

Corporate Attitudes towards Renminbi Trade Settlement and Investment

Introduction

The Australia-Hong Kong Renminbi Trade and Investment Dialogue (the Dialogue) was jointly launched by the Australian Deputy Prime Minister and the Hong Kong Financial Secretary in July 2012. The aim of the Dialogue is to bring together senior banking and business leaders to build closer collaboration between Hong Kong and Australia on the development of offshore renminbi (RMB) business opportunities and to raise awareness in the Australian private sector of RMB business opportunities.

This paper, which is based on the results of a survey conducted in early 2013 by banks involved in the Dialogue, examines the attitudes of non-financial firms with Australian operations towards RMB trade settlement and investment in the offshore RMB market. The aim of the survey was to: (i) identify the issues that firms in Australia currently face when undertaking RMB trade settlement and investment in the offshore market, and; (ii) to consider steps to address these issues. The results are intended to contribute to the discussions during the Dialogue on 12 April 2013.

The paper is divided into seven sections:

- The **executive summary** outlines the survey's main findings and identifies some key steps that the Australian and Hong Kong banking communities could take to promote RMB trade settlement and develop the offshore RMB market;
- Section **2** contains a short description of the survey sample;
- Section **3** discusses the current use of RMB trade settlement by the non-financial corporations surveyed;
- Section **4** outlines the main advantages, issues and impediments associated with RMB trade settlement, as identified by the surveyed firms;
- Section **5** focuses on what respondents see as the changes needed to increase their use of RMB trade settlement;
- Section **6** focuses on the extent to which the surveyed firms use – or plan to use – the offshore RMB market, and;
- Section **7** provides conclusions and some suggestions to promote the take-up of RMB trade settlement and investment.

1. Executive summary

RMB trade settlement by firms with Australian operations has grown rapidly since the RMB trade settlement program was expanded in June 2010, although the share of all Australian trade that is denominated in RMB remains very small. The outlook for growth in Australia's RMB trade settlement is positive, with the firms participating in this survey generally expecting their use of RMB trade settlement to increase in the future.

Firms recognise a variety of benefits that can arise from settling trade with China in RMB. In particular, RMB trade settlement was seen as being beneficial for firms' broader business relationships with their Chinese counterparties and, more specifically, as increasing their ability to negotiate better pricing terms.

The ability to hedge associated foreign currency flows was the single most important factor influencing firms' choice of trade settlement currency. In this respect, ensuring that there is adequate access to the appropriate RMB banking products, including hedging instruments, is likely to be important for increasing RMB trade settlement in the future.

The survey also suggests that some additional issues may need to be addressed to help promote RMB trade settlement. In this respect, the key issues identified by respondents as impediments to RMB trade settlement were: (i) the administrative burden associated with unclear or complex procedures (particularly for small and medium enterprises); (ii) concerns that issues with incorrect documentation could result in the rejection of trade payments settled in RMB, and; (iii) time delays in the settlement process (such as delays in payments).

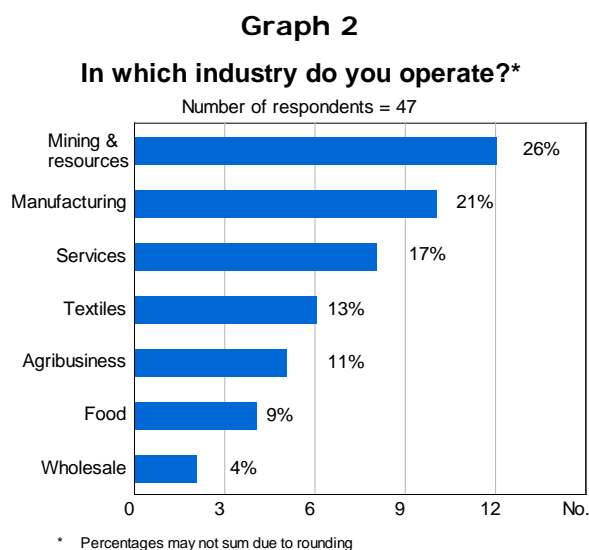
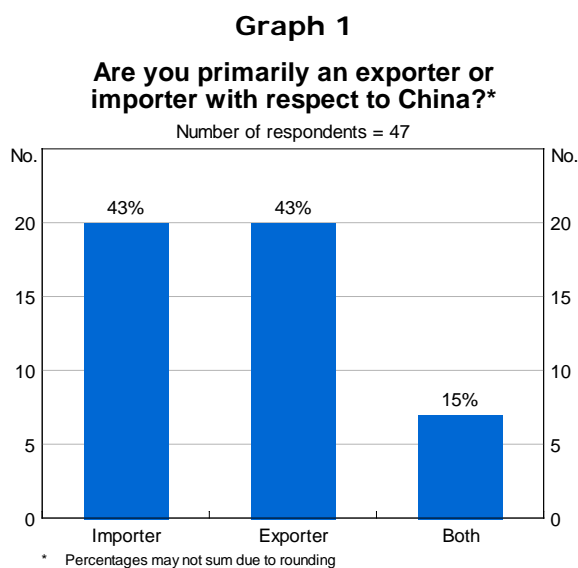
These results suggest the Australian and Hong Kong banking communities could facilitate the take-up of RMB trade settlement by:

- Ensuring they have the infrastructure in place to provide trade settlement services to clients, including an appropriate suite of products (such as hedging tools);
- Raising private sector awareness about the RMB trade settlement process, both with Australian-based corporate clients and their Chinese counterparties, and;
- Taking steps to reduce payment delays, possibly by building closer relationships between banks in China, Hong Kong and Australia.

The survey suggests that in the offshore RMB market take-up of financial products by firms with Australian operations is still relatively low: raising private sector awareness and increasing the use of RMB trade settlement would likely aid growth in the offshore RMB market, particularly with respect to the demand for hedging products. As firms' demand for RMB trade settlement grows this should increase the demand for offshore RMB products and RMB-denominated funding and investment.

2. Sample

Participating institutions from the Australian banking community interviewed a total of 47 firms with Australian operations in early 2013. Although the survey sample was relatively small, the quantitative information provided insight into the key issues that the Dialogue is intended to address. Twenty firms in the sample were importers of goods and services from China, 20 firms were exporters and 7 firms were both exporters and importers (Graph 1). Around two-thirds of firms operated in the mining & resources, manufacturing or service-related sectors (Graph 2), and the majority listed Australia as the home country of their organisation. Respondents were mainly large firms, with half having an annual turnover of greater than A\$100 million and around 70 per cent having more than 200 full-time equivalent workers and an annual turnover greater than A\$10 million.



3. Use of RMB trade settlement

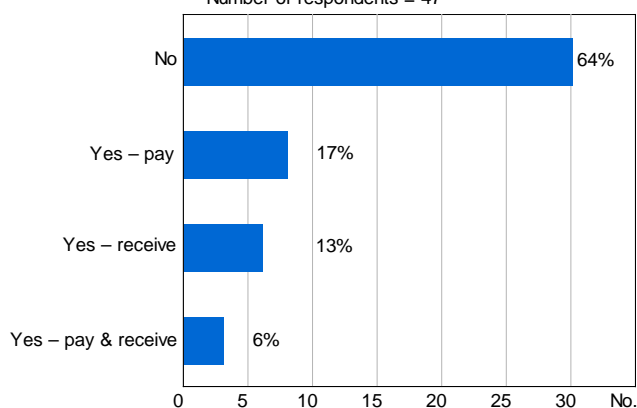
Around 35 per cent of firms indicated that they currently use RMB (to some degree) for trade settlement purposes, although take-up of RMB trade settlement in Australia is still relatively low (Graph 3). Nevertheless, the outlook for growth in RMB trade settlement is generally positive, with 57 per cent of firms reporting that they expect their use of RMB trade settlement to increase in the future (Graph 4). Of those firms that indicated that they are currently making use of RMB trade settlement, some were already settling a substantial portion of their trade with China in RMB, while others were trialling the process. Use of RMB trade settlement was generally mixed across firm size and sector.

One consistent theme was firms' belief that they needed to be ready to undertake RMB trade settlement, particularly if requested by their Chinese counterparties. Respondents noted that Chinese demand for RMB trade settlement would likely increase over time, as more Chinese businesses became familiar with the process and as trade between China and Australia increased. Australian and Hong Kong banks could facilitate this potential increase in demand for RMB trade settlement by taking steps to ensure that they have the infrastructure in place to provide trade settlement services to clients and developing an appropriate suite of associated RMB banking products.

Graph 3

Do you currently use RMB for trade settlement purposes?

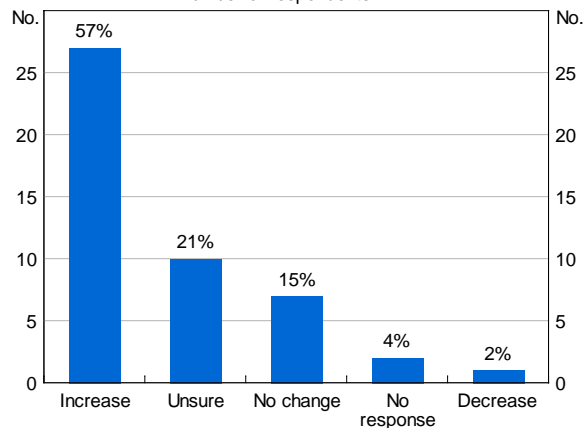
Number of respondents = 47



Graph 4

How do you expect your use of RMB trade settlement to change in the future?*

Number of respondents = 47



* Percentages may not sum due to rounding

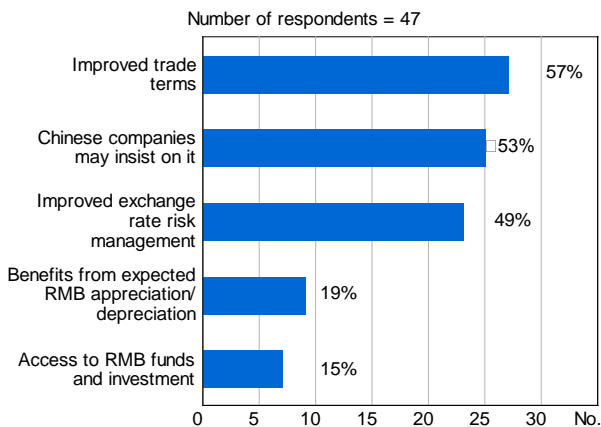
4. Attitudes towards RMB trade settlement

The survey identifies the ability to hedge against exchange rate risk as a key and complex issue for firms undertaking or considering RMB trade settlement, with exchange rate risk management identified as a potential advantage for 49 per cent of firms, but a potential disadvantage for 56 per cent of firms (Graphs 5 and 6).

The fact that some firms have identified exchange rate risk management as both a potential advantage and a potential disadvantage suggests that while firms may presently be unsure about their ability to manage foreign exchange risk, the development of improved hedging services – including clear communication about the products available – could be beneficial. This is further underscored by the fact that those firms that already settle trade in RMB generally viewed the ability to hedge associated cash flows as an advantage of the process, while those firms that do not currently settle trade in RMB generally saw an inability to hedge as a disadvantage. Some firms also noted that RMB trade settlement could provide a 'natural hedge' for cash flows to and from China, and that the process would simplify management of their balance sheets (potentially reducing operating costs).

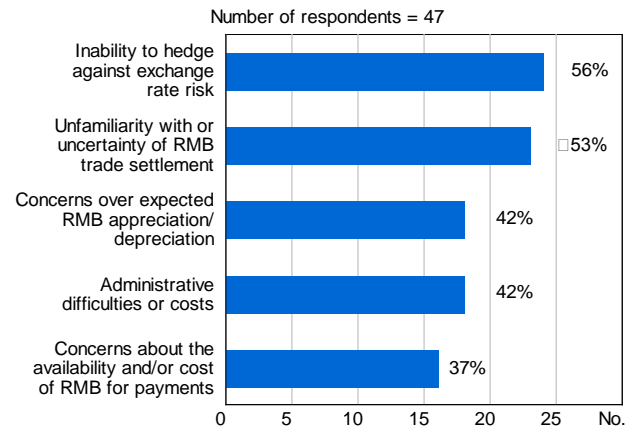
Graph 5

Potential advantages of RMB trade settlement



Graph 6

Potential disadvantages of RMB trade settlement



Corporates also noted the following additional advantages from RMB trade settlement:

- Negotiating improved trade terms with Chinese businesses, by removing the exchange rate risk that arises from settling trade in a foreign currency and therefore reducing the foreign exchange margin that Chinese businesses currently price into US dollar-denominated trade contracts;
- Establishing better relationships with Chinese businesses, by offering the flexibility for Chinese businesses to choose how they denominate trade. Fifty-three per cent of firms noted that it would be important to have the ability to undertake RMB trade settlement in the future if Chinese businesses began to request it to a greater extent, and;
- Both the ability to gain exposure to potential fluctuations in the value of the RMB and access to RMB funds and investment products were identified as being less important, possibly reflecting the limited take-up of RMB trade settlement to date.

The following issues were seen as current disadvantages of RMB trade settlement:

- A lack of confidence in the reliability of the trade settlement process, with many firms citing concerns regarding payment delays and rejections. Around half of firms noted that unfamiliarity or uncertainty around the RMB trade settlement process was an impediment;
- Some small or medium enterprises saw the additional administrative burden and internal operational changes that would be required to develop their own capacity to transact in RMB as a disadvantage, and;
- Other concerns were a potential lack of offshore RMB liquidity and access to RMB funds, consistent with firms' limited activity in the offshore RMB market and little demand for RMB funding.

The survey also asked for more detail from respondents who had undertaken RMB trade settlement about any specific issues they had encountered in doing so. Around three-quarters of the respondents who had conducted RMB trade settlement reported that they had experienced no difficulties with the process (Graph 7). Of those that did report issues, complicated procedures for approval, Chinese counterparty objections related to tax issues and a lack of accessible information were cited as important. Firms also indicated that uncertainty around the reliability and timeliness of RMB trade settlement can act as a disincentive.

These findings suggest that the availability of accessible, clear and reliable information regarding the RMB trade settlement process and its related documentation could help firms in Australia and China to overcome the associated administrative difficulties. In addition, reducing payment delays – possibly by building closer relationships between banks in China, Hong Kong and Australia – may also help to increase RMB trade settlement.

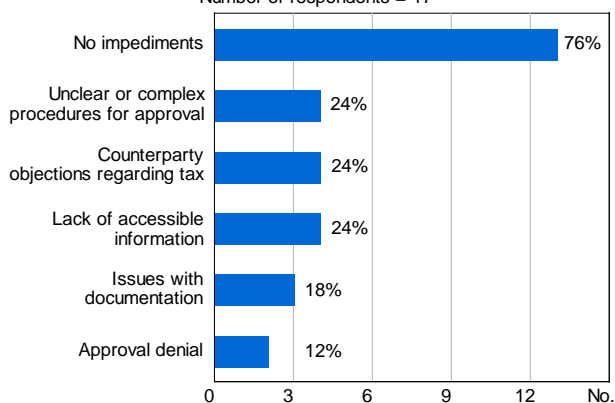
5. Increasing RMB trade settlement

Around 65 per cent of firms indicated that a change in Chinese companies' attitudes towards RMB trade settlement would increase their own use of RMB trade settlement (Graph 8). Of these respondents, 60 per cent do not currently use RMB trade settlement, suggesting that increased demand from Chinese counterparties would be an important factor in encouraging these firms to begin using RMB trade settlement. Changes in the capabilities of Australian-based banks were also reported as having an impact on respondents' use of RMB trade settlement, suggesting that banks could benefit from improving the RMB services they offer and their communications with corporates regarding these services. Respondents also noted that changes in Chinese regulation would be important for increasing their use of RMB trade settlement.

Graph 7

Impediments to RMB for trade settlement

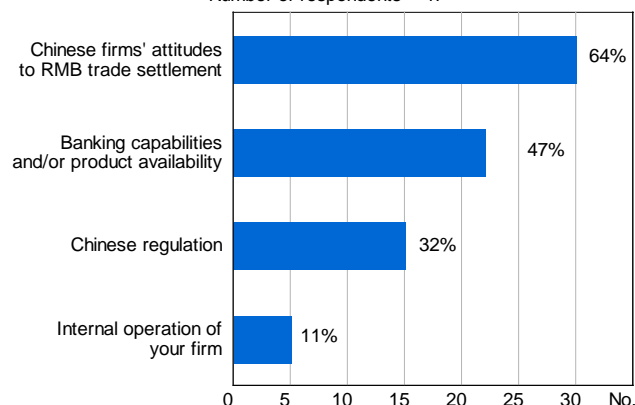
Number of respondents = 17



Graph 8

Would changes in the following increase your use of RMB trade settlement?

Number of respondents = 47

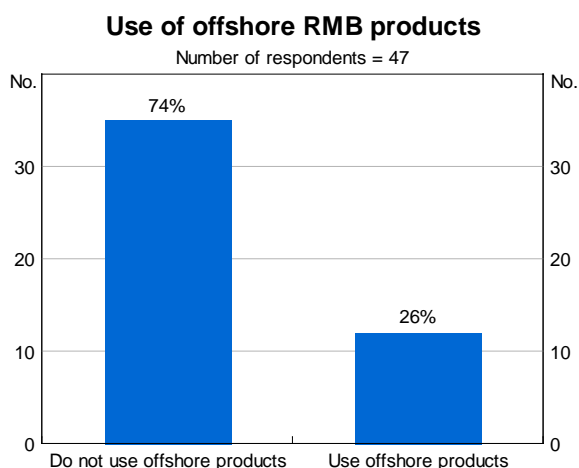


6. Attitudes towards the offshore RMB market

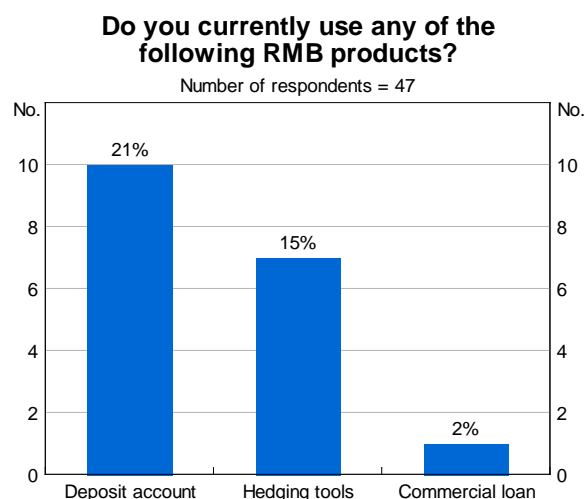
The survey suggests that the take-up of products in the offshore RMB market by firms with Australian operations is relatively limited to date, which is likely related to the fact that RMB trade settlement between Australia and China is itself at an early stage of development. Nevertheless, 26 per cent of respondents indicated that they currently use offshore RMB financial products, mainly for trade settlement and hedging purposes (Graphs 9 and 10). As RMB trade settlement develops, there would appear to be scope for increased use of the offshore RMB market by firms with Australian operations. The easing of regulations guiding the flow of currency into and out of China would also provide an incentive for firms to increase their use of offshore RMB products.

Consistent with firms' limited activity in the offshore RMB market, and given little demand for long-term RMB funding, Australian firms' appetite for issuing RMB-denominated (or 'dim sum' bonds) in Hong Kong also appears limited at this stage.

Graph 9



Graph 10



7. Conclusion

The survey results indicate that the outlook for growth in Australian RMB trade settlement is positive, with firms expecting their use of RMB trade settlement to increase in the future. In particular, RMB trade settlement can help to improve business relationships with Chinese counterparties and enable firms to negotiate better pricing terms.

Nevertheless, the surveyed firms cited several issues associated with RMB trade settlement, including: (i) uncertainty around the ability to hedge resulting foreign currency flows; (ii) the administrative burden arising from unclear or complex procedures (particularly for small and medium enterprises); (iii) issues with documentation, and; (iv) significant time delays in the settlement process.

To this end, the survey suggests that in broad terms, the Australian and Hong Kong banking communities could promote the take-up of RMB trade settlement by:

- Having the infrastructure in place to provide trade settlement services to clients and developing an appropriate suite of associated RMB products;
- Raising private sector awareness regarding the RMB trade settlement process, both with corporate clients and their Chinese counterparties, and;
- Reducing payment delays, possibly by building closer relationships between banks in China, Hong Kong and Australia.

In the offshore RMB market, take-up of products by Australian firms is relatively limited at this stage. However, it is likely that as private sector awareness of this market develops and the appetite for RMB trade settlement grows, so too will the demand for offshore RMB products and RMB-denominated funding and investment.