

JGB Insight

BOJ moves to curb downward pressure on 10Y JGB yield

- ✓ Gaining caution about the 10Y JGB yield facing downward pressure around -0.2%, the BOJ significantly adjusted JGB purchases they offered today (Aug. 9).
- ✓ Today's adjustments imply that the central bank needs to take some actions to keep the 10Y JGB yield within "about double the range of between -0.1 and +0.1%" unless they start discussing about widening it at the MPM. The confirmed limited upside of 10Y JGBs may lead the JGB yield curve in the long-to superlong-term zone to further flatten.
- ✓ It is the BOJ purchases in the 5-10Y zone which have been keeping the short- to long-term zone of the curve concaved.
- ✓ We expect the BOJ to trim its purchase in the 5-10Y zone with a higher probability on Aug. 16.

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BOJ adjusted offer amounts in JGB purchase operations

In its JGB purchase operations in the 1-5Y zone and the over 10Y zone offered today (Aug 9), the BOJ adjusted the offer amounts (up in 1-3Y zone, down in 3-5Y zone and 10-25Y zone; chart below). The offer amounts in all these zones were adjusted for the first time since the first operation in July, when the purchase amounts were modified in line with a downward revision to the offer ranges in the BOJ's "Outline of Outright Purchases of Japanese Government Securities" announced at the end of June. We attribute today's adjustments to the following factors: (1) since the beginning of August, the 10Y JGB yield has been falling on an accelerated pace, (2) after the yield temporarily fell to -0.215% early this week on an intraday basis, it has been moving at around the lower end of the current operational target range, "about double the range of between -0.1% and +0.1%," and (3) the short-term/intermediate zone of the JGB yield curve has inverted, alongside further flattening of the superlong zone. After the operation notice, JGB futures plunged at one point, but subsequently hit its highest of the leading contract. Given another rally in the futures in the afternoon session, the 10Y JGB yield declined to -0.220% at one point (-2.5bp vs. previous day's close) as of 15:00.

BOJ JGB Purchase Operations (Yen billions)

| BOJ offer day / JGB auction day | (BOJ start day/ MOF settlement day) | Up to 1 year | Over 1 to 3 years | Over 3 to 5 years | Over 5 to 10 years | Over 10 to 25 years | Over 25 years | JGB Linker | JGB Floater |
|---------------------------------|-------------------------------------|---|-------------------|-------------------|--------------------|---------------------|---------------|------------|-------------|
| 7/31/19 W | 8/1/19 | | 380.8 | 380.7 | 481.9 | | | | |
| 8/1/19 TH | 8/2/19 | 10Y JGB Auction | | | | | | | |
| 8/2/19 F | 8/5/19 | | | | | 181.3 | 40.0 | 25.1 | |
| 8/5/19 M | 8/6/19 | 50.1 | | | 480.8 | | | | 100.3 |
| 8/6/19 T | 8/7/19 | 30Y JGB Auction | | | | | | | |
| 8/7/19 W | 8/8/19 | | | | | | | | |
| 8/8/19 TH | 8/9/19 | 10Y Linker JGB Auction | | | | | | | |
| 8/9/19 F | 8/13/19 | | 400.1 | 360.4 | | 160.2 | 40.3 | | |
| 8/12/19 M | - | Public Holiday (Mountain Day obs.) | | | | | | | |
| 8/13/19 T | 8/14/19 | | | | | | | | |
| 8/14/19 W | 8/15/19 | | | | | | | | |
| 8/15/19 TH | 8/16/19 | 5Y JGB Auction | | | | | | | |
| 8/16/19 F | 8/19/18 | | | | ◎ | | | ○ | |

Note: Figures are actual: increased from the previous operation in green; decreased in red. ◎ scheduled by the BOJ, ○ Daiwa forecast as of Aug. 9
Source: Bank of Japan, Ministry of Finance, Daiwa Securities

10Y JGB yield of around -0.2% confirmed to make the BOJ uneasy

While the impact of the BOJ's flow-basis adjustments to the offer amounts on the yield curve shape becomes gradually limited, today's adjustments in the offer amounts give strong recognition to market participants that the lower end of the 10Y JGB yield is around -0.2%. BOJ Governor Kuroda's remarks with respect to the fluctuation range of the long-term interest rate at his press conference after the June Monetary Policy Meeting

(MPM) included the followings—“we keep in mind about double the range of between -0.1% and +0.1%” and “we do not need to be excessively strict about the range for yield fluctuation ... it is appropriate to flexibly cope with the moves.” Also in terms of expansion of the monetary base, scope for reducing the JGB purchase amount appears limited. In such a situation, the BOJ should have been bearable for a drop of the 10Y JGB yield to around -0.25% amid the current global downtrend in bond yields. Today’s adjustments imply that the central bank needs to take some actions to keep the 10Y JGB yield within “about double the range of between -0.1 and +0.1%” unless they start discussing about widening it at the MPM.

Confirmed lower end of the 10Y JGB yield would lead the superlong zone to further flatten

As the lower end of the 10Y JGB yield has been clarified, it is highly possible that the superlong zone will face further flattening pressure. Amid the global yield downtrend, JGB yields with about 15 years or less to maturity have fallen below zero. In such a situation, potential demand from both domestic and overseas investors for superlong JGBs with positive yields and expected high carry appears to be strong. Such demand is likely to continue to support favorable market sentiment around the long end of the curve.

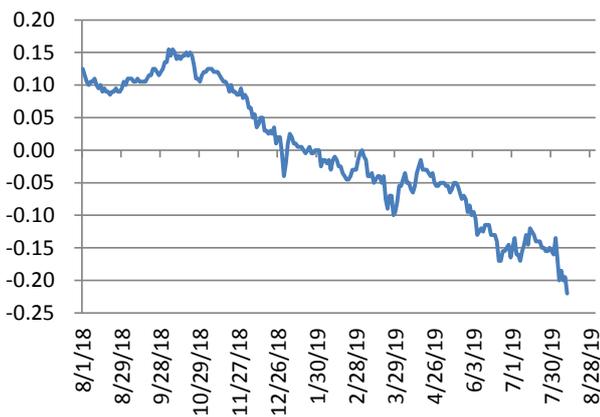
BOJ’s JGB purchase in the 5-10Y zone is the main factor to keep short- to long-term zone concaved

The short- to long-term zone of the yield curve has concaved in around the 7Y sector. This appears to be mainly caused by the BOJ’s JGB purchases in the 5-10Y zone, rather than those in the 1-5Y zone. With the fact that the BOJ is the largest holder of JGBs in the 5-10Y zone, its purchase amount in the zone via operations is the highest among the all target zones as well as in terms of the ratio to the MOF’s issuance amount. Moreover, the BOJ’s purchase targets for 10Y JGBs in the zone have been limited to issues in the 6Y and 9-10Y sectors, leading to tighter supply/demand condition for these issues. Rock-solid neighboring sectors have been providing strong support to the 7Y sector.

Paying attention to the purchase operation in 5-10Y zone on Aug 16

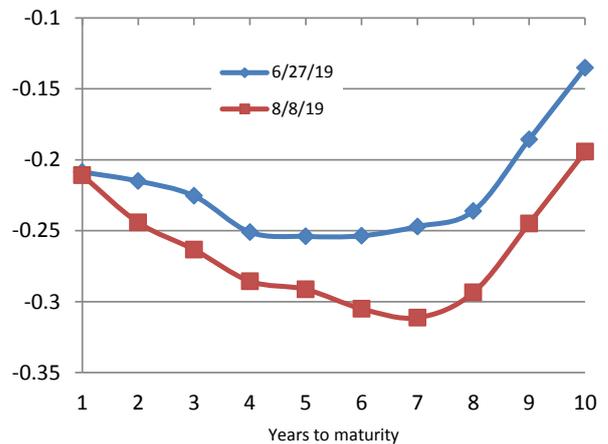
Given those factors above, we would like to closely watch the next JGB purchase operation by the BOJ (for JGBs in the 5-10Y zone on August 16). We expect the BOJ to trim its purchase at the operation with a higher probability.

10Y JGB Yield (%)



Note: On-the-run issue Japanese yield basis; as of 15.00 JST, Aug. 9
Source: Ministry of Finance, compiled by Daiwa Securities

JGB Yield Curve Shape Comparison (%)



Source: Daiwa Securities.

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[Standard & Poor's]

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[Fitch]

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