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In Step to Enhance Currency, China Allows Its Use in Some Foreign Payments

By [KEITH BRADSHER](#)

HONG KONG — Banks in China and Hong Kong began wiring Chinese renminbi directly to one another on Monday to settle payments for imports and exports, as China took another step toward establishing the renminbi as a global currency — and, eventually, an international alternative to [the dollar](#).

China has tempered its recent calls for a global reserve currency other than the dollar going into a meeting of the world's major industrialized countries and biggest emerging economies in Italy on Thursday. He Yafei, China's vice foreign minister, said on Sunday that the dollar would remain the world's dominant currency for "many years to come."

But the Chinese government is accelerating the process of making its own currency, the renminbi, more readily convertible into other currencies, which gives it the potential over the long term to be used widely for trade and as a reserve currency.

The day that the renminbi is fully convertible — more than a few years away, but perhaps less than a few decades — will most likely signal a huge shift in global economic power, and a day of reckoning of sorts not just for China but also for the United States, which will no longer be able to run up huge debt without economic consequences.

Despite the slow, cautious pace at which China is moving, few experts on Chinese monetary policy doubt that the long-term direction of policy is toward strengthening the renminbi as an alternative to industrialized countries' currencies.

"To many minds here in China the U.S. dollar's time is almost up," wrote Stephen Green, an economist in the Shanghai offices of [Standard Chartered](#), in a research note last Thursday. "The euro zone suffers from political paralysis and a too-conservative central bank, while two decades of economic stagnation and a shrinking population do [the yen](#) no favors."

For decades, China has shielded the renminbi behind high barriers. Authorities in Beijing prevented sizable amounts of the currency from building up beyond China's borders to allow them to control the exchange rate and tightly regulate the financial system.

By keeping the exchange rate low, China keeps its exports competitive.

But, as a result, almost all payments for China's imports and exports, as well as international investment in China and Chinese investment abroad, are made in dollars. Smaller sums cross China's borders as euros and yen, but seldom renminbi.

China is now starting to tear down these walls and free the renminbi — a decision driven partly by recognition of China's rising role in the world economy and partly by disenchantment with the currencies and financial systems of the industrialized world during the current downturn.

“China definitely wants to reduce its dependence on the U.S. dollar,” said Xu Xiaonian, an economist at the China Europe International Business School. “Given the [quantitative easing](#) of the Fed and the risk of worldwide inflation, it is understandable why China would want to accelerate the convertibility of the renminbi.”

China's leaders tend to plan far ahead, however, and full convertibility for the renminbi is likely to take years, said three people who have discussed the issue with China's central bank policy makers. All three said that China's recently announced goal to turn Shanghai into an international financial center by 2020 meant that China probably wants a renminbi that is fully convertible into other currencies by then.

Full convertibility is necessary for other countries' central banks to hold renminbi in their foreign exchange reserves instead of the dollar, but not sufficient by itself. China also needs to show long-term economic and financial stability — something it has demonstrated over the past year in greater abundance than most countries.

Currency specialists and economists estimate that China still holds close to three-quarters of its \$2 trillion in foreign reserves in the form of dollar-denominated assets. But these holdings have nearly stopped growing since the global [financial crisis](#) began last September, as Chinese authorities have also shifted away from the longer-maturity bonds and the securities of government-sponsored enterprises like [Fannie Mae](#), and toward shorter-dated securities, especially [Treasury bills](#).

Zhou Xiaochuan, the governor of the People's Bank of China, called this spring for a greater role in the global financial system for special drawing rights, a unit of account used in dealings with the [International Monetary Fund](#). But Mr. He, the vice foreign minister, said on Sunday that such discussions were an academic exercise.

Eswar S. Prasad, the former head of the I.M.F.'s China division, said that senior Chinese central bankers had told him that Mr. Zhou's suggestions about using special drawing rights as a kind of global currency were intended to stimulate debate, and that China's main goal is to enhance the role of its own currency.

“The Chinese authorities see full convertibility as a long-term objective, recognizing this is essential for the renminbi to become an international reserve currency,” Mr. Prasad said.

Full convertibility of the renminbi is not an unalloyed benefit for China, because it would be harder, although not impossible, for China's central bank to continue controlling the currency's value in terms of

the dollar. A sharp rise in the renminbi could drive thousands of export factories out of business and cause large-scale layoffs, which the Communist Party fears as potentially destabilizing. A more volatile currency would also require Chinese businesses to develop more sophistication in managing risk, and most likely involve losses along the way among those that fail to do so.

In the last several months, Beijing authorities have begun moving to let central banks from Argentina to Malaysia settle payments in renminbi with China's central bank. On Monday, the government moved gingerly toward allowing the private sector to handle more renminbi beyond mainland China's borders.

The new program is restricted to companies in Shanghai and in the biggest cities of Guangdong Province, a center of exports next door to Hong Kong. Companies in these cities are now eligible to send or receive payments in renminbi with customers or suppliers in Hong Kong, Macao and Southeast Asia.

Chinese exporters have been eager to see the renminbi used more widely for trade — particularly after many suffered losses a year ago, when the Chinese authorities allowed the renminbi to rise 8 percent against the dollar from December 2007 until the exchange rate was frozen through market interventions in late July 2008. That rise in the renminbi hurt Chinese companies that had signed contracts to export goods for payments in dollars, only to find that those dollars did not go as far as they hoped in covering expenses incurred in renminbi.

“Expanding the renminbi usage area and making it more flexible is great news as we sell a lot to various countries overseas — this should also remove the risks associated with currency fluctuations,” said Wang Yapeng, a sales manager at Shanghai Electric International Economic and Trading Company Ltd., which exports a wide range of machine parts.

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