(BN) China Cuts Interest Rates to Boost Growth as Inflation Ease s (1)

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China Cuts Interest Rates to Boost Growth as Inflation Eases (1)
2012-06-07 11:12:52.490 GMT

(Updates with economist's comment in fourth paragraph.)

By Bloomberg News

June 7 (Bloomberg) -- China cut interest rates for the first time since 2008, stepping up efforts to combat a deepening economic slowdown as Europe's worsening debt crisis threatens global growth.

The one-year deposit rate will drop to 3.25 percent from 3.5 percent effective tomorrow, the People's Bank of China said on its website today. The one-year lending rate will fall to 6.31 percent from 6.56 percent. Banks can offer a 20 percent discount to the benchmark lending rate, the PBOC said, widening from a previous 10 percent.

Today's move signals policy makers are concerned that the cost of borrowing is crimping companies' spending and holding back expansion in the world's second-biggest economy. The State Council warned May 23 that downside risks to growth are rising and three bank officials told Bloomberg News last month that the nation's biggest banks may fall short of loan targets for the first time in at least seven years as demand for credit wanes.

"This shows the government is speeding up and strengthening its policy stimulus, which is key to stabilizing China's growth," Sun Junwei, a Beijing-based economist with HSBC Holdings Plc, said before the announcement. "The downside risks to growth continue to pose serious challenges to the Chinese economy, outweighing inflation as the top concern for policy makers."

The central bank last reduced benchmark interest rates in late 2008, when the government unveiled a 4 trillion yuan ($586 billion at the time) stimulus package to counter the effects of the global financial crisis. Interest rates have been unchanged since an increase in July 2011.

Slowdown Worsening

The PBOC cut banks' reserve requirements in November for the first time in three years, and again in February and May, to spur lending.

China's manufacturing expanded at the slowest pace in six months in May, a government report showed on June 1, adding to signs the nation's slowdown is worsening. A separate purchasing managers' index from HSBC Holdings Plc and Markit Economics pointed to a seventh straight contraction, the longest stretch since the global financial crisis.

Premier Wen Jiabao and the State Council, or Cabinet, pledged last month to place greater emphasis on stabilizing growth after data showed April industrial production, new loans and exports all increased less than economists forecast. The data prompted banks including Goldman Sachs Group Inc., Morgan Stanley and Bank of America Corp. to cut their economic-growth estimates.

Stimulus Response

Expansion may drop to 7 percent or "slightly below" this quarter from a year earlier, Dong Tao, a Hong Kong-based economist with Credit Suisse Group AG said last month. Ding Shuang, a Hong Kong-based economist at Citigroup Inc., forecast
7.5 percent. That follows an 8.1 percent expansion in the first three months of the year, the fifth quarterly deceleration.

Tao said the government may respond with a stimulus of as much as 2 trillion yuan, half the size of a package announced in late 2008 to cushion the economy from the impact of the global financial crisis.

Even so, the official Xinhua News Agency said in a May 29 article that the government has no intention of rolling out another "massive" stimulus, damping speculation of more- aggressive policies to support growth.

China's inflation has slowed this year, giving the government more room to ease policies. The consumer-price index rose 3.4 percent in April from a year earlier, the third straight month it's been below the official target of 4 percent.
The rate was 6.5 percent in July, the highest since 2008.

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