
Mizuho Economic Outlook & Analysis

February 28, 2022

Slowdown in the Chinese economy and its impact on the world

Sluggish property investment will dampen Japan's growth rate

< Summary >

- ◆ Unfavorable headwinds buffeting China's economy (sluggish property investment and personal consumption) since the latter half of the previous year continue to blow this year. Although downward pressure is expected to gradually ease toward 2023, the risk scenario of a resurgent COVID-19 pandemic driven by new variants and other factors persists.
- ◆ The slowdown in real estate investment in China will negatively affect the global economy through reduced exports to various countries/regions, even though investment in the manufacturing sector and infrastructure will temper the downward pressure. Japan's GDP in 2022 is anticipated to fall by 0.2% from the baseline.
- ◆ If the risk scenario of closing China's major ports and suspending exports materializes, the economies of Taiwan, South Korea, and Russia will be hit particularly hard. Japan will also feel the blow centering on its machinery, chemical and metal industries.

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1. “Property” and “Zero COVID” will continue to be keywords in 2022

The Chinese economy in 2021 achieved a strong real GDP growth rate of +8.1% year-on-year, rebounding from the previous year’s downturn. However, if we recalculate the growth rate from 2019 (annualized basis) taking into account the previous year, the GDP growth rate is actually +5.1%, a rather disappointing figure compared with the 6% plus growth rates recorded up until 2019 (**Chart 1**). The reason behind this drop is the slowdown in China’s economy in the latter half of the year. Sluggish property investment on the back of lending regulations imposed on property developers, subdued personal consumption due to sporadic resurgence of COVID-19 infections, and electricity supply issues, among other factors, stood in the way of China’s economy in the latter half of 2021.¹ In particular, “property” and the government’s “Zero COVID” policy are two issues China continues to confront, and concerns over these two problems have not receded, making them important factors when analyzing the Chinese economy from a short-term perspective. In this report, we will study the outlook of the Chinese economy by examining these two factors.

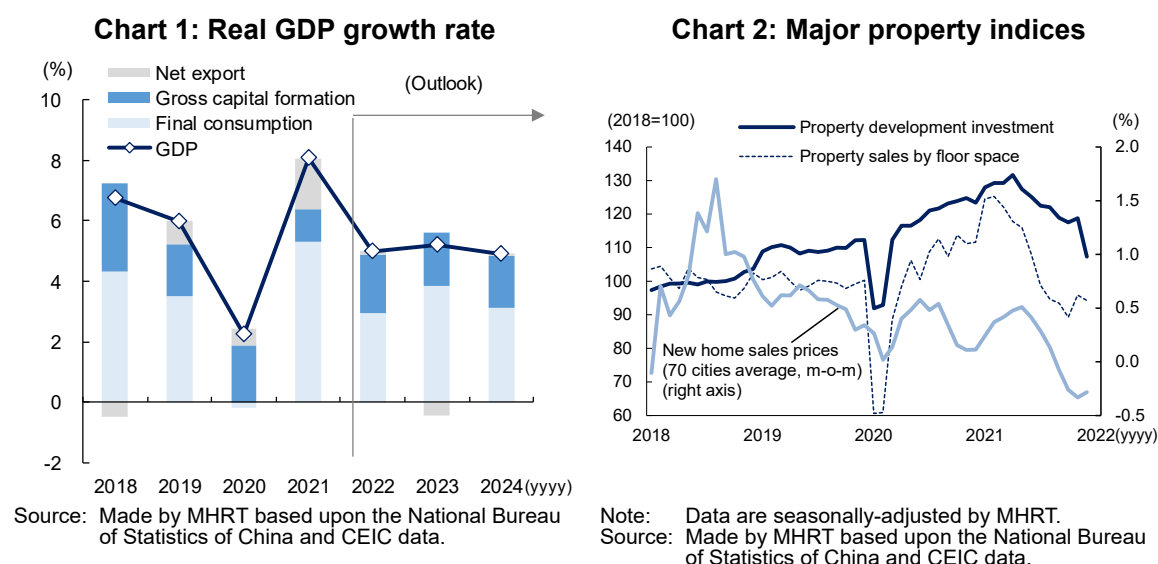
(1) Downward trend of property development investment remains unchanged

Looking at the first keyword “property,” last year’s lending restrictions on property developers continue to exert pressure, and the downward trend of investment is expected to remain unchanged through the first half of 2022. The lending restrictions were fully implemented at the beginning of 2021 with a view to reining in overheated property speculation in China. However, the restrictions invited a greater tightening of the commercial banks’ lending activity than initially anticipated by the Chinese government, and hence the government has already begun to make slight adjustments to the policy in order to fulfill the funding requirements of actual demand.² Furthermore, the government seems to be moving toward restimulating property development, which had cooled excessively, by establishing a fundraising framework for strong performing real estate developers to acquire real estate projects owned by non-performing property developers, and by excluding loans to fund the construction of affordable housing for low- to middle-income earners from the lending restriction guidelines. For this reason, some leading indicators of property development investment, including property sales by floor space, are now showing signs of bottoming out, and the downturn in real estate prices is also beginning to change. We forecast that real estate investment will stop declining by mid-

¹ For details of China’s economic slowdown in the latter half of 2021, refer to Hideki Ito, “Outlook of the Decelerating Chinese Economy” (Mizuho Insight, October 28, 2021).

² In a press conference the People’s Bank of China stated it had requested commercial banks to continue offering stable and orderly credit to the property sector (October 15, 2021).

2022 (**Chart 2**). Even after 2023, we expect property investment to continue expanding mildly supported by demand in urban areas, so we assume that China can avoid the situation of a “stall” in property investment. But with no change in the government’s basic stance to crack down on property speculation, it is not realistic to expect a strong year-on-year growth rate of around +10% as seen in the past.³



Meanwhile, looking at overall investment activity, we hold that downward pressure on the economy stemming from the slow real estate sector will be alleviated somewhat by infrastructure and manufacturing investments. With nominal growth of infrastructure investment in 2021 dull at only +0.2% over the previous year (growth rate from 2019 [annualized basis] was +1.8%), we can expect a rebound this year. The slow pace of infrastructure investment was due to the delay in issuing local government special bonds (hereinafter “special bonds”) that serve as a source of infrastructure investment,⁴ and although fund raising activity advanced in the October to December period of 2021 (**Chart 3**), it failed to contribute to investment growth. In the light of this experience, early issuance of new special bonds has been promoted⁵ in 2022, and we believe the carryover of last year’s bonds will positively contribute to this year’s investment (**Chart 4**). Likewise, in terms of manufacturing investment, growth in corporate earnings (that serve as a source of investment) jumped +34.3% in 2021 from the preceding year (+18.2% from 2019 [annualized basis]), marking a surprisingly high growth rate. Since China aims to become

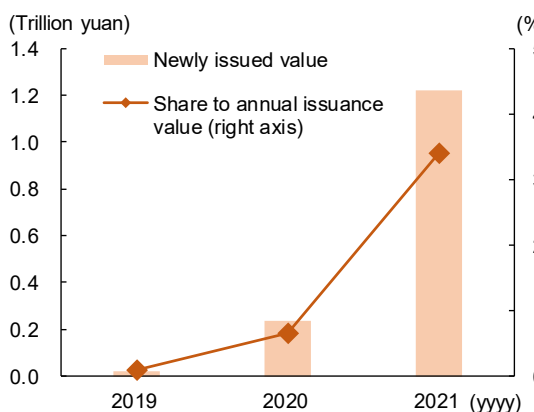
³ The nominal annual average growth rate of property development investment from 2017 to 2019 was +8.8%.

⁴ The delay was due to the absence of a deadline to issue local special government bonds unlike in usual years, and the tightening of the screening process for regional infrastructure projects by the central government.

⁵ Press conference by the Ministry of Finance of the People’s Republic of China (December 16, 2021).

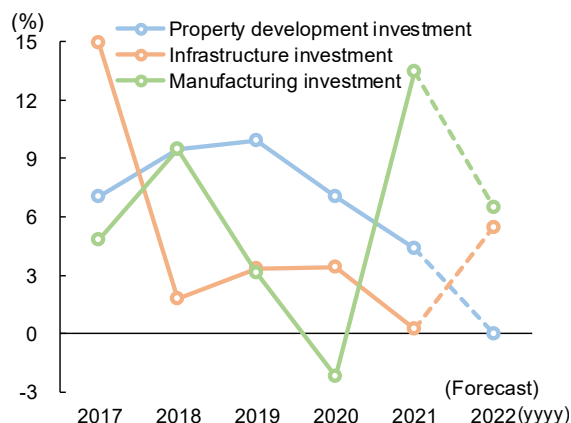
a world manufacturing power and offers various policy supports such as tax reductions centered on the high-tech sector, we expect investment activity in the manufacturing sector to retain its robustness in 2022 (**Chart 4**).

Chart 3: New issuance of special bonds in the October to December period



Source: Made by MHRT based upon China's Ministry of Finance and wind.

Chart 4: Capital investment by sector



Note: Data represent nominal changes from the previous year. Infrastructure investment is the total of the transportation, environment and electricity sectors.

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

(2) Full relaxation of the “Zero COVID” policy will be after 2023

The second factor weighing down the economy is the government’s “Zero COVID” policy. Sluggish personal consumption caused by the pandemic as well as a strict containment policy is thought to continue through 2022. While the Chinese government shows confidence in containing the spread of infection, emergence of the highly contagious Omicron variant is expected to increase the frequency of sporadic lockdowns and negatively impact personal consumption mainly related to the service sector. We project that the Chinese government will maintain its “Zero COVID” policy until the rollout of an mRNA vaccine, which is considered more effective against highly infectious COVID-19 variants. The point of focus is the timing of vaccine rollout; in view of the nation’s strong preference to administer domestically-produced vaccines,⁶ full launch of a domestically-produced mRNA vaccine is expected after early 2023 with the vaccine currently in the clinical trial stage.⁷ Personal consumption is expected to head toward full recovery later on, along with a gradual relaxation of the “Zero COVID” policy. In addition

⁶ According to CNN in the United States, China’s health ministry had considered using foreign mRNA vaccines until July 2021, but it still has not approved their use: “China was ready to approve Western mRNA vaccines months ago. Why is it still holding off?” (December 13, 2021).

⁷ Reuters, “Finding China’s Moderna is a financial long shot” (January 6, 2022).

to the mRNA vaccine, therapeutic medicines are also under development in China, and a part of the neutralizing antibodies (therapeutic antibody cocktail offered to high-risk patients) was granted emergency authorization in December last year. In February this year, China approved the import of a foreign (Pfizer's) oral medicine for the first time. These therapeutic medicines are aimed at preventing severe symptoms of the illness and not the infection itself, and their efficacy still requires verification. As such, we cannot easily conclude that they will impact the "Zero COVID" policy, but they may trigger a partial revision of the policy depending on the degree of penetration.

In view of the two factors of "property" and "Zero COVID" that continue to exert negative pressure on investment and the staged relaxation of the government's containment policy, we forecast China's real GDP growth rate in 2022 and 2023 to be +5.0% and +5.2%, respectively.

(3) China advocates stability-oriented economic policies, but risks persist that cannot be ignored

The Central Economic Work Conference held in December last year decided on "stability" as the first priority of its economic policy this year.⁸ For this reason, if concerns heighten over the possibility of economic recession, the government will try to minimize the adverse impact on the economy by implementing fiscal and monetary policies in a timely manner.

Nonetheless, the situation surrounding the coronavirus remains highly unpredictable even in China, which had succeeded in containing the spread of infection through its "Zero COVID" policy, due to the presence of many uncertain elements, including the emergence of new variants. As mentioned earlier, use of the highly effective mRNA vaccine to prevent infection is not widespread in China, and the real risk of resurgent nationwide infections overwhelming the "Zero COVID" policy remains. Should this actually occur, widespread lockdowns will become inevitable, bringing about a significant slowdown in the nation's economy. When the relatively infectious Delta variant prevailed last summer, the virus was not confined to the originating cities, including Nanjing, but quickly spread across the nation, which resulted in restrictions on domestic movement and a temporary curtailment in private sector consumption activity.

Also, a resurgent pandemic in China may cast a dark shadow over the global economy through supply chain disruptions. In particular, container volume in China accounts for more than one-third of the world's total, and should the risk scenario of major port closures

⁸ For details of the Central Economic Work Conference, refer to Naoki Tsukioka, "China's Economic Policy in 2022" (Mizuho Insight, December 27, 2021).

materialize, the adverse impact on the world will be unavoidable. In May 2021, some ports in Shenzhen temporarily suspended the handling of export containers due to an outbreak of infection among port workers, reducing the operation rate to around 30% of ordinary times. It goes without saying that such events resulted in the government beefing up its pandemic control measures, hence reducing the possibility of full-scale closure of its major ports. Nonetheless, we should bear in mind the existence of such risk factors in view of their potential impact on the global economy.

2. China's two negative factors (property/Zero COVID) will impact the global economy

The economic downturn in China caused by controlled real estate investment and the government's "Zero COVID" policy gives rise to concerns over the negative economic impact on Japan and other countries. In this section, we examine the potential impact on global economies, including Japan's, by quantitatively using the international input-output table.

(1) Deceleration of China's property investment negatively impacts other countries' economies

We begin by confirming how the change in investment trend in China may impact the economies of Japan and other countries/regions. As described in the previous section, while China's economy in 2022 will suffer downward pressure from subdued property investment, the economy will be partially buoyed by investment in its manufacturing (especially high-tech sector) and infrastructure segments, though not enough to prevent a slowdown in the overall economy. Based on this assumption, in this section we estimate the potential impact on Japan and other countries/regions of three events: (1) slowdown in property investment in China, (2) acceleration of capital investment by manufacturers (high-tech investment), and (3) acceleration of infrastructure investment. More specifically, we define a path where these three cases will not occur in 2022 as a baseline and estimated the impact of the slowdown in property investment and the acceleration of manufacturing and infrastructure investments using an international input-output table.

China's property investment growth rate is forecast to decline by -5.7%Pt in 2022 compared to the baseline,⁹ and this will negatively affect the Japanese economy through reduced exports and other factors. Items such as plastics, basic material articles including steel, and construction machinery, demand for which is susceptible to real estate

⁹ The main purpose of this report was to analyze the additional impact of controlled property investment in 2022, so we estimated the impact by setting China's annual growth rate of property investment, manufacturing investment, and infrastructure investment in 2021 from 2019 as a baseline (property investment +5.7%, manufacturing investment +5.4%, and infrastructure investment +1.8%).

development investment, account for around 15% of Japan’s exports bound for China (**Chart 5**). A decline in such exports will most likely weaken the Japanese economy. On the other hand, the growth rate of (2) acceleration of capital investment by manufacturers (high-tech investment) is estimated to expand by +1.1%Pt from the baseline in 2022, and the increase in capital goods exports, including semiconductor manufacturing equipment and metal processing machinery (machine tools), works positively for Japan’s economy. Furthermore, the growth rate of (3) acceleration of infrastructure investment is estimated to reach +3.7%Pt from the 2022 baseline, boosting Japan’s exports of construction materials and construction machinery to China, generating a positive impact on the Japanese economy in contrast to the slowdown in property investment.

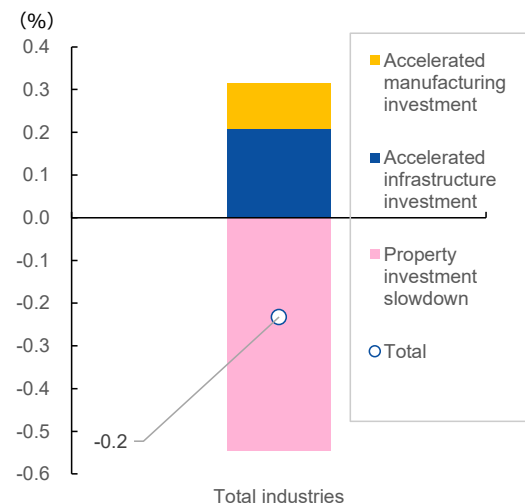
If we evaluate our estimate results in net terms, the degree of negative impact of restrained property development investment exceeds the positive impact generated by the increase in manufacturing and infrastructure investments, thereby pushing down Japan’s GDP in 2022 by approximately -0.2%Pt compared with the baseline (**Chart 6**).

Chart 5: Export items bound for China that may be affected by the investment trend of manufacturing/property/infrastructure in China

Manufacturing investment		Property/infrastructure	
Item	Share (%)	Item	Share (%)
Semiconductor machinery, etc.	6.1	Plastic materials	5.6
Metalworking machinery	1.6	Iron and steel products	3.4
Pump and centrifuges	1.8	Nonferrous metals	2.6
Mechanical handling equipment	0.7	Metal products	1.8
Industrial robots	0.3	Non-metal mineral materials	1.2
		Rubber products	0.5
		Construction machines	0.2
Total	10.5	Total	15.3

Note: Data in the table represent the share in the total export value to China as of 2019.
Source: Made by MHRI based upon the Ministry of Finance, *Trade Statistics of Japan*.

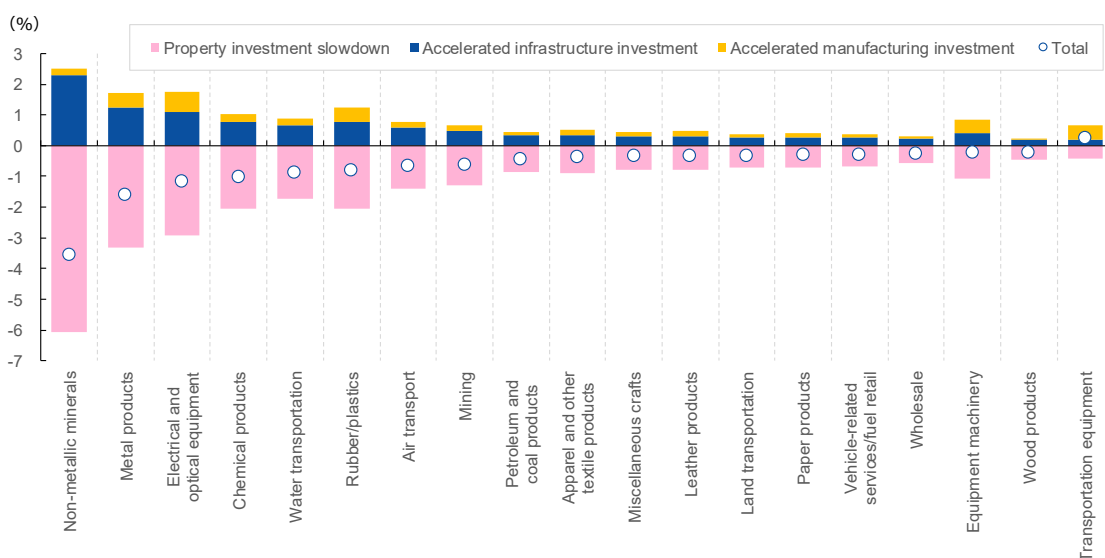
Chart 6: Impact of the investment slowdown in China on Japan’s economy



Note: The graph shows the impact on the real GDP growth rate based on the 2019 input-output table. We set the annual average growth rate of property/manufacturing/infrastructure investments in 2021 from 2019 as a baseline and estimated the impact of the slowdown in property investment and the acceleration of manufacturing/infrastructure investments.
Source: Made by MHRT based upon ADB.

We also depicted the impact on value added by industry¹⁰ in **Chart 7**. We can confirm that the decline in construction material demand driven by weakened property investment can have a significant impact on the basic materials industry centering on non-metal mineral materials and metal products. As Sakai et al. (2021) points out, the basic materials industry is characterized by a high proportion of raw materials in intermediate input, and commodity price hikes since last year place a heavier downward pressure than on other industries. In addition to the downward pressure on earnings driven by surging commodity prices, the deceleration of property investment in China is projected to worsen the business performance of the basic materials industry even further. Meanwhile, in the equipment machinery industry, the positive impact of accelerated manufacturing investment is expected to be large, thereby offsetting the negative impact in net terms.

Chart 7: Impact of China's slowdown/accelerated investment on the Japanese economy (by industry)



Note: The estimation method is the same as in **Chart 6**. Industry classification is taken from an input-output table.
Source: Made by MHRT based upon ADB.

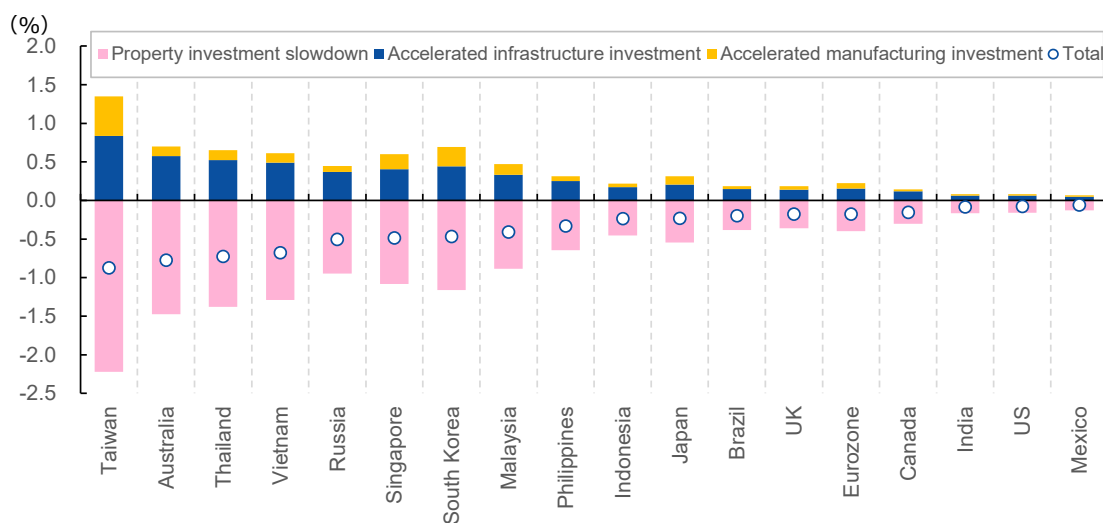
If we look at the situation by major country/region, the impact of the slowdown in property investment exceeds the push-up effect of accelerated manufacturing and infrastructure investments (**Chart 8**). In particular, the impact is greater in Taiwan, Australia, and ASEAN countries. In Taiwan, Thailand, and Vietnam, the share of plastics, metal products, chemical products, and so forth is relatively high among export items to China. In Australia, mineral resources such as iron ore occupy more than 60% of its exports

¹⁰ We calculated the impact on value added by multiplying a certain ratio (value added ratio) by the impact on production value. It should be noted that we can substitute the phrase with impact on production value for the purpose of interpreting the estimation results.

to China. We hold that countries and regions with a large share of construction material exports are exposed to downward pressure on their economies.

As mentioned earlier, since the Chinese government will basically maintain its policy of cracking down on property speculation, we cannot expect the same high economic growth experienced in past years even as investment activity picks up after 2023. Therefore, we expect the basic scenario where the deceleration of property investment tamping down the economies of various countries/regions will remain unchanged after 2023.

Chart 8: Impact of China’s slowdown/accelerated investment on the major countries/regions’ economies (by industry)



Note: The estimation method is the same as in **Chart 6**.
Source: Made by MHRT based upon ADB.

(2) Risk case: Watch out for supply chain disruptions due to the spread of port infections

Another potential risk in addition to the above factor also requires close attention. As explained in the previous section, the Chinese government will most likely maintain its “Zero COVID” policy this year. Under these circumstances, should a highly infectious variant spread in China’s major ports, exports from China may be suspended due to port closures. With many industries around the world depending on China for parts procurement, this will be a huge blow to the global economy. In this section, we quantitatively estimate the risk scenario where suspended Chinese exports impact the world and Japan’s economy.

We first examine China’s container volume by port. As presented in **Chart 9**, container volume in mainland China is concentrated in specific ports, and the top five ports of Shanghai, Ningbo, Shenzhen, Guangzhou, and Qingdao account for around 60% of the total volume. The closure of these five ports will halt most of China’s exports to the world. As we believe that it is unlikely that all five ports will be closed at the same time, in this

report we define the risk case as a scenario where each port is closed for one month at a time.

We estimate that the loss of China's export value to the world will amount to approximately \$140 billion, or roughly 5% of the total annual export value.¹¹ In examining the impact on each country, we add some underlying assumptions: (1) For items subject to export suspension, we assume that all export items will be slashed by 5%, since we believe the five major ports widely cover China's export items. (2) We assume that import countries will face difficulties in finding substitutes for suspended export items. In the case where import suspensions occur within a short period, like we presumed this time, we feel it is unlikely that import companies will be able to quickly restructure their production lines and revise the input ratio of certain parts and substitute the parts imported from China with other items. Moreover, since suspension of procurement from China occurs globally, we believe it will not be possible to procure missing parts additionally from other nations. In sum, import raw materials from China will create a bottleneck for production activities in other countries. (3) The final assumption simplifies our process by surmising no impact of price fluctuations for parts temporarily unavailable.

Chart 10 depicts the results of our estimate of the impact on major countries under the above assumptions. The darker the red color, the greater the impact, and we can see that the basic materials industry is particularly affected. As China holds a large share in the raw material products market, including chemical products, industries operating within the basic materials industry are vulnerable to the situation in China. The figures in the very right column show the impact on each economy's GDP, and we can confirm that the top three affected economies are Taiwan, South Korea, and Russia. Located adjacent to China, their dependence on China is relatively high. Especially for Taiwan where electronics is a core industry accounting for a little less than 20% of the overall economy, since it more or less depends on China for electrical equipment parts, the impact of China is by far the greatest among the other economies. The top three economies are followed by Vietnam, the Philippines, and Indonesia. Since processing and manufacturing industries are the center of these three countries' economies, the relatively heavy weight of raw materials in intermediate input explains their high position in the ranking.

The impact on Japan's GDP is estimated to be approximately -0.2%. Although the impact is smaller compared with other countries, Japan cannot afford to ignore even such a minimal impact considering that its GDP growth rate during Abenomics, an economic expansion phase that was one step away from recording the longest economic growth period after World War II, was only about 1.2% on an annualized basis. By industry,

¹¹ The share of container volume in the five main ports is about $60\% \times (1 \text{ month}/12 \text{ months})$.

machinery such as electrical and optical equipment and transportation equipment with a large industry scale as well as chemical and metal industries made greater contributions (**Chart 11**). In machinery, items with a high dependency on China include certain parts used in washing machines and traffic lights, and electric parts such as capacitors; and in chemical and metal products, there are numerous general-purpose products that depend on Chinese imports. We believe these parts will face bottleneck situations (**Chart 12**).

Not limited to Japan, supply chain dependency on China has been the center of debate since the outbreak of COVID-19. In view of our report’s estimate results, the risk factor of China’s “Zero COVID” policy may become a good opportunity to reconsider the China risk.¹²

Chart 9: Size of major ports and export decrease with ports closed

Ports	Container volume (1000 TEU)	Mainland China share (%)	Downward pressure when port closed for one month	
			To export (%)	To GDP (%)
Shanghai	43303	19.2	1.6	0.3
Ningbo	27530	12.2	1.0	0.2
Shenzhen	25770	11.4	1.0	0.2
Guangzhou	23236	10.3	0.9	0.2
Qingdao	21010	9.3	0.8	0.1
Tianjin	17264	7.7	0.6	0.1
Xiamen	11122	4.9	0.4	0.1
Dalian	8760	3.9	0.3	0.1

Note: Shenzhen comprises the three ports of Chiwan, Shekou, and Yantian. The percentage to GDP represents the nominal value. We estimated the export reduction volume of each port based on the container volume (2019) (RMB1 = USD6.35).
Source: Made by MHRT based upon Lloyd’s List One Hundred Ports 2020.

Chart 10: Impact of China’s export suspension on major countries

Country/region	Light industry			Basic materials				Machinery			[Total] Value added change rate (%)			
	Foods	Textile products	Leather products	Wood products	Paper products	Petroleum and coal products	Chemical products	Rubber/plastics	Non-metallic minerals	Metal products		Equipment machinery	Electrical and optical equipment	Transportation equipment
Taiwan														-1.1
South Korea														-0.5
Russia														-0.5
Vietnam														-0.4
Philippines														-0.4
Indonesia														-0.4
Singapore														-0.3
Malaysia														-0.3
US														-0.3
Japan														-0.2
Eurozone														-0.2
Australia														-0.2
Thailand														-0.2
India														-0.1

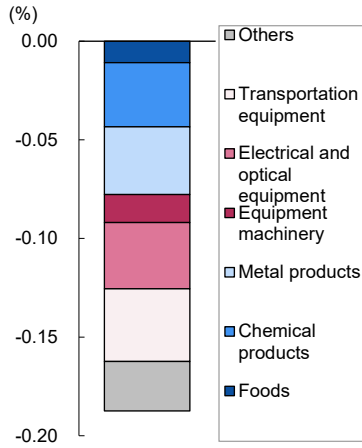
Note: The table presents the change rate of value added by country/industry in the case where China’s annual exports decrease by 5% and bottlenecks occur. Our calculation only reflects the primary impact and does not take into account ripple effects.
Source: Made by MHRT based upon ADB.

It should be noted that our estimate considered only the impact on the manufacturing industry and not the service industry for the purpose of clarifying the assumptions. We also limited our estimate to the primary impact on the manufacturing industry and did not consider any secondary ripple effects that could arise if a bottleneck occurs and production declines in a certain industry, thereby affecting other industries that procure products from the affected industry. We cannot deny the possibility that the impact will be greater than our estimate and therefore ask our readers to interpret the estimate results with a degree of

¹² From a security perspective in important sectors such as semiconductors, there is already a movement to switch to domestic procurement or strengthening alternative procurement from other countries.

latitude.

Chart 11: Impact on Japan



Note: Same as **Chart 10**.
Source: Made by MHRT based upon ADB.

Chart 12: Parts/raw materials with high dependency on Chinese imports

Item (Chemical/metal raw materials)	China dependency rate (%)	Item (Machinery parts)	China dependency rate (%)
Phosphatic fertilizers	99.3	Washing machine parts	96.7
Diphosphorus pentoxide, phosphoric acid, polyphosphoric acids	98.9	Capacitors	79.5
Magnesium, strontium, barium compounds	96.1	Parts of electrical equipment such as road signals	75.1
Hydrogen chloride (hydrochloric acid), chlorosulphuric acid	92.1	Parts for data processing and office machines, etc.	70.2
Base metals, silver or gold, clad with platinum	91.9	Vacuum cleaner parts	70.2
Magnesium	89.0	Parts for meters, pedometers, tachometers, etc.	69.0
Iron or steel anchors and their parts	86.9	Machine parts used in agriculture, forestry, etc.	67.6
Iron or steel nails, etc.	86.6	Printing machine, copier and facsimile parts	66.5
Decorative parts such as base metal bells	84.5	Parts for hydraulic turbines, water wheels, their regulators	64.4
Glycosides and their derivatives	83.8	Parts for photographic laboratory equipment, projection screens	63.8
Derivatives such as aldehydes	83.5	Parts for drawing, calculating, length measuring instruments, etc.	61.5
Bismuth	79.7	Static converters, inductors, etc.	61.5
Zinc dust, powders and flakes	78.0	Optical and precision equipment parts	60.3
Some alloy steel in ingots or other primary forms	77.8	Electrical resistors	59.4
Some cast articles	77.2	Parts for self-propelled work trucks and tractors	58.5
Cadmium	77.0	Parts for equipment similar to telephones	58.2
Cast iron tubes, pipes and hollow profiles	76.8	Parts for cranes, lifts, etc.	57.5
Manganese	76.5	Parts for electric motors and generators	56.9

Note: Data as of 2019. We extracted items that correspond to parts, materials, and processed goods from the 6-digit HS code and integrated them with the 4-digit HS code in order to calculate the degree of import dependency.
Source: Made by MHRT based upon UN Comtrade and RIETI-TID.

3. Conclusion

We have thus far examined the outlook and risks of the Chinese economy by focusing on the two keywords of “property” and “Zero COVID.” Our analysis revealed that when something goes wrong or when risks arise in China, the world’s second largest economy, many countries around the globe, including Japan, are negatively affected, particularly their supply chains. Although the degree of impact will vary depending on the country/region, we cannot ignore the size of this potential impact. China’s economic development will continue to serve as an essential factor when analyzing the recovery capability of the Japanese economy going forward.

While China prioritizes stability of its economy in 2022, we need to remain vigilant as to the risk factors of “property” and “Zero COVID” in the future.

Reference

Refer to the original Japanese report by clicking the URL below for the reference material.
<https://www.mizuho-ir.co.jp/publication/report/2022/pdf/insight-as220228.pdf>