

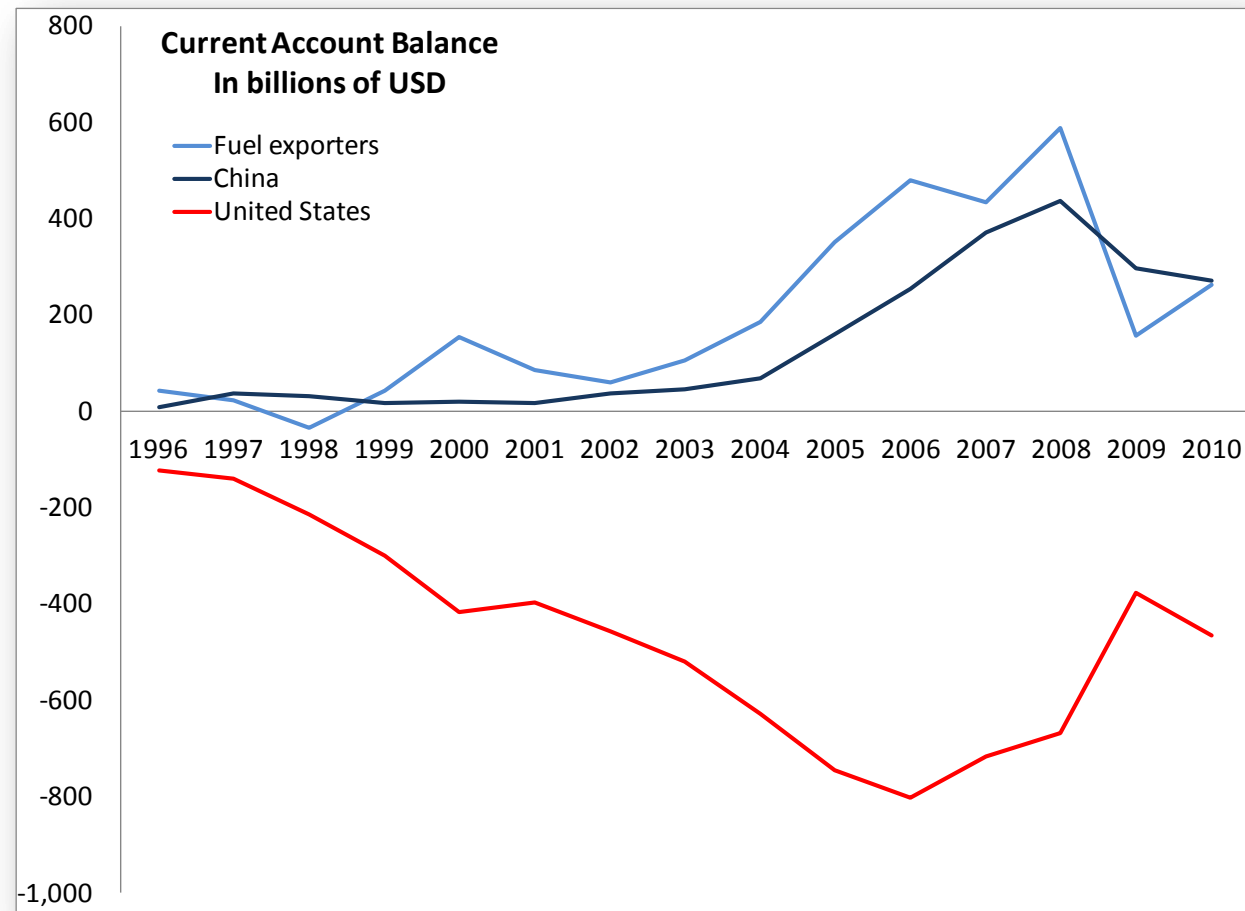
Regional Currency Arrangement

Korea National Committee for PECC (KOPEC) and KIEP

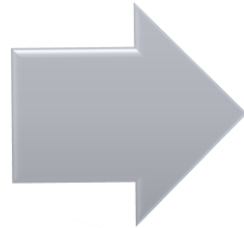
....the international economic landscape in the industrial world has been dominated by the following key developments: ... there have been unprecedented current account imbalances for the three largest economies. Last year, the United States recorded a current account deficit of \$389.5 billion, while China recorded a current account surplus of \$213 billion and OPEC's current account surplus was \$311 billion...

NBER Working Paper #2648; [July 1988](#); THE INTERNATIONAL MONETARY SYSTEM. J. A. Frenkel & M. Goldstein

Déjà vu?



Solution (an example): Allow greater independence of US monetary policy and reduce reliance on the USD by promoting the RMB along with a few other Asian currencies for cross-border use



Reforming the International Monetary System

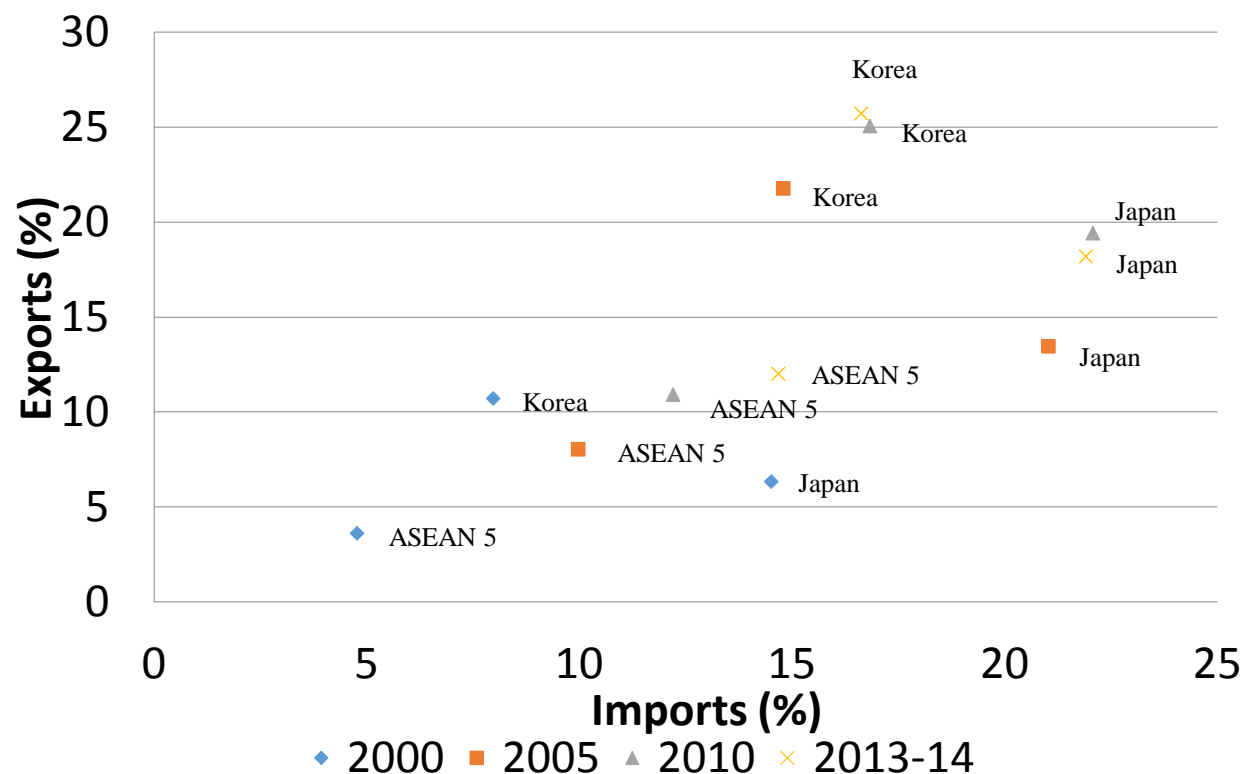
- USD
- Euro

Facilitating a tri-polar currency system

- USD
- Euro
- RMB (along with a few other Asian currencies)

ASEAN+3 is ready for stronger financial cooperation building on its growing intra-regional trade volume and growing GDP share in the world

Share of Trade with China by Country or Group



Source: UN COMTRADE Database.

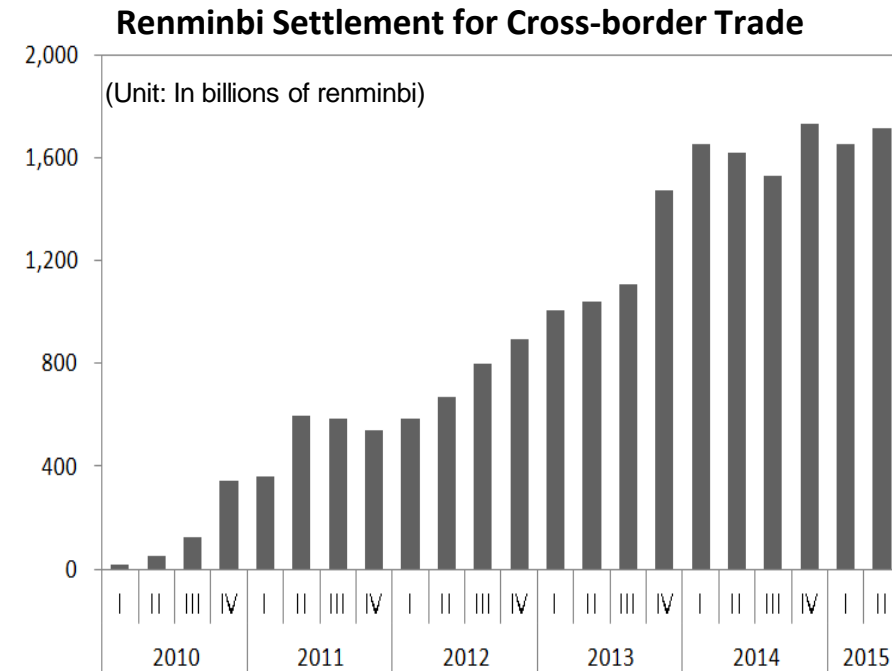
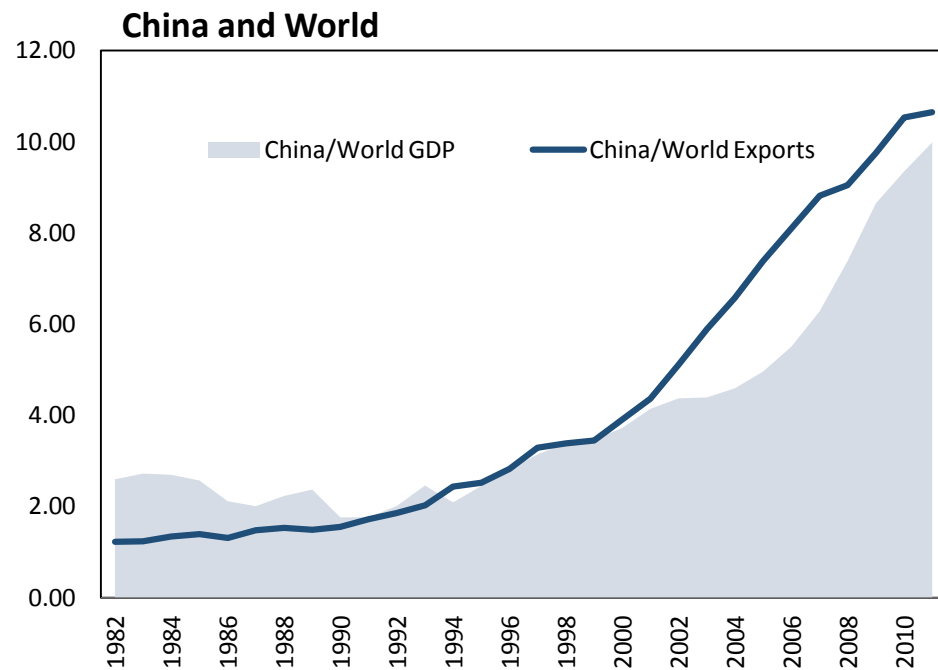
Intra-industry Trade of ASEAN-5 with China: Grubel and Lloyd Index

	Category	2000-04 average	2010-14 average
Thailand	Parts and components	0.91	0.95
	Capital goods	0.47	0.57
	Consumer goods	0.80	0.82
Indonesia	Parts and components	0.58	0.86
	Capital goods	0.31	0.06
	Consumer goods	0.38	0.48
Philippines	Parts and components	0.64	0.89
	Capital goods	0.63	0.72
	Consumer goods	0.46	0.31
Malaysia	Parts and components	0.88	0.84
	Capital goods	0.58	0.63
	Consumer goods	0.27	0.31
Singapore	Parts and components	0.95	0.77
	Capital goods	0.71	0.50
	Consumer goods	0.42	0.81

Source: UN COMTRADE Database.

A regional currency arrangement can be anchored on the RMB as China has the “**necessary economic conditions**” to promote RMB internationalization

Key variables identified as important (necessary conditions) are GDP; Trade value; Depth of the financial market; Infrastructure/institutions (Hongyi Chen, Wensheng Peng, Chang Shu)



Source: CEIC.

Internationalization is a market outcome, but governments should set up the framework in the first place to allow the market to make an optimal choice

The system should be developed first to facilitate the use of local currencies for “settlement” of trade and services, and then gradually expanded to include financial flows.

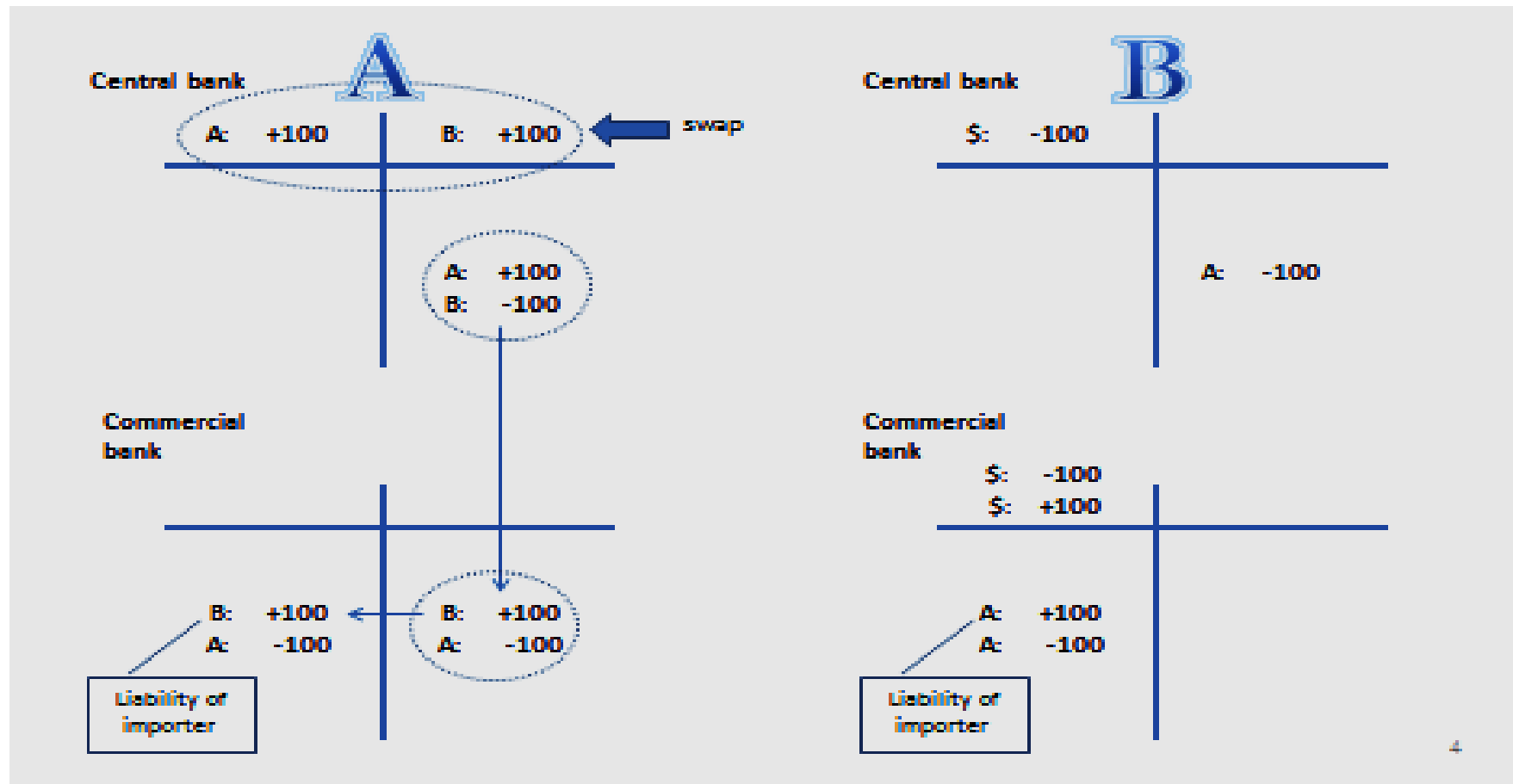
A regional payment system could start with the RMB, the Yen, and a few other Asian currencies including the Korean Won, the Singapore Dollar, and then perhaps one or all of the largest ASEAN country currencies, i.e., the Malaysian Ringgit, the Thai Baht, the Indonesian Rupee and the Philippines Peso.

At the initial stage, bilateral arrangements between the RMB and respective currencies can be set up, followed by gradual build-up of agreements among the other currencies.

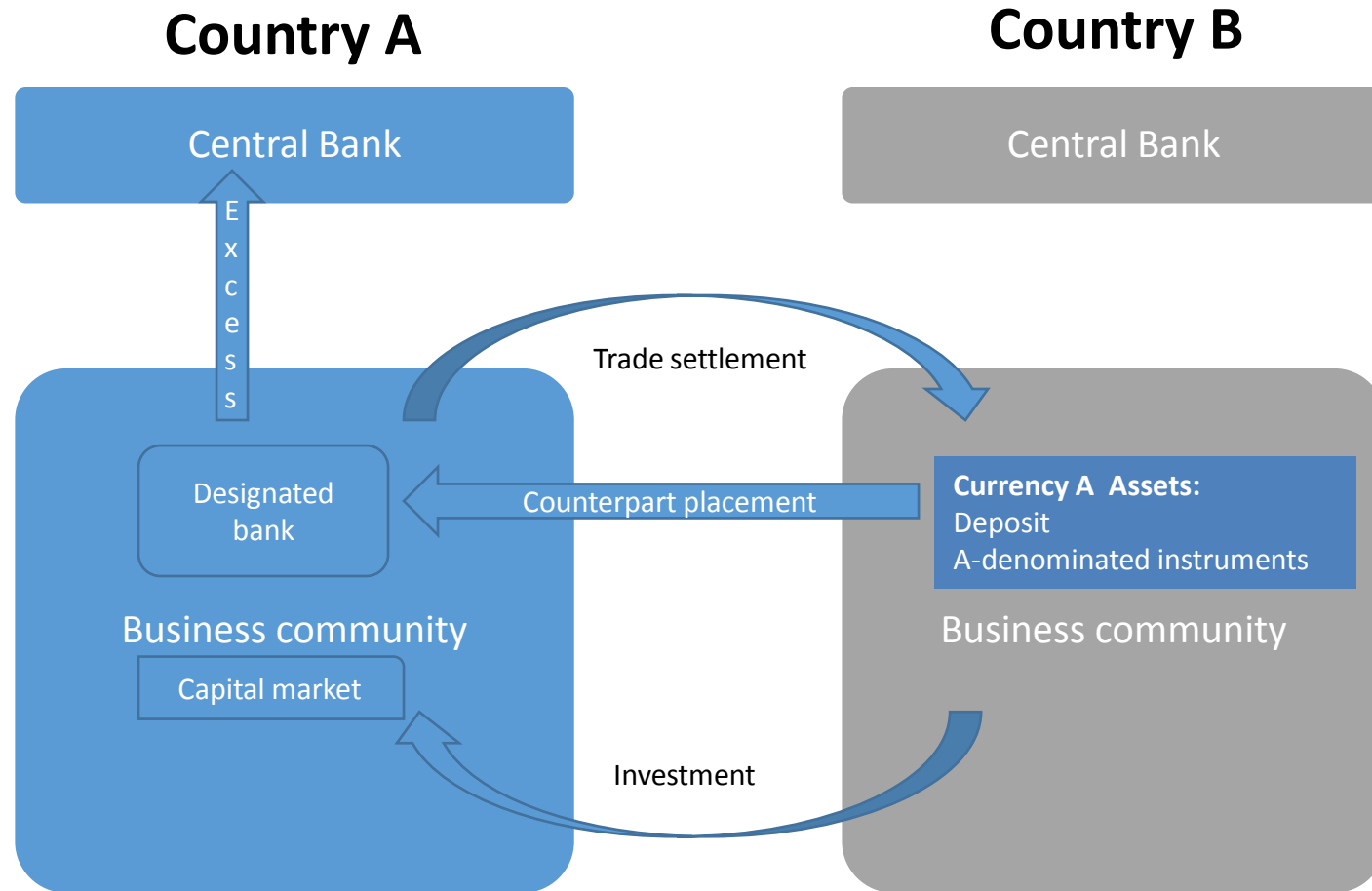
Other ASEAN countries whose currencies are not included in the original group of currencies can still join by agreeing to use any of the currencies in the group for their trade settlement. Once the framework is set up, it would consist of ASEAN+3 countries and perhaps 4-5 currencies.

The swap lines already set up by China with various parties are a useful foundation

Implication on the Balance Sheet (use of currency swap for settlement of trade)



But a swap line is not a necessary condition since cross border transactions can be initiated and conducted without a swap



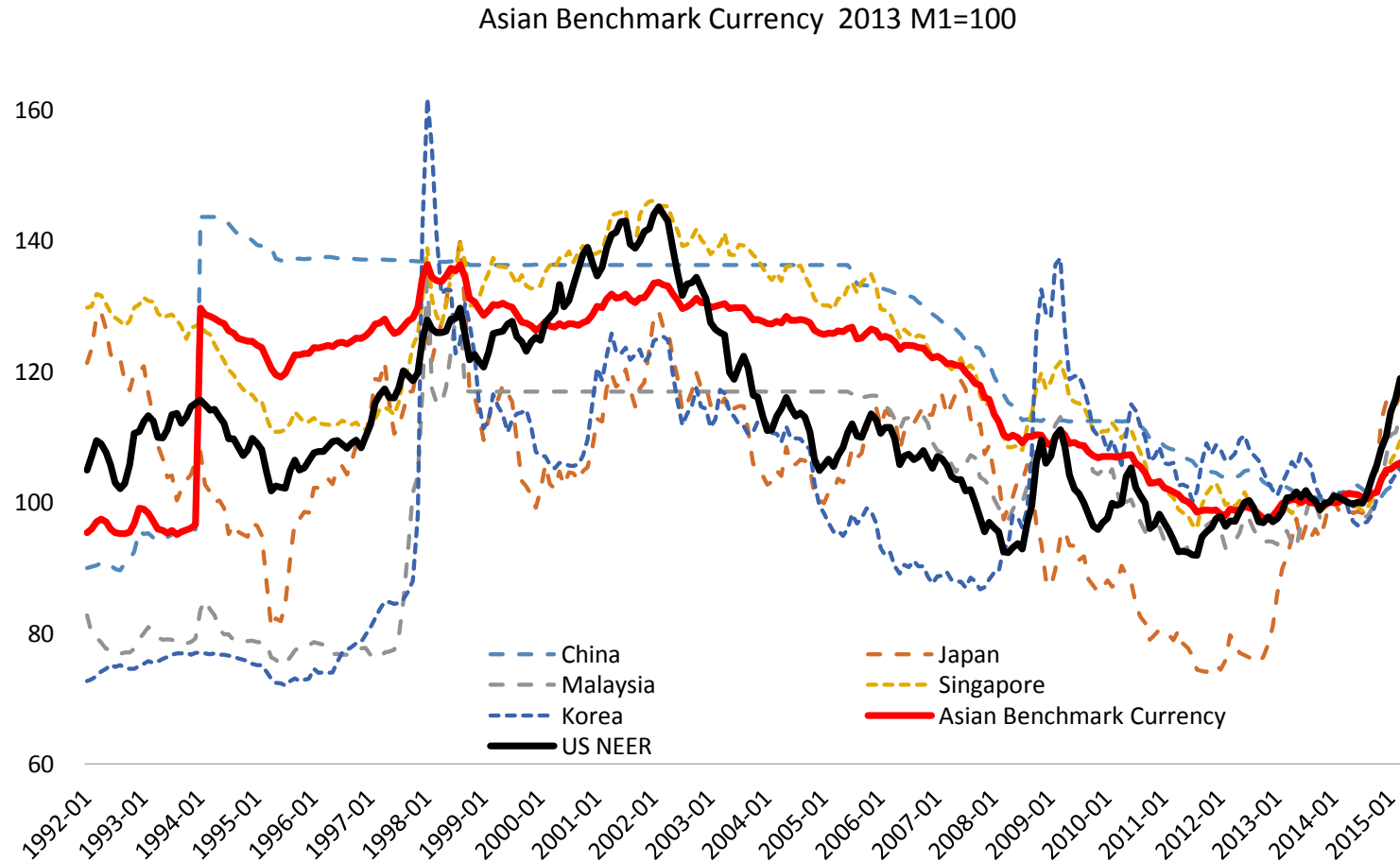
The potential amount of transactions in local currencies even if used only for trade settlement purpose is non-negligible

National Currency Outflows from the Multilateral Trade Settlement Scheme in National Currencies in 2014

(Unit: In millions of US dollars)

	Export to									
	HK	China	Japan	Korea	Indonesia	Malaysia	Philippines	Thailand	Singapore	Total
Hong Kong		290,287	16,914	8,006	2,577	3,739	2,983	7,527	7,761	339,795
China	363,088		149,410	100,335	39,060	46,355	23,474	34,293	48,912	804,928
Japan	37,804	124,986		50,488	14,665	13,958	9,812	31,105	20,970	303,787
Korea	27,256	145,288	32,184		11,361	7,583	10,032	7,599	23,750	265,053
Indonesia	2,778	17,606	23,166	10,621		9,759	3,888	5,830	16,807	90,454
Malaysia	11,314	28,223	25,277	8,572	9,706		3,682	12,308	33,263	132,343
Philippines	5,594	8,034	13,919	2,532	759	1,161		2,352	4,454	38,804
Thailand	12,610	25,084	21,821	4,520	9,510	12,764	5,868		10,455	102,633
Singapore	45,109	51,501	16,746	16,698	38,370	48,998	6,871	15,047		239,340
Total	505,552	691,009	299,436	201,772	126,007	144,317	66,611	116,061	166,371	2,317,137

An Asian Benchmark currency (ABC) can be set up as a guide which can also be used by Asian countries to denominate their bonds (unit of account)



Source: WEO, IMF; CEIC; author's calculation

If the market responds positively, this arrangement will lead to a tri-polar and two-tier international monetary system

As “medium of exchange” and “unit of account”, the IMS will be polarized around the USD, the Euro, and the RMB along with a few other less-used global reserve currencies.

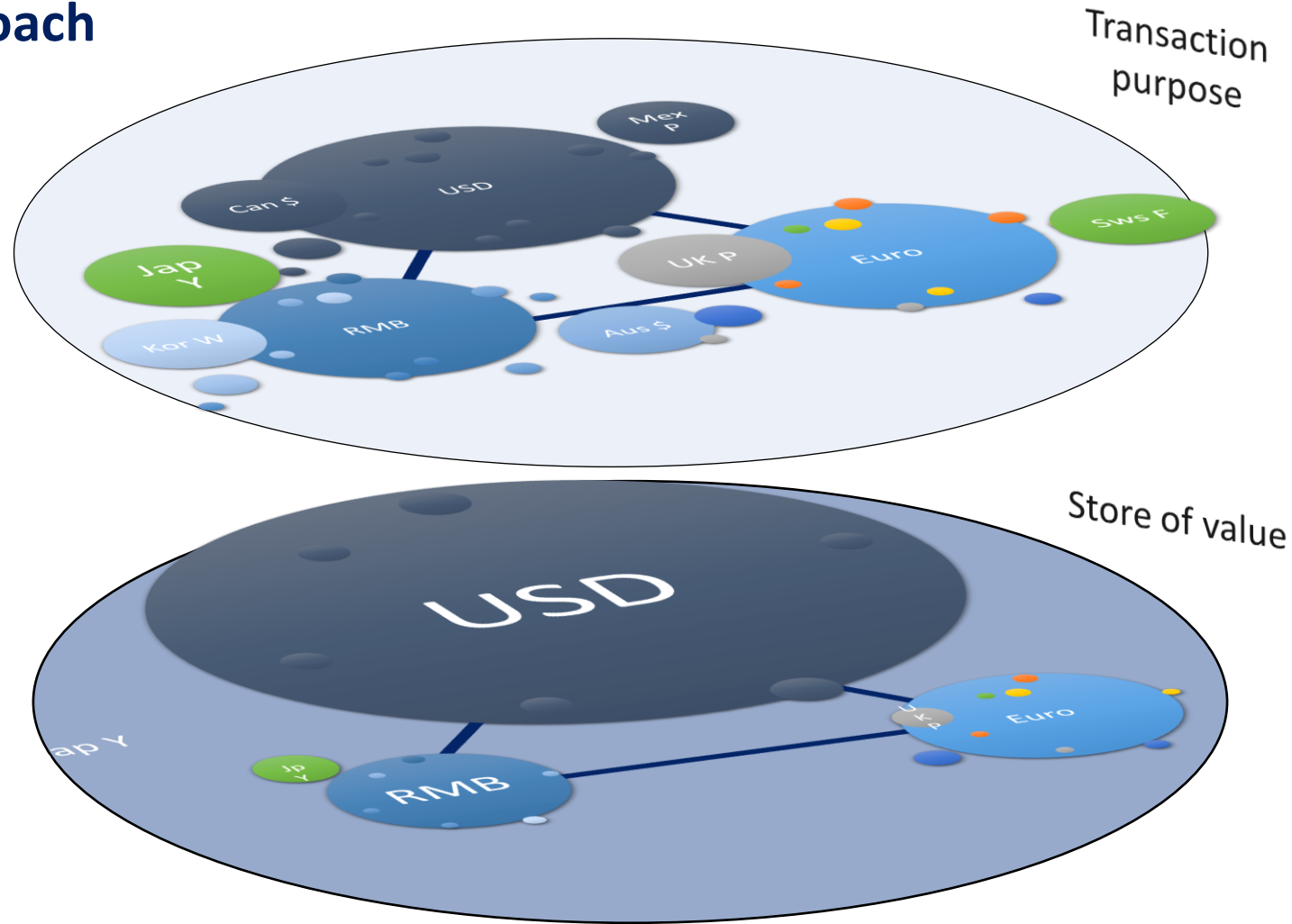
The regionalized currencies will also be used but largely be limited to specific regions and loosely anchored on any of the three main currencies.

The second tier, representing international currency demand for “store of value”, will be an asymmetric bi-polar system where the USD will dominate followed by the euro accounting for a smaller share.

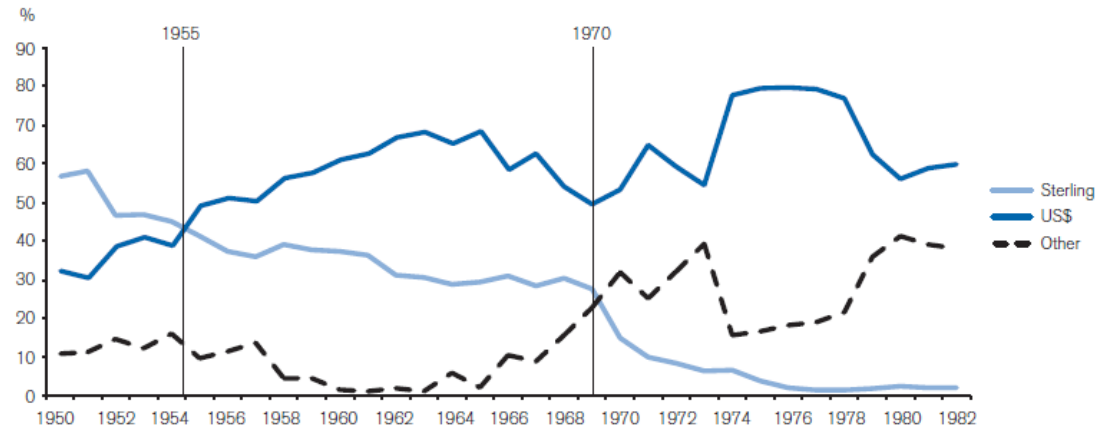
Gradually, the two tiers will merge as the demand for RMB deepens with the changing global economic landscape.

A tri-polar system

Two stage approach

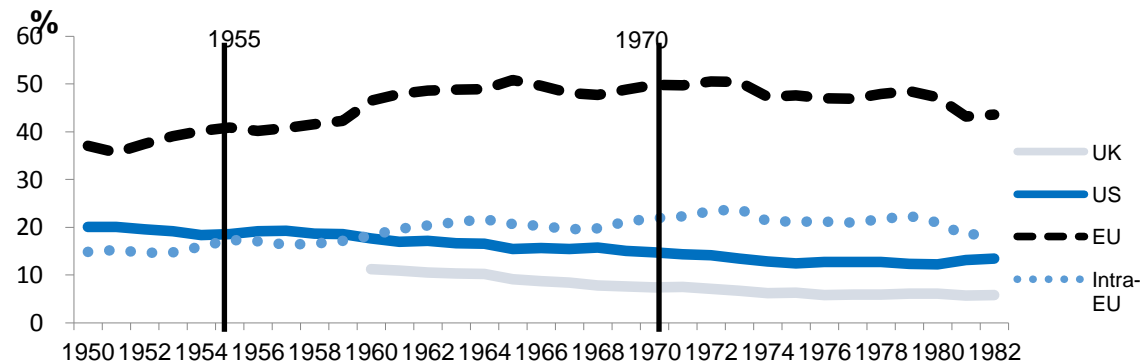


There is no “a priori” for a reserve currency to remain dominant; Once economic conditions are ripe, history attests that the any trigger could tilt the balance quickly

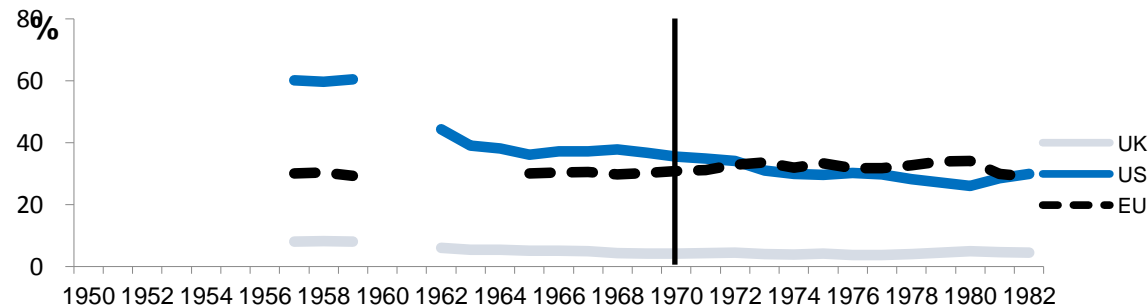


Currency distribution of global foreign exchange reserves, 1950-82 (SDR valuation)

Source: Catherine R Schenk, "Lesson from History" Beyond the Dollar: Rethinking the IMS, A Chatham House Report



Trade share of global total



GDP share of global total (actual exchange rate)

Thank you!

- Based on:
- **Use of national currencies for trade settlement in East Asia: a Proposal;**
- -ADB Working Paper (April 2014)
- **Shaping the Future of the International Monetary System: Regionalization of selected Asian Currencies;**
- -“Reinventing Bretton Woods: the Next 70 Years” (July, 2015) and
- -China Quarterly of International Strategic Studies (forthcoming):