

China: Further Expansion in RMB Internationalization

The Monetary Authority of Singapore (MAS) announced last Friday (13 June):

1. a facility for providing overnight Renminbi (RMB) liquidity to financial institutions in Singapore to be launched on 1 July 2014; and
2. a directive issued on the same day by the People's Bank of China (PBoC) Nanjing branch that will allow eligible corporates and individuals in the Suzhou Industrial Park (SIP) to conduct cross-border RMB transactions with Singapore.

According to the MAS, the overnight RMB liquidity facility will provide up to RMB5 billion in overnight funds on any given day, which will further bolster market confidence by giving financial institutions the assurance that their short-term RMB funding needs would be met. The facility complements the existing MAS RMB facility that allows banks to borrow RMB funds on a term basis for trade, direct investment and market stability purposes. MAS will release further details of the overnight RMB liquidity facility on 1 July 2014.

As for the SIP cross-border RMB initiative, the PBoC's directive will allow for a range of cross-border transactions:

- i. Banks in Singapore can conduct cross-border RMB lending to corporates in SIP;
- ii. Corporates in SIP can issue RMB bonds in Singapore;
- iii. Equity investment funds in SIP can conduct direct investment in corporates in Singapore; and
- iv. Individuals in SIP can conduct RMB remittance between China and Singapore for the settlement of current account transactions and direct investment in corporates in Singapore.

Implications

The latest initiative between China and Singapore marks another step towards the expanded use of RMB in cross border transactions for both corporates and individuals based in SIP, allowing for wider channels of two-way funds flows into and out of China within the context of its largely closed capital account.

For companies located in SIP, the program will allow them to raise RMB funding at a lower cost via Singapore. For Singapore as an offshore RMB center, the latest development offers another avenue to deploy excess RMB funds back to mainland China, which will bode well for more investment options in RMB.

The plan for SIP companies is part of the agreement reached at the 10th Joint Council for Bilateral Cooperation on 22 October 2013 to strengthen China-Singapore financial cooperation, and is now moving towards implementation. The availability of the overnight RMB facility from the MAS, in addition to the existing term facility, will be supportive of the use of the Chinese currency in Singapore with assurance of the availability of funds, which goes toward strengthening the competitiveness of Singapore as an offshore RMB centre.

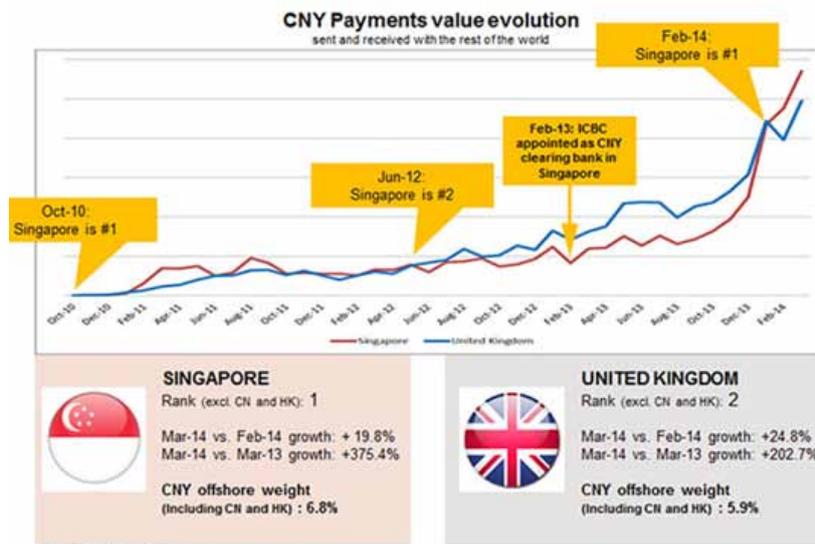
Singapore has been playing a critical role in the internationalization of RMB since becoming an offshore center in May 2013, with RMB deposits rising 70% from March 2013 to RMB200bn at end-2013, according to the MAS. Though the progress is significant, it is still behind Hong Kong's RMB deposit base of RMB 959.9 billion (end-April 2014), and Taiwan's RMB268.4

billion (end-March 2014). In all, offshore RMB deposits globally are likely to have exceeded RMB1.5 trillion (including those from London, Luxembourg, South Korea, among others), it is still just about 1% of the onshore deposit base of RMB110 trillion (as of May 2014), suggesting significant headroom for growth in offshore RMB.

Latest data from SWIFT also shows that Singapore has been making progress on the RMB payments front, overtaking London as the world's top clearing center, outside of China and Hong Kong. Singapore accounts for 6.8% of all offshore RMB-denominated currency payments in March 2014, compared with 5.9% for London and 2.4% for the US, according to SWIFT, but pales in comparison to Hong Kong's share of 72%.

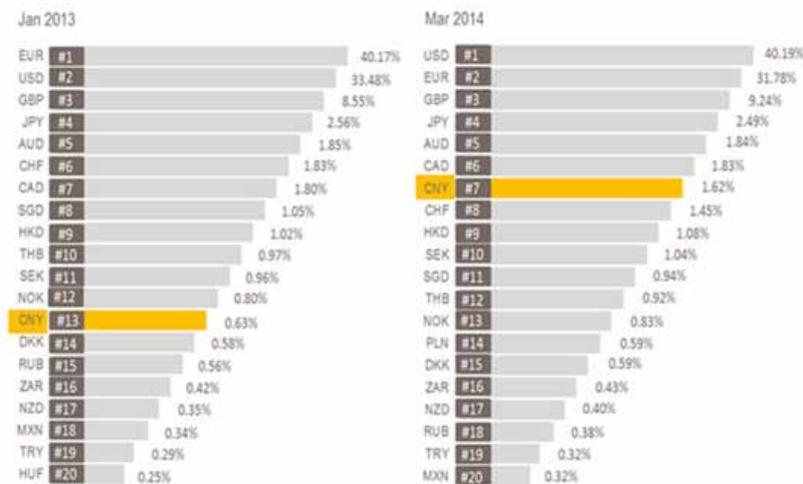
The close race between these two non-China offshore centers (shown in chart below) suggests that competition will remain keen, with more centers likely to join in the race, but at the same time the potential for growth is significant given the small shares occupied outside of the greater China, as well as the rising use of RMB as a payment currency (ranked at 7th largest in March 2014, from 13th in January 2013, as shown in the chart below).

Singapore Overtakes London as Top RMB Offshore Clearing Centre



RMB as world payments currency in value

Customer initiated and institutional payments. Inbound + Outbound traffic. Based on value.



Source: SWIFT http://www.swift.com/about_swift/shownews?param_dcr=news.data/en/swift_com/2014/PR_RMB_singapore.xml

The additional RMB5 billion overnight facility announced by the MAS (more details on 1 July 2014) will further enhance financial institutions' ability to offer RMB loans. The amount is likely to more than exceed FIs' current requirements, based on bilateral real flows of trade and investments, with cushion for financial flows.

Total bilateral external trade flows between China and Singapore in 2013 amounted to S\$115.2 billion. Total bilateral direct investment flows in 2012 were S\$5.57 billion (based on Singapore Dept of Stats data), consisting of Singapore's "Direct Investment Abroad" into China at S\$4.95 billion and "Foreign Direct Investment" from China into Singapore of S\$0.62 billion in 2012.

In aggregate, trade and investment flows alone amount to at least S\$120.77 billion between China and Singapore, or RMB597.81 billion, per year. This works out to total trade and direct investment flows of RMB1.64 billion daily, on average. Taking into account of financial flows such as foreign exchange, interest rate, bond, equity, and other financial market transactions, the RMB5 billion overnight liquidity facility would look to be sufficient for now.

Overall, the latest announcement from the MAS and PBoC last Friday pushes RMB internationalization and liberalization to another level, as Chinese companies within the SIP will be allowed to access external funding directly while at the same time, an offshore RMB center will be able to lend directly into China, albeit restricted within SIP for now. Another of Singapore-supported initiative, Tianjin Eco-City, could be the next focus for cross-border RMB flows if the program for SIP works well.

No immediate impact is expected on the USD/CNY exchange rate given that the latest development is still experimental in nature and not a full blown liberalization. For now, we are keeping our end-2014 USD/CNY forecast at 6.05, though with an eye of adjusting the figure higher given the soft (but stabilizing) economic data and policy bias towards (selective) loosening.

Sources:

MAS: New Initiatives to promote the international use of Renminbi through Singapore (13 June 2014)

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