1 Trends of JGB Market in FY2023

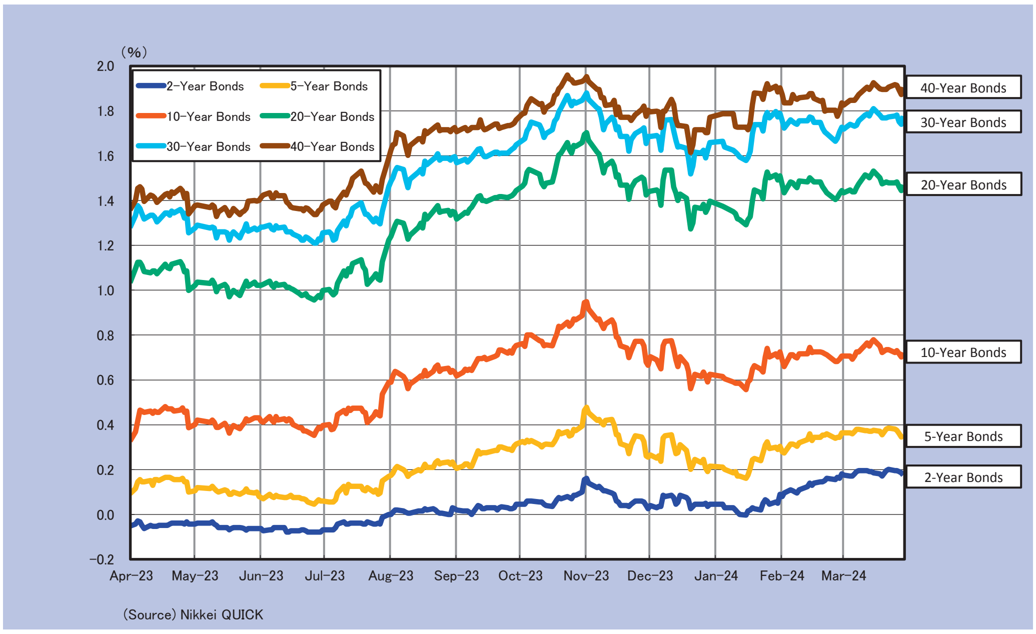
(1) Overview

In FY2023, interest rates in the JGB market trended upward due to revisions to the BOJ's monetary policy and trends in overseas markets.

In March 2023, domestic interest rates declined as concerns about the financial system intensified, particularly in the U.S., and U.S. interest rates fell due to recession fears. Subsequently, from April to mid-July, domestic interest rates generally remained stable as the BOJ maintained its previous monetary policy framework at the Monetary Policy Meetings held in April and June, although there were some temporary rises in domestic interest rates in tandem with rising U.S. interest rates on the back of the expectations of additional interest rates hikes by the Federal Reserve Board and the U.S. debt ceiling issue.

In late July, in order to enhance the sustainability of monetary easing, the BOJ decided to conduct its yield curve control with greater flexibility, such as by keeping the fluctuation range for 10-year JGB yields at "around ±0.5%" while regarding the range as a reference, not as rigid limits, and by raising the yield level of its 10-year JGB fixed-rate purchase operations to 1.0%. As a result of these actions, domestic interest rates rose.

Fig. 1-1 JGB Yield Trends by Maturity

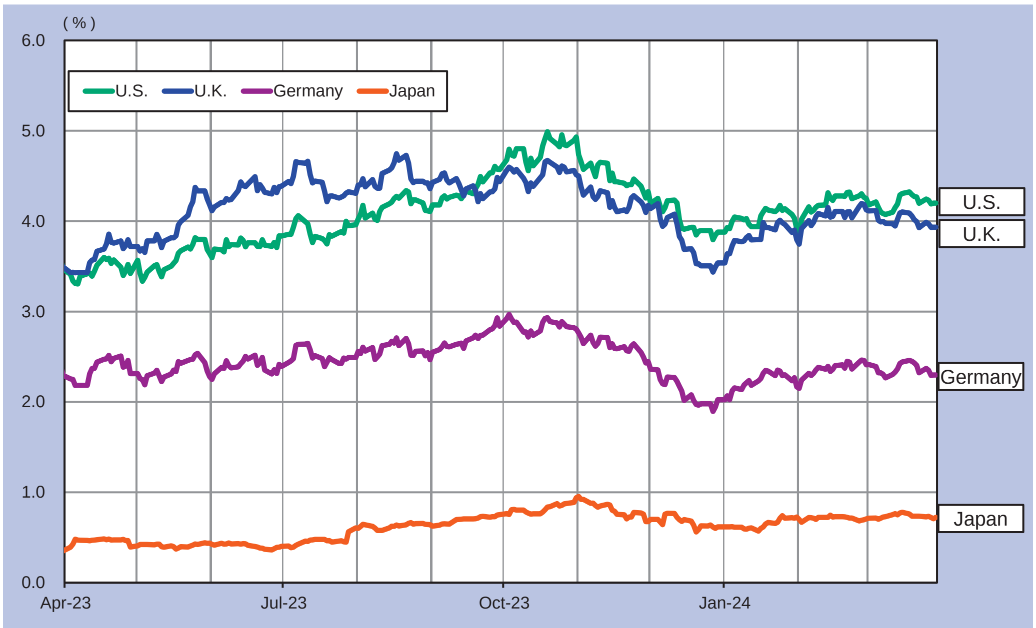


From August to October, domestic interest rates increased in tandem with rising U.S. interest rates because of persistently high U.S. inflation. Additionally, in late October, the BOJ further increased the flexibility in the conduct of its yield curve control by regarding the upper bound of 1.0% for 10-year JGB yields as a reference in its market operation. Therefore domestic interest rates rose, and in early November, 10-year JGB yields temporarily reached a record high of 0.97% since May 2013.

However, from early November, domestic interest rates trended lower as U.S. interest rates fell mainly due to the slowed growth in U.S. inflation and increased speculation that the Federal Reserve Board would cease interest rate hikes. In early December, there was a growing view that the BOJ would end its negative interest rate policy, and interest rates rose at times. However, in late December interest rates declined after the BOJ decided to maintain its current stance on monetary policy operations.

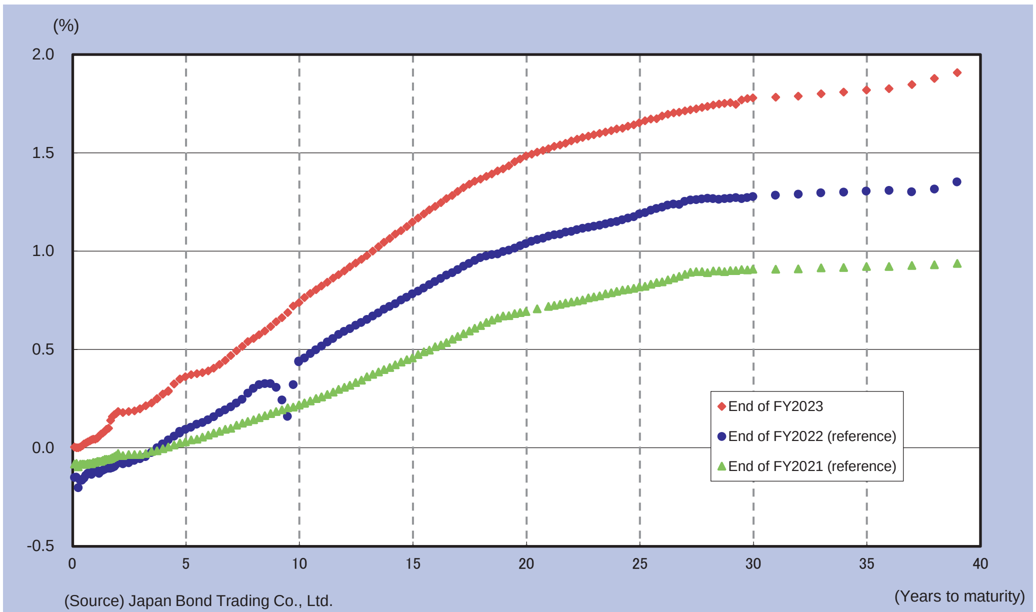
Although the BOJ also decided to maintain its current stance on monetary policy operations in late January 2024,

Fig. 1-2 Changes in 10-Year Government Bonds Yields



Note: Figures may not match other figures from different sources.
(Source) Bloomberg

Fig. 1-3 Changes in Yield Curve



(Source) Japan Bond Trading Co., Ltd.

interest rates rose as the market became aware of the possibility of BOJ's policy normalization in the near future.

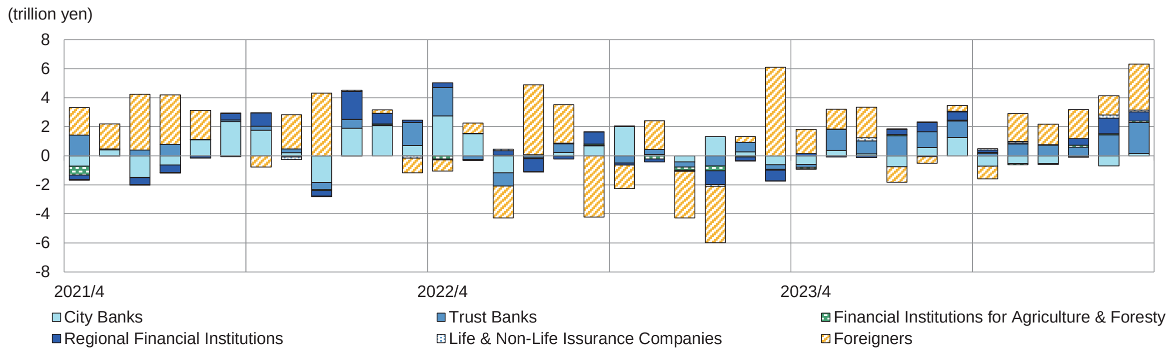
In mid-March, the BOJ decided to revise its monetary policy framework. The BOJ ended its negative interest rate policy by applying an interest rate of 0.1% to current account balances held by financial institutions at the Bank (excluding required reserve balances), and terminated the yield curve control framework. However, these changes in the BOJ's monetary policy framework had already been incorporated into the market to some extent, and interest rates did not fluctuate significantly.

(2) Investor Trends

Looking at investment trends in JGBs by investor category in FY2023, a wide range of investors, including foreign investors, pension funds, regional financial institutions, and others were net buyers of medium-to-long-term bonds (2-Year Bonds, 5-Year Bonds, and 10-Year Bonds (☞)). From April to June, both foreign and domestic investors made net purchases of the JGBs against the backdrop of the BOJ maintaining its monetary policy framework. In July, foreign investors and city banks were net sellers as expectations of revisions to the BOJ's monetary policy increased, while regional financial institutions were net buyers in light of higher interest rate levels. Additionally, pensions funds are presumed to have been large net buyers of the JGBs because it is assumed that they sold foreign assets and then purchased domestic bonds in order to adjust their investment portfolios as the yen had been depreciating and valuations on foreign assets had been rising since the beginning of the year. From August to September, domestic investors are thought to have favored the high interest rate levels and made net purchases of the JGBs as domestic interest rates rose in response to the BOJ's decision to conduct its yield curve control with greater flexibility at the end of July and the rise in U.S. interest rates. In October, foreign investors and city banks were net sellers of the JGBs, and the other investors' net buying also decreased as the market had stronger expectations of future interest rate hikes based on the view that the BOJ would further enhance the flexibility of its yield curve control. From November, foreign and domestic investors were net buyers of the JGBs as the expectations of higher interest rates waned against the backdrop of domestic interest rates falling in tandem with U.S. interest rates. From February, pension funds are thought to have sold domestic stocks and purchased domestic bonds to adjust their investment portfolios in response to the rise in domestic stock valuations caused by rising stock prices. In March, although the BOJ decided to revise its monetary policy framework, a wide range of investors were net buyers of the JGBs, buoyed by the Bank's decision to continue its JGB purchases with broadly the same amount as before.

☞ 5-Year Bonds include Japan Climate Transition Bonds, and 10-Year Bonds include Japan Climate Transition Bonds and Inflation-Indexed Bonds.

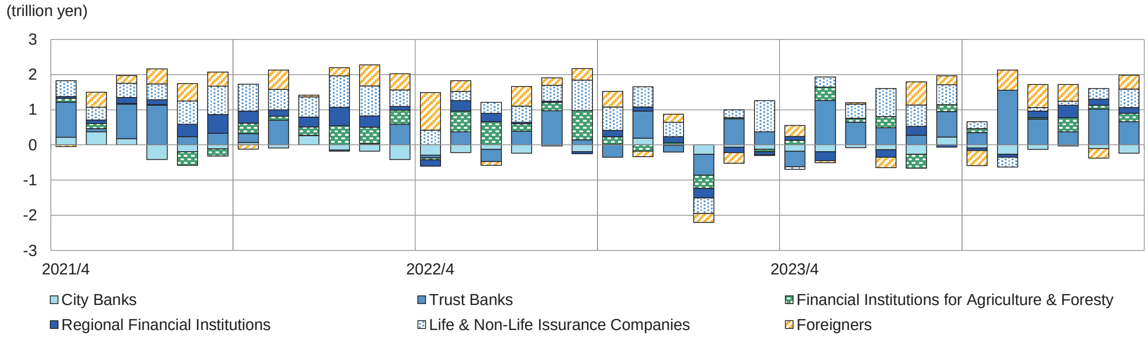
Fig. 1-4 Net Buying/Selling of Medium-to-Long-Term JGBs by Investor Category



Note: Medium-to-long-term JGBs are 2-Year, 5-Year and 10-Year JGBs. Investors' direct purchases through auctions are excluded. Trust Banks' trading covers their proprietary trading as well as transactions on behalf of pension funds, etc. "Regional Financial Institutions" includes Shinkin Banks.
(Source) Japan Securities Dealers Association

Next, ultra-long-term bonds (20-Year Bonds, 30-Year Bonds, and 40-Year Bonds) were bought by a wide range of investors, including pension funds, life insurance companies, and financial institutions for Agricultural and Forestry. In particular, pension funds were likely large net buyers of ultra-long-term bonds as well as medium- to long-term bonds in response to the weakening yen and rising stock prices throughout the fiscal year. Life insurance companies, as in the previous fiscal year, are also thought to have made net purchases of ultra-long-term bonds due to their need to increase purchases of the JGBs in order to comply with the Insurance Capital Standard, which will be introduced in the near future.

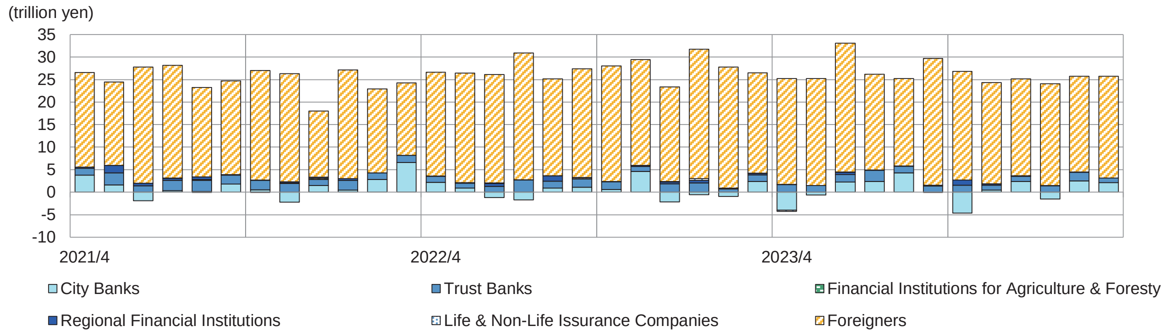
Fig. 1-5 Net Buying/Selling of Ultra-Long-Term JGBs by Investor Category



Note: Ultra-long-term JGBs are 20-Year, 30-Year and 40-Year JGBs. Investors' direct purchases through auctions are excluded. Trust Banks' trading covers their proprietary trading as well as transactions on behalf of pension funds, etc. "Regional Financial Institutions" includes Shinkin Banks.
(Source) Japan Securities Dealers Association

Foreign investors continued to be the largest buyers of short-term JGBs (Treasury Discount Bills). This is mainly because of the continued availability of premiums to dollar providers in the currency basis swap market.

Fig. 1-6 Net Buying/Selling of Short-Term JGBs by Investor Category



Note: Short-term JGBs are T-Bills. Investors' direct purchases through auctions are excluded. Trust Banks' trading covers their proprietary trading as well as transactions on behalf of pension funds, etc. "Regional Financial Institutions" includes Shinkin Banks.
(Source) Japan Securities Dealers Association