Beyond the usual motifs of China-Africa co-operation in infrastructural development and extractive industries, the forthcoming inclusion of the Chinese Renminbi (RMB) into the International Monetary Fund’s (IMF) Special Drawing Rights Basket on 1st October 2016 potentially harkens new types of financial co-operation between China and Africa. Including the RMB into the global basket of reserve currencies is a natural corollary to China’s expanding scale of trade and investment flows globally, and Africa is a region with rising uptake of the RMB given the depth of China-Africa mutual interests. However, these new modes of financial co-operation also depend on China’s own complicated relationship between RMB internationalisation, capital account liberalisation and exchange rates regimes. Resultantly, these complications can affect the speed of RMB uptake in Africa, such as the non-granting of Qualified Foreign Institutional Investor (QFII) status, while exerting spillovers effects to China-Africa outbound Foreign Direct Investment (FDI).

Renminbi as preferred trade settlement currency in Africa

With 2015 China-Africa trade hitting US$ 180 billion, African firms stand to gain from greater RMB usage for trade settlement of receipts and payments with their Chinese counterparts. For example, a 2013 HSBC poll suggested that Chinese exporters may offer up to 5 per cent discount if [African] buyers invoice in RMB. Additionally, African firms that adopt RMB for trade settlement can circumvent issues of foreign currency mismatch risk i.e. forex risks associated with converting local African currencies into RMB via the USD. While triangular transactions between non-USD currencies via the USD normally occurs given relatively low transaction costs, this is detrimental for oil-dependent African countries - Angola and Nigeria amongst others - who constantly face USD liquidity shortages given USD capital outflows in light of declining oil prices. Direct RMB trade settlements also reduces costs of currency hedging in the case of future contracts, where the agreement between a Chinese and African firm for products at a predetermined price at a specific future time do not incur extra costs of having to anticipate USD/RMB fluctuations.

To date, SWIFT data shows that RMB usage in South Africa increased by 65 per cent in 2014-2015, a remarkable result following declining Chinese demand for African commodities since its economic slowdown. This trend follows up from the first successful African RMB trade financing loan by the Bank of China (BoC) in January 2010, the establishment of Africa's first RMB clearing house through the BoC in Johannesburg in July 2015, the opening of individual RMB-denominated accounts by South Africa's Standard Bank which is 20 per cent owned by the Industrial and Commercial Bank of China and the state-owned National Bank of Kenya which also opened a clearing house facility in Nairobi in 2015. Regionally, the Common Market for Eastern and Southern Africa (COMESA) clearing house included the RMB in August 2016 as a settlement currency through the Regional Payment and Settlement System. With the COMESA looking to foster greater financial integration and intra-regional trade, this could also potentially increase RMB ‘recycling’ in the region through larger African cross-border RMB flows and larger amounts of RMB-denominated African deposits.
**African foreign reserves, debt management and the RMB**

Various African central banks such as Tanzania, Nigeria and South Africa have diversified their foreign exchange reserves to include RMB reserves. For example, the South African Reserve Bank signed an agreement in 2013 with the People’s Bank of China (PBC) for a RMB 9 billion investment in China’s interbank bond market. South Africa was also the sole African bookrunner in a 2012 ‘dim-sum’ bond issue by China Development Bank where African central banks collectively bought RMB 500 million worth of these bonds. Greater RMB usage has also been purportedly linked to debt management, as shown by Zimbabwe’s adoption of the RMB as legal tender even as China plans to offer debt forgiveness of up to US$ 40 million.

African central banks have also indicated their interest in issuing ‘panda’ bonds, or RMB-denominated bonds sold in Chinese onshore markets by non-Chinese issuers. Intuitively, this could facilitate African debt repayment of Chinese loans, currently valued at US$ 14 billion in 2014. These bonds could also help meet financing requirements for African infrastructural demands, especially projects with huge levels of Chinese contractors. Additionally, panda bonds incur lower borrowing costs than generic Eurobonds, or international bonds denominated in foreign currencies other than the issuer’s own. Where countries like Nigeria are ‘shopping around for the best [bond] deal’ to plunge their fiscal deficit, these countries hope that panda bonds would allow them to avoid offering double-digit coupon rates that characterise a huge portion of African sovereign Eurobonds. This is due to the average yield decline in Chinese bonds of a 150 basis points between 2014-2015 as well as different risks appetites associated with African countries’ problematic credit ratings.

**Complications for further RMB usage in Africa**

How African countries fund and respond to their China import driven trade deficit will affect African RMB usage, whether through policies such as protectionist measures or economic diversification through developments in tertiary industries. Additionally, African countries might also consider using ‘Samurai’ bonds, the Yen-denominated equivalent of panda bonds. This is especially relevant given the anticipated increase in Japan-Africa linkages following the latest Tokyo International Conference of Africa’s Development. Panda bonds are also fraught with perceived uncertainty over the operations of Chinese rating agencies, accountancy standards and exemption criteria as compared to more familiar Western standards. African central banks may also be wary of RMB liquidity, since central banks value the autonomy to adjust their reserves composition at low bid-ask spreads with relative ease. Having said that, ongoing currency swaps agreements such as those between China-South Africa and China-Nigeria assuages liquidity concerns since they ensure a steady supply of RMB even in situations of financial emergency.

Moreover, it remains to be seen if African RMB usage moves beyond trade settlement. After all, RMB internationalisation must be located within the context of China’s capital account liberalisation efforts. This line of logic states that RMB internationalisation places significant pressure for greater capital account liberalisation given the growing difficulties of intervening in capital flows or exchange rate regimes. The ‘gradualist’ approach of Chinese financial reforms imply that future policy tweaks can be expected in light of increases in total volume of transactions or crisis situations such as massive short selling. One prominent example is that of Chinese onshore bond and equity markets, where foreign investors can gain (limited) access via the QFII scheme. Thus far, Africa’s only QFII institution is South Africa’s Prescient Investment Management, and developments in Africa’s own financial landscape would also impact RMB adoption in the continent.

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