20 July, 2021

China's Central Bank cut the Required Reserve Ratio for banks to underpin economic recovery?

People's Bank of China announced to cut the bank's required reserve ratio on 9 July. It is speculated by the market that it is an effort to boost the recovery from pandemic. The PBOC said the cut in the reserve requirement ratio by 50 basis points, which is the first reduction since 2020 January. The reserve requirement represents the amount of money that banks must hold in their coffers as a proportion of their total deposits. A lowering of the required amount will increase the money banks can lend out to businesses and individuals. Therefore, such move will usually increase the money supply in the market. It is expected the 0.5% cut will unleash about 1 trillion yuan liquidity into the economy. Still, the central bank said the cut does not signal a sudden shift in monetary policy.

The PBOC's move just comes one day after Premier Li Keqiang mentioned the cut in the reserve ratio as a way to provide more support to the real economy, especially small, medium and micro enterprises, during a regular State Council meeting.

China government reiterated that the monetary policy should be flexible, targeted and appropriate, while keeping interbank liquidity reasonable. Instead of indiscriminate stimulus, it will ensure the liquidity is adequate but at a reasonable level and that the growth of money supply and aggregate financing to the real economy is in line with nominal GDP growth.

First reduction in reserve requirement ratio since January 2020

Source: Bloomberg

However, the move went further than many economists had expected and may suggest growing concerns about the economy's faltering recovery

1. Less than a month ago, the China top official warned the ultra-loose monetary easing in developed countries has reached an unprecedented level, already triggered widespread negative impacts globally. Guo Shuqing, the chairman of China Banking and Insurance Regulatory Commission, said that the "extraordinary measures" taken by developed countries to boost their economies drastically will have negative impact on every country, including soaring financial market and real estate market, end up be felt by the entire world, while noting that China's products are serving as a "key anchor" in stabilizing inflation.

2. The cut in RRR this time is more comprehensive when comparing to previous cuts as most of the previous cuts were only be targeted at small and medium enterprises (SMEs). As the cut this time applied to almost all banks and deposits, it will unleash a much higher amount of liquidity to the financial system than the boost by the previous cut.

3. Even though the head of central bank's monetary policy department reiterated at a press briefing the RRR cut is a standard liquidity operation after monetary policy returned to normal and the prudent monetary policy direction has not changed, as the cut is not really well expected by the market, the sudden RRR cut has been speculated by the market that the China government may worry the economic growth will slow down substantially in the second half year.

So far, we don't see any significant problems happening in China's economy

China Manufacturing PMI: Although it has continued to decline since the end of last year, the index is still higher than 50, reflecting that the manufacturing industry is still expanding

Source: Bloomberg

Year-on-year comparison of the cumulative value of China's exports: Although the year-on-year growth is indeed showing a significant decline compared with the beginning of the year, the year-to-date cumulative value has increased by as high as 40% year-on-year as of May. It is indeed an abnormal high growth rate that cannot be sustained for a long time. Therefore, it will be declined sooner or later.

Source: Bloomberg

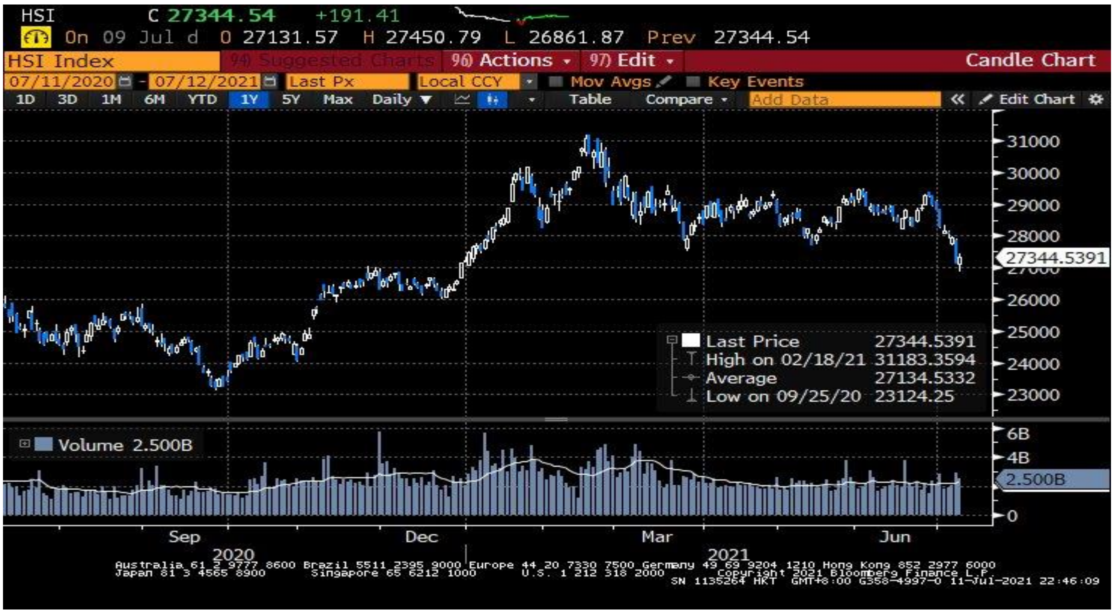
Monthly retail sales in China: The growth is not very outstanding but it is much higher than 2020, and also much higher than 2019.

Source: Bloomberg

The monetary easing should had positive impact to the stock market

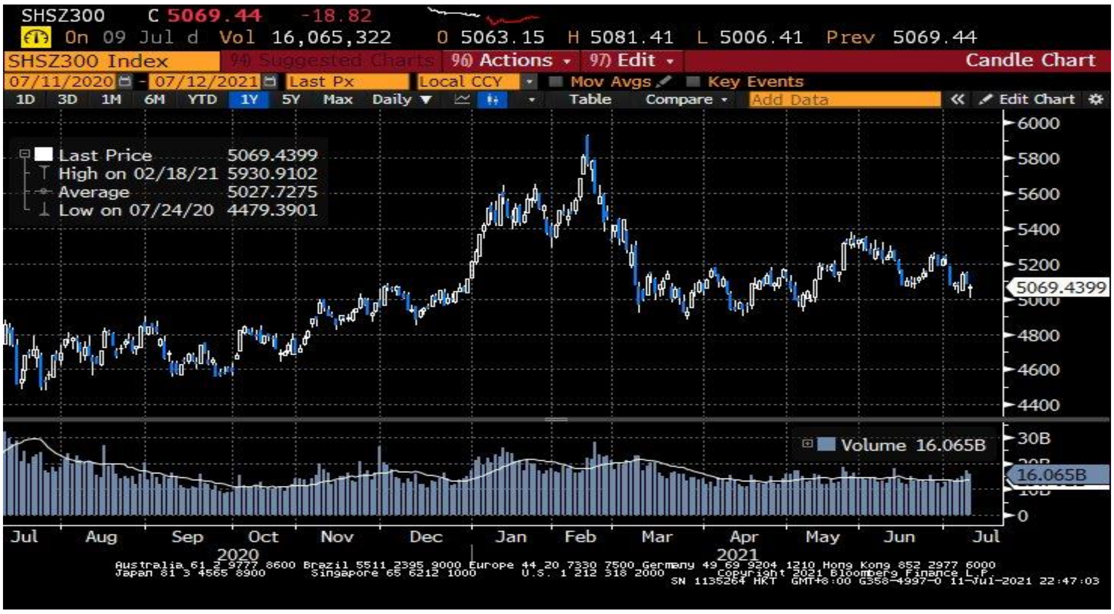
In theory, a looser monetary policy should be a positive to the stock market. However, such potential positive impact may not be applied to the stock market this time. It is because the market momentum may not be able to be boosted up given concerns over slowing economic growth due to the speculation about the sudden policy shift.

Hong Kong Hang Seng Index: Did not benefit from RRR reduction and fell 3.4% last week. However, the dropdown may be due to Chinese government continued to tighten its scrutiny to the technology sector



Source: Bloomberg

China CSI 300 Index: Down 0.2% throughout the week



Source: Bloomberg

Source: Reuters, CNBC, Yahoo Finance, Bloomberg, Investing.com, Marketwatcher.com

Important Note & Disclaimer:

- The document is property of AMG FINANCIAL GROUP. All information in this document is strictly for information purposes only and should not be considered as an invitation, an offer, or solicitation, to invest or a recommendation to buy or sell any particular security or to adopt any investment strategy mentioned herein. AMG Financial Group Limited (here after AMG) endeavors to ensure the accuracy and reliability of the information provided but do not guarantee its accuracy or reliability and accept no liability for any loss or damage arising from any inaccuracies or omission. Some of the information in this document may contain projections or other forward looking statements regarding future events or future financial performance of countries, markets or companies. These statements are only predictions and actual events or results may differ materially. Any opinion or estimate contained in this document is made on a general basis and is not to be relied on by the reader as advice. AMG reserves the right to make changes and corrections to its opinions expressed in this document at any time, without notice to the recipients of this document. Any unauthorized disclosure, use or dissemination, either whole or partial, of this document is prohibited and this document is not to be reproduced, copied, and made available to others. Investment involves risks. The value of any investment and the income from it can rise as well as fall as a result of different market risks, such as currency and market fluctuations. Past performance figures shown are not indicative of future performance. The recipients of this document should seek for professional advice if they are in any doubt about any of the information contained herein. This material has not been reviewed or approved by the Securities and Futures Commission.

For any comments, please send email to us at enquiries@amgwealth.com.

AMG FINANCIAL GROUP
40/F, 118 Connaught Road West, Hong Kong
Telephone: (852) 3970 9531 Facsimile: (852) 3426 2650