Daiwa's View

Successful "helicopter credit" measures

➢ Fallen angels also included in support target

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Daiwa Securities Co. Ltd.

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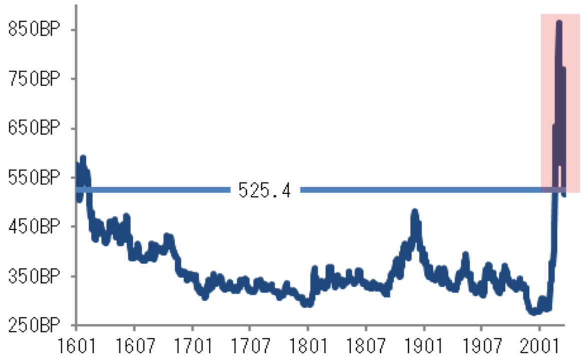
Last night, the DJIA rose to 23,719. Rather, yesterday's noteworthy point is improvement in the credit indices—the North American Investment Grade CDS Index tightened from 106bp to 87bp, and the High-yield CDS Index substantially improved from 635bp to 525bp. This time around, the Fed has decided on extraordinary measures, in which the support target will include not only investment grade bonds but also a part of bonds issued by recently downgraded firms to the speculative grade ("fallen angels"). This has eased concerns about being excluded from the Fed's support net in the case of downgrades to the speculative grade with the prolongation of economic downturns due to the COVID-19 pandemic.

We can say that this is an unprecedented action to reinforce the "helicopter credit" measures on 23 March. On the day, the Fed established a huge credit facility, and Chair Jerome Powell declared on 26 March that "We are not going to run out of ammunition" on his extraordinary TV appearance. This has relieved investment grade companies from worries about financing. It is no coincidence that risk asset prices started to rebound strongly from that day. It is hardly surprising that the market has favored the latest bold actions to strengthen support for corporate financing.

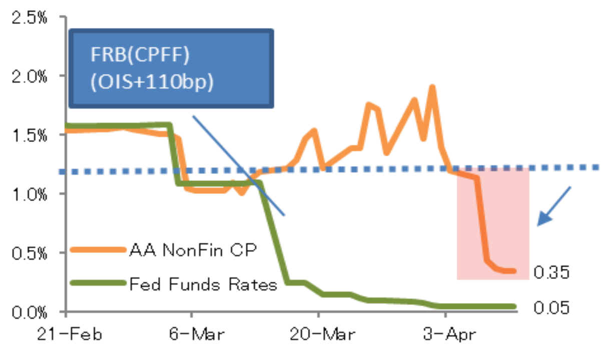
Although support measures are expanding, it is not to say that companies are falling into dependence on such measures. For example, the 1-month interest rate for AA-rated non-financial firms declined to 0.35% in the commercial paper market, a key for short-term funding. Funds are raised at a lower rate than the Fed's facility (OIS + 110bp), which implies that the market is weaning itself from Fed support. Due to the tightening of funding spreads, the benefit of the zero interest rate is finally reaching AA-rated firms, which is likely to be widespread going forward.

Chart: North American High-yield CDS Index (5Y)



Source: Bloomberg; compiled by Daiwa Securities.

Chart: US Commercial Paper (non-financial, 1M)



Source: Bloomberg; compiled by Daiwa Securities.

However, it is a pity that Japan is in a severe situation compared to the US, where bright signs have come into sight. Belatedly, the CP procurement cost is surging in Japan, leading to the postponement of bond issuance in the corporate bond market. Yesterday, it was reported that Nissan Motor sought a commitment line worth around Y500bn from three mega banks and the Development Bank of Japan. Regarding the request for the commitment line, All Nippon Airways and Toyota Motor reportedly sought Y1.3tn and Y1tn, respectively. The necessary funds amount to as much as Y2.8tn at these three firms alone. Although the BOJ decided to increase the CP/corporate bond purchase amount on 16 March, the size of funds required by companies is now rapidly expanding in Japan following the declaration of a state of emergency. I think that there is a two-digit difference in the size between the required amount and the BOJ's setting.

At yesterday's meeting of regional branch managers, BOJ governor Haruhiko Kuroda stated that "corporate financing is worsening," and "we will contribute to smooth funding at companies." He also said there would no hesitation to take additional monetary easing measures if needed. Funding support via policy-based financial institutions is also important. However, what is now required is probably an increase in purchases of assets targeting investment grade companies. In particular, pre-emptive responses are desirable for the CP market as its deterioration would raise concerns about financing and freeze corporate sentiment. We look for expansion of financing backstop measures also in Japan by referring to the establishment of the facility in the US corresponding to 20-30% of GDP.

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■ Credit Rating Agencies

[Standard & Poor's]

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As of end-December 2017, Daiwa Securities Group Inc. owned shares in GMO Financial Holdings, Inc. equivalent to approximately 9.3% of the latter's outstanding shares. Given future developments in and benefits from the prospective business alliance, Daiwa Securities Group Inc. could boost its stake in GMO Financial Holdings, Inc. to up to 20% of outstanding shares.

2) Daiwa Real Estate Asset Management is a subsidiary of Daiwa Securities Group Inc. and serves as the asset management company for the following J-REITS: Daiwa Office Investment Corporation (8976), Daiwa Securities Living Investment Corporation (8986).

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* 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.
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