

# Macro Note

## China: PBoC Cuts broad RRR By 50bps To Usher In 2020

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- China cut RRR by 50bps effective 6 Jan 2020 and expected to release liquidity of RMB880bn
- We had anticipated a RRR cut in 1Q20, which was bolstered by Premier Li's comments made in late Dec (2019)
- Another cut in RRR remains possible as the Chinese government focuses on reducing costs of financing to the real economy, even as there are positive signs of easing US-China trade tensions

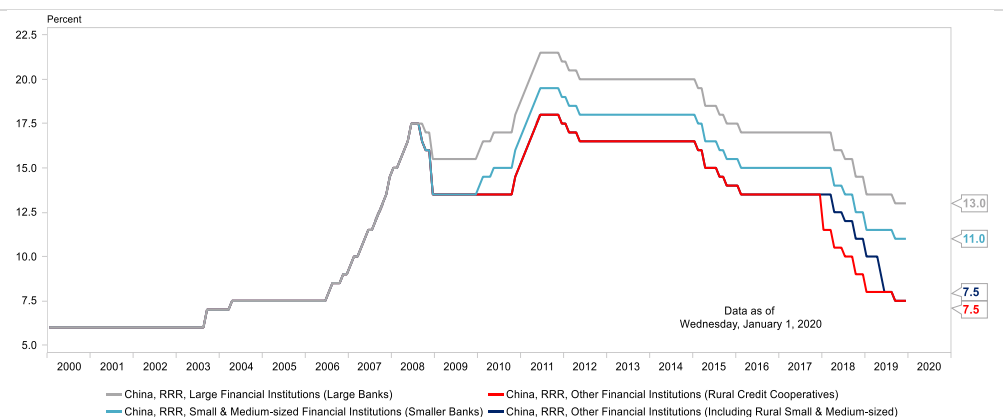
### A Broad-Based RRR Cut With Effect From 6 Jan 2020

Just as the new year began, China's central bank announced on Wednesday (01 Jan 2020) a broad-based 50bps cut to banks' reserve requirement ratio (RRR), effective 6 Jan 2020. The move is expected to release RMB880bn (USD125bn) of long term liquidity, and aimed primarily at lowering costs of financing the real economy, especially for small and micro-enterprises, according to the PBoC's Q&A.

The latest cut will bring the RRR for large banks from 13.0% currently to 12.5% on 6 Jan 2020, and add to the total of 150bps reduction in 2019.

### China: Banks' Reserve Requirement Ratio (RRR)

Source: Macrobond, UOB Global Economics & Markets Research



The RRR cut came as no surprise as we had already anticipated a reduction in the RRR to take place in 1Q20, to ease liquidity tightness in the lead up to the Spring Festival period (the first day of Spring Festival falls on 25 Jan in 2020). The previous RRR cut was announced in Sep 2019, which was more aggressive with a 50bps cut in RRR for all banks, as well as an additional, targeted 100bps cut for qualified smaller financial institutions. (For more details please refer to our report: [China RRR Cuts To Buffer Economic Slowdown And Trade Uncertainty](#), 9 Sep 2019)

Speculation had been rife for a RRR cut soon after Chinese Premier Li Keqiang's visit to the Chengdu Free Trade Zone on 23 Dec 2019. Premier said at that time that "... the government will carry out further research into the use of multiple tools including the reserve requirement

ratio, re-lending and rediscounts to cut real interest rates and financing costs to ease the financing difficulties of small and micro-businesses."<sup>1</sup>

#### **Another RRR Cut Remains On The Cards**

Notwithstanding the easing of the US-China trade tensions (with the Phase 1 trade agreement expected to be signed in the US on 15 Jan 2020), the Chinese government's current approach has been focused on reducing costs of borrowing for the small and micro enterprises. This has culminated in the reform of the domestic benchmark interest rate in Aug 2019 and starting 1 Jan 2020, financial institutions are required to price all new loans using the Loan Prime Rate (LPR) benchmark and convert existing loans to the new benchmark from 1 Mar – 31 Aug 2020. (For more details please refer to our reports: [PBoC Accelerates Interest Rate Reform](#), dated 30 Dec 2019 and [PBoC's Bold LPR Reform To Drive Borrowing Costs Lower, dated 19 Aug 2019](#))

As such, there is still a possibility of another broad-based RRR cut in 2Q or 3Q this year depending on the pace of recovery of the domestic economy as well as the progress on the interest rate front. The RRR cuts will lower funding costs for commercial banks and possibly result in lower lending rates to businesses through lower LPR fixings. We anticipate the benchmark 1Y LPR falling from 4.15% currently to 3.80% by mid-2020, assuming the LPR moves lower by around 5bps each month on average into mid-2020 and with no further cuts to Medium-term Lending Facility (MLF). The 1-year MLF rate – which the LPR is pegged to – was only cut by 5bps to 3.25% in Nov 2019, marking the first reduction since March 2016.

#### References:

PBoC announcement: 50bps in RRR cut effective 6 Jan, 1 Jan 2020

<http://www.pbc.gov.cn/goutongjiaoliu/113456/113469/3953630/index.html>

PBoC Q&A on RRR Cut, 1 Jan 2020

<http://www.pbc.gov.cn/goutongjiaoliu/113456/113469/3953633/index.html>

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<sup>1</sup> Premier Li stresses enhancing economic vitality during inspection tour, 24 Dec 2019 [http://www.china.org.cn/business/2019-12/24/content\\_75544212.htm](http://www.china.org.cn/business/2019-12/24/content_75544212.htm)

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