

A Comparative Study on the Implementation Approaches of the Internationalization of Japanese Yen and RMB

Peng Wang, Yuan Peng

Business School, Hubei University, Wuhan, 430072, China

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Abstract: Currency internationalization refers to the ability of a currency to gain widespread recognition in international economic exchanges, and is an important economic phenomenon in the modern market economy system. Currency internationalization can not only enhance a country's international status and influence, but also promote international trade and financial exchanges, which has a profound impact on achieving the smooth operation of the international monetary system and promoting global economic development. This article draws on the experience of the internationalization of the Japanese yen since the 1970s, analyzes and compares the implementation approaches in settlement currency, valuation currency, and reserve currency with the internationalization of the RMB, and looks forward to the future development trends and practical measures of the internationalization of the RMB.

1. Introduction

In recent years, with China's increasing prominence in the global economy and international trade, the internationalization of the Renminbi (RMB) has become a hot topic of domestic concern. As the world's second-largest economy, China possesses sufficient strength and influence to advance the process of RMB internationalization, which holds significant strategic importance in enhancing international competitiveness and driving global economic development. In contrast, Japan has been pursuing the internationalization of the Yen since the 1970s, but due to factors such as a lack of policy support and external influences, the pace of Yen internationalization has been less robust. Therefore, by comparing the differences in the currency internationalization practices of these two nations, conducting an in-depth analysis of the current status of RMB internationalization, and exploring future directions, this study aims to provide theoretical support and practical guidance for the development of China's financial internationalization process.

2. Literature Review

Relevant research for this paper falls into three main categories. First, starting from the late 1960s as the Bretton Woods system gradually collapsed, scholars began to pay attention to issues related to the international financial order centered around the US Dollar. This led to a wealth of currency internationalization theories with the Dollar as the primary subject of study. These scholars mainly

focused on the phenomenon of a currency's functions expanding from domestic to international use, particularly in international financial markets for trade settlement.[1]

Second, Japan actively pursued Yen internationalization policies starting in 1999, but in reality, the path to Yen internationalization has not been smooth, given Japan's economic stagnation lasting for more than two decades. Many scholars believe that a key reason for the lack of success in Yen internationalization is Japan's reluctance to allow foreign participation in its financial markets, especially in the government bond market.[2]

Third, after the global financial crisis in 2008, some scholars analyzed whether the RMB possesses the conditions for internationalization based on the determinants of currency internationalization. Eichengreen (2011) argued that China, as the world's second-largest economy, has the fundamental prerequisites for internationalization when considering its economic size. However, Prasad et al. (2012) argued that economic and trade scale alone is insufficient, and the development level of financial markets is more critical. Maziad et al. (2011) contended that RMB internationalization would increase the complexity of China's currency management and expose China to various risks due to capital flow instability.[3]

In summary, it is evident that currency internationalization is an age-old yet continually relevant issue, particularly during global financial crises. Just as the internationalization of the Dollar garnered attention when the Bretton Woods system collapsed and the Yen internationalization during the Asian financial crisis, the internationalization of the RMB post-2008 global financial crisis is a current hot topic among scholars both domestically and internationally. These studies primarily focus on the reasons, processes, and challenges of currency internationalization, with relatively limited research on implementation strategies.[4] This paper aims to be a valuable addition to this field by delving into implementation approaches.

3. Implementation Approaches for the Internationalization of the Yen

3.1. The Historical Development of Yen Internationalization

The internationalization of the Japanese Yen began in the early 1970s. At that time, due to rapid economic growth in Japan, numerous Japanese companies expanded their market size through overseas investments, and the Japanese government actively pursued open-door policies. Foreign companies started using the Yen to settle trade payments. In 1971, Japanese banks began offering international settlement services to overseas banks, which laid the foundation for the establishment of foreign exchange and currency swap markets. Subsequently, the Yen gradually gained recognition and acceptance in international trade and financial markets, reaching its peak in the early 1980s. During this process, the Japanese government implemented a series of measures to promote Yen internationalization. For instance, it took steps to lower the tax rates for foreign-held Yen, encouraged foreign capital inflows into the Japanese market, actively supported Japanese financial institutions in expanding their overseas businesses, and conducted various promotional activities related to Yen internationalization.[5]

3.2. Challenges Faced by Yen Internationalization

Although the Yen experienced a relatively prosperous period in the 1970s and early 1980s, its internationalization faced obstacles in the early 1990s as Japan's economic growth slowed down and the economic bubble burst. Firstly, due to the deceleration of Japan's economic growth, its global trade share gradually declined, leading to a decrease in the demand for Yen. Secondly, the instability in the international currency markets and the appreciation of the Yen against the US Dollar put significant competitive pressure on Japanese export companies. Consequently, the Japanese

government had to take measures to lower the Yen exchange rate, which resulted in a certain degree of deflation and had an adverse impact on Yen internationalization.[6] Additionally, the Japanese Ministry of Finance exhibited significant variations in its policy stance on Yen internationalization at different times and failed to establish a unified and stable strategic plan regarding the path and priorities of Yen internationalization. Meanwhile, the monetary policies of the Bank of Japan also affected Yen internationalization by reducing the connection between Japan's domestic financial system and the international market, further slowing down the process of Yen internationalization.[7]

3.3. Evaluation of the Implementation Approaches for Yen Internationalization

Based on the analysis above, it is evident that the Japanese government implemented a series of effective policy measures during the historical development of Yen internationalization, and Japan's foreign trade market experienced rapid growth, promoting the internationalization of the Yen. However, due to the instability and lack of continuity in its domestic economic and financial policies, Yen internationalization encountered serious difficulties after the 1990s.

Regarding the implementation approaches for Yen internationalization, it can be observed that the model used was relatively one-dimensional. The experiences and challenges faced by Yen internationalization provide insights that suggest the need for adopting long-term and effective policy measures from different perspectives to enhance the internationalization of a currency. This approach is necessary to better adapt to the trend of globalization and achieve stable economic growth and sustainable development. Drawing lessons from the experience of Yen internationalization, the following recommendations are proposed for the implementation approaches to RMB internationalization.[8]

4. Implementation Approaches for RMB Internationalization

The path to RMB internationalization can be divided into three stages: from a settlement currency to a pricing currency and finally to a reserve currency. Below, we will analyze and discuss specific implementation approaches for each of these three stages.

4.1. RMB Becoming a Settlement Currency

RMB can become an international settlement currency through three main approaches. First, in countries along the "Belt and Road" initiative, establish RMB settlement accounts and RMB clearing institutions, and support RMB settlements in cross-border trade. This approach can reduce transaction costs, improve settlement efficiency, and promote economic cooperation and development among countries along the route. Second, establish the "Petro-RMB." Reducing dependence on the "Petro-Dollar" can lessen the impact of US Dollar policies on China's economy and strengthen RMB's position in the international financial system. Currently, petroleum and natural gas remain the most important international trade commodities in the world. Therefore, the development of the "Petro-RMB" is of significant importance for advancing RMB internationalization. Third, improve the construction of CIPS (Cross-Border Interbank Payment System). CIPS, designed and built by the People's Bank of China, is a cross-border RMB payment system. Through the establishment of RMB account systems, unified settlement and clearing, and the formulation of unified standards and rules, CIPS provides efficient, secure, and convenient cross-border RMB payment services for banks, institutions, and enterprises. This solidifies technical support and infrastructure for the use of RMB on a global scale.[9]

4.2. RMB Becoming a Pricing Currency

For RMB to become a pricing currency, it needs to achieve interest rate liberalization, the development of offshore markets, and capital account liberalization. Interest rate liberalization involves gradually replacing policy interest rates with market-determined interest rates, where market mechanisms play a decisive role in determining interest rates.[10] This is an essential means of promoting financial marketization and optimizing resource allocation. Firstly, it is necessary to progressively improve market-based interest rate pricing mechanisms. Currently, the People's Bank of China has implemented and promoted the Loan Prime Rate (LPR) mechanism, and through measures such as open market operations and gradual relaxation of benchmark deposit rates, it is pushing for the gradual improvement of market-based interest rate pricing mechanisms. Secondly, the development of financial markets can provide strong support and guarantee for the development of interest rate marketization, and it provides robust support for more capital markets entering China. Thirdly, China's financial regulatory authorities have continuously improved and enhanced the effectiveness and functionality of financial regulatory mechanisms through the introduction of external institutions, the establishment of coordination mechanisms among regulatory bodies, and the adoption of risk-based regulatory approaches. These measures have effectively promoted the development and progress of China's financial markets and created favorable conditions for interest rate marketization.

In the further promotion of RMB internationalization, the development of offshore markets is crucial. To ensure the development of offshore RMB markets, it is first necessary to establish a sound offshore RMB settlement system. In particular, any market development requires suitable regulatory mechanisms and tools, and offshore market development is no exception. Secondly, financial product innovation in offshore markets can bring more financial products for RMB internationalization. Thirdly, expanding the scope and number of participants in offshore markets can further boost RMB development and strengthen its usage in international trade and investment.[11]

Capital account liberalization refers to the freedom of capital transactions and capital flow between residents and non-residents of a country. As an implementation approach for RMB internationalization, capital account liberalization allows for more extensive investment and financing activities of the RMB on a global scale, providing more channels and platforms for RMB internationalization. Currently, China has been gradually promoting capital account liberalization. In 2019, an amended version of the "Foreign Exchange Management Regulations" was officially released, further relaxing foreign exchange management policies, allowing individuals and institutions to conduct direct investment and financing transactions both domestically and abroad. China is also gradually expanding the opening of its domestic bond market to foreign investors, attracting more overseas investors to participate and enhancing the RMB's status as an investment currency.[12]

4.3. RMB Becoming a Reserve Currency

The ultimate stage of RMB internationalization is for it to become a reserve currency, and an effective implementation approach for this is the signing of bilateral currency swap agreements. Bilateral currency swap agreements involve central banks of two countries signing agreements to swap their respective currencies for a certain amount, which promotes trade, investment activities, and the elevation of the reserve status of their currencies. As an implementation approach for RMB internationalization, bilateral currency swap agreements possess the following characteristics: Firstly, bilateral currency swap agreements can reduce the costs of trade and investment, improving the convenience of trade and investment activities. Secondly, through bilateral currency swap agreements, the RMB can directly participate in international trade and payment activities, enhancing its

international use and status. Thirdly, bilateral currency swap agreements can strengthen currency cooperation and mutual trust between the two countries. According to official data, China has signed bilateral currency swap agreements with 43 countries and regions, with a total agreement amount reaching 4.2 trillion RMB. In summary, bilateral currency swap agreements are an effective means to promote RMB becoming a reserve currency.

5. Summary and Outlook

This article, through a detailed analysis of currency internationalization, draws the following conclusions:

Firstly, Japan publicly announced an accelerated process of Yen internationalization in 1999 and implemented several policy changes. However, these efforts to promote Yen internationalization did not yield significant results and, in fact, led to a decline in the Yen's status.

Secondly, Yen internationalization gradually occurred after the liberalization of capital account transactions, whereas RMB internationalization is being pursued simultaneously with capital account liberalization. Therefore, the path to RMB internationalization is more complex. Based on this, this article has proposed multiple specific implementation approaches for RMB to become a settlement currency, a pricing currency, and a reserve currency.

RMB internationalization is an inevitable choice for China to respond to the increasingly complex and competitive global economic landscape. It is also a crucial step for China to further open up to the world and deepen financial reforms. Currently, as China's global economic standing continues to rise, the role of RMB in international trade is becoming more significant. At the same time, China faces both opportunities and challenges in the context of globalization. Hence, expediting the process of RMB internationalization, elevating its status and competitiveness in international financial markets, is of great significance for China to enhance its international influence and voice in economic and political affairs globally.

However, there are several issues and difficulties in promoting RMB internationalization, such as the low recognition of the currency in international markets, imperfect foreign exchange control measures, and the limited internationalization of Chinese financial institutions. These factors constrain the status and competitiveness of the RMB in international financial markets. Therefore, in the future, it is essential to continue deepening financial reforms and opening up, further improving the market mechanisms for RMB internationalization, expanding the practical usage and convenience of RMB, and increasing investment and marketing efforts. This will enhance international market trust and recognition of the RMB, laying a more solid foundation for its status and competitiveness in international financial markets.

In conclusion, RMB internationalization is one of the essential development strategies for China in the process of globalization. It enables China to exert greater influence and enhance its international voice in economic and political affairs. Simultaneously, in the process of promoting RMB internationalization, it is crucial to strengthen cooperation with other countries and regions in the financial system, gradually elevate the status and influence of the RMB in international economic markets. The development of RMB internationalization in the future will be a long-term process that requires the collective efforts of the government, markets, and various sectors of society to continuously improve the level of RMB internationalization and market competitiveness, making a more significant contribution to China's financial and economic development.

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