ASEAN+3 BOND MARKET FORUM BRIEF No. 2

PROFESSIONAL INVESTOR CONCEPTS AND CATEGORIES

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Introduction

The ASEAN+3 Bond Market Forum (ABMF) Brief series aims to provide insights on professional bond markets, their development, and necessary or desirable components to issuers, investors, market intermediaries, regulatory authorities and policy makers, academia, and other interested parties.[1]

The first brief in this series provided a general introduction to the professional bond market in ASEAN+3; it also mentioned professional investors as a key component of a professional bond market and touched on their characteristics. This brief is dedicated to explaining the concept of professional investors, starting from their definition, types, and categories, as well as their role in the bond market. We will also cover the underlying legal and regulatory frameworks, qualifications, and eligibility criteria for professional investors. In addition, we explain how they obtain, maintain, or change their professional investor status and elaborate on measures to ringfence the professional bond market. The different types and attributes of professional investor concepts in individual ASEAN+3 economies are also explained in this brief.

HIGHLIGHTS

- The concept of professional investors is formed and stipulated by the relevant securities or capital market law(s) and/or regulations from the viewpoint of ensuring regulatory flexibility and creating a conducive environment for the bond market as a genuine financing and investment option.
- When professional investors do business with other professional investors, the strict investor protection measures designated for nonprofessionals need not be applied.
- Institutional investors make up the key professional investor categories and represent the vast majority of investments and holdings in the bond market.
- Creating and developing a specified market (or segment) for professional investors, including the nurturing of professional investors, is especially important for the sustainable development of the financial and capital market in every economy and the region to which it belongs.
- The implementation of a professional investor concept and its definitions are only complete if robust selling and transfer restrictions are defined to ringfence the professional bond market from investors that are not professionals.

Professional Investor Concepts

Professional investors are defined and categorized by their roles, rights, and obligations. While professional investor concepts may not be limited to the bond market, they are essential for the bond market because bond denominations and trade sizes are much larger than equities. Professional investor concepts become relevant in relation to any concessions from public offering market practices.

[1] ASEAN+3 refers to the 10 members of the Association of Southeast Asian Nations (ASEAN) plus the People's Republic of China, Japan, and the Republic of Korea.

In many countries, the concept of professional investors is formed and stipulated by the relevant securities or capital market law(s) and/or regulations to ensure regulatory flexibility and create a conducive environment for the bond market.

The ASEAN+3 Bond Market Forum (ABMF) was established in 2010 under the Asian Bond Markets Initiative by the ASEAN+3 Finance Ministers, with a mandate to support the development of regional local currency bond markets. Since then, ABMF has acted as a platform for dialogue among public and private sector stakeholders in the regional bond markets and promotes the exchange and evaluation of ideas among finance ministries, securities regulators, securities exchanges, depositories, custodian banks, underwriters, and other market intermediary organizations. Discussion outcomes in ABMF have helped to address common issues and formulate policy recommendations.

The Asian Development Bank publishes the ASEAN+3 Bond Market Guide series, which are created and updated by ABMF, for interested parties. The economy-level bond market guides serve as reference materials to learn more about individual regional market developments, help to address misperceptions, and project regional bond market information to a larger audience. ABMF has proposed, agreed on, and helped implement the ASEAN+3 Multi-Currency Bond Issuance Framework as one practical initiative toward harmonizing the professional bond markets in ASEAN+3.

As part of its efforts, ABMF created the Working Group for Comparative Capital Market Law and Regulations to research market foundations and practices. The working group will share observations and policy input with constituents and the public, particularly on the region's professional bond markets.

Some professional bond markets have started with informal groupings of institutions that could be regarded as professional investors due to their nature or activities in financial markets. But these market segments may not achieve full recognition by regulatory authorities and foreign institutional investors until their professional concept is formalized in law or regulations.[2] All economies in ASEAN+3 with professional bond markets or market segments have prescribed their professional investor concept in law or regulations (**Table 1**).

The key regulatory objectives in formulating a professional investor concept are to allow market institutions to facilitate business between professional investors based on the suitability principle. As a result, not only professional investors but also financial intermediaries are able to benefit from regulatory flexibility without compromising investor protection or market integrity. This means that professional investor concepts differentiate the investor base into professionals and those that are not professionals.[3] This brief will focus on the professional investor type.

Definition of a Professional Investor

Professional investors are institutions and, where included, individuals with the experience, knowledge, and expertise to adequately assess various risks to make an appropriate investment decision. Moreover, their ability to manage risks is assumed to include the capacity to absorb financial losses.

Professional investors are entities considered as such by the nature of their business or license, accreditation, or investment mandate. Other investor types may also be admitted subject to certain eligibility criteria—see **Professional Investors Subject to Qualification**.

One key distinguishing feature of professional investors is that they are able to obtain, process, and act on available information, even if that information is not readily provided. Professional investors are typically expected to be able to read information in English, as the common language of finance.

[2] "Foreign institutional investors" (often referenced simply as FIIs) is an accepted industry term for nonresident entities whose business is to invest in domestic financial and capital markets, either on behalf of clients or for their own purposes. These entities typically represent the same types of institutions that are present in the domestic market and include asset and fund managers, banks, insurance companies, and pension and provident funds. FIIs are typically included in professional investor concepts on the basis of equivalence of their licensing and supervision by a competent authority.

[3] This ABMF Brief series uses the term "retail investors" for individuals and investors that are not classified in any other manner.

Table 1: Professional Investor Concepts in ASEAN+3

Economy	Name of Professional Investor Concept	Established by
Brunei Darussalam	Sophisticated Investors	Law
Cambodia	Qualified Investors	Regulation
China, People's Republic of	**China Inter-Bank Bond Market:** Private Placement Investors	Regulation
	Exchange Bond Market: Qualified Investors	Regulation
Hong Kong, China	Professional Investors	Regulation
Indonesia	Professional Investors	Regulation
Japan	Qualified Institutional Investors, Professional Investors	Law
Korea, Republic of	Qualified Institutional Buyer	Law
Malaysia	Sophisticated Investors	Law
Philippines	Qualified Buyers	Law
Singapore	Accredited Investors, Institutional Investors	Law
Thailand	Institutional Investors, High Net-Worth Investors	Regulation
Viet Nam	Professional Investors	Law

Notes: Even where professional investor concepts are established by law, some investor categories may have been set in regulations. Details of all professional investor concepts are as of October 2022.
Source: ASEAN+3 Bond Market Forum.

Role of Professional Investors

The process of bond issuance is different from that of equities. The number of investors in bond markets is smaller, but each investment size will be larger. Investment sizes can easily exceed the local currency equivalent of USD1 million. As a market develops, bond issuances can be worth more than tens or hundreds of millions of US dollar-equivalent at a time. Since they need to regularly invest large amounts into bonds to fulfill their mandates, professional investors are necessary for a bond market's development.

Hence, professional investors represent the full breadth and depth of the potential demand for both government and corporate bonds across different instrument types, characteristics, and tenors. This allows issuers the flexibility to tap the market through several different issuance methods or instrument types and ensures regular or repeat issuance as well as continuous demand—all of which are desirable features of a well-functioning bond market.

Many markets attach specific issuance methods, such as a private placement, exclusively to professional investors, thereby enabling professional investors and also issuers and other market participants in the professional bond market to act according to their professional status.[4]

Need for a Professional Investor Concept

We have explained the role of professional investors in the bond market, representing key demand for issuers and offering them flexibility in obtaining financing. But is there really a need to define professional investors instead of just bestowing special conditions on institutional investors?[5] In fact, there is a need, and it is critical.

[4] Private placement, as the key issuance method in the context of a professional bond market, was mentioned in *ABMF Brief No. 1: The Professional Bond Market: A Practical Introduction*. The concept of a private placement will be explained in greater detail in a future brief in this series.
[5] An "institutional investor" is a company or organization that invests money on behalf of other people, according to Investopedia.

Professional investor concepts really are the essential requirement for the establishment of any professional bond market, but they are also needed to establish appropriate distinctions from retail investors. The protection of retail investors is one of the principal objectives in the mandate of any regulatory authority in the securities market.

With a professional investor concept, regulators define rights and obligations for professional investors while delineating their activities from those of retail investors. The public offering bond market sets legal and regulatory frameworks in a manner similar to the equities market because both markets target retail investors. Therefore, they require appropriate protections for retail investors.

When defining a professional investor concept, it is desirable to include appropriate mechanisms for the ringfencing of the professional market, so as to ensure the protection of investors who are not professional. We will come back to this ringfencing requirement and typical mechanisms toward the end of this brief.

Professional Investor Categories

Professional investors may be categorized as either institutional investors or other professional investors. The distinction relates to the nature of an entity, its business or license, demonstrated knowledge, experience, or expertise, and may also include the need to prove certain amounts of assets or income. The distinction will become clearer once investor categories and their qualification criteria are reviewed.

Table 2 provides an overview of which professional investor categories are evident in regional professional investor concepts in ASEAN+3 markets. Not all categories are evident or used in all professional bond markets in the region, even if entities typically included in these categories exist in a given market. That may be the result of different treatment of institutions under law or regulations, or variations in the categorization by the regulatory authorities, and may also possibly be due to the level of sophistication, expertise, or other factors specific to a domestic market.

Institutional Investors

Unlike equity market participants, which regularly include retail investors, bond investors primarily consist of large institutional investors, who also represent the vast majority of investor categories in every professional investor definition. These professional investors can generally be understood to fall into the categories described as follows (in the sequence they are shown in **Table 2**):

Government. This category describes the central government, typically in the form of the ministry of finance or its debt management office (as may be applicable), but it may often also include regional, municipal, or local governments. Some markets also include government agencies, as well as the competent authorities supervising the financial and capital markets. While the government may not be an active investor in the bond market, its inclusion in the professional investor categories ensures its ability to acquire, hold, and divest bonds for its own purpose and also in the event of market distress or issuer defaults.

Central bank. The central bank or monetary authority of an economy is charged with maintaining price stability, the value of the local currency, and desired exchange rates with other currencies. Central banks usually act as a fiscal agent for the government and support the issuance of sovereign debt instruments. They participate in the bond market to conduct monetary operations.

Statutory bodies. These bodies, which are referred to as “statutory boards” in some markets, are specific entities created through an act of government and are charged with the management and administration of certain areas of the public sector; they most often include investor protection schemes, utilities, housing agencies, and development funds. The bodies are often permitted or required to manage their own budget and invest in the domestic bond market to ensure predictable returns.

Sovereign wealth fund(s). Sovereign wealth funds are designated investment funds that invest public assets, such as pension schemes or industrial holdings, on behalf of the government or its citizens. Sovereign wealth funds invest either directly or through third-party asset managers; are active in the bond market; and, due to their nature and size, tend to only deal with other professional investors.

Securities regulator. Regulators may be included in the list of professional investor categories to facilitate market interventions, as required. While the nature of securities regulatory authorities suggests a separate

Table 2: Professional Investor Categories Evident in Professional Investor Concepts in ASEAN+3

Economy	Professional Investor Concept	Government	Central Bank	Statutory Bodies	Sovereign Wealth Fund	Securities Regulator	Exchange(s), Market Operator(s)	Central Securities Depositories	Clearing Houses	Trade Repositories	Securities Companies	Financial Institutions	Nonbank Financial Institutions	Insurance Companies	Fund Managers	Mutual Funds or Unit Trusts	Pension Funds	Trustees or Trust Companies	Others (may be admitted by authority)	Corporates	High-Net-Worth Individuals	Nonresident Investors	Multilateral Agencies (or similar entities)
Brunei Darussalam	Sophisticated Investors	●		●							●	●	●	●	●	●	●	●	○	○	○		
Cambodia	Qualified Investors		●	●							●	●	●	●	●	●	●		○	○	○	●	○
China, People's Republic of	CIBM: Private Placement Investors [a,b]			●							●	●	●	●	●	●	●	●	○	○		●	
	Exchange Bond Market: Qualified Investors [b]			●							●	●	●	●	●	●	●	●	○	○	○	●	
Hong Kong, China	Professional Investors	●		●			●	●	●		●	●		●	●	●	●	○		○	○	●	●
Indonesia	Professional Investors			○			○	○	○		●	●	○	●	●	●	●			○	○		○
Japan	Professional Investors	●	●	●	●		●	●			●	●	●	●	●	●	●	●		○	○	●	
Korea, Republic of	Qualified Institutional Buyers	●	●	●	●	●	●	●			●	●	●	●	●	●	●	●		○	○	●	
Malaysia	Sophisticated Investors		●	●			●	●	●		●	●	●	●	●	●	●	●		○	○	●	
Philippines	Qualified Buyers											●		●	●	●	●	●	○				
Singapore	Institutional Investors	●		●	●		●	●	●	●	●	●	●	●	●	●	●	●	○	○		●	●
	Accredited Investors																		○	○	○		
Thailand	Institutional Investors		●	●			●	●	●		●	●	●	●	●	●	●	●				●	●
	High-Net-Worth Investors																			○	○		
Viet Nam	Professional Investors			●							●	●	●	●	●	●	●			○	○		●

● indicates category specifically included ○ indicates category included with conditions or subject to approval or consent

ASEAN+3 = Association of Southeast Asian Nations plus the People's Republic of China, Japan, and the Republic of Korea; CIBM = China Inter-Bank Bond Market.

Note: All information as of 31 October 2022.

[a] Private Placement Investors consist of "Designated Institutional Investors" and "Specialized Institutional Investors." The categories shown represent an interpretation of relevant regulations.

[b] Nonresident investors are included under the Qualified Foreign Institutional Investor or Renminbi Qualified Foreign Institutional Investor schemes.

Sources: Asian Development Bank. *ASEAN+3 Bond Market Guide* Series. Manila; ASEAN+3 Bond Market Forum research based on public domain sources.

category distinct from other commercial entities, some markets may subsume regulatory authorities under government.

Exchange or market operator. A securities exchange or (electronic) trading platform may be included in the professional investor concept as a result of its functions regulating its markets, such as through buy-ins or default handling, as well as the management of clearing funds or investor protection schemes, as may be applicable. The nature of such exchanges and platforms is clearly professional.

Central securities depository. A central securities depository (CSD) may not be a regular investor in the bond market as such but is sometimes included in professional investor concepts, particularly if the CSD maintains a settlement fund that requires investment of its contributions) or engages in securities lending activities. Due to its nature, a CSD is considered a professional entity by default. The specific nature of a CSD as market infrastructure requires this to be a separate category from other entities.

Clearing house. A clearing house allows the netting of market obligations resulting from trades entered into by market participants, in order to reduce and consolidate payments and minimize risk. To be able to use its services, participants have to place collateral with the clearing house to guarantee their exposure; the clearing house may invest such cash or securities (as the case may be) and any funds in a clearing guarantee fund in the capital market, including in the bond market.

Trade repository. Trade repositories collect and store information on trades in the over-the-counter market, particularly for derivatives contracts, to enhance market transparency and support regulatory reporting requirements. Trade repositories are considered part of financial market infrastructure, require licensing or accreditation, and may invest any regulatory capital or reserves in the bond market.

Securities companies, including securities brokers, dealers, and underwriters. As one of the most natural investor categories in any securities market, securities companies—also variously known as brokers, broker-dealers, or securities firms—fulfill a number of functions in the bond market, including the professional market segment. Brokers buy and sell securities, including bonds, for clients or their own books; underwriters acquire bonds for the purpose of on-selling them to other investors.

Financial institutions. Financial institutions are another key investor category in bonds and other debt instruments, both on behalf of clients and for their own purposes; banks invest in bonds to hold liquidity and achieve returns, to utilize them as collateral for commercial repurchase agreement or open market operation transactions with the central bank, and while acting in an underwriter capacity where regulations so permit. Depending on each economy, the financial institutions category may include banks, other deposit-taking institutions, credit unions, saving unions, and/or similar entities. Some markets may designate commercial banks as a separate professional investor category.

Non-bank financial institutions. This category, if so segregated, includes consumer, business finance, and leasing companies; factoring firms; credit card companies; housing finance and credit foncier companies; and others that are required to maintain regulatory capital or reserves, including venture capital firms. These institutions issue and invest in bonds to manage capital and reserves.

Insurance companies. Insurance companies are significant investors in the bond market, investing their regular premium receipts in interest-bearing instruments to generate predictable returns. The bond market is of particular interest to life-insurance companies that have to match their medium- and long-term obligations with corresponding asset tenors. The nature of insurance companies and their focus on investments makes them professional investors; depending on the economy, insurance companies may also be direct participants in the primary market.

Fund managers. This category represents entities that manage the assets of or contributions from a variety of asset owners, and it includes entities described as asset managers and investment advisors. Fund managers are the quintessential professional investors in any securities market, including the bond market.

Mutual funds or unit trusts. These so-called "collective investment schemes"—the distinction between mutual funds and unit trusts lies in the underlying legal framework in a given market—are a key investor category in any securities market, including the bond market. Due to their nature as a pooled investment and the fact that they are represented as an entity by a professional fund or asset manager, collective investment schemes are considered professional investors.

Pension funds. Pension or provident funds have a regular need to invest member or participant contributions for predictable returns; they invest a significant portion in the bond market, often in longer-tenored instruments to match the profile of their obligations to members. This category may include endowment and scholarship funds; retirement schemes; and investment portfolios held by nonprofit organizations such as universities, religious organizations, hospitals, and funds.

Trustee or trust company. As a fiduciary looking out for the interest of another entity—typically, a general trust or unit trust—or individuals (as the case may be), a trustee is the nominal account holder of investments for these parties. As such, trustees are typically licensed and need to demonstrate their ability to supervise and administer investment portfolios, which makes them professional investors.

Professional Investors Subject to Qualification

In addition to the aforementioned institutional investor categories, as the "classical" professional investors, regulatory authorities may also admit other investor classes into the professional investor categories. However, in contrast to the aforementioned categories that represent entities engaged in regulated activities in the capital market as part of their business, these investor categories must demonstrate their ability to act as professional investors. The most common of such categories are described as follows:

Corporates. Typically, corporates include large companies with a treasury function, or government or nongovernment agencies with a corporate character that do not fall into any of the institutional categories. Corporates are of particular significance if the professional investor category is also relevant for the money market, as corporate treasury functions often place short-term liquidity to manage company fund flows. While these companies may be large and are often listed entities, their eligibility as professional investors will need to be evidenced, typically through proof of company assets or investable funds.

High-net-worth individuals. This category denotes individuals or their incorporated structures that can satisfy any number of eligibility criteria to be classified as professional investors. Qualifications range by market from evidence of an investment account or demonstrated activities in the capital market to regular or disposable income, or liquid assets above a certain amount.

Other Professional Investors

Other professional investors may include those institutions that are not easy to categorize or that may be subject to a different regulatory approach or oversight.

Nonresident investors. This is a collective term for institutions, corporations, organizations, and individual investors that do not have an address or a principal place of business in the economy they invest in. Nonresident investors, also often referred to as foreign investors (foreign institutional investors, or FII, is a fairly typical industry designation) may be mentioned specifically in professional investor concepts but most often are given professional investor status if their nature, purpose, or business activity falls into one of the professional investor categories that exists in a given market; a typical eligibility criterion for nonresident investors is the fact they are regulated and supervised by a comparable authority in their home market.

Nonresident (Foreign) Investors in Professional Investor Concepts

Nonresident status may also be significant if a market maintains distinctions relating to market access between domestic and foreign investors, and it certainly matters for the purpose of tax treatment. Specific requirements for market access for foreign investors remain in a few markets.

While some regional markets group all foreign investors into a nonresident investor category in relation to their professional investor concept, such classification may not represent the investors' home market regulatory environment and intended investor protection scope.

For instance, in Japan, nonresident individuals who do not have an address or residence in Japan, and nonresident corporations that do not have a principal place of business in Japan, are granted the same full-disclosure exemption concessions as those for professional investors.

Multilateral agencies. These are institutions—often also referred to as supranational agencies or international organizations—that include members from more than one country or economy. They are regarded as nonresident investors in principle, or they may be mentioned as a separate professional investor category in law or regulations. The Asian Development Bank is an example of such multilateral agency.

Obtaining, Maintaining, and Changing Professional Investor Status

Professional investor concepts may prescribe the manner in which investor categories fulfill the qualifications of professional investors, or broadly categorize entities by their business nature or purpose in the capital market. For the latter, as is typically the case for institutional investors and market infrastructure providers, it is sufficient for those entities to be categorized as professional investors, act accordingly, and assume any rights and obligations granted by the professional investor concept, as may be applicable.

In contrast, corporates and high-net-worth investors—investor categories that are each subject to initial qualification and must meet specific eligibility criteria—have to undergo a process to obtain professional investors status. In addition, some markets may stipulate a need for requalification at regular intervals and/or an obligation for market intermediaries to periodically satisfy themselves that professional investor status is still warranted. Such processes may vary from market to market and may be carried out by regulatory authorities or market intermediaries, as the case may be.

Eligibility Criteria of Professional Investors

Based on the requirements and suitability principles outlined in the scope of a professional investor concept and the definition of professional investors stated earlier in this brief, eligibility criteria for professional investors are determined through the best judgment of policy makers and regulatory authorities in each economy. They may take into consideration the actual conditions of each market and the financial literacy of their participants, particularly those that are not institutional investors.

The eligibility criteria exist in various forms, depending on the category of professional investors and the approach taken by regulators in each economy. The following are some common examples of the qualifications required:

- those that automatically constitute a professional investor (e.g., as a result of their business nature or license); this would be typical for banks, securities firms, investment managers, insurance companies, and other institutional investors;
- those that may become professional investors because of the acceptance of a registration or accreditation with the regulatory authority;
- those that may become professional investors through the filing of necessary notifications with the regulatory authority (e.g., corporations that hold and manage a certain level of financial assets under prescriptions in regulations);
- those that may become professional investors through permission or authorization by the regulatory authority; and
- those individuals that may request a change of status from general to professional investor and receive confirmation from the securities company or other intermediary they use to access the bond market.

The easiest eligibility criterion for a professional investor is belonging to a specific category of such investors. Among the institutional investors represented in professional investor categories, having the nature of one’s entity named in the professional investor concept is the only qualification required. Some institutional investor categories may have to apply to the regulatory authority to be admitted as professional investors.

To qualify for other professional investor categories, the concepts often apply “means-testing” approaches—that is, the candidates must demonstrate that they have the commercial, financial, or intellectual means to invest and hold sufficiently large amounts in the bond market freely and would be able to absorb losses in the event of issuer default or non-payment of interest.

The concept of means-testing is not limited to the bond market and may be equally applied to other market segments in a given economy where investors’ willingness or ability to invest in specific products needs to be ascertained. In such cases, the eligibility criteria—such as thresholds in the amount of assets or disposable income, or the capacity to take risks—are often the same across all market segments.

Obtaining Professional Investor Status

To prove their compliance with applicable eligibility criteria, candidates will have to submit official documents supporting their claim to their appointed market intermediary or, where applicable, the regulatory authority. Typical supporting documents include

- bank statements,
- certificates of deposit,
- investment statements,
- portfolio or asset valuation reports,
- tax assessments, and
- income and expense documents.

Some markets stipulate that evidence of an investment or securities account represents proof of an investor's ability to be considered professional. However, most often such requirements are combined with a means test. Where investment expertise needs to be demonstrated, securities account or investment reports covering a certain period of time will need to be provided to show the necessary financial data of the investor. Where a minimum investment or disposable income threshold is specified, this often follows the typical minimum trade size in the professional market, or similar thresholds set for investments in other wholesale product markets; as a guide, a typical minimum investment size may be USD250,000 or a similar amount in local currency equivalent.

The market intermediary will be required to assess the information provided, against company policies and/or specific guidance from regulatory authorities or market associations, communicate their conclusion to the candidate, and then treat the investor according to their classification result. Depending on a market's regulations, the investor may need to repeat this vetting process with every market intermediary they engage. This is to ensure that there will be no gaps in the ringfencing efforts of a professional bond market.

Maintaining Professional Investor Status

Where an investor obtains a formal professional investor certificate or similar credentials, the professional investor may use such certificate to demonstrate their status to other market intermediaries. This, however, does not free the new market intermediary from conducting their own due diligence.

At the same time, and again subject to prevailing market regulations, the professional investor status may need to be reviewed or renewed periodically, particularly where asset or income thresholds apply, since asset and income levels may change over time.

Changing of Status of Investor Types

Some countries in the region, including Japan, allow for a change in investor type (also referred to as an "opt-in/opt-out" approach) for some investor categories.

Table 3 shows examples from Japan for reference. For instance, an entity categorized as a professional investor can be treated as a general investor (i.e., a party not considered professional) if the entity so wishes and formally agrees with the market intermediary responsible for the classification, such as a securities company.[6] It should be emphasized that this change in status occurs only for the relationship with that particular market intermediary, not the market as a whole.

On the other hand, an entity or a person categorized as a general investor in Japan can be treated as a professional investor if the party so desires and is able to provide the necessary supporting evidence to the securities company that it fulfills any and all applicable eligibility criteria and qualifications. Although an individual is, in principle, treated as a general investor, a high-net-worth individual can be treated as a professional investor if the person agrees to this with the securities company they use to access the market.

The opt-in/opt-out approach allows investors to participate in the bond market to their level of comfort and takes into consideration not only experience and expertise but also the changes in financial circumstances, as the case may be.

Developing Professional Investors

A professional investor concept alone does not ensure a professional bond market, not least a well-accepted and liquid one. Any implementation of a professional investor concept has to go hand-in-hand with regulatory and market or industry efforts to develop and maintain a class of professional investors that can meet the eligibility criteria and safeguard the intended

[6] For the purpose of illustration, "general investor" is used here, as it represents the term used for nonprofessional investors in the Japanese classification of investor types on which the example is based.

Table 3: Classification and the Change of Status of Investors in Japan

Professional Investor	1. Cannot request nonprofessional treatment a. Qualified institutional investor b. Government of Japan c. Bank of Japan	Always treated as a professional investor
	2. Can request nonprofessional treatment (designated companies and organizations) a. Local government b. Public companies c. Joint stock companies whose capital is reasonably believed to be JPY500 million or more d. Foreign corporations (foreign judicial persons) e. Others	Option to be nonprofessional (opt-out)
General Investor	3. Can request professional treatment a. Designated individual (HNWI) (i) with trading experience of one year or more, and (ii) whose net assets and invested assets are reasonably believed to each be worth JPY300 million or more b. Others (joint-stock companies other than a professional investor)	Option to be professional (opt-in)
	4. Cannot request professional treatment Individuals other than in Item No. 3.	Always treated as a general investor

HNWI = high-net-worth investor, JPY = Japanese yen.
Note: Here, the term “general investor” is used as it is the official designation of an investor type in the Japanese market.
Sources: Financial Services Agency Japan, ASEAN+3 Bond Market Forum.

ringfencing. These efforts may be contained in the professional investor regulation itself but, more often, are prescribed in the specific regulations that govern the licensing, registration, or accreditation of entities regarded as professional investors. At the same time, self-regulatory organizations such as market associations often organize and administer continuous professional education programs for their member institutions and staff .

In principle, professional investors exist in every market, whether formally designated or not. As the details in this brief show, many institutions that are participants in any financial or capital market have the general qualifications and capabilities to act as professional investors, and there are other entities or even individuals that may also qualify based on typical eligibility standards.

At the same time, the identification and recognition of such investor types is a crucial task for policy makers and regulatory authorities.

Particularly, developing economies with nascent bond markets, where the number of professional investors may be small and their scale limited, should set a longer-term goal to establish a professional market segment. Hence, professional market participants (including new entrants) can grow with the market’s development and also be given opportunities to connect with their peers in other markets. The latter is critically important for learning about regional and international market and industry practices, and the adoption of those practices for the benefit of one’s own market and economy overall.

Adoption of international best practices goes hand in hand with the establishment of principles for both the professional market and its participants as they develop. Capacity building, including training of staff to instill and retain genuine professional skills, may be necessary. In turn, to nurture professional market participants, it is necessary, as a central premise, to create and develop a professional market as a platform on which practical training can be done.

Ringfencing of Professional Investors

As mentioned earlier, one key aspect of a professional investor concept and the professional investor categories within is the effective ringfencing of their activities in the professional bond market from investors that are not professional. The professional investor concept and its application in a given market is only complete when the distinctions of activities, rights, and obligations of professional and nonprofessional investors are properly enacted.

This ringfencing may be contained in the concept itself or specified in law or separate regulations. There are a number of mechanisms to ensure the continuous protection of retail investors, being a key objective of regulatory authorities. These include the active management or certification of professional investors by market intermediaries, the opt-in or opt-out practices explained above, or the setting of selling and transfer restrictions (**box**). Practices may vary between markets, simply owing to different legal traditions or implementation as regulation or market practice. In any case, ringfencing approaches should establish strong boundaries between the investor types and also stipulate penalties for breaches, as such actions can compromise the integrity of a bond market.

Professional Investor Concepts Help Ringfence the Professional Bond Market

Professional investor concepts include different measures to ringfence the professional bond market to ensure that the protection of retail investors can be observed in daily market operations. Selling and transfer restrictions are one of the key aspects of these measures.

In most markets, prescriptions contained in the professional investor concepts require the prominent placement of disclaimers in issuance documentation and subscription forms, stating that the bonds are not to be offered or transferred to nonprofessional investors, and (where applicable) making reference to an exempt regime (i.e., that the issuance documentation has not been checked or approved by the regulatory authority and, thereby, is only available for investment by professional investors). This is often supplemented by the inclusion of clauses in the sales contract that the selling or transfer of said bonds to nonprofessionals would represent a violation of law or regulations and incur fines, suspension, or other penalties.

Market laws, regulations, or rules also stipulate that—when trading (on an exchange or other electronic trading platform), settling, or transferring (at a central securities depository)—counterparties or participants are required to have checked the investor status of a client before executing a trade or transfer. Automated platforms do not allow a nonprofessional market participant to execute a trade or transfer a bond that is issued to professional investors only; market segments that are professional do not admit nonprofessional investors.

About the Asian Development Bank
ADB is committed to achieving a prosperous, inclusive, resilient, and sustainable Asia and the Pacific, while sustaining its efforts to eradicate extreme poverty. Established in 1966, it is owned by 68 members—49 from the region. Its main instruments for helping its developing member countries are policy dialogue, loans, equity investments, guarantees, grants, and technical assistance.

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