of global economic growth. This included not just China, Korea, Japan and the industrial and emerging economies of Southeast Asia (i.e., Singapore, Malaysia, Indonesia and Vietnam), but also India and South Asia, thereby drawing into sharp focus the geo-economic vitality of the Pacific and Indian Oceans. A deeper reflection on Prime Minister Abe's speech and his articulation of the concept of Indo-Pacific cannot avoid identifying the rising engagement between East and Southeast Asia, the Middle East, Africa, and the hitherto under-recognised, but nonetheless critical role of the Indian Ocean. The construct for future cross-continental trade and connectivity frameworks could be visualised in a framework assuming the combined growth of both through the congruence of the Pacific and Indian Oceans.

Since Prime Minister Abe's speech, the concept of Indo-Pacific has gained considerable traction, particularly after its expanded US iteration as the "Free and Open Indo-Pacific (FOIP)", culminating in the pronouncement of the Asia Reassurance Initiative Act (ARIA) of 2018. Signed into law on 31 December 2018, ARIA marks the US strategy to "increase U.S. security, economic interests, and values in the Indo-Pacific region"[4]. Separately, various earlier American pronouncements on the subject[5] leave little doubt about the salience of the Indo-Pacific as a multicontinental and cross-ocean entity poised to alter the geo-economic and geopolitical architectures engulfing the Pacific and Indian Oceans. The development has great significance for India and the South Asia region in terms of its impacts on trade and economic connectivity.

CONNECTIVITY: CHARACTER AND COMPETITION

The notion of connectivity, as visualised through cross-country infrastructure projects, has undergone fundamental changes. Nowhere are these changes more visible than in the Indo-Pacific region in the form of large-scale ambitious projects linking territories, markets and communities across the continent. The Pacific and the Indian Oceans have been at the core of regional connectivity schemes from well before the FOIP was pronounced. The most notable project has been the China-led

---

[4] S 2736, Bill Announcement, The White House, 31 December 2018, https://www.whitehouse.gov/briefings-statements/bill-announcement-12/, accessed on 20 March 2019.

[5] 1. "Remarks by President Trump at APEC CEO Summit | Da Nang, Vietnam", Foreign Policy, 10 November 10 2017, The White House, https://www.whitehouse.gov/briefings-statements/remarks-president-trump-apec-ceo-summit-da-nang-vietnam/; 2. "President Donald Trump's Administration in Advancing a Free and Open Indo Pacific", Economy & Jobs, 30 July 2018, The White House, https://www.whitehouse.gov/briefings-statements/president-donald-j-trumps-administration-advancing-free-open-indo-pacific/, both accessed on 20 March 2019.

Belt and Road Initiative (BRI). The Asia-Africa Growth Corridor (AAGC)[6] proposed by Japan and India is also a mega-connectivity project aiming to link Asia and Africa through the Pacific and Indian Oceans. Indeed, AAGC actually aspires to realise a "free and open Indo-Pacific" through "growth and interconnectedness between and within Asia and Africa".[7] Given the respective geographies they encompass, South Asian countries are integral to both the BRI and the AAGC.

Infrastructure projects like the BRI and the AAGC, as well as those that could come up in the Indo-Pacific in the future through sub-regional or multi-country efforts, are certain to be multi-modal and exhaustive in scale and scope. Apart from comprising land corridors through cross-country road and rail links, the projects would be linking discrete geographies through sea and the cyberspace. These characteristics make the connectivity projects complex to comprehend. However, there's little doubt about their far-reaching impacts, which are not just economic but also geo-political. The scale and scope of the BRI and AAGC can hardly avoid geostrategic implications, notwithstanding their substantial economic spillovers through creation of new infrastructure assets and additional economic activities around the generation of these assets.

China's commanding role in funding BRI projects enables it to cultivate strategic influence in host nations through control over major resources and services (e.g., roads, ports, telecoms and cyber networks) that are critical from internal security and external geopolitical perspectives. The ripples created by the BRI in South Asia are therefore understandable given the concerns arising for India through Chinese funding of infrastructure in neighbouring Sri Lanka, Maldives and Pakistan. Such a geo-strategically sensitive and significant project like the BRI is quite likely to generate counter-responses from other major regional actors like India and Japan. The AAGC, notwithstanding its emphasis on sustainable development and physical infrastructure, can hardly be overlooked in its geopolitical significance. This might mark the beginning of a period of strategic rivalry across the Indo-Pacific around infrastructure connectivity. The stage for such a prolonged connectivity competition appears set with the US pronouncement of the FOIP, which is for all practical purposes a counter to the BRI.

---

6 "Asia-Africa Growth Corridor: A Vision Document", African Development Bank Meeting, Ahmedabad, India, 22-26 May 2017, http://www.eria.org/Asia-Africa-Growth-Corridor-Document.pdf, accessed on 20 March 2019.

7 Ibid., p. 14.

WIDENING ECONOMIC GAPS

Heterogeneity is perhaps the most noticeable economic aspect of the Indo-Pacific. From an economic perspective, the region represents a collection of heavily contrasting economic geographies, where some of the world's largest and most populous economies co-exist with some of the poorest. More specifically, the Indo-Pacific is a region with some of the world's most prosperous high-income economies (e.g., Australia, Japan, Korea, New Zealand and the US) co-existing with large and populous middle-income economies (e.g., China, India, Indonesia, Iran and Malaysia); and high-income small economies (e.g., Singapore, Mauritius, Maldives, Seychelles) residing with low-income economies (e.g., Cambodia, Kenya, Lao, Myanmar, Nepal). These structural economic heterogeneities reflect a region saddled with a variety of economies in different stages of economic development and countries with varying degrees of economic capabilities and quality of institutions. These variations are further evident from the differences among regions within the Indo-Pacific in terms of their integrations with the global economy and their current infrastructure capacities, particularly those influencing their abilities to trade.

East and Southeast Asia have much higher shares of intra-regional trade than South Asia, Middle East and Africa, underscoring the strength and capability of their institutions and practices in participating in trade through regional and global production networks. The difference in capacities is easily visible from the national logistics performance indices (LPI). Logistics include a host of institutional functions ranging from operational efficiencies of ports and speed of customs clearances to domestic transport linkages between ports on coasts and their hinterlands. Quality of logistics determines the abilities of economies to exploit infrastructure facilities effectively for entrenching participation of producers in global production networks. The more economically advanced and relatively higher-income economies in the Indo-Pacific, such as Japan, the US, Singapore, New Zealand, Australia, Korea, Taiwan and China, have better logistics capacities than the rest. While India ranks 47 in overall LPI, large South Asian economies like Bangladesh, Nepal and Pakistan rank beyond 100 with Bhutan and Afghanistan being among the lowest.[8] A similar difference in capacities is noticed in the space of digital communication with more high-income developed economies like Australia, Canada, New Zealand, Japan, Singapore and the US leading the rest of the Indo-Pacific in access of local popula-

8 Logistics Performance Index (LPI) 2018, https://lpi.worldbank.org/, accessed on 20 March 2019.

tions to the internet and internet infrastructure, including speed of accessing data and broadband services. A vast number of countries from Africa, Middle East, South and Southeast Asia and the Pacific continue to suffer from low broadband speeds[9], impinging their abilities to take part in fast-paced cross-border digital transactions, particularly financial transactions.

The marked difference in infrastructure capacities and the overall ability to trade and engage in global commerce – as visible between several South Asian countries and many of the economically developed high-income economies of the region – is also noted between the latter and economies from several other sub-regions, such as Africa and Middle East, as well. This points to a situation where economies with more capacities and higher systemic and institutional efficiencies will be better placed to exploit new infrastructure – a situation that might just further widen current economic gaps within the region.

US PRONOUNCEMENTS AND INDO-PACIFIC

As mentioned earlier, various US pronouncements on the FOIP make it amply clear that connectivity and infrastructure-building in the Indo-Pacific is not just in American strategic and security interests, but also an effort to strengthen existing American alliances and create new partnerships for neutralising the Chinese influence in the region. Some key elements of the US pronouncements, such as the US interest in entering into bilateral free trade agreements (FTAs) with any Indo-Pacific country, the initial commitment of $113.5 million to digital connectivity,[10] cybersecurity and sustainable infrastructure in the region, and the introduction of the BUILD (Better Utilization of Investments Leading to Development) Act of 2018 for establishing the US International Development Finance Corporation (USDFC),[11] leave little doubt over connectivity, infrastructure, development finance, trade and investments getting embroiled in a critical game of strategic leverage across the Indian and Pacific Oceans.

For India, which is visualised as an important stakeholder in the Indo-Pacific by the US, as well as other South Asian countries located around and on the Indian Ocean – Bangladesh, Maldives and Sri Lanka – growth of FOIP as a primarily

[9] https://www.cable.co.uk/broadband/speed/worldwide-speed-league/, accessed on 21 March 2019.

[10] As in 4 earlier.

[11] "The BUILD Act", OPIC, https://www.opic.gov/build-act/overview, accessed on 21 March 2019.

security-oriented framework has serious implications. India would be hesitant to commit to a regional initiative that is limited in inclusivity and focused on economic development more for optics.[12] Notwithstanding its differences with China on various issues and its stated reservations on the BRI, India has insisted on the Indo-Pacific being "free, open and inclusive".[13] The insistence underscores its hesitation to be seen as a part of a regional order that is primarily a counter to China. Indeed, committing to such an order focusing on the geopolitical and security interests of the US might mean endorsing the precise legitimacy limitations that affect the BRI: the "strategic price" that countries might have to pay in terms of geopolitical commitment in exchange for development assistance and infrastructure funding. Countries like Bangladesh and Sri Lanka have already enthusiastically endorsed the BRI and are relying on Chinese funds for lasting infrastructure developments. For these South Asian countries, the FOIP poses a serious challenge of choice given that an enthusiastic approach to the former might be considered inimical by the Chinese. The FOIP might be able to avoid the problems of choice and legitimacy for many of the relatively smaller countries if it takes care to promote multi-country involvement, as opposed to a prominent US-centrality. The latter might invite for it the same legitimacy issues that an excessive China-centric focus has for the BRI.[14]

CONNECTIVITY AND TRADE WAR

The forceful US articulation of the Indo-Pacific comes at a time when the US-China trade hostilities are at an unprecedented high. The back and forth tariffs imposed by the US and China on a large number of items traded by each other began with the US decision to impose unilateral tariffs on steel and aluminium imports into the US in March 2018. The unilateral action was the first pointer to the emergence of a trend likely to influence global trade significantly in the days to come: viewing trade through the broad prism of national security. The US tariffs were imposed

---

12 Palit, Amitendu and Sano, Shutaro, 2018, "The Free and Open Indo-Pacific Strategy and Concerns for India and Japan", Asia Pacific Bulletin, East West Center, No. 442, 10 October 2018, https://www.eastwestcenter.org/system/tdf/private/apb442_0.pdf?file=1&type=node&id=36846, accessed on 22 March 2019.

13 "Indo-Pacific must be free, open and an inclusive region: Sushma Swaraj", The Economic Times, 19 July 2018, https://economictimes.indiatimes.com/news/defence/indo-pacific-must-be-free-open-and-and-inclusive-region-sushma-swaraj/articleshow/65060360.cms, accessed on 22 March 2019.

14 Palit, Amitendu, 2018, "Indo-Pacific Connectivity: Lessons from China's Belt and Road", Griffith Asia Institute, 28 February 2018, https://blogs.griffith.edu.au/asiainsights/indo-pacific-connectivity-lessons-from-chinas-belt-and-road/, accessed on 22 March 2019.

under Section 232 of the US Trade Expansion Act of 1962 and were justified on the grounds of national security. More American tariffs on China came under Section 301 of the Trade Act of 1974 on the grounds of specific harm caused to US business interests in China by unfair domestic trade practices. It is notable though that investigations under Section 232 are continuing on automobiles and auto parts for examining whether these imports impinge on US national security.

The US and China are engaged in intensive discussions for settling their trade acrimony. But there is no doubt that even if there is a temporary truce, the US-China battle for economic supremacy and the resultant geostrategic influence is going to continue. The battle might result in trade getting increasingly fashioned by geopolitics. This might happen through other countries being forced to make choices between the US and China and getting impacted in their trade relations accordingly. The Indo-Pacific is particularly vulnerable in this regard.

Countries aligning with the US in Indo-Pacific connectivity projects, for example, might obtain more favourable conditions for market access through bilateral deals with the US given the current US proclivity to look at all trade relations exclusively and bilaterally. The same countries, on the other hand, might find themselves encountering greater difficulties in trading with China given their strategic alignment with the US. The reverse scenario is equally possible for countries aligning with China on the BRI.

While South Asian countries reflect on these possibilities, they are also aware that geopolitical fashioning of trade would also be conditioned by connectivity. New infrastructure corridors and cross-border linkages would command a strategic price, which might include a new orientation of trade based on geopolitical loyalty. This would mark a complete shift away from market-based comparative advantages in production that has traditionally fashioned trade, particularly since the establishment of the World Trade Organisation (WTO). Unilateral trade actions – as witnessed in the ongoing US-China hostilities – are leading to a steady erosion in the significance of the multilateral rules-based trade order run by the WTO. Such a consequence might alter the global trade order fundamentally, leading to a trade landscape where politics determines partners for trade, as it was before World War I.[15]

[15] Eichengreen, Barry, Mehl, Arnaud and Chitu, Livia, 2019, “Mars or Mercury redux: the geopolitics of bilateral trade agreements”, European Central Bank, Working Paper Series, 2246, February, https://www.ecb.europa.eu/pub/pdf/scpwps/ecb.wp2246~1a43a0b375.en.pdf?144e06dd62f499eed4bf05559a304006, accessed on 22 March 2019.

CONCLUDING THOUGHTS

Trade and connectivity are being increasingly repositioned by the world's major powers in a manner that is suitable for their security and strategic interests. The tendency creates several challenges for South Asian countries as discussed in the paper in the context of the Indo-Pacific. As of now, there appears to be little that the region can do in terms of response, except for being alert and attentive to a pattern of regional development that is largely unprecedented. Improvements in internal and domestic institutional capacities, though, might always prepare the region for better responses to challenges economically.

Amitendu Palit is Senior Research Fellow and Research Lead (trade and economic policy) at the Institute of South Asian Studies in the National University of Singapore.

Currency Swap Arrangements and Its Role in Stabilising Financial Markets

Xu Mingqi

1. BASIC FUNCTION OF CENTRAL BANK CURRENCY SWAPS

Central bank currency swaps is not a new phenomenon. It first emerged under the Bretton Woods System on 28 February 1962 when the US Federal Reserve (FED) singed a currency swap agreement with the Central Bank of France, which came into effect on 1 March 1962. At that time, the US government faced great pressure to maintain the fixed exchange rate of the US dollar to gold and was obliged to convert at a fixed rate of 35 dollar per ounce with gold for the dollar to the other central banks. The swap agreement was in the form of mutual credit to each other's account. The Central Bank of France credited 500 million francs into the Federal Reserve account while the Federal Reserve credited USD 50 million into the Central Bank of France account. This enabled the Federal Reserve to use French francs to intervene in the market to maintain US dollar market stability. The Federal Reserve signed more swap agreements with other western countries' central banks subsequently, amounting to USD 0.9 billion in 1963, so as to acquire liquidity to intervene in the market. However, the stability was only short-lived and US dollar crises frequently broke out, which ultimately led to the US government ceasing the dollar convertibility with gold in August 1971.

Currency swaps once again attracted international attention in the wake of the turbulence caused by the global international financial crisis triggered by the US sub-prime mortgage crisis. In December 2007, the Federal Reserve signed currency swap agreements of USD 20 billion and USD 4 billion separately with the European Central Bank and the Switzerland National Bank; later, more swap agreements were signed and the amount was increased. By 29 October 2008, 14 central banks had signed currency swap agreements with the Federal Reserve individually and the total amount was up to USD 850 billion, which was four times the IMF's gross assets. After the international financial crisis broke out, many central banks needed the US dollar liquidity to intervene in the market and the Federal Reserve became the main supplier of USD liquidity to other countries. Paradoxically, currency swaps first emerged as a means to help the US FED to have liquidity to intervene in the market and to maintain the dollar exchange rate under the Bretton Woods System; while this time, after the global financial crisis erupted, the US FED became the only reliable source to provide additional liquidity. This was because after the US ceased its obligation to maintain the dollar's fixed rate and full convertibility to gold, the US FED became free to create US dollar liquidity at its own discretion. Currency swaps is no longer quite demanded by the US FED but rather by other central banks. Under the current international monetary system, only the other central banks need external sources to provide additional USD liquidity if they need to intervene in the market to prevent their own currency's sharp depreciation. They need the swap arrangement to have additional USD and this is why most central bank currency swaps were bilateral swaps between the US FED and other western countries' central banks during the global financial crisis.

The reason behind this is obvious. The US dollar is the key international currency and most central banks hold US dollar assets as their main reserve. Most commercial banks and non-bank financial institutions that are doing business internationally do the same. The US financial crisis hit the US financial market severely and the market price of all forms of US financial assets dropped dramatically. This created huge risk exposures not only for the US financial firms but also for international banks worldwide. If their assets' value cannot cover their debts, financial institutions' stock prices will drop. For the central banks, the reserve value's decrease may lead to currency depreciation. If a central bank wants to stabilise the market by intervention, it needs more US dollar liquidity or credit. Unlike the US FED, the other central banks could not create US dollars by themselves. In most cases, only the US Federal Reserve can act as the lender of last resort other than the IMF. That is why after the global financial crisis was triggered by the sub-prime mortgage crisis in the US in 2007-2008, it later hit others even more severely and many central banks needed additional US dollar liquidity much more badly. Hence, central bank swap agreements enabled the US FED to provide standby credit to other central banks in case they needed additional US dollar liquidity to stabilise the financial markets. However, central bank currency swaps also manifested the problem of the current international monetary system being heavily dependent on the US dollar.

On 31 October 2013, when the old type of swap agreements between the US FED and Bank of Canada, Bank of England, European Central Bank, Bank of Japan and Switzerland National Bank expired, the six central banks declared the renewal of their swap agreements with no term and quota limits. This created a new kind of swaps and the function of central bank currency swaps evolved to a new sphere. Some regarded this as the prototype of a new international monetary system (Li Yang, 2013).[1] To me, this is a move led by the US to consolidate the current US dollar-dominant international monetary system and to prevent other currencies from emerging to become more competitive relative to the US dollar. It is clear that while this new swap arrangement will enhance the stability of the US dollar-centred international financial market, it degraded the multilateral international safety net based on the IMF, limited the capability of developing countries to access the contingent liquidity as only six western central banks are included, and may create a new kind of moral hazard in relations to these developed countries' central banks pursuing monetary policy targets. There are reasons to believe that the US FED-led six central banks currency swap arrangements with no term and no quota limits has a negative impact on the reform of the international monetary system and the IMF itself. Scholars appealed for wider cooperation of global central banks by currency swaps other than US FED currency swaps (Shen, 2017).[2]

2. DEVELOPMENT OF REGIONAL CURRENCY SWAP AGREEMENTS

When developing countries build their regional economic cooperation framework, currency swaps also becomes one of the choices for bilateral or regional financial safety net building. The pioneer agreement was signed by the five ASEAN members, Indonesia, Malaysia, the Philippines, Singapore and Thailand, in 1977. After the eruption of the Southeast Asian financial crisis, this swap agreement was extended to all members of ASEAN as well as China, Japan and Korea. It developed into the so-called 10+3 "Chiang Mai Initiative (CMI)". However, most of the bilateral swap agreements under CMI are still based on the US dollar as the key currency and the swap-out currency is the US dollar. Only the agreements between China and Japan, Korea and the Philippines were in national currencies. This also showed the dominant position of the US dollar in East Asia. CMI was multilateralised and converted from a network of bilateral agreements between countries into one

1 Li Yang, 2014. "Actively Respond to Six Central Bank Currency Swap Upgrading", http://bank.cnfol.com/pinglunfenxi/20140120/16800192.shtml, accessed 10 February 2019.

2 Shen, Andrew, 2017. "World's Central Banks Need to Cooperate to Deal With Crises", Caixin, 25 July 2017, https://www.caixinglobal.com/2017-07-25/101121856.html, accessed 10 February 2019.

single agreement, the Chiang Mai Initiative Multilateralisation (CMIM), in 2010. A surveillance unit, the ASEAN+3 Macroeconomic Research Office (AMRO), was created. This Common Reserve Pool was expanded to USD 240 billion in 2012 from the original USD 120 billion.

After the global financial crisis, not only did the US FED-centred central bank swaps further developed, other bilateral and regional central bank currency swaps also arose. The US dollar's value experienced huge volatility, resulting in heavy stress to many central banks in their efforts to maintain the stable value of their foreign exchange reserve and the cost of holding USD reserve continually rising. In order to manage the reserve currency exchange rate risk, the trend of diversifying the reserve currencies appeared to gain new impetus. With the development of the multilateralisation of the international reserve currency, some major developing countries' currencies also became the assets willingly held by other countries' central banks. Against such a background, national currency swap agreements emerged. For example, on 25 June 2012, the Switzerland and Poland central banks signed a swap agreement of Swiss Franc and PLN; on 4 December 2012, India and Japan signed a national currency swap agreement of amount equivalent to USD 15 billion; this was renewed twice on 19 December 2013 and 29 October 2018 and the amount was expanded to USD 50 billion and again to USD 75 billion. Japan also signed bilateral swap agreements with Indonesia, the Philippines and Singapore and extended the amounts in 2013 when the US FED was thought to be tapering the monetary supply. Reserve Bank of Australia and Bank of Korea signed a local currency swap agreement of amount A$ 10/KRW 9 trillion in 2014 and renewed it in February 2017. Bank of Australia also signed a currency swap agreement with the Indonesian central bank of amount A $10 billion/IDR 100 trillion in December 2015 and this was renewed in August 2018. Korea and Indonesia signed a local currency swap agreement of amount KRW 10.7 trillion (9.2 billion US dollars) or 115 trillion rupiah in 2014 in addition to the CMIM and it was renewed in 2017. In Europe, most currency swaps are based on the Euro. For example, the ECB provides a swap line to Hungary; and the Swedish central bank provided the Euro standby credit to Latvia, Estonia, and Iceland with swap agreements.[3] According to di Mauro and

[3] Council on Foreign Relations. "The Spread of Central Bank Currency Swaps Since Financial Crisis", https://www.cfr.org/interactives/central-bank-currency-swaps-since-financial-crisis#!/central-bank-currency-swaps-since-financial-crisis, accessed 10 February 2019.

Zettelmeyer (2017), there are about 160 bilateral central bank currency swaps at present and they form an important part of the global financial safety net.[4]

China actively launched bilateral currency swap agreements against the background of RMB internationalisation. The first national currency swap agreement of China's central bank, People's Bank of China (PBOC), was signed with Korea in December 2008 and the amount was worth RMB 180 billion/WON 38 trillion. Since then, PBOC has signed bilateral currency swap agreements with 38 central banks respectively and the total amount has reached RMB 3.57 trillion. The latest one was signed with Bank of Japan, of amount RMB 200 billion, on 26 October 2018. Most of these swap agreements were for three-year terms and were renewed after maturity. A few of them were not renewed after maturing owing to some reasons. As at the end of 2018, there are still 31 swap agreements in effect and the existing total amount is RMB 3.2 trillion.

There are different views on the spread of central bank currency swaps. Mainstream economists in the US have a positive attitude toward central bank currency swaps and believe it would be better to build a global network of central bank swaps with three levels to form an international lender of last resort (Truman, 2013).[5] According to Ricardo Reis and Saleem Bahaj (2018), central bank swap agreements enhance the cooperation of central banks in providing liquidity, lower the cost of borrowing and promote cross-border capital flow.[6] However, some argue that central bank currency swaps could create moral hazards and insolvent countries should not normally have access to crisis lending unless they pass prequalification tests associated with access to the IMF's "flexible credit line" (FCL) and there is assurance that structural adjustments should follow.[7] Developing countries' economists believed that central bank currency swaps could be coordinated with the IMF function of lender of last resort and that the IMF can play the role of

[4] di Mauro, Weder Beatrice and Zettelmeyer, Jeromin. "The New Global Financial Safety Net: Struggling for Coherent Governance in a Multipolar System", 30 January 2017. CIGI Essays in International Finance, Volume 4, January 2017. Available at SSRN: https://ssrn.com/abstract=2946452, accessed 10 February 2019.

[5] Truman, Edwin M., 2013. "Enhancing the Global Safety Network Through Central Bank Cooperation", *Vox,* 13 September 2013.

[6] Reis, Ricardo and Saleem Bahaj, 2018. "This is the role of central bank swap lines in the global Economy", World Economic Forum, 28 September 2018, https://www.weforum.org/agenda/2018/09/central-bank-swap-lines/, accessed 14 February 2019.

[7] See di Mauro and Zettelmeyer, above-mentioned paper in note 4.

a clearing house of swaps network (Yeyati and Cordella, 2010).[8] I think that bilateral and regional central bank swap lines are only the second-best choice and that the best approach is to enhance the IMF role of lender of last resort and to have a global governance rule and principles in place. However, it will be quite difficult to enhance the IMF role of lender of last resort and to increase the IMF quota as the US is not supportive of these two proposals. Regional and bilateral central bank swaps become the second-best choice instead of enhancing a global comprehensive safety net based on the IMF.

3. RMB INTERNATIONALISATION AND THE PURPOSE OF PBOC CURRENCY SWAP AGREEMENTS

Many believe that PBOC actively participates in bilateral national currency swaps so as to promote RMB internationalisation. I do not question this view and believe that China is in favour of the trend of international currency multilateralisation and RMB internationalisation is a part of this trend. For this reason, some swap agreements that PBOC signed, especially those with developing countries that lack US dollar reserves, stated that the swap agreement was to promote bilateral trade and investment. It was regarded as helping to promote RMB denomination in trade and investment across the two countries. Empirical studies by some scholars also showed that high trade and investment interdependence between China and specific partner countries tend to correlate with the presence of currency swap agreements with PBOC (Liao and McDowell, 2015).[9] This is beyond the traditional purpose of short-term liquidity provision for market stabilisation. However, most PBOC currency swap agreements still emphasised market stability as the priority purpose. Hence, RMB internationalisation is not the only driving force of PBOC currency swaps. To help to create an additional safety net for financial stability is a higher priority than promoting RBM internationalisation. RMB internationalisation itself is not simply to enable it to become an international reserve currency, as many believe, but rather to reduce the exchange rate risk for Chinese companies doing international business. Managing the financial market risk is a more urgent

[8] Yeyati, Eduardo Levy and Tito Cordella, 2010. “Global safety nets: The IMF as a swap clearing house”, Vox CEPR Policy Portal, 18 April 2010, https://voxeu.org/article/global-safety-nets-imf-swap-clearing-house, accessed 14 February 2019.

[9] Liao, Steven and Daniel McDowell, 2015. “Redback Rising: China’s Bilateral Swap Agreements and Renminbi Internationalization”, *International Studies Quarterly*, Volume 59, Issue 3, 1 September 2015, pp. 401-422.

need for China and most other developing countries. Currency swap agreements are thought to be effective means for this purpose.

Although most of these bilateral swap quotas have not been drawn and executed, their symbolic value and function in stabilising financial markets are still important. Swap agreements could be regarded as the additional reserves of central banks and may discourage market speculation in cases of distress. On special occasions or under special conditions, increasing the swap amount could enhance the central bank's credibility so as to calm down market turbulence. For instance, in August 2018, when Argentina experienced financial market distress, the Argentine central bank asked PBOC to increase the existing bilateral swap quota from RMB 70 billion to RMB 130 billion. The agreement was reached on 2 December 2018 and helped Argentina to calm down market expectations.

As mentioned above, in some PBOC currency swaps with other central banks, there are clauses to allow the credit line to be used for trade and investment purpose. On 27 January 2013, Bank of Korea executed a currency swap agreement with PBOC and drew RMB 620 million to make a loan to Korea Exchange Bank. The latter then provided RMB loans to Korea companies for trade settlement. On 30 May 2014, People's Bank of China obtained KRW 400 million from the Bank of Korea and then loaned it to Bank of Communications to support the cross-border settlement between Korean Won and RMB in Seoul. Another case was when the Belarus central bank executed RMB 1 billion under swap agreement to provide RMB credit to their commercial banks and Belarus commercial banks then using the fund to support Belarus companies to import Chinese products. This sort of using of the central bank swaps is beyond the crisis-lending purpose that central bank currency swaps were supposed to fulfil. If swaps line becomes an export credit, it could lead to some problems, not only in disturbing PBOC's monetary policy operation but also in creating a new kind of moral hazard in using the credit line. Once the currency swap becomes loans for trade and investment purpose, the time period of loans and the risk assessment will be quite different from that of short-term liquidity provision for market intervention and crisis-relief purpose. The interest rate charged on currency swaps is usually the central banks' policy rate and lower than the commercial lending rate. This creates an incentive to use the currency swap line. If all the swaps are converted to this kind of usage, the potential risks need to be seriously considered. Until now, PBOC currency swaps have mainly focused on the financial safety net purpose and have not been largely deployed to promote trade and investment denominated by RMB. Even in promoting the Belt and Road (B&R) initiative, trade and investment project finances are mainly provided by China Development Bank and the Export and Import Bank of China. They are specialised in these kinds of finance and the relevant risk assessment. So, in practice, this kind of risk is controllable and only needs to be reviewed with case-by-case studies.

Some developing countries' economists tend to emphasise PBOC currency swap agreements together with China's intention of RMB internationalisation and have exaggerated the RMB competition with the US dollar hegemony. They quite often mention the creation of the Asian Infrastructure Investment Bank (AIIB) and RMB offshore market development and put them together with the PBOC currency swaps to sum up the trend that the RMB is going to be a competitor to the US dollar (Shen, 2014; Awan, 2018).[10] I think these comments show their wish to reform the current international monetary system and the role that RMB currency swaps could play in such a reform. But I believe that PBOC currency swaps and the promotion of RMB internationalisation are not aimed at competing with the role of the US dollar. PBOC currency swaps is only playing a supplementary role to the six western countries' central banks currency swaps that are not extended to developing countries. China benefits from the stability of the international monetary system and hopes to make a contribution to regional and global financial market stability. China's initiative to create the AIIB and to actively support the BRICS New Development Bank are aimed at providing additional development finance besides those of the World Bank and the Asian Development Bank but not at undermining existing institutions and systems. China believes that there are positive roles for emerging market economies to play in global economic governance, especially in the realm of international finance. If possible, China will enhance the bilateral swap line and also participate in the six developed countries' currency swap network.

4. HOW TO ENHANCE THE ROLE OF STABILISING FINANCIAL MARKETS BY CENTRAL BANKS CURRENCY SWAPS?

The quick development of bilateral central bank currency swaps provided a supplementary safety net parallel to the multilateral framework based on the IMF, but also created potential problems. The coordination between the IMF and bilateral swap lines is mentioned frequently by many scholars. In theory, bilateral swaps should be more flexible in usage prior to IMF financial help. In reality, when there is a need for crisis-relief finance, the IMF still plays a more important role. In a few

[10] Shen, Andrew, 2014. "Central Bank Currency Swaps Key to International Monetary System", *East Asian Forum,* 1 April 2014. Awan, Zamir Ahmed, 2018. "Currency swap good for Developing Countries", Center for China and Globalization, http://www.sohu.com/a/277918997_828358, accessed 14 February 2019.

cases, currency swaps provided timely liquidity help, enough to relieve market stress. Hence, some scholars suggested that the IMF and G20 should play a coordination role and provide global level governance on central bank currency swaps (Rhee et al., 2013; Destais, 2014).[11] How to enhance the role of the IMF and G20 in this regard? I think it would be difficult to make the IMF the clearing house of bilateral central bank currency swaps as some have proposed. The US FED-led six central banks swaps and other central banks' swaps all have their special purposes and the IMF is not capable of providing the function of a wider range of clearing and settlement. What is possible is to take a first step to entrust the IMF to get all central bank swaps' information and to make the IMF a watcher and supervisor of all central bank currency swaps. Similar to the obligation on WTO members to report their Free Trade Arrangements (FTAs), all members of the IMF should report their central bank currency swaps to the IMF. At present, most bilateral and regional swap agreements are not transparent and the terms and conditions for the swap agreements are not quite clear to others. Obligations under a swap agreement are not subject to any international organisation's supervision and governance. So the IMF and G20 could establish some basic guidelines to enhance the transparency and based on this, the IMF could consider providing coordinating finance when a swap is activated under financial distress conditions. With this kind of coordination, crisis-relief financing will be more effective.

Central bank swaps is going to become like the FTAs of recent years. It has spread widely as a means for bilateral or regional economic cooperation. In some cases, swap agreements also serve as instruments for geopolitical or geo-economic purposes. Like FTAs, swap agreements overlapping is inevitable. Central bank swaps are multifold in some regions. For example, the CMIM is a comprehensive swap agreement of ASEAN+3 countries while many ASEAN members also signed bilateral swap agreements with China, Korea and Japan respectively. Theoretically, the more swap agreements one country has, the more financial safety it can potentially gain. However, as many bilateral swaps are conditional, overlapping swap agreements are not necessarily of the same quality and ease to execute. In order to enhance the role of central bank swap agreements, I think swaps can be divided into two categories. One is related to promoting trade and investment and the other for crisis relief. The first one could be used more flexibly and could be embodied in FTA agreements. The second one is strictly to be used for financial market stability

[11] Rhee, Changhyong, Lea Sumulong, Shahin Vallee, 2013. "Global and Regional Safety Network: Lessons from Europe and Asia", *Bruegel Working Paper* 2013/06，November 2013; Destais, Christopher, 2014. "Central Bank Currency Swap and International Monetary System", *CEPII Policy Brief*, No. 2014-15, September 2014.

and should be coordinated with the IMF for collaborative fund arrangements. The main international currencies countries' central banks should consider extending their swap network to more emerging market central banks and to create a safety net with a wider range.

Xu Mingqi is senior research professor of International Economics at Shanghai Academy of Social Sciences (SASS). He is the Director of the Centre for European Studies at SASS and the President of Shanghai Institute for European Studies. He also serves as Secretary General of Shanghai Research and Coordination Centre for Free Trade Zone Studies. He graduated from Shanghai Academy of Social Sciences with MA and Ph.D Degree and was awarded a scholarship by the Chinese government to conduct visiting research in University of Western Ontario, Canada in 1987-1988, and Harvard Yenching Scholarship to do post-doctoral research at Harvard University in 1995-1996.