

**CONSTRUCTING A NATIONAL *OIKONOMIA*:  
CHINA'S GREAT MONETARY  
REVOLUTION, 1942-1950**

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# CONSTRUCTING A NATIONAL *OIKONOMIA*: CHINA'S GREAT MONETARY REVOLUTION, 1942-1950

HUANG Yanjie\*

*Renminbi*, more widely known in the world today as the Chinese Yuan, was a fiat money issued by the People's Bank of China (PBOC) in December 1948. At the point of its inception, few people were sure about its fate, since the two preceding fiat paper moneys under the Kuomintang (KMT), *fabi* and *Gold Yuan*, had both lost more than 99.999% of their initial values when they were officially abolished by the KMT government. *Fabi* had been in print for barely 13 years and *Gold Yuan*, only 10 months. However, *renminbi* turned out to be remarkably stable and long-lasting. During the three decades between 1950 and 1978, the consumer price index increased by a mere 44%, implying that the new currency lost only 30% of its initial value in almost three decades.<sup>1</sup> This record price stability would certainly rank the *renminbi* between the 1950s and 1970s as one of the most stable fiat currencies in modern times.

In a sense, it is fair to say that China underwent a monetary revolution between the late 1940s and early 1950s, when a hyper-stable *renminbi* replaced the old *fabi* and many local currencies as the sole national money. Meanwhile, a new system of money, trade and credit became the macroeconomic superstructure of a new national economy. Thereafter, this system became an integral part of Soviet-styled planned economy. China's socialist planned economy itself however was unable to account for the revolutionary success of the *renminbi*.<sup>2</sup> The Soviet-styled planned system was not set up until 1953 before it was severely dislocated during the Great Leap Forward (1958-1961) and Cultural Revolution (1966-1976). But the *renminbi* price level was relatively steady both before 1953 and during the entire Cultural Revolution. Even in the years of the Great Leap Forward, inflation rates could be regarded as high only in the year of 1960, indicating a temporary policy measure rather than a fundamental institutional change.<sup>3</sup> The reasons behind *renminbi*'s hyper-stability must be sought elsewhere.

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<sup>1</sup> National Bureau of Statistics: *Xinzhongguo liushinian tongji huibian* (A Collection of Sixty Years' of Historical Statistics of the People's Republic of China), Beijing: China Statistical Press, 2010, p. 21.

<sup>2</sup> For a historical account of the introduction of the Stalinist model to China's economic institutions, refer to Li Hua-yu, *Mao and Economic Stalinization of China*, Lanman MD.: Rowman & Littlefield, 2006.

<sup>3</sup> For a detailed study of Communist monetary policy in the Great Leap Forward years, refer to Hsiao, Catherine Y.H. Huang, *Money and Monetary Policy in China*, NY: Columbia University Press, 1971.

Although economists and historians have long examined money and banking in Communist China as a unique subject, their primary interests were mainly theoretical and their theoretical paradigm restricted to the planned economy. Early works on the Communist monetary system and political economy in general focused predominantly on state control and the planned economy framework without discussing the Communist economy's continuity with wars and inflations since the 1940s.<sup>4</sup> In recent years, some authors have noticed the uniqueness of the Communist "economic warfare" in the 1950s but they have not examined the historical roots of the new system.<sup>5</sup>

Compared to the works of economists and sociologists, recent historical studies on fiscal and monetary systems in early Communist China have tended to move away from ideological frameworks and focus on the actual socioeconomic context of the late 1940s and early 1950s.<sup>6</sup> These recent works have relied massively on newly available materials, including original documents, memoirs and writings of the principal financiers. It is primarily inspired by these new historical studies and based on these new materials that this paper attempts to reconstruct the evolution of the Communist monetary system from its inception during the Sino-Japanese War to the early days of the People's Republic.<sup>7</sup>

This paper will seek to explore the origins and evolutions of the Communist fiat paper money as a system and draw some initial inquiry about the nature and implications of the Communist monetary system. As this paper shall demonstrate, the

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<sup>4</sup> Dwight Perkins discussed the CCP anti-inflation policy in his classic *Market Control and Planning in Communist China*; Solinger also offered an extensive discussion of the ideology and rationale of market control and low inflation in a Communist economy. Her introductory chapter of *Business under Socialism* briefly discussed the monetary system in China as a Soviet-styled planned economy. Donnithorne provided a more thorough discussion of the monetary regime in *China's Economic System*, but again her discussion was primarily concerned with China having a variant of Soviet-style communist economic system. The most comprehensive treatment of the Chinese monetary system was perhaps Catherine Y.H. Huang's *Money and Monetary Policy in China*. But the analyses were essentially a technical treatment that focused on the economic and institutional aspects of the monetary system as a socialist monetary system with little reference to the pre-1953 and pre-1949 periods.

<sup>5</sup> The most notable example is Richard Burdekin, who has written several important papers on inflation in mainland China and Taiwan since the early 1950s. The most comprehensive and historically informed discussion of China's monetary system can be found in his paper *Ending Inflation in People's Republic China: From Chairman Mao to the 21st century*. But his interest was still technical and the paper did not address the development of the monetary system in the 1940s.

<sup>6</sup> In recent years, Japanese scholars have taken the lead in this field. Okumura Satoshi has provided the most systemic works so far about China's economic transition in the 1940s and early 1950s from a non-ideological perspective in his works on China's wartime mobilisation, institutional change and market integration in the 1940s. Notable examples include Izutani Yoko (state-contract), Yugi Sasagawa (grain procurement) and Kato Jun (fiscal structure). A work by a mainland historian, Chi Aiping, recorded the first year of the Central Finance Commission in great detail. But like many Chinese works, the monograph was marred by the one-sided official ideology of PRC Party history school and focused exclusively on the achievements of the CFC and its key figures.

<sup>7</sup> The primary source for this study is the multivolume *Zhonghuarenmingongheguo Jingji Danganziliao Xuanbian, 1949-1953* (PRC Selected Economic Archives) published in the 1990s. It is the most comprehensive collection of primary resources on the Chinese economy in the period published to date.

Communist monetary system predated and in fact, precipitated the introduction of a Soviet-style planned system. The new money's resistance to inflation was rooted not in the planned system, but in the Communist state's ability to peg the value of the *renminbi* to a basket of key commodities at the disposal of state commercial and industrial organs. This new approach was essentially an institutional innovation the Communists brought along from their experiences of economic struggles in predominantly rural agrarian economies in the revolution bases, in particular, pre-1945 Shandong and the Manchuria area during the Civil War. In analysing its origin and development, we can evaluate its strengths and weaknesses, which would only manifest later when it was extended from tiny rural economies to the whole of China.

### **The Development of the Material Standard, 1942-1948**

#### *Economic Struggles in Revolution Base Area: the Shandong Experience*

Although the idea of fiat money based on the control of goods markets was already in existence in the 1920s and 1930s, it was not practised by any major political forces. The country was largely characterised by monetary anarchy with a loosely defined silver standard as the only unifying element across major economic regions.<sup>8</sup> When the Communists initially adopted a fiat currency in Jiangxi Central Soviet Base, all the *Red* banknotes were made redeemable to a fixed quantity of silver coins. But the paper money was soon abandoned in favour of a silver *yuan*, styled after Yuan Shikai's silver *yuan*, after forceful nationalisation of silver in the areas under effective Communist control.<sup>9</sup>

Although these ideas of a material-based money already existed in the 1920s, the first notable practice did not come until the mid 1940s when Xue Muqiao became director of finance bureau in the Shandong Revolution Base Area (*Shandong jie fang qu*, SRBA). Before 1942, the SRBA government used the *fabi* as the main currency supplemented by its own currency (*kangbi*) pegged to the *fabi*. *Fabi* was a preferred currency partly due to the fact that its exchange with the Pound and Dollar was kept relatively stable through China's reserves in London and New York. The Japanese Occupation Authority thus found it useful to keep the *fabi* in circulation and under control by exchanging into international currencies to acquire war materials on the world market.<sup>10</sup> But since the outbreak of Pacific War, the Japanese had begun to illegalize *fabi* from territory under its effective control, dumping hundreds of millions of *fabi* they collected from the local markets in occupied areas in exchange for the much needed war materials. Concerned about the draining of valuable resources from the area under CCP control, the SRBA government decided to end the circulation of

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<sup>8</sup> For a good account of the monetary disunity in the 1920s and 1930s, refer to Tomoko Shiroshima, *China During the Great Depression: Market, State and the World Economy, 1927-1937*, MA Cambridge: Harvard University Press, 2009, chapter 1.

<sup>9</sup> Xing Guang, Feng Tianfu, *Zhongyang Gemin Genjitu Caizheng de Chuangjian he fazhan*, ("Building and Developing Fiscal System in Revolutionary Bases) in *Gemin Genjudi de Caizheng Jingji*, (Fiscal and Economic Affairs in Revolutionary Base Areas), Beijing: Zhongguo Caizheng Chubanshe, 1988, pp.10-11.

<sup>10</sup> Chen Zhijian, "Kangri zhanzheng qijian guomin dang duiwei huobizhan" (Monetary War Between KMT, Japan and Japan-backed Puppet Governments in Sino-Japanese War), in *Jingdaishi Yanjiu* (Study on Modern Chinese History), 1987, vol. 2, pp. 35-37.

*fabi* and began issuing its own currency, *kangbi*, as a means to mobilise material resources in the revolution base.<sup>11</sup>

When *kangbi* was initially issued, its credibility extended to barely one of the six areas of the SRBA in the “war of money”. Apparently, the CCP local governments did not have sufficient control over the goods markets to ensure its control of the price level of necessities but instead resorted to administrative decrees to make *kangbi* legal tender and the use of *fabi* illegal. After the fall of 1943, when the CCP government set up the Bureau of Industrial and Commerce (*gong shang ju*), the organisation responsible for “economic struggles”, the situation improved significantly. Under this new agency, three fronts of the struggle, namely money, trade and production, would be coordinated under the provincial CCP government to achieve a unified goal, that is, the establishment of a stable currency regime in the whole area.

From late 1943 to mid 1945, the SRBA Bureau of Industry and Commerce performed its duty quite successfully. In less than two years, the rising trend in market price was reversed in the ever-expanding *kangbi* market. The trade department of the bureau worked actively to buy and sell a variety of necessities. Typically, half of the *kangbi* issued were to purchase important strategic materials, such as grain, cotton, cloth and peanuts. Most of the other *kangbi* issued were used to support production, in the form of small loans to agricultural households and government self-sufficient production units (since the Japanese put an embargo on some necessary goods). In Xue’s own view, sustained production growth would yield increasing amount of materials to be employed as reserves.<sup>12</sup>

In the year 1944, *kangbi* struck a decisive victory against its rival currencies. One of the key factors was the deterioration in military situations for the KMT during Operation Ichi-Go, and Japan’s defeat at the Pacific islands. In that year, the supply of the *kangbi* expanded 100-200%, but the population of the monetary area increased by 200-300%.<sup>13</sup> Consumer price index fell and the local communist government was able to issue even more *kangbi* to capture the ever expanding market since the later half of 1944.

Since the SRBA had very small reserves of hard currency, the success of the new system was dependent on trade surpluses and centralised management of foreign currencies (*fabi* and *weibi*) earned from trade. This was achieved by a salt monopoly, obtained from the salt production base in Shandong. As the classical item for state revenue in the imperial era, salt was again harnessed by the local CCP government in Shandong as the means to secure a stable trade surplus and all foreign currencies earned from exporting salt were duly registered and deposited in the Red Banks. The

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<sup>11</sup> Xue Muqiao, “Shandong Kangri Genjudi de duidi huobi dongzheng” (Monetary Struggle in Shandong Anti-Japanese Base Area), in *Kangrizhenzheng he jiefangzhenzheng Shiqi de shandong jiefangqu de jingjigongzuo* (Economic Work in Shandong Liberated Area during Sino-Japanese and Civil Wars), Jinan: Shandong Renmin Chubanshe, 1982, pp.170-171.

<sup>12</sup> Ibid, pp.175-177.

<sup>13</sup> Xue Muqiao, “Shandong Gongshang Guanli Gongzuo de fangzhen yu zhengce” (Policy and Guideline for Shandong Industrial and Commercial Work), in “*Kangri zhenzheng he jiefangzhenzheng shiqi de shandong jiefangqu de jingjigongzuo*” (Economic Work in Shandong Liberated Area during Sino-Japanese and Civil Wars), Jinan: Shandong People’s Publishing House, 1982, pp. 222-224.

surplus was further secured by encouraging production and exports of edible peanut oil, another Shandong specialty. Besides, the SRBA governments obtained much of their indirect tax from the sales of salt.

The SRBA was so successful in its “monetary struggles” that Xue Muqiao’s report on his experiences was widely circulated in both Shandong and other base areas. Xue’s experience was rendered more valuable by the fact that money struggles in other base areas had mostly failed to achieve similar success.<sup>14</sup> This was no doubt an important milestone in Xue’s career in the CCP financial bureaucracy. When asked by an American journalist about his success, Xue argued that the SRBA actually practised a *material standard* (*wu zhi ben wei*) rather than a Gold or Silver Standard (*jin yin ben wei*), which was based on a reserve ratio of about 50% between the material reserve and the money supplied as purchasing power.<sup>15</sup> As one of the first cases of fiat paper currencies purely based on materials, Xue’s experience in Shandong was to become the preamble to Communist monetary strategy during the Chinese Civil War and later in the post-liberation era in the early 1950s. Xue’s own personal involvement in policy making was also evident. Since 1947, Xue had served as acting executive member in the Economic and Finance Department of CCP’s North China Finance Office, and eventually, in the Central Financial Commission (CFC, *zhong cai wei*), as top policy-maker for trade and financial policies.<sup>16</sup>

But the SRBA experience also had its limitations. The economic struggles in SRBA were carried out in an agrarian economy where the market was largely complementary to household in the production and circulation of most daily necessities (salt and peanut edible oil being the prominent exceptions). As a result, production directly served consumption and the functions of money were restricted to a stable medium for simple exchanges and short-term agricultural credits. In other words, the size and structure of the agrarian market provided the institutional conditions for the *material standard*. Moreover, for the particular case of SRBA between 1943 and 1945, the CCP local government had the added advantage of not being burdened by a heavy military budget and the need to provide for a large civilian bureaucracy and urban residents.<sup>17</sup> As we shall discuss later, the *material standard* and its variant would undergo significant changes as it encountered more complex economic systems, first in the North East and then in post-civil war mainland China.

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<sup>14</sup> Although other base areas adopted similar practices, the Shandong experience stood out in three aspects. First, it was the most theoretised experience based on the work of Xue. Second, Shandong achieved relative price stability with freedom of internal commerce and minimal intervention of state power as in the organised opium production and traffic in Shanxi-Gansu-Ningxia region. Third, the Shandong *kangbi* successfully became a centralised currency that covered a relatively large area and population among some 600 currencies issued by Communist local authorities during the Sino-Japanese war.

<sup>15</sup> Xue Muqiao, *Xue Muqiao Huiyilu* (The Memoir of Xue Muqiao), Tianjin: Tianjin People’s Press pp. 170-171.

<sup>16</sup> *Ibid*, pp. 188-190.

<sup>17</sup> Xue Muqiao, “Shandong Jiefangqu de Caijing Gongzuo” (Shandong Jiefangqu caizheng jingji gongzuo), in *Kangri zhenzheng he jiefangzhenzheng shiqi de shandong jiefangqu de jingjigongzuo*, (Economic Work in Shandong Liberated Area during Sino-Japanese and Civil Wars), Jinan: Shandong Publishing House, 1982, pp. 16-17.

## *The Evolution of New Money: the Manchurian Experience*

The North East Liberated Area (*Dongbei jie fang qu*, NELA) was an extended and growing area in Manchuria (China's northeast provinces of Liaoning, Jilin and Heilongjiang of today) under CCP control during the CCP-KMT Civil War (1946-1949). The CCP controlled the whole of the northern and rural heartlands in the southern part of Manchuria during most times in the Chinese Civil War. At the time of the CCP's arrival in late 1945, the region was well endowed with natural resources, heavy industry and other economic infrastructure like railways. Despite the rampage of the Soviet army, the region was still not only an important base for agricultural production but also one of the most industrialised areas in China.

In recognition of the strategic significance of this region, the CCP formally devised a strategy to transform Manchuria into a firm base for the Revolution in its Seventh Party Congress held in Yan'an in early 1945. Chen Yun, the one-time head of the powerful Organizational Department and a veteran leader of the CCP financial committee in the Shaanxi-Gansu-Ningxia RBA, was selected as a key member in the team and person-in-charge of fiscal and financial affairs in the would-be NELA.

As with the Shandong experience, the economic programmes of the NELA encountered tremendous difficulties in the first two years. The military situations were not in favour of the CCP since the KMT army had captured all major cities along the railway, controlling up to 29% of the areas and 53% of the population in Manchuria. Unlike in SRBA, the CCP government in Manchuria was burdened with heavy military spending (more than 80% of the budget) and the need to feed mobilised personnel who accounted for five to six per cent of the total population.<sup>18</sup> As the war continued, there were the additional tasks of revitalising the war-torn economy and providing for urban residents in newly conquered areas. The fiscal burden was considerably heavier than that in the SRBA.

When CCP banks first issued their first fiat *dongbeibi* in the NELA in November 1945, its rival was the Manchukuo currency *manzhoubi*. As the example of Heilongjiang province demonstrates, the market was still dominated by *manzhoubi* (40%), the Soviet army coupon (30%), the KMT local provincial currencies (20%) and foreign currencies of Japan and Korea (five per cent) until early 1946.<sup>19</sup> But the *manzhoubi* soon lost its footing during the KMT advancement in early 1946. Since the Soviet withdrawal and the outbreak of the civil war in Manchuria, the "war of money" had largely been fought between KMT-backed *dongbei jiushengquan* and the *fabi* on the one side and the various banknotes issued by CCP local banks (collectively known as *dongbeibi*) on the other side.

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<sup>18</sup> Li Liurui, "Guanyu caizheng wenti de jielun baogao" (Concluding Report on Fiscal Matters), in *Dongbei Jiefangqu Caijing Shiliao Xuanbian (NELA Selected Economic and Fiscal Archives)*, Harbin: Heilongjiang Renmin Chubanshe, vol. 1, p. 28.

<sup>19</sup> Hejiang Provincial Branch of North East Bank: "1946 Nian Gongzuo Baogao" (Work Report of the Year 1946), in *Dongbei Jiefangqu Caizheng Jingji Shigao (Economic and Financial History of the NELA)*, Harbin: Heilongjiang Renmin Chubanshe, pp. 342-343.

By late 1947, it was clear that the CCP authorities had gained the upper hand in the monetary struggles by keeping the values of their currencies more stable than that of their KMT rivals. The key to successes was to keep private speculations at bay by trading daily necessities at low prices. The most decisive struggles between the CCP government and the speculators were carried out by the General Trade Bureau (*mao yi zong ju*) in Harbin, the only large city controlled by the CCP before 1948. Applying the Shandong experience, the trade bureaus sought to dump materials (cotton cloth in this case) from state stores into the free market. This trade system initially worked well to keep prices stable.<sup>20</sup>

However, the bureau officials soon recognised the disadvantages of such a policy, as hot money was unexpectedly more flexible and easily mobilised than materials. Bureau officials realised that a change in policy was urgently required.<sup>21</sup> In the later half of 1947, Harbin Trade Bureau officials found a way to circumvent the market via direct transactions with peasant households through the CCP's powerful rural grassroots organisations. In the classic case of cotton cloth, the procurement agents in Harbin simply supplied the raw material, cotton, to the weaving women in the countryside, and collected the finished products directly from them to secure a cheap supply later.<sup>22</sup> In this way, the government effectively organised a putting-out system for cloth in rural areas around Harbin. The trade policy accordingly shifted from “free trade and massive dump” to “controlling both raw materials and finished products”. But as a side effect of this new policy, private trade was severely hurt and the number of private merchants decreased by 60% in five months.<sup>23</sup>

The experience with controlling grain supply in Harbin tells a similar story. From the beginning, the CCP had been keenly aware of the centrality of grain in price stability and set up an independent organisation, the Dongxing Company, as its grain procurement agent. About half of the grain was supplied to urban residents through the company's retail outlets at a price 25-33% lower than the black market. This deliberate low-price policy was facilitated by the success of land reforms which destroyed most organised resistance to the Communist state in Manchuria.<sup>24</sup> But unlike the case of cotton cloth, the Commission had not implemented an outright monopoly but allowed private merchants to operate as *tiaoji* (adjustment mechanism) to balance prices across localities.<sup>25</sup>

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<sup>20</sup> Zhu Jingzhi, Liu Mingfu, “Harbinshi Wujia Wenti Zongjie”, (Summary on Price Problem in Harbin City) in *NELA Selected Economic and Fiscal Archives*, vol. 3, Harbin: Heilongjiang Renmin Chubanshe, p. 48.

<sup>21</sup> Ibid, p. 52.

<sup>22</sup> Ibid, p. 54

<sup>23</sup> Ibid, p. 56

<sup>24</sup> Hejiang Provincial Government: “Hejiangshen guanyu gouliang gongzuo de Zongjie” (Hejian Province Review on Grain Procurement Work), *NELA Selected Economic and Fiscal Archives*, vol. 3, p. 20.

<sup>25</sup> North East Finance Commission: Dongbei zhengwei guanyu jiefangqu nei maoyiziyou de jue ding” (Decision on Trade Liberalization in the NELA), *NELA Selected Economic and Fiscal Archives*, vol. 3, p. 40.

Ironically, speculations lasted longer than expected. The North East Finance Commission (NEFC) soon realised that the commercial activities of *xiaogong*, namely local public organisations such as government agencies, state-owned factories, public schools and army logistics units, were also a main source of speculation. A trade bureau report noted that the regulation of *xiaogong* would be a principal task of the trade bureau.<sup>26</sup> This prompted the NEFC to centralise the fiscal administration of different work units and departments. On 1 March 1948, a General Account Office (GAO) was established under the Commission. All public fiscal units were required to deposit their cash in the treasury of GAO, whereby their expenditures would be disbursed by the GAO in the form of materials wherever possible.<sup>27</sup> The fiscal and monetary centralisation experience provided visible examples for later fiscal centralisation on a much larger scale.

With the capture of Shenyang, the last KMT garrison in Manchuria, on 2 November 1948, the NELA was finally extended to the whole of Manchuria. But the extension of liberated areas also caused the problem of significant budget commitments to the KMT captives and large number of urban residents. Consequently, the NEFC had to bear with high inflation and a precarious fiscal structure, where the majority of fiscal revenue consisted of grain tax and profits of state-owned factories.<sup>28</sup> Due to the overwhelming importance of grain, all fiscal revenues were accounted in terms of mille grain. But in spite of all these fiscal woes, the NELA achieved its monetary and fiscal unification by the end of 1948 when the Commission unified all 16 currencies, imposed cash controls and further reined in extra-budgetary expenditure of public units.<sup>29</sup> Moreover, the NELA currency did much better than its rivals, *jiushengquan* and *fabi*. The price index in terms of *dongbeibi* went up 20 times between 1947 and 1949, while that of its rivals, went up a few hundred million times before they were driven out of circulation.

The lessons of the NEFC experience are multifold. The NELA was significantly larger than SRBA both in size and population; the economic and fiscal challenges for the CCP were also much greater and more complex. Apart from the lessons of state trade, control over supply and fiscal centralisation, the NELA experience also set the rule of the thumb for issuing new money in large economic regions with both urban and rural sectors. In 1948, the *dongbeibi* issued was distributed in the following manner: 49% went to support the fiscal budget, 28% went to the trade bureaus to build their material reserves and the rest went to support production.<sup>30</sup> The experiences emerged as a nationwide template, as leading NEFC

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<sup>26</sup> Wang Shoudao, “Dangqian Caijing gongzuo de fangzhen yu renwu” (Brief on Current Fiscal and Economic Works), *NELA Selective Economic and Fiscal Archives*, vol. 4, pp. 21-23.

<sup>27</sup> Zhu Jianhua, *Dongbei Jiefangqu Caizheng Jingji Shigao* (Economic and Fiscal History of the NELA), Harbin: Heilongjiang People’s Publishing House, 1987, p. 437.

<sup>28</sup> Ministry of Finance of the Administration Commission: “Dongbei Jiefangqu Caizheng Baogao, 1947-1948”(Fiscal Report of the NELA), *NELA Selected Economic and Fiscal Archives*, vol. 4, p. 128.

<sup>29</sup> *Ibid*, p. 130.

<sup>30</sup> Zhu Jianhua, *Dongbei Jiefangqu caizheng Jingji Shigao* (Economic and Fiscal History of the NELA), Harbin: Heilongjiang Renmin Chubanshe, 1987, p. 441.

financiers like Chen Yun and Li Fuchun became the heads of the finance authority for the whole of China after the liberation.

### Construction of a New Money Regime, 1949-1950

#### *Coping With Hyperinflation*

The fiat currency of the KMT had already collapsed in September 1948 when the Communist force stood to take the whole of the northeast. In the last two years of the monetary struggle, the KMT did not have the capacity to mobilise materials in a similar way as the CCP, nor did it succeed in building a sustainable fiscal capacity to finance the war. This fatal weakness resulted in the spectacular inflation spiral from 1945 to 1948, during which the *fabi* depreciated to less than one thousandth of its initial value in less than three years.<sup>31</sup> When CCP troops took over Shanghai, the *Gold Yuan* had only 0.001% of its initial value in August 1948.<sup>32</sup> Due to its rapid depreciation, *Gold Yuan* was effectively taken out of circulation and replaced by silver, foreign currencies and goods-for-barter in July 1949.

The first challenge posed by hyperinflation to the CCP was the need to establish a viable new currency. Just as the NELA local authority was unifying its own currency, the party centre ordered the unification of all other currencies in north China. On 1 December 1948, the People's Bank of China (PBOC), formed by merging three regional banks, began to issue a new currency, *renminbi*, to replace the four principal CCP regional currencies across liberated areas in northwest, northeast (Shandong) and north China (Hebei and Shanxi).<sup>33</sup>

As the CCP troops marched to take China's key economic regions in the Yangtze River Delta in spring 1949, the government was also busy with instituting the *renminbi* to replace the *Gold Yuan*, silver, gold and foreign currencies in circulation. The *Gold Yuan*, largely driven out of market, was easily retrieved by the local branches of the PBOC. But the replacement of gold and silver proved much more difficult. Despite the Communist take-over, silver *yuan* effectively prevented the fiat *renminbi* from taking hold of the economy in Shanghai and its surrounding urban areas. Two weeks after the liberation, the *renminbi* lost 91% of its value in terms of silver coins and the general price level increased by 170% in Shanghai.<sup>34</sup> The Shanghai Party Committee suffered a surprise attack from the speculators, when its strategy of dumping silver reserves in the market failed to hold speculations in check.

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<sup>31</sup> Gia-ngau Chang, *The Inflation Spiral: The Experience of China, 1937-1950*, Cambridge: The MIT Press, 1963, pp. 87-88.

<sup>32</sup> PBOC General Office: "Jiuzhongguo Changqi de Tonghuopengzhang" (Long-term Inflation in Pre-liberation China), *People's Republic of China Selected Economic Archives (1949-1952), Financial Volume (SEAF)*, Beijing: Zhongguo Wuzi Chubanshe, 1995, pp. 3-4.

<sup>33</sup> PBOC General Office: "Guanyu Tongyi Huadong, Huabei, Xibei Huobi de Baogao" (Report on Currency Unification in East, North and Northwest regions), in *SEAF*, pp. 28-29.

<sup>34</sup> PBOC Shanghai Branch, "Huadong Jiefangqu Fanyinyuan Douzheng Jiyao" (Account of the Struggle against Silver Yuan in Eastern China Liberated Areas), *Shanghai Financial Monthly*, vol. 1, No. 7, Sep 1949, in *SEAF*, p. 179.

In response to the surprise speculative attack, the CFC reversed its relatively benign market-based approach in favour of an all-out war against the silver *yuan*. In early June 1949, Chen Yun was sent to Shanghai to guide the operation in person. On 10 June, 1,000 PLA soldiers and 200 police dressed in civilian clothes seized the Shanghai Exchange, arresting 238 speculators and confiscating 30,000 silver coins and 3,000 taels of gold on the spot.<sup>35</sup> After the financial exchanges were closed down, speculators shifted their targets to commodities. The commodities of their choice were two black (grain and coal) and one white (cotton), the most important staple goods in China's urban markets. The Central Finance Commission under Chen Yun initially responded with the dumping of local grain and cotton reserves. But when speculators hit back again in November 1949, the CFC decided on a massive mobilisation of materials. In less than two weeks, the CFC transported via railway almost one million tons of grains mostly from the NELA (0.5% of the yearly harvest, three per cent of the total grain at the government's disposal) and more than two million bolts of cotton cloth from all liberated territories to major urban markets.<sup>36</sup> In December, the rate of growth in price was halted and the key prices of grain and cotton cloth were eventually held down in March 1950.<sup>37</sup>

Another urgent policy of the new government was to establish effective financial and fiscal instruments to retrieve the money supplied. Following CFC instructions, the People's banks promptly implemented a materialised saving system (*zhe shi cun kuan*), which pledged to repay the depositors principals and interests in daily necessities.<sup>38</sup> From June 1949 to December 1949, the materialised savings increased 15 times at state banks in Shanghai.<sup>39</sup> In December, shortly after the second wave of speculation, the Zhengwuyuan (Administration Council of Government) decided to issue 200 million units of a materialised public bond in 1950.<sup>40</sup> In line with material-based approach towards currency speculation, these emergency fiscal measures required extensive material mobilisation within a much longer time span.

As the currency took hold in the urban market, market exchanges in rural heartlands in central and southern China were still primarily based on silver coins and various money substitutes, whereas some remote markets even went back to barter trade. The *renminbi* had to penetrate the rural market in order to survive the first few months. In most regions, party committees sent hundreds of work teams to the countryside to persuade the peasants to exchange their primary goods and silver coins

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<sup>35</sup> Ibid, p. 183.

<sup>36</sup> Chen Yun, "Guanyu Wujia de Baogao" (A Report On Goods Price), in *Chen Yun Wenji* (Collected Works of Chen Yun), Beijing: Zhongyang Wenxian Chubanshe, vol. 2, pp. 25-26.

<sup>37</sup> Chen Yun, "Dangqian Caijing Qingkuang" (Current Financial Situations), in *Chen Yun Wenji* (Collected Works of Chen Yun), vol. 2, p. 135.

<sup>38</sup> POBC General Office: Guanyu Juban Zhazhi Cunkuan de Jueding (Concerning the Decision to Implement Materialized Savings), in *SEAF*, pp. 144-145.

<sup>39</sup> POBC Shanghai Branch: Yinian Gongzuo Zongjie (Yearly Work Review), in *SEAF*, pp.148-149.

<sup>40</sup> Guanyu Faxing Renmin Shengli Gongzhai De Jueding (Concerning the Decision to Issue People's Victory Public Debt), *People's Daily*, 4 December 1949.

with the *renminbi*.<sup>41</sup> But a more ingenuous approach was in the employments of the military as an agent of market expansion. The Central China Finance Commission, for instance, asked local People's banks to issue currency to the procurement agencies of the Fourth Field Army to buy necessary goods at low prices in liberated areas in the north and deposit the goods at state-owned stores in the south. When the main army units marched past, the logistics department would take the lead in using the new currency to acquire goods in official quoted price and thus convinced the local residents to follow suit in using the new currency.<sup>42</sup>

Short-term anti-inflationary measures of the CFC culminated in the Shanghai Conference held between 27 July and 15 August 1949. Participants included department heads for fiscal, financial, trade affairs from all regional Finance Commissions. During the Conference, Chen Yun made an overall estimation of the financial situation. Despite many obstacles, he expected the economic and fiscal situation to improve in early 1950, as government could broaden its sources of revenue by reinstating various taxes in newly liberated rich areas in South China. Following the experiences in Shandong and Manchuria, he suggested the government take one-third of its fiscal resources to acquire material reserves.<sup>43</sup> Chen also categorically rejected a milder approach to the economy with some tolerance of mild inflation, reinstating that inflation should be contained at all costs under current circumstances.<sup>44</sup>

### *Building a New National Money*

By the end of 1949, although major inflation was over, the perception of excess cash was still widespread and inflation expectations still lingered.<sup>45</sup> The focus of the CFC shifted from anti-speculation and price stabilisation to permanent reduction of excess cash in the market. The main strategy was to convert cash in circulation to deposits, preferably long-term fixed deposits. As with the NELA experience, cash control on such a scale required centralised control of finance. In March 1950, the CFC led by Chen Yun moved quickly to centralise economic and financial works including trade, financial, fiscal, transportation and personnel management systems across all provinces and economic regions.<sup>46</sup>

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<sup>41</sup> CCP Central China Bureau: "Guanyu Faxing Xinrenminbi de Jinji Zhishi" (Urgent Guideline Regarding the Issuance of the New RMB), in *SEAF*, pp. 34-35.

<sup>42</sup> Ibid, p. 37.

<sup>43</sup> Chen Yun, "Kefu zanshide shengli zhongde kunnan" (Overcoming temporary difficulties amidst victory), *Chen Yun Wenji* (Collected Works of Chen Yun), vol. 2, p. 699.

<sup>44</sup> Chen Yun, "Guanyu Wujia Wenti de Baogao" (Report on the Problems of Price), in *Chen Yun Wenji* (Collected Works of Chen Yun), vol. 2, p. 175.

<sup>45</sup> PRC First Financial Conference Record: "Guanyu Tongyi Yiqie Xianjin" (On Centralization all Possible Cashes), in *SEAF*, p. 217.

<sup>46</sup> The PRC Government: "Guanyu Tongyi Guojia Caizheng Jingji gongzuo de jueding" (Decisions on Centralization of National Economic and Fiscal Works), *PRC Selected Economic Archive 1949-1952, General Volume*, Beijing: Zhongguo Chengshi Jingji Chubanshe, 1995, pp. 593-598.

As the fiscal system was centralised, a system of highly centralised cash controls was imposed on the entire public sector, requiring every public unit to make their cash plan in advance, get approval from the CFC and deposit all the excess cash into designated accounts after all transactions, be it a factory, a logistics department, a public school, a government bureau or state commercial enterprises. The extra cash was to be automatically deposited with the issuance treasury set up separately from the cash treasury within local POBCs.<sup>47</sup> Official data was indicative of the success of the new policy. Within half a year, 88% of these state bodies had established their bank accounts with the local branches of the People's banks and 54% had already introduced a cash plan.<sup>48</sup> Meanwhile, total deposits in the issuance treasury between January and October 1950 saw an increase of more than 800%.<sup>49</sup>

According to Chen Yun, anti-inflationary tactics like tight cash controls and fiscal discipline must be accompanied above all by the state commercial sector's control over the key daily necessities.<sup>50</sup> In April 1950, the powerful Ministry of Trade established a hierarchy of specialised state trade monopolies across the country. At the central level, there were five specialised internal trading companies that specialised in grain, coloured cloths, miscellaneous goods (*bai huo*), salt and coal, each with a direct super-regional subsidiary.<sup>51</sup> The system was supported at the provincial level by three companies that specialised in grain, daily necessities and indigenous products and in the cities, they corresponded to regionally divided state-owned wholesalers and retailers, but not to special trade companies. In accordance with cash control, all transactions between the trade companies were carried out by the People's Bank on their behalf.<sup>52</sup>

The centralised model of economic control in both material and monetary domains enabled the state to expand its role in domestic commerce. As with the case prior to centralisation, state commercial system not only focused on national price stability but also worked to complement existing market mechanisms. But contradictions soon arose between the two basic objectives.

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<sup>47</sup> PRC First Financial Conference Record: "Zhongyang Jinku Tiaoli" (Central Regulations on Bank Treasuries), in *SEAF*, p. 109.

<sup>48</sup> People's Bank Headquarter: "Bannianlai Xianjin Guanzhi Chubu Huigu" (Preliminary Review of Cash Control Work after Half a Year), in *SEAF*, p. 228.

<sup>49</sup> People's Bank Headquarter: "1950 Qiansanjidu de Huobizhengce" (Monetary Policy in the First Three Quarters), in *SEAF*, p. 267.

<sup>50</sup> Chen Yun, "Guanyu Wujia Wenti de Baogao" (Report on the Price Problem), *Chen Yun Wenji* (Collected Works of Chen Yun), vol. 2, pp. 25-26.

<sup>51</sup> PRC Government: "Guanyu Quanguo Guoying Maoyi Shishi Banfa de Jueding" (Decision on the Methods of Operation for the State-operated Trade), *PRC Selected Economic Archive 1949-1952, Commerce Volume*, Beijing: Zhongguo Wuzi Chubanshe, pp. 33-34.

<sup>52</sup> Ministry of Trade and People's Bank: "Guanyu Maoyi Jinku Hetong de Jueding" (Decision on the Contract of Trade Treasury), *PRC Selected Economic Archive 1949-1952*, pp. 593-598.

In March 1950, as the last round of major inflation was eventually brought under control, retail prices for necessities began to decline. Although there was again a price hike in late 1950, inflation was no longer the trend.<sup>53</sup> As money illusion brought by inflation disappeared, private entrepreneurs suddenly felt the full impact of cash control and the squeeze effect of state monopoly. Private enterprises previously dependent on private banking finance faced the worst challenges in meeting their financial commitments as the new state banks allocated 80-90% of their loans to finance the state sector.<sup>54</sup> The increasing market share of state trading companies in grain, cotton, salt and near state monopoly on mass transportation facilities also squeezed the space for private merchants.<sup>55</sup> Since April 1950, a nationwide debt crisis had erupted, resulting in the closure of 6,000 businesses in two months in Shanghai alone.<sup>56</sup>

Facing an imminent collapse of the private industry, the CFC immediately set out to rebalance relations between the private economy and public institutions. Although the key long-term solution to the depression, as Chen Yun remarked in his year-end economic review, was to boost domestic demand by increasing the purchasing power of peasant households, in the short-run, the government had to rescue private enterprises with an immediate demand in the form of direct state contracts with industrial firms to replace the dysfunctional market mechanism.<sup>57</sup> Typical contracts between enterprises and enterprise bureaus of local finance commissions included raw materials, a credit arrangement with state banks and an imputed profit margin.<sup>58</sup> In accordance with the ongoing cash control, the contract imposed extremely harsh conditions on private credit and required the enterprises to submit mandatory monthly production and credit reports to the People's Bank.<sup>59</sup> In the face of the extensive crisis, the system was implemented in a rapid fashion. Taking the cotton industry in Shanghai as an example, between August 1950 and July 1951, the share of state contracts in the output of coloured cloths alone increased from 32% to

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<sup>53</sup> Shanghai Academy of Social Sciences (SASS), *Jiefang qianhou Shanghai pifa Wujia huibian (Compilation of Price Index of Shanghai before and after Liberation)*, Shanghai: SASS Press, pp. 11-12.

<sup>54</sup> Nan Hanchen, "Zai Renmin Yinhang Chengli Erzhounian Jinian Huishang de Baogao" (Report at the 2<sup>nd</sup> Anniversary Ceremony of the PBOC), in *SEAF*, p. 357.

<sup>55</sup> For various regional reports on the same problem, refer to *PRC Selected Economic Archive, Domestic Trade Volume*, Beijing: Zhongguo Wuzi Chubanshe, pp. 341-350.

<sup>56</sup> Xu Dixin, "Guanyu shanghai Gongshangye Qingkuang de baogao" (Report on the Situations of Shanghai Private Entrepreneurs), *PRC Selected Economic Archives, Industry Volume*, Beijing: Zhongguo Wuzi Chubanshe, p. 378.

<sup>57</sup> Chen Yun, "Guoqu Yinian Caizheng Jingjide Zhuangkuang" (Economic and Fiscal Situations in the Past Year), *Chen Yun Wenji* (Collected Works of Chen Yun), Beijing: Zhongyang Wenxian Chubanshe, vol. 2, p. 177.

<sup>58</sup> Chen Yun, "Muqian Jingji xingshi he tiaozheng Gongshangye yu shuishou zhengce" (Current Economic Situations and Industrial and Fiscal Policy Adjustment), *PRC Selected Economic Archives, General Volume*, Beijing: Zhongguo Wuzi Chubanshe, pp. 743-744.

<sup>59</sup> PBOC General Office: "Guanyu siying qiye daikuan de shuoming" (Note for Private Enterprises Loans Contract), in *SEAF*, pp. 379-380.

81%.<sup>60</sup> While initially intended to be an expedient, state contracts were later institutionalised, as China's international and domestic political economy evolved in favour of tight state control during the Korean War.

Initial rescue policy proved effective as most private enterprises resumed operations before September 1950, but another shock permanently changed the structure of domestic commerce. As China entered the Korean War in October 1950, the goods market was again hit by a spurt of speculation and sudden price hikes in all basic necessities. In the last months of 1950, it seemed that the state was again losing control of the price of cotton cloths.<sup>61</sup> Although speculation was duly suppressed, the problem this time was that of a structural shortage instead of being purely a matter of speculation due to massive military mobilisation and the American embargo.<sup>62</sup> As in the case of initial stages of market control in the NELA, state trading companies were ill-prepared to handle a tight market, especially when there was a shortfall in supply. Officially quoted buying price was usually not as competitive as bid prices offered by private merchants, yet the selling price had to be kept low to avoid inflation. After repeated failures to acquire sufficient cotton cloth following the market-oriented approach, the CFC eventually imposed an emergency monopoly over the procurement of cotton yarns (an intermediary product for cloths) and cotton cloth from factories in January 1951.<sup>63</sup> This was the first of many decisions on monopoly trade that appeared one after another between 1951 and 1954.<sup>64</sup>

With the lessons of KMT monetary fiasco still fresh in memory, the CFC and its successor organisations were determined to contain inflation at all costs.<sup>65</sup> But financing the military action in Korea and economic construction projects were highly expensive and went beyond the nascent CCP state's meagre means. This conflict of objectives between inflation control and budget expansions could only be resolved if

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<sup>60</sup> Izutani, Yoko, *Chogoku Kengoku Syuki no Seiji to Kezai* (Politics and Economy in Early PRC), Tokyo: Ochanomizu Books, p. 72.

<sup>61</sup> Interestingly, the justification for the cotton trade monopoly given by the *People's Daily* on New Year's Eve was the backwardness of China's cotton sector and limited productive power, rather than the increasing difficulty in acquiring cheap cotton on behalf of the state commercial sector. In fact, the more sensible way to stimulate production is simply to allow state-quoted price to float slightly above actual market price, as the CFC did in March and April 1950.

<sup>62</sup> Zhu Jiamu, *Zhonghuarenmingongheguo shi Biannian* (Chronicle History of the PRC), Beijing: Dangdai Zhongguo Chubanshe, pp. 387-389.

<sup>63</sup> CFC: Guanyu Mianbu tonggou tongxiao de jue ding (Decisions on State Monopoly Trade of Cotton Cloths), *PRC Selected Economic Archives, Domestic Trade Volume*, pp. 54-55.

<sup>64</sup> These documents can be found in the volume on commerce in the Collected Archives, pp. 146-150.

<sup>65</sup> For an early economic appraisal on the low inflation policy, see Dwight Perkins, *Market Control and Planning in Communist China*, pp. 154-177. Perkins speaks approvingly about the policies of price control by the CCP, stressing the usefulness of the indirect taxes implicit in the price controls, which did not hurt incentives of the workers from a Keynesian perspective. But he did not seek to explore the costs of low inflation in terms of the huge material reserves required to support the system.

the state could set prices freely and control the circulation of a range of commodities. The natural outcome of the conflict was therefore the gradual expansion of state trade monopolies and the furthering of state contracts, which had already been instituted in certain sectors by early 1951. Between 1951 and 1954, the CFC's trade monopoly spread from cotton products to almost all important commodities.<sup>66</sup>

As private industrial entrepreneurs succumbed to state contracts and private merchants were sidelined by large state monopolies, the CFC bureaucracy at all levels had largely subsumed the market with a state-managed trade system within a short time span. Money supply now was benchmarked to state control of material reserves and estimated aggregate consumption of daily necessities at household and individual levels. In a sense, the national economy itself was transformed to a huge household management organisation (*Oikonomia*) in which economic units and factors of production were not coordinated by markets, but were organised vertically through a system of economic bureaucracy that set the prices and determined the supply of all essential commodities, with subordinate bureaucracies and economic units each performing a specific function and executing orders from the centre. The extent to which this system is a Chinese version of the Soviet system is still largely disputed.<sup>67</sup> Sometimes characterised as an organised dependency, it is at least as heavily shaped by Chinese indigenous experiences and traditional economic institutions as by the Stalinist model.<sup>68</sup>

### Monetary Revolution in Historical Perspectives

From a historical perspective, the *material standard* could be regarded as an institutional innovation based on earlier economic institutions of imperial China, namely, state-backed fiat paper money and state commercial organisations responsible for inter-temporal and regional price-stabilisation, in particular the grain baffle stores. The first institution, which had been in existence from the Song to the early Ming dynasty, disappeared from the scene after successive imperial governments failed to

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<sup>66</sup> The conflict between state and private commerce reached its climax in the Sanfan Wufan (Three Antis and Five Antis) Campaign in early 1952, when the private share fell from 60-70% to 20-30%. For a most comprehensive study on the political and policy dynamics of the Antis Campaign, refer to Yang Kuisong, *Zhonghuarenmingongheguo Jianguoshi Yanjiu* (Research on the History of the Foundation of the PRC), Nanchang: Jiangxi Renmin Chubanshe, pp. 260-363.

<sup>67</sup> To what extent is the system of the Communist economy a Chinese version of the Stalinist model in Soviet Union is still disputed. There is no doubt that China has learnt greatly from the Soviet Union in the 1950s and had shed most of the Soviet institutions since the 1980s. But as this paper has argued, it is possible that the CCP has developed an institutional framework of its own based on its own experience and only added to these fundamentals some trappings of the Soviet planned economy in the 1950s. For a detailed discussion of the impact of Soviet model on the Chinese economy, refer to *China Learns from the Soviet Union, 1949-present*, Lanman. MD: Rowman & Littlefield Publisher, 2010, edited by Thomas P. Bernstein and Hua-yu Li, pp. 153-230.

<sup>68</sup> There are few studies on the sociological aspect of the Chinese economy in the 1950s. But from Andrew Warder's *Communist Neo-traditionalism: Work and Authority in Chinese Industry*, a study of China's workplace in the late 1970s, we can still learn a great deal about "organised dependency" which has been likened to a traditional household in the Communist economy in much of the 1950s and 1960s.

follow strict fiscal and monetary disciplines.<sup>69</sup> But the second system, most famous example being the state-run ever-normal granary, eventually evolved into a national system and an institutional backbone in the imperial agrarian economy.<sup>70</sup>

Although the origins of fiat paper money and material reserve can be traced far back to China's imperial past, it was Sun Yat-sen who first raised the idea of backing fiat paper money with state-controlled materials in a sensational speech cabled nationwide in December 1913.<sup>71</sup> According to Sun, as currency is principally used in the Chinese society as a medium of exchange for basic goods, the state could simply dispense with silver coins and replace them with a new paper currency that had its value backed by a reserve of basic goods. In the early 1920s, Sun's ideas were enthusiastically expounded by his two faithful lieutenants, Zhu Zhixin and Liao Zhongkai.<sup>72</sup> But after the death of Liao, the KMT government continued using the late imperial *de facto* silver standards until 1935, when it permanently switched to the state-backed *fabi* and a foreign currency standard.<sup>73</sup>

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<sup>69</sup> Between the 11th and 14th centuries, the imperial financial administrations under Southern Song and Yuan dynasties did operate a system of fiat currency (*jiao zi/hui zi*) backed by a reserve of copper coins and silver taels with mixed results for the economy, before the experiment failed in the late Yuan due to hyperinflation and was completely given up in the early Ming. The fiat money was only raised again in the more recent past by Wang Liu, a maverick scholar and proponent of state theory of money, similar to Georg Friedrich Knapp's ideas in *Staatliche Theorie des Geldes* (State Theory of Money). His ideas triggered a debate and an ill-fated experiment with paper currency in the mid 19th century.

<sup>70</sup> Refer to Pierre-Etienne Will and R. Bin Wong, *Nourish the People: State Civilian System of Granary in China, 1650-1850*, Ann Arbor: The University of Michigan Press, 1991, chapter 1. State and civilian granaries were only part of the imperial state reserve system (*pingzhun*) that served principally to balance the seasonal fluctuation of the market in an agrarian economy.

<sup>71</sup> Sun Yat-sen, "Changqi qianbi geming duikang sha'e qinglue" (A Proposed Monetary Revolution against the Aggression of Czarist Russia), *Sun Zhongshan Quanjì* (The Complete Works of Sun Yat-sen), vol. 2, pp. 544-546. But it should be noted that Sun is not the only man who borrowed ancient Chinese economic wisdoms to solve modern economic problems. For example, Richard Graham proposed a state material store to pre-empt large shortfalls in demand during the Great Depression in *Storage and Stability: a Modern Ever-Normal Granary*, McGraw-Hill, 1937.

<sup>72</sup> Zhu Zhixin first provided a list of essential goods including grain, salt and cotton as the reserve to back a currency and coined the term goods standards, for such a system. Liao Zhongkai, another chief aide and Minister of Finance in the KMT Guangdong government, developed these ideas further. In his "*Huobi Geming yu Jianshe*" (Monetary Revolutions and Construction), Liao envisioned a monetary authority consisting of four bureaus responsible for trade and production of essential goods and the issuance and liquidation of goods-based currency. Refer to *Zhu Zhixin and Liao Zhongkai Ji* (Collected Works of Zhu Zhixin and Liao Zhongkai), Shanghai: Shanghai Bookshop, 1992, pp. 66-69, pp. 351-355.

<sup>73</sup> It is precisely because of this key distinction that KMT-controlled Taiwan could pursue an entirely different anti-inflationary policy in the immediate aftermath of the civil war from 1950 to 1954, despite important institutional similarities between Taiwan and the Mainland. Apart from direct Dollar aid from the United States, the central banks were able to stamp out inflation by the common practice of raising interest rates. The process of disinflation took longer than that for the Mainland, but was free from similar consequence of state control. Refer to Pan Zhiqi, *Guangfu Chuqi Taiwan Tonghuopengzhang Fenxi* (Analysis of the Inflation in Taiwan in the early Post-recovery Period), Taipei: Lian Jing Chubanshe, 1971, pp. 95-98.

In contrast to KMT financiers after Liao who exacerbated the monetary woes of the KMT government by financing uncontrolled military and fiscal expansions with paper money, Communist theorists of money typically rejected “bourgeois monetary theory” altogether and regarded state power in regulating and controlling markets as key to monetary success.<sup>74</sup> Whereas the KMT government often turned its currency into useless paper after exhausting its active gold, silver and foreign reserves in the fits of fiscal excesses, the Communist government would simply meet its excess fiscal demands by transferring materials and drafting labour forces directly from household units. In times of fiscal irrationalities, CCP’s forceful material mobilisations could even lead to material deprivation for the rural household sector as a fundamental unit of production and consumption. In the Great Leap Forward, for instance, peasant starvation was the ultimate result of excessive grain procurement by the Communist state, rather than a sharp fall in absolute output. During the Leap years, it was estimated that the state grain procurement reached a record high of 30-37% of the total grain output for various provinces, far above the usual 20-25% pre-1958 level, as the Communist state struggled fiercely to finance unrealistic industrial projects at the cost of the daily consumption of peasant households.<sup>75</sup>

In retrospect, the unexpected consequences of the *Monetary Revolution* might find its origins in the revolutionary architects’ unique vision of a modern monetary system. Ironically, the belief that silver and gold were useless since they could not provide for the material livelihood of the people echoed an old substantive view of the economy as quintessentially a means for material subsistence. But this old vision of money and the national economy failed to recognise that although precious metals were of no immediate use to a largely household-based economy, they could still be institutionally important for the national economy, which was more than a simple aggregate of a million households. The gold, silver and foreign currency reserves imposed a fiscal limit on the government exactly because they are scarce in supply and beyond the control of the state. Unless a country is a major producer of gold and silver, it has to acquire the reserves either through trade surplus, that is to say, by maintaining a competitive and productive export-oriented manufacturing sector, or settle with a modest budget. Thus silver, gold and foreign reserves serve as a natural counterbalance to inflation fuelled by budget deficits. This property was borne out by relative fiscal discipline and price stability in China from the late Ming to the early Republican era, when a *de facto* silver standard was in place.<sup>76</sup>

Another in-built weakness in the monetary system based on *material standard* and the centrally managed national economy in early Communist China was the *raison d’état* of an expansive party-state, developed through ideological, military and

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<sup>74</sup> For one such example, refer to Yang Peixin, *Xin Huobixue* (A New Theory of Money), 1950, pp. 203-204. This book was once the standard textbook for PBOC staff in 1951 before more extensive Soviet materials were available in translation.

<sup>75</sup> Frank Dikötter, *Mao's Great Famine: The History of China's Most Devastating Catastrophe, 1958-62*, New York: Walker. Co, pp. 156-157; in fact, the pre-1958 CCP procurement level was already at least 200% above the KMT level; refer to Sasagawa Yuji and Okumura Satoshi, *Chogo no Chugoku Shakai, Chunichi Senso shita no Sodojin to nozon* (Chinese Society Behind the Guns: Total Mobilization and the Countryside during the Sino-Japanese War), Tokyo: Iwanami Books, 2007, p. 233.

<sup>76</sup> Jia Xiuyan, Lu Manping, *Minguo Jiageshi* (History of Prices in Republican China), Beijing: Zhongguo Wujia Chubanshe, 1992, pp. 5-7.

fiscal mobilisations in the Sino-Japanese War, the Civil War and the Korean War.<sup>77</sup> Despite the inherent prudence of household management tradition from imperial China, which did find its modern embodiment in the economic thoughts of Chen Yun and many others, the political dynamics and ideological vision of the national economy came from the charismatic leader Mao Zedong and his faithful politico-ideological lieutenants in charge of local economic affairs. This fateful embeddedness, together with the inherent theoretical weakness of the *material standard*, paved the way for the system's irrational movement and tragic fate of millions of starving peasants in the late 1950s.

The *Great Monetary Revolution* was a transformational event in the century-long evolution of China's monetary and economic system and is still very much alive today. Although the CCP has gradually embraced global capitalism and adopted a *de facto* foreign currency (mainly the Dollar) standard, it has retained important traces of the old system as well. Although it is true that the CCP state has ceased to control basic materials and abolished almost the whole state commercial system since the Reform, the state power to control and mobilise has simply shifted from key commodities to key factors, such as land, natural resources and nationwide infrastructures in the name of state assets.

Nowadays, the lion's share of new money supplied still falls into the hands of bureaucratic agents in control of state assets in the form of credit from the largely state-owned banking sector, which in turn mobilises savings from all households and state-owned enterprises for the state's economic objectives. Many of the state assets, such as urban land, were still forcefully mobilised from its current users, sometimes with naked extra-legal coercive measures and meagre compensation, more or less in the same way as grain in the Leap Forward years was forcefully procured. In many ways, the contemporary monetary system is a revision and continuation of the *Monetary Revolution*, rather than its reversion.

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<sup>77</sup> For an excellent overall analysis of this development, see Okumura Satoshi, *Chogoku no Gendaishi: Senso to Shakai Shugi* (China's Modern History: Wars and Socialism), Tokyo: Aoki Books, 2000.