

Limiting Factors and Measures for RMB Cross-Border Trade Settlement

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Abstract

If the simultaneous development of cross-border trade and offshore market expands radically, it will bring about opposite effects. We need to dialectically view the various influences brought by the development of cross-border RMB trade settlement and RMB internationalization. We need to start from the crux of our own shortcomings to improve the economic and financial system construction. We should seize the current favorable time, take advantage of the economic restructuring period of domestic market, the adjustment time of international offshore financial center, the period that international markets are seeking for haven currency and other historical opportunities to promote RMB internationalization by building RMB offshore markets.

Key words: RMB; Cross-border trade; Settlement

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INTRODUCTION

Cross-border trade settlement is a very effective breakthrough to promote the internationalization of RMB. However, in the face of China's current synchronous developmental mode of "cross-border trade" and "offshore market", we cannot help thinking that what kind of relationship in the end exists between it and the internationalization of RMB? Whether this model can help

achieve the internationalization of RMB? What factors limit the RMB cross-border trade and what measures should be taken to promote the RMB cross-border trade?

1. CONSTRAINTS OF THE RMB CROSS-BORDER TRADE SETTLEMENT

After the 2008 global economic crisis, many domestic experts and scholars believe that RMB should use the US dollar weakness in the post crisis period to accelerate the internationalization process and enhance the international status and recognition. The Chinese government also timely expanded the RMB cross-border trade settlement trials, and obtained a certain economic benefits through the valuation and settlement of cross-border trade. The reason why the Chinese government did not adopt a radical approach to promote the internationalization of RMB is mainly based on the following considerations:

Firstly, the restriction of China's monetary policy. At present, China follows an independent monetary policy, managed floating exchange rate policy and partial openness of capital accounts, but the achievement of RMB internationalization requires to under the premise of ensuring the independence of China's monetary policy to open the capital accounts or fully liberalize the exchange controls to fully implement floating. In the economic crisis, the depression of the U.S. Economy quickly infected Europe and emerging economies, the liberalization of exchange rate or capital control at this time would have caused a loss which would fully offset or outweigh the gains arising from the internationalization of RMB. Meanwhile, China's serious lag in financial regulation and undeveloped financial market makes it almost impossible to bear the risk of price volatility.

Secondly, the restrictions on China's economic self-development. Instead of saying that the economic crisis was caused by enormous negative external stimuli, making the Chinese economy into a recession interval,

the exposed structural disequilibrium of Chinese economy is the root cause of the low resistance and resilience. Today, the Chinese economy is still under the shackle of “dual economy”, rural and urban productivities develop unequally, and inter-regional economies present a non-equilibrium situation. Especially after the implementation of the large-scale counter-cyclical macroeconomic policy, the overcapacity, local debt accumulation, economic imbalance and other issues have been highlighted, making negative effects of the policy continued to expand. It is said that “resisting foreign aggression after stabilizing the country”. In the face of its own complex economic situation, China has to speed up the industrial restructuring and upgrading, revive the real economy and allow the market to play a greater effectiveness in guarding against the external attacks of a variety of possible risks. Therefore, it is not the most opportune time to vigorously promote the internationalization of RMB now.

Thirdly, the restrictions on the domestic financial reform process. A series of domestic reform should follow the orders of the priority of real economic reform, followed by domestic financial sector reform, the priority of long-term investments, followed by short-term investments, and the priority of foreign direct investments, followed by security and financial projects. Finance serves for the real economy in the final analysis. Premier Li Keqiang has repeatedly stressed the need to further revitalize the money stock, showing that the current slowing down of the real economic recovery is mainly due to that fund cannot be optimally allocated and cannot be delivered to ischemic enterprises. Even if the RMB derivative products have relatively increased, effective capital back channels are still not smooth, alternative investment products are absolutely deficient and market is immature, all of which lead to the low yields of offshore RMB, affecting the willingness of the holding. From a general review of the current cross-border trade settlement, the authority had hoped it could “reversely push” the domestic financial reform, but in fact what has been truly “reversely pushed” is only the openness of capital accounts. At the same time, when the government allows cross-border trade settlement and the outflow of RMB is formed, the offshore RMB funds will flow back through the domestic bond market and realize investments as creditors to seek greater benefits. Therefore, to the Chinese capital demanders, the process is a “re-loan game” with increased costs. Such back flow of offshore funds is inefficient and meaningless.

Fourthly, the limitation of bargaining powers of domestic enterprises. Throughout the structure of China’s import and export enterprises, we can clearly find that China’s major imported products are primary materials, and the demands for resource commodities are also on the rise. However, on the other hand, most of the exported products are intermediate products or processing

products, which make the bargaining powers and profits of Chinese enterprises in the import and export trades very limited. In a complete industrial chain and value chain, Europe, the USA and other developed countries remain in an absolutely dominant position, which also leads to the weak acceptance of RMB when evaluating in RMB. At the same time, unlike Germany and other goods competitive economies, China’s exported products still have a significant gap with other countries in the scientific and technological content, technological progress and product innovation, reducing the demands for the products to a certain extent. The insufficient bargaining power of domestic enterprises makes China only accept the prices of other countries passively, thus weakens the level of the internationalization of RMB.

Fifthly, ancillary services and investment reflux channels are not developed. The cross-border trade settlement in RMB is an emerging financial service after all, and customers are often used to and rely on the existing fixed settlement mode. Therefore, the improvement and popularization of a new settlement needs the timely introduction of supporting details of the policies. The standardization and promptness of supporting measures will greatly enhance the vital interests of cross-border trade pilot enterprises. However, due to the cumbersome procedures and high transaction fees as well as multi-bank involvement and a lack of a unified global regulation, a single commercial bank cannot achieve the effective management of enterprise accounts. Therefore, to improve the financial services of cross-border trades is still a long way to go. The other issue keeping pace with the improvement of financial services is how to build the RMB offshore circulation channels. The offshore RMB is facing low yields, narrow investment modes, poor return channels and other problems, so how to diversify the value preservation and value increase properties of RMB under the premise of partial openness of capital projects is the focus of China’s urgent needs. Increase offshore RMB-denominated assets species, launch corresponding tools for RMB value preservation and value increase, explore RMB’s function of value storage while exerting the function of international settlement currency, all of which will be the core of the future work of China’s cross-border trade settlement. Size and maturity of investment sites, diversification of haven tools and value added tools, and improvement of financial service efficiency will enhance the enthusiasm of offshore RMB holders and the internationalization road of RMB will steadily push forward in this process.

Sixthly, RMB offshore mobile clearing system has not been launched. In the past, there were two clearing modes for RMB clearing: clearing bank and correspondent bank. Each model has its own advantage and complement each other. In the initial trial period commercial banks also apply different discount rates. However, at the launch of

cross-border trade settlement, due to the lack of a unified clearing standard and statistical benchmark, RMB cross-border trade settlement system has not fully played its rightful convenience. However, the old status is about to be broken. On September 25, 2014, Liu Shiyu, Deputy Governor of People's Bank of China said in Shanghai that the construction of China International payment system (CIPS) has made a significant progress, and will be located in Shanghai sooner. Liu Shiyu has made the above statement when gave a keynote speech at the special general meeting in 2014 CCP12 (Central Counter Party). Therefore, in the preliminary financial reforms of the free trade zone, the innovation of liquidation is very important. In a word, establishment and improvement of a unified clearing channel will bring more convenience to cross-border RMB trade settlement and RMB internationalization in the future.

2. MAIN MEASURES TO PROMOTE THE INTERNATIONALIZATION OF RMB

(a) Strengthen the construction of RMB offshore market The developmental mode, path and progress of RMB offshore financial market must be consistent with the actual situation and specific needs of China, and must properly handle the relationship between the development of financial reforms and stability. Firstly, expand the breadth and depth of RMB offshore financial market, increase the size of offshore RMB and gradually expand the international influences of RMB. Secondly, change the single investment channel and poor reflux mechanism of RMB, accelerate innovation of financial instruments, enrich and develop overseas RMB financial products, and strive to create more varieties of high quality RMB bond products. Improve the core competitiveness of offshore RMB products to enter the mainstream investment community. Thirdly, steadily improve the domestic financial reforms and further promote RMB interest rate and exchange rate reform, orderly liberalize the capital accounts, improve China's financial supervision system, and strengthen the coordination with other countries in the offshore market in the fields of investor secrecy, anti-money laundering, tax evasion, supervision and other aspects. Control the risks of RMB offshore market, reduce the impacts of offshore financial market on domestic economy, and safeguard the domestic economic and financial security. Finally, bring the RMB capital pool of offshore market into the scope of monetary supervision and take all factors into consideration. Innovate monetary policy tools and transmission mechanism, adhere to the combination of initiative and prudence, ensure that the pricing of RMB interest rate and exchange rate is firmly kept in the hands of the central bank, and ensure that the effectiveness of monetary policy will not be weakened.

(b) Ensure the smooth and orderly economic fundamentals The progress and development of real economy is one of the most basic conditions of internationalization of a currency. At present, China is vigorously carrying out structural reforms and guiding economic development to change from the direction of government-oriented to market-oriented. Since more than 30 years of reform and opening up, the dividends of reform have been gradually reduced, which also needs a firm government commitment to reform, fight corruption, reduce the monopoly level and help people. Authorities should give full play to market forces rather than administrative measures to avoid a manipulation of economy. We should be aware that the expansionary monetary and fiscal policy is not the universal tool to stabilize economic cycle, and may even be the culprit of expanding economic amplitude. Only when China's economy is able to endure the pains of reform, withstand long restructuring and the test of low economic growth, China can really achieve the structural improvement and increased resistance. This is also the focus of China's macroeconomic development in the future.

(c) Improve legal system and framework of offshore market Legal system building is a particular challenge that establishment and development of RMB offshore financial centers must stand up to, especially the arrangement and design of financial regulations, tax incentives, judicial systems, dispute settlement methods and other systems greatly affects the attractiveness of RMB offshore financial centers on overseas investments, coordination and cooperation with the world's major financial centers as well as the macro-control of our financial order. Specifically, we must establish separate a financial supervisory authority and a sound supervisory system in RMB offshore financial centers; establish a complete, well-targeted and strongly executive basic legal system, and convenient, friendly and efficient offshore legal system; establish sound independent and efficient jurisdiction system, litigation system, final adjudication system, judge act system, lawyer management system and pragmatic dispute settlement system.

(d) Strengthen the awareness of financial security and financial supervision The progress on the road of RMB internationalization cannot be separated from increased awareness of safety and favorable protection from financial regulation. China should firstly improve and make up its own weakness on credit system, find out the gap between the developed countries, strictly abide by the restrictions of *Basel Agreement* on commercial banks' capital adequacy ratio and other standards, and prevent financial risks from the source to ensure financial safety. Secondly, China should make use of the US dollar's weakening trend hit by subprime crisis to break the status of US dollar's "what I say goes", and enhance China's discourse power in international affairs. Strive to promote

the reform of voting rights in the IMF, and promote the construction of the existing international financial order. Finally, China should strengthen international financial regulation, and jointly guard against the spread of financial risks.

CONCLUSION

At present, China is in a critical period of economic reform and structural adjustment, and reform dividend is difficult to achieve. Overcapacity, systemic risks exacerbated by the real estate market as well as increased business costs of enterprises threaten China's macroeconomic environment. These require us to reasonably and appropriately apply the macroeconomic policies, constantly improve the level of economic regulation, transit administrative means to market behaviors, strive to create an "economic upgrade" to continue to stimulate the power and vitality of economic and social development, promote urban and rural development and industrial restructuring, and promote economic progress with technological innovations. We believe that correct national economic policies and guidelines will be beneficial to protect the healthy development of China's economy, and provide a good foundation for RMB cross-border trade settlement as well as the RMB internationalization. Therefore, under the broad environment of a sharp drop in demographic dividend and upcoming "middle income trap", China should strive to enhance the resistance to external shocks, and further promote the domestic financial reforms and

the internationalization process of RMB. In the initial stage of internationalization of RMB, the expansion of RMB cross-border settlement pilot coverage areas and the increase of uses and demands of offshore RMB will continue to enhance the international recognition and acceptance of RMB. The cross-border transactions also enhance China's adaptability and practical experience to deal with exchange rate fluctuations and changes in demands for RMB. In summary, we should fully explore the endogenous reasons of a number of limiting factors of RMB cross-border trade settlement, find out our own weaknesses and take targeted measures to endeavor to achieve the internationalization of RMB in the future

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