Reign of the Renminbi: China’s Currency is the New Royalty in International Treasury Circles

China’s leading position on the world economic stage is now universally acknowledged, and companies of all sizes and industries are positioning the country at the heart of their growth strategies.

As China becomes increasingly integrated into global networks, the renminbi’s role as a world currency – not only for international trade, but also as a treasury, capital and reserve currency – is becoming more strategic.

Some companies are already recognizing the emergence of a new world currency will change the way they conduct their business in China, therefore, they are embracing new opportunities to use the Chinese currency to support their business strategies there. On the other hand, despite China’s pivotal position in international trade, a large proportion of corporations have yet to make the shift and include the RMB in their currency mix, albeit the potential benefits of doing so.

Not ‘If’, But ‘When’

These days, treasurers who do business in China are no longer talking about ‘if’ they will use the RMB, but rather ‘when’. Companies are also finding that their competitors have increasingly taken advantage of the opportunities offered by the currency, meaning they themselves should act sooner rather than later. In 2015, the RMB became the fifth-ranked global payments currency by volume, according to SWIFT, and it is already the second most popular currency globally for trade finance after the US dollar at about 9% of flows, which is an achievement considering its starting point was zero just a few years ago.
Advice for Embarking on The RMB Journey

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Connecting China within a regional or global liquidity structure can now bring considerable advantages for cash-generative businesses, and there are a variety of opportunities to do this.

For those who have not yet embarked on their RMB journey, or are at the early stages, how should they go about it? The logical starting point for most corporates is to use the currency to settle cross-border trade, whether that is inbound, outbound or a combination of both. An opportunity that has existed since 2009, the advantages of doing so include better commercial conditions (since counterparties’ foreign exchange risk is eliminated), greater flexibility in managing cash, liquidity and risk within China, and access to a wider community of buyers and/or sellers. Documentation is less onerous when using RMB rather than foreign currencies, which speeds up the process of doing business. Payment terms can also be more attractive: suppliers may offer up to 210 days for RMB, compared with 90 days for foreign currency, resulting in obvious working capital benefits.

Connecting China
Many treasurers are less concerned about settling trade in RMB than with how they will manage the resulting surplus or deficit in the currency, including managing funding gaps across legal entities, both within China and cross-border. This has been a challenging issue in the past, but connecting China within a regional or global liquidity structure can now bring considerable advantages for cash-generative businesses, and there are a variety of opportunities to do this. For example, cross-border ‘on-behalf-of’ structures, payment netting and lending/sweeping are now feasible, and some well-known banks are experienced in supporting customers in these activities.

One issue that companies operating in China need to consider is the disconnect that exists between the onshore RMB (CNY) and offshore RMB (CNH) markets. For companies with surplus cash, the onshore market is more liquid and deposit rates are higher. In contrast, for net borrowers in RMB, offshore borrowing may be cheaper. Many companies have cash surpluses or deficits at different times, so they should speak to their banks about the most appropriate liquidity solution.

In addition to Hong Kong, offshore RMB centers are developing in London, Singapore and Taipei. As a result, liquidity pools are gradually deepening and the range of available liquidity and risk management instruments is growing. Pretty soon, treasurers should be able to manage CNH in the same way as any other international currency, which will ease the way business is conducted with China.
Taking a Consistent Approach
Just as managing RMB liquidity both domestically and cross-border is becoming easier, opportunities to set up efficient cash management processes are also increasing. Companies can take advantage of this development to centralize payment processing through a shared services center or a payment factory that uses 'on-behalf-of' structures and performs payment netting. This enables companies to centralize and streamline payments in a way that is more or less consistent with other regions than in the past. Some challenges remain, however. For example, settling transactions is subject to regulatory restrictions, while processes are less automated than when using established cross-border trading currencies such as the US dollar, but significant progress has been made.

Approaching the Final Stage
As developments in cross-border trade and liquidity increase, the final step in the RMB becoming the default currency for multinationals doing business in China is its development as a capital currency. With cross-border controls still in place, onshore and offshore markets cannot converge, and restrictions on foreign direct investment, the RMB is still in a nascent stage of becoming a reserve and capital currency. While changes are under way, transfers of RMB between China and offshore centers are subject to certain conditions. As the obstacles to the RMB becoming a capital currency reduce, we are likely to see substantial growth in the number of banks, companies and governments that hold the RMB as a reserve currency. This will cement its importance as a world currency.

Act Now, Adjust Later
Even if economic growth in China experiences periodic slowdowns, which is inevitable as its economy matures, it will undoubtedly continue to strengthen its position as a dominant global trading partner. Meanwhile, as liberalization progresses, the RMB is becoming a strategic global currency, both for doing business in China and more widely. For example, there will be more demand to settle trade transactions in RMB between counterparties that do not use the US dollar as their base currency. While the benefits will differ by organization, ultimately, it will be better to learn the game now rather than be beaten later.

Undoubtedly, companies will need to make adjustments and revisions in their RMB strategies over time, particularly since regulatory revisions unleash new opportunities. In sum, adopting the RMB is critical to a company cementing its competitive position within China and potentially globally.

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