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REVIEW OF FOREIGN DEVELOPMENTS

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Inaugural Meetings of the Fund and Bank in Savannah

Alice Bourneuf

The first meetings of the Boards of Governors of the Fund and Bank beginning on March 8 in Savannah, Georgia, will be concerned largely with organizational and procedural matters including the adoption of by-laws, the admission of countries to membership, and the election of Executive Directors. In general the purpose of the meetings is to take whatever steps are necessary to enable the Fund and Bank to start operating as soon as possible.

The by-laws will constitute a more or less permanent set of working rules for the Fund and Bank. One of the principal questions to be covered in the by-laws will presumably be the powers to be delegated to the Executive Directors by the Boards of Governors. The Articles of Agreement of both the Fund and Bank provide that all of the powers of the institutions are vested in the respective Boards of Governors but that the Boards may delegate all except certain special powers to the Executive Directors. It seems very likely that the Boards of Governors will delegate all possible powers to the Executive Directors. The Boards of Governors, being made up of one Governor appointed by each country, are too large to be concerned with the majority of problems which will be facing the Fund and Bank. Furthermore, the Boards of Governors presumably will meet at irregular intervals and perhaps not more than once a year. On the other hand, there will be twelve Executive Directors of each institution who will be in continuous session at the main offices of the Fund and Bank and these Executive Directors are elected or appointed in such a way as to represent all of the members of the two institutions.

Another question relating to the functions of the Executive Directors which may be discussed in connection with the by-laws is the question of what exactly is meant by "in continuous session." Although it has been generally assumed that the intention of this phrase was to make the Executive Directors full-time officers, differences of interpretation have arisen. The British, and representatives of some other European countries, believe the Fund should operate as automatically as possible. They regard the drawing privileges of member countries as rights which should not be interfered with except in very special circumstances. The Americans, on the other hand, believe the Fund should only be used for certain purposes and that the management of the Fund has a definite responsibility for analysing the use made of the Fund by each member country and for refusing access to the Fund in cases where the proposed use would not be in accordance with the purposes of the Fund. The British view of the way in which the Fund should operate leads them to take the position that the Executive Directors representing the individual members of the Fund need not be full-time officers. Since the Fund's operations would be more or less automatic, the Managing Director could easily be responsible for current operations and the Executive Directors could meet monthly, for example, to take up unusual problems. The American position, on the other hand, argues in favor of full-time Executive Directors since the concept is that each time a member wishes to draw on the Fund the Executive Directors may wish to consider the request and to decide whether or not it should be granted. The issue of full-time versus part-time Executive Directors may not be discussed at length in the actual meetings at Savannah. The question may be left to be worked out by the Executive Directors or an unwritten understanding may be reached. However, the views with respect to full-time versus part-time Executive Directors will certainly underlie any decisions reached as to the salaries of the Executive Directors and the salary to be paid the Managing Director of the Fund. These salaries must be determined by the Board of Governors under the terms of the Articles of Agreement and will presumably be determined at the Savannah meeting.

Another question which must be decided in Savannah is the location of the main offices of the Fund and Bank. New York and Washington seem to be two possibilities. It is probable that New York will be favored by the foreign representatives on the ground that it will eliminate undue influence by the United States Government on the management of the Fund and Bank. From the point of view of the United States, location of the main offices in Washington might be preferable since under the terms of the Bretton Woods Agreements Act the American Executive Directors are to be advised by the National Advisory Council, all the members of which are in Washington. Although it may be argued that the main office of the

International Bank should be in New York because of the close relations which must exist between the Bank and the New York securities market, a branch office in New York could perhaps serve this purpose. The operations of the International Fund could presumably be directed as easily from Washington as from New York.

A major question which is likely to come up at the Savannah meeting relates to the admission of members to the Fund and Bank. In the first place the instruments deposited by those governments which signed the Fund and Bank Agreements before December 31 will presumably be analysed with a view to determining whether the individual governments have in fact taken all the steps necessary to enable them to fulfill their obligations under the Agreements. It is probable that one or two of the countries which signed the Agreements before December 31 will be judged ineligible as original members because all of the necessary steps have not yet been taken.

Another question to be decided will be the terms on which governments represented at Bretton Woods which did not become original members will be admitted. It is understood that the United States delegates will favor a resolution permitting such nations to join on the same terms as original members and it is expected that a number of governments will sign the Fund and Bank Agreements while the Savannah meetings are being held. It is very doubtful that any governments other than those represented at Bretton Woods will be admitted to membership at the first meeting. Applications from such governments will presumably be referred to the Executive Directors for their consideration and recommendations as to the size of their quotas, etc. In the special case of Denmark the Articles of Agreement already provide that Denmark will be entitled to sign the Agreements as soon as the Fund and Bank have agreed on the appropriate subscriptions. It is probable that the subscriptions of Denmark will be determined at the Savannah meetings.

The final business to come up at the Savannah meeting will probably be the election of the Executive Directors by the Governors of those countries not entitled to appoint Executive Directors. After the election of the Executive Directors it will be possible for the Fund and Bank to begin operations and for the Executive Directors to take the first important steps of selecting the Managing Director of the Fund and the President of the Bank. The Governors may recommend that the Executive Directors begin their sessions before a certain date and it is even conceivable that the Executive Directors will hold their first meetings immediately after the close of the meetings of the Boards of Governors. This will be possible only if all the appointed and elected Executive Directors are available in this country. The five countries with the largest quotas, which are entitled to appoint Executive Directors, have not all announced their appointments as yet.

There is one interesting problem which will arise if Russia and some of the other countries represented at Bretton Woods join the Fund and Bank after the close of the Savannah meetings. In the first place, if

Russia does not join during the Savannah meetings, India will be the government with the fifth largest quota and therefore will be entitled to appoint an Executive Director for both institutions. The other four appointed Executive Directors will be named by the United States, the United Kingdom, France and China. If Russia should join the Fund after the close of the Savannah meetings, the Articles of Agreement seem to give her the immediate right to appoint an Executive Director and India's appointed Director would have to retire. According to the Articles of Agreement, furthermore, no election of the other seven Executive Directors would take place for two years so that India, or any governments joining after the close of the Savannah meetings, would not be able to participate in the election of Executive Directors until the two years had elapsed. It is always possible, of course, that the Agreements will be amended to provide for some representation or to provide for holding a special election. Much will probably depend on the identity of the countries which do join after the close of the Savannah meetings and on how soon they join.

Expiration of the Franco-British Financial Agreement

Hans J. Dernburg

The Franco-British Financial Agreement of March 27, 1945, expired on February 28, and negotiations with respect to trade between the two countries have been under way since December of last year. It is expected that future trade between the two countries will be on a cash basis or will be privately financed. If any new inter-governmental credits are extended, they will undoubtedly be on a far more modest scale.

The agreement has given France considerable assistance during the first very difficult year of reconstruction but it has been disappointing from the British point of view. It was probably foreseen that France would import more from Britain than it would export to that country, but the degree to which that happened surpassed expectations. Trade between the franc area and the sterling area assumed almost the character of one-way traffic in the direction of France, leaving Britain with a considerable claim against that country, part of which will remain even after the gold settlement provided for in the agreement has taken place.

The original agreement provided reciprocal governmental credits of 100 million pounds sterling and of 20 billion francs (at the then prevailing rate of 200 francs to the pound sterling). However, of the 100 million pounds sterling credit of Britain to France, only 60 million pounds were made available for imports from Britain, while the remainder of 40 million pounds was to be transferred to a so-called "B" account to be used, together with other French funds, for the settlement of certain British claims which had originated during the war. The funds potentially available under the agreement for British imports from France thus exceeded the funds made available for French imports from Britain by 40 million pounds sterling. This arrangement was probably chosen in the expectation that -- in partial payment of imports -- the French Government would be able to liquidate private French balances in London up to 40 million pounds sterling, the amount by which French balances in Britain were estimated to exceed British balances in France.

The agreement provided that if France should be a net debtor at the end of the agreement the balance should be settled in gold to an amount equal to one-third of the gross total of the payments from the franc area to the sterling area during the year ending February 28, 1946.1/ The remaining deficit is to be paid out of any unused funds in the "B" account; if this should be insufficient the balance is to be carried forward on conditions to be agreed upon between the two governments.2/

In drafting the agreement, it was probably intended that in practice the whole debit balance should be settled in gold. It may have been assumed that total French imports, including those paid for out of private balances, would not exceed French exports by much more than 30 million pounds sterling, equivalent to about one-third of the maximum credit of 100 million. It would have been in line with this expectation if -- in addition to paying 40 million for certain war debts -- the French had imported goods to the value of 45 to 90 million pounds sterling and exported goods valued at 30 to 60 million pounds, paying for the difference to the amount of 40 million pounds sterling in private balances and of 15 to 30 million pounds sterling in gold.

By October 1945 it was clear that the expectations underlying the agreement would not be fulfilled. French imports for reconstruction of the country were heavy while French exports lagged far behind, both because French productive capacity was slow to expand and because the franc was overvalued. In addition, the French had not succeeded in mobilizing their private balances. As a result, the credit available for imports had been exhausted. The contingency of an exhaustion of the credit was foreseen in the agreement which provided that if the credit of 100 million pounds (or the corresponding credit in terms of French francs) should prove insufficient, the two governments would consult together with a view to increasing the credit lines in order that there might always be sufficient funds. In order not to bring exports to France to an abrupt standstill and not to hold up French recovery, the British decided -- in spite of the previous experiences -- to raise the overall credit by 50 million pounds sterling to 150 million pounds.

It is believed that at the termination of the agreement on February 28, 1946, the French had exhausted the entire credit of 150 million pounds, 110 million pounds for imports from Britain and 40 million from the "B" account for the settlement of war claims. The British, on the other hand, are believed to have used up franc balances for imports from France to an amount equivalent to no more than 25 million pounds. The net debit balance to be settled by France would thus amount to 125 million pounds. Of this balance, an estimated 36 million pounds, equivalent to

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1/ Excluding payments made out of the "B" account.
2/ A similar settlement was provided should Britain be a net debtor at the end of the agreement.

one-third of 110 million pounds,[1] will have to be settled in gold and it is believed that another 10 million pounds will be available from "B" account, leaving Britain with an unsettled claim against France of almost 80 million pounds.

As a result, the present negotiations will have to deal with the problem of how this balance can be settled and furthermore how future trade between the two countries may be developed on a mutually satisfactory basis. It is not likely that the British will be willing to fund the unsettled balance into a long-term credit, and they will probably request its liquidation through the use of private balances and gold. A prerequisite for such liquidation was accomplished by the recent decree of February 14, by which the French Government requisitioned all foreign currency assets held by individuals and corporations. As far as future trade is concerned, the general outlook has become somewhat more favorable since the devaluation of the franc on December 26, 1945, but even so one may expect future trade to be based primarily on cash payments or private financing. The abandonment of the financial agreement would be in line with the spirit, if not required by the letter, of the Bretton Woods Agreements and the Anglo-American loan agreement.

1/ According to unconfirmed reports, France has already transferred 40 million pounds in gold to the United Kingdom. If this figure is correct, it would imply that imports from Britain reached 120 million pounds, of which 10 million pounds must have been privately financed.

Comments on German Monetary Conditions[1]

Paul Hermberg

At the moment, I think special attention should be given to the money and banking situation in Germany. The policy of noninterference is no longer bearable. Something has to be done with regard to German money if the economy is not to become completely paralyzed.

A gap exists between regular earnings and the official market price of rationed goods on the one side and hoarded money and black market prices on the other side. This gap must be bridged. People do not need to work very long to earn sufficient money to buy the official rations, but it does not pay to work harder because it is impossible by regular work to earn an amount which counts on the black market. On the Berlin black market one carton of cigarettes or three-quarters of a pound of butter would be equivalent to the regular annual earnings of a worker and consequently no one is interested in raising earnings. People do not work for money but to get higher ration points -- ration card number one is the dream of every Berliner.

1/ Editor's note: These comments were abstracted from a letter received from Dr. Hermberg who is at present on loan to a United States Government Department for work in Germany.

Businessmen may intend to repair their plants to be ready for business if the money situation is straightened out but they are not now interested in re-opening or extending production. No one likes to exchange valuable stocks of raw materials or merchandise for questionable money. Theoretically, two possibilities exist to bridge the gap mentioned earlier: (1) increase official prices and wages ten to twenty times; or (2) decrease the amount of money to 1/10 or 1/20 its present circulation. Everyone agrees that a reduction in the circulation would be the easier way. In fact, the question of cash money is closely connected with the question of bank deposits, monetary claims, Reich debt, private debts, mortgages, capital levy, etc.

Everyone seems to be convinced that agreement on all these questions can not be arranged between all the parties involved within a reasonable time. Consequently, the question regarding the abundance of cash money may have to be solved in an isolated way. In the American Zone, political parties and German administrative authorities (Länderregierungen) seem in fact to concentrate on the question of how to cut down the amount of cash money. In the Russian Zone and in Berlin, however, a radical solution of all phases of the financial question is more favored by the political parties. Nevertheless, I believe that no objections would be raised in the Russian Zone to a preliminary solution of the isolated question of cash money.

Two different ways for cutting down cash money have been proposed. In both cases, the mark would be exchanged for new money. The first proposal, however, would exchange 1 new reichsmark for 10 or 20 old reichsmarks while the second would call for an even exchange, one new reichsmark for each old one, but in the second case only a small amount -- say 200 reichsmarks -- would be exchanged for cash and the rest would be blocked in a special account. The first proposal certainly would have to be combined with the blocking of surplus money. The usual objection to the first proposal is that it would be unreasonably hard on holders of cash as compared with those having bank deposits. On the other hand, a simultaneous reduction of bank deposits would inevitably raise the question of Reich and private debts, etc. Under the second proposal, the par exchange would not represent a permanent solution until the future of the blocked accounts had been settled. The German people probably would prefer the exchange at par.

In the American Zone, banking life has again developed surprisingly; deposits are made and new credits are granted. Bank earnings are good because no interest is paid on deposits but interest is charged for loans. No one asks about the problematical value of all assets. The Mortgage banks are in a somewhat more difficult position since they have to pay interest on the mortgage bonds (Pfandbriefe) but do not get any interest on mortgages granted to bombed objects. Nevertheless, the mortgage banks are also very active.

Central Banking in Rumania and Bulgaria

J. Herbert Furth

For the first time since the Russian occupation of the Balkans, detailed statements of the banks of issue of Rumania and Bulgaria have become available. These statements present sufficient similarities to justify their comparison with each other as well as with prewar conditions. The figures below refer to the end of the year 1939 and to the latest data available for 1945, which means December 22 for Rumania and November 30 for Bulgaria.

Balance Sheets of Rumanian and Bulgarian National Banks
1939 and 1945

	Rumanian National Bank (Millions of lei)		Bulgarian National Bank (Millions of leva)	
	1939	1945	1939	1945
Assets				
Gold	20,768	50,403	2,006	2,562
Foreign exchange	2,271	25,560	1,786	24,191
Government debt	7,820	1,183,418	4,259	32,240
Other bills & advances	29,529	254,331	1,870	8,278
Other assets	13,910	32,794	609	8,845
Total	74,298	1,546,506	10,530	76,116
Liabilities				
Note circulation	48,800	1,210,042	4,245	44,682
Demand deposits	10,366	250,882	3,364	26,149
Other liabilities	13,540	83,091	1,225	3,577
Capital & reserves	1,592	2,491	1,696	1,708
Total	74,298	1,546,506	10,530	76,116

Both countries have experienced a considerable expansion in their note circulation although the expansion has been far greater in Rumania than in Bulgaria. The Bulgarian figure for 1945, however, understates the actual circulation since it excludes notes which during the war circulated in the parts of Yugoslavia and Greece occupied by Bulgaria and which are now held by the central banks of those countries, and also omits about 24 billion leva of Treasury bills which are being used as money substitutes. On the other hand, the rise in demand deposits in the Bulgarian statement is probably a passing phenomenon since the bulk of deposits represents receipts from the recent Liberty Loan which yielded 27 billion leva. These receipts are rapidly being spent so that in a short time the corresponding amount will show up as part of the note circulation rather than of deposits. Combining the increases in note circulation and demand deposits, and correcting the Bulgarian figures for the issue of Treasury bills, the rise in money and money substitutes from 1939 to 1945 may be computed at about 2,400 per cent in Rumania, and about 1,100 per cent in Bulgaria.

The gold holdings of both banks went up during the war. In the case of Rumania, the difference is overstated because of a revaluation of the Bank's gold reserves in 1940, which accounts for an increase of about 12 billion lei. In physical terms, the gold holdings of the Rumanian bank rose by about 50 per cent, those of the Bulgarian bank by about 28 per cent. It is believed that a large part of those increases resulted from the acquisition of gold from Germany, but in the case of Rumania the holdings were also steadily strengthened by the yield of the country's considerable gold mines. The market value of the gold holdings is substantially greater than the figures shown in the balance sheet. Gold is officially valued at 211.1 lei per gram in Rumania, and 92 leva per gram in Bulgaria. These valuations would correspond to a leu exchange rate of 0.53 United States cent, and a lev exchange rate of 1.22 cents. Actually, on the basis of the dinar-dollar cross rates (see this Review for February 11, 1946, p. 7), the leu is worth only between 0.02 and 0.004 cent, and the lev between 0.2 and 0.04 cent, and the market value of gold is proportionately even higher than that of United States currency. The market value of the gold holdings is therefore probably about 100 times higher than the official value in terms of lei, and about 30 times higher in terms of leva. This means, that on the basis of the market valuation, the gold reserves would be about as high as all bank liabilities in Bulgaria, and about three times as high as all bank liabilities in Rumania. Even a moderate revaluation of the gold holdings would thus reduce the government debts to both central banks to peace-time proportions and restore normal relations between reserves and liabilities.

In contrast to the gold holdings, most other asset items are of doubtful value. Foreign exchange holdings consist in both Rumania and Bulgaria of clearing claims against Germany. Moreover, the bulk of "other" assets in Bulgaria represents a "clearing claim" against Russia. In Rumania such a claim does not exist. Available information suggests that, if merchandise deliveries from Rumania to Russia on reparations account are excluded, the trade between the two countries results in an import surplus for Rumania. On the other hand, the bulk of the Rumanian Government debt represents financing of the armistice provisions including reparations; this item alone accounts for advances of the Bank to the Government of 815.5 billion lei or about 70 per cent of the entire Government debt. The remaining increase is due to financing the Rumanian war effort. Other advances -- most of them to other government-dominated credit institutions -- play a minor role in both countries in spite of the necessity of financing reconstruction and reconversion with the aid of central bank credit.

In summing up, it becomes apparent that the inflationary danger is far greater in Rumania than in Bulgaria. This is largely the result of the difference in the Russian attitude toward the respective countries. Although both countries are formally ex-enemies and are at present ruled by Communist-dominated administrations, the Russians treat Bulgaria almost as an ally, and Rumania as conquered territory. This results partly from traditions of long standing, partly from the very different roles played by the countries in the war against Russia, and partly from the fact that the oil wells and heavy industries of Rumania offer far better opportunities for ruthless exploitation than do the resources of agricultural Bulgaria.

Exchange Stabilization and Currency Conversions in China

John Exter

The abandonment of the official Chinese exchange rate of 20 Chinese National dollars (CN$) for one American dollar is an important milestone on the road to monetary stabilization in China. New exchange regulations, which became effective March 4, explicitly abolished the official rate of exchange, thus putting China on a flexible paper standard. On March 5, the Shanghai banks announced the new rate of 2,020 to 1, which is within the range of black market rates quoted in Shanghai during the past month.

The 20 to 1 rate, which had been official since 1941, had long been divorced from reality even when modified by official supplements which brought the effective rate first to 40 to 1 and later to as much as 500 to 1 for favored classes of buyers. Meanwhile, on the black market during the past few months the rate fluctuated between about 750 to 1 and more than 3,000 to 1. It dropped rapidly after early January, when it appeared to be stabilizing at about 1,500 to 1, and in late February was quoted in Shanghai at 2,700 to 1. Part of the drop may be explained by the general rise in commodity prices which took place at the time of the Chinese New Year in early February when there was a general settlement of debts and a rush of commodity buying comparable to our Christmas.

The wide fluctuations in the Chinese price level indicate clearly that there can be no satisfactory external stabilization until China has achieved internal stabilization. One of the most important obstacles to internal stabilization is the multiplicity of currencies in circulation. After a brief discussion of the present exchange rate regulations, the main body of this article will be devoted therefore to some of the problems which China faces in achieving internal stabilization, particularly currency unification.

Exchange Stabilization

The official 20 to 1 rate has been such an unrealistic one that official exchange transactions have been negligible. Instead, even reputable business men and governments bought and sold freely and openly on the black market. Until Chinese ports were opened to trade by the collapse of Japan, the problem was not too serious because the blockade had severed practically all of China's private trade relations with the outside world. The trading that was done was limited primarily to that between the free and the occupied regions. Since the end of the war, however, the situation has grown more and more intolerable, especially since China abandoned many of its import restrictions last fall. In early January, after foreign banks reopened their branches in Shanghai, it appeared that trade might be made possible by the practice of remitting dollars (for example) from the foreign bank to the branch in Shanghai. The Shanghai payee could then withdraw the dollars and sell them on the open market. Since there was an ample supply of dollars in Shanghai, the procedure could easily be reversed. However, the Chinese government prohibited the import and export of currencies by foreign branch banks, so that traders remained as thwarted as before.

The new exchange regulations establish a system of exchange control under the administration of the Central Bank of China. Dealings will be restricted to banks "appointed" by the Central Bank, and certain other licensed dealers. It is clear that the appointed banks, in order to prevent speculation and arbitrage, are expected to act in unison in announcing any particular exchange rate, but that at the same time the rate is subject to change from day to day. The Central Bank itself will ordinarily refrain from dealing in exchange, but it will "intervene in the financial market when it is deemed necessary to check fluctuations of rates." It is reported that the Government has provisionally allotted the sum of US $500 million for this purpose. If true, the amount seems more than adequate considering the restrictions which have been placed on imports.

Imports have been divided into three categories: necessities, which can be imported freely; semi-necessities, such as motor vehicles, oil products, woolens, and tobacco, which can be imported only under license; and luxuries, the import of which is forbidden. As for outpayments other than for imports, they may be made for legitimate personal requirements or other "legitimate purposes authorized by the Central Bank." Capital exports and the import or export of foreign currencies are prohibited.

The Central Bank of China set a rate of CN$2,020 to US$1 on telegraphic transfers from New York, while the local banks bought at CN$1,900. These quotations value the CN dollar lower than had been generally expected, but they indicate the intention of the Central Bank to keep the rate a realistic one. If the new system is successful, the black market in exchange should soon cease to exist and the Central Bank should be able to bring all foreign exchange assets within its control.

The new system appears to be an excellent transitional arrangement. It would be impossible under present circumstances to set an official exchange rate which might be anywhere near the equilibrium rate. China's exports have been negligible and her imports have thus far been financed primarily by UNRRA and lend-lease. Internal prices have fluctuated wildly since the end of the war. The open market rate in American dollars has had little significance because it has been affected by the unusual demand of those who seek them as a hedge against inflation. The normal demands of importers and exporters have been almost totally absent.

The present control scheme seems designed to permit the rate to seek its own level as normal trade relations are gradually resumed. It will be possible for the Central Bank to operate for the most part behind the scenes, permitting the going rate to change only for good reason rather than because of speculation. If she so chooses, China should in time be able to relax the restrictions on imports and reestablish the managed paper standard which had been so well started before the war.

Meanwhile, the success of the exchange stabilization program will depend as much upon the measures that are taken within China to halt the rise in prices and unify the currency as upon rigid exchange control measures or an adequate stabilization fund. For that reason, it is worthwhile to examine some of China's internal monetary problems, particularly that of currency unification.

Currency Unification

Now that the Marshall mission to China has considerably improved the prospects of China's political unification, the possibility of economic unification and stabilization becomes much more real.

The currency tangle in China is probably more complex than that existing anywhere else in the world. It is first of all a result of the political split in former "Free China" itself between the Chiang Kai-shek regime and the Communists. It is further complicated by China's recovery of formerly occupied territories which had been held by the Japanese in two principal forms: puppet regimes (Central China, North China, Manchukuo, Inner Mongolia); and as an integral part of the Japanese Empire (Formosa). Since each jurisdiction had a separate currency, the problem of welding them together is an imposing one.

The table below lists the principal currencies now circulating in China and furnishes a rough guide to the discussion which follows:

Principal Currency	Jurisdiction	Currency Issuing Agent
Chinese National dollar or yuan (CN$)	Former "Free China," controlled by National Government	Central Bank of China
Communist dollar or yuan (Com$)	Communist-controlled areas	Various provincial and district banks
Mongolian yen	Inner Mongolia	Mengchiang Bank (Central Bank of Inner Mongolia)
Central Reserve Bank dollar or yuan (CRB$)	Central China (Nanking puppet government)	Central Reserve Bank
Federal Reserve Bank dollar or yuan (FRB$)	North China	Federal Reserve Bank
Manchu yen	Manchukuo	Central Bank of Manchu
Formosan yen	Formosa	Bank of Taiwan

Chinese National Dollar

The official monetary unit of China is the Chinese national dollar or yuan, for which the Central Bank of China has been the sole bank of issue since 1942. Other notes, however, continue to circulate, particularly those issued by other government banks prior to 1942. In addition, there are customs gold units which, before the war, as their name implies, had a fixed gold content, equal in fact to that of the United States dollar, and were used primarily for the payment of customs duties. During the war-time inflation, the customs gold unit has depreciated along with the CN dollar and has been maintained at a ratio of one CGU to CN$20 (which since 1941 has been the official rate of the US dollar) except when the market has indicated a minor preference for the customs gold unit.

During the war, the note issue of the CN dollar expanded at a very rapid rate, as a result of budget deficits. This currency expansion contributed to an even more rapid advance in prices. The volume of notes outstanding increased from CN$ 1,407,000,000 in June 1937 to CN$ 805,923,000,000 in October 1945 (an index of 57,300 on the basis of June 1937 = 100) and was accompanied by a rise in the retail price index in Chungking from 100 in June 1937 to 203,000 in September 1945. Since September, prices have risen still further and reached new highs at the time of the Chinese New Year in early February.

It is not possible in the present article to analyze the inflation in China, but it should be pointed out that avoidance of inflation was virtually impossible for the Chinese Government, engaged as it was in a struggle for survival, deprived of a large share of its territory (including most of its industries), operating in an economy which provided a very small excess above consumption needs, and lacking the modern weapons of adequate taxation, a large bond market, price controls, and rationing. In general, inflation in Free China was even more severe than in occupied China or Manchuria. In fact, inflation in the Japanese-controlled areas seemed to grow worse as the authority of Tokyo diminished. Thus, one could expect to find higher and higher prices as he went from Japan proper to Formosa, to Korea, to Manchuria, to North China, and finally to Central China.

It is unfortunate from the point of view of its political prestige that the National Government must now replace the currencies of the Communist and formerly Japanese-controlled areas with a currency whose purchasing power has, with one exception, declined more than the currency it replaces.

Communist Dollar

The Communists, though they have maintained the formality of allegiance to the National Government, have nevertheless treated their economy as though it were an independent state. They strictly regulated their trade with both National and occupied China. The Communist yuan was issued by several provincial and district banks scattered throughout the Communist territories. In general, its issue was better controlled than that of the CN dollar, very largely because the Communists were able to collect a larger percentage of their revenues and make a larger share of their expenditures in kind.

Although the political settlement between the Communists and the Kuomintang has been pretty clearly outlined, there has been no indication of the nature of the economic settlement. At last report, the Communist yuan, which had appreciated in terms of CN dollars through 1944 and 1945, was quoted at 5 to 1. It is likely that an exchange of currencies will be carried out as soon as the political settlement has proceeded far enough. The problem of determining an equitable redemption rate will be difficult, but the bargaining power of the Communists is strong enough to insure a considerably more favorable conversion rate for the Communist currency than has been granted the puppet notes.

Mongolian Yen (Inner Mongolia)

The puppet "Federal Autonomous Government of Mongolia" was established by the Japanese in 1937. Through its central bank, the Meng-chiang Bank, it issued a Mongolian yen whose official par was one Japanese yen. The issue was last reported at 124 million in 1942. Its retirement is not likely to be much of a problem.

Central Reserve Bank Dollar (Central China and Canton area)

The puppet "National Government of China" in Nanking established the Central Bank of China as its bank of issue in 1941. In the early years of the war, the volume of notes was reasonably well controlled and prices in the Yangtze Valley region rose less rapidly than in Free China. In 1945, however, as the handwriting on the Japanese wall became apparent, the number of CRB notes in circulation increased rapidly. By the end of the war, there were probably from 3,000-5,000 billion in circulation and prices in CRB currency rose higher than anywhere else in China. The inflation was accentuated by widespread counterfeiting as the quality of the official notes deteriorated and by the rumor, which may well have been fostered by the National Government, that the CRB notes would be repudiated altogether. The CRB - CN$ exchange rate therefore dropped rapidly in September of 1945 when many people regarded the CRB notes as worthless. In October, however, the National Government decided to redeem the CRB currency at the rate of 200 to 1. Redemption was begun on November 1 in amounts which had to be limited by the shortage of CN currency, and is now almost completed.

Federal Reserve Bank Dollar (North China)

The puppet government in Peiping, called the "North China Political Council," set up as its bank of issue the Federal Reserve Bank of China as long ago as 1938. The Japanese consistently pursued a fairly conservative monetary policy and, until the last few months of the war, were able to keep prices rather well controlled. By August 1945, however, the FRB note circulation had increased to 132,600 million, as compared with 1,746 million in March 1943. Despite the fact that price increases had not gone so far as in Free China, the National Government decided to retire the FRB notes at a rate of 5 FRB to 1 CN$, a considerable overvaluation of CN currency in terms of purchasing power. The retirement of FRB currency has been in process since January 1 and is scheduled for completion by April 30, after which FRB notes will cease to be legal tender.

Manchu Yen (Manchukuo)

The Manchurian currency situation has been particularly chaotic. Although the note issue of the Central Bank of Manchu at the end of August 1945 was only Manchu Yen 8,157,000,000 (a rather reasonable increase of 500 per cent since December 1941), the Russian occupation has brought with it the issue of a military ruble which circulates at par with the Manchu yen and exchanges at a 4 to 1 rate with the domestic ruble. In addition, Japanese yen continue to circulate, as well as CN currency brought in by the Chinese occupying troops. The multiplicity of currencies plus the general disorder which has accompanied the collapse of Japan and the Russian occupation has driven prices up since the end of the war. Even so, the inflation is less severe than in the rest of China.

In an attempt to insulate the Manchurian economy from the rest of China during the transition period and to preserve as much of the comparatively sound monetary situation as possible, the Chinese government has adopted quite a different policy from that adopted in Central and North China. It has decided to replace the Manchou yen with an issue of special scrip which will be legal tender only in Manchuria; the exchange will be at a 1 to 1 rate. For the time being there is no legal exchange rate between the scrip and the CN dollar, although remittances may be made at a rate of CN $13 to 1 dollar in Manchurian scrip.

The effect of the issue of special scrip will be to protect Manchuria against an outflow of commodities which might result from a currency exchange that overvalued the CN dollar. Even with the present precautions, goods are being smuggled out of Manchuria, apparently paid for with gold, the price of which has skyrocketed in Manchuria.

When China is able to assert her authority in Manchuria and after the price level within China proper is stabilized, the problem of retiring the scrip in favor of CN currency will arise. Successful reintegration of the Manchurian with the Chinese economy will depend on the adoption of an equitable conversion rate.

Formosan Yen (Formosa)

Formosa, having been a part of the Japanese Empire since 1895, has used the Japanese yen as its domestic currency. Its yen notes, however, were issued by the Bank of Taiwan rather than the Bank of Japan.

Inflation in Formosa has been controlled even more successfully than in Manchuria. The note issue increased from Y 75 million in June 1937 to Y 410 million in December 1944 and Y 1,600 million in August 1945. The Chinese Government has adopted the same policy in Formosa as in Manchuria. The yen is being converted at a 1 to 1 rate into a special scrip which again is legal tender only in Formosa. As in Manchuria the presumption is that the conversion into CN currency will await more stable conditions in China.

The general strategy of the Chinese Government in its struggle for economic stabilization is now becoming apparent.

By April 30, when FRB notes cease to be legal tender, the unification of the currency will have been achieved with three notable exceptions --the Communist areas, Manchuria, and Formosa. For political reasons at least the first two of these are likely to be treated fairly when the time comes to incorporate them economically with the rest of China--the Communists because they will have the strength to bargain for fair treatment, and Manchuria because the Chinese Government is anxious to win the loyalty of the Manchurian people.

Meanwhile, by overvaluing the CN dollar in terms of CRB and FRB currency, the Government has penalized the people of Central and North China for the benefit of those in former Free China. There is evidence that these conversions are exerting a considerable deflationary influence upon prices.

In November and December at any rate, the spiral of rising costs and prices seems to have been definitely slowed.1/

There is also some indication that the Government will try to reduce the budgetary deficit. Although the new budget of CN $44,000 billion is the largest budget in the country's history, the rise in prices means that it will not necessarily represent a larger percentage of the country's real income than in the past. Meanwhile, tax revenues are likely to increase with the recovery of old taxes, such as the maritime customs, and the imposition of new. Present estimates, which are not likely to be very reliable, are that the deficit will be only 25 per cent of total expenditures. Unfortunately, military expenditures, comprising about half the budget, promise to remain high in the immediate future.

Among the reasons given for adoption of the new exchange regulations is the desire of China to implement its membership in the International Monetary Fund and the International Bank for Reconstruction and Development. The Government undoubtedly hopes that if China can achieve internal stabilization it may soon be able to adopt an official exchange rate which could be communicated to the Fund as the suggested initial par rate. Finally, China is evidently trying to stabilize its exchange rate in order to improve its chances of getting international loans.

1/ The Government might have given the Central and Northern Chinese more favorable treatment by granting a better rate and freezing some percentage in blocked accounts. If considered at all, this scheme was probably rejected as being administratively impossible under the circumstances.

New Parity of Netherlands Indies Guilder J.H.F.

The Netherlands Bank has reestablished, as of March 1, 1946, the pre-war relationship between the Netherlands guilder and the Netherlands Indies guilder, under which the two currencies were virtually at par with each other. The relation had been upset in the fall of 1944 when the Netherlands guilder was pegged to the pound sterling at the rate of 10.65 guilders per pound while the Indies guilder remained pegged at the old rate of 7.60 guilders per pound. The Indies guilder thus became worth 1.41 Netherlands guilders. The new buying and selling rates set by the Netherlands Bank for the Indies guilder are 99.75 and 100.25 guilders, respectively. Official exchange rates between the Indies guilder and other currencies have not yet been adjusted, but it is hardly possible for such a change to be long delayed if complete confusion is to be avoided. The practical effect of the new measure will be felt mainly in the accounting procedures of Netherlands enterprises which in the period between the German invasion of the Netherlands and the Japanese invasion of the Indies (April 1940 - February 1942) had moved their headquarters to the Indies and kept their books in Indies rather than Netherlands guilders. Actual commercial and financial relations between the Netherlands and the Indies have remained insignificant since liberation, and the final fate of the Indies currency will no doubt be decided by other factors than the rate set by the Netherlands Bank.