

A bigger and deeper targeted RRR cut from China

The targeted reserve-ratios cut came as a surprise as it is deeper and broader than even what was suggested. But we're not that optimistic. The ultimate amount loaned to smaller companies will be less than what the central bank expects



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More banks to enjoy the targeted RRR cut

The People's Bank of China has [cut the reserve requirement ratio \(RRR\) today](#) for some banks by 0.5 to 1 percentage point, effective from 16 March, releasing 550 billion yuan in liquidity to shore up the economy amid the coronavirus fallout.

This targeted RRR cut is bigger than expected. But not only does this move, increase the degree of the cut, it also expands the scope of banks that can lend to smaller companies.

For banks that were not in scope before, the cut is 0.5 percentage points, but for banks that were already part of the scheme, the cut will be 1.0 percentage points.

More loans for smaller companies?

This time, the central bank expects the liquidity release to be around CNY 550 billion, of which CNY400 billion is expected to be lent out for inclusive finance that benefits smaller firms. The remainder is for long-term loans.

With the pandemic rapidly spreading, supply chains are not the only thing taking the hit, global consumption demand will also fall too. Smaller factories and exporters face bigger risks and banks will be taking this into consideration when they assess credit risks.

This is why we're not that optimistic and believe the ultimate amount of inclusive finance will be significantly smaller than what the central bank expects.

Interest rates to move downwards?

We believe the actual liquidity increased by the targeted RRR cut, will probably be even smaller than is expected but this should still push down market interest rates from the short end to the long end. As such the yield curve may shift down parallel by 30-50 bps.

A rate cut is coming

We think an interest rate cut is coming, but it may be deferred to April as there is already a deeper targeted RRR cut in March.

We expect 10 basis point cuts in 7D reverse repo, 1-year medium lending facility and 1-year loan prime rate in April and this set of rate cuts will push sovereign yields down further.

Weaker yuan ahead

We expect this deeper than expected targeted RRR cut will make the yuan weaker against the dollar on Monday and believe USD/CNY and USD/CNH could cross 7.0 soon.