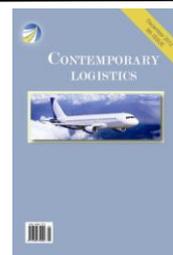




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The Feasibility and the Path Selection of Renminbi Regionalization

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ABSTRACT

China, as a rising powerful country in East Asia, the position and function in regional economy and global economy are continuously to improve. In this process, Renminbi (RMB) is receiving more and more attention. After the outbreak of the U.S. supreme mortgage crisis, the existing international monetary system using US dollar as the core currency fully exposed many defects. In recent years, RMB has been out of the country and gradually circulated in surrounding countries and regions. Along with the rapid development of China's economy, the process of RMB internationalization and regionalization will be gradually accelerated. According to the Theory of Optimum Currency Areas and related judgment standards, this article analyzes the feasibility of RMB regionalization in East Asian monetary cooperation and puts forward the path selection.

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1 Introduction

The current international monetary system--Jamaica system emerged from the Bretton Woods System, which original operation mechanism is to solve or ease international trade and international payments imbalances. In a certain period of time this system ever eased "Triffin Difficult Problem" and its various coordination mechanisms makes up the insufficient coordination abilities of Bretton Woods System. However, the defects of current Jamaica system highlight, which contributes to increasingly serious global economic and financial imbalances. It is so difficult for the current international monetary system to maintain and it is urgent for international monetary system to carry out a reform. China's GDP already surpassed Japan in 2010 and China became the second largest economy inferior to the US. RMB currently should play a bigger role in the international monetary system, and should accelerate the process of RMB internalization. But with reference to the experiences and the insufficiencies of Latin America dollarization and European monetary integration, RMB internationalization should be gradually advanced. RMB regionalization is an important step in the process of its internationalization. Considering China's trade, investment and financial status and the monetary cooperation with surrounding countries and other Asian economies, RMB regionalization is currently a realistic choice in the process of its internationalization.

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2 The Connotation of RMB Regionalization and the Theory of Optimum Currency Areas (OCA)

2.1 The connotation of RMB regionalization

RMB regionalization means that in a geographical area RMB exercises such functions as free convertibility, trading, circulation and reserves. In the present stage, RMB regionalization is not monetary integration of Asian currencies, but rather through the long-term monetary cooperation and competition with other Asian currencies, RMB becomes a key currency in the area, which plays roles as a crucial currency in finances and trades of the area.

2.2 The theory of Optimum Currency Areas (OCA)

Mundell, the father of the euro, put forward the Theory of Optimum Currency Areas (OCA) in 1961. Mundell suggested that when the essential factors can flow fully in an area, but cannot flow to outside the area "Optimum Currency Area" is constituted. When a system of fixed exchange rate is implemented in an area, the liquidity of essential factors is a balanced mechanism in the area. When a system of floating exchange rate is implemented outside an area, the floating exchange rate is a balanced mechanism outside the area. This mechanism is not only beneficial to the microeconomic efficiency in the area, but also to macroeconomic policies to make flexible reaction when affected by external shocks. Subsequently, some economists such as Ingram (1962), McKinnon (1963), Kenen (1969), Flemming (1971), Cor-den (1972), Kindleberger (1971) and Williamson (1973) respectively further deepened the Theory of Optimum Currency Area from the angle of economic openness, product diversification and financial integration.

In 1990s, some economists add cost-benefit analysis to the Theory of OCA. Krugman (1990) takes the European Union and Finland as an example. This paper analyzes the cost-benefit curve after Finland joins the European Union and the famous GG-DLL model is achieved, which provides a simple but effective standard for an economy to decide whether or not to join the currency area. Some domestic scholars have made some researches on RMB regionalization. Han Minchun and Yuan Xiulin (2007) uses endogenous OCA standard model. They select the data of 1989-2003 to analyze empirically RMB regionalization and corresponding effects from the angle of trade. Their article analyzes the trade situation of China and other Asian economies and the influences of China's economic development on Asian economies trade flows and trade structure. Through the above analysis, it is concluded that the present RMB has initially realized the premise conditions of regionalization. Li Xiao, Ding Yibing (2006) points out that under the existing "dollar system", China faces the dilemma as a "trade country". The increasing internationalization of China's economy is not congruent with the status of RMB internationalization. Therefore, China needs to surpass through RMB Asianization to achieve its internationalization goal.

2.3 The conditions of the Optimum Currency Areas

According to the Theory of OCA, it can be summed up as the following several standards: liquidity of production elements, finance market integration, degree of economic openness, inflation similarity criterion, product diversification, capital account openness, policies integration and other related standards.

3 The Feasibility of RMB Regionalization

3.1 Favorable conditions of RMB regionalization

3.1.1 Free liquidity of production elements in East Asian area is gradually enhanced

The more easily Capital and labor flow, the more likely these countries compose optimum currency area. The elimination of tariff barriers and free movement of commodities, services, labour and capital within the common market are prerequisites to establish monetary union. Although in the area some countries' capital realizes completely free flow, such as Hong Kong, Singapore. In China capital hasn't realized full liquidity, but output and input of labor will continuously increase with the establishment of free trade area. Chinese labor is gradually moving towards the completely free flow. The enhancement of overall liquidity of production elements in East Asia facilitates RMB regionalization.

3.1.2 The degree of economic openness in East Asia is higher

McKinnon suggests that economic openness is a standard that can decide whether or not a region is suitable to establish OCA. According to his arguments, the economic openness of a country is defined as the proportion of its trade products to the total social products, which can be represented by the ration of gross import and export to total gross domestic products. Currently the trade amount among East Asian countries is lower the EU, but they are already important trade partners. With the propulsion of bilateral free trade agreements and the implement of various kinds of economic cooperation, the amount of trade within the area is increasingly improved. By the end of 2008, it is Singapore where the ratio of the amount of imports and exports to its GDP (245%) is the highest among some main countries in East Asia; the lowest is Japan (40%); the average is 100%. This is a very high level. According to the theory of McKinnon, with reference to the indicator –degree of economic openness, main countries in East Asian region have reached the standards to establish OCA. Currently East Asian region except the mainland of China, the amount of trades

with America and EU is shrinking, while the amount of trades among East Asian economies is expanding. The industrial division among economies in East Asia and trade links are increasingly tight, which is greatly beneficial to RMB regionalization.

3.1.3 The similarity degree of monetary inflation of East Asian countries is higher

Hubble and Fleming put, if the inflation of an economy within an area has a good similarity, then countries in the area are fit to establish a fixed exchange rates system, thus to form the OCA. The direction of inflation of major countries in East Asia is identical, i.e. there is no phenomenon that one country is in inflation while another in deflation. Therefore, the inflation rate of the region has a high similarity which is suitable to promote RMB regionalization.

3.1.4 Countries in East Asia continuously strengthens policies coordination

Torre with Wilbur Wright put, the higher the consistency degree of policies goals among countries in a region, when payments imbalance is regulated, the easier for fiscal policies to coordinate and unify, the more stable the fixed exchange rate system, the better the feasibility to establish OCA. The Asian economic crisis in 1997 promoted countries in East Asia to increase financial and monetary cooperation continuously, which was beneficial to the establishment of OCA and promoted the process of RMB regionalization.

3.2 The obstacles of RMB regionalization

3.2.1 There exists great difference of economic development level among countries in East Asia

There is a high heterogeneity of economic cycle and product structure among the countries in East Asia. For example, Japan and Hong Kong as developed economies have higher average personal income while China, Vietnam and Thailand as developing economies have lower average personal income. The enormous differences of economic development level increases difficulties of RMB.

3.2.2 There still exist some non-economic obstacles in East Asia

The religions and cultures of the countries in East Asia have strong diversities. In the meanwhile there still exist some political and historical reasons. Thus some problems between some countries, (particularly China and Japan) are difficult to reach agreements and those countries always lack a kind of atmosphere of mutual trust, which has caused the cooperation process in East Asia to greatly fall behind the one in other regions to a great degree.

To sum up, although there are some negative factors in East Asia which restrict the formation of OCA, the positive factors to promote RMB regionalization are the core. According to the endogenous currency theory, some countries which can not reach the standards can also choose to join OCA, and then mutual trades of the countries in the region will grow rapidly. Endogenous functions greatly increase economic income and economic cycle correlation, economic development degree, trade integration, division of profession and price integration so that a real OCA finally is formed.

4 The Path Choice of RMB Regionalization

4.1 Actively promoting monetary cooperation in East Asia

Although China's GDP ranks second in 2010, but per capita GDP is lower than the world average level. Therefore, in the early phase of monetary cooperation in East Asia, China should focus on economic development and financial deepening and in the meanwhile, China should actively participate in and promote monetary cooperation in East Asia. Specific measures are: continuously deepening the reform of money and capital market, further promoting the development of Asian bond funds so as to promote the healthy development of East Asian bond market and even the entire financial market. China should actively prompt to form East Asian repertory of foreign exchange and establish the real East Asian monetary fund and enhance China's core status in East Asian monetary cooperation.

4.2 Gradually making RMB convertible

Currently, China cannot become the leading country to promote the monetary cooperation in East Asia and there is an important reason that China's capital and financial accounts in international balance sheets have more limits. RMB is still not a fully convertible currency. However if the limits to capital and financial accounts are suddenly released so that RMB freely flows, a big impact will be inevitably caused on RMB exchange rate. Therefore, it is necessary to gradually promote the process of free convertibility of RMB, so as to realize RMB regionalization.

4.3 Promoting RMB sub-regionalization in "Great China Region"

China should construct the "one country four areas" free trade area so as to end the history of one country owning four coins (RMB, HKD, AUD TWD). After those measures make some progress, sub-regional monetary cooperation will be promoted. Thus the scope of RMB regionalization will be gradually expanded with a more powerful influence, and finally become the core of Asian monetary union and even directly transit to Asia-dollar.

5 Conclusion

The realization of RMB internationalization must adopt the path of regionalization. According to the current situation of China and East Asia, geographically RMB regionalization should walk from neighboring to regionalization road. China should implement domestic economic reform, adjustment, development and gradual transformation of the foreign economic and trade mode so that prompt other Asian economies to spontaneously use RMB as an anchor currency and an intervention currency of foreign exchange markets in East Asian economies. In the process of RMB regionalization, unilateralism ideas should be avoided, and regional cooperation and coordination should be strengthened to gradually promote RMB regionalization to internationalization.

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5. The Path Selection of China-ASEAN Regional Monetary Cooperation Currently, there exist three paths for China-ASEAN regional monetary cooperation: monetary union model, multiple. 1828. Shuai Yuan et al. Because the process of RMB internationalization has not been ready for dominant currency regionalization model yet, choice will be made between the former two paths. Moreover, as the course of China-ASEAN regional monetary cooperation lags behind that of the Euro-zone, it will be very helpful to take similar process of Euro-zone countries as a mirror.