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China Slowdown Bolsters Case for Easing as Yuan Slides: Economy

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March 12 (Bloomberg) -- China's economic growth slowed in the first two months of the year, with both exports and domestic demand moderating faster than analysts had forecast, building the case for Premier Wen Jiabao to accelerate stimulus measures.

The world's second-largest economy had the biggest trade deficit last month in at least 22 years, the weakest January- February factory-production gain since 2009 and retail sales below the median economist estimate, government data showed March 9 and 10.

Central bank Governor Zhou Xiaochuan said today that the nation has large scope in theory for cutting banks' reserve requirements, and the yuan tumbled after officials weakened the daily reference rate. Moderating domestic inflation and faltering export demand in Europe may encourage officials to loosen credit and extend a pause in currency gains, with the yuan down 0.4 percent this year against the dollar after climbing 4.7 percent in 2011.

"Across Asia, the focus of macroeconomic policies is shifting towards supporting growth," said Eswar Prasad, a former China division chief at the International Monetary Fund who's a senior fellow at the Brookings Institution in Washington. "Many economies are holding some policy room in reserve as they brace for possible spillovers from external shocks."

The yuan fell 0.2 percent to 6.3253 as of 11:27 a.m. in Shanghai, the biggest decline since Jan. 20, after the central bank weakened the daily reference rate by the most since August 2010. The Morgan Stanley Asia Pacific index of stocks swung fell 0.3 percent as of 12:27 p.m. in Tokyo.

Reserve Ratios

Speaking at a briefing in Beijing as part of the annual meeting of the National People's Congress, Zhou said changes in capital flows and foreign-exchange reserves were key factors in decisions on bank reserve ratios, cut in February for the second time in three months. He said that such reductions were not an indication of policy loosening.

In a statement, the central bank reaffirmed a "prudent" monetary policy, to be fine-tuned as needed, and said "new ideas" will be used in managing a world-record $3.18 trillion of currency reserves.

Stocks around the world rallied at the end of last week as Greece's private creditors agreed to a debt swap, the U.S. reported job growth that exceeded forecasts and China's data spurred talk of new stimulus. The U.S. Standard & Poor's 500 Index gained 0.4 percent on March 9.

Preserving Firepower

In Asia, officials are weighing the need to preserve firepower for any deterioration in Europe with controlling inflation. India last week unexpectedly reduced its cash reserve ratio, while Australia's central bank said it has scope to lower rates and South Korea and Indonesia held off from stimulus.

In Asian economic data today, a Malaysian report may show that industrial production growth slowed in January, according to the median estimate in a Bloomberg survey of economists. Japan reported better-than-estimated machinery orders for January.

In Europe, Italy may report today that gross domestic product shrank 0.7 percent last quarter from the previous three- month period, confirming a preliminary estimate, according to another survey of analysts. In the U.S., the Treasury Department may say the government's budget deficit widened in February.

'Stable' Currency

China will keep the exchange rate "basically stable at an appropriate and balanced level," Wen, 69, said in the opening speech to the National People's Congress on March 5. He announced an economic-growth target for 2012 of 7.5 percent, down from the 8 percent goal in place since 2005.

Appreciation in the yuan will be "difficult," said Shen Jianguang, a Hong Kong-based economist for Mizuho Securities Asia Ltd., who previously worked for the International Monetary Fund and European Central Bank.

Zhang Zhiwei, chief China economist at Nomura Holdings Inc. in Hong Kong, is forecasting an interest-rate reduction this month and lower reserve requirements from April.

India's central bank on March 9 said it cut the amount of deposits lenders need to set aside as reserves to ease a cash squeeze in the banking system that threatens to deepen an economic slowdown. The Reserve Bank of Australia on March 6 said Europe remains a potential source of shocks "for some time yet" and that policy is "appropriate for the moment."

Rates on Hold

The Bank of Korea held off from altering borrowing costs for a ninth straight month, keeping its benchmark rate unchanged at 3.25 percent as Governor Kim Choong Soo said officials will try to keep inflation below a forecast of 3.3 percent. Indonesia's central bank on March 8 kept the reference rate at 5.75 percent.

"China and India will ease a touch," said Michael Buchanan, chief Asia-Pacific economist at Goldman Sachs Group Inc. in Hong Kong. In China, "disappointing" growth in exports and industrial production "opens more room for policy easing," he said.

In China, the February trade shortfall of $31.5 billion reported March 10 by the customs bureau in Beijing was the first in a year and four times the size of the previous largest deficit. Exports rose 18.4 percent from a year earlier, while imports gained 39.6 percent.

Data in the first two months are distorted by the timing of a Lunar New Year holiday, which fell in January this year and February in 2011. Analysts forecast a 31.1 percent increase in overseas sales and a 31.8 percent rise in inbound shipments, according to the median estimates in Bloomberg News surveys.

Slowing Inflation

China's consumer prices rose 3.2 percent in February from a year earlier, the least in 20 months, the statistics bureau said March 9. Industrial production gained 11.4 percent in January and February, less than forecast.

Retail sales rose 14.7 percent in the first two months from a year earlier, below the median economist estimate of 17.6 percent. New local-currency loans in February were 710.7 billion yuan ($113 billion), the People's Bank of China said March 9, lagging behind the median forecast of 750 billion yuan.

Wen, in his work report to lawmakers last week, said the government will "carry out timely and appropriate anticipatory adjustments and fine-tuning" of fiscal and monetary policies.

Suntech Power Holdings Co., the largest maker of solar panels, said increased competition and government subsidy cuts will lead to a first-quarter drop in shipments, according to a statement

March 8 from the Wuxi, China-based company. Deliveries in the first quarter will decline by about 30 percent from the fourth quarter, it said.

"Clearly, exports are still not strong enough to shore up 8 percent to 9 percent growth for China," said Ken Peng, a Beijing-based economist at BNP Paribas SA. "More policy support is necessary in coming months to ensure sufficient funding for investment."

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