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The USA's position as a global power may be hit hardest by China with central bank digital currency

Not even the coronavirus crisis prevented China's central bank from reaching a milestone in the development of its electronic currency. In April, the People's Bank of China (PBoC) announced that it had started testing its digital currency in actual payment transactions in four large cities across China. With this step, China has taken the global lead to fully digitise its central bank money supply. What is primarily at stake here for the East Asian power is clearly a rearrangement of geopolitical power relations by way of a fusion between technology and money. This is because the digital RMB may turn out to be more effective than anything else before in bypassing the US-dominated international payment system, thereby undermining the financial foundations of American world power.

A central bank digital currency (CBDC) is an electronic means of payment issued by the central bank of a state (unlike cryptocurrencies, such as the bitcoin, which are not controlled by sovereign countries). In contrast to money deposited in bank accounts (and hence, also electronic), the CBDC can be best described as digital "cash" (although one relevant difference is that – as opposed to cash – central bank digital currencies are not anonymous). China has been developing its own digital currency (e-RMB) since 2014, with the officially declared intent of **partly substituting cash in use.** In China's four large cities, Shenzhen, Suzhou, Chengdu and the economic zone Xiong'an near Beijing, **some people** – such as governmental employees – **are already paid their allowances in digital RMB, as part of a pilot project**.

Having started real-world tests, China is now clearly pioneering the introduction and use of central bank digital currency; however, the **country's leadership is expected to take a cautious approach in launching the digital RMB**. In the conventional long-term planning framework, they will first test its operation in additional small pilot projects and proceed towards the final objective of creating a new, 21st century global money, by gradually fine-tuning the model. **However, the gradual introduction is hardly reducing the e-RMB's geopolitical weight.** About four in five transactions in China are already cashless and as a result, the **importance of the CBDC lays** not **primarily** in improving the efficiency of payments but **in securing advantages in terms of global power positions**. This is clearly based on technological innovation, with increased governmental support, which has already resulted in the reduction of the use of cash so far, as high-tech companies offering mobile payment solutions (WeChat, Alipay) have become dominant actors of the Chinese economy. In preparation for the next (14th) five-year plan, the country's leadership continues to assign a key role to digitalisation and the economic and social power of

Internet platforms (“Internet + education”, “Internet + health”, “Internet + tourism). To this end, they are promoting acceleration of network speed, cuts in usage fees and the **development of cross-border e-commerce**. Consequently, both the PBoC and the corporate sector are provided with a wide range of subsidies by the central government.

Accordingly, the e-RMB may deliver the most meaningful results for China in terms of geopolitics. Although the East Asian giant has been making efforts to encourage the use of its own currency instead of the USD when it comes to international trade settlements, payment transactions and central bank reserves, the CBDC **is so far the most potent attempt to establish the RMB as a global currency**. This may be so because the United States’ global dominance stems – among other things – from **managing and controlling international payments**. As a result, this is not only about confidence in the USD but also the related infrastructure and the capability for processing cross-border payments. The US SWIFT system (Society for Worldwide Interbank Financial Telecommunication) transmits messages on payment orders, in many cases via US banks (so-called correspondent banks). Today, this service accounts for the overwhelming majority of international payments (in a total amount of about 5 thousand billion USD a day). **Through SWIFT, the USA can identify illegal cash movements** – including money laundering and terrorist financing – and, even more importantly, **control compliance with international sanctions**. Security policy experts emphasise that financial and economic restrictions have recently become one of the most important instruments of American foreign policy. This is also the US trump card in keeping Iran’s nuclear endeavours at bay.

These are the very capabilities that are threatened by the Chinese central bank’s digital currency as in the future, it may efficiently enable **bypassing the SWIFT system**. Such an opportunity would be welcome not only by the rivals but even perhaps by the allies of the USA. Notably, the European Union is busy looking for a solution for trade settlements with Iran despite the sanctions. Thanks to its increasingly close trade relations with China, Russia would also welcome a central bank digital currency replacing the US dollar. The acceptance of the e-RMB may be boosted in the future by its **favourable attributes for international payments**: this is a solution **which is officially supervised by a sovereign state but which enables direct flows of funds between partners.** Therefore, it may eliminate difficulties which clients outside China now have to face when choosing the RMB in international payments.

To reap the benefits, China not only needs to create an extensive and efficient international infrastructure, it also needs **to raise the attractiveness of the RMB as a denomination.** That is, the RMB should earn **the same global confidence** and benefits in terms of all money functions, as those the USD has. Consequently, from the market’s perspective not even the e-RMB guarantees a quick victory over the USD. However, **China's power position cannot be left out of the equation either**. Today, China has dominant influence in **a number of Asian, African and Latin-American economies and** through the **Digital Silk Road** project, and it has embarked on the development of infrastructure and e-trade relations as well. **Accordingly, the e-RMB will not primarily be a matter of choice for the countries concerned.** This clearly **points to a rearrangement of geopolitical power relations**.

The importance of the CBDC and, in a broader sense, that of financial digitisation, is also underlined by the increased **competition between FinTech companies of India and those of China**. This is also motivated by the rivalry between the two emerging countries. Through its giant technological companies, China now has a profound influence on the everyday life in India. Companies playing an active role in the development of the e-RMB, such as Tencent and Ant Financial (operating Alipay), and other promising Chinese tech companies **have turned towards international growth opportunities**, with a focus on **India**. Ant Financial has entered the Indian market by acquiring a stake in Paytm, a popular payment application. WeCash, connecting participants of loan transactions with BigData solutions, is also active in India, trying to bridge the gap between creditors and rural residents and enterprises without access to bank financing. **One typical characteristic of China's expansion is** trying to make profits by **providing services for the masses**. High-tech companies from China invest in online platforms satisfying not only financial but other types of needs (e.g. food delivery services) as well. Thereby, they can indirectly **build up an increasingly strong influence in India's services sector**.

As a consequence, India may scale up efforts to take back the leading role. The government has taken quick steps to facilitate the adaptation and spread of technological innovation. This is also underpinned by the Digital India programme announced by the Modi administration, and the plan of implementing a cashless society, as India also recognises great opportunities in a state-controlled CBDC, while it has banned cryptocurrency use. Indian entrepreneurs can enjoy the benefits of "late comers" and can rely on a massive market and IT knowledge base (although they are still facing difficulties in accessing internal financing). The increasingly intense digital competition between China and India may be in line with the interests of the USA as well. The **United States**, with its concerns about the advancement of Chinese technology and voicing security concerns all the time, **may have an interest in India's role as a challenger**. Consequently, in response to the Chinese geopolitical threat, in recent years India has been making efforts to strengthen its ties with the USA.

In sum, emerging powers **can forge geopolitical advantages by combining money with technology**. A JP Morgan analysis claims that digital currencies are not merely a financial innovation but are becoming a means of global power ambitions. High-income countries – including, in particular, the USA – could also use CBDC as a geopolitical instrument: they can rely on it to limit the powers of emerging rivals and thus mitigate the risk of losing their leading role. Accordingly, in the future the matter of CBDC will go beyond economic arguments even more than now. Nonetheless, the United States is increasingly lagging behind, as regards CBDC. When addressing the issue this February, Jerome Powell, Chair of the Federal Reserve only noted that they were looking into it. However, time is running out. **The USA may soon be left with a last chance to keep the US dollar's still unrivalled dominance alive in the 21st century's power skirmishes based on new digital foundations.**

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