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DP-38-2019

Who Will Lead the World Economy?
US vs. EU vs. China
USD vs. EUR vs. RMB

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Who Will Lead the World Economy?*
US vs. EU vs. China - USD vs. EUR vs. RMB

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Abstract

When we talk about leadership, we also talk about rivalry… and 2018 was undoubtedly a particularly emblematic year of rivalry, especially between the United States and China, and to some extent, between the United States and Europe. Power, leadership and domination (three different concepts) can be expressed in many ways, but this article will focus on two major concerns: the power / leadership of the country and the power / leadership of the currency. This discussion paper addresses therefore two major questions:

> "The world is neither unipolar, multipolar, nor chaotic—it is all three at the same time"
>
> *Joseph S. Nye, Jr., The Future of Power (2011)*

Question # 1: will China and Europe compete with the US as the world's leading power? We compare countries as regard hard power, soft power and smart power. The conclusion is indisputable: the US is still

**Part of this Discussion Paper has been presented at the conference "New Horizons for the World Economy" organised by "Le Cercle des Economistes / Economic Society of Singapore / Lee Kuan Yew School of Public Policy, National University of Singapore", held in Singapore in March 14-15, 2019.*

Part of this Discussion Paper has been presented at the 20th Seoul International Finance Forum entitled "The Age of Uncertainty, Questions for the Future Finance", organised by The Financial News and Oaktree, held in Seoul – South Korea in April 24-25, 2019.

an effective hegemonic power, being the only complete power on earth. No doubt some countries are on the map of power now (China, Russia, India for example), but the gap between the US and these countries is still quite significant, although declining. European countries are still on top of the list of powers, but Europe is not (not yet?) considered as a block. China will continue to reduce the gap with the US and should increase the gap with other emerging countries too.

> "When it is obvious that the goal cannot be reached, don't adjust the goals, adjust the action steps"
>
> *Confucius*

Question # 2: will the US dollar cease to be the "unique" international currency? Can the euro and the yuan take all or part of the attributes and functions of the international currency that the dollar today fills? When one compares the three currencies (USD, EUR and RMB), it is evident that the journey to an international currency for the Chinese currency is still quite long and complex (economically, financially, and politically). The full convertibility of the RMB, the openness of the capital account and the elimination of capital controls, the development of liquid, transparent and efficient fixed income markets would definitely be perceived as essential improvements... but patience is still required. Any big bang would be economically damageable and is not politically plausible. On the other hand, the euro is already an international currency, competing with the USD in some areas. It is nevertheless more a regional currency than a real international one (which is not the case of the USD), but it still has leeway to progress... should EU accept a consolidation of the Euro area institutional, economic and governance set-ups.

Keywords: US dollar, Euro, Renminbi, international currency, hard power, soft power, multipolar world

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Executive summary

1. **Power is a multifaceted concept**. **Hard power** has usually two components; economic and military forces. The **soft power** of a country comes primarily from three sources: its culture (when it is attractive to others), its political values such as democracy and human rights (when it lives up to them), and its policies (when they are seen as legitimate because they are framed with some humility and awareness of others' interests). **Smart power** is the combination of the two, and is usually considered as the optimal way to use power.

2. The US are by far the country with the strongest hard power. GDP, Development index, banks, corporates and brands value, military forces… all these indicators highlight the strength of the US. **Europe needs to push integration further to be perceived as a more credible contender.**

3. European countries are usually considered as the strongest soft power (UK, France, Germany). Some surveys also highlight the US decline in this respect. How a government behaves at home, in international institutions (consulting others and multilateralism) and in foreign policy can affect others by the influence of its example. In some areas, D. Trump has reversed attractive American policies and power indicators point out the consequences. However, America is more than either Trump or the government: unlike hard-power criteria, many soft-power resources do not depend on the government, and the US decline is more in line with global sentiment than it is with fact. The country is still unrivalled in higher education, cultural production, and technological innovation… and keeps the leadership in most studies.

4. Whatever the method used, the US remain the power of reference, which is not a big surprise. But depending on the criteria, the list of the top 10 countries may vary considerably: it is a confirmation of the multipolarity of the world, of the diversity of competitors, of the potentially evolving nature of this ranking, and of the progress of emerging countries. China appears as the major contender to the US, the country gaining ground year after year much quicker than any other "emerging" country. The gap with the US is gradually receding, and China is undoubtedly the future rival of the US. The US do have to share power with other countries. So far, the US is by far the most complete power and still represents an effective hegemonic power.

5. Leadership is not the same as domination. There have always been degrees of leadership and degrees of influence during the American century. As J. Nye recalled, the US never had complete control, and with slightly less preponderance and a much more complex world, the US will need to make smart strategic choices both at home and abroad if it wishes to maintain its position.

6. US vs. China vs. Europe, what role for India? Many questions resurface and the debate is open. Some consider that the West's two-century epoch as global powerhouse is at an end. A new world order, with China and India as the strongest economies, dawns (K. Mahbubani). On the other hand, some (like J. Nye) consider that, "contrary to those who proclaim the 21st century is the Chinese century, we have not entered a post-American world. But the continuation of the American century will not look like it did in the 20th century. The complexity represented by the rise of other countries as well as the increased role of non-state actors will make it more difficult for anyone to wield influence and organize action". "Analysts should stop using clichés about unipolarity and multipolarity. They will have to live with both in different issues at the same time". "The American century is likely to continue for a number of decades at the very least, but it will look very different from how it did".

7. Power is nevertheless no more in the hands of one country and we already live in a multipolar world. It explains why the US considers China as **the** rival… and why the tone of the US administration became more aggressive in the past years. It is expected to last for long.

8. To gain ground further, Europe needs to be perceived as a block, as an entity, and more than a group of countries. Despite that, the European countries are individually ranked at the top of the lists, especially Germany and France (and Italy and Spain to a lesser extend). European countries have high ranking on most criteria, but are significantly lagging behind the US should we refer to hard power.

9. In terms of GDP, China will not be the unique rival to the US. The so-called emerging economies will continue to be the world's growth engine: in 1995, based on GDP at PPPs, E7 countries (China, India, Brazil, Russia, Indonesia, Mexico and Turkey) represented half the size of G7 countries (United States, Japan, Germany, France, United Kingdom, Canada and Italy). They were roughly same size in 2015… but they could be double the size of G7 in 2050 and represent 50% of world GDP. China would remain the largest economy in the world, accounting for around 20% of world GDP in 2050. Mexico should be larger than the UK and Germany by 2050. The EU27 share (without UK due to the Brexit) of world GDP should be down to less than 10% by 2050, and become smaller than India (the second largest country). Six of the seven largest economies in the world could be emerging markets by that time.

10. As regard the international currency, additional efforts have to be done to complete the multipolar world. **If China wants the yuan to become an international currency, some prerequisites are to be met**: capital market liberalisation, capital account openness, capital controls abandoned, full convertibility of the currency, etc. China is still far from completing these prerequisites.

11. To reinforce the international role of the Euro, Europe has to consolidate and improve the euro-area institutional set-up. Some examples: the completion of the **European Banking union**, progress on **capital markets union**, better **credit quality of "peripheral"** sovereign bonds. The issuance of a **common "federal" bond**, with a role similar to that played by Treasuries in the US, would significantly increase the international role of the euro. Progress in the **set-up of euro-area economic policy**, in its fiscal and structural components, and **a more united, and thus more effective, external and defence policy** would favour greater international use of the euro. **Speaking with one voice** more regularly on critical issues would be a "plus" for the euro, no doubt.

12. US foreign policy might be determinant for the accumulation / decumulation of USD in FX reserves. Military alliances boost the share of a currency in the partner's foreign reserve holdings by about 30 percentage points. In other words, any U.S. disengagement from global geopolitical affairs (withdrawal from international organisations, end of "policeman of the world", abandonment (or reduction) of the protection policy (umbrella) vis-à-vis some countries would have impact on FX reserves and on the use of USD: such a scenario would inevitably favour additional diversification of FX reserves, and it would also imply a rise in US Bond yields.

13. In the long term, the international status of the USD should diminish depending on 4 conditions: i) the pursuit of FX reserves diversification by Asian central banks into alternative currencies and into gold; ii) the emergence of the RMB as a contender of the USD, alongside with the Euro; iii) the difficulty of the US to attract international savings eternally (as they have since the 1970s) to finance structural twin deficits; iv) the foreign policy of the US administration.

Introduction

When we talk about leadership, we also talk about rivalry… and 2018 was undoubtedly a particularly emblematic year of rivalry, especially between the United States and China, and to some extent, between the US and Europe.

The background of China-US (trade) conflicts is well-identified:

- **First, the US released the 'Status of Non-Market Economy' report on China questioning China's economic system**. Several reasons were mentioned (J. Ha (2018)):
  - # "The government controls fundamental economic factors like land and other resources either directly or indirectly, and state-owned enterprises have control over many economic resources through administrative monopoly.
  - # Pricing mechanism is still limited in many sectors.
  - # Effectiveness of protection on private property rights is still insufficient.
  - # The government is taking various industrial policies as measures to realize diversified goals such as technology upgrade".
- **Second, China promoted in 2015 the "Made in China 2025" program** (MIC 2025), described as largely inspired by Industry 4.0's German Plan. The "Made in China 2025" plan no longer specifically supports high-tech industries (robotics, biotechnologies), but includes among the priority sectors more traditional industries (marine, train, agriculture). The position of foreign companies in this plan remains unclear. At the same time, the scope of industrial activities related to national security is not explicit.
- **Third, the US called China its "strategic rival" in its National Security Strategy report in December 2017**. A good introduction to the current trade disputes of D. Trump. The target is to promote free, fair and reciprocal economic relationships. "*The United States distinguishes between economic competition with countries that follow fair and free market principles and competition with those that act with little regard for those principles*". More recently, Mike Pence added: "*China, as we've observed, is using debt diplomacy and unfair trade practices to expand its influence*". Mike Pence's recent speech at the Hudson Institute (4 Oct. 2018) was even worse: he referred to "*a theft of American intellectual property*", to "*predatory practice of forced transfers of technology*", to "*interference in American democracy*"…

- **The rivalry between the United States and Europe is older and different**: the political and military alliance does not prevent a strong economic and sometimes political rivalry. One of the recent culminations of this rivalry was undoubtedly, economically, the creation of the euro area and the creation of a currency, the euro, likely to compete with the dollar on some of the functions of an international currency. Power, leadership and domination (three different concepts) **can be expressed in many ways, but this article will focus on two major forms of leadership: the power / leadership of the country and the power / leadership of the currency.**

Two major questions:

- **Will China and Europe compete with the United States as the world's leading power?** It will be appropriate to answer first the following question: what is a power? And then to compare these countries as regard the different forms of power.
- **Will the US dollar cease to be the "unique" international reference currency?** Can the euro and the yuan take all or part of the attributes and functions of the international currency that the dollar fills today?

These two questions are perfectly linked: power and alliances determine to some extend the magnitude of the international role of currencies… for ages!

I. US vs. Europe vs. China: how to measure power (of States)?

1.1. What is a power? Hard power vs. soft power vs. smart power

In the past, a country with a large army (or fleet), possessing technology (weapons) and large steel production capacity (for weapons purposes) was considered a power. It refers to the ability of a country to impose its will on other countries using military and economic means. The components of this power include military power, economic power, demographic power and political power. This is what be called "**hard power**". Considering that the US alone represent close to 45% of world military expenditures, it still the biggest representative of hard power.

However, hard power is no longer enough: **power is a composite concept** that must consider economic and financial, technical, human and political factors (stability, cohesion, influence...).

"Soft power" has gained ground in the past decades. The concept was proposed by Joseph Nye in 1990 in reaction to the analysts who concluded to the decline of US power. He claimed that the US power was not declining since the concept of power was no longer the same and had to be reconsidered.

Joseph Nye argues that the United States had a new comparative advantage giving the possibility to play a growing role in the future: "*the ability to seduce and persuade other states without having to use their force or the threat*". This new form of power does not operate in the mode of coercion (the carrot and the stick), but on that of persuasion. As Nye developed, soft power (or the power of persuasion) relies on intangible resources such as "*the image or positive reputation of a state, its prestige (often its economic or military performance), the degree of openness of its society, its communication skills, the exemplarity of its behaviour (of its internal policies but also of the substance and style of its foreign policy), the attractiveness of its culture, its ideas (religious, political, economic, philosophical), its scientific and technological influence*"...

Power is a guarantee of success, but it is of little use if the country is not able to make the best of it. "**Smart power"**, a combination of hard and soft might appear optimal.

Table 1: hard power, soft power, smart power			
Type of power	**Hard power**		**Soft power**
Components	Economic power	Military power	Power of cooptation and soft power
Targets	Encourage Buy Constrain	Deter Constrain Submit	Seduce Attract Encourage
Means	Investments Subsidies Sanctions	Threat Violence Coercion	Popular culture
Combination	**Smart power**		

Source: F. Louis (2014)

1.2. Hard power indicators: from military forces to brands and GDP...

Plenty of indicators represent part of hard power. Let's focus on six of them: i) (young) population, ii) GDP, iii) human development, iv) corporates and brands, v) banks, vi) firepower index. What do these power indicators tell us?

1. (young) Population as a power indicator

A young population is a source of dynamism, optimism, capacity to innovate, to consume, to take risks... and to be a military if needed. Such an indicator is usually part of any composite index of power. According to this criterion (percentage of population below 15 or even below 25 for example), neither the US or China or Europe are in the top 150 countries list. On the opposite, 25 African countries are in the top 25. Close to 50% of people living in Niger (ranked # 1), for example, are below 15, vs. 25.4% for the world, 18.8% in the US (# 157), 18.6% in France (# 158), 17.4% in the UK (# 168), 15.4% in Spain (# 197), 13.7% in Italy (# 217), 13.0% in Japan (# 222) and 12.8% in Germany (# 224). Major differences within BRICS: 28.3% in South Africa (# 80), 27.7% in India (# 86), 22.8% in Brazil (# 128), 17.1% in China (# 176), 16.9% in Russia (# 177). The gap in population with Africa is expected to rise further. In the 1950s, the population of Europe was twice large than Africa. At present, it is precisely the reverse. In 30 years, the population in Africa should be 3.5 times larger than Europe. Note that this represent theoretically a "plus" for Africa, but it might represent a major risk for Europe should immigration continues at strong pace.

2.GDP as a power indicator

In terms of the economy alone, the United States is ahead of China, Japan, Germany, the United Kingdom, France, India and Brazil. **GDP** is a useful indicator as it gives resources to the military, research, domination and influence in the world... the 4 BRIC are now among the 12 largest economic powerhouses in the world. **The centre of gravity of the world has changed dramatically in recent years... and this is just the beginning!**

In the early 1980s, Europe and the US weighed 15% of the world's population and more than 50% of world GDP. Today, these shares are respectively 10% and one third. In 20 years, they will be even weaker.

The BRICS countries now represent nearly 45% of the world's population (3 billion people); they alone account for nearly 25% of global nominal GDP, and they have contributed to more than 50% of global GDP growth over the last decade.

Table 2: Nominal GDP and population in the world: the new powers

	GDP 2017	Population 2017	GDP 1980 (% — World)	GDP 2017 (% — Word)	Population 1980 (% — World)	Population 2017 (% — World)
United States	**19 485**	**326**	**25.7%**	**24.3%**	**5.1%**	**4.3%%**
China	**12 015**	**1 386**	**2.7%**	**15.0%**	**22.1%**	**18.4%**
EU	**17 325**	**512**	**34.2%**	**21.6%**	**10.5%**	**6.8%**
Germany	*3 701*	*83*	*7.6%*	*4.6%*	*1.8%*	*1.1%*
France	*2 588*	*67*	*6.3%*	*3.2%*	*1.2%*	*0.9%*
Italy	*1 939*	*61*	*4.3%*	*2.4%*	*1.3%*	*0.8%*
Spain	*1 314*	*47*	*2.1%*	*1.6%*	*0.8%*	*0.6%*
UK	*2 628*	*66*	*5.4%*	*3.3%*	*1.3%*	*0.9%*
BRICS	**18 599**	**3 136**	**11.0%**	**23.2%**	**44.3%**	**41.6%**
Brazil	*2 065*	*209*	*1.3%*	*2.6%*	*2.7%*	*2.8%*
Russia	*1 578*	*144*	*4.5%*	*2.0%*	*3.1%*	*1.9%*
India	*2 602*	*1 339*	*1.7%*	*3.3%*	*15.7%*	*17.8%*
China	*12 015*	*1 386*	*2.7%*	*15.0%*	*22.1%*	*18.4%*
South Africa	*349*	*57*	*0.7%*	*0.4%*	*0.7%*	*0.8%*
Japan	**4 873**	**127**	**9.9%**	**6.1%**	**2.6%**	**1.7%**
South Korea	**1 540**	**51**	**0.6%**	**1.9%**	**0.9%**	**0.7%**
WORLD	**80 051**	**7 530**	**100%**	**100%**	**100%**	**100%**

Sources: IMF, World Bank, Amundi Research

When comparing countries according to the **PPP GDP** criterion, the share of emerging countries is even stronger.

- **China has already overtaken the US and the EU**
- **The BRICS represent one third of the world GDP, like the sum of US — EU, but with a population 4 times larger.**

Table 3:
PPP GDP and population in the world: new powers

	PPP GDP 2017	Population 2017	PPP GDP 1980 (% — World)	PPP GDP 2017 (% — World)	Population 1980 (% — World)	Population 2017 (% — World)
United States	**19 485**	**326**	**21.6%**	**15.3%**	**5.1%**	**4.3%%**
China	**23 208**	**1 386**	**2.3%**	**18.2%**	**22.1%**	**18.4%**
EU	**21 069**	**512**	**29.9%**	**16.5%**	**10.5%**	**6.8%**
Germany	*4 199*	*83*	*6.6%*	*3.3%*	*1.8%*	*1.1%*
France	*2 856*	*67*	*4.3%*	*2.2%*	*1.2%*	*0.9%*
Italy	*2 317*	*61*	*4.6%*	*1.8%*	*1.3%*	*0.8%*
Spain	*1 778*	*47*	*2.2%*	*1.4%*	*0.8%*	*0.6%*
UK	*2 925*	*66*	*3.8%*	*2.3%*	*1.3%*	*0.9%*
BRICS	**40 713**	**3 136**	**NA**	**31.9%**	**44.3%**	**41.6%**
Brazil	*3 248*	*209*	*4.4%*	*2.5%*	*2.7%*	*2.8%*
Russia	*4 016*	*144*	*NA*	*3.2%*	*3.1%*	*1.9%*
India	*9 474*	*1 339*	*2.9%*	*7.4%*	*15.7%*	*17.8%*
China	*23 208*	*1 386*	*2.3%*	*18.2%*	*22.1%*	*18.4%*
South Africa	*767*	*57*	*1.0%*	*0.6%*	*0.7%*	*0.8%*
Japan	**5 443**	**127**	**7.9%**	**4.3%**	**2.6%**	**1.7%**
South Korea	**2 035**	**51**	**0.6%**	**1.6%**	**0.9%**	**0.7%**
WORLD	**127 489**	**7 530**	**100%**	**100%**	**100%**	**100%**

Sources: IMF, World Bank, Amundi Research

It is therefore obvious that, **in economic terms, emerging countries, including the BRICS, represent an increasingly important power.**

3.Human development a power indicator

As regard the 2018 *HDI index*, US is listed # 13, China # 116, while 20 European are in the top 30 countries (of which 12 Eurozone countries). The 2018 *inequality adjusted HDI index* gives a similar picture: 21 European countries in the top 30 (of which 12 Eurozone countries). The US are sliding to the ranking # 25, though. Unsurprisingly, none of the BRICS countries is ranked in the top 50 list (HDI or HDI adjusted)... so far.

Insert 1: The Human Development Index

I.D.H. is calculated by the United Nations Development Programme (P.N.U.D.). Between 0 and 1: The closer it is to 1, the higher the country's level of development. The I.D.H. allows for the preparation of an annual country ranking. It is calculated by the average of three quantifying indices, respectively (source: UNDP):

Health - longevity(measured by life expectancy at birth), which indirectly measures the satisfaction of essential material needs such as access to healthy nutrition, safe drinking water, decent housing, hygiene and medical care;
Knowledge or level of education. It is measured by the average length of schooling for adults over 25 years of age and the expected length of schooling for children of school age. It reflects the satisfaction of immaterial needs such as the ability to participate in decision making in the workplace or in society;
Standard of living. It is measured by the logarithm of gross per capita income in purchasing power parity terms. It covers those elements of the quality of life that are not described by the first two indices such as mobility or access to culture.

HDI makes it possible to classify countries according to the development veal:

The "**advanced countries**": These countries generally have HDI in excess of 0.8. This group comprises two types of countries: The "developed market economies" (PDEM) of the second half of the 20th century (United States, Western Europe, Japan), and the old "new industrialised countries" in Asia (South Korea, Taiwan, Singapore...).
"**Economies in transition**": These are the former communist countries of Eastern Europe such as Russia, Ukraine, Poland...; they are sometimes considered as developed countries, and sometimes as emerging countries.
"**Developing Countries**": In general, they have an HDI of less than 0.8 and bring together several types of countries: New industrialised and emerging countries (China, Brazil, India, Mexico, etc.), oil exporting countries (Saudi Arabia, Qatar, etc.), intermediate countries (North African countries), and LDCs, "least developed countries", sub Saharan African countries in the majority (according to UNCTAD, 32 of the 48 LDCs are African countries). It should be noted that some 30 developing countries now have HDI in excess of 0.8.

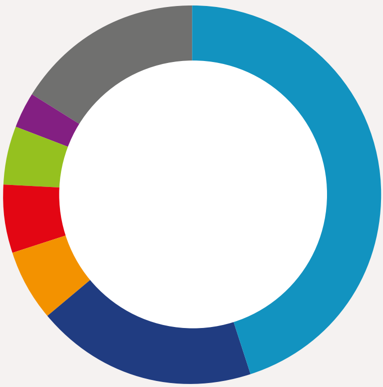
4.Corporates and brands as power indicators

Economic power is linked to the power of corporates. A simple way of looking at this power is to pay attention to the ranking of brands.

- **Strongest brand analysis: as regard the top 10 brand strength analysis,** 6 are US companies (Deloitte (#3), McDonalds (#5), Intel (#6), Neutrogena (#8), Coca-Cola (#9) and PWC (#10)), 2 are European (Ferrari (#1) and Rolex (#7)), 1 is Russian (Sberbank (#2)), 1 is Chinese (#4).

- **Brand value analysis:** the US are leading largely. The US companies represent 45% of the Top500 brand value. China comes second (19%) followed by Japan, Germany, France and UK.

Graph 1:
Top 500 Brand value: US vs. China vs. Europe



Country	Brand Value (USD bn)	% of total
United States	3124.2	45.4%
China	1307.4	19.0%
Japan	418.8	6.1%
Germany	401.0	5.8%
France	312.2	4.5%
United Kingdom	227.8	3.3%
Others	1087.4	15.8%
Total	**6878.1**	**100%**

Source: Brand Finance (2019)

In the top 10 most valuable brands, 7 are US companies (Amazon, Apple, Google and Microsoft (top 4), AT&T, Facebook (ranked # 6 and 7), and Verizon (#9), 2 are Chinese companies (ICBC (#8) and China Construction Bank (#10)) and there is 1 Korean company (Samsung (#5)). In the top 100 most valuable brands, there are 47 US (26 in the top 50), 21 Chinese (15 in the top 50), 9 German, 7 Japanese, 4 from UK (0 in the top 50), 3 South Korean, 2 Spanish, 2 French, 1 Indian (#86), 1 Canadian (#96), 1 Swiss, 1 Dutch, 1 Swedish. There are 20 European companies in total in the top 100 most valuable brands.

Three additional comments:

- The US companies are the most represented in this ranking (close to 50%);
- Chinese companies, largely absent 10 years ago, have quickly emerged and represent at present one-fifth of top500 brand value;
- European companies represent also around one-fifth.

5. Banks as a power indicator

- *By total assets*, 18 Chinese banks are listed in the top 100 banks in the world, vs. 12 US, 8 Japanese, 6 French, 6 from UK, 5 Canadian, 5 German, 5 Spanish... Around 40 European banks, of which 30 from Eurozone countries are listed in the top 100. There are 5 Asian banks in the top 5, with four Chinese at the top (Industrial and Commercial Bank of China ICBC is ranked #1, China Construction Bank Corporation CIBC # 2, Agricultural Bank of China ABC # 3 and Bank of China BoC # 4). Mitsubishi UFJ Financial Group (#4) complete the top 5 banks. 2 US banks and 2 French banks are listed in the top 10. Note that this ranking is based upon assets as reported and is not adjusted for different accounting treatments: the US use US GAAP (as opposed to IFRS), which only reports the net derivative position in most cases; as a consequence, US banks exhibit fewer derivative assets than comparable non-US banks. Adjusted under IFRS rules, US banks would have a better ranking.

- *By market capitalisation*, 11 US banks are listed in the top 50 (4 in the top 10), with 9 Chinese (5 in the top 10), 5 from UK (of which 1 in the top 10) and 4 Japanese banks. 12 banks from the BRIC and 7 from the Eurozone (2 French banks, 2 Spanish, 1 Italian, 1 Dutch and 1 German also appear in the top 50 banks by market capitalisation.

6.Military force as a power indicator

Table 4:
Military expenditures (in USD Bln and in % of GDP)

Country	Spending (USD Bln)	Ranking	Spending (% of GDP)	Ranking
United States	610.0	1	3.1	3
China	228.0	2	1.9	9
Saudi Arabia	69.4	3	10.0	1
Russia	66.3	4	4.3	2
India	63.9	5	2.5	5
France	57.8	6	2.3	6
United Kingdom	47.2	7	1.8	10
Japan	45.4	8	0.9	15
Germany	44.3	9	1.2	14
South Korea	39.2	10	2.6	4
Brazil	29.3	11	1.4	12
Italy	29.2	12	1.5	11
Australia	27.5	13	2.0	8
Canada	20.6	14	1.3	13
Turkey	18.2	15	2.2	7
World	1739.0		2.2	

Source: SIPRI (2018)

The Global Firepower Index (GFP) highlights the military force only. It places the United States in first place, followed by Russia, China, India, France, the United Kingdom, Japan and Turkey. The GFP ranking is based on the potential ability of each country to make war on land, in the air and on the sea with conventional weapons. The results incorporate values related to resources, finance and geography, with over 55 different factors that make up the final ranking. 3 of the 4 BRIC countries are among the top 4 (Brazil ranks 14th).

1.3. Soft power indices: US and Europe at the top

As J. Nye recalled (2018)), "*a country's soft power comes primarily from three sources: its culture (when it is attractive to others), its political values such as democracy and human rights (when it lives up to them), and its policies (when they are seen as legitimate because they are framed with some humility and awareness of others' interests).* The success of soft power lies on the country's reputation within the international community, and on the flow of information between countries. In other words, soft power is associated with the rise of globalization and with the neoliberal international relations theory. Soft power is a descriptive rather than a normative concept, and like any form of power, it can be utilised for good and bad purposes.

The first attempt to measure soft power was created and published by the Institute for Government and the media company Monocle in 2010. The "**IfG-Monocle Soft Power Index**" combines statistical metrics and subjective panel scores to measure the soft power of countries. Five sub-indices include culture, diplomacy, business/innovation, education, and government. According to this index, France and Germany are at the top of the list, while the US is ranked # 9 and China # 19.

The "**Elcano Global Presence Report**" (Elcano Royal Institute) scores the soft presence of 110 countries. France and Germany are ranked # 4 and # 5, Spain and Italy # 9 and # 10. The US and China are # 1 and # 2, according to Elcano. The Elcano Soft Presence Index comprises several dimensions: culture, migration, sports, education, development cooperation.... Whatever the dimension, USA is ranked # 1 and China is ranked # 2 (except on military forces, where Russia is ranked # 2). Almost all African countries are dramatically lagging behind.

The "**Soft Power 30**", is a ranking of countries' soft power produced and published by the media company Portland since 2015. It is probably the most complete and comprehensive soft power indicator to date (see insert). The ranking is based on "*the quality of a country's political institutions, the extent of their cultural appeal, the strength of their diplomatic network, the global reputation of their higher education system, the attractiveness of their economic model, and a country's digital engagement with the world.*" According to this index, UK, France and Germany are tops of the list, while the US is now ranked # 4, due to the volatility and divisiveness of its government and president Trump over the past two years. "*How a government behaves at home (for example, protecting a free press), in international institutions (consulting others and multilateralism) and in foreign policy (promoting development and human rights) can affect others by the influence of its example. In all of these areas, Trump has reversed attractive American policies" (J. Nye (2018))*. Fortunately, America is more than either Trump or the government: unlike hard-power criteria (military forces; for example), many soft-power resources do not depend on the government. As Portland notices, "*the US decline is more in line with global sentiment than it is with fact. The country is still unrivalled in higher education, cultural production, and technological innovation*". Note that the gap in soft power between the top 4 countries, at the opposite of hard power indicators, is very limited: the 2018 score is 80.55 for UK, 80.14 for France, 78.87 for Germany, and 77.80 for the US. China (#27) scores 51.85).

Table 5: Soft power indicators

Ranking	Portland's The Soft Power 30 Report 2018	Monocle's Soft Power Survey 2018/19	Elcano's Soft Presence Report 2018
1	United Kingdom	France	United States
2	France	Germany	China
3	Germany	Japan	United Kingdom
4	United States	Canada	Germany
5	Japan	Switzerland	France
6	Canada	United Kingdom	Japan
7	Switzerland	Sweden	Canada
8	Sweden	Australia	Russia
9	Netherlands	United States	Spain
10	Australia	Portugal	Italy
11	Denmark	New Zealand	South Korea
12	Italy	Italy	Australia
13	Norway	Spain	Netherlands
14	Spain	Denmark	Turkey
15	Finland	South Korea	Saudi Arabia
16	Belgium	Netherlands	India
17	Austria	Finland	Sweden
18	New Zealand	Norway	Brazil
19	Ireland	China	South Africa
20	South Korea	Belgium	Switzerland
21	Singapore	Singapore	Belgium

Ranking	Portland's The Soft Power 30 Report 2018	Monocle's Soft Power Survey 2018/19	Elcano's Soft Presence Report 2018
22	Portugal	Ireland	Austria
23	Greece	Austria	Poland
24	Poland	India	Denmark
25	Hungary	Brazil	Malaysia
26	Czech Republic	-	UAE
27	China	-	Mexico
28	Russia	-	Nigeria
29	Brazil	-	Egypt
30	Argentina	-	Thailand

Sources: Portland (2018), Elcano (2018) and Monocle (2018)

Insert 2 : Portland's Soft Power 30

The Soft Power 30 methodology gives the clearest picture to date of global soft power:

- # The index contains a digital component, developed in collaboration with Facebook, working with their data-science team to create and collect new metrics on countries' digital diplomacy;
- # The index contains international polling from 25 different countries that provide coverage of every major region of the world;
- # More than 75 metrics are normalised into comparable data calculating a single score for each country that allow for an overall ranking of global soft power resources.

The index is made of 6 components:

- # **Digital**: A country's digital infrastructure and its capabilities in digital diplomacy;
- # **Culture**: The global reach and appeal of a nation's cultural outputs, both pop-culture and high-culture;
- # **Enterprise:** The attractiveness of a country's economic model, business friendliness, and capacity for innovation;
- # **Education**: The level of human capital in a country, contribution to scholarship, and attractiveness to international students;
- # **Engagement**: The strength of a country's diplomatic network and its contribution to global engagement and development;
- # **Government**: Commitment to freedom, human rights, and democracy, and the quality of political institutions.

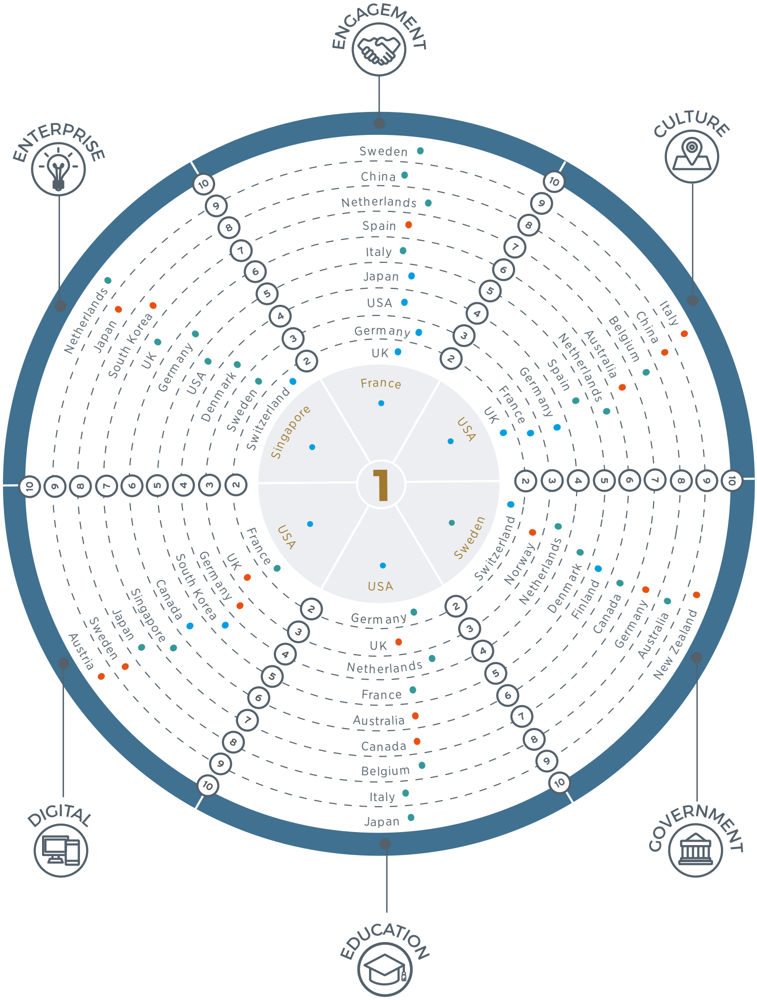
Sources: Portland

Table 6:
Soft power indicators – Portland report by sub-indices

Ranking	Global	Digital	Culture	Enterprise	Engagement	Education	Government
1	UK	USA	USA	Singapore	France	USA	USA
2	France	France	UK	Switzerland	UK	Germany	Germany
3	Germany	UK	France	Sweden	Germany	UK	UK
4	USA	Germany	Germany	Denmark	USA	Netherlands	Netherlands
5	Japan	South Korea	Spain	USA	Japan	France	France
6	Canada	Canada	Netherlands	Germany	Italy	Australia	Australia
7	Switzerland	Singapore	Australia	UK	Spain	Canada	Canada
8	Sweden	Japan	Belgium	South Korea	Netherlands	Belgium	Belgium
9	Netherlands	Sweden	China	Japan	China	Italy	Italy
10	Australia	Austria	Italy	Netherlands	Sweden	Japan	Japan
11	Denmark	Hungary	South Korea	Finland	Canada	Sweden	Sweden
12	Italy	Australia	Canada	New Zeal.	Belgium	Denmark	Denmark
13	Norway	Russia	Sweden	Norway	Russia	China	China
14	Spain	Netherlands	Japan	Ireland	South Korea	Switzerland	Switzerland
15	Finland	Norway	Switzerland	Austria	Austria	South Korea	South Korea
16	Belgium	Spain	Norway	Australia	Switzerland	Spain	Spain
17	Austria	Belgium	Austria	Canada	Norway	Austria	Austria
18	New Zeal.	Denmark	Ireland	France	Australia	Russia	Russia
19	Ireland	Poland	Brazil	Belgium	Brazil	Finland	Finland
20	South Korea	New Zeal.	Denmark	Czech Rep.	Finland	New Zeal.	New Zeal.
21	Singapore	Argentina	Russia	Hungary	Denmark	Norway	Norway
22	Portugal	Finland	Poland	China	Greece	Poland	Poland
23	Greece	Switzerland	Finland	Portugal	Portugal	Singapore	Singapore
24	Poland	Italy	Greece	Poland	Poland	Ireland	Ireland
25	Hungary	Ireland	Portugal	Spain	Ireland	Greece	Greece
26	Czech Rep.	Czech Rep.	Argentina	Russia	Hungary	Portugal	Portugal
27	China	Portugal	Czech Rep.	Italy	New Zeal.	Brazil	Brazil
28	Russia	Brazil	Singapore	Greece	Argentina	Czech Rep.	Czech Rep.
29	Brazil	Greece	New Zeal.	Brazil	Czech Rep.	Hungary	Hungary
30	Argentina	China	Hungary	Argentina	Singapore	Argentina	Argentina

Source: Portland / Facebook / USC Centre on Public Diplomacy (2018)

Graph 2:
Soft power indicators – Portland report by sub-indices



Source: Portland / Facebook / USC Centre on Public Diplomacy (2018)

To sum up, all 3 indicators do not point to the same direction. While US and European countries always have similar and excellent rankings, China is perceived differently, still growing, but in the top 30 only. However, China is now ranked soft power # 4 in Asia, with Japan #1, South Korea #2, Singapore #3, Taiwan #5, India #8 and Indonesia #9 (Portland / Facebook / USC Centre on Public Diplomacy (2018)).

1.4. Hard power + Soft power = Smart power: the power indicators

When combining both hard power and soft power, we obtain smart power. The table 7 reports the ranking of countries as regard Elcano's 2018 report and Portland's 2018 report. The **Global presence report**, which focuses on economic and military presence, is released by Elcano Royal Institute. It is not massively different from its soft power index: it also ranks US and China at the first two places, and UK, Germany and France are in the top 5. The **global ranking of power** of the French magazine "*Conflits*" (and especially Jean-Marc Holz) incorporates many indicators related to soft power, technology, wealth, cohesion of the country, armed forces, economic power. The United States still ranks first, followed by China, then Russia, France, the United Kingdom, Germany, Canada and Japan. Turkey only appears in 29th place, very far down in contribution to the index of firepower (9th rank). China and Russia rank among the top three powers.

These two surveys rank the US and China at the first two places (with a huge gap between these two countries – table 7), and UK, Germany and France are in the top 5 (losing ground gradually to China).

Table 7: Smart power indicators – Conflits' and Elcano's indices

Ranking	Power indicator of the "Conflicts" review (2018) (Perfect score = 100)		Elcano's Global Presence Report 2017	
1	United States	(76,3599)	United States	(2494.1)
2	China	(45,4717)	China	(840.7)
3	Russia	(33,0167)	United Kingdom	(636.7)
4	France	(32,1555)	Germany	(618.5)
5	United Kingdom	(31,4668)	France	(531.6)
6	Germany	(30,6573)	Japan	(518.1)
7	Canada	(27,7734)	Russia	(390.3)
8	Japan	(26,4160)	Canada	(337.4)
9	Australia	(24,4833)	Netherlands	(297.3)
10	Switzerland	(23,2957)	Italy	(271.1)
11	India	(22,7172)	Spain	(233.7)
12	Italy	(21,7936)	South Korea	(225.8)
13	South Korea	(20,7942)	India	(202.4)
14	Sweden	(20,7942)	Switzerland	(190.4)
15	Spain	(20,0723)	Australia	(185.5)
16	Taiwan	(18,3132)	Belgium	(171.5)
17	Israel	(17,6439)	Singapore	(127.7)
18	Malaysia	(17,1550)	Sweden	(126.4)
19	Saudi Arabia	(17,1387)	Brazil	(118.9)

Ranking	Power indicator of the "Conflicts" review (2018) (Perfect score = 100)		Elcano's Global Presence Report 2017	
20	Brazil	(16,7679)	Saudi Arabia	(113.3)
21	Indonesia	(16,1665)	UAE	(106.7)
22	Poland	(16,1012)	Turkey	(106.1)
23	Qatar	(16,0309)	Mexico	(99.5)
24	Vietnam	(15,3580)	Ireland	(96.2)
25	Mexico	(15,3574)	Thailand	(95.2)
26	South Africa	(15,3469)	Austria	(89.4)
27	Philippines	(15,0910)	Malaysia	(82.2)
28	Iran	(14,6287)	Denmark	(76.7)
29	Turkey	(14,6185)	South Africa	(74.8)
30	Argentina	(14,3906)	Norway	(70.1)

Sources: Conflits Magazine (2018); Elcano Royal Institute (2018)

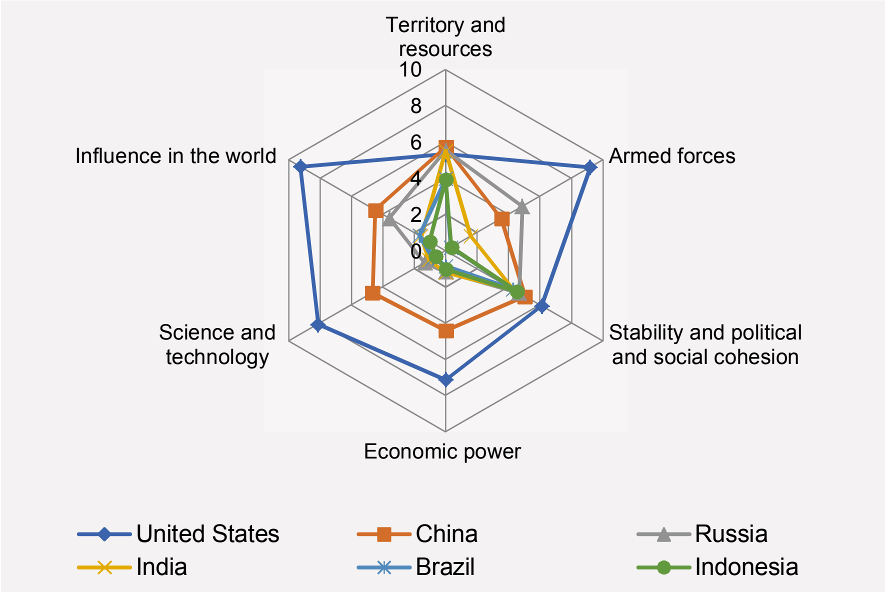
The graphs (cobwebs) below represent the power of some countries, advanced and emerging countries, with regard to the six main groups of indicators constituting the "global ranking of power" index:

- **Territory and resources** (axis 1): area, maritime domain, geographical location, arable land, renewable freshwater resources, hydrocarbon resources, population, growth of human resource...
- **Armed forces** (axis 2): military expenditure, nuclear forces, number of bases abroad, aircraft carriers, number of soldiers and their experience, conventional weaponry, military satellites...
- **Stability and political and social cohesion** (axis 3): inequalities, homicide rate, corruption, patriotism, risks of internal conflict...
- **Economic power** (axis 4): wealth creation (GDP, multinationals, insurance companies, banks, sovereign wealth funds...), competitiveness, dynamism (start-ups, GDP growth...), presence abroad, economic independence (foreign exchange reserves, energy independence...), currency (share in global reserves and international payments...)
- **Science and technology** (axis 5): volume of R & D expenditures, supercomputers, number of reputed universities in the scientific and technical fields, number of patents filed, scientific articles published, degree of automation of the industry, index of innovation...
- And finally **influence in the world** (axis 6): diplomacy (permanent member of the UN security council, networks of embassies and consulates, arms exports...), culture (global multimedia firms, exports of cultural goods, influence of language, number of foreign students...), prestige (medals at the Olympic Games, world championship organizations...), culture (museums...)...

They clearly show the superior power of the United States (whose surface is twice as large as that of its two rivals), and it also shows that this power is complete (a superiority on 5 of the 6 axes). This shows, if need be, the gap that still exists between the United States and China / European countries, for example, but also to what extent Russia remains an "incomplete" power. Three emerging countries only appear in the top 10.

If we compare the emerging countries, we see big differences in terms of power, including the domination of China, compared with Russia and India. And few EMG countries exert any power over more than 2 criteria.

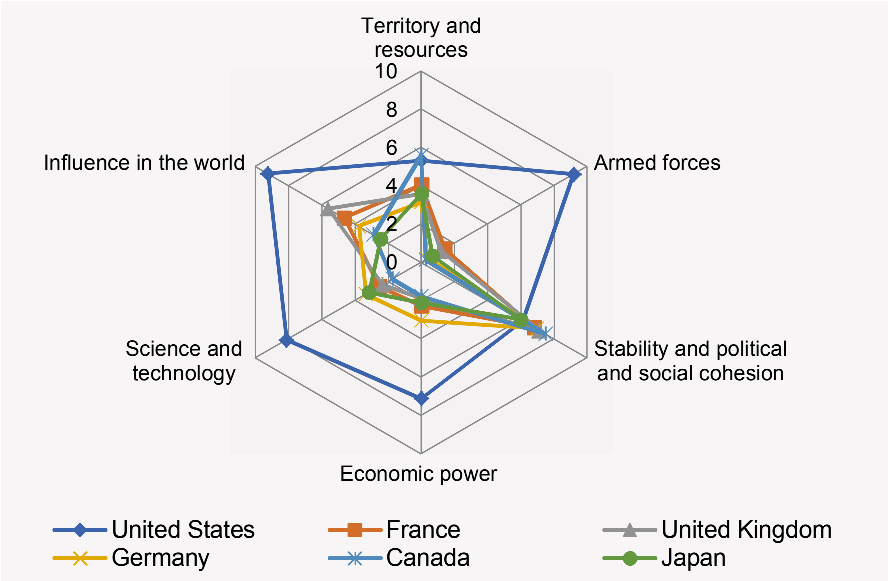
Graph 3: Power indicators
United States, BRIC and Indonesia



Source: Amundi Research

And **if we compare advanced countries**, no doubt: the US is by far the most complete power... while it is difficult to aggregate European countries as a homogeneous entity.

Graph 4: Power indicators
United States, Japan, Canada and Europe



Source: Amundi Research

In other words, **whatever the method used, the United States remains the power of reference**, which is not a big surprise. But depending on the criteria, the list of the top 10 countries may vary considerably: it is a confirmation of the multipolarity of the world, of the diversity of competitors, of the potentially evolving nature of this ranking, and of the progress of emerging countries.

1.5. Conclusion

To sum up, power is a concept with variable geometry, it is an absolute concept but also relative. It is also in many cases a legacy of history. We can now distinguish 10 different kind of power ((see also Ch. Chabert (2018)):

1. **The hegemonic power** exerted by the United States, present – and often dominant – on all the characteristics of power: army, technology, population, raw materials, diplomacy, wealth...
2. **The rival power** that China has been waging for a few years, not as complete and strong as the US, but growing rapidly.
3. **The old powers**, especially Europe: still highly significant, but losing ground to China, like the US. Japan, an old power, remains essentially an economic power. Spain, Portugal, the Netherlands, England and France have exercised over the centuries a strong power

on a global scale, linked to their fleet, their capacity for exploration, their empires and their colonization policies, their diplomacy, their military power … but these countries (even under the auspices of the European Union) find it difficult to express their power against the hegemony of the United States: heterogeneity of the European Union (currently 28 countries), the rise of the BRICS, especially China… How to transform wealth into power? This is the big question for Europe and especially for Germany. In 1900, Europe accounted for a quarter of the world's population. By 2060, it may account for just 6%—and almost a third of these will be more than 65 years old. Europe does face severe demographic problems, but the size of a population is not highly correlated with power, and "predictions of Europe's downfall have a long history of failing to materialize." (J. Nye).

4. **The continent — states** (Canada, Russia, Australia) have a significant influence capacity. Russia also has a military weight that strengthens this capacity.
5. **The city – States** such as Singapore, with economic power and local influence.
6. **Energy powers** have a weight that varies considerably depending on the price of commodities such as gas and oil, and their power is intermittent.
7. **The former powers of the Middle East**, whose ambitions go far beyond their means, and which are exerted notably by an important military investment and a systematic report of forces. Turkey is probably the best example now.
8. **Large emerging countries** such as India, Brazil, Mexico, Indonesia…, with large territories or a large population or a specific strategic positioning… In short, very different countries and disparate expressions of power.
9. **Soft power** is mainly located in highly developed countries, with a discreet but very homogeneous influence (strong social cohesion). Among the countries having soft power only, one can recognize Scandinavia and Switzerland. Soft power can also be promoted by big countries and strong powers depending on the topic and depending on the timing.
10. **Asian newcomers** (Philippines, Korea, Vietnam, …), not yet real powers, but the recent economic performances have more recently put them "on the geopolitical – economic map".

K. Mahbubani goes further, when he considers *that "the West's two-century epoch as global powerhouse is at an end. A new world order, with China and India as the strongest economies, dawns*". J. Nye considers that, *"contrary to those who proclaim the 21st century is the Chinese century, we have not entered* *a post-American world. But the continuation of the American century will not look like it did in the 20th century. The complexity represented by the rise of other countries as well as the increased role of non-state actors will make it more difficult for anyone to wield influence and organize action*". "*Analysts should stop using clichés about unipolarity and multipolarity. They will have to live with both in different issues at the same time*". "*The American century is likely to continue for a number of decades at the very least, but it will look very different from how it did*".

So, it clearly appears that it is far from the time when only two or three countries (or even one) represented power / hyper power. **The dominant countries have not lost their power, they are "simply" forced to share it now**... and we see rising many emerging countries, which justify their surge into the power indicators... These indicators are now essential should we want to apprehend these countries correctly (discrimination, selection, risk analysis...).

As B. Coeuré noted as regard monetary policy, this shift in global power might mean "*a shift in global governance, which has contributed to the belief that the US may be more exposed to the risk that the monetary power of others is not used in its best interests, or is even used against it*". Rivalry is not supposed to recede soon, the least one can say.

In terms of GDP, China will not be the unique rival to the US. With an average annual growth at 7%, world GDP would double every decade. In other words, by 2050, it is quite sure that the world economy will more than double by 2050, should we exclude a major and global catastrophe or a full trade war, which is not our scenario (Ithurbide (2018)). The so-called emerging economies will continue to be the world's growth engine: in 1995, E7 countries (China, India, Brazil, Russia, Indonesia, Mexico and Turkey) represented half the size of G7 countries (United States, Japan, Germany, France, United Kingdom, Canada and Italy). They were roughly same size in 2015... but they could be double the size of G7 in 2050 and represent 50% of world GDP. China would remain the largest economy in the world, accounting for around 20% of world GDP in 2050, and according to PwC (2017), based on GDP at PPPs, "*India would be in second place and Indonesia in fourth place. Mexico could be larger than the UK and Germany by 2050 and six of the seven largest economies in the world could be emerging markets by that time (see table 8). The EU27 share (without UK due to the Brexit) of world GDP could be down to less than 10% by 2050, smaller than India*".

Table 8:
Emerging markets will dominate the world's economy in 2050 (E7 vs. G7 GDP at PPPs)

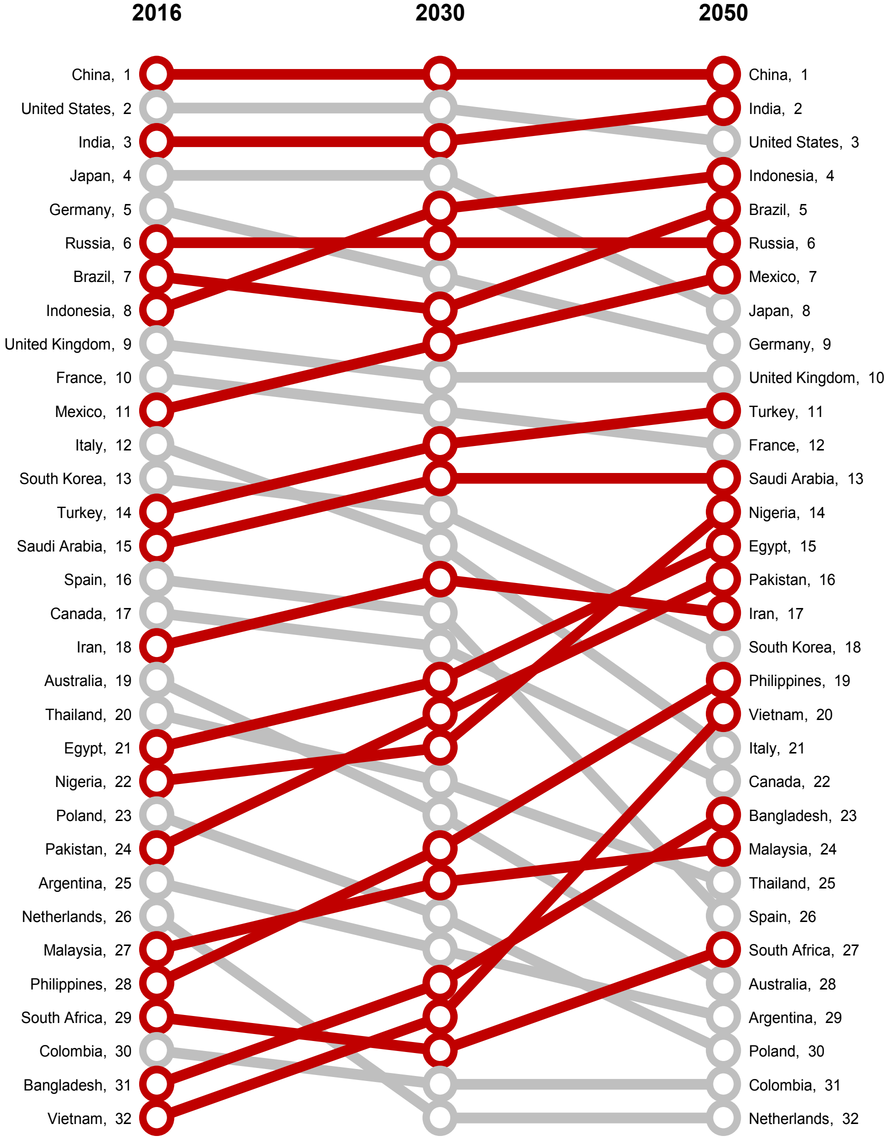
	World's ranking in 2016	World's ranking in 2050	
China	1	1	**China**
United States	2	2	**India**
India	3	3	**United States**
Japan	4	4	**Indonesia**
Germany	5	5	**Brazil**
Russia	6	6	**Russia**
Brazil	7	7	**Mexico**
Indonesia	8	8	**Japan**
United Kingdom	9	9	**Germany**
France	10	10	**United Kingdom**
Mexico	11	11	**Turkey**
Italy	12	12	**France**
Turkey	14	21	**Italy**
Canada	17	22	**Canada**

Sources: IMF for 2016 and PwC projections for 2050

E7 economies **G7 economies**

The following graph shows, if need be, the shift in economic power. The ranking of all advanced countries - without exception - should be lower in 2050 than it is today. Japan and Germany are down 4 rows, Spain 10, Australia 9 and Italy and Canada 5. Britain and France would "limit damage" and lose respectively only one and two rows. For emerging countries, the reality is more mixed: some - the vast majority of them - progress, and others decline again... in favour of other emerging countries. In other words, the dynamics of the emerging countries is different between the countries, which argues well for the diversity of the profiles. Indonesia and Mexico would win 4 rows, Nigeria 8, the Philippines 9, Vietnam 12... while Argentina would lose 4 rows and Poland 7 (which should nevertheless be, among the countries of the European Union, the one with the strongest rate of growth).

Graph 5:
Projected GDP rankings (at PPPs)



Sources: IMF for 2016 figures, PwC projections for 2030 and 2050

II. USD vs. EUR vs. RMB: where do we stand? What perspectives?

The emergence of an international currency is a long process, and it is a competitive process.

2.1. What does history tell us about international currencies?

History recalls three major conclusions:

1. **Several international currencies can coexist…** an interesting lesson for both the euro and the RMB:
   - Before 1914 the pound sterling dominated, but the French franc and the German mark each accounted for 20%-25% of international reserves and international transactions.
   - In the 1920s, the GBP and the US dollar shared this role evenly.
2. **The emergence of a new international currency occurs only if a severe shock undermines the confidence in the existing international currency (here, the USD) and its attractiveness**. **Another interesting lesson for the RMB or the euro: stability / predictability are key**.
   In the 1970s, it was the case: the decision of major central banks to refuse to defend the dollar further on FX markets, the two devaluations of the US dollar and the end of the Bretton Woods system seriously undermined the confidence in the USD. As a consequence, the Deutsche–Mark, and to a lesser extent the Swiss Franc, the GBP and the French Franc emerged in FX reserves while the USD also lost ground in cross border trade.
3. **Despite pressures on the international currency, diversification may not last: an international currency absolutely needs liquid markets.** For example, despite two devaluations, thanks to its liquidity and to the absence of any real contender having liquid and depth markets, the USD had regained all its losses less than two decades later… **Another interesting lesson for the yuan and for the euro: liquidity is key.** Note that the lack of liquidity in China come from the size, depth, transparency and access to the financial markets… while the liquidity problem in Europe comes from the excessive segmentation of financial markets.

2.2. A quick refresher on international currencies

Before assessing the current situation, we should explain what an international currency is. Its **four main characteristics** are:

- **Liquidity**: its market must be liquid. The euro and the dollar are very liquid. Not the case for the yuan so far.

- "**Acceptability**": the currency must be accepted everywhere. Undoubtedly, the lack of full convertibility of the yuan is a drawback.
- **Stability**: it is a complex concept given that currencies fluctuate by pair. But here "stability" refers to the economic situation of the country, to its structural imbalances... In that field, the yuan is gaining ground, while the PBoC has decided to change its FX policy towards more stability.
- "**Predictability**" it is also a complex concept that refers to the country's ability – or will – to manage its currency. Regarding exchange rates, the United States tend to have a more "laissez-faire" attitude than Europe and, more recently, China.

Table 9:
International functions of currencies

Functions of money	Private use	Public use
Unit of account	Invoice and quotation currency	Pegging currency
Medium of exchange	Payment and vehicle currency	Intervention currency
Store of value	Investment and financing currency	Reserve currency

Besides, an international currency has **four different functions**:

- A **reserve currency**: the emergence of new international currencies (the EUR in the the past 20 years, the RMB for the next 20 years) has favoured the diversification of international reserves. This trend might be pushed further with any structural weakness of the USD. It has not been the case in the 1970-1980's due to the absence of any challenger to the US dollar. Any rise in the euro or yuan to challenge the USD international role will certainly and ultimately force the United States to alter its FX policy.
- An **intervention currency**: from the start, the euro has always been a true intervention currency as it is the currency of a highly representative group of countries. The convertibility of the yuan and the increase of the yuan in FX reserves all over the world (or in Asia at least) are two prerequisites for the Chinese currency to become an intervention currency.
- A **settlement currency**: the true value of an international currency is determined by its ability to establish itself in third-party trade.
- A **reference currency**, especially for debt (private bonds and sovereign bonds) and commodities.

2.3. Why China or Europe should look for being home of an international currency? An international currency offers several advantages to the country:

- First, thanks to the billing process, **the internationalisation of the currency gives the country's exporters / importers the possibility to limit exchange rate risk and even to transfer the risk to the foreign customers / providers**. Thanks to the internationalisation, the domestic capital markets expands much quicker than foreign markets, a strong advantage for domestic entities.
- Second, **it allows domestic firms and financial institutions to access international financial markets without incurring exchange rate risk and to borrow more cheaply and on a larger scale than they can at home**.
- Third, **it benefits to the domestic economy, thanks to a larger and more profitable financial sector, able to better serve the domestic non-financial sector**.
- Fourth, **currency internationalisation will allow the country's government to finance its budget deficit by issuing domestic currency debt on international markets, and not by issuing in foreign currency denominated instruments**. As a consequence, at the opposite of numerous countries, internationalization of the currency may allow the government to finance current account deficits without drawing on its reserves.
- Last but not least, **history recalls that it allows the country to adopt benign neglect attitude for its own currency**, forcing economic partners to protect FX rates. The US is certainly a good example of this *laissez-faire*.

2.4. Why countries (such as Japan) never wanted to internationalise their own currency?

An international currency may represent **some dangers** for the economy:

- First, **with an international currency, there is a good chance the country's public debt to be in the hands of foreign investors**. As a consequence, periods of high volatility and depreciation of the currency are inevitable, Mistrust may also generate financial crises... This is even worse for countries having relatively small — and vulnerable — financial markets compared to the size of their economy (it is not the case for the US or the Eurozone).
- Second, **the country cannot control capital flows anymore**. Currency internationalisation usually moves in tandem with the absence (reduction) of capital controls, which limits the capacity of the central bank to control domestic interest rates. No doubt Chinese officials have that in mind...

2.5. How to internationalise its own currency: the prerequisites

Many factors determine the share of a currency in international functions: reserve currency, payment currency, intervention currency, reference currency, investment and financing currency, pegging currency.

An international currency is used and held beyond the borders of the issuing currency, for transactions with the country's residents, but more importantly for transactions between non-residents. In other words, an international currency is expected to be largely used instead of the national currencies of the parties directly involved in an international transaction (purchase of goods, services or financial assets).

What does theory tell us about the prerequisites for an international currency to emerge? Several criteria are to be met, and they show how far China is from having an international currency (Efstathiou – Papadia (2018)):

- **Size and liquidity:** to become an international currency, the size of the economy (in terms of GDP, volume of trade…) is important. Large and liquid markets reduce transaction costs and attract participants (positive for both vehicle and investment/financing functions – see table 5). A large supply of debt matter for the choice of the safe asset (which reduces the cost of borrowing via the liquidity premium) and, as a consequence, for the investment/financing and reserve functions.
- **Sustainability of debt:** good fiscal situation will impact the choice of the safe asset.
- **Political will and central bank's behaviour to promote the international use of the currency**. Japan never accepted to do it.
- **Stability:** financial stability of the issuing country comparing with the other countries is also critical to enhance the store-of-value role.
- **The removal of obstacles to the free movement of capital**: full convertibility of the currency, openness of the capital account.

As B. Coeuré mentions, "*most of these factors change softly, slowly… and they thus explain better long-term phenomena than short and medium-term changes in the use of international currencies. Financial stability, or rather financial instability, is the only factor that can change quickly enough to cause relatively fast changes to the shares of different currencies*".

2.6. Is the yuan on track to become an international currency?

First, a quick refresher on the rationale behind the decision to develop an international currency**.** China decided to accelerate the internationalisation of the RMB in the late 2000s, for 5 major (official and non-official) reasons:

- **To align the role of the currency with the size of China in the world economy;**

- **To allow Chinese corporates to reduce their dependence on the US dollar** and also to reduce FX cost and risk;
- **To reduce the accumulation of FX reserves;**
- **To develop a fixed-income market to attract foreign investors… and a way to finance reforms;**
- **To introduce additional and external pressures towards a necessary financial liberalisation**. In the same way, the entry of China into the WTO in 2001 kick-started the reforms of country's state-owned commercial banks.

At the same time, the euro was created, and many experts started to consider that the euro and the yuan would compete with the dollar in the long run for the status of international currency.

Second, some comments on the journey to an international currency. The process of internationalisation is a long process, and several conditions are to be met before concluding that a currency plays an international role. P. Kenen (2011) pointed out 7 conditions, which fully apply now to China:

- First, the government must **remove all restrictions** on the freedom of any entity, domestic or foreign, **to buy or sell its country's currency**.
- Second, **domestic firms must be able to invoice some, if not all, of their exports in their country's currency, and foreign firms must be likewise able to invoice their exports in that country's currency**, whether to the country itself or to third countries.
- Third, foreign firms, financial institutions, official institutions and individuals must be **able to hold the country's currency and financial instruments denominated in it**, in amounts that they deem useful and prudent.
- Fourth, **foreign firms and financial institutions**, including official institutions, **must be able to issue marketable instruments in the country's currency**.
- Fifth, **the issuing country's own financial institutions and non-financial firms must be able to issue on foreign markets instruments denominated in their country's own currency**.
- Sixth, international financial institutions, such as the World Bank and regional development banks, must be able to issue debt instruments in a country's market and to use its currency in their financial operations.
- Lastly, **the currency must be included in the "currency baskets" of other countries**, which they use in governing their own exchange rate policies.

Third, some figures on the current status. As regard the conditions mentioned above, China still has undoubtedly still a long way to go. However, in the past 10 years, the situation has improved, with an increase in both the development of offshore RMB markets and RMB settlement in cross-border trade:

- **More than 10,000 financial institutions are doing business in RMB**, up from just less than 1000 in 2011.
- **The PBoC permits the settlement of trade transactions with the RMB**. In 2015, trade settlement in RMB amounted to about $1.7 trillion, roughly 25% of China's annual trade volume, compared to 3% in 2010 and virtually 0% in 2008. In the US, thanks to the international role of the USD, the vast majority of trade settlements have long been in the domestic currency. Ito and Chinn (2013) have analysed the situation in China and find that the RMB underperforms as an invoicing/settlement currency, in comparison with the currencies of other countries.
- **The renminbi is the third most important currency of global issuance of letters of credit for trade-related purposes**. But, with a market share of around 5%, it is still far behind the dollar which accounts for 84% of the world total (the euro is second with 7% per cent).
- According to the latest triennial survey of foreign exchange and derivatives market activity published by the Bank for International Settlements (2016), **the renminbi is now involved in 4% of global FX transactions** (however, 97% by value in trades with the USD only). Up from 0.9% in 2010, the renminbi's market share is nevertheless quite small compared to a global share of 87.6% for the USD and 31.3% for the euro (note that given that two currencies are involved in each transaction, currency use in foreign exchange transactions totals 200%).
- **There are more and more official offshore RMB clearing centres since 2012**: Taipei (December 2012), Hong Kong (2013), Singapore (February 2013), Macau (2014), London (June 2014), Frankfurt (June 2014), Seoul (July 2014), Paris (September 2014), Luxembourg (September 2014), Doha (November 2014), Toronto (November 2014), Sydney (November 2014), Bangkok (January 2015), Kuala Lumpur (January 2015), Santiago de Chile (May 2015)... Note that following the establishment of offshore RMB markets, there are two distinct RMB markets for both residents and non-residents: the CNY market is onshore, and both exchange rates and interest rates are heavily managed by the central bank. The CNH is offshore, with exchange rates and interest rates determined by supply and demand. Arbitrage between CNH and CNY is therefore possible at this stage. The CNH market will grow over time and will become increasingly important for exporters, importers and investors.

- **China had closed (and extended) currency swap agreements with more than 30 central banks by end-2018, totalling more than RMB 3 trillion**: South Korea (December 2008), Hong Kong (January 2009), Malaysia (February 2009), Belarus (March 2009), Indonesia (March 2009), Argentina (March 2009), Iceland (June 2010), Singapore (July 2010), New Zealand (April 2011), Uzbekistan (April 2011), Mongolia (May 2011), Kazakhstan (June 2011), Russian Federation (June 2011), Thailand (December 2011), Pakistan (December 2011), the United Arab Emirates (January 2012), Turkey (February 2012), Australia (March 2012), Ukraine (June 2012), Brazil (March 2013), United Kingdom (June 2013), Hungary (September 2013), Albania (September 2013), Eurozone (October 2013), Switzerland (July 2014), Sri Lanka (September 2014), Qatar (November 2014), Canada (November 2014), Nepal (December 2014), Suriname (March 2015), South Africa (April 2015), Chile (May 2015), Tajikistan (September 2015), Morocco (May 2016), Egypt (December 2016), Nigeria (May 2018), Japan (Oct. 2018)… Like FX reserves, currency swap agreements between central banks represent financial safety nets (FSN): they are a resource that can be used during a crisis or a liquidity restriction.
- **An increasing number of central banks and sovereign wealth funds have evidently diversified their holdings to include renminbi reserves and investments or have plans to do so**. This is the case for the central banks of Australia, Austria, Brazil, Indonesia, Malaysia, Korea, Thailand, Pakistan, South Africa, Thailand, Venezuela, Nigeria, Hong Kong and Macau. The Reserve Bank of Australia (an important trading partner) invests around 5% of its foreign currency assets in renminbi securities in China. The Japanese Finance Ministry, the Kuwait Investment Authority and the World Bank/ IBRD also hold renminbi bonds.
- The **CNH market** will improve its expansion due to lower capital controls currently impeding the flow of CNH.
- **China aims to expand the international role of the CNH market by allowing foreign companies to issue bonds denominated in CNH**. For example, during 2010, the first "dim sum" bonds were issued by McDonald's, Caterpillar, China Development Bank, and some Hong Kong corporates…
- The PBoC sets up seven **clearing hubs** in different continents.
- The PBoC permits selected banks to offer **offshore RMB deposit accounts**.
- The PBoC creates a **payment system** for easier settlement of cross-border RMB transactions.

In total, **RMB is now the fifth most important payment currency** (behind the US dollar, the euro, the GBP and the JPY) but **patience is still required:**

the yuan only accounts for less than 3% of worldwide payments for cross-border trade and financial transactions... While the share of global economic output accounted for by China in 2017 was just over 17%, the renminbi's share in international payment flows in August 2018 was a mere 2.12 (2.45% in 2015). The USD and the euro are in a different position. The share of global economic output for the US in 2017 was 15%, and that for the euro just over 16%. By contrast, with a share of 39%, the USD undisputedly remains the world's most often used currency in payments, followed by the euro with 34%.

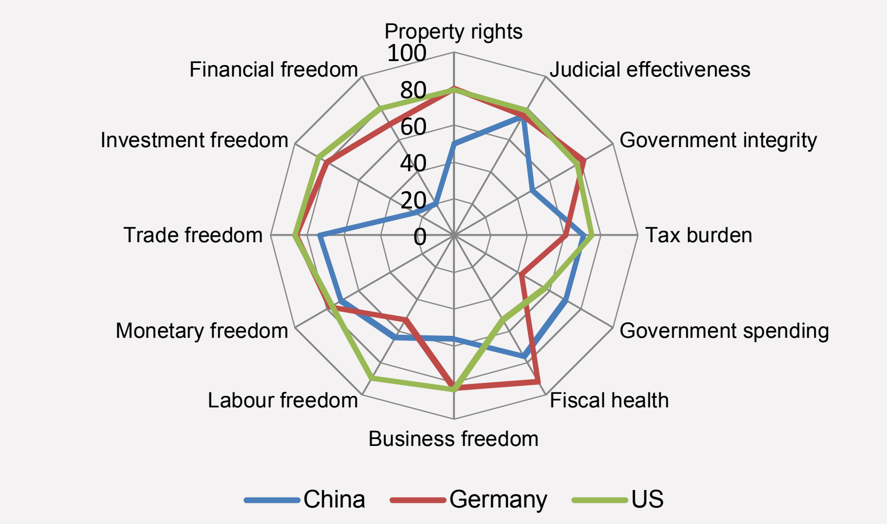
Financial liberalisation is critical, of course, but the way to go for China to be considered as a market economy is much larger. As the "economic freedom score", published by the Heritage Foundation, points out, China is significantly lagging behind Europe and the US. This index covers 180 countries, and analyses twelve aspects of economic freedom, grouped into four broad categories:

- **Rule of law**: property rights, judicial effectiveness, and government integrity;
- **Government size**: tax burden, government spending, and fiscal health;
- **Regulatory efficiency**: business freedom, labour freedom, and monetary freedom;
- **Market openness**: trade freedom, investment freedom, and financial freedom.

Asia is still the continent where disparities are at the highest, and China (ranked # 100 worldwide, and #20 in Asia-Pacific (over 43 countries))) is amongst the "mostly unfree countries" group. Its overall score is below the regional and world averages. As the report mentions, "*Non-transparent state-owned enterprises dominate the financial sector and many basic industries. The official ideology of "Socialism with Chinese Characteristics" has chilled liberalization, heightened reliance on mercantilism, raised bureaucratic hurdles to trade and investment, weakened the rule of law, and strengthened resistance from vested interests that impede more dynamic economic development*". The US ("mostly free") is ranked # 12). Europe has also good rankings: Ireland is ranked #6 and is part of the very small group of 6 countries considered as totally free (Hong Kong, Singapore, New Zealand, Switzerland, Australia and Ireland). UK (# 7), Germany (# 24), Finland (# 20), Austria (# 31), Netherlands (# 13), Luxembourg (# 17) (all "mostly free"), and France ("moderately free" - # 71) have all much better scores than China. Among the BRICS, Brazil is ranked # 150, Russia # 98, India # 129 and South Africa # 102, and all of them are considered "mostly unfree".

None of the BRICS are considered to be in the top 15 the countries having made huge strides in economic freedom in the past 25 years. The score of China stagnates for the past 2 years and has increased by only 10% in 20 years. The major concerns are still financial freedom and investment freedom. The graph 7 exhibits the lack of improvement in some components and the deterioration in monetary, investment and financial freedom components (China had implemented capital control measures at the turn of 2018).

Graph 6:
Index of economic freedom 2019: China, US and Germany

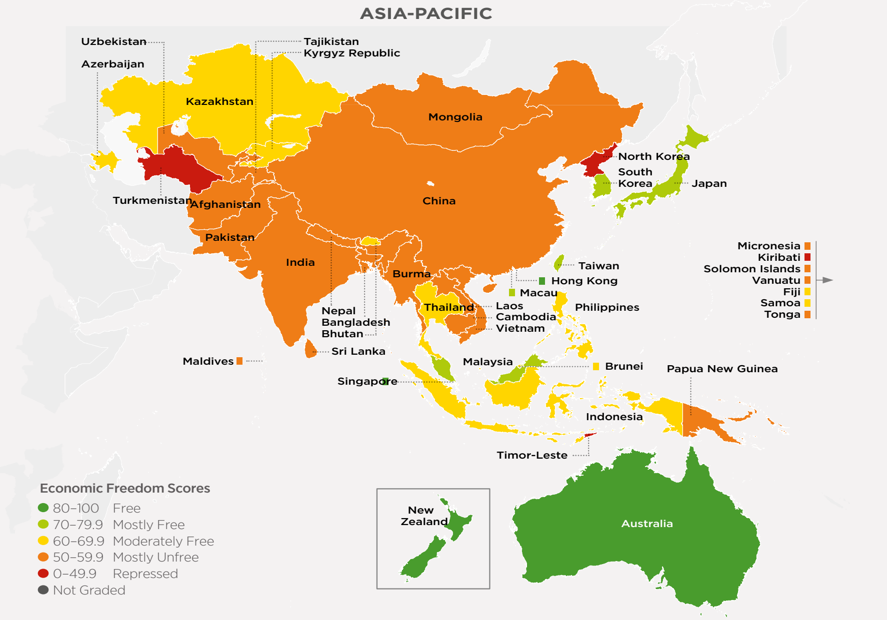


Source: Amundi Research

Graph 7:
Index of economic freedom - China from 2012 - 2019

Source: Amundi Research

Graph 8:
Index of economic freedom 2019: Asia-Pacific



SOURCE: Terry Miller, Anthony B. Kim, and James M. Roberts, *2019 Index of Economic Freedom* (Washington: The Heritage Foundation, 2019), http://www.heritage.org/index.

To conclude, as regard liquidity, convertibility, FX reserves... the yuan has a long way to go to be considered as a full international currency, for both official and private use. The lessons from the past are quite clear: **before becoming an international currency, some prerequisites are to be met: capital market liberalisation, capital account openness, capital controls abandoned, full convertibility of the currency, etc.**

It will be a long time before these prerequisites are met. It is unlikely that the yuan, (which still plays a weak role as a reserve currency, a settlement currency and an invoicing currency) will rapidly become an international currency. Financial reforms are on the way, but they will be completed over a long period of time. However, China tries to raise the international profile of the RMB.

- The RMB, for example, was included in 2016 in the IMF's special drawing rights (SDR) basket alongside the USD, euro, JPY and GBP. The RMB as a reserve currency held by foreign central banks will necessarily continue to increase after such a decision.
- China has launched in Shanghai (on March 26, 2018) the first yuan-denominated oil futures contracts. This should enhance the role of the

yuan as a global trading currency, and compel investors to increase their allocations to Chinese financial assets.

Some projections suggest that, by some years, with the RMB being largely a freely floating currency and the capital account more open (two critical prerequisites), 30% of China's trade should be invoiced in RMB, making the RMB the fourth largest global payment currency. Daily RMB FX turnover would exceed USD 500 billion (a three-fold increase compared with the 2016 situation, according to the last BIS triennial survey of FX and OTC derivatives trading).

At present, the USD and the EUR (lagging behind the USD by a wide margin, though) are the only currencies playing a serious role as international currencies. The RMB is neither a regional currency so far, nor an international currency. However, the yuan is undoubtedly gaining ground as part of FX reserves in the rest of the world. A growing number of central banks and sovereign wealth funds have diversified their holdings to include renminbi reserves and investments or have plans to do so. This is one of the major prerequisites for the yuan to become an international currency. A recent study (Drut – Ithurbide and alli (2016) suggest that the RMB is already an anchor for emerging currencies and its influence seems to go well beyond its neighbourhood area.

2.7. Is the euro fully competing the USD as an international currency? Where do we stand now?

The euro is already an international currency, since the very beginning.

1. **EUR vs. USD: the current situation**

As a reserve currency, the USD is by far the currency #1. The euro is the second currency in FX reserves, with 20.50% of total: 62% for the USD (below the 2001 level (72%)) and 2% for the RMB (JPY at 5% and GBP at 4.5%, CHF at 0.15%, AUD at 1.7% and CAD at 2%). The role of the USD has declined for some reasons:

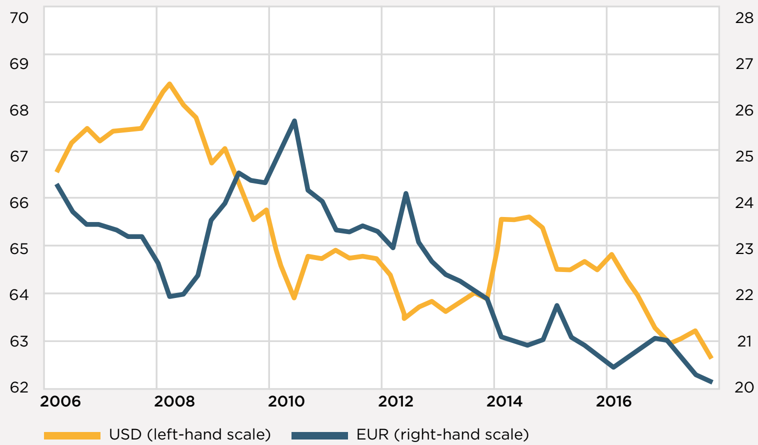
- The emergence of the euro as a reserve currency,
- Low interest rates in the US,
- Higher debt in the US,
- The decline of the US in the world economy,
- FX reserve diversification.

The role of the EUR has also declined since the GFC (Great Financial Crisis) due to diversification of FX reserves, and because of some additional and specific reasons:

- The 2011-2012 debt crisis,
- The recession that followed the GFC and the debt crisis,

- The doubt as regard the survival of the euro (the loss in predictability),
- The weakness and the instability of the euro.

Graph 9:
Share of the euro and the US dollar in FX reserves (%)

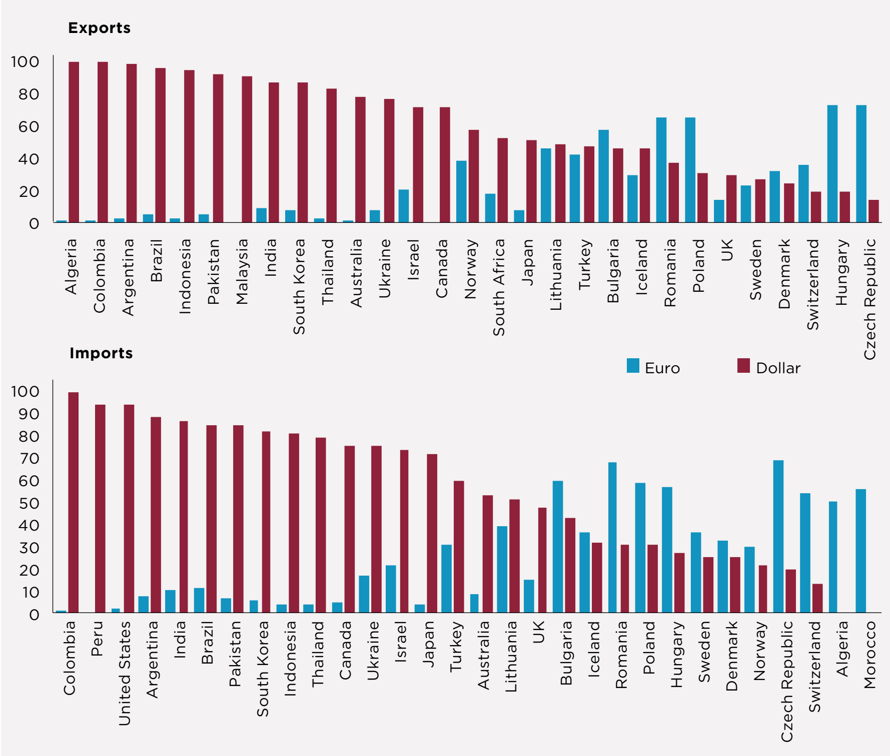


Sources: IMF and ECB calculations, B. Coeuré (2019).
Notes: Data adjusted for exchange rate valuation effects.
The latest observations are for Q4-2017

As an invoicing currency, the euro competes with the USD, but the USD remains the top currency. A recent study of Bruegel Institute shows the regional role of the euro. It is used mainly for exports/imports of non-euro area European countries and countries in the European neighbourhood. The USD, at the opposite, clearly has an international role: in East Asia and Latin America, trade is overwhelmingly invoiced in dollars. Even in Europe, the dollar's share is quite high, partially due to its role in denominating commodities (Graph.10).

In total, the US dollar is the only international currency in the world. The share of US dollar-denominated world trade is more than three times higher than the US' share of world trade (by comparison, the share of yen-denominated world trade is much smaller than Japan's share of world trade, which means that the yen is not an international settlement currency). It is too early to consider if and when the yuan will become a settlement currency in third-party trade. The first battle will be to replace the US dollar in Asia.

Graph 10:
The use of EUR and USD for export / import invoicing

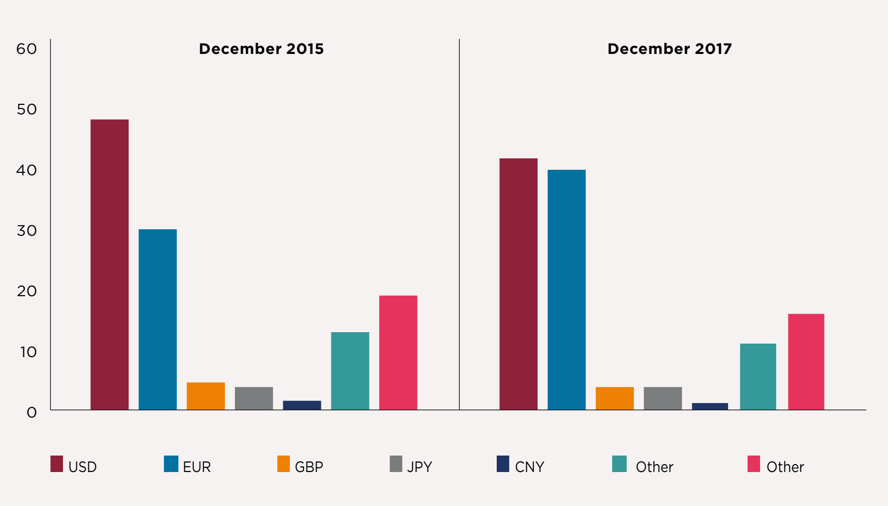


Source: Gopinath (2015)

Note: Average share of exports from imports into that country in that currency, averaged across all years for which data is available (starting 1999)

In international payments, the euro gained ground gradually vs. the dollar, and in 2017, the role of both currencies was similar, at around 40% each (Graph.10). The yuan represented 1%, the GBP and the yen around 3% each...

Graph 11:
Global payments by currency (in % of total)



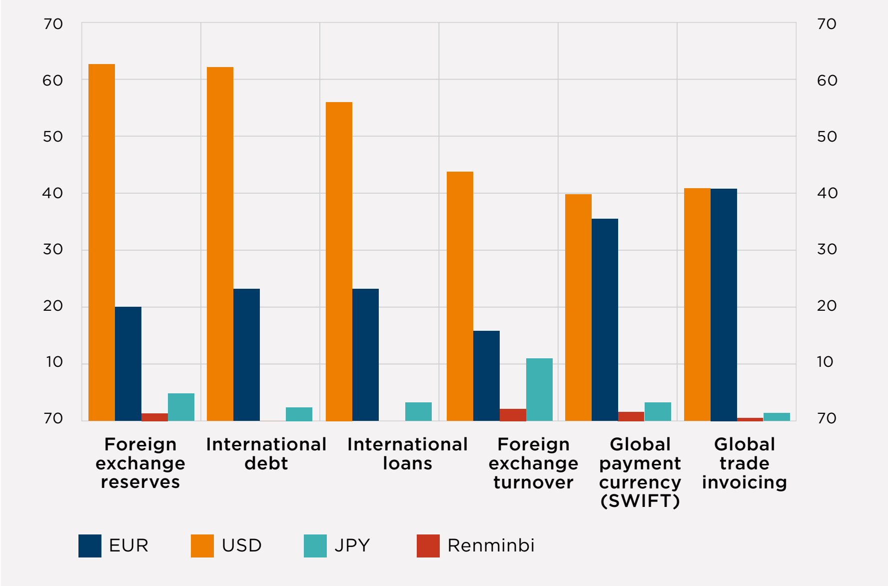
Source: Bruegel based on SWIFT via ECB (2018)

Note: Customer-initiated and institutional payments. Messages exchanged over SWIFT. Based on value. MT 103 (a SWIFT payment message format used for cash transfer specifically for cross-border wire transfer), MT 202 (a SWIFT message format for financial institution funds transfer between financial institutions), cross border only. Excluding payments within the euro-area.

As a vehicle currency, the USD is the most important currency, by far. And no currency is able so far to gain ground. In 1998, the USD was part of 87% of world trades, and this percentage is perfectly stable, with 88% in 2016, according to the last Triennial Central Bank Surveys carried out by the BIS. The euro is still ranked second, but its role is declining (39% in 2010, and 31% in 2016), due to the growing role of other currencies (JPY (22%), CNY (4%)...).

To sum up, the euro and the USD are the only currencies having an international role, but the euro is lagging behind as regard some functions such as FX turnover, FX reserves (graph 12). With the RMB emerging, one enters into a multipolar currency system.

Graph 12:
The EUR is the second world's international currency



Sources: BIS, IMF, SWIFT, Gopinath (2016) and ECB calculations.
Note: Data as at the fourth quarter of 2017 or latest available.

2. It is not completely new. Multi-polar currency systems existed in recent past.

- **Before World War One**, the Sterling Pound, the Deutsche-Mark and the French Franc all struggled for global supremacy as reserve currencies.
- **The inter-war period** was characterised by a GBP-USD duopoly.
- **In the 70s**, following two devaluations of the USD, some European currencies started to compete with the US currency.

3. How to reinforce the international role of the Euro? Some factors are linked to the euro, and some factors are linked to the USD…

3. 1 Factors linked to the Euro:

The most important step would be a significant consolidation of the **euro-area institutional set-up.** Some examples of actions: the completion of the European Banking union, progress on capital markets union. On the **debt side**, better credit quality of "peripheral" sovereign bonds, and mutualisation of debt through the issuance of a common "federal" bond, as in the US, would significantly increase the international role of the euro. Any progress in the set-up of **euro-area economic policy**, in its fiscal and structural components, would have the same positive impacts.

An important development in this respect would be for the ECB to enter into a series of swaps with central banks of countries that extensively use the euro, following the Fed example, or the PBoC. Progress in the **organisation and governance of the euro area** would also help: speaking one voice on critical issues – as it was the case for the Brexit issue would be a "plus" for the euro, no doubt.

The **segmentation** of European markets has also to be reduced: the Euro zone should be able – at last – to recycle internally, from the North to the South, its domestic savings. Last but not least, the international use of the euro would be expanded should the EU be able to adopt **a more united, and thus more effective, external and defence policy**.

The decline in the international use of the euro during the Great Recession clearly showed that the euro's international role is linked to the general stability of the euro, and sustainable stability depends on a more adequate euro-area institutional set-up.

3.2. Factors linked to the USD, with three major risks at present

First, since 2014, FX reserves ceased to increase. The reason is simple: many central banks do their best to avoid sharp appreciation of their currencies (oil-exporting countries, EMG countries, China, Japan). A **major change** comparing with the 2000-2014 period, when, FX reserves surged; it represented a massive "plus" for the USD, taking onto account the importance of the USD in reserves. **Mechanically, a large part of this increase was invested in USD, facilitating the US deficits**.

With the decline in FX reserves, the ongoing diversification of FX reserves (emergence of new currencies, gold), low US rates, the high level of US debt, and the decline of the share of the US economy in the world, the share of USD in FX reserves can only decline. EUR and mostly RMB should benefit of this trend.

Second, US deficits continue to rise significantly: US fiscal deficit and trade deficit deteriorated in the recent years, particularly due to the tax and fiscal boost, the slowdown of the US economy and the strength of domestic consumption. **The question deals with the capacity of the US to finance the twin deficit**: is the risk-free asset role of the US public debt (and the global demand for US treasuries) sufficient?

The US public debt (US-Treasuries) is the largest global risk-free asset, thanks to the liquidity of its market and the ability of the US state to remain solvent. During crises and recessions, investors rush to this asset class, which lowers US equilibrium interest rates and leads to an appreciation of the US dollar. Here lies a paradox (not sustainable): US problems give incentive to buy USD assets...

However, in history, it is easy to find periods when this risk-free asset role of the US debt is weaker.

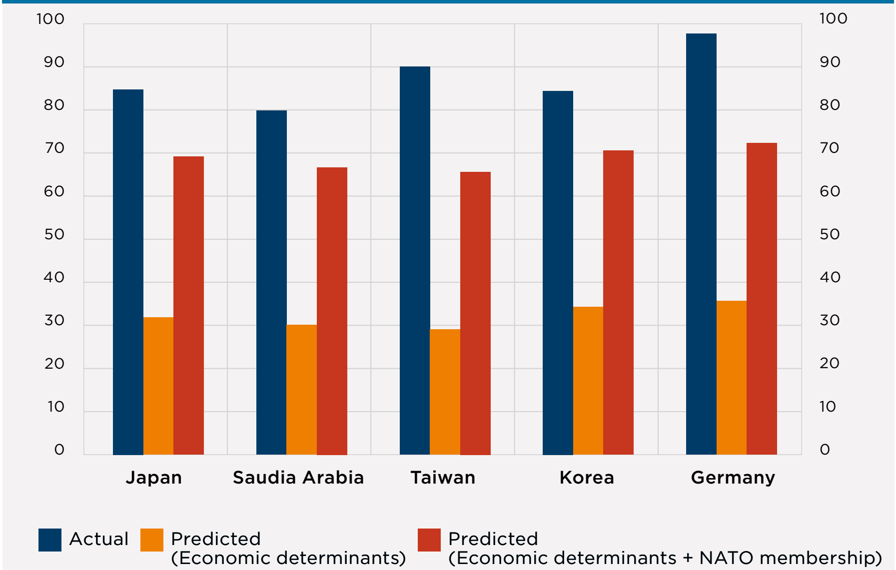
Sometimes, it is **insufficient to finance the US public deficit**, and it normally leads to a rise in US bond yields. This occurred in 1983-84, in 1990-91, in 2013-2014, and in 2017-2018.

Sometimes, it is **insufficient to finance the US external deficit**, and it normally leads to a depreciation of the dollar, as in 1985-87, and in 2004-2008.

At present, fiscal deficit and trade deficit (twin deficits) represent a risk… which is not (not yet?) priced in valuations. Such a situation would be favourable to additional diversification in FX reserves and further usage of alternative currencies.

Third, D. Trump external policy might have massive consequences. A recent study (Eichengreen et al. (2018)) shows that the share of the US dollar in the foreign reserve holdings depends on the US security umbrella (Graph.13). The authors assess the role of economic and security considerations in the currency composition of international reserves. They contrast what they call the "*Mercury hypothesis*" (currency choice being governed by pecuniary factors familiar to the literature, such as economic size and credibility of major reserve currency issuers), against the "*Mars hypothesis*" that this depends on geopolitical factors. Using data on foreign reserves of 19 countries before World War I, for which the currency composition of reserves is known and security alliances proliferated, they find that "*military alliances boost the share of a currency in the partner's foreign reserve holdings by about 30 percentage points. These findings speak to the implications of possible U.S. disengagement from global geopolitical affairs*" (i.e. a reduction in USD in FX reserves and/or a rise in bond yields as a way to still attract FX reserve flows into US assets). Said in a different way, should the U.S. withdraw from the world, keeping FX reserve composition unchanged would imply a rise in US Bond yields by as much as 80 basis points (this represents the advantage for the US (a negative risk premium) of protecting partners whose central banks allocate FX reserves into the USD assets). In such a scenario, additional diversification of FX reserves would certainly be inevitable.

Graph 13: Predicted share on the USD in international FX reserves



Source: Eichengreen, B., A. Mehl and L. Chiţu (2019).

Note: The figures show the predicted shares of the US dollar in the foreign reserve holdings of five countries which depend on the US security umbrella. Predicted shares are computed under two scenarios: (i) using estimates from a model restricted to standard economic determinants of international currency choice (shown as yellow bars); and (ii) using estimates from a model expanded to include the effect on international currency choice of the countries' NATO membership (shown as red bars). Actual US dollar shares are shown as blue bars. The actual dollar shares are based on publicly available estimates for the year 1987 (Korea), 2004 (Germany), 2006 (Japan), 2007 (Saudi Arabia) and 2016 (Taiwan); see Eichengreen et al. (2019) for further details on the sources for the data.

Being the master of NATO or being outside NATO (and other international organisations) might change the game for the US.

This would have clear implications for policymakers, in the US, and in Europe.

European initiatives to foster cooperation on security and defence, to speak with one voice on international affairs, and, in short, to further assert global leadership, might also help promote the euro's global outreach. In its 5 December 2018 communication, the EC presented some general considerations, a list of practical options and ideas to further develop its initiative. The Commission stresses that financial stability, progress on capital markets union, the perfection of banking union, the abundant supply of high-rated euro assets and the completion of Economic and Monetary Union are needed to fully develop the euro's role as an international currency.

2.8. Conclusion

As regards liquidity, convertibility, FX reserves... the yuan has a long way to go to be considered as a full international currency, for both official and private use. The lessons from the past are quite clear: before becoming an international currency, some prerequisites are to be met: capital market liberalisation, capital account openness, capital controls abandoned, full convertibility of the currency, etc. The RMB is neither a regional currency so far, nor an international currency so far. However, the yuan is undoubtedly gaining ground as part of FX reserves in the rest of the world. A growing number of central banks and sovereign wealth funds have diversified their holdings to include renminbi reserves and investments or have plans to do so.

The euro and the USD are therefore the only currencies having an international role, but the euro is lagging behind as regard some functions such as FX turnover, FX reserves. With the RMB emerging, one enters into a multipolar currency system.

So, long term, is the international status of the USD at risk?

- Some Asian central banks are at present diversifying FX reserves into alternative currencies and into gold;
- The USD has at last two contenders, the Chinese yuan and the Euro.
- The US might not be able to attract international savings eternally (as they do since the 1970s) to finance structural twin deficits.

Conclusion

It is far from the time when only two or three countries (or even one) represented power / hyper power. **These countries have not lost their power, they are "simply" forced to share it now** ... The shift in global power might mean a shift in global governance. Hard power and soft power (and the combination of the two, smart power) point that the US still represent a hegemonic power, while some powers emerge gradually. **Power is no more in the hands of one country and we already live in a multipolar world**. **With China, other countries emerge in some characteristics of power**. **Europe needs to push integration further** to be perceived as a block.

As regard the international currency, additional efforts have to be done to complete the multipolar world.

- **If China wants the yuan to become an international currency, some prerequisites are to be met**: capital market liberalisation, capital account openness, capital controls abandoned, full convertibility of the currency, etc.
- **To reinforce the international role of the Euro, Europe has to consolidate and improve the euro-area institutional set-up**. Some examples: the completion of the **European Banking union**, progress on **capital markets union**, better **credit quality of "peripheral"** sovereign bonds. The issuance of a **common "federal" bond**, with a role similar to that played by Treasuries in the US, would significantly increase the international role of the euro. Progress in the **set-up of euro-area economic policy**, in its fiscal and structural components, and **a more united, and thus more effective, external and defence policy** would favour greater international use of the euro. **Speaking one voice** more regularly on critical issues would be a "plus" for the euro, no doubt.

Once these targets achieved, it should be less and less easy for the US to impose rules and to dictate governance as it recently did when they decide to withdraw from the nuclear agreement with Iran and put pressure on Korean, German and French auto-makers, or when it refuses to appoint new judges at the WTO to weaken the organisation and to force a "shutdown" of this institution. With power better shared, global governance should be more efficient, less biased and more transparent... we do hope so...

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CROSS ASSET
INVESTMENT STRATEGY

April 2019 | Discussion Paper

Document issued by Amundi Asset Management, "société par actions simplifiée" with a share capital of €1,086,262,605 - Portfolio manager regulated by the AMF under number GP04000036 – Head office: 90 boulevard Pasteur – 75015 Paris – France – 437 574 452 RCS Paris www.amundi.com - Photo credit: Getty Images - PeskyMonkey

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