



CHINA'S RENMINBI: IT'S HIGH TIME FOR DECISIVE ACTION

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If headlines translated into trading volumes and influence, the RMB would be well on its way to dominating the world's currency markets.

China is the world's largest trader and is on track to surpass the United States as the world's largest economy. Despite its recent slowdown, it is still the largest contributor by far to global economic growth.

So, as China takes its place as the biggest economy on the globe, will its currency, the Renminbi (RMB), become the most widely used international currency as well?

If headlines translated into trading volumes and influence, the RMB would be well on its way to dominating the world's currency markets. It graces the front page and business headlines consistently - and with good reason.

The RMB has vaulted ahead of the euro and Japanese yen to become the second most widely used currency in international trade finance. In 2013, companies used China's currency for 8.7% of all credit agreements tied to global trade, up from 4.4% a year earlier, according to SWIFT, which monitors international currency flows.

This puts the RMB well ahead of the euro (6.64%) and the yen (1.36%) but still far behind the US dollar which backs 81.1% of global trade finance.

The adoption of RMB for trade is reflected in the rising importance of the RMB in global foreign exchange markets, rising in rank from 17th position in 2010 (with a negligible 0.9% share)

to 9th at the end of 2013 (with a 2.2% share). In volume terms this is significant growth for the RMB, but the US dollar is still by far the most traded currency, with an 87% share.

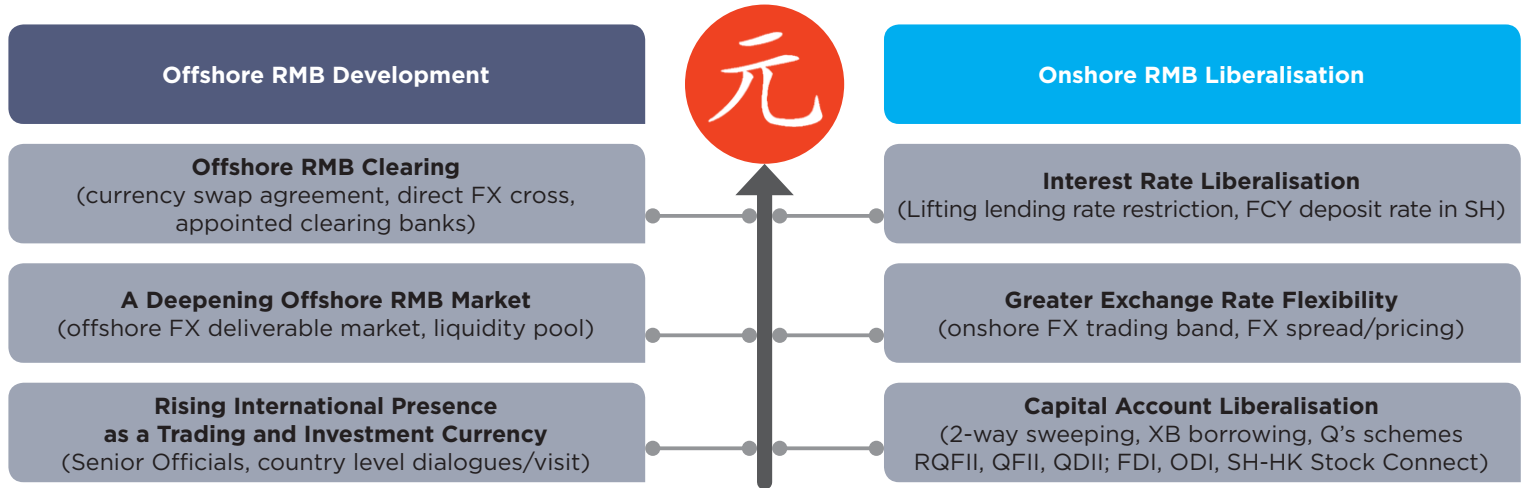
A third measure of the rising use of RMB is its use as a payment (or trade settlement) currency. The RMB now ranks 7th position, up from 35th less than four years ago. Despite this increase, the currency still holds a relatively modest 1.5% share of overall global payment flows, according to mid 2014 data from SWIFT. One explanation of why the RMB's role in overall payment lags its role in trade finance is that Chinese companies may be using RMB denominated Letters of Credit finance as way to borrow money more cheaply offshore.

While the rise in RMB globally is significant and points to the RMB's evolution from a trade settlement currency to a trade finance and treasury management currency, it will not be a true global currency until it is fully convertible.

Chinese government policies and regulatory reform have supported this ambition. Over the past decade, we have witnessed the complete opening up of cross-border RMB trade settlement and the proliferation of offshore RMB-denominated (dim sum) bond markets.

The launch and expansion of inbound and outbound investment programs for institutional investors are acting as a catalyst for market participants to use the RMB not just for trade

FIGURE 1: DEVELOPMENT IN RMB INTERNATIONALISATION



Source: Standard Chartered Bank

settlement but also for investment, asset allocation and diversification.

The list keeps getting longer, with the latest additions being the inception of the pilot Free Trade Zone in Shanghai and the launch of the Shanghai - Hong Kong Stock Connect allowing mutual access between the stock exchanges in Shanghai and Hong Kong.

Such developments come against a broader backdrop of growing market confidence and deeper financial market integration. In November 2014, Sydney joined London, Singapore, Frankfurt and a small number of other international financial centres where RMB transactions can be settled directly, confirming Sydney's status as an official offshore RMB hub.

What's driving the RMB rise? Two key factors lie behind the currency's continued advance.

The first is China's determination to use on-going financial reforms to pursue its national goal of growing a broader based consumer economy. A determination to internationalise the RMB as a means to economic growth goes hand in hand with the liberalisation of interest rates, the widening of the RMB trading band, the growth of the bond market and the development of a stronger institutional, regulatory and legal framework.

Second, there are commercial benefits to be gained from settling obligations of Chinese

enterprises in RMB. Today, companies around the world are using the RMB to achieve better terms of trade with China and more effective treasury management of China-related cash pools.

In addition, for foreign companies with a growing presence in the country, adopting the RMB enables them to self-fund investments and/or expand their market share with greater flexibility than if they had to raise RMB from the market.

SWITCHING TO RMB

Of course, as with any new initiative, there are challenges, including tax, legal, and operational issues that have prompted some companies to delay their full participation until some of the uncertainties are resolved.

The adoption of a new currency is not an easy task requiring Corporate Treasurers and Chief Financial Officers to assess the scope and cost of a move to RMB, as well as determining how precisely RMB can be leveraged to the benefit of their organisation.

Critical to this assessment is the fact that the internationalisation process is a policy driven initiative linked to China's overall development goals. This requires a clear understanding of the RMB's policy driven trajectory and the multi-faceted legal, regulatory and operational environment.



The launch and expansion of inbound and outbound investment programs for institutional investors are acting as a catalyst for market participants to use the RMB not just for trade settlement but also for investment, asset allocation and diversification.

FIGURE 2: KEY CONSIDERATIONS FOR RMB INVOICING



Source: Standard Chartered Bank

For example, while the RMB is a single currency, FX controls and regulations mean companies need to separate RMB funds into two distinct onshore and offshore pools. In practical terms, this means treating RMB as two currencies: CNY (renminbi held onshore) and CNH (renminbi held offshore).

Companies need to make every effort to stay abreast of regulatory developments. All of the major banks (local, international and Chinese) operating in Australia and legal and accounting firms with strong China capability are well placed to provide education and consultative support.

A recurrent theme in surveys undertaken over the course of the last two years in Australia is the importance of internal engagement and buy-in to an RMB strategy. Ensuring that in-house operations and thinking are aligned across all parts of the organisation is a vital consideration.

There is also the more practical question of technology. Corporates will need to upgrade their treasury and accounting systems to make them RMB-ready. The good news is that developments at the market level such as the new RMB settlement platform set up by ASX/Austraclear and Bank of China and the new RMB Clearing Bank arrangements in Sydney plus other policy initiatives put Australian corporates in a strong starting position.

USING RMB FOR COMPETITIVE ADVANTAGE

Understanding all these changes is undoubtedly a challenging task and carries with it an element of risk. For many, there is a tendency take a reactive approach and neglect market trends. They are stuck in the rut of thinking that the western focussed market will remain dominant.

With the rise of the RMB and importance of Chinese companies to global supply chains set to continue, such hesitant companies run the risk of losing business as the ability to settle in RMB becomes not only a competitive advantage but a minimum requirement.

RMB is already a major trade finance and trade settlement currency. The continued breakdown of onshore/offshore barriers heightens the RMB's use and importance as a treasury management currency. And ongoing financial reform and capital markets expansion mean the RMB's progress as an investment currency is picking up pace.

Although still far from being an international currency comparable to the US dollar or euro, Australian companies should be paying close attention to these developments. The use the RMB is fast becoming both an immediate competitive advantage and vital to future strategy for companies with any form of commercial exposure to China.

ABOUT THE AUTHOR

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