"Hurry Slowly": the maiden journey of renminbi

Considering the fact that renminbi only began its maiden journey from local circulation to an emerging currency for international trade settlement, cross-border investment and foreign-reserve management less than four years ago, the achievements of renminbi have truly been impressive.

According to the “Report on the Execution of Monetary Policies of the People's Republic of China of 4th Quarter of Year 2011” issued by the People's Bank of China (PBOC), “the amount of cross-border trade transactions denominated in renminbi in 2011 has sharply expanded 3.1 times compared to the previous year to reach CNY 2.08 trillion”\(^1\). At an aggregated basis, the total aggregate amount of renminbi trade settlement has reached CNY 2.59 trillion within two and a half years and approximately 8.9 per cent of China’s total export–import (EXIM) trade has been re-denominated to renminbi\(^2\) in the fourth quarter of 2011 (Figure 9.1).

Apart from trade settlement, the footprint of renminbi has also spread to offshore trade finance, investment and wealth-management market. As at January 2012, there are more than CNY 575.9 billion offshore renminbi deposits in Hong Kong (Figure 9.2). The amount of offshore renminbi bond (commonly known as “dim-sum” bond) issuance in Hong Kong surpassed CNY 104 billion; while more than 870 overseas banks and financial institutions have opened up renminbi agent bank nostro accounts in Hong Kong to facilitate international trade settlement and investment activities denominated in renminbi.\(^3\) Meanwhile, major international financial centres such as London, Tokyo and Singapore are eagerly jumping on the bandwagon to establish a renminbi offshore centre; while the Japan, Malaysia and Nigeria governments have announced
their intention to increase their holdings of renminbi-denominated bonds in their foreign-exchange reserves.

Yet, the journey for internationalization has never been a smooth ride – it is a path of “hurry slowly.” The Chinese government faces a policy dilemma: on the one hand, the internationalization of renminbi plays an essential role in the sustainable and steady development of the Chinese and global economy; while, on the other hand, the liberalization of the “People’s Currency” (especially relaxation of capital-account controls) may also lead to the contagion of risk into the developing financial markets of Mainland China.

To manage this “double-edged sword” and benefit from the best of both worlds, the Chinese government has undertaken a series of unprecedented, yet effective, policies to create an offshore market for renminbi in Hong Kong acting as a “testing bed” for offshore market participants to conduct trade settlement, financing, investments and wealth-management activities “applicable to the businesses conducted in other foreign currencies... as long as these businesses do not entail the flow of renminbi funds back to the Mainland.”

To safeguard against the contagion of risk back into the onshore market, the repatriation of renminbi to Mainland China has been restricted to:

(a) current-account items (i.e. cross-border trade settlement) closely monitored by People’s Bank of China (PBOC) via its Renminbi Cross-Border Payments Management Information System (RCPMIS), which also involves cross-checking with China Customs Online System to ensure the authenticity of cross-border transactions; and
(b) authorized capital-account items with regulations governing the eligibility of offshore participants, the scope of activities and the quota for repatriation managed at both a market-wide and individual-participant level.

“One currency, two systems” regime of renminbi

Paradoxically, the aforesaid “dual-track” arrangements of the deep liberalization of current-account items and the limited opening of capital-account items have naturally led to a “one currency, two systems” regime with the partial segregation of the onshore renminbi market (commonly known as the “CNY” market) and the offshore renminbi market (commonly known as the “CNH” market).

Under the current regulatory regime of Mainland China, both the onshore exchange rate and interest rates are governed by the “visible hands” of PBOC. As for onshore exchange rate, PBOC adopts a “managed float” approach where the “middle rate” of onshore renminbi against