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From Digital Cash to Regulated Deposit: China's Interest-Bearing e-CNY

By
Lāśma Kokina



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For information about Rosa&Roubini Associates, please send an email to info@rosa-roubini-associates.com or call +44 (0)20 7101 0718.

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- ✦ China's move to make the e-CNY interest-bearing is a targeted effort to boost adoption, not a fundamental departure from established CBDC design principles.
- ✦ By embedding the digital yuan within the two-tier banking system, the reform preserves commercial banks' central role in balance-sheet management, intermediation and customer relationships.
- ✦ A tightly calibrated framework positions the e-CNY as a regulated payments and settlement infrastructure - domestically and in cross-border use - reinforcing financial stability rather than displacing banks.

The Interest-Bearing e-CNY: Design, Adoption and Financial Stability

From Digital Cash to Adoption Tool: Why Interest Was Introduced

China's decision to allow interest payments on holdings of its digital currency, the e-CNY, marks a notable departure from the cautious orthodoxy that has shaped central bank digital currency (CBDC) design globally.¹ For years, most central banks have argued that retail CBDCs should not bear interest, largely to avoid destabilising commercial bank funding and accelerating deposit flight in times of stress.²³

China's People's Bank of China (PBOC), however, has chosen a different path. Under a new management framework announced in late 2025, interest will be paid on e-CNY balances held in authorised wallets from January 2026, with the stated aim of boosting adoption and expanding use cases.⁴ While the move has prompted renewed concerns about bank disintermediation, the institutional design of China's approach suggests those fears are overstated.⁵

The e-CNY has long been framed as a digital analogue of cash - part of the monetary base (M0), non-interest-bearing and primarily intended for payments.⁶ Despite extensive pilot programmes across major cities and use in government disbursements, adoption has remained modest relative to China's dominant private payment platforms, notably Alipay and WeChat Pay.⁷ The new interest feature is presented as a tool to strengthen incentives for everyday use and to integrate the digital yuan more fully into the retail financial ecosystem.⁸

Preserving the Two-Tier Banking System

Crucially, the introduction of interest coincides with a reclassification of how e-CNY balances are treated within the financial system. The Chinese government's release states that digital yuan held in commercial-bank wallets will be treated as bank deposit liabilities and incorporated into banks' standard asset-liability management frameworks.⁹ Rather than allowing households to hold large quantities of interest-bearing central bank money directly, China is embedding the e-CNY within the existing two-tier banking system.¹⁰ Under a two-tier system, the central bank issues digital currency to regulated intermediaries, while commercial banks remain the primary interface with households, retaining responsibility for balance-sheet management, compliance, and credit intermediation.¹¹

This design choice sharply limits the scope for disintermediation. In models that raise the greatest concern among regulators, retail CBDCs sit directly on the central bank's balance sheet, offering households a risk-free alternative to bank deposits. In such a setup, even small interest differentials can trigger large shifts in funding away from banks, particularly during periods of market stress.¹² China's framework avoids this by ensuring that e-CNY balances continue to fund banks, rather than bypass them. As one analyst put it in response to the announcement, banks are not losing deposits; they are gaining a new, regulated form of deposit liability.¹³

Risk Containment, Regulation, and International Positioning

The way interest is set further reinforces this point. According to the official plan, banks will be required to pay interest on e-CNY balances in accordance with prevailing deposit rate regulations¹⁴, with rates aligned with demand deposit benchmarks rather than set at a premium.¹⁵ This suggests the policy is designed to remove a structural disadvantage (zero yield on e-CNY), rather than to create an aggressively competitive alternative to traditional deposits. In practice, this limits the likelihood of large-scale shifts from conventional bank accounts into e-CNY wallets solely on yield grounds.

Other elements of the framework further decrease the risk of destabilising flows. E-CNY balances held with commercial banks will be covered by China's deposit insurance scheme, placing them on the same footing as ordinary retail deposits in terms of perceived safety.¹⁶ This reduces the incentive for households to treat the digital yuan as a superior safe haven in times of uncertainty. At the same time, e-CNY holdings are being incorporated into the reserve requirement calculation base, ensuring that the PBOC retains its ability to steer liquidity conditions as usage grows.¹⁷

The framework also tightens the role of non-bank payment institutions. Firms authorised to distribute e-CNY but lacking banking licences will be required to hold 100% reserves against digital yuan balances they manage.¹⁸ This prevents lightly regulated intermediaries from creating quasi-deposit products around the e-CNY that could amplify systemic risk - another concern often raised in debates about digital currency adoption.¹⁹

Taken together, these measures point to a strategy that is evolutionary rather than disruptive. The interest-bearing e-CNY represents a shift from "digital cash" toward something closer to deposit money, but without dismantling the core functions of the banking system.²⁰ This approach also aligns with China's broader ambitions for the e-CNY, including its use in cross-border settlement experiments such as the mBridge platform.²¹ Even internationally, the digital yuan is being positioned as infrastructure, not as a bank-free monetary alternative.²²

China's decision to pay interest on e-CNY holdings is therefore best understood as a targeted response to adoption challenges rather than a radical rethinking of the financial system. By embedding the digital currency within existing regulatory, balance-sheet and insurance frameworks, the PBOC has sought to capture the benefits of wider usage while containing the risks that have made other central banks wary. Far from heralding large-scale bank disintermediation, the reform shows how CBDC design can reinforce, rather than undermine, the role of commercial banks.

NOTES

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