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US-Dollar Dominance vs. China's Yuan as an International Trading Currency

Many Countries See Their Future in Connecting to the East: Former World Bank Economist

By Peter Koenig and Global Times
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For Chinese people, the past decade has been epic and inspirational. The country, under the leadership of the Communist Party of China (CPC) Central Committee with Comrade Xi Jinping at the core, has made great endeavors in boosting its economy, deepening reforms, improving the rights of its people and acting as a responsible global power.

*Global Times (**GT**) reporter **Yan Yuzhu** talked to Peter Koenig (**Koenig**), a geopolitical analyst and a former senior economist at the World Bank and the World Health Organization, where he worked for over 30 years around the world, over the efforts China has made in the last decade to improve the international financial architecture and how China's Belt and Road Initiative and its pursuit of a human community with a shared future differ in economic terms from the international free trade that the West has been actively pursuing for years.*

This is the 29th article of the Global Times series about this special decade.

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GT: What efforts do you think China has made in the last decade to improve the international financial architecture? What are the main areas of irrationality in the current architecture?

Koenig: It is irrational of the current international financial and monetary architecture, that currencies around the globe were and largely still are linked to the US-dollar economy. Hence, Washington, through US-dollar dominance, may interfere in most countries' economies with sanctions, coercions and outright blackmail.

The phenomenon, "dollar-dominance," has been significantly reduced in the last couple of decades and tends to further lose on importance in the near future.

One significant factor is that China has internationalized its currency, the yuan, also called renminbi. A key step in that direction was taken in 2016, when the yuan joined the IMF basket of currencies, the SDR. This was a milestone in Beijing's efforts to internationalize its currency. The US currency's current weighting in the SDR basket amounts to 43.38 percent, and that of the yuan to 12.28 percent.

Of course, with 12.28 percent, the yuan is way undervalued, given China's economic strength, as the world's second largest economy in absolute terms, and number one in terms of Purchasing Power Parity (PPP).

Other important steps in stabilizing the yuan internationally are the yuan's properties as an international trading currency. Until about two decades ago, most trading worldwide took place in US dollars. Today's ratio is significantly lower, fluctuating between 60 and 80 percent, while international foreign exchange reserve holdings in US dollars have dropped to about 60 percent.

Today, a growing number of international deals are traded in yuan, rather than in US dollars. Within the **Regional Comprehensive Economic Partnership** (RCEP), trading will take place in yuan or local currencies of the trading partners.

The RCEP is expected to bring tangible new opportunities to the business community in the Asia-Pacific region, especially in creating favorable conditions for small and medium-sized enterprises (SMEs). Employing up to 90 percent of the labor force, SMEs are a regional and community force, stabilizing national economies.

Within 3 to 5 years, the RCEP is expected to account for up to 30 percent of world trade. The RCEP will be true to the principle, promoting local production for local and regional consumption, as well as gradually extending into international markets.

The People's Bank of China, the country's central bank, is testing a central bank digital yuan for cross border trading with the country's Hong Kong Special Administrative Region, Thailand and the United Arab Emirates (UAE). This virtual currency, or digital central bank currency (DCBC), can function outside any Western currency exchange system, like SWIFT, Wall Street Banks and the City of London.

Importantly, however, is the continuation of physical cash, bank notes and coins. Cash must continue being available for people to use. Cash is and remains a signal of strength and security for people to be able to manage autonomously their own accounts, their own earnings, resources and spendings.

GT: How do you think the China-proposed Belt and Road Initiative (BRI) and its pursuit of a community of shared future for mankind differ in economic terms from the international free trade that the West has been actively pursuing for years? How does China balance its economic interests with respect to the political and financial sovereignty of other countries?

Koenig: The BRI connects the world through trade, infrastructure, cultural exchange, as well as inter-country research projects. BRI literally spans the globe by at least six different "roads," and growing.

The BRI enhances economic stability by connecting countries and may act independently from the US-dollar economy.

It is also a formidable means to forge a multi-polar world, moving away from a US-dominated one-polar world.

In addition to providing economic stability to regional and country partners, the BRI aims at creating an economically more balanced world by linking regions and countries through common economic development projects or long-term mutually beneficial programs.

The BRI provides an excellent instrument for China's objective to achieve a community with a shared future for all mankind. China, through the BRI, encourages all countries to coexist peacefully, engaging in sound interaction and seeking common grounds, while preserving individual national sovereignty.

GT: In what ways do you think the BRI will change the world? What other economic strategies and policies of the CPC have impressed you in the last decade?

Koenig: So far, the BRI has been widely ignored by the West. When recognized, it was and still is, fought against by Western negative China propaganda and by outright "punishing" countries who participate in it. However, there is a muffled but growing interest in Western countries to become part of the BRI, stretching all the way to Latin America.

As the dollar hegemony is losing strength, many countries see their future in the East, in cooperating and connecting to the East, to China and the SCO. A great opening to do so is becoming engaged in the BRI and, generally, approaching closeness to the SCO – which already today encompasses close to half of the world population and a third of the globe's GDP.

An impressive strategy of the CPC over the last decade or so is China's shift from predominantly "vertical" growth, to a more "horizontal" growth path. It is a shift from manufacturing and export orientation, toward internal growth through local and regional infrastructure, cultural, educational, health facilities, as well as housing development.

This approach furthers internal stability, improves economic equilibrium between eastern and western China. Over time, it is also expected to reduce west-east in-country migration, thereby laying the groundwork for a solid western China multi-faceted development; for a vibrant, cultural, educational and health infrastructure.

GT: The CPC has been around for 101 years. Looking at the history of the Party's development, why was it able to lead China to independence and become the second largest economy in the world? What are the lessons of China's economic development path for other developing countries?

Koenig: One of the most effective means that China applied for her extraordinary development trajectory follows the principle of two phases: First, local production for local markets with local currencies and resources, with local public banking and a sovereign national central banking system – to attain national self-sufficiency. Second, gradual opening up of borders for regional and international trading, to the extent possible with partners pursuing similar development philosophies and objectives, and whenever possible, based on comparative advantages, thus, targeting win-win situations for China as well as partner nations.

GT: Although the Chinese economy is also under pressure amid the COVID-19 epidemic, the general trend of high-quality development of the Chinese economy has not changed, in terms of both foreign investors' trust and China's economic boosting policies. What role can China play in the recovery of the world economy from the pandemic?

Koenig: Under the US-dollar system, every country of the 193 UN members, when using the dollar, or keeping dollar reserves, especially in US or British banks, is vulnerable to US "sanctions". If they don't dance to Washington's tune, they may be "punished" and robbed of their reserves – see Venezuela's gold reserves of over $ 1 billion equivalent stored with the Bank of England; they were confiscated on the orders of the US.

Other monetary sanctions may include Washington blocking payments from "disobedient" countries to their trading partners – and more.

Today, under the Western monetary transfer system which is mostly through SWIFT, all transactions, whether in US-dollars or not, have to transit a US bank, either in New York or London, stressing the vulnerability of "disobedient" partners.

China can help creating an alternative monetary system, away from the Western dollar-based fiat money. As mentioned before, China's central bank is working on a digital currency – a digital yuan – to be used for international trading. This currency will be fully delinked from the dollar – therefore, "safe" from US sanctions.

When that happens, many countries may switch from trading in US-dollars to trading in Chinese yuan, using the new digital central bank currency (DCBC). Many countries may also dump US-dollars from their reserves and replace them with yuan.

There will be a growing demand for yuan which may result in currency arrangements, especially between China and its closest trading partners, for example, the associates and partners of the RCEP trading agreement.

One or more parallel currencies by several countries joining together, were also mentioned on several occasions, especially by the BRICS+ but also by the SCO.

To repeat – beware from a single currency for an association of sovereign countries without any political links toward creating a sovereign federate nation. The monetary failures of the European Union may serve as an example.

As a first step toward closer monetary association, swap agreements among individual partners may be a solution.

Over the past weeks, the emergence of an artificially strengthened dollar has hit the international monetary arena. It may be targeting China and providing incentives to those who seek more liberal market policies to invest in dollar-based assets abroad, causing capital flights. Tighter currency transaction regulations may become the order of the day.

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