	HZH	Khazna	2008/1/3

Source: MSE

According to the 2013 Annual Report of FRC, among 323 listed companies (as of the end-2013), 23 companies are state-owned, 30 are parastatal, 193 are private companies with over 75% ownership concentration and 77 are with less than 75% concentration. This high concentration of ownership of listed companies implies very thin trading activities<sup>2</sup>. Coupled with the recent economic downturn in Mongolia, share trading value at MSE has been declining dramatically for the past two years, as mentioned in “I. Overview of the Mongolia’s Capital Markets”

According to the market participants interviewed by the team, there are many listed

<sup>2</sup> According to the 2013 Annual Report, 99% of trading amount and 98% of traded volume were of 30 stocks that were most actively traded. This indicates almost 300 listed companies were poorly traded or were not traded at all in 2013.

companies which have not been traded at all. However, due to the lack of explicit delisting rules and weak enforcement at FRC and MSE, many of these companies are still on the board. FRC, MSE and the market participants share the view that such companies should be delisted as soon as possible for MSE to gain confidence both from domestic and international investors.

Due to this inactive market with low liquidity and very thin investor base, it is generally regarded by Mongolian companies, including those already listed, that economic and social benefits of being listed at MSE are quite limited.

Under such circumstances, the level of the corporate governance and information disclosure of the listed companies have been at a low level, despite the efforts by FRC and the development partners (DPs). According to the “Corporate Governance Scorecard 2011” provided by IFC in 2013, even for the 20 largest listed companies surveyed in this report, the overall mean score was 27.5%<sup>3</sup>, implying ‘poor application of good corporate governance practices.’ Based on the evaluation of the report, among the five major areas of company corporate governance --- 1) shareholders’ rights, 2) equitable treatment of shareholders, 3) stakeholders’ roles in corporate governance, 4) disclosure and transparency and 5) the responsibilities of the board --- 3), 4) and 5) should be given much more attention by the companies.

FRC, as the government agency in charge of regulations related to corporate governance, will need to make additional efforts to improve corporate governance and information disclosure of the listed companies.

Table 2-3 is the list of companies included in MSE Top 20 Index (as in October 2013) and their market capitalization up to date. Out of the 20 companies, 6 are mining-related, mainly in the coal mining, followed by 3 in the food and hospitality sectors, respectively. Market capitalization of the mining sector has decreased substantially due to the turbulent economic conditions, although some signs of recovery can be observed on the back of the expectation on another move going forward. Performance of other sectors varies to a great extent.

---

<sup>3</sup> Based on similar studies by IFC for other Asian countries, the overall mean scores are: Vietnam 43.9% (2009), Hong Kong 72% (2008), Thailand 50% (2001) and 77% (2011), Philippines 53% (2004) and 72% (2008).



**Table 2-3 Market capitalization of the companies included in MSE Top 20 Index**

№	Symbol	Company name	Industry	Market capitalization (MNT billion)			Change	
				2011/5/18 (A)	2013/10/1 (B)	2015/2/18 (C)	(A)→(B)	(B)→(C)
1	APU	APU	food	222.9	282.5	267.7	27%	-5%
2	BAN	Baganuur	coal mining	398.6	83.9	48.2	-79%	-43%
3	BNG	Bayangol Hotel	hospitality industry	16.1	20.3	23.5	26%	16%
4	BDS	BDSec	broker, dealer, underwriter, investment consulting	44.0	33.0	34.0	-25%	3%
5	GOV	Gobi	textile	41.0	37.4	56.9	-9%	52%
6	JTB	Genco tour bureau	hospitality industry	9.4	8.5	8.8	-10%	4%
7	BDL	Mogoin gol	coal mining	34.8	9.4	7.2	-73%	-23%
8	MSH	Mongol shiltgeen	hospitality industry	n.a.	8.5	7.0	n.a.	-18%
9	MDR	Mongolia development resources	real estate	23.4	8.1	6.5	-65%	-19%
10	MCH	Telecom Mongolia	telecommunication	75.8	34.1	31.0	-55%	-9%
11	RMC	Remicon	construction material manufacturing	15.1	13.8	7.2	-9%	-48%
12	SIL	Silicate	chalk refining	n.a.	9.2	10.4	n.a.	14%
13	SUU	Suu	food	n.a.	27.5	31.2	n.a.	14%
14	TTL	Tavantolgoi	coal mining and trade	416.1	168.5	202.8	-59%	20%
15	TCK	Talkh-Chikher	food	n.a.	12.9	20.0	n.a.	55%
16	ULN	Ulaanbaatar Hotel	real estate	15.4	26.8	(Delisted)	74%	n.a.
17	UID	Ulsyn ikh delguur		12.7	15.5	19.4	22%	25%
18	HGN	Khukh gan	iron concentrate	19.3	13.0	12.0	-33%	-8%
19	SHG	Sharyn Gol	coal mining	123.0	76.7	57.3	-38%	-25%
20	SHV	Shivee Ovoo	coal mining	322.1	73.8	83.2	-77%	13%

Source: MSE

Turning to the IPO/SPO markets, the track records in recent years are quite limited, with only two IPOs and six SPOs in the past 6 years (Table 2-4). Among these, three are mining-related, two from construction materials and three from others (finance, logistics and petro importing). Sector-wise, in the team's observation, financing needs tend to be skewed to those with revenue potential outside the country, due partly to the limited size of the domestic demand. Among the domestic demand-oriented sectors, construction has greater presence than others, possibly reflecting the heating real estate market.

**Table 2-4 Past public offerings at MSE**

**IPOs since 2005**

№	Symbol	Name of JSCs	Industry	Listed date	Amount (MNT)
1	MRX	"Merex" JSC	construction material	2014/1/14	2,600,000,000
2	ETR	"E-Trans logistics" JSC	cargo reloading service	2012/4/9	924,000,000
3	HGN	"Khukh gan" JSC	mining	2008/7/30	3,195,456,280
4	NKT	"Nako Fuel" JSC	semi-coke processing	2008/6/24	-
5	RMC	"Remicon" JSC	cement & concrete product manufacturing	2008/5/19	5,048,820,200
6	HRM	"Hermes Centre" JSC	owner of shopping center	2008/5/16	2,356,290,000
7	OLL	"Olloo" JSC	leading portal website	2007/9/12	582,029,900
8	HBO	"Hai Bi Oil" JSC	importing petroleum & oil	2007/5/2	400,000,000
9	BDS	"BDSec" JSC	securities	2006/6/22	750,000,000
10	JTB	"Jenco Tour Bureau" JSC	tourism	2006/1/17	8,259,239,676
11	MSH	"Mongol Shiltgeen" JSC	hotel, restaurant	2005/5/25	800,000,000

#### SPOs since 2007

No	Symbol	Name of JSCs	Industry	Listed date	Amount (MNT)
1	BDS	"BDSec" JSC	securities	-	-
2	SHG	"Sharyn gol" JSC	coal mining	2011/10/13	18,301,439,069
3	SIL	"Silikat" JSC	manufacturing lime & concrete blocks	2011/5/6	3,650,017,500
4	SHG	"Sharyn gol" JSC	coal mining	2011/1/13	-
5	HBO	"Hai Bi Oil" JSC	importing petroleum & oil	2010/8/25	728,474,814
6	NKT	"Nako Fuel" JSC	semi-coke processing	2010/8/25	270,264,655
7	BDS	"BDSec" JSC	securities	2008/6/12	2,625,346,500
8	HBO	"Hai Bi Oil" JSC	importing petroleum & oil	2007/11/29	-
9	MIB	"Moninjbar" JSC	construction	2007/1/16	1,000,000,000

Source: MSE

Based on our discussions with the industry experts, potential issuers on the MSE will be state-owned companies (hereafter 'SOCs', including those in the mining sector, MIAT, Mongolian Railways, power plants, etc.), medium-sized growing companies in such sectors as the agriculture, tourism, construction and real estate, and financial institutions.

As for SOCs, the government of Mongolia (hereafter 'GOM', including SPC and other relevant line ministries) has its basic policy that percentage of the future government ownership shall be determined by industry and plans to sell the remaining shares to the market going forward. GOM maintains and updates the list of companies to be privatized for the coming years, which is approved by the Parliament. Once the latest list becomes available, the team shall review and examine it for possible incorporation into this TA.

Another catalyst for further activating the capital market will be IPO of the major private corporate groups such as MCS Holding LLC (having consumer goods, real estate, telecom and energy businesses under the group. Its coal mining subsidiary was listed on HKEx.) and Tavan Bogd Group (having Khan Bank, hotel, travel agency, Gobi Corporations listed on MSE, etc.). While these conglomerates face hurdles on financing from the domestic banks regulated by the Bank of Mongolia, they generally have negative views on utilizing the domestic capital market as an alternative due to the lack of market liquidity, and tend to finance more efficiently from international organizations such as EBRD or through capital markets abroad. It is also pointed out that these corporate groups tend to be owned and managed by the founders who typically hesitate to sell their shares to the third parties.

As for the listing abroad, there are - more than 40 companies listed on the foreign stock exchanges (Table 2-5). Under the new Securities Market Law, as well as the requirement of the Minerals Law on the strategic deposits as introduced later in this section, listing of these companies at MSE could possibly be further promoted.

**Table 2-5 Overseas-listed companies with assets/businesses in Mongolia**

Company	Ticker	Market	Prices	Market cap	Sector	Main business
			31-Dec-14	US\$m		
Aspire Mining	AKM	ASX	AUD 0.033	19	Metals & Mining	Coking coal
Blina Minerals	BDI	ASX	AUD 0.001	1	Metals & Mining	Copper
Carajas Copper	CJC	ASX	AUD 0.001	1	Metals & Mining	Copper, Gold
Cougar Energy	CGM	ASX	AUD 0.002	1	Metals & Mining	Coal
Draig Resources	DRG	ASX	AUD 0.013	1	Metals & Mining	Coal
Eumeralla Resources	EUM	ASX	AUD 0.055	2	Metals & Mining	Tungsten
FeOre	FEO	ASX	AUD 0.026	2	Metals & Mining	Iron ore
General Mining Corp	GMM	ASX	AUD 0.005	1	Metals & Mining	Metals
Guildford Coal	GUF	ASX	AUD 0.036	27	Energy	Coal
Haranga Resource	HAR	ASX	AUD 0.014	3	Metals & Mining	Iron ore
Modun Resources	MOU	ASX	AUD 0.003	176	Energy	Thermal coal
Mongolian Resources - suspended	MJB	ASX	AUD 0.023	108	Metals & Mining	Gold
Newera Resources	NRU	ASX	AUD 0.002	81	Energy	Coal
Tian Poh Resources	TPO	ASX	AUD 0.200	198	Metals & Mining	Coal, Copper
Viking Mines	VKA	ASX	AUD 0.020	166	Metals & Mining	Coal, Zinc
Wolf Petroleum	WOF	ASX	AUD 0.045	446	Energy	Oil
Xanadu Mines	XAM	ASX	AUD 0.100	1,203	Metals & Mining	Copper, Gold
			31-Dec-14	US\$m		
Asia Coal	835	HKEx	HKD 0.14	163	Metals & Mining	Coal
China Daye Non-Ferrous Metals Mining	661	HKEx	HKD 0.14	315	Metals & Mining	Molybdenum
CNNC International	2302	HKEx	HKD 2.85	180	Metals & Mining	Uranium
Mongolia Energy Corp	276	HKEx	HKD 0.41	88	Metals & Mining	Coal
Mongolian Mining Corp	975	HKEx	HKD 0.36	424	Metals & Mining	Coking coal
North Asia Resources	61	HKEx	HKD 0.15	117	Metals & Mining	Gold
Peacemap Holding	402	HKEx	HKD 0.34	295	Metals & Mining	Coal
SouthGobi Resources	1878	HKEx	HKD 3.87	109	Metals & Mining	Coal
Winsway Coking Coal	1733	HKEx	HKD 0.26	124	Metals & Mining	Coking coal
			31-Dec-14	US\$m		
Central Asia Metals	CAML	AIM	£1.83	319	Metals & Mining	Molybdenum, Gold
Origo Partners	OPP	AIM	£0.06	34	Private equity	Coking coal, Mo, Cu
Petro Matad	MATD	AIM	£0.02	9	Energy	Oil
			31-Dec-14	US\$m		
Altan Rio Minerals	AMO	TSXV	CAD 0.020	2	Metals & Mining	Copper, Gold
Centerra Gold	CG	TSXV	CAD 6.040	1,235	Metals & Mining	Gold
Denison Mines Corp	DML	TSX	CAD 1.130	494	Metals & Mining	Uranium
East Asia Minerals Corp	EAS	TSXV	CAD 0.010	1	Metals & Mining	Gold
Entrée Gold	ETG	TSX	CAD 0.205	26	Metals & Mining	Copper, Gold
Erdene Resource Development Corp	ERD	TSX	CAD 0.105	8	Metals & Mining	Gold, Mo, Cu
Lundin Gold	LUG	TSX	CAD 4.300	376	Metals & Mining	Copper etc.
Minecorp Energy	GMZ	TSXV	CAD 0.025	2	Metals & Mining	Coal
Kincora Copper	KCC	TSXV	CAD 0.025	7	Metals & Mining	Copper
Khan Resources	KRI	CSX	CAD 0.485	29	Metals & Mining	Uranium
Lucky Strike Resources	LKY	TSXV	CAD 0.015	1	Metals & Mining	Uranium
MNP Petroleum	MNP	TSX	CAD 0.095	14	Energy	Oil
Mongolia Growth Group	YAK	TSXV	CAD 0.740	22	Property	
Prophecy Development Corp	PCY	TSX	CAD 0.050	13	Metals & Mining	Coal
Turquoise Hill Resources	TRQ	TSX	CAD 3.590	6,247	Metals & Mining	Copper, Gold
			31-Dec-14	US\$m		
Banpu	BANPU	SET	THB 24.90	1,941	Metals & Mining	Coal

Source: JICA Consultant team

In order to check information disclosure of the companies listed at MSE, the team have picked up 5 companies among those in the Top 20 Index and looked into their websites to find English annual reports (Table 2-6). For these companies, no English annual reports were found. Given the importance for the Mongolian capital market to broaden international investor base in the future, it should be noted that without prompt and proper information disclosure by listed companies, international players would hesitate to invest in the Mongolian capital markets. Hence, more proactive attitude toward information disclosure by the MSE listed companies should be regarded as the urgent issue.

**Table 2-6 Availability of English disclosures for the companies in Top 20 Index**

	website in English	Availability of financial reports in English
Company A	○	×
Company B	○	×
Company C	×	×
Company D	×	×
Company E	○	×

## b) Investors

**Institutional investors:** Table 2-7 summarizes an overview of the institutional investors, both of foreign and domestic, trading at MSE.

**Table 2-7 Overview of foreign and domestic investors, end-September 2013**

	Number of accounts		Trading volume (2013)	
	entity	citizen	entity	Citizen
Local investors	2,388 (0.3%)	769,037 (99.5%)	32%	17%
Foreign investors	155 (0.0%)	1,706 (0.2%)	44%	7%

Source: “Overview of MSCH&CD operations” (October 9, 2013)

Domestic entities include commercial banks and companies under major conglomerates. Commercial banks invest mainly in bond products especially the government bonds, and **tend to hold them to maturity rather than trading them actively. Commercial banks’ investments in stocks are limited due to the regulation on banks’ shareholding in the Banking Law.** The insurance industry is still at the infant stage and the companies are still small in size as shown in Table 2-8. The insurance companies are not regarded as the institutional investors, since their experience and expertise in fund management are very **limited and they put most of their fund in bank deposits under FRC’s regulations on fund operations.** There is a hope for the future development of the industry with an enactment of the Private Pension Law and the Sovereign Wealth Fund (SWF) for managing the national revenue from the mining sector, although it should take some time for them to gain enough presence as institutional investors in the Mongolian capital markets.

**Table 2-8 Total assets of insurance companies**

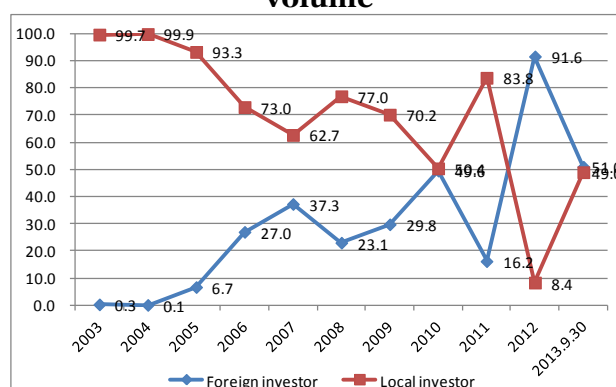
(MNT million)

insurance companies	2010	%		2012	%
1 Mongol daatgal	16,058	28%	1	21,274	20%
2 Bodi daatgal	5,072	9%	2	10,937	10%
3 Tenger daatgal	4,310	8%	4	7,412	7%
4 Practical daatgal	4,184	7%	3	7,728	7%
Mandal			5	7,271	7%
5 Mig daatgal	4,104	7%	6	6,655	6%
6 Nomin daatgal	3,029	5%	9	5,993	6%
7 Ard daatgal	2,983	5%	8	6,345	6%
8 Soyombo daatgal	2,438	4%	7	6,366	6%
9 National life daatgal	2,143	4%	10	4,683	4%
10 Ganzam daatgal	2,032	4%	15	3,144	3%
11 Monre daatgal	1,695	3%	11	3,600	3%
12 Mongoltrust holding daatgal	1,678	3%			
13 Ulaanbaatar city daatgal	1,656	3%	13	3,263	3%
14 Munkh daatgal	1,527	3%	14	3,166	3%
15 Jonon daatgal	1,409	2%	18	1,646	2%
16 Grand daatgal	1,402	2%			
Ger daatgal			16	2,584	2%
17 Monnis daatgal	1,046	2%	12	3,283	3%
18 Khan daatgal			17	2,255	2%
<b>Total</b>	<b>56,764</b>	<b>100%</b>		<b>107,605</b>	<b>100%</b>

Source: 2010, 2012 Annual Report of FRC

As for foreign entities, investment funds focusing on the frontier markets are major players in the Mongolian market. According to an industry expert, just one U.S. investment fund is considered to have occupied most of the trading value by foreign institutional investors, implying that there are not many active foreign investors in the market. As shown in Figure 2-2, foreign investors' presence in terms of trading volume has been fluctuating dramatically. Small capital markets with dominant share of foreign investors tend to be more volatile due to possible speculative activities by such foreign investors. Hence, the regulatory authority of the capital market will need to monitor carefully the investment activities by foreign investors. Also custodian services, currently prepared by some of the commercial banks, are expected to prompt the benefit of foreign investors, which eventually contribute to expanding the investor base.

**Figure 2-2 Percentage of foreign vs domestic investors in terms of trading volume**



Source: "Overview of MSCH&CD operations" (October 9, 2013)

**Retail investors:** As shown in Figure 2-3, the number of accounts held by Mongolian citizens reaches almost 770 thousand, meaning that 27.5% of the total population or every household has an investment account. However, most of these accounts are likely to be inactive, as they were opened when vouchers were distributed in early 1990s and in 2011.

Currently commercial banks in Mongolia offer a deposit interest rate at around 15% p.a., which tends to drive local citizens to leave their money in the deposit as the safest and the most accessible investment. Due also to the perception of the general public that stocks are illiquid and risky, participation of local citizens in the capital markets is very limited in Mongolia except for a few wealthy individuals.

Given all these, as well as the small population in Mongolia, the upside for the retail investor base shall be rather limited for the time being. However, there should be some rooms for increase in individual investors, if there are more opportunities for financial educations and if new financial products such as investment trust fund are marketed effectively through distribution channel of commercial banks, considering high percentage of adults holding investment accounts as mentioned above. This can also be supported by an introduction of preferential tax treatment for securities investment by individuals.

**Figure 2-3 Percentage of adults (age 15+) with an account at a formal financial institution**



Source: The World Bank

### c) Securities intermediaries

The history of securities companies in Mongolia goes back to 1991, when 29 state-owned brokers were established in each 21 provinces and Ulaanbaatar City to distribute stocks of SOCs to the people. They were privatized later, and many others were established when stocks of Erdenes Tavan Tolgoi LLC (ETT) were distributed to the public.

As of the end-2013, there are 26 security companies with the underwriting license and 91 with the brokerage license. The number of brokerage firms increased by 40 in 2011, when shares of Erdenes Tavan Tolgoi LLC (ETT) were distributed to the general public in Mongolia. However, according to the interviews with the market participants, there are only a few security firms which have actual underwriting capability<sup>4</sup>, and there are many small-sized brokers which have been dormant. In its 2013 Annual Report, FRC analyzes

<sup>4</sup> A market participant commented that only BD Sec and couple of others have underwriting capacity.

that a lack of skilled human resources and financial constraints of security intermediaries were part of the reasons behind the decline in the market capitalization.

**Table 2-9 Number of capital market licensees**

Year	Underwriting	Investment Advisory	Professional Intermediaries
2006	2	0	25
2007	8	8	36
2008	17	4	46
2009	15	5	48
2010	16	8	52
2011	22	16	92
2012	25	18	97
2013	26	18	91

Source: FRC

In order to ensure the soundness and stability of the security industry, FRC planned to raise the minimum capital requirement, starting from July 1, 2014. When a company cannot clear the requirement in three-month grace period, FRC will cancel the license of such company. However, facing strong objections from the security companies and the industry association (MASD), FRC decided to postpone the enforcement to July 2015. The actual enforcement of the new rule is likely to throw many security companies out of business.

FRC also examines possibility of introducing ‘capital adequacy ratio’ as an important indicator to measure financial soundness of securities companies. It will be necessary for the Mongolian securities industry to introduce and utilize financial soundness indicators effectively, and hence, to realize sustainable development of the industry. However, after introducing financial soundness measures, there will be restructuring and consolidation of the industry, including withdrawals of small brokers that cannot meet the minimum requirements. Such process will be inevitable for the entire industry to become sounder and more competitive with players above a certain level of business base and financial stability. Therefore, it will be very important for FRC to foresee the future image of the securities industry, and to respond to the industry restructuring in a careful manner to avoid the turmoil.

**Table 2-10 Minimum capital requirements for security-related business licenses**

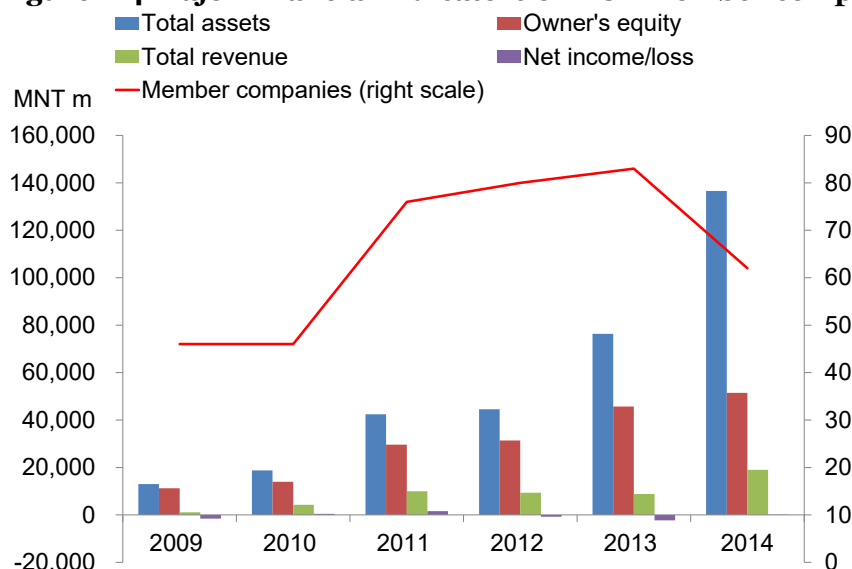
	Current minimum capital based on the present Security Market Law (article 27 & 28)	Revised Minimum capital
Brokers	MNT 50 million	MNT 200 million
Dealers		MNT 300 million
Brokers & Dealers		MNT 500 million
Underwriters	MNT 200 million	MNT 1,000 million
Brokers, Dealers & Underwriters		MNT 1,500 million

Source: FRC

Figure 2-4 illustrates major financial indicators of the total MSE member companies. With increase in the number of securities companies when stocks of ETT were distributed, total assets, owner’s equity, and total revenue of the securities industry increased substantially in

2011. However, total revenue has been stagnant and the net profit has been sluggish since then. 35 companies out of 76 in total in 2011, and 60 out of 80 in 2012 reported net loss. More than half of securities companies continued making loss for 2013 and 2014.

**Figure 2-4 Major financial indicators of MSE member companies**



Source: MSE's website

Ability to plan and develop financial products will be a very important factor for the future growth of the industry. With the implementation of Investment Fund Law in 2014, new financial products such as investment fund and mortgage-backed securities (MBS) can be designed and marketed, which can contribute to broadening the investor base in Mongolia. To take advantage of this opportunity, securities companies need to build up their expertise to deal with such new products.

Also strengthening marketing/distribution network will be critical. Currently a limited number of active companies are dependent on the relationship with particular foreign investors or wealthy local individuals, and there are only a few securities companies that have broad marketing/distribution networks for the mass market. It will be important to expand the network with clients including potential investors, in order for new products to penetrate in the market.

#### **d) MSE**

**Listing rules:** In line with the enforcement of the new Securities Market Law by FRC, MSE has revised its listing rule in October 2014 to make the stock exchange comply with the international standards, to gain confidence from the investors, to improve credibility of listed companies and to increase IPOs by SMEs and growing companies in Mongolia. Comparing the criteria of Classification 1 with that of the former listing rule, minimum percentage of floating shares has decreased from 30% to 25%, minimum operating years increased from 1 to 3 years, and numerical criteria for revenue and profit has been introduced as well as qualitative requirements for the management. According to MSE, there is currently no listed company that meets all requirements for Classification 1. Classification 2 has looser criteria than the former rule, in the sense that its minimum floating shares percentage is 15%, minimum market capitalization is MNT 1 billion (instead of MNT 10 billion in the former rule) and there is no requirements for the profit size. According to the MSE website, 89 listed companies out of 237 fall into this category. Classification 3 is designed for professional investors and more IPO activities by SMEs, but there is no IPO up to now. Also, MSE intends to delist a part of the 148 companies falling



into this category step by step.

**Table 2-11 Listing rules for MSE**

**Classification 1**

<b>Criteria for the Issuer</b>		
<b>Nº</b>		
1	Operating years	At least 3 years
2	Accounting Standard	IFRS, GAAP, last 3 years
3	Profit	Revenue - above MNT 10 billion Net Profit - above MNT 1 billion
4	Requirements for Board, Management, and controlling shareholders	<ul style="list-style-type: none"> <li>- All debt and other liabilities must be disclosed in the prospectus. Must NOT have significant past-due loans</li> <li>- There should be no changes in 2/3<sup>rd</sup> of the management team within the last 2 years. There should be no significant changes in the composition of the controlling shareholders within the last 1 year.</li> <li>- Top management must possess relevant experiences to the business</li> </ul>
5	Corporate Governance	Must be compliant with the local (FRC CG Codex) or international codes
6	Market intermediary	Must have an underwriter or have an agreement signed with an underwriter
<b>Criteria for the Security</b>		
<b>Nº</b>		
7	Market capitalization	Above 10 billion MNT
8	Floating %	At least 25% of the total shares
9	MSE listed period / trading history	At least 2 years

**Classification 2**

<b>Criteria for the Issuer</b>		
<b>Nº</b>		
1	Operating years	At least 2 years
2	Accounting Standard	IFRS, GAAP, last 2 years
3	Working Capital	Must have sufficient working capital for at least 12 months of operation
4	Requirements for Management	<ul style="list-style-type: none"> <li>- All debt and other liabilities must be disclosed in the prospectus. Must NOT have significant past-due loans</li> <li>- Top management must possess relevant experiences to the business</li> </ul>
5	Corporate Governance	Should be compliant with the local (FRC CG Codex) or international codes
6	Market intermediary	Must have an underwriter or have an agreement signed with an underwriter
<b>Criteria for the Security</b>		
<b>Nº</b>		
7	Market capitalization	Above MNT 1 billion
8	Floating %	At least 15% of the total shares

**Classification 3**

<b>Criteria for the Issuer</b>		
<b>Nº</b>		
1	Requirements for Management	<ul style="list-style-type: none"> <li>- All debt and other liabilities must be disclosed in the prospectus. Must NOT have significant past-due loans</li> <li>- Top management must possess relevant experiences to the business</li> </ul>
2	Corporate Governance	Should be compliant with the local (FRC CG Codex) or international codes
3	Market intermediary	Must have an underwriter or have an agreement signed with an underwriter

No	Criteria for the Security	
4	Market capitalization	MSE will decide based on its other requirements
5	Investor base	Professional investors, and other sophisticated and informed investors, who understand the risks of this type of securities

**Table 2-12 Listing examination criteria**

No	Requirement criteria	General	Specific *
1	Shareholder equity	more than MNT 10M	more than MNT 10M
2	Non-current asset size in the price of a security to be listed	more than 10%	more than 20%
3	Number of shareholders**	more than 50	more than 50
4	Percentage of common stock that are publicly offered**	more than 30%	more than 10%
5	Years of running a business operation**	more than 1 year	more than 3 years
6	Profit size**	Shall generate a profit. If incurred a loss, the loss size shall be no more the 30% of an equity capital	No requirement
7	Others	1. Company shall adopt and comply with its governance rules and regulations under internationally standardized practice and guidance. 2. Financial reports, securities transaction, price, trading data, influential information and operational information of the company and management shall be distributed transparently to the public and MSE as soon as possible. 3. Companies must have a specialist who is responsible for securities trading. 4. <b>Announce and arrange the shareholders'</b> meeting to the public within the term stated in the Law. These include meeting notes and resolution to be provided to MSE within the time frame.	

Note:

\* Companies that have a significant role to the sector with infrastructural and strategic importance for the economy shall be reviewed under specific listing criteria.

\*\* Requirement criteria 5 and 6 are not applicable to companies founded under project implementation, requirement criteria 3, 4 and 6 are not applicable to companies being privatized by the state.

Source: MSE website

According to the market participants, examination process for IPOs conducted both by MSE and FRC is quite time-consuming (usually taking 9 to 11 months)<sup>5</sup>, and getting loans from commercial banks is much easier for most companies. After the introduction of the new listing rule which is more friendly and realistic to IPO candidates, it is now very important for MSE to implement the rule in more efficient and effective manner.

<sup>5</sup> Article 7 of the MSE's new listing rule stipulates that "after receiving all the necessary documents and application from the securities issuer, MSE shall conduct inspection and revision of submitted documents within 20 working days."

**Corporate governance:** MSE introduced a new function in charge of corporate governance of listed companies in September 2014. MSE is now conducting a survey on corporate governance and information disclosure of MSE Top 20 companies, in which MSE prepares “self-assessment check list” of 90 questions related to the management, board of directors, information disclosure, accounting standards of these companies. According to the interview with the staff in charge at MSE, the result of survey will be announced in the near future.

**Business planning:** Market Development Department of MSE has prepared the business plan of 2015, and the plan is now under discussion with the government. In this plan, the target number of IPOs in 2015 is set at five, although there is no concrete potential deal as of today.

#### **e) FRC**

Securities Regulation Department is in charge of examining listing companies and monitoring the listed companies in MSE. Some of the functions that FRC used to have in checking IPO applicant have been transferred to MSE as well as the third parties including auditing firm, law firm and evaluators, with the enforcement of new Securities Market Law and MSE’s new listing rule. However, FRC still has authority to approve registration of prospectus of each IPO candidate in MSE. In other words, IPO candidates need to apply to both FRC and MSE for IPO examination process, and there seems to be some overlapping work<sup>6</sup> between FRC and MSE in their examination process, which could lead to complaint about time consuming procedure by underwriters and listing companies. Also, in monitoring work of MSE listed companies, there could be some overlap between FRC and MSE<sup>7</sup>.

According to the Division manager, under the current limitation of the number of staff (nine in total), it is not possible for FRC to monitor all of the 237 listed companies. FRC cooperates with auditing firms to conduct on-site inspection for the listed companies, but FRC would need to prepare some type of inspection manual to receive appropriate results from the work of auditing firms.

Also, the National Council on Corporate Governance which was established under FRC as the institution implementing corporate governance policy has been working with MSE and MSE Top 20 companies to improve understanding and practices on better corporate governance and information disclosure.

As commented earlier, IPO examination process partly covered by FRC is time-consuming, and such situation should be resolved as early as possible.

#### **f) Relevant laws and regulations**

**Securities Market Law:** The Securities Market Law was initially enacted in 2002, which was amended to a large extent in May 2013 and took effect on January 1, 2014, with the main purpose of providing an effective regulatory environment for further developing the securities market. Table 2-13 and 2-14 summarize the basic structure and the changes from the previous version, for which the parts closely related to IPO and dual-listing are marked.

---

<sup>6</sup> According to former Securities Issuer Division of FRC, in IPO examination process, FRC mainly focuses on accuracy of content in prospectus including information on management, financial conditions, business plan, methodology of public offering, etc., while MSE need to check criteria set in each Category.

<sup>7</sup> According to former Securities Issuer Division of FRC, monitoring work of MSE listed companies has been mainly conducted by FRC up until now due to capacity limitation of MSE.

**Table 2-13 Structure of the Amended Securities Market Law**

**Chapter 1: General provisions**

Article 1. Purpose of the Law Article 2. Legislation relating to the securities market	Article 3. Scope of application of the Law Article 4. Definitions of terms used in this Law
---	--

**Chapter 2: Issue and trading of securities**

Article 5. Securities Article 6. Issue of securities Article 7. Securities issuers Article 8. Procedures for issuing securities by way of public offer Article 9. Registration of securities and approval of public offer Article 10. Securities prospectus Article 11. Public offer of securities Article 12. Selling securities on the primary securities market and related reporting Article 13. Depositary receipt	Article 14. Mongolian depositary receipts Article 15. Global depositary receipts Article 16. Company debt instruments Article 17. Issue of securities in a foreign jurisdiction by a company listed on the stock exchange Article 18. Issuing of securities in Mongolia by a legal entity registered in a foreign jurisdiction Article 19. Issuing derivative financial instruments Article 20. General obligations of the issuer Article 21. Demand of information relating to securities issuers and submission of claims
---	--

**Chapter 3: Purchasing all or a controlling block of the shares of a company**

Article 22. Making of an offer to purchase the shares of a company Article 23. Procedures for the purchase the shares of a company
---

**Chapter 4: Regulated activities**

<p><b>Sub-chapter 1: General regulations</b></p> <p>Article 24. Regulated activities Article 25. Principles to be observed when undertaking regulated activities Article 26. Regulations for regulated activities</p> <p><b>Sub-chapter 2: Issuing and registering licenses to legal entities to undertake regulated activities</b></p> <p>Article 27. Applications for licenses Article 28. Granting a license Article 29. Suspension of a license Article 30. Revocation of a license Article 31. Consequences of suspension or revocation of a license Article 32. Measures to be taken and implemented by the FRC in connection with suspending, restoring, and revoking a license Article 33. Regulated activities to be undertaken on the basis of registration Article 34. Right to make a complaint</p> <p><b>Sub-chapter 3: Professional certification</b></p> <p>Article 35. Professional certification</p>	<p><b>Sub-chapter 4: Types of regulated activities</b></p> <p>Article 36. Securities broker activities Article 37. Securities dealing activities Article 38. Investment fund activities Article 39. Securities investment advisory activities Article 40. Security nominee activities Article 41. Underwriting activities Article 42. Securities ownership rights registration activities Article 43. Securities clearing activities Article 44. Securities trade settlement activities Article 45. Securities central depository activities Article 46. Custodial services Article 47. Securities trading activities Article 48. Participating in trading on the stock exchange Article 49. Conditions and requirements for stock exchange activities Article 50. Credit rating activities Article 51. Concurrently conducting regulated activities</p> <p><b>Sub-chapter 5: Accounting and auditing</b></p>
---	---

	Article 52. Keeping accounting registers Article 53. Auditing Article 54. Audit inspection
--	--

## **Chapter 5: Securities market information**

Article 55. Primary securities market information Article 56. Secondary securities market information Article 57. Information regarding regulated entities	Article 58. Investor information Article 59. FRC information Article 60. Receiving of information by the FRC
--	--

## **Chapter 6: Securities market regulation**

<b>Sub-chapter 1: State regulation of securities market</b> Article 61. The central state administrative body in charge of finance and budget matters Article 62. Organization in charge of implementing state regulation in the securities market Article 63. Authority of the FRC Article 64. Cooperation with competent regulatory bodies of foreign jurisdictions and international organizations Article 65. Issuing recommendations Article 66. Issuing instructions Article 67. The register of regulated entities Article 68. Determining suitable persons	<b>Sub-chapter 2: Self-regulatory organizations of the securities market</b> Article 69. Self-regulatory organizations Article 70. Authority of a self-regulatory organization Article 71. Registration of a self-regulatory organization Article 72. The charter and by-laws of a self-regulatory organization Article 73. Management and organizational structure of self-regulatory organizations Article 74. Relations between the FRC and self-regulatory organizations Article 75. Supervising the operations of self-regulatory organizations
--	---

## **Chapter 7: Prohibited activities in the securities market**

<b>Sub-chapter 1: Activities prohibited to a holder of inside information</b> Article 76. Inside information Article 77. Holders of inside information Article 78. Prohibition on participation in trading activities using inside information Article 79. Disclosing inside information to the public	<b>Sub-chapter 2: Market abuse</b> Article 80. Prohibition on market abuse Article 81. Obligation to compensate damage
--	--

## **Chapter 8: Supervision and inspection of the securities market**

Article 82. Demand of information Article 83. Regular supervision Article 84. Inspection of the activities of regulated entities	Article 85. Authority of the State Inspector of the FRC Article 86. Prohibition on obstruction of inspections Article 87. Emergency situations
--	--

## **Chapter 9: Miscellaneous**

Article 88. The Dispute Resolution Board Article 89. Sanctions for violations Article 90. Entry into Force
--

**Table 2-14 Changes in the Securities Market Law and their purposes<sup>8</sup>**

<b>Change</b>	<b>Purpose</b>
<p><b>1. Implementation of segregation between legitimate ownership and beneficial ownership</b></p> <p>In Mongolian law, a legitimate owner used to mean a beneficial owner and the concept of titular ownership did not exist. The amendment introduced the difference between legitimate and beneficial ownerships.</p>	<p>To make it possible for local banks to operate custody businesses so that depository and relevant process are conducted in Mongolia, while the beneficial ownership remains with foreign investors.</p> <p>If there are no reliable local banks which can operate custody business, foreign institutional investors may not invest in the market.</p> <p>To enable local banks to operate custody business and to accelerate investment in Mongolia from foreign institutional investors.</p>
<p><b>2. Dual listing and depository receipts (DRs)</b></p> <p>Old law mentioned the possibility of dual listing, but there were no detailed rules. The amended law explicitly stipulates that dual listing of both Mongolia and foreign listed companies are allowed. Also the definition of eligible securities for trading has been expanded to cover DRs.</p>	<p>Currently, Mongolian securities market is not deep enough to fulfil the financing needs of companies. As a realistic solution, raising a certain part of the funds in foreign markets, besides domestic financing, can be considered. The amendment clarifies the availability of dual listing. It also aims at encouraging the usage of domestic capital market.</p> <p>Introduction of DR aims at 1) facilitating dual listing of Mongolian companies by listing their securities in foreign markets, and 2) making it easier for foreign blue chips to be listed at MSE. 2) is especially designed to enhance the status of the Mongolian market with more foreign company listings.</p>
<p><b>3. Strengthening information disclosure</b></p> <p>Requirements of 1) issuance disclosure and 2) periodic disclosure will need to be enhanced. For 1), details of financial statements, stakeholders list, financing/ investment plans, and risk management plans should be provided in a prospectus. Disclosed Information must be audited by a certified public accountant and verified by a legal professional.</p> <p>While the old law used to require listed companies to disclose all the information required in the relevant laws, the amended law clearly defines a limited scope of disclosure and obliges them to disclose facts such as the certain forms of reorganization, significant changes in shareholder</p>	<p>Under the old law, many listed companies failed to disclose important information such as annual reports and financial statements. The amendment aims at improving the reliability of the market by enhancing the transparency of the market through enforcing the disclosure of the listed companies.</p>

<sup>8</sup> Study team used Hogan Lovells "Mongolia Adopts An Amended Securities Market Law, July 2013" as reference to make this table.

<p>composition and other information that may affect its stock price within one business day from the occurrence. Immediate disclosure is also required for certain situations. In addition, MSE must post information on its website which its listed companies need to disclose.</p>	
<p><b>4. Preventing unfair trading</b> The amended law includes more detailed provisions prohibiting insider trading &amp; market abuse.</p>	<p>It aims at aligning with the global standard on prevention of unfair trading to ensure fairness/ transparency and enhance the market reliability.</p>
<p><b>5. Enhancing supervision by FRC</b> The amended law defines greater number of securities market operations than the old one, enabling FRC to supervise a broader range of securities businesses. In addition, asset valuation companies, audit firms and law firms need to be registered with FRC to provide their services for the listed companies. Relevant regulations are being prepared by FRC.</p>	<p>FRC is going to ensure fairness &amp; transparency in the securities market and protect investors by imposing stricter responsibilities &amp; obligations on market participants.</p>
<p><b>6. Introduction of SRO</b> Stock exchanges, securities depository organizations and regulatory business organizations can be registered as SRO under the amended law. SROs will be responsible for a certain level of oversight of its market participants.</p>	<p>Introduction of SRO is intended to implement a framework for self-regulation among its members.</p>
<p><b>7. Implementation of a Dispute Resolution Board</b> The amended law mentions that a Dispute Resolution Board will be established within FRC to deal with disputes among relevant regulators, listed companies, and investors.</p>	<p>Instead of taking judicial action, a Dispute Resolution Board can provide services for faster, less expensive, undisclosed and more satisfactory dispute resolution.</p>

In connection with the enforcement of the amended Securities Market Law, 34 regulations (shown in Table 2-15 below) have already been issued.

**Table 2-15 New regulations under the amended Securities Market law**

Record of publicly offered securities in Mongolia, IPO & trading
Opening securities trading account, disposition & transaction of the securities & cash assets from the account
Custodian licensing and operations
Regulated activities in securities market
Granting, extending, suspending, reinstating & revoking license, and actions that will be taken in case of revocation/suspension of the license;
<b>Regulated entities'/market intermediaries/operation</b>
Accounting operation
Determination of the cap for the service charge & fee charged by regulated entities
Submitting information to FRC and informing to the public & its surveillance
10. Advertisement of regulated entities & securities issuers
<b>Receiving and completing the client's order</b>
. Nominating the authorized person at regulated entities and determining fit & proper person
. Collection, maintenance and transfer of archive documents of regulated persons
. Instructions on submitting information & reports to FRC
. Setting the fee for regulated operations payable by regulated persons
. Brokerage service of the securities on foreign capital market
. Record and trading of Depositary Receipts
. Inside information of listed company
. Delivering information from listed company to shareholders
. Buying all shares or a controlling block of share of a listed company
. SROs
. Adjustment in emergency circumstance of regulated legal body in security market
. Preventing market manipulation
. Issuing financial derivatives
. Code of corporate governance
. Registering a legal body conducting legal advisory service for securities market participants
. Registering a legal body conducting auditing service for securities market participants
. Registering a legal body conducting asset valuation service for securities market participants
. Trustee management operation of securities
. Conducting qualification examination of securities market and granting suspending and revoking the qualification license of individuals
. Investments funds
. Investment Management Company
. Defining the financial strength ratings operation
34. Council settling dispute

Source: FRC

**Investment Law:** Given the recent decline in FDIs, the Investment Law was enacted in November 2013 in place of the Foreign Investment Law and relevant regulations, with a view to securing stable investments in strategically important sectors, both from foreign and domestic investors. Under this law, domestic and foreign investors are treated in the same way, and the provisions regarding the investment in sectors of strategic importance were removed, although they are still subject to the approvals under other sector-specific laws and regulations, where state involvement are required for business approval in some cases.

**Investment Fund Law:** The Investment Fund Law, which came into effect on January 1, 2014, is the first comprehensive law for investment funds and provides the enabling framework. It aims to pool small-lot funds to nurture new institutional investors and invite wealthy individuals to invest in domestic securities through Private Funds. It also aims to



attract investment from abroad by providing more convenient investment schemes.

It details the types, establishment, operation, management, accounting records and liquidation of investment funds, as well as the investment management companies and custodian banks, with FRC as the main regulator. The law defines two types of investment funds; mutual funds (open-ended or closed-ended) and private funds, which can be established by investment management companies for a period of up to 10 years. Investment incomes are exempt from Mongolian corporate income tax, but no other tax benefits are provided.

According to FRC, the following sub rules have been established or revised in connection with the enforcement of the law.

Establishing investment fund
Investment fund operation and supervision
Member record-keeping of investment fund law
Calling investment fund member meeting
Investment fund accounting, requirement for financial report, investment fund activities and its valuation
Investment fund information and advertisement
Liquidating investment fund
Asset/investment management operation
Custodian operation
Set of detailed regulations on investment fund operation
Investment fund registered in foreign countries
Merger and consolidation of investment fund
13. Defining fit and proper candidates

Source: FRC

**Minerals Law:** The Minerals Law, aiming at regulating mineral exploration/extraction within the jurisdiction of Mongolia, has a provision related to the securities market activities. For example, Article 5.6 stipulates that a legal person holding a mining license for a mineral deposit of strategic importance shall float no less than 10% of its shares at MSE. While this is based on the idea that even 10% of such promising businesses should have substantial positive impact on domestic capital market, there is no penalty for incompliance with this rule at this point.

## (2) Possible solutions

Provided the development stage of Mongolian capital markets as detailed above, potential demands and the strategy of assistance for IPO/dual listing can be summarized as follows.

The basic idea is how to present the potential sectors/companies to the investors (especially foreign investors for the time being) in this difficult time of macroeconomic instability. In order to do that efficiently and effectively, the main focus should be marketing the Mongolian capital markets as a transparent one in line with the global standard, which can provide full investment opportunities attractive enough for global investors interested in high growth emerging markets. This is a reasonable and rational approach, particularly as a short-term strategy, as it takes much longer time to broaden the domestic investor base. (See the target image for the short-term in Figure 2-5, which was prepared by the JICA Study Team for the 'Data Collecting Survey for Development of Financial and Capital Market, and Capacity Building of its Regulation and Supervision in Mongolia', as a basis of this TA.)

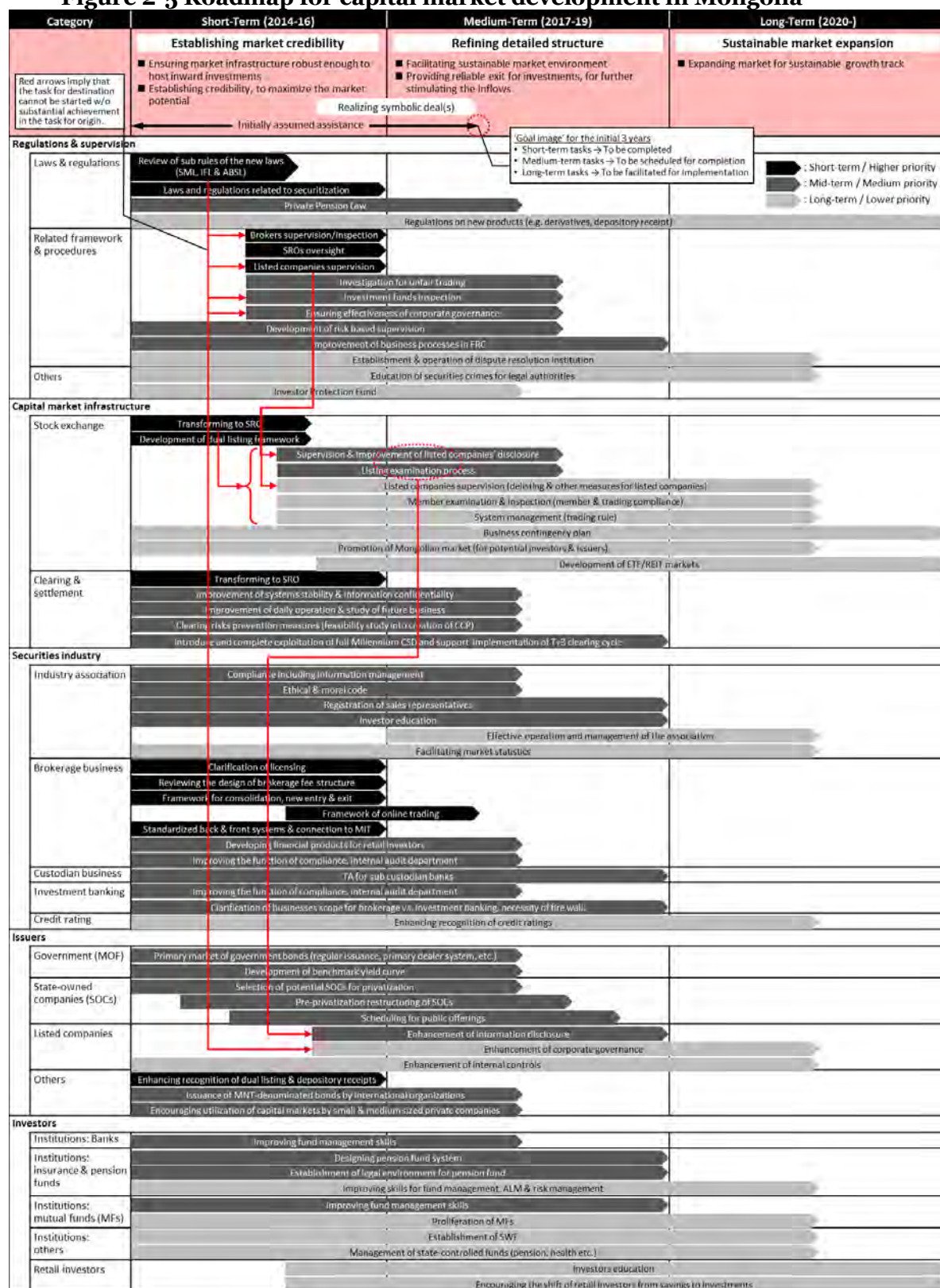
More specifically, the key for the success is to 'remove uncertainty' for the investors as

much as possible. In this regard, introduction of the new laws, such as Securities Market Law and Investment Fund Law, had quite positive impact on the investor sentiment, which was, unfortunately, more than offset by the recent macroeconomic downturn. Going forward, it is critical to keep pushing the implementation of these laws and the relevant regulations, introducing the new products, and providing reliable market infrastructure which contribute to reducing the transaction costs.

At the same time, it is necessary to address the longer-term objectives and to start working on their basis, although immediate result cannot be expected. These challenges include retail investor education, fostering institutional investors through training investment professionals and investment deregulation (although they are not included in the target outputs of this TA), and expanding the variety of the capital market products, etc.

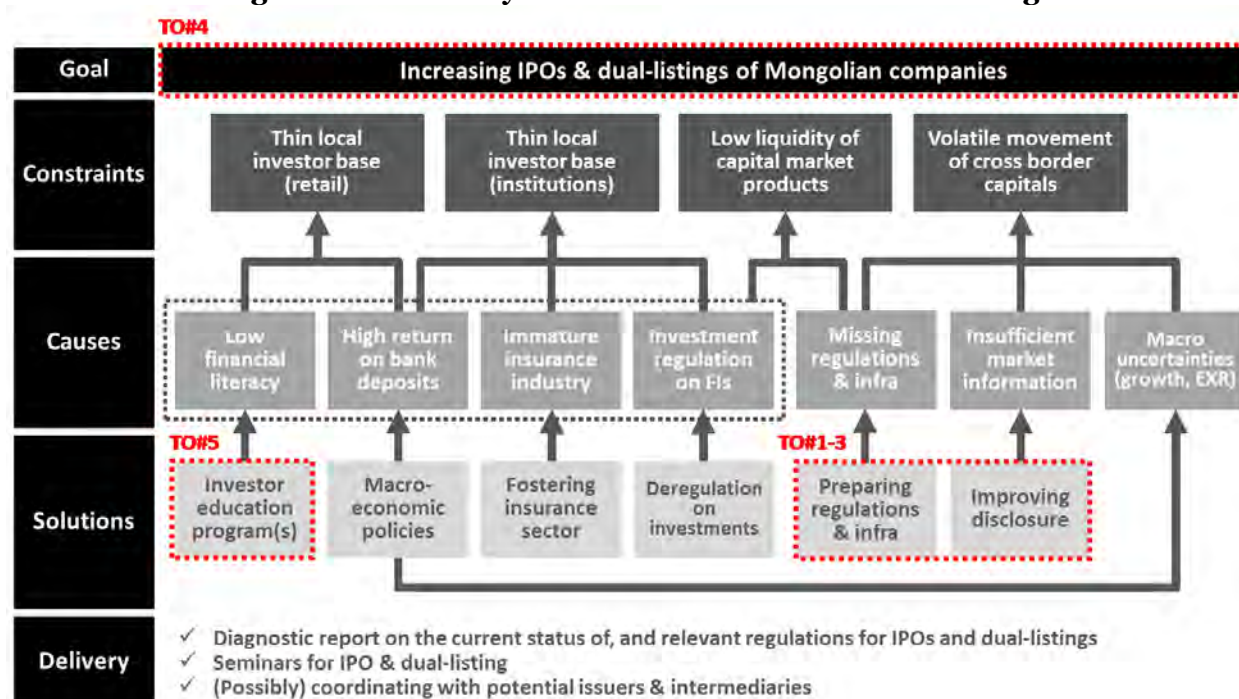
These issues and challenges are summarized in Figure2-6, which shows that IPO/dual listing component of this TA (target outcome #4) is a complex outcome of the measures for other targets (#1, 2 3 and 5). In the rest of this section, relevant measures are listed for the same categories as the previous section --- issuers, investors, intermediaries, stock exchange and the regulator.

**Figure 2-5 Roadmap for capital market development in Mongolia**



Source: JICA Study Team for the 'Data Collecting Survey for Development of Financial and Capital Market, and Capacity Building of its Regulation and Supervision in Mongolia' (2013-14)

**Figure 2-6 Summary of the issues on IPO and dual listing**



Source: JICA Expert Team

#### **a) Issuers**

As discussed earlier, in order for MSE to receive more confidence of the market participants, the most imperative issue is to clean up some of the existing listed companies by delisting those not traded at all. In doing so, it is necessary for FRC and MSE to make rule of delisting rule explicit<sup>9</sup> and to enforce it properly.

In addition, the listed companies will need to make more effort to improve its corporate governance and information disclosure. As for this issue, appropriate cooperation with other DPs and local institutions should be carefully considered to avoiding overlaps, since DPs including the World Bank and IFC have conducted projects on this issue before, and there are local institutions specialized in corporate governance including the National Council on Corporate Governance and Corporate Governance Development Center.

More importantly, it would be helpful to have symbolic IPO deal(s) in drawing attention of the stakeholders and driving relevant resources toward the success of the actual deal(s). In general, potential demand can be classified into the following three groups.

- **Needs for privatizing state owned companies (SOCs)** – Currently the State Property Committee (SPC) is in the process of preparing the list of around 20 candidates for privatization and restructuring for 2015-16. Specifically, additional floating of the power plant companies and coal mining companies such as Baganuur and Shivee Ovoo (both under Erdenes MGL), IPO of MSE, Agricultural Commodity Exchange and other mining-related companies, are being considered. For the IPO candidates, feasibility studies and pre-privatization restructuring are the main emphasis, whereas the possibility of re-listing has been sought for some of the companies delisted so far.

<sup>9</sup> In the MSE's new listing rule, there is an article (Article 23) stipulating conditions and procedures on suspension of trading activity and delisting of securities.

- **Financing needs by medium-sized non-mining private sector companies** – On the domestic-demand oriented side, some of the prospective sectors include infrastructure- related, agro/food processing, telecommunication and import substitution sectors such as construction materials.
- **Financing needs by major banks** – Due to the lack of successful cases in the past, most of the commercial banks are cautious about IPO, and are likely to seek bond financing outside Mongolia. But greater usage of domestic capital markets is expected in the longer-term, as the market impact cannot be ignored once they decide to go for IPO.

## **b) Investors**

**Foreign investors:** Investor demography in Mongolia, with relatively large share of the limited number of foreign institutions/individuals as well as the thin domestic investor base, is less likely to go through immediate change in the near future. Especially considering the growing attention of Western institutional investors on Mongolia as one of the strategic emerging markets, this trend is likely to be strengthened, especially once the current macroeconomic uncertainty is removed.

**Domestic investors:** While the pace of the growth is likely to be slow, gradual changes are necessary. For the retail investors, as one of the focuses of this TA, fund flows into the markets are currently limited, given the high deposit interest rates and the lack of knowledge/ confidence in capital markets. It will become necessary, in the long run, to expand the needs for more active capital markets through guiding the investors from ‘savings’ to ‘investments’ with a view to diversifying their assets. Measures such as tax incentives (e.g. those focusing on IPO deals) shall be considered based on other countries practices, including those in Japan.

## **c) Securities intermediaries**

Most of securities companies in Mongolia do not have actual experience and sufficient expertise to achieve successful IPO transactions. Even the most experienced underwriter in Mongolia, BD Sec, commented during the interviews by the team that they need to have better understanding on the international standards of IPO prospectus. In order to increase the number of IPO deals in MSE, capacity building of securities companies is one of the indispensable component to be included in this TA. In addition to building up overall financial strength of the securities companies, capacity development in underwriting businesses will be needed, not only as an additional source for the securities companies, but also for the sustainable growth of the overall capital markets in Mongolia.

## **d) MSE**

It will be important for MSE to enforce the new listing rule effectively and properly. In addition, MSE will need to strengthen its capacity of analyzing the current and future prospect of business, corporate governance and financial conditions, and of examining the related documents from IPO applicants effectively and efficiently.

## **e) FRC**

As discussed earlier, there are some overlaps between FRC and MSE in supervising newly listing and the already listed companies. FRC will need to streamline its roles and functions of monitoring the listed companies and examining IPO applicants, in coordination with MSE.

## **(3) Probable technical cooperation activities under JICA program**

### **a) Listed companies**

New Chair of FRC commented in the meeting with JICA Expert Team on January 15, 2015 that the target output #4 (increasing IPOs and promoting dual listing of Mongolian companies) is the top priority which FRC expects from this TA project. Even one successful

and symbolic IPO deal could vitalize the current stagnant market through further attracting the investors and candidate issuers at MSE.

In order to accelerate this positive cycle, JICA Consultant team is planning to work closely with FRC, MSE, SPC, MOF, relevant line ministries and underwriters to identify the candidates for IPO at MSE, as well as for dual listing at other exchanges. Especially, the team shall take advantage of the close communications with these stakeholders in;

1. Matching the financing needs with intermediaries, and
2. Identifying the constraints/obstacles in the process of preparing for IPO/dual listing, with a view to feeding them back into the process of revising the existing systems,

on a real time basis. While the direct support for specific issuers and securities companies is beyond the scope of this TA, it is critically important to have a close look at the problems and issues faced by individual players to improve the quality of the feedbacks to FRC, MSE and other stakeholders.

As for the currently listed companies at MSE, improvement in corporate governance and **information disclosure is considered as one of the most urgent issues to restore investors' confidence**. JPX will be able to provide information and training programs on their practices or experiences in the field of corporate governance and information disclosure.

#### **b) Investors**

See “5. Enhancing financial literacy for general public”

#### **c) Securities intermediaries**

In order to strengthen capacity and expertise in underwriting, the team, with the support of Japanese major securities companies including Daiwa Securities, will be able to provide information and training programs on the roles and functions of underwriters in the process of IPO and dual listing. The delivery shall take the form of seminars involving both potential issuers and intermediaries, and the possible topics include:

- Benefit of IPO/dual listing (by),
- Global trend of IPO/dual listing ( - do - ),
- **Underwriter's roles in IPO/dual listing** ( - do - ),
- Relevant laws/regulations/institutional framework in Japan (by FSA)
- Listing rules and examinations (by JPX), and
- Preparation and procedure for IPO/dual listing (by securities companies and MSE),

with an emphasis on the implications on the capital market in Mongolia.

#### **d) MSE**

In this TA project, JPX will play the most important role in strengthening the capacity of MSE in its examination of IPO candidates and monitoring of the listed companies. MSE will also need more marketing activities to broaden international investor base including those from Japan. The team and JPX will work together to hold seminars for MSE, covering these issues.

#### **e) FRC**

With a view to ensuring the sustainable securities industry which can accommodate future IPO/dual listing deals, FRC will need to focus on designing the securities industry, including optimal size, number of players, etc., in addition to developing the framework of risk-based supervision discussed in the previous chapter. Specifically, it will become necessary to prepare future consolidation scenario of the industry after enforcing new minimum capital requirements. FSA and the team shall provide information on policy experiences in Japan and implications for Mongolia regarding the industry consolidation. Also for stimulating the appetite for IPO shares, tax measures can be examined and

adjusted, with the inputs from FSA based on the experiences/practices in Japan and other countries.



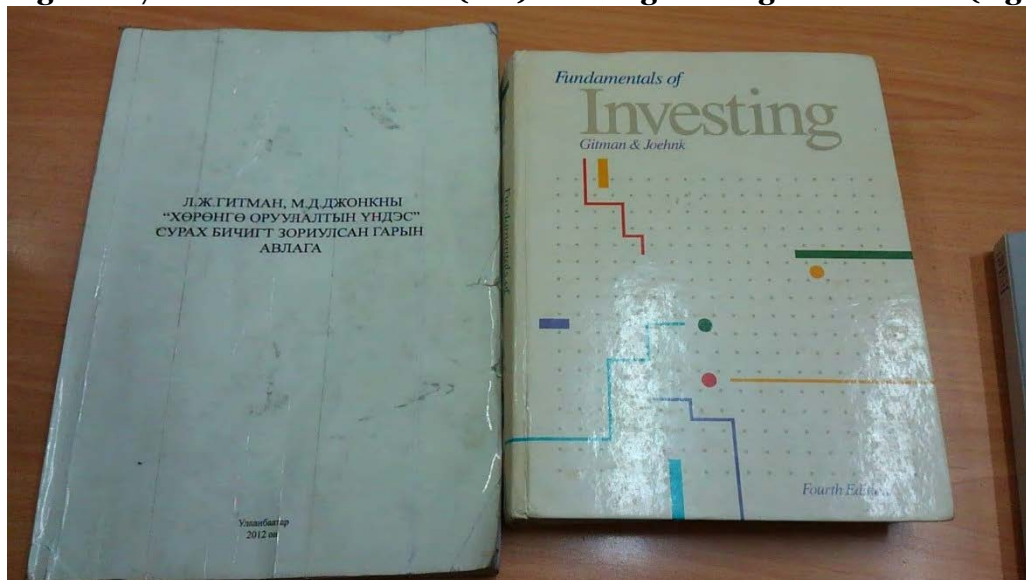
## 5. Enhancing financial literacy for general public

### (1) Review on the current situation in Mongolia

In Mongolia, there is neither specific education nor training focused on improving financial literacy including the investor education open for the public in general.

At middle school and high school age, there are no curriculum that aims on money education and courses that teach financial terms, while only occasion that is related securities industry is the study tour to the MSE during the excursions to UB. Even at the higher education for instance, there is no finance textbook written in Mongolian language used amongst the faculties of Economics Department at the National University of Mongolia a prestigious university in Mongolia. Given the situation, some of the professors prepare translated version of the English textbooks obtained from abroad as handout materials.

**Figure 2-7 Translated textbook (left) and original English textbook (right)**



Source: JICA Consultant team

Similarly, the investor education channels available to the retail investors are also scarce. FRC provides very brief explanation of knowledge and concepts regarding the capital markets in Mongolia on their website. At MSE, some basic knowledge on securities and investment are shown on their website and in addition, short basic training courses on securities trading are offered to the general public. Few securities companies provide capital markets related half-day seminars in several occasions and one of them also provide some knowledge and awareness via its publications. Moreover, currently there exist no platform of financial knowledge and jargons available to the public to fully understand and meet their interests towards capital markets and securities trading.

**Figure 2-8 Publication by one of the securities company**





Source: JICA Consultant team

Likewise, structured educational and training programs for the financial professionals are also limited in Mongolia. MSE provides series of training courses for the prospective professionals and examination for dealers and brokers. Mongolian Association of Securities Dealers (MASD) also provides internal training to those 45 (out of 71 securities dealers/brokerage licensed firms) member companies however, the trainings are conducted on an ad-hoc basis due to limited trainers and 26 non-members to the association do not usually participate. In addition, the Financial Markets Association (FMA) offers training courses to the professionals but the contents and frequencies are both insufficient due to limited capacity.

Given the current situation, the World Bank has been supporting the Mongolian government as well as the financial regulators including BoM and FRC to draft “National Strategy for Financial Literacy” in order to improve awareness and financial literacy of the general public. This strategy is aiming to be implemented by the end of 2015 and the actual financial education and training programs will start from the following year. In addition, ADB has been supporting relevant institutions to create a series of TV drama aiming to educate the general public and started broadcasting since December 2014. However, these programs provided by the international donors have more focuses on financial inclusion rather than the

Luxembourg Agency for Development Cooperation (Lux Dev) has been providing technical cooperation programs targeting more specifically FRC and financial institutions since 2012. As one of their key outputs, Lux-Dev supported the FRC to publicize three booklets on capital markets, insurance business, and microfinance all with financial terms and glossaries in local language. These booklets however are limited only amongst the relevant counterparties such as the financial authorities and financial institutions such as banks, insurance companies and NGOs. The training programs are also not specifically focused on the actual operations regarding capital markets and securities trading but rather more emphasis on institutional capacity buildings aspects.

**Figure 2-9 Publication by Luxembourg Development**



Source: JICA Consultant team

## (2) Possible solutions

Based on the current situation and the necessities for the capacity buildings to improve financial literacy and awareness amongst the relevant parties such as the regulators and financial institutions as well as the public, the consultants propose several technical cooperation activities as follows:

- Provide series of seminars / lectures: target audiences and the contents shall be determined at the necessary basis with prioritizations along with the level of difficulties.
- Assist in structuring the national framework regarding the financial literacy: this includes who takes the initiative and what sort of knowledge and information to be disseminated to the public from which platform.
- **Support in drafting “media mix strategy” to promote financial literacy: primary focus on the delivery channels via social network services (SNS), TV shows, radio program, newspapers, magazines, websites, educational institutions, etc.**

## (3) Probable technical cooperation activities under JICA program

Further details of the activities are subject to consultation with the FRC as well as JICA.



Japan International Cooperation Agency

# **Self Regulatory Organization:**

**A concept paper**

---

15 December 2016

JICA Consultant Team

## **Contents**

---

- 1. What is an SRO?**
- 2. MSE as an exchange SRO**
- 3. MASD as an association SRO**

## 1. What is an SRO? - Overview

---

### Overview

- ✓ Self Regulatory Organization (SRO) is **an organization that is organized to regulate the market operations and the ethical standards of practice and business conducts of its members** as for the purpose to promote investor protection and market development.
- ✓ SROs are usually stipulated by relevant laws, and registered or regulated by the government authorities.
- ✓ SROs function as a semi-regulator as they monitor the market operations to minimize any wrong doings and frauds .
- ✓ SROs also function as a promoter of industry development via providing necessary trainings and education to those professionals working for the industry.

3

## 1. What is an SRO? - IOSCO's principles

---

### IOSCO's principles

- ✓ The regulatory regime should make appropriate use of SROs that exercise **some direct oversight responsibility** for their respective areas of competence and to the extent appropriate to the size and complexity of the markets.
- ✓ SROs should be subject to the oversight of the regulator and should observe standards of fairness and confidentiality when exercising powers and delegated responsibilities.

## 1. What is an SRO? - Benefits from SROs

---

### Benefits from SROs

- ✓ SROs may require the observance of ethical standards which go beyond government regulations.
- ✓ SROs may offer considerable depth and expertise regarding market operations and practices, and may be able to respond more quickly and flexibly than the government authority to changing market conditions.

Source: IOSCO, *Objectives and Principles Of Securities Regulation*, May 2003

5

## 1. What is an SRO? - SRO categories

---

### Types of SROs

- ✓ There are mainly two types of SROs in the capital markets, each with different functions and responsibilities: **exchange SROs**; and **association SROs**.
- ✓ FRC approved MASD, then MSE as an SRO in 2015.

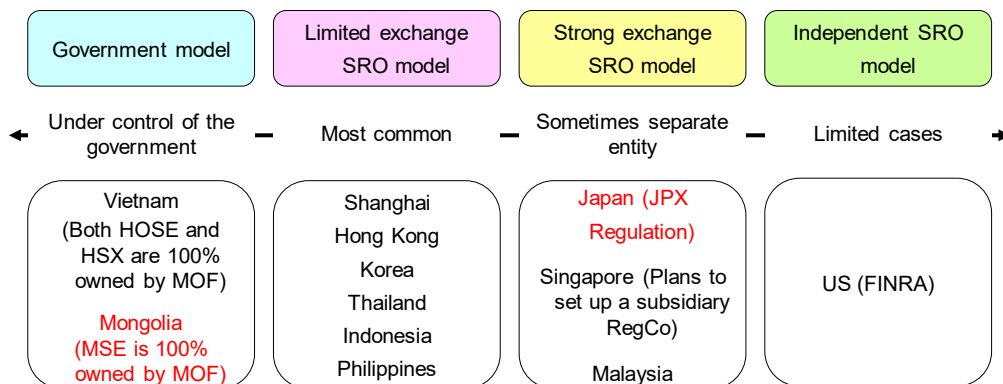
Categories	Major functions
Exchange SROs	<ul style="list-style-type: none"><li>✓ Management of listed companies' eligibility</li><li>✓ Monitor trading activities</li><li>✓ Monitor trading participants</li></ul>
Association SROs	<ul style="list-style-type: none"><li>✓ Promote standards and ethical practices for member companies and sales representatives</li><li>✓ Provide guidelines and best practices</li><li>✓ Educate and train sales representatives</li></ul>

6

## 1. What is an SRO? - Exchange SROs

### Models of exchange SROs

✓ Exchange SROs are categorized in four models: **government**; **limited exchange SRO**; **strong exchange SRO**; and **independent SRO**.



Source: Clemente L. del Valle, *The Future of Self-Regulation in Securities Markets*, April 2010, JICA Consultant Team

7

## 1. What is an SRO? - Association SROs

### Association SROs - list of securities industry associations in Asia

Country	Association	Regulated by	SRO
Japan	Japan Securities Dealers Association	Financial Instruments and Exchange Act	Yes
China	Securities Association of China	Law of the People's Republic of China on Securities	Yes
Hong Kong	Hong Kong Securities Association	-	No
Korea	Korea Financial Investment Association	Financial Investment Services and Capital Markets Act	Yes
Taiwan	Taiwan Securities Association	Securities and Exchange Act	Yes
Singapore	Securities Association of Singapore	-	No
Malaysia	Association of Stockbroking Companies Malaysia	Societies Act	No
Thailand	Association of Thai Securities Companies	Securities and Exchange Act	No
	Thai Bond Market Association	Securities and Exchange Act	Yes
Indonesia	Association of Indonesian Securities Companies	-	No
Philippines	Philippine Association of Securities Brokers and Dealers	Securities Regulation Code	No
Vietnam	Vietnam Association of Securities Business	Ministry of Home Affairs Decree	No
	Vietnam Bond Market Association	Ministry of Home Affairs Decree	No
Mongolia	Mongolian Association of Securities Dealers	Securities Market Law	Yes

Source: 6<sup>th</sup> Comparative Analysis of Asian Securities Regulators & SROs and Market Characteristics

8

## 1. What is an SRO? - SROs' major responsibilities

---

Regulatory responsibilities by SROs

Level of regulation	Responsibilities	Regulatory activities
Overall market regulation	Overall supervision of markets and intermediaries' market conduct and trading practices	<ul style="list-style-type: none"><li>• Rule making</li><li>• Supervision</li><li>• Enforcement</li></ul>
Market conduct standards	Principles of fair dealing, regulation of insider trading, deceptive and manipulative trading	<ul style="list-style-type: none"><li>• Rule making</li><li>• Supervision</li><li>• Enforcement</li></ul>
Exchange trading rules	Market integrity rules and trading practice rules for each marketplace	<ul style="list-style-type: none"><li>• Rule making</li><li>• Supervision</li><li>• Enforcement</li></ul>
Market surveillance	Monitoring of trading in each marketplace for compliance with rules	<ul style="list-style-type: none"><li>• Supervision (market surveillance, trading analysis)</li><li>• Investigations and enforcement</li></ul>

Source: The World Bank, *Self-Regulation in Securities Markets*, January 2011

9

## 2. MSE as an exchange SRO - Responsibilities

---

### Responsibilities as an SRO

- ✓ We believe that there will be **no major changes** in MSE's operations. MSE's major operations are **1) listing management, and 2) monitoring trades**.
- ✓ A major change is that MSE is now **a responsible entity** to make the rules, supervise, and enforce them. MSE is responsible for listing and trading matters in the stock market, instead of FRC.
- ✓ FRC supervises MSE. Approval of the rules made by MSE is FRC's responsibility.

10

## 2. MSE as an exchange SRO - Listing management

---

### Listing management

- ✓ We believe that improving listing management is **top priority** for MSE. MSE's SRO activities should be focused on listing management, in our view.
- ✓ Tighter control of listing management helps **separating quality companies with good disclosure** from those with weak fundamentals or those not meeting the current listing requirements.



Two big issues for the current listed companies:

- 1) Disclosure by most of the current listed companies are far from the international standards; and
- 2) MSE's average public float is below 10%, resulted in very low liquidity.

11

## 2. MSE as an exchange SRO - Key tasks for listing management

---

### Major tasks for listing management

- 1) Approve **only good companies** for listing.
  - ✓ Set appropriate **listing requirements** – only limited number of companies are eligible to list their shares.
- 2) Monitor listed companies' **eligibility**.
  - ✓ Enforce continuing listing obligations – **disclosure** and **public float** are two of the major obligations.
  - ✓ Set **delisting rules** – ineligible companies need to leave the market.

12



## 2. MSE as an exchange SRO - Listing requirements

Listing requirements consist of 1) **quantitative requirements**, and 2) **qualitative requirements**. Typical quantitative and qualitative requirements are as follows:

Quantitative requirements	Profitable for the last two consecutive years
	Minimum share capital / market cap
	Minimum number of shareholders
	Minimum public float
Qualitative requirements	Business continuity with profitability
	Quality management
	Good corporate governance and internal control
	Disclosure

13

## 2. MSE as an exchange SRO - Disclosure

### Types of disclosure

- 1) Legal disclosure
  - ✓ Annual financial reports (**not only numbers**)
  - ✓ Semi-annual/quarterly financial reports (**not only numbers**)
- 2) Timely disclosure
  - ✓ **Earnings releases**
  - ✓ Material facts (earnings forecast change, dividend increase/decrease, M&A, financing, stock split, new product/service launch, change of CEO etc.)
- 3) Voluntary disclosure
  - ✓ Production volume, product/material prices, sales breakdown by product etc.

14

## 2. MSE as an exchange SRO - Public float

---

### MSE's public float

- ✓ MSE's public float is **below 10%**, in our understanding
- ✓ Too low public float adversely impacts minority investors' interest
- ✓ Listed companies with too low public float should understand meaning of listing
- ✓ For instance, a listed company with 95% of shares outstanding held by certain investors, such as founders' family, cannot be called a "public company"
- ✓ Foreign investors do not invest in those with low public float, as they are afraid of **difficulty in selling their shares**
- ✓ We believe that **companies with too low public float should be delisted**

15

## 3. MASD as an association SRO - Responsibilities

---

### Responsibilities as an SRO

- ✓ Only half of securities associations in Asia are SROs, the rest of them are industry association without self-regulatory functions.
- ✓ Association SROs are typically responsible for **1) regulating securities sales representatives, and 2) monitoring securities companies.**
- ✓ Some association SROs are also **responsible for qualifying securities professionals.**

16

### 3. MASD as an association SRO - Securities professional license

---

#### Securities professional license

- ✓ MASD provides a two-week training course for sales representatives, which is mandatory for those who want to be licensed as securities professionals.
- ✓ Although a series of lectures for the training course is quite comprehensive, we think that some of the current subjects are **less relevant to securities business in Mongolia**.
- ✓ In addition, there is **no official textbook** for the securities professional license exam.
- ✓ We believe that publishing an official textbook is **top priority** for MASD's SRO activities.

**Policy Committee**  
**Project for Capacity Building of Capital Market in Mongolia**

**Contents**

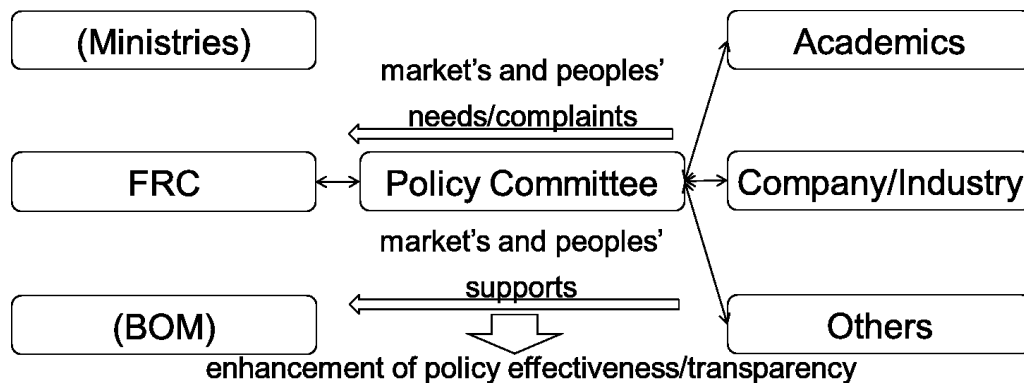
1. A Concept of Policy Committee (Council)
2. Japan's Financial System Council
3. Current FRC Policy Committee\*

\*According to acquired information by JICA Consultant Team

**1. A Concept of Policy Committee (Council)**

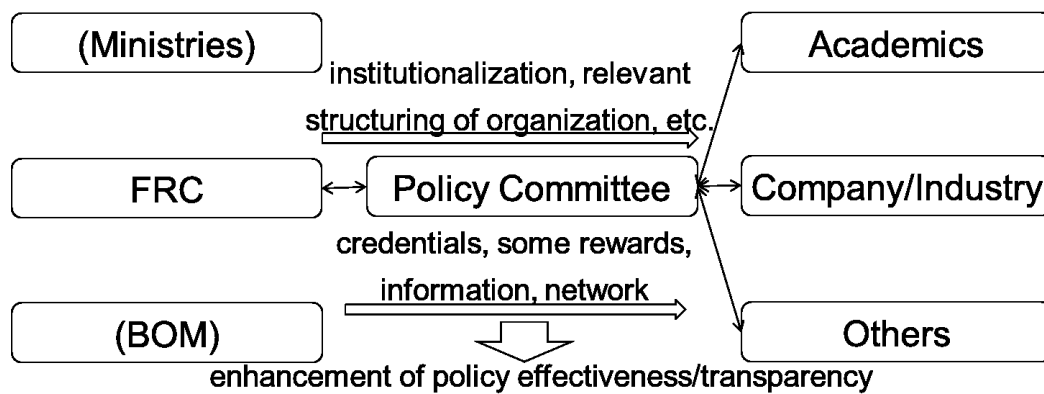
**Definition and Merits for FRC**

- Definition: An advisory, deliberative, or administrative body of people formally constituted and meeting regularly
- For FRC, a tool to draw up needs, complaints and supports on certain issues, thus enhance policy effectiveness and transparency



**Precondition and Merits for Company/Industry, Academics**

- Precondition: FRC should ensure of institutionalization, relevant structuring of organization, member, etc.
- Company and Industry, Academics can gain credentials, some rewards, alongside with information and network.



## 2. Japan's Financial System Council

### Institutionalization

- Based on Financial Services Agency (FSA) Establishment Act, 1998, with organization, member, etc. stipulated
- To have deliberation and deliver an opinion on important issues
  - ✓ related to financial system improvement, etc.
  - ✓ based on a request from the Prime Minister, the Commissioner of FSA, the Minister of Finance

### Organization

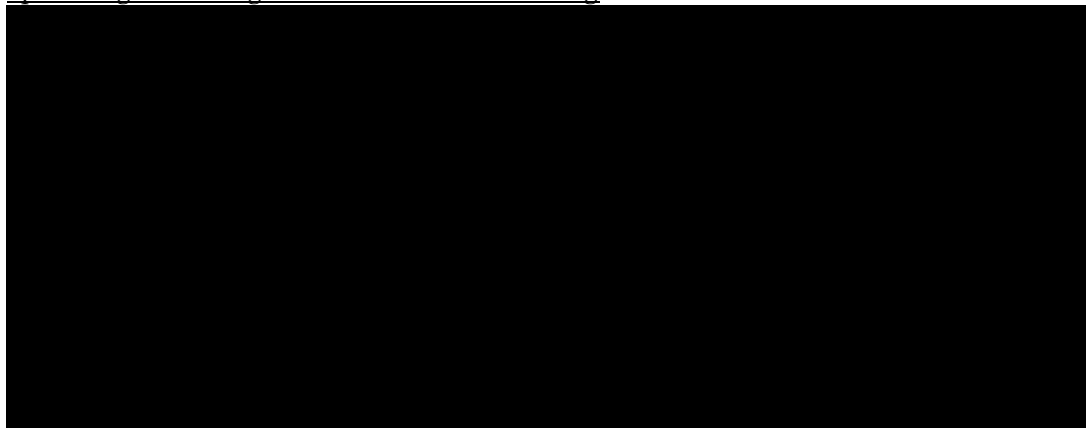
- Financial System Council is one of FSA's many advisory bodies.

<p><b>Panel of Experts on Fin-Tech Start-ups</b></p> <p><b>Advisory Council on the Systems of Accounting and Auditing</b></p> <p><b>Council of Experts Concerning the Follow-up of Japan's Stewardship Code and Japan's Corporate Governance Code</b></p> <p><b>Council of Experts Concerning the Corporate Governance Code</b></p> <p><b><u>Financial System Council</u></b></p> <p><b>Business Accounting Council</b></p> <p><b>Study Group on Regulation of Financial Benchmarks</b></p> <p><b>Panel for Vitalizing Financial and Capital Markets</b></p> <p><b>Council of Experts Concerning the Japanese Version of the Stewardship Code</b></p> <p><b>Public-Private Financial Roundtable</b></p> <p><b>Study Group on Financial Education Report</b></p> <p><b>Compulsory Automobile Liability Insurance Council</b></p> <p><b>Financial service dispute resolution liaison group</b></p> <p><b>Study Group on taxes related to financial markets and financial transactions</b></p> <p><b>Roundtable Committee on the Vision of the Japanese Financial System and Policies in the Future</b></p>
--

<http://www.fsa.go.jp/en/measures/index.html#02> (regularly updated)

### Agenda

- Financial System Council has Working Groups for market /company needs, operating according to the definite scheduling.



[http://www.fsa.go.jp/en/refer/councils/singie\\_kinyu/reports.html](http://www.fsa.go.jp/en/refer/councils/singie_kinyu/reports.html) (regularly updated)

Member

- Totalling less than 30 with ad hoc members when needed
  - ✓ Appointed by the Prime Minister with approval from the Diet
  - ✓ Basically, Not from government ministries or political party
  - ✓ Primarily from Private company, Academics, etc.
  - ✓ Banks, securities company and their affiliates included
  - ✓ Foreign company invited (foreign nationals Not excluded)
  - ✓ Credentials bestowed with some rewards
  - ✓ Significant for information retrieval and network

<Financial System Council Member as of Oct. 2016>

- Totalling 19 members
- 11 from Academics including the chairman
- 5 from Private companies including bank and securities group  
(Boston Consulting, Nomura Research Institute, Japan Research Institute, Mitsubishi Corp., Recruit Holdings)
- 1 lawyer, 1 from labor union, 1 from consumer organization

<Working Group Member: examples>

Name of the Working Group (WG)	Term / # of meetings	# of members / Head of the Group	examples of outside lecturers
<b>WG: Investment Management</b>	Oct 2014 - / 6	17 / Mr. Kanda, prof., Univ. of Tokyo, Graduate school of law and politics	Nomura Institute of Capital Markets Research, SESC, National Consumer Affairs Center, Nippon Technology Venture Partners, The Japan Academic Society for Ventures and Entrepreneurs, Japan Federation of Bar Associations, Japan Venture Capital Assoc., etc.
<b>WG: Sophistication of Payment and Settlement Operations</b>	Oct 2014- / 10	23 / Mr. Iwahara, prof., Waseda Univ. Law School	NTT Data Group, Japan Bankers Assoc., The Japan Research Institute, Fujitsu, Bank of Japan (BoJ), Deloitte Tomatsu Consulting, JCCI, National Consumer Affairs Center, The Center for Financial Industry Information Systems, etc.
<b>WG: Mid- and Long-Term Roadmap of the Financial Industry in Japan</b>	Jun 2011 - May 2012 / 14	21 / Mr. Yoshino, prof., Keio Univ. Economics Dept.	Bank of Tokyo-Mitsubishi UFJ, Tokio Marine Holdings, Daiwa Securities, Japan Center for Int'l Finance, Sumitomo Chemical, Mitsubishi Corp., HSBC, JPMorgan, Goldman Sachs, Citigroup, BoJ, Dogan Advisors, The Kagoshima Bank, Sumitomo Mitsui Asset Management, Japan Assoc. for Financial Planners, MorningStar, Carlyle Japan, A.T.Kearney, Nomura Research Institute, etc.

[http://www.fsa.go.jp/en/refer/councils/singie\\_kinyu/20150713/01.pdf](http://www.fsa.go.jp/en/refer/councils/singie_kinyu/20150713/01.pdf)  
(WG: Investment Management, regularly updated)

#### Number of Meetings

- Financial System Council: A few times a year
- Working Groups: Frequently
  - ✓ Investment Management WG: 5 times in 3 months
  - ✓ Provision of Risk Money to Emerging and Growing Companies WG: 11 times in 6 months

#### Management

- Financial System Council & Working Groups:
  - ✓ FSA secretariats implement research on issues and prepare materials beforehand for members' use.
  - ✓ After the meeting, minutes & materials of every meeting are web-disclosed.
  - ✓ FSA reflects meeting results to policy amendment and new legislation, while continuously following up pending issues.

1

July 19th, 2016

Financial Services Agency

### **Publication of the Report by the “Working Group on Corporate Disclosure” of the Financial System Council**

The “Working Group on Corporate Disclosure” of the Financial System Council (chairman Hideki KANDA, Professor, Law School, Gakushuin University) has discussed and deliberated on corporate disclosure five times since November 2015.

Based on the results of the discussions, the Working Group has compiled and published the “Report - Promoting Constructive Dialogue”.

The “Report” (as attached hereto) is a provisional translation of the original Japanese report.

[Report - Promoting Constructive Dialogue \(PDF: 220KB\)](#)

[Summary of the Report - Promoting Constructive Dialogue \(PDF: 61KB\)](#)

#### Contact

Financial Services Agency

Tel +81-(0)3-3506-6000(main)

Corporate Accounting and Disclosure Division, Planning and Coordination

Bureau

(ext. 3665, 3802)

[http://www.fsa.go.jp/en/refer/councils/singie\\_kinyu/20160719-1.html](http://www.fsa.go.jp/en/refer/councils/singie_kinyu/20160719-1.html) (regularly updated)

### 3. Current FRC Policy Committee

#### Institutionalization

- By the Order of the FRC Chairman, September 2014
- To have deliberation and to issue recommendation on important issues on the relevant policy and regulations
- FRC Law does not clarify roles/functions of Policy Committee
  - ✓ which could strengthen its position and influence in the policy process, and
  - ✓ which could ensure of credentials and some rewards for participating Company/Industry and Academics.

#### Organization, including Number of Meetings

- In September 2014 FRC decided to establish Policy Committee.
- In March 2015 FRC amended its decision into establishment of 6 Policy Councils.
- Since then, Orders of the FRC Chairman were issued for establishment of each Policy Council.
- 4 Policy Councils have been working until March 2016, followed by a current standstill, reflecting change in the political situation.

(Council name)	(hosted month/year)
✓ Capital Market	(6,9/2015, 3/2016)
✓ Mining Investment and Minerals	(4,6,8,10/2015)
✓ Commodity Exchange	(4,5,9/2015)
✓ Insurance	(no meeting)
✓ Microfinance	(6,7,7/2015)
✓ Risk Management	(no meeting)

#### Agenda

- Capital Market Council, at first, planned to discuss 6 areas:
  - 1) new financial products
  - 2) raising of institutional investors
  - 3) securities infrastructure
  - 4) legislation
  - 5) taxation
  - 6) investor education
- Actually, meetings were held ad-hoc, depending on the current and urgent issues which FRC thought should be addressed:
  - 1) split of function of CSD (Clearing, Settlement, Deposit)
  - 2) tax policy to promote the capital market
  - 3) privatization of SOEs listed in MSE
  - 4) private pension funds, etc.

#### Management

- Capital Market Council
  - ✓ Documents for discussion were sent to members by FRC.
  - ✓ After the meeting, summary of the meetings was disclosed on the FRC website in Mongolian but not in English.
  - ✓ Although FRC submitted recommendations of the Committee to the



Parliament and Ministries, it is not certain if they were considered seriously by them, possibly because:

- 1) Policy Committee was not regarded as officially institutionalized advisory body yet, and also,
- 2) More importantly, thorough discussions with a wide range of viewpoints were not made within a very short time-frame of the past meetings.

Member

- Capital Market Council (totaling 13)
  - ✓ Assigned by FRC Chairman  
Appointment by Prime Minister/Diet should be considered.
  - ✓ 3 from Government-related organizations (FRC/MOF/BOM)  
Government-related sector can be reduced.
  - ✓ 7 from Company/Industry and 1 from DBM
    - 1) Financial Market Association and Golomt Bank
    - 2) MASD, Ard Capital Group Securities Company
    - 3) Mongolian Bankers Association, Deposit Insurance
    - 4) BDSec
    - 5) Energy Resource <Lawyer>
    - 6) TDB
    - 7) MNCCIPrimarily from Company, Academics, etc.  
Affiliates of banks/securities company should be increased.  
(ex: TDB Capital, Golomt Securities, Tulgat Chandmani B)  
Foreign company and foreign expats should be utilized.
  - ✓ 3 from Academics
  - ✓ 1 from others
  - ✓ Merits: Credentials? Some rewards? Information?

**Project for Capacity Building of Capital Market in Mongolia:  
Consulting Approach for IPO & Dual Listing**

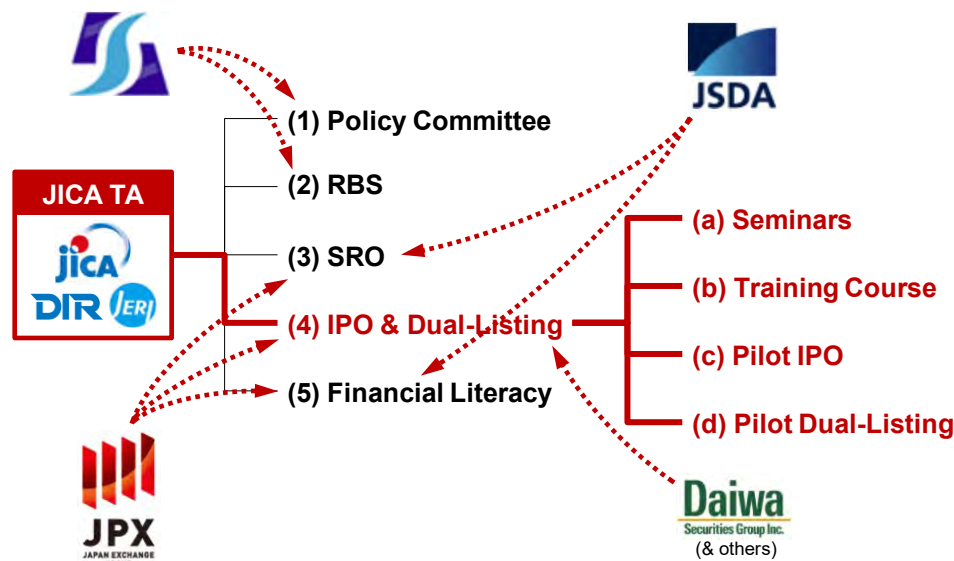
---

March 31, 2015

Daiwa Institute of Research  
Japan Economic Research Institute

Consulting Framework

---



#### (4)-(a) Seminars (on IPO & Dual-Listing)

---

- **Target beneficiaries:** FRC, MSE, underwriting companies, potential issuers of equity securities (SOCs, private sector companies)
- **Schedule (tentative):** Apr-Jun 2015, Jan-Mar 2016, Oct-Dec 2016 (all in UB)
- **Inputs expected from:** JPX, securities company/ies in Japan
- **Issues to be covered (tentative):**
  - Benefit of IPO / dual-listing
  - Preparation process for IPO / dual-listing
  - Pre-IPO restructuring
  - Introduction of other exchanges
  - Listing rules & other regulations
  - Investor relations (IR) activities
  - Secondary market regulations, etc.

3

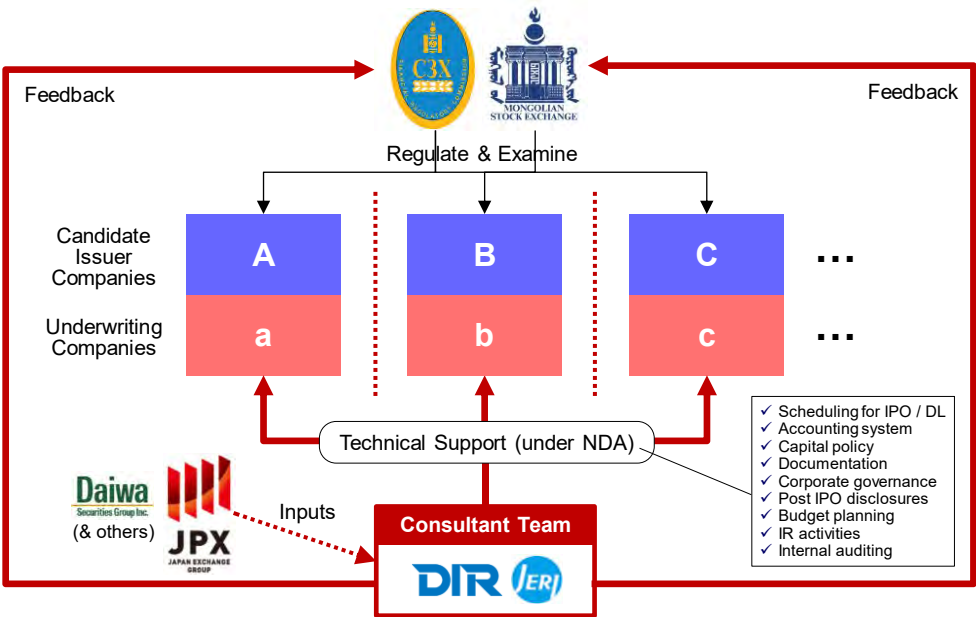
#### (4)-(b) Training Course (on IPO & Dual-Listing)

---

- **Target beneficiaries:** FRC, MSE
- **Schedule (tentative):** Apr-Jun 2016 (Tokyo), Oct-Dec 2016 (UB), Jan-Mar 2017 (Tokyo)
- **Inputs expected from:** JPX, securities company/ies in Japan
- **Issues to be covered (tentative):**
  - Benefit of IPO / dual-listing (incl. other countries' practices)
  - Listing rules & regulations
  - Listing examination
  - Roles of regulatory authorities & stock exchange
  - Roles of security companies, etc.

4

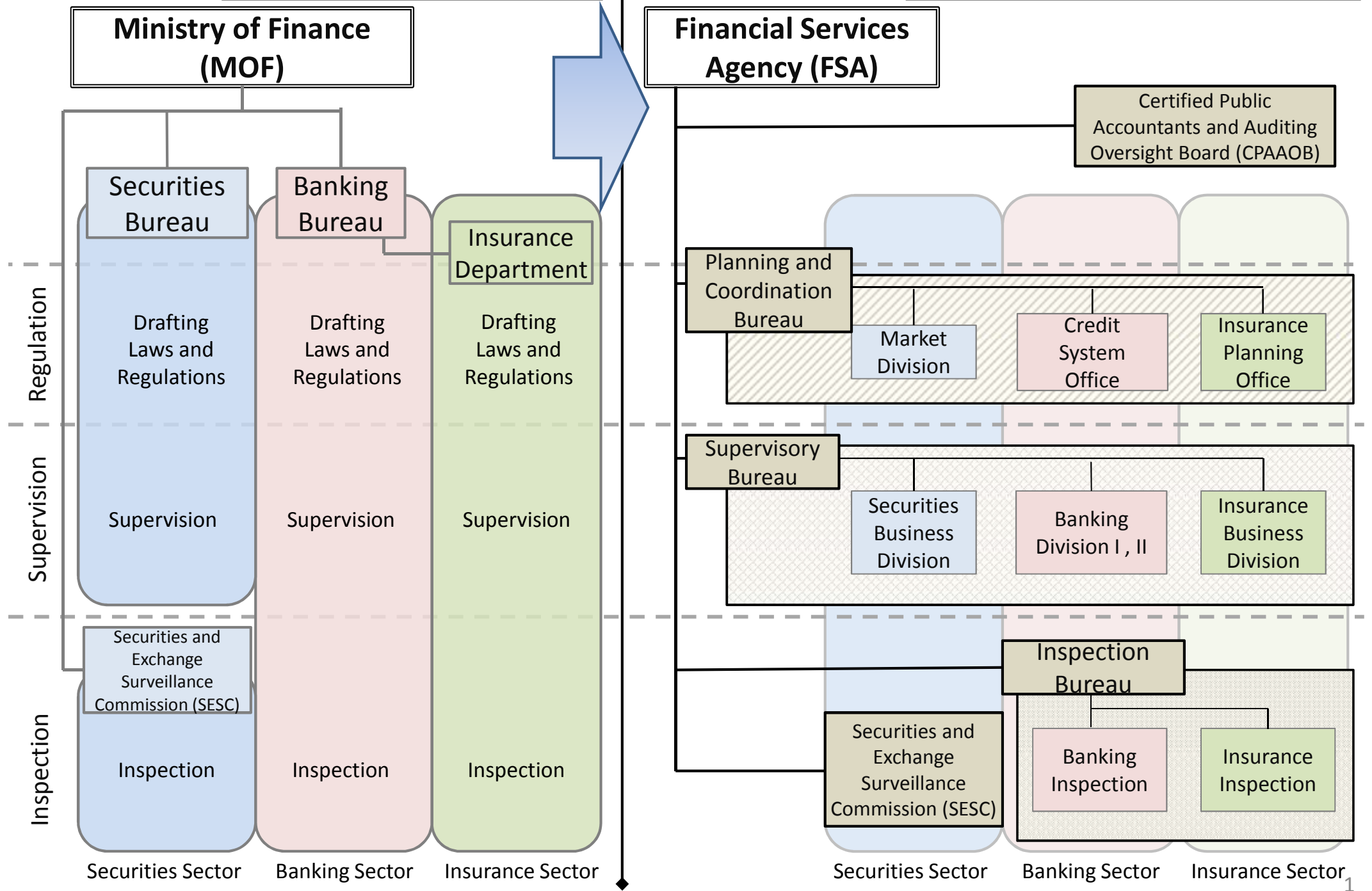
(4)-(c),(d) Pilot IPO & Dual-Listing



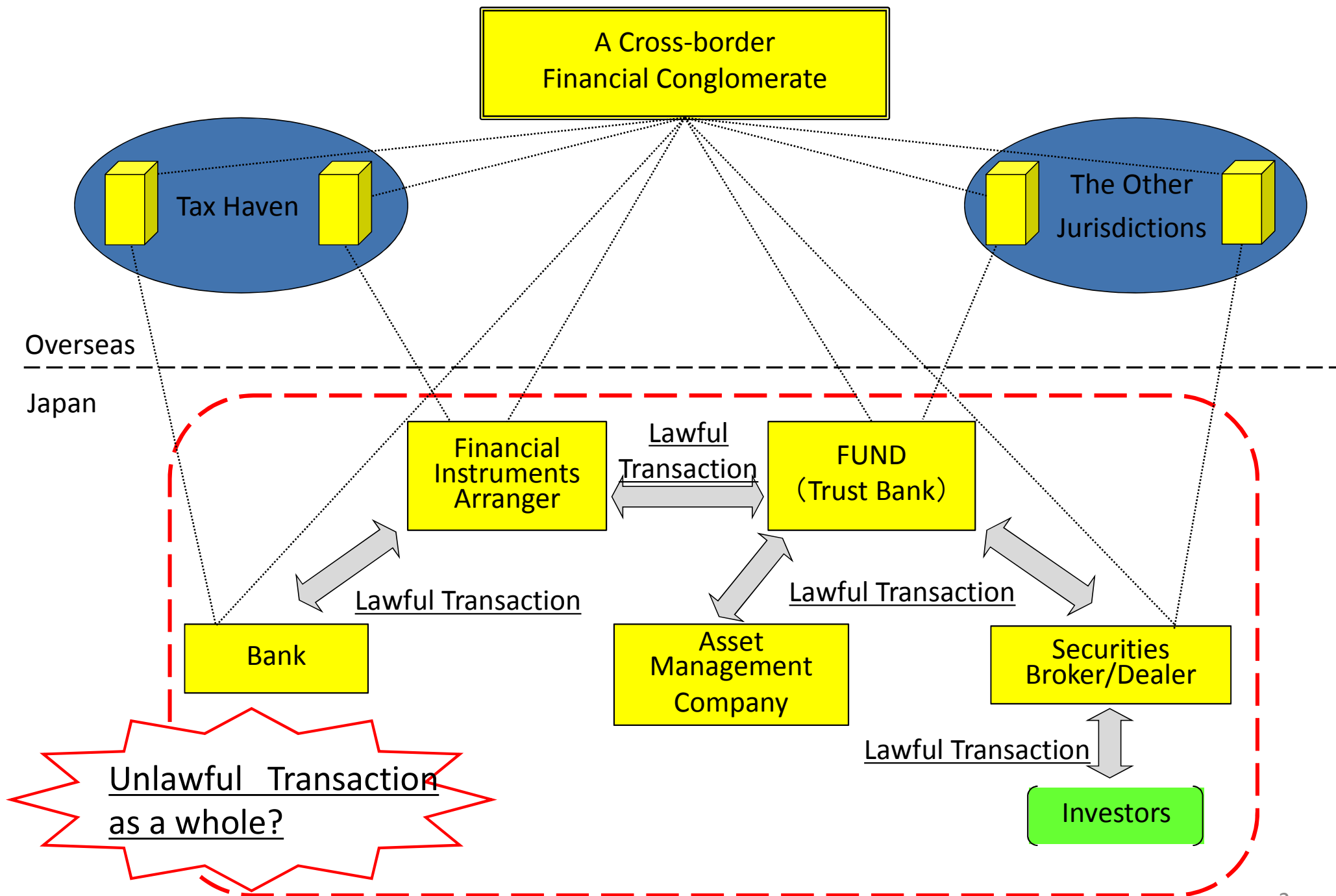
# Organization Structure for Regulating & Monitoring Financial Sector

*Past : Vertically Divided*

*Present : Functionally Divided*

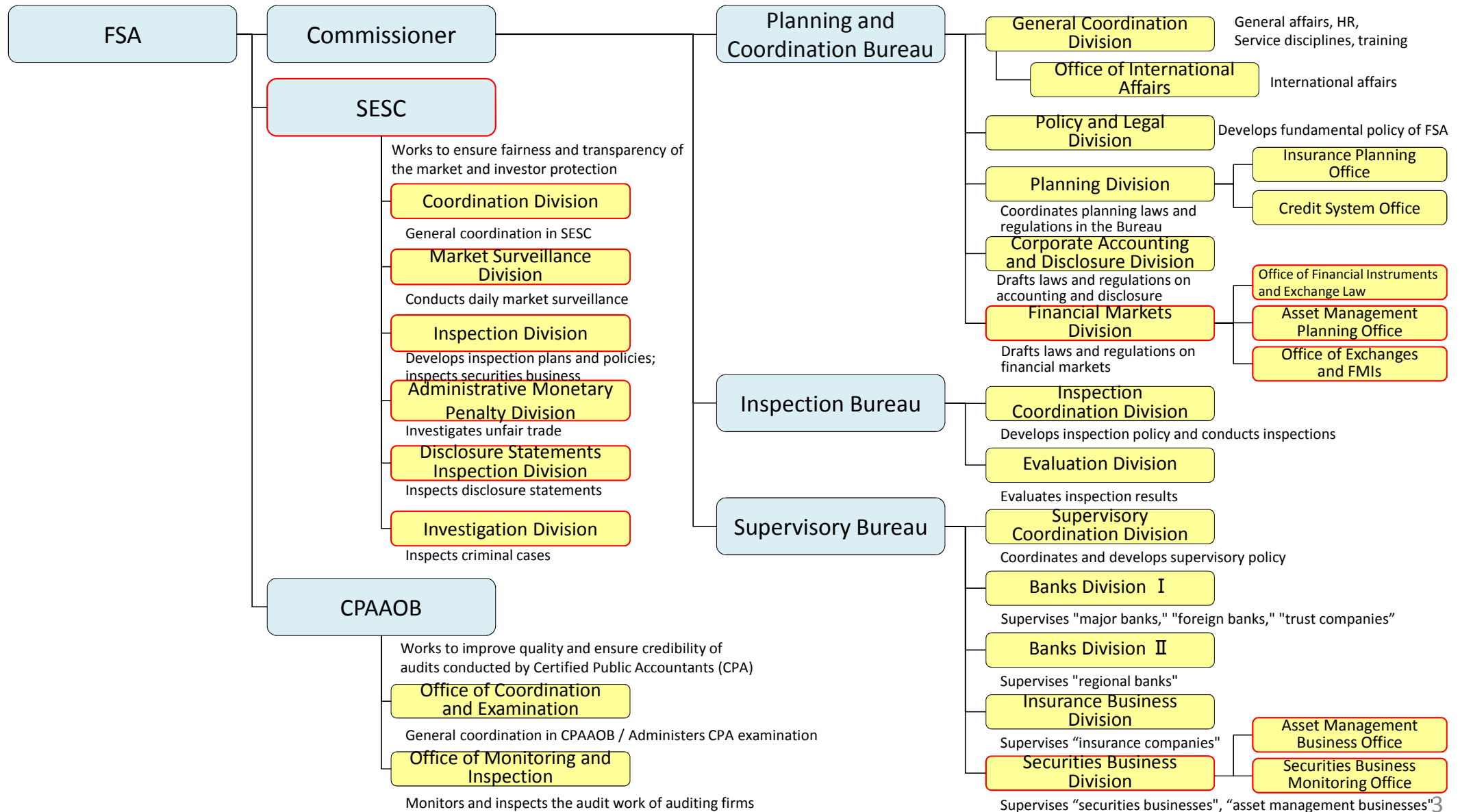


# Problem in the Vertically Divided Administrative Structure



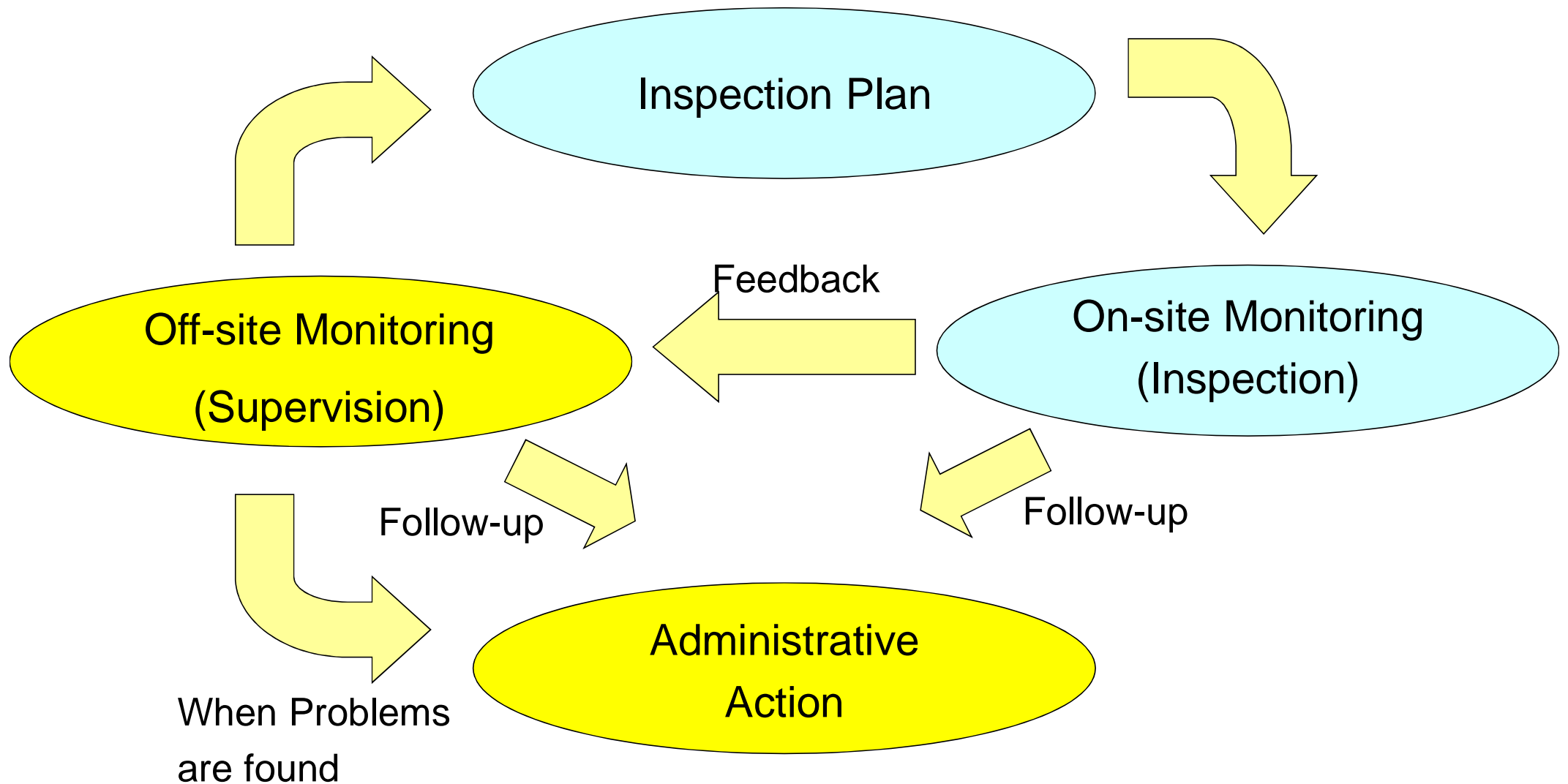
# Detailed Organization Structure

- The FSA is responsible for supervision and inspection for Banking, Securities and Insurance sectors as well as planning relevant laws and regulations and participating in international discussions.
- The number of staff in the FSA have increased to **1,600** while it was about **400** when the FSA was established.



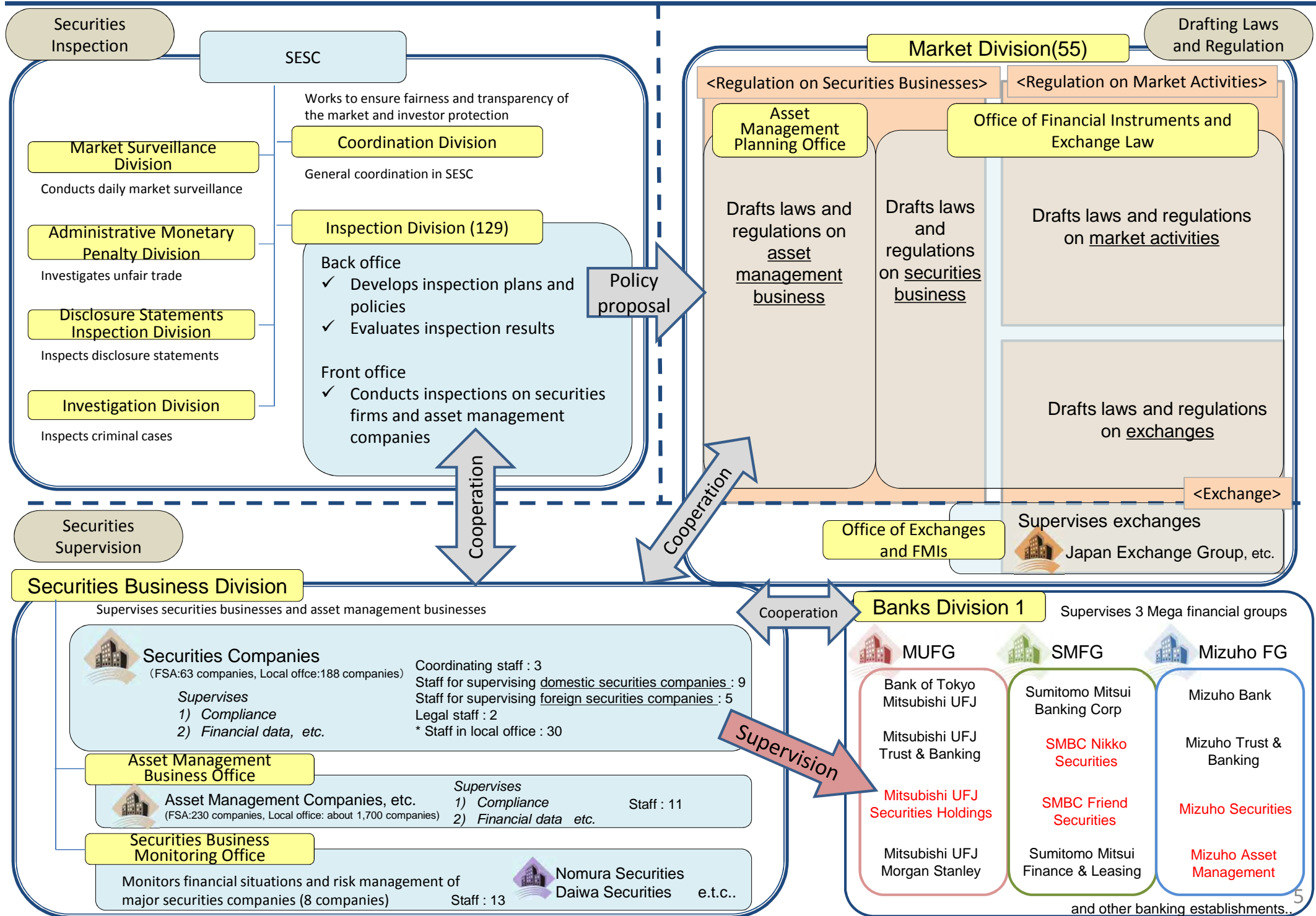
# General Framework of Supervisory Activities

---





# Framework of Regulating & Monitoring Securities Sector



## Human Resources in the FSA

- The FSA is composed of a large variety of staff, including the people directly employed by the FSA (*since 1999*), assigned employees from the Ministry of Finance (MOF) and local government offices, and professionals from the private sector.

Total Staff at the FSA : about 1,600 people	
Employed by FSA (main career track)	about 130
Employed by FSA (general track)	about 270
Employees from MOF (main career track)	about 70
Employees from MOF (general track)	about 40
Employees from local government offices (main career track)	about 40
Employees from local government offices (general track)	about 600
Professionals from the private sector (fixed-term employment)	about 200
Mid-career employees	about 200
Other (temp staff, staff members on tentative leave , etc..)	about 50

### Professionals from the private sector (fixed-term employment)

Attorney	about 30
Certified Public Accountant (CPA)	about 60
Actuary	7
Real-estate appraiser	3
Professional with practical business experience (e.g. financial institutions, IT companies)	about 100

(Ref.) The FSA employees who are on study programs or dispatched to other organizations

Study abroad	Study in Japan	International organization	Japanese embassy	Other Ministries	Local office
about 20	about 10	about 10	about 10	about 20	about 40

## [Reference ] Recruitment/Appointment of National Government Employees

- Basic principles of a fair and equitable government employee system are stipulated under the National Public Service Act.
  - Officials are recruited based on open and equal competitive examinations conducted by the National Personnel Authority (NPA), in principle.

(23 types of examinations including the examination for comprehensive service, examination for general service, the examination for financial specialists and examination for national taxation specialists)
  - Officials are appointed based on their examination results, work performance and any other demonstrated abilities, in principle (merit system).
  - Officials are promoted when they are selected by an appointer based on their work performance.

[Reference] Implementation status of national government employee recruitment examinations in FY2014

	Graduate students/university graduate level		High school graduate level (General track)
	(Main career track)	(General track)	
Number of applicants	23,047	68,712	136,584
Number of first-stage exam passers	3,976	17,355	32,179
Number of final passers	2,080	10,454	18,626

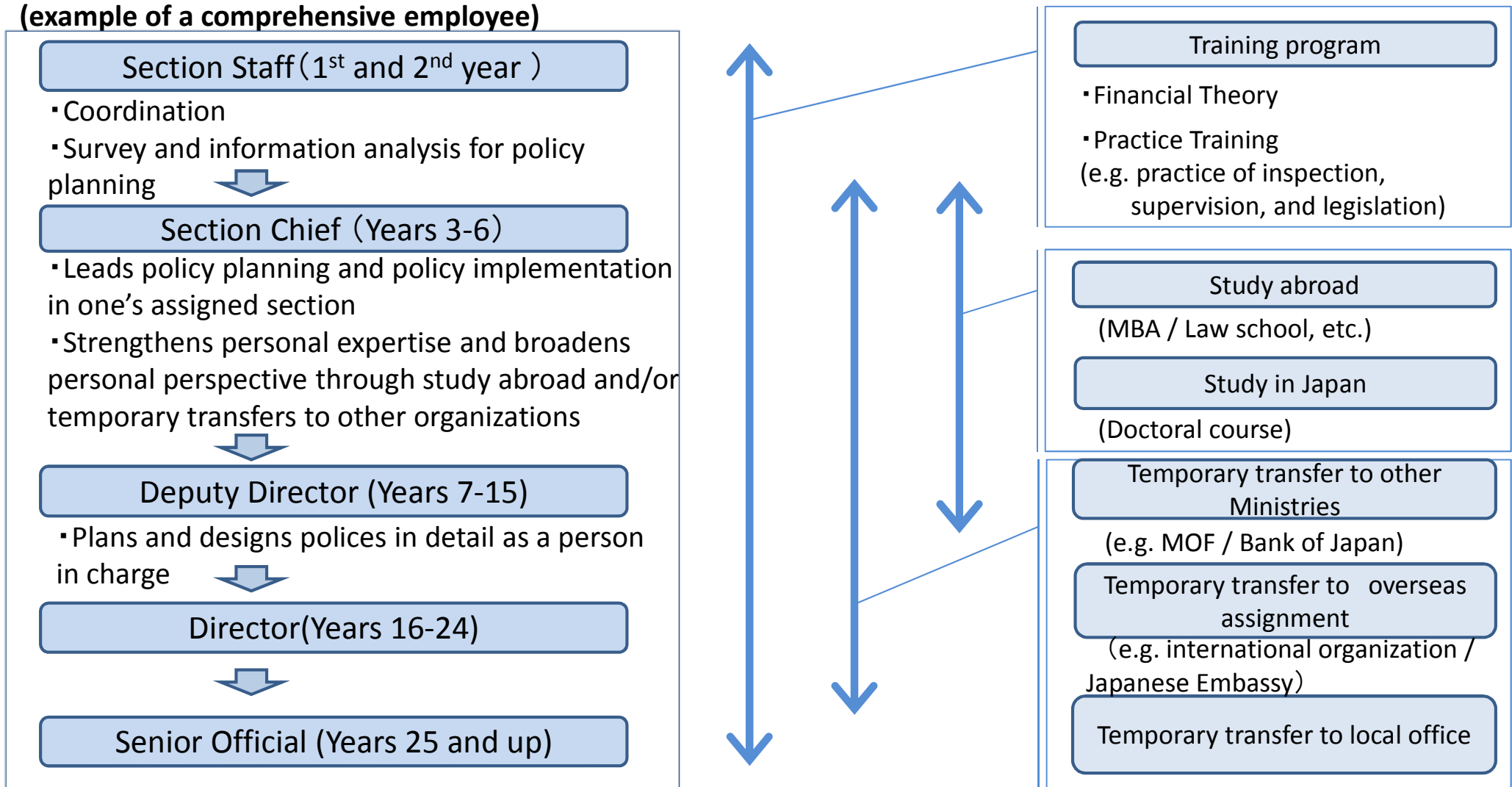
(Extract from NPA data)

# Career Path at the FSA

- FSA employees are due to gather a broad range of experience through study abroad and/or temporary transfers to other Ministries, local organizations and international organizations in their junior careers.
- FSA employees are due to be involved in all of the banking sector, the securities sector, the insurance sector, and general coordination work at the FSA. They can strengthen their expertise in certain areas based on their aptitude.

## Career track of FSA employees

(example of a comprehensive employee)



**The AFPAC was established at the Financial Services Agency in April 2014. Since last summer, it has started to invite officials from Asian financial authorities as Visiting Fellows. It offers training programs tailored to the areas of interest for each Visiting Fellow.**

### **[Main Objectives of AFPAC]**

- To study issues related to financial and capital markets in Asia and to utilize the findings for financial sector development in Asian countries**
- To contribute to the development of business operations by Japanese firms in Asia and by Asian firms in Japan through enhancing cooperative relationships with Asian financial authorities**
- To effectively express a stronger Asian voice in the discussions for global financial regulatory reform**

## The AFPAC Visiting Fellow Program I

---

- Through the Visiting Fellow Program, Visiting Fellows will acquire knowledge, enhance their understanding of, and develop expertise in financial regulation and supervision, with a view to contributing to the development of the financial sectors of their home countries.
- The findings of Visiting Fellows are to be disseminated at seminars/symposiums.
- Through the program, AFPAC aims to build stronger cooperative relationships with other Asian financial authorities.



*At the Opening Ceremony of AFPAC*



# The AFPAC Visiting Fellow Program II

- On 29 July 2014, AFPAC welcomed its first three Visiting Fellows – two officials from the Financial Regulatory Commission of Mongolia and one official from the State Bank of Vietnam.
- During their first month, they attended various lectures led by JFSA staff to study the basics of the Japanese financial system, financial regulation and supervisory practices at the JFSA. They also visited other organizations and institutions, including the Bank of Japan, the Tokyo Stock Exchange, self regulatory organizations, private financial institutions, and research institutes, to attend lectures and exchange views with them on various topics.
- Following those visits, each Visiting Fellow undertook a training program focused on their respective areas of interest at the JFSA and other relevant organizations and could deepen their understanding of specific topics.



*After a lecture on “Lessons from the Banking Crisis in Japan” by Mr. Ryoza Himino, Deputy Director-General of the Supervisory Bureau*



*AFPAC Visiting Fellows at the Tokyo Stock Exchange*



# **“Supervision of Securities Firms in Japan”**

**Kumi INOUE**

**Deputy Director, Securities Business Division**

**27 April 2015**

*\*Any views expressed in this presentation are those of the author, and are not the official views of the JFSA.*



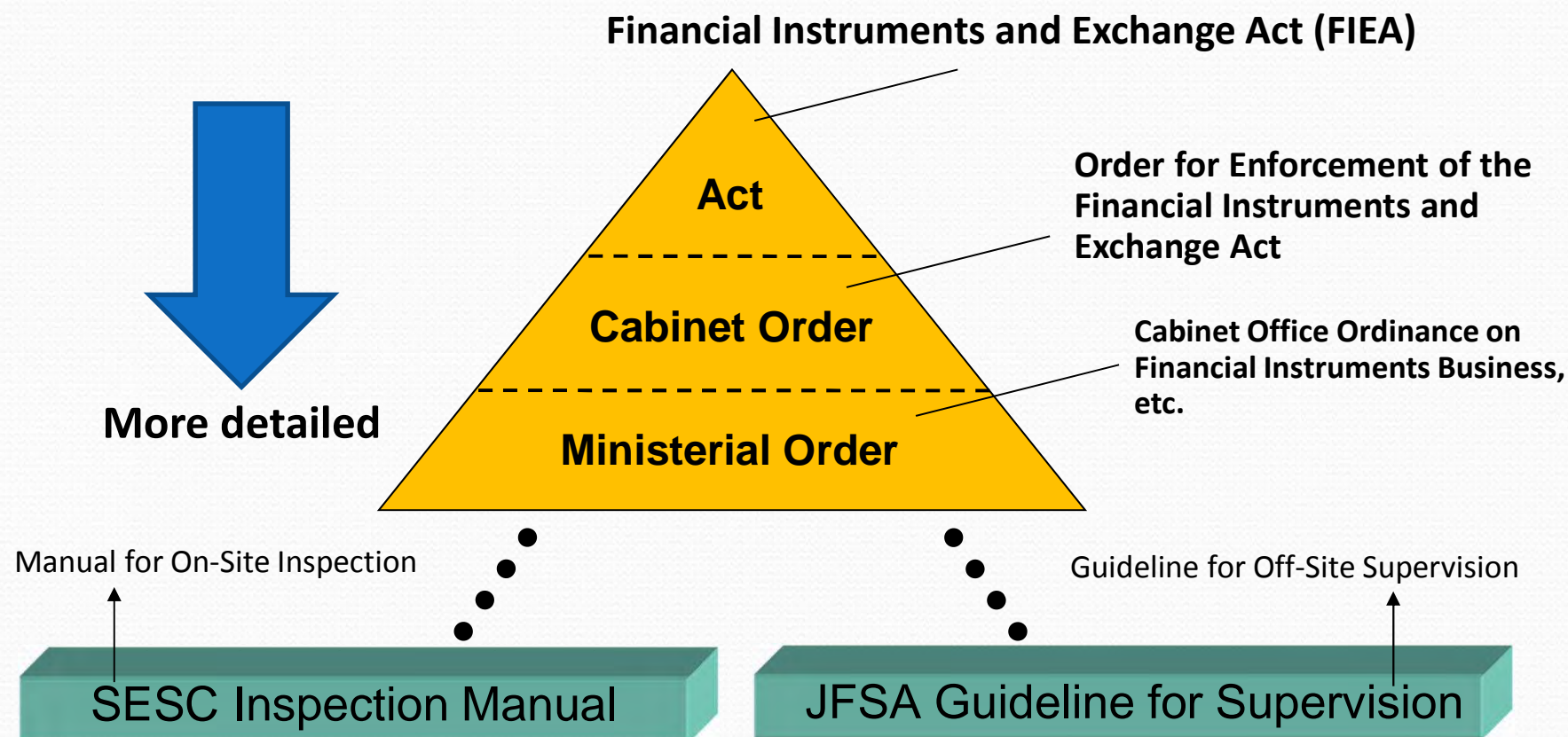


# Contents

- 1. Framework for Supervision of Securities Firms**
- 2. Legal and Supervisory Framework**
- 3. Case Example of Administrative Actions**
- 4. Off-site Monitoring**
- 5. Capital Adequacy Ratio**
- 6. Investor Protection**

# 1. Framework for Supervision of Securities Firms

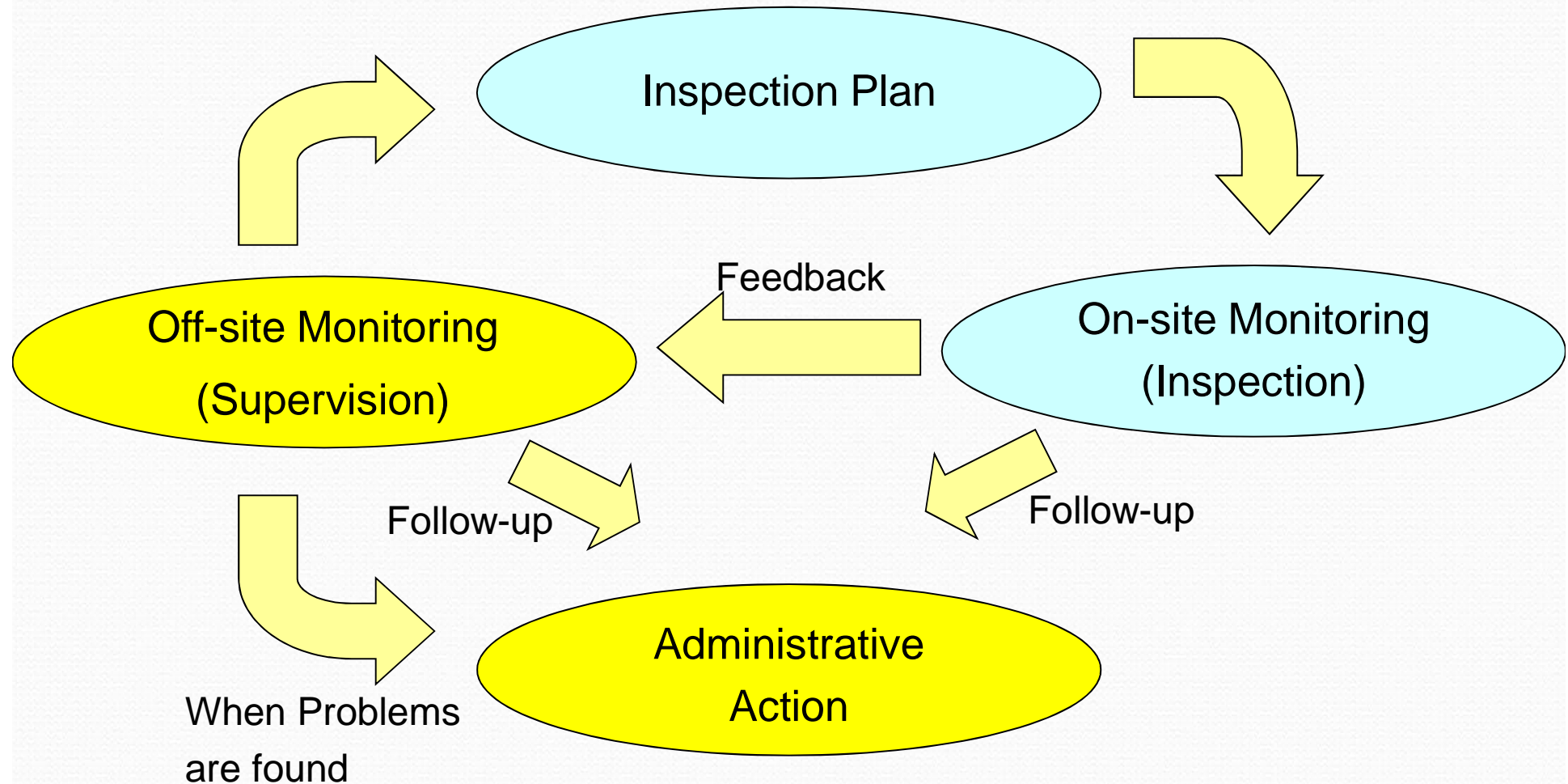
# Framework for Regulations of Securities Firms



- All of the above information is made public for transparency and also available on the JFSA's website ([http://www.fsa.go.jp/en/laws\\_regulations/index.html#02](http://www.fsa.go.jp/en/laws_regulations/index.html#02)).



# General Framework of Supervisory Activities



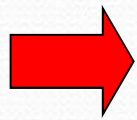
# Functions of On-site and Off-site Monitoring

## On-site Monitoring

- The Inspection Bureau conducts on-site monitoring periodically (as necessary).
  - Verify information obtained through Off-site Monitoring
  - Obtain and evaluate information that is not available through Off-site Monitoring

## Off-site Monitoring

- The Supervisory Bureau conducts off-site monitoring continuously.
  - Collect and analyze information on an ongoing basis even during intervals between one on-site inspection and another
  - Find problems in soundness and appropriateness of operations at an early stage
  - Impose administrative actions as necessary



**Close coordination and communication between the Inspection Bureau and the Supervisory Bureau makes monitoring activities more effective.**

- Risk-focused / forward-looking approach
- Transparency and predictability



# Recent Efforts in On-site and Off-site Monitoring

## Integration of on-site and off-site monitoring

- In September 2014, FSA published the financial monitoring policy for 2014-2015.
- Under the common policy, both the Supervisory Department and the Inspection Department are working together in close cooperation and mitigate the burden on financial institutions.

## 2. Legal and Supervisory Framework

# Securities Firms under the FIEA

- Under the FIEA (Article 29), those who engage in securities activities in Japan are required to register as a Financial Instrument Business Operator (FIBO). There are four main types of FIBOs as follows.

<b>Type I FIBOs</b>  <i>- Most of them are usually called “Securities Firms” -</i>	<ul style="list-style-type: none"><li>Permitted to engage in <b>sales and solicitation of a long list of “highly liquid” securities</b> such as shares, bonds and OTC derivatives trading, clearing, underwriting of securities, public offering of securities, secondary distribution of securities and dealing in public offering securities.</li></ul>
<b>Type II FIBOs</b>	<ul style="list-style-type: none"><li>Only permitted to engage in <b>sales and solicitation in connection with “low liquid” securities</b>.</li></ul>
<b>Investment Management Business</b>	<ul style="list-style-type: none"><li>Permitted to <b>manage Collective Investment Schemes (CIS) and individual portfolio management</b>.</li></ul>
<b>Investment Advisory and Agency Business</b>	<ul style="list-style-type: none"><li>Basically permitted to <b>conduct advisory businesses only</b> and cannot accept deposits or securities from a customer.</li></ul>



# Ref. Number of FIBOs as of the End of Feb 2015

Financial Instrument Business Operators (FIBOs)	2,846
Type I FIBOs	277
Type II FIBOs	1,250
Investment Management Business	328
Investment Advisory and Agency Business	991

- A list of all FIBOs is available on the JFSA's website (<http://www.fsa.go.jp/en/regulated/licensed/index.html>).

# Ref. Number of Staff in Charge of Each Securities Firms

- There are 250 securities firms as of Feb 2015 in Japan, and Financial Services Agency (JFSA) supervises them along with Local Finance Bureaus.

Category	Staff Assignment
<b>1) Major</b> (Daiwa, Nomura)	<b>3</b> staff for <b>2</b> firms
<b>2) Semi-major</b> (Mitsubishi, Mizuho, SMBC Nikko, etc.)	<b>3</b> staff for <b>13</b> firms
<b>3) Local and small</b> (Ichiyoshi, etc.)	<b>3</b> staff (+ <b>30</b> staff in Local Finance Bureaus) for <b>180</b> firms
<b>4) Foreign</b> (Goldman Sachs, JP Morgan, Deutsche, etc.)	<b>5</b> staff for <b>32</b> firms
<b>5) Internet</b> (Monex, Rakuten, etc.)	<b>3</b> staff for <b>14</b> firms

- Also, the JFSA has a professional team dedicated to the risk management for 4 major securities firms (Nomura Holdings, Daiwa Group, Mitsubishi UFJ Morgan Stanley Securities (MUMSS), Mizuho Securities) and 4 major foreign securities firms (Goldman Sachs, Morgan Stanley, JP Morgan, Deutsche Securities). This team is called the Securities Monitoring Office and consists of 13 staff.



# Ref. UKFCA Firm Classification

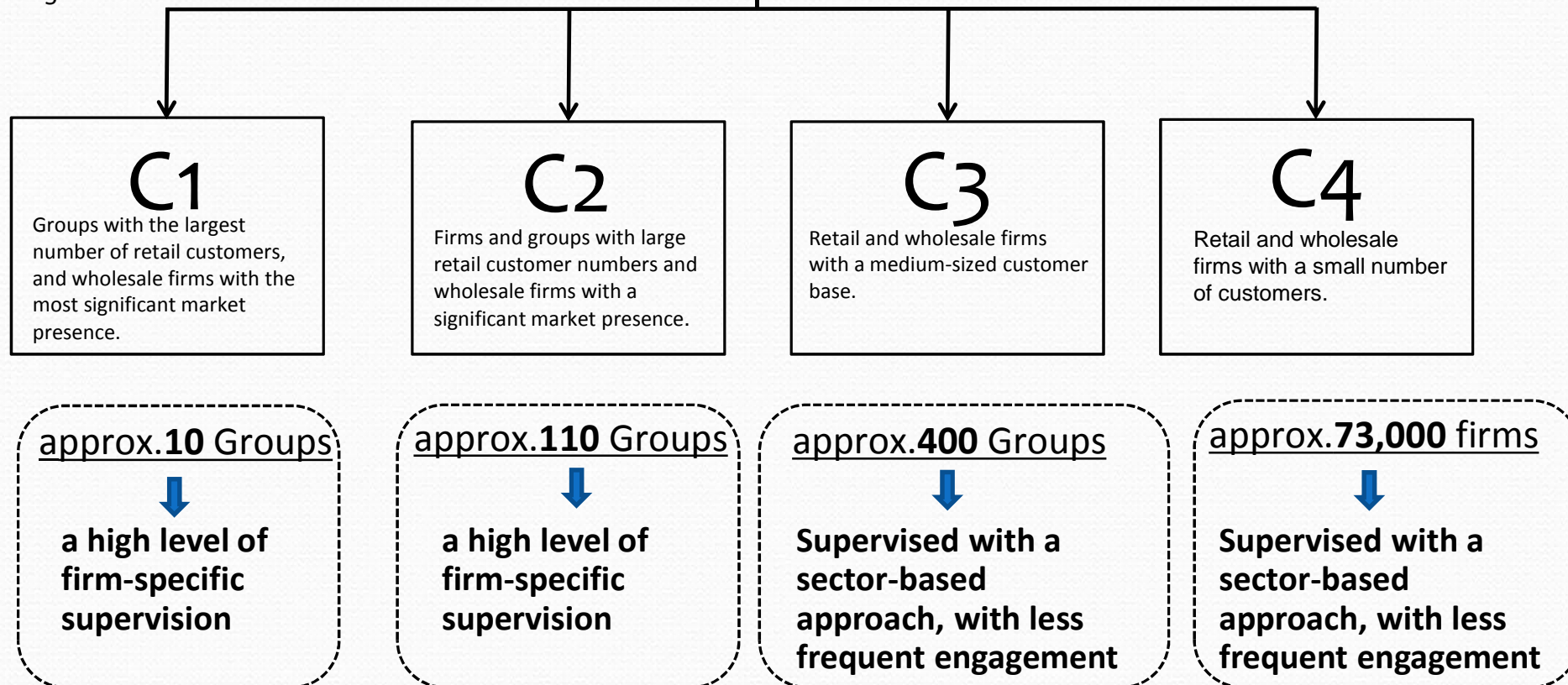
## Conduct categories

- Reflect a firm's size and retail customer numbers or wholesale presence, and the corresponding level of risk the firm potentially poses.
- Each category is subject to a different level of supervision, allowing UKFCA to use their resources as efficiently as possible and concentrate on the areas that pose the greatest risks.



## UKFCA's approach

- *Seven forward-looking areas of focus*
- *Five key priorities*



# Registration Requirements for Securities Firms

- Minimum entry requirements are established in the FIEA for each category of FIBO.
- Grounds for “refusal of registration” are also established. (FIEA Article 29-4)
- The system of registration replaced the licensing system in 1998. This change was one of the measures taken in the Financial System Reform in 1996.



# Minimum Entry Requirements for Securities Firms

- The minimum entry requirements in the FIEA for securities firms (Type I FIBOs) are mainly as follows.
  - ✓ Minimum capital requirements (Type I FIBOs are required to have no less than ¥ 50 million for capital and net assets (roughly US \$ 5 billion))
  - ✓ The applicant's directors and officers are checked to ensure they have no recent criminal record or links to organized crime
  - ✓ Submission of reports setting out business operations including risk management, internal control, details of shareholders and human resources structure
  - ✓ Adequate internal controls and risk management systems (Article 29-4 (1) of the FIEA, IV-3-1 of the Supervisory Guidelines)
  - ✓ Establishment of a compliance unit (Article 29-4 (1) of the FIEA, IV-3-1 of the Supervisory Guidelines)

# Registration Process(1)

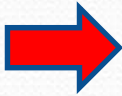
- Applications for registration for FIBOs are handled by the Local Finance Bureau.
- The applicant and its staff are required to show up and answer questions at the Local Finance Bureau as a part of the vetting process as needed.
- Processing the application may take several months.



## Registration Process(2)

- The application will be reviewed by focusing on whether it can contribute to the smooth circulation of securities, protecting the investors at the same time, which are the qualifications expected as market intermediaries.
- We will check whether the applicant is clearly understanding its business plan, whether the personnel, system, rules to conduct that business appropriately are prepared, whether the management has good governance such as sense of compliance and internal control, through sufficient discussion with the applicant.

## Registration Process(3)

- e.g. Review whether the applicant has adequate staffing to conduct financial instruments business appropriately.
  - ✓ Knowledge and experience of the top management
  - ✓ Knowledge and experience of the managing directors
  - ✓ Knowledge and experience regarding compliance, etc.
  - ✓ Conducting business
  - ✓ Function of the internal checking
-  ***Secure the companies' understanding of legal obligation and regulation through full communication prior to registration.***
- For your information, when a registered operator has not resumed its business within 3 months since the day of registration or has continued to suspend its business for 3 months or more without any justifiable grounds, the JFSA may rescind registration of that operator.



# Major Rules of Conduct for Securities Firms under the FIEA (1)

- **Suitability requirement**

- FIBOs must not engage in inappropriate solicitation that may result in insufficient investor protection in light of customer knowledge, experience and assets as well as the purpose of concluding a contract. (Article 40(i))
- FIBOs are required to ensure appropriate handling of customer information obtained in the course of the business. (Article 40(ii))

- **Prohibition of loss compensation (Article 39)**

- **Information to be given to clients**

- Before entering into a transaction, a FIBO is required to provide a document to customers that outlines the contract and discloses fees and consideration payable by the customer. (Article 37-3)
- After a transaction is effected, a FIBO is required to provide a confirmation which sets out the contract date and names of the parties and other relevant particulars. (Article 37-4)
- A FIBO must provide clients with a statement of “outstanding balance of transactions” at least once a year. (Article 37-4 and Cabinet Office Ordinance Article 98)

# Major Rules of Conduct for Securities Firms under the FIEA (2)

- **Duty of Best Execution (Article 40-2)**
- **Duty of Record Keeping (Article 46-2)**
  - A FIBO is required to prepare and preserve the books and documents on its transactions with its clients in order to enable confirmation of inflows and outflows of accounts under article 164 and 157 of Cabinet Office Ordinance:
    - a. Client account books which record inflows, outflows and net balances
    - b. Safe custody securities statements which record reasons for withdrawals of deposited securities received.
  - Such information must be preserved for a period of five to ten years.
- **Management of Conflicts of Interest**
  - All FIBOs and their directors and employees are required to execute business in good faith and fairly to customers. (Article 36)
  - Conflicts of interest must be prevented and appropriate management structures to identify and address them must be developed. (Article 36 and 44)



# **Supervisory Evaluation Points**

- **Governance**
- **Soundness of Financial Condition**
- **Appropriateness of Business Operations**
  - **Legal Compliance**
  - **Management of Sales Staff**
  - **Management of Customer Information**
  - **Risk Management (Liquidity, Market, Credit, Operational)**
  - **Computer System Management**
  - **Business Continuity Management**
  - **Internal Audit, etc.**

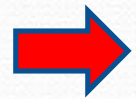
# Ref. Supervisory Viewpoints for Foreign Securities Firms(1)

- Entry of foreign securities firms has benefits such as vitalizing the domestic market and enhancing the convenience of the customers by the advanced financial products and services offered by the foreign financial groups and by the global network. On the other hand, there are special viewpoints, such as the conformity to the domestic regulation and the business customs, and the JFSA needs to cooperate with the foreign management and the foreign authorities.
- The JFSA is striving to identify the supervisory issues and to share the understanding of those issues by communicating with the headquarter in Japan and the headquarter of the group, etc. among (1) business management, (2) appropriateness of business conduct, (3) appropriateness and sufficiency of capital (4) risk management, etc. also taking the characteristics of the headquarter in Japan into consideration.
- Also, the JFSA is striving to enhance the effectiveness of supervision on the identified issues concerning the head quarter in Japan and the head quarter of the group by close cooperation and information sharing with the home supervisory authority.



## Ref. Supervisory Viewpoints for Foreign Securities Firms(2)

- Examples of issues regarding foreign securities firms
  - ✓ Local governance and internal control are not sufficient.
  - ✓ Personnel familiar with the domestic conditions and resource not enough due to the outsourcing of operational risk management, etc. to other group headquarters.
  - ✓ The system is not appropriately adjusted to the domestic regulation because it is developed and managed globally.



The JFSA sends out questionnaires to foreign securities companies annually in order to obtain more information regarding their risk profile and risk management, etc.

# The JFSA's Powers over Securities Firms (1)

- FIEA Article 56-2 provides the JFSA with broad supervisory power over FIBOs. In particular, JFSA has the power to:
  - **Request reports and information** (materials) from any FIBO, as well as from the **holding company** of the FIBO for the purpose of understanding the status of business or property of the firm.
  - **Inspect** the status of business or property of a FIBO, or its books and documents and other articles.
  - Order a **major shareholder** of a FIBO to submit reports or materials, notifications under Article 32, or have the officials inspect documents or other articles of the major shareholder.
  - Order a **parent financial institution** or a **subsidiary FI** of a FIBO to submit reports or materials and have the officials of the JFSA inspect their status of business or property, or books and records.



# The JFSA's Powers over Securities Firms (2)

- JFSA has the following enforcement powers:
  - Issue orders of improvement of business (Article 51). These orders can include
    - ▣ requiring immediate remedy of particular business conduct
    - ▣ demanding investigations of management responsibilities
    - ▣ ordering to establish preventive measures
    - ▣ amending business operations.
  - Issue suspension orders for a period not exceeding six months or rescind the registration. (Article 52).
- When those measures above are conducted, it is disclosed to the public.

# Verification for Administrative Actions(1)

(A-1) Seriousness		Assessment	Remarks
Degree of Damage to Public Interests	Whether the Financial Instruments Business Operator, etc., is undermining public interests significantly by, for example, originating and providing products markedly inappropriate from the viewpoint of appropriate disclosure of financial conditions to customers, thereby damaging confidence in the financial markets.		
Extent of Damage to Users	Whether a number of users across wide regions have suffered damage.		
	How serious the damage done to individual users is.		
(A-2) Maliciousness			
Maliciousness of Acts	Whether the Financial Instruments Business Operator, etc., has acted in a malicious way, such as by continuing to sell similar products despite receiving numerous complaints from users.		
Duration and Repetitive Nature of Acts	Whether the act in question committed by a Financial Instruments Business Operator, etc., has been committed for a long period of time. Whether the act has been committed repeatedly and continuously or only once. Whether the Financial Instruments Business Operator, etc., committed a similar illegal act in the past.		
Intentionality	Whether the Financial Instruments Business Operator, etc., has committed the illegal/inappropriate act intentionally while recognizing the illegality and inappropriateness, or has done so through negligence.		
Institutional Involvement	Whether the act has been committed based on an individual employee's judgment or a manager has been involved. Whether the management team has been involved.		
Presence or Absence of Cover-Up Actions	Whether an attempt to cover up the act has been made after its illegality was recognized. Whether a cover-up, if one exists, was an institutional act.		
Involvement of Anti-Social Forces	Whether any anti-social forces have been involved. How much involvement, if any.		



# Verification for Administrative Actions(2)

<b>(B) Appropriateness of Control Environment for Governance and Business Operation</b>		<b>Assessment</b>	<b>Remarks</b>
<b>Representative Director and Board of Directors</b>	Whether the representative director and the board of directors are fully aware of the importance of legal compliance and make sufficient efforts to ensure compliance.		
<b>Internal Audit Section</b>	Whether the internal audit section is adequately staffed and equipped to conduct audits and whether the division is functioning properly.		
<b>Compliance and Risk Management Divisions</b>	Whether the compliance and risk management divisions are adequately staffed and equipped to perform their tasks and whether they are functioning properly.		
<b>Employees Engaging in Business</b>	Whether employees engaging in business are fully aware of the importance of legal compliance and whether sufficient internal training is provided.		
<b>(C) Attenuation Factors</b>			
<b>Voluntary Efforts</b>	Whether there are attenuation factors, such as the implementation of voluntary efforts by the Financial Instruments Business Operator, etc., to protect investors before the administrative response.		
<b>Others</b>	Whether there are any other attenuation factors.		
<b>(D) Other factors</b>	Whether there are any other factors to be considered.		

- The JFSA compare some relevant cases in one chart and decide what sanction should be appropriate.

# 3. Case Example of Administrative Actions

# Case Example of Administrative Actions on Violations of Short-Selling Regulation

**Confidential**

Securities Firms	Administrative action	Number of disclosing violation	Number of pricing violation	Reasons	Elements to consider in administrative action
		(duration of violation)			
A	order for business improvement & business-suspension (5 business days)	4,613 (510/month)	293 (32/month)	▪ flaw in the ordering system, while front staff recognize it ▪ insufficient engagement of compliance and IT department	- voluntary surrender - marked shortage of the knowledge about legal matters
		9 months			
B	order for business improvement & business-suspension (10 business days)	1,200,000 (60,000/month)	128 (7 /month)	▪ flaw in the ordering system ▪ insufficient prior confirmation and periodic checkup	- voluntary surrender - prior record of violating the same regulation - extremely insufficient system management structure
		18 months			
C	Order to submit reports	1,106 (23/month)	—	▪ solely relied on pre-approval of its regional compliance department ▪ insufficient ex-post monitoring	- Voluntary surrender - Voluntarily work out measures for preventing a recurrence of this legal violation
		4 years			
D	Order to submit reports	8,517 (2,100/month)	—	▪ a flaw in the system concerning cross-border transaction ▪ insufficient ex-post monitoring	- Voluntary surrender - Voluntarily work out measures for preventing a recurrence of this legal violation
		4 months			
E	Order to submit reports	33,087 (7,000/month)	196 (23/month)	▪ change the ordering system without pre-approval, wrongly ▪ insufficient ex-post monitoring	- Voluntary surrender - Voluntarily work out measures for preventing a recurrence of this legal violation
		5 months			



# Business Improvement Order against Barclays Securities Japan Limited

- On September 30, 2011, the JFSA took an administrative action against Barclays Securities Japan Limited due to “Short-Selling in breach of the FIEA” and “Inadequate management of the electronic data processing systems for the financial instruments business”.
- In addition to the business suspension order, the following business improvement orders were issued.
  - a. Clarifying the responsibility of the management and staff regarding the above-mentioned violations.
  - b. Securing strict compliance by all the directors and staff and taking preventive measures against recurrence of the above- mentioned violations.
  - c. Strengthening the internal control system, including the management of the electronic data processing systems.
  - d. Submitting a written report to the JFSA on the implementation of the above measures (a - c) by October 21, 2011, and b and c by January 4, 2012, every 3 months thereafter, and at any times as needed in consideration of the implementation status.

# 4. Off-site Monitoring

# Information and Data Collected from Securities Firms(1)

- Under the law, the securities firms are obliged to submit the Business Report (annually, article 46-3 (1)), the Report on relevant companies and the Report on International Business (annually, article 46-3 (2) and article 173 of the cabinet ordinance), the capital adequacy ratio (monthly, article 46-6).
- Additionally, though not stipulated in law, the JFSA has ordered all the securities firms to report major accounts (financial data), status of asset segregation, status of capital and risk, and financial status, etc. monthly or semi-annually. *(see the next page for details)*



# Information and Data Collected from Securities Firms(2)

Data	submission	reference date
★ Capital Adequacy Ratio	monthly	End of each month
Major Account Balance	monthly	End of each month
State of Business	monthly	End of each month
State of Operating Proprietary Trading System	monthly	End of each month
State of Operating Foreign Exchange Margin Transactions	monthly	End of each month
★ State of Segregation of Client Funds	monthly	Every Friday (every business day)
★ State of Segregation of Client Securities	quarterly	End of each quarter
State of claims subject to compensation	annually	End of each year
State of Segregation of Funds for Clearing Margins	monthly quarterly monthly	End of each month End of each quarter Every Friday (every business day)
Market Risk	monthly	every business day
List of Top Large Positions	monthly	End of each month
Balance on Securities	semi-annually	End of each half year
Profit and Loss on Securities	semi-annually	End of each half year
Market Fluctuation Effect	monthly	End of each month
Counterparty Risk	monthly	End of each month
Data on Loss by Operational Risk	quarterly	End of each quarter
Data on Sources and Uses of Cash	monthly	every business day
Data on Sufficient Liquidity	monthly	End of each month
State of Financing Method	monthly	End of each month

# Utilizing Collected Information and Data in Supervision

- Information reported by securities firms is utilized in daily supervision for checking their business and conditions. It is also utilized as basic information for inspection and as reference materials for amending regulations by sharing with the inspection section and rule-planning section.
- Especially, for data reported monthly, one staff member exclusively conducts analysis and verification utilizing interviews if necessary, and the analysis is provided to relative staff in the supervisory section and the inspection section and used for daily supervision and inspection.



# 5. Capital Adequacy Ratio

# Overview of Capital Adequacy Framework for Securities Firms

## (1) Background / Objectives

- First introduced in the 1990's in view of maintaining financial soundness of securities firms and ensuring investor protection.
- Through efforts to maintain an adequate level of capital adequacy ratio, FIBOs must identify and manage risks involved in their businesses in a comprehensive manner and keep liquid assets (non-fixed capital) in sufficient quantity and quality, to enable them to withstand losses that may be caused by the materialization of various risks.

## (2) Supervisory framework based on Capital Adequacy Ratio

Capital Adequacy Ratio	Early Remedial Measures
$\frac{\text{Non-fixed Capital}}{(a) \text{ Market Risk} + (b) \text{ Counterparty Risk} + (c) \text{ Basic Risk}}$	<p>&lt; 140%</p> <p>Required to notify JFSA</p>
<p>[Note1]</p> <p>(a) The risk of a FIBO incurring losses due to fluctuations in prices of its asset holdings (including positions related to off-balance transactions) caused by changes in various market-related risk factors, such as prices of securities and other financial instruments, interest rates and exchange rates, as well as credit and other risks associated therewith</p> <p>(b) The risk of a FIBO incurring losses due to a failure by the counterparties to its transactions to fulfill their contractual obligations</p> <p>(c) The risk of a FIBO regarding operating expenses and operational error which should be noted in the business as usual</p>	<p>&lt; 120%</p> <p>Ordered to improve business</p>
<p>[Note2] Actual figures of Capital Adequacy Ratio (as of Feb 2015)</p> <p>Nomura: 283.7% / Daiwa: 317.8% / Mitsubishi UFJ Morgan Stanley: 293.6% / Mizuho: 333.4%</p>	<p>&lt; 100%</p> <p>Ordered to suspend business for a period</p>

# An Image of Non-fixed Capital

Assets	Liabilities
Current Assets	Liabilities
<div>Non-fixed Capital = Current Assets – Liabilities = Capital – Fixed Assets</div>	Capital (Equity)
Fixed Assets	



# Early Remedial Measures Based on Capital Adequacy

Capital Adequacy Ratio	Early Remedial Measures
$\frac{\text{Non-fixed Primary Capital}}{\text{The amount of various risks}} \times 100$	<p>&lt; 140(%)...Required to notify JFSA</p> <p>&lt; 120(%)...Ordered to improve businesses</p> <p>&lt; 100(%)...Ordered to suspend businesses for a period</p>

- The ratio is derived from a formula where the numerator is calculated by deducting the amount of illiquid assets such as unlisted securities, loans and real estate from capital and where the denominator is the equivalent of credit risk, market risk and operational risk.
- The JFSA will take “Early Remedial Measures” against Type I FIBOs based on their Capital Adequacy Ratios.
- If the ratio of a Type I FIBO goes below pre-set thresholds, a corrective order will be issued (e.g. Business Improvement Order, Business Suspension Order).
- On an ongoing basis, Type I FIBOs must maintain a capital ratio formula with monthly/quarterly/annual reporting to the JFSA.

# Early Warning System

- Even if a securities firm does not fail to keep the capital adequacy ratio more than 140 percent, it may still need to improve its soundness and management continuously. Thus, the JFSA has the early warning system, in which the JFSA analyzes information and data, categorize the companies, focus on some relatively fragile ones, and conduct a dialog with them or order them to improve their soundness and management.

(as of Feb 2015)

	Promote Improvement				Focus on Improvement			Total
	Decrease by more than 100%	Decrease for 2 consecutive months + Not exceed 200%	Impact of Change in Prices of Securities and Interest Rates	Impact of Change in Foreign Exchange	Decrease by more than 200%	Decrease for 3 consecutive months + Not exceed 200%	Impact of Change in Foreign Exchange	
A	8	0	0	1	1	0	1	11
B	1	0	0	0	0	0	0	1
C	0	0	0	0	0	4	1	5
D	0	0	0	0	0	0	0	0
Total	9	0	0	1	1	4	2	17

- ✧ A: Temporary factors or CAR remains at a high level.
- ✧ B: Remedial measures such as capital increase are planned.
- ✧ C: Remedial measures are not planned. Continued attention is necessary.
- ✧ D: During a follow-up by an order for submission of reports



# Ref. Stress Scenarios and Recovery Actions

## ● Examples of stress scenarios

- ✓ Severe Losses through a Rogue Trader
- ✓ Rating Downgrades
- ✓ Collapse of Global Financial Markets
- ✓ Fraud, etc.

\* Refer to “Guidance on Recovery Triggers and Stress Scenarios” published by FSB on 16 July 2013 for details.

## ● Recovery Options

- ✓ Liquidity (Raise Immediate Short Term Funding, Debt Financing, Unwind of Liquidity Portfolio, etc.)
- ✓ Capital/RWA (Capital Planning, Cost Reduction, Asset Disposal, Business Disposal, etc.)

# 6. Investor Protection

- Segregation Requirement
- Investor Protection Fund

# Segregation of Client Assets(1)

- FIBOs are required to segregate clients assets from their own properties. (Article 43-2)
- Clients money or securities must be deposited with a trust company licensed in Japan. (Article 43-2)
- Type I FIBOs are required to have an audit on clients assets by a CPA or audit firm at least once a year. (Article 43-2, Cabinet Office Ordinance Article 142)
- Written consent from a client is required for a securities firm to use the securities posted by the client. (Article 43-4)



## Segregation of Client Assets(2)

- In Japan, the way of asset segregation is different between securities and cash.
- For listed stocks, most are managed by JASDEC (Japan Securities Depository Center, inc.), which is a securities depository.
- Regarding cash, some are cash for purchasing stock, etc. There are also sales proceeds and redemption that are deposited temporarily. Cash that should be returned to the clients are entrusted to trust banks as “Customer discretionary trust”.
- Such status of asset segregation is inspected by the JFSA and JSDA (Japan Securities Dealers Association).

# Investor Protection Fund

- Type I FIBOs are required to join an investor protection fund established in 1998 (Article 79-20) and to contribute to it.
- In the event of the insolvency of a FIBO, segregated clients assets are expected to be returned to the clients promptly or transferred to another FIBO. Based on Article 51 of FIEA, the JFSA can issue an administrative order for those purposes.
- The maximum reimbursement amount by the fund in the event of bankruptcy of a firm is not more than ¥10 million per investor.
- The fund does not compensate for loss to clients owing to a decline of the securities holding prices.



**Thank you**

# An overview of Securities Inspection

28 April, 2015

Kaoru Murakami  
Deputy Director for Inspection Division  
Securities and Exchange Surveillance Commission

# Contents

1. SESC's Mission
2. SESC's Organization
3. Outline of Activities
4. Legal Framework
5. Securities Inspection
6. Collection and Analysis of Information
7. Recent Cases

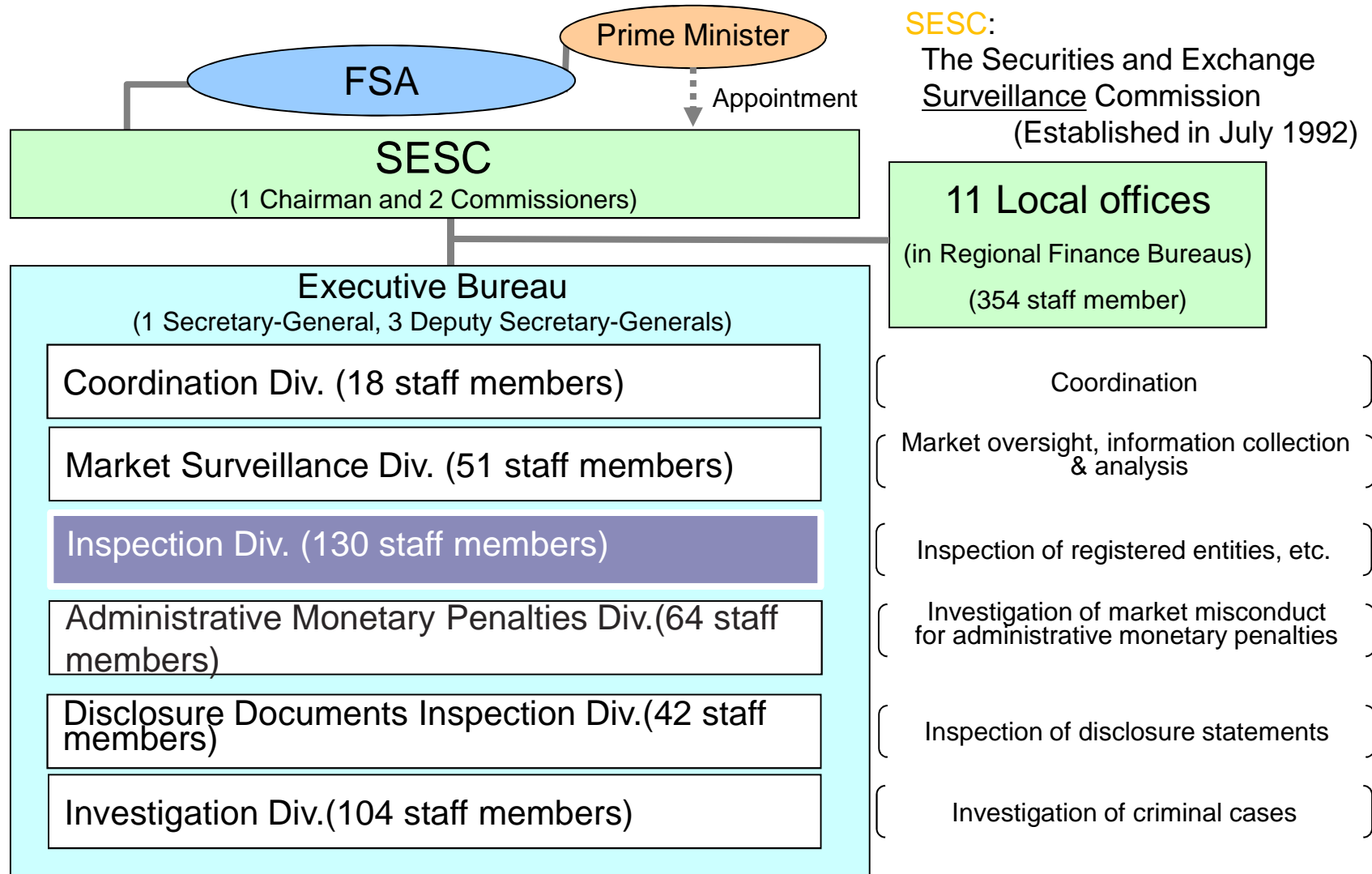


## 1. SESC's Mission

- To ensure the integrity of the Japanese capital market
- To protect investors

"To be feared by wrongdoers and  
trusted by ordinary investors"

## 2. SESC's Organization(1)



Note : Staff members of Executive Bureau are quota as at the end of FY2014.

## 2. SESC's Organization(2)

- The SESC (chairman and commissioners) executes its official authority independently, though it is within the Financial Services Agency (FSA).  
(Chairman and commissioners will not be dismissed against their will.)
- The SESC doesn't have the power to make rules or to take administrative actions. Instead, it can submit policy proposals or make recommendations to take administrative actions.

## 2. SESC's Organization(3)

### USA

	Securities transactions, etc.
Rulemaking	SEC
Supervision (Administrative action)	
Inspection Surveillance	

### Japan

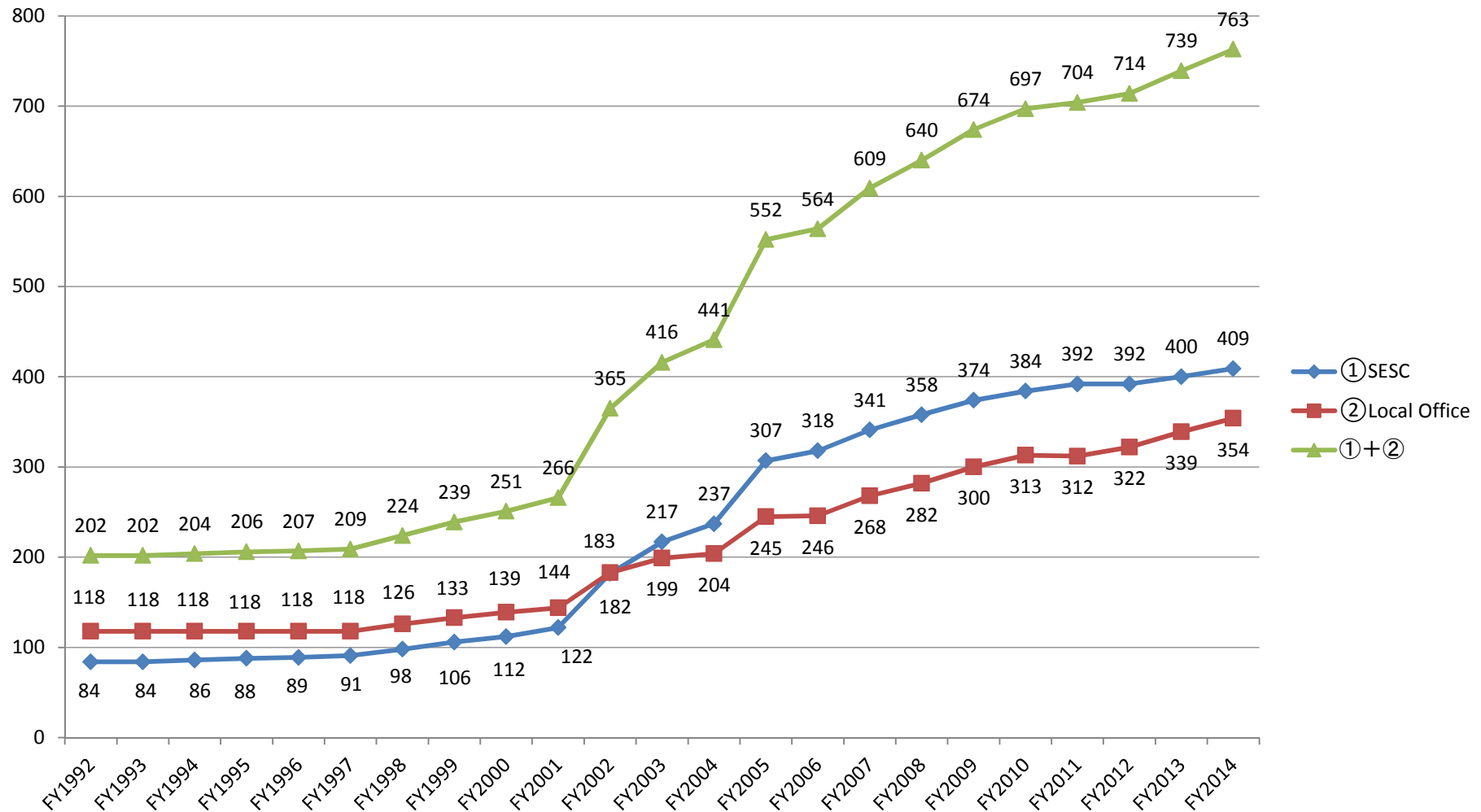
	Securities transactions, etc.
Rulemaking	FSA
Supervision (Administrative Action)	FSA
Inspection Surveillance	SESC (in FSA) independently executes its authority

Policy proposals

Recommendation for administrative actions

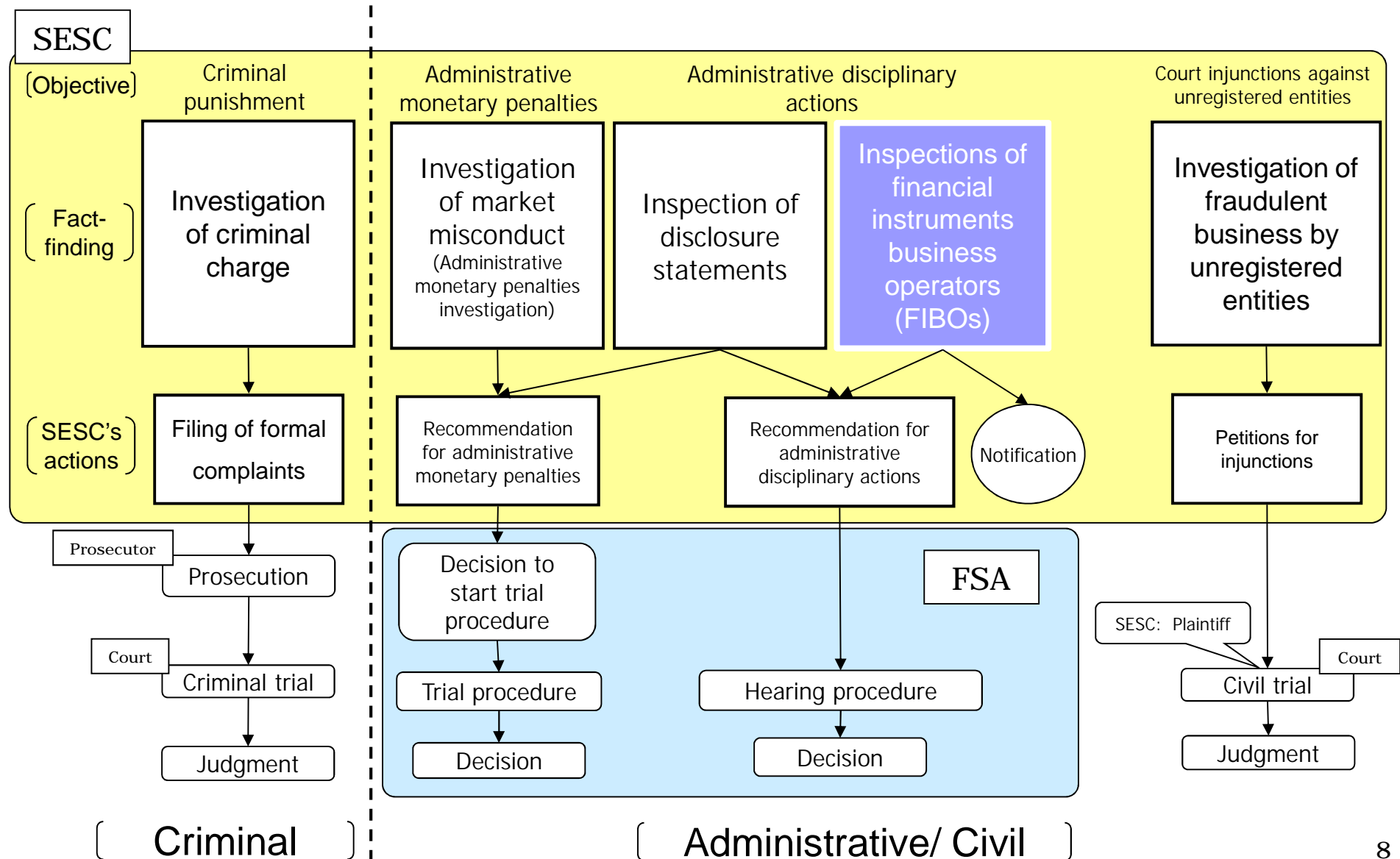
## 2. SESC's Organization(4)

### Changes in Number of SESC Staff Members

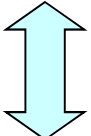




### 3. Outline of Activities (1)



### 3. Outline of Activities (2)

Activity type	Typical "target"	Possible result	Purpose	Characteristics
Inspection for <u>administrative disciplinary actions</u>	Registered entities (e.g. FIBOs)	<ul style="list-style-type: none"> <li>• Revocation of Registration</li> <li>• Business suspension order</li> <li>• Improvement order</li> </ul>	<u>Improvement</u> of business operations	<ul style="list-style-type: none"> <li>• Based on <u>dialogue</u> (but not always)</li> <li>• No coercive measure</li> </ul>
Investigation for <u>administrative monetary penalties</u>	Listed companies that made false statements	Monetary penalties	<u>Deterrence</u> of market misconducts to ensure the effectiveness of regulations	<ul style="list-style-type: none"> <li>• Less severe penalty</li> <li>• No coercive measure</li> <li>• Lighter burden of proof</li> </ul> 
	Insider traders, market manipulators			
Investigation for <u>criminal charge</u>	Offenders of certain statutory provisions (including above)	Imprisonment and/or fine	<u>Imposition of criminal sanctions</u>	<ul style="list-style-type: none"> <li>• More severe penalty</li> <li>• Coercive measure (search &amp; seizure with warrant)</li> <li>• Heavier burden of proof</li> </ul>

### 3. Outline of Activities (3)

## Supervisory powers over Securities Companies

#### 1. **Submission of Reports and On-site inspection**

- ✓ ordering any securities company to submit reports and information from
- ✓ inspecting the status of business or property of a securities company or its books and documents and other articles

#### 2. **Business Improvement Order**

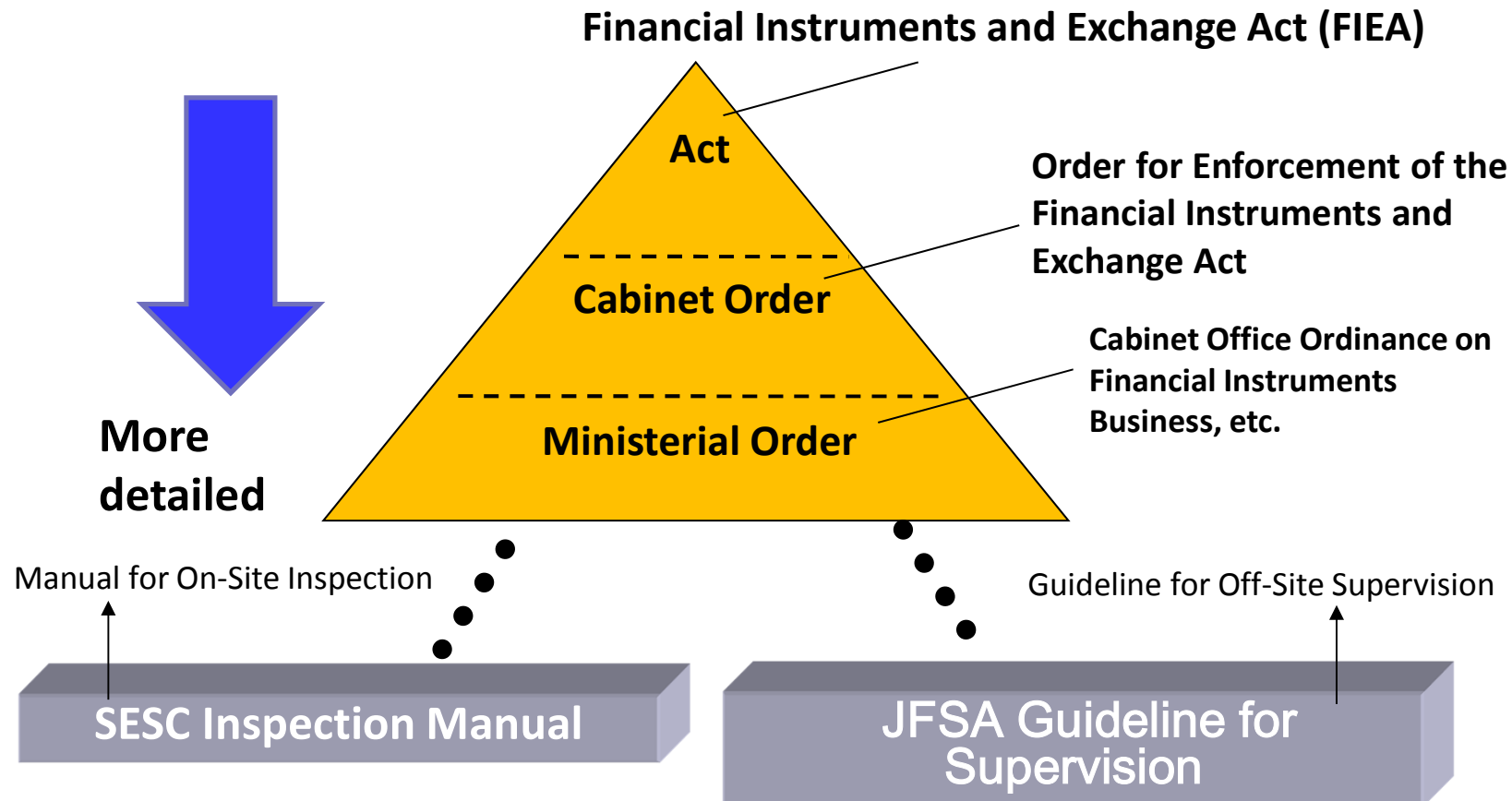
- ✓ requiring immediate remedy of a particular business conduct
- ✓ demanding investigations of management responsibilities
- ✓ ordering the establishment of preventive measures
- ✓ amending business operations.

#### 3. **Business Suspension Order**

- ✓ period not exceeding six months

#### 4. **Registration Revocation Order**

## 4. Legal Framework(1)



All of the above information is made public for transparency and also available on the JFSA's website

[http://www.fsa.go.jp/en/laws\\_regulations/index.html#02](http://www.fsa.go.jp/en/laws_regulations/index.html#02)

<http://www.fsa.go.jp/sesc/english/guideline/index.htm>

## 4. Legal Framework(2)



### Inspection Manual

(a tool to enable an inspector to make verification)

- Inspection Manual is not “regulations” or “instructions”.
- Inspection items are Examples of items considered effective for comprehending the actual conditions of business operators.
- It is necessary to take care so as not to merely verify each item of the Inspection Manual automatically and uniformly.



## 5. Securities Inspection (1)

### -Objectives

- To encourage the improvement of internal control systems in the Financial Instruments Business Operators (FIBOs)
- To ensure the appropriateness of risk management systems including financial soundness in the FIBOs
- To enhance awareness of the FIBOs as gatekeepers

## 5. Securities Inspection (2)

### -Changes in Circumstances

#### Diversification and increase in the number of FIBOs

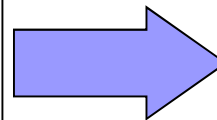
- Around 8,000 operators engage in business
- Actions have to be taken against unregistered business operators
- Financial instruments and transactions have become more diverse and complex

## 5. Securities Inspection (3)

### -Number of entities to be inspected

#### SESC's establishment

- Domestic Securities Companies  
216 (Dec.1992)
- Foreign Securities Companies  
49 (Jun. 1992)
- Financial Futures Dealers  
216 (May. 1993)
- Registered Financial Institutions  
619 (Jul. 1993)



#### Feb 2015

- |   |       |
|---|-------|
| 1. Type I FIBOs   | 277   |
| 2. Type II FIBOs  | 1,250 |
| 3. Investment Advisories/Agencies   | 991   |
| 4. Asset Management Firms   | 328   |
| 5. Registered Financial Institutions  | 1,097 |
| 6. Specially Permitted Business Notifying Firms for Qualified Institutional Investors | 2,884 |
| 7. Financial Instruments Intermediaries   | 818   |
| 8. Self-Regulatory Organization   | 13    |
| 9. Investment Corporation   | 68    |
| 10. Credit Ratings Agencies   | 7     |
| (+ Unregistered Business Operators)   |       |

## 5. Securities Inspection (4)

### Type of Financial Instruments businesses

Type I financial instruments business	Type II financial instruments business	Investment advisory and agency business	Asset management business
<ul style="list-style-type: none"> <li>• Sales and solicitation of securities with high liquidity</li> <li>• Market derivatives transactions of highly liquid securities</li> <li>• Underwriting</li> <li>• Over-the-counter derivatives transactions</li> <li>• Asset management</li> </ul>	<ul style="list-style-type: none"> <li>• Sales and solicitation of securities with lower liquidity</li> <li>• Market derivatives transactions of securities with lower liquidity</li> <li>• Market derivatives transactions of those other than securities</li> <li>• Self placement</li> </ul>	<ul style="list-style-type: none"> <li>• Investment advice</li> <li>• Acting as agent or intermediary in concluding investment advisory contracts and discretionary investment contracts</li> </ul>	<ul style="list-style-type: none"> <li>• Investment management</li> </ul>

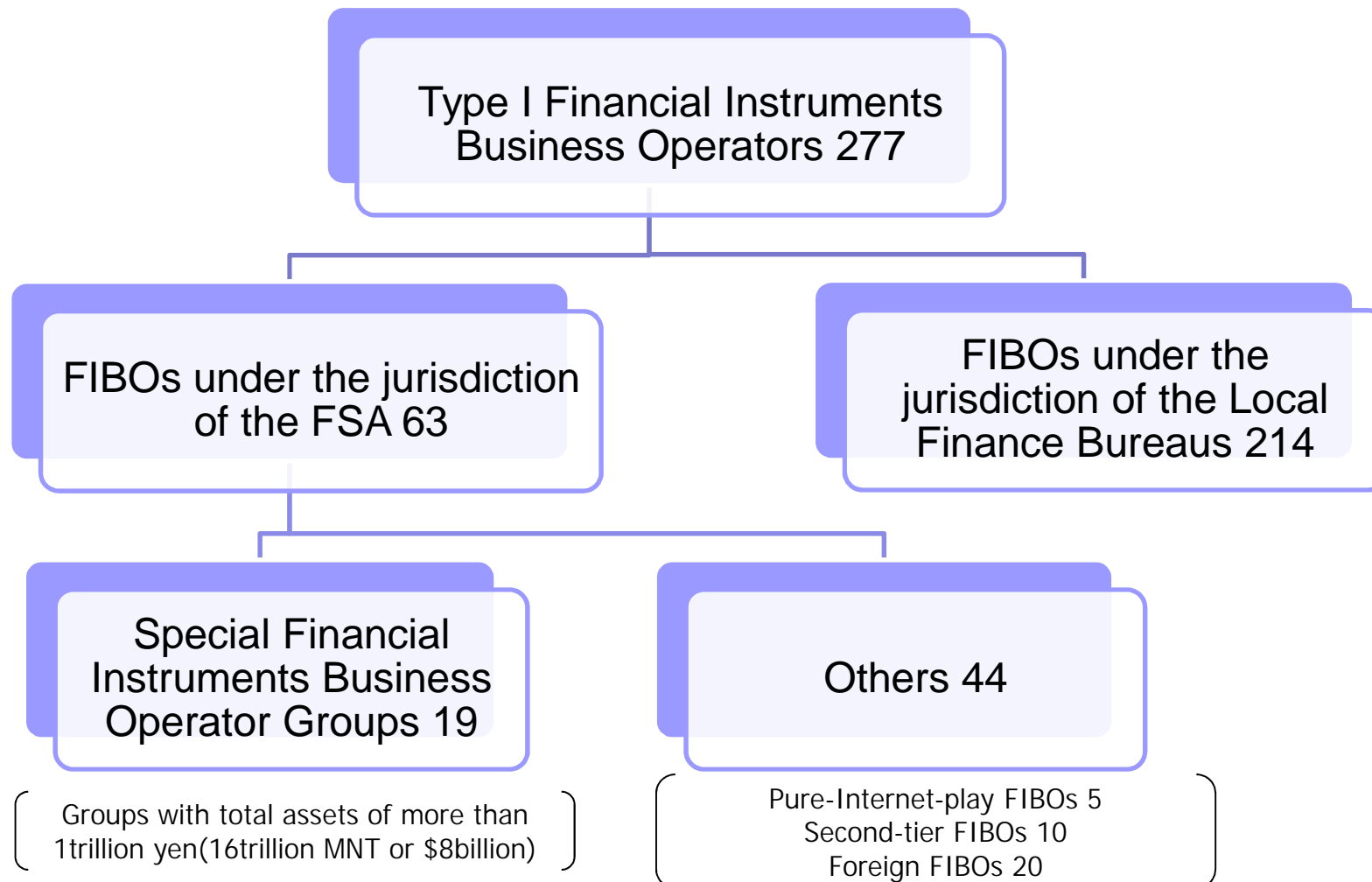
## 5. Securities Inspection (5)

- Risk-based prioritization of the inspection reflecting business type
  - FIBOs to inspect on a regular basis
    - ✓ Type I FIBOs
    - ✓ Type II FIBOs particularly on those which sell finds many individual investors
    - ✓ Asset Management Firms
  - FIBOs to inspect as needed
    - ✓ Investment Advisories/Agencies
    - ✓ Financial instrument intermediaries, etc.



## 5. Securities Inspection (6)

### -Number of the Type I FIBOs



## 5. Securities Inspection (7)

### -Inspection Policy and Program for 2014-15

#### Inspection Implementation Policy

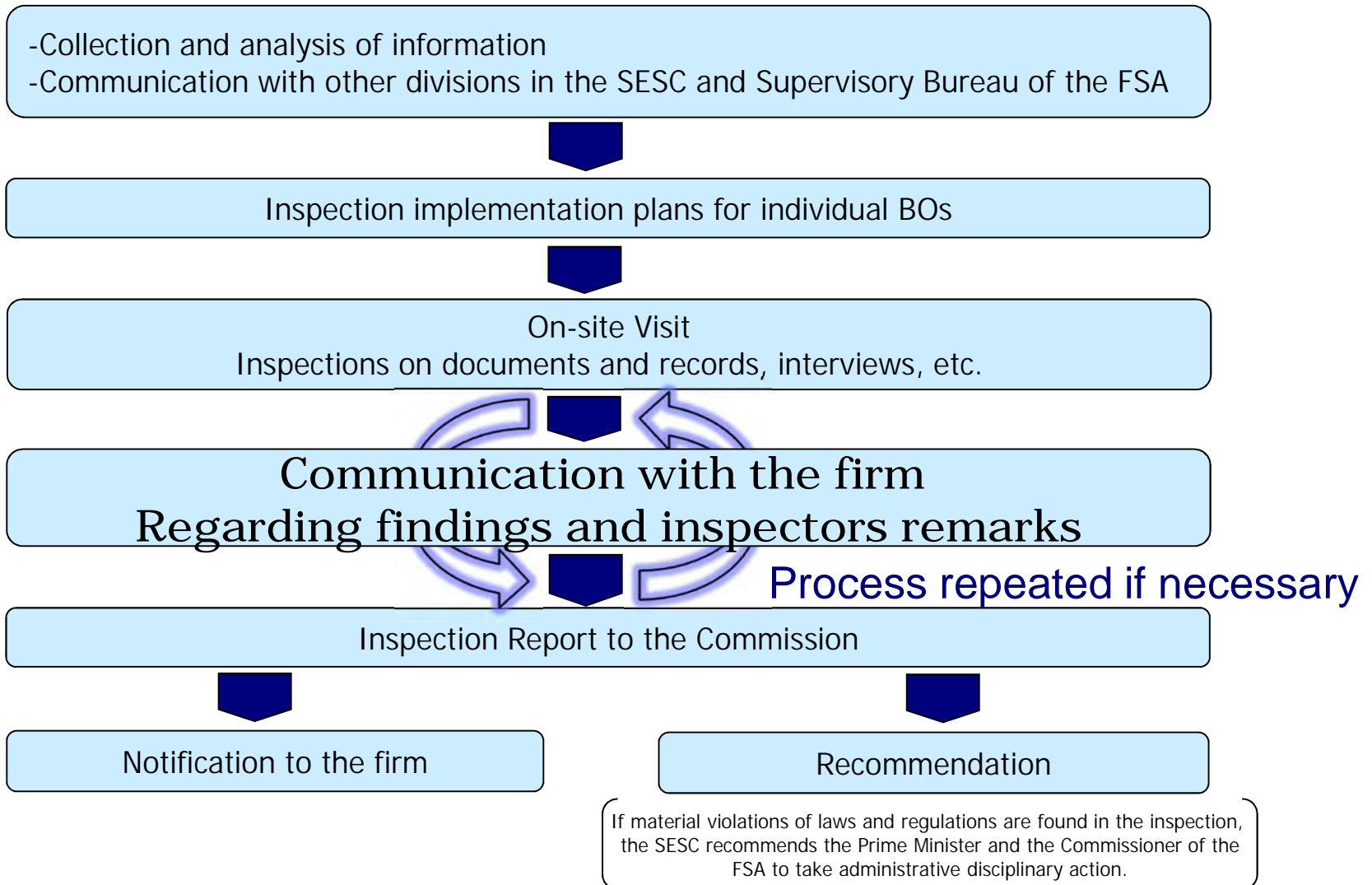
- Constantly monitoring large-scale securities company groups' financial soundness as a whole

#### Efficient, effective and viable securities inspections

- When determining inspection priorities for individual BOs, the SESC will collect and analyze a variety of information,
- Corresponding to their business types, sizes, other characteristics and the market conditions at the time,
- Then utilize a risk-based approach to decide which BOs to inspect, considering their market positions and inherent problems in a comprehensive manner.

## 5. Securities Inspection (8)

### -Inspection Process



## 5. Securities Inspection (9)

### -Inspection Areas

1. Business Management			
2. Internal Control, Legal Compliance			
3. Risk Management (including Financial Soundness)			
Risks concerning Regulations on Capital Requirements	Operational Risk	System Risk	Other Risks (e.g. Investment Risk, Funding Risk)
4. Internal/External Audit Function			
5. Crisis Management (BCP)			

\*For more details visit [http://www.fsa.go.jp/sesc/kensa/manual/kinyusyouhin\\_en.pdf](http://www.fsa.go.jp/sesc/kensa/manual/kinyusyouhin_en.pdf)

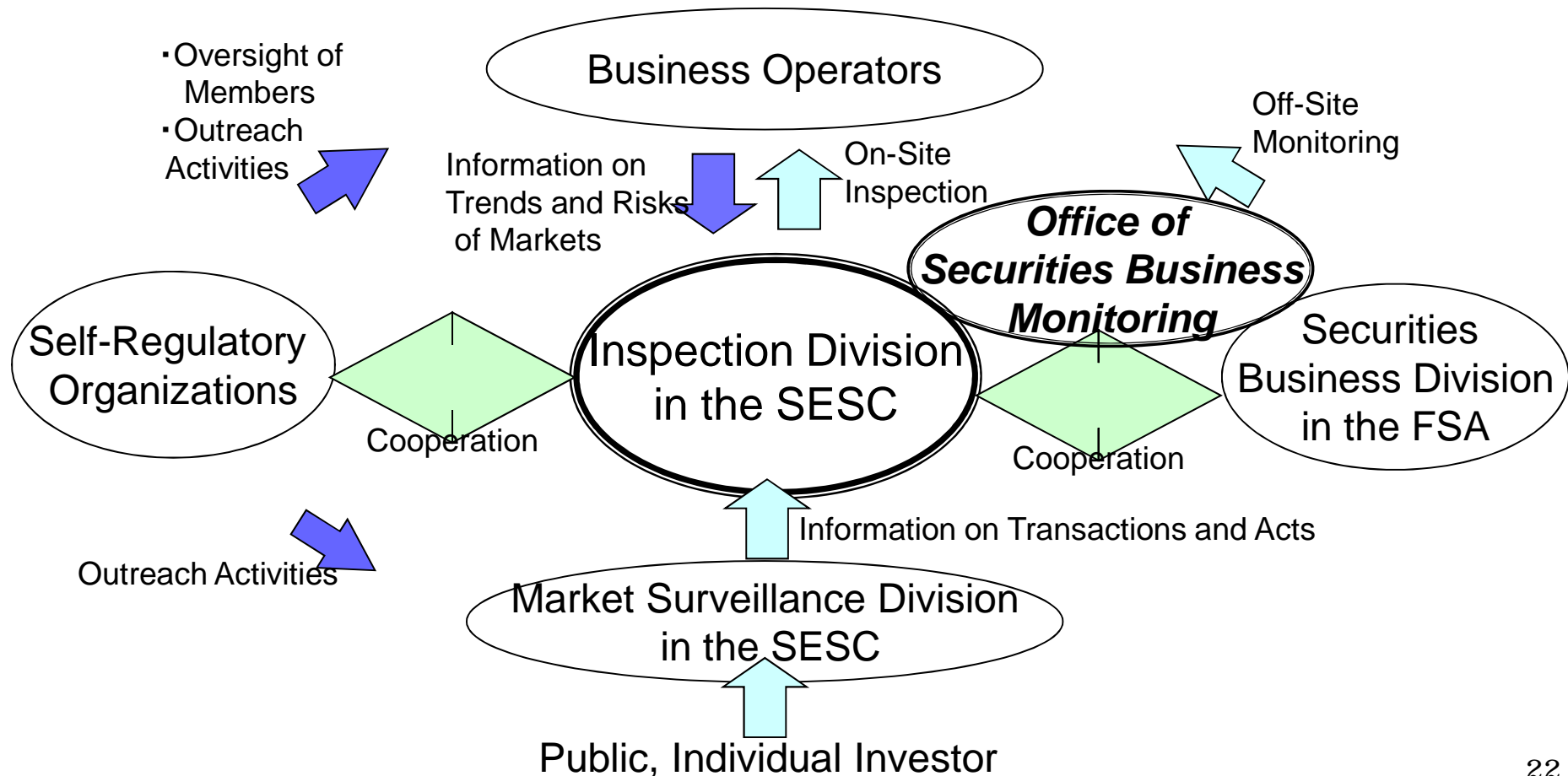
## 6. Collection and Analysis of Information(1)

Process and Practice of Securities Inspection



### Enhanced Communication and Cooperation with Other Institutions

- Importance of Information gathering
- Importance of Cooperation with SROs



## 6. Collection and Analysis of Information(2)



### Types of inspection

#### 1) General inspections

- General inspections are conducted focusing on general operational issues of the business operators, taking into comprehensive account various information, the results of the previous inspection and the inspection cycle.

#### 2) Special inspections

- Special inspections are conducted expeditiously on a part of a business operator's business operations based on information acquired.



## 6. Collection and Analysis of Information(2)



### Information Reception

Fiscal Year	2009	2010	2011	2012	2013
1.Amount of information received	7,118	6,927	6,179	6,362	6,401
Internet	4,293	4,040	3,543	3,881	4,316
Telephone calls	1,917	2,219	2,033	1,883	1,518
Letters	380	393	385	346	395
Visitation	60	45	54	57	56
Information forwarded from the FSA and Local Finance Bureaus	468	230	164	195	116
2.Content of the information					
Individual stock	3,889	3,640	3,227	3,751	4,040
Issuer	835	597	440	436	402
Sales approach of financial instruments business operator, etc.	1,349	1,142	878	790	907
Other(opinion, inquiry, etc.)	1,045	1,548	1,634	1,385	1,052

## 6. Collection and Analysis of Information(3)



### Analysis of data(1/2)

FY2013	Company A	B	C	FY2013	Company A	B	C
Balance sheet(Billions of yen)				Statement of income(Billions of yen)			
Current assets	6,937	10,919	16,145	Operating revenue	333	279	322
Trading products	3,054	5,263	10,076	Commission received	184	148	165
Loan secured by securities	2,865	4,926	4,340	Brokerage commissions	44	43	43
Other current assets	1,019	730	1,729	Underwriting and distribution commissions	35	24	21
Noncurrent assets	189	356	116	Flotation and distribution fees	65	37	51
Property and equipment	7	17	17	Other fees received	41	43	51
Intangible assets	32	30	23	Net trading income	127	96	137
Investments and other assets	149	308	76	<Equities>	11	26	48
Investment securities	60	231	60	<Bonds>	108	70	96
<b>Total assets</b>	<b>7,126</b>	<b>11,274</b>	<b>16,260</b>	<Other>	7	-1	-7
Current liabilities	6,069	9,583	15,521	Financial revenue	23	33	19
Trading products	1,871	4,210	7,232	Financial expenses	15	26	9
Loans payable secured by securities	2,526	4,252	5,855	Net operating revenue	319	253	313
Short-term loans payable	1,033	510	1,997	Selling, general and administrative expenses	222	203	197
Other current liabilities	638	612	438	Operating income/loss	97	50	116
Noncurrent liabilities/Reserves under the special laws	482	1,093	359	Ordinary income/loss	97	54	118
Long-term loans payable	198	405	345	Extraordinary income/loss	-1	-0	5
Bonds payable	274	456	0	Net income before income/loss	97	54	123
<b>Total liabilities</b>	<b>6,551</b>	<b>10,677</b>	<b>15,881</b>	Income taxes-current	18	2	9
<b>Total net assets</b>	<b>575</b>	<b>597</b>	<b>379</b>	Income taxes-deferred	17	-8	-7
<b>Total liabilities and net assets</b>	<b>7,126</b>	<b>11,274</b>	<b>16,260</b>	Net income/loss	61	60	121

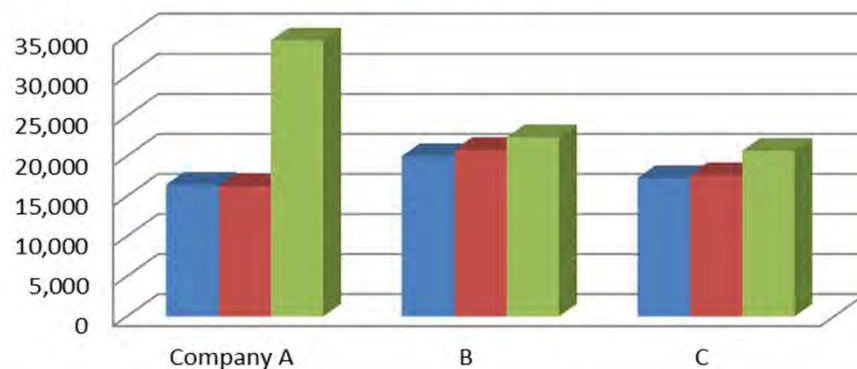
## 6. Collection and Analysis of Information(4)

### Analysis of data(2/2)



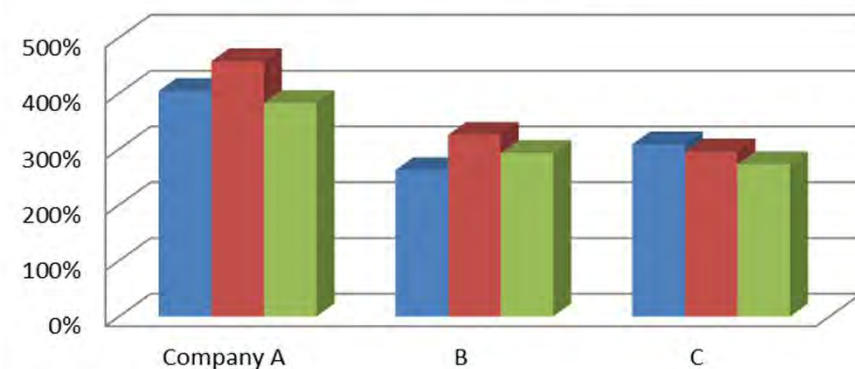
**Underwriting Fee**

(Millions of yen) Mar-12 Mar-13 Mar-14



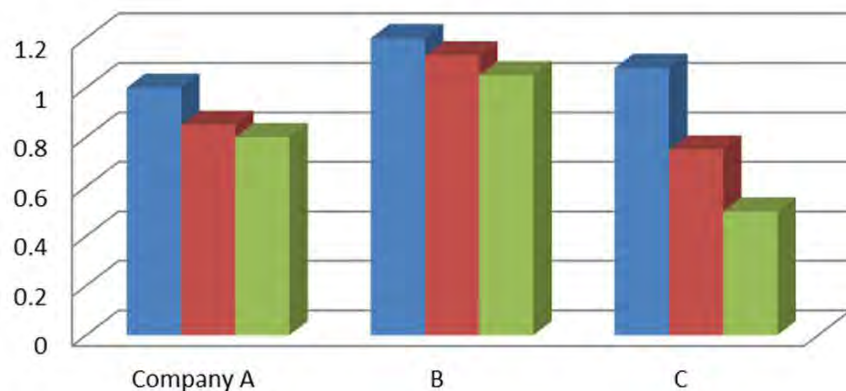
**Capital-to-risk ratio**

Mar-12 Mar-13 Mar-14



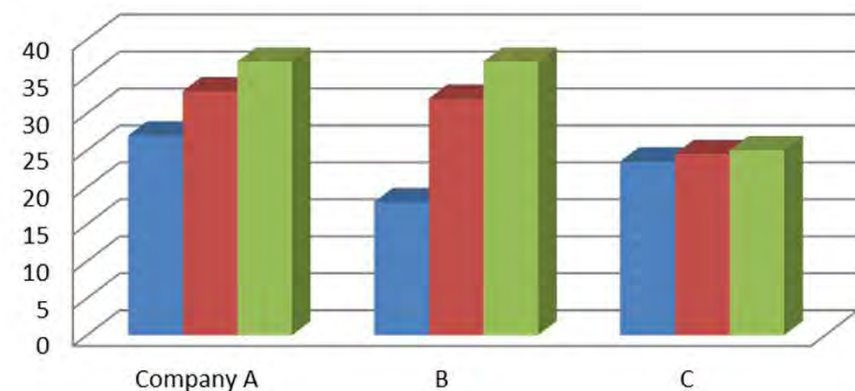
**Average holding period of Investment Trust**

(year) Mar-12 Mar-13 Mar-14



**Client Assets**

(Trillions of yen) Mar-12 Mar-13 Mar-14



## 7. Recent Cases(1)

~ Lack of adequate staffing, failure to maintain the statutory levels of net assets, and violation of business improvement order ~

### ■ Findings

- The on-site inspection revealed that:
  - Securities Company M did not have adequate staffing to conduct securities business appropriately.
  - Though the FSA had issued an improvement order to Securities Company M to increase its net assets, it didn't take any remedial measures, so their net assets were still below the statutory level.(50million yen or 800million MNT)
  - Securities Company M had not submitted a business improvement report even though the due date of submission had already passed.

## 7. Recent Cases(2)

### ■ Enforcement action (Aug. 12, 2011)

A) Registration Revocation Order

B) Business Improvement Order:

- i. Comprehend the situation of customers and the management of customers' assets promptly, developing a plan for returning these assets to customers, and implement the plan properly.
- ii. Adequately explain to the customers the plan regarding i. above and the enforcement actions.
- iii. Do not misappropriate Securities Company B's assets.
- iv. Submit a written report by Aug. 26, 2011, describing the actions taken and the implementation status regarding i. to iii. above.

## 7. Recent Cases(3)



### ■ TIBOR/LIBOR cases (Recommended on December 9, 2011)

- Against UBS Securities Japan Ltd. & Citigroup Global Markets Japan Inc.
- Recommendations made concerning inappropriate actions related to TIBOR, etc.
- FSA suspended their related derivative transactions.

### ■ Nomura case (Recommended on July 31, 2012)

- Against Nomura Securities Co., Ltd.
- Recommendation made concerning its insufficient systems to prevent misuse of confidential corporate information related to public offering of new shares
- FSA issued a business improvement order.





## 7. Recent Cases(4)



- **Deutsche Securities cases** (Recommended on December 5, 2013)
  - ☐ Against Deutsche Securities Inc.
  - ☐ Recommendations made concerning special benefits to officers of three employees' pension funds.
  - ☐ FSA issued a business improvement order.



# Reference Material

# Main points of Inspection Policy for 2014-15



## 《Basic Direction》

### Role of inspections

- To take rigorous actions against illegal activities and play a role in sending alerts to the markets
- To ensure investor confidence in the markets by enhancing self-discipline of BOs

### Change in Circumstances

- Diversification and increase in the number of BOs (Around 8,000 operators engage in business)
- Financial instruments and transactions have become more diverse and complex

### Current Challenges

- Revelation of serious cases
- To restore investors' confidence by not only verifying the compliance but also urging BOs to improve compliance posture and professional ethics

## < Efforts toward efficient, effective and viable securities inspection corresponding to the diverse characteristics of the BOs >

- Strengthening the capabilities to collect and analyze information by enhancing the capacity of the SESC to identify potential problems with consideration given to the characteristics of business types, customers types, and types of financial instruments and transactions.
- Utilizing a risk-based approach to decide which BOs to inspect by considering their business types, sizes, other characteristics and other information in a comprehensive manner.

## 《Inspection Implementation Policy》

- ◆ Conducting on-site inspections and off-site monitoring on large-scale securities groups
- ◆ Enhancement of cooperation with FSA for inspections of Type I FIBOs
- ◆ Conducting regular inspections on Type II FIBOs, particularly on those which sell funds to a large number of individual investors
- ◆ Conducting regular inspections on investment management business operators
- ◆ Conducting concise inspection of registered information on Type II FIBOs and investment advisors/agencies
- ◆ Rigorous actions against fund related business operators engaging in illegal activities and unregistered business operators

## < Implementation Plan and Focus in Verification >

- Establishment of systems for properly soliciting and explaining to aged customers or customers utilizing the NISA
- Management of material non-public information
- Organizational actions to block relations with anti-social groups
- Financial soundness of BOs
- Due diligence, monitoring and customer solicitation activities by fund related business operators selling overseas instruments

# Number of Inspected Entities

Business categories	Apr.-10 Mar.-11	Apr.-11 Mar.-12	Apr.-12 Mar.-13	Apr.-13 Mar.-14	Apr.-14 Mar.-15
Financial Instruments Firms	148	148	153	222	206
Type I Financial Instruments Business	91	85	57	69	77
Type II Financial Instruments Business	6	14	20	108	72
Asset Management Firms	15	9	36	16	15
Investment Advisories/Agencies	36	40	40	29	42
Registered Financial Institution	28	32	28	9	1
Financial Instrument Intermediary Service Providers	1	9	9	8	18
Investment Companies	6	2	0	3	2
Self Regulatory Organizaitions	1	0	0	3	3
Others	2	11	24	26	36

(Note ) The number above is that of inspections undertaken.

# Findings from Inspections

Category		Apr.-12 Mar.-13	Apr.-13 Mar.-14	Apr.-14 Mar.-15
Recommendation		18	18	16
Firms with problems found		102	118	105
	Unfair transactions	6	5	7
	Lack of investor protection	52	65	71
	Improper financial soundness	11	9	19
	Others	71	69	52

Note) "firms with problems found" shows the number of the firms for which we pointed out some problems in the inspection.

# List of the item we ask for



"for investors, with investors"

検査会場においてご準備いただきたい資料等 (Material to submit)

検査基準日：平成27年3月8日 (AS of 3/8/2015)

証券取引等監視委員会 (SESC)

番号 (No.)	項目 (Items)	期間 (Term)	提出形態等 (Submission method)	提出期限 (Due Date)	備 考 (Remarks)
<b>1. 全般資料 (General)</b>					
1-1	組織図 (Organizational chart)	2012/4～2015/3	イントラ (Intranet)	2015/3/19	改正の経緯がわかるもの、検査基準日現在では部署毎に常勤職員数記入のこと (include the number of the employees)
1-2	グループ図 (Correlation chart)	2012/4～2015/3	イントラ (Intranet)	2015/3/19	改正の経緯がわかるもの (include transition)
1-3	各種社内規程集 (Internal rule)	直近のもの (Latest)	イントラ或いは紙 (Intranet or paper)	2015/3/19	各業務マニュアル等も含む (include various operating manual)
1-4	役員の履歴 (List of the executive)	直近のもの (Latest)	イントラ或いは紙 (Intranet or paper)	2015/3/19	検査対象期間中に退任した役員分も含む、役員については兼職状況も併せて記載 (Include ex-executives)
1-5	業務概況メモ (Operation overview)	直近のもの (Latest)	イントラ或いは紙 (Intranet or paper)	2015/3/19	対象は営業部門のみ。各営業部門の提出資料と重複しないように要相談。 (only for sales division)
<b>2. 会議録資料 (Minutes)</b>					
2-1	主要会議・委員会等の記録 (Board Minutes, etc.)	2012/4～2015/3	イントラ或いは紙 (Intranet or paper)	2015/3/19	議事録等の一覧を提出、個別記録は別途相談 (submit the list of the minutes at first)
<b>3. 法定帳簿等 (Statutory Books)</b>					
3-1	注文伝票 (Order invoice)	2012/4～2015/3	イントラ或いは紙 (Intranet or paper)	2015/3/19	
3-2	取引日記帳 (Trading diary)	2012/4～2015/3	イントラ或いは紙 (Intranet or paper)	2015/3/19	
3-3	顧客勘定元帳 (Customer accounts ledger)	2012/4～2015/3	イントラ或いは紙 (Intranet or paper)	2015/3/19	
3-4	トレーディング商品勘定元帳 (traded instruments accounts ledger)	2012/4～2015/3	イントラ或いは紙 (Intranet or paper)	2015/3/19	
3-5	法定帳簿のコード索引表等 (Code table of the books)		イントラ或いは紙 (Intranet or paper)	2015/3/19	電子データで保存の場合、その使用手引き等を含む (include manual that explains how to use)
<b>4. 内部管理 (Internal Control Systems)</b>					
4-1	内部統制・法令遵守・内部管理体制について (Management system)		イントラ或いは紙 (Intranet or paper)	2015/3/19	①当社の内部統制・法令遵守・内部管理体制全般について記載 ②①については当社営業部門に対する牽制、チェック体制について記載 (describe management system)
4-2	メール記録等 (E-mail data)	直近のもの (Latest)	イントラ (Intranet)		検査予告後削除禁止 (don't delete until a further instruction)
4-3	証券事故関係 (Reporting of problematic conduct)	2012/4～2015/3	イントラ或いは紙 (Intranet or paper)	2015/3/26	
4-4	苦情処理・訴訟関連 (The list of complaints)	2012/4～2015/3	イントラ或いは紙 (Intranet or paper)	2015/3/26	
<b>5. Stock Sales</b>					
<b>6. Debenture Business</b>					
<b>7. Investment Banking Business</b>					
<b>8. Property and Accounting</b>					
<b>9. Separate Management</b>					
<b>10. Internal Audit System</b>					
<b>11. Risk Management System</b>					
<b>12. Liquidity Risk Management System</b>					
<b>13. Market Risk Management System</b>					
<b>14. Credit Risk Management System</b>					
<b>15. Operational Risk Management System</b>					
<b>16. Information Technology Risk Management System</b>					





# Thank you

SESC's pamphlet: <http://www.fsa.go.jp/sesc/english/aboutsesc/all.pdf>

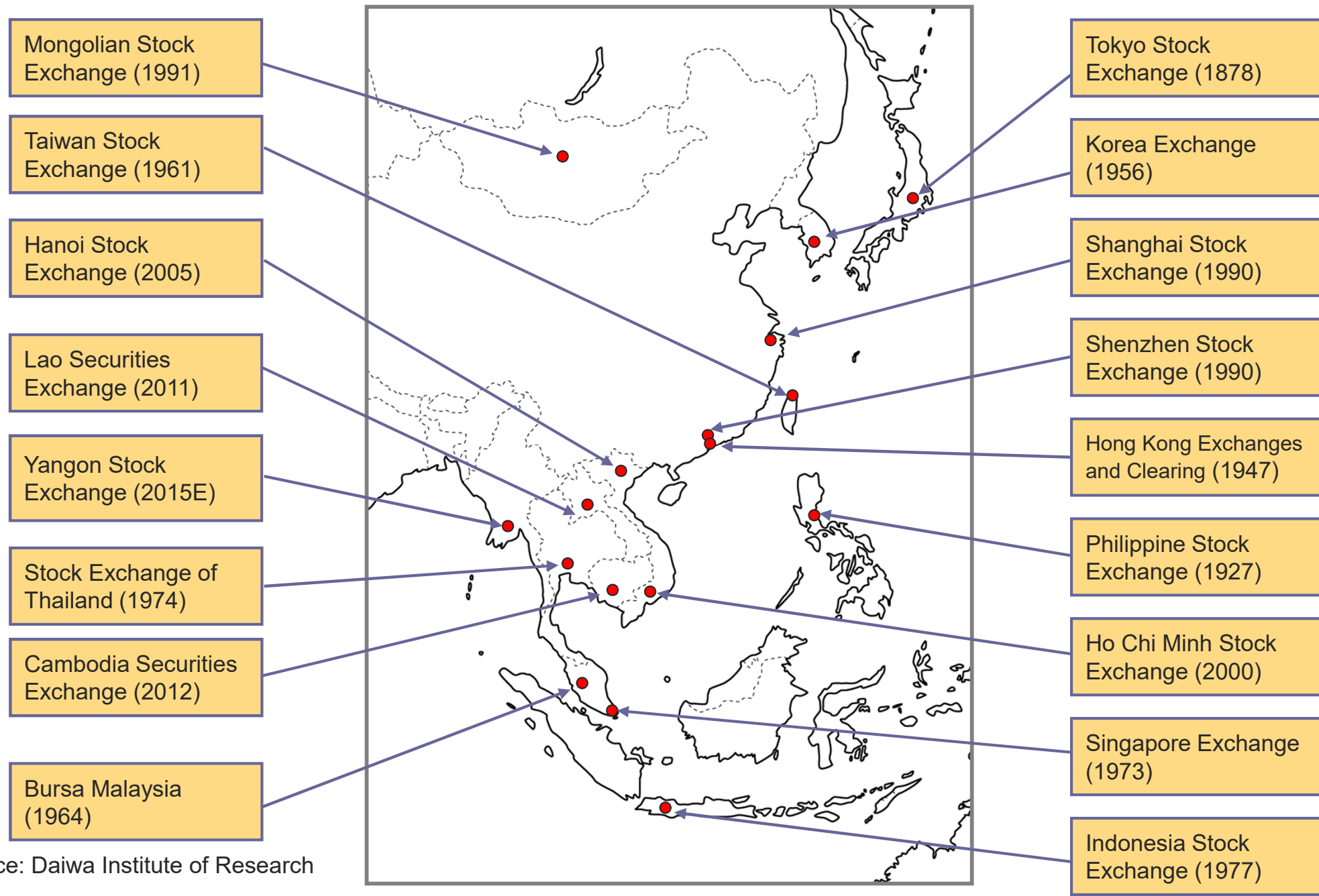
# **Project for Capacity Building of Capital Market in Mongolia: Stock Markets in Asia**

---

29 April 2015

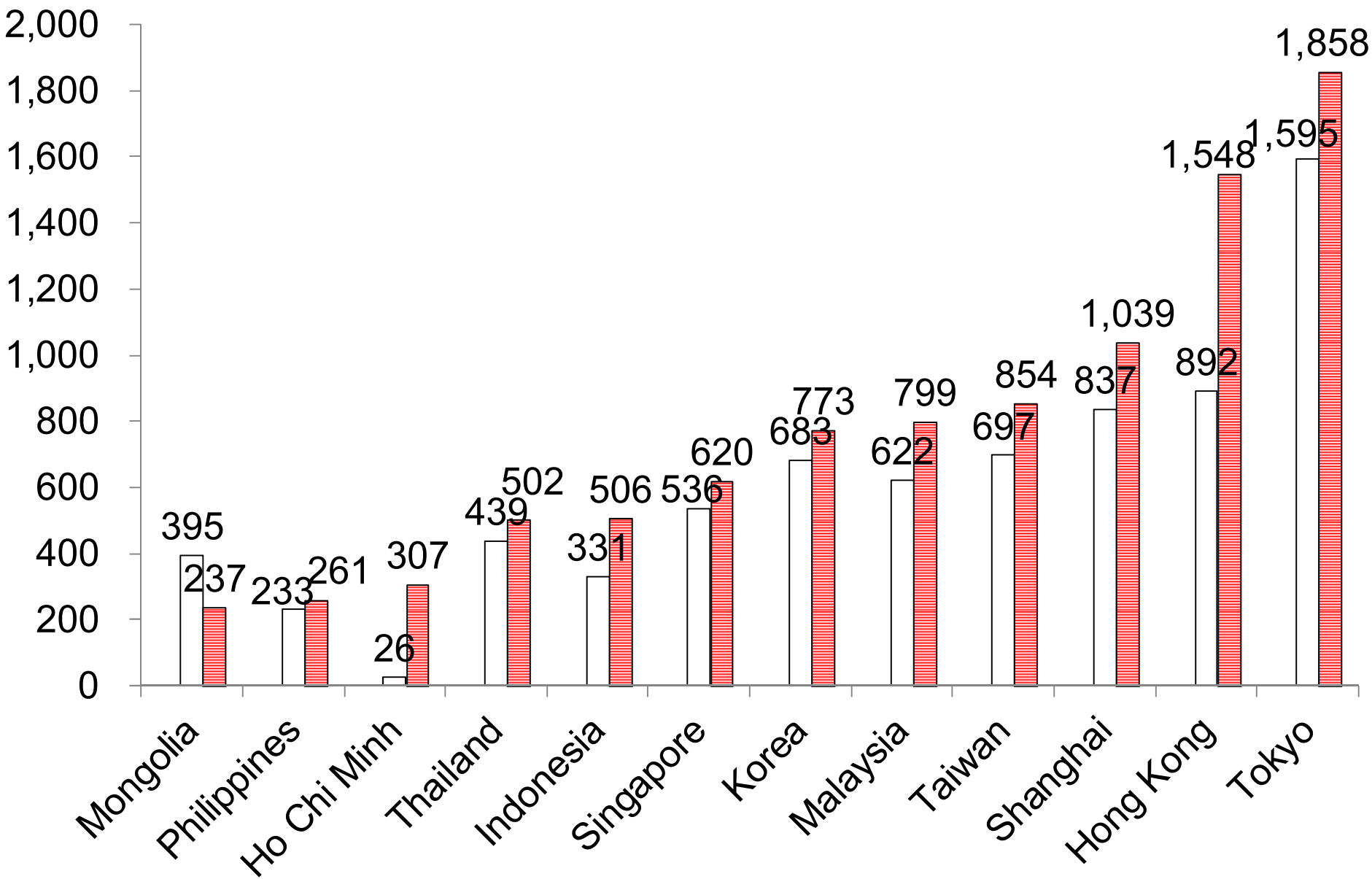
Daiwa Institute of Research  
Japan Economic Research Institute

# 1-a. Stock exchanges in Asia



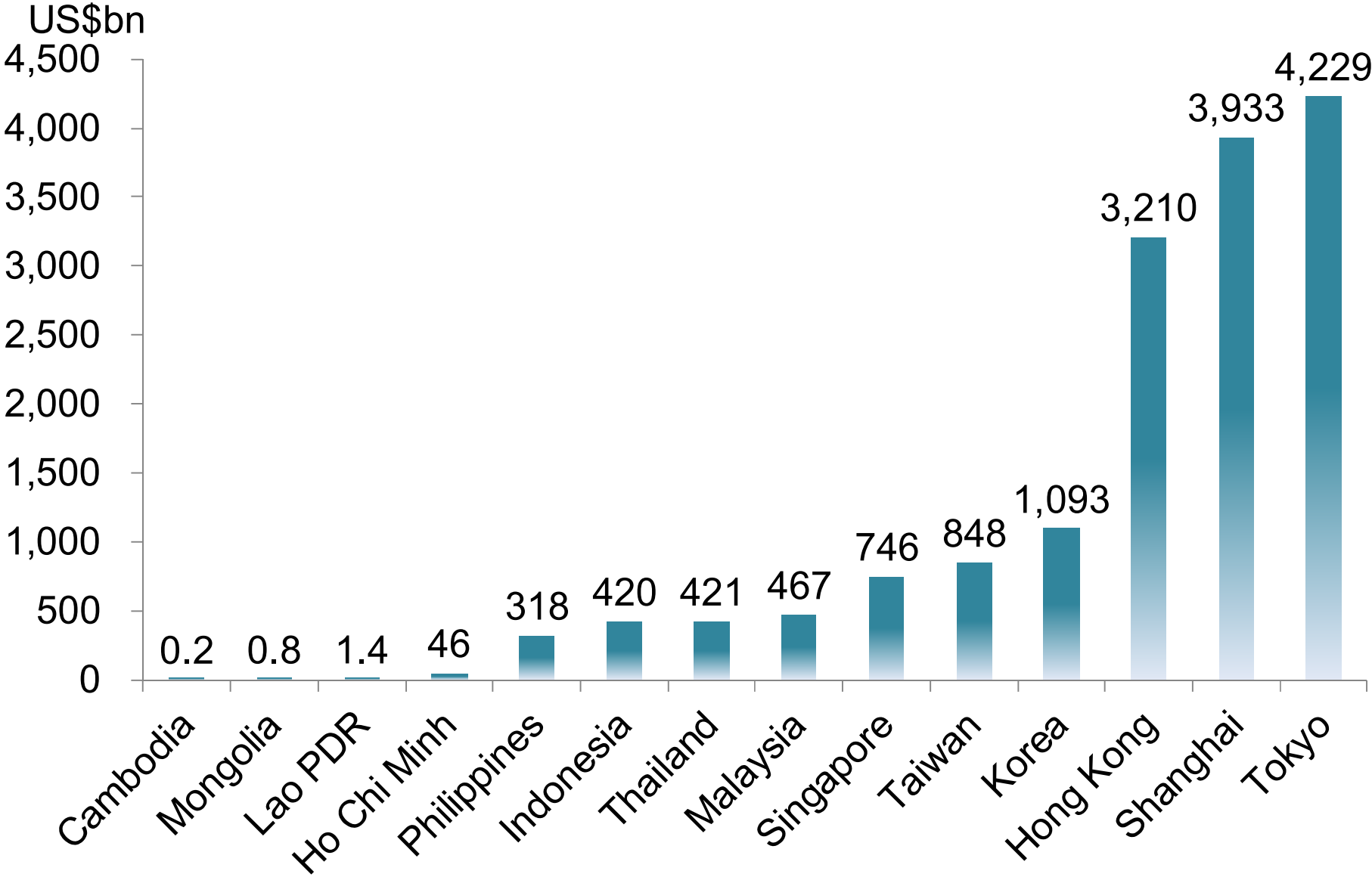
Source: Daiwa Institute of Research

**1-b. Number of listed companies, end-Dec04 and end-Dec14**



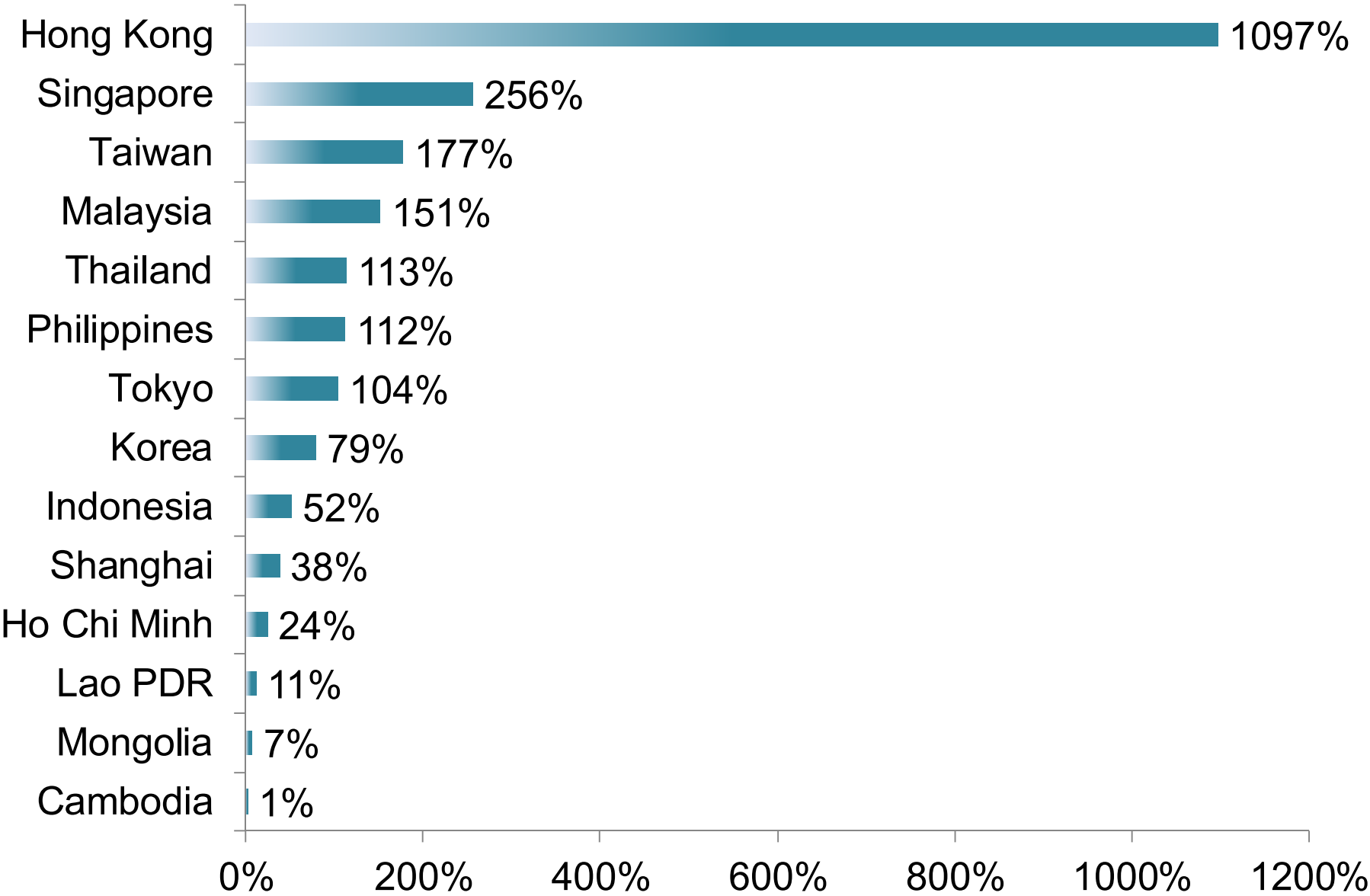
Source: various stock exchanges

1-c. Market capitalization, end-Dec14



Source: various stock Exchanges

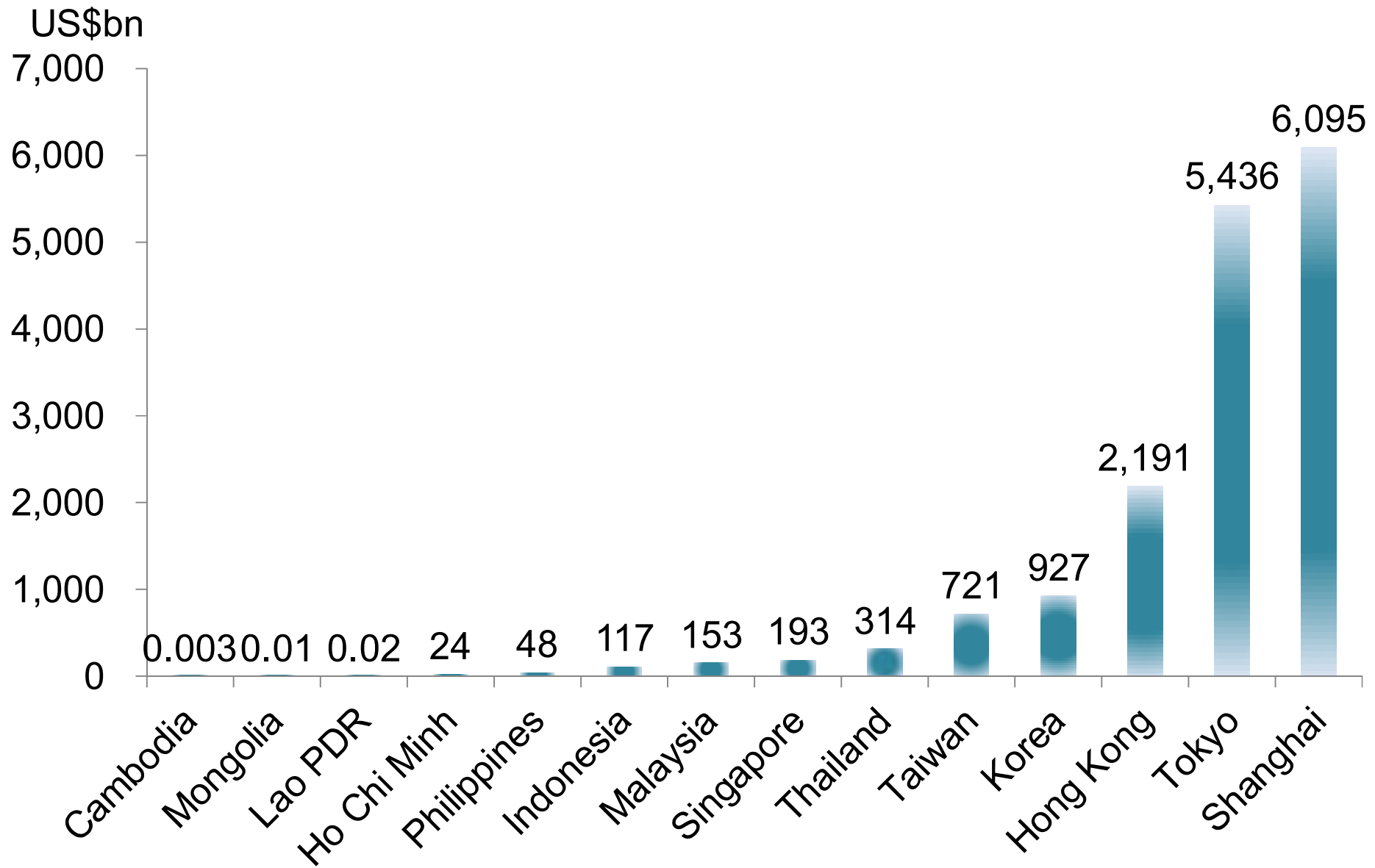
# 1-d. Market capitalization to GDP, 2014



Source: various stock exchanges

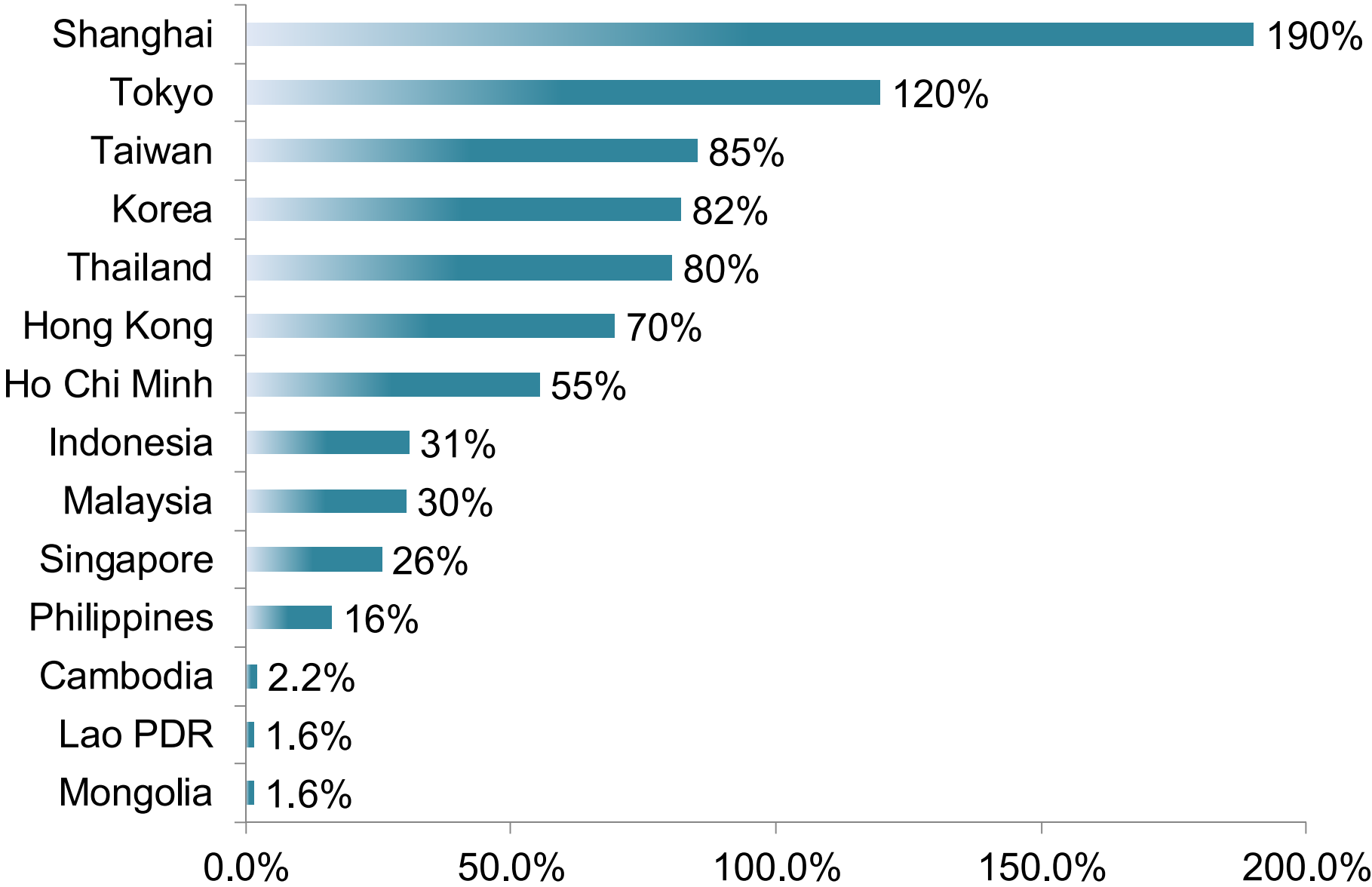


1-e. Annual trading value, 2014



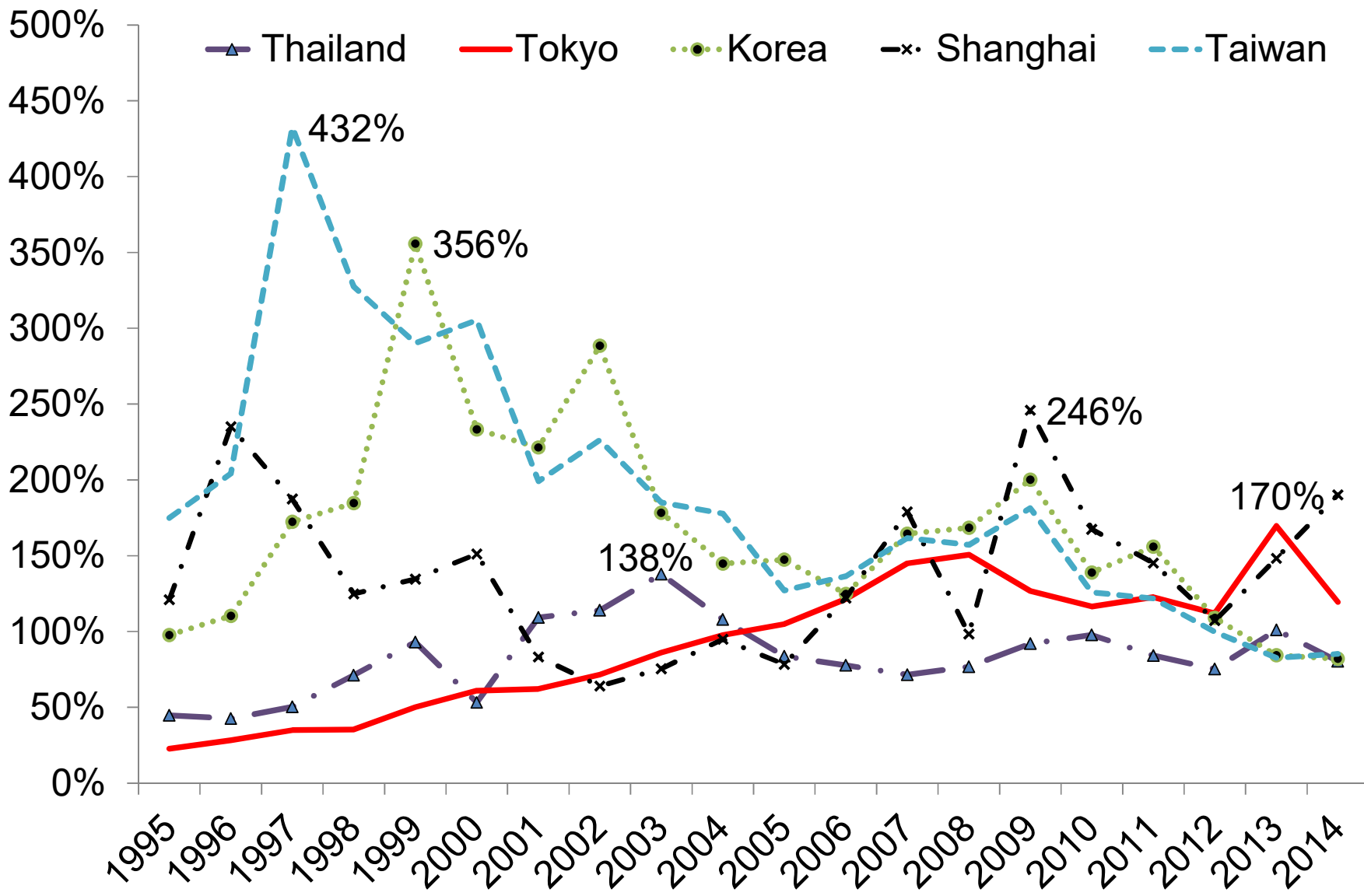
Source: various stock exchanges

**1-f. Turnover ratios (trading value / market capitalization), 2014**



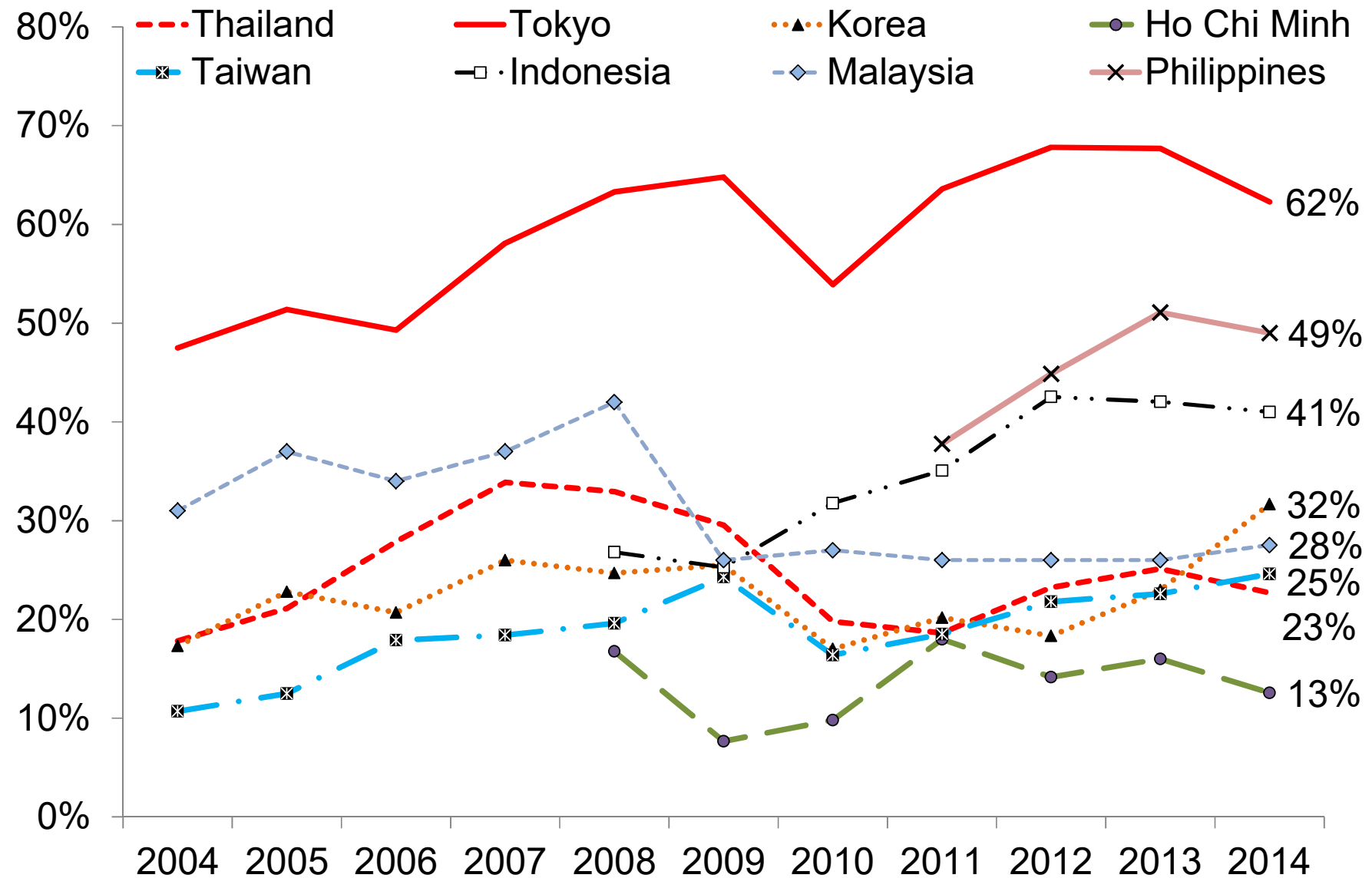
Source: various stock Exchanges

# 1-g. Historical turnover ratios (trading value / market capitalization)



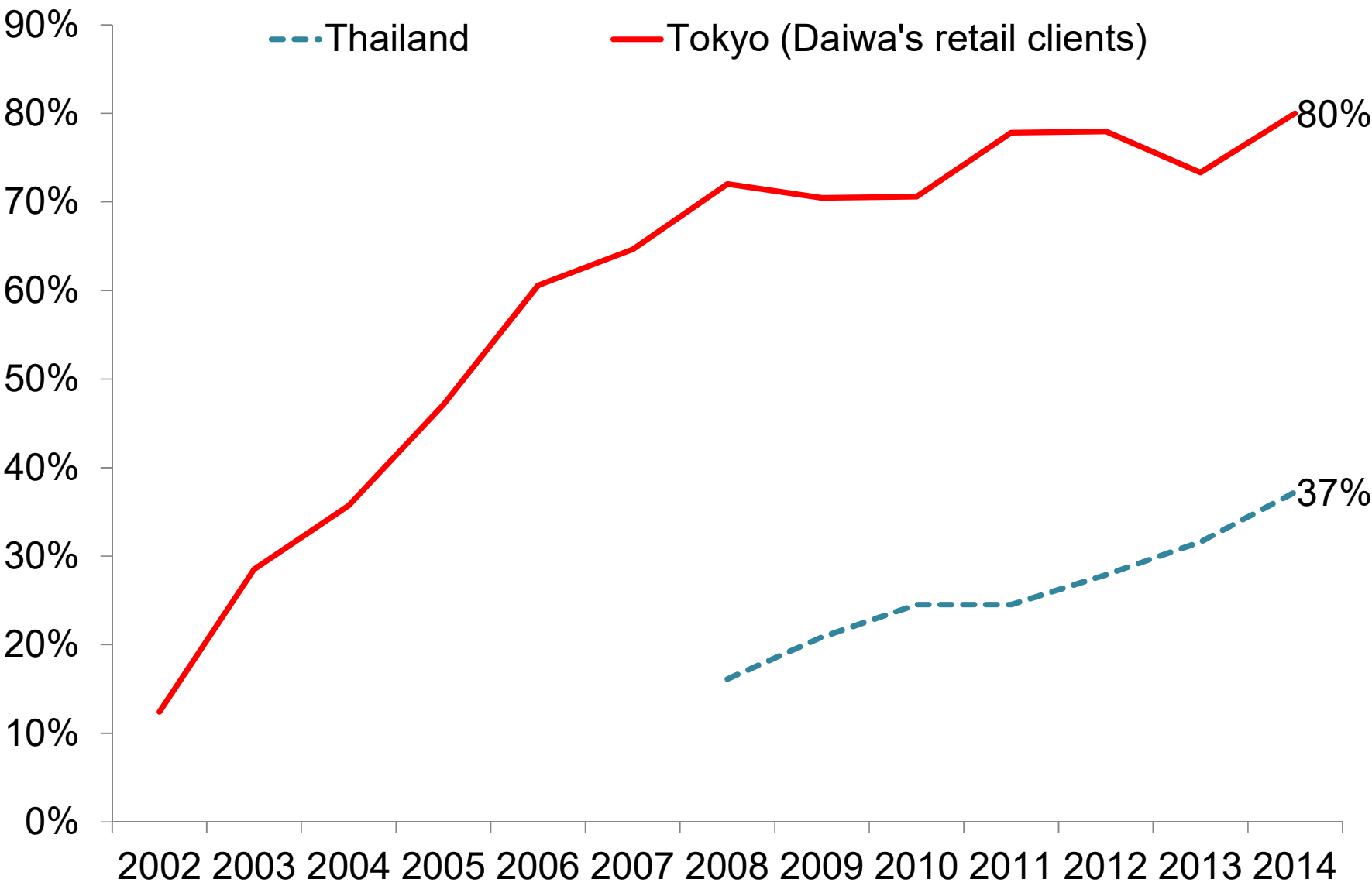
Source: Stock Exchange of Thailand, Japan Exchange Group, Korea Exchange, Shanghai Stock Exchange, Taiwan Stock Exchange

# 1-h. Shares for foreign investors in trading value



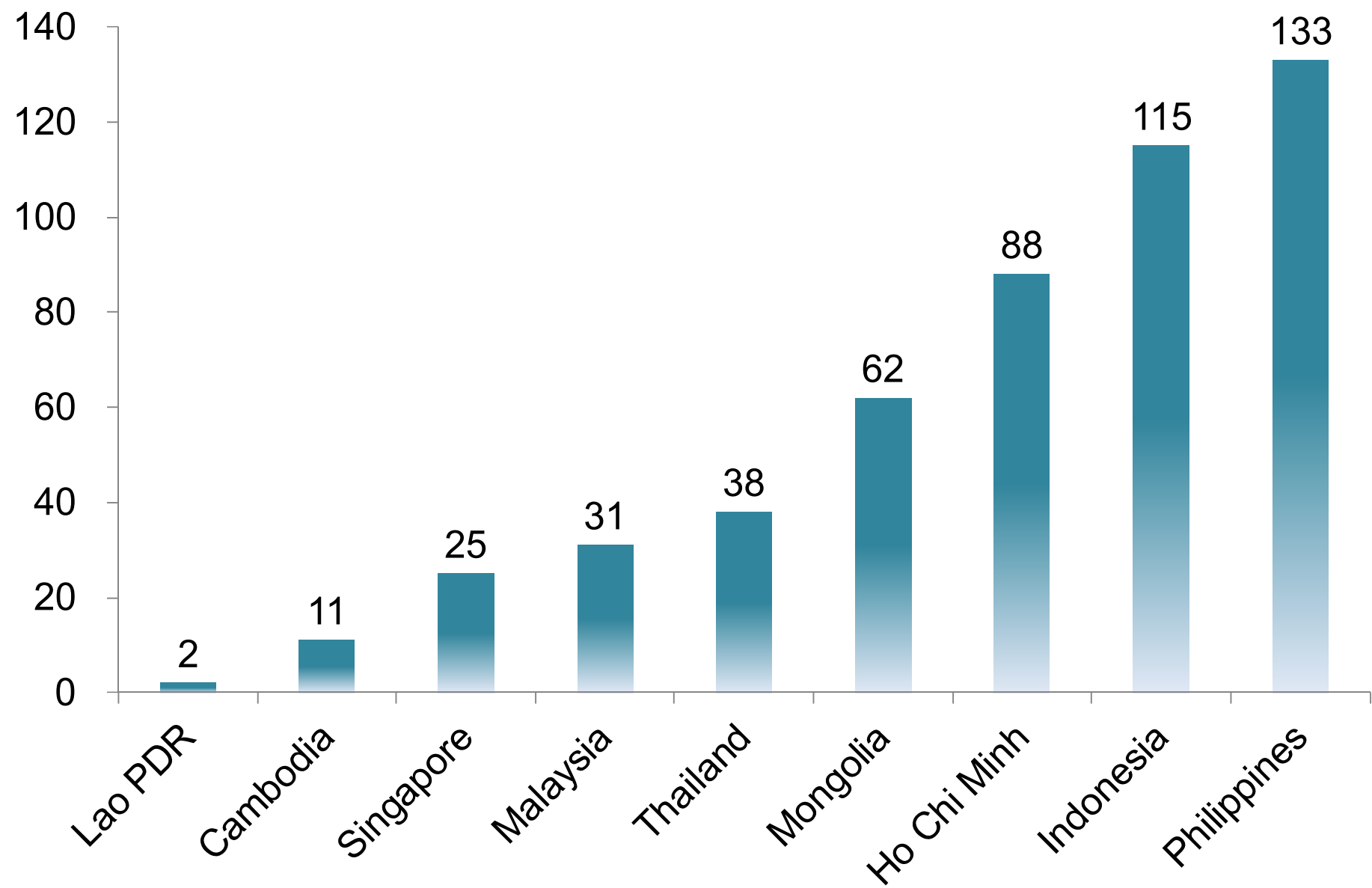
Source: Indonesia Exchange, Bursa Malaysia, Philippine Stock Exchange, Stock Exchange of Thailand, Japan Exchange Group, Korea Exchange, Hochiminh Stock Exchange, Taiwan Stock Exchange

# 1-i. Shares of online trading



Source: Stock Exchange of Thailand, Daiwa Securities Group

**1-j. Number of member securities companies, end-Dec14**



Source: various stock exchanges



## 2-a. Main features of selected stock exchanges in Asia

### Japan

- 1) There are multiple number of stock exchanges. Tokyo Stock Exchange has a market share of 90% or over.
- 2) Foreign investors account for 60% or so.
- 3) Share prices are highly influenced by the US market.

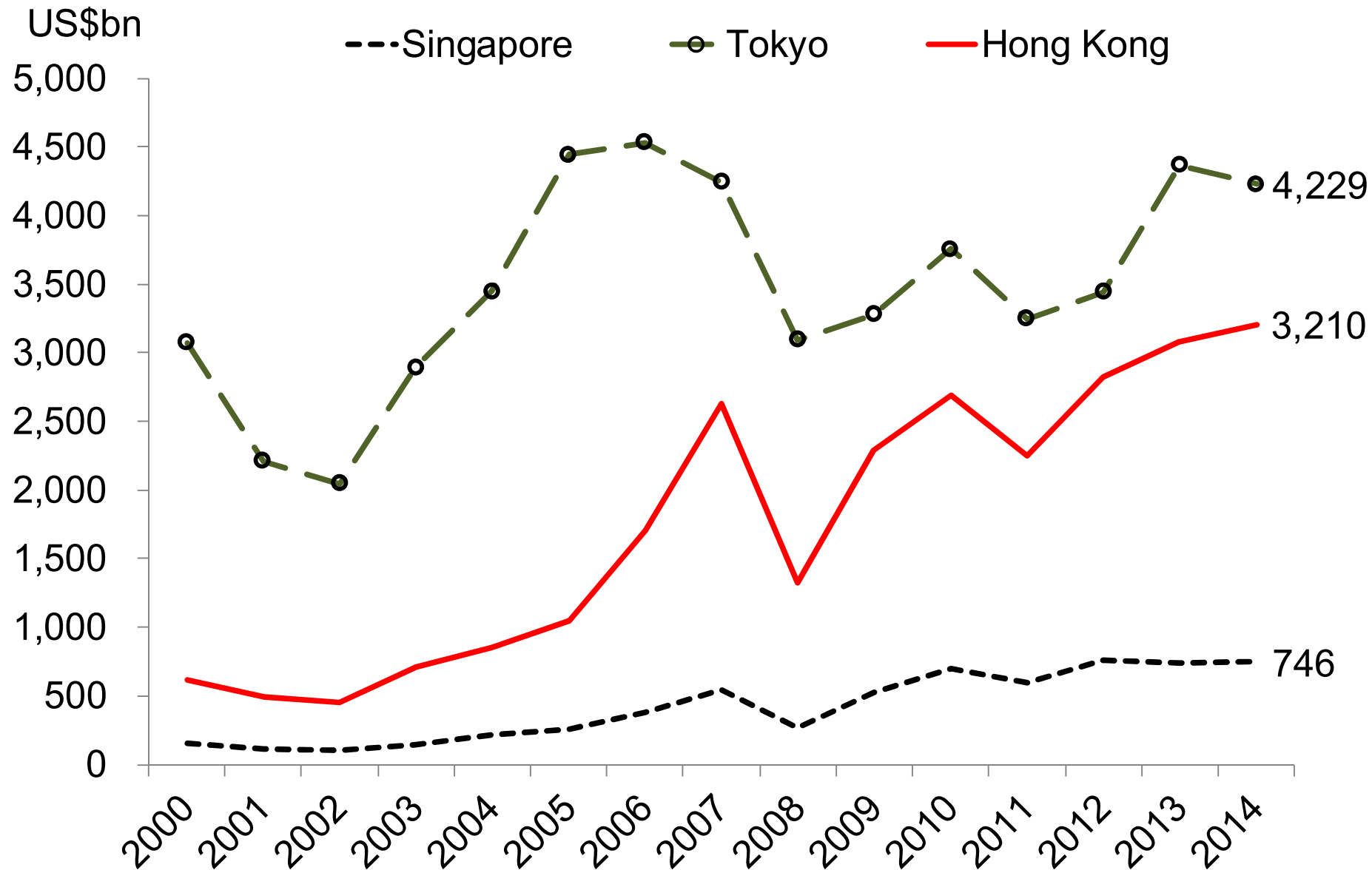
### Hong Kong

- 1) Many of large-cap Hongkong-origin stocks are property and service companies.
- 2) China-related stocks have been the biggest driving force.
- 3) Foreign companies' IPO activities are relatively popular.

### Taiwan

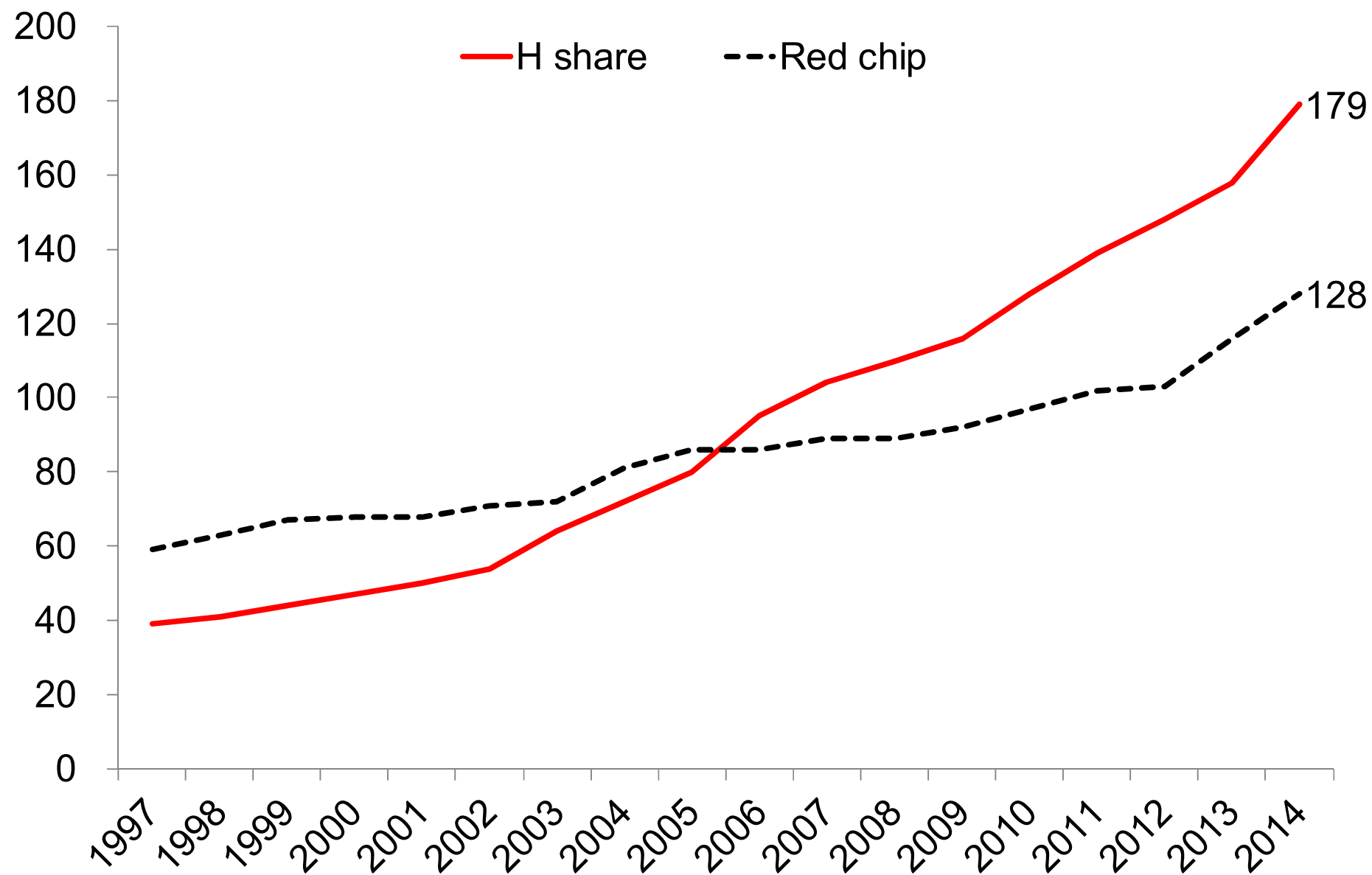
- 1) Highly concentrated in the electronics sector.
- 2) Retail investors are very active.
- 3) Share bonus scheme has helped the market to develop.

## 2-b. Hong Kong: Historical market capitalization



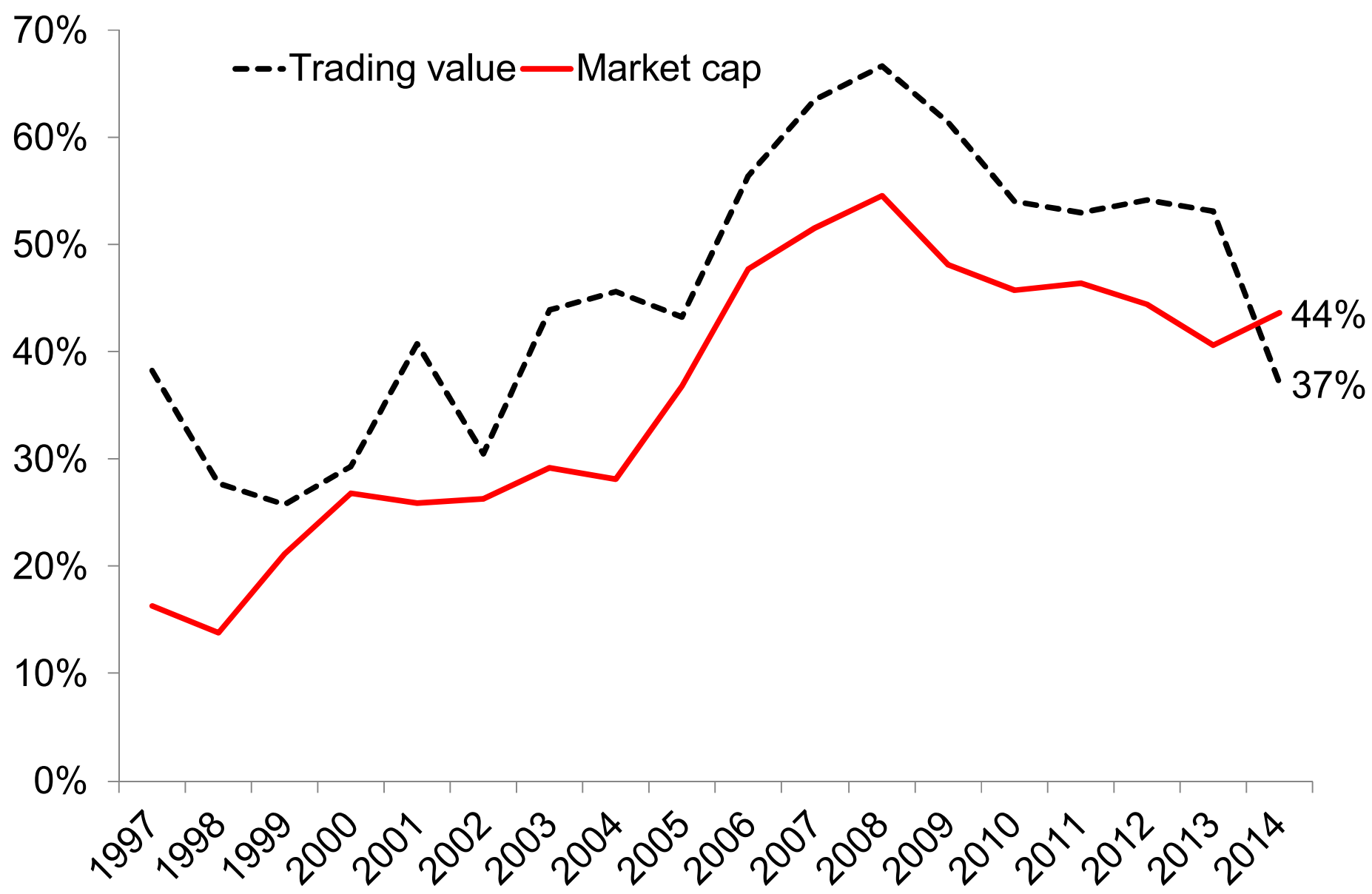
Source: Singapore Exchange, Tokyo Stock Exchange, Hong Kong Exchange and Clearing

## 2-c. Hong Kong: No of H shares and red chips



Source: Hong Kong Exchange and Clearing

**2-d. Hong Kong: Share of H shares and red chips in trading value and market cap**



Source: Hong Kong Exchange and Clearing

## 2-e. Hong Kong: Listed companies place incorporated, end-Dec13

Place of incorporation	No of listed companies	Market capitalization		Trading value	
		HK\$bn	Share	HK\$bn	Share
Cayman Islands	599	5,755	24.1%	2,564	23.0%
Bermuda	461	2,210	9.2%	1,007	9.0%
Hong Kong	203	8,703	36.4%	2,928	26.3%
China	158	4,907	20.5%	4,218	37.9%
Singapore	8	12	0.1%	1	0.0%
Canada	4	2,005	8.4%	317	2.8%
UK	4	13	0.1%	9	0.1%
British Virgin Islands	4	10	0.0%	8	0.1%
Jersey	3	40	0.2%	5	0.0%
Japan	2	58	0.2%	39	0.4%
Luxembourg	2	20	0.1%	6	0.1%
Brazil	1	-	-	0.001	0.0%
Italy	1	177	0.7%	38	0.3%
US	1	-	-	0.03	0.0%
Total	1,451	23,909	100.0%	11,143	100.0%

## 2-f. Hong Kong: Top 20 listed companies by market cap, end-Dec14

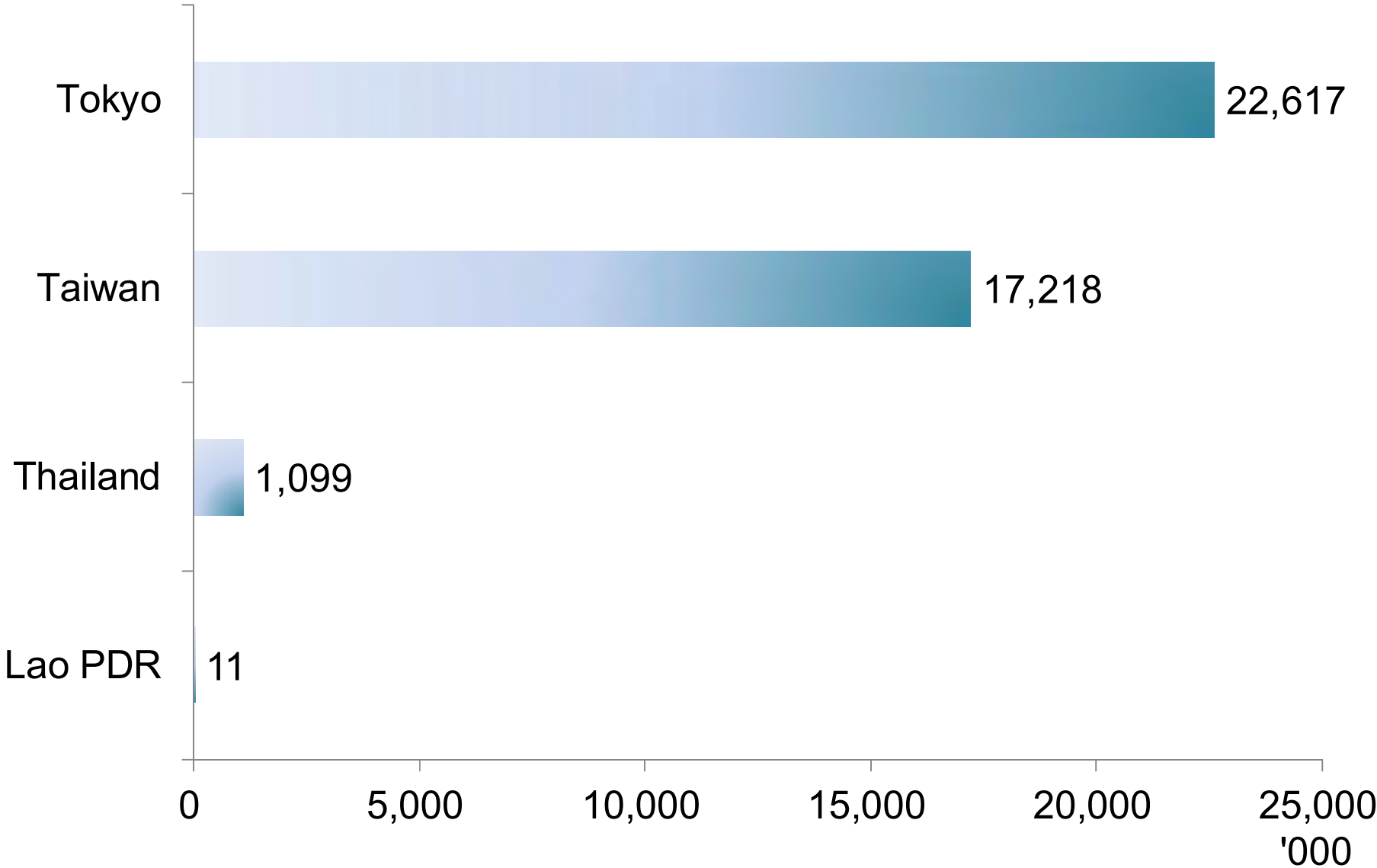
	Code	Company name	Country of origin	Market cap	Share
				HK\$bn	
1	941	China Mobile Ltd.	Red chip	1,846	7.4%
2	939	China Construction Bank Corporation	H share	1,531	6.2%
3	5	HSBC Holdings plc	England	1,422	5.7%
4	700	Tencent Holdings Ltd.	China	1,054	4.2%
5	1299	AIA Group Ltd.	ex-AIG	520	2.1%
6	1398	Industrial and Commercial Bank of China Ltd.	H share	491	2.0%
7	805	Glencore plc *	Swiss	482	-
8	883	CNOOC Ltd.	Red chip	466	1.9%
9	2378	Prudential plc *	England	466	-
10	13	Hutchison Whampoa Ltd.	HK	381	1.5%
11	3988	Bank of China Ltd.	H share	365	1.5%
12	16	Sun Hung Kai Properties Ltd.	HK	334	1.3%
13	267	CITIC Ltd.	Red chip	329	1.3%
14	1928	Sands China Ltd.	US	308	1.2%
15	1	Cheung Kong (Holdings) Ltd.	HK	302	1.2%
16	2318	Ping An Insurance (Group) Co. of China Ltd.	H share	295	1.2%
17	2888	Standard Chartered PLC	England	287	1.2%
18	945	Manulife Financial Corporation *	US	279	-
19	2388	BOC Hong Kong (Holdings) Ltd.	Red chip	274	1.1%
20	3328	Bank of Communications Co., Ltd.	H share	253	1.0%



## 2-g. Hong Kong: Selected foreign listed companies

Place incorporated	Code	Company name	Date of listing
England	5	HSBC	n.a.
England	847	Kazakhmys	Jun-11
England	2378	Prudential	May-10
England	2888	Standard Chartered	Oct-02
Canada	2099	China Gold International Resources Corp	Dec-10
Canada	1878	SouthGobi Resources	Jan-10
Canada	2012	Sunshine Oilsands	Mar-12
Japan	6889	Dynam	Aug-12
Japan	6288	Fast Retailing	Mar-14
Luxembourg	973	L'Occitane	May-10
Luxembourg	1910	Samsonite International	Jun-11
Italy	1913	PRADA	Jun-11
Brazil	6210	Vale	Dec-10
US	6388	Coach	Dec-11

2-h. Taiwan: Number of securities accounts, end-Dec14



Source: Taiwan Stock Exchange, Korea Exchange, Japan Exchange Group, Lao Securities Exchange

## 2-i. Taiwan: Some stories about Taiwanese general public

- 1) If you take a taxi and tells him you work in a securities company, the taxi driver is highly likely to ask you, “Foreign investors’ buying momentum is strong this week, which stock do you recommend ? ”
- 2) Quite a few number of Taiwanese employees at your office are perhaps monitoring their PC screens every morning. They are looking for a chance to place buy/sell orders.
- 3) Taiwanese individuals are also active in investing in unlisted companies. One may say, “One of my friend’s brother used to be an engineer at the largest semiconductor company in Taiwan, and he started up his own company last year. His company’s technology level is leading-edge and a big US smartphone manufacturer has just qualified his company’s products. His company wants to increase its share capital, don’t you want to buy some shares ?”
- 4) If you work at a Taiwanese listed company and you contribute significantly, you may be entitled to receive your company’s shares as bonus stock, which is sometimes much larger than your cash salary.

## 2-j. Taiwan: Top 20 listed companies by market cap, end-Dec14

	Code	Company name	Sector	Market cap US\$bn
1	2330	TSMC	Electronics - semiconductor	115
2	2317	Hon Hai	Electronics - EMS	41
3	2412	Chunghwa Telecom	Telecommunications	23
4	2454	MediaTek	Electronics - semiconductor	23
5	6505	Formosa Petrochemical	Chemical	21
6	2882	Cathay Holdings	Financial	19
7	1303	Nanya Plastic	Chemical	16
8	2881	Fubon Financial	Financial	16
9	1301	Formosa Plastic	Chemical	15
10	2308	Delta Electronics	Electronics – components	14
11	2002	China Steel	Steel	13
12	1326	Formosa Chemicals & Fiber	Chemical	12
13	3045	Taiwan Mobile	Telecommunications	11
14	3008	Largan Precision	Electronics – lens	10
15	2891	Chinatrust Group	Financial	10
16	2382	Quanta Computer	Electronics – PC	10
17	2886	Mega Financial Holding	Financial	10
18	2311	ASE	Electronics – semiconductor	9
19	1216	President Enterprise	Food & Beverage	9
20	2207	Hotai Motor	Automobile distributor	8

Source: Taiwan Stock Exchange

# **Project for Capacity Building of Capital Market in Mongolia: Investors' Roles**

---

29 April 2015

Daiwa Institute of Research  
Japan Economic Research Institute

## 1-a. Investors in Capital Markets

- A company may have different purposes for raising funds by different stages: establishment, expansion, stability, stagnation or reconstruction. Investor types may differ between stages.
- Different types of investors have different investment policies and strategies.

### **Establishment: growth stage**

- Companies often offer new stocks privately to their founders or their relatives to obtain initial equity capitals or working capitals at the initial stage.
- It is reasonable for new companies to raise funds in capital markets because they do not have enough credit or collaterals required for bank borrowings.

### **Enlargement: stability stage**

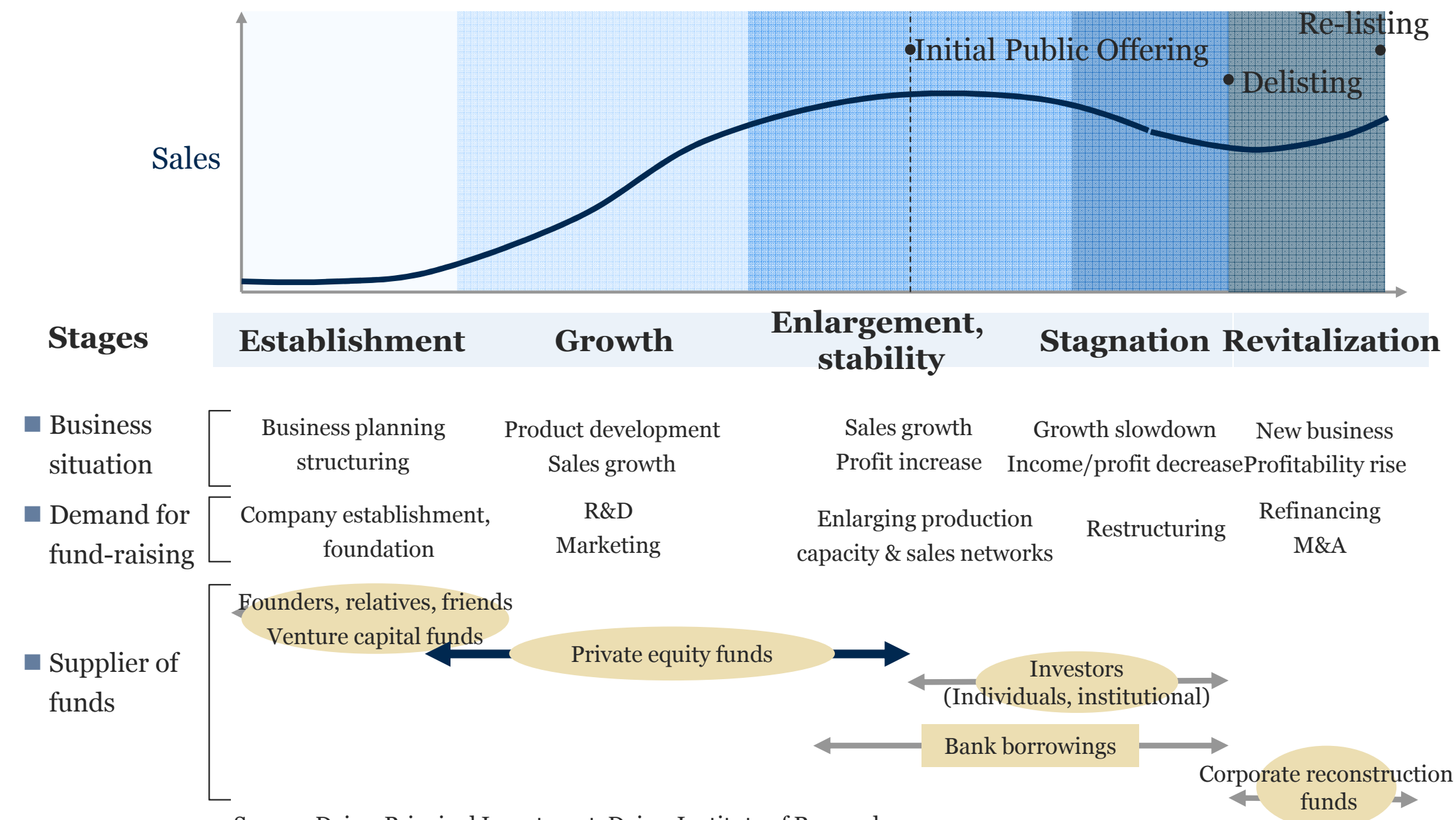
- Number of investors tend to increase after Initial Public Offering (IPO). Investors expect to receive capital gains and dividends.
- By this stage, both individual and institutional investors invest in shares. Individuals trade shares to increase their own assets whereas institutional investors invest their clients' assets and the size of investment is usually much larger than that of the individual.

### **Stagnation: revitalization stage**

- When the business performance falls steep or in some cases face bankruptcies, “revitalizing funds” may provide necessary finance for restructuring the business in exchange of stocks. Once the successful restructuring take place, revitalizing funds could expect capital gains by selling their re-listed shares or selling the business segment to another company.



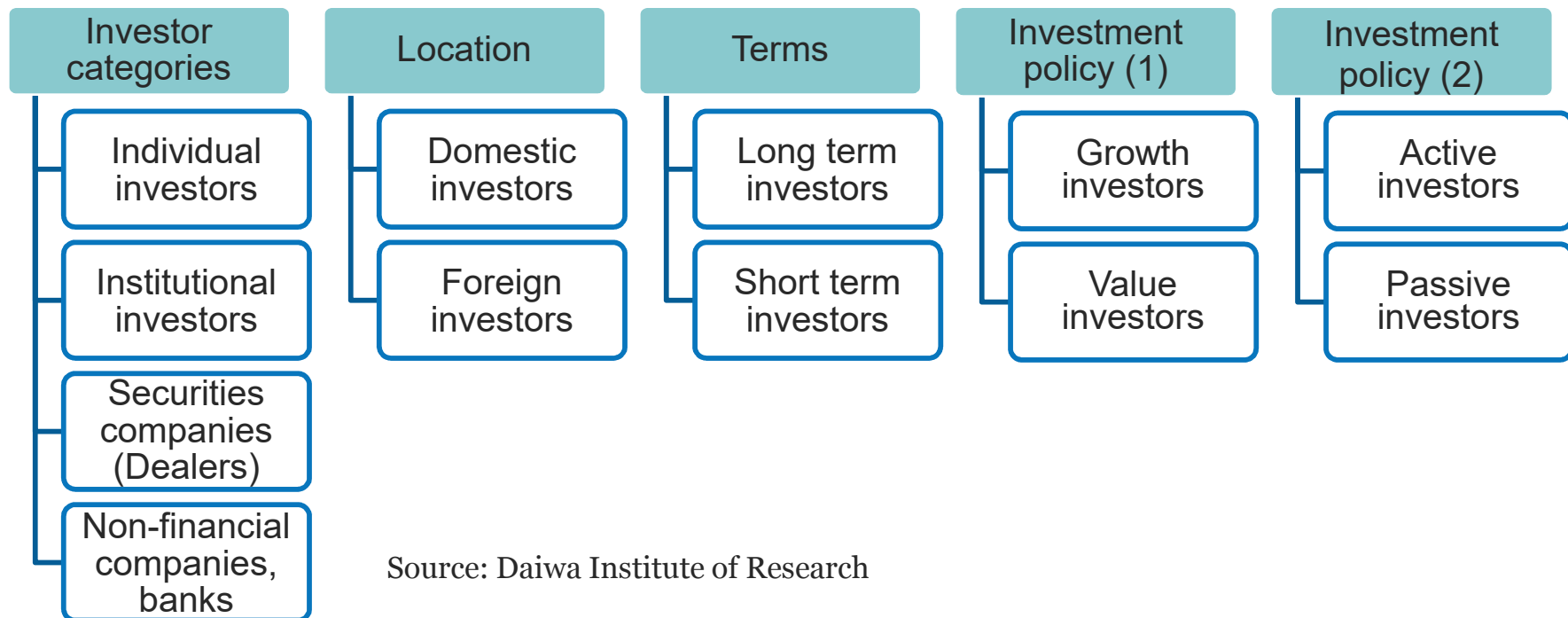
# 1-b. Company's development stages and investors



Source: Daiwa Principal Investment, Daiwa Institute of Research

## 1-c. Types of Investors

- Investors are mainly categorized to individual and institutional. Securities companies trade stocks on their own account (dealing). Non-financial companies and banks sometimes hold other companies stocks as a means of establishing business relationships.
- Recently, proportions of trade values of foreign investors are rising in Asian countries. Hence, their investment activities depend strongly to the changes in global investment climates.
- Some investors hold stocks for long term, some prefer short term investment based highly on daily price fluctuations.
- “Growth investors” focus more on the future business performances, while “value investors” prefer stocks with low-valued prices. “Active investors” target higher performance than the market indices, while “passive investors” aim the same performance with the market indices.

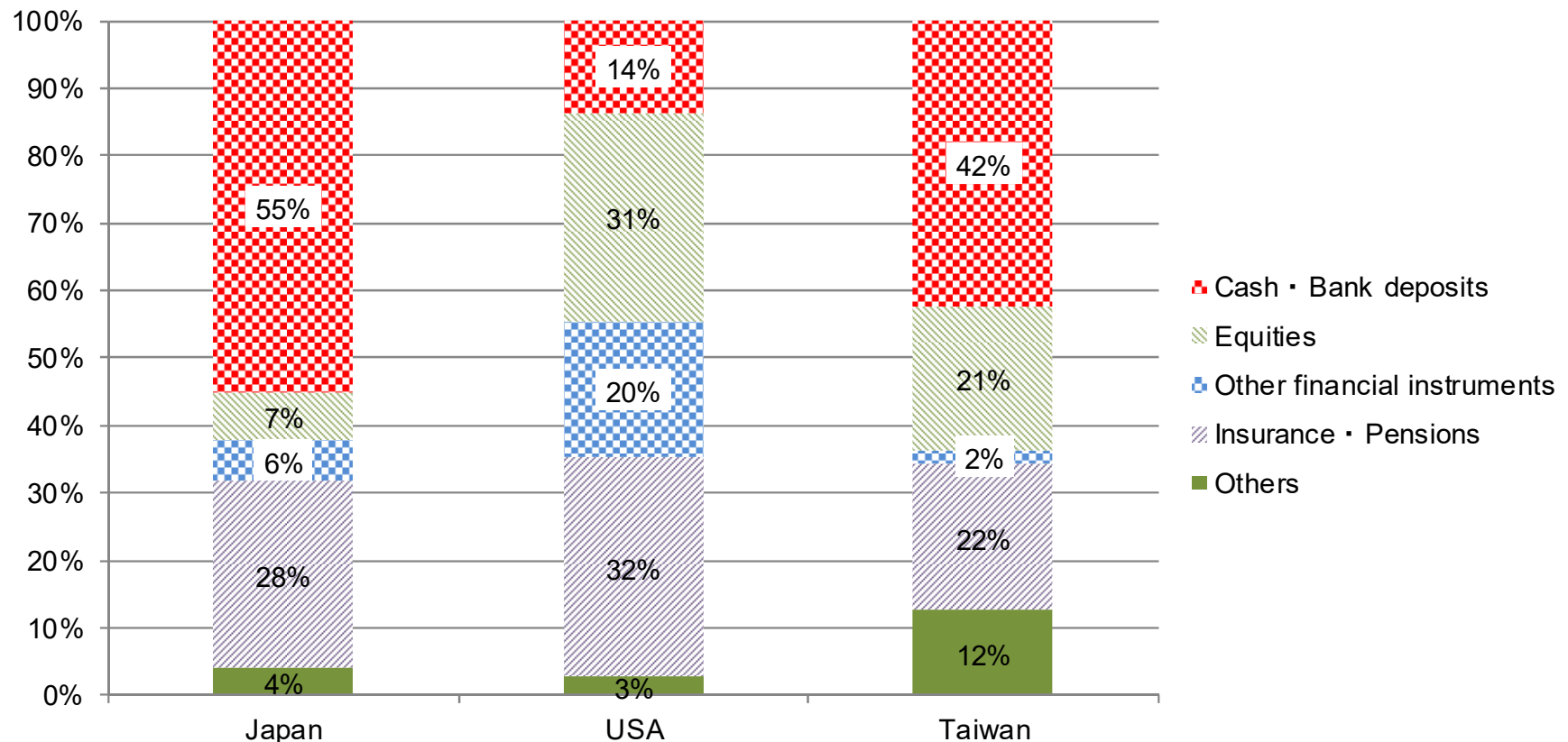


Source: Daiwa Institute of Research

## 2-a. Individual investors

- Individual investors invest their own assets thus investment size tend to be smaller.
- Recently, proportion of online trading is increasing. There are investors called “day-traders” who solely depend on online trading to make their livings.
- Japanese people are conservative. 55% of their asset consist of risk-free cash and deposits. Stocks only account for 7%. People in the USA or Taiwan are more positive for taking risks.

**Proportion of households' financial assets in Japan, USA and Taiwan, 2012**



Note: USA & Taiwan household data includes NGOs

Source: Bank of Japan, Federal Reserve Board, Central Bank of the Republic of China

## 2-b. Institutional investors (1) Categories

- “Institutional investors” are corporates who invest funds on behalf of their clients or on their own surplus money. Well known ones are insurance companies, investment trusts, pension funds, sovereign wealth funds, investment advisors.
- Their investment size are large. They usually hold various types of stocks. Some of them invest in nearly all stocks listed on the exchange, some also invest in foreign stocks and fixed income securities.
- They invest according to their own investment policies; short term / long term, growth investing / value investing, passive investing / active investing.

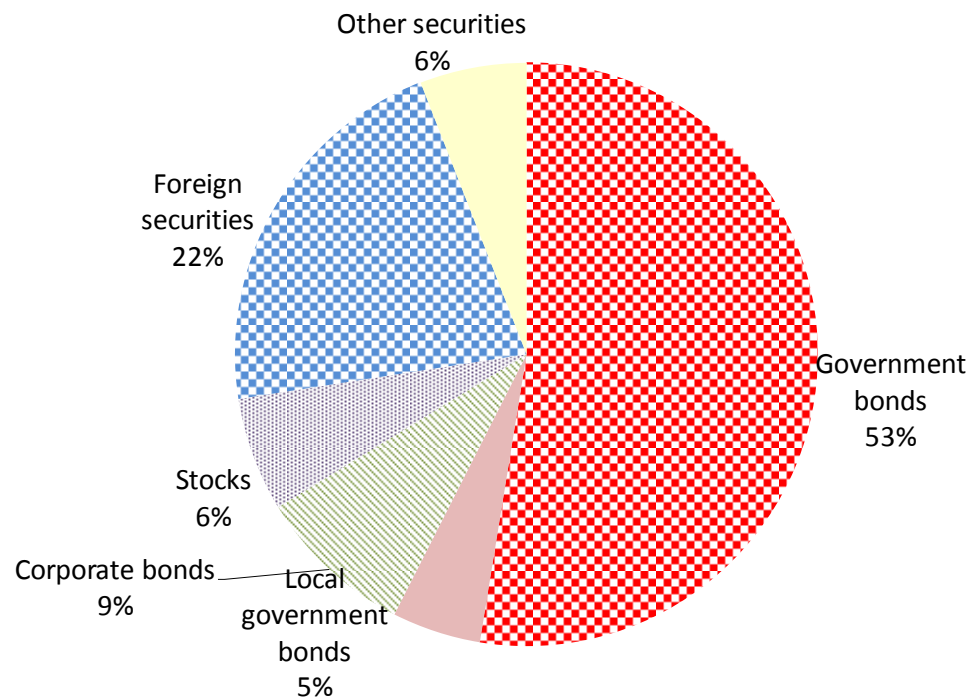
Major categories	Funds	Investment policy
Life insurance	Insurers' money	Mid- to long-term
General insurance	Insurers' money	Mid- to long-term
Mutual fund/investment trust/unit trust	Investors' invested money	Policies are defined by each financial product
Pension fund	Pensioners' money	Mid- to long-term
Sovereign wealth fund	National financial assets (foreign reserves etc.)	Differs by funds
Investment advisor	Clients' assets	Short-term
Hedge fund	Institutional and wealthy investors' money	Short-term

Source: Daiwa Institute of Research

## 2-b. Institutional investors (2) Life and general insurance companies

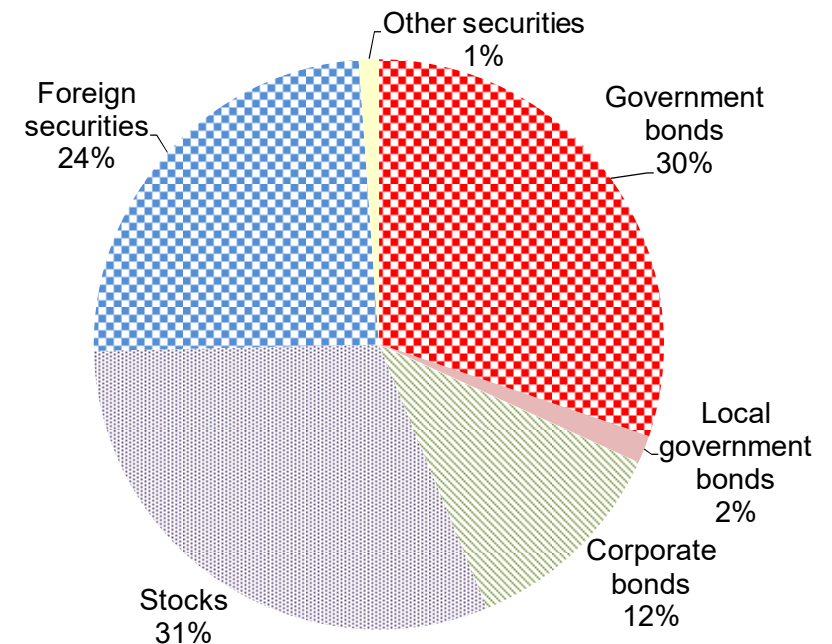
- There are life and general insurance companies.
- A life insurance product is on a super-long term. Therefore, long-term Government bonds (such as 30-year government bonds) take up a larger share in life insurers' portfolios than those of general insurance companies.

**Breakdown of securities portfolio by life insurance companies in Japan, end-March 2014**



Source: The Life Insurance Association of Japan

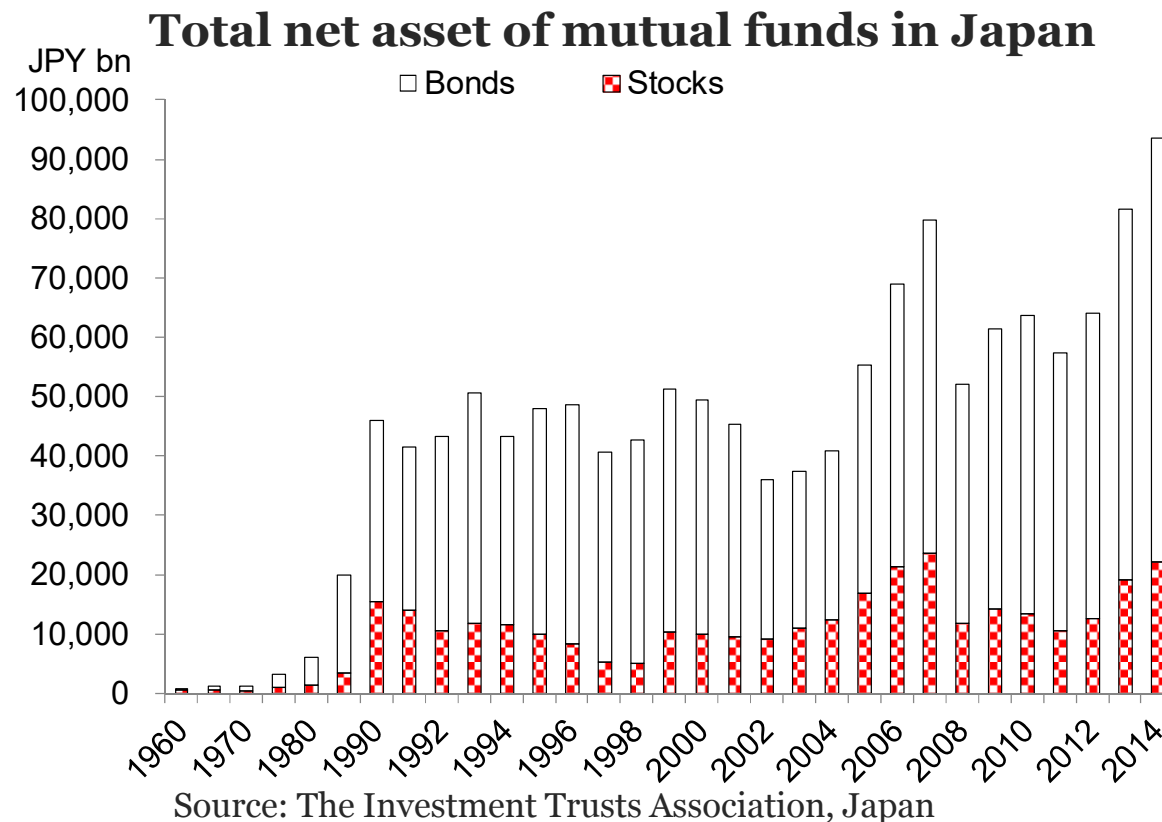
**Breakdown of securities portfolio by general insurance companies in Japan, end-March 2014**



Source: The General Insurance Association of Japan

## 2-b. Institutional investors (3) Mutual funds

- Mutual funds (unit trust/investment trust) accept funds from wide range of customers (mainly individual investors). Fund managers and portfolio managers, known as “professional investors”, invest the fund on behalf of their customers.
- According to their investment performance, dividends are paid to customers each fiscal year and funds are redeemed after a certain period.
- Investment trusts enable individuals to invest in smaller size of different stocks as opposed to buying individual stocks. They could also reduce risks by diverting their investments.

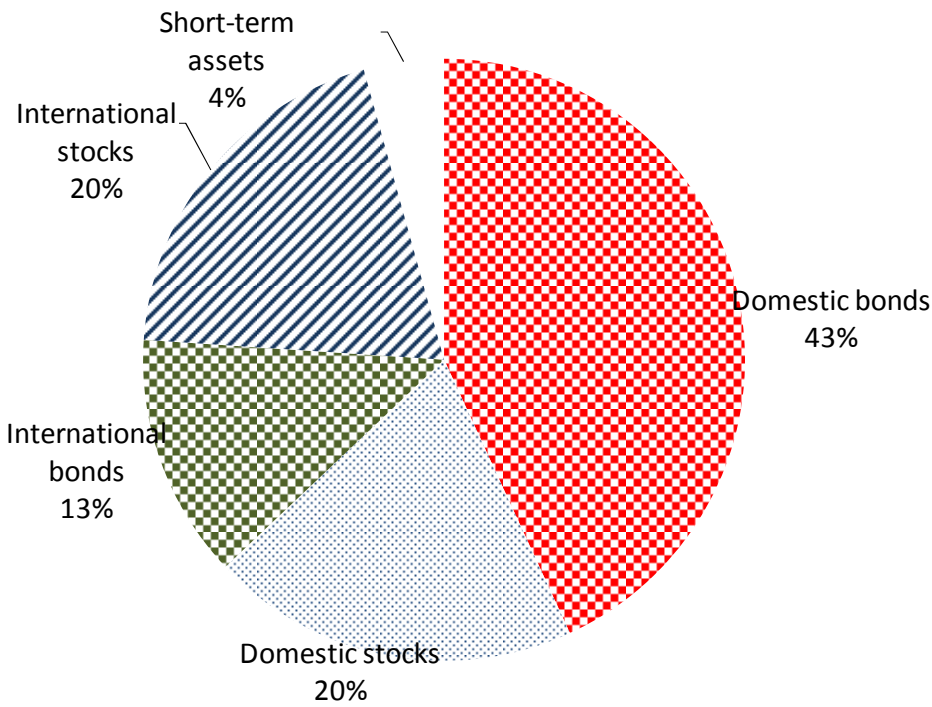




## 2-b. Institutional investors (4) Pension funds

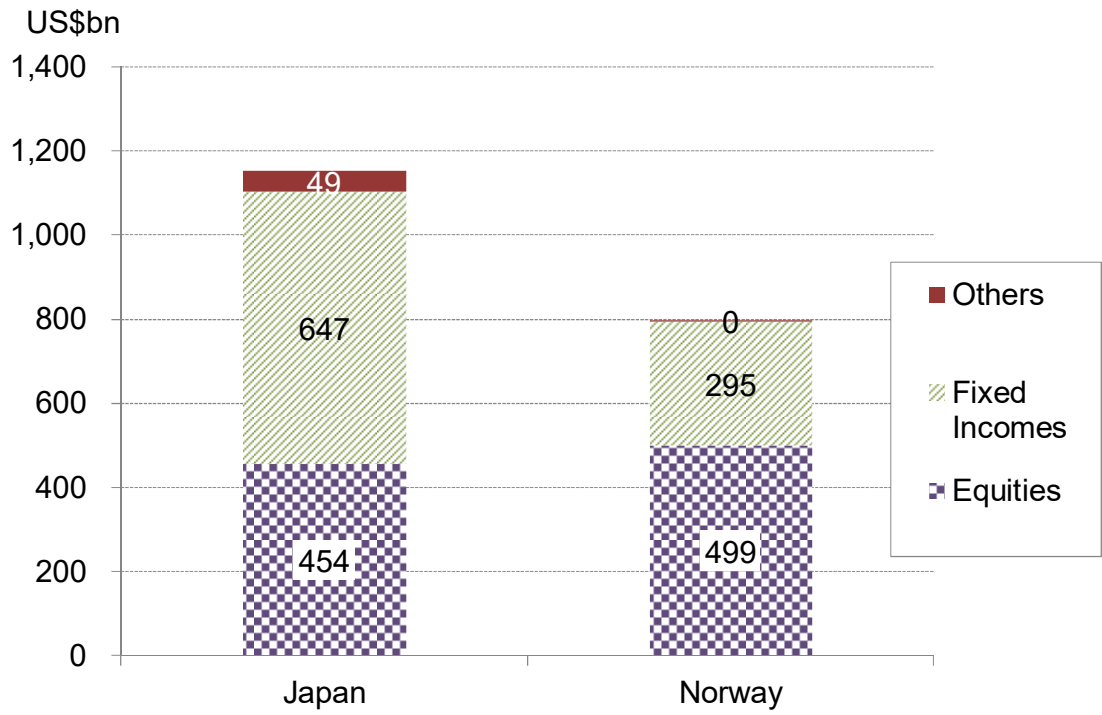
- Government Pension Investment Fund (GPIF) in Japan is the largest institutional investor in the World. More than half of the GPIF's portfolio consists of bonds, which is quite large compared to that of other pension funds.
- While the total assets managed by Norwegian Government Pension Fund Global (GPFG) is smaller than GPIF, GPFG's equity investment is much larger than GPIF. GPFG is considered to be an active investor, while GPIF is regarded as a passive investor.

**Asset proportion of GPIF in Japan  
(Dec 2014)**



Source: Government Pension Investment Fund

**Comparison of portfolio: Japanese GPIF (Sep 2014) and Norwegian GPFG (Dec 2014)**



Source: Government Pension Fund Global

## 2-b. Institutional investors (5) Sovereign wealth funds (SWF)

- Sovereign Wealth Funds (SWF) manage government funds and are recognized as an active investment type of investors. Natural-resource rich countries and countries with large amount of foreign reserves typically have SWFs. Recently, Middle Eastern countries and China have increased their assets under management by their SWF.

### Sovereign Wealth Fund Ranking

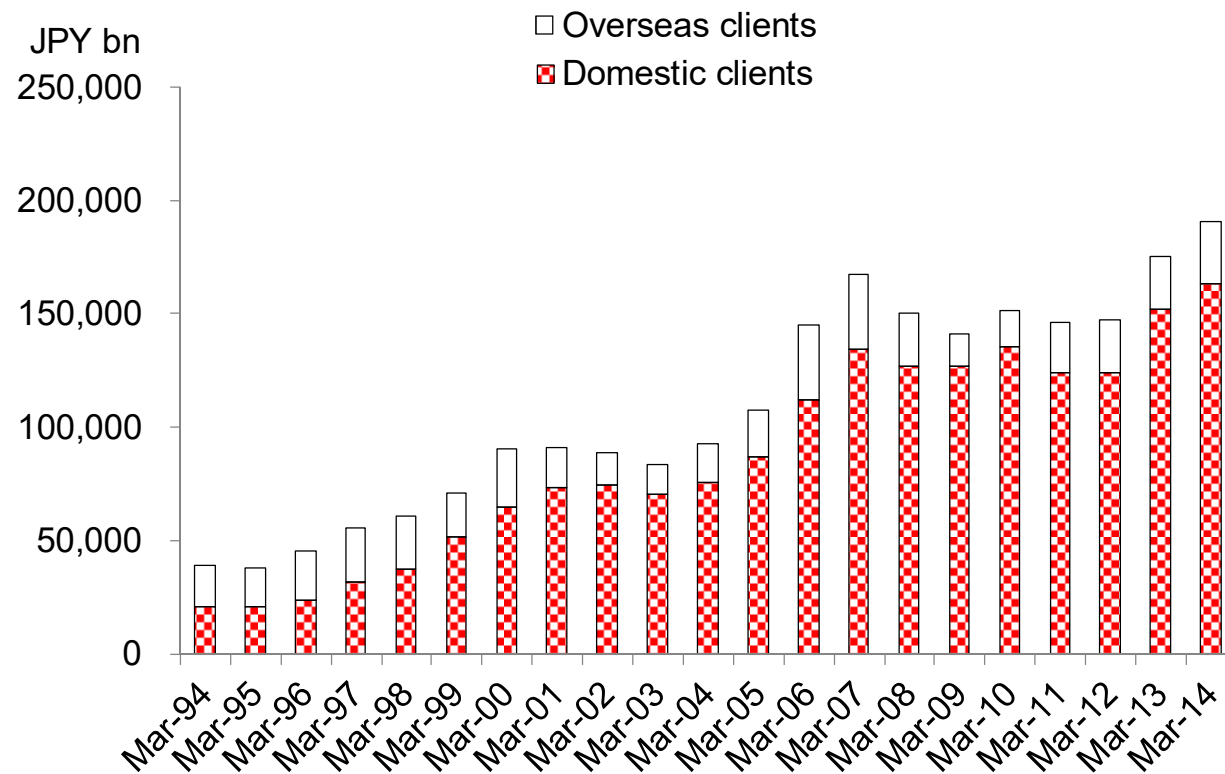
	Government	Assets US\$bn	Inception
Government Pension Fund – Global	Norway	863	1990
Abu Dhabi Investment Authority	UAE - Abu Dhabi	773	1976
SAMA Foreign Holdings	Saudi Arabia	757	n.a.
China Investment Corporation	China	652	2007
SAFE Investment Company	China	567	1997
Kuwait Investment Authority	Kuwait	548	1953
Hong Kong Monetary Authority Investment Portfolio	China – Hong Kong	400	1993
Government of Singapore Investment Corporation	Singapore	320	1981
Qatar Investment Authority	Qatar	256	2005
National Social Security Fund	China	236	2000

Source: SWF Institute

## 2-b. Institutional investors (6) Investment advisors

- Asset management companies or advisors manage assets on behalf of their clients (investors) based on investment discretion contracts. Usually, clients leave all investment decisions and the actual investments to the asset managers while some receive only the advisories but make investment decisions on their own.
- Public pension funds also seek investments and advisories from such asset managers.

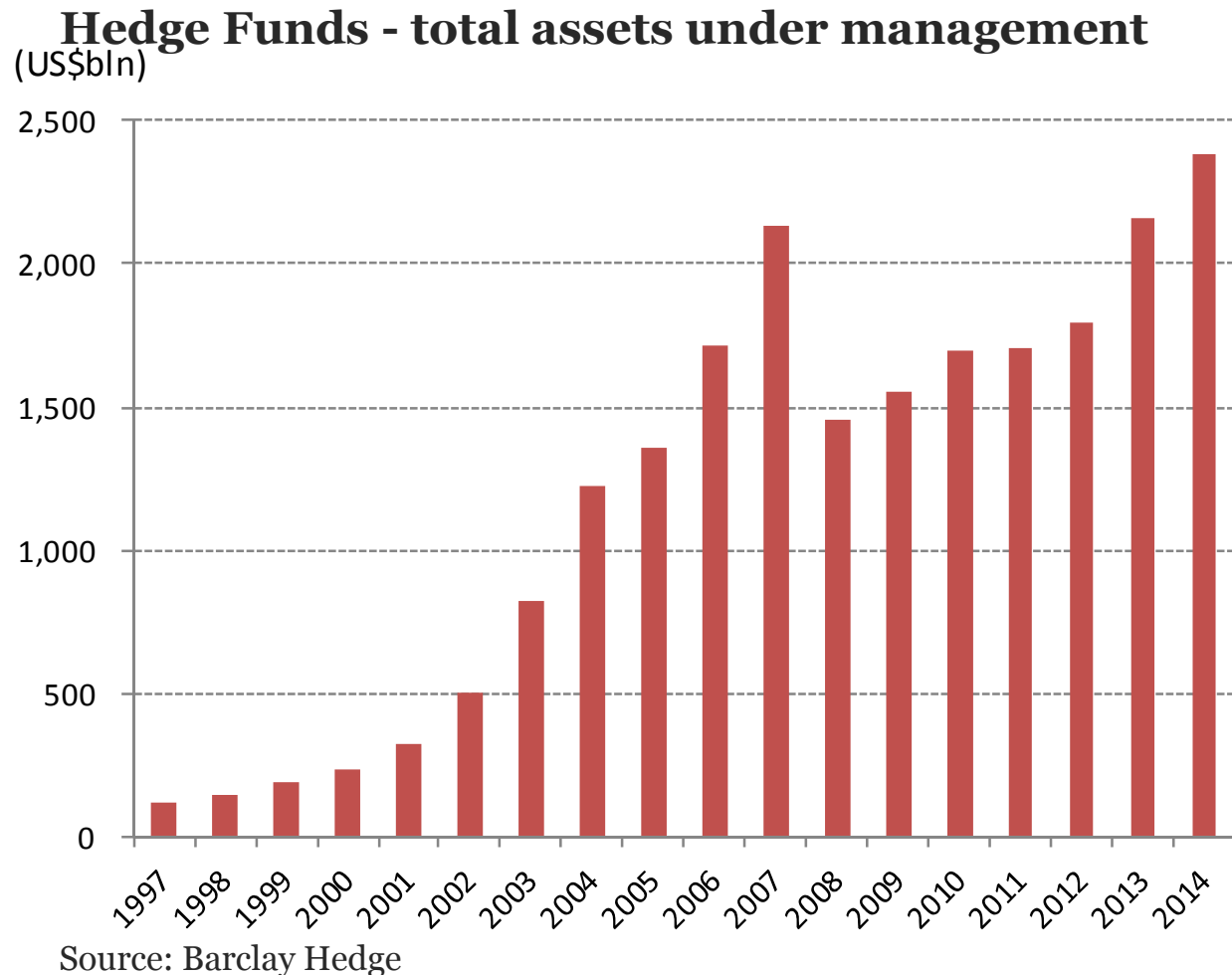
### Assets Under Management by Investment Management Members



Source: Japan Investment Advisors Association

## 2-b. Institutional investor (7) Hedge funds

- Hedge funds usually manage assets accumulated from institutional investors and wealthy households. They occasionally appear on news for being the key market makers.
- They are eager to achieve high return on investment through aggressive buy and short selling strategies.



## 2-c. Foreign investors

- Foreign investors are permitted to invest in many stock exchanges with certain limitations.
- With few exceptions, usually foreign investors are defined either institutional or retail.
- Foreign investors have high presence in recent years. In some stock exchanges, more than half of the transactions come from foreign investors.

### Presence and restrictions on foreign investors in selected ASEAN countries

Country	% of foreign investors (trading value)		Restriction on foreign investors
	2013	2014	
Thailand	22%	23%	Upper limit differ by listed companies but usually 49%. (Financial institutions 25%)
Vietnam	32%	n.a.	49% (Banks 30%)
Lao PDR	63%	69%	Determined by the government or else by the shareholders' meetings
Cambodia	n.a.	n.a.	None
Philippines	51%	49%	Limitation only for those listed on the negative list of foreign investments.
Indonesia	42%	41%	None

Source: various stock exchanges

## 2-d. Private equity funds and venture capital funds

- Private equity (PE) funds usually inject equity investments to non-listed companies and expect high return on investments by increasing the value of such companies through providing necessary management advisories as a majority shareholder. Typical PE funds spend 6-10 years per deal from initiating the fund to exiting by sharing profits to investors
- Venture capital also invests in an emerging (usually non-listed) companies but with smaller amount. In general, PE funds and venture capitals earn profits through selling equity shares.

**Global PE Funds Assets under Management (US\$bn)**

Company name	Location	Assets
Kohlberg Kravis Roberts	USA	46.7
TPG	USA	46.5
Blackstone Group	USA	41.7
Carlye Group	USA	40.6
CVC Capital Partners	UK	37.0
Apollo Global Management	USA	30.6
Bain Capital	USA	29.1
Goldman Sachs Merchant Banking Div.	USA	28.8
Apax Partners	UK	24.8
Adevent International	USA	21.7
Hellman & Friedman	USA	20.7
Permira	UK	18.0
Providence Equity Partners	USA	16.4
JC Flowers & Co	USA	14.4
Silver Lake	USa	14.1

Note: Total accumulated assets between 2000 and 2010

Source: Preqin



## 2-e. Revitalization funds

- Revitalization funds invest in a company that suffers stagnation. They provide funds as well as their know-hows for restructuring and try to improve management and company values.
- They could restructure the whole company or focus on particular department or operations.
- Their goal is to gain huge profit from selling their shares at an IPO or re-listing on a stock exchange.

### Restructuring Japan Airlines (JAL)

- In January 2010, JAL filed an application to the Enterprise Turnaround Initiative Corporation of Japan (ETIC) for support for restructuring. At the same time, JAL also filed the petitions for commencement of corporate reorganization proceedings with the Tokyo District court under the Corporate Rehabilitation Law.

- ✓ ETIC injected JPY350 bn
- ✓ Debt forgiveness (JPY520 bn)
- ✓ 100% reduction of capitals for the existing stocks

- ✓ Reduction of businesses
- ✓ Personnel reduction
- ✓ Reduction of labor costs
- ✓ Reduction of company pension
- ✓ Divestiture

	JPY bn			
	FY2009	FY2010	FY2011	FY2012
Income	1,494.8	1,325.0	1,222.9	1,273.3
Operating profit	-133.7	64.1	75.7	117.5

Returned to profitability in one year

Re-listed in September 2012 on TSE 1<sup>st</sup> section  
(ETIC sold its shares and completed its support)

Source: Enterprise Turnaround Initiative Corporation (ETIC)

### 3-a. Share price valuation (1) Price-earnings ratio (P/E)

Price - earnings ratio = share price / EPS (earnings per share)

EPS = Net income / total number of shares outstanding (period average)

Sugi Corp's FY2015 earnings forecast:

Revenues	MNT 100 million
Expenditures	MNT 70 million
Income before tax	MNT 30 million
Net income	MNT 20 million

Total number of shares: 100,000

Sugi Corp's EPS forecast for FY 2015  
= MNT 20 million / 100,000 shares  
= MNT **200**

(1) When Sugi Corp's share price is MNT 4,000  
P/E ratio = MNT 4,000 / MNT 200 = **20x**

(2) When Sugi Corp's share price is MNT 2,000  
P/E ratio = MNT 2,000 / MNT 200 = **10x**

- ✓ P/E ratio compares the current share price with its earnings.
- ✓ Whether the company's share price is trading at a premium or a discount is judged from the comparison with the P/E ratio of companies in the similar sector, or a historical range of its P/E ratios.
- ✓ P/E ratio trends may vary amongst sectors or the economic trends of the country and timing.

### 3-b. Share price valuation (2) Price-book ratio (P/B ratio)

Price - book ratio = share price / BPS (book value per share)

BPS = shareholders' equity (net assets) / total number of shares outstanding

Sugi Corp's FY2015 financial forecast

Total assets	MNT500 million
Liabilities	MNT300 million
Shareholders' equity	MNT200 million

Total number of shares: 100,000

BPS = MNT 200 million / 100,000 shares  
= MNT **2,000**

(1) When the share price is MNT 4,000  
P/B ratio = MNT 4,000 / MNT 2,000 = **2x**

(2) When the share price is MNT 2,000  
P/B ratio = MNT 2,000 / MNT 2,000 = **1x**

- ✓ P/B ratio is a ratio that is often used in a down cycle to judge downside potential of the a stock.
- ✓ When the P/B ratio is 1x or below 1x, it suggests that the price may be undervalued.

### 3-c. Share price valuation (3) Dividend yield

$$\text{Dividend yield (\%)} = \text{dividend per share} / \text{share price} \times 100$$

Sugi Corp's FY2015 dividend forecast

Dividend per share	MNT150
Share price	MNT4,000

(1) Dividend yield for Sugi Corp  
= MNT150 / MNT4,000 = **3.75%**

Urade Trading's FY2015 dividend forecast

Dividend per share	MNT100
Share price	MNT2,000

(2) Dividend yield for Urade Trading  
= MNT100 / MNT2,000 = **5.00%**

-> Investors can receive more dividends from Urade Trading when investing the same amount of money.

- ✓ Generally, dividend yields of companies in a growing stage are lower, some even pay no dividends (for example Microsoft did not pay any dividends until FY2003).
- ✓ On the other hand, there are cases where institutional investors claim more dividends against companies that profit growth become moderate or those have too much cash.

Source: Daiwa Institute of Research

# **Project for Capacity Building of Capital Market in Mongolia: The Roles of Securities Firms and the Implications**

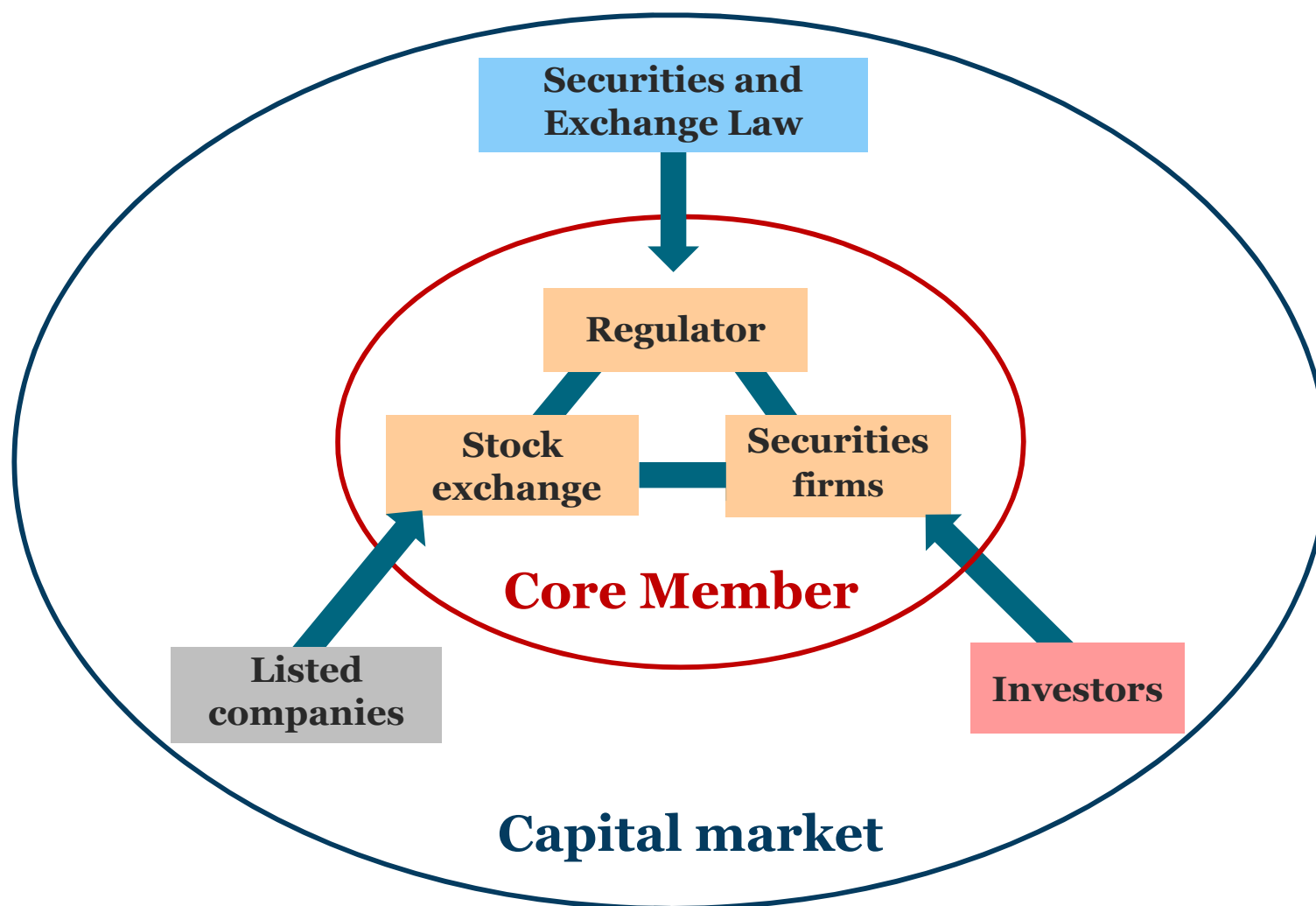
---

29 April 2015

Masa Igata, JICA Consultant

# Participants in capital markets

Without securities firms, the formation of the capital market will not happen. If no securities firms exist, companies cannot be listed on the stock exchange, and investors cannot be brought in.



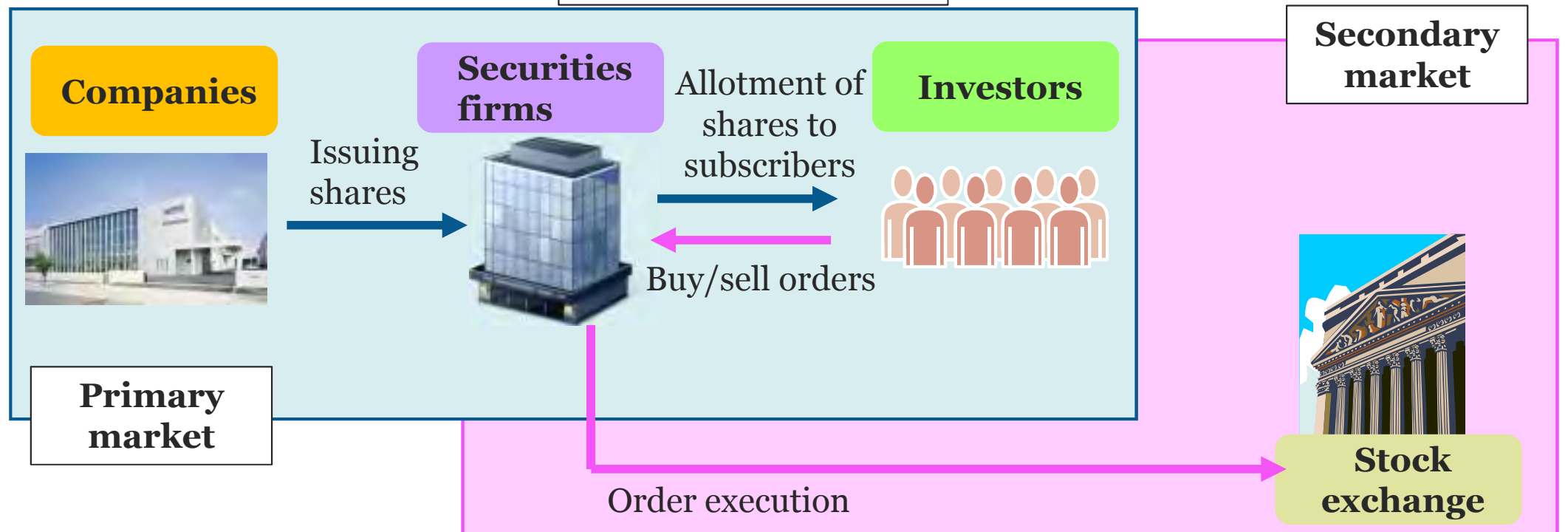
Source: Daiwa Institute of Research.



# The Function of securities firms

- 1) Capital markets consist of the primary market and the secondary market.
- 2) The primary market is where companies issue new shares, which are underwritten by securities firms, to sell to investors.
- 3) The secondary market is where an investor buys/sells shares from/to another investor by placing orders to a securities firm, which executes orders at the stock exchange.
- 4) Securities firms are involved both in the primary and the secondary market.

## Capital markets



# Categories of securities licenses and the Expectations of Sec firms

## The Securities and Exchange Law(2013)

The securities firms shall, after obtaining any type of license issued by Commission, have the **right** to operate the securities business permitted according to the type of license.

- (a) Securities dealing business license.
- (b) Securities brokerage business license.
- (c) Securities underwriting business license. etc

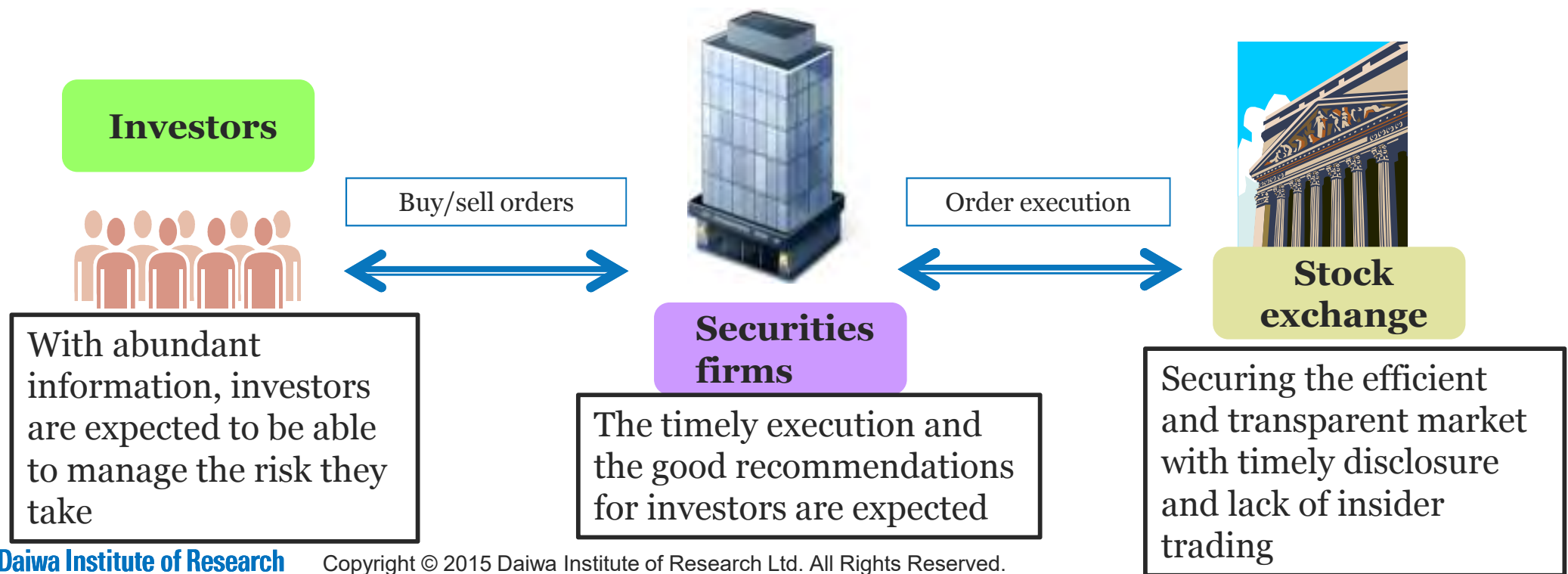
The business that licenses are given should be **reasonably profitable** for the securities firms to continue their business as their costs of complying with rules and regulations are higher than companies in the unregulated industries. Followings are some **guidelines** for international securities firms to conduct their business in a long run.

1. The **market capitalization**: The minimum 300mil USD for analyst coverage and 1billion USD for underwriting business are generally accepted rule of thumb of **doing business** for international securities firms.
2. The **liquidity of the market**: In addition, at least 25% of float ratio and certain amount of shareholders should be maintained to secure **active trading** at secondary market.

Even in Japan, only around **10%** of the listed companies are **properly covered** by bankers and brokers at securities firms. In case of Mongolia, **none** of the listed firms are eligible for being properly covered by any reputable international securities firms.

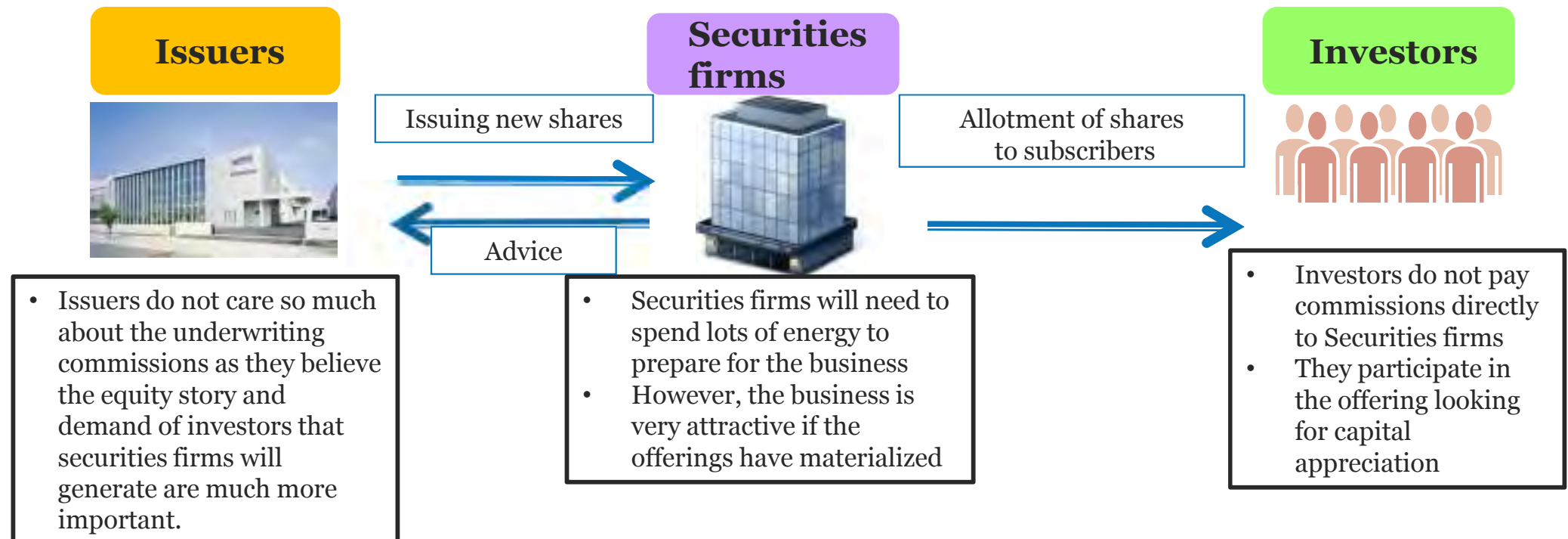
# Brokerage business

- 1) If you want to buy or sell shares of a listed company, you place orders to securities firms.
- 2) You cannot place orders directly to the stock exchange. Securities firms act as intermediaries to execute orders on behalf of investors at the stock exchange.
- 3) Securities firms are paid brokerage commissions by investors.
- 4) Commissions vary based on commission rate and amount of transactions.
- 5) Due to the decline of the commission rate globally in the last few decades, traditional securities firms are less dependent on this business. More market share are taken by internet brokers and smaller local brokers who do not pay so much cost to account maintenance.



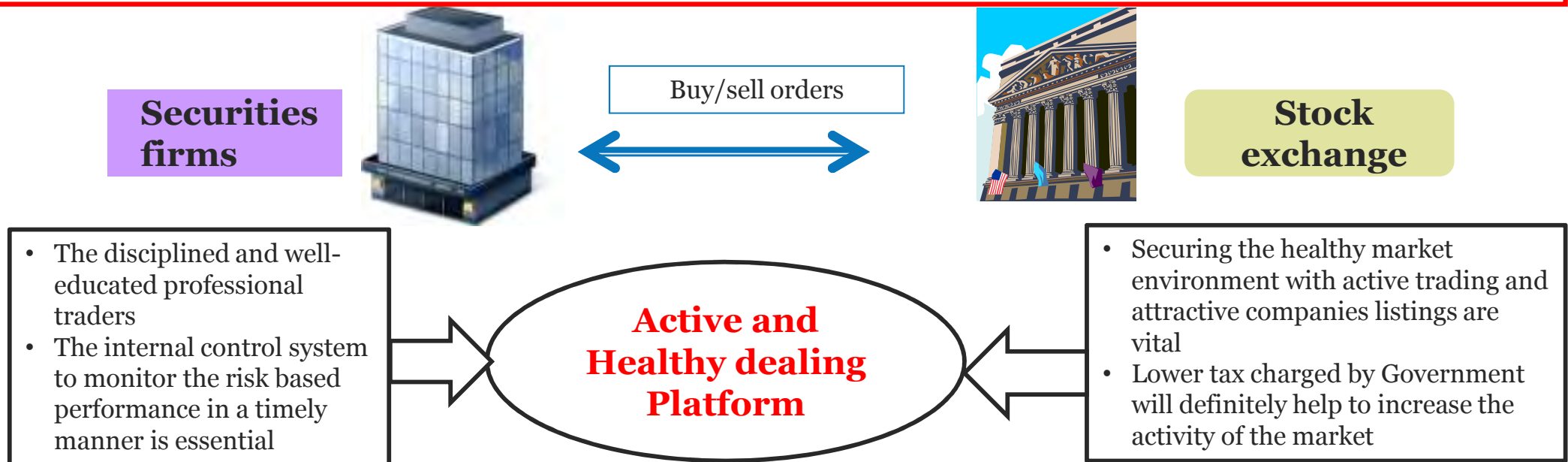
# Underwriting business

- 1) Securities firms advise targeted issuers for their IPO process (listing application, pricing etc.)
- 2) Securities firms buy newly issued shares from issuers (underwriting).
- 3) Given that securities firms take risks of underwriting, issuers for shares or bonds pay underwriting commissions to securities firms.
- 4) Underwriting commissions fluctuate depending on number of issuers doing IPO and fee charged to each issuer.
- 5) Underwriting commission rate remains to be fat because the business is concentrated by small number of big securities firms who have experience and expertise. However, the business can be influenced by the market.



# Dealing business

- 1) Only major securities firms have the dealing business section.
- 2) Dealing means buying and selling shares or bonds on their own account. In other words, securities firms act as investors in the market.
- 3) Securities firms sometimes can gain huge profit from their dealing activities, but they might make huge losses as well depending on stock market conditions and their buy/sell decisions.
- 4) As brokerage business has become thin margin business in major capital markets, brokers tend to seek higher profits doing dealing business recently. However, whether brokers can make profits depends on market direction and trading techniques. In addition, securities firms normally seek for short term profits. Hence, liquidity of the market is essential for them to enter into this business.



# Advisory business

## M&A

- Advise on acquisitions for enhancing corporate value.
- Acquisition, a means of business expansion or entry into new field.

- Only small number of Invest Bankers can make satisfactory service to the clients.
- As they can access to the very high level of corporate secrets, certain rules and regulations are required.

## Business tie-ups

Advise on business tie-ups for enhancing corporate value, which could entail equity alliances.

## Dividend/capital policy

Advise on dividend policy, new share issues, secondary offerings by existing shareholders, to reward shareholders adequately and to maximize corporate value.

**Wide range of expertise and experience with high ethical standard will be required.**



**Securities firms**

**Companies**



**Management advice**  
(drawing up mid-term business plans/  
incentive programs)

Advise on business policies or performance-based pay system to encourage further corporate growth.

## Timely disclosure

Advise on prompt and accurate corporate disclosure

- More and more companies realize the importance of enhancing corporate value.
- They believe raising capital effectively will be key to win in the market.

## Investor relations

Propose and advise on investor relations programs, which report business conditions to shareholders, introduce corporate strengths to potential investors.



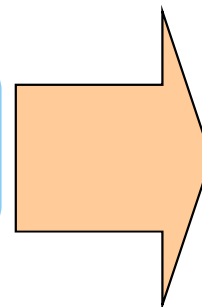
# Contributions by securities firms

---

**1) Support equity financing for issuers and advise for investors' wealth**

**2) Developing government bond market**

**3) Financial support for social issues**

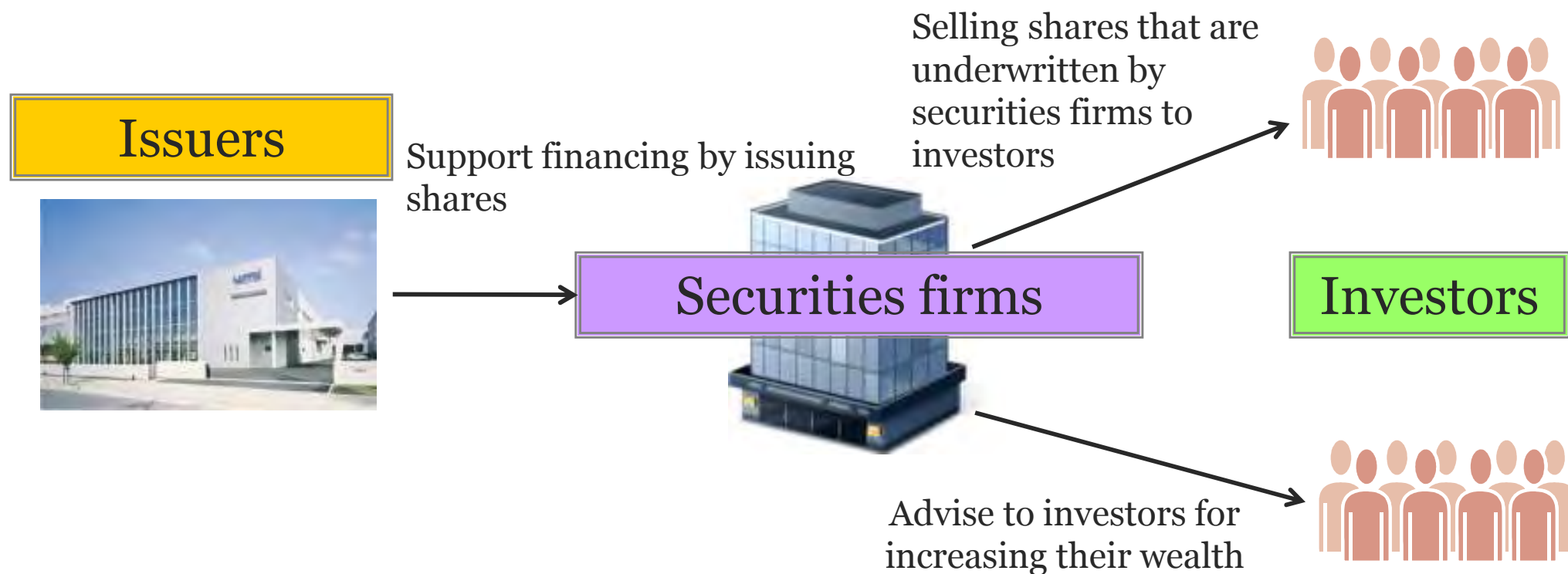


**Contributions to economic growth by securities firms**

**As the regulator, it is important to secure the **attractive and healthy platform** for them**

## Support equity financing for corporates and advise for investors

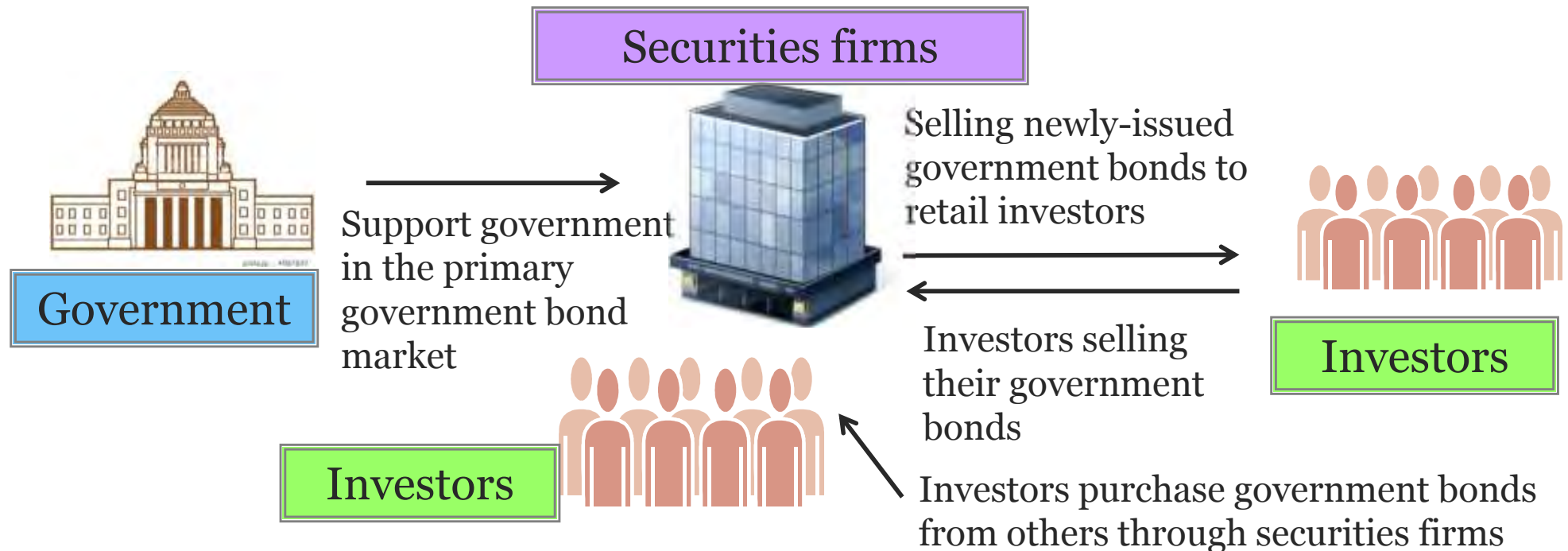
Issuers are able to obtain cash by issuing shares at attractive cost, with help of bankers at securities firms. As a result of financing, issuers can increase their operational capacity. In addition, brokers at securities firms can provide advices to investors.



# Developing government bond market

Securities firms can help develop the government bond market. Government needs to continuously issue government bonds for financing its public sector projects, and securities firms purchases newly-issued government bonds for investors. In addition, securities firms play a role as brokers for government bond holders including banks and other institutional investors, if investors need to trade.

Government bonds prices are variable with the result that investors may incur losses. Sales representatives must have sufficient knowledge to deal with this, in other words, government bonds should be handled by securities firms.



Government Bond is very important for capital market at this moment because of the high demand of issuing the bond and interest to participate into the deal from investors in public sector in foreign countries. However, securing the transparency and timely disclosure of the money being spent are not properly done for the previous bond. Therefore, monitoring the issuance of the bond is important for the success of the future issuance.

# Financial support for social issues

Social bonds	Issues	Use of funds
Microfinance bonds	Poverty	Financing for microfinance institutions
Poverty reduction bonds	Poverty	Poverty reduction
Green bonds	Global warming	Reduce global warming
Ecology bonds	Global warming	Renewable energy and low-power consumption projects
Vaccine bonds	Medical	Vaccine for kids in low-developed countries
Water bonds	Water	Water treatment
Education bonds	Education	Support educational programs for low-income public

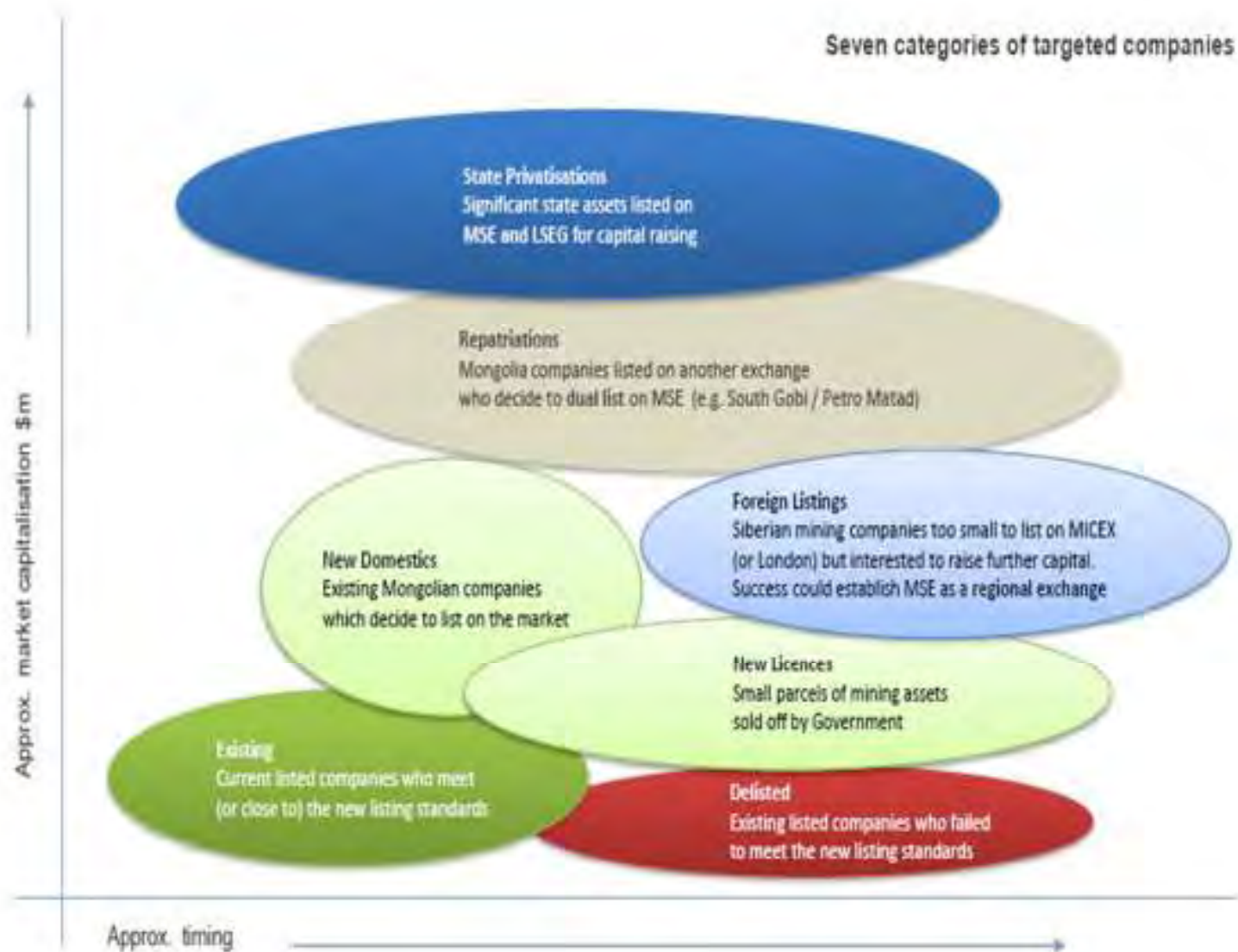
Securities companies also propose to international organization to issue

particular bonds for tackling social issues and promote to investors.



The challenges are 1. the potential size of the issuance is too small for international investors. 2. investors are mainly social funds and multi-national agencies. So, fostering the environment to encourage local companies to establish the fund should be considered.

# PROFILE OF TARGET LISTED COMPANIES



## TOP-10 Local Cos of year 2014

1	Erdenet LLC
2	MCS group
3	Khan bank
4	Mobicom Corporation
5	Trade and Development bank
6	Golomt bank
7	XAC Bank
8	MAK LLC
9	NIC LLC
10	Sod Mongol Group LLC

Source: Chamber of Commerce, Mongolia

Source: Presentation by Mongolian Stock Exchange, 2014

# **Project for Capacity Building of Capital Market in Mongolia: 'Finance 101'**

---

April 30, 2015

Daiwa Institute of Research  
Japan Economic Research Institute



## **1. Financial Statement Analysis**

- Structure of Financial Statements
- Key Points of Financial Statement Analysis
- Ratio Analysis (Profitability, Stability, Efficiency, Growth)
- Other Analysis Methods
- Window, Dressing

## **2. Corporate Finance**

- Objectives
- Investment Decision Making
- Equity Financing vs Debt Financing
- Financing Decision
- Corporate Finance vs Project Finance

## **3. Relevant Issues**

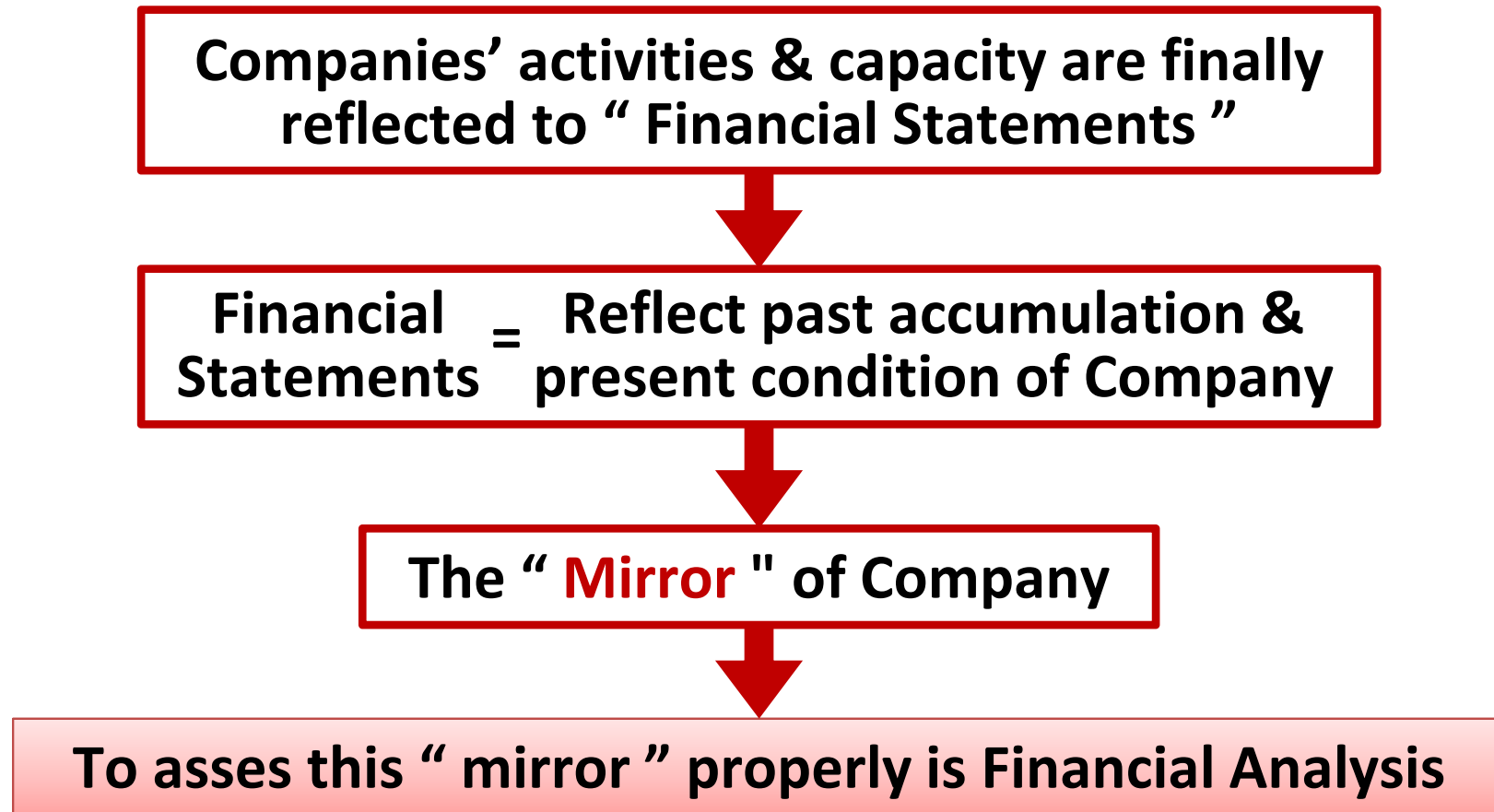
- PPP
- Privatization

# **1. Financial Statement Analysis**

---

## Why Analyze Financial Statements ? (1)

---



(Major Financial Statements)

- ✓ **Balance Sheet (B/S)**
- ✓ **Income (or Profit & Loss) Statement (I/S or P/L)**
- ✓ **Cash Flow Statement**

## Why Analyze Financial Statements ? (2)

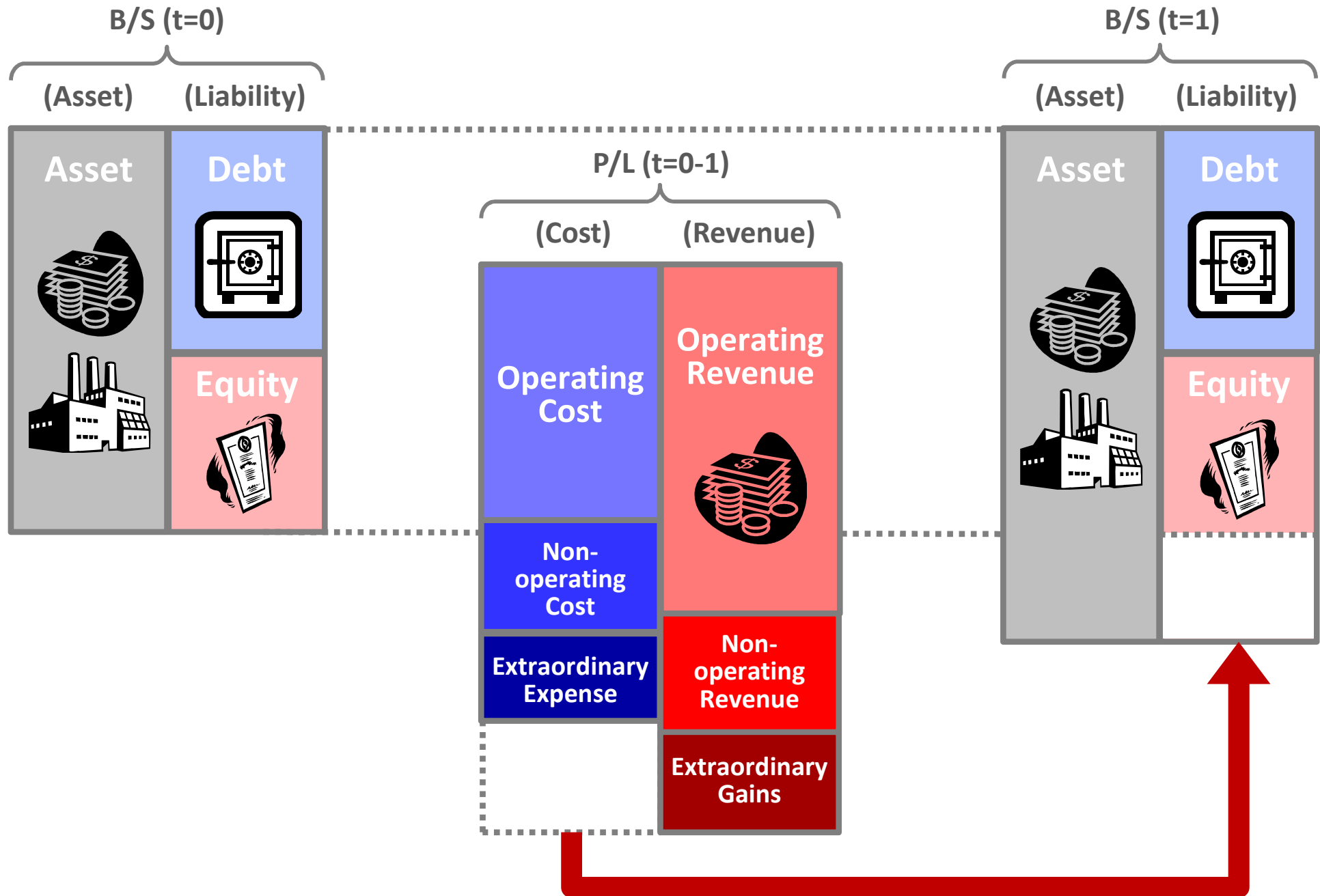
---

Financial statements are used for financial analysis to understand the company's present strengths & weaknesses through its activities & capacity.

There are several objectives of financial analysis:

User	Purpose
Corporate managers	To formulate management strategies
Financial managers	To make investment/fund raising decisions
Banks	To examine the creditability of customers (credit analysis)
Investors	To investigate possible acquisitions

# Structure of Financial Statements



# Structure of Financial Statements: B/S (1)

Prepared to show **financial situation** as of the end (=closing date) of the accounting period

(Unit Million JPY)

		FY2009	FY2010	FY2011			FY2009	FY2010	FY2011
<b>Assets</b>					<b>Liabilities</b>				
<b>Current Assets</b>		5,279,382	5,580,410	6,345,835	<b>Current Liabilities</b>		3,988,694	3,856,858	4,380,545
	Cash	3,632,714	802,410	998,822		Account payable	621,904	1,001,287	1,181,469
	Accounts Receivables	429,078	641,154	738,950		Short-term borrowings	660,956	349,427	593,095
	Securities	126,968	50,641	158,012		current portion of long term borrowings	770,494	695,655	933,976
	Inventory	760,070	802,278	982,233		Commercial paper	639,152	174,393	256,601
	Other	429,228	3,375,380	3,549,773		current portion of bonds	220,884	407,130	87,280
	Allowance for Doubtful	(98,676)	(91,453)	(81,955)		Others	1,075,304	1,228,966	1,328,124
<b>Fixed Assets</b>		4,960,158	4,634,410	4,390,858	<b>Long term liabilities</b>		3,324,793	3,342,857	3,082,365
	Property, Plant and	4,110,047	3,858,129	3,637,042		Bonds	595,309	507,142	640,850
	Buildings	668,943	679,829	645,414		Long term borrowings	1,700,015	1,791,983	1,422,478
	Machinery	2,149,693	1,980,991	1,841,480		Others	1,029,469	1,043,732	1,019,037
	Land	688,704	675,029	659,985	<b>Total Liabilities</b>		7,313,487	7,199,715	7,462,910
	others	602,707	522,280	490,163	<b>Net Assets</b>				
	Intangible Fixed Assets	167,218	143,911	133,769		Shareholders' Equity	3,556,479	3,598,966	3,981,513
	Investment and other assets	682,893	632,370	620,047		Accumulated other	(930,846)	(891,615)	(1,040,098)
						others	300,420	307,754	332,368
<b>Total Assets</b>		10,239,540	10,214,820	10,736,693	<b>Total Net Assets</b>		2,926,053	3,015,105	3,273,783
					<b>Total Liabilities and Net Assets</b>		10,239,540	10,214,820	10,736,693

(source : Nissan Motor Co., Ltd)



## Structure of Financial Statements: B/S (2)

- Good Assets on the left side (**debit**), and Bad Assets & Net Assets on the right side (**credit**) of the balance sheet

Assets	Liabilities
	Equity

$$\text{Assets} = \text{Liabilities} + \text{Equity}$$

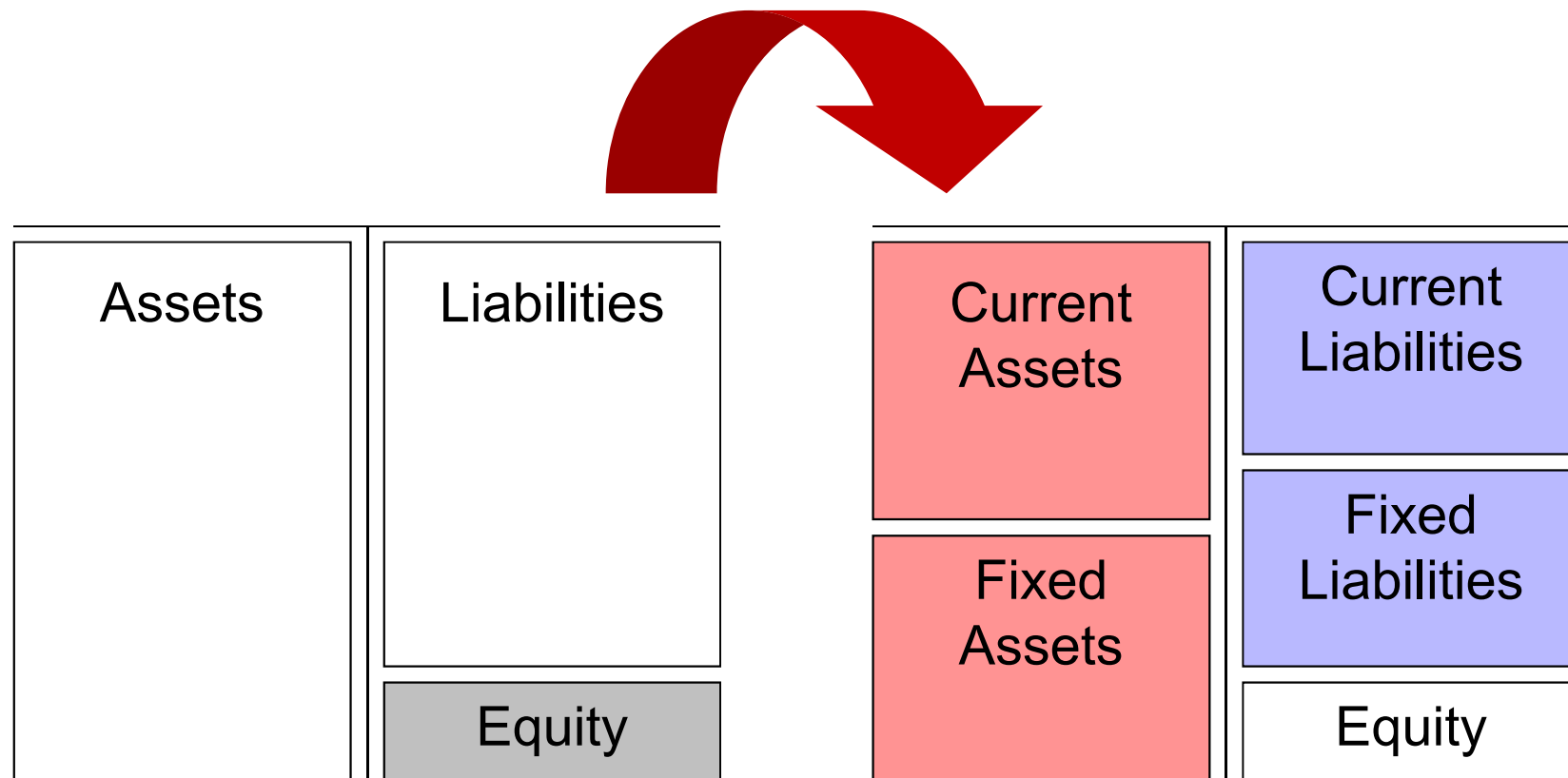
- 「**Assets**」・・・Good assets  
(Ex) Cash, goods, equipment
- 「**Liabilities**」・・・Bad assets  
(Ex) borrowings
- 「**Capital**」・・・Net assets  
(Ex) Share capital, Retained earnings

## Structure of Financial Statements: B/S (3)

---

The left side (Debit) : shows how you spent money

The right side (Credit): shows how you collect money



Assets = Current Assets + Fixed Assets

Liabilities = Current Liabilities + Fixed Liabilities

## Structure of Financial Statements: B/S (4)

The point to divide current/fixed is **one year**



**One Year Rule**

(Unit Million JPY)

	FY2011		FY2011
<b>Assets</b>		<b>Liabilities</b>	
<b>Current Assets</b>	<b>6,345,835</b>	<b>Current Liabilities</b>	<b>4,380,545</b>
Cash	998,822	Account payable	1,181,469
Accounts Receivables	738,950	Short-term borrowings	593,095
Securities	158,012	current portion of long term borrowings	933,976
Inventory	982,233	Commercial paper	256,601
Other	3,549,773	current portion of bonds	87,280
Allowance for Doubtful	(81,955)	Others	1,328,124
<b>Fixed Assets</b>	<b>4,390,858</b>	<b>Long term liabilities</b>	<b>3,082,365</b>
Property, Plant and	3,637,042	Bonds	640,850
Buildings	645,414	Long term borrowings	1,422,478
Machinery	1,841,480	Others	1,019,037
Land	659,985	<b>Total Liabilities</b>	<b>7,462,910</b>
others	490,163	<b>Net Assets</b>	
Intangible Fixed Assets	133,769	Shareholders' Equity	3,981,513
Investment and other assets	620,047	Accumulated other	(1,040,098)
		others	332,368
<b>Total Assets</b>	<b>10,736,693</b>	<b>Total Net Assets</b>	<b>3,273,783</b>
		<b>Total Liabilities and Net Assets</b>	<b>10,736,693</b>

Current assets:  
cash, accounts  
receivable,  
inventories, etc.  
→ Convertible into cash  
within one year

Fixed assets:  
building, equipment,  
(right to use) land, etc.  
→ Useful life more than  
one year

Current liabilities:  
accounts payable,  
short, term debt, etc.  
→ Payment due within  
one year

Fixed liabilities:  
Long, term debts/  
bonds, etc.  
→ Repayment due later  
than one year

(source : Nissan Motor Co., Ltd)

## Structure of Financial Statements: P/L (1)

P/L are prepared to show  
the results of operations (Revenue – Expenses = Profit)  
 for the year ended the closing date.

Unit : Million JPY

	FY2009	FY2010	FY2011
<b>Net Revenues (Sales)</b>	8,436,974	7,517,277	8,773,093
- <b>Cost of Sales</b>	7,118,862	6,146,219	7,155,100
<b>Gross Profit</b>	1,318,112	1,371,058	1,617,993
- <b>Selling General and administrative expenses</b>	1,456,033	1,059,449	1,080,526
<b>Operating Income</b>	▲ 137,921	311,609	537,467
+ <b>Non operating income</b>	38,121	29,126	86,603
- <b>Non operating expenses</b>	72,940	132,988	86,256
interest expense	33,798	28,995	28,357
<b>Ordinary Income</b>	▲ 172,740	207,747	537,814
+ <b>Special gains</b>	62,156	20,552	27,989
- <b>Special losses</b>	108,187	86,679	85,662
<b>Income before income taxes and others</b>	▲ 218,771	141,620	480,141
- <b>Income taxes and others</b>	14,938	99,230	160,920
<b>Net Income</b>	▲ 233,709	42,390	319,221

(source: NissanMotor Co., Ltd)

## Structure of Financial Statements: P/L (2)

- Revenue on the right side (**credit**), and Expenses & Profit on the left side (**debit**) of the P/L
- P/L shows how profits are generated.

Expenses	Revenue
Profit	

$$\text{Revenue} - \text{Expenses} = \text{Profit}$$

- 「**Revenue**」・・・Resources of Profit  
e.g. sales
- 「**Expenses**」・・・Items required to acquire profit  
e.g. cost of sales, rents, salaries
- 「**Profit**」・・・Revenue－Expenses > 0
- 「**Loss**」・・・Revenue－Expenses < 0

# Structure of Financial Statements: P/L (3)

## Five Stages of Profits

1. **Gross Profit;**  
→ Sales minus the cost of Sales
2. **Operating Profit;**  
→ Income by main profession
3. **Ordinary Profit;**  
→ Consider non,operating accounts  
after Operating Profit
4. **Profit before Taxes;**  
→ Consider extraordinary accounts after  
Ordinary Profit
5. **Net Profit;**  
→ Income less all expenses

Unit : Million JPY

		FY2011
Net Revenues (Sales)		8,773,093
-	Cost of Sales	7,155,100
Gross Profit		1,617,993
-	Selling General and administrative expenses	1,080,526
Operating Profit		537,467
+	Non operating income	86,603
-	Non operating expenses	86,256
	interest expense	28,357
Ordinary Profit		537,814
+	Special gains	27,989
-	Special losses	85,662
Profit before income taxes and others		480,141
-	Income taxes and others	160,920
Net Profit		319,221

(source: NissanMotor Co., Ltd)





# Key Points of Financial Statement Analysis (1)

## After seeing the Forest, checking the Woods

1. To check the sales figure
2. To check the profit level
3. To check the equity
4. To check the repayment capacity

	FY2011
Net Revenues (Sales)	8,773,093
- Cost of Sales	7,155,100
Gross Profit	1,617,993
- Selling General and administrative expenses	1,080,526
Operating Profit	537,467
+ Non operating income	86,603
- Non operating expenses	86,256
Interest expense	28,357
Ordinary Profit	537,814
+ Special gains	27,989
- Special losses	85,662
Profit before income taxes and others	480,141
- Income taxes and others	160,920
Net Profit	319,221

(Unit Million JPY)

	FY2011		FY2011
<b>Assets</b>		<b>Liabilities</b>	
<b>Current Assets</b>	6,345,835	<b>Current Liabilities</b>	4,380,545
Cash	998,822	Account payable	1,181,469
Accounts Receivables	738,950	Short-term borrowings	593,095
Securities	158,012	current portion of long term borrowings	933,976
Inventory	982,233	Commercial paper	256,601
Other	3,549,773	current portion of bonds	87,280
Allowance for Doubtful Accounts	(81,955)	Others	1,328,124
<b>Fixed Assets</b>	4,390,858	<b>Long term liabilities</b>	3,082,365
Property, Plant and equipment	3,637,042	Bonds	640,850
Buildings	645,414	Long term borrowings	1,422,478
Machinery	1,841,180	Others	1,019,037
Land	659,985	<b>Total Liabilities</b>	7,462,910
others	490,163	<b>Net Assets</b>	
Intangible Fixed Assets	133,769	Shareholders' Equity	3,981,513
Investment and other	620,047	Accumulated other	(1,040,098)
		others	222,368
<b>Total Assets</b>	10,736,693	<b>Total Net Assets</b>	3,273,783
		<b>Total Liabilities and Net Assets</b>	10,736,693

(source : Nissan Motor Co., Ltd)

## Image the company

## Key Points of Financial Statement Analysis (2)

### Balance Sheet

- Account fluctuations
- Relation between Sales and Account Receivables
- Obsolete Inventory
- Transactions with other banks (loan size, conditions)
- Irrecoverable Investments and loans
- Balance between long,/short,term Liabilities and Assets

### Income Statement

- Breakdown of Production Costs
- Breakdown of Expenses
- Depreciation  $\Rightarrow$  Life Span for Fixed Assets by Type and Depreciation Method
- Ratio of Interest Expense to Sales  $\Rightarrow$  Conditions of Loans
- Ratio of Dividends to Profit

### Common Check Point

(Financial Balance)

Check the account of big outstanding in each account, Assets (cash, etc.)/Liabilities (loan, etc.)/Equities.

## Major Index for Ratio Analysis

### Profitability

- Gross Profit Margin
- Operating Profit Margin
- Return on Assets
- Return on Equity

### Efficiency

- Account Receivables Turnover Period
- Inventory Turnover Period
- Total Assets Turnover
- Working Capital Required

### Stability

- Current Ratio
- Quick Ratio
- Debt to Total Asset Ratio
- Debt/Equity Ratio
- Interest Coverage Ratio

### Growth

- Growth Ratio

(Purpose of Ratio Analysis)

To understand actual condition of business & business efficiency by analysis linking B/S & P/L

# Ratio Analysis: Profitability (1)

## Gross Profit Margin

$$\frac{\text{Gross profit}}{\text{Sales}} (\%)$$

**Nissan Case**  
**Gross Profit :1,617,993**  


---

**Sales:8,773,093**

**18.4%**

Unit : Million JPY

		FY2011
Net Revenues (Sales)		8,773,093
-	Cost of Sales	7,155,100
Gross Profit		1,617,993
-	Selling General and administrative expenses	1,080,526
Operating Profit		537,467
+	Non operating income	86,603
-	Non operating expenses	86,256
	interest expense	28,357
Ordinary Profit		537,814
+	Special gains	27,989
-	Special losses	85,662
Profit before income taxes and others		480,141
-	Income taxes and others	160,920
Net Profit		319,221

(source: NissanMotor Co., Ltd)

## Ratio Analysis: Profitability (2)

### Operating Profit Margin

**Operating profit**  
-----  
**Sales** (%)

**Nissan Case**  
**Gross Profit :537,467**  

---

**Sales:8,773,093**

**6.1%**

Unit : Million JPY

	FY2011
<b>Net Revenues (Sales)</b>	8,773,093
- Cost of Sales	7,155,100
<b>Gross Profit</b>	1,617,993
- Selling General and administrative expenses	1,080,526
<b>Operating Profit</b>	537,467
+ Non operating income	86,603
- Non operating expenses	86,256
interest expense	28,357
<b>Ordinary Profit</b>	537,814
+ Special gains	27,989
- Special losses	85,662
<b>Profit before income taxes and others</b>	480,141
- Income taxes and others	160,920
<b>Net Profit</b>	319,221

(source: NissanMotor Co., Ltd)

### ROA (Return on Assets)

How well do the assets in total generate profits?

$$\frac{\text{Net Profit}}{\text{Total Assets}^*} (\%)$$

\*Beginning and ending average

Nissan Case

$$\frac{\text{Net Profit : 319,221}}{\text{Total Assets: (10,214,820 + 10,736,696) / 2}}$$



3.0%



### ROE (Return on Equity)

How well does the stockholder's equity generate money?

$$\frac{\text{Net Profit}}{\text{Shareholder's Equity}^*} (\%)$$

\*Beginning and ending average

Nissan Case

$$\frac{\text{Net Profit : 319,221}}{\text{Shareholder's Equity:}(3,598,966+3,981,513)/2}$$

8.4%

# Ratio Analysis: Stability , Liquidity Ratio (1)

## Current Ratio

How Liquid are the current liabilities?

(Unit Million JPY)

**Current Assets**  
-----  
**Current Liabilities** (%)

**Nissan Case**  
**Current Assets :6,345,835**  
**Current Liabilities:4,380,545**

**144.9%**

	FY2011		FY2011
<b>Assets</b>		<b>Liabilities</b>	
<b>Current Assets</b>	6,345,835	<b>Current Liabilities</b>	4,380,545
Cash	998,822	Account payable	1,181,469
Accounts Receivable	738,950	Short-term borrowings	593,095
Securities	158,012	current portion of long term borrowings	933,976
Inventory	982,233	Commercial paper	256,601
Other	3,549,773	current portion of bonds	87,280
Allowance for Doubtful	(81,955)	Others	1,328,124
		<b>Long term liabilities</b>	3,082,365
<b>Fixed Assets</b>	4,390,858	Bonds	640,850
Property, Plant and	3,637,042	Long term borrowings	1,422,478
Buildings	645,414	Others	1,019,037
Machinery	1,841,480	<b>Total Liabilities</b>	7,462,910
Land	659,985	<b>Net Assets</b>	
others	490,163	Shareholders' Equity	3,981,513
Intangible Fixed Assets	133,769	Accumulated other	(1,040,098)
Investment and other assets	620,047	others	332,368
		<b>Total Net Assets</b>	3,273,783
<b>Total Assets</b>	10,736,693	<b>Total Liabilities and Net Assets</b>	10,736,693

(source : Nissan Motor Co., Ltd)

## Ratio Analysis: Stability , Liquidity Ratio (2)

### Quick Ratio

Can the current liabilities be covered by assets immediately convertible into cash?

(Unit Million JPY)

$$\frac{\text{Cash} + \text{Marketable Securities} + \text{Account Receivable}}{\text{Current Liabilities}} (\%)$$

Nissan Case

$$\frac{998,822 + 738,950 + 158,012}{\text{Current Liabilities: } 4,380,545}$$

43.3%

	FY2011		FY2011
<b>Assets</b>		<b>Liabilities</b>	
<b>Current Assets</b>	6,345,835	<b>Current Liabilities</b>	4,380,545
Cash	998,822	Account payable	1,181,469
Accounts Receivables	738,950	Short-term borrowings	508,095
Securities	158,012	current portion of long term borrowings	933,976
Inventory	982,233	Commercial paper	256,601
Other	3,549,773	current portion of bonds	87,280
Allowance for Doubtful	(81,955)	Others	1,328,124
<b>Fixed Assets</b>	4,390,858	<b>Long term liabilities</b>	3,082,365
Property, Plant and	3,637,042	Bonds	640,850
Buildings	645,414	Long term borrowings	1,422,478
Machinery	1,841,480	Others	1,019,037
Land	659,985	<b>Total Liabilities</b>	7,462,910
others	490,163	<b>Net Assets</b>	
Intangible Fixed Assets	133,769	Shareholders' Equity	3,981,513
Investment and other assets	620,047	Accumulated other	(1,040,098)
		others	332,368
<b>Total Assets</b>	10,736,693	<b>Total Net Assets</b>	3,273,783
		<b>Total Liabilities and Net Assets</b>	10,736,693

(source : Nissan Motor Co., Ltd)

# Ratio Analysis: Stability , Debt Utilization Ratio (1)

## Debt to Total Asset Ratio

How is the whole company financed?

(Unit Million JPY)

**Total Liabilities**  
-----  
**Total Assets** (%)

**Nissan Case**

**Total Liabilities:7,462,910**

**Total Assets:10,736,693**

**69.5%**

	FY2011		FY2011
<b>Assets</b>		<b>Liabilities</b>	
<b>Current Assets</b>	6,345,835	<b>Current Liabilities</b>	4,380,545
Cash	998,822	Account payable	1,181,469
Accounts Receivables	738,950	Short-term borrowings	593,095
Securities	158,012	current portion of long term borrowings	933,976
Inventory	982,233	Commercial paper	256,601
Other	3,549,773	current portion of bonds	87,280
Allowance for Doubtful	(81,955)	Others	1,328,124
		<b>Long term liabilities</b>	3,082,365
<b>Fixed Assets</b>	4,390,858	Bonds	640,850
Property, Plant and	3,657,042	Long term borrowings	1,422,478
Buildings	645,414	Others	1,019,037
Machinery	1,841,480	<b>Total Liabilities</b>	7,462,910
Land	659,985	<b>Net Assets</b>	
others	490,163	Shareholders' Equity	3,981,513
Intangible Fixed Assets	133,769	Accumulated other	(1,040,098)
Investment and other assets	620,047	others	332,368
		<b>Total Net Assets</b>	3,273,783
<b>Total Assets</b>	10,736,693	<b>Total Liabilities and Net Assets</b>	10,736,693

(source : Nissan Motor Co., Ltd)

## Ratio Analysis: Stability , Debt Utilization Ratio (2)

### Debt/Equity Ratio

How is the whole company financed?

(Unit Million JPY)

**Total Liabilities**  
-----  
**Shareholder's Equity** (%)

**Nissan Case**  
**Total Liabilities: 7,462,910**  
**Shareholder's Equity: 3,981,513**

**187.4%**

	FY2011		FY2011
Assets		Liabilities	
<b>Current Assets</b>	<b>6,345,835</b>	<b>Current Liabilities</b>	<b>4,380,545</b>
Cash	998,822	Account payable	1,181,469
Accounts Receivables	738,950	Short-term borrowings	593,095
Securities	158,012	current portion of long term borrowings	933,976
Inventory	982,233	Commercial paper	256,601
Other	3,549,773	current portion of bonds	87,280
Allowance for Doubtful	(81,955)	Others	1,328,124
		<b>Long term liabilities</b>	<b>3,082,365</b>
<b>Fixed Assets</b>	<b>4,390,858</b>	Bonds	640,850
Property, Plant and	3,637,042	Long term borrowings	1,422,478
Buildings	645,414	Others	1,019,037
Machinery	1,841,480	<b>Total Liabilities</b>	<b>7,462,910</b>
Land	659,985	<b>Net Assets</b>	
others	490,163	Shareholders' Equity	3,981,513
Intangible Fixed Assets	133,769	Accumulated other	(1,040,098)
Investment and other assets	620,047	others	332,368
		<b>Total Net Assets</b>	<b>3,273,783</b>
<b>Total Assets</b>	<b>10,736,693</b>	<b>Total Liabilities and Net Assets</b>	<b>10,736,693</b>

(source : Nissan Motor Co., Ltd)

## Ratio Analysis: Stability , Debt Utilization Ratio (3)

### Interest Coverage Ratio

How are the interest payments assured?

$$\frac{\text{Profit before Tax \& Interest Expense}}{\text{Interest}} (\%)$$

$$\frac{\text{Nissan Case } 480,141 + 28,357}{\text{Interest } 28,357}$$

1,793%

Unit : Million JPY

	FY2011
Net Revenues (Sales)	8,773,093
- Cost of Sales	7,155,100
Gross Profit	1,617,993
- Selling General and administrative expenses	1,080,526
Operating Profit	537,467
+ Non operating income	86,603
- Non operating expenses	86,256
Interest expense	28,357
Ordinary Profit	537,814
+ Special gains	27,989
- Special losses	85,662
Profit before income taxes and others	480,141
- Income taxes and others	160,920
Net Profit	319,221

(source: NissanMotor Co., Ltd)

### Account Receivables Turnover Period

Are Account Receivables properly collected ?

$$\frac{\text{Account Receivables}^*}{\text{Average Sales per month}} \quad (\text{month})$$

\*Beginning and ending average

Nissan Case

Account Receivables:  $(641,154 + 738,950) / 2$

Average Sales per month :  $8,773,093 / 12$



0.9 month





### Inventory Turnover Period

How large are the inventories in terms of monthly sales ?

$$\frac{\text{Inventory}^*}{\text{Average Sales per month}} \quad (\text{month})$$

\*Beginning and ending average

Nissan Case

$$\frac{\text{Inventory: } (802,278 + 998,822) / 2}{\text{Average Sales per month : } 8,773,093 / 12}$$



1.2 month



### Total Assets Turnover

How do the total assets generate sales? (asset utilization efficiency)

$$\frac{\text{Sales}}{\text{Total Assets}^*} \quad (\text{Number of times/year})$$

\*Beginning and ending average

Nissan Case

$$\frac{\text{Sales : 8,773,093}}{\text{Total Assets: (10,214,820+10,736,693)/2}}$$



0.8times



### Working Capital Required

Cash is the lifeblood of a business. It keeps operation going. Required cash balances should be set aside for operating needs. Working capital required is calculated as follows.

#### Calculation Formula of Working Capital

1. Account Receivables Turnover Period(months) ..... **A**
2. Trade-Payables Turnover Period(months) ..... **B**
3. Inventory Turnover Period (months) ..... **C**
4. Working Capital Required (months) = **A - B + C**

# Ratio Analysis: Growth

## Growth Ratio

How well is the company growth?

**Current Figure** ←  
— 1 (%)  
**Previous Figure** ←

**Nissan Case (sales)**  
$$\frac{8,773,093}{7,517,277} - 1(\%)$$

**16.7%**

Unit : Million JPY

	FY2009	FY2010	FY2011
Net Revenues (Sales)	8,436,974	7,517,277	8,773,093
- Cost of Sales	7,118,862	6,146,219	7,155,100
Gross Profit	1,318,112	1,371,058	1,617,993
- Selling General and administrative expenses	1,456,033	1,059,449	1,080,526
Operating Income	▲ 137,921	311,609	537,467
+ Non operating income	38,121	29,126	86,603
- Non operating expenses	72,940	132,988	86,256
interest expense	33,798	28,995	28,357
Ordinary Income	▲ 172,740	207,747	537,814
+ Special gains	62,156	20,552	27,989
- Special losses	108,187	86,679	85,662
Income before income taxes and others	▲ 218,771	141,620	480,141
- Income taxes and others	14,938	99,230	160,920
Net Income	▲ 233,709	42,390	319,221

(source: NissanMotor Co., Ltd)

## Other Analysis Methods (1): Trend Analysis

---

### Method

**Compare the past 5 years order (If possible, 10 years)**

### Purpose

**Assess the actual condition of the company by understanding tendency of performance through checking business activity in a continuous year**

### Point

**Determine causes of those tendency**

### Example of Analysis

- ✓ **Protracted account receivables turnover period**
  - **it is impossible to collect account receivables due to financial trouble of customers (Bad debt)**
- ✓ **Protracted inventory turnover period**
  - **Record dummy products, obsolete products as inventory, and report window-dressing profit**

## Other Analysis Methods (2): Cross Sectional Analysis

---

### Methods

**Comparison with the target company and sector peer/benchmarking companies in the field of profit level, financial ratio, turnover period.**

### Purpose / Background

**Competition in the field of same sector is severe. Therefore, it is important to assess whether the target company can survive in this sector or not through comparison.**

### Example of Analysis

- ✓ **Low profitability : High procurement cost, Low productivity**
- ✓ **Inventory turnover period is longer : Low productivity, dead-stock, bad production plan**
- ✓ **Low total assets turnover : Low assets efficiency, the company doesn't make good use of assets**

# Window,Dressing

---

*Some examples...*

## **1. Large fluctuation in sales**

- , Sales should be recognized in next fiscal year unless it is booked this fiscal year's sales.
- , Book the dummy sales etc.

## **2. Large fluctuation in profitability**

- , Expense should be recognized in this fiscal year unless it is booked next fiscal year's expense.
- , Price adjustment to subsidiaries
- , Change of evaluation method of assets.

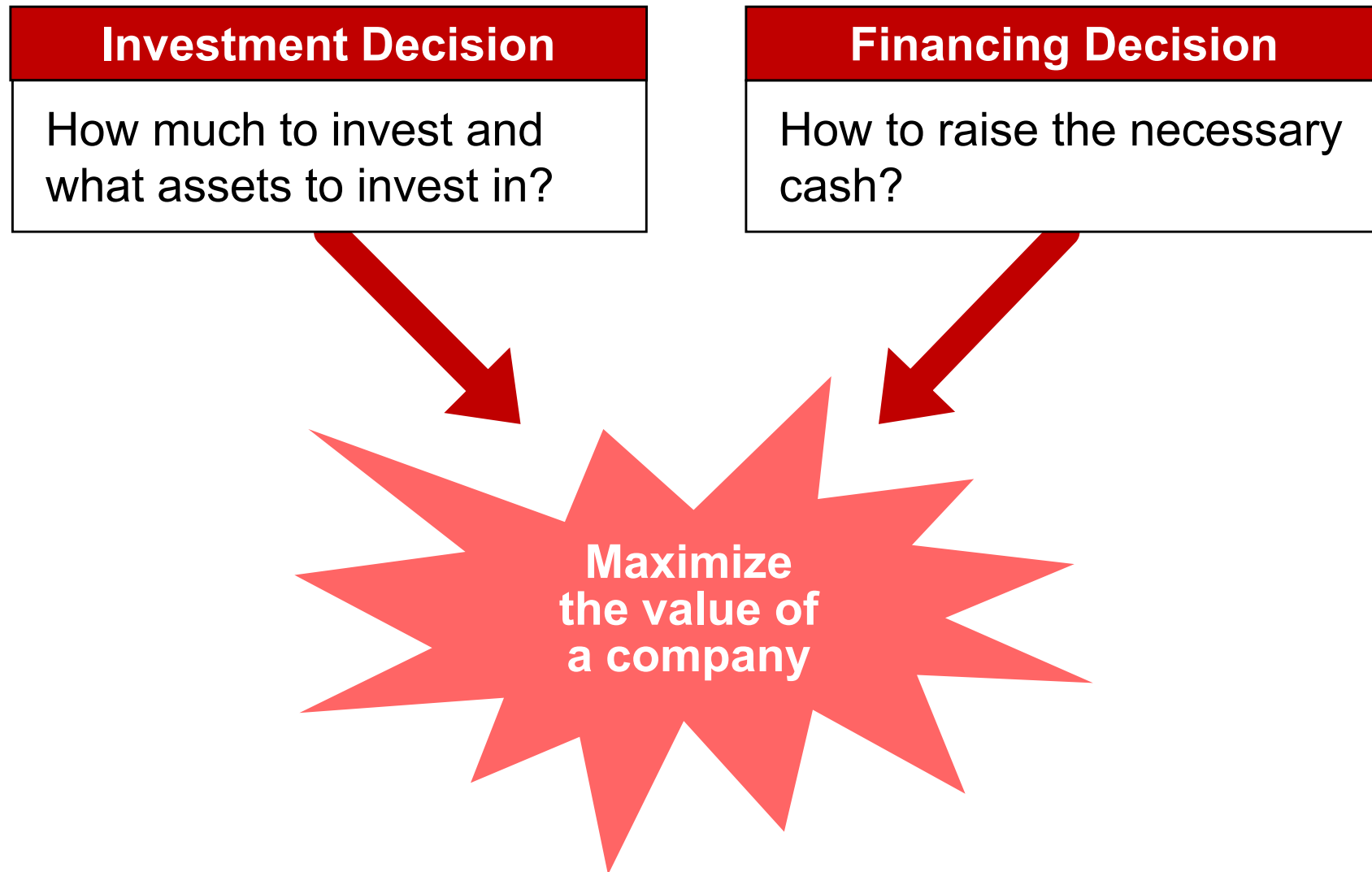
## **3. Interest**

- , High interest rate  
the possibility of loan from loan shark and off,balance sheet debt
- , Low interest rate  
the possibility of delinquency or transfer of account (expense , assets).



## **2. Corporate Finance**

---



## Investment Decision Making (1)

---

	<u>Project A</u>	<u>Project B</u>
Year 0	,100	,100
Year 1	50	10
Year 2	40	30
Year 3	30	40
Year 4	10	60

- Suppose you are a CFO of company X.
- Now company X needs to choose one of two projects, Project A and Project B.
- Which project do you choose and why?

## Investment Decision Making (2)

	<u>Project A</u>	Cumulative CF	<u>Project B</u>	Cumulative CF
Year 0	,100	,100	,100	,100
Year 1	50	,50	10	,90
Year 2	40	,10	30	,60
Year 3	30	<u>20</u>	40	,20
Year 4	10		60	<u>40</u>

### Payback

- The payback period of a project is found by counting the number of years it takes before cumulative forecasted cash flows equal the initial investment.
- The payback period of Project A is 3 years, while that of Project B is 4 years.  
→ Then, you will choose Project A when you apply payback period.
- This approach might underestimate future cash flows after the payback period.

## Investment Decision Making (3)

	<u>Project A</u>	Total future CF	<u>Project B</u>	Total future CF
Year 0	,100		,100	
Year 1	50		10	
Year 2	40		30	
Year 3	30		40	
Year 4	10	<b>Year 1-4: 130</b>	60	<b>Year 1-4: 140</b>

### Simple Addition of CF

- Total future cash flows of Project A is 130, while that of Project B is 140.  
→ Then, you will choose Project B.
- This approach does not consider the concept of time value of money.

### **“A dollar today is worth more than a dollar tomorrow.”**

- Suppose you have \$100 now (Year 0) and deposit this \$100 in a bank with 10%/year interest rate.
  - In Year 1, your \$100 now will be \$110. ( $100 \times 1.1 = 110$ )
  - In Year 2, your \$100 now will be \$121. ( $100 \times 1.1^2 = 121$ )
- The present value of \$100 one year from now is \$90.9. ( $100 / 1.1 = 90.9$ )  
The present value of \$100 two years from now is \$82.6. ( $100 / (1.1)^2 = 82.6$ )
- Present value is sum of discounted future cash flows.

## Investment Decision Making (4)

	<u>Project A</u>	PV of future CF	<u>Project B</u>	PV of future CF
Year 0	,100	,100	,100	,100
Year 1	50	45.45	10	9.09
Year 2	40	33.06	30	24.79
Year 3	30	22.54	40	30.05
Year 4	10	6.83	60	40.98
NPV		<u>7.88</u>		<u>4.92</u>

### Net Present Value (NPV)

- Present value is calculated by multiplying discount factor,  $1/(1+r)^n$ . In this case,  $1/(1+0.1)$  in Year 1,  $1/(1+0.1)^2$  in Year 2, R  
NPV is sum of current cash flows and discounted future cash flows.
- NPV of Project A is 7.88, while NPV of Project B is 4.92.  
→ Then, you will choose Project A.



## Investment Decision Making (5)

	<u>Project A</u>	IRR	<u>Project B</u>	IRR
Year 0	,100		,100	
Year 1	50		10	
Year 2	40		30	
Year 3	30		40	
Year 4	10	<b>14.5%</b>	60	<b>11.8%</b>

### Internal Rate of Return (IRR)

- The internal rate of return is defined as the rate of discount which makes NPV=0.
- IRR of Project A is 14.5%, while IRR of Project B is 11.8%.  
→ Then, you will choose Project A.

## Investment Decision Making (6)

	<u>Project A</u>	<u>Project B</u>
Year 0	,100	,100
Year 1	50	10
Year 2	40	30
Year 3	30	40
Year 4	10	60
<u>Year 5</u>	<u>5</u>	<u>70</u>
NPV	<u>10.98</u>	<u>48.38</u>
IRR	<u>16.0%</u>	<u>23.2%</u>

- Your choice of project will change when future cash flows in Year 5 is added.
- Hence, projection of future cash flows is very important!

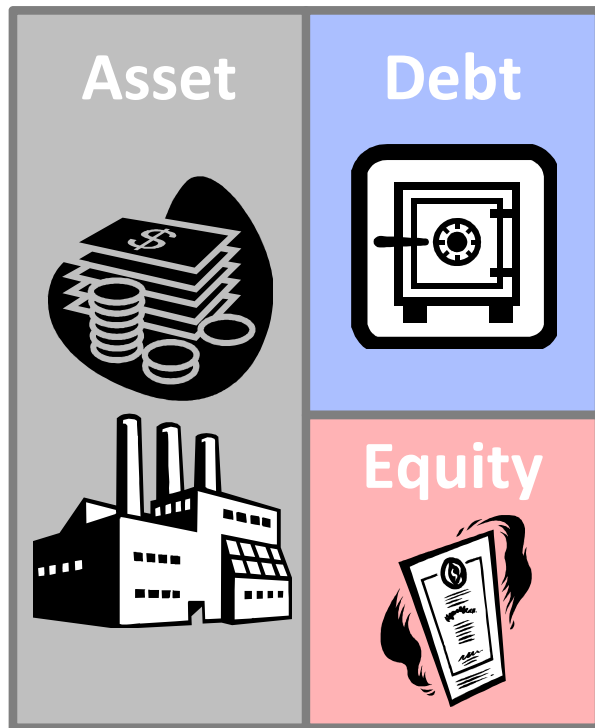
## Investment Decision Making (7)

	<u>Project A</u>	<u>Project B</u>
Year 0	,100	,100
Year 1	50	10
Year 2	40	30
Year 3	30	40
Year 4	10	60
Year 5	5	70
<u>NPV</u>	<u>, 6.4</u>	<u>9.4</u>
IRR	16.0%	23.2%

- Your decision making will change when a discount factor is  $1/(1+0.2)^n$ , instead of  $1/(1+.01)^n$ .
- Hence, picking an appropriate “r”, a rate of return, is also very important.

# Equity Financing vs Debt Financing (1)

*Basic understanding on the differences...*



From?	Repay principal?	Term?	Collateral, guarantor	Costs?	Priority in waterfall?
Banks, (Bond) Investors	Yes	Long Short	Necessary	Interest, Fees	V
(Equity) Investors	No	Long	Not Necessarily	Dividend, Fees	

Source: JICA experts

## c.f. IRR & Cost of Capital

---

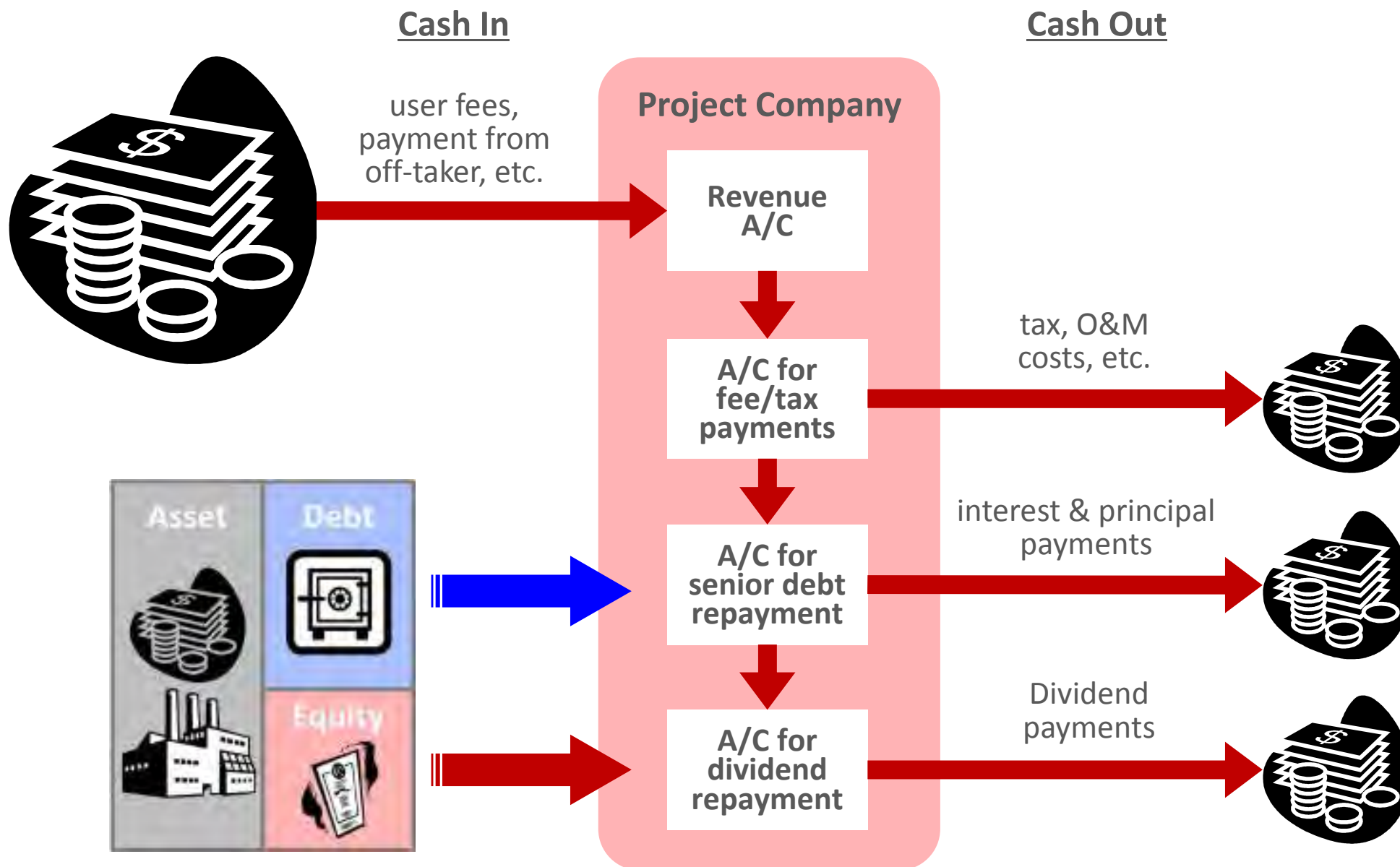
- Cost of Capital refers to the cost of a company's funds (both debt and equity).
- If IRR is smaller than Cost of Capital in a project, you will reject the project.  
If IRR is larger than Cost of Capital, you will go for it.
- Weighted Average Cost of Capital (WACC) is the weighted average of cost of debt and cost of equity.

e.g.) Debt: 20, Equity 30, Cost of debt: 8%, Cost of equity: 15%  
$$WACC = 8\% \times 20/50 + 15\% \times 30/50 = 12.2\%$$

- In general, cost of debt is cheaper than cost of equity, because debt holders tend to be secured by collateral and have higher priority of being paid in case of bankruptcy, i.e., less risky compared to equity holders.
- Cost of debt of company X is higher, when the amount of debt increases and the default risk rises.

## Equity Financing vs Debt Financing (2)

### *Flow of cash under waterfall distribution*



## c.f. Scenario Analysis

---

- In today's rapidly changing world, precise projection is very difficult.
- You could attempt to forecast several possible scenarios depending on the state of the economy, etc., and assign probabilities to each scenario.
- For example, NPV of Project A will be one of the following.

	<u>Base</u>	<u>Best</u>	<u>Worst</u>
NPV	50	200	,100
Probability(%)	50	25	25

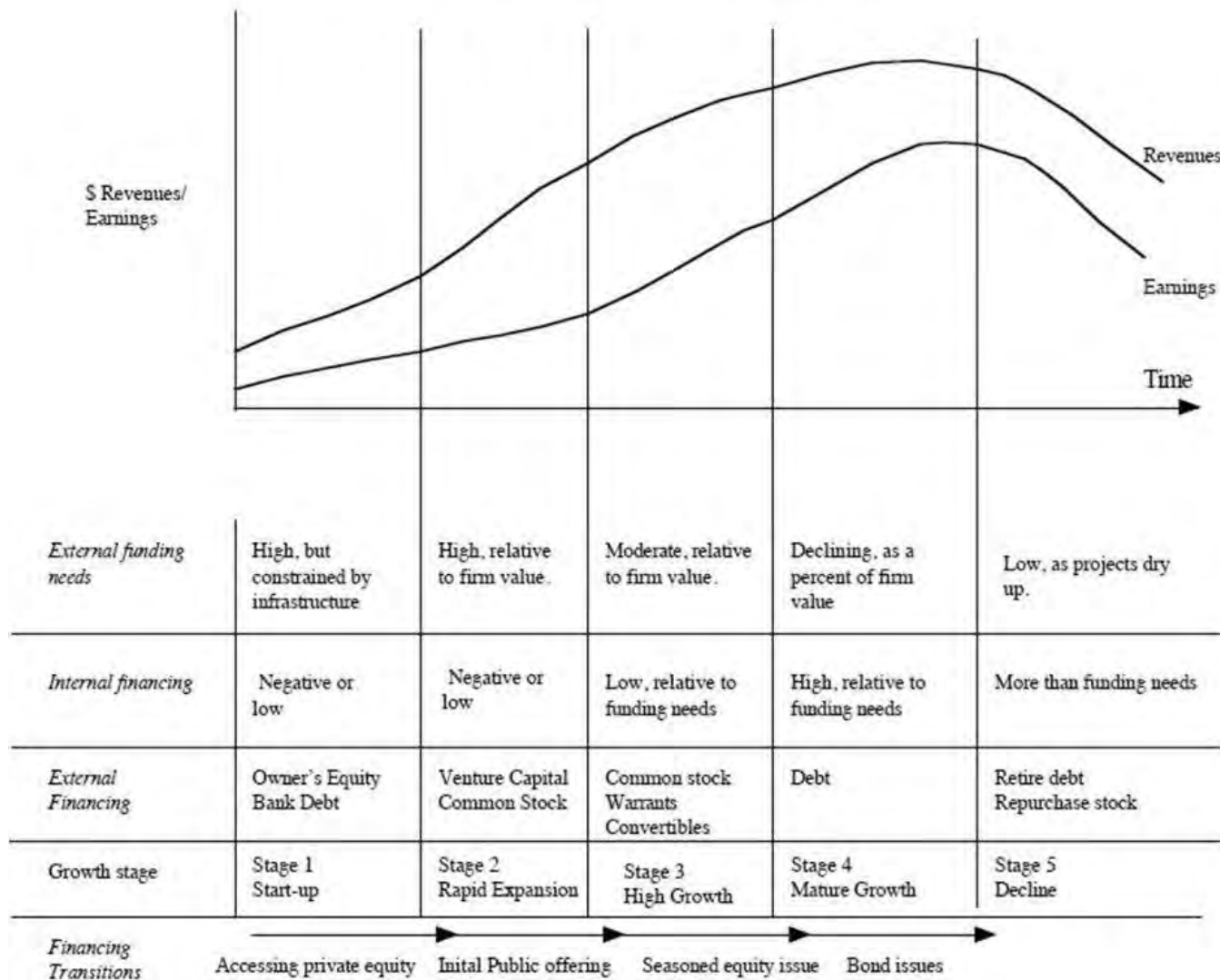
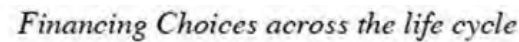
Then, the expected average NPV is 50. ( $= 50 \times 0.5 + 200 \times 0.25 + ,100 \times 0.25$ )

What if probability of each scenario would be Base: 50%, Best: 5%, Worst: 45%?

Then, the expected average NPY is ,10. ( $= 50 \times 0.5 + 200 \times 0.05 + ,100 \times 0.45$ )



## Financing Decision (1)



When company X needs funds for a new project, two common options for financing are equity and debt.

**Equity:** Owner's equity, venture capital, common stock

**Debt:** Bank loan, corporate bond, CP

Financing needs of a company will change depending on its growth stage.

Source: Aswath Damodaran's "Corporate Finance Lecture Note" ([http://w4.stern.nyu.edu/~adamodar/New\\_Home\\_Page/cflect.htm](http://w4.stern.nyu.edu/~adamodar/New_Home_Page/cflect.htm))

## Financing Decision (2)

	Advantages	Disadvantages
<b>Equity financing</b>	<ul style="list-style-type: none"><li>• No need to pay back money invested.</li><li>• Involvement of high, profile investors may help the credibility of a business</li><li>• Possible to have valuable assistance from investors.</li></ul>	<ul style="list-style-type: none"><li>• Dilution of ownership interests and possible loss of control.</li></ul>
<b>Debt financing</b>	<ul style="list-style-type: none"><li>• Interest paid on debt financing is tax deductible.</li><li>• Lenders do not gain ownership interest.</li><li>• Adds discipline to management</li></ul>	<ul style="list-style-type: none"><li>• Too much debt increases the perceived risk and reduces ability to raise additional funds.</li><li>• For new businesses, in which cash flows are not stable, it is difficult to get bank loans.</li></ul>

The best mix of debt and equity financing depends on various factors such as:

- current debt, to, equity ratio
- the long, term goal of business
- the amount of control managers would like to maintain
- condition of financial market.

Types of debt financing (duration, currency, fixed/floating rate) should be considered based on nature of businesses.

## c.f. Debt, to, Equity Ratio

---

Debt, to, equity ratio varies depending on the industry.

e.g.) Listed companies in Japan

	<u>1999</u>	<u>2009</u>
<u>All industries:</u>	254.4	168.3
Manufacturing:	183.4	143.7
[                    ]:	56.3	43.8
Cement:	422.1	389.6
Iron & Steel:	407.3	161.3
Automobiles:	243.0	199.1
Non, Manufacturing:	394.2	209.5
Wholesale Trade:	1,295.2	323.3
Retail:	181.0	160.8
Railroads:	812.9	378.6
[                    ]:	1,767.5	291.2

Source: DBJ “Handbook of Industrial Financial Data 2010”

## c.f. Bank Loans & Bonds

---

	<b>Bank Loans</b>	<b>Bonds</b>
Borrower	Size does not matter	Should be larger in size
Creditors	Banks	Bond holders (institutional investors, banks, general public, etc.)
Repayment	Regular installments in general	Bullet payment in general (Early redemption option could be included, but after a certain number of years)
Collateral	Required in general	Not required in general
Covenants	More strict (Violation of covenant could lead to request for immediate repayment by banks)	Less strict
Procedure	Quicker	Time consuming

## c.f. Credit Ratings & Default Risk

Sample numbers  
↓

2000 コホート

	1 年後	2 年後	3 年後	4 年後	5 年後	6 年後	7 年後	8 年後	9 年後	10 年後	サンプル数
AAA	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	18
AA	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	92
A	0.00	0.38	0.76	0.76	0.76	0.76	0.76	0.76	0.76	1.15	263
BBB	0.00	0.36	0.73	0.73	1.46	1.46	1.46	1.46	1.83	2.21	279
BB	0.00	0.00	1.39	5.62	7.05	8.48	9.91	9.91	11.36	11.36	74
B 以下	18.18	36.36	54.55	54.55	54.55	65.91	65.91	65.91	65.91	65.91	11
BBB 以上	0.00	0.31	0.62	0.62	0.93	0.93	0.93	0.93	1.09	1.41	652
BB 以下	2.35	4.71	8.32	12.04	13.30	15.81	17.07	17.07	18.34	18.34	85
全体	0.27	0.82	1.51	1.92	2.34	2.62	2.76	2.76	3.05	3.33	737

Source: Rating and Investment Information, Inc. "The Relationship between Credit Ratings and Default" (June 30, 2011)

For a company with lower credit rating, default risk will be higher, and hence, cost of borrowing will be more expensive.

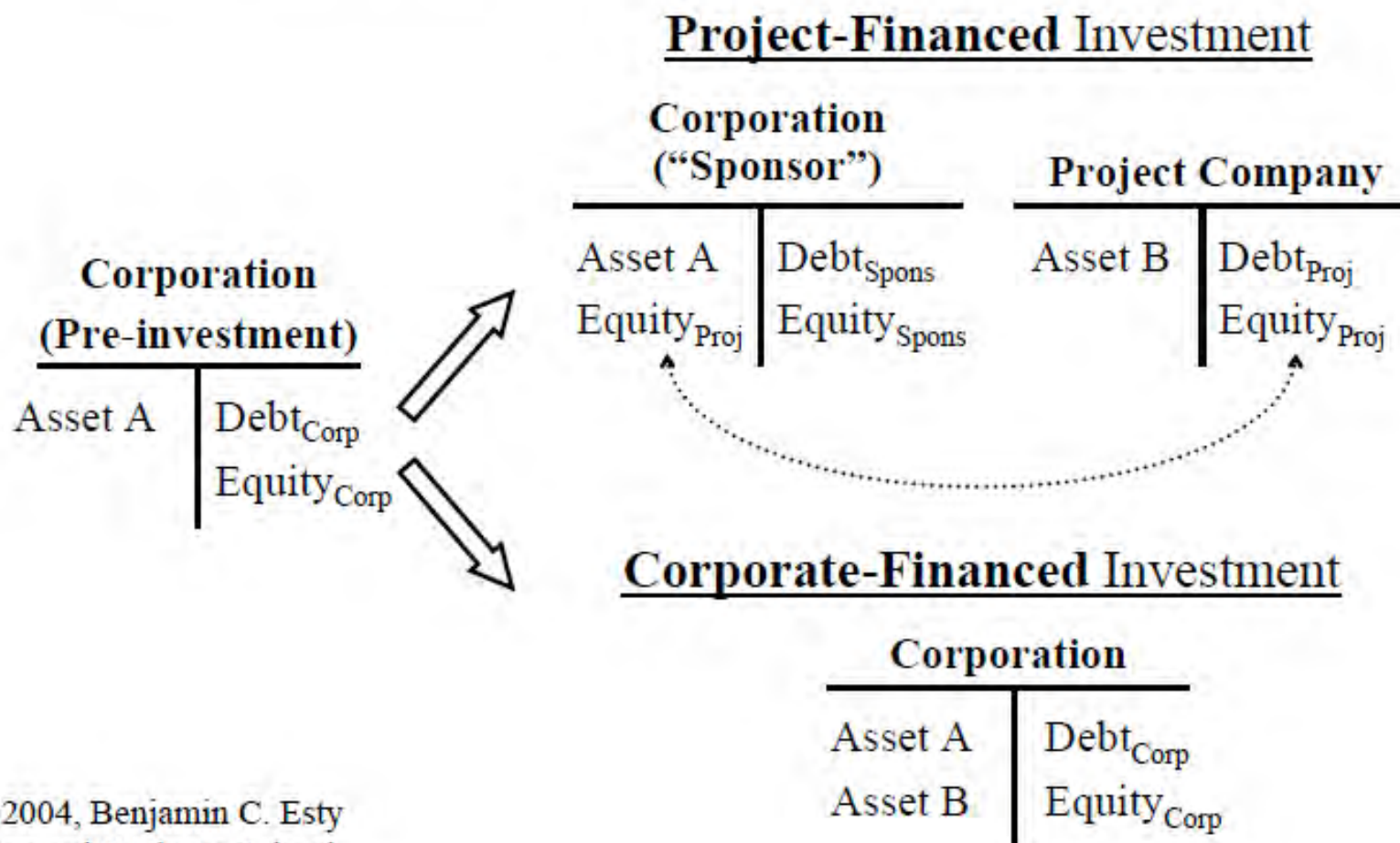
# Corporate Finance vs Project Finance (1)

	Corporate Finance	Project Finance
Financing vehicle	Multi,purpose organization	Single,purpose entity
Type of capital	Permanent ,,, an indefinite time horizon for equity	Finite ,,, time horizon matches life of project
Dividend policy and reinvestment decisions	Corporate management makes decisions autonomous from investors and creditors	Fixed dividend policy ,,, immediate payout; no reinvestment allowed
Capital investment decisions	Opaque to creditors	Highly transparent to creditors
Financial structures	Easily duplicated; common forms	Highly,tailored structures which cannot generally be re,used
Transaction costs for financing	Low costs due to competition from providers, routinized mechanisms and short turnaround time	Relatively higher costs due to documentation and longer gestation period
Size of financings	Flexible	Might require critical mass to cover high transaction costs
Basis for credit evaluation	Overall financial health of corporate entity; focus on balance sheet and cashflow	Technical and economic feasibility; focus on project's assets, cash flow and contractual arrangements
Cost of capital	Relatively lower	Relatively higher
Investor / lender base	Typically broader participation; deep secondary markets	Typically smaller group; limited secondary markets

Source: The Wharton School "Project Finance Teaching Note" (<http://finance.wharton.upenn.edu/~bodnarg/ml/projfinance.pdf>)

## Corporate Finance vs Project Finance (2)

### The Definition of Project Finance: Comparison of Project- vs. Corporate-Financed Investment



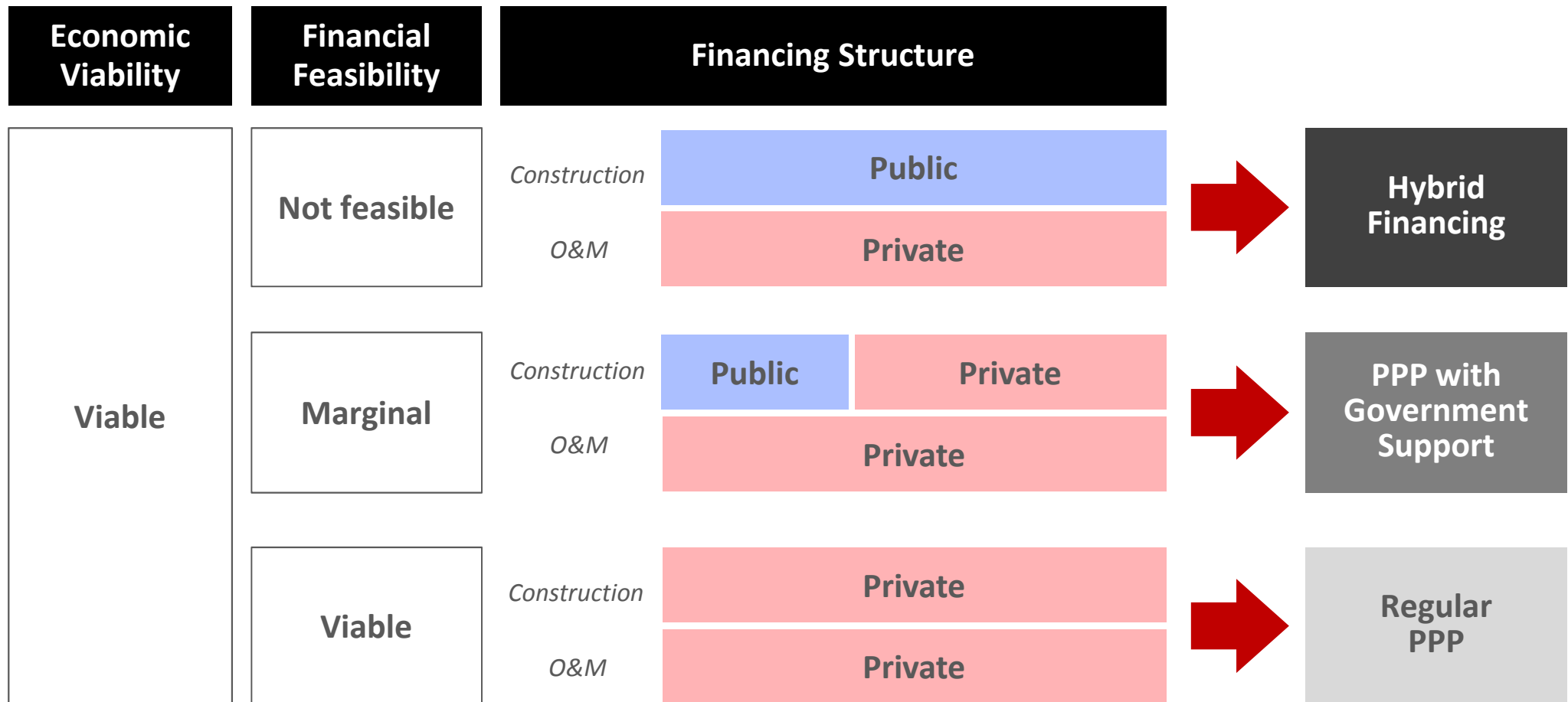


### **3. Relevant Issues**

---

# PPP (1)

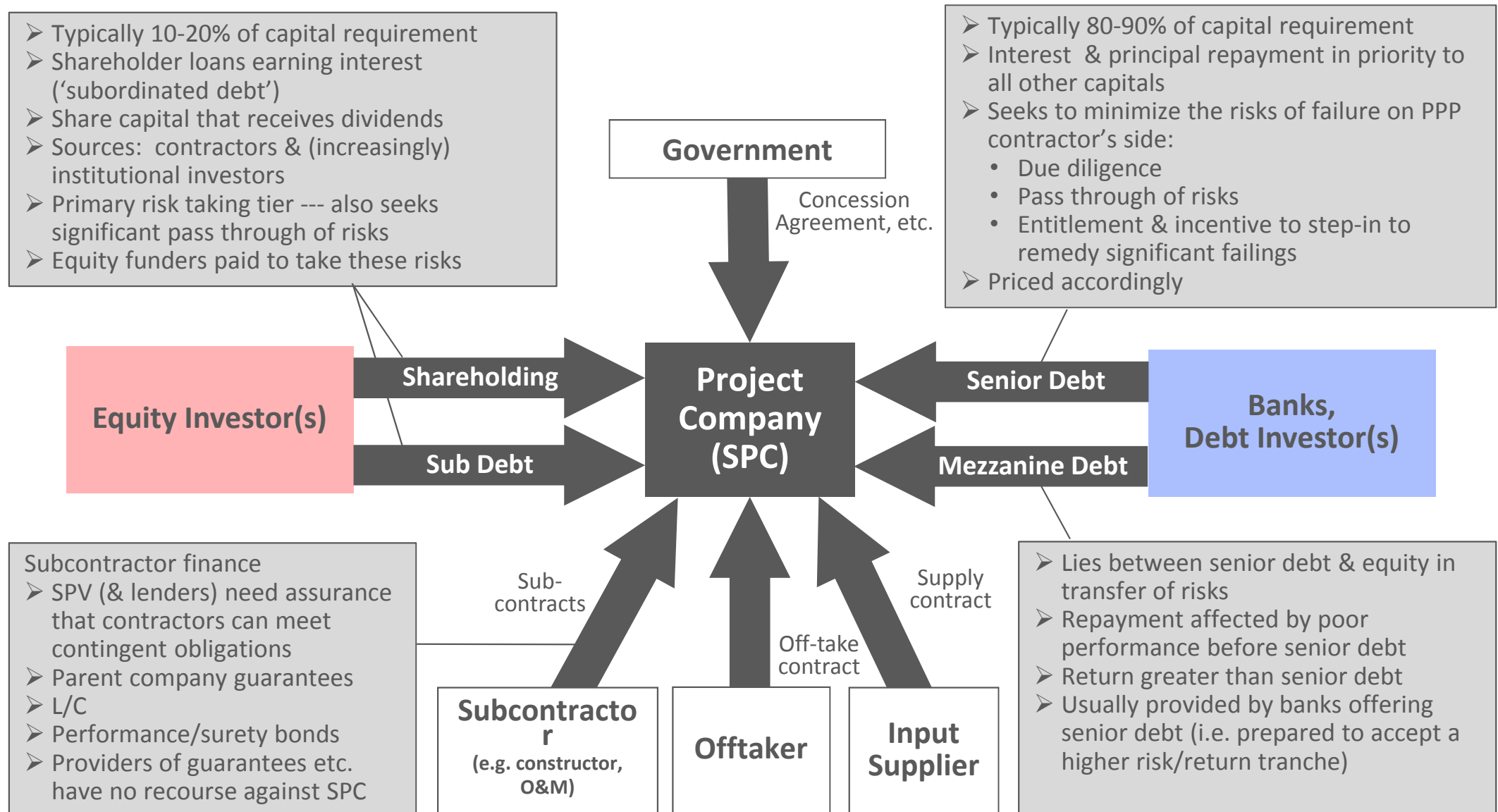
## How to finance PPP?



Source: JICA experts from Bastary Pandji Indra, 'Urban Infrastructure PPP –an Indonesian Perspective' (2010)

## PPP (2)

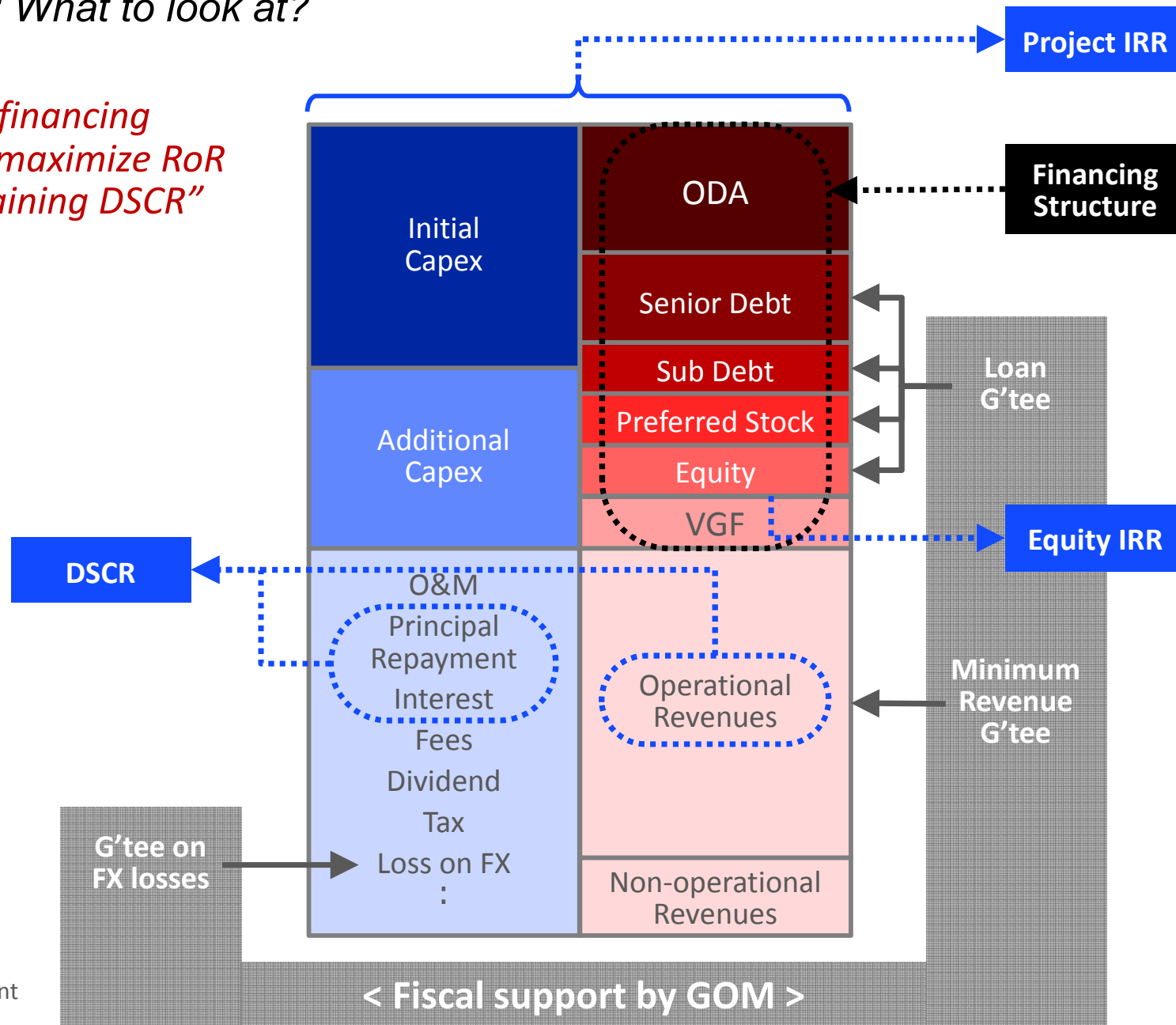
### General financing structure for PPPs



## PPP (3)

### PPP finance: What to look at?

*“Optimizing financing structure to maximize RoR while maintaining DSCR”*



# Privatization (1)

---

## *Definition (1)*

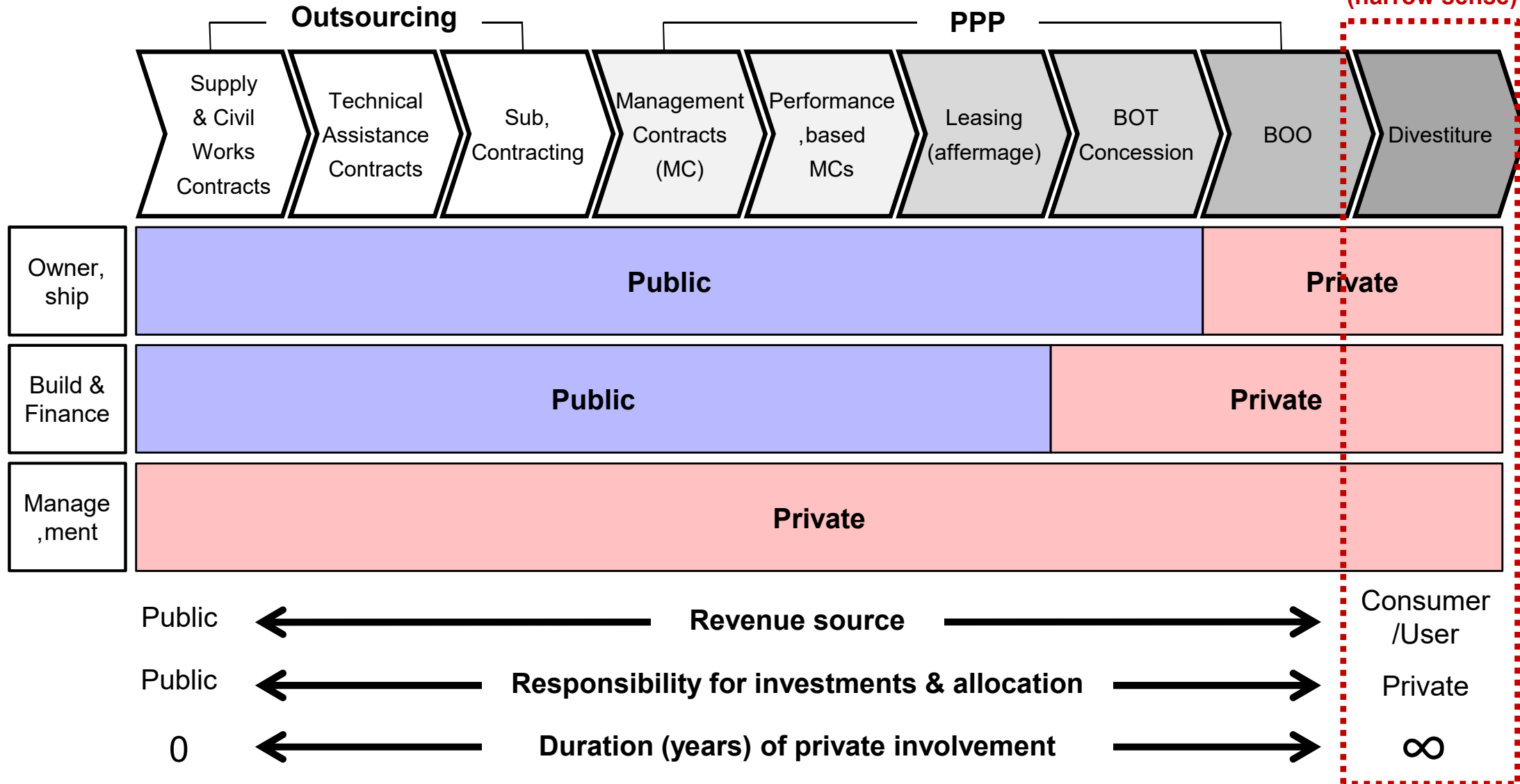
- Process of transferring ownership of a business, enterprise, agency, public service, or public property from the public sector to the private sector
- Choice of privatization method is influenced by the depth of capital markets, political and company-specific factors



# Privatization (2)

## Definition (2)

**Privatization  
(narrow sense)**



## Privatization (3)

### *Why Privatize?*

- **Burden of loss making SOEs on government budget. (SOE losses against GDP)**
  - ✓ 9% Poland (incl. subsidies)
  - ✓ 9% Argentina in 1989
  - ✓ Mongolia?



- **Benefits (Most cases had shown better result~)**
  - ✓ Productivity increase
  - ✓ Faster growth
  - ✓ Greater cost savings
  - ✓ Enhance domestic capital markets





# Privatization (4)

## Framework for Privatization Strategy

### Settlement of Political Target

- **Government's budget reconstruction**

- ✓ realize capital gain
- ✓ securement of tax revenue
- ✓ reduction of government spending

- **Enhance service for consumer**

- ✓ reduction of cost
- ✓ improvement of service quality
- ✓ depoliticization

- **Flourish domestic industry**

- ✓ creation of business opportunity
- ✓ enhancement of competitiveness
- ✓ developing capital market

### Analysis of Strategic Key Factors

- **Ownership**

- ✓ pursuing economical efficiency
- ✓ improvement of governance
- ✓ liberation of legal restriction

- **Management know-how**

- ✓ improve efficiency
- ✓ benefit by creating demand
- ✓ enhance convenience

- **Finance**

- ✓ Contribute to government's budget
- ✓ Non,budget system
- ✓ disciplined control

- **Market mechanism**

- ✓ Improving efficiency

### Choice of Method

- **Ownership transfer**

- ✓ IPO
- ✓ Trade sale
- ✓ MBO

- **PPP**

- ✓ PFI
- ✓ Concession
- ✓ BOT / BOO
- ✓ Outsourcing

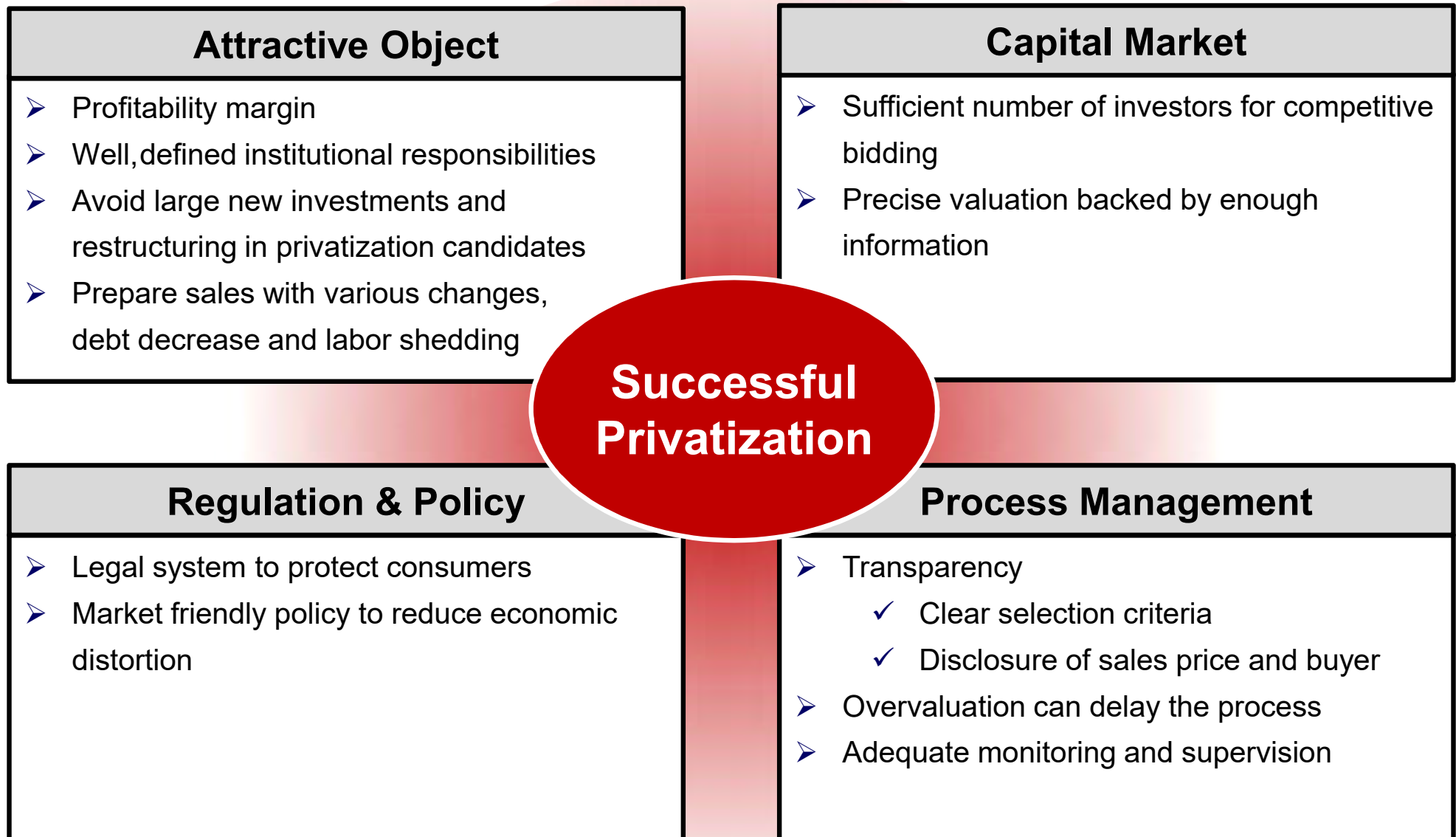
- **Market liberation**

- ✓ bidding
- ✓ deregulation

\* Source: Yumiko NODA, *Strategy and Methods of Privatization* 2004

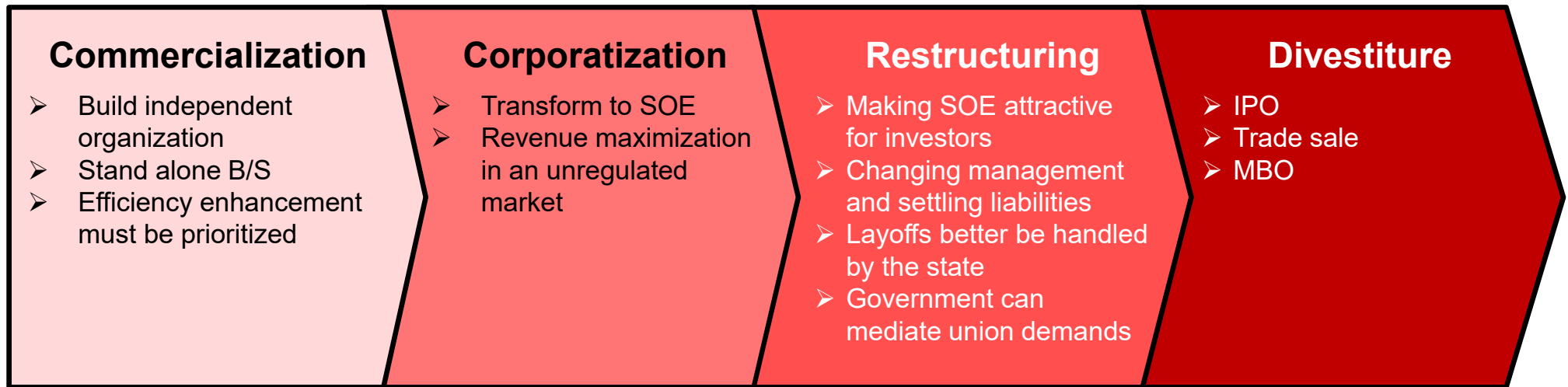
# Privatization (5)

## Keys for Success



# Privatization (6)

## 4 Steps







- Deregulation of the relative markets contributes to the smooth process
- Promoting competition and ensuring competitive market for divestiture in favorable terms

# Privatization (7)

## Cases in Japan

\* Simple sum of the numbers for the group companies

(As of March 31, 2014) Consolidated				
	Nippon Telegraph and Telephone corporation	East Japan Railway and 6 companies	Japan Tobacco	Tokyo Electric Power Company
Establishment / Listed	1985 / 1985	East: 1987 / 1992 West&Central: 1987 / 1993	1985 / 1994	1952 / 2003
Employees (person)	239,750	East: 73,511 Group total: 173,591	51,341	35,723
Paid, In Capital (JPY bn)	938	East: 200 Group total*: 460	100	1,400
Total Asset (JPY bn)	20,285	East: 7,428 Group total*: 18,481	4,611	14,801
Total Revenue (JPY bn)	10,925	East: 2,704 Group total*: 6,432	2,400	6,631
Market Capitalization (JPY bn)	9,092	9,890 (East & West & Central Sub, total)	8,132	770
Ownership (Voting rights base) (red= public sector)	MOF: 35.65% Employee: 0.81%	Privatized 3 companies Private: 100.00%  Other 4 companies JRTT: 100.00%	MOF: 33.35%	NDF*: 50.10% Employee: 1.46% Tokyo Metropolis: 1.35%
Floated stock (%)	64.35%	100.00% (East & West & Central)	66.65%	48.55%

\* Nuclear Damage Compensation and Decommissioning Facilitation Corporation

## c.f. Structure of Cross Border Financing

*Recent changes in cross border money flows captured through IIP(\*)*

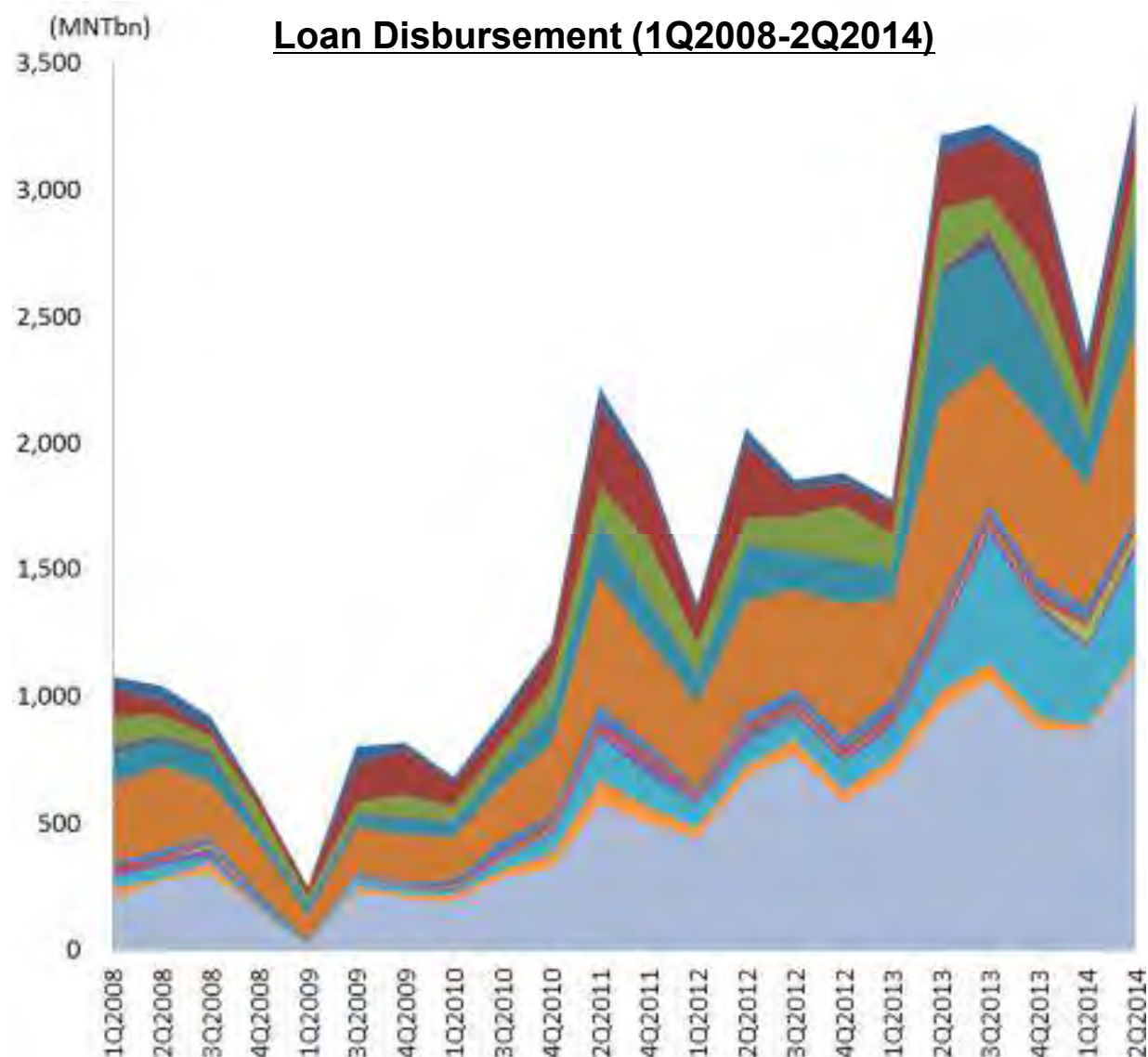
(\*) IIP = International Investment Position  
Source: JICA experts from Mongol Bank



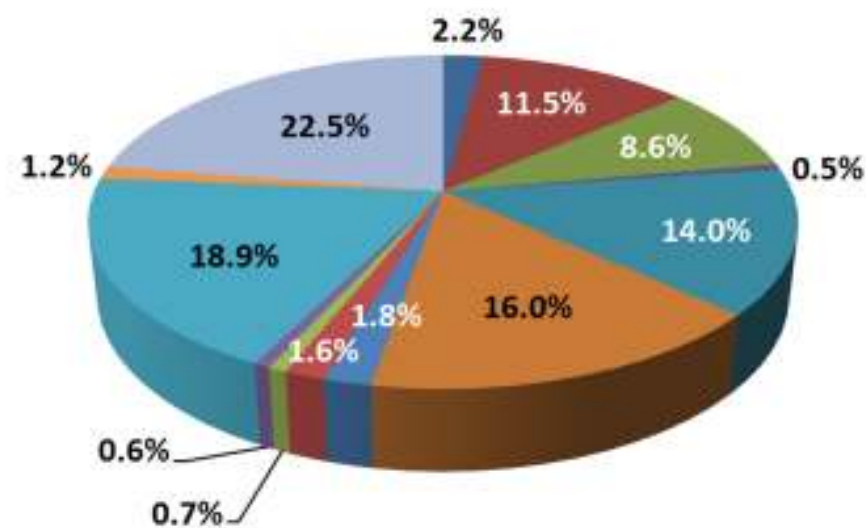


## c.f. Sector Composition of Debt Financing

### *Loan disbursement & outstanding by sector*



### **Sector Composition of Loan Outstanding (2Q2014)**



Source: JICA experts from Mongol Bank

For Further Questions/Inquiries...

---

## JICA Consultant Team / Corporate Finance Analysis

➤ **Takayuki URADE** ([urade@jeri.co.jp](mailto:urade@jeri.co.jp))

**(Ulaanbaatar)**

Room #207, Financial Regulatory Commission, Mongolia

**(Tokyo)**

Japan Economic Research Institute Inc. (JERI)

Shin Otemachi Bldg. 3F, 2-2-1 Otemachi, Chiyoda-ku, Tokyo, Japan

Phone: +81-3-6214-4630



# **Project for Capacity Building of Capital Market in Mongolia: Financials for Securities Companies**

---

30 April 2015

Daiwa Institute of Research  
Japan Economic Research Institute

## 1a. Securities companies' business

---

### 1. Brokerage

Traditional and main source of income for most of securities companies. Branch network and online IT system are keys to success.

### 2. Underwriting

Requires skilled staff. It usually takes years from the time when an underwriter starts talking with a company to its IPO. Underwriting commission rate can be as high as 5%, taking risks of price variation of shares that are bought from the company before selling out to investors.

### 3. Dealing

Securities companies also act as an investor.

### 4. Others

With diversified business, securities companies also collect commissions such as M&A advisory fees, fund management fees, administrative commissions, other financial product related commissions etc.

## 1b. Securities companies' business: Brokerage commission

Brokerage commission is the fee an investor pays to a securities broker for placing buy/sell order.

Example: You place buy order for Sugi Corp, 3,000 shares, at MNT15,000.

Sugi Corp current share price	MNT15,000
Order volume	3,000 shares
Brokerage commission rate	0.8%

Brokerage commission you have to pay to your securities company, in other words your securities company's income is:

$$\text{MNT}15,000 \times 3,000 \text{ shares} \times 0.8\% = \text{MNT}360,000$$

## 1c. Securities companies' business: Underwriting commission

Underwriting commission is the fee that a company pays to securities companies/investment banks for underwriting. Underwriting is that securities companies/investment banks buy new shares from a issuer before an IPO.

Example: Sugi Corp makes an IPO by issuing new shares and three securities companies (Urade Securities, Kaneko Securities, Ozaki Securities) underwrite the shares.

Sugi Corp IPO price	MNT15,000
New shares issued	30,000,000 shares
Underwriting commission rate	5.0%
Urade Securities' allotment	15,000,000 shares
Kaneko Securities' allotment	10,000,000 shares
Ozaki Securities' allotment	5,000,000 shares

Underwriting commission that Sugi Corp has to pay to Urade Securities, in other words, Urade Securities' income is:

$$\text{MNT}15,000 \times 15,000,000 \text{ shares} \times 5.0\% = \text{MNT}11.25\text{m}$$

## 1d. Securities companies' business: Dealing

Dealing is buy/sell activities by a securities company using its own money.

Example: A dealer at Urade Securities bought Sugi Corp's shares last month, then sells all of them this month.

Sugi Corp's share price on 31 Mar	MNT15,000
Volume at dealer's account	30,000 shares
Sugi Corp's share price on 30 Apr	MNT 16,000
Urade Securities' client Mr Z agrees to buy Sugi Corp's shares	at MNT16,000, 30,000 shares

Urade Securities' dealer made profit in this transaction:

$$\text{MNT}16,000 \times 30,000 \text{ shares} - \text{MNT}15,000 \times 30,000 \text{ shares} = \text{MNT}30\text{m}$$

## 2a. Aggregate statements of income for Japanese securities industry

JPY bn

	Mar-10	Mar-11	Mar-12	Mar-13	Mar-14
<b>Commission received</b>	2,128	1,898	1,635	1,794	2,461
<b>Net gain on trading</b>	805	540	636	896	1,098
<b>Other revenues</b>	32	53	33	41	49
<b>Operating revenues</b>	3,382	2,920	2,711	3,171	4,089
<b>Net financial revenues</b>	149	161	167	166	192
<b>Net operating revenues</b>	3,114	2,652	2,471	2,898	3,801
<b>Selling, general and admin expenses</b>	2,774	2,618	2,286	2,317	2,628
<b>Operating income</b>	340	34	185	581	1,172
<b>Net non-operating income</b>	-7	53	33	25	17
<b>Income before tax</b>	334	87	218	606	1,189
<b>Extraordinary items</b>	-19	-198	-42	8	26
<b>Income tax</b>	112	160	202	156	301
<b>Net income</b>	202	-271	-26	457	914

Source: Japan Securities Dealers Association

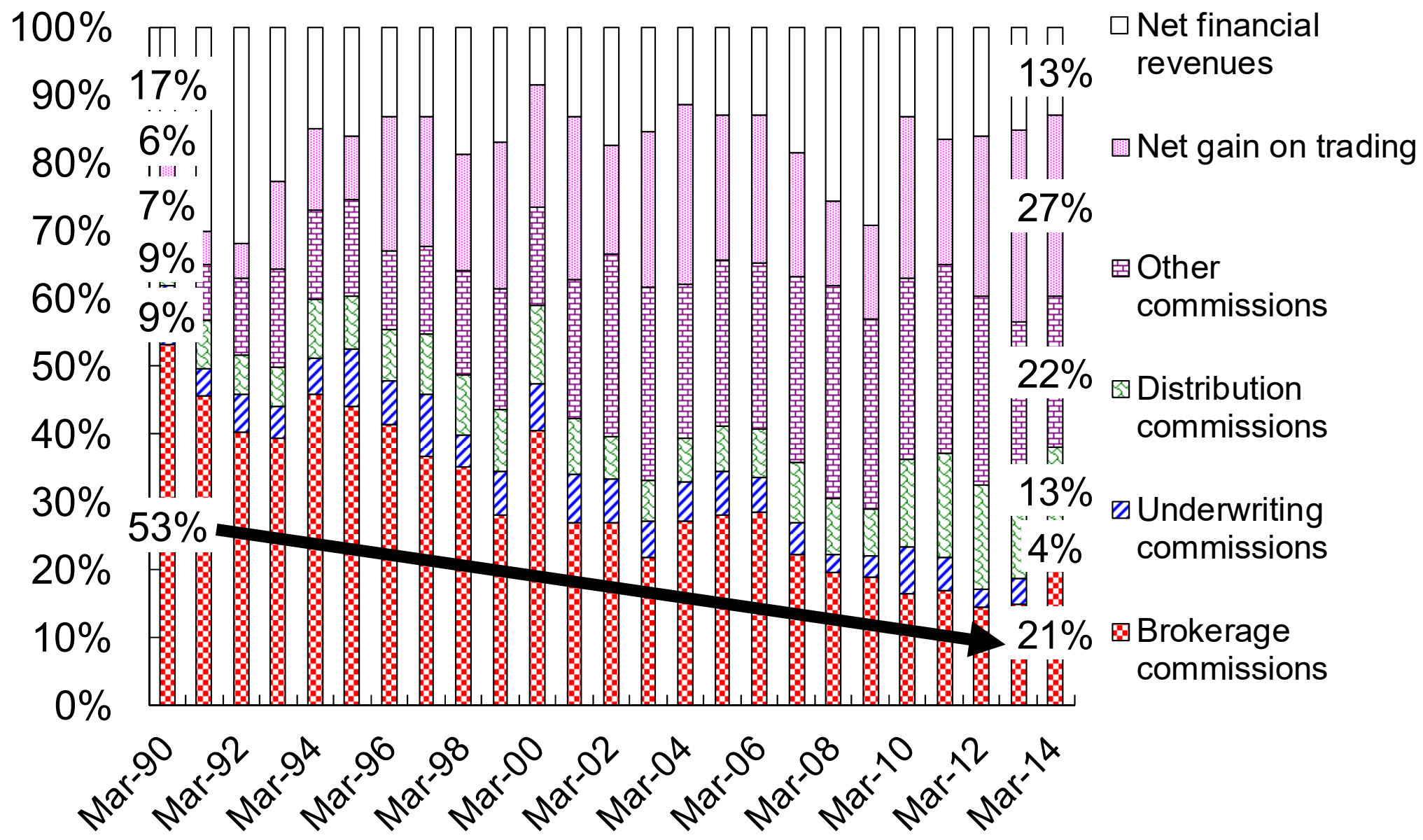
## 2a. Brief description for securities' companies' statements of income

Item	Description
<b>Commission received</b>	Brokerage commission, underwriting commission etc.
<b>Net gain on trading</b>	Dealing
<b>Operating revenues</b>	Commission received + Net gain on trading
<b>Net financial revenues</b>	Dividend income, bond coupon income, margin trade income, securities lending income etc.
<b>Net operating revenues</b>	Operating revenues + net financial revenues
<b>Selling, general and admin expenses</b>	Employees' compensation & benefits, occupancy & rental, trading related expense, IT system, office supplies etc.
<b>Operating income</b>	Profit from operations
<b>Net non-operating income</b>	Net interest & investment income not included in net financial revenues
<b>Income before tax</b>	Profit before corporate tax
<b>Extraordinary items</b>	Temporary items such as one-time charge
<b>Income tax</b>	Corporate tax
<b>Net income</b>	Net profit

Source: Daiwa Institute of Research

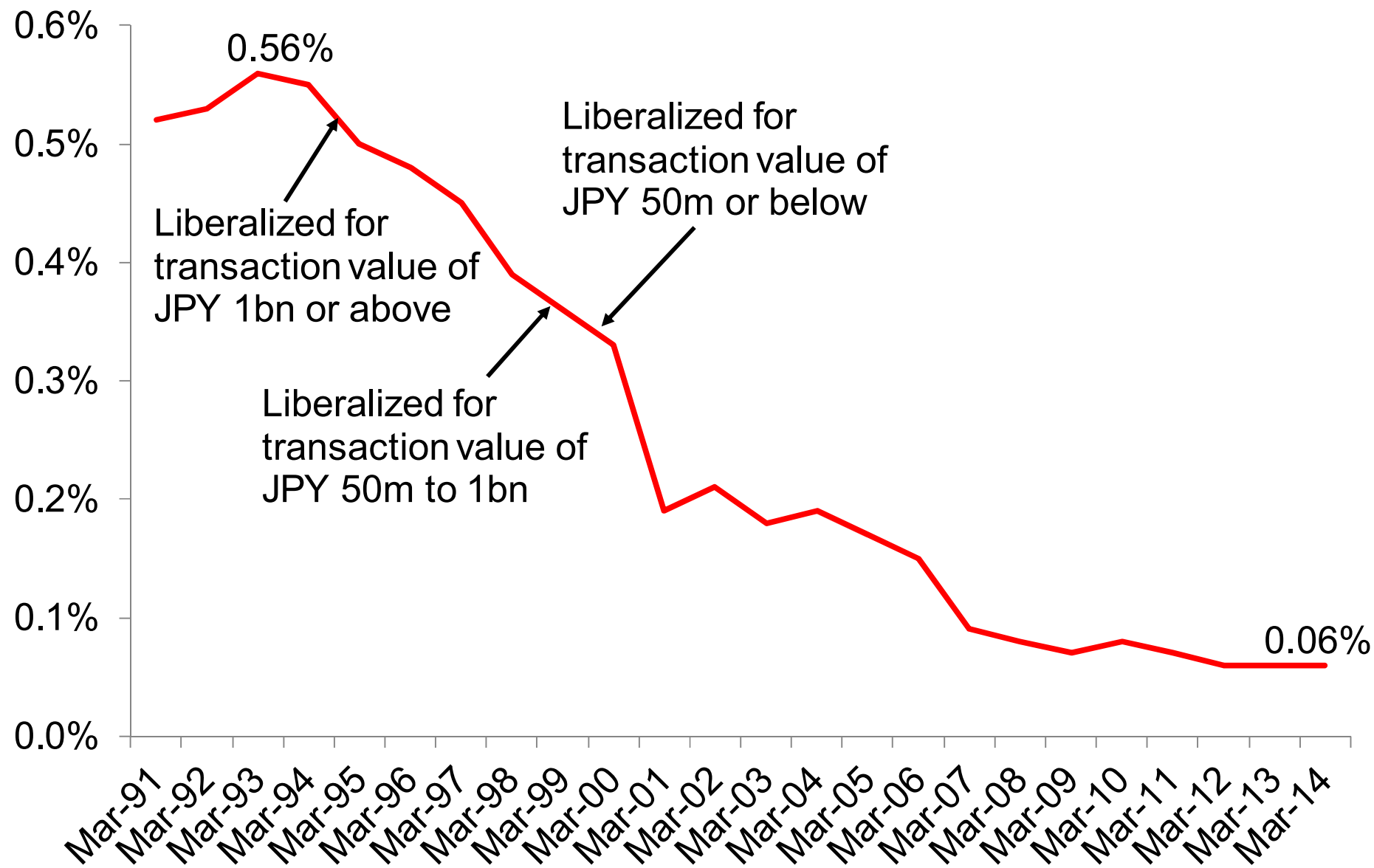


## 2b. Net operating revenue breakdown for Japanese securities industry



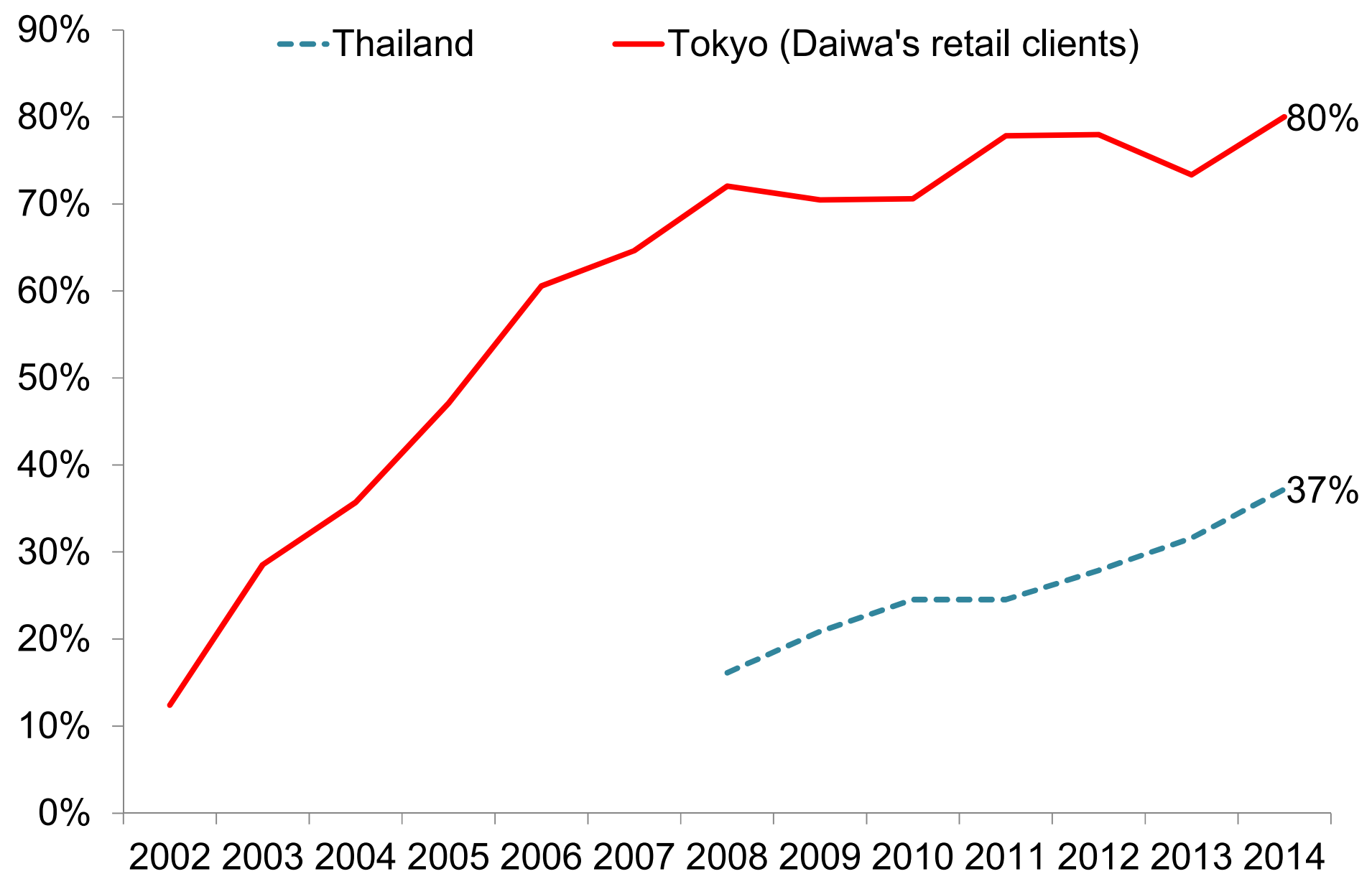
Source: Japan Securities Dealers Association

## 2-c. Declines in brokerage business: Liberalization of brokerage commission



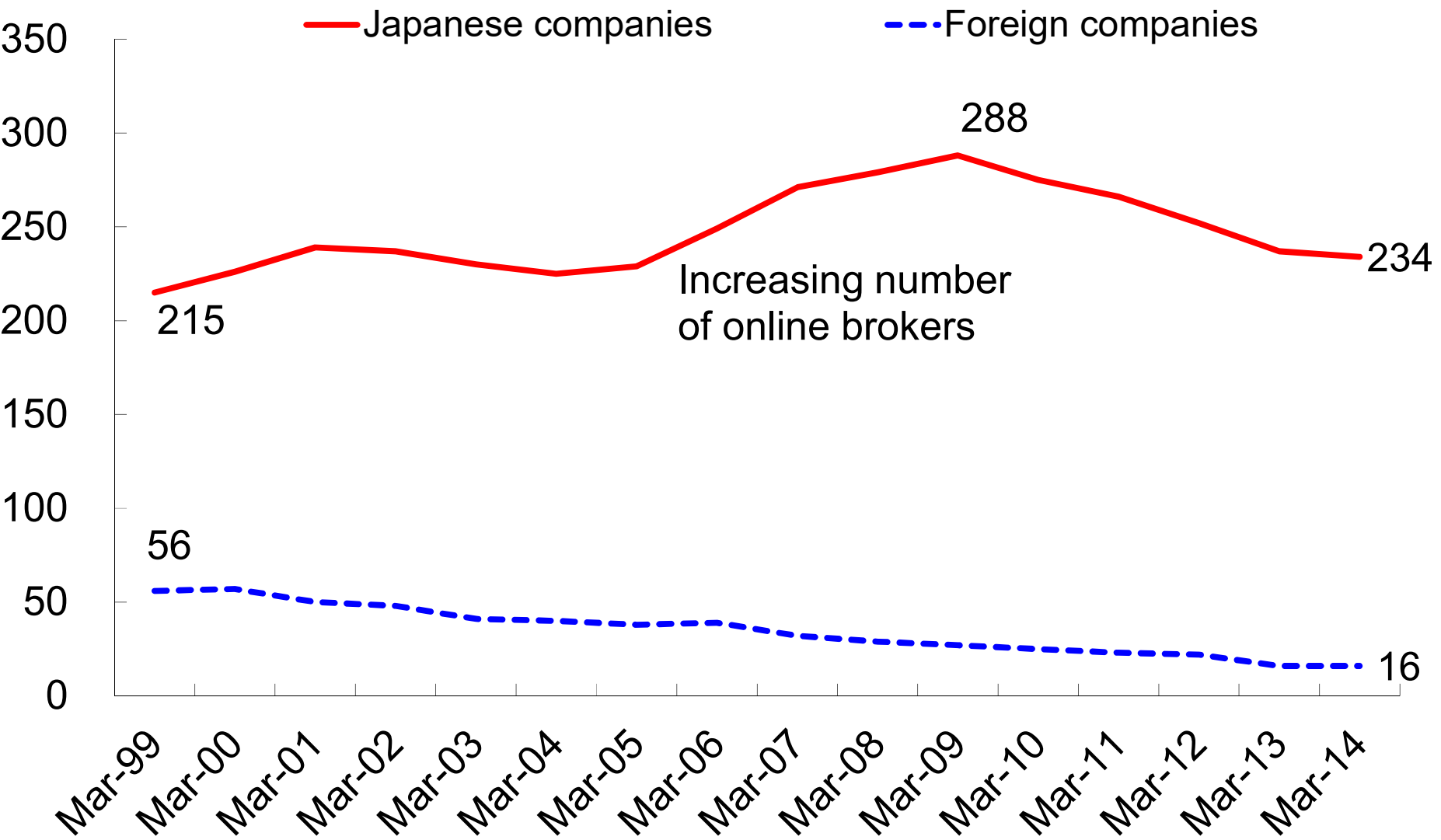
Source: Tokyo Stock Exchange

**2-d. Lowering brokerage commission rate: Rising % share of online trading**



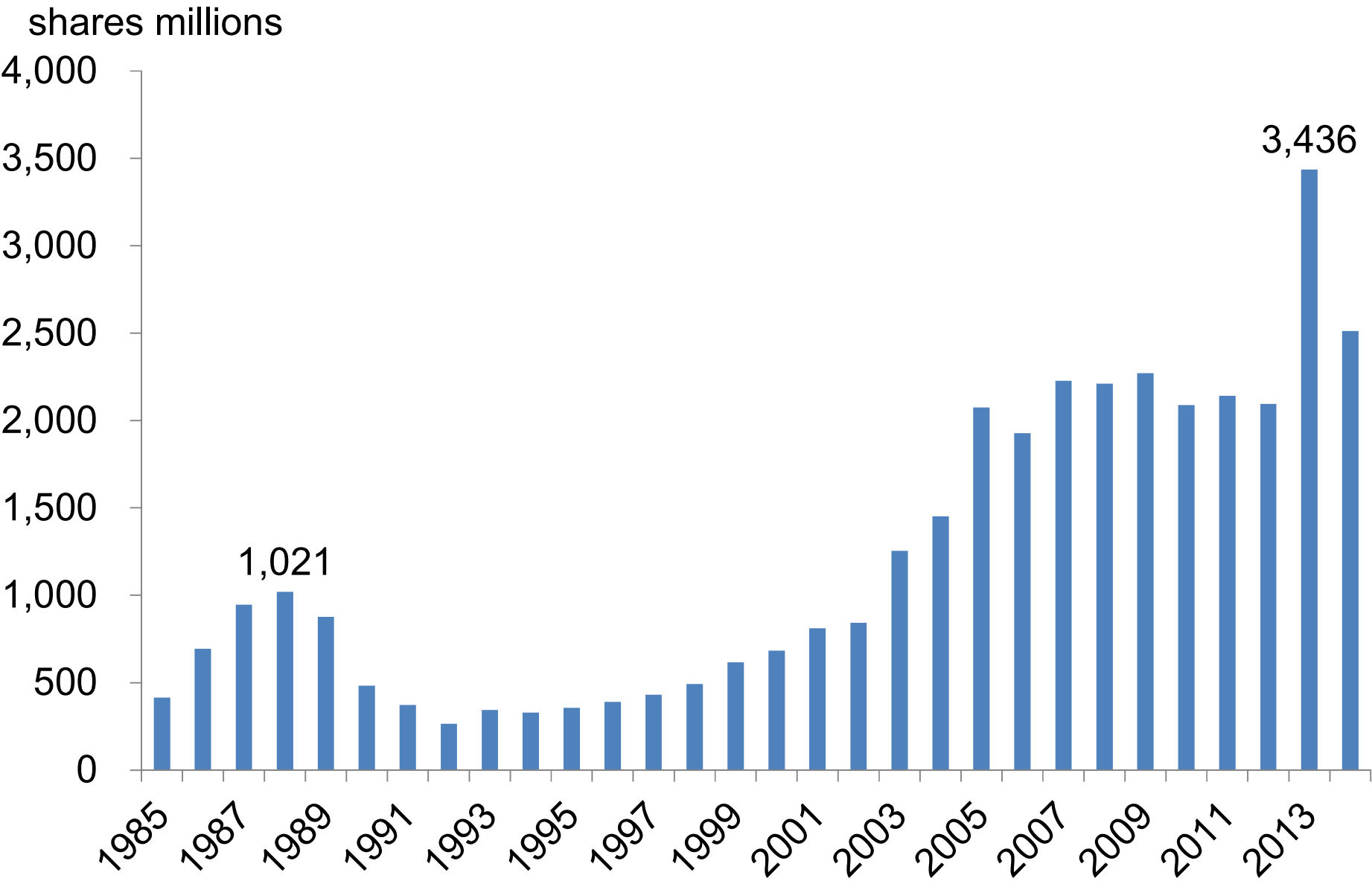
Source: Daiwa Securities Group, Inc., Stock Exchange of Thailand

**2-e. Online brokers: Trend in number of securities companies in Japan**



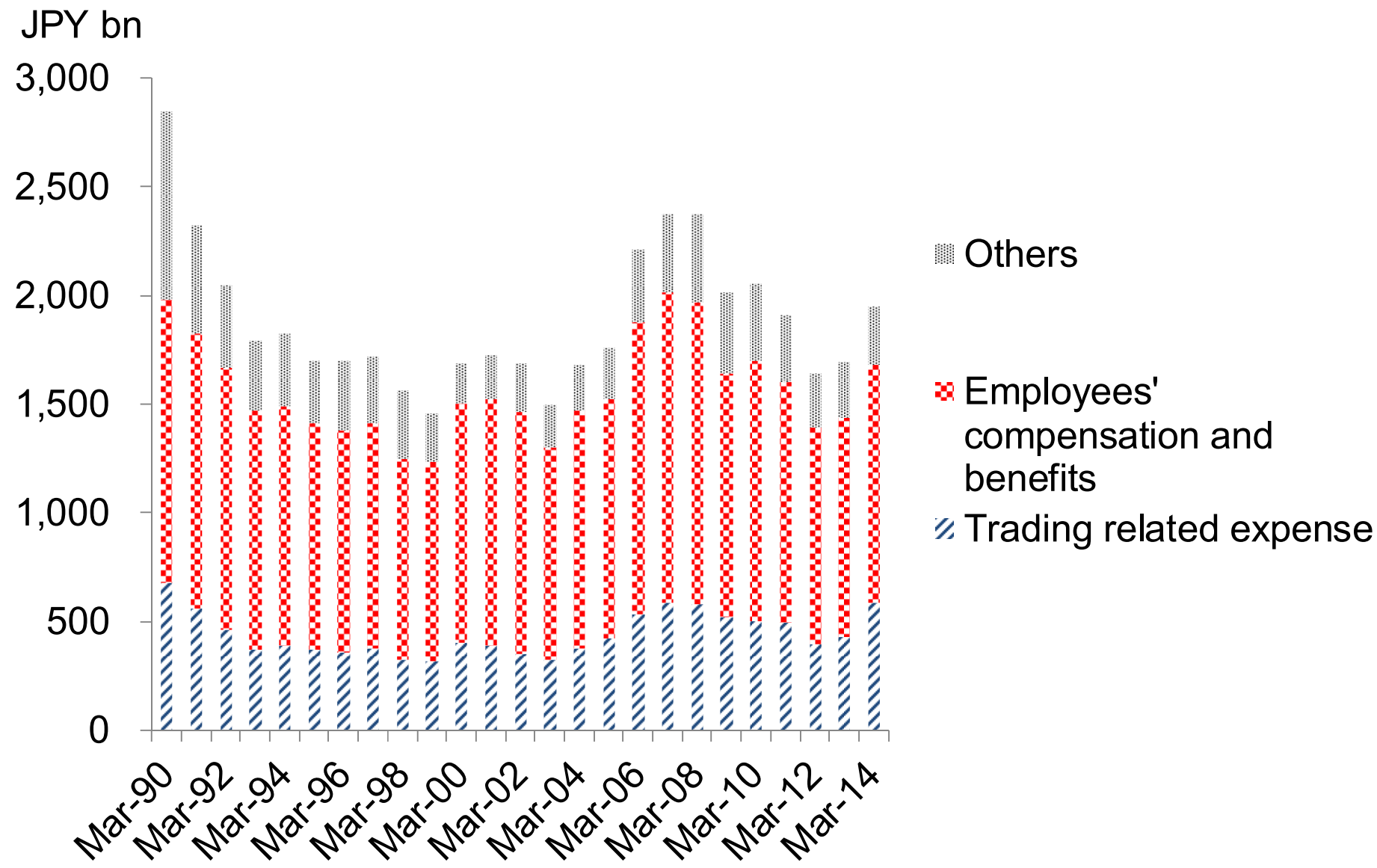
Source: Japan Securities Dealers Association

**2-f. Lower commission rates: Increased daily avg trading vol at Tokyo Stock Exchange**



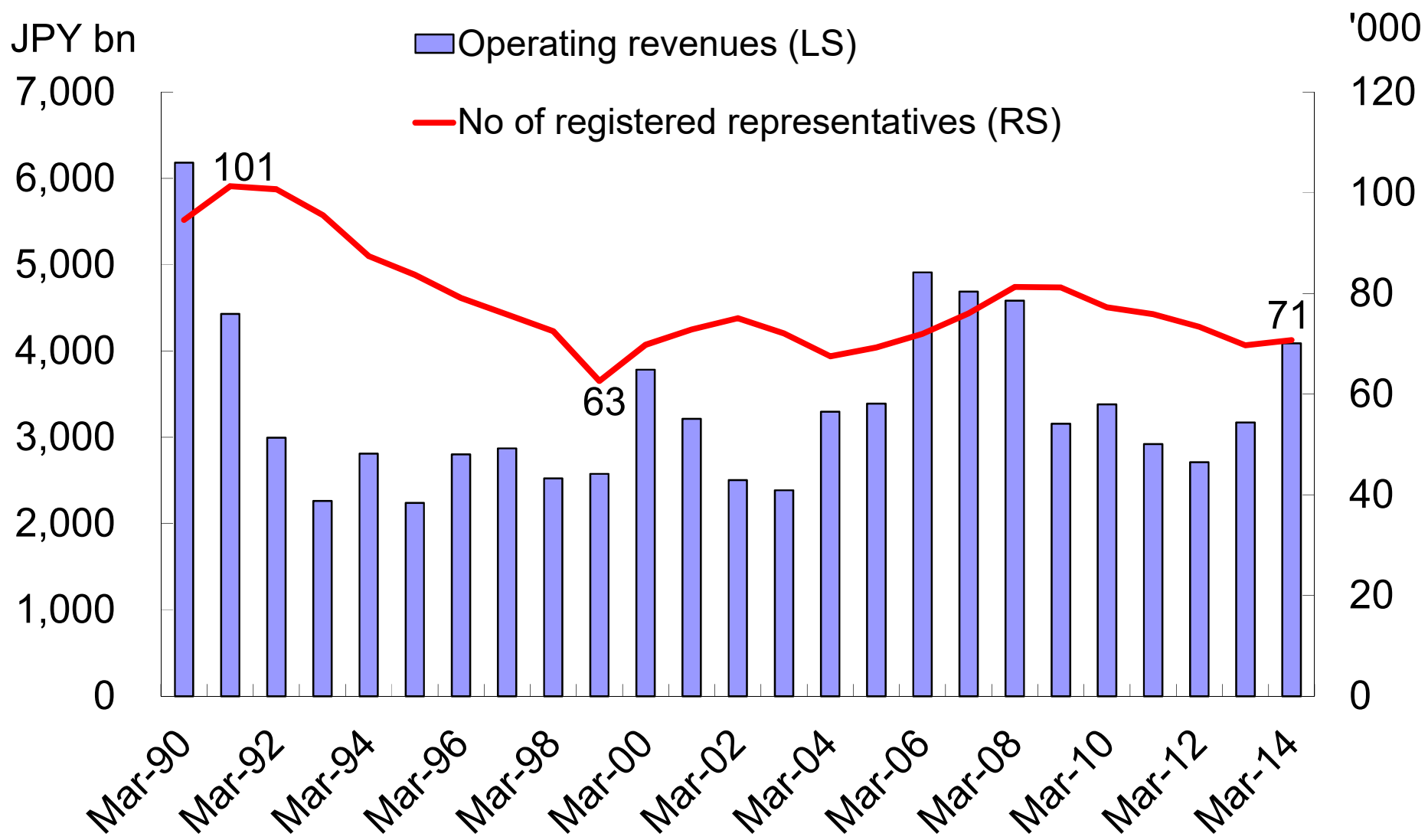
Source: Tokyo Stock Exchange

**2-g. Selling, general and administrative (SGA) expenses for Japanese securities industry**



Source: Japan Securities Dealers Association

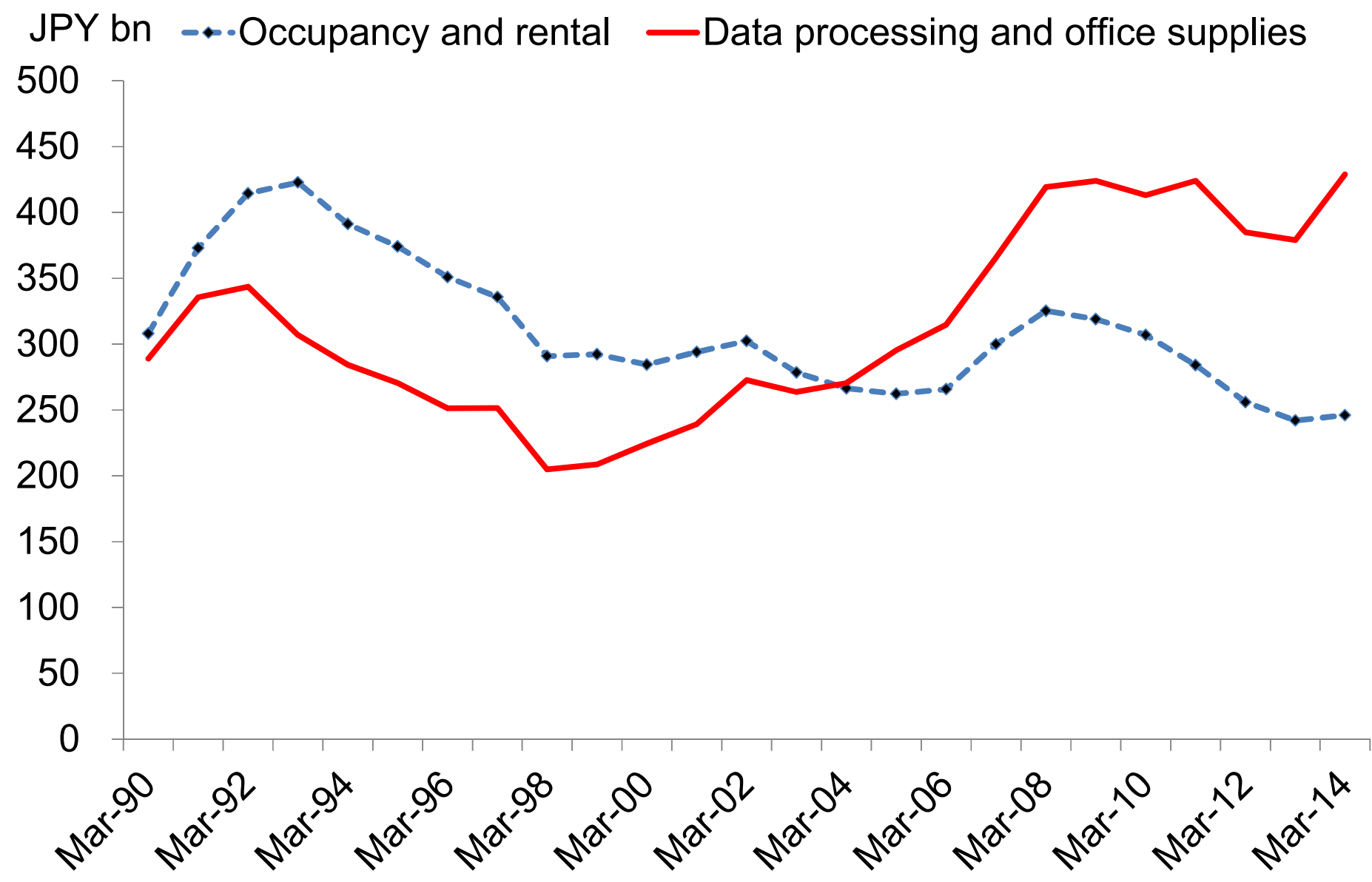
**2-h. Largest fixed cost: Number of registered representatives decreased**



Source: Japan Securities Dealers Association



## 2-i. SGA: Declining office cost and increasing IT system/OA cost



Source: Japan Securities Dealers Association

### 3-a. Consolidated income statement for Daiwa Securities Group (1)

	JPY bn							
	Mar-08	Mar-09	Mar-10	Mar-11	Mar-12	Mar-13	Mar-14	Mar-15
<b>Total operating revenue</b>	825	414	538	403	422	525	643	659
<b>Net operating revenue</b>	447	200	458	319	336	417	542	532
<b>Total selling, general and admin expenses</b>	364	343	363	364	360	333	357	361
<b>Operating income (loss)</b>	84	-144	95	-45	-24	84	185	171
<b>Ordinary income (loss)</b>	90	-141	103	-33	-12	95	197	185
<b>Income (loss) before income tax</b>	82	-164	97	-35	-17	92	196	182
<b>Net income (loss)</b>	46	-85	43	-37	-39	73	169	148

Source: Daiwa Securities Group, Inc.

### 3-b. Consolidated income statement for Daiwa Securities Group (2)

	JPY bn							
	Mar-08	Mar-09	Mar-10	Mar-11	Mar-12	Mar-13	Mar-14	Mar-15
<b>Brokerage commission</b>	84	56	56	51	41	49	90	70
<b>Underwriting commission</b>	25	21	54	26	20	27	30	38
<b>Distribution commission</b>	43	19	33	32	49	45	53	41
<b>Other commission</b>	143	113	109	110	111	109	130	143
<b>Total commission received</b>	294	209	253	219	221	230	302	291
<b>Net trading income</b>	103	41	111	92	79	124	156	157
<b>Net gain (loss) on private equity etc</b>	19	-79	76	-17	2	17	17	7
<b>Financial revenue</b>	358	193	55	72	80	93	108	126
<b>Other operating revenue</b>	50	51	44	37	40	63	59	78
<b>Total operating revenue</b>	825	414	538	403	422	525	643	659
<b>Financial expenses</b>	340	176	48	58	60	70	60	80
<b>Other operating expenses</b>	38	38	32	26	27	38	41	47
<b>Net operating revenue</b>	447	200	458	319	336	417	542	532

Source: Daiwa Securities Group, Inc.

### 3-c. Consolidated income statement for Daiwa Securities Group (3)

	JPY bn							
	Mar-08	Mar-09	Mar-10	Mar-11	Mar-12	Mar-13	Mar-14	Mar-15
<b>Trading related expenses</b>	85	66	62	70	69	67	74	74
<b>Personal expenses</b>	157	142	170	160	158	157	177	182
<b>Real estate expenses</b>	39	44	44	45	45	38	36	37
<b>Office cost</b>	30	30	26	27	28	23	25	25
<b>Depreciation</b>	28	36	39	39	40	31	27	24
<b>Taxes and dues</b>	7	7	8	7	7	6	7	7
<b>Others</b>	18	20	14	15	13	12	12	12
<b>Total selling, general and admin expenses</b>	364	343	363	364	360	333	357	361

Source: Daiwa Securities Group, Inc.

### 3-d. Consolidated income statement for Daiwa Securities Group (4)

	JPY bn							
	Mar-08	Mar-09	Mar-10	Mar-11	Mar-12	Mar-13	Mar-14	Mar-15
<b>Operating income (loss)</b>	84	-144	95	-45	-24	84	185	171
<b>Non-operating income</b>	10	8	9	16	13	14	15	16
<b>Non-operating expenses</b>	3	5	2	3	1	3	3	3
<b>Ordinary income (loss)</b>	90	-141	103	-33	-12	95	197	185
<b>Extraordinary income</b>	4	6	2	9	40	10	10	5
<b>Extraordinary loss</b>	12	29	7	11	44	13	11	8
<b>Income (loss) before income tax</b>	82	-164	97	-35	-17	92	196	182
<b>Income tax</b>	41	0	50	10	24	12	18	27
<b>Minority interests</b>	-5	-61	4	-7	-2	7	8	6
<b>Net income (loss)</b>	46	-85	43	-37	-39	73	169	148

Source: Daiwa Securities Group, Inc.

### 3-e. Consolidated balance sheet for Daiwa Securities Group, Mar-15

JPY bn

<b>Cash and deposits</b>	2,985	<b>Trading products</b>	6,014
<b>Short-term investment securities</b>	2,629	<b>Loans payable secured by securities</b>	7,553
<b>Trading products</b>	8,304	<b>Deposits for banking business</b>	2,745
<b>Operational investment securities</b>	119	<b>Short-term loans payable</b>	1,011
<b>Loans secured by securities</b>	6,728	<b>Commercial papers</b>	388
<b>Current assets</b>	22,190	<b>Current portion of bonds</b>	264
<b>Property, plant and equipment</b>	458	<b>Current liabilities</b>	19,353
<b>Intangible assets</b>	77	<b>Bonds payable</b>	1,179
<b>Investments and other assets</b>	275	<b>Long-term loans payable</b>	946
<b>Non-current assets</b>	810	<b>Non-current liabilities</b>	2,209
		<b>Total liabilities</b>	21,566
		<b>Shareholders' equity</b>	1,434
<b>Total assets</b>	23,001	<b>Total liabilities and shareholders' equity</b>	23,001

### 3-f. Capital adequacy ratio

---

#### 1. Simple CAR

$\text{CAR} = \text{Shareholders' equity} / \text{Total assets}$

Daiwa Securities Group's CAR is 5.4% as at Mar-15.

#### 2. CAR by Financial Instruments and Exchange Act

$\text{CAR} = \text{Capital that are not immobilized} / \text{Risk assets}$

FSA's requirement is a securities company's CAR should be above 140%.

Daiwa Securities Group's CAR is 288.5% as at Mar-15.

#### 3. CAR by Basel 3

$\text{CAR} = \text{Total qualifying capital} / \text{Total risk-weighted assets}$

Basel 3's requirement is a financial institution's CAR should be 8% or above.

Daiwa Securities Group's CAR is 22.3% as at Dec-14.



### 3-g. Capital adequacy ratio, Basel 3 basis

		JPY bn	
		Sep-14	Dec-14
Total Qualifying Capital	(D)=(A)+(B)+(C)	11,598	12,387
Common Equity Tier 1	(A)	10,854	11,338
Additional Tier 1	(B)	288	491
Tier 2 Capital	(C)	455	557
Total Risk-Weighted Assets	(E)	51,721	55,478
Credit Risk		30,717	32,155
Market Risk *1		11,723	13,570
Operational Risk *1		9,281	9,752
Consolidated Common Equity Tier 1 Capital Adequacy Ratio	(A)/(E)	20.9%	20.4%
Consolidated Tier 1 Capital Adequacy Ratio	((A)+(B))/(E)	21.5%	21.3%
Consolidated Total Capital Adequacy Ratio *2	(D)/(E)	22.4%	22.3%

\*1 Market and Operational Risk hereunder is computed by multiplying each risk amount by 12.5 (the Reciprocal of 8%).

\*2 Consolidated Capital Adequacy Ratio hereunder is calculated under the principal of Financial Service Agency Public Notice 130 of the Financial Instruments and the Exchange Act (Article 57-17-1).

# **Project for Capacity Building of Capital Market in Mongolia: Case Study – BDSec's annual financial summary**

---

1 May 2015

Daiwa Institute of Research  
Japan Economic Research Institute

## 1. Income statement for BDSec (1)

MNT'000

	<b>Dec-12</b>	<b>Dec-13</b>	<b>Dec-14</b>
<b>Operating revenues</b>	5,898,647	2,596,428	2,299,827
<b>Financial revenues</b>	53,781	39,715	163,693
<b>Net operating revenues</b>	5,952,428	2,636,143	2,463,520
<b>Cost of investment securities</b>	1,093,568	650,221	1,259,413
<b>Gross profit</b>	4,858,859	1,985,922	1,204,107
<b>Operating expense</b>	3,108,205	1,636,030	1,720,019
<b>Non-operating income</b>	-85,120	-26,924	-19,289
<b>Income before tax</b>	1,665,534	322,969	-535,201
<b>Income tax</b>	174,140	35,086	-50,479
<b>Net income</b>	1,491,394	287,883	-484,722

Source: BDSec

## 2. Income statement for BDSec (2)

	MNT'000		
	Dec-12	Dec-13	Dec-14
<b>Brokerage and trading income</b>	5,695,402	2,114,899	1,789,532
<b>Underwriting income</b>	67,114	206,833	-
<b>Investment and financial advice</b>	15,567	124,333	369,339
<b>Other income</b>	120,565	150,364	140,955
<b>Operating revenues</b>	5,898,647	2,596,428	2,299,827
<b>Interest income</b>	35,878	36,055	157,888
<b>Dividend income</b>	1,059	3,197	5,805
<b>Others</b>	16,844	463	-
<b>Financial revenues</b>	53,781	39,715	163,693
<b>Operating income</b>	5,952,428	2,636,143	2,463,520

Source: BDSec

### 3. Income statement for BDSec (3)

	MNT'000		
	Dec-12	Dec-13	Dec-14
<b>Wages and salaries</b>	395,178	505,525	649,992
<b>Social securities contributions</b>	43,814	56,693	72,621
<b>Maintenance costs</b>	32,508	23,187	23,293
<b>Operating costs</b>	80,518	76,851	113,163
<b>Allowance</b>	25,065	133,062	89,247
<b>Transportation expense</b>	621	4,099	-
<b>Depreciation</b>	239,184	274,650	268,784
<b>Advertising expense</b>	62,480	22,558	37,737
<b>Postage</b>	10,993	25,071	23,681
<b>Fuel cost</b>	23,816	30,276	23,683
<b>Remuneration</b>	-	-	14,200
<b>Interest expense</b>	-	7,459	2,707
<b>FRC service fee</b>	2,300	2,300	2,300
<b>Mongolian Stock Exchange membership fee</b>	1,000	5,000	2,500
<b>MSCH&amp;CD service fee</b>	193	257	328
<b>Regulatory fees</b>	232,139	31,364	9,853
<b>Mongolian Stock Exchange commission</b>	744,356	173,051	112,113
<b>MSCH&amp;CD commission</b>	665,966	121,319	63,550
<b>Other expenses</b>	548,076	143,308	210,268
<b>Operating expenses</b>	3,108,205	1,636,030	1,720,019

## 4. Balance sheet for BDSec

				MNT'000			
	Dec-12	Dec-13	Dec-14		Dec-12	Dec-13	Dec-14
<b>Cash and equivalents</b>	661,214	857,856	5,119,886	<b>Accounts payable</b>	175,323	75,557	55,551
<b>Short-term investments</b>	3,800,784	3,683,799	3,892,570	<b>Salaries payable</b>	18,296	17,418	21,101
<b>Securities fair value adjustment(+/-)</b>	619,458	445,419	433,734	<b>Taxes payable</b>	9,710	12,696	40,287
<b>Securities risk protection fund</b>	-33,000	-33,000	-33,000	<b>Health insurance premium payable</b>	7,478	-	605
<b>Trade and other receivable</b>	938,104	1,290,442	1,423,156	<b>Dividends payable</b>	0	660,000	678,469
<b>Others</b>	-	-	24,486	<b>Short-term loans</b>	-	-	720,000
<b>Current assets</b>	5,986,559	6,244,515	10,860,832	<b>Others</b>	8,411	21,485	22,642
<b>Non-current assets</b>	3,763,661	3,505,293	3,866,825	<b>Current liabilities</b>	219,217	787,156	1,538,654
				<b>Non-current liabilities</b>	61,946	44,542	-
				<b>Total liabilities</b>	281,163	831,698	1,538,654
				<b>Shareholders' equity</b>	9,469,057	8,918,111	13,189,002
<b>Total assets</b>	9,750,220	9,749,808	14,727,657	<b>Total liabilities and shareholders' equity</b>	9,750,220	9,749,808	14,727,657

# Basics & Scheduling

---

Project for Capacity Building of Capital Market in Mongolia  
Training Course for Securities Companies (1)

Shinji Ohno  
JICA Consultant Team

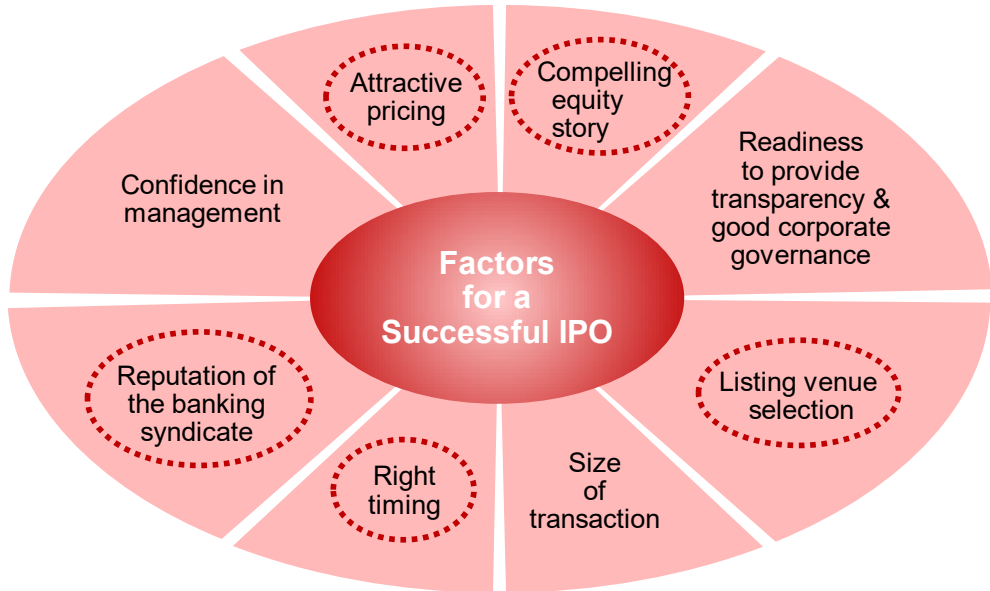
## Contents

---

- What are the key roles of a securities company as an Underwriter in the IPO process ?
- What is crucial steps and factors when considering IPO scheduling (venue, timeline)?



# Factors for a Successful IPO



2

# Consultation for Pilot IPO & Dual Listing Companies

Task Item	Current Status <sup>(*)</sup>	Consulting Needs (Y/N)	Priority (H/M/L)	Comments
<b>Scheduling</b>				
Identifying an appropriate venue/scheme				
Preparing timeline				
Designing & implementing ESOP				
<b>Valuation</b>				
<b>Accounting System</b>				
<b>HR / General Affairs</b>				
<b>Capital Policy</b>				
Pre-IPO financing				
Identifying appropriate shareholding structure				
Identifying measures to change shareholding structure				
Scheduling for altering capital structure				
<b>Corporate Governance / Compliance</b>				
<b>Budget Planning</b>				
<b>Internal Auditing</b>				
<b>Pre-IPO Restructuring</b>				
<b>Documentation</b>				
<b>Post IPO Disclosure</b>				
<b>IR Activities</b>				

3

## Role of Underwriter (1)

### The Underwriter is

- ✓ the most important *partner* for the Issuer and the principal player in the IPO
- ✓ “*recommender*” of the issuer ⇒ if sent off an immature company to the market, it needs to take certain responsibility (damage reputation)



### Advice on ...

- Listing schedule and Selection of IPO market
- Business Plan and Capital Policy
- Coordinate activities of all parties
- Drafting prospectus and listing application, etc.
- Marketing strategy for listing
- Issue price, size, timing and distribution
- Coordinate road show
- IR Support
- Capital raising strategy, stabilizing stock price
- Provide necessary market information

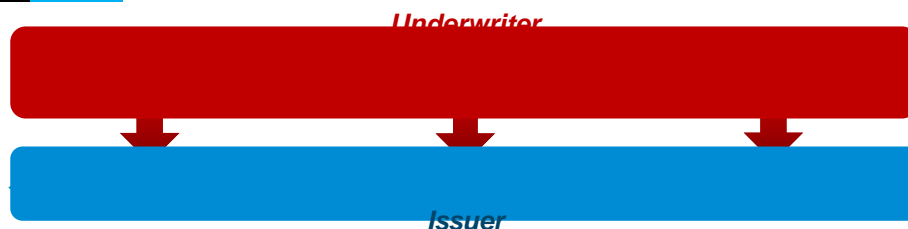
4

## Role of Underwriter (2)

### Underwriter Selection – *factors to be considered by the issuer*

- Sufficient track record and expertise supporting past IPOs
  - ✓ Knowledge of industry, business model
  - ✓ Understanding of listing market's restrictions, rules, etc.
  - ✓ Proposal capabilities for IPO scheduling and capital policy
  - ✓ Underwriter's internal resources
- Well underwriting arrangement : cost/price competitiveness, underwriting commitment
- Strong distribution expertise
- Good proposal capabilities for post-IPO : IR, finance, M&A, etc.

The **Underwriter** needs to provide services from the standpoint of both the *Issuer* and the *Investor*



5

## c.f. Types of Underwriting

---

### 'Firm Commitment' Underwriting

- Issuer sells entire issue to U/W'ers
- U/W'ers then resell them to the public
- U/W'ers make money on the spread btw:
  - the price paid to the issuer and
  - the price received from investors when the shares are sold
- **U/W'ers bear the risk of not being able to sell** the entire issue for more than the cost
- Most common U/W type in US.

#### Firm Commitment as an Option

- Issuer buys a put option from the U/W'er.
- U/W'er gives a call option to investors.
- Issuer's put option becomes real only in the final pricing meeting.

### 'Best Efforts' Underwriting

- U/W'er makes 'best effort' to sell the shares at an agreed offering price
- **Issuer bears the risk of the unsold part**
- IBKs only markets the issue. Prospectus states:
  - Offer price (P)
  - Min # of shares that must be sold ( $Q_{\min}$ )
  - Max # of shares that will be sold ( $Q_{\max}$ )
- If  $Q_{\min}$  is not reached in 90 days (e.g.), investors get their money back from an escrow A/C.
- In US, only **35% of IPOs**, accounting for **13%** of the total money raised.
- **Generally for small firms.**
- Issuers can choose the price itself, otherwise IBKs would force the company to go public at very low price.

6

## c.f. Pricing Issue

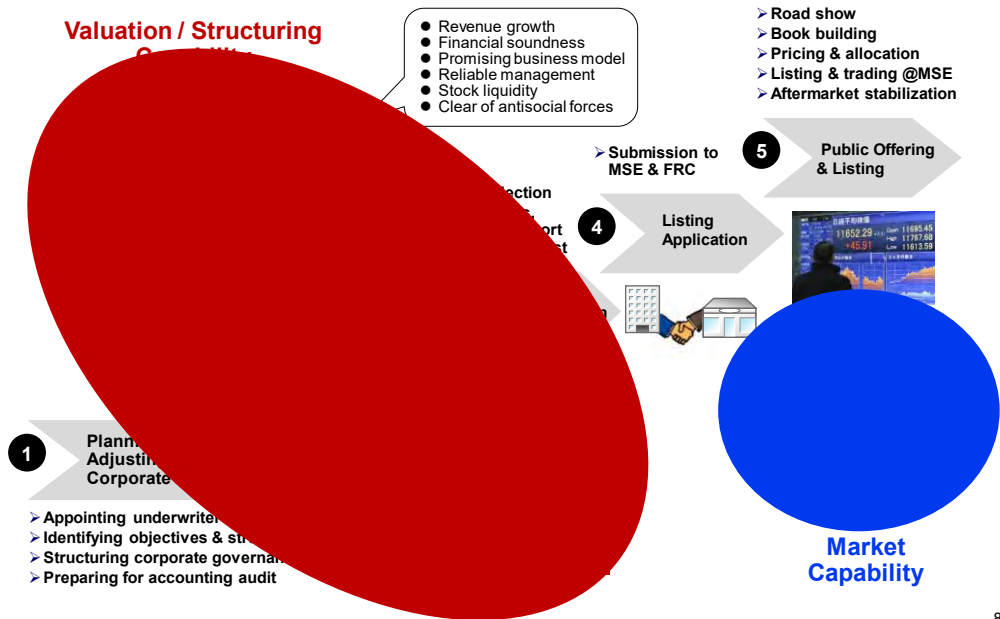
---

### Underpricing

- Defined as '**the difference in price between the closing price on the 1<sup>st</sup> day of trading & the offer price**'
- IPO pricing is very difficult, as no current market price is available.
- General practice, in which Underwriters earn reputations through;
  - ✓ Achieving **higher price than the offer price**
  - ✓ **Selling out the shares**
- **Smaller, riskier IPOs underprice to attract investors.**

7

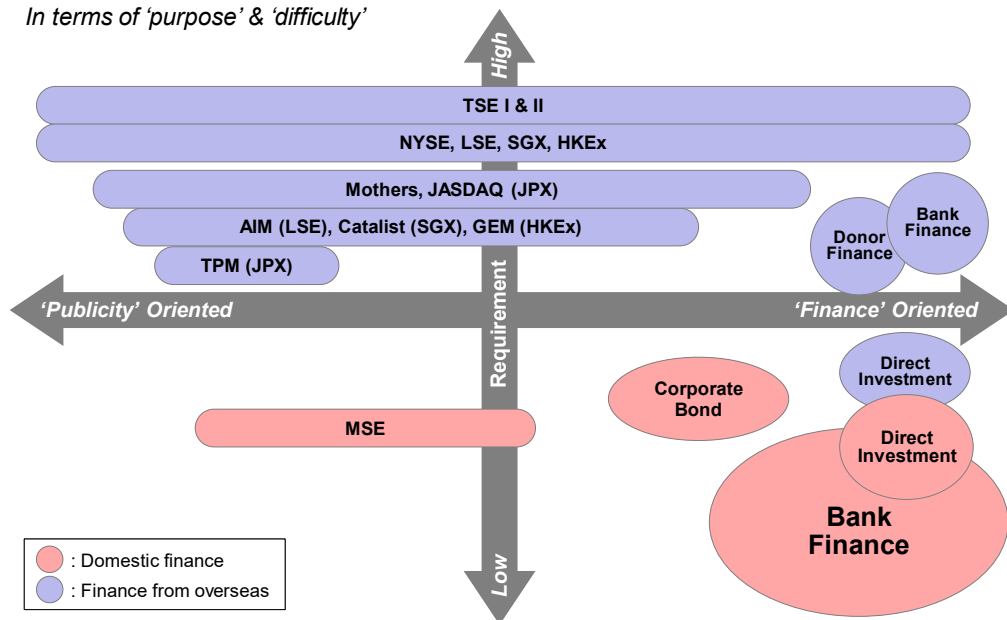
## Typical IPO Process



8

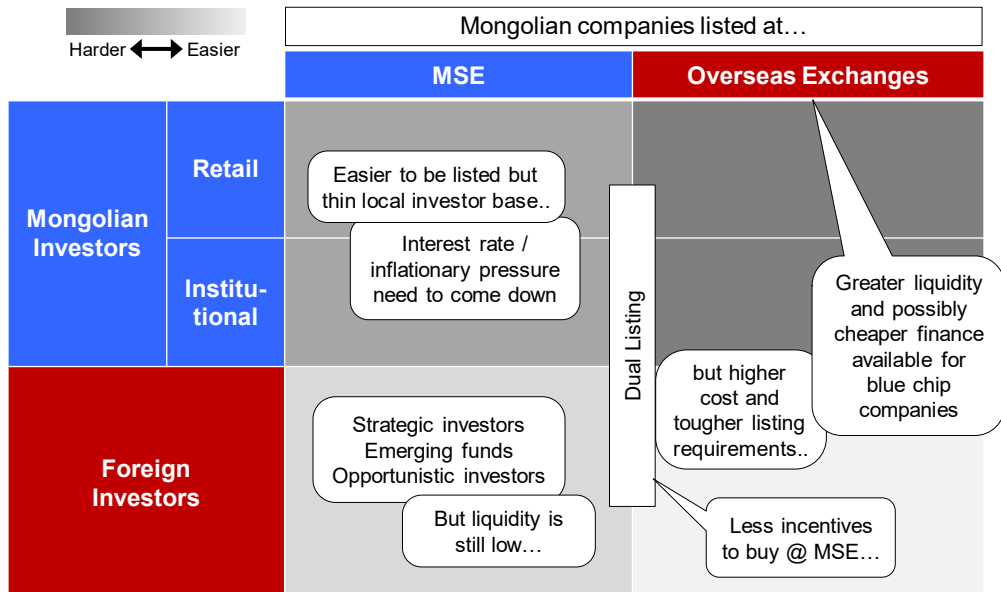
## Consideration of Financing Tools

*In terms of 'purpose' & 'difficulty'*



9

## Consideration of Equity Financing in Mongolia vs Overseas



10

## Consideration of Listing Venue

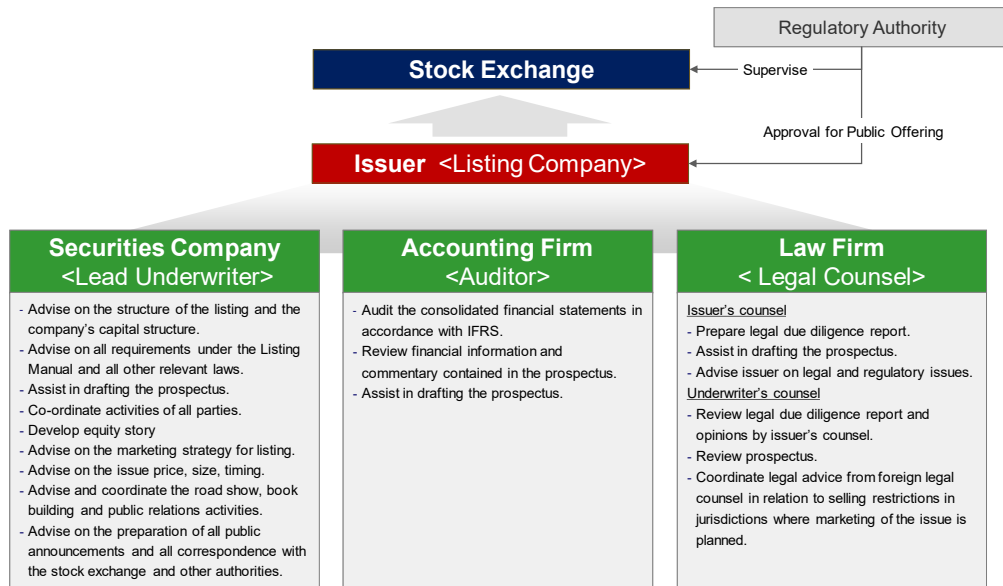
	Mongol Stock Exchange	Tokyo Stock Exchange		Hong Kong Stock Exchange		Singapore Exchange	
Investor base	Limited local investors and frontier market focused foreign investors, PE funds	Extensive institutional investor base, local high net worth individuals and foreign investors		Extensive institutional and private banking investor base, regionally focused to ASEAN equities		Extensive institutional investor base and active local retail investors, domestically focused	
Total market cap	USD 0.63 billion	USD 4,915 billion		USD 3,185 billion		USD 640 billion	
# of listed companies	235	3,511		1,866		769	
Number of IPOs	■ 2015: 1 ■ 2014: 1	■ 2015: 85 ■ 2014: 71		■ 2015: 124 ■ 2014: 115		■ 2015: 14 ■ 2014: 30	
IPO funds raised	■ 2015: USD 2.6 mil ■ 2014: USD 37.2 mil	■ 2015: USD 14.6 bn ■ 2014: USD 10.5 bn		■ 2015: USD 26.1 bn ■ 2014: USD 29.7 bn		■ 2015: USD 0.4 bn ■ 2014: USD 2.4 bn	
Listing Requirements	II Classification	1 <sup>st</sup> Section	Mothers	Main Board	GEM	Main Board	Catalist
Listing format	Primary & secondary listing	Primary & secondary listing		Primary & secondary listing	Primary listing only	Primary & secondary listing	Primary listing only
Min # of shareholders	None	2,200	200	300	100	500	200
Free-float ratio	15%	35%	25%	25%	25%	12-25%	15%
Operating track record	2 years	3 years	1 year	3 years	2 years	3 years	None
Financial requirements	Min market cap (No financials)	Either Min profit or Min sales & market cap		Either Min profit & market cap or Min sales & market cap	Min cash flow and market cap	Either Min profit, Min profit & market cap, or Min sales & market cap	None

Sources: HP of MSE, TSE, HKE, SGX

11

## Key Parties Involved in IPO Process

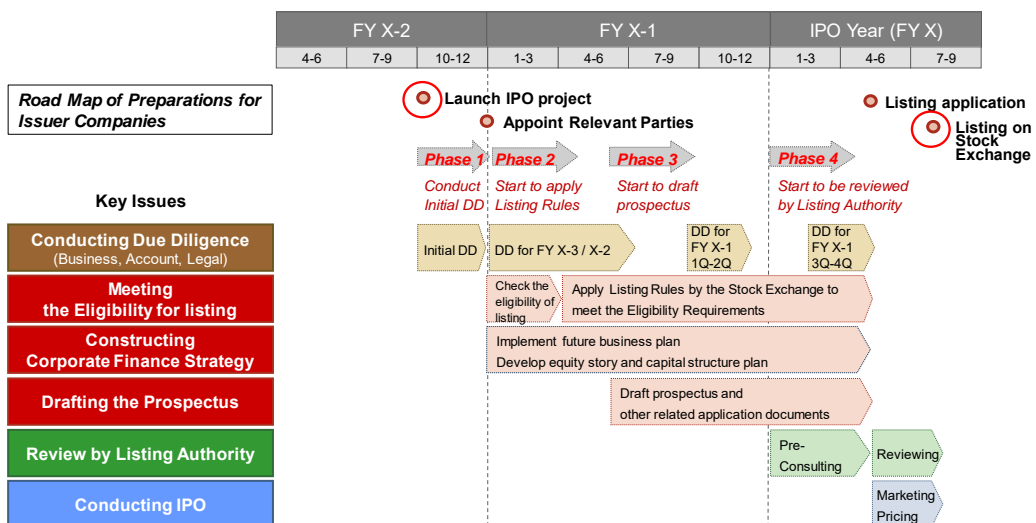
- Appoint a team of advisors having deep experience and a strong grasp of regulatory trends



12

## Scheduling IPO Journey (1) – Preparations for the IPO

*This schedule is based on typical IPO process in major foreign markets but subject to change depending on each cases*



13

## Scheduling IPO Journey (2) – Consideration of Target Timing

*Tentatively set Target Timing of IPO from **Internal Factor***

Consider timing of IPO mainly focusing on the following **five view points**

1. Issuer's business target and strategy
2. Timing of satisfying the listing requirements
3. Timing of achieving profitability and growth base expected by the investors
4. Capital policy and strategy
5. Sufficient period of time for establishment of internal management and control system



According to target IPO timing,

***Plan a working schedule for IPO preparation***

and..

**Get ready for the opening of the “IPO windows of opportunity”**

14

## Scheduling IPO Journey (3) - Timing the Market

*Decide the Timing of IPO from **External Factor** “**Windows of Opportunity**”*

***Timing is crucial*** – Timing of IPO can strongly impact stock performance

- ○ If good timing : Not only provides the issuer with an optimal valuation but will provide its IPO investors with the greatest upside in their investment after the IPO
- × If bad timing : Shares may have to be offered at a lower price or the stock price will drop in the aftermarket
- There are clear “**windows of opportunity**” that open and close for IPO issuers
- Determinants of suitability
  - ✓ General stock market condition
  - ✓ Industry market condition
  - ✓ Frequency and size of all IPO's in the financial cycle



*Many factors influence the stock market*

- Political environments
- Macro economic conditions (Interest rates, Inflation)
- Micro economic forecast, etc

➡ ***Each market/country has its own factors***

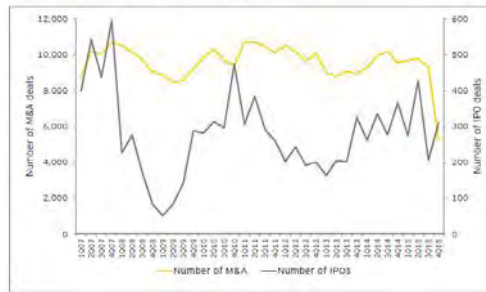


15

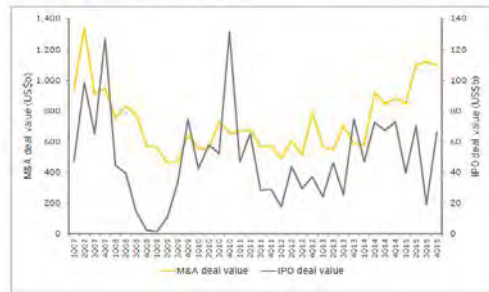


## Scheduling IPO Journey (4) – Common Mistake

Global IPO and M&A by deal numbers



Global IPO and M&A by deal value



Sources: EY Global IPO Trends

One of the common mistakes of newly listed companies is to *hurry into their IPO journeys before the companies are ready*

The frequent rush to go public is due to ...

- Company's immediate need for capital
- Pressure from its stakeholders (board members, owners, etc.)
- Desire to capitalize on a limited window of opportunity

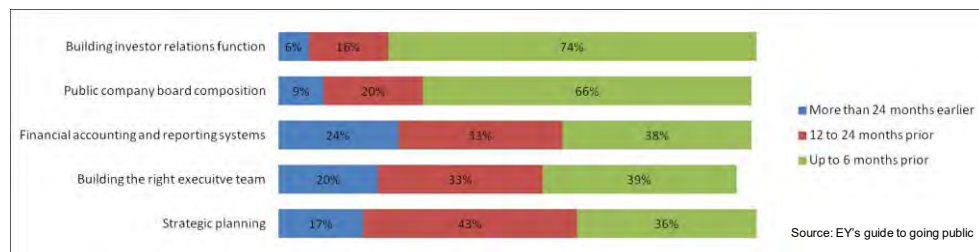


16

## Scheduling IPO Journey (5) – Successful Planning

### 1. Prepare early

Begin the IPO readiness process early enough so that the company acts and operates like a public company before the IPO. Don't underestimate the amount of time the IPO journey will take.



### 2. Have an alternative financing strategy

It is imperative to have the flexibility to execute alternative financing strategies, in case the IPO does not happen or needs to be delayed. e.g. PE, bank or bond financing



17

# **Thank you !!**

For further questions, comments & suggestions, please contact:

Shinji Ohno / Takayuki Urade / Ryota Sugishita

JICA Consulting Team

Office (Local): Room #204, FRC



# МОНГОЛЫН ХӨРӨНГИЙН БИРЖИД ҮНЭТ ЦААС БҮРТГҮҮЛЭХ, ҮНЭТ ЦААСНЫ ТАНИЛЦУУЛГАД ТАВИГДАХ ШААРДЛАГА



## Агуулга

---

- Үнэт цаас гаргагчид тавигдах шаардлага
- Бүртгүүлэх ажиллагааны бэлтгэл
- Биржид бүртгүүлэх хүсэлт гаргах
- Хувьцааны бүртгэлийн шалгуур
- Бүртгэлийн шалгуураас чөлөөлөх буюу хөнгөлөх
- Үнэт цаасны танилцуулга /Prospectus/
- Биржид төлөх төлбөр, хөлс



# Үнэт цаас гаргагчид тавигдах шаардлага



- Санхүү эдийн засгийн үзүүлэлт (Борлуулалт, ашиг орлого, хөрөнгийн өгөөж г.м), зах зээлийн үнэлгээ, хувьцааны тархалт зэргийн хувьд журамд заасан шалгуур, шаардлагыг хангасан байх,

- Аудитын үйл ажиллагаа эрхлэх хуулийн этгээдээ дүгнэлт гаргуулсан байх (ҮЦЗЗТХ 10.6)

- Хууль зүйн зөвлөгөө үзүүлэх хуулийн этгээдээр дүгнэлт гаргуулсан байх (ҮЦЗЗТХ 10.6)



AUDITED

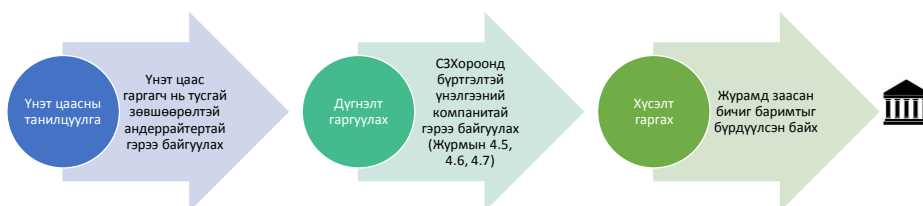


- Хөрөнгийн болон бизнесийн үнэлгээ хийлгэсэн байх

- Андеррайтерийн байгууллагатай гэрээ байгуулсан байх



## Бүртгүүлэх ажиллагааны бэлтгэл



# Биржид бүртгүүлэх хүсэлт гаргах

## Бүрдүүлэх материал

Өргөдөл (Маягт 1)

Үнэт цаас гаргагчийн мэдэгдэл (Маягт 3)

Андеррайтерийн мэдэгдэл (Маягт 4)

Үнэт цаас гаргах тухай эрх бүхий этгээдийн шийдвэр

Үнэт цаасны танилцуулга

Журмын 4.5, 4.6, 4.7-д заасан хууль, үнэлгээ болон аудитын дүгнэлт

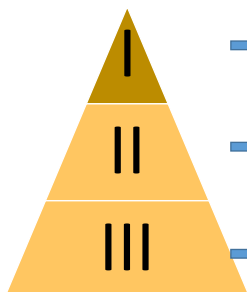
Хөндлөнгийн шинжээч, мэргэжилтэн оролцсон бол журмын 4.4-т заасан үнэлэлт, дүгнэлт

Өргөдөл хүлээн авах, хянах үйлчилгээний хөлс төлсөн баримт



# Хувьцааны бүртгэлийн ангилал, шалгуур

## ХУВЬЦААНЫ АНГИЛАЛ



- Нэр хүндтэй, 33Ү өндөртэй, тогтвортой үйл ажиллагаа явуулж, ашиг орлоготой ажилладаг **ТОМООХОН** компаниуд
- 33Ү болон эргэлтийн хөрөнгийн шаардлагыг хангасан **ДУНД** зэргийн компаниуд
- Хувьцаагаа мэргэжлийн хөрөнгө оруулагчдад санал болгон арилжаалдаг, шинэлэг санаа бүхий, эрсдэл өндөртэй **ЖИЖИГ, ДУНД** хэлбэрийн компаниуд



## Хувьцааны бүртгэлийн ангилал шалгуур



## Хувьцааны бүртгэлийн ангилал шалгуур (үргэлжлэл)



МОНГОЛЫН  
ХӨРӨНГИЙН БИРЖ

# Бүртгэлийн шалгуураас чөлөөлөх, хөнгөлөх

## Хөнгөлөлт, чөлөөлөлт

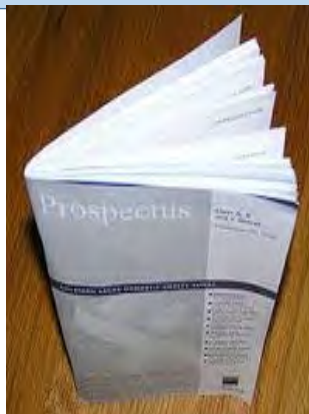
- Бүртгэлийн шалгуураас чөлөөлөх, хөнгөлөх боломжтой:
  - Үнэт цаас гаргагч, түүнд мэргэжлийн үйлчилгээ үзүүлж байгаа зохицуулалттай этгээд нь журмаар тогтоосон хувьцааны болон өрийн хэрэгслийн шалгуураас чөлөөлүүлэх буюу хөнгөлүүлэх тухай үндэслэл бүхий хүсэлтээ Биржид гаргах эрхтэй.
  - Дээрх асуудлыг Биржийн Гүйцэтгэх захирлын тушаалаар шийдвэрлэнэ. Ингэхдээ тухайн үнэт цаас гаргагчийн хувьд, эсхүл тухайн үнэт цаасны хувьд хугацаа тогтоож тодорхой нөхцөл хангахыг үүрэг болгож болно.
- Төлбөр, хураамжийн хөнгөлөлт, чөлөөлөлт эдлүүлэх боломжтой:
  - Анх удаа бүртгүүлэх бол жилийн үйлчилгээний хөлс төлөхөөс чөлөөлнө.
  - I ангилалд нэмж үнэт цаас гаргах, Бүртгэлийн ангилал өсөх, бодитоор буюу шүүд хөрөнгө татаагүй тохиролдолд гэх мэт хэд хэдэн тохиолдолд Бүртгүүлэх үйлчилгээний хөлсийг 20% хүртэл хөнгөлнө.
  - ЗГ болон орон нутгийн үнэт цаасны хураамжийн хэмжээг гэрээгээр уян хатан байдлаар зохицуулах боломжтой.



# Үнэт цаасны танилцуулга

Үнэт цаасны танилцуулга нь хөрөнгө оруулалтын шийдвэрт нөлөөлөх чухал баримт бичиг юм.

1. Үнэт цаас гаргагчийн тухай мэдээлэл
2. Үнэт цаасны тухай мэдээлэл
3. Үнэт цаас гаргах ажиллагаанд оролцсон этгээдүүдийн мэдээлэл





# Үнэт цаасны танилцуулга

Үнэт цаасны танилцуулга нь 3 хэсгээс бүрдэнэ.

## Үнэт цаас гаргагчийн тухай:

- Үнэт цаас гаргагчийн оноосон нэр, хаяг, үйл ажиллагаа;
- Улсын бүртгэлийн болон регистрийн дугаар, бүртгэсэн он, сар, өдөр;
- Бүтэц, зохион байгуулалт, эрх бүхий албан тушаалтны талаарх мэдээлэл, тэдгээрийн өмчлөлд дэх хувьцааны тоо, хувь хэмжээ;
- Хувь нийлүүлсэн хөрөнгийн хэмжээ, өмнө зарласан болон гаргасан, эргүүлэн худалдан авсан үнэт цаасны тоо, төрөл, нэрлэсэн үнэ болон өөрийн хөрөнгийн хэмжээ, биет болон биет бус хөрөнгийн талаарх мэдээлэл;
- Санхүүгийн тайлан, үүний талаар аудитын байгууллагаас гаргасан дүгнэлт;
- Хувь нийлүүлсэн хөрөнгийн тав болон түүнээс дээш хувьтай тэнцэх хэмжээний үнийн дүн бүхий үүрэг хүлээсэн гэрээ, хэлцэл, тэдгээрийн хэрэгжилтийн тухай;
- Холбогдох этгээдийн тухай
- Нөлөө бүхий хувьцаа эзэмшигчдийн талаарх мэдээлэл
- Хөрөнгө өр төлбөр санхүүгийн талаарх
- Дунд хугацааны бизнес төлөвлөгөө, санхүүгийн эрсдэл, ногдол ашгийн бодлогын талаар

## Үнэт цаасны тухай

- Нийтэд санал болгох үнэт цаасны төрөл тоо, хэлбэр, нэрлэсэн үнэ, нийтэд санал болгох болон арилжих нөхцөл, өрийн хэрэгслийн хувьд хугацаа, үндсэн төлбөр, хүү төлөх нөхцөл, журам;
- Үнэт цаасаар гэрчлэгдэх эрх, үүрэг;
- Хувьцаанд хөрвөх үнэт цаас бол тухайн үнэт цаасыг хувьцаанд хөрвүүлэх нөхцөл, журам;
- Өрийн хэрэгслийн хувьд эргэн төлөгдөх баталгаа, барьцаа эд хөрөнгийн бүртгэлтэй холбоотой мэдээлэл

## Үнэт цаас гаргах ажиллагаанд оролцсон этгээдийн тухай

- Тухайн үнэт цаасыг нийтэд санал болгох ажиллагаанд хамтран оролцож байгаа зохицуулалттай этгээд болон бусад мэргэжлийн үйлчилгээ үзүүлж байгаа этгээдийн тухай
- Тэдгээртэй байгуулсан гэрээгээр хүлээсэн эрх, үүрэг, хариуцлагын тухай мэдээлэл



# Үнэт цаасны танилцуулгад тавигдах шаардлага

МХБ нь үнэт цаасны танилцуулгад тусгагдсан мэдээлэлд үндэслэн хөрөнгө оруулалтын зарцуулалтыг хянан.

- Танилцуулгын эхний хуудсанд хөрөнгө оруулагчдад зориулсан анхааруулгыг бичсэн байна. /журмын 6.6.1/
- Үнэт цаас гаргагчийн ТУЗ-ийн дарга, Гүйцэтгэх захирал, ерөнхий нягтлан бодогч, андеррайтерийн Гүйцэтгэх захирал нар гарын үсэг зурж, тэмдэг дарж баталгаажуулсан байх
- Үнэт цаасны танилцуулгын бүх хуудсыг нэг бүрчлэн дугаарлаж, үнэт цаас гаргагчийн Гүйцэтгэх захирал, андеррайтерийн Гүйцэтгэх захирал гарын үсэг зурж баталгаажуулах
- 400-с илүүгүй хуудастай үдэж хавтасласан, товъёог хийсэн байх



# Биржид төлөх төлбөр, хөлс

Өргөдлийг хүлээн авч хянах үйлчилгээний хөлс		I ангилал	II ангилал	III ангилал
	Шинээр болон нэмж үнэт цаас бүртгүүлэх	2,000,000	2,000,000	2,000,000
Үнэт цаасыг бүртгэх үйлчилгээний хөлс		I ангилал	II ангилал	III ангилал
	Хувьцаа /хувьцааны нийт арилжаалсан	10,000,000 төгрөгөөс барагуй, 100,000,000	5,000,000 төгрөгөөс барагуй, 50,000,000	1,000,000 төгрөгөөс барагуй, 10,000,000 төгрөгөөс ихгүй
Жилийн үйлчилгээний хөлс		I ангилал	II ангилал	III ангилал
	Жилийн үйлчилгээний хөлс /компанийн зах зээлийн үнэлгээний 0.005%/	1,200,000 төгрөгөөс барагуй, 24,000,000 төгрөгөөс ихгүй	1,200,000 төгрөгөөс барагуй, 24,000,000 төгрөгөөс ихгүй	500,000 төгрөгөөс барагуй, 10,000,000 төгрөгөөс ихгүй



## АНХААРАЛ ХАНДУУЛСАНД БАЯРЛАЛАА



# Capital Policy

---

Project for Capacity Building of Capital Market in Mongolia  
Training Course for Securities Companies (1)

Takayuki Urade  
Capital Market Specialist  
JICA Consultant Team

## Contents

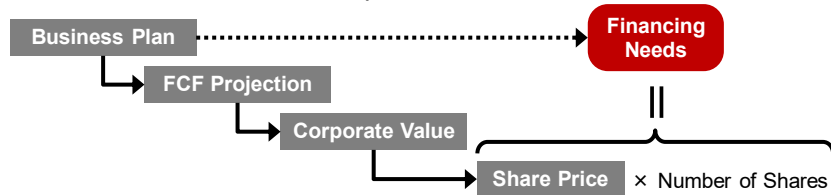
---

- What is 'Capital Policy'?
- Why is 'Capital Policy' Necessary?
- How to Apply Capital Policy?
- Tools for Capital Policy
- Strategic Considerations
- Legal / Accounting Considerations
- Cases of Failure
- Case Study

## What is 'Capital Policy'?

### Definition

- Plan to achieve a particular ownership structure by identifying how many shares will be allocated to whom at what price, based on;



- Rolling process: Need to keep updating by feeding relevant variables (e.g. biz models, other financial sources).



3

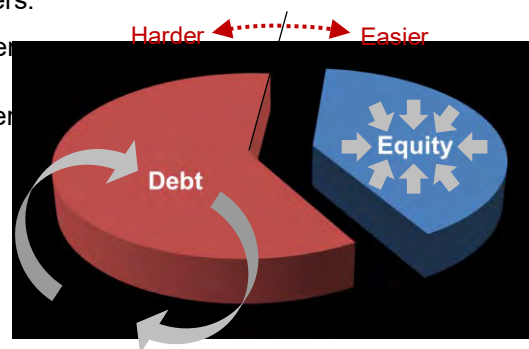
## Why is 'Capital Policy' Necessary? (1)

*Harder than the business itself...*

Mistakes in capital policy at an earlier stage are not easy to correct...

('.')

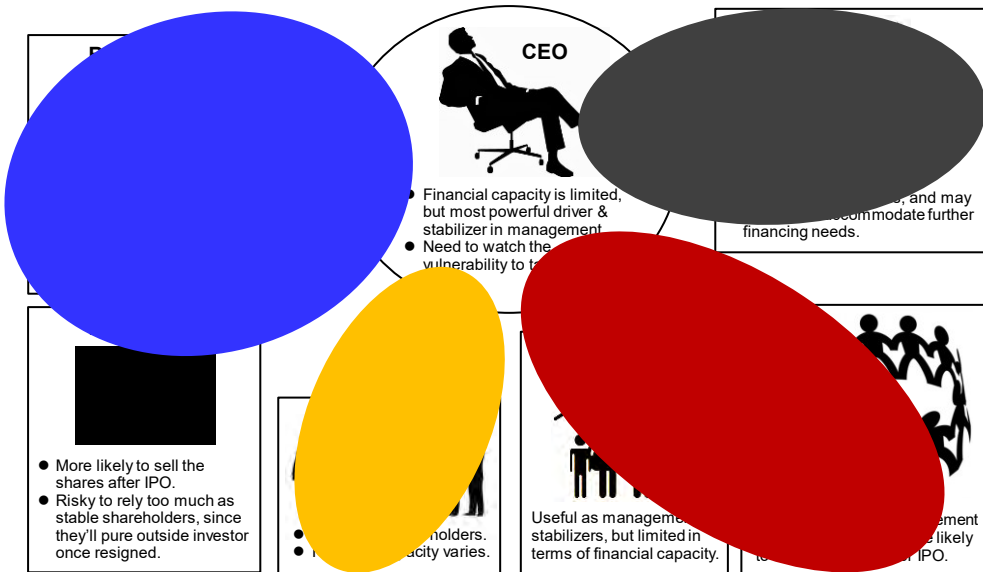
- **Debt** = '**Outside**' capital  
**Equity** = '**Own**' capital  
 → Difficult to kick out existing owners.
- Greater cost of moving shares under increasing corporate value.  
 → Once diluted, not easy to recover the founder's ownership share.



4

## Why is 'Capital Policy' Necessary? (2)

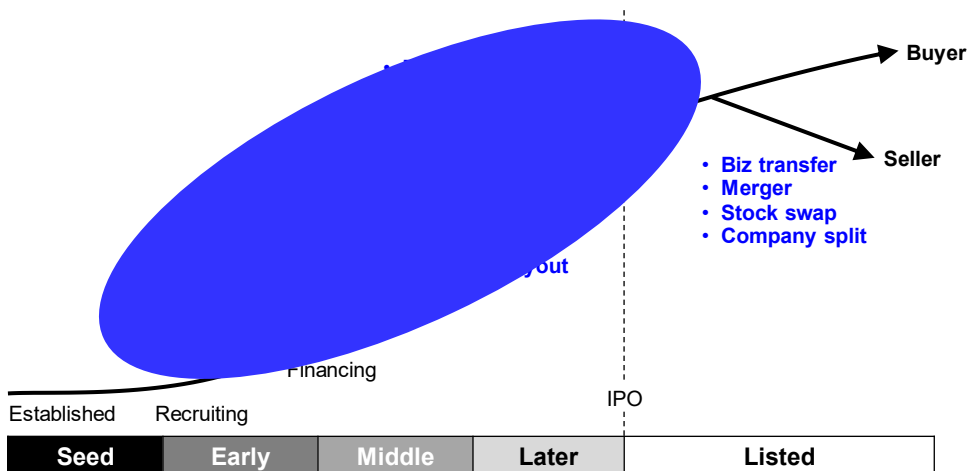
Stakeholders with varying motivation, capacity & constraints



5

## Why is 'Capital Policy' Necessary? (3)

Capital policy needs to be designed in the context of 'business lifecycle'.

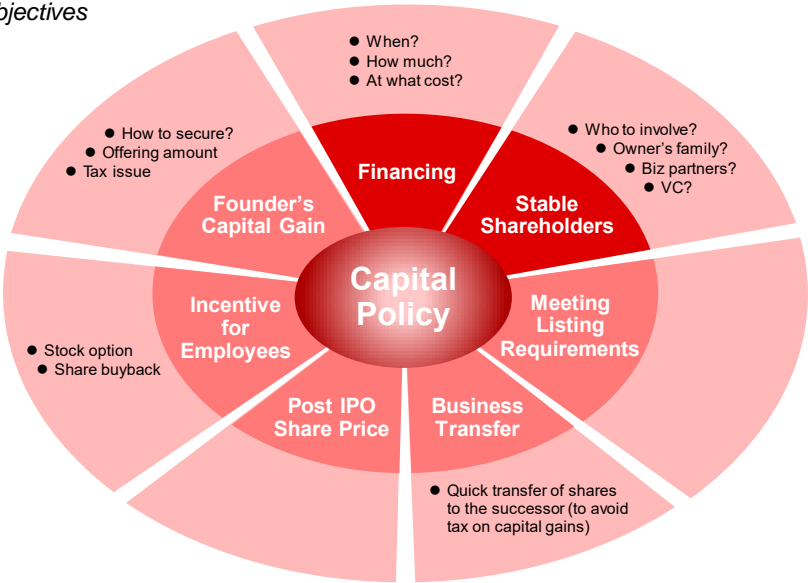


Note: Above events do not necessarily take place in this order.  
Source: JICA Consulting Team from 磯崎哲也『起業のファイナンス』（日本実業出版社、2010年）(Japanese only)

6

# Why is 'Capital Policy' Necessary? (4)

## Major objectives



Source: JICA Consulting Team, from 石崎由紀人『ベンチャー企業を上場成功に導く資本政策立案マニュアル(第2版)』(中央経済社、2014) (Japanese only)

7

# How to Apply Capital Policy? (1): PDCA Cycle

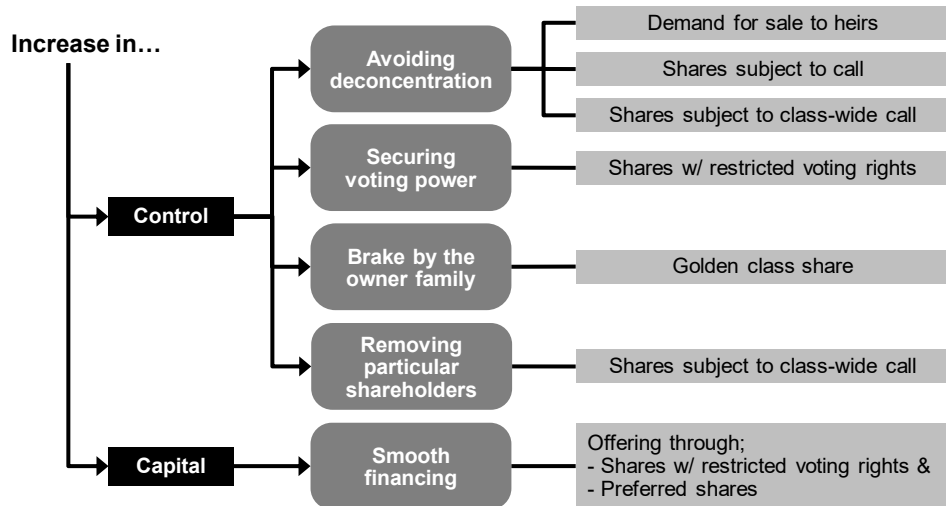
*Capital policy needs to be adjusted to the environmental changes on a real-time basis...*



8

## How to Apply Capital Policy? (2): Decision Process (A)

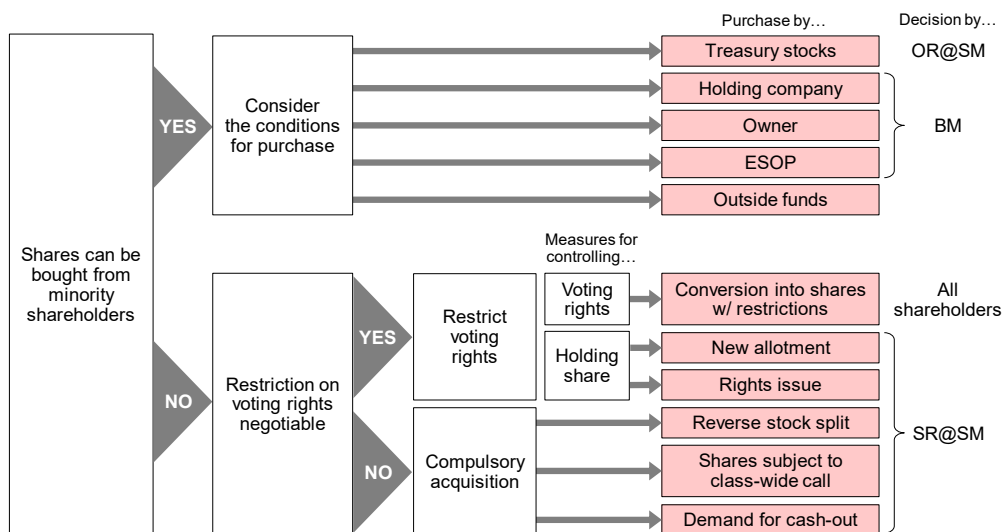
Identifying necessary measures by 'purpose'



9

## How to Apply Capital Policy? (3): Decision Process (B)

Identifying necessary measures by 'external constraints'



Source: JICA Consulting Team

10



# Tools for Capital Policy (1)

## Measures for transforming the capital structure

Measure \ Detail	Purpose					Decision by... (in the case of unlisted companies)
	Altering shareholding structure	Increase # of shares	Decrease # of shares	Financing	Incentive Plan	
Share transfer	○					Board meeting (BM), unless specified in the article of incorporation (AI)
3 <sup>rd</sup> party allotment	○	○		○		Share subscription: Special resolution (SR) @ shareholder meeting (SM), while the decision can be deputed to BM Allotment: BM, unless specified otherwise in AI
Warrant bond	○	○		○		SR@SM, while the decision on subscription details can be deputed to BM
Shareholder allotment		○		○		SR@SM, while the decision can be deputed to BM
Rights issue	○	○		○	○	SR@SM, while the decision on subscription details can be deputed to BM
Stock split, free allotment		○				BM
Share buyback	○			×		From all shareholders: Ordinary resolution (OR)@SM From particular shareholders: SR@SM From subsidiaries: BM From the market or through tender offer: OR@SM
Retirement of treasury stocks	○		○			Same as new allotment
Disposal of treasury stocks	○			○		BM
Capital reduction	△		△			SR@SM
Reverse stock split			○			SR@SM
Class shares	○			○		SR@SM & SR@Class SM

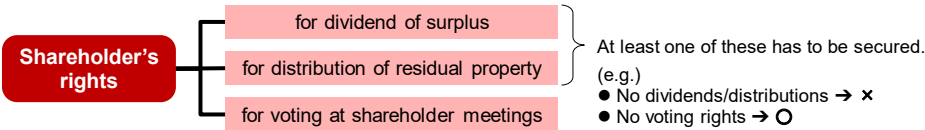
Source: JICA Consulting Team from 一般社団法人 日本経営調査士協会 (編著), 『これですべてがわかるIPOの実務 (第2版) 』(中央経済社, 2014)(Japanese only)

11

# Tools for Capital Policy (2)

## Class Shares: rights & obligations specified by type

#	Type	Details
1	Dividend of surplus	Altering dividend rate (preferred / subordinated stocks)
2	Distribution of residual property	Altering shares in distributing residual property at liquidation
3	Shares w/ restricted voting right	Excluding particular resolution matter(s) that can be voted
4	Shares w/ restriction on transfer	Requiring issuer's approval for transferring
5	Shares w/ put option	Holders have an option to ask the issuer to buy the shares
6	Shares subject to call	Issuer has an option to buy the shares under particular conditions
7	Shares subject to class-wide call	Issuer has an option to by all the shares class-wide, under the resolution of the shareholders' meeting
8	Shares w/ veto right (Golden Shares)	Allowing veto right to the holders for particular matters
9	Shares w/ the right to vote for directors / auditors	Allowing the holders the voting right to select the directors / auditors

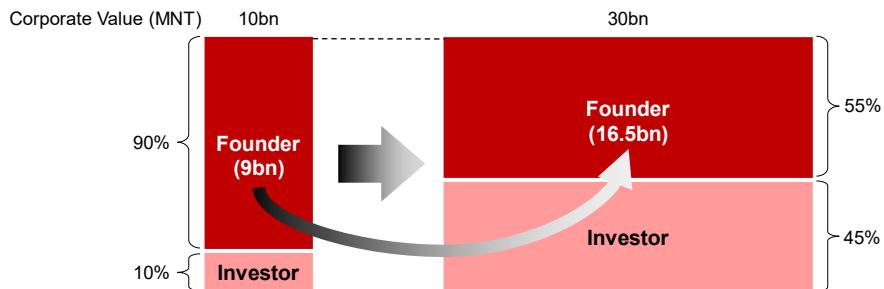


12

## Strategic Considerations

### Optimizing Shareholding Structure: Key Issues

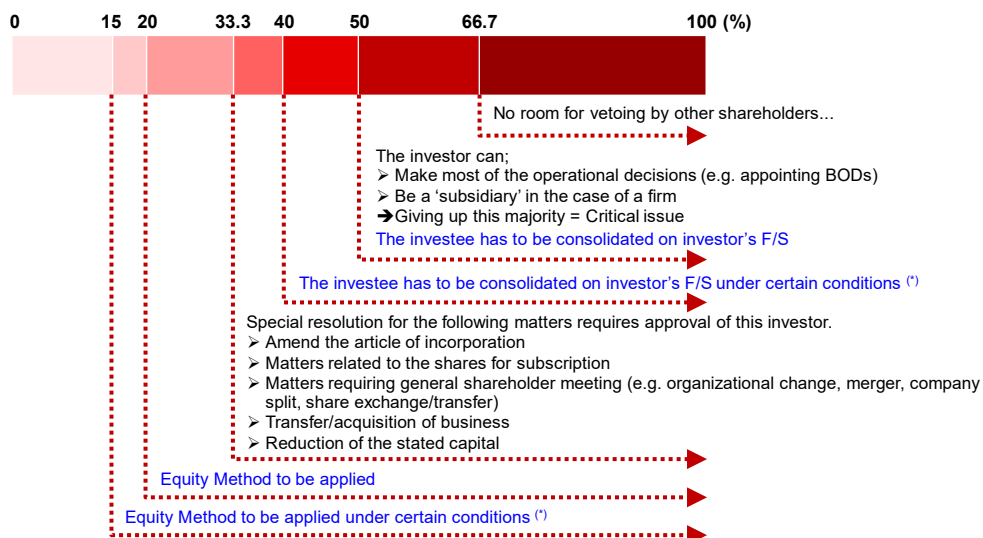
1. **Financing:** Can necessary amount be financed (thru appropriate valuation & share price)?
2. **Shareholding structure:** Stable enough even after listing?
  - Appropriate level of stock options?
  - Risk of scattered ownership
  - Strategic investors: Capable of increasing the corporate value?
3. **Capital gains:** Enough to compensate the efforts by the founder & investors?
4. **Listing criteria:** Are they cleared?
5. **Other factors:** Capital market structure, market of corporate managers...



13

## Legal / Accounting Considerations

### Under Japanese Commercial Code, Companies Act & accounting rules









(\*) e.g. BODs sent from the investor, contractual influence on decision making.  
Source: JICA Consulting Team

14

# Cases of Failure

## Obstacles to successful capital policy

	Imbalance between financing amount & ownership share	Greater than expected dilution as a result of too much financing compared to the actual needs.
	Inappropriate valuation/pricing for pre-IPO financing	Too high valuation compared to what strategic investors can afford to pay in, also making future financing harder.
	Loose forecast for business planning	Lower than forecasted profit level, resulting in lower post IPO share price. Not only enough capital gains cannot be realized, but also may not be able to meet the listing requirement (if any on market cap).
	Failure in identifying stable shareholders	Too large shareholding by VC, scaring away the potential underwriters. Founding members' unexpected resignation after the share price becomes too high, making it difficult to find the buyer(s).
	Unexpected taxation on share transfer	Too low price for 3 <sup>rd</sup> party allotment compared to the valuation required by tax law, resulting in unexpected taxation.
	Bad timing for business transfer	Too late share transfer from the founder to the successor, resulting in higher than expected share price, which makes it difficult for the successor to acquire the shares.

Source: JICA Consulting Team, from 石崎由紀人『ベンチャー企業を上場成功に導く資本政策立案マニュアル(第2版)』(中央経済社、2014) (Japanese only)

15

# Case Study

## Start-up company going public in 5yrs...

Financing needs (#1) for;  
- Hiring more staff  
- Expanding production line, etc.

Financing needs (#2)

CEO's share comes down to less than half, but still the company has more than 60%

	Jan 2011		Dec 2011				Mar 2014			Dec 2016		
	Establishment		Third party allotment (#1)				Third party allotment (#2)			IPO		
	# of shares	%	Increase	# of shares	%		Increase	# of shares	%	Increase	# of shares	%
CEO	16,000	80.0		16,000	53.2			16,000	48.3		16,000	43.5
Employee	4,000	20.0		4,000	13.3			4,000	12.1		4,000	10.9
Internal holdings	20,000	100.0		20,000	66.4			20,000	60.4		20,000	54.3
VC			10,100	10,100	33.6		1,000	11,100	33.5		11,100	30.2
Biz partner (1)							1,000	1,000	3.0		1,000	2.7
Biz partner (2)							1,000	1,000	3.0		1,000	2.7
Others			Additional investment under 'anti-dilution' clause @investment A/G							3,700	3,700	10.1
Total	20,000	100.0	10,100	30,100	100.0		3,000	33,100	100.0	3,700	36,800	100.0
Per share (MNT)	500		10,000				60,000			250,000		
Financed amount (MNTmn)	10		101				180			925		
Corporate value @post financing (MNTmn)	10		301				1,986			9,200		

The company is assumed to have (MNT200mn) of pre-financing value. (i.e. The corporate value has increased by 20x.

Amount for public offering

Market cap@IPO

Source: JICA Consulting Team, from 石崎由紀人『ベンチャー企業を上場成功に導く資本政策立案マニュアル(第2版)』(中央経済社、2014) (Japanese only)

16

# Thank you!

For further questions, comments & suggestions, please contact:

**Takayuki Urade**

JICA Consulting Team

Office (Local): Room #204, FRC





Japan International Cooperation Agency



## **Project for Capacity Building of Capital Market in Mongolia**

# **How to Approach Potential Clients**

23 May 2016

Ryota Sugishita  
JICA Consultant, Daiwa Institute of Research

### **1. Know your business - What is brokerage?**

---

Q1. How can securities companies make money?

Your company's business performance highly depends on brokerage.

Q2. How can you earn brokerage commission?

- A) Just sit and wait in your office chair.
- B) Proactively contact clients.

Which do you think is better?

## 1. Know your business - How can brokerage business be conducted

---

### A) Just sit and wait in your office chair.

- ✓ Hope it works. You may be able to earn enough in the bull market.
- ✓ But it is not sustainable. Perhaps you can not even cover your personnel cost if you just sit and wait.



### B) Proactively contact clients.

- ✓ Tough job. You may be ignored when you contact.
- ✓ But your performance may improve dramatically if you can find good clients.



3

## 1. Know your business - What is your role?

---

You are a financial advisor for your clients.

- ✓ You do not just execute buy/sell orders for your clients. Your role is to contribute to your clients' financial asset management.

So, you are advised to:

- know your clients' financial asset profiles;
- classify your clients by type;
- advise your clients individually.

4

## 1. Know your business - Client profiles

---

An example of client profile sheet

Your experiences in investments	<input type="checkbox"/> Mongolian stocks <input type="checkbox"/> Mongolian government bonds <input type="checkbox"/> Mongolian corporate bonds	<input type="checkbox"/> Overseas stocks <input type="checkbox"/> Overseas bonds <input type="checkbox"/> Mutual funds <input type="checkbox"/> Other products <input type="checkbox"/> Online trading
Your investment plan	<input type="checkbox"/> Mongolian stocks <input type="checkbox"/> Mongolian government bonds <input type="checkbox"/> Mongolian corporate bonds	<input type="checkbox"/> Overseas stocks <input type="checkbox"/> Overseas bonds <input type="checkbox"/> Mutual funds <input type="checkbox"/> Others
How did you know our company	<input type="checkbox"/> Introduced by someone <input type="checkbox"/> Called by our staff <input type="checkbox"/> Saw our website	<input type="checkbox"/> Received an e-mail from us <input type="checkbox"/> Saw advertisement on TV
Investment strategy	<input type="checkbox"/> Long-term <input type="checkbox"/> Mid-term <input type="checkbox"/> Short-term	<input type="checkbox"/> Higher capital gains <input type="checkbox"/> Stable dividend income <input type="checkbox"/> Others
Your assets	Your annual income: <input type="checkbox"/> MNT 10m or below <input type="checkbox"/> MNT 10-50m <input type="checkbox"/> MNT 50-100m <input type="checkbox"/> MNT 100m or above	Your financial assets: <input type="checkbox"/> MNT 10m or below <input type="checkbox"/> MNT 10-50m <input type="checkbox"/> MNT 50-100m <input type="checkbox"/> MNT 100m or above

5

## 2. How to reach out clients - Retail clients

---

- 1) Phone calls - for potential clients that have not opened an account with your company yet

You should make as many phone calls as possible to potential clients to:

- i. increase number of your clients;
- ii. support your brokerage business especially when you are in the bearish market.



6



## 2. How to reach out clients - Retail clients

---

### 1) Phone calls - for clients with an account

You should sometimes call your existing clients in order to:

- i. know how your clients feel their financial assets;
- ii. provide new information that possibly encourages your clients to make new investment decisions;
- iii. keep in touch with your clients.

You may be reluctant to call a client when the client's financial asset is devalued. However you should keep relationships with your clients in the difficult times.

7

## 2. How to reach out clients - Retail clients

---

### 1) Phone calls - for clients with an account - cont.

Example 1: One of your clients Mr Sugi bought APU shares six months ago. Prices for APU were up 30% so far.

Example 2: Mr Sugi bought APU shares last year. Share prices keep falling, down 30% till to-date.

Are you going to keep quiet not contacting Sugi? Or are you going to contact to persuade him for an investment decision?

8

## 2. How to reach out clients - Retail clients

### 2) E-mails

If you know clients' e-mail addresses, you can maintain your relationships with your clients. For instance, you can send:

- daily/weekly/monthly market comments
- company/industry news
- economic data updates
- your recommendation list
- new product information (e.g. IPO)

You should still make phone calls, in addition to sending e-mails.

9

## 2. How to reach out clients - Retail clients

### 2) E-mails - cont.

Market report by Daiwa Securities

**Market Review for 3rd Week of May**

**Japanese stock strategy memo**

- TOPIX up 1.78% vs. last Friday on yen depreciation, higher commodity prices
- Financials outperformed sharply and materials, capital goods
- Supermarket, electrical, consumer goods, transportation & utilities, technology underperformed, with retail retail effect notable, high-tech, low-P/E, low-P/B, low-price stocks outperformed

**Market review:** In the third week of May, the April FOMC minutes suggested a gradual rate hike in June, which the yen-denominated TOPIX gained 1.78% from last Friday to 1,245.45, reflecting higher commodity prices and favorable economic data. The performance includes performance in the market, where transportation, energy, materials and metals, and the worst performers included consumer products, air transportation, information & communications, electric power & gas, and food.

**16 May TOPIX rebounded:** The index rebounded from the value of overnight weakness on 15th Street, but it then picked up, reflecting yen depreciation vs. the dollar and gains across all prices. Expectations for government stimulus and a smaller degree of market highs.

**17 May TOPIX down:** A mixed range of sectors, particularly auto and other export-oriented companies, followed by a rise in the yen and a rise in the external environment, such as yen depreciation and higher commodity prices.

**18 May TOPIX closed higher:** Financials advanced as higher-than-expected GDP data for April has led to higher expectations for additional monetary easing by the BOJ.

**19 May TOPIX ended lower:** Japanese stocks, particularly foreign demand-driven firms, suffered from a sharp decline, reflecting a sharp decline in machinery orders and yen depreciation. However, the index then fell back as markets reacted to the yen's gains. Some markets had growth or more natural resource prices.

**20 May TOPIX advanced:** The index rebounded from the value of a pull-off in US shares. That said, it then gained ground, reflecting expectations for the US House stimulus package and Japan's government stimulus.

**21 May TOPIX advanced:** The index rebounded from the value of a pull-off in US shares. That said, it then gained ground, reflecting expectations for the US House stimulus package and Japan's government stimulus.

**22 May TOPIX advanced:** The index rebounded from the value of a pull-off in US shares. That said, it then gained ground, reflecting expectations for the US House stimulus package and Japan's government stimulus.

Macro economy report by Daiwa Securities

**Outlook for domestic economy (update, May)**

**Economy remains in a soft patch**

- Unemployment rate (49.7%) remains relatively stable, but the government's goal through JGD is to reduce it to 48.0%.
- The impact of the recent 10% increase in the consumption tax rate and the impact of the recent 10% increase in the consumption tax rate.

**Table of Economic Indicators:**

Indicator	2014	2015	2016	2017	2018	2019	2020	2021	2022
GDP (Billion Yen)	460,000	470,000	480,000	490,000	500,000	510,000	520,000	530,000	540,000
Unemployment Rate (%)	49.7	49.7	49.7	49.7	49.7	49.7	49.7	49.7	49.7
Consumer Price Index (CPI) (2010=100)	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Industrial Production Index (IPI) (2010=100)	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Export (Billion Yen)	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000
Import (Billion Yen)	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000

10

## 2. How to reach out clients - Retail clients

---

### 3) Visits

You are sometimes advised to visit your clients. Face-to-face communication is more valuable.

- ✓ If you receive a visit by one of your clients to your office, that is a good chance to strengthen relationship with the client. It may provide you with opportunity to persuade him/her to make a new investment decision.
- ✓ If you do not receive clients' visits, you may have to consider if you should visit them to introduce yourselves and inform them your advice on investments.

11

## 2. How to reach out clients - Retail clients

---

### 4) Website

Website is increasingly important for your business. We expect it will be common for Mongolian brokers to provide an online trading platform.

In the online trading market, website design is one of key points for success. A simple but visually appealing website design may attract more investors.

12

## 2. How to reach out clients - Retail clients

---

When you communicate with your clients:

- ✓ Do you think you can sell something you do not know?
- ✓ When you call your clients or potential clients, you need to be ready for telling your recommendations.
- ✓ For recommending to your clients, you have to fully understand what you are going to talk about.
- ✓ Sometimes your client know better than you about a company you recommend.
- ✓ You are a professional. You need to learn every day.

13

## 3. How to reach out clients - Foreign investors

---

Although foreign investors are inactive in the Mongolian stock market in recent years, they are your potential big clients.

1) Institutional or retail?

- ✓ Foreign investors can be both institutional and retail.
- ✓ Mongolian securities brokers may have a bigger chance to talk to foreign institutional investors, given that it is usually hard to reach foreign retail investors, unless you have a partnership with an overseas securities company with retail clients that are interested in the Mongolian stocks.

14

### 3. How to reach out clients - Foreign investors

---

#### 2) What are foreign institutional investors like?

- ✓ Foreign institutional investors are professional investors with wide knowledge in finance, macro economy and industries.
- ✓ They are sometimes demanding. Unless most of their minimum requirements are cleared, they will not invest.
- ✓ Their requirements include size of a stock, profitability of the company, liquidity, reliability in financial statements, corporate governance etc.

15

### 3. How to reach out clients - Foreign investors

---

#### 2) What are foreign institutional investors like? - cont.

- ✓ They may be not familiar with Mongolia in the beginning. But they can learn quickly, by reaching out variety of information and in-depth research about Mongolian companies.
- ✓ They also want to contact listed companies directly. You may be sometimes requested to set up a conference call or a meeting with a listed company.
- ✓ You need to continue studying to deal with foreign institutional investors.

16

### 3. How to reach out clients - Foreign investors

---

#### 3) What are typical services for foreign institutional investors?

##### i. Sending e-mails regularly

Institutional investors can access to multiple number of brokers. You are not the only one. You better contact them frequently to appeal that you are the best partner.

##### ii. Conference call with local companies

They may not be able to visit Mongolia often. They appreciate if you can set up a conference call with a company, especially with management.

17

### 3. How to reach out clients - Foreign investors

---

#### 3) What are typical services for foreign institutional investors? - cont.

##### iii. Research trip to Mongolia

Foreign institutional investors may sometimes ask you to arrange a research trip to Mongolia. If you can arrange good meetings, that should be helpful for the them.

##### iv. Investment conference

Another possibility is to host a investment conference, either in Ulaanbaatar or overseas. If you can invite major entrepreneurs, policy makers and professionals, that is a good opportunity for foreign institutional investors to learn about Mongolia's market outlook.

18

### 3. How to reach out clients - Foreign investors

#### 3) What are typical services for foreign institutional investors? - cont.

Oyu Tolgoi site visit for investors, Oct14      Conference Notice by Daiwa Securities



19

### 4. Educating fresh graduates - Japan's typical case

- ✓ In Japan, major companies including securities companies recruit fresh graduates every year.
- ✓ Only a part of fresh graduates have learned financials. Almost all of the fresh graduates do not know anything about the securities industry.
- ✓ Japanese securities companies spend months to educate the fresh graduates.

Training fresh graduates at Daiwa Securities



20

#### 4. Educating fresh graduates - Japan's typical case

---

What fresh graduates learn after employed in April:

i. Studying for securities representative's license

For the first 3 months, new employees learn basics for securities business and are ordered to pass the exam for a securities representative license by June.

ii. Understanding financial products

In June, they are sent to a branch to learn retail sales. They study financial products such as major stocks, mutual funds, bonds etc. so that they can explain to potential clients.

21

#### 4. Educating fresh graduates - Japan's case

---

What fresh graduates learn after employed in April:

iii. Learning how to communicate with a client

- ✓ Before contacting retail investors, new employees practice how they should talk to clients. Role-playing is often used, assuming a senior staff is a retail client and he/she is a sales staff talking to the client.
- ✓ The senior staff purposely ask tough questions to the new staff. Not only knowledge of financial products, but also how sales staff should talk and behave is also monitored.

iv. Calling as many clients as possible every day

In Japan, new staff are often ordered to call as many as possible.

22



---

# Баярлалаа!

Та бүхэн асуулт асуух, өөрийн санал, зөвлөмжөө илгээхийг хүсвэл  
доорх хаягаар хандаарай.

**Ryota Sugishita**

Жайка Зөвлөхийн Баг

Офис (орон нутгийн): өрөө #204, FRC



Japan International Cooperation Agency



## **Project for Capacity Building of Capital Market in Mongolia**

### **Lecture on Investor Education**

23 May 2016

Akifumi Nakanishi  
JICA Consultant, Daiwa Institute of Research

#### **Contents of the lecture**

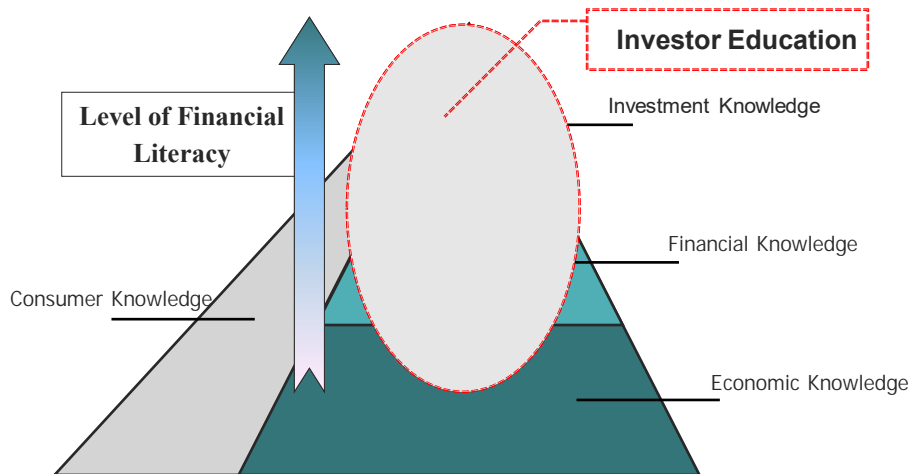
---

1. Investor Education (IE): Why important?
2. Various channels for IE
3. Actual contents and menus for IE
4. Basic knowledge: Valuation tools
5. Q&A

## 1-1. Investor Education - Concept

---

- ◆ Improving financial literacy requires multiple level of understandings
- ◆ Investor education covers advanced knowledge of finance and investment



2

## 1-2. Investor Education and Financial Literacy – Importance

---

- ◆ Improving financial literacy will help develop public awareness which is a very important factor and step towards market oriented economy.
- ◆ Why important in Mongolia?
  - Prerequisite for a stable and credible financial market
  - Promote investment hence stimulating economic growth
  - Increase awareness leads to widening the investor base
  - Diminish all kinds of anxiety towards capital market and gain confidence.

3

### 1-3. Relevant Institutions – Roles and Objectives

#### ◆ Securities companies are most responsible to educate investors

Group	Institution	Role and Objectives	Legal Enforcement	Target Stakeholders
Financial Authority	Ministry of Finance	Decide on the issuance schedule and provide public announcement	○ mandatory	public, financial institutions
	Central Bank	Conduct monetary operation via bond intervention, financial education	○ mandatory	bankers, financial institutions
	Securities Exchange Commission	Supervise and monitor via rules and regulation, financial education	○ mandatory	brokers, dealers, financial professions, investors
Financial Institutions / Intermediaries	Stock Exchange	Control stock market operation,	△ certain extent	market participants, investors
	Commercial Banks	Provide macro-economic and market information,	△ certain extent	investors
	Securities House / Asset Management	Provide information on financial services and instruments, seminars	△ certain extent	investors
Associations	Securities' Dealers, Banking, CPAs etc.	Provide updated market information and benchmarks	△ certain extent	market participants, investors
Educational Institutions	Universities, Higher education	Provide relevant academic knowledge and educational materials	× voluntary	students, educators, potential investors

### 1-4. Specific actions ① Financial authorities

#### ◆ Efforts in providing information at real time basis

- Establish framework of timely disclosures of relevant information.
- Consult necessary market data to financial institutions.
- Announce any policy changes and amendments to the public.

#### ◆ Activities for improving public awareness

- Utilize financial institutions, market participants and medium equally to reach the public.
- Establish investor protection scheme.
- Conduct social networking programs.

## 1-5. Specific actions ② Securities companies & financial institutions

---

### ◆ Efforts in updating information and data

- Gather relevant data and market information on daily basis.
- Inquire necessary details to the financial authorities.
- Provide any changes and amendments to the clients.

### ◆ Activities for information dissemination

- Inform the public using all kinds of medium such as newspapers, magazine, television programs, banners, post letters, internet website, mobile gadgets, etc.
- Socialization activities via seminars and events at regular basis.

6

## 2-1. Various Channels for Investor Education

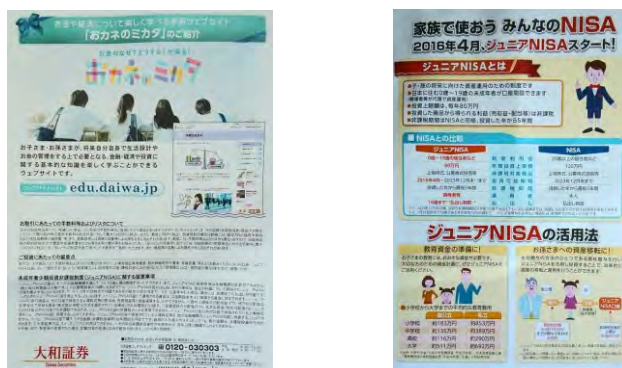
---

- ◆ Investor education can be delivered through various channels as an extension of the ordinary activities done by the securities companies
  - ✓ Direct contact: sales and marketing activities such as at the branch, customer's property, as well as via post mails, emails, phones, faxes, text messages, etc..
  - ✓ Publication and reports: information dissemination activities such as the market data (indices, forex, trade stats, etc.) macroeconomic reports, industry outlooks, instruments, etc..
  - ✓ Socialization events: socialization activities targeting the existing and potential investors via seminars, workshop, lectures, webinars, "investor day", etc..
  - ✓ Media: advertisement and promotion activities via media such as the television, radio, newspapers, magazines, websites, SNS (YouTube, Facebook, Twitter, etc.) , etc..

7

## 2-2. Various Channels for IE (1): Direct contact

- ✓ The advantage of the direct contact is that you may know better about the Investors' preference, objectives and risk taking level directly from face to face communication.
- ✓ One may also explain better regarding the possible investment opportunities as well as the actual products.



Brochures on Investor Education and new products

8

## 2-3. Various Channels for IE (2): Publications and reports

- ✓ Investors usually gain confidence if they have access to various information that they need to know before the actual investment activities.
- ✓ Reports may vary from market analysis, macroeconomic status, industry based, and/or individual companies or product based.

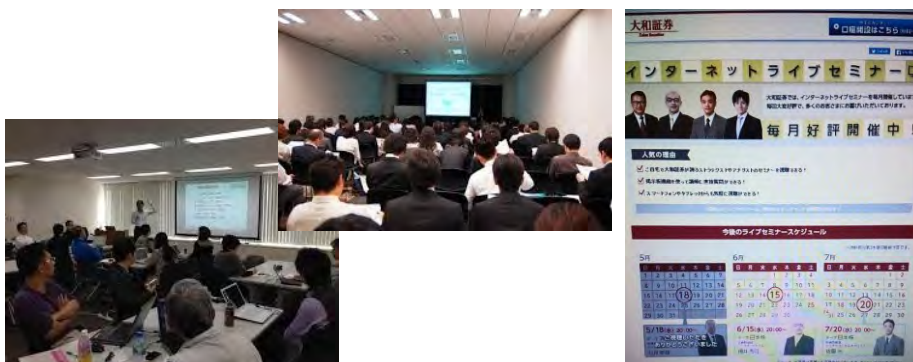


Various reports published by Daiwa Securities Group

9

## 2-4. Various Channels for IE (3): Socialization events

- ✓ Seminars and workshop type events will definitely help investors to understand the current market situation, investment opportunities and investable products.
- ✓ Such event will also allow securities companies to widen the networks on potential investors as well as promote products to the clients.



Seminars and Webinars by Daiwa Securities Group

10

## 2-5. Various Channels for IE (4): Media sources

- ✓ Media sources is also a very powerful channel to reach potential investors and promote sales and marketing.
- ✓ One may differentiate which type of media to be utilized depending on the targeted audience (i.e. by gender, age, location, nationality, etc.).



Daiwa TV programs and Twitter sites

11

### 3-1. Actual Contents of Investor Education

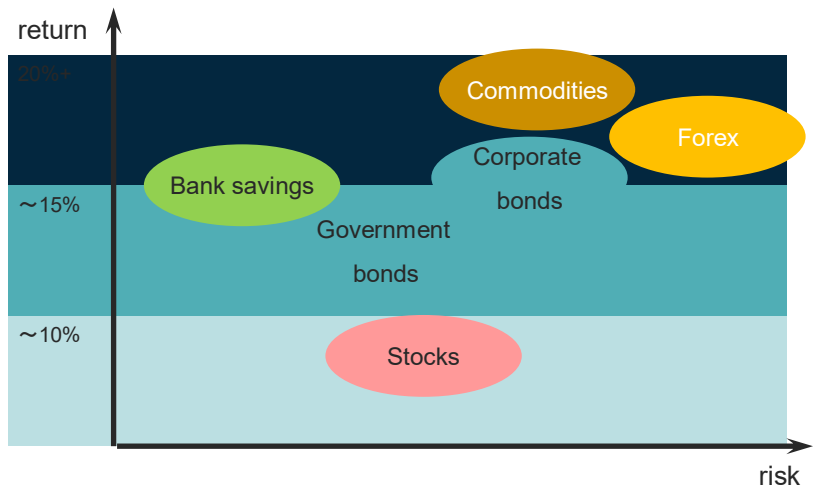
- ◆ Investor education can be delivered depending on the investors' investment needs and level of financial literacy
- ◆ Prepare necessary materials to maintain and assure the quality disseminated

Investment needs	Product types (currently available in Mongolia)
First time investment	Stocks
Retirement Plans	Government bonds/corporate bonds
Short-term / Long-term horizon	Foreign Currencies
Asset Management	Commodities
Diversification	Foreign products
Inheritance Plans	

12

### 3-2. Probable Menu for investment opportunities (current Mongolia)

- ◆ Essential to understand the probable returns and risks on each instruments
- ◆ Introduce options of products depending on the investors' preference on investment and risk taking level



13



3-3. Probable Menu for investment opportunities (current Mongolia)

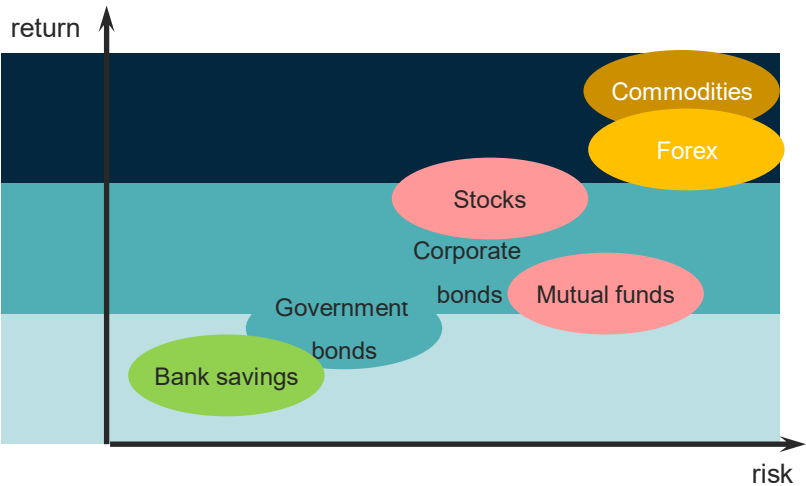
- ◆ Bank savings is the most attractive opportunity and favored in current Mongolia
- ◆ Government bonds have also attracted certain amount of investors due to high yield compared to other investable products

Product	Annual return	Risk
1-year max. bank deposit rate	18.00%	Low
Weighted avg bank deposit rate	13.30%	Low
12-week Government securities yield	13.19%	Lowest
1-year return for a stock	?	High
Annual USD/MNT depreciation	5-10%	High

14

3-4. Probable Menu for investment opportunities (other markets)

- ◆ Recommended to understand probable returns and risks in other markets
- ◆ It is also helpful to access to other countries' institutions who are initiating the investor educations with various kinds of references and resources



15

### 3-5. Underlying Risks for Investments

◆ Ability to explain the risks behind the investment activities is very important

Types of Risks	Description
Political / Legislative Risk	Risk occur when changes in the government ruling parties and associated policies and legislative matters realized.
Inflation Risk	The chance that the value of an asset or income will be deflated (inflated) as inflation rate shrinks (widens).
Foreign Currency Exchange rate Risk	Risk that arises from the possible fluctuations in the prices between local and foreign currency exchanges.
Interest Rate Risk	Possibility of a fixed-rate debt instrument will decline in value as a result of a rise in interest rates.
Credit Risk	Possibility that a particular debtors will no be able to pay the interest rate payments and/or principals.
Market Risk /Systematic Risk	Risk that cannot be avoided such as the natural disasters, economic recessions, changes in the natural resource prices, terrorist attacks.
Liquidity Risk	Risk that an investor may not be able to buy (sell) the securities product when desired due to insufficient quantities and/or opportunities are limited.

16

### 3-6. Example of Educating Investors (1): First time investors

#### 1) For first time investors

- ✓ If a new client of yours does not have any experience in investments, first of all you have to explain differences between saving and investing.

#### Example

- Unlike bank deposits, you may lose your money when you invest in stocks.
- Even when a bank goes bankrupt, your deposit, to a certain extent, will be secured by Deposit Insurance Corporation of Mongolia. The money you invest in stocks is not insured. A share price decline means the value of your stocks falls.
- But you may earn more from your investment than your saving.

17

### 3-7. Example of Educating Investors (2): Experienced investors

---

#### 2) For non first-time investors

- ✓ If your client understands the differences between saving and investing, now you can promote a certain product to your client, by your own idea.

#### Government bonds

- Under the current interest rate environment, it is very difficult to promote stocks.
- The government bond is perhaps the first choice for many of your clients.
- You need to appeal what kind of advantages a client of yours can take from government bond investment.

18

### 3-8. Example of Educating Investors (3): Experienced investors

---

#### 2) For non first-time investors - cont.

#### Stocks

- How can you promote stocks under the current difficult situation?
- Bottom fishing is a phrase that is often used in the downcycle.
- What indicators can be implications for a turnaround of share prices?

19

#### 4-1. Basic Knowledge: Valuation

---

- ✓ Before an investor makes investment decisions, he/she measures if the price of a stock is overpriced (expensive) or undervalued (cheap) by calculating valuation.
- ✓ Most commonly used valuation is the price-earnings ratio (P/E ratio).
- ✓ P/E ratio is simple and easy to use. It is applicable if a company is profitable. Institutional investors and analysts mostly uses the P/E ratio.
- ✓ Another well-known valuation is the price-book ratio (P/B ratio). P/B ratio is often used in the downturn of the market. Theoretically you can say the stock is oversold if its P/B ratio falls below x1.0.
- ✓ Dividend yield is often used for long-term investors, especially when interests rates are low.

20

#### 4-2. Basic Knowledge: Price-earning ratio (P/E ratio)

---

- ✓ When you calculate P/E ratio for a stock, you should use an estimate EPS for the current year or the next year, not previous year's actual EPS.
- ✓ In Mongolia, it appears to be quite difficult to estimate EPS of a listed company due to poor disclosure. What you can do could be, at best, looking at the past earnings and making a bold estimate.
- ✓ Interviewing listed companies is also a part of your job, although most of them may refuse to comment. You need to get to know listed companies' information to be familiar with them. Your better knowledge on listed companies will contribute to investor education.

21

### 4-3. Price-earning ratio (P/E ratio)

---

- ✓ P/E ratio cannot be applied if a company reports a loss.
- ✓ Mining companies' earnings momentum is quite dynamic. Is P/E ratio good enough to value mining companies' valuation?
- ✓ In the exploration stage, mining companies do not have revenue, thus they are loss-making companies. When a loss-making mining company in the exploration stage makes an IPO, what valuation should we use?
- ✓ Perhaps you need a bold long-term estimate for the company's financials, based on probable reserves, company's long-term exploration and production plan as well as price forecast of mining products.

22

### 4-4. Basic knowledge (1): Price-earning ratio (P/E ratio)

---

Price - earnings ratio = share price / EPS (earnings per share)

EPS = Net income / total number of shares outstanding (period average)

Sugi Corp's FY2015 earnings forecast:

Revenues	MNT 100 million
Expenditures	MNT 70 million
Income before tax	MNT 30 million
Net income	MNT 20 million

Total number of shares: 100,000

Sugi Corp's EPS forecast for FY 2015  
= MNT 20 million / 100,000 shares  
= MNT **200**

(1) When Sugi Corp's share price is MNT 4,000  
P/E ratio = MNT 4,000 / MNT 200 = **20x**

(2) When Sugi Corp's share price is MNT 2,000  
P/E ratio = MNT 2,000 / MNT 200 = **10x**

- ✓ P/E ratio compares the current share price with its earnings.
- ✓ Whether the company's share price is trading at a premium or a discount is judged from the comparison with the P/E ratio of companies in the similar sector, or a historical range of its P/E ratios.
- ✓ P/E ratio trends may vary amongst sectors or the economic trends of the country and timing.

Source: Daiwa Institute of Research

23

## 4-5. Basic knowledge (2): Price-book ratio (P/B ratio)

Price - book ratio = share price / BPS (book value per share)

BPS = shareholders' equity (net assets) / total number of shares outstanding

Sugi Corp's FY2015 financial forecast		BPS = MNT 200 million / 100,000 shares = MNT <b>2,000</b>  (1) When the share price is MNT 4,000 P/B ratio = MNT 4,000 / MNT 2,000 = <b>2x</b>  (2) When the share price is MNT 2,000 P/B ratio = MNT 2,000 / MNT 2,000 = <b>1x</b>
Total assets	MNT500 million	
Liabilities	MNT300 million	
Shareholders' equity	MNT200 million	
Total number of shares: 100,000		

- ✓ P/B ratio is a ratio that is often used in a down cycle to judge downside potential of the a stock.
- ✓ When the P/B ratio is 1x or below 1x, it suggests that the price may be undervalued.

Source: Daiwa Institute of Research

24

## 4-6. Basic knowledge (3): Dividend yield

Dividend yield (%) = dividend per share / share price x 100

Sugi Corp's FY2015 dividend forecast

Dividend per share

MNT150

Share price

MNT4,000

(1) Dividend yield for Sugi Corp

= MNT150 / MNT4,000 = **3.75%**

(2) Dividend yield for Urade Trading

= MNT100 / MNT2,000 = **5.00%**

-> Investors can receive more dividends from Urade Trading when investing the same amount of money.

Urade Trading's FY2015 dividend forecast

Dividend per share

MNT100

Share price

MNT2,000

- ✓ Generally, dividend yields of companies in a growing stage are lower, some even pay no dividends (for example Microsoft did not pay any dividends until FY2003).
- ✓ On the other hand, there are cases where institutional investors claim more dividends against companies that profit growth become moderate or those have too much cash.

Source: Daiwa Institute of Research

25

---

# Баярлалаа!

Та бүхэн асуулт асуух, өөрийн санал, зөвлөмжөө илгээхийг хүсвэл  
доорх хаягаар хандаарай.

**Akifumi Nakanishi**

Жайка Зөвлөхийн Баг  
Офис (орон нутгийн): өрөө #204, FRC

## **Project for Capacity Building of Capital Market in Mongolia**

# **Ethics for Securities Representatives**

23 May 2016

Ryota Sugishita  
JICA Consultant, Daiwa Institute of Research

### **1. Ethics – Minimum standards for securities representatives**

---

- ✓ If you are licensed as a securities representative, you are requested to be a reliable professional.
- ✓ Nothing else is more important than trust and reputation. Without investors' trust, stock market never develops. If your reputation is bad, you cannot make a deal.
- ✓ In fact, investors stay away from the market if an event that loses investors' trust happens (e.g. placing an order without client's approval, investment fraud etc.).
- ✓ In recent years, a code of ethics for securities companies' representatives is set in major markets.
- ✓ A code of ethics is expected to:
  - improve investors' trust;
  - avoid legal and reputation risks of your company;
  - result in selecting new entrants upon licensing.



## 1. Ethics – Minimum standards for securities representatives - cont.

---

- ✓ International Organization of Securities Commissions (IOSCO) released *Model Code of Ethics*<sup>1</sup> in Jun06.
- ✓ IOSCO recommends 6 ethical principles:

- i. Integrity and truthfulness
- ii. ~~P~~romise keeping
- iii. ~~L~~oyalty - Managing and fully disclosing conflicts of interest
- iv. ~~F~~airness to the customer
- v. ~~D~~oing no harm to the customer or the profession
- vi. ~~M~~aintaining confidentiality

<sup>1</sup> <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD217.pdf>

## 1. Ethics – Minimum standards for securities representatives - cont.

---

- ✓ In Japan, Japan Securities Dealers Association (JSDA) set *Model Code of Ethics* in Sep07.
- ✓ JSDA's *Model Code of Ethics* consists of 9 principles:

- i. ~~S~~tandards of conduct and compliance with laws
- ii. ~~M~~anaging conflicts of interest
- iii. ~~C~~onfidentiality of information
- iv. Social responsibility
- v. Maximizing your client's interests
- vi. Loyal and fair treatment
- vii. Neutral advice to clients
- viii. Higher ethical behavior
- ix. Healthy development of capital markets

## 2-i. Model code of ethics - Standards of Conduct and Compliance with Laws

---

- ✓ You have to be an ethical person.
- ✓ For building trust and good reputation with your clients, you have to understand laws, rules and regulations for capital markets.
- ✓ Not only acting with integrity in compliance with laws, rules and regulations, you also need to behave ethically even in a space where the current legal framework does not cover.

5

## 2-ii. Model code of ethics - Managing conflicts of interest

---

- ✓ If you have an incentive to serve one interest at the expense of another interest, that is a conflict of interest.
- ✓ Conflicts of interest can sometimes be seen. You have to be fair in managing conflicts of interest.

### Example 1

- Your company is licensed for brokerage and underwriting.
- You begin to think that Sugi Corp's current share price is overvalued, and want to advise your clients to sell Sugi Corp shares.
- Then you are informed that a colleague of yours is discussing with Sugi Corp for SPO.

6

## 2-ii. Model code of ethics - Managing conflicts of interest - cont.

---

- ✓ You have to recognize that you can sometimes access privileged or confidential information. You should avoid making a deal, using your privileged or confidential information.
- ✓ You should not pass it if you know privileged or confidential information.

### Example 2

- You are an underwriter and are close to Urade Mining's CEO.
- You heard from the CEO that the company would obtain an exclusive license to develop one of Mongolia's strategic mining deposits.
- This information is not publicly announced yet.

7

## 2-iii. Model code of ethics - Confidentiality of information

---

- ✓ Information that you have obtained from your clients, listed companies and others should be mostly kept confidential.

### Example 3

- Mr Ohno is one of your clients.
- One day someone you do not know calls you and requests to provide Mr Ohno's address, mobile phone number, e-mail address and other personal information with him.

8

### 2-iii. Model code of ethics - Confidentiality of information - cont.

---

- ✓ Information on your clients' financial assets cannot be disclosed to anyone.
- ✓ Trade information is also confidential.

#### Example 4

- Mr Nakanishi is an active client of yours.
- Every day he places an buy/sell order.
- Another client of yours wants to know which stock Mr Nakanishi trades how many.

9

### 2-iv. Model code of ethics - Social responsibility

---

- ✓ You are a business person, at the same time a good citizen, contributing to social stability.
- ✓ Be careful of dealing with anti social forces.

10

## 2-v. Model code of ethics - Maximizing your client's interests

---

- ✓ You should always make a diligent and professional effort.
- ✓ You need to get to know your client's financial assets, experiences, knowledge as well as his/her investment goals so that you can advise to maximize his/her interests.

11

## 2-vi. Model code of ethics - Loyal and fair treatment

---

- ✓ You should show loyalty towards your clients.
- ✓ When you make a trade on behalf of your clients, top priority should be given to your clients' interests.
- ✓ You should be fair to all of your clients. Information that you have obtained is for all of your clients, not only for your important clients.

### Example 5

- Mr Kaneko is your biggest client.
- To serve Mr Kaneko better, you provide updated information on Sugi Corp only with Mr Kaneko.
- Days later, after Sugi Corp's share prices rose substantially, you started to inform other clients about Sugi Corp.

12

## 2-vi. Model code of ethics - Loyal and fair treatment

---

- ✓ Performance of your client's investment is a result of his/her decision. This is a basic principle for investment.
- ✓ You have to explain to your clients so that they can clearly understand their personal responsibility.

### Example 6

- Mr Ohno is your company's biggest client. Without Mr Ohno's orders, your company will make a loss.
- Mr Ohno bought shares, based on your recommendation, but share prices keep falling and he had to sell all of the shares.
- Mr Ohno requests you to compensate his loss, otherwise he says he will switch to a different broker.

13

## 2-vi. Model code of ethics - Loyal and fair treatment - cont.

---

- ✓ However, it may be your fault if a client feels forced to trade.

### Example 7

- Mr Sugi is a 85-year old man and he has not invested in the stock market in the past.
- You heard that Mr Sugi had a lot of cash in his bank account.
- You visited Mr Sugi and talked non-stop about your recommendation. Mr Sugi did not want to be bothered any further and placed an order.

14

## 2-vii. Model code of ethics - Fair advice to clients

---

- ✓ You must be a fair investment advisor.
- ✓ You cannot be biased when you advise your clients.
- ✓ Your advice has to be based on a high level of professional knowledge for capital markets.
- ✓ You should distinguish facts from opinions.
- ✓ Be careful of advising based on insider information.

### Example 8

- The policy lending rate fell to 10.5% in May from 12.0%.
- You think the policy rate will be further cut to 9.0%.
- When you talked to a client over the phone, you said “the policy rate will be down to 7.0% in July.”

15

## 2-viii. Model code of ethics - Higher ethical behavior

---

- ✓ You are always requested to behave ethically.
- ✓ In an event that is not written in any of laws, rules and regulations for capital markets, you also have to judge from your code of ethics and act accordingly.
- ✓ If you happen to know information that can materially impact on share prices, you should keep the information carefully.

### Example 9

- Urade Mining’s CEO is a good friend of yours.
- A week before Urade Mining releases its financial results for 2015, you heard from him that Urade Mining’s net profit was much higher than expected.
- You are sure of a substantial upside for its share price.

16

- ✓ Your daily work contributes to capital market development.
- ✓ Fairness and integrity are critical for health development of capital markets.
- ✓ Beware of losing trust. Unfair disclosure, manipulation of share prices and other misconduct could dampen healthy capital market development.

17

---

## Баярлалаа!

Та бүхэн асуулт асуух, өөрийн санал, зөвлөмжөө илгээхийг хүсвэл  
доорх хаягаар хандаарай.

**Ryota Sugishita**

Жайка Зөвлөхийн Баг  
Офис (орон нутгийн): өрөө #204, FRC

18



Project for Capacity Building of Capital Market in Mongolia:  
IPO & Dual Listing Seminar  
Costs & Benefits of IPO

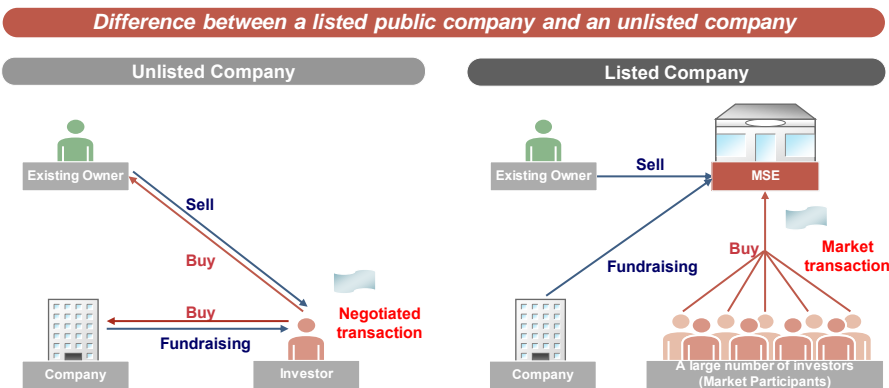
---

June 23, 2015

Daiwa Institute of Research  
Japan Economic Research Institute

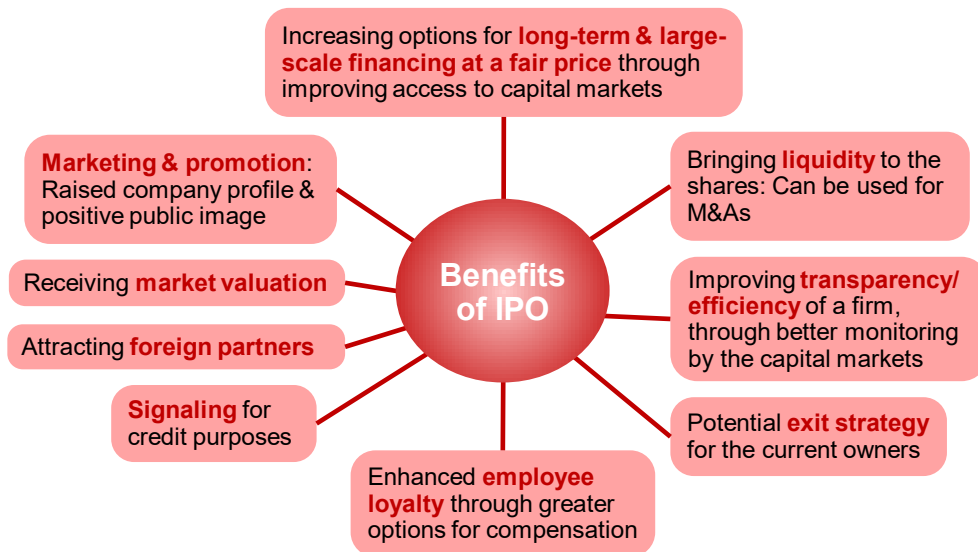
What is IPO (Initial Public Offering)?

*A company lists for the first time on a stock exchange and conducts a public offering*



## Benefits of IPO

---



3

## Why Do Firms Go Public?: Theories

---

### Life Cycle Theories

- **Zingales (1995)**: For a potential acquirer, **public targets are easier to spot** than private ones. Entrepreneurs can facilitate the acquisition of their company for a **higher value after IPO**.
- **Black & Gilson (1998)**: In VC-backed companies, entrepreneurs often **regain control of the company** from the VC.
- **Chemmanur & Fulghieri (1999)**:
  - Allows greater **dispersion of ownership**. Pre-IPO angel investors & VCs hold undiversified portfolios, therefore, are not willing to pay as high a price as diversified market investors.
  - As a firm grows & faces profitable investment opportunities, the costs of going public become worth incurring.
  - Public trading can itself add value to the firm as it inspires **confidence from investors, customers, suppliers & employees**.

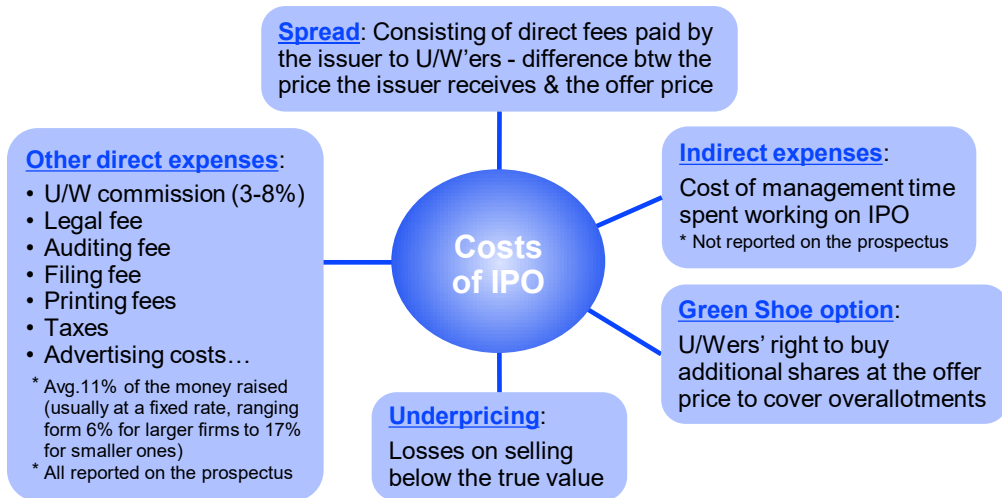
### Market-Timing Theories

- **Schultz (2000)**: **Markets provide valuable info** to entrepreneurs. Higher stock prices of companies in the same industry signal higher growth opportunities.
- **Welch & Ritter (2002)**: Semi-rational theory w/o asymmetric info to explain increased IPO volume following bull markets. Entrepreneur's sense of value derives more from their operations perspective & underlying business fundamentals than from public markets.

4

## Costs of IPO

According to the practices in US, total IPO costs are a big portion of the issue proceeds (avg. **15-30%**), which can be divided into the followings.



5

## Concerns Related to IPO



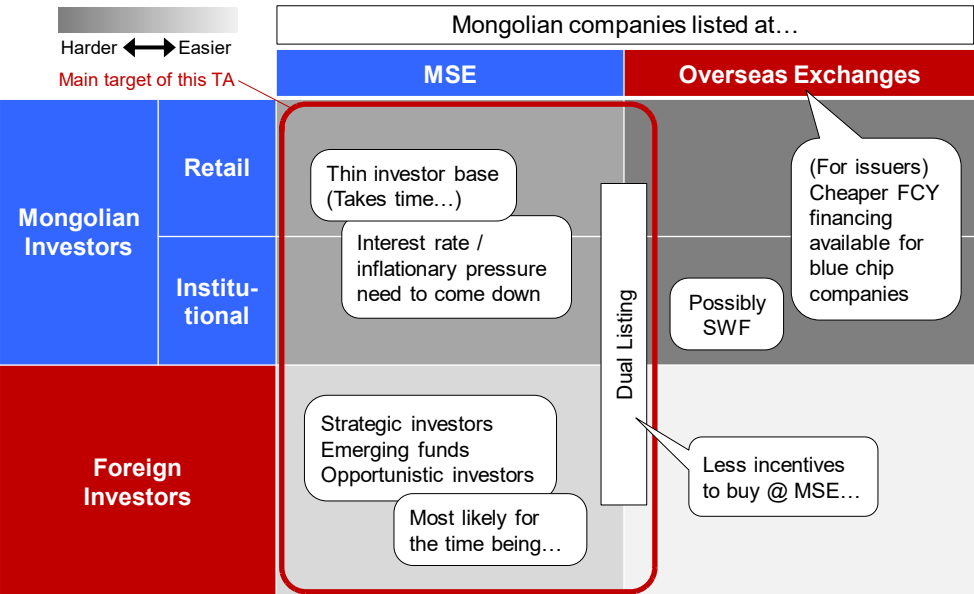
6

Private Placement vs. Public Offering

Private Placement	Public Offering
<ul style="list-style-type: none"><li>➤ Securities are sold to <b>a few investors</b> rather than to the public (e.g. VCs).</li><li>➤ Shares are <b>not registered</b>, so sales must be to <b>'accredited' (high net worth) investors</b>.<ul style="list-style-type: none"><li>- Send out <b>'offering memorandum'</b> with 20-30 pages of data &amp; info, prepared by securities lawyers.</li><li>- Buyers certify that they meet net worth/income requirements &amp; they will not sell to unqualified investors.</li></ul></li></ul>	<ul style="list-style-type: none"><li>➤ Securities are offered to the <b>public</b></li><li>➤ Shares must be <b>registered</b> with the authority (e.g. SEC@US).</li><li>➤ <b>Large-scale financing at a fair price</b> becomes available</li></ul>

7

Equity Financing in Mongolian Context



8

## Underwriting: Types

### 'Firm Commitment' Underwriting

- Issuer sells entire issue to U/W'ers
- U/W'ers then resell them to the public
- U/W'ers make money on the spread btw:
  - the price paid to the issuer and
  - the price received from investors when the shares are sold
- **U/W'ers bear the risk of not being able to sell** the entire issue for more than the cost
- Most common U/W type in US.

#### Firm Commitment as an Option

- Issuer buys a put option from the U/W'er.
- U/W'er gives a call option to investors.
- Issuer's put option becomes real only in the final pricing meeting.

### 'Best Efforts' Underwriting

- U/W'er makes 'best effort' to sell the shares at an agreed offering price
- **Issuer bears the risk of the unsold part**
- IBKs only markets the issue. Prospectus states:
  - Offer price (P)
  - Min # of shares that must be sold ( $Q_{\min}$ )
  - Max # of shares that will be sold ( $Q_{\max}$ )
- If  $Q_{\min}$  is not reached in 90 days (e.g.), investors get their money back from an escrow A/C.
- In US, only **35% of IPOs**, accounting for **13%** of the total money raised.
- **Generally for small firms.**
- Issuers can choose the price itself, otherwise IBKs would force the company to go public at very low price.

9

## Underwriting: Underwriters

### Services

- **Formulating method to issue securities**
- **Pricing** the securities
- **Selling** the securities
- **Price stabilization** in the aftermarket (by lead U/W'er)
- **Over-Allotment Option** or '**Green Shoe**' Provision:
  - Option granted to an U/W'er for a period of **15-45 (usually 30) days** after the issue date to purchase additional shares. (Typically, **up to 15%** of the shares being sold.)
  - = Call option issued by the firm to IBK.

### Profits

- Commission from the spread between the issue price (P) investors pay & the amount paid to the firm ( **$P(1-C)$** ).

10

### Underpricing

- Defined as '**the difference in price btw the closing price on the 1<sup>st</sup> day of trading & the offer price**'
- IPO pricing is very difficult, as no current market price is available.
- General practice, in which U/W'ers earn reputations through;
  - ✓ Achieving **higher price than the offer price**
  - ✓ **Selling out the shares**
- **Smaller, riskier IPOs underprice to attract investors.**

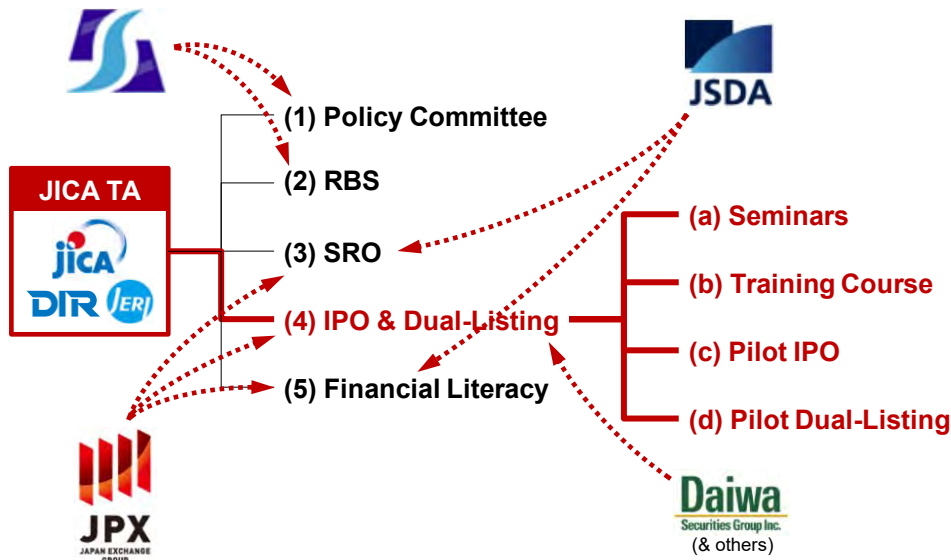
11

### Factors for a successful IPO

---

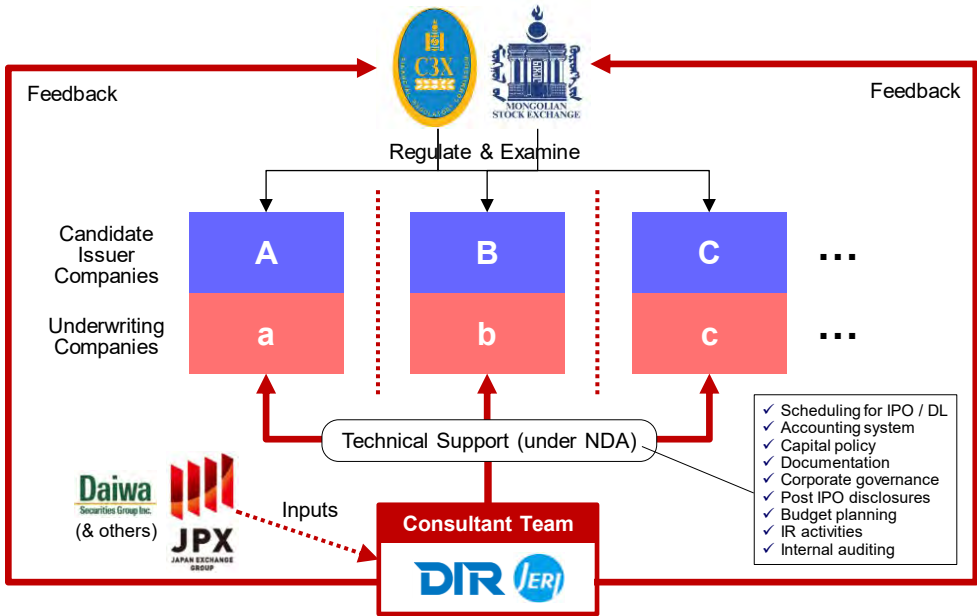


12



13

(4)-(c),(d) Pilot IPO & Dual-Listing



14

# Dual Listing: Benefits & Introduction of Asian Major Stock Exchanges

---

Discussion Material

June 2015

**Daiwa Capital Markets Hong Kong Limited**

Investment Banking Department



# What is a Dual Listing and Why?

A dual listing is a situation in which the securities of a given company are listed on more than one exchange.

A dual listing sometimes occurs when a company begins to establish an international presence by operating facilities in foreign nations. When this occurs, it is sometimes advantageous to be listed on international exchanges as well as domestic exchanges.

Assuming that the company meets the listing qualifications related to the exchange, there is usually no problem in arranging for shares/depository receipts of the company's stock to be traded on those markets.

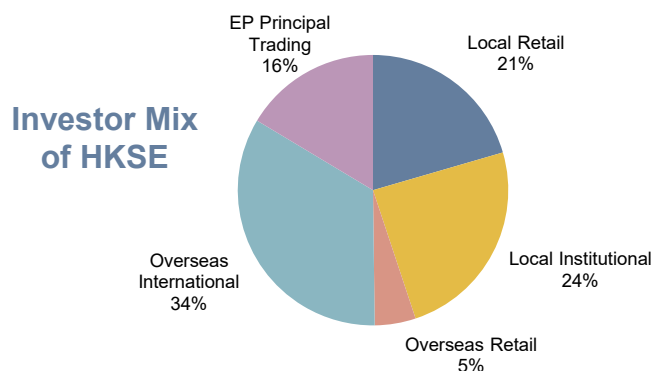
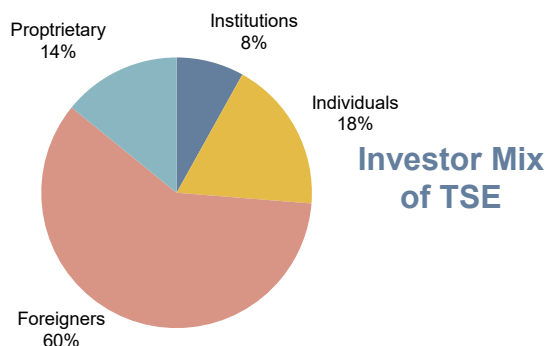
With a dual listing approach, a company can choose to list on more than one exchange simultaneously. Alternatively, a company can choose to list on one exchange followed by a secondary listing on another exchange. Subject to the listing examination that the company go through, this does not necessarily mean that the listings are not equal.

Typically, the reasoning behind a dual listing is to provide investors with more options in trading the shares/depository receipts which in turn can increase the liquidity of the company.

# Merits of Dual Listing

## Expanding Investor Base

- Dual listing might provide easier access to the investors base in that market. For example, high quality retail investors and high net worth individuals through TSE, HKSE, SGX and mainland Chinese investors (Qualified Domestic Institutional Investors) through the HKSE
- Getting listed in another exchange would also bring additional financing opportunities by conducting follow-ons in the secondary listed exchange



## Improving Foreign Investors' Awareness

- The company's name can be speeded to foreigners such as global investors and potential business partners through marketing activities including press conference
- Newspaper advertising will be prepared for the marketing and can introduce the company's name to local residents as well as global investors

**L'OCCITANE**  
EN PROVENCE

Skincare brand L'Occitane seeks up to US\$708m in HK listing



**L'Occitane sets sights on HK\$2.45b in IPO**

**Labels: Skincare**  
Provençal skincare company L'Occitane is looking to raise up to \$708 million in Hong Kong today and aims to raise about HK\$2.45 billion, with the company of Provence's L'Occitane group.  
The L'Occitane group, which is a subsidiary of the L'Occitane group, is a quarter of the company's share capital, priced at between HK\$1.00 and HK\$1.50 per share, with an overall amount of up to \$708 million.  
The shares will be listed on the HKSE and will be listed on the HKSE.  
The company is expected to close on April 15 and the shares will be listed on the HKSE on May 7, according to the company.






## **Section 1**

---

### **Dual Listing: Overview of Asian Major Stock Exchanges**




# Listing Venue Comparison

## Overview of TSE, SGX and HKSE

			
<b>Total market cap</b>	■ USD 4,378bn	■ USD 753bn	■ USD 3,233bn
<b>Total fund raised through IPO</b>	<ul style="list-style-type: none"> <li>■ 2014: USD 10.5bn</li> <li>■ 2013: USD 9.5bn</li> <li>■ 2012: USD 12.2bn</li> </ul>	<ul style="list-style-type: none"> <li>■ 2014: USD2.4bn</li> <li>■ 2013: USD5.4bn</li> <li>■ 2012: USD3.0bn</li> </ul>	<ul style="list-style-type: none"> <li>■ 2014: USD29.7bn</li> <li>■ 2013: USD21.7bn</li> <li>■ 2012: USD11.5bn</li> </ul>
<b>No. of issuer</b>	■ 3,470	■ 775	■ 1,752
<b>Turnover</b>	■ USD 5,444bn (2014)	■ USD209bn (2014)	■ USD1,521bn (2014)
<b>Issuers average historical P/E ratio</b>	■ Nikkei 225 18.3x	■ Straits Times Index: 13.4x	■ Hang Seng Index: 10.6x
<b>Investor base</b>	■ Extensive institutional investor base and very active participation from local high net worth individuals as well as foreign investors	■ Extensive institutional and private banking investor base. Investors are regionally focused on ASEAN equities	■ Extensive institutional investor base and very active participation from local retail investors. Investors are domestic focused looking for businesses that have a strong China play
<b>Listing preparation time</b>	■ c. 12 months	■ 6.5 - 8 months	■ 6 - 9 months
<b>Listing cost</b>	■ Moderate listing cost applies	■ Moderate listing cost applies	■ Moderate listing cost applies
<b>Ongoing cost</b>	<ul style="list-style-type: none"> <li>■ Moderate ongoing cost; mainly in relation to disclosure and corporate governance requirements</li> <li>■ Litigation against the issuer or its directors is uncommon</li> </ul>	<ul style="list-style-type: none"> <li>■ Moderate ongoing cost; mainly in relation to disclosure and corporate governance requirements</li> <li>■ Litigation against the issuer or its directors is uncommon</li> </ul>	<ul style="list-style-type: none"> <li>■ Moderate ongoing cost; mainly in relation to disclosure and corporate governance requirements</li> <li>■ Litigation against the issuer or its directors is uncommon</li> </ul>

# Listing Venue Comparison

## Overview of TSE, SGX and HKSE (Cont'd)

	 JPX JAPAN EXCHANGE GROUP	 SGX SINGAPORE EXCHANGE	 HKEX 香港交易所
<b>Board</b>	■ First Section	■ Main board	■ Main board
<b>Track record</b>	■ 2 years audited accounts	■ 3 years audited accounts	■ 3 years audited accounts
<b>Financial reporting</b>	■ Japanese GAAP, US GAAP <sup>1</sup> , IFRS or other GAAP <sup>2</sup> permitted by Japan's Financial Services Agency	■ FRS, IFRS or US GAAP	■ China GAAP, IFRS and HK GAAP
<b>Minimum # of shareholders</b>	■ 2,200	■ 500	■ 300
<b>Financial requirements</b>	Expected aggregate market capitalization must be at least JPY 25bn. In addition, the company must meet at least one of the following requirements: <ul style="list-style-type: none"> <li>■ (1) The total amount of profits in the last 2 years must be at least JPY 500m</li> <li>■ (2) The company's total market capitalization must be at least JPY 50bn, with sales of JPY 10bn or more in the most recent year</li> </ul>	Fulfilling one of the following requirements: <ul style="list-style-type: none"> <li>■ (1) Minimum consolidated pre-tax profit of at least SGD30m for the latest financial year and operating track record of at least 3 years</li> <li>■ (2) Profitable in the latest financial year, with an operating track record of at least 3 years and a market capitalization of at least SGD150m</li> <li>■ (3) Operating revenue (actual or pro forma) in the latest completed financial year and a market capitalization of at least SGD300m</li> </ul>	Fulfilling one of the following requirements: <ul style="list-style-type: none"> <li>■ (1) Profits of HKD50m in the last 3 years (with HKD20m in the most recent year and an aggregate of HKD30m in the two preceding years)</li> <li>■ (2) Market cap at least HKD4bn; revenue of HKD500m for the most recent audited financial year</li> <li>■ (3) Market cap at least HKD2 billion; revenue of HKD500m for the most recent audited financial year; Positive cashflow from operating activities of HKD100m in aggregation for the 3 precedent years</li> </ul>
<b>Lock-up requirements</b>	■ N.A.	■ 6 – 12 months for controlling shareholders (>15%)	■ Controlling shareholders (>30%) not to dispose of any shares within 6 months of listing, and to maintain as the controlling shareholding in the following 6 months
<b>Post-IPO equity fundraising</b>	■ 6 months constraint according to market practice	■ Capital raising of up to 50% allowed under general mandate; shareholders' approval required above that	■ Capital raising of up to 20% allowed under general mandate, which is normally obtained through the annual general meeting; shareholders' approval required for more than 20%

Notes:

1. US GAAP is only applicable for a company registered with the US SEC that prepares consolidated financial statements in accordance with regulations by SEC
2. Other GAAP includes GAAP in Canada, UK, Korea, HK, Taiwan, Australia, Singapore and Malaysia

# Listing on the TSE

## Key Listing Requirements

### ✓ Financial Requirements

- New applicants must fulfill one of the following three financial requirements:
  - I. The total amount of profits in the last 2 years must be at least JPY 500m
  - II. The company's total market capitalization must be at least JPY 50bn, with sales of JPY 10bn or more in the most recent year

### ✓ Operating history

- A foreign company is required to have continuously carried out its business for three full fiscal years before the date of its listing application, as evidenced by setting up a board of directors (or an analogous institution)

### ✓ Auditor's opinion / financial statements

- There must be no false statements in any of the year-end financial statements for the last 2 years or in any quarterly financial statements for a quarterly accounting period ending in the current year
- A CPA must have opined that the financial statements represented the company's financial position "fairly," on "unqualified terms" or "fairly" albeit on "qualified terms" in an audit report attached to the financial statements for the next-to-last full business year
- A CPA must have opined that the financial statements represented the company's financial position "fairly," on "unqualified terms" or "represented valid information" in an audit report attached to the financial statements for the most recent full business year and the quarterly financial statements for the current business year

### ✓ Corporate Governance

- The company must have an internal control system under J-SOX provisions for a board member to adequately execute his or her duties and for the company to effectively conduct its business activity, which is appropriately secured and operated
  - I. Basic approach to corporate governance and information about its capital structure, corporate attributes etc.
  - II. The company's business management function, as regards its management decision, execution and supervision and other matters pertaining to corporate governance system, and the reasons for selecting this organization and system
  - III. The implementation status of any measures to protect the interests of shareholders and other stakeholders
  - IV. The company's basic approach to, and implementation status of, its internal control system, including matters concerning the development of the corporate structure for eliminating anti-social forces and
  - V. Other matters deemed necessary by the TSE

### ✓ Minimum Public Float

- At least 20,000 trading units of tradable shares (i.e., not held by insiders or large shareholders)
- Ratio of tradable shares to listed shares of at least 35%

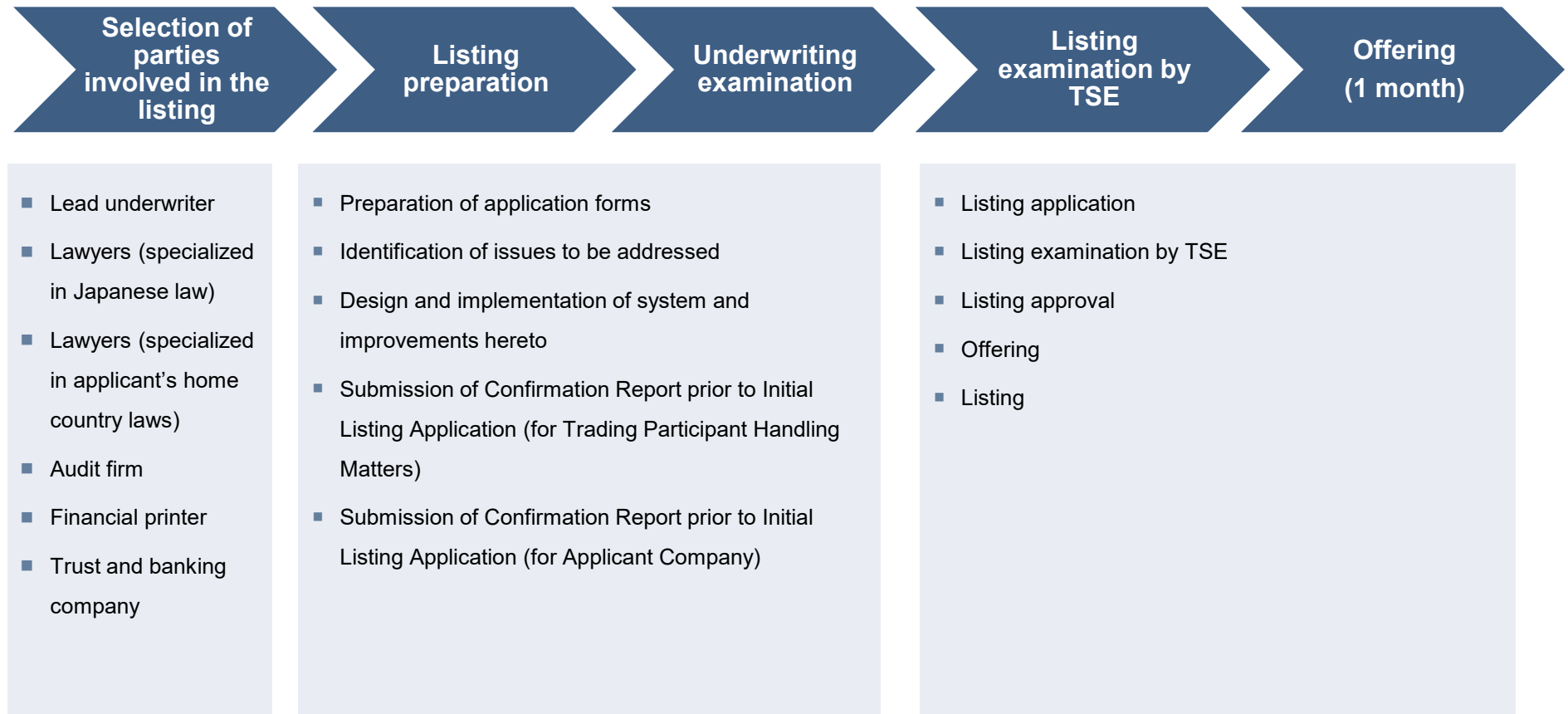
### ✓ Connected Transaction

- Listing Rules requires that The company and its related companies must not be making transactions with interested persons, related companies or other entities under conditions clearly advantageous and/or disadvantageous to the applicant company

- It is advisable for a contemplating issuer to consider these requirements carefully prior to preparing its listing on the TSE
- Daiwa is happy to discuss further with you to design the most appropriate approach to solve potential issues

# Listing on the TSE

## Overview of the Listing Process



# Listing on the HKSE

## Key Listing Requirements

### ✓ Financial Requirements

- A trading record of not less than 3 financial years
- New applicants must fulfill one of the following three financial requirements:
  - I. Profit Test: Profits of HKD50 million in the last 3 years (with HKD20 million in the most recent year and an aggregate of HKD30 million in the two preceding years)
  - II. Market Cap/Revenue Test: Market cap of at least HKD4 billion at the time of listing; and Revenue of at least HKD500 million for the most recent audited financial year
  - III. Market Cap/Revenue/Cashflow Test: Market cap of at least HKD2 billion at the time of listing; Revenue of at least HKD500 million for the most recent financial year; and Cashflow from operating activities of at least HKD100 million in aggregate for the 3 preceding financial years

### ✓ Corporate Governance

- Board comprises of at least 3 independent non-executive director ("INED")
- Audit committee with at least 3 members, with a majority of INEDs (at least one INED with appropriate professional qualifications/accounting/financial management expertise)

### ✓ Connected Transaction

- Listing Rules requires that the interest of shareholders as a whole are taken into account by a listed issuer when entering into any connected transactions
- If size of any connected transaction is above a certain threshold, waivers from the stock exchange will be required

### ✓ Management & Ownership Continuity

- Management continuity for at least the 3 preceding years; and
- Ownership continuity and control for at least the most recent audited financial year

### ✓ Competition with Controlling Shareholder

- Listing Rules requires that, before listing, competition between the issuer and its controlling shareholders' other business should be minimized through proper segregation of business
- All existing competition should be eliminated and future competition will not be permitted
- The issuer should be able to demonstrate: (i) Management independence; (ii) Financial independence; and (iii) Operational independence

### ✓ Minimum Public Float

- At least 25% of the total issued share capital (minimum of HKD50 million) must at all times be held by the public
- For issuers with an market cap of over HKD10 billion at the time of listing, the public float can be lowered to a percentage between 15% and 25%
- A minimum of 300 shareholders

### ✓ Lock-up Period

- The issuer's controlling shareholder (and any pre-IPO investor) shall not: (i) dispose of shares in the period of 6 months from the listing date; and (ii) cease to be a controlling shareholder in the period of another 6 months on the date on which the period referred to above expires

- It is advisable for a contemplating issuer to consider these requirements carefully prior to preparing its listing on the HKSE

- Daiwa is happy to discuss further with you to design the most appropriate approach to solve potential issues



# Listing on the HKSE

## Overview of the Listing Process

### Preparation

- Appoint sponsor(s) and other intermediaries (submit sponsor engagement letter to SEHK at least 2 months before A1 submission)
- Draw up timetable
- Perform all due diligence
- Complete prospectus for publication upon A1
- Complete audited annual reports for the last 3 financial years
- Identify conflict issues with parent group and connected transactions
- Clearly delineate business from the parent group
- Complete internal control report and remedy material deficiencies
- Finalize legal opinions
- Resolve compliance issues (if any)
- Complete verification
- Parent group to submit spinoff proposal to SEHK for approval (3 months before A1)
- Parent group to publish spinoff announcement at A1
- Prepare other listing application documents("A1 filings")
- Appoint directors and other committee members

### SEHK Approval

- File A1 application
- Publish Application Proof of prospectus upon A1 on HKEx website (from 1 April 2014 onwards)
- Response to comments from SEHK
- Update financial reports (if applicable)
- Listing hearing
- Shareholder approval of parent group may be required

### Marketing & Pricing

- Prepare marketing materials
- Syndicate research analysts prepare research reports
- Secure cornerstone investors
- Pre-marketing roadshow
- Global roadshow
- Issue prospectus and commence Hong Kong public offering
- Pricing and allocation
- Receive listing approval
- Commence trading

# Listing on the SGX

## Key Listing Requirements

SGX Mainboard Primary Listing				
Quantitative Requirements		Alternative 1	Alternative 2	Alternative 3
	Pre-tax profit	SGD30M in latest FY	Profitable in latest FY	Operating revenue in latest completed FY
	Operating track record	3 years	3 years	1 year or Nil for REIT/BT
	Market Cap	Nil	SGD150M	SGD300M
Shareholder Spread	Companies with market cap <SGD300M – 25% public float Companies with market cap ≥SGD300M– 12-20% public float At least 500 public shareholders			
Independent Directors	Foreign company must have at least 2 Singapore resident independent directors			
Moratorium	<div>➤ After IPO, promoters to retain 100% for 1<sup>st</sup> 6 months</div> <div>➤ Pre-IPO investors &gt;5% shareholding to retain profit portion for 6 months</div>			
SGX Mainboard Secondary Listing				
Shareholder Spread	At least 500 shareholders worldwide, or At least 500 shareholders in Singapore or 1,000 shareholders worldwide where there is no established framework and arrangement to facilitate the movement of shares between SGX and the primary home exchange			
Accounting Standard	Restatement to SFRS or IFRS or US GAAP			
Prospectus Requirement	Required. Subject to the Securities and Futures Act (Chapter 289) of Singapore			

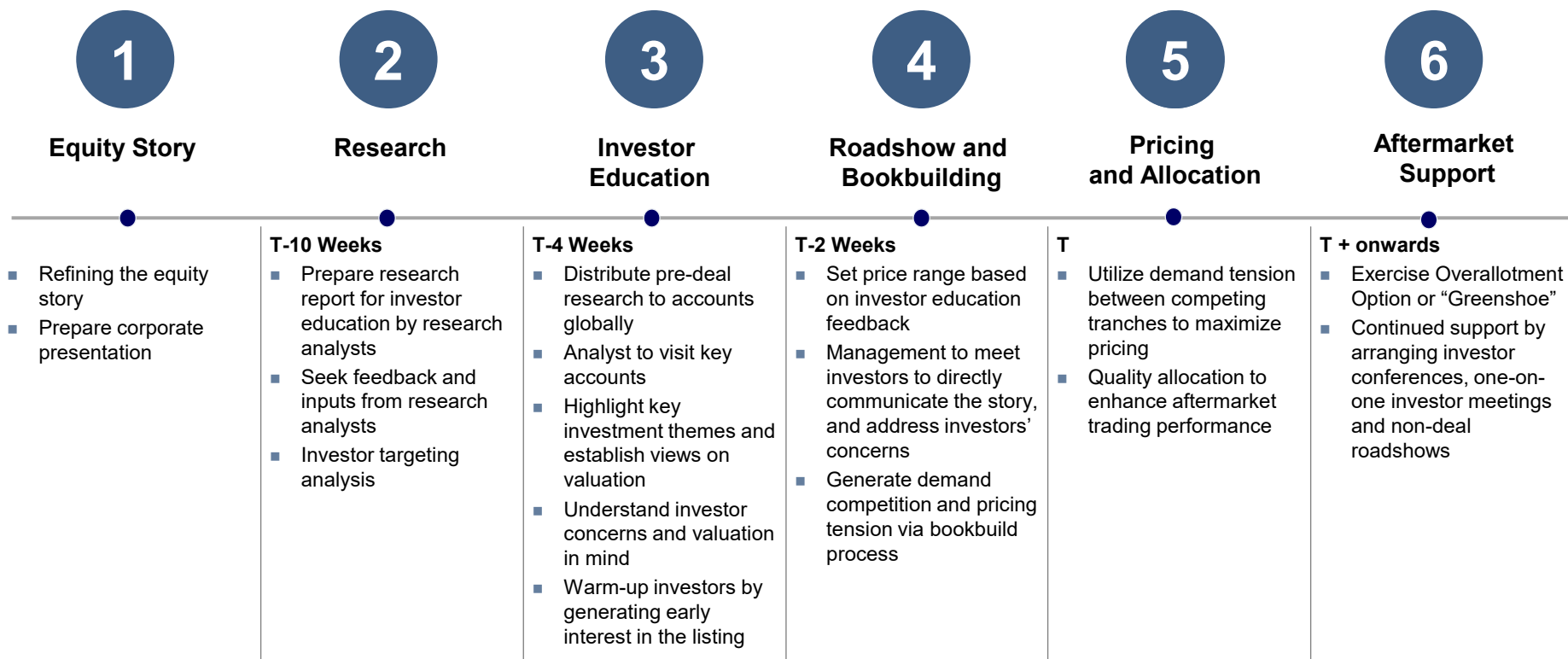
# Listing on the SGX

## Primary Listing Timetable

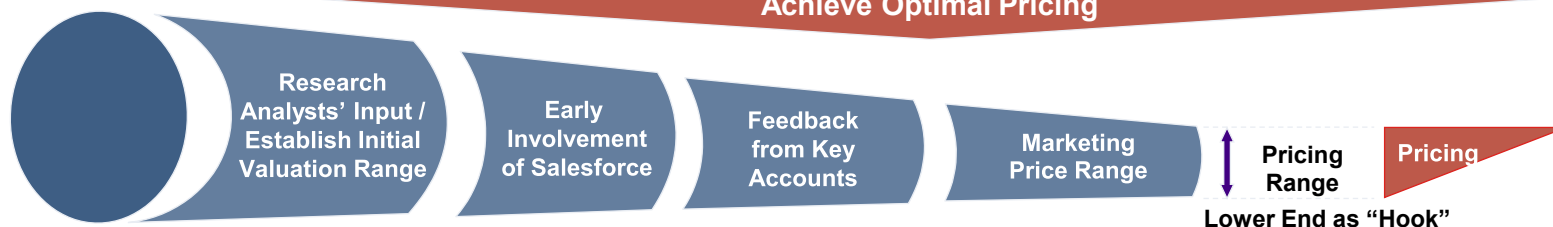
Submission Preparation	SGX & MAS Review	Public Comments	Registration	Trading Commences
<p>Preparation of SGX listing application and submission documents</p> <p>Pre-meetings with Singapore listing authorities</p>	<p>Submit listing application &amp; prospectus to SGX</p> <p>Submit prospectus to MAS for pre-lodgment review</p> <p>SGX reviews listing application for compliance with listings requirements and indicates eligibility to list</p>	<p>Lodge prospectus with MAS</p>	<p>Launch offer</p> <p>Submit replacement or supplementary prospectus to MAS and SGX concurrently (if any)</p>	<p>Issuer makes pre-quotation disclosure (if any)</p> <p>SGX lists issuer's securities and commences secondary trading</p>

# Overview of the Listing Process

## Marketing Strategy



### Achieve Optimal Pricing






# Overview of the Listing Process

## Management Roadshow and Bookbuilding

- A well-executed, focused roadshow and bookbuilding process is critical to achieving the optimal valuation for the issuer. The management roadshow should focus on delivering a compelling equity and mitigating investor concerns to maximize demand tension

### Indicative Management Roadshow Itinerary – Maximizing the Investment Tension

	Locations	Duration	Targets
Asia	<ul style="list-style-type: none"> <li>Hong Kong, Singapore, Tokyo</li> </ul> 	3 – 5 days	<ul style="list-style-type: none"> <li>“Local” investors who understands the industry dynamic</li> <li>Substantial holders of comparables</li> </ul>
Europe	<ul style="list-style-type: none"> <li>Edinburgh, Frankfurt, Geneva, London, Paris, Zurich</li> </ul> 	3 – 4 days	<ul style="list-style-type: none"> <li>Top sectorfunds</li> <li>HNW private banking accounts</li> <li>Government pension funds</li> </ul>
U.S.	<ul style="list-style-type: none"> <li>New York, Boston, Los Angeles San Francisco</li> </ul> 	2 – 3 days	<ul style="list-style-type: none"> <li>Global institutional investors</li> <li>Top sector focusedfunds</li> </ul>



#### Preparatory Phase...

#### ...On the Road...

#### ...Building up the Book

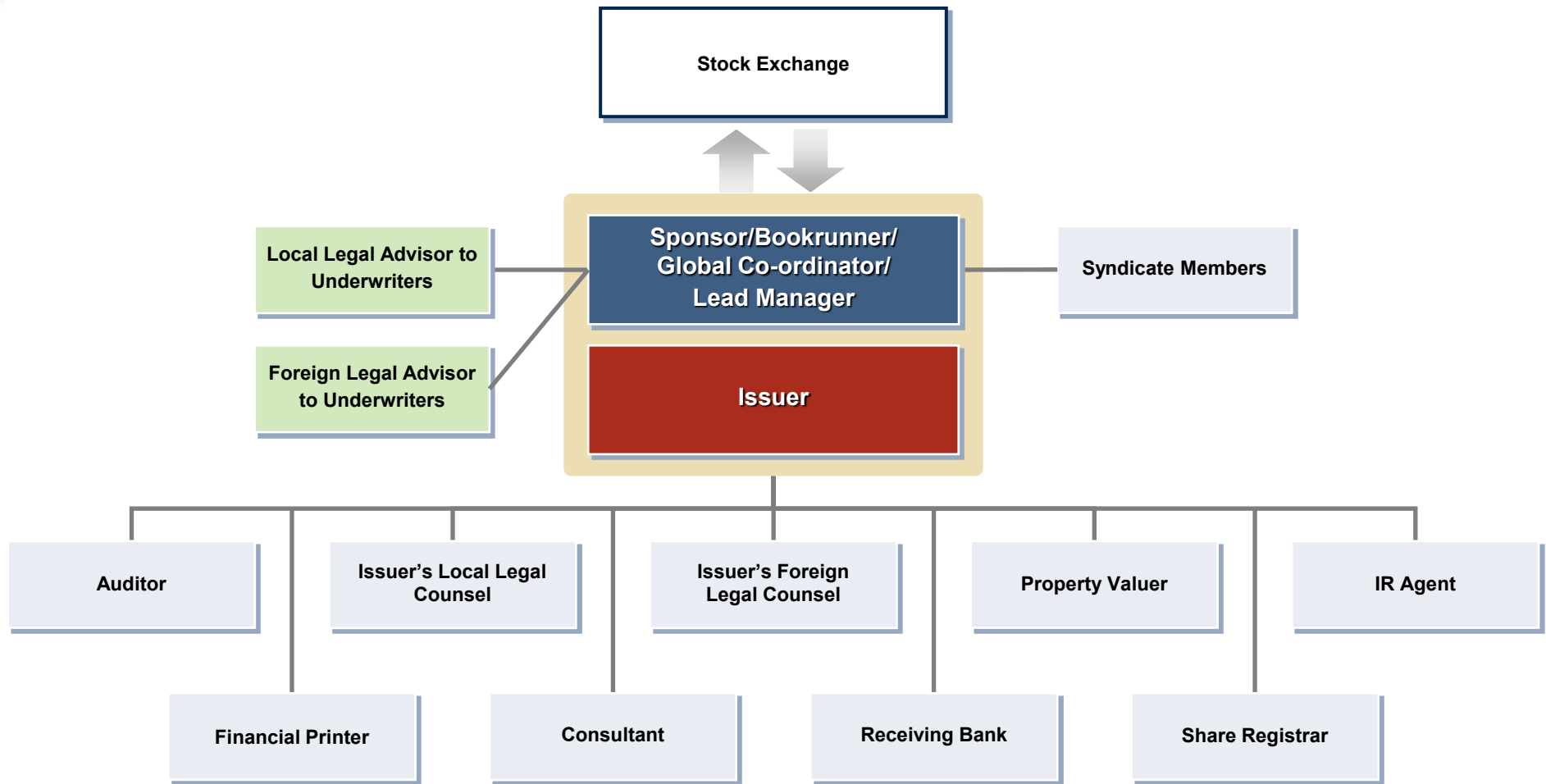
- Format:** One-on-one meetings, group luncheons, breakfast meetings, and press conference
- Investors:** ~ 100 – 150 investor meetings
- Teams:** Two management teams for international roadshow
- Objectives:** 1) Educate investors on equity story; 2) Build demand momentum and perceived scarcity of shares; and 3) Achieve optimal pricing and over-subscription levels for the offering

- Daiwa will assist the issuer in preparing the roadshow presentation which will be used to showcase the issuer's equity story, highlighting the investment merits and addressing key investor concerns
- Daiwa will coordinate all logistical matters

- A typical roadshow will consist of meeting close to 100-150 investors
- Daiwa will provide daily updates to the issuer's regarding the status of bookbuilding as well as briefing management ahead of investor meetings

- While management team is on the road marketing the issue, investors will register their interest and price sensitivity to Daiwa via our global sales force
- Daiwa ECM team will compile a book of demand and present it to the issuer at the end of the roadshow period

# Working Parties for Listing



# Role of Each Party

<b>Sponsor</b>	<ul style="list-style-type: none"> <li>• Administrative responsibilities</li> <li>• Assistance in drafting the prospectus with legal advisers</li> <li>• Negotiation of the prospectus with the regulator or exchange</li> </ul>
<b>Bookrunner Global Coordinator Lead Manager</b>	<ul style="list-style-type: none"> <li>• Global roadshow arrangements</li> <li>• Coordinating between various parties involved in the transaction</li> <li>• Maintaining the list of orders placed by institutional investors in the listing process and deciding on the allocations of stock</li> <li>• Marketing, selling and branding for the issuer</li> </ul>
<b>Issuer's Legal Adviser</b>	<ul style="list-style-type: none"> <li>• Lead role in drafting the prospectus</li> <li>• Conducts due diligence into the affairs of the issuer</li> <li>• Advises on listing rules</li> <li>• Negotiation of various agreements entered into by the issuer with banks and other parties</li> <li>• Issues legal opinions and disclosure letter if necessary</li> </ul>
<b>Underwriter's Legal Adviser</b>	<ul style="list-style-type: none"> <li>• Drafts the underwriting and other agreements, as well as guidelines for pre-deal research</li> <li>• Communicating with listing authority or regulator</li> </ul>
<b>Auditor</b>	<ul style="list-style-type: none"> <li>• Draw up audited accounts according to the generally agreed accounting principles required by the regulator for the relevant period</li> <li>• Provide the issuer and underwriters with comfort letters in which they will source, cross-check or re-compute all financial information included in the prospectus with the company's existing records</li> </ul>
<b>Receiving Bank</b>	<ul style="list-style-type: none"> <li>• Often one or more large commercial banks</li> <li>• Appointed to manage the application process by the public for the retail offering</li> </ul>

# Role of Each Party

<b>Internal Control Consultant</b>	<ul style="list-style-type: none"> <li>• Provide guidelines to internal control, including corporate governance, segregation of duties, retention of records, review and analysis of results versus organization goals/plans, IT controls, etc.</li> </ul>
<b>Property Valuer</b>	<ul style="list-style-type: none"> <li>• Carry out independent valuation of property assets, with the reports included in the prospectus</li> </ul>
<b>Share Registrar</b>	<ul style="list-style-type: none"> <li>• Maintain a record of the public shareholders in the company to establish authenticity of ownership, ensure the accurate payment of dividends</li> <li>• Process and ballot applications from retail investors and to dispatch share certificates to applicants allocated shares in the listing process</li> </ul>
<b>IR Agency</b>	<ul style="list-style-type: none"> <li>• Develop issuer's image and promote its investment case to the wider world, which may include creation/update of website</li> <li>• Handling the logistics during the roadshow, including air travel, booking hotels and conference rooms, arranging luncheon presentations, inter-city limousine transportations, etc.</li> </ul>
<b>Financial Printer</b>	<ul style="list-style-type: none"> <li>• A third party to handle the typesetting and input multiple detailed overnight amendments</li> <li>• Distribute printouts to what will become an increasingly large number of recipients</li> </ul>
<b>Depository Banks</b>	<ul style="list-style-type: none"> <li>• Issues and redeems certificates (depository receipts – DRs)</li> <li>• Ensures payments through a custodian of dividends to the owners of the certificates</li> </ul>



# Key Considerations for Listing Candidates' Dual Listing

- Based on Daiwa's extensive dual listing deal execution experience, we summarized key considerations for listing candidates as below, subject to the specific situations that different companies are facing:

## Key Considerations for Dual Listing

- Due to different requirements of the exchange to be listed, it calls for companies' extra commitment to execute with more documentation requirements

### 1 Waiver Application

- Waivers could be applied when there is difference in regulation between Mongolia and respective exchanges

### 2 Accounting Standard

- The accounting standard of listing applicant generally ought to be shifted to GAAP accepted by respective markets

### 3 Continuous Disclosure

- Annual report, interim report and other documents (quarterly reports, if applicable) required by various stock exchanges need to be disclosed in English and/or other languages

### 4 Due Diligence

- Due diligence is required to be conducted within a short time frame, to subsidiaries and related parties as well

### 5 Hong Kong Deposit Receipt

- Due to certain restrictions, there are cases where a listing candidate can only get listed in Asian exchanges through issuing DRs

## **Section 2**

---

### **Dual Listing Case Studies**

# Tosei Corp. – US\$26.8mm SGX Secondary Listing

July 2013  
Real Estate

**T O S E I**

Tosei Corporation

SGX Secondary Listing  
& Follow-on

USD 26.8 mm

Sole Bookrunner  
Sole Placing Agent

✓ First listing of Japanese real estate company on the SGX

✓ Highly successful marketing strategy – book was fully covered on the 1st day of bookbuilding

✓ Top-end priced (4.05% discount to TSE share price)

✓ Precision investor targeting – Most investors met during roadshow placed order

## Transaction Summary

Issuer	▪ Tosei Corporation
Description	▪ Diversified real estate business in Japan, engaged in property revitalization, development, rental, management and alternative investment
Ticker	▪ SGX: S2D.SP / TSE: 8923.JP
Transaction	▪ Listing by way of introduction on the SGX (Mar 2013) ▪ Follow-on offering on the SGX (Jul 2013)
Offering dates	▪ Trade: July 22, 2013; Listing: July 26, 2013
Share type	▪ 72.2% primary shares ▪ 27.8% secondary shares from CEO
Tranche split	▪ 100.0% international placing
Distribution	▪ Reg. S
Offer price range	▪ 4.0% - 8.0% discount to the TSE stock price
Offer price:	▪ SGD9.4 per share (4.05% discount to the TSE)
Offer size:	▪ US\$26.8mm (7.5% of enlarged share capital)
Valuation:	▪ 18.6x 2013E P/E and 1.35x 1Q13 P/B
Use of proceeds	▪ Partially fund the acquisition and revitalization of office buildings and residential properties ▪ Partially fund the acquisition and development of land for office, residential and commercial properties ▪ Co-equity investment in real-estate funds
Daiwa's role	▪ <b>Sole Bookrunner and Sole Placing Agent</b>

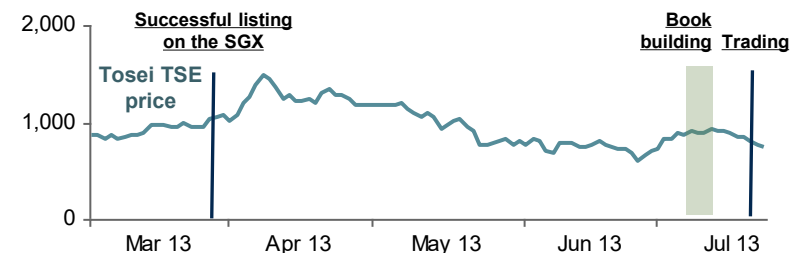
## Company Overview

- Headquartered in Tokyo, Tosei mainly engaged in the renovations, refurbishments and selling of small and mid-sized properties developed by other developers in Tokyo
- Also engaged in property rental, management and alternative investment
- Primarily listed on the first section of the Tokyo Stock Exchange
- Listed on the Singapore Stock Exchange in order to prepare itself for the intended expansion to the South East Asia market

## Daiwa's Contribution


- Acted as Manager to Tosei's successful introduction on the SGX
- Book fully covered on the 1st day of bookbuilding and multiple-times covered at book closed with good mix of long-only investors and hedge funds across Asia, Europe and the U.S.
- Top-end priced (4.05% discount)

## Transaction Timeline



# YTL Corporation Berhad – US\$43.6mn TSE Secondary Listing

February 1996  
Conglomerate



YTL Corporation Bhd  
TSE Secondary Listing  
& Follow-on  
USD 43.6mn  
Sole Bookrunner

✓ First listing of Asian non-Japanese company listed in TSE

✓ Has properties in 3 continents across Australia, Japan, Malaysia, China, Indonesia, Thailand, France, UK and Spain

✓ Largest non-government linked company in Malaysia

✓ Listed subsidiaries has a combined market capitalization of about US\$10.15 billion

## Transaction Summary

Issuer	▪ YTL Corporation Berhad
Description	▪ Conglomerate in Malaysia, engaged in utilities, property development, power generation and hotel management and development
Ticker	▪ KLSE: YTL.MK / TSE: 1773.JP
Transaction	▪ Secondary Listing in TSE (Feb 1996)
Offering dates	▪ Trade: Feb 15, 1996; Listing: Feb 29, 1996
Share type	▪ 100% Ordinary Shares
Deal Execution	▪ Fully Marketed
Distribution	▪ Reg. S
Offer price:	▪ M\$11.1 (US\$4.358)
Offer size:	▪ US\$43.58mn
Use of proceeds	▪ General corporate purpose
Daiwa's role	▪ <b>Sole Bookrunner</b>

## Company Overview

- Headquartered in Kuala Lumpur, Malaysia, YTL Corporation is the largest non-government linked company in Malaysia
- Principal business is power generation, with other business areas include construction contracting, property development, manufacturing industrial products and supplies and hotel management and development
- Extensive business coverage in Europe, Asia and Australia

## Daiwa's Contribution

- Daiwa blazed the trail by bringing the first non-Japanese company into Japanese stock market
- Deal was successful with shares fully marketed
- YTL is welcomed by Japanese investors, and thus conducted a follow-on issuance in June 1996, with another US\$102.9mn of shares issued

## Transaction Timeline



# POSCO – US\$690.6mn TSE Secondary Listing



✓ Based in Pohang, South Korea with extensive overseas presence in Asia, America, Europe & Africa

✓ 146<sup>th</sup> world's largest corporation by the Fortune global 500 in 2012

✓ 3<sup>rd</sup> largest steel maker globally in 2010

✓ Listed in Korea Stock Exchange in 2003, secondary listed in Tokyo Stock Exchange in 2005

## Transaction Summary

Issuer	▪ POSCO
Description	▪ Steel maker based in South Korea with presence in Asia, America, Europe & Africa
Ticker	▪ KRX 005490.KS / TSE: 5412.JP
Transaction	▪ Secondary Listing in TSE (Oct 2005)
Instrument Type	▪ American Depositary Receipt
Deal Execution	▪ Fully Marketed
Offer price:	▪ US\$ 49.33
Offer size:	▪ US\$43.58mn
Use of proceeds	▪ General corporate purposes

## Aftermarket Performance

Aftermarket	Open	1 Day	1 Week	2 Weeks	1 Month	3 Months	6 Months	1 Year
Price	50.5	50.86	52.72	57.28	55.63	70.78	59.13	80.74
% Changes	2.37%	3.10%	6.87%	16.12%	12.77%	43.48%	19.87%	63.67%

## Company Overview

- Recorded the largest profits in global steel industry in 2004.
- Operates a joint venture with U.S. Steel, the 15<sup>th</sup> largest steel maker in 2013, named USS-POSCO in Pittsburg, California.
- Subsidiaries and affiliates reach China, Japan, Vietnam, Myanmar, Malaysia, India, Australia, US, Canada, and Mexico.
- Aims to achieve "Global Top 100, 200 Trillion Sales" by 2020.
- Manufactures six major types of steel products: cold-rolled steel/galvanized steel, hot-rolled steel, steel plates, wire rods, stainless steel and electrical steel plates.

## Timeline

Announcement / Filing Date	▪ 24 Oct 2005
Pricing Date	▪ 15 Nov 2005
Trade Date	▪ 15 Nov 2005
First Trade Date	▪ 19 Jan 2006
Settlement Date	▪ 22 Nov 2005

# Fast Retailing –HKSE Secondary Listing by Introduction

February 2014  
Clothing Retail



Fast Retailing

HKSE  
Secondary Listing

☒ Leading clothing retailer in Asia with an extensive global retail network

☒ Strong portfolio of established brands with “Uniqlo” as one of the most well-known

☒ Known for its high quality clothing, innovation, and exceptional customer value

☒ 4<sup>th</sup> Company listed in HKSE through HDR

## Transaction Summary

Issuer	▪ Fast Retailing Co. Ltd
Description	▪ Leading clothing retailer in Asia with an extensive global retail network
Ticker	▪ TSE: 9983.JP / HKSE: 6288.HK
Transaction	▪ Secondary Listing in HKSE (Feb 2014)
Instrument Type	▪ Hong Kong Depository Receipt
Offer price:	▪ HKD 27.37 (USD 3.53)

## Timeline

Announcement Date	▪ 28 Feb 2014
Amendment Date	▪ 03 Mar 2014
Effective Date	▪ 05 Mar 2014

## Aftermarket Performance

Aftermarket	Open	1 Day	1 Week	2 Weeks	1 Month	3 Months	6 Months	1 Year
Price (in HKD)	28.90	29.40	27.75	27.70	28.55	25.75	25.60	29.65
% Changes	5.59%	7.42%	1.39%	1.21%	4.31%	-5.92%	-6.47%	8.33%

## Company Overview

- A Japanese retail holding company whose shares are listed on the TSE and a retailer of quality clothing
- Total market cap reached HK\$282bn by the time it is listed in HKSE
- The listing was by introduction through HDR. 1 TSE Share equals to 100 HDRs
- Largest clothing retailer in Asia Pacific in 2012 according to Euromonitor, with a 2.2% share of the Asia Pacific clothing market
- Uniqlo, its mainstay brand, has 251 stores in China, 19 in Hong Kong and 17 in US as of Nov 30, 2013

## Transaction Highlight

- 4<sup>th</sup> Company listed in HKSE through HDR
- No capital raised. The listing is mainly for marketing purpose, and liquidity is therefore comparatively lower
- Price surged in its Hong Kong trading debut, with intraday high of 31% increase, but then fell back and closed the day 5.6% higher
- Direct comparable stocks include Coach Inc. (HDR), and Prada SpA (primary listing in Hong Kong)

# South Gobi – US\$442.3mn HKSE Secondary Listing



☒ High quality coal asset located in Mongolia, targeting at Chinese market

☒ Well received by investors and therefore exercised overallotment option

☒ Attracted cornerstone investors including Baytree Investments and CIC

☒ IPO in TSX on 15 December 2003, and secondary listed in HKSE on 29 Jan 2010

## Transaction Summary

Issuer	▪ South Gobi Resources
Description	▪ Mining company based in Vancouver, Canada, with coal mine in Mongolia
Ticker	▪ TSX: SGQ.CA/ HKSE: 1878.HK
Transaction	▪ Secondary Listing in HKSE (Jan 2010)
Distribution	▪ Reg. S / 144A
Instrument Type	▪ Ordinary Shares
Offer price:	▪ HKD126.04 (US\$16.23)

## Company Overview

- An integrated coal mining, development and exploration company, focused on exploration and development of its Permian-age metallurgical and thermal coal deposits in Mongolia's South Gobi Region
- The coal assets are strategically located on China-Mongolia boundary, targeting at the Chinese market

## Timeline

Announcement Date	▪ 11 Jan 2010
Roadshow Start Date	▪ 11 Jan 2010
Subscription End Date	▪ 20 Jan 2010
Pricing Date	▪ 21 Jan 2010
First Trading Date	▪ 29 Jan 2010
Overallotment Exercised Date	▪ 19 Feb 2010

## Aftermarket Performance

Aftermarket	Open	1 Day	1 Week	2 Weeks	1 Month	3 Months	6 Months	1 Year
Price (in HKD)	123.5	112.00	116.60	122.50	119.90	100.00	100.50	113.20
% Changes	-2.02%	-11.14%	-7.49%	-2.81%	-4.87%	-20.66%	-20.26%	-10.19%

## **Section 3**

---

### **Introduction to Daiwa Capital Markets**



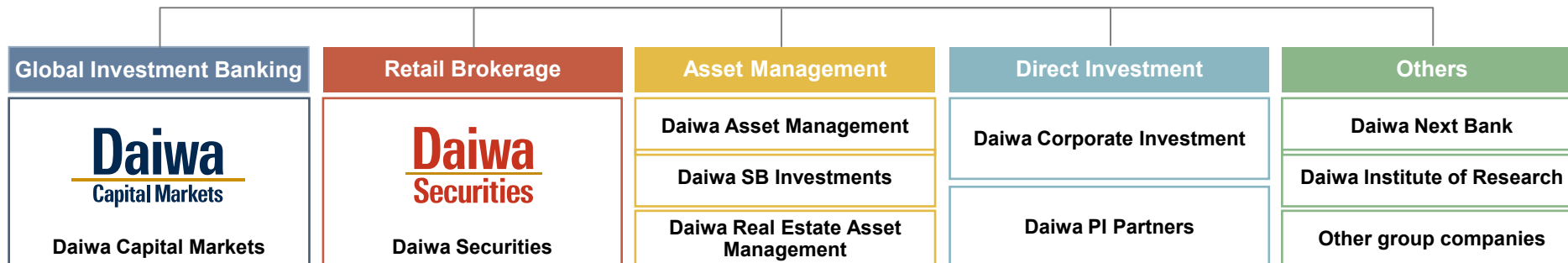
# Overview of Daiwa Securities Group

Japan's Leading Financial Services Group with Global Operations

**Daiwa Securities Group Inc.**

Market cap: approx. USD 14 billion

Employees: over 13,000



**Best Samurai  
House  
2014**



**Most Creative Global  
Investment Bank  
2013**



**Asia Equity  
Follow-on  
2013**



**Asia Equity &  
Equity-linked  
2013**



**Asia IPO  
Underwriting  
2012**

**Daiwa**  
Capital Markets

# Overview of Daiwa Capital Markets

A Comprehensive and Award-winning Investment Banking Platform

## Daiwa Capital Markets

M&A	Corporate Finance	Debt Origination	Structured Finance	Derivatives	Sales and Trading	Brokerage	Research
<ul style="list-style-type: none"> <li>■ M&amp;A</li> <li>■ Corporate Restructuring</li> <li>■ Private Placements</li> </ul>	<ul style="list-style-type: none"> <li>■ IPO (Primary markets)</li> <li>■ Underwriting</li> <li>■ Placements (Secondary markets)</li> <li>■ Private Placements</li> </ul>	<ul style="list-style-type: none"> <li>■ Samurai bonds</li> <li>■ Yen bonds</li> <li>■ Dollar bonds</li> <li>■ Other currency bonds</li> <li>■ Primary market trading</li> <li>■ Secondary market trading</li> </ul>	<ul style="list-style-type: none"> <li>■ Securitization</li> <li>■ Structured notes</li> </ul>	<ul style="list-style-type: none"> <li>■ Interest rate derivative products</li> <li>■ Equity derivative products</li> <li>■ FX derivative products</li> <li>■ OTC derivative products</li> </ul>	<ul style="list-style-type: none"> <li>■ Equities</li> <li>■ Bonds</li> <li>■ Futures</li> <li>■ Options</li> <li>■ FX</li> </ul>	<ul style="list-style-type: none"> <li>■ Stock custodian</li> <li>■ Margin financing</li> <li>■ Brokerage</li> <li>■ Bond settlement</li> <li>■ Investment advisory</li> </ul>	<ul style="list-style-type: none"> <li>■ Investment Strategy</li> <li>■ Macro Economy</li> <li>■ Sector Research</li> <li>■ Major Global Listed Companies</li> </ul>

 <p><b>Deal Watch</b></p> <ul style="list-style-type: none"> <li>■ Samurai Bond House of the Year</li> <li>■ Best Yen bond</li> </ul> <p>Mar 2015</p>	 <p><b>IFR</b></p> <ul style="list-style-type: none"> <li>■ Yen Bond House of the Year</li> </ul> <p>Jan 2015</p>	 <p><b>Thomson Reuters</b></p> <ul style="list-style-type: none"> <li>■ Most Recognized Investment Bank in Japan</li> </ul> <p>Sep 2014</p>	 <p><b>Finance Asia</b></p> <ul style="list-style-type: none"> <li>■ Best Samurai House</li> </ul> <p>Apr 2014</p>	 <p><b>EMEA Finance</b></p> <ul style="list-style-type: none"> <li>■ Yen Bond House of the Year</li> <li>■ Best Yen Bond</li> </ul> <p>Mar 2014</p>	 <p><b>Euromoney</b></p> <ul style="list-style-type: none"> <li>■ Best Equity House in Japan</li> </ul> <p>Jul 2013</p>	 <p><b>EMEA Finance</b></p> <ul style="list-style-type: none"> <li>■ Yen Bond House of the Year</li> <li>■ Samurai Bond House of the Year</li> </ul> <p>Mar 2013</p>	 <p><b>Asia Money</b></p> <ul style="list-style-type: none"> <li>■ Best Yen Bond</li> <li>■ Best IPO</li> <li>■ Best M&amp;A in Japan</li> </ul> <p>Feb 2013</p>
---	---	---	--	---	---	--	--

# Overview of Daiwa Capital Markets

Unparalleled Presences Across Asia Pacific

Daiwa Capital Markets  
Hong Kong Limited

Daiwa Capital Markets  
Singapore Limited

Daiwa Securities Capital  
Markets Korea Co., Ltd.

Daiwa Capital Markets  
India Private Ltd.

Daiwa Capital Markets  
Australia Limited



Daiwa Securities Co. Ltd.  
Beijing Representative  
Office

Daiwa (Shanghai)  
Corporate Strategic  
Advisory Co. Ltd.

Daiwa Securities Co.  
Ltd. Bangkok  
Representative Office

Daiwa Securities Co. Ltd.  
Hanoi Representative  
Office

Daiwa-Cathay Capital  
Markets Co.Ltd.

DBP-Daiwa Capital  
Markets Philippines, Inc.

# Daiwa is a Leading Asia Pacific Equity House

## Highly Ranked in Asian Equity League Tables

### 2014 Equity and Equity-linked – Asia <sup>(1)</sup>


Rank	Bookrunner	Deal Value (USD mm)	No. of Deals	% Market Share
1	Morgan Stanley	15,781	114	9.4%
2	Nomura	13,863	126	8.3%
3	Goldman Sachs	11,177	82	6.7%
4	Bank of America Merrill Lynch	8,004	56	4.8%
5	UBS	7,391	96	4.4%
6	JPMorgan	6,810	64	4.1%
7	Sumitomo Mitsui Financial Group	6,247	70	3.7%
8	<b>Daiwa</b> Capital Markets	<b>5,713</b>	<b>78</b>	<b>3.4%</b>
9	HSBC	5,707	47	3.4%
10	Deutsche Bank	5,256	57	3.1%

### 2014 Equity and Equity-Linked – Major Asian Markets <sup>(2)</sup>

Rank	Bookrunner	Deal Value (USD mm)	No. of Deals	% Market Share
1	Morgan Stanley	14,921	100	12.8%
2	Nomura	13,770	122	11.8%
3	Goldman Sachs	8,647	64	7.4%
4	Bank of America Merrill Lynch	6,368	42	5.5%
5	Sumitomo Mitsui Financial Group	6,247	70	5.4%
6	<b>Daiwa</b> Capital Markets	<b>5,653</b>	<b>77</b>	<b>4.9%</b>
7	HSBC	5,295	40	4.6%
8	Mizuho	4,557	52	3.9%
9	UBS	4,489	70	3.9%
10	Bank of China	3,496	44	3.0%

### Key Transactions

  
CT Environmental  
Private Placement to GIC  
USD 80 mm  
Financial Advisor  
Jan 2015

  
WH Group  
HKEx IPO  
USD 2.4 bn  
Joint POWL Arranger  
Aug 2014


  
Accordia Golf Trust  
SGX IPO  
USD 612 mm  
Joint GC  
Joint Bookrunner  
Aug 2014


  
Neo Solar Power  
Convertible Bonds  
USD 120 mm  
Joint GC  
Joint Bookrunner  
Jul 2014


  
China CNR  
HKEx IPO  
USD 1.3 bn  
Joint Bookrunner  
Joint Lead Manager  
May 2014


  
REXLot Holdings  
Convertible Bonds  
USD 244 mm  
Joint GC  
Joint Bookrunner  
Apr 2014

  
China Everbright Bank  
HKEx IPO  
USD 3.2 bn  
Joint Bookrunner  
Sole POWL Arranger  
Dec 2013

  
econtext Asia  
HKEx IPO  
USD 66 mm  
Sole GC  
Sole Sponsor  
Dec 2013

  
Modern Land  
HKEx IPO  
USD 77 mm  
Joint GC  
Sole Sponsor  
Jul 2013

  
Tosei Corporation  
SGX Listing & Follow-on  
USD 27 mm  
Sole Bookrunner  
Sole Listing Manager  
Jul 2013



















  
CPM Resources  
Convertible Bonds  
USD 130 mm  
Sole GC  
Sole Bookrunner  
Jan 2013

  
PICC Group  
HKEx IPO  
USD 3.6 bn  
Joint Bookrunner  
Joint Lead Manager  
Dec 2012

# Daiwa is a Leading Asia Pacific Equity House

## Selected ECM Track Record in Asia Ex-Japan


### Selected ECM Track Record in Asia Ex-Japan

 <b>GF Securities</b> <b>广发证券</b> <b>GF SECURITIES</b> <b>HKEx IPO</b> <b>USD 3.6 bn</b> <b>Joint Lead Manager</b> <b>Apr 2015</b>	 <b>CT Environmental</b> <b>中滔環保</b> <b>CTEG</b> <b>Private Placement to GIC</b> <b>USD 80 mm</b> <b>Financial Advisor</b> <b>Jan 2015</b>	 <b>Hua Hong Semiconductor</b> <b>華宏宏力</b> <b>HH Grace</b> <b>HKEx IPO</b> <b>USD 331 mm</b> <b>Joint Lead Manager</b> <b>Oct 2014</b>	 <b>WH Group</b> <b>萬洲國際</b> <b>WH GROUP</b> <b>HKEx IPO</b> <b>USD 2.4 bn</b> <b>Joint POWL Arranger</b> <b>Aug 2014</b>	 <b>Accordia Golf Trust</b> <b>ACCORDIA GOLF TRUST</b> <b>SGX IPO</b> <b>USD 612 mm</b> <b>Joint GC</b> <b>Joint Bookrunner</b> <b>Aug 2014</b>	 <b>Neo Solar Power</b> <b>NEO SOLAR POWER</b> <b>Convertible Bonds</b> <b>USD 120 mm</b> <b>Joint GC</b> <b>Joint Bookrunner</b> <b>Jul 2014</b>	 <b>China CNR</b> <b>中国北车</b> <b>CNR</b> <b>HKEx IPO</b> <b>USD 1.3 bn</b> <b>Joint Bookrunner</b> <b>Joint Lead Manager</b> <b>May 2014</b>
<b>REXLOT</b> <b>御泰中彩</b> <b>REXLot Holdings</b> <b>Convertible Bonds</b> <b>USD 244 mm</b> <b>Joint GC</b> <b>Joint Bookrunner</b> <b>Apr 2014</b>	 <b>China Everbright Bank</b> <b>中國光大銀行</b> <b>CHINA EVERBRIGHT BANK</b> <b>HKEx IPO</b> <b>USD 3.2 bn</b> <b>Joint Bookrunner</b> <b>Sole POWL Arranger</b> <b>Dec 2013</b>	 <b>econtext Asia</b> <b>HKEx IPO</b> <b>USD 66 mm</b> <b>Sole GC</b> <b>Sole Sponsor</b> <b>Dec 2013</b>	 <b>Modern Land</b> <b>MO MA</b> <b>HKEx IPO</b> <b>USD 77 mm</b> <b>Joint GC</b> <b>Sole Sponsor</b> <b>Jul 2013</b>	<b>TOSEI</b> <b>Tosei Corporation</b> <b>SGX Listing &amp; Follow-on</b> <b>USD 27 mm</b> <b>Sole Bookrunner</b> <b>Sole Listing Manager</b> <b>Jul 2013</b>	 <b>Hyundai HYSCO</b> <b>HYUNDAI HYSCO</b> <b>Block Trade</b> <b>USD 13.3 mm</b> <b>Sole Agent</b> <b>Mar 2013</b>	 <b>CPM Resources</b> <b>CPM</b> <b>Convertible Bonds</b> <b>USD 130 mm</b> <b>Sole GC</b> <b>Sole Bookrunner</b> <b>Jan 2013</b>
 <b>PICC Group</b> <b>御泰中彩</b> <b>PICC</b> <b>HKEx IPO</b> <b>USD 3.6 bn</b> <b>Joint Bookrunner</b> <b>Joint Lead Manager</b> <b>Dec 2012</b>	<b>REXLOT</b> <b>御泰中彩</b> <b>REXLot Holdings</b> <b>Follow-on CB</b> <b>USD 50 mm</b> <b>Sole Bookrunner</b> <b>Sole Lead Manager</b> <b>Sep 2012</b>	 <b>Huadian Fuxin Energy</b> <b>HKEx IPO</b> <b>USD 319 mm</b> <b>Joint Lead Manager</b> <b>Jun 2012</b>	 <b>Jiangnan Group</b> <b>HKEx IPO</b> <b>USD 70 mm</b> <b>Sole GC</b> <b>Sole Sponsor</b> <b>Apr 2012</b>	 <b>Sato Holdings</b> <b>DAIWA</b> <b>DCS &amp; Labeling Worldwide</b> <b>Convertible Bond</b> <b>USD 226 mm</b> <b>Sole Bookrunner</b> <b>Mar 2012</b>	 <b>InfraWare</b> <b>InfraWare</b> <b>Block Trade</b> <b>USD 13 mm</b> <b>Sole Bookrunner</b> <b>Feb 2012</b>	 <b>Beijing Jingneng</b> <b>BJE</b> <b>HKEx IPO</b> <b>USD 272 mm</b> <b>Joint Bookrunner</b> <b>Joint Lead Manager</b> <b>Dec 2011</b>

# Daiwa is a Leading Asia Pacific Equity House

## Selected ECM Track Record in Asia Ex-Japan (Cont.)

### Selected ECM Track Record in Asia Ex-Japan

 <p><b>China Outfitters</b></p> <p>HKEx IPO USD 150 mm</p> <p>Joint Bookrunner Joint Lead Manager</p> <p>Dec 2011</p>	 <p><b>KDDI Corporation</b></p> <p>Convertible Bond USD 2.6 bn</p> <p>Sole GC Joint Bookrunner</p> <p>Nov 2011</p>	 <p><b>REXLOT</b> 御泰中彩 REXLot</p> <p>Convertible Bond USD 124 mm</p> <p>Sole Bookrunner Sole Lead Manager</p> <p>Sep 2011</p>	 <p><b>Elpida Memory</b></p> <p>Equity and CB Dual Offering USD 938 mm</p> <p>Joint GC Joint Bookrunner</p> <p>Jul 2011</p>	 <p><b>Shunfeng PV</b></p> <p>HKEx IPO USD 60 mm</p> <p>Joint Bookrunner Joint Lead Manager</p> <p>Jul 2011</p>	 <p><b>SK Gas</b></p> <p>Block Trade USD 31 mm</p> <p>Selling Agent</p> <p>May 2011</p>	 <p><b>SBI Holdings</b></p> <p>HKEx IPO USD 210 mm</p> <p>Sole GC Sole Sponsor</p> <p>Apr 2011</p>
 <p><b>San Miguel</b></p> <p>Follow-on USD 350 mm</p> <p>International Co-bookrunner</p> <p>Apr 2011</p>	 <p><b>CJ E&amp;M Corp.</b></p> <p>Block Trade USD 45 mm</p> <p>Selling Agent</p> <p>Mar 2011</p>	 <p><b>Hutchison Ports Trust</b></p> <p>SGX IPO USD 5.5 bn</p> <p>Joint POWL Arranger Co-lead Manager</p> <p>Mar 2011</p>	 <p><b>Elpida Memory</b></p> <p>TDR Follow-on USD 145 mm</p> <p>Underwriter</p> <p>Feb 2011</p>	 <p><b>China 33 Media</b></p> <p>HKEx IPO USD 37.6 mm</p> <p>Sole Sponsor</p> <p>Feb 2011</p>	 <p><b>China Metal Resources</b></p> <p>Follow-on USD 37 mm</p> <p>Sole Placing Agent</p> <p>Dec 2010</p>	 <p><b>Sabana REIT</b></p> <p>SGX IPO USD 505 mm</p> <p>Joint GC Issue Manager</p> <p>Nov 2010</p>
 <p><b>AIA</b></p> <p>HKEx IPO USD 20.5 bn</p> <p>Joint POWL Arranger</p> <p>Oct 2010</p>	 <p><b>Sihuan Pharmaceutical</b></p> <p>HKEx IPO USD 853 mm</p> <p>Joint Lead Manager</p> <p>Oct 2010</p>	 <p><b>Strides Arcolab</b></p> <p>QIP Offering USD 100 mm</p> <p>Joint Bookrunner</p> <p>Sep 2010</p>	 <p><b>Sanjiang Fine Chemicals</b></p> <p>HKEx IPO USD 116 mm</p> <p>Joint Bookrunner Joint Sponsor</p> <p>Sep 2010</p>	 <p><b>Agricultural Bank</b></p> <p>HKEx IPO USD 22.1 bn</p> <p>Joint POWL Arranger Co-lead Manager</p> <p>Jul 2010</p>	 <p><b>Ess Dee Aluminium</b></p> <p>QIP Offering USD 20 mm</p> <p>Joint Bookrunner Joint Lead Manager</p> <p>Jul 2010</p>	 <p><b>International Taifeng</b></p> <p>HKEx IPO USD 74 mm</p> <p>Sole GC Joint Bookrunner</p> <p>Jun 2010</p>

# **Project for Capacity Building of Capital Market in Mongolia: IPO & Dual Listing Seminar Privatizing SOCs - Lessons from Japanese Experiences**

---

June 23, 2015

Daiwa Institute of Research  
Japan Economic Research Institute

## **Contents**

---

➤ What is Privatization	p.3
➤ Strategic Framework	p.6
➤ Privatization in Japan	p.9
- Case Study (Telecom): NTT	p.12
- Case Study (Railway): JR	p.15
- Case Study (Tobacco) : JT	p.20
- Case Study (Electricity): Electric Power Companies	p.23
➤ Implications for the Privatization in Mongolia	p.24

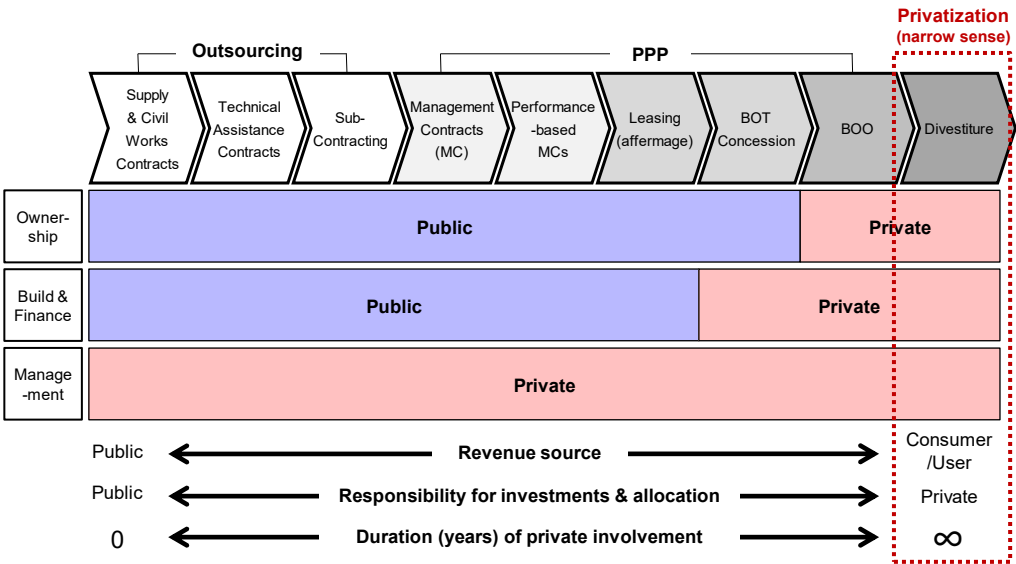
# Privatization: Definition (1)

- Process of **transferring ownership** of a business, enterprise, agency, public service, or public property from the public to the private sector
- Choice of method is influenced by the **depth of capital markets, political & company-specific factors**



3

# Privatization: Definition (2)



4

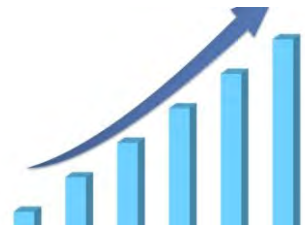


# Why Privatize?

- Burden of loss making SOEs on gov't budget.  
(SOCs' losses against GDP in '70s)
  - ✓ Average **4.0%** developing countries<sup>(\*)</sup>
  - ✓ Average **1.8%** advanced countries<sup>(\*)</sup>
  - ✓ Mongolia?



- Benefits (Most cases had shown better results)
  - ✓ **Productivity** increase
  - ✓ Faster **growth**
  - ✓ Greater **cost savings**
  - ✓ Enhance domestic **capital markets**



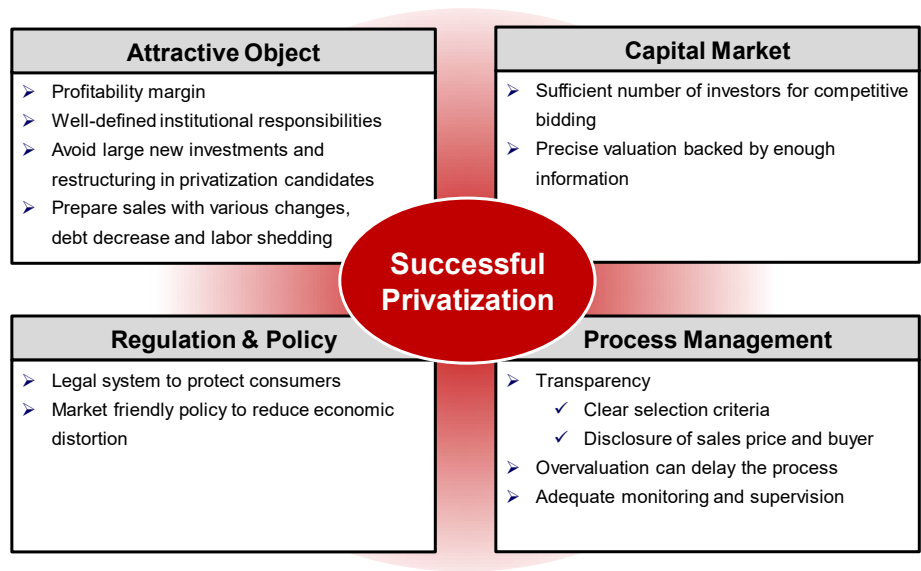
(\*) Source: R.P. Short, *The Role of Public Enterprises: A statistical Comparison*

# Strategic Framework

Setting Policy Target	Analyzing Strategic Key Factors	Choosing Method
<ul style="list-style-type: none"> <li>● <b>Government's budget reconstruction</b> <ul style="list-style-type: none"> <li>✓ Realize capital gain</li> <li>✓ Securement of tax revenue</li> <li>✓ Reduction of government spending</li> </ul> </li> <li>● <b>Enhance service for consumer</b> <ul style="list-style-type: none"> <li>✓ Reduction of cost</li> <li>✓ Improvement of service quality</li> <li>✓ Depoliticization</li> </ul> </li> <li>● <b>Flourish domestic industry</b> <ul style="list-style-type: none"> <li>✓ Creation of business opportunity</li> <li>✓ Enhancement of competitiveness</li> <li>✓ Developing capital market</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>● <b>Ownership</b> <ul style="list-style-type: none"> <li>✓ Pursuing economical efficiency</li> <li>✓ Improvement of governance</li> <li>✓ Liberation of legal restriction</li> </ul> </li> <li>● <b>Management know-how</b> <ul style="list-style-type: none"> <li>✓ Improve efficiency</li> <li>✓ Benefit by creating demand</li> <li>✓ Enhance convenience</li> </ul> </li> <li>● <b>Finance</b> <ul style="list-style-type: none"> <li>✓ Contribute to government's budget</li> <li>✓ Non-budget system</li> <li>✓ Disciplined control</li> </ul> </li> <li>● <b>Market mechanism</b> <ul style="list-style-type: none"> <li>✓ Improving efficiency</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>● <b>Ownership transfer</b> <ul style="list-style-type: none"> <li>✓ IPO</li> <li>✓ Trade sale</li> <li>✓ MBO</li> </ul> </li> <li>● <b>PPP</b> <ul style="list-style-type: none"> <li>✓ PFI</li> <li>✓ Concession</li> <li>✓ BOT / BOO</li> <li>✓ Outsourcing</li> </ul> </li> <li>● <b>Market liberation</b> <ul style="list-style-type: none"> <li>✓ Bidding</li> <li>✓ Deregulation</li> </ul> </li> </ul>

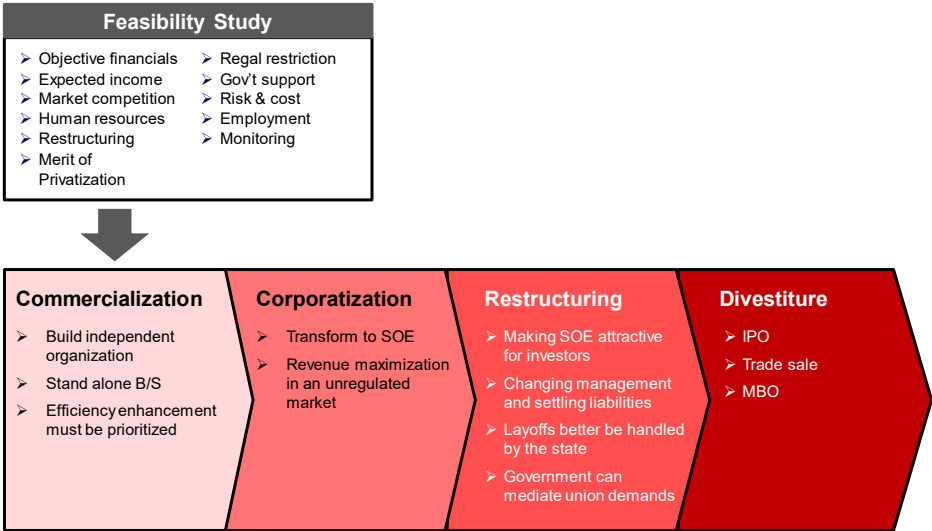
Source: Yumiko NODA, *Strategy and Methods of Privatization* 2004

## Keys for Success



7

## Four Steps of Privatization



8





## Privatization in Japan: Summary

- Japanese gov't promoted privatization w/strong leadership in 80's, to address;
  - **Fiscal deterioration**,
  - **Slowdown in economy**, and
  - Pressure from outside for **deregulation**.
- As a result of the privatization;
  - **Fiscal position has improved**,
  - **Market discipline** has been introduced,
  - **Corporate governance** has been improved, and
  - Domestic **capital markets** has grown.
- Privatized companies have become **global players** w/own growth strategies.



9

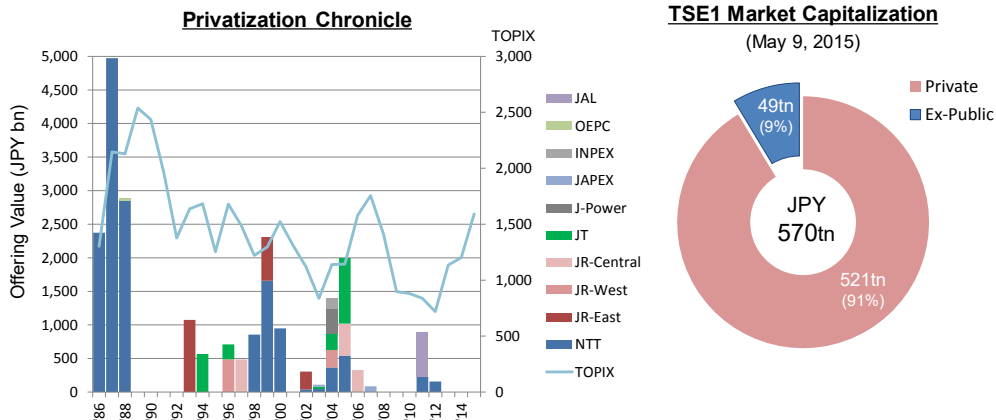
## Privatization Cases in Japan

* Simple sum of the numbers for the group companies				
(As of March 31, 2014) Consolidated				
Establishment / Listed	1985/1985	East:1987/1992 West&Central:1987/1993	1985/1994	1951/1951
Paid-In Capital (JPY bn)	938	East: 200 Group total*: 460	100	1,400
Total Revenue (JPY bn)	10,925	East: 2,704 Group total*: 6,432	2,400	6,631
Ownership (Voting rights base) (red= public sector)	MOF: 35.65% Employee: 0.81%	Privatized 3 companies Private: 100.00%  Other 4 companies JRTT: 100.00%	MOF: 33.35%	NDF*: 50.10% Employee: 1.46% Tokyo Metropolis: 1.35%
* Nuclear Damage Compensation and Decommissioning Facilitation Corporation				

10

## Privatization & Capital Markets

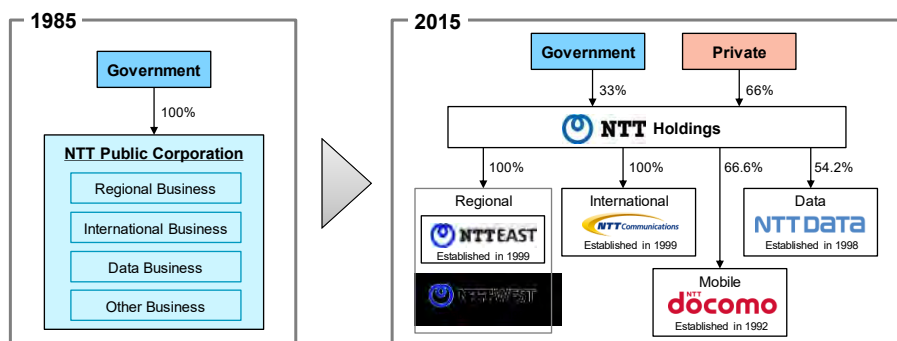
- Privatization in Japan has accelerated in **80's**.
- **NTT** has been the largest privatization, bringing a number of retail investors into the capital market
- Privatized companies currently occupy **9%** of the total market cap in TSE1.



11

## Case Study (Telecom): NTT (1)

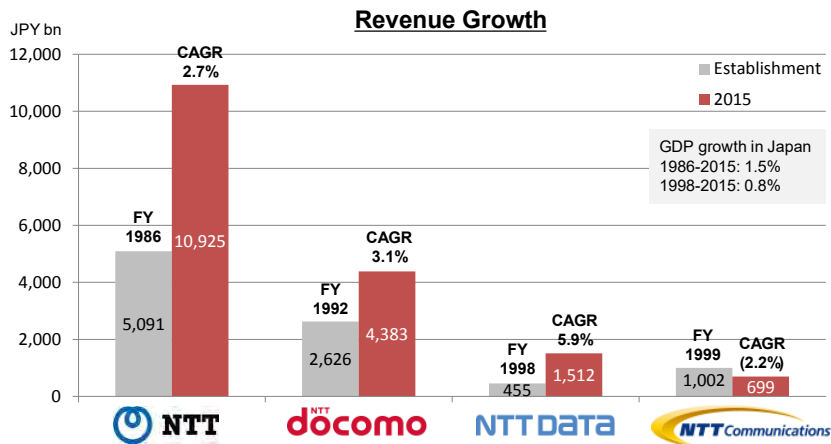
- Why privatized?
  - To **enhance efficiency** by ensuring management independence
  - To **introduce competition** through liberalizing telecom market
- Since the listing in **1987**, gov't gradually sold its holdings until **2005** for **JPY14tn**.
- Gov't still has to hold over **1/3** of total outstanding, and foreign ownership is restricted to **1/3**.



12

## Case Study (Telecom): NTT (2)

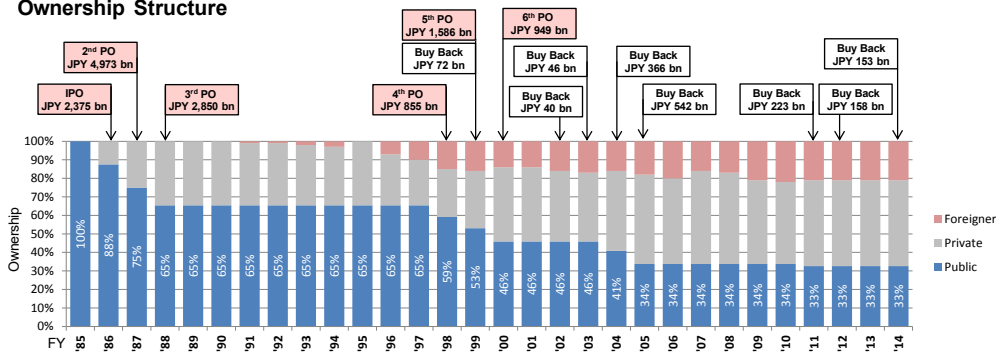
- NTT group has **faster grown than GDP** in Japan after privatization.
- Only NTT Communications (for long-distance & international communications) has gone through revenue decline since its establishment, due to worldwide shrink of the market.



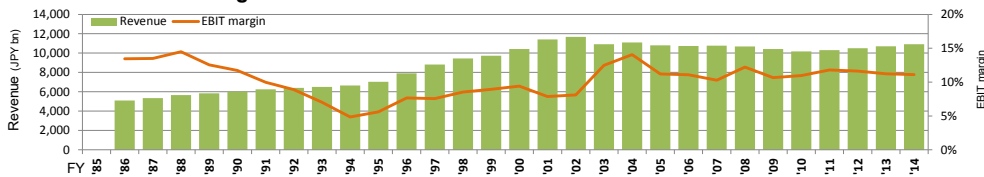
13

## Case Study (Telecom): NTT (3)

### Ownership Structure



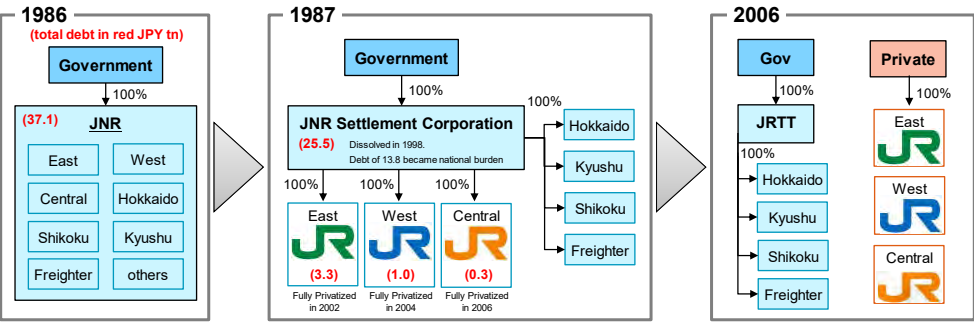
### Revenue & EBIT Margin



14

## Case Study (Railway): JR

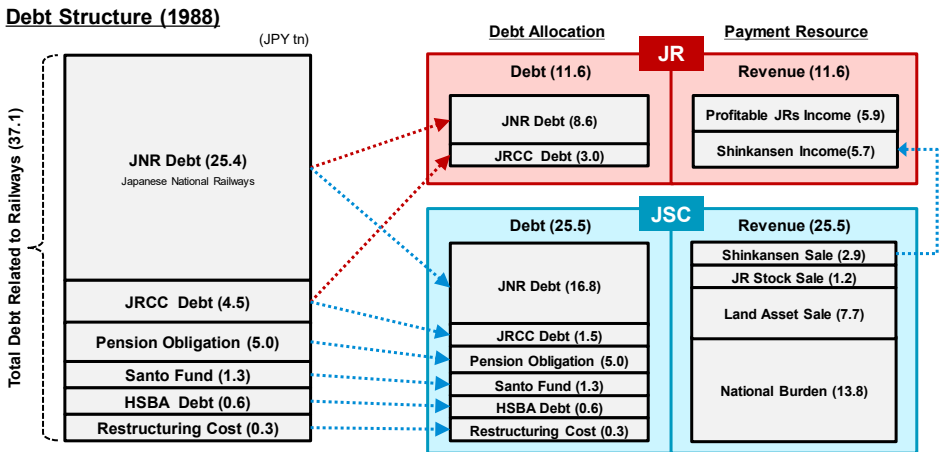
- Why privatized?
  - To reduce huge debt of **JPY 37.1tn** of **Japanese National Railways (JNR)**
  - To optimize management policy suitable for each region
- JNR was divided into **6 regional companies & a freight company**, of which 3 profitable companies were listed, whose shares were sold for **JPY 4.0tn**.
- Privatization effort has **overcome extremely strong union** and the business operation was successfully improved with a reduction of over **30%** of employees.



15

## Case Study (Railway): JNR Settlement Corporation (JSC)

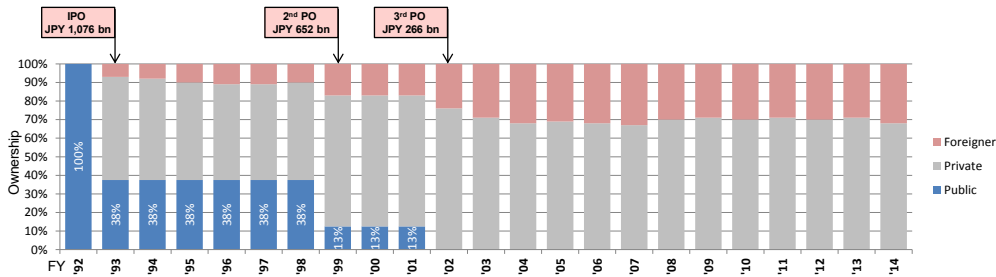
- **JSC** was established for restructuring B/S of JNR.
- Only 4 profitable JR companies took over the debt related to their assets, and JSC succeeded the rest of all the debt.



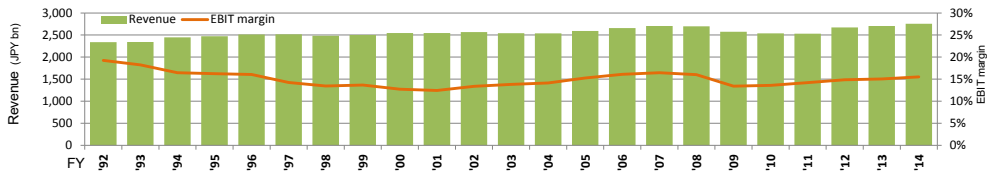
16

## Case Study (Railway): JR East

### Ownership Structure



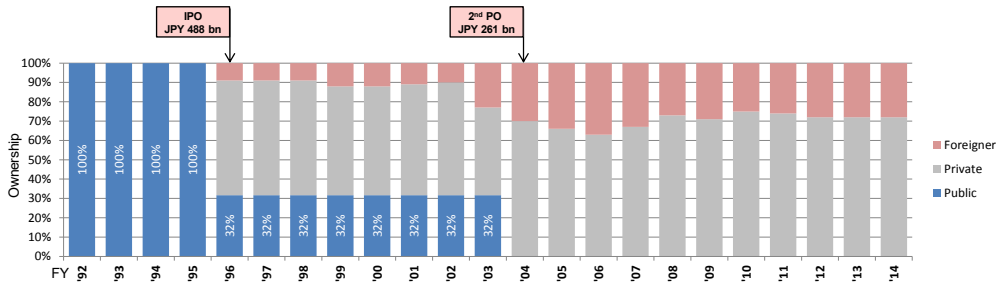
### Revenue & EBIT Margin



17

## Case Study (Railway): JR West

### Ownership Structure



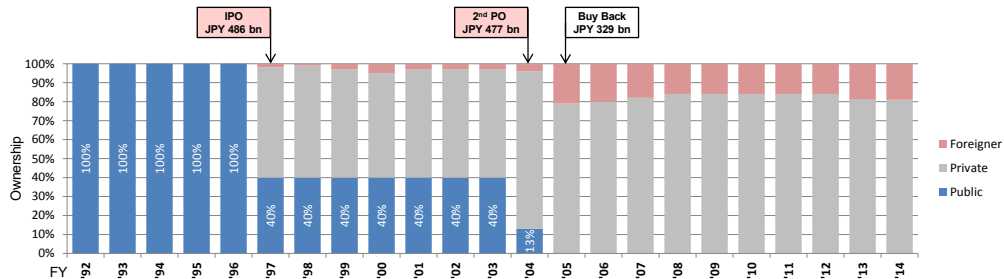
### Revenue & EBIT Margin



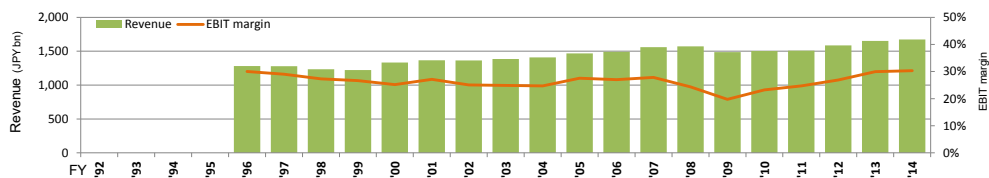
18

## Case Study (Railway): JR Central

### Ownership Structure



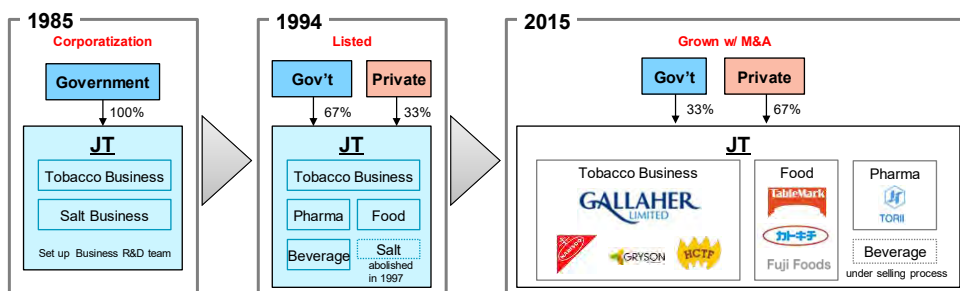
### Revenue & EBIT Margin



19

## Case Study (Tobacco) : JT (1)

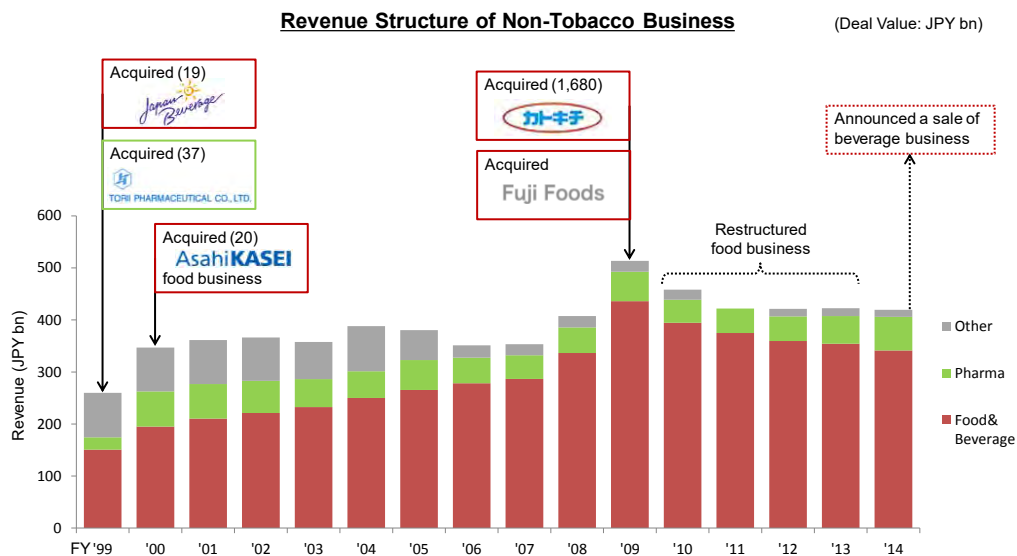
- Why privatized?
  - **Pressure from outside** to deregulate & open the tobacco market
  - To **enhance efficiency** by allowing independent management
  - To **reduce gov't debt** and to finance for reconstruction after the earthquake in 2011
- Listed in **1985**, and the gov't gradually sold its shares for **JPY1.0tn**.
- Gov't still has to hold over **1/3** of total outstanding, due to its obligation to purchase all domestic tobacco leaves.
- JT has **expanded business scope** & became global player w/own growth strategy.



20

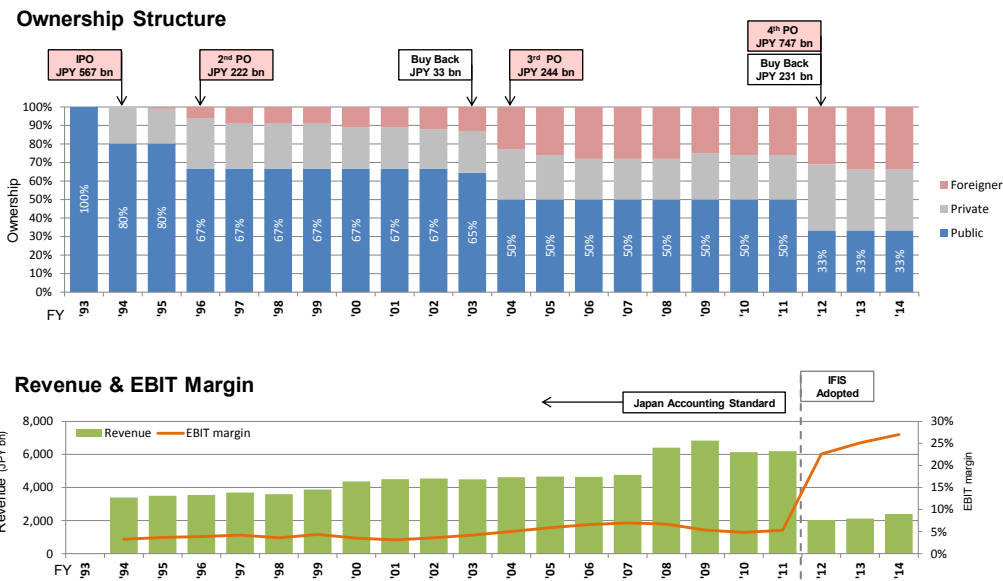


## Case Study (Tobacco) : JT (2)



21

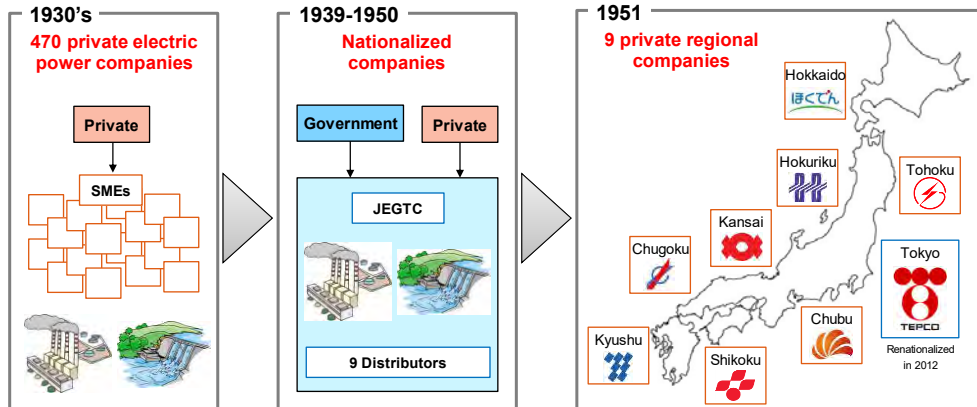
## Case Study (Tobacco) : JT (3)



22



## Case Study (Electricity): Electric Power Companies

- There were many private electric power companies before WWII.
- During the war, gov't forced to merge them into **Japan Electric Generation & Transmission Co. (JEGTC)** and **9 distributors** under **National General Mobilization Act**.
- GHQ divided JEGTC into 9 regional companies in **1951**, while TEPCO was **renationalized** in **2012** due to the nuclear accident caused by the earthquake.



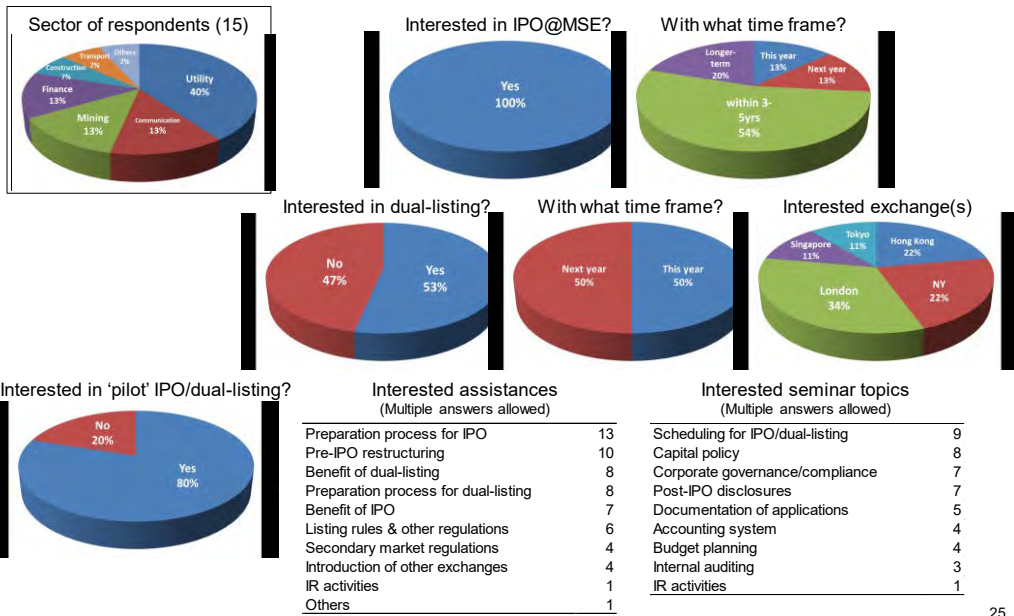
23

## Implications for the Privatization in Mongolia

		
<b>Objective</b>	<ol style="list-style-type: none"> <li>1. Reducing fiscal deficit</li> <li>2. Improving efficiency</li> <li>3. Promoting deregulation</li> </ol>	<ol style="list-style-type: none"> <li>1. } Same as Japan</li> <li>2. }</li> <li>3. }</li> <li>4. Developing capital markets</li> </ol>
<b>Sector</b>	<ul style="list-style-type: none"> <li>✓ Telecom</li> <li>✓ Railway</li> <li>✓ Tobacco</li> <li>✓ Electricity</li> <li>✓ Airline</li> <li>✓ Petroleum</li> </ul>	<ul style="list-style-type: none"> <li>✓ Telecom</li> <li>✓ Electricity</li> <li>✓ Post</li> <li>✓ Mining</li> <li>✓ Airline</li> <li>✓ Exchanges</li> </ul>
<b>Main Consideration</b>	<ul style="list-style-type: none"> <li>✓ Strengthening core business</li> <li>✓ Minimizing capital market impacts</li> <li>✓ Gradual decrease of gov't ownership</li> <li>✓ Dividing operations by region or function</li> </ul>	<ul style="list-style-type: none"> <li>✓ Reaching; <ul style="list-style-type: none"> <li>- Strategic investors</li> <li>- Retail investors</li> <li>- Foreign Investors <ul style="list-style-type: none"> <li>• At MSE</li> <li>• At overseas exchanges</li> </ul> </li> </ul> </li> </ul>

24

## SOCs' Reply to the Questionnaire (Mar 31, 2015)



# Opportunities for Mongolian Companies to IPO in Japan

---

**June 23, 2015**



New Listings, Tokyo Stock Exchange, Inc.

# Tokyo Stock Exchange at a Glance

**No. 1** in Asia By Market Capitalization

**51%** by **IT** industry in 2014 IPOs<sup>1</sup>

**50.9 X** Median of **PE Ratio** of 2014 IPOs<sup>1,2</sup>

Note: 1 The number excludes Tokyo Pro Market and REITs.

2 PE Ratio = Market capitalization based on first price / Net profit (last fiscal year).



## 1. Japan-Mongolia Relations

2. Comparison among Major Stock Markets

3. Expansion of IPO Market in Japan

4. Features of IPO Market in Japan

5. Listing on Tokyo Stock Exchange

A. TOKYO PRO Market

B. Overview of the Japanese Financial Market

# Japan-Mongolia Summit Meeting, Signing Ceremony for an Economic Partnership on February 10, 2015

## 1. Japan-Mongolia summit meeting

On February 10, Prime Minister Shinzo Abe held a summit meeting with Mr. Chimed Saikhanbileg, Prime Minister of Mongolia.

### a. Economic areas

The two leaders both celebrated that the Japan-Mongolia EPA had reached the signing stage on this day at the end of negotiations for approximately three years, and confirmed their resolve to take the necessary respective domestic legal procedures in order to bring the EPA into force as quickly as possible.

Prime Minister Abe stated that Japan will continue to support Mongolia's formulation of medium- to long-term economic policy, through measures including dispatching economic advisors, and explained that Japan will provide an additional yen loan of 36.85 billion yen for a new international airport that is currently under construction based by a yen loan.

Prime Minister Saikhanbileg expressed appreciation for this support from Japan, and stated that with the conclusion of the EPA as an opportunity, he wants to further vitalize bilateral cooperation in economic areas, and deepen cooperation between the two countries in economic areas regionally and in the international arena.

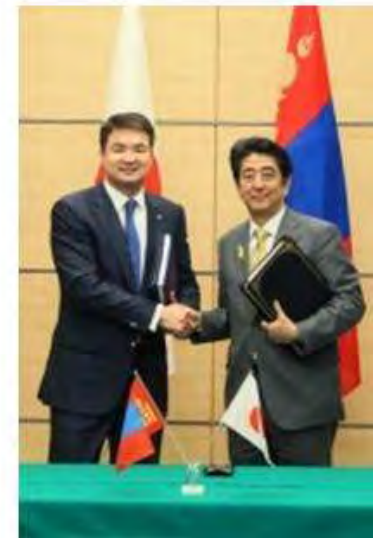
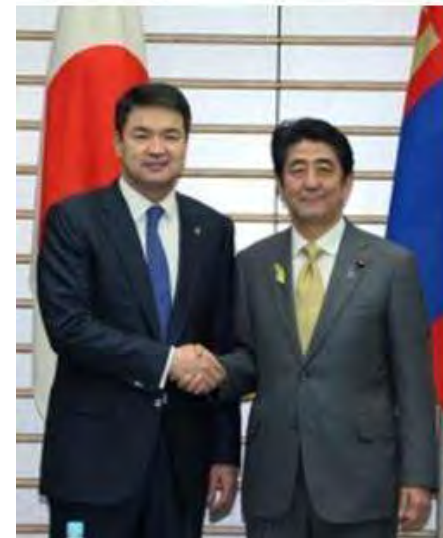
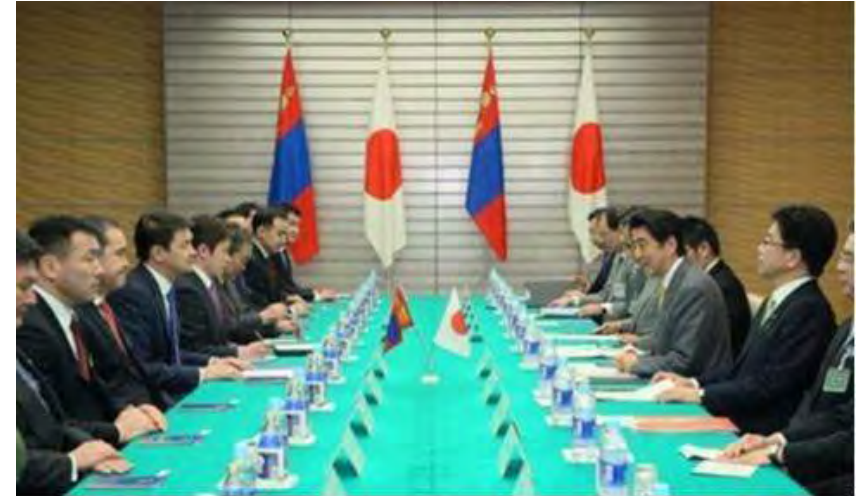
### b. Politics and security

Prime Minister Abe said that based on the policy of Proactive Contribution to Peace, Japan will make a greater contribution to the peace and development of Asia and the world. The two leaders shared the view that the two countries will continue to cooperate closely, both regionally and in the international arena.

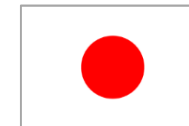
The two leaders also exchanged views on regional affairs in East Asia, including North Korea.

## 2. Signing ceremony and dinner hosted by the Prime Minister

a signing ceremony was held for the Japan-Mongolia EPA, the Implementing Agreement for the EPA, and the "Joint Statement on the Signing of the Agreement between Japan and Mongolia for an Economic Partnership."



# Japan-Mongolia Relations

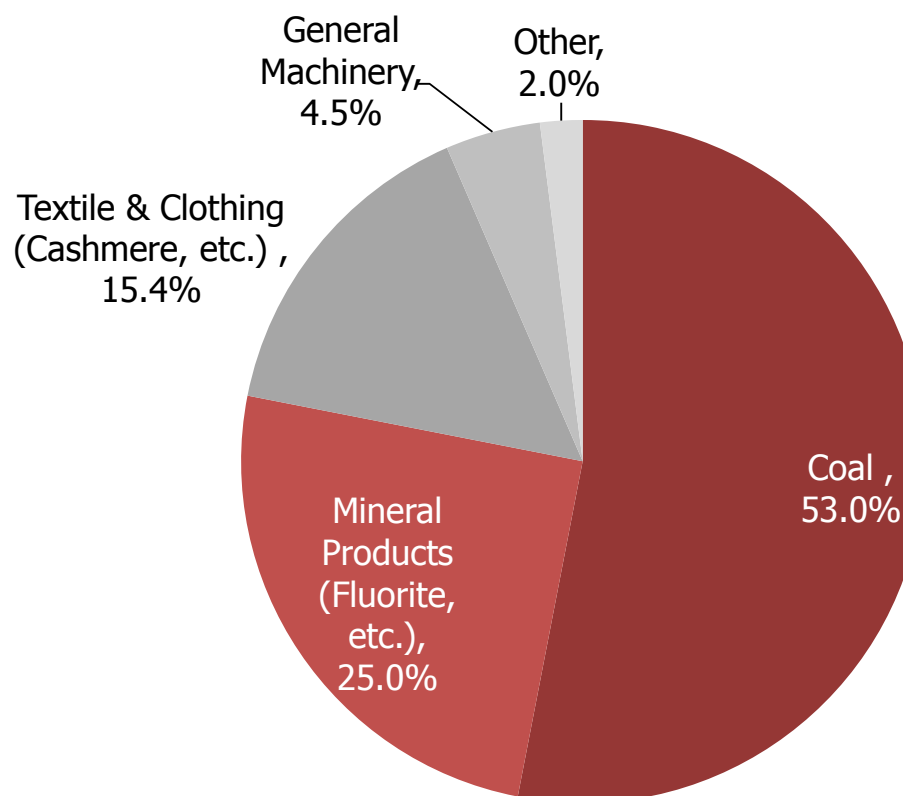


## Recent Political Ties

- 2010: Building a Strategic Partnership
- 2012: New level of expanded commercial relations
- 2013: Developing a Strategic Partnership
  - Prime Minister Abe's visit to Mongolia in March 2013. The two countries shared the intention to enhance mutual relations based on the following three pillars.
  - Prime Minister Altankhuyag's visit to Japan in September 2013. The two countries issued "Joint Statement" and "Mid-term Action Plan", which would become a basis for the two countries to elevate their "strategic partnership" to even higher levels and further strengthen their mutually beneficial and complementary relationship.

- Japan-Mongolia trade: US\$ 311 million
  - Mongolia to Japan: US\$ 18 million
  - Japan to Mongolia: US\$ 293 million

## Mongolia to Japan: US\$ 18 million



Source: Ministry of Foreign Affairs of Japan



# Development Bank of Mongolia Issued Samurai Bonds of JPY 30 billion Guaranteed by JBIC

**JBIC provided this guarantee under the Guarantee and Acquisition toward Tokyo market Enhancement (GATE) facility as the result of exchanging views and information with DBM based on the Mid-term Action Plan agreed on between the top leaders of both countries in Sep. 2013.**

**This was the first JBIC guarantee for issue of Samurai bonds by a Mongolian institution. By supporting the launching of Samurai bonds issued by DBM, JBIC helped diversify funding sources for DBM and the Government of Mongolia.**

**This guarantee provision was expected to strengthen bilateral relations and contribute to more vigorous Japanese business activities in a wide range of areas.**

## Summary of Samurai Bond Issuance

Issuer	Development Bank of Mongolia (DBM)
Date of Payment	6-Jan-2014
<b>Maturity</b>	<b>10 years</b>
<b>Coupon</b>	<b>1.52%</b>
Currency	Japanese Yen (JPY)
Issuance	Privately Placed Issue
<b>Amount</b>	<b>JPY 30 billion (approx. US\$ 300 million)</b>
Guarantee Fee (One-time Fee)	JPY 5.7 billion (approx. US\$ 57 million)
Guarantor <sup>1</sup>	Japan Bank for International Cooperation (JBIC)
Joint Lead Arrangers	Nomura Securities Co., Ltd. Daiwa Securities Co., Ltd.
Bond Administrator	Mizuho Bank, Ltd.

Source: JBIC, InfoMongolia.com

Note: JBIC's guarantee will cover the principal and part of the interest of the issue.

# Trade and Development Bank of Mongolia (TDB) Opened Tokyo Representative Office



Trade and Development Bank of Mongolia (TDB), Mongolia's financial gateway to the world, has expanded its operation and successfully opened its first international representative office in Tokyo, Japan on July 23, 2014.



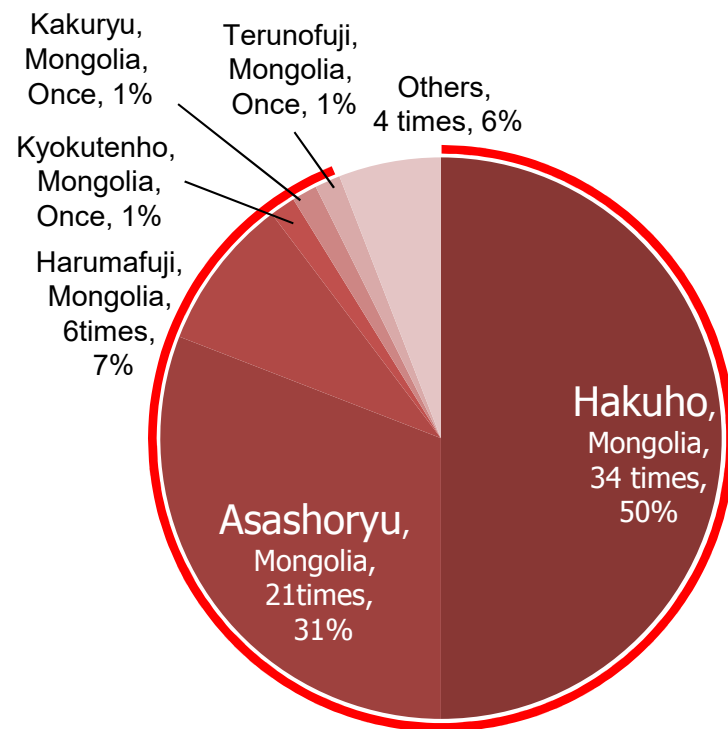
Source: Website of Trade and Development Bank of Mongolia

# Mongolian Sumo Wrestlers in Japan

**25 Mongolian wrestlers play an active roles in sumo in Japan. 3 Mongolian wrestlers are “Yokozuna”, highest rank in sumo.**

**Mongolian wrestlers occupy 64 championships of 68 tournaments since 2004.**

## Number of Championships (Jan. 2004 – Jul. 2014)



**Mongolian Wrestlers  
64 times, 94%**

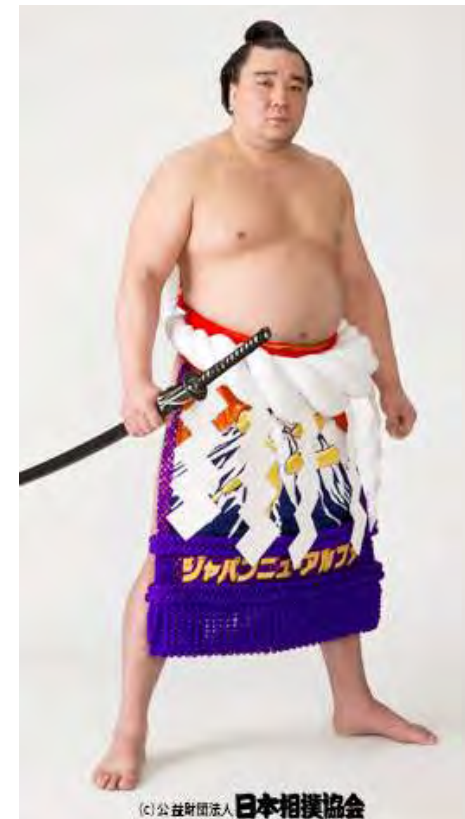
## Hakuho Shō

Yokozuna, highest rank in sumo



## Harumafuji Kōhei

Yokozuna, highest rank in sumo



## Kakuryū Rikisaburō

Yokozuna, highest rank in sumo





1. Japan-Mongolia Relations

**2. Comparison among Major Stock Markets**

3. Expansion of IPO Market in Japan

4. Features of IPO Market in Japan

5. Listing on Tokyo Stock Exchange

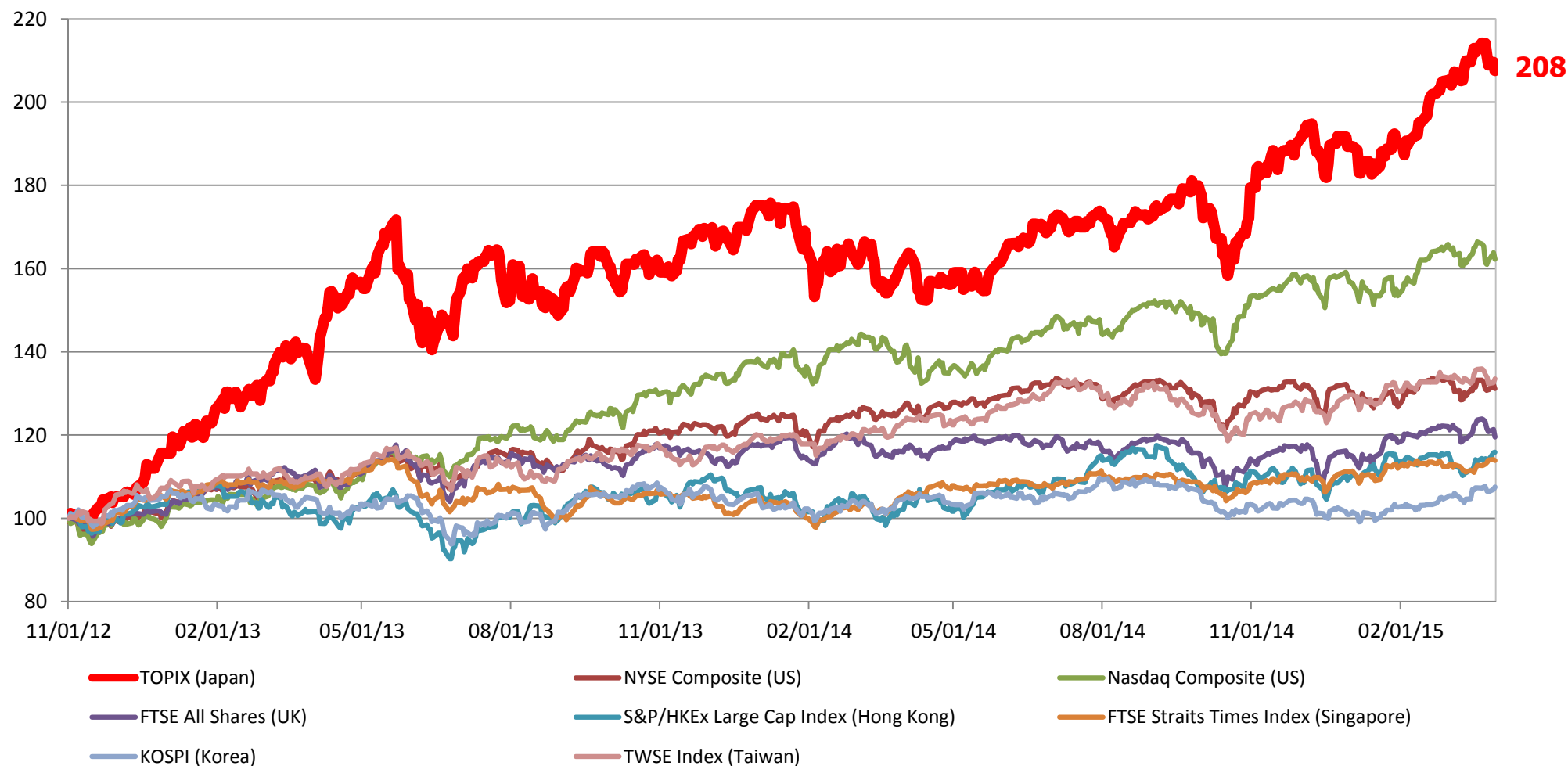
A. TOKYO PRO Market

B. Overview of the Japanese Financial Market



# Stock Market Index Performance

**TOPIX, which represents the movement of the Tokyo market overall, is recording a high growth rate as compared with other markets.**

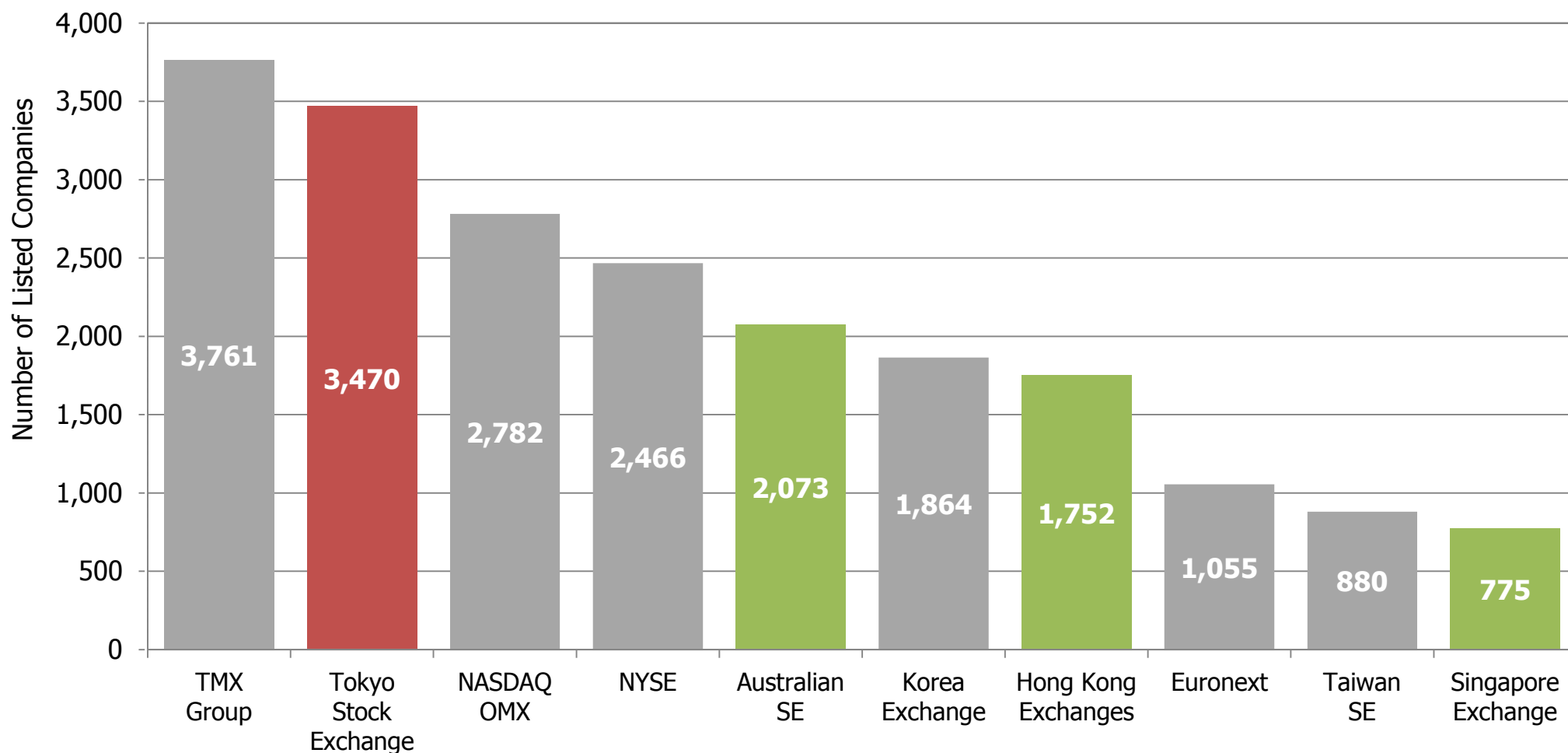


Source: Bloomberg

Note: As of March 31, 2015. Indices rebased to 100 as of November 1, 2012.

# Number of Listed Companies

**Tokyo Stock Exchange exceeds NYSE and NASDAQ in terms of number of listed companies.**

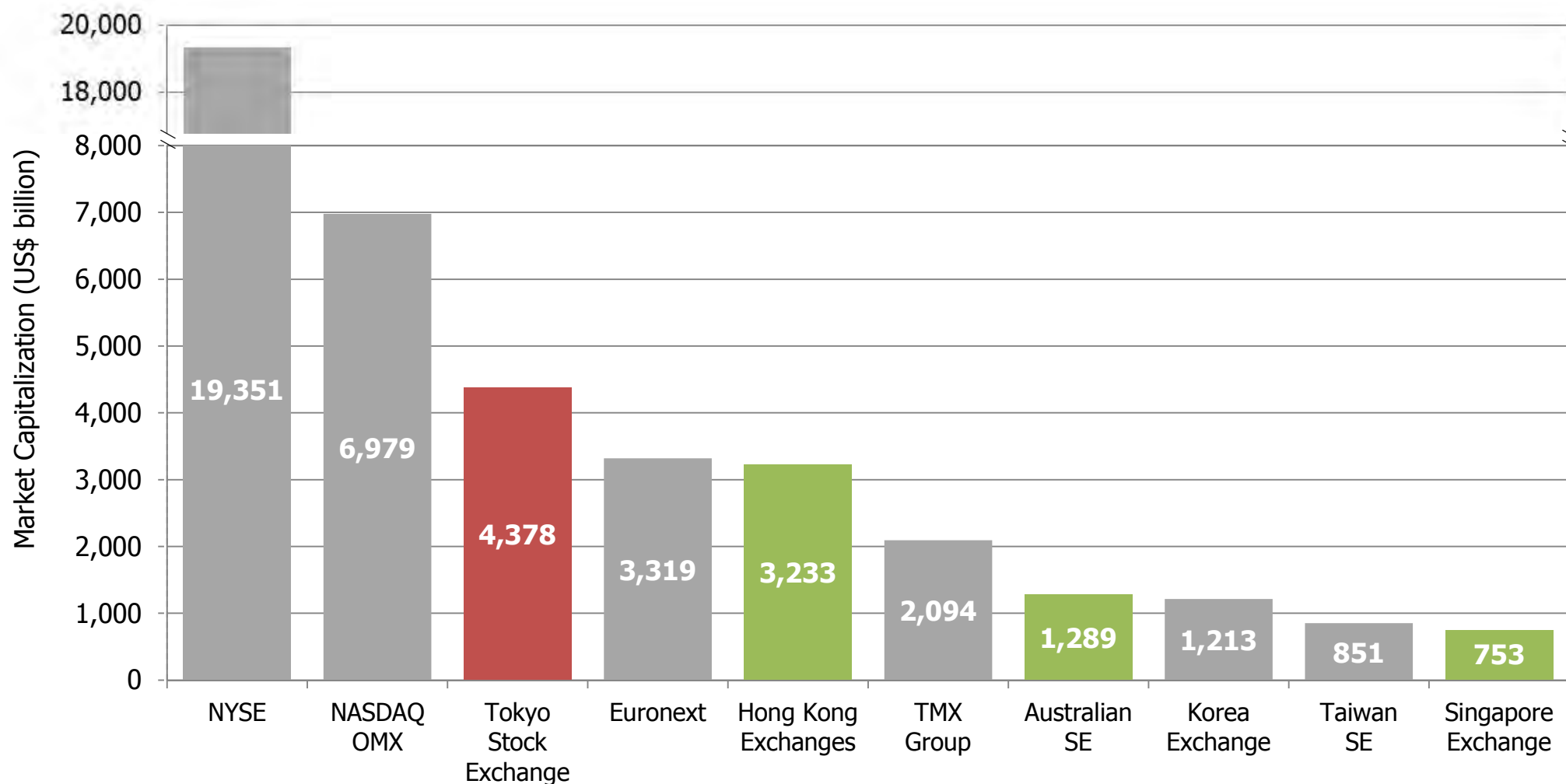


Source: WFE

Note: Number of listed companies as of the end of December 2014

# Market Capitalization

**Tokyo Stock Exchange ranks No.3 globally and No. 1 in Asia by market capitalization.**

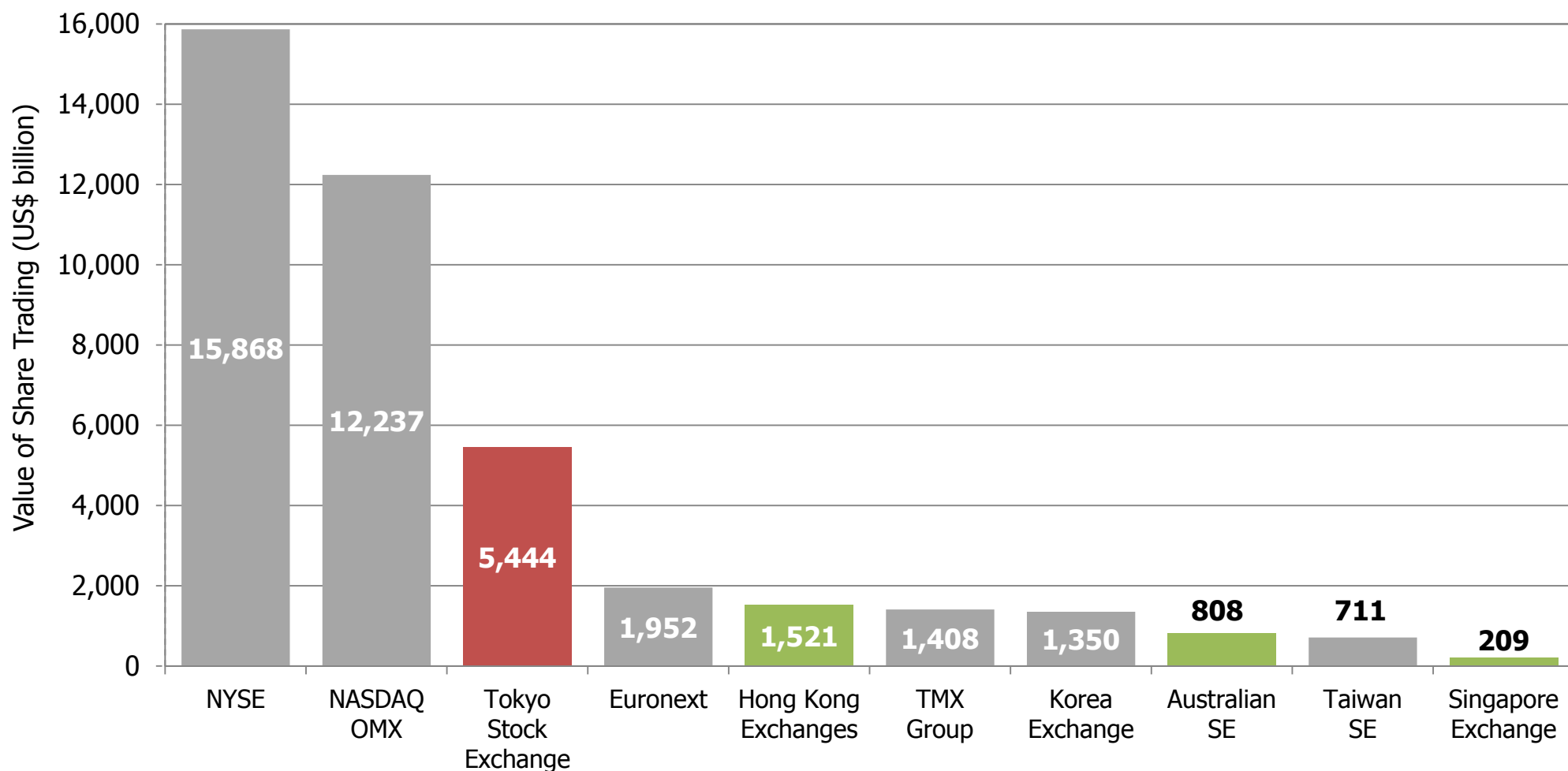


Source: WFE

Note: Domestic market capitalization as of the end of December 2014

# Value of Share Trading in the World

**Tokyo Stock Exchange is about 3.6 times larger than Hong Kong Exchanges by value of share trading.**



Source: WFE

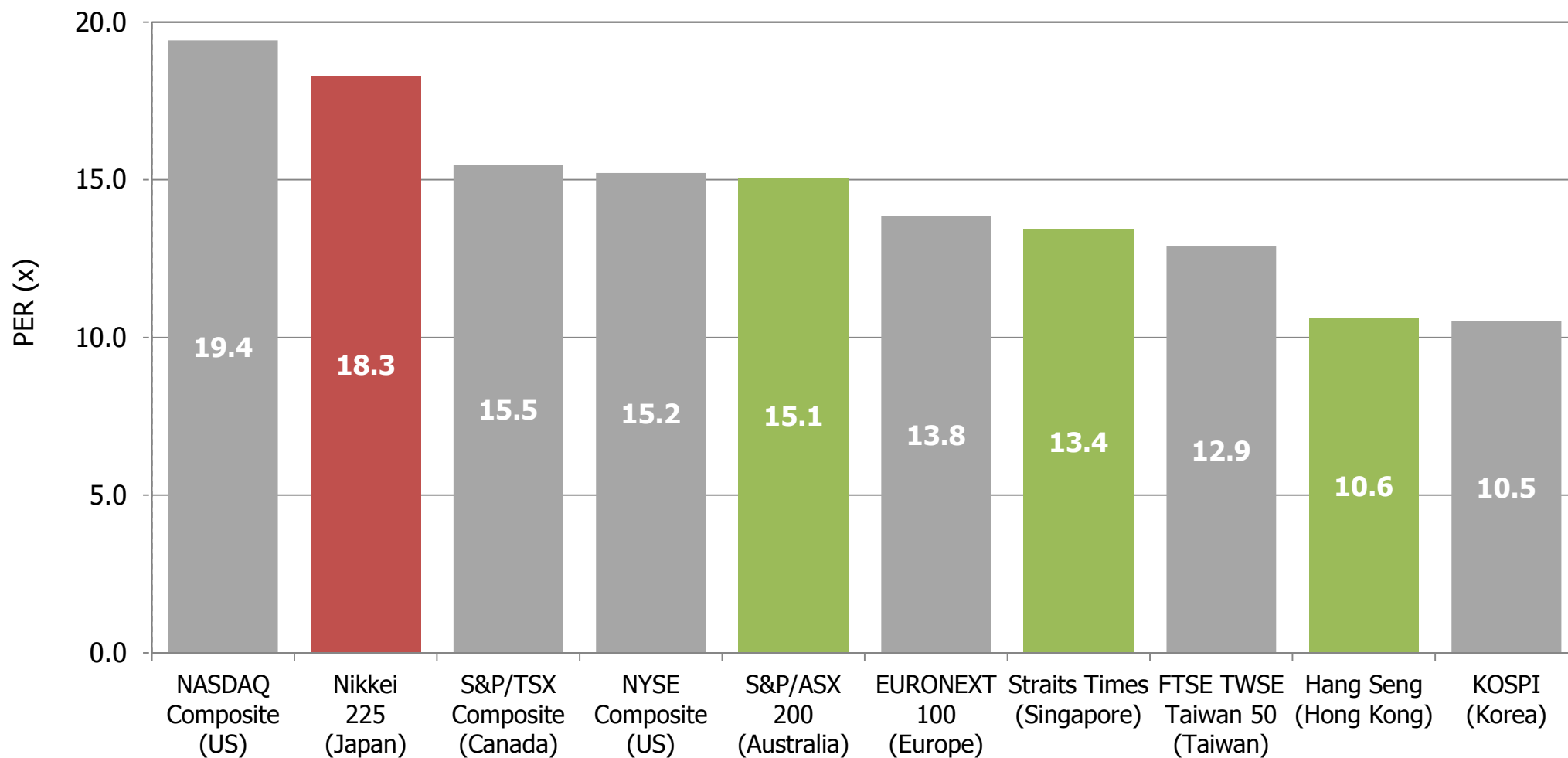
Note: Value of share trading - Electronic order book trades from January 2014 to December 2014

© 2015 Japan Exchange Group, Inc. and/or its affiliates. All rights reserved.



# Valuation: PER

**Valuations for Japanese companies are highly appreciated based on PER.**



Source: Bloomberg

Note: Based on estimated PER from Bloomberg as of January 6, 2015. PER = Price/Estimated EPS Ratio



1. Japan-Mongolia Relations

2. Comparison among Major Stock Markets

**3. Expansion of IPO Market in Japan**

4. Features of IPO Market in Japan

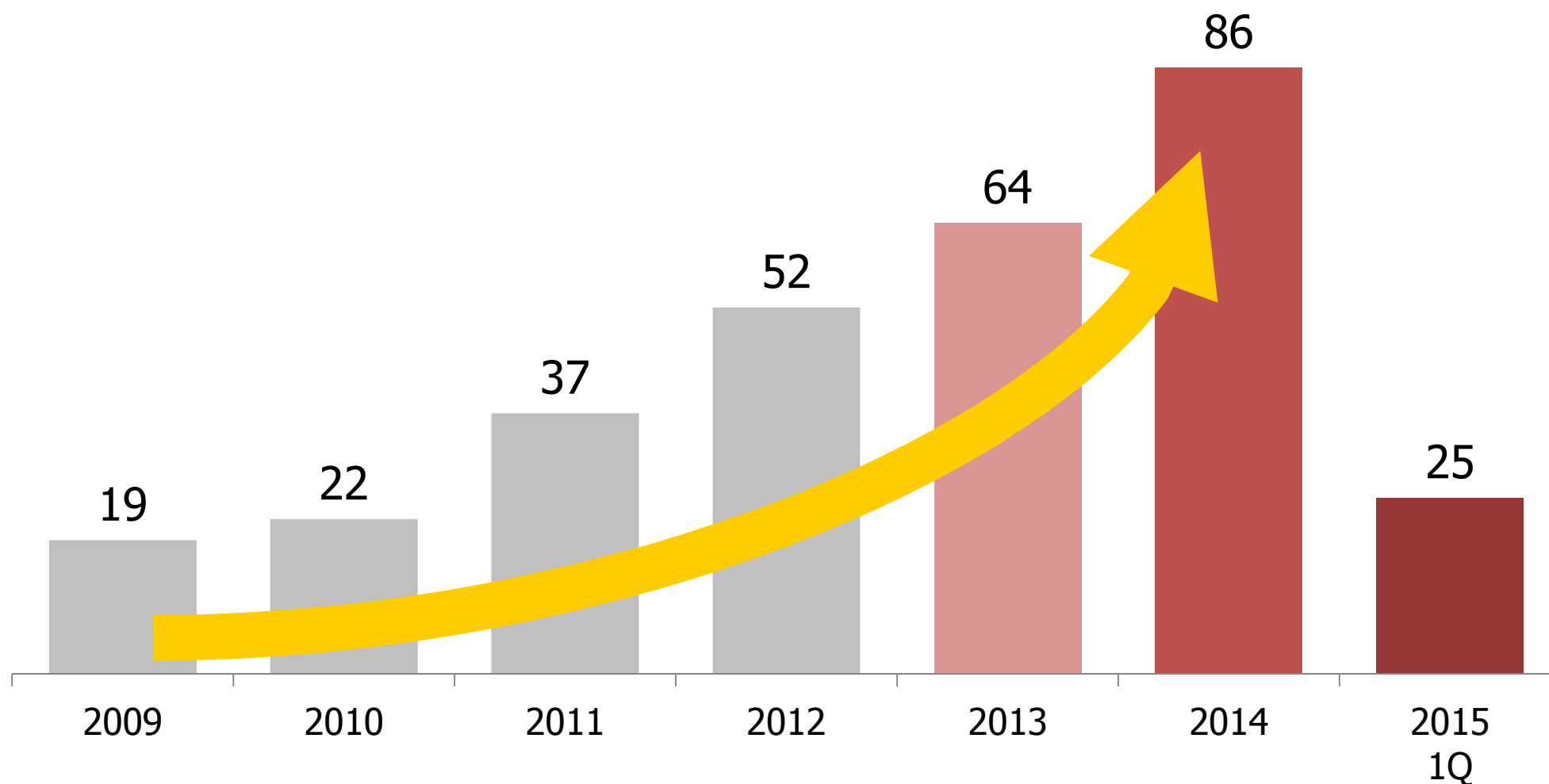
5. Listing on Tokyo Stock Exchange

A. TOKYO PRO Market

B. Overview of the Japanese Financial Market

# Number of IPOs in Japan

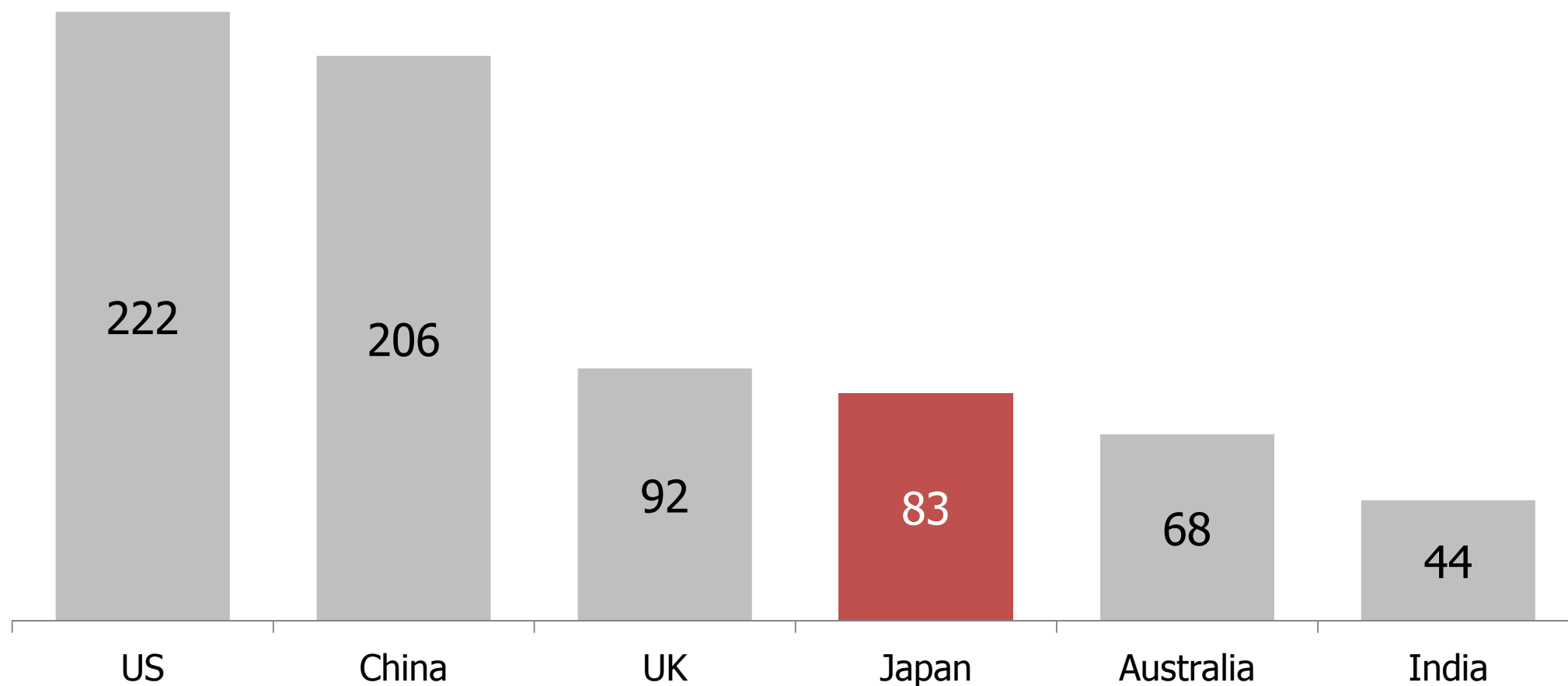
**IPOs figures showed a significant increase to 86<sup>1</sup> in 2014 from 64 in 2013, confirming a full-fledged recovery in the Japanese IPO market. The number of IPOs is expected to increase from 2014 onward.**



Note 1: The number includes Tokyo Pro Market and REITs.

# Top Six Countries by Number of IPOs in 2014

Japan ranks No.4 globally by number of IPOs in 2014.

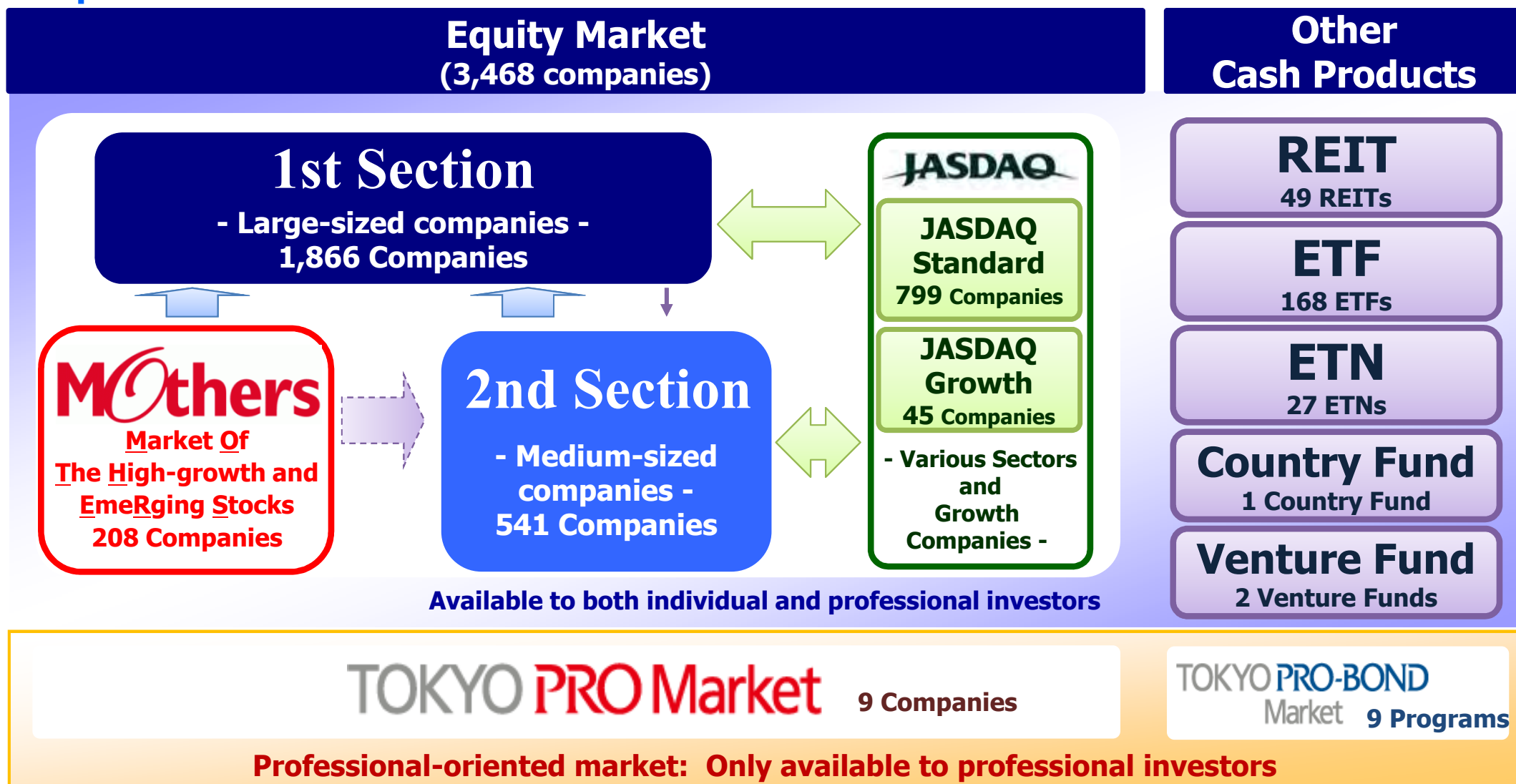


Source: EY Global Trends 2014 4Q

Note: Based on the listed company domicile nation. Number of Japan IPOs does not include TOKYO PRO Market.

# Structure of TSE Cash Equity Market

JPX offers several markets with different concepts to allow companies to make an optimal choice.



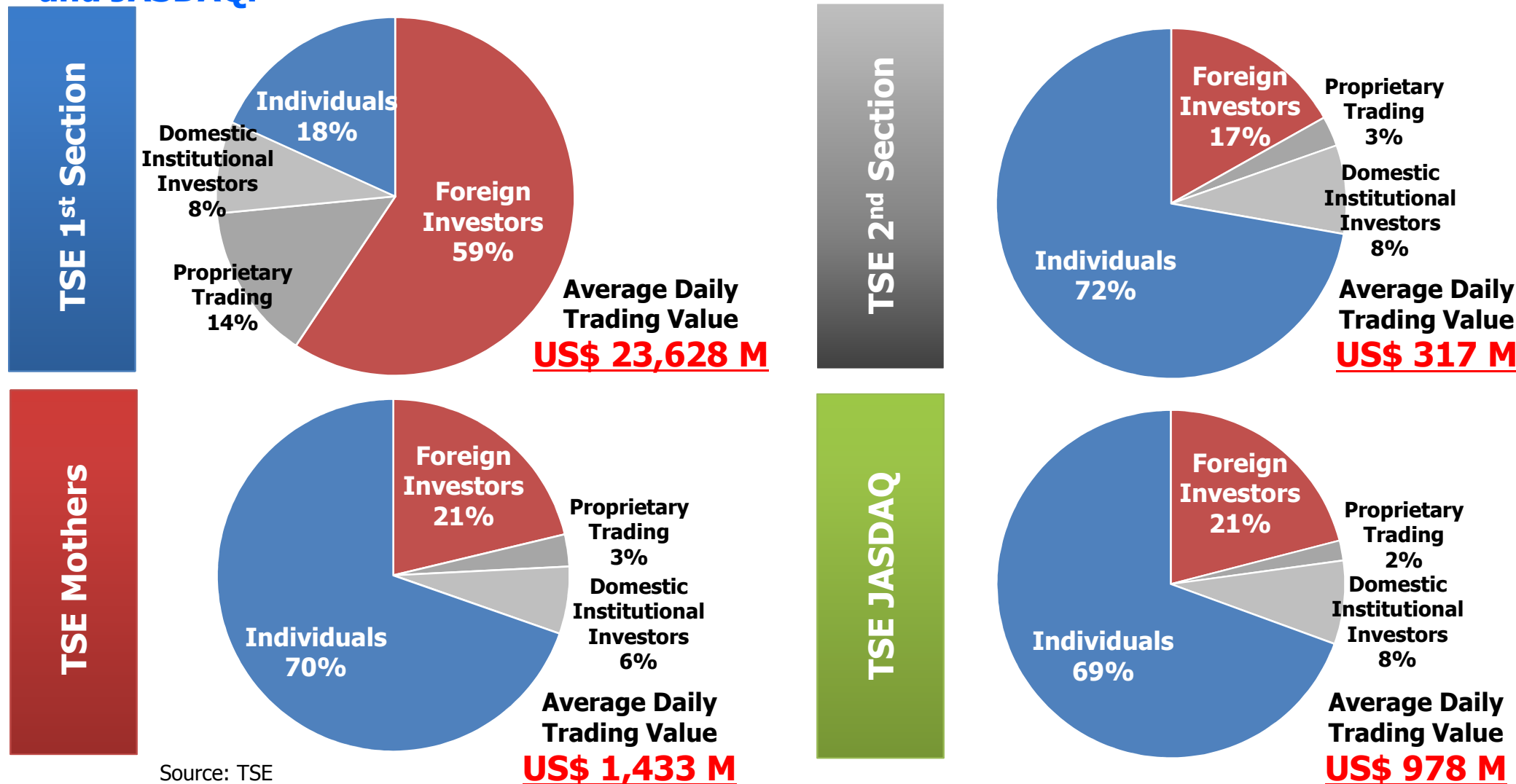
Note: As of December 31, 2014

© 2015 Japan Exchange Group, Inc. and/or its affiliates. All rights reserved.

# Stock Trading Value by Investor Category (2014)

Foreign investors account for more than half of trading in the TSE 1st Section.

By contrast, individual investors make up the majority in the TSE 2nd Section, Mothers, and JASDAQ.



Source: TSE  
Note: 1 US\$= 100 JPY

# IPO Companies Size (2010-2014)

<div>Max</div> <div><b>Median</b></div> <div>Min</div>	Revenue	Net Profit	Net Asset	Market Cap (First Price)	Actual PER (First Price)	IPO Amount <sup>2</sup>
<b>TSE 1st</b>	US\$ 52,253M <b>US\$ 1,637M</b> US\$ 112M	1,866M <b>US\$ 41M</b> US\$ -1.8M	9,485M <b>US\$ 704M</b> US\$ -35M	US\$ 18,197M <b>US\$ 958M</b> US\$ 297M	214.6x <b>16.5x</b> 3.7x	US\$ 10,089M <b>US\$ 425M</b> US\$ 67M
<b>TSE 2nd</b>	US\$ 854M <b>US\$ 197M</b> US\$ 41M	US\$ 19M <b>US\$ 6.3M</b> US\$ -1.0M	US\$ 130M <b>US\$ 50M</b> US\$ 13M	US\$ 183M <b>US\$ 64M</b> US\$ 34M	130.8x <b>11.8x</b> 5.6x	US\$ 455M <b>US\$ 69M</b> US\$ 34M
<b>Mothers</b>	US\$ 283M <b>US\$ 18M</b> US\$ 0.5M	US\$ 26M <b>US\$ 1.9M</b> US\$ -11M	US\$ 177M <b>US\$ 6.1M</b> US\$ -0.8M	US\$ 1,018M <b>US\$ 108M</b> US\$ 23M	10,210x <b>63.8x</b> 9.6x	US\$ 190M <b>US\$ 11M</b> US\$ 1.7M
<b>JASDAQ</b>	US\$ 1,173M <b>US\$ 69M</b> US\$ 0.6M	US\$ 29M <b>US\$ 4.0M</b> US\$ -13M	US\$ 91M <b>US\$ 17M</b> US\$ 1.6M	US\$ 1,478M <b>US\$ 41M</b> US\$ 9.6M	71.4x <b>15.0x</b> 2.8x	US\$ 74M <b>US\$ 7.9M</b> US\$ 3.6M

Source: TSE

Note:

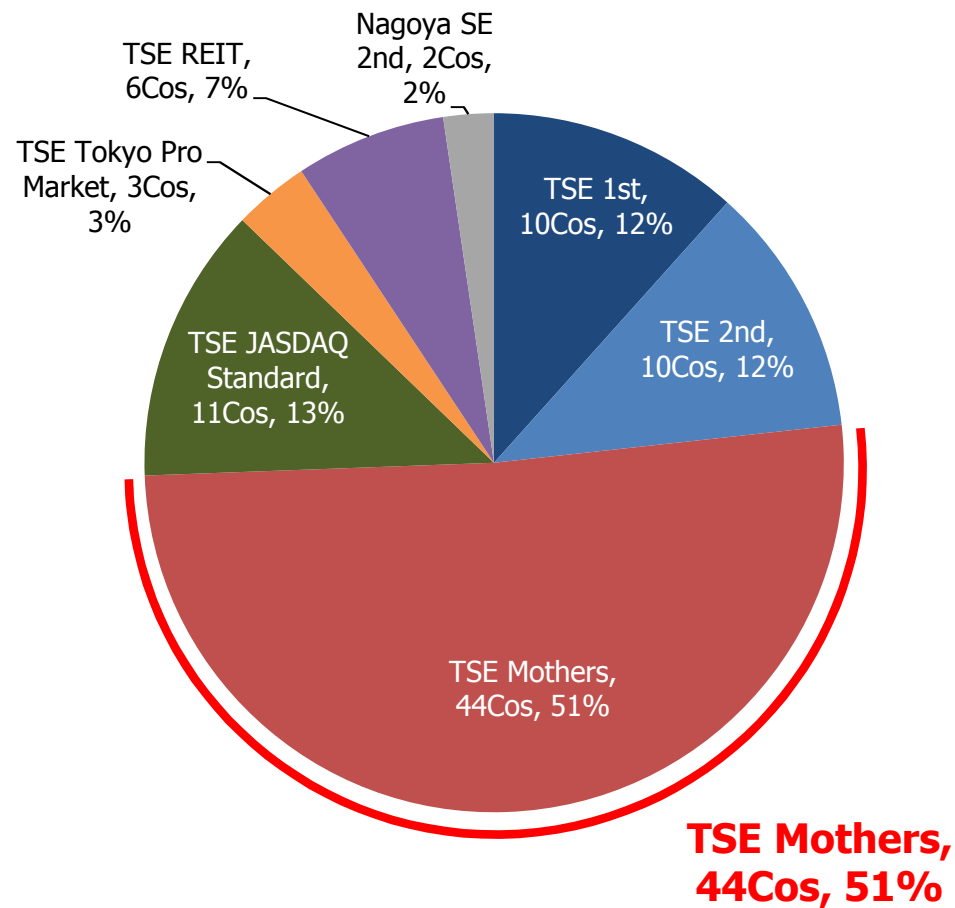
1 Excluding REIT. US\$ = 100JPY.

2 Total of offering and sales.

# IPOs in Japan in 2014

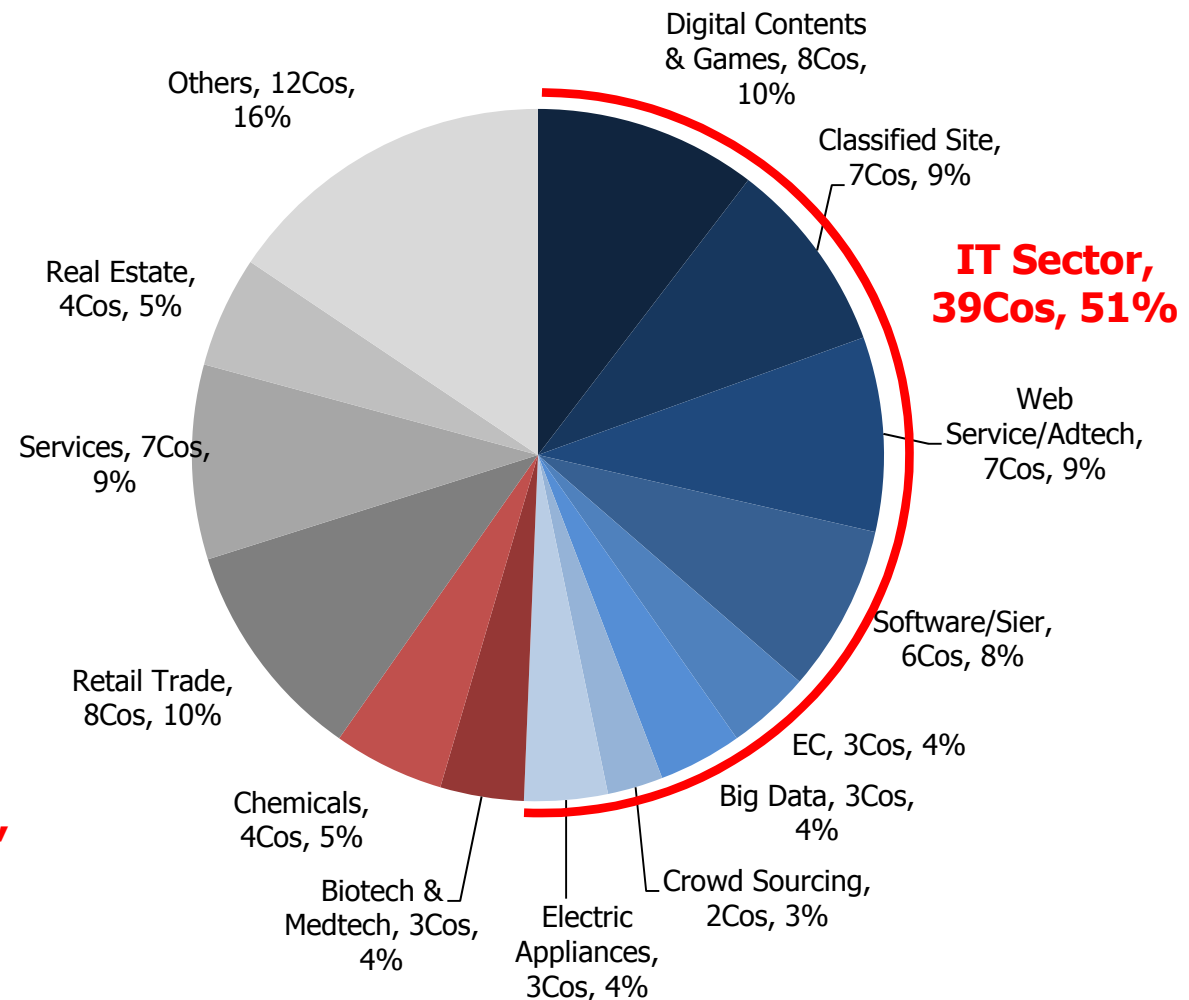
## - Markets & Sectors

**Number of IPOs by Market in Japan in 2014**  
(Total: 86 Cos)<sup>1</sup>



Note: 1 The data includes Tokyo Pro Market and REITs.  
2 The data excludes Tokyo Pro Market and REITs.

**Number of IPOs by Sector in Japan in 2014**  
(Total: 77 Cos)<sup>2</sup>





# E-Commerce IPOs from 2013 to 2014

Listing date	Ticker	Company Name	Market	Lead Underwriter	Revenue (US\$ m)	Net Profit (US\$ m)	Total IPO Amt (US\$ m)	Market Cap (IPO Price) (US\$ m)	Market Cap (First Price) (US\$ m)	PSR (First Price) (x)	PER (First Price) (x)	Market Cap (12/30/14) (US\$ m)	Change (IPO to 12/30/14)
18-Dec-14	6030	ADVENTURE	Mothers	Daiwa	8.9	0.2	9.5	54.6	124.0	13.9	586.7	83.7	53%
24-Sep-14	3195	GENERATION PASS	Mothers	Nomura	36.7	0.5	5.6	19.7	43.2	1.2	83.0	22.0	11%
23-Apr-14	3192	SHIROHATO	JQS	Nomura	29.5	0.7	6.8	19.6	28.7	1.0	42.0	30.2	54%
19-Nov-13	3189	ANAP	JQS	Daiwa	84.1	2.3	5.4	20.6	105.1	1.2	44.7	14.3	-31%
13-Sep-13	3187	SANWA COMPANY	Mothers	Nomura	46.4	1.8	4.2	26.4	97.3	2.1	55.3	126.3	378%
10-Jul-13	3185	DREAM VISION	Mothers	Nomura	62.0	0.3	12.0	34.9	70.0	1.1	252.5	8.1	-77%
13-Mar-13	3182	OISIX	Mothers	Mizuho	126.1	3.3	9.7	64.4	198.8	1.6	59.9	120.0	86%
14-Feb-13	3180	BEAUTY GARAGE	Mothers	SBI	43.5	1.5	5.5	26.5	48.0	1.1	32.6	35.5	34%
Median					44.9	1.1	6.2	26.5	83.7	1.2	57.6	32.8	44%

**ADVENTURE**  
(Air Ticket)



**GENERATION PASS**  
(Multiple Platforms)



**SHIROHATO**  
(Women's Underwear)



**ANAP**  
(Women's Fashion)



**SANWA COMPANY**  
(Housing Equipment)



**DREAM VISION**  
(Women's Fashion)



**OISIX**  
(Food)



**BEAUTY GARAGE**  
(for Beauty Salons)



Source: Bloomberg,  
Companies' website

Note:

- 1 US\$ = 100 JPY
- 2 As of December 30, 2014.

# Crowd Sourcing IPOs from 2013 to 2014

Listing date	Ticker	Company Name	Market	Lead Underwriter	Revenue (US\$ m)	Net Profit (US\$ m)	Total IPO Amont (US\$ m)	Market Cap (IPO Price) (US\$ m)	Market Cap (First Price) (US\$ m)	PSR (Frist Price) (x)	PER (Frist Price) (x)	Market Cap (12/30/14) (US\$ m)	Change (IPO to 12/30/14)
12-Dec-14	3900	CROWDWORKS	Mothers	Daiwa	0.5	-1.6	16.2	95.4	165.1	321.3	na	152.2	60%
18-Sep-14	3691	REAL WORLD	Mothers	Daiwa	20.7	0.0	14.3	68.4	121.8	5.9	5,914.2	57.5	-16%
10-Jul-13	6075	PHOTOCREATE	Mothers	SBI	24.8	0.6	3.8	19.6	44.2	1.8	68.5	17.5	-10%
Median					20.7	0.0	14.3	68.4	121.8	5.9	2,991.3	57.5	-10%

## CROWDWORKS (Crowd Sourcing)



## REAL WORLD (Crowd Sourcing)



## PHOTOCREATE (Photography)



Source: Bloomberg, Companies' website

Note:

1 US\$ = 100 JPY

2 As of December 30, 2014

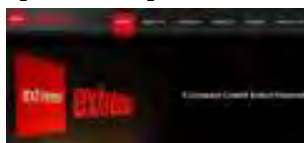
# Digital Contents & Games IPOs from 2013 to 2014

Listing date	Ticker	Company Name	Market	Lead Underwriter	Revenue (US\$ m)	Net Profit (US\$ m)	Total IPO Amt (US\$ m)	Market Cap (IPO Price) (US\$ m)	Market Cap (First Price) (US\$ m)	PSR (First Price) (x)	PER (First Price) (x)	Market Cap (12/30/14) (US\$ m)	Change (IPO to 12/30/14)
25-Dec-14	3904	KAYAC	Mothers	Daiwa	28.0	1.3	8.9	42.1	135.5	4.8	102.8	117.2	178%
25-Dec-14	6033	EXTREME	Mothers	Daiwa	13.3	-0.3	4.0	15.8	62.7	4.7	na	72.9	362%
18-Dec-14	3903	GUMI	TSE 1st	Nomura	111.9	-1.8	450.4	945.9	945.9	8.5	na	763.6	-19%
16-Dec-14	9418	U-NEXT	Mothers	Daiwa	179.0	11.8	46.9	158.1	208.2	1.2	17.7	375.1	137%
30-Oct-14	9467	ALPHAPOLIS	Mothers	Daiwa	20.5	3.9	28.5	102.9	198.7	9.7	50.9	91.4	-11%
15-Jul-14	3689	IGNIS	Mothers	Nomura	8.7	2.0	26.1	111.3	492.2	56.3	245.2	290.2	161%
26-Mar-14	3686	DLE	Mothers	Nomura	9.4	0.7	18.0	62.3	125.2	13.3	188.9	129.4	108%
12-Mar-14	9414	NIPPON BS BROADCASTING	TSE 2nd	Nomura	70.2	13.2	48.8	156.1	166.4	2.4	12.6	171.4	10%
20-Nov-13	3678	MEDIA DO	Mothers	Ichiyoshi	40.9	0.0	12.9	73.6	262.5	6.4	5,848.3	206.5	181%
14-Mar-13	3672	ALTPLUS	Mothers	Nomura	9.1	1.1	23.4	60.0	160.6	17.6	143.2	84.5	41%
<b>Median</b>					<b>24.3</b>	<b>1.2</b>	<b>24.7</b>	<b>88.2</b>	<b>182.6</b>	<b>7.4</b>	<b>123.0</b>	<b>150.4</b>	<b>122%</b>

## KAYAC (Games & Apps)



## EXTREME (Games)



## GUMI (Games)



## U-NEXT (Video on demand)



## AlphaPolis (Novel/Comic)



## IGNIS (Apps & Games)



## DLE (Animation)



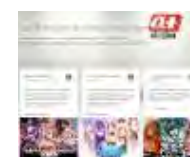
## NIPPON BS BROADCASTING (Television Broadcasting)



## MEDIA DO (Electronic Book)



## ALTPLUS (Mobile Social Game)



Source: Bloomberg,  
Companies' website

Note:

- 1 US\$ = 100 JPY
- 2 As of December 30, 2014



# Classified Site IPOs from 2013 to 2014

Listing date	Ticker	Company Name	Market	Lead Underwriter	Revenue (US\$ m)	Net Profit (US\$ m)	Total IPO Amont (US\$ m)	Market Cap (IPO Price) (US\$ m)	Market Cap (First Price) (US\$ m)	PSR (Frist Price) (x)	PER (Frist Price) (x)	Market Cap (12/30/14) (US\$ m)	Change (IPO to 12/30/14)
26-Dec-14	6034	MRT	Mothers	Daiwa	7.3	0.1	6.7	18.1	74.0	10.2	1,178.7	64.6	257%
22-Dec-14	6032	INTERWORKS	Mothers	Daiwa	26.7	2.9	18.5	83.7	97.7	3.7	33.3	82.4	-2%
16-Dec-14	3901	MARKLINES	JQS	SBI	8.5	1.5	6.5	61.8	109.6	12.9	71.4	91.6	48%
11-Dec-14	6027	BENGO4.COM	Mothers	Nomura	2.9	0.1	15.8	86.9	274.1	94.1	2,044.3	188.9	117%
16-Oct-14	6098	RECRUIT HOLDINGS	TSE 1st	Nomura	11,916	654	2,138	17,795	18,197	1.5	27.8	19,447	9%
27-Jun-14	6095	MEDPEER	Mothers	Nomura	5.7	1.1	10.8	65.1	150.5	26.2	132.5	123.4	90%
25-Mar-14	3685	MINNANO WEDDING	Mothers	Nomura	10.1	1.1	47.6	205.4	261.2	25.8	237.7	85.8	-58%
11-Dec-13	6084	O-UCCINO	Mothers	SBI	14.0	1.2	5.6	43.3	99.7	7.1	83.0	19.9	-54%
22-Nov-13	3679	ZIGEXN	Mothers	Nomura	11.7	3.6	59.0	306.3	893.4	76.2	250.4	374.8	22%
Median					10.1	1.2	15.8	83.7	150.5	12.9	132.5	91.6	22%

**MRT**  
(Medical Staffing Site)



**INTERWORKS**  
(Staffing Site)



**MARKLINES**  
(Automobile Industry Site)



**BENGO4.COM**  
(Lawyer Advisory Site)



**Recruit Holdings**  
(Sites for HR, Housing, Bridal, Travel, Restaurants, Beauty, Automobiles, Education and more)



**MEDPEER**  
(Medical SNS)



**Minnano Wedding**  
(Wedding Site)



**O-uccino**  
(Housing Site)



**ZIGEXN**  
(Classified Sites)



Source: Bloomberg, Companies' website

Note:

1 US\$ = 100 JPY

2 As of December 30, 2014

# Big Data IPOs from 2013 to 2014

Listing date	Ticker	Company Name	Market	Lead Underwriter	Revenue (US\$ m)	Net Profit (US\$ m)	Total IPO Amt (US\$ m)	Market Cap (IPO Price) (US\$ m)	Market Cap (First Price) (US\$ m)	PSR (First Price) (x)	PER (First Price) (x)	Market Cap (12/30/14) (US\$ m)	Change (IPO to 12/30/14)
24-Dec-14	3905	DATASECTION	Mothers	Daiwa	3.2	0.5	13.2	48.6	84.1	26.5	186.1	106.2	119%
19-Dec-14	6031	SCIGINEER	Mothers	SMBC Nikko	5.6	-1.0	11.6	50.3	113.6	20.5	na	178.9	256%
24-Jun-14	6094	FREAKOUT	Mothers	Nomura	21.6	0.9	16.0	120.4	421.3	19.5	485.6	202.0	68%
9-Dec-13	3680	HOTTO LINK	Mothers	Nomura	6.4	0.3	14.6	49.3	130.9	20.5	446.3	109.0	121%
25-Apr-13	3674	AUCFAN	Mothers	SMBC Nikko	6.2	1.0	9.6	45.9	184.8	29.8	182.9	97.1	112%
<b>Median</b>					<b>6.2</b>	<b>0.5</b>	<b>13.2</b>	<b>49.3</b>	<b>130.9</b>	<b>20.5</b>	<b>316.2</b>	<b>109.0</b>	<b>119%</b>

## DATASECTION (Social Data Analysis)



## SCIGINEER (Personalized Recommendation)



## FREAKOUT (Big Data Analysis)



## HOTTO LINK (SNS Data Analysis)



## AUCFAN (EC Statistics)



Source: Bloomberg, Companies' website

Note:

- 1 US\$ = 100 JPY
- 2 As of December 30, 2014

# Web Service and AdTech IPOs from 2013 to 2014

Listing date	Ticker	Company Name	Market	Lead Underwriter	Revenue (US\$ m)	Net Profit (US\$ m)	Total IPO Amount (US\$ m)	Market Cap (IPO Price) (US\$ m)	Market Cap (First Price) (US\$ m)	PSR (First Price) (x)	PER (First Price) (x)	Market Cap (12/30/14) (US\$ m)	Change (IPO to 12/30/14)
11-Dec-14	6026	GMO TECH	Mothers	Daiwa	23.7	1.1	18.4	63.8	150.0	6.3	130.9	73.3	15%
22-Oct-14	3696	CERES INC/JAPAN	Mothers	SBI	11.7	0.9	11.9	84.4	131.2	11.2	145.8	93.8	11%
21-Oct-14	3695	GMO RESEARCH	Mothers	Daiwa	19.4	0.9	10.9	33.8	78.9	4.1	87.7	44.6	32%
17-Sep-14	3690	LOCKON	Mothers	Nomura	10.9	0.4	5.1	39.7	152.8	14.0	360.4	103.6	161%
2-Jul-14	3688	VOYAGE GROUP	Mothers	Nomura	98.6	3.1	104.9	265.4	371.6	3.8	120.1	253.8	-4%
27-Jun-14	6096	RAREJOB	Mothers	Daiwa	11.3	-1.1	3.5	22.2	60.0	5.3	na	54.2	144%
6-Mar-14	3683	CYBERLINKS	JQS	Mizuho	71.1	1.5	6.9	35.1	95.7	1.3	62.0	69.1	97%
10-Dec-13	3681	V-CUBE	Mothers	Nomura	20.1	1.2	44.3	141.8	215.3	10.7	184.3	143.6	1%
29-Nov-13	6081	ALLIED ARCHITECTS	Mothers	Nomura	10.7	1.3	13.0	70.3	231.5	21.5	171.6	43.7	-38%
<b>Median</b>					<b>19.4</b>	<b>1.1</b>	<b>11.9</b>	<b>63.8</b>	<b>150.0</b>	<b>6.3</b>	<b>138.3</b>	<b>73.3</b>	<b>15%</b>

**GMO TECH**  
(SEO Service)



**CERES**  
(Point Media)



**GMO Research**  
(Research via Internet)



**LOCKON**  
(AdTech)



**VOYAGE GROUP**  
(Web Media & AdTech)



**RAREJOB**  
(Online English)



**CYBERLINKS**  
(Cloud Computing)



**V-CUBE**  
(Video Conferencing)



**Allied Architects**  
(Social Media Marketing)



Source: Bloomberg, Companies' website

Note:

1 US\$ = 100 JPY

2 As of December 30, 2014

# Software/Sier IPOs from 2013 to 2014

Listing date	Ticker	Company Name	Market	Lead Underwriter	Revenue (US\$ m)	Net Profit (US\$ m)	Total IPO Amount (US\$ m)	Market Cap (IPO Price) (US\$ m)	Market Cap (First Price) (US\$ m)	PSR (First Price) (x)	PER (First Price) (x)	Market Cap (12/30/14) (US\$ m)	Change (IPO to 12/30/14)
16-Dec-14	3902	MEDICAL DATA VISION	Mothers	SMBC Nikko	15.3	2.0	14.3	57.2	135.0	8.8	65.9	114.6	100%
27-Nov-14	3698	CRI MIDDLEWARE	Mothers	HS	9.9	0.5	7.6	33.6	188.9	19.1	377.8	146.1	335%
13-Nov-14	3697	SHIFT	Mothers	Nomura	13.1	-0.9	7.8	34.3	158.3	12.1	na	137.4	301%
22-Oct-14	3694	OPTIM	Mothers	Daiwa	17.1	0.5	10.6	64.7	233.1	13.6	466.2	399.8	518%
30-Sep-14	3692	FFRI	Mothers	Nomura	6.6	1.2	5.6	26.7	73.9	11.2	63.8	456.8	1608%
23-Apr-14	3687	FIXSTARS	Mothers	Mitsubishi UFJ Morgan Stanley	17.3	1.7	4.9	42.4	111.0	6.4	65.6	193.0	356%
11-Dec-13	3682	ENCOURAGE TECHNOLOGIES	Mothers	Nomura	9.2	1.9	12.9	55.2	119.8	13.1	62.7	69.4	26%
22-Oct-13	3677	SYSTEM INFORMATION	JQS	SBI	40.4	1.4	5.1	19.0	90.0	2.2	64.3	34.6	82%
22-Mar-13	3673	BROADLEAF	TSE 1st	Nomura	153.2	35.0	233.2	267.4	297.2	1.9	8.5	444.7	66%
12-Mar-13	3671	SOFTMAX	Mothers	Nomura	29.6	0.5	7.5	24.9	105.3	3.6	193.0	38.2	54%
20-Feb-13	3670	KYORITSU COMPUTER & COMMUNICATIONS	JQS	Mizuho	42.7	1.1	6.0	18.0	60.0	1.4	57.1	26.6	48%
<b>Median</b>					<b>17.1</b>	<b>1.2</b>	<b>7.6</b>	<b>34.3</b>	<b>119.8</b>	<b>8.8</b>	<b>64.9</b>	<b>137.4</b>	<b>100%</b>

**MEDICAL DATA VISION**  
(Medical System)



**CRI MIDDLEWARE**  
(Middleware)



**SHIFT**  
(Software Testing)



**OPTiM**  
(Security Software)



**FFRI**  
(Security Software)



**FIXSTARS**  
(Software & Multi-core Processors)



**ENCOURAGE TECHNOLOGIES**  
(IT Systems Monitoring Software)



**SYSTEM INFORMATION**  
(Customized Development of Software)



**BROADLEAF**  
(Software Development & Support)



**SOFTMAX**  
(Medical Record System)



**KYORITSU COMPUTER & COMMUNICATIONS**  
(System Solution for SMEs)



Source: Bloomberg,  
Companies' website

Note:

- 1 US\$ = 100 JPY
- 2 As of December 30, 2014

# Biotech/Medtech IPOs from 2013 to 2014

Listing date	Ticker	Company Name	Market	Lead Underwriter	Revenue (US\$ m)	Net Profit (US\$ m)	Total IPO Amount (US\$ m)	Market Cap (IPO Price) (US\$ m)	Market Cap (First Price) (US\$ m)	PSR (First Price) (x)	PER (First Price) (x)	Market Cap (12/30/14) (US\$ m)	Change (IPO to 12/30/14)
25-Sep-14	4591	RIBOMIC	Mothers	Daiwa	1.5	-2.1	57.2	277.8	221.0	146.2	na	165.1	-41%
26-Mar-14	7779	CYBERDYNE	Mothers	SMBC Nikko	2.9	-5.7	89.6	401.6	923.6	322.4	na	3,171.1	690%
13-Feb-14	4589	ACUCELA	Mothers	Mitsubishi UFJ Morgan Stanley	47.6	4.3	190.4	641.2	819.3	17.2	191.4	254.2	-60%
24-Dec-13	6090	HUMAN METABOLOME TECHNOLOGIE	Mothers	Ichiyoshi	5.0	-1.0	22.0	66.3	146.8	29.6	na	64.0	-4%
6-Dec-13	4588	ONCOLYS BIOPHARMA	Mothers	SMBC Nikko	4.0	-1.0	66.4	221.3	297.9	75.1	na	71.4	-68%
26-Jun-13	4978	REPROCELL	JQG	SMBC Nikko	3.2	-0.2	47.7	265.6	1,477.6	466.8	na	399.2	50%
11-Jun-13	4587	PEPTIDREAM	Mothers	Mizuho	2.7	0.1	77.6	322.2	1,018.0	378.4	10,209.8	1,443.2	348%
13-Feb-13	4586	MEDRX	Mothers	Nomura	7.4	-4.3	26.8	51.1	112.5	15.2	na	58.3	14%
<b>Median</b>					<b>3.6</b>	<b>-1.0</b>	<b>61.8</b>	<b>271.7</b>	<b>558.6</b>	<b>110.6</b>	<b>5,200.6</b>	<b>209.7</b>	<b>5%</b>

**RIBOMIC**  
(Biotech - Aptamers)



**CYBERDYNE**  
(Medical Device  
-Cyborg-type Robot)



**ACUCELA**  
(Biotech -Ophthalmic)



**HUMAN METABOLOME TECHNOLOGIE**  
(Metabolome Analysis Service)



**ONCOLYS BIOPHARMA**  
(Biotech -Infectious)



**REPROCELL**  
(iPS Cell Supply)



**PEPTIDREAM**  
(Peptide Therapeutics)



**MEDRX**  
(Biotech – Cardiovascular,  
Inflammation)



Source: Bloomberg,  
Companies' website












Note:

1 US\$ = 100 JPY

2 As of December 30, 2014




# (Reference) Mining Sector

Ticker	Sector	Name	Revenue (US\$ M)	Net Profit (US\$ M)	Net Asset (US\$ M)	Market Cap (US\$ M)	PER (x)	PBR (x)
8058	Trading Company	MITSUBISHI CORP  Mitsubishi Corporation	76,352	3,614	55,394	35,266	9.8	0.64
8031		MITSUI & CO LTD  MITSUI & CO., LTD.	57,319	3,501	41,003	30,837	8.8	0.75
8001		ITOCHU CORP  ITOCHU	55,875	2,453	23,995	22,067	9.0	0.92
8053		SUMITOMO CORP  Sumitomo Corporation	33,174	2,231	25,402	16,752	7.5	0.66
8002		MARUBENI CORP  Marubeni	70,557	2,109	15,332	13,130	6.2	0.86
2768		SOJITZ CORP  sojitz <small>Other names: Sojitz Ltd etc.</small>	18,031	273	4,930	2,165	7.9	0.44
1605	Oil, Gas	INPEX CORP  INPEX <small>INPEX CORPORATION</small>	13,346	1,837	29,960	21,825	11.9	0.73
1662		JAPAN PETROLEUM EXPLORATION  JAPEX	2,766	290	4,969	2,206	7.6	0.44
1515	Limestone	NITTETSU MINING CO LTD  NITTETSU MINING	1,143	39	848	373	9.5	0.44
1518	Coal	MITSUI MATSUSHIMA CO LTD  三井物産マツシマ株式会社	773	15	328	189	12.3	0.57
1514		SUMISEKI HOLDINGS INC  SUMISEKI	246	4	58	71	18.3	1.21
Average (Trading Cos)			51,885	2,363	27,676	20,036	8.2	0.71
Median (Trading Cos)			56,597	2,342	24,699	19,409	8.4	0.71
Average (excluding Trading Cos)			3,655	437	7,233	4,933	11.9	0.68
Median (excluding Trading Cos)			1,143	39	848	373	11.9	0.57
Average (Coal Cos)			510	10	193	130	15.3	0.89
Average			29,962	1,488	18,384	13,171	9.9	0.70
Median			18,031	1,837	15,332	13,130	9.0	0.66

Source: Bloomberg

Note: As of August 22, 2014

# (Reference) Privatization

Ticker	Sector	Name	Revenue (US\$ M)	Net Profit (US\$ M)	Net Asset (US\$ M)	Market Cap (US\$ M)	PER (x)	PBR (x)
1605	Mining (Oil, Gas)	INPEX CORP  INPEX CORPORATION	13,346	1,837	29,960	21,825	11.9	0.73
1662		JAPAN PETROLEUM EXPLORATION 	2,766	290	4,969	2,206	7.6	0.44
9513	Power Utilities	ELECTRIC POWER DEVELOPMENT CO 	7,068	287	5,195	5,630	19.6	1.08
9432	Telecom	NIPPON TELEGRAPH & TELEPHONE 	109,252	5,855	109,248	78,546	13.4	0.72
9437		NTT DOCOMO INC 	44,612	4,647	56,935	79,639	17.1	1.40
2914	Tobacco	JAPAN TOBACCO INC 	23,998	4,280	25,961	72,610	17.0	2.80
9020	Railway	EAST JAPAN RAILWAY CO 	27,029	1,999	21,994	33,030	16.5	1.50
9022		CENTRAL JAPAN RAILWAY CO 	16,525	2,557	18,023	30,993	12.1	1.72
9021		WEST JAPAN RAILWAY CO 	13,310	656	8,074	9,542	14.5	1.18
Average (Mining)			8,056	1,064	17,465	12,016	9.7	0.59
Average			28,656	2,490	31,151	37,114	14.4	1.29
Median			16,525	1,999	21,994	30,993	14.5	1.18

Source: Bloomberg

Note: As of August 22, 2014



1. Japan-Mongolia Relations

2. Comparison among Major Stock Markets

3. Expansion of IPO Market in Japan

**4. Features of IPO Market in Japan**

5. Listing on Tokyo Stock Exchange

A. TOKYO PRO Market

B. Overview of the Japanese Financial Market

# Features of IPO Market in Japan

---

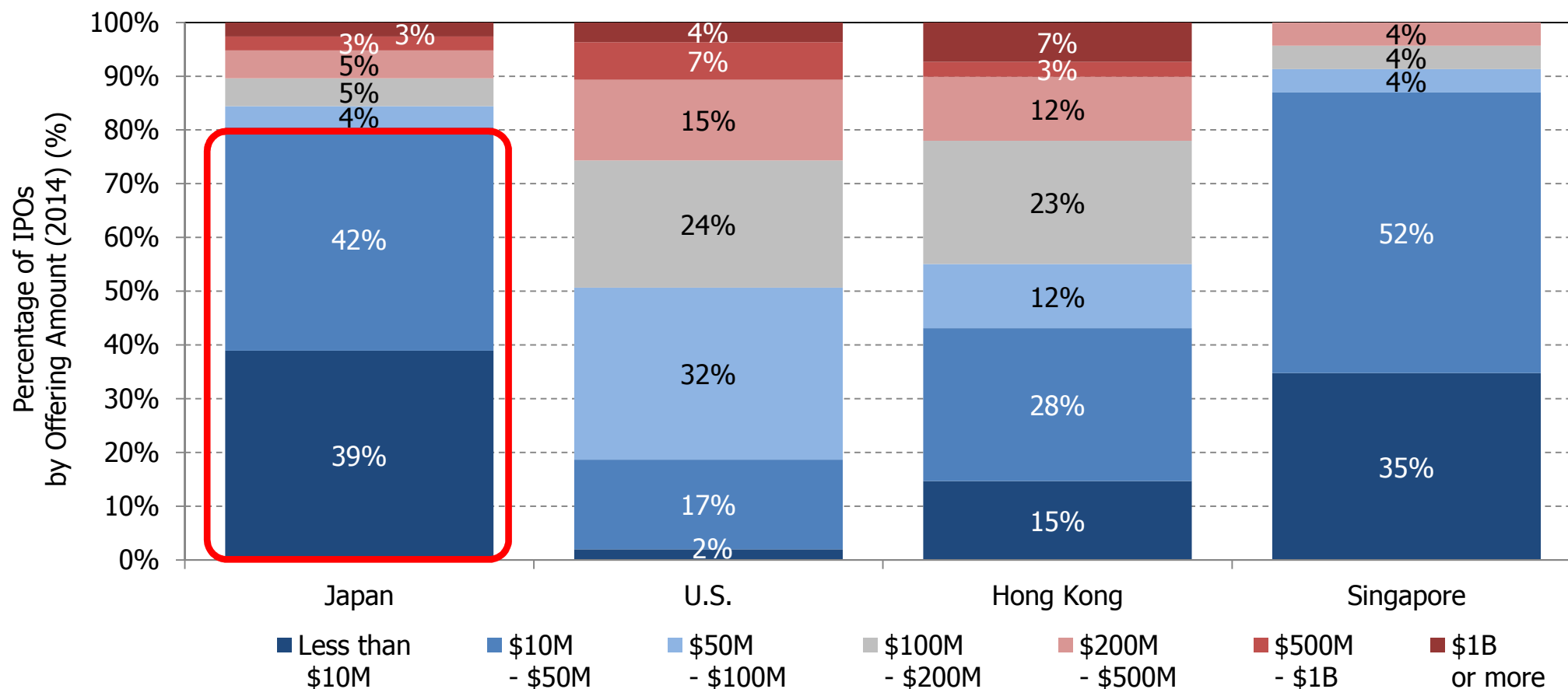
- 1 Successful Small IPOs**
- 2 High Liquidity**
- 3 Low IPO Cost & High IPO Valuation**
- 4 Many Companies Moved up to the TSE 1st Section**
- 5 Successful Follow-on Offerings**
- 6 Large IPOs**

# 1. Successful Small IPOs

## - IPO Deal Size Comparison of JP, US, HK and SG

**More than 80% of IPOs in Japan raised less than \$50M.**

**Comparison of Number of IPOs by Offering Amount in 2014 (Japan, US, Hong Kong, Singapore)**



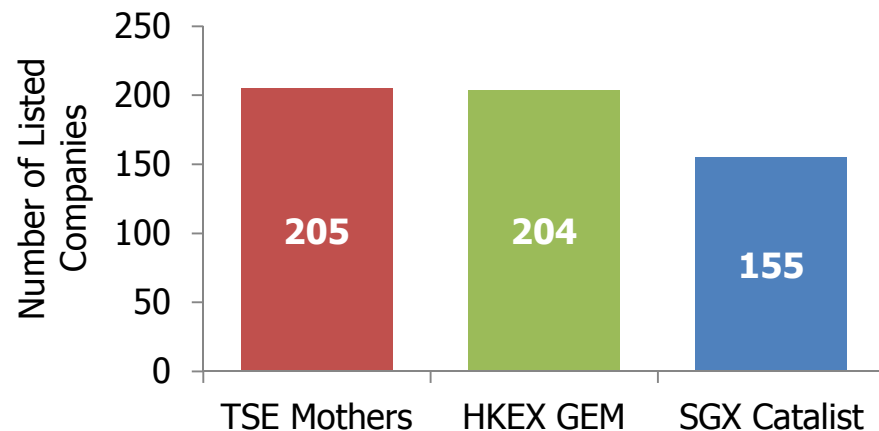
Source: Tokyo Stock Exchange, NASDAQ website, Hong Kong Exchanges and Clearing Limited website, Singapore Exchange website

Note: The total number of IPOs in each country. It includes new listings of foreign companies in the country, excludes listings without public offerings or selling and JREIT. It includes new listings on NASDAQ and NYSE in the United States. Exchange rates as of the listing date.

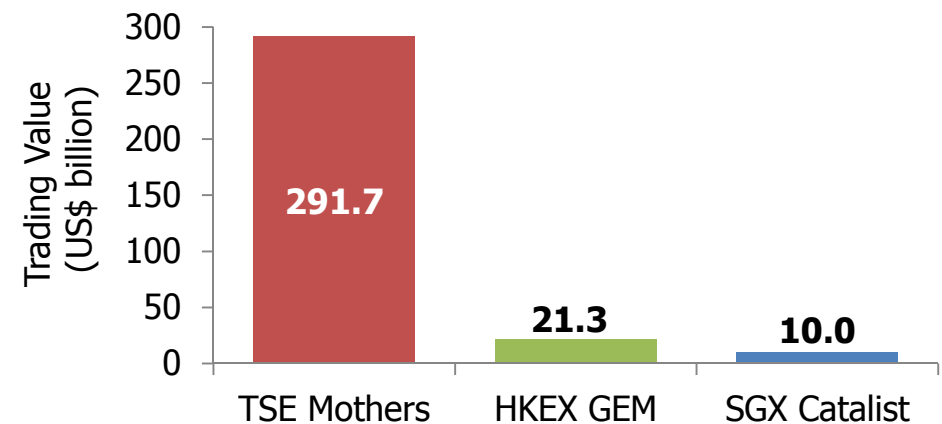
## 2. High Liquidity - Comparison of Emerging Enterprise Markets

**TSE Mothers is larger and more liquid than HKEX GEM and SGX Catalist.**

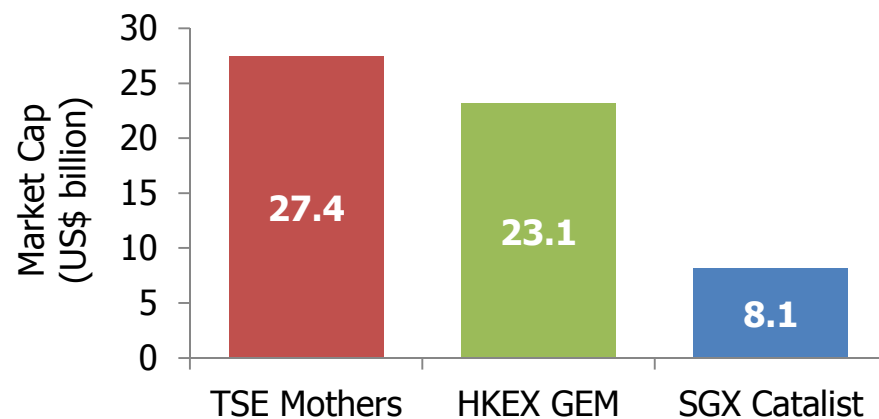
**Number of Listed Companies (as at of end of Dec. 2014)**



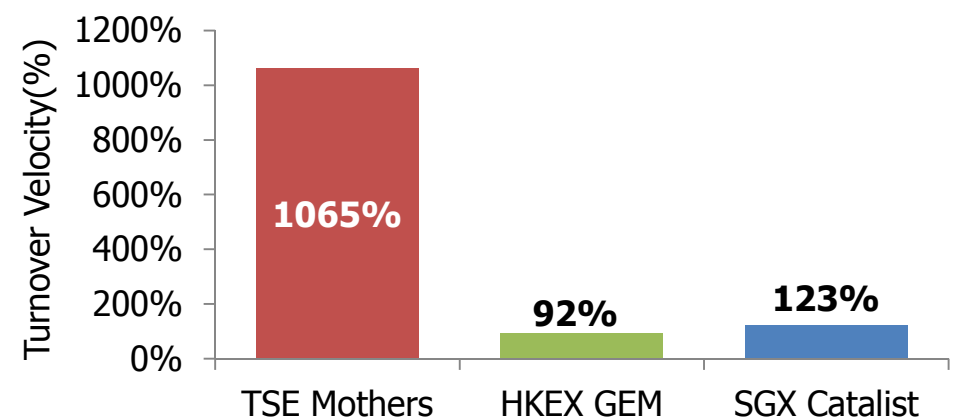
**Annual Trading Value (2014)<sup>1</sup>**



**Market Capitalization (as of end of Dec. 2014)<sup>1</sup>**



**Turnover Velocity (2014)<sup>2</sup>**



Source: Tokyo Stock Exchange, Hong Kong Exchanges and Clearing Limited, Singapore Exchange

Note: 1 Converted into USD as at the end of Dec 2014

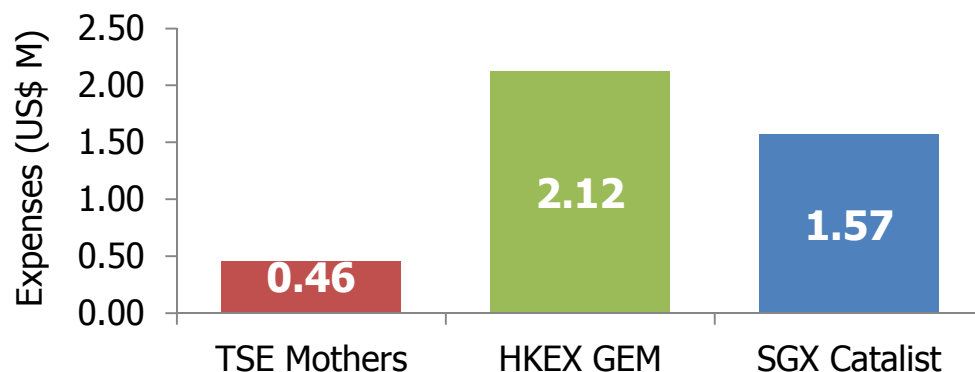
2 Turnover Velocity = Annual Trading Value / Market Capitalization as at the end of Dec. 2014



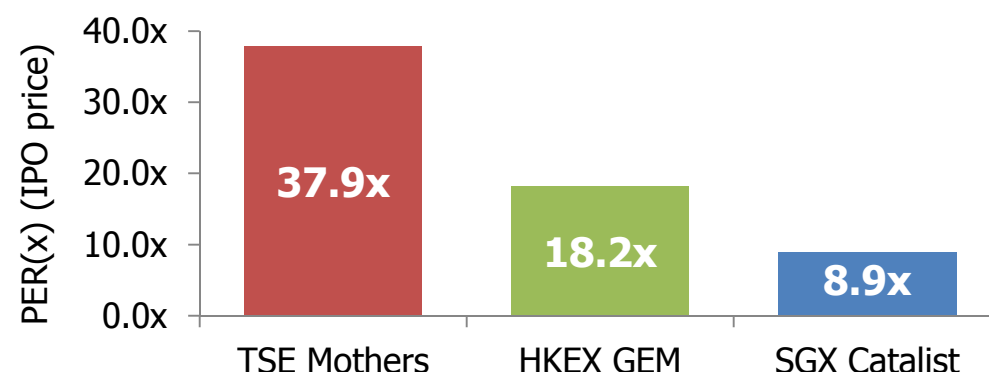
### 3. Low IPO Cost & High IPO Valuation

**Listing expenses at listing on TSE Mothers is much lower than the others.  
IPO valuation in TSE Mothers is relatively higher than IPO valuation in the others.**

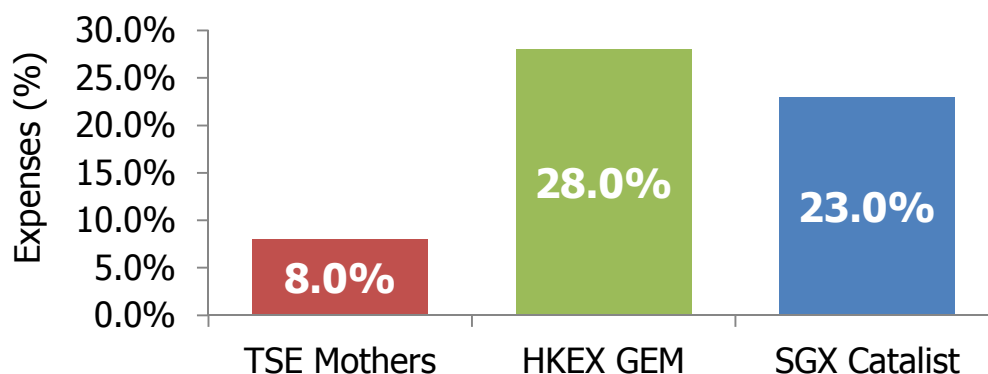
**The Median of Expenses through IPO (2014)**



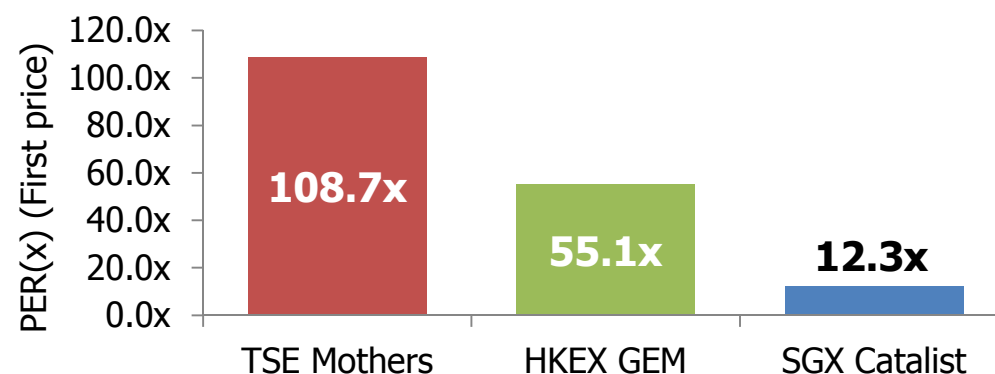
**The Median of PE Ratio of IPO Price (2014)**



**The Median of Expenses Ratio through IPO (2014)**



**The Median of PE Ratio of First Price (2014)**



Source: Prospectus and annual report of each company.

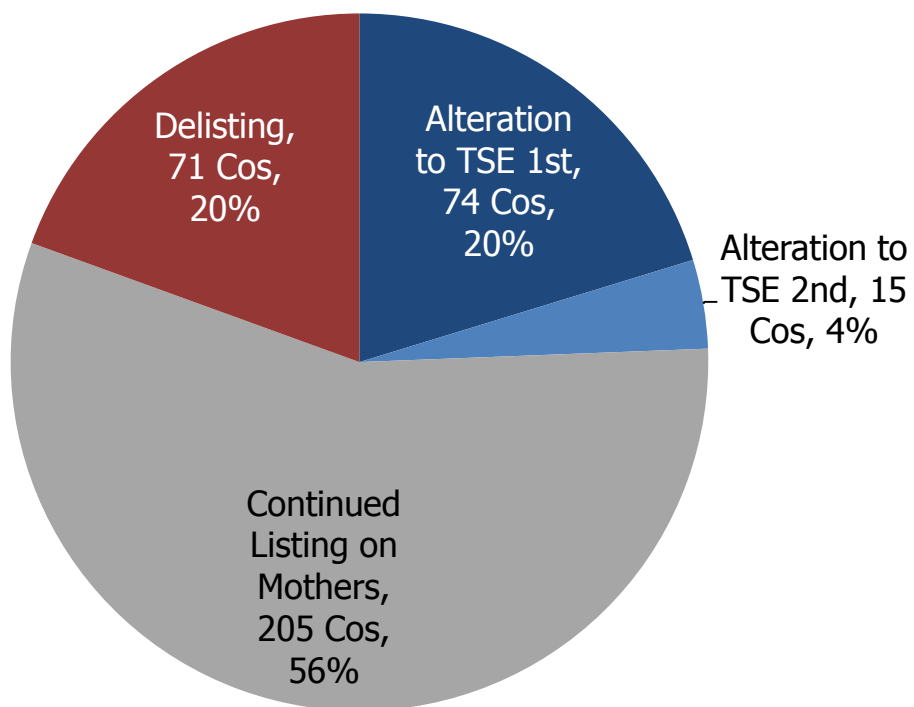
Note: 1 Listing expenses is defined as the difference between gross proceeds and net proceeds.

2 Currency exchange rates are as of the listing date.

## 4. Post-listing Trends on Mothers

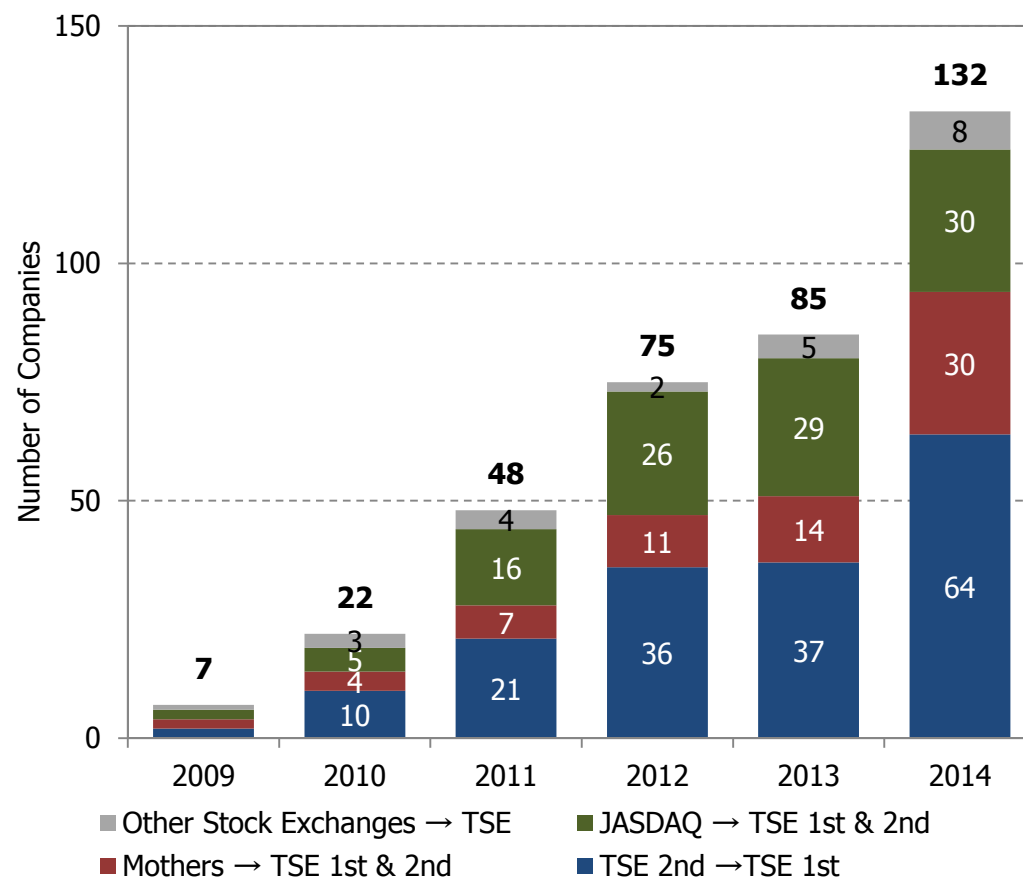
**20% of Mothers IPO companies (74 cos.) moved up to the TSE 1st Section.**

**Post-listing Trends on Mothers  
(365 companies)**



Note: As of the end of 2014

**Trend of Market Transfers**



Note: As of the end of 2014



# 5. Successful Follow-on Offerings

**Companies of Emerging Enterprise Markets successfully conduct follow-on offerings.**

## **Largest 25 Follow-on Offerings in 2014**

#	Date	Ticker	Market	Company	Sector	Offering Amount (US\$ M)	Offering Place
1	23-Jun-14	8801	TSE 1st	MITSUI FUDOSAN CO LTD	Real Estate	3,138	Japan and Overseas
2	23-Jul-14	8750	TSE 1st	DAI-ICHI LIFE INSURANCE	Insurance	2,590	Japan and Overseas
3	29-Jan-14	7211	TSE 1st	MITSUBISHI MOTORS CORP	Transportation Equipment	2,439	Japan and Overseas
4	26-Feb-14	5406	TSE 1st	KOBE STEEL LTD	Iron & Steel	650	Japan and Overseas
5	12-Mar-14	7550	TSE 1st	ZENSHO HOLDINGS CO LTD	Retail Trade	251	Japan
<b>6</b>	<b>12-Dec-14</b>	<b>7779</b>	<b>Mothers</b>	<b>CYBERDYNE INC</b>	<b>Precision Instruments</b>	<b>221</b>	<b>Overseas</b>
7	19-Mar-14	6141	TSE 1st	DMG MORI SEIKI CO LTD	Machinery	209	Overseas
8	16-Dec-14	9044	TSE 1st	NANKAI ELECTRIC RAILWAY CO	Land Transportation	188	Japan
9	22-Oct-14	3360	TSE 1st	SHIP HEALTHCARE HOLDINGS INC	Wholesale Trade	173	Japan
10	17-Jun-14	3880	TSE 1st	DAIO PAPER CORP	Pulp & Paper	132	Japan
11	25-Nov-14	3258	TSE 1st	JOWA HOLDINGS CO LTD	Real Estate	103	Japan
12	17-Jun-14	4631	TSE 1st	DIC CORP	Chemicals	98	Japan
<b>13</b>	<b>21-Apr-14</b>	<b>3668</b>	<b>Mothers</b>	<b>COLOPL INC</b>	<b>Information &amp; Communication</b>	<b>98</b>	<b>Japan</b>
14	27-Nov-14	2193	TSE 1st	COOKPAD INC	Services	90	Overseas
<b>15</b>	<b>17-Mar-14</b>	<b>2121</b>	<b>Mothers</b>	<b>MIXI INC</b>	<b>Services</b>	<b>69</b>	<b>Japan</b>
16	22-Apr-14	6269	TSE 1st	MODEC INC	Machinery	62	Japan
<b>17</b>	<b>09-Jul-14</b>	<b>7777</b>	<b>JASDAQ</b>	<b>3-D MATRIX LTD</b>	<b>Precision Instruments</b>	<b>53</b>	<b>Overseas</b>
<b>18</b>	<b>04-Jun-14</b>	<b>6079</b>	<b>Mothers</b>	<b>ENERES CO LTD</b>	<b>Services</b>	<b>51</b>	<b>Japan</b>
19	02-Sep-14	7294	TSE 1st	YOROZU CORP	Transportation Equipment	47	Japan
20	22-Jul-14	7283	TSE 1st	AISAN INDUSTRY CO LTD	Transportation Equipment	47	Japan
<b>21</b>	<b>11-Mar-14</b>	<b>4565</b>	<b>Mothers</b>	<b>SOSEI GROUP CORP</b>	<b>Pharmaceutical</b>	<b>44</b>	<b>Japan</b>
22	27-Nov-14	3397	TSE 1st	TORIDOLL CORP	Retail Trade	42	Japan
23	27-Jan-14	7212	TSE 1st	F-TECH INC	Transportation Equipment	39	Japan
24	16-Jun-14	7148	TSE 1st	FINANCIAL PRODUCTS GROUP CO	Securities & Commodity Futures	38	Japan
25	06-Mar-14	5852	TSE 2nd	AHRESTY CORP	Nonferrous Metals	34	Japan

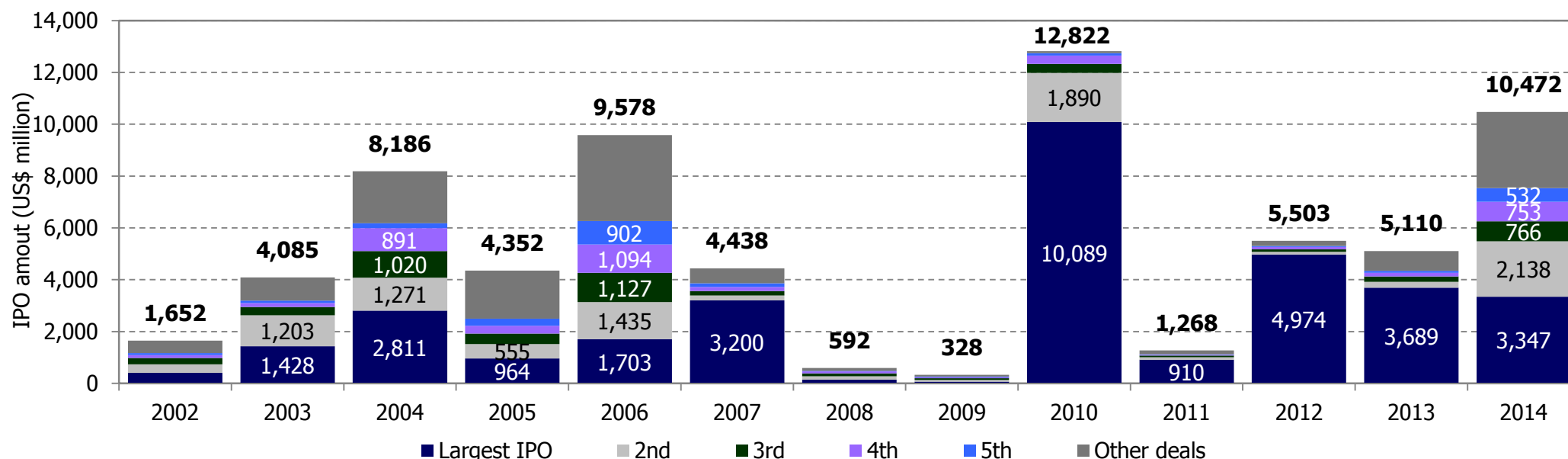
Source: TSE

Note: 1 US\$ = 100 JPY

# 6. Large IPOs

**Dai-ichi Life's IPO in 2010 was the largest deal that exceeded US\$ 1 billion.**

## Historical IPO Amount on TSE



	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
Largest	SOHGO SECURITY SERVICES	NEC Electronics	Electric Power Development	SUMCO	Aozora Bank	Sony Financial Holdings	Hulic	Japan Drilling	The Dai-ichi Life Insurance	NEXON	Japan Airlines	Suntory Beverage & Food	Japan Display
2nd	NEC Fielding	SEIKO EPSON	Shinsei Bank	The Tokyo Star Bank	Nomura Real Estate Holdings	KITO	Morimoto	FOI	Otsuka Holdings	CALBEE	LIFENET INSURANCE	Ashikaga Holdings	Recruit Holdings
3rd	NS Solutions	Japan Petroleum Exploration	Elpida Memory	PGM Holdings	Accordia Golf	Universal Studios Japan	GREE	Mitsubishi Research Institute	Paltac	W-SCOPE	ZENKOKU HOSHIO	Broadleaf	Hitachi Maxell
4th	AEON Mall	OncoTherapy Science	NTT URBAN DEVELOPMENT	So-net Entertainment	Idemitsu Kosan	TS TECH	HOSHIZAKI ELECTRIC	Jowa Holdings	POLA ORBIS HOLDINGS	Poletowin Pitcrew Holdings	CHIMNEY	Open House	Skylark
5th	NEC Mobiling	Century Leasing System	ULVAC	HAKUHODO DY HOLDINGS	Takata	The Yachiyo Bank	Tri-Stage	COOKPAD	Tera Probe	Kurotani Corporation	COLOPL	Tama Home	TechnoPro Holdings

Source: TSE

Note: Including domestic selling. Excluding REITs, overseas selling, and over-allotment. Shaded pink deals exceeded US\$ 500 million. 1 USD = 100 JPY  
IPOs on OSE including JASDAQ has included since July 16, 2013 when the equity market of TSE and OSE.

© 2015 Japan Exchange Group, Inc. and/or its affiliates. All rights reserved.



1. Japan-Mongolia Relations

2. Comparison among Major Stock Markets

3. Expansion of IPO Market in Japan

4. Features of IPO Market in Japan

**5. Listing on Tokyo Stock Exchange**

A. TOKYO PRO Market

B. Overview of the Japanese Financial Market

# Key Benefits of Listing on TSE

---

## Fundraising

- ✓ Expand fundraising opportunities with High Net Worth Individuals that hold US\$15.68 trillion in assets as of end of 2013
- ✓ High valuation due to great interest in foreign stocks

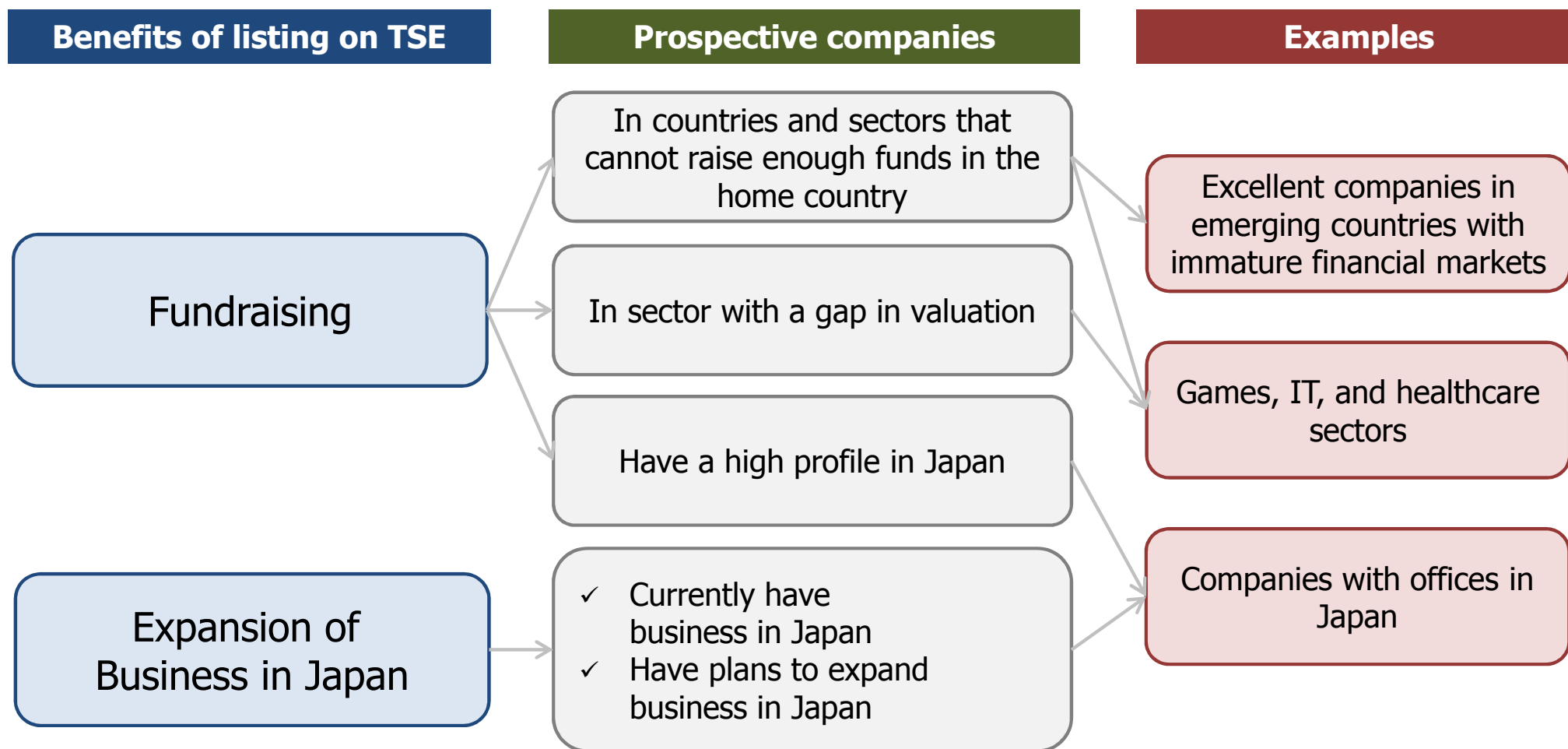
## Expansion of Business in Japan

- ✓ Enhance corporate profile and credibility in Japan
- ✓ Expand opportunities for strategic alliances with Japanese corporations

## M&A with Japanese Companies

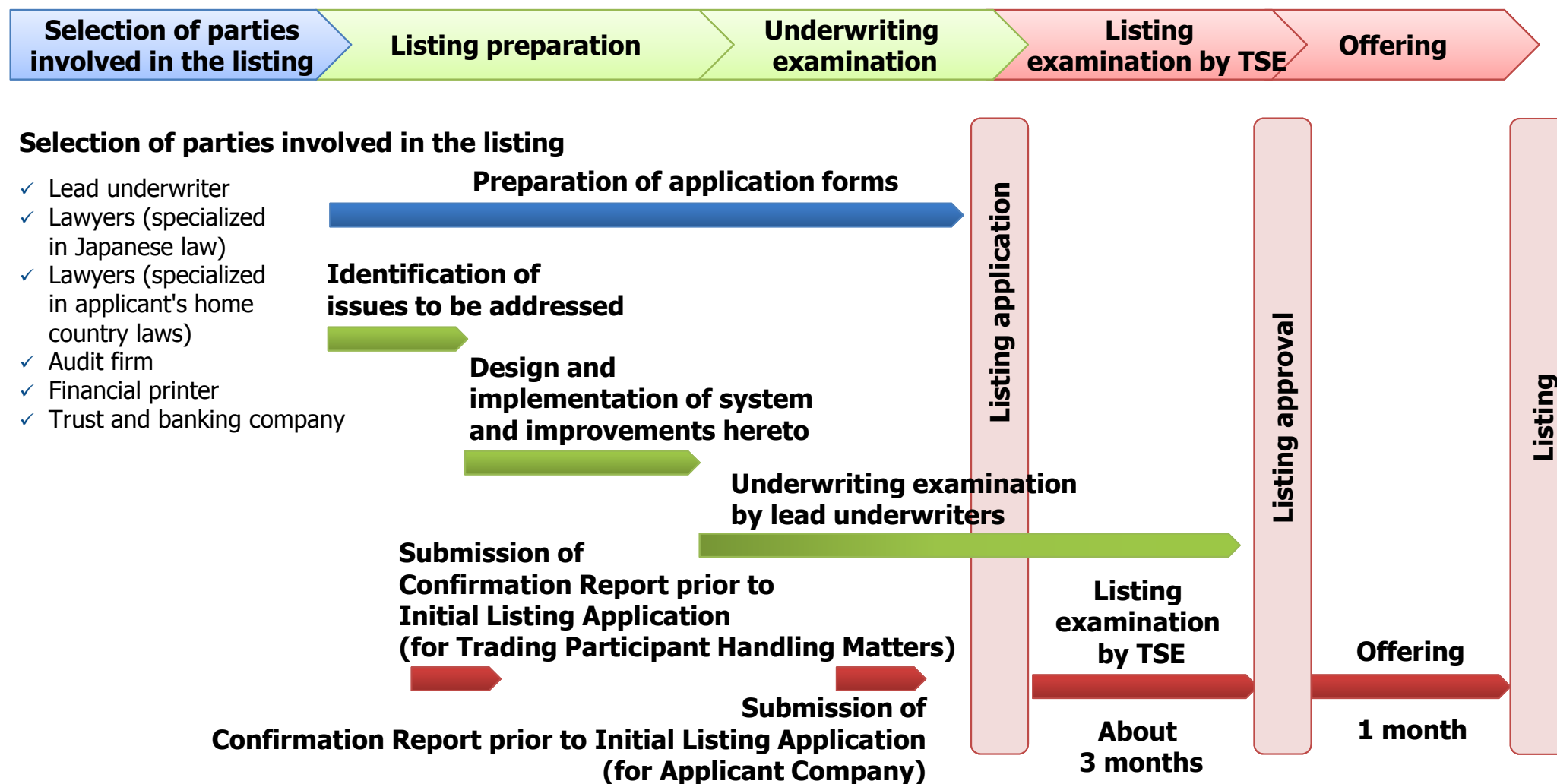
- ✓ Increase chances of M&A with Japanese corporations

# Prospective Companies

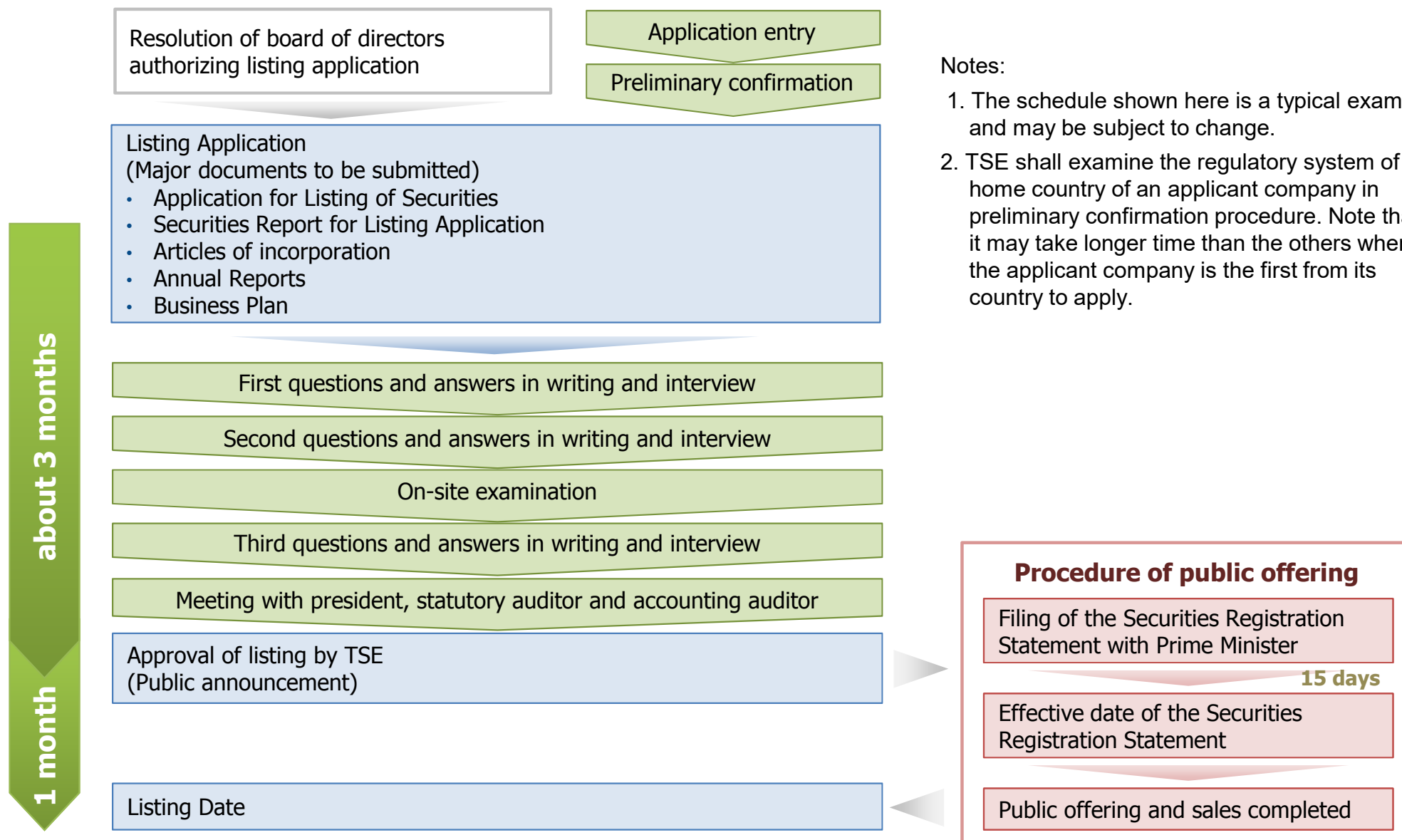


# Listing Schedule

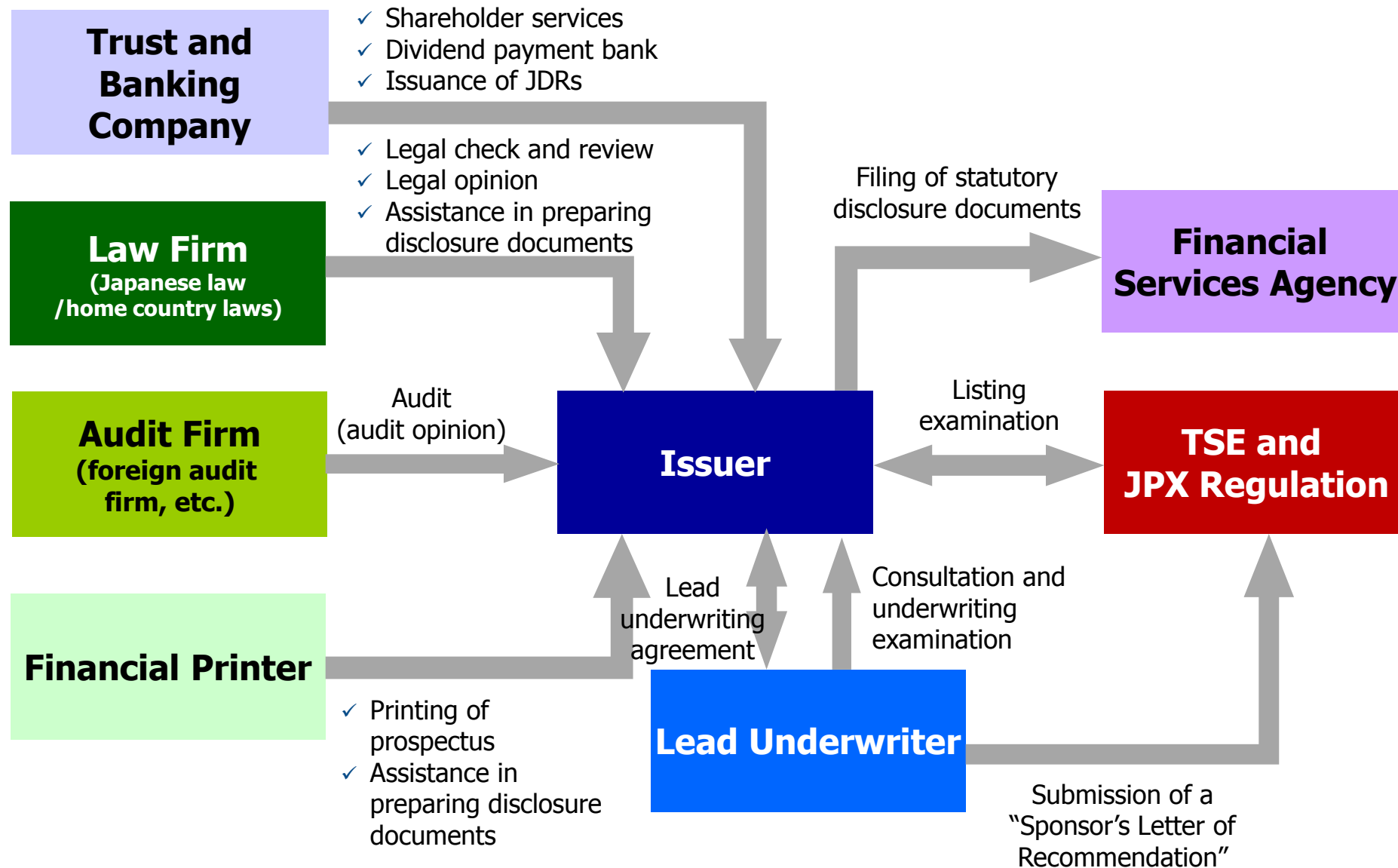
Depending on the internal systems of the company, however, it takes about one year from kick-off to listing. Note that the company needs to be audited for two business years.



# Listing Examination Schedule



# Roles of Each Party Involved in an IPO





# Roles of Each Party Involved in an IPO

The following are the key parties in Japan and the home country who support the listing of a foreign company on TSE. These participants work together closely during the pre-listing process to support preparations for a listing.

● **Lead Underwriter (TSE trading participant)**, is comprehensively involved in the procedures and preparations for listing overall. It provides underwriting business by entering into a lead underwriting agreement with an issuer and provides advice and consultation on the listing and listing schedule. At the time of listing, the lead underwriter submits a Sponsor's Letter of Recommendation to TSE.

● **Law Firm**, checks and reviews listing-related matters from a legal perspective and prepares a legal opinion. It also helps the applicant prepare disclosure documents. After listing, it discloses corporate information as a legal representative of the listed foreign company.

● **Audit Firm (foreign audit firm, etc.)**, provides provides advice on the design and implementation of the accounting organization and financial statements and also audits the financial statements (expression of an audit opinion).

● **Trust and Banking company**, acts as a shareholder services agent for Japanese shareholders after the listing and may act as a dividend payment bank to provide services related to dividend payment. If a foreign company lists through JDRs, the trust and banking company will be responsible for the issuance of the JDRs. Please see section 7 for details on listing through JDRs.

● **Tokyo Stock Exchange**, explains its listing system to companies, IPO-related parties, and so on, and provides preliminary or prior consultation on the listing.

# Formal Requirements for Listing

Each market has different criteria in line with its concept.

	Main Market		Mothers	JASDAQ		TOKYO PRO Market
	1st Section	2nd Section		Standard	Growth	
Number of shareholders	2,200 or more	800 or more	200 or more	200 or more		—
Tradable shares						
Number of tradable shares	20,000 units or more	4,000 units or more	2,000 units or more	—		—
Market capitalization of tradable shares	JPY 1 billion (USD 10m) or more	JPY 1 billion (USD 10m) or more	JPY 500 million (USD 5m) or more	JPY 500 million (USD 5m) or more		—
Ratio of tradable shares to listed shares	35% or more	30% or more	25% or more	—		—
Public offering	—	—	500 trading units or more	10 percent or more or 1,000 trading units		—
Market capitalization of listed shares	JPY 25 billion (USD 250m) or more	JPY 2 billion (USD 20m) or more	JPY 1 billion (USD 10m) or more	—		—
Number of years of business operation	3 years or more		1 year or more	—		—
Shareholders' equity	JPY 1 billion (USD 10m) or more		—	JPY 200 million (USD 2m) or more	Not negative	—
Amount of profits or Market capitalization	[Ordinary profit] Total amount of JPY500 million (USD 5m) or more in the last 2 fiscal years [Market cap] Market cap: JPY 50 billion (USD 500m) or more Sales: JPY 10 billion (USD 100m) or more		—	[Ordinary profit] JPY100 million (USD 1m) or more [Market cap] JPY5 billion (USD 50m) or more	—	—

Note: 1US\$ = 100JPY

# Overview of Listing Examination for Mothers

**TSE examines the company, which meets “Formal Requirements” and conducts an examination based on the “Eligibility Requirements.”**

**When applying TSE rules to a foreign country or a foreign corporation where the foreign country or the foreign corporation is an issuer of a listed security, TSE shall also take into account the legal systems, practices and customs in such foreign country or the country of the foreign corporation.**

- 1 Appropriateness of the Disclosure of Corporate Information, Risk Information, etc.**
  - The company is able to make disclosure of the corporate information, risk information, etc. may be carried out in an appropriate manner
- 2 Soundness of Corporate Management**
  - The company is carrying out business in a fair and faithful manner
- 3 Effectiveness of Corporate Governance and Internal Management System of an Enterprise**
  - Corporate governance and internal management system are developed in accordance with the size, corporate maturity, etc. of the enterprise, and functioning properly
- 4 Reasonableness of the business plan**
  - The listing applicant has developed reasonable and suitable business plans, and has developed the operating base necessary for executing such business plans, or there is reasonable expectation that it will develop such operating base
- 5 Other matters deemed necessary by the Exchange from the viewpoint of the public interest or the protection of investors**
  - a. Shareholders’ rights and exercise of such rights are not unduly restricted.
  - b. Relationship with a parent company is deemed appropriate.
  - c. Other matters are deemed appropriate in light of public interest and investor protection.

# Listing Fees to Tokyo Stock Exchange

## Fees for Initial Listing on TSE

	When TSE is the main market		When TSE is not the main market	Mothers	JASDAQ
	First Section	Second Section	First & Second Sections		
<b>Listing Examination Fee</b>	US\$ 40,000		US\$ 20,000	US\$ 20,000	US\$ 20,000
<b>Initial Listing Fee</b>	US\$ 150,000	US\$ 120,000	US\$ 25,000 + Fixed rate fee (See below)	US\$ 10,000	US\$ 60,000
<b>Public Offering/Sales Fee</b>	Number of new shares offered $\times$ offer price $\times$ (9/10,000) Number of existing shares sold $\times$ sales price $\times$ (1/10,000)		—	Number of new shares offered $\times$ offer price $\times$ (9/10,000) Number of existing shares sold $\times$ sales price $\times$ (1/10,000)	—

Note:

- 1 US\$ = 100JPY
- 2 Furthermore, in cases where an applicant previously filed a listing application or preliminary application and the applicant intends to file a re-application within three years counting from the beginning of the business year to which the most recent application date belongs (in case of the preliminary application, the date which was described in the preliminary application form for listing of securities as the date on which the listing application was expected to be filed), the listing fees is expected to be halved.
- 3 When TSE implements a on-site visit or meeting, etc. at locations remote from Japan, in particular including Europe, the US, and so on, TSE will separately charge the applicant the amount equivalent to actual expenses incurred for the on-site visit and meeting purposes.

## Initial Listing Fee for Foreign Stock, etc. with a Main Market Listing on any Overseas Exchange

Initial listing fee for foreign stock, etc. with a main market listing on any overseas exchange is computed as JPY2.5 million plus a fixed rate fee as shown in the table below:

Ratio of number of foreign stock, etc. held by individuals and legal entities having address and residence in Japan to the total number of listed foreign stock, etc.	Initial Listing Fee
More than 5%	US\$ 25,000 + Number of Listed Foreign Stock, etc. $\times$ (225/10 <sup>6</sup> ) $\times$ 1/10
More than 2% and less than or equal to 5%	US\$ 25,000 + Number of Listed Foreign Stock, etc. $\times$ (225/10 <sup>6</sup> ) $\times$ 1/20
Less than or equal to 2%	US\$ 25,000 + Number of Listed Foreign Stock, etc. $\times$ (225/10 <sup>6</sup> ) $\times$ 1/50

Note:

- 1 US\$ = 100JPY

# List of TSE-listed Foreign Companies

**Asian companies on TSE include those based in Korea, Malaysia, and China.**  
**U.S. drug development companies, MediciNova and Acucela, had successful IPOs on TSE.**

Region	Country	Ticker	Issue name	Market	Sector	Stock / DR	English Disclosure	Accounting standard	Multiple /Single
Asia	S. Korea	5412	POSCO	TSE 1st	Iron & Steel	ADR	-	K-IFRS	Multiple
	Malaysia	1773	YTL Corporation Berhad	TSE 1st	Construction	Stock	-	Malaysia GAAP	Multiple
	The Cayman Islands	9399	Xinhua Holdings Limited	TSE 2nd	Information & Communication	Stock	-	JGAAP	Single
North America	US	4850	THE DOW CHEMICAL COMPANY	TSE 1st	Chemicals	Stock	-	US GAAP	Multiple
	US	8648	Bank of America Corporation	TSE 1st	Banks	Stock	-	US GAAP	Multiple
	US	8685	American International Group, Inc.	TSE 1st	Insurance	Stock	Conducting	US GAAP	Multiple
	US	8686	Aflac Incorporated	TSE 1st	Insurance	Stock	-	US GAAP	Multiple
	US	8710	Citigroup Inc.	TSE 1st	Banks	Stock	Conducting	US GAAP	Multiple
	US	4589	Acucela Inc.	Mothers	Pharmaceuticals	Stock	-	US GAAP	Single
	US	4875	MediciNova, Inc.	JQ	Pharmaceuticals	Stock	-	US GAAP	Multiple (IPO)



1. Japan-Mongolia Relations

2. Comparison among Major Stock Markets

3. Expansion of IPO Market in Japan

4. Features of IPO Market in Japan

5. Listing on Tokyo Stock Exchange

### **A. TOKYO PRO Market**

B. Overview of the Japanese Financial Market

# History of TOKYO PRO Market

Year	Summary	Number of J-Adviser	Number of Listing Companies
2009	<b><u>(Jun) Launch of "TOKYO AIM"</u></b> (Jun) Admission of J-Nomad (Current J-Adviser)	6 (+6)	0
2011	(Jun) Admission of J-Adviser: <b>Phillip Securities</b> (Jul) <b>Mebio Pharm</b> (Tokyo) Listed on TOKYO AIM (J-A: Phillip) <u>*Mebio delisted in 2013.</u>	7 (+1)	1 (+1)
2012	<b><u>(Mar) TSE acquired the remaining 49% in TOKYO AIM held by London Stock Exchange</u></b> (May) <b>GOYO foods Industry</b> (Fukuoka) Listed on TOKYO AIM (J-A: Phillip) <b><u>(Jul) Integrate "TOKYO AIM" in TSE's Market and launch of "TOKYO PRO Market"</u></b> (Sep) Shintokyo Group (Chiba) Listed on TPM (J-A: Phillip) (Nov) Admission of J-Adviser: <b>OKINAWA J-Adviser</b>	8 (+1)	3 (+2)
2013	(Jun) <b>HEKI</b> (Okinawa) Listed on TPM (J-A: OKINAWA) (Jul) <b>HABITA CRAFT</b> (Gunma) listed on TPM (J-A: Phillip) (Sep) <b>Ad Me Tech</b> (Ehime) listed on TPM (J-A: Phillip) (Oct) <b>Eco Green</b> (Tokyo) listed on TPM (J-A: Phillip)	7社 (-1)	6 (+3)
2014	(Jul) <b>CHUOU INTERNATIONAL GROUP</b> (Saga) listed on TPM (J-A:OKINAWA) (Jul) <b>HAKATA TAKUMI KOUGEI</b> (Fukuoka) listed on TPM (J-A: Phillip) (Aug) Admission of J-Adviser: <b>Leading Securities</b> (Oct) <b>E-COMETRUE</b> (Hokkaido) listed on TPM (J-A: Phillip)	8 (+1)	9 (+3)
2015	(Jan) <b>Simplex Financial Holdings</b> (Tokyo) listed on TPM (J-A:OKINAWA) (Mar) <b>TSON</b> (Nagoya) listed on TPM (J-A: Phillip)	8 (+1)	11 (+2)

Note: As of March 31, 2015

© 2015 Japan Exchange Group, Inc. and/or its affiliates. All rights reserved.

# Main Features of TOKYO PRO Market

## Professional Investors

**TOKYO PRO Market prohibits stock buying by general investors excluding "professional investors" and non-residents in Japan.**

## J-Adviser

**A J-Adviser investigates/confirms the listing eligibility of a company before listing instead of TSE. Also A J-Adviser supports timely disclosure after listing, and examines the status of compliance with requirements to maintain a listing.**

## Flexible Listing Requirements

**No set requirements for Minimum shareholders, Profit, Market capitalization etc. unlike the other markets.  
Listing Criteria judged by J-Adviser .**

## English Disclosure

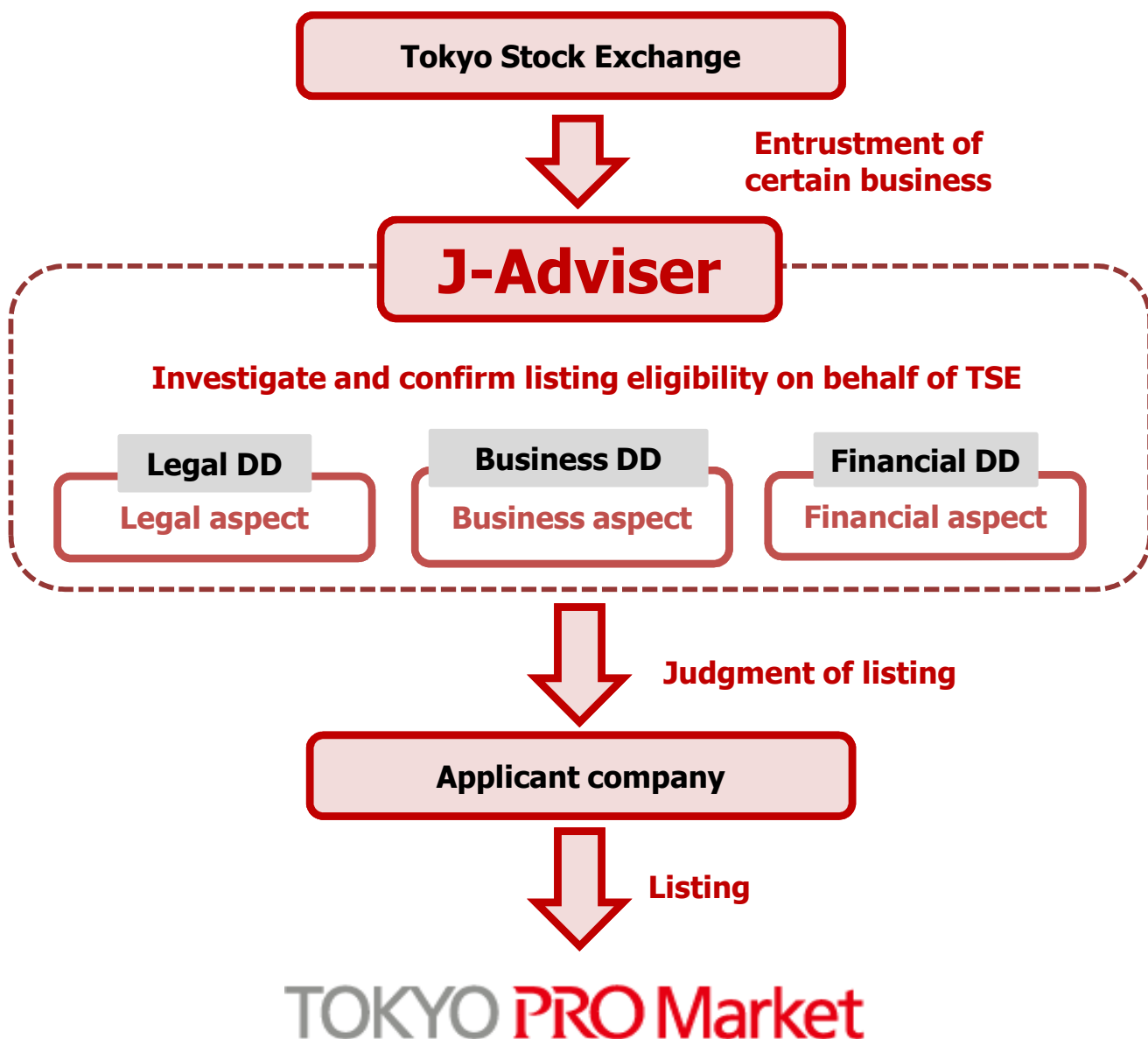
**Timely Disclosure materials and fiscal documents to be submitted to TSE can be prepared not only in Japanese but also in English.**



# Investors who can trade in TOKYO PRO Market

Investor Segment	Example	Buy in TPM	Sell in TSE
Specified Investors	Qualified institutional investor (financial institutions, etc.), national government, Bank of Japan	Possible	Possible
Specified investor (transferrable to general investor)	Listed company, stock company with capital of 500 million yen and more	Possible	
General Investor (transferrable to specified investor)	<u>Stock company other than a specified investor</u> Individual with financial assets or net assets worth 300 million yen and more	Possible (In case of transferring to Specified Investors)	
Non-resident	Individual who does not have an address or residence in Japan, corporation that does not have a principal place of business in Japan	Possible	
General Investor	Investors except the above investors	Impossible	

# J-Adviser System



## J-Adviser System

### ■ Role

- Company must retain a J-Adviser while listed on TOKYO PRO Market
- J-Adviser must evaluate the company and declare to the exchange that it is suitable for listing
- J-Adviser will continue to support and evaluate the company for the entire period it is on TOKYO PRO Market

### ■ Requirement

- J-Advisers are firms that have proven track record in corporate finance/IPO and have staff with expertise in respective areas (Majority of J-Advisers will be security firms)

## Current J-Nomads (alphabetical order)

- Daiwa Securities
  - Leading Securities
  - Mitsubishi UFJ Morgan Stanley Securities
  - Mizuho Securities
  - Nomura Securities
  - OKINAWA J-Adviser
  - Phillip Securities Japan
  - SMBC Nikko Securities
- (As of 31 Mar, 2015)

# Summary of Listing Requirements

	Other Markets in Japan	<b>TOKYO PRO Market</b>
<b>Disclosure</b>	Japanese	<b>Japanese or English</b>
<b>Accounting Standards</b>	Japan GAAP, IFRS (If the company has not disclosed financial statements in another country before)	<ul style="list-style-type: none"> <li>• <b>Japan GAAP</b></li> <li>• <b>IFRS</b></li> <li>• <b>US GAAP</b></li> <li>• <b>Other standards approved by J-Adviser or accountant</b></li> </ul>
<b>Listing Criteria</b>	Minimum shareholders, free float, profit, market capitalization, etc.	<b>No set requirements</b> <b>*Criteria judged by J-Adviser</b>
<b>Application Period</b>	2 - 4 months	<b>Minimum 10 business days</b> <b>* J-Adviser expresses intent for a listing application within about 30 business days prior to the actual listing application</b>
<b>Auditor's report</b>	The 2 most recent fiscal years	<b>The previous fiscal year only</b>
<b>Internal control reports</b>	Required	<b>Not required</b>
<b>Quarterly reports</b>	Required	<b>Not required</b>
<b>Investors</b>	No restrictions	<b>Professional investors and non-residents</b>

# Listing Eligibility Requirements

**The supervising J-Adviser investigates and confirms the listing eligibility of the applicant company based on the eligibility requirements specified by TSE in its regulations.**

## **(Listing Eligibility Requirements)**

**An initial listing applicant must satisfy the matters enumerated in each of the following items.**

- (1) An initial listing applicant does not damage the reputation of the market of the Exchange and is a company that is suitable for listing on such market.**
- (2) An initial listing applicant conducts business fairly and in good faith.**
- (3) The corporate governance and internal management structure of an initial listing applicant is appropriately developed in accordance with corporate scale and maturity, etc. and functions properly.**
- (4) An initial listing applicant carries out disclosure of corporate content and risk information, etc. appropriately and has developed a system and framework which enables it to fulfill its disclosure obligations based on the Special Regulations.**
- (5) No relations with anti-social forces and other matters deemed necessary by the Exchange from the perspective of the public interest and investor protection.**



1. Japan-Mongolia Relations

2. Comparison among Major Stock Markets

3. Expansion of IPO Market in Japan

4. Features of IPO Market in Japan

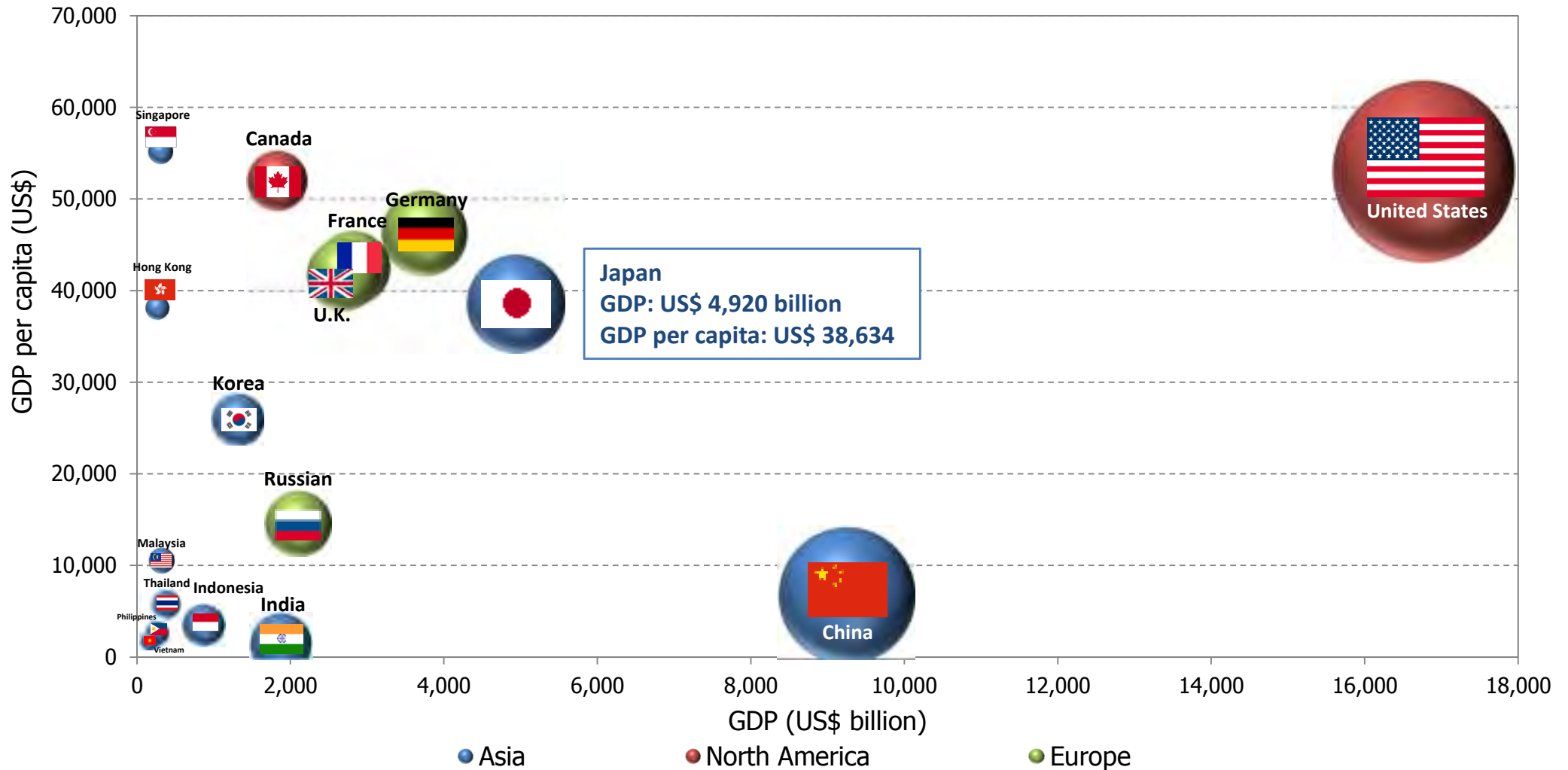
5. Listing on Tokyo Stock Exchange

A. TOKYO PRO Market

**B. Overview of the Japanese Financial Market**

# GDP and GDP per capita (2013)

Japan is a leading global economy with world-class GDP and per capita GDP.



Source: World Bank

Note: Circle size indicates relative GDP

# Deep and Diverse Investor Base

**Participation by various types of investors in the TSE market creates fair and reliable valuations of its listed companies.**

## **1 The World's Largest Institutional Investor**

- Japan is the primary investment focus for the Government Pension Investment Fund, Japan (GPIF), the largest institutional investor in the world.
- Assets under management at GPIF was valued at US\$1.3 trillion<sup>1</sup> (Sep. 2014), an amount comparable to the GDP of South Korea (US\$ 1.3 trillion, 2013). GPIF's investments in foreign stocks accounted for 17.41% of its entire portfolio, an amount valued at US\$228 billion<sup>1</sup> (Sep. 2014).
- There are also other pension funds that manage huge amounts of funds.

## **2 High Net Worth Individuals**

- Financial assets held by Japanese individuals stood at US\$15.68 trillion at the end of 2013<sup>1</sup>.
- This is comparable to 2.6 times Japan's GDP (US\$5.96 trillion, 2012 year end).

## **3 Accessibility to Japanese Markets for International Investors**

- Foreign investors are the largest players in Japan. The increase in investments by foreign investors can be seen from their trading value, which reached US\$6.5 trillion<sup>1, 2</sup> in 2013.
- Globally reputable investors from many countries have shown interest in the Tokyo market. A TSE listing promises a company access to investment by international investors.

Source: GPIF web site, BOJ, World Bank

Note: 1 US\$= 100 JPY

2 Total amount of buy and sell

# Top 12 Pension Funds

**GPIF (Government Pension Investment Fund) is the largest investor in the world.**

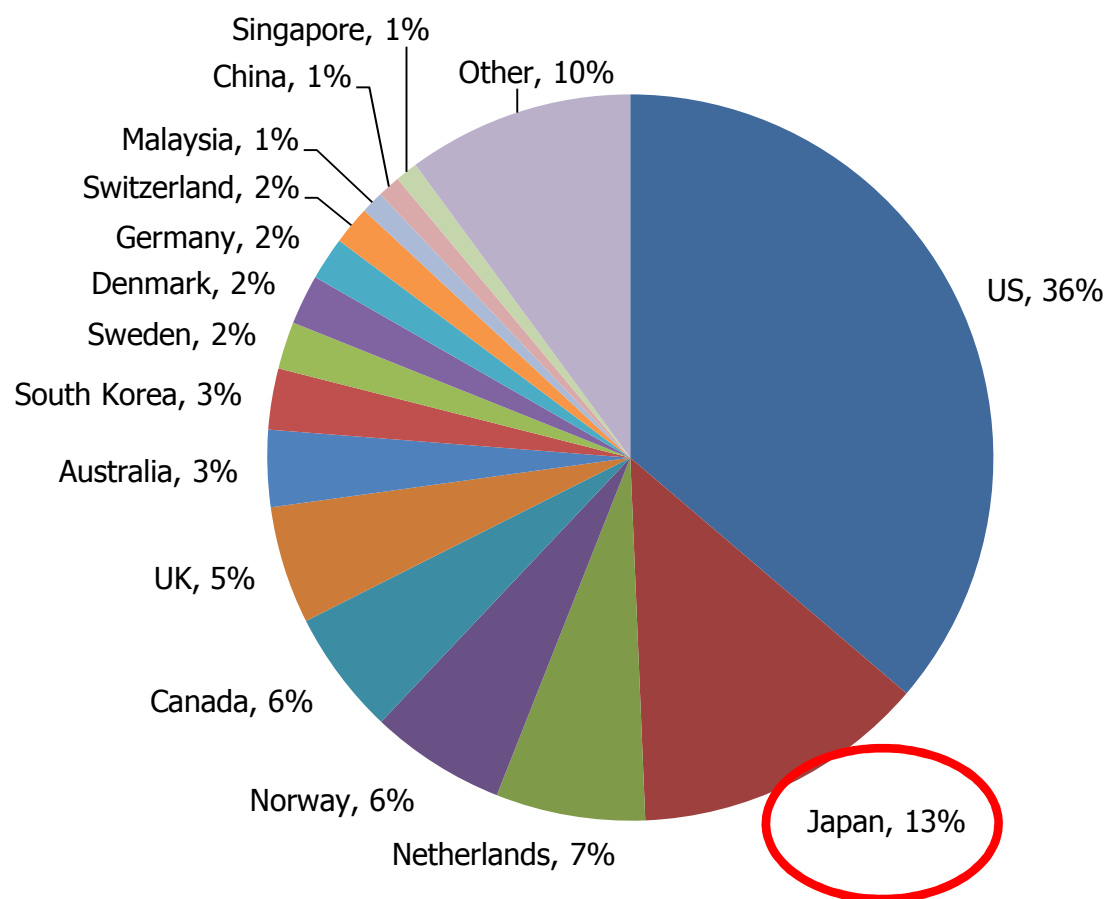
Rank	Fund	Market	Total Asset (US\$ billion)
1	<b>Government Pension Investment</b>	<b>Japan</b>	<b>1,292</b>
2	Government Pension Fund	Norway	713
3	ABP	Netherlands	373
4	National Pension	South Korea	368
5	Federal Retirement Thrift	U.S.	326
6	California Public Employees	U.S.	245
7	Canada Pension	Canada	206
8	National Social Security	China	205
9	Central Provident Fund	Singapore	200
10	PFZW	Netherlands	197
11	Employees Provident Fund	Malaysia	182
12	<b>Local Government OfficialsJapan\$</b>	<b>Japan</b>	<b>180</b>

Source: P&I / TW Top 300 Pension Funds Analysis as at 2013 year end



# Total Value of Fund Assets

## Total Value of Fund Assets (Split by fund domicile)

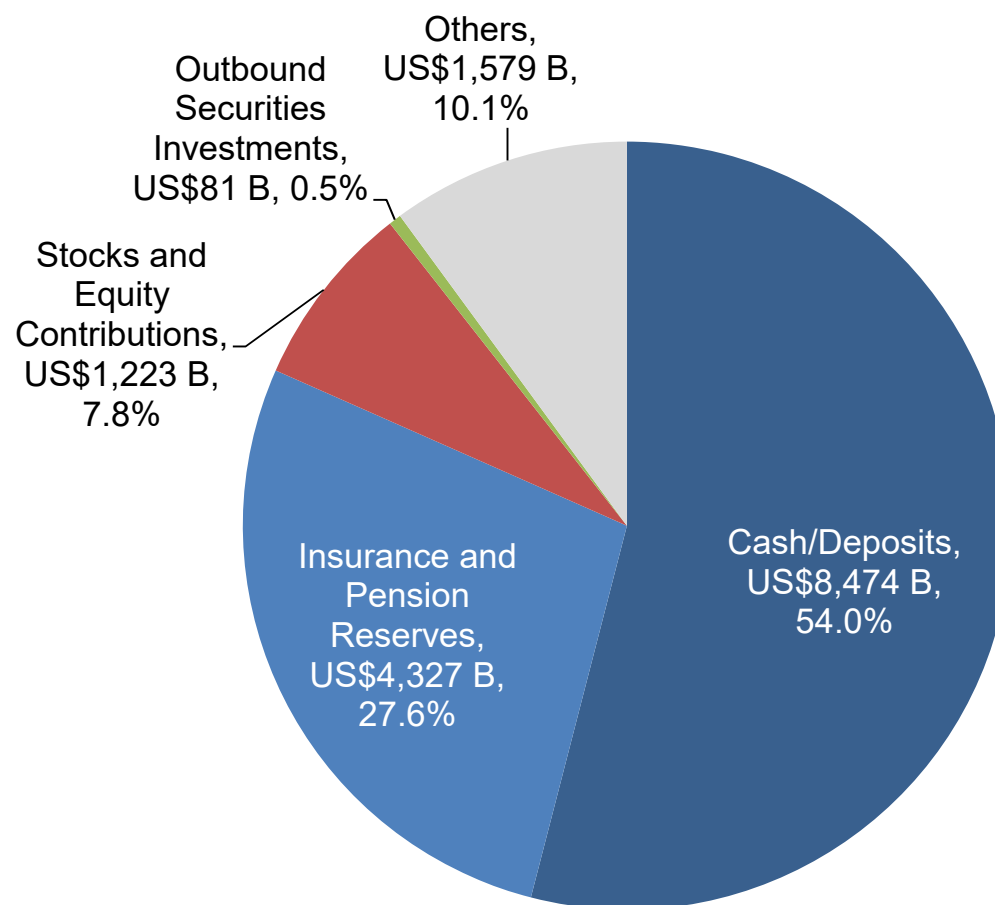


#	Country	% of Total Value	No. funds
1	US	36%	126
2	Japan	13%	14
3	Netherlands	7%	13
4	Norway	6%	1
5	Canada	6%	19
6	UK	5%	26
7	Australia	3%	16
8	South Korea	3%	3
9	Sweden	2%	7
10	Denmark	2%	8
11	Germany	2%	12
12	Switzerland	2%	10
13	Malaysia	1%	2
14	China	1%	1
15	Singapore	1%	1
16	Other	10%	41
Total		100%	300

Source: P&I / TW Top 300 Pension Funds Analysis as at 2013 year end

# High Net Worth Individuals

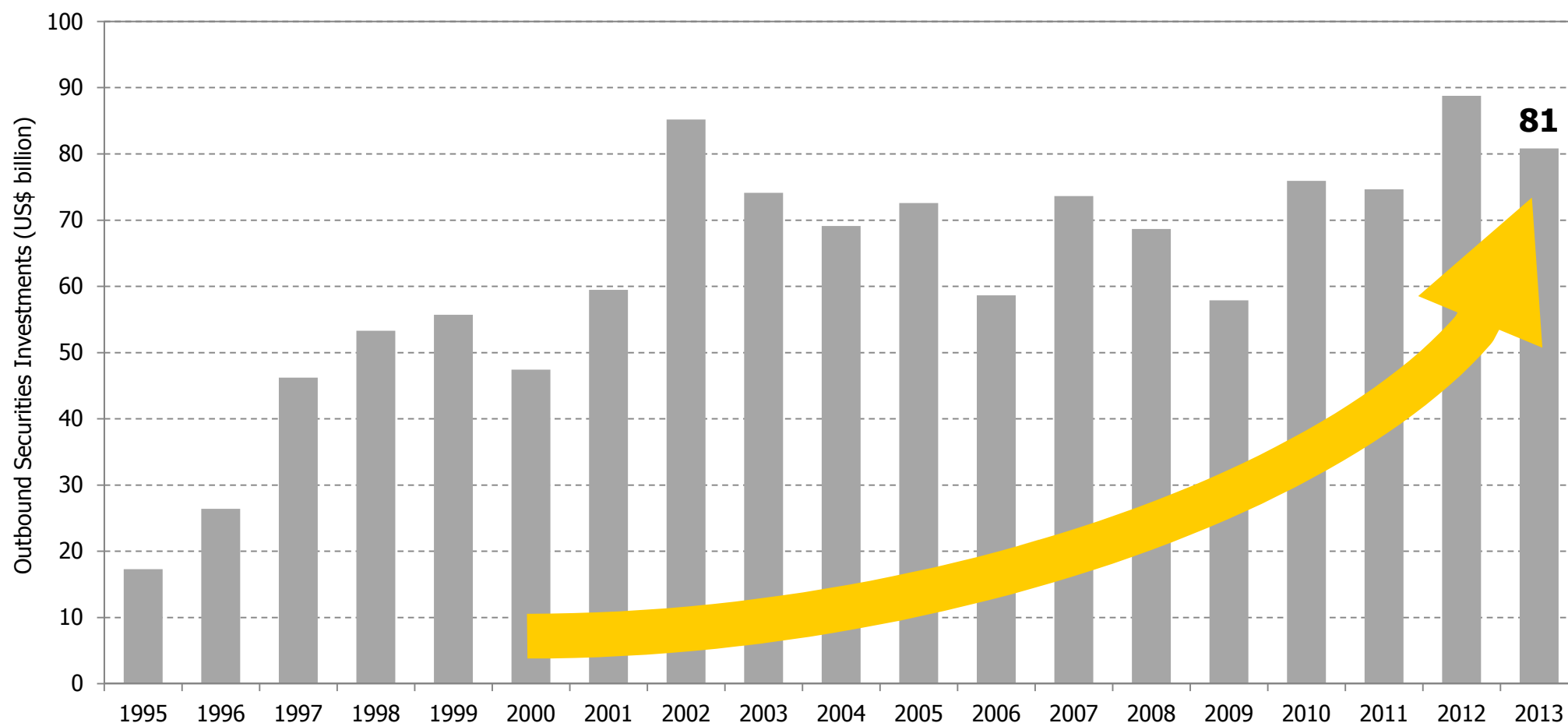
**Financial assets held by Japanese individuals stood at US\$15.68 trillion at the end of 2013 and is comparable to 2.6 times of Japan's GDP. This is a very high level worldwide.**



Source: Bank of Japan  
Note: US\$ = JPY 100

# Outbound Securities Investments

**The value of outbound securities investments from household assets by Japanese individual investors shows a continued upward trend. Japanese investors also warmly welcome foreign stock listings on the TSE market.**



Source: Bank of Japan  
Note: US\$ = JPY 100

## 【Contact】

### **Toru Onoda (Mr.)**

General Manager, New Listings Dept.

### **Atsushi Joden (Mr.)**

Account Manager, New Listings Dept.

## 【Important Information】

- Please note that this presentation is for informational purposes only. Japan Exchange Group, Inc. and Tokyo Stock Exchange, Inc. are not responsible for any damage caused by using the information contained herein. Please also note that the information is not guaranteed to be complete, correct, or up-to-date, and may be changed without notice. Unauthorized copying, reproduction, republishing, uploading, posting, transmitting or duplicating any part of the material is prohibited.