

# On the Necessity and Importance of RMB Internationalization

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**Abstract:** *As China's economic strength continues to grow, the RMB has gradually entered the international arena, and the term RMB internationalization has gradually arisen to the public. This paper will discuss the necessity of RMB internationalization and its advantages. It is concluded that RMB internationalization has a positive role in enhancing China's international status, promoting smooth trade between China and other countries, reducing the risk of other factors, increasing government revenue, diversifying international payment instruments, and improving the stability of various international systems. Therefore, RMB internationalization has become an inevitable trend.*

**Keywords:** *RMB internationalization; Necessity; Importance*

## 1. The Concept of RMB Internationalization

The RMB is the legal tender of China and is issued by the People's Bank of China. In economic terms, the internationalization of the RMB means the process by which the RMB can become a currency of exchange, settlement and reserve that enjoys universal recognition in the international community. Three measures are used to determine whether it is an international currency:

1) In the international arena, RMB should be in circulation to a certain extent. That is, it should be accepted by various countries and become a currency like "euro and US dollar" in a specific region.

2) Major international financial institutions invest in financial products denominated in RMB. That is, the financial market denominated in RMB, especially the financial market, needs to reach a definite scale.

3) A certain percentage of transactions in international trade are settled in RMB as the settlement currency. A set number of organizations, institutions and individuals, including China, are willing and proactive in settling in RMB[1].

RMB has gradually been accepted by more and more countries as a currency of payment and settlement, and has even become a hard currency in some countries and regions [2]. At the same time, China is using its policies to advance internationalization, and RMB internationalization is constantly on its way. The circulation of RMB is not equivalent to RMB internationalization, but the expansion of RMB circulation overseas will inevitably lead to RMB internationalization and eventually RMB will become a world currency. At present, one of the supreme manifestations of national economic competition is monetary competition. If the international status of RMB is enhanced, it will not only change the two-legged situation of the world currency, but also have a profound impact on the political landscape of Western countries.

## 2. The Necessity and Importance of RMB Internationalization

### **2.1 RMB Internationalization as a Long-term Strategy and as an Inevitable Trend in China's Economic Development**

#### **2.1.1 Adhering to opening to the outside world**

At present, China's international political status is rising, and China is actively involved in international affairs, insists on opening up to the outside world, and has extensive cooperation with many countries, which guarantees the strong political status of Chinese currency. And the strong economic power is the fundamental assurance of currency internationalization.

### ***2.1.2 Rapid economic growth***

Currencies such as the U.S. dollar and the euro have long been recognized as world currencies because they rely on the strong economic power of the countries that issue them. The RMB has risen to the stage of history because China's economy has built up over the past 20 years, the country has become the largest economy in the developing world, and the country boasts a robust foreign exchange reserve system. China's economy has sustained medium-to-high growth over the long term, instilling greater international confidence and recognition in the RMB[3].

### ***2.1.3 Deepened international cooperation***

The international cooperation and infrastructure construction of RMB is escalating, and the international cooperation is deepening, which improves the stability of RMB. Moreover, it has increased the use of RMB at home and abroad with the development of the Belt and Road, the establishment of bilateral currency system and the expansion of RMB clearing banks. More than that, the establishment of cross-border RMB pilots and the construction of cross-border RMB settlement systems have facilitated the cross-border use of RMB and expanded the scale of cross-border RMB application.[3]

### ***2.1.4 Special Drawing Right***

China has always adhered to the high level of opening up to the outside world. The scale and proportion of cross-border trade settlement in RMB have been rising. Moreover, the RMB has joined the Special Drawing Right (SDR), which is favored by more international investors [4]. Currently, RMB has been included in foreign exchange reserves of 75 countries and regions.

### ***2.1.5 Means to mitigate the impact***

The turbulence of the financial crisis has brought about huge negative economic impacts. The macro-financial management of the international currency issuers must have the capability of strong macro-financial regulation to attenuate the negative impact, and RMB internationalization is undoubtedly an effective instrument to mitigate the impact.

### ***2.1.6 Decline in dollar credit***

The economic integration of neighboring countries and regions requires the support of a unified monetary system. Moreover, the credit of the U.S. dollar is declining, and the infinite quantitative easing and ultra-low interest rate policies have posed the risk of a decline in the credit of the U.S. dollar, and the internationalization of the currency is a "last resort".

### ***2.1.7 Steady growth of China's GDP***

China has done the best job worldwide in preventing and controlling the COVID-19 pandemic, controlling the spread of the epidemic in a short time, restoring economic production, returning people's lives to normal, and achieving steady economic growth. Although global GDP growth is expected to be negative in 2020 according to the IMF's forecast table in Table 1, China still maintains a growth rate of 2% to 3%, the only one among the world's largest economies with positive growth. China's domestic social stability and economic growth have become the internal driving force for the internationalization of the RMB, creating a sound breeding ground environment for the internationalization of the RMB.

## ***2.2 Importance of RMB Internationalization***

### ***2.2.1 Raising China's International Status***

RMB internationalization has a catalytic effect on the improvement of China's international status. For the RMB to become a global currency alongside the US dollar and the euro, it is essential for China to be universally recognized by various countries and international authorities. In this regard, China's RMB is currently included in the Special Drawing Rights (SDR) basket of currencies by the International Monetary Fund, where RMB is globally recognized as a reserve currency. Although the SDR can only be used to withdraw reserve assets when needed and cannot be used directly as a currency, it makes the RMB more stable in foreign exchange savings. Secondly, it allows Chinese people to spend money in RMB when traveling abroad without the need to exchange, and it also makes it easier to allocate overseas assets. Finally, in terms of transactions, RMB denomination reduces the risk of exchange rate conversion. The internationalization of the RMB has enabled China to improve its international status and to increase its voice in international political and economic affairs. RMB

internationalization is complementary to China's political and economic development and they move forward together. In conclusion, RMB internationalization is of great significance to the enhancement of China's international status.

### ***2.2.2 Contributing to the Construction of China's Financial Center and the Establishment of a Fair and Reasonable International Monetary System***

RMB internationalization is of great significance for promoting the construction of China's international financial center and the establishment of a fair and reasonable international monetary system. The current international monetary system is dominated by RMB, with developed countries in a dominant position and developing countries in a disadvantageous position, while RMB internationalization can break the dominance of developed countries and allow the international monetary system to be relatively fair.

### ***2.2.3 Reducing Trade Transaction Costs***

In 2020, China's share of the total global import and export volume reached 15.8%, making China the world's largest trader. It means that when RMB is used as the international settlement currency, the transactions between China and foreign customers will be free from the exchange rate, and the risk of exchange rate fluctuations will not affect the enterprise's income, which is a mutually beneficial choice for both parties to the transaction. Therefore, the adoption of RMB for international settlement can save a lot of time and costs, which not only effectively improves the efficiency of economic operation, but also lessens the exchange rate risk of enterprise transactions and lowers the cost of transactions, which has far-reaching significance for the trade between China and foreign countries.

### ***2.2.4 Generating Seigniorage Revenues***

RMB internationalization generates seigniorage revenues for China, which is an important source of government revenue. For instance, if a \$10 bill is printed at a cost of one cent and can be used to purchase \$10 of goods, the difference of 99 cents is seigniorage, which means that seigniorage is the revenue earned by issuing the currency. With the continuous development of RMB internationalization, the more countries use RMB, the more RMB printing will be done, and the more seigniorage revenues will be generated naturally.

### ***2.2.5 Reducing Foreign Exchange Reserve Risk***

RMB internationalization can reduce foreign exchange reserves, lower the cost of large foreign exchange reserves, and thus mitigate the additional risk of foreign exchange reserves. As a state-owned special financial asset, foreign exchange reserves are exposed to other risks arising from the devaluation of the reserve currency. Excessive foreign exchange reserves increase the cost of foreign exchange, cause waste of resources and idle capital, and tend to exacerbate domestic inflation. With RMB internationalization, the demand for foreign exchange reserves is reduced, the cost of foreign exchange reserves is lowered, the funds are used rationally, and the risk of inflation is mitigated.

### ***2.2.6 More trade options***

As the US dollar has become monopolistic in the international arena, the most direct implication of the internationalization of the RMB is that it gives companies, individuals and countries a choice of new currencies for international settlements. In the context of globalization, countries are more closely linked to each other and their economies are mutually influenced, so the turbulence of the US dollar exchange rate has unknown effects not only on one country, but on the whole world economy. The internationalization of the RMB, on the other hand, may effectively curb the dollar-euro monopoly, and the stability of the RMB exchange rate may make the RMB an alternative trading option for the international community.

## **3. Data References**

### ***3.1 RMB Internationalization Index (RII) Exceeding That of JPY and GBP***

As can be seen from the Table 1, the RII rose from 3.03 in 2019 to 5.02 by the end of 2020 and surpassed the JPY and GBP from fifth to third place, an increase of 54.20% year-on-year. However, in terms of numbers, RMB internationalization index is still far from the internationalization index of USD and EUR.

Table 1: Changes in RMB Internationalization Index and Ranking, 2019-2020

Major Currencies	2019		2020	
	Internationalization Index	Ranking	Internationalization Index	Ranking
USD	49.52	1	51.27	1
Euro	29.84	2	26.17	2
RMB	3.03	5	5.02	3
JPY	3.34	4	4.91	4
GBP	4	3	4.15	5

3.2 Growth in the Size of foreign exchange reserves in RMB

The size of RMB in the foreign exchange reserves of central banks and monetary authorities around the world is growing steadily visually. Currently, the number of foreign central bank-type institutions entering China's interbank bond market has reached more than 70, and over 75 countries and regions have included the RMB in their foreign exchange reserves. As can be seen from the Table 2, the RMB has reached US\$287.5 billion in foreign exchange reserves of central banks and monetary authorities around the world.

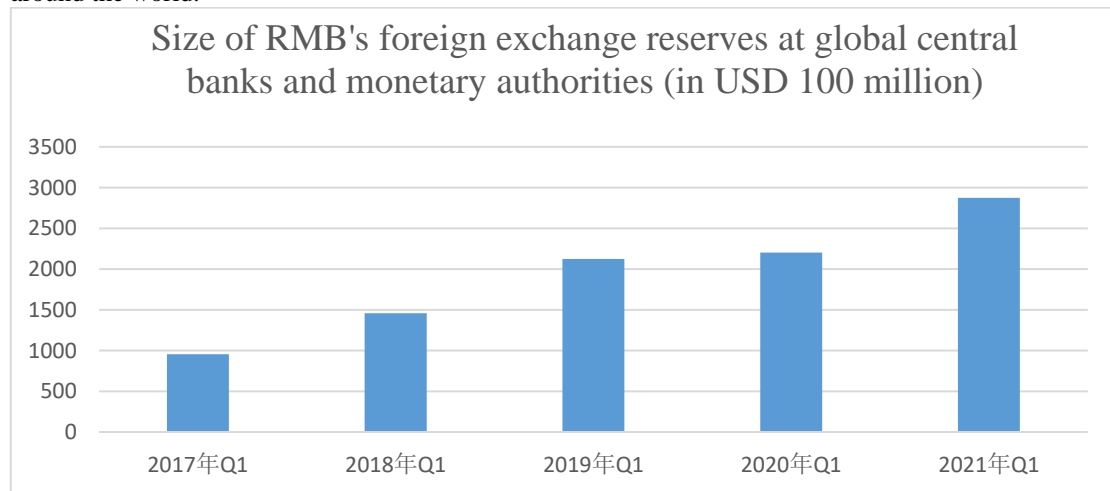


Fig. 1 Size of RMB's foreign exchange reserves at global central banks and monetary authorities (in USD 100 million)

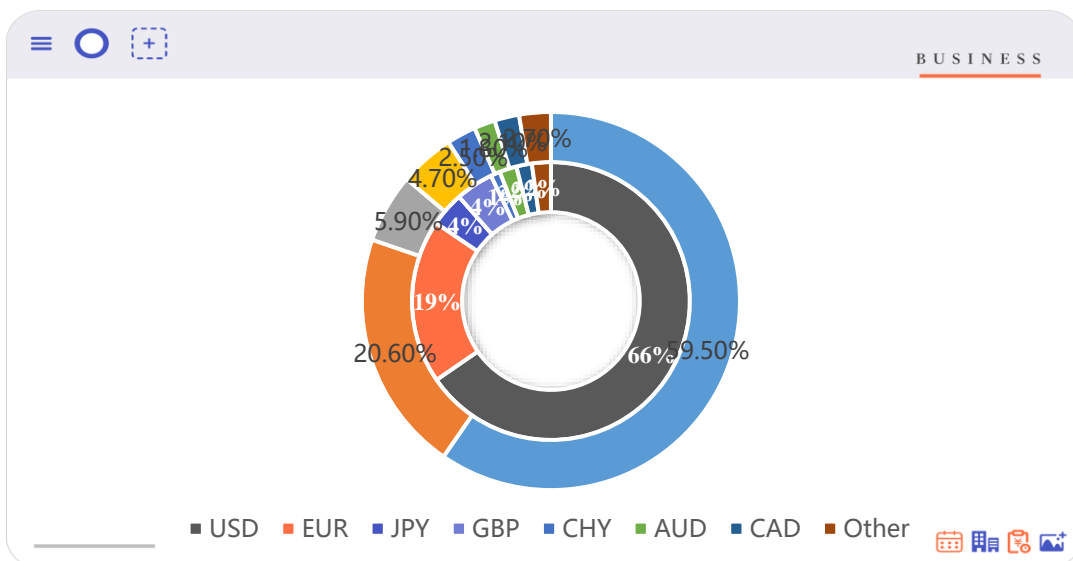


Fig. 2 Change in RMB's share of foreign exchange reserves of global central banks and monetary authorities in 2016 vs. 2021 (in %)

As can be seen from the Table 3, in 2016, when the RMB joined the SDR, the RMB accounted for only 1.1% of the foreign exchange reserves of global central banks and monetary authorities, while as of Q1 2021, the RMB accounted for 2.5% of the foreign exchange reserves of global central banks and monetary authorities, an increase of 1.4%. As can be seen, the internationalization of the RMB continues to progress and the size of foreign exchange reserves in RMB is growing steadily.

**3.3 China's Growing Share of Exports in Trade**

As shown in the Table 4, China accounts for a record 15% of global export market share in 2020. China's exports have continued to grow despite the global trade shrinkage. China has effectively curbed the epidemic, taken the lead in resuming work and production, and its manufacturing sector has become increasingly competitive globally, giving the RMB a greater voice in the settlement of global trade.

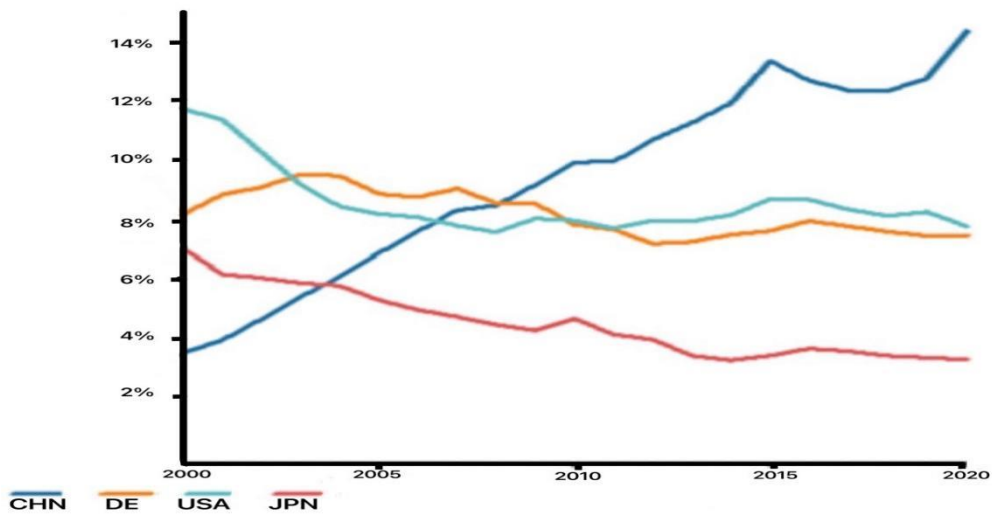


Fig. 3 China's market share of global exports in 2020 (in %)

**3.4 Increasing Business Volume of Cross-border Interbank Payment System in RMB**

The CIPS system plays an essential role in the development of RMB internationalization. The increasing business volume of the Cross-border Interbank Payment System in RMB shows that CIPS has made great progress in terms of system construction, coverage of partner institutions, and transaction volume. The number of users settling in RMB is increasing and the scope of RMB use is growing, which suggests that RMB is moving internationally.

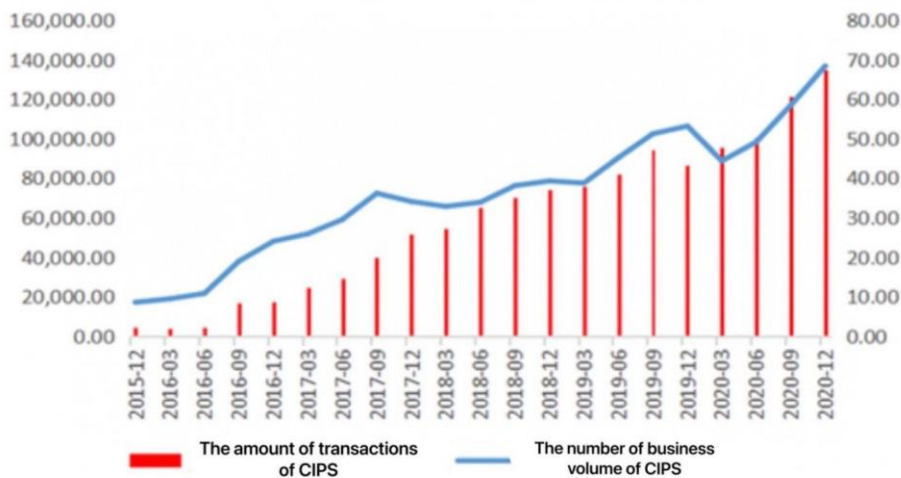


Fig. 4 The number of transactions and business volume of Cross-border Interbank Payment System (CIPS) in the current quarter

From the above data, we can clearly see that the internationalization of the RMB is in a favorable environment and that the trend of RMB internationalization is moving forward.

#### 4. Summary

With the enhancement of China's national strength and economic power, the internationalization of RMB is an inevitable trend. In the 2021 RMB Internationalization Report, we can clearly perceive that the role of RMB as a payment currency has been enhanced, its investment and financing functions have been improved, and its function as a storage and denomination currency has been enhanced. Positive progress has been made in RMB internationalization. According to the report, China's economy remains stable and RMB assets are more attractive to global investors. In addition, the RMB is ranked 5th among the world's major international payment currencies, with RMB payments accounting for 2.5% of all currency payments. The cross-border use of RMB in some current items will be further expanded [4], and the channels of cross-border RMB investment will be further broadened, and bilateral currency cooperation will be steadily launched. From the above data, RMB internationalization has already achieved some positive results. Moreover, the trend of internationalization of RMB is becoming more and more obvious, and the basic conditions for Asianization are already in place, and it is developing towards a new international monetary system of "tripod" of USD, EUR and RMB.[5]

RMB internationalization has surged ahead, not only because of the times, but also because of the accumulation of internal forces in China. China's international status keeps improving, its economic strength keeps growing, international cooperation keeps expanding, and it adheres to the correct policy of reform and opening up, all of which drive the RMB to advance in a higher and further direction, and thus RMB internationalization is inevitable.

But the internationalization of the RMB is not only a matter of necessity but also a matter of active response. We should adhere to the market-driven approach, further improve the policy support system and infrastructure arrangements for the cross-border use of RMB, improve China's offshore market and economic market, create a more convenient environment, and further accelerate the internationalization of RMB in China and advance it to the status of a world currency.

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