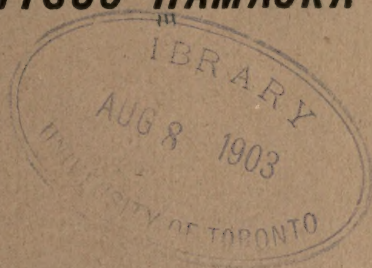


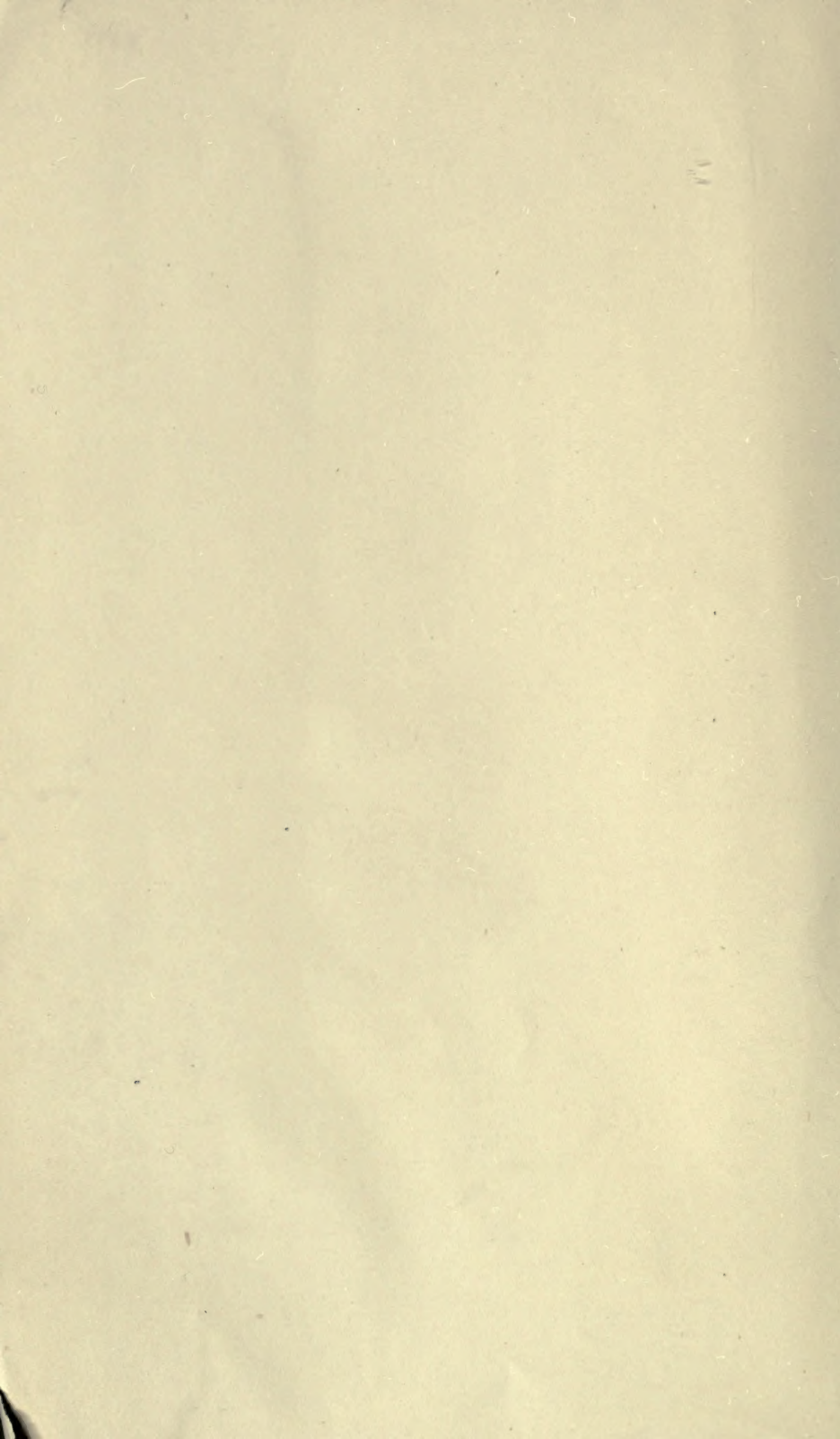
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# The Bank of Japan

ITSUO HAMAOKA




*Thesis for degree of Ph. D.  
Univ. of Michigan*



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A STUDY  
ON THE  
**Central Bank of Japan**

BY  
ITSUO HAMAOKA, PH. D.

WITH  
*Introductory Note by*  
PROF. HENRY C. ADAMS, PH. D., LL. D.

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TOKYO  
The Publishing Department of  
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1902

A STUDY

OF THE

Central Bank of Japan

BY

ITSUO HAMAKA, Ph. D.

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BY

ITSUO HAMAKA.

WITH

INTRODUCTION BY

PROF. HENRY C. ADAMS, Ph. D.

TOKYO, JAPAN,

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## INTRODUCTORY NOTE.

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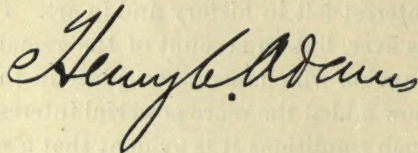
The attention of the people of the United States at the present time is drawn, with ever increasing interest, to the commercial and financial institutions of foreign countries. This is due, primarily, to the fact that the industrial growth of this country has brought her to the point when a foreign market seems a necessity. For more than a century her development has rested upon the cultivation of new lands for new crops. There has been a steady movement Westward in search of unclaimed soil for the growth of wheat and corn. This movement is now drawing to a close. The opportunity for agricultural expansion, under the old form of extensive farming, is past, and out of this fact there has sprung an increased interest, not merely in intensive farming, but in the development of manufactures without which intensive farming is not possible. This is the explanation of the new interest which the people of the United States are taking in manufactures and in a foreign market for the disposal of manufactured goods. There was a time when the attention of the American people was drawn to the institutions of foreign lands because of the interest felt in history and in art. This interest is as strong as ever, but on account of the remarkable commercial expansion which has taken place in the last decade, there is now added the more powerful interest of commerce. Under such conditions it is evident that a monograph like that of Dr. Hamaoka, upon the Bank of Japan, will claim the attention of the United States, for not only does it tell us something of the character and life of the Japanese people, but it describes an institution which may be regarded as



the highest expression of the commercial intelligence of the Japanese nation.

For another reason, also, will this monograph claim attention. The Bank of Japan, with its many branches, furnishes a concrete illustration of a highly centralized banking system, and there are many publicists in this country who advocate the substitution of such a bank for the present somewhat loosely organized system of National Banks. These will read with interest the present description of the Bank of Japan, for it must be admitted that the phenomenal success which has attended this institution is a strong argument in favor of the idea that underlies it.

It may not be inappropriate that this note of introduction should include a word of a personal sort. The University of Michigan has been a favorite resort, during the past twenty years, for Japanese students, and a very considerable number of those who have sought here an education have chosen Political Economy, Finance and Political Science as their chief work. Many of these young men have returned to their native land to assume honorable and responsible positions, and I feel in writing this note as though I were speaking a word of remembrance to my old students. To them all would I send greeting. It is with ever increasing pleasure, as the years go by, that I hear of their continued prosperity, and I trust the tie which has given me so direct an interest in the life of the Japanese people may not be broken.

A handwritten signature in cursive script, reading "Henry Adams". The signature is written in dark ink and is positioned in the lower right quadrant of the page.

March 1st, 1902,

University of Michigan, Ann Arbor, U.S.A.

## PREFACE.

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In consideration of the need of a comparative study of the economic institutions of nations, which is felt in every line of interests, the present thesis has been prepared. It is the purpose of the essay to portray the centralized bank system of Japan and to analyze the principles which underlie the system. However, this paper is not limited to an analytical presentation of the institution and its principles, but, as a result of the investigation, some suggestions regarding the national policy towards the system are also submitted.

I have to express my warm thanks to the many persons who have cordially assisted me with material and information, especially to Count Matsukata, oftentimes Minister of Finance of Japanese Government, to Prof. Fred M. Taylor of the University of Michigan, and to Dr. Y. Ono of the Bank of Japan.

ITSUO HAMAOKA.

Tokyo, Japan, April, 1902.







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THE  
CENTRAL BANK OF JAPAN.

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CHAPTER I.

GENERAL CONSIDERATIONS.

The relation of the state to the business interests of the nation appears in the State's two capacities. The one is its capacity as sovereign and the other, as an economic person. The State should in the former capacity provide the order and development of the business community as a whole, while in the latter one it cannot be free from participation in the general economic activity. The responsibility of establishing and maintaining a national currency must be assumed by the State, both in its capacity as sovereign and as an economic person. Without a certain regulation and control by the State upon the circulating medium, the order and progress of industrial society will not be maintained, condition of things which would be detrimental to the very being of the State itself. It is for this reason that the modern State assumes the function of nationalizing the currency. At least it is the duty of the sovereign State to control the uniformity and safety of circulation, either in the form of coin or in that of credit, while in the face of the public weal such control can by no means be left to the autonomy of the business community.\*

Thus the State does not only appear before the business

\* Cf. Tooke, *History of Prices*, Vol. III, P. 207.

interests of the nation as a sovereign but it has itself indisputable interests as an economic person. That is to say, the State is one of the members of economic society from which it can hardly separate itself. It must necessarily live in order to perform its many functions, however they may differ among different nations the sphere of its activity according to the various political, social, and industrial conditions. Living, as it does, in the economic community, the Government makes use of the same medium of payments as individuals and in consequence it becomes directly interested in the nature and consideration of the currency. Should one consider the greatness of public transactions within a community, he will readily see how closely the State is interested in this matter as one of many economic persons. The State as such can not remain without a certain active policy toward the currency. It is on account of its standing on the same footing as the others that the orderly payments of commerce are, without proper provision, much affected by the revenues as well as the expenditures of the Government. It is equally true that the Government is, on the other hand, not the less often influenced by commercial conditions in general. In as much as it is concerned as an economic person, the Government cannot be devoid of direct interest in the general state of industry and exchange in economic society.

Assuming the responsibility of the State respecting the national currency, both as the duty of a sovereign and the interest of an economic person, the question then arises, naturally, whether the State shall undertake the issue business. As a matter of fact, as Ernest Seyd said, "all issues of bank notes must be brought into direct contact with commercial interests and no government can issue a presumably convertible bank-note



without becoming a banker liable to all the chances of that business."\* Without entering upon theoretical considerations at length it will be sufficient for us to say that the modern State has discovered (1) that it is unable to adjust the currency volume to business conditions; (2) that it is inclined to make an over-issue of notes.<sup>8</sup> Thus the privilege of issue which the State ought to subsume, has been entrusted, under its strict control, to the hands of banking institutions.

It may be said that the issue of notes may become a source of revenue to the public purse. Indeed, "le cours forcé est ainsi devenu un des grands moyens de crédit des nations modernes."† But revenues obtained through this form of governmental credit can be well replaced by rendering the privileged banks subservient of certain public duties, either as fiscal organs or as taxpayers. Confronted by these views, most of the nations being deeply concerned with the two aspects of the State's capacity, have solved the question by establishing a centralized bank with public functions. Although there may be differences in the conditions and government of such institutions according to the condition of the various nations, yet it is none the less true that such institutions presuppose, in their very essence, a very lively sense of responsibility to the public in the performance of functions of public interest. Acting through such an organ, the State while securing the safety and convenience of the public transactions can bring little harm to the general transactions of commerce. It seems likely that undue panic can be prevented through the operation of such a centralized system with sole responsibility, more satisfactorily than in any other way. To

\* Journal of Royal Statistical Society, 1872, P. 459.

<sup>8</sup> Leroy Beaulieu, *Traité de la Science des Finances*, Vol. II, P. 634.

† Leroy Beaulieu, *Traité de la Science des Finances*, Vol. II, P. 613.

preserve the specie reserve of the nation and to maintain the standard of value can be best done by such a central bank.

The policy which Japan pursued was, in general, I believe, nothing more than to avail herself of the advantages of the system which we have just considered. A brief study, however, of the actual condition in Japan prior to the establishment of the central bank will be interesting and will also bring to view the then existent circumstances.

Japan had, before the adoption of a central bank of issue, experimented with government paper money and local banks of issue. With the restoration of 1868 the new national government had to meet a large deficit of the public revenue by issuing paper money, since the political conditions for the time, as one might imagine, did not allow other means of revenue. In addition to this, the national government, assuming the burden of all the notes of which there were over 1,600 kinds issued by nearly all the feudal lords, began to issue also its own currency to replace them. Such issues were originally intended to be redeemable, but the Government was soon unable to do its part, on account of the efflux of specie.

With regard to the fiscal transactions, there were before the Restoration a number of so-called exchange houses which used to act as the fiscal agencies of the Shogunate Government or local feudal Daimyos, and were also dealers in capital and credit. As the utilization of fiscal agencies in this manner was by no means a new thing in Japan, it is not strange that the new Imperial Government took measures to specially patronize certain firms for this purpose, soon after the change of the political organization. They received a large sum of Government money as the public deposit and had even the right of issuing certificates secured by specie. Although the fiscal trans-

actions were carried on largely through these agencies, yet they passed away before long, without having had any success. In 1871 a scheme of setting up an issue bank a capital of 7,000,000 yen was considered by the Tokyo Chamber of Commerce, but it was frustrated by difficulty in obtaining the necessary funds.

In 1870 Mr. Ito (now Marquis), then Vice-Minister of Finance, went to the United States to investigate its systems, and advised the establishment of banks after the type of the national banking system there. His advice was favored by the Japanese Government, and the National Bank Act was enacted on November, 1872. Under this Act a bank was allowed to issue notes convertible in gold, having Government bonds as their security to the extent of sixty per cent. of the issue, the remaining forty per cent. to be secured by a specie reserve kept for their redemption. The capital was not to be less than 50,000 yen. As its inflated paper money did not have a fair circulation at this time, the Government in establishing these national banks had it in view to withdraw its own notes by issuing redemption bonds, and to let the convertible notes of banks, with these bonds as their basis, fill the vacancy thus created in the circulation. For the time, however, the gold went at a considerable premium as compared with the paper, the fact being that the latter was driving the former out of the country. The Government, therefore, was disappointed in its plan. There were but four banks organized under this Act, and they could issue only a small amount of bank-notes,—less than 2,000,000 yen. The constant efflux of bullion made these banks lose their specie reserve and rendered their position untenable.

Radical amendments to the Act were introduced in 1876, by which bank notes based on Government bonds and custom duties became convertible into the Government notes instead



of the standard gold. This alteration meant evidently that the bank notes were no more convertible but simply legal tenders. At this time the issuing power of the banks was also raised, so that the amount of the Government bonds deposited in the Treasury by them was increased from sixty to eighty per cent. of their capital, these bonds being required to bear four per cent. interest. As to the reserve, what was formerly a gold reserve of forty per cent. of the capital was changed to twenty per cent. thereof, by the 'currency reserve,' as it was called, which was, of course, of Government paper money. Simultaneous with these amendments to the act there was the action of the Government in issuing bonds to the amount of more than 174,000,000 yen for payment to feudal pensioners in exchange for their hereditary rights. These facts taken together afforded great facilities for bank organizing so that within a few years a large number of national banks sprang up in rapid succession. Down to 1879 there were one hundred fifty three national banks organized throughout the country the total capital of which was 48,816,100 yen. Such being the case, the Act was again amended so that the Minister of Finance was empowered to restrict, on the basis of both population and taxation, the total issue amount of bank-notes and also the number and capital of the national banks. The amount issued of bank notes advanced by leaps and bounds from 1,750,000 yen in 1876 to 13,300,000 yen in 1877, 26,200,000 yen in 1878 and 34,000,000 yen in 1879. Besides these bank notes, as we have already noticed, there was an enormous amount of Government notes, which were increased to the total amount over 13,000,000 yen in 1878, on account of the financial necessity engendered by the South-Western Rebellion.

The results of such an inflated currency were, beyond all doubts, a rise in all prices and in the rate of money interest,

while the Government bonds lost their value. The situation inevitably brought up the question of how to secure proper regulation of the currency, from the view-point of both the Governmental and general finances. To solve this problem the idea of establishing the central bank called Nippon Ginko (the Bank of Japan) originated. Thus the Bank of Japan was called into existence to relieve a difficult situation. It will not be without interest, at this point, to contrast the two systems of the central bank and of the national banks which Japan has had in her career, because by doing so one can get, I believe, some general notions upon the Bank of Japan and especially of its historical situs.

(1) Concerning the unification of circulating notes. The diversified notes of the national bank system were oftentimes unable to circulate throughout the country with the same credit in all parts. A spirit of exclusiveness prevails to a greater or less degree among bankers. Although this inequality of credit may not be an inevitable evil of the system, the uniform note is much preferable to the other in safety and in generality of circulation throughout the community. This was especially true in respect to the greater body of the people, who were unused to such business transactions. When we look upon the circulating notes as the national currency, meant to pass from hand to hand we grant that the State should see their uniformity secured by issue from a single source. The central bank system supplies the need.

(2) Concerning co-operation for business accommodation. The serious difficulty which lay in the national bank system was the lack of co-operation among the banks. It was found from bitter experience that they were not fitted to regulate the issue either in ordinary times or in times of stringency. At times

of prosperity and confidence, they extended their loans so as to stimulate the business expansion, but no sooner was the condition reversed than each bank hurried to guard itself by contracting its own credit, even excluding other banks. The private interest of the banks could not be induced to sacrifice itself to the public interest of the business community. The lack of perfect co-operation among them was thus apt to lead to a worse condition of the market at the very time when some effective means were needed for amelioration. The late Prof. Dunbar says. "It is clear that, in banking, a republic with many competitors means not merely a divided responsibility, but at times the probability that required action will be impossible, unless some means are found of securing uniformity at the expense of individual independence,—in other words, some means of practically converting many reserves into one reserve, under a common authority, for the time being."\* To do away with the difficulty above indicated and to reap the advantages of co-operation by the national banks, Japan found it expedient to adopt the central bank system of centralized responsibility.

(3) Concerning elasticity of issue and the protection of the final reserve. The national bank system did not rest, strictly speaking, upon the business principles as to its basis of issue and was far from being conformable to the commercial demand. The system was over-taxed by a circulation based only upon evidences of the public debt, which followed the ups and downs of governmental credit. To maintain any elasticity of issue it was necessary to have notes based upon the regular business assets, that is to say, commercial papers. The credit of the Government was indeed unassailable, but it is proper in principle to make banking credit independent of public credit. The elastic issue based

\* The Theory and History of Banking, P. 80.



on business assets was to be maintained in view of the state of general market rather than that of the local market, for it was thought to have at bottom, a considerable, though not entire, dependence upon the preservation of the final reserve of the nation. Moreover, since Japanese commercial interests were of a comparative unity, action through the sole central bank was considered very practicable.

(4) Concerning the capacity of the fiscal agent. Considered from the view point of the national interest, it is a most wasteful method to let the money lie idle in the vaults. In so far as its safety and convenience can be secured in public transactions it is wise to intrust to banking institutions the custody and management of the public purse. As we have already pointed out, the Japanese Government has pursued the policy from the very beginning of employing in greater or less degree a fiscal agent in its public transactions. Keeping in mind the safety and utilization of the public money as a primary consideration, it is almost out of the question to inquire whether or not a strong, centralized bank is superior to any other banking system. For the national bank system involves necessarily a number of institutions standing on a equal footing. Wherefor, any attempt at partiality by Government in their use as its depositories may lead to serious evils. The more we consider the nature of Government money, the more we feel that its benefit, whenever it can be brought about, should be for the general market of the whole Empire. That to effect this end, the central bank system is the fittest and most efficient agent, no one can deny.

(5) Concerning Governmental supervision. In as much as the privileged banking organ is entrusted with the public interests, the strict supervision of the Government over it is necessarily required. Obviously, it was much harder for the

Government to oversee a good many independent national banks scattered throughout the country, as was formerly the state of affairs, than to oversee a single bank. Indeed, one might object that, this single bank would have a number of branch offices and agencies; there is, however, a great difference between the two systems, for, in the latter, responsibility is centralized in one bank. It is worth while to recall, at this point, what Napoleon said, "One bank is easier to watch than several."

Our consideration of the contrasts between the two systems has been confined to their respective capacity to fill the part of a national system, for its superiority in this regard was, I believe, the main reason why the Bank of Japan came to take the place of the national system. Nearly all the national banks which had come into existence have, by the present time, been transformed into private joint-stock banks and are subserving the ordinary banking functions, being of the same standing as numerous other ordinary banks, while the Bank of Japan is the sole central bank, entrusted with special privileges. Our purpose is to look at the Bank as the national organ and to examine its departments and functions from various points of interest. This great institution is a living, positive, financial organ at the center of all business activity, although its action is directed in general by law. I say living organ because it has had its evolution in the sphere of action, concomitantly with the economic and financial development of the nation; I say positive organ because it has to determine for itself its business policy, resting it upon principles of public interest, in dealing with thousands of phenomena arising in connection with commerce and industry, since the text of the law cannot enter into such details.

Putting in preface these general notions, our further study of the Bank of Japan shall be made from several points of view.

To give a prospectus of the present thesis, an examination of its organization and work will mark its starting point, because the physiological view of the organ is considered to be the prime necessity, preceding all other investigations. Following this, a careful analysis of the essential functions of the Bank will be taken up, so as to make clear the presentation of its mission as the national organ. In the third place will be traced the developmental history of the Bank whereby its action in the real business world as well as the growth of its physical structure will be brought into view. By understanding its actual development, we can indirectly picture the difference of the present situation of the Bank from that of European banks. Then comes our final consideration of what would be the best public policy towards the Bank, the present policy to be, of course, reviewed in connection with this discussion.

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## CHAPTER II.

### THE ORGANIZATION AND WORK OF THE BANK.

How is the Bank of Japan organized and in what manner is its work done are the questions which will first be taken under consideration. When we look at the Bank merely from the capitalistic side, it is nothing but a private institution of the joint-stock association sort. But it has, from its nature, a mission to perform, a public function to subserve. So is it then, from the latter standpoint, a national institution strongly backed by the Government. It is for this reason that one finds interest in analyzing its administrative organization and its work.

Though complicated in the manner of its organization, it is, carefully looked at, constituted of but three different interests of correspondent functions; namely,—capitalistic, administrative, and supervisory. These elements or organs working together in unity, the great machinery of the Bank of Japan moves forward to perform its part. Every action of the Bank should be carried on through the co-operation, directly or indirectly effected, of these three. In order, therefore, to secure a clear notion of it, our study will be made from these different sides, which our analysis has revealed.

(I) Capitalistic organization of the Bank. The Bank is a corporation with a capital, at present, of 30,000,000 yen, consisting of 150,000 shares. It is entirely private so far as concerns the ownership. On this account, the Bank does not evince much difference in its rights and duties as a capitalistic institution from other private corporations. There are, how-

ever, some peculiarities even at this point. Let us look a little further.

As with a corporation, the right of the collective body of stock-holders is represented by what is called the 'general meeting of the shareholders.' But herein there is a contrast between the Bank and others as to the capacity of shareholders. Since the Bank has public functions to perform as the national organ, the right to hold its shares is confined to those whose satisfy the two qualifications, (1) to those who are Japanese citizens, and (2) to those who have been granted a special permission to become proprietors, by the Minister of Finance. It is worth while to pay attention to the fact that the capital of the Bank is organized under such a strict requirement. The idea is evidently to avoid such difficulties as might be occasioned by an intervention of foreigners or reckless citizens, as stockholders, in the management of the Bank. Nothing will explain this more plainly than to refer to the history of the organization of the Central Bank. Japan having come into the new era with the Restoration in 1868, every sort of scheme for her material improvement was brought forward. In order to get these carried out the introduction of foreign capital became the prime desideratum. Indeed it was at this time that the foreign loans of the Government were raised and the first railway system in Japan was established with foreign capital. All minds were then filled with the exalted notion of the benefits to be conferred by an introduction of foreign capital into all schemes. Such being the case, it was hardly possible that the Central Bank, in its establishment, should have escaped the current idea. The plan was, initially, to borrow the capital from the Oriental Bank, through Sir Harry Parkes, at that time British Minister to Japan. But in view of what were to be the nature and functions of the new

institution, Count Matsukata and other officials of the Finance Department of the Japanese Government disapproved of this scheme. Accordingly, from the very beginning the capital organization of the bank was effected with the restrictions above referred to, which were declared by the Act of 1882.

Membership to the general meeting of the shareholders is limited to those who own more than 10 shares, sixty days before the time of meeting, 10 shares having one vote and every 50 shares over the said 10 adding one more, while those with less than 10 shares are excluded from the membership and, consequently, voting, right. It is said that these provisions were copied from the system of the Bank of Belgium after a comparative study of banks of the European continent.\*

The meetings are of two classes, ordinary and extraordinary. An ordinary meeting is to be held once semi-annually, while an extraordinary meeting can be convened at any time, in the following cases, (a) when proposed by the Minister of Finance or Board of Directors, (b) when demanded by Board of Audits or by over fifty members of shareholders.

According to the "Business Report of the Bank for 1898," 150,000 shares, of which 69,660 are owned by the Imperial Household, are held by 876 persons; on the average, each person holding over 170. Setting aside for the moment the largest proprietor, the Imperial Household, it is noticed that 80,340 shares are distributed among 876 persons, each owing over 92 on the average. Proprietors of over 100 shares number 206, representing one-fourth of the whole body. It seems at present to be a fact that proprietorship in the bank is extensively distributed among the people. When we consider how slight has been the change through successive years in the whole number

\* Octave Noël, *Les Banques d'Émission en Europe*, P. 222.



of shareholders and that rather towards its increase, it can be seen how confident are the proprietors in the Bank itself. Moreover it is not too much to conclude from the above statement that those shareholders are free from any speculative interest in the enterprise. Finally it will be interesting to examine what proportion of the shareholders common banks constitute, the Bank is looked upon as the higher financial organ set over the other banks. 10,564 shares are owned by such banks, sixty-five in number, which constitute one-eighth of all the shares not held by the Imperial Household. Thus is it seen that the influence of banks as shareholders in the Bank is for the time being quite insignificant. We shall not here discuss the common attributes of shareholders, because as to such the Bank is similar to an ordinary corporation.

(II) Administrative organization of the Bank. Our study will proceed to the administrative side of the organization. By administration is meant, the government of the Bank. What gives to the study of the bank as an administrative organ an interest greater than that of its two remaining aspects is, that through its administration its work is carried on. To effect its administration there are three important boards in the Bank, namely, (a) Board of Directors, (b) Board of Audits, and (c) General Council of the Bank.

(a) Board of Directors. The Bank is Governed by the Board of Directors which consists of the Governor, the Deputy-Governor and four directors. It meets every day and transacts business. The Governor and the Deputy-Governor are appointed by the Government for the term of five years, but their expenses devolve for payment upon the Bank. They are reappointable at the expiration of their terms, and in practice this is usual, as is shown on nearly every occasion. Being entirely denied the

privilege of enjoying other official positions or professions during their terms, they are required to devote themselves entirely to the government of the Bank. They are officials in the strict sense of the word, but are not subjected even in the slightest degree to the civil service regulations. They are experts in banking business. The Governor presides over each meeting of the Board of Directors, the General Council of the Bank and the General Meeting of shareholders, and stands as the chief executive, carrying all the proceedings of the above meetings into effect.

The Board of Directors decides upon all questions arising in connection with the Bank, except what is already determined by law or by-laws. Such being the case, the Board takes authoritative action, and is entirely responsible for all the administrative transactions. The constitution of the Board requires the presence of more than one-half of its members in making a quorum. The casting vote belongs, of course, to the president of the meeting. When the Governor does not favor a decision of the board of directors, he has the power to refer it to the General Council of the Bank for their consideration. More than that, he is authorized, in cases when he finds it contrary to the Act, the By-laws, or the interests of the Government, although such cases seldom arise, to suspend action upon the decision of the Board or Council and to present it to the Government. In such instances, he shall act according to the instructions given by the Government; when no instruction on the other hand is rendered within thirty days he ought to execute the original decision of the Board or the Council. From this analysis, we see that he has, so far as theory goes, no final authority simply because of his conspicuous position in the Bank, but acts only as a member of the Board, or, more exactly, as the presiding officer; for the

final, authoritative decision lies with either the Government or the Board. The principle of organization recognized is, "the Governor in the Board," not apart from it. Whenever he finds it necessary to act separately from the board or the council, he must be directly under the Government, acting as its agent. In this way, however influential be his prestige, he is kept far from a position of absolute responsibility as the sole, independent authority; at least in the view of the law and by-laws, strictly interpreted.

The Deputy-Governor not only assists the Governor in every line of business, but acts as one of the members of the Board of Directors. The position has been often vacant in the past, but it is filled at present. According to the Yokohama Specie Bank Act, the Minister of Finance may direct the Deputy-Governor when necessary to occupy, at the same time, the position of president of the Yokohama Specie Bank, which is the sister institution to the Bank of Japan and acts as its agency in foreign countries. In a word this provision has as its aim to complete the co-operation of these two Banks or rather to make the one perfectly subservient to the other as its foreign agent.

Directors are appointed by the Minister of Finance from the two candidates nominated by the general meeting of shareholders. A candidate is required by the provisions of the by-laws to be a proprietor of over 100 shares which are to be deposited in the Bank, when he is appointed, as a guarantee of his business responsibility. The term of directors expires in four years, only one director being retired each year, and a re-election of the same person is allowed. Thus the inexperience of all new directors is obviated. They are strictly forbidden from having any connection with other banking or business institutions. Thus, not only is their responsibility centered about



one institution, but impartiality in judging of the operations of the bank is thus guaranteed. It is the notion of many that the directors are, contrasted with the Governor and the Deputy-Governor, representative of the capitalistic interest in the administration of the Bank. It may be so, but it should also be noticed that the selection of the directors is not entirely free from the Governmental control. There is no need to thus set the administrative interest over against the capitalistic, though indeed such a case of conflict between the interests, capitalistic and public, is barely conceivable from the nature of the organization. However, there is a way, as we have seen, to eliminate the difficulty if it occurred, but in fact no such circumstance has ever actually arisen.

(b) Board of Audits. This board consists of from three to five auditors elected by the general meeting of the shareholders, the only qualification of eligibility being ownership of over forty shares. Their term is three years and they are required to deposit the forty shares, the same as in the case of the directors. As with the other officers, to have relations with other business outside the Bank is entirely prohibited them. The board usually meets once a week, at least, and has as its duty to inspect the business condition of the Bank and to examine its accounts and book-keeping. It is also required to consider subjects presented by the Governor. Their most important function is, however, overseeing the business of the Bank, as presented from the capitalistic side. Whenever the Board of Directors desires to adjust the rates for discount and loans, any change must gain, before taking effect, the acquiescence of the Board of Audits, though within these limits: that such change may, in exceptional cases, take immediate effect without action by the Board of Audits.

The Board of Audits cannot be convened in the absence of two or more members. In case a decision of the Board fails of a majority, it is then referred to the General Council of the Bank for its determination. Also when the Board cannot be convened on account of absences, though its decision is needed without delay, the General Council of the Bank may take its place, but only in such a case. We have thus referred to another organ of the administration, called the General Council of the Bank. Let us discover its organization and work.

(c) General Council of the Bank. The council is made up of the Governor, the Deputy-Governor, Directors and Auditors, so that all members with full responsibility for the whole management of the Bank both, to the Government and to shareholders, here assemble. The subjects set before this meeting must be submitted, as a rule, by the Governor, but by agreement of a majority of the members subjects may be introduced, not initiated by the Governor. Among others the following important matters of the Bank are required to be referred to this meeting:—

(1) Review of the business policy of the Bank once every month.

(2) Statement of the amount of dividends and grants of the bonuses to all Bank officers.

(3) The custody of objects of value and documents deposited with the Bank.

(4) Attention to all the inner regulations necessary to execute the business of the Bank.

(5) Plans for the establishment or abolishment of branch or sub-branch offices and agencies.

The last four subjects can not take the form of actual proceedings unless they are approved by the Minister of Finance.

A meeting of this council can be held only with a majority of the board of directors and of that of audits present, an exception to which rule is necessarily allowed in the case of its taking the place of the Board of Audits, a circumstance to which we have already referred. It meets usually once a month, but it is so regulated that whenever necessary it may be convened.

So far as the execution of the policy and the management of the business are concerned, they are entirely entrusted to the Governor, with the help of the directors. No other persons have to share the responsibility of action, while, as has been pointed out, all the essential business of the Bank comes finally under the deliberation of the General Council. It is the final authoritative board in the determination of the Bank's policy, and to check its decisions nothing remains but the power of the Minister of Finance.

We have already referred to the machinery through which the business policy of the Bank is determined in general. It is obvious that the Governor must needs use a great system of subordinate functionaries in performing the actual work and administration of the Bank. This system is well adapted to the functions of the Bank as the centralized institution, so that through its workings, the great rôle of the Bank becomes readily patent.

At present, the development of the Bank has necessitated the following departments, through which the daily transactions are very systematically carried on.

- |                             |                                |
|-----------------------------|--------------------------------|
| (1) Examination Department, | (5) State Treasury Department, |
| (2) Business Department,    | (6) Secretary's Department,    |
| (3) Teller's Department,    | (7) Securities Department,     |
| (4) Issue Department,       | (8) Accountant Department.     |

The present system of the organization came into effect to-



wards the beginning of 1899, when the Examination Department was first established. The control of each department is entrusted to its chief who is entirely responsible to the Governor of the Bank in the execution and arrangement of all the business of his own department. The work of the branch or sub-branch offices of the Bank is carried on in the same way. The chiefs of departments and of the branch or sub-branch offices may, on an occasion of necessity, be present at the Board of Directors, although they are not granted the voting power. Within a large department, bureaus can from time to time be established as its sub-divisions, each having a chief who is necessarily under the supervision of the chief of the department. As the relations between the head office, and branch or sub-branch offices and agencies become more and more complicated, with the development of the Bank as a whole, the greater necessity was there for the unification of business and quick action on the part of all administrative organs. The Bank of Japan paid so much attention to this point that she established recently the Examination Department, with this main reason in addition of other minor ones for its establishment. To this end, occasional inspections are made into all departments of the head office as well as of all other minor offices and agencies. Thus the whole system of the Bank administration throughout the country acts under one centralized control. There are three to five inspectors especially appointed with higher powers in the Examination Department. The chief of this department may organize a council of inspectors for the consideration of all business of an important nature in this line, whose decision is directly communicated to the Governor. Besides inspections, among other interesting works carried by the Bank, are, a study of all regulations of the Bank, the preparation of the business statistics of the Bank, statistics and

investigations of economic features at home and abroad, and the compilation of business reports,—all the functions of the Examination Department.

Since the practical business of banking proper is carried on in the Business Department, the activity of the Bank centers here. It is natural that the eyes of the whole business world should be directed upon the transactions of this department, for the business policy of the Bank presents itself in actual vital form through this machinery. Moreover, on the side of the Bank itself, whether it is to be a paying or losing investment is largely dependent upon the action of this department. Directing our consideration to the other parts, the organs especially provided on account of the peculiar functions of the central Bank are, the Issue Department and the State Treasury Department; while the former refers to only the mechanical work of the Bank's function as note-issuer, the latter assumes charge of the public money in the place of the Treasury of the Government.

There is one more feature of the Bank's organization that deserves notice. Whenever the Bank sees the necessity of an elaborate, broad investigation of a practical question of great financial importance, in connection with the higher functions of the central Bank, it provides for a body, temporary in its nature, and organized outside the ordinary machinery of the Bank. This body consists of members appointed by the Governor of the Bank, usually from chiefs from its departments or bureaus. They are supposed to be specialists in finance and economy. The Bank had an instance of such investigation as a consequence of the late War with China. The question arose how to manage, and also how to introduce into the country, the indemnity money received from China at London to the best advantage of the nation. The organization which we have above portrayed is

evidence of the caution observed by the board of directors in mapping out the policy of the Bank, which is growing into a lively sense of its responsibility as it becomes a potent factor in the financial market. Over one thousand persons, so it is reported, are employed altogether in the Bank, with whose assistance the Governor manipulates the whole vast machinery of the great central Bank of Japan.

Related to the administration of the Bank, there is one more organ. I refer to the so-called Committees on Discount. The by-law of the Bank says that such committees must consist of more than three persons and should be elected by the General Council of the Bank. It is also provided that places of such committees may be filled by the auditors. Their function is to examine bills; when they find these to be satisfactory for discount, the matter is presented to the Governor. In face of the fact that discounting commercial papers is the chief business of the Bank nobody can doubt the desirableness of a careful examination of bills. However, I can hardly see why it requires a special organ consisting of elected members. To my mind the work of these committees could be better and more reasonably undertaken directly by the members who incur the responsibility for the business of the Bank, such as directors. But this question is not of much importance relative to the system itself when considered from the view point of organization. Consequently a further discussion upon it will not here be entered into.

(III) Supervisory organization of the Bank. When we speak of the supervising agencies of the Bank, the matter may assume a two-fold aspect, viz. :—the capitalistic and the governmental. As the organ of the former side, there is a body called the "Board of Audits" which, elected from the share-holders, has the duty of supervising all the business, the accounts, of the



Bank. But we have already considered that organ, because it has an administrative nature the no less than a mere superintending character. Moreover, auditors are regularly members of the General Council of the Bank which is of great importance so far as the determination of the essential business goes. Therefore, what I intend to say under the present head refers exclusively to the supervising organization over the administration, viewed from the stand point of the public interest.

It must be borne in mind that the Bank is a national institution in its final make-up differing from other banks in a good many points. For this reason, the Government especially superintends all the business of the Bank and has the power even to suspend its operations, whenever contrary to the Bank Act and the by-laws or against the best interest of the Government. The Minister of Finance has not only such control over the Bank's officers as we have indicated, but also is personally influential at the Bank because upon him devolves the Governmental responsibility of executing the Bank Act.

For maintaining its supervision over the Bank, the Government has two means, according to law; namely, (a) Reports required to be made to the Minister of Finance, (b) An official organ called Comptroller.

The Bank of Japan must make reports at least once a month in detail concerning the business conditions obtaining at the head office and branch or sub-branch offices and agencies. The spirit of this regulation involves the incessant supervision of the Minister himself over the Bank. In a single word, all the transactions, whether of greater or lesser importance, which take place in the Bank, are required to become immediately matters of information for the Minister. Needless to say, that the Bank is, by such constant reports, made aware of its responsibility for the

proper correlation of its assigned functions and the public interests. As to the part of the Minister of Finance, it is his duty, if there be found in the reports any evidence of attempted violation of the law or national policy, to effectively enjoin the Bank from such action.

However effective supervision through reports may be, it is an indirect way, so to speak, negative rather than positive in method. The establishment of the office of comptroller finds therefore ample excuse from the need of a more positive check. No sooner was the Bank established in 1882 than a comptroller was appointed by the Government. With the rapid development since the foundation, the functions of the Bank as a fiscal agent had grown to such an extent that by August 1889 it was found necessary to add two more comptrollers for purposes of inspection and supervision. At the present time the three comptrollers are appointed from among officials of higher position in the Finance Department of the Government. August, 1888, precise instructions as to duties and powers of the comptrollers were furnished them by the Minister of Finance. The instructions read as follows:—

(1) The comptroller of the Bank of Japan should visit the Bank once every month for the inspection of the business transacted in all its departments and the examination of its books, chests, etc.

(2) The comptroller of the Bank of Japan is authorized to ask, whenever necessary to the discharge of his duty, for written statements of the condition of the Bank signed by the Bank authorities.

(3) The comptroller of the Bank of Japan may be present at whatever meetings are held by the Bank and may express his opinions.

(4) The comptroller of the Bank of Japan shall immediately inform the Minister of Finance whenever he recognizes any business operation of the bank as being contrary to the law, the by-laws or the interest of the Government.

(5) The comptroller of the Bank of Japan is empowered to present his opinion to the Minister of Finance upon improved methods of executing the business of the Bank.

The duties this functionary has to perform are so plain from the instructions which we have just quoted that it will be useless to dwell upon the subject any further. There is, however, one feature of the instructions which deserves especially to be called to our attention. It is the fact that the comptrollers have power to attend any authorized meetings of the Bank and to express freely their views. They will, therefore, be able to discuss any important matters of the Bank, either in the Board of Directors or in the other councils, so as to influence the business policy of the Bank and especially to give to the consideration thereof the Governmental view. Yet as the voting right upon any decision is not granted to them, authoritative action devolves, of course, entirely upon the Bank officers themselves. An interchange of the ideas as between the Government and the Bank is thus most effectually brought about. Such an arrangement must be of inconceivable value. Moreover, since the Minister of Finance has the final veto power upon the Bank's action, a way is thus provided in which it can be discretely and effectively exercised.

Through both the reports returned by the Bank and by the controllers, the Minister of Finance is rendered a full knowledge of the actual condition of the Bank and is thus enabled to perform the Governmental supervision under which the Bank is required to act.



Thus far we have considered the organization and work of the Bank. Let us now examine the difficulties that may very probably arise from the nature of the organization. The difficulties will proceed chiefly from the fact that the Governor of the Bank has, as has been pointed out, no power of final decision. Mention has already been made of the possibility of conflict between the Governor and the General Council of the Bank, in which instance, however, since the Minister of Finance has the final voice, all serious difficulty is effectually obviated.

There are, however, other classes of difficulties which may arise: (1) Either between the Minister on the one hand and the Governor on the other, (2) or between the Minister, and the Governor, supported by the General Council. The former case is quite analogous to the one which we have been discussing, but the latter may well prove serious. Hence let us consider it for a moment. Here we see the Governor strenuously endeavoring to carry out a line of policy against the Finance Minister's opposition, which will be based on the ground of public interest. Such conflicts will be simply practical differences of opinion as to what should be the policy of the Bank. Otherwise, no reason for difficulty will exist. As to the out-come of such a struggle, one writer says: "Besides appointing the president (Governor) and directors, the Government can direct the general policy of the Bank, the president having no alternative but to resign if he does not approve of his instructions. Indeed such a case happened. A conflict may occur because of the personality of the Minister and the president. If the former be a man of strong will, the Government policy will carry the day, but if the latter be stronger, the interest of the Bank and share-holders will prevail. These two interests, however, seldom come into

conflict, because the Government acts with moderation and the Bank for the public good.”\*

The difficulty may end with the resignation of the Governor, but it involves a broader and more important question as to the business policy of the Bank. It seems to me that any such difficulty comes from a confusion as to the proper distribution of responsibility between the two men of highest authority. Our solution of the difficulty will, however, be postponed to another chapter. At present it will suffice simply to present the nature of the difficulty.

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\* A History of Banking in All the Leading Nations, IV, P. 470.

## CHAPTER III.

### THE ESSENTIAL FUNCTIONS OF THE BANK.

Before entering upon the statement of the main problem of this chapter perhaps I might be allowed to make one or two side remarks. Of the great functions of the bank I discover three which are, in my view, absolutely essential from its nature as the centralized institution of Japan; but one must not think I draw the dividing line too rigidly. As a matter of fact, there is no distinct demarkation between them, because they are so related each to the others that the performance of one function necessarily involves that of the others in most cases. What we desire, however, from such division of functions is merely to point out the distinctive significance of each in order to comprehend which is vitally important in our study of the function of the Bank as a whole. The three significant functions of which I make classification are (1) its function as the note-issuing organ, (2) as the fiscal organ, and (3) as the economic organ; following the order of this division our investigation shall proceed to a careful analysis whereby the fundamental idea and mission of the Bank itself will be made clear.

#### I. THE BANK AS THE ISSUE ORGAN.

The Bank of Japan is, at present, the only issuer of circulating notes in Japan and is the regulator of the currency volume of the nation.\* In consequence of its position as such,

\* As to Formosa, the Island being under the especial conditions, both commercially and socially, for the time being, an institution of issue called 'Taiwan Ginko' (the Bank of Formosa) was recently established under a similar arrangement to that of the Bank of Japan.



it is also the guardian of the metallic reserve of the whole empire, upon which rests the circulating system of convertible notes.

It maintains the very foundations of the complicated system of modern commercial credits, which is, doubtless, the main factor in promoting the enormous development of Japan's commerce and industry. Founded with this intent, the Bank supplies the notes which constitute the circulating medium for the daily transaction of all classes of the entire community. In view of the fact, one is able to see how the Bank of Japan is, like the central banks of the other nations, subjected to a great responsibility at this point. Its function as the issuer and regulator of notes is just the most indispensable element in its make-up as the central Bank of the empire. How the Bank acts to fulfill this responsibility is the question which we are to consider in the present part.

To any system of national finance, there are these two important requisites: (1) the maintenance of the convertibility of the notes of the system, i.e., a stable credit system; and (2) an elastic regulation of the currency volume, in accordance with the business demand. The Bank of Japan came into existence to attain these purposes. The "Bank of Japan Act" says the Bank has the privilege to issue 'convertible Bank notes.' The privilege, however, was not to be exercised until another regulation with respect to the circulating notes went into operation. This regulation was called the 'Convertible Bank Notes Act,' enacted on May, 1884, two years after the Bank was founded. Under this act the Bank began to issue its notes in May of the following year. The notes are convertible at any time into specie either at the head office of the Bank or at its branches, and are legal tender, with a free circulation, for taxes, custom duties, and all other dues.

Our attention shall be directed, in the first place, to the process by which the Bank came to monopolize the sole power of issue and regulation. At the time when the Bank was organized, in 1882, there were two sorts of notes in circulation in the country: namely, the Government notes and the National Banks' notes. Prior to the organization of the Central Bank, a financial measure of greatest import in the economic history of Japan, was adopted by Mr. Matsukata, the Minister of Finance, who took his office, avowing his policy. He began to contract the currency on October, 1881, so as to reinforce the stability of credit, the lack of which was indeed the chief hindrance to an orderly advancement of commerce and industry. Before this policy of contraction was adopted there prevailed great mistrust as to condition of the currency. It was thought that the premium on silver over the paper currency, at this time, was not due to the depreciation of the paper but to the appreciation of silver. The remedy was to be, consequently, to increase the quantity of silver rather than to diminish the volume of paper. In other words, men were not wise enough to perceive what were the results of inconvertible paper money, but, on the contrary, they were still inclined to expand its volume. In this misinterpretation of the financial phenomena of the times they tried to do away with the existing evils, but in vain. The evils were so fundamental and deeprooted that such homeopathic treatments were ineffective. Count Matsukata dared to carry on the contraction despite the temporary embarrassment of certain trades which had maintained thus far an apparent prosperity. The whole amount of paper currency outstanding at this moment (October 20, 1881) was as follows:

	yen
(a) Government paper money ... ..	105,905,212
(b) Gov't paper money issued as a temporary relief of the Treasury deficit of the current year. ... ..	14,500,000
(c) National banks notes ... ..	34,398,030
Total ... ..	154,803,242

The Government paper money of the second kind above mentioned was replaced in 1884 by what was called "Treasury Notes" (Exchequer Bills), similiar to those employed in the treasury management of civilized nations. Accordingly, this class of paper money no more appeared in the market, since it was entirely withdrawn from circulation in January, 1883.

As to the Government paper money, it was thought that the establishment of their convertibility was the first thing to be done, and the gradual retirement of it should take place while the Bank-notes should supersede them. In order that this program might be carried out, two things were mutually essential:—(1) The restriction of Government paper, and (2) the accumulation of a specie reserve. As the first step toward realizing these conditions the Minister of Finance thought it best to secure a surplus revenue, by which operation his objects could be obtained. Thereupon in 1882 and 1885, the tax reforms were achieved by him which afforded an increased revenue, while, on the side of expenditure, the most stringent possible system of economy was inaugurated. The annual surplus thus derived was used, one-half for the redemption of the Government notes, and one-half for purchasing bullion. At this time, the Government spared no effort to absorb specie from abroad by encouraging the exportation of domestic products. Thus it became apparent that the specie reserve of the Treasury was



increasing to a considerable degree, while the paper currency was, on the other hand, contracting. The figures for the specie reserve were 7,000,000 yen and 8,600,000 yen, respectively, for the end of 1880 and for October of 1881, just previous to the inauguration of the new policy. At the end of the same year, 12,700,000 yen had been accumulated.

The endeavor of the Government was rewarded with a gradual appreciation of the silver price of the paper currency. The parity between the two having been thus brought about, the Government declared that its notes would be convertible after January, 1886, and the business of their conversion was assumed by the Bank of Japan. In this manner, the redemption of the Government notes went on very smoothly and the amount left unredeemed by the end of March, 1890, was only about 40,000,000 yen. To provide definite means for the redemption of the entire amount of outstanding notes, the Government established a special fund. Out of the 40,000,000 yen mentioned above, the amount of notes of denominations above one yen was about 32,000,000 yen, while the remainder about 8,000,000 yen consisted of the subsidiary paper money of denominations below one yen. The latter amount the Government took measures to redeem by an annual appropriation from the general fiscal account, making the process a gradual and continuous one from that date down to the end of the fiscal year, 1898. For the redemption of the former amount, a special fund was provided which consisted of the Government reserve of 10,000,000 yen and a sum of 22,000,000 yen borrowed without interest from the Bank of Japan, both together making 32,000,000 yen. The redemption carried on by this method left the unredeemed amount at the end of March, 1898, only 6,000,000 yen. In the same year, therefore, a law was passed which announced the Government notes to be out of circulation by

December, 1899. This is a brief account of the process followed in the retirement of the Government notes.

As we have said, there was another sort of notes besides the Government notes. It was the kind issued by the national banks, numbering over one hundred and forty. The entire amount handed over to them by the Government, according to law, was roughly estimated at 35,000,000 yen. The Bank of Japan, as has been said, was established with the purpose of assuming the entire power to issue notes. Stability of credits and the unification of the national currency being then the established policy of the nation, no delay in the furtherance of this end was permissible. Accordingly an amendment of the law (National Banks Act) was adopted on May, 1883, enacting that the power of issuing notes should be withdrawn from the national banks at the expiration of their charters. However, here arose a difficulty. For, if the banks, under the text of law, should retire their notes at the very moment and not at all before or after the extinction of their legal capacity, such action would evidently occasion a violent change on the financial market in the volume of currency. And as a privilege of issuing notes for twenty years had been granted them, the Government could not oblige them to reduce gradually their issues during that term except it made them some desirable return. The Government considered several measures relative to this point and finally determined to transform these national banks into the private banks of the ordinary character at the expiration of their charters, and to exact of them the gradual redemption of their notes during their chartered terms, imposing however no hindrance upon their business activity. On this basis the process of the retirement of the national bank notes were regulated as follows :

(1) As a fund for redeeming its notes, each national bank should deposit, during its chartered term, with the Bank of Japan, all the legal reserve kept against its issue.

(2) It should also deposit semi-annually out of the business profits, for the same purpose, with the Bank of Japan a sum of 2.5 % per annum of its entire amount of notes.

(3) On the other hand, the Bank of Japan should convert the national banks notes at any time into a national currency, at the pleasure of the holder.

(4) The public bonds deposited with the Treasury as securities of the issue should, in such amount as the notes were redeemed, be returned to the national banks.

The Bank of Japan was thus obliged to purchase the Government bonds with a sum deposited by the national banks, and with the interest raised from these bonds it was to redeem the national bank notes. If there should be as a result of this process, at the expiration of a charter, any amount left unredeemed, it should be supplied by a sale of the Government bonds obtained by the Bank of Japan in the way indicated. It will be worth our while to mention what was said by the Finance Minister as to the advantages of this methods: (1) No banking capital nor business action of a national bank will be affected by this means because note liabilities of the bank will be taken away with a gradual redemption by the interests produced from the reserves, the employment of which had been originally prohibited by the Act. (2) The notes issued will be practically returned to the issuing bank converted into the national currency, and the Government bonds deposited with the Treasury, and the reserve, will, without any change, be the bank's own. (3) Such disturbance will be avoided as would be occasioned by the redemption, all at once, of an enormous amount of national



bank notes. (4) There will be a convenient method provided for unifying the circulating system, with the volume of paper currency reduced to the proper amount.

The redemption of the bank notes carried on in this manner left the unredeemed amount at 20,000,000 yen by the end of 1895. It was in 1895 and 1896 that a violent discussion arose in the Imperial Diet upon the question of continuing the existence of the national banks. Why did such a question arise? Because the national banks found themselves unable to obtain as liberal a fund to redeem their notes with as had been estimated at the outset. This inability of the national banks was brought about, it was said, by the conversion of Government bonds bearing 6% interest to 5% bonds. For the redemption fund, as we have seen, was to be provided largely from the interest accruing off the Government bonds bought for this purpose. Indeed, the estimate of redemption was made a few years prior to the time of the conversion of the Government bonds, which was carried out in 1886. Therefore, it was contended that the existence of the national banks should equitably be extended, so that any loss to the banks by the conversion of the notes would be obviated. Those who insisted upon the extension of the charters assumed that the Government was responsible for the failure of the national banks to have completed the redemption and thought it reasonable to have the national banks saved from an unexpected loss, while the opponents of the extension maintained that such an extension would necessarily mean a change of the established policy, which had obtained since 1883. Avoiding a review of the arguments of either side, any further, interesting as they are, it will be sufficient for us to note the settlement arrived at. A law was passed, providing that any deficit in the fund for redemption should be loaned by the Bank of Japan to the

national banks without interest. Thus the circulation of these notes was limited to December, 1899. As to the national banks, most of them were transformed, under the particular law, into ordinary banks at the expiration of their chartered life.

While the withdrawal of both Government notes and the national banks notes was thus being carried on, the notes issued by the Bank of Japan took their place of and so came to monopolize the right of issue entirely,—a change which was brought about in accordance with the law called ‘Convertible Bank Notes Act,’ to which we have already referred. What was the principle of the note issue at that time, and to what it was later altered, are now questions for our study. This lies at the very basis of the national circulating system and indeed imposes the only regulations which the Bank is obliged to regard, so far as its issue is concerned.

By the Act of 1884, it was provided that an adequate amount of silver should be reserved in the Bank against the notes issued. There was no definite proportion to be maintained between the specie reserve and the notes issued, but this matter was left to the discretion of the Bank authorities.

The Act was, however, amended on July, 1888, in such a manner that the principle of issue was clearly set forth and the Japanese system was in large part based upon the German system, although there are some differences between the two. From this time down to the present the law has remained unchanged so far as concerns its principle. The Bank notes issued since this amendment are of three kinds: namely, (1) the notes issued on specie reserves; (2) those issued on securities and business assets within legal limit; (3) those issued on business assets beyond the legal limit.

(1) The notes issued on specie reserves. Every note issued

by the Bank must be secured by a corresponding sum of specie, except those issues especially provided for by the law. Similarly to the English and German systems, there is no limit to the amount of notes that may be issued, covered by specie. The reserve consisted, in large part, of silver until the gold standard was adopted on October 1, 1897. Since then, however, this is substantially gold although silver may be kept to an amount within one-fourth of the whole metallic reserve.

(2) The notes issued on securities and business assets within the legal limit. Public bonds, Treasury notes, and other excellent securities, as well as commercial bills, are mentioned as securities of issued notes under this head. The maximum amount that may be issued of this sort of notes was limited to 70,000,000 yen in 1888 when the Act was passed. But there was imposed this condition, that the outstanding circulation of the national banks notes were to be reckoned in this amount. The law provided that 27,000,000 of the above 70,000,000 yen of notes issuable should be availed of only as the National Banks notes were retired after January, 1889. The intention was that the vacancy thus created should be gradually filled by the Bank notes and so the volume of currency would be kept right. The limit was, however, extended to 85,000,000 yen on May, 1890, and again recently to 120,000,000 in 1899, to meet the business expansion that succeeded the Chino-Japanese War.

(3) The notes issued on business assets beyond the legal limit. This kind of issue is what is called the emergency issue. If any issue beyond the legal limit were absolutely prohibited, such limitation might occasion serious difficulties, particularly in critical times. In order to obviate such calamities the German system of an elastic limit was adopted. England, as we all know, used to suspend her Bank Act in the cases of panics. But in



view of the fact that panics start, in most cases, as a psychological phenomenon rather than anything more substantial, the system of elastic limit has this superiority over the other, in that it is able to pre-check a crisis before it arises. The law provides that the Bank may issue any amount beyond the limit, whenever the business market demands such action. It must not, however, be without certain checks upon a reckless issue. There are two, I think, in the Japanese system; one is the requirement of authorization at the hands of the Finance Minister and the other is the payment of an annual tax whose rate is not less than five per cent. upon the excess.

Thus it appears at bottom that all uncovered notes, whether notes issued within or beyond the legal limits, are issued at the authorization respectively either of Legislation or Administration. The power to determine whether or not the market necessitates, when the Bank proposes it, the issue of emergency notes, is conferred upon the Minister of Finance. Fortunately, there has been hardly a single case in which the Minister and the Bank differed as to their views on this point. A tax on the excess, only the minimum rate (5%) of which provided by law, is subject to the discretion of the Finance Minister, who shall fix it according to the condition of the money market. Herein there is a difference between the Japanese and German systems, for in the latter the rate is fixed at five per cent. This is a difference worthy of notice, one which is, however, very commonly overlooked by writers.\* This is a necessary measure, particularly in a country like Japan where the rate of interest quoted is sometimes quite high, for securing the instantaneous withdrawal of

\* See Conant, *History of Modern Banks of Issue*, P. 439; *Special Consular Reports of U. S.*, Vol. XIII, Part II, P. 337; and *The Bankers' Magazine* (N. Y.) Vol. LVIII, No. 4, P. 517.

superfluous notes when the necessity is over, whilst preventing a sudden stringency of the money market. But also when we consider the matter merely from the theoretical point of view, free from practical considerations, there will be conceivable the case of the market-rate's becoming so low that a five per cent. tax may result as a prohibition of the note issue. For the sake of the theory, therefore, it is desirable, other things being equal, to provide an Administrative authority which may lower the rates below the five per cent. in certain states of the market, although this consideration is not of much import practically at present. From this analysis, it is seen that in the Japanese system, at least from the spirit of the law establishing it, the final responsibility devolves upon the Minister of Finance.

By means of this emergency issue the Bank can give accommodation to the business community whenever such is of paramount necessity, and in practice it has often made use of its power, without any question by the public as to the convertibility of its notes. Thus the Bank is fairly well adapted to meet the varying demands of trade, while, at the same time, the system avoids all injury to commerce. "This is especially indispensable in the case of Japan, where for the reason of her geographical situation specie cannot be called in from abroad to respond to the immediate demand of trade."\* In most instances the tax rate on this sort of issue was five per cent., but there were some occasions where the Minister of Finance made the rate higher. For instance, on November 1, 1897, the tax rate was increased from six per cent. which was already higher than the minimum rate, to seven, while the Bank's rates on discounts and loans were in this time respectively at 2.2 and 2.4 per day.†

\* Bankers' Magazine (N. Y.), April, 1899, P. 543.

† Interest counted so much a day per hundred yen, 2.4 means two 'sen' and four 'rin' for one hundred yen per day.

The Bank is required by law to publish in the Official Gazette which appears every Wednesday the issue of the Bank notes for the week previous. In order that we may know the condition of issue, the latest return will be here put down.

THE REPORT OF THE AVERAGE ISSUE OF THE BANK-  
NOTES FOR THE WEEK, JANUARY 22-27, 1900.

Bank notes issued	yen 236,196,239	<b>Specie Reserve</b>
		Gold coin and bullion ..... yen 101,154,256
		Silver..... 4,000,000
		<u>105,154,256</u>
		<b>Securities</b>
		Government bonds ..... yen 19,695,622
		Exchequer Bills... 22,000,000
		Securities ..... 11,474,992
		Commercial Bills.. 67,872,369
		<u>131,041,983</u>
Total.....	yen 236,196,239	Total..... yen 236,196,239
		Amount beyond legal limit 11,263,708

As has been described in another chapter, the Bank has the Department of Issue within its inner organization wherein all work connected with the issue is carried on. But it would be a great mistake to conclude from this that the amount of circulation and the entire issuing policy are determined in this department which in fact has nothing to do with fixing the volume of notes to be issued. On the other hand, the Business Department



of the Bank performs this important function in accordance with business conditions. The Issue Department is nothing, therefore, but an instrument of the Business Department to whose directions it must comply. Why is this so? Because the issue of notes is simply a business action on the part of the Bank, determined either by discount or loan, which, in turn, is subject to the business demand and the general state of industry. The making of all such transactions is in the hands of the Business Department. It determines practically, of course under the general policy of the Bank, for what purpose, in what amount and manner, shall the notes be issued, and thus it makes demands for such and such amounts upon the Issue Department, which acts under its directions. What important feature, involved in the organization and work which we have just described, deserves to be noticed? The fact is that there are no regulations prescribed by law for directing the issue or fixing the volume of circulation. This is, however, entirely entrusted to the Bank to be done according to the principles of the banking business. In a single word, the Bank of Japan, *as a banker*, regulates the circulation of the national currency. All issues are in direct conformity with commercial interest, so that the amount of issue fluctuates, at all times, with the business demand.

There is a question whether there is any provision regarding the proportion to be kept by the amount of notes issued to the specie reserve. The law says nothing concerning the matter, but all notes, as we have seen, must be convertible at any time. Convertibility is the underlying principle of the Japanese system, which regulates implicitly the proportion between issued notes and specie, for the time being. And the maintenance of the convertibility of the notes is effected by salutary conduct of the Bank, which is always kept aware of commercial conditions.

On account of this fact, the Bank of Japan is charged with a great responsibility to maintain, unaided, the specie reserve of the entire nation. Sometimes there is much popular misapprehension, in connection with the legal limit of uncovered notes. Men think that the Bank ought to issue its notes up to the limit, and that to this extent only are the notes always sure of convertibility. But such is not the principle, I think, of the Japanese note issue. It is very evident, that, whether notes are convertible or not, is not a thing to be determined by Legislation. The legal limit of 120,000,000 yen is, to my mind, nothing more than the standard of the caution to be observed by the Bank in normal times. It is doubtful whether the legal limit is so important a factor of the Japanese issue principle as is generally considered to be the case. The Bank should vary its issue, either within or without the legal limit, the ruling considerations being commercial condition and the convertibility of the notes. In the line of our argument, therefore, the regulation of the currency must be very cautions, *even within the legal limit*, so that it keeps a proper volume of circulation and maintains the stability of credit; while, on the other hand, an adequate issue, even though beyond the legal limit, may, without much danger, be made under legitimate conditions. When we speak of the Bank's issuing policy "under salutary regulation," not only a keen perception by the Bank of the nature of the money demanded on discounts and loans, but the balancing of trade, the proper relation of prices, a systematic survey of the general market, and a policy adapted to preserving the specie reserve, should be included under this head.

The amount of notes the Bank issues, as has thus far been noted, fluctuates largely with the business demand. The ability of the Bank to regulate the money market depends upon the

elasticity of the system. The movements of the amount issued, for this reason, afford a reflection of the economic condition of the nation. In Japan, the activity of the money market is greatest normally in the latter half of the year, so that the amount of issue at the end of each year, shows the highest figure for the year, although we have had some exceptions to this rule in the past.

The following table presents a statement of amounts of notes in circulation during successive years since the first issue by the Bank on May 1, 1885.\*

End of year.	Total Amount of issue. yen.	Covered.		Uncovered.	
		Amount. yen.	Ratio to total	Amount. yen.	Ratio to total
			issue. %		issue. %
1885.....	3,956,161	3,311,461	83.70	644,700	16.30
1886.....	39,549,815	23,855,238	60.32	15,694,577	39.68
1887.....	53,454,803	31,579,905	59.08	21,874,898	40.92
1888.....	65,770,580	45,022,871	68.45	20,747,709	31.55
1889.....	79,108,652	57,409,299	72.57	21,699,353	27.43
1890.....	102,931,766	44,622,413	43.35	58,309,353	56.65
1891.....	115,734,545	63,178,333	54.59	52,556,212	45.41
1892.....	125,843,363	81,158,265	64.49	44,685,098	35.51
1893.....	148,663,128	85,928,516	57.80	62,734,612	42.20
1894.....	149,813,700	81,718,291	54.55	68,085,409	45.45
1895.....	180,336,815	60,370,797	33.48	119,966,018	66.52
1896.....	198,313,896	132,730,192	67.14	65,583,704	32.86
1897.....	226,229,058	98,261,473	43.40	127,967,585	56.60
1898.....	197,399,901	89,570,239	45.37	107,829,662	54.63

\* Based on the figures of the table prepared by the Bank of Japan.

## II. THE BANK AS THE FISCAL ORGAN.

Not only does the Bank possess the exclusive right of issuing paper currency, but it has a great function to perform as the fiscal organ. In other words it is the banker of the Government. In describing the Bank of England, Adam Smith says, "It acts, not only as an ordinary bank, but as a great engine of State. It receives and pays the greater part of the annuities



which are due to the creditors of the public, it circulates exchequer bills, and it advances to government the annual amount of the land and malt taxes, which are frequently not paid up till some years thereafter.”\* What he says here indicates in what manner the central bank acts as associated with the Treasury. As we said among our general observations, the State is a great economic person demanding an enormous amount of income and incurring vast expenditure, so that it holds a significant position in the economic community. Its influence is much greater than one can imagine, especially in a country where the administrative functions are greatly extended. Since the state must, as an economic person, adjust itself to the commercial community the use of a central bank as its fiscal instrument is essential for its own successful management, and for the general good. The more indispensable is any function of the Administration and its successful financial management, the more essential is such an institution as the Central Bank, as the State’s fiscal organ.

It is for this fundamental reason that the Bank of Japan has a mission to fulfill as the co-operator of the Treasury. Let us see how great an economic person the Japanese Government is. The latest general budget shows the following figures:—

THE GENERAL BUDGET.		
Fiscal year. ‡	Income.	Expenditure.
	yen	yen
1899	Ordinary.....	178,558,944
	Extraordinary ...	68,394,130
	Total .....	246,953,074
1900	Ordinary.....	148,545,128
	Extraordinary ...	85,391,571
	Total .....	233,936,699

\* Wealth of Nations, Book II, Chap. II.

‡ Japanese fiscal year commences with April 1 and ends with March 31 of next year, so that when we say fiscal year 1899 it covers one year from April 1, 1899, to March 31, 1900 inclusive.

These figures of the last two fiscal years tell us that the Japanese Government draws every year a sum of over two hundred millions of yen to defray a corresponding expenditure, though to arrive at the correct total of these budgets it is necessary to add to these figures those of the supplemental budgets of each year. Japan has a strong inclination to extend her Governmental functions; hence the gradual augmentation of her annual expenditures. Thus the Japanese Government is a great economic person, the sum of whose annual income and expenditure is over 400 million yen, a factor of considerable influence upon the industrial community.

As a primary consideration, there must be, on the one hand, a sufficient guaranty for the absolute safe keeping of the public money; while, on the other hand, the Government is by no means separable, in its fiscal management, from the business world, its own prosperity being involved in the general welfare of the nation. For these reasons one can not fail to raise the following questions. Who shall be the banker of the Government? Who shall be the custodian of public money? Who can undertake profitably to the Treasury the management of the public finance? Who can make the great economic person act in accordance with the commercial benefit? The Bank of Japan finds right here its essential functions. These are the points at which the Bank is closely united to the Treasury. The Treasury transactions are found to be carried on, through the co-operation of the Bank, with considerable facility and convenience. At the same time the Treasury ought to preserve a healthy order of business condition, which it cannot do without the assistance of the Bank. Evidently, therefore, we have two distinct reasons why the Treasury can not, in a national point of view, escape from the necessity of using the Bank as its fiscal organ.

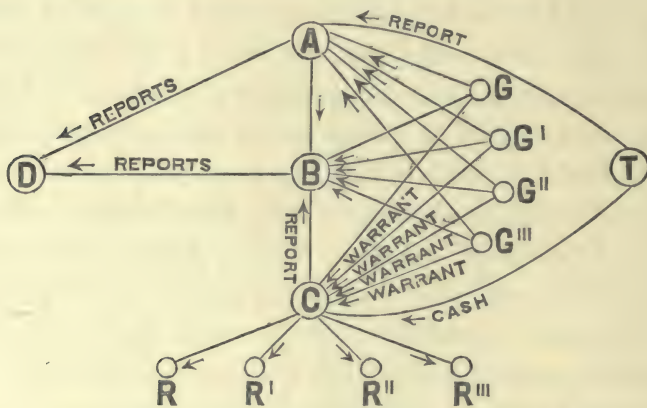
No sooner was the Bank organized in 1882 than it began to engage in dealing with the public money. In 1890 immediately after the promulgation of the Fiscal Law and the Fiscal Regulations, the sphere of action of the Bank in the realm of public finance was largely extended so that the Governor of the Bank came to assume the whole responsibility for the receipt, custody and disbursement of the public money, at the order of the Minister of Finance. According to the regulation on the subject the Chest, which is officially defined as a place to receive, keep and disburse the public moneys of the Treasury, is partitioned into three divisions, the central, the main and the branch chests. The Central Chest is established in Tokyo, and the main chests are located, one at the capital of each Prefecture, while the situation of the branch chests is determined by necessity. The Central Chest controls all the minor chests, a charge which is entrusted by the Government to the Bank of Japan ; so that practically, the Central Chest is established in the Bank itself, and to carry on the business of main and branch chests the Bank is required to establish its own branch offices or agencies. As we have already seen, the Bank has, for the purpose, within its internal organization what is called the State Treasury Department, which is not seen in an ordinary banking institution. This Department in the Bank has its function confined merely to fiscal matter pertaining to the public money. Such an organization is established not only in the main office of the Bank, but in its branch and sub-branch offices also a like arrangement is provided, having the same function. Moreover, to perform this duty completely the Bank has forty four agencies throughout the whole country which have in turn 442 sub-agencies.

Day by day moneys paid in the form of taxes and in other ways are deposited in the chests, for which the Bank renders



full account to the Government. On the other hand, large public payments are constantly being made, for which the Bank is also equally responsible, with the risk of profit or loss devolving upon it. Thus the whole income and expenditure of the Japanese Empire passes through the Bank of Japan, on the account of the Minister of Finance, who is empowered to inspect and examine the chests at any time he may desire.

The Governor of the Bank has the work of the State's treasurer in consequence of the custody of the public moneys entrusted to the Bank. Until after the 'Board of Fiscal Audit' has examined the accounts presented by the Governor of the Bank, which he is required to make, he cannot be released from his responsibility as Treasurer. To show the relative position of the Bank, we present here the following diagram indicating the entire stage of fiscal transactions, though not in detail.



D=Imperial Diet,  
A=Account Bureau of the  
Treasury,  
C=Chest: Bank of Japan,  
T=Tax collectors,

B=Board of Fiscal Audit,  
G=Departments of the Govern-  
ment,  
R=One in whose favor the pay-  
ment is made by the Treasury.

All the taxes collected flow into the chests from the tax collectors who at the same time send their reports of taxes collected to the Accountant Bureau of the Finance Department of the Government. Whenever payments are demanded, the heads of the Department of Government issue warrants upon the Chest in favor of creditors and also send the reports thereof to the above bureau as well as to the Board of Fiscal Audit. The Chest pays money upon the warrants to those who are legitimately in the credit of the Government, and then it has to send to the Board of the Fiscal Audit all the necessary writs with respect to the payment. It is the function of the Accountant Bureau of the Treasury to present all the reports both to the Board of Audit and to the Imperial Diet. The Board of Fiscal Audit standing aloof from the Administration and in the immediate confidence of the Emperor, has for its chief function the control of all the fiscal transactions of the Administration and particularly of its treasurers. From this rough explanation of the process which the fiscal transactions of the Empire undergo, it can be seen that the Bank assumes the sole responsibility for the keeping and handling of the ready money of the Government, while the duties of the Treasury are simply those of a book-keeper of accounts.

Such is the Bank's work as a fiscal organ in the custody, of the receipts and disbursements of public purse. The aspect we shall consider next of its fiscal function is the distribution of the public money throughout the country so as to maintain a good, stable money market. As has been already pointed out, the management of the public money is, at bottom, very much related to the general market, a fact which one must always bear in mind. Consider for a moment the relation of a single locality to the chest. The chest constantly calls in and pays

out, one way or another, the money of that locality. To be sure, there are some localities where the amount of money absorbed by the Government is much larger than that which returns to those from the chest. Moreover, each locality has its own peculiar seasons of demand for money which differ from those of the others. One often hears of one locality's being in financial straits in a certain season while other are not, and vice versa. Since the receipts and disbursements of the public purse are the chief factor in affecting the monetary conditions of the market, it is evident that the operations of the Chest has a large influence upon the facilities for carrying on industry and commerce both local and national. Is it not, therefore, highly desirable to transfer the public money from localities of a plethoric market to those of a stringent market? So arises the question of the distribution of the public money throughout the localities in so far as the convenience of public transactions allows. As such a distribution has to be made in face of the condition of the money market, naturally and wisely the Bank has to perform this function instead of the Treasury of the Government. For this reason, the Bank came practically in 1894 to assume the function of distributing public money throughout the country in accordance with commercial needs. Within the Bank the work of this sort, like other fiscal business, is carried on by its State Treasury Department. There is no doubt that this function is being performed more satisfactorily year by year as the development of transportation facilities goes on throughout the country.

Thirdly, the Bank has the custody of the money as well as of the goods, entrusted to it by the Government. The Treasury of the Government has to receive deposits of certain classes, such as postal deposits, legal reserves secured by the several official



grades of the Administration, rents received from the common property of people, and the like. In most of these cases, the Government is to pay certain rates of interest on such deposits. Thus it is necessary for the Government to make something out of the money deposited to an extent sufficient to meet the payment of rates. In the cases we are considering now, the public purse of the Government assumes toward the depositors entire responsibility for their profit or loss. Here again the Bank of Japan comes to the front to provide a way for the profitable management of such money. The Bank in behalf of the Treasury of the Government, to this end, receives and disburses all money with full responsibility, and moreover manages it profitably. Besides money, there are securities, entrusted to the Government in the same way, the custody of which the Bank also undertakes as the Governmental organ, but on its own risk.

The next point to be referred to, in considering the Bank as the fiscal organ of the Government, is its part in the withdrawal from circulation of the Government paper money and of the National Bank Notes. Although such work of the Bank is to be considered as merely temporary, differing, therefore, from its other fiscal functions, and as occasioned merely by the transformation of the system, yet the Bank performs it with the same thoroughness and the same elaborateness of detail. As soon as the unification of the currency and the central regulation of its volume became a settled policy of the Empire, an enormous amount of the Government and the national bank notes, as we have already seen, was to be put out of circulation. Since 1886 the Government made the Bank engage the business of their redemption so that the Bank became in this respect the agency of the Government, as well as of the national banks. To assume

such a work was, on the part of the Bank, nothing but one of its duties as the fiscal organ.

Since the establishment of the Bank, the two great improvements in the monetary system of Japan were brought about and well wrought with admirable success. One was specie resumption in 1886, for which end the central Bank had spared no effort what-so-ever, as the fiscal machinery of the Government. It is beyond the truth to say that the entire energy of the Bank, during these times, was directed toward the foundation and strengthening of the convertible system which was an urgent necessity. The other was the recent change of the monetary system to the gold standard in 1897. With the coming into effect of the 'Gold Currency Law' there was as its necessary attendant the work of the retirement of the silver yen from circulation. It must be perceived by every mind that the successful with-drawal of the silver yen had much effect upon the maintenance of the gold system which was just being initiated. Indeed the task was carried on very smoothly, and was completed in December, 1898, with no difficulty. In a part of the budgetary speech delivered by the Minister of Finance before the House of Commons, November 25, 1899, reference is made to the work of the retirement of the silver yen in which the task is represented as being carried on mainly by the Bank of Japan and its agencies, a work which was most satisfactorily accomplished. To perform all such functions, which, though temporary in their nature, are not less important, the Government always looks to the co-operation of the Bank; whereby an invaluable convenience both to the public and to the Government is secured.

The administration of the national debt is another significant function of the Bank as the fiscal organ. In the modern civilized nations, there is hardly a single one that does not use its own

credit as a means of securing money either for an unusual demand or for a demand of unusual amount. Every nation has strongly increased this tendency, during the present century, to extend the employment of the public credit, under the influence of the new ideas of social and national development.\* Japan, herself shares the common notion of the world of emergency financiering, as well as of investment loans. The administration of national debts holds, therefore, a very significant place in public finance and obtains great relative importance among all the transactions of the Treasury.

In the place of the Treasury, the Bank conducts all transactions involving public debts, whether in payment of the principal or in periodical payments of the interest thereon. Moreover, it happens not infrequently that the Government attempts to purchase its own bonds, in which case the Bank is always used as its agency. Such duties seem to be simply mechanical, but there is another more significant office which the Bank fills for the Government in this connection. We are to consider the influence of the Bank upon the national credit.

Needless to say, a modern governmental bond should rest normally upon the principle of commercial loans, appealing to the ordinary business motives which underlie the processes of purchase and sale. Suppose an instance of Government's issuing its bonds. No matter whether the loan is or not a popular subscription, it must, after all, be drawn, technically, from the money market of the country. In the existing condition of industrial society the bankers are the guarantors of the market. In Japan, it is true that the Central Bank stands as the guiding influence among these bankers. The Bank of Japan is thus, in business circles, called, and very properly, the barometer of the

\* H. C. Adams, Public Debts, Part I., Chapter I.



general money market of the nation. Assuming the Bank to be such, the Government with its co-operation evidently incurs no risk of the failure of its credit policy through a misapprehension of the general commercial market. Not only can the Government secure many favors in loan-making by employing such an agency, but it can harvest the legitimate results of its better credit. It does not matter here whether the Government makes the loan itself or employs syndicates to do it. What we want to point out is that, in either case, the Government may, through the backing of the Bank, obviate many a difficulty and obtain more favorable conditions than would otherwise be the case. This is indeed an undeniable advantage to the Government in normal times, but much more so in cases of emergency, a point to which our consideration shall turn later.

There is also to be mentioned, in this connection, the Exchequer Bill or Treasury Note, the management of which the Bank undertakes in the same manner as it does that of the national debt. According to the general budget, for the fiscal year of 1900, laid by the Government before the Imperial Diet, the maximum amount of the exchequer bills issued for the current year is reckoned at 35,000,000 yen. Whenever the Government finds public money unused temporarily during the current year, it may be deposited with the Bank drawing certain interest. On the other hand, in the case of a temporary deficit, during the fiscal year, the Government is authorized by law to borrow money from the Bank paying a reasonable rate, but such an amount added to that of the exchequer bills then outstanding can not exceed the maximum amount of the latter, as authorized by the budget. The Bank, closely connected with the Department of Finance of the Government, thus from time to time

satisfies the fiscal needs of public transactions in its capacity as the banker of the Government.

So far our consideration has been confined to cases arising under a normal condition of the public finances. In the time of emergency, however, we ascribe an added importance to the Bank's functions as a fiscal organ. Whenever a war arises the question that presents itself to financiers is how to support it in the way most compatible with all interests involved. "Nothing in history is gratis."\* How to meet the cost of the struggle must be the first consideration that presents itself to the financiers, and it seems to be a well settled policy of nations to employ loans "to bridge over the time between the out-break of hostilities and the productivity of newly levied taxes."<sup>8</sup> Assuming the issue of bonds in war financiering, the call should be quickly and adequately responded to. If there be no assistance from banking institutions, the Government may find it necessary to be its own broker. It would not be easy for the Treasury to constitute itself a broker's office in such an abnormal situation, and the process would undoubtedly be too slow to meet the immediate financial needs. On the contrary, when the Bank is used as the machine in such a case, the loans, given at however short notice, can be placed. Indeed the Bank and like institutions are the only places where large amounts of money can be obtained upon immediate demand.

There is also another important point in connection with a public loan, namely, the engenderment of popular confidence in the Government. And whether or not the Government has the co-operation of a banking institution, is an important factor in this process. Dr. David Kinley has pointed out, in considering

\* Gibbins, *History of Commerce in Europe*, P. 6.

<sup>8</sup> H. C. Adams, *The Science of Finance*, P. 542.

the operations of the Independent Treasury of the United States during the war, "the fact that the arousing of confidence is an essential element in the floating of a loan, and for the government to have established confidence directly in the minds of thousands of individual subscribers would have been, under existing circumstances, a very difficult task. But when the banks showed sufficient trust in the government to loan it their funds, the establishment of public confidence received a powerful impulse. For the banks are institutions which are supposed to know the trustworthiness of those to whom they lend, and individual capitalists will follow where they lend."\* Now then, in as much as the Central Bank may most advantageously view the interests of the public, in general survey, it is patent that it is the institution best adapted to become the supporter and sustainer of the public credit. In view of these considerations, the fact is indubitable that by the Bank the chief difficulties occasioned by a fiscal emergency can be readily removed, and its influence and assistance thus be made a genuine public benefit.

The establishment of a war chest, as exemplified by the practice of certain nations at the present time, has been frequently considered both by students and public men. In our view, however, whether or not it is a wise policy of financiering cannot be determined without an extended discussion. I may only venture to say that the policy is of doubtful expediency in a nation where a central bank exists. The effectiveness of a war chest consists in furnishing, at the out-break of war, an immediately available source of supply, prior to the securing of the proceeds from public loans, etc., so that no hinderance is offered to the exercise of the national force. But this is just the assistance, that can be rendered by a central bank. I may say, there-

\* David Kinley, *The Independent Treasury of the United States*, P.P. 105-6.



fore, that the bank serves the Government in the same capacity, to equal advantage with a war chest in the occasion of an emergency; and at the same time it is much superior in keeping off the evils which are likely to arise in normal times.

Fortunately for our investigation, Japan has lately had the experience of a war with China and has seen how the Bank was able to serve the public as the national fiscal organ. We can do no better than to quote the following paragraph written by Dr. Y. Ono in the Banker's Magazine.\*

“In addition to all these (services rendered the public, in normal times), the Bank is under an important obligation to support the public credit in times of financial emergency. During the late war of 1894-5 it performed most valuable services for the country. Indeed the war would not have been possible without the effective co-operation of the Bank. At the commencement of the war the negotiation of a foreign loan was quite generally favored in influential quarters. But the Bank opposed this idea, and was fully confident that it could depend upon the internal resources. While it supplied the Government with the necessary funds and did its best in collecting subscriptions to the war loan, the Bank was always active in providing capital to trade and industries. To the high credit of the Bank, its notes circulated during the war even in the heart of the Leao-Tung Peninsula of China. The total cost of the war was 200,457,508 yen, but this was paid without causing any serious calamities in industrial circles.”

Whenever a nation encounters emergency, the real question before the public is, how can emergency funds be easily obtained and the business interests suffer the least in consequence. In such a case, statesmen look to one source of supply and men of

\* The Bankers' Magazine (N. Y.), April, 1899, p. 549.

business bethink themselves of another. The harmonization of these two conflicting interests is absolutely essential to the best interests of the nation. That this may be brought about, the interests of both competing parties must be regarded. The Bank from its vantage-point is best capable of viewing both sides dispassionately and fairly, because it is at the same time the great instrumentality of governmental finance and the central organ of commerce. Thus the public weal is sure to be served. For this reason, in cases of emergency, Japan expects much from the Bank's management of the financial market.

### III. THE BANK AS THE ECONOMIC ORGAN.

Our consideration has been, so far, devoted to the Bank's functions as the currency regulator and as the fiscal organ. There is, however, another function which is, in my opinion, of paramount importance from the very nature of its mission; viz.,—its function as the economic organ of the nation. No sooner was political unity effected in Japan than the economic development of the nation as a whole became the chief object of state policy; for it was wisely recognized that the growth of commerce and industry is always fundamentally and indispensably essential to the existence of a nation. For the attainment of this purpose it was of the highest importance to establish banking facilities throughout the country. Furthermore, in order to bring this idea into perfect realization a strong centralized banking organ which should act in accordance with the economic policy of the nation was of the utmost importance. There was indeed a banking system in existence at the time when a central bank was first proposed. But it had proved to be an imperfect system from the view-point of the unified national interest. It

is in this sense that the Bank of Japan fulfills a significant function as the national economic organ.

Hence, if there were not any national economic policy as to the financial market, such a function of the Bank would no longer exist. In fact, however, Japan has pursued an active policy along this line, so that the function of the Bank as the economic organ is one of the most importance. No doubt, the Bank of Japan does transact its business like other ordinary banks, but there is also a significant difference between it and such banks, in that the former acts as the commercial organ of the nation as a whole, while the latter primarily have no such function to fulfill. On this account, the superintendence of the Government over the Bank should not only be directed toward the maintenance of the highest degree of public credit, but also towards securing the entire accord of the policy of the Bank with the national interest and the economic development of the state.

As to the sphere of action of the Bank, in its rôle as economic organ, we may derive information from the memorandum of Mr. Matsukata (now Count), Minister of Finance, in which he set forth the objects of the projected institution, as follows: (1) to promote the co-operation and assimilation of banks under a central bank; (2) to increase the capital available to trade and industry; (3) to reduce and to equalize the rate of interest; (4) to transfer various duties of the Treasury to the Bank; (5) to discount foreign bills so as to regulate the influx and efflux of specie. For performing these offices the Bank is rewarded, under the law, with the monopoly of issuing notes. It is quite natural that this institution should assume the leadership among the whole banking system and should stand sponsor for the arrangement of the financial market.

Let us consider more fully, in analysis, the situation of the



Bank as the economic organ. First will be taken into consideration, the relation of the Bank to the common banks. The Bank of Japan is not put forth on the same plane with the other banks to be their rival and competitor for the banking business, but rather it is the support of such banks within certain limitations. It lies within the purview of her purpose to afford such strong backing for the common banks and the entire system of credit, as is adequate to prevent any undue disturbance of monetary market. It is not its purpose to swallow up the smaller banking institutions, but rather to further their development in every legitimate way possible. When considered from the standpoint of a merely private institution, the Bank might quickly plunge into competition with the others in order to get highest profits and to the consequent enjoyment of its stockholders. This, however, should not be done. If such a policy were inaugurated by the Bank, its function as the nation's economic organ would forthwith terminate. At least in the present stage of economic development in Japan, a policy that conduced to put the central Bank on the same plane with other banks, with unlimited competition, would not be admissible. On the other hand, the Bank furthers competition between the lesser institutions through its discount system. It is largely due to the influence of the central Bank that the smaller banks are always inclined to avoid reckless competition while on the other hand they are not without legitimate competition. The result is a healthy growth of the entire banking system. Thus it appears that they come naturally into cooperation and mutual support under the central Bank's supervision.

The Bank itself is the leader among the whole system of banks and gives an authoritative guide to that system as to the management of the existent financial market. All banks turn

finally towards the Bank for its assistance when needed, so that the scope of their operations is thus enlarged as if by their own resources. As to the Bank, it indeed occupies the position of Bank of banks, preeminent over all. Nothing will make this fact more explicit for our comprehension, than to trace the attitude invariably assumed by the Bank towards the common banks. From the outset until recently, its loan and discount privileges were offered exclusively to bankers, which sufficiently proves that the Bank did not act as the competitor of the other banks. But from this system an evil result ensued: viz., that, the other bankers, acting as intermediaries between the Bank and the public, set out to secure for themselves an excessive profit, in consequence of which the benefits of the lowered rate of interest were not allowed to extend to the general public. Moreover it was perceived that such a system would hinder the healthy development of the banking system itself and thus would be against the general interest of the nation. A measure to do away with these evils was brought into effect in June, 1897.

Since that date, the privileges of the Bank have been the public's as well as the bankers', and transactions have been made directly with individuals and corporations. This policy was essential to the realization of the Bank's primary purposes, viz.—its aim to make capital available to industry and commerce, and to effect the development of a banking system with a broad national program. But what must be noticed here is that the Bank's change of policy was not undertaken for its own interest, as the competitor of other banks. Nor was the change at once excessive and radical, but two rates of interest were announced by the Bank, distinguished as "bankers' rates" and "private rates," the former being always lower than the latter, e.g. on

Jan. 10, 1899 the former was 2.3\* while the latter was 2.5. The expected results were realized, the banks were not affected in their business activity except that they were henceforth unable to procure excessive profit, because the Bank assumed the function of determining the difference of rates between the banks and the public. This measure involved an important principle, because thereby indication was given of the fact that the Bank has in view the interest of the general public rather than merely that of the bankers, and because also it marks a turning point in the process of the evolution of the Bank's business policy. In taking this step, the Bank showed a lively appreciation of the part it was ultimately to bear in the economic development of the realm.

The provision of different rates for bankers and for individuals naturally occasioned the rise of a large number of minor banks. It is very evident that all who wished capital to be furnished them by the central Bank found it convenient to first organize themselves as banks because they would be able to secure lower rates by applying to the central Bank, as banks than they would by applying as individuals. But the encouragement of numerous weak banks organized with this motive was certainly not a healthful economic phenomenon. The Bank, on its part, considered it to be in contradiction with its policy of securing the general weal to discriminate between the banks and individuals of a good business standing. Thus on November, 1899, the Bank abolished the policy of discrimination and announced itself ready to deal with all on the same terms. In our opinion, this is not new in principle, but a natural advance in the course pursued by the Bank since June, 1897.

What has thus far been said shows that the Bank does not act in the same manner as do other common banks, but, in its

\* 2 sen 3 rin per day for 100 yen.



operations, is always subject to the economic policy of the nation. Although the attitude of the Bank towards the banks has changed, to a certain degree, yet it still stands as guarantor of their banking capacity. Any competition based merely upon considerations of private profit never exists between them. It must be borne in mind, however, that the Bank is not forced to assume such a generous attitude by any interpretation of legal provisions, but its policy is simply derived from the notion it entertains of its public duty as the central Bank.

The kinds of business to be transacted by the Bank are mentioned in the Act: thus,—

(1) The purchase or discount of exchequer bills, bills of exchange, and other commercial papers ;

(2) Dealing in gold or silver ;

(3) The making of loans upon gold and silver coin or bullion ;

(4) The collecting of bills due to banks, corporations and individuals who are the regular customers of the Bank ;

(5) The receiving of deposits and the custody of objects of value, and documents ;

(6) The making of advances in current account or in loan upon securities, such as Government bonds, exchequer bills, or bonds and shares guaranteed by the state.

Among these, the discounting of bills constitutes the chief business of the Bank, just as in the case of other commercial banks. One of the offices which the Bank has to perform as the economic organ of the nation is to increase the capital available to commerce and industry, as has been already mentioned. This purpose may be effected in many ways. The Bank of issue must always provide to the community an adequate supply of free capital, though the amount is limited in every legitimate way

possible. The growth of the credit system and the improvement of banking facilities also look towards this end. Quick exchanges of capital have the same effect as of an increase of capital, so that the use of bills in commercial transactions is highly desirable. Credits of modern forms, however, being rather new things in Japan, nearly all transactions were made on a cash basis, but, as the result of the efforts that the Government as well as the Bank has put forth to encourage their use, their employment has now grown to a considerable extent.

It is provided that bills discounted by the Bank must be endorsed by at least two substantial names and be payable within one hundred days. Those which bear a single name are required to be backed by collaterals either in the form of warehouse receipts of merchandise, or of shares and bonds classed at securities of good credit. The loans upon securities are made always at a little higher rate than that of discount. These securities are bonds of the Government and of certain municipalities, and also bonds and shares guaranteed by the Government. The terms of loans are limited in duration and their renewal is allowed only once except in cases where particular conditions prevail. The deposits with the bank are, in reality, very insignificant in amount, for it does not pay interest on current deposits, and but a very low one on time deposits. The chief item under this head is furnished by the accounts of the Government Treasury with the Bank. As to common customers, they merely place their surplus money in the Bank, upon which checks can be drawn at their convenience.

Turning our study to interest rates we find that they were very high about the time when the central Bank was organized. It was, therefore, highly desirable to effect a reduction of these rates, as well as to equalize them throughout the country. The

high rates obtaining upon the money market were so considerable a hindrance to the development of commerce and industry, that their amelioration was looked upon as one of the principal necessities demanding the establishment of a central bank. The Bank ever since its organization has endeavored to realize this end, a function which naturally, of course, falls to its part as the economic organ of the entire nation. While the loan rates of the common banks, when the Central Bank began its career in October, 1882, were above twelve per cent. per annum, the latter made its loans at eleven or ten per cent. and by the end of next year it was able to reduce its rates to eight per cent. per annum. This reduction was continued, until, at the end of the first decade of the Bank's existence, the rate was but half what it was when the Bank started. There were, of course, occasional fluctuations up and down according to the conditions of the money market, but it was nothing less than significant that the rate in May, 1893, was as low as 4.7 % per annum. So far as concerns equalization of rates, the Bank performs its function through branch or sub-branch offices and a number of agencies. And the Bank is always ready enough to establish more branches when conditions are favorable.

The rate of interest is not unfrequently altered by the Bank. It is obvious that the Bank should have this power, bearing, as it does, the responsibility for the orderly arrangement of the monetary market as well as for the healthy development of industry. The Bank, as has already been said, is entrusted with the specie reserve, upon which the entire credit system of the nation is based, a fact also making unavoidable certain fluctuations in the interest rate. Thus the variation of the Bank's rate, giving authoritative indication of the state of the money market, are carefully studied in business circles. At the present time,



the Bank charges lower rates than other banks. This is not always the case, however, as when the money market is extremely plethoric. The City of Osaka, in 1893, offered such a contradictory instance. The clearing house rate of discount was quoted 5 "rin," while the loan rate of the Central Bank was 1 "sen" and 3 "rin." Such an occurrence is, however, very rare.

All alterations in the rate of interest for discounts and loans, as made by the Central Bank of Japan, should be simply responsive to a change of conditions in the money market, which change may in turn have taken place in connection (1) with the specie reserve, or (2) with the economic conditions prevailing at home. If there be any alteration not thus motivated, the result will be an unnecessary disturbance of the money market. It is well-known that international money has a tendency to move, after all, in accordance with the condition of foreign trade, and that free capital tends always towards the most favorable market within certain limitations. In pointing out the acute effects of this latter movement upon the movement of the precious metals, J. S. Mill says:

"As much money might thus go out as had previously come in, while the prices of commodities would have shown no trace of the temporary presence. This is a case highly deserving of attention, and it is a fact now beginning to be recognized, that the passage of the precious metals from country to country is determined much more than was formerly supposed, by the state of the loan market in different countries, and much less by the state of prices."\*

Both the conditions of foreign exchange and the money market of foreign countries affect directly the specie reserve of unfavorable nations. A nation which cannot, in time of monetary stringency, attract specie from other nations through the operation

\* Principles of Political Economy, Book III, Chapter VIII, Sec. 4.

of rates may, nevertheless, at other times, be in a position to effect a transference of its own specie to other nations. Therefore, the Central Bank of Japan cannot, without putting in jeopardy its own specie backing, alter its rates regardless of the above consideration affecting rate determination. The Bank, however strong, cannot determine its loan and discount policy free from conditions obtaining at foreign markets. Nay, if it attempted to do so, artificial measures for preserving the basis of the public credit would be constantly necessary and the normal healthfulness of a self-adjustable national market would be deleteriously affected.

The other point which the Central Bank must take into consideration in fixing its rate of interest has reference to the conditions of domestic industry. To stimulate lethargic enterprise and to check speculation are the main items of the Bank's policy to be brought about through the machinery of rate fluctuation. At the present time, the normal condition of the Japanese money market is as follows: The year opens with a plethora which becomes most strongly emphasized in the early spring. The productive season of tea and raw silk opening up, money gradually finds employment throughout the middle spring. Although August shows the counter-tendency, the season of crops and crop-movements ensuing, from autumn on till winter there is again plenty of employment for money. Since the end of the year is the usual time for settling accounts, the money market tends more and more toward stringency, making this the busiest season of the year for money. The movement up or down of the Bank's rates is, in general, in response to the varying demands of the seasons.

Another function belonging to the Bank in its capacity as economic organ has reference to the foreign trade of Japan. Japan being an insular country of small area, it is very evident

that the growth of foreign commerce bears an important relation to her economic existence. It is also obvious that the influx and efflux of specie, upon which the whole credit system rests, is largely influenced by the real conditions of foreign trade. To encourage foreign commerce is for Japan her established national economic policy, resultant from her special situation. Looking to this end, the Bank of Japan is directed particularly to enter into the work of developing the foreign commerce. While having itself no direct dealings in the foreign market the Bank has the Yokohama Specie Bank act as its foreign agent. In rediscounting foreign bills at the low rate of two per cent per annum the Bank of Japan advances to this institution, at present, upward of 20,000,000 yen. Thus facilities for discounting foreign bills are afforded the public by the Bank of Japan through the Yokohama Specie Bank, this arrangement being for encouragement of foreign commerce.

With the development of the credit system the Bank reveals more and more the importance as a machine of exchange. And "the functions of a bank as a machine of exchange are but seen in the operations of the clearing house."\* The Bank of Japan being the Bank of banks it is very natural that it should assume the business of transferring accounts in the daily settlement of the balances of the banks of the clearing house association. The whole transaction is carried on in the building of the Bank of Japan. Each bank of the association makes, for this purpose, current deposits with the Bank. The Bank should strive in every way for the improvement of the banking facilities in connection with the clearing-house system, for this is one of the functions the Bank has to fulfill as the economic organ of the nation. Hence the Bank not only as a member of the clearing house association:

\* White, Money and Banking, P. 238.



i.e.—as a common banker as well as the banker of the Government, but also as the leader of all banks will serve to oversee them for the preservation of credit.

So far we have been looking upon the operations of the Bank in a normal economic condition. Our consideration, however, will be extended to those demanded by an abnormal state of the financial market. The functions subserved by the Bank as the economic organ in such cases are not of less importance, at least to the nation, than those subserved in ordinary times. The abnormal cases in which the Bank's special functions are demanded, are two in number. These two cases will be separately considered.

(1) In the case of national emergency. What we want to do here is not to examine the work which the Bank performs for the Government in such a case, but the attitude which the Bank assumes toward business circles in its effort to do away with emergency difficulties. Whenever war breaks out, the Bank as the fiscal organ should promptly make advances to the Government of an adequate fund. But what the Bank cannot neglect in the least, while still performing its duty towards the Government, is its function as the economic organ. It is of paramount necessity that productive industry and commerce should be kept in as great activity as is possible, for the nation, after all, must rely upon its wealth in time of war. These two duties, to be simultaneously performed, constitute, no doubt, a Herculean task for the Bank.

Let me give as an illustration the course pursued by the Bank in the late war, because this is the only case that has arisen since the organization of the institution. The money market which quoted 1.3 as the rate for loan and discount, about the middle of the year previous to the war, tended gradually toward stringency

at the end of the same year, so that rates rose to 1.5 and 1.7, respectively in September and in November. Since, however, not only did the demand for money not decrease because of this measure, but also the balance of foreign trade was against the country at this time, with a consequent outflow of specie, the Bank warned the market by gradually raising rates to 1.8 in January, 1.9 in February and 2.0 in June of 1894, in summer of which year the Chino-Japanese war broke out. No sooner was the war in de facto existence than the rates announced by the Bank were raised to 2.2 on loans and to 2.1 on discounts. Everybody thought, at this time, that the rates would henceforth be enhanced so extraordinarily as to mean the virtual stopping of loans. But the rise ceased at this point. While the business circle was thus warned, the necessary demand for money in the general market was at the same time satisfied. In December of the same year the Bank issued emergency notes in order to satisfy the Government as well as commercial circles, which issue, however, was withdrawn in time, partly because entrepreneurs suspended their industrial enterprises to as great an extent as was allowable under the circumstances, and partly because the Government money devoted to defraying the expenses of war was scattered broadcast among the people at home. It thus happened that all the banks had home money from January to March of 1895. Still the Bank did not find itself free to relax its cautious guard. It was not until July of the next year that the rates were lowered to 2.0 on loans and 1.9 on discounts. The Bank's policy at this time was well stated by one in authority: "Though it was necessary, as long as the war lasted, to check more or less the ordinary loans, owing to the necessity of a reserve for war supplies, it was not necessary to pursue the same policy until after the peace had been actually concluded. It is always unwise to restrain enter-

prise, but it is more prudent to afford the loans needed to satisfy the natural demand." Thus commerce resumed its normal activity towards the latter half of the year. Such, in brief, is an account of the task the bank incurred on this occasion of national emergency. In effecting its successful management of the money market the Bank wisely availed itself of the emergency issue beyond the legal limit. From the course pursued by the Bank on this occasion, we get an idea of the Bank's preserving the constant harmony of its two-fold nature; and of how, in time of emergency, it is able to subserve its functions as fiscal agent of the Government without prejudice to its function as economic organ of the nation, and vice versa; only laying emphasis, now upon this aspect of its duty and now upon that, as the circumstances of the case, or the condition of the money market demands.

(2) In the case of commercial panic. The duty of the Bank in a commercial panic or in the like circumstances is an important consideration for us in viewing it as the economic organ of the nation. Since the Japanese system of note issue, as has been already said, is provided with an elastic limit, the Bank can issue emergency notes, having first obtained the permission of the Minister of Finance, whenever necessary. The market may thus be relieved of any serious panic. The efforts of the Bank, on such occasions, therefore, should be to realize what is called the expansion theory of currency. It is largely due to this system that the Bank never fails to meet the varying demands of trade, so that Japan as a nation is always free from a general paralysis of business. Although Japan has thus far had no tremendous panic, yet there are a few cases somewhat ápropos.

For illustration let us take the business disturbance of 1890. Unduly speculative enterprises dating from the preceding years,



whose rise had been concomitant with the fall of interest rates, demanded, in this year, an enormous sum for investment. This year, also, the price of rice, which is a leading staple in Japan, arose on account of the short crop of the previous year, so that a large amount of rice was imported from abroad; while, on the other hand, there was, at this time, a rise in the price of silver which affected more or less adversely the Japanese export trade. The result is clearly presented in the following figures:—

	Export of Commodity.	Import of Commodity.
1889.....	70,060,706 yen.	66,103,767 yen.
1890.....	56,603,506 „	81,728,581 „
1891.....	79,527,272 „	62,927,268 „

The export of specie during the year of 1890 was something over twelve million yen. Such economic conditions caused a very tight money market. The serious condition of affairs, threatening business interests, first made itself apparent at Osaka and Kyoto, but soon cities all over Japan were affected by the impending calamity. The way was open for a tremendous panic. In view of this state of affairs, the Bank at once had recourse to the issue of emergency notes for the relief of the market. At the same time it greatly extended the sorts of collateral acceptable as securities, so as to turn a great number of merchantile papers into the more available cash. Bills were discounted on this extended basis of credit securities. As the business disturbance, at this time, was, as a matter of fact, mainly due to the collapse of the stock upon which the solvency of business men rested, the extension of loaning facilities by the Bank had the effect of reinforcing the diminished credit of the money market. Thus, as soon as the measures taken by the Bank were carried out the market assumed at once an aspect of order, and the business disquietude passed away without its development into a real panic.

There was another instance, a few years ago, after the late war, in which an overwrought market started out to dishonour certain merchantile papers and certain banks began to suspend payment. The Bank adopted, as its first step, a somewhat conservative policy, viz.—to raise the money rates in order to check speculative enterprise. While thus warning the general market on the one hand, the Bank tried, on the other, to relieve certain embarrassed banks by special advances to them upon the guarantees of other banks of good standing. This could not have been done if there had been no agreement of mutual support among the banks, because without others' guarantee the Central Bank would not have dared to attempt to give any such assistance to the distressed banks. However this may be, the result was that the distressed banks were relieved and the matter ended without any serious disturbance of the market.

We have said that the Central Bank was pre-eminently a banker's bank. Especially is this true, as is evident from the above illustrations, when a commercial crisis impends. One must bear in mind, however, that the Bank fulfills this especial function with the general interest of the state in view, not from any sense of its own particular interest. It is simply because the Bank is the supporter of the whole system of credit and stands sponsor for the salutary management of the general money market of the nation, that it incurs this task.

We have thus described the activity of the Bank as the economic organ. As one may well surmise, its action in this rôle is somewhat indefinite, but it is none the less important from the national point of view. And from the view-point of the Bank itself, it is the most elaborate of all the public services which it undertakes. Economic conditions change each day and year, the policy of the Central Bank must keep pace. Financial develop-

ment is necessitated by the promotion of commerce and industry  
The Bank of Japan should endeavor to make the process an  
orderly one.

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## CHAPTER IV.

### THE DEVELOPMENT OF THE BANK.

The Bank of Japan (Nippon Ginkō) is an institution newly established under the so-called "Bank of Japan Act." It did not come into existence as the successor of any particular banking or mercantile institution, as has been frequently the case in other nations. There is this difference too between the origin of the Central Bank of Japan and that of European banks. It did not arise because of political reasons nor because of the pending necessity of governmental finance. Neither was its charter granted it in return for its having subscribed the public debt. The Bank was established primarily and purely for promoting the business development of the nation. It was only after a careful study of the institution needed that the Act was passed. Therefore both theoretical considerations and practical desirability, as well as other nations' experiences with a central bank system, called the Bank of Japan into actual being. From the official point of view, the establishment of the Bank was a part of the broad financial scheme of Mr. Matsukata, then Minister of Finance, to whom the nation owes much for its financial successes. At any rate, the system of a central bank was a new thing in Japan, so that nobody could, at the outset, tell with assurance whether the institution would achieve success. But writing now, we can say that the merits of the Bank have been universally recognized and the expectations of its founders have been fulfilled.

With the promulgation of the Bank of Japan Act, June, 1882, the organizing commission was appointed by the govern-

ment. Every particular of the scheme of organization having been brought to perfection by them, the Bank commenced business on October 10 of the same year. As the Bank started up entirely new in Japan, though a desire for such an institution had been long felt in Japanese business circles, the Government, in accordance with provisions of the Act, assisted in its establishment by subscribing from the governmental surplus fund one-half of the Bank's capital, taking stock in return. The course of the Government was exactly parallel to that pursued by Napoleon in the case of the Bank of France.\* The capital of the Bank was at first 10,000,000 yen, divided into 50,000 shares of 200 yen each. So far as concerns the rates of dividend, there was a distinction for some years between the shares owned by the Government and those owned by the public. It was the idea in the beginning that the profit should be distributed thus: a 6 per cent dividend to the Government and an 8 per cent dividend to the public, while at least one-tenth of the remainder should be carried to the reserve fund and another one-tenth of it should be distributed to the officers of the Bank as the bonus; the remainder of the profit should then be distributed among all the shares both of the Government and of individuals on equal terms. In the early part of the very next year, 1883, however, the Bank got permission of the Government to refrain from making a second dividend for the shares owned by the government, which were afterward, in 1885, transferred to the Crown. It thus appears that the original idea ceased of operation even before coming into full practice. The Government's action was, of course, prompted by a desire to protect and enhance the credit of the Bank whose fundamental purpose it should be to render financial aid to the Nation at large. This assistance was further necessitated by the

\* Noël, *Les Banques d'Emission en Europe*, Vol. 1, p. 97.

fact that the privilege of issuing notes was not granted to the Bank until May, 1886, while the Bank was none the less required to perform its functions as the national organ. The Government had no intention of deriving pecuniary profit from its ownership of the shares as was the case with the people. Indeed it was originally the idea that the Government would cease being a share-holder as soon as the business of the Bank was placed on a firm foundation.

An increase having taken place in the profit of the Bank, in the course of time, the above distinction observed in the apportionment of the dividend was removed towards the latter half of 1886. Since the amendment of the by-laws of the Bank in 1887 all the shares, whether belonging to the Imperial Household or to the people, are equally treated. The profit, divided semi-annually from that time on, is dealt with in the following manner: (1) Out of the net profit the first dividend of six per cent per annum goes directly to share-holders; (2) then at least one-tenth of the rest, to the reserve fund; (3) another one-tenth, to the Bank officers as a bonus; (4) out of the remainder the second dividend is taken some part of which may be carried over to the reserve account. The rate of the second dividend requires the sanction of the Minister of Finance. The two dividends, taken together, have always amounted, since their first declaration in 1887, to something between 10 and 15 per cent per annum on the capital stock. The reserve fund is provided for two purposes, stated by the Act; viz.,—to make up for losses of capital and to equalize the annual dividends. The by-laws of the Bank require that the fund is to be invested only for the purchase of gold, silver and Government bonds. Since the Bank began to issue notes in 1885 the increase of the fund has been made a matter of strenuous endeavor on the part of the Bank for the



purpose of strengthening the basis of convertibility. The Bank started out as the economic organ, to use our classification of functions, rather than as the fiscal organ, or as the regulator of the currency. The original Bank Act left it to succeeding enactments and to instructions by Government to prescribe for the Bank these two latter functions, and its function as note-issuer, which became the theme of a special law.

The Bank, however, conducting its business operations successfully, demonstrated to the Government its competency and ability to act as the fiscal organ of the state. Accordingly, in the very year succeeding its foundation, in 1883, acting under instructions from Government it assumed control of the public moneys, an office previously fulfilled by the Finance Department. With the resumption of specie payment in January, 1886, the Bank began to do other fiscal work, such as exchanging the Government paper money for either coin or the convertible notes issued by itself. Also, in the same year all the business concerning the public bonds was transferred from the Treasury of the Government to the Bank. As has been said in another place, the scope of the Bank's action as the fiscal organ was largely extended, finally, in April of 1890. In the mean time, its function as note-issuer was given the Bank, in 1885, under a law called the Convertible Bank Notes Act, proclaimed on May of the previous year. This delay of three years in conferring upon the Bank the power to issue notes was occasioned by the fact that during these three years there was still a considerable difference of value between silver coin and paper money. Thus its three essential functions were gradually assumed by the central Bank of Japan. Strictly speaking, therefore, it would be proper to say that the real activity of the Bank did not begin until this time and that its work hitherto was a period preparing it for the exercise of all its functions.

The head office was placed at Tokyo, the capital of Japan, where the Governor, the Deputy-Governor and the Directors of the Bank are required to live. Immediately after the commencement of its career, the Bank intended to establish a branch office at Osaka, which is the most prosperous city of commerce and industry in Japan, and is situated about 350 miles west of Tokyo. On December of the first year, 1882, the Osaka branch office was opened. The city Osaka being a great center of business enterprise and always filled with people interested in all sorts of projects, is a very likely starting point for business panics. Indeed, this has been frequently the case. Such being the fact, the branch office in that city has an important influence upon the Central Bank's efforts to maintain a salutary condition of the money market. Later, with the growth of its business to an enormous extent, the Bank directed its efforts toward establishing other branches in the different quarters of the country. The Western branch office was opened at Shimonoseki in 1893 and was recently removed to Mozi just opposite. The city Mozi is the newly-opened port situated on the Strait of Shimonoseki in the northern end of the Island of Kyushyu. Thus the Western branch office is likely to extend its business to the whole southwestern part of the country. In the year, 1895, another branch office was established at Hakodate, the "Hokkaido," whose business periphery takes in the northern part of the country. In 1897, still another branch office was opened at Nagoya, which is a large city situated between Kyoto and Tokyo. Besides these four branches, there are four sub-branches, at present, in Otaru, Sapporo, Kyoto and Fukushima, established in response to the demands of commerce in these quarters. For the handling of the Government's money the Bank has, as has been already indicated, many agencies in every part of the country. When Formosa

became a part of the Japanese territory as a result of the late war, the Bank of Japan established a sub-branch office at Taihoku mainly for the management of the public money in its capacity as fiscal organ ; also minor sub-treasuries in the several places on the Island. But with the establishment of the Bank of Formosa in 1899 the Bank's business in the Island was altogether transferred to this new institution, so that the sub-branch office was closed the same year.

In order to afford a relative view of the business transaction<sup>s</sup> of the head, branch and sub-branch offices of the Bank, the following figures will here be quoted. The total transactions of the Bank for 1898 amounted to 9,019,330, 231 yen, according to the ' Business Report of the Bank.'

Head Office .....	6,933,000,000 yen.
Osaka Branch Office .....	1,218,000,000 „
Western „ „ .....	189,000,000 „
Hokkaido „ „ .....	87,000,000 „
Nagoya „ „ .....	263,000,000 „
Sapporo Sub-Branch „ .....	22,000,000 „
Kyoto „ „ „ .....	228,000,000 „
Taihoku „ „ „ .....	25,000,000 „
Otaru „ „ „ .....	49,000,000 „

Since January, 1897, the Bank has begun to make public the statement of its business condition from which the tendency of the money market can be gleaned. For it is an indicator of the economic condition of the country in general. The report is published, together with a statement of the average amount of the note issue, every Wednesday in the Official Gazette. We shall quote here the latest report from the Gazette.



## THE BUSINESS CONDITION OF THE BANK ON

JANUARY 13TH, 1900.

Dr.		Cr.	
Item,	Amount;	Item,	Amount.
	yen.		yen.
Capital .....	30,000,000.000	Bills .....	70,728,301.710
Reserve and Rest.	16,646,336.304	Foreign bills ... ..	16,507,562.300
Notes issued .....	230,492,312.000	Advances to Gov't.	22,000,000.000
Public deposit.....	63,820,442.465	Loans .....	69,010,883.428
Other deposit .....	5,137,893.343	Due from banks... ..	2,483,174.753
Due to banks .....	47,724.290	Public bonds ... ..	56 100,606.880
		Bank premises .....	2,007,056.566
		Money and Bullion.	107,307,122.765
Total .....	346,144,708.402	Total .....	346,144,708.402

The growth of the business of the Bank is shown by the following figures :—

Year.	Total business transactions.	Am't rec'd in deposit account.	Total loans and discounts.
1882...	6,357,244 yen.	647,613 yen.	987,800 yen.
1883...	157,639,152 „	14,988,494 „	5,943,950 „
1886...	1,687,955,588 „	21,343,023 „	27,468,648 „
1889...	2,767,516,604 „	19,211,115 „	113,393,508 „
1892...	1,888,088,536 „*	216,112,764 „	159,773,825 „
1895...	3,013,921,233 „	410,353,000 „	350,603,400 „
1898...	9,019,330,231 „	532,530,150 „	415,806,935 „

The policy of the successive directors of the Bank has been addressed toward increasing the reserve fund to a much higher ratio of the capital stock than the law provides. The price of the Bank shares is, for the time being, always quoted at about

\* After 1890 the central Treasury (Chest) was established within the Bank, so that the Government account was separated from the ordinary account of the Bank's business and transferred to the former.

double their face value; for instance, in November, 1899, according to the 'Monthly Report of Kyoto Chamber of Commerce,' they were quoted at 435 yen while their face value was 200 yen.

At the time when the Bank began its career, Japan was in the process of contracting its depreciated paper currency. All industries which have stood thus far on a basis of apparent prosperity were sinking down into inactivity, with the collapse of the prices of commodities. From the year 1881 down to 1886 inclusive there was a period of lethargy, so far as industrial enterprises were concerned, although the germs of the future business development were implanted in this interval. At the end of 1885 the amount of notes which the Bank had issued was about three million and nine hundred thousand yen, of which three million and three hundred thousand were covered by specie. No sooner was the parity between silver and paper re-established than industrial enterprises began to resume their normal activity.

February, 1887, the Bank increased its capital to double the original amount, that is, to 20,000,000 yen, the expansion of business and the general economic condition of the country having necessitated this step. Railroad stocks quoted up to this time below their face value (all paid up) took an upward turn; spinning industries, which were then coming into existence, were found profitable. A good many other kinds of investments also were made during 1887 and 1888. While business prosperity seemed thus assured, reactionary phenomena began to appear, gradually, from 1889 on, reaching a climax in the next year, with a disturbance of the money market. The action of the Bank at this time, which has already been described in another connection, need not again be detailed here. But, in passing, it is interesting to note that, at this time, business circles were clamorous in demanding that the state purchase the railroads,

alleging, as an argument, that otherwise many systems would not be completed. The permanent social interests of the nation demanded such a policy, it was urged. But it is undeniable that the main arguments emanated from the self-interest of invested capital. For the stringency of the money market rendered it impossible for those interested in such vast undertakings as the building of a railway system to carry on to completion their projects. The fact that such a reason for State purchase was most strongly urged at Osaka, the center of the prevailing disturbance, shows the business condition of the realm. After an investigation for relief of the difficulty, carried on at Osaka by the Minister of Finance, the Governor of the Bank and some other financial experts, an effective measure was adopted by the central Bank. Emergency notes were issued in the midst of the disturbance, in March of 1890. This was the first utilization of the system of elastic limit by the Bank, the tax rate on the issue being five per cent. The amount issued was merely 500,000 yen which were recalled early in the next month, so that the notes continued in circulation but one month. The instantaneous relief afforded was due to the rise of business confidence in financial circles concomitantly with the measures taken by the Bank. Another important factor in the improved situation was the redemption by Government of 5,000,000 yen of public bonds.

Up to this time, the amount of uncovered notes that the Bank was allowed to issue in normal times had been limited to 70,000,000 yen, by the provisions of a law enacted in 1888; but the growth of commerce and industry was so rapid and general throughout the country that this legal limit was felt by the Bank too restricted for the salutary arrangement of the money market. Consequently, May, 1890, the limit was extended by the Govern-



ment to 85,000,000 yen which was to be utilized as fast as the outstanding circulation of the Government and the national banks notes were withdrawn. By the amendment to the Convertible Bank Note Act the Bank obtained much greater power than it had hitherto possessed to supply a circulating in accordance with the demands of developing commerce; but to this power was joined an added responsibility to guard the credit of the nation.

As soon as the industrial disturbance of 1890 passed away a new economic order set in. The tight money market of 1890 and 1891 became gradually free during the next year. However, in spite of favorable financial conditions, there were, for some time after, no considerable undertakings, particularly in the direction of new industries, owing to the after-effects of the trouble of 1890. The shock, which was, we should say, psychological rather than substantial, was so remarkable that a revival of the business activity did not immediately succeed. The result of such a general condition of lethargy was the lowering of the rate of interest caused by the lack of demand for capital. However, the industrial depression precedes the return to activity. Such was the case with Japan, in 1892, after a rest of nearly one year. There was an agitation to transfer the State railways to private hands, the very opposite to what had taken place a few years previous. This showed, as nothing else, the easiness of the money market. The rates for loans and discounts announced by the Bank for the years following 1891 up to the breaking out of the Chino-Japanese war are as follows:—

Date of the rate change,	For loans,	For discount.
March 2, 1891,	2.10 sen.	2.00 sen.
May 6, "	1.90 "	1.80 "
July 21, "	1.75 "	1.70 "

November 24, 1892,	1.65 sen.	1.60 sen.
March 23, 1893,	1.50 „	1.40 „
May 31, „	1.30 „	1.30 „
September 2, „	1.50 „	1.50 „
November 21, „	1.70 „	1.70 „
January 22, 1894,	1.80 „	1.80 „
February 8, „	1.90 „	1.90 „
June 18, „	2.00 „	2.00 „
July 26, „ (Outbreak of war.)	2.20 „	2.10 „

What we notice, first of all, in the above table is that the money market experienced a period of lethargy, after the passing away of the trouble which has just been described. Also there was no alteration of rates made by the Bank for the long period of seventeen months between July, 1891 and November, 1892. This fact indicates that it was a time of depression without any active demand for capital. The Bank, hereupon, perceived the necessity of lowering still more its rates, otherwise a serious check would be imposed upon the industrial growth of the nation. On May 1893, the rates declined to 1.30. This tendency was not confined to the central Bank but was a general financial movement. All the banks in each city lowered their rates with the evident purpose of getting their free capital into use. The lowest rate the Japanese money market ever witnessed obtained at this time. Not only was there no difference between the rates of the common banks and those of the Central Bank, but the former had lower rates than the latter ;—a quite unusual state of affairs for Japan as we have shown above. From the nature of the case, there were three leading causes which contributed to produce such a plethoric market : (1) the inactivity of the money market continued from the previous years ; (2) the balance of foreign trade was favorable, so that it attracted a large amount of specie ;

—over 5,500,000 yen from abroad during the first four months of the year alone; (3) in addition to these, the Government redeemed its evidences of indebtedness to the amount of 23,000,000 yen. The rate, as altered on May 31, 1893, was the lowest ever announced by the Bank.

The question now arises whether or not the Bank, at this time, could not have reduced its rates to a lower point than could the other ordinary banks have done. As a mere banking institution, it might probably have so acted, but the Bank of Japan is more than such an institution. As has been already demonstrated, it is primarily a national organ, holding in view the public interest. The money market was so easy at this time that there was no call for the Central Bank's advances. While such was the case, it is doubtful whether the Bank, in view of the public interest, should have lowered its rates to the extreme point, as such action would quite likely have resulted in stimulating excessive speculation.

Under such favorable financial conditions it was not long before industrial enterprises and investments, as well as commercial activity, began to experience a revival. This was in the years 1893 and 1894. Thus, when the war with China broke out Japan was in the midst of business undertakings of all sorts. The Bank, already about to increase its rates on loans and discounts when the new emergency arose, now issued warning to business circles by inaugurating a more restrictive policy and advancing capital on less easy terms. The experimental development of the Bank as the nation's fiscal organ took place at this critical time. New enterprises, generally speaking, were suspended, as long as the war lasted. But when the war was ended by the conclusion of the Shimonoseki Treaty, signed on April 17, 1895, the business undertakings which had been suspended



temporarily began to resume activity. Although the popular clamour throughout the country for another war on the occasion of the intervention of the three allied Powers, immediately after the conclusion of the Treaty, checked enterprise again for the moment, the peaceful condition obtaining toward the latter half of the year restored business activity to its norm. The Bank of Japan kept the rate down to 2.00 on loans and 1.90 on discounts which rates remained stationary until September, 1896. These unvarying rates during this interval of fourteen months were designed, in the main, for the encouragement of business undertakings. The business projects in every line of industry sprang up in every quarter of the country. As to the Bank itself, the growth of its business with the industrial expansion after the war, necessitated the increase of its capital to 30,000,000 yen divided into 150,000 shares. This increased capital all paid up constitutes the present amount of its stock.

The national emergency passed by. It had been, indeed, an important epoch in the financial and commercial history of Japan; but a period still more worthy of our attention succeeded, in which the services of the Bank of Japan were wanted much more than ever before. As history shows, from the financial and industrial point of view a nation confronts oftentimes more serious problems after the close of a war than during its actual continuance. Especially was this the case with Japan. For she secured an indemnity from China as one of the conditions of peace and, moreover, she was driven to incur a large increase of the Governmental budget, largely on account of the political conditions in the Far East, which had been brought about by the war.

Without entering upon the question of the war indemnity in detail, interesting as it is, let us bear in mind that it was agreed between the two nations that its payment should be made at

London in English coin instead of the Chinese silver Tael. When the first payment of a part of the indemnity was made, in October, 1895, a speculative price of silver prevailed at London, so that the Japanese Government did not attempt to introduce its indemnity immediately into the country, lest the foreign trade, especially as this was the season of silk export, would be disadvantageously affected thereby. It was not until January, 1896, that the Bank of Japan began, under instructions from the Government, to transfer gradually the indemnity money from London to Japan through its foreign agent, the Yokohama Specie Bank. Herein a very important question 'How may the indemnity be managed to the greatest advantage and to the least disadvantage,' was put by the Finance Minister to the Bank. The Government's policy, at this time, looked to the introduction of the indemnity through the purchase of bullion or through the exchange operations. Whenever the former method should be employed caution was to be taken to absorb gold as well as silver so as to avoid any loss to the Treasury on account of alterations in the ratio between the metals. As to exchange operations, not only direct exchanges between London and Yokohama but also transfer exchanges with the United States, India, Shanghai, or other places were to be utilized. After the adoption of the gold standard, this policy was changed to one favoring the purchase of gold. A standard price per ounce for the purchase of gold bullion was set, and for the purpose of keeping the price constant the purchase of either the English gold coin or silver bullion was allowed. In this manner all of the indemnity which was paid off by China up to May, 1898, was transferred, the transaction having required three years. The whole sum thus dealt with amounted to 363,446,464 yen.

During the time consumed in the process of payment, the

money of the indemnity was deposited by the Government with the Bank of England through the Bank of Japan, the latter being allowed to issue its notes on this deposit.

Let us turn our consideration to the money market at home and see how the Bank of Japan was acting during this interval. At the end of May, 1895, there was an issue beyond the legal limit amounting to one million three hundred thousand yen, with which the Bank satisfied the special demand of silk and tea producers, and also advanced certain sums to the Government to meet war expenses, but this issue was immediately called in after only four days. In the latter half of 1895, as we have seen, business gradually recovered as a natural result of the encouraging policy which was adopted by the Bank. During this interval the Bank issued again notes beyond the authorized limit, its issues reaching at times more than 55,000,000 yen and the ratio of the specie reserve to the total amount of outstanding notes was 35.48 per cent of the latter, the lowest proportion the Bank ever attained. The Governmental expenditure occasioned by the war had already mounted 180,000,000 yen, of which 130,000,000 yen were covered by revenues from public holdings and other sources. The deficit, evidently, had to be advanced to the Government by the Bank. On account of the circumstances, the issue of about 50,000,000 yen beyond the limit in order to meet the demand of the general market, as well as that of the Government, was considered by the Bank not to be strange in the slightest degree but to be necessary and proper from the very nature of the case.

This issue was, however, all cancelled in May, 1896, when the Bank began to issue on its deposit of indemnity money in the Bank of England which it had secured from the Government, as we have already seen. This measure meant that notes were



being issued by the Bank on a specie reserve in London, the result being that the uncovered issue was replaced by a covered issue.

The introduction of the indemnity money into the country whether by exchange operations or by bullion purchases was not without marked effect upon the specie reserve. In spite of an excess of imported commodities over the exports during the years succeeding 1896, there was no decrease in the specie holdings of the Bank but rather an increase. Thus the specie reserve of the Bank at the end of 1895 was 60,000,000 yen which amount had increased to 98,000,000 yen two years later, that is, by the end of 1897, while the excess of imports over exports during these two years amounted to 108,000,000 yen, a sum needing to be offset by specie exportations. But as a matter of fact, this excess entered the Treasury in the form of notes while the trade balance was paid in London by the Government out of the indemnity. After the war the Government expended its money in the furtherance of schemes of considerable extent, and from the nature of the expenditure the State's money was broadly distributed among the laboring classes at home. Thus the consuming powers of the lower classes, at the close of the war, increased enormously and concomitantly with this movement industrial enterprises had to be projected to meet this increased demand of the consuming classes. On the other hand, the loanable capital on the market was insufficient to satisfy the demand for it. Since the money market was tending more and more to stringency, and some banks even had recourse to suspension, the Bank of Japan raised its rates one-tenth of one per cent, in September, 1896.

Shortly after the opening of the year, 1897, the money market lost its active appearance, and nearly every bank reflected the monetary condition. The Bank of Japan, however, con-

tinuing its monetary policy, raised its rates in the month of June. Toward the latter half of the year the money market became again disturbed, and for this demand the Bank resumed the issue of notes beyond the limit, in July. What one must notice here is that the Bank had no other alternative than an issue of emergency notes, in its effort to arrange the market, the case being that there was no Government deposit of the indemnity money in the Bank at this time. In August and October the rates of the Bank were still further raised while the facilities for loaning were extended as much as possible. This was to be seen from the fact that the amount of capital thus advanced, by the end of the year, excluding loans to the Government, reached the largest figure in the history of the Bank, viz., over 104,000,000. With this enormous advance, the issue of notes naturally corresponded, mounting up to 226,000,000 yen, of which about 47,000,000 yen were issued beyond the legal limit. To devote one word to the subject, this latter kind of issue continued after the war practically without interruption. Indeed its disappearance during the interval, May, 1896 to July, 1897, was possible only because of the presence of the specie in London, as has been described. The emergency issue, at this time, was, therefore, not specially adapted to afford a remedy for the disquietude of the market. As such an issue was inevitable at all times, it naturally became a question in men's minds whether the legal limit of 85 millions of yen were not too narrow, since an 'emergency issue' was constantly necessary to supplement it; and 'emergency issue' was a term whose unknown terrors were apt to affect the market psychologically in a very adverse manner. But the limit was not extended until 1899.

The year 1898, came in without such an easy condition of the money market as usually attends the opening of a year. The Bank raised the rates successively in February and in March.

On account of the stringency, business enterprises ceased almost entirely from their activity. The quotations of Government bonds and nearly all other stocks became lower and lower, and the condition finally became so serious that certain corporations, banking and industrial, seemed about to be pushed to the wall. The Bank, as the agency of the Government, began to purchase the public bonds, and, at the same time, certain other measures were initiated by Government with the intention of relieving the situation. Down to the latter half of the year, these reactionary phenomena continued to appear. The general purchasing power diminished and commerce and industry perceptibly declined. The result being no demand for capital, the money market quieted down once more. The favorable condition of foreign trade and good crops, combined, made the Bank lower its rates twice,— in October and in December.

The recent general business expansion necessitated the extension of the note issue limit by 35,000,000 yen beyond the amount heretofore allowed. The 'Higher Council of Agriculture, Industry and Commerce'\* which met in October, 1898, presented an opinion to the Government with respect to the extension of the legal limit of the issue. Among other things, it was said that "There has been a vast development in all branches of business and industry since the time when the existing limit was authorized. The foreign trade has trebled since that time. Now, such expansion means an increased demand for money.

\*The Council, somewhat analogous to the German Volkswirtschaftsrath and established under the auspice of the Minister of Agriculture and Commerce Department of the Government, is an advisory organ to the Administration for determining national policies upon all lines of industry. It consists of twenty or thirty members who are nominated by the Government from the business men of the first rank, specialists on political economy and finance, and high officials of the Governmental Departments with relation to commerce, industry and finance.



Nevertheless the check of a minimum tax of 5 per cent is still imposed upon all note issues exceeding 85 million yen. The result being an inevitable advancement of money rates, it is natural that a serious condition of money market should not infrequently take place. As a matter of fact, the remedy of an emergency issue has to be employed in a normal condition of the market, a practice contrary to the principles of its salutary regulation. It is expedient, therefore, to extend the legal limit to 120,000,000 yen." The Administration which had been considering such an extension adopted readily this suggestion and presented a bill effecting this end to the Imperial Diet, which passed it immediately. On March, 1899, the measure became a law by which the legal limit was extended to 120,000,000 yen. With this extension, another law came into existence also which requires of the Bank a tax on its issue.

The Bank has thus derived from experience the course of action which it should pursue in performing its three significant offices for the nation. The Bank has already developed in every direction from its infancy, not only in the external forms of its organization, but also in the internal management. Brief, however, has been its career so far, some seventeen or eighteen years merely. It is inevitable that the Bank will develop more and more with the economic growth of the nation in the future and exercise its functions as the central bank with ever increasing precision.

But before leaving this chapter let us consider for a moment what course this future development of the Bank will be apt to take. From the facts which have been presented so far, it can be seen how different is the position of the Bank of Japan in its money market from that of the central banks of European nations in theirs. The Bank is, at the present day, in direct contact

with the commerce and industry of the nation, freely advancing its credits at all the times, normal or critical. At the present stage of the economic development of Japan, this is necessary, and an even wider sphere of action for the Bank in the financial world is desirable. In the development of modern banking, it is noticeable that bank-note issues constitute the first step of the evolution of credit facilities, preceding, as they do, the mechanism of the check and deposit system.\* Turning our attention to the general banking system of Japan, this same process of development is fairly indicated by the facts of the existing situation. Although the amount of deposits is increasing year by year, they are still far behind those of the leading commercial nations, especially the United States and England; so that the note-issue Bank is still of prime importance and must necessarily be so. One can not, without being aware of successive processes of banking development, comprehend the modern financial system. In order to understand the past and present actions of the Bank of Japan and the course of its future development, we must observe the process of the evolution of society itself. The Bank of Japan being the Bank of banks, its actions should always conform to the vicissitudes of industrial development and thus it would come to lead in orderly process the economic growth of the Nation.

After stating the actual amounts of discounts and advances made by the central banks of France and England, M. Paul Leroy-Beaulieu says: "Il est clair que ces escomptes et avances de la Banque d'Angleterre et de la Banque de France ne représentent qu'une très faible partie des escomptes et des avances auxquels se livre l'ensemble des banques dans ces deux pays." †

\* Cf. C. A. Conant, *The Evolution of Modern Banking*, *Political Science Quarterly*, December, 1899.

† *L'économiste Français*, June 5, 1897, pp. 770-771.

Recognizing the principle underlying the evolution of the central bank, he refers to its true function thus: "C'est que toute grande banque, occupant l'échelon le plus élevé dans un pays et investie du privilège d'émission cesse par là même et doit cesser d'être la dispensatrice habituelle du crédit, même à courte échéance sous la forme d'escompte, du moins en temps normal. Elle devient alors la gardienne de la réserve métallique du pays, la régulatrice de la monnaie fiduciaire, la caisse générale des banquiers, la ressource et la garantie suprême du pays en temps de crise économique et en temps de danger national." Going farther, he says that "La Bank de France est la banque des banquiers, cela est très vrai; mais dans quel intérêt? C'est dans l'intérêt de leurs déposants et de leurs créanciers de toutes sortes. La Banque de France est une banque de réescompte pour les circonstances graves, une banque de réserve, et voilà pourquoi il ne faut pas qu'elle emploie ses ressources en réescomptes ou avances considérable dans les temps réguliers."

The sphere of action of the Bank of Japan will follow this course of evolution and its future development will be directed toward its subsumption of new functions corresponding to those of the Bank of England or the Bank of France of to-day. In this sense, the Bank of Japan is a living organ which will undergo evolutionary development demanded by its essential nature as a central banking institution

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## CHAPTER V.

### THE PUBLIC POLICY OBSERVED TOWARDS THE BANK.

In view of the fact that the Bank of Japan while a private institution is also a national organ endowed with the special privilege aiding its performance of the certain public functions, one can readily perceive how important is the relation of public policy to the Bank.

I. With respect to the pecuniary duty of the Bank. Let us examine first the public policy regarding the pecuniary duty of the Bank. After the legal limit of the uncovered issue of Bank-notes was extended in 1890 to 85,000,000 yen the Bank came to shoulder the following burdens, besides the many services which it rendered to the state as the central Bank :

(1) To advance without interest the sum of 22,000,000 yen to the Government and a certain amount to the national banks for the purpose of withdrawing their notes ;

(2) To rediscount foreign bills to the extent of 10,000,000 yen at the low rate of 2% per annum, in favor of the Yokohama Specie Bank ;

(3) To administer the whole business of public debts ;

(4) To supervise the handling of public money in behalf of the Treasury.

On account of these services, rendered in return for its profitable privileges, the Bank was until recently exempt from any further pecuniary burdens. But as in most nations of European continent there has been in Japan an idea prevalent in the mind

of the public that it ought to participate still more sharing the Bank's profit. For the last few years there have been introduced at every session of the Imperial Diet propositions to impose a special tax upon the Bank, though such propositions failed as often as brought forward. At the time of the recent extension of the legal limit of the security issue, from 85,000,000 yen to 120,000,000 yen, the Government introduced into the Legislature a bill providing for its own participation into a certain share of the Bank's net profit beyond a prescribed limit. The Legislature, however, amended the Government bill, establishing it on the principle of a tax on issue and fixing the annual rate of such tax at 1.25 per centum, but issues bearing no interest or only 1% and less were exempted from taxation. It should be pointed out in this connection, that the Bank is already taxed as a private business association, just like any other legal person of business; and this tax is said to amount annually to over 100,000 yen. Thus the Bank has to make double contributions to the fiscus according to its respective capacities, namely the business tax and the tax on issue, besides performing the pecuniary duties which have been mentioned. At the same time that this tax was imposed on its issue, the Bank increased, in view of the public interest, its advances to the Yokohama Specie Bank to 20,000,000 yen, which is another burden that it has incurred.

At the occasion of the recent legislation just referred to, a strong tendency disclosed itself to tax the Bank heavily and this idea is still frequently voiced by public men. Whether or not this is a proper attitude for the State to assume towards the Bank, we cannot determine too hastily, since the question at bottom involves a consideration of public policy as a whole. The imposition of a special tax upon the Bank, no matter what its forms, is motivated by a desire to prevent the shareholders from deriving

excessive profit from their right of note-issue, which is granted the Bank by the State as a special privilege; while, on the other hand, a fair return to the capitalists who have invested in the Bank's stocks must be admitted. Thus the question is, after all, what the percentage of the tax on issues will leave a fair and stable remuneration to the owners of the Bank. It is scarcely possible to determine with accuracy what is a fair return to the shareholders, even from comparison with the general rate of remuneration redounding to the capital from investments of a similiar nature. As a result of the indeterminate character of the problem, two lines of policy are put forth by their respective advocates,—the one demanding a moderate rate of taxation; the other a heavy rate, but admitting of a limited exemption. It is my opinion that the pecuniary burden of the Bank, imposed in the form of a tax should be moderate, at present, for the following reasons among others:

(a) Its need of establishing more branches, it being the Central Bank. The benefit of the central Bank in promoting commerce and industry should, from its nature, be felt generally throughout the country. "The peculiar advantage of a banking currency issued by a net-work of local banks is in affording banking accommodation to all parts of the country where the system prevails. In this respect, if in no others, a system of local banks enjoys an advantage over a great national bank in promoting the development of industry and commerce.....A single bank of issue usually promotes the commerce of the capital where it is located at the expense of the commerce of outlying sections. This was peculiarly the case in France before the establishment of the independent departmental banks and it became the case again after those banks were deprived of the power of note issue.....The promotion of the banking facilities of the



capital at the expense of other sections has been the feature of all the great national banks of Europe,—at Vienna and Buda Pesth, at Berlin, at St. Petersburg, and at Madrid,—and the countries in which they are situated have lagged far behind England, Scotland, Switzerland, the United States, and Canada in the development of their industrial activity.”\* Such a condition obtains also in Japan. To remedy this inadequacy of the central bank system the establishment of branch banks is indispensable, in lack of which the system cannot satisfactorily serve the public good, in its capacity as the national organ. The Bank of Japan has already pursued, mainly for this reason, the policy of establishing such branches and sub-branches, as we have seen in another part of our study.

Nothing can be of more urgent necessity in Japan than the perfection of means for the conveyance of capital throughout the country, so intense is the demand for it on account of the activity of business enterprise. The equalization and lowering of money rates throughout the Empire by a better arrangement of the banking system are indeed, as has been pointed out, significant functions of the Bank as the economic organ of the nation. The difference of the money rates of the different parts of the country is, however, still so considerable that one can readily perceive the necessity of equalizing the benefits of the central Bank,—though, indeed, he should also take into consideration the demands made by local peculiarities. Since the assimilation of the ordinary banks by the Bank of Japan and their co-operation therewith as auxiliary institutions, upon the latter has devolved the function of affording monetary facilities to the entire country and of properly distributing capital among all localities. For the attainment of these ends there is hardly any better measure

\* Conant, *History of Modern Banks of Issue*, pp. 569—570.

than a further extension of the branch system. Indeed, the establishment of branches or sub-branches will not initially be found profitable to the Bank, owing to the lack, at first, of business activity in those localities where the establishment is made. In consequence, when viewing the question from the stockholders' stand-point, the Bank would likely hesitate before making any such extension. In view, however, of the national interest any such delay should not be allowed the Bank. The case is well set forth in the words of Gilbert, "It is not the banks that give rise to the trade, it is the trade that gives rise to the banks ; though after trade is established the introduction of a bank extends the trade."\* For promotion of trade, even though it results at first not in a gain but a loss to the Bank, the provision of more branches should be insisted upon. For it is always legitimate to demand that the Bank perform its public functions.

Then, again, one should not forget the Bank's rôle as fiscal organ of the nation and its duty as such to so distribute the public money as to ensure the orderly condition of the market of the entire realm. The effective performance of this function also demands the establishment of branches by the Bank, a fact which further justifies our assertion of the preponderating importance of the public duty of the Bank over and above considerations of profit. Only a few years since the Bank began to extend the scope of its operations by means of the machinery of the branch system. Yet, beyond all doubt, the existing form of the Bank does not sufficiently respond to the requirements of the public interest. The Bank should not, in its capacity as the central bank, neglect to do its duty. If it were found too slow in this respect, it would become necessary for the Minister of Finance

\* Gilbert, *History and Principles of Banking*, P. 101.

to force it to provide branch establishments, a step which the Minister is empowered to take by Article II of the Bank Act.

Just here is the point which we must consider most precisely. When the Bank is burdened by a heavy tax, the Government will naturally be obliged to be lax in its supervision of the public functions of the Bank, especially of its establishment of branches, an office which in its fulfillment is likely to lead to loss on the part of the Bank. But, to my mind, what the nation wants primarily from the central Bank is a perfect performance of its public functions, not that it becomes a source of revenue. The Government, of course, may oblige the Bank to subserve both ends, but this is by not *á propos*. Whenever the two aspects of the Bank's public relationship come into conflict, the Bank as the nation's fiscal and economic organ must always prevail over the Bank as a source of revenue, either public or private. For this reason we believe that the tax rate levied against the Bank should be moderate rather than the contrary. How, indeed, can it be a legitimate policy to levy upon the Bank so heavy a rate of taxation as to make impossible the establishment of branches and the consequent extension of its administrative expenses without loss on the part of its shareholders? Of any augmentation of the pecuniary burdens of the Bank in performing its primary functions, no stock-holder can complain. But it is otherwise with a tax burden. Although both are equally pecuniary burdens at bottom, yet there is a great contrast between them from the very *raison d'être* of the Bank.

(b) Necessity of its fiscal aid in normal times, as well as in emergency times. The greater part, if not all, of the capital and surplus of the Bank are invested in the Government bonds, which is undoubtedly a considerable burden to the Bank. The reason for the Bank's so acting, contrary to the requirements of profit



making, is its regard for the national interest. Its services rendered to the Government in capacity as the fiscal organ, are important, particularly, for the maintenance of a higher premium on the public bonds, while thus the Bank is frequently required to sacrifice its own profit, though, of course, within limits, solely for the profit of the Government. The Bank does not retire from its co-operation with the Treasury on the ground that such co-operation diminishes its own profit. Although the loss to the Bank thus resulting can not be accurately calculated, yet it is frequently an appreciable pecuniary burden to that institution. This does not include expenses usually incurred in the administration of Government bonds. The presentation of an illustration will make the case plain. In the year of 1899, the Government raised a foreign loan of £10,000,000 on the London market. Not only did the Bank transact all business, in connection with the issue of the bonds, but it furthered the raising of the loan in every possible. And in this latter connection, I want to point out that the Bank was itself a subscriber for £2,000,000 out of the entire £10,000,000 raised. The reasons given by the Governor of the Bank in his annual report for the Bank's taking such a measure are two: (1) A desire to enable the Government to secure more favorable terms on the London market than would otherwise have been obtainable, and, (2) a desire to own national securities salable on the foreign market at any time such sale should be necessary for the maintenance of the convertible system. We shall not here enter into any further discussion of the Bank's subscription to this foreign loan, but it is, for our purpose, worth while to observe how, by this action, the Bank assisted the administration of the public finances in furtherance of the fiscal interest of the Government, even at a loss on its own part. Whenever the Government has had to raise money on the foreign market a most elaborate

discussion has always been given rise to by misapprehensions for the national credit. In view of this fact, it is obvious that such action as was taken by the Bank had a very salutary influence in the way of supporting the general credit of the nation and making that credit realizable in the form of a loan.

But the performance by the Bank of its duty as fiscal organ of the nation may occasion pecuniary loss on its own part, not only when the national credit is to be preserved but even when it is called upon to handle the public moneys. Nevertheless, the Bank is not at liberty to retire from its rôle because of the resultant disadvantages to itself. For this is one of its prime and most essential functions, viewed from the standpoint of the commonwealth and largely motivated its establishment. In times of emergency the Bank's activity in the assistance of the Government is of course much increased. It often happens that administrative projects depend for their success upon its despatch and secrecy. Thus in the conduct of its financial affairs, Government invariably first turns to the Bank, which, in admirable disregard of the dictates of its own private interest, is always ready to respond. The Government would find it well nigh impossible to render adequate compensation for such services. Certainly wise statesmanship demands that the Bank be so supervised and guarded as to keep it ever prompt in serving the nation with its own resources. But the policy best adapted to securing this end is one of a moderate tax. Only thus can Government obtain the Bank's efficient co-operation when it is needed.

(c) The necessity of a strong confidence in the Bank. Since the Bank has the three essential functions which we have enumerated, confidence in it should obviously be the strongest possible throughout the nation ; that is to say, confidence in it should not be inferior to that felt in the State itself among business circles.

And we are amply justified in making this assertion when we remember that that institution is the chief foundation of the entire credit system of the nation. In this sense, the Bank assumes a more or less representative character in the eyes of foreign countries with respect to the national credit. Whether or not the credit of the Bank reflects directly as well as indirectly that of whole nation, still that is the fact. In a demoralized state of the central Bank's credit there cannot be prosperity in the nation at large. It, therefore, becomes evident that public policy should be directed toward securing an end of such primary importance: viz., a strong general confidence in the Bank. To be sure, there is no one who today entertains any suspicions of the credit of the Bank. We do not assert otherwise. It must be borne in mind, however, that the Bank has only a short history. Its career is of fewer than twenty years. A moment's comparison with either the Bank of England or the Bank of France will enable us to discover the difference of their situation from that of the Bank of Japan. Japan being in the process of rapid industrial development, it is very probable that the Bank will, in succeeding years, confront ten-thousand phenomena which will tax to the utmost the resources of its management and which demand for the present the constant upbuilding of its credit and stability.

As to what are the essential qualities which engender confidence in the Bank, many might be enumerated. We prefer however to especially emphasize only two; namely, (1) its financial success, and (2) its administrative capacity.

(1) *Its financial success.* Since the Bank is purely a private institution in its capitalistic constitution, it is very evident that its financial success has fundamental connection with confidence in it as the Central Bank. Indeed, financial success is the condition sine qua non of the existence of the Bank of Japan, as such. **Fi-**



nancial success and honest management comprise the basis of trust in such an institution. Moreover, the Central Bank, in the fulfillment of its public functions, needs the prestige and instrumental aid of financial competence. The independence of the Bank from Government in matters of credit and finance is not only extremely desirable, but, indeed, is the spirit of the Bank Act. It is largely for this reason that the Government, in spite of its subscriptions as a capitalist at the outset, immediately renounced its part as stock-holder. It desired to avoid assuming to itself direct responsibility for the profit or loss of the Bank, while on the other hand it was necessary that it still superintend in large degree the management of an institution, whose success and the confidence engendered thereby are matters of such paramount importance to itself. In the constant upbuilding of its credit and in the strengthening of the foundations of its policy of financiering, the Bank is not left without some guidance by the Act, though these are matters left, for the most part, to the discretion and prescience of the management itself.

(2) Its administrative capacity. The consideration of the financial success of the Bank is drawn chiefly from the view-point of its private ownership. The requisite at present under consideration: viz.—its administrative capacity is on the contrary to be viewed largely in connection with its public functions. The great functions the Bank has to subserve either as the economic organ or as the fiscal organ impose upon it considerable responsibility for the administration. Herein, of course, the Central Bank differs from ordinary banks. It is only as we come to feel the relation between administrative capacity and confidence in the Bank, that we begin to appreciate the greatness of the Bank's responsibility for the former. The work of the Bank, as has been pointed out, does not end simply with that of discriminating com-

mercial papers, but extends to the more complex functions of currency regulation and the like. Although its administrative capacity is largely due to clear, prompt judgment on the part of its officers, rendered possible by their experience, yet none the less important, on their part also, is a thorough mastery of economics, enabling them to read with discerning eye the multitudinous phenomena that daily reveal themselves both at home and abroad. This means not only a thorough acquaintance with the experiences of foreign nations, but also constant investigations, both statistical and analytical, into the conduct and conditions of economic society;—knowledge without which the salutary arrangement of the financial market could hardly be effected. Also, for the perfection of its administrative capacity various instrumentalities must be provided within the Bank, thus calling inevitably for an increase in its current expenses. But this fact must not, for a moment, stand in the way of the fulfillment of its office as the National Organ, a capacity demanding even more and more accurate and extended knowledge of the financial phenomena attendant upon the economic and industrial development of the country. Now, a heavy tax upon the Bank, provoking a tendency to curtail administrative expenses, is bound to affect detrimentally its administrative capacity and consequently the public's confidence in it.

(d) Governmental control over the accounts of the Bank. One more reason might be added why the tax rate imposed upon the Bank should be moderate. As we have seen in the chapter on the organization of the Bank, the Government has not only the power of appointing the Bank's administrators but it also has complete authority and the necessary machinery to examine and supervise all the accounts and actions of the Bank, however minute in point of detail. The entire accounting system of the

Bank is, therefore, thoroughly fair, and no concealments nor secrecy is possible under it. More than that, the rate of any other dividend than the first dividend of 6% per annum must be determined, according to the by-laws of the Bank, with the sanction of the Minister of Finance. Thus it appears that the division of profits is, after all, subjected to the strict control of governmental authority. Such being the case, no illegitimate or excessive remuneration can be pocketed by the stock-holders of the Bank,— a very palpable difference from the course usually pursued by corporations in their division of profits. This fact then makes it unnecessary, at the very least, to impose a heavy rate of taxation upon the Bank.

What I have thus far said tends, in fine, to this result: that the Bank should be so directed as to subserve, to the *maximum*, the public interest, while the tax should be levied upon it at the *minimum* rate. The satisfactory performance of its public functions is our primary requirement of the Bank and its contributions to the State in the form of taxes constitute but a minor consideration. Regarding the Bank of France, M. Wolowski writes as follows: "C'est que la Banque de France n'a jamais perdu de vue des obligations que lui impose son caractère d'institution publique; elle a constamment fait passer le soin de l'intérêt général avant le désir d'augmenter les bénéfices des auctionnaires."\* We look upon the Bank of Japan in precisely the same light. But while it is necessary that the shareholders of the Bank should always be kept conscious of their situation, yet, at the same time, they should not be too sorely tried; their own private interests should be brought as little as possible into conflict with the interests of the public. Our conclusion is, then: let strict supervision and moderate taxation, on the part of the Government, make possible,

\* La Question des Banques, P. 5.



on the part of the Bank, the fulfillment of its business duty to itself and its fiscal and economic duty to the nation.

Sometimes arguments are deduced from the current tendency in the continental Europe to impose heavy pecuniary burdens upon the central banks. The case of the Bank of Japan is hardly analogous. Circumstances attending the situation of both the nation and the Bank are entirely different in Japan from those of continental Europe. A national policy should be judged of in the light of conditions, and especially does this remark prove true, when it comes to devising a system of taxation.

II. With respect to the Administration of the Bank. What shall be the public policy with respect to the administrative sphere of the Bank, is the question now under consideration. In other words, how far shall the Government exercise control over the Bank, and to what degree shall the former enter into the business policy of the latter?

In connection with a further analysis of the problem we have presented to us, in the first place, the difficulty that would arise should the Governor of the Bank and the Minister of Finance dissent, one from the other, as to the *business* policy of the Bank. In the next place we may consider the control that Government itself exerts upon the *administration* of the Bank. The points of contact may be thus enumerated: First,—the Government has a veto upon any policy of the Bank which it may deem to be detrimental to the best interests of the public as well as of itself. Second,—for its inspection of, and even the control over, the Bank, it has specially provided officers, called Comptrollers. In the third place, the Governor and the vice-Governor are appointed directly by the Government, and the Directors are also more or less under its influence in the method of their appointment. Fourth and lastly, though not least, alterations in the

money rates of the Bank are made only with the sanction of the Finance Minister. From this enumeration one can derive some idea of how strong Governmental control over the Bank really is. Such thorough Governmental control, however, may sometimes result in unfortunate determinations of the Bank's policy, and the fiscal interest of the State may be made to overshadow the commercial interest of the whole nation. And it may further happen that the interference of Government may be the direct force determining what form the administration of the Bank shall take. For, as I have already pointed out in another connection, the Governor of the Bank is not vested, at least by virtue of the law, with the final responsibility for the policy of the Bank, which is left, for its ultimate determination, to the Government or to the Board of Directors. All this goes to show how entirely the Bank's administration is subjected to the discretion of Government. Whether, at the present time, such a policy conforms to the best interest of the nation is questionable, because banking, after all, is a *trade* differing widely in character from political service. On this account, there is nobody in Japan who advocates direct management of the Central Bank by the Government. That the idea of the Act establishing the administrative system of the Bank was also averse to Government's exercising such a function, is fairly evident from the elaborate system provided, which calls into requisition an entire hierarchy of governors, directors, auditors. Such being the principle underlying the Act, there can be no doubt that the Bank is entirely too subservient to Government in its administration, which approximates State management. In short, the respective spheres of influence, of Bank and Government, are not clearly and distinctly demarked.

At this point a criticism upon the present system of the government of the Bank is often presented, favoring the election

of the governor from the shareholders as in the case of ordinary joint-stock associations. The advocates of this reform argue that the Bank should be independent in every way from the Government on account of its private ownership, which, they assume, does not allow of any administrators appointed by Government. This argument, however, has no sound basis, because it identifies the central Bank with the ordinary legal person, forgetting that its essential nature is imparted to it by its national functions. So far as theory goes, the criticism is all wrong, and we may assert the very reverse; viz.,—that the Government may very properly choose its functionaries. But the point at issue, I believe, is one of public policy. Whether the Bank has its administrators elected or appointed is a question to be decided from the standpoint of public expediency. What we want is that the administration of the Bank render it as competent as possible to exercise its essential functions in the public's behalf.

Another argument in favor of an elective governorship alleges that thus will the Bank be kept aloof from political contest. They say that under the present system tenure of office in the governorship is determined by changes in the cabinet and, hence, that the evil of the office's being utilized by partisans is a very possible one. Also they argue that it is due to the appointive character of the governorship that the Governor may be forced to resignation whenever he dissents, concerning the Bank's business policy, from the opinion of the Minister of Finance. The argument that alleges discontinuity of governorship subject to cabinet change has not proved true in Japan. Nor, as long as the main business of the Bank's administration is dependent not upon considerations of politics, but upon those of trade, will it prove true. As has been already mentioned, the Governor has a term of five years, and as a matter of fact he is reappointed so long as his



ability is evident and his policy is popular. One can readily see that there is no connection between the position of Governor and cabinet politics. Whenever necessity demands that the Government exercise control over the Governor in the interest of a certain line of policy, it little matters whether he holds his position by virtue of election or of appointment. As to cases of difference between the Governor and the Minister of Finance, the resignation of the former is the only feasible alternative at such times, since his responsibility is a nullity and the Minister's prerogative is plain. Strictly speaking, the position of Governor is, from present practice, merely that of an executive agent of the Finance Minister. In our opinion, therefore, unless the relation of Governor to Minister is made less distinctly one of client to superior the difficulty under consideration cannot be removed, and, of course, the system of an elective governorship is totally inadequate to its solution.

Again there are those who say that in order to remove the subservience of the Bank to the Government, the one way open is to have the administrators elected from the shareholders. This scheme, however, provides a remedy of very doubtful merit. For in thus attempting to eliminate a partial disadvantage from the present system, we should destroy all its virtues. Before resorting to so radical a departure, we should first endeavor to discover some remedy, which, while preserving the advantage of the present system, removes its unfavorable features. To this task we now address ourselves.

Having so far analyzed criticism upon the existing system, we now have to consider what policy public expediency demands shall be observed toward the administrators. The administrators of the Bank must be men of great ability, knowledge and experience.† Since the Bank is the national organ vested with

† Cf. Gilbart, *History and Principles of Banking*, p. 313.

many public functions, the qualifications of the administrators are necessarily of particular importance. That the living organ, the Bank of Japan, acts largely in accordance with the dictates of officers rather than in accordance with prescribed regulations indicates the exceeding importance of its administrators. How to secure them is a question to be answered differently, according to the different conditions of each nation. The system of appointed governors which has proved so successful to the central Bank of France might not answer so well in England, and vice versa.\* So, the relative merits of elective and appointive administrators must be judged of in Japan in light of her real condition, in view of which fact I favor the present system of the Bank administration. In the first place, under the existing system we can get the best men for the position. Again greater administrative constancy, efficiency, and confidence can be secured thus than otherwise. Thirdly, the public's interests as well as the Government's can be better preserved by such a system. In short, the Bank is administered, under the present system, by those who are thoroughly conscious of just what the central Bank of Japan is. On the contrary, the other system has not only this drawback, that it can hardly secure the best men, but it is also apt to put into power a shifty administration. Attempts among stock-holders of business associations at undue alterations of the administration are very frequent in Japan, owing to the absence of business ideals among the Japanese people. Many such instances have occurred recently in large corporations: e.g., the Nippon Railway Company, the Kyushu Railway Company, Japan Mail Steamship Company and other large banking institutions, showing the truth of my statement.

\* Bagehot, Lombard Street, pp. 70-71.

After all, public policy towards the Bank must be directed toward obtaining the strongest administration wherefore I am decidedly inclined, in view of the real condition of the nation, to insist upon the present system of Bank administration.

One might object that the system of an appointive governorship might be apt to disregard entirely the interests of the owners of the Bank. It is under the existing system, however, that the directors are made representative of the will of the shareholders and the auditors moreover are elected entirely from their number, so that the objection is immediately found to be absurd.

Having decided in favor of the appointive governorship in the administration of the Bank, our next question concerns the precise relation of the Bank to the Government. It is at this point that adverse criticism finds an entering wedge. For it is to this relation that such evils as the liability of the business of the Bank to interference from the Minister of Finance, excessive subservience to the Government on the Bank's part, and certain ambiguities of relationship, are assignable. The power of the Minister to interfere in the Bank's business was probably a necessity initially, because in its infancy the Bank was but a component part of a grander scheme of financial arrangement. But we should understand in the first place, that the minister is, after all, a politician rather than a business man, while the Bank administration ought to be exclusively an affair of the latter sort. An excessive subservience on the part of the Bank to the Government will lead to the sacrifice of its commercial interests to its fiscal interests, while the completest harmony of all interests is the true aim of the Bank. I am opposed, therefore, to introducing any radical alterations into the existing system, but, nevertheless, strongly insist upon the reform of certain defects in the present practice.



(1) All the administration of the Bank should be entirely entrusted to its officers. What I intend is to make clear the respective spheres of action of Government and Bank, because their indistinction is a real source of difficulty in the Bank's administration. So far as administration and business policy are concerned, the Bank should act upon its own responsibility allowing of no intervention on the part of the Government. An essential point in the business policy of the Bank is, undoubtedly, involved in the power of rate-making, which at present cannot be exercised except with the sanction of the Finance Minister. This is an intervention by Government in the Bank's business which must be entirely done away with according to our view. It may sometime not only occasion a great misfortune, but it always results in making the residence of business responsibility not with the Bank but with the Government. Administrative despatch is indispensably necessary in the action of the Central Bank, and to this, the governmental intervention must surely be an obstacle. As we have seen when analysing the work of the Bank, occasional difficulties may arise in the determination of business measures. In case of disagreement between the Governor and the Board or the Council, the deciding power should remain, as in the present system, with the Minister of Finance. But a more serious case arises when Government and Bank disagree at which time the resignation of the Governor may perhaps be forced. When the determination of the Bank's business policy lies solely in the hands of its administrators, such a difficulty will no longer be possible. In view of the fact that the governor is appointed by the Government, we can hardly see the necessity for governmental intervention in the Bank's business, especially since the result of such action is frequently to occasion grave disorders of administration. Our proposition if

carried into effect, would indeed augment the responsibility of the Bank, which might, however, very properly take place, otherwise the institution may become really, though not apparently, an official bureau of the Finance Department of the Government. It would enhance the power of the Governor, because whenever the Governor endorsed a decision of the Board or the Council the intervention of the Government would be excluded; but it is just such a course of procedure, I think, which supplies a valid reason for an appointed governor, otherwise he is likely to become a mere agent of the Treasury of the Government. Let not my meaning be misapprehended. I do not minimize the importance of governmental influence and advice, but I do insist that the Bank's responsibility should be made adequate.

(2) Governmental supervision should be more strict. Although the Bank should act mainly in accordance with the business principles of sound banking, it also should regard many regulations expressly prescribed by laws and by-laws on account of the particular functions belonging to it as the central institution. There would be no need here to dwell upon the nature and necessity of governmental supervision, but for the important part it plays in the furtherance of the public's interests. But for this reason it deserves especial emphasis. One reason why Government should withdraw from business interference with the Bank is, that its energies may be entirely devoted to the task of supervision. With such a distinction between supervision and administration the Government can more satisfactorily perform its proper duty towards the Bank. The veto power of the Finance Minister upon all actions of the Bank contrary to the best interest of the nation, should remain without the slightest change, which might impair its position as the Central Bank.

(3) A closer connection between the Bank and the Treasury

should exist. We have already stated that the work of administration should be entrusted to the Bank while its governmental supervision should, at the same time, be efficient. Thus, the relation between the two would be definitely brought forth without any further ambiguities. Next I shall call attention to the close connection between the Treasury and the Bank, necessary for a satisfactory management of the money market. This necessity arises from the fact that the State is a great economic person. If, now, both Bank and Treasury should project measures without any understanding between them, the result would probably be disorder in the economic community. The State should allow its own fiscal interest to be modified by consideration for the public good of industrial society, while the Bank, on the other hand, should act as an economic as well as a fiscal organ. The harmony of both interests must be considered, since the business welfare of the nation demands it. Thus the business measures of the Bank will take into account the fiscal interests of the State, for which service, in addition to others, the Comptrollers are appointed. And it is equally necessary that the fiscal measures of the Government be harmonized with the demands of the money market, for which end its views should be available by the Treasury. Up to the present time, the Treasury has had a marked influence upon the Bank, a relation however which is not reciprocal; wherefore many find an opportunity to accuse the Bank of subservience to Government. Chiefly to this lack of mutuality can be traced the recent economic disorder of Japan, as evidenced by the vast discrepancies between budgets of different years. A constant interchange of the views of both interests would make matters more satisfactory than at present.

(4) The business sphere should be less restricted. As we have noticed, the sphere of the Bank's loaning and discounting



power is restricted by the Act to commercial papers of short term and to loans on collaterals of a very limited number, loans on real estate and industrial enterprises being entirely prohibited by the Act. All such provisions of the law are aimed at maintaining the safety of the convertible system by keeping the Bank's assets in a form easily convertible into cash. The rule is a safe one and one which an issuing bank ought always to regard and a violation of which has often occasioned tremendous disaster as shown by the experience of several nations. It must, however, be remembered at the same time, that, a too rigid observance by the Bank of this general rule may lead to a lack of capital facilities and sometimes even to unnecessary anxiety in the business world. For just these reasons, the industrial disturbance of 1890 caused the Bank to widen its sphere of business operations to include collateral loans of a very limited number of kinds. Good negotiable securities may be regarded as quick assets, to which, in my view, the Bank should still further extend its loaning privileges, though, as a matter of course, such action must be performed with caution and judgment. It is desirable to permit to the Bank an elastic extension of its loaning sphere at the present stage (I do not say at a future stage) of the economic development of Japan in which industrial enterprises are, for the most part, being conducted in close union with commercial transactions. No commercial development is expected there outside of certain lines of industry. To what sorts and in what proportion an extension of collateral loaning may take place is a matter to be considered in light of the economic necessity of the nation and the condition of the Bank itself. I am not saying that the Bank must necessarily extend the sphere of its business operations, but that too rigid legal restrictions upon it in this respect should be

removed. A high authority makes the following wise suggestion :

“ Les ressources que l'émission des billets à vue et au porteur fournissent aux banques de circulation sont infiniment moins mobiles que les dépôts particuliers des banques de première classe.....Elle peut donc faire, contrairement à l'opinion en France, des placements à plus longue échéance que les banques ordinaires qui opèrent sur des dépôts particuliers.

Lorsqu'une banque de circulation est ancienne, elle peut considérer son minimum de circulation comme un dépôt permanent et faire avec les capitaux de ce dépôt, des placements à long terme. Je ne dis pas qu'elle doive le faire, ni surtout qu'elle ne doive pas réfléchir beaucoup avant de s'engager dans cette voie; mais seulement qu'il ne faut avoir sur ce point ni préjugés, ni craintes superstitieuses.” \*

Furthermore, in Japan, at the present day, commerce and industry are in the same hands ; so that a legal provision is needed which shall allow the Bank as much elasticity as possible in the adequate use of its powers, on occasions of anxiety, for the accommodation of solvent business men and the relief of the market from a useless panic. And, of course, to make less restricted the sphere of the Bank's business operations means to increase the sphere of the Bank's business responsibility.

To resume,—our conclusion with respect to the administration of the Bank is, that a distinct line of demarkation should be drawn between Government and Bank, the former confining itself to the supervising function, the latter incurring full responsibility for the business administration. Such, I believe, is the best policy to be observed toward the Bank, being seemingly adapted to securing perfection of business action on the part of the Central Institution, and to the elimination of the existent difficulties of administration.

\* Courcelle-Seneuil, *Opérations de Banque*, pp. 192-193.

THE END



### ERRATA.

Page	1,	Line	12,	For condition	read	a condition.
"	5,	"	3,	" a capital	"	with a capital.
"	9,	"	22,	" atpartiality	"	at partiality.
"	10,	"	13,	" national system	"	national banks system.
"	13,	"	8,	" whose	"	who.
"	15,	"	6,	" the Bank	"	because the Bank.
"	36,	"	20,	" notes	"	bonds.
"	41,	"	13,	" 19,695,622	"	29,695,622
"	"	"	15,	" 11,474,992	"	11,473,992
"	55,	"	15,	" adqutely	"	adequately.
"	64,	"	13-14,	" wares house	"	ware-house.
"	"	"	22,	" curren-	"	current.
"	104,	"	bottom	" existance	"	existence.

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