



M I C

Local Government Bond System and Market in Japan

**Ministry of Internal Affairs
and Communications**

September 2016

I JLGB as an alternative to JGB

II Safety of JLGB

Appendix

I JLGB as an alternative to JGB

The type and issue amount of the JLGBs and JFM's Bonds (FY2015)

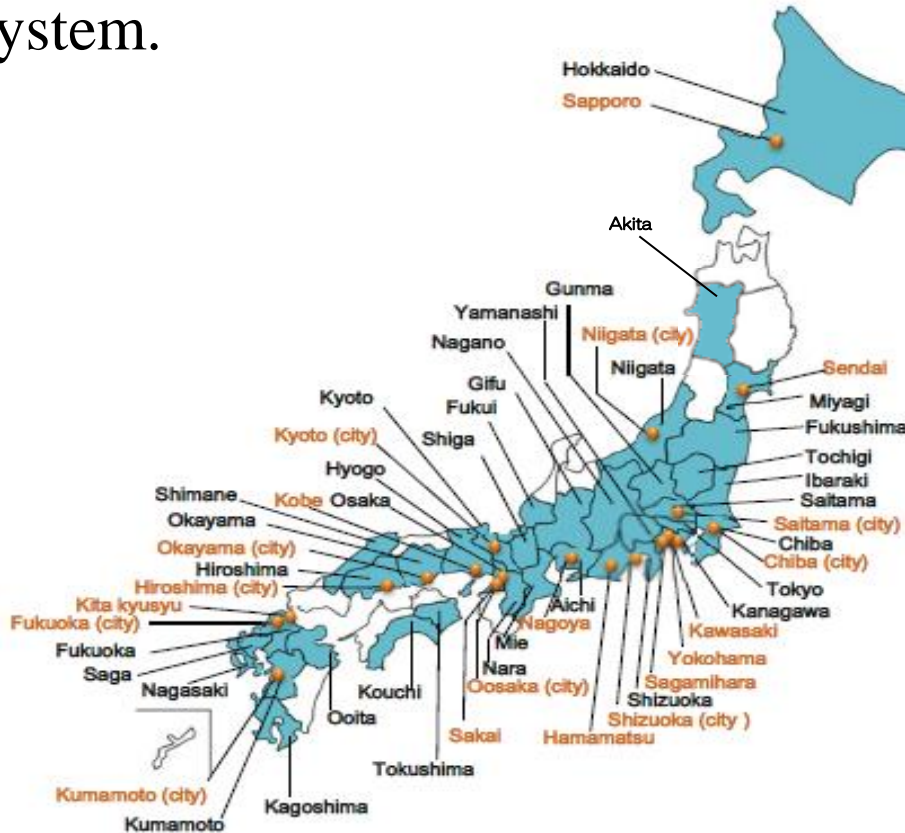
	Denominated in JPY	Denominated in foreign currency
JLGBs	LGB <JPY 5.2 trillion> ≒ USD 50.5 billion Joint local government bond <JPY 1.4 trillion> ≒ USD 13.8 billion	Tokyo Met. <USD 1 billion>
JFM's Bonds	<JPY 1.4 trillion> ≒ USD 13.7 billion	<USD 1.5 billion>
Total	<JPY 8.0 trillion> ≒ USD 78.0 billion	<USD 2.5 billion>

※【Reference】 Issue amount of JGB (FY2015) : JPY 167 trillion ≒ USD 1,616 billion

Note : USD 1 = JPY 103.18 as of 31 August ,2016

I JLGB as an alternative to JGB (diversity of JLGB)

- ◆ A lot of LGs successfully issue public offering bonds underpinned by the solid creditworthiness supported by the local public finance system.

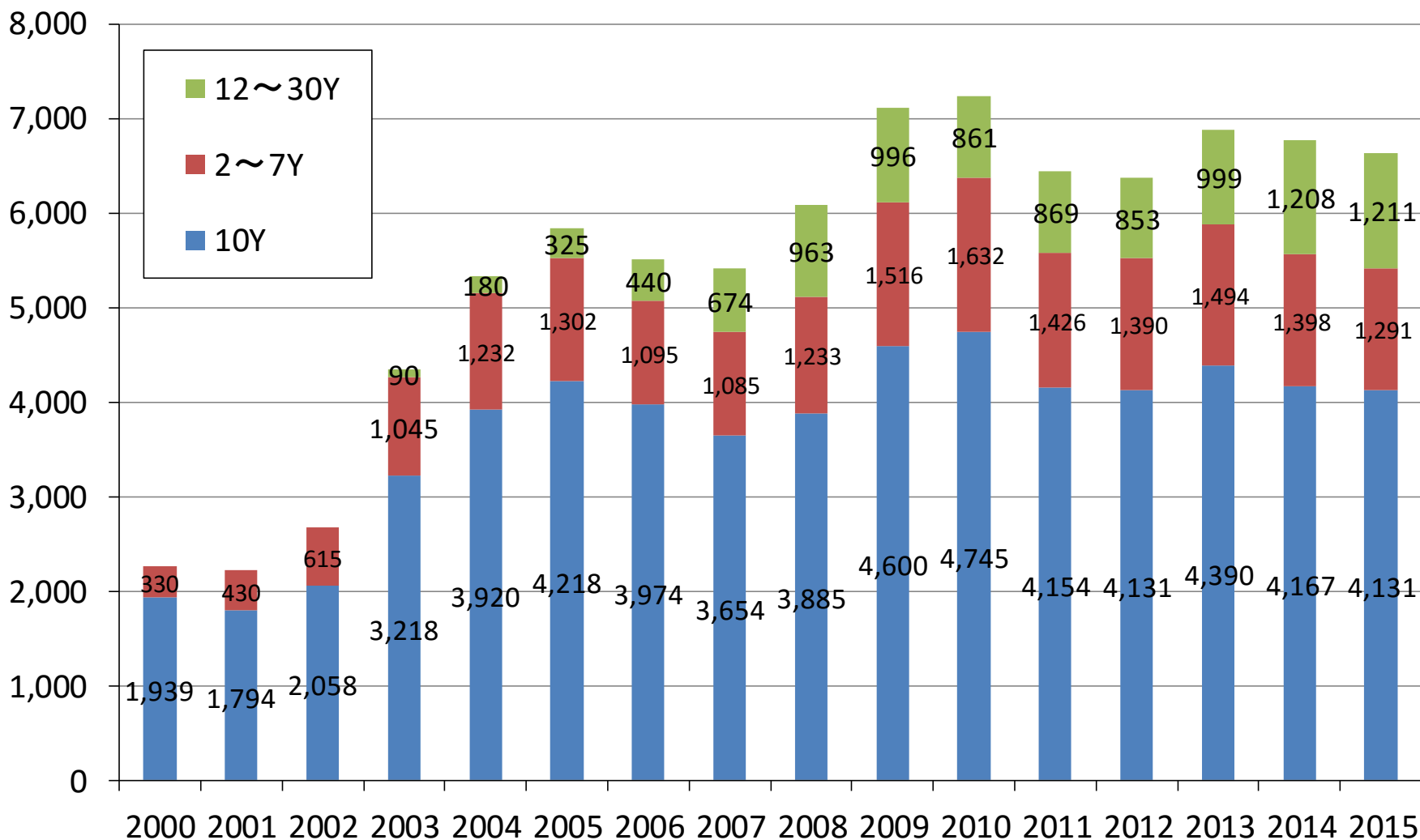


- ◆ 55 LGs issue public offering bonds in FY 2016.
 - ▶ 35 prefectures (shown in black)
 - ▶ 20 designated cities (shown in red)

I JLGB as an alternative to JGB (diversity of JLGB)

◆ Issue amount of public offering LGBs

(Unit: billions of JPY)



- 1. Solid support by the central government on redemption**
- 2. Check and control system by the central government**
- 3. Control of fiscal discipline**

Principal and interest of JLGB have been fully paid without default (similar to JGB).

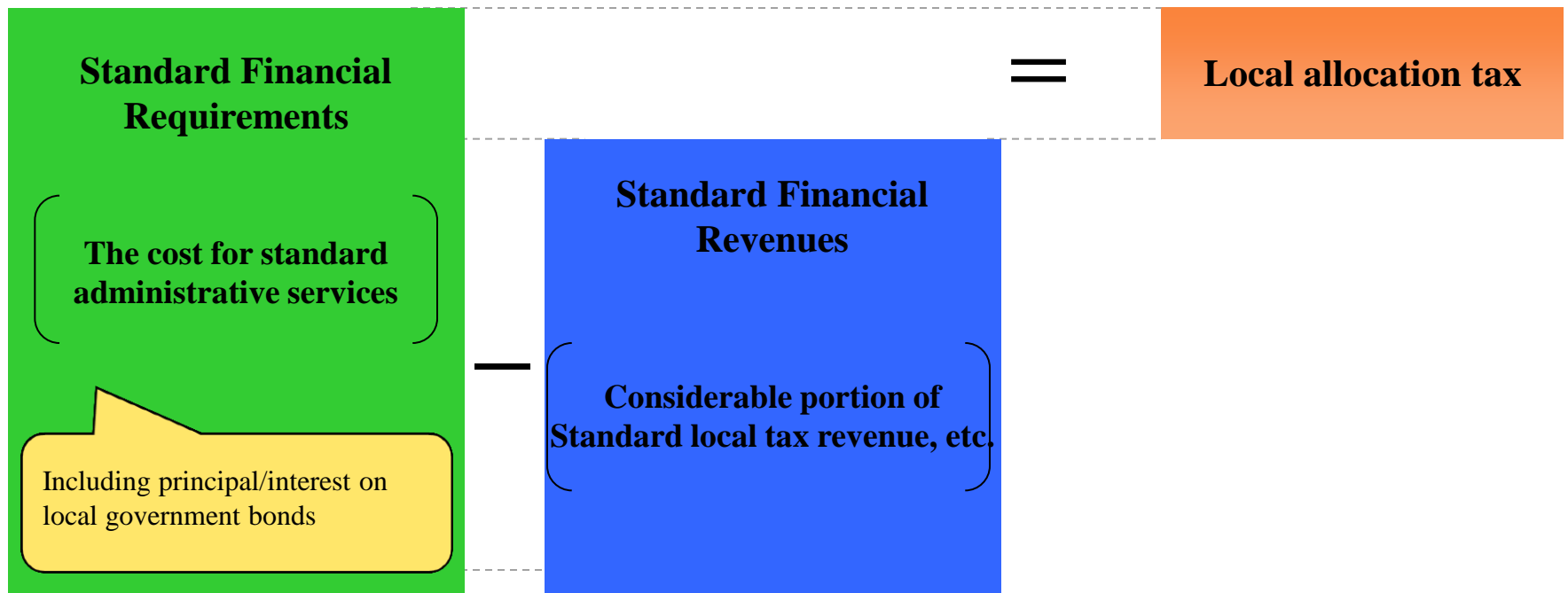
II -1 Solid support by the central government on redemption

The central government secures revenue sources required for principal/interest payment on local government bonds through the local public finance system.

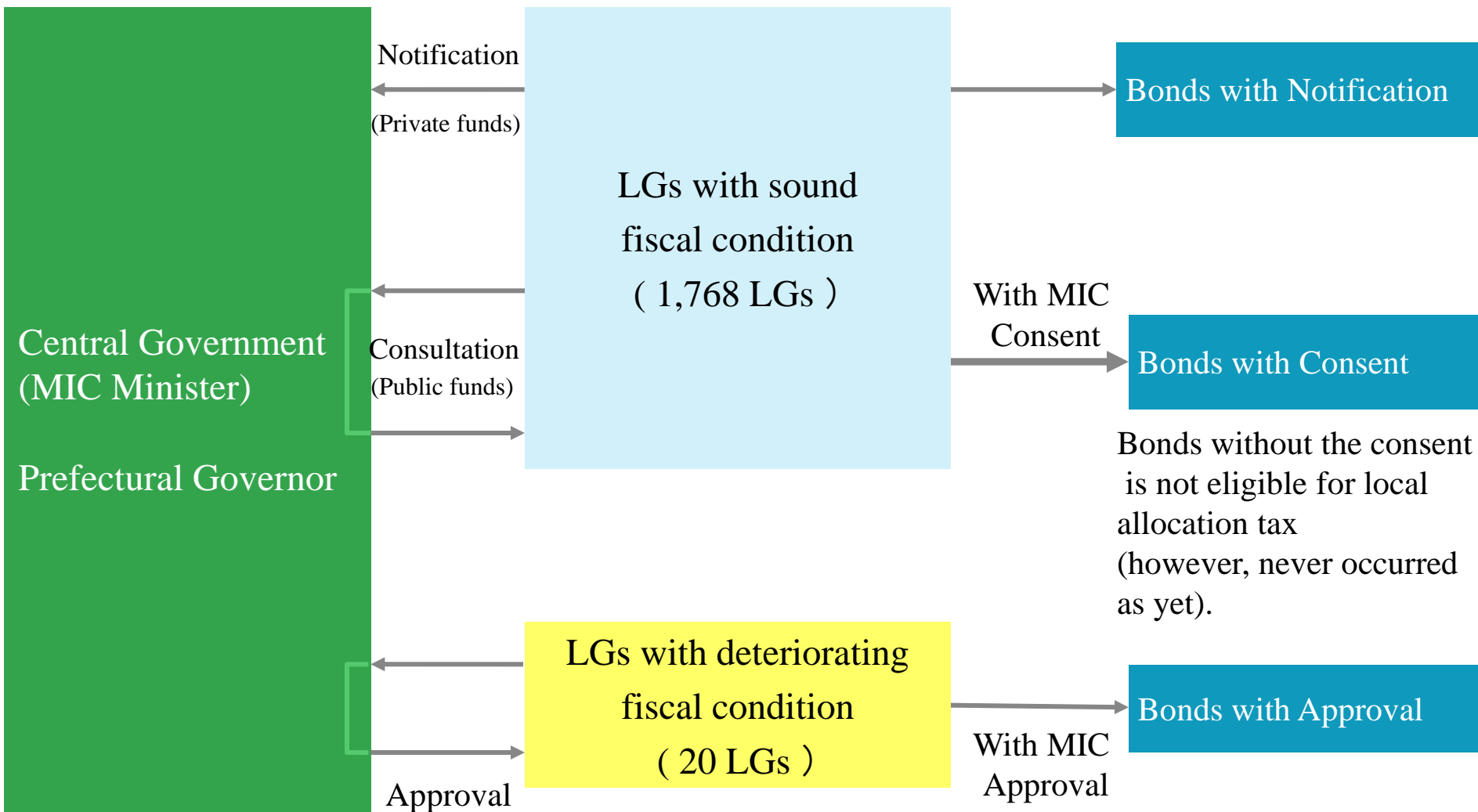
In particular, it is secured through local allocation tax each local government receives from the central government to provide basic social capital and standard administrative services to citizens.

The principal / interest on JLGB is included in the standard fiscal demand amount when calculating local allocation tax.

The local allocation tax system has functioned for over 60 years since 1954. The amount of the local allocation tax is around 17 trillion yen.



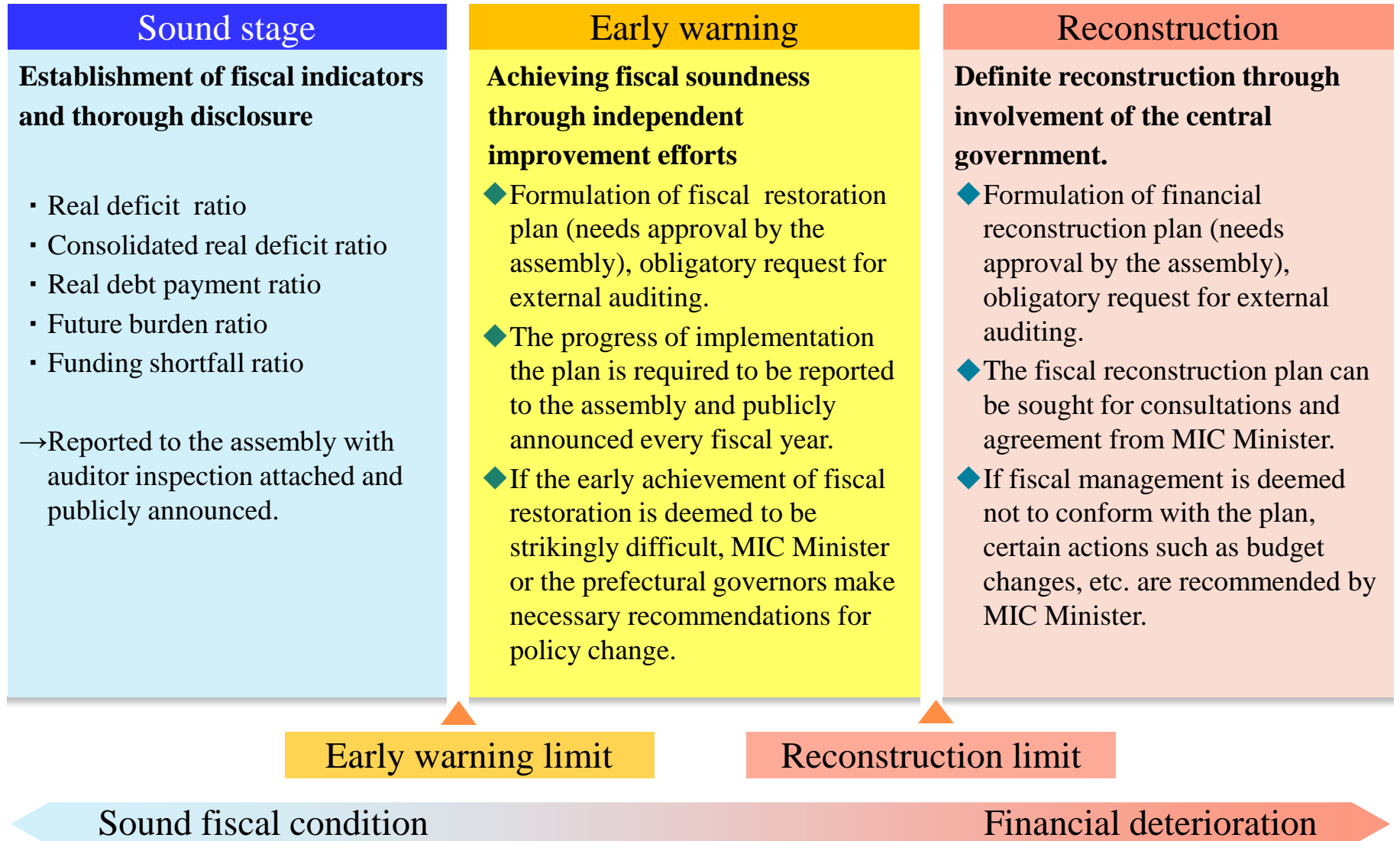
II -2 Check and control system by the central government



Note :LGs are classified by the fiscal conditions etc.

The numbers of LGs is FY2016

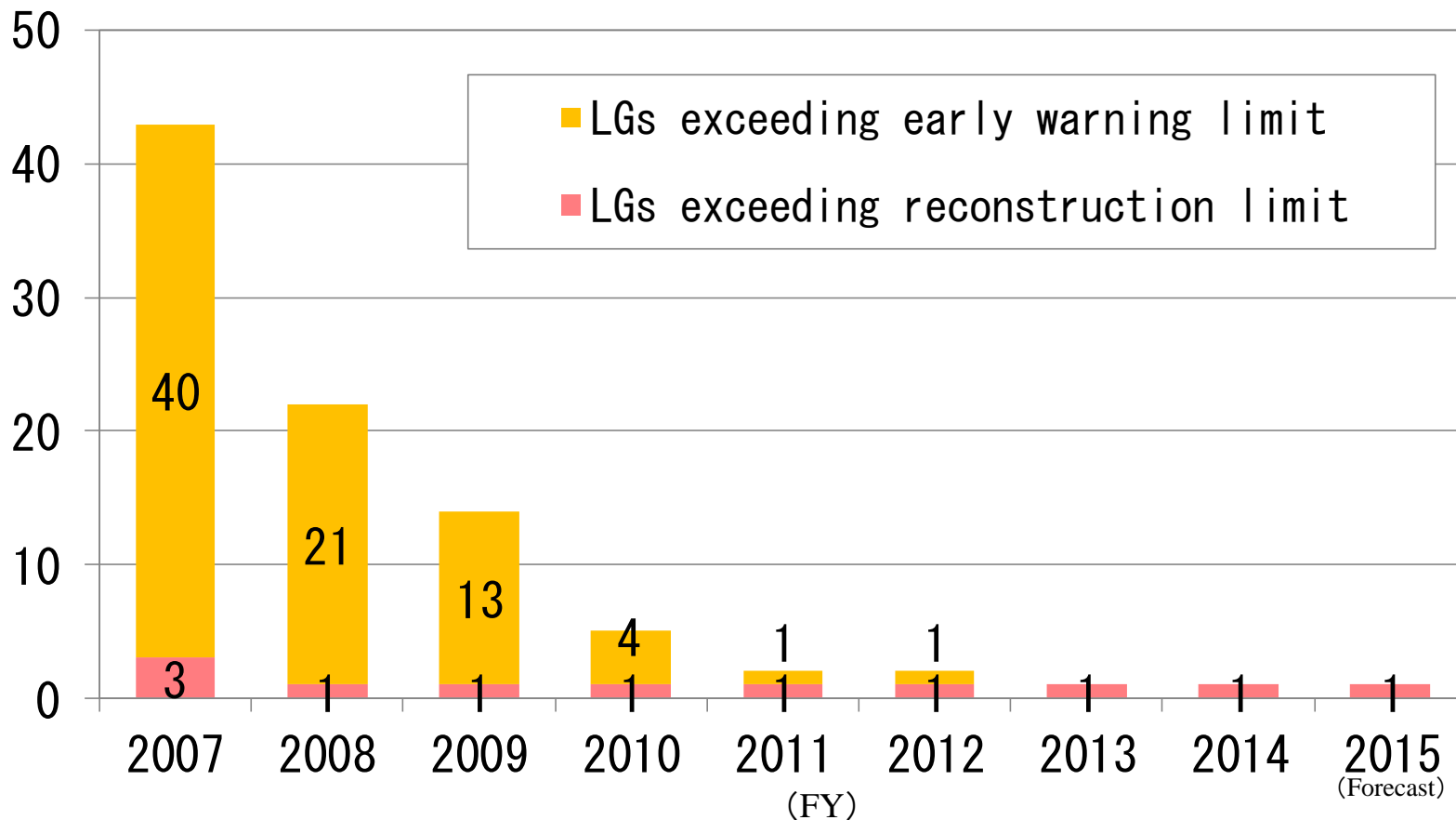
II-3 Control of fiscal discipline



II -3 Numbers of LGs exceeding early warning limit

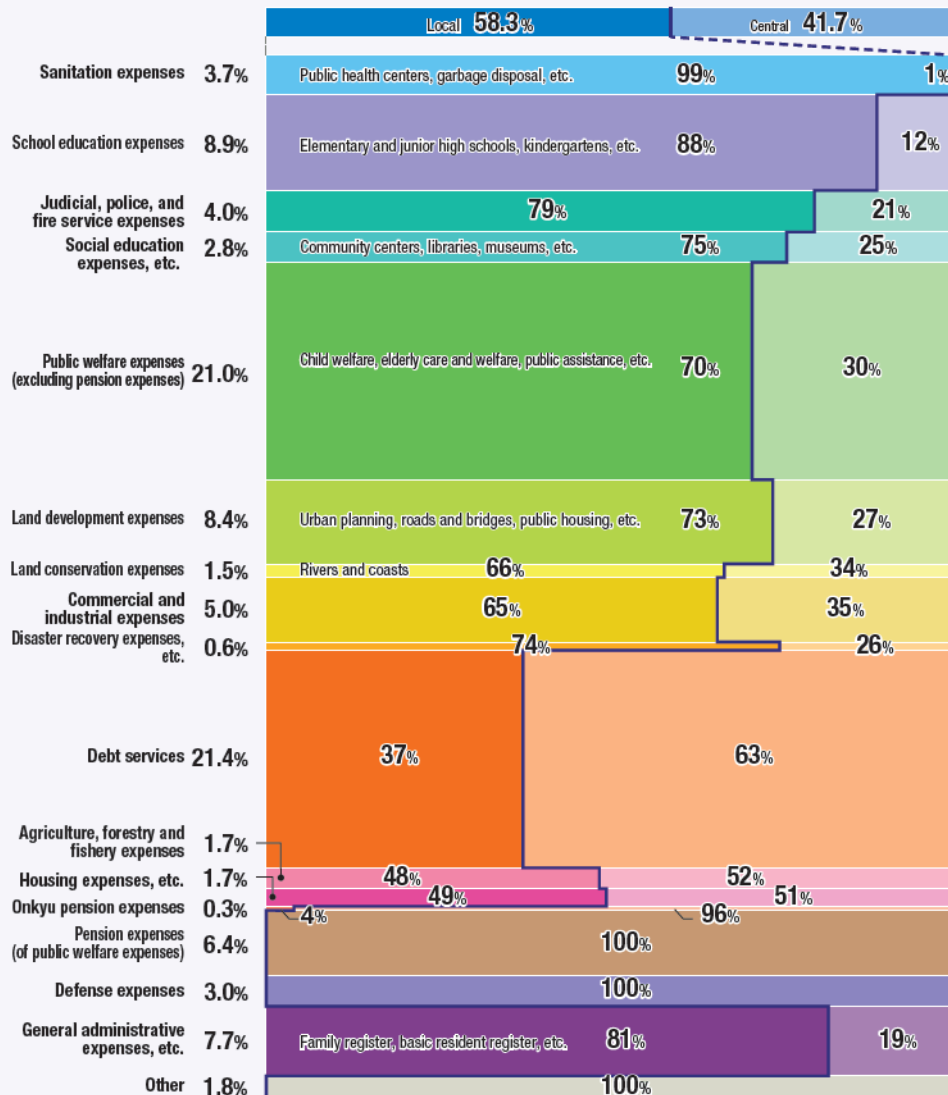
- ◆ In recent years, the numbers of LGs exceeding early warning limit have decreased.

(Numbers of LGs)



Appendix

Share of Expenditures by Purpose of Central and Local Governments (final expenditure based)



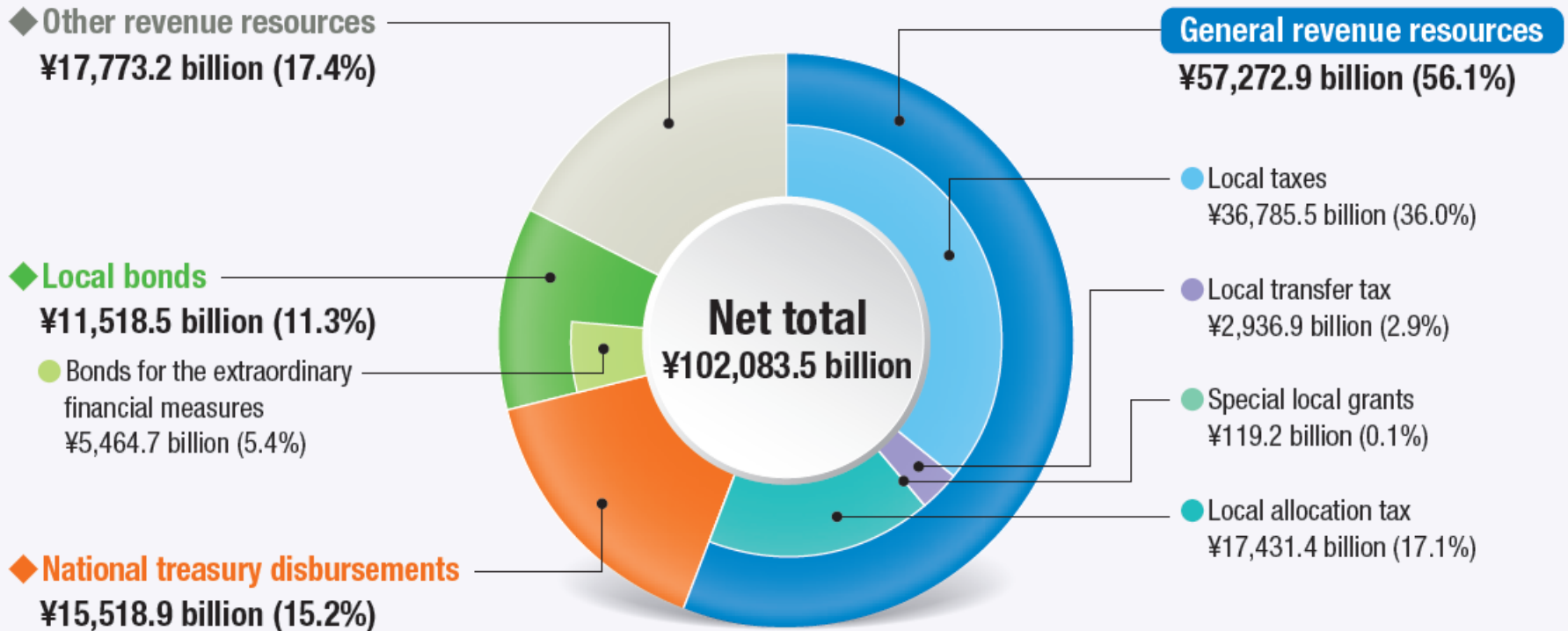
◆ LGs have relatively large responsibilities & functions.

◆ The greatest portion of local government annual expenditures is directed toward supporting everyday public services: public health and sanitation, education, social education, and police and fire prevention, etc.

Source: White Paper on Local Public Finance, 2016 “FY2014Settlement” by Ministry of Internal Affairs and Communications

- ◆ The revenue of LGs comes mainly from local taxes, local allocation tax, national treasury disbursements, and local bonds.

Composition of Revenues (FY2014 settlement)



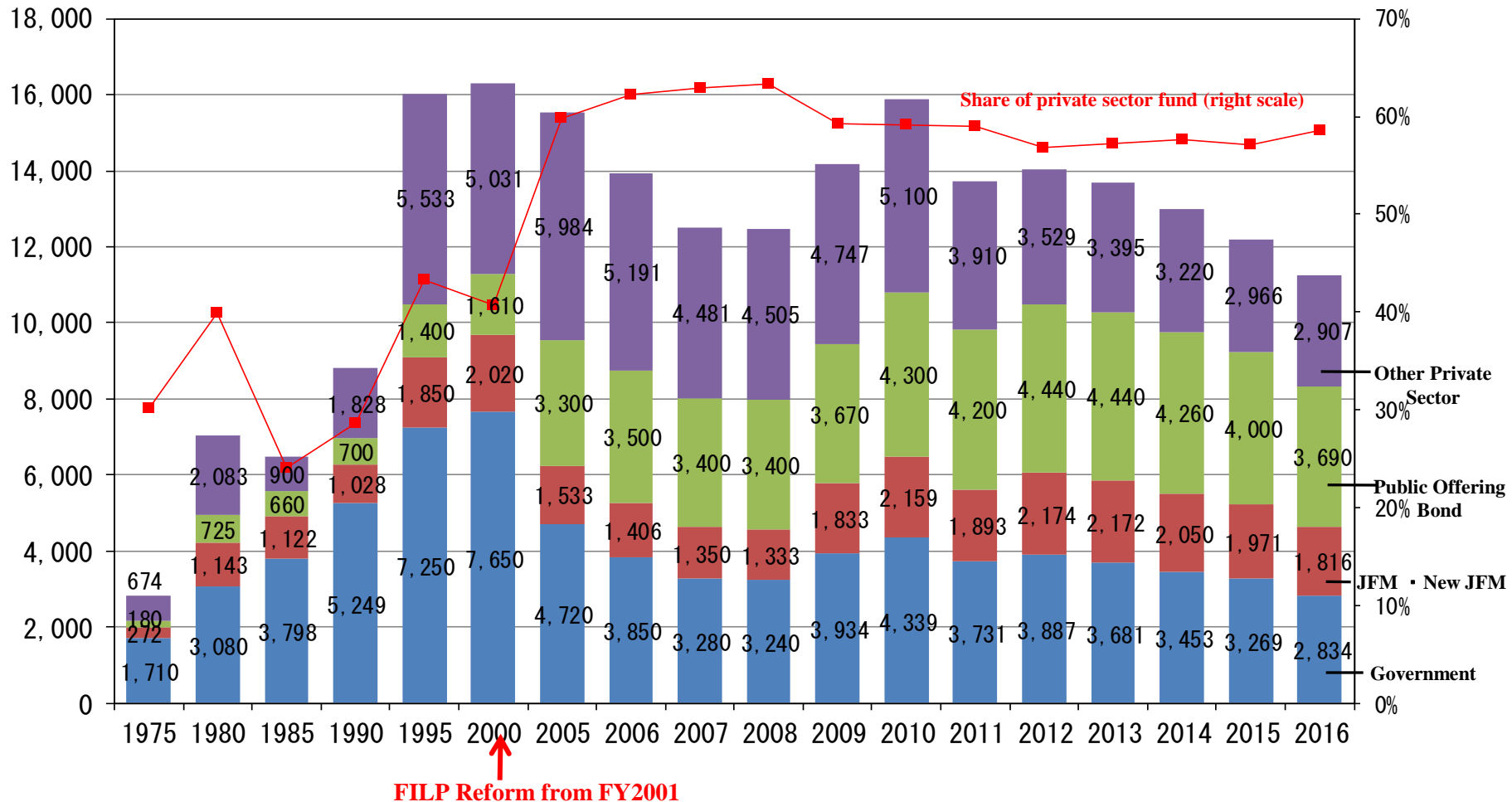
Source: White Paper on Local Public Finance, 2016 "FY2014 Settlement" by Ministry of Internal Affairs and Communications

Historical changes of annual issue amount

- ◆ Reduction in government funding due to FILP (Fiscal Investment and Loan Program) Reform to minimize government funding role from FY2001.

(Unit: Billions of yen)

(Unit: %)



Source: Ministry of Internal Affairs and Communications



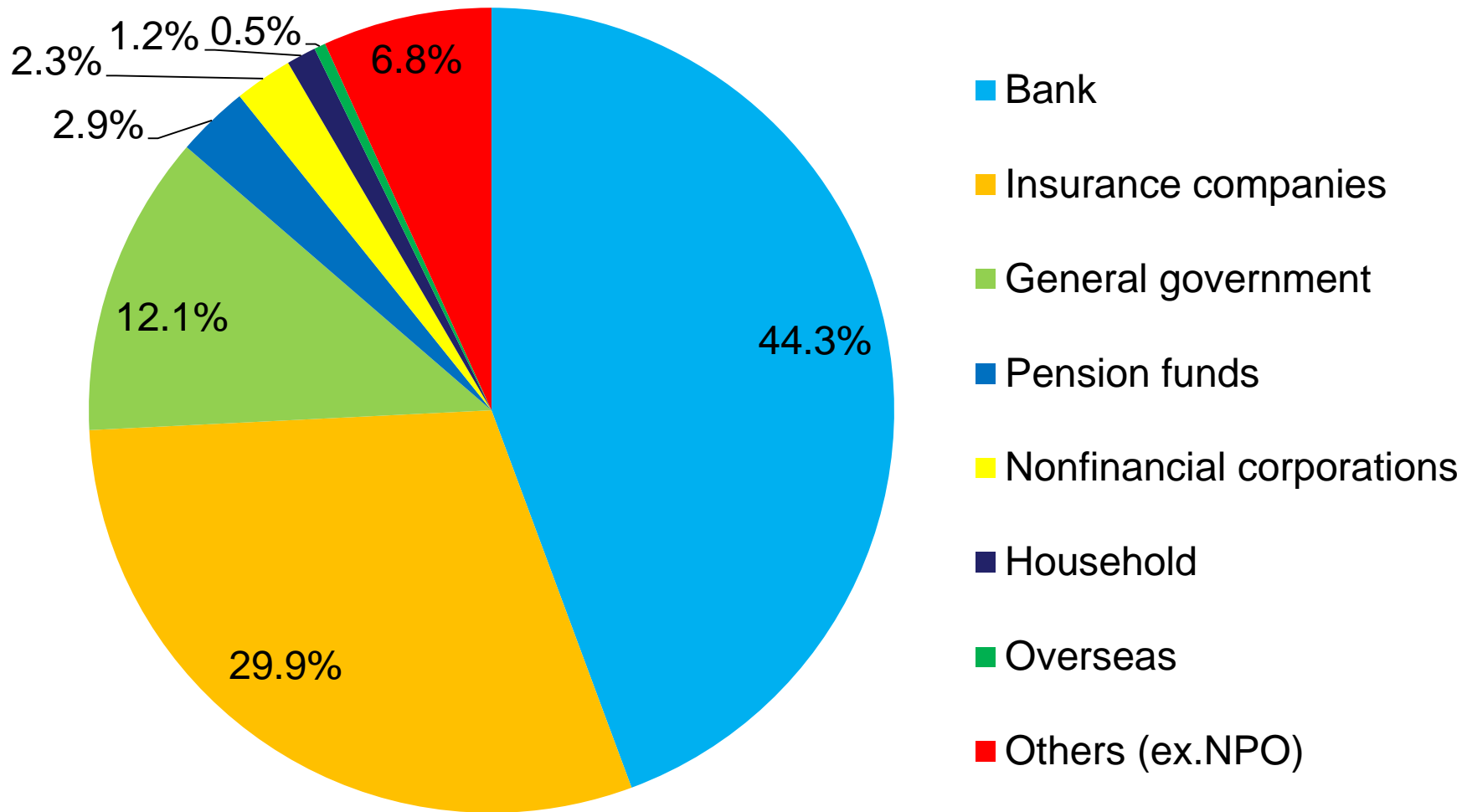
Planned Issuance for Nationwide Public Offering LGBs in Fiscal-Year 2016

(Unit: Hundred Million Yen)

Local government	total	2y or 3y 5y or 7y	10y	15y or 20y or 30y	joint-LGB	other	Local government	total	2y or 3y 5y or 7y	10y	15y or 20y or 30y	joint-LGB	other
Hokkaido	2,900	600	1,100	0	800	400	Kochi	100	0	100	0	0	0
Miyagi	1,100	200	200	0	400	300	Fukuoka	2,400	300	750	600	0	750
Akita	100	0	100	0	0	0	Saga	100	0	100	0	0	0
Fukushima	530	100	200	0	230	0	Nagasaki	100	0	100	0	0	0
Ibaraki	500	100	100	0	300	0	Kumamoto	500	100	100	0	300	0
Tochigi	100	0	100	0	0	0	Oita	300	0	100	0	200	0
Gunma	500	100	300	100	0	0	Kagoshima	800	100	0	0	700	0
Saitama	3,800	400	1,600	200	500	1,100	Sapporo City	1,100	300	200	0	300	300
Chiba	2,400	400	1,200	300	300	200	Sendai City	510	150	0	0	360	0
Tokyo	5,600	0	3,800	800	0	1,000	Saitama City	100	0	100	0	0	0
Kanagawa	2,700	600	1,400	400	300	0	Chiba City	500	0	200	0	300	0
Niigata	1,200	0	600	0	600	0	Yokohama City	1,800	300	700	300	0	500
Fukui	430	0	200	0	100	130	Kawasaki City	930	210	80	300	200	140
Yamanashi	200	0	200	0	0	0	Sagamihara City	100	0	100	0	0	0
Nagano	650	200	0	0	450	0	Niigata City	200	0	100	0	100	0
Gifu	350	0	150	0	200	0	Shizuoka City	300	0	200	0	100	0
Shizuoka	2,300	300	700	600	300	400	Hamamatsu City	100	0	100	0	0	0
Aichi	2,900	200	1,800	200	300	400	Nagoya City	1,350	100	600	200	0	450
Mie	200	0	100	0	100	0	Kyoto City	1,150	200	200	100	350	300
Shiga	100	0	100	0	0	0	Osaka City	2,100	400	400	400	300	600
Kyoto	2,000	400	400	300	500	400	Sakai City	200	0	100	100	0	0
Osaka	6,900	2,200	2,200	0	800	1,700	Kobe City	1,100	200	200	200	200	300
Hyogo	2,800	600	700	200	800	500	Okayama City	100	0	100	0	0	0
Nara	200	100	0	0	100	0	Hiroshima City	650	200	350	0	100	0
Shimane	450	150	100	200	0	0	Kita-Kyusyu City	1,200	150	300	100	350	300
Okayama	300	0	200	0	100	0	Fukuoka City	1,600	600	200	200	150	450
Hiroshima	1,620	120	700	200	600	0	Kumamoto City	100	0	100	0	0	0
Tokushima	350	0	100	0	250	0	Total	62,670	10,080	23,930	6,000	12,040	10,620

※This is based on the figures of domestic bonds announced by Ministry of Internal Affairs and Communications in Apr 2016.

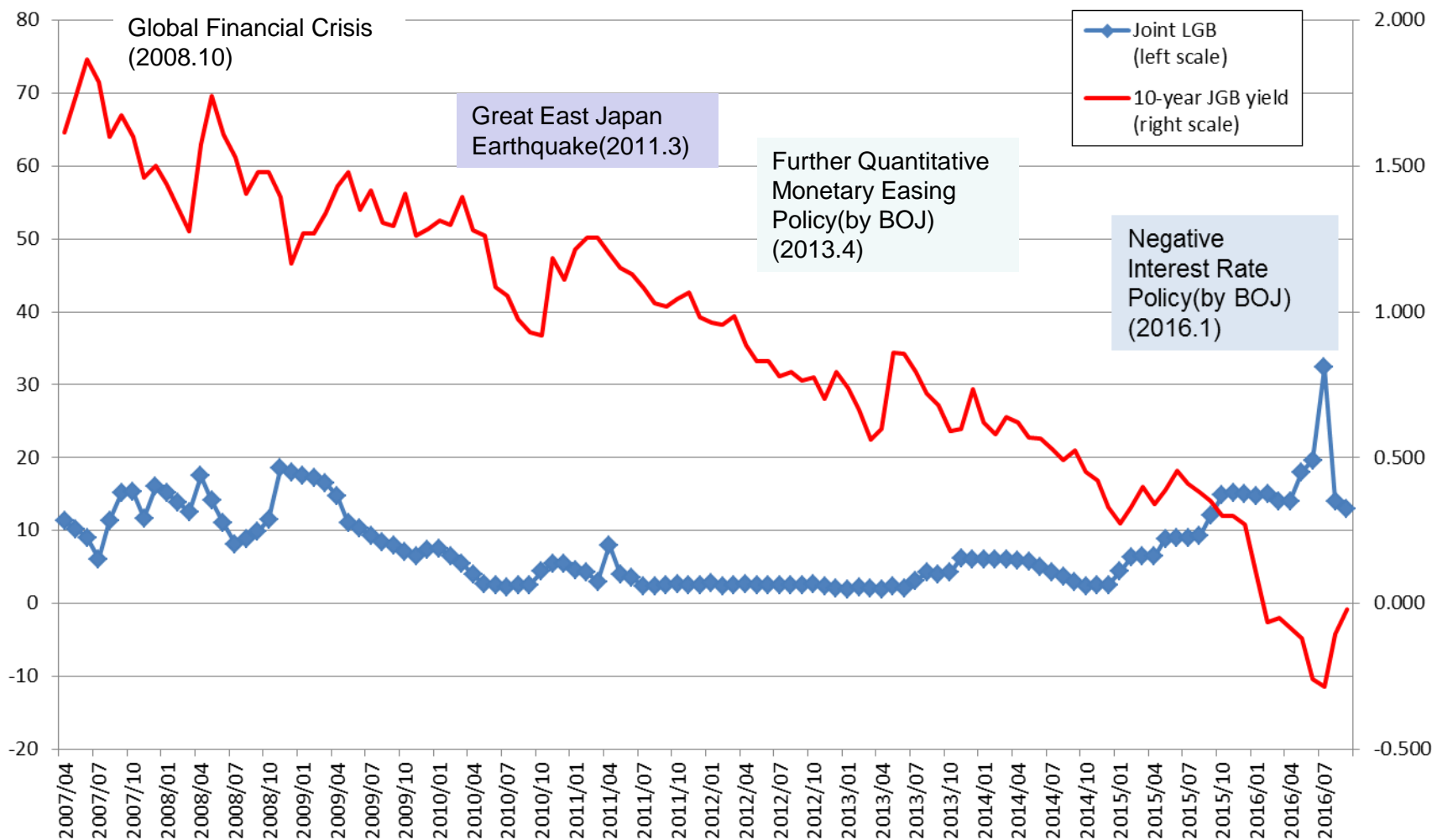
Distribution of JLGB holders (2015/March end)



Source: Bank of Japan "Flow of funds accounts"

Spread for public offering JLGB over JGB

◆ Spread over JGB



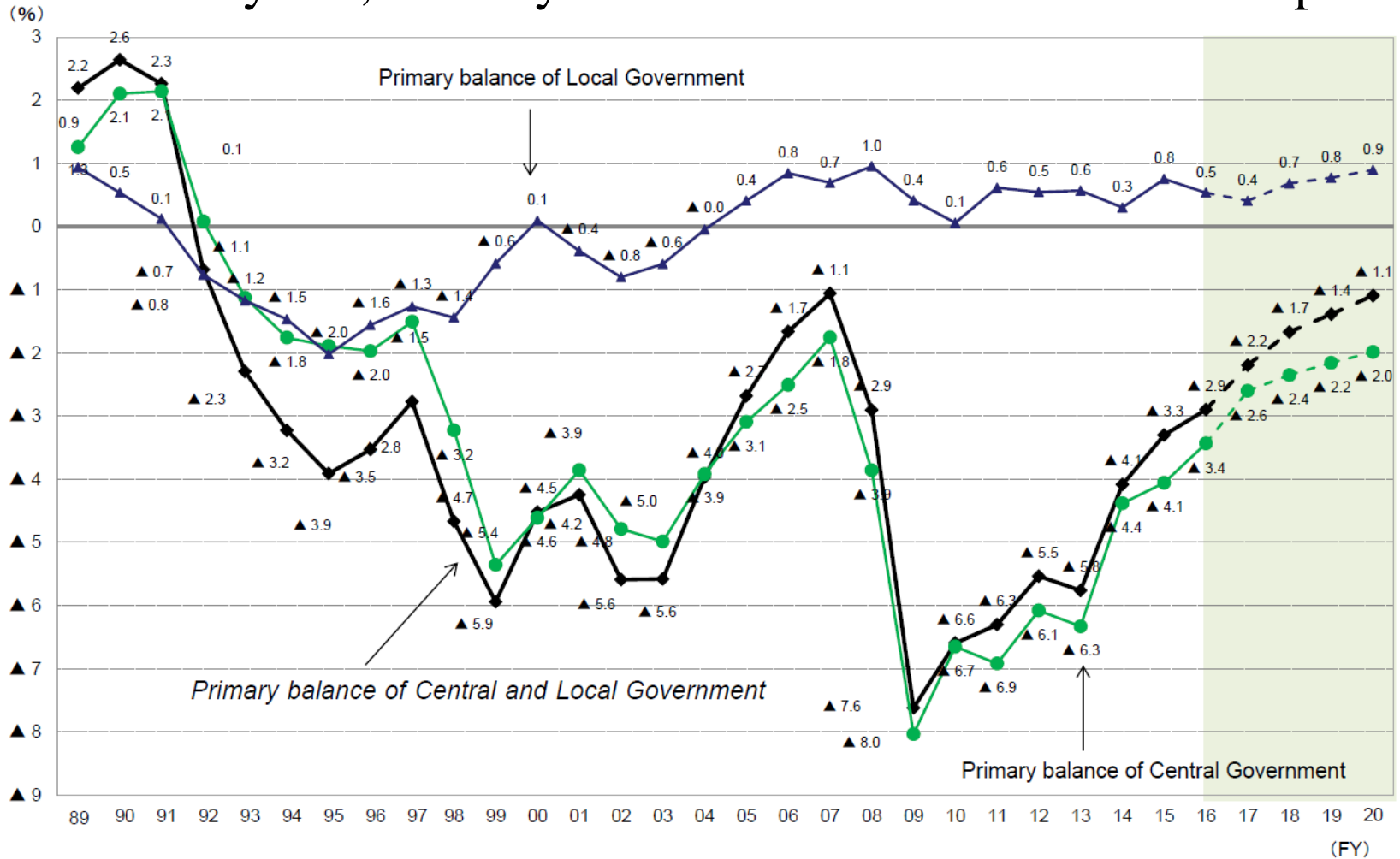
※Issuance Yield(Apr.2007-Sep.2016)
Source: Japan Local Government Bond Association

Credit rating of JLGB

Local Government	Ratings	
	Moody's	S&P
JGB(Central Government)	A1/Stable	A+/Stable
Tokyo	-	A+/Stable
Niigata Prefecture*	A1/Stable	-
Shizuoka Prefecture*	A1/Stable	-
Aichi Prefecture*	-	A+/Stable
Hiroshima Prefecture*	A1/Stable	-
Fukuoka Prefecture	A1/Stable	-
Sapporo City*	A1/Stable	-
Yokohama City	A1/Stable	-
Shizuoka City*	A1/Stable	-
Hamamatsu City	A1/Stable	-
Nagoya City	A1/Stable	-
Kyoto City*	A1/Stable	-
Osaka City*	A1/Stable	A+/Stable
Sakai City	A1/Stable	-
Fukuoka City*	A1/Stable	-
JFM	A1/Stable	A+/Stable

Trends in Primary Balance of Central and Local Governments to GDP Ratio

◆ In recent years, Primary Balance of LGs has achieved surplus.



(Source) FY1989-2015:Cabinet Office “Annual Report on National Accounts”

FY2016-2020:Cabinet Office ”Economic and Fiscal Projections for Medium to Long Term Analysis”

Effects of Abenomics

The first "arrow"

Aggressive Monetary Policy

- The price stability target of 2%
- The quantitative and qualitative monetary Easing

The second "arrow"

Flexible Fiscal Policy

- The Economic Measures for Realizing Investment for the Future (the supplementary budget for fiscal 2016 at JPY28 trillion)

The third "arrow"

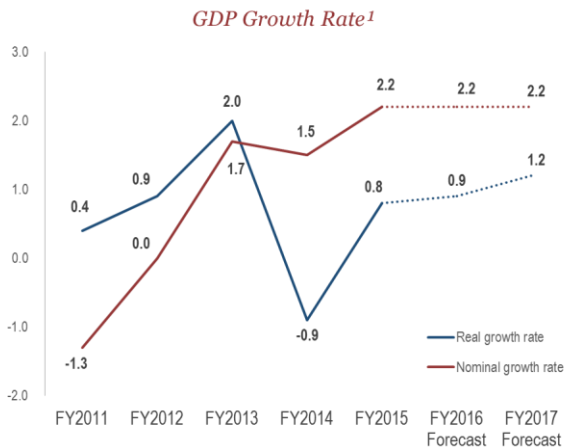
The Growth Strategy that encourages private sector

- "Growth Strategy 2016" toward nominal GDP 600 trillion yen

[Targets] • Ending deflation
• Revival of Economy

The government aims to achieve economic growth over the medium to long term surpassing approximately 2% for real GDP and 3% nominal GDP.

Aberomics has set the economy on course to make a steady recovery



- Recent increase (in the past year)*: Nominal GDP +1.5%
- Real GDP +0.8%
- (* : Change between Q2 2015 and Q2 2016)

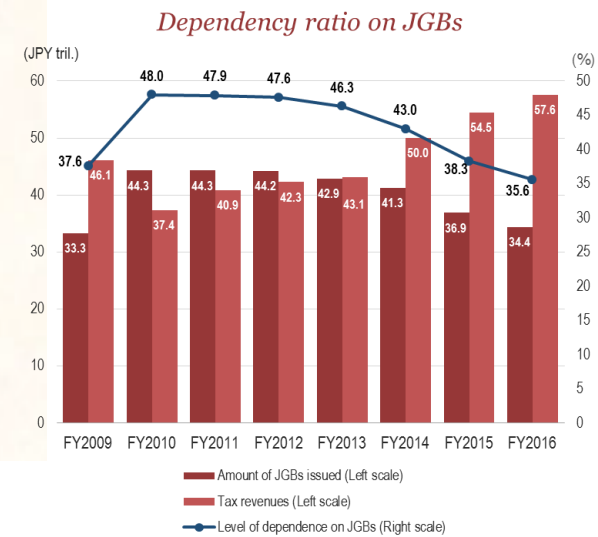
Although the real GDP decreased by 0.9% in FY2014 due to the effect of the consumption tax hike, it is expected to grow steadily from this point forward.

Corporate profitability has increased significantly



- Increase in annual corporate ordinary profits: 20 trillion yen (FY2012 – FY2015)
- Increase in annual capital investment: 8 trillion yen (FY2012 – FY2015)

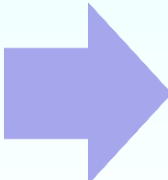
Steady progress of fiscal consolidation



- Tax revenue is expected to increase, and dependency ratio on Japanese Government Bonds (JGBs) is declining steadily
- Primary deficit to GDP ratio has been reduced to target level, halving from FY2010 to FY2015 (FY2010 -6.6% → FY2015 -3.2%)

Check and control system by the central government

- Local governments (LGs) are required to consult with, or notify the Minister of MIC (or the prefectural governor) at the time of issuance of Local Government Bond (LGB).
- LGB issuance without the consent of the Minister of MIC (or prefectural governors) is not eligible for public funds nor for local allocation tax system (Although LGs can issue LGBs without the consent, there are no such case.).
- In addition, LGs with deteriorating fiscal conditions are required to obtain an approval of the Minister of MIC (or the prefectural governor) in their issuance. LGB issuance without the approval shall not be issued in this case with LGs with relatively weak fiscal conditions.

- 
- The central government (or prefectures) check all the LGBs.
 - The central government secures the redemption of LGBs as a form of a consent.
 - Issuance of LGBs by LGs with deteriorating fiscal conditions is restricted.
(the number of LGs necessary to obtain the approval FY2015: 20(total LGs : 1,788))

Consultation system for the issuance of JLGB

- ◆ JLGB system changed from approval system to consultation system in FY2006 due to decentralization. Moreover, notification system was introduced in FY2012 limited to Private Fund from the perspective of enhancement of LGs' autonomy.

1. Consultation

LGs are required to consult with, or notify the Minister of MIC (prefectures and government designated cities) or the prefectural governor (municipalities) before debt issue.

2. Allocation of public funds for LGB with the consent

Only LGB with the consent by the Minister of MIC or the prefectural governors may borrow public funds [Government funds, JFM funds].

3. Debt payment for bonds with the consent included in Local Allocation Tax system

Debt payment for LGBs with the consent by the Minister of MIC or the prefectural governors is included in Local Allocation Tax system.

4. LGs are required to report issuance of the bond without the consent to the assembly

In order to issue LGBs which need consultation without the consent, the head of the LG is the required to report issuance of bond without the consent to the assembly.

5. Standard for consent

The Minister of MIC releases the standard for the consent every fiscal year. Issuers in high deficit, issuers with high real-debt-payment-ratio, and public enterprises in high deficit, etc. are required to obtain the approval of issuance from the Minister or the governor.

Consultation system for the issuance of JLGB (2)

◆ In order to secure fiscal soundness, LGs with higher real-debt-payment-ratio or higher deficit than a set limit are required to get the approval for bond issue instead of the consultation.

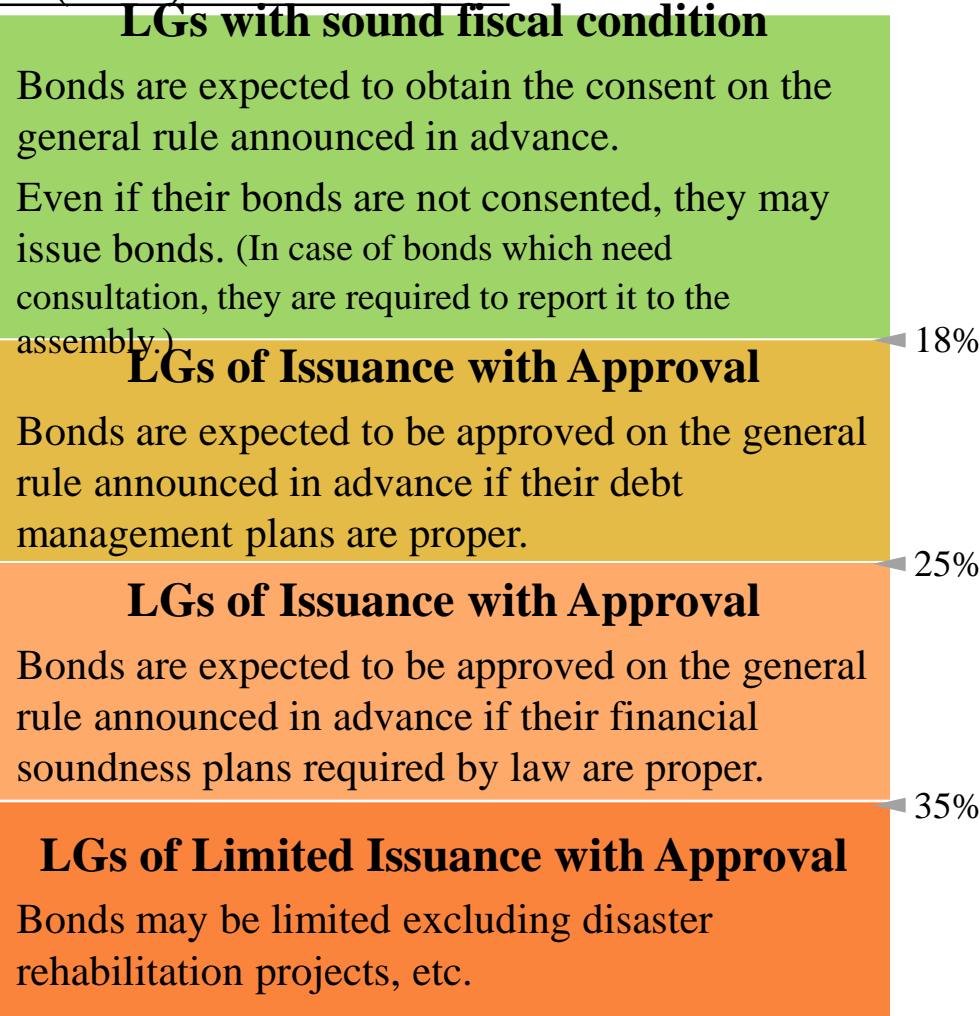
Approval required if real-debt-payment-ratio(RDP) is 18% or more

◆ Issuers with RDP under 18% must consult with, or notify the MIC minister (or the prefectural governor) before debt issue.

◆ Issuers with RDP between 18% ~ 25% must draft the debt management plan and obtain the approval of the MIC minister (or the prefectural governor), based upon the general approval standard.


◆ Issuers with the ratio between 25% ~ 35% must draft the financial soundness plan required by law and obtain the approval of the MIC minister (or the prefectural governor), based upon the general approval standard.

◆ Issuers with the ratio of 35% or more must draft the financial rebuilding plan and obtain the approval of the MIC minister. Otherwise, Issuers are prohibited from debt issue excluding disaster rehabilitation projects, etc.



Control of fiscal discipline

- In Japan, there is a system of maintaining fiscal discipline by checking the fiscal conditions of LGs through the disclosure of relevant information, and taking measures for early-stage improvement of fiscal conditions before they seriously deteriorate.
- Under this system, local residents, local assemblies and auditors are to examine latent risks of relevant local public corporations and third-sector companies in addition to LGs.
- These examinations are designed to confirm both flow and stock indicators from the perspective of ensuring the medium- and long-term improvement of fiscal management.
- In addition, if the rehabilitation by LGs on their own is deemed difficult, the central government will play a role to ensure their rehabilitation.

- 
- The fiscal conditions of local governments are checked in detail in terms of both flow and stock.
 - The fiscal conditions of related entities are also checked in order to prevent unforeseen liabilities.
 - As of the end of FY2015, only 1 LG exceeds the early warning limit, and this LG exceeds the reconstruction limit(out of a total of 1,788 LGs).

Control of fiscal discipline (2)

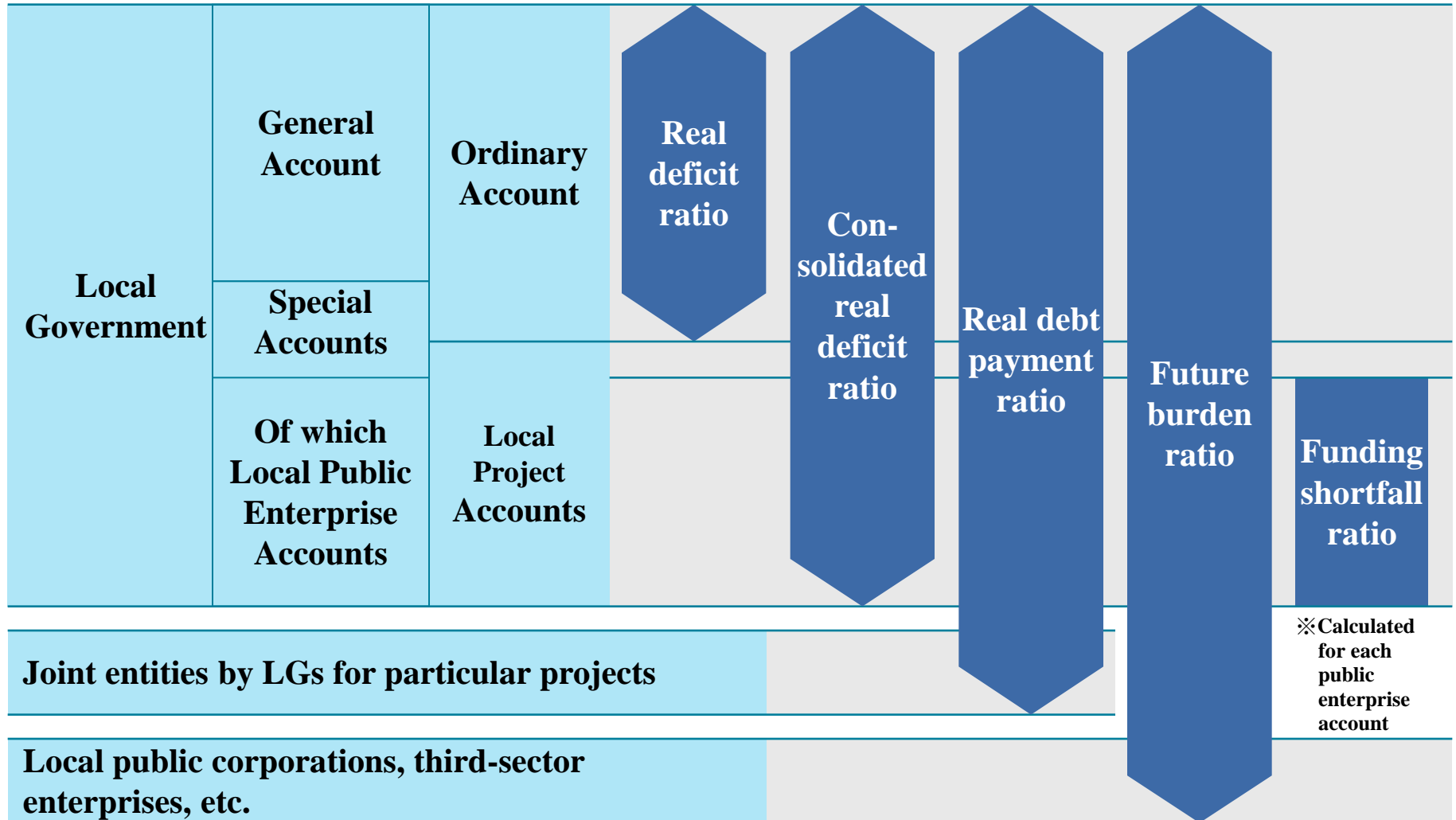
- ◆ LGs are required to report the following ratios to the local assembly every fiscal year after receiving an assessment by the auditor, and to disclose those ratios to the public.

Fiscal indicator	Definition
1. Real deficit ratio	The ratio of deficit to the standard financial scale.
2. Consolidated real deficit ratio	The ratio of consolidated deficit in the all accounts to standard financial scale.
3. Real debt payment ratio	The ratio of debt payment by general revenue to standard financial scale.
4. Future burden ratio	The ratio of outstanding debt as well as contingent liabilities of public enterprises and government affiliates, to standard financial scale.
5. Funding shortfall ratio at Public Enterprises	The ratio of the previous fiscal year's shortfall in funds for each public enterprise to the previous fiscal year's business scale.

Limits for Early warning and reconstruction

	Early warning limit	Reconstruction limit
1. Real deficit ratio	Prefectures: 3.75%	Prefectures: 5%
	Municipalities, depending on fiscal size: 11.25 ~ 15%	Municipalities: 20%
2. Consolidated real deficit ratio	Prefectures 8.75%	Prefectures: 15%
	Municipalities, depending on fiscal size: 16.25 ~ 20%	Municipalities: 30%
3. Real debt payment ratio	Prefectures, and Municipalities: 25%	Prefectures, and Municipalities: 35%
4. Future burden ratio	Prefectures and government-designated cities: 400%	
	Municipalities: 350%	
Management Improvement limit		
5. Funding shortfall ratio at public enterprises	20%	

Scope of fiscal indicators in the Law



Revision of consultation system for the issuance of LGB

- ◆ Notification system for the issuance of LGB was introduced from FY2012 by revising the part of consultation system in order to enhance the independence and autonomy of LGs.

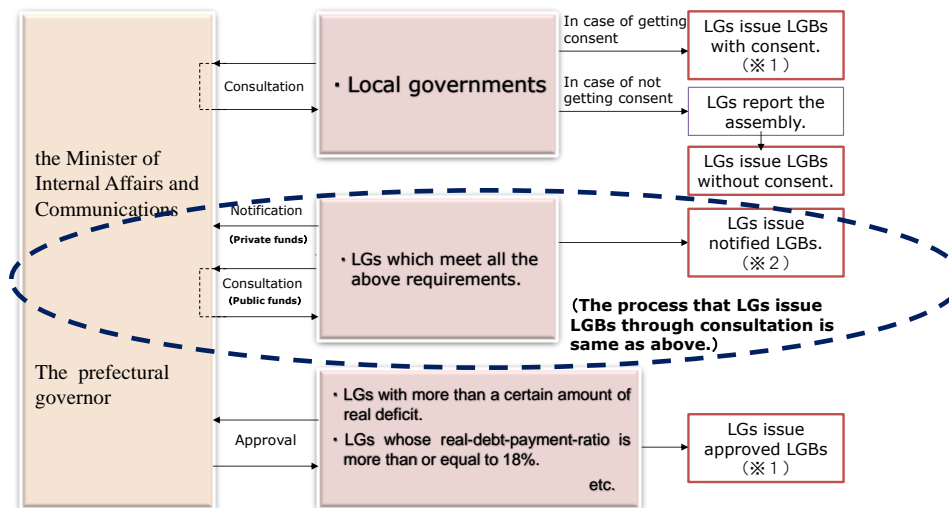
1. Conditions of LGs that don't need consultation when they issue LGBs

If they meet the following requirements, LGs can issue LGBs[※] without the consultation with the Minister of Internal Affairs and Communications or the prefectural governor. [※]LGBs by private funds only.

- ① Real debt payment ratio is less than 18%.
- ② Real deficit is 0.
- ③ Consolidated real deficit ratio is 0.
- ④ Future burden ratio is less than 400% (prefectures and government designated cities) or 350% (municipalities).

2. Local Allocation Tax system

Debt payment for notified LGBs which are approved that LGs could issue with the consent if they consult with the Minister of Internal Affairs and Communications or the prefectural governor is included in Local Allocation Tax system.



※1 LGBs with the consent(or the approval) are approved to be allocated public funds and debt payment for LGBs with the consent(or the approval) is included in Local Allocation Tax system.

※2 Debt payment for notified LGBs which are approved that LGs could issue with the consent if they consult with the Minister of Internal Affairs and Communications or the prefectural governor is included in Local Allocation Tax system.

Information in English Available on Website

Japan Local Government Bond Association Website

(<http://www.chihousai.or.jp/english/07/investor.html>)

English Publications on JLGBs

English Publications on JLGBs	
Presentation Materials	Local Government Bond System and Market in Japan
	Public Offering Joint Local Government Bond
	Japan Finance Organization for Municipalities
	Kawasaki City
Other issuers	Tokyo Metropolitan Government (TMG), Chiba Prefecture, Shizuoka Prefecture, , Aichi Prefecture, Kyoto Prefecture, Sapporo City, Yokohama City, Kyoto City, Kobe City, Fukuoka City
White Paper	FY2014 Settlement White Paper on Local Public Finance, 2016
Laws and Ordinances	Law on the Fiscal Consolidation of Local Governments
	Local Autonomy Law
	Local Finance Law
	Local Allocation Tax Law

- **Japan Local Government Bond Association**

Website <http://www.chihousai.or.jp/english>

(This includes most comprehensive information in English)

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