KGRI Working Papers

No.2

A Cautionary Tale of Market Power and Foreign Policy: Beyond the Geoeconomics of Renminbi Internationalization

Version1.0

March 2017

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Abstract

This paper attempts to spark a policy discussion on the effects of China's renminbi internationalization and foreign policy. Defining China's market power as a form of structural power in geopolitics backed by China's consumption power, it unravels the ramifications of renminbi internationalization based on China's market power beyond the geoeconomic perspective. It argues that, such ramifications are an outcome of the strategic bind that has been gradually developed by China and its trading partners via economic transactions, owing to the market power that China possesses. Such binds are often asymmetric in bilateral relations, and increase China's bargaining leverage in foreign policy used for wielding power on the global stage. The paper therefore emphasizes that renminbi internationalization should not be simply considered as China's earnest efforts toward global currency diversification to assuage the side-effects of the dollar dominance, but rather be understood as a subset of China's global strategem, in which the renminbi is translated into a medium of power projection for Chinese foreign policy. The paper presents two case studies of renminbi internationalization – *a)* electronic payment services via *China UnionPay*, and *b)* oil transactions denominated in renminbi and the sale of China's renminbi-denominated oil futures that signal to the beginning of the end of the petrodollar dominance that has existed for decades since the 1970s.

Keywords: market power, foreign policy, electronic payment services, petrodollar, renminbi

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I. Introduction: Why the Cautionary Tale?

In the midst of the renminbi's gradual rise, we often fail to question its externalities or consequences outside the economic spectrum – the ramifications of the renminbi's full or partial convertibility in the future beyond pure economic impacts. But the renminbi's influence on foreign policy could be larger than expected. The lack or avoidance of discussion on non-economic impacts of the renminbi stem from the reluctance to assume anything else besides the dollar standard as the predominant setting in the global financial system, which has been the primary mode of international financial transactions since the breakdown of the Bretton Woods system. We also refrain to assume the kind of world in which the renminbi plays a significant role equivalent to other key currencies. In contrast, there is a widespread recognition of China's trade volumes. While China's trade policy is often accompanied by warnings of its consequences, its policy on renminbi internationalization does not go that far nor gathers as much attention - because we fail to assume a world in which the dollar is significantly challenged by another currency. In turn, the renminbi's inclusion in the International Monetary Fund (IMF)'s special drawing rights (SDR)[2] is often viewed only as a symbolic change to the existing global monetary system, as the proportion of the renminbi in the currency basket is still very minimal and the currency plays a minor role in the context.

The renminbi's rise is an admirable achievement in that, its value has risen as a result of China's rapid economic development in a relatively short span of time, and has begun to play a significant role in China's recent projects that are transforming the global economic order. The launch of the Asian Infrastructure Investment Bank (AIIB) and the OBOR (One Belt One Road) initiatives are the most notable projects associated with internationalizing the renminbi.[3] Thus far, the dominant view in evaluating renminbi internationalization is that, at a glance, with the renminbi constituting about 1.1 percent of official reserves around the world (the dollar is at 63.7

[2] On October 1, 2016, the Chinese yuan (hereafter renminbi) officially joined the Special Drawing Rights (SDR) basket of currencies designated by the International Monetary Fund (IMF). Along with the US dollar, the Euro, the Japanese yen, and the British pound, the renminbi became part of SDR that can be exchanged for freely usable currencies. The decision toward the international acceptance of the renminbi was reached after years of China's lobbying within the international organization, spearheaded by Zhou Xiaochuan of the People's Bank of China (PBOC). Zhou's argument in a 2009 essay pointed towards the inherent vulnerabilities of the international monetary system largely dominated by the US dollar. Currently, the yuan enjoys the third-largest weighting in the IMF's SDR at 10.92 percent of the whole basket. See IMF SDR (http://www.imf.org/external/np/exr/facts/sdr.htm).

[3] OBOR began with an official statement by Xi Jinping in Kazakhstan on September 7, 2013. (http://www.fmprc.gov.cn/mfa_eng/topics_665678/xjpfwzysiesgjtfhshzzfh_665686/t1076334.shtml)

percent), and only 2 percent in currency trades involve the renminbi (as opposed to the dollar at 90 percent and the Euro at 40 percent), the renminbi has a long march toward internationalization.[4] [5]

This paper acknowledges the shortcomings of renminbi internationalization in global finance, but offers an alternative perspective by turning to the other side of renminbi internationalization – its effects on shaping China's foreign policy, backed by its market power. China's market power, in this context, can be defined as a form of structural power based on purchasing or consumption power, which empowers the Chinese authorities to utilize it toward other objectives – in large part for China's global strategy.

For a nation state, economic and financial policymaking are indeed inseparable, and are closely intertwined. Thinking about China's foreign policy agenda in accordance with its the renminbi's movements enables us to read into China's strategic mindset, and it is a task that is all the more essential for countries that are largely dependent on trade with China, as the understanding of China's motivations is required for policy responses to China's interventions. The point of argument here is that, although using the renminbi-denominated market power may not have been China's pure and original policy intent, China can indeed utilize it toward its foreign policy interests as the renminbi becomes internationalized toward full convertibility.

The paper proceeds as follows: following this introductory section, the second section develops the logic of China's market power as a foreign policy measure in geopolitics. The third section compares China's power projection via the renminbi with the US dollar domination and power projection in Asia. The fourth section provides case studies of China's renminbi internationalization that impacts geopolitics – via the electronic payment services *China UnionPay* and China's transactions for oil denominated in renminbi – or PetroYuan, which signals to the end of the petrodollar system. Finally, the concluding section provides policy

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[4] 'Renminbi as a reserve currency', Central Banking, August 11, 2014 (http://www.centralbanking.com/central-banking-journal/advertisement/2357296/renminbi-as-a-reserve-currency)

[5] According to international political economist Benjamin Cohen, a currency must be competitive in order to operate as an international currency. He elaborates on the criteria for international currency as the following: 1) widespread confidence in the currency's future value backed by financial stability in the country of origin, 2) qualities of "exchange convenience" and "capital certainty", and 3) the promise of a broad transactional network with the prospect of acceptability by others. See Cohen, B., 'Will History Repeat Itself? Lessons for the Yuan', in Eichengreen, Barry J., and Masahiro Kawai eds., Renminbi Internationalization: Achievements, Prospects, and Challenges. Tokyo: Asian Development Bank Institute/Washington DC: The Brookings Institution, 2005.

implications as to predicting China's geopolitical moves based on renminbi internationalization and responding to such moves from the Asian perspective.

II. The Logic of China's Market Power as a Foreign Policy Measure

The Projection of Market Power and the Role of the Renminbi

In economics, particularly in industrial organization (IO), market power is defined as a firm's ability to raise the price of goods or services above the marginal cost.[6] But market power in political science and international relations – particularly in international political economy (IPE) – is broader in concept than it is in economics. In the field of IPE, market power is directly associated with a state's political and economic capacity on the global stage. Market power is a form of structural power in geopolitics. In explaining structural power, Susan Strange makes it very clear that finance – the control of credit – is the facet which has come to be of decisive importance in international economic relations and in the competition of corporate enterprises.[7] Projecting market power requires the economic capacity of a state, and the recognition of such economic capacity by its trading partners. A state with the currency that is internationally recognized is able to project a significant level of market power in the global market. China has strived to achieve this goal since its entry into the global economy, although it still has ways to go in fully internationalizing the renminbi as a safe-haven currency that can overthrow the existing international monetary system that is dominated by the dollar. China is not the international 'lender of last resort', it may never be, and it will take time to confirm whether China wants to play such role, but it has been made clear by China's initiatives that it wants to increase its bargaining leverage globally using its accumulated reserves.

The definition of market power is important in explaining how China projects it and puts it to use. Simply defining China's market power requires looking at it from two angles: China's imports – manifested by its consumption power; and its exports – manifested by the competitiveness of their products. China's ability to consume resources – especially oil and gas – for continued economic development is a crucial component of its market power. China's export competitiveness is still questionable, as China's labor costs are on the rise, and despite the

[6] Tirole, J. p.284. Tirole distinguishes an economist's definition of market power from that of a policymaker, which generally means pricing above *average* cost instead of marginal cost.
[7] Strange, S. 1988. p.30.

incremental appreciation of the renminbi in recent years, China's relatively low price of goods largely depends on the renminbi-dollar exchange rate. Bearing the limitations of its financial market and dwelling on the time frame for increasing export competitiveness, China has pursued very rapid and aggressive promotion of its currency internationalization but with capital controls remaining, reflecting the Chinese government's recognition that they have yet to possess the full-fledged market power. For the purposes of analysis in this chapter, I consider the 'consumption power-based' market power.

Table 1. China's Recent Policies toward Renminbi Internationalization

Policy-Driven Efforts	*Market-Driven Forces*
-Bilateral Currency Swap (BCS) agreements to ensure liquidity of renminbi for trade and direct investment (33 swap agreements with foreign central banks worldwide)* -Promotion of cross-border trade and direct investment denominated in renminbi	-Pilot schemes set up for renminbi use in settlements -Direct renminbi trading with non-USD currencies -Offshore market renminbi (CNH, or Chinese Yuan traded outside the Chinese mainland) -Official renminbi clearing banks designated across 22 locations around the world**

* For a complete list of countries that have entered in a BCS agreement with China, see Aravind Yelery. 2016. "China's Bilateral Currency Swap Agreements: Recent Trends". *China Report.* 52 (2): 138-150. Also see Prasad's *'Gaining Currency'*, pp.138-139.
** The renminbi offshore clearing banks are located in Hong Kong, Macao, Taiwan, Singapore, United Kingdom, Germany, South Korea, France, Luxembourg, Qatar, Canada, Australia, Thailand, Malaysia, Chile, South Africa, Argentina, Zambia, Switzerland, United States, Russia, and United Arab Emirates (as of March 14, 2017).

The maintenance of capital controls by China in the course of renminbi internationalization is a big departure from most advanced economies that have liberalized their capital accounts.[8] In retrospect, taking the Japanese yen for instance, the amendment of Foreign Exchange and Foreign Trade Controls preceded the internationalization efforts, and the amendment of the Foreign Exchange and Foreign Trade Act ensued in 1998.[9] For the yen internationalization, Japan's moves were focused on convertibility of the currency and capital liberalization, but such moves were also accompanied by prolonged stagnation of the Japanese economy. What propelled China's efforts toward renminbi internationalization was the strong expectation of the

[8] Prasad, E. 2016. p.37.
[9] 'The New Foreign Exchange and Foreign Trade Law and Japan's Balance of Payments', prepared by the Bank of Japan for the Eleventh Meeting of the IMF Committee on Balance of Payments Statistics, Washington DC, October 21-23, 1998. (https://www.imf.org/external/bopage/pdf/121.pdf)

renminbi to appreciate. Nonetheless, expectations on renminbi depreciation have been on the rise, and the Chinese government has issued guidelines to limit capital outflows via issuing ten guidelines.[10] It is expected that a sharp change in the renminbi's international circulation would expose Chinese domestic financial markets to greater volatility.[11] In this regard, renminbi internationalization is far from stable and is largely dependent on the global economic shifts.

Beyond Geoeconomics: Market Power Projection as a Foreign Policy Tool for Global Strategy

Nation states today are engaged in geopolitical frictions and tensions, but not necessarily in full-scale combat involving human warfare. Since the Obama administration, drones were used in air strikes intended for minimizing human casualties has proved otherwise, and nuclear arsenal buildup is on the rise for deterrence in theory, but there is less and less guarantee for nuclear weapons to serve as mere deterrence tools. Instead, new forms of wars have emerged – economic wars such as cyber theft of commercial secrets via unchartered territories of cyberspace, or resource wars emanating from energy pursuits and climate change among environmentalists, developers of renewable energy and traditional forms of energy toward competition. The field of geoeconomics – the study of spatial, temporal, and political aspects of economies and resources – has been developing since the 1990s, since Luttwak coined the term geoeconomics as 'the logic of war in the grammar of commerce'.[12] Fast-forwarding to post-Global Financial Crisis of 2008, Blackwill and Harris have elaborated on the term by defining the statecraft of geoeconomics as 'the use of economic instruments to achieve geopolitical goals'. They argued that America's geoeconomic policies that were established post-WWII are hampered by neglect and resistance, making it overly reliant on its traditional military force.[13] Meanwhile, China is engaged in geoeconomic expansion via the OBOR and giving out loans via the AIIB, but it

[10] 'Capital controls the talk of China parliamentarians: Official blackout on widespread discussion of measures to stop outflow of money', *Financial Times*, March 9, 2017 (https://www.ft.com/content/0ece9690-048c-11e7-ace0-1ce02ef0def9)
[11] Research paper, Liu Dongmin, Gao Haihong, Xu Qiyuan, Li Yuanfang and Song Shuang International Economics Department, The 'Belt and Road' Initiative and the London Market – the Next Steps in Renminbi Internaitonlaization, Part 1: The View from Beijing, *Chatham House: The Royal Institute of International Affairs*, January 2017. (https://www.chathamhouse.org/sites/files/chathamhouse/publications/research/2017-01-17-belt-road-renminbi-internationalization-liu-gao-xu-li-song.pdf)
[12] Luttwak, Edward N. 'From Geopolitics to Geo-Economics: Logic of Conflict, Grammar of Commerce', *The National Interest*, No. 20 (Summer 1990), pp. 17-23.
[13] Blackwill and Harris, 2016. pp.23-24.

certainly does not limit itself to geoeconomic activities only.[14] By providing loans and economic deals through its initiatives, it forges ties with other nations – particularly those that stand against America, and secures energy for further economic development and to expand its military power. But none of such activities would have come about had it not been for the buildup of China's market power – mostly consumption power – post-WTO (World Trade Organization) entry. In other words, China's market power is an outcome of China's economic activities since 2001, which benefitted largely from the US-led neoliberal order and globalization. But it is no longer mere market power – it is now China's tool to bolster its foreign policy measures and affect other nations in their decision-making.

Domestically, China's state-led, geoeconomic initiatives and foreign policymaking is supported by China's market power is also reflected in China's joint ventures with foreign companies. Foreign firms that have vested interests in the Chinese market cannot afford to forego the attractiveness of the exponentially growing market that China offers, as consumption levels are on the rise. In turn, foreign firms that are bound by its Chinese market shares end up voluntarily or involuntarily contributing to China's market power projection overseas. China has been very proactive in developing its private sector, striving to develop its own standards for goods and services and to brand them under Chinese brands and labels, and has been proactive in launching cooperation schemes with multinational corporations (MNCs) for sectors that it needs improvement, particularly in sectors associated with science and technology. The economic interests that are intertwined between Chinese authorities that control the Chinese market and foreign entities at firm levels are the sources of core strengths of China on which it can build its power to compel others toward realizing its global strategy.

III. China's Power Projection in Asia via the Renminbi and Comparisons with the Dollar Dominance

China's Strategic Binds in Asia: From Economic to Security, From Regional to Global

China's expansion of power may be traced back to the very beginning of China's economic opening via Deng Xiaoping's economic reform in 1978. But strictly put, the paths toward

[14] 'FT investigation: Beijing has spent billions expanding its ports network to secure sea lanes and establish itself as a maritime power', *Financial Times*, January 12, 2017. (http://ig.ft.com/sites/china-ports/?segmentId=7005c83a-1f5c-33ca-66c5-ca8c9d224ab6)

renminbi internationalization were not clearly visible until China joined the WTO in 2001. China's global power projection via military means were accelerated only after the Global Financial Crisis (GFC) and economic downturn in the US in 2008.[15] China's impact on its Asian economies grew exponentially as it developed into a manufacturing powerhouse and became the dominant exporter of the region.

The GFC was a turning point in which China came to understand the fundamental shortcomings of the US economy and US global leadership.[16] Accumulating dollar reserves for financial crisis prevention proved to be less beneficial than originally expected. Moreover, China saw opportunity on upping its game on Sino-US trade as its bargaining power. In the aftermath of the GFC, on the basis of understanding that China would need and should pursue a financial system that adheres to its best interests in economic growth, it began to develop and exercise its monetary policy aligned with its global strategy. China began testing its diversification initiatives via accelerating the internationalization of the renminbi. Such initiatives led to the inclusion of the renminbi in the IMF SDR basket of currencies, and the launch of the AIIB. Albeit in a relatively smaller scale as opposed to the dollar, it increased its efforts toward expanding cross-border transactions denominated in renminbi.[17] These initiatives are clear indications that China would seriously pursue renminbi internationalization, in rebuttal to the dollar dominance in the global economy.

In all of these initiatives, China's top-down decision-making structure by the central leadership adds to the speed and power in pursuing its agenda and ulterior motives. But there are limitations, because China's ample foreign reserves alone cannot solve all the institutional issues. Taking the AIIB for example – the system of lending for infrastructure building that China pursues lacks mechanisms for audit and supervision, and relies on co-financing with the World

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[15] Coincidentally, the timing of China's power launch was met with the technology boom of platforms that began around 2007 with the release of the iPhone by the late Steve Jobs of Apple. This version of the paper will not dwell on technology spill-overs, but subsequent revisions will shed light upon how the technology sharing impacted Chinese entrepreneurs to rise based on platforms.

[16] Yong and Pauly, 2013.

[17] Cross-border RMB Settlements, *Mizuho Bank* (https://www.mizuhobank.com/service/global/cndb/rmb/pdf/cross_border.pdf).

Bank.[18] None of the applications for projects have been rejected by the AIIB thus far.[19] In other words, China is still in the early stages of exploring the methods of power projection through the use of renminbi, and is figuring out how to consolidate it. Meanwhile, it has decided and demonstrated through its actions that it would proceed with strategic military power projections in tandem with internationalizing its currency.[20]

US policymakers understand the need for China's economic reform, but the Obama administration was not successful in bringing out a strategic response to China's moves. The Asia Pivot, for one, ended in a failed attempt by the Obama Administration to bring out the best policy outcomes for the US and its Asian allies, both in economic and strategic terms. Because China's economic reform entails capital liberalization (albeit the remaining capital controls), and renminbi internationalization is part of it, the US sees as one of its mutual economic interests. With further capital account liberalization by China, US firms and investors will benefit from a more open environment for businesses operating in China.

Yet, there is a pushback factor – largely geopolitical and institutional – that lies in the US reluctance for full convertibility of the renminbi. The concerns regarding full convertibility range from anticipated worries on currency volatility and economic instability to bigger ones such as geopolitical expansion (i.e., the plausible control and blockage of the Straits of Malacca that would deter freedom of navigation in the South China Sea, and the construction of silk roads encompassing East and South, and Central Asia, as well as the Middle East and Europe - all in the context of China's energy pursuits and geoeconomic gains). Put another way, the US has come to welcome the renminbi internationalization in the context of China's domestic economic reform, but is reluctant to welcome China's dominance in global or regional finance. The US seeks to sustain the dollar dominance, and wants to refrain from allowing for full convertibility of the renminbi. It also does not think that China should be granted market economy status at the

[18] On a side note, China has come to realize that domestic market expansion is necessary and a departure from an export based economy. Although China's position in exports would be pursued for the time being, it quite clear that its foreign policy drives via the OBOR and the AIIB is also to resolve overcapacity issues in steel, metals, and other major (heavy) sectors of manufacturing.

[19] Personal interviews via Q&As on a lecture regarding the AIIB by an anonymous Thailand Ministry of Finance official regularly attending AIIB board meetings, Bangkok, Thailand, January 7, 2017.

[20] The attempted control over the South China Sea is a clear example of this endeavor.

current stage (the anticipated date that China would be given market economy status was December 11, 2016).[21]

America's Strategic Binds in Asia: From Security to Economics, as part of Global Strategy

In the postwar era, East Asian economies such as Japan and the Four Dragons - South Korea, Taiwan, Singapore, and Hong Kong – and certain Southeast Asian countries considered to be in line with Kaname Akamatsu's 'Flying Geese Model' were dependent on the US economy for development loans and trade.[22] But before mutual economic interests were met, many of the countries were heavily reliant on military ties with the US and were placed under the US nuclear umbrella via the 'hub-and-spoke' system that the US retained.[23] Under the US nuclear umbrella, country attempts to develop nuclear weapons were denied by the US government.[24] The US-led neoliberal order manifested in East Asia was based primarily on mutual security interests, as East Asia remained the hotbed of any potential conflict during the Cold War era. Building on the mutual security interests, the US deepened bilateral economic interests in the region in order to solidify the military ties, and East Asian countries benefitted tremendously (particularly Japan, South Korea and Taiwan) from US sponsored aid programs and investment in the postwar years. Japan, in particular, was discouraged from engaging in military activity excluding the operation of the self-defense force, and was expected to solely adhere to the Yoshida Doctrine. Instead, the US would guard the countries from military threats – although such guarantees were questioned by East Asian states at various points in time in their bilateral relationships. Amidst the cross-straits conflicts of the 1990s and the North Korean nuclear and missile threats from the 1990s and into the 2000s, the US alliance system as the military stronghold in the region remained intact.

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[21] For developing discussions on China's Market Economy Status, see details on the two rapidly developing WTO dispute cases, *DS471: United States — Certain Methodologies and their Application to Anti-Dumping Proceedings Involving China* (Complainant: China, December 3, 2016, https://www.wto.org/english/tratop_e/dispu_e/cases_e/ds471_e.htm), and *DS515: United States — Measures Related to Price Comparison Methodologies* (Complainant: China, December 12, 2016, https://www.wto.org/english/tratop_e/dispu_e/cases_e/ds515_e.htm)

[22] Akamatsu K. A historical pattern of economic growth in developing countries. Journal of Developing Economies, 1(1):3–25, March–August, 1962.

[23] Cha, 2016. In *Powerplay*, Cha explains that the US built bilateral security networks with Asian states as opposed to the aggregate form of security alliance system such as North Atlantic Treaty Organization (NATO) in Europe, due to the complex political landscape in Asia.

[24] Such cases include South Korea and Taiwan in the 1970s.

In sum, in the case of US power consolidation in Asia, mutual economic interests were met and pursued based on the foundations of security alliance that was served as the fundamental pillars of the bilateral relationships. US dominance in Asia evolved from security dynamics and spilled over to the economic arena. In the Chinese case, it was vice versa: mutual economic interests were met first, but security tensions remained, and military power projection followed suit. It took almost half a century for the US (from 1971 to present) to first consolidate a security architecture, then to exercise its economic power in tandem with the military pursuits. China is working towards what America accomplished in Asia but in a different path, in a reversed order – gaining recognition for its economic significance first, then adding geopolitical expansion to its economic stronghold, all in the scope of only a decade and a half (from 2001 to the present). While China's footsteps are not entirely a duplication of US power buildup in the postwar years, there are foreign policy ideals that China pursues for power projection by building a similar structure for itself in the global economy. For this reason, the ramifications of China's renminbi internationalization may be more than what is perceived only in the realm of global finance.

Superpower and Rising Power: The US-China Tension Buildup

There are two main critical junctures in the waxing and waning of US hegemonic power in the new millennium since China's WTO entry in December 2001. The first is the US decision to wage war against Iraq in 2003 in response to the 9.11 Terror. In the aftermath of the 9.11 terrorist attacks, the Bush Administration waged war against Iraq, citing the need to abolish the Saddam Hussein regime for developing the weapons of mass destruction (WMD). During the Iraq War, the US bilateral security ties with Japan and South Korea were fortified. In response to US requests to take part in the Iraq War, Japan's medical assistance groups and South Korea's military troops to be stationed in Erbil, Iraq. Japanese and South Korean civilian deaths in Iraq were minimal, but did occur, but the two countries did not engage further with Middle Eastern politics nor voice concerns in such a way that would hinder their alliance with the US. But the Bush administration's inability to find WMD and involvement in petroleum and military industries put American leadership under severe scrutiny, and US motivations and involvement in the Middle East conflict was looked upon with suspicion from the global community.[25] The Iraq War led to increased defense spending for the US economy and exacerbated the twin deficit (fiscal and current account deficits).

The second critical juncture for US hegemonic power post-China's WTO entry is the Lehman shock and the US economic downturn that led to the Global Financial Crisis from 2008. In the years leading up to the Global Financial Crisis, China's moves indicated that it would part ways with the US-led neoliberal order to a certain extent, by creating its own pathways based on its core interests. China's pursuit of an independent track was witnessed in the following moves: China issued the Panda bond – Chinese renminbi-denominated bonds issued by non-Chinese nationals to be sold within Chinese mainland for the first time in 2005; upon becoming weary of the US dollar accumulation in its official foreign exchange reserves, China created the China Investment Corporation (CIC) to manage China's sovereign wealth funds (SWFs) in 2007 and began to heavily invest overseas; and the launch of the 'indigenous innovation' (*zizhu chuangxin*) path for science and technology development to create China standards based on the 15-year *Medium to Long Term Plan for the Development of Science and Technology*. Tectonic shifts followed in the global arena – upon the inaugural leaders' summit in 2008, the G20 and its leaders announced on September 25, 2009 that the G20 would replace the G8 as the main economic council of wealthy nations, paving the way toward a multipolar international system. In the aftermath of the Global Financial Crisis, China began to engage with the US toward "cooperation" on a regular, bilateral basis in the US-China Strategic and Economic Dialogues from 2009.

Into the 2010s, the Chinese Communist Party (CCP) leadership seized the opportunity to push onward with domestic reforms to lessen China's heavy reliance on exports (with the US as the number one trading partner) and to adjust its foreign policy direction in accordance with the waning US leadership in the global arena.[26] In the aftermath of the financial meltdown, it dawned upon US policymakers that they were left with the task to work towards domestic economic recovery while also dealing with China. The US leaned towards "cooperating" with

[25] As an alternative view, while many American and foreign observers appear to think that oil (particularly oil producing states and oil companies as the real culprits) was the real motivation behind the invasion of Iraq in 2003, John Mearsheimer and Stephen Walt in 'The Israel Lobby and US Foreign Policy' (2004) have suggested that the critical driving forces behind the US Middle policy toward the Iraq War were Israel and the neoconservatives in the lobby.
[26] Yong and Pauly, 2013.

China by holding regular policy discussions and gaining economic benefit from the relationship rather than coercing China to succumb to US security interests. By this time, the US-China economic symbiosis since China's WTO entry had become extremely vital to US businesses, as US companies were heavily reliant on the Chinese market and US consumers were looking for cheaper products imported from China. The US government was also in a symbiotic bind with China financially, as China became the primary holder of US treasury bills.[27] China demonstrated its retaliatory measures in the WTO during this period against US trade protectionism.[28] However, because the bilateral economic relationship made the two economies dependent on each other, it was difficult for the Obama Administration to force China to adhere to US requests. On the security front, cautionary warnings were raised regarding China's military buildup and expansion of geopolitical influence within the Asia-Pacific region and beyond.

The turnaround of the US-led neoliberal order has come with the election of Donald J. Trump as the president-elect of the US on November 8, 2016 (sworn in on January 20, 2017). A dramatic shift is to come in foreign policy and domestic policymaking. As the election results started flowing toward the final vote count for the 2016 US presidential election, European and Asian stock markets went erratic, striving to absorb the shocks from the unexpected election results. Because the world (and Asian economies in particular) had bet entirely on Hillary Clinton's win, it took time for the markets to absorb the shocks from the election results. Asian local currencies went volatile – the Japanese yen plummeted and the Korean won plunged as opposed to the dollar. But it is with skepticism that such currency volatilities can be resolved by the renminbi's rise. What would happen if the renminbi rose to full convertibility and the local currencies responded frantically both to the dollar and the renminbi? What are the plausible impacts of the renminbi if it becomes fully convertible? The next section of case studies on market power and renminbi internationalization provide possible scenarios of the ramifications.

IV. Cases of Market Power in Renminbi Internationalization

[27] The US Treasury's December 2016 indicate Japan's holdings slightly ahead of China. (http://ticdata.treasury.gov/Publish/mfh.txt) In August 2016, China held more US treasury bills than Japan.
[28] For further details on the poultry and tires cases in the WTO DSB that ignited the US-China trade frictions during this period, see *DS392 United States — Certain Measures Affecting Imports of Poultry from China* (17 April 2009, https://www.wto.org/english/tratop_e/dispu_e/cases_e/ds392_e.htm) and *DS399 United States — Measures Affecting Imports of Certain Passenger Vehicle and Light Truck Tyres from China* (14 September 2009, https://www.wto.org/english/tratop_e/dispu_e/cases_e/ds399_e.htm).

The cases that demonstrate China's market power in this section renminbi operating as *a)* credit, in a fiat money-based global economy, and *b)* transaction medium for oil, in a commodity-based global economy. Both are important cases that illustrate how China's renminbi internationalization backed by market power can be translated into foreign policy projection.

Electronic Payment Services in Renminbi: China Unionpay Challenging VISA and MasterCard

In a world of fiat money, the method of electronic payment services (EPS) plays a significant role in delivering the exchange of goods and services. In recent years, electronic payment methods such as Paypal, Apple Pay, Samsung Pay, and other forms of fiat money such as bitcoins supported by the protocol of the blockchain technology came about as mediums of electronic payment. But the dominant players in fiat money are still credit cards. While in advanced countries like Japan and Germany still have a preference of cash use for everyday transactions and high rates of cash circulation domestically, credit cards issued by banks have gained a dominant position in goods and services trade. Right after joining the WTO, since the year 2002, China has been developing and pushing for its own credit card for domestic and foreign use under the auspices of the People's Bank of China (PBOC) – China UnionPay (CUP), or *yinlianka*. Headquartered in Pudong in Shanghai, China, China UnionPay has expanded rapidly in terms of the number of countries it covers for transactions in the past decade and a half. It is now used in over 141 countries, and is the third-largest payment network by value of transactions it processes behind VISA and MasterCard. By 2016, China UnionPay had become a global leading bankcard association for credit cards.[29]

But EPS was not an exception to the Sino-US competition and contest. On September 15, 2010, the US filed a complaint in the WTO with respect to "certain restrictions and requirements maintained by China pertaining to electronic payment services for payment card transactions and the suppliers of those services".[30] The US questioned whether China was complying with WTO

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[29] It is said that the concept of a nationwide payment network in China dates back to 1993 when Jiang Zemin, the then-Chinese president, advocated for the 'Golden Card Project'. China UnionPay is an outcome of China's multiple attempts at creating a unified Chinese bank card system since the 1990s. Launched on March 26, 2002 by then PBOC governor Dai Xianglong, it started with four state-led banks of China as members: the Industrial and Commercial Bank of China (ICBC), the Agricultural Bank of China (ABC), the Bank of China (BOC), and the China Construction Bank (CCB).
[30] For details on this case, see *DS413 China – Certain Measures Affecting Electronic Payment Services*, September 15, 2010 (https://www.wto.org/english/tratop_e/dispu_e/cases_e/ds413_e.htm). Japan and South Korea requested for third party participation in the case, in addition to Australia, India, and the European Union among others.

rules on market access, and alleged that China poses a series of requirements imposed by China to constitute impermissible market access restrictions or national treatment limitations on foreign suppliers of the electronic payment services (EPS). China UnionPay was expanding throughout China, but VISA and MasterCard was facing difficulty penetrating into the Chinese market. The US argued that *a)* China permits only China UnionPay to supply EPS for payment transactions denominated and paid in renminbi, *b)* foreign suppliers of EPS can only supply the services for payment card transactions in renminbi, *c)* requires that all payment card processing devices to be compatible with that the China UnionPay system bearing the China UnionPay logo, and that *d)* while China UnionPay has guaranteed access to all merchants in China that accept credit cards, foreign suppliers of EPS must negotiate for access to merchants. The WTO Panel rejected claims a) and b) but concluded that China UnionPay is a sole supplier of EPS issued in mainland China and used in Hong Kong or Macao, or issued in Hong Kong or Macao and used in mainland China, and found China's demands for all payment cards issued in China to bear the China UnionPay/Yinlian logo were inconsistent with China's national treatment obligation under *Article XVII* of the General Agreement on Trade in Services (GATS). Upon the adoption of the panel report by the WTO Dispute Settlement Body (DSB) on August 31, 2012, China stated that it will need time to comply with WTO obligations according to the panel rulings, and was given 11 months from the date of adoption of the panel report, which lapsed on 31 July 2013. The US did not agree that China complied with the WTO panel rulings. China announced subsequently in 2015 that it would open up the market for foreign payment networks from June 2016.

Realizing that the WTO is not where they can obtain satisfactory results, VISA and MasterCard proceeded with the only other option – to cooperate with China UnionPay, but the cooperation did not last very long. On February 2016, China UnionPay and VISA signed a Memorandum of Understanding (MOU) to collaborate on EPS.[31] China UnionPay ended monopoly on domestic bank card clearing in June 2015, and gave foreign EPS providers direct access to the Chinese market (valued at $6.84 trillion in 2014) for clearing bank card transactions. However, the co-branded cards (with both China UnionPay and VISA/MasterCard logos) are to lose China market shares asthey will expire without the opportunity for renewal, as announced by PBOC authorities banning the co-branded card renewals citing concerns of capital

[31] CUP and VISA Sign MOU to Collaborate on Payments Security, Innovation and Financial Inclusion (http://investor.visa.com/news/news-details/2016/CUP-and-Visa-Sign-MOU-to-Collaborate-on-Payments-Security-Innovation-and-Financial-Inclusion/default.aspx)

flight on December 5, 2016.[32] VISA and MasterCard were not available for comments on the abrupt decision. The ban on co-branded cards came shortly after US president-elect Trump accepted a phone call from Tsai Ying-wen, upending the 'One China' policy.

In July 2016, China UnionPay overtook VISA in the global cards market (valued at $22 trillion in 2016) by value of card payments, resulting mainly from the rapid expansion of the Chinese market. According to Retail Banking Research (RBR), The Chinese market power is demonstrated in global card market shares – VISA and MasterCard maintained 50 percent and 31 percent respectively in global cards market, while China UnionPay remained predominantly domestic with just 0.5% outside China.[33] The mission for China on EPS, it seems, will be expanding that offshore marketshare in the next decade. China does not see eye to eye on operations with foreign EPS providers such as VISA and MasterCard, and if cooperation is deemed implausible, it would best expand globally based on its expanding domestic market.

Oil Transactions in Renminbi: Challenging the Petrodollar

During the postwar period, since the year 1974, the dollar was supported by the petrodollar system, in the aftermath of the Bretton Woods breakdown. The petrodollar system was created through series of Henry Kissinger's secretive meetings with King Faisal bin Abdulaziz Al Saud of Saudi Arabia. The US and Saudi Arabia would come to an agreement that if the Saudis, the primary exporter of oil among the Organization of the Petroleum Exporting Countries (OPEC) nations to the US, priced all of its oil in dollars, it would be guaranteed military security and protection from Israel by the US. By 1975, all of the OPEC member countries were producing oil priced in dollars, and held their oil surplus proceeds in US government debt securities by the US Treasury for military protection offered by the US. By this unofficial arrangement, it may well be argued that the dollar became fully convertible for oil instead of gold. And in turn, the US developed and maintained strong military presence in the Gulf states (of which the people are largely Sunni muslims) - Bahrain, Iraq, Kuwait, Oman, Qatar, Saudi Arabia, United Arab

[32] 'Bank Cards to Lose China Market Share', Financial Times, December 5, 2016 (https://www.ft.com/content/1f26b75c-bac2-11e6-8b45-b8b81dd5d080)
[33] 'UnionPay takes top spot from VISA in $22 trillion global cards market – RBR', *Finextra*, July 22, 2016 (https://www.finextra.com/pressarticle/65412/UnionPay-takes-top-spot-from-visa-in-22-trillion-global-cards-market---rbr).

Emirates, Egypt, Jordan, and Yemen. Under this system, the US balanced its power against Iran (of which the people are mainly Shia muslims) and protected Israel, the Jewish state, and prevented Soviet power from penetrating into the region.

During the Obama administration, however, two important factors that came into play made the solidity of the petrodollar system into the mid-to-long term future questionable. First, the US discovered fracturing methods to utilize its shale gas, and no longer became dependent on Saudi oil. Second, the Iran Nuclear Deal (or the Joint Comprehensive Plan of Action, JCPOA) was reached, paving the way toward oil transactions that are denominated in Euro.[34] Prior to the JCPOA, Iran was accepting various currencies for oil – including the Chinese renminbi and the Indian rupee, because under US sanctions it could not trade its oil in dollars.[35] Although the Iranians stopped accepting the renminbi and the rupee citing currency volatility, and requested that all of its oil transactions be done in Euro post-JCPOA, China learned from its interactions with Iran that oil transactions denominated in renminbi could contribute to the internationalization of the renminbi.

So began China's drive toward 'renminbi-for-oil'. China's activities in using renminbi as the currency for oil transactions are escalating. In June 2015, Russia's third-largest oil producer Gazprom Neft announced that it is now settling all of its crude sales to China in renminbi, down the East Siberia Pacific Ocean pipeline to China.[36] This was even before the agreement was reached on renminbi inclusion in the SDR at the IMF (November 30, 2015). Saudi Arabia, which has been the number one oil exporter to China in the 2000s, is now also pressured to do oil transactions in renminbi, because it is very close to losing its lead to Russia that is accepting renminbi in the Chinese market share for oil.[37] The Saudis will be all the more pressured to do so, especially if *a)* US oil imports from the Saudis decrease significantly if self-sustainability in

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[34] The Iranian nuclear capability was becoming a threat to the region (particularly to Israel) and motivated the US, along with other P5 members – UK, France, China, Russia of the UN Security Council and Germany, to sign an agreement – the Joint Comprehensive Plan of Action (JCPOA) to lift EU and UN sanctions on Iran to halt (or delay for 15 years) its nuclear development. Although primary US sanctions are still placed on Iran under the surveillance of the US Treasury, lifting other sanctions paved the way for the reopening of the Iranian economy.

[35] 'Iran accepts renminbi for crude oil', *Financial Times*, May 8, 2012 (https://www.ft.com/content/63132838-732d-11e1-9014-00144feab49a)

[36] 'Gazprom Neft sells oil to China in renminbi rather than dollars: Currency switch highlights impact of western sanctions against Russia over Ukraine', *Financial Times*, June 2, 2015 (https://www.ft.com/content/8e88d464-0870-11e5-85de-00144feabdc0)

[37] 'Russia Pips Saudi Arabia in Race to Grab China Oil Market Share', *Bloomberg News*, June 23, 2015 (https://www.bloomberg.com/news/articles/2015-06-23/russia-pips-saudi-arabia-in-race-to-grab-china-oil-market-share)

oil production is realized in the US or renewable energy production takes off, and if *b)* the OPEC's recent decision to control production does not lead to significant rebound of oil prices in the longer run.

China's market power is a definite source of support for renminbi use in oil transactions. Such use of the renminbi in oil transactions will only increase as China's demand for oil increases exponentially into the future. China's onshore oil fields are already in decline, and its oil use is only increasing, thereby contributing to its increased appetite in foreign imported oil.[38] The International Energy Agency (IEA) estimated that by the year 2030, China will be the primary consumer of Iraqi oil.[39] Backed by the market power, China is able to demand the use of renminbi for payment. At the same time, China is ambitiously preparing to launch its oil futures denominated in renminbi.[40]

If China successfully challenges the petrodollar system by rendering the renminbi the currency of exchange for oil transactions, its current efforts in OBOR will bolster its geopolitical leverage along the Straits of Hormuz and the Straits of Malacca, through which a dominant percentage of the world's oil exports pass. China appears to be interested in playing a political role in the Middle East, with Xi Jinping calling for the creation of a Palestinian state during his visit to Egypt in January 2016.[41] Xi Jinping was also the very first leader to visit Iran post-JCPOA, and China's longstanding ties with Iran make it very likely that China will be standing against US domination of the region in the coming years. In this manner, China is advancing into the Middle East with a foreign policy agenda, backed by its market power in oil consumption. China's ongoing efforts to challenging the petrodollar system with renminbi transactions for oil is backed by its market power, which will only increase with time. It would be an understatement that such efforts are purely for energy consumption – they are closely aligned with its geopolitical motivations to decrease US influence in the Middle East.

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[38] 'China's Oil Imports Will Keep Surging, Rebalancing Global Markets', *Forbes*, September 14, 2016 (http://www.forbes.com/sites/damonevans/2016/09/14/chinas-oil-imports-will-keep-surging-rebalancing-global-markets/#57b7ad6f5023)

[39] 'China said to be main buyer of Iraqi oil by 2030', *China Daily*, November 13, 2012. (http://www.chinadaily.com.cn/business//2012-11/13/content_15921354.htm)

[40] 'China's ambitious oil futures contract delayed: Burst of speculation in metals futures gives regulators cold feet about complex contract', *Financial Times*, September 15, 2016. (https://www.ft.com/content/dbd43e5c-78cc-11e6-a0c6-39e2633162d5)

[41] 'China's Xi calls for creation of Palestinian state: President says Palestinian problem "should not be marginalised" as he outlines series of economic deals for Middle East', January 22, 2016 (http://www.aljazeera.com/news/2016/01/china-xi-calls-creation-palestinian-state-160122061202778.html).

V. Conclusion and Policy Implications

This paper has dwelt on the impacts of renminbi internationalization from the perspectives of market power and foreign policy, with comparisons between the Chinese and American pathways toward economic and security binds in the Asian region, and case studies of Chinese market power projected onto foreign policymaking via the renminbi, in fiat money-based and commodity-based realms of the global economy. While it is unclear whether the renminbi will rise to replace the dominant as the main anchor, it is for certain that it is a leveraging tool for China and that the push toward renminbi internationalization it is backed by its market power – via consumption power and via expectation of renminbi appreciation. We stand at a crossroads where we see the practice of foreign policy not only convened with conventional military engagements but with economic coercion, and where the direction of global hegemony could be altered significantly.

For a sustainable cooperation among countries of Asia toward further economic growth, a system of monitoring and checks-and-balances is needed, via the World Trade Organization (WTO) as necessary, particularly in economic sectors that have not been opened by China through the market access protocols for China's entry to the WTO, in concerted efforts to restrain negative consequences of China's utilization of market power for foreign policy results. Recent development of skirmish between China and South Korea – mainly economic retaliation on sectors not included in the market access protocol that China signed onto upon WTO accession – upon South Korea's recent decision to deploy the Terminal High Altitude Area Defense (THAAD) missile battery against China's wishes[42] add to a serious of previous economic retaliation behavior by China. For the record, China's restriction of tourism flow to Taiwan upon its election of Tsai Ing-wen as president in 2016 – who does not endorse the 'One China Principle' advocated by China, or China's export ban of rare earths upon the Japanese government's purchase of the Senkaku/Diaoyu Islands in 2012[43], were exemplary cases in which China used its market power to coerce other countries to fulfill its foreign policy agenda, which

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[42] 'Report: South Korea could file WTO complaint for China THAAD retaliation', *United Press International*, January 25, 2017. (http://www.upi.com/Top_News/World-News/2017/01/25/Report-South-Korea-could-file-WTO-complaint-for-China-THAAD-retaliation/9741485359801/)

[43] 'Fight against China on rare earths', *Financial Times*, March 14, 2012. (https://www.ft.com/content/4c3da294-6cc2-11e1-bd0c-00144feab49a)

were a manifestation of China's vehement contests. Ironically, such records are against Chinese President Xi Jinping's proclamations on abiding by the principles of free trade at the World Economic Forum in January 2017.[44] As long as China claims that it is part of the global trading system and benefits from it, checks-and-balances should be placed on the movements of the renminbi in cases of its usage toward economic retaliation.

The renminbi is clearly an aspiring currency that has the possibility to rise to counterbalance other dominant global currencies in the future. Bearing in mind the nature of linkages between renminbi internationalization and foreign policy, expectations that it would counterbalance the dollar does not equate to nor guarantee a more stable global order. On the contrary. Moreover, it increases China's bargaining leverage to deliver unexpected foreign policy consequences. It is important to understand that renminbi internationalization is not just a question of avoiding transaction fees for converting local currencies to the dollar and vice versa using VISA or MasterCard, or being able to purchase oil in renminbi in rates that would be cheaper as opposed to the petrodollar system when the OBOR and pipeline projects come through. The understanding that renminbi can be used as foreign policy projection just as the dollar has had is vital to understanding the global financial architecture of the future. This is a crucial task for all countries that are engaged heavily in bilateral or regional economic relations with China for years to come.

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