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I hereby recommend that the thesis prepared under my supervision by Nathan M. Becker entitled A Critical Study of China's Monetary Problems, with Suggested Proposals for Reform.

be accepted as fulfilling this part of the requirements for the degree of

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Preface

China in the Twentieth Century presents a picture vastly different from that of the "Sleeping Dragon" which European nations feared to waken just a half-century ago. A large, under-developed, low-standard area, lacking in real political and economic unity, is slowly emerging into a modern state, with all the economic, political, and social problems associated with that condition. For good or ill, China has begun to change. And more and more are the obstacles to that change becoming apparent to the Chinese themselves; obstacles which have their roots deep in the past, in the previous and still existing conditions and customs of the people. The problem of creating or building a modern industrial state is sufficient to tax the energies and resources of any people, but China must add to this tremendous task two all-important changes which, by their very nature, must be the fore-runners of any industrial advance worthy of mention: political stability and monetary reform. These two may be considered to be the outstanding problems that face China today. Upon the particular solutions evolved depends, in great measure, the future of China--and until some solution at least, is given to each, there cannot, in a very real sense, be any future at all. Today (March, 1938) each of these struggles has reached its climax; China is moving rapidly in the direction of modern monetary organization; at the same time China is fighting desperately against the Japanese invaders for the right to exist.

In this thesis we are concerned mainly with the problem of monetary reform. Now actually, of course, the two problems must be considered in complete harmony for no such separation is possible. The nature of

political reform and the status of political freedom set the limits within which monetary reform can become operative. The artificial but necessary distinction on which this study is predicated we must bear in mind at all times until it is convenient to consider the possibilities of the economic reforms in the light of political realities.

The writer who is concerned with monetary reform in a country where there exists a constant flux and flow, where institutions are undergoing marked and rapid changes, must proceed with rather cautious steps. What he proposes today may be fact tomorrow or a useless collection of words. During the course of the writing of this essay sentence after sentence, indeed whole paragraphs and chapters, had an annoying habit of becoming out of date overnight. This essay is based on a preliminary study made in 1934 which was later extended to include the momentous events of the year 1935. The present study carries the date of March, 1938, and is written from that point of view and time with the exception of the Proposal for Reform presented as Appendix A. This proposal, a part of the original essay, has been included in its old form; written before the reform of 1935 it furnishes an interesting point of departure for debate on the question of the efficacy of the new monetary system introduced in China in November, 1935.

If it be brought against the methods and conclusions of this thesis that they display too much emphasis on economic principles and too much confidence in their applicability to the Chinese scene, and, consequently, are politically unreal, the writer calls to his defence Professor C. F. Remer, who says in the introduction to his notable work, "Foreign Investments in China":^{1/}

1-Remer, C. F., Foreign Investments in China, Introduction, p. x

"It is probably more necessary to emphasize objectivity when a study of China is presented than in the case of any other country. This is not entirely because emotion and prejudice are strong and interests are involved, but, also, because there is among the practical students of China's economic problems a school of perverse mystics who maintain that principles do not hold for China. The student of China must, of course, freely acknowledge that caution is necessary when it comes to generalizing about the country, but he is tempted to answer those who hold that no rules apply by asking whether a bank account ought not to balance in Shanghai or Tientsin as well as in Tokyo or London."

Table of Contents

	Page
Preface	1
Table of Contents	iv
Chapter I Geographic and Economic Background	1
Chapter II Political Background	11
Chapter III The Problem of Monetary Reform before 1929	23
The Media of Exchange	24
Silver	30
The Foreign Trade of China	38
The Balance of Payments	44
Banking	50
Fiscal Policy	51
Conclusion	59
Chapter IV Twentieth Century Proposals for Reform	61
Chapter V China under Depreciated Silver	73
Chapter VI Appreciating Silver: 1932-1935	82
The Trend of Events	82
Minor Reforms	95
1935: A Year of Climax	99
Chapter VII Monetary Reform in Operation	106
Chapter VIII Can China Survive?	126
Appendix A: A Proposal for Monetary Reform in China	132
Appendix B: Statistics	151
I Silver	152
Table 1 Prices of Bar Silver at New York, 1874-1938	153
II Exchange Values	154
Table 2 Value of the Haikwan Tael in U.S. Gold Dollars, 1919-1933	155
Table 3 Value of the Yuan Dollar in U.S. Gold Dollars, 1926-1938	155
Table 4 Value of the Customs Gold Unit in U.S. Gold Dollars, 1931-1938	156

	Page
Appendix B: Statistics	
III Wholesale Prices	157
Table 5 Indexes of Chinese Wholesale Prices, 1913-1937 (North China, Shanghai, Canton)	158
Table 6 Indexes of Chinese Wholesale Prices, 1930-1937 (Hankow, Tsingtao, Nanking)	159
Table 7 Indexes of Chinese Import and Export Prices and Barter Terms of Trade, 1919-1935	160
IV Specie Flow	161
Table 8 Net Flow of Gold and Silver to or From China, 1900-1937	162
V Foreign Trade	163
Table 9 Foreign Trade of China in millions of U.S. Dollars, 1910-1937	164
Table 10 Foreign Trade of China in millions of Haikwan Taels, 1910-1932	165
Table 11 Foreign Trade of China in millions of Customs Gold Units, 1931-1937	166
Table 12 Foreign Trade of China in millions of Yuan dollars, 1926-1937	166
Table 13 Index Numbers of the Foreign Trade of China in U.S. Dollars, Haikwan Taels, Yuan Dollars, Physical Volume and Customs Gold Units, 1910-1937	167
 Bibliography	 169

**A CRITICAL STUDY OF CHINA'S MONETARY PROBLEMS
WITH SUGGESTED PROPOSALS FOR REFORM**

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Chapter I Geographic and Economic Background

The estimates of China's natural wealth have been as varied as the imaginativeness of the human mind. From the time when Marco Polo returned to Europe with tales of the wealth and richness of Cathay, to the present century, the true nature of China's natural wealth has been shrouded in just such a veil of inaccuracy, mystery, glamour and romance---aided and abetted by the exotic accounts of numerous pseudo-scientific expeditions. Slowly, but surely, the real truth is beginning to emerge, and the facts do not uphold to any extent the fantastic stories of bygone years. This is not to say that China is a desolate area, bereft of the stuff which the gods drop into the laps of the deserving. Indeed such is not the case. In recent years numerous and exhaustive studies have been made so that the natural wealth of China is no longer a matter of conjecture.

China, in the Nineteenth century, was, for all practical purposes, not only a nationally self-sufficient area; even her communities were more or less economically independent of each other. Existing custom and habit--the most important general set of institutions in China--found no fault with this system, and, as we shall see later, one of the obstacles in the way of China's industrial development is just this lack of active discontent with existing conditions.

Mineral wealth is said to be the basis of the modern industrial state. We must, then examine China's mineral wealth as a clue to her possible industrial future.^{1/} Coal and iron are essential, yet China definitely

1-"The future material prosperity of China is directly linked with her natural resources. The great industrial development forecast by some prophets is strictly conditioned upon the presence in accessible areas of the needed basic materials. Without coal and oil for fuel and power, iron and copper for construction, limestone for cement and as a flux, and sulphur for sulphuric acid, a nation is distinctly handicapped in this modern age." Cressey, George B., China's Geographic Foundations, pp. 109-10

lacks the necessary iron ore, her actual and potential reserves totalling only 95 million tons, according to Tegengren.^{2/} Her situation in coal is much better, conservative estimates placing China's reserve at about 246 million metric tons.^{3/} In fact, there are only two known areas in the world which are as richly endowed with coal as the Loess Highlands of China: the Appalachian mountains of eastern United States, and the lower valley of the Rhine. Yet China's annual production of coal averaged only 25 million tons for the entire last decade.^{4/} The best fields, however, are in Shansi and the south-western wedge of China, where transportation facilities are poor and costly, and population is sparse.^{5/}

Petroleum, a possible substitute for coal, and essential in itself, is practically lacking. Water power is underdeveloped, and in the North, because of the changeableness of the rivers, is an impossibility. In the South, however, water power is a potentiality which must not be overlooked.

In copper, lead, zinc, silver and gold, China is also deficient, and very little timber is available.^{6/} Next to iron, tin is the most valuable mineral in China. In 1925 China produced 7% of the world supply of tin and ranked fourth among all the nations of the world.^{7/} Manganese is mined to a considerable extent, but it is in the production of antimony and tungsten that China assumes a leading position on the world market. She produces 80% of the world supply of antimony (about 20,000 tons

2-Ibid., p. 118

3-Ibid., p. 111

4-Ibid., p. 113

5-Frey, John, "Economic Significance of the Mineral Wealth of China", Annals, American Academy of Political and Social Science, November, 1930, p. 118

6-Ibid., p. 117

7-Cressey, G. B., op. cit., p. 123

annually) and from 50% to 75% of the world supply of tungsten (between 5000 and 7000 tons annually).^{8/}

In building materials China is sadly situated. Limestone is present but relative to the demand is scarce, and the poor transportation facilities make shipment of stone and other heavy materials, even if desirable, an impossibility. The shortage of fuel likewise militates against the manufacture of bricks because of the high cost involved.^{9/} The timber scarcity we have already mentioned, and this is a real problem to China, not only because of the direct need for this material, but also because of the tremendous damage by erosion and flood to the soil, and to human life and welfare, which has resulted from the denuding of China's forest-lands.^{10/}

In general, there are two chief areas of mineral wealth in China. The Loess Highlands are rich in coal, while the South Yangtze Hills and the Southwest Tableland have a variety of minerals, mostly low in bulk and high in value. But the coal and iron are separated, and the lack of low-cost transportation makes their union--necessary to industry--unlikely for some time.^{11/}

There are, according to Dr. Cressey, three possible areas where industrialization may take place, no one of which has all the requisites for modern industry. The Yangtze Valley has iron ore and cheap transportation facilities; the Western edge of the North China Plain is poor in metals, but Shansi coal is easily and cheaply secured; and South

8-Ibid., p. 124; Frey, J., *op. cit.*, p. 117

9-Frey, J., *op. cit.*, p. 123

10-Lowdermilk, W. C., and Li, T. I., "Forestry in Denuded China", The Annals, *op. cit.*, p. 141

11-Cressey, G. B., *op. cit.*, pp. 129-30

Manchuria, which under Japanese protection has shown signs of industrial advance which probably will not be sustained in the future.^{12/}

But China has two other agents of production: land and labor. Although the supply of land is great in absolute amount, it is not to be considered so relative to the requirements of China's hungry millions. However, the climatic range and general physical basis allow for a great degree of diversity in crops and, contrary to general opinion, agriculture is not so intensive, when we consider the possibility of utilizing modern machinery and technique, as we ordinarily imagine it to be. The average family living upon a farm in China has but five acres for its 5.7 average number of mouths. The average annual income, exclusive of house rent, is \$147.00 in United States currency, which amounts to \$2.30 per capita per month. When we consider that 80% of the Chinese are farmers we begin to understand the economic level of China today.^{13/}

After deducting the cash payments (for seed, taxes, etc.,) the average family must live on \$73.00 a year, plus the real income derived from the soil and other non-monetary forms of income.^{14/} One can understand, by these figures, why foreign trade per capita is so low in China, and why there does not exist in the mind or purse of the average Chinese, a thought of, or demand for, goods from foreign lands.

In the rural districts there are 621 persons to the square mile, as compared with 48 in the United States, 77 in Denmark, and the staggering sum of 1,238 in Japan.^{15/} And yet we cannot say, as Dr. Buck seems to indicate, that China is doomed to such an existence for many years. With

12-Ibid., p. 130

13-Buck, John L., "Agriculture and the Future of China", The Annals, op. cit., p. 109

14-Cressey, G. B., op. cit., p. 110

15-Ibid., p. 110

proper economic and political organization much could be done to increase the productivity of the Chinese, and once the desire for modern goods and equipment, necessities and luxuries alike, has become a part of the Chinese customary life, then we may count on the natural forces of such a rise in the standard of living working upon the problem of a population which tends to outrun subsistence.

At the present time only about 54% of the total crop is sold for cash--the rest being retained for domestic use. Chinese agriculture differs from that of the United States ^{IN} ~~is~~ three distinct ways: about 50% of the land is double-cropped; crops are raised primarily for their grain, leaf or fibre products since no animal industry exists; and the crops must supply both city and farm with a cheap, but poor fuel. The lack of animals makes the problem of fertilization very difficult, and with adequate fertilizer and farm machinery there could be experienced an agricultural production boom which would surpass that of many other regions and would forever alleviate the hardship and privation which famine and flood periodically bring to the children of "The Good Earth".^{16/}

But the most important factor of production available in China today is labor. The supply is not only plentiful, but conditions are slowly breaking down the reluctance of the Chinese to leave his ancestral soil, so that the potential supply of labor is already becoming an actual supply. And high wages, relative to the possibilities of income on a farm, will sooner or later break the traditional resistance of many, especially the younger men. Whether for good or ill, labor is the

16-Buck, op. cit., p. 111

resource which China has in sufficient quantity to satisfy heavy demand. For the time being, labor is, and perhaps will be for many years, cheaper than capital in China. Much capital is needed, of course, and must be secured, but China's real absolute advantage, or least comparative disadvantage, lies in the production of goods requiring a relatively great amount of direct labor.

We normally speak of the presence of three essentials in man's material life: food, clothing and shelter. It is interesting to note, because of the light it sheds upon China's economic position, that Mr. C. C. Wu, in his "Nationalist Program for China", tells us that: "four essentials in Man's material life are: food, clothing, shelter and transportation."^{17/} China has suffered so terrifically from the lack of adequate transportation that its significance looms upon the Chinese horizon as large as the three factors normally considered as basic. The maladjustments in transportation serve to illustrate the recent failure to match expanding economic life as well as to indicate the original failure, previously mentioned, to develop any kind of transportation system at all. And this is to be traced directly to the self-sufficiency of early Chinese community life which only recently has shown any signs of modification.

High wages will increase the supply of labor, but what is needed also, is the development of skilled technicians. The problem in China is not vastly different from the problem which the successful revolutionists faced in Russia. It is one thing to set out to industrialize a nation; another thing actually to perform the transformation from agrarian

17-Wu, C. C., The Nationalist Program for China, p. 16

backwardness to modern, technical, round-about processes of production.

The backwardness of China in transportation and communications is illustrated by the following comparisons:^{18/}

	<u>United States</u>	<u>China</u>
Railroad mileage	265,000 miles	9,000 miles
Surfaced roads	200,000 miles	4,000 miles
Dirt roads	1,000,000 miles	36,000 miles
Post offices	52,000	13,000
Telephones	17,000,000	100,000
Telegraph	1,500,000 miles of wire	150,000 miles of wire

Admittedly the United States is far richer than China in natural resources and in the ability to use them advantageously. But the lack of Chinese development is most clearly indicated by comparison with a nation such as the United States, whose advance has been nothing short of phenomenal. For a country of her size and population and resources, China is nowhere near the stage of development she could have reached had not other factors militated against such industrial and commercial progress.

A few words might be added concerning the traditional Chinese economy. It has long been the custom to compare pre-Westernized China with the feudal system of Europe in the Middle Ages. On the surface there is parallelism in the form and structure of the two economies; but a closer examination of the Chinese economy and its growth proves conclusively that the two systems are basically different. Both systems, it is true, were based upon a philosophic and customary localism; but an economic system is judged primarily from the point of view of the control of the productive and distributive systems, not on the basis of surface manifestations. For

18-Vinacke, Harold M., "Problems of Industrial Development in China", The Annals, op. cit., p. 179; and, China Year Book, 1934, Chapter XXI, pp. 568-639

example, capitalism and communism from one point of view are quite similar: both are large-scale productive enterprises using considerable amounts of capital and exhibiting a remarkable degree of division of labor. Such parallelisms might be extended, but the two systems differ basically in the matter of control. Capitalism, in its essence, is controlled by the activities of free individuals pursuing personal gain within the framework of a more or less restrictive legal system. Communist economy, on the other hand, is controlled, in theory, by the State, which represents the collective and general will of the people, with little or no freedom of the individual to take initiative in production or distribution except as it is consistent with the goal of the State, or the Party.

The same general distinctions exist between feudal Europe and traditional China. The feudal system was in the control of individual lords who owned the land, whose serfs were tied to them by many bonds. In China a type of control peculiar to the East existed, the economic system being controlled by the most powerful of all social forces: the family. Nor can the function of the family be dismissed by saying merely that the family was the unit of production. Such, indeed, has been the case among many peoples. In China the family ruled the entire economic life; all rights and privileges, all property, existed only through the agency of the family. That the Chinese are among those people who revere family above all else is generally recognized. It must also be remembered that the family is a rather inclusive term, reaching out to a variety of cousins many degrees removed, who in Western usage would rarely be

included in the term family. One can understand that if property is held in the name of the family rather than the individual, restrictions for the protection of the family right and heritage would prevent the easy and ready flow and exchange of land and other factors of production. It is not surprising, then, to find that the closed family corporation developed in China at an early date; nor is it difficult to imagine the obstacles in the way of introducing the modern economic corporation into such a social system. The guild, as an agency of control, was as active as the guild of Europe, but again a closer examination reveals that the guilds were primarily village organizations and as such were controlled by family policies.

A closed economic system, divided into small areas more or less self-sufficient, has no desire to develop a far-flung, complex transportation system, nor any desire to produce those commodities which must be transported to be sold. This complex, yet unmodern economic system accounts for the lack of development of China's natural resources. It must be emphasized that the free market, both internally and externally, is a basic essential to any further industrial progress of note. Through the widening of the trade area come the increased use of the available factors of production, the advantages of specialization and the division of labor and the increased exchange of all commodities with a consequent increase in the material welfare of all concerned. Isolation is a thing of the past; modernization must be speeded up. And a basic reform in that general program must be an adequate monetary system. Only when this has been established will there flow to China the assistance--mechanical, financial and technical--without which progress must be slow, halting and

uncertain.

It has been necessary to omit from consideration, above, the political development of China. But now more than ever it becomes necessary to consider that political situation realistically as it relates to the economic problems which China faces.

Chapter II Political Background

In 1664 the first Manchu sat upon the Dragon Throne of China. On January 1, 1912, Sun Yat-sen was inaugurated as the first provisional president of the Chinese Republic. Throughout those 268 years of Manchu rule there were many who looked forward to the day when a Chinese would again occupy that throne, for the Manchus were foreigners, a northern people who had swept down to conquer China in the middle of the seventeenth century. But it was more than just a Chinese-thrones-for-the-Chinese movement which sent the Manchus into the seclusion from which they have only recently emerged (with the encouragement of Japanese "requests" and at the point of Japanese bayonets); it was a revolution which sired another revolution, and then another; which even today is being fought in China. The Revolution of 1911 was the beginning; the end has not yet been written.

Out of the Civil War grew the powerful Kwangtung (Canton) government which soon marched northward and established the present National Government of China. But before this was accomplished there was a split between the conservative and left wings which resulted in the loss of power by the latter and the divorcement of the Chinese government from the Russian Soviet advisers who had played so important a part in the successful campaign against the central war lords. Chiang Kai-shek established his anti-communist government at Nanking. "The Kuomintang and the Communist Party of China gave up their partnership; the Hankow (leftist) Government was by August discontinued, and the Nanking Government accepted authority for the whole of South China. Chiang Kai-shek removed himself for several months, but by the end of the year was back in the saddle, building a

government which, from 1928 to 1932, destroyed the authority of the Peking government, sought to unify the country by armed force, embarked on a program of national economic reconstruction, education, public health, and transportation."^{1/}

Before we can turn to an examination of the monetary problems of China, we must examine the political situation in order to see just how the present National Government functions; to what extent its control and authority is accepted by the provinces and regions of China; and to what extent the agencies through which any reform must operate to become effective have been established.

As we have indicated above, China was never a unified nation in the real sense of the word; it was an empire, it is true, but an empire which saw a minimum of governmental functions performed by the central government. It is not surprising, then, to find a similar situation in modern China. Outer Mongolia has become a People's Republic with no allegiance to China and a de facto if not de jure alliance with the U. S. S. R.; the three provinces of Manchuria and Jehol and part of Charar in Inner Mongolia were occupied by the Japanese in 1931-32; Sinkiang, or Chinese Turkestan, is independent for all practical purposes with definite leanings toward the Soviet Union with whom she carries on most of her trade relations; Tibet is a British Protectorate; and today (1938) China is fighting desperately to maintain even a shred of territorial integrity against the advancing hosts of Nippon.

But even before the present conflict was generated, the National

1-Sokolsky, George, The Tinder Box of Asia, p. 46

Government had only an ephemeral or nominal control over many parts of China. The Soviet districts have been quite extensive for many years and the partisan areas (former soviet districts or areas where pro-soviet sentiment and action are strong) included many more square miles of territory nominally under the jurisdiction of the National Government. Nor did the government enjoy control over the remaining area in its entirety, for war lords and strong provincial governments were kept in nominal obedience by bribery or military power, or their allegiance consisted solely of cooperation in such matters as customs returns, trade statistics, and similar activities. Direct and immediate control was never universal and always there existed tenuous cords which threatened from time to time to break.

As for the political organization of China, it must be emphasized at the outset that the majority of the laws promulgated in recent years are merely "paper" laws, that is to say, a plan or bureau is decided upon, an appropriate legislative act or decree "establishes" the plan, but in reality no change is affected. The Law is placed on the statute books, but no more attention is given to it than its handling by the government merits. Nevertheless much has been done, and whether on paper or not, there are in existence certain departments, commissions, and other government agencies through which a monetary reform plan could be made operative: provided, that the National Government desired such reforms to become operative. The proposed constitution for China, released to the press on March 8, 1934, says: "A province is an administrative area directly controlled by the Central Government."^{2/} Of course

2-China Year Book, 1934, p. 475

under such a definition the National Government has very few "provinces", but this is not to say that the National Government deals with the existing provinces as if they were directly under its control; political reality demands other methods while the words of the constitution remain. So it is with other departments.

Organizations such as the National Reconstruction Commission, the National Economic Council, and minor commissions dealing with financial and rural rehabilitation have given good service, especially in the light of the difficulties which beset them. It is not too much to say, then, that proper organizations for the carrying out of a proposed monetary reform do exist and that other organizations even better able to do such service could be established in fact. True, the field of operation of such commissions is necessarily limited to the areas where the National Government has direct control, but there is also the very plausible likelihood, which we shall discuss in more detail below, that effective cooperation in such matters could be achieved by mutual agreements between the National Government and the provincial governments not directly controlled.

The National Government, in its effort to establish a unified China, chose the path of internal war--unity by force--rather than internal reform which would encourage and make mutually beneficial the union of all the Chinese provinces. As we have indicated above, the major goal of the National Government was the suppression of communism; only then, ran the argument, could internal reforms be instituted. This is not to say that much reform and modernization did not take place. To hold such a view would be to fly in the face of the facts presented in the following

chapters. Yet it is true that much of the reform that has come about has been through the efforts of business men and bankers to provide a greater degree of stability to their enterprises than existed before. And just because of this fact such reforms as have been introduced have been sporadic and particular, rather than consistent and general instruments of a well formulated program. Nor have such reforms always looked towards the general welfare of the masses of the Chinese people and the general economic development of the country.

In the light of actual events let us see just how successful the program of internal war instead of internal reform has been. From 1928 to 1935 five distinct drives against the communists ended in failure. During that same period China lost Manchuria and parts of Mongolia and North China to Japan or the "autonomy" movement (i.e. Japan also), a total area much larger than that which the Communists have at any time controlled. And the National Government lost this territory while refusing to fight back. Passive "resistance" to aggressive Japan but genuinely aggressive campaigns against the communists characterized this period. Even granting that such a policy was based on the sincere belief that it was to China's best interests for the National Government to behave in such a manner, the course of events has been such that the Chinese Government has finally changed its position in favor of an anti-Japanese alliance with the communists.

When the Japanese bombarded Shanghai in 1931 (making certain to destroy only Chinese owned textile factories) it was the famous 19th Route Army of Cantonese that heroically offered stubborn resistance to the Japanese. Where was Chiang Kai-shek, Generalissimo of the model

army, during that bitter struggle? Where were the supplies and munitions with which the 19th Route Army might have defeated the Japanese, unaccustomed to Chinese resistance? Where was the remainder of the ten-million dollar (U. S.) fund raised by American Chinese for the provisioning of the 19th Route Army, only several hundred thousand of which reached the proper destination?^{3/} These questions, and many others have disturbed the Chinese people, and the silent, ominous answers have given new life to the student movement which, in its endeavor to build a strong anti-Japanese front, has again become a powerful political influence in China. By 1936 that political influence was great enough to help shape the policy of the National Government.

It is no wonder, then, that the heroes of the 19th Route Army, betrayed at the moment when victory seemed imminent, marched southward to join hands with the Red Army of the Soviets in Fukien during the so-called Fukien Rebellion. But by placing an economic blockade around the Soviet areas in South China, the effectiveness of which was admitted by Hong Shieh Chung Hua (news organ of Soviet China), Chiang was able to force the evacuation of the communists. However, this was really no victory at all, for the communists had already determined to leave for the inland, more western regions, as their policy was to sovietize, leave communist cells behind, and then move on to new regions. Chiang's real goal, the trapping and annihilation of the Red Army, was a dismal failure. The Red Army of the South was able to outmaneuver the slower moving National and provincial armies and effect a contact with the Red Armies coming toward

3-Kimm, Dr. Kiusic, New York Times, June 18, 1933, quoted in Field, Economic Handbook, p. 221 (footnote)

Szechwan from the north and central portions of China.^{4/}

The Communist movement in China (and its partisan support) is a powerful force which must not be underestimated by the student of Chinese problems. Not only did it represent at its height, an area of over 200,000 square miles, equal in size to five times the state of Ohio, and containing 100 million people, but the conditions of poverty everywhere give further impetus to its growth. It has been suggested--and certainly, the discussion above should indicate, with some measure of truth--that the real reason for Chiang's "cooperation" with Japan was to be found in the common anti-communist ideology of both governments. Taraknath Das said: "The Nanking government realizes that the value of support from Western States and the League of Nations is something like a pleasant dream and an illusion, and that China must work out her salvation through a strong army and a centralized government--if need be, a dictatorship. Therefore, it seeks inspiration from the strong centralized government of Japan, the Fascist regime of Il Duce in Italy, and also the military genius of the German generals who have been acting as advisers."^{5/} But note that strength and arms were not at that time for the defense of China against imperialist Japan--for Japan's rulers and China's rulers were of the same stuff. No, those military forces were for the holy crusade against communism. Yet all the time the very conditions which make it possible for Communism to flourish and grow in China were left practically untouched. This is the real heart of the question; this is the real indictment of the National

4-Field, Frederick V., "The Recent Anti-Communist Campaign in China", Far Eastern Survey, Vol. IV, No. 16, August 14, 1935, pp. 124-26

5-Das, Taraknath, "Significance of Political Trends in the Far East", Annals of American Academy of Political and Social Science, Vol. 180, July 1935, p. 18

Government in the early thirties.

"The whole spirit of China in 1930", says Nathaniel Peffer, "is one of social reaction. The new industrial plutocracy is blatantly complacent in its feeling of security from any interference with the right to make as much money as possible as quickly as possible. . .all other considerations are communism. As for labor, unions are Russian poison. Let workers be happy at twelve hours a day in the factory for wages perhaps enough to keep them alive. . . .This is almost type statement for nine out of ten Shanghai bankers and industrialists when asked to give their social philosophy."^{6/} In general, industrial life developed all of the festers of industrialism with few of the healing-plasters. Class war, Peffer tells us, does not need to be manufactured by the communists; it exists in fact by the actions of the rulers. It is no idle thought that stirs Peffer to remark that "unless present tendencies are arrested there lies before the mass of the Chinese people industrial serfdom."^{7/}

But 80% of the Chinese people live on the soil; how are they faring under present conditions? Two basic problems, unsolved as yet by the National Government, have made the Chinese peasants aware of the communist movement: land ownership and crop-financing. With the peasant generally at the mercy of the large landowner and the money-lending gentry, crowded upon the soil available, and forced to pay interest rates averaging 36% per annum, there is little wonder that the Soviet land program has had wide appeal among the Chinese peasants and small landowners.

No monetary reform could be introduced so long as no unity existed.

6-Peffer, Nathaniel, China: The Collapse of a Civilization, pp. 235-36
7-Ibid., p. 243

It must be emphasized that political unity is itself a modernization, a reform, a western innovation. In the past there was only a cultural and linguistic unity in China, and even ~~these were~~ ^{that was} confined, in the main, to the ruling class. The Nationalist government proceeded first on the belief that political unity must precede any other sweeping change in Chinese institutions. Yet eventually that same government--even the same individuals--were gradually but completely won over to the opposing view. Despite the expenditure of much wealth and energy that might better have been utilized for social purposes to the gain of the nation, as well as the Kuomintang, little, in the end, was accomplished.

But from 1932 on, a new spirit began to manifest itself. Slowly at first, and against the opposition of the National Government, the idea of unity against the Japanese, preached by the communists, began to penetrate the minds of the Chinese people. And while Japan attempted to consolidate her position, creating one rumor after another of "autonomy" movements on the part of "Chinese", China prepared for the life-and-death struggle she knew was inevitable. More and more it became apparent that local cooperation between the Reds and those ordered to fight the Reds was helping the formation of a United Front opposed to Japanese imperialism. The climax came in December 1936, when Chiang Kai-shek was "detained" for some time by the officers and troops of Marshal Chang Hsueh-liang. These men under Chang (son of the former war lord of Manchuria) were Manchurian Chinese who had been ordered to retreat in 1932 rather than to fight against the Japanese. Later they were formed into the N. E. Anti-Communist Army. Before long, however, the desire to return to their homes in Manchuria and their hatred of the Japanese invaders made them susceptible to the

propaganda of their red enemies. That propaganda reiterated the old Red cry for unity of action against Japan and the promise of the Reds to place themselves under the orders of the National Government if that government would pursue a vigorous anti-Japanese policy.

The accounts of the Sianfu Incident differ widely. It has been said that Chiang was not kidnapped; that the entire affair was pre-arranged in order that he might accept the anti-Japan program without losing face--i.e.--because it was the will of his people. Other accounts tell us that the Red generals at the Sianfu Conference saved Chiang's life when the younger rebellious officers wanted to kill him and thus, according to the cautious Red generals, provoke disastrous Civil War. But whatever be the truth of the situation this much is known: that the price of Chiang's freedom, whether set by himself or by Chang, was the cessation of the civil war and the beginning of cooperation between the Reds and the National Government.

What conditions were specifically made at that time and what were added or clarified later is not precisely known by any save those who were participants, but in the next few months it was evident that cooperation was in effect. The Red Areas were restricted (practically recognized as a formal local governmental area by Nanking) and councils of war and peace between the various factions were held. Many political prisoners were released and known pro-Japanese officials were either eased out or thrown out of office. China was experiencing a climax to a long hard climb toward unity. Then came the incidents of July, 1937 and unofficial war between China and Japan began. It has been said repeatedly that the present war is unifying China. It seems more correct to say the

present war is being fought because China was rapidly becoming unified. Japan feared that unity, feared the consequences of a National Government which no longer took orders from Tokyo. So Japan struck, and the events were similar, at the outset, to those which took place in 1931 and 1932.

Without a doubt the secret service men of the Japanese army did not earn their pay in 1936 and 1937, for they should have known--and it appears they did not--that China in 1937 would not be the same as China in 1931. Again, as in 1931, Japan struck in the North and threatened at Shanghai. From the numbers of men and ships and equipment dispatched to Shanghai it was obvious that Japan expected to fire a few salvos and then hand to the meek and subservient Chinese officials the conditions of peace. But such was not the case, as the Japanese themselves can well testify. Despite numerous reinforcements which raised the Japanese forces to really great expeditionary strength, the Chinese army for three months resisted the Japanese attack on Shanghai. Today (Spring, 1938) the war goes on at a furious pace on numerous and wide-spread fronts.

A real and effective United Front has been established between the Kuomintang and the Communists, and the Red Armies operate under the command of the National War Council whose members include representatives of the Red General Staff. Mao Tse-tung, ex-president of the Chinese Soviet Republic, takes an active part in the political affairs of United China. The writer has no desire to make rash prophecies but is convinced that in the end China will win in her defence against Japanese imperialism. This decision is not reached by emotional processes or through wishful thinking, but by an examination of the realistic situations

which exist in China and Japan and the rest of the world. The discussion of this problem is postponed to the last chapter.

Of course, no reform such as that which is the problem to be discussed in this essay can have meaning except in relation to a political situation. Yet having thus briefly described and analysed the political background of the problem we will proceed to a discussion of the problem of monetary reform itself. In the end we must return to a discussion of the political factors; in the meantime we must secure an answer to our problem in economic terms which can later be translated into political reality.

Chapter III The Problem of Monetary Reform before 1929

The problem of monetary reform in China has two aspects: 1. the unification and reorganization of the currency system; 2. the general rehabilitation of China's financial position, especially the balancing of the budget and the modernization of the revenue system. The second aspect is, of course, dependent upon the first, for there can be no financial rehabilitation on the existing currency basis. For the balancing of the budget must precede any attempt at financial rehabilitation and the reform and standardization of the currency must accompany if not precede the balancing of the budget.^{1/}

We have only to examine the existing currency system of China to see why its reform is so necessary, so fundamental to the advancement of China's economic position.^{2/} In 1929 the Commission of Financial Experts under Dr. E. W. Kemmerer reported that despite agitation for currency reform for many years, China's currency was worse than at the turn of the century.^{3/} In fact, the Commission raised serious doubts as to the very existence of a Chinese currency system.^{4/}

In this chapter we will consider the situation as it existed at the time of the Kemmerer Report with special reference to the problems of the kinds of money in use, the standard of value, the balance of trade, the balance of payments, banking, budgets and public finance.

1-Condcliffe, China Today: Economic, p. 144

2-In 1889, J. Edkins wrote: "No (Chinese currency) chaotic eccentricities would drive any occidental nation to madness in a single generation.... Under these grave disabilities the wonder is that the Chinese are able to do any business at all." Quoted in Condcliffe, op. cit., p. 144

3-Kemmerer Report, p. 50

4-Ibid., p. 55

The Media of Exchange

Coins, paper money, and taels have been used in China for exchange purposes and each has its own particular history and problems. Up to the Sixteenth century only brass and copper coins were to be found in China. As trade with the outside world grew, however, silver was introduced in ever increasing amounts. But for the great mass of Chinese, copper and brass were still used almost exclusively up to the time of the World War, when the high price of these metals on the world market caused them to be melted down and shipped abroad. We shall see later that this habit of melting down coins is one of the basic questions to be considered in proposing a new currency system for China.

By far the most widely used silver coins in China have been the silver dollars, generally though often incorrectly referred to as Mexican dollars. They varied in weight and fineness from the American Trade Dollar of 378 grains to the Sun-Yat-Sen Dollar of 369 grains.^{5/} China, we must remember, is not a silver producing region of any importance, and consequently most of the early coins were of foreign mintage. In 1890 the first Chinese-made coins appeared but the other coins continued to circulate freely for they were needed--and both foreign and Chinese-made coins were judged by only one criterion: the exchange value of the silver within the coins.

Fractional silver has had a very unhappy history in China. It was not generally accepted and each province, region or village made its own coins which were, therefore, accepted only in the region of origin.^{6/}

5-Ibid., p. 54

6-Ibid., Appendix I

These fractional coins were known as "little" money and generally circulated at a discount. It might require six twenty-cent pieces or twelve ten-cent pieces to equal a dollar in "big" money.^{7/} This resulted from the fact that coins in China were judged by their metallic worth, not the value which a government arbitrarily stamped on their surfaces. The provincial banks and governments, in issuing fractional coins, expected them to circulate at par with other silver coins ("big" money), but the excessive seigniorage charge (which often was used as a method of raising funds in lieu of taxation) so depreciated the value of the coins that a dollar in fractional money did not have the same metallic content as a silver dollar, the ratio between them expressing the relative amount of silver in each. We might add to this the more than usual operations of the counterfeiters who "sell" their adulterated money to money-changers who then proceed to pass the bad money over their counters and into the regular channels of trade.

Hundreds of varieties of copper coins existed, varying slightly in weight, size and design. They were minted in units of 200, 100, 50, 20, 10, and in a few cases, 5 cash. Cash met the same difficulties as did fractional silver for the Chinese took even their copper coins seriously and insisted on discounting the face value of the coin if it did not coincide with its metallic value. The value of these coins, in terms of silver, varied from day to day as China, the nation of exchange shops, traded.

7-Leavens, Dickson H., "Chinese Money and Banking", The Annals of the American Academy of Political and Social Science, Vol. CLII, November 1930, p. 211

It might be well to add here a few words concerning the term "value" as used in relation to money. By value is meant the exchange value, the purchasing power of the silver content of the coin. By nominal value or face value is meant the value stamped on the coin by the issuing agency. Some typical variations are shown by the following average quotations for October 1929:^{8/}

Nanking	315 single coppers (10 cash) equal	
Shanghai	298	Chinese dollar (\$1.00)
Foochow	260	
Canton	235	

The value of the Shanghai single copper in terms of the Chinese dollar has been known to vary from 293 to 300 overnight. The old cash coins (i.e., one cash) of copper and brass have disappeared from most parts of China and are of little significance. Their removal led to the use of single and double coppers (10 and 20 cash) with a less than proportionate increase in metallic value, thus causing their immediate depreciation by the Chinese. Whereas 1,000 cash formerly exchanged for one silver dollar, the rate rose to 4,000. Since wages in many parts of China are more or less fixed, this rise (inflation) meant increasing hardship for the masses of people.^{9/}

Paper money was used in China before the Western States developed it. Marco Polo mentions his surprise at the use of paper money by the Chinese and seemed to favor its use by European countries. But in this case experience was not a good teacher for China because her paper money has almost always been badly managed. A nationwide inflation or deflation, however, was rare in China since every province, being more or less

8-Kemmerer Report, p. 57
9-Leavens, op. cit., p. 211

self-sufficient geographically and economically, was also more or less independent in this matter. While one province experienced inflation its neighbor might be suffering from deflation; while still another might have a stable paper currency.^{10/}

The note issues of China were just as diverse as those of the coins examined above, but notes played a less significant role in the life of the average Chinese than did coins, especially coppers. In all there have been five important types of paper money in use in China. The notes of the Central Bank were secured by a cash reserve of 60% and securities of 40%. About twenty million dollars of this money was in circulation in 1929 and in general had maintained its value. The provincial bank notes, on the other hand, generally depreciated badly, especially in Manchuria, where fifty Fengpiao dollar notes were equal, in 1929, to only one "big" dollar. In Kwangsi and Yunnan, Gresham's Law has been at work with a vengeance and by 1930 all the "good" money was driven out of circulation by the depreciated "bad" notes of the provincial banks. While the banks were to blame for much of this it must be remembered, in all fairness, that they were often ordered by the provincial and local governments to flood the provinces with notes, the money being used, in lieu of taxes, to carry on the particular war or rebellion currently active. It has also been claimed, with what seems to be good authority, that the Japanese used inflation as a political weapon in Manchuria, (before "autonomous" Manchukuo came into existence) and since then in North China.

The large private banks in China, including the Bank of China and

10-Ibid., p. 212

the Bank of Communications, had the right to print and issue paper money and it is interesting to note that these issues circulated very close to par and were in good repute in all business circles since they were redeemable, on demand, in silver. But even the notes of strong Shanghai banks were at times discounted from one to three per cent at Tientsin.^{11/}

The foreign banks, chiefly in the concession areas, had a good record as far as safety is concerned. But the real complications arise when we consider the notes of private factories, villages, and other small organizations, which have no place in a real currency system and whose presence, like so many other factors, merely added confusion to a system which already suffered from lack of unity and organization.^{12/} Even the barber shops, in this strange economy, have been known to issue paper money!

More romantic and historical than any other portion of China's currency was the tael, originally and almost exclusively a unit of weight (about 1 1/3 ounces) but coined in a few very rare cases. True to what may be expected in China, there was not one tael, with a fixed weight and fineness, generally accepted--but many varieties, ranging in weight from 500 to 600 grains of silver (32-39 grams). The word "tael" is probably of non-Chinese origin since the Chinese word for ounce is liang.^{13/} The principal taels were as follows:

Name	Weight in grains	Fineness	Actual Fine Weight
Haikwan	583.3	1.000	583.3
Kuping	575.8	1.000	575.8
Tsaoping	565.65	1.000	565.65
Shanghai	565.65	.935	518.512

11-Condcliffe, op. cit., p. 153

12-Kenmerer Report, pp. 59-60; and Leavens, op.cit., pp. 212-13

13-Chinese Economic Bulletin, Vol. 15, No. 1, July 6, 1929

The Shanghai tael was really the discarded Tsaoping tael, but with the added complexity that arose from the "olo" custom, by which 98 Shanghai taels of account were accepted as the equivalent of 100 Shanghai taels. To put this in another way, the Shanghai tael, although equal in weight to the old Tsaoping tael, and accepted in trade as its equal, had a fineness of only .935, whereas the Tsaoping tael had a fineness of 1.000. So there existed a Shanghai tael which contained, theoretically, 518.512 grains of pure silver.

But the Shanghai tael, as all others, was only a unit of account, nothing else. It was not a fixed weight and fineness ordained by the government but was maintained only by custom--and lack of anything to take its place. Further complications appeared in the use of sycee or "shoes", made up of silver equivalent to about 50 taels, and stamped by private smelting houses. These "shoes" were examined by the Public Assay Office (a private institution) where the examiner scorned scientific devices and estimated the fine silver content by the color and size of the shoe. The remarkable fact is that these men rarely misjudged the value of the sycee. But since these smelting and assaying shops had to exact a toll for their services, to turn out a tael with a theoretical content of 518.512 grains required the presentation, in 1930, of 521.619 grains to the assay office.^{14/} The sycee were used mainly in Shanghai, Hankow and Tientsin.

For many years the Haikwan tael was used for the listing of all foreign trade statistics and by treaty was equal to Sh. Tls. 1.1140 (1.1140 Shanghai taels). In Shanghai, the banks carried about one-half

14-Leavens, op. cit., pp. 207-9

of their reserves in taels, and large boxes containing about 3,000 taels, or 60 "shoes" were used to settle balances between banks. More recently, as indicated elsewhere, silver dollars and silver bars have been used in greater proportion, the "shoes" being melted down and recast.

When prices were quoted in taels and dollars there was an added confusion to consumers, business men and bankers. Double accounting and a daily rate of exchange between dollars and taels was the highly undesirable result. To get cash, for example, one had to exchange taels for Chinese dollars and then exchange dollars for cash. The exchange shop or bank often made both transactions at once so that only one commission payment was necessary but there was the possibility, nevertheless, of an adverse rate on one or both of the exchanges. So we may add to the fluctuations in the gold value of silver, secondary fluctuations in the values of the various circulating media in terms of each other and in terms of silver; paper money, copper coins, fractional silver, silver dollars, and silver bullion fluctuating constantly. Silver has been considered the main reason for these fluctuations because of China's long adherence to the silver standard despite the world trend towards the use of gold. Therefore, it is necessary to consider silver in relation to China and to remember that silver is perhaps more accurately described not as a standard of value in China, but as a basis for trade.

silver

About 1870 there began the world-wide trend towards the gold standard which left China, eventually, as the only country of importance still retaining the white metal as its standard of value. In the late years of the Nineteenth century and the first decade of the Twentieth century almost every other Asiatic country followed the lead of the

Western powers. Japan changed to the gold standard in 1897, India to the gold-exchange standard in 1893, Siam in 1902, the Philippine Islands in 1903, and the Strait Settlements in the years 1903-1906.^{15/}

This solitary position of China with respect to the silver standard was an aggravating circumstance of vital importance in the history of Chinese currency.

There were, of course, no fixed pars of exchange between China and the gold standard countries. There were moving pars, shifting ratios which reflected the fluctuating gold value of the silver unit. Around these moving pars the day to day fluctuations in the rates of exchange took place. For the par of exchange the smelting shop number of grains (521.619) was used. The leading silver market of the world was formerly London but in recent years the New York market has pressed London for leadership. In New York silver is quoted in cents per ounce of 479.520 grains of silver, 1.000 fine; in London the quotation is in pence per ounce of 444 grains of silver, also 1.000 fine. This can be shown by the simple formulae below:

$$\frac{521.619}{479.520} = 1.088$$

$$\frac{521.619}{444.000} = 1.175$$

which mean that the New York price, multiplied by 1.088, the constant, and the London price multiplied by its constant, 1.175, give the parities of the Shanghai tael in gold cents and sterling pence respectively.^{16/}

There were silver "points" above and below this parity, just as there are gold "shipping points", and the rate of exchange, at any time, could not go beyond either of these two rates without forcing the export

15-Condcliffe, op. cit., p. 165

16-Leavens, op. cit., pp. 206-9

of silver by the country against which the rate was moving. But there was considerably more freedom between the silver points than between the gold points because the larger bulk made for higher shipping cost than for gold. Consequently, although gold rates have a possible movement of .5% above or below par, silver exchange could fluctuate as much as 2.5% on either side before causing a specie flow.^{17/}

The fundamental question to be answered is this: has China's adherence to the silver standard injured or benefited her economic life? The problem becomes at once the problem of comparing stable exchange rates with fluctuating exchanges, for the gold standard provides the former, silver the latter. The discussion must include, however, not only the gold and silver standards but other possibilities, such as a managed exchange standard. Many arguments have been levied against unstable exchanges and these arguments have in turn been used against the continuation of unstable exchanges for China. But it is not correct to confuse the two problems. For example, to prove that unstable exchanges are either good or bad for foreign trade does not necessarily prove it to be true for China. Customs and habits, the nature of the economic organization, may alter considerably the theoretical conclusions. A conclusion may be correct and yet the reasons for that conclusion incorrect. Some such situation is to be found in discussions of the problem of stability of the exchanges for China.

Table / in the statistical appendix (p.153) shows the exchange value of silver from 1920 to 1937. Since 1873, when demonetization of silver by other countries began, the trend in the price of silver

17-Ibid., p. 208

has been down. It rose in the war years, but fell sharply after 1920 as production increased. India released more of her demonetized silver and at the same time stopped her own demand for more. Moreover, the rising price of gold lowered the value of silver. In June, 1930, silver hit an all-time low of $33\frac{1}{2}$ ¢ per ounce. This represented, of course, a change in the par value of silver units, with a consequent change in the rate of exchange. In the pre-war years the parity fluctuations averaged about 25% of the average price of silver in pre-war years. It rose 65% in 1919 and fell 55% in 1920.^{18/} From January to October, 1930, the rate of exchange varied from G\$1.00 = \$2.20 to G\$1.00 = \$2.50; and during the ten year period, 1920-1929, from G\$1.00 = \$.79 to G\$1.00 = \$2.50.^{19/}

It is customary to point out at once that these vicissitudes are the cause for China's economic backwardness and to add that the establishment of a gold standard would remove these difficulties. Both of these contentions need further analysis, however, before we can concur. The particular aspects of China's economic life that are affected by the use of silver will be treated below under separate headings. At the present our problem is the general theoretical problem of unstable versus stable exchanges.

Our task is first to ascertain the way in which the value of silver is determined. Mr. Y. C. Koo, in a memorandum submitted to the American Economic Mission to the Far East, in 1935, (and later published in the China Quarterly)^{20/}, offers what he terms a new and more accurate approach

18-Ibid., p. 208

19-Kemmerer Report, p. 65

N.B.: In this essay the sign "G\$" refers to United States gold dollars, the sign "\$", to Chinese silver dollars.

20-Koo, Y.C., "Silver: A Memorandum Submitted to the American Economic Mission", The China Quarterly, Vol. I, No. 1, September 1935, pp.81-93 Shanghai, China

to the problem of the value of silver. The value of gold is determined, he says, by its use as money, not by its use for gold teeth. Why then do economists fail to recognize that the price of silver is set by its use as money in China and not by its use in the arts?^{21/} The supply of silver comes from demonetized hoards and as a by-product of other minerals. The demand in the arts is fairly stable. Therefore, the demand for silver in China represents the marginal demand which sets the price of silver.^{22/} But this argument assumes the industrial demand for silver to be absolutely inelastic--which is certainly not true. It also fails to appreciate that what is true of gold and its value is not true of silver for the very reason it is true of gold: that most nations do use gold for money and China almost alone uses silver. Therefore, it does not seem to be sound to argue that China alone determines the price of silver. Koo admits that special circumstances may indeed take away China's function as the marginal demander of silver, and even make her the marginal seller,^{23/} but this merely makes his own case weaker. It becomes an argument which holds that China is the marginal demander of silver when she is the marginal demander of silver.

But Koo carries his argument still further and declares that the price of silver is set by China with two objectives in mind: "to tend to effect a state of equilibrium between Chinese prices and international prices, and secondly, to enable China to have just enough favorable balance of payments to absorb the amount of surplus silver supply offered at the rate as she determines."^{24/} If the price is set to equalize world

21-Ibid., pp. 82-3

22-Ibid., p. 83

23-Ibid., p. 83

24-Ibid., p. 84

prices with Chinese prices, there is only one possible point of equilibrium--and that equilibrium is not consistent with an import of silver which will raise Chinese prices and destroy it. In other words there are really many possible equilibria, each consistent with a certain quantity of silver imports, a certain effect on the Chinese level of prices and a certain price of silver. Which is to deny at once that China can set the price of silver, for with such a wide range any other factors may be the determinants of which point of equilibrium will actually come about.

Nor is it possible for China to set a price of silver which will ensure her a large enough balance of payments to purchase all the silver offered at that price. She does so only by accident, for if all were not taken, the price of silver would fall, leading to an increased sale to the arts as well as to China. The real determinant of the amount of silver imported by China is the balance of payments and the item in that balance which is most likely to determine the amount of funds free to purchase silver is immigrant remittances. For an examination of the balance of payments for China indicates that in all other major current items the flow of funds is out of China and it is generally admitted that the only item which made it possible for China to import annually a net amount of silver was emigrant remittances.^{25/}

Under equilibrium conditions a flow of silver to China causes a rise in prices (but no fall in prices elsewhere) and if the world price of silver is constant, silver will tend to flow out of China where it has greater purchasing power. In other words, the favorable balance of payments would tend to become an unfavorable balance and silver would

25-The balance of payments of China is discussed in detail below, pp.44-50.

move out as the export point was reached. How then has it been possible for China to import annually a net amount of silver? The answer would seem to be that in-payments have been underestimated and that internal and external prices have never been equated and, therefore, there never existed a perfect equilibrium between Chinese prices and world prices. Both of these matters will be considered in more detail below.

Koo's argument, furthermore, is subject to the criticism of circular reasoning, for it assumes a price of silver with China as the marginal demander in order to prove her to be the marginal demander. Certainly the amount of silver offered depends upon the price which exists in the world market, for the supply is not as inelastic as Koo assumes. Furthermore, as Professor Remer has shown, a falling price of silver encouraged the flow of remittances to China from the United States in ^{26/}1930, which meant an increase in the amount of silver going to China. It cannot be maintained, then, that China lowered the price of silver in order to get more silver for she could only attract silver to China by raising the price. The figures for this period give further weight to the argument that the real determinant of silver flow to China (in the sense of degree of importance) is emigrant remittances.

W. Y. Lin, the well-known Chinese economist, introduces his discussion of China's new monetary system with a section on the place of silver ^{27/}in the Chinese economy. The fluctuations within the silver points, he declares, are due to the net balance of payments. This, of course, is a truism. When the demand for bills in Shanghai exceeds the supply, the

26-Remer, C. F., Foreign Investments in China, pp. 184-86

27-Lin, W. Y., The New Monetary System of China

rate goes to the silver export point, and vice versa. But, adds Lin, in the long run the net balance of payments also determines the position of the silver points themselves by determining the price of silver. This is true because the Chinese balance of payments furnishes the marginal demand for silver.^{28/} Now here Lin seems to take a position midway between that of Koo and the writer. In fact, he then turns to Koo's article, quotes from it significant passages, and proceeds to accept this analysis despite the fact that it is inconsistent with his own arguments a few pages previous.

It must be remembered that when China gains silver and thereby allows her level of prices to rise, the nation which loses silver does not feel a corresponding urge to allow prices to fall as would be the case if silver and not gold were the universal standard of value. This means that the full effect must be felt upon Chinese prices or the rate of exchange on China. If the price of silver does not change enough to allow the rate to take the full effect, then Chinese prices must rise more. Nor can it be maintained that the rate will rise and therefore force the price of silver into line since we have already demonstrated that there are insufficient grounds for the contention that China's demand for silver is marginal and therefore price-setting. If equilibrium does not come about then, it is because the processes of adjustment are sticky, and when the general economic conditions of China are taken into account, the reasons for this stickiness are not difficult to understand.

Since the above discussion is in the nature of an extended introduction to the particular problems resulting from the use of silver by

28-Ibid., p. 6

China it is now time to proceed with those problems before any conclusions can be made as to the general effect of the use of silver on the economic system of China.

29/
The Foreign Trade of China

Before 1842 foreigners were allowed to trade in China only through the Hong merchants. Nor were the laws of the empire designed to further or facilitate such trade. But soon, after strong retaliation for supposed offences, the Western Powers forced China to open treaty ports, took over the administration of the Chinese Customs, and likewise deprived China of tariff autonomy. Yet despite all these efforts on the part of the Western World, the foreign trade of China was a negligible item as late as 1870.

In 1869, however, the Suez Canal was completed and 25% of the distance between London and Shanghai was saved. At the same time (1873) there began the decline in the gold value of silver as the white metal was demonetized by many nations. Both of these factors tended to stimulate trade with China, and although the expansion was not phenomenal, it did indicate the future possibilities of Chinese trade. The growth is shown below in Haikwan taels:

<u>Year</u>	<u>Exports</u>	<u>Imports</u>	<u>Total</u>
1871	66,853,000	70,103,000	130,956,000
1899	195,785,000	264,748,000	460,535,000

The year 1899 saw trade reach the highest total figure ever before achieved in China, but the Boxer Rebellion which followed shortly afterwards seriously curtailed this advance. Recovery, however, saw even greater

29-Where no other source is given, the reader is referred to tables in the statistical appendix, below.

heights reached while the balance of trade moved definitely against China.

Then came the World War with a consequent reduction in exports to China as the belligerents demanded more and more of the world's goods. This was partly offset by the stimulation given to Chinese exports to help satisfy the growing European demand for goods. Thus the balance of trade moved almost to the point where Chinese exports completely paid for Chinese imports. In terms of U.S. dollars the rise was even greater than in terms of Haikwan taels, for silver was rising in value and gold was falling. The close of the war changed all this; Chinese exports slumped badly; the European nations rushed to recapture their pre-war markets; silver fell in value even more rapidly than it had risen. Just as the rise in trade was exaggerated in terms of U.S. dollars, so was the fall in trade exaggerated by the inverse of the war-time situation: i.e., a rising value of gold, a falling value of silver.

Recovery, however, was rapid. Imports and exports, in physical volume as well as in Haikwan taels and U.S. dollars, rose steadily (with minor recessions) up to the fateful year 1929. Foreign trade showed an immediate reaction to the world situation, but not as much as one might expect. The silver slump which had begun in 1929 acted as a buffer between the world depression and China's industrial position. In terms of the physical volume of trade the decline was significant in the next few years, but not serious. In terms of U.S. dollars the decline was phenomenal, but in Haikwan taels, although exports suffered from a small recession, total trade rose rapidly to a new high

in the year 1932. But here we must leave the history of China's trade development for the time being and consider in more detail the effect on this trade of the use of silver by China.

It is customary among business men and economists to maintain that unstable exchanges are inherently detrimental to a nation's foreign trade.^{30/} In the incisive style of his remarkable work on International Monetary Issues, Whittlesey points out that there is no more reason for protecting the foreign trader against price vagaries than the investor, the insurance purchaser, etc. Nor does it seem just that the security of the foreign trader is often purchased at the expense of other business groups.^{31/} The three objections most often raised against unstable exchanges are, "first, that a decline in the value of any monetary unit relative to foreign currencies has the effect of stimulating exports from, and of retarding imports to, the country whose currency is depreciating. In the second place, it is held that variations in the exchange rates introduce an element of risk that seriously impedes trade. Finally, such exchange fluctuations are alleged to lead to the erection of direct barriers, such as quotas and exchange controls, to the movement of goods between countries."^{32/}

Depreciation, it is generally admitted, is a stimulus only for a short time. As soon as external and internal prices are adjusted to each other again the advantage is gone. But although we may agree with Whittlesey that such processes may be delayed on gold as well as on

30—"No idea," writes Professor Whittlesey, "is more firmly entrenched in the general and even the semi-professional economic consciousness than that stable foreign-exchange rates are essential to active foreign trade." Whittlesey, Charles R., International Monetary Issues, p. 77

31-Ibid., p. 77

32-Ibid., p. 78

fluctuating exchanges, in the case of China such processes are unduly delayed. A rising gold value of silver encourages imports, but higher prices in general in the Western world and transportation costs tend to nullify much of this advantage. Also there is a noted tendency for such an advantage, if it does appear, to "stick" with the wholesaler, as it takes considerable time for domestic prices to adjust themselves. But when the opposite cause operates, and exchange is less favorable, the trader is the first to feel the results. A falling rate (falling gold value of silver) causes a rise in the cost of imports and cripples the import trade, since the Chinese, having paid a certain price for an article for some time, cannot understand why the same article should suddenly cost more, especially since wages have not risen. This is further aggravated if it is remembered that prices must be transferred, in many cases, to copper and "small" money prices. So the Chinese refuse to buy until the price falls: the merchant must sell his goods at a loss, if at all. The importer receives no further orders and may not be paid for past orders. Exports should be encouraged, but high transportation costs and a slow, inefficient, and inadequate transportation system prevent any great increase in the movement of goods for some time. As the disequilibrium reaches the domestic price level a whole series of disequilibria are set up, making even greater confusion in prices and trade. It is under these conditions that China must carry on her trade, 95% of which is with countries on the gold standard and therefore having stable exchanges.

The risk element introduced into foreign trade by the presence of unstable exchange rates must next be considered. Here again Professor

Whittlesey explodes his bombs in rather devastating fashion by pointing out that risk is not necessarily a deterring influence on foreign trade, that hedging is possible, that the statistics of trade cannot lead us to any definite statement concerning the effects of unstable exchange rates on foreign trade.^{33/} It is true indeed that all international trade involves some speculation, but in Chinese trade the speculation is so great as to make the international merchant more a speculator than a trader. A Chinese merchant orders goods at a certain price in gold for delivery at a certain date. The importer, as Whittlesey points out, is safe since he buys and sells in gold; but the merchant in China for whom he bought the goods is at the mercy of the exchange rate since he buys in gold and sells in silver or copper. He can hedge, it is true, but in so doing he takes the chance of paying more for his goods than he might have to had he not hedged. This would be no drawback were it not for the fact that "spot" buyers are constantly ready to purchase goods at any favorable moment. Thus if the merchant hedges he may be undersold and lose regardless. So he must "bet" on the exchange rate whichever method he chooses. Even if hedging were widely used, its cost, because of the extreme danger under unstable conditions, would be so great as to act as an indirect tax on foreign trade, tending to cut down the volume. The importer worries with the merchant, for should his client lose money, he stands to lose also. This led many importers and exporters to "carry" merchants on their books who lost money steadily, since they could not afford to let go once they had invested in the merchants' business, and it was to their interest to give them a chance to recoup their losses.

33-Ibid., pp. 81-85

Therefore, although Whittlesey's comments on unstable exchanges are generally sound, they cannot be applied directly to the Chinese situation. Whittlesey presupposes a modern industrial nation, with an adequate financial structure. In China, as we have indicated above, this does not exist. There is a profound difference between unstable exchanges in the western world as the result of the permanent abandonment of gold and unstable exchanges in China which are the result of adherence to silver when the world uses gold, an incomplete and faulty silver standard monetary system, the lack of an adequate and responsible banking system, and the lack of government unity and authority. Unstable exchanges have indeed been a hindrance to China's economic development. On the other hand, China's lack of economic development has aggravated the influence of her unstable exchanges.

China has, indeed, become a land of speculation. Buying and selling of gold bars was a hedging device, but also led to confusion in legitimate trade. Interestingly enough, the speculation in gold bars--buying and selling in furious fashion--took place without any gold bars actually changing hands since there were none to exchange.^{34/}

This brings to mind another serious obstacle in the path of monetary reform. The business of exchanging various monies within China is vast and consumes the energies of a large group whose vested interest in instability has created a class which may sabotage any movement at unification or reform of the currency. Theirs, indeed, is a livelihood that depends upon instability, uncertainty, confusion and chaos.^{35/}

34-Leavens, *op. cit.*, p. 210

35-Mr. J. B. Condliffe protests against this "unproductive" money-changing. (Condliffe, *op. cit.*, p. 154). But surely, under such conditions, such activity is not unproductive. Only when a proper and unified monetary system is established in China will such labor be unproductive, for money-changing will no longer be "productive" of income.

Professor Whittlesey cautions us about one more matter which is worth our consideration at this point. "Far too much emphasis has been placed upon exchange rates as a determinant of foreign trade. The ultimate determinant of trade, both exports and imports, is the balance of payments, within which exports and imports are merely two, albeit two very important, entries among many; the exchange rate is much less determinant than determined."^{36/} Our problem seems always to return, then, to that of the balance of payments which seems in every way the key to the complexities of the Chinese scene. All understanding of monetary problems in China may be said to be conditioned by the understanding of the Chinese balance of payments. The disturbances and risks involved in China's foreign trade because of her adherence to the silver standard do not so much reflect unstable exchanges as they represent a poorly functioning monetary system. A system as poor in organization and centralization would, even with gold as the standard, suffer from these disturbances.

The Balance of Payments

As true as it is that a knowledge of China's balance of payments is a fundamental requisite to a knowledge of China's monetary problems, it is equally true that this field has until recent years been painfully neglected. Today, with the publication of Professor Remer's "Foreign Investments in China" the problem of the balance of payments has come into its rightful place in the field of research among those interested in the economic problems of the Far East. In fact, there is little that can be said in this field which does not refer indirectly or directly

36-Whittlesey, op. cit., p. 79

to the work of Professor Remer. Because of the political and economic conditions of the country the construction of an acceptable balance of payments account was and still is an extremely difficult task. A summary statement of the net annual balance of payments for the years 1902-1930 appears below: (in millions of Chinese dollars)^{37/}

<u>Inpayments</u>	<u>1902-1913</u>	<u>1914-1930</u>
Remittances	150.0	200.0
Capital Imports	113.8	97.4
<u>Outpayments</u>		
Trade and Specie	148.6	280.3
Debts and Investments	158.5	209.7
Unexplained Difference	43.3	192.6

38/

Average Annual Balance of Payments for China, 1914-1930
(in millions of Chinese dollars)

<u>Outpayments</u>		<u>Inpayments</u>	
<u>Current items</u>		<u>Current items</u>	
Government debt	70.9	Overseas remittance	200.0
Business investments	138.8	Gold Exports (net)	3.3
Merchandise imports	1,297.3	Merchandise exports	1,025.
Silver imports (net)	62.9	Correction of exports (5%)	51.3
Total	<u>1,569.9</u>	Total	<u>1,279.9</u>
<u>Capital Items</u>		<u>Capital Items</u>	
		New Business Investments	73.6
		Loans of the Chinese Government	23.8
		Total	<u>97.4</u>

Net outpayments on current items	290.0
Inpayments on capital items	97.4
Unexplained difference	<u>192.6</u>

In general it may be said that China's receipts of capital imports and remittances from Chinese overseas have paid for her current net outpayments for goods, specie and investments. Nor is it likely, or

37-Based on Remer, op. cit., p. 206

38-Remer, op. cit., p. 221

desirable, that this situation will change much in the years immediately ahead. If China is to expand and modernize her economic system she must import capital. Chinese overseas will continue to send funds to China for one reason or another and thus make available for China's use a large amount of foreign exchange. Current out-payments on debts and investment will likewise continue to play an important role in the balance of payments as China has borrowed and will continue to borrow in the future, and on these borrowings current payments must be made. Some adjustment of these payments coincident with the adoption of a stable monetary unit is likely and this may mean a saving to China, as well as a greater degree of certainty in her payments. The balance of trade should cause no great anxiety, for it is extremely difficult for a borrowing nation to have a favorable balance of trade. In fact, to have such a balance would mean for China the cutting down of capital imports, which is inconsistent with her economic position. Specie outpayments may be reduced in the future if China becomes a steady seller of silver and uses the mechanism of the gold exchange standard. But this item is in any case less important than those mentioned above.

We have already noted how changes in the value of silver affect the balance of trade. Other items in the balance of payments also may be expected to react to such fluctuations in the value of silver. When silver is falling in price and Chinese exchange in silver also falls, inpayments resulting from emigrant remittances tend to increase, as pointed out above, because it is more profitable to transfer at that rate than when foreign money is worth less in Chinese money, as would be the case at a higher rate of exchange. But minor remittance for the

upkeep of embassies, foreign troops, etc., would tend to fall off, as only a certain amount of exchange is desired and it may be bought merely by using less units of the foreign money. Capital items increased sharply during the years when silver price was falling, 1928-1930, again indicating the effect of silver movements on the balance of payments, and also disproving what is often stated as an axiom: that unstable exchange rates prevent and hinder the flow of capital funds. We shall see that a period of prosperity existed in China during the first two years of the world depression.

The following table shows the balance of payments for China for 1928-1930 and serves to illustrate also the effect of a change in the value of silver on the balance of payments, for between 1928 and 1930 the price of silver fell drastically.^{39/}

The Balance of Payments of China 1928-1930
(millions of Chinese dollars)

	<u>1928</u>	<u>1929</u>	<u>1930</u>
<u>Outpayments</u>			
<u>Current items</u>			
Government debt	63.0	79.1	111.4
Business investments	179.0	198.5	198.0
Merchandise imports	1,794.0	1,898.7	1,964.6
Gold and silver imports		158.7*	100.5*
(net)	168.7		
Travelers and students abroad	6.0	6.0	8.0
Diplomatic and consular offices			
abroad	4.4	4.4	5.0
Remittances by foreigners in			
China-professional classes	0.5	0.5	1.0
Insurance	15.0	15.0	20.0
Motion picture royalties			8.0
Total	<u>2,230.6</u>	<u>2,360.9</u>	<u>2,416.5</u>

*-silver only

39-Remer, op. cit., pp. 221-22

The Balance of Payments of China 1928-1930 (continued)
(millions of Chinese dollars)

<u>Inpayments</u>	<u>1928</u>	<u>1929</u>	<u>1930</u>
<u>Current items</u>			
Overseas remittances	250.6	280.7	316.3
Gold exports (net)	0.0	3.0	24.9
Merchandise exports	1,487.0	1,523.5	1,342.3
Unrecorded gold exports	0.0	0.0	22.5
Correction of exports	74.4	114.3 (7½%)	134.2 (10%)
Tourist trade	30.0	30.0	40.0
Mission and philanthropic remittances	25.0	30.0	40.0
Diplomatic and consular offices in China	30.0	32.0	38.0
Foreign military and naval establishments	139.7	124.0	100.0
Total	<u>2,056.7</u>	<u>2,137.5</u>	<u>2,058.2</u>
<u>Capital items</u>			
Sales of domestic securities to Chinese overseas	4.0		
New business investments	96.0	170.0	202.0
Total	<u>100.0</u>	<u>170.0</u>	<u>202.0</u>
Net outpayments on current items	193.9	223.4	358.3
Inpayments on capital items	<u>100.0</u>	<u>170.0</u>	<u>202.0</u>
Unexplained difference	<u>93.9</u>	<u>53.4</u>	<u>156.3</u>

A few words must be added concerning the "unexplained difference" in the Chinese balance of payments. That difference has always perplexed and confused students of China's monetary system. It arises from the confusion which surrounds the very nature of inpayments and outpayments, from smuggling of goods (and "unreported" trade), from a host of minor items which until recently were never carefully analyzed and estimated, from the disunity and lack of organization which prevails in the entire economic and political life of China. Professor Remer has added much to our knowledge of this unexplained difference, but there still remains a substantial sum to defy the observer. Perhaps in the future these secrets

will be disclosed, but in any case the future will probably find the "unexplained difference" rapidly diminishing in size, both absolutely and relatively to the total balance of payments.

The basic problem, however, is the question of the adjustment in the balance of payments after a dis-equilibrating force has entered the picture. The normal process of adjustment between two gold standard countries does not function between China on silver and the world on gold. This normal adjustment would take place through the movement of specie and consequent price changes, or through the movement of goods without a change in relative prices through the transfer of purchasing power (as Ohlin argues). These forces always move in the opposite direction to the disturbing force and are, therefore, equilibrating in nature. But China on the silver standard is unable to use either method. The price adjustment does not take place because different species are used and a loss of gold causing contraction in the United States would not necessarily lead to an expansion of credit in China or would the loss of silver to China cause a contraction of credit in the United States, whereas it would cause an expansion, to some extent, in China. Furthermore, the use of silver effectively discourages any corrective flow of short time funds to China.^{40/} The adjustment, then, is achieved by the effect, outlined above, of movements in the price of silver on the items which make up China's balance of payments. The "hottest" of these items--from the point of view of ability to react quickly to changes in the value of silver--are remittances from Chinese overseas and silver itself (considered as an item of physical trade rather than as money).

40-Ibid., p. 47

We may summarize by saying that in the long run the value of silver is set by the various factors which make up its demand and supply. One factor of major importance in the demand for silver is the Chinese demand which in turn depends upon the price. The most significant of all items in the Chinese balance of payments (from the view of adjustability) is emigrant remittances. Emigrant remittances in turn depend in great part upon the price of silver exchange in China. The price of silver exchange in turn depends upon the whole balance of payments within the limits set by the cost of shipping silver, the par being, of course, determined by the world price of silver.

Banking

The first banks in China were exchange shops and pawn shops and as late as 1910 foreign organizations did all the real banking in China. The Manchus, in their last years, organized two banks which the Republic has continued: The Bank of China and the Bank of Communications. These banks have been forced to lend to governments and have lost many times in such ventures, but, as a whole, have done remarkably well. In 1929 the National Government organized the Central Bank and the other two became semi-official.^{41/}

A great deal of what may be called modern banking is done by foreign banks. This development has been aided in part by circumstances and in part by political control as well as by the initiative of the private banks.

The native banks, patterned after the original Shansi banks, were at

41-Leavens, op. cit., p. 212

first "uncontrolled, unregulated and uncoordinated." Nor were they related directly to the currency system of the country.^{42/} Although many of these banks have failed, there still exists a large number which are gradually beginning to operate along western lines. One source of friction in China today is the fact that the foreign banks handle the government business connected with the salt and customs revenues, a situation which is bitterly resented by the native bankers. Also the foreign banks almost necessarily finance the great portion of China's foreign trade. Although sound commercial banks in addition to the semi-official banks mentioned above existed in China before 1929, they were in general inferior to the foreign banks in services and financial strength. The great period of banking reform did not begin until after 1929.

Fiscal Policy

Let us now turn to an examination of China's fiscal policy and her foreign debt in their relation to needed monetary reform. "China's public finances are weak. Her financial credit is at a low ebb, the provincial and national governments are impoverished, taxation is multifarious, indirect, inequitable, and insufficient, the collection of revenue is interfered with by local autonomy, there is cruelly heavy expenditure upon civil war and upon the service of the existing debt, and the main sources of revenue are already burdened with debt commitments."^{43/} Here is an eloquent and truthful picture of the sad plight of China's financial position. Here are the conditions which sweeping reform can alleviate or remove

42-Condliffe, op. cit., pp. 155-56

43-Ibid., p. lll

completely.

Let us look first at the balance sheet of the Chinese National Government. A. G. Coons estimated^{44/} that the average annual revenue of the National Government between 1917 and 1924 was between 173 and 234 million Chinese dollars; but, in his opinion, in no year did the National Government actually receive more than about 180 million dollars. This is a startling fact and at the same time a significant commentary upon the economic and political position of China. The figures for the provincial governments are not even available because of the multiplicity of taxation and the corruption and inefficiency associated with its collection and disbursement.

⁴⁴-Ibid., p. 122, quoted from Coons, A. G., The Foreign Public Debt of China, University of Pennsylvania, 1930

45/

Receipts of the National Government
1928-29 and 1929-30

(In millions of Chinese dollars)

	<u>1928-29</u>	<u>1929-30</u>
A. Revenue		
I. Taxes		
1. Customs	179.1	975.5
2. Salt	29.5	122.1
3. Rolled tobacco and kerosene	27.7	36.6
4. Collected by provinces	14.5	11.4
5. Tobacco and wine	3.5	6.8
6. Stamps	3.0	5.4
7. Flour	2.0	3.9
8. Parcel post	.9	- -
9. Miscellaneous	- -	21.9
	Total Taxes	483.7
	Less cost of collection	45.6
	Net tax receipts	260.6
II. Miscellaneous revenue	1.9	- - - -
III. Unclassified		
1. National revenue collected and spent by local government for military purposes	62.4	- - - -
2. Miscellaneous	7.6	- - - -
B. Refunds		
I. Return of Russian indemnity	1.7	- - - -
II. Other refunds	.1	- - - -
C. Bonds, treasury notes, loans	100.1	100.9
	GRAND TOTAL	434.4
		539.0

45-Condcliffe, op. cit., p. 121

46/

Expenditures of the National Government
1928-29 and 1929-30

(In millions of Chinese dollars)

	<u>1928-29</u>	<u>1929-30</u>
I. Party Expenses	4.0	4.6
II. Civil Establishments		
1. State council	4.1	1.8
2. Executive yuan	22.3	29.8
3. Legislative yuan	.5	1.0
4. Judicial yuan	.5	.4
5. Examination yuan	.2	.6
6. Supervisory yuan	.4	.6
7. Famine relief	- -	10.0
8. Subsidies to provinces	4.7	6.7
9. Miscellaneous	1.4	.5
Total civil expenses	34.1	51.5
III. Military establishments	209.5	245.4
IV. Transfers to local governments from salt revenue	- - -	35.6
V. Loan service	121.3	159.0
VI. Indemnity service	38.7	41.2
VII. Advances for capital of Central Bank	20.0	- - -
VIII. Suspense	6.8	1.7
GRAND TOTAL	434.4	539.0

47/

Percentage of National Government Expenditures for 1928-30

	<u>Per Cent of Total</u>	
	<u>1928-29</u>	<u>1929-30</u>
I. Party expenses	.9	.9
II. Civil establishments	7.9	9.6
III. Military establishments	48.2	45.5
IV. Transfers to local governments	- - -	6.6
V. Loan service	27.9	29.5
VI. Indemnity service	8.9	7.7
VII. Central Bank Capital	4.6	- -
VIII. Suspense	1.6	.2
Total	100.0	100.0

46-Ibid., pp. 124-25

47-Ibid., p. 125

These three tables add much to our understanding of China's poor financial position. The most striking fact is the tremendous proportion of the total national revenue (pitifully small as that total is) which is devoted to three items: military establishments, loan services and indemnity payments. In the two years studied above, these three items accounted for between 82% and 85% of the total income of the National Government. Less than 10% can be said to have been employed for the true civil functions of government, and a truly disproportionate amount of this was for the use of the executive yuan, while the legislative and judicial yuans received practically nothing. These facts, too, are explicable only in the light of politics--National Government politics.

We notice, too, that in 1929-30 the total tax collections were 433.7 million dollars and that the cost of collection was 45.6 million dollars. A collection cost of almost 10% is far too great and is indicative of poor administration, corruption, or both. The last item of the receipt column is also interesting. The Chinese government has been spending more than it received; while this in itself is no disgrace in the family of nations, especially in recent years, when we consider that the Chinese government has had no great relief expenses (not that they could not have been used) we must look with alarm at a government that depends upon borrowing for over 20% of its annual expenses.

The source of income is changing. It has, in fact, already changed. There was always a land tax in China. It came, literally speaking, in Chinese belief, from the gods. From the year 2000 B.C.E. down to the fall of the Tsing Dynasty in 1911, the land tax was based on the theory that the state owned the land and allowed the farmers to work, charging

a fee for this privilege (usually payable in kind). In 1927 the Nanking government made this land tax a local affair, with a surtax levied for the National Government. From the tables above it can be readily seen, however, that the income of the National Government is today mainly derived from the customs revenue. The sharp rise in customs receipts in 1929-1930 over the previous fiscal year was due mainly to the fact that tariff autonomy was restored to the Chinese government, enabling the Nationalists to raise the tariff schedule.

Between 1927 and 1930 the provinces as well as the National Government levied many surtaxes above the regular land tax as well as increased taxes on goods moving between provinces. The Government gave as its reason for this action its desperate need of funds and inability to increase revenue so long as the tariff was controlled by other nations. Tariff autonomy has hastened the repeal of many internal restrictions to trade such as the internal export and import levies of Sh. Tl. 0.27 on each tan (15 tan equal one ton) of tung oil as it moved from Hankow to Shanghai for shipment abroad. Perhaps the slump in tung oil exports which followed helped cause the elimination of these impediments to trade, but the Chinese government protested bitterly that it was solely the fault of the U. S. protectionist policy--Congress having voted a sizeable subsidy to the infant tung oil industry of Florida. It seems more logical that Chinese internal restrictions to trade, coupled with a falling price-level for agricultural products, made the opportunity for interested parties to secure the subsidy for tung oil in the U. S.

Custom Revenue in U. S. Gold Dollars^{49/}

(000 omitted)

	<u>1914</u>	<u>1930</u>	<u>1931</u>	<u>1932</u>
Maritime customs	26,074	107,085	83,502	67,681
Native customs	2,606	3,039	765	-----
Total customs	28,680	110,124	84,267	67,681

This does not indicate that internal import and export duties were of no importance in 1932, but it does mean that some of the multifarious internal taxes had disappeared. The tax program of the National Government and the provinces still requires a thorough overhauling and unification. The annual income of the government must be increased, but it must be done efficiently and the funds must reach the National Government; and the National Government must use its income in a more productive fashion.

One of the greatest evils which her monetary system visited upon her is apparent when we consider China's foreign debt and the problems arising from it. Regaining tariff autonomy and the collection of customs duties in the new gold unit aided China somewhat, but the basic problem remained. Eduard Kann estimated the foreign debt of the National Government alone on January 1, 1933, as follows:^{50/}

In U. S. Dollars

Domestic loans	151,422,000
Foreign loans	317,524,000
Total	468,966,000

49-Moser, C. K., "Economic Notes On China", Special Circular No. 271, Far Eastern Series No. 132, Department of Commerce, Bureau of Foreign and Domestic Commerce, p. 2. The figures were converted from Haikwan taels to gold dollars by the writer at the following rates of exchange: 1914, G\$.67; 1930, G\$.46; 1931, G\$.34, and 1932, G\$.338.

50-Ibid., p. 2

The foreign portion of the debt was secured as follows:^{51/}

Security for the Foreign Debt

Customs revenue	164,112,000
Salt revenue	80,928,000
Nominally secured	72,483,000
Total	317,425,000

China was for years unable to make an adequate adjustment of her foreign debt. 97% of the debt is in terms of gold upon which payments must be made in gold, yet China could only collect revenue in silver. As the price of silver fell, there was, in effect, an increase in the debt burden. Monthly expenses on debt payments were \$1,000,000 (Chinese) greater in October, 1929, than the service of the same debt in January 1929, merely as the result of the decline in the world price of silver.^{52/} When that very slump continued through the summer of 1930 the Chinese foreign debt was, in silver dollars, twice what it had been in 1928. It was for this reason that after Chinese tariff autonomy was achieved, the theoretical gold unit was established in which all imports were valued and all duties levied and paid. It was a step in the right direction, but not a final solution. China on a silver standard was still helpless against many forces and currents which were contrary to her needs and desires. Not until the entire monetary system is unified and reformed upon some stable standard will these problems be solved.

It is true that a rise in the price of silver would make the debt burden lighter, but such rises have been few and far between and usually associated with perhaps greater dangers to the Chinese economy than a falling price of silver. Secondly, the very fact of instability and

51-Ibid., p. 2

52-Kemmerer Report, p. 71

variation made it impossible for China to plan her budget for an entire fiscal year, as do other countries where the debt burden is a fixed and known amount. More important than either of the above reasons is the fact that China, both as a government and as a business nation, must borrow heavily abroad in the future if she is to expand industrially, yet neither the government nor private industry can get the required funds properly while the currency system is haphazard and chaotic.

Conclusion

China has not been unaware of the need for monetary reform and financial rehabilitation. In 1914 a Coinage Law was passed which created the Yuan silver dollar, fractional silver in denominations of 50, 20, and 10 cents, nickel five-cent pieces, and copper coins valued at 2 and 1 cents and fractions thereof. They were all intended to circulate at par--as "big money"--and thus a national currency was almost achieved. But the usual evils of over-issue and excessive seigniorage caused depreciations to the level of other coins in circulation.^{53/}

The problem we have here reviewed briefly is a vast one. Reform is greatly needed, yet we must not minimize the tremendous obstacles to be overcome or the limitations imposed, for the time being at least, by the multifarious forces of both internal and external politics. To this problem we return later.

The Chinese currency system needs a thorough-going reform if China is to prosper. That reform must include a new system of coins, a new system of notes, and a new monetary standard. There must be only one kind of each subsidiary coin and the various coins in circulation must

be decimal divisions of a unit, with interchangeability of all coins. There must be only one mint authority, and a uniformity of weight and fineness of all coins. There must be no provincial coinage whatsoever.

The above must be also true of the new paper money system and there must be established a responsible Central Bank with the sole right of note issue and the duty of maintaining the value of the notes at a legal coin parity. There must be convenient places for the exchange of coins and notes at par.

As for the new standard of value, China must recognize that a standard similar to that employed by the rest of the world would be of great help to industry and trade. If adherence to silver for so many years has taught China anything, it should have indicated the folly of playing the game of international monetary relations with chips different from those used by her opponents.

When some practical plan for monetary reform has been adopted "one of the serious handicaps to the development of industry will have been removed. Inter-provincial distribution of goods will take place with greater assurance, and to a greater extent, thus widening the market for the products of industry, which in turn will stimulate production. The need for reform of the currency will be emphasized as more adequate communications are established, and the consequences of reform will be more marked with each such advance."^{54/}

54-Vinacke, H. M., Problems of Industrial Development in China, p. 123

Chapter IV Twentieth Century Proposals for Reform

To admit that monetary reform is necessary in China is one thing; to get a particular program adopted is quite another; and to see that program put into operation is still another. At the outset we must recognize the difficulties in the way of a reform that must be so sweeping as to constitute a major change in Chinese life. The Kemmerer Report was the seventh major reform proposal since 1900, yet its Introduction, as we have seen above (p.23) says that monetary conditions were far worse in 1929 than in 1903.^{1/} This indicates the progress of reform in the first quarter of the century, and since the world depression followed hard on the heels of the Kemmerer Report it is to be understood why relatively little was done to correct the existing evils.

The fundamental principles of the reform proposals which preceded the Kemmerer Report are shown below in summary form, with brief comparison and evaluation of the various plans on certain basic questions.^{2/}

1903 Economic disturbances growing out of the troubled war years (1900-1902) led the Chinese government in 1903 to invite the United States to send to China a commission to study Chinese monetary conditions. On March 3, 1903, Congress authorized a Commission on International Exchange, composed of Hugh Hanna, Charles A. Conant, and Jeremiah W. Jenks. This commission was to study monetary conditions in China and Mexico and, after conferring with European authorities, make suitable recommendations for the adoption of the gold exchange standard by the two countries under consideration. The commission

1-Perhaps the main reason why currency and monetary conditions were so much worse in 1929 than in 1903 is that during those years China began to industrialize, to expand her economic life, especially in the sphere of international trade. The existing evils were, consequently, more obvious and more disturbing. As economic development goes on, it is easily apparent, the need for a smoothly functioning monetary system becomes more crying.

2-Kemmerer Report, Appendix H, and
Kann, Eduard, The Currencies of China, pp. 356-95
The single spaced summaries which follow are based on the materials listed in this footnote. The double spaced sections which follow each summary are the writer's comments.

proposed a gold exchange standard with an alternate silver standard based on the use of the Kuping tael. A gold unit equal in content to G\$.30 was proposed, equal also to two shillings by treaty. The silver dollars were to have a metallic content equal to 85% of face value, and, along with new subsidiary coins, were to be issued by the government in payment of its obligations. Definite rates of conversion between the old and new coins were also recommended as an aid in securing popular acceptance of the reform. To maintain the gold exchange standard the government was to be empowered to buy and sell drafts on New York and London at a premium which covered the cost of shipping gold. A gold reserve of at least 35% was required, most of which was to be held in foreign balances. The tael was to be slowly withdrawn. A private central bank with a capital of G\$20 million was proposed, with the government having a share in its management and profits. This bank was to have control over the issue of paper money. The entire commission agreed that a direct change to the gold standard through the device of the gold exchange standard was immeasurably better for China than unification on a silver basis with the transfer to the gold standard coming at a later date.

As a whole this plan was sound and workable, utilizing as it did the well-known mechanism of the gold exchange standard to maintain stability of the rate of exchange and establishing modern devices for credit control and management. But several flaws appear. The value of the silver in the unit proposed (85% of its face value) was too high, not allowing a sufficient margin of safety to prevent the melting down of the new coins after a relatively small rise in the price of silver. Experience has shown that even 33% is not too great a margin of safety, and while excessive seigniorage must be guarded against, a coinage system which is constantly threatened by small rises in the world price of silver would not add greatly to the desired stability. And it seemed unnecessary to postpone the day when the tael must be withdrawn from circulation or use. We need hardly add that this plan was not put into operation, nor was any real effort to do so made by the Imperial Government.

1903 and

1905-6 In these years came the Imperial Edicts of Kwang Hsu. They proposed a silver standard on the basis of the tael with coinage rights reserved to the Imperial Government. At the existing price of

silver (G\$.55 per ounce) the tael unit would have had a value of G\$.63. Provision was made for subsidiary coins, the old coins to be exchanged for the new according to comparative bullion value plus a seigniorage charge. Severe penalties were established for any persons found guilty of discounting coins. A central mint in Peking was to control all branch mints.

We might expect just such a plan as this from the Chinese Emperor. It attempted a mild unification of the existing coinage system but left untouched the really basic problems such as the changing value of silver, the lack of adequate banking facilities (no mention of a central bank appears in the edicts), the need for a workable monetary system. The plan was all that experts before and since have warned against, for it presented no solution to China's monetary difficulties, but offered only a few minor reforms.

1908 Sheng Hsuan-hwai of the Chinese diplomatic service proposed an ultimate gold standard, but, as an intermediate step, unification on the existing silver basis. His Memorandum is vague concerning the size of the unit desired, but seems to indicate that .72 of the Kuping tael, .900 fine, would be desirable. The new coins were to be issued by the government in payment of debts and accepted for tax payments by the government. Sheng likewise proposed to stabilize the exchange rates by the use of a reserve fund and by definitely limiting the amount of coinage issue. He proposed abolition of the tael, but advocated the coinage of a unit equal to Ch\$.50, the value of the Kuping tael. A central bank, privately owned, but with a government policy board to assist in its control, was a major point of this scheme.

The author of this plan perhaps made more mistakes than any other reformer during this period, yet he was definitely groping for the correct solution to many of China's difficulties. We need not repeat again the arguments against the retention of the tael, directly or indirectly. The amazing portion of this plan is the section dealing with the proposed fund to stabilize the exchanges. Sheng correctly recognized that stability of the exchanges was a highly desirable feature but to recommend the use of a reserve fund to bring this about would, even in an emergency, be

somewhat rash: to recommend its attempted use as a regular policy for China in 1908 can only be termed ignorance of the real situation. For stabilization of the rate of exchange can only be attempted when there exists the full battery of devices and institutions of the modern financial world, such as a strong commercial bank system, a Central Bank, a unified currency, and credit markets of various kinds.

1912-

1914

The Minister of Finance of China and representatives of French, German, British and American banking interests signed a loan agreement on April 15, 1911. Ten million sterling was to be placed at the disposal of the Chinese government, 30% of which was to be for improvements in Manchuria; the remaining 70% was to be utilized in reforming the currency system, provided a suitable plan was agreed upon. After several conferences, it was decided to extend an invitation to Dr. G. Vissering, former president of the Javische Bank, to act as monetary adviser and to recommend a suitable plan for the reform of the Chinese monetary system. But his appointment came on the eve of the Revolution which took place on October 10, 1911. Vissering continued his work for a year and then Dr. E. A. Roest took up the task. Upon the latter's death in 1913 Vissering returned to China under appointment from the new government as Honorary Adviser. His proposals are to be found in two volumes, published in 1912 and 1914 respectively. He proposed a dual currency as a step towards the ultimate adoption of the gold standard. Silver and gold standards were to exist side by side for twenty or thirty years with a unit equal to about one-third of the Kuping tael (about G\$.25 at current silver price). The ratio between silver and gold was set at 21 to 1. The new unit was to be introduced first as a theoretical unit of account, the coins to appear slowly over the transition period. The usual gold exchange standard mechanism was included as well as provision for converting taels into the unit at a fixed rate. The ratio of 21 to 1, Vissering believed, would prevent the melting down of the silver coins.

There seems to be a definite line of development among the various plans presented, although this need not necessarily be so. However, Gerard Vissering, although his plan was far from adequate, did more nearly approximate what we, second guessing after the event, believe would have been the best policy. He displayed the usual weakness for

the tael but was wise enough to see that its value was too high to form an adequate unit. Therefore he made his unit equal to one-third of the Kuping tael and proposed a definite rate of conversion between them. The argument over the question of whether it is best to proceed directly to the gold standard or unify the monetary system first on the silver basis we reserve for consideration until we deal with the Kemmerer Report below. Vissering erred in thinking his ratio of 21 to 1 would be satisfactory, for the war soon raised the price of silver to such a point that his coins would have been melted down.

1918 Tsao Ju-lin, one of China's innumerable generals, proposed the immediate adoption of the gold standard, with reserves accumulated in six cities. The unit recommended was equal to G\$.50. Gold notes were to be issued, redeemable in gold at any reserve city on demand. A date was to be set for the transfer of all obligations, accounts, etc., into the new Chinese dollar. The Bank of China and the Bank of Communications were to act as the fiscal agents of the government and have the sole right to issue paper money.

Mr. Tsao knew, at least, when to take advantage of a golden opportunity. Silver was extremely high in price, but Tsao knew that it would not remain so. Likewise, with gold relatively low in value (also a short run phenomenon) the time was ideal for China to sell her silver and secure enough gold to establish and maintain a gold standard currency. The entire plan seems to indicate that the author was a close student of American banking, for the Federal Reserve System (just being introduced in the U. S.) is written all over the proposed reform. One cannot quarrel with the general outline of the plan. The time for such action was ripe. The action was not taken and China lost an opportunity not only to secure the benefits of the gold standard, but to do so at the least possible cost, socially and economically.

1928 A general Economic Conference on China's monetary situation proposed the gold standard as an ultimate goal but declared that unification on a silver basis should come first. The Conference proposed a silver dollar equal to G\$.42, the average value of the dollars then circulating in China. The old dollars were to be called in and exchanged for new dollars on a one for one basis. Seigniorage fees, etc., were to be used to build up a fund towards the day when it might be expedient to change to the gold standard. The tael was to be abolished and converted into dollars at a fixed rate. A Central Bank with capital subscribed by the public was recommended with provisions for branches similar to the Reserve Banks of the U. S. and the proposal of Tsao Ju-lin in 1918.

One can only suggest at this point that there is little to be gained by delaying the adoption of the gold standard and merely unifying on a silver basis. The problem is discussed in more detail below. The plan of the Economic Conference was admirable in many respects but it did not touch the really vital issues. At best, it can only be damned with faint praise.

The Kemmerer Commission's Report

In 1928 Mr. T. V. Soong, Finance Minister of China, requested Dr. E. W. Kemmerer and a staff of financial experts to study the Chinese monetary system and formulate a program for reform. After months of study and observation, the Commission, on November 11, 1929, submitted to the National Government its currency project with a report in its support.

Articles I and II of the Projected Law establish the gold exchange standard and a new unit, called the sun, of 60.1866 centigrams of fine gold. This gold unit was not to be coined, but was to remain as a theoretical standard. Article III provides for the division of the sun into 100 cents, and of each cent into 10 mills. Article IV grants to the

National Government the exclusive right to coin money.^{3/}

Article V provides for the following weights, compositions, and finenesses for the subsidiary coins.^{4/}

<u>Denomination</u>	<u>Weight</u>	<u>Fine Silver</u>	<u>Fineness</u>	<u>Pure Nickel</u>	<u>Copper 95% Pure</u>
1 sun	20	16.0	.800		
50 cents	10	7.2	.720		
20 cents	4	2.88	.720		
10 cents				4.5	
5 cents				3.5	
1 cent					5.0
$\frac{1}{2}$ cent					3.0
2 mills					1.5

(All weights in grams)

A date was to be set for the adoption of the new standard in each province, since it was not deemed desirable to proclaim one date for the entire country.^{5/} The fund for the maintenance of the gold exchange standard was to be obtained from the following sources:^{6/}

1. seigniorage profits
2. premia from sale of exchange
3. interest on funds abroad
4. tax on reserve of central bank
5. sale of government stock in Bank of China
6. loans for the stabilization of the currency
7. miscellaneous

A National Currency Commission of three men was proposed, with power to effect the reform in the best possible manner and to guide the entire process through all its uneven steps until the task of monetary reform was completed.

The ten cash pieces in use at the time of the report (1929) were to be gradually withdrawn until the rate of 200 equal one sun had been reached, when their value was to be stabilized and the old coins to be redeemed in

3-Kemmerer Report, p. 32

4-Ibid., p. 32

5-Ibid., p. 33

6-Ibid., pp. 34-35

exchange for new coins as fast as the mint could produce them. Eventually all of the non-gold standard coins were to be replaced by the new coins. In the paper money field it was recommended that there be a definite date for the retirement of the notes of each province.^{7/} In other words, the gold standard was to be introduced in completed form, yet slowly enough to allow adjustments to take place with the least amount of friction. The plan was to move forward, province by province, in this manner: a first date would be announced for the circulation of gold standard currency; at least one year later, a debt-adjustment date would be announced, after which all debts must be converted into the sun, rather than the dollar or the tael. At least one year after the introduction of the new currency, but no later than two years after the debt-adjustment date, there would be announced a legal tender date, after which only the gold standard currency would be legal tender. Ample provision for the exchange of the old currency for the gold standard currency was outlined.^{8/}

The sun, with its gold content of 60.1866 centigrams, would have a value of G\$.40, thus making for the following pars of exchange:^{9/}

Sl equals G\$.40 (U. S.)
 Sl equals 1/ 7.7265d. (England)
 Sl equals .8025 yen (Japan)

Such a unit, the Commission reported, would have little disturbing effect on wages or prices since the old silver dollars ranged about the same figure.

All coins were to be fiduciary and maintained at par with gold by

7-Ibid., p. 44

8-Ibid., p. 40

9-Ibid., p. 41

means of unlimited redemption in drafts on gold standard countries. On these drafts a premium would be charged equal to the cost of shipping gold, thus allowing for the use of the gold points although no gold was available.^{10/}

Approaching the problem which has always confronted China--the melting down of coins in response to a rise in the price of silver--the Commission favored a "spread" of 33 $\frac{2}{3}\%$ between the bullion and the face value. Thus only an extreme and extraordinary rise in the price of silver could endanger the existence of China's subsidiary coins.^{11/} To secure the acceptance of these "depreciated" coins the Commission recommended that the government stand ready to redeem or exchange in legal tender money any coin or note presented to it, and, ultimately, stand ready to sell drafts on foreign banks at any time. Until the people became accustomed to this form of currency the redemption fund would be truly the redeemer and indispensable. It would require management that would satisfy the doubts and misconceptions of the people for it would be, itself, the most powerful educative force available. The use of old coppers for a relatively longer period would also contribute to stability and tend to bridge the gap between the old and new currencies as well as prepare the Chinese for the new monetary system.^{12/}

Dr. Kemmerer scoffed at the suggestion that if China were to establish a gold standard a shortage of supply of that metal would immediately present itself. Even if the increased demand for gold should force up its price, why should China sacrifice the advantages of the gold standard

10-Ibid., p. 75

11-Ibid., p. 43

12-Ibid., p. 44

because of the inconvenience it might cause to other nations? Those same nations (especially the U. S., as we shall see below) have shown precious little regard for China's position. After all, when China is on the gold standard, international agreement may be used to settle certain basic questions. It is not a problem that any one nation or group of nations can or should tackle alone.^{13/}

It has also been claimed, the Commission wrote, that the gold standard would cause a rise in the Chinese international price level. There is no basis for such a statement except insofar as the gold standard increases production and thus causes the level of prices to rise in the sense of an upturn in the business cycle. Certainly there can be no logical objection to this.^{14/}

The Commission reported two ways--alternate methods--for reaching the same result; the gold standard. The Indirect plan (used in the Straits Settlements) calls for unification of the currency and then a gradual change from silver to gold as a basis. The Direct plan (used in the Philippine Islands) proceeds directly, as the name implies, to the simultaneous introduction of the gold standard and the necessary monetary reforms. The Commission, after careful consideration, recommended the Direct plan, but with modifications as noted above. They were agreed that the Indirect plan, while advantageous in many respects, carries with it many disadvantages. For example, claimed the Commission, after the currency had been unified under the Indirect plan and the time had come to shift to the gold standard, the existing coins would

13-Ibid., p. 75

14-Ibid., p. 77

have to be suddenly raised in value. This would lead to two evils: the seigniorage would fall to the holders of the coins whereas under the Direct plan the government receives this seigniorage and utilizes it in the establishment of a redemption fund. More dangerous, however, is the fact that raising the value of the coins would lead to contraction of the currency and serious deflation, bringing harm to everyone in general, and to exporters and laborers in particular.^{15/}

In general we can but acknowledge that the Kemmerer Report is a careful, scientific study of an extremely complicated and intricate situation. The recommendations contained therein show that consideration was given to a host of related problems in such a way as to make it perhaps the only logical and clear-cut proposal that could be made in 1929. On one major point alone was there disagreement when the Report was published: the use of the Direct rather than the Indirect plan. E. Kann of the Shanghai Bank and many other authorities were inclined to disagree with the Commission and to favor unification on a silver basis. Since the method and scope of reform depended on the answer given to this question we might have expected a lively debate among Chinese and foreign business interests and government offices centering around the Kemmerer recommendations. Sadly enough, however, before any action or even debating could take place, the grip of the world-wide depression and the associated decline in the world price of silver delayed all consideration of any but the most immediate problems. Since 1929 much has happened that affects the recommendations of the Kemmerer Commission, so that even if the Report was the answer to the original problem, the problem itself

15-Ibid., p. 47

has meanwhile--as it so often does in the field of social science--
undergone considerable changes that necessitate further modifications
in the solution previously reached. Let us turn, now, to a consider-
ation of the events and conditions in Chinese monetary history since
the fateful year 1929.^{16/}

16--The reader may well examine, at this point, the writer's proposal for
reform submitted as Appendix A of this essay.

Chapter V China under Depreciated Silver

When we turn to a consideration of the trend of events in Chinese monetary affairs from 1929 until the present it is interesting to note at the outset that during the period under consideration there was at no time a condition which might be called a stable equilibrium in the gold value of silver. After the most alarming slump in value in its history, a slump which indeed taxed the energies of the Chinese government, came the period (1932-35) when the price of silver rose to heights which changed (perhaps forever) the character of the Chinese monetary system. The events themselves furnish additional proof--if such be needed--of the helplessness of a single silver-standard nation in its efforts to provide security against such price movements, for by its very nature silver is opposed to such stability in price. The price of silver fluctuates as all prices fluctuate, but to the general set of price-fixing factors must be added, in the case of silver, the special actions of men and governments which can, to a great extent, distort the fluctuations caused by the play of normal forces. We may, indeed, well argue that these extra forces are, for silver, "normal", and therefore explain the unstable nature of the white metal.

As demonstrated elsewhere in this essay (pp. 30-38) neither a high nor a low price of silver is necessarily or inherently bad for China. What is bad, is a price of silver that is constantly changing--rising or falling--as the result of forces over which the Chinese have little control.

Between 1928 and 1929 the price of silver continued the downward movement which had begun in 1926 and had only been interrupted by a slight rise in 1928. The average price of silver in 1925 was G\$.6907

per ounce; in 1932 that average had fallen to G\$.2830. Sheltered from the world depression by this depreciation of silver China experienced a mild boom in the years 1930 and 1931 when the rest of the world was experiencing deflation. But while this boom reached dimensions of great magnitude in some parts of China--especially in the important commercial cities such as Shanghai--it was by no means as general or as beneficial as many persons, in China and elsewhere, have assumed. It is true that many Chinese were led to believe that the boom represented the growth of China's economic system and others argued that the situation proved that all those who favored the abandonment of silver in favor of gold were in error. In the United States, China's condition became a key argument by those who still preached the villainy of gold and accepted the principles of William Jennings Bryan. Obviously, however, it was only the fact that the world was on gold and China was on silver that made such a situation possible. Further events demonstrated that even the temporary advantages of retaining silver were not beneficial to China in the long run.^{1/}

At the same time that business seemed to be improving, speculation increasing, there were many who decried the false prosperity. A true picture of this period is given by the survey (presented below) of the ideas and opinions advanced by leading Chinese individuals and organizations. Early in 1930 the price of silver began to slump even more rapidly. On January 11, 1930, Mexican silver mines began to lay off men because of the rapidly diminishing demand for silver for monetary purposes in China. A record low was recorded on that day (January 11), and this

1-A more complete statistical survey of the situation is given in the Appendix B, below, Tables 1-13, pp. 151-168.

low price of 45 3/8¢ per ounce was believed to reflect the holdings of a large speculative pool in China.^{2/} Since the average price of silver in 1929 had been G\$.533 per ounce the fall in price had immediate repercussions.

In the ordinary import transaction three parties are involved: the dealer, or real importer, who must pay for the goods and distribute them, and who therefore needs credit, the importing firm which secures the order from the dealer and buys the required goods on the world market, and the bank which finances the transaction and which owns the goods while in transit, and will, if things move nicely, receive a commission plus interest on each shipment. But in 1929 the rates were not moving nicely. Between January, 1929, and January, 1930, the exchange rate fell from G\$.63625 to G\$.4925. After this gold value of imports was changed to taels the price was prohibitive. Goods piled up, orders declined, banks were forced to carry non-liquid debts, and general commercial and financial contraction resulted. Silver, which sold on the New York market for G\$.62 in 1926 and for G\$.58 in 1928, fell to G\$.383 in 1930, the figure for December of that year being decidedly below the average.^{3/}

Dr. H. H. Kung of the Chinese Ministry pointed out that the slump in silver had already (January 18, 1930) cost the government some ten million dollars and must be stopped.^{4/} All governmental agencies were ordered to cope with the situation to the fullest extent, but Mr. T. V. Soong, Finance Minister, was unwilling to interfere with "the free

2-Chinese Economic Bulletin, Vol. 16, No. 2, January 11, 1930, p. 24

3-Ibid., p. 36

4-Ibid., p. 36

market of silver".^{5/} But the free market of which Soong spoke no longer existed, for one of the major reasons for the decline in the price of silver was the determined dumping of silver on the Chinese market by India and other regions which, being on the gold standard, were attempting to rid themselves of unnecessary supplies of the white metal. Here is further evidence, if any more be required, of the foolhardiness of attempting to maintain a silver standard in the face of demonetization of the white metal by the rest of the world. Soong argued that the "best stabilization of the value of silver can be achieved by the restoration of peace and order and the free movement of our products throughout the country".^{6/} This purely nationalistic view was not acceptable. True, the peace and order of which Soong spoke were urgently required, and would, by the increase of trade and the consequent increased demand for circulating media, have tended to improve the price of silver. But directly these things have little to do with the price of silver, which is an international problem. And in the light of the above statement how could Soong justify the retention by his government of countless internal restrictions to the very trade he desired to be widened and freed?

This nationalist treatment of the silver question was the point of view of the National Government, more or less, until recently, and there are many who think that the cry of "political stability first" was too often used to prevent the introduction of necessary reforms. Gratuitous advice it may be, but, in the writer's opinion, the National

5-Ibid., p. 36

6-Ibid., p. 36

Government would have gained far more by first cleaning up the areas under its jurisdiction. If the job was done well enough the other provinces, lost at the time, would have found it more to their advantage to seek union with the National Government.

Mr. Ma Ying-chu, government economist, recommended an embargo on silver alongwith further restraint on speculation.^{7/} It is indeed strange to note in all the journals that during this period of silver slump everyone protested against wild speculation. Resolutions were passed, yet the National Government brought forward no constructive control but merely condemned the practices. On January 15, 1930, Soong and Kung met together to consider what possible steps could be taken to alleviate the situation.^{8/} Chiang Kai-shek announced that "speculation and adherence to the silver standard, plus lack of monetary unity, is the cause of the distress."^{9/} For perhaps the first time in his period of rule the communists were not held responsible for national distress. But Chiang did not go beyond the announcement; nothing was done about it.

The Bankers of Shanghai met together and after some deliberation presented a five-point program to the National Government, as follows:^{10/}

1. that the Central Government mint be given the sole right of coinage;
2. that a uniform yuan dollar be adopted;
3. that all import and export duties should be made payable in the new yuan dollar to facilitate the abolition of the tael;
4. that a definite and fixed date for the abolition of the tael be set; and
5. that a new system of subsidiary coins be established.

These proposals would have meant a close approximation of a true silver

7-Ibid., p. 38

8-Ibid., Vol. 16, No. 4, January 25, 1930, p. 50

9-Ibid., p. 50

10-Ibid., p. 51

standard and while they would not have relieved the major cause of the silver slump they would have meant the introduction of a great degree of stability and permanence in the currency system. But Soong and Kung, as a result of their conference, introduced a new scheme. Soong announced the adoption of a Gold Customs Unit, a theoretical weight and fineness of gold, in which all import duties would thenceforth be collected.^{11/} This unit was equal in gold content to the Sun proposed by Dr. Kemmerer's Commission and was, therefore, valued at G\$.40. Duties levied in haikwan taels were to be converted as follows: t1.1 equals $1\frac{1}{2}$ C.G.U. up to March 15, 1930; from then on t1.1 equals $1\frac{3}{4}$ C.G.U. This change, of course, tended to stop all losses on gold debt payments and made the tariff of 5% "effective", for although the tariff had been 5% for some time, the gold value of the customs receipts naturally varied with the gold price of silver, so that the tariff was usually considerably less than 5% of the gold value of imported goods. This constructive move on the part of the government helped to relieve the drain on the national treasury but in no way helped to alleviate the effects of the silver slump on other aspects of Chinese economic life.

Repeated resolutions demanding the removal of internal trade restrictions resulted in the abolition of some likin taxes, effective October 30, 1930. Here was a feeble step, but one in the right direction--one which at least was consistent with the oft-repeated policy of the National Government to eliminate internal restrictions to trade. The

11-Following three paragraphs based on:

Chinese Economic Bulletin, Vol. 16, No. 5, February 1, 1930, pp. 60-62; No. 8, February 22, 1930, pp. 100-101; and Chinese Economic Journal, Vol. VI, No. 3, March, 1930, pp. 250-269

policy was renewed in the general program for 1931-1934 with some success.

Likewise, in response to the appeals of bankers and business men, the government placed a prohibition on the export of silver. But this was really unnecessary since there was little danger of losing silver to the world at the existing price. But these same bankers and business men objected to the curbing of gold bar speculation, arguing that such a policy would weaken their hedging activities. In the light of our previous discussion of this point this objection cannot be considered valid.

Two conferences were called by the government to which industry and finance were invited to send delegates.^{12/} Dr. Kung was indisposed and in his absence his secretary read his paper in which he declared that the gold standard was inevitable but that other reforms must come first. Nevertheless no general action was taken. After reading page after page of discussion of the same issues, with the same pat phrases being used over and over again, one begins to wonder just what the policy of the National Government really was. The disparity between stated aims and actual performances was too great to be waved aside in the usual manner by saying that things must go slowly because of tradition and custom. Mr. Calder-Marshall rightly called the government to task for dissipating

12-Following three paragraphs based on:

Hsia, C. L., and Hope, Richard I., "The Silver Slump: Its Causes and Remedies", Chinese Economic Journal, Vol. VI, No. 3, March 1930, pp. 250-269

Mr. S. U. Zau, Shanghai Director of the Finance Ministry, in opening the first conference, said: "Business has been thrown out of gear as a result of the silver slump. Its disastrous repercussions on trade are bound to be prolonged in duration and calamitous in character."

its energies over too wide a field. More action and reform in the areas where political power had already been achieved, he said, would be more effective. If prosperity returned, so would the "lost provinces", he drily remarked at the close of the conference.

At the second conference Mr. Jabin Hsu protested against the action of the Indian and French Indo-Chinese Governments in dumping silver on the Chinese market and laid the entire blame for the silver slump upon this situation. Mr. Arnhold added that the prohibition of silver imports would not help China, but merely cause a further collapse in the world price of silver--a point well taken but in contrast to the actual policy adopted by the National Government. The elimination of internal trade restrictions to stimulate exports, and other measures to increase trade and the demand for silver as well as to turn the balance of trade to China's favor, added Arnhold, should be the policies adopted.

Whereupon Mr. Tsuchiya suggested that silver not be sold at a price below $21\frac{1}{2}$ pence sterling (about G\$.43) and that the export of gold be forbidden. To achieve these two points he suggested the League of Nations as the proper organization to consider the first, and the National Government to consider the second. Such a proposal would mean that the governments and/or the central banks would so regulate their purchases of silver that a price equal to or above the figure quoted above would be maintained. In effect this means that governments must stand ready to purchase any and all silver offered at G\$.43. It is doubtful if such a plan could have been effected, or would be effective. Valorization schemes have never been noted for success. Other suggestions included requiring the banks to carry a 60% reserve in silver, thus creating a demand for about taels

120,000,000 of silver which would then be removed from the glutted market. In general the conference concluded by recommending:

1. that peace is necessary before anything else can be done;
2. that no restrictions be placed on the import of silver;
3. that international cooperation through the League of Nations was essential to solve the silver problem; and
4. that an embargo on the export of gold was desirable.

In contrast to these luke-warm proposals for reform, a Chinese banker, name unknown, writing in the Chinese Economic Journal, stated emphatically that the tael must be eliminated at once, that such elimination was the first logical step in the direction of monetary reform.^{13/} The National Government, as we shall see below, eventually reached the same conclusion.

But despite the many complaints and protest meetings, the price of silver continued to decline. In 1931 the average price of silver at New York was G\$.29, and even in 1932 a slight decline was evident, the price of silver reaching an all-time low with a yearly average of G\$.283. During this time the exchange value of the Chinese dollar fell from G\$.415080 in 1929 to G\$.21487 in 1932. Perhaps a solution for China's monetary problems might have been achieved at that time, given silver stability, but in 1931, as we have pointed out above, new forces appeared which reversed the trend in the price of silver and carried it up and beyond the price which existed before the drastic slump of 1928-1931.

13-Anonymous, "A Chinese Banker's View of China's Economic Situation", Chinese Economic Journal, Vol. VI, No. 6, June, 1930, p. 645

Chapter VI Appreciating Silver: 1932-1935

The false prosperity and the cushion against the world depression provided for China by its adherence to a silver standard while the rest of the world was experiencing deflation on the gold standard came suddenly to an end in September, 1931, when the pound sterling and its followers were divorced from gold. In terms of pounds, yen, and other non-gold currencies the Chinese dollar began to rise. In April, 1933, when the United States abandoned gold the Yuan was also forced upwards in relation to the dollar. Still there was no great danger to the Chinese economy from these events; the price of silver in 1933 was but 35¢ per ounce, (as compared to 28.3¢ per ounce in 1932) and still below the relatively low figure of 38.3¢ per ounce in 1930. It remained for another series of events to carry the price of silver to such levels that serious harm to the Chinese Economy was inevitable.

The Preparatory Commission experts of the World Economic Conference which had been called for the summer of 1933 dealt with three suggestions regarding silver as follows; bi-metallism was impossible under existing world conditions, if at all; silver as metallic reserve for banks of issue was not feasible since the price of silver was too erratic; and, although the increased use of silver for subsidiary currency would add to the demand for silver, too much could not be expected.^{1/}

1-Bratter, Herbert M., Should We Turn to Silver?, pp. 18-19

The Commission added: "From the point of commercial relations with silver-using countries, particularly China, trade interests would best be served, not by a rise in the price of silver as such, but by a rise in the general level of commodity prices. Any action which would tend to raise that level and in due course achieve its stabilization may be expected to have a favorable effect on the price of silver and would, on general grounds, be welcome."

On June 12, 1933, the World Economic Conference convened at London. At the urgent request of the government of the United States silver had been included on the agenda and, as Mr. Herbert M. Bratter reminds us, it was the only item on which an agreement was reached. Even then, it was not the Conference which reached the agreement, for only eight of the sixty-six states represented showed any interest at all in the silver question. But the three countries holding large stocks of silver (China, Spain, and India) and the five countries engaged in the production of silver (United States, Canada, Mexico, Peru, and Australia) met outside the regular conference sessions and drew up the London Silver Agreement on July 22, 1933. In the preamble it is declared that the purpose of the agreement is to stabilize the price of silver. The articles provide:^{2/}

1. that the Agreement must be ratified by all the signatory nations by April 1, 1934;
2. that for the four years following that date the five producing regions would refrain from selling silver abroad and would purchase for domestic monetary use, 140,000,000 ounces from their mines;
3. that during the same period India would limit her sales of demonetized silver to a total of 140,000,000 fine ounces;
4. that Spain would limit her sales to a total of 20,000,000 ounces; and
5. that China would refrain from selling silver on the open market.

One provision was made, however, whereby India could sell silver outside of her quota to any country which wanted it in order to pay war debts to the United States. (We still had illusions then, it seems.)

The moving spirit of this agreement was Senator Key Pittman, from silver-producing Nevada. Certainly he earned his re-election from that state. Closer examination of the provisions of the Agreement show very clearly that no one really thought of giving anything--although much may

²⁻Ibid., p. 22

have been given unknowingly. British India's quota was greater even than her annual sale of silver in the years of 1928-1929, when silver was high in price; the Spanish quota was an even greater surprise since Spain had not been selling silver on the open market for some time; the Chinese Government was not interested in selling silver and had never done so. The silver world received the Agreement with jeers.^{3/}

But even the North China Daily News reckoned without the United States Government and the United States Senate. There is considerable reason for believing that the insistence of the U. S. on the inclusion of silver on the agenda of the Conference and the predominant part played by the U. S. in forming the provisions of the Agreement was a veiled attempt on the part of the United States to lay the foundation for her ensuing silver policy. For the U. S. was already a hot-bed of silver remonetization discussion fomented by the silver-producers' lobby and the silver-state senators, of whom Pittman was the leader. By this Agreement the U. S. may have hoped to close the American market to foreign sellers of silver so that the rise in price to follow would result in

3-The following quotation from the North China Daily News was typical: "No one will grudge Mr. Pittman his happiness for the simple reason that, if he is pleased with the agreement, then, like the friends of Mr. Peter Magnus, he is not difficult to please.... Mr. Pittman and his friends, with their superior flair for publicity, were able to make much cry. Little wool have they collected but they profess to be happy. In leaving them to that blissful condition it is only necessary to say that they have done very little harm and conceivably have done some service to the world. They have shown that the London Conference is an even bigger failure than it was at first expected. They have expounded the limit of the successes of sheer publicity or 'ballyhoo' in disposing of awkward economic facts. The difference between what they have actually achieved and what they promised for their nostrums is a point on which tactfulness prefers to remain silent. The London Conference's ewe lamb must surely be allowed to display its engaging charms without captious blemish or spot." Ibid., p. 23 (footnote)

benefit to American silver producers only, rather than in a benefit to be shared by all silver producers. There was no danger, Mr. Pittman could have argued, that the high price would attract silver from China since she was forbidden to sell and would make every effort to retain her monetary stocks. India and Spain were limited by the Agreement to silver sales equal to India's 1929 sales and so could not pump extra silver on the market, while the other producing regions were bound to buy their own production. The way, therefore, was open for the United States to launch its silver program with the benefits assured to the domestic silver interests. Perhaps the government and Pittman did not plan the whole affair so neatly as that, but certainly it was immediately seen just how the Agreement would affect the silver program for which domestic interests had been clamoring.

One might say that it should have been apparent to the keen Chinese observer that the advent of the Roosevelt administration meant that something would be done about silver. The price of silver in 1933 had risen to 35¢ per ounce and although still far from the 1928 price, the Chinese government realized, with the Preparatory Commission quoted above, that there was danger already that the price of silver might be hoisted to such heights that the entire monetary structure of China would be threatened.^{4/} China, therefore, ratified the Silver Agreement on March 21, 1934,

4-Said Dr. Kung: "Last February, (1934) when ratification of the agreement was under consideration, I informally called to the attention of the American Government China's vital interest in measures affecting the value of silver, pointing out that any action resulting in a rise of China's currency out of relation to the prices of world commodities would have deflationary effects in China, and would further decrease her already reduced exports and so impair her ability to purchase goods from abroad. I also pointed out at that time that such a rise of China's vital exchange would probably increase the tendency towards heavy silver exports as a necessary means of settling large adverse balances of

but made the following reservation which reiterated her fears of American silver policy:^{5/}

"In ratifying this Agreement, the National Government of China declares that as silver is the basic monetary standard of China, the National Government will consider itself at liberty to take whatever action it may deem appropriate, if, in its opinion, changes in the relative values of gold and silver adversely affect the economic condition of the Chinese people, contrary to the spirit of stabilizing the price of silver as embodied in this Agreement."

In the end the fears of the Chinese Government were realized. From a period of depressed silver prices there came a rapid and violent rise in the price of silver until in December, 1934, the price stood at 54.390¢ per ounce as compared with 28¢ in 1932--and the price was still rising. Buffeted by alternate winds from either direction it is no wonder that the average Chinese has lost all sense of monetary direction.

The Silver Purchase Act of the United States authorized the government to buy silver up to 25% of the total monetary reserves of the nation or until the price of silver had reached the phenomenal figure of \$1.29 per ounce. Silver was nationalized and the government set a price at which silver would be purchased. Immediately there was a sympathetic rise in the world price. The entire chain of events was repeated again and again, the price of silver being forced upward

4-(continued) international payments, which even then were beginning to cause concern, and expressed hope that in view of China's vital interests, the Government of China would be consulted in advance if measures concerning silver that might materially affect China's currency and exchange were in fact being contemplated."

Kung, H. H., "National Finance", The China Quarterly, Vol. I, No. 1, September, 1935, pp. 150-51

5-Ibid., p. 151

each time. To purchase the amount of silver required by the law would mean that 1,000,000 of the required 1,300,000 ounces would have to come from abroad although this amount need not be purchased if the price of silver reaches \$1.29, which latter alternative was, of course, the desire of the silver interests.

But alas for the desires of the silver producers of the United States! Silver from other countries began to gravitate toward the benefactor who offered high prices. Alas, too, in less humorous vein, for the Chinese economy. The silver exodus began.

6/

Movement of Gold and Silver to and from China

(in millions of yuan dollars)
(-) indicates net export

<u>Year</u>	<u>Net Gold Movements</u>	<u>Net Silver Movements</u>	<u>Total Net Movements</u>
1928	9.3	164.1	173.4
1929	-3.1	163.9	160.8
1930	-25.5	103.2	77.7
1931	-49.3	69.8	20.5
1932	-110.7	-11.6	-122.3
1933	-66.9	-14.2	-81.1
1934	-52.0	-260.0	-312.0

From this table we see that China had a favorable balance of payments in 1928 and 1929. The change began in 1930 and by 1932 the balance of payments was definitely adverse. But even so this condition was as nothing compared to the adversity caused by the American silver policy. In the five months period June-November, 1934, China lost silver to the value of 167 million yuan--yet in the previous six months the loss was

6-Monthly Letter, National City Bank, November, 1934, p. 166; Monthly Returns of Trade, National Government of China, December Issues, 1928-1934

only 31 million.

We must remember what such a loss means to China, for she suffers a double reaction. Her loss of silver, in one respect, has the normal effect of a depletion of the metal used as reserve in any country--a loss of reserves and a consequent contraction of credit. This can be offset, normally, by other factors, so that the total means of payment need not necessarily decrease. In China, however, not only are the reserves held in silver, but silver itself is the most common medium of exchange. Consequently a loss of silver immediately reduces the available means of payment and the results are falling prices, contraction of credit, and all the other manifestations of deflation. Yet this is exactly the course of events in China which the policy of the United States precipitated.

In August, when the silver drain began to manifest itself in earnest, a note from China to the American Government was sent pointing out that the stability of the price of silver and the economy of China were menaced by the Silver Purchase Act of June 19, 1934. On September 24 the Chinese Minister at Washington presented a note to the government of the United States, calling attention to the profound results of the American Silver policy and pointing out the necessity for joint action in stabilizing the price of silver under the general sections of the London Agreement. The note closed by saying: ^{7/}

"Since the American government desires an increased proportion of silver in its monetary reserve, the National Government desires to ascertain in principle whether the American government is willing to exchange with the Chinese Government gold for silver."

7-Kung, op. cit., p. 151; National City Bank Letter, op. cit., p. 167. Quarterly, Vol. I, No. 1, September 1935, p. 167

On October 2, Dr. Kung sent a subsequent note to the United States, emphasizing the gravity of the situation. Mr. Cordell Hull, Secretary of State, replied that the Administration did not really desire to injure China but that the current silver policy had been made mandatory upon the President by Congress. As far as the proposed exchange was concerned, Mr. Hull pointed out that both gold and silver were open to purchase by all who cared to possess them, and that exchange was therefore unnecessary.^{8/} He might have added that exchange would have lowered the bonus which the American government, in its munificence, had voted to domestic silver producers. China, seeing that the "Good Neighbor" policy did not apply to her turned to other means to attempt to stave off the wrecking of her economy.

Silver had been rising in price much faster than the rise in China's exchange so that the bullion value of the Chinese dollar was greater than the face value. The rates were deficient as compared to the theoretical parity of the Chinese dollar by the following amounts:^{9/}

	<u>Per cent of deficiency</u>
July average	4.13
August average	5.08
September average	4.31
October 1-9 average	4.98
October 10 (holiday)	
October 11	5.31
October 12	8.88
October 13	9.72

That the deficiencies of October 12-13 imposed a terrific strain on the currency is obvious. As a desperate attempt to save their silver and so

8-Kung, op. cit., p. 151; National City Bank Letter, op. cit., pp. 166-67
 9-Kung, op. cit., pp. 139, 151

remain on a metallic base the Chinese government, on October 14, placed further levies on the export of silver. There had previously existed an export tax of $2\frac{1}{2}\%$ ad valorem on the exportation of silver sycee, bars, ingots, slabs, and silver in mass. This served to equalize the value of all silver in China, as $2\frac{1}{4}\%$ represented the cost of converting bars into coined silver dollars. The new export levy was $7\frac{3}{4}\%$ on silver dollars and mint bars and 10% on all other forms of silver. Since it was feared, and rightly so, that this would not be great enough, an equalization fee was also established to prevent any discrepancy between the theoretical parity and the actual exchange rate (including the export tax).^{10/} Actually China had abandoned the silver standard by her protective action; officially she adhered to the silver standard until late in the year 1935.

As a result of this theoretical restriction in supply the price of silver rose to $55\frac{1}{4}\%$ per ounce with no indication as yet that it would stop before reaching the price set by the United States as its goal--\$1.29. While silver was low in value, in 1929 and 1930 (before the slump to abnormal depths in the latter year) there was a commodity price level rise and a pseudo-prosperous situation, generally speaking, in China. As silver rose in price, other prices fell, devaluation set in, and the pressure on the internal prices became increasingly severe. China, after all, produces little silver, so that there were not even miners (as in the U. S.) to profit from this rise. But even Mexico, a silver producing region, which supplies much silver to China, protested that the rise was so great that she had lost a significant portion of

10-Ibid., p. 152

her circulating coins.

During the latter half of 1934, Dr. Kung reports, interest rates charged by native banks rose from 6% to 25% per annum. So scarce did money become that foreign exchange was reported sold for cash at a premium over forward delivery amounting to 30% per annum. "The value of government and industrial securities and real estate has shrunk by 10 to 15%" between July, 1934 and January, 1935. Foreign trade fell off alarmingly, the second half of 1934 being 18% below the similar ^{11/} period for 1933.

Yet it will be recalled that many persons, in newspapers, over the radio, and in public addresses, made much of what the United States silver program would do to increase the ability of countries such as China to buy abroad. Americans were deluded into believing that over-night a poor nation could become a nation of 400,000,000 cash customers. ^{12/}

The only weapon at China's disposal was the tax--a weapon of national policy only. Yet the London Silver Agreement, in whose name China

11-Ibid., p. 152

12-Perhaps the best refutation of this colossal hoax was delivered by Mr. Li Ming, Chairman of the Bank of China and of the Chekiang Industrial Bank, who said:

"The theory that by raising the price of silver, China would be able to buy more in America or America would be able to sell more in China is not economically sound. The effect, if any, would be very short-lived, as China could not afford to pay for American imports of commodities with exports of silver because she needs all the silver she has for her medium of exchange.

"America's purchasing power is not measured by the gold you possess, but is measured by the productivity of your national wealth. China, like every other country, pays for her imports chiefly with her exports. The silver in her possession, no matter how big that amount may be, does not help much in her purchases abroad. She will have to depend upon her exports and her exports alone."

Surely the hypocrisy, self-interest, and ignorance responsible for these fallacious "theories" stands condemned with them.

National City Bank Letter, op. cit., p. 168

appealed to the United States, contained the promise of international cooperation in matters of silver rehabilitation. It was not the first time, however, that the American Administration wrecked an international economic conference and thereby forced increased economic nationalism upon other nations.

In December, 1934, the following industries in China reported decreases in the volume of production as compared with the period immediately preceding the American silver program:

	<u>Per cent decrease</u>
Weaving and spinning	25%
Hatmaking	30%
Silk filatures	80%
Dyestuffs	40%
Printing	45%
Painting	40%
Electrical appliances	45%
Ironwork and glassware	50%
Rubber goods	35%

Another effect of the rise in the price of silver has been the rise in China's barter terms of trade since the increased value of Chinese currency has made China a "dear" place to buy and an excellent market for the goods of other countries. This has meant even greater exports of silver and/or gold in order to meet international obligations. Increased tariff duties on many commodities resulted, and many more increases may be expected. But such a turn of events means that sooner or later international trade, as far as China is concerned, will disappear, and with it will disappear the mythical "advantages" of a high silver price of which the "Detroit Economist

13-National City Bank Letter, January 1935, p. 6

of the Air" has spoken so much and with so little truth.

Increased difficulty for China has appeared with the tremendous increase in smuggling which has taken place. Smuggling has indeed become a profitable business and estimates of the value of specie smuggled out of China are staggering in proportion to the recorded exports.^{14/} And with the imposition of the export tax on silver the same thing has taken place with that metal--to an even greater extent, we may assume, since the premium to be gained is much greater. The Chinese government has recently outfitted a coast fleet of some sort in an attempt to "discourage" smuggling.^{15/} But when we recall the success of the Coast Guard of the United States in enforcing the prohibition of intoxicating beverages, and also examine the long and ragged coast-line of China, we may be forgiven for not taking too seriously the efforts of this new division of the Chinese Navy. China's alternatives upon the failure of the export tax to bring relief (and few expected such relief) were as follows: she could attempt to adopt the gold standard, she could devalue her currency (but the monetary stocks were held by banks and individuals, not by the government), or she could abandon the silver standard for an

14-Sir Arthur Salter wrote: "Since May, 1930, when the ban on gold exports was adopted, it is safe to say that at least as much gold has been smuggled out as has been officially exported. That is to say, instead of an export in the two years 1931 and 1932 of \$176,000,000, the real export was probably well over \$300,000,000." National City Bank Letter, November, 1934, pp. 168-69

15-Kung, op. cit., p. 140

inconvertible paper standard. Her monetary position in January, 1936,
^{16/}
 is shown by the following table:

Shanghai Monetary Silver Stocks

(in thousands of ounces)

1934, May	447,280
June	446,220
July	426,420
August	381,840
September	348,460
October	321,360
November	283,000
December (15)	267,000

Thus we have observed the cruel impact of the U. S. silver policy on the Chinese economy. Chinese nationalism has been further promoted and to this extent recovery in world trade, as far as China is concerned, is made more difficult, if not impossible. The question arises, then: Had the United States the "right" to do this? Yes, we did have a right to carry out our policies, but we had also a duty to fulfill the obligations of the London Silver Agreement which stated "that agreement be sought with a view to mitigating the fluctuations in the price of silver." And we had the further duty, self-imposed, of maintaining the Good Neighbor Policy. We neither asked the opinion of other nations when considering our silver policy nor did we accept their warnings or their pleas. China signed the London Agreement precisely because she wanted to protect herself against such action as the United States inaugurated. In his proclamation of December 31, 1933, President Roosevelt said he wanted to "augment the purchasing power of peoples in silver-using countries." In the light of succeeding events, those silver-using

16-National City Bank Letter, January, 1935, p. 6

people under consideration would have much preferred, themselves, that Mr. Roosevelt had not concerned himself about the position of their purchasing power. They would like to have a little of it left.

Bound by these solemn pledges, did we still have the right to bring about such wide fluctuations in the value of silver, with attendant poverty and distress to those whose economic life was thus upset? We cannot plead ignorance of the possible results of our action. China protested before and after that action that its result would be, and was, what it has been. And even apart from ethical considerations, what we have done is nothing more or less than bad business, for we have made commercial enemies in China.

China was defenseless against this policy. Devaluation could not solve the problem for the same conditions would still exist and the same chain of events would be repeated. So long as the United States continued its silver policy--and, in the early months of 1935 there was every indication that it would continue to follow that policy--China, we repeat, was defenseless.

Minor Reforms

During this period several monetary reforms of a minor nature were introduced. Although internal trade was yet far from free, several important steps were made in that direction. In February, 1933, the import duties on wheat, rice, and paddy were abolished, and later in the same year the export of these cereals allowed without payment of an export tax.^{17/} The revenue system as a whole was modernized, at least

17-Kung, op. cit., pp. 139-40

theoretically, and, as indicative of future possibilities, the debt-arrears on the 1908 French loan were met during 1934. Despite the multiplicity of taxes, total revenue in 1932-33 was only 559 million yuan dollars while expenses increased to 645 million yuan dollars, necessitating loans totaling 113 million dollars. Of course it must be understood that customs receipts fell off sharply during this year as well as in the following year when total receipts were increased to 622 million dollars. Expenditures increased to 769 million dollars, making loans of 180 million dollars necessary. Below are shown the chief items of expense and income for 1932-33 and 1933-34:^{18/}

Expenses and Receipts of the National Government of China
1932-1933

(in millions of yuan dollars)

<u>Receipts</u>		<u>Payments</u>	
Customs	326	Civil expenses	78
Salt taxes	158	Military expenses	321
Consolidated taxes	80	Indemnity service	41
Other receipts	50	Loan service	170
		Cost of collection	55
		Other expenses	35
Total receipts	614	Total payments	700

Expenses and Receipts of the National Government of China
1933-1934

(in millions of yuan dollars)

<u>Receipts</u>		<u>Payments</u>	
Customs	352	Civil expenses	99
Salt taxes	177	Military expenses	373
Consolidated taxes	105	Indemnity service	42
Other receipts	55	Loan service	203
		Cost of collection	68
		Other payments	52
Total receipts	689	Total payments	837

18-Ibid., pp. 133-39

We observe, therefore, that the main items of both income and expense are not different from those we examined for the years 1928-30. Military expenses still dominated the Chinese budget, amounting to over 45% of total expenses; the cost of collection was still too high, nearly 10%; and an insufficient portion of the revenue was expended upon the institutions of civil government. Expenses have consistently outrun income, but the slight increase in this deficit in 1932-1934 over 1928-1932 was not necessarily ominous. The Chinese market for bonds, both governmental and industrial, held up remarkably well during these trying years.

After many fruitless years of effort to remove it, after decades of unofficial rule and tyranny, the "abdication" of the tael was announced in the Spring of 1933. As a matter of fact, it had been slowly abolishing itself since banks were carrying increasing proportions of their silver reserves in bar silver rather than in taels, and tael-prices were everywhere being discouraged and abandoned by business men. Nevertheless it was important officially to abolish the tael as well as remove it as the unit in which export taxes were paid and export statistics listed. To replace the dishonored tael the National Government promulgated, on March 8, 1933, the Standard Silver Coinage Law. This law provided for the coinage of a uniform dollar, known as the yuan, with a gross weight of 26.6971 grams of silver .890 fine, or, in other words, 23.493448 grams of fine silver. Further orders of the Ministry of Finance decreed that:

19/
that:
"Notice is hereby given that on and after April 6, 1933, all public

and private financial transactions are to be made in terms of silver dollars and not in taels.

"All public and private obligations in Shanghai entered into in terms of taels and dated before April 6 shall be payable in dollars at the fixed rate of taels 71.5 to \$100. All payments and receipts in taels in ports other than Shanghai shall first be converted into Shanghai taels at the exchange rate of April 15 and then into silver dollars at the fixed rate of 71.5.20/

"All business contracts, drafts, cheques, and other documents for receipts or payments made on and after April 6 shall be made in silver dollars, and those made in taels shall be considered invalid.

"Those holding silver sycee may either present them to the Central Mint for coinage into silver dollars or hand them over to the three authorized banks, the Central Bank of China, The Bank of China, and the Bank of Communications, for exchange into silver dollars."

Up to December, 1934, the mint, according to Dr. Kung, made one million silver dollars, and silver bars to about half that value. It was expected that the Mint would be able to transform all sycee and American bars into yuan and Chinese bars within a few months.^{21/} Of course, the silver policy of the United States made the Mint's task much easier by causing the removal of a great deal of silver in bulk form, but we doubt whether the Chinese authorities appreciated this help.

By this law China was placed on a rough silver standard, a position which, albeit of dubious honor and low fame, she had never before achieved. But the fundamental problems of monetary reform still confronted China. As yet no attempt had been made to strike the double blow to achieve unification of the entire currency and the establishment of a universal

20-The legal parities were finally fixed at:

.715 Shanghai tael = 1 yuan dollar
 .670 Tientsin tael = 1 yuan dollar
 .691 Hankow tael = 1 yuan dollar
 .642 Haikwan tael = 1 yuan dollar

21-Kung, op. cit., p. 50

standard of value. The year 1935 cast its shadow over China before this attempt was made.

1935: A Year of Climax

The first six months of 1935 were indeed trying for the Chinese government and economy. The continued rise in the price of silver, with the subsequent rise in the foreign value of the yuan and depressed internal prices presented a series of problems which could not be solved by merely raising the equalization fee. In effect, this charge meant that China was no longer on the silver standard externally although her internal economy was still based on the white metal. From an average value of 34.5¢ U. S. in January the yuan rose steadily to an average of 40.975¢ in May and 40.3325¢ in June. Thus the June rate of exchange more nearly approximated the London parity than at any other time in the year, a factor which acted to discourage the smuggling out of silver. But this was only made possible by a serious deflation in prices which fell from an average of 99.4 in January (Shanghai, 1926 equal 100) to 92.1 in June. At the same time import prices declined more than export prices to make China's net barter terms of trade less disadvantageous. During this period, also, silver stocks at Shanghai remained rather stable for end-of-the-month figures, closing in December, 1934, at 335 million ounces and in June, 1935, at 331.8 million ounces. This stability resulted partly from purchases of silver from abroad by the Central Bank and partly as a result of the equalization fee which made it difficult for silver reserves to move legally out of the country. Furthermore, the bankers were not very desirous of selling their silver, knowing

full well that their position regarding liquidity--poor as it was--
 would be made even worse by such action.^{22/}

Money and credit continued to be very tight throughout the period. The normal seasonal return of silver from the interior did not materialize, causing a very marked contraction in the credits based upon the lost metal. Interest rates for short-term funds were reported as high as 25%-30% per annum during the Lunar Settlement Period (February 4-9) and there was evidenced a definite and strong movement of funds out of China.^{23/} The equalization fee was raised to $6\frac{1}{2}\%$ on March 27, but the rate continued to rise in terms of foreign currencies.

Then on April 6, Roosevelt set the buying price of silver at 71.11¢, a considerable increase over the former 64.64¢. On April 24 the price was raised to 77.57¢. The next day China protested again to the United States, but on April 26 silver hit a new high (since November 10, 1920) of 81¢. The United States Treasury refused to raise its offer from 77.57¢ to 81¢, so the next day (April 27) silver fell to $76\frac{3}{4}\%$. But the damage had already been done. Mexico called in all silver and placed her currency on a paper-copper standard and on May 3 Peru followed by declaring an embargo on the export of silver. The treasury backtracked, realizing it had purchased too rapidly, and by June 24 the price of silver had fallen to $70\frac{3}{4}\%$.

With an estimated 200,000 yuan of silver leaving the country daily without benefit of duty,^{25/} the Chinese government, perhaps seeing the

22-Arnold, Julian, Monthly Trade Report: China, Bureau of Foreign and Domestic Commerce, Department of Commerce, U.S.A., February-July, 1935, monthly issues, summary sections of each report.

23-Ibid., March, 1935, pp. 5, 23-24

24-Ibid., April, 1935, pp. 3, 24

25-Ibid., June, 1935, p.5

writing on the wall, began to increase its activities in the field of gathering control of the note issues of the Shanghai banks. On March 20 a loan secured on the customs revenue had enabled the government to achieve further control over the Bank of China and the Bank of Communications; ^{26/} on June 10 the Commercial Bank of China was brought under National Government control--the seventh of ten Chinese Shanghai banks of issue to be so brought under a unified policy. Since these banks had a note issue of 312 million yuan of a total issue of 356.6 million yuan, the way was effectively open for further reform and change in this branch of ^{27/} currency.

The 1935-36 budget was "balanced" at 957.5 million yuan, an increase of 40 million over the budget of 1934-35 when a deficit of 126 million ^{28/} resulted. Since it was more than likely that receipts would be even smaller than the previous year and possible that expenditures might exceed the stated amount, the deficit showed promise of approaching some 200 million for the fiscal year ending June 30, 1936.

It might further be noted, especially in its relation to decreased imports and consequently to falling import duties, that the existing tariff schedule made the smuggling of many types of goods profitable. In the case of such articles as sugar and rayon, which have high import duties, the legitimate trade almost disappeared in favor of the clandestine activities so prevalent in China. The Japanese are especially responsible for this smuggling. It has been reliably reported that not

26-Ibid., May, 1935, p. 7

27-Ibid., May, 1935, p. 7

28-Ibid., June, 1935, pp. 6-8

only was North China swamped with cheap, smuggled Japanese goods, but that in many cases Japanese goods were carried to Chinese ports in Japanese warships.^{29/} It can only be concluded, then, that the so-called effective tariff of recent years was not effective, either in keeping out foreign goods and thus protecting Chinese industry, or in securing an increased customs revenue relative to the amount of trade.

July saw a turn of events. The yuan fell to 38.715¢ as the London silver market almost broke on July 9, only to be saved by the purchases of the United States treasury. By October the yuan had sunk to 35.44471¢, but this really meant that the price of silver was no longer the major factor in determining the rate of exchange on the yuan: the yuan was free to fluctuate according to its purchasing power and its position in the various markets of the world.

Prices in Shanghai continued to fall in July, but by October had risen to 94.1 (90.5 in July). Import prices rose from 121.8 in July to 123.7 in October, but the most welcome rise was that in export prices--from 71.0 to 80.6. During the same period Shanghai silver stocks fell slightly, to 326.5 million yuan.^{30/}

On August 14 the United States Treasury bought 25 $\frac{1}{2}$ million ounces of silver at London--an amount equal to the 1934 output of the U. S.^{31/} Silver continued to be drained out of China. On October 1 a new subsidiary paper note (Ch\$.25) was issued, reflecting the need for subsidiary money as a result of the silver losses. On the same date the notes of

29-Ibid., August, 1935, pp. 6-7; Ibid., February, 1936, p. 1

30-Ibid., July, 1935, pp. 23-24; August, 1935, pp. 28-30; September, 1935,

p. 13

31-Cincinnati Enquirer, January 1, 1936, Financial Section, p. 1

the Central Bank for the first time surpassed in total volume those of any other Chinese bank of issue. This was partly achieved by the issuance of some 10 million yuan in notes in exchange for the provincial notes of Szechuan and close to one million in notes for depreciated subsidiary coins in several other provinces.^{32/}

October was perhaps the most hectic month in China's financial history. Speculation, rumors, fear, hoarding, the complete breakdown of legitimate trade--these were its chief characteristics. The yuan declined rapidly in the last two weeks, closing at 31¢ as compared to the peak of 38 $\frac{1}{2}$ ¢ reached earlier in the month.

Faced with this situation the Chinese government took the only possible course of action left open to it. On November 3, 1935, the Minister of Finance of China issued the following press release, which was virtually a new monetary system for China:^{33/}

"With the abandonment of the gold standard in recent years by many leading nations, and the rapid rise in the world price of silver, China's currency has become seriously overvalued. There has been severe internal deflation, with growing unemployment, widespread bankruptcies, flight of capital abroad, fall in Government revenues and an adverse balance of payments. For the three and a half months commencing July 1934, exports of silver amounted to more than 200 million yuan and it was evident that unless immediate measures were taken, the country would be drained of its silver stock. Accordingly, on October 15, 1934, the Government imposed a duty and an equalization charge on the exodus of silver through legitimate channels, and averted an immediate calamity.

"It was, however, clear at the outset that while the measure adopted could only be temporarily effective, it was not a fundamental solution. During the past year numerous petitions were received urging the government to devise appropriate remedies. Recently internal deflation became even more severe, and the business depression more acute. If continued, conditions would become intolerable.

"In order to conserve the currency reserves of the country and to

32-Monthly Trade Report, *op. cit.*, October, 1935, p. iv
33-Ibid., November, 1935, pp. iii-v

effect a stable monetary and banking reform, and to prevent a financial catastrophe, the Government, following the precedents of many countries in recent years, has decreed as follows:

"1. As from November 4, 1935, the banknotes issued by the Central Bank of China, the Bank of China, and the Bank of Communications shall be full legal tender. Payment of taxes and discharges of all public and private obligations shall be effected by legal tender notes. No use of silver dollars or bullion for currency purposes shall be permitted; and in order to prevent smuggling of silver, any contravention of this provision shall be punishable by confiscation of the whole amount of silver seized. Any individual found in illegal possession of silver with intention to smuggle it shall be punishable in accordance with the law governing acts of treason against the State.

"2. Banknotes of issuing banks, other than the Central Bank of China, the Bank of China, and the Bank of Communications, whose issues had been previously authorized by the Minister of Finance, shall remain in circulation, but the total outstanding banknotes of each bank shall not exceed the amount in circulation on November 3, 1935. The outstanding Banknotes of these banks shall be gradually retired and exchanged for Central Bank of China banknotes within a period to be determined by the Ministry of Finance. All reserves held against the outstanding banknotes, together with unissued or retired notes of these banks, shall be handed over at once to the Currency Reserve Board. Notes previously authorized and in process of printing shall also be handed over to the said Board upon taking delivery by the banks.

"3. A Currency Reserve Board shall be formed to control the issue and retirement of legal tender banknotes, and to keep custody of reserves against outstanding banknotes. Regulations governing the said Board shall be separately enacted and promulgated.

"4. As from November 4, 1935, banks, firms, and all private and public institutions and individuals holding standard dollars, other silver dollars, or silver bullion, shall hand over the same to the Currency Reserve Board or banks designated by the Board in exchange for legal tender notes, at face value in the case of standard dollars, and in accordance with the net silver content in the case of other silver dollars or silver bullion.

"5. All contractual obligations expressed in terms of silver shall be discharged by the payment of legal tender notes in the nominal amount due.

"6. For the purpose of keeping the exchange value of the Chinese dollar stable at its present level, the Central Bank of China, the Bank of China, and the Bank of Communications shall buy and sell foreign securities in unlimited quantities.

"The measures set forth above are designed for economic rehabilitation. The Central Bank of China will be reorganized to function as a bankers' bank. The general banking system will be strengthened, giving increased liquidity to the commercial banks under sound conditions, so that they may have resources available to finance the legitimate requirements of trade and industry. Measures have been prepared to create a special institution to deal with mortgage business; and steps will be taken to amend the present legal code affecting real estate mortgages so as to make real estate more acceptable as security for loans.

"Plans of financial readjustment have been made whereby the National budget will be balanced. Also with the centralization of note issue, the provision of adequate reserves against the legal tender currency and a system of rigorous supervision, confidence in the currency will be strengthened. It is hoped that the nation will whole-heartedly support the Government in measures to promote the national prosperity. The Government will take drastic measures to deal with speculation and attempts to bring about unwarranted increase in prices, and with any action intended to hamper the execution of the measures set forth in this decree."

That the Chinese government had assumed an herculean task was evident. In one act there were provisions for the modernization of the Central Bank and the transference to its control the issue of a new kind of paper money to replace existing paper money and silver dollars. At the same time the Bank was empowered to stabilize the rate of exchange through unlimited purchase and sale of bills. Silver was nationalized. An ambitious program, certainly! In the following chapter the results of two years of operation under the new monetary system are analyzed.

Chapter VII Monetary Reform in Operation

It is an extremely difficult task to describe the operation of China's new monetary system, to present an account of important economic events, and at the same time to criticize that new system both as to theory and practice. Yet we must consider these three elements together or we would present a wretched and imperfect account indeed. To the last chapter of this essay is reserved the analysis of the present struggle and its relation to China's future; here we will consider only those aspects of the war which are directly concerned with monetary reform.

The direct cause of China's new monetary program was, as indicated in the preceding chapter, the unstable position of the exchanges. Therefore our attention is at once drawn to the foreign exchange problem. The Chinese government decided that stability of the yuan was more important than stability of the internal level of prices. It has long been argued that such goals (stable price level and stable exchanges) are inconsistent. With this opinion the writer is not in accord. It is maintained in the reform proposal which appears in this essay as Appendix A that a successful monetary program implies, to a great extent, stability--or positive control of movements--of both items. For it is quite impossible to maintain a stable rate of exchange if the price level is changing and putting increasing pressure on that stability. If there is not some control of the price level the ability to maintain a stable rate of exchange is conditioned solely by the ability of a nation to build up a tremendous equalization fund capable of unlimited activities in support of the exchange value desired. For the world in general and certainly for China in particular, this is not likely to be the case. Therefore

it seems evident that a controlled exchange policy that pays no attention to internal price control will be difficult to carry out.

Leonard T. K. Wu, writing in the Far Eastern Survey, calls the government to task for attempting to achieve two inconsistent and mutually exclusive goals; stable exchange and stable price level.^{1/} But, as we shall see, prices have been allowed to fluctuate. It may be argued that by controlling the rate of exchange Chinese prices have been forced upward, which is to be desired. But let us remember that it is only possible to pursue such a policy (the internationalization of Chinese prices) when the entire country is using one kind of money and when the banking system is centralized, with power to influence credit and money policies resting in the hands of a strong central reserve bank. To attempt to raise prices before this unification has been completed is to cause depreciation of the new currency in terms of the currencies of other regions and to bring about consequent friction and confusion. Furthermore, the very problem of raising prices in China to the world level is a regional one in the sense that before any attempt can be made to relate prices in China to a world level, the various levels within China must be brought closer together. Yet this problem cannot be solved by raising all prices in all regions. It must be remembered that index numbers of prices in the large commercial centers of China are important and significant in their places, but that they do not represent a true picture of the price levels in China which in the main are village prices, expressed in copper rather than in silver. Of this matter we shall say more below.

On the other hand it is true that psychologically the effect of a stable rate of exchange on the business men of China was profound and

1-Wu, Leonard T. K., "China's Monetary Dilemma", Far Eastern Survey, Vol. IV, No. 24, December 4, 1935, p. 1

did much to promote confidence in the reform inaugurated in November, 1935. The matter of timing is the point of difference, in the main, between the plan adopted and that recommended by the writer. As we shall see below many local problems resulted from the reform which might have been eliminated or mitigated had the government provided a policy calling for a gradually rising price level together with as much stability of the exchanges as would be consistent with such a program.

The rate of exchange on November 4, 1935, was yuan equals G\$.2975 (sterling $1s/2\frac{1}{2}d$). The Central Bank (not yet organized as a central reserve bank) was authorized to buy at G\$.30 and sell at G\$.295 (sterling $1s/2\frac{5}{8}d$ and $1s/2\frac{3}{8}d$). Since the sterling-dollar cross rate was stable the yuan was in effect stabilized in relation to a cross rate rather than to the value of any country's currency. This makes it necessary to describe China's monetary system as a managed exchange standard rather than a foreign exchange standard, since the latter implies a fixed relationship to some country's currency. Much discussion has centered around this point, some maintaining that China was tied to the dollar, others that she was tied to sterling. The conviction is strong that early in the reform period the yuan was related more closely to the pound but that since the monetary agreements with the U. S. the yuan has been tied to the dollar. But since the cross rate has remained relatively stable the debate has significance only from the point of view of political relationships or as a key to future economic relationships. The pro-sterling feeling is very strong and it has been rumored that the Customs Gold Unit will be revalued in accordance with a fixed rate on sterling if and when England returns to the gold standard and stabilizes

the gold content of the pound. At present the C.G.U. is in effect stabilized at a value of CH\$. 2.25.

Whatever else may be said of the new law, one effect is certain and striking: yuan stability has been maintained. For more than two years the yuan has remained within a fraction of a cent of its "par" value--the first time in the history of China that such has been the case. Of course, to achieve this goal tremendous efforts and funds of great magnitude were necessary. The task was not easily done. There were many bear attacks which were successfully overcome, but which might prove dangerous in the future: in December, 1935, when the U. S. stopped buying silver and the price dropped sharply; in May, 1936, when franc instability threatened the sterling rate; in September, 1936, when the franc was devalued; in September-October, 1936, when Sino-Japanese relations grew strained; in December, 1936, during the Sianfu Incident (the kidnapping of Chiang); and several times since the outbreak of hostilities, when the flight of capital has taxed the funds of the Central Bank.^{2/}

To accomplish such exchange control, to withstand bear attacks, large sums are needed. The major sources of these funds for China were and still are her stocks of demonetized silver and the proceeds of foreign loans. In truth China has not divorced her currency completely from silver. Although its value no longer determines the value of the yuan, silver is still employed as a monetary reserve against the outstanding note issues. We proposed (see Appendix A) that China sell her silver hoards, after nationalization, and use the proceeds to establish an exchange fund.

2-Chi, Ch'ao-ting, "China's Monetary Reform in Perspective", Far Eastern Survey, Vol. IV, No. 17, August 18, 1937, pp. 1-2

The actual plan in operation is a compromise, the greatest advantage of which is the psychological effect on the Chinese of knowing that there is still some solid metal behind their currency. Yet fundamentally both plans are alike; silver is being sold abroad and the credits used to maintain the stability of the yuan externally. Yet we must repeat that because of inadequate price control much of this reserve has been dissipated to offset a disequilibrating force generated by the Chinese themselves.

How much silver did the Chinese government secure by this plan? Early reports indicated that at Hankow, Tientsin, Peiping and Canton the National Government was forced to appoint sub-committees to "supervise" the concentration of silver at those points.^{3/} This general lack of desire on the part of the Chinese to send their silver to Shanghai is based, perhaps, on two main reasons: first, they simply did not wish to give it up and knew that they could not be forced to do so; second, they did not wish, under existing political conditions, to surrender their silver for the notes of a government with which they might be at war at any time. For the North of China the latter reason would be the basis for pro-Japanese refusal; for the Canton Government and others it was probably a feeling of doubt as to the future policy of the National Government regarding the encroachment of Japan. On the other hand, the British Government issued Orders in Council calling on all British subjects and forms to obey the new laws, emphasizing that there could be no protection for those who violated these laws.^{4/} This is not to say that all Britishers

3- Wu, op. cit., p. 2

4- Monthly Trade Report, op. cit., November, 1935, pp. v-vi

and their employees complied with the laws, but the Orders have been of moral as well as practical assistance to the Chinese government.

For political reasons (coincident with the visit of the Japanese Economic Mission to China) China was able to secure additional funds of silver in later months. On April 1, 1936, the Japanese banks in Shanghai handed to the Currency Board CH\$ 9,300,000. in silver and the Bank of Chosen branch at Amoy surrendered CH\$ 229,000.^{5/} Kwangtung cooperation improved almost in direct ratio to the growth of anti-Japanese feeling in the National government. The rates finally established were as follows:^{6/}

CaC\$ 1.20 = Ch\$1.00 (paper)
 5 20¢ silver pieces = Ch\$1.20
 One silver dollar = Ch\$1.44

This arrangement took into account the depreciation of Canton paper in terms of silver and the paper money of Nanking, and also the depreciation of 20¢ pieces in terms of silver dollars. A similar project for Szechuan was carried out. For Yunnan and Kwangsi the rates established were as follows:^{7/}

Yuan (Chinese dollar) = Kwangsi \$2.00
 New Yunnan \$2.00 (paper)
 Old Yunnan \$10.00 (paper)

Following the outbreak of hostilities the Japanese confiscated certain silver supplies, but in the summer of 1937 the Chinese government sent Ch\$ 300 million in silver to Hongkong and thence to London for safe-keeping. This sum represented about one-third of the silver supply of

5-Far Eastern Survey, Vol. VI, No. 11, p. 127

6-Lewis, A. B., "Chinese Currency Policy", Pacific Affairs, Vol. IX, No. 1, March, 1936, p. 103

7-Far Eastern Financial Notes, Department of Commerce, U.S., No. 241, November 4, 1937

the government at that time. Dr. Kung reported in May, 1937, that the total monetary reserve held abroad for use by the Central Bank of China in pegging the rate of exchange was Ch\$ 800 million. Of course, there are also large private holdings which can be converted into foreign exchange should the need arise.^{8/}

It will be recalled that when Dr. Kung asked Secretary Hull if the U. S. would exchange gold for silver (late in 1935) the answer was in the negative. But shortly after the act of November 3 a monetary agreement between the U. S. and China was reached whereby the U. S. took 50 million ounces of silver at the price of G\$.65 per ounce.^{9/} On May 17, 1936 a further exchange arrangement was negotiated and upon its expiration (coincident with Kung's visit to the U. S. in the summer of 1937) a new agreement was signed on July 12.^{10/} This last agreement, the specific terms of which are still not available, was preceded by a joint statement by Dr. Kung and Secretary Morgenthau on July 9, which said, in part:^{11/}

"the United States Treasury will broaden the scope of the arrangements under which the Central Bank of China has been enabled.....to obtain dollar exchange for currency stabilization purposes."

The new plan called for a program identical to that asked for by the Chinese in 1935--the direct exchange of Chinese silver for U. S. gold, the latter to be kept by China as a reserve for her exchange fund. As a whole, then, China has done remarkably well--considering the disturbing factors--in carrying out her silver program for the purpose of stabilizing the exchanges.

8-Bloch, K., "The Last of China's Currency Silver", Far Eastern Survey, Vol. VII, No. 3, February 2, 1938, pp. 30-31

9-Ibid., pp. 30-31

10-Amerasia, August 1937, p. 281

11-Ibid., p. 281

The second important source of stabilization funds has been the securing of large and important foreign loans. And perhaps more significant than the loans themselves is the fact that they were secured without the political sacrifices which have characterized such loans to China in the past. Not only have direct currency loans been important, but those made for industrial or financial purposes (railroads, refinancing, etc.,) have relieved a normal strain on the exchanges, making it possible for the government to devote a larger share of its reserves for stabilization activities.

When the new law was announced, Sir Malcolm Leith-Ross, chief economic adviser to the British government, was completing his visit to China which, rumor says, was concerned with the problem of closer economic cooperation between England and China. The Japanese had protested bitterly about the visit and had declared in no uncertain terms that Japan would not tolerate a large loan to China by any government other than Japan. But there was nothing in the way of an unofficial loan between the Bank of England and the Central Bank of China, and perhaps the rumored £ 10 million loan was actually negotiated under some such set of conditions. Certainly the Chinese government would have hesitated before launching such an extensive program without some assurance that funds would be available to meet the sudden and wild flight of capital that might be expected after the announcement of November 3. To add further weight to this belief there is the statement by Leith-Ross, immediately after the law was announced, which spoke favorably and encouragingly of the new monetary system and expressed confidence in the ability of the Chinese government to carry out the program.

In order to further this borrowing program Dr. Kung left China in the Spring of 1937 for a trip around the world which took him first to the U. S. He was unsuccessful in securing further loans in this country but did secure the monetary agreement discussed above (this agreement, incidentally, was renewed for six months in December, 1937). After leaving the U. S. Kung went to Europe where his itinerary could be traced by the newspaper announcements of successful loan negotiations. On August 3 the Chinese Embassy in London reported the conclusion of an agreement, with the permission of the British government, by which a group of bankers in England, France, and the U. S. were to float a G\$100 million loan. The loan, which was to be for 30 years, was to be secured on the customs revenue, and to be subscribed in part by popular sale. The main purpose of the issue was to refinance certain obligations of the Chinese government. The loan was made, however, only "in principle"; actually nothing has been said publicly about the loan since the announcement. At the same time another loan of G\$35 million was announced to finance railroad construction. This loan carried a rate of 5%^{13/}.

On August 9, the French bankers agreed to place special funds at the disposal of the Chinese exchange account, amounting to 100 million francs. Likewise an agreement with the Swiss and Netherlands financiers was to provide an additional 22,965,000 Swiss francs with silver as security. On August 17, a G\$50 million credit was established with the Skoda firm of Czechoslovakia, mainly for the purchase of war materials.^{14/} The Skoda loan was the only loan to be labeled "for war materials" but it is possible and quite likely that other loans were so intended or will be so

13-Far Eastern Survey, Vol. VI, No. 19

14-Ibid.,

used. Even if the loans were restricted to other purposes the net result is the same since every dollar relieved from one use is thereby made available for another use--war materials. Of course it must be added that nothing can yet be said definitely about any of these loans since the political situation grew suddenly more dangerous and possibly cooled the ardor of some of the lenders. It is not unlikely, however, that some of the loans have already been completed, or will be completed in the very near future.

To carry out the reform in general as well as to secure for China the specific benefits of a modern central bank, a central reserve bank was provided for in the reform proclamation. But it was not until the late months of 1937 that positive steps towards this end were taken. A central reserve bank was created with a capital of Ch\$ 50 million, 40% of which was to be subscribed by the government and the remaining 60% by individuals and member banks.^{15/} The war had disturbed to a great degree the program looking towards the centralization and unification of the note issue of China. For some time after the law was passed the Central Bank of China and the two quasi-government banks (the Bank of China and the Bank of Communications) continued to work together in the unification of note issue. Currency agreements, discussed above, were made with as many provinces and regional banks as possible. In 1936 the Central Bank of China became the leading bank of issue in China for the first time. From November, 1935 to the end of 1936 the notes of the three government banks increased from 427 million yuan to 1,143 million

15-Chi, op. cit., p. 189

^{16/}
yuan. Nor did this increase represent a wild inflation on the part of China's banks; it represented mainly an increased conversion of notes. In May, 1937, considerable trouble arose over the conversion of "small coin" dollars in Kwangtung and Kwangsi, but the situation was rectified in short time. The rate established in Kwangtung was K\$1.50 equals Ch\$1.00.^{17/} Meanwhile the Central Banks opened branches at Kunning in the province of Yunnan and at Nanning in the province of Kwangsi to facilitate conversion and to aid in further control of the banking system.^{18/} On September 26, 1937 the notes were distributed as follows:^{19/}

Central Bank of China	416	million yuan
Bank of China	543	
Bank of Communications	372	
Farmers Bank of China	214	
total	1,545	
7 commercial banks in Shanghai, and provincial and municipal banks	575	
Grand total	2,120	

We notice at once that the Central Bank of China has lost its newly won position as the leading bank of issue but that the three government banks have become considerably stronger. Unification of the note issue is also closer to realization than at any time before. But we must note in addition the inclusion with the government banks of a new bank, the Farmers Bank of China. This bank was established during the anti-communist campaigns to "rehabilitate" the devastated areas. Actually it is

16-Far Eastern Survey, Vol. VI, No. 11, p. 128

17-Ibid., p. 127

18-Far Eastern Financial Notes, op. cit., No. 244, December 19, 1937

19-Ibid., No. 241, November 4, 1937

the private bank of Chiang Kai-shek, established to finance military operations. Originally it was chartered to issue only subsidiary coins, but the name was changed to its present title in 1935 and permission was granted to issue notes up to one million Chinese dollars. In 1936 these notes were declared to be legal tender. By September of 1936 the issue of this bank had reached 108.5 million yuan and continued to increase. A temporary permit allowed a further expansion of note issue but already that has been surpassed by the present figure of 214 million yuan. The bank is supervised by the Currency Reserve Board, but because of its political and military position such control is not very strong. Therefore the bank represents a constant threat to monetary control and stability.^{20/}

The notes of the government banks have also been used to secure quantities of subsidiary silver, mainly depreciated, and this has served the double purpose of supplying silver to the exchange fund and of aiding in the creation of a uniform system of subsidiary coinage. Large quantities of new subsidiary coins were made within China and much was ordered from abroad. But a great hardship resulting from the reform was caused by the omission of any positive and constructive action in regard to copper coins. Here it must be repeated that the great mass of the Chinese people use copper coins almost exclusively, and that their price level is a copper price level in contrast to the usual silver price level represented by index numbers. The immediate effect of the new monetary law was to raise the value of copper in relation to silver, i.e., less coppers

were required in exchange for silver subsidiary coins or for paper money. When copper prices rose, therefore, extreme hardship resulted since wages did not tend to rise for some time after. As copper stabilization agreements were made in various provinces for the conversion of old copper coins this effect was somewhat neutralized but there was an apparent lack of coppers which caused paper money and other temporary devices to be employed in lieu of metallic subsidiary money.^{21/} Had the program of the government included the stabilization of nickel and copper coins in terms of the new currency much of this difficulty might have been avoided. The conflict with Japan has disturbed the belated efforts to rectify this error, yet even under war conditions the National government has seen fit to place an order in Austria for a large supply of new subsidiary coins.^{22/}

It might have been expected that a period of wild inflation would follow the important changes inaugurated by the act of November 3, 1935. Yet such was really far from the case. We have already mentioned the encouraging statement by Leith-Ross; business men, bankers, and others also expressed confidence in the change. Business conditions as a whole took a change for the better. Credit was easier, optimism was the outstanding characteristic of the period. Of course many of the optimists were merely whistling in the dark to keep up their courage, but the two years since reform have justified their optimism.

The table below indicates the changes which took place in the levels

21-Monthly Trade Report, op. cit., December, 1936, pp. ii-iv, and 15

22-Far Eastern Financial Notes, op. cit., No. 241, November, 1937, p. 5

of wholesale prices in China after the reform of 1935.^{23/}

<u>Year</u>	<u>Shanghai</u>	<u>North China</u>	<u>Canton</u>	<u>Hankow</u>
1928	100.0	100.0	100.0	
1930				100.0
1934	97.1	91.8	94.3	89.0
1935	96.4	95.5	84.0	89.2
1936	108.5	110.6	105.4	97.2
1937 (May)	125.1	134.1	119.8	110.6

In Shanghai calculations show that 1936 prices were 12.6% higher than 1935. In Canton the rise was much greater, 25.5%, because of currency exchanges, while in North China where the government had least control or cooperation the rise was 15.8%. It is interesting to note that in Hankow, an interior city under government control the rise was only 9%. Of course it must be remembered that prices had begun to rise from their depressed state before the introduction of monetary reform, but it is quite impossible to separate the two movements.

The Hankow price increase is indicative of another important factor that must be remembered. For as we have said above, wholesale prices do not give an accurate picture of the Chinese scene. Cost of living indexes show a much greater stability than wholesale price indexes because costs are in great part determined by copper costs. Except where the reform acted to remove coppers from circulation the cost of living rose much less than wholesale prices. In Shanghai, for example, the wholesale price index for December, 1936 was 26.2% above that for October, 1935, but the cost of living in the same period rose only 13%.^{24/}

23-Far Eastern Survey, Vol. VI, No. 11, p. 128

The May figures for 1937 are used because shortly thereafter came the outbreak of war in China. Since then price indexes have reflected war conditions even more than the effects of monetary reform.

24-Ibid., p. 128

Furthermore, export prices rose more than import prices so that China's barter terms of trade moved in her favor and the pressing problem of the balance of payments was more easily met. From October, 1935 to December, 1936, import prices rose 19.3% while export prices in the same period rose 27.6%. The export price rise was indeed greater than the increase in the index of all wholesale prices.

May, 1937 prices show a further increase. The Shanghai index shows an increase of 29.8% compared to the average for 1935. In the same period prices in Canton rose 42.6%, in North China, 40.4%, and in Hankow only 24.0%. Again the superior position in respect to price increases is found in those areas where government control or cooperation were greatest and outside interferences least.

The possibility of a wild inflation still worries the Chinese, especially since the outbreak of hostilities has seriously interfered with the monetary system and the mechanism of control. Mr. T. V. Soong^{25/} voiced this fear when he said recently:

"It is essential that there shall be national budgetary equilibrium, effectively centralized control of bank note issues, and a satisfactory machinery to coordinate the activities of the commercial banks. The project for the reorganization of the Central Bank of China as a central reserve bank will, it is hoped, materially strengthen the currency and help to provide a means of ensuring the observance of sound principles of finance."

Yet, as we have pointed out above, many months passed before the Chinese government took the first steps towards the establishment of a central reserve bank without which the entire program of monetary reform was jeopardized. In a sense the Currency Reserve Board and the

25-Quoted in Far Eastern Survey, op. cit., Vol. VI, No. 11, p. 128

various agencies employed in carrying out specific reforms were laying the groundwork for the organization of the central reserve bank. The basic international function of a reserve bank is the maintenance of equilibrium in the economic system in relation to the rest of the world. This function is performed in two ways: first by action designed to bring about a short run equilibrium in the balance of payments, through the use of short term funds; second, by action upon the rate of exchange to bring about long run adjustments leading towards equilibrium in the balance of payments. The three main weapons of reserve bank control are changes in the bank rate, open market operations, and the more recent device of changing reserve requirements. Yet it is at once apparent that these controls are of no avail in a nation where banks are not intimately related to one another through their connection with a central reserve bank. Such methods of archaic banking as still exist in China must give way to modernization and reform. (For example, the practice of requiring a certain reserve against note issues is a modern innovation to Chinese banking.) Furthermore there must be an increased use of credit in order for the credit control devices of central banking to be effective. Likewise the uneconomic financial structure of the country which makes it impossible to secure the most economic use of available funds must give way to modern credit devices to pool funds for special purposes and so prevent the loss of the utility of those funds during whole seasons of the year. Steps in this direction have already been taken with the establishment of a Bankers' Acceptance House (in March, 1936) under the auspices of the Joint Reserve Board of the Shanghai Bankers' Association.^{26/} The Central Trust, a subsidiary of the Central

26-Chi, op. cit., p. 195

Bank, was authorized to underwrite war insurance up to ten million yuan on the transport of goods within China.^{27/} Later a mortgage House was established to fill another need long felt in China's banking structure.^{28/}

The political situation in regard to central banking is quite important. A central reserve bank should be free to carry out its program (program being that which has been decided upon as bank policy) without government interference. The old intimate relationship between the Treasury of China and the Central Bank cannot be retained if the new central reserve bank is to maintain equilibrium. Of course there must be cooperation between the two agencies, but central bank policy dictated by government is no longer central bank policy. The problems of war finance make this separation more difficult than ever as even the strongest of western central banks have succumbed to governmental desires under the exigencies of war finance.

Perhaps it goes almost without saying that the Japanese looked with disfavor on the reform of China's monetary system, especially after it showed signs of success. And in the North, where Japanese influence is greatest, many attempts were made to sabotage the reform. We have already pointed out that distinct obstacles were put in the way of note unification and the centralization of silver reserves. In recent months, with the military campaigns of the North have come monetary campaigns as well.

After the outbreak of hostilities and the early victories of the Japanese, restrictions on the circulation of Chinese money were put into effect by the Japanese army and local "peace preservation-autonomy"

27-Far Eastern Financial Notes, op. cit., No. 241, November 4, 1937, p. 5
28-Chi, op. cit., p. 189

governments. Orders were issued that Japanese money was to be accepted by all merchants, and since the Japanese soldiers used only Japanese money it was not long until Japanese money had practically displaced Chinese money in many sections.^{29/} Late in 1937 rumors (reported by the U. S. consul)^{30/} were circulated that the Japanese intended to establish a branch of their central bank in North China to finance trade, using a currency unit pegged to the yen at equality. Complete control of the exchanges was achieved and restrictions similar to those already in effect in Manchuria make it necessary to secure a permit for all exchange dealings with countries other than Japan. Of course such restrictions have no basis in either national or international law, but that is not likely to cause much worry for the Japanese.

In December, 1937, the Japanese established a Kalgan Mongolian Bank capitalized at 12 million yen.^{31/} But it was not until early in 1938 that the financial plans of the Japanese for North China were completely revealed.^{32/} The present plan calls for the organization of a Federal Reserve Bank to control the eight large banks in the area. This bank will be capitalized at 50 million yen and will issue a new currency to replace all existing note issues, the reserve for this new issue to be composed of the silver holdings of the eight banks (not previously handed to the National government) valued at 60 million yen and a loan of 100 million yen from Japan. The notes of the new bank are to be inconvertible and pegged to the Manchurian yuan and the Japanese

29-Far Eastern Financial Notes, *op. cit.*, Nos. 241-247

30-Ibid., No. 241, November 4, 1937, p. 6

31-Far Eastern Financial Notes, No. 244, December 19, 1937, p. 5

32-Ibid., No. 246, p. 5

yen at equality (the latter two units were pegged at equality late in 1935). The bank would act as the depository for all gold and silver reserves in North China and serve as the agent for exchange control and possibly receive the customs duties paid at the northern ports.

And already the customs receipts of China have fallen off drastically, although before the outbreak of the war it seemed that receipts for 1937 would be an all-time high. Not only the loss of large cities where customs are collected but the increase in smuggling have operated to remove a large portion of China's most important source of national government income.

In conclusion, a few words might be said about a new "currency" which has made its appearance directly as the result of the war. The balances held in the Shanghai banks were blocked for many months by restrictions imposed by the Bankers' Association and the government. Withdrawals were limited at one time to 5% per week of deposits with a maximum personal withdrawal each week of 150 yuan. These restrictions were later relaxed but there are still large blocked balances. As the result of this situation there developed an extensive use of wei-wah, or blocked balance notes. For some time they circulated at a discount of 10% but more recently the bankers have agreed not to discount the notes and their use has diminished somewhat and they circulate at face value. Loans which were due during the October settlement date (1937) were put off until the April date--another example of the confidence of the Chinese people in their government and in the new banking system, as well as

in the ability of that government to survive.^{33/}

The war has interfered with monetary reform in many ways, it is true, but at the same time the courage and vision that have been shown, the support from the people as a whole as well as from banking and business interests, the very fact that foreigners even consider loans to China at this time, indicate the confidence which China has merited in the last few years, and indicate that many involved interests are not yet selling Chinese freedom short.

33-Far Eastern Survey, op. cit., Vol. VII, No. 1, January 5, 1938, p. 8;
Far Eastern Financial Notes, op. cit., Nos. 241-247

Chapter VIII Can China Survive?

The basic question can be quickly stated: can China survive? The answer is also quickly--and confidently--stated: yes. The reasons for that answer are discoverable only in the complex maze of China's economic and political background and development.

We have seen the clumsy and uncontrollable confusion that was China's monetary system give way to modernization and reform. Not that China's monetary problems have been solved, but it is evident at last that the way to the solution has been seen, that action is no longer a dream but a reality based on accomplishments. Much has been done, much more remains to be done, much that has been done has been undone, and today that reform program is only a part of the new China which is fighting for its very existence.

In a very real sense the fact that China has not progressed in the modern way of life may be her greatest bulwark against the Japanese invaders. We have seen that the Chinese economic life of the traditional pattern was carried over into the modern period, that only along the seacoast was there the kind of economic life that can truly be called Western. The great portions of China which had just begun to feel the impact of the West still retain the framework and even the outer trimmings of the traditional economic life. And so Japan may capture China's large commercial cities, she may bomb and destroy others, she may capture or destroy the lines of communication--but she does not by these actions destroy China. Of course China suffers when these material injuries are inflicted upon her, but for the great mass of the Chinese

people life goes on in the same way. A return to some of the handicraft methods that were being slowly replaced by modern factories may mean less efficiency as compared to factories, but the system is nonetheless productive.

In order to defend herself China must reorganize and strengthen the old transportation systems of the interior and establish some kind of central control over production and the supply of goods necessary to the conduct of war. The guilds, the tongs, the political, social and religious organizations that exist within China--all of these represent the media through which such control can be established. Perhaps the best teachers in this field are the communists, whose ability to organize and direct the activities of the masses enabled them to maintain a rather strong and strategic position in China for the last ten years, despite the opposition of the National Government. At no time in the history of China has any government had such popular support. Nationalism, if no other characteristic of the West, has at last taken root in the mass of the Chinese people. Of course there is always the danger that the government may lose such mass support. But this is not likely for several reasons. Chiang Kai-shek has accepted the struggle against Japan, whether against his original intentions or not does not matter. He is determined to be a great leader in China, to remain in power. To do so he would sacrifice almost anything (some, indeed, feared he would sacrifice China). The masses in China are bitterly anti-Japanese. Probably no pro-Japanese government could remain in power long, for the masses without question would rise up against it. And here is a factor of great importance for the cause of reform in China, monetary and otherwise. In order to retain

the backing of the people the National government may be forced to institute general reform legislation which will go a long way towards freeing the new China from the social injustices and maladies which today are so rampant.

China, protected by her vast size, her poor transportation system, her traditional economic system, employing the guerilla methods of warfare suited to her topography and equipment, can successfully resist any further great inroads into her territory by Japan. And these factors will enable China to fight the long and deadly war the present conflict seems destined to be.

Japan, on the other hand, is in a difficult and delicate position. As we have pointed out, Japan has over-reached herself and at this time perhaps no one knows it better than Japan. Her finances are weak, she is dependent upon foreign trade for her supplies of raw materials for basic industries, and she is not without those within her borders who await the chance to sabotage the war and secure a peace on the basis of friendship between the masses of Chinese and Japanese people. As Japan's forces are spread over a wider and wider area their position is less secure. Who can say how many garrisons in Manchuria, in North China and even in Korea have been attacked and wiped out by the roving bands of Chinese and Korean patriots? Nor does Japan forget that a continuation of her present policies means an inevitable clash with the Soviet Union. Already the Japanese have recognized in their budgetary statements that the war will be a long one, and already they have tried--unsuccessfully--the maneuver which extricated them from a similar position during the war with Russia in 1904-5. At that time Japan, after winning a few

major battles early in war, realized that a long war would mean disaster since her own position was weak and that of Russia increasingly stronger. Therefore a third party was brought in to ask the Russians if they would accept a peace provided that Japan would be willing to forgo the "knock-out punch". Germany attempted, unsuccessfully, to do for Japan in recent months what the U. S. did for Japan earlier in the century. But the Chinese are unified and determined to resist; and they are ready to fight a long war.

Japan, then, is vulnerable. China can fight on without any possibility of Japan's destroying her economic basis. Eventually, if the forces discussed above are adequately pictured, China will win. That victory will leave both Japan and China impoverished (as would also be the case were Japan to win). The next question, then, concerns the future of China. As indicated above, much depends upon the steps taken by the government of China during the war. The form and nature of China's future economic and political organization will be determined mainly by the course of events during the struggle. Even today this question is in the minds of many Chinese. Not long ago Lin Yu-tang, eminent Chinese philosopher and writer, also pondered this question:^{1/}

"Where are the good men in China?.....So, in my mind, I picture the Saviour of China. I would believe in a revolution, any revolution, and in a party, any party, that would replace the present government by Force, Fate and Favor with a government by law."

That desire, that belief, is echoed by millions of Chinese today. For no reform, whether monetary or otherwise, has meaning if China is to be

1-Yu-tang, Lin, "The Way out for China", Asia, October, 1935, Vol. XXXV, No. 10, p. 586

dismembered, and survival itself loses meaning if that survival is not accompanied by a removal of the yoke of industrial and agricultural serfdom against which the masses of the Chinese people struggle today.

If all this leads to some doubt and uncertainty as to the future of China, to pessimistic thoughts concerning the possibility of achieving the survival of China and with it the thorough-going reforms essential to China's progress, it is, despite the optimism of the writer, a true picture of the Chinese scene today. More we cannot say, for in the words of Nathaniel Peffer:^{2/}

"There are only questions. Except for the stuff of journalism, the reporting of day-to-day events, no statement can be made concerning China that does not end in an interrogation point. The past can be understood; the present can be observed; the future can be conjectured--that is all."

2-Peffer, Nathaniel, China: The Collapse of a Civilization, p. 281

Appendix A

A Proposal for Monetary Reform in China

Appendix A: A Proposal for Monetary Reform in China^{1/}

It must be apparent to the reader that no one of the solutions to China's monetary problems advanced in the years up to 1935 can be considered applicable today. Nevertheless, the reports we have examined (and especially the Kemmerer Report) furnish an excellent statement of the particular problems that China and Chinese monetary reform must face. In this respect alone, regardless of the recommendations made, the Report of the Kemmerer Commission is important and significant in the history of China.

The basic necessities of monetary reform are generally agreed upon by all who have studied the Chinese situation. Clearly enough, the silver standard for China is both undesirable and untenable. The past five years have surely demonstrated this to the satisfaction of both Chinese and foreign observers. It is likewise generally conceded that unification of China's currency and monetary systems must form a basic part of any acceptable reform measure. It is further agreed that the ultimate goal must be a standard in harmony with the standards of other countries, but the real clash appears when consideration is given to the means whereby the given common end is to be achieved. Further consideration must be given to the future course of China's economy: that is, the plan must, at the least, place no obstacles in the path of further industrialization, and at the best should promote that expansion and extension of economic life.

1-This appendix, as indicated in the Introduction, was written in 1935 before the promulgation of the New Monetary System of China; whatever value and interest it contains is, therefore, historical and comparative. It is not necessarily a program that could be adopted today.

What is there about the picture presented in the early months of 1935 that has so changed the conditions described by the Kemmerer Commission in 1929? Paradoxically, there has been little change, but there is much that is different. There is today a Central Bank, a Central Mint, a more efficient (but woefully weak) revenue system, a Customs Gold Unit, a uniform Yuan dollar in place of the clumsy taels, and a lessening of the internal restrictions to trade; there is indeed all this, and much more. Yet the basic problems still remain, for the reform measures introduced have neither been complete, uniform, nor consistent. Nor has the fundamental task of transferring the Chinese economy to a universally accepted monetary basis moved perceptibly nearer its goal.

We recall (p. 70) that Kemmerer, after discussing the direct and indirect plans for the adoption of the gold standard, gave the weight of his authority and opinion to the former method. In so doing he effectively demonstrated the disadvantages of the indirect plan as he perceived the indirect plan. We hesitate to read Dr. Kemmerer's mind but surely it seems that he was so convinced, on the evidence of previous examinations and experiences, of the greater efficacy of the direct plan, that he overlooked certain aspects of the indirect plan, which even if undesirable, certainly were vital enough to merit investigation, discussion, and --if the Commission so concluded--refutation. For it will be further recalled that the entire case against the indirect method presupposes and assumes that such a plan must proceed to the gold standard after the establishment of unification on a silver basis. But there has always been the possibility--never mentioned in the Kemmerer Report--of

unification on a paper basis before the introduction of the gold standard. And it will be seen below that the introduction of this variation in the indirect plan destroys, at one blow, the two greatest arguments leveled against it. Nor, strangely enough, is such a revised plan so inconsistent with the direct plan suggested by the Kemmerer Commission as that Commission declared the silver-to-gold plan to be; it is, rather, almost between the two, utilizing, as we shall see, many of the advantages of both.

Whether we are proposing such a paper-to-gold plan or not it is essential that we first determine wherein the Kemmerer Report has given us something which is today useful in the formation of a reform proposal, and wherein its errors of omission and commission have opened up new vistas to the eyes of the would-be reformer.

The first objection raised by the Kemmerer Report against the indirect plan is that the government would lose the seigniorage on the silver coins when the gold standard was adopted. That is, silver coins which had been circulating at a bullion value equal to face value during the unification process would be suddenly raised in value to provide the spread between bullion and face value necessary to keep the coins in circulation. Since these coins would have cost the government their full silver bullion value when coined, the creation of the spread would leave the profits, or seigniorage gain, in the hands of those who actually held the coins, not the National Government. There can be no denial of this obvious fact. But if the currency in circulation was composed of paper money rather than silver coins, and the government had title to all the silver, then there would be no unearned "currency profits" to those who happened to

hold Chinese dollars; the dollars held would merely become convertible where formerly they had not been. Further consideration of this point we reserve to the section dealing with the actual reform proposal.

The second important objection to the silver indirect method is that when the coins would suddenly be raised in value (a spread of 33 1/3% was recommended in the Kemmerer Report) there would be a necessary and violent deflation. But this "necessary" deflation results from the necessity of choosing a gold content of the new unit before the gold standard is actually adopted: that is, a unit is chosen and then the circulating media so raised in value that a spread of 33 1/3% results. But if the gold content of the proposed unit were not chosen during the unification period, when the time came to adopt the gold standard the new unit could be so chosen that deflation would not be a necessary result. For the spread desired would already exist and the absence of silver coins as the temporary standard would further facilitate the adjustment. Again we promise to discuss this matter in greater detail below.

Therefore, while the Kemmerer Report may still be justified in its conclusions, it is evident that the paper type of reform proposal must be refuted before it can be said that the Kemmerer Commission has presented an absolute and complete statement of the problem and its solution. Again, we may speculate as to what the Commission would have answered to such charges. Most likely they would have charged the proposed variation with preoccupation with idle dreams, wool-gathering in the land of managed currency slumber, without considering the fact that paper money is not and will not be respected in China. Therefore, they

might say, without further argument, the proposed paper standard is useless as a means of achieving monetary reform in China. But the writer holds no such view of the situation. There is a time in the economic life of any nation when it must learn to respect paper money, whether it is to the nation's liking or not. Such a time we feel is upon China today. For it is evident from the trend of recent events that if China does not of her own will and accord place her currency on a managed paper standard it will be only a matter of time until she will be forced to do so--with greater evil to her economic system.

As for the many other valuable aspects of the Kemmerer Report we can have only general admiration. And it is important to remember that many of the reforms and changes since 1929 were direct results of the Kemmerer Report. The Customs Gold Unit (which, it was probably hoped, would be extended to all monetary transactions) has a gold content equal to that of the sun recommended by Kemmerer. The establishment of the central bank and its operations may be attributed partially to this Report, as well as the creation of a central mint and the inauguration of the first positive steps in the direction of uniformity in the issues of coins and paper money. The record clearly shows, then, that regardless of whatever else can or may be said concerning the merits and demerits of the Kemmerer Report, that report has had more practical significance for Chinese monetary reform than any other proposal to date. Nor is it likely that much will be accomplished in the future that does not bear a heavy burden of indebtedness, either directly or indirectly, to the Report of the Kemmerer Commission.

When we turn to the consideration of our proposal for monetary

reform for China we must face certain conditions which have arisen since 1929. The existing silver situation must be taken into account and that situation, as we have indicated above, is such that in the very near future China will be forced to abandon her make-shift silver standard. Even had the coinage of the sun as proposed by Kemmerer been actually accomplished, that coin, with its spread of 33 1/3%, would disappear from circulation when silver reaches a price in the neighborhood of G\$.75 per ounce. Considering that it is the avowed policy of the United States to raise the price of silver to G\$1.29 per ounce, the melting down of the sun would come about even should the silver policy of the United States prove to be a failure. For it is evident that at the present rate, (May, 1935), the death mark of the sun would be soon reached. So it is readily seen that it is not because of blind and foolish faith in the ability of the Chinese to administer a managed paper currency that we recommend that China should immediately abandon the silver standard and place her entire monetary system on a paper basis. We recommend this course of action because there is for China no other feasible alternative. To use the analogy--well worn by this time--China must quit before she gets fired. And that she will be fired is no longer open to serious doubt.

The first step must be the nationalization of all silver and gold monetary stocks, including all silver coins equal to or greater in value than the Yuan dollar. In exchange the Central Bank must be empowered to issue notes, while the issuance of paper money by any other organization, whether public or private, must be absolutely forbidden. Only in this way can the danger of over-issue be minimized. The paper yuan dollar should be declared the standard money in which all payments and receipts

of the Government as well as private individuals and corporations are to be made. There is no longer any reason, as there was in the provisions of the Kemmerer plan, for the postponing of the legal tender date and it must be declared and enforced as soon as the mechanism of the change is established.

To the Central Mint must be given the sole right to issue coins. The divisions of the unit may well be those suggested in the Kemmerer Report since they are units to which the Chinese have been long accustomed and will therefore minimize the friction set up by the change. The subsidiary coins should therefore (the yuan being omitted) be as follows:

50 cents	silver
20 cents	silver
10 cents	silver
5 cents	nickel
1 cent	copper
$\frac{1}{2}$ cent	copper
2 mills	copper (only if thought necessary)

The paper yuan and the subsidiary coins must be kept at par in order to prevent any one kind of money from driving out of circulation other kinds of money. In order to keep this parity the government must stand ready at all times to exchange the various units at face value, i.e., without discount or premium. This can be greatly facilitated by the use of numerous and widely situated exchange shops operated by the government, for only thus can discounting be prevented and the confidence of the people buoyed up until they understand that they will not lose by the reform.

For international purposes the usual mechanism of the gold exchange standard can be utilized, but not in reference to the currency of any particular country. The Bank must stand ready to buy and sell drafts

on gold standard countries at all times and at fixed prices, with the customary premium charges to be added to secure the benefits and actions of the gold shipping points. Again it should be emphasized that these buying and selling points need not be permanently fixed, but should vary with the policy desired. By the use of this well-known gold-exchange standard mechanism the entire system will remain finally convertible into gold or gold drafts.

But solvency and safety are not thus assured for there arise what at first blush are two quite embarrassing questions: where will the Chinese government get the necessary funds to establish this gold exchange fund, and how can she survive the first few months when any demand for gold or gold drafts that is not satisfied will wreck the entire reform plan before it actually begins? The answer is to be found in the first proposal for reform: the nationalization of silver and gold. The National Government will have control over the major supply of silver in China and this supply must be sold on the world market for whatever price it will bring. Of course such sales will tend to cause the price of silver to fall--a consideration, however, which must not deter the government from continuing its sales. For the silver price of today--and the higher price which will no doubt exist tomorrow--cannot be sustained indefinitely. As soon as the United States policy proves itself to be a failure--as it must since the price of silver cannot be arbitrarily and indefinitely kept at so high a price--the price of silver will fall anyway, and fall sharply. Even should the policy of the United States be a success at first and the silver reserves be built up to the required ratio of one to three of gold, the United States

Government will not be able to step out of the silver market. To do so would cause a fall in the price of silver which would wipe out the desired ratio between gold and silver so painstakingly established. In other words, the United States is holding firmly to the tail of a wildcat and although the wildcat may carry the U. S. to its destination, the passenger will find it more difficult to leave the vehicle of transportation than it was to grab the tail and command ~~and~~ ~~the~~ animal to run. So that even initial success will merely postpone the day when the United States must realize that it cannot permanently raise the price of silver, and the government at Washington must take its clawing from the wildcat. Come what may, then, the price of silver will fall--whether at the hands of the Chinese or the Americans is not, at the moment, important.

If it be further argued that the Chinese Government has pledged itself not to sell demonetized silver, we can only answer that the pledge was contained in an agreement which was broken "a long time since and by some other sea." Besides, China ratified the Agreement with the provision that if and when any signatory power acted in such a way as to affect adversely the Chinese economy she reserved the right to "go and do likewise", to act according to the dictates of her own interests and defense.

Lastly, if it be brought against this plan that the sale of silver is not feasible or desirable, there is but one blunt and obvious fact which contradicts this attack: the silver under consideration is being rapidly sold abroad today by individuals instead of the government, and, as a matter of fact, to the monetary loss of the government. From this point of view alone it is necessary and desirable for China to nationalize the white metal and conduct its sale abroad to the best national advantage

possible.

But there still remains unanswered the question of how the immediate period, before silver sales have commenced, can be financed. In the interests of solvency and safety it is necessary that China borrow sufficient short-term funds from the nations where the exchange fund will be kept, to tide over the anxious period when the stress of unsatisfied demands for gold credits might well wreck the entire proposal. This loan must be for a short time only and should not be secured on anything but the reserve fund itself. As the reserve fund grows in size the loan should be repaid out of this fund. Once established, the sales of demonetized silver, the premia from sales of exchange, the profits of seigniorage, and other minor items of income relative to the plan, will provide sufficient revenue for the maintenance of the reserve fund. Furthermore, once the maladjustments attendant upon the adherence to the silver standard are eliminated by the reform, the balance of payments will return to its normal position in favor of China. This excess of inpayments over outpayments was formerly used to purchase silver; after the inauguration of the reform proposal it can be used to purchase gold to be brought to the central bank or to be added to the reserve fund kept abroad.

One problem demands further discussion and elucidation: the relation of subsidiary coins to the paper yuan and gold drafts. The present exchange value of the silver yuan (December, 1934) is about G\$.34. Thus the paper yuan to be issued by the government under the proposed plan would have a similar exchange value since the government would exchange paper for silver at that ratio. The subsidiary coins of silver (50¢ and 20¢) will therefore have exchange values of G\$.17 and G\$.068 respectively.

So the existing silver units below one yuan must be exchanged for this new set of subsidiary coins on the basis of the actual silver content or value of the old coins. If a silver coin circulating before the reform had an exchange value of more than G\$.17 the government must offer in exchange for it a new half-dollar plus the number of copper coins necessary to make the exchange equal. If this is not done the silver coins will tend to move to the world market via the melting pot, leaving the government of China without the means of maintaining a subsidiary coinage other than paper, which, for small denominations, is both difficult to manage and annoying to use. Equal exchange, therefore, means that the government loses the seigniorage on money below the value of one Chinese dollar but it will encourage the people rapidly to exchange their old coins for the new ones--an effect of no little importance. When the price of silver falls as a result of the sales of silver by the Chinese government there will exist a subsidiary coinage system with a spread between the actual value and face value--a spread achieved without deflation and at merely the cost of losing the seigniorage on the subsidiary coins. But the government need not bemoan this loss for it will be amply compensated by its seigniorage profit on the yuan paper dollars of almost 100%.

To supervise and direct the carrying out of the many angles of this reform there should be appointed a Currency Commission, similar to that recommended by the Kemmerer Report, which should have full authority to make the minor changes, set the dates, etc., which the reform entails. The general policy of this commission must be to facilitate the reform and to do so without attempting to fix a permanent exchange rate. They

should, however, watch carefully the actual rate of exchange, for it is the reflected opinion of Chinese and foreigners as to the worth of Chinese currency. The rate will, therefore, enable the commission to see if, and how much, the new currency is depreciated or appreciated in value, and indicate the necessity for remedial action, i.e., the necessity for expanding or contracting the currency.

To facilitate the maintenance of this more or less constant par of exchange and to secure further benefits of the gold exchange standard it might be best for China to consider more carefully the position of the pound sterling than any other unit. Since a rise in the price of silver is to be expected in the very near future, a suggested rate is one yuan equals 1/8d., which would make its equivalent in U. S. currency slightly above that recommended by Kemmerer, (G\$.405 rather than G\$.40, using the old rate of exchange between England and the U. S.). But the reform plan here presented is not dependent upon any given set of prices or values. Its principles can easily be adapted to whatever price relationships exist at the time when reform is being established, and even should the present conditions continue unabated for some time without any positive steps being taken towards their rectification the principles here laid down can be utilized.

The commission must also watch carefully the relationship between silver coins and paper money. The silver in two fifty-cent pieces will have a value of G\$.36 as compared to a value of the yuan paper dollar of G\$.405 so that those who are holding silver will not find it to their advantage to sell it abroad since they can, in fact, get more for it by exchanging silver for paper which, if presented in units of at least

10,000 yuan (or any other figure decided upon by the commission), will be convertible into gold or gold drafts. As the price of silver falls and the silver coins sink in silver bullion value (although slowly, to be sure) the rate between paper and silver must be kept constant so that the necessary spread between the bullion and face value of silver coins will be achieved. Therefore prices in China need not rise or fall and this stability, impossible under silver, will give further confidence to the Chinese people as well as to those foreigners who trade with them.

It might be argued that China would gain more by tying her unit to the American dollar as Kemmerer no doubt wished to do, since his sun was chosen to give an "even" rate of exchange between China and the United States. The United States dollar has a definite amount of gold today (although it may not have one tomorrow), whereas the pound has no such fixed content and China's position also requires the use of a unit with no fixed content of gold. But even were the U. S. willing to make the loan necessary for the reserve fund the actions of the American Government have not been conducive to the encouragement of Chinese affection or friendship. Nor is it likely that the American government would greatly desire to facilitate a plan which would assure the failure of the American silver program and which is itself an outgrowth of that program. There is no such conflict between the aims and desires of England and China and there is, in fact, a further advantage: India, jewel of the British Empire, also has tremendous stocks of demonetized silver to sell so that both India and China have interests in common which it would not be wise for England to disturb. This consideration of mutual interests assures that England will not act against China's

silver policy, for to do so would be to injure India as well. Of course, India may look with disfavor upon a new competitor in the silver markets of the world, but either an agreement could be reached with India, or, what is not very far from the truth, the Indians might be convinced that legalized sale of Chinese silver will not be much greater than the sale that has been going on in recent months through illegal channels.

Several other points remain to be clarified. It would seem that such a paper standard as proposed would discourage the movement of international funds to China, and ordinarily this might be so. But China can contract her debts--and if she is to increase her economic activity she must borrow heavily in the years ahead--in terms of the lending country's currency or in English pounds, which will give her a degree of stability never before attained in Chinese debt-funding. Or, if so desired, the Customs Gold Unit might be employed for this purpose; but this is not desirable since the existence of several units of value is a confusion from which China should escape rather than further entangle herself. With interest and principal as fixed sums no longer dependent on the value of silver there will be a minimum of friction when the ultimate gold standard is adopted and the debts are converted to the new unit. This stability will do more than encourage the lending of funds to China--it will make the Chinese who need such funds anxious to borrow since the fear generated by the instability in the value of silver would be removed.

An interesting and delicate side problem presents itself: as productivity increases and as it becomes necessary to increase the supply of money, care must be taken to ensure that too great an issue does not

result, which would endanger the value of the yuan. In many places within China the level of prices is extremely low. It is desirable, therefore, to take action which will create a more uniform level of prices throughout China and secure a greater degree of conformity between this level of prices and the general world level.

Copper coins and nickel coins must be re-issued more slowly than other units of the currency. As Dr. Kammerer says, these coins form the basis of all transactions for the great mass of people so that to keep them in circulation as long as possible at fixed ratios to the other coins will help provide ready acceptance for them. These technical points, however, such as how and when certain kinds of money should be issued and old ones recalled we must leave to the Commission itself, for much will depend on the actual conditions existing at the time of reform. We are here concerned only with the broad outline which that reform should take.

The change to a regular gold exchange standard (i.e., one in which the unit is tied to a pound sterling of fixed gold content) will not be a difficult task. Whatever is the value of the Chinese unit when English monetary policy includes a fixed and definite gold content of the pound will be the yuan's value thereafter. The yuan, then, will have a fixed value in relation to the pound which can be maintained after England's return to the gold standard. Thus there need be no revaluation of the yuan, or, to repeat what has been said above, a devaluation of the currency.

Two major political problems, one internal and the other external, still beset the economic reformer. Internally there is the question of

the authority of the National Government, which admittedly is none too strong. How then, it might well be asked, can such a government introduce so sweeping a reform? The answer takes us back once more to a fundamental point of difference ^{Between} ~~among~~ the Chinese and foreign political-economic observers: political stability versus economic stability as the first step in major reform. It is here maintained that the first step must be economic. There can be no permanent union of China by force. Already the National Government itself has realized this fact and is reversing its old policy of military action in order to unify China before attempting reform. Within the area under the direct control of the Nanking Government, small though it may be in relation to the total area of China, there are in existence the machinery and channels through which monetary reform must operate. We are still convinced that a successful monetary reform would be the most important single factor in bringing about the unity of China. It will be a difficult task but it can be done. Indeed, it must be done.

The external problem is of a similar yet diverse nature. It, too, involves the question of authority: not authority as between the various political or regional divisions within a country, but the authority imposed by one state upon a neighbor state. To put the matter briefly, Japan has declared a Far Eastern Monroe Doctrine, with Japan as the "guardian" state. Aside from other points of conflict between Japan and China, there is the question brought into sharp relief by the proposal here presented of Japan's notice to the world that no state may participate in loans to China without Japanese permission. Nor would Japan look with favor upon a reform which would tie the yuan to the

pound sterling--the monetary unit of her greatest competitor in trade. All that can be said is that Japan herself has been unable or peculiarly unwilling to make such a loan to China and that the time is past when China can supinely accept Japanese ultimata. China must resist or she is lost as a nation. Furthermore, it seems highly doubtful that Japan would wage war upon powerful England because of such a loan. Economically, Japan stands to gain by Chinese currency stability. Her vast commercial and financial interests in China would thus be put on a sound basis. And since Japan is herself a member (in disrepute at the moment) of the sterling bloc, a yuan tied to sterling would, in effect, mean a yuan closely associated with the yen.

We have made certain recommendations for the reform of the currency system of China which must precede any attempt at complete monetary reform. The plan here presented is not only what the writer believes to be best suited to China's needs; it also recognizes and includes in its scope the conditions which actually face China today. It is a plan that can be established with a minimum of friction and change in prices and the value of money in China, thus contributing to the confidence which the Chinese people must have in the reform if it is to be effective. Wherever any portion of the plan calls for changing such conditions, some effective device for checking adverse reception or action is included. It is, however, but another answer to the dilemma which China has faced for so many years without reaching an adequate solution. No doubt it contains errors and would require many changes before its general plan of reform could be adopted. But present conditions, more than ever, call for immediate action. Upon the present National Government of China

rests the duty and obligation to China of acting in this matter. The record of monetary reform has been mostly black in the past, but that Chinese Government which fails to take opportunity, or make opportunity for effecting monetary reform in the near future to some degree and in some definite fashion, must account to history for its neglect and failure --and may, perhaps, be called to account by the Chinese people as well, which, for politicians, is perhaps a more alarming prospect.

Appendix B
Statistical Appendix

I
Silver

Table 1
 PRICES OF BAR SILVER AT NEW YORK, 1874-1938
 (dollars per ounce)

<u>Period</u>	<u>Price</u>	<u>Period</u>	<u>Price</u>	<u>Period</u>	<u>Price</u>
Average					
1874-79	\$1.276	1911	.541	1925	.6907
1880-89	1.045	1912	.615	1926	.6243
1890-99	.749	1913	.604	1927	.5668
1900	.621	1914	.556	1928	.5843
1901	.597	1915	.507	1929	.5330
1902	.528	1916	.657	1930	.3830
1903	.542	1917	.840	1931	.2900
1904	.578	1918	.989	1932	.2830
1905	.610	1919	1.126	1933	.3500
1906	.674	1920	1.0194	1934	.4796
1907	.660	1921	.6312	1935	.6427
1908-	.535	1922	.6793	1936*	.4475
1909	.522	1923	.6524	1937	.4475
1910	.542	1924	.6678	1938**	.4275

Figures for 1874-1919 from Warren and Pearson, Gold and Prices, p. 257

Figures for 1920-1929 from Kemmerer Report, pp. 178-181

Figures for 1930-1934 from The China Quarterly, Vol. I, No. 1, September, 1935, Statistical tables, p. 179

Figures for 1935-1938 through courtesy of Bureau of Business Research, University of Toledo

*- Buying price of U. S. Government at New York. It might be well to repeat here that after its phenomenal rise in price silver fell to a price of \$.457 early in 1936.

** - In March the U. S. lowered its buying price to \$.4275. It is charged that this action was designed to punish Mexico for her expropriation of American oil interests.

II

Exchange Values

It is quite obvious that the exchange value of the silver units employed in China varied directly with the fluctuations in the price of silver, for a change in the price of silver represented a change in the par of exchange between gold and silver standard countries. An argument made in the body of this essay bears repetition at this point, namely: that a high or low price of silver is neither an evil nor a good per se, as far as China's monetary system is concerned. Whether either situation is in fact at any given time an evil depends entirely on the level of prices which prevails. The real evil then, is a falling, or a rising price of silver since either condition implies a reaction on prices and monetary transactions which disturbs the existing equilibrium or the tendency to achieve an equilibrium. In an economic world less rigid and controlled the effects might not be so severe; but even at best there must result an instability in the value of China's unit, internally as well as externally, which is a retarding influence on her economic development.

TABLE 2

VALUE OF THE HAIKWAN TAEI IN U.S. GOLD DOLLARS, 1919-1933

<u>Year</u>	<u>Value</u>	<u>Year</u>	<u>Value</u>	<u>Year</u>	<u>Value</u>
1910	\$.66	1918	\$1.26	1926	\$.76
1911	.65	1919	1.39	1927	.69
1912	.74	1920	1.24	1928	.71
1913	.73	1921	.76	1929	.65
1914	.67	1922	.83	1930	.46
1915	.62	1923	.80	1931	.34
1916	.79	1924	.81	1932	.34
1917	1.03	1925	.84	1933	.31

(Jan.-Feb.)*

Figures for 1910-1928 from Condliffe, China Today: Economic, p. 197
 Figures for 1929-1933 from Monthly Returns of Trade, National Government
 of China (first page of each monthly issue)

*-The Haikwan tael was abolished early in 1933.

TABLE 3

VALUE OF THE YUAN DOLLAR IN U.S. GOLD DOLLARS, 1926-1938

<u>Year</u>	<u>Value</u>
1926	\$.5039
1927	.4468
1928	.4614
1929	.4151
1930	.2905
1931	.2224
1932	.2149
1933	.2611
1934	.3378
1935	.3657
1936*	.2971
1937	.293
1938**	.2775

Figures for 1926-1934 from China Quarterly, op. cit., p. 179
 Figures for 1935-1938, Monthly Returns of Foreign Trade of China,
 December issues. 1938 figure is current value (April, 1938).
 The legal rate between the yuan and the Haikwan tael is Ch.\$1.558 = Tl.1

*-The new monetary law of November 3, 1935, established a "par" value
 for the new paper yuan of G\$.2975.

**--This quotation will vary as the U.S. dollar--pound sterling rate varies
 as the yuan is "tied" to the pound.

TABLE 4

VALUE OF THE CUSTOMS GOLD UNIT IN U.S. GOLD DOLLARS

1931-1938

<u>Year</u>	<u>Value</u>
1931	\$.405
1932	.388
1933	.504
1934	.658
1935	.671
1936	.677
1937	.667
1938	.682

Figures for 1931-1934 from Monthly Returns of Trade, National Government of China, December issues

Figures for 1935-1938 from Monthly Trade Report: China, United States Department of Commerce, Bureau of Foreign and Domestic Commerce

The customs gold unit had an exchange value equivalent to \$.40 of the former gold dollar. When the United States dollar began to depreciate the value of the Customs gold unit rose accordingly so that its present parity with the United States dollar is slightly above \$.67.

III

Wholesale Prices

TABLE 5

INDEXES OF CHINESE WHOLESALE PRICES, 1913-1937
 NORTH CHINA, SHANGHAI AND CANTON
 (1926 = 100)

<u>Year</u>	<u>North China</u>	<u>Shanghai</u>	<u>Canton</u>
1913	67.2		58.2
1914	66.9		60.3
1915	68.8		65.1
1916	74.2		69.1
1917	80.0		71.7
1918	82.2		75.3
1919	81.1	88.0	77.4
1920	88.9	92.6	77.1
1921	88.9	91.4	81.8
1922	86.4	88.7	85.3
1923	90.4	95.3	89.1
1924	93.6	93.8	94.3
1925	97.4	97.1	100.1
1926	100.0	100.0	100.0
1927	103.0	104.4	100.8
1928	108.0	101.7	96.8
1929	111.1	104.5	96.7
1930	115.9	114.8	101.4
1931	122.6	126.7	112.6
1932	112.9	112.4	113.0
1933	100.6	103.8	102.6
1934	91.8	97.1	94.3
1935	95.5	96.4	84.0
1936	110.6	108.5	105.4
1937 (May)	134.1	125.1	119.8

Figures for 1913-1927 from Franklin L. Ho, Wholesale Prices and Price Index Numbers in North China, 1913 to 1929

Figures for 1927-1934 from The China Quarterly, op. cit., p. 167

Figures for 1935-1937 from Far Eastern Survey, Vol. VI, No. 11, p. 128

Prices had already begun to rise in the summer of 1935 after a steady and disastrous decline when the National government announced the nationalization of silver. Admittedly that action has given a further impetus to a rise in the price level.

TABLE 6
 INDEXES OF WHOLESALE PRICES IN
 NANKING, HANKOW, AND TSINGTAO, 1930-1937

<u>Year</u>	<u>Nanking</u>	<u>Hankow</u>	<u>Tsingtao</u>
1930	100.0	100.0	100.0
1931	106.1	114.5	107.6
1932	100.8	112.4	103.6
1933	92.2	98.9	94.9
1934	80.6	89.0	86.9
1935		89.2	
1936		97.2	
1937 (May)		110.6	

Figures for 1930-1934 from The China Quarterly, op. cit., p. 167

Figures for 1935-1937 from Far Eastern Survey, Vol. VI, No. 11, p. 128

TABLE 7

INDEXES OF CHINESE IMPORT AND EXPORT PRICES
AND BARTER TERMS OF TRADE, 1919-1935
(1913 = 100)

<u>Year</u>	<u>Import Prices</u>	<u>Export Prices</u>	<u>Net Barter Terms</u>
1910	102.6	91.8	111.8
1911	102.3	91.5	111.8
1912	100.1	88.6	113.0
1913	100.0	100.0	100.0
1914	108.9	105.4	103.3
1915	86.4	107.8	80.1
1916	93.6	117.0	80.0
1917	93.5	106.2	88.0
1918	104.9	114.5	91.6
1919	107.2	112.0	95.7
1920	125.4	112.9	111.1
1921	119.5	117.6	101.6
1922	104.4	124.7	83.7
1923	105.2	136.3	77.2
1924	105.3	140.5	74.9
1925	106.9	145.1	73.7
1926	107.7	149.7	71.6
1927	115.6	152.2	75.5
1928	110.5	155.8	71.6
1929	116.0	155.0	74.8
1930	136.4	158.6	72.0
1931	161.8	158.4	102.0
1932	151.0	133.2	113.3
1933	142.5	120.8	117.8
1934	142.3	105.7	134.6
1935	125.6	75.1	167.2

Figures for 1910-1925 from Franklin L. Ho, Index Numbers of the Quantities and Prices of Imports and Exports and of the Barter Terms of Trade, 1887-1928. Figures for 1926-1934 derived from linking Ho's index numbers for 1926-1928 and those of The China Quarterly, op. cit., p. 168. The following method of linking was employed: A ratio was struck of the difference between the figures for respective years of the two index numbers; the geometric mean of these three (1926-1928) ratios was found and this figure was used as a constant by which to multiply each of the Quarterly index numbers. This process was done for import and export prices and the barter terms of trade. The three constants employed were: import prices, 1.0769; export prices, 1.4736; and barter terms of trade, .73047.

Figures for 1935 are unrevised averages of the first ten months of 1935 based on statistics in The China Quarterly, op. cit., p. 169, and the United States Monthly Trade Report: China, February-December, 1935

IV

Specie Flow

TABLE 8

NET FLOW OF GOLD AND SILVER TO OR FROM CHINA, 1900-1937

(millions of Chinese dollars)

<u>Period</u>	<u>Net Gold Flow</u>	<u>Net Silver Flow</u>	<u>Net Total Flow</u>
1900-09	- 5.9	- 63.0	- 68.9
1910	- 0.6	14.4	13.8
1911	1.0	24.9	25.9
1912	5.6	14.3	19.9
1913	- 1.0	26.3	25.3
1914	- 8.7	- 9.1	- 17.8
1915	- 10.8	- 11.4	- 22.2
1916	9.3	- 22.7	- 13.4
1917	9.1	- 21.7	- 12.6
1918	- 1.4	29.6	28.2
1919	57.2	73.8	131.0
1920	- 21.7	114.9	93.2
1921	- 12.6	24.6	12.0
1922	3.4	32.8	36.2
1923	- 4.5	53.7	49.2
1924	- 8.0	21.1	13.1
1925	- 0.3	52.5	52.2
1926	- 5.8	40.4	34.6
1927	- 0.9	44.9	44.0
1928	4.4	75.5	79.9
1929	- 1.3	67.7	66.4
1930	- 7.6	30.9	23.3
1931	- 10.9	15.5	4.6
1932	- 23.8	8.3	- 15.5
1933	- 17.9	- 3.7	- 21.6
1934	- 17.2	- 88.4	-105.6
1935	- 38.8	- 59.4	- 98.2
1936	- 40.7	-249.6	-290.3
1937	- 58.5	-398.5	-457.0
Total Net Flow			
1900-1937	-237.9	-161.4	-399.3

The sign (-) indicates a net export; the absence of any sign, a net import.

Figures for 1900-1932 from Leong, Silver, p. 11

Figures for 1933-1937 from Monthly Returns of Trade, December issues

For the years since 1934 the above figures cannot be considered adequate or complete because of the smuggling operations stimulated by export restrictions. Estimates have been various but it seems safe to say that if the registered flow of specie since 1934 was increased by 25% a closer approximation of the net flow would be achieved.

Foreign Trade

The following tables represent an attempt to gather together the statistics on the foreign trade of China in the various units that are or have been used. Table 13 summarizes these trade figures by showing the index numbers for Chinese foreign trade in all units.

TABLE 9

FOREIGN TRADE OF CHINA IN MILLIONS OF U.S. DOLLARS, 1910-1937

<u>Year</u>	<u>Imports</u>	<u>Exports</u>	<u>Import Balance</u>	<u>Total</u>
1910	306	251	55	557
1911	307	245	62	552
1912	350	274	76	624
1913	416	294	122	710
1914	381	239	142	620
1915	282	260	22	542
1916	408	381	27	789
1917	566	477	89	1,043
1918	699	612	87	1,311
1919	900	877	23	1,777
1920	945	672	273	1,617
1921	689	457	232	1,146
1922	784	544	240	1,328
1923	739	602	137	1,341
1924	825	625	200	1,450
1925	797	652	145	1,449
1926	854	657	197	1,511
1927	698	634	64	1,332
1928	850	704	146	1,554
1929	819	657	162	1,476
1930	592	404	188	996
1931	498	316	182	814
1932	350	165	184	514
1933	351	158	193	509
1934	348	181	167	529
1935	336	200	136	536
1936	279	210	69	489
1937*	264	229	35	493

Figures for 1910-1928 from Condliffe, op. cit., pp. 196-97
 Figures for 1929-1937 converted from yuan dollars at yearly average
 rates of exchange.

*-For eleven months only

TABLE 10

FOREIGN TRADE OF CHINA IN MILLIONS OF HAIKWAN TAELS, 1910-1932

<u>Year</u>	<u>Imports</u>	<u>Exports</u>	<u>Import Balance</u>	<u>Total</u>
1910	463	381	82	844
1911	472	377	95	849
1912	473	371	103	844
1913	570	403	167	973
1914	557	345	212	902
1915	454	419	36	873
1916	516	482	34	998
1917	550	463	87	1,013
1918	555	486	69	1,041
1920	647	631	16	1,278
1921	762	542	220	1,304
1922	906	601	305	1,507
1923	945	655	290	1,600
1924	923	753	170	1,676
1925	1,018	772	246	1,790
1926	948	776	172	1,724
1927	1,124	864	260	1,988
1928	1,013	919	94	1,932
1929	1,196	991	205	2,087
1930	1,266	1,015	251	2,281
1931	1,310	895	415	2,205
1932	1,434	909	525	2,343

Figures for 1910-1928 from Condliffe, *op. cit.*, pp. 196-97

Figures for 1929-1931 from *China Year Book, 1932*, p. 143

Figures for 1932 converted from yuan dollar figures at average rate of exchange between the two Chinese units.

In April, 1933, the Haikwan tael was officially abolished and the yuan dollar established.

TABLE 11

FOREIGN TRADE OF CHINA IN MILLIONS OF CUSTOMS GOLD UNITS
1931-1937

<u>Year</u>	<u>Imports</u>	<u>Exports</u>	<u>Import Balance</u>	<u>Total</u>
1931	1,231	773	458	2,005
1932	903	420	483	1,322
1933	697	314	383	1,010
1934	529	272	256	801
1935	501	417	84	918
1936	312	306	6	618
1937*	396	344	52	740

Figures from Monthly Returns of Trade, December issues. Yuan exports converted to gold units at yearly average values by writer.

*-For eleven months only

TABLE 12

FOREIGN TRADE OF CHINA IN MILLIONS OF YUAN DOLLARS, 1926-1937

<u>Year</u>	<u>Imports</u>	<u>Exports</u>	<u>Import Balance</u>	<u>Total</u>
1926	1,752	1,347	405	3,098
1927	1,578	1,431	147	3,009
1928	1,863	1,545	319	3,408
1929	1,972	1,588	390	3,555
1930	2,041	1,394	646	3,435
1931	2,333	1,417	816	3,650
1932	1,635	768	867	2,402
1933	1,346	612	734	1,957
1934	1,030	535	494	1,565
1935	919	576	343	1,495
1936	942	706	236	1,648
1937*	901	783	118	1,684

Figures for 1926-1934 from The China Quarterly, op. cit., p. 169

Figures for 1935-1937 from Monthly Returns of Trade, December issues.

Import figures converted from gold units at yearly average values by writer.

Although the yuan was not officially adopted until 1933 trade statistics of years before that date are given in terms of yuan, having been converted from Haikwan tael figures by the Chinese government.

*-For eleven months only

TABLE

SI INDEX NUMBERS OF THE FOREIGN

(in units
1913)

Year	U. S. Dollars (1)			Total	Physical Units (2)	
	Imports	Exports	Balance**		Imports	Exports
1910	73.6	85.4	45.1	78.2	79.2	102.9
1911	73.8	83.3	50.8	77.7	81.0	102.1
1912	84.1	93.2	62.3	87.9	82.9	103.9
1913	100.0	100.0	100.0	100.0	100.0	100.0
1914	91.6	81.3	116.4	87.3	91.6	83.8
1915	67.8	88.4	18.0	76.3	92.1	96.5
1916	98.1	129.6	22.1	111.1	98.6	102.4
1917	136.1	162.2	73.0	146.9	103.1	108.3
1918	168.0	204.8	71.3	184.6	92.8	105.5
1919	216.3	298.3	18.9	250.3	105.9	140.1
1920	227.2	228.6	237.8	227.7	106.5	119.4
1921	165.6	155.4	190.2	161.4	132.9	127.0
1922	188.5	185.0	196.7	187.0	158.5	130.6
1923	177.6	204.8	112.3	188.9	155.0	137.4
1924	198.3	212.6	163.9	204.2	170.8	144.8
1925	191.6	221.8	118.9	205.5	157.0	140.9
1926	205.3	223.5	161.5	212.8	186.7	149.6
1927	167.8	215.6	52.5	187.6	157.2	183.4
1928	204.3	239.5	119.7	218.9	188.3	165.5
1929	196.9	223.5	132.8	207.9	199.5	149.0
1930	142.3	137.4	154.1	140.3	186.7	130.9
1931	119.7	107.5	149.2	114.6	190.7	131.2
1932	84.4	56.1	150.9	72.4		
1933	84.4	53.7	158.2	71.7		
1934	83.7	61.6	136.9	74.5		
1935	79.6	68.0	114.1	75.5		
1936	67.1	71.4	56.6	68.9		
1937*	63.5	77.9	28.7	69.4		

*-For first eleven months only

**-Balance in all cases is an excess of imports

(1)-Index numbers made by writer from data in Table 9.

(2)-From Franklin Ho, Index Numbers, and Leong, Silver, the latter numbers being converted to present base year by writer.

13

TRADE OF CHINA, 1910-1937

indicated)
= 100

Haikwan Taels-Yuan Dollars #(3)				Customs Gold Units (4)			
Imports	Exports	Balance**	Total	Imports	Exports	Balance**	Total
81.2	94.6	49.1	86.7				
82.8	93.5	56.9	87.3				
83.0	92.1	61.7	86.7				
100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
97.7	85.6	126.9	92.7				
79.6	104.0	21.6	89.7				
90.5	119.6	20.4	102.6				
96.5	114.9	52.1	104.1				
97.4	120.6	41.3	107.0				
113.5	154.1	9.6	131.3				
116.1	134.5	126.3	134.0				
158.9	149.1	177.2	154.9				
165.8	162.5	168.3	164.4				
161.9	186.8	101.8	172.3				
178.6	191.6	141.3	184.0				
166.3	192.6	103.0	177.2				
197.2	214.4	155.7	202.3				
177.7	228.0	56.3	198.6				
209.8	245.9	116.8	214.5				
222.1	251.9	150.3	234.5				
229.8	222.1	243.5	226.6				
251.6	225.6	314.4	240.8	118.4	105.2	150.0	113.0
180.5	120.3	331.7	152.1	86.8	67.1	158.4	74.6
151.6	97.5	282.3	129.1	67.0	42.7	125.6	56.9
116.0	85.2	190.0	103.2	50.9	37.0	83.9	45.1
103.5	91.7	131.9	98.6	48.2	56.7	28.2	52.3
106.1	112.5	90.8	108.7	30.0	41.6	2.0	35.2
101.5	124.7	45.4	111.1	38.1	46.8	17.1	42.2

(Mythical base year figures
derived from U. S. dollar
figures at par of exchange
for the C.G.U.: \$.40.)

#-Since both the Haikwan tael and the yuan dollar are fixed silver units they have the same index numbers.

(3)-Index numbers made by writer from Tables 10 and 12.

(4)-Index numbers made by writer from data in Table 11.

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