EASTERN EXPRESS
and 23
22 JUN 1996

20 years to China's full convertibility

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With a lack of monetary tools, China is expected to take as long as two decades to achieve full convertibility of its domestic currency, economists said.

But China is going one step closer by making its currency convertible for current account trading from July 1.

"China is not ready for a full covertibility, it does not have the ability to handle the capital flow," Tao Dong, an economist at Schroders Securities Asia, said.

The central bank was weak in handling currency stability in the market since the development of the open market operation is close to zero, Tao said.

It would take 15-20 years before China is ready for full convertibility, he added.

The move to further deregulate the renminbi market followed a trial scheme in four mainland cities to allow foreign enterprises to make their currency transactions in designated banks or swap centres three months ago.

The success in the trial period has prompted the central bank to incorporate all foreign funded enterprises into the interbank market, Pan Ming, senior economist of DBS Investment Research said.

"The new regime is conducive for introducing foreign investment but is unlikely to depress the renminbi exchange rate," Pan said.

On the belief that the renminbi exchange rate in the medium term is determined by the supply and demand of the domestic and foreign currency, he said the exchange rate will not face depreciating pressure.

The demand for the renminbi will be tremendous in the next few years as more foreign capital will be attracted into big infrastructural projects in China coming on line.

On the other hand, the supply of United States dollars is expected to exceed the demand in the medium term on the back of an expected surplus in both the merchandise trade and capital account, plus a sharp rise in income from tourism, he added.

"This is clearly shown by China's rapidly rising foreign reserves which reached US$85bn by the end of May, up more than US$12bn from the year's beginning," Pan said.

The strong foreign reserves also added to the government's strength to speed up the deregulation process, he added.

Tao disagreed that the reserve amount is a crucial factor to convertibility since the definition of a strong reserve is a subjective judgment.

On the move's implications to foreign-funded enterprises, economists said joint ventures now have easier access to foreign currency.

However, companies aiming at entry into China's domestic market are unlikely to benefit substantially due to their small scale at the early stage of investment, Tao said.