

# Daiwa's View

## Upper House election update: JGB yields surge on momentum for fiscal expansionists

- Latest opinion polls clearly show that ruling parties in danger of losing their majority; super-long JGB yields surged roughly 10bp
- With fiscal expansionist parties (DPP, Sanseito) gaining ground, JGB market pricing in retreat from fiscal discipline

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The political situation surrounding the 20 July Upper House election is having a significant impact on the JGB market. On 14 July, JGB yields rose across the board, with super-long JGB yields (20yr, 30yr) in particular surging roughly 10bp. This is because, with the ruling parties clearly struggling, support for fiscal expansionary policies is growing and concerns about future increases in JGB issuance are rising.

A special opinion poll conducted by the *Mainichi Shimbun* on 12-13 July revealed that the Liberal Democratic Party (LDP) and its coalition partner, Komeito, continue to struggle to secure the 50 seats needed to maintain their majority in the Upper House. Compared to the situation at the start of the election campaign, among the 32 single-seat constituencies up for election nationwide, the number of closely contested constituencies has increased from 7 to 8, while the number of constituencies where opposition candidates are in the lead has increased from 16 to 18. The situation is becoming increasingly difficult for the ruling parties. The projected number of seats likely to be won by the LDP has been revised downward from a 32-46 range in the early stages to a 27-43 range at this juncture. Likewise, the number of seats targeted by Komeito is also likely to fall significantly short of the 14 seats up for re-election, with the party now expected to capture only 4 to 12 seats. The LDP and Komeito combined are projected to win between 31 and 55 seats. This means that the current situation is delicate in terms of maintaining a 50-seat majority.

A nationwide poll of about 34,000 people conducted by FNN over two days (12-13 Jul) also confirmed the same trend. In last week's survey, the LDP was leading in half of the single-seat constituencies, but LDP candidates are now in close races with opposition candidates. Even in the case of proportional representation, capturing the needed 19 contested seats is becoming more difficult. The projected number of seats is expected to remain in the low 40s. Even in the case of Komeito, many of its candidates running in constituencies with three or more seats up for re-election are on the bubble. Securing a majority is proving to be an extremely difficult battle.

### Comparison of Seat Projections for Major Parties in Upper House Election (*Mainichi Shimbun*, FNN)

Surveyed by	LDP / Komeito (66)	LDP (52)	Komeito (14)	CDP (22)	DPP (4)	Sanseito (1)	JIP (5)	Japanese Communist Party (7)
<i>Mainichi Shimbun</i>	Increasingly difficult (31~55)	27~43	4~12	23~32	11~19	8~17	5~7	3~5
FNN	Uphill battle to maintain majority	Low 40s	Decline	High 20s	16	Double digit	Around 5	Decline

Source: *Mainichi Shimbun*, FNN; compiled by Daiwa.

Notes: (1) Number of seats up for re-election is indicated in parentheses ( ) next to the name of each party.

(2) Political parties expected to win fewer than five seats are not included in the chart.

Turning to the opposition parties, gains made by the Democratic Party for the People (DPP) are worth noting. The DPP has strong candidates in constituencies in the Tokyo metropolitan area and the Tokai region. The party also has good momentum toward doubling its number of proportional representation seats. A significant increase from four seats up for re-election to between 11 to 19 seats is expected for the upcoming election. The situation is such that the DPP now appears close to achieving its target of 16 or more seats. Its expansionary fiscal policy is likely to have a significant impact on future administrative operations.

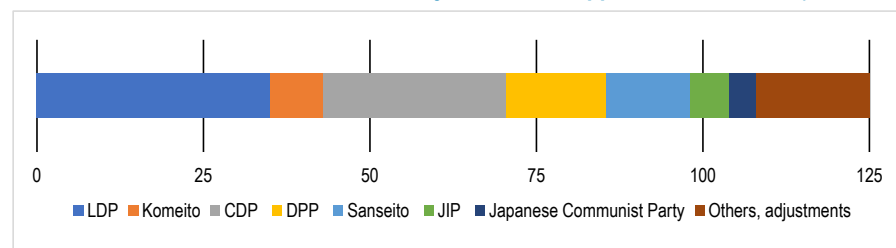
Another noteworthy development is the rise of the Sanseito. This party, which is campaigning on a platform of tax cuts, is gaining momentum nationwide in the proportional representation races and has multiple candidates leading in constituencies with three or more seats up for re-election. The situation is such that, at this juncture, Sanseito will likely win double-digit seats. The Constitutional Democratic Party of Japan (CDP) is gaining momentum in constituency races, exceeding its projected number of contested seats. However, it is struggling in the proportional representation races. Overall, it is expected to remain in a 25-29 seat range. The Japan Innovation Party (JIP) is failing to gain support outside its stronghold in the Kinki region and so is expected to only retain its current five seats.

The current political situation is such that the LDP and Komeito are now a minority ruling coalition in the Lower House. As there has been no real cooperation with opposition parties and no change in administration, the ruling coalition is managing the administration by forming partial alliances with the CDP, JIP, and other parties on a bill-by-bill basis. The 4 March budget was approved with the support of the LDP, Komeito, and the JIP. In this case, JIP policies that have relatively low fiscal costs were accepted by the LDP and Komeito. However, the DPP and Sanseito, which are advocating expansionary policies ahead of the Upper House election, could significantly increase their number of seats, leading to major changes for the political dynamics.

There is a growing view among JGB market participants that the administration will be forced to cooperate with forces calling for increased fiscal spending in its administration after the Upper House election. The DPP is demanding the costliest policies and even Sanseito is strongly advocating tax cuts. The growing influence of such political parties has heightened concerns about fiscal discipline and raised awareness of the risk of increased JGB issuance.

In [our 24 June report](#), we said, “Depending on the conduct of monetary policy after the July Upper House election, there is a risk that the fiscal risk premium could increase further, completely cancelling out the JGB issuance reduction effects.” Our assumption is moving closer to reality. Despite MOF reducing its issuance of super-long JGBs, increased political pressure for fiscal expansion is likely to offset the desired effect of MOF’s action and upward pressure on super-long JGB yields will most likely continue. Depending on the results of the Upper House election, we will need to consider the possibility that super-long JGB yields will rise further through an additional expansion of the fiscal risk premium.

#### No. of Seats Forecasted to Be Won for Major Parties in Upper House Election (*Mainichi Shimbun*)



Source: *Mainichi Shimbun*; compiled by Daiwa.

Notes: (1) As seat projections are shown as ranges, median values are applied.

(2) Political parties expected to win fewer than five seats are not included in the chart.

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