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CHARACTERISTICS OF THE SECURITY MARKET IN CHINA ITS SPECIAL RELATIONS WITH CHINESE NATIVE CAPITAL

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1. FINANCIAL SECURITIES AND INDUSTRIAL SECURITIES

For the development of a nation's economy, a smooth motive power in its financial basis is an important requisite. In modern times in which capital formation is turned into securities in a large measure, the development of the financial market has a very close connection with the security market. The security market is unique in that it carries on the transaction of securities and controls the market prices of such securities. The fluctuations of the security market have a close relation with the financial market. The banks use part of their assets for the purchase of securities and make loans against securities. The banks also make call loans out of their idle funds largely by means of securities. Securities are used as reserves by the banks for their bank certificates issued. In case of a financial panic, the security market is used as the spring of cash supply. In normal times, the security market is the foundation for the activities of the financial market; and in times of panics, it proves as the outer wall of the financial market as well.¹⁾ There is nothing strange about the foregoing views of the Chinese experts concerning the security market.

The security market deals with both financial securities

1) Article 1, the Security Market Act (證券交易所法), promulgated in the third year of the republican regime.

and industrial securities, the former being issued by the Government and the latter by corporations²⁾. The former is also known as the bond market and the latter as the stock market which deals also with debentures. Thus, the objects of the security market might be classified into stocks and bonds. Corporations issue stocks and debentures, while the Government issues bonds. Thus, this classification is not plausible. Further divisions may be made if classification is made more precisely. Furthermore, the security market deals with spot and futures, and calls and long-term loans. However, my present object is to examine the characteristics of the security market in China having the special role of enabling native capital to participate in the exploitation and development of national industries. For this purpose, I shall conveniently use the classification of financial securities and industrial securities in surveying the operation of the security market. The use of native capital in this connection undoubtedly is extremely backward. On one hand, a measure of advance has been made by financial securities, although they are rather abnormal in nature. On the other hand, industrial securities are marked by inactivity. If they are sane, there should be no discrepancy between the objects of financial securities and industrial securities. I shall endeavour to elucidate the causes of their unhealthy condition, for the purpose of studying the problem of utilizing economic powers at spot as a source of cooperation in building up the proposed Greater East Asia Co-prosperity sphere.

- Although the Chinese security market is not limited to Shanghai, so important has been the position of this city in the financial circles of China in the past that the examination of the security market there would clarify the general condition of the security market in China. Security markets in Shanghai are either Chinese or foreign. The native market is called "the Shanghai Chinese Security Exchange"

2) J. E. Meeker: *The Work of the Stock Exchange*, 1922, pp. 3-10.

(上海華商證券交易所) while the foreign market is known as "the Shanghai Stock Exchange" (上海衆業公所)³⁾. In taking them up, it is observed that, whereas the former deals with financial securities and is a bond market in reality, the latter deals with industrial securities and is thus a stock market. The fact that the Chinese security market in Shanghai deals only with financial securities does not mean that it received a direct blow from speculation, although it failed to cultivate the sanity of investment on one hand and had the effect of stimulating the insanity of speculation, on the other^{4) 5)}. Nor does the Shanghai Stock Exchange contribute to the sanity of industrial capital, although it had the capacity of a security market inasmuch as it deals with industrial securities. There is one point worthy of special attention about this exchange in Shanghai. The fact is that investments in industrial securities were made largely by Chinese, for such was in reality the foreign capital in China. Nor does this mean that industrial capital contributed to Chinese economy through the Shanghai Stock Exchange. This opinion is expressed by a Chinese economist, Chang Nai-chi (章乃器). Taking up the 1933 report of the holders of the preferential stocks of the Shanghai Power Corporation which is an American firm, this Chinese economist states that 69 per cent of the shareholders were Chinese, and that this was one way the Chinese militarists and business-men were united with the foreign influence in China, as well as in the other sphere from the deposits made by the Chinese with the banks of foreign nationalities. At the same time, the amount of the securities of foreign firms held by Chinese banks was by no means small. The foregoing fact indicates the failure of the native Chinese capital to make an advance into either industry of finance and the effects are seen by

3) The Financial Market of Shanghai, Economic Study (經濟研究), Vol. III, No. 7, pp. 133—134.

4) The Bond Market, Economic Study (經濟研究), Vol. III, No. 9, pp. 386—387.

5) J. E. Meeker: *ibid.* pp. 397—400.

this failure in furthering the control of foreign capital in China⁶⁾.

2. THE SHANGHAI CHINESE SECURITY EXCHANGE

The history of the security business in China has shown the same tendency as that shown by the banking business in that country. Both had the same origin during the closing period of the Kuang Hsu (光緒) era during the Former Chin Dynasty. Shanghai being the center of Chinese finance and commerce, it was there that the security business came to be developed. At first, the security market took the form of a stock market, and before the advent of the organized Chinese security business, there were two foreign establishments, namely, the Shanghai Sharebrokers' Association (上海洋商股票捐客公會) and the Shanghai Stock Exchange (上海衆業公所). It was in the third year of the Chinese Republican regime (1914) that the Chinese side began its security business by establishing the Shanghai Chinese Sharebrokers' Association (上海股票商業公會)⁷⁾. Although the Chinese security market appeared to have made its advance as a bond market in later years, it clearly originated as a stock market, as indicated by the special circumstances that prevailed at that time. Shanghai towards the close of the Chin Dynasty was marked by a busy commercial life and a consequent prosperity, with the increasing amount of foreign securities imported, especially the rubber stocks which aroused an active interest among Chinese business-men. However, the share brokerage business was largely in the hands of foreigners, with only a very small number of native Chinese engaged in it. After "the rubber storm" of the second year of the Hsuan Ting (宣統) era, the transac-

6) Wan Cheng-chih, *The Treatise on Chinese Financial Capital* (王承志, 中國金融資本論), p. 114.

7) *The Financial Market of Shanghai, Economic Study* (經濟研究), Vol. III, No. 6, p. 35.

tion of securities in Shanghai came to be a foreign monopoly, and there were no Chinese who specialized in security transactions. It was in the beginning of the Republican regime that Chinese came to be engaged in the security business for the first time. But still these Chinese were a sort of brokers and it was the establishment of the Shanghai Chinese Sharebrokers' Association that marked the real beginning of the Chinese security business; and it was after the establishment of the Shanghai Chinese Merchants' Security Exchange that the sphere of the business came to be expanded.

The Shanghai Chinese Sharebrokers' Association was established in the third year of the Republican regime and dealt with various bonds, stocks and miscellaneous shares, and its business was marked by a great activity. The share-transactions of the association were limited to the bank shares of the Bank of China, the Bank of Communications. The Commercial Bank of China and the corporate shares of the Chao Shang Chu, the Han Yeh Ping, the Ao Hang Railway and the Commercial Press. After some advance was made in the security business, the Shanghai Chinese Merchants' Security Exchange was established at the proposal of the Shanghai Chinese Sharebrokers' Association in the ninth year of the Republican regime⁸⁾. It was then expanded and reformed as if it reflected its development as an industrial security market, but it met its reversal in the spring of the eleventh year of the same regime only after it had entered its period of early development. Its shares dropped and many of its brokers had to suspend their business. Finally it had to undergo a reorganization. However, after the establishment of the Nationalist Government, it made a normal development and has been in a better condition compared with other similar organizations. A national unification of stock markets was brought about by law adopted

8) Some give the date for the eighth year of the regime, the truth is not clearly established.

by the Government in May, the 22nd year of the regime. By virtue of Article 2 of the Stock Exchange Act (交易所法), the establishment of more than a single exchange of the same nature within each district was prohibited. At that time there was in Shanghai an exchange named the Shanghai Security Goods Exchange(上海證券物品交易所) which dealt with securities. The security department of this exchange was amalgamated with the Shanghai Chinese Merchants' Security Exchange and the reorganized exchange was capitalized at 1,200,000 yuan with 80 brokers participating in it. It came to be called "the Shanghai Chinese Security Exchange".

A perusal of the foregoing simple account of the history of the Chinese security market in Shanghai will indicate the necessity of examining whether the Shanghai Chinese Merchants' Security Exchange made its development as a bond market or prospered as stock market, although it outwardly trod the road of general development. We have already seen that the Chinese security market has had a very little connection with industrial capital. Now, a survey of the business of the Chinese Merchants' Security Exchange reveals that it has made a deformed transition although outwardly it appeared to make normal development. It seems to have gone astray from industrial securities, especially since the time of its reorganization in the eleventh year of the Republican regime. It was around the fifth and sixth year of the regime that the transaction of not only stocks but also bonds began to arouse the attention of Chinese; but after the reorganization of the exchange in the eleventh year, its transaction of bonds has made its real development. This tendency was further increased in later years the position of bonds finally coming to occupy the place of predominance.

3. THE SHANGHAI STOCK EXCHANGE

It is necessary here to know something about the Shanghai Stock Exchange. It is the only stock exchange in Shanghai that it managed by foreigners. It came into

existence through the amalgamation of the Shanghai Share-brokers' Association with the Stock Exchange, the former having been established in the seventeenth year of the Kuang Hsu period and composed of foreign exchange brokers, the latter having been established in the thirty-first year of the same era⁹⁾. Its mechanism consists in free transaction by its members and has no capital of its own. The official number of its members is 100 (of which 87 are foreigners and 13 Chinese). Its dealings are composed of more than one half of foreign company stocks.

The Shanghai Stock Exchange deals with the stocks of the following banks and firms: ten banks, five insurance companies, sixteen real estate companies, six docks, warehouses and transportation companies, eight official labor companies, four cotton-spinning companies, thirty-eight rubber and plantation companies. It also deals with thirteen preferential stocks, thirty-six corporate debentures, seventeen Shanghai Municipal bonds and two club stocks. The total number of these stocks are 155, and all belong to foreign firms in Shanghai. All this made a sharp contrast with the business of the Shanghai Chinese Merchants' Security Exchange which dealt chiefly with bonds. Moreover, probably more than one half of the real investments made on these stocks dealt by the Shanghai Stock Exchange were made by Chinese. Now, what is the significance of the series of facts—that the Shanghai Stock Exchange is managed by foreigners, that it deals with industrial securities and that investments in these stocks have been made chiefly by Chinese? They betray that, although the Chinese investments represent an industrial capital which is thus made in stocks, that very capital is in the control of foreign firms. Although stocks are also dealt with to some extent by the Shanghai Chinese Merchants' Security Exchange, these are deformed and speculative and are not a purely industrial capital in nature. This exchange deals chiefly with government bonds and this is

9) Somewhat ambiguous.

why it is known in Chinese documents as a financial market. Chang Nai-chi summarizes this state of affairs as follows: the exchange indicates: (1) the backward position of Chinese native capital (2) control of Chinese capital by foreign firms and (3) control of domestic influence over the Chinese financial market. He then draws the following conclusions from the above stated facts: (1) the development of corporate enterprises and the establishment of a healthy capital market (2) the perfection of a modern financial market and of a modern capital market and (3) the establishment of the right of finance¹⁰¹.

It is inevitable that Chinese financial capital should decrease its unproductive investments and at the same time increase its industrial capital. However, this is only possible when the management of the Chinese financial market has been freed from the foreign yokes and the domestic fetters. The industrial securities should not be left in their narrow field simply because they are not suited to the security market. The financial market also should take preliminary steps in order to improve its industrial relations.

The Chinese security market has developed first from "the tea party" (茶會). Then it assumed the form of an association (公會) and finally became an exchange (交易所), which was established in the ninth year of the Republican regime at Shanghai. Although the Chinese security market has thus traced the stages which are universal in the history of security markets, it has had its own Chinese characteristics in all of its historical stages, namely, as the tea party, the association and the exchange. But here I shall take up a particular stage just before the establishment of the exchange. I refer to the establishment of the Peking Security Exchange established in the seventh year of the same regime. It was capitalized at one million yuan and was composed of sixty brokers. It had made a measure of business success up to

10) Chang Nai-chi: *The Problems of the Chinese Monetary Problems* (章乃器, 中國貨幣金融問題), pp. 345—346.

the time when China removed its capital from Peking to Nanking. Thus, it is possible, to be more precise, to take up this Peking security exchange in the north and the Shanghai Chinese Merchants' Security Exchange and the Shanghai Security and Goods Exchange in the south. The last named exchange was established in the ninth year of the Republican regime and was capitalized at five million yuan. Of various exchanges, it occupied the foremost place in respect to organization. It covered an extensive field of business activity and included the following seven departments: negotiable securities, cotton yarn, raw cotton, furs, gold and silver, provisions and textiles. However, it is impossible to describe its business success and, in fact, its department of negotiable securities was absorbed by the Shanghai Chinese Merchants' Security Exchange in May, the 22nd year of the Republican regime, as has been already noted. Being established in the ninth year of the regime, the Shanghai Security and Goods Exchange was a large-scale organization and dealt with securities and goods, and thereby had its special importance. However, it is the Shanghai Chinese Merchants' Security Exchange that was the main organization of its kind in entire China, especially *vis a vis* the Peking Security Exchange. We have already seen that the importance of the Shanghai Stock Exchange consisted in its business activities and not in its being a foreign organization against the similar Chinese organizations.

Let us now see whether the securities handled by the Shanghai Stock Exchange were appropriately evaluated. Whereas the rate of yielding for the Shanghai Stock Exchange was five or six per cent, that of the Shanghai Chinese Merchants' Security Exchange was usually higher than twelve per cent and very rarely below eight per cent, for six-percent bonds handled. Regarding this point, Wu Cheng-hsi (吳承禧), after comparing the yielding rate of the Chinese exchange with that of the foreign exchange, says:

"This shows us the following thing: though in the same financial market in Shanghai, a high rate of money lending

of feudal character is shown on one hand, by the native capital, while an opposite phenomenon is indicated by the foreign capital, on the other. It is easy for any one to see that under such a drastic difference in the rate of yielding between the two forms of capital, it is clear that the Chinese native capital is unable to compete with the foreign capital."

There are other security exchanges of some note at two places, namely, Ningpo (established in the 20th year of the Republican regime) and Hankow (established in the 24th year of the same regime), but their history does not entitle them to special mention in this connection. We shall here be content with centering our study on clarifying the reasons both formal and substantial of why the Shanghai Stock Exchange makes a sharp contrast with the Shanghai Chinese Merchants' Security Exchange.

4. THE SECURITY MARKET AND THE FINANCIAL MARKET

Having so far described the general characteristics of the security market in China, I shall now supplement my above description. The Chinese security market has been developed, as a matter of fact, as a bond market as it principally handled financial securities, instead of being a stock market which handles industrial securities. The reasons why the Chinese security market proved to be in reality a bond market are: first, the scarcity of industrial investments, and second, the prevalence of speculation. Both of these are considered to be the two great impediments in the process of development for the Chinese security market. This corresponds to the deformed transition of the Chinese banking development. One may indeed say that the Chinese security market has been characterized by a semi-colony and semi-feudalism, namely has been thus subject to both international and domestic fetters. The Chinese security market in fact has been a realm which can be explained in terms of both internationalism and localism in Chinese economy.

Although this deformed transition may have aided the development of the Chinese security market, there is no doubt that it has never succeeded in carrying on its mission, whether the market is taken in its broad or narrow meaning.

I shall next clarify the weaknesses of the Chinese security market by tracing the development of the Chinese bond market and the backwardness of the Chinese stock market by taking up the activities of banks and the financial measures of the Chinese Government. It is impossible to know the exact proportions of bonds and negotiable securities in the amount of credit given by the Chinese banks¹¹⁾. However, we do know this much, that the influence of the banks is centered in the nine cities of Shanghai, Tientsin, Peking, Nanking, Kuangtung, Hankow, Chungking, Hangcho and Tsingtao and the two provinces of Kiangsu and Chekiang. It is also known that the banks' connections with the domestic agriculture and industry are very weak. Considered from investments, similar weaknesses of the Chinese security market may be seen in their concentration on bonds and on landed property in Shanghai, not to mention their dependence on foreign capital and the deformed nature of Chinese trade activities. Wang Cheng-chih (王承志) is convinced that the salvation of Chinese finance lies in the reduction of investments in bonds and landed property and in the increasing attention to industrial loans as well as in the overthrow of the financial control by international capital in China. A similar thing may be said of the Chinese security market, also. The existing enhancement of the bond market and the backwardness of the stock market should be reversed, if the Chinese security market is to make an advance.

It is desirable here to explain how the security market in China has been flooded by investments in bonds which became the principal items of transactions in the security

11) Wu Cheng-hsi: Chinese Banking (吳承禧, 中國的銀行), p. 16, pp. 68-72. Wan Cheng-chih: *ibid.* pp. 18-20.

market—so much so that it virtually became a bond market. Transactions in bonds became active in the fifth or sixth year of the Republican regime, due to the fact that bonds issued by the Peking Government at that time began to draw the general attention of investors. And it was around the eleventh year of the same regime, the year of a big financial panic, that bond transactions came to attract the special attention of Chinese investors. The Chinese stock business having thus met its financial set-back at an important stage of its early development, the transaction of government bonds became the greater object of attention on the part of investors. The following usual advantages of bond transaction are not sufficient reasons for the overwhelming importance of bonds in the Chinese security market: (1) Bonds are a certain security (2) Their credit is firm (3) Their interest rate is comparatively high and (4) Their transaction is comparatively easy.

As may be referred from views expressed by Chinese economists themselves, bond transaction is carried on not because it is suited to the demands of the security market, but because it is comparatively safe, and interest rate is comparatively high. Now, this very fact clearly indicates that the security market has been dragged into the whirlpool of speculation, instead of being able to play its role of normal investment.

It is possible, of course, to detect how closely the investment relations of Chinese banks have been running parallel with bonds by taking up the business conditions of banks themselves¹²⁾. But there is one factor that very universally testifies to the above phenomenon—I refer to the time relation between the date of the establishment of banks and the time of the issue of government bonds. The very fact that many banks were established during the period between the first year and the tenth year of the Republican regime and between the eleventh year and the twentieth year of

12) Wu Cheng-hsi: *ibid.* pp. 70—81.

the same regime corresponds to the fact that during the same period many bonds were issued by both the Peking Government and the Nanking Government. Moreover, the existence of more than 400 banks and their branches in the twenty-second and twenty-third year of the regime corresponds to the issuance of a great number of government and financial bonds during the same years. Both Chinese financial circles and the Chinese financial conditions have run in the same direction and their goal was ultimately bond investment. In tracing the transition of the Chinese monetary system, the above tendency is also shown around the abolition of the *tael* and the revision of the *yuan*. Here, the relations between the Government and new banks are shown by the coalition of finance and banking activities. Of course, these relations had no normal reality and only represented the injury due to the spread of speculation over to the Chinese people. Negotiable bills possessed by banks being mostly government bonds, the proportion of stocks was very small¹³⁾. Of various bonds, national government bonds occupied the major portion, thereby indicating the close relations between the Government and the banks. It will be noted, therefore, that although the bonds are highly important for the life of Government, they had no support of the people in the market. We have already seen that the main reason for this is the monopoly of interest by the banks, the bonds being the object of their speculation. The view that the Chinese masses lacked financial ability to purchase bonds because of their economic poverty is not plausible, since what is more important than the economic conditions of the Chinese masses is the undeniable fact that the machinery of bond consumption has been speculatively monopolized. Moreover, the issuance of bonds was not prompted by productive needs but by the need of military expenditure for suppressing bandit activities. In other words, bonds were issued in a realm having no rela-

13) Wu Cheng-hsi: *ibid.* p. 76.

tion with production. This may be taken as a confession that the issuance of bonds has had the effect of destroying production itself. Furthermore, the fact already seen that the bonds stand as an object of speculation by means of interest discount betrays the unhealthy nature of bond issue.

If the employment of bank capital is made mostly in the transaction of bonds, it follows that the banks are unable to fulfill their task of developing industry through the employment of their capital. Even if their business success is shown by large figures, their inherent business mission is not executed. Let us therefore examine the proportion of capital invested by the banks in industrial securities. The general ratio between the amount of various loans and that of negotiable securities has so speedily enlarged that the amount of negotiable securities held by the various banks nearly surpass that of their paid-up capital. Of the amount of negotiable securities, bonds occupy about two-third and they have been issued for unproductive purposes. All this has made the abnormal development of the banks and their relations with the Government deformed in nature. This deformed development of the banks, controlled by the internal fetters of locality and the foreign fetters of internationalism, had to remain quite detached from intensive production.

This does not mean, of course, the absence of an intention on the part of the Government to accord soundness to Chinese finance and banking. We know that the Government strengthened its control over banks and that the general depression of the banks reflected the decline of bond speculation on their part. And yet the measures taken in connection with the issuance of bonds amounting to 100 million yuan by the Finance Ministry in the spring of the twenty-fourth year of the Republican regime had the effect of not only consolidating the banks and native banks, but failed to make any contribution to the industrial salvation of China.

Since the banks are very inactive in industrial enterprises, the mere fact that their paid-up capital and reserves have increased is no proof of their close connection with

either industry or commerce. Increases in their convertible notes should be also examined in a similar light. Increases in the amount of bank deposits also reflect inactivity in industry and commerce and show the prevalence of an idle capital. Thus, no active investment in industry or commerce could be expected, such investments being invariably only patchwork. The fact is that the banks have been aiming at securing exorbitant speculative profits by means of bond transaction, instead of making low-interest loans to industrialists and traders. High-interest deposits cannot be but high-interest loans, and industrial and commercial loans advanced by the banks could not be as desired by the banks themselves.

We have briefly surveyed government finance. We cannot find any assurance for the development of Chinese commerce and industry either in the history of Chinese finance or in the pursuit of profits by the Chinese banks. What is absolutely necessary in this connection is cooperation by which the stocks and debentures of industrial and commercial firms should become the objects of bank loans. It is because of such a necessity that there should be financial measures connecting such factors as the security market, the financial market and the open market operation.

5. THE SECURITY MARKET AND THE CAPITAL MARKET

We have already explained that in the Chinese security market, there developed the bond transaction by means of financial securities and the stock and debenture transaction were not developed by means of industrial securities. The reasons for this are as follows: (1) The basis of both commerce and industry being unsound, both investments in and transactions with, commercial and industrial securities, were of a negligible amount. (2) The rate of yielding in the transaction of government bonds being highly profitable, all idle capital has been concentrated therein.

Depression in the transaction of industrial securities in the Chinese security market is due to the following causes:

(1) The capital of the Chinese firms and factories being very small in amount, their stocks are circulated in a correspondingly small amount. (2) Company stocks are possessed by a small number of stockholders and thus the amount of stocks in circulation in the market is reduced to that extent. (3) The accounting of companies not being published, social confidence therein is not clear and this makes the market circulation of stocks highly difficult. (4) The companies themselves dislike to see the market quotations of their stocks remain below par and this is why they do not desire the market circulation of their stocks. (5) Because of the cumbersome process of transferring stocks from one person to another, their market circulation is not generally desired. (6) Business enterprises are not secured and investors are cautious in making investments in corporate stocks on this account. (7) Stock investment has been found to be unprofitable.

In a nutshell, depression in the transaction of industrial securities is due mainly to their lack of market circulation.

I have so far observed why stock investment failed to make any development in China and how it failed to make any contribution to the industrial advance of the nation. I have also noted how bond transaction has expanded into the security market. It is not denied that bond transaction consisted in the consumption of national bonds. Even supposing that the consumption of national bonds is carried on smoothly, it should be noted that the Chinese national bonds lack in construction programs, and that large figures in the amounts of national bonds issued only reflect the increased military expenditure for civil disturbances. Thus, the national bonds themselves lacked sanity. What was in the minds of Chinese investors was not in conformity with the bond policy of the Government. Moreover, as has been already noted, the banks tried to gain fat profits by their speculative interest manipulation by means of the stock

exchange. Although the Shanghai Chinese Security Exchange had its own historical development, it failed to offer any basis for industrial development by carrying on its inherent mission as a stock exchange.

The following three measures may be proposed in order to ameliorate the deformed condition of the Chinese security market and to assure its smooth activity for both bond consumption and industrial investment^{14) 15)}. (1) The Government should consolidate credit for national bonds and drive out speculation from government certificates. (2) Prosperity should be ushered into commerce and industry through closer cooperation between the Government and the people. (3) Both the banks and the stock exchanges should jointly endeavour to pay closer attention to the development of stocks and debentures in the security market. It goes without saying that the foregoing three measures bound not only to advance the security market and contribute to the smooth financial operations, but also will benefit the commerce and industry of the entire country.

To state that the amount of investments in securities is low because of the unsoundness of the Chinese commerce and industry does not clarify the sequence of relations involved. To begin with, the industrial organization of China has been largely individual in nature. Although the system of industrial corporation imported from the West has increased the number of corporate firms, their development has been so slow that some believe that the Chinese national characteristic is not suited for their development. It cannot be said that the industrial system is suited to individual management, even in China. Nor can any one say that the guild system is any better solution. What is to be stressed is the fact that social conditions in China have been so backward that the development of industry into the corpo-

14) Yang Yin-pu: *The Treatise on Chinese Finance* (楊蔭溥, 中國金融論), pp. 399—405.

15) Chang Chi-yen: *The Treatise on Chinese Finance* (張輯猷, 中國金融論), pp. 529—532.

rate system has been impossible. However, one cannot say on this account that the system of corporation is not suited to China. We have already seen an example of the inflow of Chinese industrial capital into the Shanghai Stock Exchange, a foreign institution. A similar phenomenon has challenged our attention after the outbreak of the China Incident. It has been urged from various directions that the Chinese industrial security market should be consolidated because of the following reasons:

(1) The strengthening of the stock market will increase the fluidity of stocks and thus contribute to the commercial and industrial prosperity of the nation.

(2) Commerce and industry will be enabled to make an active use of capital and thus the market operations will be enhanced.

(3) Concentration of capital will facilitate large-scale industrial and commercial management.

(4) Investment will become more convenient.

(5) The State will be benefitted¹⁶⁾.

All of these foregoing factors are interrelated and tend to act on industrial capital from the side of the security market¹⁷⁾.

6. THE RECONSTRUCTION OF THE SECURITY MARKET

A great increase was made in the amount of stocks issued and in their sales during the First European War when the organization of corporations was made actively and much development and improvement were registered in China's commerce and industry. The majority of the superior stocks were above par. Especially popular was the stock of the Chung Hwa Kuo Ming Sugar Manufacturing Company. However, all this boom due to the European War disappeared with the ending of the conflict. Moreover,

16) The Security Market in China, Economic Study (經濟研究), Vol. II, No. 8, p. 111.

17) Chen Chia-Tsün: Das chinesische Bankwesen, 1938, SS. 92—98.

the *post bellum* world depression spread to China also, resulting in the decline of popularity for commercial and industrial stocks; and all the factors for the construction of the Chinese stock market were lost.

In this connection the significance of the stock policy of the Chinese Government following the adoption of the new monetary policy should be observed¹⁸⁾. The renewal of the unified new bond in February in the twenty-fifth year of the Republican regime played an important role in the bond market. A similar effect of the monetary reform was also seen on the stock market. There were such phenomena as prosperity in commerce and industry and increases in the amount of investments in stocks, the latter in particular having the effect of stimulating positive plans on the part of the Shanghai stock market to respond to the demand for stock investments. Let us now see what effects the outbreak of the China Incident had on the Chinese stock market at such an opportune time. The Lu Kou Chiao Incident having led to the Shanghai conflict, it was only too natural that the latter stopped the transaction of stocks and bonds and caused a deadlock on the Chinese security market. Great was the blow on China's commerce and industry and nothing was now heard of the Chinese security market. At that time there were foreign exchange bills by means of the old *fapi*, while the concentration of capital, stock investments and speculative transactions and the like were all carried on by means of foreign stocks. In the words of the old Chinese regime, all this happened at the time when the value of the *fapi* had been proudly upheld on the basis of the people's confidence and monetary operations. It was said that speculative investments in foreign stocks were unprecedented in amount but that the Chinese stocks were in the same depressed conditions as they had been hitherto. Then, the outbreak of the Second European War brought about a

18) W. Y. Lin: The New Monetary System of China, 1937, pp. 103—104.

sharp drop in the value of American stocks and the strained state of affairs in the southern region further depreciated the value of stocks. There was a big upset in the speculative transaction of foreign stocks. The Chinese people came to know that even foreign stocks are not a safe object of investment, and new proposals were introduced for the revival of the Chinese stock market.

In Shanghai at present, there are tens of billions of yuan of idle capital lying in the way of speculation, while the development of regular industries is impeded by the lack of capital. Thus, there is a deep and engulfing ditch between the two. If, therefore, the plans of reconstructing the Chinese security market should materialize, idle capital could be led to the normal channels and both commerce and industry could make their rational development. It may be expected further that both could benefit each other and thereby contribute to the welfare and healthy expansion of Chinese economy.

Various demands for the Chinese security market have been manifested on every side. At the present, they may be summarized as follows: Although the Chinese stock market has been making a headway, but it is still in the condition of a dark market. Idle capital fills the Shanghai market. It has flown out of the stocks of foreign firms. Bank deposits complain of their small rate of yielding because of the reduction in interest rates, and the comparative safety of investments in Chinese stocks has been reported. On the other hand, the steady depreciation of the value of the old *fapi* has brought about a deformed development in the management of various industries. The Chinese stocks are said to be facing a hopeful opportunity for their development inasmuch as their value is above par.

The Chinese security market has failed to function as a market for corporate stocks. Nor is the field of industrial capital explored, there being ample room for further exploitation. The security market has also failed to contribute as a bond market; it has rather been speculative in nature

in the consumption of financial securities. The security market, in short, failed to conform to its construction object. Even in the field of speculation, it did not transact local government bonds.

Securities both as an asset in loaning in the financial market and investment funds are of great importance. Important, indeed, is the desire of the Chinese native capital for reconstructing the security market, inasmuch as its operation by native hands had been regarded as impossible of accomplishment. The function of negotiable securities in the financial market is very important. Not only are they transacted as an object of speculation, but the security market itself is expanded first into the financial market and then into the capital market in the present stage of economy in which capital is turned into securities. The security market should have been improved for the sanitary of the financial market. It should also function as the capital market in order that the financial market may fulfill its mission for the smooth working of commercial and industrial capital. The fact remains, however, that the security market with the existing economic mechanism as its background cannot be expected to carry out its function adequately. This is why the establishment of a new economic order is considered as imperative for the reconstruction of the Chinese security market.