

The Risk Control of Qianzhuang

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Abstract

Qianzhuang is the traditional bank born in China. During the late Qing Dynasty to the Republic of China, plenty of historical data proves that Qianzhuang has always been a true financial service provider for Chinese agribusiness and commercial households. The control of deposit and loan risk in Qianzhuang is a concentrated expression of the localization advantages of Qianzhuang, and it still has a strong enlightenment for the risk control of contemporary financial institutions. This paper elaborates the risk control mechanism of Qianzhuang by explaining the risk control of Qianzhuang credit loan and the prevention mechanism of the credit risk, and further discusses the effectiveness of the risk control in Qianzhuang. Money Industry Association was built mainly to resist industrial risk. So there also is a discussion about Money Industry Association's function to resist industrial risk.

Key words: Qianzhuang; Risk control; Credit loans; Money Industry Association

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1. THE MAIN FUNCTIONS AND ORGANIZATIONAL STRUCTURE OF QIANZHUANG

From the late Qing Dynasty to the Republic of China, from townships and cities to the general public, Qianzhuang

was everywhere, and played an important role in the social economy and the modernization of China's industry and commerce.¹ Through the financial exchanges between Qianzhuang and Qianzhuang, Qianzhuang and Piaohao, Qianzhuang and domestic and foreign banks, a huge financial network was established to communicate cross-regional trade and foreign trade. As we can see, Qianzhuang is one of the most representative forms of business development in China's financial industry. It plays an indispensable role in the history of finance and even economic history, as well as the transition from traditional economy to modernization.

The internal organization structure of Qianzhuang is following the figure 1: eight butlers structure. Apart from the manager and manager's associates, other staff members' positions are based on the "eight butlers".

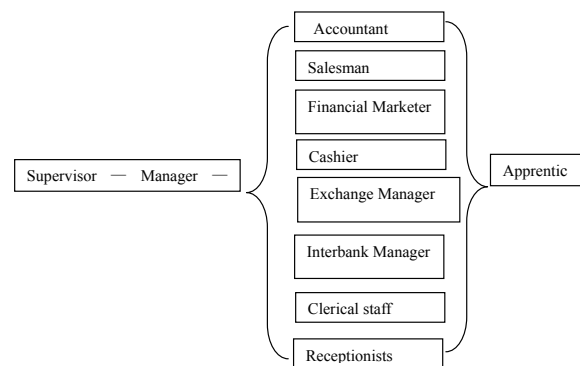


Figure 1
Eight Butlers Structure

Every position in the "eight butlers" is ranked according to its importance to Qianzhuang, so the

¹ "Qing Gao Zong Shi Lu", Volume 165, Qianlong seven years in April. This was the official literature for the first time to record Qianzhuang. It says: the shopkeepers are different, the government should check out how many shopkeepers and Qianzhuang for every territory, and list as a book.

order of their positions is slightly different for different Qianzhuang. Qianzhuang in short supply relies on interbank manager lending money. Rich Qianzhuang ranks salesman first to expand business, while interbank manager and accountant rank second and third. So the specific arrangement totally depends on the business strategy.

Within Qianzhuang, the manager has great power and is the highest decision maker, the manager is responsible for all the daily trifles, transactions and staff transfers. Therefore, in order to achieve the sustainable operation of the Qianzhuang, shareholders should first carefully select a qualified manager, and then give him the greatest trust. At the meantime, in order to ensure the interests of shareholders, some shareholders appoint supervisors to supervise the manager's work, so as to report to shareholders at any time. Besides, there are several associates assisting manager.

In addition, from apprentice to manager, the number of employees in each position is uncertain, all employees are shifting according to business scale and business focus. Staffs are mostly employed by shareholders or recommended by managers.

Such an organizational structure can not only maintain the authority of management, effectively implement policies and guidelines, but also could flexibly adjust to specific business with strong adaptability. There are not only checks and balances between the same level, but also supervisory constraints between the upper and lower levels, which enhance the ability of enterprises to withstand risks.

2. THE RISK CONTROL OF QIANZHUANG CREDIT LOANS

2.1 The Objective Existence of Credit Loan for the Local Business

The Qianzhuang loans are mainly credit loans, merely mortgages, as they have always been since Qianzhuang was founded.

This is because credit loans are mostly needed for the local business. First, in modern China, agricultural economy was the main economy, every year, a large number of agricultural products would be purchased, processed and trafficked, which requires a large amount of funds, but those business dealers could not provide collateral. Second, traditional commerce in China are not industrialized as the West, fixed assets investment is rare in businesses, but liquidity accounts for the majority, so it's hard to mortgage. Third, even for some modern factories, the capital invested by entrepreneurs is often only used for the purchase of fixed assets, while liquidity relies on borrowing, and even some enterprises rely on borrowing when purchasing fixed assets, so it is rare to

have enough collateral.

The lending business of Qianzhuang is entirely based on credit, which seems to be very risky. In fact, there exists an implicit and effective risk control mechanism. The risk control of modern banks pays special attention to objective data, the most typical example is financial information, so the modern risk control investigation must check the accounts of credit granting enterprises. However, for Qianzhuang in the traditional banking industry, no auditing is allowed. The fact that Qianzhuang do not check accounts is not that credit-granting enterprises do not have accounts to check. Traditional firms, of course, own their traditional accounting, which is also very meticulous.

However, the current capital situation of Chinese traditional firms is very liquid. For example, Chinese traditional firms always carry out unlimited risk liability. There are two kinds of own funds, one is the equity capital, the other is the demand deposit in firm deposited by shareholders, which is called copy or passport. Because shareholders often own many firms, their deposits in one firm are often variable. For example, to withdraw from No. A, or withdraw from No. C, deposit into No. B, as a relief fund to help No. B who is insufficient. Moreover, if a firm is facing a broken capital chain, with poor liquidity, or debt crisis, shareholders will take unlimited risk responsibility to ensure the interests of creditors with all their capital strength outside Qianzhuang. Not only that, when necessary, shareholders can also use their own commercial credit to mobilize capital from the social network to maintain the credit of their business.

Therefore, for the risk control of the granting capital to Qianzhuang, there is no practical significance to just check the accounts of one firm. However, Qianzhuang still check the details of their businesses, mainly depends on checking their credit.

2.2 Credit Investigation by "Street Running"²

Chinese society has already formed the credit economic operation rules which is suitable for credit loan. It is said that since the middle ages, the rise of Commerce in the West has been adapted to the rise of civil and commercial law. In China, up to the end of the Qing Dynasty and the beginning of the Republic of China, there was basically no civil and commercial law, but Chinese have developed adequate commercial contacts depended on credit. The credit lending of Qianzhuang operates on the track of this credit economy. Credit survey is the most important thing for Qianzhuang to lend money. Generally, the investigation contents include: the assets of the shareholders, the morality and management ability of the managers, the market conditions and prospects of the invested projects. Even the private life of shareholders

² "street running" is the position of salesman in the "eight butlers" structure

and managers belongs to the scope of investigation.

The accuracy of investigating information is largely related to the geographic relationship and human relations between Qianzhuang and firms. Qianzhuang usually have a special position called “street running” (the position of salesman in the “eight butlers” structure). As the name implies, it means that every day they go to the streets to have extensive contacts with customers and their business associations, and to explore everywhere. In fact, it is equivalent to the current credit investigators. According to the situation of the merchants, the situation of the whole business group and even the industry, and according to the situation of the business group to estimate the business situation of customers. This is something that Western banks don’t have. Their research method is not the current audit. Running the streets never checks the accounts of credit enterprises. It’s a kind of non-standard research.

In traditional society, for every city and every profession, there will be an informal gathering place, like tea house. Businessmen in the same industry no matter they have something to do or not, just gather in a fixed tea house, exchange information and discuss business. The running street of Qianzhuang specializes in this teahouse, making friends with businessmen and listening for information. As time goes by, they will have a clear understanding of those businessmen’s characters, capital strength, current business and current situation. Then they will return to report to the manager of Qianzhuang, and the manager will decide whether to loan money to them or not.

Running street is often the most important functional department in a standard Qianzhuang. Qianzhuang in small towns are totally involved into the local network, while those in big cities often deal with specific commercial group, such as Qianzhuang in Hankou, which have several different groups and do not compete with each other, because Qianzhuang of each commercial group mainly deal with their own businesses in Hankou. Another big city, Shanghai, every Qianzhuang’s Street runner will focus on several industries and established business associations. This kind of special network leads to the thoroughly informing about merchants. Although it is not quantitative, but it is more comprehensive, more perceptual and more accurate. No matter foreign banks or domestic banks that imitated the western system in the early stage, they had neither the habit of in-depth investigation nor the pipeline of in-depth regional business relationship network, so they could not directly contact local customers and provide financial services. That’s the main reason why they can’t lend directly to Chinese businessmen.

2.3 Business Circles Attach Importance to Commercial Credit

In the whole business circle, businessmen extremely value their commercial credit, their credit is their second

life. “A promise is weightier than one thousand bars of gold”, which is often regarded as a basis morality, in traditional society, such morality does exist widely. But in fact, once this habit is formed, it will form an effective exile mechanism. With good credit, even if business is in danger, some people are willing to help, even if business fails, credit is not lost, there are opportunities for a comeback. On the contrary, with bad credit, it will be resisted by the others, every business move is difficult. Therefore, in traditional business circles, credit is not only a kind of morality, but also a kind of practical latent rules. It is no less effective than the law of the West.

The loans of a Qianzhuang are credit loans, and the risk control of credit loan mainly depends on the credit of the debtor. The so-called business credit does not have a normative definition. Generally speaking, it should include three aspects and three levels:

First is the objective aspect, which is the firm owner’s capital strength and property. As mentioned earlier, Chinese firms have always implemented an unlimited risk liability system. Therefore, whether a firm can afford to pay its debts does not depend on the capital of the firm itself, but on the capital strength of its shareholders.

Second is the subjective aspect, which is the moral conduct of the boss, because the loan is assumed according to unlimited risk liability, and how much capital the firm and its shareholders have, loaners can only have a rough knowledge, if the shareholders go back on their words, it is difficult to chase back, so whether the shareholders are trustworthy matters a lot.

The third aspect is between subjective and objective. It’s the social network of shareholders. This kind of network generally refers to the relatives, friends and customers of shareholders. Shareholders have the ability to accommodate capital in their personal relationships. On the one hand, the greater the capital power of shareholders, the more friends, the richer friends. On the other hand, the more credible the shareholders are, the more righteous the friends are. Therefore, the networked shareholders, even without using their own assets, can also get enough capital only by their friends.

Credit, in a deep sense, is the key element for Chinese business circles. This is a Chinese ancient cultural tradition, if a person has god virtue and credit, then his personality is recognized by the society, he will easily accumulate network contacts. If he gets contacts, he will easily grasp business organizations and get more business opportunities. With business opportunities and talents available, he will naturally easily accumulate money. Therefore, in the traditional business circle, businessmen attach great importance to commercial credit, credit is the largest capital. A person’s capital has been lost, but if he maintains his credit, there is still a chance to make a comeback. If you lose your credit, you have no chance. Therefore, the most important risk control of bank lending

is actually to see the credit of a business shareholder in the business circle.

Credit could decide one's career, so when businessmen loan, they rarely default, for fear of losing their credit. But what if someone defaults? How to check and balance? In traditional society, there is no developed commercial law system as in the West. Government for those who do not pay their debts, of course, will give creditors strong support. However, in China's tradition, civil disputes have never been preferred to be settled by judicial means, but mainly by means of civil checks and balances.

More commonly used, of course, is guarantees. This is mainly used when Qianzhuang doubts the creditworthiness of the debtors, but they still want to do this business, so how to control the risk of such people? They ask for a guarantee. For example, if A applies for a loan from Qianzhuang, but Qianzhuang does not know much about A's credit, or has doubts about it, then A could make B as his guarantor to provide a guarantee to Qianzhuang for him. As long as Qianzhuang recognizes the credit of B, it is willing to lend money to A with unknown credit. If A fails to repay the debts in the future, the guarantor B may repay the debts on his behalf.

Is this kind of guarantee reliable? This depends on two points, one is whether the credit of the guarantor is reliable, the other is whether the guarantor is responsible for the borrower. In the former part, as we have already mentioned above, we mainly discuss the latter part, namely, the relationship between the guarantor and the guarantee. Between A and B, there is either a relationship of relative or friend, or business partner. A person who is closest to himself is naturally the most trustworthy. The farther the relationship is, the credit will naturally decline. So, A may be willing to default on Qianzhuang subjectively, but he is unwilling to do something to harm his guarantor (relatives or friends).

In Chinese society, relationship circles are very important. Take everybody as a core, then there is a semi-closed and semi-open circle of contacts. A person in business needs the help of friends in his circle. The relationship between businessmen and circles is like the relationship between fish and water. The businessman relies on his circle to survive and cannot live without it, then the circle will form a restrict to a person. The circle's check and balance to the people in the circle seems very informal, but in fact it is very effective. The reason for this is the so-called "collective exile mechanism" raised by institutional economics.

The collective exile mechanism actually includes three interrelated keywords: semi-closed collective, monopoly profit and collective exile. A semi-closed collective monopolizes an industry, and outsiders can't easily get in. Then it is easy to form monopoly profits. This means that members of the collective can share monopoly profits. Once one leaves the collective, the profits of business

operations will be greatly reduced. On this basis, the collective will formulate some rules or hidden rules that members must abide by together to ensure collective interests. If members violate this rule, they will be resisted by the collective "non-violent non-cooperation", and the members who violate the rules will be pushed out of the collective. This is collective exile. Members, taking into account the role of collective exile, will inevitably abide by the rules or hidden rules in the collective. Therefore, guarantees, because of collective exile mechanism, is very effective.

Above all, Qianzhuang's credit loans, although not mortgaged, are rarely maliciously backed. The risks are not as great as bankers think.

3. THE PREVENTIVE MECHANISM OF RUNNING RISK IN QIANZHUANG

During the late Qing Dynasty to the Republic of China, taking Shanghai's strongest Qianzhuang as an example, even for the first-class Qianzhuang, there may be only ten thousand silver capital and at most one hundred thousand silver capital. But the loan scale of Shanghai's Qianzhuang is generally millions silver. On the other hand, stock capital of banks typically could reach for millions. Therefore, bankers believe that Qianzhuang have too little capital to deal with the runs, which is easy to produce bad debts, and could trigger a chain reaction, to endanger the financial order.

Running is the direct cause of the bankruptcy of financial institutions in the past. It is also the direct result of the credit crisis. If depositors have doubts about the Qianzhuang's credit, then withdrawing deposits simultaneously, and if Qianzhuang fails to pay cash in time, then Qianzhuang will be facing bankruptcy. There are three aspects in the conventional prevention mechanism of run risk: daily balance of income and expenditure, interbank lending and unlimited joint liability of shareholders.

3.1 Daily Balance of Income and Expenditure

In modern banking business, there is a basic concept called deposit reserve. That is to say, the bank must keep part of the cash in order to cope with the depositor's daily withdrawal. Another concept called the deposit reserve ratio, which is the ratio of the amount of reserve to the amount of deposit deposited by the depositor. The larger the amount of deposit, the more cash must be prepared for withdrawal. The higher the reserve ratio is, the more insurable the withdrawal should be, but the cash stays at home without interest income. On the contrary, the more the loan is, the more the interest will be, but the less the reserve, the easier it will not be enough to withdraw. Banks will determine a rough reserve ratio based on their daily expenditure.

In traditional Chinese Qianzhuang, there is no term for reserve and reserve ratio, but there are similar concepts. For example, Shanghai's money industry has so-called concepts of multi-sheet and short-sheet.

The so-called multi-sheet means that Qianzhuang's daily cash inflow (deposit) is greater than its cash outflow (withdrawal). The remaining cash can be borrowed overnight in the interbank lending market to other Qianzhuang. The so-called short-sheet, on the contrary, means that Qianzhuang's daily cash inflow is less than the cash outflow, insufficient cash to pay for withdrawals, it is necessary to find other Qianzhuang to borrow money in the interbank lending market. Therefore, the interbank lending market provides a relative insurance. When some are short of money, the others would provide mutual support. This support is also a way of collective survival, because if one fails, it will often cause large-scale runs as a chain reaction.

3.2 Interbank Lending

In addition to interbank lending, Qianzhuang often borrow cash from larger financial institutions, such as Shanghai Qianzhuang borrow money from Shanxi Piaohao, or from foreign banks in Shanghai, or lately from major domestic banks. Which forms the pattern that the large financial institutions become financial wholesalers and Qianzhuang becomes a retailer.

Qianzhuang in the second-tier cities, such as Jiujiang in Jiangxi, Wuhu in Anhui and Zhenjiang in Jiangsu, may borrow cash and banknotes from Qianzhuang in big cities such as Shanghai. The next-class Township Qianzhuang, such as those in Liyang of Jiangsu province, borrow money from Zhenjiang.

The manager and street runner of Qianzhuang have an important task, which is to establish long-term human relations with big Qianzhuang, Piaohao and banks, to acknowledge the tightness degree of money and interest rate fluctuations in the financial market, and to be ready to borrow more cash when the business is developing and the reserve is insufficient. Shanghai's Qianzhuang is more professional. Three positions of eight butlers are doing this job, namely, Financial Marketer, Exchange Manager and Interbank Manager.

3.2.1 Unlimited Risk Liability of Shareholders³

Qianzhuang do not have much equity capital, usually tens of thousands silver, but the scale of deposits and loans reaches for million. Which is unusually easily misunderstood by bankers. In fact, whether banks or Qianzhuang, the main source of operating funds is deposits, not equity. Equity is mainly used to deal

with credit crisis and to cash depositors in the event of bankruptcy and liquidation. Banks are limited liability, and their equity is their only guarantee of credit to depositors. The situation of Qianzhuang is different. When a credit crisis occurs, the shareholders of Qianzhuang bear unlimited risk liability. Therefore, the credit of Qianzhuang to the depositors does not depend on the amount of equity, but on the abundance degree of shareholders and family background, as well as on the operation of property.

In most cases, when Qianzhuang is liquidated at risk, it is not insolvency that results in the loss of the depositor's capital, but repayment by shareholders. In this regard, Qianzhuang can be regarded as a model of traditional business circles, plenty of shareholders., after a year or two of closure, still insist on paying Qianzhuang's debts. As long as there is still a little possibility, they will never lose Qianzhuang's credit to depositors.

The shareholders of Qianzhuang bear unlimited liabilities for the debts of Qianzhuang. That is to say, if there is a problem in the operation of Qianzhuang, the debts of Qianzhuang will be distributed by the shareholders according to their shares, and the shareholders will be fully responsible for the debts. If there is a problem in Qianzhuang, the shareholders will pay immediately. In this way, the credit of Qianzhuang is mainly guaranteed by the credit of the shareholders, not by the amount of equity invested by the shareholders. Therefore, judging the strength and credibility of a Qianzhuang in society does not only depend on its total equity, but also on the whole family and personal credit of its shareholders. The stronger the financial resources of shareholders and the more prominent their reputation in the business world, the stronger their banking power will be.

“Therefore, the establishment of Qianzhuang reputation does not depend entirely on the amount of capital, but mainly on: a. all the property credit of shareholders, that also is the credit of Qianzhuang, b. when shareholders invest in Qianzhuang, there must be a considerable amount of deposits in Qianzhuang⁴.

The more powerful capitalists in the society, besides Qianzhuang they invest in, choose another Qianzhuang with good reputation at the end of March or September of the Old Calendar to deposit in a six-month fixed deposit with a slightly lower interest rate than the general deposit, which is called “inner plate”. In this way, shareholders have a considerable amount of time deposits in different Qianzhuang, which are spread among Qianzhuang, and gradually form the image of a solid capitalist. In addition, in order to improve the reputation and expand the reputation, “the prestigious relatives and friends can

³ Shanghai Branch of the People's Bank of China. Historical materials of Shanghai Qianzhuang. Shanghai People's Publishing House, 1978, 152. "Shareholders bear unlimited responsibility and pay in advance as soon as necessary. Capital is limited, but responsibility is infinite.

⁴ Shanghai Branch of the People's Bank of China. Historical materials of Shanghai Qianzhuang. Shanghai People's Publishing House, 1978, 460

raise money for listing on the first day. In the money market, they can open up large amounts of loans to show that they have sufficient capital and are flexible in hand⁵. This greatly increases the depositor's confidence in Qianzhuang, greatly reduces the risk of runs and eliminates instability.

4. THE EFFECTIVENESS OF RISK CONTROL MECHANISM OF QIANZHUANG

4.1 Reliability and Rationality of Personnel System

a. Supervision of managers. Managers have great responsibilities and centralized power. If this is the case, then there must be a corresponding system to check and balance managers. There are two ways for Shanghai Qianzhuang to do this. One is to actively restrain the behavior. That is to set up positions for supervision within Qianzhuang on the basis of expressing trust in managers, so as to supervise and balance the managers. Second, negative restraint behavior, that is some restraint effect which existing as some customs in the Money Industry Association on managers.

The year-end closing system is one of them. Every new business year, shareholders are free to decide whether to withdraw their shares before opening. In fact, this is somewhat similar to the modern corporate system of "voting with feet" approach, in order to restrain the behavior of managers. In addition, in order to make managers loyal, shareholders also let managers participate in dividend distribution or public investment as incentives, so that the Qianzhuang manager's interests and shareholders' interests are linked together.

b. Manager's robustness. Typical example is Qin Runqing⁶, a tumbler in Shanghai's money industry. Qin Runqing, a native of Ningbo, Zhejiang Province, was an apprentice in Shanghai Qianzhuang since he was a teenager, and then the manager (or supervisor) of a wealthy Suzhou man's Qianzhuang. He has made four Qianzhuang top in Shanghai's money industry, and he has also become the head of Shanghai's money industry. He has served as the chairman of Shanghai Money Industry Association for consecutive 15 years.

In the past decades when he serves as the chairman, the money industry in Shanghai has experienced five or six large-scale financial upsurges, including the rubber storm (1910), the 1911 Revolution (1911), the Xinjiao storm (1921), the scrapping of silver to yuan (1931). In

the case of a large number of Qianzhuang being dragged down by bad debts, Qin's four Qianzhuang have survived from all those upsurges, and after the upsurge, Qin's banking business was even stronger.

For Qin Runqing's professional experience, the first is to be steady. The key to stability is prudence. To begin with, there are roughly several levels: first, for each loan, they must carefully check the ability and morality of shareholders and managers of lenders, check their personal privacy, and their credit, and then have a comprehensive understanding of the operation of the business, the use of loans, and the quality of the market. Therefore, when he ran the street in Qianzhuang, he didn't let a bill go back.

Secondly, the overall structure of lending should be decentralized and the eggs are not put in one basket. Thirdly, the overall scale of lending should not be greedily concerned. That is to say, always keep the balance of money within means, so that not to borrow from other Qianzhuang, let alone borrow funds from other banks, so as to avoid checks and balances from other financial institutions. Fourthly, the type of lending should not be speculative businesses, should not be tempted by high interest rates, or not engage in high-risk loans. However, for well-targeted business projects, to boldly lend money, regardless of short-term risks, and achieve win-win long-term cooperation.

The above lending principles have greatly reduced the risk of loans, and thus Qin Runqing's Qianzhuang passed smoothly in the turbulence of financial turmoil. It is generally understood that businessmen are greedy, but in fact, businessmen have their own ways. In Historical Records, it is said that, greedy businessmen have high profits and can recover their principal in three years. Businessmen who are not greedy avoid risks and make lower profits, so it takes five years to recover costs. The development of honest businessmen is slow but steady. Especially for the financial industry, the risk is high, and it is easy to spread or be affected by others.

It should be pointed out that the stability of managers is not only a policy and strategy of risk control, but also the moral faith of managers to shareholders. In the traditional banking industry, the identity stock system is generally implemented, that is a typical Chinese style. Identity stock is a Profit Dividend system. When Qianzhuang makes profits, the manager can share the dividend. When Qianzhuang loses money, especially when it is liquidated, all the debt losses are borne by the shareholders. Qianzhuang is typically highly indebted, with a capital-to-debt ratio of tens of times. In case of a run, shareholders are required to compensate with their own lives. When the debt reversal occurs, the debts can not be repaid (for Qianzhuang the goal of debt recovery is scattered, and those debtors may indeed be no money), but depositors of Qianzhuang would hardly push Qianzhuang (for depositors the goal of debt recovery is obvious

⁵ Liu Meiyong, Research on the Internal Control System and Control Mechanism of Shanghai Qianzhuang, Business Research, No. 409, 2011/05

⁶ Sun Shangen, Zhou Xiaosheng: Collection of Qin Runqing's Historical Materials, Tianjin Ancient Books Publishing House, 2009

and concentrated), together with the support of the government, a wealthy family shareholder, within several days, may ruin all fortune and become a street beggar.

Therefore, the management of managers is to take the lives of shareholders in the game, the responsibility is heavy, naturally there is a high sense of moral responsibility. Lending is the source of the risk of the bank. As the loan is steady and the risk is greatly reduced, the key to the risk control of the bank is grasped.

c. Personnel selection system. Qianzhuang has a strong family style about personnel arrangement. The selection of shareholders, managers and even apprentices is based on the tradition of "consanguinity, kinship, geographic and professional affinity", which we call "pan-family" relationship network. It is precisely because of this family-like personnel mechanism, so that Qianzhuang with less rigorous internal control system have reduced the occurrence of internal risks.

For example, if managers are not personally held by shareholders, they are mostly selected from the three-year-old Qianzhuang apprentices or other employees, and most of them have "pan-family" relationships with shareholders. There is also a strong pan-family tendency in the appointment of other positions in Qianzhuang, such as recruiting apprentices, introducing relatives and friends, training exchange students, etc. Through this family personnel system, the bankers are not only doing a job, but also standing for the family.

4.2 Prudence in Qianzhuang's Banking Business

a. Do not arbitrarily expand the scale of deposits. The deposit of Qianzhuang is the main source of Qianzhuang's fund operation, which roughly includes personal deposit and current deposit. For personal savings, the shareholders generally have to deposit a large sum of money in Qianzhuang for the purpose of operation. For other deposits, depositors and managers have personal relationships to some extent. Current deposits, in fact, are deposits of business people. Businessmen borrow money from Qianzhuang and deposit money in Qianzhuang when they have surplus funds.

It is worth noting that Qianzhuang do not accept deposits at will, nor do they expand deposits at will like modern western banks. First, do not accept deposits from strangers, but only deposits from acquaintances. First, they are afraid of unknown origin, such as stolen money; second, acquaintances will not withdraw their savings at will, resulting in Qianzhuang's shortfall. When there are rumors on the market, it is also easy to work with depositors and not easy to run. Second, they are unwilling to expand their deposits at will because they are afraid of imposing additional burdens on shareholders. Because when faced with a possible run, shareholders have to pay in advance first, and when closing down, shareholders have to pay cash to depositors. If the deposit plate is large, the scale of lending is large, and the amount of risk of

external backing is large, the shareholders may not be able to compensate for the loss of property.

b. Strict regulations on negotiable instruments. For example, when Shunkang Qianzhuang receives Hongsheng Qianzhuang's bill, the first thing to do is to send the old secretary or apprentice to Hongsheng Qianzhuang to check the bill. When delivering tickets, he holds a bill return book, which indicates the number of bills. After checking by the important staff of Hongsheng Qianzhuang, he confirms that there is no problem with the ticket. In order to prove this, Hongsheng Qianzhuang stamps on the left or right corner of the ticket. Once a ticket has been passed, the issuer must cash it when it matures.

"The relationship between Qianzhuang is very credible. Whoever holds Qianzhuang's note is regarded as cash."⁷ That is to say, the cashing of Qianzhuang's bill is a "promissory non-recognizer". However, in 1906, the regulations of the North and South city money industry reorganization stipulated that when Qianzhuang tickets expired, if people who did not know came to cash, they would not pay until 12:00 p.m. in accordance with the general rules of the money market. If the bill is discounted as an unexpired one, all of them need to be carefully identified."

Reporting loss then stopping payment. In fact, there may be tickets loss, because of theft and so on. If Qianzhuang pays the bill at sight, it will cause losses to the customers. But if Qianzhuang stop paying with no conclusive fact, it will easily cause losses to the credit of Qianzhuang. Therefore, Qianzhuang has made detailed provisions on the situation of suspension of payment of tickets by reporting the loss of tickets. "when the dealer come to Qianzhuang with the intention to ask for suspension of payment by reporting loss, if the ticket has been paid, or has been used to buy goods, or has been discounted, and there are accounts to be recorded, and goods to be pointed out, then we can be sure that ticket entries into others' hands, or is stolen by self-theft, or there are other situations, no matter when, Qianzhuang shall not agree to any suspension of payment by reporting the loss of the ticket."⁸

If the ticket is truly lost because of theft, water or fire, the person who losses the ticket must issue a certificate, apply to Qianzhuang for suspension of payment of loss, and declare in the famous newspapers at home and abroad that the ticket is invalid, at the same time, report to the local government, so as to suspend payment temporarily. And the money is immediately sent to the guild for safekeeping, after 100 days, if there is no dispute, the loser can find a solid guarantor, or a solid firm name, issue

⁷ "Shanghai Money Business Rules" (revised in January 1920), upscale S174-1-11. Article 13, paragraph B.

⁸ Pan Liangui, *The History of Shanghai Money* (Second Edition), Shanghai People's Publishing House, 2015.

a guarantee, and then the loser would get the payment; if it is found that there are other disputes, the request of suspension of payment is not valid.

5. THE PREVENTIVE FUNCTION OF MONEY INDUSTRY ASSOCIATION ON INTER-INDUSTRY FINANCIAL RISKS

Financial risk has strong inter-industry transmission, like infectious diseases. Therefore, for Qianzhuang, many risks may come from the inter-industry. Therefore, there is a strong demand for mutual assistance and internal self-discipline in the banking industry, and the Money Industry Association is such an organization for mutual assistance and self-discipline in the banking industry. In traditional Chinese society, the number of Qianzhuang is more than ten even in an ordinary city, there usually exists Money Industry Association within the scope of the city. The Money Industry Association can be regarded as a special organization to guard against industry-specific financial risks. The purpose of the establishment of the Money Industry Association is to strengthen management, seek the security of financial circulation and transactions, safeguard the interests of the money industry and promote the development of the money industry.

5.1 Setting up Barriers to Entry to Prevent Vicious Competition

a. The Money Industry Association has the right to set qualifications for entry into the industry. The strength of Shanghai Money Industry Association is the strongest. As early as the Qianlong Dynasty, the Money Industry Association of Shanghai was established. There are two main reasons why the Money Industry Association has the power to set qualifications for entry into the industry:

The first is the “public facilities” function of the Money Industry Association, including the interbank remittance function and the interbank lending market. If the new entries can not become members of the guild, they will naturally be shielded from the exchange and lending markets of the money industry. It is difficult for them to start business, or they can only become small Qianzhuang. In addition, members of the association have high social credit, easy access to deposits, and easy access to customers. In a word, it is difficult to carry out business without joining the association.

The second is the support of local governments. Because the money industry deeply involves in the local financial stability, local governments cannot ignore it. Therefore, in the late Qing Dynasty, local governments often required to submit applications for the establishment of Qianzhuang. The function of examination is handed over to the Money Industry Association. With the support of the government, the guild naturally has real power. In some small towns, there are few Qianzhuang and no

association, so the relevant functions can only be assumed by the government. However, because the government does not understand the actual situation, the effect of the review is greatly reduced.

b. The direct procedure for setting entry threshold by the guild is peer recommendation and qualification examination of applicants. Its main focus is two considerations: first, whether the shareholders are well-educated, whether they have the ability to assume unlimited risk liability; and, how about ethics and qualifications of managers they appoint. According to such censorship standards, it is naturally easy to screen out abusers and even some speculative fraudsters. In historical materials, we can see that in some small towns without money guilds, there are sometimes fraudsters who run Qianzhuang, absorb enough savings and then roll up the money to escape.

Second is to consider the supply and demand situation of the industry and not allow the number of members to expand too much, leading to serious vicious competition within the inter-industry. One of the major reasons for the inadvertent operation of the money industry is vicious competition. In Shanghai’s money industry, we can see that the riskier means of operation are often used by newly established Qianzhuang, who are eager to stand on their feet. Imagine that if the industry is too crowded, or even leading to vicious competition, it will be even more inevitable that there will be speculative risk-taking in the whole industry, and ultimately bring significant risks to the whole industry.⁹

5.2 Establish Intra-City Remittance and Lending Markets to Finance Each Other

Interbank remittance is originally used to support banknotes issued by Qianzhuang. But it differs from modern banknotes in which its credit does not come from the credit of state power, but from the function of convertible metal coins (silver). It not only saves the amount of money in circulation, but also facilitates the cross-regional trade of businessmen.

However, due to the lack of local Qianzhuang semicolons. Therefore, the convenient way of circulation is to admit and accept the banknotes of other Qianzhuang in different places or in the same city. In this way, there must be a place for exchange and debit. The Shanghai Money Industry Association has long invented this kind of exchange system, which makes the bill play its scale effect, which is equivalent to expanding the operating funds of Qianzhuang, similar to the so-called monetary multiplier effect of commercial banks in modern banking science.

As a result of the transfer and rolling of accounts,

⁹ There are many similar cases all over the country. See *Modern Chinese Economic History (1927-1937)*, edited by Liu Kexiang and Wu Taichang, 2010 edition, P1996-1997.

there must be imbalances in expenditures, some need to pay the cash, and some need to recover the cash. When a Qianzhuang's existing cash is insufficient to pay its arrears, it naturally requires short-term borrowing. So, the guild set up the interbank lending market and provide adjustment. This enables the banks to obtain the buffer space of insufficient money through the lending market, which naturally plays a very convenient role in the daily operation of Qianzhuang.

5.3 Establish Internal Rules to Prevent Risk Behaviors of Some Qianzhuang From Endangering Group Interests

With the power of managing the inter-industry, it is natural to specify internal competition rules and uniform business ethics. For example, in terms of deposit and loan, the most common provision is the agreement on deposit and loan interest rates, which can greatly prevent vicious competition among the industry. Where there is no money guild, it is easy to compete among Qianzhuang, or among Qianzhuang gangs, to hold high interest rates and to lend at low interest rates, which leads to uncontrolled competition and financial risks in the whole industry.

At the same time, the Money Industry Association has also formulated numerous norms. Some are moral advice, others are rules, and once violated, severe sanctions will be imposed. For example, the Shanghai Money Industry Association, which has the most stringent rules, once stipulated that the associates of the members of the association should not participate in the brokerage of the credit exchange or in the trading of stocks, and once found out, those who participate should be severely punished. This is mainly aimed at preventing the prevailing speculation on the Shanghai Credit Exchange in the 1920s (the credit tide) from causing great harm to Qianzhuang.

CONCLUSION

Credit loans are implemented by Qianzhuang in order to meet the objective needs of local businesses. When lending, Qianzhuang pay great attention to credit investigation, relying on the geographic relationship and personal contacts with the merchants to ensure the accuracy of the survey information, and the whole business circle also cherishes commercial credit. These factors make the risk of credit loans controllable. For the risk of runs, Qianzhuang take precautions through daily balance of revenue and expenditure, cross-bank dismantling and unlimited risk liability of shareholders.

In the whole Qianzhuang system, managers act very steadily. Qin Runqing is a typical representative. This is not only a policy of risk control, but also the moral faith of managers to shareholders. When banks absorb deposits, they strive for the stability of depositors and never expand at will. These two points strongly guarantee the effectiveness of the risk control mechanism of the banking

industry.

At the same time, the risk of the financial industry has a strong inter-industry transmission. As an organization of mutual assistance and self-discipline within the Qianzhuang industry, the Money Industry Association specially guards against the industrial risk. The Money Industry Association shall set barriers to entry, prevent vicious competition and shield potential harmful ones out of the industry; set up inter-city remittance and lending markets to accommodate funds; and formulate internal plans to prevent someone's risk behaviors from endangering the interests of groups.

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