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# The RMB's Delicate Dance: Exploring the Complexities and Constraints of the Chinese Yuan on the Global Stage

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## Abstract

This paper investigates the internationalization of the Chinese Yuan (RMB) and its potential impacts on global financial systems, including challenges and implications for the competitiveness of the US dollar. We begin by analyzing China's efforts to promote the RMB's internationalization, which involve establishing currency swap agreements, developing offshore RMB centers, and securing the RMB's place in the IMF's Special Drawing Rights basket. The study then identifies key challenges the RMB must overcome to achieve internationalization, including capital account controls, exchange rate management, China's debt concerns, and geopolitical obstacles. We further examine how RMB internationalization could reshape global trade, investment, and financial markets, potentially leading to efficiency gains, shifts in trade patterns, and changes in global currency reserves and exchange rate dynamics. The paper explores China's options to mitigate financial system risks and enhance transparency and credibility in exchange rate policies to facilitate the RMB's future internationalization.

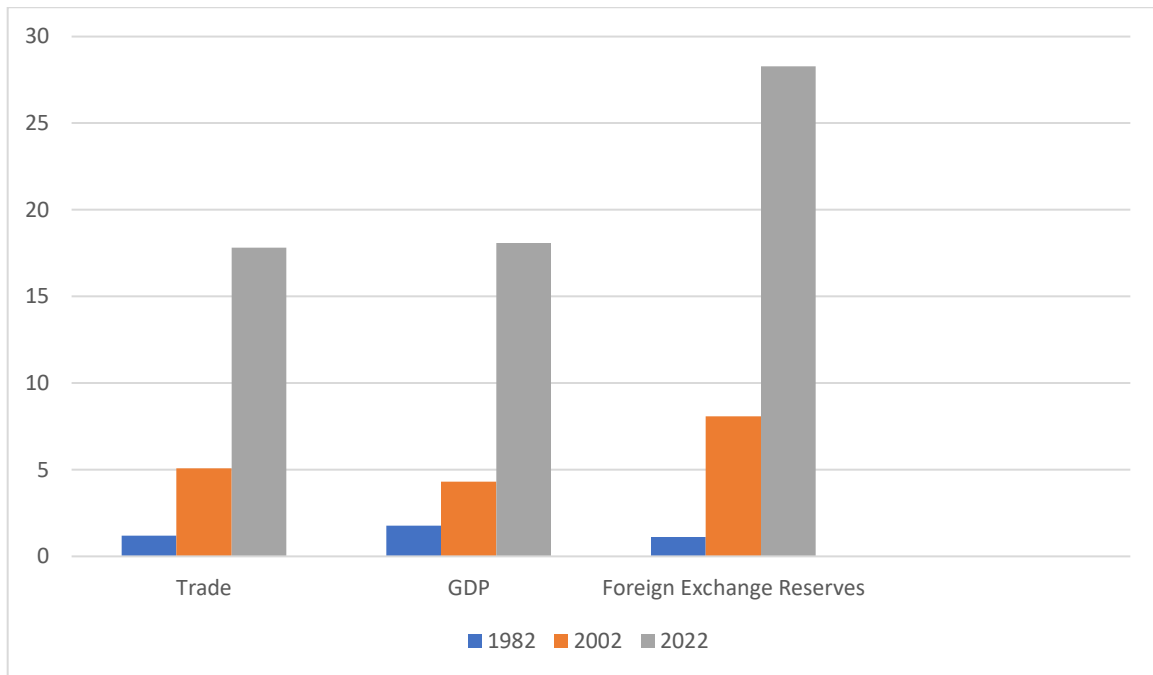
The final part of our study presents policy recommendations for the United States to retain dollar competitiveness. These include enhancing economic innovation, promoting international trade, strengthening global economic governance, participating in multilateral initiatives, assisting emerging economies, maintaining a stable macroeconomic environment, and addressing geopolitical tensions through diplomacy. We conclude by underlining the necessity of fostering a cooperative and inclusive global financial system to uphold economic stability in a highly interconnected world.

The views and findings expressed here are those of the authors and do not necessarily reflect those of the Middlebury Institute of International Studies or any officials of the Institute.

## I. Introduction

The Chinese Yuan (Renminbi or RMB) has significantly transformed since China's economic reform policies began in the late 1970s. Over the past four decades, China has become the world's second-largest economy and a key player in global trade. China accounts for nearly 30 percent of the world's foreign exchange reserves and significant global financial growth (Figure 1).

Figure 1: China's Share (%) of Global Finance



Note: GDP is in market prices, while Trade refers to merchandise trade.

Sources: People's Bank of China, World Trade Organization, International Monetary Fund, and World Bank.

China's economy and financial influence are significant. Alongside its economic growth, the Renminbi has become an increasingly substantial currency in the international financial landscape. Despite China's growing economic strength, its currency stature does not fully match it yet. This paper aims to provide an analytical overview of the RMB's internationalization and its implications for US Dollar dominance.

### A. Background on the Chinese Yuan (RMB) and China's currency policies

The Chinese Yuan has a lengthy and intricate history. It was first introduced in the early 1900s and has undergone several modifications. However, the most significant transformation occurred in the late 1970s as China shifted from a centrally planned economy to a market-oriented

economy.<sup>1</sup> This economic transition allowed China to integrate into the global economy and brought forth the need to modernize its financial system.

China's currency policies have played a significant role in its economic growth. The RMB was pegged to the U.S. dollar for much of its history. This policy facilitated trade and investment by maintaining a stable exchange rate, making the currency vulnerable to external economic shocks. In 2005, China reformed its exchange rate regime, gradually allowing the RMB to appreciate against a basket of currencies.<sup>2</sup> This change aimed to enhance the exchange rate's flexibility and reflect the RMB's growing importance in global trade.

### *B. Importance of RMB internationalization for China and the global economy*

Internationalization of the RMB is a crucial element of China's long-term economic strategy. As the world's largest exporter and second-largest economy, China seeks to reduce its reliance on the U.S. dollar and other major currencies, which can expose it to financial risks and limit its monetary policy independence.<sup>3</sup> The RMB internationalization can reduce transaction costs for Chinese businesses, increase the efficiency of China's financial system, and enhance its influence in the global economy.<sup>4</sup>

The internationalization of the RMB has significant implications for the global economy. As the RMB becomes a more influential currency, it has the potential to diversify the basket of reserve currencies and reduce the dominance of the U.S. dollar, potentially reshaping the international monetary system. Additionally, the RMB's internationalization could stimulate other economies' development.

### *C. Purpose and Scope*

The primary purpose of this paper is to investigate the process of RMB internationalization, its impact on international finance, and implications for US Dollar dominance. By examining the factors that have driven the RMB's internationalization and assessing the challenges and opportunities that lie ahead, this paper seeks to contribute to understanding the complex interplay between China's currency policies, its domestic economic development, and its role in the global economy. Specifically, this paper will explore capital account liberalization, the inclusion of RMB in IMF's Special Drawing Rights (SDR), and the development of offshore RMB centers and its effect on RMB Internationalization. This paper aims to offer beneficial insights for policymakers, academics, and market participants who want to comprehend the economic and strategic aspects of RMB internationalization.

## **II. Progress of RMB Internationalization**

### *A. Measures taken by the Chinese government to promote RMB internationalization*

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<sup>1</sup> Chunsom et al., 2018

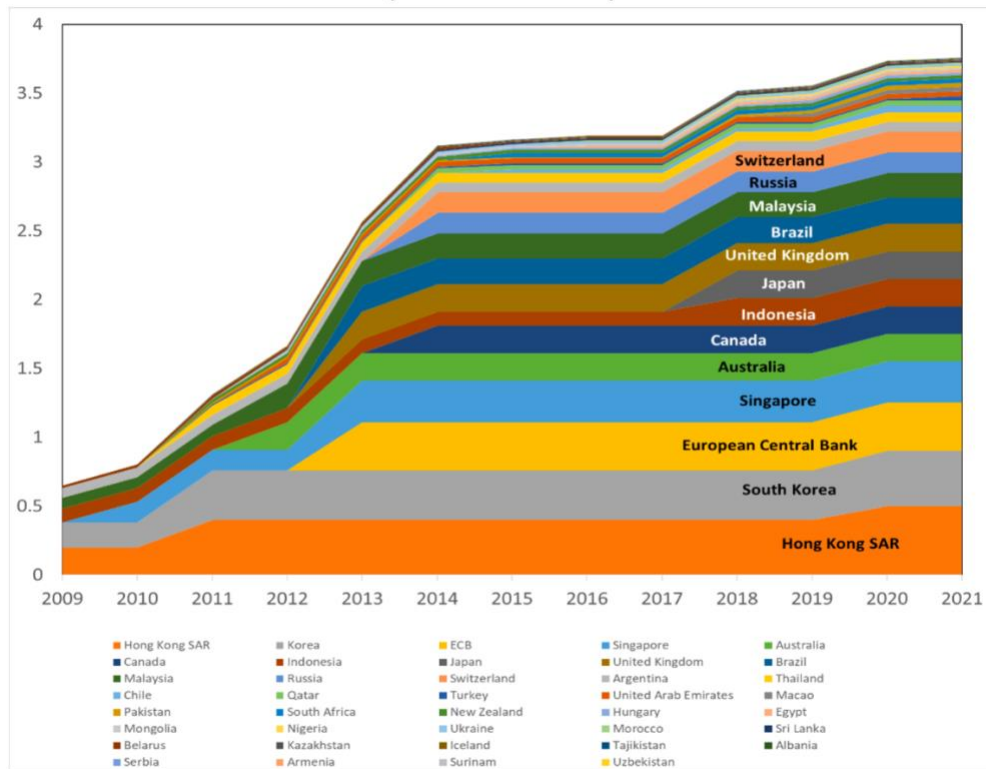
<sup>2</sup> Liang et al., 2022

<sup>3</sup> Which are the world's biggest economies by GDP? World Economic Forum.

<sup>4</sup> Why Does China Want to Internationalize the RMB? South China Morning Post.

One of the key measures the Chinese government employs to promote RMB internationalization is the establishment of currency swap agreements with foreign central banks.<sup>5</sup> These agreements allow for the exchange of local currencies between central banks, facilitating trade and investment between countries while reducing reliance on significant currencies such as the U.S. dollar.<sup>6</sup> Since the early 2000s, Bilateral swap lines have been a critical policy tool used by the People's Bank of China (PBC) to promote RMB internationalization.<sup>7</sup> Initially introduced to facilitate RMB settlement in international trade, swap lines were necessary because of limited RMB liquidity overseas. The geographic coverage started with neighboring Asian countries and later expanded to include other emerging markets. Subsequently, a few advanced economies, such as Canada, the European Central Bank, and the United Kingdom, signed swap lines with the PBC, mainly to address potential financial stability risks (Figure 2).<sup>8</sup>

Figure 2: People's Bank of China Swap Lines over Time<sup>9</sup>



<sup>5</sup> Wang et al., 2021

<sup>6</sup> Song, K., and Xia, L. (2020). Bilateral swap agreement and renminbi settlement in cross-border trade.

<sup>7</sup> Zhu, J, 2021, RMB Internationalization and International Monetary System Reform, China Finance Press, 2021

<sup>8</sup> Perez-Saiz and Zhang (2023), Renminbi Usage in Cross-Border Payments: Regional Patterns and the Role of Swaps Lines and Offshore Clearing Banks. International Monetary Fund

<sup>9</sup> Ibid.

As of 2022, China established 38 outstanding bilateral swap lines totaling around 4 trillion RMB.<sup>10</sup> These agreements have contributed to expanding RMB-denominated trade and investment and provide a foundation for developing offshore RMB markets.

Another essential measure the Chinese government took was the establishment of offshore RMB centers. These centers are financial hubs outside mainland China where RMB-denominated transactions can be conducted, thus promoting the use of RMB in international trade and finance. Key offshore RMB centers include Hong Kong, Singapore, London, and Frankfurt.<sup>11</sup> Offshore RMB centers have helped increase the use of the RMB as a global currency. These centers have made it easier for people to access RMB-based products and services and have made the RMB more liquid in global financial markets.

In addition to offshore RMB centers, issuing RMB-denominated bonds, known as Dim Sum bonds, is another measure the Chinese government employs to promote RMB internationalization.<sup>12</sup> These bonds are issued by both Chinese and foreign entities in offshore RMB markets, allowing issuers to raise capital in RMB and investors to diversify their portfolios with RMB-denominated assets.<sup>13</sup> Since the first Dim Sum bond issuance in 2007, the market has grown significantly, with issuances totaling over RMB 1 trillion.<sup>14</sup> The growth of the Dim Sum bond market has contributed to the increased use of RMB in global finance and facilitated the development of RMB-denominated capital markets.

Chinese officials lobbied the International Monetary Fund (IMF) for nearly a decade to include the RMB as a reserve currency. Finally, in 2016, the IMF included the RMB in its Special Drawing Rights (SDR) basket, recognizing it as one of the world's primary reserve currencies.<sup>15</sup> The SDR basket is a supplementary reserve asset created by the IMF to supplement its member countries' official reserves and provide additional liquidity in the global financial system.<sup>16</sup> Including the RMB in the SDR basket has enhanced the currency's international status. Given its SDR status, the RMB could be considered a viable alternative to traditional reserve currencies such as the U.S. dollar, euro, Japanese yen, and British pound.

Trends in RMB usage in global trade, investment, and financial markets have increased significantly over the past decade but are less than many predicted initially. However, some experts argue that including the RMB in the SDR basket may only sometimes lead to its widespread adoption as a reserve currency.<sup>17</sup> They point out that there are still concerns about China's economic and political stability and willingness to open its financial markets fully.<sup>18</sup> Additionally, many central banks and investors may be hesitant to hold large amounts of RMB

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<sup>10</sup> Ibid.

<sup>11</sup> The Rise of the Renminbi: Hong Kong's Role as an Offshore RMB Hub.

<sup>12</sup> Ibid.

<sup>13</sup> "Onshore vs offshore China bonds", Pictet Asset Management.

<sup>14</sup> Ibid.

<sup>15</sup> IMF Launches New SDR Basket Including Chinese Renminbi. International Monetary Fund

<sup>16</sup> Ibid.

<sup>17</sup> Atlantic Council. Renminbi ascending: How China's currency impacts global markets, foreign policy and Transatlantic financial regulation.

<sup>18</sup> Ibid.

due to limited convertibility into other currencies and lack of liquidity compared to traditional reserve currencies like USD or EUR.<sup>19</sup> Despite these concerns, there has been a notable increase in the usage of RMB in global trade, investment, and financial markets.

### *B. Trends in RMB usage in global trade, investment, and financial markets*

Assessing its share of international trade settlement is critical in evaluating RMB usage globally. While the global adoption of RMB usage remains early, it has become an important reference currency for some emerging economies. It is increasingly used for cross-border payments in Asia. Since 2009, the PBC has permitted cross-border settlement in RMB, initially in selected provinces, and then expanded nationwide.

Despite a slow start, RMB usage has expanded significantly in recent years.<sup>20</sup> Figure 3 illustrates the evolution of RMB in cross-border payments, measured as the RMB's share in an economy's total payments with China.<sup>21</sup> This is often the first phase of currency internationalization when the currency is used in transactions involving the issuing country. The payment data is based on the Swift messaging system that processes most global banking transactions. The Swift dataset spans most countries and regions and covers cross-border transactions dating back to 2010 regarding currency usage. In a sample of 125 economies, it has been observed that the median use of RMB has increased from 0 in 2014 to 20% in 2021. This indicates that at least half of the economies in the sample now settle 20% or more of their transactions with China in RMB. Furthermore, the 75th percentile has significantly increased from 0 to 70% in 2021, implying that a quarter of the sample economies now primarily transact with China using RMB. On the other hand, 25% of the economies in the sample hardly use RMB in their transactions with China, as shown by the fact that their usage falls close to zero in the 25th percentile.

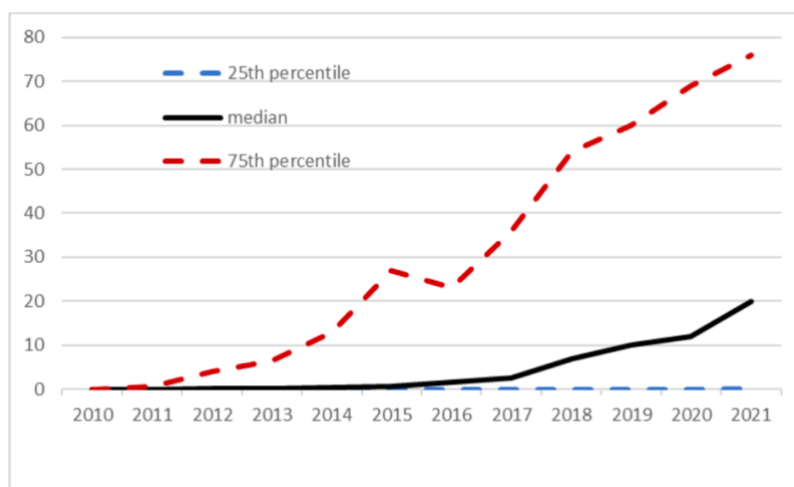
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<sup>19</sup> Ibid.

<sup>20</sup> Perez-Saiz and Zhang (2023), Renminbi Usage in Cross-Border Payments: Regional Patterns and the Role of Swaps Lines and Offshore Clearing Banks.

<sup>21</sup> Ibid.

Figure 3: RMB Cross-Border Payments and Settlements with China<sup>22</sup>



Sources: SWIFT Watch, IMF calculations

In addition to international trade settlement, the use of RMB in foreign direct investment (FDI) has also increased in recent years. China has encouraged using the RMB in cross-border investment by implementing various policy measures, such as the RMB Qualified Foreign Institutional Investor (RQFII) program and the RMB Cross-Border Direct Investment Scheme.<sup>23</sup> These programs allow foreign investors to invest in RMB-denominated assets and Chinese companies to invest in RMB overseas, thereby promoting the use of the currency in global investment transactions. Consequently, RMB-denominated FDI has grown substantially, accounting for an increasing share of China's total outbound FDI.<sup>24</sup> This trend signifies the growing acceptance of the RMB as an investment currency and its expanding role in global capital flows. Even though it has grown considerably, the RMB still represents only a tiny portion of all FDI transactions.

The RMB's share of global foreign exchange reserves has also risen steadily since its inclusion in the IMF's SDR basket. According to IMF data, the RMB's share of allocated global foreign exchange reserves has increased from 1.1% in the fourth quarter of 2016 to approximately 2.5% in the second quarter of 2021.<sup>25</sup> The RMB's share in global reserves remains relatively small compared to traditional reserve currencies, such as the U.S. dollar and the euro. However, this growth indicates the currency's increasing importance as a reserve asset.<sup>26</sup>

The expansion of the RMB's share in global foreign exchange reserves is primarily attributed to the Chinese government's efforts to liberalize its capital account and promote its international use.<sup>27</sup> With the growing integration of the RMB in the global financial system, central banks, and

<sup>22</sup> Ibid.

<sup>23</sup> Chen et al., 2021

<sup>24</sup> Ilman, 2016

<sup>25</sup> Perez-Saiz and Zhang (2023), Renminbi Usage in Cross-Border Payments: Regional Patterns and the Role of Swaps Lines and Offshore Clearing Banks.

<sup>26</sup> IMF (2018). People's Republic of China 2018 Article IV Staff Report, July 2018.

<sup>27</sup> Prasad, E. S., "China's Efforts to Expand the Internationalization of the RMB."

institutional investors are now allocating a portion of their reserves to RMB-denominated assets. This move helps diversify their portfolios and reduce dependence on traditional reserve currencies.

In summary, the Chinese government has taken several measures to promote RMB internationalization, including establishing currency swap agreements, developing offshore RMB centers, issuing RMB-denominated bonds, and including the RMB in the IMF's SDR basket. These efforts have made notable progress in using RMB in global trade, investment, and financial markets.<sup>28</sup> The RMB's increasing share in international trade settlement, its growing role in foreign direct investment, and its expanding presence in global foreign exchange reserves all demonstrate the currency's rising importance in the international financial landscape. Despite significant growth, the RMB still faces an uphill battle in its challenge to the US Dollar. While the overall share of RMB utilization has grown, it still pales compared to US Dollar utilization and even the Euro and Japanese Yen.

### **III. Challenges to RMB Internationalization**

#### *A. Capital account controls and financial market liberalization*

One of the significant challenges to RMB internationalization is China's capital account control and the pace of financial market liberalization.<sup>29</sup> Capital account controls limit the free flow of capital across borders, restricting foreign investors' access to RMB-denominated assets and Chinese investors' ability to invest overseas. Historically essential for China's economic stability, these controls hinder the acceptance of the RMB as a global currency.

The slow and inconsistent advancement in financial market liberalization is hindering RMB internationalization. This could discourage foreign investors and prevent the currency from fully integrating into the global financial system. To tackle this issue, the Chinese government has gradually relaxed capital account restrictions and implemented moderate measures to open up its financial markets. However, the pace of liberalization has been cautious due to concerns about potential risks to domestic financial stability, such as capital outflows and fluctuations in exchange rates.

#### *B. Exchange rate management and currency stability*

Another challenge to RMB internationalization is China's exchange rate management and currency stability. Historically, China has maintained a managed floating exchange rate regime that involves regular interventions by the central bank to stabilize the RMB's value.<sup>30</sup> While this approach has contributed to the stability of the RMB and supported China's export-driven growth model, it has also raised concerns about the currency's actual market value and the transparency of its exchange rate policy.

To increase the international use of the RMB, the Chinese government has implemented measures such as allowing its value to rise and increasing flexibility in its exchange rate

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<sup>28</sup> Perez-Saiz and Zhang (2023)

<sup>29</sup> Zheng et al., 2021

<sup>30</sup> Hu, Xiaolian: "Three characteristics of the managed floating exchange rate" (July 22, 2010)



system.<sup>31</sup> However, the ongoing management of the RMB's value may continue to pose challenges. It could lead to perceptions of currency manipulation and deter foreign investors from holding RMB-denominated assets. Ensuring currency stability while allowing for greater exchange rate flexibility is a critical balancing act for the Chinese government in pursuing RMB internationalization.

### *C. Concerns about China's debt levels and financial system risks*

China's rising debt levels and potential financial system risks challenge RMB internationalization. Over the past decade, China has experienced a rapid increase in debt, particularly in corporate and local government sectors.<sup>32</sup> This debt buildup has raised concerns about the sustainability of China's economic growth and the stability of its financial system.

High debt levels and potential financial risks could undermine confidence in the RMB as an international currency. They may lead to doubts about the creditworthiness of RMB-denominated assets and China's ability to manage its financial system effectively. The Chinese government will need to address these concerns by implementing prudent fiscal and monetary policies and strengthening the regulation and supervision of its financial system to ensure the RMB's credibility and attractiveness as a global currency.

### *D. Geopolitical factors and competition with the US dollar*

Geopolitical factors and competition with the US dollar also challenge RMB internationalization. The US dollar remains the dominant global reserve currency widely used in international trade, investment, and financial transactions.<sup>33</sup> As a result, the RMB faces an uphill battle to challenge the dollar's supremacy and achieve widespread acceptance as an international currency.

Moreover, geopolitical tensions between China and the United States and concerns about China's political and economic influence could hinder the RMB's internationalization process. As the competition between the two economic superpowers intensifies, some countries may be reluctant to adopt the RMB because of political considerations or concerns about potential economic dependence on China.

RMB internationalization faces several challenges, including capital account controls and financial market liberalization, exchange rate management and currency stability, concerns about China's debt levels and financial system risks, geopolitical factors, and competition with the US dollar.<sup>34</sup> China needs strong policies, financial reforms, and effective communication to build trust in the RMB as a reliable global currency.

Moving forward, China must continue to liberalize its financial markets and ease capital account controls while ensuring domestic financial stability. This may involve striking a delicate balance between opening up the economy to foreign investors and maintaining control over capital flows

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<sup>31</sup> Ibid.

<sup>32</sup> Li et al., 2020

<sup>33</sup> Fendoglu et al., 2020

<sup>34</sup> RMB Internationalization: Prospects and Challenges, BRINK.

to avoid disruptive shocks. The Chinese government also needs to enhance the transparency and credibility of its exchange rate policy to foster trust in the RMB's value and stability.

Moreover, addressing concerns about China's debt levels and financial system risks is crucial to maintaining confidence in the RMB. This will require the implementation of prudent fiscal and monetary policies as well as the strengthening of financial regulation and supervision to mitigate potential risks.

Navigating the geopolitical landscape and fostering cooperation with other countries will be essential for the RMB's internationalization. By engaging in constructive dialogue and promoting economic collaboration, China can work to alleviate concerns about its political and economic influence and create a favorable environment for the RMB's acceptance as a global currency.

Ultimately, the successful internationalization of the RMB will depend on China's ability to address these challenges and demonstrate its stability, reliability, and attractiveness as an international reserve asset. Achieving this objective could enhance China's role in the global financial system and contribute to a more diversified and resilient international monetary order.

#### **IV. Implications of RMB Internationalization**

##### *A. Impact on global trade*

Internationalization of the RMB is expected to have significant implications for global trade. One of the primary benefits for trading partners is the reduction in transaction costs associated with currency conversions. By conducting business in RMB, firms can avoid the costs of exchanging their local currency for a more widely accepted currency, such as the US dollar, and then convert it back into their domestic currency.<sup>35</sup> This can lead to efficiency gains and cost savings for both Chinese and foreign firms engaged in international trade.

Furthermore, using RMB in trade transactions can reduce the exchange rate risks for trade partners.<sup>36</sup> To reduce uncertainties in trade and promote stable trade relationships, companies can invoice and settle trade in RMB. This minimizes their exposure to exchange rate fluctuations between their local and US currencies.

The increased use of the RMB in global trade may also affect trade patterns and regional economic integration. As the RMB becomes more widely accepted as a trade currency, it could facilitate more significant trade ties between China and its trading partners, particularly those participating in the Belt and Road Initiative (BRI).<sup>37</sup> This could lead to a broader reorientation of global trade networks, with a growing emphasis on intra-Asia trade and increasing regional economic integration.

The continued internationalization of the RMB may encourage other countries to increase their use of local currencies in trade transactions, potentially leading to a more diversified and

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<sup>35</sup> “How do foreign exchange rates affect a business”, FXStreet.

<sup>36</sup> Lu & Lu, 2022

<sup>37</sup> Liang, Yan. RMB Internationalization and Financing Belt-Road Initiative.

multipolar global trade system. This could contribute to greater economic resilience and reduced dependence on major reserve currencies, such as the US dollar, in international trade.

### *B. Impact on global investment*

The RMB internationalization is also expected to have implications for global investments. As China liberalizes its capital account and promotes the use of RMB in cross-border investments, foreign direct investment (FDI) flows may shift in their composition and direction.<sup>38</sup>

For example, the increased use of RMB in outbound FDI could lead to increased Chinese investment in RMB-denominated assets overseas, potentially providing new sources of capital for countries seeking to finance infrastructure projects and other investment needs. Conversely, opening up China's financial markets may attract more significant foreign investment inflows into RMB-denominated assets, further integrating China into the global investment landscape.

As China continues to liberalize its financial markets and open its capital account, new opportunities may arise for international investors in RMB-denominated assets. Access to a broader range of investment products, such as RMB-denominated bonds, equities, and other financial instruments, could provide investors with greater diversification and potential returns.<sup>39</sup>

Additionally, including RMB-denominated assets in global indices, such as the Bloomberg Barclays Global Aggregate Index and the MSCI Emerging Markets Index, may encourage international investors to allocate a portion of their portfolios to RMB-denominated assets, enhancing the RMB's role in global investment and contributing to internationalization.<sup>40</sup>

### *C. Impact on global financial markets*

The RMB internationalization may also have implications for global financial markets, particularly in shifts in global currency reserves and its role as a reserve currency. As the RMB gains acceptance as a global reserve currency, central banks and other institutional investors may increase their holdings of RMB-denominated assets, diversifying their reserves and reducing their reliance on traditional reserve currencies such as the US dollar, euro, and Japanese yen.<sup>41</sup>

This shift in reserve allocations could affect global financial stability and international monetary systems. A more diversified reserve currency landscape may reduce the risks associated with overreliance on a single dominant currency, such as the US dollar, and contribute to a more resilient global financial system.

In addition to impacting global financial markets, the internationalization of the RMB is also expected to influence currency markets and exchange rate dynamics. As the RMB becomes more widely used in international transactions, its role in currency markets may expand, increasing currency trading volumes and liquidity. This, in turn, could affect exchange rate dynamics and the relationship between the RMB and other major currencies.

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<sup>38</sup> Ollo, 2018

<sup>39</sup> China Daily, "Central bank to expand cross-border investment, strengthen Yuan"

<sup>40</sup> China Daily, "International investors pursue RMB-denominated assets", June 8, 2021.

<sup>41</sup> Central banks up reserves of RMB to a high - Chinadaily.com.cn

For instance, the growing importance of the RMB in global financial markets may result in a stronger correlation between the RMB and other major currencies, as market participants increasingly view the RMB as a significant global currency. Moreover, increased RMB trading may lead to greater exchange rate flexibility as the Chinese government gradually moves towards a more market-oriented exchange rate regime.

Overall, the internationalization of the RMB has far-reaching implications for global trade, investment, and financial markets. The increased use of RMB in trade transactions can yield potential benefits for trade partners and influence trade patterns, promoting regional economic integration. Liberalizing China's financial markets and capital accounts may reshape global investment flows and present new opportunities for international investors in RMB-denominated assets. Finally, the RMB's growing role as a reserve currency and its impact on global financial markets may lead to shifts in currency reserves and exchange rate dynamics.

To fully realize the potential benefits of RMB internationalization, China must continue to address the challenges discussed earlier, such as capital account controls, exchange rate management, financial system risks, and geopolitical factors. In doing so, China can contribute to a more diversified and resilient international monetary system, fostering more excellent economic stability and cooperation in an increasingly interconnected world.

## **V. Conclusions**

### *A. Summary of the progress, challenges, and implications of RMB internationalization*

The internationalization of the Chinese yuan (RMB) represents a significant development in the global financial landscape. Over the past decade, China has made considerable progress in promoting the RMB's internationalization through measures such as establishing currency swap agreements, developing offshore RMB centers, issuing RMB-denominated bonds, and securing the RMB's inclusion in the IMF's Special Drawing Rights (SDR) basket.<sup>42</sup> As a result, the RMB has gained prominence in global trade, investment, and financial markets, reflecting its growing importance as an international currency.

Despite this progress, the RMB faces several challenges on its path to internationalization, including capital account controls, exchange rate management, concerns about China's debt levels and financial system risks, and geopolitical factors. Addressing these challenges is crucial for the RMB to establish itself as a stable and credible international currency, contributing to a more diversified and resilient global monetary system.

The implications of RMB internationalization are far-reaching, with potential impacts on global trade, investment, and financial markets. As the RMB becomes more widely accepted as an international currency, it can lead to efficiency gains and reduced transaction costs for trade

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<sup>42</sup> Federal Reserve Bank of San Francisco (October 2, 2017)

partners, influence trade patterns, and promote regional economic integration.<sup>43</sup> The RMB's growing role in global investment and financial markets may also reshape investment flows, create new opportunities for international investors, and contribute to shifts in global currency reserves and exchange rate dynamics.

### *B. Prospects for the future of RMB internationalization and its role in the global economy*

Looking ahead, the prospects for RMB internationalization will depend on China's ability to address the challenges discussed earlier and demonstrate its stability, reliability, and attractiveness as an international reserve asset.<sup>44</sup> This will require continued efforts to liberalize China's financial markets, ease capital account controls, and enhance the transparency and credibility of its exchange rate policies. Additionally, prudent fiscal and monetary policies and strong financial regulation and supervision are essential to mitigate concerns about China's debt levels and financial system risks.

As the RMB continues integrating into the global financial system, it will likely play an increasingly prominent role in the global economy, potentially contributing to a diversified and multipolar international monetary order. This may affect global financial stability and the relationships between major economies, particularly the United States and China.

### *C. Potential policy recommendations for the USA to maintain dollar dominance*

As the RMB gains popularity as a global currency, it may be necessary for the United States and the international community to implement various policies to uphold the dominance of the US dollar and promote a stable and collaborative global financial system.<sup>45</sup> A strong and innovative economy will help maintain the attractiveness of the US dollar and its dominant position in the global financial system.

First, the United States should focus on boosting its economic competitiveness and productivity by investing in education, research and development, and infrastructure. Second, the US should pursue policies that promote international trade and investment, including negotiating trade agreements, reducing trade barriers, and fostering a favorable environment for foreign direct investment. These measures can help maintain the US dollar's central role in international trade and investment transactions.

Third, the United States should work closely with other major economies and international institutions, such as the International Monetary Fund (IMF) and the World Bank, to strengthen global economic governance and financial stability. By playing a leading role in these organizations and collaborating on key issues, the US can maintain its influence in the global financial system and ensure the continued relevance of the US dollar as a reserve currency.

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<sup>43</sup> Chinese Renminbi Internationalization, PNC Bank.

<sup>44</sup> Will China's Push to Internationalize the Renminbi Succeed?. Center for Strategic and International Studies (CSIS)

<sup>45</sup> Taylor & Francis, A decade of RMB internationalisation.

Fourth, the United States should actively participate in and support multilateral initiatives and forums to address global challenges such as climate change, inequality, and financial instability. By doing so, the US can demonstrate its commitment to international cooperation and maintain the trust and confidence of other countries in the US dollar.

Fifth, as part of its efforts, the United States can work with global financial institutions to assist in the growth of financial markets in emerging economies. This is especially important in countries where the RMB is becoming more prevalent. This can help create a more diversified and balanced global financial system, reducing the potential risks associated with overreliance on a single dominant currency.

Sixth, the United States should pursue sound monetary and fiscal policies to maintain a stable and predictable macroeconomic environment. This will help preserve investor confidence in dollar-denominated assets and ensure the smooth functioning of global financial markets.

Seventh, the United States should engage in dialogue and diplomacy to address geopolitical tensions and risks that may undermine confidence in the US dollar. By reducing conflicts and fostering stability in critical regions, the US can help maintain the dollar's position as a safe-haven currency and reliable store of value in times of uncertainty. The United States should continue to support Bretton Woods institutions, such as the IMF and the World Bank, which have played a critical role in shaping the current global financial system. By reinforcing these institutions and their principles, the US can maintain the stability and resilience of the global financial system.

Additionally, the US should encourage China to integrate further into the existing international monetary system and adhere to established norms and rules. This can help ensure that China's growing influence on the global economy is channeled through a cooperative and inclusive framework, thereby reducing the risks associated with decoupling and fragmentation. Should the US push too hard in a non-collaborative way, it could result in the potentially adverse effect of China's pursuit of decoupling and its active undermining of the existing global financial order.

By implementing these policy recommendations, the United States can maintain the dollar's dominance in the global financial system while promoting a more stable and cooperative environment for the internationalization of the RMB and other emerging market currencies. This approach could contribute to a more resilient and inclusive global monetary order, fostering greater economic stability and collaboration in an increasingly interconnected world.

By pursuing these policy recommendations, the United States can maintain the dollar's dominance in the global financial system while fostering a more stable, cooperative, and inclusive international monetary order. Encouraging China to play within the existing global financial system and supporting Bretton Woods institutions can help mitigate the risks associated with the internationalization of the RMB, promoting more excellent economic stability and collaboration in an increasingly interconnected world.

Overall, the expansion of the RMB on a global level offers advantages and drawbacks to the world economy. Although the RMB's increasing involvement in worldwide trade, investments,

and financial markets could result in substantial benefits, it is essential to confront challenges such as capital account regulations, exchange rate supervision, and financial system dangers to establish the RMB as a dependable international currency. By pursuing sound economic policies and fostering international cooperation, China and the United States can work together to shape a more stable and resilient global financial landscape that accommodates the rise of the RMB as an international currency while maintaining the dollar's dominant position in the global economy. Although there has been much focus on the increasing value of the RMB, it still has a significant distance to cover before it can compete with the US Dollar's dominance.

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