**CHINA**

The renminbi enters the special drawing right basket

On October 1, China's currency, known as the renminbi or yuan, was added to the International Monetary Fund’s (IMF) special drawing right basket (SDR). It will have a weight of 10.92%, compared with 41.73% for the U.S. dollar, 30.93% for the euro, 8.33% for the yen and 8.09% for the pound.

The first SDRs were created in 1969 to supplement official currency reserves. They are allocated to IMF member nations in proportion to their respective quotas. SDRs are not actually money or a claim against the IMF. However, if necessary, they can be exchanged for currency on the basis of agreements between the countries or at the IMF’s request. SDRs outstanding now total approximately 204 billion (US$285B).

Only the currencies of leading export nations or the currencies most involved in international finance are included in the SDR basket. Currencies must also be freely and widely usable. While China has been an international trade heavyweight for many years, the freely usable aspect of its currency remained to be proven. The reforms implemented by Chinese authorities in recent years to make the yuan more accessible and increase its use abroad, particularly by central banks, finally convinced the IMF. However, it is still far from being a fully convertible currency with a floating exchange rate like the other currencies in the SDR basket.

**Implications:** The addition of the renminbi to the SDR basket definitely does not imply immediate purchases of the currency. However, a country that is in difficulties could request yuans in exchange for its SDRs. This type of operation is rare; the yuan’s new function will mainly be to establish the exchange rate for SDRs. The yuan’s fluctuations now account for about 11% of the fluctuations in SDRs.

The SDR valuation has barely changed since the start of 2015, oscillating around SDR0.72/US$. This trend contrasts with the yuan’s, especially since August 2015. The Chinese exchange rate has changed about 8%, which would have altered the SDR exchange rate by about 0.9% if the yuan had been contained in the basket. Even so, the movement would have been slight. The trend is primarily dictated by the U.S. dollar and the euro.

The interest rate calculation applicable to SDRs will also change (effective October 7). The rate corresponds to the weighted average of the interest rates on 3-month government securities. At around 2%, the Chinese 3-month rate is higher than those of the other countries included in the calculation, which will push the result up. IMF member nations must pay interest on their SDR allocations and receive interest on their SDR holdings. On a net basis, some countries need to pay interest, but the amounts involved are very small.

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