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Analysis of the Dual Interaction of RMB Exchange Rate and Fujian Foreign Trade Export

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Abstract

The floating exchange rate management system implemented by our country based on market supply increases the flexibility of the RMB exchange rate and intensifies the impact on the fast-growing export trade of Fujian Province. While Fujian's external exports continue to increase, the factors affecting export growth have also changed; this change is reflected in many aspects. Among them, the way that exchange rate changes affect exports is through price adjustments, and the pressure on the transition of low-price competition export trade models stems from the continuous appreciation of the RMB. Under the premise of constantly changing exchange rates, most Fujian foreign trade companies must learn to deal with the uncertainty brought about by exchange rate changes. Based on Fujian's exports in recent years, this paper analyzes the impact of changes in the RMB exchange rate on Fujian's exports and verifies the mechanism of exchange rate changes on Fujian's export trade structure. Finally, according to the actual status of Fujian's export, from the perspective of foreign trade companies, countermeasures and suggestions for the risk of RMB exchange rate fluctuations are proposed.

Keywords

RMB exchange rate changes; Fujian export trade; Exchange rate risk; Countermeasure.

1. INTRODUCTION

The exchange rate between the unit currency of one country and the unit currency of another country is called the exchange rate. It can also express the value of one country's currency against another country's currency. Exchange rates play an important role in price indicators in international activities. The foreign trade of a country is mainly affected by changes in the exchange rate. Fujian Province mainly exports labor-intensive and mechanical and electrical products, which fall within the scope of general trade. This thesis analyzes the status quo and existing problems of Fujian Province's export trade, finds out the factors that affect the changes in the RMB exchange rate in Fujian Province, and finds out measures to prevent and take countermeasures when export trading companies face exchange rate risks. In this way, the pressure on exports from exchange rate changes can be reduced, the development of Fujian's export economy and the optimization and adjustment of the commodity structure can be promoted, and the economic benefits of Fujian's export industry can be improved.

2. CHANGES IN THE RMB EXCHANGE RATE

Since the People's Bank of China announced that it would adjust according to market supply and demand, concerning a basket of currencies, and implement a floating exchange rate management system, the RMB exchange rate is no longer linked to the US dollar exchange rate,

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and a more flexible exchange rate mechanism has been formed. Since the core of this exchange rate reform is to improve the exchange rate formation mechanism while maintaining the stability of the RMB within a controllable range, the role of a basket of currencies itself is to act as a price stabilizer, referring to a basket of currencies can make the exchange rate more effectively reflect the actual economic changes and stabilize the exchange rate to a certain extent.

According to the China Statistics Museum, the average price of RMB/USD in February was 6.31RMB/USD. The average USD/RMB exchange rate in March was as low as 6.2785RMB/USD, a record low since 2015. At the end of 2017, the average USD/RMB exchange rate data was 6.59RMB/USD. After March 2018, the exchange rate of the U.S. dollar to the RMB has been slowly increasing, from 6.26RMB/USD to 6.96RMB/USD; it was not until October 2019 that the average exchange rate of the U.S. dollar to RMB declined. From 2012 to 2014, the average annual exchange rate of the euro to the RMB was almost the same. After that, the price of the euro against the RMB fell from 8.16 RMB/EUR in 2014 to 6.91 RMB/EUR in 2015, a full drop of 1.25 RMB/EUR. Since 2015, the exchange rate of the euro against the RMB has been increasing steadily. In the past two years, the highest exchange rate between the euro and the RMB was 7.80RMB/EUR in 2018.

In the eight years from 2010 to 2018, the overall value has dropped from 7.73JPY/RMB to 5.99JPY/RMB. From 2010 to 2015, RMB's annual average exchange rate to Japanese Yen reached the lowest level, which was 5.15JPY/RMB in 2015. Within this range, the annual average exchange rate of RMB to Japanese Yen fluctuates wildly. Starting in 2016, RMB's annual average exchange rate to Japanese Yen has only begun to stabilize. As of April 25, 2020, the exchange rate of RMB to Japanese Yen has risen to 15.18JPY/RMB.

3. THE IMPACT OF RMB EXCHANGE RATE CHANGES ON FUJIAN'S EXPORT TRADE

Typically, a country or region can suppress imports and increase its exports through currency depreciation. The processing trade in Fujian Province is dominated by electromechanical products, with the characteristics of "big import and big export." From a theoretical point of view, since imports can offset part of the additional costs caused by exchange rate appreciation, the processing trade industry is more affected by the appreciation of the RMB exchange rate, while general trade is less affected by the appreciation of the RMB exchange rate.

3.1. The Positive Impact of Changes in the RMB Exchange Rate on the Development of Fujian's Export Trade

China is an export-oriented economic development entity. The devaluation of the RMB can effectively alleviate our country's economic pressure and raise its economic development to a higher level. Foreign export trade occupies a large proportion of our country's economy. Fujian Province is also dominated by export trade. The devaluation of the RMB causes the cost of export products to be inversely proportional to the export volume. The lower the cost, the higher the export volume. However, the continuous appreciation of the RMB in recent years has caused the cost of export products to rise, which has virtually increased pressure on Fujian enterprises. This has led exporters to adjust and upgrade their industrial structure, improve product quality, and force companies to improve production efficiency, reduce production costs, move to industries where cheap labor can obtain a competitive advantage, and abandon low energy consumption industries. For high-polluting industries, it is necessary to introduce advanced and additional technologies to transform high-end industries with low energy consumption.

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3.2. The Negative Impact of Changes in the RMB Exchange Rate on the Development of Fujian's Export Trade

The devaluation of the RMB will not only increase the cost of foreign investment. In recent years, China's "Going Global" strategy has dramatically promoted the increase of foreign investment, reduced the purchasing power of the RMB, and increased the cost of foreign investment. Under the influence of the national strategy, Fujian Province has increased the financial pressure on some enterprises and was forced to withdraw from the international investment market under unbearable conditions. The shortcomings of Fujian's traditional intensive products are small scale, low-risk resistance, and poor exports. In the national economic environment, its competitiveness is relatively weak. Some sources point out that the export volume of large-scale enterprises is decreasing. The export changes of private and non-private enterprises will contribute to the development of labor-intensive industries in Fujian Province. The market economy system is constantly changing, which has led to an increase in the experience cost of labor-intensive enterprises in Fujian Province. Since 2012, a quarter of the total labor costs have been used to pay for labor costs, increasing about 10% over the previous year, which has seriously affected labor-intensive export enterprises in Fujian Province.

4. COUNTERMEASURES FOR FUJIAN EXPORT COMPANIES TO DEAL WITH EXCHANGE RATE FLUCTUATION RISKS

4.1. Adjust Product Structure and Trade Structure

The problems faced by Fujian foreign trade enterprises are not only the economic downturn and shrinking foreign demand, but the lack of competitiveness of Fujian's own foreign trade products and low innovation capabilities. The current effective measures to promote the development of foreign trade are to adjust the product structure and foreign trade structure to improve the province's product export competitiveness. Enterprises should continue to innovate and develop new technologies, use high-tech technologies to increase the core competitiveness of enterprises in the province, and firmly establish product leadership in overseas markets to achieve irreplaceable effects. At the same time, it is necessary to use the province's technology to increase investment in domestic and foreign companies and provide technical support and financial support for the industrial structure. It is possible to seize the opportunity to innovate and develop industrial trade through industrial transfer within the enterprise and decentralized industrial layout.

The continuous appreciation of the RMB exchange rate will bring many challenges to different types of foreign trade companies. For example, cotton textile companies in the coastal areas of Fujian Province cannot afford the labor cost of exchange rate appreciation, leading to company bankruptcy and unemployment of workers. At the same time, technology-intensive industries are less affected by exchange rate appreciation. This proves that enterprises themselves need to upgrade and innovate the structure of foreign trade exports, increase the proportion of foreign service trade, and increase the proportion of their own capital-intensive and technology-intensive factors.

4.2. Seek National Policy Guidance and Government Service Support

Enterprises must use a specific macroeconomic and financial environment as operating conditions for exchange rate risk management. Strengthen its construction by making full use of the superior resources of the government, financial institutions, and other departments, actively seek technical service support and gentle policy guidance from the government, keep abreast of new trends, new policies, and new risks in the external environment promptly, and

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continuously improve the company's ability to effectively avoid risks. For enterprises in Fujian, they should respond to the country's call for sustainable development, eliminate high-pollution and high-consumption industries, transform to sustainable development industries, enjoy national policy subsidies, and enhance their viability.

4.3. Choose Reasonable Financial Derivative Products

Financial derivatives are financial instruments derived from primary assets. They are characterized by margin trading. They do not need to spend all the funds but only need to pay a portion of the funds. The conclusion of foreign exchange contracts is usually carried out employing cash settlement. When the buyer needs to pay the total price of the goods, the contract will be fulfilled by delivering the product on the day when the specified deadline is reached.

Fujian export companies can choose reasonable financial derivatives to avoid exchange rate risks. For example, the signing of foreign exchange forward contracts can effectively avoid transaction risks. Signing a foreign exchange forward contract means that the company can lock in the exchange rate in advance to avoid exchange rate fluctuations between the contract signing date and the actual foreign currency receipt and payment date from affecting the company's interests. When a company needs to pay foreign exchange in the future, if the currency to be paid is expected to appreciate in the future, it can lock in the current foreign exchange by signing a foreign exchange forward contract in advance to lock in foreign exchange costs to avoid the company from incurring losses. On the contrary, if the company has foreign exchange income for a certain period in the future, and the income of the foreign currency exchange rate tends to decline, it can lock in the income of the foreign exchange rate by signing a foreign exchange contract. The actual cost of hedging is greater than the cost of no hedging mainly because the company cannot accurately predict the trend of exchange rate changes. In addition, the guaranteed funds provided by the company when signing the forward contract will increase the company's capital share, which will invisibly bring about the cost of capital. Therefore, when using forward contracts to avoid transaction risks, companies must carefully consider them carefully, combine their actual conditions, and weigh in advance whether the costs and revenues of forwarding contracts are proportional or inversely proportional. Plus, it is necessary to strictly follow the total value of foreign exchange to avoid exchange rate risks and not conduct currency transactions with speculative gains to avoid causing more significant exchange rate risks for the company.

4.4. Establishing Provisions on Currency Preservation Clauses

In foreign trade transactions, enterprises set up currency hedging clauses in advance to reduce the impact of exchange rate fluctuation risks. For example, in mid-December 2017, a customer ordered 20 tons of hardware products from Fujian Jinjiang Jikun Company. Jikun responded that the customer could provide 20 tons of goods but hoped to settle the contract at the exchange rate when the contract was signed. Because it is a temporary order, the time is tight, and the amount is 400,000 U.S. dollars. The buyer and the seller will use the spot exchange rate of $6.4738 on January 5, 2018, as the settlement time and the bill of lading will be paid after 30 days. After the expiration of the 30th day, the exchange rate dropped by 0.1884, and according to the contract: the buyer should pay the company $411989.69. In this transaction, Jikun Foreign Trade Company, which was supposed to lose ￥75360, did not cause this significant loss because of the currency hedging regulations with the customer and avoided the loss caused by exchange rate fluctuations.

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4.5. Formulating Import and Export Hedging Strategies

When enterprises conduct import trade, capital flows out; on the contrary, when they export trade, capital flows. Therefore, when an enterprise can operate both import and export trade methods at the same time, it can make the import and export trade reach a specific equilibrium state and hedge the foreign exchange receipt and payment amount generated in the trade to achieve a relative balance and reduce the adverse impact of foreign exchange changes on the enterprise. In addition, now that China's RMB is devaluing, Fujian's import and export enterprises can reduce the number of imports, put some of the exported products into the domestic market for sales, reduce the proportion of export business, and increase the proportion of domestic market business, which can also better avoid the adverse impact of RMB exchange rate changes.

5. CONCLUSION

In recent years, due to the influence of domestic and foreign macroeconomic factors, the growth of Fujian's foreign trade exports has slowed down, and the growth momentum is insufficient. In this context, Fujian foreign trade companies must change their traditional ways of thinking, make full use of the positive factors in the current domestic and foreign economic environment changes, accelerate industrial restructuring, enhance foreign trade competitiveness, and lay a solid foundation for the long-term and steady development of enterprises. Enterprises should actively adjust the export structure of commodities, increase the share of high-tech content and high value-added commodities in export commodities, reduce the share of low value-added products, actively promote overseas marketing promotion of export commodities, and make contributions to the healthy and sound development of Fujian's economy.

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