Chinese economy

China cuts interest rates in bid to prop up lagging economic growth

Reductions come in wake of Communist party's third plenum but impact likely to be moderate, warn analysts

The People's Bank of China cut the one-year loan prime rate, widely used as a benchmark for corporate lending, for the first time since August last year © Jason Lee/Reuters

Cheng Leng in Hong Kong and **Thomas Hale** in Shanghai JULY 22 2024

China has unveiled unexpected cuts to lending rates days after a top Communist party policy meeting, in a sign of government efforts to boost lagging momentum across the world's second-largest economy.

The People's Bank of China announced on Monday that the one-year loan prime rate, widely used as a benchmark for corporate lending, would be lowered 0.1 percentage point to 3.35 per cent, the first such cut since August last year.

The five-year equivalent, which influences mortgage pricing, was also reduced 0.1 percentage point for the first time since February, to 3.85 per cent.

The cuts came after China's central bank reduced the so-called reverse repo rate, a seven-day rate used to price short-term lending, by 0.1 percentage point to 1.7 per cent. The PBoC said the move was intended to "strengthen countercyclical adjustments to better support the real economy".

The PBoC on Monday also lowered rates on the so-called standing lending facility, loans made to banks in need of short-term cash, by 0.1 percentage point across all maturities.

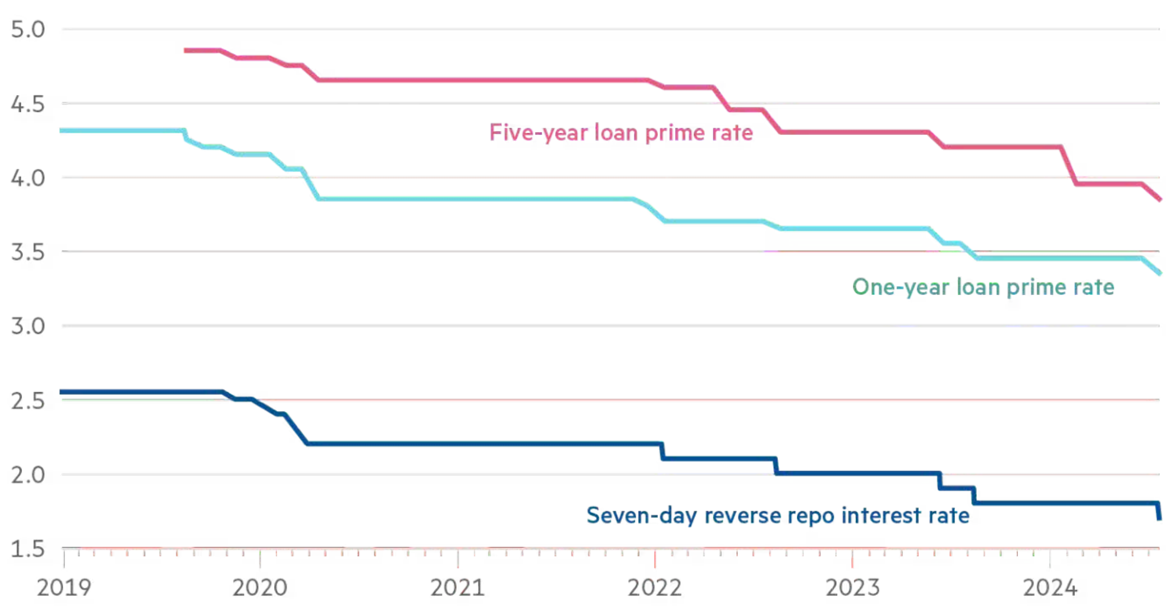
China has repeatedly cut its main lending rates in recent years against the backdrop of a prolonged property slowdown and weak domestic consumption. Policymakers have come under pressure to take greater action to shore up investor and consumer confidence.

Official data last week showed the economy grew 4.7 per cent in the second quarter, missing forecasts, while metrics across the property sector worsened.

"This quantitatively modest but symbolically significant set of actions signals the government's willingness, finally, to use macroeconomic stimulus to support faltering economic activity," said Eswar Prasad, an economics professor at Cornell University.

China unveiled a slew of rate cuts on Monday

Per cent



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The rate cuts came on the heels of the Chinese Communist party's third plenum, a closely watched closed-door meeting in which the party's elite Central Committee lays out its policy direction. At this year's event, which wrapped up on Thursday, officials signalled concerns over the economy and pledged additional support.

Beijing has in recent months allowed state-owned enterprises to buy unsold housing in order to tackle the property slowdown. But there are few signs of improvement in the sector, with new home prices falling 4.5 per cent last month, the most in almost a decade.

China's rate-setting framework has evolved considerably in recent years, with rates such as the LPR linked to a medium-term lending facility set by the PBoC that influences banking sector liquidity. Pan Gongsheng, the central bank's governor, hinted in June at a bigger role for the repo rate in setting policy in the future.

Lynn Song, chief economist for greater China at ING, said Monday's cuts "could be seen as the PBoC signalling the seven-day reverse repo rate's new status as the primary policy rate", depending on whether other benchmark rates were also reduced in the coming weeks.

Analysts warned that the impact of such cuts was likely to be moderate. Prasad said the LPR reductions were "unlikely to be effective" unless "accompanied by fiscal stimulus and broader policy reforms to revive flagging private sector confidence".

"If the PBoC is serious about monetary stimulus, it should cut rates much more substantially," said Julian Evans-Pritchard, head of China economics at Capital Economics. "However, efforts to stabilise long-term yields and keep currency depreciation in check mean that large-scale rate cuts still seem unlikely."

China's 10-year sovereign bond yield dropped to 2.24 per cent on Monday following the cut, while the renminbi weakened to a near two-week low of 7.28 a dollar.

Additional reporting by Joe Leahy in Beijing