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World News China cuts bank reserves in policy shift to lift economy by Ahtasham Ul Haq

Article published on December 4th 2011 | Art

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Date December 04 , 2011

BEIJING China's central bank cut reserve requirements for commercial lenders on Wednesday for the first time in three years, a policy shift to ease credit strains and shore up an economy running at its weakest pace since 2009.

China's policy change came just hours before coordinated action by major central banks, including the Federal Reserve and the European Central Bank, to ease credit strains in world markets buffeted by the euro zone debt crisis.

Official concern is rising that the global economy is on a slippery slope as the euro zone struggles to decisively tackle its two-year crisis. Global markets rallied on the combination of central bank news.

China's central bank said on its website it lowered the amount of cash that banks have to set aside by 50 basis points, effective Dec 5. That cut the reserve requirement ratio (RRR) for the biggest banks to 21 percent from a record high 21.5 percent, freeing up funds that could be used for lending.

"This is a big move -- this is easing," said Stephen Green, China economist at Standard Chartered Bank in Hong Kong. "It's a clear signal that China is on a loosening mode. The next move will be another RRR cut in January."

The cut releases between 350 billion yuan and 400 billion yuan ($54.8 billion to $62.7 billion) into the banking system, analysts estimated.

The People's Bank of China (PBOC) joins the central banks of Brazil, Indonesia, Thailand and the euro zone, among others, in easing monetary policy, a reflection of the alarm that the euro zone debt crisis and a sluggish U.S. economy could drag the world back into a recession.

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China's unusually high reserve rate requirements have made life difficult for private-sector companies. While they account for 75 percent of urban employment, they find it far harder to secure bank loans than politically well-connected state-owned enterprises.

Worried about a destabilizing jump in unemployment, Beijing is eager to lend them a hand. In recent weeks, China has seen a spate of major strikes in its export powerhouse in the Pearl River Delta.

Ten of 19 analysts in a Reuters poll on Tuesday had predicted China would cut its bank reserves in December by 50 basis points. Eight had expected a move in the first quarter of 2012 and one not until the second quarter.

Purchasing managers' data on Thursday could confirm the pressure on China's manufacturers from the global slowdown after a flash PMI from HSBC last week suggested the sector was shrinking.

As recently as the middle of 2011, China was still tightening monetary policy to combat stubbornly

high inflation, which rose in July to a three-year high of 6.5 percent.

However, as the economy felt the chill of a slowdown in global activity and inflation eased, Beijing adopted a policy of "fine tuning" that included loosening credit for cash-starved small firms.

Beyond growth concerns, capital outflows driven by the global market jitters also help explain the central bank's move, said analysts. Capital inflows have been the main source of money supply growth in China.

"I think the move is partially driven by capital outflows in November. Also, it may indicate that the economy has weakened quite bit and that the official PMI reading does not look very good," said Zhiwei Zhang, China economist at Nomura.

There are fewer maturing central bank bills due in December, which also put strains on liquidity conditions for banks. (Reuters)

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Article Keywords:
world news, world news today, recent world news, the world news, world news live, world breaking news, business world news, bbc news world, bbc news live, forex news, education news, politics news, entertainment new, weather news, today s weather news, we

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