Minutes of the Meeting of JGB Investors
(87th Round)

1. Date: Monday, November 29, 2021 (10:30 a.m. to 11:55 a.m.)
2. Place: International Conference Room, Ministry of Finance /online
3. Gist of Proceedings: Current status and issues for the compilation of the JGB Issuance Plan for FY2022

▶ The Financial Bureau gave the following explanation about the current status and issues for the compilation of the JGB Issuance Plan for FY2022.

・ Regarding the revision of the JGB Issuance Plan as a result of the supplementary budget for FY2021 published on past November 26, while the amount of the Newly-issued Bonds was increased by about ¥22.1 trillion, the amount of the Fiscal Investment and Loan Program(FILP) Bonds was decreased by ¥30 trillion by making use of the surplus cash of the fiscal loan fund. Consequently, the total JGB issuance size and the JGB Market Issuance (Calendar Base) will be reduced by ¥11.6 trillion and ¥9.2 trillion, respectively.

・The JGB Market Issuance (Calendar Base) for FY2021 was heavily dependent on short-term bonds and the funding structure was vulnerable to fluctuations in interest rates. Therefore, the amount of ¥9.2 trillion which is the reduction amount of the JGB Market Issuance (Calendar Base) will be allotted to the reduction of 6-month bonds of short-term bonds.

・ As a result of these revisions, the total JGB issuance size was reduced to ¥224.4 trillion in the supplementary budget for FY2021 from the initial amount for FY2021 of ¥236 trillion, a reduction by ¥11.6 trillion.

・ In addition, the JGB Market Issuance (Calendar Base) was reduced to ¥212.2 trillion in the supplementary budget for FY2021 from the initial amount for FY2021 of ¥221.4 trillion, a reduction by ¥9.2 trillion. The ratio of short-term bonds in the JGB Market Issuance decreased from the initial 37.6% for FY2021 to 34.9%. When compared to the situation before the outbreak of COVID-19, the ratio is still high. However, we believe that we have taken the first step towards normalization.

・ Regarding changes in the outstanding amount of JGBs, the total JGB issuance size was reduced as a result of the supplementary budget for FY2021. However, since the Newly issued Bonds was increased significantly, the outstanding amount of ordinary government bonds excluding FILP Bonds is estimated to stand at ¥1,004.5 trillion at the end of FY2021.

・ Regarding the average term to maturity, although it was significantly shortened on a flow basis in FY2020 to deal with COVID-19, it has been corrected gradually since then. On a stock basis, although it was shortened a little in FY2020, no significant change has been seen.

・ When the average term to maturity on a stock basis is compared to that of other countries, the average term to maturity of JGBs is comparatively high among industrialized nations except United Kingdom.

・ Regarding the current issues about the government debt management policy, its basic policy is (1) to ensure capital funding through secure and smooth issuance and (2) to control the medium-to-long term funding costs. To that end, it is our rule to conduct a careful dialogue with the market. We will keep such policy also in the future.

・ When the JGB issuance size in the future excluding FILP Bonds and Reconstruction Bonds is estimated based on the assumption that the ratio of the composition of maturities in the issuance plan of the initial budget for FY2021 will be maintained even from FY2022 onwards based on the medium-to long-term estimation by the Cabinet Office, it is expected that short-term bonds will continue to be issued at a significantly high level from the next fiscal year onwards, with the proviso that the medium-to long-term estimation by the Cabinet Office is the figure in July of this year and this supplementary budget is not included. As a result, it is expected that the amount of refinancing bonds and the overall issuance size will continue at the current level in the future.

・ Therefore, although we will need to remain vigilant of a variety economic situations in the future, we believe it necessary to consider the composition ratio of issue maturities based on market needs in the phase in which the total issuance size can be reduced like in this supplementary budget, while controlling the issuance size of refinancing bonds through the reduction in amount of short-term bonds with an increased issuance.

・ As regards the shape of the current yield curve of JGBs, it shows a slight slackening in supply and demand for 20-Year and 30-Year Bonds in a relative manner.

・ Regarding the purchase trends of JGBs by the Bank of Japan (BOJ), according to the ratio of purchase of JGBs by the BOJ, while the ratio of purchase of JGBs with a maturity longer than 10 years in particular has been on the decline since the introduction of the yield curve control, the ratio of purchase of JGBs with a maturity between 1 year and 10 years still stands at around 60%. According to the year-on-year change from the same month last year in the amount outstanding of JGBs held by the BOJ, it is currently on the decline. As seen in the discussions on The Advisory Council on Government Debt Management in June this year, it is necessary for us to consider the effects of the monetary policy of the BOJ and attitude towards the purchase of JGBs on the JGB market and interest rates.

・ While BOJ has increased the holding ratio of JGBs, financial institutions have decreased its ratio in recent years. However, they have currently increased its ratio slightly. This is considered to be due to the increased collateral demand.

・ Regarding life insurance companies, although the amount of JGBs held by them has almost remained unchanged, it is currently on the rise. As far as the maturity is concerned, the ratio of JGBs with a remaining maturity longer than 10 years is large in line with the duration on the liabilities side.

・ Regarding regional banks, although the amount of JGBs held by them has been declining, it is currently on the rise. As far as the maturity is concerned, the ratio of JGBs with a remaining maturity longer than 10 years has significantly increased.

・ Regarding individual investors, the issuance size of JGBs for individual investors for FY2021 has been decreased due to the effects of the COVID-19 pandemic and a decreased impact of the campaign for the revision of the fee structure implemented by securities companies since October last year. On the other hand, regarding the redemption amount, although the amount of redemption before maturity has decreased due to the decreased issuance size of the preceding fiscal year, since the redemption amount on maturity has increased compared to that of the preceding year, the redemption amount has increased as a whole.

・ We prepared randomly 2,000 patterns of maturity composition of interest-bearing bonds based on the ratio of the composition of maturities in the initial issuance plan for FY2021 and conducted a cost-at-risk analysis on the relationship between cost and risk, and it was found that when compared to the case in which the initial plan for FY2021 was left unchanged, (1) both cost and risk for 20 Year-Bonds and 2-Year Bonds would decrease when the issuance ratio was decreased, and (2) both cost and risk for 10-Year Bonds would decrease when the issuance ratio was increased.

・ Regarding the JGB Issuance Plan for this fiscal year, the current basic idea of the debt management office is as stated in The Advisory Council on Government Debt Management held in June this year, and it consists of (1) planning to decrease short-term bonds in the future for the purpose of stable issuance and purchase because the ratio of the market issuance of short-term bonds has increased to about 40% in response to COVID-19; (2) of planning to decrease short-term bonds by controlling the total issuance size of JGB without increasing the amount of interest-bearing bonds following the decrease in the amount of short-term bonds; and (3) of increasing the number of investors because of the expansion of the market of 40-Year Bonds. It is considered important to examine the possibility of issuing JGBs monthly and shifting the auction method to the discriminatory price auction in the case where the increase in the number of investors has been confirmed and the amount will be increased further.

・ When the background of the expansion of the 40-Year Bond market and that of the 30-Year Bond market are compared to each other, it has been 14 years since 40-Year Bonds were issued for the first time in 2007 and its market scale has grown to be mature. However, they are handled differently from other bonds, such as that they are auctioned six times a year.

・ Regarding changes in the spread in ultra-long-term bonds, the 40 to 30-Year Bonds spread fluctuated roughly at 2 to 3bps in the last fiscal year. Although it increased temporarily to about 9bps in this fiscal year, currently it fluctuates at about 4 to 5bps.

・ Regarding the status of the Liquidity Enhancement Auctions for bonds with a remaining maturity of 15.5 to 39 years, many of 20-Year Bonds, 30-Year Bonds and 40-Year Bonds with a remaining maturity similar to that of current issues are sold, and, for example, ¥60 billion of bonds with a remaining maturity of 38 to 39 years are sold in one auction as an average.

・ Regarding the application ratio for the Liquidity Enhancement Auctions, that for bonds with a remaining maturity of 1 to 5 years has fluctuated by 4 times or more this year and 5 times or more currently, and that for bonds with a remaining maturity of 5 to 15.5 years fluctuates also by around 4 times, while that for some bonds with a remaining maturity of 15.5 to 39 years fluctuates by about 2 times.

・ According to the financial system report of the BOJ, the amount of interest rate risk on yen-denominated bonds held by financial institutions is at the same level as that of the peak in the past. Since the increased spread of the new coronavirus, all types of businesses have increased their investment position along with an increase in deposit inflow against the backdrop of the expansion of government spending, and the amount of risk has been increasing, consequently. It is necessary to bear in mind that the increase in the amount of interest risk may trigger the risk of sharp rise in interest rates.

▶ Summarized below are the views and opinions submitted by participants.

・ As an insurance company, we require a very long duration. Basically, we manage funds entrusted to us by policyholders in the form of insurance premiums of life insurance as the capital for a long period of time. The policy of maintaining the issuance size of 20-Year Bonds and other bonds with a longer maturity, increasing the amount of 40-Year Bonds and adjusting the reduction amount with 10-Year Bonds and other bonds with a shorter maturity in order to maintain the overall issuance size matches with the direction of fund management of life insurance companies. Since the duration of liabilities is long, we basically buy JGBs with maturities longer than 20 years including the matching of the period from the perspective of interest risk control.

On the other hand, the income of insurance premium of life insurance companies has been on the decline as a whole. Although the decreasing tendency varies depending on the circumstances of each company, we are strongly interested in long-term JGBs such as 40-Year Bonds, 30-Year Bonds and 20-Year Bonds continuously in order to securely manage a large amount of assets.

In the last week market, both interest rates and stocks dropped significantly due to the effects of the new COVID-19 variant. However, we have not changed our view that interest rates will gradually rise. However, while interest rates overseas will rise, interest rates will not rise much in Japan due to the continuation of the monetary policy of the BOJ, resulting in differences in interest rates between Japan and overseas. Even in these circumstances, we will continue to buy JGBs with long maturities.

There is no sense of discomfort in issuing 40-Year Bonds every month.

・ About 70% of our company’s assets consists in the pension management on behalf of the government and we manage this in awareness of GPIF's management. As a result, we are not focused on investing, in particular, in 30-Year Bonds and 40-Year Bonds, and we will invest in them whenever they are relatively cheap. Currently, we have strong needs for 10-Year Bonds and 20-Year Bonds.

Regarding funds used as the source of investment, the maturity of pension funds is increasing and the state in which benefit payment exceeds premium payment continues. Since stock prices are steadily increasing currently, pension funds are invested sometimes in bonds depending on their balance. However, since the amount of benefits is basically large, the situation does not allow us to make new investments.

As to the question of what will happen if negative interest rates are normalized, we are always looking for options for where to focus our investment by considering relative variations such as overseas interest rates and credits other than government bonds. Therefore, we are not currently in a position to suddenly increase investment in JGBs when interest rates normalize.

Regarding the market situation, since interest rates on foreign bonds have been slightly rising with some fluctuations in relative terms, we have increased slightly our investment in foreign bonds and we will consider our investment in JGBs by carefully examining the past trends and liquidity.

As far as our investment in foreign bonds is concerned, investment in hedged foreign bonds is limited and we invest more in non-hedged foreign bonds. Although we adjust the hedge ratio in such a situation as where the dollar is a little higher currently than that in the past, basically we invest more in non-hedged foreign bonds.

・ Regarding the issuance plan for the next fiscal year, we would like to see an increase in the amount of 40-Year Bonds and ¥700-800 billion if issued 6 times a year, or desirably a monthly issuance of ¥400 billion. The current situation is such that the supply has not caught up with the demand for 30-year or longer bonds, and the spread of the yield curve of 30-Year Bonds and 40-Year Bonds has continued to remain low since last year. Although the spread returned to 9bps, it has gradually dropped to the current level of about 5bps in line with the return of demand by investors who took the wait and see attitude temporarily. Therefore, we believe that there is a strong demand.

The BEI of Inflation-Indexed Bonds fell significantly due to the COVID-19 pandemic. However, the BEI was raised by Outright Purchase of JGBs and Buy-back Auctions by the Financial Bureau to become flat. Currently, there is an improvement in supply and demand and there are concerns over a world-wide price increase. Therefore, we would like to see a reduction in the amount of Buy-back Auctions, and if possible, an increase in the issuance size in order to foster the market of Inflation-Indexed Bonds.

Our company keeps a lot of foreign funds. Since the demand for short-term bonds is very strong and there is demand for specific maturities which are used as T-Bill or which are less than 5 years, we would like to see an increase in the amount of bonds with a remaining maturity of 1 to 5 years of Liquidity Enhancement Auctions.

Regarding the outlook for the next fiscal year and beyond, although the effects of COVID-19 will remain for some time, since the scale of new government funds provided by this supplementary budget is very large, we believe that its positive impact on economy is very large, although it is unknown whether or not this scale of money can be digested by economy.

While we believe that interest rates will rise in such a situation as the coexistence with COVID-19, as we consider that there will be no change in the BOJ's policy, our company will buy long-term and ultra-long-term bonds when interest rates rise. Even if the fiscal stimulus is large, if measures with low cost-effectiveness continue to be implemented, the market captures something like MMT, we worry about any adverse effect on Japan, such as an excessive yen depreciation. From that perspective, we believe it necessary for us to hold Inflation-Indexed Bonds to some extent.

Regarding the demand for 30-Year and 40-Year Bonds, it is not that our clients instruct us to invest in said zone, but that our company keeps their funds and determines where to invest. In the negative interest rate zone, if bonds are bought at a negative interest rate, they should be sold at an even lower negative interest rate for making a profit, even considering the rolling down effect. Basically, we buy bonds with a positive interest rate and hold them for a certain period of time. Therefore, although we buy bonds when they are underpriced and if interest rates for bonds with a longer maturity rise, they are attractive. Currently, however, the investors' demand for 30-Year Bonds and 40-Year Bonds is stronger and they are relatively more expensive. Therefore, in that sense, we would like that the issuance of these bonds be increased and become attractive for our company when compared to JGBs in other zones.

Currently, the market of Inflation-Indexed Bonds is not mature enough and there is hardly any liquidity. In addition, if the price outlook does not improve, it is natural to think that the BEI will fall. According to the current worldwide policy, we believe that it is not wrong to somehow hedge against a price increase. In particular, the fiscal expansion continues in Japan, and we believe it possible that a price increase may occur supported by the depreciation of yen. Since Inflation-Indexed Bonds with a floor have good marketability, we consider that they are worth being held considering the risk of price increase and the floor.

Regarding the demand for short-term bonds, some of our clients want us to manage them in cash by designating a zone. Since there is a merit in this in terms of cross currency by exchanging dollars into yen, we believe that our investment will continue until the demand by these investors disappears.

・ As seen in page 26 of the material, the amount of interest rate risks has been increasing for regional banks as a whole. As a result, our capacity to buy JGBs in the ultra-long-term zone is limited and our company does not handle JGBs with a maturity longer than 20 years. Therefore, to tell the truth, we will find it very attractive as investors that 10-Year Bonds or 10-20 Year Bonds produce a bit better yield.

In terms of balance sheet, the deposits have been increasing in the past 1 or 2 years. In the beginning, the amount of loans increased. However, since the growth of loans has been recently decreasing, we have abundant funds for investment.

In terms of overseas interest rates and domestic interest rates, the weight of US bonds has increased. In the future, in the process in which yen interest rates will increase and if the gap is filled, it is naturally necessary to consider shifting money from the US to Japan.

・ Regarding the recent state of the JGB market, it is greatly affected by changes in overseas interest rates and economic indicators and it is rather volatile due to concerns over inflation across the world against the backdrop of the high level of commodity prices. However, since investors' demand for buying on dips is strong at milestones such as 0.10% of 10-year interest rates and 0.50% of 20-year interest rates, the rise in interest rates is limited. Amid the outlook that the domestic market in the future will be influenced by overseas inflation and corresponding tightening measures such as monetary policy set by overseas central banks, we have the policy to flexibly respond to the market trends by adjusting appropriately our portfolio when interest rates decline, while increasing our purchase of 10-Year Bonds and 20-Year Bonds in order to secure carry and roll down when interest rates rise.

Regarding the current status and issues related to the formulation of the JGB issuance plan, we understand and recognize that a large scale issuance of JGBs is also required in FY2022 as a result of the large scale economic measures of the government. Since the average term to maturity has been shortened by the increase in short-term bonds in the COVID-19 pandemic, we consider it appropriate that the issuance size of ultra-long-term bonds for which there is strong need by institutional investors is increased. In particular, we believe it desirable that the issuance size of 40-Year Bonds whose most recent auction was also successful be increased and issued every month. In addition, as the tendency that the demand is biased towards a specific issue continues with an increase in the amount of JGBs held by the BOJ, we are of the view that there is room for increasing the issuance size in Liquidity Enhancement Auctions, in particular, in bonds with a remaining maturity of 1 to 5 years and bonds with a remaining maturity of 15.5 to 39 years.

・ As our company needs to match the duration with the liability, we buy a certain amount of ultra-long-term bonds every year. In addition, in an integrated approach to risk and compliance management, a rigorous control of interest rate risk is required, and the needs for 30-Year Bonds and 40-Year Bonds have increased in recent years.

In particular, regarding 40-Year Bonds, since we are contemplating the possibility of increasing their purchase for the purpose of controlling interest rate risk as an initiative for the next fiscal year and beyond, we would like to ask an increase in the issuance size of 40-Year Bonds for FY2022. Moreover, we would like that 20-Year Bonds and 30-Year Bonds be issued for the same amount or larger.

Incidentally, regarding 40-Year Bonds, we would like to ask the debt management office to shift the bimonthly issuance to monthly issuance in order to remedy the adverse effects of the bimonthly issuance.

Regarding the market, in the wake of the resumption of economic activities and further the introduction of large scale economic measures, the market is subjected to raise interest rates. However, since there is investors' demand for the ultra-long-term zone including our company, we believe that domestic interest rates will continue to remain at a comparatively low level.

Although the overall cash outflow of our company is large, we have investment capability due to new contracts and maturity of assets. In addition, since there is need for matching the cash flow of existing liabilities, we continue to have a strong appetite for investment in JGBs in the ultra-long-term zone.

・ If general demand for 30-Year Bonds or bonds with a longer maturity of life insurance companies is stated in a broad perspective, we believe that there is still a duration gap between assets and liabilities. In other words, the duration of assets is overwhelmingly shorter than that of liabilities. Although the disclosure standard of all companies is not necessarily the same, when the financial condition of each company whose information is disclosed is analyzed, the gap is still big. We are of the view that this movement to reduce interest rate risk will continue including the compliance with the ICS Class Rules and Regulations in 2025, and if we look at the actual monthly trading, we can see that steady and relatively high-level purchases continue.

As far as our view on issues by maturity is concerned, we believe that the demand of life insurance companies for the zone combining 30-Year and 40-Year Bonds will continue, and their focus will be placed on 30-Year Bonds in terms of volume, although there are slight differences depending on individual companies. If we consider the situation bearing in mind the BOJ's purchase amount, we believe that the relevance of the BOJ's purchase of 25-Year or longer Bonds is low with the monthly purchase of ¥50 billion. On the other hand, the relevance of the BOJ's purchase of 10 to 25 years is comparatively large with the monthly purchase of ¥150 billion. When considering that the demand of life insurance companies is strong and there is no room for further reduction in the BOJ's purchase, we would like that a reduction from the current issuance size should be avoided as much as possible including 30-Year Bonds.

We agree to the development of the market for 40-Year Bonds. Generally speaking, in terms of the medium term, liability cash flow such as individual insurance exists for a very long period of time in the situation in which the reduction of interest rate risk will progress and will be refined. Therefore, we believe that there will be considerable needs for 40-Year Bonds and become more apparent. From that perspective, we consider it appropriate that they will be issued monthly or their auction method will be shifted to the discriminatory price auction in due course. When the bimonthly issuance of 40-Year Bonds in the amount of ¥600 billion is changed to monthly issuance, we believe that the amount of ¥200-300 billion is small and the amount should be ¥400 billion. The problem is when this is put into practice. We think it appropriate to give it time. For example, it will be an option to increase ¥100 billion bimonthly and shift to monthly issuance after seeing how it goes. We consider it possible that the bimonthly issuance is increased by ¥100 billion from April and it is determined whether or not the change is made depending on auction results.

Although the competition ratio of bonds of Liquidity Enhancement Auctions with a remaining maturity of 15 years or longer is low, insurance companies back the flow in said zone by the asset and liabilities management (ALM) and we believe that there is constant demand. Since the additionally issued bonds are comparatively concentrated in current portion, if the amount of current bonds is increased, the competition ratio will be reduced a little. On the other hand, many insurance companies in which the reduction of interest rate risk is advanced in terms ofALM adjust their needs by the yield curve in a comparative manner. Since we believe that these investors continue to be in considerable need of off-the-run issues, it is appropriate that the current status quo is maintained.

Regarding investment fund resources for reasons of coronavirus, in terms of insurance sales, the volume of sales dropped significantly due to the difficulty of face-to-face sales activities in the COVID-19 pandemic. As a result of promoting sales by using digital tools, the sales have improved slightly this year. While investment funds were considerably affected in terms of flow, the effect on the overall stock is slight. Therefore, we consider that the effect on investment funds is limited.

Regarding the normalization of interest rates, we wish that it will be realized. In terms of allocation of foreign bonds and JGBs, while each company determines the pros and cons of investments from a short-to-medium-term perspective, currently we are in a stage where we will increase our purchase and reduce interest rate risk from the perspective of the needs for long-term JGBs. As a result, we do not think that this situation will change much. Generally speaking, when interest rates rise, each company presses the accelerator and when interest rates decrease, it stops its acceleration. We believe that the normalization will allow us to reduce interest rate risk in an accelerated manner.

At the current interest rate level, it was difficult to develop products such as pensions and insurance that would serve as a means of long-term savings in Japan. However, if the level of interest rates rises in a corresponding manner toward the normalization, new products will appear. There are very strong needs for long-term asset formation savings including young people. While there are many people who invest in foreign bonds due to the current interest rate level, there are also needs of people who prefer stably saving money in Japanese yen to a certain extent. As a result, it is possible to think that these needs will come back with a rise in interest rates,

・ Since investment fund resources of non-life insurance companies are mainly from car insurance and fire insurance, they are not affected by COVID-19 and the income of insurance premiums has not changed. They are affected more by the presence or absence of natural disasters. If a natural disaster occurs, insurance benefits are paid out by selling JGBS and obtaining cash, but, fortunately, there has been no such necessity for the past 1 or 2 years. Conversely, non-life insurance companies are not in particular need of buying JGBs. Non-life insurance companies have comparatively large short-term liabilities and their needs for 30-Year Bonds and 40-Year Bonds are not large. However, they have also ultra-long liabilities, for example, in excess of 40 years, and in that sense, their needs for JGBs in the 40-year zone exist. In addition, regarding subsidiaries of life insurance companies, although the ALM has been established to some extent, since there are certain needs for replacing 30-Year to 40-Year Bonds, we consider desirable the development of the market of 40-Year Bonds. We consider very desirable the monthly issuance and increase in the issuance size of 40-Year Bonds from the perspective of development of its market.

Regarding the issue whether or not we come back to invest in Japanese yen when interest rates are normalized, we position Japanese yen as an asset to ensure liquidity and we gain profits mainly with foreign assets. The status of non-life insurance companies is such that unless there is more credit spread in Japanese yen assets, investment in yen interest-bearing assets including JGBs will not be increased.

Although we recognize that the extent of hedging against purchase of foreign assets varies depending on each company, since we conduct M&A overseas and take currency exchange risk considerably in that connection, we basically provide full hedging.

・ Regarding ultra-long-term bonds, our investment is focused on 20-Year Bonds. Since there are considerable needs by other investors for them, we believe that the current issuance size is desirably maintained, or there is room for slight increase. As our company does not actively invest in 30-Year and 40-Year Bonds currently, we do not feel uncomfortable in maintaining the current status quo.

Regarding our investments when interest rates return to positive territory, although we will increase our investment in JGBs if profitable upon comparison with government bonds of other countries, they will greatly depend on interest rates of other countries when interest rates actually return to positive territory.

As to the market outlook, we expect that the market will be affected mainly by the prices in the US and the indicators related to labor market conditions. Although we expect that interest rates of other countries will be affected to some extent by the rise and fall of US interest rates, since we expect that JGBs will continue to be supported by the BOJ for the time being, we are of the view that the volatility will remain low in comparison with overseas markets.

Regarding the fundraising of our company amid COVID-19, there is no significant change from the last fiscal year, and we believe that there will be no significant change in the future either.

・ Regarding the market outlook for the time being which serve as a premise for JGB issuance, we are of the view that risks will be avoided for the moment because of current concerns over the new variant which is suspected of having strong infectious capacity. On the other hand, we believe that the government and society of each country have learned how to deal with a variety of events in the COVID-19 pandemic for the past two years. For example, there is a report that a major pharmaceutical company can deliver a new vaccine for the new variant within 100 days, and we think that the extent of its influence is probably limited. If the effect on the economy is limited, the US and other countries in which the inflation rate has been trending upward, we believe that they will tighten the monetary easing steadily. However, we are of the view that the economic constitution or structure will not be turned inflationary by COVID-19 in the medium to long run, and our main scenario is that the economy will turn to the low inflationary environment that has been continuing since the 1980s when COVID-19 is behind us.

Regarding JGBs, although prices will somewhat rise a bit, we believe that the situation is not such that the BOJ will tighten monetary easing and we are of the view that yen interest rates will continue to be stable and low. Based on this assumption, we expect that the issuance size of JGBs for the next fiscal year will be slightly reduced compared to this fiscal year, as shown in the explanatory material. Under this premise, maturities will be lengthened and the amount of T-Bills reduced. As regards the issuance size by maturity of interest-bearing bonds, we believe that the auction results have been stable since the increase by the supplementary budget in the last fiscal year and we are of the view that there is no need for significant change from this fiscal year. As far as maturities are concerned for which there is room for amount increase, we recognize that the 40-year yield curve has been continuously more expensive than the 30-year curve as a whole. Therefore, since, in terms of supply and demand, the demand exceeds the supply, we believe that there is room for amount increase in 40-year bonds.

From the perspective of the JGB rating, while it is rated A, we do not think there is any problem. However, when it is rated BBB, we imagine that things will be different. Since it is considered that one of the motivations for investment in JGBs of overseas investors is the cross currency basis, we think that when the rating is changed, the supply and demand balance will also change.

・ In regional financial institutions, the growth rate of loans and deposits has been slowed down compared to the time before the COVID-19 pandemic, whereas the loan-to-deposit gap has widened. Further, due to the revision of the Special Interest Grant System of the BOJ Current Account Deposit announced on November 16, the fund's investment needs of regional financial institutions will increase as a whole from the next fiscal year onwards when the period of transitional measures ends. In the circumstances, since domestic interest rates have been steady when compared to overseas interest rates, in addition to investing in 20-Year Bonds for mid to long-term holding and flexible buying and selling of 10-Year Bonds for rolling down, we are contemplating the possibility of investing in government bonds and other bonds for cash crush. On the other hand, it is difficult for regional financial institutions to invest in JGBs with a maturity longer than 20-years due to high interest rate risk. We will replace 20-Year Bonds with 10-Year Bonds when interest rates come back.

・ Currently, the volume of deposits have been on the rise. When public spending is increased, it necessarily takes some time before money goes out and piles up as deposits as a result. On the other hand, corporate fund demand for dealing with coronavirus has ceased and deposits exceed loans significantly in terms of the loan-to-deposit gap. Therefore, the needs for investment are high. In the situation in which overseas interest rates are expected to rise, we believe that Japanese government bonds with interest rates relatively hard to rise will play a leading role sometime in the future for investment and if their interest rates rise in line with the rise in overseas interest rates, they will become the target for investment. In addition, since the interest rate cap is tied up by the Interest Rate Risk in the Banking Book (IRRBB), the risk amount is currently directed to tradable foreign currency interest rates.

Since ultra-long-term bonds are not a target for investment for a mega bank, we gave the answer in the advance hearing that we will maintain the current status quo and there is room for an increase in amount for bonds in the medium-to-long-term zone. Regarding the return to normalization from negative interest rates, we are of the view that the scenario will change depending on the trends of the US monetary policy. Although the market forecasts that interest rates will be raised against the inflation in the US, there is a possibility that the downsizing of the balance sheet will be done first to allow interest rates to rise in the long run. The interest rate rise cycle worldwide starts with the rise in US interest rates, followed by that in Europe and in Japan. However, since the overall cycle is turning faster, if interest rates are tightened in Japan at the juncture at which interest rates tightened in the US will be eased, yen interest rates will be affected by global interest rates and will not be raised forever. We believe that this scenario will pose a risk for investors. The effect of the current global inflationary environment on Japan may cause sluggish economic growth because cost increase will not allow wages to be raised in Japan. We are also aware of the effect produced by excessive yen depreciation on foreign currency funding and the rating.

・ Regarding the funding status of our company in the COVID-19 pandemic, the increase in deposits and loans is more moderate compared to mega banks and our investment remains almost same as usual.

Regarding our needs for JGBs, we have needs for T-Bills as collateral in consideration of the BOJ's policy interest rate or a variety of systems. In addition, we also invest in JGBs with a maturity of 5 years and 10 years in combination with other investments aimed at the roll down return and price fluctuations. We invest in these with needs in consideration of the BOJ’s interest rates.

As a whole, the needs for investment and collateral are large and JGBs are included in the collection of investment products (universe) together with foreign currencies. We invest in them in consideration of their merits and demerits and currently, our needs are in foreign currencies in terms of both liquidity and interest rate levels. However, when the time comes when JGBs are relatively advantageous in terms of market liquidity and a variety of economics when interest rates rise, we believe that at such a time the needs for JGBs will increase naturally for home bias.

・ Our company keeps funds of a very wide variety of clients ranging from institutional investors to individuals for management purpose. Currently, due to the expansion of global inflation, deposits for investment in sovereign bonds have significantly decreased. We have the impression that funds are continuously deposited, instead, for credits with a short duration, securities that produce yield or those with low interest rate risk.

Our business consists of active management without need of holding securities based on a benchmark, and we place weight on those that produce higher value and pay back the return to clients. As far as JGBs are concerned, ultra-long term bonds are more interesting than 10-Year Bonds or shorter term bonds which are under the control of the BOJ, and we are keenly interested in how to invest in them.

Regarding the amount increase of 40-Year Bonds, we have the impression that the diversification of investors is still uncertain. In other words, we have the impression that there are fluctuations in liquidity. Therefore, we are of the view that an increase in the issuance size should be carefully examined. There is a talk about monthly issuance and shift to the discriminatory price auction. Since the auction of bonds with a remaining maturity of 15.5 years or longer of Liquidity Enhancement Auctions is alternated with the auction of 40-Year Bonds and actually issued bimonthly.If the monthly issuance is adopted, an adjustment should be made. In addition, regarding the shift to the conventional method (discriminatory price auction), attention should be paid to the tail risk. Therefore, we believe it more desirable that instead of shifting to the monthly issuance all at once, for example, a minimum increase of ¥100 billion is issued to begin with before taking the next step by checking the increase in the number of investors.

We believe that it will take some time to increase the number of participants in 40-Year Bonds. Although the number of investors may increase when investment attractions increase with an increase in yield, as a result of increasing the issuance size, we believe all depends on the balance with the risk. Since an adverse effect such as a rapid increase in interest rates may occur, we believe that it is the best option to find a good balance gradually with time.

・ Regarding 40-Year Bonds, since the duration of liabilities is basically based on deposits of clients with a deposit period of less than 10 years according to the ALM of our bank, there is no need for 40-Year Bonds. Regarding the issuance of interest-bearing bonds, we do not see any problem in increasing ultra-long-term bonds and reducing short-term bonds. From the perspective the ALM, we believe that the reduction in the amount of 10-Year to 20-Year Bonds is undesirable because this will tighten the balance between supply and demand. This is due to the fact that we will need to continue to buy a certain amount of them with positive interest rates from the perspective of the ALM.

Regarding the movement of deposits of our company in the past in the COVID-19 pandemic, deposits which tended to increase in the past have increased further because a large amount of cash handout piled up. However, an increase in liabilities does no increase the capital. Although a certain adjustment is naturally required from the perspective of the ALM, we will not change the investment risk itself basically.

Regarding whether or not we shift our investment from foreign bonds to domestic bonds when interest rates rise, as we make it a rule to promote internationally diversified investment, we will not change this policy. However, we may possibly increase the ratio of domestic bonds based on risk and return from the perspective the ALM on the assumption that there is a very large amount of yen deposits on liabilities side and interest rates rise.

Regarding our investment policy, it is not that we are increasing foreign bonds because deposits have increased, but that yen interest rates have been very low for a long period of time, and we have shifted assets over time from the perspective of internationally diversified investment. Therefore, we have not taken any special action because deposits have increased in the COVID-19.

・ Expenditures surged because of the three supplementary budgets in the last fiscal year and a large amount of short-term government bonds were issued to cover them, We believe that it is worth noting that JGBs in the medium-to-long-term zone have been issued in a regular and predictable manner. Further, as explained by the debt management office, the amount of short-term bonds could be reduced albeit slightly.

The Newly-issued Bonds increased by ¥22 trillion in the general account as a result of the supplementary budget of FY2021. While tax revenues are expected to increase by ¥6.4 trillion, an additional expenditure of ¥36 trillion has been added. When this figure is compared to the additional amount of ¥74 trillion as a result of the three supplementary budgets in the last fiscal year, the amount has been halved. Incidentally, ¥30.8 trillion is available this fiscal year from the expenditure and budget carried forward from the previous fiscal year. Although it is necessary to pay close attention to the effect of Omicron variant of COVID-19, we should work for normalization by taking advantage of the trial and error experience from the last year and by not fixing response measures against COVID-19 for a long period of time. For example, regarding the medical supply system such as beds reserved for COVID-19 patients, there were hospitals which did not accept patients despite receiving financial support. Therefore, we should take into consideration the reflection that what is lacking is not the financial support, but the coordination and role division between hospitals.

In addition, regarding the trends of deposits and loans as described by other members, currently the household deposit balance has been surging as a result of a variety of measures taken including the Special Cash Payment. The total amount of COVID-19 related financing between credit guaranteed financing from private financial institutions and financing from governmental financial institutions for companies is as high as ¥60 trillion. In such circumstance, the ratio of corporate current deposits to current liabilities has been increasing and exceeds 45%.

We should be prepared not only for the re-spread of the pandemic, but also for disasters such as an earthquake occurring directly beneath the Tokyo Metropolitan Area in the future. In the past, immediately after the Great Kanto Earthquake, the Japanese government had great difficulty in fund raising and issued JGBs with Deep Discount at high interest rates referred to as the humiliating bonds, that is, government bonds that humiliated Japan in New York in 1924. The bonds were issued at 92.5% with interest rates of 6.5% for 30 years.

Regarding the increased government debt due to COVID-19, foreign governments have started to secure financial resources and fiscal consolidation including tax increase. It is also necessary for Japan to continue to firmly perform fiscal consolidation. If it is possible for the government to avoid fixing and lengthening temporary measures against the COVID-19 pandemic in future supplementary budgets, we do not think it is an impossible task to turn the primary balance into surplus in FY2025 in combination with the upward revision of tax revenue in this time's supplementary budget. The issuance size of short-term bonds was about ¥20 trillion in the initial budget before the occurrence of COVID-19. We believe it possible to return to such a level. In the meantime, it is important that JGBs in the medium-to-long-term zone continue to be issued in a regular and predictable manner.

Regarding the Omicron variant, a bull steepener occurred in the US market last Friday and the 5-year BEI in five year's time fell albeit slightly. It seems that the movement to accelerate the tapering so far was rewinded. However, there are basically things that are difficult to understand. We share the view that the effect of COVID-19 is not inflationary. What we worry about is the fact that the labor force participation rate in the US labor market does not return to normal. The effect of the decreased labor force participation rate on the wage cannot be ignored. The decision to be taken by the Fed is awaited. In addition, it is difficult to understand the effect of decarbonization which has become a big issue on prices. It is also a difficult problem to determine the effect of the US-China conflict on long-term interest rates. Basically, however, we are of the view that the long-term interest rates in Japan will continue to be stable for the time being including the next fiscal year.

・ Although an issuance of a considerable amount of JGBs was contemplated in the initial budge for FY2021 and a significantly large supplementary budget was compiled this time, we are pleased to highly evaluate the fact that the total amount of JGBs was adjusted with FILP Bonds to minimize the impact on the market.

At the time of the Great East Japan Earthquake, the issuance size of JGBs was increased while keeping a close eye on financial resources. In FY2020, it could not be helped to some extent because of an emergency state. However, we are greatly concerned over the fact that while a huge amount of JGBs continues to be used also in FY2021, their funding resources are not fully discussed. If a large scale government spending is continued also in FY2022, it is important to build an environment to allow discussions on funding resources to match it. As a part thereof, it is important to build an environment in which the JGB market issues a warning of the importance of the fiscal discipline before the rating is lowered.

The BOJ controls 10 year or shorter-term bonds with the yield curve in a considerable manner and we believe it important that the issuance maturities of government bonds are adjusted in such a manner that the JGB market issues an early warning for 10 year bonds.

Currently, there are concerns over price increase in the US and other countries. It is also important for Japan to continuously discern the trends and calculate indicators of inflation. We believe it important to develop the market of Inflation-Indexed Bonds, not only from the perspective of continuously developing the market, but also from the perspective of developing important indicators for future fiscal management.

Contact:
Market Control Section, Market Finance Division,
Financial Bureau,
Ministry of Finance
03-3581-4111 (ext.5700)