

Tokyo Stock Exchange

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The world's financial markets have changed immensely in the past year, and will certainly continue to change in 2005 and beyond. Cooperation between markets is on the rise, new capital markets are emerging, and regulations and procedures are constantly in flux to deal with these increasing shifts.

Within this environment, Tokyo Stock Exchange (TSE) aims to be an innovative market that can survive increasing global competition. One way of doing this is by securing our international position. TSE strives to be a true "Global Financial Exchange" with significant international presence by providing domestic and international investors, issuers and intermediaries with a market that has a high level of integrity and abundant liquidity.

To consolidate TSE's international position as the central market for Japanese financial products, our top priority is strengthening the functions of our market and increasing our international competitive advantage in Japanese stocks, the core products of our cash market, and long-term Japanese Government Bond futures and TOPIX futures, which form the cornerstone of our derivatives market.

Our markets cannot grow on image alone. This year at TSE we intend to promptly and steadily carry out the following measures in order to make our market even more user-friendly and accessible.

First, we will facilitate the listing of attractive, high

quality companies for investment on our First Section and Second Section, and will develop 'Mothers' by providing unlisted companies with full support in their preparation for listing.

TSE will also increase the attractiveness of listed stock by improving corporate governance and disclosure regulations. We aim to further increase the fairness of our market by strengthening market surveillance and inspection of participants.

Thirdly, we will operate our market with a greater emphasis on the fundamental importance that fair corporate management from an investor point of view and timely and appropriate corporate information disclosure have in constituting a base for trust in the securities market. TSE plans to swiftly implement the revisions we announced last year to our listing system while making efforts toward enhancing timely and appropriate information disclosure. We will also conduct various activities to promote improvements in corporate governance practices as well as encourage listed companies to implement management methods that take full account of the securities market and investors.

As an effort to strengthen TSE's international role as a place to raise capital and manage assets we actively promote the listing of foreign companies, especially from the Asian region. TSE is also committed to reviewing business conduct and procedural matters which may be obstructive to listing or raising of capital in Japan.

In FY2005 we plan to list our shares for trading on our own market in an organisational enhancement that will strengthen our market function and heighten international competitiveness. With the listing of our shares we aim to realise the high level of potential that becoming a stock corporation brings by further improving our management efficiency and gaining access to a diverse means to raise capital.

Various Products Offered

The TSE market consists of the cash market and derivatives market.

Listed cash market products include stocks, convertible bonds (CBs), Exchange Traded Funds (ETFs), real estate investment trusts (REITs), and straight bonds. TSE has some of the world's leading derivative products, key products including futures on the Tokyo Stock Price Index (TOPIX), the stock price index that most accurately reflect movements in the Japanese equity market, options on the index, as well as options on Japanese Government Bond (JGB) futures, and JGB futures, the most liquid product in Japan.

Beyond our dynamic market, TSE is home to the development and publishing of Japan's most comprehensive family of indices. TOPIX, the principle index consisting of all of TSE's First Section stocks, is widely used as a benchmark for Japanese stocks. Sub-indices include the TOPIX Core 30, TOPIX 100, and TOPIX 1000. TSE has also established indices for the Mothers and REIT markets, allowing investors to track movements in these exciting markets.

TSE's market attracts a wide variety of investors, with a significant portion of trading coming from overseas. In November 2004 overseas investors generated 37.7 per cent of TSE's trading value, while institutions made up 14.6 per cent and individuals 18.1 per cent.

The Japan Securities Dealers Association (JSDA) surveyed 265 trading participants and results showed that 53 participants, around 20 per cent, offered internet trading. The number of internet trading accounts was 5.81 million and this number continues to grow. The percentage of total trading carried out by brokers from internet orders has greatly increased and now stands at 25.4 per cent of all trading (as of September 2004).

Trading Platforms

All products listed on TSE are traded on an electronic trading platform. Our current system capacity is sophisticated enough to process even the highest amount of orders. However, with the aim of increasing convenience for investors, we will further increase the capabilities of the trading system in May 2005 so that it will be able to handle up to 6.2 million orders a day. The derivatives trading system already has a high capacity and can deal with 100,000 transactions a day.

TSE has measures in place to minimise possible adverse effects of natural disasters and other unexpected events. In response to such a disaster, based on the concepts of "Fault Tolerant" and "Hot Stand-by" TSE has the ability to directly switch systems. To further reduce the risk of system failure in the event of a disaster, we will be moving TSE's primary data center to a site which will have an even greater level of security.

Clearing and Settlement Systems

TSE introduced Delivery Versus Payment (DVP) settlement for its stock transactions in 2001. DVP settlement eliminates the risk that a member firm could impair other firms by failing to deliver funds after having received securities in the settlement process. By linking the receipt and payment of securities and funds, a member firm can only receive securities up to the amount that it has paid in securities funds. DVP settlement not only increased the efficiency and safety of TSE's market, but it also raised its settlement standards to that of global standards, thereby raising the global trust of its market.

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Settlement for securities trades executed on the TSE market happens on T+3 and settlement for derivatives transactions on a T+1 basis. Japan Securities Clearing Corporation (JSCC) acts as central counterparty to settlement, so that funds and securities are transferred between members (securities companies) and JSCC, not directly between the transacting members and/or customers. To streamline the whole process and to reduce the sheer volume of funds and securities that must be handled, settlement is done on a net basis, with only the difference between each member's sales and purchases changing hands.

In February of 2004 JSCC, the sole CCP for equities and fixed income products traded on all Japanese stock exchange markets, broadened its role so as to include trades conducted on TSE's derivatives market. JSCC began operations in January of 2003. JSCC assumes the rights and obligations of trades executed on each of the six exchanges and markets in Japan as a central counterparty and guarantees finality of settlement. JSCC offsets the rights and obligations assumed, and sends the results of netting and settlement instructions to clearing participants and settlement organizations respectively.

Market Integrity and Risk Measurements

TSE's self regulatory function has become our symbol of quality and is essential in maintaining fairness and trust of our market.

Market surveillance is carried out on a real-time basis through computer trading systems and completed transactions are carefully monitored in order to keep trading in line with Exchange rules and properly determined prices.

TSE is also proactive in monitoring trading that overlaps between the cash and derivatives markets.

TSE also monitors positions on derivative products in real time. Also, using the Standard Portfolio Analysis of Risk (SPAN) for risk control, TSE requires traders to have margin with accordance to their liabilities to cover sudden changes in the market.

TSE aggressively undertakes investigations of unfair trading and issues warnings to trading participants whose actions risk potential violations of relevant laws.

Investor Protection Methods

In Japan, company and customer assets must be separate by law. Securities firms in Japan must be also affiliated to either the Japan Investor-Protection Fund or the Securities Investor Fund.

TSE continuously monitors listed companies and securities in order to maintain high listing standards. TSE can suspend the trading of, or delist, a listed company if listing criteria are not met.

In order to ensure investor protection and fair and transparent transactions, TSE requires the accurate, swift, and fair disclosure of corporate information. Rules relating to the disclosure of corporate information are stated in the Securities and Exchange Law, and TSE maintains guidelines for the timely disclosure of important corporate information resulting from business activities. The TSE also provides a filing system which facilitates investor access to disclosure documents.

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