

## Outlook for 5Y JGB Auction

### Dip-buying at -0.095 - -0.085%

- ✓ Under the YCC policy, it is proven that JGBs have certain degree of tolerance against the rise in overseas yields. In the near term, the 5Y JGB yield is likely to remain in the -0.115 - -0.085% range.

Strategic Memorandum DSTE237  
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### Auction Details

**Auction Date:** May 17, 2018  
**Issue Date:** May 18, 2018  
**Maturity Date:** March 20, 2023  
**Offering Amount:** About 2.0 trillion yen

\* New 5Y JGBs will likely be the second reopening of JS135 carrying a 0.1% coupon.

\*\* On May 16, JS135 traded at -0.100% (unch v. previous day's close) and closed at -0.100% (unch). WI traded at -0.095% (+0.5bp) and closed at -0.100% (unch).

### Exp. Rating on Auction Results

|        |      |         |      |             |
|--------|------|---------|------|-------------|
| 1      | 2    | 3       | 4    | 5           |
| Failed | Poor | Average | Good | Outstanding |

### Dip-buying at -0.095 - -0.085%

Since the previous 5Y JGB auction went well at the -0.120 - -0.115% level on April 17, the 5Y JGB yield has been moving in a -0.115 - -0.085% range on an intraday basis. For the past several days, it is moving in a -0.105 - -0.100% range.

Key points to think about the bidding level at tomorrow's auction are as follows:

- Decent short-covering is expected for JS135;
- The 5Y sector is currently neither noticeably expensive nor cheap on the JGB yield curve (Appendix 3). It appears rather expensive on the total return curve and overvalued vs. the 10Y and 20Y JGBs with about 5 years left to maturity (Appendix 7-8);
- While market participants appear to be becoming less cautious about reduction in the BOJ's offer amount, it is highly possible that the BOJ will conduct six to seven purchase operations (three operations in May and three to four more operations expected in June) by the next 5Y JGB auction to be held on June 21;
- New 5Y JGBs to be auctioned in June will also likely be the reopening of JS135: and

- With the start of the new reserve maintenance period, the money market has been stabilized as witnessed by a fall in the GC repo rate, which leads TDB yields down;

and so.

We check the environment surrounding 5Y JGBs. On May 15, the 10Y US Treasury yield rose to 3.09% at one point for the first time in six years and ten months or since July 8, 2011. As recently-announced economic indicators, including inflation readings, appear mixed, the outlook for US long-term interest rates seems to be divided—the pessimistic view (expecting further rise) and the optimistic view (projecting that rates will remain flat). In Japan, Jan-Mar GDP was expected to post negative growth, and the actual data announced on May 16 was weaker than expected. Regarding the GDP as well, there are both pessimists (viewing that economic growth has paused) and optimists (expecting recovery in Apr-Jun). However, today's GDP data are not something that could destabilize the BOJ's yield curve control (YCC) policy yet. As witnessed by the fact that 10Y JGBs trade at 0.55% today (May 16), we can confirm the tolerance of JGBs against the rise in overseas yields under the YCC policy. In the near term, we believe that the 5Y JGB yield would remain in the recent range (-0.115 - -0.085%).

Today, JS135 trades at -0.100% (unchanged vs. previous trading day) and WI trades at -0.095% (+0.5bp vs. previous trading day). Given that and the aforementioned factors, we would like to take a dip-buying stance for JS135 at the -0.095 - -0.085% level. If JS135 softens near to the level in pre-auction trading, the auction is likely to go in a trouble-free manner.

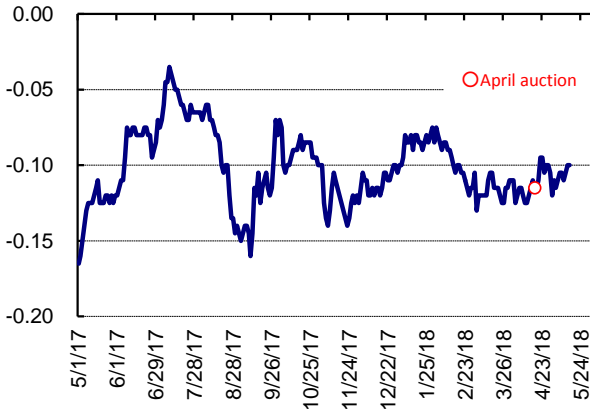
The 5Y sector is currently neither noticeably expensive nor cheap on the JGB yield curve (Appendix 3). This month, however, superlong JGBs will face a wave of new supplies, starting from yesterday's 30Y JGB auction. Accordingly, switching out from the superlong zone (including 20Y sector) into the 5Y sector may become active. We will carefully watch impact on the bidding level at the auction by such activities.

#### 5Y JGB Auction Results

| Auction Date | Issue # | Marurity Date | Coupon % | Issue Size (trillion yen) | B/C  | Average Price | Lowest Price | Price Tail (yen) | Average Yield | Highest Yield | Yield Tail (%) | Allotment (%) |      |
|--------------|---------|---------------|----------|---------------------------|------|---------------|--------------|------------------|---------------|---------------|----------------|---------------|------|
| 5/17/18      | 135R*   | 3/20/23       | 0.1*     | 2.0**                     |      |               |              |                  |               |               |                |               |      |
| 4/17/18      | 135R    | 3/20/23       | 0.1      | 2.0                       | 4.40 | 101.09        | 101.08       | 0.01             | -0.120        | -0.118        | 0.002          | 95.5045       | Good |
| 3/13/18      | 135     | 3/20/23       | 0.1      | 2.2                       | 4.18 | 101.05        | 101.04       | 0.01             | -0.108        | -0.106        | 0.002          | 67.4216       | Avg  |
| 2/14/18      | 134R    | 12/20/22      | 0.1      | 2.5                       | 4.67 | 100.94        | 100.94       | 0.00             | -0.093        | -0.093        | 0.000          | 91.9530       | Good |
| 1/16/18      | 134R    | 12/20/22      | 0.1      | 2.4                       | 5.24 | 100.91        | 100.90       | 0.01             | -0.084        | -0.082        | 0.002          | 8.9750        | Good |
| 12/12/17     | 134     | 12/20/22      | 0.1      | 2.5                       | 4.38 | 101.03        | 101.02       | 0.01             | -0.104        | -0.102        | 0.002          | 83.4736       | Good |
| 11/14/17     | 133R    | 9/20/22       | 0.1      | 2.5                       | 4.19 | 101.01        | 101.00       | 0.01             | -0.107        | -0.105        | 0.002          | 53.5278       | Avg  |
| 10/19/17     | 133R    | 9/20/22       | 0.1      | 2.5                       | 4.24 | 100.90        | 100.90       | 0.00             | -0.082        | -0.082        | 0.000          | 88.7951       | Good |
| 9/12/17      | 133     | 9/20/22       | 0.1      | 2.2                       | 4.07 | 101.06        | 101.03       | 0.03             | -0.110        | -0.104        | 0.006          | 47.7913       | Poor |
| 8/17/17      | 132R    | 6/20/22       | 0.1      | 2.3                       | 4.46 | 100.89        | 100.88       | 0.01             | -0.083        | -0.081        | 0.002          | 69.6951       | Avg  |
| 7/11/17      | 132R    | 6/20/22       | 0.1      | 2.5                       | 4.85 | 100.67        | 100.66       | 0.01             | -0.035        | -0.033        | 0.002          | 81.8127       | Avg  |
| 6/8/17       | 132     | 6/20/22       | 0.1      | 2.4                       | 4.71 | 100.83        | 100.82       | 0.01             | -0.065        | -0.063        | 0.002          | 83.4769       | Good |
| 5/16/17      | 131R    | 3/20/22       | 0.1      | 2.3                       | 3.59 | 101.06        | 101.04       | 0.02             | -0.117        | -0.113        | 0.004          | 41.5877       | Avg  |
| 4/18/17      | 131R    | 3/20/22       | 0.1      | 2.3                       | 3.28 | 101.29        | 101.25       | 0.04             | -0.160        | -0.152        | 0.008          | 50.9655       | Poor |

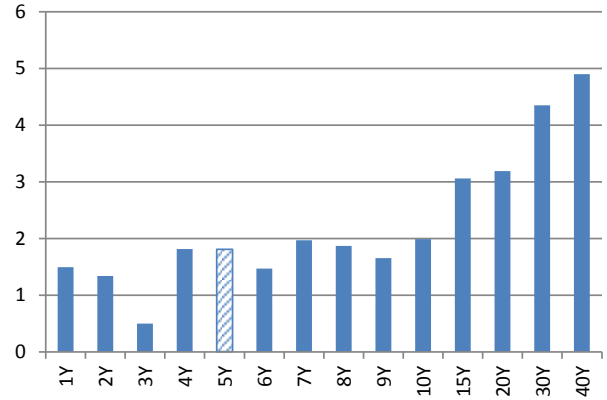
\* Daiwa forecast (as of May 16) \*\* Amount the MOF plans to issue  
Source: Ministry of Finance (MOF), Daiwa Securities.

Appendix 1: 5Y JGB Yield (%)



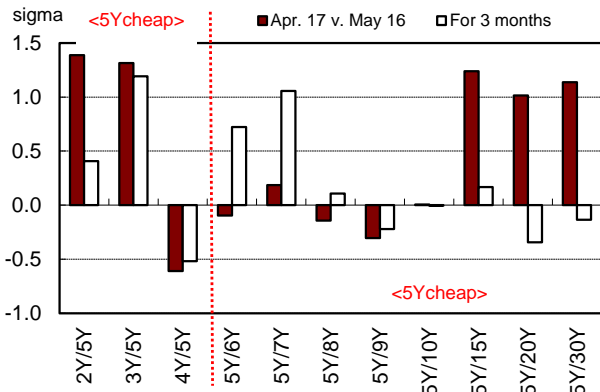
Source: Daiwa Securities.

Appendix 2: JGB Yield Change (April 17 v. May 16; bp)



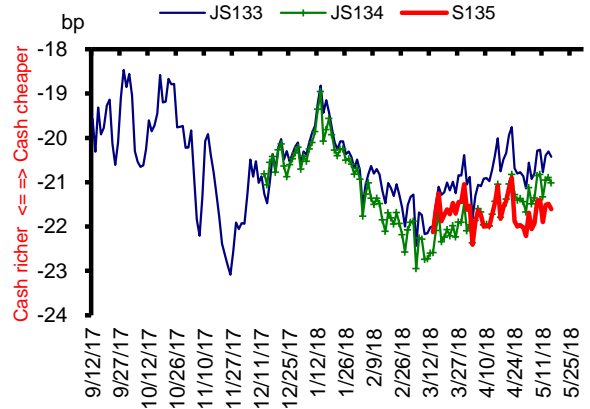
Source: Daiwa Securities.

Appendix 3: Z-scores of JGB Yield Spreads



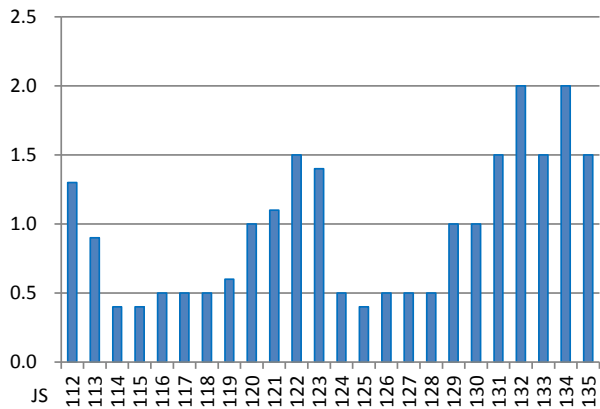
Source: Daiwa Securities.

Appendix 4: 5Y JGB Asset Swap Spreads



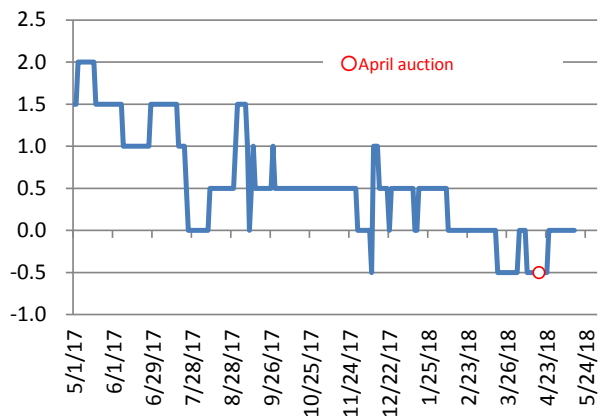
Source: Daiwa Securities.

Appendix 5: JS Yield Change (bp): Apr. 17 v. May 16



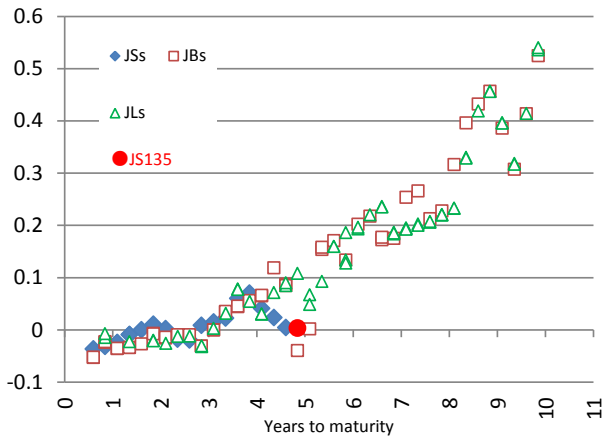
Source: Daiwa Securities.

Appendix 6: JS On-the-run and Off-the-run Spread (bp)



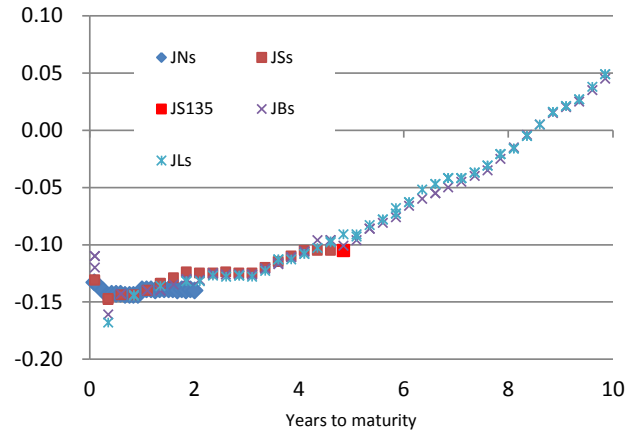
Source: Daiwa Securities.

**Appendix 7: 6M Total Returns of JSs, JBs and JLS (%)**



Note: Based on JB, JS and JL yield curves on May 15, respectively; Assuming that those yield curve shapes do not change and factoring roll-down effect etc.  
Source: Daiwa Securities.

**Appendix 8: JGB Yield Curve (%)**



Note: as of May 15  
Source: Daiwa Securities.

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- There is a risk that you will incur losses on your transactions due to changes in the market price of financial instruments based on fluctuations in interest rates, exchange rates, stock prices, real estate prices, commodity prices, and others. In addition, depending on the content of the transaction, the loss could exceed the amount of the collateral or margin requirements.
- There may be a difference between bid price etc. and ask price etc. of OTC derivatives handled by our company.
- Before engaging in any trading, please thoroughly confirm accounting and tax treatments regarding your trading in financial instruments with such experts as certified public accountants.

\* The amount of the trading commission cannot be stated here in advance because it will be determined between our company and you based on current market conditions and the content of each transaction etc.

\*\* The ratio of margin requirements etc. to the amount of the transaction cannot be stated here in advance because it will be determined between our company and you based on current market conditions and the content of each transaction etc.

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|                 |  |
|-----------------|--|
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