

Daiwa's View

Things to watch for in 2021: Part 3

- Outlook of chart (10-year US yield: triangle formation)

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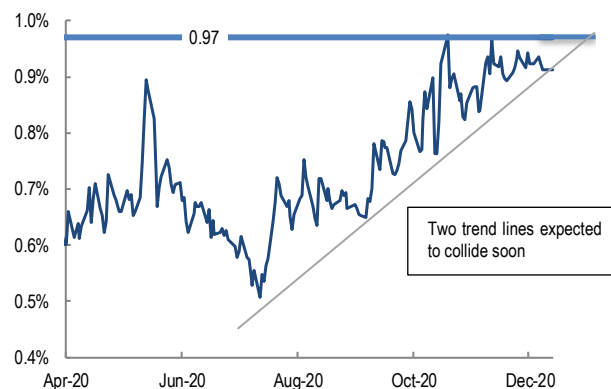
Outlook of chart (10-year US yield: triangle formation)

Things to watch for in 2021: Part 3

Last night, the 10-year US yield again rose to around 0.96%, while (1) we found that last month's headline ISM manufacturing index jumped to 60.7, which implied a rapid economic expansion, and (2) the market was strongly aware of expansion of the Democratic Party in Georgia's Senate runoff elections.

However, 0.95-1.0% is a familiar level as an upper limit of the range thus far. In addition, at least as of last night, an upside breakout did not occur in the chart of the 10-year US yield, which is forming a triangle (see [our 28 Dec 2020 report](#)). Looking at the breakdown, the 5-year yield is 0.37%, the 5-year forward 5-year yield is 1.59%, the 10-year forward 10-year yield (tends to reflect neutral interest rate) is 2.12%, and the 20-year forward 10-year yield is 2.27%. As each part is largely balanced with the guidance or fundamentals, the figures seem reasonable in comparison with [our forecasts](#). The Fed is unlikely to see the levels as a particular problem.

US Long-term Yield



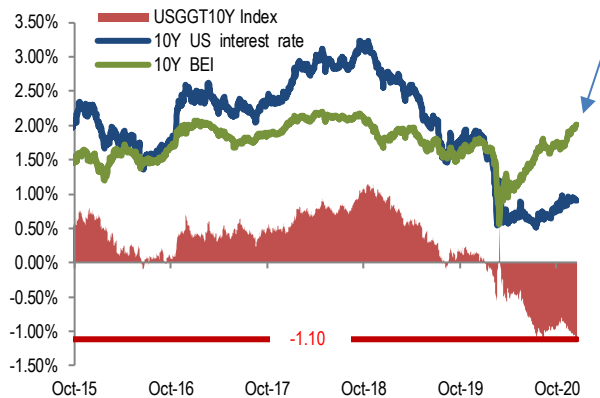
Source: Bloomberg; compiled by Daiwa Securities.

US Yield Forecasts for 2021 (% , as of 23 Dec 2020)

UST	5Y	5Y5Y	10Y	UST	10Y	10Y10Y	20Y	20Y10Y	30Y
06-Jan-21	0.37	1.59	0.95	06-Jan-21	0.95	<u>2.12</u>	1.49	<u>2.27</u>	1.70
Main scenario at end-2021	0.50	1.65	1.06	Main scenario at end-2021	1.06	2.10	1.55	2.25	1.74
Upper limit scenario	0.70	1.90	1.28	Upper limit scenario	1.28	2.35	1.78	2.50	1.98
Lower limit scenario	0.20	1.00	0.58	Lower limit scenario	0.58	1.85	1.18	2.00	1.41

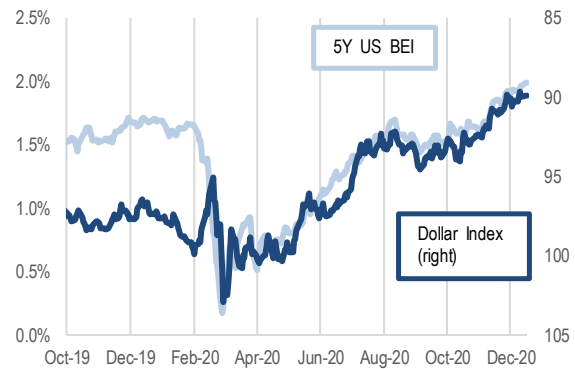
Source: Bloomberg; compiled by Daiwa Securities.

10Y US Interest Rate (nominal, real, BEI)



Source: Bloomberg; compiled by Daiwa Securities.

5Y US BEI, Dollar Index (DXY)



Source: Bloomberg; compiled by Daiwa Securities.

What is showing a kind of surprising move is the “real interest rate,” rather than the nominal interest rate. Driven by the real interest rate, which declined to -1.1% , the 10-year US breakeven inflation rate (BEI) exceeded 2% , and it is continuing to rise (left-hand chart above).

The BEI is data based on CPI. As there has been a 0.2-0.3-point difference on average between the Fed’s most focused core PCE and core CPI, we should not necessarily overreact to the “ 2% ” level of the BEI. However, it is safe to say that the move is striking. One characteristic in the yield uptrend stage in Aug-Oct 2020 was that the BEI rose ahead of the nominal interest rate and then the latter followed suit slightly later. In forecasting the outlook of the above-mentioned chart as well, inflation is likely to be the most important point.

Under the circumstances, pressure on a stronger yen/weaker dollar is increasing in the international financial market. Last night, the yen again strengthened to around the mid-102 level against the dollar. Such a move in the international financial market appears to be increasing the cost for the BOJ [to raise JPY yield levels \(in real terms\)](#) at the upcoming March Monetary Policy Meeting by focusing only on the side effects at financial institutions.

That said, it is premature to jump to a conclusion. The new Biden administration has yet to start, and there are many points to be confirmed regarding future developments (incl. vaccines, pandemic). In the sense that such a situation should be ascertained as well, the BOJ’s setting of a time frame for the announcement of the “assessment meeting” result in March, instead of January, is appropriate, in our view.

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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]

The Name of the Credit Rating Agencies Group, etc

The name of the Credit Rating Agencies group: Moody's Investors Service ("MIS")

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[Fitch]

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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).

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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 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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