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Rong360 Jianpu Technology Inc. (NYSE:JT) Big Data Institute: How First-ever 5Y LPR Cut to Influence Mortgage Rates?

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Rong360 Jianpu Technology (NYSE:JT)

Insights on LPR Cut

After the adjustments, loan prime rate (LPR) was lowered five basis points to 4.15 percent for one-year maturities, and the five-year prime rate was reduced five basis points alike to 4.8 percent. This was the fourth offering since introduction of the new LPR mechanism, and marked the first-ever cut of the five-year LPR.

In November, the People's Bank of China strengthened counter-cyclic adjustment, and launched a series of open market operations in succession. In the wake of the two medium-term lending facility (MLF) operations and one recent seven-day reverse repurchase in the month, interest rates were five basis points less than the previous readings. The Symposium on Monetary Credit Situation Analysis of Financial Institutions held on November 19 stressed again that China would bring the guiding role of LPR into full play and move real interest rates downwards. In this context, the said LPR cut happened just as expected by the market.

The five-year LPR, which is pegged to rate on the medium and long term lending facility, was cut based on the following two overriding considerations: First, although reforming LPR to boost reduction of real interest rates for lending to the real economy has made an initial success, the credit support for traditional manufacturing needs to be stepped up further, particularly in terms of medium and long term loans; second, the China Monetary Policy Report Quarter Three, 2019 mentioned the conversion plan for benchmark interest rates of existing loans again. The reduction of existing loan rates will have a more significant influence on the financing cost of real economy and existing loans belong to medium- and long-term loans.

Influence on Residential Mortgage Loan Rates

The cut of the five-year LPR which is generally used as a reference for mortgages will inevitably exert an influence on residential mortgages. Accordingly, the floor for China's residential mortgage loan rates is changed to 4.8 percent and 5.4 percent for the first-time and second-time home buyers, respectively.

Previously, some cities have raised the mortgage loan rates on the basis of the floor rates required by the Chinese government after the new regulation on mortgages came into force. Consequently, people with a rigid demand have to pay more for buying a home, and there is not a positive reaction from the market. Following the present cut, residential mortgage loan rates will possibly drop in the cities which have been affected largely by the floor rates (4.85 percent and 5.45 percent for the first-time and second-time home buyers, respectively) in order to ensure the local property market is stable.

But the number of such cities is small, and it is also necessary to make adjustments consistent with the general guiding principle of local property market policies. Areas where the property market is stable will not be very sensitive to the LPR cut before the end of this year. It is underlined in the China Monetary Policy Report Quarter Three, 2019 again that China will carry out the long-term effective management mechanism of real estate in line with the basic principle of “adopting measures tailored to specific local conditions” as well as the long-term management mechanism for the real estate market, refrain from using real estate as a way of stimulating economy in short term.

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