June 22, 2015
Financial Markets Department
Bank of Japan

Minutes of the "Bond Market Group" Meetings on June 11 and 12, 2015

1. Outline

(1) Date	Buy-side group (21 firms)	June 11 at 6:00-7:30 pm
	Commercial banks group (22 firms)	June 12 at 4:00-5:30 pm
	Securities firms group (25 firms)	June 12 at 6:00-7:30 pm

(2) Place The Head Office of the Bank of Japan

(3) Participants

- Persons in charge of bond market issues in financial institutions, participating in the "Bond Market Survey" or the "Meeting with Market Participants"
- Director-General of the Financial Markets Department, Head of Coordination and Market Analysis Division,[1] Head of Market Operations Division, Head of Financial Markets Analysis Group,[2] Head of Market Infrastructure Group

2. Views provided by participants

The Bank explained to each group (1) the results of the "Bond Market Survey," (2) liquidity in the JGB market, and (3) recent developments in the financial markets and market operations. The Bank also exchanged views with participants on these topics.

Views provided by participants are as follows.

Bond Market Survey

- The functioning of the JGB market has stabilized notably, as the May 2015 survey shows.
- Although the May 2015 survey shows that the functioning of the JGB market

[1] Present on the meetings of the buy-side group and securities firms group.
[2] Present on the meeting of commercial banks group.

has improved compared with three months ago, investors have the impression that the degree of its functioning is still low.

- Some investors may be sitting on the sidelines under the current low interest rate environment. This market development may have resulted in the low degree of JGB market functioning shown in the survey, but cannot be properly captured by traditional liquidity indicators.

<u>Liquidity in the JGB market</u>

- The bid-ask spread for 5-year JGBs after the expansion of QQE at the end of October 2014 was wider than that immediately after the introduction of QQE in April 2013. It might be reflecting the changing regulatory environment.

- The bid-ask spread is tight when trade size per transaction is small, but if the size gets larger, it may cause unexpectedly large price movement.

- In the long run, the number of market participants has been decreasing in the JGB market under the current low interest rate environment. In this circumstance, daily market activity seems to depend on whether JGB auctions by the Ministry of Finance or the Bank's outright purchases is conducted.

- Volatility in the JGB market is relatively subdued compared to that in overseas markets.

- Liquidity conditions in the JGB market frequently change, while the level of liquidity remains low. This may be suggesting that under the current low interest rate environment, investors are trying to purchase bonds with as high yield as possible. Therefore whenever there is a slight increase in the yield, it is met with heightened demand by investors, barely contributing to an increase in liquidity.

- "Price impact" indicator shown in the Bank's working paper "Liquidity in JGB Markets" released on March 19, 2015[3] seems to reflect the current liquidity conditions well.

- Our firm reduces the trade size per transaction when market activity is low. For this reason, we don't have the impression that the functioning of the JGB market is impaired.

[3] The English version was released on the Bank's website on May 8, 2015.

- Liquidity conditions in the JGB market are not affecting our firm's operations at present. We should rather focus on the risk of impairment of price discovery mechanism, which can be caused by asset fire-sales under stressed market conditions.

- The Ministry of Finance and the Bank have introduced various measures to address the scarcity of specific issues. Reflecting this, it has become rare for SC repo rates for a large number of issues to become considerably negative at the same time.

- In the exit phase from QQE, one should be aware that some financial institutions may face balance sheet constraints if recent financial regulations become binding.

Market Developments and the Bank's Operations

- Constantly negative short-term interest rates adversely affect a certain type of market participants who invest mainly in T-bills.

- The recent rise in interest rates has been accompanied by an increase in the number of market participants. This situation is different from that in the beginning of this year. Therefore, the current interest rate environment can be accepted with some relief.

- The change in the amount of Bank's outright purchases of JGBs with no monetary policy change could cause an increase in interest rate volatility.

- It would be helpful if the Bank pre-announced the details of the operations schedule, specifying maturity range and purchase amount per auction.

- Since the variety and the number of Bank's operations have increased, our firm has a concern on risk of error when submitting offers.

- Although our firm does not have trouble executing trades at present, the Bank may need to consider measures to ensure liquidity in the JGB market under the environment of heightened interest rate volatility. One option would be the further relaxation in conditions for the Bank's Securities Lending Facility.

- It would be helpful if the Bank increases the amount of outright purchases of inflation-indexed bonds, taking into account the increase in its issuance.

Dialogue with Market Participants

- The Banks' holding forums for dialogue with market participants and sending a message that it is carefully monitoring market developments would be effective in increasing market stability.