



Nota Rápida

21st December 2007

CHINA: Central bank hiked interest rates to a nine-year high

- The People's Bank of China (PBoC) raised interest rates for the sixth time this year, effective 21st December. The one-year lending rate was raised by 18 bps to 7.47%, while the one-year savings rate was raised by 27 bps to 4.14%.
- Yesterday's hike did not surprise markets which had expected a more aggressive tightening since October. The unusual move is the asymmetric change in interest rates: longer rates are hiked by smaller amounts than the short-end and by more in deposit than lending rates. Current deposit rates were trimmed by 9 bps.
- Some possible interpretations to this move: (i) the government want to make longer term deposits more attractive and thus lower the incentive to keep demand deposits where funds are readily available to shift into stocks and property; (ii) to manage inflation expectations suggesting that inflation may stay higher in the short term than in the longer term; (iii) and by cutting the demand deposits rate, to cushion the negative impact of the rate hike on banks' profitability.
- The announcement of the interest rate increase came after the People's Bank of China published the results of a survey of 20,000 depositors, 48% of whom said current prices were "overly high and hard to accept" whereas 64% of respondents said they expected prices to continue to rise next year. Another survey of 5,497 companies found they were under growing pressure from rising prices and were concerned about economic overheating. A separate PboC report on banking industry's confidence for the last quarter of 2007 showed that Chinese banks expect less demand for loans next year as compared to the previous quarters, mainly due to rising interest rates.
- In our view, the asymmetric pattern in the adjustment of interest rates might reflect the government's reluctance to hike rates, especially on the lending side and for longer maturities. We expect the rate hike cycle to be less aggressive in 2008 –due to a slowdown in external demand and a faster RMB appreciation- but still with four more hikes in both deposit and lending rates, by 27 bps on average, as CPI inflation could remain stubbornly high for more time than the government is currently anticipating.

Ya-Lan Liu

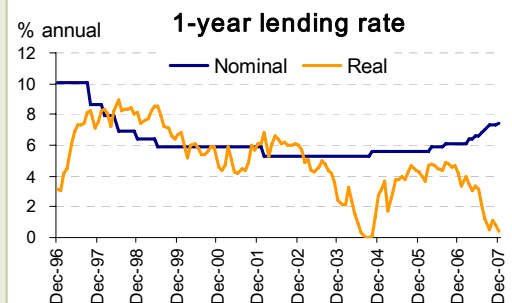
Economic Research

yalan@grupobbva.com

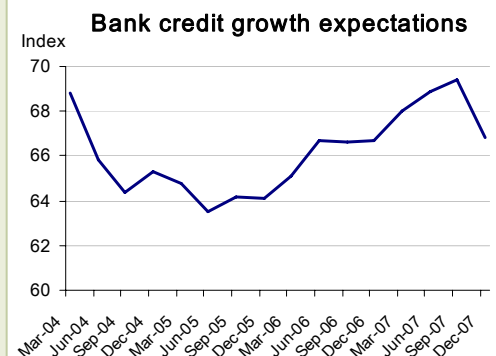
Reference interest rates

	Previous	Current	Change
Savings deposits			
Demand	0.81	0.72	-0.09
Fixed			
3 months	2.88	3.33	0.45
6 months	3.42	3.78	0.36
1 year	3.87	4.14	0.27
2 years	4.5	4.68	0.18
3 years	5.22	5.4	0.18
5 years	5.76	5.85	0.09
Loans			
Below 6 month	6.48	6.57	0.09
1 year	7.29	7.47	0.18
1-3 years	7.47	7.56	0.09
3-5 years	7.65	7.74	0.09
Above 5 years	7.83	7.83	0

Source: PBoC, BBVA



Source: Thomson Financial, BBVA



Source: PBoC, BBVA