

Carl-Ludwig Thiele: Internationalization of the renminbi – prospects and challenges

Keynote speech by Mr Carl-Ludwig Thiele, Member of the Executive Board of the Deutsche Bundesbank, at the 3rd European-Chinese Banking Day, Frankfurt am Main, 16 November 2016.

* * *

Ladies and gentlemen

I am delighted to have this opportunity to deliver the keynote speech at Euro Finance Week's European-Chinese Banking Day, which is already in its third year. In September 2015, I had the privilege of giving the opening speech at the opening ceremony of the Sino-German Center for Finance and Economics in Beijing. Although this event was not a long time ago, the internationalisation of the renminbi has progressed rapidly since then.

1. Where does the renminbi currently stand from an international perspective?

The timing of our meeting and the subject of my speech - the internationalisation of the renminbi (RMB) and the opportunities and challenges that this presents - could not be more topical. It was only weeks ago, on 1 October 2016, that the Chinese currency was officially added to the International Monetary Fund's basket of currencies. It has therefore joined the ranks of the US dollar, Japanese yen, pound sterling and, last but not least, the euro as one of the five most-used currencies in the world. This is a major political triumph for the People's Republic of China, as well as for the IMF, as China is the world's second largest economy, with growth of more than 6 per cent per year.

The Chinese government had been resolutely pressing ahead with the process of including the renminbi in the Special Drawing Right Basket since the year 2009. In doing so, it had more than just the prestige of being included in the IMF's basket of currencies in its sights - in actual fact, the internationalisation of the renminbi is closely linked to the opening-up of the capital markets in China as a whole and to the advancement of the Chinese economy. China's objective here is to morph from "the world's workshop" into a modern, service-oriented economy, with the international financial markets and the renminbi both having an important role to play: the former as a source of financing for economic activities and the latter as a lubricant for imports and exports.

2. Has the renminbi already established itself as an international key currency?

Three criteria come into play when assessing a currency's significance at the international level. The currency's use

- ♦ in the settlement of transactions, ie as a trading currency;
- ♦ in the capital markets, ie as an investment currency;
- ♦ and as an investment vehicle for central banks, ie as a reserve currency.

Let's examine the individual criteria in a little more detail now.

The renminbi has already firmly established itself as one of the world's most-used trading currencies. While the share of global payments made in renminbi was no more than 0.25 percent in January 2012, making it the world's 20th most-used trading currency, this share had

climbed to 1.86 percent by August 2016 - an increase of more than sixfold. Behind the US dollar, which remains the undisputed number-one trading currency in the world, the euro, the pound sterling and the Japanese yen comes the Chinese currency in fifth place - and there are signs that it will rise through the ranks.

The second step towards securing the renminbi's position as an international key currency is to strengthen its role as an investment currency. The greater the number of liquid, renminbi-denominated securities that are issued, the more foreign investors will also be interested in investing in renminbi. The prerequisite for this is that the Chinese capital markets are sufficiently deep and receptive to foreign capital. What's more, the Chinese markets need to be opened up to foreign investors. The Chinese government has recently made several efforts in this direction. Various programmes enable investors to make investments with fixed quota restrictions on the onshore bond market. Another option open to foreign central banks, sovereign wealth funds and offshore renminbi clearing banks is the China Interbank Bond Market (CIBM). Since mid-2015, the only prerequisite for access to this market has been prior registration with the People's Bank of China (PBoC), eliminating the need for the quota system.

Nowadays, the Chinese bond market is the third-largest in the world after the US and Japanese bond markets. However, only 2 percent of bonds are currently held by foreign investors. Holding a share of around 70 percent, the largest investors remain the Chinese commercial banks. Consequently, it is vital that further reforms are implemented in the future to open up the financial markets for foreign investors so that the renminbi can gain a foothold among the flexible and internationally used investment currency elite. One example of such necessary reforms would be to eliminate obstacles hindering access to the capital market, such as the quota model for investment in the bond market.

The final step towards becoming a globally recognised key currency is for a currency to be used as an international reserve currency. The renminbi's inclusion in the IMF's Special Drawing Rights basket has provided the framework for this. It is now expected that a wider range of market participants will invest capital in renminbi-denominated securities. These participants will likely be joined by an increasing number of central banks that will, in the future, invest parts of their reserve assets in corresponding securities, mostly government bonds.

3. What is the role of the Frankfurt financial centre in the internationalisation of the renminbi?

The renminbi's internationalisation strategy does not culminate with the currency's inclusion in the IMF's basket of currencies, however. On the contrary, the Chinese government is currently focusing on a whole raft of measures. One of these is the Cross-border Interbank Payment System (CIPS). It was launched in October 2015 and is the sole provider of settlement services for offshore renminbi payments. The People's Bank of China designed CIPS to provide an infrastructural buffer for the expected growth in renminbi transactions and to stem the disadvantages with regard to settlement efficiency vis-à-vis other currencies (particularly the US dollar).

Other measures include bilateral cooperation agreements that aim to further promote use of the renminbi as a trading and investment currency. The potential for efficient renminbi clearing is significant to enterprises that operate internationally. As China's largest European trading partner, Germany is of crucial importance in this context.

It was not for nothing that the first renminbi clearing hub located outside Asia was established in Frankfurt. Since 2014, it has been possible to settle renminbi-denominated payments via the Frankfurt branch of the People's Bank of China. This service provides attractive opportunities for small and medium-sized enterprises, for instance, to establish and expand business

relationships with Chinese enterprises while at the same time settling payments with China within their own local time zone and jurisdiction.

The China Europe International Exchange, or CEINEX, is another collaborative initiative. This joint venture of the Deutsche Börse Group, the Shanghai Stock Exchange and the China Financial Futures Exchange was opened exactly one year ago and is the first trading venue outside China for Chinese investment products in renminbi. CEINEX uses the Deutsche Börse's infrastructure and provides investors with the enticing option of gaining access to the Chinese capital market during European and US trading hours.

In addition to the formation and expansion of close and dynamic economic ties, activities that promote mutual understanding are another integral part of the renminbi's internationalisation strategy. Mutual trust is established by regularly exchanging information in the fields of politics, business and academia, and this is an important factor for successful cooperation with Chinese partners.

In mid-October this year, for example, a delegation of members of the Renminbi Initiative Group Frankfurt headed by the Deutsche Bundesbank and the Hessian Ministry of Economics travelled to Beijing and Shanghai for talks. This was in connection with a workshop in Beijing organised by the Sino-German Center of Finance and Economics, which boasted high-ranking participants from the People's Bank of China, academia and the financial sector. The Sino-German Center, which is part of the Goethe University in Frankfurt, is a research centre that conducts independent research and promotes interaction and improved mutual understanding by means of education and training. The Sino-German Center opened in September 2015 and I am proud of the fact that the Bundesbank, as a member of its Board of Trustees, is actively contributing to its success.

4. What conclusions can be drawn?

Ladies and gentlemen

The inclusion of the renminbi in the IMF's Special Drawing Rights basket marks a milestone in the internationalisation of the Chinese currency. There can be no doubt that this is a great political and economic triumph for China as well as an endorsement of the path to openness that the country has been treading with great determination since the end of the 1970s.

However, there is still some way to go if the renminbi is to become as important as the other four key currencies. Foreign investors' access to the onshore capital markets in China, which is still restricted, is a case in point and underscores the necessity for Chinese policymakers to continue to resolutely press ahead with the opening-up and liberalisation of the Chinese markets.

Thank you very much for your attention.