Minutes of the Meeting of JGB Market Special Participants
(95th Round)

1. Date: Tuesday, September 28, 2021
2. Place: Held in writing
3. Gist of Proceedings:

1. Issuance size of Inflation-Indexed Bonds in the October-December 2021 quarter

▶ The Financial Bureau gave the following explanation about the issuance size of Inflation-Indexed Bonds in the October-December 2021 quarter.

・ As shown on page 3, according to the JGB Issuance Plan for FY2021, it is stipulated that there will be issuance of Inflation-Indexed Bonds four times a year for the size of ¥200 billion per each time while stating that "The size of issuance may be adjusted in a flexible manner in response to market circumstances and demands of investors which will be determined based on discussions with market participants." In addition, as shown on page 4, it is stipulated about Buy-back Auctions that "Buy-back Auctions in FY2021 is planned to be implemented based on market conditions and through discussions with market participants." Today, we would like to hear your opinions about the size of issuance in the October-December quarter.

・ In the July-September quarter, as shown on page 5, we conducted an auction of issuance for the amount of ¥200 billion in August and conducted Buy-back Auctions for the amount of ¥50 billion every month by considering market circumstances and exchanging opinions with market participants. The results of the issuance by auctions and Buy-back Auctions are shown on pages 6 and 7.

・ The situation of the secondary market is shown on pages 8 and 9. Since the beginning of the year, the BEI rose steadily. In July, however, Inflation-Indexed Bonds were sold temporarily in a rather large amount. However, they picked up again and the 10-year BEI generally averages out at over 0.2%, currently. If we look at the BEI by issues, while BEI of a part of issues with a short period to maturity has been on a rise, that of the issue number 26 as the current bond shifts at a low level. Therefore, there are some differences among issues in terms of BEI.

・ In the circumstances, we asked for your opinions in advance. Some members said that since it is seen that the balance between the supply and demand has improved by the fact that the application rate for Buy-back Auctions decreased suddenly, but also overseas investors are buying very recently in view of the rising share prices in addition to the improvement of the BEI itself, it is preferable that the size of issuance is left as it is and the amount of Buy-back Auctions is reduced.

・ However, many participants expressed the view that since not only there are strong needs continuously for selling Inflation-Indexed Bonds on temporary recovery, but also the balance between the supply and demand of the issue number 26 which is not currently subject to purchase is relatively weak compared to other issues, it is desirable that the size of issuance and the amount of Buy-back Auctions are left as they are by adding said issue to the list of issues to be purchased.

・ We believe that the development of the Inflation-Indexed Bonds market is an important issue in Debt Management Policy and since the current size of issuance and the amount of Buy-back Auctions are the results of extraordinary and temporary measures in the wake of the significant market deterioration caused by the spread of the infections of the COVID-19, we consider it undesirable that the current situation is normalized.

・ However, since there is still a sense of uncertainty over the balance between the supply and demand, as stated earlier, we are considering conducting an auction of size of issuance of ¥200 billion in the October-December quarter in the same manner as in the July-September quarter, as shown on page 10. In addition, regarding the Buy-back Auctions in the October-December quarter, we are considering adding the issue number 26 which is relatively weak in terms of supply and demand to the purchase list and carrying out a Buy-back Auction in the amount of ¥50 billion every month in the same manner as in the July-September quarter.

・ As above, we explained the situation regarding the Inflation-Indexed Bonds market and our proposal in consideration thereof.

Since we will make a comprehensive decision based on the contents of today's meeting on the size of issuance in the October-December quarter, we will hear your opinions again.

Incidentally, in view of the fact that the balance between the supply and demand for Inflation-Indexed Bonds has been improving compared to the situation from March 2020 onward when these extraordinary and temporary measures have been introduced, we are contemplating the possibility of conducting an in-depth review for the January-March quarter 2022 with a view to normalizing the current situation in light of the situation of the auctions of the October-December quarter.

▶ Summarized below are the views and opinions submitted:

・ We agree to the proposal of the debt management office. Although the supply and demand is currently favorable, the price fluctuations are large and the situation in which liquidity is not sufficiently ensured continues. We expect that the debt management office will endeavor to help develop the market by issuing an amount capable of maintaining market liquidity and buying back an appropriate amount.

・ Apparently, the BEI of Inflation-Indexed Bonds has improved when compared to some time back as described by the debt management office and the market has been rehabilitated to a certain extent. However, they still lag behind other macro assets in a conspicuous manner. Although the results of Outright Purchase of JGBs and Buy-back Auctions in which the current bonds are excluded are somewhat favorable, since no positive deviation from the transaction price at the last minute has been seen, it can be hardly said that the balance between the supply and demand has been restored. Therefore, we believe it appropriate as proposed by the debt management office that the current size of issuance and the amount of Buy-back Auctions be maintained.

・ We would like that the current size of issuance and the amount of Buy-back Auctions be maintained. Currently, the prices are formed in line with the external environment. However, when a sell flow occurred, the BEI sharply dropped without matching between sell and buy orders some time ago. Therefore, we believe that there is no need to change the balance between the supply and demand at the present moment. In addition, as it has been some time since the issue number 26 was first issued, and the size of issuance was large and the difference in terms of supply and demand is growing compared to other issues, we want that said issue be included in the list of issues to be bought.

・ Since the issue number 26 which is a newly issued bond has been excluded from Buy-back Auctions so far, transactions have been concentrated on existing bonds. As a result, the issue number 26 has been left at a price cheaper than the theoretical price and the price formation of Inflation-Indexed Bonds has been distorted. Since the outstanding balance of issue amount has exceeded, we agree to that the newly issued bond be included in the list of issued to be bought back.

・ We agree to maintain the status quo of the current size of issuance of ¥200 billion and the (monthly) amount of Buy-back Auctions of ¥50 billion. Although the BEI sharply dropped to +10bps or less at the end of July, the drop was temporary and we are of the view that the supply and demand environment has improved significantly. We also agree to the explanation of the debt management office that “we are contemplating the possibility of conducting an in-depth review for the January-March quarter 2022 with a view to normalizing the current situation in light of the situation of the auctions of the October-December quarter.”

・ We agree to the proposal of the debt management office.

・ When considering that existing bonds have been sold to a certain extent, while the demand for the current bond by domestic investors lacks vigor, we believe it appropriate that the status quo of the current size of issuance and the amount of Buy-back Auctions be maintained. In addition, since there is no much difference in supply and demand between the newly issued bond and existing bonds, we consider that it is time to study the possibility of incorporating the newly issued bond in the list of Buy-back Auctions.

・ There are strong needs for current issues. In order to maintain and improve liquidity, we would like the size of issuance of ¥200 billion which is the same amount issued in August. Regarding Buy-back Auctions , we support the current monthly amount of ¥50 billion in order to stabilize supply and demand in consideration of the fact that selling on temporary recovery by investors continues and the average buying price difference in Buy-back Auctions in July, August and September is in the negative range. In addition, we agree to the proposal that the issue number 26 be incorporated in the list of Buy-back Auctions from October due to the relatively weakening supply and demand.

・ Although we would like that both the current size of issuance and the amount of Buy-back Auctions be maintained, if top bidders have some opinions, we will support them.

・Since there is no demand for buying the product for ALM matching, if the balance between the supply and demand deteriorates, we would request a flexible response. As the situation is stable currently, we agree to the proposal of the debt management office.

・ We agree to maintain the status quo.

According to the results of the Outright Purchase of JGBs and Buy-back Auctions from July onward, the balance between the supply and demand has seemingly improved than before in terms of both the cutoff point and bid-to-cover ratio. However, since the issue number 26 is excluded from Buy-back Auctions, it seems that the BEI is becoming distorted when compared to the existing bonds (the issue number 25 and issue number 24, etc.) We would like to see that the issue number 26 is also included in the list of Buy-back Auctions also from the perspective of index.

・ Although the inflation barometer currently shows 2% or more, the inflationary pressure in Japan is limited and a heightened sense of uncertainty continues. Both Outright Purchase of JGBs and Buy-back Auctions have been smoothly digested and no significant changes are observed.

Under the circumstances, the investors demand is low. Therefore, we believe that it will be appropriate from the perspective of stable issue as well that the issuance and Buy-back Auctions of the current size be implemented.

・The level of the BEI has increased when compared to the beginning of September. Therefore, we believe that the situation will be normalized (increase of size of issuance and reduction in the amount of Buy-back Auctions by including the newly issued bond in the list of issues to be bought). However, if the situation is normalized too quickly, the current momentum may be lost. Therefore, we consider it desirable that the current status quo be maintained in the current quarter to attempt to normalize the situation from the next quarter.

・We recognize that the Inflation-Indexed Bonds market continues to show solid price movement when compared to nominal bonds in the situation in which the future price increase continues to be unpredictable in Japan and inflation is concerned in overseas. On the other hand, it seems that the gap in supply and demand between the current bond and off-the-run bonds still remains despite a slight improvement. Under the circumstance, we presume that it is important to improve the balance between the supply and demand for the time being and we support that the issuance and Buy-back Auctions of the current size continue to be maintained.

・ According to the changes in the BEI in the last year, a recovery trend is observed with small fluctuations. In the circumstances, we believe it reasonable that the amount of Buy-back Auctions for issues subject to a large purchase compared to the size of issuance be reduced by about ¥20-30 billion. We have no objection to the incorporation of the issue number 26 which is the current issue in the list of issues to be purchased.

2. Liquidity Enhancement Auctions in the October-December quarter 2021

▶ The Financial Bureau gave the following explanation about the Liquidity Enhancement Auctions for the October-December 2021 quarter.

・ As shown on page 12, according to the FY2021 JGB Issuance Plan regarding Liquidity Enhancement Auctions,

(1) while it is assumed that JGBs in a total of ¥11.4 trillion will be issued in a year, including ¥2.4 trillion with remaining maturity of 1 to 5 years, ¥6.0 trillion with remaining maturity of 5 to 15.5 years and ¥3.0 trillion with remaining maturity of 15.5 to 39 years,
(2) finally, “the details will be flexibly adjusted in view of the market environment and investment needs,” .
Today, in response to this plan, we would like to hear your opinions regarding the issuance size of issuance for each maturity zone for the October-December quarter.

・ As shown on page 13, we issued JGBs with remaining maturity of 1 to 5 years in the amount of ¥400 billion in the odd-numbered months of July and September, JGBs with remaining maturity of 5 to 15.5 years in the amount of ¥500 billion every month and JGBs with remaining maturity of 15.5 to 39 years in the amount of ¥500 billion in the even-numbered month of August. These results are shown on pages 14 to 16.

・ In the circumstances, we asked your opinions about the Liquidity Enhancement Auctions for the October-December quarter in advance, and some members indicated strong investment demand for specific issues and maturities. However, since no significant change in the balance between the supply and demand that requires the balance of the distribution of size of issuance among issues to be changed, we found that all members were of the opinion that it was appropriate to maintain the current size of issuance.

・ In response to this, we prepared our draft for the issue amount for each maturity zone in the October-December quarter, as shown on page 17. We are contemplating the idea of issuing JGBs with remaining maturity of 1 to 5 years in the amount of ¥400 billion in the odd-numbered month of November, JGBs with remaining maturity of 5 to 15.5 years in the amount of ¥500 billion every month and JGBs with remaining maturity of 15.5 to 39 years in the amount of ¥500 billion in the even-numbered months of October and December.

・ Regarding the size of issuance for each maturity zone for Liquidity Enhancement Auctions for the October-December quarter, we will make a comprehensive decision based on the contents of today’s meeting, and we will ask your opinions again.

▶ Summarized below are the views and opinions submitted:

・ We agree to the proposal of debt management office. Although there is room for an increase in amount in all maturity zones, we believe it reasonable that the amount in the previous quarter be left unchanged.

・ We agree to maintain the status quo.

Although strong demand for off-the-run issues continues in auctions for issues with a remaining maturity of 1 to 5 years and 5 to 15.5 years, we do not think that currently, the balance between the supply and demand is tighter than before according the auction results from July onward. Therefore, we believe that there is no need to increase the current size of issuance.

・ The amount is evenly distributed among maturities and JGBs have been stably absorbed by short covers by security companies and investors' demand. Therefore, we believe that the distribution similar to the current one is appropriate.

・ Since investors' demand and needs for short covers by security companies are strong for each zone, we want that the status quo be maintained. Particularly, as the yield curve of the issues with a remaining maturity of 1 to 5 years is frequently distorted, we belive that there is room for an amount increase.

・ We agree to the proposal of the debt management office to keep the current status quo.

・ We want that the same plan as that in the July-September quarter be continued. Since there are seasonal fluctuations in Liquidity Enhancement Auctions and there is fair demand for each zone, we acknowledge that there is no particular reason to change the size of issuance at the moment.

・ Since strong needs continue, we want that the current status quo be maintained.

・ We do not see any problem in maintaining the status quo.

・ We agree to the proposal of the debt management office.

・ In order to meet the needs of investors and traders for each zone and maintain liquidity in the secondary market, we support the current size of issuance.

・ We have no objection to the current distribution.

Strong needs for JGBs with remaining maturity of 5 to 15.5 years have been confirmed. If the supply of ultra-long term JGBs poses a burden for the market due to an operational change on the part of the Bank of Japan (BOJ) in the future, we believe it an option that the amount of JGBs with remaining maturity of 5 to 15.5 years is reduced and the reduced amount is distributed to other issues.

・We believe that the current purchase amount is well balanced. Although the liquidity of off-the-run issues with remaining maturity of 1 to 5 years significantly drops sometimes due to purchase by overseas investors, the situation is not so serious as to cut the amount of other maturities.

・The money is distributed in a well-balanced manner in each maturity zone and we believe it desirable that the status quo is maintained.

3. Latest JGB market situation and outlook for future investments

▶ Summarized below are the views and opinions submitted:

・ Entering September, yen interest rates that remained low in a narrow range (0 - 0.03% for 10-Year Bonds) until August are pressured to gradually rise against the backdrop of the Japanese political situation and high share prices in addition to interest rate rises overseas. However, we believe that it is rather difficult to anticipate an excessive future rise in interest rates throughout the fiscal year in the market in the situation in which YCC and Outright Purchase of JGBs continue. Therefore, we believe that the current environment is such that each maturity bond will be stably issued and digested without large adjustments.

・YCC by the BOJ is working effectively and the market remains stable as a whole. On the other hand, however, there is no significant change in the purchase of issues by the BOJ amid the amount increase of the current bonds last year and the gap in supply and demand between issues after the amount increase and issues prior to the amount increase is widening. Therefore, we believe that we should bear in mind the possibility that the market functionality may decrease.

・Although yen interest rates for 10-Year Bonds have continued to change in a narrow range close to zero percent for a long time against the backdrop of the demand by overseas investors and no significant change in dollar interest rates, currently, yen interest rates tend to rise amidst the rise in global interest rates. Although we do not think that interest rates will continue to rise amid concerns over the Chinese economy, we should be mindful of the trends and movements of overseas interest rates. Furthermore, the fiscal policy after the LDP presidential election will gather attentions and volatility will increase for the time being for the first time in a while.

However, since no significant change has occurred in the JGB market, we do not expect that interest rates for 10-Year Bonds will exceed 10bps.

・The demand to buy JGBs at average winning bid prices has increased in JGB auctions from a few years ago due to an increase in demand by overseas investors, and the tendency currently continues. Some members proposed several times in this meeting in the past that the JGB auction system be changed into the uniform price auction. Since it is expected that demand by investors in different time zones will further increase in the future, we believe that the uniform price auction will conform more to the market demand. Therefore, we believe it appropriate that the auction system for JGBS other than 40-Year Bonds and Inflation-Indexed Bonds be changed into the uniform price auction from the perspective of stable issuance of JGS in the future.

・After a significant drop in interest rates from the beginning of the fiscal year, interest rates for 10-Year Bonds were in the range of 0.00 to 0.05% in July to August in the same manner as in the latter half of last year. Interest rates rose throughout this month for a variety of reasons, such as the rising share prices after the resignation of Prime Minister Suga in the beginning of September, contents of the latest FOMC and Hawkish remarks of BOE, uncertainties over the LDP presidential election, concerns over a reduction in amount as seen in the publication of detailed purchase of the quarter by BOJ, etc., and the current situation is such that 10-Year Bonds, 20-Year Bonds and 30-Year Bonds are traded at 0.065%, 0.460% and 0.695%, respectively.

In the wake of the summer rally in bonds in Europe and the US, 10-Year Bonds was bought at the bid of 0.00% one time in the beginning of August. However, unlike the last fiscal year, no bull flattener of the yield curve was observed. We attribute this to the increase in the amount of 40-Year Bonds, slowing of purchase activity by life insurance companies, monthly implementation of BOJ purchase of ultra-long term bonds, etc.

Regarding market prices in subsequent months, when considering that the possibility of unforeseen circumstances, such as a change of government after the general elections, a revision of the YCC policy, etc. is low, we are of the view that interest rates for 10-Year Bonds and 20-Year Bonds will remain in the core range of 0.04 to 0.10% and 0.43 to 0.50%, respectively, within the year. Although there is a concern in the market about an increase in JGB size of issuance as a result of economic measures after the New Year, there is no prospect of interest rate rise unlike in the US and Europe. Therefore, we are currently of the view that there will be no significant interest rate rise.

・ There was no demand response in the market to the decision of BOJ to conduct the revision of the Outright Purchase of JGBs of long-term bonds every 3 months, and the reaction to the external environment is comparatively weak. The fluctuation range is small as in the October-December quarter in FY2020. There is a possibility in the future that the external environment may have a large influence due to the rise in interest rates in the US and some changes in the yield curve due to fiscal factors may occur. However, we believe that the situation in which the fluctuation range is limited will continue.

・The market is generally stagnant partially due to the fact that interest rates overseas fluctuate within the range, and we are of the view that the market crisis continues in terms of its functionality. On the other hand, as the number of customers at home has increased since the spread of the COVID-19 pandemic, not only the number of transactions in the secondary market has decreased, but also the number of overseas investors has increased. As a result, the auctions have taken on more importance and it seems that the demand to buy JGBs at average winning bid prices has increased. In the circumstance, we would like that the amount of non-price competitive auction I will be increased.

・While BOJ's ongoing large-scale JGB purchase has been extended for a very long period of time, the interest rate level is low and there is hardly any movement. As a result, the balance between the supply and demand of current issues of each maturity whose volume has been increased as a result of the increase in the issuance of JGBs from the last fiscal year has been deteriorating. In other words, a decrease in liquidity of existing bonds and the relaxation in the balance of the current bond and similar ones are progressing simultaneously to cause current issues to become cheaper. We consider that it is necessary for BOJ to reexamine to conduct switch auctions.

・We think that there will be an opportunity to discuss the size of issuance for the next fiscal year and we are aware of the need to prioritize the opinion of companies with higher bid acceptance ratio in such discussion.

・In addition to the prospect that the tapering and interest rate rise will be implemented ahead of time in the US, since there are expectations for the new prime minister in Japan, share prices are rising and interest rates are moderately rising. However, as investors are strongly willing to buy on dips, we believe that there will be no significant increase in interest rates.

・Yen interest rates continue to remain stable at a low level in response to overseas trends and positioning. Not only the monetary policy but also a large amount of surplus funds support the market and the issuance plan tailored to investors' needs is working effectively. On the other hand, 3M size of issuance absorbs all FB issuance, only 3M among T-Bills tend to be unstable in terms of supply and demand.

・Volatility is high recently. However, we believe that basically, volatility continues to be under control by YCC.

・We assume that the current level of issuance of interest-bearing bonds will continue. However, since the size of issuance is already considerable currently, the impact of each auction has increased compared to before. According to most recent surveys, it seems that there is a high possibility that Mr. Kishida will become the next prime minister. However, concerns over an increase in the issuance of JGBs may lead to an unexpected volatility rise depending on the formation of a cabinet. Therefore, we would like that careful coordination among debt management office and close communication with the market will be continued so that stable issuance of JGBS may not be impaired.

・We are paying attention to the LDP presidential election and the political schedule before the House of Representatives election. We believe that the market is closely monitoring the effects of speculations over financial resources for various policies of campaign promises made by each political party, appointment of the successor of BOJ by the post Suga administration, and momentum for the revision of the bold monetary easing on long-term interest rates.

・ The 10-Year JGB yield between July 1 and yesterday (September 27) has changed in a narrow range of 0.000 to 0.055% (this is identical to the range between the middle of June, last year and the end of January this year). During this period, there were factors for interest rates to rise, such as (1) the announcement of resignation by Prime Minister Suga, (2) improvement in the situation of COVID-19 crisis and (3) the rise again of long interest rates in the US.

Regarding the item (1), the JGB market was calm despite a sharp rise of share prices. The economic and fiscal policies of the four candidates for the new LDP president differ to a certain extent. However, it is the general view that the yield will not be changed by thrusting aside the pressure of the strong yield curve control no matter who is elected. Although the new president is elected tomorrow, September 29, we believe that the reaction to the result will be limited.

Regarding the item (2), our view is basically that “It is not easy to acquire herd immunity with vaccinations and it is highly probable that the number of infected people will increase and decrease repeatedly due to new variants in the future. In that case, the risk that economic activities will be restricted several times is relatively high in Japan in the same manner as today, due to insufficient medical preparedness compared to other countries.” In the circumstance, the ups and downs in the number of infected people have affected the ups and downs of the yield to a certain extent and contributed currently to a slight rise in the yield.

Regarding the item (3), the statement of the FOMC of September 21 and 22 and the interview with FRB chairman Powell to end the tapering and raise interest rate ahead of schedule were viewed as Hawkish. However, the price rise due mainly to supply restrictions will eventually calm down and the pace of economic recovery will also slow down with the fading of fiscal effects. Uncertainties over the economic and financial environment in the future are strong and the possibility that the economy will evolve according to the estimation of the FRB is not necessarily high. Therefore, if the yield of 10-year treasury bonds in the US comes close to 1.77% recorded on March 30 this year, there is a possibility that the 10-Year Bonds in Japan may rise to 0.10%.

Summing up, we predict that the yield of 10-Year Bonds will change in the range of -0.050 to 0.125% until the end of March, next year.

・When compared to the trends of the financial markets overseas, interest rates in the JGB market change comparatively stable in a low range and weak JGB auction results are seen here and there. We will be mindful of economic fundamentals in Japan and abroad and the supply and demand trends in the future.

・Since the FOMC on September 22, overseas interest rates fluctuate dynamically. However, yen interest rates are limited despite such a fluctuation factor as the LDP presidential election. Although we believe that the operation management policy of BOJ to decrease the involvement of the operation in the market is right, the adjustment of the operation method based on the idea of 10-year YCC serves only as a symptomatic therapy to treat minor and incidental details, as demonstrated by the past price actions. The functionality and liquidity continue to remain in a collapsed state due to the prolonged YCC policy. The volatility index of Japanese bonds before the introduction of YCC was 3.41 on an average, while that of this quarter is 1.45, which is a decrease of around 60% showing clearly the decreased functionality. It can be said that this figure shows the low attraction of the JGB market compared to other interest rate markets and we believe that YCC, strictly speaking, 10-year pinning is the main factor for the decrease in functionality and liquidity. As shown earlier, we think that at least a price movement over 3 is a normal market when considering current overseas interest rates and political situation. We find it strange to refer to the current situation in which variations are artificially controlled as that “interest rates are stable at a low level” and feel that something is wrong.

In addition, although the specific reasons are omitted here, we continue to ask the dept management office to change the auction method of the ultra-long term zone to the uniform price auction.

・ According to the current size of JGB purchase by BOJ, it is difficult for long-term interest rates to fall to a negative range unless a proportionally impactful event occurs. On the other hand, since investors' needs to use capital are still strong and interest rates have not risen sharply, the environment with low volatility continues. As the increase in the size of issuance of JGBs is not minded so much, we believe that interest rates may rise when the increase in the JGB is taken into consideration.

4. Communication from the Finance Bureau

・ The amount of bids accepted and pro rata rates were corrected due to a clerical error of the debt management office in the 5-Year Bonds auction on September 9. We apologize to all participants. We did not only investigate the cause and take measures to prevent recurrence, but also are considering improving the system. We would like to take this opportunity to apologize again.

・ On the other hand, we do not only confer a special qualification to participants, but also impose certain responsibilities for bidding and successful bidding in the auction. There are rare cases in which the bidding responsibilities are not fulfilled due to minor calculation mistakes or neglect of confirmation. We would like to ask all participants to thoroughly fulfill their responsibilities by using a variety of means such as a check sheet to check whether or not bidding responsibilities have been fulfilled, reconfirmation of appropriate clerical procedures, etc.

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