

China's PBoC injects liquidity to support growth but yuan could turn weaker in March

The People's Bank of China has kept the 1Y Medium Lending Facility rate at 2.75% but increased the volume of the facility by CNY79 billion in January. The market should perceive this as a supportive measure. But the yuan could be weaker in March when retail sales data is released



Leading members of the People's Bank of China, including Governor, Yi Gang (waving)

The PBoC paused rate policy, but increased liquidity

The PBoC decided to leave the 1Y Medium Lending Facility (MLF) policy rate at 2.75% today. But there was an extra liquidity injection on the 1Y MLF volume of CNY 79 billion to CNY779 billion for January.

One reason for this increase is that the Chinese New Year holiday is coming, and liquidity is usually tight ahead of this, though the PBoC has already been injecting liquidity to cover the holiday period through open market operations.

We believe there is another more important reason for the increase in volume. And that is that the PBoC would like to support strong loan growth by injecting extra liquidity via the MLF at the beginning of the year rather than cutting the required reserve ratio, which is a more aggressive monetary policy tool.

Chance of RRR cut in 1Q23



Lower after increase in 1Y MLF volume

Yuan should remain robust before the Chinese New Year holiday but this could be temporary

The market should perceive more liquidity injections as supportive for economic growth, and this should help support the yuan.

Our forecast of USD/CNY at 6.9 at the end of 1Q23 looks off the mark. But we expect to see weaker-expected economic activity when retail sales data for January to February come out in March. That could change the course of the yuan. We expect that retail sales from January to February will increase only slightly from last year as consumers focus more on healthcare services and medicines instead of general shopping activity for the Chinese New Year. Retail sales should pick up in the second quarter.

Our USD/CNY forecast for the end of 2023 is 6.72