

Daiwa's View

FICC Research Dept.

Impact of Lower House dissolution on 10yr JGB yield

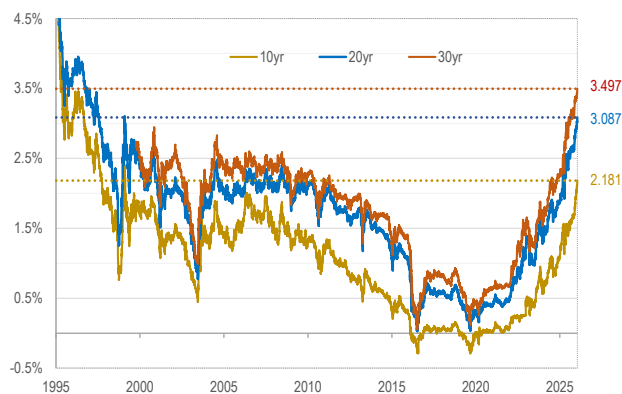
- Impact of Lower House election on JGB term premium
- We anticipate 11-16bp yield rise due to deteriorating fiscal sentiment
- Responsibility behind “responsible proactive fiscal policy” to be tested after Lower House election

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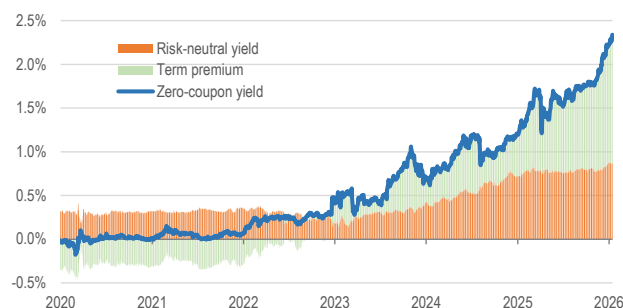
Daiwa Securities Co. Ltd.

10yr JGB yield hits highest level in 27 years amid Lower House dissolution reports

Since the launch of the Takaichi administration in October 2025, the 10-year JGB yield has continued to steadily rise. The BOJ's December rate hike pushed the 10-year JGB yield above 2% and the 9 January speculative media report regarding a dissolution of the Lower House pushed this yield up to 2.18% (as of 14 Jan close, simple yield), marking the highest level in roughly 27 years. This can be described as a term premium-driven yield rise brought about by concerns over increased government debt due to the Takaichi administration's pursuit of proactive fiscal policy. A Lower House election is now expected sometime in the first half of February. So, in this report we want to quantitatively grasp the election's impact on the 10-year JGB yield and examine key points going forward.

Chart 1: JGB Yields

Source: Bloomberg; compiled by Daiwa.

Chart 2: Daiwa JGB Term Premium (10yr)

Source: Compiled by Daiwa.

Fiscal sentiment and JGB term premium

In our 5 November 2025 *Daiwa's View* ("Impact of fiscal policy and QT on JGB term premium")¹ we analyzed the factors influencing the JGB term premium, which represents the risk premium component in the 10-year JGB yield, and reported that it is impacted by JGB volatility, the 10-year UST yield's term premium, the outstanding balance of JGBs, and the amount of JGBs held (purchased) by the BOJ. Meanwhile, it can be said that this outstanding balance of JGBs and JGBs held by the BOJ are known information on the market (already priced in). So, by incorporating into this model the Fiscal Policy Uncertainty Index (FPU)² introduced in our 13 January report, we aim to visualize the impact of fiscal sentiment on JGB yields.

The specific results of our quantitative analysis are shown in Chart 3. In the case of Model (1), as variables explaining the JGB term premium, we added the logarithm of the fiscal uncertainty index³ to a simple model consisting of the JGB VIX index and the UST term premium. As a result, the coefficient is significantly positive, indicating that a per unit increase in the logarithm of the uncertainty index raises the term premium by 11bp. Also, even in Model (2), which incorporates the BOJ's holdings of JGBs and the outstanding amount of JGBs (both as % of GDP), this result does not change significantly. Rising fiscal risks will push up the JGB term premium.

Chart 3: Analysis Results

Explanatory variables		Explained variable					
		JGB term premium: TP_JGB					
		Model (1)		Model (2)		Model (3)	
JGB VIX		12.41	***	11.68	***	8.03	***
	JGBV	(0.000)		(0.000)		(0.000)	
UST term premium		0.25	***	0.37	***	0.13	***
	TP_UST	(0.000)		(0.000)		(0.000)	
Fiscal Policy Uncertainty Index (log)		11.10	**	14.04	**	18.88	***
	LN_FPU	(0.025)		(0.025)		(0.004)	
Ratio of BOJ's JGB holdings to GDP				0.03			
	BOJ/GDP			(0.819)			
Ratio of outstanding JGBs to GDP				0.97	***		
	JGB/GDP			(0.002)			
Constant term		-80.29	**	-252.63	**	-78.95	*
	Intercept	(0.000)		(0.000)		(0.000)	
Determination coefficient		0.7303		0.7699		0.4425	
Degrees of freedom		210		210		109	

Source: Various data; compiled by Daiwa.

Notes: (1) One, two, and three stars (*) indicate statistical significance at the 10%, 5%, and 1% level, respectively.

(2) P-value shown in parentheses.

(3) Monthly data from Aug 2008 to Dec 2025. Model (3) excludes period from Apr 2013 to Dec 2022.

This analysis utilizes data from 2008 through the end of December 2025. As introduced in our 13 January *Daiwa Memorandum* (Japanese only), during the period of large-scale monetary easing by the BOJ, the impact of finances on JGB yields was likely diminished due to the Bank's massive purchases of JGBs and the implementation of yield curve control (YCC). As such, Model (3) is a regression analysis conducted excluding the period of large-scale monetary easing, defined as the timeframe from April 2013, when former BOJ Governor Haruhiko Kuroda initiated QQE, to December 2022 when the YCC range was expanded. As a result, the FPU is significantly positive and its coefficient consists of a large value compared to Model (1). Therefore, as large-scale monetary easing comes to an end and the process of monetary policy normalization unfolds, we can say that fiscal sentiment is now exerting a greater influence on JGB yields.

¹ Shun Otani (5 Nov 2025). [Daiwa's View: Impact of fiscal policy and QT on JGB term premium](#).

² Elif C. Arbatli, Steven J. Davis, Arata Ito, and Naoko Miake, [Policy Uncertainty in Japan](#), 10 January 2022.

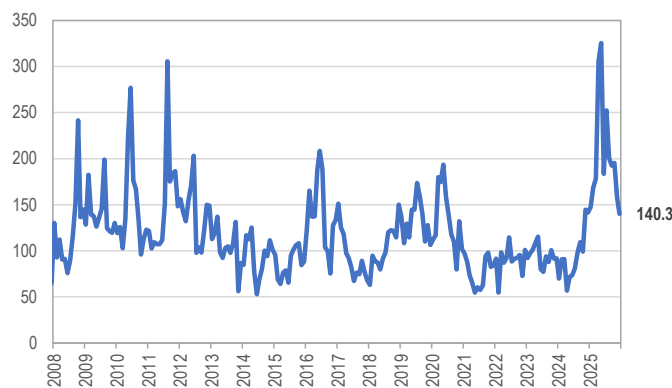
³ Indices like the FPU tend to have a positive skew that spikes with each event and they are generally analyzed using logarithmic transformation.

Points of reference for a rise in 10yr JGB yield

Based on the above models, our aim is to understand the quantitative impact of deteriorating fiscal sentiment on JGB yields. The coefficients of the FPU logarithm were 11.1 for Model (1) and 18.88 for Model (3). The actual FPU value as of December 2025 was 140.3. The value was 252.4 in July 2025 when the last Upper House election was held. In May 2025, when super-long JGB yields surged, the figure reached 325.5, marking the recent high. Converting these into logarithmic values results in 4.94, 5.53, and 5.79, respectively. As for the Lower House election expected sometime during the first half of February, if fiscal risks are perceived as they were last spring and summer, the FPU logarithmic values are projected to rise by approximately 0.59 (= $5.53 - 4.94$) and 0.85 (= $5.79 - 4.94$), respectively. Multiplying these figures by the coefficients in Model (3) results in values of roughly 11bp (= 18.88×0.59) and approximately 16bp (= 18.88×0.85), indicating an expected 10-year JGB yield rise of just over 10bp.

The impact of this Lower House election on the 10-year JGB yield, particularly the term premium, is expected to fall between 11bp and 16bp. The 10-year JGB yield just before the speculative media report on the evening of 9 January was approximately 2.10%, with 2.20% to 2.25% likely serving as points of reference for a rise.

Chart 4: Fiscal Policy Uncertainty Index



Source: Arbatti, Davis, Ito, and Miyake (2022); compiled by Daiwa.

Key points going forward

In the 2024 Lower House election and the 2025 Upper House election, policies to alleviate burdens became key issues as citizens struggled amid the first significant price increases in 30 years. The proposed policies included raising the tax-free annual income threshold, consumption tax cuts, and handouts. Meanwhile, gasoline prices have been falling recently, partly due to the abolition of the provisional gasoline tax rate. Furthermore, the rise in rice prices has also started to level off. Prime Minister Sanae Takaichi has set a goal of reducing the ratio of outstanding government debt ("approximately equal to outstanding JGB issuance) to GDP as part of her "responsible proactive fiscal policy." Given Japan's current political environment, "austerity" and "fiscal consolidation" are unlikely to win votes. During the election period, as each party promotes fiscal spending, fiscal sentiment is likely to deteriorate, placing some upward pressure on the 10-year JGB yield. The subsequent developments will depend on the election results, but should the Takaichi administration prevail, the market will surely test the responsibility of its "responsible proactive fiscal policy."

◆ PM Takaichi's 24 Oct 2025 policy address

My cabinet regards as fundamental the principle that the economy is what enables fiscal spending. In order to build a robust economy, we will strategically employ fiscal policies as we endeavor to raise incomes, transform people's mindsets regarding consumption, and boost tax revenues without raising tax rates as business earnings increase, all in keeping with our approach of responsible and proactive public finances. By realizing this economic virtuous cycle, we will enable the public to feel the fruits of economic recovery in a tangible manner, thereby changing worry into hope. Following this path, we will curb the rate of growth of Japan's outstanding debt balance so as not to exceed the rate of economic growth and lower Japan's ratio of outstanding government debt to GDP. This will bring about the sustainability of public finances and ensure trust from the markets.

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