



TSE Explanatory Material

*The Second Council of Experts Concerning
the Follow-up of Market Restructuring*

Exchange & beyond

Tokyo Stock Exchange, Inc.

September 9, 2022

Discussion at the Last Council

Objectives

- **The main objective is to support and promote the benefits of capital markets in Japan** by helping listed companies increase their corporate value, which will lead to listed companies becoming more active, increased international competitiveness, higher wages, and enhanced pension assets.
- The new capitalism advocated by the Kishida administration aims for **financial inclusion**. Specifically, it aims to create a society where no one is left behind financially, and a brand of mass capitalism where the benefits of financial markets are widely available to the people, who are the major shareholders. Since **TSE plays a major role in this process, TSE should speedily implement reforms**.
- The market restructuring is **an important initiative to improve corporate value of listed companies over the medium- to long-term, and to increase international competitiveness and attractiveness as a market**. This review is the first step, and **sustained efforts are needed in order to make it an opportunity for reform**.
- The goal of the market restructuring is to **encourage the improvement of corporate value. TSE has already put forth measures in line with this, and we must think about how they can be accomplished**.

Procedures

- **Setting a proper agenda** is essential for effective discussions.
- After discussing what the market and listed companies should ideally look like in the future, we should **present a roadmap** for achieving this.
- As a whole, discussions and initiatives should be conducted with **a sense of urgency**.
- The opinions of listed companies and market participants, including overseas investors, should be **carefully considered** and used in future initiatives.
- As we **ensure the transparency** of discussions through the publication of meeting minutes and the like, we should **actively distribute information** regarding the **main points and direction** of the discussions.
- It is worth considering establishing objective indicators for **periodically evaluating results**, such as market capitalization and market liquidity.
- Further, we must be careful not to **fall into micromanagement**, and rather **utilize the self-discipline of the market**.

⇒ We shall immediately begin **conducting stakeholder hearings and holding a public consultation**, as described below, to **quickly summarize issues that require follow-up and the need for additional measures** and the like.

■ Stakeholder Hearings

Fidelity Investment Trust and JPX Market Innovation & Research join this second council as guest speakers.

We will continue to conduct stakeholder hearings at the third and subsequent meetings.

■ Public Consultation

TSE will hold a public consultation through its website (starting during September, expected to last for about one month).

Note: In order to **ensure transparency**, TSE will continue to **promptly release the minutes** of this and future meetings.

Discussion at the Last Council (Prime Market)

- **Nearly half of the companies have a PBR lower than 1.**
 - A PBR lower than 1 is a situation in which **management is not bothered about stock price or capital efficiency.**
 - One idea would be to require companies with a PBR lower than 1 to **publish a roadmap** of their efforts and **continue the PDCA cycle of dialogue and engagement with investors** regarding the roadmap's contents.
- Even though the Prime Market is for companies committed to dialogue with global investors, **English disclosure practices are inadequate** and the **ratio of foreign investors in the market is low.**
 - Regardless of market capitalization, **English disclosure practices should improve at the very least.**
- Issues such as capital efficiency should be resolved through dialogue with investors, but **only a small number of investors are engaging in dialogue.**
 - It is essential that **asset owners** including corporate pension funds **actively participate in such dialogue.**

Discussion at the Last Council (Standard Market)

- The **positioning of the Standard Market is ambiguous** compared to that of the other two market segments.
 - It is necessary to **discuss what can be done to revitalize the Standard Market while looking at what is actually happening** within the market segment. One idea is to promote public relations and branding by **communicating the advantages of the Standard Market and the changes within the listed companies.**
 - Even if **the management approach is different from the global standard** adopted by companies in the Prime Market, **it is fine as long as the company can achieve decent results** in ROE and PBR.
 - It is important to **demand a solid level of governance**, not in terms of formality, but in terms of **the quality of dialogue.**
 - **English disclosure** is also important in order to increase PBR, as it is essential in order to be evaluated by domestic and foreign investors.

⇒ At the last council, members listed **issues on which to follow up**, focusing on **market valuation, profitability, English disclosure practices, and participants that engage in dialogue for the Prime Market, and the positioning of the Standard Market.**

⇒ We would like to **deepen our discussions on these issues and the need for additional measures while conducting hearings with domestic and foreign institutional investors and holding a public consultation for stakeholders.**

Discussion at the Last Council

Realization of High Growth Potential after Listing

- The Growth Market is expected to play a role in nurturing companies that will become pillars of Japanese industry in the future. Some companies succeed and others fail as a result of aggressive risk-taking, so an unchanging median market capitalization is not necessarily a problem. However, **the fact that only a small number of companies have achieved significant growth is problematic.**
 - Compared to the U.S., there is a **lack of investment for growth**. We should **work to increase market capitalization while encouraging investment for growth**.
 - The problem here is that **companies that have failed to grow remain listed on the Growth Market**. It is crucial for there to be **regeneration and for those companies to leave the market**.
- Since many companies in the Growth Market have high business risk, **information disclosure is essential** for attracting risk capital, such as investments made by institutional investors.
 - It is necessary to check listed companies' business plans and other information which they disclose in terms of **whether that information is sufficient for investors to make investment decisions**.
 - TSE should instill a **more proactive stance on early disclosure** regarding matters for which investors may have concerns, beyond the standards for timely disclosure.

Functioning as an IPO Market

- There is **not enough participation from institutional investors**, as the companies are small in size. Measures should be taken to address this.
- It is **important to create an environment that supports the growth of startup companies in general by developing a secondary market for unlisted stocks**, rather than rushing them to go public.

⇒ At the last Council meeting, members listed **issues on which to follow up**, focusing on **achieving high growth potential, information disclosure practices, and participation from institutional investors in the Growth Market**.

⇒ We would like to **deepen our discussions on these issues and the need for additional measures** while conducting **hearings with venture capital firms and other stakeholders** related to startup companies and **holding a public consultation for stakeholders**.

Detailed Topics (Transitional Measures)

Discussion at the Last Council

Handling of the Transitional Measures

- It is important to **promptly determine and clarify our policies for handling the transitional measures to make things more foreseeable for listed companies.**

(Specific Opinions on the Handling)

- **The transitional measures should be terminated as soon as possible anyway, as they will make the continued listing criteria meaningless.**
- It is **important for each company to firmly adhere to the commitments** made in the plan, and **extensions of the originally disclosed deadlines should not be allowed.**
- Another option would be **a two-step approach with an interim target of 2025**, for example, rather than prohibiting companies from renewing their plans from the beginning.
- Considering how the planning periods have been structured, it is appropriate to **draw the line around 5 years following transition (2027).**

- **The effectiveness of these plans is important**, so in order to properly evaluate them, **their progress should be disclosed appropriately.**

⇒ Regarding the transitional measures, which are currently set as "for the time being", **a policy on the handling of such measures, including a termination date, must be promptly set forth** in order to make things more foreseeable for listed companies and appropriately realize the concept of each market segment.

⇒ We would like to **deepen our discussions on the handling of these measures while conducting hearings to ascertain the actual status of companies and holding a public consultation for stakeholders.**

Discussion at the Last Council

Impact on Shareholders upon Delisting

- Stricter rules should not end up disadvantaging shareholders. Therefore, in the unlikely event that a company is delisted, we must be keenly aware of shareholder protections. It is essential that we discuss carefully with sufficient awareness of this point.
- Given that companies under the transitional measures are already a drop down in quality from normal listed companies, a secondary trading venue for delisted companies would be an even further drop down from there and a pointless addition. This issue is directly connected to the market restructuring and therefore **should be discussed at this Council.**

⇒ With regard to delisting upon the termination of transitional measures, the Final Report by the Expert Study Group on Capital Markets in Japan of the Financial System Council states "Once the strict delisting criteria are applied, securing opportunity for investors to sell their shares to be delisted is necessary. Therefore, when considering tightening the delisting criteria, it is also necessary to consider developing secondary markets which seamlessly function as alternative, secondary venues of trading for these investors."

⇒ TSE foresees that it will **conduct a practical study on a specific framework for securing opportunities for shareholders to sell their shares of companies to be delisted** so that measures can be put in place **before any companies are delisted due to the termination of the transitional measures, at the very latest.**

- For example, **the current designation period for Securities to Be Delisted could be extended** to ensure sufficient selling opportunities for shareholders, or **a market segment could be established for stocks delisted from the regular market segments for a limited period, such as one year, for liquidation trading.**

Discussion at the Last Council

- It is **important to encourage competition among listed companies to join TOPIX**, after the end of the transition period in January 2025. We must consider raising the current inclusion criteria of JPY 10 billion in tradable share market capitalization and periodically replacing constituent stocks.
- Foreign investors seem to be confused when investing in Japan, as to whether to invest in TOPIX or the Prime Index. Therefore, it is also important to **appeal index strategies to foreign investors**.
- In order to solve the issue of low liquidity in the Growth Market, it may be possible to engage in **marketing activities and devise ways** to lead investment trusts and other investors to utilize **Growth Market indices** more.