Minutes of the Meeting of JGB Investors
(81st Round)

1. Date: Tuesday, November 26, 2019 (1:30 p.m. to 2:50 p.m.)
2. Place: Special Conference Room 3, Ministry of Finance
3. Gist of Proceedings

1. Latest JGB market situation and outlook for future investments

2. JGB Issuance Plan for FY2020

▶ The Financial Bureau gave the following explanation about the JGB Issuance Plan for FY2020.

(Introduction of the presentation by the Financial Bureau at the Advisory Council on Government Debt Management October 25, 2019)

・Issuance of JGBs based on market demand is crucial for stable and smooth issuance and minimization of funding cost in the medium to long terms. Since projected issuance amounts of JGBs remain at a high level far beyond 100 trillion yen, secure issuance based on assessment of demand trend over the medium to long term, rather than opportunistic issuance, leads to cost minimization and stable and smooth issuance.

・The issuance amount of JGBs has been declining, which has fallen below 150 trillion yen recently. This is because the attempt to extend the weighted average maturity has led to a decline in the issuance amount of Refunding-Bonds, despite an increase in the outstanding amount of JGBs. The net issuance, which represents the amount of issuance minus the amount of redemption, of super long-term bonds was higher than 20 trillion yen while that of medium- and long-term bonds has turned negative, resulting in the extension of the weighted average maturity on a stock basis. The weighted average maturity of JGBs has become the longest internationally except for the United Kingdom.

・The issuance amount of Refunding Bonds is projected to remain almost flat over the next 10 years. While projected net issuance in the super long-term zone stays positive, that in other zones remains flat or negative, which implies a continuous extension of the weighted average maturity on a stock basis for a while.

・Although the JGBs holdings by banks have been trending downward since the introduction of the Quantitative and Qualitative Monetary Easing policy by the BOJ, the pace of decline has recently been moderating due to demand for collateral use and other purposes. On the other hand, as the amount of their current account deposits at the BOJ has continued to increase, they have a potential for investments in JGBs.

・The outstanding amount of JGB holdings by life insurance companies showed an upward trend between 2008 and 2012, with their holdings of bonds in the super long-term zone also increasing. However, the amount has remained almost flat since 2013 while purchases of foreign bonds have been increasing instead. The reason behind this is the risk that duration matching of assets and liabilities under the low interest rates environment would fix losses. It suggests that their investment trend may change in the future depending on the movements of interest rates.

・It has been pointed out that there is the possibility that the changes in the population demographics in the future may lead to decrease in insurance premium revenues or development of needs for new insurance plans. Since the change in needs for insurance plans would have an influence on the investment style of life insurance companies, it is necessary to keep a close watch on the change in the composition of their liabilities from both sides of amount and quality.

・Accompanied by the discussions on the international regulations on insurance companies which will be newly introduced in 2025, an advisory panel was established at the Financial Services Agency in June 2019 and discussions on domestic regulation have started as well. Depending on the specifics of the regulations and the timing of introduction, the demand for JGBs is expected to change before or after the preparation for the regulatory compliance. Close observation on these developments are important for considering the JGB issuance plans in the future.

・Looking at a comparison of investors' funding sources and the duration between Japan and the United States, the share of banking sector is higher in Japan, which results in the shorter duration of funding sources. Close observation on the trend in entire funding sources is also necessary for considering the JGB issuance plans from the medium to long term perspective in the future.

・The transaction volume and turn-over ratio for JGBs have improved slightly since the latter half of last year. The improvement of the bond market functionality in Japan has been stalling due to the recent interest rate situation, according to the bond market survey conducted by the BOJ. On the other hand, the GC-SC spread and the amounts of bids accepted for Securities Lending Facility have stayed stable. It suggests that the supply-demand imbalance of specific issues was largely improved.

・Liquidity Enhancement Auctions have been conducted for the purpose of improving the supply-demand imbalance of specific issues. The issuance amount for Liquidity Enhancement Auction increased after the global financial crisis and when the BOJ introduced the Quantitative and Qualitative Easing policy. However, the total amount of JGBs issuance has turned to decrease. Also, the amount of Outright Purchases of JGBs by the BOJ has declined recently. Although reduction in the amount of on-the-run issues was mainly discussed when considering the issuance amount of JGBs thus far, Liquidity Enhancement Auction should be included into the discussions as well under these situations.

・In the estimate which was made in FY2013, the issuance amount of Refunding Bonds projected to increase by around 30 trillion yen over the following 10 years. At that time, it was intended to extend the weighted average maturity on a flow basis from the viewpoint of curbing the growth in the amount of Refunding Bonds. As a result, the latest estimates projects a roughly constant transition in the issuance amount of Refunding Bonds, which means the advantage of extending the weighted average maturity has been diminished. In addition, the discussion at the Advisory Council on Government Debt Management held three years ago included the need for a revision in such policy course of extending the weighted average maturity on a flow basis and a formulation of the JGB issuance plan in a flexible manner in light of investors' demand in the medium- to long-term.

・The outstanding amount of front-loading Refunding Bonds increased in the last fiscal year even though the initial plans had intended a certain amount of reduction for the past two years. The amount may increase in the current fiscal year as well, depending on the market circumstances because the financing need was reduced by 1.5 trillion yen in June this year and the amount of excess revenue from calendar-based market issuance is expected to surpass the amount estimated in the initial plan by one trillion yen or more under the current negative interest rate environment.

・Some measures were employed for curbing the issuance of front-loading Refunding Bonds recently. For example, the amount of issuance from non-price competitive auction II and excess revenues from calendar-based market issuance listed on the issuance plan have been increased in light of the results at the time of formulating the initial plan. However, introduction of further measures needs to be considered. For example, revising issuance plans in the middle of the fiscal year in accordance with the gap between the plan and the results, decreasing the maximum amount of bidding for the non-price competitive auction II from 15% to 10% and lowering the floor of the coupon rate on JGBs from 0.1% to 0.001% are under consideration. Examples of such revisions of issuance plans during the fiscal year can be seen in other major countries. Germany, the United Kingdom and France formulate government bonds issuance plans before each fiscal year and revise the plans during the fiscal year.

(Introduction of the discussion at the Advisory Council on Government Debt Management October 25, 2019)

・Some members stated that effective use of super long-term zone, active trading by foreign investors in short- to medium-term zone and employment of innovative technology are important for maintaining the market's functionality. On the other hand, others pointed out macro-prudential issues about investing in super long-term zone and the challenge that the super long-term zone lacks a hedging facility such as future trading.

・Some members noted the need for considering the appropriate target for weighted average maturity, taking into account that issuance of super long-term bonds leads to steepening of the yield curve. Others stated that the possibility that functionality of the market may remain existing only in the longer-term zone in the future should be considered while the lengthening of weighted average maturity is not necessary at this point.

・Some members asserted that it was necessary to optimize the issuance volume of front-loading Refunding Bonds in the medium- to long-term. Others stated that the front-loading Refunding Bonds should be used for leveling off the amount of JGB issuance, considering that there will be ups and downs in the estimated issuance amount of Refunding Bonds in the future.

▶Summarized below are the views and opinions expressed by the attendees:

・Although the yield curve has recently recovered from the excessive flattening that was observed globally until the beginning of autumn, no significant change is expected to occur in the global accommodative monetary situation. Also, it seems that investors are shifting their funds to domestic bonds from foreign bonds. While the decline in the interest rates was led by the interest rates in the United States, remarks made by the BOJ governor Kuroda had an influence on the interest rates when they were rising.

The JGB Issuance Plan will affect the global interest rate because it seems that foreign investors are making some investments in the 30- and 40-Year Bonds. The issuance amount of 30- and 40-Year Bonds should not be reduced substantially to avoid affecting the global interest rate.

・While the interest rates had continued to decline until the summer, the trend has changed since the autumn. In particular, the BOJ’s response to the low level of the super long-term interest rates and the reduction of the Outright Purchases of JGBs have made it slightly easier for interest rates to rise. However, the powerful demand for bonds with positive interest rates caused the present interest rate level to remain low, which has not recovered to the level in April and May in the current fiscal year. For example, the movement of interest rates on the 20-, 30- and 40-Year Bonds is not catching up with the rise of interest rates on the bonds with remaining maturities of 10 years or less. The interest rates in the super long-term zone have not recovered to the level of the yield curve observed at the beginning of the fiscal year, which shows the strong demand for bonds with longer maturities.

Although it might be difficult to increase the total amount of market issuance, it is desirable to increase the amount of issuance in the super long-term zone as much as possible on the JGB Issuance Plan for the next fiscal year, considering the current market environment. In particular, an increase in the issuance amount of the 40-Year Bond, which has the longest maturity, will bring a positive impact because there is a significant demand for bonds with long duration.

・The JGB interest rates became more susceptible to foreign interest rates than before because an influence of players with low-interest liabilities denominated in US dollar on the JGBs prices has become larger, which coincided with the decline in JGBs interest rates deeper below zero. The market situation is expected to stabilize to a certain degree, unless the policy interest rate is changed, because the recent yield curve of U.S. Treasury has been reasonable, compared with when the pressure for flattening of the yield curve was strong as a result of the yield curve inversion.

Banks that have demand for foreign currencies will continue to hold some JGBs as collateral. In addition, if the shape of the yield curve is favorable for investments, there will be demand in zones with positive interest rates. Therefore, we are considering making investments in JGBs in light of the regulation and other factors though it is difficult to hold them in a large amount.

As explained by the Financial Bureau, purchases of the 5-year Bond by foreign investors, including foreign central banks, help Japanese banks to procure foreign currencies. Yen-denominated investments made by foreign investors who hold US dollar and Japanese investors’ procurement of US dollar by yen are two sides of the same coin. As JGB purchases by foreign investors are helpful for the procurement, a tightening of the supply-demand balance should be avoided in zones for which foreign investors, including foreign central banks, have demand.

・As the interest rates on bonds with the remaining maturities of 10 years or shorter have stayed below zero, demand is concentrating on the super long-term zone due to hunting for yields. Although some improvement has been made due to the reduction of the Outright Purchase of JGBs by the BOJ, flattening of the yield curve have been continued because the interest rates and liquidity in that zone are low.

On the other hand, along with the discussion of the introduction of economic value-based solvency regime, life insurance companies have continued to have strong investment needs for super long-term bonds for internal management and ALM. Under the recent low interest rate situation, they have been diversifying their investments, including currency-hedged foreign bonds and credit assets, in addition to JGBs. However, such investment strategy might change when the interest rates rise.

It is expected that the Financial Bureau would reduce the total amount of issuance on the JGB Issuance Plan for the next fiscal year to decrease the issuance of front-loading Refunding Bonds. However, we request the Financial Bureau to maintain or increase the current issuance amount of super long-term bonds, including the 20-Year Bond. In particular, the issuance amount of the 40-Year Bond should be increased, as reported by the media, because the low liquidity of the 40-Year Bond can trigger a flattening of the whole yield curve.

While the issuance amount and its allocation among each zone will be adjusted based on market circumstances and opinions from investors on a quarterly basis, reduction in the issuance amount for the Liquidity Enhancement Auction should be considered if necessary, taking into account that the BOJ has reduced the amount the Outright Purchase. In particular, there is a room for reduction in the remaining maturities of 5-15.5 years zone because the supply-demand situation for the cheapest-to-deliver issue has been eased by the BOJ's Securities Lending Facilities. On the other hand, it is desirable to maintain the current amount of issuance for the Liquidity Enhancement Auction in the remaining maturities of 15.5-39 years zone for the same reason as super-long bonds.

At the Meeting of JGB Market Special Participants held yesterday, some members suggested that there is a room for reduction in the issuance of the 10-Year Bond. However, there would be a certain demand if interest rates turn positive in this zone. Also, the balance with the issuance in this zone needs to be considered if the issuance amount for the Liquidity Enhancement Auction is going to be reduced. Therefore, if further reduction is necessary, the 2-Year and 5-Year Bonds should be included to the options for reduction.

・There has not been a big change in our investment policy. While we are paying careful attention to credit risks because financial leverage of U.S. companies has become higher, we will continue internationally diversified investments. In this situation, we will continue to invest in JGBs, mainly in zones with positive interest rates, in order to control the duration of deposits. However, our prospect is that our balance of JGBs will decrease moderately.

As we are not purchasing JGBs in zones with negative interest rates for such reasons, we request the Financial Bureau to maintain the current issuance amount in the remaining maturities of 20 years or longer zone where interest rates are positive. In particular, it is desirable to maintain the issuance amount of 20-Year Bond and the Liquidity Enhancement Auction in the remaining maturities of 15.5-39 years zone, which we can invest in from the viewpoint of ALM. It is difficult to purchase the necessary amount of the 20-Year Bond through the auctions due to the low liquidity in the market, though a certain amount of transactions has been made. Therefore, we request a maintenance of the current issuance amount for the Liquidity Enhancement Auction to make sure that the purchase opportunity is provided twice every month or three times every two months.

・We have reduced our outstanding balance of JGBs, accompanied by their redemption. The ratio of JGBs to yen-denominated bond investments has fallen below 10%. However, we have recently started to invest in JGBs in the super long-term zone, including the 20-Year Bond, because of the continued negative interest rate situation. As investment in assets with negative yield is not allowed in our company’s policy, we are considering investing in zones with positive interest rates.

The issuance amount of the 5-Year Bond has a room for reduction because there is no irreplaceable demand for the bond. In addition, though an increase in the issuance amount of the 40-Year Bond was reported by the media, it is uncertain how much demand there is because the interest rate spread between the 30-Year Bond and the 40-Year Bond is tight, looking at the recent yield curve. When revising the JGB Issuance Plan, such revision should be made in accordance with the changes in the yield curve.

・From an investor’s perspective, demand is not strong for the zone with negative interest rates while there is a high demand for JGBs with the remaining maturities of 10-20 years. As in the explanation about the issuance amount provided by the Financial Bureau and the report about increase in the issuance amount of the 40-year Bond, it is desirable to increase the issuance amount for the super long-term zone, particularly in the remaining maturities of longer than 20 years zone.

On the other hand, it is acceptable to reduce the issuance amount in the zone with negative interest rates, particularly the 5-Year Bond. While demand for the 10-Year Bond might arise, reflecting the interest rate movement, and there is a stable demand for the 2-Year Bond for collateral use, the issuance amount can be reduced for the 5-Year Bond because the demand is scarce. Although maintenance of the issuance amount for the Liquidity Enhancement Auction is strongly desired for the market circumstances, a reduction in the remaining maturities of 5-15.5 years zone would have the smallest impact on the market because a short squeeze has not occurred frequently due to the various measures taken by the BOJ.

・Interest rates on JGBs are unlikely to rise. Regarding the balance of payments in the insurance industry, which was explained by the Financial Bureau, we recognize the importance of providing insurance products in a well-balanced manner. It is needed to consider providing insurance products adapting growing longevity, including healthcare, nursing insurance, pension and death insurance. In designing insurance products, the assumed interest rate is important, which is set in advance based on the interest rates of JGBs. However, the low interest rates environments has kept the assumed interest rate low, which would influence insurance premium as well. Therefore, the difficult environment is expected to continue for providing insurance products for people.

Our basic policy for investment is to invest in the super long-term zone, corresponding to our liabilities with super long-term duration. As explained by the Financial Bureau, we are making investments in complying with economic value-based solvency regime. Therefore, we request the Financial Bureau to pay close attention to the super long-term zone in formulating the JGB Issuance Plan for the next fiscal year, in light of the need for holding assets with long duration corresponding to the liabilities.

・Since the Expansion of Quantitative and Qualitative Monetary Easing by the BOJ in October 2014, a shift from JGBs to yen-denominated foreign bonds occurred on a significant scale. This shift stopped in the past a half to one year, after which the amount of investments in JGBs is neither increasing nor decreasing.

The amount of our JGBs holding, which is 10 trillion yen currently, depends on the amount of issuance because our policy is based on the index investing. In accordance with inflows and withdrawals of clients' funds and portfolio adjustments, we constantly trade JGBs worth tens of billion yen in the super long-term zone with the remaining maturities of 20 years or longer and those worth hundreds of billion yen in the remaining maturities of 10 years or shorter on a weekly basis. If it is considered to increase the issuance amount under the JGB Issuance Plan for the next fiscal year, the 40-Year Bond is the desirable candidate. It can lead a steepening of the JGB yield curve so that JGBs become more attractive relative to foreign bonds, which is a favorable environment for new customers. On the other hand, it may be better to wait for one to two years before increasing the issuance amount of the 40-Year Bond from the point of its liquidity. In trading every week, there is still some uncertainty over the 30-Year and 40-Year Bond compared with the 20-Year Bond.

Initially, the Liquidity Enhancement Auction in the remaining maturities of 15.5-39 years zone was contributing to stabilizing the market by supplying issues for short covering. However, looking at the market movements, some speculative actions have been observed these days on the auction day.

Overly volatile movements are undesirable from the viewpoint of investing in the super long-term zone. The Liquidity Enhancement Auction in the remaining maturities of 15.5-39 years zone can be an option for the reduction in the issuance amount as a steep yield curve and low volatility attract investors.

・Although some improvement have been observed, the yield curve remain flat in the remaining maturities of 2-8 years zone. Also, issues with the remaining maturities of around 10 years zone have been undervalued. The reason behind this is that the reduction of the Outright Purchases of JGBs makes significant differences in the BOJ's share of JGBs holding for each issue. For example, the BOJ holds around 80% of the 10-Year Bond (351) and other issues with the remaining maturities up to 8.5 years despite the Liquidity Enhancement Auctions. On the other hand, the BOJ has only 20% of the on-the-run issue at the second re-opening and around 50% of the two preceding issues.

Looking only at the shape of the yield curve, it appears that there is no room for reduction in the issuance amount for the Liquidity Enhancement Auction in the remaining maturities of 5-15.5 years zone. In particular, the auction results show that there have been continuous solid demand for the issues with the remaining maturities of 6-7 years. The possibility of a short squeeze occurring cannot be denied when the issuance amount for the zone is reduced. Therefore, reducing the issuance amount for the Liquidity Enhancement Auction requires a prudent consideration.

In addition, there is a strong demand from investors for the JGBs with positive interest rates, including the 30-Year and 40-Year Bonds. Return from holding issues with the remaining maturities shorter than 10 years are not commensurate with the investment because holding them to the maturity results in losses. Even if they are used as collateral for funding, it yields negative interest under the recent situation. Therefore, reducing the issuance amounts of the 30-Year and 40-Year Bonds would be unacceptable for investors.

・While the JGB market situation had been unusual until this summer with a steep decline in the interest rates, such situation has been recovered and investment environment has become more favorable after the global decline in the interest rates of government bonds paused and the inverted yield curve returned to normal yield in many cases. There are profit opportunities in JGBs because the market function has started to work in the super long-term zone.

Although the stock market is pricing in an optimistic view, it is likely to take some more time before investment environment improve substantially given the low inflation rate. Under such circumstances, we will continue to invest in government bonds globally for interest income. Our investment will be targeted at bonds with a yield spread or positive interest rates.

Regarding the JGB Issuance Plan for the next fiscal year, we do not have demand for the 40-Year Bond. If the reduction of the issuance amount is necessary, the Liquidity Enhancement Auction in the remaining maturities of 5-15.5 years zone should be the option. The impact on the market may be relatively small because it corresponds to the reduction of the Outright Purchases of JGBs by the BOJ. Meanwhile, revising the JGB Issuance Plan during the fiscal year would be effective if the revision is announced in advance.

・Although the U.S.-China trade negotiation have had a significant impact, the U.S. monetary tightening was the most influential factor for the economic stagnation, slowing global economic growth and interest rate decline since last year. In addition to the U.S. monetary tightening, China was taking a tightening policy as well by reducing debt outstanding. However, the U.S. changed course toward monetary easing and China appears to be easing the debt reduction policy. Therefore, the trend of economic slowdown will come to a halt and start recovering. The recovery would remain weak as economic uncertainties continue to be strong due to the uncertain outlook on the future course of the U.S.-China trade negotiation. Japanese current monetary easing is expected to continue for a long period of time as well though the BOJ may refrain from additional easing.

In the short term, interest rates are likely to rise compared with the situation until now as the U.S.-China trade negotiation seems to be proceeding to reach an agreement. However, in the medium to long term, interest rates are unlikely to rise for a long period of time because the economic growth rate and price are staying at a low level. If the view becomes dominant that the current monetary easing policy will be maintained for a long period of time, demand for the super long-term zone will increase and the yield curve will flatten structurally.

Under the JGB Issuance Plan for the next fiscal year, the reduction in the issuance amount of super long-term bonds will have the greatest impact on the market. In particular, continuous demand for the 30-Year and 40-Year Bonds is expected from life insurance companies for dealing with the introduction of economic value-based solvency regime. As an investor, we hope an increase in the issuance amount, rather than reduction, for those bonds. On the other hand, it is possible to reduce the issuance amount in the remaining maturities of shorter than 10 years zone where interest rates are negative, including the medium-term zone, which would be decided based on the demand for collateral use and the balance with future issuance of Refunding Bonds.

The issuance amount for the Liquidity Enhancement Auction in the remaining maturities of 15.5-39 years zone should be maintained for the same reason. Also, there are relatively many issues for which the supply-demand balance tends to be tight due to individual factors in the remaining maturities of 1-5 years. That leaves the remaining maturities of 5-15.5 years zone as the candidate for reduction.

・While interest rates declined steeply in the summer in the global bond market, which was led by long-term interest rate, such decline has paused recently. Although the yield curve flattens temporarily influenced by the fading expectation of the Fed rate cut or developments in the U.S.-China trade negotiations, it has been substantially normalized. In Japan, the BOJ Governor Kuroda made comments about interest rates in the super long-term zone and it led the steepening of the yield curve more than expected.

However, investing in such environment is still challenging as a bond investor. The only investing strategy we can take is to disperse risks by diversifying investments across various field, rather than concentrating risks on a particular field, considering the global interest environment, funding cost and the spread environment. In investing JGBs, we will pay due consideration to redemption, demand for collateral use, liquidity and other factors as well.

To make comments about the JGB Issuance Plan for the next fiscal year, mainly at zones where we engage in trading, we hope for high liquidity for the 5-Year, 10-Year and 20-Year Bonds. Although we are not requesting the Financial Bureau to avoid any reduction in the issuance amounts of those bonds, there should be a certain level of liquidity in the market. Concerning an increase in the issuance amount of the 40-Year Bond, which was reported by media, we do not have any particular opinion because it is not included in our investment target. If there is plenty demand, the increase in the issuance amount is acceptable. In addition, the liquidity of the Inflation-Indexed Bond remains low despite the increase in the amount of the Buy-Back. We expect that market’s functions will be gradually activated through such measures.

We support the idea of revising the JGB Issuance Plan during the fiscal year in light of other countries' cases. However, as it is expected that the reaction of market participants will likely to be greater than other countries, adequate communication will be important for maintaining predictability.

・Although JGBs will continue to be an important investment target, the current interest rate level is too low for repurchase while many banks hold large amount of JGBs reaching the maturity within several years. In the process of investing funds corresponding to the gap between loan and deposit, the share of JGBs will continue to be large. However, it is virtually impossible to include JGBs with negative interest rates in the portfolio if they are going to be held for a certain extended period of time, which promotes the banks to purchase the 20-Year Bond. As such investment increase the interest rate sensitivity and risks corresponding to it, we need to pay close attention to risk management and control interest rate risks when investing under the situation where it is difficult to expect that interest rates in the remaining maturities of shorter than 10 years zone turn positive.

We request the Financial Bureau to continue a constant issuance of JGBs under the JGB Issuance Plan for the next fiscal year without any negative surprise because absolute level of interest rates is lowering as our investment target is the remaining maturities of shorter than 20 years zone and the liability duration is being extended.

・We are paying close attention to investment trend of foreign investors because their investment have been expanding significantly. A rise in the foreign interest rates may induce foreign investors to sell the JGBs, leading to the rise in the yen interest rates as well.

We are investing mainly in yen-denominated foreign bonds for an ALM-based investment strategy, in which asset portfolio is built in accordance with the cash flow of yen-denominated liabilities by maturity. However, under the recent situation where interest rates decline steeply, we have started to include corporate bonds, in addition to yen-denominated bonds, in the target of investment while engaging in dialogue with issuers. We are waiting for a rise in yen interest rate while continuing to invest in open foreign bonds, stocks and alternative assets within limits in order to diversify investments under the low interest rate environment.

The level of yen interest rate is important as well because JGBs are the only bonds with long term to maturity compared with corporate bonds and yen-denominated bonds. Although we are investing a substantial amount of funds in currency-hedged foreign bonds as substitutes for yen-denominated bonds when interest rates are too low, which fixes a negative cash flow, this is no more than substitutes and we are waiting for a rise in yen interest rates. It is because the investment return from currency-hedged bonds after hedging costs have fallen significantly too due to the steep decline of currency-hedged bonds. Therefore we are exploring the right time to return from currency-hedged bonds to JGBs. Under the JGB Issuance Plan for the next fiscal year, we request the Financial Bureau to increase the issuance amount of the 30-Year and 40-Year Bonds because there is strong demand for bonds with long term to maturity from the industry as a whole in order to secure the soundness of the investment of the people's insurance assets. On the other hand, it should be considered to reduce the issuance amount in zones with negative interest rates. With respect to the Liquidity Enhancement Auction, for which the issuance amount have increased, we have been using the auction in the remaining maturities of 15.5-39 years zone in particular in a way corresponding to the maturities of liabilities. We request a continued increase in the issuance amount for the zone because there is a sustained demand. On the other hand, the issuance amount should be reduced in the remaining maturities of 5-15.5 years zone because the auctions are conducted every month.

・I will explain the overview of the proposal paper by the Fiscal System Council submitted to the Minister of Finance Aso yesterday, as it is related to the JGB Issuance Plan for the next fiscal year.

The national budget for the next fiscal year is the second budget since the target year for achieving a primary balance surplus was postponed from FY2020 to FY2025. There has been budgetary requests for dealing with the consumption tax rate hike and increased uncertainty over national security and the natural environment. Those requests tend to increase under the current low interest rate environment. In addition, there is a growing public argument that the monetary policy has reached its limits and fiscal policy measures need to be employed. In such circumstances, the Fiscal System Council mentioned the following four points about the national budget for the next fiscal year.

First, as a basic point of view, fiscal issues and social security issues are inseparable from each other. Over the past 30 years, the expenditure for social security has increased most. While local allocation tax grants have increased, social security expenditure accounts for most of the increase, which were covered by issuance of newly-issued bonds. Therefore, fiscal issues are issues of social security, which means that fiscal issues are inseparable from the imbalance between the social security benefits and payments, namely the intergenerational imbalance. That means it is necessary to promote fiscal consolidation through social security reform, regardless of economic conditions or interest rate movements.

Second, some people insist that the easing monetary policy is benefitting the government in terms of interest payments of JGBs. It is only possible when confidence in fiscal management is secured, while Japan's credit rating is only single A. Therefore, revenue and expenditure reform need to be conducted continuously even under the low interest rate policy.

Third, although the fiscal review of pension system has showed a sustainability of the pension system, an estimate by a think-tank has casted a doubt on the fiscal sustainability of national treasury, which underlies the sustainability of pension system as half of the National Pension expenditure is financed by public funds.

Fourth, the consumption tax rate hike to 10% that was implemented last month is a milestone on the long way toward achieving fiscal sustainability and the sustainability of the social security system. As the first step, fiscal reform needs to be implemented to achieve the goal of a primary balance surplus and balancing revenue and expenditure excluding interest payments by FY2025, when all people of the baby boomer generation will have become 75 years or older. I expect the budget for the next fiscal year will be formulated under the broad policy.

・In considering the relationship between demand of JGBs from insurance companies and the capital regulations, it is necessary to identify the short-term demand during the transition period and the long-term sustainable demand which lasts after the transition period. While such demand might arise temporarily, the issuance amount for the long-term and super long-term zones should be decided carefully based on a long term perspective including the situation after the transition.

While optimization of the level of front-loading Refunding Bonds is important, stable issuance of JGBs based on the market demand is also important because unexpected expenditures may arise under supplementary budgets due to the frequent occurrence of natural disasters.

Japan's tax system over the Inflation-Indexed Bond has a room for improvement, compared with the systems in the United Kingdom and the United States. When the yield curve steepens and inflation rate rises, such tax system has a possibility to disturb the market though it would not have any immediate impact under the current situation. It is necessary to deal with this issue when inflation rate rises and demand for the Inflation-Indexed Bond arises in the future, communicating with the market.

Contact:

Financial Bureau, Market Finance Division

03-3581-4111 (ext.5700)