

Daiwa's View

10-year US yield fell back to 0.7% level

- Overwhelming purchases of 'all risk assets' in market

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Daiwa Securities Co. Ltd.

Overwhelming purchases of 'all risk assets' in market

10-year US yield fell back to 0.7% level

Yesterday, the market bought 'all risk assets' overwhelmingly. At around 9:00am Tokyo time, the long-term US Treasury yield rose to 0.94% at one point. However, once the media reported President Trump's strong fight in battleground states, 'blue wave trading' was unwound and eventually the US long-term yield fell to 0.76%. Regarding the congressional election, the Republic Party is leading in the Senate, meaning that a divided congress will be inevitable. Although Mr. Joe Biden is leading in the presidential election by a narrow margin, it looks like the election will end up being settled in a court battle.

Among yesterday's series of price movements, we will first focus on the substantial decline in the breakeven inflation rate (BEI). Yesterday, the 10-year US yield fell by 13bp, 9bp of which was caused by a lower BEI. The substantial drop in the BEI suggests progress in the unwinding of trades that expected a 'blue wave.'

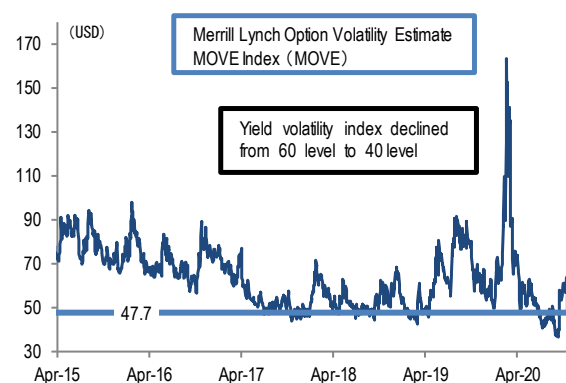
More importantly, however is that this decline in inflation expectations will stabilize the 5-year yield. With the Fed's target of average inflation of 2% and forward guidance, a decline in inflation expectations has the effect of deferring the timing of the expected rate-hike. In that sense, the decline in the 5-year yield from 0.40% to 0.33% in line with the drop in the BEI is more significant than it looks. If we assume that the 5-year yield has restored stability amid diminishing uncertainty about the presidential election, we could say that yield volatility, which has risen recently, has taken its cue to decline.

10Y US Inflation Expectation Rate (BEI)



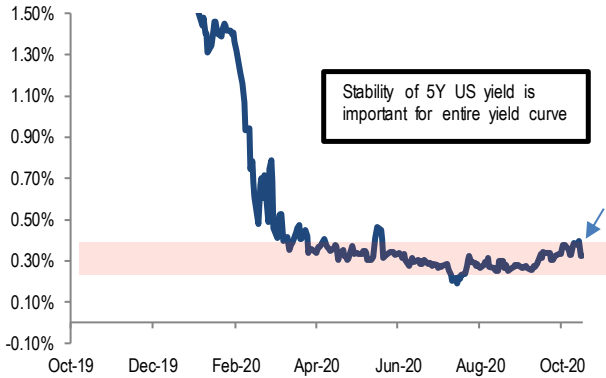
Source: Bloomberg; compiled by Daiwa Securities.

US Bond Volatility Index



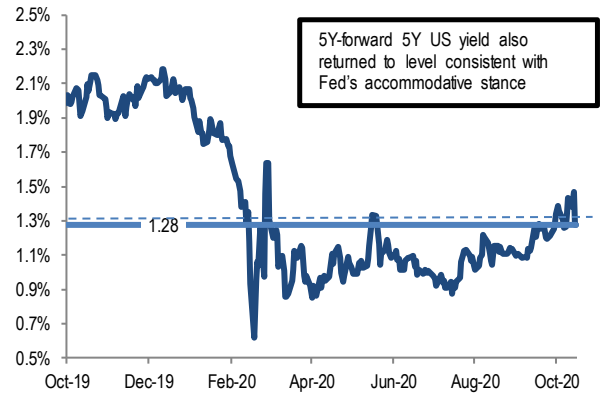
Source: Bloomberg; compiled by Daiwa Securities.

5Y US Yield



Source: Bloomberg; compiled by Daiwa Securities.

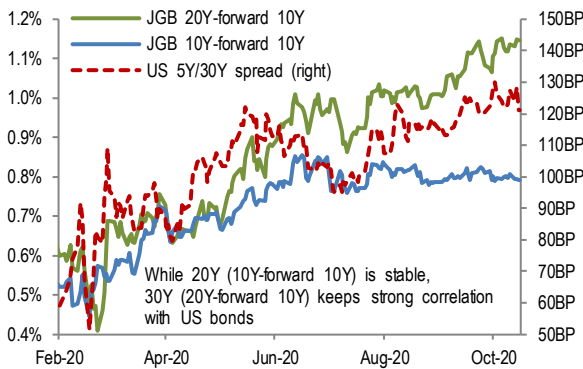
5Y-forward 5Y US Yield



Source: Bloomberg; compiled by Daiwa Securities.

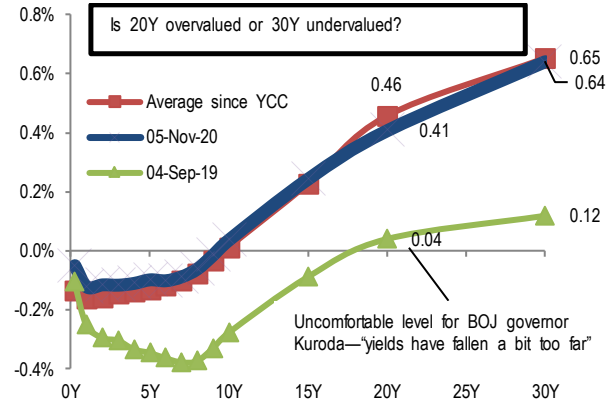
Recently, the correlation between JGBs and US yields has not been particularly strong. However, the 30-year JGB yield (20-year forward 10-year yield) has seen exceptional steepening, maintaining a high correlation with rising US yields. Therefore, this zone may face the strongest impact from the US presidential election. This may serve as a slight incentive to buy at the 30-year JGB auction slated for 10 November next week, particularly considering that the absolute level of the 20-year forward 10-year yield has already risen to 1.13% and its spread with the 10-year forward 10-year yield has widened to 33bp.

JGB 10Y Forward Yields, US 5Y/30Y Spread



Source: Bloomberg; compiled by Daiwa Securities.

JGB Yield Curve



Source: Bloomberg; compiled by Daiwa Securities.

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■ Credit Rating Agencies

[Standard & Poor's]

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[Moody's]

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[Fitch]

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Daiwa Securities Co. Ltd. and Daiwa Securities Group Inc.: Daiwa Securities Co. Ltd. is a subsidiary of Daiwa Securities Group Inc.

Other Disclosures Concerning Individual Issues:

1) As of 26 April 2016, Daiwa Securities Co. Ltd., its parent company Daiwa Securities Group Inc., GMO Financial Holdings, Inc., and its subsidiary GMO CLICK Securities, Inc. concluded a basic agreement for the establishment of a business alliance between the four companies.

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).

3) Samty Residential Investment became a consolidated subsidiary of Daiwa Securities Group Inc. effective 10 September 2019.

4) On 30 May 2019, Daiwa Securities Group Inc. formalized an equity/business alliance with Samty, and as of 14 June 2019 it owned 16.95% of shares outstanding in Samty along with convertible bonds with a par value of ¥10bn. Conversion of all of said convertible bonds into common shares would bring the stake of Daiwa Securities Group Inc. in Samty to 27.28%.

5) Daiwa Securities Group Inc. and Credit Saison Co., Ltd. entered into a capital and business alliance, effective 5 September 2019. In line with this alliance, Daiwa Securities Group Inc. is to acquire up to 5.01% of Credit Saison's total common shares outstanding (excl. treasury shares; as of 31 Jul 2019).

Notification items pursuant to Article 37 of the Financial Instruments and Exchange Law

(This Notification is only applicable to where report is distributed by Daiwa Securities Co. Ltd.)

If you decide to enter into a business arrangement with our company based on the information described in this report, we ask you to pay close attention to the following items.

- 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 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.

When making an actual transaction, please be sure to carefully read the materials presented to you prior to the execution of agreement, and to take responsibility for your own decisions regarding the signing of the agreement with our company.

Corporate Name: Daiwa Securities Co. Ltd.

Registered: Financial Instruments Business Operator, Chief of Kanto Local Finance Bureau (Kin-sho) No.108

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