New Markets Enter The Battle for Japan's Venture Businesses

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On November 11 1999 "Mothers", the Tokyo Stock Exchange's new market for the trading of stocks in venture firms, opened for business. On November 17 approval was given to two companies, the Internet Research Institute and Liquid Audio Japan, to list their shares on Mothers, and they started trading on December 22. December 24 then saw the official announcement by Nasdaq Japan Planning, who in concert with the US Nasdaq intends to set up a new exchange for start-ups in Japan, that it was to enter into a comprehensive alliance with the Osaka Stock Exchange. The new Nasdaq Japan market is set to start trading from end June 2000. These developments now herald a new age of inter-market competition for venture firms in Japan, a three-way battle between the two new exchanges and the traditional OTC market run by the Japan Securities Dealers Association.

1. The Backgrounds of Competition between Venture-oriented Markets in Japan

1) "Big Bang" and Global Competition between Rival Markets

Traditionally in Japan, the listing of a company on a stock exchange, particularly the prestigious Tokyo (TSE) or Osaka (OSE) stock exchanges, has not been seen as just a way to procure funds or to enhance the liquidity of shares, but is evidence of a certain social status for a company that will enhance its name and also help it to hire better quality staff. Venture start-ups, however, that want to raise funds and have their shares traded, have been expected to list on the OTC market or on regional exchanges. Most of the firms listed on the OTC market have seen a listing on the TSE as their final objective, with graduation from the OTC market to the 2nd section of the TSE, then from there to the 1st section as the firm grows in size the natural ladder of progression.

This traditional view of the structural hierarchy of stock exchanges has been profoundly shaken by the program of financial deregulatory reforms termed the "Big Bang." Overruling a 1983 report by the Securities and Exchange Council, a consultative body to the Minister of Finance, that had stated that the role of the OTC market was to be "auxiliary" to the role of the main stock market, amendments to the Securities Exchange Law passed in December 1998 classed the OTC market on the same level as the regular stock market (Article 67-2), for the first time putting the two markets in direct competition.

On a global level, the competition between stock exchanges has intensified over recent years spurred by the ever greater globalization of the world economy and rapid advances in computer and communications technologies. In the US, while the New York Stock Exchange and the Nasdaq continue to compete over new company listings, there has also been intensifying competition over order flows between the traditional exchanges and the new Electronic Communications Networks (ECNs) and Alternative Trading Systems (ATS) run by securities companies. In Europe a number of new markets have been set up since 1995 – the Alternative Investment Market (AIM) of the London Stock Exchange, the Neuer Markt of the German Stock Exchange, the Nouveau Marche of the Paris Stock Exchange, and EASDAQ, the pan-European equivalent to NASDAQ – which have served to intensify competition over new market listings for venture start-ups (Table 1).

Table 1 Comparison of European Venture Company Stock Exchanges

	UK	Germany	France	Belgium	Japan
Market name	AIM	Neuer Markt	Nouveau Marché	EASDAQ	OTC market
Operated by	London Stock Exchange	German Stock Exchange	Paris Stock Exchange	Europen Association of Securities Dealers Automated Quotation (under the EVCA)	Japan Securities Dealers Association
Established	1995	1997	1996	1996	1963 (computerized in 1991)
Companies listed (registered)	332	163	101	49	859
No. of new listings in 1998	75	46	43	16	61
Market cap.	・ 7.2 bn.	・ 49.6 bn.	・ 6.1 bn.	・ 19.7 bn.	¥19.99 trn.
Ave. market cap. / company	・ 21.7 mn.	・ 300 mn.	・ 60.5 mn.	・ 400 mn.	¥23.27 bn.
Monthly turnover	・ 510 mn.	・ 3.23 bn.	・ 170 mn.	・ 210 mn.	¥1.5 trn.
Listing criteria (main characteristics)	No quantitative criteria. There are no restrictions on selling on, and requires UK/US or IAS accounting standards based information disclosure	Simple quantitative criteria of: shareholders' equity of at least ・ 1.5 mn., free float of at least 100,000 shares, 3 years or longer company history	Simple quantitative criteria of: shareholders' equity of at least ・ 1.5 mn., free float of at least 100,000 shares. No company history requirement.	Minimum of 100 shareholders. Disclosure must be in English.	Requirements different for growth or regular companies. No minimum profitability requirement for growth companies.
Trading method	Combined market-maker and order-matching. It is not obligatory to appoint a market-maker, though must at least appoint a broker who will try to make a market in the shares.	Combined market-maker and order-matching.	Opening and closing rotations set by supply / demand auction, with market-maker in between. Certain issues are traded by two-sided auction.	Market-maker system. If there is only one market-maker, then once per day price is set by a supply / demand auction.	Order-driven type order-matching system. Some market-maker traded issues.

Note: Figures quoted here are true as at end or during September 1999, except where stated.

In April 1998 the TSE requested its Securities Policy Committee to examine the future role of the stock exchange, and in February 1999 the committee submitted a report entitled "The

Future of the Tokyo Stock Exchange - The Way Forward." This report contained many proposals regarding the future position of the TSE in the light of the government's program of financial deregulation and the current state of the Japanese economy. These recommended taking bold steps to change the TSE, from shortening settlement times to an examination of tie-ups with other exchanges, and also looked to the possibility of turning the TSE into a limited company. This report concluded that, since the amended Securities and Exchange Law had placed the OTC and main stock markets in competition with each other in terms of a market for growth companies, and that the OTC was tending towards the use of a market-maker system that would result in an entirely different trading system from the main market, that the size of the company was no longer relevant in choosing on which market to list – instead it should "create an environment" where companies would not feel forced to list on either exchange but could choose according to their own criteria. It further stated that it was necessary for the TSE to encourage the listing of new growth companies in order to provide them with easier access to funding, and that it would be necessary to examine the question of establishing an entirely new market, in concept radically different from the existing market, and aimed at start-up companies.

In fact, the Tokyo Stock Exchange had already set up certain exemptions to its normal listing criteria in order to encourage the listing of companies involved in 'the new economy,' allowing companies who spent over 3% of total sales on research and development to list their shares even if they did not meet the criteria for the first or second sections of the exchange.[1] However the existence of such exemptions was not widely known, partly because the TSE itself had not made much effort to encourage companies to list. As a consequence, no companies to date have taken advantage of them.

The OSE had similar rules in place, but in December 1998 it abolished them to make way for a "New Market Division" that would target growth companies who operated mainly in the Osaka region. In August 1999 the character design and sales company SK Japan was the first to list on the new market, and in November approval was given to the condominium designer and builder SEED.

2) The Nasdaq Japan Project[2]

The announcement on 15 June 1999 that the National Association of Securities Dealers (NASD), the operator of the Nasdaq market in the US, and the major software distributor Softbank were to jointly set up a new stock market called "Nasdaq Japan" opened the curtains on a new era of real competition among Japanese stock markets. The TSE's preparations for setting up its new market aimed at growth companies also jumped up a gear after it heard this announcement.

The plan to set up a "Nasdaq Japan" by the end of 2000, where investors could trade the stocks of both Japanese and US venture companies, was hailed as a daringly fitting plan for the "Big Bang" age, and has attracted a great deal of attention. Nasdaq Japan Planning, the company charged with paving the way for the new exchange, has formed a working group

1 Called the "Special Regulation Market".
2 S. Osaki, H. Hayashi "Nasdaq Japan – The Next Phase of Nasdaq's Global Strategy" (Capital Research Journal, Autumn 1999)

composed of major securities companies who have since September been engaged in drawing up concrete plans for beginning trading on the exchange. It has also since October presided over the "Nasdaq Japan Club," a group of over 2,000 venture firm entrepreneurs who hope to gain a listing on the new market.

Until now Japan has always tended to look to the model of the Nasdaq market, the most successful of its kind in the world, when considering in what form to set up a venture-oriented exchange. The main reason why, when reform of the OTC market is discussed, that it is generally in terms of the introduction of a market-maker system, is that Nasdaq's success has been in a large part owed to its use of just such a market-maker system. This made the news that the original Nasdaq market was going to "invade" Japan even more of a shock to Japan's exchanges and related institutions. On the surface the TSE and JSDA (Japan Securities Dealers Association) did their best to appear calm, but underneath they were naturally feeling a great sense of urgency at the thought that such competition was about to appear in their midst.

JSDA felt that it had been betrayed by the US exchange with whom it had a long history of friendly relations even extending to the exchange of trainees. In August it published a report in which it pleaded for the urgent reform of the OTC market. It called for a market at which small venture firms could easily find access to capital, and that would also attract the global investment community. In order to achieve this it proposed more flexible listing requirements, a reduction in market registration times, and a market-maker based trading system. It also proposed a "Green Sheet market," modeled on the US "Pink Sheet", market for unlisted and unregistered stocks with an increased frequency of quotes.

Meanwhile the TSE was frantically trying to flesh out its own plans for a new venture-oriented exchange based on the Securities Policy Committee report, and in September it announced it was setting up a new market called "Mothers" (Market of the high-growth and emerging stocks). The exchange moved fast to amend the regulations governing the exchange, and the new market officially opened in November and started to consider listing applications. The new market received a lot of attention when top TSE's executives were found to be visiting the offices of venture companies in order to drum up listing applications.

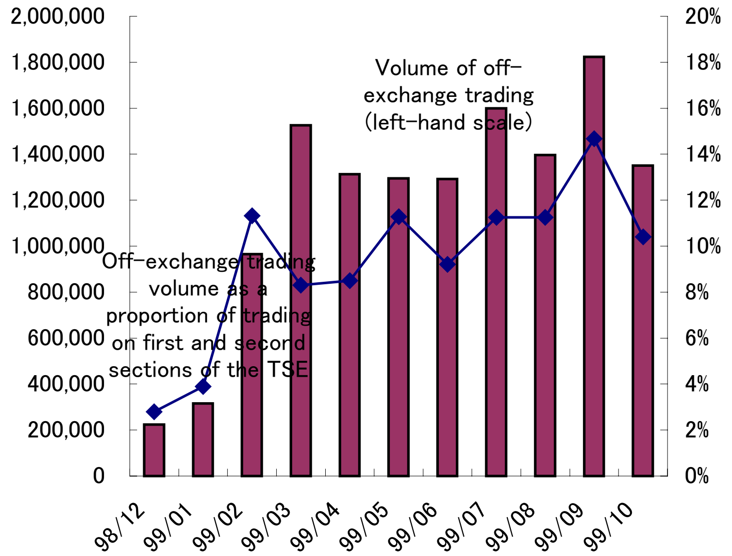
The "Mothers" market was, in essence, a fundamental reform of the existing but non-functioning Special Regulations Market, based on the February report by the Securities Policy Committee, and as such the Nasdaq plan announced in June was not the direct cause. However the fact that it was set up so unusually quickly was no doubt due to the challenge from Nasdaq Japan. The atmosphere of confrontation however in effect helped to give TSE some publicity for the new exchange.

3) The effect of the lifting of the ban on off-exchange trading

It is also important not to overlook one other development that, though indirectly, also motivated the TSE to hurry in setting up a new market - the increase in off-exchange trading since December 1998. This was caused by the substantial relaxation of the severe restrictions on off-exchange trading, allowing members of the exchange to handle such trades given certain restrictions such as on price-setting and reporting requirements to the JSDA.

Since March 1999 the amount of off-exchange trading has remained at a fairly constant 1.2 ~ 1.5 billion shares traded per month, equivalent to some 10 ~ 15% of the trading volume on the TSE itself (Figure 1). On a volume basis, 55.5% of the total trades from January 1999 to October 1999 have been basket orders, with 37.4% being large basket orders of over ¥50 million. This would indicate that off-exchange trading, which institutional investors turn to in order to execute large orders while minimizing the market impact of the trades, has developed into a properly functioning market.

Figure 1 Off-exchange trading in listed shares



Source: Japan Securities Dealers Association, Tokyo Stock Exchange

The increase in off-exchange trading is linked directly to a decrease in exchange commission for the TSE, and is in effect another competing market formed by securities houses themselves. That the TSE saw this as a competitive threat, and that this spurred it on to form plans for a new market to answer the challenge, is probably not far off the mark.

2. The Tokyo Stock Exchange's New Venture-Oriented Market – "Mothers"

The new "Mothers" market run by the TSE was officially opened on 11 November, and on 17 November approved the listing of its first issues, Internet Research Institute Inc., and Liquid Audio Japan Inc.. Trading in these two stocks started on 22 December, but swamped by buy orders the stocks were left untraded for the first day and priced bid-only on a wave of novelty interest in the new market.

The name "Mothers" is both an abbreviation of the new stock market's stated purpose (investment in high-growth and emerging stocks) and is intended to imply the nurturing of these emerging businesses under the caring and watchful eye of the TSE. Ranked equal yet separate to the existing first and second sections of the TSE, it is in concept entirely different. It is aimed at companies recognized for their high growth potential, either because they are companies that operate in a growth field, or because they are advanced in terms of technology or the originality of their business concept. The listing requirements are much more relaxed than on the traditional sections, but at least as far as the TSE is concerned, rather than a simple lowering of standards, this represents a proactive attempt at cultivating a new type of company.

The Mothers market is characterised by the following features:

(1) Easier listing requirements

The listing requirements have been made easier than for the existing first and second sections of the TSE, for instance allowing the listing of companies without recorded profits. In order to compete with those markets the listing requirements have been set at the same level as those announced by the rival OTC and Nasdaq Japan markets (Table 2).

At the same time, to allay fears that shares in smaller companies may not achieve sufficient liquidity, efforts have been made to maximize the amount of shares being actively traded, by for example stipulating that on listing a company must make a public offering of at least 1,000 shares (of face value ¥50,000), and that the listing must create at least 300 new shareholders. Further, the stock will be de-listed if the average monthly traded amount is less than 10 shares (of face value ¥50,000), or if the stock remains un-traded for a period of 3 months.

(2) Lifting of regional jurisdiction restrictions

Up to now Japan's 8 stock exchanges have operated on the basis that each has a local "jurisdiction" area, so that if a company wishes to list on an exchange in another jurisdiction area, it must first have a listing on its own local exchange. Further, other exchanges also impose more stringent listing requirements on companies outside their own jurisdiction areas.

In contrast the Mothers market is not required to have the Tokyo area (Kanto and Tohoku regions, plus Shizuoka, Yamanashi and Nagano prefectures) as its jurisdiction, and can open its doors to companies from all over Japan. In fact, there are already 2 companies based in Osaka on the waiting list as candidates for listing (Table 3).

Table 2 Share listing requirements for OTC, Mothers and Nasdaq Japan markets

Listing, registration criteria	OTC market: Regular Companies (Grade 1)	OTC market: Venture Companies (Grade 2)	Mothers	Nasdaq Japan: Growth company criteria
Company	No restriction	Company is under 10 years old (or operating history for its core businesses of under 10 years), or if 3% or more of total sales is spent on R&D for new or core businesses.	Companies recognized as having significant growth potential on account of either being involved in a business sector that is expected to show high rates of growth, or on account of the business being based on advanced technology or business concepts.	Net assets of ¥400 million or market capitalization of ¥5 billion or more, or pre-tax profits of ¥75 million.
Outstanding share issuance	Enough to create a healthy secondary market		-	-
Shareholders	At least 300 shareholders for total issuance of under 10 million shares on registration date, or 400 for share issuance of 10 million or more and under 20 million, or 500 for 20 million shares or above		At time of listing 300 additional shareholders must be created	300 or more
No. of shares in public offering	Free float ratio of 30% or more or at least 500,000 shares		An offering of at least 1,000 trading units at time of listing	Free float of at least 1000 trading units. Secondary offering / IPO of at least 500 trading units.
Profits	Net profits in the black at both parent and consolidated levels	-	The firms high growth / new technology operations must be already achieving sales	-
Net asset value	¥200 million or over the previous term end at both parent and consolidated levels	Market cap. at listing of ¥500 million or more	Market cap. at listing of ¥500 million or more	Free float of ¥500 million or more
Other	-		Auditor's opinion on auditors report does not need to be "unqualified" ("fair" and "valid" accounting information is sufficient)	-
Cancellation, de-listing conditions	**OTC market**		**Mothers**	**Nasdaq Japan**
Outstanding issuance	Under 2 million shares		-	Where the free float is under 500 trading units
Shareholders	No. of shareholders at the end of the immediately preceding accounting term is under 150		Under 150 for a period of 1 year	Under 300
State of business	Excess liabilities in each business operation for the last 3 years running at term end		Excess liabilities in each business operation for the last 3 years running at term end	-
Issue liquidity	Average monthly trading of under 10,000 shares for last 6 months		Average monthly trading of under 10 trading units for the past year, or no trading in the last 3 months	Market value of free float goes under ¥100 million
Other	A pricing ratio (the ratio of shares on which a price is set through the conclusion of a trade in any day's trading to the total share issuance) rule has been recently added, where an issue can be de-listed if the average pricing ratio is below 20% for the past 6 months		-	-

Note: Nasdaq Japan public offering criteria are current proposals
Source: NRI, from various materials supplied by the parties concerned

Table 3 Companies listed on Mothers and candidates for listing

Company	Head-office location	Main area of operations
Internet Research Institute	Tokyo (Minato)	Support of internet related technologies, research and development contracting
Liquid Audio Japan	Tokyo (Shinjuku)	On-line music distribution
Met's Corporation	Tokyo (Minato)	Computer software development
Crayfish	Tokyo (Shinjuku)	Internet technology development
Snova	Tokyo (Chuo)	Artificial skiing facilities development
Cyber Agent	Tokyo (Minato)	Internet advertising
On the Edge	Tokyo (Minato)	Systems development
NextWare	Osaka	Systems development, consulting
ValueClick Japan	Tokyo (Bunkyo)	Internet advertising
Global Insurance	Tokyo (Chiyoda)	Financial / insurance consulting
Digit	Tokyo (Minato)	Internet-related publishing and advertising
Plat'Home	Tokyo (Chiyoda)	PC peripherals and software development
NSJ	Tokyo (Minato)	Electronic verification related software development
Access	Tokyo (Chiyoda)	Software development for mobile data terminals
V-Sync	Tokyo (Shibuya)	Digital music distribution
Nihon Tsushin	Tokyo (Shinagawa)	Re-sale of telephone line space
Planex Communication	Tokyo (Chiyoda)	Networking equipment sales
Autobytel-Japan	Tokyo (Koto)	On-line car sales
Magclick	Tokyo (Shibuya)	E-mail advertising
Dream Arts	Tokyo (Minato)	Network development, consulting
Site Design	Tokyo (Chiyoda)	Systems development, consulting
Colour Field	Tokyo (Shibuya)	On-line direct marketing
SFD	Tokyo (Chiyoda)	Internet related services
Xaxon	Osaka	Internet connection
Netweb	Tokyo (Minato)	Internet related services

Note: Companies with bold have been listed by 6 April 2000. Other companies are reported to be candidates on Nihon Keizai Shimbun, 25 November 1999.

(3) Simplified listing procedures

In order to simplify the listing procedure for start-up companies, Mothers has introduced various measures that help to lessen the expense and procedures involved. For example, in terms of listing reports it does not require the submission of the Securities Report (so-called Section II of the annual report) that has been often criticized for taking an inordinate amount of time to complete. Further, fees for the examination of a listing application are only half those of existing exchanges, while it also gives a discount (for the first 3 years) on the annual listing fee. The time taken to examine a listing application has also been brought down to around 1 month.

(4) Disclosure

While start-up companies aiming at listing on the new Mothers market will on the one hand have higher growth prospects than companies listed on established markets, on the other hand the risk of investing in them is also assumed to be greater. Accordingly, Mothers requires the disclosure of detailed risk related information, and the examination of the company for listing will concentrate on the appropriateness of the corporate and risk information provided.

Further, subsequent to listing a company is required to submit quarterly earnings reports, not obligatory under Japanese Securities and Exchange Law, and to hold an analysts meeting twice a year for three years following the listing. The TSE also offers the use of its own facilities for the holding of these meetings.

3. Recent Developments Concerning The OTC Market And Nasdaq Japan

1) The OTC Market

As mentioned previously, the JSDA, operator of the OTC market in Japan, had appeared positive towards the subject of market reform by publishing a report advocating an action plan to accelerate those reforms it deemed necessary. The JSDA's plans have been surrounded by a certain amount of confusion however – for example it referred to a plan to share price and company information with NASD, whereas NASD denied that there was any such agreement. There have also been personnel problems with a JSDA section chief overseeing the OTC market defecting to Nasdaq Japan Planning.

Subsequently however it has been working hard to encourage companies to list on the OTC market, for example trying to persuade companies listed solely on regional exchanges to transfer their listing to the OTC market. It has also learned from the Mothers market, and in order to simplify listing procedures has reduced the items companies are required to complete on the Securities Report (so-called Section II of the annual report) that they must file in order to be considered for a listing. Further, it is also considering whether to recognize the more "flexible" application of its registration criteria, which would in effect permit the listing of companies who do not meet its quantitative listing requirements.

2) Nasdaq Japan

(1) The OSE and Nasdaq Japan form a comprehensive alliance

Nasdaq Japan seems to have replaced its original plan, of June 1999, to set up a new securities dealers association which would then run the new exchange, by a plan to form a comprehensive alliance with the OSE. Some newspaper reports have said this would involve the replacement of Mr. Masayoshi Son, who had been one of the most important figures in this project, as the president of Nasdaq Japan Planning, Inc. However, since the last meeting of the Nasdaq Japan Club in October there has been no formal announcement from either party.

On 24 December however, Nasdaq Japan Planning and the OSE announced they were signing an agreement to set up and run the Nasdaq Japan Market together. The main points of this agreement were as follows:

"Nasdaq Japan" is to be set up as a new stock market at the OSE, with trading set to begin at the end of June 2000.

A "Japan Nasdaq Association" will be set up to decide the basic policies and trading rules, listing and disclosure requirements. Hirotaro Higuchi, honorary chairman of Asahi Breweries, is to be appointed president of the new association, and Softbank president Masayoshi Son is to be vice-chairman. The rest of the association will be made up by ten or so representatives from major foreign and Japanese securities firms, representatives from the OSE (three people including the board vice-chairman), and three representatives of the U.S. NASD.

Nasdaq Japan Planning, the preparatory company for the new market, will then change its name and become a services company tasked with various operational functions. Tatsuyuki Saeki, former vice president of IBM Japan will be president. It will provide Nasdaq Japan with technology and solutions services, but its main role will be to drum up candidates for listing.

At first the new market will be a place for Japanese venture firms to list, but the future should see it linking up with the US and European Nasdaq markets to offer 24-hour international trading.

Nasdaq Japan plans to offer mutual listing on the U.S. and the soon to be set up European Nasdaq market, and offer mutual access to each others markets for their members. It is also considering eventually providing a market-place for trading the shares of companies from all over S.E. Asia. Masayoshi Son, the Softbank president and principal driving force behind the Nasdaq Japan plan, said that he is also eager to see his group companies and investments listed on the market.

(2) Evaluation of the alliance

If this agreement is implemented as planned, then this will go a long way towards answering all those questions on which we previously entertained serious doubts (who will participate in the market? what sort of trading system and settlement and clearing systems will be adopted? how will the system development costs be shared? etc.). With the OSE providing the trading infrastructure (trading system, listing examinations and market supervision etc.), a new market can be set up without incurring exorbitant costs. Further, trade parties will be made up of existing OSE members.

The most striking feature of this agreement is its practicality. When the idea of a Nasdaq Japan market was originally touted it was the access to the 5,000 shares of U.S. firms listed on the U.S. Nasdaq market that was pushed to the fore. This has now taken second priority behind that of a market for Japanese venture firms. Further, by using the existing systems infrastructure of the OSE and not having to develop entirely new systems, the plan could be brought forward from the original end 2000 to June 2000. While Nasdaq Japan still intends to develop its own trading system, which it eventually plans to install globally across its U.S., European and Japanese markets, the fact that it can start trading before such a system is ready is extremely important as regards competition with the rival Mothers and OTC markets.

Nevertheless, there is still a certain degree of uncertainty over the new market's major selling point, its international aspect. For example, in order to offer mutual listing and access across European and U.S. markets, there are many regulatory obstacles to be cleared such as national differences in disclosure requirements and securities company regulations. In fact, we would not be surprised if its plans for an "international" market leant more towards such practical objectives as luring such U.S. Nasdaq heavyweights as Microsoft, Intel and Cisco Systems to list on Japan Nasdaq at an early stage. This is perhaps only natural, given that the new market's main purpose is not so much to nurture Japanese start-up companies, but rather to stimulate trading in Nasdaq stocks by Japanese investors. If the major U.S. high-tech stocks do list on Nsadaq Japan, then it is not just going up against the Mothers and OTC markets, but also the foreign section of the TSE. Through this it perhaps hopes to tap into Japan's huge pool of individual savings.

When the plans were originally announced some fears were voiced over the neutrality of the exchange given the prominent role to be played by Softbank, a private company. However, whereas originally Softbank president Masayoshi Son had proclaimed his intention to give the market an initial boost by listing all his Softbank group companies, now that it has been made clear that the OSE will have control over the examination of listing applications and the setting of trading rules, these fears of "undue influence" by a single corporate group have been allayed to some extent.

4. Conclusion

The Nasdaq Japan project and the new TSE "Mothers" market have now brought Japan into a new age of inter-market competition for venture firms, a three-way battle of the two new exchanges and the traditional OTC market. The effect of this competition should be to offer a wider choice for emerging companies as to where to list their shares, coupled with a low-cost high-quality market infrastructure. However there is no guarantee that simply because there are several exchanges competing for business that this will automatically lead to a better environment for venture firms. While there is certainly the possibility that clear winners and losers will emerge, there is also the danger that they will all collapse together.

Market size (market capitalization) and liquidity will be the main determinants of success. From an investor's standpoint, it is also of vital importance that the exchange has a fair price-setting mechanism, in order that investors will feel safe trading. However, while the trend towards demutualization of stock exchanges gathers pace and stock markets around the world are turning into business concerns, it is also important to remember that a stock market fulfills a very important public service.

In this light, we have identified the following important issues and concerns.

Firstly, while emphasizing that they are trying to expand the choice of mid-size and small venture firms in listing shares in order to raise funds, there is also the danger that the exchanges are relaxing their listing requirements and procedures too far and too fast.

Already the listing requirements seem fairly lax when compared to those of other countries. In August 1997, the U.S. Nasdaq toughened its listing requirements causing a number of issues to be de-listed. Japan's OTC market did in fact also carry out a review of its registration requirements in December 1998, and subsequently made its de-listing criteria more stringent in order to safeguard the liquidity of the market. The danger remains however, and Japan's exchanges must not let the pressure of competition force them into a beggar-thy-neighbour battle for lower standards.

A second concern, related to the first point above, is that the market operators themselves are being involved less and less in the examination of listing candidates. On the OTC market, perhaps because the trade counterparties have always been the securities houses themselves, the member securities house that is bringing a new company to market also takes on the examination of the listing candidate. On the Mothers and Nasdaq Japan markets as well, emphasis is on the due diligence carried out by the securities house, while examination by the market operators is being gradually cut down in terms of time and thoroughness. While it is of course true that the securities houses are taking on a heavy responsibility themselves at IPOs, as it is they who are underwriting the share issue, this surely does not negate the need for the market operators to carry out a thorough examination of listing candidates. It is in their interests to maintain and improve the "quality" of their markets. Previous criticism of examination by market operators was more because of the lack of flexibility and uniform criteria being applied to differing candidates, rather than the fact that it was the market operator carrying it out. Neglecting the issue of examination runs the risk of repeating the mistake of the failed ECM market run by the American Stock Exchange.[3]

Our third point is that the markets need to pay due attention to the issue of providing sufficient liquidity. While the OTC market did introduce a market-maker system in December 1998, problems with their computer systems resulted in the exchange being criticized for the non-transparency of its prices. Others criticized it for not reducing the bid-offer spreads, or for size limits on executable orders. Mothers on the other hand is intending to offer trading using the same system as the TSE, which gives us cause for concern that, since it will be mainly start-ups being traded, it may run in to the same problems that the OTC market encountered regarding lack of liquidity. While there are rules in place governing public offerings and for the de-listing of issues, it is by no means clear that these will be

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3 "ECM" was a market for small-cap stocks set up by the American Stock Exchange in March 1992. Bent on competing for IPOs with the dominant Nasdaq market, it offered particularly lax listing requirements to companies who would transfer from Nasdaq to ECM. However, new listings ceased as of October 1994, and the market closed in 1995.
The main reason for its failure was the large number of scandals surrounding the firms whose stocks were trading on the exchange. In June 1992, only a few weeks after opening, reports appeared in the press that a major stockholder of one of its listed companies, PNF Industries (de-listed in July 1992), was a convicted arsonist and had been expelled from the American Stock Exchange 6 years earlier for fraud involving stock options. Then in September 1994, reports surfaced that the president of one of the companies that had floated on ECM at its inception, Printron (de-listed in April 1993), had had a sex change and changed his name in order to disguise the fact that he had previously been prosecuted by the SEC.
No doubt the reason why such firms were able to list and cause the exchange such embarrassment was the fact that, desperate to compete with Nasdaq, ECM had not carried out any strict examination of listing candidates and had rather tended to ignore any blemishes. It had also been over zealous in securing the listing of many companies who had little chance of being sufficiently traded. In the end, the amount of trading on ECM remained small compared to the similar small-cap stocks on Nasdaq.

enough to provide sufficient liquidity. Nasdaq Japan meanwhile has not clarified its own position on what trading system to adopt – a market maker system or the order-driven trading system of the TSE.

Europe's venture-oriented exchanges have all taken steps to ensure trading liquidity and to enhance the value of listed shares, by adopting market-maker systems, allowing call-option and two-sided auction trading, combined with order-driven trading systems (as seen previously in Table 1). Japan's exchanges should perhaps get away from the constraining idea that the over-the-counter market must be a market-maker system while exchanges have to use auction trading, and themselves consider the development of a hybrid system.

Fourthly, a major determinant of success will be how to balance the two contrasting roles of being a business-like exchange operator (or association), and of being a self-regulating organization that can ensure market fairness. Currently the new Mothers and Nasdaq Japan markets are spending a great deal of effort on marketing themselves, presenting themselves as a business offering a service - market provision for emerging and high-growth companies. Naturally their ability to live up to the expectations of a self-regulating organization will only be decided after the exchanges have been up and running for a while, and we should not make any hasty judgements, only to say that developments will be closely watched. In terms of organization, there is also the view that the new markets and the JSDA should limit their current wide responsibilities as self-regulatory organizations and instead assign this activity to an independent body. This mirrors a similar debate in the U.S., where inter-market competition, previously between markets run by exchanges and associations, has been further intensified by the presence of electronic trading systems run by securities houses.