

Daiwa's View

Theme that changed during Golden Week holidays

➤ Warning against excessive risk-taking

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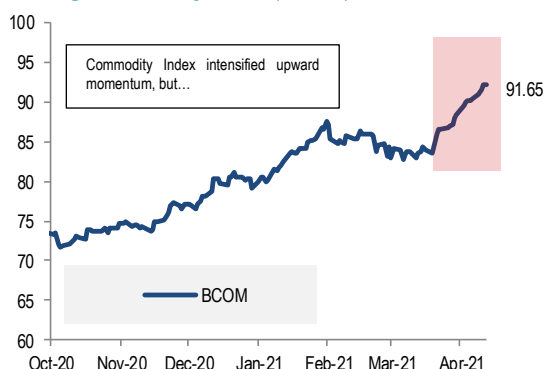
Daiwa Securities Co. Ltd.

Warning against
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Theme that changed during Golden Week holidays

In the global market, high-tech issues were bearish and commodities continued to advance during the Golden Week holidays in Japan. That said, the 5-year forward 5-year inflation expectations (BEI) was stable at around 2.2-2.3%. At this point, higher commodity prices do not appear to be directly leading to speculation that the uptrend will boost long-term inflation expectations. The 10-year US Treasury yield rose slightly from time to time, reflecting remarks by Dallas Fed president Robert Kaplan and Treasury Secretary Janet Yellen as well as [quarterly refunding](#) (no cut in 20-year bonds). However, the yield stayed at around 1.6% for most of the period, eventually closing at about 1.57%.

Bloomberg Commodity Index (BCOM)



Source: Bloomberg; compiled by Daiwa Securities.

5Y-forward 5Y US Breakeven Inflation Rate (BEI)



Source: Bloomberg; compiled by Daiwa Securities.

◆ Warning against excessive risk-taking?

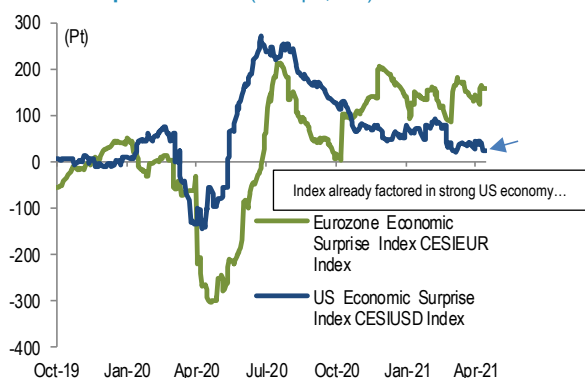
A noteworthy change during the Golden Week holidays was seen in the tone of remarks regarding risk-taking. As previously reported, Fed chair Jerome Powell stated in the post-FOMC press conference that "some of the asset prices are high. You are seeing things in a capital markets that are a bit frothy." Following this, Dallas Fed president Robert Kaplan said on 30 April that "We are now at a point where I'm observing excesses and imbalances in financial markets," recognizing that "at the earliest opportunity, I think it would be appropriate for us to start talking about adjusting those (asset) purchases." It is a well-known fact that Kaplan has recently been leaning toward a hawkish stance. However, the in-depth remark on the excesses and imbalances in financial markets somewhat surprised us.

The change in the tone would not be the only reason, but recently, US yields have not risen straightforwardly on the announcement of strong economic indicators. In addition, it appears to have become more difficult for such yield trends to serve as a support for higher US stock prices. The US Economic Surprise Index has already factored in strong indicators, representing a rise in the surprise hurdle. Of course, the absolute level of economic indicators is still strong. However, if it is becoming difficult for even such strong indicators to

create positive surprises, we can say that the foundation for future negative surprises has been established.

Given the fact that Powell referred to “froth,” we should brace for central banks not to stop moves toward the exit if indicators and asset prices soften slightly, although it would be overdoing it to talk of “bubble popping.” This potential shift in stance weighs on risk asset prices. Meanwhile, [we can still interpret](#) the failure of yields to rise despite strong economic indicators as a reactionary move following the excessive rise led by the term premium.

Economic Surprise Indices (Europe, US)



Source: Bloomberg; compiled by Daiwa Securities.

10Y US Treasury Term Premium



Source: Bloomberg; compiled by Daiwa Securities.

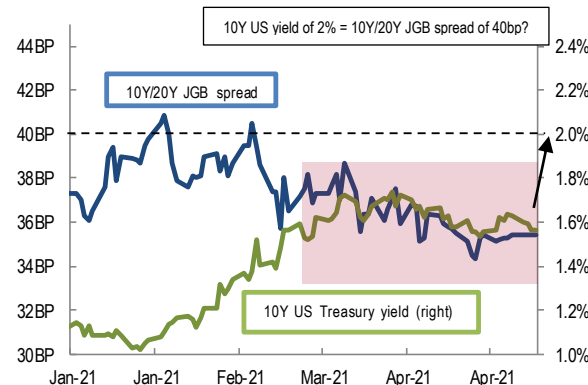
◆ Not much hope for near-term dip in 20-year JGBs

JGBs are influenced by this change in the tone of the Fed's view of asset prices and by the stability of the 10-year US Treasury yield. In particular, the JGB market has recently been demonstrating a clear recovery of the correlation between the 10-year/20-year JGB yield spread and the 10-year US Treasury yield (charts below). The impact of stable US yields appears to be reasonably strong. If we assume that this balance will continue for the time being, the 10-year/20-year JGB yield spread is unlikely to widen beyond around 40bp even if the 10-year US Treasury yield rises to 2%. And even if a dip does form in response to specific factors, such as expectations for the formulation of a supplementary budget in line with an extension of the declaration of the state of emergency, we should keep in mind the possibility that the aforementioned balance may blunt the rise in JGB yields.

10Y US Treasury Yield, 10Y/20Y JGB Yield Spread



Source: Bloomberg; compiled by Daiwa Securities.



Source: Bloomberg; compiled by Daiwa Securities.

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■ Credit Rating Agencies

[Standard & Poor's]

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[Moody's]

The Name of the Credit Rating Agencies Group, etc

The name of the Credit Rating Agencies group: Moody's Investors Service ("MIS")

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[Fitch]

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Daiwa Securities Co. Ltd. and Daiwa Securities Group Inc.: Daiwa Securities Co. Ltd. is a subsidiary of Daiwa Securities Group Inc.

Other Disclosures Concerning Individual Issues:

1) As of 26 April 2016, Daiwa Securities Co. Ltd., its parent company Daiwa Securities Group Inc., GMO Financial Holdings, Inc., and its subsidiary GMO CLICK Securities, Inc. concluded a basic agreement for the establishment of a business alliance between the four companies.

As of end-December 2017, Daiwa Securities Group Inc. owned shares in GMO Financial Holdings, Inc. equivalent to approximately 9.3% of the latter's outstanding shares. Given future developments in and benefits from the prospective business alliance, Daiwa Securities Group Inc. could boost its stake in GMO Financial Holdings, Inc. to up to 20% of outstanding shares.

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), Daiwa Securities Living Investment Corporation (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).

Notification items pursuant to Article 37 of the Financial Instruments and Exchange Law

(This Notification is only applicable to where report is distributed by Daiwa Securities Co. Ltd.)

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- In addition to the purchase price of a financial instrument, our company will collect a trading commission* for each transaction as agreed beforehand with you. Since commissions may be included in the purchase price or may not be charged for certain transactions, we recommend that you confirm the commission for each transaction. In some cases, our company also may charge a maximum of ¥2 million per year as a standing proxy fee for our deposit of your securities, if you are a non-resident.
- For derivative and margin transactions etc., our company may require collateral or margin requirements in accordance with an agreement made beforehand with you. Ordinarily in such cases, the amount of the transaction will be in excess of the required collateral or margin requirements**.
- There is a risk that you will incur losses on your transactions due to changes in the market price of financial instruments based on fluctuations in interest rates, exchange rates, stock prices, real estate prices, commodity prices, and others. In addition, depending on the content of the transaction, the loss could exceed the amount of the collateral or margin requirements.
- 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.

When making an actual transaction, please be sure to carefully read the materials presented to you prior to the execution of agreement, and to take responsibility for your own decisions regarding the signing of the agreement with our company.

Corporate Name: Daiwa Securities Co. Ltd.

Registered: Financial Instruments Business Operator, Chief of Kanto Local Finance Bureau (Kin-sho) No.108

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