

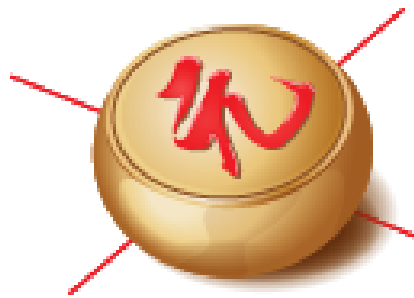
Renminbi's Future as a Reserve Currency



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RENMINBIWORLD 2015

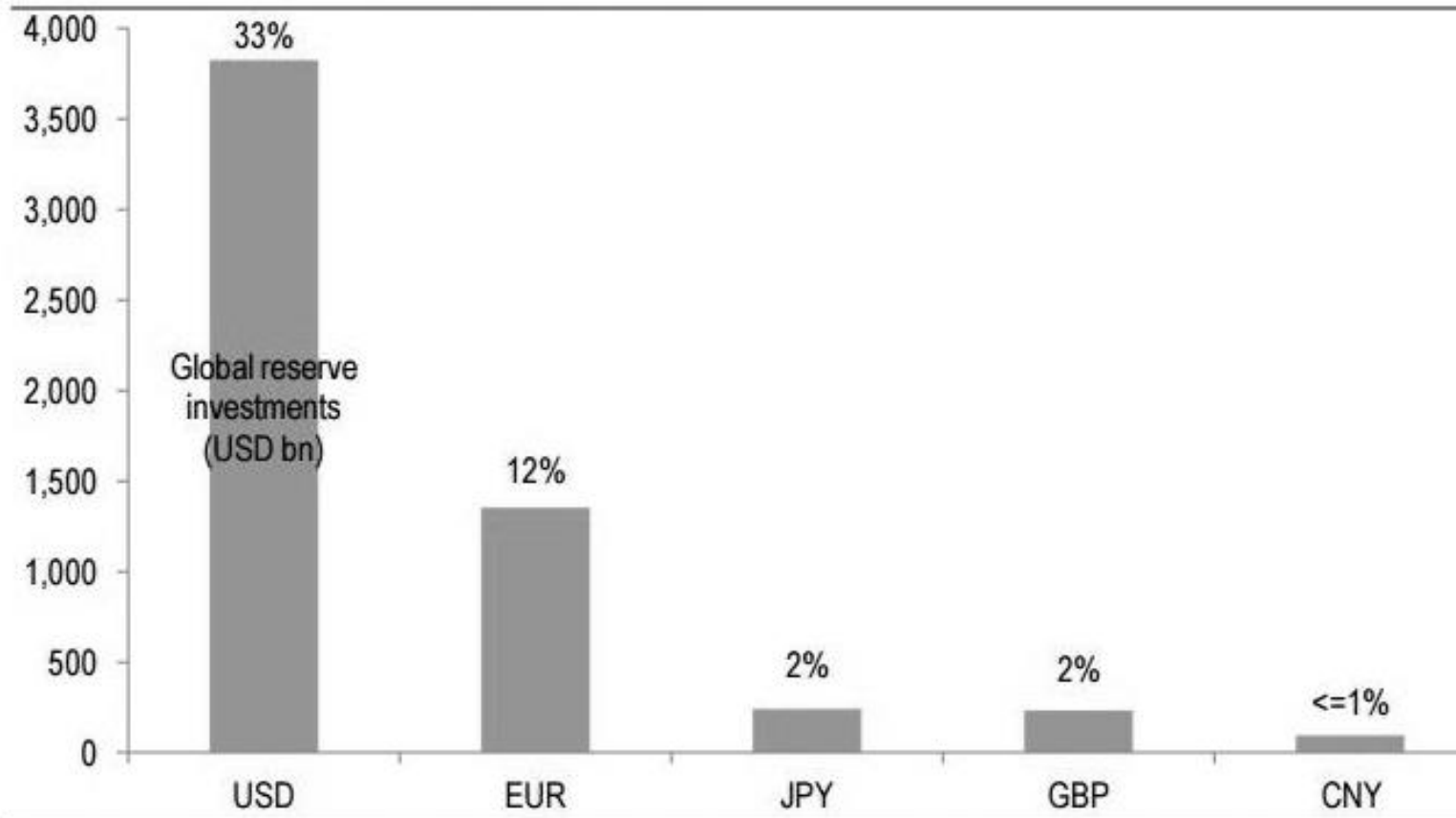
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The issue of the RMB's future as a reserve currency brings up a number of fundamental questions:

- What exactly is a reserve currency?
- What are the characteristics of a reserve currency?
- How does a country's currency become a reserve currency?
- What are the pluses and minuses of being a reserve currency?
- How does a currency lose its reserve currency status?



RMB is not a meaningful reserve currency today:



Note: CNY allocation is estimated by Standard Chartered Research; Source: IMF, Standard Chartered Research



SDR's and the RMB

- In fact, the RMB is not recognized by the IMF as part of its supplementary foreign exchange reserve assets known as Special Drawing Rights, or SDR's
- SDR's are composed of a basket of currencies with weights assigned to take into account their current prominence in terms of international trade and national foreign exchange reserves
- SDR's today:
 - US dollar 41.9%
 - Euro 37.4%
 - Japanese Yen 9.4%
 - British Pound 11.3%
 - Chinese Renminbi 0.0%
- The basket and weights are reviewed every 5 years, and the RMB may be included as early as tomorrow



The Renminbi will be included in SDR's now or in the future

- China has the international trading volume to be included
- Liquidity is improving
- Clear steps are being taken to improve convertibility, but more remains to be done



To consider where the RMB is going, it is useful to look at where it has come from

- I have a somewhat unique perspective
- In 1993 I was hired by the People's Bank of China to help modernize the institution
- Worked with PBOC as an independent advisor or broker for over the next 15 years



Let me give you some vignettes from that time

- Since China was a closed country for decades without functioning capital markets, it is understandable that there was a knowledge gap
- The "Trading Room"
- Assets of less than US\$10 billion
- No computer systems
- No trading systems or screens
- No risk management systems or procedures
- People the smartest of the smart, but inexperienced on how global bond and currency markets worked

Given how far China has advanced in just 22 years, do not underestimate where the RMB will be in 10 years





PBOC today (Trading room is the circular part of the building in front)



Foreign Exchange Reserves (Forget the BRICS)

China 1993 <\$10 billion

World Rank

#

1	China	\$3,514 Billion
2	Japan	\$1,248
6	Russia	\$ 371
8	Brazil	\$ 361
9	India	\$ 351
18	United States	\$ 121



- Note: Large Foreign Exchange Reserves beyond US\$ trillion may be more of a liability than a benefit
- For China, those funds are stuck primarily in low yielding Treasuries, agencies and other country debt
- One of the big opportunities for bankers is to help recycle those funds more productively



There have been few true “reserve currencies” throughout history, including:

- The Greek drachma
- Roman denarius
- Byzantine solidus
- Venetian ducato
- Dutch guilder
- British pound
- US dollar



Observations

- Reserve currency status is not forever
- Issuing country must be a leader in international trade
- Benefit for others to engage in trade with the issuer and hold the resulting currency as a store of value
- Military power secondary after trade, but supports trade in the currency
- Must be convertible from one store of value to another



Desirable reserve currency and country characteristics

- Leader in international trade
- Stable value
- Convertible
- Economically strong and improving issuing country
- Issuing country must have a strong, transparent and enforceable legal system
- Military capability not key but a sign of stability
- Low inflation
- Fiscal surplus of issuing country
- Philosophy of issuing country to think not just about their interests, but also those of the holder of the currency
- Trade surplus of issuing country



Forecasts:

As China moves to make the Renminbi fully convertible it will

- Become a widely accepted as a reserve currency
- Overtake the Yen and Sterling in 5 years
- Overtake the Euro to challenge the Dollar in the next 10 years

