

# Monthly Economic Report

June 23, 2021

Mizuho Research & Technologies, Ltd.

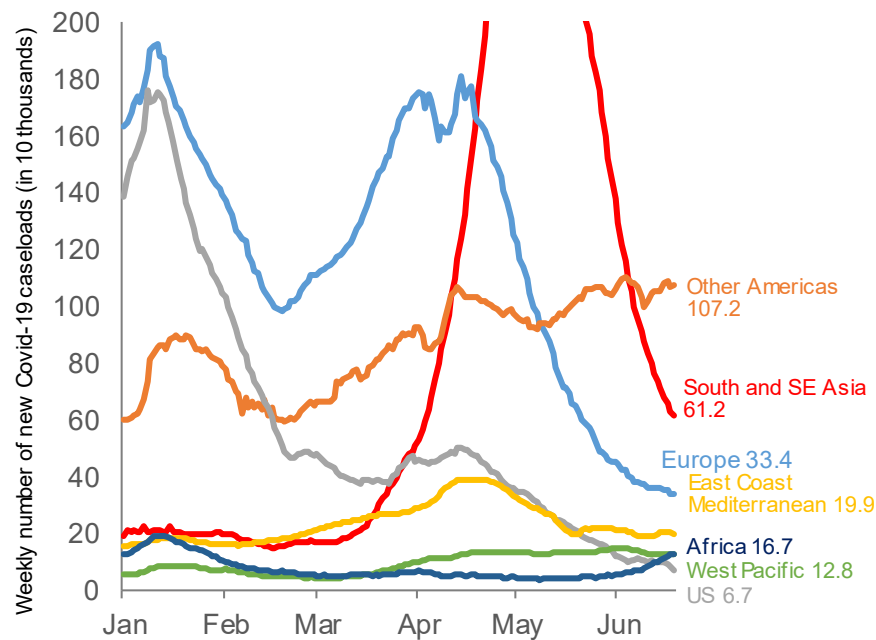
**MIZUHO**

The Mizuho logo consists of the word "MIZUHO" in a bold, white, sans-serif font, positioned above a white, curved horizontal line that resembles a stylized wave or a bridge.

# The number of new Covid-19 cases is continuing to fall

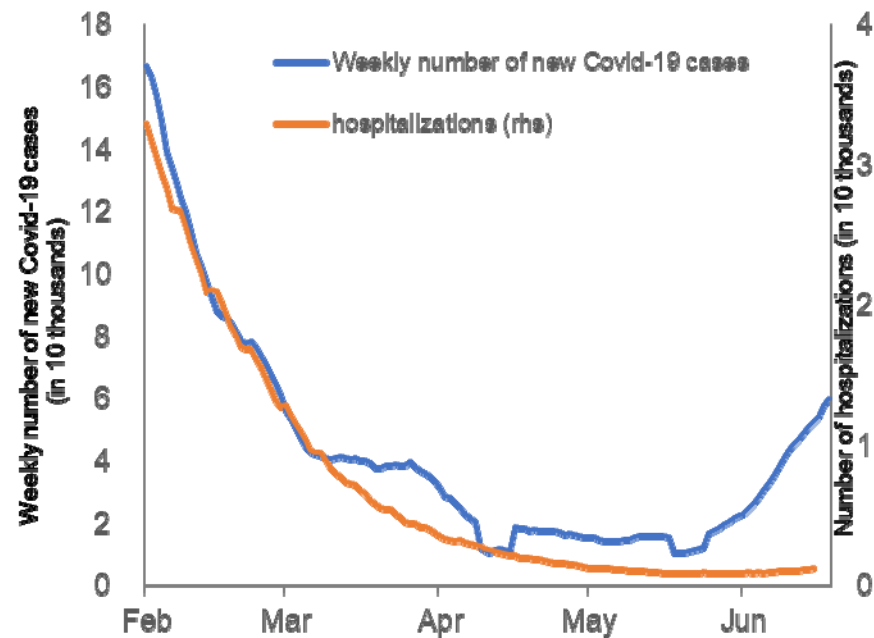
- Global Covid-19 cases (cumulative) reached 178.33 million as of the morning of June 21.
- The number of new Covid-19 cases/week stood at 2.54 million (previous week: 2.7 million), recording an ongoing decline.
  - The fall of cases in India (previous week: 6.64 million → this week: 4.64 million) served to push down the number of new cases. In Europe, while the number of new cases in major countries is falling, new cases are resurging in the UK. In the UK, while the number of new cases is increasing, the burden on medical facilities is limited (due to the effect of vaccinations).
  - In Central and South America, countries such as Brazil and Colombia have not achieved peak-outs. In terms of averages, cases are plateauing. In Africa, there are signs of a resurgence mainly in South Africa.

## Number of weekly new Covid-19 cases reported worldwide



Note: Figures represent number of cases counted as of June 20 (latest data as of June 18).  
 Regional classification based upon the WHO  
 Source: Made by MHRT based upon Johns Hopkins University and WHO

## Weekly number of new Covid-19 cases and number of hospitalizations in the UK

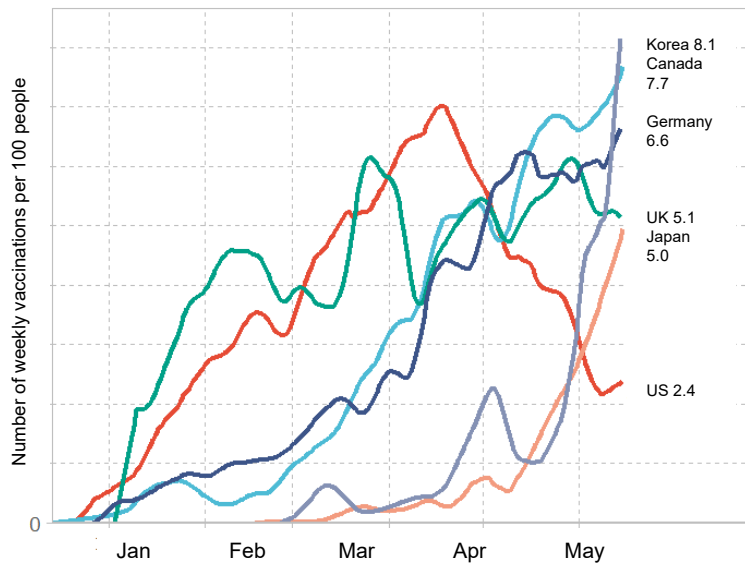


Note: Figures represent number of cases counted as of June 17 (latest data as of June 15)  
 Source: Made by MHRT based upon Our World in Data

# Global vaccination trends show that vaccine rollouts are progressing steadily in Canada and Korea, in addition to major European countries

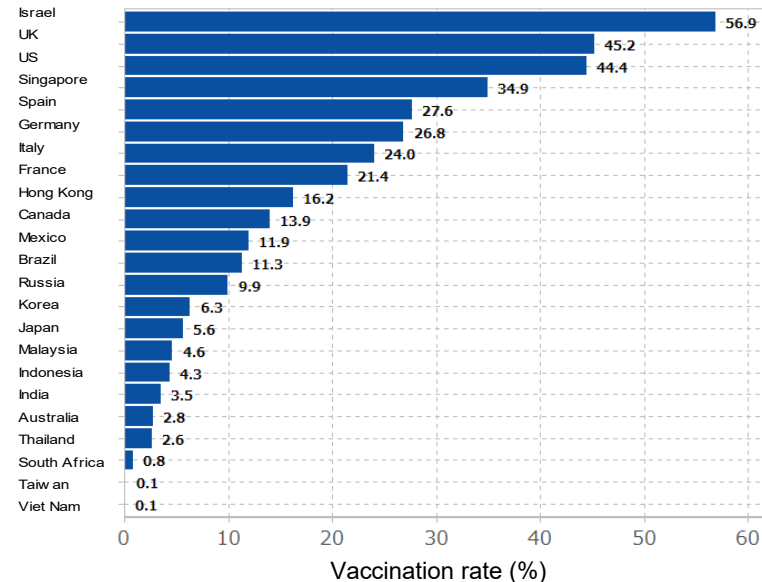
- Overseas, vaccine rollouts are progressing steadily in Canada and Korea, in addition to major European countries.
  - Korea and Canada are progressing at an extremely fast pace, with around eight doses a week per 100 people.
  - In Europe, Germany and the UK maintain a steady pace of five to six doses a week per 100 people.
  - In the US, the pace of vaccinations has slowed significantly, but from mid-June, there are signs that the rate stopped falling to 2.4 doses a week per 100 people.
- The rate of secondary vaccinations is 40% in the US and the UK, 30% in Singapore, and around 20% in major continental European countries.
  - Although the rates are still low in Canada at 10% and in Korea at 6%, vaccinations are progressing at a fast pace, and this is expected to lead to a rapid increase in the percentages of people who have received their second dose.

## Number of weekly vaccinations per 100 people by country



Note: Figures represent data as of June 17 (latest data is from June 15).  
Source: Made by MHRT based upon Our World in Data

## Vaccination rates in major countries (percentage of the total population administered a second dose of vaccine)

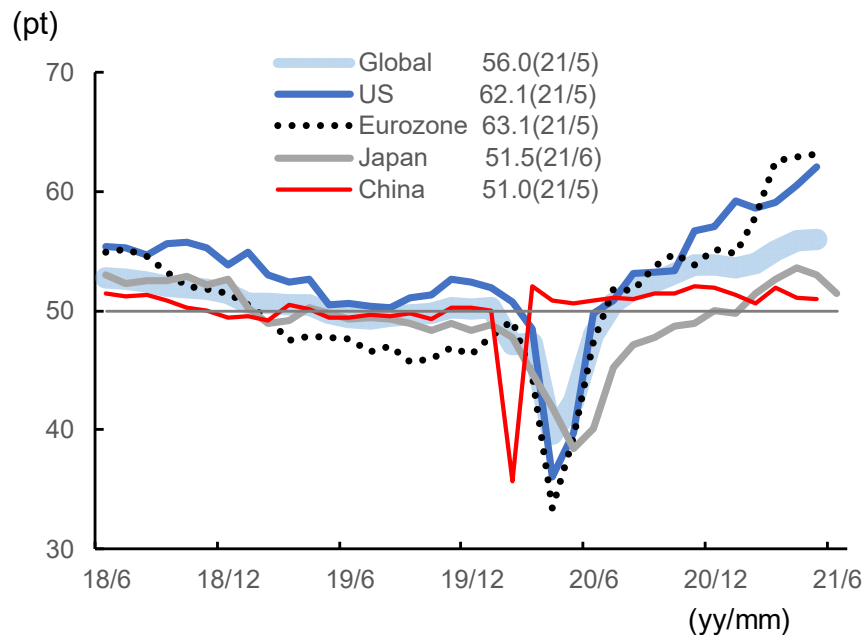


Note: Counted as of June 17 (latest data as of June 15).  
Source: Made by MHRT based upon Our World in Data

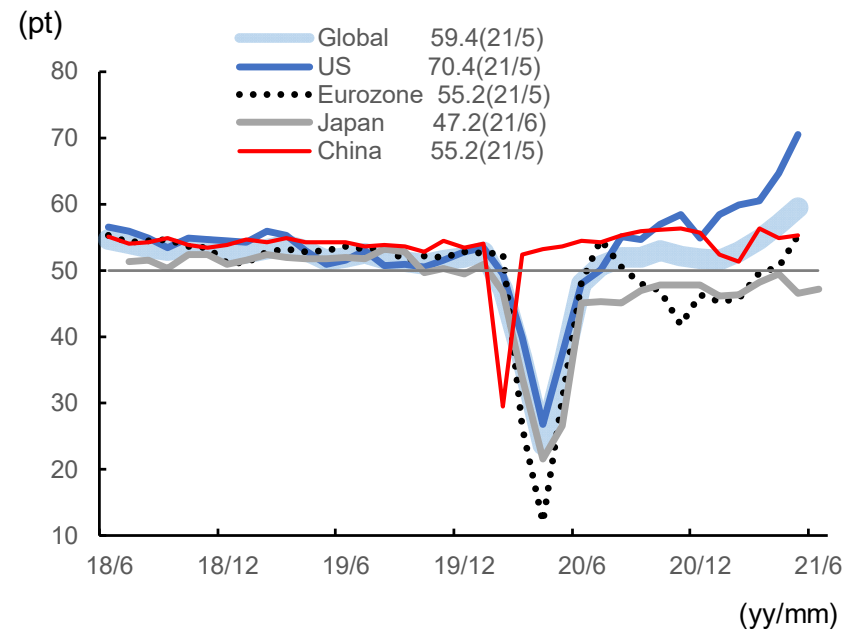
# Current state of the global economy: note a significant expansion of nonmanufacturing business conditions in the US which is serving as the driver of the global economy

- The US economy, one of the main drivers of the global economy, is continuing to follow an expansion track.
  - In the US, the nonmanufacturing PMI in May recorded a high level of 70. Personal consumption, remaining at a high level, shows signs of a shift of consumption from goods services.
- Likewise in Europe, vaccinations are progressing and infection control measures are being eased. Even in the nonmanufacturing sector, where recovery was delayed, the PMI edged up over 50, indicating an expansion trend.
- In Japan, the nonmanufacturing PMI remains below 50 due to the impact of the declaration of a state of emergency. The nonmanufacturing sector is expected to remain sluggish until the progress of vaccination rollouts.

## Manufacturing PMI



## Nonmanufacturing PMI



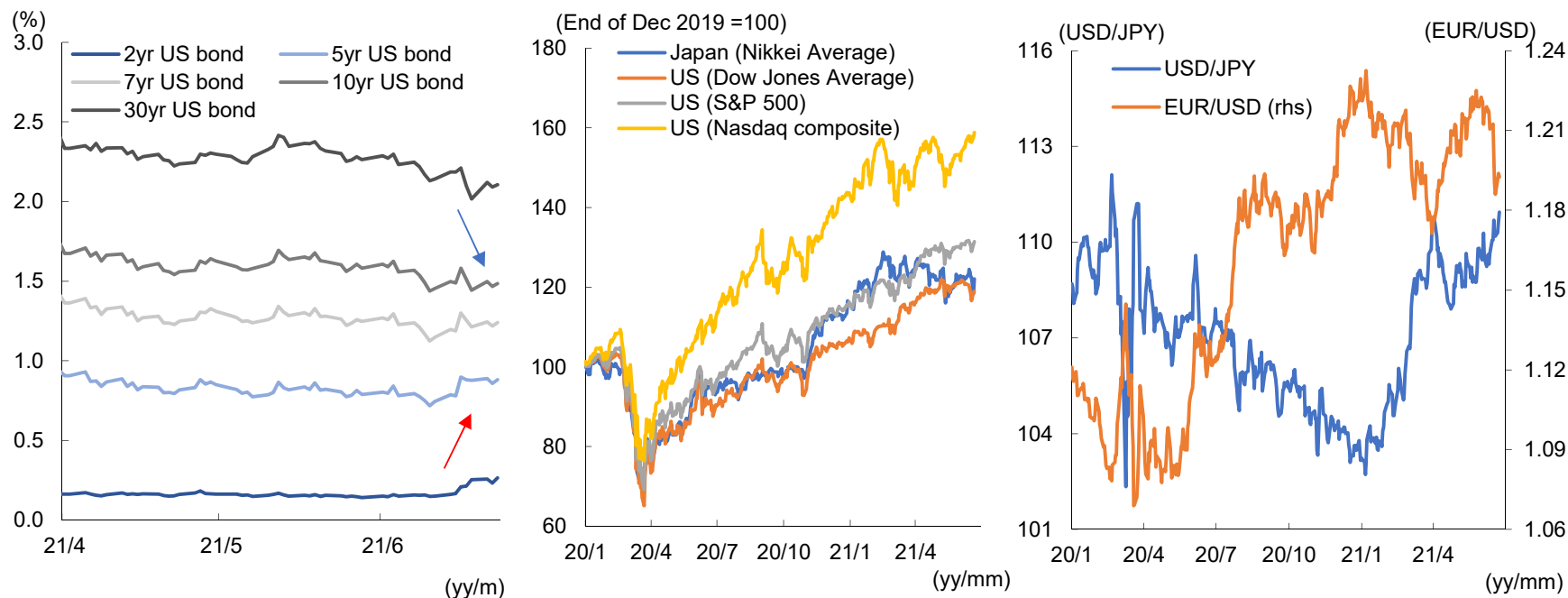
Note: The Purchasing Managers' Index (PMI) is an index calculated by weighting indexes such as new orders, output, order backlogs, prices, employment, and quantity of purchases. The reading of 50 in the PMI is the "expansion-contraction" threshold.  
 Source: Made by MHRT based upon the National Bureau of Statistics of China, Markit Economics.

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 Source: Made by MHRT based upon the National Bureau of Statistics of China, Markit Economics.

# Overview of financial markets: US interest rates twist-flattened reflecting FOMC meeting, stocks faced volatility

- In the policy rate projections announced at the FOMC meeting (held June 15 and 16), expectations for rate hikes in 2022 and 2023 increased. In the financial markets, concerns about early rate hikes strengthened, US interest rates twist-flattened, and stock prices faced volatility.
  - While medium-term US bond yields rose, long-term and ultra-long-term US bond yields fell due to the fall of expected inflation rates and stock prices, etc.
  - The stock market fell sharply, mainly among stocks sensitive to economic conditions, due to concerns regarding speculation on earlier-than-scheduled interest rate hikes. The stock market subsequently turned volatile, including rebounds reflecting the pause in rise of medium-term US bond yields.
  - Even though the dollar strengthened against the backdrop of rising US medium-term interest rates, the dollar strengthening also took a breath due to the pause in rise of US medium-term interest rates.

## Major market trends

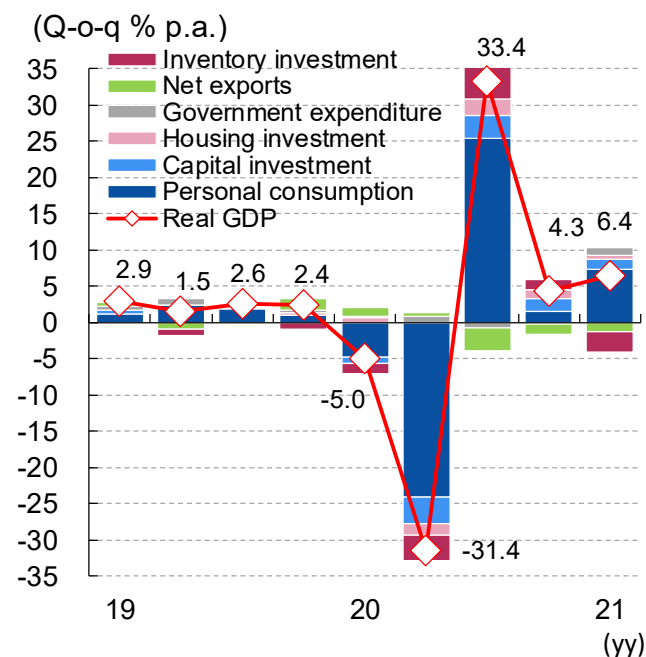


Note: All indexes show actual results up to June 23.  
Source: Made by MHRT based upon Refinitiv

# US Economy: GDP second estimate remains unchanged and reconfirmed that the acceleration was driven mainly by domestic demand

- The real GDP growth rate in the Jan-Mar quarter (second estimate) was +6.4% q-o-q p.a., remaining unchanged from the first estimate.
  - Although domestic final demand is favorable, domestic supply could not keep up, and inventories and net exports remain drawn down. The results reconfirmed that the US economy has accelerated due to policy effects and the relaxation of restrictions.
    - ◆ Upward revisions include personal consumption, housing investment, and capital investment. Downward revisions include inventory investment, net exports, and government expenditure.

## Real GDP growth



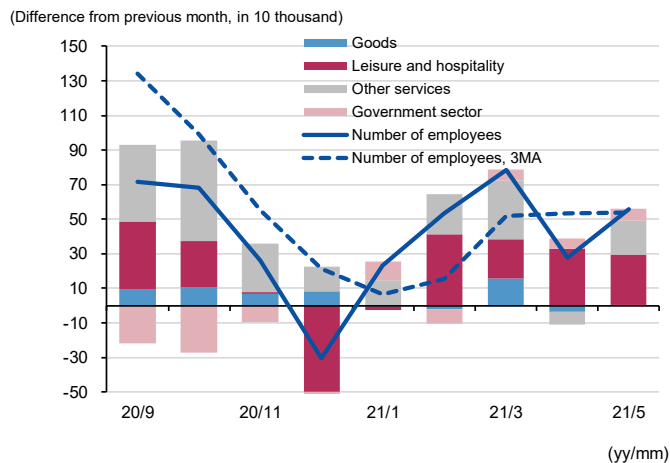
	20Q4	21Q1 (First estimate)	21Q1 (Second estimate)	Key points
<b>Real GDP</b>	+4.3	+6.4	+6.4	Confirmed that the pace of economic recovery in the Jan-Mar quarter accelerated
<b>Personal consumption</b>	+2.3	+10.7	+11.3	Consumption is generally strong, including services requiring face-to-face interactions, against the backdrop of cash benefits, increased employment income, and relaxation of restrictions
<b>Housing investment</b>	+36.8	+10.8	+12.7	Housing construction continues to increase, especially for single-family homes
<b>Capital investment</b>	+13.1	+9.9	+10.8	Machinery investment (especially information-processing related) and intellectual property investment increased significantly. On the other hand, construction investment remains sluggish overall
<b>Inventory investment (※)</b>	+1.4	-2.6	-2.8	Manufacturers and retailers (exclusively car dealers) withdraw inventory amid tight supply constraints
<b>Government expenditure</b>	-0.8	+6.3	+5.8	Significant increase in federal expenditures, especially in small business lending programs (Paycheck Protection Program, PPP) and vaccine related purchases
<b>Net exports (※)</b>	-1.5	-0.9	-1.2	Contribution of external demand is negative due to decreased exports and increased imports
<b>Exports</b>	+22.3	-1.1	-2.9	Decreased mainly in goods. Supply constraints seem to have weighed on production for export-related items
<b>Imports</b>	+29.8	+5.7	+6.7	Imports of consumer goods and capital goods boosted overall, driven by strong consumer goods and machinery investment

Source: Made by MHRT based upon US Department of Commerce.

# May employment statistics confirm that April's sluggishness was temporary. Challenges remain in broadness and inclusiveness

- The growth in the number of employees in May accelerated by +559 thousand (April m-o-m change +278 thousand), but recovery remains unfinished.
  - By industry, the leisure/entertainment industry continues to increase against the backdrop of relaxing restrictions. Goods and services excluding leisure/entertainment also turned upwards.
  - The employment levels are at -7.34 million compared to that of pre-Covid-19. If the pace of the past three months continues, pre-Covid-19 levels will be recovered in mid-2022.
- Looking at a wide range of labor indicators, although job offer and recruitment-related indicators show significant improvements, the employment rate (+0.1% Pt m-o-m) improved only slightly, while the labor force participation rate fell (-0.1% Pt m-o-m). The pace of improvement for various unemployment rates is not uniform, and there is a situation where the improvement of unemployment rates for black people's, etc., is delayed.
  - Excluding job offer and recruitment-related indicators, the degree of improvement in labor indicators in May is limited to 10 to 30%. Challenges remain in broad and inclusive improvement.

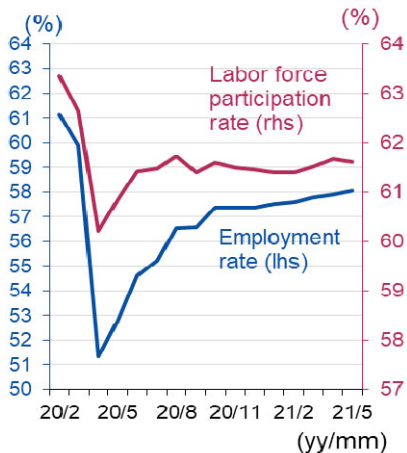
## Number of employees by industry



Note: The degree of improvement is indexed between 0 and 100 in each month of 2021 after setting the level in December 2020 to 0 (red) and the level before the Covid-19 pandemic to 100 (green). Higher numbers indicate improvement.

Source: Made by MHRT based upon US Department of Labor

## Labor force participation rate and employment rate



## Degree of improvement in a wide range of labor-related indicators

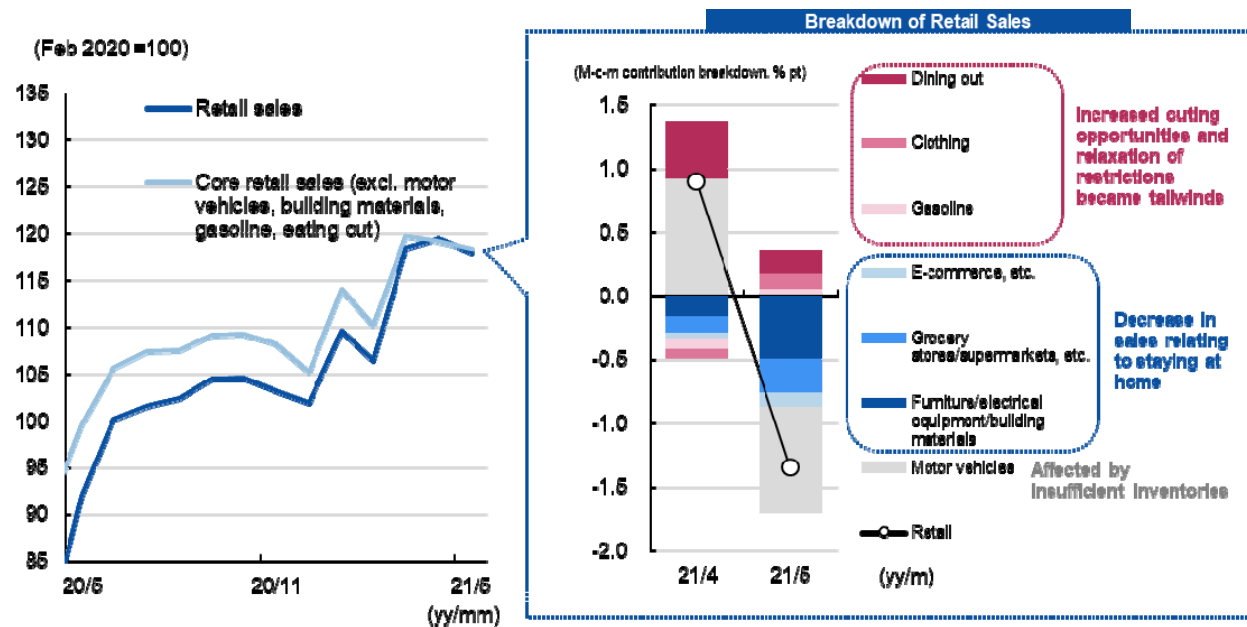
No improvement (red) to Improvement (green)

		2021				
		Jan	Feb	Mar	Apr	May
Corporate behavior	Number of employees	2	8	16	18	24
	Civilian job openings rate	100	100	100		
	Civilian hiring rate	0	100	100		
Employment recognition	Plans to increase employment	0	25	100	100	100
	Job availability	0	8	25	60	100
	Civilian job turnover rate	100	100	100		
Utilization rate	Unfilled job opening rate	0	75	75	100	100
	US: Unemployment rate	13	16	22	19	28
	Black people's unemployment rate	18	0	8	5	21
	Hispanic people's unemployment rate	14	16	29	29	41
	Unemployment rate of those with a high school diploma or lower qualifications	16	9	29	19	22
	US: Unemployment rate including marginal workers	14	17	22	19	28
	US: Unemployment rate including part-time workers for economic reasons	13	13	21	28	32
	Labor participation rate	0	0	0	11	6
	Employment rate	3	5	11	14	16
	Liquidity	Initial unemployment insurance claims	0	2	15	39
Employment rate		25	31	0	14	14

# Goods consumption shows signs of peaking out, but upside risks remain

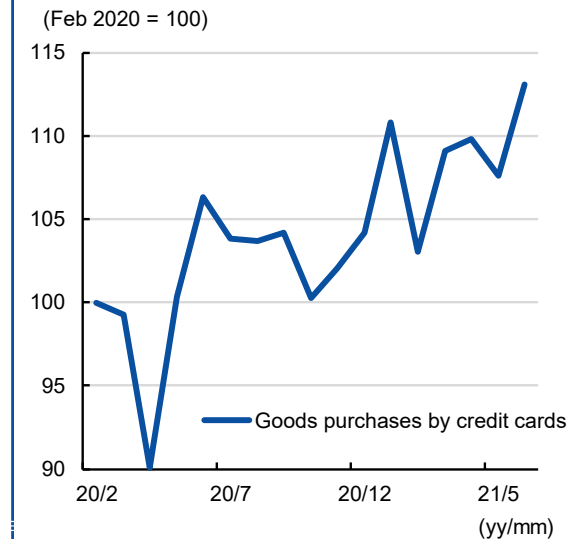
- May retail sales (-1.3% m-o-m) and core retail sales (-0.7% m-o-m) both fell. While the demand for goods seems to have peaked out, upside risks remain such as a rebound of high-frequency data in June.
  - Goods related to staying at home (furniture, appliances, etc.) decreased. On the other hand, eating out and clothing sales increased due to relaxation of restrictions and increased opportunities to go out.
    - ◆ Due to the upward revisions in March and April, core retail sales in the Apr-Jun quarter increased by 7.5% Pt (based on q-o-q p.a.).
  - Credit card spending (retailers) in the first week of June increased again. Although there is a high possibility of this being a temporary fluctuation, the upside risks in goods consumption remain due to such factors as major E-commerce sites bringing their summer sales forward.

## Retail sales



Source: Made by MHRT based upon US Department of Commerce

## Goods purchases by credit cards



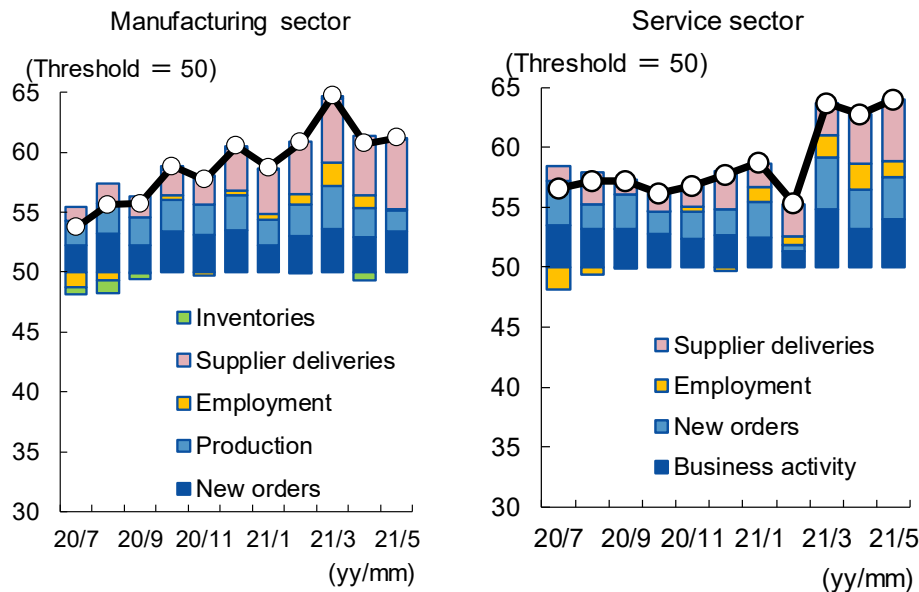
Note: Credit card spending in June this year is for the first week  
Source: Made by MHRT based upon US Department of Commerce



# Supply continues to be unable to keep up with favorable demand

- In May, the ISM index marked a high level of over 60 in both the manufacturing and service sectors. The new orders index has risen further, indicating favorable demand. On the other hand, the rise in the supplier deliveries index and the decline in the employment indicators suggests that supply constraints continue to be strong.
  - Concerns about supply from corporations are apparent, such as labor and material shortages and distribution disruptions. No pessimistic comments on demand were observed.
    - ◆ There is a situation where deficiencies of a wide range of materials have been pointed out (a growing sense of shortage of chemical products suggests that the effects of the February cold snap remain).
  - As a result, corporations could not handle all the orders, which led to a further rise in order backlog index, and the customer inventory index set a new record low.

## Breakdown of ISM index



Source: Made by MHRT based upon Institute for Supply Management

## Materials, etc., that manufacturers cited as being "deficient"

	2020												21				
	3	4	5	6	7	8	9	10	11	12	1	2	3	4	5		
Hygiene/Medical equipment	7	6	8	4	4	1	4	1	3	2	1	1	1	1			
Metal	Steel							1	2	3	4	5	5	5	7		
	Aluminum						1	1	1	1	2		1	1	2		
	Copper										1						
Electrical / Electronic	Semiconductors									1	1	1	1	1	1		
	Others		3					4	3	1	2	2	4	3	2		
Chemical products								2	1			5	9	5	9		
Others	Wood products							1					3	2	3		
	Plastics & Rubber products												1	2	2		
	Cardboard									1	1	2	2	1	1		

Note: The table represents a categorization of materials, etc., that were cited as "deficient" in press release materials. The numerical values of each category is the number of citations of said materials, etc., included in that category.

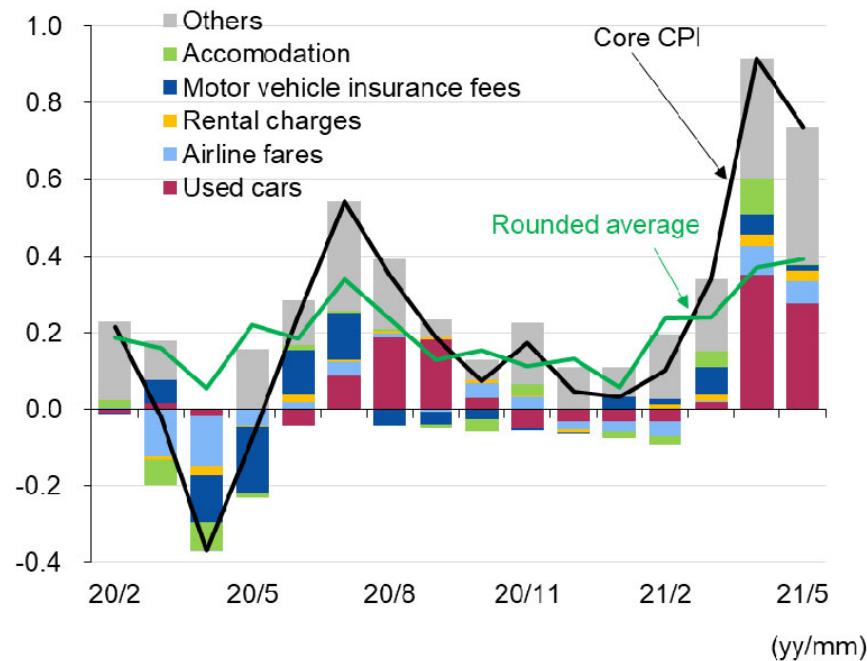
Source: Made by MHRT based upon Institute for Supply Management

# Inflation remains at a high level against the backdrop of tight supply and demand and normalization following the Covid-19 pandemic

- In May, core CPI rose +0.7% m-o-m (April +0.9% m-o-m), showing a high level of growth. Y-o-y, core CPI rapidly accelerated to +3.8% (April +3.0% y-o-y)
  - The impact from such sources as used car sales (+7.3% m-o-m) and airline fares (+7.0% m-o-m) was significant. The rounded average also greatly rose by +0.4% m-o-m (April +0.4% m-o-m), excluding items with large fluctuations, but movements were related to normalization.
- In May, the core PCE deflator is expected to increase by around +3.4% y-o-y (April +3.1% y-o-y).
  - Although the effects of the current normalization movements and tight supply and demand exceed expectations, the inflation rate is expected to slow down toward the end of the year as these effects ease.

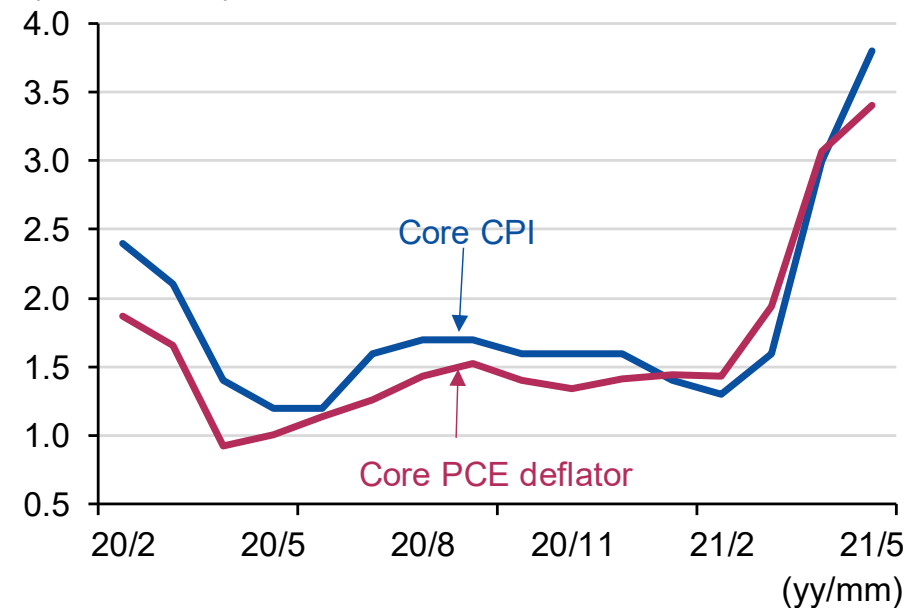
## Core CPI (m-o-m)

(M-o-m % ch)



## Core CPI and core PCE deflator (y-o-y)

(M-o-m % ch)



Source: Made by MHRT based upon US Department of Labor, Federal Reserve Bank of Cleveland

Note: May 2021 core PCE deflator is forecast value based on CPI, etc., of the same month  
Source: Made by MHRT based upon US Department of Labor, US Department of Commerce

# FOMC's projections in June show a drastic change to the dot plot chart for 2022 and 2023, and a rapid increase in participants supporting interest rate hikes

- In June, the FOMC publicly announced that it had held a discussion on the progress made towards its goals since the adoption of its asset purchase guidance in December 2020.
  - They also confirmed the policy to continue to evaluate of progress at future meetings.
- Economic projections were revised upward for 2021 and remained mostly unchanged for 2022 and 2023, reflecting the impact of the progress of vaccinations and additional economic stimulus.
- The dot plot chart for 2022 and 2023 changed drastically. In addition to the possible start of rate hikes in 2022, the outlook for 2023 covers a wide range.
  - FRB Chair Jerome Powell played down the 2023 dot plot chart, stating that “there's a lot of uncertainty [a few years ahead]” and “discussing lift-off (rate hikes) now would be highly premature.”
  - Attention will gather around the FOMC minutes (July 7) regarding the degree of progression on evaluations toward the start of tapering, and the presence or absence of discussions on rate hikes.

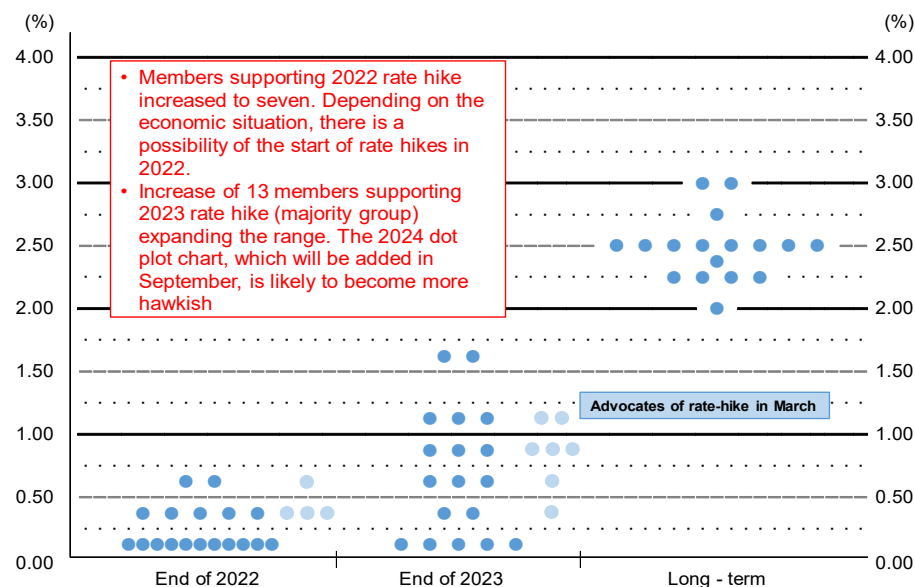
## Economic projections (note these are y-o-y comparisons and levels as of Oct-Dec quarter of each year)

Oct-Dec quarter of each year		2021	2022	2023	Long-term
Real GDP growth rate	Jun	7.0	3.3	2.4	1.8
	(Y-o-y % change) Mar	6.5	3.3	2.2	1.8
Unemployment rate	Jun	4.5	3.8	3.5	4.0
	(%) Mar	4.5	3.9	3.5	4.0
Inflation rate	Jun	3.4	2.1	2.2	2.0
	(Y-o-y % change) Mar	2.4	2.0	2.1	2.0
Core inflation rate	Jun	3.0	2.1	2.1	-
	(Y-o-y % change) Mar	2.2	2.0	2.1	-

Growth rates and inflation rates were both revised upward

Possibility of broad inflationary pressure being incorporated (Chair Powell)

## FOMC economic projections



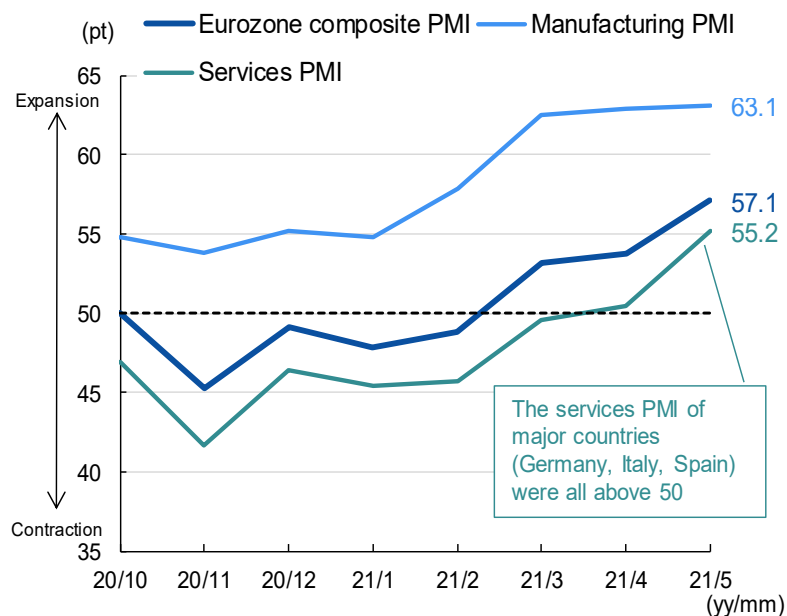
Source: Made by MHRT based upon FRB

Source: Made by MHRT based upon FRB

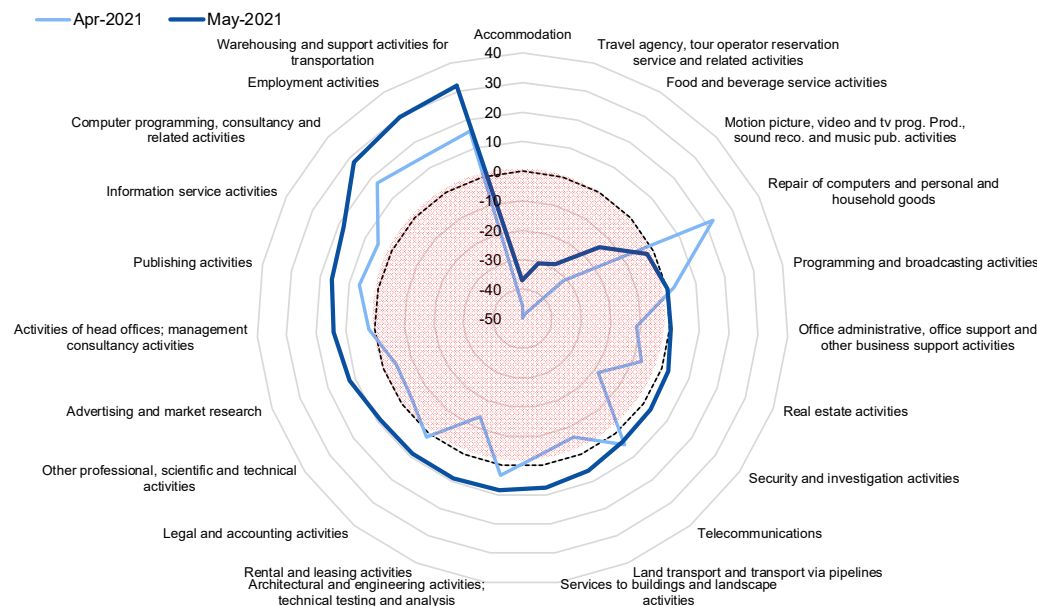
# The Eurozone economy: service sector boosts composite PMI in May. The recovery of the tourism industry will serve as a tailwind going forward

- The Eurozone composite PMI in May (final) was 57.1, up from April (53.8), reaching the highest level since the start of the Covid-19 pandemic. The service sector improved (50.5 → 55.2) against the backdrop of vaccine rollouts and the relaxation of mobility restrictions in major countries, thus serving to boost the overall PMI.
  - Although the manufacturing sector was dragged down by supply constraints and rising input costs, the manufacturing PMI remained at a high level of 63.1 due to robust demand.
- By industry, according to a survey by the European Commission, business sentiment is positive in each sector except for services requiring face-to-face interactions, such as accommodation and food and beverages.
  - Even though services requiring face-to-face interactions continues to be sluggish, the odds are high that the outlook will improve along with the relaxation of restrictions.

## Eurozone: PMI



## Eurozone: Service sector DI for current conditions by industry



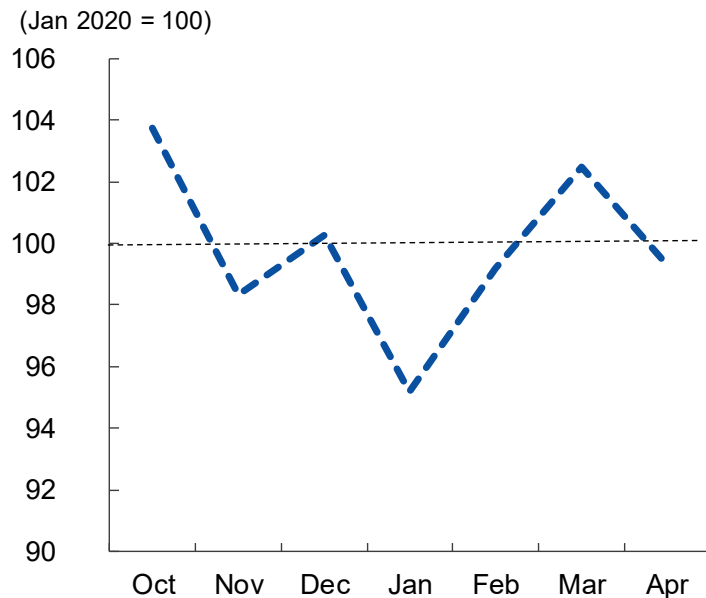
Note: The reading of 50 is the "expansion-contraction" threshold.  
Source: Made by MHRT based upon Refinitiv

Note: The reading of zero is the "expansion-contraction" threshold of the DI for current conditions  
Source: Made by MHRT based upon European Commission

# Retail sales are following an ebb-and-flow pattern at pre-Covid-19 levels. Full-fledged consumption recovery expected along with the relaxation of infection control measures.

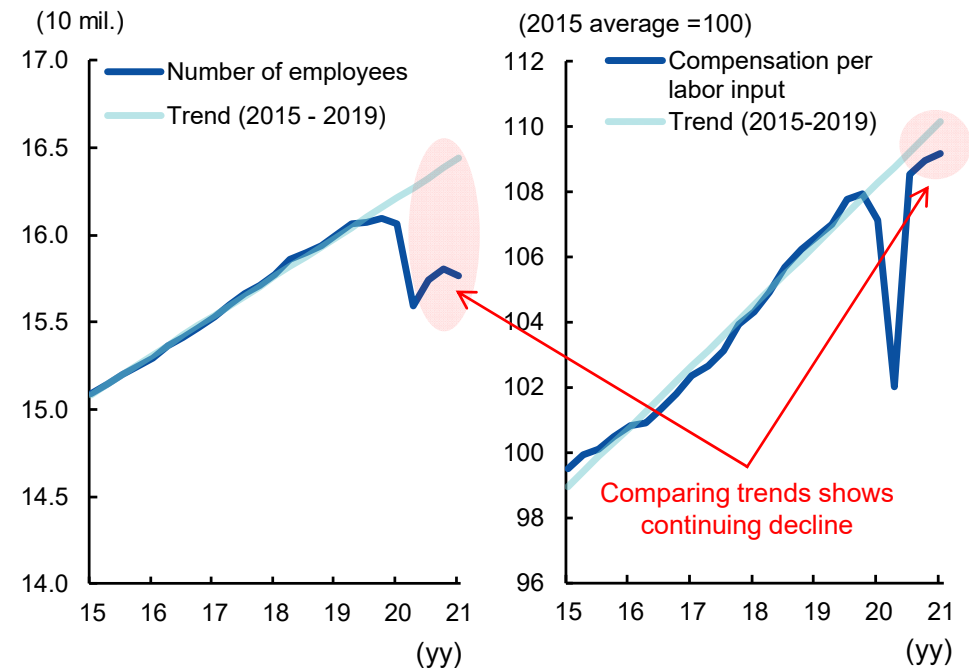
- Eurozone real retail sales in April stood at 99 (January 2020 = 100), down -3.1% m-o-m, reflecting the reinforcement of infection prevention measures in some major countries.
  - Given the progress of the relaxation of infection prevention measures/recovery of mobility along with vaccine rollouts, the odds are high that consumption will achieve a full-fledged recovery.
- The pace of recovery in the employment and income environment is gradual. Despite prospects of a moderate recovery due to the normalization of economic activities, a strong recovery surpassing the pre-Covid-19 trend is unlikely.
  - The number of employed persons and per capita compensation are continuing to fall below pre-Covid-19 trends.

## Eurozone: real retail sales (excl. motor vehicles)



Source: Made by MHRT based upon Eurostat

## Eurozone: employment and income environment

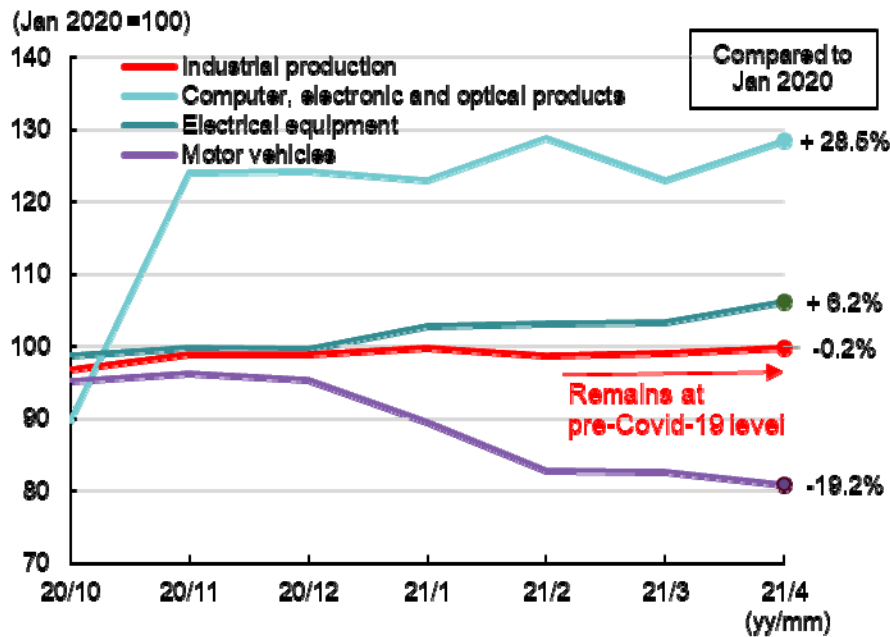


Note: Based on ESA  
Source: Made by MHRT based upon Eurostat and ECB

# Sluggish motor vehicle production due to supply constraints is serving as a drag on recovery in eurozone manufacturing industry

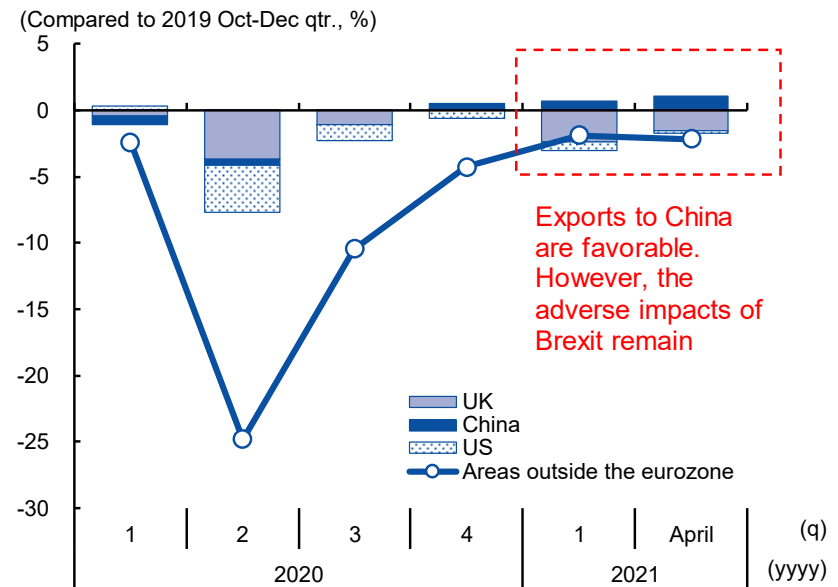
- While eurozone industrial production (April: 99.8 (Jan 2020 = 100)) rose for the second straight month, it still remains at pre-Covid-19 levels, against the background of sluggish motor vehicle production.
  - Supply constraints on motor vehicles continue, and a recovery is expected in the second half of 2021. Some major corporations announced production adjustments for June.
  - On the other hand, PCs, electronic and optical products and other items are driving production. It will be necessary to monitor the risks of adverse effects, such as semiconductor shortages, spreading beyond motor vehicle industries.
- Even though exports to areas outside the eurozone in April decreased (-2.3% m-o-m) due to a backlash from the previous month, they are levelling off when averaged out.
  - While exports to China are favorable, there are lingering impacts from Brexit on exports to the UK.

## Eurozone: industrial production



Source: Made by MHRT based upon Eurostat.

## Eurozone: nominal exports to areas outside the eurozone

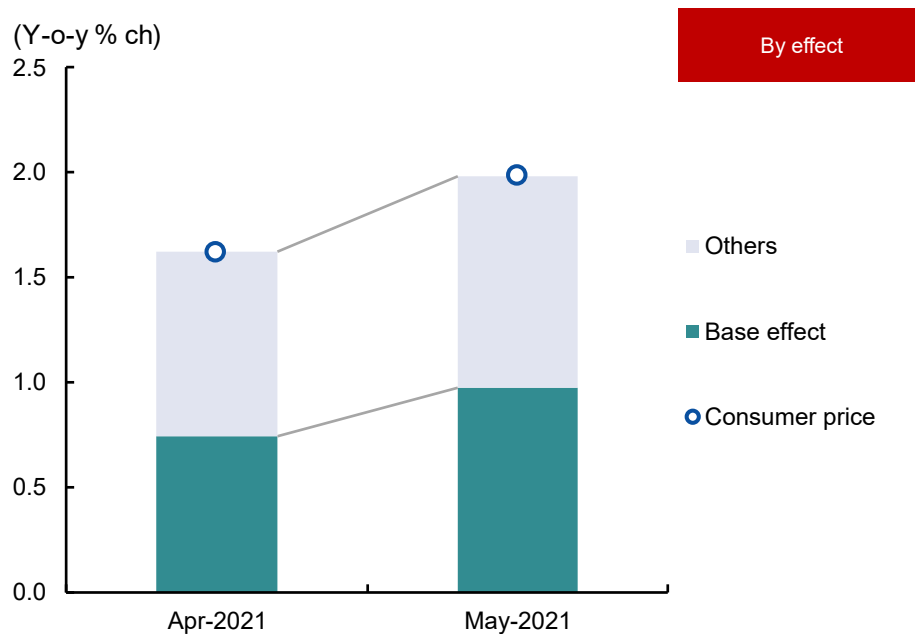


Source: Made by MHRT based upon Eurostat.

# Base effect boosts eurozone prices. Core prices continue remain around 1%

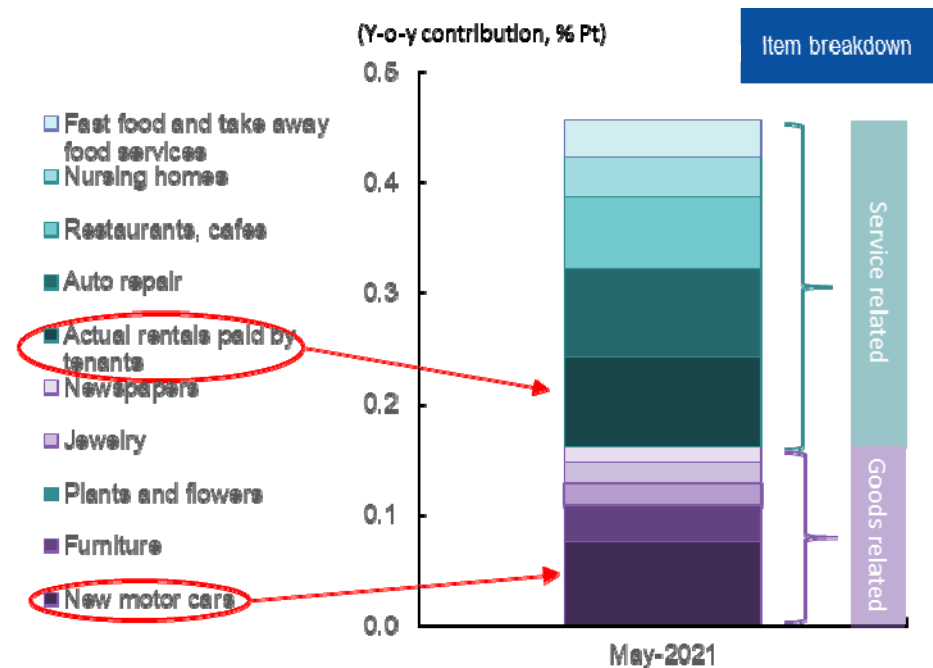
- In May, Eurozone consumer prices (+2.0% y-o-y (final)) rose +0.4% Pt from the previous month. Looking closer, the impact of 2020's base effect contributed about +0.3% Pt, mainly driven by rising energy prices.
  - Base effects during the second half of 2021, such as the rebound of the VAT tax cut, will be strengthened, while the CPI is expected to rise to the mid +2% range (the effect will fade in 2022).
- Core prices stood at +1.0 y-o-y, (revised up by +0.1% from flash estimate), remaining stable around +1% y-o-y. New cars, rentals paid by tenants, and others were contributing factors.
  - Looking at price levels, prices of goods are more or less on par with the trend. On the other hand, service prices turned out to be lower than expected, pushing down core prices. From 2022, service prices are likely to return to the trend due to the expansion of demand for service consumption accompanying the normalization of economic activities.

## Eurozone: breakdown of CPI factors



Note: The base effects are deviations from the 2012-19 average m-o-m change for each month.  
Source: Made by MHRT based upon Eurostat.

## Eurozone: degree of contribution by item affecting CPI



Source: Made by MHRT based upon Eurostat.



# ECB maintains its PEPP purchasing policy. The decision to slow down the purchase pace will be carried over to September

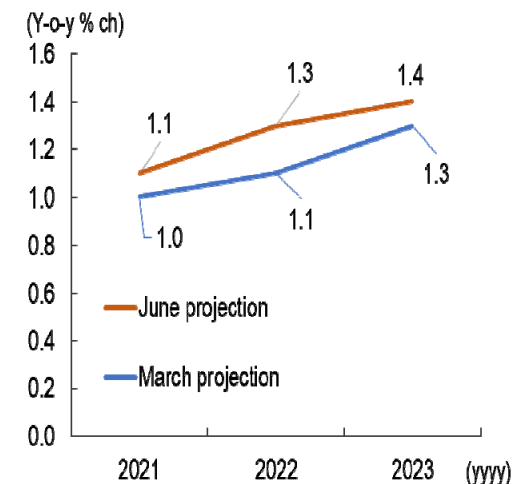
- At the Governing Council meeting on June 10, the ECB decided to maintain the purchase policy in the Pandemic Emergency Purchasing Program (PEPP) for the next quarter.
  - It was decided that the continued rise in market interest rates at this stage is premature (a downward risk) for the eurozone, which is currently undergoing economic recovery.
- Although the GDP and inflation outlook from ECB staff were revised upward, core prices are expected to remain below 2% until 2023.
  - 2021 GDP (+4.6% y-o-y) has been revised upward by +0.6% Pt. The period of recovery to pre-pandemic levels has been brought forward by one quarter to the 2022 Jan-Mar quarter.
- At the September Governing Council, when the next outlook revision will take place, it is likely that it will be possible to confirm the economic recovery trend with hard data, and that the results of the strategic review will also be released. It is expected that the decision to slow down the PEPP purchase pace will be made in September.

## Key points of the ECB Governing Council (accounts of June 10)

ECB staff macroeconomic projections	Growth rates for 2021, 2022 and 2023 are +4.6%, +4.7% and +2.1% respectively. (March projections: +4.0%, +4.1% and 2.1% respectively.) Inflation rates for 2021, 2022 and 2023 are +1.9%, +1.5%, +1.4% respectively. (March projections: +1.5%, +1.2%, 1.4% respectively.)
Economic situation	<ul style="list-style-type: none"> <li>• In the service sector, surveys suggest a strong bounce-back, and the manufacturing sector also remains favorable. However, supply-side bottlenecks will weigh on activities in the near term.</li> <li>• <b>While uncertainties remain</b>, such as the trend of infections and the response from the economy after lockdown restrictions have been lifted (e.g. reduction in household savings), <b>risks surrounding the outlook are broadly balanced (improvement compared to previous outlook)</b>.</li> </ul>
Outlook for prices	<ul style="list-style-type: none"> <li>• Prices have increased in recent months due to temporary factors and higher energy price inflation. Price inflation is expected to rise further in the second half of the year, before declining as temporary factors fade out.</li> <li>• During the projection horizon, core prices are expected to increase gradually, but will be weighed down by labor market slack.</li> </ul>
Financing conditions	<ul style="list-style-type: none"> <li>• While already favorable, market interest rates have increased further. While part of this is reflecting expected economic recovery, <b>a sustained rise in market interest rates could translate into a tightening of wider financial conditions. Such a tightening would be premature and could pose a risk to the ongoing economic recovery and the outlook for inflation.</b></li> </ul>
Pandemic Emergency Purchase Program (PEPP)	<ul style="list-style-type: none"> <li>• The Governing Council expects purchases over the coming quarter to continue to be conducted at a significantly higher pace than during the first months of the year (unchanged from the previous outlook). <b>There may be seasonal impacts</b> on the purchase pace <b>(considering that there's typically less liquidity in the summer)</b>.</li> <li>• <b>Discussions on reducing PEPP did not take place as it is premature.</b></li> </ul>

Source: Made by MHRT based upon ECB.

## Eurozone core prices (ECB staff projections)



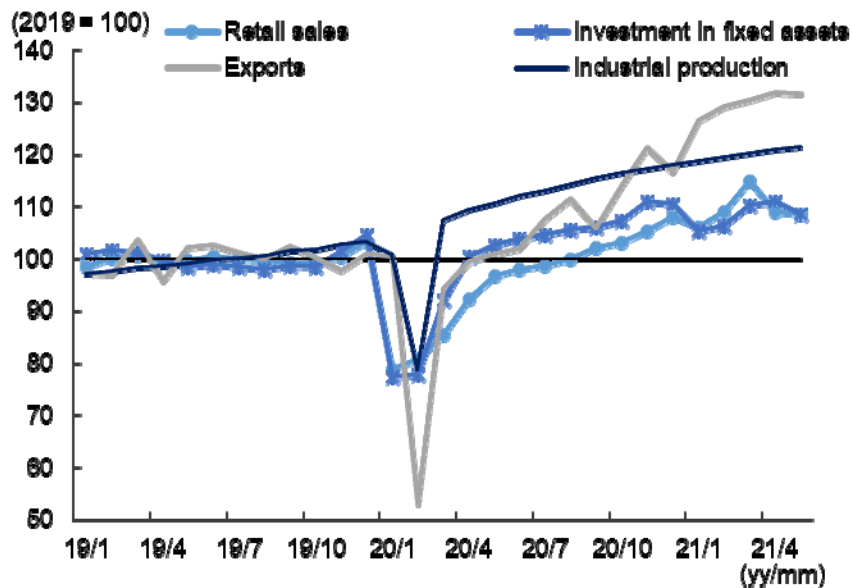
Source: Made by MHRT based upon ECB.



## Chinese economy: May's main indicators are trending flat due to a stronger pause

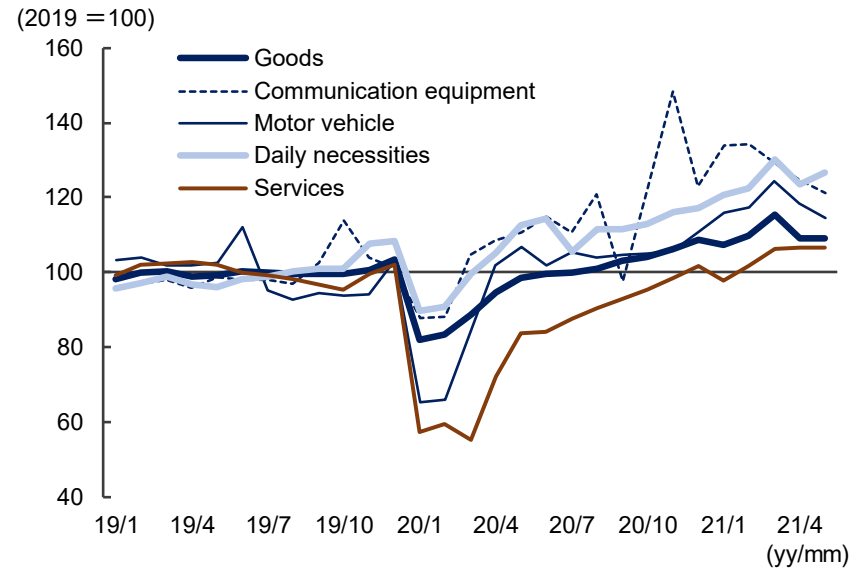
- A look at the key indicators in May reveal that the pace of recovery has slowed, except for production, and is levelling off.
  - Production is continuing to recover, particularly for electronics/machinery and high-tech related products (electronics/pharmaceuticals, etc.), which are mostly produced for export.
  - Despite the strength of manufacturing (such as high-tech manufacturing) and infrastructure investment, real estate investment is falling due to measures implemented to control the rise of housing prices.
  - As for retail sales, while daily necessities and other areas remain firm, communication equipment and motor vehicles are declining, reflecting the drop in special demand due to Covid-19.
- The Chinese economy is expected to continue to gradually recover, particularly in investment in manufacturing and consumption (which reflects the improvement in the employment environment). However, there are lingering downside risks regarding investment due to negative pressures on earnings reflecting the rise of costs and appreciation of the yuan.

### Key monthly indicators



Note: Industrial production are estimates based on seasonally adjusted m-o-m change announced by the National Bureau of Statistics of China. Retail sales, investment in fixed assets, and exports are adjusted for seasonal factors by MHRT  
 Source: Made by MHRT based upon the National Bureau of Statistics of China and CEIC data.

### Goods/service consumption

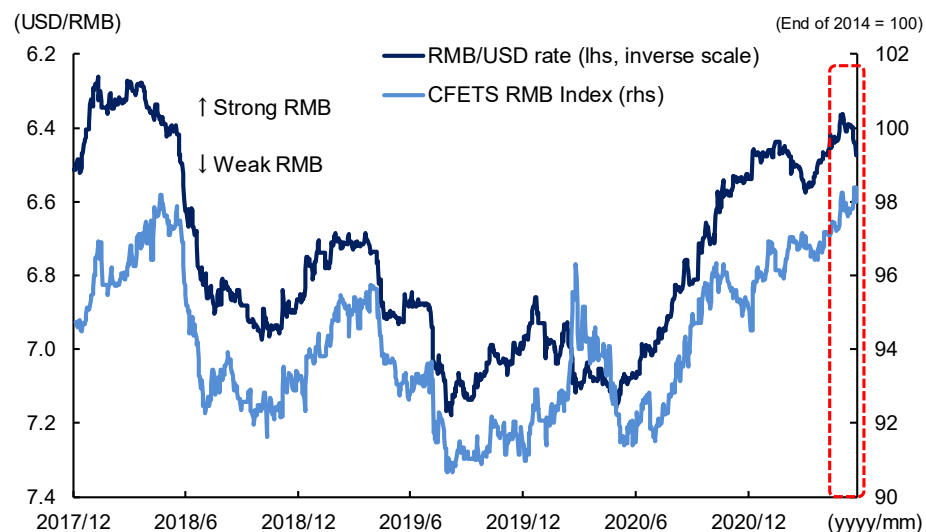


Note: Adjusted for seasonal factors by MHRT  
 Source: Made by MHRT based upon the National Bureau of Statistics of China and CEIC data.

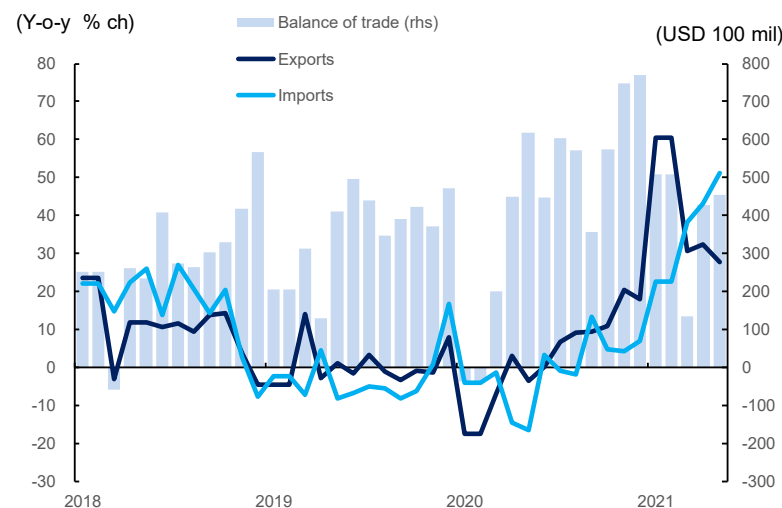
# The RMB is rising due to growing import inflation concerns. The PBOC clarifies its stance to control RMB appreciation

- RMB-US dollar rate recorded its strongest yuan level in about three years against the backdrop of soaring international commodity prices.
  - In addition to the general depreciation of the dollar, the yuan strengthened due to import inflation concerns. On May 28, the yuan recorded 1 USD = 6.36 RMB level for the first time in approximately three years.
  - In response to the rapid appreciation of the yuan, the People's Bank of China (PBOC) announced it will raise the foreign currency reserve requirement ratio, indicating its stance of curbing excessive RMB appreciation.
- Even though the appreciation of the yuan since early April has paused due to the PBOC's measures, there is limited room for further depreciation.
  - Given the peak-out of exports in contrast to the ongoing rise of imports due to soaring commodity prices, we expect yuan strengthening pressures to gradually ease.
  - However, a certain degree of yuan-strengthening pressure will linger due to the US-China interest rate differential. Movements towards yuan depreciation are expected to remain limited.

## RMB-USD rate



## Trade statistics (USD base)



Note: The CFETS RMB Index are estimates by MHRT. Daily data. Most recent data is from June 21, 2021

Source: Made by MHRT based upon CFETS, CEIC data.

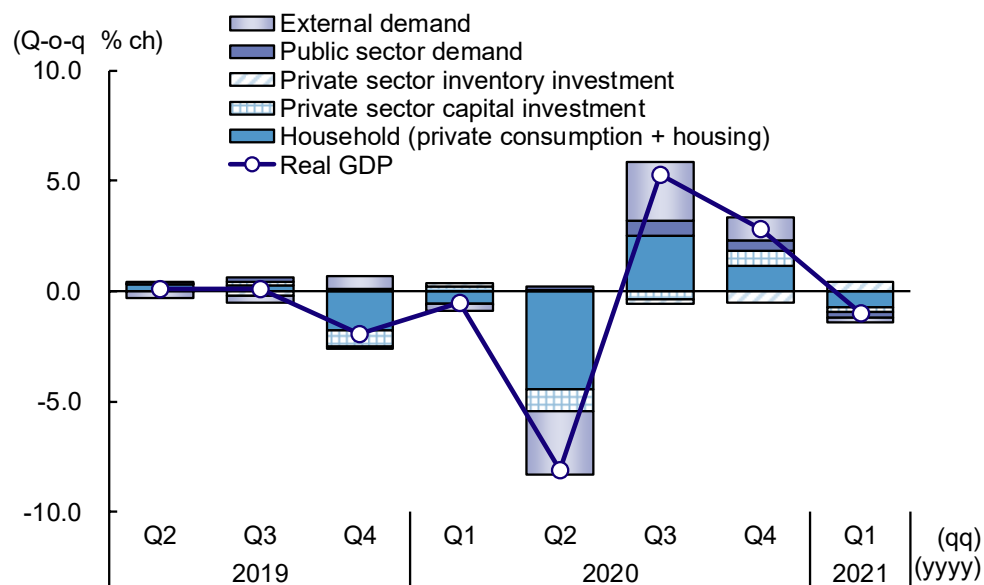
Note: January-February of each year is the cumulative y-o-y comparison of January-February of the years indicated.

Source: Made by MHRT based upon the General Administration of Customs of the National Bureau of Statistics of China and CEIC data.

# The Japanese economy: the 2nd QE for the Jan-Mar quarter was revised upward. Negative growth expected for Apr-Jun quarter

- The *Second Preliminary Quarterly Estimates of GDP* ("2nd QE") of the Jan-Mar quarter was revised upward to -1.0% q-o-q (-3.9% p.a.) from the 1st QE (-5.1% p.a.).
  - Although there were upswings mainly in inventory investment and public sector demand, the content of negative growth remains unchanged, mainly due to a significant decrease in personal consumption stemming from the declaration of a state of emergency. The results reiterate the difficulty of achieving both the recovery of economic activities and prevention of Covid-19 infections.
  - For the Apr-Jun quarter, real GDP is forecast to stand at -0.7% q-o-q (-2.7% p.a.), recording negative growth for the second quarter in a row as a result of: (1) a decrease in personal consumption due to the third declaration of a state of emergency, and (2) a reduction in motor vehicle production due to semiconductor shortages.
  - For the Jul-Sep quarter, the pace of recovery is expected to remain slow as a result of continued Covid-19 preventive measures and measures unique to prefectures (requests for shortened working hours, etc.).

## 2nd QE for 2021 Jan-Mar quarter



	2020			2021	
	Apr-Jun	Jul-Sep	Oct-Dec	Jan-Mar	Apr-Jun
Real GDP	-8.1	5.3	2.8	-1.0	-0.7
(Q-o-q % change)	-28.6	22.9	11.7	-3.9	-2.7
(Y-o-y % change)	-10.1	-5.6	-1.1	-1.6	6.4
Domestic demand	-5.2	2.6	1.8	-0.8	-0.7
(Q-o-q % change)	(-5.2)	(2.6)	(1.8)	(-0.8)	(-0.7)
Private sector demand	-7.2	2.6	1.8	-0.7	-1.1
(Q-o-q % change)	(-5.4)	(2.0)	(1.3)	(-0.5)	(-0.8)
Personal consumption	-8.3	5.1	2.2	-1.5	-1.6
Housing investment	0.6	-5.7	0.0	1.2	-0.5
Capital investment	-6.1	-2.1	4.3	-1.2	0.5
Inventory investment	(0.1)	(-0.2)	(-0.5)	(0.4)	(0.0)
Public sector demand	0.5	2.5	1.7	-1.0	0.3
(Q-o-q % change)	(0.1)	(0.7)	(0.5)	(-0.3)	(0.1)
Government consumption	0.2	2.9	1.8	-1.1	0.2
Public investment	2.2	0.8	1.3	-0.5	0.7
External demand	(-2.8)	(2.6)	(1.0)	(-0.2)	(0.0)
Exports	-17.5	7.3	11.7	2.2	-0.4
Imports	-0.7	-8.2	4.8	3.9	-0.7
Nominal GDP	-7.8	5.6	2.4	-1.3	-2.2
GDP deflator (y-o-y change)	1.4	1.2	0.2	-0.1	-2.0

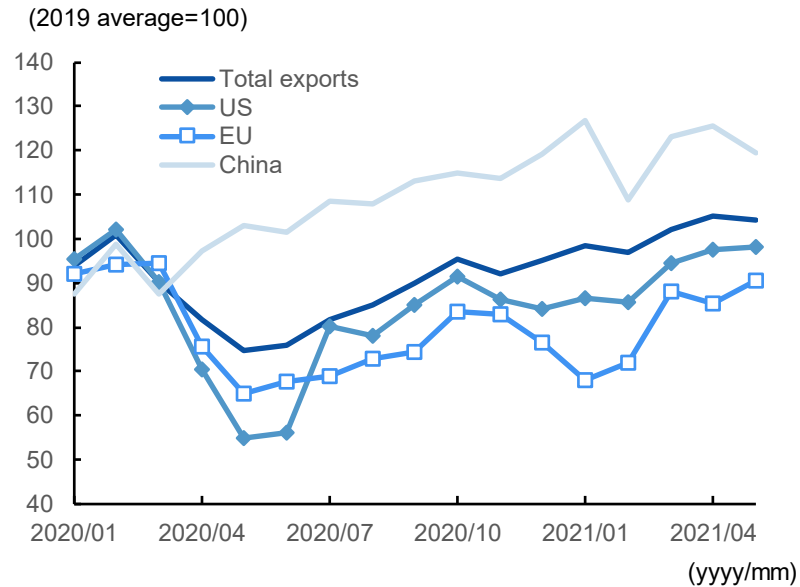
Note: Figures in the right-hand chart indicate changes to the previous quarter (in real terms) unless otherwise noted. The figures in parentheses represent the contribution to growth. Figures for the Apr-Jun quarter 2021 are forecasts

Source: Made by MHRT based upon Cabinet Office, *Quarterly Estimate of GDP*.

# Exports declined in May, while a gradual increase is expected ahead

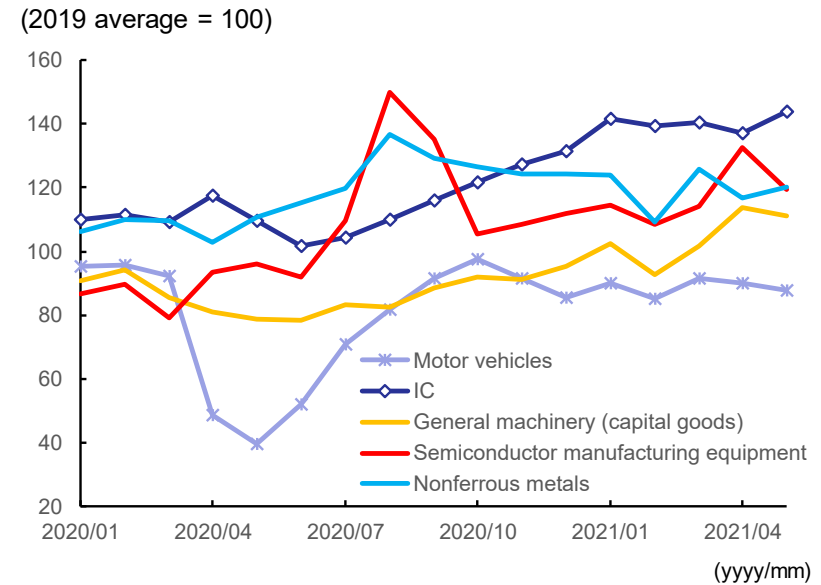
- Even though the export volume index stood at -0.7% m-o-m in May, the Apr-Jun quarter is likely to be positive (higher than expectations).
  - By major destinations, exports to the US and EU increased, while exports to China took a downturn, serving to push down total exports.
  - By item, ICs, nonferrous metals, iron & steel, etc., increased, while capital goods such as semiconductor manufacturing equipment decreased, and motor vehicles took a downturn due to the shortage of semiconductors (the impact of the semiconductor shortage on the Apr-Jun quarter is expected to be smaller than MHRT projections).
- Looking forward, despite a temporary decline of motor vehicle exports due to semiconductor shortages, exports are expected to remain on a gradual upward trend, reflecting support provided by information-related goods and increase in capital goods.

## Export trends by major destination



Note: Adjusted for seasonal factors by MHRT  
 Source: Made by MHRT based upon Ministry of Finance, *Trade Statistics*.

## Export trends by major item

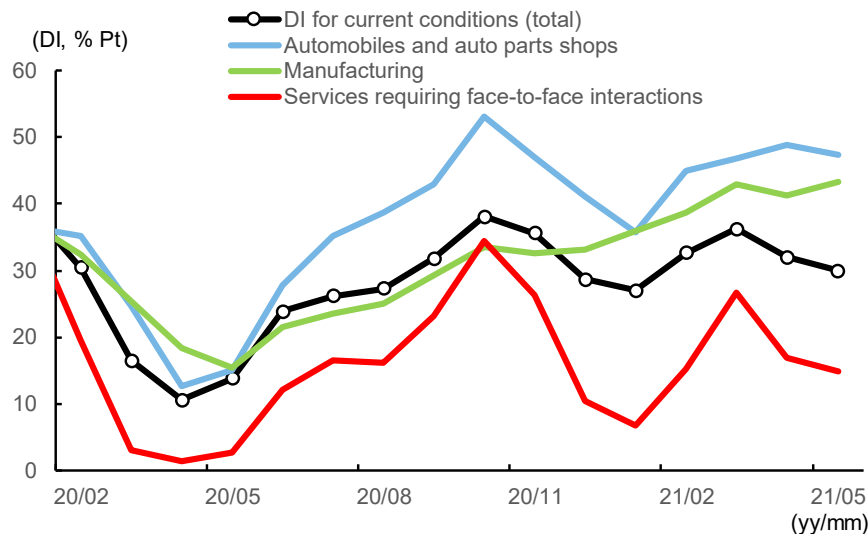


Note: General machinery is on a nominal value basis. Adjusted for seasonal factors by MHRT.  
 Source: Made by MHRT based upon Ministry of Finance, *Trade Statistics*.

# Business sentiment deteriorated in May. Vaccine expectations should improve sentiment going forward

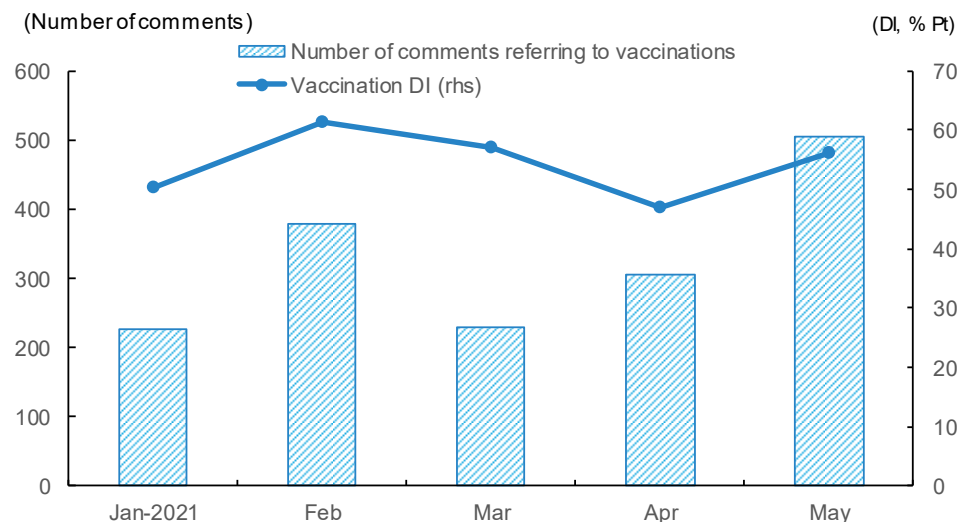
- Due to the impact of the declaration of a state of emergency, the DI for current conditions (direction) in May deteriorated slightly at -1.0 Pt m-o-m (April: -9.9 Pt m-o-m).
  - Even though the DI for current conditions deteriorated slightly (April: 32.0 → May: 30.0), it surpasses the level at the time of the previous declaration (January: 27.0)
  - However, references to semiconductor shortages increased mainly in the motor vehicle-related industries (number of comments, April: 11 → May: 21)
- Expectations toward the normalization of economic activities due to the acceleration of the pace of vaccinations served to lift judgments on future economic conditions.
  - The DI for future economic conditions improved by +5.9 Pt m-o-m. Comments referring to vaccine rollouts increased significantly (April: 306 → May: 506). The vaccine DI, which aggregates business sentiment, has also improved, and expectations for economic recovery due to vaccine rollouts have increased.

## Economy Watchers Survey: DI for current conditions (by sector)



Note: 1. Adjusted for seasonal factors by MHRT  
 2. Services requiring face-to-face interactions is the average for sectors related to food and beverage and related to tourism and transportation  
 Source: Made by MHRT based upon Cabinet Office, *Economy Watchers Survey*.

## Future economic conditions: number of comments referring to vaccine rollout and DI

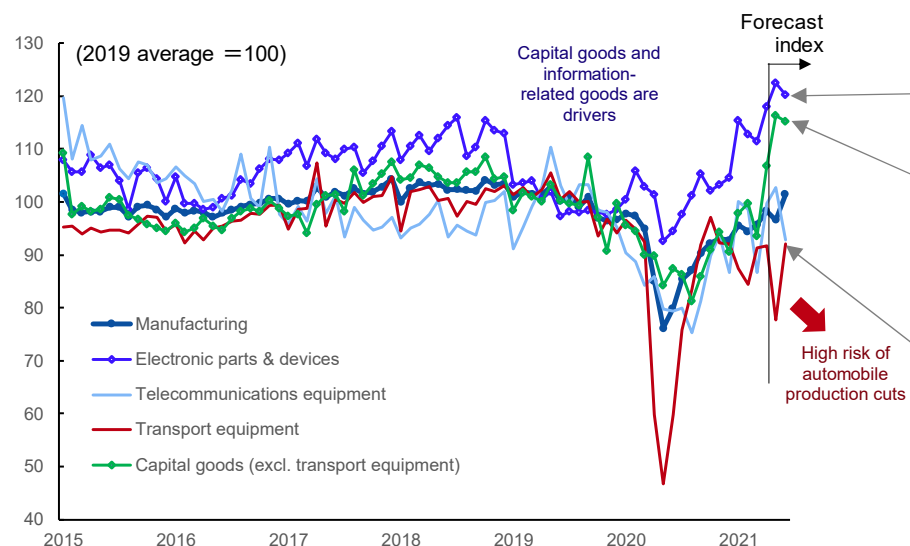


Note: 1. The vaccine DI is the aggregated value of business sentiment of comments including "vaccine"  
 2. The total number of comments is over 1400 per month  
 Source: Made by MHRT based upon Cabinet Office, *Economy Watchers Survey*.

# In April, production was driven by capital goods and information-related goods. Looking forward, motor vehicle production cuts will serve as a drag

- In April, industrial production improved by +2.5% m-o-m (March: +1.7% m-o-m), being positive for the second consecutive month.
  - Capital goods and information-related goods served to drive production against the backdrop of strong capital investment demand in the US and China, and robust IT demand in Japan and overseas.
- Looking forward, even though capital goods and information-related goods are expected to remain on a recovery trend, motor vehicle production cuts due to semiconductor shortages will serve as a drag on overall production.
  - If actual production is in line with production plans (May: -1.7% m-o-m, June: +5.0% m-o-m), Apr-Jun quarter industrial production would remain positive at +3.7% m-o-m. However, given prospects that motor vehicle production will fall short of production plans due to the impact of semiconductor shortages, Apr-Jun quarter industrial production is forecast to turn out around the same level as the previous quarter.

## Production results/forecast index by major sector/goods



### ○Electronic parts & devices

Increased production of MOS-type semiconductor integrated circuits (memory), fixed capacitors, electronic circuit boards, etc., against the backdrop of firm online demand in Japan and overseas

### ○Capital goods (excl. transportation equipment)

Against the backdrop of rising global demand for semiconductors, semiconductor manufacturing equipment has remained at a higher production level than before Covid-19. Increased production of industrial robots, shovel type excavators, etc., due to increased investment in manpower saving equipment in Japan and overseas and housing investment in the US

### ○Transport equipment manufacturing industry

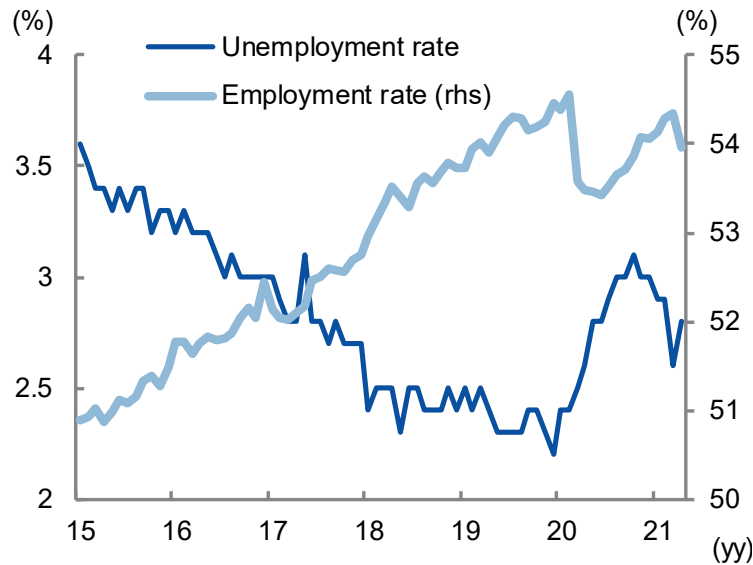
It is highly likely that the June forecast index (+18.5% m-o-m) does not reflect the production cut plans announced by automobile makers in mid-May. Thus there is a risk that automobile production will decline

Source: Made by MHRT based upon Ministry of Economy, Trade and Industry, *Indices of Industrial Production*

# Unemployment rose to 2.8% from the previous month. The number of employed persons is declining, mainly in the service sector

- The unemployment rate in April rose to 2.8% from the previous month (2.6%), mainly due to a decline in the number of employed persons (employees).
  - The total number of unemployed persons increased (+140 thousand m-o-m) from the previous month. Both involuntary and voluntary turnovers increased.
  - The number of persons employed decreased (-260 thousand m-o-m) from the previous month. Looking closer, the decrease was mainly seen in the wholesale/retail, accommodation/eating and drinking services, living-related services/entertainment sectors, and the impact of the third declaration of a state of emergency appears to have emerged in some industries.
  - The employment rate, which indicates the percentage of the number of employees in the total population aged 15 and over, decreased (-0.4% Pt m-o-m), recording the steepest fall since April 2020.
  - Looking forward, the unemployment rate is expected to rise further due to anticipated cautious recruiting attitudes and employment reduction due to the full-scale impact of the declaration of a state of emergency.

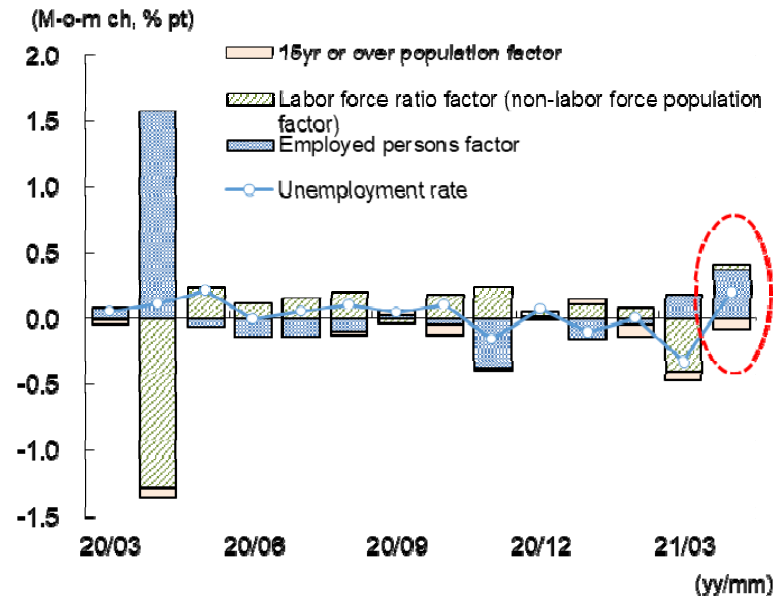
## Trends in unemployment and employment rates



Note: Seasonally adjusted figures. The employment rate = number of employed persons divided by the total population aged 15 and over.

Source: Made by MHRT based upon the Ministry of Internal Affairs and Communications, *Labour Force Survey*.

## Unemployment rate factors



Note: Increase in the number of employed persons, increase in the non-labor force population (decrease in the labor force participation rate), and decrease in the population aged 15 and over are factors that lower the unemployment rate.

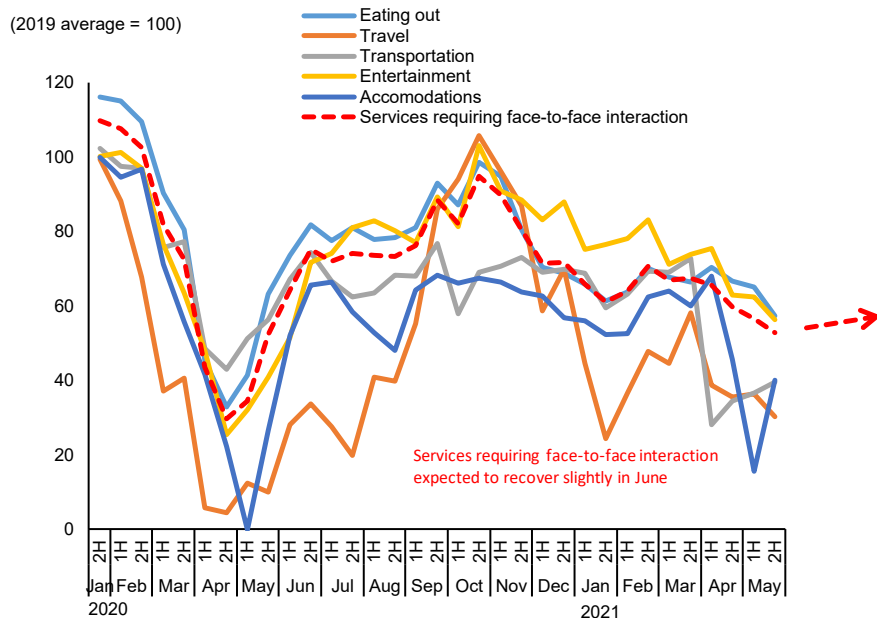
Source: Made by MHRT based upon the Ministry of Internal Affairs and Communications, *Labour Force Survey*.



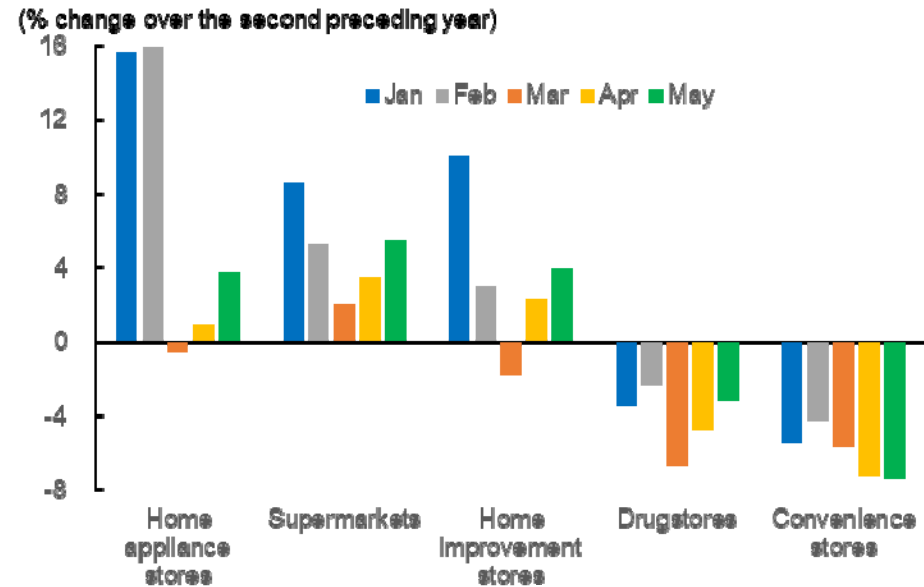
# Service consumption decreased due to the declaration of a state of emergency. Goods consumption is weak for motor vehicles and department stores

- Consumption of services with face-to-face interaction in the second half of May decreased mainly in eating out, travel, and entertainment services, due to the impact of the third declaration of a state of emergency.
  - Levels are below those at the time of the second declaration. Based on mobility trends, a slight recovery is expected in June.
- Goods consumption is expected to weaken for the Apr-Jun quarter, mainly in motor vehicles and department stores.
  - Background factors include a decrease in retail at department stores, etc., due to requests for business closures and people refraining from going out, and a decrease in motor vehicle sales due to semiconductor shortages.
  - However, appliances/furniture/food sales are maintaining a strength surpassing pre-Covid-19 levels (according to POS data). The variation by business/item requires attention.

## Service consumption with face-to-face interactions in the second half of May 2021



## Trends in retail sales index (POS data)



Note: Reference data series. Adjusted for seasonal factors by MHRT  
 Source: Made by MHRT based upon JCB and Nowcast, *JCB Consumption NOW*.

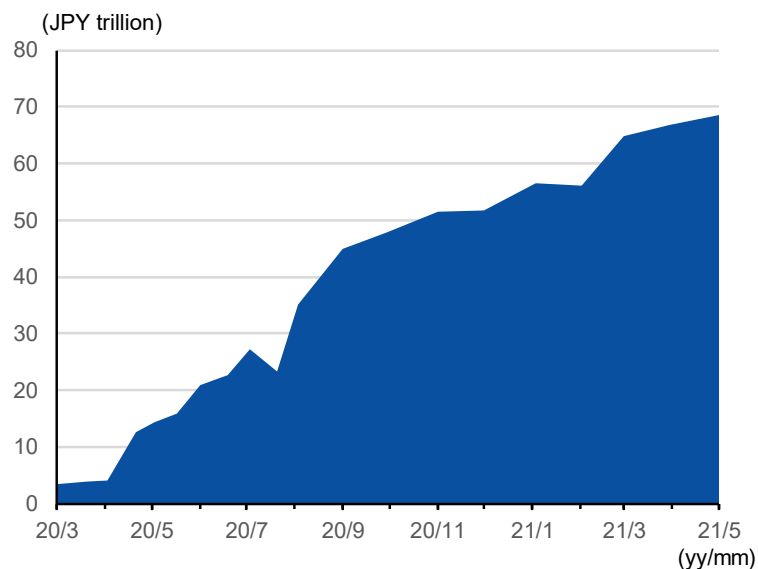
Source: Made by MHRT based upon Ministry of Economy, Trade and Industry, *METI POS retail sale index*.



## BOJ expected to continue its current monetary easing framework over the long term

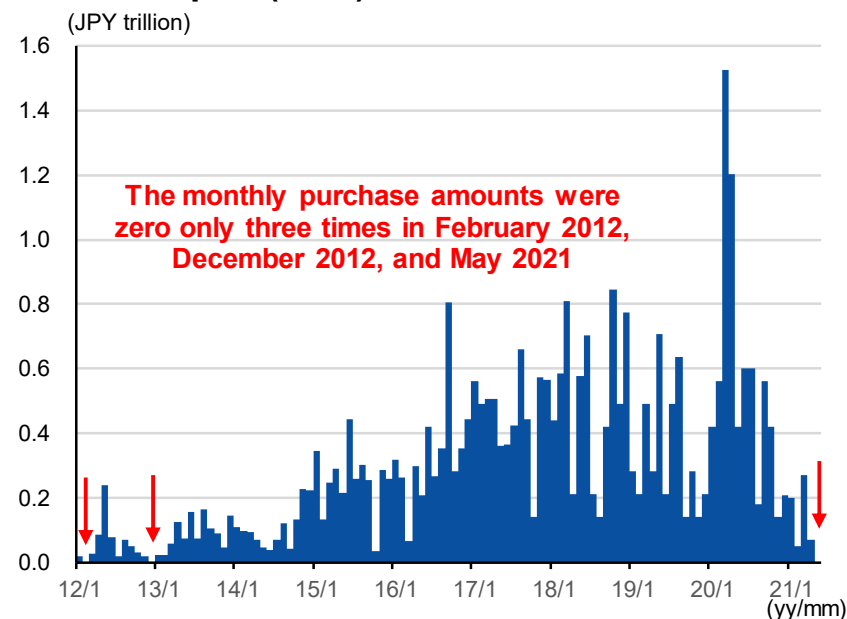
- At the June Monetary Policy Meeting (June 17 and 18), the Bank of Japan (BOJ) decided to maintain its current monetary policy stance.
  - The duration of the *Special Program to Support Financing in Response to the Novel Coronavirus* (COVID-19) will be extended by six months until the end of March 2022. Also, BOJ decided to introduce a new fund-provisioning measure to provide funds to financial institutions for investment or loans that they make to address climate change issues (BOJ will announce the preliminary outline at the July MPM, and launch the new measure likely within 2021).
- Based on the results of the "assessment" (March 2021) to implement more effective and sustainable monetary easing, BOJ is expected to continue its current monetary easing framework over the long term.
  - BOJ did not conduct ETF purchases in May. It was the first time in about eight and a half years, since December 2012, that there was no monthly purchase.

### Balance of special operations to financially support Covid-19 response



Note: Expected loan balance as of the date of loan  
Source: Made by MHRT based upon Bank of Japan.

### Monthly ETF purchase amounts by the Bank of Japan (BOJ)

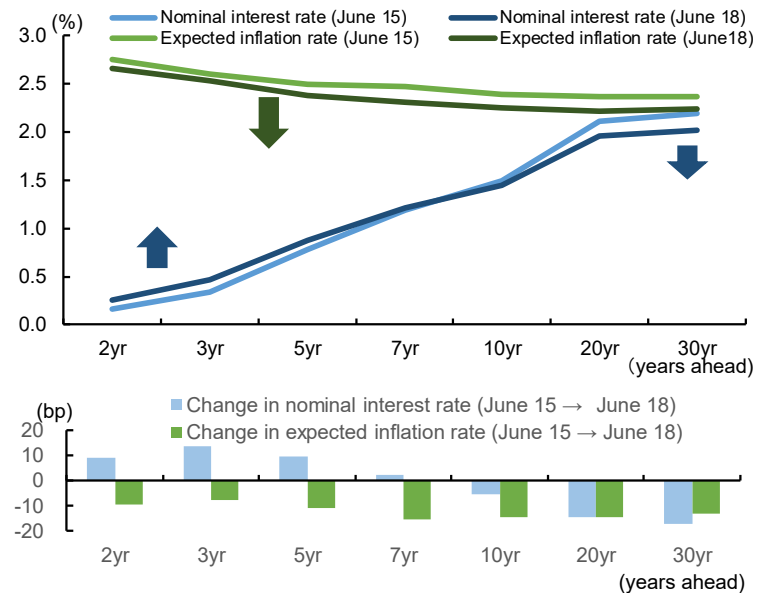


Source: Made by MHRT based upon Bank of Japan.

# US bond market: the 10yr UST yield is expected to move around 1.2% to 1.6%

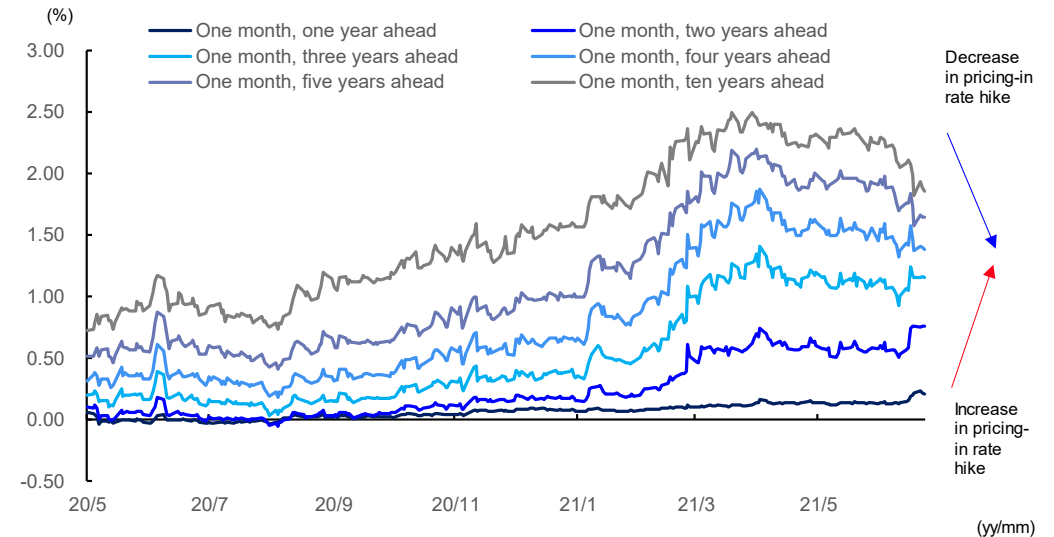
- As the number of participants in the FOMC (June 15 and 16) expecting a rate hike by the end of 2023 increased, the 2yr, 3yr and 5yr UST yields increased by around 10bp. On the other hand, the 10yr UST yield temporarily dropped to the 1.3% level, and ultra-long-term yields also fell sharply.
  - The expected inflation rate fell by more than 10bp after the FOMC, especially for 5yr-or-longer durations. Looking at the OIS forward rate, pricing-in of interest rate hike in the next one to three years rose, but those of five years or longer fell reflecting the ebb of concerns regarding medium- to long-term inflation.
- 10yr UST yield is expected to move around 1.2 to 1.6%, as the outlook for normalization of monetary policy tends to fluctuate and become a highly volatile development. The rise of medium-term yields is expected to pause, as speculation pricing in interest rate hikes exceeding the FOMC's policy rate projections recede.

## Nominal interest rate and expected inflation rates before and after the FOMC



Note: The expected inflation rates are break-even inflation rates  
Source: Made by MHRT based upon Bloomberg.

## Discounting of rate hikes by OIS forward rates

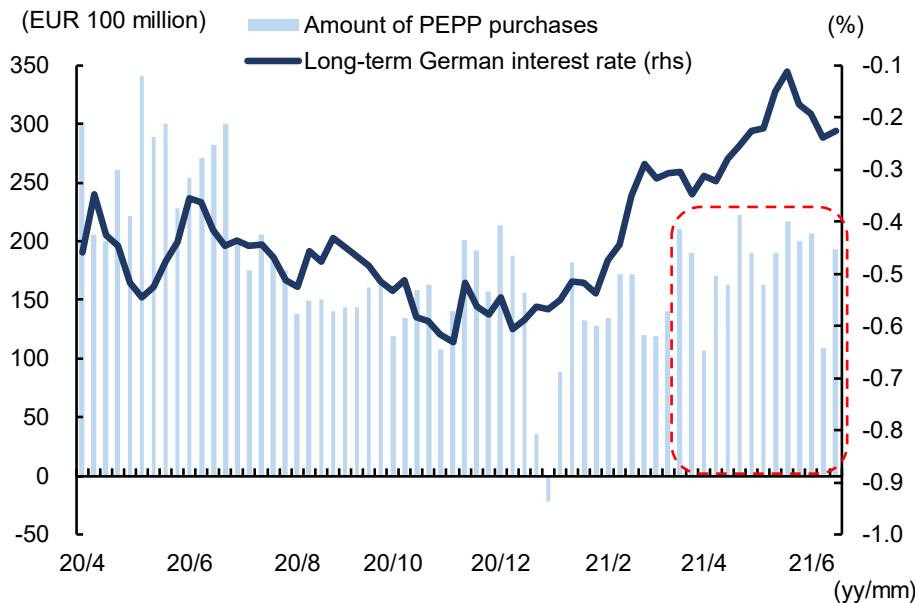


Note: The graph shows rates obtained by subtracting the federal funds rates from the one-month ahead OIS forward rates for a particular number of years ahead.  
Source: Made by MHRT based upon Bloomberg.

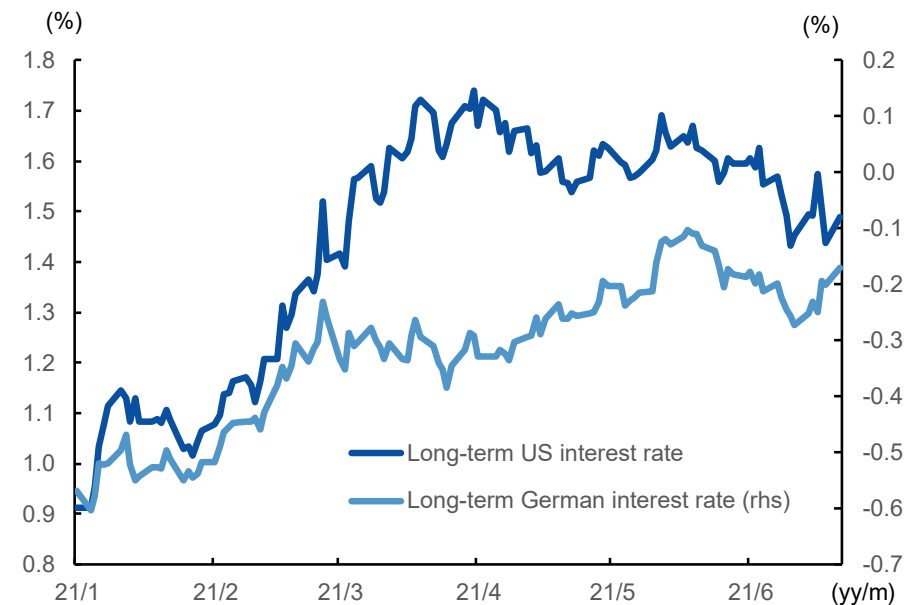
# Eurozone bond market: German 10yr government bond yield expected to move around -0.4 to -0.1%

- The German 10-year government bond yield temporarily fell to the upper -0.2% level, due to the ECB Governing Council (June 10) maintaining the PEPP purchase pace that had accelerated in March. However, it surpassed -0.2% due to a temporary decrease in the amount of PEPP purchases and the recognition of the US normalization of monetary policy.
- Looking forward, a further rise of the German 10yr government bond yield is expected to be limited, and move around -0.4 to -0.1%.
  - In contrast to the hawkish stance indicated by the FRB, ECB President Christine Lagarde stated that discussions on exiting the PEPP would be “just too early and premature” (June 14). The ECB will maintain its easing stance. German 10yr government bonds are expected to flatten out.

## Trend of PEPP purchase amount and Long-term German interest rate



## Trend of long-term US and German interest rates



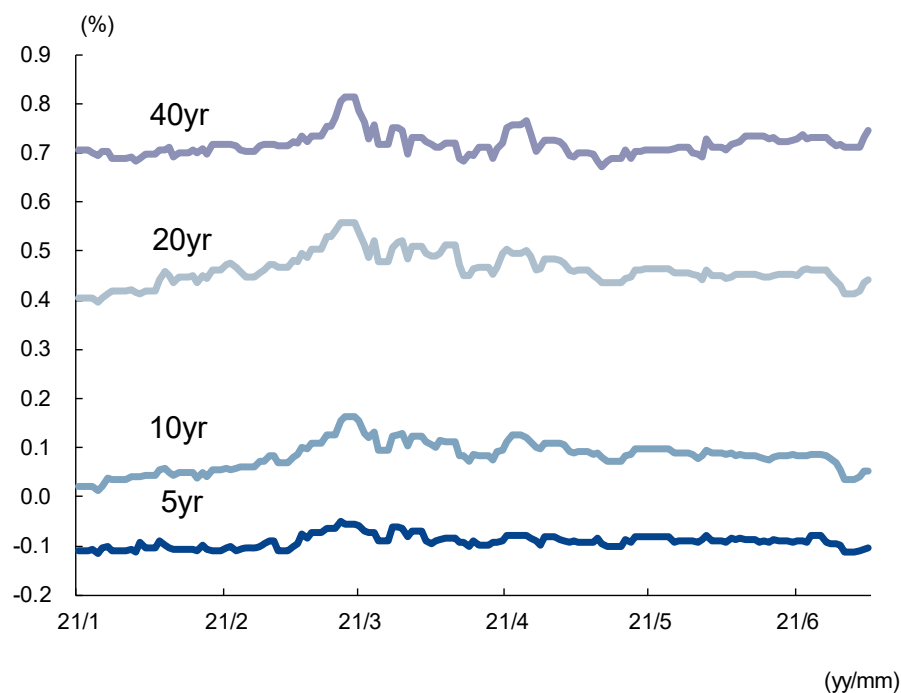
Note: The “Amount of PEPP purchases” refers to the weekly net purchase amount, less the redemption amount up to June 18.  
 The German 10yr government bond yield refers to the weekly average (up to June 18).  
 Source: Made by MHRT based upon Bloomberg

Source: Made by MHRT based upon Bloomberg

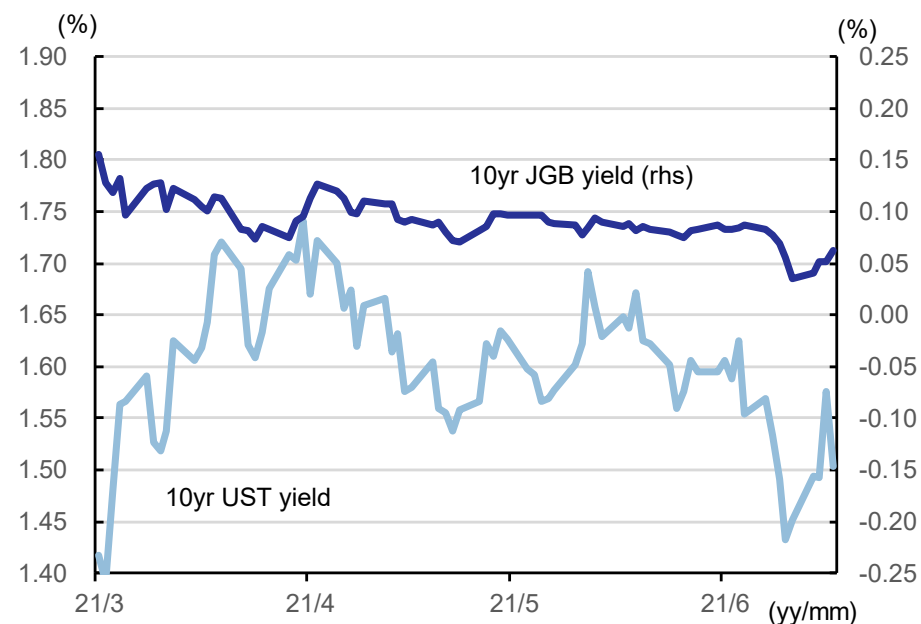
## Japanese bond market: 10yr JGB yield is projected to trend around 0.10%

- The yield on 10yr JGBs moved within a narrow band even after the breadth of fluctuation was clarified at  $\pm 0.25\%$ , and fell slightly to around 0.05% due to the decline in US interest rates.
- The 10yr JGB yield is projected to trend around 0.10%
  - BOJ's June plan for outright purchases of JGBs remains unchanged for the third consecutive month in terms of the amount and number of offers per auction.
  - As the rise in US interest rates remains gradual, upward pressure on the 10yr JGB yield is expected to be limited, and 10yr JGB yield is projected to trend around 0.10%.

### Trend in JGB yields



### 10yr UST yield and 10yr JGB yield



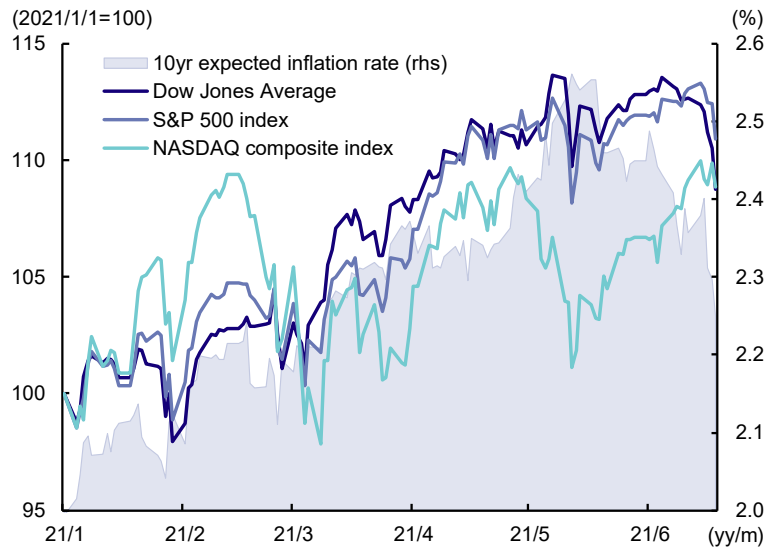
Source: Made by MHRT based upon Bloomberg

Source: Made by MHRT based upon Bloomberg

# US stock market: heavy upside expected due to caution against the tapering of monetary easing

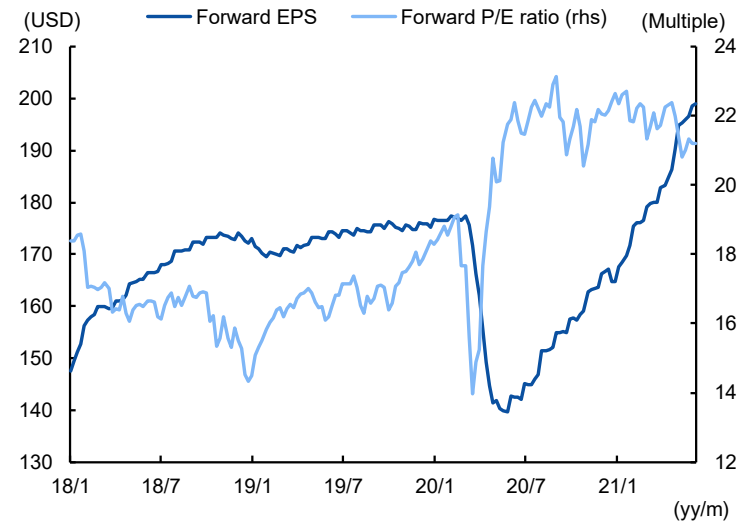
- The Dow Jones Average fell due to increasing concerns about an early rate hike following the FOMC meeting (June 15 and 16)
  - Given the ebb of medium to long-term inflation expectations due to speculation on early interest rate hikes, stocks sensitive to economic conditions such as the energy and materials declined, and served as a drag on the Dow Jones Average.
  - While high-tech stocks remained firm due to the decline of long-term interest rates, they edged down due to the decline of stocks sensitive to economic conditions.
- The forward EPS is continuing to rise due to expectations toward the normalization of economic activities. The forward P/E ratio stood at 21x, revealing the persistence of a strong sense of overvaluation.
- Despite the ongoing expansion of corporate earnings due to economic recovery, the upside of the stock market is forecast to be heavy due to a sense of overvaluation and caution against the tapering of monetary easing.

## US major stock indices



Note: Expected inflation rate is break-even inflation rate.  
Source: Made by MHRT based upon Refinitiv.

## S&P 500 forward EPS and forward P/E ratio

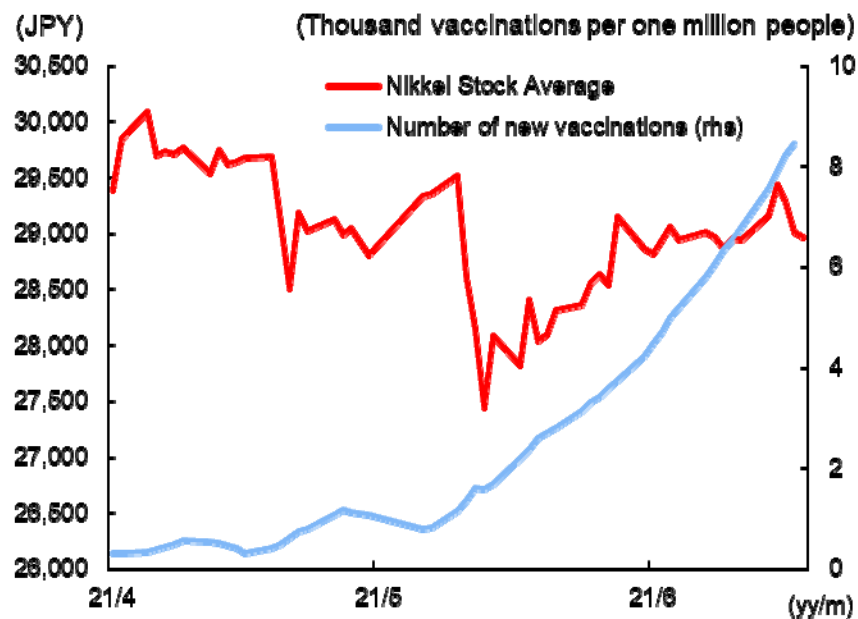


Note: Forward EPS and forward P/E ratio are based on 12-month forward forecast.  
Source: Made by MHRT based upon Refinitiv.

## Japanese stock market: although stocks sensitive to economic conditions will serve as a drag, the market is likely to remain firm due to the expansion of corporate earnings

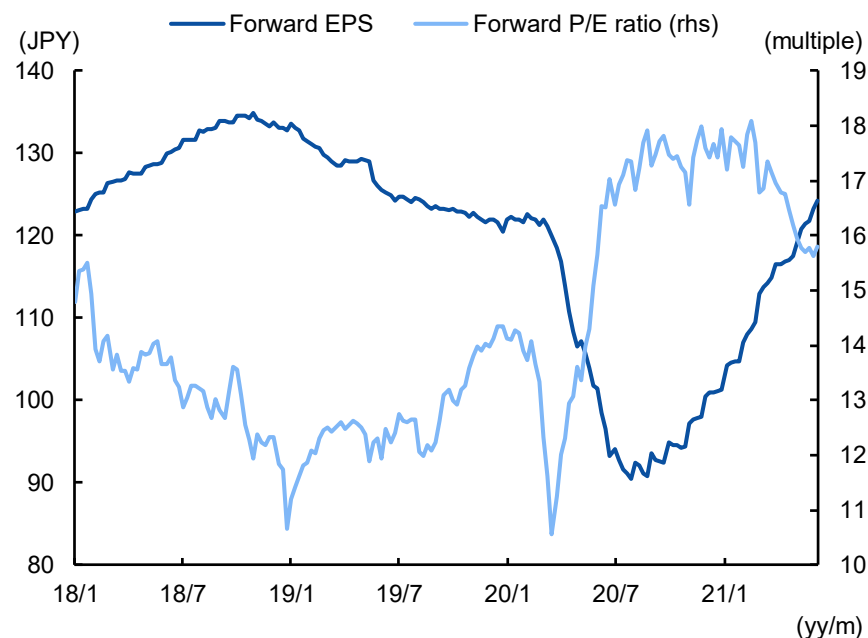
- Since mid-May, the Nikkei Stock Average has remained firm at around 29,000 yen due to the acceleration of vaccine rollouts in Japan and the depreciation of the yen. However, it temporarily dipped below 28,000 yen (June 21) due to the fall of US stocks.
- The 12-month forward EPS has continued to be revised upward for both the current and next term outlooks, and has recovered to pre-Covid-19 levels (end of 2019). On the other hand, the forward P/E ratio is higher than the past at a level of 15.8x (as of June 8), indicating a lingering sense of overvaluation.
- For the time being, even though stocks sensitive to economic conditions will serve as a drag against a backdrop of receding inflation expectations over the medium to long-term, Japanese stocks are likely to remain firm as corporate earnings expand due to the recovery of the real economy along with vaccine rollouts toward the end of the year.

### Nikkei Stock Average and number of new vaccinations



Source: Made by MHRT based upon Refinitiv, Our World in Data.

### TOPIX forward EPS and forward P/E ratio

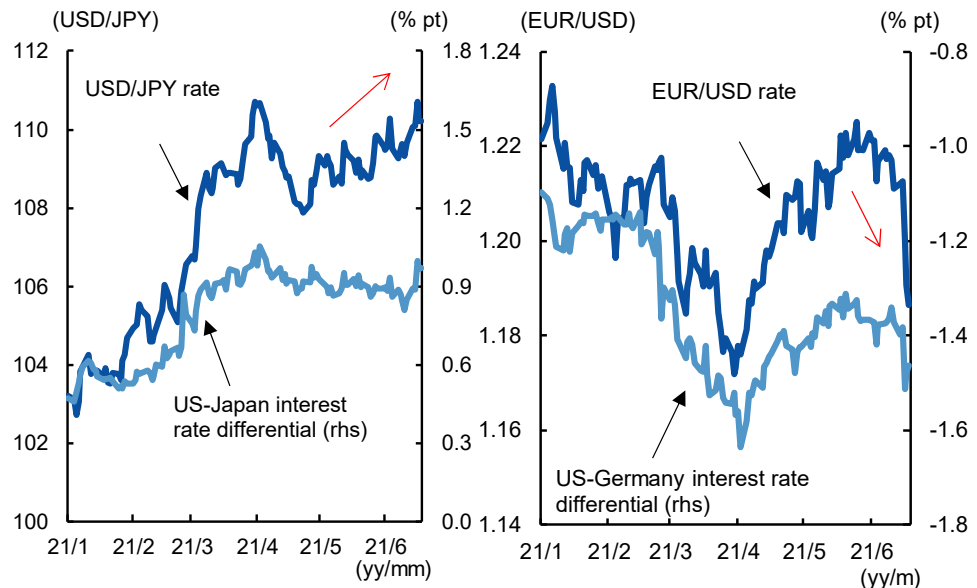


Note: Forward EPS and forward P/E ratio are based on 12-month forward forecast.  
Source: Made by MHRT based upon Refinitiv.

# Forex market: the dollar strengthened reflecting the results of the FOMC meeting. Looking forward, the dollar is expected to flatten out

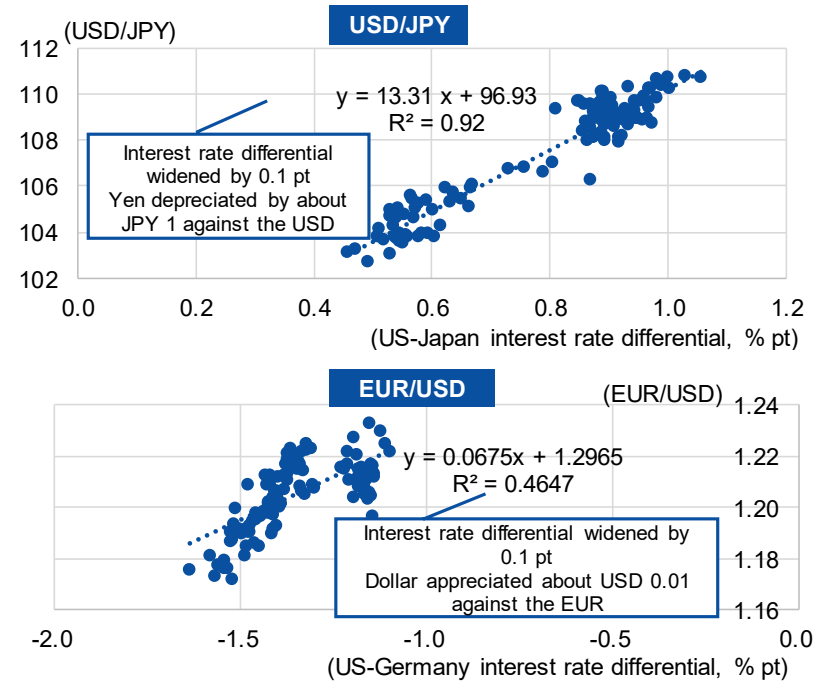
- Reflecting the results of the FOMC meeting in June (June 15 and 16), the dollar strengthened against the yen and the euro.
  - After the FOMC, US interest rates rose, particularly for medium-term bonds. Against the backdrop of widening US-Japan and US-Germany interest rate differentials, the dollar has strengthened against the yen and the euro. Furthermore, the EUR/USD rates are dominated by euro-selling, due to ECB Chief Economist Philip Lane's statement that it is too early to discuss exiting the PEPP.
- Looking forward, both the USD/JPY and EUR/USD rates are expected to remain flattened out.
  - Looking forward, the rise of US medium-term bonds, which was a factor in the appreciation of the US dollar, will pause, leading to the flattening of both the USD/JPY and EUR/USD rates.

## USD/JPY and EUR/USD rates and US interest rate differential



Note: Japan-US interest rate differential = US 5yr interest rate – Japan 5yr interest rate  
 US-German interest rate differential = German 5yr interest rate – US 5yr interest rate  
 Source: Made by MHRT based upon Bloomberg

## Sensitivity to interest rate differentials with the US

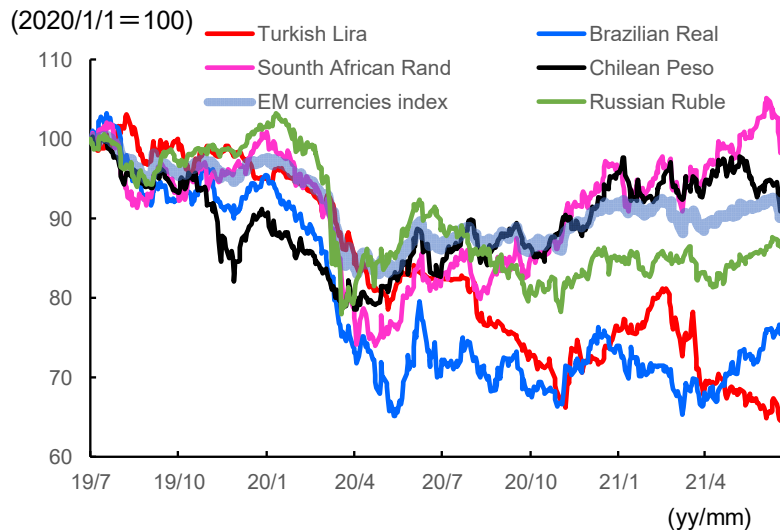


Note: The interest rate differential is those of the 5yr bond yields. The estimate period is from early 2021 to June 18  
 Source: Made by MHRT based upon Bloomberg.

# EM financial markets: currencies of emerging markets weaken due to concerns that US interest rates would be raised ahead of schedule

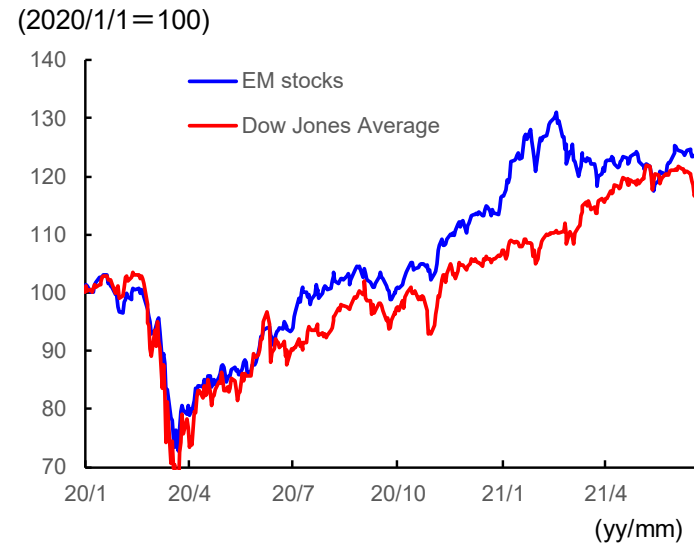
- Emerging market (EM) currencies depreciated, reflecting speculation that interest rates would be raised ahead of schedule after the US FOMC meeting.
  - As for the currencies of commodity-producing countries, the weakness of commodity prices also served as downward pressures upon the Chilean peso and South African rand.
  - In Turkey, the president's monetary policy intervention left the policy rate unchanged after March, which also contributed to the currency depreciation.
  - On the other hand, Brazil and Russia have implemented three consecutive interest rate hikes, given their high inflation rates, thus contributing to the appreciation of their currencies.
- EM stocks remain under downward pressures. The fall of US stocks following the FOMC also served as negative pressures.
- Even so, given prospects of a global economic recovery in 2021, both stocks and currencies are expected to pick up in the second half of 2021.

## Trend of EM currencies



Note: EM currencies are indicated by JP Morgan Emerging Markets FX Index  
Source: Made by MHRT based upon Refinitiv

## EM stocks and Dow Jones Average



Note: EM stocks are indicated by MSCI Emerging Markets  
Source: Made by MHRT based upon Refinitiv



## Outlook on the financial markets

		June 22, 2021	Apr-Jun	Jul-Sep	Oct-Dec
Japan	Interest rate on Policy-Rate balances (End of quarter, %)	-0.10	-0.10	-0.10	-0.10
	Newly-issued JGBs (10yr, %)	0.05	0.05 to 0.15	0.05 to 0.15	0.05 to 0.15
	Nikkei Stock Average (JPY)	28,884	28,400 to 29,400	28,900 to 29,900	29,700 to 30,700
US	Federal Funds rate (End-of-quarter, %)	0.00 to 0.25	0.00 to 0.25	0.00 to 0.25	0.00 to 0.25
	Long-term UST (10yr, %)	1.46	1.55 to 1.70	1.65 to 1.85	1.75 to 1.95
	Dow Jones Average (USD)	33,946	33,200 to 34,200	32,500 to 33,500	32,600 to 33,600
Eurozone	ECB deposit facility rate (End of quarter, %)	-0.50	-0.50	-0.50	-0.50
	Long term government bond (Germany, 10yr, %)	-0.16	-0.35 to -0.20	-0.45 to -0.25	-0.40 to -0.20
Forex	USD/JPY rate (USD/JPY)	110.65	107 to 109	107 to 109	108 to 111
	EUR/USD rate (EUR/USD)	1.194	1.19 to 1.22	1.18 to 1.21	1.15 to 1.19

Note: 1. The foreign exchange rates (actual) are NY closing rates.

2. The projected policy interest rate indicated for the Apr-Jun, Jul-Sep, Oct-Dec quarter is the end-of quarter closing rate, while others indicate that the average value in the quarter will fall within the range indicated.

Source: Made by MHRT based Bloomberg.

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