

Daiwa's Economic View

Revised our forecasts for FY26 initial budget, JGB issuance plan

- FY26 initial budget and JGB issuance plan likely finalized by 26 Dec
- FY26 initial budget to reflect policies of Takaichi administration; new JGB issuance likely to increase to mid-Y30tn range
- Expect decrease for 20yr, 30yr, and 40yr JGB issuance, increase for 2yr, 5yr, and 10yr issuance in FY26 JGB issuance plan with maximize consideration of market opinions

FICC Research Dept.

Koji Hamada

81-3-5555-8791

kouji.hamada@daiwa.co.jp

**Kenji Yamamoto**

81-3-5555-8784

kenji.yamamoto@daiwa.co.jp



Daiwa Securities Co. Ltd.

Japan's Diet passed the FY25 supplementary budget on 16 December and this extraordinary Diet session will adjourn on 17 December. The fiscal policy focus will now shift to the FY26 initial budget. Expectations are that the Cabinet will approve this initial budget by 26 December. The JGB issuance plan will also be announced on that day.

The FY26 initial budget strongly reflects the tone adopted by the Takaichi administration as its "Basic Principles of FY26 Budget Formulation" decided on 9 December was added on top of the "Basic Policies for Economic and Fiscal Management and Structural Reform" ("Basic Policies") prepared in June by the previous of Shigeru Ishiba cabinet. The amount of new JGBs issued is likely to increase to the mid-Y30tn range.

Formulation of the FY26 JGB issuance plan is expected to maximize consideration of opinions from previous Meetings of JGB Market Special Participants and Meetings of JGB Investors. We expect the issuance of 20-year, 30-year, and 40-year JGBs to decrease, with the issuance of 2-year, 5-year, and 10-year JGBs increasing.

Cabinet approval of FY26 initial budget expected by 26 December

The FY25 supplementary budget was adopted by the Diet on 16 December. This extraordinary Diet session will adjourn as scheduled on 17 December. Discussions on the FY26 initial budget will now begin in earnest between the government and ruling parties, as well as between the ruling and opposition parties.

Last year, the FY24 supplementary budget was enacted on 17 December and the FY25 initial budget was approved by the Cabinet on 27 December, which was the last working day of the year for government agencies. This year, the FY25 supplementary budget was enacted on 16 December. Perhaps by Friday 26 December (last working day of year for government agencies), the FY26 initial budget will be approved by the Cabinet and the JGB issuance plan will also be announced. Typically, the details of the JGB issuance plan are reported in advance, one day before the official announcement.

Four key points for FY26 initial budget; new JGB issuance likely to increase to mid-Y30tn range

As for the FY26 initial budget, in June the Ishiba cabinet approved the "Basic Policies," which serve as the government's basic concepts. While prioritizing regional revitalization and wage increases, the government aimed to achieve a surplus in both national and local primary balances by FY25-26, with some flexibility for the timeline.

However, the Takaichi cabinet, which took office in October, approved the “Basic Principles of FY26 Budget Formulation” at a Cabinet meeting on 9 December, which were added on top of the Ishiba cabinet’s “Basic Policies.”

- Ideal form of economic and fiscal management is “responsible expansionary fiscal policy.”
Achieve a “strong economy” through strategic fiscal stimulus to increase tax revenues, while keeping debt growth within the bounds of the growth rate to reduce the government debt-to-GDP ratio.
Achieve fiscal sustainability and secure market confidence.
- Existing expenses shall appropriately reflect factors such as inflation.
- While boldly prioritizing expenditures and taxation, review these when their effectiveness is lacking.
- Supplementary budgets have become routine and their scale has expanded, so need to normalize the expenditure structure (consideration will be given to including necessary policies in the initial budget).

Accordingly, the FY26 initial budget will likely focus on:

- (1) Extent to which inflation is reflected in expenditures
- (2) Extent to which additional measures to promote crisis management investments and growth investments will be included
- (3) Extent to which ineffective expenditures and taxation will be reviewed.

Also, the FY25 supplementary budget was passed by both the Diet’s Upper House and Lower House because, in addition to the Japan Innovation Party, Komeito and the Democratic Party for the People (DPP) voted in favor of that budget. The FY26 initial budget proposal and budget-related bills also face an uncertain path to passage unless some opposition parties in both the Upper House and Lower House vote in favor of those bills.

As such, to secure the support of the DPP, another key point will be:

- (4) Extent to which the annual income threshold for income tax is again raised.

In Chart 2 of our 2 December report ([Daiwa's Economic View “FY25 supplementary budget announcement: Key points for FY26 initial budget, JGB issuance plan”](#)), we factored in points (1) to (4) to a certain extent to forecast the amount of new JGBs to be issued. Therefore, in this report we have revised the figure to Y34.6tn based on the latest information, even though it remains largely unchanged from the previous forecast of Y34.3tn (Chart 1).

Chart 1: Initial Budget for National Government's General Account: Actuals and Forecasts (Y tn)

	2022	2023	2024	2025	2026 (forecasts)	25→26
Expenditures	107.6	114.4	112.6	115.2	124.9	9.7
Social security	36.3	36.9	37.7	38.3	38.9	0.6
National defense	5.4	10.2	7.9	8.7	9.6	0.9
Other general expenditures	20.2	20.2	20.1	20.4	22.6	2.1
National debt service	24.3	25.3	27.0	28.2	31.5	3.2
Redemption of national debt	16.1	16.8	17.3	17.7	18.2	0.5
Interest payments, etc.	8.2	8.5	9.7	10.5	13.2	2.7
Local allocation tax grants, etc.	15.9	16.4	17.8	18.9	21.9	3.0
Special contingency reserves	5.0	5.0	1.0	0.0	0.0	0.0
Contingency reserves	0.5	0.5	1.0	0.7	0.5	-0.2
Revenues	107.6	114.4	112.6	115.2	124.9	9.7
Tax revenues	65.2	69.4	69.6	77.8	82.5	4.7
Other revenues	5.4	9.3	7.5	8.7	7.8	-0.9
Newly-issued bonds	36.9	35.6	35.4	28.6	34.6	6.0

Source: MOF; compiled by Daiwa.

Expect 20yr, 30yr, and 40yr JGBs to decrease, 2yr, 5yr, and 10yr JGBs to increase in FY26 JGB issuance plan

We have also revised our forecast for the FY26 JGB issuance plan as compared to our 1 December report.

For the “JGB Issuance Plan by Legal Grounds,” which outlines the types of JGBs required for FY26 budget execution, we revised the new issuance amounts for both JGBs and FILP bonds. This is because, in order to realize the \$550bn for investment in the US, the Japan Bank for International Cooperation (JBIC) increased its request for FILP loans by Y3.2tn (Chart 2; had projected increase of Y2.0tn as of our 1 Dec report).

We revised our FY26 total JGB issuance amount to Y190tn (Y188.1tn as of our 1 Dec report), Y0.4tn higher than the FY25 total of initial budget and supplementary budget (Y189.6tn).

We also made minor revisions to the “JGB Issuance Plan by Financing Methods,” which indicates how the total amount of JGBs issued will be absorbed. That said, adjustment amounts between fiscal years shall be zero or negative and front-loaded issuance of refunding bonds shall not be used. The approach of covering the increase in total JGB issuance compared to the initial budget for the previous fiscal year, primarily through increased market issuance on a calendar basis, remains unchanged (Chart 3).

Chart 2: JGB Issuance Plan by Legal Grounds: Actuals and Forecasts (Y tn)

	FY25			FY26		
	Initial (after revision in Jun)	Total of initial budget and extra budget	Change due to extra budget	Initial (forecasts)	Difference between FY25 and FY26 initial plans	Difference between FY26 initial plan and FY25 total (initial plan and extra budget)
	(a)	(b)	(b)-(a)	(c)	(c)-(a)	(c)-(b)
Newly-issued bonds	28.6	40.3	11.7	34.6	6.0	-5.7
Reconstruction bonds	0.1	0.0	-0.1	0.1	0.0	0.1
GX economy transition bonds	0.7	1.4	0.6	0.7	0.0	-0.6
Children special bonds	1.1	1.1	0.0	1.1	0.0	0.0
Semiconductor/AI bonds	0.0	0.0	0.0	0.0	0.0	-0.0
FILP bonds	10.0	12.0	2.0	13.6	3.6	1.6
Refunding bonds	136.2	134.7	-1.5	139.8	3.6	5.1
Total	176.9	189.6	12.7	190.0	13.1	0.4

Source: MOF; compiled by Daiwa.

Chart 3: JGB Issuance Plan by Financing Methods: Actuals and Forecasts (Y tn)

	FY25			FY26		
	Initial (after revision in Jun)	Total of initial budget and extra budget	Change due to extra budget	Initial (forecasts)	Difference between FY25 and FY26 initial plans	Difference between FY26 initial plan and FY25 total (initial plan and extra budget)
	(a)	(b)	(b)-(a)	(c)	(c)-(a)	(c)-(b)
Calendar-based market issuance	171.8	178.7	6.9	178.5	6.7	-0.2
Non-price competitive auctions II	6.8	5.5	-1.3	5.7	-1.1	0.2
Fiscal year adjustment	-6.9	-0.0	6.9	-0.0	6.9	-0.0
Subtotal financed in market	171.7	184.2	12.5	184.2	12.5	-0.0
Sales to individual investors	5.1	5.4	0.3	5.8	0.7	0.4
Total	176.9	189.6	12.7	190.0	13.1	0.4

Source: MOF; compiled by Daiwa.

As for the breakdown of calendar-based market issuance amounts by maturity, we have made significant changes from our 1 December report that better maximize consideration of market participants' requests (Chart 4).

Super-long JGBs with 20-year, 30-year, and 40-year maturities were all reduced. The 20- and 30-year JGBs were each reduced by Y0.1tn/auction. There was the opinion that reducing the 40-year JGB issuance by Y0.1tn/auction to Y0.3tn/auction would reduce liquidity. Therefore, we believe the plan to increase issuance by Y0.1tn/auction to Y0.5tn/auction and reduce the frequency from every other month to once each quarter will be adopted.

Medium- and long-term JGBs with 2-year, 5-year, and 10-year maturities were all increased. The 5-year and 10-year JGBs were each increased by Y0.1tn/auction. The 2-year JGB, which many believed had significant room for increase, was raised by Y0.2tn/auction.

We expect the 6-month T-bill amount to decrease slightly from the FY25 total of initial budget and supplementary budget, curbing the increase in refunding bonds.

Chart 4: Breakdown of Calendar-based Market Issuance Amounts by Maturity in JGB Issuance Plan (Y tn)

	FY25 initial (after revision in Jun)			Total of FY25 initial budget and extra budget				FY26 initial (forecasts)				
	(per auction)	(No. of auctions)	(Annual issuance amount: a)	(per auction)	(No. of auctions)	(Annual issuance amount: b)	(b)-(a)	(per auction)	(No. of auctions)	(Annual issuance amount: c)	(c)-(a)	(c)-(b)
40yr JGBs	0.5 0.4	× 1 5	2.5	0.5 0.4	× 1 5	2.5	0.0	0.5 0.4	× 4 12	2.0 7.2	-0.5 -1.5	-0.5 -1.5
30yr JGBs	0.8 0.7	× 3 9	8.7	0.8 0.7	× 3 9	8.7	0.0	0.6 0.7	× 12 12	7.2 8.4	-1.5 -1.8	-1.5 -1.8
20yr JGBs	1.0 0.8	× 3 9	10.2	1.0 0.8	× 3 9	10.2	0.0	0.7	× 12	8.4	-1.8	-1.8
10yr JGBs	2.6	× 12	31.2	2.6	× 12	31.2	0.0	2.7	× 12	32.4	1.2	1.2
5yr JGBs	2.4	× 12	28.8	2.4 2.5	× 9 3	29.1	0.3	2.6	× 12	31.2	2.4	2.1
2yr JGBs	2.6 2.7	× 6 6	31.8	2.6 2.7 2.8	× 6 3 3	32.1	0.3	3.0	× 12	36.0	4.2	3.9
TBs			42.9			49.2	6.3			45.6	2.7	-3.6
1yr	3.2 3.3	× 9 3	38.7	3.2 3.3	× 9 3	38.7	0.0	3.3	× 12	39.6	0.9	0.9
6mo	0.7	× 6	4.2			10.5	6.3	1.0	× 6	6.0	1.8	-4.5
10yr JGB linkers	0.25	× 4	1.0	0.25	× 4	1.0	0.0	0.25	× 4	1.0	0.0	0.0
Climate Transition JGBs			1.2			1.2	0.0			1.2	0.0	0.0
10yr	0.3	× 2	0.6	0.3	× 2	0.6	0.0	0.3	× 2	0.6	0.0	0.0
5yr	0.3	× 2	0.6	0.3	× 2	0.6	0.0	0.3	× 2	0.6	0.0	0.0
Liquidity enhancement auction			13.5			13.5	0.0			13.5	0.0	0.0
15.5yr-39yr			2.3			2.0	-0.3			2.0	-0.3	0.0
5yr-15.5yr			7.8			7.8	0.0			7.8	0.0	0.0
1yr-5yr			3.4			3.7	0.3			3.7	0.3	0.0
Total			171.8			178.7	6.9			178.5	6.7	-0.2

Source: MOF; compiled by Daiwa.

Concerns about fiscal deterioration have tended to smolder under the Takaichi administration. If rising food and energy prices persist, the administration will have no choice but to continue providing fiscal support. We expect the JGB issuance plan to adopt a form that is more likely to instill greater confidence among market participants.

IMPORTANT DISCLOSURES

This report is provided as a reference for making investment decisions and is not intended to be a solicitation for investment. Investment decisions should be made at your own discretion and risk. Content herein is based on information available at the time the report was prepared and may be amended or otherwise changed in the future without notice. We make no representations as to the accuracy or completeness. Daiwa Securities Co. Ltd. retains all rights related to the content of this report, which may not be redistributed or otherwise transmitted without prior consent.

Ratings

Issues are rated 1, 2, 3, 4, or 5 as follows:

- 1: Outperform TOPIX/benchmark index by more than 15% over the next 12 months.
- 2: Outperform TOPIX/benchmark index by 5-15% over the next 12 months.
- 3: Out/underperform TOPIX/benchmark index by less than 5% over the next 12 months.
- 4: Underperform TOPIX/benchmark index by 5-15% over the next 12 months.
- 5: Underperform TOPIX/benchmark index by more than 15% over the next 12 months.

Benchmark index: TOPIX for Japan, S&P 500 for US, STOXX Europe 600 for Europe, HSI for Hong Kong, STI for Singapore, KOSPI for Korea, TWII for Taiwan, and S&P/ASX 200 for Australia.

Target Prices

Daiwa Securities Co. Ltd. sets target prices based on its analysts' earnings estimates for subject companies. Risks to target prices include, but are not limited to, unexpected significant changes in subject companies' earnings trends and the macroeconomic environment.

Disclosures related to Daiwa Securities

Please refer to https://drp.daiwa.co.jp/rp-daiwa/direct/reportDisclaimer/e_disclaimer.pdf for information on conflicts of interest for Daiwa Securities, securities held by Daiwa Securities, companies for which Daiwa Securities or foreign affiliates of Daiwa Securities Group have acted as a lead underwriter, and other disclosures concerning individual companies. If you need more information on this matter, please contact the Research Production Department of Daiwa Securities.

Explanatory Document of Unregistered Credit Ratings

This report may use credit ratings assigned by rating agencies that are not registered with Japan's Financial Services Agency pursuant to Article 66, Paragraph 27 of the Financial Instruments and Exchange Act. Please review the relevant disclaimer regarding credit ratings issued by such agencies at: https://drp.daiwa.co.jp/rp-daiwa/direct/reportDisclaimer/credit_ratings.pdf. If you need more information on this matter, please contact the Research Production Department of Daiwa Securities.

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.)

If you decide to enter into a business arrangement with our company based on the information described in this report, we ask you to pay close attention to the following items.

- 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

Memberships: Japan Securities Dealers Association, The Financial Futures Association of Japan, Japan Investment Advisers Association, Type II Financial Instruments Firms Association, Japan Security Token Offering Association