Renminbi's growing global influence

Internationalisation of Chinese currency remains on track despite recent stalling

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During 2016, the internationalisation of the Chinese renminbi (RMB) appeared to stall in the wake of symptoms of capital flight, volatility in share markets and the overall and continuing slowdown in the Chinese economy. For example, in 2015, over 30 **per cent** of China's foreign trade was settled in its own currency. In 2016 it had fallen to 20 **per cent**. The RMB had become the **sixth-most** used currency globally in 2015 but is presently the **eighth**. There has also been a decrease in RMB deposits in **Hong Kong**, a good indicator of the currency's international profile. These are currently estimated at 3.3 trillion yuan against a peak of 4.6 trillion in 2015. Though formal regulations were not changed**,** Chinese authorities moved in to impose informal restrictions on capital outflows, with greater scrutiny of overseas acquisitions by its large corporations. The equity markets were more tightly regulated but some measures such as putting in circuit breakers to check volatility achieved the opposite and had to be abandoned.

All these developments throughout 2016 led analysts to conclude that while the Chinese authorities would loosen capital controls they would not eliminate them and this would mean that the RMB's emergence as a truly international, freely traded reserve currency was unlikely. There was also the assessment that the objective of political stability and regime survival would always trump that of a truly open and globalised market economy. As one analyst observed, "The RMB will continue to rise in global finance but don't expect it to rule."

There is no doubt that there has been stalling in the RMB's internationalisation and even some reversals, but a deeper analysis reveals a steady, **step-by-step**, pursuit of making China a global financial power with its currency taking its place as a premier financial instrument rivalling the US dollar. Here are some developments that one should take note of.

The RMB can now be traded in 15 offshore centres, including key markets across the world. London is emerging as the most important offshore centre for both RMB currency trading and for **RMB-denominated** bond issuance. China has now allowed foreign entry into its huge inter-bank bond market without prior approval and this will help create a large and relatively liquid bond market which is a prerequisite for internationalisation. The share of external holdings of **the** Chinese government's bonds now stands at 3.9**per cent** of the global total and is expected to increase steadily in the coming years. Another important development is the launch of **panda** bonds, allowing foreign entities to raise funds through **the** RMB bonds issued in the Chinese domestic market.

China has increased the number and volume of swap arrangements with central banks across the world. There are now 35 such arrangements**,** and the amount is 3.3 trillion yuans. These are important in enabling countries to bypass the US dollar in financial transactions. They played an important role in helping Russia deal with the sanctions imposed by the West in the aftermath of the Ukraine crisis when Russian companies were cut off from international banking where the US dollar still reigns supreme.

China has made systematic efforts to diminish the American hold on global financial and currency markets but these have not received the attention they deserve. The Chinese **UnionPay** was launched as early as 2002 as an alternative to **US-owned** credit card payment schemes such as Visa and MasterCard. Over the past few years, the **UnionPay** logo has become more ubiquitous on ATMs throughout the world. Wherever international credit cards have been compelled by the US government to stop international payments, as was done recently with Russia, the Chinese alternative has become more attractive. Furthermore, in the same direction, the Chinese have established the International Payment System (CIPS) or their own international payments gateway with the objective of establishing some control over financial transfers globally. At present, the American SWIFT network is indispensable to effecting such transfers among banks, but with the CIPS China seeks to challenge that monopoly, A trial run has been instituted with Russia and an MoU has been concluded with SWIFT itself to build this into an efficient and convenient alternative gateway. These moves ride on the sheer size of the Chinese economy, the fact that it constitutes 16 **per cent** of world GDP and 13 **per cent** of global trade in goods and services.

A mention should be made here of the various financial **free-trade** zones which have been set up to promote financial liberalisation. but under controlled conditions. The Shanghai FTZ**,** which was set up on the basis of a negative control list**,** has been able to develop as a successful international financial and banking centre. The experience gained here has enabled 11 such centers to be set up just in the past **two** years alone.

Clearly, temporary challenges are not holding up the **long-term** plan from proceeding ahead.

The ambitious Chinese One Belt One Road (OBOR) initiative has a significant bearing on the internationalisation of the RMB. One of its stated objectives is the "financial coordination" among participating countries. The OBOR could become an important platform for promoting the use of the Chinese currency in trade settlement among these countries just as it is Chinese financial institutions which will play a major role in financing the various infrastructure projects planned under the initiative. As a senior Chinese banker observed, **"We** will support more infrastructure projects from the Chinese side. Many countries along the route will be willing to accept RMB as a trading currency." Another Chinese official stated that "The internationalisation of the RMB is practically an essential part of the China's OBOR initiative. It will pave the way for capital flows, trade and **people-to-people** exchanges."

It may also be noted that three institutions which India is a part of, namely the Asia Infrastructure Investment Bank, the BRICS Development Bank and now the Shanghai Cooperation Organisation (SCO) are all expected to play a critical role in the unfolding of the OBOR. Financial coordination is one of the stated objectives of the SCO. How should India formulate its own role in these platforms is a matter which needs careful and well-researched deliberation**?** Do we ride on the Chinese challenge to the West-dominated global financial and monetary system or are our interests better served by resisting it? Does India itself have ambitions to become a major player in the global financial market? Not confronting these issues will inevitably lead to a default result, that is, a growing Chinese influence on the global financial system which itself is a component of China's larger geopolitical ambition.

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