

Outlook for 10Y JGB Auction

Smooth auction is expected amid good market sentiment

- ✓ Tomorrow's auction will be held at the lowest yield level since July 2016, but smooth auction is expected as market sentiment for the 10Y sector remains favorable
- ✓ We would like to place our bids to be able to take the necessary amount at tomorrow's auction, assuming that the 10Y JGB yield will move in the range centered at -0.10% over the next one month.
- ✓ In terms of the relative value, we think of the possibility of a pause in tightening of 10Y/30Y spread over the short term

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Auction Details

Auction Date:	June 4, 2019
Issue Date:	June 5, 2019
Maturity Date:	March 20, 2029
Offering Amount:	About 2.1 trillion yen

* New 10-year JGBs will likely be the final reopening of JB354 carrying a 0.1% coupon.

** On June 3, JB354 traded at -0.100 - -0.095% (unch - +0.5bp v. previous day's close), and closed at -0.095% (+0.5bp).

Exp. Rating on Auction Results

1	2	3	4	5
Failed	Poor	Average	Good	Outstanding

Tomorrow's auction will be held at the lowest yield level since July 2016

Since the previous 10Y JGB auction went smoothly at around -0.060% on May 8, the bond markets have firmed up around the globe due to caution about risk-off trends as the outlook of US-China trade talks have become more uncertain. In such a situation, the 10Y JGB yield has declined from -0.045% to -0.100% on an intraday basis. Tomorrow's auction will be held at the lowest yield level since July 2016.

Demand from investors appears strong for 10Y with attractiveness in terms of carry on the short- to long-term zone of the curve

Worries about the global economy are lingering partly because of factors that are unlikely to be resolved immediately, such as Brexit and trade frictions vs. the US. As witnessed by an increase in the number of market participants expecting Fed's multiple rate cuts in 2019, it is difficult to globally expect strong upward pressure on yields. In such an environment, investor demand for neighboring issues of the on-the-run 10Y JGB appears to be strong partly because those issues are the most attractive in terms of carry on the short- to long-term zone of the curve, where yields are falling in negative territory across the board (Appendix 5). Reflecting this, the market sentiment for the 10Y sector remains favorable.

BOJ purchase operations to be skipped on the following day of auction

A near-term concern is the BOJ's purchase operations. In June, purchase operations in the 5-10Y zone are not planned on the following day of the 10Y JGB auction. This is the first time since the BOJ set the guideline of about 80tn yen for an annual pace of increase in its JGB holdings. This may have an impact on the bidding stance in a greater or lesser degree as a risk of the so-called "BOJ trade" would increase slightly.

We would like to place our bids to be able to take the necessary amount / In terms of relative value, we assume short-term pause in tightening of 10Y/30Y spread

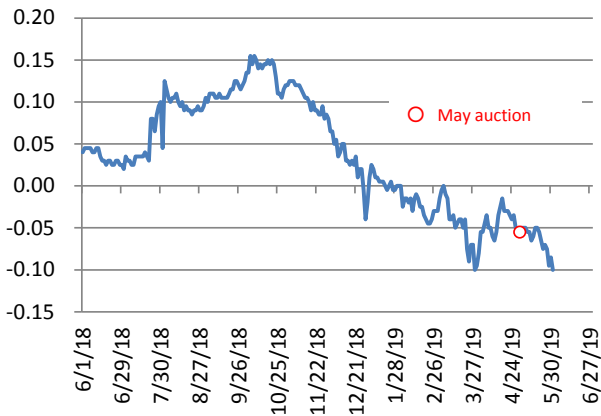
All in all, we would like to place our bids to be able to take the necessary amount at tomorrow's auction, assuming that the 10Y JGB yield will move in the range centered at -0.10% over the next one month. In terms of the relative value, we think of the possibility of a short-term pause in the tightening of 10Y/30Y spread (Appendix 6). Reflecting the BOJ's JGB purchase guideline for June, the yield curve in the superlong zone may be volatile until the first offer amount in the over 10Y zone is confirmed. Meanwhile, the offer amount in the 5-10Y zone may be unchanged from that in the final operation in May because the central bank plans to skip a purchase on the following day of the 10Y JGB auction for the first time. Activities to reduce existing flattening positions may correct the latest tightening of the 10Y/30Y spread in the short term.

10Y JGB Auction Results

Auction Date	Issue#	Coupon %	Maturity Date	Issue Size (billion yen)	Bid/Cover	Average Accepted Price	Lowest Accepted Price	Tail (yen)	Average Accepted Yield	Highest Accepted Yield	Tail (%)	Allotment %	
6/4/19	354R*	0.1*	3/20/29	2,100**									
5/8/19	354R	0.1	3/20/29	2,099	4.44	101.59	101.57	0.02	-0.060	-0.058	0.002	36.0139	Avg
4/2/19	354	0.1	3/20/29	2,412	5.07	101.61	101.60	0.01	-0.060	-0.059	0.001	37.4603	Good
3/5/19	353R	0.1	12/20/28	2,233	4.25	101.00	100.98	0.02	-0.002	0.000	0.002	74.5124	Poor
2/5/19	353R	0.1	12/20/28	2,528	4.80	101.12	101.11	0.01	-0.013	-0.012	0.001	61.9168	Good
1/8/19	353	0.1	12/20/28	2,235	4.04	100.84	100.83	0.01	0.015	0.016	0.001	39.9871	Good
12/4/18	352R	0.1	9/20/28	2,526	3.82	100.25	100.22	0.03	0.074	0.077	0.003	8.7628	Poor
11/1/18	352R	0.1	9/20/28	2,513	4.33	99.95	99.93	0.02	0.135	0.137	0.002	12.9543	Avg
10/2/18	352	0.1	9/20/28	2,436	4.21	99.59	99.58	0.01	0.141	0.142	0.001	47.4678	Good
9/5/18	351R	0.1	6/20/28	2,506	4.55	99.87	99.86	0.01	0.113	0.115	0.002	57.5664	Avg
8/2/18	351R	0.1	6/20/28	2,485	4.17	99.74	99.62	0.12	0.126	0.138	0.012	48.9994	Poor
7/3/18	351	0.1	6/20/28	2,478	4.37	100.62	100.60	0.02	0.037	0.039	0.002	38.2288	Good
6/5/18	350R	0.1	3/20/28	2,255	4.38	100.50	100.49	0.01	0.048	0.049	0.001	94.4896	Good
5/8/18	350R	0.1	3/20/28	2,432	4.20	100.53	100.52	0.01	0.046	0.047	0.001	91.9407	Good

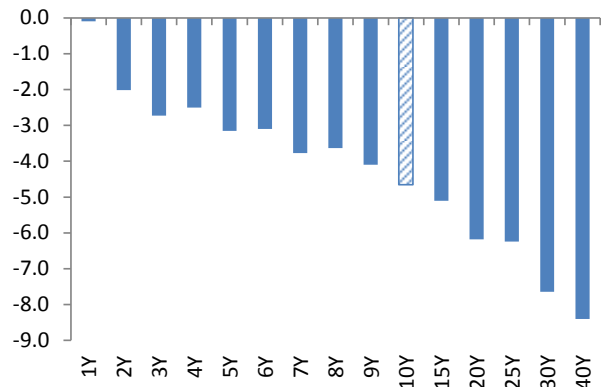
* Daiwa forecast as of June 3 ** Amount the MOF plans to issue
Source: Ministry of Finance (MOF), Daiwa Securities.

Appendix 1: 10Y JGB Yield (%)



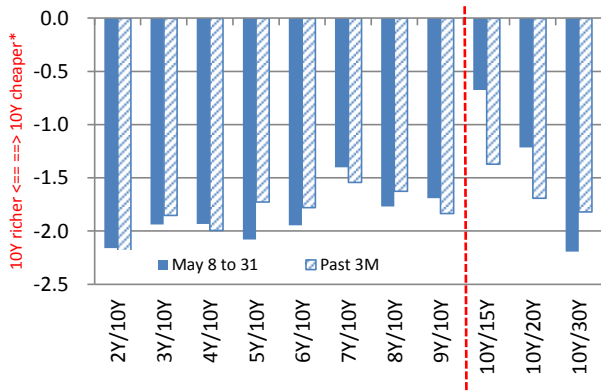
Source: Daiwa Securities.

Appendix 2: JGB Yield Change (May 8 v. May 31, bp)



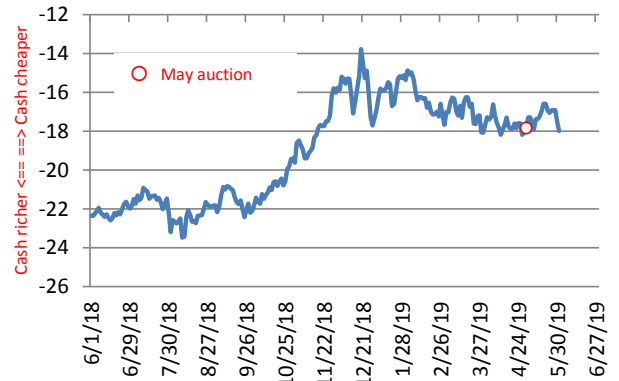
Source: Daiwa Securities.

Appendix 3: Z-scores of JGB Yield Spreads



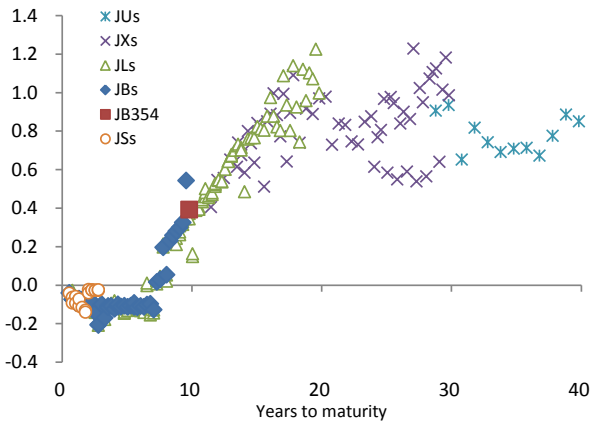
Note: + (-) 10Y richer (cheaper) for 10Y/15Y, 10Y/20Y and 10Y/30Y
 Source: Daiwa Securities.

Appendix 4: 10Y JGB Asset Swap Spread (bp)



* Yen LIBOR basis
 Source: Daiwa Securities.

Appendix 5: JGB Total Return Curve (3M, %)



Note: Based on JGB yield curve on May 31; assuming that those yield curve shapes do not change and factoring roll-down effect etc.
 Source: Daiwa Securities.

Appendix 6: JGB 10Y/30Y Spread (bp)



Note: On-the-run issue basis
 Source: Daiwa Securities

Explanatory Document of Unregistered Credit Ratings

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- 2) Establishment of control systems (fairness of the rating process, and prevention of conflicts of interest, etc.).
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■ Credit Rating Agencies

[Standard & Poor's]

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[Moody's]

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[Fitch]

The Name of the Credit Rating Agencies group, etc

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May 2018

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- In addition to the purchase price of a financial instrument, our company will collect a trading commission* for each transaction as agreed beforehand with you. Since commissions may be included in the purchase price or may not be charged for certain transactions, we recommend that you confirm the commission for each transaction. In some cases, our company also may charge a maximum of ¥ 2 million (including tax) per year as a standing proxy fee for our deposit of your securities, if you are a non-resident.
- For derivative and margin transactions etc., our company may require collateral or margin requirements in accordance with an agreement made beforehand with you. Ordinarily in such cases, the amount of the transaction will be in excess of the required collateral or margin requirements**.
- 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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