

RMB Internationalization Based on the Perspective of the Belt and Road

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ABSTRACT

This paper mainly expounds on the motivation of RMB internationalization and the mutually beneficial relationship between the Belt and Road Initiative (BRI) and renminbi (RMB) internationalization through literature collection. As China's economic power and voice grow, the yuan also needs a place in the world monetary system. The inclusion of RMB into SDR is a sign of recognition by the world monetary system. However, the RMB is expected to become a successful regional and even international currency through the deepening cooperation between the Belt and Road and countries along the routes.

Keywords: RMB internationalization, BRI, World Currency

1. INTRODUCTION

The main motivation for the Chinese government's determination to internationalize the renminbi was triggered by the 2008 world financial crisis. The current world monetary system is based on the Jamaica system after Bretton Woods. This system is more diversified than the Bretton Woods system, but it still takes the DOLLAR as the dominant world monetary system. The Jamaican system still faces the risk of a potential financial crisis caused by the Triffin problem. For The Chinese government and enterprises, after the successful internationalization of RMB, China can enjoy seigniorage dividends. Chinese enterprises can enjoy more efficient international trade.

The Belt and Road Initiative will encourage more projects to use the yuan as a settlement currency and expand its use in the international market. Direct investment can promote international technology, capital, and material factors of production, increase the speed of the use of RMB between countries, form the mechanism of RMB cross-border circulation, and help improve the investment value of RMB.

However, the risks of financial cooperation in the BELT and Road Initiative also need to be noted. On the other hand, against the background of anti-globalization, there are uncontrollable factors in China's BRI project and the goal of RMB internationalization. Risks and opportunities coexist. The Belt and Road Initiative aims to build a community of shared interests featuring

political mutual trust, economic inclusiveness, and cultural inclusiveness. Therefore, the development and improvement of the Belt and Road can help RMB realize internationalization. The RMB is expected to gradually become the main settlement currency in countries and regions along the Belt and Road. Further, the increase of RMB's direct outbound investment in BRI also contributes to the increase of RMB's overseas liquidity. Finally, the RMB is expected to become the reserve currency of all countries through the Belt and Road projects, as the recognition of the RMB increases. The international status of the RMB will also be enhanced through the deepening cooperation among countries in the Belt and Road.

2. THE CAUSE OF RMB NATIONALIZATION

China is the world's largest trading nation and the second-largest economy. It is fair to both China and the world to promote the internationalization of the RMB in the Belt and Road Initiative. On the other hand, with the increase of RMB's international influence, more and more countries believe that the "Jamaica System" is not the only world monetary system [1]. At present, the currencies of the RMB are inversely proportional to its geographical distance from China, which means the RMB is currently more of a regional currency [2]. The Belt and Road project provides a practical platform for RMB internationalization. The Belt and Road initiative

requires long-term and stable capital input, which is conducive to the export of RMB under the capital account and the repatriation of RMB through cross-border trade under the current account. Furthermore, the Chinese government plans to help the yuan become a settlement currency, investment currency, and reserve currency through the Belt and Road initiative, thus achieving its goal of internationalizing RMB.

2.1. World monetary system

It is widely accepted that the world monetary system began when Britain went on the gold standard in 1717. With the development of globalization over the centuries, the world monetary system has also experienced different periods, and in the process of continuous development has become more and more diversified. The current Jamaica system is a new one following the end of the Bretton Woods system. The system still regards the dollar as the leading currency in the international monetary system. However, compared with the Bretton Woods system, the international standard and international reserve currency status of the dollar was weakened.

Multi-currency is regarded as the trend of the future international monetary system. The international monetary system faces three possible development scenarios: one is to maintain the status quo of dollar-centric, which will make financial crisis inevitable because of the Triffin dilemma; The second is to establish an international currency dominated by Special Drawing Right (SDR), but the international currency dominated by SDR does not have the possibility of practical use in the short and medium-term. Third, establish a multi-currency system [3].

With the rise of China's international status, the RMB, which is more stable than the US dollar, has come into the eyes of more and more people. The establishment of a diversified world monetary system cannot be separated from the entry of RMB. Nor would a new system with the yuan necessarily replace the existing Jamaican system. Two or more world monetary systems may coexist in the future. A pluralistic world is hardly dominated by a single currency. Inclusiveness and openness are the way forward.

2.2. The importance of RMB internationalization

After the 2008 financial crisis, The Chinese government was determined to accelerate the internationalization of the RMB. This is mainly because the Chinese government sees a potential financial crisis in the current monetary system. As China's international influence and economic level improve, it is in China's interest to promote the internationalization of the RMB.

On the other hand, the seigniorage dividend from the successful internationalization of the RMB is also attractive. The internationalization of the RMB would also help China conduct international trade more efficiently and reduce costs.

2.2.1. Seigniorage bonus

The most direct and biggest benefit after RMB internationalization is the income from international seigniorage. Seigniorage is the difference between the face value of a banknote issued and the cost of the banknote issued by the issuer for the privilege of issuing the currency. Issuing a world currency is the equivalent of collecting seigniorage from other countries, and the benefits are almost cost-free [4]. China will enjoy seigniorage dividends after the RMB is widely accepted as a reserve currency around the world. However, given the peculiarities of China's domestic political system, the RMB is unlikely to become the leading reserve currency in the next few years [5].

On the other hand, as of September 2021, China held more than \$3.2 trillion in foreign exchange reserves. Most of the reserves amount to huge unpaid loans to foreign governments, while the Chinese government is also responsible for its inflation-induced depreciation. After the internationalization of the RMB, China can not only reduce the loss of wealth caused by the use of foreign exchange but also obtain income from international seigniorage. The internationalization of the RMB has helped to widen China's access to capital.

2.2.2. Good for international trade

Since China joined the WTO in 2001, its trade relations with the rest of the world have greatly strengthened. In terms of the utilization rate of RMB, expanding the development of the capital market is conducive to improving the influence of RMB and promoting the internationalization of RMB [6]. Chinese enterprises can effectively reduce trade costs in international trade in which the RMB is used as the settlement and measurement currency [7]. In a way, RMB internationalization and international trade are mutually beneficial and win-win. The development of either side has the opportunity to promote the development of the other.

The rapid development of foreign trade makes foreign trade enterprises hold a large number of foreign currency claims and debts. Due to the high risk of currency exposure, exchange rate fluctuation will have a certain impact on enterprise operations. After the internationalization of RMB, foreign trade and investment can be denominated and settled in domestic currency, and the exchange rate risk faced by enterprises will be reduced accordingly. This can further promote the development of China's foreign trade and investment.

At the same time, it will also promote the development of renminbi-denominated bonds and other financial markets.

However, it should be noted from the perspective of enterprise demand that when RMB appreciates, commodity prices will be higher, thus reducing the market demand for their commodities. When the RMB depreciates, although the market demand increases, enterprises will receive relatively little foreign currency funds, which will virtually reduce the profits of enterprises. Even in the context of RMB internationalization, enterprises still cannot completely avoid the pressure of exchange rate fluctuations and need to face the profit fluctuations caused by them.

On the other hand, the cross-border flow of RMB cash in the real economy, such as border trade and tourism, alleviates the shortage of settlement means in bilateral exchanges to a certain extent. It has promoted and expanded bilateral economic and trade exchanges and accelerated the economic development of border areas inhabited by ethnic minorities. In addition, many of China's neighboring countries are rich in natural resources but their markets are short of supply. The contrast with China is stark. The outflow of RMB will help alleviate China's shortage of natural resources and market oversupply.

In terms of international trade, China needs to promote the internationalization of the RMB, which is in line with its own needs as the world's largest trading nation. However, RMB internationalization also comes with a large number of uncertain risks. The internationalization of RMB will improve the efficiency of Chinese foreign trade enterprises.

3. THE GOAL OF RMB INTERNATIONALIZATION

The internationalization of the RMB needs to achieve five goals: the RMB should be freely convertible into foreign currencies both at home and abroad; It should be possible to use RMB as the pricing unit in international investment and trade; the RMB may be used as the payment currency in international investment and trade settlement; the RMB can be used as an investment and financing currency in international finance; the RMB can be used as a reserve currency [8].

3.1. The risk of financial cooperation in BRI

The Belt and Road Initiative will encourage more projects to use the yuan as a settlement currency, thus increasing its use in the international market. At the same time, under the impetus of the "area" initiative for the construction of infrastructure, direct investment can promote international technology, capital, and material factors of production such as communication, can

increase the use of yuan between countries along with the corresponding rate, form the RMB cross-border circulation mechanism, help to improve the investment value of the RMB. As China's outbound investment continues to increase under the Belt and Road Initiative, financial institutions such as banks and trusts are developing accordingly. This will provide a broader space for the improvement of domestic and international financial markets.

Finance serves the real economy. The deepening of trade and investment cooperation between China and countries and regions along the Belt and Road is bound to be accompanied by the deepening of financial cooperation. Financial cooperation lowers the cost of using the money for enterprises, facilitates investment and trade cooperation, and maximizes benefits for countries and regions along the Belt and Road. In terms of financing, The Asian Infrastructure Investment Bank and other Chinese financial institutions have set up several convenient platforms and supported a large number of important cooperation projects. In terms of RMB clearing, China has identified RMB clearing banks in more than 20 countries and regions, seven of which are in countries and regions along the Belt and Road. In currency swaps, China has signed bilateral currency swap agreements with 33 countries or regions worth more than rmb3.3tn. In foreign exchange, China can directly trade with more than 20 currencies. On the reserve currency front, the International Monetary Fund (IMF) for the first time broke out RMB holdings separately, which will give other countries the confidence to accept the RMB in their foreign exchange allocation. These circumstances objectively lower the barriers of financial cooperation in the Belt and Road projects to a certain extent.

However, there are three obvious problems with belt and Road financial cooperation. Firstly, big projects are mostly funded by traditional credit, but there are few breakthroughs in top-level design such as international credit standards [9]. Secondly, Chinese financial institutions are more involved than those of countries and regions along with the project and international financial institutions. It takes too long for Chinese financial institutions to set up branches overseas, making it difficult for them to integrate into the local social environment. Therefore, the financing problem cannot be solved fundamentally. Thirdly, cross-border financing relies heavily on the US dollar, euro, and other currencies, and there are few RMB financial products [10]. On the other hand, countries, and regions along the Belt and Road have different political systems, people's religious beliefs, and local wars in volatile areas, which may affect the internationalization of RMB through the Belt and Road [11]. These difficulties will not stop the internationalization of the RMB. Instead, China will continue to explore solutions suited to the national conditions of countries and regions along the

Belt and Road and gradually achieve the goal of RMB internationalization.

3.2. The risks of anti-globalization

"Anti-globalization" is built based on "globalization". From the perspective of economics, economic globalization has externalities [12]. For developed countries, multilateral trade means sharing their advanced technological resources with others, and there is a risk of market share dilution by developing countries. For developing countries, there are high transaction costs if they want to be part of the global economic wave. Due to the imbalance of international status and development, developing countries need to continuously improve their core competitiveness and bear the risks of reform. In recent years, developed countries transfer transaction costs to developing countries in an endless stream of cases. The main cause of "anti-globalization" is the conflict of interests among countries.

Although "anti-globalization" has increased the market barriers of international currency, globalization is generally beneficial to the development of the whole society [13]. The emergence of the "anti-globalization" phenomenon has increased the barriers for RMB to integrate into the international monetary system. China does not play an obvious role in RMB settlement in import and export trade, and the international currency market has always been in a state of high barriers. Since 2016, the proportion of cross-border RMB settlements has decreased significantly. Although China's import and export trade capacity has been continuously enhanced, the liquidity of RMB in the international settlement is not strong enough.

"Anti-globalization" increases the risk of currency internationalization. This economic development strategy against the tide of The Times has increased the uncertainty of the entire international market.

4. THE BRI PROMOTES RMB INTERNATIONALIZATION

The Belt and Road Initiative aims to build a community of shared interests featuring political mutual trust, economic inclusiveness, and cultural inclusiveness. This is in line to build a community with a shared future for mankind in the new era. However, investment and trade under the BRI will not be entirely driven by free markets [14]. In terms of economy, China has the excess production capacity and is short of mineral resources. BRI helps to consume China's excess production capacity and reduce resource dependence on countries such as the UK and the US. In addition, from a financial perspective, trade with neighboring countries is conducive to strengthening the flow of RMB and the issuance of the financial market, which can inject

vitality into China's financial market and promote its virtuous cycle.

4.1. Settlement currency

The IMF added RMB to its SDR basket in 2015. This means the RMB is one step closer to internationalization. However, the most effective way to promote the cross-border flow of RMB is still regional economic cooperation [15]. The RMB is considered to be the strongest currency in the major belt and Road regions. While details of the policy have yet to be worked out, many Chinese experts say the RMB should be used as the settlement currency for the region's massive trade in goods. At the same time, we will increase Chinese capital's investment in infrastructure construction and promote cross-border payment in RMB.

The cross-border settlement function of RMB is not well recognized by BRI countries. China's RMB internationalization process can be said to be still in the development stage, not as mature as the development of the US dollar. Therefore, in the "Belt and Road" trade, different countries have different recognition of RMB's international settlement function. Less than 10 countries account for more than 10 percent of their trade under the Belt and Road initiative, with the proportion remaining below 5 percent. If RMB's cross-border settlement function is not fully utilized for a long time, it will be difficult to achieve the economic goals of the Belt and Road Initiative.

However, the Belt and Road initiative will help promote the internationalization of the RMB. The core content of the Belt and Road Initiative, on the one hand, is to promote economic cooperation among countries in the region by strengthening regional economic cooperation and increasing the demand for the development of the eurozone and other unified currencies. The US dollar is the currency of choice for the Belt and Road Initiative. However, having learned the hard lessons of the financial crisis, many countries are still experimenting with alternative currencies to reduce risk through currency diversification [16]. BRI allows the yuan to be used as the settlement currency for its projects.

Experience in the internationalization of the U.S. dollar shows that RMB pricing and settlement in the field of bulk commodities is not only conducive to winning the pricing power of bulk commodities but also can accelerate the internationalization of the RMB [17]. In the BRI project, China should strengthen commodity cooperation with countries and regions along the Belt and Road using RMB as the main pricing and settlement currency, and vigorously promote RMB pricing and settlement of domestic crude oil futures. Necessary

RMB financial derivatives will be provided in support for bulk commodity transactions.

The Belt and Road Initiative is an important trade project for China. The pricing and settlement of international trade in RMB can effectively avoid third-party currency risks. In recent years, RMB has gained more international recognition, and its advantages as a tradable currency are emerging. The stable market value of RMB provides a good international reputation for its international expansion. Increasing the renminbi's international market coverage would reduce the exchange rate risk of other currencies used as pricing and settlement currencies. As a result, returns on RMB assets continue to be high. In addition, holding yuan can realize a big increase in asset value. It also provides liquidity insurance on the RMB, China's growing economic power.

4.2. Investment currency

The proportion of RMB in Outward Foreign Direct Investment (ODI) and international trade activities is an important factor for the success of RMB internationalization [18]. At present, there is a mismatch between the use of the yuan and China's share of global trade and investment. Foreign investment and trade cooperation are mainly denominated and settled in US dollars and euros. The yuan cannot be exchanged directly with the currencies of many countries and regions along the Belt and Road.

According to the White Paper on RMB internationalization for 2020 released by the Bank of China, 3,200 domestic and foreign industrial and commercial enterprises were surveyed. In 2020, 51% of domestic industrial and commercial enterprises used RMB at least 20% of their OFDI, up 13 percentage points from 2019. The proportion of industrial and commercial enterprises using RMB less than 20% of THEIR OFDI was 27%, down 11 percentage points from 2019. The proportion of enterprises that did not use renminbi to make the OUTBOUND direct investment was 22%, down 2% from 2019.

There is still a long way to go for RMB internationalization. Carrying out RMB foreign direct investment (ODI), especially RMB equity investment, is the key to further effectively mobilizing RMB demand potential [19]. Objectively, the biggest difficulty in carrying out the RMB of DI is to overcome the inertia of using the US dollar.

However, in the long term, with the in-depth development of projects along the Belt and Road (expansion of projects, improvement of policies, popularization of financial institutions, and deepening of mutual trust among countries), the utilization rate of RMB in ODI will gradually increase. As the influence of the Belt and Road Initiative continues to expand,

China's total investment in countries along the routes continues to increase. China's direct investment in countries along the Belt and Road reached \$15.64 billion in 2018, accounting for 13 percent of the total outbound investment, according to the Ministry of Commerce. The total investment represents a 77-fold increase from 2003 when the total investment was \$200 million, and a 16.5 percent increase from 2013 when the total investment was \$13.4 billion.

The Belt and Road Initiative has led more and more enterprises to participate in the investment, including both financial investment and non-financial investment, but the non-financial investment is the main category. Most of the investors are state-owned enterprises [20]. In the future, with the continuous improvement of the financial market system, SMEs in BRI projects will also have the opportunity to make ODI using RMB. The export of RMB will increase the utilization and liquidity of RMB in the overseas market.

4.3. Reserve currency

A reserve currency is defined as assets or deposits denominated in a foreign currency that is held primarily by governments or official institutions as foreign exchange reserves. In recent years, more and more countries and regions have adopted RMB as their reserve currency in different ways, and there is a great demand for RMB liquidity support in the international community. A currency swap is an effective way to promote countries and regions along the Belt and Road to increase RMB foreign exchange reserves.

The internationalization of sterling, DOLLAR, and other currencies benefited from currency swap [21]. Historically, the Bank of England effectively resolved the sterling credit crisis through the currency swap system [22]. At present, China has signed bilateral currency swap agreements with the central banks of more than 23 countries and regions along the Belt and Road, with a total volume of more than ONE trillion yuan. The currency swap agreements signed between China and countries and regions along the Belt and Road will not only provide liquidity support to each other but also promote the use of RMB as a bilateral trade settlement currency. At the same time, we will promote direct investment and financial asset investment in RMB as the denominated currency, and on this basis, encourage countries and regions along the Belt and Road to increase their RMB foreign exchange reserves.

However, based on a conservative estimate, the renminbi's international role should increase in the coming years, but it will take a long time to become a global reserve currency.

5. CONCLUSION

The belt and Road initiative has promoted economic cooperation among the upper echelon of countries, enhanced economic exchanges between them, brought new development vitality to these countries, and enhanced China's comprehensive national strength, but it has also brought a series of challenges. This is due to the differences in the political system, level of economic development, cultural ideology, and market structure among countries. There is no doubt that the Belt and Road initiative will help the RMB achieve its goal of internationalization. The underlying logic is to expand the use of RMB abroad through sound policies and reasonable incentive systems. Both the Jamaica system and the Bretton Woods system had a potential financial crisis based on the Triffin problem. The internationalization of RMB offers a new alternative to the international monetary system. However, it should be emphasized that RMB internationalization is still in the development stage and is unlikely to replace the US dollar as the main international currency in the short term. In the process of RMB internationalization, besides theoretical economic and financial issues, political and religious factors should also be considered in reality.

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