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China Economics

PBoC's O/N Rate Move Points to a Likely July Cut

CITI'S TAKE

The PBoC today reportedly set its inaugural O/N reverse repo rate at 1.25% — 10bps below consensus — while holding the 7D reverse repo rate steady at 1.40% (Bloomberg, Jun 29th; PBoC, Jun 29th). The asymmetric move likely signals an easing bias, without a formal cut. A 15bp term premium between the O/N and 7D rates looks too wide compared with market rates. We maintain our out-of-consensus call for a 10bp cut to 7D reverse repo rate and LPR in 2H26, with risks skewed to an earlier move (see: 26H2 Outlook: AI Supercycle Cuts into the K-shaped Economy). We believe a *de facto* LPR cut on July 20 now looks increasingly likely. Beyond rates, fiscal acceleration — bond issuance, fund deployment, and the RMB800bn facility — is already underway. That said, we do not expect a policy pivot from the July Politburo meeting.

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What happened? – The PBoC conducted its first overnight reverse repo operation today, disclosing the injection size at RMB300bn but not the rate (PBoC, Jun 29th). Bloomberg (Jun 29th) subsequently reported the O/N reverse repo rate at 1.25% (citing people close to the matter) — 10bps below the consensus forecast of 1.35% — likely signaling an easing bias. The PBoC also conducted an operation at the 7D tenor but kept the 7D reverse repo rate unchanged at 1.40%, in line with expectations. Today's move follows the PBoC's earlier tweak on its interest rate corridor (see: Takeaways from Lujiazui Forum). Relatedly, one PBoC monetary policy committee member called for rate cuts last week (Bloomberg, Jun 24th). Reuters reported a third consecutive month of window guidance to boost loan issuance (Reuters, Jun 26th).

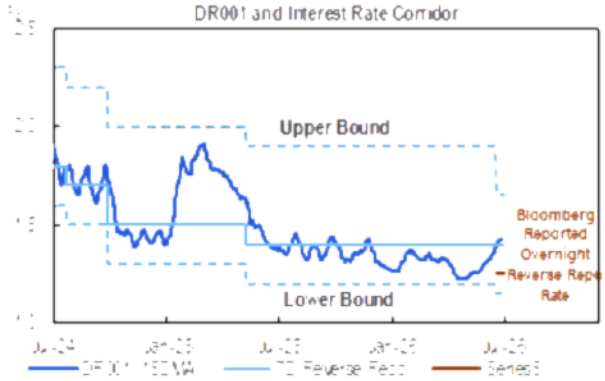
What to make of it? – The O/N reverse repo rate is still in the process of being established as a formal policy rate; the current framework remains anchored to the 7D reverse repo rate and the LPR, which move in tandem. Today's move is not an outright easing, in our view — but it likely opens the door to one. A 15bp term premium between the O/N and 7D rates looks too wide compared with market rates. We maintain our out-of-consensus call for a symbolic 10bp policy rate cut in 26H2E, premised on sluggish domestic demand. We believe the risks are skewed towards an earlier move, especially with a likely resolution of the Middle East conflict. Today's development lends further support to our view. A *de facto* LPR cut as soon as July 20th now looks more plausible — whether delivered as an outright cut under the current pricing regime, or via a structural shift toward DR-based LPR pricing. Either way, a lower LPR cut would confirm the easing direction.

What else to expect? – We believe targeted easing is coming, but a policy pivot is not. Fiscal policy deployment is the key variable and should be set to accelerate — specifically: **[1]** bond issuance, **[2]** fund deployment, and **[3]** RMB800bn policy financing tool. The bar for a budget revision remains prohibitively high, in our view, as the full-year growth target appears within reach despite a Q2 slowdown. The July Politburo meeting may underscore consumption and household income, though we see limited scope for immediate and material stimulus.

See Appendix A-1 for Analyst Certification, Important Disclosures and Research Analyst Affiliati



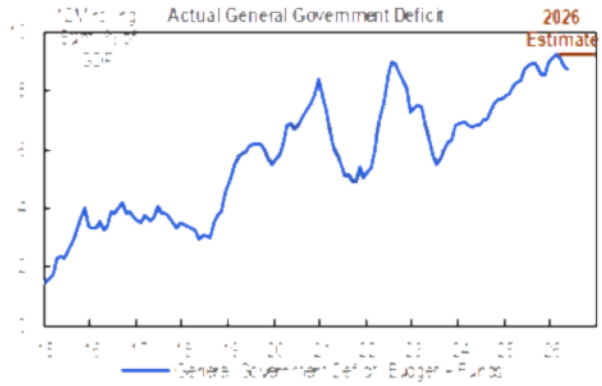
Figure 1. The PBoC today reportedly set its inaugural O/N reverse repo rate lower than expectation today



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Source: PBoC, CEIC, Bloomberg, Citi Research

Figure 2. Fiscal policy deployment is the key variable to watch for cyclical policies and should be set to accelerate



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Source: MoF, NBS, NPC, CEIC, Citi Research