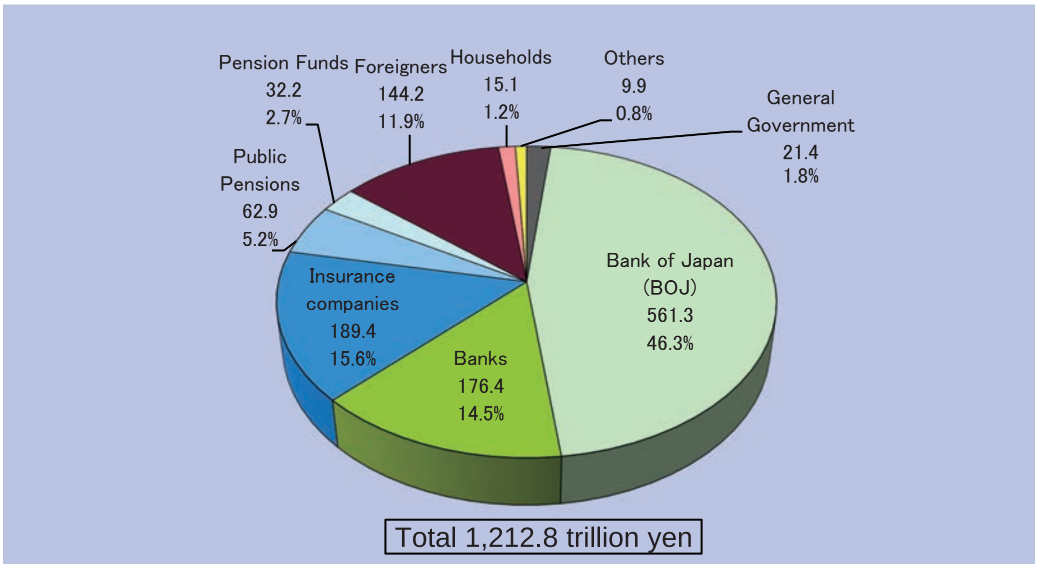
3 Diversification of JGB Investor Base

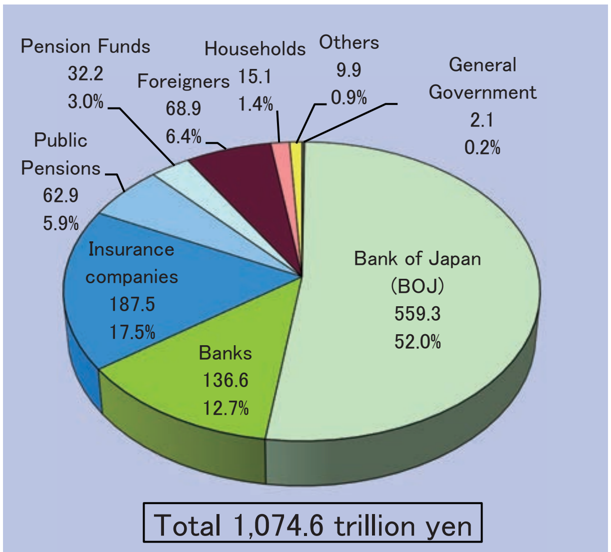
At present, the outstanding amount of JGBs is enormous. Therefore, the promotion of JGB holdings by a wide range of investors has become important for stabilizing the market's absorption of JGBs and their holdings. Diverse investors' JGB holdings based on various investment needs are expected to stabilize the market by preventing transactions from going in a single direction even if market conditions change. Therefore, the MOF has made efforts to encourage JGB market participation and JGB holdings not only by domestic institutional investors, such as banks and life insurance companies, but also by a wide range of investors, both domestic and foreign. This section explains the status of JGB holdings by both domestic and foreign investors, measures to promote holdings by domestic retail investors, and IR activities for both domestic and foreign investors.

Fig. 1-19 Breakdown by JGB and T-Bill Holders (December 2024, QE)



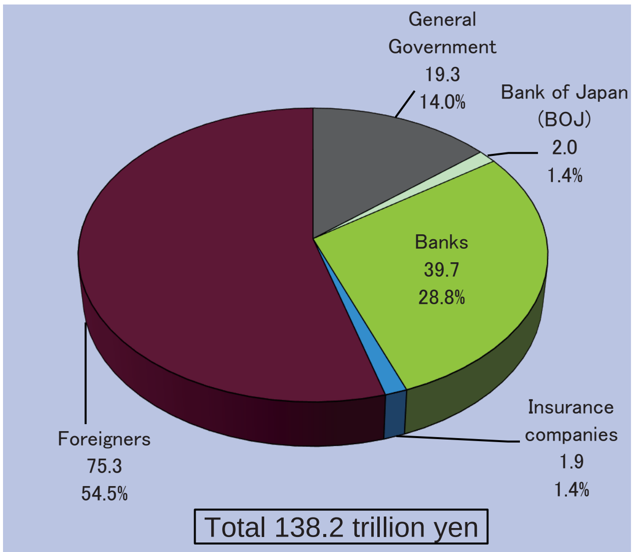
(Source) Bank of Japan "Flow of Funds Accounts" (Unit: trillion yen)

Fig. 1-20 Breakdown by JGB Holders (December 2024, QE)



(Source) Bank of Japan "Flow of Funds Accounts" (Unit: trillion yen)

Fig. 1-21 Breakdown by T-Bill Holders (December 2024, QE)



(Source) Bank of Japan "Flow of Funds Accounts" (Unit: trillion yen)

Note 1: "T-Bill" is the sum of "Treasury Bills (TBs)" and "Financial Bills (FBs)" with a maturity of 1 year or less. TBs and FBs have been jointly issued since February 2009.
Note 2: "JGB" in the figures represents the outstanding balance of JGBs (including FILP bonds) excluding TBs maturing within 1 year or less.
Note 3: "Banks" includes "Japan Post Bank," "Securities investment trusts," "Securities companies," etc
Note 4: "Insurance companies" includes "Life insurance," "Nonlife insurance," and "Mutual aid insurance."
Note 5: "General Government" excludes "Public Pensions."

(1) JGB Holdings by Retail Investors

Ref: II Chapter 1 2(2) “Methods of Issuance” (P58)

To promote JGB sales to retail investors, since the introduction of 10-Year Floating-Rate Bonds for Retail Investors in March 2003, we have introduced 5-Year Fixed-Rate Bonds for Retail Investors in January 2006, 3-Year Fixed-Rate Bonds for Retail Investors in July 2010, and launched the new Over-The-Counter(OTC) sales system in October 2007.

In FY 2024, due to the rise in market interest rates, the interest rates on JGBs for Retail Investors also increased, leading to a substantial increase in sales to approximately 4.5 trillion yen, and the outstanding balance of JGB holdings by households also increased.

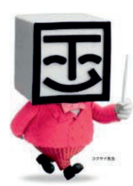
However, in the long term, the proportion of JGBs held by households remains at a low level.

In light of this situation, we are carrying out advertising campaigns aimed at expanding the medium- to long-term base of purchasers for JGBs for Retail Investors. In FY 2024, advertisements were implemented with the main target being the existing primary buyer demographic of those aged 50 and older, aimed at encouraging purchasing decisions. Additionally, advertising was rolled out to increase awareness and product understanding among the secondary target groups, which include the working generation and younger individuals.

Specifically, in addition to using the characters "Koko-chan for JGBs for Retail Investors” and "Kokusai Sensei" (JGB teacher), we employed celebrities for internet advertising (such as banner ads), social media and video advertisements, newspaper and magazine ads, transit advertising, and TV commercials. We also created and distributed posters and pamphlets and participated in events with booth displays. Additionally, we conducted region-specific advertising, seminars, and outreach classes in areas such as Aichi Prefecture and Okayama Prefecture.

In FY 2025, similar to FY 2024, we plan to emphasize the appeal of the product features of JGBs for Retail Investors and other related products in our advertising campaigns to encourage purchases.

<Kokusai Sensei>



<Kokochan>

Fig. 1-22 JGB Holdings by Households

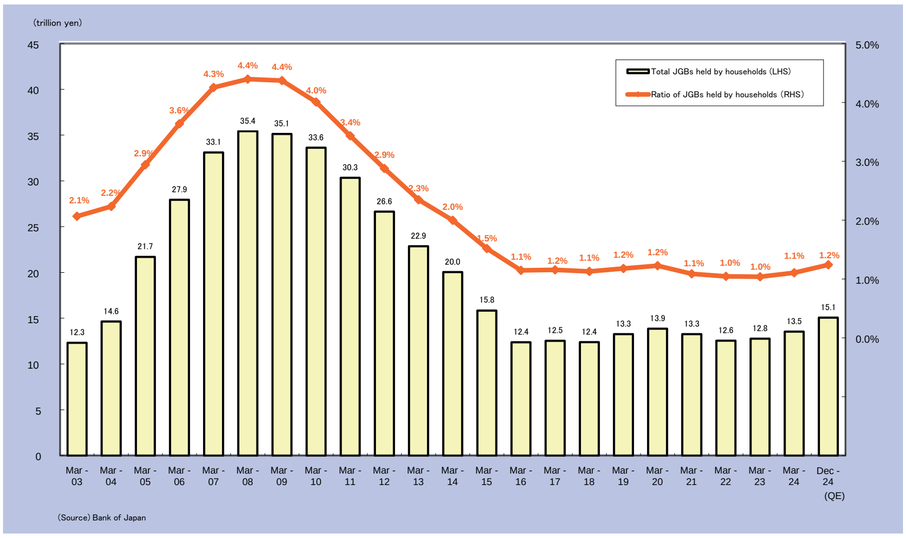


Fig. 1-23 Issuance and Redemption of JGBs for Retail Investors

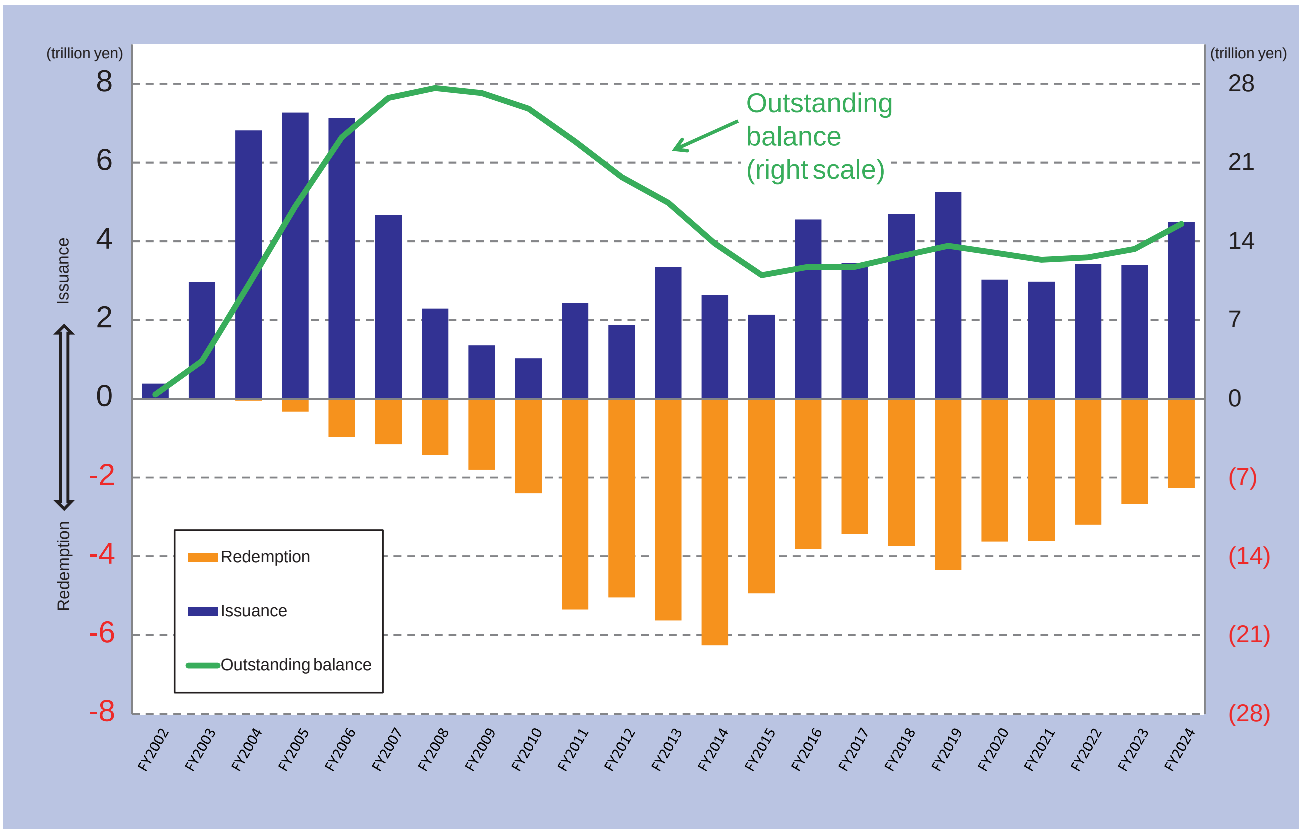
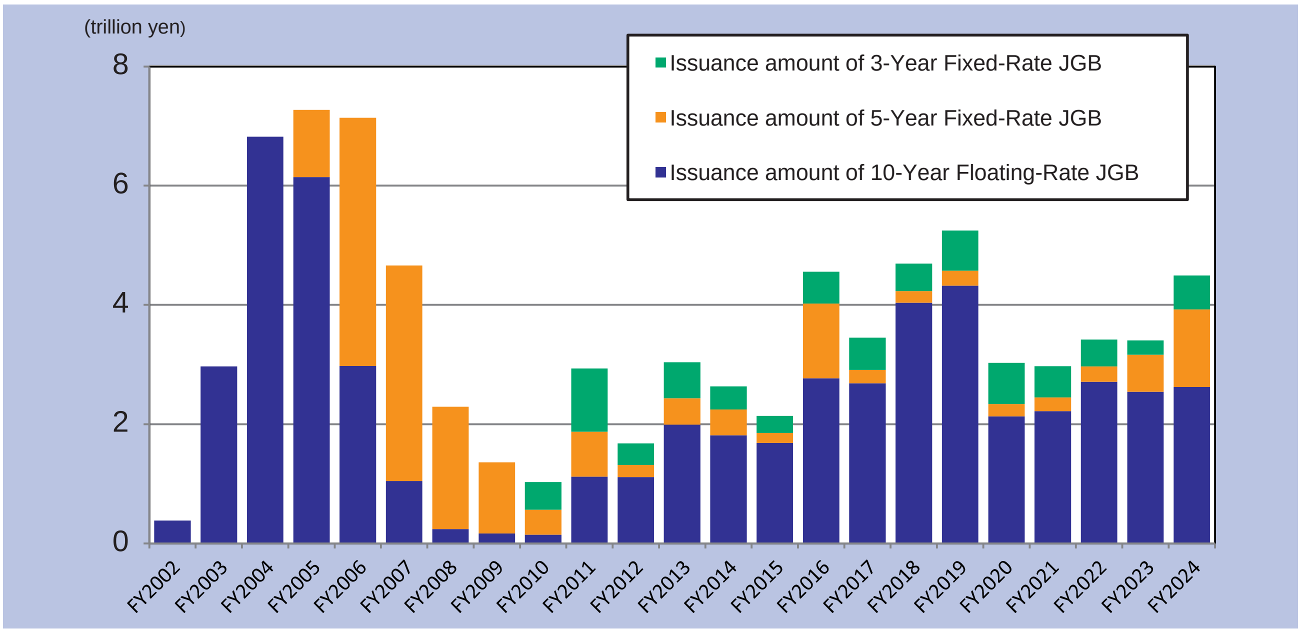


Fig. 1-24 Outstanding JGBs for Retail Investors



(2) JGB Holdings by Foreign Investors

A. Foreign Investors' Presence

The status of JGB holdings by foreign investors can be found in the "Flow-of-Funds Accounts" published by the BOJ on a quarterly basis (Fig. 1-25).

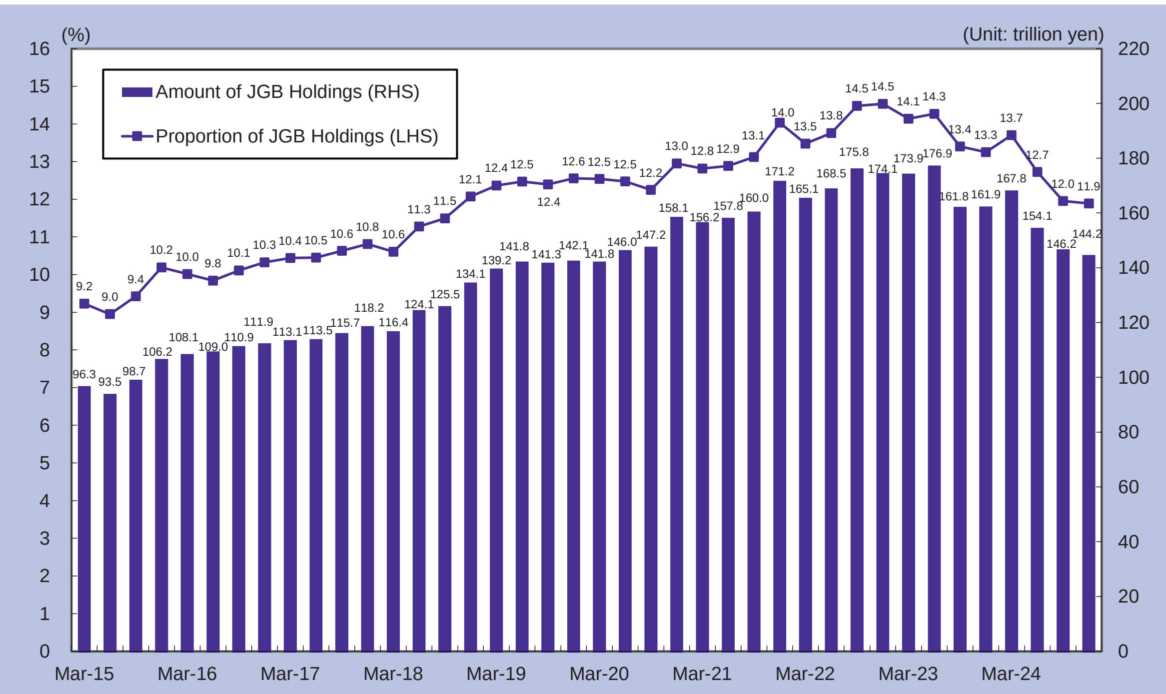
Foreign investors temporarily reduced JGB holdings as JGB volatility headed higher just after the BOJ's decision at its Monetary Policy Meeting in April 2013 to introduce the Quantitative and Qualitative Monetary Easing policy. Nevertheless, foreign investors' JGB holdings turned upward as JGB yields remained stable at low levels due to destabilization factors in emerging and other foreign countries.

In CY 2024, the investment trends of foreign investors showed a sell-off in government bonds at times, partly due to the interest rate increase following the BOJ's revision of its monetary policy framework in March 2024. However, for most of the period, there was a continued net purchase of bonds. Factors cited include continued investment in short- and medium-term bonds utilizing currency basis swaps and the ongoing need for short covering of long-term bonds. In response to the BOJ's additional interest rate hike in July 2024, domestic investors who had refrained from investing under negative interest rates resumed operations using Treasury Discount Bills (T-Bills). Combined with the reduction in the issuance amount of T-Bills, these factors led to a tightening in supply and demand. Consequently, the percentage of T-Bills held by foreign investors declined, especially in 2024. On the other hand, looking at medium- to long-term trends, as JGBs have looked attractive to foreign investors due to the low yen fundraising costs on the back of the tightening dollar supply-demand balance in recent years, their JGB holdings have remained stable. Some foreign investors hold JGBs in favor of their stable yield trends compared to those of other countries. At the end of December 2024, foreign investors' share of outstanding JGBs totaled 144.2 trillion yen, or 11.9%.

Foreign investors' JGB investment has featured a focus on T-Bills. At the end of December 2024, they held 6.4% of outstanding JGBs (excluding T-Bills) and 54.5% of T-Bills (Fig. 1-26). Foreign investors also feature their active trading on the secondary market. Their share of secondary market transactions at the end of December 2024 reached 48.2% for spot trading and 76.3% for futures trading (Fig. 1-27). Foreign investors' presence on the secondary market is greater than indicated by their JGB holdings. We should keep an eye on the presence of foreign investors.

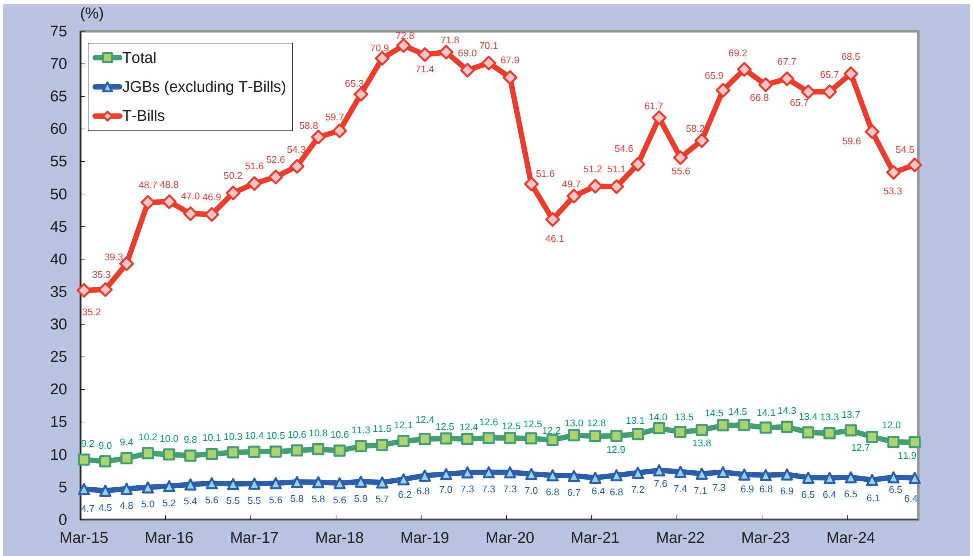
3 Diversification of JGB Investor Base

Fig. 1-25 JGB Holdings by Foreign Investors



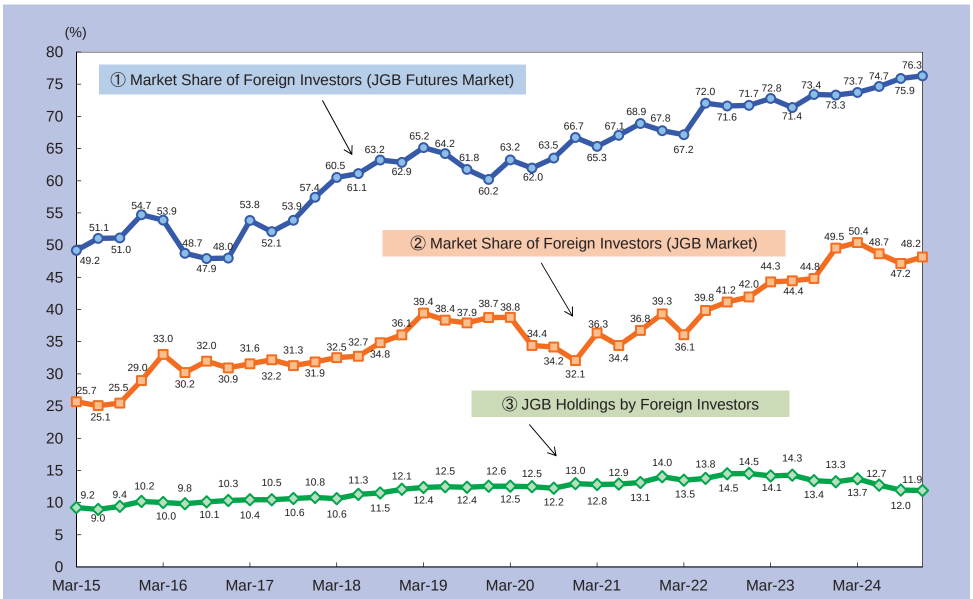
Note: "JGB" includes "FILP Bonds" and "T-Bills."
(Source) Bank of Japan "Flow of Funds Accounts"

Fig. 1-26 JGB (including T-Bills) Holdings by Foreign Investors



(Source) Bank of Japan "Flow of Funds Accounts"

Fig. 1-27 JGB Holdings and Trading by Foreign Investors



Note 1: "JGB" includes T-Bills. Figures on ② exclude dealer's transaction.
Note 2: Figures on ① and ② indicate the market share during each quarter.
(Sources) Bank of Japan, Japan Securities Dealers Association, Japan Exchange Group, Inc.

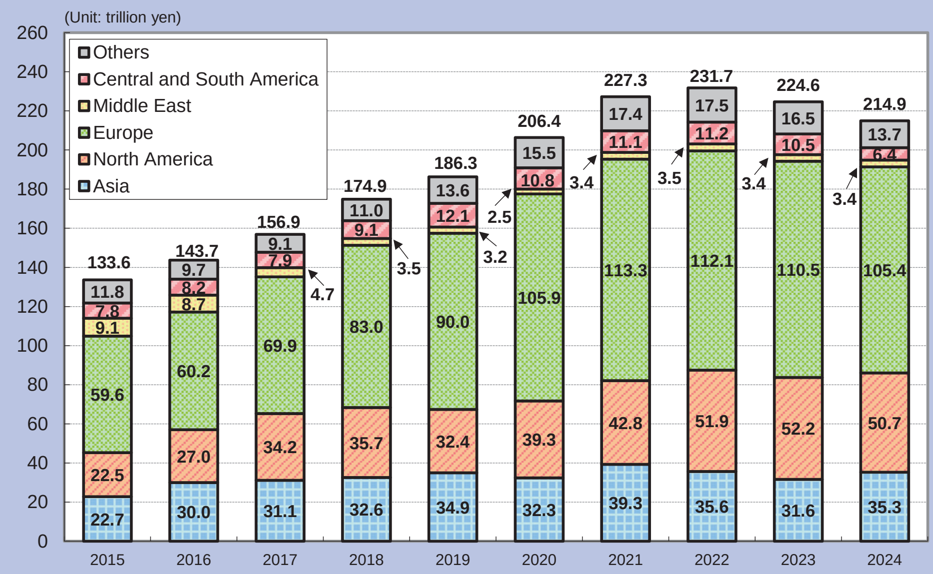
B. Breaking down Foreign Investors

There are various foreign investors, including "real money" institutional investors (such as central banks managing foreign exchange reserves, international financial institutions, pension funds, life insurance companies and asset management firms) and hedge funds.

Generally, it is said that "real money" institutional investors give greater priority to safety, liquidity and stable long-term holdings, while hedge funds mainly invest in a relatively short-term period utilizing derivatives and so on. However, some "real money" institutional investors conduct relatively short-term investment, while some hedge funds implement relatively long-term investment. As shown above, there are a variety of investment styles. Recently, a wide range of foreign investors have intensified investment in short- to medium-term JGBs by taking advantage of basis swaps.

As for a region-by-region breakdown of foreign investors, the Ministry of Finance and the BOJ release statistics (Regional Portfolio Investment and Financial Derivatives Position (Liabilities)). According to these statistics, JGB and other Japanese bond holdings total (1) 105.4 trillion yen in Europe, (2) 50.7 trillion yen in North America (3) 35.3 trillion yen in Asia, (4) 6.4 trillion yen in Central and South America and (5) 3.4 trillion yen in the Middle East (Fig. 1-28). A country-by-country breakdown of Japanese bonds held overseas indicates that the five largest holders of these bonds are (1) the U.S. with 48.8 trillion yen, (2) Belgium with 43.9 trillion yen, (3) Luxembourg with 27.9 trillion yen, (4) China with 16.6 trillion yen, and (5) the U.K. with 9.3 trillion yen.

Fig. 1-28 Foreign Investors' Bond Holdings by Region (Custodian Base)



Note: In addition to JGBs, all of the bonds issued by residents in Japan such as Local Government Bonds and corporate bonds are included. Given that these statistics provide a region by region breakdown of Japanese bond holders including custodians (financial institutions that take custody of and manage securities including shares and bonds on behalf of investors), we must take note of the fact that the breakdown does not necessarily give a region-by-region breakdown of final investors.

(Sources) Ministry of Finance, Bank of Japan

(3) JGB Investor Relations

The Ministry of Finance has made efforts to enhance relations with domestic and foreign investors in JGBs (IR: Investor Relations). These efforts aim to stabilize the JGB market by diversifying the investor base. Furthermore, we provide accurate and timely information that meets investors' needs, encourage long-term stable holding of JGBs, and aim to understand the trends and needs of both domestic and international investors accurately to provide feedback for Debt Management Policy. As part of these efforts, in July 2014, the Office of Debt Management and JGB Investor Relations was established within the Debt Management Policy Division of the Financial Bureau. By collaborating with research and analysis divisions, the office has enhanced our information dissemination system to implement more effective and efficient IR activities. In IR, we provide detailed information to a diverse range of domestic and international investors, tailored to meet the specific needs of each type of investor.

Currently, in light of the BOJ's review of its monetary policy framework in March 2024 and the subsequent decisions to reduce government bond purchases, there is a need to encourage a wide range of domestic and international investors to maintain long-term stable holdings of JGBs.

Additionally, regarding Japan Climate Transition Bonds, which began issuance in 2024, it is crucial to stimulate demand from both domestic and international investors, as they represent the world's first transition bonds issued by a national government.

To this end, in July 2024, as part of the public-private partnership efforts in IR, we designated "JGB/GX Promoter" from among securities companies that are JGB Market Special Participants (Primary Dealers) to further strengthen the domestic and international IR of JGBs, including Japan Climate Transition Bonds.

A. Efforts for Overseas IR

a. The Introduction and Evolution of Overseas IR

The efforts for overseas IR have been initiated since 2005, incorporating methods that cater to investor needs, taking into account trends among foreign investors, changes in market conditions, and feedback from meetings related to government debt management. Initially, we focused on conducting seminars to increase awareness of JGBs, but in recent years, we have also strengthened individual visits to investors. Through direct dialogue with each investor, it becomes possible to gain a more detailed understanding of and respond to investors' needs, further enhancing understanding of JGBs and the Japanese economy, and building a close relationship with investors.

Additionally, the Ministry of Finance is striving to conduct overseas IR activities more effectively and efficiently, building on over 20 years of accumulated experience in this area. For example, we create explanatory materials focused on past inquiries and the interests of foreign investors, conduct meetings, and then organize and accumulate information on investor interests and investment trends. This process follows a PDCA cycle aimed at building better relationships.

In these overseas IR, we receive a variety of questions and opinions from foreign investors. In addition to incorporating the feedback from these foreign investors into Debt Management Policy, we also strive to enhance information dissemination by publishing a monthly "JGB Newsletter" in English.

b. Overseas IR in FY2024

In FY2024, following on from FY2023, in addition to traditional overseas IR, we also conducted overseas IR aimed at enhancing understanding of Japan Climate Transition Bonds among both domestic and foreign investors. Since the decision on the aforementioned "JGB/GX Promoter," we have been strengthening overseas IR for JGBs, including Japan Climate Transition Bonds, as part of public-private partnership efforts, by obtaining cooperation from the Promoters for the following:

1. Arranging meetings with foreign investors and organizing seminars for investors
2. Supporting the update and revision of materials used in IR and providing information related to domestic and international market environments

Specifically, we conducted overseas IR activities 14 times throughout the fiscal year, visiting 25 cities in 18 countries and one region across North America, Europe, Asia, and the Middle East, with a focus on key locations where many investors are based, such as New York, London, Paris, Singapore, and Hong Kong. Additionally, we enhanced our information dissemination by not only holding meetings with local investors and debt management authorities, but also by speaking at a JGBs seminar attended by numerous investors.

As part of our domestic efforts, we actively conducted individual meetings with foreign investors visiting Japan, in addition to seminars inviting foreign investors and speeches at forums organized by international organizations.

Through such overseas IR activities, we conducted a total of 204 meetings throughout the fiscal year (Fig. 1-29). Foreign investors have shown significant interest and raised numerous questions regarding Japan's Debt Management Policy, the goal of achieving a primary balance surplus, macroeconomic trends such as Japan's wage and price conditions, and the GX policy.

Fig.1-29 Number of Meetings with Foreign Investors

	FY2019	FY2020	FY2021	FY2022	FY2023	FY2024
Number of Meetings	120	82	76	130	185	204

Note 1: The figures are limited to meetings arranged by Office of Debt Management Policy Division.
Note 2: The numbers include face-to-face meetings in Japan or abroad and online meetings.

In this way, overseas IR activities play a role in directly and clearly conveying accurate information on Japan's government debt management and economic policies, in order to meet investors' needs for extensive and in-depth information not only about JGBs but also about the economy and fiscal matters.

B. Efforts for Domestic IR

a. Strengthening Domestic IR activities

Traditionally, IR for JGBs targeting domestic investors were limited to disseminating information through this report and conducting meetings with select investors. As previously mentioned, the importance of IR targeting domestic investors is increasingly significant for diversifying the investor base. We are strengthening our domestic IR efforts, including seminars and one-on-one meetings with a wide range of domestic investors, with the cooperation of JGB/GX Promoter. Our aim is to better understand the diverse potential needs of these investors.

b. Domestic IR in FY2024

In FY2024, we undertook the following activities:

1. Participation in seminars co-hosted with various Local Finance Bureaus, primarily targeting investors within the jurisdiction of each local finance bureau
2. Presentations at various seminars for investors nationwide, hosted by industry associations and the JGB/GX Promoter
3. Individual meetings with regional financial institutions

In the seminar, we gave a lecture on the current situation surrounding the JGB market and Debt Management Policy including Japan Climate Transition Bonds, etc. In individual meetings, we made efforts to accurately understand and address investors' concerns. Additionally, we are actively engaging in new efforts to diversify the investor base, such as participating in small meetings for discussions with a select group of investors and speaking at seminars for non-profit organizations like incorporated educational institutions and public interest corporations.

In these domestic IR activities, many questions were raised by domestic investors regarding the future direction of Debt Management Policy, the progress of GX policy, and the trends of foreign investors as discussed in the aforementioned overseas IR activities.

Fig.1-30 Number of Seminars and Meetings for Domestic Investors

	FY2023	FY2024
Number of Seminars	16	17

	FY2023	FY2024
Number of Meetings	52	70

Note : The number of IR targeting domestic investors conducted by Office of Debt Management Policy Division

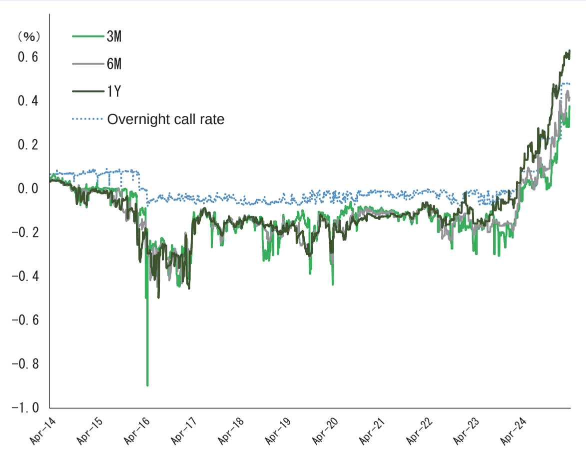
Box 5 On the Demand for T-Bills

Treasury Discount Bills (T-Bills), which are issued with maturities of one year or less, have a shorter duration until maturity. Consequently, they carry less price volatility risk compared to long-term government bonds and are considered to be highly safe. As a result, it serves as a stable investment for both domestic and foreign investors and is also utilized as collateral in financial transactions.

During the negative interest rate policy period, T-Bill interest rates reflected strong demand from both domestic and foreign investors, remaining below the Bank of Japan's policy rate. Subsequently, in March 2024, the negative interest rate policy was lifted, and interest rates turned positive across all maturities. However, due to the increased demand driven by the transition to positive interest rates, the rates for the 3-month and 6-month maturities continue to remain below the policy rate.

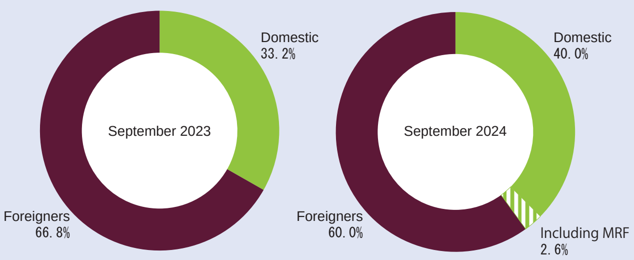
Looking at the breakdown by holder, during the period when interest rates were negative, foreign investors, who could secure profits through currency basis swap transactions, had a high share. However, after interest rates turned positive, the share held by domestic investors has increased.

Fig. B5-1 Trends in T-Bill and Other Interest Rates



(Sources) Tanshi Association, Japan Bond Trading Co.,Ltd.

Fig. B5-2 Proportion of T-Bill Holdings by Domestic and Foreign Investors



Note: Excluding the Bank of Japan and the general government (excluding public pensions).
(Source) Bank of Japan "Flow of Funds Accounts"

◯ T-Bill Investments by Foreign Investors

A distinctive feature of the composition of T-Bill holders is that the proportion of foreign investors is relatively higher compared to government bonds (excluding T-Bills).

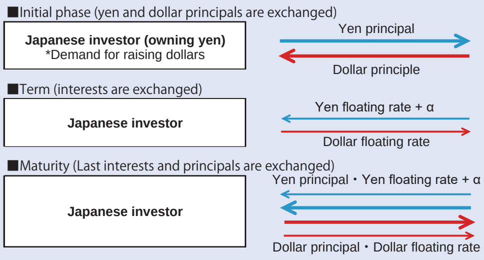
Foreign investors include a variety of entities such as institutional investors referred to as "real money," as well as hedge funds. These investors make investment decisions based on various perspectives, including individual corporate strategies and economic trends both domestically and internationally. One of the strategies adopted by foreign investors when investing in T-Bills is using currency basis swaps. The following explains the mechanism of investment using currency basis swaps.

A currency basis swap is a transaction in which the principal amounts in different currencies are exchanged at a predetermined exchange rate, and the variable interest rates arising in each currency over the period are swapped. The Fig. B5-3 below presents an overview of trading in the dollar-yen currency basis swap (dollar-yen basis) as an example. In the figure, α is the so-called basis spread. The spread means a premium on a yen interest rate (annual rate) and fluctuates depending on supply and demand between the currencies.

If demand is strong for raising yen even at the cost of an increase in yen interest payments, for instance, upward pressure is exerted on α. If demand is strong for raising dollars even at the cost of a decline in yen interest receipts, downward pressure is exerted on α.

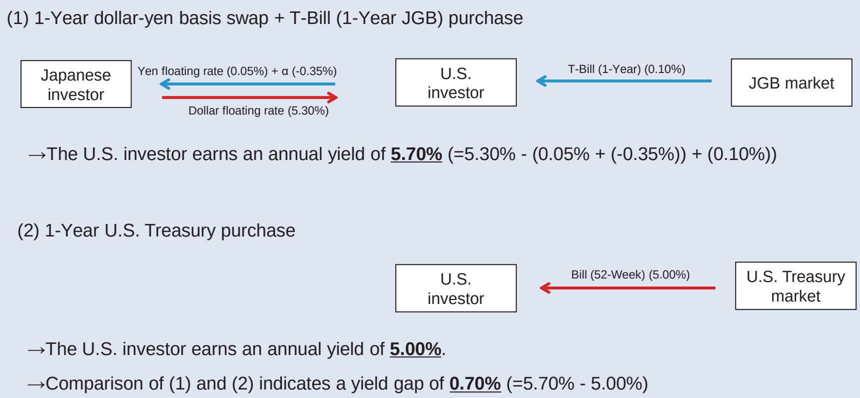
In recent years, due to strong demand for dollar funding, α has generally remained negative across most tenors in the dollar-yen basis. This condition, where α is negative, is expressed as a "premium in dollar funding is occurring."

Fig. B5-3 Scheme Diagram of Currency Basis Swap(dollar-yen basis swap) (In the Case of a 1-Year Maturity)



For instance, if the one-year α (the basis spread of the dollar-yen basis with a one-year maturity) is assumed to be -0.35% (-35 bps), when U.S. investors utilize the one-year dollar-yen basis as shown in Fig. B5-3, U.S. investors will incur a "receiving dollar floating rate" and "paying yen floating rate plus α (-35 bps)" over the course of one year. Here, the fact that U.S. investors pay -35 basis points in interest implies that they receive an equivalent amount in interest. Considering various interest rate levels, U.S. investors, in pursuit of receiving this 35 basis points, would achieve a higher yield by swapping dollars for yen to invest in Japanese government bonds rather than investing in U.S. Treasuries.

Fig. B5-4 Comparison Between a U.S. Investor Swapping Dollars to Yen and investing in JGBs and the Investor Investing in U.S. Treasury Securities (using 1-year dollar-yen basis swap) (transactions in the mid-term portion of Fig. B5-3)



Note 1: Although the yen floating rate and the dollar floating rate in the descriptions above are assumed to remain unchanged, they actually fluctuate.

Note 2: Interest rate swap transactions for fixing the yen floating rate and the dollar floating rate are omitted here to simplify the explanation.

○ Trends of Domestic Investors

For domestic investors, the primary entities include domestic banks with collateral holding needs and domestic institutional investors with short-term fund management needs. Among other things, regarding the short-term operational needs of domestic institutional investors, the use of T-Bills for fund management was restrained during the period when T-Bill rates remained in negative territory. However, with the lifting of the negative interest rate policy in March 2024, leading to interest rates moving into positive territory, the use of T-Bills for operations has resumed from April of the same year. One example of an investment entity that has resumed operations with T-Bills is the Money Reserve Fund (MRF), and an overview of it is provided below.

MRF was established in 1997 as a repository fund for idle funds that arise with the introduction of comprehensive securities accounts. Since the start of "Abenomics" in 2012, the rise in stock prices has led to an increase in transactions of stocks and investment trusts, resulting in an expansion of idle funds in securities accounts, and the net asset balance of MRF has been continuously increasing. Since MRF is fund that manage idle funds in securities accounts, a high level of safety is required in their operations. For example, there are certain regulations concerning their management methods, such as "including more than 50% securities" and "limiting the remaining maturity of included bonds to within one year." Under such regulations, T-Bills, which are securities with short maturity periods, were originally highly compatible investment targets for MRF. With T-Bill interest rates moving into positive territory, their investment is currently being resumed.