

RMB Internationalization and the Belt and Road Initiative

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The realization of the potential of the international use of the RMB requires the creation a sufficiently thick market through the positive feedback effect: People will use it because it is widely used, and it is widely used because many people use it. The current lack of market thickness for the RMB is due to China's capital controls and the lack of capital account convertibility for the RMB (i.e. a lack of liquidity); China's underdeveloped financial system (i.e. the lack of a deep, broad, and liquid financial market); and the persistent use of the US Dollar. To achieve market thickness, there needs to be a free flow of funds between the offshore and onshore markets. Thus, the key factors in the internationalization of the RMB are capital account liberalization and financial sector reform. The BRI can possibly stimulate the formation of a large and liquid offshore RMB capital market to increase the offshore market thickness of the RMB. This would facilitate the development of the offshore RMB market and enhance the internationalization of the RMB. However, the effect of the BRI on RMB internationalization would be too small without concurrent onshore capital account liberalization and onshore financial market liberalization; these are still the two crucial factors in the successful internationalization of the RMB.