



M I C

Local Government Bond System and Market in Japan

**Ministry of Internal Affairs
and Communications**

September 2017

I JLGB as an alternative to JGB

II Safety of JLGB

Appendix

I JLGB as an alternative to JGB

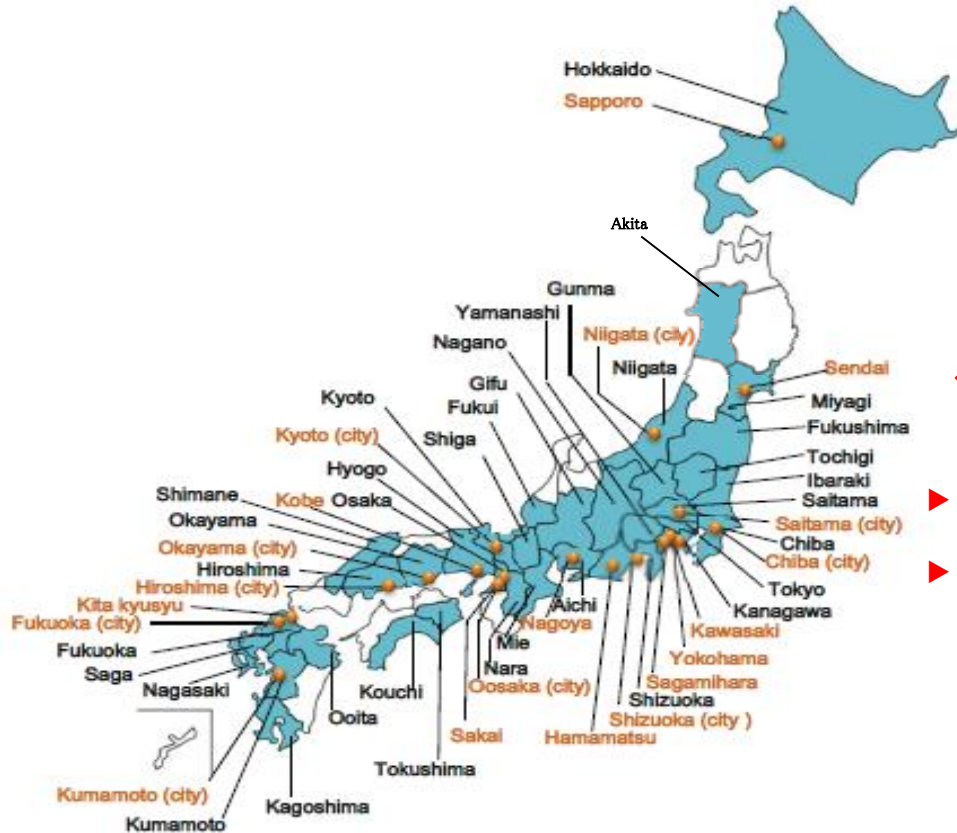
The type and the issue amount of JLGBs and JFM's Bonds (FY2015)

	Denominated in JPY	Denominated in foreign currency
JLGBs	LGB <JPY 5.0 trillion> ≒ USD 45.4billion Joint local government bond <JPY 1.2trillion> ≒ USD 10.89billion	Tokyo Met. <USD 1 billion>
JFM's Bonds	<JPY 1.3trillion> ≒ USD 11.8 billion	<USD 2.5 billion> <AUD 0.1 billion>
Total	<JPY 7.5trillion> ≒ USD 78.0billion	

※【Reference】 Issue amount of JGB (FY2016) :JPY 167 trillion ≒ USD 1,544 billion

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

- ◆ Some LGs successfully issue public offering bonds, supported by the credibility of the local public finance system in Japan.

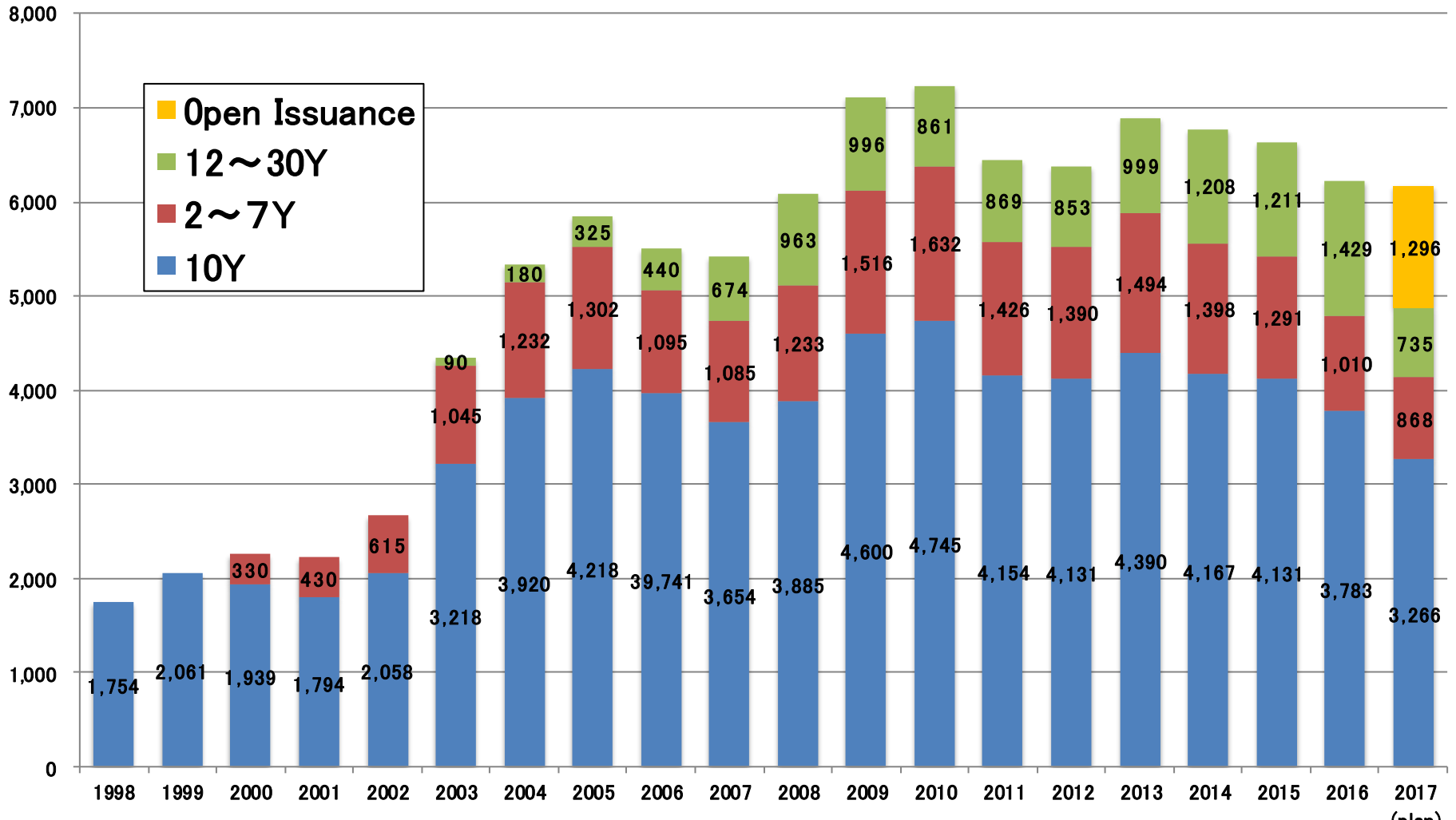


- ◆ 55 LGs issue public offering bonds in FY 2017.
- ▶ 35 prefectures (in black)
- ▶ 20 government-ordinance-designated cities (in red)

ILJGB as an alternative to JGB (diversity of JLGB)

◆ Issue amount of public offering LGBs

(Unit: billions of JPY)



1. **Solid support of the central government for redemption of principal and interest of LGBs**
2. **Check and control system of the central government**
3. **Control of fiscal discipline**

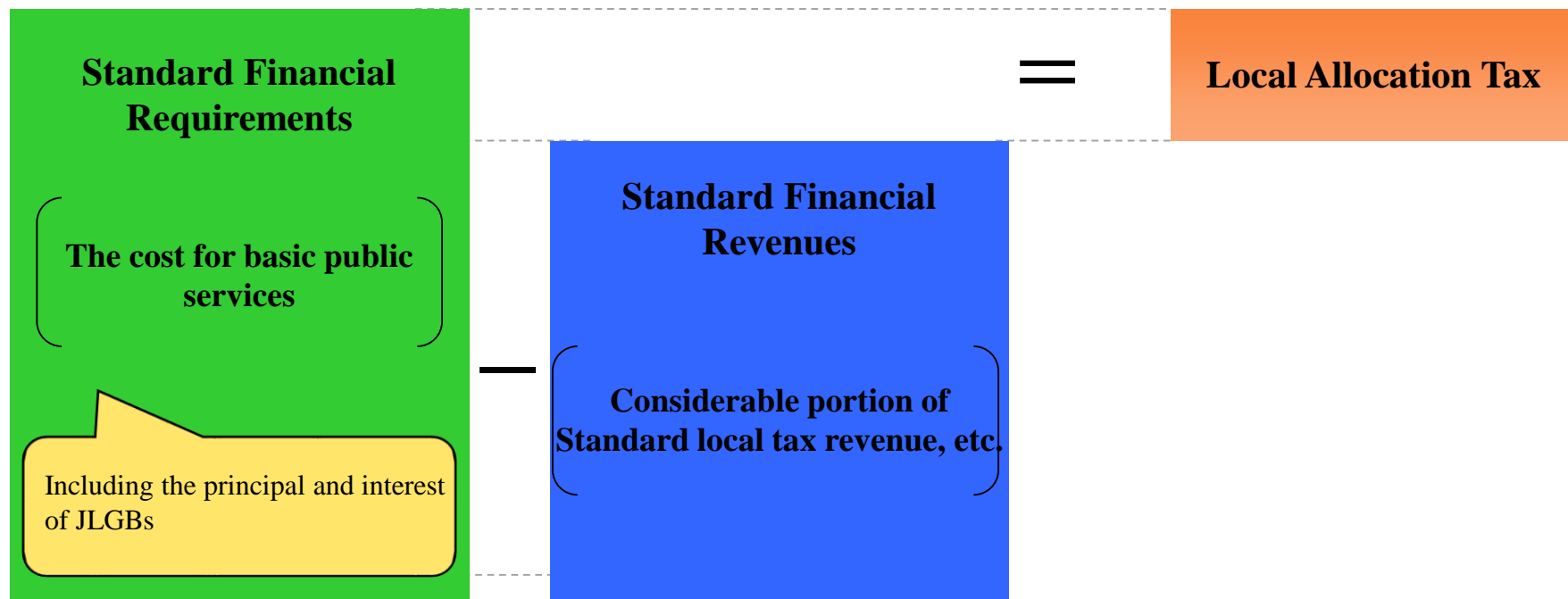
The interest and principal payments of LGBs are fully guaranteed. No LG has ever fallen into the default.

1. II-1 Solid support of the central government

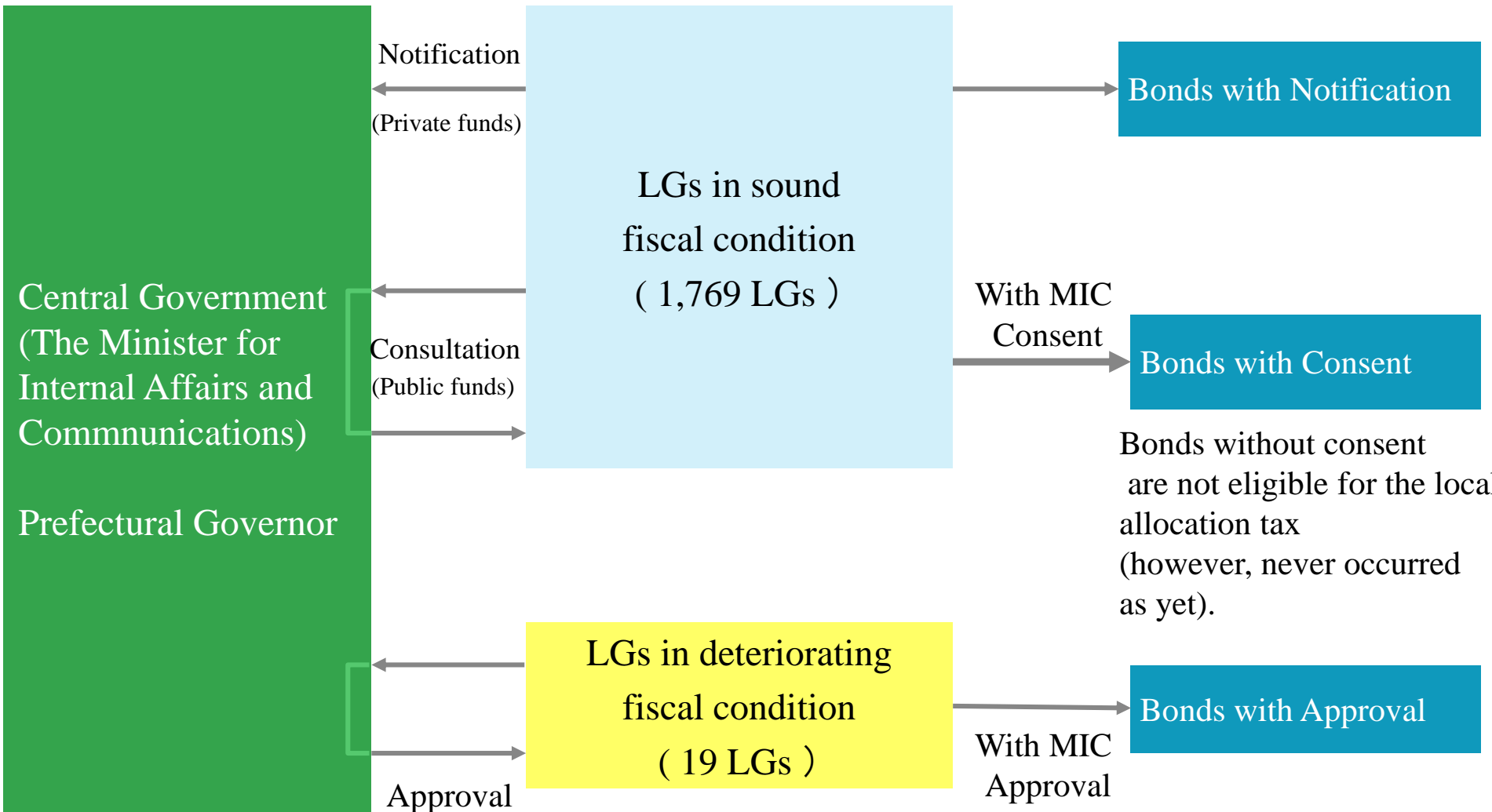
The central government guarantees revenue resources to pay the interest and principal of JLBGs through the local public finance system.

In particular, the payments are ensured through the local allocation tax (each local government receives from the government of Japan to provide basic public services and basic infrastructure to residents.).

The local allocation tax system has functioned for over 60 years since 1954. The amount of the local allocation tax is around 16 trillion yen.



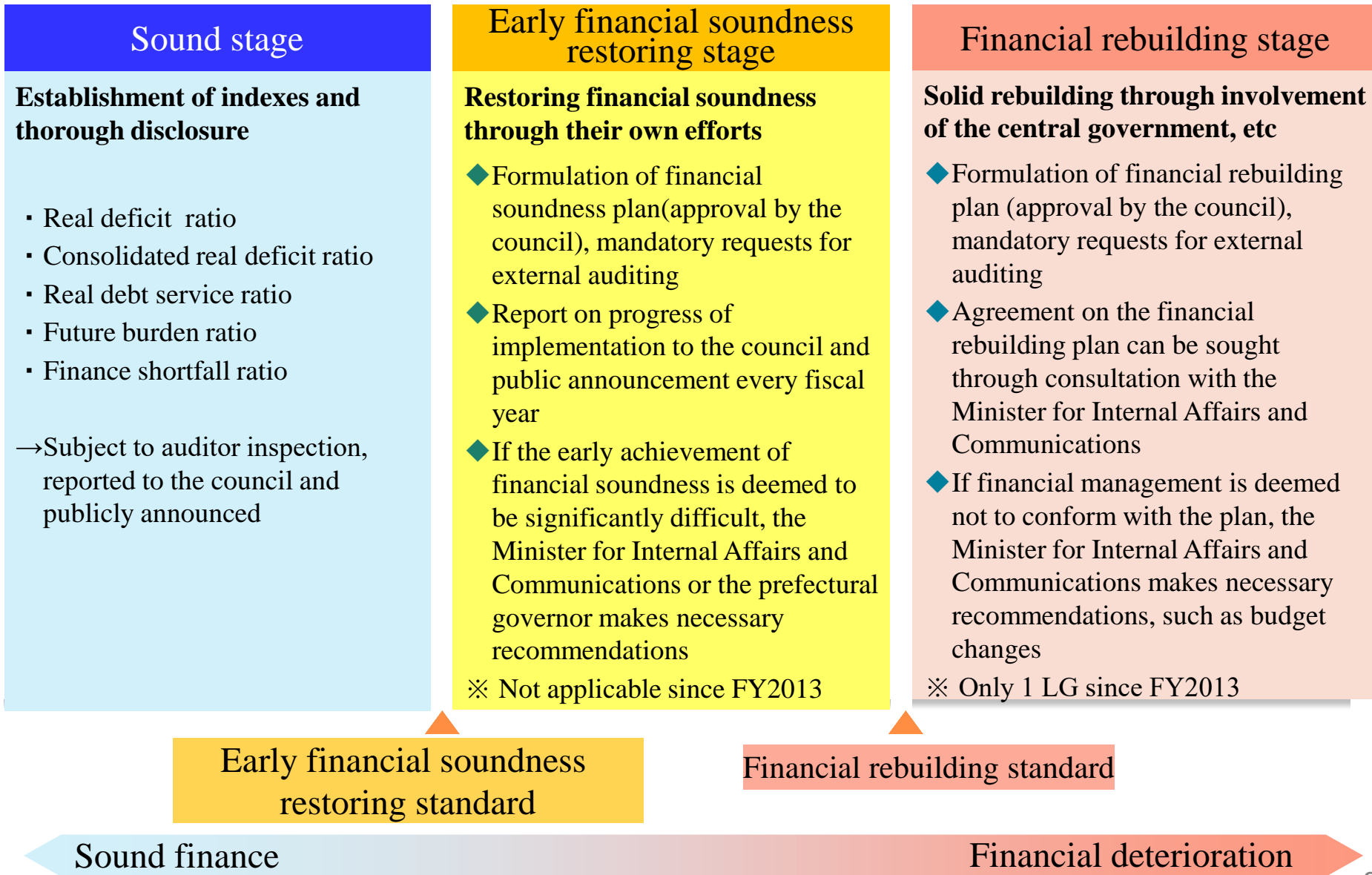
II-2 Check and control system of the central government



Note :LGs are classified by the fiscal condition etc.

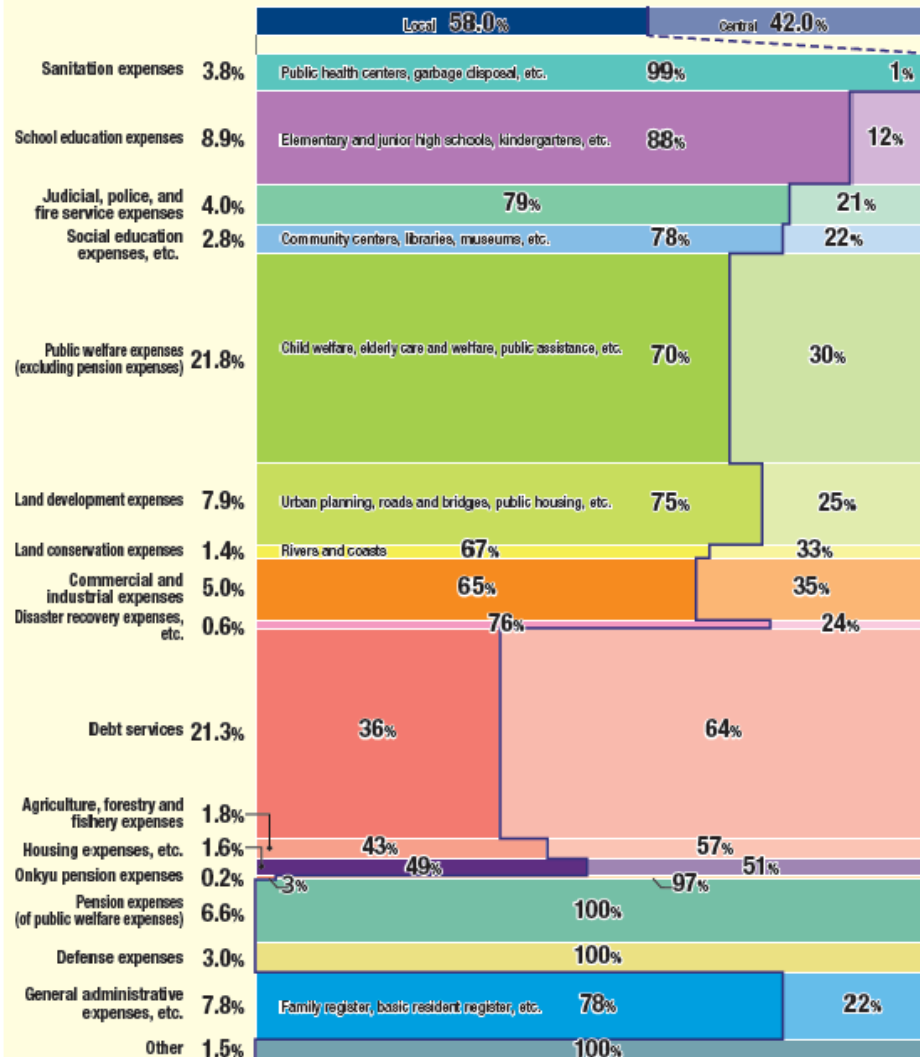
The numbers of LGs (FY2017)

II-3 Control of fiscal discipline



Appendix

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

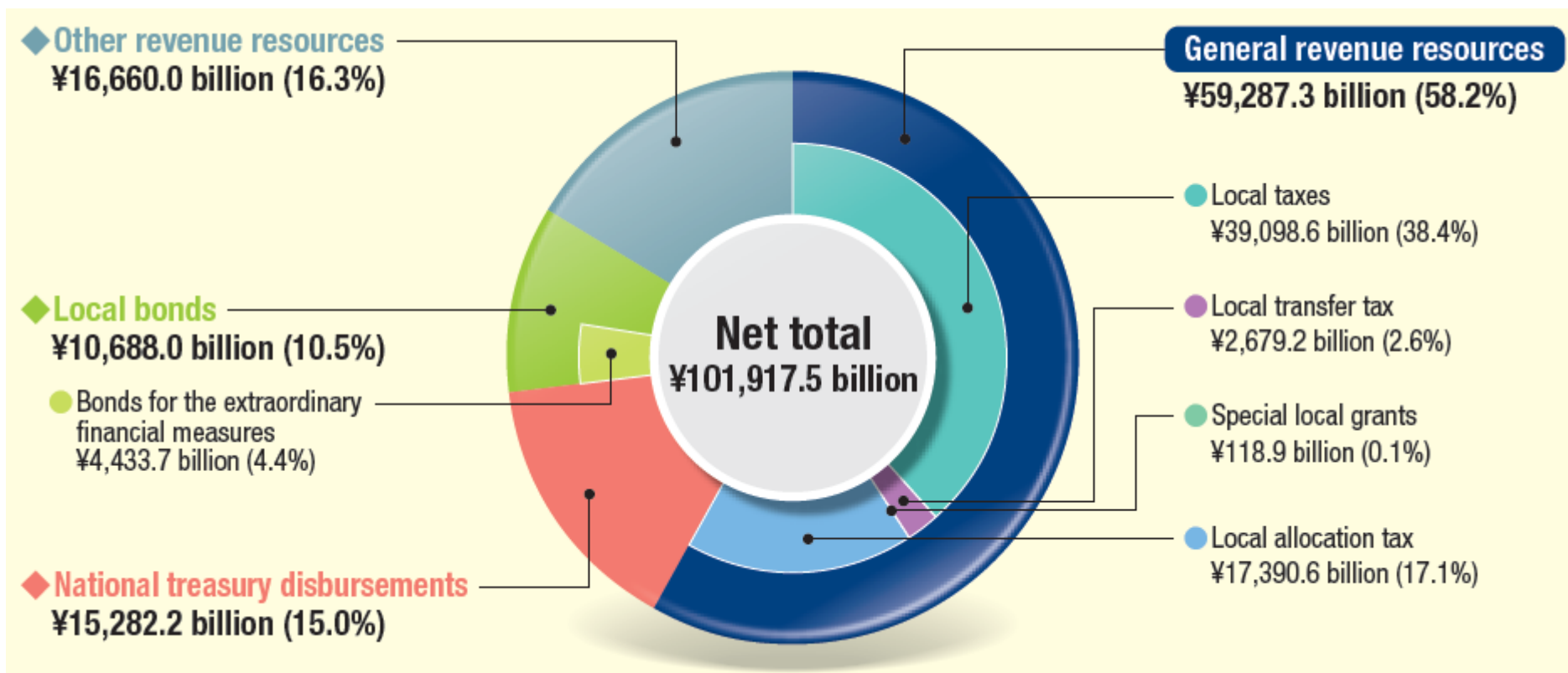


- ◆ LGs take responsibility for and play a major role in the lives of the citizens of the nation.
- ◆ The share of LGs' expenditures is higher in areas that are deeply related to daily life, such as public health and sanitation, school education, social education, and police and fire services, etc.

Source: White Paper on Local Public Finance, 2017 "FY2015 Settlement" by Ministry of Internal Affairs and Communications

The revenue of LGs

- ◆ The revenue of LGs consists mainly of local taxes, local allocation tax, national treasury disbursements, and local bonds, in order of share size.

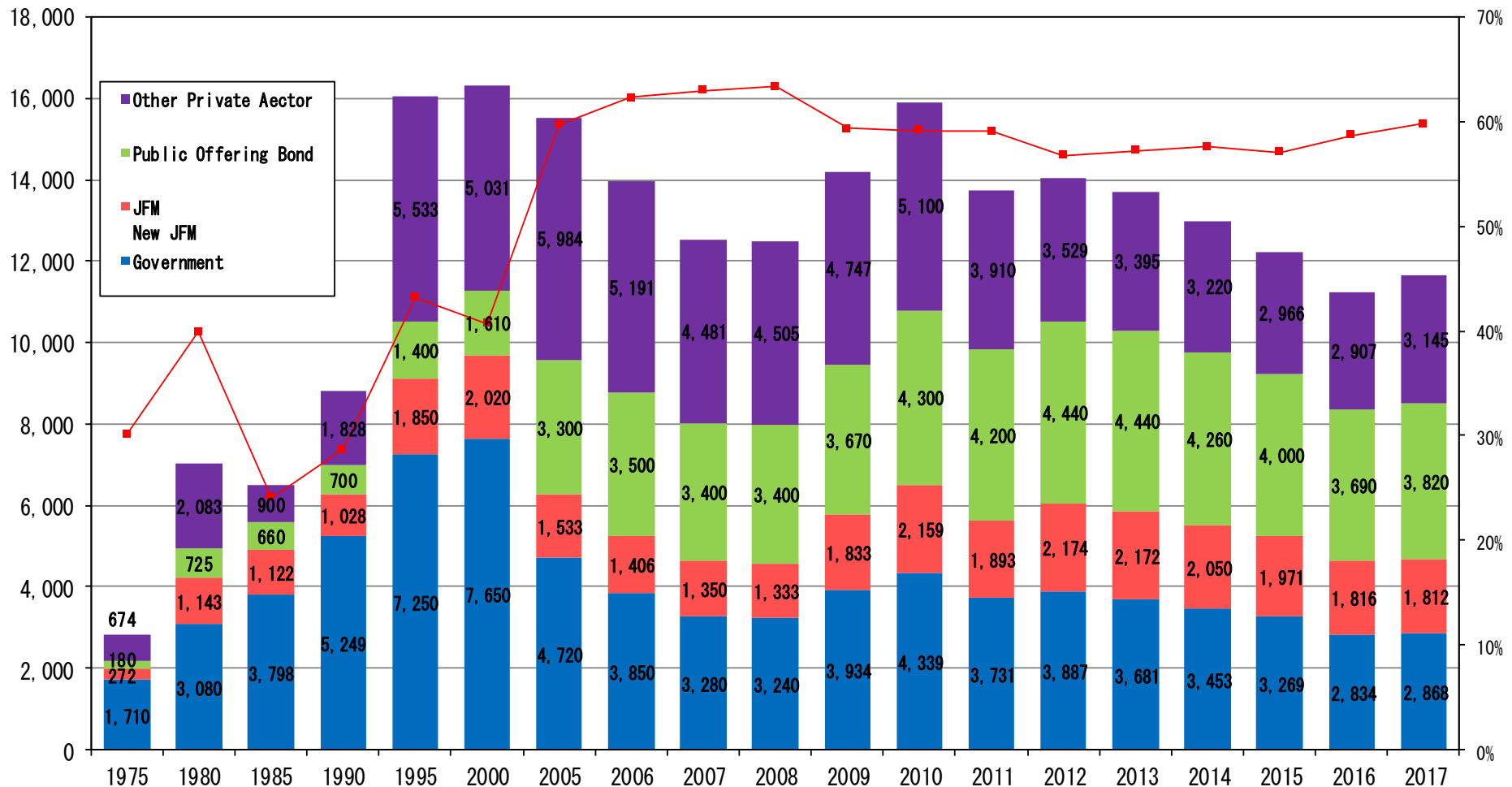


Transition of annual issue amount

- ◆ The share of government funding decreases due to FILP (Fiscal Investment and Loan Program) to minimize that role from FY2001.

(Unit: Billions of yen)

(Unit: %)



↑ FILP Reform from FY2001

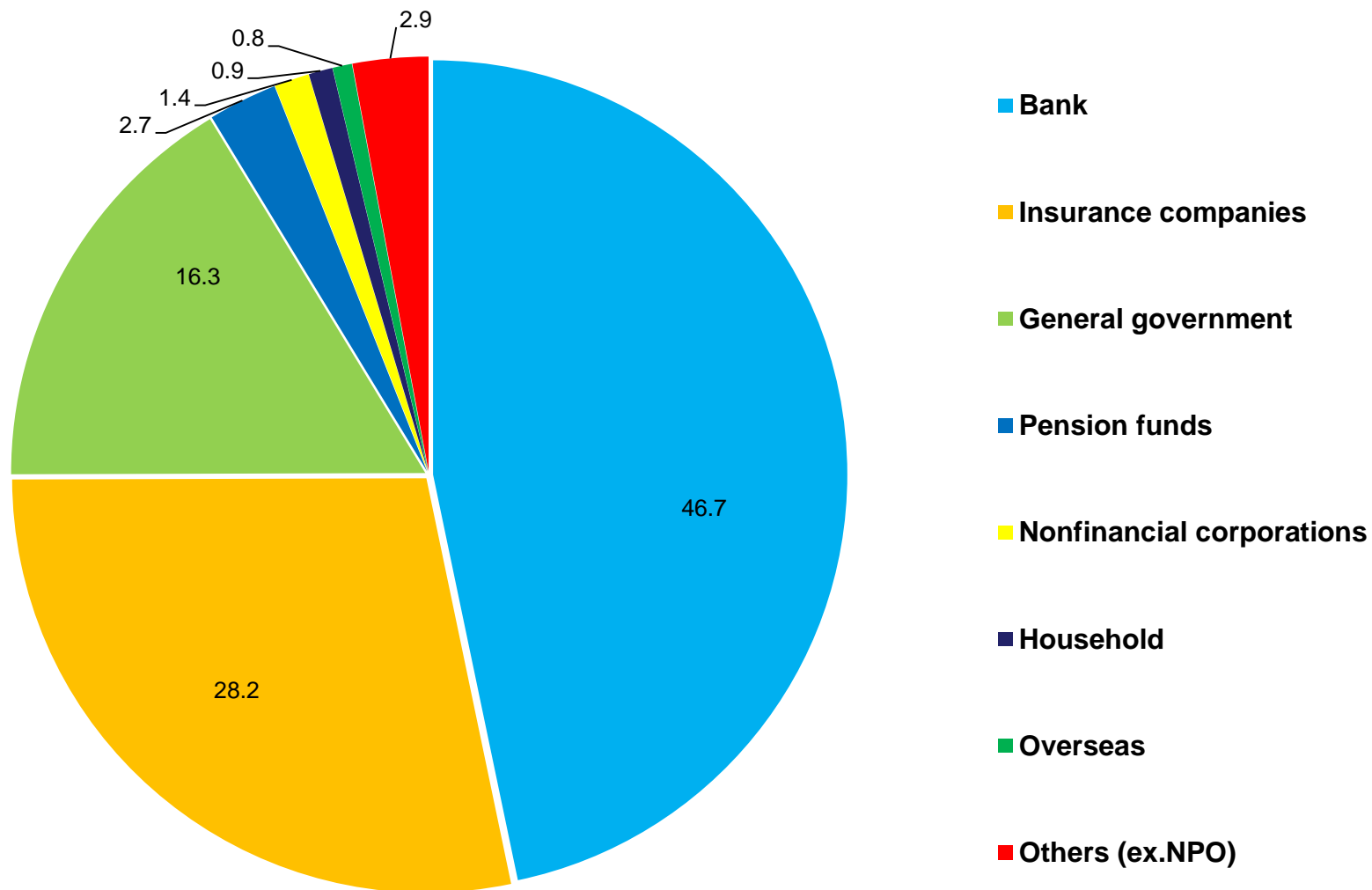
Issuance Plan of Public Offering LGBs in FY2016

(Unit: Hundred Million Yen)

Local government	total	5y	10y	20y or 30y	joint-LGB	other	Local government	total	5y	10y	20y or 30y	joint-LGB	other
Hokkaido	3,100	600	1,200	0	800	500	Kochi	100	0	100	0	0	0
Miyagi	950	100	200	0	350	300	Fukuoka	2,500	300	750	600	0	850
Akita	100	0	100	0	0	0	Saga	100	0	100	0	0	0
Fukushima	550	100	200	0	250	0	Nagasaki	200	100	100	0	0	0
Ibaraki	600	100	100	100	300	0	Kumamoto	500	100	100	0	300	0
Tochigi	100	0	100	0	0	0	Oita	300	0	100	0	150	50
Gunma	500	100	300	100	0	0	Kagoshima	800	100	0	0	700	0
Saitama	3,600	400	1,400	200	500	1,100	Sapporo City	1,350	300	300	0	350	400
Chiba	2,600	400	1,200	400	300	300	Sendai City	600	150	0	150	300	0
Tokyo	4,100	0	2,600	500	0	1,000	Saitama City	100	0	100	0	0	0
Kanagawa	2,900	800	1,200	600	300	0	Chiba City	700	100	300	0	300	0
Niigata	1,200	0	400	200	600	0	Yokohama City	1,500	200	700	200	0	400
Fukui	430	0	200	0	100	130	Kawasaki City	1,060	210	100	300	200	250
Yamanashi	200	0	200	0	0	0	Sagamihara City	100	0	100	0	0	0
Nagano	710	200	0	0	510	0	Niigata City	200	0	100	0	100	0
Gifu	350	0	150	0	200	0	Shizuoka City	350	0	200	0	150	0
Shizuoka	2,600	800	700	500	300	300	Hamamatsu City	200	0	200	0	0	0
Aichi	3,100	200	1,800	200	400	500	Nagoya City	1,180	100	600	200	0	280
Mie	200	0	100	0	100	0	Kyoto City	1,200	200	200	100	350	350
Shiga	100	0	100	0	0	0	Osaka City	2,300	400	400	400	300	800
Kyoto	1,900	400	400	100	600	400	Sakai City	200	0	100	100	0	0
Osaka	6,700	1,200	1,200	0	800	3,500	Kobe City	1,150	0	0	200	200	750
Hyogo	2,300	0	400	1,100	800	0	Okayama City	100	0	100	0	0	0
Nara	300	100	0	0	100	100	Hiroshima City	700	200	200	200	100	0
Shimane	400	100	0	300	0	0	Kita-Kyusyu City	1,050	150	200	200	300	200
Okayama	300	0	200	0	100	0	Fukuoka City	1,400	400	200	200	150	450
Hiroshima	1,370	70	600	200	500	0	Kumamoto City	100	0	100	0	0	0
Tokushima	350	0	100	0	200	50	Total	61,650	8,680	20,600	7,350	12,060	12,960

※This is based on the figures of domestic bonds announced by Ministry of Internal Affairs and Communications in Apr 2017.

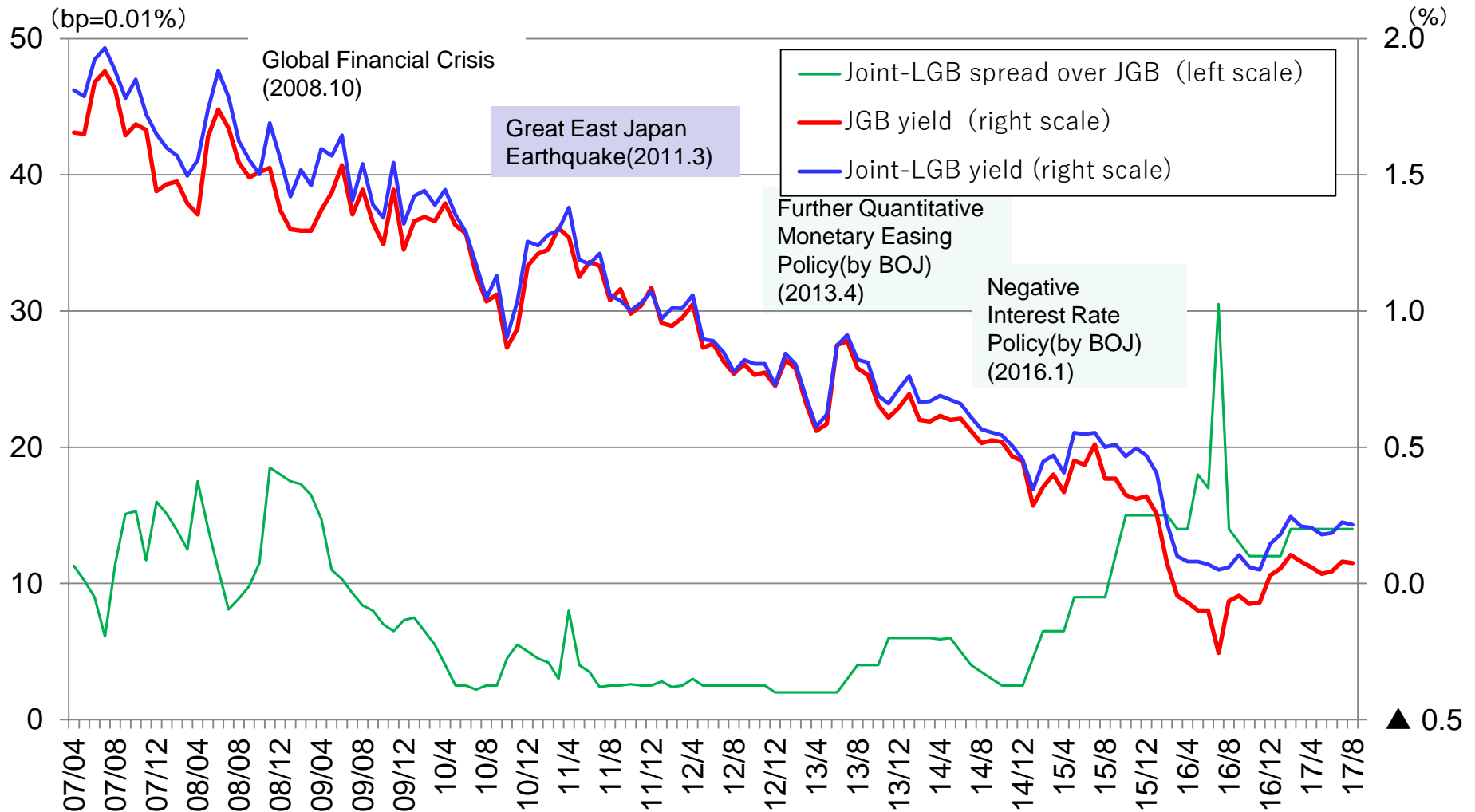
Distribution of JLGB holders (2016/March end)



Source: Bank of Japan “Flow of funds accounts”

Spread of public offering LGB against JGB

◆ Spread of the joint-LGB against JGB



Credit rating of JLGB

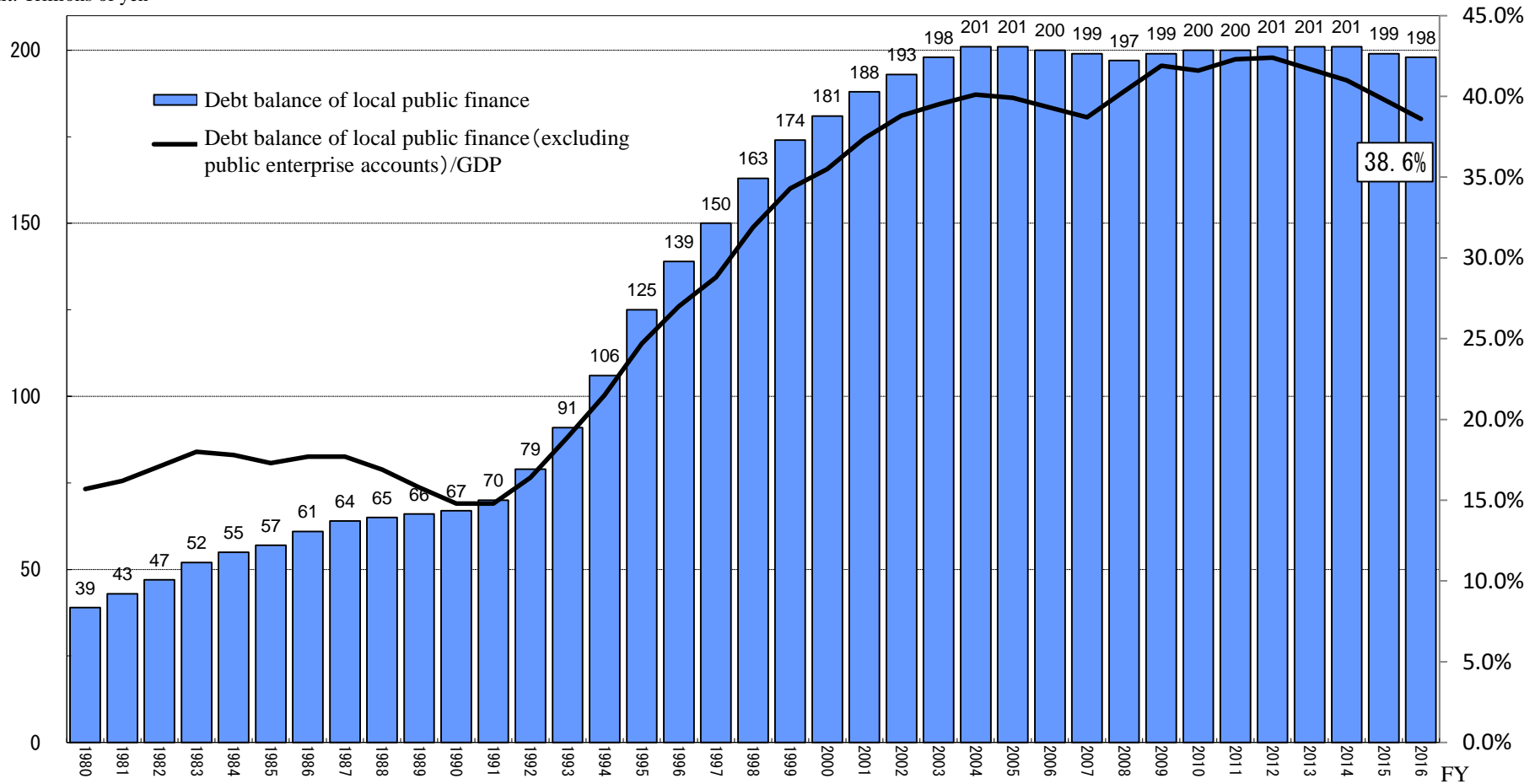
Local Government	Ratings	
	Moody's	S&P
JGB(Central Government)	A1/Stable	A+/Stable
Tokyo	-	A+/Stable
Niigata Prefecture*	A1/Stable	-
Shizuoka Prefecture*	A1/Stable	-
Aichi Prefecture*	-	A+/Stable
Hiroshima Prefecture*	A1/Stable	-
Fukuoka Prefecture	A1/Stable	-
Sapporo City*	A1/Stable	-
Yokohama City*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



MIC Debt balance of local public finance

◆ Debt balance of local public finance is about 200 trillion yen at the end of FY2016.

Unit: Trillions of yen



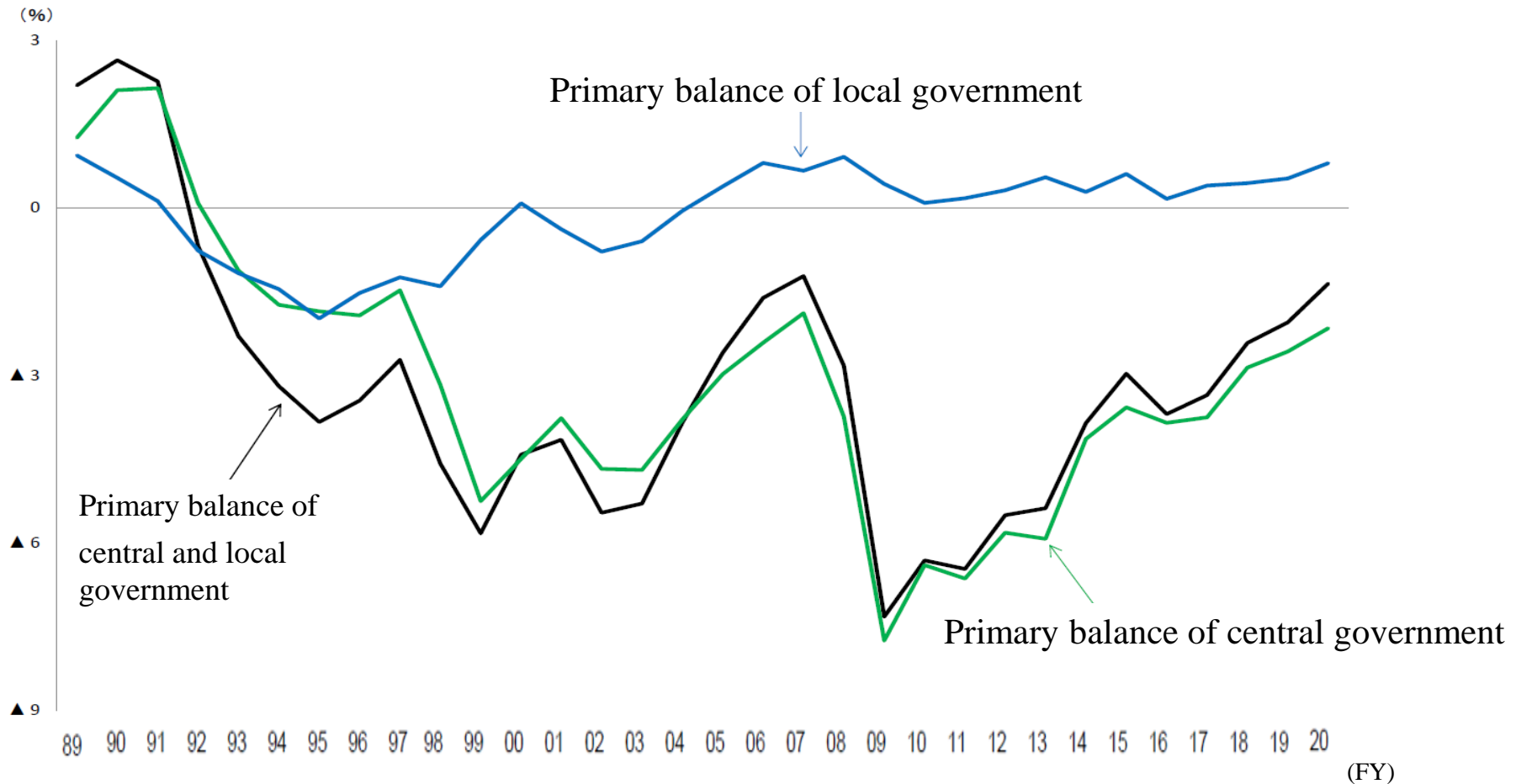
※ 1 Debt balance of local public finance = FY1980 ~ 2015 :settlement based, FY2016:actual valued expected, FY2017:prospction

※ 2 GDP = FY1980 ~ 2015 : actual values, FY2016:actual valued expected, FY2017:prospction

※ 3 Number of decimal places is rounded off.

Trends in Primary Balance of Central and Local Governments against GDP

◆ Primary Balance of LGs was surplus in the past more than 10 years



(Source) FY1989-2016:Cabinet Office "Annual Report on National Accounts"

FY2017-2020:Cabinet Office "Economic and Fiscal Projections for Medium to Long Term Analysis"

How Abenomics Works

The first “arrow”

Aggressive Monetary Policy

The second “arrow”

Flexible Fiscal Policy

The third “arrow”

Growth strategy including structural reform

[Setting the economy on course to overcome deflation and make a steady recovery]
 ※To achieve a nominal GDP of 600 trillion yen

- The third arrow, structural reform, is the core policy within Abenomics
- A plan to establish a new social model - the Growth Strategy 2017 – and realizing Society 5.0 will play a pivotal part
- Abenomics 2.0 will accelerate its efforts towards comprehensive reforms in three vital areas: ① boosting productivity, ② driving innovation and trade, and ③ energizing corporate activities

Economic indicators¹

Category	Indicators	Units	Pre-Abenomics	Post-Abenomics	Progress
Overall	Nominal GDP	JPY	495 tn	537 tn	↗
Corporate performances	Nikkei stock average	JPY	8,803	19,687	↗
	Corporate ordinary profits ²	JPY	48.5 tn	68.2 tn	↗
	Capital investment	JPY	71.8 tn	82.6 tn	↗
Job market	Number of employed persons (female)	Persons	62.7 mn (26.6 mn)	64.7 mn (28.1 mn)	↗
	Jobs to applicants ratio (regular)	%	0.74 (0.44)	1.48 (0.97)	↗
	Unemployment rate	%	4.5	2.8	↗
Fiscal condition	Tax revenue	JPY	42.3 tn	57.7 tn	↗
	Amount of JGB ³ issued	JPY	44.2 tn	34.4 tn	↗
	Level of dependency on JGB	%	38.1	35.6	↗

* Average exchange rate for May 2017: USD = JPY 112

January 2017)

** The Japanese fiscal year starts in April and concludes in March of the following year.

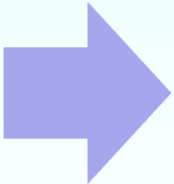
1 Pre-Abenomics vs. Post-Abenomics; FY2012 vs. FY2016 = nominal GDP, corporate ordinary profits, capital investment, amount of JGB issued, level of dependency on JGB; FY2012 vs. FY2017E = tax revenue; Jan 2012 vs. May 2017 = Nikkei stock average; 2012 avg. vs. 2016 avg. = number of employed persons; Jan 2012 vs. April 2017 = jobs to applicants ratio, unemployment rate

2 Source: Nikkei Inc “Nikkei Indexes,” monthly average, closing price

3 Japanese Government Bonds

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) before issuing Local Government Bonds (LGBs).
- LGB issuance without the consent of the Minister of MIC (or the prefectural governor) is not eligible for public funds nor for local allocation tax system (Although LGs can issue LGBs without consent, there have never been such a case.).
- In addition, LGs in deteriorating fiscal condition are required to obtain an approval of the Minister of MIC (or the prefectural governor) when they issue LGBs. In this case LGs can't issue LGBs without approval.

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- The central government (or prefectures) check all the LGBs.
 - The central government guarantees the redemption of LGBs by approving the issuance of LGBs.
 - Issuance of LGBs by LGs in deteriorating fiscal condition is restricted.
(the number of LGs necessary to obtain the approval FY2017: 19 (total LGs : 1,788))



Consultation system for the issuance of JLGB

- ◆ JLGB system was transferred from approval system to consultation system in FY2006 in the process of distributing or dispersing functions, powers, people or things away from a central location or authority(decentralization) . Moreover, notification system was introduced to improve LGs' autonomy while LGs planning to use public funds should adopt consultation system.

1. Consultation

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

2. Allocation of public funds to LGBs with consent

Only LGs with the consent of the Minister of MIC or the prefectural governor may finance from public sectors [Government funds, JFM funds].

3. Inclusion of the debt payments for bonds with consent in Local Allocation Tax system

Debt payments for LGBs with the consent of the Minister of MIC or the prefectural governor are included in Local Allocation Tax system.

4. Obligation to report issuance of bonds without the consent to the council

In order to issue LGBs (Consultation is required) without consent, the head of the LG is required to report the council.

5. Consent standards

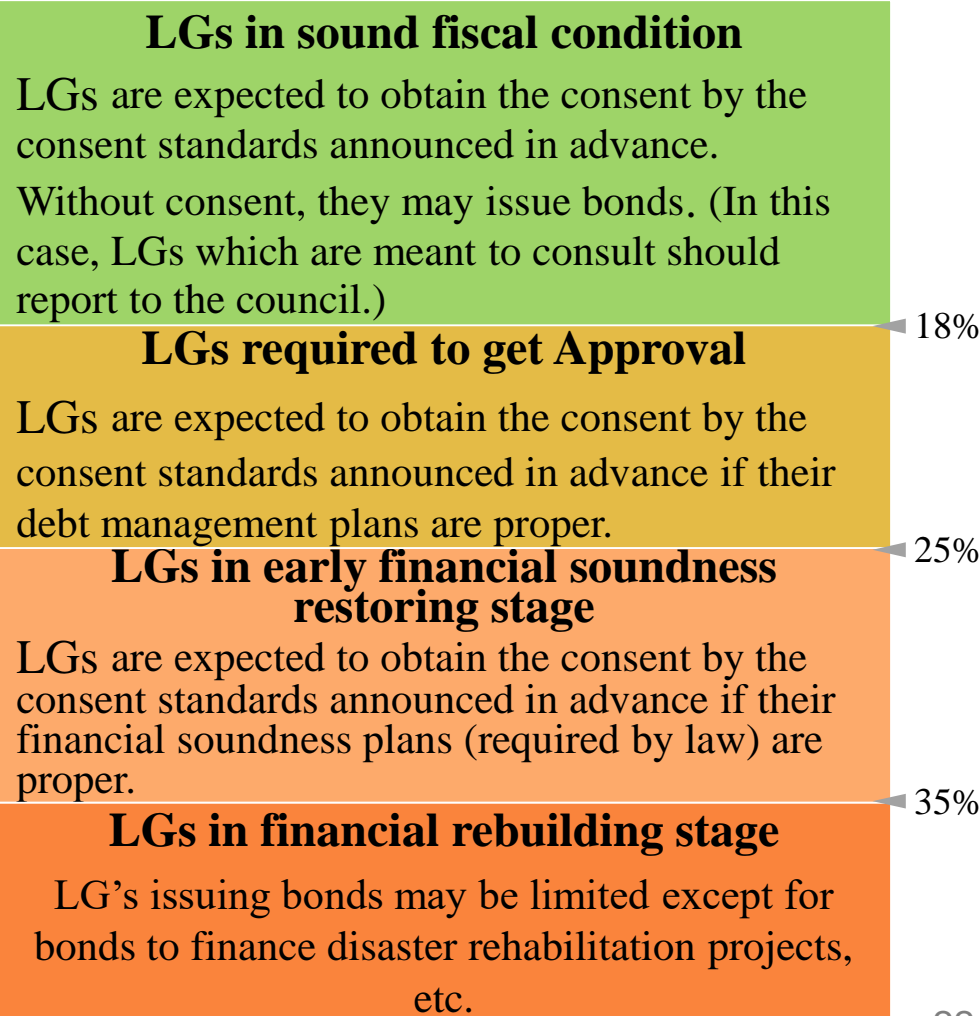
The Minister of MIC announces consent standards every fiscal year in public. LGs in deficit or with high real deficit ratio, or the public enterprises in deficit should be approved to issue bonds by the Minister or the governor.

Consultation system for the issuance of JLGB (2)

◆ In order to maintain fiscal soundness, LGs with high real debt service ratio or in a certain level of deficit are required to get the approval for bond issuance instead of the consultation.


LGs with more than 18% of real debt service ratio are required to get permission.

- ◆ Issuers with real debt service ratio under 18% must consult with, or notify the MIC minister (or the prefectural governor) before issuing bonds.
- ◆ Issuers with real debt service ratio between 18% and 25% must submit the debt management plan and obtain the approval of the MIC minister (or the prefectural governor).
- ◆ Issuers with real debt service ratio between 25% and 35% must submit the financial soundness plan(required by law) and obtain the approval of the MIC minister (or the prefectural governor).
- ◆ Issuers with real debt service ratio more than 35% must submit the financial rebuilding plan and obtain the approval of the MIC minister. Otherwise, Issuers are prohibited from issuing bonds except for bonds to finance disaster rehabilitation projects, etc.



Control of fiscal discipline

- In Japan, a system to maintain fiscal discipline was established. In this system, the central government checks fiscal conditions of LGs through the disclosure of financial information and takes prompt corrective actions to prevent LGs from deteriorating financially.
- Under this system, local residents, councils and auditor inspections confirm potential risk of not only LGs but also relevant entities (local public enterprises, third-sector enterprises, etc)
- These processes are designed to confirm both flow and stock indicators to maintain the soundness of fiscal management in medium- and long- term.
- In addition, if the rehabilitation by LGs on their own is deemed to be 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 financial rebuilding standard (out of a total of 1,788 LGs).

Control of fiscal discipline (2)

- ◆ LGs are required to report the following ratios to the council after subjecting to the auditor inspection and to announce publicly every fiscal year.

Fiscal indicator	Definition
1. Real deficit ratio	The ratio of deficits to standard financial scale
2. Consolidated real deficit ratio	The ratio of consolidated deficits of all accounts to standard financial scale
3. Real debt service ratio	The ratio of debt payment to standard financial scale
4. Future burden ratio	The ratio of debts of LGs as a whole(including third-sector enterprises, public enterprises, etc) to standard financial scale
5. Finance shortfall ratio (for each public enterprise)	An index of the deficit of funds of public enterprises compared to the size of their income, which shows the size of business of local public enterprises, and represents the extent to which financial health has worsened

Limits for Early warning and reconstruction

Early financial soundness restoring standard

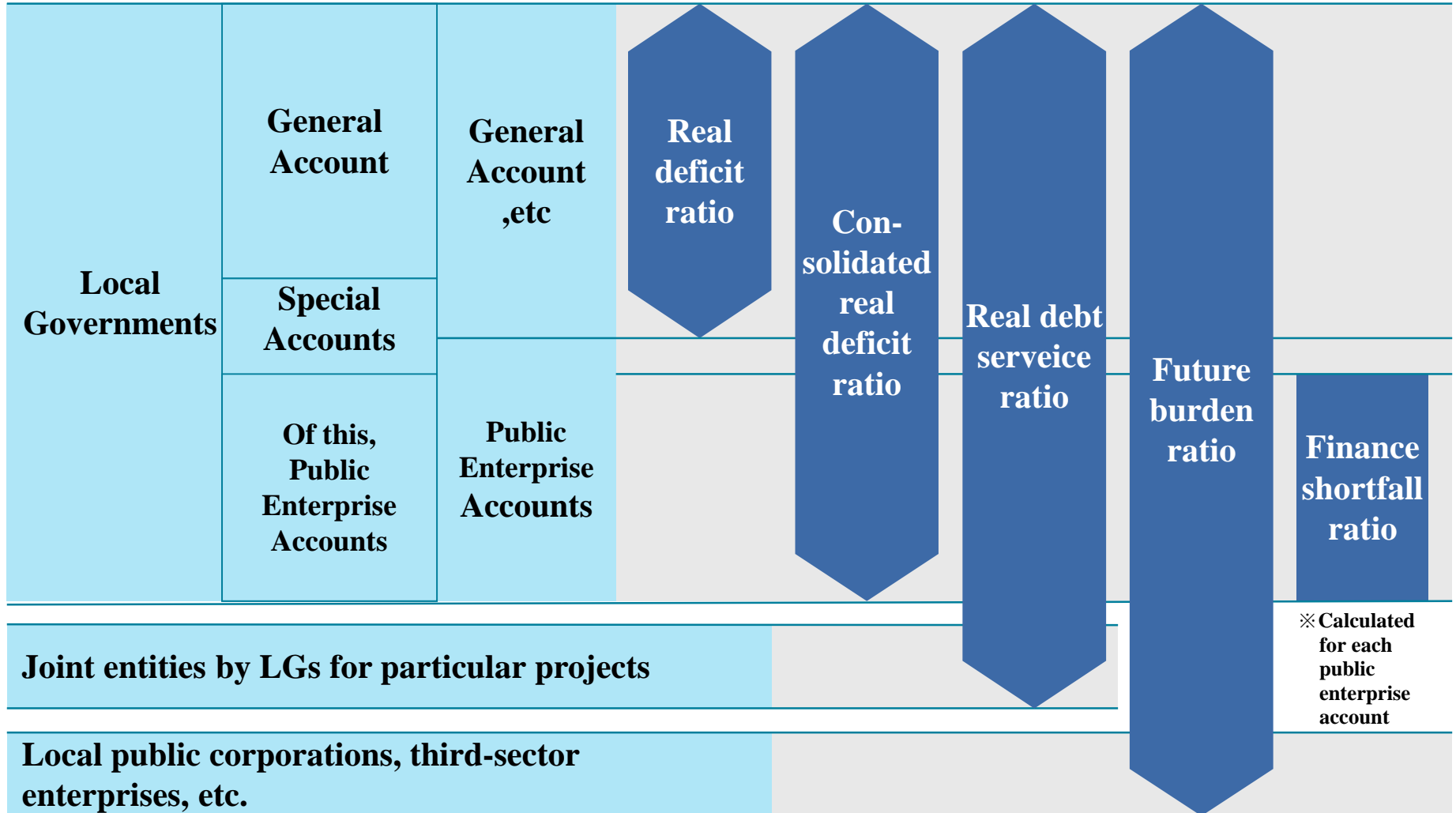
Financial rebuilding standard

1. Real deficit ratio	Prefectures :	3.75%	Prefectures :	5%
	Municipalities :	11.25 ~ 15%	Municipalities :	20%
2. Consolidated real deficit ratio	Prefectures :	8.75%	Prefectures :	15%
	Municipalities :	16.25 ~ 20%	Municipalities :	30%
3. Real debt service ratio		25%		35%
4. Future burden ratio	Prefectures and government-ordinance-designated cities :	400%		
	Municipalities :	350%		

Management soundness standard

5. Finance shortfall ratio (for each public enterprise)	20%
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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.

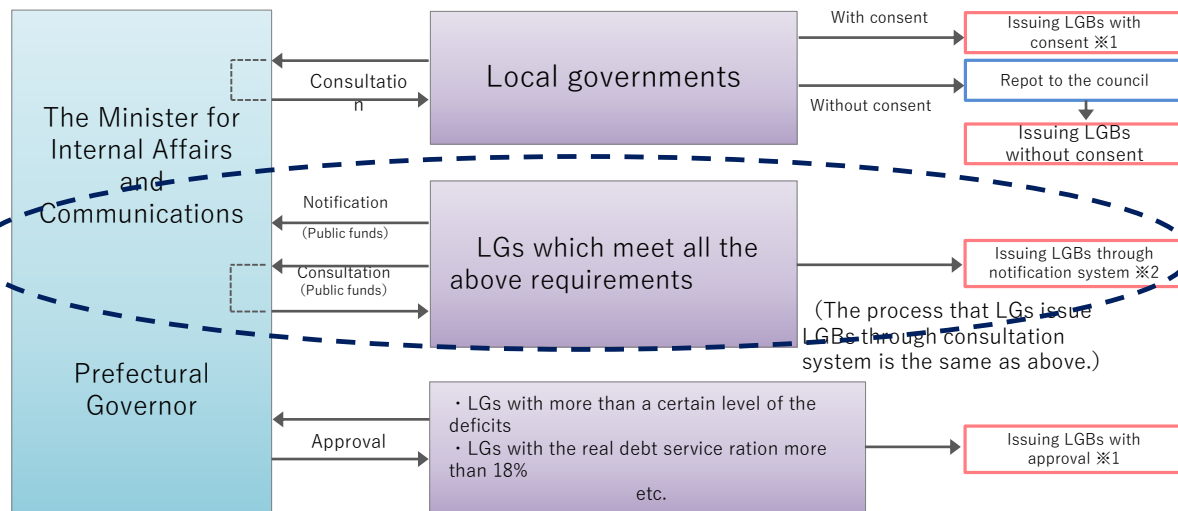
1. LGs that aren't required to consult in issuing LGBs

LGs that meet the following requirements can issue LGBs[※] without consulting with the Minister for Internal Affairs and Communications or the prefectural governor. [※]Only LGs financing from the private sector

- ① Real debt service 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-ordinance-designated cities) or 350% (municipalities).

2. Local Allocation Tax System

Debt payments of LGBs which LGs notified and is to be approved if they consult with the Minister for Internal Affairs and Communications or the prefectural governors are included in Local Allocation Tax System.



※1 LGBs with consent(or approval) are allocated public funds and debt payments of LGBs with consent(or approval) are included in Local Allocation Tax System.

※2 Debt payments of LGBs which LGs notified and is to be approved if they consult with the Minister for Internal Affairs and Communications or the prefectural governor are included in Local Allocation Tax System.

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), Saitama Prefecture, Chiba Prefecture, Shizuoka Prefecture, Aichi Prefecture, Kyoto Prefecture, Sapporo City, Yokohama City, Nagoya City, Kyoto City, Kobe City, Fukuoka City
White Paper	FY2015 Settlement White Paper on Local Public Finance, 2017
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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