

## Outlook for 20Y JGB Auction

### Decent primary sale expected for JL173 tap, but the auction may have a longer tail than it did in August

- ✓ We think about our bidding stance, expecting that the 20Y JGB yield will remain at the 0.40-0.45% level for a while, with the anomaly of the 20Y JGB yield seen in September-October under the YCC in mind.
- ✓ A 20Y JGB auction generally goes smoothly, and so would do this auction. But it may have a longer tail than it did in August.
- ✓ In terms of relative value, it would be worth considering buying asset swaps.

Strategic Memorandum DSTE402  
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### Auction Details

**Auction Date:** September 10, 2020  
**Issue Date:** September 11, 2020  
**Maturity Date:** June 20, 2040  
**Offering Amount:** About 1.2 trillion yen

\* New 20Y JGBs will be the last reopening of JL173 carrying a 0.4% coupon.

\*\* On September 9, JL173 traded at 0.405% (-1.0bp v. previous day's close) and closed at 0.405% (-1.0bp).

### Exp. Rating on Auction Results

1	2	3	4	5
Failed	Poor	Average	Good	Outstanding

### Mostly moving at the 0.405-0.440% level since previous auction

The previous 20Y JGB auction was held at the 0.405-0.410% level (-0.5bp - unchanged vs. previous day's close) and went well with the lowest accepted price of 99.90 yen (0.405%) vs. surveyed cut-off price range of 99.75-99.80 yen (0.410-0.413%). After the auction, the 20Y JGB yield momentarily declined to 0.395% during intraday trading. Since then, the yield has been moving at the 0.405-0.440% level. As of 14:00 today (Sep 9), JL173 is quoted at 0.405% (-1.0bp vs. previous day's close)/0.410% (-0.5bp) with no major trades.

### Even under new administration, the top priority should be to measures to cope with pandemic; major policy shift is unlikely

We look at the conditions surrounding the JGB market. Excessive concern over the economy appears to be receding in the US, but in Europe, anxiety appears strong over the direction of the European economy, in part because of the second wave of virus infections. Although there are heightening expectations for the practical use of COVID-19 vaccines in the immediate future, it remains difficult to be optimistic about the future path of economic activity. Even the US lacks progress in discussions over a new pandemic relief package to replace the one that has already expired. In Japan, the process of preparing for a new administration has started since Prime Minister Abe announced to resign. With yesterday's public notification of the LDP presidential election scheduled for September 14, 3 declared candidates will fight for the chief position. Among them, Chief Cabinet Secretary Yoshihide Suga appears to be the closest to the presidential seat at the moment. Under this assumption, current fiscal/monetary policies will likely be maintained with a high probability

amid the pandemic. In such a situation, we summarize key points to think about the bidding stance at tomorrow's auction as follows:

- ✓ **Solid demand expected from investors above 0.4%:** Demand from investors for 20Y JGBs sold under par appears strong. Although we need to carefully watch the demand level, decent support is expected for tomorrow's auction;
- ✓ **Not cheap in terms of the relative value:** Our analysis based on data since the previous 20Y JGB auction and that during the past three months shows that the 20Y sector is not noticeably cheap on the intermediate to superlong zone of the curve (Appendix 3). Rather, it is not advantageous to build new positions by buying the 20Y sector partly as it is noticeably overvalued vs. the 30Y sector (Appendix 3). Since the previous auction, the 20Y asset swap spread had widened, but it has recently been tightening. We can say that 20Y cash is neither especially undervalued nor overvalued against swaps at the current level (Appendix 6);
- ✓ **The 20Y JGB yield tends to rise in September-October:** As an anomaly, an upward tendency of the 20Y JGB yield in September-October appears strong under the BOJ's yield curve control (YCC) policy (see table below). We have to be cautious about this tendency in FY20, given the relatively small purchase amount by the BOJ vs. the largest issuance amount of 20Y JGBs.

#### Anomaly of 20Y JGB Yield

	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar
Average*	-4.6	-3.5	-5.8	3.0	0.7	6.4	1.6	0.3	1.4	0.1	-4.4	1.5
FY2020	-0.7	4.9	5.8	-2.9	3.9							
FY2019	3.6	-7.8	-6.9	-2.2	-15.5	15.0	3.0	2.5	2.4	-4.4	-7.9	15.7
FY2018	0.5	-2.4	-0.9	3.3	8.5	3.3	0.1	-5.7	-9.2	-5.1	-2.5	-8.8
FY2017	-7.7	1.0	2.4	-0.5	-4.8	3.9	1.4	-2.4	0.0	1.9	-4.3	-1.9
FY2016	-14.6	-4.9	-17.8	11.5	14.6	3.3	2.0	6.8	12.4	8.0	-2.8	1.0

Note: end-month to month change in bp \* FY2016 to FY2019 average  
 Source: Daiwa Securities.

**We think about our bidding stance, expecting that yield will remain at 0.40-0.45% level for a while**

All in all, we would like to think about our bidding stance, expecting the 20Y JGB yield to move in the 0.40-0.45% level for a while. A 20Y JGB auction generally goes smoothly, and so would do this auction. But it may have a longer tail than it did in August. In terms of the relative value, it is difficult to take an aggressive stance, but it would be worth considering buying asset swaps. Positive carry is expected, and the tightening from the current level may be limited partly because of the widening trend in the US superlong zone (30Y, Appendix 5). It may work better in a slightly long-term investment horizon with the target set at the 6M Yen LIBOR+10-15bp level (Appendix 6a).

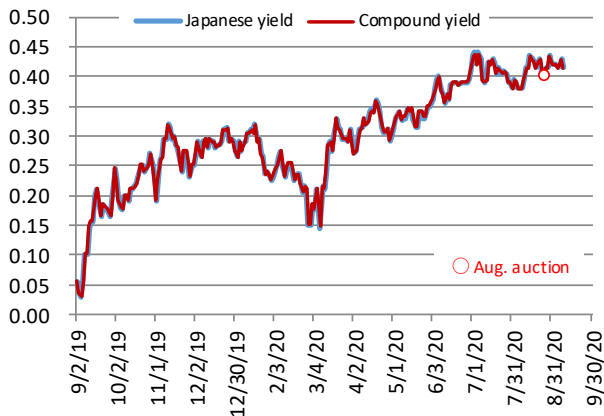
## 20Y JGB Auction Results

Auction Date	Issue #	Coupon (%)	Maturity Date	Issue Size (billion yen)	B/C	Average Accepted Price (Yen)	Lowest Accepted Price (Yen)	Tail (Yen)	Average Accepted Yield (%)	Highest Accepted Yield (%)	Tail (%)	Allotment (%)	Rating
9/10/20	173R	0.4	6/20/40	1,200*									
8/25/20	173R	0.4	6/20/40	1,316.2	3.92	99.94	99.90	0.04	0.403	0.405	0.002	67.8187	Good
7/21/20	173	0.4	6/20/40	1,313.4	3.80	99.70	99.65	0.05	0.416	0.419	0.003	28.5714	Good
6/26/20	172R	0.4	3/20/40	977.7	3.87	100.24	100.20	0.04	0.386	0.389	0.003	59.9036	Good
5/20/20	172R	0.4	3/20/40	957.3	4.25	101.26	101.20	0.06	0.332	0.335	0.003	36.3983	Good
4/21/20	172	0.4	3/20/40	899.4	3.58	101.21	101.10	0.11	0.335	0.340	0.005	16.5349	Avg
3/12/20	171R	0.3	12/20/39	963.5	3.69	100.98	100.90	0.08	0.248	0.252	0.004	97.2897	Good
2/20/20	171R	0.3	12/20/39	969.8	3.99	101.27	101.25	0.02	0.232	0.234	0.002	81.9560	Good
1/17/20	171	0.3	12/20/39	899.1	3.83	99.99	99.90	0.09	0.300	0.305	0.005	93.4722	Good
12/17/19	170R	0.3	9/20/39	1,027.5	4.10	100.25	100.20	0.05	0.286	0.289	0.003	30.5611	Good
11/20/19	170R	0.3	9/20/39	1,032.8	4.21	100.63	100.60	0.03	0.266	0.268	0.002	43.6701	Good
10/24/19	170	0.3	9/20/39	899.3	3.91	101.04	100.95	0.09	0.245	0.249	0.004	57.2532	Avg
9/18/19	169R	0.3	6/20/39	949.3	3.48	101.79	101.70	0.09	0.205	0.210	0.005	20.3703	Good
8/20/19	169R	0.3	6/20/39	1,018.7	3.81	103.67	103.60	0.07	0.110	0.114	0.004	32.8061	Avg

\* Amount the Ministry of Finance plans to issue

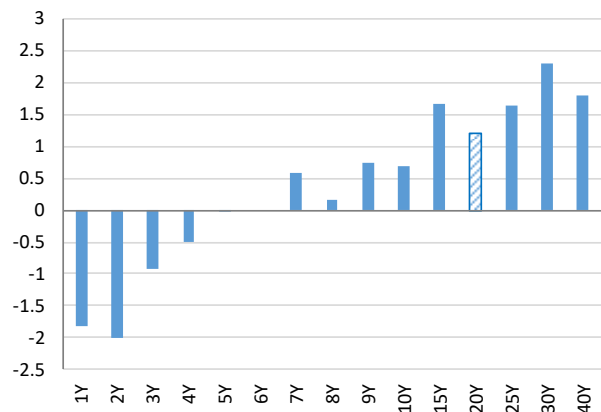
Source: Ministry of Finance (MOF), Daiwa Securities.

## Appendix 1: 20Y JGB Yield (%)



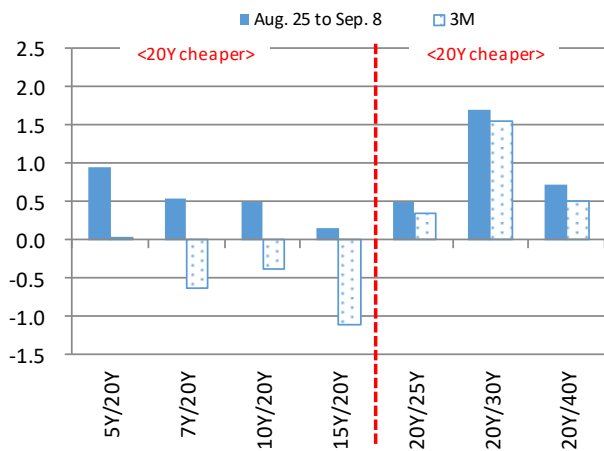
Source: Daiwa Securities.

## Appendix 2: JGB Yield Change (bp): Aug. 25 v. Sep. 8



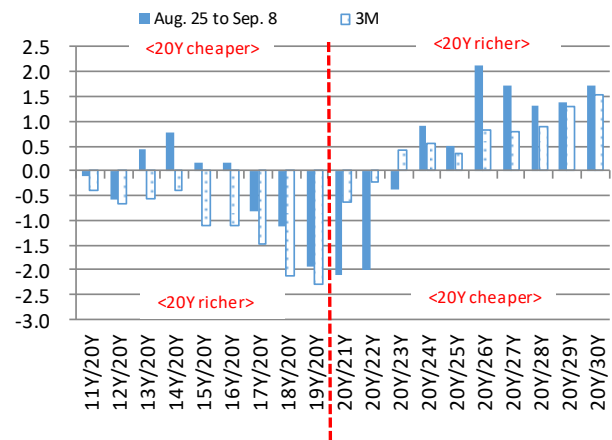
Source: Daiwa Securities.

## Appendix 3a: Z-score I

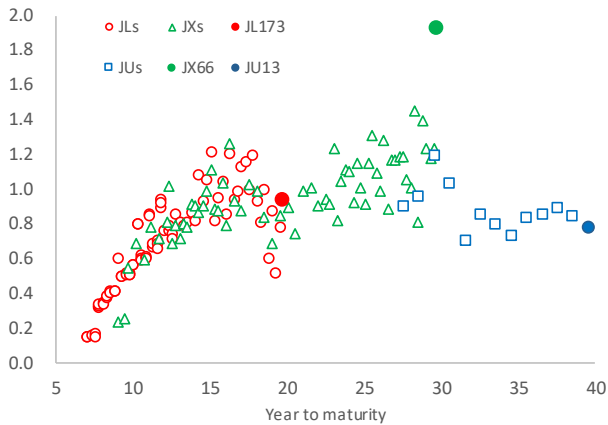


Source: Daiwa Securities.

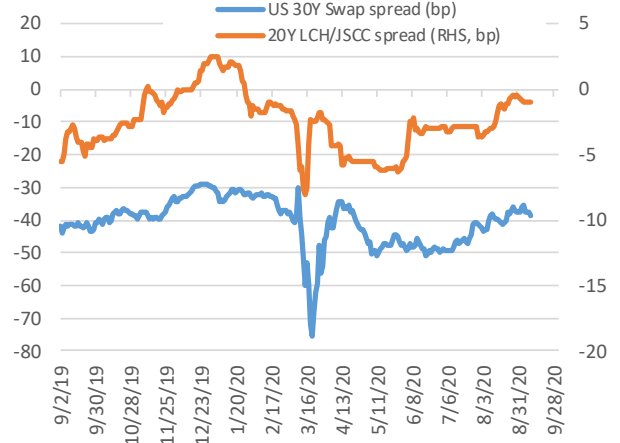
## Appendix 3b: Z-score II



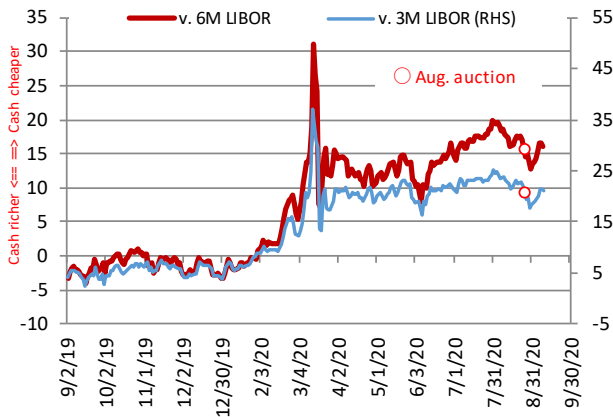
Source: Daiwa Securities.

**Appendix 4: J JGB Total Return Curve (3M, %)**


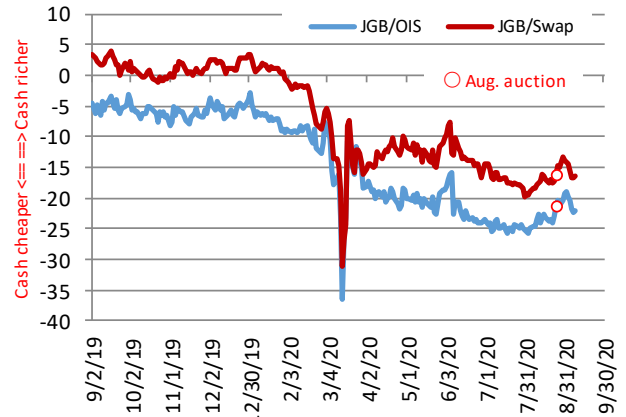
Note: Based on the Sep-8 JGB yield curve; factoring in roll-down effect etc.  
 Source: Daiwa Securities.

**Appendix 5: US Swap Spread and 20Y LCH/JSCC Spread**


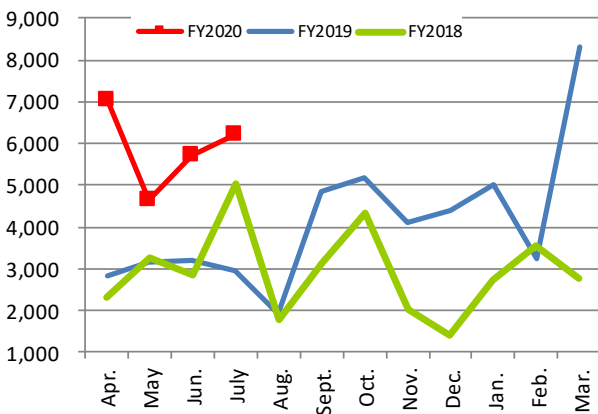
Source: Bloomberg.

**Appendix 6a: 20Y JGB Asset Swap Spread (bp)**


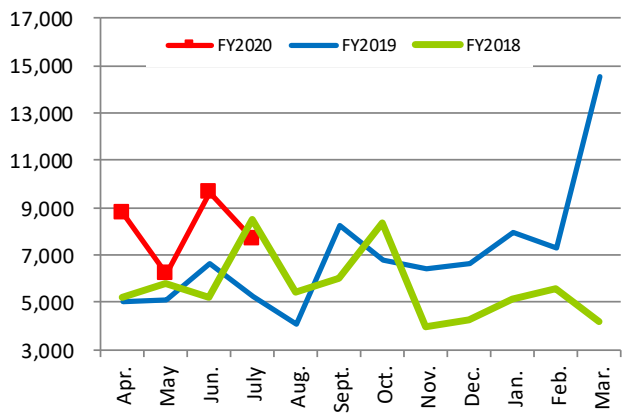
Source: Daiwa Securities.

**Appendix 6b: 20Y JGB/Swap and JGB/OIS Spreads (bp)**


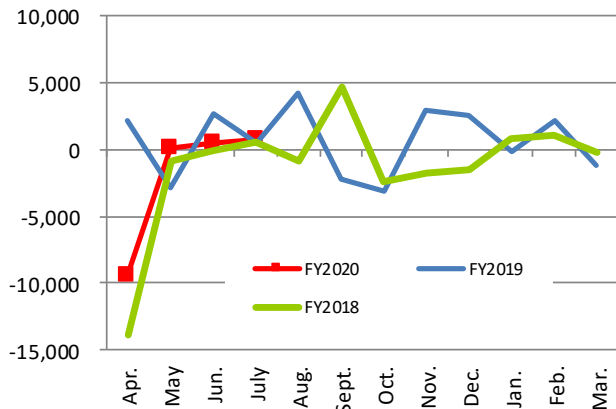
Source: Daiwa Securities.

**Appendix 7a: Trend of Life and Non-life Insurers' Net Purchase of Superlong JGBs (Yen 100M)**


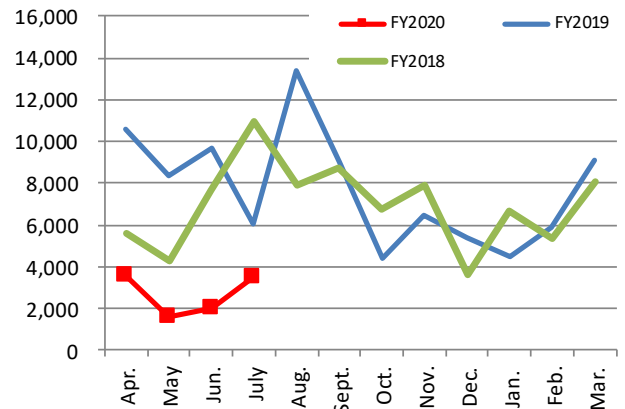
Source: JSDA

**Appendix 7b: Trend of Life and Non-life Insurers' Gross Purchase of Superlong JGBs (Yen 100M)**


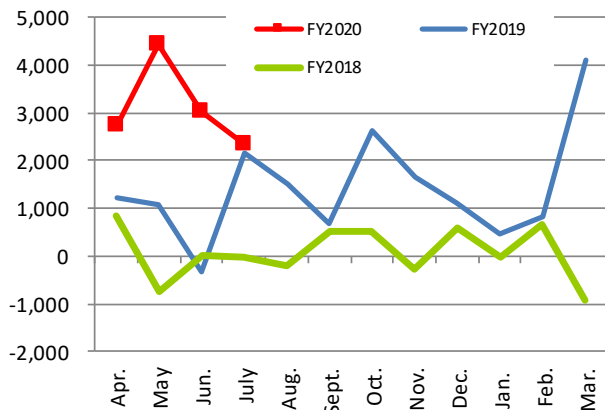
Source: JSDA

**Appendix 8a: Trend of Major Banks' Net Purchase of Superlong JGBs (Yen 100M)**


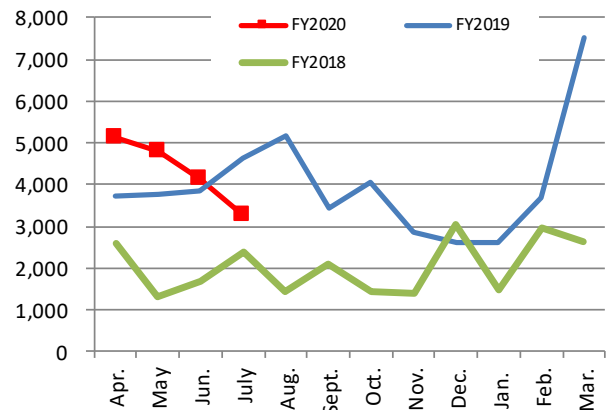
Source: JSDA

**Appendix 8b: Trend of Major Banks' Gross Purchase of Superlong JGBs (Yen 100M)**


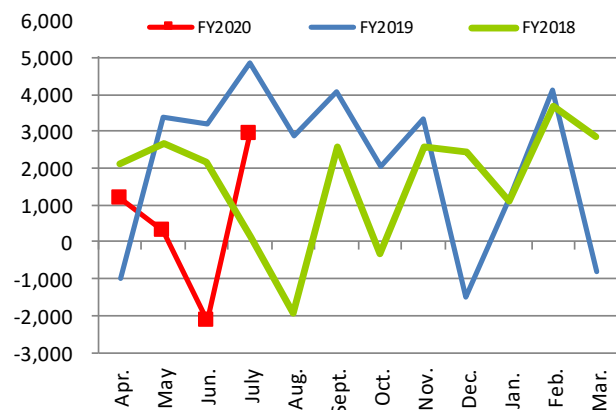
Source: JSDA

**Appendix 9a: Trend of Regional Banks' Net Purchase of Superlong JGBs (Yen 100M)**


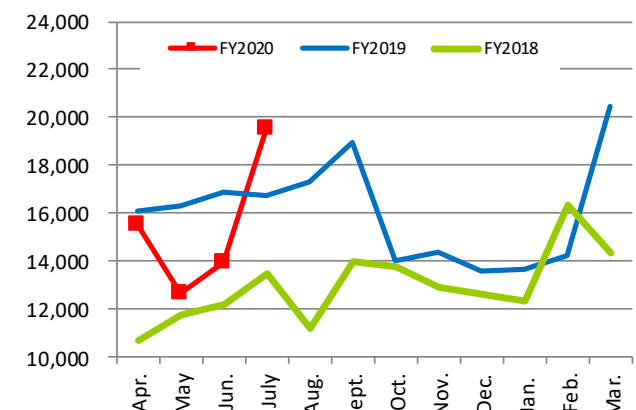
Source: JSDA

**Appendix 8b: Trend of Regional Banks' Gross Purchase of Superlong JGBs (Yen 100M)**


Source: JSDA

**Appendix 10a: Trend of Overseas Accounts' Net Purchase of Superlong JGBs (Yen 100M)**


Source: JSDA

**Appendix 10b: Trend of Overseas Accounts' Gross Purchase of Superlong JGBs (Yen 100M)**


Source: JSDA

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February 2020

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2) Daiwa Real Estate Asset Management is a subsidiary of Daiwa Securities Group Inc. and serves as the asset management company for the following J-REITS: Daiwa Office Investment Corporation (8976), Nippon Healthcare Investment Corporation (3308), Japan Rental Housing Investments (8986).

3) Samty Residential Investment became a consolidated subsidiary of Daiwa Securities Group Inc. effective 10 September 2019.

4) On 30 May 2019, Daiwa Securities Group Inc. formalized an equity/business alliance with Samty, and as of 14 June 2019 it owned 16.95% of shares outstanding in Samty along with convertible bonds with a par value of ¥10bn. Conversion of all of said convertible bonds into common shares would bring the stake of Daiwa Securities Group Inc. in Samty to 27.28%.

5) Daiwa Securities Group Inc. and Credit Saison Co., Ltd. entered into a capital and business alliance, effective 5 September 2019. In line with this alliance, Daiwa Securities Group Inc. is to acquire up to 5.01% of Credit Saison's total common shares outstanding (excl. treasury shares; as of 31 Jul 2019).

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- There may be a difference between bid price etc. and ask price etc. of OTC derivatives handled by our company.
- Before engaging in any trading, please thoroughly confirm accounting and tax treatments regarding your trading in financial instruments with such experts as certified public accountants.

\* The amount of the trading commission cannot be stated here in advance because it will be determined between our company and you based on current market conditions and the content of each transaction etc.

\*\* The ratio of margin requirements etc. to the amount of the transaction cannot be stated here in advance because it will be determined between our company and you based on current market conditions and the content of each transaction etc.

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