

Daiwa's View

20-year JGB auction: Little concern about the auction itself

- Keep in mind the possibility of limited upside in secondary market

Fixed Income Research Section
FICC Research Dept.

Strategist
Kazuya Sato
(81) 3 5555-8773
kazuya.sato@daiwa.co.jp



Daiwa Securities Co. Ltd.

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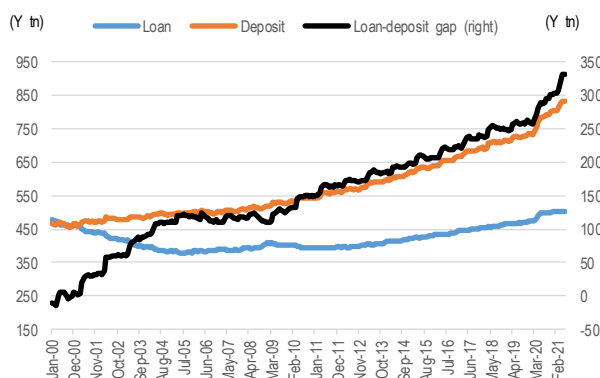
20-year JGB auction: Little concern about the auction itself

20-year JGBs are to be auctioned on Tuesday, 13 July. The scheduled maturity date is 20 June 2041, and the planned issuance amount is around Y1.2tn, the same as in the previous auction. This time, new 20-year JGBs will be issued in a new maturity basket (JL177). In terms of the current level, the coupon is expected to be set at 0.4%. As of 15:00 on 9 July, the yield of the on-the-run JL176 closed at 0.415% on a conventional basis (up 1.0bp vs. previous day's close).

In the recent bond market, the favorable results of the 10-year JGB auction (held on 1 Jul) led to a gain of JL176 alongside superlong JGBs. In the US, with the weaker-than-expected ISM services index being associated with the peaking of the economy, yields declined tremendously. For three days during 6-8 July, the 10-year US Treasury yield slid by around 13bp. Affected by this, yields declined further in the JGB market also, driven by futures. Due to this, tomorrow's auction is expected to be held at a slightly lower yield level than the previous auction. We consider key points about tomorrow's auction under the current circumstances.

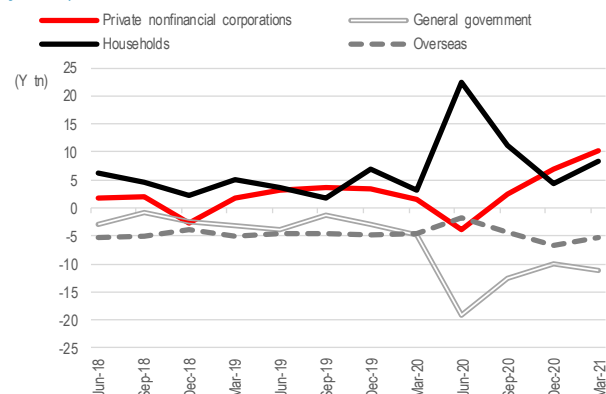
Excess money at depository institutions has been garnering attention recently. [The Principal Figures of Financial Institutions](#) shows that excess money increased further as of June (left-hand chart below). In this regard, trends with the loan-deposit gap since autumn can be given as a key point in bond investment. According to [the Flow of Funds](#) for Jan-Mar 2021 (released on 25 Jun), we can confirm that financial surpluses in the household and corporate sectors expanded on a flow basis (right-hand chart below).

Loan-deposit Gap at Major Banks and Regional Banks



Source: BOJ; compiled by Daiwa Securities.

Financial Surplus and Deficit by Sector (flow basis, seasonally adjusted)



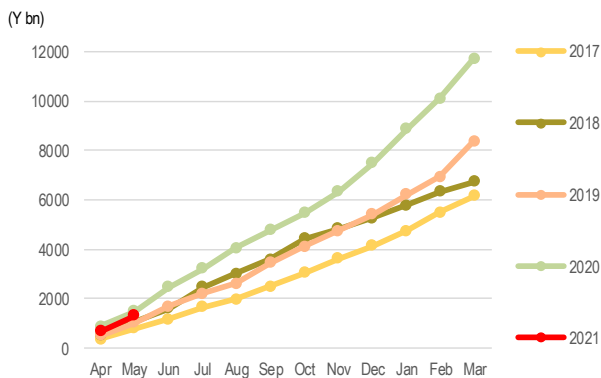
Source: BOJ; compiled by Daiwa Securities.

If companies implement the vigorous capex plans indicated in the BOJ's June Tankan thanks to a recovery of household consumption in line with economic normalization amid progress with vaccinations, deposits in the corporate sector will be withdrawn. This is likely to narrow the loan-deposit gap. Regarding households, however, a decline in supply of services in line with the declaration of a fourth state of emergency starting today (with shorter operating hours and store closures) could contain growth of demand.

The USD/JPY currency basis, which has an impact on the stance of overseas investors, has been widening recently (next page). If purchases by overseas investors concentrate on intermediate/long-term bonds alongside the expansion of the dollar-funding premium, this will indirectly put downward pressure on the 20-year yield on the curve.

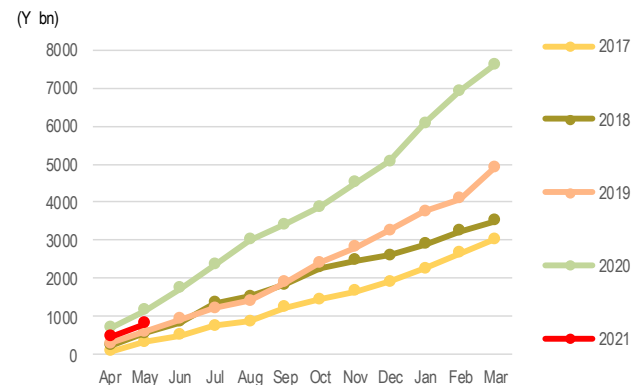
Regarding life/nonlife insurers, growth of purchases of superlong JGBs since the start of FY21 appears to be limited. In light of this, the favorable results of last week's 30-year JGB auction allow us to forecast that these purchases will pick up going forward.

Cumulative Purchases of Superlong JGBs by Life- and Non-life Insurers (gross)



Source: Japan Securities Dealers Association (JSDA); compiled by Daiwa Securities.

Cumulative Purchases of Superlong JGBs by Life- and Non-life Insurers (net)



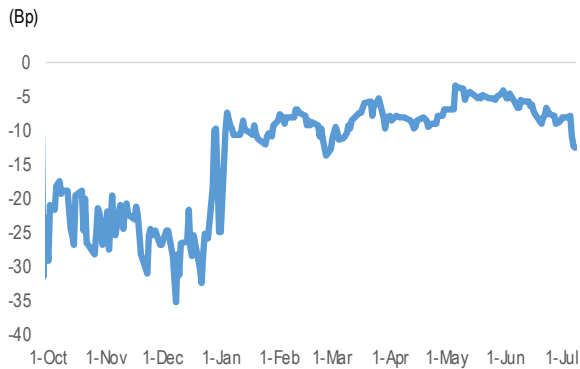
Source: JSDA; compiled by Daiwa Securities.

As risk factors, we can point out the comparatively high cost of 20-year JGBs on the curve vs. 30-year and 40-year JGBs, as well as concerns about the issuance of additional JGBs in line with expansion of a supplementary budget, similar to the previous auction. In particular, regarding the size of the extra budget, which determines the issuance size, LDP Secretary-General Toshihiro Nikai made positive comments regarding the compilation of a budget worth around Y30tn following the significant setback of ruling parties in the Tokyo Metropolitan Assembly election. However, it is unclear whether the figure indicates the amount for all projects, making it difficult to factor it in at this time.

If tomorrow's auction is held at a slightly lower yield level than the previous auction, we won't be very concerned. This is because (1) new 20-year JGBs will belong to a new maturity basket and (2) they will be sold under par at the auction if the coupon is set at 0.4%. Recent bearish trends with risk assets and substantial widening of the 20-year swap spread (next page) are also likely to support tomorrow's auction.

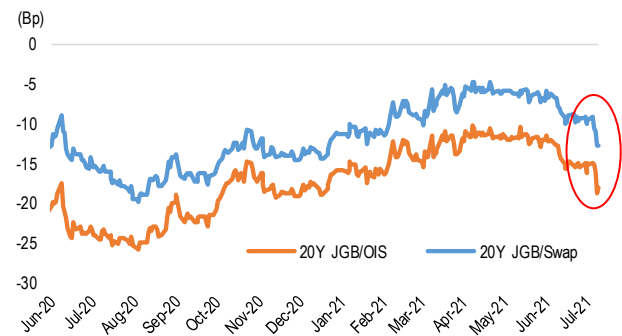
However, we think that the recent decline in US yields is [excessive](#). In fact, at the end of last week, the 10-year US Treasury yield bounced back by 6.7bp in the overseas market. At tomorrow's auction, we would like to keep in mind the possibility of limited upside in the secondary market.

USD/JPY Currency Basis (3M)



Source: Bloomberg; compiled by Daiwa Securities.

Swap Spread (20-year JGB/OIS. JGB/Swap)



Source: Bloomberg; compiled by Daiwa Securities.
Note: Based on generic yields.

20-year JGB Auction Results

Auction date	Issue #	Maturity date	Coupon (%)	Issuance amount (Y bn)	Bid-to-cover ratio (X)	Average accepted yield (%)	Highest accepted yield (%)	Tail (Y)	Allotment
13-Jul-21	177	20-Jun-41	0.40**	1,200*					
24-Jun-21	176R	20-Mar-41	0.50	1,207	3.62	0.433	0.436	0.06	31.1%
21-May-21	176R	20-Mar-41	0.50	1,219	3.48	0.445	0.450	0.10	37.5%
20-Apr-21	176	20-Mar-41	0.50	1,225	3.34	0.438	0.439	0.02	79.6%
11-Mar-21	175R	20-Dec-40	0.50	1,300	3.40	0.513	0.519	0.10	33.2%
18-Feb-21	175R	20-Dec-40	0.50	1,273	3.13	0.482	0.488	0.11	47.0%
18-Jan-21	175	20-Dec-40	0.50	1,209	3.35	0.443	0.448	0.09	78.8%

Source: MOF; compiled by Daiwa Securities.

*Scheduled issuance amount.

**Author's forecast.

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