

## Outlook for 5Y JGB Auction

### A pre-auction correction to -0.07 - -0.06% level is desirable, though

- ✓ Relative-value wise, it will be worth considering switching out from 7-9Y sectors into new 5Y JGBs

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### Auction Details

**Auction Date:** November 15, 2018

**Issue Date:** November 16, 2018

**Maturity Date:** September 20, 2023

**Offering Amount:** About 2.0 trillion yen

\* New 5Y JGBs will likely be the first reopening of JS137 carrying a 0.1% coupon.

\*\* On November 14, JS137 traded at -0.095 - -0.090% (-1.0 - -0.5bp v. previous day's close) and closed at -0.090% (-0.5bp).

### Exp. Rating on Auction Results

1	2	3	4	5
Failed	Poor	Average	Good	Outstanding

### A pre-auction correction to -0.07 - -0.06% level is desirable, though

We look first at the environment surrounding 5-year JGBs. After the previous 5-year JGB auction held on October 16, which went smoothly at the level around -0.55%, the 5-year JGB yield headed down to -0.090% on an intraday trading basis, its lowest since August, within the context of the firmness of the JGB market on the back of global decline in share prices driven by US-China trade friction and other concerns. Since then, it has moved in a range of around -0.090% to -0.080%. Given also the sharp drop in oil prices recently, there appears to be a heightening of concerns over the direction of the global economy. With equity markets still performing poorly both in and outside of Japan, we think the JGB market may remain high and range-bound particularly in the near term.

In such an environment, key points to think about the bidding level at tomorrow's auction are as follows:

- ✓ The supply-and-demand balance on JS137 looks very tight in the repo market, which suggests relatively strong demand for short-covering.
- ✓ The narrow investor base brought by the low levels of liquidity in 5Y JGBs is a source of concern.
- ✓ The 5-year JGB yield reached an intraday trading low of -0.095% today, its lowest since July.

- ✓ The BOJ will not offer a purchase operation for JGBs in the 1-5Y zone the day after tomorrow's auction.
- ✓ Relative-value wise, the 5-year sector is now measurably cheap vs. the 7-9-year sector (Appendix 3). In the sector, JGBs are cheap to swaps as well.

**Switching out from 7-9Y into 5Y to think about**

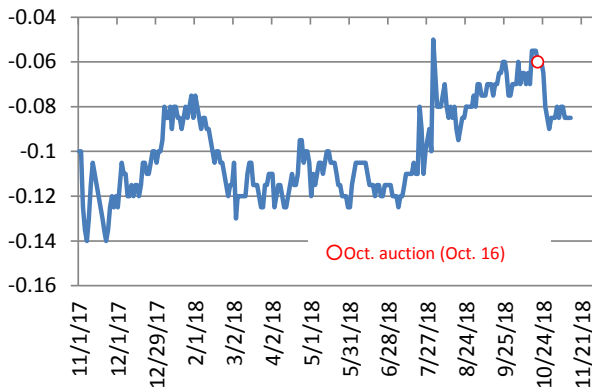
Given all together, we would like to hold our primary purchases of new 5Y JGBs to the necessary minimum, if bidding has to be done in the -0.095 - -0.085% level. Relative-value wise, it will be worth considering switching out from 7-9Y sector into new 5Y JGBs.

**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 (%)	
11/15/18	137R	9/20/23	0.1*										
10/16/18	137	9/20/23	0.1	2.0	4.88	100.77	100.76	0.01	-0.055	-0.053	0.002	40.2505	Avg
9/13/18	136R	6/20/23	0.1	2.0	5.53	100.82	100.81	0.01	-0.071	-0.069	0.002	10.5496	Good
8/16/18	136R	6/20/23	0.1	2.1	3.95	100.86	100.85	0.01	-0.076	-0.074	0.002	37.0117	Avg
7/10/18	136	6/20/23	0.1	2.0	4.87	101.03	101.02	0.01	-0.107	-0.105	0.002	39.4402	Avg
6/21/18	135R	3/20/23	0.1	2.0	3.88	101.02	101.00	0.02	-0.113	-0.109	0.004	61.1594	Poor
5/17/18	135R	3/20/23	0.1	2.0	4.22	100.99	100.98	0.01	-0.103	-0.101	0.002	33.7643	Avg
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

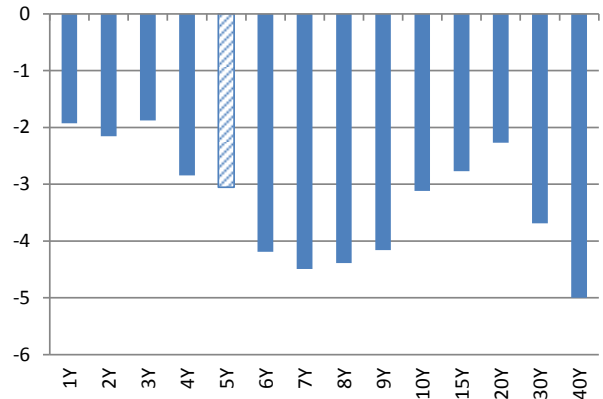
\* Daiwa forecast (as of Nov. 14) \*\* Amount the MOF plans to issue  
Source: Ministry of Finance, Daiwa Securities.

**Appendix 1: 5Y JGB Yield (%)**



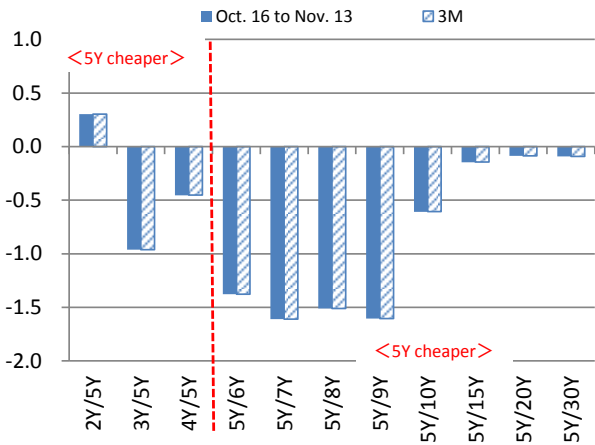
Source: Daiwa Securities.

**Appendix 2: JGB Yield Change (bp): Oct. 16 v. Nov. 13**



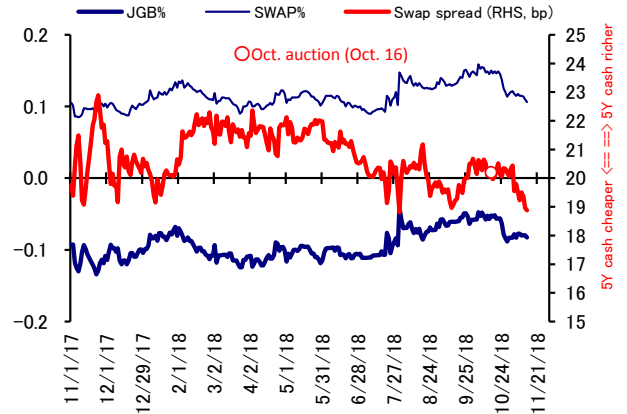
Source: Daiwa Securities.

### Appendix 3: Z-scores of JGB Yield Spreads



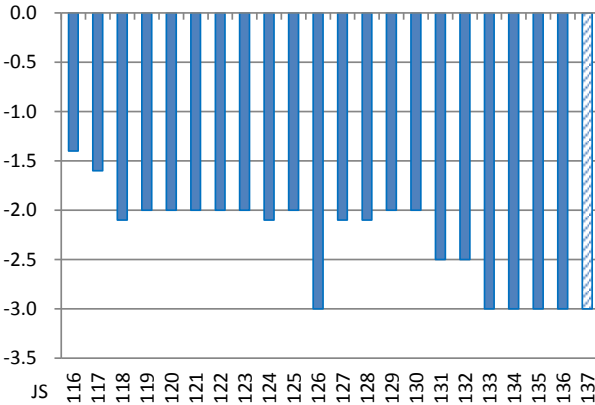
Source: Daiwa Securities.

### Appendix 4: 5Y Swap Spread



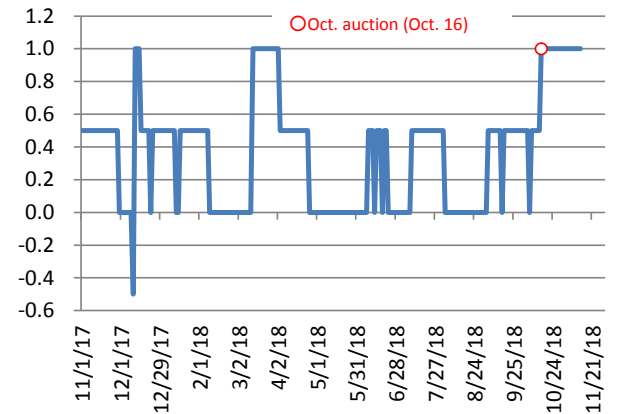
Source: Daiwa Securities.

### Appendix 5: JS Yield Change (bp): Oct. 16 v. Nov. 16



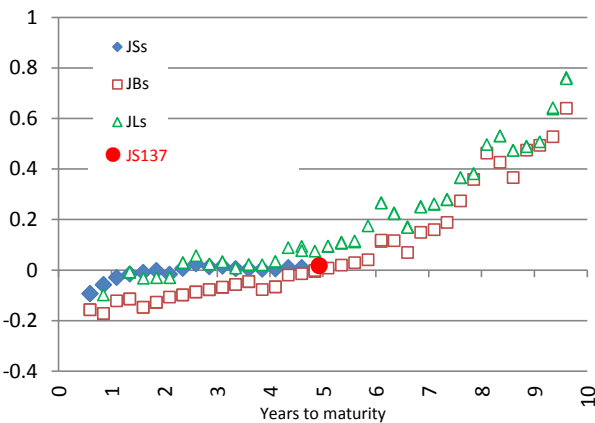
Source: Daiwa Securities.

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



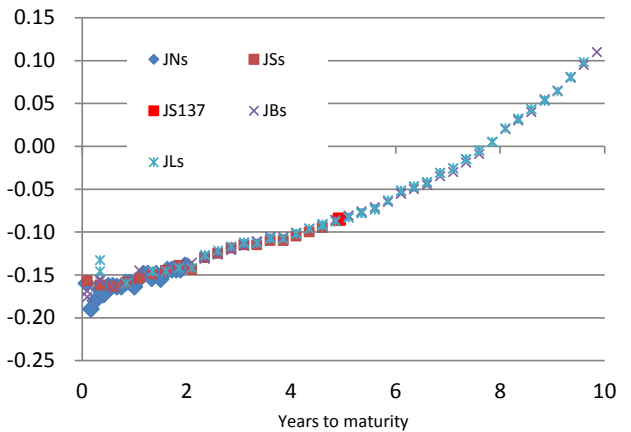
Source: Daiwa Securities.

### Appendix 7: 6M Total Returns of JSs, JBs and JLs (%)



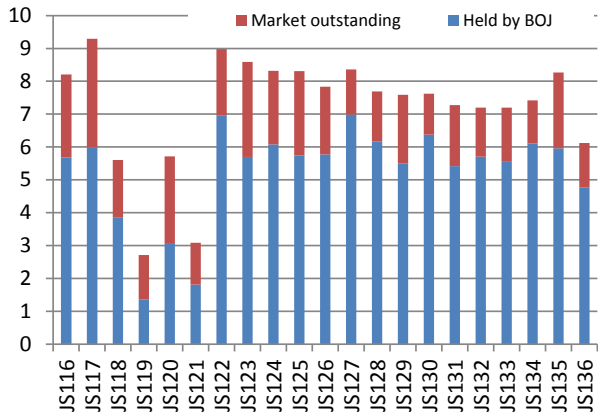
Note: Based on JB, JS and JL yield curves on Nov. 13, respectively; Assuming that those yield curve shapes do not change and factoring roll-down effect est.  
Source: Daiwa Securities.

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



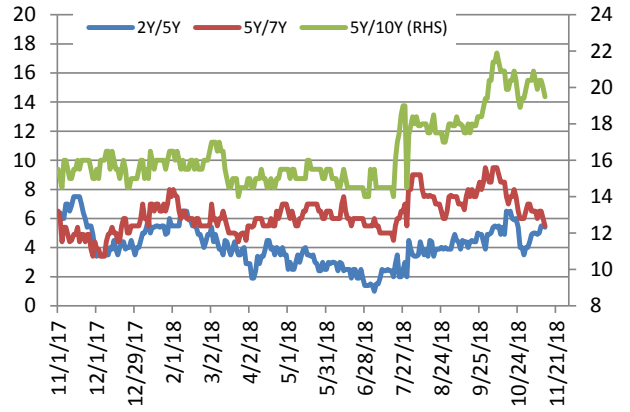
Note: as of Nov. 13  
Source: Daiwa Securities.

**Appendix 9: BOJ and Market Outstanding of JSs (Yen trillions)**



Source: Ministry of Finance, Bank of Japan, Daiwa Securities.

**Appendix 10: JGB Yield Spreads (bp)**



Source: Daiwa Securities.

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May 2018

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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.
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