
Regionalization of Renminbi: A Tale of Taiwan and Hong Kong

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Using More RMB

- Goal of trading with direct currency:
 - To avoid transaction cost
 - To avoid additional exchange rate fluctuation (as well as hedging expense)
 - However, when being an international currency, it needs more stability to encourage use, probably also less regulation on free flow.
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Taiwan's Strategy

Timelines and Legal Framework

- 2009 . Cross-strait Financial Cooperation Agreement (ECFA, 海峽兩岸金融合作協議) and the MOU on banking supervision between Taiwan and mainland China were signed and later ratified.
 - August 31, 2012. Taiwan and mainland China signed the Memorandum on Cross-strait Currency Clearing Cooperation (海峽兩岸貨幣清算合作備忘錄) .
 - The memorandum allows Taiwanese institutions to offer yuan-denominated settlement services.
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Development and Public Stance

- Some optimism. In 2012 and 2013. RMB market boomed.
 - But in 2014, Sunflower Movement and the setback of service trade pact with China quieted discussion.
 - But due to the delayed approval of Cross-Strait Agreement on Trade in Services in 2014, an anticipated currency swap mechanism is also postponed.
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Current Status

- Moving forward, in a slow and steady pace.
 - RMB-denominated bonds, fund, insurance products abound, sold through either local platform or via Hong Kong.
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More than 300 bn RMB in Deposit

銀行人民幣存款餘額

單位：人民幣億元



註：DBU是外匯指定銀行；OBU是國際金融業務分行

資料來源：中央銀行

Asset and Payment

- Asset in RMB is more than twice of deposit.
 - Payment system
 - Monthly RMB settlements hit 393 billion (2015/9. 286 bn in 2014/10).
 - However, loan is small
 - By end of August 2015, the outstanding loan conducted by Taiwanese banks is about 20 bn RMB. (18 bn as of end of September 2014)
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Trade Surplus: 75 bn USD in 2014

- According to data in 2014, China (HK and Macau included) is Taiwan's largest trade partner, with a trade surplus of 75 billion US dollar that year (124.8 bn export, 49.7 bn import), the fifth year in a row with surplus more than 70 billion USD.
 - For export, mostly optical instruments/parts (ranked 2nd, 15.7 bn USD) and electrical/machinery/telecommunication equipment and parts (ranked 1st, 59.6 bn USD).
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Hong Kong's Edge

Timeline and Background

- Trade surplus and foreign capital inflows have led to a rapid swelling of China's reserves, causing a “monetary indigestion”.
 - To ease this pressure, in 2009 China officially allowed cross-border trade settlement in RMB in a pilot scheme covering five Chinese cities.
 - The year 2010 saw what was arguably the first “Big Bang” event for RMB internationalization. Hong Kong signed a clearing amendment agreement with Mainland China
 - Under which all corporates and institutions from anywhere in the world could open RMB bank accounts in Hong Kong, and funds in RMB bank accounts became freely transferrable.
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The Largest Offshore RMB Centre

● Advantages

- Strong infrastructure, diverse products
 - Regulatory institutions that uphold the rule of law
 - Open economy with free capital and information flows
 - Tie between Mainland China and Hong Kong, summed up by “One Country, Two Systems”
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Deposit and Payment

- Strong liquidity.
 - At the end of 2014, RMB customer deposits and certificates of deposit issued by banks in Hong Kong together amounted to over 1.1 trillion.
 - In 2014, renminbi trade settlement handled by banks in Hong Kong grew over 60% year on year to the total RMB6.3 trillion.
 - The average daily turnover of the renminbi Real Time Gross Settlement (RTGS) system exceeded RMB 880 billion yuan in December 2014.
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Bond Market, Loan and Funds

- The outstanding bonds amounted to RMB 381 billion at end-2014. More than 100 issuers issued bonds totaling RMB 197 billion over the whole year.
 - The outstanding amount of renminbi loans in Hong Kong rose by over 60% year on year to RMB 188 billion at end-2014.
 - At end-2014, the outstanding amount of listed renminbi funds in Hong Kong was RMB 53 billion, while unlisted funds amounted to RMB 40 billion yuan.
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Prospect

- Policy: one-way inflow is over.
 - In the meanwhile, China is dealing with several issues. Including,
 - Economy growth
 - Inflation
 - Exchange rate fluctuation
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Hub and *the Race*

Centers in a Race

- China has appointed renminbi clearing banks in Singapore, London, Luxembourg and Taipei and other locations. 15 in total, by June 2015.
 - Agreeing currency swap lines with 32 central banks.
 - Each hub is fulfilling different roles and that they are not necessarily competing directly with each other, even as the total pie is growing.
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London catching up

- RMB trade volumes in London more than doubled in 2014.
 - Average daily volumes reached **US\$61.5 billion** and spot trading volumes stood at US\$18.4 billion dollars per day in 2014, up more than three times compared with the previous year.
 - While London is dominant in global foreign exchange trading, Hong Kong is currently the biggest offshore renminbi centre. Daily turnover through its clearing and settlement platform exceeded 880 billion yuan (**US\$142 billion**) in December 2014.
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Taiwan's Strategy Reconsidered

Criticism

- Taiwan's banks are complaining government's inaction.
 - For example, 15 % of income tax of bond yield bars many Chinese issuers from issuing their bond in Taiwan.
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Evaluation

- Comparative advantage?
 - Taiwan's government seems okay.
 - Reasons?
 - More tools and channels available
 - Considering the economic investment (and probably political investment) needed to be a successful hub
 - Lack of political consensus
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Evaluation

● Domestic environment

1. Political unease, inside and outside
 2. Financial industry competitiveness
 3. Regulatory philosophy
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“Wall Strategy”

- More stability at the expense of loss of efficiency.
 - Survived from the ‘97, ‘01, and ‘08 crises.
 - Mid-size (and limited) financial industry
 - The market capitalization of the top two groups are a bit less 20 bn USD, and the third and fourth are both about 10 bn USD.
 - In contrast, TSMC is about 7 times larger of the largest financial firm.
 - For the top 25 largest companies in Taiwan, only four of them are banks/financial groups.
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“Wall Strategy” Continued

- Largest national wealth among Asian Tigers, according to Credit Suisse 2015 Global Wealth Report.

- Taiwan 3.59 trillion USD, Korea 3.55, Hong Kong 1.07, Singapore 1.09.

- Wealth distribution, ranked 2nd

- Gini index 0.727, Singapore 0.708, Hong Kong 0.837, Korea 0.738

- Social justice, universal health care and democracy.

Current Steps on Integration

1. Expansion in ASEAN countries (162 branches in total, 32% of growth in two years)
 2. Demand more frequent filing and risk assessment, and tighter scrutiny in risk exposure, for branches in Mainland
 3. Fintech development (data securities, identification)
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Back to Hong Kong's Dilemma

- Hong Kong, Singapore, Taipei, London, Frankfurt, Luxembourg. And the list can go on and on....
 - Each of these centers serves different purposes?
 - But are all going to survive?
 - As a leader, HK faces competition from both ends:
 - London has time-zone advantage, with similar institutional advantages
 - Shanghai Free-Trade Zone and its policy support
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Shrinking Market

● “This year, dim sum bond market sees a substantial decline as China speeds up the opening of the far bigger domestic renminbi credit market.

- In May, more than 30 overseas financial institutions, including HSBC, Morgan Stanley and BNP Paribas, were given regulatory approval to access the interbank bond market by the People’s Bank of China.

- In mid-July, the PBoC allowed central banks, supranational organizations such as the World Bank and sovereign wealth funds buy onshore bonds without the need for prior approval.”

--- *Josh Noble, Appetite wanes for dim sum bonds as entree to renminbi investment, FT, July 29, 2015.*

Comparative advantage

- Still, dim sum market has its first-mover advantage, as well as implicit political support
 - Better legal protection counts.
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Uncertain China: Economic Side

● Marco Economic Backdrops

- Lower economic growth
 - High household saving
 - local fiscal discipline and large borrowing
 - decreasing trade surplus, as foreign expansion continues
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Uncertainty Ahead: Political Side

- Capital control
 - Full convertibility and the elimination of onshore/offshore line
 - China's exchange-rate controls still cast a long shadow over the market's infrastructure.
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Summary

- Wider use of RMB:
 - The Chinese currency was used in January-April for 31 per cent of payments between China (including Hong Kong) and the rest of the Asia-Pacific region, up from 7% back in April 2012
 - Two key ingredients of crises are deregulation and leverage, and China has both in spades.
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Conclusion

- The RMB has grown fast over the past four years, from the trade settlement perspective.
 - This trend is expected to continue.
 - With the slowdown of currency appreciation, RMB will face its challenge if its earlier pace of expansion needs to continue.
 - National strategy depends on each place's goals and cost.
 - Probably more importantly, it is about time for Chinese officials to think about how to control situations (or what to do) when things go wrong in offshore centers.
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