

Research on RMB Depreciation and Its Impact on Chinese Corporate and Society

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Abstract: Raising interest rates by the Federal Reserve forces global capital flows to the US market, which in turn causes other countries' economic growth to slow or currency to depreciate. China has been inevitably affected by the Fed's higher interest rates, which have led to the devaluation of the RMB and have had a negative impact on the normal operation of Chinese corporations and society. Therefore, this paper analyzes the impact of RMB depreciation caused by the Federal Reserve interest rate hike on China through literature review and case analysis. Through research, the Federal Reserve adopted the policy of interest rate increases to force the Chinese government to tighten its internal monetary policy while continuing to promote the internationalization of the RMB, which in turn caused the depreciation of the RMB. Export-oriented enterprises can avoid interest rate risk caused by RMB depreciation through financial means, and the overall advantages outweigh the disadvantages. However, the depreciation of the RMB has increased the costs of cross-border e-commerce, Chinese tourists traveling overseas, and studying abroad, and the overall disadvantages outweigh the advantages.

Keywords: Federal Reserve interest rate hike, RMB exchange rate, RMB depreciation, corporate impact

1. Introduction

Given the US's dominance in the global economy, the Federal Reserve's monetary policy has a highly consequential influence on the global economy. Since this rate hike cycle, the Fed has raised interest rates a total of 10 times. The continuous pace at which the Federal Reserve raises interest rates has forced many countries to follow suit in making monetary policy adjustments. For multiple reasons, such as curbing inflation and stabilizing the currency exchange rate, major developed economies followed the United States into the interest rate hike cycle in order to maintain macroeconomic stability [1]. However, China and its government have made a dramatically different choice regarding exchange rate adjustments than other countries. While the Federal Reserve keeps announcing raising interest rates, China's central bank has announced that it has adopted interest rate reductions for the RMB. As of July 6, 2023, the exchange rate of RMB against the US dollar has broken through 7.2, with a cumulative depreciation of more than 5,000 points. The US dollar raised interest rates, and the RMB interest rate reduction is one of the main reasons for the depreciation of the RMB. The depreciation of the RMB has also had a more serious impact on the daily operations of Chinese enterprises as well as Chinese society and people. Therefore, the

research topic of this paper is the impact of RMB depreciation on the enterprise society, and the impact of the exchange rate change on enterprises through case analysis. Through the analysis of the existing case studies, theory and practice are combined to make a comprehensive, multi-directional research. From the specific content and other aspects of in-depth analysis, getting the relevant experience and enlightenment to the corporate society.

2. Reasons for the RMB's devaluation

The causes of RMB depreciation can be generalized into external and internal factors.

2.1. External factors

One of the main external factors is the repatriation of the United States dollar to the United States mainland through monetary policy. The Federal Reserve has adopted a policy of interest rate increases (tightening the monetary policy) to tighten the money supply by raising the interest rate on domestic currency in order to control domestic inflation and the economic growth rate. Since the 21st century, the East-West trade war has led to a rise in American commodity prices and a further increase in inflation. In addition, the Russian and Ukrainian conflicts have led to the transmission of inflation from daily commodities to the real estate market, which in turn has caused real estate prices to skyrocket. As a result, the US needed to control inflation by continuing to raise interest rates and, in the process, reducing its own Treasury sovereign debt. The Fed affects interest rates by issuing short-term treasury bonds in money markets, setting bank reserve ratios, lowering lending ratios, and reducing the number of dollars circulating in the market. With the reduction of dollars in circulation in the market, the purchasing power of the dollar has increased, the value of the currency has increased, and eventually the dollar has appreciated. For investors, the higher interest rate on the dollar and the appreciation of the dollar prompted investors to sell other currencies, such as RMB, and use them to buy the dollar. With more and more RMB in the market, eventually the RMB depreciated.

2.2. Internal factors

One of the internal factors contributing to the depreciation of the RMB is a series of monetary policy measures taken by the Chinese government. The Chinese government tightened regulation of the domestic currency and adopted a tightened monetary policy to curb economic the impact of economic risks such as asset bubbles. However, these policies have exacerbated the recession through capital repatriation and reduced foreign investment. In addition, in recent years, the Chinese government has promoted the internationalization of the RMB and gradually liberalized foreign exchange controls [2]. While these measures help to enhance the international status of the RMB, they may also have some impact on the RMB exchange rate due to changes in the international economic situation.

On the other hand, from the perspective of economic cycles, as the economic cycles between China and the United States are opposite, China's central bank chose to lower interest rates to stimulate China's economic growth in the face of the Federal Reserve's continuous interest rate hiking behavior, thus increasing the circulation of the RMB in the market. However, as the amount of RMB circulating in the market increased, the RMB depreciated.

Furthermore, the weakness of China's economy caused by the epidemic has long been regarded as the main internal reason for the depreciation of the RMB. However, a comparison of China's GDP with that of other countries reveals that although China's economic growth rate shows a slow trend, China's GDP growth rate is significantly higher than that of other countries. China's GDP growth rates in the first three quarters of 2023 were 4.5%, 6.3%, and 4.9%, respectively, while the

GDP growth rates of the United States, Japan, and the United Kingdom in the same period of 2023 were significantly lower than those of China (Figure 1). Therefore, from a data perspective, China's economic situation is still in a state of positive growth compared to other countries, and is not the main reason for the depreciation of the RMB.

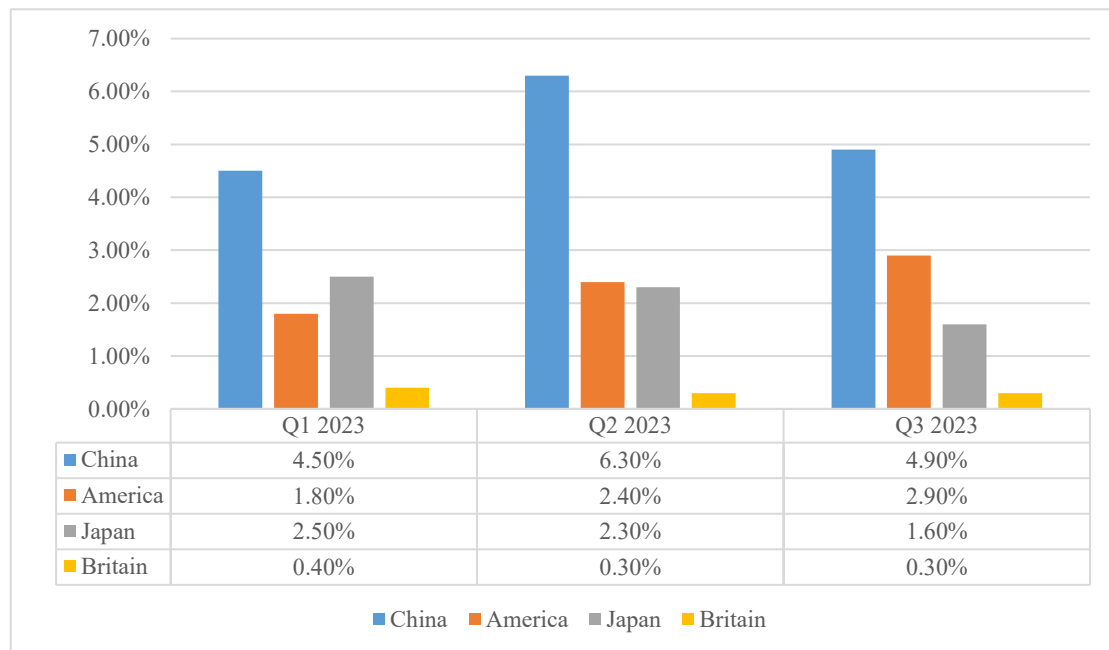


Figure 1: Comparison of GDP growth rates among China, America, Japan, and Britain in the first three quarters of 2023[3]

3. The impact of RMB depreciation and the corresponding measures

3.1. Export-oriented enterprises

The depreciation of the RMB has more beneficial than detrimental effects on export-oriented enterprises. When the RMB depreciates, exporters can sell their products at lower prices, and have more price advantage in the international market. And, when the RMB depreciates, the foreign exchange income will increase with the depreciation of the RMB, which improves the profitability of export enterprises [4]. In this case, export enterprises can reduce costs and carry out mass production. As the number of export products increases, the profit opportunities of enterprises will further increase. Taking Keystone Electrical, an export-oriented foreign trade enterprise, as an example, the depreciation of RMB brought obvious exchange income and overseas competitiveness to the company. Keystone Electrical mainly provides power tool products for overseas customers, and its revenue mainly comes from overseas markets. The proportion of the company's overseas sales revenue to the company's total sales revenue will be 85.05%, 83.74%, and 90.34%, respectively, in the period 2020-2022 [5]. The proportion of sales revenue from overseas markets is relatively high, and the dependence on overseas markets is expected to remain high in the future. The depreciation of RMB has improved the price competitive advantage of export enterprises, and the overseas income of export businesses is also expected to benefit from the exchange income, further increasing the profits of export enterprises. The expansion of exports by export enterprises will also have a driving effect on economic growth.

In addition, export-oriented enterprises can control or reduce the risk of the negative impact of RMB depreciation on foreign trade enterprises through a series of measures. Hamaton Automotive

Technology Company is also a foreign trade enterprise mainly engaged in export business, and the company's export business accounts for about 88%. Due to the uncertainty of exchange rate fluctuations, the company has adopted a series of exchange rate hedging measures to reduce the impact on the company's profits, such as the choice of self-interested currency settlement, early or delayed foreign exchange settlement, and sale methods [6]. Therefore, on the one hand, export enterprises can avoid the risk of exchange rate fluctuations and currency depreciation by delaying delivery, delaying payment, advance payment, and opening long-term letter of credit for financing. On the other hand, export enterprises can choose exchange rate preservation products to actively manage the exchange rate risk. Reducing the impact of exchange rate fluctuations on enterprise finance can increase the predictability of financial costs, thus avoiding the impact of large exchange rate fluctuations on financial costs.

3.2. Cross-border e-commerce

For Chinese cross-border e-commerce, the depreciation of RMB means the relative increase of overseas goods, so the price of imported goods becomes more expensive, which directly affects the operating cost of cross-border e-commerce [7]. In addition, a depreciation of the RMB makes orders more expensive to pay for using the RMB. In this case, consumers may consider buying domestic products and abandoning cross-border shopping. Therefore, the depreciation of the yuan is a big challenge for cross-border e-commerce. In the face of this challenge, cross-border e-commerce can strengthen procurement and supply chain management, expand the domestic product market, build brands, carry out diversified payment methods, and find other ways to deal with the crisis, so as to improve their profitability and achieve sustainable development.

3.3. Tourism

The depreciation of RMB directly leads to an increase in the cost of outbound tourism, thus, the price of overseas tourism products increases, which is not conducive to the healthy development of outbound tourism. At the same time, the purchasing power of Chinese tourists overseas also declines with the depreciation of the RMB, thus leading to a decrease in overall consumption [8]. But this is beneficial to the development of tourism within China, and domestic consumers will be more inclined to prioritize domestic destinations for vacation and travel. Moreover, the depreciation of RMB means that the cost of foreign tourists traveling to China is reduced, thus attracting more foreign tourists to stimulate the economic growth of China's domestic tourism industry.

3.4. Overseas study and education

For overseas students, the depreciation of the RMB means that the amount of foreign currency that can be exchanged for the same RMB is less than before, and therefore the tuition fee and living cost for studying abroad will be much higher compared to before. The increased cost forces many students and families who originally planned to study abroad to choose other ways to enhance their academic background. For students and families who are already studying abroad, the plummeting of RMB will cause some parents of international students to panic, thus exchanging more foreign currencies in a short period of time, leading to a rise in the amount of exchanged US dollars [9]. Faced with this problem, international students can cope with the possible increased cost of studying abroad by exchanging US dollars in advance. At the same time, international students also need to pay more attention to the changes in the exchange rate market, so as to reserve more foreign exchange for the subsequent living expenses and tuition fees in a suitable time.

4. Conclusion

Due to the impact of the epidemic, global economic development has been sluggish in recent years, and the economy is still slightly weak after the liberalization. In this context, substantial changes in the currency are also a policy means to stimulate economic development, such as the appreciation of the US dollar and the reasonable depreciation of the RMB. The change of currency has both advantages and disadvantages for the operation of enterprises and the lives of all sectors of society. In China's economic system, export, and foreign trade are one of the key factors, so depreciation has certain benefits to export enterprises, but this requires the attention of the negative impact of depreciation on the domestic economy, inflation, foreign exchange reserves and other aspects while formulating appropriate monetary policies and regulatory measures.

Although this paper analyzes the influencing factors of RMB depreciation and the impact on different industries, the information sources are mainly based on the existing literature and lack the support of relevant empirical data. Moreover, the analysis of the impact of RMB depreciation on enterprises only investigates a few enterprises, the conclusion may have a certain one-sidedness. Considering the development trend and long-term impact of the economy, more in-depth field investigations will be carried out on the impact of RMB depreciation on all aspects of society in the future, and the correctness of the conclusions and the feasibility of the depreciation measures will be verified combined with a large number of actual cases.

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