The RMB Internationalization Strategy and the Role of the e-CNY

An Analysis of the Potential and Challenges of the RMB/e-CNY as Reserve Currency in Reducing USD Dependence

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Abstract

This research investigates the reasons and motivations behind the active efforts of China to develop the status of the RMB, specifically through RMB internationalization and the development of the e-CNY. The research is structured around seven sub-questions that analyze the drivers, current state, US response, potential benefits and risks, and potential impact of the RMB internationalization strategy and the usage of digital currencies on the global financial system and the dominance of the USD as the global reserve currency. The hypothesis suggests that the RMB internationalization strategy of China revolves around the goal to reduce dependency on the USD while enhancing the economic and geopolitical influence of China. Additionally, that the digital nature of the e-CNY presents advantages that can be leveraged over traditional currencies such as the USD to achieve its goal. The research is based on a theoretical framework comprised out of International Political Economy (IPE), Structural Realism, and Rise and Fall theory; a qualitative (deductive content analysis) and quantitative (descriptive quantitative analysis) mixed methods approach. The findings of the research suggest that there has been an upwards trend in the efforts of China to internationalize the RMB despite recent financial and geopolitical influences. In addition to that, that the e-CNY could be a viable alternative to traditional currencies. Therefore, it enhances the RMB internationalization strategy and poses a potential challenge to the dominance of the USD over the current international monetary system (IMS).

Keywords: China, USD, RMB, e-CNY, Internationalization, Digital Currency, Reserve Currency, Economic, Geopolitical, Competition

Abbreviations

BRI – Belt and Road Initiative

BRICS – Brazil Russia India China South Africa

CBDC – Central Bank Digital Currency

CMIC – Chinese Military-Industrial Complex Companies List

E-CNY – Digital Yuan

EUR - Euro

FDI – Foreign Direct Investment

FTA – Free Trade Agreement

FX – Foreign Exchange

GBP – Pound Sterling

GDP – Gross Domestic Product

G-SIB – Globally Systematic Important Banks

IMF – International Monetary Fund

IMS – International Monetary System

IPE – International Political Economy

JPY – Japanese Yen

PBoC – People's Bank of China

PPP – Power Purchasing Parity

Q – Quarter

QE – Quantitative Easing

QT- Quantitative Tightening

RCEP – Regional Comprehensive Economic Partnership

RMB – Renminbi

SDC – Sovereign Digital Currency

SDN – Specially Designated Nationals and Blocked Persons List

SDR – Special Drawing Rights

SWIFT – Society for Worldwide Interbank Financial Telecommunication

US – United States

USD – United States Dollar

WTO – World Trade Organization

Y-o-Y – Year on Year

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1. Introduction

The United States Dollar (USD hereafter) has been the global reserve currency for the larger part of modern history; as such the majority of international reserves are denominated in USD. Transactions for international trade are largely conducted in USD. Moreover, it has shown itself a valuable asset in times of crisis.[1] Nevertheless, since last quarter of 2022 there has been a surge in headlines which suggest that the USD dominance is being challenged by the Chinese Yuan (RMB hereafter).[2] The second largest global economy – based on GDP - severing ties with the US hardly comes as a surprise.[3] Furthermore, the process of decoupling from the USD which has been titled "dedollarization"[4] is not just a phenomenon coming from China, as many countries are currently in the process of setting up trade deals which would be conducted in their own respective currencies, which in turn get right around the USD.[5] This type of bilateral agreements are the foundation for the creation of a secondary economy in the world which is totally independent of the US.[6] The USD dominance which is often portrayed in the form of sanctions[7] could potentially be something of the past; if current trends continue there will be a majority of countries transacting in currencies other than the USD, that there will be no contingency for US sanctions.[8] This has sparked debates with

[1] "The U.S. Dollar as the World's Dominant Reserve Currency," Congressional Research Center (Congressional Research Center , September 15, 2023), https://crsreports.congress.gov/product/pdf/IF/IF11707.

[2] See for example: Andy Mukherjee, "Why the Fed Needs to Take the Digital Yuan Seriously," Bloomberg.com (Bloomberg, December 19, 2022), https://www.bloomberg.com/opinion/articles/2022-12-19/dollar-challenge-the-fed-needs-to-take-the-digital-yuan-seriously#xj4y7vzkg.; Zongyuan Zoe Liu, "China Is Quietly Trying to Dethrone the Dollar," Foreign Policy, September 21, 2022, https://foreignpolicy.com/2022/09/21/china-yuan-us-dollar-sco-currency/.

[3] Michael Hirsh, "The U.S. and China Haven't Divorced Just Yet," Foreign Policy, June 22, 2022, https://foreignpolicy.com/2022/06/22/united-states-china-decoupling-business-ties/.

[4] Tyler Cowen, "The Dollar Rules the World, Now and for the Foreseeable Future," Bloomberg.com (Bloomberg, April 13, 2023), https://www.bloomberg.com/opinion/articles/2023-04-13/the-dollar-rules-the-world-now-and-for-the-foreseeable-future.

[5] See for example: Nidhi Verma and Promit Mukherjee, "Venezuela Hopes to Create Non-Dollar Trading Bloc," Reuters (Thomson Reuters, February 12, 2019), https://www.reuters.com/article/us-india-oil-venezuela-idUSKCN1Q11GF.; Dave Sherwood and Felipe Iturrieta, "Asia-Pacific Nations Sign Sweeping Trade Deal without U.S.," Reuters (Thomson Reuters, March 8, 2018), https://www.reuters.com/article/us-trade-tpp-idUSKCN1GK0JM.; Kaixuan Hao, Liyan Han, and (Tony) Wei Li, "The Impact of China's Currency Swap Lines on Bilateral Trade," *International Review of Economics &Amp; Finance* 81 (September 2022): pp. 173-183, https://doi.org/10.1016/j.iref.2022.05.004.

[6] Saleem Bahaj and Ricardo Reis, "Central Bank Swap Lines: Evidence on the Effects of the Lender of Last Resort," *The Review of Economic Studies* 89, no. 4 (November 8, 2021): pp. 1654-1693, https://doi.org/10.1093/restud/rdab074.

[7] Huricihan Islamoglu, "Sanctions Are the New Global Hegemony," Indian Council on Global Relations, March 15, 2022, https://www.gatewayhouse.in/sanctions-are-the-new-global-hegemony/.

[8] Agathe Demarais, "How U.S. Sanctions Can Backfire ," Center on Global Energy Policy at Columbia University | SIPA, March 15, 2023, https://www.energypolicy.columbia.edu/how-u-s-sanctions-can-backfire/.; Ben Norton, "Countries Worldwide Are Dropping the US Dollar: De-Dollarization in China, Russia, Brazil, ASEAN," Geopolitical Economy Report, April 7, 2023, https://geopoliticaleconomy.com/2023/04/06/dedollarization-china-russia-brazil-asean/.

politicians and analysts on both sides whether or not the dedollarization would mark the beginning of the end for the USD as the global reserve currency, and possibly the establishment of an entirely new global financial system that replaces the USD; the end for the financial hegemony of the US in general.[9]

1.1 The USD as Global Reserve Currency

A global reserve currency is essentially any given currency that is most accepted and traded worldwide.[10] General reserve currencies, including the Euro (EUR hereafter) and the Japanese Yen (JPY hereafter) to some extent, are regarded as particularly safe seeing that they can reliably be used for any transaction.[11] States and Banks tend to hold substantial amounts of these currencies in their portfolio, hence the name "reserve currency." It therefore is a vital asset in international economic governance.[12]

The USD has not always been the global reserve currency and its current form had only been established in the early 1900s. It was not until the mid-20th century that it effectively took the title from the Pound Sterling (GBP hereafter), which had been the global reserve currency during the colonial era of international trade. The Bretton Woods agreement changed this system. At the end of World War II 44 countries sat down and established an efficient system of global finance and trade. The Bretton Woods agreement stipulated that the USD were to be pegged to a set amount of gold: the "gold standard." Consequently, the currencies of all other involved nations were then pegged to the USD.[13] This enabled countries to keep USD in reserve rather than physical gold; which could always be exchanged for gold at any given time should the need arise. This made the USD the default choice in international trade seeing the chance was high that the currencies of trading nations were

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[9] Alex Lo, "End of Dollar Dominance Will Also Spell Demise of US Hegemony," South China Morning Post, April 4, 2023, https://www.scmp.com/comment/opinion/article/3215976/end-dollar-dominance-will-also-spell-demise-us-hegemony.

[10] Anshu Siripurapu, "The Dollar: The World's Currency," Council on Foreign Relations, September 29, 2020, https://www.cfr.org/backgrounder/dollar-worlds-currency.

[11] Serkan Arslanalp, Barry Eichengreen, and Chima Simpson-Bell, "Dollar Dominance and the Rise of Nontraditional Reserve Currencies," IMF, June 1, 2022, https://www.imf.org/en/Blogs/Articles/2022/06/01/blog-dollar-dominance-and-the-rise-of-nontraditional-reserve-currencies.

[12] Thomas Costigan, Drew Cottle, and Angela Keys, "The US Dollar as the Global Reserve Currency: Implications for US Hegemony," *World Review of Political Economy* 8, no. 1 (1, 2017): pp. 104-122, https://doi.org/10.13169/worlrevipoliecon.8.1.0104.

[13] Ramaa Vasudevan, "Dollar Hegemony, Financialization, and the Credit Crisis," *Review of Radical Political Economics* 41, no. 3 (May 4, 2009): pp. 291-304, https://doi.org/10.1177/0486613409335044.

pegged to the USD. It is effectively mandated that nations keep a certain amount of USD in reserve as to always be able to honour currency exchanges at the agreed upon peg price.[14]

During the 1970s the Bretton Woods system fell apart, but the USD has remained the global reserve currency. Mostly because even after the rigid system fell apart, the USD remained the logical choice in international trade.[15] Nowadays the title of "global reserve currency" is lacking in foundation. There is no international treaty or organization which mandates that countries need to recognize the USD as the global reserve currency. And the same was true in the period before the Bretton Woods Agreement.[16] Actually, the Bretton Woods Agreement was effectively the exception which proves the rule: that global reserve currencies become reserve currencies because they are the best available option, and not through official or legal ruling.[17]

The USD has been the global reserve currency since the end of World War II given its historical safety, stability, resiliency, wide recognition, wide circulation and fair value, inasmuch as the system displayed when it was first adopted as a way to keep the price of exchange rates, investments and commodities like oil and gold stable.[18] This accompanied with the fact that no matter which currency, it was pegged to that of the USD: a universal accepted currency with a predictable value in which transactions can be conducted without the concern of getting paid in an uncertain and/or volatile currency.[19] In simpler terms: a global transfer of value through USD which everyone agreed to be safe. Despite no longer being backed by gold, the USD value is fair in the sense that the exchange price is determined by the international market; the strength of the currency of a nation is largely based[20] on the strength of the economy of that nation.[21] Stability, fair value, wide acceptance and wide

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[14] Costigan, Cottle, and Keys, "The US Dollar as the Global Reserve Currency."

[15] Masayuki Tadokoro, "After Dollar?," *International Relations of the Asia-Pacific* 10, no. 3 (2010): pp. 415-440, https://doi.org/https://www.jstor.org/stable/26159514.

[16] "The End of the Bretton Woods System," International Monetary Fund, accessed April 18, 2023, https://www.imf.org/external/about/histend.htm.

[17] "Report to Congress on International Economic and Exchange Rate Policies," U.S. Department of the Treasury Office of International Affairs, 2009, pp. 36-37.

[18] Tamim Bayoumi and Barry Eichengreen, "Ever Closer to Heaven? an Optimum-Currency-Area Index for European Countries," *European Economic Review* 41, no. 3-5 (April 1997): pp. 761-770, https://doi.org/10.1016/s0014-2921(97)00035-4.; Douglas A. Irwin, *Free Trade under Fire*, 5th ed. (Princeton University Press, 2020).

[19] Carol Bertaut, Bastian von Beschwitz, and Stephanie Curcuru, "The International Role of the U.S. Dollar," The Federal Reserve, June 10, 2021, https://www.federalreserve.gov/econres/notes/feds-notes/the-international-role-of-the-u-s-dollar-20211006.html.

[20] Anupam Manur and Varun Ramachandra, "Does a Strong Currency Mean a Strong Economy?," Medium (Indian National Interest, February 9, 2017), https://nationalinterest.in/does-a-strong-currency-mean-a-strong-economy-84c17f2bc11d.

[21] H. Ross Perot and Paul Simon, *The Dollar Crisis: A Blueprint to Help Rebuild the American Dream* (Arlington: Summit Publ., 1996).

circulation are the main components that any currency needs to exhibit to become the global reserve.[22] As of 2023, the USD tops all other currencies in all of these categories.[23] Today around 50% of all international transactions, including the majority of oil purchases, are denominated in USD.[24] Consequently, USD is accepted as legitimate currency basically anywhere in the world,[25] accounts for the majority of reserves,[26] and people view it as safe: one of the main uses for reserve currencies is to protect countries in times of crises.[27]

1.2 A Questionable USD Standard

As turbulence swept through the global economy the past couple of years investors turned towards the USD and drove it to a 20-year high.[28] The global reserve currency status of the USD bestows the US with the exorbitant privilege of an always in demand currency.[29] This gives the US a heightened purchasing power, its government can borrow more in comparison to other countries,[30] and it enables the US to exercise and combine its own dominance with that of the USD on the global financial system.[31] In more general terms, as to effectively sanction any adversaries[32] as it showcased then the US barred Russia out of the SWIFT inter-bank system.[33]

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[22] Vivek Joshi, "'Reserve' Currency: Criteria, Candidates and Consequences," The Sunday Guardian Live, June 25, 2022, https://sundayguardianlive.com/opinion/reserve-currency-criteria-candidates-consequences.

[23] Colby Smith, "US Dollar Remains World's Currency of Choice despite Slide," Financial Times, September 28, 2020, https://www.ft.com/content/3db4174c-d40b-4f3c-8277-481e7175bbd1.

[24] Linda S. Goldberg, Robert Lerman, and Dan Reichgott, "The U.S. Dollar's Global Roles: Revisiting Where Things Stand," Liberty Street Economics (Federal Reserve Bank of New York, July 1, 2022), https://libertystreeteconomics.newyorkfed.org/2022/07/the-u-s-dollars-global-roles-revisiting-where-things-stand/.

[25] Eswar Prasad , "Enduring Preeminence," International Monetary Fund , June 2, 2022, https://www.imf.org/en/Publications/fandd/issues/2022/06/enduring-preeminence-eswar-prasad.

[26] "Currency Composition of Official Foreign Exchange Reserves (COFER)," International monetary Fund, March 31, 2023, https://data.imf.org/?sk=E6A5F467-C14B-4AA8-9F6D-5A09EC4E62A4.

[27] "Global Economic Prospects," World Bank Group, January 2023, https://doi.org/10.1586/978-1-4648-1906-3.; Indradip Ghosh, "Dollar to Rebound, Accumulate Safe-Haven Strength in 2023: Reuters Poll," Reuters (Thomson Reuters, December 7, 2022), https://www.reuters.com/markets/currencies/dollar-rebound-accumulate-safe-haven-strength-2023-2022-12-07/.

[28] Siladitya Ray, "U.S. Dollar Hits 20-Year High: Here's What That Means," Forbes (Forbes Magazine, October 12, 2022), https://www.forbes.com/sites/siladityaray/2022/08/29/us-dollar-hits-two-decade-high-heres-what-that-means/?sh=3ee609455b86.

[29] Barry Eichengreen, *Exorbitant Privilege: The Rise and Fall of the Dollar and the Future of the International Monetary System* (Oxford: Oxford University Press, 2012).

[30] Carmen M. Reinhart, "Addicted to Dollars," Project Syndicate, December 13, 2017, https://www.project-syndicate.org/commentary/dollar-global-dominance-unsustainable-by-carmen-reinhart-2017-03.

[31] Craig Karmin, *Biography of the Dollar: How the Mighty Buck Conquered the World and Why It's under Siege* (New York: Three Rivers Press, 2009).

[32] Stephen Kirchner, "The 'Reserve Currency' Myth: The US Dollar's Current and Future Role in the World Economy," United States Studies Centre, November 11, 2019, https://www.ussc.edu.au/analysis/the-reserve-currency-myth-the-us-dollars-current-and-future-role-in-the-world-economy.

[33] Marco Cipriani, Linda S. Goldberg, and Gabriele La Spada, "Financial Sanctions, SWIFT, and the Architecture of the International Payments System," 1047 Financial Sanctions, SWIFT, and the Architecture of

This exercise of power and dominance by the US is something that both China[34] and Russia have addressed for a longer amount of time. In particular after the financial crisis of Russia in the 90s, which forced Russians to adopt the USD instead of the Ruble.[35] Back in 2009, after the Russian Parliament banned public officials from using USD as a unit of account, Dmitry Medvedev proposed a super currency which would replace the USD.[36] This sentiment can also be detected more recently on the Chinese side. In February 2023, the Ministry of Foreign Affairs of the People's Republic of China published the "US Hegemony and Its Perils," which criticized that the USD is the main source of uncertainty and instability in the global economy. Moreover, it argued that the US (ab)uses the global reserve currency status of the USD to coerce other nations into serving the economic and political strategy of the US.[37]

Given the fact that Russia has been shunned from much of the global financial system, it has been searching for alternatives to soften the blow of Western sanctions. It saw an economic lifeline in China[38] and the trade between the two nations rose 34.3% marking a record of 190 billion USD in 2022;[39] another 19.8% increase in Q1 of 2023.[40] Much of the associated transactions were made in RMB and Rubles respectively.[41] The Russian Central Bank has been trying to reduce its dependence on Western currencies, even before the start of the war in Ukraine in 2022.[42] That said, the invasion further accelerated these efforts during the third quarter of 2022. In the past year transactions in USD and EUR on the Russian foreign exchange (FX hereafter) market and foreign currency within the Russian banking system fell to an all-time-low of 15%. In April of 2023 the RMB surpassed the USD as the most traded currency on the Russian FX market with a market share of almost 40% of trading

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the International Payments System (2023), pp. 12-25.; Henry Farrell and Abraham L. Newman, "Weaponized Interdependence: How Global Economic Networks Shape State Coercion," *International Security* 44, no. 1 (2019): pp. 42-79, https://doi.org/10.1162/isec_a_00351.

[34] Covell Meyskens, "China Is Pushing Disengagement with the United States Hard," Foreign Policy, March 8, 2023, https://foreignpolicy.com/2023/03/08/china-disengagement-america-cold-war/.

[35] Alan H. Smith, *Russia and the World Economy: Problems of Integration* (London: Routledge, 1993).

[36] Tamás Gábor, "The ASSYMETRICAL Dollar-Based Monetary System and Global Financial Imbalances," *SSRN Electronic Journal* 2 (May 2010): p. 7, https://doi.org/10.2139/ssrn.1599463.

[37] "US Hegemony and Its Perils," Ministry of Foreign Affairs of the People's Republic of China, February 20, 2023, https://www.fmprc.gov.cn/mfa_eng/wjbxw/202302/t20230220_11027664.html.

[38] Philipp Ivanov, "Can Russia Get Used to Being China's Little Brother?," Foreign Policy, March 21, 2023, https://foreignpolicy.com/2023/03/21/xi-putin-meeting-russia-china-relationship/.

[39] "China's 2022 Trade with Russia Hit Record $190 Bln - Customs," Reuters (Thomson Reuters, January 13, 2023), https://www.reuters.com/world/china-customs-says-trade-with-russia-hit-new-high-2022-2023-01-13/.

[40] "China's Trade with Russia Surges at Double-Digit Pace in Jan-Feb," Reuters (Thomson Reuters, March 7, 2023), https://www.reuters.com/business/chinas-trade-with-russia-surges-double-digit-pace-jan-feb-2023-03-07/.

[41] Maia Nikoladze and Mrugank Bhusari, "Russia and China Have Been Teaming up to Reduce Reliance on the Dollar. Here's How It's Going.," Atlantic Council, February 22, 2023, https://www.atlanticcouncil.org/blogs/new-atlanticist/russia-and-china-have-been-teaming-up-to-reduce-reliance-on-the-dollar-heres-how-its-going/.

[42] Juliet Johnson, "Forbidden Fruit: Russia's Uneasy Relationship with the US Dollar," *Review of International Political Economy* 15, no. 3 (2008): pp. 379-398, https://doi.org/10.1080/09692290801928749.

volume.[43] Russia, while increasingly turning towards the RMB as its reserve currency, supports the use of the RMB in trade with other countries. The two largest geopolitical adversaries of the US suited their actions to their words with Putin pledging to adopt the RMB as the unit of account for transactions between Russia and countries in Latin America, Africa and Asia, in a bid to displace the USD. This while also expressing confidence that a similar form of payment will be adopted between Russian partners and their colleagues in third countries.[44] The adaptation of the RMB as account unit cemented the "No Limits" partnership between Russia and China; an agreement was made to expand their economic ties.[45] China already is a major importer of discounted Russian gas and oil and its imports of Russian coal have surged 31% (y-o-y) to more than 68 million tonnes in 2022. Russia, in turn, has also been ramping up imports of Chinese goods including machinery and metals.[46]

This was the catalyst for some major anxiety in the US about a scenario in which the USD lost its status as the global reserve currency, followed by a total implosion of the US economy through inflation and recession, and ultimately end in the US losing its status of superpower. Correspondingly, statements have been made that the US would need to default on its deficits if the USD lost its status as the global reserve currency.[47] With reference to data of the past 20 years, Russia and China might be on the right course when it comes to their aim for dedollarisation.[48] Even though the USD has dominated global capital flows and trade for decades, its share in global central bank reserves has in 20 years dropped to less than 60% (from roughly 70%).[49] This might be a warrant, in the next 20 years, if the strategy of Russia and China works out that there might be the rise of a new reserve currency in the form of the RMB.

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[43] Alexandra Prokopenko, "The Risks of Russia's Growing Dependence on the Yuan," Politika (Carnegie Endowment for International Peace, February 2, 2023), https://carnegieendowment.org/politika/88926.
[44] "Russia Supports Yuan Payments in Trade with Other Countries - Putin," TASS, March 21, 2023, https://tass.com/economy/1592277.
[45] Long Zhao, "Constructive Synergy: Beijing–Moscow No-Limits Partnership in Perspective," *China Quarterly of International Strategic Studies* 08, no. 02 (2022): pp. 107-126, https://doi.org/10.1142/s2377740022500051.
[46] Georgi Kantchev and Chelsey Dulaney, "Russia Boosts China Trade to Counter Western Sanctions," The Wall Street Journal (Dow Jones & Company, January 31, 2023), https://www.wsj.com/articles/russia-ramps-up-china-trade-to-counter-western-sanctions-11675079584.
[47] Paul Krugman, "Wonking Out: International Money Madness Strikes Again," The New York Times (The New York Times, April 14, 2023), https://www.nytimes.com/2023/04/14/opinion/dollar-reserve-currency.html.
[48] Zoe Liu Zongyuan, "Besides China, Putin Has Another Potential De-Dollarization Partner in Asia," Council on Foreign Relations (Council on Foreign Relations, March 11, 2022), https://www.cfr.org/blog/besides-china-putin-has-another-potential-de-dollarization-partner-asia.
[49] Serkan Arslanalp and Chima Simpson-Bell, "US Dollar Share of Global Foreign Exchange Reserves Drops to 25-Year Low," International Monetary Fund , May 5, 2021, https://www.imf.org/en/Blogs/Articles/2021/05/05/blog-us-dollar-share-of-global-foreign-exchange-reserves-drops-to-25-year-low.

1.3 The RMB and e-CNY

The RMB has become an increasingly significant currency in the international market in recent years. Since 2016, the RMB has been included in the International Monetary Fund's reserve currency pool, along with the USD, EUR, JPY, and GBP. This recognition reflects the growing importance of the RMB as a global currency.[50] The rise of the RMB to prominence has been driven largely by the expanding economy of China and the efforts of the country to internationalize its currency.[51] In 2009, China launched the "dim sum bond" market, which allowed foreign investors to purchase RMB-denominated bonds. This development helped to promote the use of RMB in international trade and investment. Since then, China has continued to take steps to increase the global use of the RMB.[52] Despite these efforts, the position of the RMB in the international currency market is still relatively small compared to the USD. However, the RMB has been steadily gaining influence in recent years, and many analysts believe that it could eventually challenge the dominance of the USD.[53] Historically, the RMB has undergone significant fluctuations in value over the past decades. From 1995 to 2005, the yuan was pegged to the USD,[54] which many experts believed was undervalued. This led to criticism from multiple countries, particularly the US, that argued that China was manipulating the value of the RMB to gain an unfair advantage in international trade.[55] In 2005, China abandoned the fixed exchange rate and allowed the RMB to appreciate gradually against the dollar, except for during the global financial crisis when the exchange rate was kept stable.[56] This move was seen as a step towards a more market-oriented exchange rate system and helped to ease tensions with other countries;[57] to

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[50] "IMF Adds Chinese Renminbi to Special Drawing Rights Basket," International Monetary Fund , September 30, 2016, https://www.imf.org/en/News/Articles/2016/09/29/AM16-NA093016IMF-Adds-Chinese-Renminbi-to-Special-Drawing-Rights-Basket.

[51] Cameron Rotblat, "Weaponizing the Plumbing: Dollar Diplomacy, Yuan Internationalization, and the Future of Financial Sanctions," *Journal of International Law and Foreign Affairs* 1, no. 2 (2017): pp. 311-316.; Agnès Bénassy-Quéré and Yeganeh Forouheshfar, "The Impact of Yuan Internationalization on the Stability of the International Monetary System," *Journal of International Money and Finance* 57 (October 2015): pp. 115-135, https://doi.org/10.1016/j.jimonfin.2015.05.004.

[52] Hung-Gay Fung, Derrick Tzau, and Jot Yau, "Offshore Renminbi-Denominated Bonds," *The Chinese Economy* 46, no. 2 (December 9, 2013): pp. 6-28, https://doi.org/10.2753/ces1097-1475460201.

[53] Garić Dankoa and Filipović Sanjab, "Ima Li Izgleda Da Juan Bude Nova Svetska Rezervna Valuta?," *Industrija* 47, no. 2 (2017): pp. 61-75.; Alec Chrystal, "PDF" (London, October 2021).

[54] Jing Qin et al., "The Effectiveness of China's RMB Exchange Rate Reforms: An Insight from Multifractal Detrended Fluctuation Analysis," *Physica A: Statistical Mechanics and Its Applications* 421 (March 2015): pp. 443-454, https://doi.org/10.1016/j.physa.2014.11.053.

[55] Arthur R. Kroeber, "The Renminbi: The Political Economy of a Currency," Brookings (Brookings, September 28, 2016), https://www.brookings.edu/research/the-renminbi-the-political-economy-of-a-currency/.

[56] Sonali Das, "China's Evolving Exchange Rate Regime" (International Monetary Fund, 2019), p. 6.

[57] Uri Dudush, Shimelse Ali, and Rachel Espin Odell, "Exchange Rate Regimes and Protectionism ," Carnegie Endowment for International Peace, July 1, 2011, https://carnegieendowment.org/2011/07/01/exchange-rate-regimes-and-protectionism-pub-44894.

achieve financial and macroeconomic stability in China.[58] Since then, the RMB has continued to display a fluctuation in value in response to various economic and political factors.[59]

Adjusted for purchasing power (GDP[60] tracked in PPP[61] terms), China has now the largest economy in the world. China is also the biggest global trading nation, importing and exporting more than the US and EU.[62] Despite its wide use, the share of RMB constitutes less than 3% of global currency reserves,[63] this seeing the amount of roadblocks China faced in its attempts to expand the international role of the RMB.[64] This limits the economic potential of China, and probably more importantly, its influence.[65] Being the global reserve currency comes with a lot of advantages.[66] This is why there is a high probability that the Chinse government wants to aim for the RMB to become the global reserve or at the very least a viable alternative to the USD.[67]

Regardless of the attempts of the USA to maintain its supremacy over the global financial system, more and more countries are establishing trade agreements in local currencies and gold, rather than the dollar. There are plenty of other headlines in regard to,

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[58] "Further Reform the RMB Exchange Rate Regime and Enhance the RMB Exchange Rate Flexibility," The People's Bank of China, June 9, 2010, http://www.pbc.gov.cn/publish/english/955/2010/20100622144059351137121/20100622144059351137121_.html.

[59] Wei Guo and Zhongfei Chen, "China–US Economic and Trade Relations, Trade News, and Short-Term Fluctuation of the RMB Exchange Rate," *Review of International Economics* 31, no. 1 (2022): pp. 180-203, https://doi.org/10.1111/roie.12622.

[60] Gross Domestic Product, or GDP, is a way of measuring the output of an economy. It is representative of the total value of all goods and services produced in a country, plus any net income from abroad, over a specific period. GDP is often indicative of the health and size of an economy.

[61] Purchasing Power Parity, or PPP, is one of the methods used to compare standards of living and economic productivity between countries. PPP takes notice of the relative cost of living and inflation rates in countries, adjusted for differences in purchasing power of currencies, which enables a more accurate overview of economic indicators in comparison to GDP.

[62] Edie Purdie, "Tracking GDP in PPP Terms Shows Rapid Rise of China and India," World Bank Blogs, October 16, 2019, https://blogs.worldbank.org/opendata/tracking-gdp-ppp-terms-shows-rapid-rise-china-and-india.

[63] "Currency Composition of Official Foreign Exchange Reserves (COFER)," International monetary Fund.

[64] See for example: Terry E. Chang, "Slow Avalanche: Internationalizing the Renminbi and Liberalizing China's Capital Account," *Columbia Journal of Asian Law* 25, no. 1 (January 1, 2012), https://doi.org/https://doi.org/10.7916/cjal.v25i1.3315.; Guorui Sun and Alex Payette, "China and the Impossible Trinity: Economic Transition and the Internationalization of the Renminbi," *Contemporary Chinese Political Economy and Strategic Relations: An International Journal* 2, no. 3 (December 2016): pp. 1049-1093.: Cheung-Kwok Law, "Sustainability of RMB Internationalization," in *Green Finance, Sustainable Development and the Belt and Road Initiative*, 1st ed. (Rootledge, 2020), pp. 58-88.

[65] Gerard DiPippo and Andrea Leonard Palazzi, "It's All about Networking: The Limits of Renminbi Internationalization," Center for Strategic & International Studies CSIS, April 18, 2023, https://www.csis.org/analysis/its-all-about-networking-limits-renminbi-internationalization.; Edward Prasad and Lei Ye, "The Renminbi's Prospects as a Global Reserve Currency," *Cato Journal* 33, no. 3 (2013): pp. 563-570.

[66] Anshu Siripurapu, "The Dollar: The World's Currency," Council on Foreign Relations, September 29, 2020, https://www.cfr.org/backgrounder/dollar-worlds-currency.

[67] Christopher Clayton et al., "Internationalizing like China," *National Bureau of Economic Research*, August 2022, https://doi.org/10.3386/w30336.

for example, France, India, Brazil and Saudi Arabia also turning away from the USD.[68] China and France settled a major liquefied natural gas contract in RMB, followed by an announcement of French president Emmanuel Macron stating that Europe needs to lessen its dependence on the Dollar.[69] India announced that it would no longer require USD in its trade with Argentina. Additionally, Brazil announced plans to set up a common currency for South America.[70] And, on top of the ASEAN agenda is now the reduction of the dependence on the USD, EUR, JPY, and GBP in financial transactions and move to settlements in local currencies.[71] Probably even more noteworthy is BRICS[72] announcing plans to develop a new currency which will be backed by gold and other crucial commodities. That said, it has not formally been announced whether or not a currency of one of the member states would be adopted as BRICS reserve currency. In this aspect, and seeing that China is by far the most influential of the BRICS[73] it would be quite logical to adopt the RMB as BRICS reserve currency, rather than creating a completely new currency.[74] The Russian State Duma indicated that the future BRICS reserve currency might very well be a central bank digital currency (CBDC hereafter):[75] something China has been developing since 2014.[76]

The digital RMB (e-CNY hereafter), is a new form of currency developed by the People's Bank of China. The e-CNY is a CBDC that is designed to complement the existing physical RMB and provide a more efficient and secure payment system within the economic

[68] Ben Norton, "Countries Worldwide Are Dropping the US Dollar: De-Dollarization in China, Russia, Brazil, ASEAN," Geopolitical Economy , April 24, 2023, https://geopoliticaleconomy.com/2023/04/06/dedollarization-china-russia-brazil-asean/.
[69] Jamil Anderlini and Clea Caulcutt, "Europe Must Resist Pressure to Become 'America's Followers,' Says Macron," POLITICO, April 12, 2023, https://www.politico.eu/article/emmanuel-macron-china-america-pressure-interview/.
[70] Federico Steinberg and Miguel Otero-Iglesias, "South America's 'Common Currency' Is Actually about De-Dollarization," CSIS, February 14, 2023, https://www.csis.org/analysis/south-americas-common-currency-actually-about-de-dollarization.
[71] Prime Sarmiento, "ASEAN Makes Big Push to Use Local Currencies," China Daily, April 3, 2023, https://www.chinadaily.com.cn/a/202304/03/WS642a2abca31057c47ebb7f9d.html.
[72] BRICS can be seen as a rival to the Western G7 Alliance and stands for Brazil, Russia, India, China and South Africa. As of 2023, BRICS is set to expand with possible new members such as Saudi Arabia, Algeria, Iran, Argentina, Turkey and the UAE.
[73] Gundumella Raman, "China and the BRICS," *SSRN Electronic Journal*, March 28, 2018, https://doi.org/10.2139/ssrn.3151252.
[74] Joseph W. Sullivan, "A BRICS Currency Could Shake the Dollar's Dominance," Foreign Policy, April 24, 2023, https://foreignpolicy.com/2023/04/24/brics-currency-end-dollar-dominance-united-states-russia-china/.
[75] Zahra Tayeb, "The Anti-Dollar Drive Spearheaded by Asia Has Spread to Europe, with France Growing Sour on the Greenback's Dominance. Here Are 6 Rising Threats to the Buck's Supremacy of Global Trade.," Business Insider, April 19, 2023, https://markets.businessinsider.com/news/currencies/dollar-dominance-russia-china-india-brazil-oil-trade-reserve-currency-2023-1#russia-and-iran-eye-a-gold-backed-stablecoin-4.
[76] *Progress of Research & Development of E-CNY in China*, Working Group on E-CNY Research and Development of the People's Bank of China (2021): 1.

influence sphere of China.[77] Sovereign digital currency (SDC) or CBDC is the monetary power of an economy's digital equivalent of sovereign money.[78] CBDC regards itself to many segments such as, but not limited to, financial inclusion, compliance, governance models, data protection and sovereignty, and digital payment ecology.[79]

China is expected to be the first major economy to launch CBDC on a large scale (out of pilot phase).[80] The People's Bank of China started CBDC research in 2014. e-CNY pilots have been conducted on a large scale in ten regions (e.g. Shenzhen, Beijing and Shanghai).[81] There is a high probability that e-CNY will lead to an economic ecosystem that encompasses more than just valuta or a new currency infrastructure.[82] E-CNY is "an entire ecosystem with connectors to existing and newly developing payment systems and currencies,"[83] with systems comprised of, among others, payment and e-commerce which involve banking institutions, big tech and individuals. Multinationals such as Starbucks and McDonald's have been involved in the e-CNY trial.[84] It is very likely that the e-CNY is going to become an important future of the financial system and digital economy of China.[85] China's CBDC holds potential to become a major currency CBDC with global implications.[86] In regards to CNBC, it has been commented that whatever move China makes will affect other national economies.[87] It is rather likely that China's CBDC will be "*the* powerful disruption that kickstarts a move from the extensive SDC-related research and piloting […] to multiple cases of issuance of SDC, in particular by major economies."[88] The e-CNY has the potential to

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[77] Arendse Huld, "China Launches Digital Yuan App – All You Need to Know," China Briefing News, accessed March 17, 2023, https://www.china-briefing.com/news/china-launches-digital-yuan-app-what-you-need-to-know/.

[78] John Kliff, et al., *A Survey of Research on Retail Central Digital Currency*, IMF Working Paper No. 20/104 (2020): 5.

[79] *Central bank digital currencies: system design and interoperability*, Bank for International Settlements No. 2 (2021): 1-2.

[80] Theodore Benzmiller, "China's Progress Towards a Central Bank Currency," CSIS, accessed March 16, 2023, https://www.csis.org/blogs/new-perspectives-asia/chinas-progress-towards-central-bank-digital-currency

[81] *Progress of Research & Development of E-CNY in China*, People's Bank of China.

[82] David Olsson et al., "China's Digital RMB – Is Your Business Ready?" King & Wood Mallesons, accessed March 17, 2023, https://www.kwm.com/au/en/insights/latest-thinking/chinas-digital-rmb-is-your-business-ready.html.

[83] Vipin Bharathan, "E-CNY Progress Report Reveals Telling Details About The Chinese Retail CBDC Project," Forbes, accessed March 17, 2023, https://www.forbes.com/sites/vipinbharathan/2021/07/19/e-cny-progress-report-reveals-telling-details-about-the-chinese-retail-cbdc-project/?sh=223ecdc06a59.

[84] Georgiana Lee and Samuel Shen, "China's digital yuan stands out in cross-border pilot in a show of global ambition," Reuters, accessed March 17, 2023, https://www.reuters.com/markets/currencies/chinas-digital-yuan-stands-out-cross-border-pilot-show-global-ambition-2022-10-27/.

[85] Olsson et al., "China's Digital RMB – Is Your Business Ready?"

[86] Dirk Andreas Zetzsche et al., "Sovereign Digital Currencies: The Future of Money and Payments?" *University of Hong Kong Faculty of Law Research Paper* 53 (October 19, 2020): 11, https://doi.org/10.2139/ssrn.3714386.

[87] Bharathan, "E-CNY Progress Report Reveals Telling Details About The Chinese Retail CBDC Project."

[88] Zetzsche et al., "Sovereign Digital Currencies: The Future of Money and Payments?"

reinforce the position of China as a global economic powerhouse. By developing and implementing the e-CNY, China positions itself at the forefront of the emerging digital currency market, while demonstrating its technological capabilities. Additionally, the e-CNY has the potential to reduce China's reliance on the USD and help its process of dedollarization, which aligns with China's broader goal of internationalizing the RMB.[89]

1.4 Problem Formulation

The aim of this research is to explore the potential and challenges in the RMB internationalization strategy of China and the potential role of the RMB as global reserve currency. More specifically, the research will explore the development of the e-CNY and the probably impact of it on reducing the dependency of China on the USD. Moreover, the research will also investigate how China is leveraging the advantages of its economy, global status, and future digital currency to enhance its global geopolitical and economic influence. Therefore the following research question is posed:

Why is China so active in developing the status of the Yuan; consequently the e-CNY?

Through the usage and application of International Political Economy (IPE), Realism, and the Rise and Fall theory, the research will either accept or refute the following hypothesis:

The efforts of China to promote the usage of RMB and e-CNY are part of a broader strategy to reduce the dependency of China on the USD while enhancing its geopolitical and economic influence. The digital nature of the e-CNY presents advantages over traditional currencies such as the USD that China can capitalize on, in competition with the USD, to achieve this goal.

Research into the internationalization strategy of the RMB and the place of the e-CNY within this strategy is highly relevant and timely given the growing economic influence of China and the current geopolitical climate. The research aims to contribute to the knowledge of how the currency strategy of China is intertwined with its long-term political and economic goals. Additionally, the research aims to display the potential implications of the rise of the RMB as a possible major reserve currency and viable alternative to the USD for the global financial system and the dominance of the USD.

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[89] Cameron Roblat, "Weaponizing the Plumbing: Dollar Diplomacy, Yuan Internationalization, and the Future of Financial Sanctions," *UCLA Journal of International Law and Foreign Affairs* 21 (2017): pp. 311-360.

2. Methods and Methodology

The aim of the research is to analyze the RMB internationalization strategy of China; the development of the e-CNY. Moreover, the research also puts a focus on the potential and challenges of the role of the RMB as a reserve currency, and potential global reserve currency, in reducing the dependence of China on the USD. The research hypothesizes that the efforts of China to push the usage of the RMB and e-CNY are part of a larger scale strategy to reduce the dependency of China on the USD and increase its geopolitical and economic influence. The digital nature of the e-CNY displays advantages compared to traditional currencies, which China can hone in on to achieve this goal. Research into this topic is highly relevant given the current geopolitical climate and the growing economic influence of China, as well as the potential implications the rise of the RMB as a reserve currency may impose on the dominance of the USD and the global financial system.

To achieve the aim of the research and test the posed hypothesis, the study will use a mixed methods approach that combines deductive qualitative analysis and descriptive quantitative analysis. The main source of data will be government publications, academic articles, and other publications from official sources, which will be analyzed using a deductive content analysis. Additionally, supporting statistical data will be analyzed using descriptive statistical methods. This to provide additional context and detail for the analysis.

In the methods and methodology section a detailed explanation of the research design, data collection methods, and analytical techniques used in the research will be provided. Moreover, potential biases and limitations of the data sources and the methods used to analyze them will be discussed. Overall, the mixed methods approach will allow for a nuanced and comprehensive understanding of the RMB/e-CNY internationalization strategy of China, and potential impactions for the global financial system.

2.1 Research Strategy

As stated before, the research aims to answer the following research question:

Why is China so active in developing the status of the Yuan; consequently the e-CNY?

Based on the research question, the following sub question have been established as to guide the research process:

1. What is the historical context of the USD becoming the global reserve currency and how is this status challenged by current events?

2. What is the historical context of the efforts of China to internationalize the RMB and develop the e-CNY?
3. What are the main drivers of the RMB internationalization strategy of China and how do these drivers relate to the broader economic and geopolitical goals of China?
4. What is the current state in regard of the internationalization of the RMB, and which factors influence the adoption rate of the RMB?
5. What has been the response of the US concerning the RMB internationalization strategy of China, and how might this response pose potential implications for the broader geopolitical position of China?
6. What are the potential benefits of using digital currencies such as the e-CNY for international transactions?
7. What is the potential impact of the usage of digital currencies such as the e-CNY on global financial systems and the dominance of the USD as the global reserve currency?

The research opts for a mixed methods approach of deductive qualitative analysis and descriptive quantitative analysis for multiple reasons. Firstly, the posed research question and aims require a comprehensive understanding of the RMB internationalization strategy of China, and the role of the RMB as a reserve currency. Through the usage of a mixed methods approach, a more holistic view of the topic can be obtained. The mixed methods approach allows for a broader range of information which provides a more complete overview of the subject matter.

Secondly, a deductive qualitative analysis can provide insights in regard to the motivations behind the currency strategy of China and the geopolitical and economic goals connected to the strategy. The deductive qualitative analysis allows the research for an analysis and interpretation of the underlying meaning of the gathered date, including relationships, themes, and patterns, to get a better understanding of the research topic. Despite the fact that qualitative research has a general association with the gathering of theories rather than testing them, numerous studies have highlighted that, this approach can indeed be used to test them.[90] Deductive content analysis is a method that combines qualitative data with a deductive approach. This entails starting with a pre-existing theory or hypothesis and utilizing it to drive qualitative data analysis. Thus, the research starts with a preset set of categories or codes that correspond to the theory or hypothesis, and then utilize

[90] Colin Robson and Kieran McCartan, *Real World Research* (Fourth Edition) (Hoboken, U.S.: Wiley, 2017).

those codes to methodically evaluate the data. This method can be used to validate or reject the hypothesis, or to develop the theory by finding additional themes or categories that arise from the data.[91] To further hone and validate or reject the hypothesis, the research can be combined with and supported by quantitative data which will ultimately lead to the revision of the theory to greater or lesser extent depending on the presented data.[92]

The descriptive quantitative analysis part of the mixed methods approach allows for the usage of numerical data to gain an understanding of the current state of the internationalization of the RMB and the role of the e-CNY in reducing the dependence of China on the USD. Statistical information coming from the quantitative analysis provides the research with the ability to identify patterns and trends, and to make comparisons with the USD.

2.1.1 Data Collection

Seeing that the research will not employ any primary data collection such as surveys or interviews, gathering secondary data sources will be the main way of data acquisition. In this context secondary data includes sources such as books, reports, journals, and other relevant materials. The sources used in the research have been selected according to their trustworthiness, dependability, and how applicable they are. In order to collect data for this research, a combination of search strategies was used:

1. **Keyword search:** use appropriate keywords and phrases within the research topic to gather pertinent sources.
2. **Database search:** use credible scholarly databases such as JSTOR and Wiley to find applicable references.
3. **Citation chaining:** scan the reference lists of used sources to find further relevant material.
4. **Official website search:** search on the official websites of governments, NGO's and reputable companies for published reports.

Additionally the following criteria were considered during the selection of sources for the research:

[91] Helvi Kyngäs and Pirjo Kaakinen, "Deductive Content Analysis," The Application of Content Analysis in Nursing Science Research, November 1, 2019, pp. 26-30, https://doi.org/10.1007/978-3-030-30199-6_3.
[92] Alan Bryman, *Social Research Methods*, (Oxford: OUP Oxford, 2012), pp. 416-424.

1. **Relevance:** the research question and sub questions need to be pertinent to the selected sources.
2. **Credibility:** reliable, trustworthy and from reputable publishers, writers or groups such as scholarly books and peer-reviewed journal papers.
3. **Currency:** sources need to be up to date and relevant.
4. **Objectivity:** sources ought to be neutral and impartial, or disclose potential bias such as their own view, opinion or association.
5. **Authority:** sources from subject-matter specialists or leaders in the field, such as scholars, professionals, or research groups.
6. **Accessibility:** the research materials are openly available and only full-text sources were used.

Seeing that the main body of data consists out of secondary literature, it will be largely analyzed through a deductive content analysis; to evaluate the research hypothesis. In order to carry out a deductive content analysis, a structural coding method will be employed. For this a pre-defined category scheme needs to be set up. This category scheme is based off the research topic and lead by the research question and sub questions and aims to recognize and classify data in accordance to a preset of ideas. The research proposes the following predetermined codes:[93]

1. **RMB internationalization strategy:** any texts that are related to the overall strategy of China to promote the RMB as an international and reserve currency. Topics include currency swaps, bilateral agreements, and the internationalization of the RMB bond market.
2. **E-CNY development and adoption:** any work that addresses the development and adoption of the e-CNY. Codes include adoption rates, pilot programmes, and regulatory frameworks.
3. **Economic and geopolitical implications:** refers to any literature related to the economic and geopolitical implications of the currency strategy of China. Codes include the international relations of China, potential risks and challenges, and global economic power dynamics.

[93] Note: During the line-by-line coding process, these themes have been revised and further refined.

4. **USD dependence:** any text which refers to potential impacts of the rise of the RMB in connection with dedollarization. Codes include international trade settlements, currency swaps, and the usage of RMB as reserve currency.
5. **Advantages and disadvantages of digital currencies:** codes include reduced transaction costs, increased efficiency, and technological lead.

Given that the predefined categories and codes are consistently applied across the collected data, structured coding ensures the uniformity and objectivity of the research; that the analysis is based on the research question and any findings legitimate.

2.2 Method of Analysis

Taking the research strategy and data collection in mind, the research employs a mixed methods approach of qualitative analysis, more specifically a deductive content analysis, and a quantitative analysis, in the form of descriptive quantitative analysis. This section will define the characteristics of the chosen methods of analysis and elaborate on the justification of the use of the chosen methods.

2.2.1 Qualitative Analysis

Qualitative analysis is a method of researching that aims to gather and interpret non-numerical data such as documents and observations. The objective is to understand and interpret the meaning of social phenomena. A key benefit of qualitative research is that it can generate detailed and in-depth data, which helps to understand complex issues.[94] Deductive content analysis is a specific method of qualitative analysis, which makes use of a pre-existing theoretical framework in order to analyze the gathered data. A pre-determined set of categories and codes based on the framework are applied to the data in order to identify themes and patterns. Deductive content analysis is a useful method to determine how certain data fits with a hypothesis or pre-existing theory.[95] In the context of this research into the RMB internationalization strategy of China and the development of the e-CNY, a qualitative analysis and specifically, deductive content analysis are highly applicable. This seeing that the research question and sub-questions focus on analyzing the potential and challenges of the strategy of China, as well as interpreting how China is utilizing the advantage digital currencies to enhance its geopolitical and economic influence. Qualitative analysis enables a

[94] Monique Hennink, Inge Hutter, and Ajay Bailey, *Qualitative Research Methods* (Los Angeles: Sage, 2020).
[95] Kyngäs and Kaakinen, "Deductive Content Analysis."

deeper understanding of these complex topics, and deductive content analysis enables the research to identify themes and patterns that fit within the pre-determined framework. Additionally, seeing that the topic is current, qualitative research supports the exploration of insights, which may not be captured through quantitative methods due to a lack of reliable and long-term data.

2.2.2 Quantitative Analysis

Quantitative analysis regards to the use of numerical data and statistical methods in order to analyze phenomena and identify relationships or patterns.[96] In the context of this research, quantitative analysis can be used to measure the degree of internationalization of the RMB and the impact of the trend on reducing the dependency of China on the USD. Descriptive quantitative analysis is applicable to this research seeing that it provides a concise summary of data. The research will, for example be used to analyze the usage of RMB in international transaction or the amount of RMB in FX reserves. The descriptive quantitative analysis is complimentary to the qualitative analysis given that it provides quantitative evidence to support or refute the qualitative findings.[97]

2.2.3 Choice of Theory

The theoretical framework for the research consists out of three perspectives: International Political Economy (IPE), Realism, and the Rise and Fall theory. IPE presents insights into the interaction between politics and economics within international relations, and will establish a foundation for understanding the context of the RMB internationalization strategy of China. Realism focusses on the behavior of power and the state. This will aid in exploring the motivations and actions of China in pursuing this strategy. The rise and fall theory will enable the research to provide a comparative and historical perspective on the rise of China and potential implications for the international system. Through the synthetization of these three perspectives, the research aims to set up a comprehensive analysis of the currency strategy of China and the potential impact on the global political and economic order. In the theory chapter of this research a more thorough elaboration on each of the chosen theories and a justification for its use for this thesis will be presented.

[96] Mark Balnaves and Peter Caputi, *Introduction to Quantitative Research Methods: An Investigate Approach* (London: Sage, 2007).
[97] Julie Scott Jones and John E. Goldring, *Exploratory and Descriptive Statistics* (London: SAGE, 2022).

2.3 Limitations

The research takes into account a number of possible limitations. The following are the most notable:

1. **Availability of data:** there is no guarantee that all pertinent data will be accessible, usable, or even existing (this due to the topic being current).
2. **Biases in data:** the potential of prejudice in the secondary data.
3. **Generalisability:** the qualitative research has a relatively small sample size, which may reduce the applicability of the conclusion.
4. **Time constraints:** seeing that the topic is current and highly volatile, any data that is highly impactful that comes out after the writing cut-off date will not be taken into account.
5. **Language barriers:** Due to the emphasis of the research on China, the research can not limit itself to only using Western sources. Materials published in Chinese will be subjected to an automated translation for this research which might influence the analysis to a greater or lesser extent. Consequently, there might be a linguistic barrier that makes it difficult to comprehend and evaluate some sources.
6. **Coding scheme:** the use of a coding scheme helps guaranteeing consistency in the analysis of data. However, there is a chance that the assumptions of the coding scheme do not accurately reflect specific details of the data. Additionally, another limitation of deductive coding is that the research could potentially miss out on valuable insights as a result of the tight predetermined focus of the approach.
7. **Scope:** an evident limitation of the scope of the research is the primary focus on the perspective and aims of China in the RMB internationalization and the development of the e-CNY. Despite the fact that the research acknowledges the potential implications of the rise of the RMB as a reserve currency for the global financial system, it may not fully cover the perspective of other major player within the international financial system such as the EU. Moreover, the research does not go into detail about the potential impact of the e-CNY on the stability of the global financial system and any potential regulatory challenges. Lastly, the research focuses primarily on the external developments for China in regard to the topic and does not touch upon any internal developments. Therefore, the research may provide a more limited perspective on the complex issues, which surround the internationalization strategy of the RMB and the role of the e-CNY.

Figure 1. The methodological approach to the research

Research question: *Why is China so active in developing the status of the Yuan; consequently the e-CNY?*

Methodology:

• Objectives	• Examine the historical context and development of the currency policies and strategies of China, focusing on the RMB internationalization and development of the e-CNY. • Analyze the potential challenges of the role of the RMB as a reserve currency in reducing the dependency of China on the USD, including that could potentially influence its failure or success. • Research the limitations and advantages of the e-CNY in regard to the efforts of China in reducing their dependence on the USD and enhance its global geopolitical and economic influence. • Assess the impact of the currency policy and strategy of China on the USD dominance and global financial system.
• Research design	• Mixed methods approach. • Deductive strategy.
• Choice of Theory	• International Political Economy (IPE), Structural Realism, Rise and Fall theory.
• Choice of data	• Secondary data. • Extracted from both Western and Chinese (limited) sources. • Official publications, press conferences, news articles, research papers, reports and supporting literature.
• Choice of Analysis	• Qualitative and quantitative analysis. • Deductive content analysis and descriptive qualitative analysis.
• Limitations	• Availability of data. • Biases in data. • Generalisability. • Time constraints. • Language barriers. • Coding scheme. • Scope.

3. Theory

The theory chapter of the research aims to provide a theoretical framework for understanding the RMB internationalization strategy of China and its role as a reserve currency. Within the chapter, the following theories will be discussed: IPE, Realism, and Rise and Fall Theory. The chapter will form the basis of how these theories can be applied to the research of the currency strategy of China and how they can aid in understanding the challenges and potential of the role of the RMB as a major or global reserve currency. The chapter will be divided into three sub chapters, each with a focus on one of the theories mentioned above. The first sub chapter will introduce the theory of IPE and outline its relevance to the research of the currency strategy of China. It will discuss key concepts within IPE, such as institutions, power, and interest, and how they relate to dynamics within the global financial system. Moreover, a justification will be given on how IPE can help the research into understanding the motivations of China behind the RMB internationalization strategy. The second section will have a focus on the theory of Structural Realism. Key aspects such as supremacy of the state, self-help, and power maximization, and how they relate to the pursuit of China to internationalize the RMB, will be discussed. Additionally, the research will highlight on how Structural Realism can be used to understand the challenges and potential of the role of the RMB as a major or global reserve currency in reducing the dependence of China on the USD. The last chapter will introduce the Rise and Fall theory and aims to explain how it can be employed to analyze the currency strategy of China. The chapter will discuss some of the key concepts of this theory such as, power transitions, decline and hegemony, and what their connection is to the long-term political and economic goals of China. Furthermore, the chapter will explore how the Rise and Fall Theory can help the research in understanding and interpreting the potential implications of the rise of the RMB as a major or global reserve currency for the dominance of the USD and the global financial system.

3.1 International Political Economy

The theory of International Political Economy (IPE) encompasses a multidisciplinary field of research that explores, on a global scale, the relationships between politics and economics. IPE concerns itself with the actors within the global economy such as markets and states, and how their behavior is formed or influenced by social norms, economic policies, and political institutions. The theory of IPE is highly relevant when it comes to the research of the currency strategy of China. This seeing that it provides a framework that can be used to analyze the complex interactions between the political and economic factors of the international arena.[98]

One of the before mentioned key concepts of IPE is institutions. Institutions are the formal and informal rules through which economic behavior in a society is governed. Regulations, laws, organizations, and norms that influence economic activity can be included in what constitutes "institutions." Institutions are an integral part of functioning markets, seeing that they provide the social and legal framework that enables economic exchange. With reference to the currency strategy of China, it is important to understand the role of institutions. This seeing that China will need to build new institutional arrangements that are supportive of the RMB internationalization. Another key concept within IPE is power. This refers to the ability of actors to assert influence over others in a particular way. Power can be exercised in various ways. For example through military, economic, or political means and can establish itself in different ways, including influence, coercion, or persuasion. A central theme within the research of IPE is the distribution of powers between actors within the global economy seeing that it is critical to determining economic outcomes. In regard to the currency strategy of China, it is essential to be able to understand the distribution of power between actors within the international monetary system (IMS hereafter). This is because China aims to increase its political and economic influence within the global economy. The last key concept of IPE that is relevant for this research is interests. Interests refers to the aims and objectives of actors within the global economy. Factors that can influence interest include social, political and economic considerations. It is crucial to understand the interests of the various actors within the IMS in order to understand global economic dynamics. In the context of the currency strategy of China, being able to understand the interests of China and other actors within the IMS is of great importance in order to interpret the motivations of China behind the internationalization strategy of the RMB.[99]

3.2 Structural Realism

The theory of realism puts an emphasis on the importance of a state as a key actor within international politics. Structural realism mainly concerns itself with the supremacy of the state, self-help and the pursuit of power as the main concepts of international politics. Realism describes international politics as a constant struggle for security and power, in

[98] Thomas Oatley, "International Political Economy," in *International Political Economy: Interests and Institutions in the Global Economy* (London: Routledge, 2016), pp. 1-20.
[99] Ibid.

which states pursue their own interests through a system of self-help. With reference to the currency strategy of China, realism can give insights into the motives of China in pursuing the internationalization of the RMB. Realism is of the opinion that states pursue security and power. Consequently, the RMB internationalization strategy of China could be seen as a means to enhance its geopolitical and economic power. Realism can also provide a useful lens through which to understand the challenges and potential of the role of the RMB as a major or global reserve currency in reducing the dependence of China on the USD. It is argued by realism that the main characteristic of the global financial system is a power struggle between states, in which the dominant state seeks to maintain its control and power over the system. Accordingly, the potential of the RMB to reduce the dependence of China on the USD is dependent on the ability of China to challenge the USD dominance within the global financial system. Additionally, realism maintains that states operate within a system of self-help. States act on their own interests in order to maximize their security and power within this system.[100] In the context of the currency strategy of China, the RMB internationalization strategy can be interpreted as a way for China to reduce its dependency on the global financial system that is dominated by the USD, and by that pursuing an increase in its geopolitical and economic power.

3.3 Rise and Fall Theory

The rise and fall theory is a widely used framework that is based on the idea that the world, and therefore the political and economic arena, consists out of various power centers that cyclically rise and fall. The theory argues that dominant powers within the international system inevitably experience decline, and that rising powers are opportunistic as well as aspiring to replace these powers. The rise and fall theory has been applied to many historical cases, most notably on the case of the decline of the British Empire and the rise of the US as a superpower.[101] In the case of the currency strategy of China, the theory can be used to examine the long-term goals of China and the alignment of this strategy with its goals. Seeing that China has become the second-largest economy in the world, it indisputably challenges the dominance of the USD over the global financial system. The efforts of China to promote the RMB internationalization could be viewed as a part of a larger scale strategy of China to

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[100] John J. Mearsheimer, "Structural Realism," in *International Relations Theories: Discipline and Diversity*, 4th ed. (Oxford : Oxford University Press, 2016), pp. 51-67.
[101] Mancur Olson, *The Rise and Decline of Nations: Economic Growth, Stagflation, and Social Rigidities* (New Haven: Yale University Press, 1992).

increase its global influence and reduce its dependence on the USD. The rise of the RMB as a major or global reserve currency could potentially bring significant implications for the dominance of the USD over the global financial system. The rise and fall theory can be used to determine what these potential outcomes might be. One of the key concepts of this theory is power transitions. A power transition occurs when the global system experiences a shift in the distribution of power. This shift results in the change in the hierarchy of power among states.[102] This is a relevant aspect towards the research seeing that China is an emerging rising power within the global financial system, a development that challenges the dominance of the US over the IMS. Through the rise and fall theory it could therefore be argued that a power transition between the US and China is inevitable. Moreover, the decline and hegemony concept of the rise and fall theory refers to the decline of the current hegemon,[103] which is the US, and the emergence of a new one, which could potentially be China.

4. Historical Context

In order to fully grasp the complexity of the issues relating the research question, a historical context needs to be given around how the US gained dominance over the global financial system. The rise and fall theory can be applied over a large period of 500 years through which it identifies large cycles consisting out of three phases: the rise, top, and decline. Successful new orders that rise, display three typical behaviors. Firstly, they aim to gain more power by enlarging their support base.[104] Secondly, they consolidate power by converting weakening or eliminating any adversaries.[105] Lastly, they establish new systems and institutions.[106]

During the rise phase, leaders of a country have to establish a system through which they can raise the wealth and power of a country.[107] If successful, this system enables a population to unite behind a common purpose and high work output. Because of this, a country increasingly shifts from a basic form of production to a stage of general innovation, including the technological sector. Empires that became leading tend to display a behavior of enhancing their thinking through influence and learning of a current dominant power. This

[102] Ibid.
[103] Ibid.
[104] Paul Kennedy, *The Rise and Fall of the Great Powers: Economic Change and Military Conflict from 1500 to 2000* (New York: Random House, 1988).
[105] John Hobson, *The Sociology of Imperialism* (New York: James Pott & Company, 1902).
[106] John Kenneth Galbraith, *Anatomy of Power* (London: Hamish Hamilton, 1984).
[107] Kennedy, *The Rise and Fall of the Great Powers: Economic Change and Military Conflict from 1500 to 2000.*

openness towards knowledge[108] results in the population of a country to become more productive and competitive on the world market. This is evident in the growth in economic output and growing share of world trade.[109] This phenomenon can be seen when comparing the US and China when it comes to their shares of world trade and economic outputs. When countries engage in more global trade, they need to protect their trade routes and foreign interest from the competition; this is when great military strength is developed. If done correctly, this virtuous cycle leads to a strong growth of income, which can be used for all aspects of the development of a country. In all historical cases, empires that were the most successful used a capitalist approach in order to stimulate entrepreneurship across all sectors.[110] Even China, which is led by the Chinese Communist Party, used a form of capitalist approach.[111]

A natural consequence of great powers is the development and establishment of leading global financial centers in order to attract and distribute global capital. For example, New York is currently the financial heart of the world, and China is currently developing their own financial centers at a fast rate.[112] Another thing that can be observed within these cyclical periods of rise and fall is the interplay between capitalism (in any form), government and military operations. When the US rose as the global superpower the establishment of the US military industrial complex followed suit,[113] similarly to the Chinese system today.[114]

When a country becomes the largest international trading empire, its currency becomes the preferred medium of exchange and store hold of wealth, and thus the global reserve currency. Before the dominance of the USD, the British Empire imposed an international financial system with the GBP functioning as the global reserve currency. This seeing that historically the global reserve currency was controlled by the dominant power of the time. The GBP being the world reserve currency conferred huge privileges to the British

[108] Karl Raimund Popper, *The Open Society and Its Enemies* (London: Routledge, 2008).

[109] Adam Smith, *The Wealth of Nations* (New York: American Home Library Co., 1902).

[110] Max Weber, Talcott Parsons, and R. H. Tawney, *The Protestant Ethic and the Spirit of Capitalism: The Complete Text: Inclusive of Notes* (Pantianos Classics, 2022).

[111] Capitalism with Chinese characteristics is characterized by a market economy built on particularistic relationships, an opportunistic state, and a culturally self-sustaining society that embodies a strong pragmatic tradition; Loren Brandt, Thomas G. Rawski, and Debin Ma, *China's Great Economic Transformation* (Cambridge: Cambridge University Press, 2011).

[112] Mike Wardle and Michael Mainelli, "The Global Financial Centres Index 33" (London & Shenzhen, March 2023).

[113] Robert J. Gordon, in *The Rise and Fall of American Growth: The U.S. Standard of Living since the Civil War* (Princeton, NJ: Princeton University Press, 2016), pp. 621-679.

[114] Ho-fung Hung, *The China Boom: Why China Will Not Rule the World* (New York: Columbia University Press, 2017).

but this changed during World War II.[115] During the second World War, Britain had to release most of its colonies seeing that it had to dedicate all of its resources in order to participate in the war. Britain, and basically any country that participated in World War II, experienced a serious setback due to large scale destruction. However, despite its participation in the war, the US emerged from the war intact.[116] The US mainland was never attacked and the US spent the majority of the war building up its industrial capacity.[117] Moreover, it rose as the sole capitalist superpower.[118] The US used the wartime crisis to create a new world financial system in the form of the Bretton Woods Agreement.[119] The agreement stipulated that the USD would be the new global reserve currency, which presented the US with tremendous financial power.[120] From that moment on seeing that every nation needed USD for international transactions. At that time the value of the USD was pegged to a gold price of 35 USD per ounce. This was, theoretically, a preventative measure for the US against money printing because the US needed to keep enough gold reserves in order to honor the exchange rate.[121]

Controlling the global reserve currency presents a huge advantage as it enables a country to borrow more money in comparison to others. Global actors are keen to have reserves of the global reserve currency and hence lend back their currency to the controlling actor. In addition, when the controller runs out of its own currency, such as the US in 1971, they can always print more. The theory of the gold standard for the USD instilled trust in the value of the currency, hence how it kept its status.[122] In reality however, the US did not honor the agreement and it became clear in the 1960s that the US was printing extensively more USD than it had reserved in gold. The fact numerous nations accept as principle a USD value in gold lead the Americans to get into debts for free at the expense of other countries. This seeing that what the US owed them was paid, at least partially, with USD, something which

[115] Barry Eichengreen, *Exorbitant Privilege: The Rise and Fall of the Dollar and the Future of the International Monetary System* (Oxford: Oxford University Press, 2012), pp. 7-13.

[116] Joshua Freeman, *American Empire: The Rise of a Global Power, the Democratic Revolution at Home, 1945-2000* (New York: Penguin Books, 2013), pp. 3-6.

[117] Kennedy, *The Rise and Fall of the Great Powers: Economic Change and Military Conflict from 1500 to 2000*, pp. 47-48.

[118] Kennedy, *The Rise and Fall of the Great Powers: Economic Change and Military Conflict from 1500 to 2000*, pp. 357-372.

[119] S. N. Broadberry and Kevin H. O'Rourke, eds., *The Cambridge Economic History of Modern Europe* (New York: Cambridge University Press, 2011), pp. 174-178.

[120] Stanley L. Engerman and Robert E. Gallman , eds., *The Cambridge Economic History of the United States* (Cambridge: Cambridge University Press, 2000), pp. 745-747.

[121] Larry Neal and Jeffrey G. Williamson, eds., *The Cambridge History of Capitalism* (Cambridge: Cambridge University Press, 2015), pp. 227-230.

[122] Benjamin J. Cohen, *The Future of Money* (Princeton, N.J: Princeton University Press, 2006), pp. 72-77, 84-85, 97-101.

only the US is allowed to print. Countries started to demand their gold back when the US entered an inflationary crisis.[123] In reaction to this, the Nixon Administration suspendeforeign the convertibility of the dollar into gold in 1971. The US kept their gold reserves and left the rest of the world with USD and beholden to the USD.[124]

Another key aspect in the top part of the US cycle is something called the petrodollar. In 1973, a secret deal was negotiated between the US and the Saudi monarchy: Saudi Arabia would only sell its oil in USD, or petrodollar, in exchange for military protection from the US.[125] The USD became essentially a prerequisite for international trade, seeing that oil is the most traded commodity in the world.[126] This was a highly beneficial deal for the US, seeing that it only costs a few cents for the country to produce a hundred USD bill, but other countries have to put up a hundred USD worth of goods and services in order to obtain one. Another aspect of this is the fact that the entirety of the global financial system is based around institutions, such as the IMF and World Bank, created by the US.[127] Consequently, these institutions are essentially an extension of the strategic interests of the US.[128]

The exorbitant privilege bestowed on a country by controlling the global reserve currency leads to an increase in borrowing and marks the start of a financial bubble.[129] This cycle of cause and effect relationships, leading to interconnected and mutually supportive military, political and financial power, endorsed by the borrowing power of a global reserve currency, have been observed continuously throughout history.[130] All great powers in the world followed this path to the top. During the top phase, the strengths of the great power are sustained. Consequently, the population of these rich and powerful countries earn more, which makes them gradually more expensive and less competitive compared to people in other countries. Simultaneously, other countries naturally copy the methods and technologies of the leading power, which adds further to the reduction of competitiveness of the leading

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[123] Eichengreen, *Exorbitant Privilege: The Rise and Fall of the Dollar and the Future of the International Monetary System*, pp. 67-69, 74-75, 78-80, 87-89, 94-97, 103-105.
[124] Eswar S. Prasad, *The Dollar Trap: How the U.S. Dollar Tightened Its Grip on Global Finance* (Princeton: Princeton University Press, 2015), pp. 25-30, 41-46, 94-96.
[125] Daniel Yergin, *The Prize: The Epic Quest for Oil, Money & Power* (New York, NY: Free Press, 2009), pp. 674-675.
[126] Michael Hudson, *Super Imperialism: The Origin and Fundamentals of U.S. World Dominance* (London: Pluto Press, 2003), pp. 169-170, 175-176.
[127] William Engdahl, *A Century of War: Anglo-American Oil Politics and the New World Order* (Palm Desert, CA: Progressive Press, 2012), pp. 52-54, 65-66.
[128] Cohen, *The Future of Money*, pp. 80-83, 96-98.
[129] Charles Poor Kindleberger and Robert Z. Aliber, *Manias, Panics, and Crashes: A History of Financial Crises* (Hoboken, NJ: Wiley, 2009), pp. 5-8, 14-19, 66-72.
[130] Niall Ferguson, *The Ascent of Money: A Financial History of the World* (New York, NY: Penguin Books, 2018), pp. 177-185; William Bonner and Addison Wiggin, *Empire of Debt: The Rise of an Epic Financial Crisis* (Hoboken, NJ: Wiley, 2006).

power.[131] This can also be observed in relation to the US and China, more specifically as an advantage of China over the US. Chinese people have learned from the US through study and work, and take this knowledge back to China and apply what they have learned within the country. As a result of this China is becoming increasingly more competitive in comparison to the US.[132] Moreover, the US has generally not displayed a mindset of enhancing their thinking by studying other nations, something that will gradually make them less competitive on the global market.[133]

Controlling the global reserve currency inevitably leads to excessive borrowing and contributes to large debts with foreign lenders for the controlling actor.[134] Despite the fact that this boosts short-term spending power, it weakens the financial health and currency over the long-term. More concisely, when there is a strong mentality of spending and borrowing, a nation appears to be strong, however its finances are actually being weakened. Borrowing sustains the power of a country beyond its fundamentals through financing both domestic over consumptions and international military conflicts. Inescapably, the cost of maintaining and defending becomes greater than the generated revenue, and therefore becomes unprofitable.[135] For example, since September 11th, the US has spent over eight trillion USD on foreign wars and their consequences, and trillions more to fund other military operations and the keep up the support for military bases in 70 countries. Yet, it is still not spending enough to support military competition with China in the greater China area.[136] This cycle stipulates that richer countries eventually burry themselves into debt[137] by borrowing from less influential countries that tend to save more, and it is one of the early signs of a shift in power and wealth.[138] This shift started when the US had a per capita income of 40 times that of China during the 1980s. This is the time that China essentially started to buy US debt in the form of treasury bonds,[139] seeing that China wanted to keep reserves in USD given its

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[131] Kennedy, *The Rise and Fall of the Great Powers: Economic Change and Military Conflict from 1500 to 2000*, pp. 213-251.
[132] 1. Joseph S. Nye, *The Future of Power* (New York: PublicAffairs, 2012), pp. 1-22, 165-185.
[133] Ha-Joon Chang, *Kicking Away the Ladder: Development Strategy in Historical Perspective* (London: Anthem, 2007), pp. 52-60.
[134] Kindleberger and Aliber, *Manias, Panics, and Crashes: A History of Financial Crises*, pp. 29-30.
[135] Kennedy, *The Rise and Fall of the Great Powers: Economic Change and Military Conflict from 1500 to 2000*, pp. 207-243;
[136] Daniel W. Drezner, "Military Primacy Doesn't Pay (Nearly As Much As You Think)," *International Security* 38, no. 1 (2013): pp. 52-79, https://www.jstor.org/stable/24480569.
[137] Micheal Pettis, "How Does Excessive Debt Hurt an Economy? ," Carnergie Endowment for International Peace , February 8, 2022, https://carnegieendowment.org/chinafinancialmarkets/86397.
[138] Matt Pottinger and Daleep Singh, "Great Powers Don't Default," Foreign Affairs, April 27, 2023, https://www.foreignaffairs.com/united-states/great-powers-dont-default.
[139] Aliber Z. Robert, "The Global Savings Tsunamies," *The Wilson Quarterly (1976-)* 33, no. 3 (2009): pp. 56-58, http://www.jstor.org/stable/40261862.

status as global reserve and due to increase in international trade of China by opening up the economy.[140] When a major power starts to run out of new lenders, actors that have their currency in reserve begin to look for alternatives and to sell, rather than to buy, lend, save, and get in. Because of this the strength of the controller starts to decline.[141]

A stage of decline is initiated through internal economic weakness combined with internal challenges, external challenges such as war (in whichever sector), or both. When debts become unmanageable and economic downturn instigates, a country can no longer borrow or acquire enough financial resources to repay its debts; a financial bubble bursts.[142] This creates major domestic hardships and forces a country to choose between defaulting on its debts or printing more of its currency,[143] resulting in currency devaluation and a spiking inflation.[144] In the context of the research, this can be observed in the three cycles of debt, booms and busts of the US since the nineties in which the central bank had to de-escalate the situation, through harsher measures each time.[145]

Since there is no concrete system to resolve international disputes, may they be economically, politically, or military, these conflicts are generally resolved through tests of power and influence.[146] As a major power is confronted with greater challenges, competition and threats, it is faced with the complex choice of fighting or retreating.[147] Fighting and losing constitutes the worst outcome. However, retreating also carries a significant negative signal towards allies, or countries that side with a power out of strategic interests, that the dominant power is weak; it cedes progress to any adversaries.[148] When the economic conditions of a country are in bad shape, this usually leads to a fight for more wealth and

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[140] "Is It a Risk for America That China Holds over $1 Trillion in U.S. Debt?," Carnegie Endowment for International Peace, February 2, 2016, https://www.csis.org/analysis/it-risk-america-china-holds-over-1-trillion-us-debt.

[141] David Hume, *Essays, Moral, Political, and Literary*, ed. Tom L. Beauchamp (Oxford: Clarendon Press, 2021), pp. 386-387; Mervyn A. King, *The End of Alchemy: Money, Banking, and the Future of the Global Economy* (New York: W.W. Norton & Company, 2017).

[142] Kindleberger and Aliber, *Manias, Panics, and Crashes: A History of Financial Crises*, pp. 29-30; Ferguson, *The Ascent of Money: A Financial History of the World,* pp. 315-316;

[143] Kennedy, *The Rise and Fall of the Great Powers: Economic Change and Military Conflict from 1500 to 2000*, pp. 70-72.

[144] King, *The End of Alchemy: Money, Banking, and the Future of the Global Economy*, pp. 181-184; Carmen M. Reinhart and Kenneth S. Rogoff, *This Time Is Different Eight Centuries of Financial Folly* (Princeton u.a.: Princeton University Press, 2011), pp. 86-95.

[145] Michael Lewis, *The Big Short: Inside the Doomsday Machine* (London ; New York: Norton & Company, 2011), pp. 5-23, 97-116; Alan Greenspan, *The Age of Turbulence: Adventures in a New World* (New York: Penguin Books, 2008), pp. 201-235, 353-394.

[146] Kennedy, *The Rise and Fall of the Great Powers: Economic Change and Military Conflict from 1500 to 2000*; John J. Mearsheimer, *The Tragedy of Great Power Politics* (New York: W. W. Norton & Company, 2014), p. 4.

[147] Mearsheimer, *The Tragedy of Great Power Politics*, pp. 109-144, 185-208.

[148] Robert O. Keohane and Joseph S. Nye, *Power and Interdependence* (Glenview, IL: Pearson, 2012), pp. 133-159, 189-214.

power, this in the form of an actual war or even trade war; any type of war is extremely costly.[149] Simultaneously, wars are the catalyst of tectonic shifts that establish the realignment of new orders in accordance to the new distribution of wealth and power in the world.[150] The moment that actors that are holding the global reserve currency of the declining power lose faith and sell off their reserves, marks the end of the reoccurring cycles of the rise, the top, and the decline.[151]

Currently the US has not yet reached this point, despite that it has massive debts, spends more than it gains, and funds its deficit with more borrowing and printing large amounts of new money, the major run on USD sell-offs has not yet started. Even though there are sizeable internal and external conflicts occurring for all the classic reasons, they have not escalated to the point of full-blown wars. Resulting out of these conflicts disregarding their violent or non-violent nature, emerge new winners that group together and restructure the debt and political systems of the loser, to ultimately establish a new world order.

5. RMB Internationalization: Not a New Phenomenon

For the context of the research it is important to note that the internationalization of the RMB and the potential of the RMB to emerge as a major reserve currency are related but not equivalent. The aim of RMB internationalization is to increase the usage of RMB in international trade and financial transactions. Whereas the possible emergence of the RMB as a major reserve currency calls for RMB-denominated financial assets being widely and heavily held in the FX reserves of central banks. The efforts of China to internationalize the RMB is not a new phenomenon. As early as 1993, China aimed to "achieve full currency convertibility by the end of the century." China started to gradually remove capital account restrictions and established current account convertibility in 1996. In the aftermath of the 1997 Asian financial crisis, China dropped its full-convertibility target and resulted in a

[149] Kennedy, *The Rise and Fall of the Great Powers: Economic Change and Military Conflict from 1500 to 2000.*
[150] Zbigniew Brzezinski, *The Grand Chessboard: American Primacy and Its Geostrategic Imperatives* (New York: Basic Books , 1997).
[151] Linda S. Goldberg, "The International Role of the Dollar: Does It Matter If This Changes?," *SSRN Electronic Journal*, no. 522 (October 1, 2011), https://doi.org/10.2139/ssrn.1945339.

halting drive to internationalize the RMB.[152] That said, the 2001 accession of China to the WTO, helped to establish a favorable environment for RMB internationalization.[153]

The long-term strategy of China to internationalize RMB intensified the global financial crisis of 2008, when the dominance of the USD over the global financial system and its role as the global reserve currency where, once again, called into question. China emerged as a new trading superpower in 2009, having become the largest exporter and second largest importer in the world.[154] Exuberant surges in the GDP, FX reserves, trade, import, and export of China between 2001 and 2009 can be observed.[155] As history suggests the strength of the currency of a nation is largely based[156] on the strength of the economy of that nation.[157] This is therefore related to the potential of a currency to be become a reserve currency. Along the same line, the export criteria that must be "large relative to others, which makes it important to trading partners," is part of the methodology of the IMF in determining currencies that qualify to be drafted into the IMF reserve currency basket.[158] Indeed, the 2008-2009 global financial crisis presented new challenges and opportunities for the Chinese leadership in terms of RMB internationalization.[159] 2016, the moment that the RMB was included in the reserve currency basket of the IMF, was "an important milestone in the integration of the Chinese economy into the global financial system."[160] As with other policies, the Chinese government has pursued RMB internationalization in a methodical, cautious, and gradual manner. The Chinese government is "working towards multiple objectives" because the RMB's internalization is "tied up with many complex domestic and geopolitical considerations."[161]

[152] Pieter Bottelier and Uri Dadush, "The Future of the Renminbi as an International Currency," Carnegie Endowment for International Peace , June 2, 2011, https://carnegieendowment.org/2011/06/02/future-of-renminbi-as-international-currency-pub-44338.
[153] Hyo Sung Park, "China's RMB Internationalization Strategy: Its Rationales, State of Play, Prospects and Implications ," *M-RCBG Associate Working Paper Series* 63 (August 2016): pp. 1-187.
[154] *China and the World Trade Organization*, 1st ed. (Beijing: The State Council Information Office of the People's Republic of China, 2018), pp. 15-20.
[155] Graham Boden, "China's Accession to the WTO: Economic Benefits," *The Park Place Economist* 20, no. 1 (2012): pp. 13-17; "World Development Online Indicators," World Bank, May 4, 2023, https://databank.worldbank.org/source/world-development-indicators.
[156] Manur and Ramachandra, "Does a Strong Currency Mean a Strong Economy?,"
[157] Perot and Simon, *The Dollar Crisis: A Blueprint to Help Rebuild the American Dream*.
[158] "What Is the SDR?," IMF, January 5, 2023, https://www.imf.org/en/About/Factsheets/Sheets/2023/special-drawing-rights-sdr.
[159] Barry Eichengreen and Masahiro Kawai, *Renminbi Internationalization: Achievements, Prospects, and Challenges* (Washington, DC: Brookings Institution Press, 2015), pp. 1-33.
[160] "Press Release: IMF's Executive Board Completes Review of SDR Basket, Includes Chinese Renminbi," IMF, November 30, 2015, https://www.imf.org/en/News/Articles/2015/09/14/01/49/pr15540.
[161] Edward S. Prasad, "China's Efforts To Expand The International Use Of The Renminbi," Report prepared for the U.S.-China and Security Review Commission, February 4, 2016, p. 98.

5.2 Motivation behind the RMB Internationalization

The efforts of China to internationalize their currency have been unprecedented. This because China is the first emerging country that was added to the IMF reserve currency basket, this in contrast with other countries that had been fully developed before they started to internationalize their currency. Historical cases show that convertibility and opening of a capital account always came after the international use of a currency, which has not been the case with China.[162] It is unusual, seeing that it defies the logic of classic economics, which prescribe that the internationalization of a currency can only take place when it has acquired a fully market based exchange rate formation regime, a liberalized capital account, and an unregulated interest rate.[163] In this context, it was another challenge for China that there was no road map to guide the process of internationalization. Moreover, the Chinese leadership, while being unguided in this process, was pursuing two seemingly conflicting objectives which were simultaneously at stake: China sought to expand the international usage of the RMB while retaining a progressive approach to capital account convertibility through the gradual liberalization of long-term flows and the protection of China's most vulnerable domestic industries.[164]

Something that is worth noting is that the unique internationalization approach of China has resulted in a system of "one currency, two markets" – one offshore, one onshore – with a firewall between the two markets,[165] allowing full convertibility in the offshore market and limited convertibility in the onshore market.[166] Arguments have been made that the unique internationalization strategy of China is actually advocative of China not wanting to internationalize the RMB, or at least not within the current liberalist IMS, or on the short run. This seeing that a full internationalization of the RMB would require China to remove

[162] Paola Subacchi, "One Currency, Two Systems: China's Renminbi Strategy," Chatham House, *International Economics,* October 2010, IE BP 2010/01, pp. 2-4.
[163] Alex He, "Domestic Sources and RMB Internationalization: A Unique Journey to a Major Global Currency," *GIGI Papers* No. 67, May 2015, p. 3.
[164] Subacchi, "One Currency, Two Systems: China's Renminbi Strategy, pp. 4-5.
[165] Edwin L.-C. Lai, *One Currency, Two Markets: China's Attempt to Internationalize the Renminbi* (Cambridge, United Kingdom: Cambridge University Press, 2021).
[166] Chinese officials eased limitations on RMB trade settlements between mainland China and Hong Kong in 2009; this was first time RMB settlements were permitted outside of mainland China. The CNH was created to mark this, with the 'H' standing for Hong Kong (RMB having the international ticker CNY). As China steadily internationalized the RMB, these laws have been gradually lifted, resulting in the growth of RMB markets in Hong Kong and other offshore RMB markets such as Australia, the United States, Singapore, and the United Kingdom. These exist alongside the RMB onshore market in mainland China, where restrictions on buying and selling still apply. As a result, the RMB market is currently divided into two parts: offshore and onshore (CNY and CNH); Yin-Wong Cheung, "The Role of Offshore Financial Centers in the Process of Renminbi Internationalization," *SSRN Electronic Journal*, no. 427 (April 8, 2014): pp. 1-30, https://doi.org/10.2139/ssrn.2421043.

restrictions on capital account transactions. This would make it, if not impossible, highly difficult, for China to manage the RMB exchange rate and/or manage an autonomous monetary policy. Domestic financial market reform through liberalization, long fought by politically strong state-owned banks and enterprises, is a requirement for complete RMB internationalization. To overcome domestic financial sector liberalization opposition, the "one currency, two markets" policy was implemented. This can be seen as a tactic for applying pressure in the opposite direction (known as daobi /倒逼).[167] At the time of writing, the domestic financial market liberalization is far from complete, and will continue to be a significant obstacle towards the goal of China to internationalize the RMB for some time. There are several motivations behind the efforts of China to internationalize the RMB. These can be generalized into the following key aspect areas: trade facilitation, combatting inflation, getting out of the "dollar trap," reforming the IMS, and geostrategic interests.

5.2.1 Trade Facilitation

The internationalization of the RMB would be one of the most effective ways through which China can promote trade and therefore also extend its sphere of influence. As mentioned before, one of the main factors that attributed to the meteoric rise of China as a trading superpower is the accession of China to the WTO in 2001. This trend has further accelerated, despite turmoil, deep into 2023.[168] At the core of the trade facilitation motivation lies the manufacturing power of China. China currently accounts for roughly 30% of the global manufacturing output.[169] Because of its enormous network of factories, which are generally driven by inexpensive labor, China is able to create items at cheaper rates than many other nations, making it a favorite destination for outsourcing and offshoring. This has enabled Western corporations to use the industrial capabilities of China, resulting in the establishment of global supply networks spanning many continents.[170] It especially makes sense, within the context of the trade pattern of China, to promote the use of the RMB in international transactions. This seeing that the processing of trade accounts for about half of its GDP. A

[167] Lai, *One Currency, Two Markets: China's Attempt to Internationalize the Renminbi.*
[168] Junaid Haleem, "The Rise of China as a Global Economic Superpower and Its Impact on International Trade," Modern Diplomacy, March 5, 2023, https://moderndiplomacy.eu/2023/03/06/the-rise-of-china-as-a-global-economic-superpower-and-its-impact-on-international-trade/.
[169] "China accounts for 30% of global manufacturing output: Official," The State Council Information Office of The People's Republic of China, June 12, 2022, http://english.scio.gov.cn/pressroom/2022-06/14/content_78269516.htm; *World Manufacturing Production: Decelerating growth, growing concerns, Quarterly Report, Q4 2022,* Vienna: United Nations Industrial Development Organization, 2023; "Manufacturing, value added (current US$) – China," The World Bank, 2023, https://data.worldbank.org/indicator/NV.IND.MANF.CD?locations=CN.
[170] Haleem, "The Rise of China as a Global Economic Superpower and Its Impact on International Trade."

large part of the global supply and manufacturing chain consists out of Chinese factories assembling parts and components that originate from other East-Asian countries, which are then exported to the West.[171] Consequently, it economically makes sense to invoice and settle this type of transactions in RMB rather than USD, as long as the trade involves transportation of items within the greater China area, rather than between them and the US.[172]

With this in mind, encouraging cross-border trade settlements in RMB was viewed as a practical way of enlarging the share of China in international trade through aiding Chinese ex- and importers in lowering transaction costs and minimizing FX rate risks associated with the use of USD.[173] Transactions in RMB also relieve these parties of the need to hedge exchange-rate risk, especially during periods of a highly volatile and fluctuating USD. Over the long-term, the RMB internationalization strategy allowed Chinese enterprises to increase their market share by making them more competitive in an increasingly competitive market. This type of benefits are also applicable to foreign enterprises that have trade deals with China. Similarly, these enterprises can reduce transactions costs and FX risks through using the RMB rather than the USD, which facilitates the use of RMB trade settlements when looking at the future.[174]

An important aspect to take notice of is the fact that more RMB settlements do not only encourage commerce, but will also assist the RMB internationalization strategy through providing a forward momentum. This seeing that if RMB-based commerce between China and its trading partners develops, so will the position of the RMB as a reference currency[175], leading to further development of the Yuan-bloc.[176] The Yuan bloc has the potential to

[171] "Global Firms Are Eyeing Asian Alternatives to Chinese Manufacturing," The Economist, February 20, 2023, https://www.economist.com/business/2023/02/20/global-firms-are-eyeing-asian-alternatives-to-chinese-manufacturing.

[172] Park, "China's RMB Internationalization Strategy: Its Rationales, State of Play, Prospects and Implications." p. 7.

[173] Yukon Huang and Clare Lynch, "Does Internationalizing the RMB Make Sense for China?" *Cato Journal*, 33, no. 3 (Fall 2013), pp. 573-574.

[174] Park, "China's RMB Internationalization Strategy: Its Rationales, State of Play, Prospects and Implications."

[175] A reference currency is used to benchmark the value of other currencies. This can be in the context of both financial and non-financial purposes such as pricing goods and services, setting exchange rates, or comparing economic indicators between different countries; Hwee Kwan Chow, "Is the Renminbi Asia's Dominant Reference Currency? A Reconsideration," *China Economic Policy Review* 03, no. 01 (2014): p. 1450002, https://doi.org/10.1142/s1793969014500022.

[176] The Yuan bloc refers to a group of countries which have adopted the RMB as anchor, reference, or reserve currency in international transactions. According to some analysts, the development of a Yuan bloc might lessen the reliance of nations on the USD as leading international currency and aid to expand the usage of the RMB in international transactions; Martin Kessler, *The Renminbi Bloc Is Here: Asia Downs, Rest of the World to Go?* Working Paper 12-19, Washington, DC: Peterson Institute For International Economics, 2012, p, 18.

expand beyond a regional barrier to a more global level, aiding the RMB in becoming a major global currency.[177]

5.2.2 Combatting Inflation, And Currently, Deflation

The strong economic growth of China resulted in rising inflationary pressures, which the Chinese government attempted to moderate through monetary policy. Between 2007 and 2013, China accounted for more than half of the broad-money[178] stock globally, making it the largest money-printing economy in the world. Moreover, the amount of broad money on the account of China increased threefold during 2008 and 2015.[179] Fiscal stimulus, a lending boom powered by state-owned banks, significant shadow banking, and expanding trade and current-account surpluses[180] all contributed to this liquidity expansion. The large inflow of FX in broad money resulted into an increase in money supply that was outside the control of the Chinese central bank.[181] Furthermore, the Chinese government became increasingly worried about the rising stocks of foreign reserves of China, owing to the fact that the reserves of China were primarily held in dollar-denominated assets, which were not considered by the Chinese government to be a safe haven anymore following the 2008 global financial crisis.[182] In addition, despite the US generally exporting their inflation to the rest of the world (spillover effect) by printing USD, observers have noticed that China, in a sense, facilitates this by opting to import inflation.[183] An additional observation along this line is the fact that the decision of the People's Bank of China (PBoC) to peg the RMB to the USD,[184] is

[177] Park, "China's RMB Internationalization Strategy: Its Rationales, State of Play, Prospects and Implications." p. 8.

[178] Broad money or M2 is a measure of the total amount of money that circulates within an economy. It is one of the most commonly used measures of money supply. Broad money is a key indicator of the overall health and liquidity of an economy and ought to be monitored closely when managing inflation and guarantee stability within a financial system; *Base money, broad money and the APP,* ECB Economic Bulletin 6, Brussels: European Central Bank, 2017, p. 62.

[179] "Broad money (% of GDP) – China," The World Bank, 2020: https://data.worldbank.org/indicator/FM.LBL.BMNY.GD.ZS?locations=CN.

[180] The exponential growth in the broad money of China was in large fueled by the purchase of USD from Chinese exporters by the Chinese central bank, because it resulted in the issuance of more RMB.

[181] Ruchir Sharma, "Why China Is Not Rising as a Financial Superpower," Financial Times, June 20, 2022, https://www.ft.com/content/68b48e96-ed0d-4620-8f89-4f3f5bb0c937; Gregory Chi-Chong Chow, *China as a Leader of the World Economy* (Singapore: World Scientific, 2012), p. 9.

[182] Wayne M. Morrison, "China's Economic Rise: History, Trends, Challenges, and Implications for the United States," *Current Politics and Economics of Northern and Western Asia* 28, no. 2/3 (2019): pp. 189-242, p. 192; Qiao Yu, "Relocating China's Foreign Reserves," Brookings, May 10, 2017, https://www.brookings.edu/research/relocating-chinas-foreign-reserves/.

[183] Jinyue Dong and Le Xia, *China | China's role in global inflation: stabilizer or contributor?* Madrid: BBVA Research, July 2022, p. 2.

[184] The RMB was pegged to the USD at a fixed exchange rate. This policy was meant to stabilize the RMB and encourage foreign investment. The peg lead to accusations, notably from the US, that China conducted currency manipulation in order to obtain an unfair advantage in international trade. Combined with these accusations,

essentially opting to transfer control of its domestic monetary policy to the US Federal Reserve.[185]

Under these circumstances, the PBoC sought to limit liquidity through sterilization and other contractionary monetary measures,[186] in order to control passive money supply.[187] The issue of liquidity was attempted to be controlled through a variety of measures, including, raising required reserve rations, open market operations, and non-market tools such as the transfer of deposits from the commercial banking system to the central bank and window guidance (moral suasion). Moreover, FX swaps with large commercial banks were established.[188] But sterilization has a cost: first, if the PBoC maintains sterilization to handle rising FX reserves, it will need to continue to issue more debt, which may cause a raise in interest rates of PBoC bills. Second, it will cause the RMB to appreciate against the USD, something that will not only lead to a net capital loss in local currency terms, because PBoC bills are denominated in RMB and FX reserves are denominated in USD, but will also impact the exports of China.[189] The US administration criticized China for its FX strategy in this regard.[190]

Taking all of this into account, it can be argued that the internationalization of the RMB can serve as a practical and effective instrument since it strives to build and boost demand for RMB-denominated assets available to overseas investors. This will assist to counter the domestic flood of RMB, through lowering the likelihood of inflation.[191] It is also worth mentioning that the large outside demand for USD-denominated assets has helped to

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China was pressed into allowing the RMB to float more freely in international currency markets. Chin revalued the RMB in 2005 and pegged it to a basket of currencies rather than just the USD. This enabled the RMB to gradually appreciate against the USD and other currencies, hereby easing worries about currency manipulation. Since 2005, the RMB has become increasingly more flexible, with the RMB exchange rate becoming more determined by market forces. The Chinese government does, however, retain some influence over the RMB through monetary policy and FX regulations; Daniel Mcdowell, "What Is Holding the Yuan Back? Xi Is.," Georgetown Journal of International Affairs (Georgetown University Walsh School of Foreign Service , February 9, 2022), https://gjia.georgetown.edu/2022/02/11/what-is-holding-the-yuan-back-xi-is/.

[185] Christopher Joseph Neely, "Chinese Foreign Exchange Reserves, Policy Choices, and the U.S. Economy," *Review* 99, no. 2 (January 2017): pp. 207-231, https://doi.org/10.20955/r.2017.207-231l; Ke Tang, Changyun Wang, and Shiyi Wang, "China's Imported Inflation and Global Commodity Prices," *Emerging Markets Finance and Trade* 50, no. 3 (2014): pp. 162-177, https://doi.org/10.2753/ree1540-496x500309;

[186] Chenying Zhang, "Sterilization in China: Effectiveness and Cost," *SSRN Electronic Journal*, November 13, 2010, pp. 1-57, https://doi.org/10.2139/ssrn.1708162, p. 11-14.

[187] The term "passive money supply" refers to the rise in the money supply of a country caused by an increase of FX reserves rather than domestic sources such as government expenditure and bank lending.

[188] Zhang, "Sterilization in China: Effectiveness and Cost."

[189] Ibid., p. 28.

[190] Andrea Shalal and Alexandra Alper, "U.S. Treasury Drops China Currency Manipulator Label Ahead of Trade Deal Signing," Reuters (Thomson Reuters, January 13, 2020), https://www.reuters.com/article/us-usa-trade-china-idUSKBN1ZC2FV.

[191] Yan Liang, "Rebalancing, Deleveraging and Sustaining Growth in China," *The Chinese Economy* 50, no. 6 (December 2, 2017): pp. 370-380, https://doi.org/10.1080/10971475.2017.1379934.

maintain the inflation of the US as low as possible, despite the practices of the Federal Reserve which inflate the USD massively.[192] RMB internationalization might potentially help China avoiding importing inflation.

On another note, RMB internationalization might also aid China with combatting deflation. As the majority of the world is battling high inflation rates in 2023, China is facing an atypical domestic deflation cycle. Domestic deflation poses a big issue for China. Deflation can limit consumer spending because consumers postpone purchases in the hope that prices will continue to decline. As a result of this, there can be a decrease in demand for products and services and decreased economic activity. Debt burdens can also be increased by deflation when the real worth of debt rises over time. Additionally, deflation can cause a downward spiral of price cuts when prices are further reduced to encourage demand, which eventually creates a downward spiral. Falling prices can make exports less competitive on the global market, which can be especially detrimental to an economy that relies on exports, such as China.[193] Largely the same factors of the RMB internationalization that aid China in combatting inflation may be applied to the deflation problem. First, by internationalizing the RMB, China can attract more international investment and strengthen its economy. This, can serve to boost domestic demand for goods and services, therefore offsetting deflation. Second, the internationalization of the RMB can aid China to reduce its dependency on exports as a source of economic development. This can assist to mitigate the negative impact of global economic crises on the Chinese economy and avoid domestic deflation. Lastly, by promoting the usage of RMB in international transactions and investment, China may limit how vulnerable it is to currency swings, of for example, the USD. This can help stabilizing the Chinese economy and prevent domestic deflation.[194]

5.2.3 Getting out the "Dollar Trap"

The purpose of the internationalization of the RMB is for the RMB to be used in international trade, lending investment and borrowing. This can reduce Chinese currency risk in financial

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[192] Patrick Baron, "Why It Matters If the Dollar Is the Reserve Currency: Patrick Barron," Mises Institute, March 6, 2015, https://mises.org/library/why-it-matters-if-dollar-reserve-currency.

[193] Kevin Yao, "Analysis: China's 'Atypical' Deflation Cycle Gives Central Bank a Headache," Reuters (Thomson Reuters, April 19, 2023), https://www.reuters.com/business/finance/chinas-atypical-deflation-cycle-gives-central-bank-headache-2023-04-19/; Thomas Hale, "While the World Fights Inflation, China's Problem Is Deflation," Financial Times, November 15, 2022, https://www.ft.com/content/b68a10bd-45fe-4bb1-8edc-e7c7fb441f83.

[194] Guo Kesha, "Avoiding the Impact of Deflation and Deflation Expectations on Economic Growth," *China Finance and Economic Review* 5, no. 1 (April 23, 2021): pp. 14-27, https://doi.org/https://doi.org/10.1515/cfer-2016-050103.

and trade operations, as well as the possibility of balance of payment problems in China induced by speculative attacks on the RMB. Developing countries such as China, which often cannot borrow in their own currency, are subject to such crises, or "original sin."[195] Using the RMB in international transactions is a critical step toward resolving the issue of the "original sin." Moreover it would present China with the opportunity to borrow significant sums of money from overseas at low interest rates in RMB, rather than USD. The USD is currently the leading invoicing, investment, and reserve currency under the present IMS. The current IMS is a very asymmetric system: most nations aim to maintain a steady exchange rate with the USD by engaging in the FX market, whilst the US is not concerned with the value of the USD in comparison to others. As a result the RMB was pegged to the USD for a certain amount of time, and it still closely tracks the USD today.[196] As a result of this pegging the PBoC amassed a massive quantity of USD assets.[197] Any significant decile of the USD could therefore result in massive losses for China. To avoid the aforementioned "dollar trap," China favors the use of a super sovereign currency as the global reserve currency, with the currencies of major economies, which includes the RMB, serving as constituent currencies, each weighted by its GDP share. China wants to eventually tie the currencies of its primary trading partners to the RMB, while the RMB is pegged to this super-sovereign reserve currency. Whether or not a super-sovereign will become reality, China wants the RMB to become a major reserve currency to foreign central banks. With the three cycles of financial crises in mind, and the US as inflation exporter on the main stage, now is a good time to push for RMB internationalization.[198] This mainly due to the risk of depreciation of the USD because of quantitative easing.[199] In addition to this, the Federal Reserve Bank balance sheet

[195] Barry Eichengreen, Ricardo Hausmann, and Ugo Panizza, "The Pain of Original Sin," *Other People's Money*, 2005, pp. 13-47, https://doi.org/10.7208/chicago/9780226194578.003.0002, pp. 13-16.
[196] Edwin L.-C Lai, *Renminbi Internationalization: The prospects of China's Yuan as the Next Global Currency,* Thought Leadership Brief 9, Hong Kong: The Hong Kong University of Science and Technology Institute For Emerging Market Studies, 2015, pp. 1-2.
[197] In 2023 China is the second largest holder of US treasury securities amounting to 859.4 billion USD. Despite it being the second largest holder, there has been a downward trend of Chinese holding of US bonds, with 2023 marking the lowest point in over 12 years. Observers note that China is likely shifting some of its reserves into alternative assets such as gold as an alternative to US treasuries. Indicative of this is the rise of 60% of the gold imports of China to a worth of 76.6 billion USD at the end of 2022: "Major foreign holders of United States treasury securities as of January 2023," Statista, March, 2023, https://www.statista.com/statistics/246420/major-foreign-holders-of-us-treasury-debt/; Yuta Saito and Iori Kawate, "China's U.S. Treasury Holdings Hit 12-Year Low on Rate Hikes, Tensions," Nikkei Asia, February 16, 2023, https://asia.nikkei.com/Business/Markets/Bonds/China-s-U.S.-Treasury-holdings-hit-12-year-low-on-rate-hikes-tensions.
[198] Lai, *Renminbi Internationalization: The prospects of China's Yuan as the Next Global Currency.*
[199] Quantitative easing or QE is a monetary policy strategy employed by central banks. A central bank uses QE to buy securities to lower interest rates, increase availability of money, and encourage greater lending. It serves as a tool to encourage economic activity and keep credit flowing amid a financial crisis; Anna-Louise Jackson

has been giving off mixed signals, seeing that its balance sheet increased by 300 billion USD in Q1 of 2023.[200] In relation to quantitate easing, quantitative tightening can also be observed.[201] This seeing that the Federal Reserve let 9 trillion USD worth of bonds mature without replacement.[202] Quantitative tightening is something analysist fear as it may push the US economy into a deep state of recession and/or destabilize its financial market, which in turn could trigger a global economic crisis.[203] These mixed signals are quite possibly an indicator of the relatively bad health or mismanagement of the US economy. Moreover, the USD appreciated over 12% in 2022, which market a 20-year high, but observers note that the trend has been weakening and might eventually turn into depreciation as a result of inflation.[204] Taking this into account, plus the fact that China is the largest supplier of goods imports of the US,[205] China ought to take notice of this, to prevent, rather than cure.

5.2.4 Reforming the IMS

As mentioned before, Chin has proposed the replacement of the USD as the global reserve currency by a super sovereign currency based on special drawing rights (SDR hereafter), a unit of account employed by the IMF. The goal of the proposal was to create a reserve currency "that is disconnected from individual nations."[206] Commenters noted that the idea of China, or a similar change to the IMS would be in the best interests of the US, while also

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and Benjamin Curry, "Quantitative Easing Explained," Forbes, March 18, 2023, https://www.forbes.com/advisor/investing/quantitative-easing-qe/.

[200] Daniel Dubrovsky, "US Dollar Gains as Fed Balance Sheet Swells, but It Is Not What You Think," DailyFX, March 16, 2023, https://www.dailyfx.com/news/us-dollar-gains-as-fed-balance-sheet-swells-but-it-is-not-what-you-think-20230316.html.

[201] Qualitative tightening or QT is a monetary policies that contract or reduce the balance sheet of a central bank. By employing QT a central bank shrinks its monetary reserves through either selling government bonds or letting them mature which removes them from the cash balance. QT is seen as a tool to remove liquidity from financial markets; Kristie M. Engemann, "What Is Quantitative Tightening?," Saint Louis Fed Eagle (Federal Reserve Bank of St. Louis, December 9, 2021), https://www.stlouisfed.org/open-vault/2019/july/what-is-quantitative-tightening.

[202] Graham Buck, "Limits Seen to RMB Internationalisation – Industry Roundup: 2 June," CTMfile, June 2, 2022, https://ctmfile.com/story/limits-seen-to-rmb-internationalisation-industry-roundup-second-june.

[203] Adrian Ma and Darian Woods, "Quantitative Easing, Meet Quantitative Tightening," NPR, May 4, 2022, https://www.npr.org/2022/05/04/1096752841/quantitative-easing-meet-quantitative-tightening; J. Scott Davis, "Don't Look to the 2013 Tantrum for the Effect of Tapering on Emerging Markets," Federal Reserve Bank of Dallas, August 10, 2021, https://www.dallasfed.org/research/economics/2021/0810.

[204] "Will a Strong US Dollar Return?: J.P. Morgan Research," J.P. Morgan , February 3, 2023, https://www.jpmorgan.com/insights/research/currency-volatility-dollar-strength.

[205] "The People's Republic of China," Office of the United States Trade Representative, 2023, https://ustr.gov/countries-regions/china-mongolia-taiwan/peoples-republic-china.

[206] Jamil Anderlini, "China Calls for New Reserve Currency," Financial Times, March 24, 2009, https://www.ft.com/content/7851925a-17a2-11de-8c9d-0000779fd2ac; Yexia Sun, "The Disadvantages of Sovereign Currency as the World Currency," *World Review of Political Economy* 13, no. 1 (2022): pp. 45-59, https://doi.org/10.13169/worlrevipoliecon.13.1.0045, pp. 45-51.

serving the interests of the rest of the world.[207] Moreover, it was also noted that the current system is not sufficient for any nation, including the US. It is inevitable that a new and more stable global reserve system will emerge from the current flawed one. This development would be beneficial to both the world in general and the US. It would result in a more stable global financial system and increase global economic development.[208] Seeing that the idea of China to reform the IMF is based on the expansion of the role of SDRs, it was vital for China to be included into the IMF reserve currency basket. This in turn would aid in expanding the role of the SDR and, ultimately, create an environment supportive to the reform of the IMS.[209] In this regard, it is not surprising why China is pushing for RMB internationalization.

In line with the aim of China to reform the IMS a very influential argument of former president of the World Bank, Robert Zoellick. Zoellick argued that influential groups of nations such as the G20 need to come up with a strategy for developing a cooperative monetary system that reflects the realities of emerging economies. A new system would very certainly require the USD, EUR, JPY, GBP, and RMB that is progressing toward internationalization and ultimately an open capital account. Gold should therefore be used as an international reference point for market expectations concerning deflation, inflation, and future currency values. Despite gold being viewed as 'old money' nowadays, markets currently use gold as an alternative monetary asset. That said, the world must look beyond the idea of a Bretton Woods II.[210] This is an especially interesting thought taking into account the current mixed signals that the Federal Reserve is giving out (signs of qualitative easing and qualitative tightening), could be a potentially harmful factor towards major exporting nations such as China, seeing that these practices ought to weaken the USD.[211] It is noteworthy to recognize the call of Zoellick for leading economies to adopt a modified global gold standard, which would be a guiding factor to currency rates.[212] In fact, Zoellick may have been trying to highlight the need of China to internationalize the RMB, rather than to establish an anchor

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[207] Anderlini, "China Calls for New Reserve Currency."; Fred C. Bergsten, "The Dollar and the Deficits," Foreign Affairs, October 15, 2009, https://www.foreignaffairs.com/articles/united-states/2009-10-15/dollar-and-deficits.

[208] Joseph E. Stiglitz, "Joseph E. Stiglitz -- Farewell to the Dollar as the World's Currency of Choice," The Washington Post, August 30, 2009, https://www.washingtonpost.com/wp-dyn/content/article/2009/08/28/AR2009082802111.html.

[209] "Xi Jinping Chairs G20 Hangzhou Summit and Delivers an Opening Speech," Ministry of Foreign Affairs of the People's Republic of China , April 9, 2016, https://www.fmprc.gov.cn/mfa_eng/topics_665678/2016zt/XJPCXBZCESGJTLDRDSYCFHJCXYGHD/201609/t20160906_704134.html.

[210] Stiglitz, "Joseph E. Stiglitz -- Farewell to the Dollar as the World's Currency of Choice."

[211] "World Bank Chief Surprises with Gold Proposal," Reuters (Thomson Reuters, November 9, 2010), https://www.reuters.com/article/us-gold-zoellick-idUSTRE6A72LT20101109.

[212] Stiglitz, "Joseph E. Stiglitz -- Farewell to the Dollar as the World's Currency of Choice."

role for gold (gold standard) once again, something that most central banks and economists view as unrealistic.[213]

The Chinese government has tried to grasp every chance to highlight the importance of IMS reform. In addition, that the role of China within this reform will "help to lift the representativeness and attraction of the SDR, improve the international monetary system, and safeguard global financial stability."[214] Arguably, the motivation of China behind reforming the IMS lays in self-interest. A realistic consideration is that it will be impossible for China to escape the 'dollar trap' until there will be a reform in the current USD dominated IMS. The reason for this is that the current IMS still favors the USD when it comes to government reserves, asset holdings, and transactions,[215] this limits the extant and pace of China to diversify away from the USD. That said, China has attempted to diversify away from the USD as available data shows, seeing that the exact composition of the FX reserves of China is classified information.[216] According to China's State Administration of Foreign Exchange, USD holdings accounted for 58% of the total reserves of China at 2014 years ending; down from 79% in 2005. Moreover, the percentage of USD currency assets of China was lower than the world average of 65% in 2014.[217] China is steadily lowering its holdings of USD reserves, which fell to 23% in 2023, from 59% in 2016.[218]

5.2.5 Geostrategic Interests

The country that controls the global reserve currency can enjoy enormous economic benefits, particularly the ability to finance huge deficits in its own currency; indeed, it is an "exorbitant privilege."[219] Controlling the global reserve currency also has political advantages, such as the "'hard' geopolitical power derived from the monetary dependence of others." This

[213] Bettina Bien Greaves, "How to Return to the Gold Standard: Bettina Bien Greaves," FEE (Foundation for Economic Education, November 1, 1995), https://fee.org/articles/how-to-return-to-the-gold-standard/.
[214] "Xi Jinping Chairs G20 Hangzhou Summit and Delivers an Opening Speech," Ministry of Foreign Affairs of the People's Republic of China.
[215] Serkan Arslanalp, Barry Eichengreen, and Chima Simpson-Bell, "Dollar Dominance and the Rise of Nontraditional Reserve Currencies," IMF Blog (International Monetary Fund , June 1, 2022), https://www.imf.org/en/Blogs/Articles/2022/06/01/blog-dollar-dominance-and-the-rise-of-nontraditional-reserve-currencies.
[216] Gabriel Wildau, "China's Dwindling Forex Reserves Raise Worries," Financial Times, October 18, 2015, https://www.ft.com/content/6359c170-6e52-11e5-8171-ba1968cf791a.
[217] Zhou Xin, "How Much of China's Foreign Exchange Reserves Are in US Dollars?," South China Morning Post, July 29, 2019, https://www.scmp.com/economy/china-economy/article/3020410/how-much-chinas-forex-reserves-us-dollars-beijing-gives-two.
[218] Todd C. Lee, "China (mainland) may move to limit impact of US financial weapons," S&P Global, November 11, 2022, https://www.spglobal.com/marketintelligence/en/mi/research-analysis/china-may-move-to-limit-impact-of-us-financial-weapons.html.
[219] Eichengreen, *Exorbitant Privilege: The Rise and Fall of the Dollar and the Future of the International Monetary System.*

advantage enables a controlling government to pursue foreign interests without restraint or even to apply some degree of international coercion.[220] Moreover, based on historical cycles, "great powers have great currencies."[221] The Chinese government is well aware of the need to elevate the RMB to the position of an international currency that is befitting and accommodating the rise of China as a global power. Moreover, the Chinese government also recognizes the role played by the USD as foundation of the geopolitical privileges of the US. It is clear that China is not content with, what has been called by them, "Washington's global hegemony."[222] As a result, the internationalization of the RMB, while primarily aimed at making the RMB a major reserve currency, is also worthwhile as a means of furthering the geopolitical agenda of China.[223] Due to close economic ties with China, East Asia has been especially susceptible to the internationalization strategy of the RMB. Since the 1980s, China became the production base for East Asian firms seeing that China started to be involved with Asian economies through international production sharing.[224] China has, through the rise of the RMB, enhanced its economic and political status across East Asia. This, in turn, has provided momentum to further internationalize the RMB.[225]

5.3 Key Developments in RMB Internationalization

It is difficult to pinpoint the precise timing when China started to pursue the goal of internationalizing the RMB. Nevertheless, it seems that 2006 was the key turning point and the start of the process of RMB internationalization.[226] Seeing that the internationalization of the RMB is a unique case, the research needs to take into consideration the following factors, which are associated with the internationalization of a currency. First, a currency serves the

[220] Benjamin J. Cohen, *The Geopolitics of Currencies and the Future of the International System*, paper prepared for a conference on The Geopolitics of Currencies and Oil, Madrid: Real Institute Elcano, 7 November, 2003, p. 5.
[221] Robert A. Mundell, "The International Monetary System: The Missing Factor," *Journal of Policy Modeling* 17, no. 5 (October 1995): pp. 479-492, https://doi.org/10.1016/0161-8938(95)00053-v, pp. 1-2.
[222] Benjamin J. Cohen, "The Future of Reserve Currencies, Finance & Development," International Monetary Fund, September, 2009, https://www.imf.org/external/pubs/ft/fandd/2009/09/cohen.htm.
[223] Park, "China's RMB Internationalization Strategy: Its Rationales, State of Play, Prospects and Implications," p. 18.
[224] Guillaume Gaulier, Françoise Lemoine, and Deniz Ünal-Kesenci, "China's Integration in East Asia:Production Sharing, FDI & High-Tech Trade," *Economic Change and Restructuring* 40, no. 1-2 (May 22, 2007): pp. 27-63, https://doi.org/10.1007/s10644-007-9013-5, p. 12; Simon Tay, "Managing China's Regional Economic Integration," East Asia Forum, April 26, 2022, https://www.eastasiaforum.org/2022/04/28/managing-chinas-regional-economic-integration/.
[225] Dimitrios Lyratzakis, "The Determinants of RMB Internationalization: The Political Economy of a Currency's Rise," *American Journal of Chinese Studies* 21, no. 2 (October 2014): pp. 163-184, p. 180.
[226] Benjamin J. Cohen and Chiu Eric M P., *Power in a Changing World Economy: Lessons from East Asia* (London: Routledge, 2014), pp. 1-14.

domestic functions of medium of exchange, store of value, and unit of account.[227] An international currency can be used as a medium of exchange (vehicle) for private transactions and as an intervention currency by central banks to invoice trade and serve as a peg in exchange rates. Moreover, it is used to hold liquid assets denominated in a specific currency by private agents (banking role) as well as by central banks as a reserve.[228] Secondly, as proven by the history of major currencies such as the GBP and USD, the internationalization of the currency of a country often goes through three stages: trade currency, investment currency, and lastly an international reserve currency.[229] Finally, as noted before, stability, fair value, wide acceptance and wide circulation are the main components that any currency needs to exhibit to become the global reserve.[230] The strategy of the Chinese government to internationalize the RMB can be seen in a framework of three segments. The first segment concerns itself with the promotion of usage of the RMB in trade settlements and financial transaction denominated in RMB. The second segment revolves around the efforts of China to create a global web of financial infrastructure and networks around the RMB. This will give further momentum to the international use of the RMB, something that will establish a growing and favorable environment in which to internationalize the RMB. The last segment relates to the intention of China to reform the current USD dominated IMS. The connection of the topics of each segment can be seen in the appendix.[231]

5.4 Theoretical Considerations

Based on the three-segment framework in the appendix the research observes multiple connections between the RMB internationalization strategy of China and the theories of IPE, Rise and Fall, and Structural Realism. The RMB internationalization strategy employed by China is a great example of international political economics in action. The strategy aims to increase the economic power of China within the international system by promoting the

[227] Cohen and Chiu, *Power in a Changing World Economy: Lessons from East Asia*, p. 4.
[228] Paul R. Krugman, "The International Role of the Dollar: Theory and Prospect," *in Exchange Rate Theory and Practice, ed.* John F. O. Bilson and Richard C. Marston (University of Chicago Press, 1984), p. 263.
[229] *The Internationalization of the Renminbi,* International Monetary Institute and Renmin University of China (Routledge, 2014), p.16.
[230] Bayoumi and Eichengreen, "Ever Closer to Heaven? An Optimum-Currency-Area Index for European Countries."
[231] [231] Park, "China's RMB Internationalization Strategy: Its Rationales, State of Play, Prospects and Implications," pp. 21-80; *2021 RMB Internationalization Report,* Beijing: The People's Bank of China, 2021, pp. 41-75.
Note: the framework in the appendix merely generalizes the steps China has undertaken to facilitate the internationalization of the RMB. For a more detailed timeline reference the sources used to construct the framework (see above).

adoption and use of the RMB as global currency. The goal of China to lessen its dependence on the USD and make itself less vulnerable to the influence of US monetary policy on the Chinese economy is accomplished by increasing the use of the RMB in international trade as a settlement currency. Within this strategy, the internationalization of Chinese financial infrastructure and networks is also included; allows China to exercise greater influence over the IMS. As a result of this, the RMB internationalization strategy reflects the ambitions of China to restructure the global economic order and thereby also establishing itself as a prominent actor within the international political economy. Moreover, a connection between the RMB internationalization strategy and the rise and fall theory can be observed. The rise and fall theory stipulates that the relative influence of a nation within the international system is determined by its economic and military capabilities. The strategy is highly representative of the goal of China to enhance its economic power and with that influence the international system, as well as to challenge the dominance of the US over the current system. China intends to enhance its economic capabilities and position in the international system through the promotion of the use of the RMB as an international currency and by expanding the Chinese financial infrastructure and networks. The attempt to shift the balance of power in the international system can especially be noted through the fact that China is promoting and facilitation the use of RMB in international trade transactions, the establishment of RMB trading and clearing centers, and the expansion of bilateral swap agreements with other countries. Lastly, the RMB internationalization can also be analyzed through the lens of structural realism. Structural realism argues that states operate rationally within the anarchic international system with the goal to maximize their power and security. The RMB internationalization strategy represents the efforts of China to strengthen its economic power and security in the face of the perceived threat of the US. A main goal of China is to improve its economic autonomy and decrease/mitigate the influence of external factors on the Chinese economy. This by reducing the reliance of China on the USD and extending its financial infrastructure and networks abroad. China is essentially protecting its own security and sovereignty within the increasingly volatile and competitive international system, which can be viewed as a main driver for its strategy.

6. US-China Trade War and Ukraine: Accelerating Dedollarization

It ought to be emphasized again that the internationalization of the RMB and the potential of the RMB to become a major/global reserve currency are highly related but not equivalent. That said, in the light of the current volatile geopolitical and economic climate, it is important to recognize the impact of the US-China trade war and the war in Ukraine on the dedollarization efforts of China, seeing that it connects with one of the main motivations behind the RMB internationalization strategy of China.

6.1 The US-China Trade War

The term "China First" stems from policy implemented by the Trump administration which prioritized the interest of the US over those of China. The policy included a range of measures such as restrictions on Chinese investments in the US, imposing tariffs on Chinese imports, and large scale scrutinizing of Chinese technology companies. Moreover, the US stated that the policy was aimed at addressing what they viewed as the unfair trade practices of China. Resulting from the "China First" policy was the US-China trade war. In an effort to reduce trade deficits between the two countries, the US imposed tariffs on Chinese imports, simultaneously, China responded with tariffs on US imports in retaliation.[232] As an extension of the dragging effects of the US-China trade war, the "Compensation For Americans Act" needs to be taken into consideration. Despite the act only being introduced, it is very showing of the hardline US lawmakers are eager to get started in lieu of protecting US interests. The specific measures proposed by the Wagner bill that the research wants to draw attention to includes the following: freezing the necessary Chinese assets in the US in order to reach a US-China bilateral compensation agreement, removing the eligibility of China for World Bank development loans, removing the "developing country" status of China in international organizations, and prohibiting the use of federal retirement saving as a way to invest in China.[233] More recently, can the "China Trade Relations Act of 2023" be observed, which calls for:

> To withdraw normal trade relations treatment from, and apply certain provisions of

[232] Paweł Paszak, "U.S.-China Trade War: Origins, Timeline and Consequences," Warsaw Institute, September 21, 2021, https://warsawinstitute.org/u-s-china-trade-war-origins-timeline-consequences/.

[233] "H.R.3882 – Compensation for Americans Act of 2021," Library of Congress, 14 April, 2021, https://www.congress.gov/bill/117th-congress/house-bill/3882.

title IV of the Trade Act of 1974 to, products of the People's Republic of China, and to expand the eligibility requirements for products of the People's Republic of China to receive normal trade relations treatment in the future, and for other purposes.[234]

These developments have highlighted numerous things for China when it comes to the US, the most important, for the research, being: increasing the rate of RMB internationalization is vital for China, seeing that further financial sanctions on China from the US would put immediate pressure on the RMB. Moreover, developing and diversifying away from the USD would be in the best strategic interest of China, seeing that a small or no reliance on the USD would also result in mitigating the effect of any US sanctions, rendering them essentially useless. However, within this context, there is a critical question that needs to be considered. Can the RMB and its monetary support fulfill the entire body of tasks of an international currency and keep the Chinese economy within effective operation under a worst-case scenario, such as barring Chinese state-owned banks from utilizing the USD? This is a question that relates deeply to the medium- and long-term objectives of the internationalization strategy of the RMB.[235]

The US has been weaponzing the USD through economic sanctions to pressure its opponents numerous times in the past decades, a process that has only intensified during the Obama and Trump administrations.[236] Recent numbers show that the amount of sanctions against China from the US total up to 441 on the Specially Designated Nationals and Blocked Persons List (SDN).[237] Additionally 68 entries can be found on the CMIC list, which is directly related to US national security and foreign policy concerns about the behavior of China and is part of a broader strategy of the US to manage the systemic competition with China. The growth in and current size of SDN designations of Chinese persons is observed to be corresponding with an increase in the amount of underlying sanctions programs. The majority of SDN designations on China are intended at providing material assistance to sanctioned countries such as Iran, rather than targeting China specifically. As a result of this, even though the increase in SDN designations could reflect broader bilateral tensions

[234] "S,125 – China Trade Relations Act of 2023," Library of Congress, 26 January, 2023, https://www.congress.gov/bill/118th-congress/senate-bill/125?s=1&r=55.
[235] Xiong Lan, "Escalating China-US Confrontation Will Accelerate RMB Internationalisation," ThinkChina, July 28, 2021, https://www.thinkchina.sg/escalating-china-us-confrontation-will-accelerate-rmb-internationalisation.
[236] Jeffry J. Scott, *Raising a Caution Flag on US Financial Sanctions against China,* Washington DC: Peterson Institute for International Economics, 2021, pp. 1-2.
[237] "Sanctions List Search," Office of Foreign Assets Control, 8 May, 2023, https://sanctionssearch.ofac.treas.gov.

between the US and China, it is more likely the outcome of the US expanding the use of sanctions as a global foreign policy instrument. It could also indicate the interconnectedness of Chinese enterprises in international trade, which includes trade with adversaries of the US. Since 2000, 258 SDN designations on China were implemented under sanctions programs that were not directed towards China, compared to 67 that actually were. [238]

The financial and monetary dominance of the US stems from its financial strength, hegemony with the USD as the global currency, and its asymmetric dependency with other nations. Simply put, there are three possibilities to avoid US sanctions. One of them being alliance with the US. Second, nations can try to accomplish financial and monetary independence from the US, as is the case for Russia and Iran. Lastly, nations may enhance their financial and monetary position as to compete with the US and the USD.[239] Moreover, as can be seen from SDN designations on China, a country may also encounter and suffer from the consequences of indirect sanctioning, which is advocative of the dominance of the US and the USD over the wider international system, including the IMS.

When looking at the dimensions of leadership, geopolitics, and opportunity, it is quite likely that China will continue encountering US sanctions. Leadership, here, regards to the leader of the US. There is no guarantee that black swan events will not occur regularly if the US is not being led by someone well informed, tactful, and considerate about global politics. An example of this is the idea of the succession of Biden by a president that adopts a political style inspired by Trump, in which the US wins as long as adversaries lose more, or as instigating the trade war, and financial and currency war is waged against China again. Geopolitics refers to specific issues that the US views as a potential reason to sanction. This includes anything related to, for example, the origin of Covid-19, Xinjiang, Taiwan, the South China Sea, and Hong Kong.[240] Commenters have stated that the US treasury ought to avoid the designation of global systematically important banks (G-SIBs) and other high-profile entities when there has not been a full analysis and a lack of understanding of the potential consequences of doing so for US interests and related financial markets. However, the reality teaches that the 'full analysis' and 'clear understanding of potential consequences'

[238] Emily Kilcrease and Michael Frazer, "Sanctions by the Numbers: SDN, CMIC, and Entity List Designations on China," Center for a New American Security , March 2, 2023, https://www.cnas.org/publications/reports/sanctions-by-the-numbers-sdn-cmic-and-entity-list-designations-on-china.

[239] Lan, "Escalating China-US Confrontation Will Accelerate RMB Internationalisation."

[240] Frank Tang, "Yuan to Become No 3 Global Currency by 2030, Morgan Stanley Predicts," South China Morning Post, September 8, 2020, https://www.scmp.com/economy/china-economy/article/3100575/chinese-yuan-become-no-3-global-currency-2030-after-us-dollar.

is something that is often overlooked by the US.[241] Opportunity revolves about megatrends, including Covid-19 and the war in Ukraine that have caused global divisions. The shift in the economic emphasis from "great international circulation" to "dual circulation," that prioritizes local consumption, appears to be the response of China to these megatrends. As China is becoming the number one adversary of the US and therefore seen as a major threat, the US will probably deal with its "China problem" the same way it has with past competition: through gradually isolating China by decoupling, something that might be the deciding factor.[242] But, in the grand scheme of things, the deciding factor for whom? Because this could be viewed as a reverse way of getting China to where it wants to be, and where does that leave the US?

To all issues posed in the dimensions of leadership, geopolitics and opportunity, the answer of China is to accelerate RMB internationalization. That said, China has never set any specific goals for its strategy. Only early 2021, the PBoC proposed that the long-term goal for the internationalization of the RMB should consist out of a 20% of international settlement and clearing, and that the RMB should be 30% of the global reserves. Moreover, that the internationalization strategy should aim, in 2029, for the RMB to exceed a 10% market share of international currencies.[243] This falls in line with the 10.92% currency weight that was envisaged at the time that the RMB was included in IMF SDR basket in 2016.[244]

In the context of the comprehensive US-China competition, it could be argued that the rate at which the RMB internationalizes is determined by the rate at which the US-China competition develops towards confrontation. If the competitive momentum surpasses that of conflict, the RMB will probably continue to slowly and gradually internationalize at its current rate (with the RMB expected to overtake the JPY and GBP in reserve currency share around 2040). In the contrary scenario, the internationalization of the RMB will accelerate (with the RMB overtaking either the JPY or GBP before 2029).[245] With the US-China confrontation in mind, China and Iran signed a 25-year cooperation agreement in 2021,

[241] Scott, *Raising a Caution Flag on US Financial Sanctions against China,* p. 9.
[242] Lan, "Escalating China-US Confrontation Will Accelerate RMB Internationalisation."
[243] Ibid.
[244] "IMF Lifts Weighting of Dollar, Chinese Yuan in SDR Basket," Reuters (Thomson Reuters, May 15, 2022), https://www.reuters.com/markets/us/imf-lifts-weighting-dollar-chinese-yuan-sdr-basket-2022-05-15/.
Note: In 2022 the IMF has increased the weighting of the RMB, for the first time since its accession to the SDR, to 12.28%.
[245] Tang, "Yuan to Become No 3 Global Currency by 2030, Morgan Stanley Predicts."; Lan, "Escalating China-US Confrontation Will Accelerate RMB Internationalisation."

which enables China to purchase Iranian oil in RMB.[246] Moreover, China can currently also purchase Russian oil in RMB,[247] plus the fact that China has been engaging in talks with the Gulf States about either pricing oil in RMB, or at least enable China to purchase oil in RMB.[248] The usage of RMB to price and settle payments for oil will have a direct impact on the monopoly of the USD in oil trade. In this case, when and if the US imposes further and harsher financial sanctions on China, it is almost certain that the internationalization of the RMB will accelerate. Something that also should be considered the fact that the most important "stabilizer" of US-China relations is the fiscal and monetary interdependence between the US and China. If the US applies its financial (cutting off financing channels) and monetary power (excluding China from using the USD) to sanction and suppress China, China will most certainly take steps in retaliation, such as selling large amounts of USD denominated assets (as has been observed is happening) and restricting the use of USD in foreign trade. Without the most important user of the USD, the USD market share will eventually fall, and in turn, boost the share of the RMB.[249]

6.2 War in Ukraine: Waking up the Global Community

The entire IMS is based around institutions created by the US, this makes it able for the US to use it against its adversaries. The US controls the SWIFT digital payment system, which is akin to the blood vessels of the IMS. The US has unilaterally banned countries such as Iran, Cuba, and North Korea from SWIFT, essentially excluding them from international trade. The US also leverages the stockpiles of USD and USD denominated assets of foreign countries against them, Russia is a good example of this. When Russia invaded Ukraine, the US froze over 600 billon USD of gold in foreign reserves held in the US and EU, this action and US made Russia unable to pay its foreign debts.[250] The dominance and control of the US over the global financial system highlights that the US can intervene in any conflict on earth, something that is very concerning for China in regard to financial and national security, and it

[246] William Figueroa, "China and Iran since the 25-Year Agreement: The Limits of Cooperation," The Diplomat, February 16, 2023, https://thediplomat.com/2022/01/china-and-iran-since-the-25-year-agreement-the-limits-of-cooperation/.
[247] Phil Rosen, "China Is Buying Russian Oil at a Bigger Discount Using Yuan as Price Cap Looms, Report Says," Business Insider, December 2, 2022, https://www.businessinsider.com/china-russian-oil-yuan-steep-discount-price-cap-europe-sanctions-2022-12?r=US&IR=T.
[248] Javier Blas, "Pricing Petroleum in China's Yuan Sounds Inevitable. Not for Saudi Arabia.," Bloomberg, February 27, 2023, https://www.bloomberg.com/opinion/articles/2023-02-27/pricing-petroleum-in-china-s-yuan-sounds-inevitable-not-for-saudi-arabia.
[249] Lan, "Escalating China-US Confrontation Will Accelerate RMB Internationalisation."
[250] Elisabeth Braw, "Freeze-Don't Seize-Russian Assets," Foreign Policy, January 13, 2023, https://foreignpolicy.com/2023/01/13/putin-sanctions-oligarchs-freeze-seize-assets/.

allows them to financially ruin the side they oppose.[251] This is completely opposite of the free trade and political neutrality the US promised when it established the current globalized financial architecture.[252] This arrangement is incredibly beneficial to the US, but current circumstances have highlighted one problem that the US will probably face very soon: the system only works if the rest of the world, especially oil-bearing states, continue to use the USD.

The weaponization of the USD against Russia following the invasion of Ukraine has increased the expectation that China will speed up its dedollarization strategy in order to defend itself against similar financial sanctions from the US. Despite observations that state that the RMB is unlikely to dethrone the USD in the global financial system on the short run, there are concerns that the weaponization of the USD against Russia has started an irreversible fracturing of the global financial system, which seems to be resulting in two types of IMS, one led by the US and one by China.[253] Essentially, the SWIFT sanctions were a double edged sword for the US.[254] This is underlined by the sheer amount of countries that have moved towards dedollarization shown in figure 2. The sanctions on Russia also acted as a wakeup call for countries, especially those with weak ties to the US, that it is worth diversifying their emergency reserves and to include some currencies or assets that cannot be cut off by the West. As far as options to avoid sanctions from the US go, the RMB is the best option. The RMB can be used to conduct direct trade with the largest exporter in the world, and the war in Ukraine has shown that China is willing to do business with economies that the West has rejected. Despite the continuous attempts of the US to preserve its dominance over the global financial system, an increasing number of countries (figure 2) are establishing agreements to conduct trade in their local currencies and gold rather the USD, or they establish bilateral currency swaps, which eliminates the USD from FX operations.[255]

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[251] Satyajit Das, "'Our Currency, Your Problem': The US Has Made a Weapon of the Dollar," The Sydney Morning Herald, September 7, 2018, https://www.smh.com.au/business/markets/our-currency-your-problem-the-us-has-made-a-weapon-of-the-dollar-20180907-p502d7.html.
[252] Andrew Sheng and Xiao Geng, "The International Monetary System Is More Unfit than Ever," Project Syndicate, May 5, 2022, https://www.project-syndicate.org/commentary/us-dollar-dominance-unsustainable-international-financial-reform-by-andrew-sheng-and-xiao-geng-2022-04.
[253] Lee, "China (mainland) may move to limit impact of US financial weapons."; Robert Greene, "How Sanctions on Russia Will Alter Global Payments Flows," Carnergie Endownment for International Peace, accessed May 9, 2023, https://carnegieendowment.org/2022/03/04/how-sanctions-on-russia-will-alter-global-payments-flows-pub-86575.
[254] Xu Wenhong, "How Much Have the West's Swift Sanctions Affected Russia?," Global Times, May 16, 2022, https://www.globaltimes.cn/page/202205/1265735.shtml.
[255] Faisal Khan, "Why Are Countries Moving towards De-Dollarization?," Medium, March 28, 2023, https://medium.com/technicity/why-are-countries-moving-towards-de-dollarization-da0969460b08; Burgess, Matthew. "De-Dollarization Is Happening at a 'stunning' Pace, Jen Says." Bloomberg, April 18, 2023.

Figure 2. Countries that have moved towards dedollarization in 2022-2023

Egypt	Brazil	Indonesia	Kenya
Russia	China	Myanmar	Saudi Arabia
Bangladesh	Kazakhstan	Philippines	South Africa
UAE	Malaysia	Singapore	France
Laos	Brunei	Thailand	Venezuela
India	Cambodia	Vietnam	Argentina
Cuba	Sri Lanka	DPRK	Ghana
Mongolia	Tanzania	Pakistan	Turkey
Zimbabwe			

All plans for alternative currencies and agreements that avoid the usage of the USD begs the question why the majority of the global economy would utilize the USD. Especially given its reputation as a weapon against those who use it. Ironically, and as can be seen from figure 2, the USD standard essentially pushes all countries that have abundant resources and labor power, based on their place in the global supply and manufacturing chain, to exchange their real wealth for pieces of paper worth a few cents to produce. This development can observed to be a reaction to a famous quote of ex treasury secretary John Connoly back in 1971 when the gold standard was abolished: "The dollar is our currency but it is your problem."[256] Now the world is waking up and recognizing that the US wants their wealth, and therefore it is the problem of the US.

Another thing that should be taken notice of is the idea of leverage. Leverage is one of the most powerful tools in geopolitics. Just like the US is leveraging its control and dominance over the IMS against its adversaries. The countries that have started dedollarizing, are leveraging their own resources such as oil (and other highly traded commodities), labor force, technology, essentially their place and role in the global supply and manufacturing chain, against the US. This is highly telling of the discontent over the current financial system. Within the context of leveraging, there is however, a very abnormal situation when it comes to China. As argued before, there is a relation between the strength of an economy and the power of a currency. Power of a currency, in this case, relating to how much it is being used in trade, transactions, and as reserve currency. China currently has the second largest GDP in the world.[257] It is the largest manufacturing country with close to 30% of the global

https://www.bloomberg.com/news/articles/2023-04-18/de-dollarization-is-happening-at-a-stunning-pace-jen-says#xj4y7vzkg.
[256] Das, "'Our Currency, Your Problem': The US Has Made a Weapon of the Dollar."
[257] "China," OEC, March, 2023, https://oec.world/en/profile/country/chn.

manufacturing output,[258] the largest exporter in the world and second largest importer.[259] Moreover, it is the second largest recipient of foreign direct investment (FDI) and ranks 29 out of 146 in economic complexity within global value chains.[260] Yet, the power of its economy in relation to its currency cannot be found when looking at correlating data for the RMB in figure 3.

Figure 3. Ranking and share of RMB compared to USD[261]

	RMB	**USD**
Rank and share of currency activity for global payments by value	Rank: 5 Share: 2.26%	Rank: 1 Share: 41.74%
Rank and share of international payments	Rank: 7 Share: 1.67%	Rank: 1 Share: 50.61%
Rank and share as a global currency in trade finance market	Rank: 3 Share: 4.50%	Rank: 1 Share: 83.71%
Rank and share as global currency reserve	Rank: 6 Share: 2.69%	Rank: 1 Share: 58.36%

As can be observed from figure 3, the US has by far and large more leverage than China when it comes to the weight of their currency, which, again showcases the abnormal situation in regard to the power of the RMB. This however, does not mean that China is not leveraging other advantages to increase the weight of the RMB. The main asset China can leverage is the BRI, a 3 trillion USD worth project whereby China has given out loans to countries across the world.[262] Many of these countries, for example Pakistan and Sri Lanka, have taken so much debt from China that they are unable to pay it back.[263] How unfortunate the situation may be, this presents a strategic interest for China. China has leverage over these countries and can ask them to take and pay back loans in RMB. Since the launch of the BRI, China has

[258] Joseph Quinlan and Lauren Sanfilippo, "China Is Leading the World on Manufacturing, but the Race Isn't Over," Barron's, August 31, 2022, https://www.barrons.com/articles/china-manufacturing-semiconductor-electronics-us-competition-51661894538.
[259] "China," OEC.
[260] "Supply Chains: China," Asia Society, 2022, https://asiasociety.org/policy-institute/supply-chains-shifting-indo-pacific/china.
[261] "Currency Composition of Official Foreign Exchange Reserves (COFER)," International monetary Fund; *RMB Tracker, Monthly reporting and statistics on renminbi (RMB) progress towards becoming an international currency,* Brussels: Society for Worldwide Interbank Financial Telecommunication (SWIFT), 2023, pp. 2-8.
[262] James Mcbride, Noah Berman, and Andrew Chatzky, "China's Massive Belt and Road Initiative," Council on Foreign Relations, February 2, 2023, https://www.cfr.org/backgrounder/chinas-massive-belt-and-road-initiative.
[263] Dylan Gerstel, "It's A (Debt) Trap! Managing China-IMF Cooperation across the Belt and Road," CSIS, September 17, 2018, https://www.csis.org/analysis/its-debt-trap-managing-china-imf-cooperation-across-belt-and-road; Ayjaz Wani, "Invest, Indebt, Incapacitate: Is China Replicating Its 'Xinjiang Model' in BRI Countries?," ORF, September 8, 2020, https://www.orfonline.org/research/is-china-replicating-its-xinjiang-model-in-bri-countries/.

increasingly issued outstanding loans in RMB, therefore without relying on the USD.[264] Moreover, the Free Trade Agreement (FTA) network of China has been steadily expanding, especially within the global south and among BRI participants.[265] Most FTAs are concluded between China and nations that figure 2 shows, are currently dedollarizing. Additionally, China is also the largest trade partner of more than 120 countries,[266] many of which are BRI participating countries, so again, it is leveraging trade. China may not be able to leverage the weight of the RMB yet, but they can most certainly leverage the combination of debt and trade. With this leverage China has over more than two thirds of the world population,[267] it could influence them to use the RMB over the USD. This would mean that China could simultaneously enhances its efforts in building global RMB financial infrastructure and networks, accelerating momentum for the new IMS, and promoting the use of RMB over the long-term; which falls in line with the RMB internationalization strategy outlined in the appendix.

What can also be observed from figure 2 is the fact that dedollarizing countries and countries that are part of the BRI initiative are generally underdeveloped. But for the internationalization of the RMB to succeed, China will need to get some of the developed nations of the West also on board so to speak. This process takes place through bilateral swap agreements.[268] Bilateral swap agreements enable even major actors to conduct international trade without depending on the USD. Bilateral swap agreements present a couple of advantages that can aid China in its RMB internationalization strategy. First, both countries can eliminate their exchange risk. Second, trade can be carried out more economically so the business relationship between the swapping countries gets better over time. Lastly, and most importantly, the dependency on the US decreases by a large extent. It is therefore logical that China signed bilateral currency swap agreements with over 40 countries.[269] Seeing that China is the largest manufacturer in the world, they could leverage even further by asking for

[264] Keith Bradsher, "After Doling out Huge Loans, China Is Now Bailing out Countries," The New York Times, March 27, 2023, https://www.nytimes.com/2023/03/27/business/china-loans-bailouts-debt.html.
[265] "China FTA Network," Ministry of Commerce People's Republic of China, 2023, http://fta.mofcom.gov.cn/english/fta_qianshu.shtml.
[266] Mark A. Green, "China Is the Top Trading Partner to More than 120 Countries," Wilson Center, January 17, 2023, https://www.wilsoncenter.org/blog-post/china-top-trading-partner-more-120-countries.
[267] Mcbride, Berman, and Chatzky, "China's Massive Belt and Road Initiative."
[268] Bilateral currency swap agreements are financial arrangements between central banks that allows for the exchange of the respective currencies of two countries at a predetermined exchange rate for a specific time period.
[269] Zhitao Lin, Wenjie Zhan, and Yin-Wong Cheung, "China's Bilateral Currency Swap Lines," *China &Amp; World Economy* 24, no. 6 (2016): pp. 19-42, https://doi.org/10.1111/cwe.12179; Maia Nikoladze, "Internationalization of the RENMIBI via Bilateral Swap Lines," Atlantic Council, April 7, 2022, https://www.atlanticcouncil.org/blogs/econographics/internationalization-of-the-renmibi-via-bilateral-swap-lines/.

transactions in RMB rather than USD. Moreover, with the idea that the Gulf States are considering to price oil in RMB, this would mean that numerous countries would want to obtain RMB, and that excess RMB could be invested in Chinese bonds, enhancing the Chinese economy and RMB internationalization over time.[270]

6.3 Theoretical considerations

From the perspective of realism, the foreign policy of a state is primarily driven by the pursuit of power and security, to survive within an anarchic international system. With this in mind, the internationalization of the RMB, the actions of China in the US-China trade war, and the efforts of China to dedollarize can be viewed as a part of the pursuit of China for economic and financial power; this is essential for the long-term security and survival of China. The internationalization of the RMB can be seen as an attempt of China to reduce its dependence on the USD dominated IMS, which China views as a vulnerable point of its economy. The promotion of the RMB in international trade and finance helps China strengthening its economic influence and therefore increased financial autonomy and a reduction in the degree of vulnerability to US economic pressure. Based on realism it could be argued that the US-China trade war is a manifestation of the efforts of the US to control the rise of China as a global economic power. In order to defend its interest the response of China to was adopt a more assertive and aggressive approach towards the US, this included tariffs and other economic measures in retaliation. This is reflective of the understanding of China that economic power is a key component of the overall power of a nation. Therefore, China needs to defend and protect its economy from external threats such as US sanctions.

From the perspective of IPE, the US-China trade war, dedollarization and the internationalization of the RMB can be viewed as an interrelated development which is reflective of the growing role of China within the global economy and its efforts to reshape the IMS in such a way that it can accommodate its growth. The US-China trade war is reflective of the growing tension and as result of that conflicts that arise from the competing economic interest between the largest and second largest economies in the world. For China the trade war highlighted the need to reduce its reliance on US trade goods and US in general, therefore diversifying its trade partners. In order to achieve this, China has expanded its trade

[270] "The U.S. Dollar Tale: Entering the 'Petrodollar' System," Medium, April 13, 2022, https://medium.com/coinmonks/the-u-s-dollar-tale-entering-the-petrodollar-system-620c56211825; Frank Holmes, "Petrodollar Dusk, Petroyuan Dawn: What Investors Need to Know," Forbes, March 28, 2023, https://www.forbes.com/sites/greatspeculations/2023/03/27/petrodollar-dusk-petroyuan-dawn-what-investors-need-to-know/?sh=663a18155aa5.

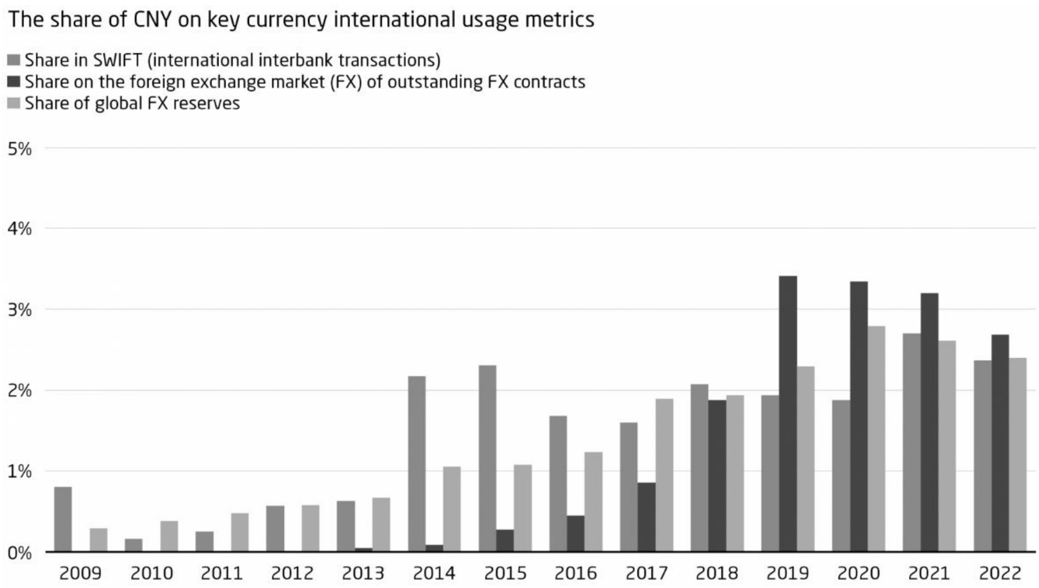
relations with other countries, particularly along the BRI, and by investing in its domestic technological capabilities, of which the e-CNY is a good example. Moreover, the dedollarization strategy of China can be seen as part of a broader strategy to shift the balance of power in the global economy away from the US. The promotion of the use of the RMB, and development of alternative financial institutions such as the Asian Infrastructure Investment Bank, highlight that China wants to change the international economic order that is currently dominated by the US. This in order to create a more balanced and inclusive IMS.

7. Challenges and Opportunities for the RMB Internationalization

Taking current developments into consideration, challenges and opportunities can almost be taken as one and the same when it comes to the internationalization of the RMB. As stated before the internationalization of the currency of a country often goes through three stages: trade currency, investment currency, and lastly an international reserve currency. And for a currency to become the global reserve currency it must display stability, fair value, wide acceptance and wide circulation. The RMB is currently lacking most of these categories. China has proven multiple times that it is the exception to a lot of conventional rules, but given the amount of obstacles in RMB internationalization and lack of clear RMB internationalization planning is telling of how well equipped the RMB is to take on the role of global reserve currency at the moment. It may therefore be better that at this stage in the RMB internationalization China needs to focus on becoming a regional hegemon in regards to the usage of the RMB as a reserve currency. That said, the internationalization of the RMB will, in the long run, present a major benefit to the international system namely, if the strategy succeeds the RMB will be an alternative global medium of exchange and safe asset for central bank. This to fill the gap caused by the decreasing weight of the EUR and USD. Because relatively speaking the US and Eurozone economies will shrink compared to the rest of the world. In addition, developing countries such as China and India will be expanding their economic size and therefore the US treasury security will not be enough to supply the world with safe assets, which highlights the need for at least a third major reserve currency, and China is an obvious candidate for this position.[271] Therefore, the current observed fracturing in the international system might further facilitate the internationalization of the RMB at a regional level.

[271] Edwin L.-C Lai, "One Currency, Two Markets: China's Attempt to Internationalize the Renminbi," Conference, Institute for International Economic Policy, Washington DC, November 5, 2021.

Figure 4. *International use of the RMB*[272]



The internationalization of the RMB has halted in recent years (see figure 4), and even Chinese experts agree that for the RMB to become usable cross-border, it will need to meet three requirements: accessibility, availability, and trust.[273] The RMB has made significant progress towards meeting the first condition, seeing that the financial markets of China have become more accessible to foreign investors via "stock connect" trading linages to Hong Kong. Chinese securities are now included in major international financial indexes, and reforms have enhanced the liquidity and depth of the bond market, which is popular among foreign investors seeking to invest in secure assets. Despite this leading to massive inflows from outside of China, the other two criteria are have blocked significant advances towards internationalizing the RMB. Recent years show that the current account of China went back into surplus, which means that other countries had a net outflow of RMB as they paid for Chinese imports. The constrained international availability of the RMB will likely continue seeing the official objective of China to maintain an industrial share of GDP like that of countries with big trade surpluses. Moreover, the trust factor has hardly improved in the eyes of the West. Western observers note that despite the significant reforms of the financial and legal framework of China, the transparency and predictability of the Chinese financial system has barely improved.[274] Moreover, that FX management was outsourced to state-owned

[272] François Chimits, "The E-CNY Will Not Help the Yuan Displace the Dollar Any Time Soon," Merics, May 5, 2023, https://merics.org/en/comment/e-cny-will-not-help-yuan-displace-dollar-any-time-soon.
[273] Yiping Huang, Dali Wang, and Gang Fan, "Paths to a Reserve Currency: Internationalization of the Renminbi and Its implications," *ADBI Working Paper Series,* no. 428 (2014): pp. 9-22.
[274] Chimits, "The E-CNY Will Not Help the Yuan Displace the Dollar Any Time Soon."

banks in very arcane ways,[275] and that the Chinese monetary policy returned to using more opaque instruments.[276] Additionally, that there is a widely shared perception, especially among the US and its allies, that the more ideologized political environment of China has done nothing to foster the trust of foreign investors.[277]

There are four key factors when it comes to the success of the RMB internationalization strategy of China: economic size, capital mobility, a deep, broad and liquid financial market, and the confidence of foreigners in the Chinese system. It is clear that China has the required economic size, but a lot needs to be done to acquire the other three factors. Currency internationalization requires a currency to be largely or fully convertible in the capital account. In addition, as mentioned before, China does not want to fully integrate the Chinese system with the West on the short run. This can be seen from the adoption of China of the "one currency, two markets" approach. It essentially is a firewall between the on- and offshore markets, that allows for partial convertibility in the onshore market and full convertibility in the offshore market. However, the internationalization of the RMB requires more than an offshore market alone. It would, for example, need liberalize its capital account and financial sector.[278] That said, in case of economy and monetary liberalization China will face something called the "open economy trilemma." The open economy trilemma is a concept that highlights the three incompatible policy goals associated with an open economy. These goals are fixed exchange rates, free capital mobility, and autonomous monetary policy. In order to internationalize the RMB, China will need to loosen its capital controls (gain free capital mobility). As can be seen from the general realist approach of the Chinese government and its goal to create an RMB financial structure away from the USD dominance, it can be argued that China therefore would also want autonomous monetary policy. Therefore, China may have to give up a considerable degree of stability of the RMB exchange rate.[279] That said, free and full convertibility is not always a good thing, as can be seen from the EUR that became a victim of its own success. By having sufficiently developed financial markets to support large amounts of foreign capital inflows, the Eurozone was able to access cheap credit for an extended period of time, this lead to a staggering surge of the

[275] *Report to Congress. Macroeconomic and Foreign Exchange Policies of Major Trading Partners of the United States.* Washington: U.S. Department of the Treasury Office of International Affairs, 2022, pp. 57-59.
[276] Helge Berger *et al.,* "People's Republic of China: Selected Issues," *IMF Country Report,* no. 22/22 (2021): pp. 71-77.
[277] Barry Naughton and Briana Boland, "CCP Inc.: The Reshaping of China's State Capitalist System," CSIS, January 31, 2023, https://www.csis.org/analysis/ccp-inc-reshaping-chinas-state-capitalist-system.
[278] Lai, "One Currency, Two Markets: China's Attempt to Internationalize the Renminbi."
[279] Dirk Schoenmaker, "The Financial Trilemma," *Economics Letters* 111, no. 1 (January 13, 2011): 57–59, https://doi.org/10.1016/j.econlet.2011.01.010.

value of the EUR. Later, the free convertibility of the EUR led to an unsustainable growth in certain sectors which resulted in collapse.[280] Moreover, periodic crises have highlighted that nonconvertible currencies control the impact of economic shocks on domestic financial markets easier.[281] This is, quite obviously, an interest of internal security for China.

The openness of the capital account of China is low even for a developing country. There are many capital control measures in place, and the foreign ownership of Chinese bonds is low. When taking a look at the gross international investment position as a percentage of GDP,[282] it shows that the openness of China is less than one third of that of the US.[283] Capital account opening is important for the internationalization of the RMB for several reasons. Firstly, increased capital mobility enhances inward and outward investment flows. Moreover, less capital control increases the degree of how much a currency can be used internationally as it increases the market thickness (total amount of international transactions) of a currency. To put it simply if RMB is allowed to leave China, the accumulation of offshore RMB will increase the internationalization of the RMB. Lastly, a thicker market for the RMB lowers transaction costs of currency conversion and increases the convenience of using the RMB.[284]

Financial sector liberalization is also an important factor for the internationalization of the RMB, seeing that the financial development index of China is still low.[285] Deeper, broader and more liquid financial markets increase the amount of FDI in RMB-denominated assets. An increase in financial development also results in a wider use of RMB internationally (it increases the market thickness). It basically revolves around the attractiveness of keeping a currency and its associated financial products. This is why, for example, the USD is so attractive to keep offshore, because it can still be used for a wide variety of things such as buying US bonds or conduct international trade. An underdeveloped financial market cannot be deep, broad and liquid, and therefore also cannot be open. Seeing

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[280] Miguel Otero Otero Iglesias, "The Internationalisation of the Renminbi: Prospects and Risks (ARI)," Elcano Royal Institute, January 17, 2022, https://www.realinstitutoelcano.org/en/analyses/the-internationalisation-of-the-renminbi-prospects-and-risks-ari/.

[281] Oriol Caudevilla, "Opinion - Internationalizing the RMB: How Will the Digital Yuan Be of Help?," Macau Business, January 29, 2023, https://www.macaubusiness.com/opinion-internationalizing-the-rmb-how-will-the-digital-yuan-be-of-help/.

[282] De facto measurement tool of capital account openness.

[283] "SAFE Releases China's International Investment Position as at the End of 2022," State Administration of Foreign Exchange, March 31, 2023, https://www.safe.gov.cn/en/2023/0331/2063.html; "U.S. International Investment Position, 4th Quarter and Year 2022," Bureau of Economic Analysis, March 23, 2023, https://www.bea.gov/news/2023/us-international-investment-position-4th-quarter-and-year-2022.

[284] Lai, "One Currency, Two Markets: China's Attempt to Internationalize the Renminbi."

[285] "Financial Development Index Database," International Monetary Fund, 2023, https://data.imf.org/?sk=F8032E80-B36C-43B1-AC26-493C5B1CD33B&sId=1485894037365&ref=mondato-insight.

the disproportionally large size of the banking sector of China, it will need to develop its bond and stock market significantly. The development of the bond market, specifically the central government bond market, is crucial for the internationalization of the of the RMB.[286] That said, there are many obstacles, such as its small size, its lack of liquidity and the small share of foreign ownership of Chinese bonds.[287] This can be seen in the central government bond turnover ratio of China, it is extremely low, indicating that people are barely buying and selling.[288] In order for a central government bond to be attractive it needs to have a lot of turnover, for it to be considered a liquid and safe asset for foreigners. When it comes to the stock market, many problems can be observed. Most of them having to do with the lack of transparency, track record of government intervention, corporate governance and capital controls.[289] Therefore, the fund raising capacity of China is still way too low in comparison to the developed and mature markets.[290]

Seeing these internal obstacles towards RMB internationalization, the importance of the offshore RMB market becomes clear. Because it enables China to internationalize the RMB while opening the onshore capital account of China at their own pace. That said, the onshore financial development and freeing up the capital account are still the main drivers of the RMB internationalization. Seeing that the offshore market is unable to fully carry the internationalization of the RMB. Offshore foreign banks can send and receive RMB payments directly to and from China through the Cross-Border Interbank Payment System (CIPS). In the long run, CIPS can enable Chinese international payment flows without the intervention and legal reach of the US, which will provide more financial and national security to China.[291]

When looking back at the cycles within the rise and fall theory, it can be observed that China is the largest trading nation, and that is why it is logical that China will develop its capital markets and open them up for foreign investment; it is part of a pattern that has happened cyclically throughout history. Seeing that the RMB will in all likeliness not be a major reserve currency on the short term, but it is probably going to happen much faster than

[286] Lai, "One Currency, Two Markets: China's Attempt to Internationalize the Renminbi."
[287] Dorothy Neufeld, "Ranked: The Largest Bond Markets in the World," World Economic Forum, April 17, 2023, https://www.weforum.org/agenda/2023/04/ranked-the-largest-bond-markets-in-the-world/.
[288] "Financial Market Report (March 2022)," The People's Bank of China, 2022, http://www.pbc.gov.cn/en/3688235/3688609/3688612/4541041/index.html.
[289] Lai, "One Currency, Two Markets: China's Attempt to Internationalize the Renminbi."
[290] "Largest stock exchange operators worldwide as of March 2023, by market capitalization of listed companies," Statista, April 24, 2023, https://www.statista.com/statistics/270126/largest-stock-exchange-operators-by-market-capitalization-of-listed-companies/.
[291] Lai, "One Currency, Two Markets: China's Attempt to Internationalize the Renminbi."

expected. This assuming the data projection 5 years from now when it comes to the store hold of wealth, which indicates an increased move into different financial assets, including into those of China.[292] However, a reoccurring problem in the West when it comes to China is the assumption of a debt issue in China which is primarily associated with the BRI.[293] There is a basic idea behind debt problems for countries, and depends whether the debt is denominated in its domestic currency or not. If the debt is in its domestic currency there are a lot of ways to deal with it such as restructuring or monetizing. If a country can control debt in its domestic currency it is manageable, Japan is a good example of this.[294] It is therefore of importance that China pushes for debt payments along the BRI in RMB, rather than any other currency. This for the long-term attractiveness of the RMB for investment. Moreover, the fact that the policy making structure of China is the one party system, may very well be a positive asset towards the internationalization of the RMB. In comparison to the US, China has a low risk when it comes to frequent policy changes. Another benefit is the fact that Chine can hire quality leadership and does not have a random popularity contest such as the US. China is essentially being run like a big corporation (top down) and it does lead itself, which makes that China is often not as disorderly as democracies. These are advantages China has over the US, in particular during conflict or stressful periods.[295] This aspect of internal order and low-risk approach of the Chinese government will most certainly help positioning the RMB as a safe asset for foreign investors.

7.1 The Role of the e-CNY

China is currently working to expand the scenarios to which the e-CNY can be applied while setting up the facilitation for cross-border payments in e-CNY, a process that will also aid the economic recovery of China. The trials for the e-CNY started in 2019 and have gotten a lot of attention seeing that China was one of the first, and the first major country to develop a

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[292] Phil Rosen, "China Will Become the Global Economy's Biggest Growth Driver in the next 5 Years, Doubling the US Contribution, IMF Says," Business Insider, April 17, 2023, https://markets.businessinsider.com/news/stocks/china-economic-growth-us-imf-europe-fund-markets-forecast-outlook-2023-4; "An Update to the Economic Outlook: 2020 to 2030," Congressional Budget Office, July 22, 2022, https://www.cbo.gov/publication/56465; *China 2030 Building a Modern, Harmonious, and Creative High-Income Society* (Washington, D.C.: World Bank, 2013), pp. 367-401.

[293] "China's Local-Debt Crisis Is about to Get Nasty," The Economist, April 4, 2023, https://www.economist.com/finance-and-economics/2023/05/04/chinas-local-debt-crisis-is-about-to-get-nasty; "China's Emerging Belt and Road Debt Crisis," Financial Times, July 27, 2022, https://www.ft.com/content/eb2d89f6-afd1-491e-b753-863e9727f6de.

[294] Brent Radcliffe, "How Countries Deal with Debt," ed. Michael J. Boyle, Investopedia, June 30, 2022, https://www.investopedia.com/articles/economics/10/sovereign-debt-default.asp.

[295] Jia Qingguo, "Economic Development, Political Stability and International Respect," *Journal of International Affairs* 49, no. 2 (Winter 1996): 572–89, pp. 582-583.

CBDC. CBDCs are expected to become a critical financial infrastructure in the digital age and within the emerging dimension of the competitiveness of a currency in the IMS.[296]

The e-CNY, will most likely enhance the promotion of the RMB internationalization. Especially once the RMB becomes the third-largest currency in the world, when it comes to international reserves, pricing, and settlement. The e-CNY is currently still subject to testing and pilots. Cross-border e-commerce payments could present the next key scenario for the usage of the e-CNY, seeing that it is "natural and particularly easy to accept." Since the accession of the RMB in the IMF SDR basket, the RMB has increasingly been used in the facilitation of cross-border financial transactions. It can therefore be said that financial transactions are an important driving force behind the internationalization of the RMB, and FDI have promoted the international use of the RMB more than bonds and bank lending.[297] Once the e-CNY is readily used in cross-border payments, it will make cross-border RMB payments and settlements less costly and more efficient, therefore boosting the international use of the RMB.[298] Through cross-border payments the e-CNY can try to convert some of the USD denominated international trade transactions into RMB-denominated ones, therefore challenging the USD dominance over international finance and trade. If the e-CNY gain enough acceptance and market penetration in a separate region or jurisdiction, it is possible that a finance and trade system parallel to the USD-system can gain critical mass, allowing certain countries an alternative to the current global banking system and US sanctions.[299] International transactions in e-CNY would also aid China in fighting illegal financial flows through "controllable anonymity." The e-CNY gives Chinese authorities a tool to scrutinize transactions and if needed identify the counterparties.[300] However, this feature has been found, by the US, to be very problematic. Stating that international users of the e-CNY would be at risk of becoming a target of the Chinese repressive system[301] and that the e-CNY is merely a tool of China to facilitate its "digital authoritarianism."[302]

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[296] Zhou Lanxu, "E-Cny Use Set to Expand on PBOC Push," China Daily, April 8, 2023, https://www.chinadaily.com.cn/a/202304/08/WS6430c030a31057c47ebb8fd6.html.

[297] Chen Jia, "E-Cny Certain to Promote Renminbi's Internationalization," China Daily, July 29, 2021, https://global.chinadaily.com.cn/a/202107/29/WS610201faa310efa1bd66528b.html.

[298] Lanxu, "E-Cny Use Set to Expand on PBOC Push."

[299] Caudevilla, "Opinion - Internationalizing the RMB: How Will the Digital Yuan Be of Help?,"

[300] Eli MacKinnon, "Lexicon: 'controllable Anonymity' or 'Managed Anonymity' (可控匿名) and China's Digital Yuan," DigiChina, March 8, 2022, https://digichina.stanford.edu/work/lexicon-controllable-anonymity-or-managed-anonymity-and-chinas-digital-yuan/.

[301] Chimits, "The E-CNY Will Not Help the Yuan Displace the Dollar Any Time Soon."

[302] ""DIGITAL AUTHORITARIANISM: A GROWING THREAT" AT THE CARNEGIE ENDOWMENT FOR INTERNATIONAL PEACE," Office of the Director of National Intelligence, April 25, 2023, https://www.dni.gov/index.php/newsroom/speeches-interviews/speeches-interviews-2023/item/2375-digital-authoritarianism-a-growing-threat-at-the-carnegie-endowment-for-international-peace.

Moreover, the e-CNY is expected to have an impact on the reform of the IMS, aside from helping the promotion of RMB internationalization. However, this would require the international community to come to a consensus on the rules and standards for the use of sovereign digital currencies. Therefore, the PBoC has initiated active participation in international communications and exchange of the legal digital currency. The PBoC has stated that it will actively respond to initiatives of international organizations such as the G20, in order to help developing and improving cross-border payments, and research the applicability of CBDCs in cross border scenarios.[303] That said, the e-CNY alone will not instigate a large scale increase in the international use of the RMB. This seeing the closed capital account of china and the lack of full convertibility of the RMB; the under-developed state of the Chinese financial markets; and the fact that foreign users of the e-CNY will be subjected to monitoring of the Chinese authorities – something that many potential users may be hesitant to accept, unless pushed to do so by Western sanctions.[304]

Next to the ability of the cross-border use of e-CNY to facilitate lower transaction costs and more efficiency, international transactions in e-CNY would also benefit China in another way. The e-CNY would help protecting transacting parties from sanctions, especially from the long-arm jurisdiction of the US. This seeing that there is no real alternative to SWIFT, the monopolistic international interbank system that adheres to US sanctions, something where the US draws considerable power from. Any entity on the SDN can potentially be banned from SWIFT, making international transactions virtually impossible. The e-CNY could provide a safe alternative to SWIFT.[305] This feature of the e-CNY has therefore been a strong driver behind the support of China for the e-CNY, and has also been pressed by high-level Russian officials within the financial sector.[306] Seeing that China can and is allocating countries and economies that have been sanctioned by the west within its financial infrastructure, it is not unlikely that China will face more secondary sanctions from the US. That said, an action such as excluding Russia from SWIFT is very unlikely to happen, seeing the entrenchment of China in the international manufacturing and supply chain. Therefore banning China from SWIFT would cause catastrophic shockwaves through the

[303] Jia, "E-Cny Certain to Promote Renminbi's Internationalization."
[304] Hung Tran, "Internationalization of the RENMIBI via Bilateral Swap Lines," Atlantic Council, April 7, 2022, https://www.atlanticcouncil.org/blogs/econographics/internationalization-of-the-renmibi-via-bilateral-swap-lines/; Helen Warrell and Roula Khalaf, "UK Spy Chief Raises Fears over China's Digital Renminbi," Financial Times, December 11, 2021, https://www.ft.com/content/128d7139-15d6-4f4d-a247-fc9228a53ebd.
[305] Chimits, "The E-CNY Will Not Help the Yuan Displace the Dollar Any Time Soon."
[306] "Russia Plans to Use Digital Rouble in Settlements with China, Says Lawmaker," Reuters, September 26, 2022, https://www.reuters.com/markets/currencies/russia-plans-use-digital-rouble-settlements-with-china-says-lawmaker-2022-09-26/.

global economy, and essentially mean a hard decoupling with China from the West. Only the most extreme geopolitical conflict between the US and China would instigate this. Freezing USD-denominated assets of China would be less catastrophic than removing China from SWIFT, but the shocks it would create for the global economy would still be immense given the weight of China within the international economy. Freezing the FX holdings of China would majorly affect the ability of China to stabilize the exchange rate of the RMB and avert a currency crisis. This would quite possibly lead to tight capital controls in China to stabilize the RMB,[307] something that is very unfavorable for the internationalization of the RMB, as it is currently already a challenging factor for RMB internationalization.

The BRI and Regional Comprehensive Economic Partnership (RCEP) are the best possible candidate areas for China to internationalize the e-CNY. The BRI is currently a key program for China, it is therefore not hard to imagine how important the integration of the e-CNY along the BRI can become for China. The RCEP will help China to strengthen trade ties with neighboring countries. Moreover, China can leverage the agreement in order to facilitate cross-border adoption of the e-CNY to benefit, bankers, consumers, dealers, and industries in the region. Given its role as the larges offshore RMB center, Hong Kong can also play a critical role in aiding the internationalization of the RMB. This because it is at the forefront of the one country two systems principle and the expertise of Hong Kong in CBDCs through e-CNY tests for cross-border payments and projects such as the e-HKD and mBridge.[308] Something that should be noted however, is that even the e-CNY will probably not be able to completely eradicate problems associated with the acceptance of the RMB.

7.2 Theoretical considerations

The internationalization of the RMB is quite unique in comparison to how other international currencies have evolved, this lays in the fact that it is predominantly government policy that has facilitated its promotion. Despite most of the key RMB and e-CNY infrastructures have been planned out by the Chinese government, the adoption by foreign governments goes obviously paired with cooperation of these countries. Therefore, it can be stated that not only the Chinese government plays a significant role in the internationalization of the RMB, but foreign governments as well. Countries holding RMB reserves tend to be more receptive and have more RMB financial infrastructure. Moreover, countries with a more developed financial market tend to implement more policies of the RMB infrastructure. This may be

[307] Lee, "China (mainland) may move to limit impact of US financial weapons."
[308] Caudevilla, "Opinion - Internationalizing the RMB: How Will the Digital Yuan Be of Help?,"

reflective of the concern of governments regarding the competitiveness of the financial sector of the country, or demand from financial institutions that RMB be supported for domestic businesses, as can be argued from the case of Russia and its adoption of the RMB as reserve currency. Moreover, it is very clear that the rate of RMB internationalization is very dependent on the economic and political relations China has with other countries.[309] As can be seen from the divide in RMB adoption rate of countries with deep relations with China versus those that do not. Looking at data from 2021, there is a significant geographic disparity in the usage of RMB. What can be observed is the emergence of RMB usage in Asian countries such as Laos and Mongolia, and other developing and emerging markets such as Turkey, Argentine, and Chile. Countries that were sanctions by the US, such as Iran, also increasingly used RMB for transactions.[310] The idea of the relation between RMB infrastructure adoption and degree of relationship with China can further be solidified when cross-referencing the geographical distribution of BRI participants and members of CIPS. Cross-referencing this data also shows the correlation between RMB adoption and competitiveness of financial sectors of developing countries.[311] Based on this it is very important to recognize the impact and influence of foreign states and non-China related factors on the internationalization of the RMB. Despite the rise and fall theory being highly suggestive of China becoming the new major superpower and will therefore control the new global reserve currency, the economic developments of China suggest that its trajectory will set the rise of China apart from other historical experiences. Moreover, the emergence of the RMB of reserve currency will, in the case of China, be highly dependent on numerous factors, many of which are beyond its control.[312]

From a realist perspective, it is very logical for China to still have tight capital controls and a relatively underdeveloped financial market, because it enables the Chinese government to maintain control over its financial system and economy. This is an important aspect when it comes to maintaining the national power and sovereignty of China. By

[309] Hyoung-kyu Chey, Geun-Young Kim, and Dong Hyun Lee, "Which Foreign States Support the Global Use of the Chinese Renminbi? The International Political Economy of Currency Internationalisation," *The World Economy* 42, no. 8 (2019): 2403–26, https://doi.org/10.1111/twec.12794, p. 2422.
[310] Hector Perez-Saiz and Longmei Zhang, "Renminbi Usage in Cross-Border Payments: Regional Patterns and the Role of Swap Lines and Offshore Clearing Banks," *International Monetary Fund Working Paper* 77, (2023), pp. 8-9.
[311] "Financial Development Index Database," International Monetary Fund; "Countries of the Belt and Road Initiative (BRI)," Green Finance & Development Center, March, 2022, https://greenfdc.org/countries-of-the-belt-and-road-initiative-bri/; "CIPS worldwide participants," Cross-Border Interbank Payment System, May 11, 2023, https://www.cips.com.cn/en/index/index.html.
[312] Christopher A. McNally, "The Political Economic Logic of RMB Internationalization: A Study in Sino-Capitalism," *International Politics* 52, no. 6 (November 9, 2015): 704–23, https://doi.org/10.1057/ip.2015.15, pp. 718-719.

restricting the in- and outflow of capital, China can prevent any possible negative effects of foreign capital, such as economic instability or speculative bubbles. Moreover, tight capital controls also help in mitigating the chances of capital flight, something that can cause serious issues for the economic stability and national security of China. That said, in order to internationalize the RMB, China will need to liberalize its economy and financial markets. Liberalization can help the internationalization of the RMB through creating investor confidence and attract foreign capital, therefore promoting economic growth for China. Even though market liberalization seems to be a departure from the generally realist approach of China, it can still be argued that it falls in line with realism seeing that it will enable China to maintain national power and sovereignty. This through internationalization of the RMB and changing the current IMS so it will accommodate the economic and geopolitical goals associated with the RMB strategy of China.

8. Conclusion

Despite the economic miracle China has performed, the international status of the RMB, has never really gained ground, until recently. The internationalization of the RMB is definitely not a new phenomenon, but it really started to accelerate after the 2008-09 financial crisis and the accession of the RMB into the IMF SDR basket in 2016. The body of research into the internationalization has grown considerably over the past 10 years. That said, most studies cover the issue whether the RMB eventually will become a major international currency, or that the RMB will ultimately challenge the USD for the status as global reserve currency. This research falls largely within this presented body of literature but differs in its approach towards answering the research question: "*Why is China so active in developing the status of the Yuan; consequently the e-CNY"* Seeing the largely economical nature of the topic, very little research has employed theories other than economical ones, aside from the interdisciplinary theory of IPE, to interpret the internationalization of the RMB. This research highlights, through the usage of a mixed methods approach of qualitative deductive content analysis and descriptive quantitative analysis, in combination with the theories of IPE, Structural Realism, and Rise and Fall, that there is more to the internationalization of the RMB than just the economic dimension. This is also represented in the posed hypothesis: "*The efforts of China to promote the usage of RMB and e-CNY are part of a broader strategy to reduce the dependency of China on the USD while enhancing its geopolitical and economic influence. The digital nature of the e-CNY presents advantages over traditional* *currencies such as the USD that China can capitalize on, in competition with the USD, to achieve this goal."*

In order to guide the research several sub-questions have been posed. The research looked into the historical context behind the USD and its status of global reserve currency, and how current events such as the war in Ukraine and the internationalization of the RMB challenge this position. In line with this, the research also elaborated on the efforts of China behind the internationalization of the RMB and the development of the e-CNY. In order to examine the geopolitical aspect of the hypothesis the research looked into the motivations behind the RMB internationalization strategy and how this relates to the broader economic and geopolitical goals of China. To address the current state of the RMB internationalization, the research examined developments stemming from the US-China trade war and the war in Ukraine. Related to this, the research elaborated on the weaponization of the USD and further sanctions, and the possibility of China facing similar measures in the future. The research looked further into the e-CNY and its potential benefits for international transactions, thus creating leverage for China. Lastly, the research looked into the capability of the e-CNY to challenge current financial systems and the USD as global reserve currency. Given the expanding economic dominance of China and the current geopolitical tensions, research into the internationalization of the RMB and the role of the e-CNY within this strategy is particularly important and timely. The research adds to the development of a more comprehensive understanding of the evolving dynamics within the global financial landscape and the apparent changing balance of power in the IMS.

The USD became the global reserve currency after the establishment of the Bretton Woods Agreement and its associated institutions. This enabled the US to create an international financial system adherent to the US and USD. Since then the US has enjoyed its "exorbitant privilege" of controlling the global reserve currency. However, cyclical crises and the US exporting its inflation to the rest of the world have caused doubts with nations whether or not the current USD dominated IMS still holds. This has been underlined by the weaponization of the USD in the sanctions measures against Russia. This is currently leading to changes in the global economic landscape. The internationalization of the RMB traces back to the 2000s, with the initial goals of reducing the reliance of China on the USD while enhancing the economic and geopolitical influence of China. In recent years, the efforts of China to internationalize the RMB have been accelerated through the BRI and economic digitalization, with the e-CNY being developed as a potential tool to aid the RMB internationalization into the status of major reserve currency.

The main drivers of China behind the RMB internationalization strategy are to increase the market thickness and usability of the RMB, reducing its dependence on the USD, while increasing the influence of China within the current IMS and facilitate the establishment of a global RMB based financial infrastructure and associated networks. The current state of the RMB internationalization is increasing, however it still has a long way to go before research should even consider that the RMB will challenge the USD. This has to do with numerous factors such as Chinese capital controls, financial market development, attitude towards Chinese financial products, transparency, and the influence of foreign governments and non-Chinese actors. The US has expressed, out of its own political and economic interests, concerns towards the internationalization of the RMB, and sees it as a threat for the USD dominated IMS. This response could lead to heightened tensions between the US and China, as showcased in the US-China trade war, which is pushing China to instigate closer economic and financial ties with other countries. There is a high probability of China getting sanctions from the US in reaction to the internationalization of the RMB. This is a matter of the China maintaining its internationalization by also incorporating countries and economies that are currently under sanction of the West in its RMB financial structure.

Lastly, the benefits of the e-CNY for China and those within its financial structure include lower transaction costs, more transparency, and the ability to conduct business outside of the current USD dominated global financial infrastructure. Therefore highly reducing any potential impact of the USD and bypassing US sanctions. This in turn, challenges the current IMS, and increases the economic and geopolitical influence of China. Because it will find allies in countries that have been shunned by the West, and those getting increasingly concerned by the abuse of the US over the current global financial system.

The theory of IPE argues that the international economic system is shaped through the power relations between states and that economic policies are used by states in order to attain their interests. The idea behind the RMB and e-CNY becoming an alternative to the USD is showing of the desire of China to have more economic and financial autonomy away from the current US stipulated IMS. That said, RMB internationalization and China advancing its economic and geopolitical goals are two sides of the same coin. This seeing that without China gaining a wider influence it also cannot push for the facilitation of a broader and large scale use of the RMB. Similarly, and from a Realism perspective, the efforts of China to reduce its dependency on the USD comes from its primary motivation to secure itself and accommodate its rising economic power status. Moreover, the rise and fall theory argues that major powers display a cycles of rising and falling and that two key factors within these cycles are geopolitical and economic considerations. What indeed can be observed is the rise of the RMB is in competition with the USD. However this but not based on the principle of a currency war. It is rather the result of a natural occurrence that falls in line with the rise and fall theory. Moreover, the e-CNY is showing of the technological advancements China has over the US, something that correlates to the rise segment of the rise and fall cycles. Based on the research findings and the interconnection of the theories between the findings, the research supports the hypothesis. The hypothesis consequently also forms the answer to the research question to a great extent.

The internalization of the RMB paired with the development of the e-CNY is part of the broader economic and geopolitical strategy of China. Through reduction of its reliance on the USD, China aspires to increase its influence in the global economy and mitigate the effects of external shocks, such as US sanctions. Moreover, the rise of China as an economic power calls for the need of a currency supportive of its increasing global trade and investment. Therefore, it can be argued that the promotion of the RMB and development of the e-CNY are strategic moves of China to increase its economic and geopolitical power.

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10. Appendix: Key Developments RMB Internationalization

Segment I: Promoting the use of RMB

- **Facilitation of RMB trade settlements**
  - Promote the use of RMB as a settlement currency for cross-border trade transactions.
  - Simplify procedures and reduce transaction costs for businesses using RMB settlements.
  - Encourage cross-border RMB trade settlements through preferential policies and incentives.
- **Financial reforms and capital market opening**
  - Launching RMB Banking Services: Encourage domestic and foreign banks to offer RMB services to meet the increasing demand for RMB.
  - Liberalizing Bank Deposit and Lending Rates: Promote the marketization of interest rates to improve the efficiency of capital allocation and promote the development of the bond market.
  - Cultivating Bond Markets: Support the development of a diverse and efficient bond market to provide more investment channels for domestic and foreign investors.
  - Facilitating RMB Inflows and Outflows: Allow more channels for RMB inflows and outflows to increase the flexibility of cross-border capital flows.
  - Opening the Foreign Exchange Market: Further, liberalize the foreign exchange market to increase market-driven pricing and enhance risk management.
- **Domestic securities investment by qualified foreign institutional investor regulation (QFII)**
  - Encourage foreign investors to participate in China's capital markets through the QFII scheme, which grants qualified foreign institutions access to the domestic securities market of China.

Segment II: Building global RMB financial infrastructure and networks

- **Establishing infrastructure and mechanisms to facilitate a wider use of RMB**
  - Building a Global Network of RMB Trading and Clearing Centers: Establish RMB clearing centers in key financial centers to facilitate cross-border RMB transactions.
  - Starting Direct RMB Trading: Encourage the use of RMB for direct trading with other currencies to reduce foreign exchange costs and risks.
  - Expanding a Network of Bilateral Swap Agreements (BSAs): Sign more BSAs with other countries to provide liquidity support and promote the use of RMB in trade and investment.
  - Launching the China International Payment System (CIPS): Develop a secure and efficient payment system to support cross-border RMB transactions.
- **Expand FTA networks**
  - Promote the use of RMB in free trade agreements (FTAs) with other countries to facilitate trade and investment.
- **Launch Belt and Road Initiative (BRI)**
  - Encourage the use of RMB in countries participating in the BRI to support the development of trade and investment.
- **Offshore RMB bond market**
  - Promote the development of offshore RMB bond markets to provide more investment channels for global investors.

Segment III: Accelerating momentum for the new IMS

- **Expand regional financial structure**
  - The Chiang Mai Initiative (CMI): Establish a regional currency swap agreement among ASEAN+3 countries to provide liquidity support.
  - Chiang Mai Initiative Multilateralization (CMIM): Multilateralize the CMI to increase the size and scope of the currency swap arrangement.
- **Launching development banks**
  - Asian Infrastructure Investment Bank (AIIB): Establish a new development bank to finance infrastructure projects in Asia and promote regional economic integration.
  - BRICS New Development Bank: Establish a new development bank among BRICS countries to finance infrastructure projects in emerging markets.
  - Inter-SCO Development Bank: Establish a new development bank among SCO countries to finance infrastructure projects in Central Asia.
- **Inclusion of RMB in the SDR basket**
  - Encourage the inclusion of RMB in the SDR basket to increase the international status and recognition of RMB.