June 27, 2019
Financial Markets Department
Bank of Japan

Minutes of the Ninth Round of the "Bond Market Group" Meetings

1. Outline

(1) Date	Commercial banks group (24 firms)	June 10 at 4:00 pm
	Securities firms group (24 firms)	June 10 at 5:30 pm
	Buy-side group (21 firms)	June 11 at 5:45 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"
- Director-General of the Financial Markets Department, Head of Coordination and Market Analysis Division, Head of Market Operations Division, Head of Market Infrastructure Division

2. Introduction by the Bank of Japan

- 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.

3. Views provided by participants

- The Bank exchanged views with participants on the above topics. Views provided by participants are as follows.

<u>Recent trends in the Japanese bond market</u>

- Japanese interest rates have declined since the end of last year due to such factors as declining overseas interest rates. The decline in Japanese interest rates seems to be also attributable to foreign investors' increased investment in JGBs, which reflect the heightening investment attractiveness of JGBs when taking into account currency-hedging costs amid declining U.S. long-term interest rates.

- In addition, the supply and demand conditions of JGBs with a residual maturity of more than 3 years and up to 5 years have tightened while the residual maturity of 10-year JGBs with a reduced market share due to the Bank's purchases since the introduction of Quantitative and Qualitative Monetary Easing has sequentially fell to more than 3 years and up to 5 years. As a result, 5-year interest rates have fallen below 2-year interest rates.

- The yield curve for long- and super-long-term JGBs has flattened due to the significant decline in yields on super-long-term JGBs. This is because, in addition to the continuous demand from life insurance companies, investors who seek to earn carry income have shifted their funds to super-long-term JGBs in view of long-term interest rates remaining in negative territory and the current shape of the short- and medium-term yield curve.

- We would like to continue to pay attention to the impact of the growing presence of foreign investors on the Japanese bond market.

<u>Functioning and liquidity of the Japanese bond market</u>

- With more flexibility in market operations after the Bank's decision to strengthen the framework for continuous powerful monetary easing last July, the degree of functioning in the bond market has improved such that Japanese interest rates, particularly those on long- and super-long-term JGBs, have tended to fluctuate in tandem with overseas interest rates.

- We highly evaluate the measures to relax the terms and conditions for the Securities Lending Facility (SLF) decided at the Monetary Policy Meeting this April, along with the expansion of non-eligible issues for purchases of JGBs with a residual maturity of more than 5 years and up to 10 years, as contributing to enhanced liquidity in the JGB market.

- However, the degree of market functioning has remained low such that it has been difficult to trade in large lots.

- Market-making ability of securities firms has remained low such that securities firms have continued to face difficulty in covering their short positions, particularly in certain issues of JGBs of which the Bank holds a large share.

- Yields on super-long-term JGBs might not necessarily reflect long-run developments in economic activity and prices. This is attributable to the effects stemming from investment funds shifting their funds from long-term JGBs for which yields remain in negative territory, and the decline in yields on super-long-term JGBs driven by the tightening of supply and demand conditions of certain issues.

- While yields on long-term JGBs remain in negative territory, for bonds other than JGBs, the absolute level of yields might be considered as a key factor and it might be difficult to set prices based on creditworthiness.

<u>The Bank's operations</u>

- We expect the Bank to strive to conduct market operations in an even more flexible manner, including by reducing the amount of purchases of JGBs, so that the degree of market functioning and liquidity will improve further.

- Despite the Bank taking initiatives such as the reduction in the amount of purchases of JGBs, particularly super-long-term JGBs, yields on short- and medium-term JGBs have become inverted. Moreover, taking into account the effects of such factors as the tightening supply and demand conditions of JGBs with a residual maturity of more than 3 years and up to 5 years and the yields on long-term JGBs remaining in negative territory, we would like to ask the Bank to reduce the amount of purchases in a balanced manner, including for medium- and long-term JGBs.

- Possible adjustments could include reduced purchases of JGBs, for which supply and demand conditions are tight and deterioration of liquidity is evident, and increased purchases of other JGBs.

- We would like to ask the Bank to continue to reduce the amount of purchases of super-long-term JGBs because yields on such JGBs have declined significantly and supply and demand conditions have remained tight.

- For long-term JGBs, it is necessary to pay attention to the possibility that purchases could increase price volatility because the large amount of a purchase could result in an unexpected outcome.

- With regard to the Bank's market operations such as the purchases of JGBs, we would like to ask the Bank to continue to thoroughly communicate with market participants.