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Flash Notes

China: Direct Trading Of RMB With SGD Commences

- More than one year after the announcement, direct RMB-SGD trading will commence tomorrow, 28 Oct 2014 as the pace of RMB internationalization accelerates further
- The latest development should boost the appeal of offshore RMB in the region, given Singapore's role as a financial center and the increased trade and investment linkages between ASEAN and China. The potential of RMB's acceptance and usage in ASEAN should rise along with the increased influence of China as well, and the direct SGD and RMB trading could be a main catalyzer.
- In terms of outlook for the RMB itself, direct quoting is unlikely to have significant impact near term, although increased internationalization means that 2-way fluctuations of the currency will be here to stay, in place of the one-way appreciation. The RMB is on track to meet our target of 6.10/USD for end-2014 from around 6.12/USD currently and we are optimistic of upside for the RMB towards 6.00-6.05/USD by end-2015.

Direct Trading Of RMB-SGD To Start On Tuesday

More than one year after the announcement from MAS (see our report "China: Direct Trading of RMB with SGD To Start", dated 22 Oct 2013), direct trading between RMB and SGD finally commences, starting from 28 Oct 2014 (Tue).

Based on announcement from PBoC today (Mon, 27 Oct 2014), the Mainland-incorporated entities of the three Singapore banks will be part of the panel of market makers for the SGD direct trading, joining the likes of major China banks including ICBC, ABC, BOC, among others, and several foreign banks (Source: http://www.chinamoney.com.cn/fe/Channel/22308).

The SGD thus becomes one of the handful of currencies that are quoted directly against the RMB to date, rather than crossing out via a third currency (typically USD). Other directly quoted currencies are the euro, Japanese yen, sterling, Aussie, NZ dollar, Malaysian ringgit, and Russian ruble (please see table below).

Operationally, the setting of the CNY-SGD daily midpoint will be similar to that of other directly traded currencies. Prior to the start of each trading day, CFETS (China Foreign Exchange Trade System) will inquire prices from market makers (also called liquidity providers), and calculates the average of the quotes as the central parity of RMB against SGD, and published at 915am each trading day. The trading band for the CNY-SGD will be +/-3% from the midpoint (as opposed to, e.g. +/-2% band for the USD/CNY), according the announcement (Source: http://www.chinamoney.com.cn/fe/Info/9426087).

Currencies Trading Directly Against RMB

Currency	Commenced
US Dollar (USD/CNY)	July 2005
Malaysian ringgit (CNY/MYR)	19 Aug 2010
Russian ruble (CNY/RUB)	22 Nov 2010
Japanese yen (100JPY/CNY)	1 Jun 2012
Australian dollar (AUD/CNY)	10 Apr 2013
NZ dollar (NZD/CNY)	19 Mar 2014
British pound (GBP/CNY)	19 Jun 2014
Euro (EUR/CNY)	30 Sep 2014
Singapore dollar	28 Oct 2014

Source: CFETS, UOB Economics & Markets Research compilation

RMB Internationalization Gathering Speed

The direct trading of RMB-SGD is adding to evidence that the administration under Pres Xi Jinping and Premier Li Keqiang is boosting the pace of RMB internationalization much faster compared to the previous administration. This is reflected in recent official announcements and implementations, compared to those announced in the past years.

For instance, so far in 2014, there are already four currencies (including SGD) added to the ranks of direct trading against the RMB. This is a huge improvement compared to just one currency (AUD) in the entire year of 2013, and in 2012 (Japanese yen).

In addition, as we had observed earlier, the Chinese government announced altogether a total of 5 offshore RMB centers in the period between June and July this year, from Seoul in East Asia to London, Frankfurt, Paris, and Luxembourg in Europe. This means that in one fell swoop, offshore RMB trading encompasses the range from East Asian time zone to European time zone. This is a far faster pace compared to years past, where basically one offshore center was announced each year: 2010 for Hong Kong, 2012 for Taipei, and then 2013 for Singapore, all of which are located in the Asian time zone (GMT+8).

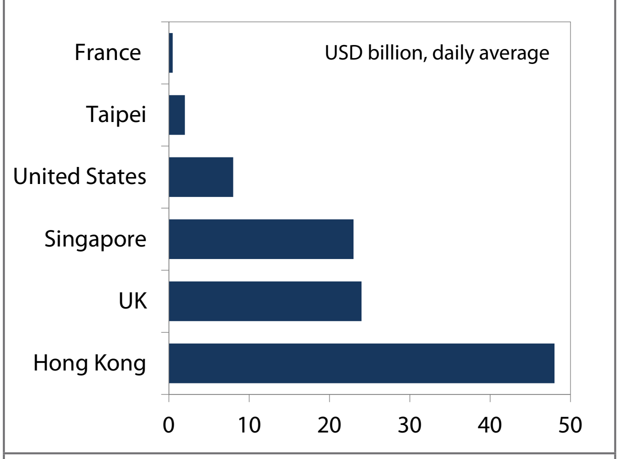
On China's capital account front, steps are also being taken to widen the channels of capital flows, with the impending Shanghai-HK Stock Connect being one of the bolder moves which will involve individual investors (for more details on the "through train" scheme, please refer to our note: "China: The Shanghai-HK Through Train–Pushing Ahead Market Reforms" dated 03 Sep 2014). In addition, the Chinese authorities are also considering widening the current QDII (Qualified Domestic Institutional Investor) programs to individual investors as well, and expanding the eligible assets that QDII programs can access outside of China. At the same time, the Chinese authorities are also looking to expand the QFII (Qualified Foreign Institutional Investor) program to allow individual foreign investors to invest in Mainland asset, under the so-called QDII2 and QFII2 programs.

Implications Of The Latest Development

Over time, direct quoting against the RMB will certainly add further to liquidity and volume in the offshore RMB market. Singapore's position as the largest FX trading center in Asia and a financial hub in the region will also boost RMB's role given increased economic activities between ASEAN and China. According to IMF, offshore RMB trading volume in Singapore is on par with London, and it is likely that direct RMB-SGD trading will further enhance Singapore's position as an offshore RMB center (see chart below).

Based on our projections, we expect China's share in ASEAN's total trade to rise from 16% in 2013 to more than 22% share by 2030. This suggests that the potential of RMB's acceptance and usage in ASEAN should rise along with the increased influence of China as well, and the direct SGD and RMB trading could be a main catalyzer. While the RMB may not rival USD's position anytime soon, it is conceivable that the Chinese currency could become a viable alternative currency (medium of exchange, unit of account, and store of value) in the future as trade and investment links between ASEAN and China grow.

RMB OTC Foreign Exchange Turnover: Apr 2013



Source: IMF Country Report: Hong Kong 2014, No. 14/132, p 21

For both Mainland and Singapore businesses, especially importers and exporters at this early stage, will be able to benefit from the narrower spreads from direct trading of RMB-SGD, as they need not incur the trouble and costs of going through another third currency, which is US dollar in majority of the cases. This will thus encourage further interest in using the RMB and thus broadening its liquidity and appeal.

China overtook Malaysia for the first time in 2013 to become Singapore's number one trade partner (total trade) at S$115bn (vs. S$114bn with Malaysia), to account for 12% share of Singapore's total trade that year, up from sub-10% share, or S$92bn, in 2008, just prior to the global financial crisis. This means that increased usage of the RMB, would increase the liquidity of the offshore RMB in a significant, with every 1% would add in more than S$1bn, vs. deposits of RMB254bn (S$53bn equivalent) as of June 2014 in Singapore.

In terms of outlook for the RMB itself, direct quoting is unlikely to have significant impact near term, although increased internationalization means that 2-way fluctuations of the currency will be here to stay, in place of the one-way appreciation that one has been so accustomed to in the past. The RMB appreciated 37% against the USD from July 2005-2013, and if SGD were to strengthen in such a manner, it would be close to 1.05/USD today, from around 1.67/USD in mid-2005. The RMB is on track to meet our target of 6.10/USD for end-2014 from around 6.12/USD currently and we are optimistic of upside for the RMB towards 6.00-6.05/USD by end-2015, bearing in mind potential for greater 2-way moves ahead as RMB internationalization progresses.