China’s central bank unlikely to ease further this year

With such unexpectedly small credit growth, we believe China's central bank has used actions rather than words to let the market know that it won't be easing any more this year

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

Chinese credit growth was unexpectedly low in July

New yuan loans were only CNY992.7 billion in July, falling from CNY1,810 billion a month ago. Aggregate financing was only CNY1,690 billion for the same period, decreasing from CNY3,430 billion in June. Both numbers were the lowest growth numbers since February 2020 when banks were closed for the Chinese New Year holiday.

All items in aggregate financing grew less than a year ago, except for yuan loans and stock fundraising.

This means that not only shadow banking activities decreased on a yearly basis but also corporate and government bond issuances decreased too.

PBoC has acted as if the economy will continue to recover

Apart from not cutting the reserve requirement ratio (RRR) and interest rates, the central bank has absorbed liquidity from the interbank market, which has moved the 3-month Shanghai interbank overnight benchmark rate, or Shibor, from 2.12 at the end of June to 2.60 as of today.

It is clear that the central bank is not going to ease unless Covid-19 returns on a large scale, which seems unlikely at this stage given China's continued tight social distancing measures even given that there are only small clusters of cases.

The central bank may also ease again if the technology war hurts Chinese short-term growth significantly. However, we doubt this will be the case as we see the tech war hurting long-term growth more than short-term growth.

We think the central bank may only provide some liquidity support on a small scale to SMEs and agricultural activities, and this will be too small to move the interbank rate.

But we don't expect any tightening from raising RRR or policy interest rates. Tightening monetary policy is only expected when the economy is overheating, and we do not see this happening in 2020.

Forecasts

We expect the RRR to stay at 12.5%, and the seven-day reverse repo, 1-year Medium lending rate, 1Y and 5Y loan prime rates to stay at 2.20%, 2,95%, 3.85% and 4.65%, respectively, at least until the end of 2020.

Author

Iris Pang
Chief Economist, Greater China
iris.pang@asia.ing.com