

Daiwa's View

Implications of halting reduction of JGB purchases by BOJ: Balance sheet's landing point in 2035

- BOJ's JGB holdings expected to decline to Y248tn in FY35, with its share to outstanding amount falling to 19%
- Relationship between decrease in current account balances and banknotes
- Establishing rules for JGB holdings

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Halting reduction of JGB purchases from FY27 onward at June MPM

As reported in yesterday's *Daiwa's View*¹, at the Monetary Policy Meeting (MPM) on June 16, alongside a 25bp rate hike, the interim assessment of Quantitative Tightening (QT) is increasingly likely to result in an announcement that the current quarterly reduction of monthly purchases by Y200bn will continue until March 2027, after which the reductions will be stopped, and JGB purchases will continue at a pace of Y2.1tn per month for the time being.

Until now, we had assumed that the reduction of JGB purchases would continue, albeit at a slower pace. This was based on the view that the BOJ would need to respond to the rapid rise in long-term yields while also demonstrating its intention to continue shrinking its balance sheet, which is considerably large compared to those of other countries. However, it can be said that the BOJ has now placed greater emphasis on the former factor. If the rise in long-term yields is attributed to the two concerns about fiscal policy and being "behind the curve," halting the reduction would contribute to improving supply/demand conditions in the short term, although the effect on curbing the rise in yields is uncertain. Indeed, in the JGB market on the 9th, repurchases were prominent in the superlong zone, where the supply/demand impact is significant.

BOJ's JGB holdings and share of holdings after reduction is halted

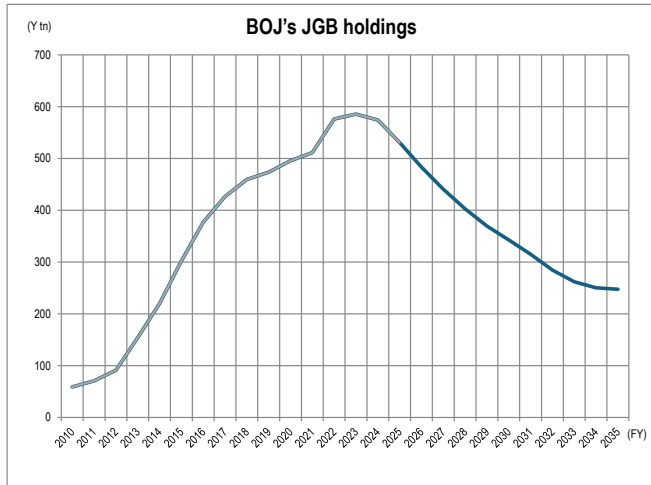
If the BOJ halts reduction of its JGB purchases from FY27 and continues to buy Y2.1tn per month, its JGB holdings (and its share to total JGBs outstanding) are projected to decrease to Y483tn (42%) by the end of FY26, Y315tn (26%) by the end of FY31, and Y248tn (19%) by the end of FY35². Looking at the BOJ's balance sheet as of the end of May, JGBs amounted to Y533tn, accounting for over 80% of its Y664tn in total assets. On the liabilities side, the main components are banknotes (Y115tn) and current account balances (Y452tn). Assuming that the reduction in BOJ's JGB holdings is offset by a decrease in current account balances and that other items remain unchanged³, current account balances are projected to decrease to Y450tn by the end of FY27, then to Y234tn by the end of FY31, and to Y166tn by the end of FY35.

¹ Kenta Tadaide and Kengo Shiroyama (10 Jun 2026). [Daiwa's View: Rate hikes and halt to reductions in JGB purchases.](#)

² For assumptions of QT simulation, please refer to our 15 Apr 2026 report [Daiwa's View: BOJ's QT and JGB market—Landing point indicated by maturities of JGBs purchased under June interim assessment.](#)

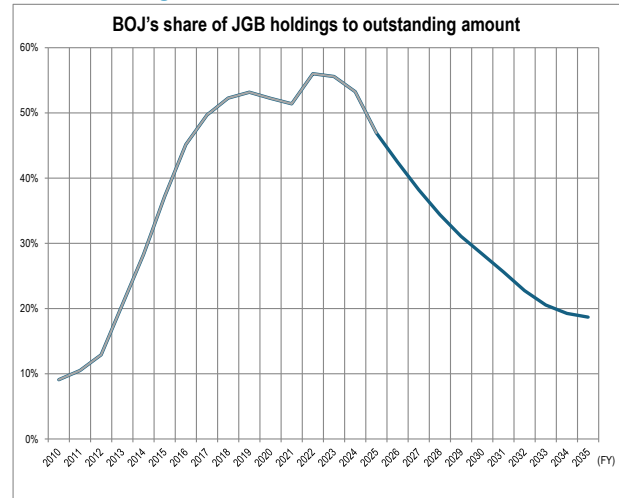
³ To be more specific, the sale and disposal of pecuniary trusts, which consist of ETFs and other assets, have begun, but the pace is extremely slow, on the order of a century. Additionally, loans are expected to decrease by several tens of trillions of yen in the coming years as various fund-supplying operations are discontinued. Strictly speaking, these are factors that will contribute to a further reduction in current account balances.

Chart 1: Forecasts for BOJ's JGB Holdings After Halting Reduction in JGB Purchases



Source: BOJ, etc.; compiled by Daiwa.

Chart 2: Forecasts for BOJ's Share of JGB Holdings After Halting Reduction in JGB Purchases



Source: BOJ, Cabinet Office, etc.; compiled by Daiwa.

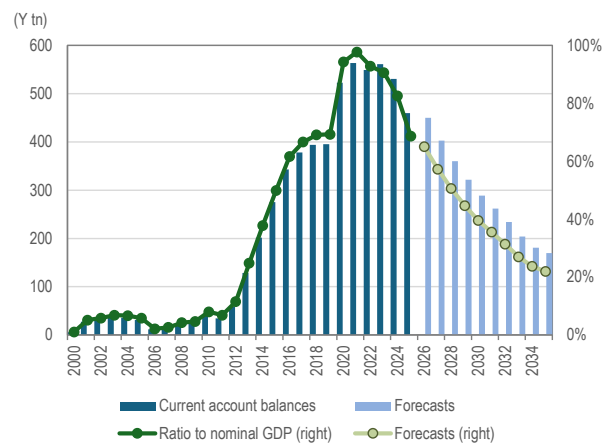
From a long-term perspective, halting the reduction carries a stronger signaling effect. Once the reduction is halted, the hurdle to restarting it would be high from a political standpoint, and the monthly purchases of Y2.1tn are likely to continue for some time. Currently, the average maturity of JGBs purchased by the BOJ is approximately 7 years, which roughly matches the average maturity of newly issued JGBs by the MOF (on a flow basis). If the BOJ were to permanently purchase Y2.1tn per month with an average maturity of 7 years, its JGB holdings would converge to Y176.4tn (= Y2.1tn × 12 months × 7 years). The corresponding current account balances under the above assumptions would be Y95tn.

Chart 3: BOJ's Balance Sheet (Y tn, as of end-May 2026)

Total 664	
JGBs	533
Banknotes	115
Current account balances	452
Pecuniary trusts	38
Loans and bills discounted	77
Others	16
Other deposits	49
Others	33
Owner equity	15

Source: BOJ; compiled by Daiwa.

Chart 4: Current Account Balances, Ratio to Nominal GDP



Source: BOJ, Cabinet Office; compiled by Daiwa.

Relationship between decrease in BOJ's JGB holdings and current account balances

Just before the start of Quantitative and Qualitative Easing (QQE) in FY12, the balance of current accounts stood at Y58tn, representing about 11% of nominal GDP. According to the Cabinet Office's medium- to long-term projections (projection of past trend case), nominal GDP is expected to reach Y772tn in FY35. Therefore, the projected current account balance of Y166tn at the end of FY35 would be 22% of nominal GDP. Furthermore, a balance of Y95tn would correspond to 12%.

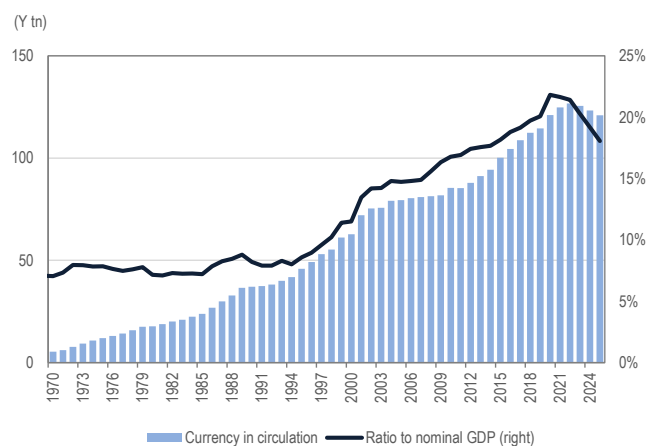
Excellent research by David Lopez-Salido and Annette Vissing-Jorgensen⁴ has suggested thresholds for the reduction of reserve balances in the US (the equivalent of current account balances) as a percentage of nominal GDP at 7%, 11%, and 13.5%. Based on such empirical studies, the Fed halted its balance sheet reduction last year, and resumed purchases centered on short-term Treasuries under the RMP framework. The author does not have the materials to discuss the appropriate level of current account balances in Japan, but the balance of these accounts can become a constraint on policy operations through its impact on tightness in short-term money markets. The optimal balance sheet size will be sought by also considering the slowdown in deposit growth in the banking sector, the narrowing of the loan-to-deposit gap, the demand for current account balances from private banks to comply with liquidity regulations (LCR and NSFR), and the uneven distribution of current account balances among participants.

Trends in banknotes and their impact

Looking at the ratio of banknotes (nearly equal to currency in circulation), another component of the central bank's balance sheet liabilities, to nominal GDP, we see that it was stable at around 7-8% until the mid-1990s. However, it began to rise after 1997, reaching 21% in 2020. The factors behind this are thought to include an increased preference for cash in 1997 and 1998 when the financial crisis deepened, as well as a decline in the opportunity cost of holding cash (such as cash kept at home) amid the subsequent low interest rate environment. In addition, the expected real return on cash holdings was high in the deflationary environment.

In recent years, however, this ratio has been on a downward trend, partly due to the increase in the denominator (nominal GDP) alongside a decrease in banknotes. This may be influenced by technological factors, such as the spread of credit card payments and various forms of electronic money, in addition to the effects of inflation and rising interest rates. If the ratio of currency in circulation to GDP falls to 7% by FY35, the amount would decrease to Y54tn (= Y772tn × 7%). While this is a somewhat bold calculation, it will be one of the key points of discussion, including in relation to Central Bank Digital Currency (CBDC).

Chart 5: Currency in Circulation, Ratio to Nominal GDP



Source: BOJ, Cabinet Office; compiled by Daiwa.

⁴ David Lopez-Salido and Annette Vissing-Jorgensen (2023). "Reserve Demand, Interest Rate Control, and Quantitative Tightening."

Rule-making for JGB holdings and its impact on JGB market

If banknotes were to decrease while the central bank's balance sheet remains constant, it could become a factor that increases current account balances. While this could provide a certain buffer for the banking system, the situation is more complex from the perspective of the central bank's profit and loss. Under the ample reserve system, interest is paid on excess reserves, whereas banknotes, needless to say, do not bear interest. This indicates that banknotes play a role akin to a form of capital for the central bank through seigniorage. More directly, a decrease in banknotes and an increase in current account balances would be a factor in worsening the central bank's profitability through increased interest payments. In the past, a measure known as the "Banknote rule" was in place, which limited the holdings of JGBs to within the amount of banknotes in circulation. As the balance sheet shrinks, how the BOJ establishes rules for its JGB holdings, considering their absolute amount and maturity composition, will also become a factor affecting supply/demand conditions of JGBs.

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