

JGB Insight

Issuance of 40-year JGBs to increase in response to strong market demand

- ✓ Total JGB issuance in FY2021 will decline Y27.1 trillion relative to FY2020 issuance (including third supplementary budget) to Y236 trillion; large increase in FILP bond issuance is somewhat of a surprise
- ✓ Calendar-based market issuance will decline on an annualized basis; 40-year JGB issuance to increase, as strongly demanded by the market; 6-month T-bill issuance will decline to reduce issuance of refunding bonds
- ✓ We expect the 40-year JGB issuance increase to correct excessive distortions in the 20y/30y/40y curve

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Total JGB issuance in FY2021 will decline Y27.1 trillion relative to FY2020 issuance (including the third supplementary budget) to Y236 trillion

The Suga Cabinet approved the FY2021 budget at a cabinet meeting held on December 21. At the same time, the MOF announced its FY2021 JGB issuance plan. The FY2021 budget includes funding from Y43.6 trillion of newly issued bonds (Y6.3 trillion of construction bonds and Y37.3 trillion of special deficit-financing bonds). The initial FY2021 JGB issuance plan reflecting this is shown in Table 1 below. JGB issuance in FY2021 will total Y236 trillion, which is Y27.1 trillion less than in FY2020 after including funding for the third supplementary budget.

Table 1: JGB Issuance Plan for FY2021 (Yen trillions)

<Breakdown by Legal Grounds>

	FY2020 Initial <a>	FY2020 after the 3rd s/b 	FY2021 Initial <c>	FY2021 Initial	
				<c>-<a>	<c>-
Newly-issued Bonds	32.6	112.6	43.6	11.0	▲ 69.0
Construction Bonds	7.1	22.6	6.3	▲ 0.8	▲ 16.3
Deficit Bonds	25.4	90.0	37.3	11.8	▲ 52.7
Reconstruction Bonds	0.9	0.8	0.2	▲ 0.7	▲ 0.6
FILP Bonds	12.0	40.7	45.0	33.0	4.3
Refunding Bonds	108.0	109.0	147.2	39.2	38.2
For Reconstruction Bonds	1.7	2.7	2.9	1.2	0.1
TOTAL	153.5	263.1	236.0	82.5	▲ 27.1

<Breakdown by Financing Methods>

	FY2020 Initial <a>	FY2020 after the 3rd s/b 	FY2021 Initial <c>	FY2021 Initial	
				<c>-<a>	<c>-
Financed in the Market	146.5	257.7	229.7	83.2	▲ 28.0
Calendar-based Market Issuance	128.8	212.3	221.4	92.6	9.1
Non-price Comp. Auction II	8.0	7.7	8.2	0.2	0.5
Adjustment between fiscal years	9.7	37.6	0.1	▲ 9.6	▲ 37.5
Sales for Households	4.8	3.2	4.1	▲ 0.7	0.9
BOJ Rollover	2.2	2.2	2.2	-	-
TOTAL	153.5	263.1	236.0	82.5	▲ 27.1

Source: Ministry of Finance (MOF)

Large increase in FILP bond issuance is somewhat of a surprise

On issuance by legal grounds, issuance of newly-issued bonds appears to be relatively small mostly because total spending and revenues will be about Y106.6 trillion, only Y4.0 trillion higher than the initial FY2020 budget. Meanwhile, issuance of FILP bonds will increase substantially from the Y11.5 trillion initially requested and nearly to 54.2 trillion yen after the second supplementary budget in FY2020 (which was revised down to Y40.7 trillion after the third supplementary budget). This is somewhat of a surprise, considering that the FY2021 FILP plan was Y40.9 trillion (including fiscal loan of about Y31 trillion). There was also a large increase in refunding bonds to Y147.2 trillion, up from the Y136.5 trillion target set by MOF after the second supplementary budget, on the back of the decline in FILP bonds after the third supplementary budget in FY2020.

Calendar-based market issuance to decline on an annualized basis; 40-year JGB issuance to increase, as strongly demanded by the market; 6-month T-bill issuance to decline to reduce issuance of refunding bonds

Looking at issuance based on financing methods, calendar-based market issuance will increase to Y221.4 trillion, Y9.1 trillion higher than FY2020 issuance after the third supplementary budget. For purposes of issuing bonds that meet market demand while also striving to reduce the issuance of T-bills that will cause refunding bond issuance to increase in FY2022, this represents a decline in 6-month T-bill issuance (annual decline of Y4.4 trillion) and increase in 40-year JGB issuance (annual increase of Y0.6 trillion). The decline in T-bill issuance and increase in 40-year JGB issuance has been expected by the market since the JGB market special participants meeting held on December 11, and thus not a surprise (Table 2).

Table 2: Calendar-based JGB Issuance in FY2021 (Yen trillions)

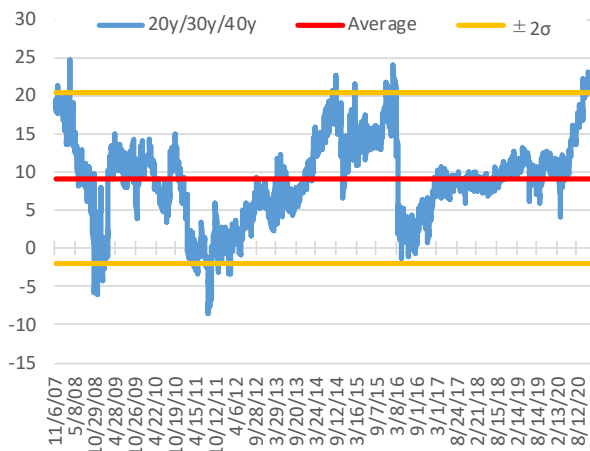
	FY2020 initial			FY2020 after 2nd&3rd s/b				FY2021 initial					Increase/decrease acceptable for primary dealers and investors discussed on Nov. 26
	per time	# of auctions per year	total <a>	per time	# of auctions per year	total 	-<a>	per time	# of auctions per year	total <c>	<c>-<a>	<c>-	
40Y JGBs	0.5	x 6	= 3.0	0.5	x 6	= 3.0	-	0.6	x 6	= 3.6	0.6	0.6	Increase with top priority
30Y JGBs	0.7	x 12	= 8.4	0.7 0.9	x 3 x 9	= 10.2	0.9	0.9	x 12	= 10.8	2.4	0.6	Unch or Decrease
20Y JGBs	0.9	x 12	= 10.8	0.9 1.2	x 3 x 9	= 13.5	1.8	1.2	x 12	= 14.4	3.6	0.9	Increase
10Y JGBs	2.1	x 12	= 25.2	2.1 2.6	x 3 x 9	= 29.7	2.7	2.6	x 12	= 31.2	6.0	1.5	Increase and also decrease
5Y JGBs	1.9	x 12	= 22.8	1.9 2.5	x 3 x 9	= 28.2	3.6	2.5	x 12	= 30.0	7.2	1.8	Increase and also decrease
2Y JGBs	2.0	x 12	= 24.0	2.0 3.0	x 3 x 9	= 33.0	5.4	3.0	x 12	= 36.0	12.0	3.0	Increase and also decrease
1Y TBs	1.8	x 12	= 21.6	1.8 3.5	x 3 x 9	= 36.9	9.9	3.5	x 12	= 42.0	20.4	5.1	Decrease
6M TBs	-					= 45.6	35.6			= 41.2	41.2	▲ 4.4	Decrease
10Y JGBIs	0.4	x 4	= 1.6	0.2	x 4	= 0.8	▲ 0.4	0.2	x 4	= 0.8	▲ 0.8	-	-
AEL			= 11.4			= 11.4	-			= 11.4	-	-	Decrease in 1-5Y zone
TOTAL			128.8			212.3	59.5			221.4	92.6	9.1	

Source: Ministry of Finance (MOF), compiled by Daiwa Securities.

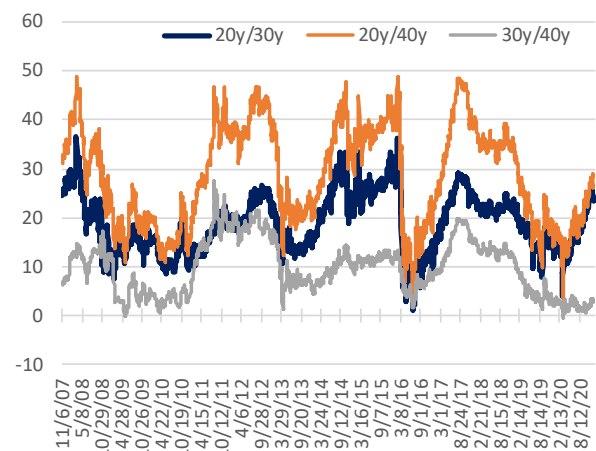
For other items, the coefficient for non-price competitive auctions II is 5.5%, about the same as it was after the third supplementary budget but down from the 7% of the initial FY2020 budget. The amount of front-loaded JGBs in FY2020 will be drawn down significantly, leaving the annual adjustment in FY2021 at only Y98.6 billion. The issuance limit in FY2021 on FY2022 front-loaded JGBs will be Y20 trillion. The amount of issuance sold to individual investors, which totaled about Y2.2 trillion as of December 2020, will be Y4.1 trillion, about Y900 billion higher than after the second and third supplementary budgets.

Expecting the 40-year JGB issuance increase to correct excessive distortions in the 20y/30y/40y curve

Expectations have been growing recently for widespread COVID-19 vaccinations. There is a possibility that FY21 will be the year that the post-COVID reality becomes clear. Uncertainties abound, including over the Tokyo Olympics (if it is cancelled, it will expand government spending) and the dissolution of the Diet and general election (which will be one of factors to increase government spending). Although not on the scale of FY2020, multiple supplementary budgets may be required in FY2021 as well. Partly owing to the small amount of front-loaded issuance (in FY2020 of refunding bonds in FY2021), there could easily be upward pressure on calendar-based market issuance. By maturity, issuance of 40-year JGBs will be increased in response to strong demand from the market. We recommend pursuing an investment strategy that reflects the possibility that the increased issuance of 40-year JGBs will correct the excessive distortions in the 20y/30y/40y curve.

Appendix 1: JGB 20y/30y/40y Butterfly Spread (bp)


Note: On-the-run compound yield basis
 Source: Daiwa Securities.

Appendix 2: JGB 20y/30y, 20y/40y and 30y/40y Spreads (bp)


Note: On-the-run compound yield basis
 Source: Daiwa Securities.

Appendix 3: 20y/40y/40y Butterfly Position Sensitivity

Change (bp)			Total Return (%)
20y	30y	40y	
0	0	0	0.1
4.5	4.5	4.5	0.0
-5	0	5	1.7
0	0	5	3.4
-5	0	0	-1.6
-5	5	5	-3.4
-5	-5	-5	0.2

Note: Based on change from JL174, JX68 and JU13 closes on Dec. 14; Total return calculated on 3-moth horizon with cash-and-duration neutral weights)
 Source: Daiwa Securities

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[Standard & Poor's]

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February 2020

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- 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.
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- 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), Nippon Healthcare Investment Corporation (3308), Japan Rental Housing Investments (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).

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