

Daiwa's View

The Meeting of JGB Market Special Participants and Meeting of JGB Investors: The latest measures are appropriate, but...

- The proposals, such as increasing short- to medium-term JGB issuance and introducing semi-annual reviews, are welcomed as appropriate and proactive responses to market changes
- However, if the market were to develop the habit of demanding public intervention from MOF when market intervention by BOJ has begun to decrease, that would be like putting the cart before the horse
- To avoid dependence on the public sector, decisions about reductions to JGB issuance must proceed by carefully distinguishing between structural changes and temporary factors during transitional periods

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Materials were posted on the MOF's website and multiple media reports quoted remarks from senior officials in relation to yesterday's Meeting of JGB Market Special Participants (primary dealers) and Meeting of JGB Investors. Broadly speaking, the following three points sum up the discussions that took place. (For details on these meetings yesterday, please refer to [a separate report by our Strategist Kazuya Sato.](#))

- FY25 issuance plan: Authorities proposed increases to Treasury Discount Bills (TDBs), 2-year JGBs, and 5-year JGBs.
- FY26 issuance plan: Participants held the view that superlong JGBs should be decreased and long-, medium-, and short-term JGBs increased.
- New proposal: A proposal was made to review the issuance plan on a semi-annual basis starting next fiscal year.

From the author's perspective, taking a course of action towards increasing short- and medium-term JGB issuance and reducing superlong JGB issuance to reflect structural demand changes seems reasonable. Furthermore, considering the mid-year revisions made this year following the poor results of 20-year JGB auctions, and the BOJ's "interim assessment" scheduled for June 2026, a semi-annual review would also be a welcome proactive measure in line with market changes. That said, I think there are several points that will warrant attention as these adjustments are made going forward.

Are they really structural changes?

In general terms, making adjustments to the issuance of JGBs in response to structural changes in demand is desirable for correcting supply/demand imbalances and enabling the market to send proper price signals. However, in reality, distinguishing between "structural changes" and "temporary changes" is not as easy as it sounds. We have obviously seen two clear trends since last fiscal year: (1) a decrease in demand due to the BOJ's exit strategy and the start of Quantitative Tightening (QT) and (2) a decline in demand from life and non-life insurers. A major underlying factor for point (2) in particular is that, as the response to new regulations has run its course, demand for duration matching of previously accumulated stock (JGB holdings) has subsided. Given these circumstances, reducing issuance in the superlong sector can be seen as a structural adjustment that will enhance market discipline, ensure smooth issuance, and contribute to curbing medium- to long-term funding costs. There is likely broad consensus that the things being discussed and considered at the Meeting of JGB Market Special Participants and the Meeting of JGB Investors are moving in the right direction.

Systemic fatigue / Transitional periods

However, as pointed out, for example, in the latest report "[1H FY25 Earnings Results of Major Life Insurers \(3\)](#)" by our Chief Credit Strategist Yuki Sakamoto, one of the possible factors behind the sluggish demand for superlong JGBs from life insurers since the sharp rise in superlong yields starting in April 2025 is that the "Standard Policy Reserve system" may be hindering the virtuous cycle that should naturally occur in "a world with positive interest rates."

While the standard interest rate is seen as having played a major role in ensuring the soundness of insurers during the past 25 years of falling interest rates, today, with Japan making a full-scale transition to a world with positive interest rates, the possibility has now emerged that it has transformed into a factor that constrains the "virtuous cycle" of setting policy rates commensurate with current interest rates and delivering the benefits of rising rates to policyholders. The crucial point here is that, under the current circumstances in which systems like this standard policy reserve framework, which were designed based on a premise of 25 years of declining interest rates, are becoming bottlenecks, there is a risk that "structural demand" could be underestimated or overestimated.

Market discipline / Signals

My concern is that the market will develop an excessively strong, simplistic association (or expectation) that rising superlong yields will equate to a reduction in the issuance of JGBs. Recently, every time yields have risen, it has been pointed out that buybacks or reductions in JGB issuance must be made. The current course of action being taken in response to the structural decrease in demand for superlong JGBs is, of course, reasonable. However, a signal of caution from market participants was likely part of what accounted for the rise in long-term and superlong yields that occurred in conjunction with the expansion in the supplementary budget that took place under the Takaichi administration. If the market's response to these signals were to become entrenched, like a Pavlovian response, to expect a rise in yields to prompt requests for reductions in JGB issuance, market discipline would become distorted, possibly causing the side effect of political populism being encouraged in the end.

When making decisions about reducing JGB issuance, it is essential to ensure that the market can continue to send accurate price signals. This means implementing appropriate reductions in response to declines in structural demand, but avoiding undermining market signals by making permanent reductions to cope with temporary or transitional factors. If, just as the BOJ's large-scale market interventions are finally beginning to recede, market participants are developing a tendency to seek public intervention from the MOF, this should be described as a dependency on the public sector, and reacting in this way would be like putting the cart before the horse.

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