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**RBI Staff Study  
Internationalisation of Currency :  
The case of the Indian Rupee and Chinese Renminbi**

The Reserve Bank of India today published a Staff Study entitled '[Internationalisation of Currency: The case of the Indian Rupee and the Chinese Renminbi.](#)' Authored by Dr. Rajiv Ranjan and Shri Anand Prakash, the study examines the costs and benefits associated with internationalisation of currency with specific cases of the Chinese renminbi and the Indian rupee. It also examines whether Indian rupee could be a candidate for internationalisation.

**Context**

The recent global economic downturn and weakness of the US dollar in the international market has prompted a wide-ranging debate on the need for a new global reserve currency. It is quite unlikely that the dollar will lose its predominance as global reserve currency in the foreseeable future. The current crisis has, however, thrown open the debate on the need for a new global reserve currency in case the US economy fails to make a significant turnaround and the weakness of the US dollar persists making its continuance as a global reserve currency unsustainable.

The issue of a new global reserve currency is attracting the attention of policy makers all over the world in recent times. The issue has assumed significance for Asian central banks, including the Reserve Bank of India, which have invested a significant proportion of their reserves in dollar denominated assets. Any sharp depreciation in the value of the dollar would entail significant losses to these central banks. The moot question, however, is which currency is capable of replacing the US dollar in the medium to long-term. China has already stepped up its efforts towards greater internationalisation of renminbi.

The study is descriptive and analytical in nature and draws upon various recent studies on the issue of internationalisation of currency, especially in the context of Chinese renminbi. The study thus provides an in-depth analysis of various issues pertaining to internationalisation of the Chinese renminbi and the Indian rupee.

**The case of Chinese Renminbi**

Detailing the various issues pertaining to internationalisation of the Chinese renminbi and the Indian rupee, the study argues that among the emerging market currencies, renminbi and Indian rupee are natural contenders for an international currency status. This is on account of increasing economic prowess of these countries and their ability to withstand the adverse impact of the global financial crisis with relatively greater ease. The study notes that Chinese authorities have taken a number of steps to bring about greater internationalisation of renminbi which

is already visible in transactions with its neighbouring economies. China has, for instance, promulgated provisional rules governing the issuance of renminbi-denominated bonds by international development institutions; allowing non-residents to issue in Chinese markets the so-called *panda* bonds; People's Bank of China (PBOC) has entered into a series of bilateral currency swap agreements whereby the PBOC and other central banks have agreed to exchange the renminbi (not the US dollar) with the respective counterparty currencies, mainly for supporting trade between these countries; Hong Kong is increasingly becoming an offshore Renminbi trading center and the Chinese government is fully supports the move.

According to the authors of the study, for China, the greatest advantage in renminbi internationalisation is reduced foreign exchange risk for Chinese enterprises. The renminbi's internationalisation will also enhance the international competitiveness of Chinese financial institutions. Furthermore, when the renminbi gains wide acceptance as an international currency, China will enjoy the additional benefit of seigniorage. On the other hand, one major drawback of renminbi's internationalisation would be China's increased susceptibility to the inflows and outflows of international hot money.

In view of the authors, the renminbi is far from ready to achieve reserve currency status at the moment. Progress towards Renminbi internationalisation depends not only on China's own cost-and-benefit calculation but also on China's share in the world economy, confidence of global markets and well functioning financial market in China. Before the Renminbi becomes fully convertible, the offshore renminbi market will have to be in place. Apart from economic aspects, political elements are equally important for the renminbi internationalisation, say the authors. The renminbi is likely to become a regional currency because of China's expanding trade links before it gains acceptance as an international reserve currency, the study concludes.

### **The case of Indian Rupee**

In view of the authors, India needs to proactively take steps to increase the role of the Indian rupee in the region. They conclude this after noting that significant strength exhibited by the Indian rupee in the recent months and continued good performance of the Indian economy have raised the issue of greater internationalisation of the Indian rupee. India's has so far followed a calibrated approach towards capital account liberalisation. India, at present, does not permit rupee to be officially used for international transactions except those with Nepal and Bhutan though there are indications of Indian rupee gaining acceptability in other countries. There are, however, problems associated with Internationalisation of the rupee as it could increase volatility of its exchange rate. Withdrawal of short-term funds and portfolio investments by non-residents could also be a major potential risk of internationalisation of the Indian rupee. Unlike China, which runs a large current account surplus, India generally runs a significant trade and current account deficits. The Indian rupee is rarely being used for invoicing of international trade. Further, all the necessary preconditions need to be in place before India could proceed further on the issue of internationalisation of the rupee.