

Features and Prospects of Hong Kong as a Leading Offshore RMB Hub

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The offshore RMB market in Hong Kong is an early promoter and full-cycle participant of RMB internationalization. For a long time, through cross-border trade and investment transactions, the offshore RMB market has functioned as a new investment channel for foreign investors and an enhancement to the diversification of RMB business modes, which could be considered building up the advantages of first-mover by the volume of transactions. In 2022, Hong Kong will promote the further development of an offshore RMB hub and enhance the depth and breadth of the RMB market, thereby continuously enriching the currency basket of Hong Kong as an international financial center and adding more unique competitive advantages to it.

1. Steadily Increasing RMB Exchange Rate Has Bolstered the Development of the Offshore Market

In 2021, the exchange rate of RMB against USD showed a rising trend amid two-way fluctuations. From the beginning of 2021 to early September, this exchange rate fluctuated in both directions, while the rate of USD to RMB hit its highest point this year, which refers to RMB's depreciation to 6.577. Since then, from September to the end of 2021, the RMB exchange rate had performed a trend of volatile appreciation and recorded its lowest point within the year at 6.3458 against USD.

The dominant factor for the recent strengthening of the RMB exchange rate is that the balance of payments of China remains in good condition, and the surplus on the balance of trade in goods and services has brought a large demands for foreign exchange settlement. In the third quarter of 2021, China's trade surplus was 476.2 billion yuan, a year-on-year increase of 30.7%; the capital and financial account recorded a deficit of 311.9 billion yuan, accounting for a year-on-year increase of 63.3%. In the first 11 months of 2021, the trade surplus in goods and services reached 2.7571 trillion yuan, accounting for a year-on-year increase of 18.1%.

In general, the marketization of the RMB exchange rate has been further improved, and the exchange rate flexibility has gradually increased. The RMB exchange rate has remained stable against the items in the currency basket, while it shows two-way expectations and two-way fluctuations against the USD. It can be said that while maintaining the flexibility of the exchange rate, the RMB has improved the resilience of fluctuations and improved the confidence of the global market in RMB assets.

In line with the steady and rising trend of the RMB exchange rate, the offshore RMB market in Hong Kong has developed steadily and is characterized by the fact that the size of the RMB capital pool remains the world's leading, and the RMB product system is increasingly diversified.

According to the data released by the Hong Kong Monetary Authority, the balance of RMB deposits in Hong Kong at the end of November 2021 reached 868.7 billion yuan, an increase of 4% on a month-on-month basis and a 20.4% increase from the end of 2020, hitting a recorded high since October 2015. In 2021, the RMB capital pool in Hong Kong had exceeded 800 billion yuan for seven consecutive months. The balance of RMB loans was 188.2 billion yuan, an increase of 2.2% on a month-on-month basis and a 23.8% increase from the end of 2020, which reached its historically high in the past four years. In the first 11 months of 2021, the cross-border trade settlement for RMB in Hong Kong amounted to 6,375 billion yuan, an increase of 10.1% over the same period last year. The size of the capital pool is an important indicator of market depth, and it is also the key to maintaining Hong Kong as the world's largest offshore RMB hub.

2. Clearing System is the Cornerstone for Hong Kong being an Offshore RMB Hub

The payment and clearing system in Hong Kong brings benefits from the number of transactions they have been dealing with. Specifically, about 75% of the global offshore RMB payment is settled through Hong Kong, which strengthens Hong Kong's position in offshore RMB payment and clearing. The volume of RMB clearing transactions in Hong Kong rank first among the overseas clearing centers. According to data from Hong Kong Interbank Clearing Limited (HKICL), in December 2021, the volume of RMB Real Time Gross Settlement (RTGS) in Hong Kong was 37.18 trillion yuan, recording a year-on-year increase of 27.8%. The total volume of RMB Real Time Gross Settlement (RTGS) in 2021 was 357.7 trillion yuan, accounting for a year-on-year increase of 26.6%.

The cross-border use of the RMB for trades in goods has a direct impact on the global payment currency ranking, and it is also a determining foundation for the development of the offshore RMB market. Data released by the Society for Worldwide Interbank Financial Telecommunication (SWIFT) shows that RMB has regained its popularity for cross-border payment among the other currencies. In November 2014, based on the statistics of the global payments by value, the proportion of the RMB used in international payments had reached an all-time high of 2.45% in the ranking. In December 2015, the RMB accounts for 2.31% in the global payments market, but it had dropped to 1.67% at the end of 2016 and climbed back to 1.88% in December 2020. Then, RMB's market share in global payments increased from 2.14% in November to 2.7% in December 2021. In terms of the total value, the RMB raised to the fourth place in global payments in December 2021, which accounts for an increase of 34.6% on a month-to-month basis comparison to November and thus surpassed the Japanese yen for the first time in the last five years. It is noticeable that the overall value of global payments in all currencies increased by only 6.44% during the same period. In December 2021, the top three active currencies for global payments were USD for 40.51%, Euro for 36.65%, and British pound for 5.89%.

The cross-border RMB trade settlement is a decisive factor that determines the realization and enhancement of RMB's function as an international currency and builds the foundation for other RMB

businesses. The increase in the size of the RMB capital pool in Hong Kong would persistently support the activities of trade and financial transactions, and diversify and expand the RMB products, including stocks, bonds, funds, insurance, and derivative products, in the offshore market in Hong Kong.

The issuance of the bonds denominated in RMB, or the “dim sum bonds”, is closely related to the stock of capital pools in the offshore RMB market, which directly affects the willingness of investors to trade bonds for financial purposes in the offshore RMB market. According to statistics released by Bloomberg, as of the end of December 2021, the issuance of offshore RMB bonds in the primary market was 169.6 billion yuan, including 120 billion central bank bills and 14 billion treasury bills. This figure is 10% lower than the 188.9 billion yuan in 2020, which accounts for 155 billion central bank bills and 5 billion treasury bills.

At present, the value of products traded in RMB in Hong Kong is still lower than that in other international currencies, which means that products denominated in RMB have more room for development. According to sample statistics conducted by the Bank for International Settlements (BIS) every three years, the average daily volume of RMB foreign exchange trading in Hong Kong was USD 107.6 billion in 2019, an increase of 39.6% from the survey three years ago. This figure accounts for 30 percent of RMB foreign exchange trading globally, compared with USD 56.7 billion in London and USD 41.5 billion in Singapore.

3. Interconnection of Financial Markets Provides New Impetus to Offshore RMB Hub

In recent years, the Mainland has accelerated the opening up of the onshore financial market, and the home market has driven the RMB. The cross-border use of RMB in the trade sector has been fully unrestricted, which empowers the market to adjust to the equilibrium in response to the changes in the RMB exchange rate and capital flows. Specifically, Stock Connect and Bond Connect, the landmark mutual market access program linking the Hong Kong and Mainland China equity and bond markets, have pioneered greater accessibility and investor choice, resulting in record trading volumes of 86.5 billion yuan in 2014 and 2 trillion yuan in 2021.

On September 24, 2021, the “Southbound Bond Connect” was officially launched, providing an institutional basis for the two-way opening of the Mainland bond market and Hong Kong’s capital market, and also providing domestic investors with cross-border investment convenience. This move has been considered to support Hong Kong as an important channel for foreign investors to access the capital market in the Mainland, and also makes Hong Kong the preferred destination for mainland investors to invest in overseas assets.

The “Northbound Bond Connect” has been growing steadily and continuously since it was put into operation, and it has gradually become an inevitable channel for foreign investors to flow into the Chinese bond market. According to data from the China Central Clearing Corporation, as of the end of December 2021, the RMB bonds held by foreign investors reached 3.6834 trillion yuan in terms of par value, and the cumulative increase in RMB bonds was 798.5 billion yuan. According to data from the Shanghai Headquarters of the Central Bank of China, as of the end of December 2021, the total amount of bonds held

by foreign institutions in the interbank market reached 4 trillion yuan, accounting for about 3.5% of the par value of the total interbank bond market.

On October 19, 2021, the “Outline Development Plan for Guangdong-Hong Kong-Macao Greater Bay Area” suggests the consolidation of the high-level interconnection of the financial markets in the region, and the formation of free flow of resources and the factors of production. The Guangdong-Hong Kong-Macao Greater Bay Area (GBA) has become the first experimental site for the Cross-boundary Wealth Management Connect Scheme (Cross-boundary WMC), which consists of the Southbound Scheme and the Northbound Scheme that offer full coverage of state-owned banks, joint-stock banks, and foreign-funded banks. The operation of the Cross-boundary WMC is completely market-driven, that is to say, under the framework of macro policies and closed-loop management of funds, it provides convenience for the residents in the Mainland GBA cities investing in wealth management products distributed by banks in Hong Kong and Macau. Such a cross-border channel has brought more investment opportunities for the investors in the GBA, which not only deepens the interconnection of the financial markets in the three places but also promotes the integration and development of regional economies. The Cross-boundary WMC has boosted the two-way capital flow, improved the service quality of asset management in Hong Kong, and drove Hong Kong to develop its wealth management services with a business characteristic of RMB.

The interconnection of the financial markets between Hong Kong and the Mainland has boosted the RMB’s share in the world currency reserves. In March 2017, the International Monetary Fund (IMF) released the Currency Composition of Official Foreign Exchange Reserves (COFER), separately identifying holdings in RMB for the first time in its statistics for the fourth quarter of 2016. Later on, in the third quarter of 2017, the claimed foreign exchange reserves in RMB were USD 107.9 billion, accounting for 1.12% of the overall allocated foreign exchange reserves. In 2021, the amount of RMB as foreign exchange reserves has risen from USD 314.2 billion in the second quarter of 2021 to USD 319 billion in the third quarter, recording 11 consecutive quarters of growth. That growth also reflects the changes in the proportion of RMB in the total foreign exchange reserves, which rose from 2.61% in the second quarter to 2.66% in the third quarter of 2021, ranking as the world’s fifth-largest reserve currency and recording the highest ever, since the IMF added RMB to its Special Drawing Rights basket in 2016.

4. Enhancement of the Market Depth and Breadth of Hong Kong as an Offshore RMB Hub

The National 14th Five-Year Plan also sets out a very important and attractive development theme for Hong Kong that to prudently advance the internationalization of RMB through market-driven policies and enterprises’ independent choices, and promote a new mutually beneficial and cooperative relationship with the free use of RMB. In 2021, the People’s Bank of China together with 5 other Chinese regulators issued new rules covering the promotion of the cross-border RMB settlement process, optimizing the management of cross-border RMB investment and financing, and facilitating personal current accounts, sending a clear signal to the market to accelerate the internationalization of RMB with salient practical and policy significance. In the future, the RMB will vigorously enhance the investment reserve function in addition to maintaining the trade payment function. As foreign investors continue to increase their holdings of RMB

assets, Hong Kong will have more business opportunities in RMB settlement, investment management, foreign exchange transactions, and risk management.

As the world's leading international financial center, Hong Kong has long been widely recognized by global investors for the depth, breadth, and internationalization of its financial market, as well as the degree to which its legal rules are in line with international standards. These outstanding advantages have made Hong Kong an optimal gateway for foreign investors to access the financial market in the Mainland.

In 2022, Hong Kong should actively take the following measures to further promote the construction of offshore RMB hub:

First of all, Hong Kong should promote and attract the demands for offshore RMB business in reference to the progress of the opening-up of the financial market in the Mainland. In recent years, the holdings of RMB bonds and stocks by foreign central banks, institutional investors, and individuals have continued to grow significantly, which resulted in bringing more foreign investors and bolstering greater integration of the Mainland's financial market with the international standards. The People's Bank of China and other regulatory agencies have adopted a series of reform measures, including unifying the management of Qualified Foreign Institutional Investor (QFII) and RMB Qualified Foreign Institutional Investor (RQFII) and canceling their quotas, simplifying market entry procedures for foreign institutions, introducing the market interconnection and multi-level custody model, and opening the Wealth Management Connect and Southbound Bond Connect. The purpose of these new policies and practices was to improve the degree of free convertibility of capital in the Mainland's financial market and to catalyze the transformation of the market to adopt a modern financial system with international standards. The offshore RMB market in Hong Kong should take the initiative to serve as a trailblazer who offers an experimental platform for the RMB business, and such an arrangement also can be a buffer for the further opening of the Mainland's capital market. As the Mainland accelerates the opening of its onshore financial market, Hong Kong can walk at the same pace with the progress of RMB internationalization and capital account opening and play a more important role as an intermediary in cross-border capital activities.

Secondly, Hong Kong should make good use of its existing advantages to further enhance the depth and breadth of the offshore RMB market. Based on serving the needs of the local market, Hong Kong should play its role as a capital pool facing the global market, and extend RMB business to Southeast Asia. By focusing on key regions, key areas, and key enterprises, Hong Kong should cultivate market demand, guide global RMB capital flows, and assist foreign investors in flexibly holding RMB assets. These practices are considered meeting market demands, strengthening the interconnection for the offshore market with the onshore market, and promoting the internationalization of the RMB.

It is equally important that the offshore RMB market in Hong Kong should continue to expand the scale of existing RMB-denominated products and further promote RMB product innovation. These changes will help meet the diversified needs of investors and assist Hong Kong to embrace the transformation of having a scaled offshore RMB capital pool to the comprehensive advantages in offshore RMB business.

主要經濟指標 (Key Economic Indicators)

	2019	2020	2021/Q2	2021/Q3
一. 本地生產總值 GDP				
總量 (億元) GDP(\$100 Million)	27,997	26,277	6,757	7,205
升幅 (%) Change(%)	-1.2	-6.1	7.6	5.4
二. 對外貿易 External Trade			2021/11	2021/1-11
外貿總值 (億元) Total trade(\$100 Million)				
總出口 Total exports	40,961	39,275	4,744	44,725
進口 Total imports	45,714	42,698	4,860	47,859
貿易差額 Trade balance	-4,753	-3,422	-116	-3,134
年增長率 (%) YOY Growth(%)				
總出口 Total exports	-5.6	-1.5	25.0	26.5
進口 Imports	-8.1	-3.3	20.0	24.9
三. 消費物價 Consumer Price			2021/12	2021/1-12
綜合消費物價升幅 (%) Change in Composite CPI(%)	2.9	0.3	2.4	1.6
四. 樓宇買賣 Sale & Purchase of Building Units				
合約宗數 (宗) No. of agreements	74,804	73,322	7,076	96,133
年升幅 (%) Change(%)	-5.5	-2.0	-6.8	31.1
五. 勞動就業 Employment			2021/9-2021/11	2021/10-2021/12
失業人數 (萬人) Unemployed(ten thousands)	139	259.1	15.8	14.3
失業率 (%) Unemployment rate(%)	2.9	5.5	4.1	3.9
就業不足率 (%) Underemployment rate(%)	1.1	3.1	1.8	1.7
六. 零售市場 Retail Market			2021/11	2021/1-11
零售額升幅 (%) Change in value of total sales(%)	-11.1	-24.3	7.1	8.3
零售量升幅 (%) Change in volume of total sales(%)	-12.3	-25.5	4.2	6.8
七. 訪港遊客 Visitors			2021/12	2021/1-12
總人數 (萬人次) arrivals (ten thousands)	5,590	356.9	0.9	9.1
年升幅 (%) Change(%)	-14.2	-93.6	94.1	-97.4
八. 金融市場 Financial Market			2021/10	2021/11
港幣匯價 (US\$100=HK\$)				
H.K. Dollar Exchange Rate (US\$100 = HK\$)	779.3	775.2	778.1	780.2
貨幣供應量升幅 (%) change in Money Supply(%)				
M1	2.6	30.1	-15.6	9.4
M2	2.8	5.8	-4.3	2.9
M3	2.7	5.8	-4.2	2.9
存款升幅 (%) Change in deposits(%)				
總存款 Total deposits	2.9	5.4	-4.4	3.3
港元存款 In HK\$	2.5	6.2	-11	1.7
外幣存款 In foreign currency	3.2	4.6	3.2	4.9
放款升幅 (%) in loans & advances(%)				
總放款 Total loans & advances	6.7	1.2	-4.8	4.2
當地放款 use in HK	7.1	1.7	-6.9	5.6
海外放款 use outside HK	5.8	0.1	0.8	1.1
貿易有關放款 Trade financing	-0.7	-6.2	18.8	14.9
最優惠貸款利率 (%) Best lending rate (%)	5.0000	5.0000	5.0000	5.0000
恆生指數 Hang Seng index	28,189	27,231	25,377	23,475