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Analysis of the Effects of Frequent Increases of the Reserve Requirement Ratio by the People's Bank of China

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“The legal required reserves system is a monetary policy that is used by central banks to perform macroeconomic adjustments. In China, the required reserves system is one of the most important policies of the People's Bank of China. In this study, using information from the Vector Auto-Regression Model and utilizing monthly data of the reserve requirement ratio (RRR), money supply, Consumer Price Index (CPI), and loan scale from January 2006 to March 2011, we quantitatively studied the effects of frequent increases in the RRR in China. We found that China's monetary policy regarding required reserves has not had a significant effect on dealing with excess liquidity, preventing inflation or controlling increases in the loan scale. We briefly analyzed the reasons for the limited actual effects of China's required reserves policy regarding the required reserves system, monetary transmission mechanism, system of forced RMB sale, and purchase of foreign exchange.”

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