

Analysis of the relationship between the RMB exchange rate and China's bilateral investment

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Abstract

This paper examines the economic impact of RMB exchange rate movements and bilateral investment on countries along China's Belt and Road Initiative from 2009 to 2020. It is found that the exchange rate fluctuation of RMB countries will have a significant impact on the economic indexes of the countries along the Belt and Road, such as import and export, debt scale, and there is a threshold effect. When the exchange rate rises and the RMB appreciates, China's outbound investment increases and foreign investment decreases, and vice versa. When the exchange rate fluctuation range is lower than the threshold value, its impact on the host country is obviously greater than that when it is higher than the threshold value. Therefore, it can be concluded that when promoting the "Belt and Road" initiative, China should stabilize the exchange rate of RMB, accelerate the internationalization process of RMB, pay attention to optimize the investment structure and trade layout, and coordinate development with the countries along the "Belt and Road".

Keywords

Belt and Road; bilateral investment; RMB exchange rate.

1. Introduction

There are many countries along the Belt and Road, but there are big gaps in economic development, resource sharing and institutional environment among them. Various experts and scholars have not reached a conclusion on the interaction between the Belt and Road and bilateral investment. At the same time, studies on how RMB exchange rate fluctuations affect Chinese enterprises' overseas direct investment under the Belt and Road Initiative have not yet reached a systematic conclusion. This paper takes the countries along the Belt and Road as research samples to conduct research on the relationship between the two, which is helpful to explore the path of China's direct investment in the countries along the Belt and Road, and also to put forward policy suggestions for further promoting the construction of "The Belt and Road" and promoting the growth of China's foreign investment.

2. Research background and significance

2.1. Research background

The "Belt and Road" refers to the "Silk Road Economic Belt" and the "21st Century Maritime Silk Road". The purpose of the "Belt and Road" is to make use of the historical symbols of the ancient Silk Road, hold high the banner of peaceful development, and establish economic partnership with countries along the routes. Let us build a community of shared interests, shared future and shared responsibilities featuring political mutual trust, economic integration and cultural inclusiveness. Since the opening up of the Belt and Road Economic Zone, more than

3,000 projects have been contracted. In 2015, Chinese companies made direct investment in 49 countries related to the Belt and Road Initiative, up 18.2 percent year on year. [1] At the same time, in view of the existing literature, domestic and foreign academic circles have conducted in-depth analysis on exchange rate fluctuations, OFDI and the relationship between them, and formed a wealth of research results, but no unified conclusion has been formed yet. There is still room for expansion and improvement as follows: Most academic circles take developed countries as the main research objects. However, there are relatively few literatures that study the relationship between the two with developing countries as the object, especially those that study the exchange rate changes of RMB against currencies of countries along the Belt and Road. Therefore, this paper focuses on the mutual influence of currency exchange rates of countries along the Belt and Road on bilateral investment.

2.2. Research significance

Service and implementation of national strategy, this study is conducive to enriching the connotation of the Belt and Road, improving the quality of the construction of the Belt and Road, and constantly finding problems in the process of implementation, put forward reasonable suggestions and solve problems. China has always been the image of a responsible big country in the world. The Belt and the Road has played a further role in promoting China's "going out" strategy, to make more countries know about China, feel the enthusiasm of China for other countries and the development and changes of China. At the same time, the Belt and Road Initiative also plays a significant role in promoting the internationalization of RMB. Trade settlement and transactions in the Belt and Road Initiative will be settled in RMB, thus reducing the use of third-party currencies such as US dollar. In this way, the status of RMB in the international monetary system is greatly improved, and the role of RMB exchange rate is stabilized to some extent. In the process of studying the internationalization of RMB in the Belt and Road Initiative, the interaction between the effectiveness of RMB exchange rate policy in the Belt and Road Initiative and bilateral investment can be further explored. Therefore, it further puts forward the methods and suggestions on the influence of the Belt and Road on RMB exchange rate.

3. Theoretical basis and mechanism of action

3.1. Bilateral investment Treaty (BIT)

Bilateral Investment Treaty (BIT) refers to a series of special agreements or clauses signed by two countries to promote mutual investment. It is the most extensive international treaty in the world at present. By signing relevant agreements, foreign investors have different rights from domestic investors. In case of disputes, good mechanisms can be used to adjust, so that the interests of foreign investors are not harmed. Signing bilateral investment treaties has become an important way for countries to attract foreign direct investment (FDI). Bilateral investment treaties, as an investor protection mechanism, will also have a very important impact on the layout of OFDI. The BIT covers access conditions, preferential treatment, taxation, and settlement of investment disputes among the participating countries, as well as various matters related to bilateral investment. These terms and regulations are undoubtedly good news for investment, which will greatly attract investment and imperceptibly improve investment quality and level. This is a good thing for the host country, which will get a certain degree of development of infrastructure and stimulate the continuous development of local economy. For the home country, foreign investment will enhance its national influence and further promote the international influence of investment enterprises, which is of great benefit to both sides. In the process of the Belt and Road development, our country has also actively signed a BIT with other countries, further increasing the protection of trade interests and rights between the two countries. Through the signing of bilateral investment treaty, bilateral countries can further

trade with each other and enhance the sense of trust between countries, which is of great significance for the stability of RMB exchange rate in the international exchange rate market and the internationalization of RMB. It will also play a key role in promoting the development of the Belt and Road Initiative, which in turn will affect the stability of RMB exchange rate. According to the research results of relevant literature, from the national level, there is a long-term co-integration relationship between RMB real effective exchange rate and its fluctuations and FDI.

3.2. Influencing factors of exchange rate fluctuations

All foreign exchange transactions are made from one currency to another. At any given moment, the actual exchange rate will be determined primarily by the supply and demand of the corresponding currency, so factors affecting the supply and demand of the currency will affect the exchange rate. Its factors mainly include: monetary policy, interest rate factor, inflation factor, political factor, speculative transaction, international balance of payments, market psychology factor, emergency. At the same time, exchange rate changes also include other influencing factors, such as carry trade, Dow Jones index, gold, oil and so on. In the balance of payments, the total amount and balance of imports and exports is an indispensable part, which has a very strong response to the changes of the RMB exchange rate, so the total amount and balance of imports and exports and their changes can effectively reflect the RMB exchange rate. In a sense, the import and export income will also have a certain impact on the supply of funds in the foreign exchange market, which will have a significant impact on the current fluctuations and future trends of the exchange rate. No matter the appreciation or depreciation of RMB, it will directly reflect the amount and scale of foreign investment, and the actual utilization of foreign investment is also greatly affected by the fluctuation of RMB exchange rate. Therefore, the actual use of foreign capital can fully reflect the current fluctuations and future trends of RMB exchange rate. Many other scholars have made interpretations based on the two decision theories of purchasing power parity and interest rate parity, and formed corresponding conclusions, which are of important reference significance when analyzing the changes of RMB exchange rate and bilateral investment of the Belt and Road.

3.3. Influencing factors of foreign investment

The influencing factors of foreign investment can be divided into host country and home country. There are obvious industrial and regional differences in the entry control of infrastructure in the "Belt and Road" countries. Among them, the intensity and mode of entry control in the host country's infrastructure sector will reduce the scale and willingness of Chinese enterprises to invest abroad by increasing the transaction cost of Chinese enterprises to enter the market. The empirical analysis of China's outbound investment behavior shows that the infrastructure entry control of "One Belt and One Road" countries will significantly reduce the scale and investment intention of China's outbound investment in "One Belt and One Road" countries, especially the willingness of enterprises to enter in the form of greenfield investment, indicating that the host country's entry control will restrict the infrastructure investment cooperation between China and "One Belt and One Road" countries. Meanwhile, it is not conducive for Chinese enterprises to choose greenfield investment to carry out investment activities. The influence factors of home country include national policy factors, enterprise development strategy and so on. National policies support foreign investment and create a good investment atmosphere. For example, the promotion of the Belt and Road Initiative will enable enterprises to carry out active investment activities under the guarantee of the state. At the same time, corporate strategy will also have a certain impact on investment activities. The formulation of corporate expansion strategy will further promote the popularity of foreign investment.

4. RMB exchange rate fluctuations and the development trend of China's bilateral investment

The fluctuation of RMB exchange rate will be affected by many aspects. On the one hand, it will be affected by the above mentioned changes of supply and demand relationship, import and export balance and actual utilization of foreign capital. The development of the Belt and Road will make countries use RMB for settlement, and then the demand for RMB will increase and the RMB will appreciate, and the exchange rate will show an upward trend. At the same time, bilateral investment brings about changes in China's import and export balance and actual utilization of foreign capital, so the RMB exchange rate will also change to a certain extent. On the other hand, changes in domestic and foreign forms will also cause changes in the exchange rate of RMB. In recent years, our country has fully entered a well-off society, is building toward a prosperous, democratic, civilized, harmonious and beautiful great modern socialist power, our investment environment is good. At the same time, the development of our country also leads to the continuous development of world peace and the international situation and tends to be stable. With the development of the Belt and Road, the economies of the countries along the Belt and Road have developed. More countries see the image of China as a responsible country, and people's trust in China has increased, so more RMB is used for settlement, thus increasing the RMB exchange rate. To sum up, the RMB exchange rate will show a rising trend. The stability of RMB exchange rate is good news for both domestic and foreign enterprises, which will encourage more Chinese enterprises to invest abroad, because they can get more welfare at this time, which will encourage them to increase investment. On the other hand, a rising exchange rate would reduce foreign investment somewhat, but it would be offset by more foreign investment. Overall, China's bilateral investment will still increase to a certain extent. Relevant studies also show that there is a negative impact between exchange rate and foreign direct investment, and there is a long-term relationship between the two. The relative depreciation of RMB will increase the scale of foreign direct investment, while the relative appreciation of RMB will reduce the scale of foreign direct investment, and the impact will be delayed four periods. In addition, foreign direct investment is also affected by domestic industrial structure adjustment and upgrading, financial development level, economic development level and other factors, and there is also a long-term relationship.

5. Research conclusions and policy recommendations

5.1. Conclusion

RMB exchange rate has an important interaction with foreign bilateral investment. The stability of RMB exchange rate will promote the growth of bilateral investment. In turn, the development of bilateral investment will further promote the stability of RMB exchange rate. The two influence each other and promote each other. Therefore, when promoting the Belt and Road Initiative, China should stabilize the RMB exchange rate, speed up the RMB internationalization process, focus on optimizing the investment structure and trade layout, and coordinate development with countries along the Belt and Road.

5.2. Policy suggestions

At present, our country is promoting the development of domestic and foreign large circulation, while the domestic and foreign large circulation pattern has already taken shape, therefore the foreign direct investment as the important part of foreign circulation, has an important significance to the development of international circulation. Although the domestic cycle has been weakened by the impact of the epidemic, its main process is still going on. In the past six months, the domestic cycle has also been recovering and further developing in a good

momentum with the improvement of the domestic and foreign epidemic. Based on the discussion and research of RMB exchange rate and bilateral investment in this paper, the following suggestions and countermeasures are put forward.

1. Reasonably control the fluctuation of RMB exchange rate and further stabilize the RMB exchange rate. In the foreign exchange market, efforts should be made to maintain the stability of the RMB exchange rate, and both macro and micro methods should be used to play their role. In the process of the development of the Belt and Road, while pursuing economic benefits, enterprises also pay more attention to the stability and sustainability of trade. At the same time, the government should strengthen the financial support for enterprises "going global", solve the problem of industrial financing difficulties of individual enterprises, so as to promote the construction of the "Belt and Road". Reasonable control of RMB exchange rate can make relevant trade enterprises have certain psychological expectations and adequate preparation for countermeasures.

2. Further support from national policies, especially for financial development. Capital circulation is a necessary condition for economic development. If you want to be rich, first build roads. Capital is like a highway in the process of getting rich. When the speed of capital circulation is accelerated, an enterprise will have vitality, and then it can better carry out all aspects of work. And an important means to promote the circulation of funds is that the financial policy should have enough support. Therefore, the support of national financial policies will further promote the development of the Belt and Road. When formulating financial policies, it is necessary to fully understand the local customs, adapt to the local market, downplay the colors of the home country, and formulate financial policies suitable for the local area, so as to further promote the investment enterprises to take root and sprout in the local area and have the ability of sustainable growth.

3. The continuous stability of domestic economy will promote the development of bilateral investment, and the stability of domestic economy will make enterprises have confidence in economic development, which will increase the desire and enthusiasm for investment, and further promote the development of domestic and foreign economy. At the same time, further coordination by the government will make the development of enterprises orderly and steady. This in turn enables orderly and high-quality economic development. Corporate image also plays an important role in bilateral investment. In countries along the "Belt and Road", Chinese enterprises should maintain a high quality image, which is conducive to the smooth development of their local investment activities. Chinese enterprises should make investments on the basis of respecting local customs and protecting local natural environment, so as to establish a responsible image as a major country enterprise.

4. The government will actively take service measures for bilateral investment and build a service-oriented government. The government should build and improve our unique database based on the existing data, so as to provide more precise risk warning, scientific protection and guidance for Chinese enterprises investing in countries along the Belt and Road. International risk assessment will be conducted for major countries along the Belt and Road, and specialized investment environment analysis will be conducted for participating countries to provide scientific decision-making guidance for foreign investors. In areas with high investment risks, the government should give full play to the advantages of information resources, build investment service platforms, provide adequate information for enterprises, further improve the security system, and minimize the investment risks of Chinese enterprises in countries along the Belt and Road.

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