Daiwa's View

"Behind the curve" concerns and super-long JGBs

- "Behind the curve" concerns as viewed from JGB yield curve
- Super-long JGB supply/demand conditions as indicated by BOJ Gov Ueda
- Endure volatile winter, wait for spring when supply/demand conditions likely to improve

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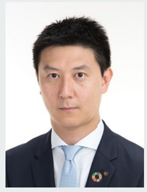


Policy mix and supply/demand conditions for super-long JGBs

During his press conference following the 23 January Monetary Policy Meeting, BOJ Governor Kazuo Ueda was asked about his view on the rising 10-year JGB yield. In addition to changes in the outlook for fiscal and monetary policy, he cited deteriorating supply/demand conditions for super-long JGBs due to fiscal year-end factors. Meanwhile, there were sharp price movements among super-long JGBs last week stemming from rising inflationary pressures as the government pursues aggressive fiscal policy. Meanwhile, there are also concerns that the BOJ, mindful of government considerations, may fall behind the curve by failing to respond with appropriate rate hikes and, instead, allow inflation to persist (= result of policy mix inconsistencies[1]). In this report we want to analyze the movement of yield curve factors since the launch of the Takaichi administration last October and summarize the supply/demand conditions for super-long JGBs heading into the next fiscal year.

◆ **BOJ Governor Kazuo Ueda's Press Conference (23 Jan 2026)**

I assume there were several questions regarding the recent rise for the 10-year JGB yield. First, our assessment is that this yield has been rising at quite a fast pace. In that regard, there are opinions in the market suggesting that the outlook for economic activity and prices, fiscal policy, and monetary policy are having impacts. We have also heard concerns that fiscal year-end factors are destabilizing supply and demand conditions for super-long JGBs.

Yield-rising factors: Inflation expectations and real yields

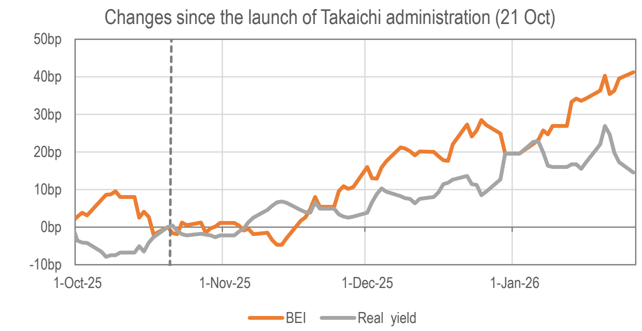
Since the Takaichi administration took office on 21 October, the 10-year JGB yield has risen by roughly 55bp (from 1.676% to 2.227%). When breaking down these components into inflation expectations (BEI) and real yields, the former rose by 41bp, while the latter increased by only 14bp. In particular, while both had been rising at similar rates until December 2025, since the start of 2026, BEI has risen noticeably while real yields have remained flat. The absolute value of BEI (JYGGBE10) stood at 1.991% as of 26 January, moving closer to the key 2% level. The BOJ, recognizing that real yields are extremely low, intends to adjust the degree of monetary easing by raising the policy interest rate. Real yields are thought to directly refer to the difference between short-term yields and the underlying inflation rate. However, as for the long-term zone, since rising JGB yields are primarily driven by inflation expectations, changes in real yields impacting the real economy have been limited.

[1] Ryoma Kawahara and Kento Minami (26 Jan 2026). [Daiwa's View: Policy mix contradictions: Jan BOJ meeting and pressure to hike rates].

Yield-rising factors: Risk-neutral yields and term premium

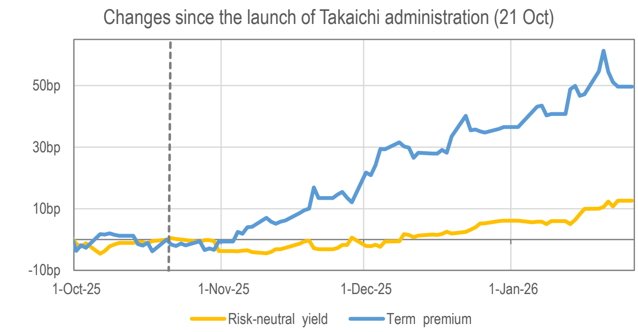
Also, using our JGB term premium model, when broken down into risk-neutral yield and term premium, the former is +13bp while the latter is +50bp. Given the model's characteristics[2], even considering that short-term fluctuations are absorbed by the term premium and the risk-neutral yield changes only gradually to reflect past JGB price movements, it would not seem unexpected if fiscal concerns and worries about falling behind-the-curve steepen the yield curve.

Chart 1: 10yr Inflation Expectations (BEI), Real Yield



Source: Bloomberg; compiled by Daiwa.

Chart 2: 10yr Risk-neutral Yield, Term Premium

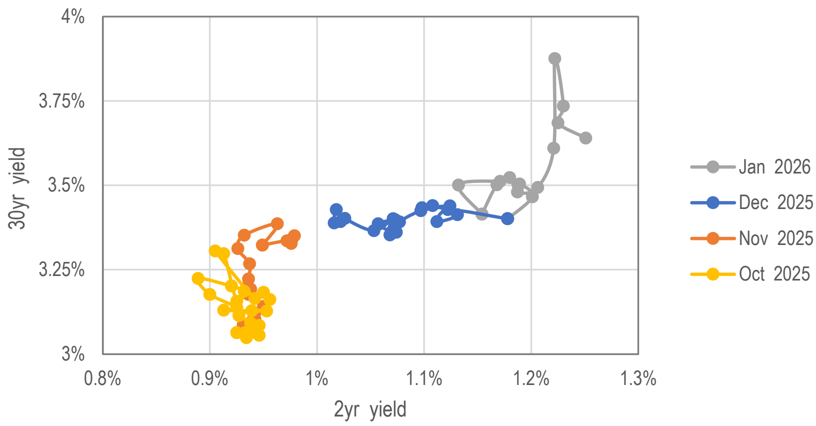


Source: Bloomberg; compiled by Daiwa.

Concerns about falling behind curve from 2-year, 30-year JGB perspective

Also, Chart 3 shows a scatter plot of the yields for 2-year and 30-year JGBs covering the price movements since October. Until November, the 2-year JGB yield remained within a fairly narrow space in the low 0.90% range, while the rise for the 30-year JGB yield was noticeable. Conversely, from the start of December, the 30-year JGB yield stabilized at around 3.4%, while the 2-year JGB yield topped the 1.0% line to approach 1.2%. Since the start of 2026, while the 2-year JGB yield once again remained in the low 1.2% range, 30-year zone yields and volatility clearly rose.

Chart 3: Scatter Plot of 30yr and 2yr JGB Yields



Source: Bloomberg; compiled by Daiwa.

2-year JGBs are highly dependent on the policy interest rate due to the characteristics of the yield curve. Since Ueda's speech on 1 December[3], market expectations for a December rate hike rapidly intensified. Expectations that the policy interest rate would rise to 0.75% pushed the 2-year JGB yield above 1%. Meanwhile, expectations that the policy interest rate will remain at 0.75% for some time after January will place certain constraints in terms of the 2-year JGB yield exceeding 1.2%. As seen in October and November, this environment may be triggering a mechanism whereby upward pressure on yields spreads to the back end of the yield curve,

[2] Shun Otani (15 Dec 2025). Daiwa Memorandum: Rate hike expectations and risk-neutral yield.
[3] Kento Minami and Kenji Yamamoto (2 Dec 2025). Daiwa's Economic View: BOJ Ueda's speech: Greater certainty on December rate hike.

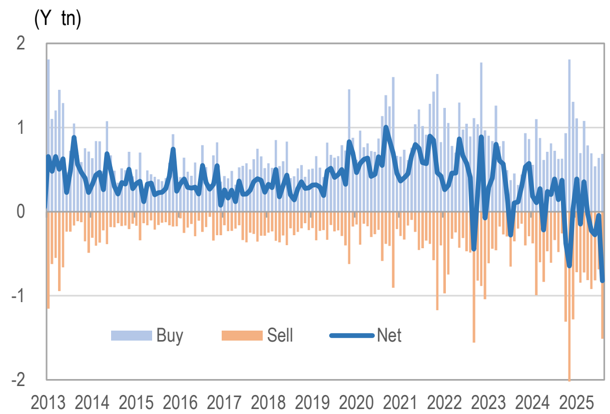
making it easier for the emergence of higher yields and increased volatility in the long- and super-long zones. It is hard to determine whether or not the BOJ is falling behind the curve. However, at the very least, enhancing the effectiveness of rate hikes seems likely to contribute to stabilizing the super-long zone of the yield curve.

Supply/demand for super-long-JGBs and spring of 2026 (start of FY26)

Ueda cited the deteriorating supply/demand conditions for super-long JGBs brought about by fiscal year-end factors. Indeed, reviewing the investor-specific trading trends published by the Japan Securities Dealers Association reveals that in December life and non-life insurers were net sellers of super-long JGBs to the tune of Y822.4bn, marking the largest single-month figure since FY04. Rising yields are creating a need to adjust portfolios[4], which could become more significant as the fiscal year-end approaches. Meanwhile, on the supply side, the JGB issuance plan for FY26 includes a scheduled issuance amount of Y17.4tn for super-long JGBs with maturities exceeding 20 years. The plan anticipates a 40% reduction from the peak in FY22. There are also plans for a 15.5% ratio of super-long JGBs within fixed-rate JGBs with maturities exceeding two years, the lowest level since FY07.

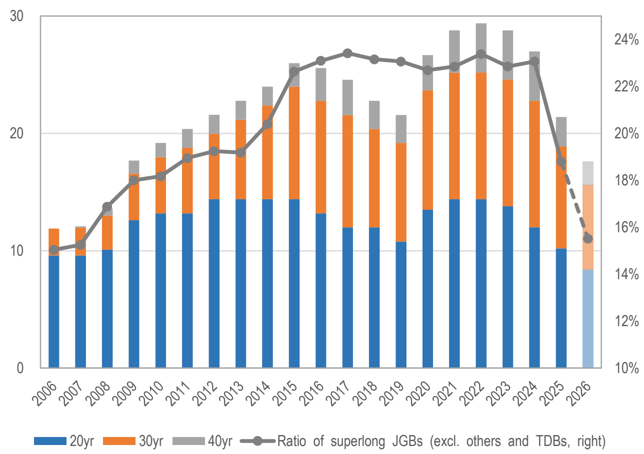
During the winter election period, each political party will likely tout their fiscal spending plans, which could easily increase risk in terms of fiscal instability. When also including year-end factors, super-long JGBs are expected to experience high volatility. Meanwhile, taking into account the results of the 2026 spring labor-management wage negotiations, the likelihood of an interest rate hike is expected to gradually increase. We must wait for the spring of 2026 (start of FY26), when the JGB issuance amount will actually be reduced.

Chart 4: Trading of Superlong JGBs by Investor Type: Life & Non-life Insurers



Source: Bloomberg; compiled by Daiwa.

Chart 5: Issuance Amount of Superlong JGBs



Source: MOF; compiled by Daiwa.
Note: Figures are actuals through FY24, on a post-supplementary budget basis for FY25, and on an initial plan basis for FY26.

[4] Yuki Sakamoto (23 Jan 2026). *Life Insurance ALM Convexity Shock*.

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