

# Internationalization of Renminbi as A Response of China's Economic Development

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**Abstrak**-Tulisan ini mencoba untuk mempelajari internasionalisasi Renminbi sebagai ambisi Tiongkok dalam mendukung perkembangan pesat ekonominya. Dalam beberapa tahun terakhir, penggunaan Renminbi dalam perdagangan internasional terus mengalami perkembangan. Penggunaan Renminbi oleh banyak Negara mendorong Renminbi untuk bergabung dalam keranjang mata uang internasional. Internasionalisasi mata uang harus sesuai dengan status ekonomi suatu Negara dalam percaturan ekonomi global. Hal ini tergantung pada tingkat pertumbuhan ekonomi suatu Negara dibandingkan dengan tekanan eksternal yang ada. Setelah bergabungnya Renminbi dalam keranjang mata uang internasional, muncul pertanyaan apakah ekonomi Tiongkok dapat mempertahankan perkembangannya meskipun tingkat pertumbuhannya mengalami tren menurun dalam beberapa tahun terakhir?. Sementara itu, internasionalisasi Renminbi memberikan manfaat dan menimbulkan kekhawatiran politik. Manfaat bagi Negara ASEAN, internasionalisasi Renminbi akan menghilangkan biaya tambahan dan resiko nilai tukar. Akan tetapi, bergabungnya Renminbi dalam keranjang mata uang internasional menimbulkan kekhawatiran politik akan mempengaruhi kemampuan Barat dalam menjatuhkan sanksi ekonomi dan meningkatkan pengaruh politik Tiongkok.

**Kata Kunci:** Internasionalisasi, Renminbi, Ekonomi, Tiongkok

**Abstract**-This paper is aimed to study the internationalization of Renminbi as the ambition of China in supporting its economic rapid development. Over the last few years, use of Renminbi for international trade has been growing steadily. The use of Renminbi by more countries encourage Renminbi to be involved in International currency basket. The internationalization of a currency should match with a country's economic status in the global economy. It's depend on growth rate of country's economic rather than external pressures. After the joining Renminbi in the international currency basket, the question arises will China's economy maintain its development despite its growth rate experiencing the decreasing trend in recent years? Meanwhile, the internationalization of Renminbi provides benefits and raises political concern. The benefits for ASEAN countries, will eliminate the additional cost and exchange rate risk. But the joining of Renminbi in international currency basket raises political concern will affect to the ability of West in imposing economic sanctions and enhance China's political influence.

**Keywords:** Internationalization, Renminbi, Economic, China

## 1. Introduction

The basic conception of currency internationalization illustrates how country's currency is accepted as cross-border settlement medium in cross-border transactions among countries or other actors such as organizations and multinational corporations (Subacchi and Huang: 2012).

On 1 October 2016, Renminbi (Chinese Yuan, or CNY) is officially accepted as a part of IMF's SDR (Special Drawing Right) basket of currency. Renminbi has approved as the fifth currency in the Special Drawing Rights (SDR). According to the International Monetary Fund review in 2016, the share of each currency in SDR basket are US Dollar (41.73%), EU Euro (30.93%), Japanese Yen (8.33%), British Pound (8.09%), and China Renminbi coming in for the first time at (10.92%). Renminbi now is considered as one of the five reserve currencies of the world together with the US Dollar, the EU Euro, the Japanese Yen, the British Pound.

Internationalization of Renminbi had already popularized as the research topic over 15 years ago. Some Chinese economist at that time proposed this topic to become a study. In the terms of Implementation, the road to internationalize Renminbi had began in 2004 when banks in Hongkong started to accept Renminbi deposits.

In 2007, Renminbi bonds in Hongkong began to be marketed after Chinese government allowed financial institutions in issuing Renminbi bonds in Hongkong. This marks the early stage of Renminbi become (international) capital investment medium.

The next period of Renminbi Internationalization continued in 2009, when more enterprises in China started to use Renminbi in cross-border trade settlements with its major partners (Hong Kong, Macau, Taiwan, and ASEAN countries) on a trial basis. This step is aimed to increase the quantity of Renminbi overseas.

In July 2010, the People's Bank of China (PBOC) signed a new settlement agreement with the Hong Kong Monetary Authority allowing free flows of the Renminbi between individual and enterprise accounts. This helped to invigorate the whole market. Meanwhile, the central Chinese government also clarified Hong Kong's position as an offshore center of the renminbi.

In early stage of Renminbi Internationalization process, some researchers had underestimated with the ability of Renminbi becomes international currency (Dobson & Masson,2008; Orastean, 2013). They argued Renminbi has none characteristics of international currency. Because at that time, Renminbi was not used for invoicing export and import, and also was not circulated beyond border of China.

Sheldon (2009) noted the internationalization of Renminbi has been forecasted before after China becoming the world's second largest trading nation in 2008. The main constraint of Renminbi to be used widely in few years ago is the restrictions of the Chinese authorities and the under development of Chinese financial market.

The reason Renminbi to be involved in the international monetary system is there an international need for more currencies in SDR basket of currencies and the Renminbi is considered positively could reach all this purpose.

On the other hand, the reason also lies in the rapid development of China's economy over the past 30 years. The Chinese economy is still developing although it is slowing down during last several years. The Chinese GDP grew at 6.7 per cent in the second quarter of 2016, with its GDP reaching 10.86 trillion US Dollars and becoming the second largest economy in the world. The GDP of China represents 17.53 percent of the world economy. Meanwhile, China has the largest foreign exchange reserves and the second largest trade volume in the world.

## **2. Methods**

This paper used qualitative approach. Qualitative approach used to produce descriptive data. The descriptive data describes or portrays information on the facts, characteristics and the relationship between the investigated phenomenon in a systematic, factual and accurate.

In this paper, the author used the literature review method or library research. The data obtained in this paper is secondary data from books or literature, relevant literature, documents, notes, journals, results of previous research, academic writings contained in books, newspapers, internet, as well as information from other printed media. In addition, this study also cited several theories, concepts and expert opinion as a basis for discussing simultaneously analyzing the problems in research.

### **3. Result and Discussion**

#### **3.1. Theoretical Review**

Orastean (2013) mentioned the international currency is a currency used within and outside the issuing country. The internationalization of Renminbi means encourage the using of Renminbi outside China and allowing non-residents to use Renminbi extensively in international transaction and use it as a currency for routine payments, settlements, investments, and reserves.

International currency is not only used in the transaction among resident of the country, but also used in the transaction between the resident and non-resident outside the country. As the international currency, Renminbi will widely used in international trade across country.

According to Hiroyuki (2016), the IMF sets two requirements for currency to be able involved in the SDR basket: the country has to be one of the largest exporters in the world, and its currency must be freely useable in the market.

When a country's currency is accepted as a medium of exchange between countries, its status becomes an international currency. The main characteristics of the international currency is can be used and stored outside the territorial of the issuing country, and can facilitate transactions between residents and non-residents of other countries. There are at least three dimensions of international currencies, ie the unit of account, medium of exchange and store of value (Kenen: 2009).

Renminbi in the past few years is growing importance in the international monetary system as a new alternative in doing international trade worldwide. Long years ago, China started its pilot program to promote Renminbi used globally. And after a decade of its efforts, Renminbi accepted by IMF as one of SDR basket currency. It indicates that Renminbi represent China's economy in playing significant role in global economy. The internationalization of a currency should depend on a country's inherent growth rate of economic development rather than external pressures.

#### **3.2. China's Strategy in the Internationalization of Renminbi**

For several years, China's government has taken a number of initiatives to promote international use of Renminbi. The major partners of China in promoting Internationalization of Renminbi are Hongkong, Macau, and ASEAN countries.

China's main purpose in internationalization of Renminbi is to create a stable international monetary environment which promotes its own economic development (Edwin L. C. Lai: 2015). After considered as one of leading nation in economic development, China started to set up the long term strategy to dominate global economy by promoting Renminbi as international currency.

China has taken the following strategies to popularize Renminbi abroad: First, encouraging the use of the Renminbi in cross-border trade settlement. China shares borders with 14 neighboring countries, and there is cross-border trade at each border. It reach 80% of the volume of these cross-border trades is settled in Renminbi because most people are willing to use Renminbi for cross-border settlement.

Second, China signed a free-trade agreement with ASEAN. According to this agreement, 95% of trade between China and 10 ASEAN member countries is free tariff, the trade volumes are on the rise in both directions. In addition, many ASEAN countries accept Renminbi as the trading currency for transactions with China. They are using Renminbi for settlement more and more frequently.

Third, according to the data released by People's Bank of China (PBOC), China has signed currency swap agreements with 31 countries since 2008. Currency swap agreement allowed each country to use their own currency in making international trade. it means China can purchase counterparty's resources and products in their local currencies and counterparties can purchase China's resources and product in Renminbi without involving US Dollar as medium exchange.

#### **3.3. The Driving Factors in Internationalization of Renminbi**

An unexpected development in internationalization of Renminbi in recent years is the significant increase in the use of the Renminbi as a reserve currency by foreign central banks. This is not only a reflection of China's economic strength but also a result of the weakening status of traditional reserve

currencies, particularly the US Dollar and Euro. This implies that efforts to expand the use of the RMB will also be influenced by changes in preference for the US dollar.

Another important driving factors in internationalization of Renminbi is the participation of China's authorities in making continuous reform for its financial market system and gradually relaxing capital controls and support independent monetary policy.

Ito Hiroyuki (2016) noted the internationalization of Renminbi has made significant progress in fundamental economic reforms such as large scale privatization and the downsizing and consolidation of state owned enterprises (SOEs).

The reason behind involving Renminbi in the Special Drawing Rights (SDR) by IMF has clearly served as a progress of the latest reform measures the People's Bank of China (PBOC) has adopted. It will also help keep the internationalization of Renminbi program on track.

President of China Xi Jinping said (November, 2016) the new status of Renminbi will improve the international monetary system and safeguard global financial stability. China maintains heavy regulatory control over the country's financial system. The country also falls short in legal protections, with the Communist Party continuing to play a strong role in deciding court cases.

In some cases, China doing international trade with its trading partner using Renminbi as a medium of transactions payment. Regarding with invoicing, Tavlas and Ozeki (1992) pointed out that the invoicing practices in international trade provide a stimulant for the internationalization of the country's currency.

In international trade, the determining factor in the invoicing practice is the contribution of a country's exports to the world's exports. When currency referred to as a store of value, financial stability and macroeconomic determine a currency can be used as a store of value. In addition, the high GDP growth and low inflation both are important consideration of the country's currency can be used as the foreign exchange reserves of other countries. Some countries have kept the Renminbi as their reserves. The following is the figure of Foreign Reserve and China's Balance of Trade.



Figure 1. China Reserve and Balance of Trade  
Source: National Bureau of Statistic – China

### 3.4. Benefit from Internationalization of Renminbi for ASEAN Countries

The internationalization of Renminbi provides benefits on ASEAN countries. Trade cost between China and ASEAN countries has been lowered due to the internationalization of Renminbi. Internationalization of Renminbi eliminates the additional cost caused by exchange risk and allows the two parties to remove the third foreign currency but use Renminbi directly in transaction. The financial

institutions and the enterprises in ASEAN nations are encouraged to enlarge their business cooperation with China as they accept Renminbi to be used in their settlement with China.

In general, the benefits of internationalization of Renminbi for ASEAN countries are to stimulate growth of trade between China and the ASEAN countries. The ties between China and the ASEAN countries are to be strengthened with increase of cooperation and business interactions.

ASEAN countries enjoying the internationalization of Renminbi because they ensure the stability of Renminbi as trading currency. It's in accordance with the statement of the former Indonesian Trade Minister, Thomas Lembong "the internationalization of Renminbi gives tremendous advantage to ASEAN member states that use the greenback as their trading currency". ASEAN countries would not be affected with US Dollar appreciation. The Renminbi should therefore be used in our ASEAN trading system and in all transactions with China.

The admission of Renminbi as international currency will be favorable to ASEAN local companies to conduct trade activities with China. The admission of Renminbi in the SDR currency basket will make the exchange rates of Renminbi against US Dollar and other currencies more stable. Meanwhile, the internationalization of Renminbi will also boost global trade and economic growth of its major partner.

### **3.5. Political Concerns in Internationalization of Renminbi**

In the internationalization of currency, politics can play its role both indirect or direct. Politics can impact indirectly in the internationalization of currency when it use economic determinant to influence international use of a country's currency. In the other hand, politics also determine the confidence value of the currency in order to be used by other countries as reserve currency. When a country has stability in security and politic, it will increase its function as store of value.

Furthermore, politics can impact directly in the internationalization of currency when policymakers of the country use its political power in encouraging other country to use its currency internationally. The policymakers of the country promote the international use of currency using their diplomacy toward counterparty.

As the Renminbi becomes widely used in the global economy, arise a concern it will impacts the ability of the West country to impose economic sanctions to countries suspected with human rights abuses and other violations. This concern arises because China has closer economic relations with the adversary country. The suspected countries, they have more choices to do international transaction in Renminbi. Christopher Brummer said after the inclusion of Renminbi in international currency basket, countries will have more choices about where they do their banking and how to potentially circumvent sanctions.

The more political wrangles in West country erode economic confidence from its counterparty. It gives more scope to China to extend its political influence and economic determination toward countries that rely on West country in order to change their direction to China.

It will become balance of power in global economy. Because up to now the unipolar world still dominated by West country. Even though after suffering economic crises in 2008, the West country has not recovered yet. China finds its momentum to be counterbalance and savior of global economy.

### **3.6. Will China's Economy Maintain its Development despite its Growth Rate Experiencing the Decreasing Trend in Recent Years?**

Petr Mozias, an economist from the National Research University's High School of Economics pointed out that China's economy predicted can maintain its growth with a focus on innovation and consumption while shifting away from large-scale exports supported by cheap labor during the decreasing of export volume.

There was a rise in business confidence and industrial output in the first quarter of 2016, which indicates that the Chinese economy might stop slowing down, or even accelerate in the coming months. China's services sector is developing rapidly and has overtaken the processing industry in economic growth, which in turn has pushed up people's incomes and private domestic demand.

As a large country, China can achieve sustainable economic development and tap the enormous possibilities in domestic demand. The rate of economic growth in China remained one of the highest in the world.

China rose to the top in international trade in recent years. It was natural for the Renminbi to become much more widely accepted in the trading of goods and services. Up to now, China still remain the second largest trading nation in the world. And it will maintain China's economic development until the coming few years.

The China's efforts in the internationalization of Renminbi are quite understandable given the rapid rise of China's economic size. Long term goal of China in Renminbi internationalization is promoting Renminbi as the dominant invoicing, investment, and reserve currency in the world replace US dollar.

#### **4. Conclusion**

China's government indicates its desire in the internationalization of Renminbi to further push economic reforms. They fully committed to the liberalization of the financial market. In the sense that the China's economy will continue to rise in the future, and that the country will continue to be a major trading country in the world.

For ASEAN countries, the admission of Renminbi as international currency will be favorable to local companies to conduct trade activities with China. Internationalization of Renminbi eliminates the additional cost caused by exchange risk and allow the two parties to remove the third foreign currency.

Internationalization of Renminbi rises a concern it will impacts the ability of the West country to impose economic sanctions and gives more scope to China to extend its political influence and economic determination toward countries that rely on West country in order to change their direction to China.

China can achieve sustainable economic development and tap the enormous possibilities in domestic demand. Recently, China still remain the second largest trading nation in the world. And it will maintain China's economic development until the coming few years.

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