PBC Official Answered Press Questions on Announcement of Targeted RRR Cuts and Benchmark Loan and Deposit Interest Rates Reductions

Q: What is the background of the targeted reserve requirement ratio (RRR) cuts and benchmark loan and deposit interest rates reductions?

A: Since the beginning of this year, the PBC has continued to implement a sound monetary policy, paid greater attention to the stance so that it is neither too tight nor too loose, carried out pre-emptive adjustments and fine-tunings at the proper time and with appropriate strength, improved the dynamic adjustment mechanism of differentiated reserve requirements, cut RRR cuts for targeted financial institutions, strengthened the structural guidance of credit policy, and encouraged financial institutions to increase credit resources allocation to the key areas and weak sectors, such as the agricultural sector, rural areas and farmers and the micro and small enterprises. At the same time, the PBC have employed a combination of monetary policy instruments, such as interest rate and RRR, to keep the liquidity at adequate levels, and to guide the market interest rates to move downward moderately and to reduce the social financing costs. In general, as the effects of various policy measures gradually unfolded, money, credit and social financing aggregates posted reasonable growth, liquidity in banking system remained abundant, social financing structure improved, market interest rates of various maturities declined, and the high financing costs for enterprises was alleviated effectively.

Against the backdrop of the new normal, the economy is undergoing a critical period of industrial transformation and growth driver shift, and there is still a lot of work to be done to ensure steady growth, to make structural adjustments, further reforms, to improve people’s livelihood, and to prevent risks. Therefore, it is necessary to use the monetary policy instruments flexibly, promote the stable and healthy development through structural adjustments, and focus on reducing financing costs. Meanwhile, the level of consumer prices remains low and the real interest rates are above historical average, thus providing favorable conditions for the use of instruments such as RRR and interest rates. In view of this, with the approval of the State Council, the PBC decided to further cut the RRR of RMB deposits for targeted financial institutions, and lower the benchmark loan and deposit interest rates, in an effort to strike a balance between maintaining stable aggregates and optimizing economic structure, to promote steady growth and structural adjustments, and to reduce social financing costs.

Q: What are the details of the targeted RRR cuts?

A: The contents of this round of targeted RRR cuts are as follows. First, the RRR is cut by 0.5 percentage point for city commercial banks and non-county-level rural commercial banks which, according to the results of evaluation in early 2015, have reached the required ratios in their lending to the agricultural sector, rural areas and farmers as specified by the targeted RRR cuts in June 2014. Before this, targeted RRR reduction of 0.5 percentage point was applied to the aforesaid institutions that reached the required ratios in their lending to the agricultural sector, rural areas and farmers, and a cumulative reduction of 1 percentage point was applied to those that reached the required ratios in their lending to the micro and small enterprises.

Secondly, the RRR is cut by 0.5 percentage point for large state-owned commercial banks, joint-stock commercial banks and foreign-funded banks which, according to the results of evaluation in early 2015, have reached the required ratios in lending to the agricultural sector, rural areas and farmers or to the micro and small enterprises as specified by the targeted RRR cuts in June 2014. Prior to this one, a targeted RRR cut of 0.5 percentage point was applied to the institutions that have reached the required ratios in lending to the agricultural sector, rural areas and farmers, or lending to the micro and small enterprises. As a result, the large state-owned commercial banks, joint-stock commercial banks, city commercial banks, non-county-level rural commercial banks and foreign-funded banks, which have been evaluated in early 2015 as having complied with prudential requirements, and also have reached the required ratios in their agro-lending or lending to the micro and small enterprises as specified by the targeted RRR cuts in June 2014, are all entitled to a RRR reduction of 1 percentage point. Thirdly, the RRR is cut by 3 percentage points for finance companies to enhance the capacity of large corporate groups to finance from inside, improve the efficiency of fund turnover, relieve the funding and cost pressures of state-owned enterprises and provide support to the transformation and development of the real economy.

Q: Why did the PBC choose targeted RRR reduction instead of a universal one?

A: After the RRR was cut by 1 percentage point at the end of April, the volume of reserves of banking system reached a record high at some time points. It is estimated that the excess reserves of the banking system will remain at about 3 trillion yuan at the end of June. Meanwhile, the lowest overnight interest rate on monetary market got very close to its record low of 1%. Due to the recent freezing of massive volume of fund before the imminent IPOs, interest rates on the inter-bank market have rebounded from the lowest point, but remain low. Since liquidity in the banking system is abundant on the whole, it is unnecessary to provide extra liquidity by RRR cuts for all financial institutions.

The PBC has used monetary policy instruments to support adjustment of economic structure, and especially to encourage and direct financial institutions to provide more credit to agricultural sector, rural areas and farmers, and of micro and small enterprises. The current government always attaches importance to targeted adjustment, and aims to enhance the focus and effectiveness of macroeconomic management. The Central Economic Work Conference has decided that the targeted and structural adjustment should continue in 2015. This round of targeted RRR cuts aims at strengthening the capacity of financial institutions to support the developments of agricultural sector, rural areas and farmers and micro and small enterprises, reinforcing the positive incentive, supporting the key areas and weak sectors in national economy, and providing financial support to popular entrepreneurship and innovation.

Q: What are the positive effects of the benchmark loan and deposit interest rate reductions in reducing the costs of social financing?

A: In order for the benchmark interest rates to guide market interest rates, cut the social financing costs and provide support to the sustainable and healthy development of the real economy, the PBC lowered the benchmark loan and deposit interest rates for financial institutions three times since the beginning of 2014. As a result, the one-year benchmark loan interest rate has been lowered by 0.9 percentage point cumulatively to 5.1%, and the one-year benchmark deposit interest rate has been lowered by 0.75 percentage point cumulatively to 2.25%. Due to the successive reductions of benchmark interest rates, the weighted average interest rate on new loans granted by financial institutions was 6.16% in May 2015, down 0.91 percentage point from the same period last year, hitting the lowest level on record since 2011. Meanwhile, deposit rate pricing by financial institutions tends to be more rational, deposit interest rates have come down in general, and a tiered, differentiated, and competitive deposit rate pricing mechanism is basically in place. As the policy measures take effect gradually, the interest rates on monetary market and bond market have also come down substantially, and the social financing costs have declined.

Looking at the effects of the recent interest rate reductions, though the interest rates on loans are fully market priced, the benchmark loan interest rate released by the PBC still plays a strong steering and signaling role. Thus, further cut of benchmark loan interest rates is likely to guide the real interest rates for loans to move downward. In addition, the RRR cuts announced at the same time will help reduce the funding costs for financial institutions, to bring along further declines in various market interest rates and financing costs for enterprises, and to reinforce the effects from the previous macroeconomic management policies.

Q: What are the other considerations of the PBC in the conduct of monetary policy at the next step?

A: This round of targeted RRR cuts combined with benchmark loan and deposit interest rates reductions is conducted to further strengthen the vital role of monetary policy in optimizing economic structure, promoting the stable, healthy and sustainable development of the economy, and meanwhile continuing to use benchmark interest rate to guide market interest rates and to reduce the costs of social financing. At the next step, we will continue to follow the strategic arrangements of the CPC Central Committee and State Council, adhere to the general principle of seeking progress while maintaining stability and the requirements of having stable macro policies and flexible micro policies, take initiatives to adapt to the new normal, and properly manage the magnitude and pace of the macro policies. We will continue to implement a sound monetary policy, employ a combination of various monetary policy instruments, strengthen and improve macro-prudential regulation, optimize the policy mix, and build a neutral monetary and financial environment for the structural adjustment, transformation of growth model and upgrading of the economy. At the same time, we will further improve the monetary policy framework, continue the reforms of market-based interest rate and RMB exchange rate regime, improve the channels of monetary policy transmission, enhance the efficiency of financial resource allocation, and promote the sustainable development of the economy.

Date of last update JUL. 22, 2015