

## China Watch

# Larger-than-expected 50bp RRR cut signals more monetary policy support underway

## 50bp RRR cut sent a clear signal to boost sentiment

The People's Bank of China (PBoC) said it will lower the reserve requirement ratio (RRR) by 50bps, effective on February 5, according to Governor Pan at a press conference today. This RRR reduction will release RMB1tn of long-term liquidity to commercial banks. After the cut, the weighted average RRR will decline to around 7.0% (from 7.4%).

This RRR cut was a slight beat in terms of magnitude, as the market was expecting a 25bp drop. It marked the first time over the past two years that the PBoC reduced RRR by 50bps at one time, after slowing the pace to 25bps each time since April 2022.

The RRR cut should help meet liquidity demand ahead of Lunar New Year (LNY) holidays, when liquidity demand is strong. However, the net liquidity impact would also depend on the size of PBoC's OMO injections subsequently. After disappointing the market with no rate cuts last week, we believe the move today sent a clear signal that the PBoC will step up on easing measures to lift market sentiment and economic growth.

## More actions on the way to support credit growth

During the press conference, Governor Pan revealed that the central bank will issue new policies in conjunction with the National Administration of Financial Regulation in order to improve the scope of fund use and liquidity for property developers. Detailed policy is expected to be released later today or tomorrow.

Governor Pan also announced that the central bank will establish a new department focusing on guiding financial institutions to injecting more funds to targeted areas (technology, green economy, SMEs, senior care and digital economy). In addition, the central bank emphasized that it will (1) optimize credit structure, (2) restrict financing to industries with overcapacity, and (3) guide financial institutions to smooth the pace of credit growth. Meanwhile, the PBoC shall maintain accommodative liquidity condition in accordance with the pace of government bond issuance.

## LPR likely to see a small drop; PBoC reiterated FX stability

The PBoC also announced today that the relending and rediscount rates for agriculture and SMEs will be lowered by 25bps to 1.75%, effective on January 25. This, along with the deposit rate cuts in Nov-Dec and today's RRR cut, should help the Loan Prime Rate (LPR) to move lower, according to Governor Pan.

Touching upon the external environment for 2024, Governor Pan mentioned that spillovers from advanced economies will lessen in 2024. Specifically, the central bank will have more room for monetary easing as the Federal Reserve pivots to rate cuts. That said, Pan reiterated that the PBOC will keep the yuan at a reasonable "equilibrium" level, implying limited tolerance for currency depreciation in the near term.

Taking all of the above into consideration, we expect to see a small decline in the 1yr LPR in the near term, possibly 15bps in 1Q, and another 30bps accumulatively before the yearend, to 3.0%.

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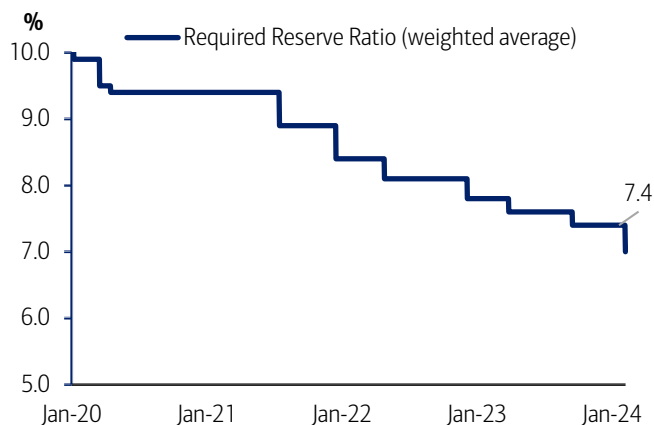
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**Exhibit 1: RRR cuts since 2020**

PBoC cut RRR by 50bp, pushing the weighted average RRR down to around 7.0% from 7.4% previously

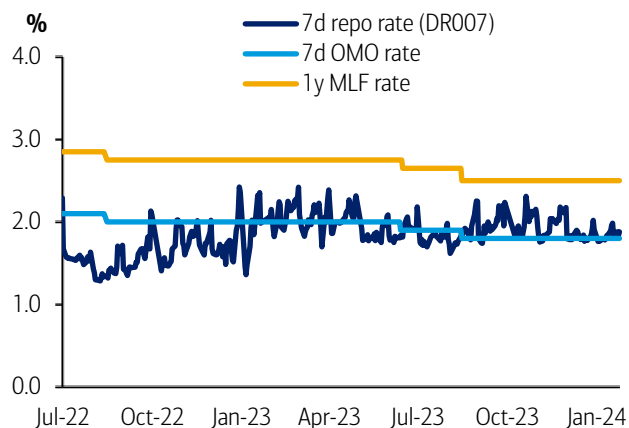


Source: CEIC

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**Exhibit 2: Money market rates vs. policy rates**

DR007 stayed close to the policy rate (7d OMO rate) recently, suggesting improved financial conditions

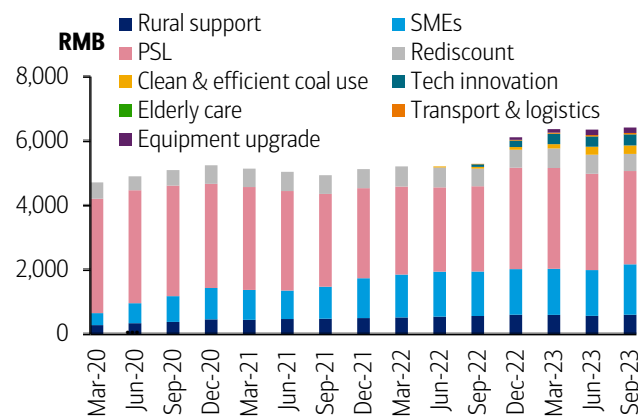


Source: CEIC, Bloomberg

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**Exhibit 3: PBoC's targeted lending tools**

The total outstanding balance of targeted lending tools increased gradually

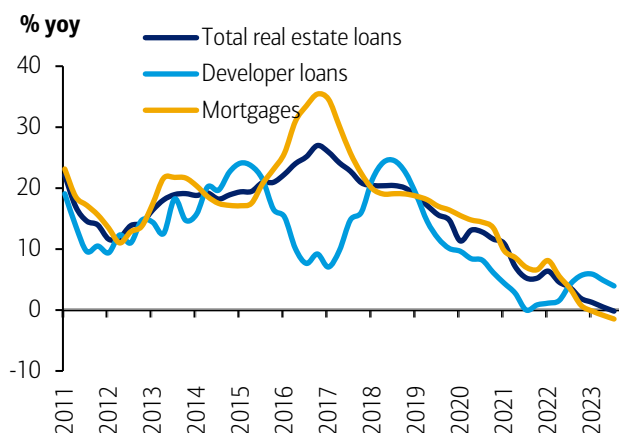


Source: PBoC, CEIC

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**Exhibit 4: Total real estate loans by breakdown**

The growth of total real estate loans yet to turn around



Source: CEIC

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