

## Counter-cyclical Measures Benefit China's Bond Market

### Summary:

In order to support the real economy and reduce financing cost, China's central bank announced a reduction of the required reserve ratio ("RRR") for most financial institutions by 0.5% on 16 September 2019. City commercial banks operating in Chinese provinces will reduce the RRR by additional 1% (0.5% on 15 October 2019 and another 0.5% on 15 November 2019). The RRR cut, together with the recent reform of the loan prime rate ("LPR") formation mechanism and the early issuance of local government special debt, would shore up economic growth and benefit the bond market.

The RRR cut will unleash long-term funds of about RMB900 billion, which will effectively increase the sources of funds for financial institutions and reduce banks' funding cost by about RMB15 billion per year. On 17 August 2019, the central bank announced measures to promote a more market-oriented quotation method, add five-year and longer tenors, and expand the scope of banks allowed to submit LPR quotations to improve the LPR formation mechanism. The transmission of these policies would help lower the lending rates for borrowers.

On 4 September 2019, the State Council proposed local governments to finish issuing special debt within the 2019 quota by end-September 2019 and allocate proceeds to projects by end-October 2019. This measure aims to further expand investment as China's manufacturing and infrastructure construction investment (excluding electricity) are facing pressure of slowing down.

Regarding the potential impact on the bond market, the RRR cut would drive down the bond yields and promote bond issuance. Meanwhile, countercyclical measures would strengthen market confidence and increase investors' risk appetite. In terms of industries, the scale of bond financing may increase significantly in construction and engineering, road and railway transportation, etc. The financing environment for some small and micro private enterprises may further improve, which would alleviate their liquidity risk to a certain extent.

For more details, please refer to the Chinese report:

《经济逆周期调节“三管齐下”，整体利好债券市场》

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