Daiwa Securities

Daiwa's View

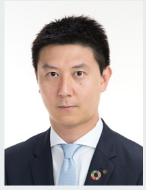
BOJ intervention (unscheduled JGB purchases) likelihood, consumption tax cut impact

- JGB yields surged on 20 Jan, positions bought back on 21 Jan
- Possibility of unscheduled JGB purchases by BOJ should be viewed with caution
- Impact of consumption tax cuts on 10yr JGB yield

FICC Research Dept.

Shun Otani
81-3-5555-8764
shun.otani@daiwa.co.jp

Daiwa Securities Co. Ltd.



Super-long JGB yields surged on 20 Jan following Takaichi's press conference

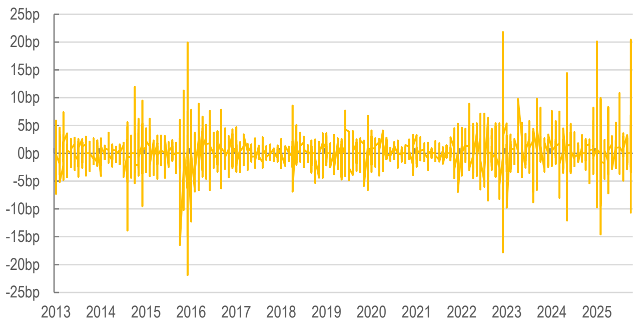
On 20 January, the on-the-run 30-year JGB (JX89) yield rose sharply by 26.5bp on a simple yield basis and 20.3bp on a compound yield basis. At the end of last week, it was reported that Prime Minister Sanae Takaichi plans to add to her campaign pledges a consumption tax cut for food, lasting a period of two years. Also, at her 19 January press conference[1], Takaichi emphasized her "strong desire" for such a consumption tax cut and added that the tax cut would not rely on special deficit-financing JGBs. Still, the failure to specify funding sources for the tax cut sparked fiscal concerns. On 21 January, US Treasury Secretary Scott Bessent said, "I am sure that they (Japan) will begin saying the things that will calm the market down." Meanwhile, Finance Minister Satsuki Katayama said, "We have been taking steps to stabilize the market and can absolutely promise to continue doing so." As a result, in addition to expectations for policy measures, the BOJ's scheduled JGB purchasing operation yielded solid results, triggering buybacks. The on-the-run 30-year JGB yield closed lower, falling by 16.5bp on a simple yield basis and 12.6bp on a compound yield basis.

20 Jan price movements, possibility of unscheduled JGB purchasing operations

When comparing the 20 January price movements (compound yield basis) with the past, as Bessent pointed out the "six standard deviation" move, the standard deviation of the daily compound yield change for 30-year government bonds (≈ volatility/past 250 trading days) was 3.68bp, meaning the move was equivalent to 5.5 standard deviations (= 20.3 ÷ 3.68). That said, looking back on the past, there was also a rise of 20bp on 8 April 2025, when the market was hit by Trump's tariff shock. At that time as well, there were no unscheduled measures such as the BOJ increasing its JGB purchases. Also, as for the 10-year JGB, the yield rose 8.5bp on 20 January. Since December 2022, when the course was set toward monetary policy normalization, there have been six cases in which this yield rose by more than 8.5bp. Since the normalization of monetary policy, with control of short-term interest rates becoming the primary policy variable, the rationale for conducting unscheduled purchases of JGBs likely lies in the fact that the formation of the yield curve also influences monetary policy (≈ short-term interest rates). In that case, the degree of impact is long-term > super-long-term. As for the long- and super-long sector price movements on 20 January, the application of an "exceptional case" warranting unscheduled JGB purchases is a delicate judgment call. The feasibility of BOJ market intervention (unscheduled JGB purchases) must be carefully evaluated.

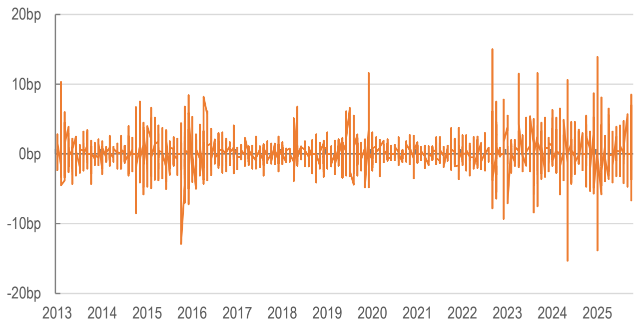
[1] Kento Minami and Kenji Yamamoto (20 Jan 2026). *Daiwa's View: PM Takaichi's press conference: Glimpsing future through midwinter election*.

Chart 1: Changes in 30yr JGB Yield (d/d, compound yield)



Source: Bloomberg; compiled by Daiwa.

Chart 2: Changes in 10yr JGB Yield (d/d, compound yield)



Source: Bloomberg; compiled by Daiwa.

◆ **BOJ Gov Ueda's 13 Nov 2025 Testimony Before Upper House Budget Committee**

· We believe that the long-term yield is fundamentally determined by the market. To elaborate further, the long-term yield is thought to be formed by adding what is often called the "term premium," which reflects expectations for short-term interest rates going forward and the various risks associated with holding government bonds. We anticipate that it will fluctuate based on market views regarding future economic and price conditions, monetary and fiscal policies, and any changes in overseas government bond yields. Furthermore, in exceptional cases where long-term yields rise sharply in a manner diverging from normal market movements, **we would flexibly implement measures such as increasing JGB purchases, conducting fixed-rate purchase operations, and implementing funds-supplying operations against pooled collateral, from the perspective of promoting stable market formation**. This stance has remained unchanged, and we intend to closely monitor market trends going forward."

Impact of consumption tax cut on long-term yield

The elimination of consumption tax on food is projected to result in a tax revenue loss of roughly Y5.0tn each year. If the ruling parties implement this tax cut for only two years as promised and no alternative funding source exists, that would add roughly Y10tn to government debt. This is equivalent to 1.6% of current nominal GDP (= Y10tn ÷ Y642tn). In our 5 November 2025 *Daiwa's View*[2], we estimated the impact of the government debt-to-nominal GDP ratio on the JGB term premium. Our findings indicated that a 1% deterioration in this government debt-to-GDP ratio would push up yields by approximately 1bp. These results (1% increase in government debt-to-nominal GDP ratio caused long-term yield to rise 1.2bp) are consistent with those presented in a paper by Professor Keigo Kameda of Kwansei Gakuin University[3], a member of MOF's "Study Group on Government Debt Management," who hosted a seminar in August 2025. Accordingly, the impact of a two-year 0% consumption tax for food on the long-term yield would be limited to 1.6bp (=1.6% × 1bp).

Meanwhile, there is also a view that the impact of the single-year fiscal balance (flow) is significant. According to Kameda's paper mentioned earlier, a 1% increase in the fiscal deficit-to-GDP ratio (flow) raises the long-term yield by 26 to 34bp. So, a single-year deficit of Y5tn, equivalent to 0.8% vs nominal GDP, would push up the long-term yield by 21 to 27bp. This analysis is worth noting. Kameda pointed out during his seminar that the analysis period covered from 1981 to FY07 was outdated and an analysis extended to 2023 indicated that since the large-scale easing in 2013, the primary balance has had a smaller impact on yields. That said, this impact has again grown significantly since 2020. Certainly, Kameda's results (2014) could be somewhat exaggerated. Still, during the monetary policy normalization phase, fiscal policy's impulse on the long-term yield tends to be amplified and unexpected changes in flow can have a significant effect.

---

[2] Shun Otani (5 Nov 2025). *Daiwa's View: Impact of fiscal policy and QT on JGB term premium*.
[3] Keigo Kameda (2014). Budget deficits, government debt, and long-term interest rates in Japan. *Journal of the Japanese and International Economies*.

The most important point is that the 20 January market reaction intensified because it is politically difficult to again raise the consumption tax once it has been lowered. As such, the market is pricing in the risk that the proposed consumption tax cut for food will become permanent. The implementation of a tax cut generally requires about one fiscal year of preparation. However, if the tax cut is implemented starting in FY27, extending the tax cut would likely become a political issue in the Upper House election scheduled for the summer of 2028. Also, from a long-term perspective, the primary cause behind Japan's fiscal deterioration is the expansion of social security expenditures driven by the population decline (declining birthrate and aging population). Japan's consumption tax was first introduced in 1989 as a funding source to address this issue. Its rate has been raised incrementally despite political difficulties. These tax rates have never been lowered. The ruling parties' pledge to reduce consumption taxes marked a major turning point for the market in terms of fiscal sustainability.

Given that both the ruling parties and the main opposition parties are pledging a consumption tax cut on food items in the runup to the Lower House election (vote casting/counting on 8 Feb), it is highly likely that the tax cut will be implemented. That said, if the tax cut is limited to two years as promised by the ruling parties, their impact on government debt-to-GDP ratio will not necessarily be significant. If the economy can enter a growth track, offsetting such loss through increased GDP could be entirely possible. This election involves many uncertainties such as (1) Takaichi's popularity but poor support for her Liberal Democratic Party (LDP), (2) shift from an LDP-Komeito coalition to an LDP-Japan Innovation Party coalition, and (3) formation of a new political party consisting of former Constitutional Democratic Party of Japan and Komeito. High market volatility is expected during the election period. Subsequent developments will depend on the election results. However, should the Takaichi administration emerge victorious, demonstrating the effectiveness of the "two-year limit" to the markets would be the first step toward reducing the heightened fiscal premium.

IMPORTANT DISCLOSURES

This report is provided as a reference for making investment decisions and is not intended to be a solicitation for investment. Investment decisions should be made at your own discretion and risk. Content herein is based on information available at the time the report was prepared and may be amended or otherwise changed in the future without notice. We make no representations as to the accuracy or completeness. Daiwa Securities Co. Ltd. retains all rights related to the content of this report, which may not be redistributed or otherwise transmitted without prior consent.

Ratings
Issues are rated 1, 2, 3, 4, or 5 as follows:
1: Outperform TOPIX/benchmark index by more than 15% over the next 12 months.
2: Outperform TOPIX/benchmark index by 5-15% over the next 12 months.
3: Out/underperform TOPIX/benchmark index by less than 5% over the next 12 months.
4: Underperform TOPIX/benchmark index by 5-15% over the next 12 months.
5: Underperform TOPIX/benchmark index by more than 15% over the next 12 months.

Benchmark index: TOPIX for Japan, S&P 500 for US, STOXX Europe 600 for Europe, HSI for Hong Kong, STI for Singapore, KOSPI for Korea, TWII for Taiwan, and S&P/ASX 200 for Australia.

Target Prices
Daiwa Securities Co. Ltd. sets target prices based on its analysts' earnings estimates for subject companies. Risks to target prices include, but are not limited to, unexpected significant changes in subject companies' earnings trends and the macroeconomic environment.

Disclosures related to Daiwa Securities
Please refer to https://drp.daiwa.co.jp/rp-daiwa/direct/reportDisclaimer/e_disclaimer.pdf for information on conflicts of interest for Daiwa Securities, securities held by Daiwa Securities, companies for which Daiwa Securities or foreign affiliates of Daiwa Securities Group have acted as a lead underwriter, and other disclosures concerning individual companies. If you need more information on this matter, please contact the Research Production Department of Daiwa Securities.

Explanatory Document of Unregistered Credit Ratings
This report may use credit ratings assigned by rating agencies that are not registered with Japan's Financial Services Agency pursuant to Article 66, Paragraph 27 of the Financial Instruments and Exchange Act. Please review the relevant disclaimer regarding credit ratings issued by such agencies at: https://drp.daiwa.co.jp/rp-daiwa/direct/reportDisclaimer/credit_ratings.pdf. If you need more information on this matter, please contact the Research Production Department of Daiwa Securities.

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
Memberships: Japan Securities Dealers Association, The Financial Futures Association of Japan, Japan Investment Advisers Association, Type II Financial Instruments Firms Association, Japan Security Token Offering Association