

Monthly Economic Report

August 24, 2021

Mizuho Research & Technologies, Ltd.

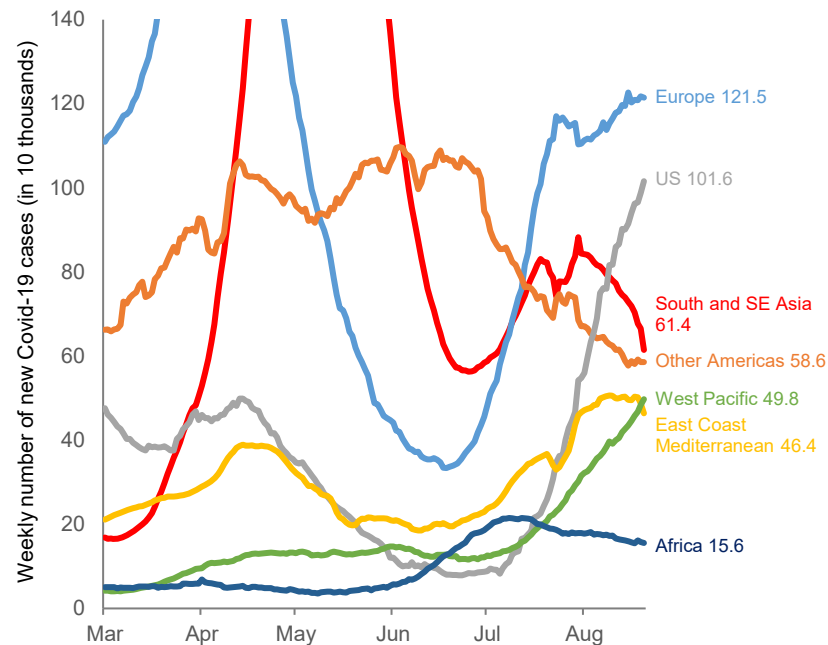
MIZUHO

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

The number of new Covid-19 cases around the world remains high, but the pace of increase is slowing

- The number of Covid-19 cases worldwide (cumulative) reached 211.73 million as of the morning of August 23.
- While the weekly number of new Covid-19 cases around the world stood at 4.55 million (previous week: 4.53 million), revealing an ongoing rise, the pace of increase has slowed.
 - By country, the number of new infections decreased in emerging countries in the Americas and Asia, such as Brazil, Argentina, Colombia, Indonesia, and Bangladesh.
 - On the other hand, the number of new cases surged in the US and major developed countries in Europe. Similarly, among emerging Asian countries, infections in the Philippines, Malaysia, Thailand, etc. show no sign of abating. The number of deaths is also increasing at the moment in the US, the UK, and France.

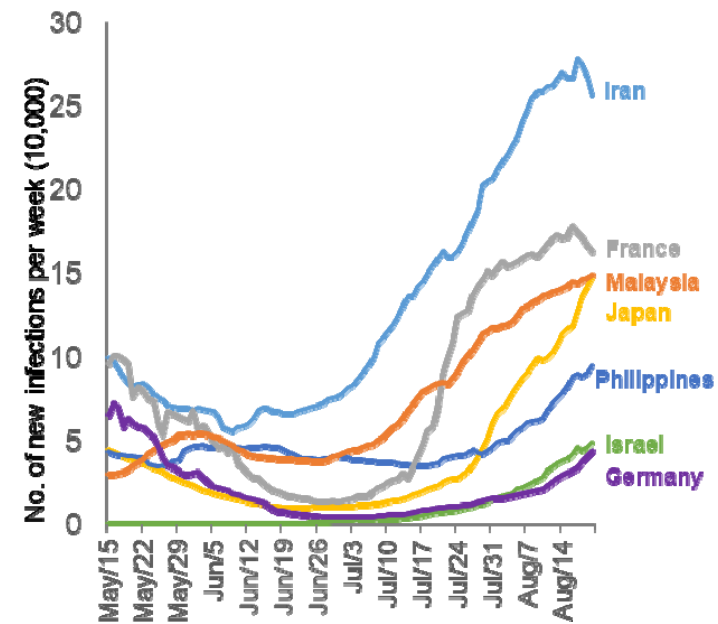
Weekly number of new Covid-19 cases reported worldwide



Note: Figures represent number of cases tallied as of August 21 (latest data as of August 20).
Regional classification based upon WHO.

Source: Made by MHRT based upon Johns Hopkins University and WHO.

Weekly number of new Covid-19 cases in countries currently showing large increases



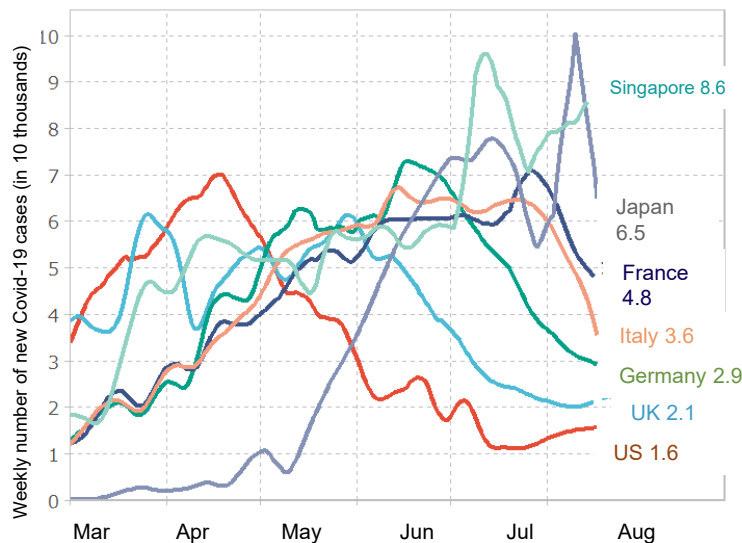
Note: Figures represent number of cases tallied as of August 21 (latest data as of August 20).

Source: Made by MHRT based upon Johns Hopkins University.

Global vaccination trends show that continental Europe's vaccination pace has slowed down

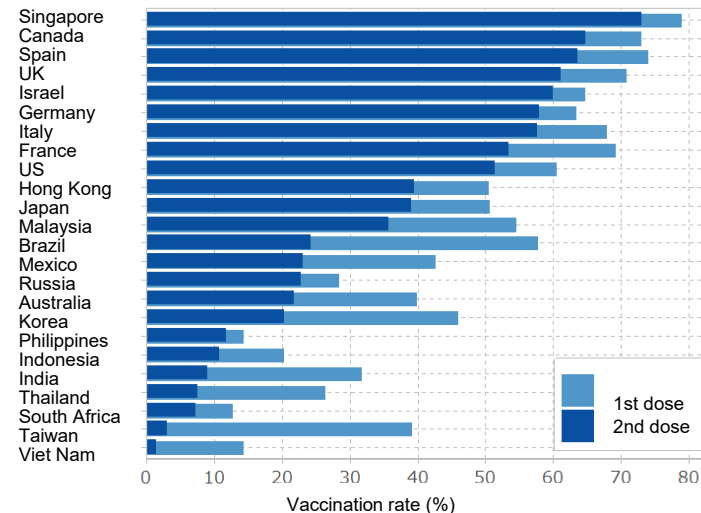
- Among major overseas countries, the pace of vaccination in Germany, France, and Italy has slowed. On the other hand, the pace of vaccination in the US and the UK has currently shown a slight rebound.
 - In the US and the UK, the recent spread of Covid-19 infections may have heightened people's sense of crisis, leading to an increased willingness to be vaccinated.
 - In Japan, the impact of the inclusion of data from workplace vaccinations has faded. The weekly pace of vaccinations remains firm at slightly above 6 doses per 100 people.
- Among the major countries, Singapore continues to top the list in terms of vaccination rate. In emerging countries, Malaysia's vaccination rate rose rapidly.
 - In the US, the percentage of those that have received their first vaccination dose finally exceeded 60% of the total population. This is now the lowest vaccination rate among the Western countries.
 - In Japan, over 50% of the total population has received their first vaccination dose. The rate has increased by more than 10% during the past one month, and is expected to surpass the US rate by the end of September.

Number of weekly vaccinations per 100 people (by country)



Note: Figures represent data tallied as of August 19 (latest data is from August 17).
Source: Made by MHRT based upon Our World in Data.

Vaccination rates in major countries by 1st and 2nd doses (percentage of the total population)

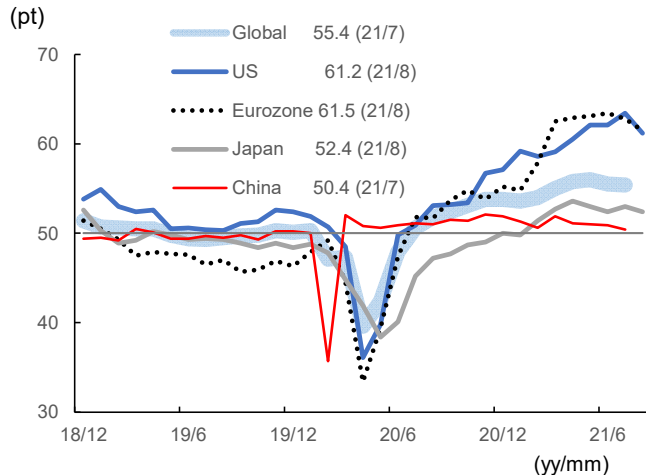


Note: Figures represent data tallied as of August 19 (latest data is from August 17).
Source: Made by MHRT based upon Our World in Data.

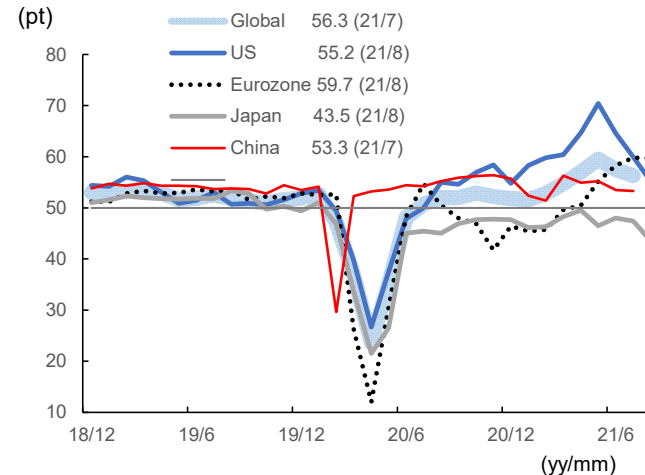
Current state of the global economy: July sees pause in the rise of global PMI

- In the US, the nonmanufacturing PMI in August fell for the third consecutive month.
 - Although the PMI remains above 50, which indicates corporate business expansion, Covid-19 infections are resurging in the US. It should be noted that the resurgence of Covid-19 infections may serve as a drag on service consumption etc., slowing down the pace of economic expansion.
 - Even in the Eurozone, where the nonmanufacturing PMI rose due to the easing of mobility restrictions, the improvement in business sentiment came to a pause in August.
- In China, both the manufacturing and nonmanufacturing PMIs declined. Production in the high-tech sector is firm, but flooding and Covid-19 infections are serving as downward factors.
- In Japan, the nonmanufacturing PMI remained below 50 in August due to the continued declaration of a state of emergency. Sluggishness in the nonmanufacturing sector is expected for the time being.

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 IHS Markit, the National Bureau of Statistics of China.

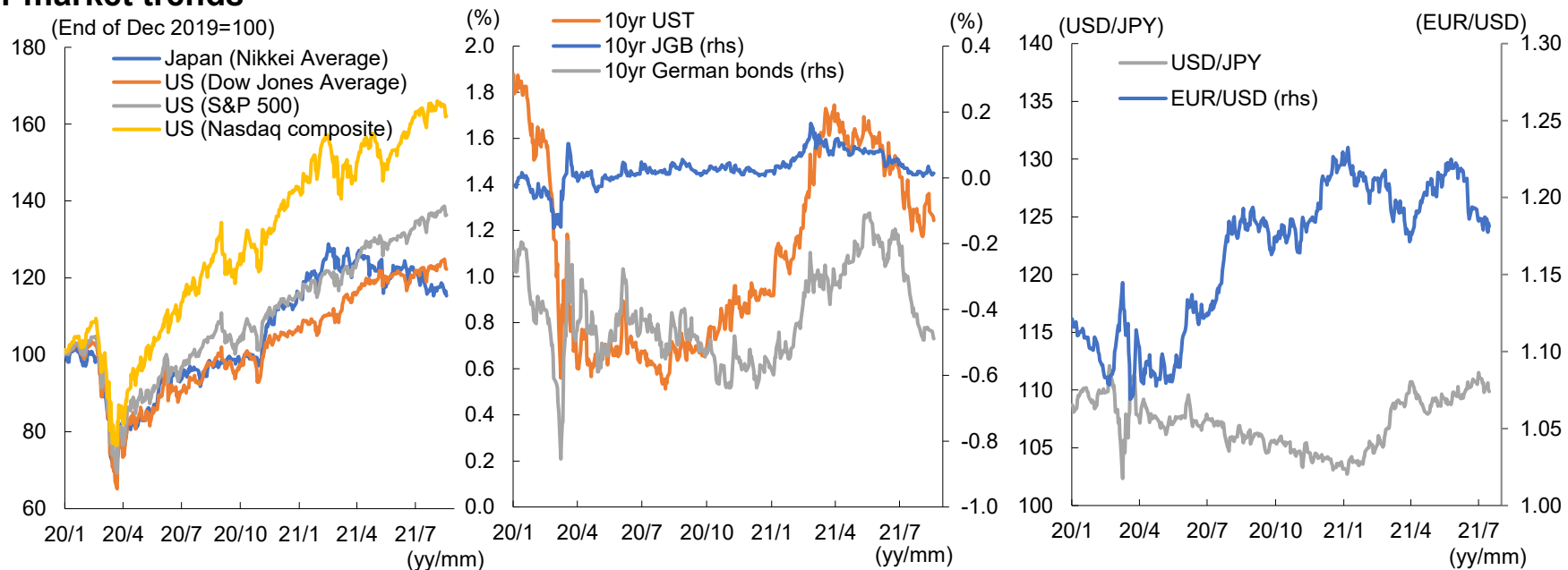
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Source: Made by MHRT based upon IHS Markit, the National Bureau of Statistics of China.

Overview of financial markets: US stocks remain steady on the back of strong corporate earnings

- US stocks remained steady on the back of strong second quarter earnings results, although weak US and Chinese economic indicators and the resurgence of Covid-19 infections weighed them down somewhat.
 - In the US, the Dow Jones Average and the S&P 500 index hit daily highs in mid-August for consecutive days on the back of strong second quarter earnings results. The US market remained at its record-high level, despite being weighed down by weak US and Chinese economic indicators, the spread of Covid-19 infections, and expectations of the start of tapering within the year. Japanese stocks, on the other hand, weakened due to concerns about the impact of the spread of Covid-19 infections on the economy, including factors such as the extension of the declaration of a state of emergency and further expansion of the areas subject to the declaration.
 - US long-term interest rates temporarily rose to the upper 1.3% range on favorable job reports and hawkish comments by FRB officials, but fell back to the 1.2% range due to deteriorating consumer confidence and the spread of Covid-19 infections.

Major market trends

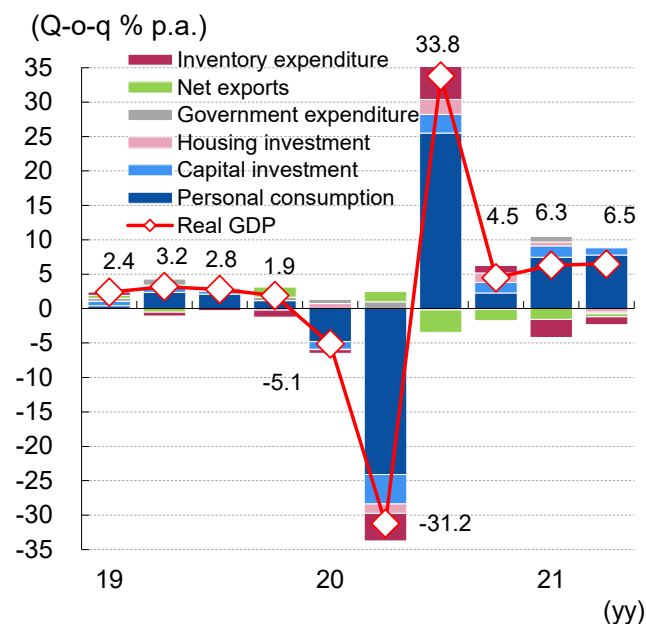


Note: All indexes show actual results up to August 19.
 Source: Made by MHRT based upon Refinitiv.

US Economy: Apr-Jun quarter GDP growth limited to a modest acceleration due to drag from supply constraints

- The real GDP growth rate in the Apr-Jun quarter (first estimate) was +6.5% q-o-q p.a., far below the market consensus (+8.5% q-o-q p.a.). The main factor dragging down growth was progress in inventory reduction due to supply constraints and a decline in housing investment.
 - Consumer spending continued to show double-digit growth, while capital investment was firm despite a slowdown. On the other hand, inventory investment and housing investment served as a drag on the overall growth rate.
 - ◆ Production is expected to recover in the second half of the year, when supply constraints will be alleviated, contributing to an upturn in the growth rate.

Real GDP growth



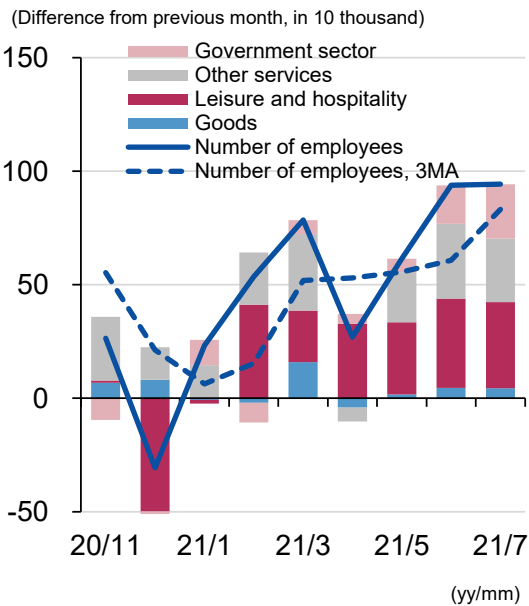
	20Q4	21Q1	21Q2	Key Points
Real GDP	+4.5	+6.3	+6.5	Modest acceleration in the growth in the Apr-Jun quarter
Personal consumption	+3.4	+11.4	+11.8	Substantial growth continues. Shift from goods to services is progressing amid easing of restrictions (goods consumption decelerating, services consumption accelerating).
Housing investment	+34.4	+13.3	-9.8	First decline in four quarters. Despite strong demand for housing, labor and material shortages (downward pressure on construction) and property shortages (downward pressure on sales commissions) are serving as a drag on housing investment.
Capital investment	+12.5	+12.9	+8.0	Growth decelerated. Construction investment continued to be sluggish, and machinery investment slowed, especially for motor vehicles.
Inventory investment (※)	+1.1	-2.6	-1.1	Negative growth for two consecutive quarters. Amid serious supply constraints, inventory recovery has been sluggish, with retailers drawing down inventories.
Government expenditure	-0.5	+4.2	-1.5	A reactionary drop from the previous quarter, when there was a large increase, mainly related to the financing program for small and medium-sized enterprises (Paycheck Protection Program, PPP) and vaccine purchases.
Net exports (※)	-1.7	-1.6	-0.4	Imports increased more than exports, with negative external demand contribution.
Exports	+22.5	-2.9	+6.0	Exports increased. However, despite a tailwind from the global economic recovery, the downturn in US domestic production and container shortages served as a drag on export recovery.
Imports	+31.3	+0.3	+7.8	Imports accelerated. Capital goods (expansion of investment in machinery) are the main driver for imports growth. Motor vehicle-related demand is expected to drop

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

Employment rose, primarily in services requiring face-to-face interactions, but growing Covid-19 concerns may serve as a drag going forward

- The number of employees increased significantly in July by +943 thousand m-o-m, while the cumulative total of May and June was revised upward by +119 thousand.
 - Employment growth continued to be driven by the leisure/hospitality industry, which is likely to benefit from the easing of Covid-19-related restrictions, but other industries also generally saw an increase.
 - Wages (hourly wages in the private sector) rose moderately by +0.4% m-o-m. Retail sales sector wages declined, while those for leisure/hospitality and transportation/warehousing also slowed. However, low-wage industries generally maintained somewhat high growth.
- The impact of the resurgence of Covid-19 infections on the latest survey appears to be limited, but growing concerns about the infection may serve as a drag on people's intention to work.
 - As of early July, the number of people not working due to concern about Covid-19 infections has been on a declining trend.

Number of employees by industry Private sector hourly wages



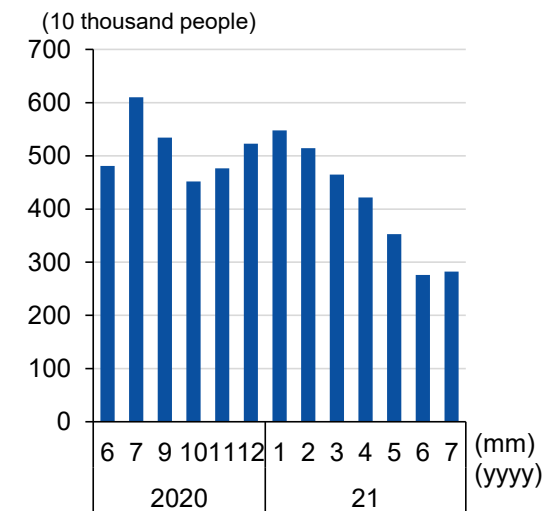
Source: Made by MHRT based upon US Department of Labor.

(M-o-m, % ch)

	April	May	June
Private sector	0.7	0.5	0.4
Constuction	1.0	0.5	0.3
Manufacturing	0.6	0.6	0.3
Wholesaling	0.4	0.4	0.1
Retail sales	0.9	0.9	0.5
Transport/warehousing	1.6	0.2	1.9
Public services	0.5	0.5	-0.1
Information services	1.0	-0.3	0.2
Financial activities	0.1	0.7	0.2
Professional and business services	0.7	0.8	0.4
Education and health services	1.2	-0.1	0.5
Leisure and hospitality services	1.4	1.2	1.8

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

Trends of people not working due to concern over Covid-19 infections

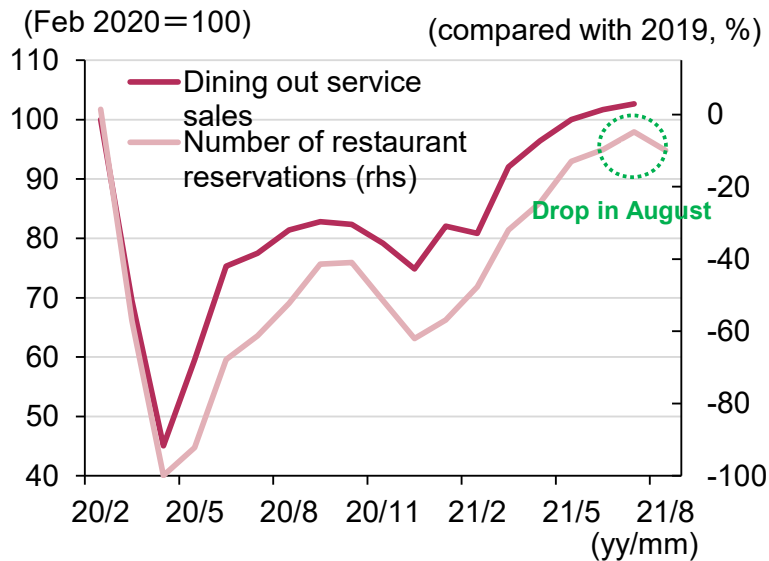


Note: The July 2021 data is for the week of July 6 only.
 Source: Made by MHRT based upon US Department of Commerce.

Sustained recovery in service consumption through July; downward pressure from concerns about Covid-19 infections in August

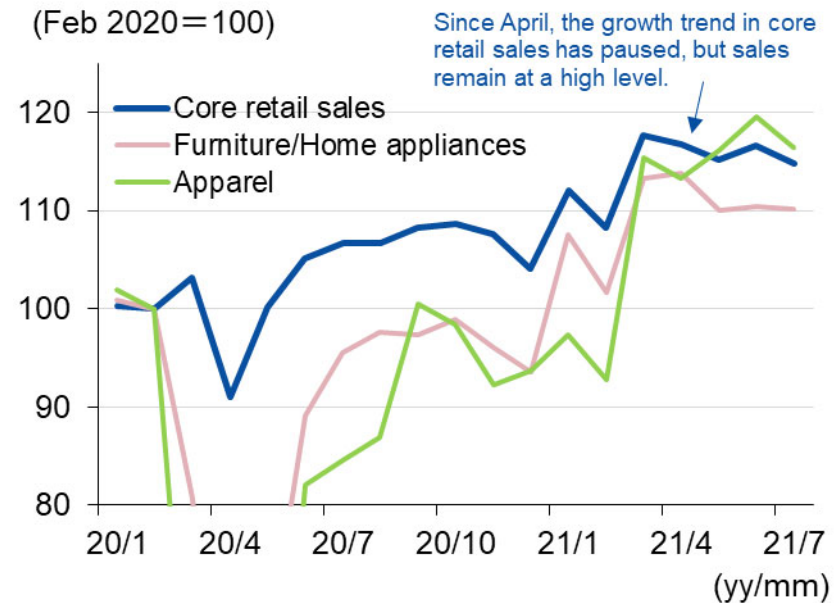
- In July, dining out sales in real terms (+0.9% m-o-m, MHRT estimate) increased and exceeded pre-Covid-19 levels. Real core retail sales (-1.6% m-o-m) declined, but remained at a high level. The shift of consumption from goods to services is progressing but at a moderate pace.
 - In terms of core retail sales breakdown, furniture/home appliances flattened out, while apparel sales declined. Overall, there is a general sense of peaking out, but core retail sales remain at a high level.
- Since the beginning of August, increasing concerns about the spread of Covid-19 infections appear to have been putting downward pressure on service consumption.
 - The number of restaurant reservations in the first half of August decreased from July. According to media reports, there have been decreased airline bookings and hotel reservations or increased cancellations in August.

Dining out service sales in real terms and number of restaurant reservations



Note: Dining out service sales indicate real value estimated by MHRT.
Source: Made by MHRT based upon US Department of Commerce.

Real core retail sales by industry

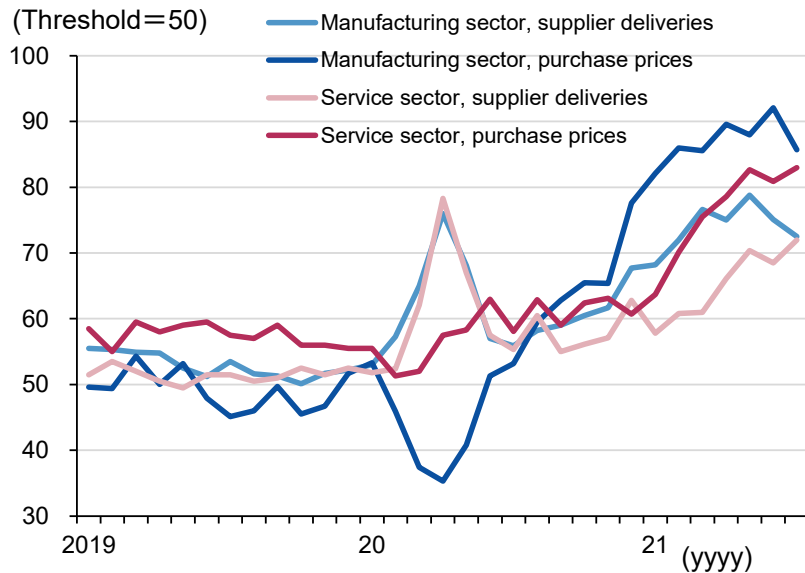


Note: Estimated real value by MHRT. Core retail excludes motor vehicles, building materials, gasoline, and dining out.
Source: Made by MHRT based upon US Department of Commerce.

Corporations in July continue to face strong demand and severe supply constraints

- The July ISM index registered high levels, with the new orders index remaining at a high level of over 60 for both the manufacturing and service sectors, while the supplier deliveries index registered over 70. This indicates that the pattern of the coexistence of strong demand and severe supply constraints weighing down business activity remained unchanged. Comments from corporations indicate wariness about whether the situation will improve.
 - The supplier deliveries and purchase price indices for the manufacturing sector dropped, indicating that supply has not become even further constrained. However, it appears that supply constraints continue to serve as a drag on production, with corporations commenting on the negative impact of logistics disruptions.
 - ◆ According to ISM, the average lead time for production materials is 86 days, a slight decrease from the recent peak (88 days in July), but an increase from the beginning of the year (68 days).
 - There were limited corporate comments citing the negative impact of the resurgence of Covid-19 infections (health care only).

ISM supplier deliveries and prices indices



Source: Made by MHRT based upon Institute for Supply Management.

Comments from corporations regarding ISM

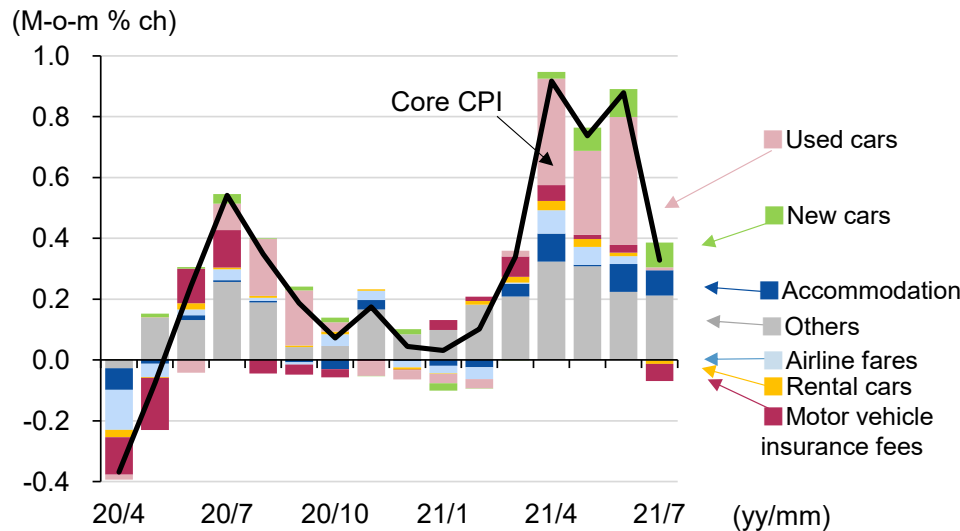
Current status of supply constraints	<ul style="list-style-type: none"> • Can only fill 75 percent of our order requirements due to the labor shortage. [Primary Metals] • The congestions at (the ports of) Long Beach/Los Angeles and Seattle have increased lead time by 15 days. Additional delays are occurring at the Chicago rail yard, (causing) two to three weeks of additional lead time. [Wholesale Trade]
Future supply constraints	<ul style="list-style-type: none"> • Meeting demand is just not possible due to force majeure situations, logistics, and labor shortages. We don't anticipate this ending until well into 2022. [Nonmetallic Mineral Products] • The slow movement of container traffic has definitely impacted our business. We expect the situation will take another year to correct itself. [Primary Sector] • (For supply chains) rumor is a full return to normal may be nearer to year's end, but the situation is progressing. [Chemical Products]
Spread of Covid-19 infections	<ul style="list-style-type: none"> • The COVID-19 delta variant is impeding our ability to manage increased surgical volumes due to increased COVID-19 case admissions. [Health Care]

Source: Made by MHRT based upon Institute for Supply Management.

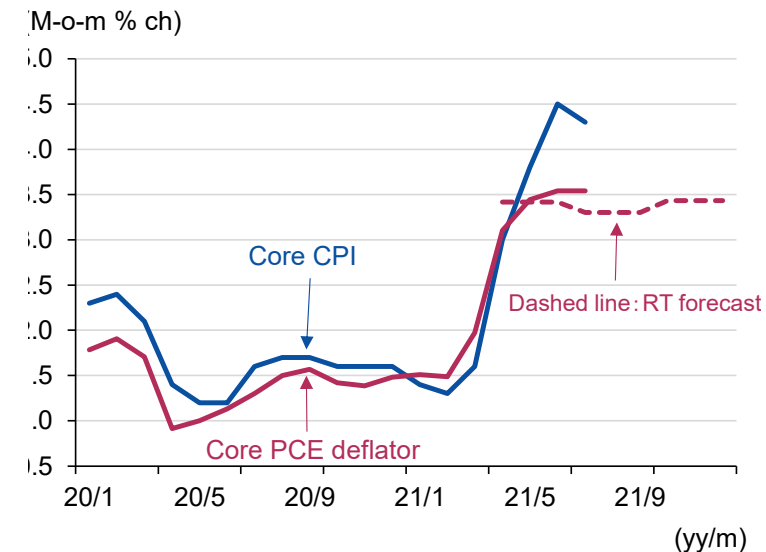
Pause in sharp rise of inflation, reflecting the fading impact of tight supply-demand balance and normalization

- In July, the rise of the core CPI slowed to +0.3% m-o-m (June: +0.9% m-o-m). The main reason for the slowdown was a pause in the rapid rise of used car prices.
 - Used car prices have more or less levelled off at +0.2% m-o-m (June: 10.5% m-o-m). Its contribution to overall core CPI shrank by 0.4%pt. Despite the sharp rise of accommodation fees thus far (+6.0% m-o-m), it has returned to pre-Covid-19 levels. The pace of rise is expected to be moderate going forward.
 - On the other hand, while airline fares (-0.1% m-o-m) have taken a downturn, this is most likely temporary (airline fares are currently in the process of normalization).
- Even though the year-on-year rise of the core CPI stood at a high +4.3% in July (June: +4.5% y-o-y), the sharp pace of acceleration thus far appears to have paused.
 - Given these results, we expect the rise of the core PCE deflator to come to in July (+3.5% y-o-y) (June: +3.5% y-o-y).

Core CPI (m-o-m ch)



Core CPI and core PCE deflator



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

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

Most FOMC participants expect tapering to begin this year (July FOMC minutes)

- FOMC will implement tapering in December if it is confirmed that the spread of Covid-19's Delta variant will not cause a serious impact on the economy and employment.
 - Even though there is also a high possibility that tapering will be implemented at the November FOMC meeting, it is expected that time is needed to determine the impact of the Delta variant.
- The FOMC will make an announcement in advance regarding the timing and pace of tapering at the September FOMC. The pace of tapering is expected to be such that tapering will conclude before the conditions for raising the federal funds rate are satisfied (hawkish participants expect to raise the rate in 2022). Treasury securities and MBS are expected to be proportionally tapered.

Overview of the minutes of the July FOMC meeting

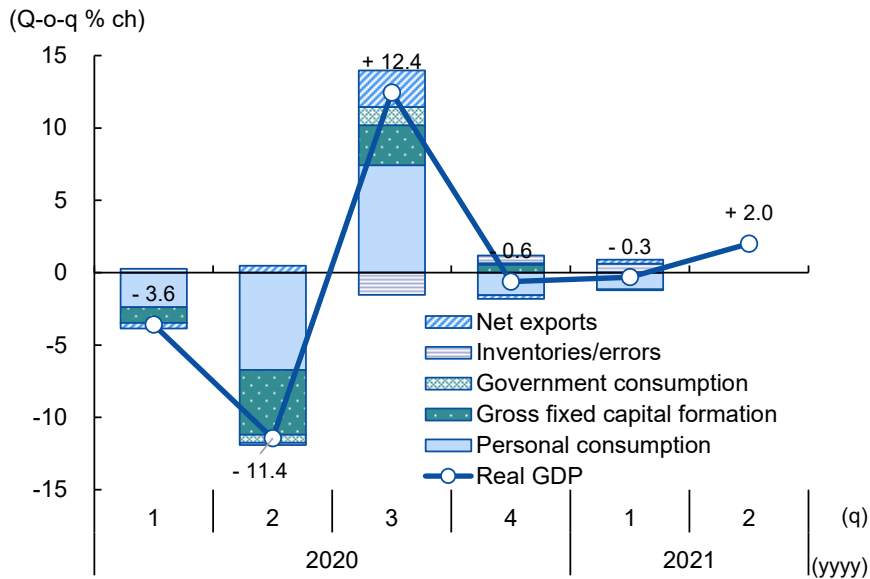
Discussions	Majority view	Minority view
Views on when to start reducing the pace of asset purchases	Start this year <ul style="list-style-type: none"> • Standard satisfied with respect to the price-stability goal • Standard close to being satisfied with respect to the maximum-employment goal • Earlier start to risk-management also suggested 	Early next year <ul style="list-style-type: none"> • Conditions in the labor market not close to meeting the standard • Uncertainty around inflation dynamics, etc.
Views on appropriate pace of tapering	End tapering before raising the federal funds rate (An earlier start could be accompanied by) more gradual reductions and mitigate the risk of an unintended tightening of financial conditions	
Views on MBS	Reduce net purchases of Treasury securities and agency MBS proportionally and end both at the same time <ul style="list-style-type: none"> • Treasury securities and MBS had similar effects on financial conditions • Purchases not intended as credit allocation 	Reduce MBS purchases more quickly <ul style="list-style-type: none"> • Housing sector exceptionally strong and does not need support • Purchases could be misinterpreted as a type of credit allocation

Source: Made by MHRT based upon FRB.

The Eurozone economy: Eurozone GDP grew for the first time in three quarters; rapid recovery of consumption contributed to growth

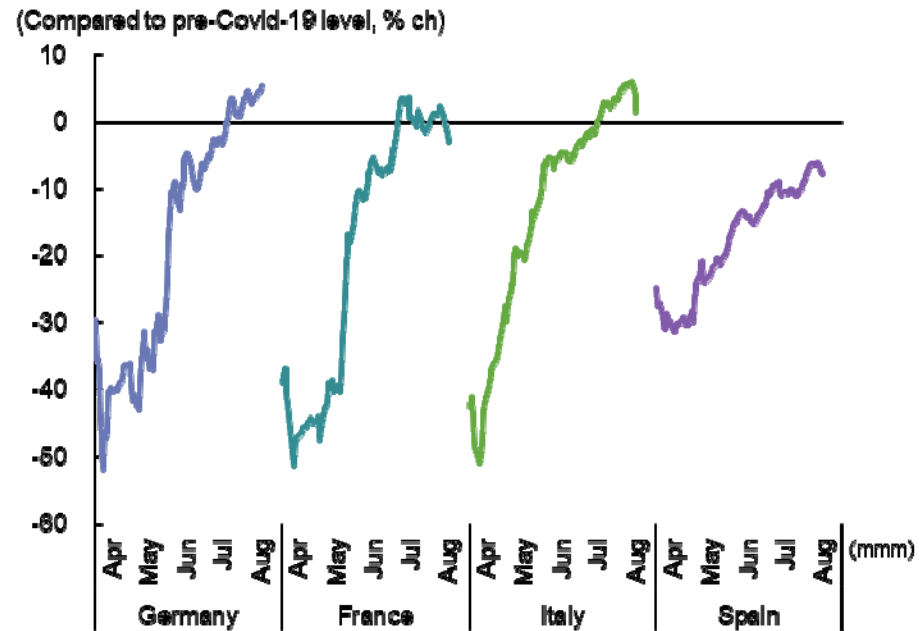
- Eurozone real GDP growth for the Apr-Jun quarter stood at +2.0% q-o-q, recording positive growth for the first time in three quarters. This was due to a strong recovery in household consumption following the easing of mobility restrictions.
 - By country, major countries such as Germany (+1.5% q-o-q), Spain (+2.8% q-o-q), and Italy (+2.7% q-o-q) all posted positive growth.
 - According to releases on the components of GDP growth for France, service consumption increased due to the easing of mobility restrictions from late May, thus serving as a boost to overall growth.
- Despite the slowdown of consumption in many of the major countries due to factors such as the pause in the expansion of mobility, the odds are high that GDP growth will remain in positive territory.

Eurozone: real PMI



Note: Real GDP q-o-q growth and the degree of contribution by demand component.
Source: Made by MHRT based upon Eurostat.

Eurozone: retail sales and leisure mobility in major countries

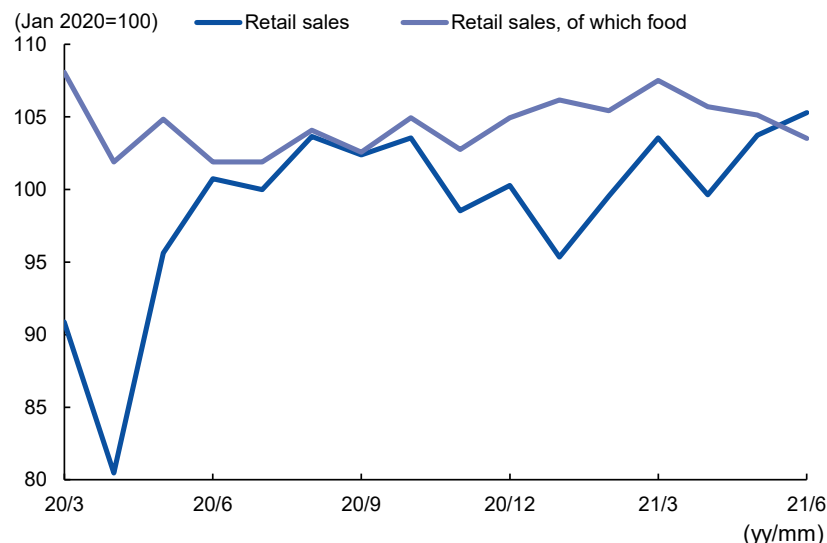


Note: Latest data as of August 15. 7-day backward moving average.
Source: Made by MHRT based upon Google LLC.

Retail sales slowed in June; recovery in goods consumption expected to slow down and level off

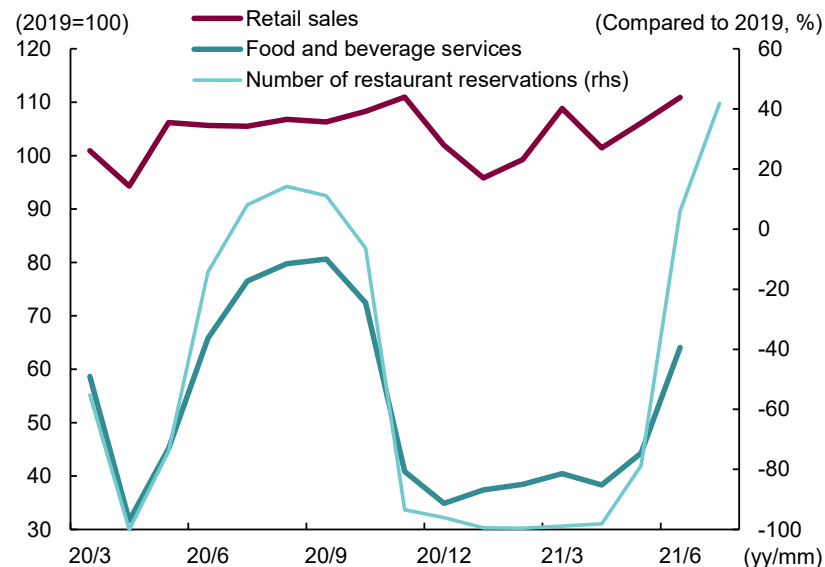
- Eurozone real retail sales (excluding motor vehicles) in June slowed to +1.5% m-o-m, along with the decline of stay-at-home consumption. Going forward, goods consumption is expected to level off.
 - Food sales declined month-on-month for the third consecutive month against the backdrop of increased opportunities to dine out as restaurants re-opened.
- In Germany, consumption of food and beverage services rebounded sharply in June due to the easing of mobility restrictions.
 - However, in view of the slowdown in rise of restaurant reservations since the beginning of July, it should be noted that factors such as concerns over Covid-19 infections, notably the spread of the Delta variant, may serve as a drag on service consumption.

Eurozone: real retail sales



Note: Excludes motor vehicles.
Source: Made by MHRT based upon Eurostat.

Germany: retail sales and eating/drinking sales

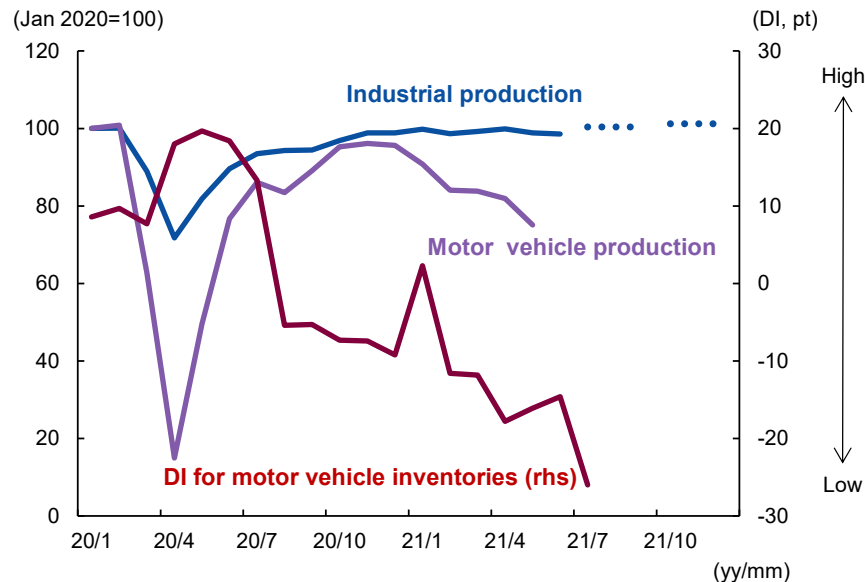


Note: Real terms
Source: Made by MHRT based upon the Federal Statistical Office of Germany, and OpenTable.

Industrial production fell slightly in June reflecting output cuts of motor vehicles. Production should remain flat going forward

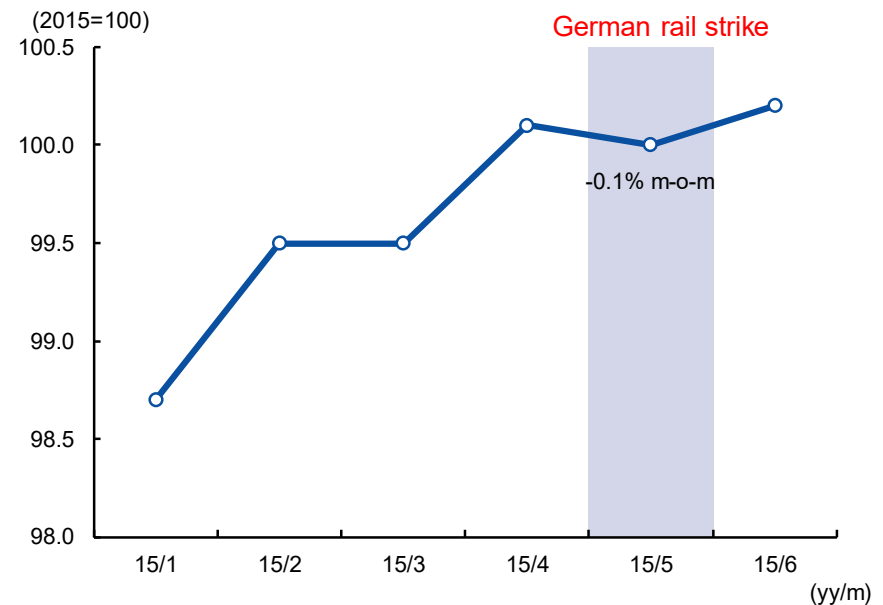
- Eurozone industrial production fell in June (-0.3% m-o-m), declining for two consecutive months. It remains below the pre-Covid-19 level (Jan 2020=100, 98.5). The reduction in motor vehicle production (-1.4% m-o-m) due to semiconductor shortages continued to serve as drag on overall industrial production.
 - The DI for motor vehicle inventories fell further in July. Although demand for motor vehicles is firm, supply constraints continue to weigh on production in the Eurozone.
- In Germany, Germany's train drivers' union (Gewerkschaft Deutscher Lokomotivführer, GDL) went on strike on August 11 due to unsuccessful negotiations over wages. The strike is expected to have little impact on production for the time being, but if it is prolonged or occurs frequently, it could disrupt logistics networks and spur supply constraints.
 - During the strike in May 2015 (lasting 6 days), industrial production declined slightly (-0.1% m-o-m), mainly due to the impact on transportation of chemicals and steel.

Eurozone: industrial production



Note: The dotted line is the forecast by MHERT (quarterly average). The reading of zero is the "expansion-contraction" threshold for the inventory DI.
 Source: Made by MHERT based upon Eurostat and European Commission.

Germany: industrial production (May 2021)

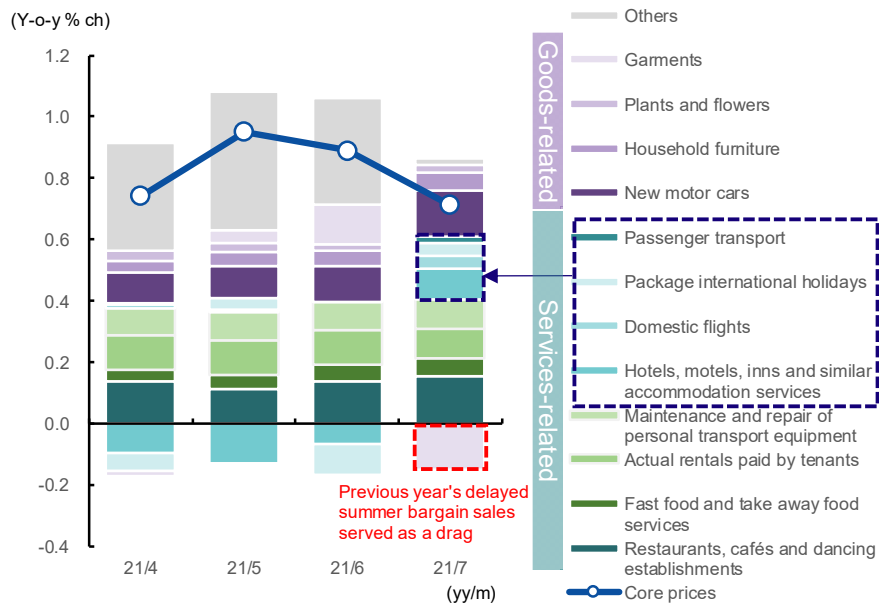


Source: Made by MHERT based upon Eurostat.

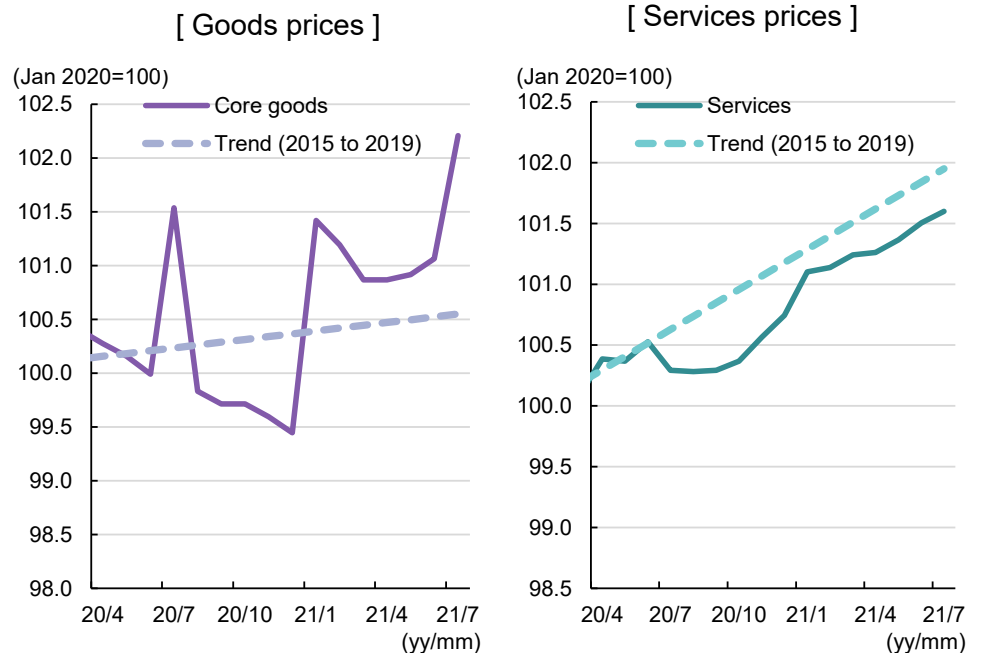
Although Eurozone core prices slowed in July, this should be temporary

- In July, Eurozone consumer prices (+2.2% y-o-y, final) rose +0.3%pt from the previous month against a backdrop of rising energy and food prices.
- Core prices (+0.7% y-o-y) fell -0.2%pt from the previous month. However, since this is largely due to the delayed start of summer bargain sales in the previous year, the decline is assessed to be temporary. Prices are expected to rise to around 2% going forward reflecting the rebound from last year's VAT tax cut and the resumption of economic activity.
 - The recovery in travel demand due to the easing of mobility restrictions lifted service prices. The price level is still below the pre-Covid-19 trend, indicating that there is room for further rises.
 - The core goods price level rose at a faster pace. The price level of core goods should remain high for the time being reflecting soaring raw material prices and supply constraints.

Eurozone: core prices (composite, excl. energy and food, etc.)



Eurozone: goods/service price trend



Source: Made by MHRT based upon Eurostat.

Note: Seasonally adjusted value.
Source: Made by MHRT based upon ECB.

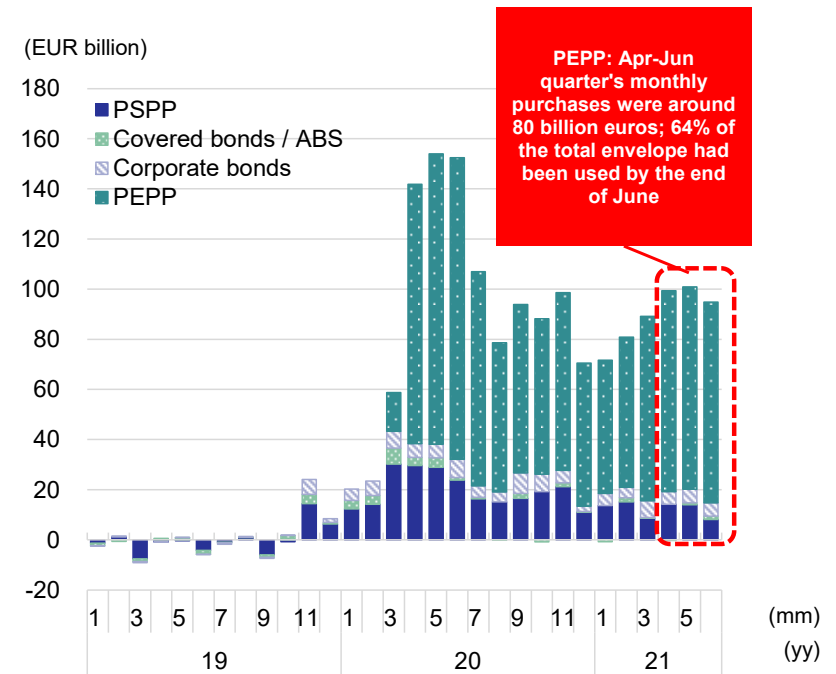
ECB revised its forward guidance in line with its new monetary policy strategy. Policy stance to continue monetary easing

- At the Governing Council meeting on July 22, the ECB revised its forward guidance for the policy rate in line with its new strategy and symmetric 2% inflation target. President Christine Lagarde expressed the ECB's intention "to avoid premature tightening."
 - The forward guidance was revised to maintain the policy rate until (1) the inflation outlook reaches 2% by the mid-point of the projection horizon, (2) inflation remains durably at around 2% for the rest of the projection horizon, and (3) progress in underlying inflation is consistent with the inflation target.
- No discussion was held on the pace of PEPP purchases, or whether to increase or extend the PEPP envelope. ECB's updated decision will be made based on the September ECB staff projections.

Key points of the ECB Governing Council meeting (July 22)

Forward guidance on interest rates	<p>The Governing Council expects the key ECB interest rates to remain at their present or lower levels until the ECB sees that the following conditions are met:</p> <p>(1) the inflation outlook reaches 2% by the mid-point of the projection horizon; (2) it remains durably at 2% for the rest of the projection horizon; and (3) progress in underlying inflation is sufficiently advanced to be consistent with inflation stabilizing at two per cent over the medium term.</p> <p>*Previous guidance The Governing Council expects the key ECB interest rates to remain at their present or lower levels until: (1) the inflation outlook rises to a level sufficiently close to, but below, 2 per cent over the medium term; (2) the inflation outlook converges robustly to the inflation target; and (3) such convergence has been consistently reflected in underlying inflation dynamics.</p>
Inflation outlook	(In reaction to the previous year) The Governing Council expects inflation to increase further over the coming months and to decline again next year.
Financing conditions	Financing conditions for most firms and households remain at favorable levels.
Pandemic Emergency Purchase Program (PEPP)	<p>Keep the current pace of purchases.</p> <p>The pace of purchases from September onwards and any extension of the March '22 end date were considered to be too premature to discuss and not issues for debate.</p>

ECB: outstanding asset purchases

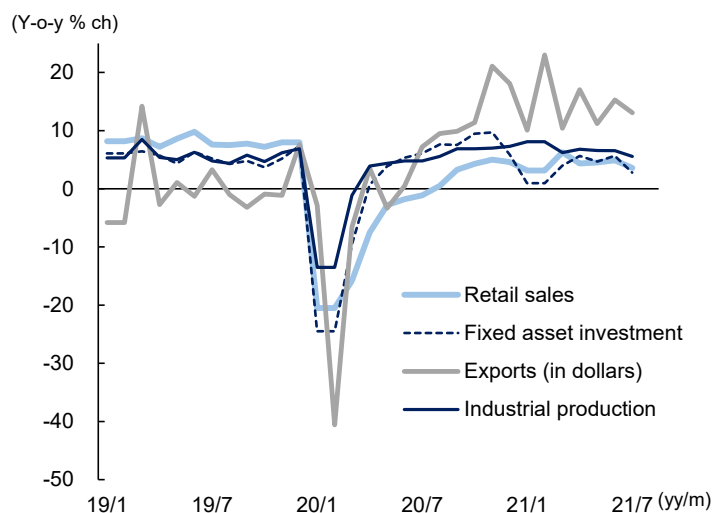


Source: Made by MHRT based upon ECB.

Chinese economy: key monthly indicators weakened in July

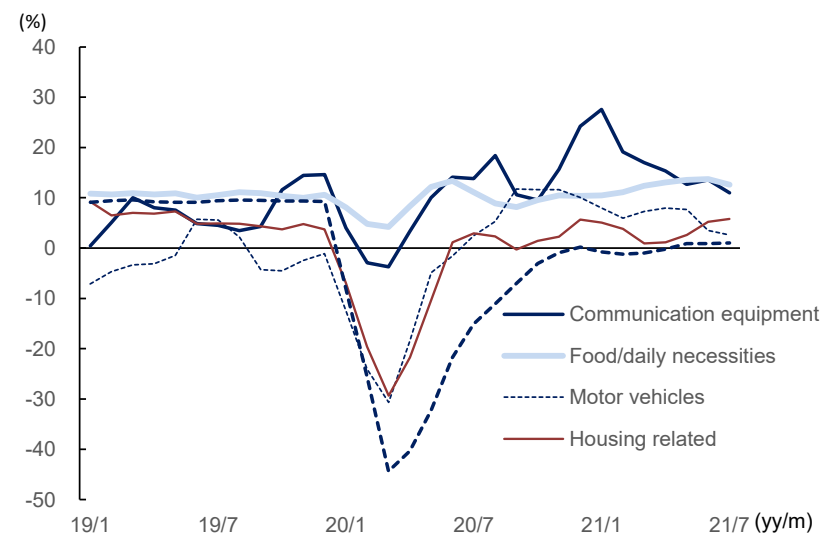
- The rise of all key monthly indicators moderated in July due to the impact of natural disasters and the resurgence of Covid-19 infections.
 - The production adjustment in mining and other industries was also a negative factor. The high-tech sector, which continues to be firm, remained on an expansionary trend.
 - Investment in real estate and infrastructure showed a clear downward trend reflecting factors such as the reinforcement of real estate-related regulations and the flood disasters.
 - Consumption of food and daily necessities is firm. However, demand for telecommunications equipment has peaked, and motor vehicles-related consumption has also slowed significantly due to semiconductor shortages.
- While the decline in consumption and investment may be attributed in part to natural disasters and regulations, the rise of future uncertainties may not be ruled out altogether. Although the economy as a whole is following a recovery path, the pace of recovery is expected to moderate.

Key monthly indicators



Note: Y-o-y growth until 2020, and 2-yr average growth compared to 2019 from 2021 onward.
Source: Made by MHRT based upon the National Bureau of Statistics of China and CEIC data.

Goods/service consumption

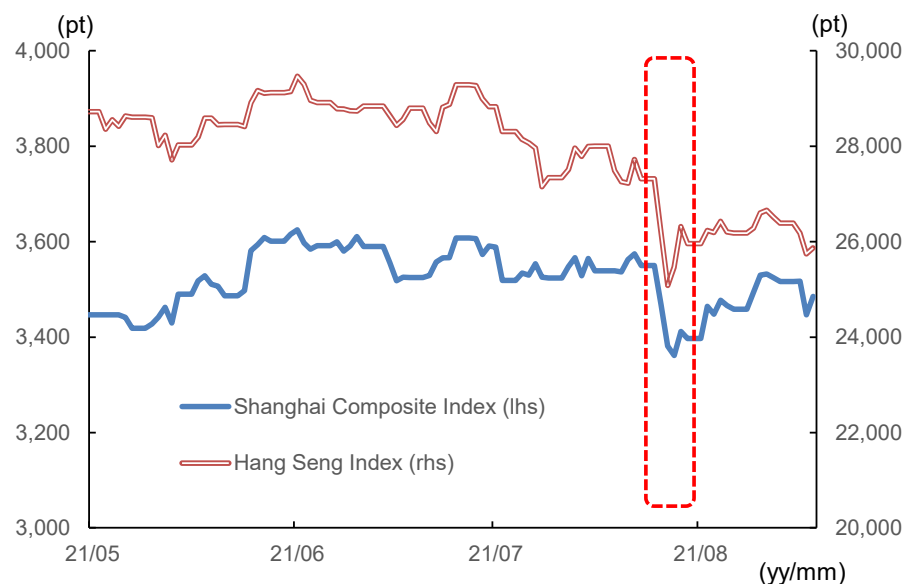


Note: Y-o-y growth until 2020, and 2-yr average growth compared to 2019 from 2021 onward.
3-month moving average.
Source: Made by MHRT based upon the National Bureau of Statistics of China and CEIC data.

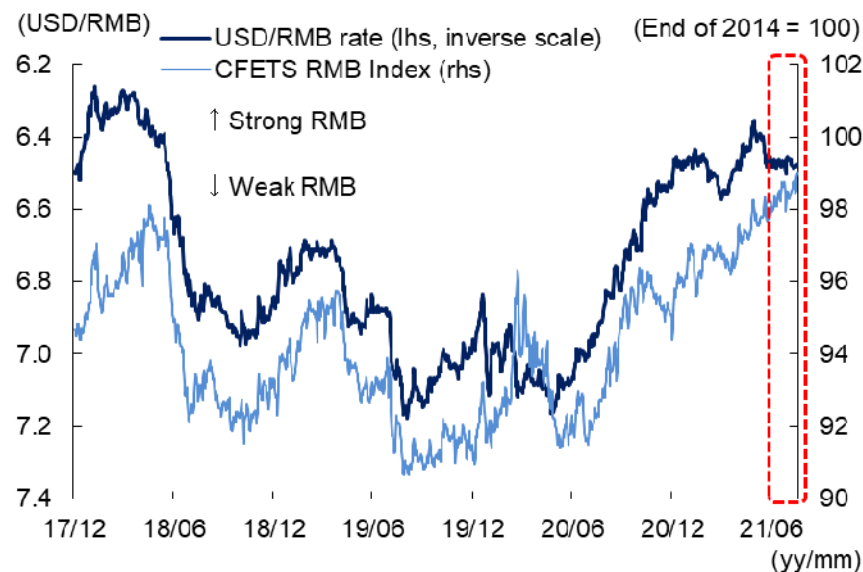
Education and internet-related stocks fell sharply due to tighter government regulations. The RMB exchange rate continues to move in a narrow range

- On July 26, Chinese stocks related to education and the internet, including EdTech, fell sharply on the stock market after the Chinese government announced plans to tighten regulations on the education industry, including plans to turn tutoring companies for elementary and junior high school students into non-profit organizations, and to increase control over IT platform companies.
 - Although the market unrest was contained within a few days, caution about regulatory risks is growing. The Hong Kong market, where many tech stocks such as Alibaba and Tencent are listed, is expected to remain weak for the time being.
- The yuan temporarily weakened to 1 USD= 6.51 RMB when stock prices fell, but later recovered somewhat and is moving in a narrow range around the upper 6.40 yuan level.
 - Amid the lack of market-moving incentives, there is a risk that pressure to weaken the yuan will increase depending on movements by the FRB toward policy normalization and Chinese government regulatory actions.

Shanghai Composite Index and Hang Seng Index



RMB-USD rate and CFETS RMB index



Source: Made by MHRT based upon Shanghai Stock Exchange, Hang Seng Indexes Company, and CEIC Data.

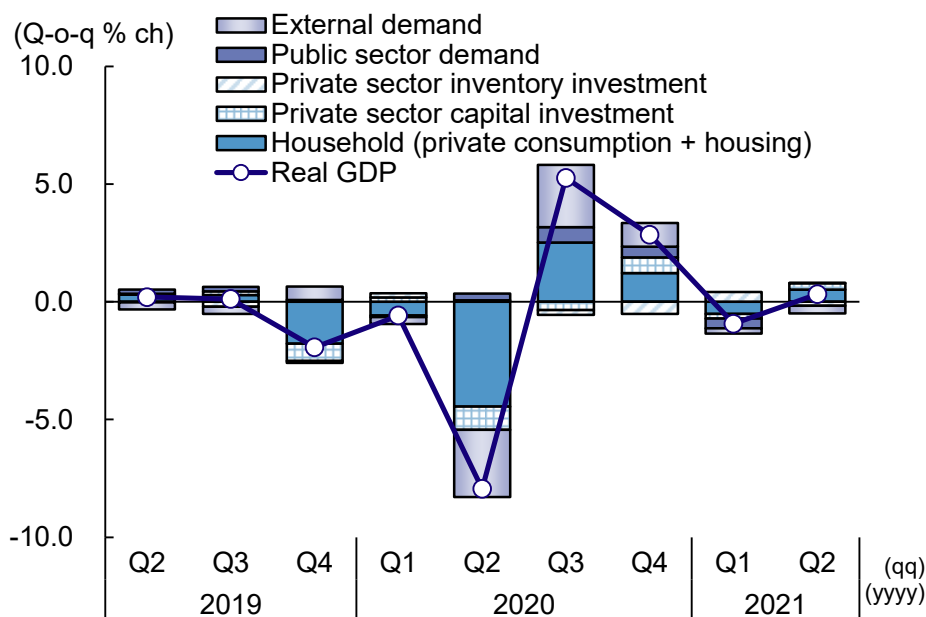
Note: The CFETS RMB Index are estimates by MHRT. Daily data. Most recent data is from August 18, 2021.

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

The Japanese economy: Apr-Jun quarter growth turned positive for the first time in two quarters. Spread of the Delta variant may serve as a negative factor in the Jul-Sep quarter

- The *First Preliminary Quarterly Estimates of GDP* (“1st QE”) revealed that Japan’s real GDP growth in the Apr-Jun quarter of 2021 was +0.3% q-o-q (+1.3% p.a.), the first positive growth in two quarters.
 - Exports maintained their growth trend, boosted by strong overseas economies, particularly in the US and China, as well as the robust semiconductor market. Capital investment also marked positive growth for the first time in two quarters, mainly due to the resumption of replacement investments.
 - Personal consumption dropped in the period from April to May due to the third declaration of a state of emergency, but picked up in June amid the easing and lifting of restrictions.
 - For the Jul-Sep quarter, the spread of the Delta variant, semiconductor shortages, and the reduced supply of components from Southeast Asia are expected to serve as negative factors.

Apr-Jun quarter of 2021 (1st QE)



	2020			2021	
	Apr-Jun	Jul-Sep	Oct-Dec	Jan-Mar	Apr-Jun
Real GDP	-7.9	5.3	2.8	-0.9	0.3
(Q-o-q % change, p.a.)	-28.2	22.8	11.9	-3.7	1.3
(Y-o-y % change)	-10.1	-5.6	-1.0	-1.3	7.5
Domestic demand	-5.1	2.5	1.8	-0.7	0.6
	(-5.1)	(2.6)	(1.8)	(-0.7)	(0.6)
Private sector demand	-7.2	2.6	1.9	-0.4	0.9
	(-5.4)	(2.0)	(1.4)	(-0.3)	(0.6)
Personal consumption	-8.3	5.1	2.3	-1.0	0.8
Housing investment	0.6	-5.7	0.0	0.9	2.1
Capital investment	-6.0	-2.1	4.3	-1.3	1.7
Inventory investment	(0.1)	(-0.2)	(-0.5)	(0.4)	(-0.2)
Public sector demand	1.1	2.3	1.6	-1.5	0.1
	(0.3)	(0.7)	(0.4)	(-0.4)	(0.0)
Government consumption	0.7	2.8	1.8	-1.7	0.5
Public investment	2.9	0.7	1.0	-1.0	-1.5
External demand	(-2.9)	(2.6)	(1.0)	(-0.2)	(-0.3)
Exports	-17.5	7.3	11.7	2.4	2.9
Imports	-0.7	-8.2	4.8	4.0	5.1
Nominal GDP	-7.6	5.4	2.3	-1.0	0.1
GDP deflator (y-o-y % change)	1.4	1.2	0.2	-0.1	-0.7

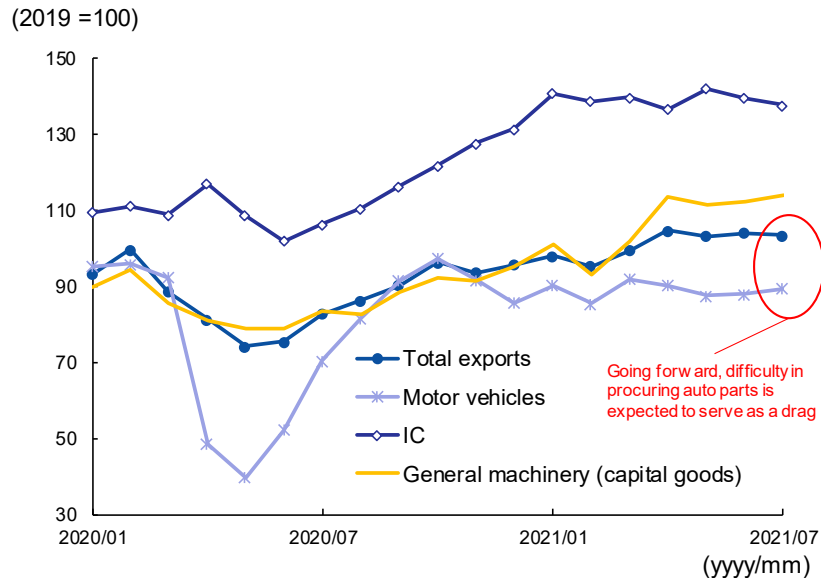
Note: Figures in the right-hand chart are on a q-o-q basis (in real terms) unless otherwise noted. The figures in parentheses represent the contribution to growth. Figures for the Apr-Jun quarter 2021 are forecasts.

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

Decrease in imports of motor vehicle parts from Southeast Asia expected to serve as a drag on production and exports

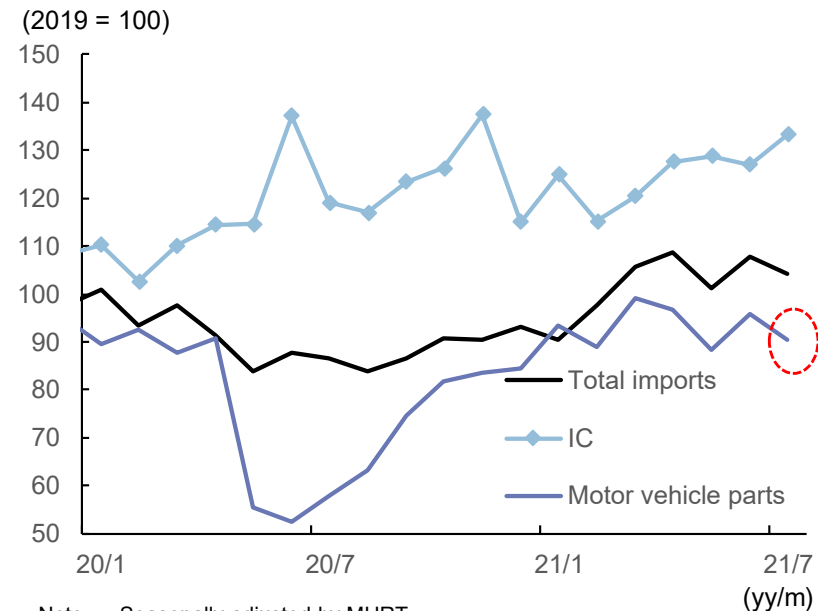
- The export volume index fell by -0.5% m-o-m in July, the first decline in two months.
 - In addition to ICs, where negative growth was recorded for the second consecutive month, non-ferrous metals and computer-related parts also declined. On the other hand, motor vehicle exports temporarily increased as the impact of the semiconductor factory fire faded. Capital goods such as semiconductor manufacturing equipment also served as a positive factor pushing up exports.
- Difficulty in procuring motor vehicle parts from Southeast Asia is expected to serve as a downside factor for production and exports for the Jul-Sep quarter.
 - Imports from ASEAN countries in July declined for the first time in two months (July: -3.3% m-o-m; June: +6.5% m-o-m) due to the decline of motor vehicle parts.
 - Imports of motor vehicle parts from ASEAN are expected to decline further from August onward, serving as a negative factor for motor vehicle production and exports.

Trends in exports by major items



Note: Seasonally adjusted by MHRT.
Source: Made by MHRT based upon Ministry of Finance, *Trade Statistics*.

Imports from ASEAN countries

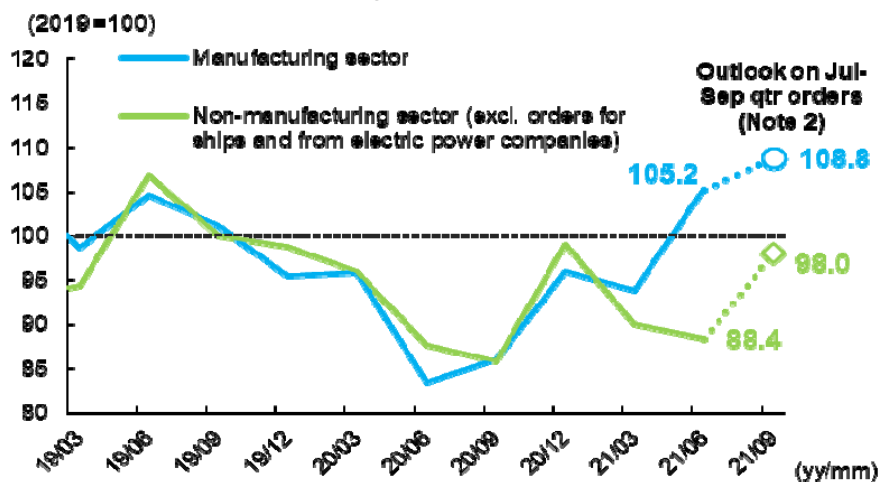


Note: Seasonally adjusted by MHRT.
Source: Made by MHRT based upon Ministry of Finance, *Trade Statistics*.

Capital investment is improving mainly in the manufacturing sector. In the second half of the fiscal year, the nonmanufacturing sector is also expected to recover

- Capital investment for the Jul-Sep quarter (on a progress basis) is expected to continue expanding, mainly in the manufacturing sector.
 - Private sector machinery orders, a leading indicator of capital investment, showed a +4.6% q-o-q increase in the Apr-Jun quarter. The manufacturing sector has shown a substantial increase.
- From the Oct-Dec quarter onward, the nonmanufacturing sector is also expected to bottom out, leading to a gradual recovery of capital investment.
 - The Cabinet Office outlook on private sector machinery orders for the Jul-Sep quarter rose a dramatic +11.0% q-o-q. The nonmanufacturing sector, whose recovery had been lagging behind, is expected to take an upturn (+16.9% q-o-q). (For reference, the Jul-Sep outlook for the manufacturing sector is +3.4% q-o-q.)
 - By type of machinery, orders for transport machinery, heavy electrical machinery, and electronic and communication equipment are expected to increase.

Private sector machinery orders

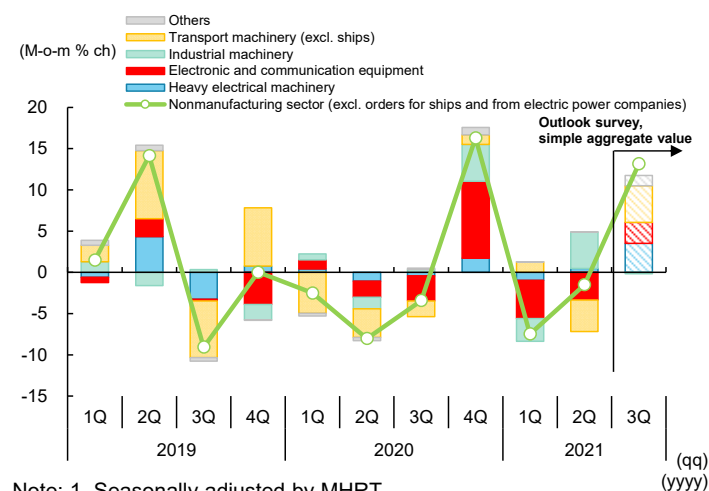


Note: 1. The Cabinet Office's outlook is calculated by multiplying the simple aggregated amount, according to respondents' outlooks for the next fiscal year, by the average achievement rate for the past three quarters.

2. Values are calculated using the achievement rate at the time of the first and second declarations (Jan-Mar 2021 quarter and Apr-Jun 2021 quarter, respectively) of states of emergency.

Source: Made by MHRT based upon Cabinet Office, *Machinery Orders*.

Nonmanufacturing sector machinery orders: Actual results and outlook by type of machinery



Note: 1. Seasonally adjusted by MHRT.

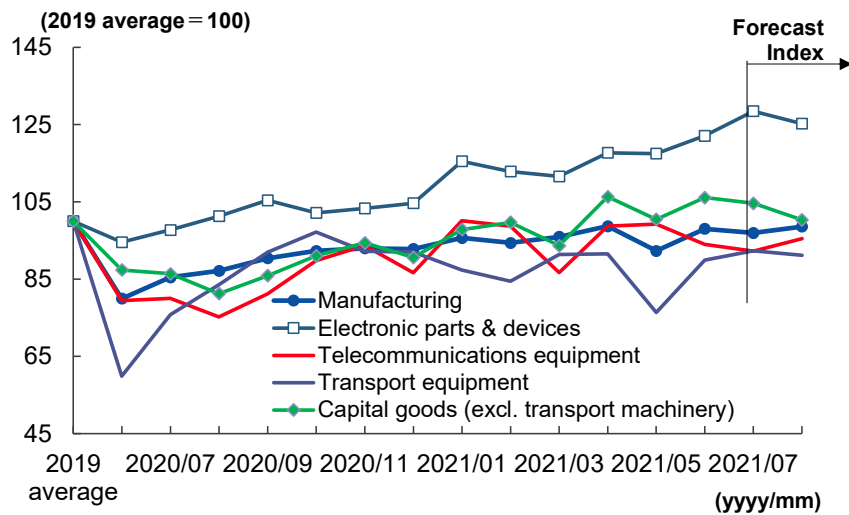
2. Nonmanufacturing (excl. order for ships and from electric power companies) and breakdown total do not match due to seasonal adjustment.

Source: Made by MHRT based upon Cabinet Office, *Machinery Orders*.

Prolonged semiconductor shortages and supply shortages due to the spread of Covid-19 infections in Asia are expected to put downward pressure on production

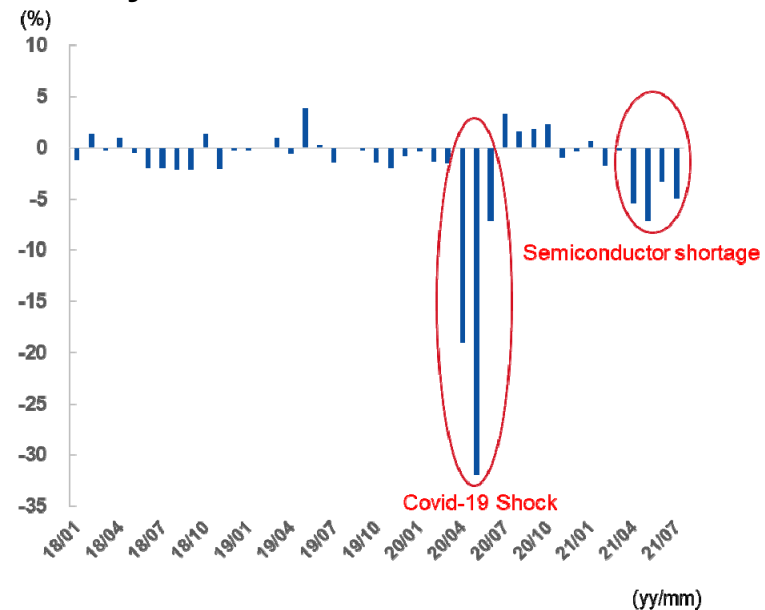
- In June, the indices of industrial production rose +6.2% m-o-m (May: -6.5% m-o-m), the first increase in two months.
 - Production of motor vehicles and capital goods increased due to a rebound from output cuts in May. The index for the Apr-Jun quarter ended at +1.0% q-o-q (Jan-Mar quarter: +2.9% q-o-q).
 - The forecast index stood at -1.1% m-o-m in July and +1.7% m-o-m in August, revealing that production projections are more or less flat when averaged out.
- Given the high possibility that motor vehicle production will decline further, industrial production for the Jul-Sep quarter may turn negative compared to the previous quarter.
 - Production of transport machinery has been lower than planned during the last four months due to semiconductor shortages. In addition to the prolonged semiconductor shortages, there is a large possibility that production in the summer will also fall short of plans due to the reduced supply of parts from Southeast Asia caused by the spread of Covid-19 infections.

Actual production / production forecast index of major industry/goods (comparison to pre-Covid-19 levels)



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

Revision rate forecasts for the transport machinery industry

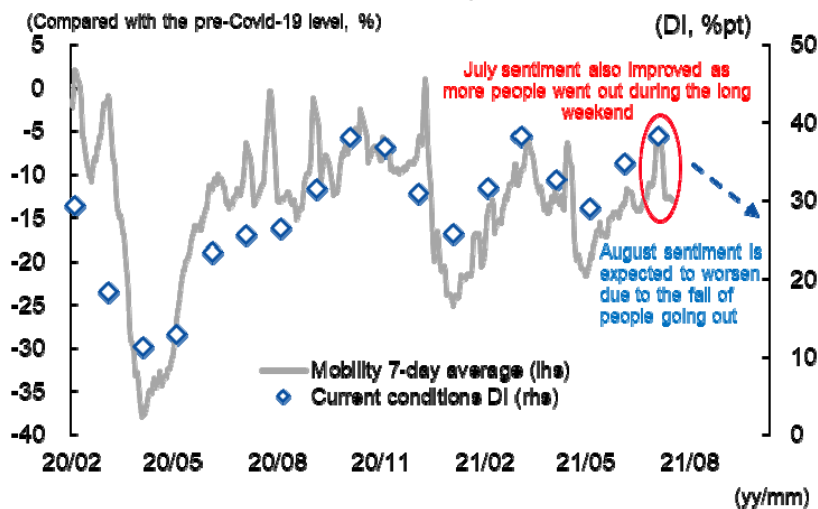


Source: Made by MHRT based upon Ministry of Economy, Trade and Industry, *Indices of Industrial Production*.

Business sentiment improved in July helped by an increase in the number of people going out during the long 4-day weekend

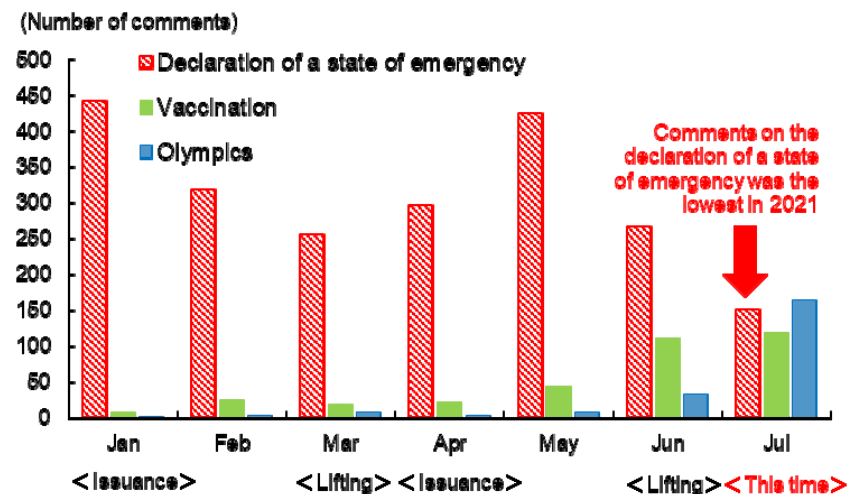
- Business sentiment in July improved despite the declaration of a state of emergency and the rapid spread of Covid-19 infections in the latter half of the month. The improvement was higher than expected.
 - The DI for current conditions (level) (June: 35.2 → July: 39.0) improved for the second consecutive month. The DI for current conditions (direction), which indicates the direction of economic conditions, also improved from the previous month, reflecting a limited decline in mobility in Tokyo during July and increased number of people in other prefectures who went out during the long 4-day weekend.
 - A tally of comments referring to the declaration of a state of emergency and the Olympics Games showed an increase in references to the Olympics. On the other hand, the number of comments referring to the declaration of a state of emergency decreased substantially compared to the previous occasions in which it was declared or lifted. This suggests that the announcement effect of emergencies may be weakening.
- Business sentiment is expected to worsen in August due to the impact of the spread of Covid-19 infections, the overwhelmed health care system, and the expansion of areas subject to the declaration.

Economy Watchers Survey: DI for current conditions and retail / mobility



Source: Made by MHRT based upon Cabinet Office, *Economy Watchers Survey* and Google LLC, *COVID-19 Community Mobility Reports*.

DI for current conditions: number of comments regarding the declaration of a state of emergency, etc.



Note: Each DI is the aggregated value of business sentiment of comments including the respective words.
Source: Made by MHRT based upon Cabinet Office, *Economy Watchers Survey*.

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

- The Bank of Japan's (BOJ) *Summary of Opinions* at the July Monetary Policy Meeting (released on July 28) included the point that there is a long way to go to achieve the price stability target of 2 percent and maintain that level in a stable manner and thus it is important not to tighten monetary policy prematurely. With regard to the fund-provisioning measure to support efforts on climate change, some participants noted that financial institutions need to disclose a certain level of information both ex ante and ex post. Based on concern that various distortions may occur in the financial system if the BOJ directly intervenes in addressing climate change, the view was also expressed that July's preliminary outline of the measure, which places the responsibility for making financing decisions on financial institutions, was appropriate.
- The BOJ is expected to continue its current monetary easing framework for the time being.
 - ETF purchases by the BOJ have been drastically reduced since the March meeting, and the monthly ETF purchases have been reduced to zero in July as was the case in May.

Summary of Opinions at the July BOJ Monetary Policy Meeting (released on July 28, excerpts)

(Conduct of Monetary Policy)

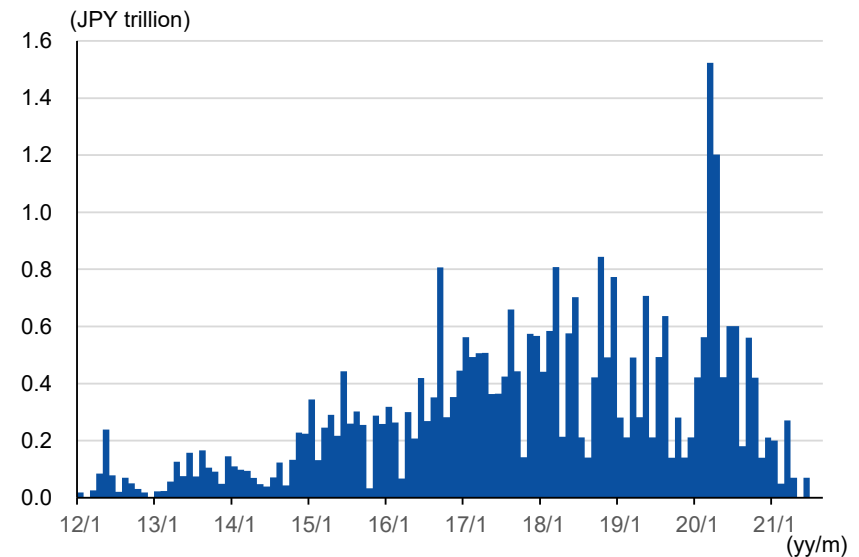
- Even though the year-on-year rate of change in the CPI excluding fresh food is likely to increase on the back of a rise in commodity prices, there is a long way to go to achieve the price stability target of 2 percent and maintain that level in a stable manner. Thus, it is important not to tighten monetary policy prematurely.

(Fund-Provisioning Measure to Support Efforts on Climate Change)

- The Bank's new fund-provisioning measure is appropriate, in that it gives consideration to market neutrality and allows for policy flexibility at the same time.
- Financial institutions need to disclose a certain level of information both ex ante and ex post from the viewpoint of policy accountability and data collection. The policy effects of the measure should be reviewed.
- If the Bank directly intervenes in addressing climate change, various distortions may occur in the financial system. This can be avoided with the new fund-provisioning measure, which will support investment or loans that financial institutions make to address climate change based on their own decisions.

Note: Underlining added by MHRT.
Source: Made by MHRT based upon the Bank of Japan.

The BOJ's monthly ETF purchases

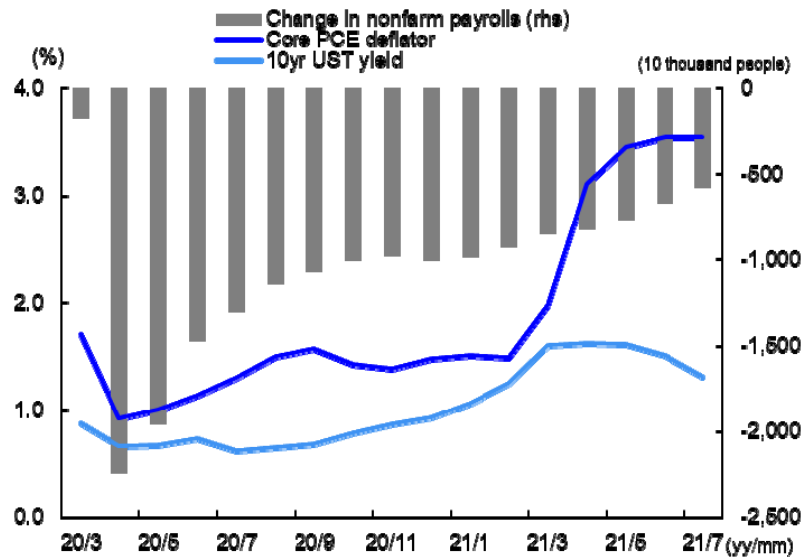


Note: Data for August 2021 is actual results for the period from Aug 1 to Aug 19, with no actual purchases as of Aug 19.
Source: Made by MHRT based upon Bank of Japan.

US bond market: the 10yr UST yield is expected to move around 1.3% to 1.5%

- The 10yr UST yield temporarily rose to the mid-1.3% range for the first time in approximately a month on the back of factors such as expectations for greater fiscal spending and the recovery in employment. However, it dropped to the 1.2% level again due to factors such as the deterioration of consumer sentiment caused by the spread of the Covid-19 Delta variant.
 - Employment data for July improved and significantly exceeded market expectations. CPI remained at a high level despite a slowdown of the rise on a m-o-m basis.
 - According to the July FOMC minutes, most participants judged that the start of tapering by the end of the year would be appropriate if the economy grows as projected.
- The 10yr UST yield is expected to rise moderately to around 1.3% to 1.5% amid economic recovery and as an interest rate hike is factored in.
 - Given the recovery of employment and higher-than-expected inflation, there is expected to be greater pricing-in of an interest rate hike, including for medium- to long-term bonds, due to the focus of attention upon the normalization of monetary policy.

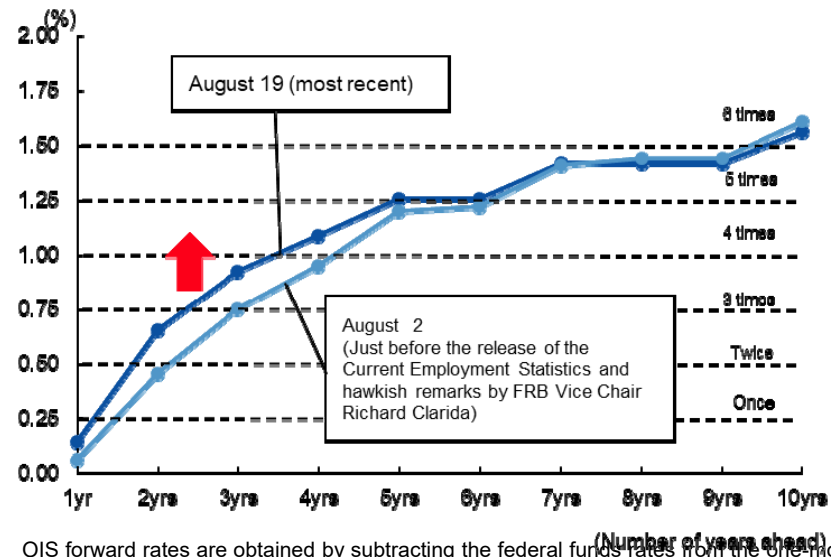
Trend of 10yr UST yield and employment / inflation



Note: Change in nonfarm payroll is the cumulative change from March 2020.
 10yr UST yield is its monthly average yield.

Source: Made by MHRT based upon Bloomberg.

Factoring in rate hikes by OIS forward rates



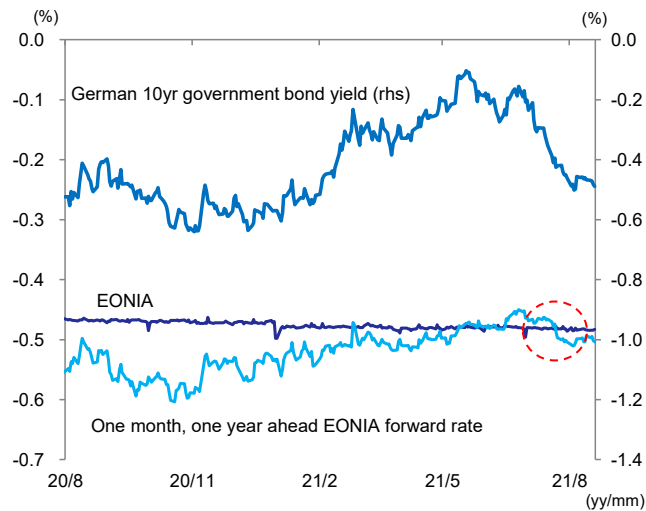
Note: OIS forward rates are obtained by subtracting the federal funds rates from the one-month ahead OIS forward rates for a particular number of years ahead. The rise in rates per one rate hike is assumed to be 0.25 percentage points.

Source: Made by MHRT based upon Bloomberg.

Eurozone bond market: German 10yr government bond yield expected to move around -0.5% to -0.3%

- The German 10yr government bond yield temporarily fell to the -0.5% level, reflecting the spread of Covid-19 variants and concerns regarding a slowdown in the pace of economic recovery.
 - At the ECB's Governing Council meeting on July 22, the ECB changed its forward guidance. Due in part to negative comments by a senior ECB official regarding the tapering of asset purchases at the September Governing Council meeting, along with other factors, speculation on the prolongation of monetary easing led to a further fall of interest rates as the market factored in interest rate cuts.
- German 10-year government bond yields are expected to rise along with the recovery of economic conditions and the rise of US interest rates, trending around -0.5% to -0.3%.
 - According to the ECB's Eurozone HICP projection (as of June), one of the forward guidance conditions, which was inflation reaching 2% by the midpoint of the projection horizon (2022), has not been achieved. Given prospects that it will take some time before an interest rate hike, the odds are high that the rise of interest rates will be moderate.

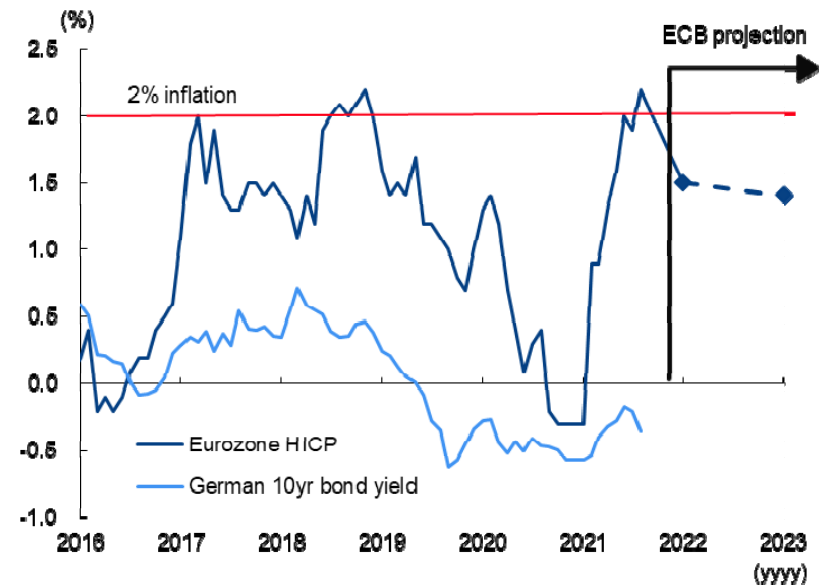
German 10yr government bond yield and factoring in rate cuts



Note: The EONIA forward rate is the floating rate for interest rate swap transactions and refers to the EONIA, which is the short-term interest rate that the ECB is referencing. If the EONIA forward rate is lower than the EONIA, it can be seen as an indication that expectations for future rate cuts are becoming higher.

Source: Made by MHRT based upon Bloomberg.

German 10yr government bond yield and Eurozone core prices

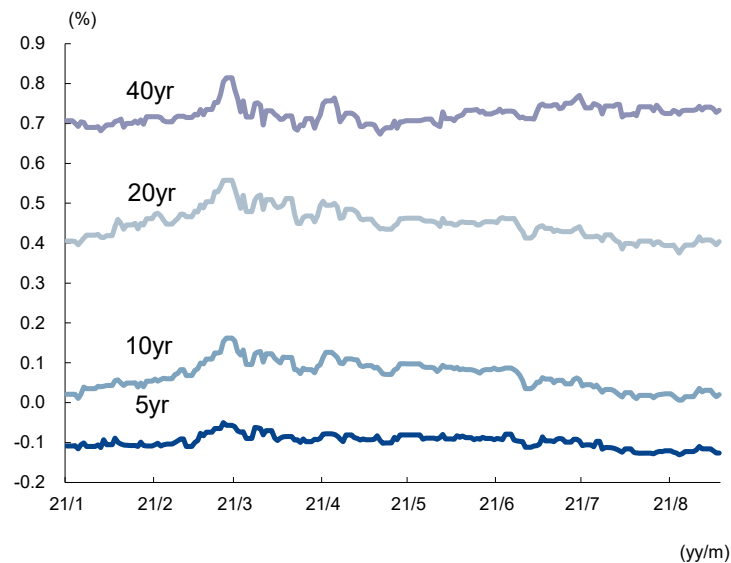


Note: The German 10yr government bond yield is its monthly average. Source: Made by MHRT based upon ECB and Bloomberg.

Japanese bond market: the 10yr JGB yield is projected to rise modestly to the mid-0.0% range

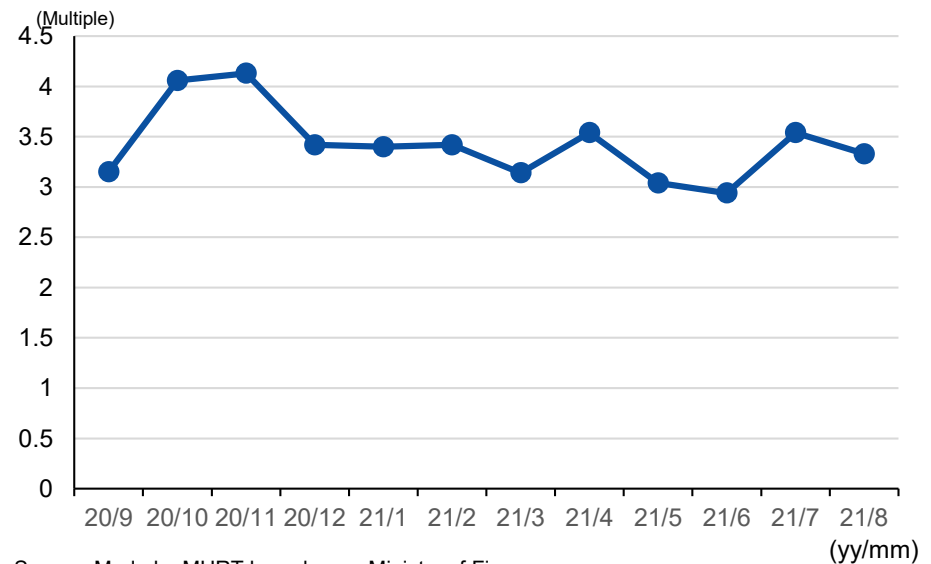
- The 10yr JGB yield rose momentarily to the highest level in approximately a month, reflecting the rise of US interest rates. However, it subsequently fell to the lower half of the 0.0% level, reflecting the downturn in US interest rates, the spread of Covid-19 infections in Japan, and concerns about an economic slowdown in China.
 - While the bid-to-cover ratio for 10yr JGBs (Aug 3) fell slightly from the previous auction to 3.33x, the results turned out to be benign.
- Amid a gradual rise in US long-term interest rates, the 10yr JGB yield is expected to rise slightly to the mid-0.0% range.
 - We do not expect the release of information that might affect financial markets at the Jackson Hole meeting in August. On the other hand, the market will likely continue to factor in speculation on a US interest rate hike on the basis of factors such as the recovery of employment and rise of inflation in the US, leading to a gradual rise of US interest rates, thus serving as upward pressure on Japan's long-term interest rates.

Trend in JGB yields



Source: Made by MHRT based upon Bloomberg.

Bid-to-cover ratio of 10yr JGBs

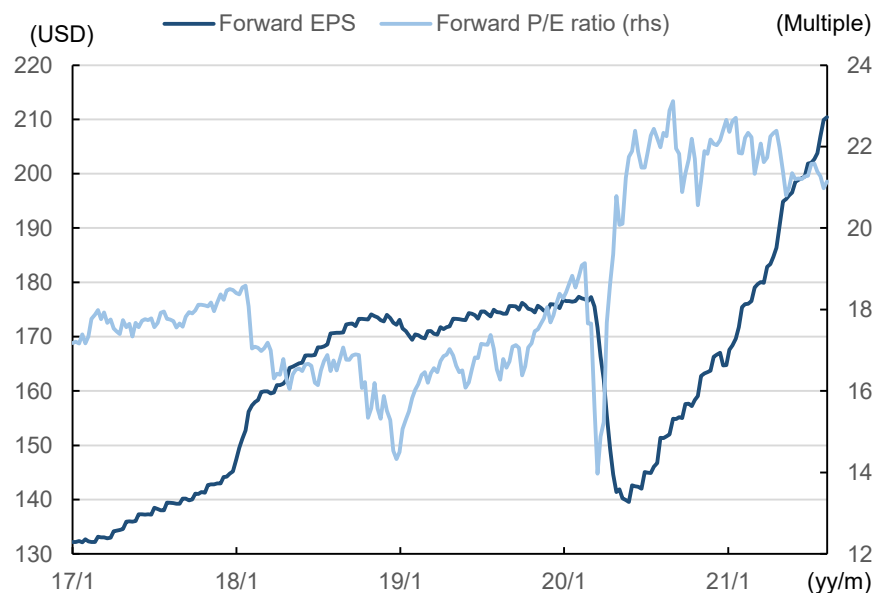


Source: Made by MHRT based upon Ministry of Finance.

US stock market: should trend on firm ground due to expansion of corporate earnings

- The US stock market continued to follow firm footing on the back of robust second quarter earnings, with the Dow Jones Average reaching a historical high on August 16. However, the market subsequently softened due to concerns regarding a slowdown in the pace of economic recovery.
- The forward EPS continued to expand buoyed by favorable earnings announcements.
 - On the other hand, the P/E ratio is slightly overvalued at 21.1x due to firm stock market trends.
- Nearing the end of corporate Q2 earnings announcements, 87% of the S&P 500 Index companies posted better-than-expected results. Despite a lingering sense of overvaluation, the market is expected to remain firm, given the rise of confidence in future corporate earnings.

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



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

S&P 500 companies' 2021 Q2 corporate earnings announcements

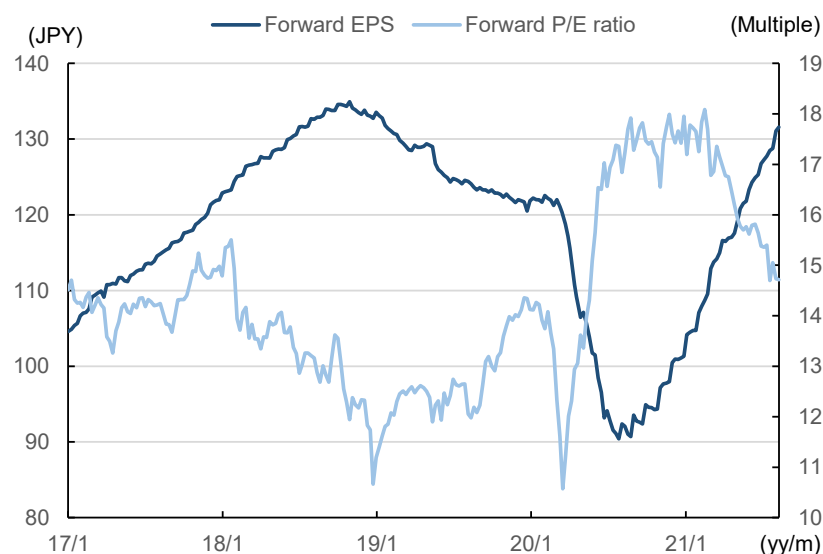
	Higher than expected	No surprise	Lower than expected	Progress rate (%)	No. of companies which have reported earnings
Energy	82%	0%	18%	100.0	22 / 22
Materials	75%	4%	21%	100.0	28 / 28
Capital goods	85%	6%	10%	97.3	72 / 74
General consumer goods	86%	0%	14%	88.9	56 / 63
Consumer staples	85%	4%	11%	84.4	27 / 32
Healthcare	92%	3%	5%	95.3	61 / 64
Finance	95%	2%	3%	100.0	64 / 64
Information technologies	94%	3%	3%	90.5	67 / 74
Communication services	92%	4%	4%	100.0	26 / 26
Public services	71%	7%	21%	100.0	28 / 28
Real estate	83%	3%	14%	100.0	29 / 29
S&P500	87%	3%	10%	95.2	480

Source: Made by MHRT based upon Refinitiv.

Japanese stock market: although the spread of Covid-19 infections serves as a drag, a gradual rise is expected going forward

- Even though the Nikkei Stock Average rose at times on the back of strong first quarter corporate earnings, it has softened recently due to the state of Covid-19 infections in Japan, fall of overseas stock markets, and reports of motor vehicle output cuts due to shortages of parts.
- The 12-month forward EPS exceeded its pre-Covid-19 level (end of 2019). It is also close to its highest level in the last five years.
 - On the other hand, the forward P/E ratio dropped to 14.7x amid the spread of Covid-19 infections.
- Japanese corporations have reported strong results for the first quarter of FY2021. Net income rose 22% from the first quarter of FY2019 (prior to the Covid-19 pandemic). Given the maintenance of solid corporate earnings among Japanese corporations, we expect a gradual rise of the Japanese stock market.

TOPIX forward EPS and forward P/E ratio



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

Overview of Japanese corporations' FY2021 Q1 earnings announcements

	Net income growth rate compared to FY2019 1Q earnings	Percentage of companies that exceeded FY2019 1Q earnings	Percentage of companies falling below FY2019 1Q earnings	No. of companies included in tally
Energy	175%	60%	40%	15
Communication services	-9%	62%	38%	55
Healthcare	53%	63%	37%	68
General consumer goods	46%	56%	44%	253
Finance	15%	73%	27%	135
Public services	-73%	30%	70%	20
Capital goods	17%	62%	38%	430
Information technologies	135%	78%	22%	204
Consumer staples	29%	63%	37%	94
Materials	103%	78%	22%	170
Real estate	-5%	52%	48%	27
Overall	22%	65%	35%	1,471

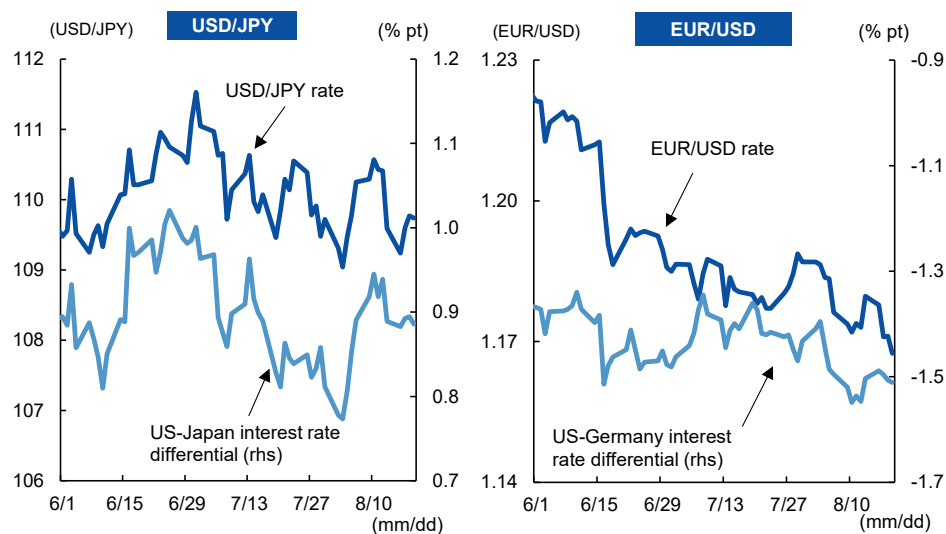
Note: The tallied companies are those companies that are listed on the First Section of the Tokyo Stock Exchange with a fiscal year ending March 31 and for which data was available for the first quarter of 2019 and 2021. Industry classification is based on the Global Industry Classification Standard. Data is as of August 19.

Source: Made by MHRT based upon Refinitiv.

Forex market: dollar-buying expected to prevail against the backdrop of US economic recovery

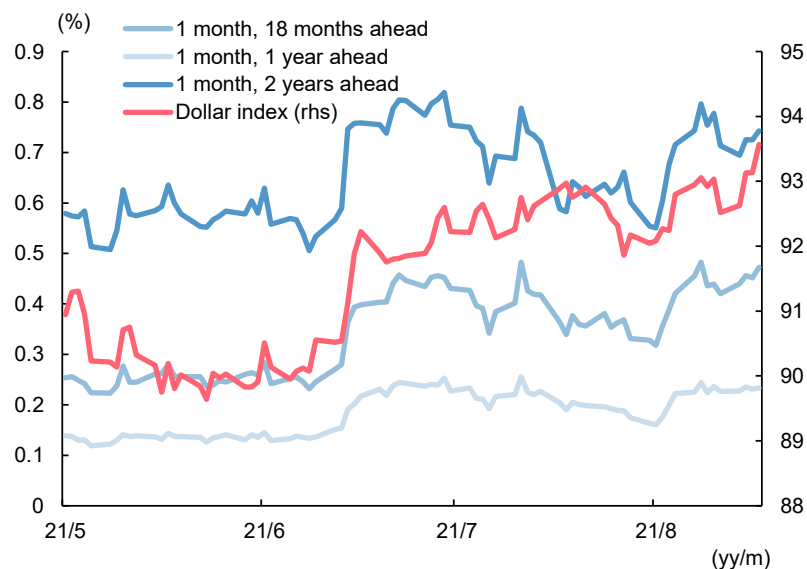
- Given comments by FRB officials and the results of US and Chinese economic indicators, the dollar has more or less leveled off against the yen and the dollar has strengthened against the euro since mid-July.
 - US interest rates rose and the dollar strengthened against the backdrop of favorable US employment data for July (Aug 6) and hawkish comments by FRB Vice Chair Richard H. Clarida.
 - However, the dollar trimmed its gains against the yen following a weaker University of Michigan Consumer Confidence Index (Aug 13) in the US in August. On the other hand, the dollar held firm against the euro due to the revision of the ECB forward guidance and the deterioration of Chinese economic indicators that have a significant impact on the European economy.
- Since the June FOMC meeting, the dollar index rose along with short-term expectations for a rate hike. The dollar is also following an upward trend, due to the rise of speculation on an earlier-than-expected tightening, stemming from favorable US employment data and comments by the FRB. Looking forward, we expect strong dollar-buying due to the focus of attention on an interest rate hike along with the recovery of the US economy.

USD/JPY, EUR/USD rates and interest rate differentials



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

Trend of OIS forward rates and the dollar index

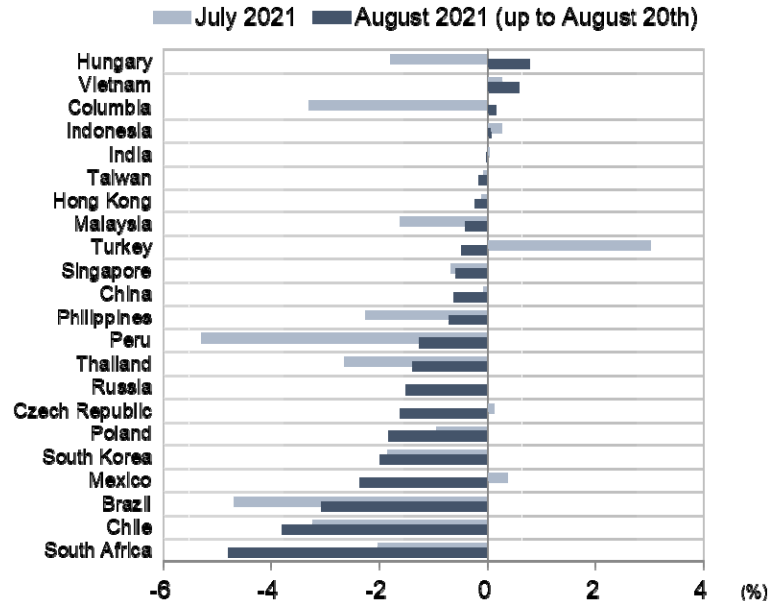


Source: Made by MHRT based upon Bloomberg.

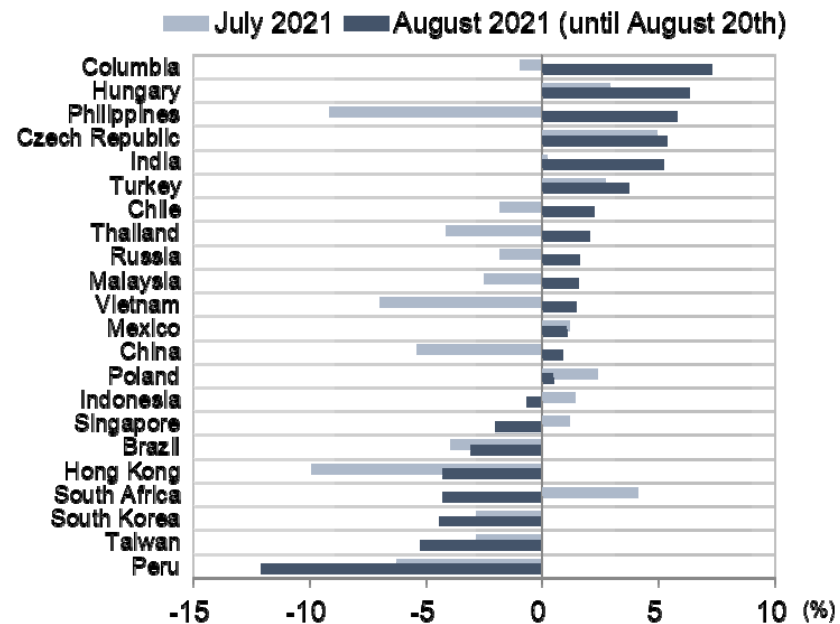
EM financial markets: EM currencies are generally weak

- Given speculation on US tapering by the end of the year and employment recovery, the forex market is generally bullish regarding the dollar and bearish with respect to EM currencies.
 - EM currencies have been weakening even in Latin America where countries have shifted to raising interest rates. In August, interest rate hikes were implemented in Brazil (for the fourth consecutive meeting), Mexico (for the second consecutive meeting), and Peru, but failed to halt the weakening of their currencies. The sharp fall of iron ore prices and the weak copper market also had an impact in Brazil and Chile, respectively.
- Political factors also served as factors behind the weakness of the currencies in South Africa, Brazil, and Peru.
 - In South Africa, the political unrest involving the former president served as an ongoing factor. In Latin America, there are concerns about Brazil's fiscal deterioration ahead of the presidential election next year. In Peru, its currency hit its lowest mark, and stock prices fell due to investors' concerns regarding leftist policies by the new president.

Rise and fall of EM currencies against the US dollar



Rise and fall of EM stocks



Source: Made by MHRT based upon Refinitiv.

Source: Made by MHRT based upon Refinitiv.

Outlook on the financial markets

		August 20, 2021	Jul-Sep	Oct-Dec	Jan-Mar
Japan	Interest rate on Policy-Rate balances (End-of-quarter, %)	-0.10	-0.10	-0.10	-0.10
	Newly-issued JGBs (10yr, %)	0.01	0.00 to 0.10	0.05 to 0.15	0.05 to 0.15
	Nikkei Stock Average (JPY)	27,013	28,500 to 29,500	29,500 to 30,500	30,000 to 31,000
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, %)	1.26	1.40 to 1.60	1.60 to 1.80	1.60 to 1.80
	Dow Jones Average (USD)	35,120	34,100 to 35,100	34,500 to 35,500	34,500 to 35,500
Eurozone	ECB deposit facility rate (End-of-quarter, %)	-0.50	-0.50	-0.50	-0.50
	Long-term government bond (Germany, 10yr, %)	-0.50	-0.35 to -0.15	-0.30 to -0.10	-0.30 to -0.10
Forex	USD/JPY rate (USD/JPY)	109.78	109 to 111	110 to 112	110 to 112
	EUR/USD rate (EUR/USD)	1.170	1.17 to 1.19	1.16 to 1.18	1.15 to 1.17

Note: 1. The foreign exchange rates (actual) are NY closing rates.
 2. The projected policy interest rate indicated for the Jul-Sep, Oct-Dec, and Jan-Mar 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 upon Bloomberg.

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