

Delayed, not derailed

The likelihood of a benchmark interest rate cut this month has significantly diminished in view of China's solid economic data year-to-date. Meanwhile, construction activity remains a major drag, clouding the investment outlook this year.

Although we believe the case for two rate cuts this year remains intact, we push back the timing by one quarter and now anticipate a 10bp cut in 2Q26 and another 10bp in 3Q26. Additionally, we expect the PBoC to deploy more liquidity-easing measures, including RRR cuts and bond purchases, to anchor rate expectations at the ultra-long end and contain refinancing costs for local governments.

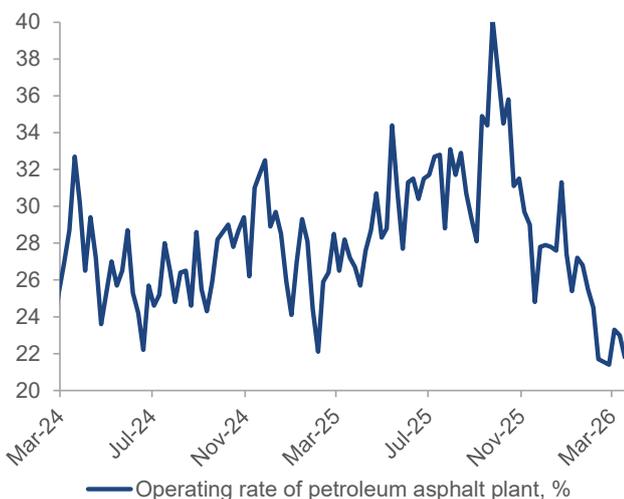
The likelihood of a benchmark interest rate cut this month has diminished meaningfully as China's data for January and February consistently surprised to the upside:

- Industrial production accelerated to 6.3% YoY, the fastest pace since September, powered by a broad-based rebound, most notably high-tech manufacturing (+13.1%).
- Retail sales rose 2.8% YoY, supported by fresh government subsidies and holiday spending.
- Fixed asset investment unexpectedly returned to positive territory at 1.8% YoY, driven by robust public-sector investment. A slower price decline in raw materials, such as ferrous and non-ferrous metal, also provided support.

Moreover, most high-frequency indicators point to steady or slightly improved activity in early March compared with a year ago. For example, the PTA factory operating rate, widely viewed as an indicator of downstream polyester demand, averaged 80% in the first two weeks of March, up from 77% during the same period last year.

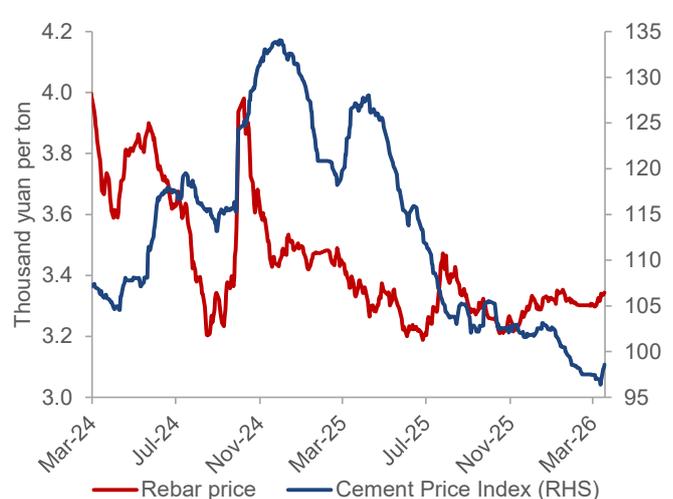
However, construction-related metrics remain a major drag even after the Lunar New Year holiday, clouding China's investment outlook. Road construction activity remains roughly 20% below last year's levels (Fig. 1), and cement prices, an important indicator to gauge construction demand, are hovering near a decade-low (Fig. 2).

Fig 1 Road construction activity has remained subdued in March



Source: Wind, Mizuho

Fig 2 Cement and rebar prices bode ill for construction demand



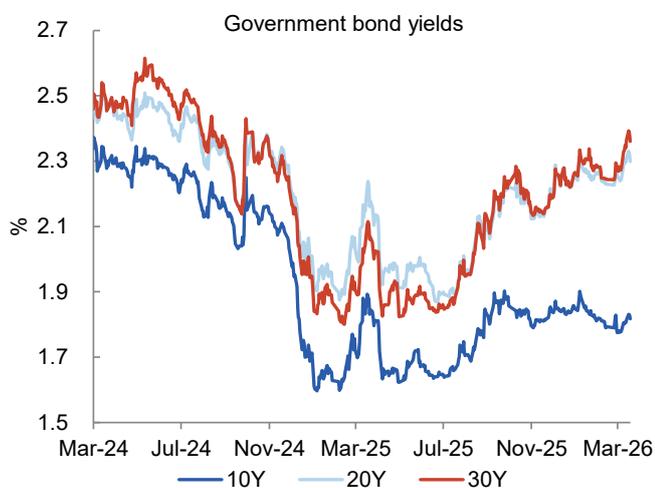
Against this backdrop, we believe the case for two rate cuts this year remains intact, with policymakers likely waiting

for a more opportune moment, particularly given China's relatively restrained fiscal stance. China is expected to issue RMB 13.89 trillion in central and local government bonds in 2026, below the actual net issuance of RMB 13.95 trillion last year. Accordingly, we push back the timing of rate cuts by one quarter in view of the solid economic data YTD and now expect a 10bp cut in 2Q26 and another 10bp in 3Q26.

In addition, we note the recent rise in ultra-long-tenor CGB yields. Earlier this week, 20-year and 30-year CGB yields reached 2.33% and 2.39%, respectively, marking their highest levels since late 2024, while movements in 10-year CGB yields were muted (Fig. 3). Beyond the RMB 1.3 trillion in ultra-long CGBs issued in 2025 and another RMB 1.3 trillion scheduled for this year, local governments are increasingly leaning on ultra-long bonds for financing. According to Wind, 57.5% of YTD local government issuance consists of maturities of 15 years or longer, up from 46.7% in 2024.

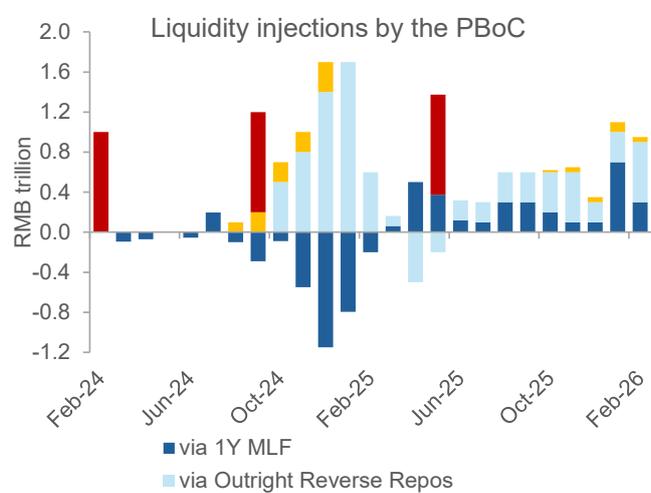
Given the substantial pipeline of such issuance, we expect the PBoC to deploy additional liquidity-easing measures, including RRR cuts and CGB purchases from the secondary market (Fig. 4), to smooth market liquidity, anchor expectations for long-end rates, and help cap refinancing costs for local governments.

Fig 3 The notable rise in ultra-long CGB yields since 2H25



Source: CEIC, PBoC, Mizuho

Fig 4 The PBoC may ramp up liquidity injections in coming months



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