

Minutes of the Meeting of JGB Market Special Participants (96th Round)

1. Date: Monday, November 29, 2021 (4:00 p.m. to 5:00 p.m.)
2. Place: International Conference Room, Ministry of Finance /online
3. Gist of Proceedings: Current status and issues for the compilation of the JGB Issuance Plan for FY2022

▶ The Financial Bureau gave the following explanation about the current status and issues for the compilation of the JGB Issuance Plan for FY2022.

- Regarding the revision of the JGB Issuance Plan as a result of the supplementary budget for FY2021 published on past November 26, while the amount of the Newly-issued Bonds was increased by about ¥22.1 trillion, the amount of the Fiscal Investment and Loan Program(FILP) Bonds was decreased by ¥30 trillion by making use of the surplus cash of the fiscal loan fund. Consequently, the total JGB issuance size and the JGB Market Issuance (Calendar Base) will be reduced by ¥11.6 trillion and ¥9.2 trillion, respectively.

- The JGB Market Issuance (Calendar Base) for FY2021 was heavily dependent on short-term bonds and the funding structure was vulnerable to fluctuations in interest rates. Therefore, the amount of ¥9.2 trillion which is the reduction amount of the JGB Market Issuance (Calendar Base) will be allotted to the reduction of 6-month bonds of short-term bonds.

- As a result of these revisions, the total JGB issuance size was reduced to ¥224.4 trillion in the supplementary budget for FY2021 from the initial amount for FY2021 of ¥236 trillion, a reduction by ¥11.6 trillion.

- In addition, the JGB Market Issuance (Calendar Base) was reduced to ¥212.2 trillion in the supplementary budget for FY2021 from the initial amount for FY2021 of ¥221.4 trillion, a reduction by ¥9.2 trillion. The ratio of short-term bonds in the JGB Market Issuance decreased from the initial 37.6% for FY2021 to 34.9%. When compared to the situation before the outbreak of COVID-19, the ratio is still high. However, we believe that we have taken the first step towards normalization.

- Regarding changes in the outstanding amount of JGBs, the total JGB issuance size was reduced as a result of the supplementary budget for FY2021. However, since the Newly-issued Bonds was

increased significantly, the outstanding amount of ordinary government bonds excluding FILP Bonds is estimated to stand at ¥1,004.5 trillion at the end of FY2021.

- Regarding the average term to maturity, although it was significantly shortened on a flow basis in FY2020 to deal with COVID-19, it has been corrected gradually since then. On a stock basis, although it was shortened a little in FY2020, no significant change has been seen.

- When the average term to maturity on a stock basis is compared to that of other countries, the average term to maturity of JGBs is comparatively high among industrialized nations except United Kingdom.

- Regarding the current issues about the Debt Management Policy, its basic policy is (1) to ensure capital funding through secure and smooth issuance and (2) to control the medium-to-long term funding costs. To that end, it is our rule to conduct a careful dialogue with the market. We will keep such policy also in the future.

- When the JGB issuance size in the future excluding FILP Bonds and Reconstruction Bonds is estimated based on the assumption that the ratio of the composition of maturities in the issuance plan of the initial budget for FY2021 will be maintained even from FY2022 onwards based on the medium- to long-term estimation by the Cabinet Office, it is expected that short-term bonds will continue to be issued at a significantly high level from the next fiscal year onwards, with the proviso that the medium- to long-term estimation by the Cabinet Office is the figure in July of this year and this supplementary budget is not included. As a result, it is expected that the amount of refinancing bonds and the total issuance size will continue at the current level in the future.

- Therefore, although we will need to remain vigilant of a variety of economic situations in the future, we believe it necessary to consider the composition ratio of issue maturities based on market needs in the phase in which the total issuance size can be reduced like in this supplementary budget, while controlling the issuance size of refinancing bonds through the reduction in amount of short-term bonds with an increased issuance.

- As regards the shape of the current yield curve of JGBs, it shows a slight slackening in supply and demand for 20-Year and 30-Year Bonds in a relative manner.

- Regarding the purchase trends of JGBs by the Bank of Japan (BOJ), according to the ratio of purchase of JGBs by the BOJ, while the ratio of purchase of JGBs with a maturity longer than 10

years in particular has been on the decline since the introduction of the yield curve control, the ratio of purchase of JGBs with a maturity between 1 year and 10 years still stands at around 60 %. According to the year-on-year change from the same month last year in the amount outstanding of JGBs held by the BOJ, it is currently on the decline. As seen in the discussions on the modality of government debt in June this year, it is necessary for us to consider the effects of the monetary policy of the BOJ and attitude towards the purchase of JGBs on the JGB market and interest rates.

- While the BOJ has increased the holding ratio of JGBs, financial institutions have decreased its ratio in recent years. However, they have currently increased its ratio slightly. This is considered to be due to the increased collateral demand.

- Regarding life insurance companies, although the amount of JGBs held by them has almost remained unchanged, it is currently on the rise. As far as the maturity is concerned, the ratio of JGBs with a remaining maturity longer than 10 years is large in line with the duration on the liabilities side.

- Regarding regional banks, although the amount of JGBs held by them has been declining, it is currently on the rise. As far as the maturity is concerned, the ratio of JGBs with a remaining maturity longer than 10 years has significantly increased.

- Regarding individual investors, the issuance size of JGBs for individual investors for FY2021 has been decreased due to the effects of the COVID-19 pandemic and a decreased impact of the campaign for the revision of the fee structure implemented by securities companies since October last year. On the other hand, regarding the redemption amount, although the amount of redemption before maturity has decreased due to the decreased issuance size of the preceding fiscal year, since the redemption amount on maturity has increased compared to that of the preceding year, the redemption amount has increased as a whole.

- We prepared randomly 2,000 patterns of maturity composition of interest-bearing bonds based on the ratio of the composition of maturities in the initial issuance plan for FY2021 and conducted a cost-at-risk analysis on the relationship between cost and risk, and it was found that when compared to the case in which the initial plan for FY2021 was left unchanged, (1) both cost and risk for 20-Year Bonds and 2-Year Bonds would decrease when the issuance ratio was decreased, and (2) both cost and risk for 10-Year Bonds would decrease when the issuance ratio was increased.

- Regarding the JGB Issuance Plan for this fiscal year, the current basic idea of the debt management office is as stated in The Advisory Council on Government Debt Management held in June this year, and it consists of (1) planning to decrease short-term bonds in the future for the purpose of stable issuance and purchase because the ratio of the market issuance of short-term bonds has increased to about 40% in response to COVID-19; (2) of planning to decrease short-term bonds by controlling the total amount of JGB issuance without increasing the amount of interest-bearing bonds following the decrease in the amount of short-term bonds; and (3) of increasing the number of investors because of the expansion of the market of 40-Year Bonds. It is considered important to examine the possibility of issuing JGBs monthly and shifting the auction method to the conventional method (discriminatory price auction) in the case where the increase in the number of investors has been confirmed and the amount will be increased further.
- When the background of the expansion of the 40-Year Bonds market and that of the 30-Year Bonds market are compared to each other, it has been 14 years since 40-Year Bonds were issued for the first time in 2007 and its market scale has grown to be mature. However, they are handled differently from other bonds, such as that they are auctioned 6 times a year.
- Regarding changes in the spread in ultra-long-term bonds, the 40 to 30-Year Bonds spread fluctuated roughly at 2 to 3bps in the last fiscal year. Although it increased temporarily to about 9bps in this fiscal year, currently it fluctuates at about 4 to 5bps.
- Regarding the status of the Liquidity Enhancement Auctions for bonds with a remaining maturity of 15.5 to 39 years, many of 20-Year Bonds, 30-Year Bonds and 40-Year Bonds with a remaining maturity similar to that of current issues are sold, and, for example, ¥60 billion of bonds with a remaining maturity of 38 to 39 years are sold in one auction as an average.
- Regarding the bid-to-cover ratio for the Liquidity Enhancement Auctions, that for bonds with a remaining maturity of 1 to 5 years has fluctuated by 4 times or more this year and 5 times or more currently, and that for JGBs with remaining maturities of 5 to 15.5 years fluctuates also by around 4 times, while that for some bonds with a remaining maturity of 15.5 to 39 years fluctuates by about 2 times.
- According to the financial system report of the BOJ, the amount of interest rate risk on yen-denominated bonds held by financial institutions is at the same level as that of the peak in the past. Since the increased spread of COVID-19, all types of businesses have increased their investment position along with an increase in deposit inflow against the backdrop of the expansion of

government spending, and the amount of risk has been increasing, consequently. It is necessary to bear in mind that the increase in the amount of interest risk may trigger the risk of sharp rise in interest rates.

- Regarding the revision of the bidding responsibility of JGB Market Special Participants, in order to ensure secure and smooth issuance of JGBs, we would propose to change the current "amount equal to 5% or more of the planned issuance size of the JGB" for "100 / n% or more of the planned issuance size of the JGB when the number of JGB Market Special Participants is n". We plan to apply this measure from the beginning of FY2022 after considering the details of the system, such as the handling when the percentage is not divisible, notification period, etc.

▶ Summarized below are the views and opinions submitted by participants.

- Regarding the issuance plan for the next fiscal year, we will talk about three points. The first point refers to 40-Year Bonds. The bimonthly issuance size has been increased by ¥100 billion in this fiscal year. However, the supply and demand balance continues to remain tight, and we believe it desirable also for the market that the issuance size be further increased. Since there is a significant difference in liquidity between the month in which they are issued and the month in which they are not issued under the current bimonthly issuance system, we believe it desirable that the current bimonthly issuance is shifted to the monthly issuance of ¥400 billion x 12 times even if the total issuance size increases slightly.

The second point refers to Inflation-Indexed Bonds. Investment in Inflation-Indexed Bonds has increased across the world under the worldwide increased inflationary environment. The current issuance size of ¥200 billion per auction is the reduced amount to deal with COVID-19, and the bidding situation in the last auction was considerably strong. In light of the demand by foreign investors at the counter of our company, we believe it appropriate that the issuance size per auction of the next fiscal year is returned to ¥300 billion.

The third point is Liquidity Enhancement Auctions. We have the impression when we buy and sell JGBs that the liquidity of the current JGB market has been declining focused on off-the-run issues due to the monetary easing by the BOJ for a long period of time. Although we asked for an increase in the amount of Liquidity Enhancement Auctions strongly in the last fiscal year to no avail, we would like to see it increased in the next fiscal year without fail. As is seen in the material of the debt management office, the bid-to-cover ratio for bonds with a remaining maturity of 1 to 5 years or shorter is particularly very strong. As such a situation that it is considerably difficult to buy them continues, we would like to see that the issuance size be increased decisively. Although we understand the difficulties involved, we believe it more desirable for the secondary market of

JGBs that Liquidity Enhancement Auctions which are implemented in three different sectors with JGBs in the short-term sector and in the ultra-long term sector auctioned bimonthly will be conducted every month. As we think that there is room for reduction in the amount of 2-Year Bonds, we believe that if the issuance size of currently issued 2-Year Bonds is reduced and the issuance size of Liquidity Enhancement Auctions is increased, the liquidity of the JGB market will be considerably improved.

- We want to discuss mainly on one issue. We would like to see an increase in the issuance size of 40-Year Bonds as far as the issuance plan for the next fiscal year is concerned. The spread increased temporarily due to a sense of uncertainty when the amount per auction was increased to ¥600 billion. However, according to the data of the debt management office, they have been very stably issued in the end. In addition, there are inconveniences in bimonthly issuance such as the difficulty for traders to cover, biased supply and demand, etc., and its liquidity is inferior to that of 30-Year Bond. Therefore, we believe it desirable that the issuance size is increased and issued every month.

Since contracts are executed at an unexpectedly high price sometime in the current yield-based uniform price auction system, we think that actually volatility is produced unnecessarily. When considering that it has been a considerable time from the start of their issuance, we wish that their auction method is shifted to the discriminatory price auction like other maturities in order to reflect the overall demand of the market. Currently, the market of 40-Year Bonds depends on the demand of a part of end investors. However, if an environment which improves liquidity more than ever before is built, we believe that, not only RV investors, but also end investors who are mainly investing in 30-Year Bonds may be directed to investing in 40-Year Bonds. Therefore, we would like to see that the issuance size is increased and the auction system is shifted to the discriminatory price auction.

Regarding other maturities, we have no special request. However, we are of the view that the issuance size of bonds with a remaining maturity of 1 to 5 years may be increased due to strong demand for them both in Japan and overseas.

- In these recent months, there have been speculations about whether or not JGBs will be increased by the previous additional economic measures. The main scenario was that if they were increased, they would be issued mainly in the form of short-term bonds and their amount would be reduced thereafter. In the circumstances, the speculation was about whether or not there was room for an increase in interest-bearing bonds.

The view of our company is that the situation is different between bonds with a maturity shorter than 10 years and longer than 10 years. As seen in the data provided by the debt

management office, bonds with a maturity shorter than 10 years still continue to strongly depend on the BOJ's purchase. Therefore, from the perspective of whether or not there is an intrinsic demand or investors truly demand for 10-Year Bonds or shorter, we are of the view that there is no intrinsic demand for these bonds.

On the other hand, the BOJ bought a considerable amount of 10-Year Bonds or longer in the past and its purchase has decreased gradually. However, currently, when compared to bonds with a maturity shorter than 10 years, the BOJ's purchase is very small and the market of JGBs of 10 years or longer has remained stable. Therefore, we believe that it can be said in terms of bonds with a maturity shorter than 10 years and longer than 10 years, there is room for an increase in bonds longer than 10 years. Among these, when 20-Year Bonds, 30-Year Bonds and 40-Year Bonds are compared to each other, we conclude that the priority is for 40-Year Bonds. When considering that the investors' demand for 40-Year Bonds is strong and that the demand for 40-Year Bonds is the strongest in terms of demand among 20-Year Bonds, 30-Year Bonds and 40-Year Bonds, with the proviso that the respective issuance size is different from one another. Therefore, we believe that 40-Year Bonds should be given priority.

On the other hand, regarding 20-Year Bonds and 30-Year Bonds, the spread in 20-Year Bonds has considerably decreased in historical terms when compared to that of 10-Year Bonds. However, since there are many investors who buy 20-Year Bonds by a process of elimination because of the very low yield of bonds with a maturity shorter than 10 years, such a situation occurs. Therefore, when interest rates begin to rise due to a change in the external environment for 10-Year Bonds or a change in the stance of the BOJ's purchase, if the issuance size is increased, we believe that uncertainty in terms of supply and demand will be produced. Regarding 30-Year Bonds, as shown in the table of comparison of the spread between 30-40 Year Bonds and 20-30 Year Bonds, we believe that the spread of 20-30 Year Bonds is maintained to a certain extent. On the other hand, the spread of 30-40 Year Bonds has been on the declining trend historically over the years. Therefore, from the perspective that the spread of 20-Year Bonds is ensured to some extent, the supply and demand balance of 30-Year Bonds is not tight. As a result, we conclude that 40-Year Bonds should be given the top priority.

We believe that one idea is to start with a bimonthly increase of ¥100 billion. However, if the current bimonthly issuance is shifted to monthly issuance in light of the increase in the number of investors in said maturity and the market growth, the monthly issuance size of ¥300 billion obtained by halving the current bimonthly amount of ¥600 billion may be too small as an issuance size per auction and not appropriate for stable issuance. Therefore, if the shift is made, we are of the view that the issuance size of ¥400 billion will be appropriate.

Regarding Liquidity Enhancement Auctions, we have the overall impression that the issuance size and frequency and the market needs are roughly balanced with each other. However, since

the supply and demand balance of some issues in bonds with a remaining maturity of 1 to 5 years is constantly tight, and considering that their most recent auction result has been strong, we would like to see an increase in the issuance size in this zone.

- The new type of virus Omicron is having a relatively large effect on share prices as far as the recent market environment is concerned, but it is not having such a large effect on interest rates. Rather, the low volatility situation continues and we believe that interest rates are not sensitive to changes in the external environment and their functional status is low.

We wonder if the increase in the number of operations by the BOJ and in the volume of transactions at JGB auctions is driven by such a situation.

We have three opinions concerning JGB issuance in the future. The first opinion is related to the issuance of 40-Year Bonds. Some of our clients say that the liquidity is low under the current issuance frequency and size and they cannot buy the necessary amount and tend to buy on dips. In the last auction, the volume by bidding increased and the bidding prices become higher than expected, which may affect the inventory. Therefore, we believe it the right way to increase the issuance size of 40-Year Bonds.

Most recently, the spread of 30-40 Year Bonds is about 4 to 5bps and it fluctuated roughly between around 1 to 8 bps, while the spread of 20-30 Year Bonds is currently about 20bps. When considering that it fluctuates between 30 to 20bps, we wonder if it is possible to increase the number of investors through an increase in interest rates on 40-Year Bonds and an increase in the spread of 30-40 Year Bonds by increasing their issuance size. For the time being, we would like to propose to shift from the current bimonthly issuance of ¥600 billion to ¥700 billion or to a monthly issuance of ¥400 billion.

The second opinion is related to Liquidity Enhancement Auctions. In particular, the needs based on the Asset Swap Spread (ASW) from overseas investors are very high for bonds with a remaining maturity of 1 to 5 years. There are many issues whose supply and demand in the debt credit market is very tight and many issues are traded at -20 to 30bps. Since it is difficult in many occasions to buy back these issues in the frequency of once in every two months, we believe it necessary that the bimonthly issuance of ¥400 billion be increased at least to ¥500 billion.

The third and final opinion is related to Inflation-Indexed Bonds. We believe that this issue will be discussed in the next Meeting of JGB Market Special Participants. The debt management office buys about ¥50 billion every month through Buy-back Auctions. The amount of purchase relative to the issuance size is very large, when Outright Purchase of JGBs is added. Since Inflation-Indexed Bonds are bought almost every day also in the transactions for Securities Lending Facility by the BOJ, it is an option to increase the issuance size, but, it is necessary to reduce Buy-back Auctions for the time being.

- Regarding the JGB issuance plan, we would like that the issuance of 40-Year Bonds be increased. When looking at the supply and demand balance in the ultra-long-term zone and the spread of 30 to 40-Year Bonds and the spread of 20 to 30-Year Bonds, currently, the supply and demand balance of 40-Year Bonds is remarkably tight and we believe that there continues to be room for an increase.

Specifically, we wonder if this is not the right time to shift from the bimonthly issuance of ¥600 billion to a monthly issuance of ¥400 billion. However, as we recognize that the overall supply and demand balance of ultra-long-term bonds is slightly slackened, we also believe that it may be an option to reduce the amount of 30-Year Bonds when the amount of 40-Year Bonds is increased.

- Regarding 40-Year Bonds, we believe it desirable that they are issued 12 times in a year in an amount of ¥400 billion each time. However, this does not mean necessarily that the current bimonthly issuance of ¥600 billion is bad. This is due to the fact that although the current demand by life insurance companies to comply with the ICS by 2025 is strong for the time being, it is difficult to see whether or not the same situation will continue afterwards. We are of the view that the amount increase is an option, but it is not a must.

Regarding Inflation-Indexed Bonds, we have no particular comment.

Regarding Liquidity Enhancement Auctions, we are of the view that the supply and demand is also well balanced at the current issuance size.

Regarding the overall market, we believe that, not only that interest rates on 10-Year Bonds are strictly controlled by the yield curve control, but also interest rates on ultra-long-term bonds which are not subject to Outright Purchase of JGBs are also controlled or gradually rise if they rise without any sharp rise due to the current position of the 10-Year Bond yield. Regarding deflation, it is a dominant view that the inflation rate will not rise in Japan. However, the CPI may rise fueled by pent-up demand and when this occurs, since we believe that 10-Year Bonds will react in the market, it will be desirable to increase the issuance size of ultra-long term bonds for which the demand remains.

- We believe that 40-Year Bonds have a high priority for amount increase and they should be issued 12 times in a year in an amount of ¥400 billion each time. However, since this means an increase of ¥1.2 trillion in a year, the supply and demand balance may be considerably affected, and if the amount of 30-Year Bonds is decreased instead, there is a possibility that the supply of 30-Year Bonds will become deficient. In addition, what will be affected most will be Liquidity Enhancement Auctions of bonds with a maturity of 15.5 years or longer. Currently, an average monthly amount of ¥400 billion is issued between Liquidity Enhancement Auctions and 40-Year

Bonds. If 40-Year Bonds alone are issued monthly in an amount of ¥400 billion, the already low bid-to-cover ratio for Liquidity Enhancement Auctions will further decrease and their demand and the demand for 40-Year Bonds may damage each other. If 40-Year Bonds are auctioned every month, they overlap with Liquidity Enhancement Auctions every other month and we are concerned with those occasions. Therefore, instead of increasing ¥1.2 trillion all at once in a year, it may be an option to reduce the amount of JGBs of Liquidity Enhancement Auctions with a remaining maturity of 15.5 years which are conducted every other month by ¥100 billion. And, we believe that it is possible to improve distortions among sectors by assigning the reduced amount to bonds with a remaining maturity of 1 to 5 years of Liquidity Enhancement Auctions.

- Regarding the supply and demand situation of bonds with a maturity of 20 years or longer, since the demand by life and non-life insurance companies is strong in particular for bonds with a remaining maturity of 25 years or longer, we do not think there is any problem in a monthly increase of ¥100 billion. Regarding the frequency of auctions for 40-Year Bonds, we are of the view that there is no need necessarily for issuing them monthly because their monthly issuance overlaps with Liquidity Enhancement Auctions of bonds with a remaining maturity of 15.5 years and a bias in the balance of supply and demand may occur. Regarding the auction system, there are voices in favor of the shift to the discriminatory price auction. However, when considering that the number of overseas investors who give us orders for firm purchase has been increasing in recent years, we believe it appropriate that the Dutch auction system be maintained for bonds of other maturities as well.

Regarding Inflation-Indexed Bonds, the current topic is the inflation and we believe that their amount needs to be increased in the future and that there is room for an increase from the middle of the fiscal year. However, we consider it a priority to reduce the buy-back amount.

Regarding bonds with a remaining maturity of 10 years or shorter, since they are under the yield curve control, we consider that there is no problem even if their amount is increased to some extent. Since the BOJ may choose to increase the amount of JGB purchase in some cases, we consider it not appropriate to reduce the amount.

Regarding Liquidity Enhancement Auctions, since the supply and demand balance becomes tight for JGBs with a remaining maturity of 1 to 5 years, we consider it appropriate to increase their amount.

- Regarding the JGB market situation, we have the impression that it is steady because of the efficacy of the yield curve control when compared to overseas interest rates. Due to the announcement made by the BOJ in March on “the operation for the purchase of long-term JGBs for the time being”, we have the impression that market participants do not need to think about

the possibility that the BOJ will intervene unexpectedly in the JGB market and they follow the trends of overseas interest rates more obediently.

As regards the outlook of the JGB market in the future, we consider that 10-Year Bonds will fluctuate in the range of 5 to 10bps. Variations in overseas interest rates will affect yen interest rates in the future and the market situation will vary depending on the JGB issuance plan. We believe that it is the market consensus that there will be no significant increase in the JGB issuance plan for FY2022 due to the reduction in refunding bonds and increase in tax revenues.

Regarding the JGB issuance plan for FY2022, the number of JGB Market Special Participants has decreased to 20 companies. Since the increase in the JGB issuance size of FY2020, it is a pure fact from our point of view that there are some issues that make us uneasy before the auctions whether or not they are absorbed at an appropriate level, and actually, there are auctions in which tails appear. There is a talk about shifting the auction of 40-Year Bonds to a monthly auction. Securities companies may consider that they are not comfortable with the shift in terms of liquidity. Since the bid-to-cover ratio of 40-Year Bonds which have been increased in issuance size remains at about 2 times, it is doubtful whether or not if the total amount can be absorbed by the market, that is, by investors after the auction if the issuance size is increased to ¥400 billion x 12 times. We will have difficult time if interest rates fluctuate considerably, and if the market of 40-Year Bonds collapses, that of 30-Year Bonds and 20-Year Bonds may also collapse. As a result, we are of the view that this step should be taken cautiously. Since it is unknown how COVID-19 will affect the market in the future, we consider that it is more appropriate to shift the uniform price auction system to the discriminatory price auction gradually instead of shifting all at once.

Regarding short-term bonds, their amount was reduced in the JGB issuance plan for FY2021 and the average term to maturity has been lengthened to a certain extent, which is a matter that needs to be achieved in the medium term. On the other hand, currently, there are plenty of collateral needs and short-term interest rates have considerably dropped due to the tight supply and demand balance, which may change depending on COVID-19 in the future. We consider that it is also an option to reduce short-term bonds when the amount of operations change or collateral needs decrease when the end of COVID-19 is in sight. We have the impression that the reduction speed of the issuance size of short-term bonds is too fast. However, we understand that there are a variety of views on matter. If it is necessary to reduce the amount of short-term bonds, we think it possible to make adjustment by increasing the amount of bonds with a remaining maturity of 1 to 5 years of Liquidity Enhancement Auctions.

- Regarding the JGB issuance plan, ultra-long-term bonds are difficult for us to manage from the perspective of ALM and risk management because of the type of industry we are in. Of course, we partially invest in or hold 20-Year Bonds. However, considering the environment we are in

currently, we find it difficult to include them as a target for investment, and we are content with the status quo.

On the other hand, although it is difficult for us to acquire mid-term or short-term bonds at negative interest rates to meet deposits, since a certain demand continues to exist for collateral needs, we want that their amount will be increased. However, we consider it inevitable to reduce the issuance size of short-term bonds when considering the need to lengthen the maturity of JGBs for continuing their stable issuance. We believe it sufficient that the reduction in the issuance size of short-term bonds is carried out gradually instead of reducing them all at once.

Regarding Liquidity Enhancement Auctions, we use them for their ease of use and consider that the increase in the amount of Liquidity Enhancement Auctions is priority to the increase in the issuance size of interest-bearing bonds.

As far as the overall market is concerned, interest rates of JGBs remain stable despite the topic of global inflation and interest rate rise overseas, and we recognize that the qualitative and quantitative monetary policy is effective by the large scale purchase of the BOJ. Outright Purchase of JGBs does not only affect the level of interest rates, but also liquidity in a significant manner for the ease of their handling at the time of issuance. Although we have a feeling of security in that sense, we are watching very carefully how long this policy will continue with the end of the term of the president of the BOJ in sight.

- Almost everybody wants an increase in amount of 40-Year Bonds. We believe that is alright. However, the opinion of companies with a large number of successful bids should be given priority and if they agree to it, we believe that the amount may be increased. According to the recent auction results, the results of Inflation-Indexed Bonds and 40-Year Bonds which are conducted under the yield uniform price auction method were very strong. Since we believe that they are strong because their auctions are conducted under the yield uniform price auction method, we strongly favor the shift to discriminatory price auction on this occasion.

Regarding Liquidity Enhancement Auctions, it seems according to other market participants that the demand for them is strong, we would like to see an increase in amount in the same manner as others.

Regarding bonds with a remaining maturity of 10 years or shorter, since they depend on the purchase by the BOJ, regardless of whether they are increased or decreased, the remainder in the market will be purchased by the BOJ, the outcome is not greatly affected in the end.

- We would like to refer to liquidity and 40-Year Bonds.

Regarding 40-Year Bonds, the number of investors has been increasing since the last fiscal year due to increased needs for real money both in Japan and overseas, which is seen even at the

counter of our company. In line with such increase, people who use the yield curve to make predictions and use this information to make their investment decisions are participating and thus, the number of investors has been on the rise qualitatively and quantitatively. Although we believe that there will be no problem in increasing the amount, we consider it more appropriate to wait and see how it goes by increasing ¥100 billion every other month for the time being, instead of shifting to a monthly issuance of ¥400 billion all at once. The current situation is such that the amount was increased once in this fiscal year resulting in an increase once and a decrease once in the spread. The current issue is the shift to a monthly issuance and to the discriminatory price auction system, and we believe it appropriate that the shift is made gradually.

Regarding Liquidity Enhancement Auctions, the needs for bonds with a remaining maturity of 1 to 5 years are particularly strong and we believe that the needs for bonds with a remaining maturity of 5 to 15.5 years are also strong. Regarding whether or not there is room for increase in amount, there is room for increase in amount for Liquidity Enhancement Auctions. On the other hand, if their amount is increased while maintaining the total amount, we consider that the increase in amount of Liquidity Enhancement Auctions while decreasing the amount of either 2-Year Bonds or 5-Year Bonds will contribute to stable issuance and provision of liquidity in the market.

In addition, the bimonthly issuance does not allow us to cover all our requirements. Therefore, although we understand the difficulties involved, if Liquidity Enhancement Auctions are conducted monthly for all maturities, this will contribute to the stability of the market.

- We agree to the reduction of short-term bonds. Regarding Liquidity Enhancement Auctions, we believe that there is room for increase in bonds with a remaining maturity of 1 to 5 years. Regarding Inflation-Indexed Bonds, we are of the view that the first thing to do is to reduce the amount of Buy-back Auctions rather than increasing the amount, and the increase in amount will come afterwards.

Regarding the ultra-long term zone, we are of the view that the issuance size of 20-Year Bonds, 30-Year Bonds and 40-Year Bonds may be left unchanged. Unlike the last fiscal year, the tapering and early increase in interest rates are expected in overseas market, whereas the number of Outright Purchase of JGBs in the ultra-long term zone has been reduced to once a month and thus, the market is comparatively stable in this fiscal year. However, since it is unknown when the deterioration in the supply-demand balance will occur or the market will deteriorate significantly, we believe that the increase in the issuance size of ultra-long term bonds should be considered carefully.

According to the market of this fiscal year, as far as 40-Year Bonds are concerned, the difference between the spread of the issue number 13 issued in the last fiscal year and the spread

of the issue number 14 issued in this fiscal year is gradually increasing. Although some other participants expressed the view that there is a strong demand for 40-Year Bonds, the current issues of 40-Year Bonds are comparatively cheaper than the preceding off-the-run issues. As described by the debt management office, the spread of 30-40-Year Bonds in the last fiscal year moved in the range of 2 to 3bps. Since the spread of both the issue number 13 and that of the issue number 14 are already over 1bps, we do not believe that the demand for current issues of 40-Year Bonds is necessarily strong.

According to Liquidity Enhancement Auctions of ultra-long-term bonds in this fiscal year, investors seemingly refrained from tending a bid for fear of an increase in issuance size in April. However, bonds with a remaining maturity of 35 to 39 years were issued in an amount of ¥150 billion each time in Liquidity Enhancement Auctions in June, August and October. Consequently, we wonder if there continues to be a certain demand for off-the-run issues.

The main target of investment for life insurance companies are 30-Year Bonds. Although the supply-demand balance of off-the run issues of 30-Year Bonds has weakened, when considering that the demand for current issues of 30-Year Bonds is comparatively strong, we may think that the demand for 30-Year Bonds by investors is strong. Therefore, when the plan to shift the bimonthly issuance of 40-Year Bonds to monthly issuance of ¥400 billion x 12 times that is currently discussed is put into practice, there will be an issue whether the issuance size of 30-Year Bonds or of Liquidity Enhancement Auctions is reduced over concerns about the supply-demand balance of ultra-long term bonds. We are of the view that it is currently impossible to reduce the amount of bonds with strong demand and increase the amount of current issues of 40-Year Bonds with less demand and issue monthly in an amount of ¥400 billion x 12 months. Although we agree on making a shift to monthly issuance and discriminatory price auction as a general rule, we believe we had better settle to the bimonthly issuance of ¥700 billion, that is, an increase of ¥100 billion per auction at this stage under the current supply and demand environment.

- We do not request an increase in the issuance of 40-Year Bonds and we request an increase in the issuance size of bonds with a remaining maturity of 5 to 15.5 years instead of bonds with a remaining maturity of 1 to 5 years as far as Liquidity Enhancement Auctions are concerned. Regarding an increase in the issuance size, roughly speaking, since JGBs with a remaining maturity of up to 10 years are under the yield curve control of the BOJ, if they are increased, the BOJ will have to buy them, if they are reduced, the BOJ will have to reduce its purchase accordingly. As a result, there is no problem at all in a sense.

However, this is a completely different discussion from the discussion in original sense about the development of the JGB market or the best interest of end investors. In that sense, it is shown in the article “Changes in the BOJ's JGB Purchase Ratio” on the left side of the page 15 of the

material provided by the debt management office that the sound market is only applicable to the market of 10-Year Bonds or longer. We wonder if this means that there is soundness only in supply and demand of 20-Year Bonds, 30-Year Bonds and 40-Year Bonds. If we emphasize this point and if there is a strong demand for an increase in 40-Year Bonds from each JGB market special participant, it may be possible to consider increasing the amount despite the fact that we do not request an increase in 40-Year Bonds.

I'm not going to simplify it, it took 15 years for 30-Year Bonds to be issued monthly from the start of its issuance and it has been 16 years this year since 40-Year Bonds were issued. Therefore, 40-Year Bonds may be naturally issued monthly. However, as haste makes waste, we deem it reasonable to increase the bimonthly amount before shifting to monthly issuance, to shift from the uniform price auction system to the discriminatory price auction and to definitely shift to monthly issuance starting in the next fiscal year.

Regarding the current market situation, bonds with a maturity of 10 years or shorter are protected under the yield curve control. Further, since there is a time structure of interest rates also for ultra-long term bonds, if the yield of bonds with a maturity of 10 years or shorter is fixed, there is no reason why the yield of JGBs in the ultra-long-term zone will rise unilaterally. Therefore, if JGBs in the ultra-long-term zone is increased, there is no serious concern. For example, since there is no such possibility that 40-Year Bonds alone will yield 1 % under the current yield curve, there is room for an increase in the end.

There is currently global concern over inflation. Personally, we believe that the concern is currently maximum and the supply constraint will be eliminated constantly in the future. Even if the yield curve control is effective, the correlation of long-term interest rates between the US and Japan is high, and we are concerned over the long-term interest rates in the US. However, if the inflation extends longer than expected focused on supply constraint under the current environment, the growth rate will drop and the inflation will be basically absorbed by the flattening of the yield curve including some twists. Therefore, we believe that the peak of the US long-term interest rates will not be so high. Since the real interest rate is negative, the issuance size will decrease after the tapering and thus, there is no concern for the time being. However, what worries us the fact that if the real interest rate becomes zero %, there is room for an increase in the yield by 1%. However, even considering these, the essence of the thing is that the yield curve control exists on top of these factors.

The prices in Japan will rise when the effect of the reduction of the mobile phone tariff rates is lost in April next year. However, according to the BOJ's Outlook Report, the BOJ itself says that the yield will not reach 1%. Therefore, we will believe the report of the BOJ.

- We will request an increase in the issuance size of 40-Year Bonds. When doing so, if the

issuance frequency of 40-Year Bonds is changed from bimonthly to monthly, instead of a monthly issuance of ¥300 billion obtained by halving the current amount, we request that a total amount of ¥400 billion per auction be issued by increasing ¥100 billion. In addition, although we have invested in one issue every year so far, since there are clients who want to invest in JGBs with a longer maturity, it is one of our big issues to change to one issue every half a year in the sense to issue a security with a longer duration.

As regards the overall tendency of ultra-long-term bonds, we believe that the purchase amount has been increasing including that by life insurance companies and we expect that the purchase amount of 40-Year Bonds will be further increased in the future. In addition, it was characteristic in the past that the purchase amount varied significantly according to the level of interest rates. However, currently, the purchase amount has been regularized. If they are issued every other month, the market liquidity increases when the auction is held, and the supply-demand balance tightens and the market becomes unstable when the auction is not held. From this perspective, we consider it is important to meet the needs of investors by shifting to the monthly issuance, resulting in stable issuance, and to level the supply-demand balance through monthly issuance and allow investors to plan their investment operations.

Regarding Liquidity Enhancement Auctions, we request that their issuance size be increased. In particular, we request an increase of ¥200 billion instead of ¥100 billion for bonds with a remaining maturity of 1 to 5 years because their supply-demand balance is tight for a very long time. As the background thereof, not only that investors are encouraged to return to JGBs when interest rates rise moderately, but also the number of overseas investors increase and investors' needs diversify. Since there are strong needs for off-the-run issues other than Newly-issued Bonds (Calendar Base), we believe it necessary to increase the amount of bonds with a remaining maturity of 1 to 5 years of Liquidity Enhancement Auctions by reducing, for example, the amount of 2-Year Bonds to level out the outstanding amount in the market and achieve market liquidity by making a good use of Liquidity Enhancement Auctions.

Regarding Inflation-Indexed Bonds, against the backdrop of the current favorable supply-demand balance, their prices have been on the rise and it is hard to believe what is occurring now. However, we do not think that the number of participants in its market has increased. The fact that the number of participants has not increased means that the market is not resilient to a shock. Therefore, we believe it important that the BOJ reduces its purchase amount and control market liquidity in order to develop the market instead of increasing the amount.

Contact:

Market Control Section, Market Finance Division,

Financial Bureau,

Ministry of Finance

03-3581-4111 (ext.5700)