Benoît Cœuré: Taking stock of the global role of the renminbi

Speech by Mr Benoît Cœuré, Member of the Executive Board of the European Central Bank, at the European-Chinese Banking Day, Frankfurt am Main, 17 November 2014.

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Dear Ladies and Gentlemen,

It is an honour to be invited here to the European-Chinese Banking Day, part of the Frankfurt Euro Finance Week, and I would like to thank my hosts for giving me the opportunity to share some thoughts on the issue of yuan (or RMB) clearing. Clearly, the increasing importance of the Chinese economy and its currency over the last decades brings many new challenges, some of which also encompass international payment activities. As a major economy, the euro area is naturally affected by this process.

The rise of China has been astonishing. Since 1990, its weight in global GDP has increased from just below 2% to over 13% this year, and is projected to surpass 15% before 2020. In PPP terms, China's share in the global GDP is, as of this year, even larger than that of the US[1]. This rapid economic development would not have been possible without China also becoming one of the world's main trading nations, together with the euro area and the US.

This economic prowess is also gradually translating itself into a greater presence in the financial sphere. China has liberalised cross-border financial transactions, first those related to trade and direct investment, but increasingly also those related to portfolio investment. Approved investments under the different schemes that allow domestic and foreign institutional investors to make cross-border investments in and out of China have been rising steadily, although, so far, they amount only to about 2% of China's GDP. However, we should not forget that financial liberalisation is an ongoing process, which is still not complete.

Additionally, in the last few years, central banks across the world have started to hold onshore Chinese renminbi (CNY) in their reserves portfolios, usually with the expectation that CNY may become a reserve currency in the coming years. Many others indicate interest in reserve asset diversification into CNY once China's onshore market opens up further. This is an issue that the Eurosystem will also have to further reflect on in the future.

Also, the Shanghai – Hong Kong Stock Connect programme, which allows institutional and private investors from mainland China to invest up to a certain quota in Hong Kong and vice versa, is operating as of today and represents a further important step in opening the capital account and liberalising financial flows. The growth in cross-border transactions has also led to an increasing volume of RMB circulating outside China, giving rise to local RMB markets, in Asia and in the euro area. In response to these developments, many central banks have established a bilateral currency swap arrangement with the People's Bank of China (PBC). In October 2013, the ECB signed a bilateral currency swap arrangement with the PBC with maximum sizes of 45 billion euros when euro are provides euros to the PBC and 350 billion yuan when yuans are provided to the ECB. From the ECB's perspective, the swap line serves as a backstop facility to address sudden and temporary disruptions in the RMB market owing to liquidity shortages, so as to reassure market participants that a safety net is in place to address possible future market malfunctioning and reassure euro area banks regarding the continuous provision of RMB. After having launched direct trading between the renminbi and a number foreign currencies in China's onshore forex market over the last few years, direct trading between the euro and the onshore renminbi was launched in September 2014. This has the potential to reduce transaction costs, enhance the price discovery of the

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[1] 16.5% vs 16.3% for the US, IMF World Economic Outlook, October 2014.

EUR/CNY exchange rate and ultimately improve the functioning of the global financial system.

Considering the rise of China in the global economy, the extent of its external trade and the continuing development of its domestic financial markets, it is no surprise that also the number of payments and financial transactions being conducted between parties in China and elsewhere has been growing rapidly. Five years ago, the use of RMB in trade settlement was marginal, but according to SWIFT statistics, it is now already the seventh most popular payment currency, accounting for 1.72% of global payments in September 2014. This might not sound like a lot, but the growth rates are impressive; and it is worth noting that even the fourth most popular currency, the Japanese Yen, only accounts for 2.74% of global payments. The RMB as an invoicing currency for international trade has also been growing sharply: nowadays, about 25% of Chinese trade is invoiced in RMB, up from less than 2% in 2011. Looking forward, the RMB clearly has the potential to become a major international currency and to be included, when the International Monetary Fund will deem it appropriate, in the basket of currencies that determines the value of the Special Drawing Rights (SDRs).

That said, any currency of a truly global reach needs, amongst others, safe and efficient arrangements and seamless processes to clear and settle transactions in that currency. In the euro area, we have undertaken great efforts to introduce safe and efficient financial market infrastructures for payments and the clearing and settlement of financial instruments. Also within China, extensive work has been, and is, underway in this regard. However, while these infrastructures facilitate the safe and efficient handling of transactions within the respective economies, they do not yet provide for effective automated linkages between the two currency areas. Therefore, the institutions participating in domestic infrastructures are acting as intermediaries and service providers to corporates and financial actors wishing to transact within and between the two currency areas.

Various challenges exist in the processing of cross-border transactions. One is the need to have common or interoperable technical standards, a lack of which hamper a fully automated and fast processing of transactions, leading to higher failure rates and costs. In this regard, we appreciate the efforts undertaken in China to introduce state-of-the-art standards such as ISO20022, as well as those by SWIFT to increase fully-automated processing, for example by developing a standardised dictionary for the Chinese Commercial Code (CCC).

The setting up of RMB clearing arrangements like the one introduced here in Frankfurt – which I understand is starting operations today- and those existing or planned for other centres in Europe and other parts of the world, will play an important role in facilitating cross-border payments, as well as closer integration and relations between economies. I am convinced that the continuous development of more efficient payment and clearing arrangements will benefit corporates and financial actors, both in the euro area and in China.

To conclude, we should not forget that, together with many opportunities, the integration of a new major currency in the global economy also brings risks, as it allows shocks to propagate more easily across borders. To minimise risks, such a process therefore must be monitored carefully and complemented by close cooperation between authorities in China and abroad. Even more important however, is to strengthen the Chinese financial sector, in particular banks, so that it is sufficiently resilient to cope with the new pressures that financial liberalisation inevitably brings. I fully trust Chinese authorities to continue upgrading financial sector supervision and cooperate closely in order to safeguard overall financial stability.

Thank you for your attention.