OUTLINE OF 2004 PENSION SYSTEM REVISION

Outline of 2004 pension system revision  
Pension reserve funds are united and inseparable with the framework for benefits and contributions under pension systems.

Contributions
(1) Raising the premium level step by step: Raising the premium level step by step while fixing the future premium level
(2) Raising the portion of national subsidy for basic pension: Raising it to a half by FY2009

Benefits
○ Rebalancing the benefit level through macro-economy indexation

Reserve funds
○ The method of maintaining a certain amount of reserve funds into the future was changed to “a limited balance method” that will maintain roughly 1 year of benefit expenses in a period of roughly 100 years.

Approaches to investment of reserve funds

Conditions in those days
○ Given that cumulative loss amounted to ¥6 trillion at the end of FY2002 because of the sluggish stock markets in Japan and overseas, there was a growing argument led by the Diet that “stock investments should be discontinued.”

Basic approaches
○ The Subcommittee for Pension Fund Management of the Social Security Council (consisting of well-informed persons, including those concerned in labor and management) and others clarified their approaches, such as “focusing on domestic bonds,” “focusing on index investments,” and “minimization of risks to the whole portfolio.”
○ Independence and expertise should be strengthened through, for example, the establishment of the “Government Pension Investment Fund” in charge of the investment and the “Investment Advisory Committee.”

<Investment targets>
○ Target yield  
  Real investment yield that exceeds the wage growth rate by 1.1%
○ Basic portfolio  
  • Domestic bonds: 67%  
  • Domestic stocks: 11%  
  • Foreign bonds: 8%  
  • Foreign stocks: 9%  
  • Short-term assets: 5%
**Purpose of revision**

**Thorough expertise**

**Clarification of responsibility**

(Until FY2005)

- Design of pension system
- Inspection of pension finance

- **Formulation of the asset allocation, such as stocks**
  - Request for/provision of advice
  - Guidance/supervision
  - Council
    - Experts in finance, economics, etc.

- Minister of Health, Labour and Welfare

- Former GPIF
  - Board of Directors
    - Management of external asset management institutions
    - Implementation of in-house investment

- (Asset management institutions)
  - Trust banks
  - Investment advisory firms

(From FY2006)

- Design of pension system
- Inspection of pension finance

- **Investment Advisory Committee**
  - Experts in finance, economics, etc.

- President

- Setting of mid-term objectives
- Evaluation of achievements
- Demands for improvements
- Authority over personal issues

- New GPIF

- Formulation of the asset allocation, such as stocks

- ○ Management of external asset management institutions
- ○ Implementation of in-house investment

- (Asset management institutions)
  - Trust banks
  - Investment advisory firms

- Board of Directors
  - Affairs concerning Green Pia
  - Affairs concerning housing and other loans
  - Abolition
  - Management and collection of loan credits

- Implemented by Welfare and Medical Service Agency
With regard to the GPIF’s investment results of the past six years (from FY2003, the first year of estimation of financial re-calculation, to FY2008), the nominal investment yield was 2.00% on annual average, which exceeded the nominal investment yield that becomes the basis for financial re-calculation.

### Changes in investment results

<table>
<thead>
<tr>
<th></th>
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</tr>
</thead>
<tbody>
<tr>
<td>Real investment yield for financial re-calculation</td>
<td>1.10</td>
<td>1.10</td>
<td>1.10</td>
<td>1.10</td>
<td>1.10</td>
<td>1.10</td>
<td>1.10</td>
</tr>
<tr>
<td>Nominal wage growth rate (actual result)</td>
<td>-0.27</td>
<td>-0.20</td>
<td>-0.17</td>
<td>0.01</td>
<td>-0.07</td>
<td>-0.26</td>
<td>-0.16</td>
</tr>
<tr>
<td>Nominal investment yield in line with financial re-calculation</td>
<td>0.83</td>
<td>0.90</td>
<td>0.93</td>
<td>1.11</td>
<td>1.03</td>
<td>0.84</td>
<td>0.94</td>
</tr>
<tr>
<td>Nominal investment yield for all investment assets</td>
<td>8.40</td>
<td>3.39</td>
<td>9.88</td>
<td>3.70</td>
<td>-4.59</td>
<td>-7.57</td>
<td>2.00</td>
</tr>
</tbody>
</table>

(Note 1) Investments were made by the former GPIF from FY2003 to FY2005.
(Note 2) Investment results are the results of investments by the GPIF (including FILP bonds).
(Note 3) For the purpose of the financial re-calculation in FY2004, the real investment yield was estimated to be between 0.3% and 0.8% in the transitional period between FY2003 to FY2008, and the long-term yield from FY2009 was estimated to be 1.1%. Therefore, it may be appropriate to apply a real investment yield lower than 1.1%. In the above table, however, the real investment yield is estimated to be 1.1% for the purpose of comparison from a long-term viewpoint.
INVESTMENT PERFORMANCE OF GPIF (FY2008)

Due to a global financial crisis, stock prices in domestic and foreign stock markets greatly fell and the value of yen sharply increased especially against Euro in exchange markets. As a result, the GPIF’s investment yield was minus 7.6% in FY2008 (about minus ¥9.4 trillion (after deducting investment charges)).

* The yield only from its market investments was minus 10.0% (about minus ¥9.7 trillion).

Amount and rate of return by type of assets (FY2008) (Unit: ¥100 million)

<table>
<thead>
<tr>
<th>Market investments</th>
<th>Amount of return</th>
<th>Rate of return</th>
</tr>
</thead>
<tbody>
<tr>
<td>Domestic bonds</td>
<td>8,700</td>
<td>1.4%</td>
</tr>
<tr>
<td>Domestic stocks</td>
<td>-50,613</td>
<td>-35.6%</td>
</tr>
<tr>
<td>Foreign bonds</td>
<td>-6,213</td>
<td>-6.8%</td>
</tr>
<tr>
<td>Foreign stocks</td>
<td>-48,547</td>
<td>-43.2%</td>
</tr>
<tr>
<td>Total</td>
<td>-96,670</td>
<td>-10.0%</td>
</tr>
<tr>
<td>FILP bonds</td>
<td>3,189</td>
<td>1.2%</td>
</tr>
<tr>
<td>All invested assets</td>
<td>-93,481</td>
<td>-7.6%</td>
</tr>
<tr>
<td>Charges &amp; loan interests</td>
<td>-534</td>
<td>-</td>
</tr>
<tr>
<td>Investment balance</td>
<td>-94,015</td>
<td>-</td>
</tr>
</tbody>
</table>

(Reference) Results of investment of reserve funds (from beginning of discretionary investment until FY2008) (Unit: ¥100 million)

<table>
<thead>
<tr>
<th>Fiscal year</th>
<th>GPIF</th>
<th>Funds entrusted</th>
<th>Return on investment of reserve funds</th>
<th>Rate of return</th>
<th>Cumulative return</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY2001</td>
<td>-13,084</td>
<td>40,870</td>
<td>27,787</td>
<td>1.9%</td>
<td>27,787</td>
</tr>
<tr>
<td>FY2002</td>
<td>-30,608</td>
<td>32,968</td>
<td>2,360</td>
<td>0.2%</td>
<td>30,146</td>
</tr>
<tr>
<td>FY2003</td>
<td>44,306</td>
<td>24,407</td>
<td>68,714</td>
<td>4.9%</td>
<td>98,860</td>
</tr>
<tr>
<td>FY2004</td>
<td>22,419</td>
<td>17,169</td>
<td>39,588</td>
<td>2.7%</td>
<td>138,448</td>
</tr>
<tr>
<td>FY2005</td>
<td>86,811</td>
<td>11,333</td>
<td>98,344</td>
<td>6.8%</td>
<td>236,792</td>
</tr>
<tr>
<td>FY2006</td>
<td>37,608</td>
<td>8,061</td>
<td>45,669</td>
<td>3.1%</td>
<td>282,461</td>
</tr>
<tr>
<td>FY2007</td>
<td>-56,455</td>
<td>4,678</td>
<td>-51,777</td>
<td>-3.5%</td>
<td>230,684</td>
</tr>
<tr>
<td>FY2008</td>
<td>-94,015</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Total</td>
<td>-3,018</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
</tbody>
</table>

* The figure in < > indicates a cumulative balance of investments, including the Pension Welfare Service Public Corporation’s balance in or before FY2000 and the increase through revaluation at the time of the establishment of the new GPIF in April 2006.

The nominal investment yield was 2.0% on average in the past six years, exceeding the basis for the financial re-calculation in 2004.

(Note) The financial re-calculation in 2004 was based on the real investment yield of 1.1% (because the wage growth rate was minus 0.2% on average in the past six years, if this is taken into account, the nominal investment yield becomes 0.9%).

Compared with foreign pension funds, more importance is placed on the safety of investments (“diversified investments centering on domestic bonds”).

(Reference) Investment of pension funds in foreign countries (FY2008)

- CalPERS <Ratio of stocks: about 60%>: -29.1% (California Public Employees’ Retirement System)
- CPPIB (Canada) <Ratio of stocks: about 70%>: -18.6%
- GPF-G (Norway) <Ratio of stocks: about 60%>: -9.5%
- GPIF <Ratio of stocks: about 20%>: -7.6% (Market investments -10.0%)
- AP1-4 (Sweden) <Ratio of stocks: about 50%>: -21.6% (Jan. to Dec.; average for each fund)
○ As for the stock market, benchmark shows:

- The Japanese market suffered a sharp decline in stock prices by 35.55% because the financial crisis expanded due to the Lehman Shock and its effect reached the real economy, resulting in a sharp economic slowdown.

- Developed nations’ markets suffered a decline by 36.9%. In addition, as a result of a decline of about 6% due to stronger yen, their declining rate became 43.2%.

○ As for the bond market, benchmark shows:

- The Japanese market rose by 1.35% in line with lower interest rates.

- In overseas markets, developed nations’ national bond markets rose by 8.1% on local currencies. However, they reduced by 6.8% as a result of a decline of 15% due to stronger yen.
COMPARISON WITH FOREIGN COUNTRIES’ PENSION FUNDS

○ Size of assets (as of the end of March 2009)

<table>
<thead>
<tr>
<th>Country</th>
<th>Size of Assets</th>
</tr>
</thead>
<tbody>
<tr>
<td>CalPERS (US) (California Public Employees’ Retirement System)</td>
<td>¥17 trillion</td>
</tr>
<tr>
<td>CPPIB (Canada) (Canada Pension Plan Investment Board)</td>
<td>¥8 trillion</td>
</tr>
<tr>
<td>GPF-G (Norway) (Government Pension Fund-Global)</td>
<td>¥30 trillion</td>
</tr>
<tr>
<td>AP1-4 (Sweden) (National Pension Funds 1-4)</td>
<td>¥8 trillion (about ¥2 trillion for each fund)</td>
</tr>
<tr>
<td>GPIF (Government Pension Investment Fund)</td>
<td>¥118 trillion</td>
</tr>
</tbody>
</table>

*As of end of Dec. 2008


(Note) The figure for each fund was calculated by the GPIF based on each fund’s website and annual report.

○ Basic (reference) portfolio

(Note) The figure for each fund was calculated by the GPIF based on each fund’s website and annual report.