

# China in the Global Economy

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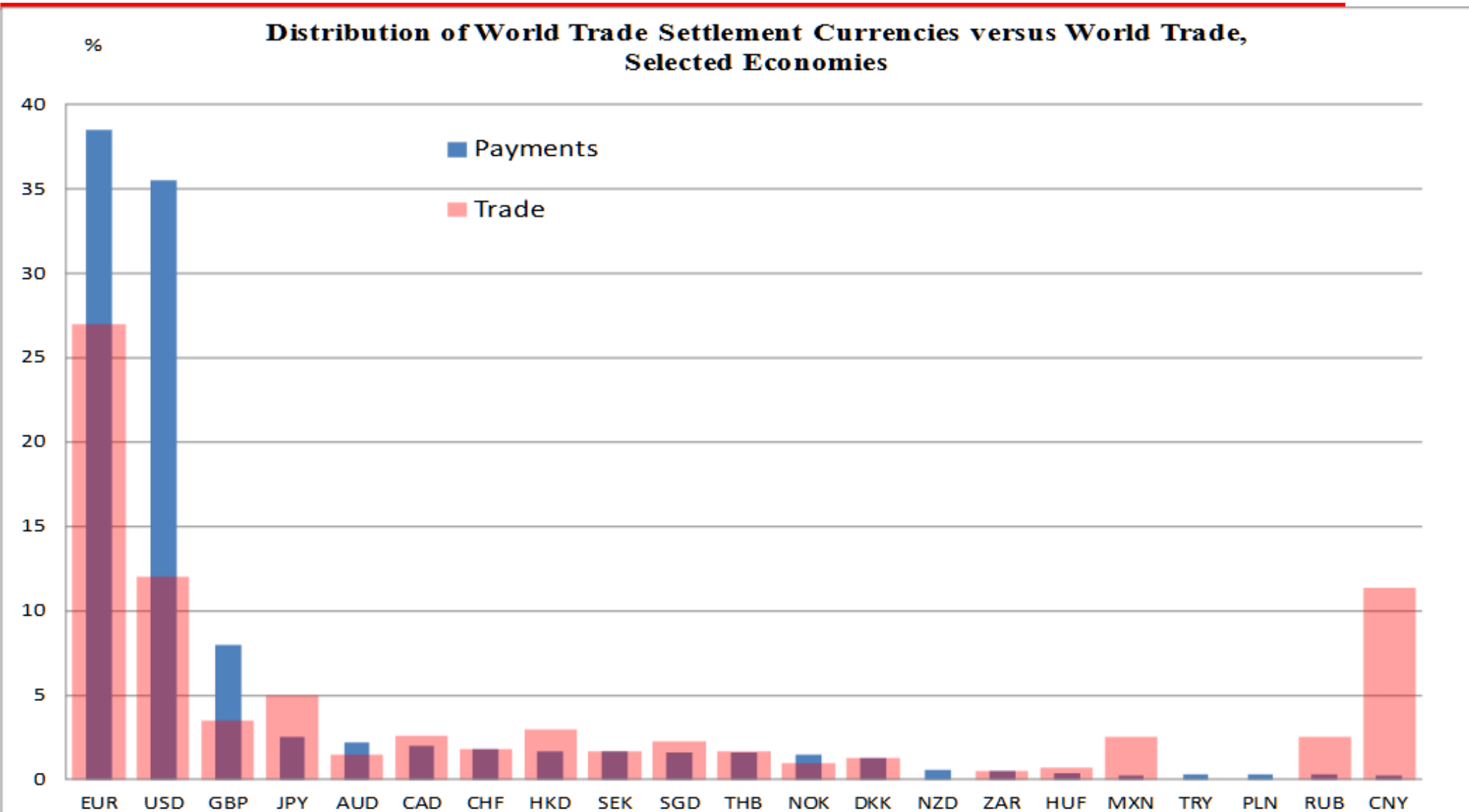
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# The Internationalisation of the Renminbi

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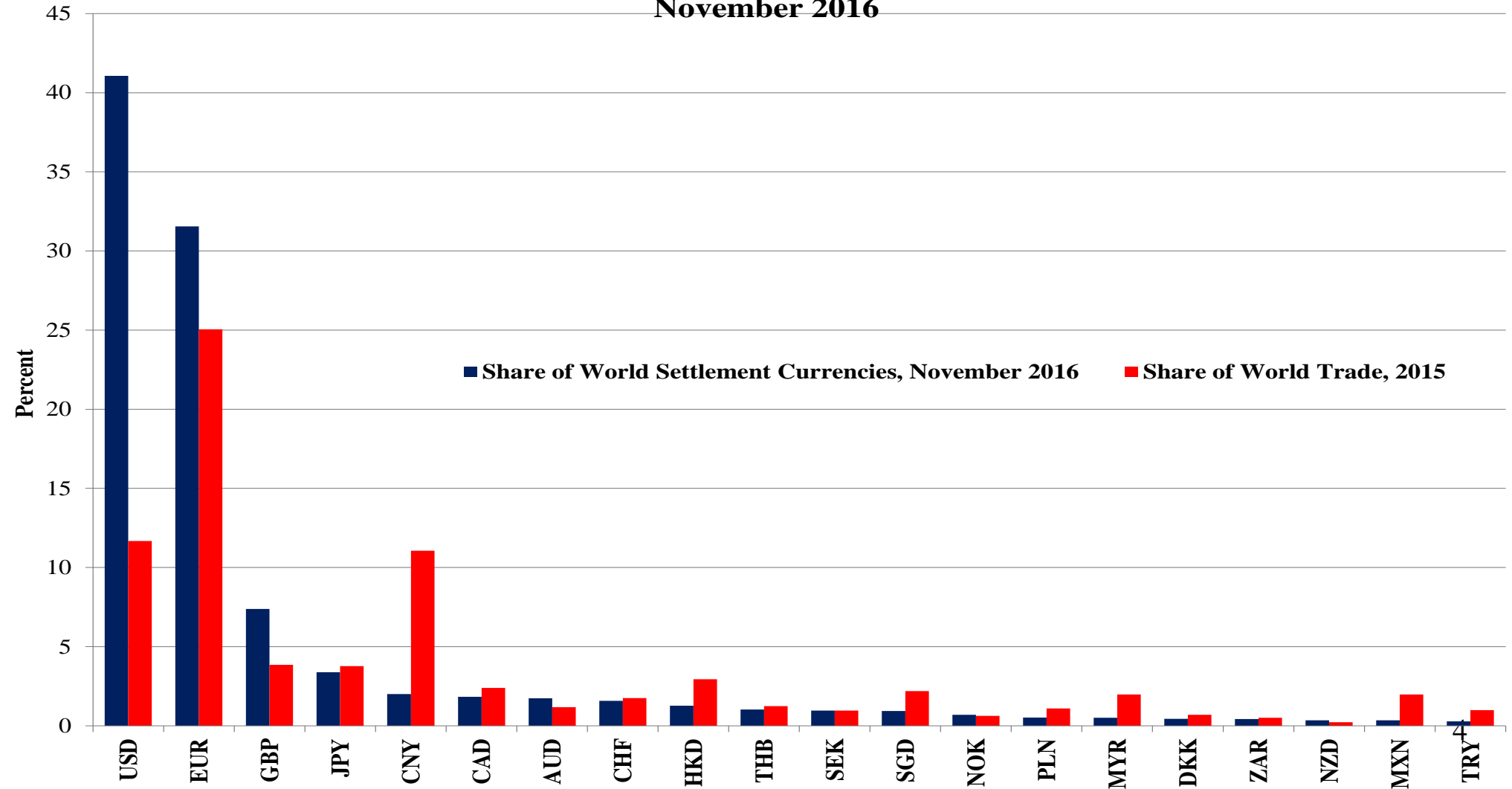
- ◆ The Renminbi, the Chinese currency, is increasingly used as an invoicing, clearing and settlement currency for cross-border transactions, especially those involving Chinese enterprises as transacting parties.
- ◆ In the fourth quarter of 2015, Chinese cross-border trade settled in Renminbi amounted to an annualized rate of US\$1.1 trillion, or 26.4% of total Chinese cross-border trade, compared to virtually zero in the first quarter of 2010. (Actually, the proportion of Chinese trade settled in Renminbi already reached 32.4% in the third quarter of 2015 and would have grown higher were it not for the unexpected Renminbi devaluation of 4% last August.)
- ◆ If the same proportion of Chinese trade is settled in its own currency as Japan (75%), then more than US\$3 trillion of Chinese trade will be settled in Renminbi annually, greatly diminishing the necessity for China to have a large foreign exchange reserve.
- ◆ The central banks and monetary authorities of many countries and regions have entered into swap agreements with the People's Bank of China, the central bank of China.

# Shares of World Settlement Currencies and World Trade of Currency Issuers, 2010



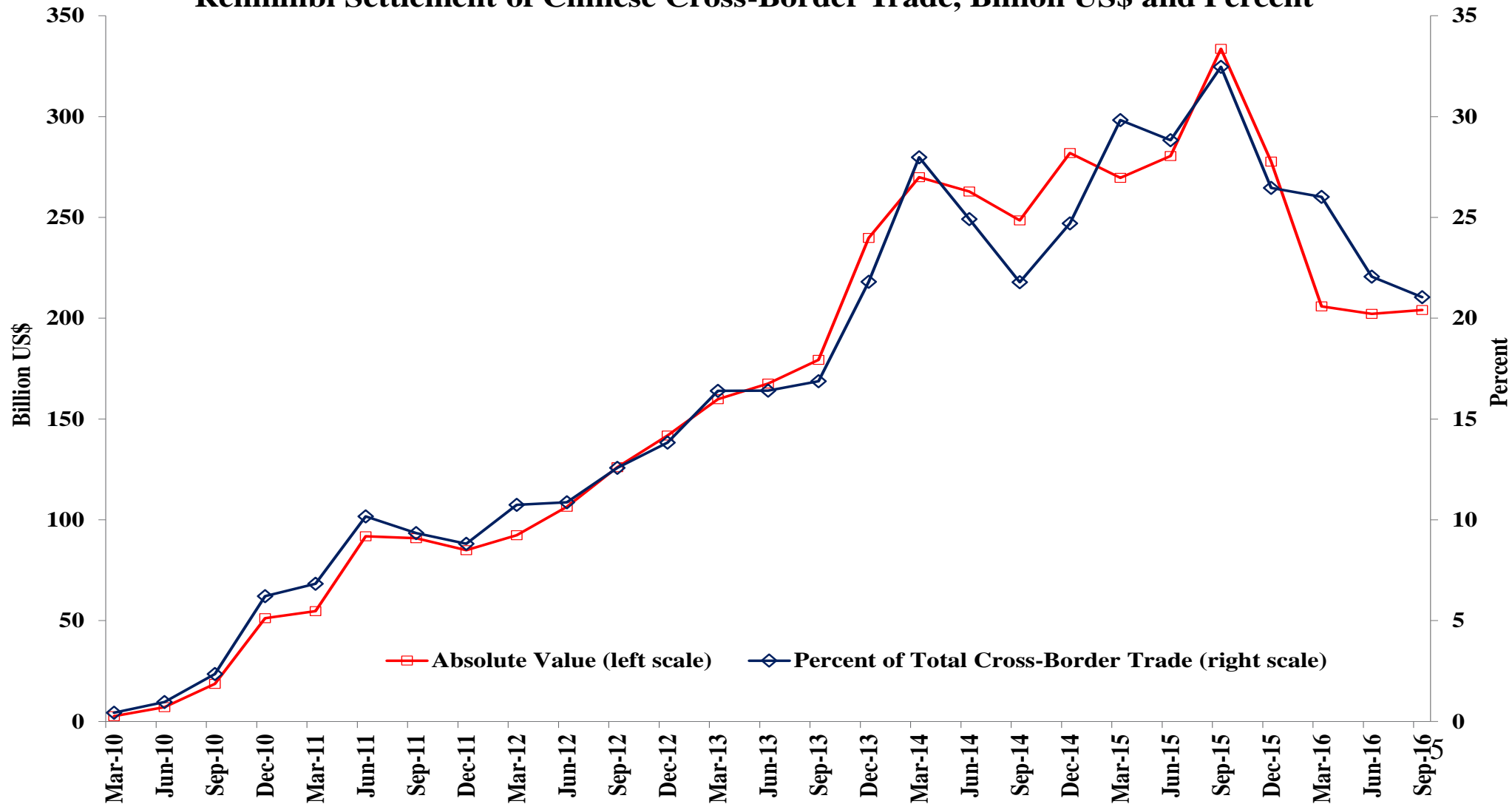
# Shares of World Settlement Currencies and World Trade of Currency Issuers, 11/2016

Shares of World Settlement Currencies and World Trade of Currency Issuers, November 2016



# Renminbi Settlement of Chinese Cross-Border Trade, Billion US\$ and Percent

Renminbi Settlement of Chinese Cross-Border Trade, Billion US\$ and Percent



# The Internationalization of the Renminbi

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- ◆ The exchange rate of the Renminbi relative to U.S. Dollar is likely to fall over 2017.
- ◆ It is in China's interests to promote the use of its own currency, the Renminbi, as a medium of international exchange, certainly in international transactions in which its national is one of the transacting parties. This requires a relatively stable exchange rate vis-a-vis the US\$.
- ◆ The Renminbi, being regarded as “freely usable”, has been included as part of the basket of major currencies (which includes the US\$, the Euro, the British pound and the Japanese Yen) constituting the “Special Drawing Rights (SDR)” basket, with a weight of 10.92%, which is higher than the British pound and the Japanese Yen. This has become effective on 1 October 2016.
- ◆ This should marginally increase the holdings of Renminbi as part of the foreign exchange reserves of foreign central banks and monetary authorities.
- ◆ Capital account convertibility is expected to be achieved before 2020. It can occur sooner if short-term capital flows, both outbound and inbound, can be appropriately “discouraged”.

# The Internationalization of the Renminbi

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- ◆ China will continue to face a net capital outflow, which is natural and expected as its enterprises (and in time its households) diversify their investment to overseas.
- ◆ However, this does not necessarily diminish its ability to stabilize the Renminbi exchange rate. It has large foreign exchange reserves in excess of US\$3 trillion as of the end of 2016, which is approximately one and a half years of worth of Chinese imports. It still runs a significant trade surplus in goods and services combined amounting to 3% of its GDP, or approximately US\$500 billion a year.
- ◆ China will over time become a large net capital exporter, especially as its enterprises and households attempt to re-balance their portfolios if and when capital controls are fully lifted. There will be a significant one-time stock adjustment when capital control is finally completely lifted.

# The Internationalization of the Renminbi

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- ◆ A devaluation is unlikely to be helpful to the Chinese economy. China does not want to return to making garments, shoes and stuffed toys with the lower standard of living that it implies. The Chinese economy has also become too large to be sustained by exports alone.
- ◆ It is also not in the best interests for China to compete with the other East Asian developing economies through competitive devaluation. China should be moving up the value chain, as Japan, Hong Kong, South Korea and Taiwan did before.
- ◆ The Renminbi has actually been appreciating relative to all the other major reserve currencies—the Euro, the pound sterling, and the Japanese Yen—as the U.S. Dollar.



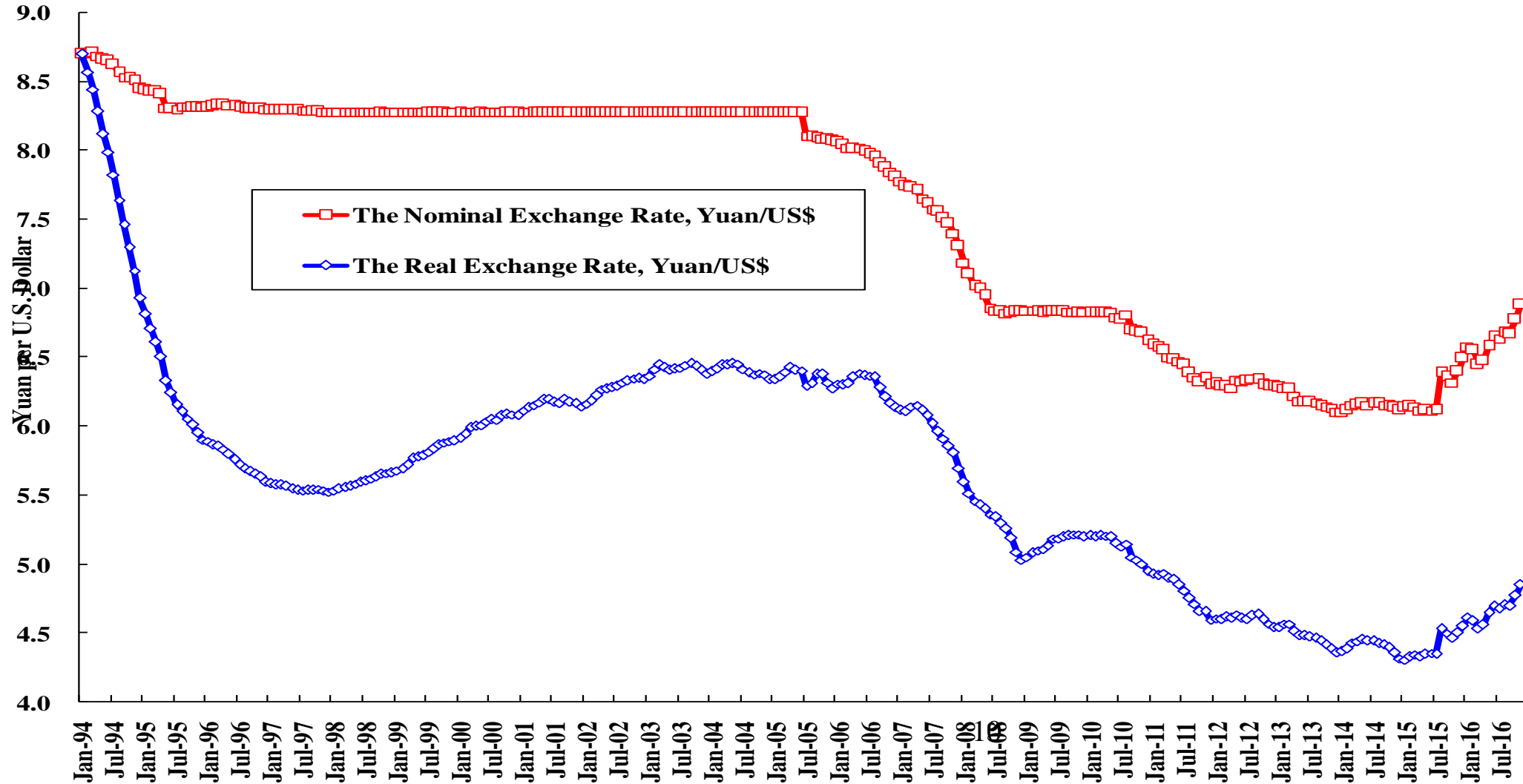
# The Internationalization of the Renminbi

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- ◆ However, with the rising U.S. rate of interest, the U.S. Dollar may be expected to continue to appreciate relative to all the other major international reserve currencies within the next year or two.
- ◆ Chinese exports to the U.S. accounts for less than 20% of total Chinese exports. Thus, it does not make too much sense for the Renminbi exchange rate to follow the U.S. Dollar, which means that Chinese exports will become more expensive to all other trading partner countries of China. It is therefore more reasonable for the Renminbi to follow an index of the exchange rate of a trade-weighted basket of currencies as the U.S. Dollar becomes super-strong relative to all other currencies.
- ◆ Thus, the Renminbi will appreciate with respect to all other currencies, but not as much as the U.S. Dollar. Relative to the U.S. Dollar, the Renminbi will devalue.
- ◆ However, when the U.S. Dollar eventually weakens, the Renminbi will also devalue with respect to all other currencies, but also not as much as the U.S. Dollar. Relative to the U.S. Dollar, the Renminbi will appreciate.
- ◆ In the long run, the Renminbi exchange rate, by following the exchange rate of a trade-weighted basket of currencies, will be more stable and less volatile than the U.S. Dollar.

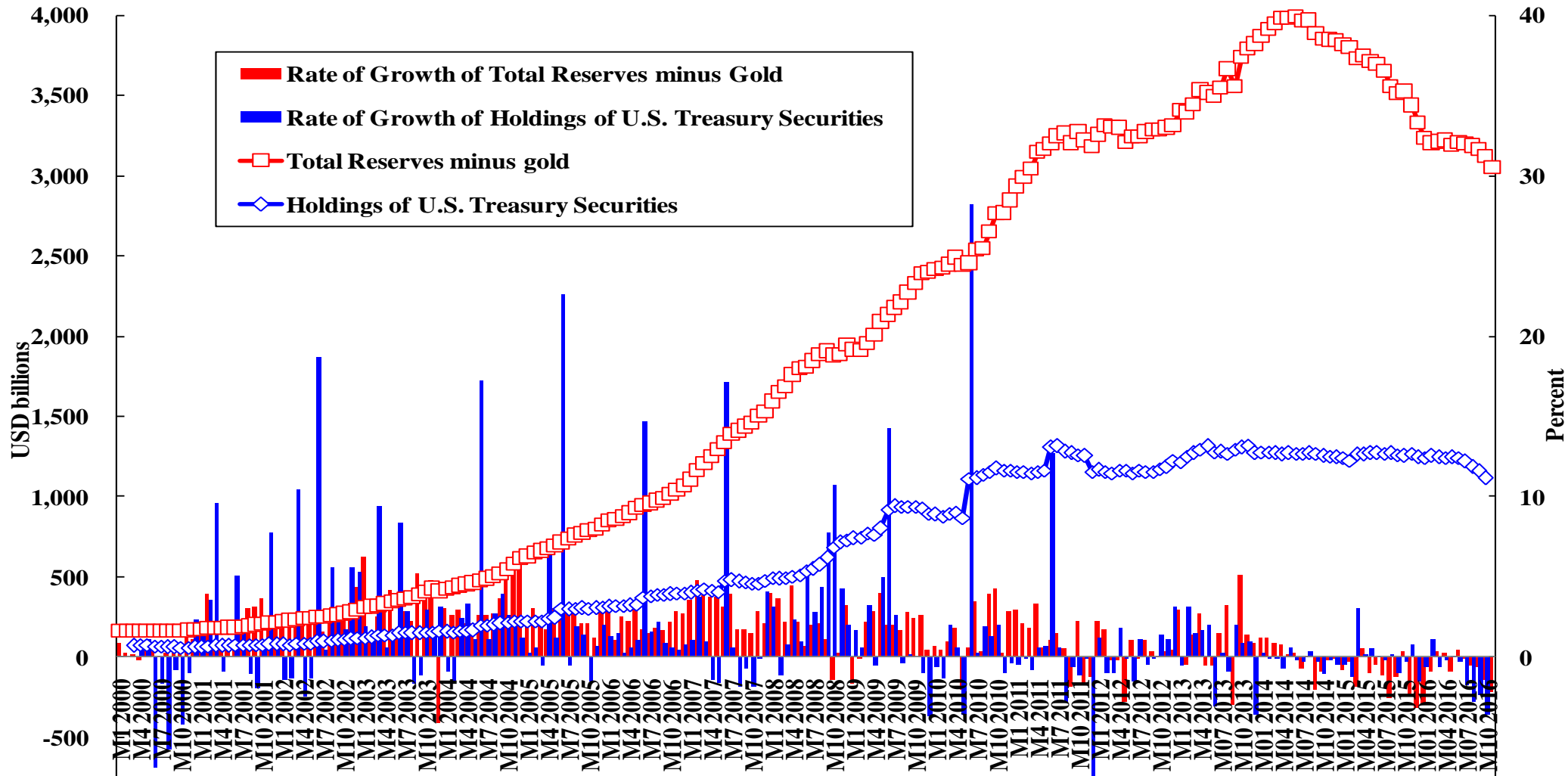
# The Nominal and Real Yuan/US\$ Exchange Rates

The Nominal and Real Yuan/US\$ Exchange Rates (1994 prices)



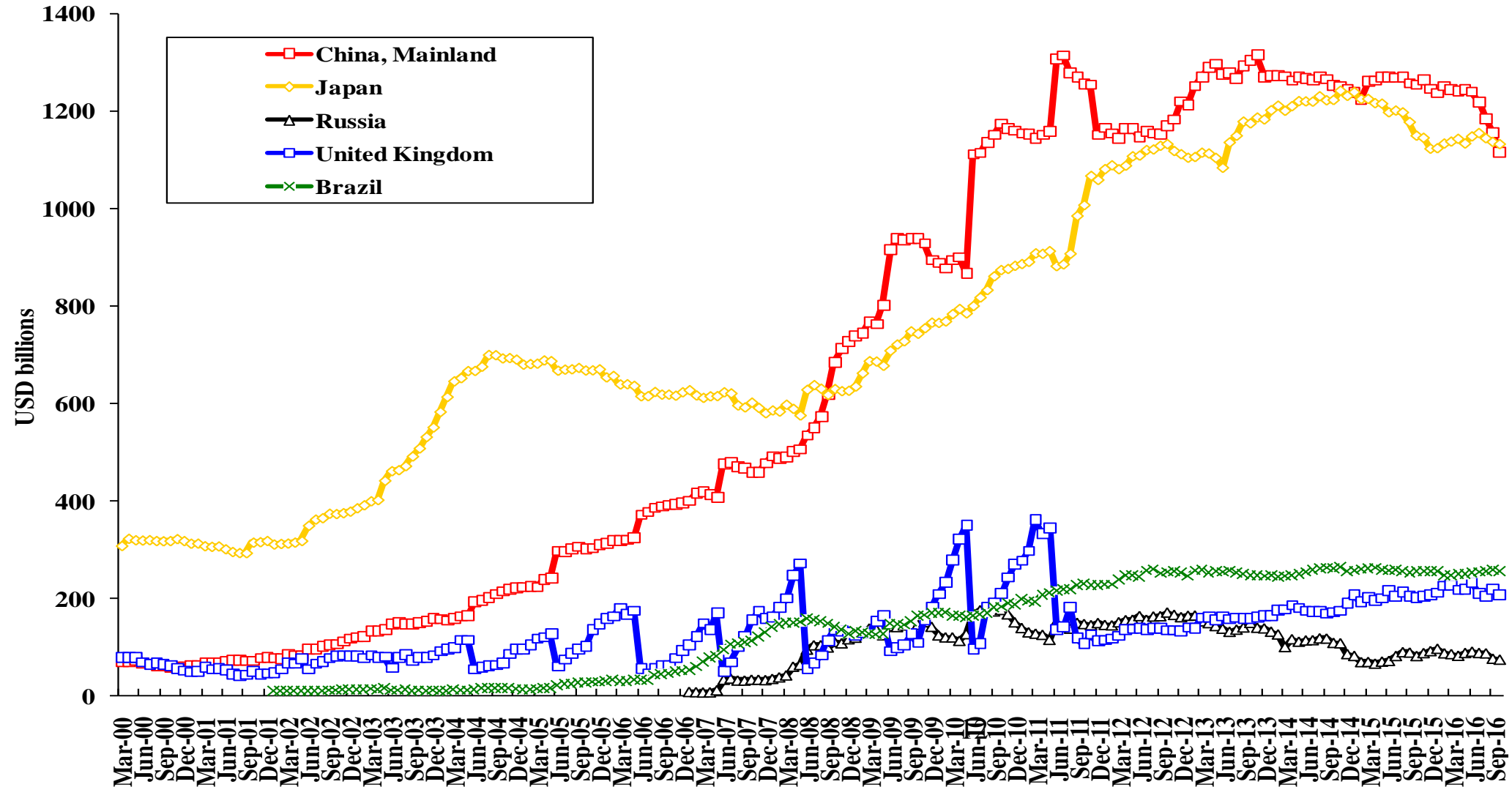
# Chinese Foreign Exchange Reserves and Holdings of U.S. Treasury Securities and Their Growth Rates, Month-over-Month

Chinese Foreign Exchange Reserves and Holdings of U.S. Treasury Securities and Their Growth Rates, Month-over-Month



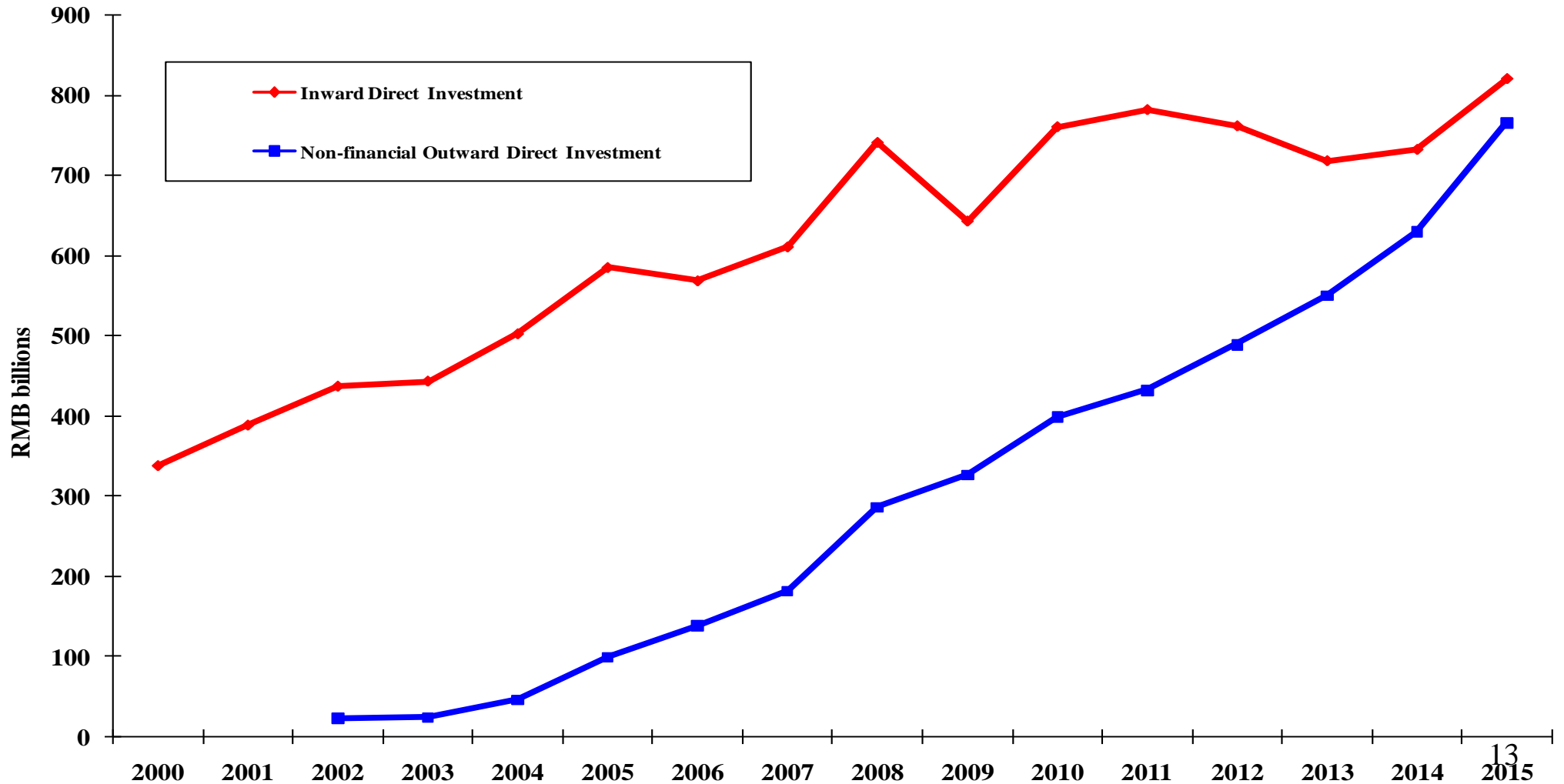
# Major Foreign Central Banks' Holdings of U.S. Treasury Securities

Major Foreign Central Bank's Holders of U.S. Treasury Securities



# Chinese Inbound and Outbound Foreign Direct Investment, in RMB Billions

Chinese Inbound and Outbound Foreign Direct Investment, in RMB billions



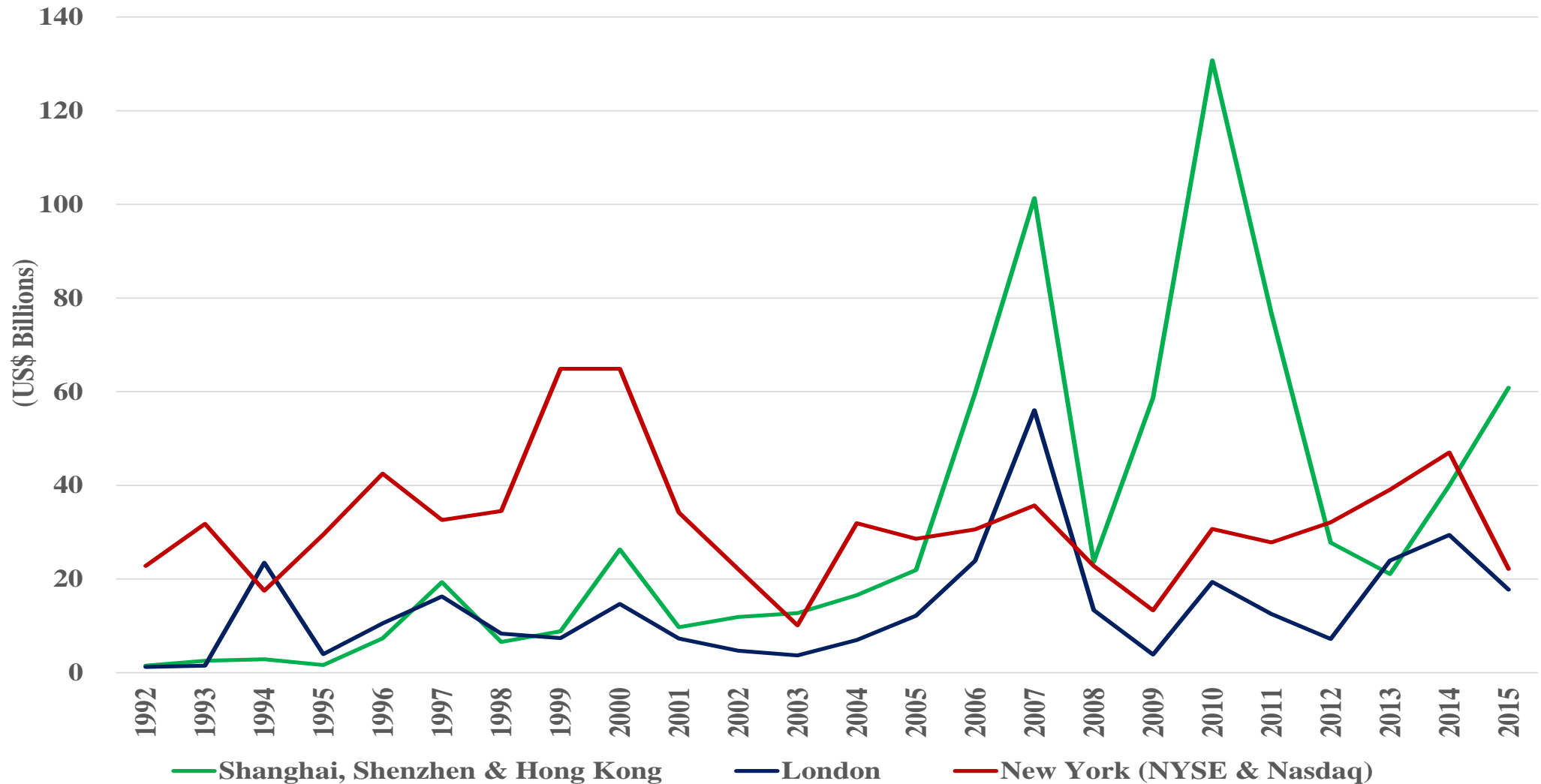
# China in the Global Economy—Capital Markets

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- ◆ The Chinese and Asian markets have been rising in importance in terms of the total amount of “Initial Public Offerings (IPOs)”. However, in terms of total market capitalization, they still lag behind the U.S. stock exchanges.

# Annual IPO Values for China (Hong Kong + Shanghai + Shenzhen), U.K. & U.S.A.

IPO Values for Selected Regions



# Market Capitalization of Stock Exchanges

## Year End 2014 and 2015(US\$ trillion)

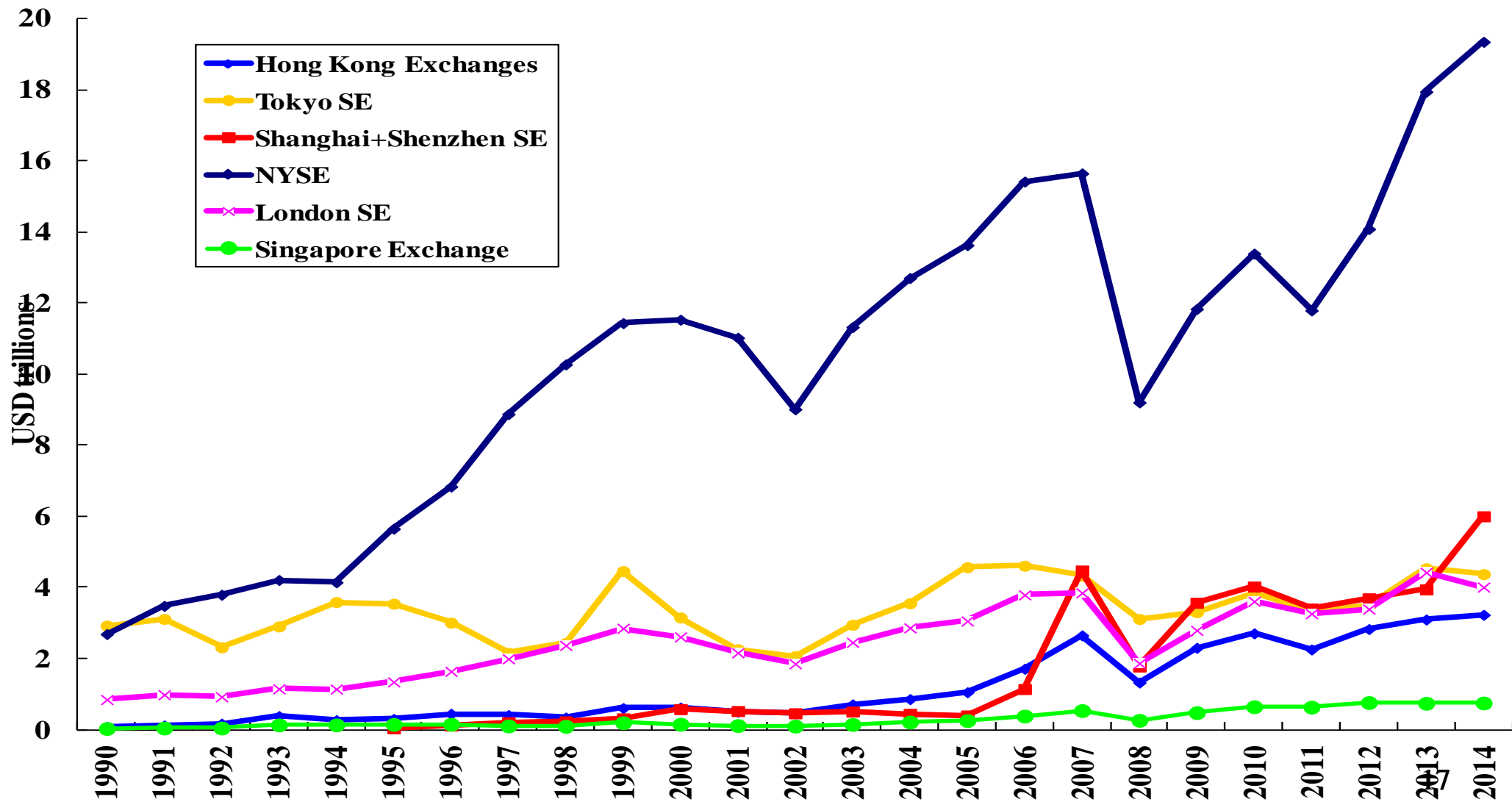
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	2014	2015
◆ U.S.A.	26.3	25.9
◆ Europe	12.1	7.8
◆ East Asia	18.0	19.5
◆ Exchanges:		
◆ U.S.A.: NASDAQ and NYSE		
◆ Europe: Athens Exchange, BME Spanish Exchanges, Budapest SE, Cyprus SE, Deutsche Borse, Irish SE, London SE group, Luxembourg SE, NYSE Euronext (Europe), Oslo Bors, SIX Swiss Exchange		
◆ East Asia: Bursa Malaysia, Hong Kong Exchanges, Indonesia SE, Korea Exchange, Philippine SE, Shanghai SE, Shenzhen SE, Singapore Exchange, Taiwan SE, Thailand SE, Tokyo SE Group		
◆ Data source: World Federation of Exchanges		



# End of Year Market Capitalization of Selected Stock Exchanges

End of Year Market Capitalisation of Selected Stock Exchanges, in USD trillions



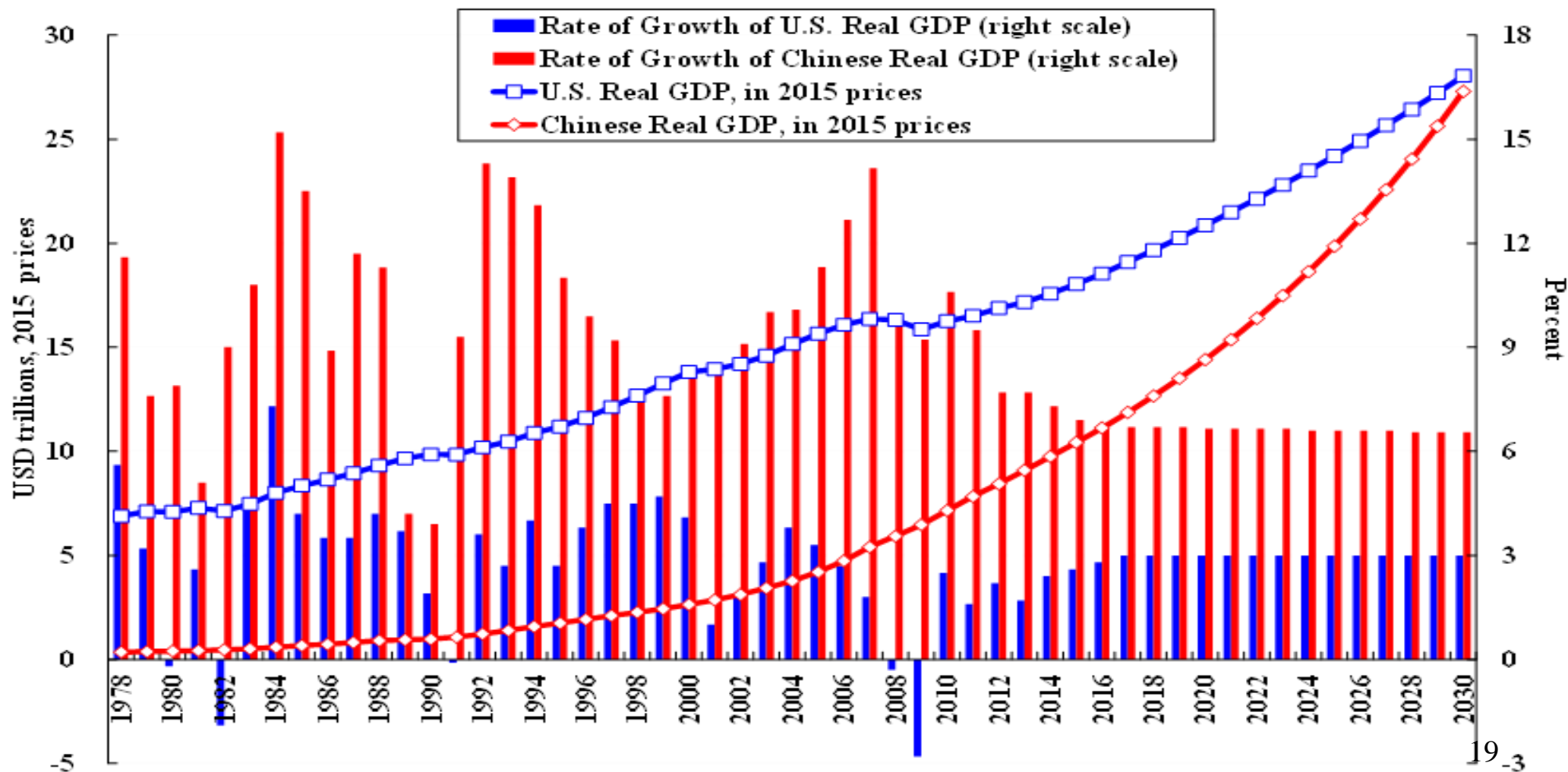
# Projections of the Future

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- ◆ It is projected that the Chinese and the U.S. economies will grow at average annual real rates of approximately 6.6% and 3.0% respectively between 2016 and 2030. Chinese real GDP is projected to catch up to U.S. real GDP around 2030, at which time both Chinese and U.S. real GDP will exceed US\$28 trillion (in 2015 prices), almost three times the Chinese GDP and approximately one and a half times the U.S. GDP in 2015. By that time, China and the U.S. will each account for approximately 15% of world GDP.

# Actual and Projected Real GDPs and their Annual Rates of Growth: China & the U.S.

**Actual and Projected Chinese and U.S. Real GDPs and Their Rates of Growth  
(trillion 2015 US\$)**



# Projections of the Future

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- ◆ By 2030, the Chinese real GDP per capita is projected to reach 19,000 (in 2015 prices), which would still be less than a quarter of the projected then U.S. real GDP per capita of US\$77,000. It will probably take until 2060 for China to catch up to the United States in terms of real GDP per capita.

# Concluding Remarks

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- ◆ The center of gravity of the world economy has been gradually shifting to East and South Asia. The center of gravity of the East Asian economy has been gradually shifting to China.
- ◆ The Chinese and East Asian economies have been partially decoupled from the United States and Europe.
- ◆ Will the Chinese economy be able to avoid the “Middle-Income-Trap”? The answer is yes.
- ◆ The Chinese economy will catch up to the U.S. economy in terms of aggregate GDP some time around 2030. However, it will be past the middle of this century, perhaps around 2060, before the Chinese economy can catch up to the U.S. economy in terms of per capita GDP.