*Bank i Kredyt 57(3), 2026, 325-348*
*DOI: 10.5604/01.3001.0055.7780*

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# The impact of Chinese history on shaping monetary policy: a special case of the People's Bank of China

Paweł Kowalewski*

Submitted: 4 February 2026. Accepted: 8 April 2026.

**Suggested citation:** Kowalewski P. (2026), The impact of Chinese history on shaping monetary policy: a special case of the People's Bank of China, *Bank i Kredyt*, 57(3), 325–348, DOI: 10.5604/01.3001.0055.7780.

## Abstract

In July 2024, the People's Bank of China (PBoC) Governor Pan Gongsheng announced the intention of moving towards a worldwide recognized system of targeting a short term interest rate, by promoting the 7-day reverse repo rate as the reference rate, thus moving away from previous efforts targeting longer tenors. In spite of this announcement, the PBoC still remains far from an internationally prevailing formula for its pursued policies. This state of affairs has not impeded the PBoC in the last twenty years to show the ability to adjust its operational framework to trends prevailing in the international monetary system. This adaptiveness was often accomplished by questioning classical monetary policies' conventions and building on experience from China's past. In this text we shall try to assess reasons behind this unique PBoC policy mix by describing the sources of inspiration for its current policies.

**Keywords:** economy, interest rate, liquidity, People's Bank of China, involution

**JEL:** E50, E58, F31, N15, P40

* Narodowy Bank Polski, Market Operations Department; e-mail: pawel.kowalewski@nbp.pl.

## 1. Introduction

The People's Republic of China (PRoC) has received a lot of credit for its achievement in reducing poverty across the board and preserving economic expansion on a sustainable basis. Still, with some notable exceptions (Bolton, Huang 2024), there has been relatively little detailed debate about the PBoC's role in this unprecedent achievement. This text is aimed to fill this void by presenting the PBoC adaptiveness to changes in the world economy.

The way the PBoC operates and subsequently fulfils its mission may surprise many observers around the world. The aforementioned mission forms a sort of an amalgamate of different aims, which often goes beyond preserving low inflation. These aims range from preserving stable exchange rates to putting enormous emphasis on structural policies (addressed toward the real sector of the domestic economy). As a result, the PBoC is a unique central bank, making it impossible to find any point of reference worldwide.

This paper will try, among other things, to present the reasons behind this state of affairs. With its 1.4 billion inhabitants, it may be questionable to expect China to follow the patterns of other major economies in the area of monetary policies. Hence, China has been opting to pursue its own policies, which does not mean that its authorities remain indifferent to events taking place elsewhere. The latter may be an important point of reference for Beijing but in order to be included in the domestic policy mix, they must be checked beforehand for matching the so-called domestic uniqueness of China's own economy. After all, the Chinese authorities define their own policies as socialism with Chinese characteristics. Embracing the latter seems to be essential from the point of view of understanding Chinese policies. This is important, especially when comparing to all those economies which experimented with socialist policies and failed badly as a result.

From the point of view of understanding China's uniqueness, it may be helpful to address yet again the so-called Needham's question. After all, China was most probably the first country ever to experiment with paper money. Still, this was not conducive for this country to deliver anything resembling a central bank in the Western meaning of the word. In other words, it did not come to pass until the early 20$^{th}$ century with the creation of the so called Hubu bank in 1905, when the first embryo of a central bank was brought to life. However, neither the late Qing dynasty's effort, nor all the attempts dating from the Republican era (1912–1949) prepared the ground for the fiat money's economy. After all, the Central Bank of China, created by Sun Yat-sen in 1923 following a period of brief monetary stability, lost its control over money supply and subsequently paved way to painful hyperinflation.

It was not until the creation of People's Republic of China that the country experienced durable price stability (although in the first three decades it was achieved through tough administrative measures in a rather autarkic environment), with inflation never surpassing the threshold of 30% for prolonged periods. Even if the PBoC was created 10 months ahead of the PRoC, it had to go a long way before it started to enjoy prerogatives vaguely comparable to similar institutions around the world. Like in many other centrally planned economies, the PBoC used to sit under the shadow of the Ministry of Finance. It was not until the advent of Deng Xiaoping that the long transition of the PBoC into a modern central bank had started (under a supervision of Zhu Rongji). This was a long process. Almost a quarter of a century passed before Zhou Xiaochuan' tenure, who during his three terms in office (lasting from 2003 to 2018) contributed enormously to building the PBoC's reputation and converted it

into a strength to reckon with. The ability to adjust its operational policies proved to be essential from the point of view of meeting its objectives.

During Zhou's tenure, the PBOC went through various transitions, of which we believe one merits special mention: the shift of the money creation factor from externally driven to internally driven. This transition along with the current efforts to combat deflation provide for the backbone of this article. The above mentioned transition is denominated by us as the Great Switch (GS). While the GS seems to have been accomplished, the issue of overcoming deflationary pressures poses a great challenge to the Chinese monetary authorities. In the wake of this challenge, it seems that the decision makers seem yet again to fall back on domestic idiosyncrasy, with their policies aimed to counter the involution (nei-juan) being the best example of such attitude.

In order to preserve due balance, we will refer to literature coming from both the Chinese economists as well as renowned international experts specializing in China. The present text is divided into three main parts. The first part focuses on the peculiarities of the Chinese approach deeply rooted in China's complex history, which makes the PBoC follow idiosyncratic policies. The second one focuses on the aforementioned GS, the third one addresses both the current and the forthcoming challenges that the PBoC has to confront. This is followed by a summary and conclusions.

## 2. The impact of cultural heritage on the economic and monetary policymaking

Misconception seems to be the key world in describing the Western skewed perception of China and its history. As a result, our ability to judge the achievements of the Chinese civilization is disturbed, biased and, consequently, it misses the mark. The tradition of the aforementioned misconceptions is deeply rooted in history, as Western countries searched for a justification of their rather hostile and aggressive attitude towards China across centuries.

Much of the damage to the Western perception of China was caused by Johann Herder and Georg Hegel, among others, but it was probably the American historian of German origin, Karl August Wittfogel, whose works really exerted a negative impact on the Western perception of China. Wittfogel coined two terms, namely 'oriental despotism' and 'hydraulic society', which cast a long shadow on the way Chinese society has been perceived ever since (Spengler 1977).

It was only Joseph Needham who tried to undo the damage caused by preceding European scholars and subsequently to eliminate a deeply rooted bias towards China. In spite of extremely versatile interests, however, Needham did not specialize in economy. Science and, above all, technology were closer to Needham's heart. Still, his works offer many interesting insights, which prove useful in understanding the impact of Chinese heritage on the way the PRoC used to manage its economy.

Needham resorted in his research to the aforementioned concept by Wittfogel but fiercely disputed its meaning. If Wittfogel perceived the hydraulic society as a factor which paved way to oriental despotism, Needham had a totally distinct vision of this kind of society. He emphasized the importance of amelioration, without which a development of civilization in China would simply have not been possible.

The huge continental area needed a well-developed administration, which was formed of bureaucrats. Rice cannot be grown on an individual basis; it can be grown by collective effort only.

The society was at the mercy of bureaucrats, who were nominated only after successfully passing civil service examinations. The key feature of such a society was that the bureaucratic title was not hereditary. As a result, each generation of a given family had to try from the scratch to obtain the title of its ancestors. This was one of the reasons why accumulation of capital failed to take place. The demand for knowledge used to outperform the hunger for material wealth.

Sticking to the geographical location, China did not resemble peninsular Europe with its multiple islands. As a result, incentives for navigations were smaller thus giving commerce less room to rise to relevance than in Europe. Needham believed that a poorly developed fleet in China stemmed from yet another peculiarity of this society, namely it did not have a tendency to command because it preferred persuasion to subordination. Furthermore, it has had a strong bias towards organic order supported by harmony. With this kind of attitude neither navigation nor even farming were the preferred professions. It was the land's tillage (cultivation), which was able to ensure the aforementioned full harmony with nature. This issue, along with Confucian principles, is well highlighted by Rudyak (2025). All that made Chinese people more inclined to gravitate towards bureaucratic feudalism.

Sticking to bureaucrats and literati, their ability to exert influence on the domestic society was far greater than the army's. The sword used to be the ultimate solution but usually gave way to the art of persuasion. Under such circumstances, the rulers were not inclined to launch costly military adventures as their counterparts in other parts of the world. And it cannot be forgotten that one of the key reasons for establishing central banks in Europe was to accumulate funds aimed to cover war expenses.

Focusing on wealth, everything in China was in the hands of the emperor. That is why the rule of one person over the rest of society has been nothing new. Furthermore, this state of affairs, along with special reverence for knowledge, helped Chinese rulers to eschew the European scenario where certain layers of society accrued an enormous amount of capital, often surpassing the rulers in this particular respect. Avoiding the European scenario was possible mainly thanks to missing incentives for commerce. As a result, bureaucratic feudalism was unable to undergo the transition to mercantilism (not to mention industrial capitalism).

While in Europe rulers found themselves quickly (as early as the 16$^{th}$ century) at the mercy of either the wealthy aristocracy or the emerging merchant class, this kind of dependency was out of the question in China. With rulers preserving their uniquely privileged position, there were no incentives for the creation of the debt market – a process which started to flourish in the 17$^{th}$ century Netherlands. And the non-existence of the debt market was one more reason which inhibited any early shift towards the creation of central banking in China.

Last but not least, the lack of strong commerce (stimulated by navigation, amongst others) excluded the emergence of the so-called city states in China (to the likeness of Venice, for example, or even Amsterdam). This kind of cities formed a cradle for the banking system in Europe, and in the case of Amsterdam the commerce (and the subsequent chaos related to the settlement of transactions) paved way to the origin of the Wisselbank, which is widely regarded as a prototype of the central bank.

The aforementioned processes were often abrupt and stimulating. In contrast to Europe, China seemed to avoid abrupt changes, thus making some experts believe in its propensity towards stagnation. But this term does not reflect the processes taking place in China well enough, if at all. The notion of homeostasis seems to illustrate the Chinese attitude toward progress better (Needham 1977).

Little has changed across the centuries. But as Xu (2021) points out, a central government without the means to obtain credit issuing a fiduciary currency can only bring the ruin of the empire. The Chinese economist from the Republican era, Zhao Lanping, once said that throughout the ages

China had had currency but no currency system. As a result, China was poorly equipped to face a brutal confrontation with the West, which inflicted huge losses and economic pain on the country (the so--called century of humiliation). This kind of outcome should not be surprising. The Beiyang government was quick to recognize as early as 1914 that China's greatest illness was the lack of a currency standard. A similar tune echoes in Yan Hanzhong's opinion, according to which in the period stretching from the late Qing to the Republican era, China had had no currency standard because of monetary chaos with no precedent in history.

As late as 1933, Herber Bratter from the US Department of Commerce described the Chinese monetary system in the following way: "China's currency system is complicated, and may best be described without making detailed reference to the numerous coinage laws promulgated since the overthrow of the Empire in 1911 or to the various local currencies. While the greater part of China's small business is conducted with copper as the medium of exchange, the country's principal currency metal is silver, which may be said to be the standard of value. In certain sections silver circulates principally in the form of yuan coins, while in others, bullion in the form of 'shoes' of sycee comprises the main medium of exchange in large-size business transactions. Bank notes secured by silver are extensively used in the larger cities. It may be said that practically throughout China, silver in almost any form is money. In this sense China can be said to have free coinage." (Bratter 1933).

In the middle of the aforementioned century of humiliation, there was a scramble to catch up in the area of monetary sovereignty. Liang Qichao, widely considered the Chinese Newton, was one of the forerunners of this movement. The future director general of the Tianjin mint and the minister of finance in 1917, Liang perceived sound currency as financial lifeblood. Most probably because of Liang's efforts, the creation of the Hubu bank (known also as Da-Qing Bank) in 1905 took place. According to Xu (2021), the bank was to aggregate the flow of wealth and currency. It enjoyed the privileges of acting as agent of the State Treasury, managing public debt, issuing bank notes, and minting and issuing national currency. But it was not until 1923 that steps were taken under the auspices of Sun Yat Sen to create the Central Bank of the Republic of China. Established in Guangzhou a year later, it was only on 1 November 1928 that it formally started its operations in Shanghai. Its opening was preceded by the promulgation of the Statute of the Central Bank of China. Following the revision of the latter, the Central Bank of the Republic of China Act was enacted on 23 May 1935.[1]

Efforts aimed to regain monetary sovereignty during the Republican era deserve some credit for establishing temporarily monetary order. Perhaps the most important date is 8 March 1933, when the Nationalist Government announced the Silver Standard Currency Minting Ordinance which linked the yuan to the silver. Nevertheless, a combination of a rather still fragile domestic bank along with foreign adversities resulted in all these efforts paving way to hyperinflation.

This brief overview allows for a smooth transition to the history of the establishment of the People's Bank of China. It was founded on 1 December 1948 as a result of the consolidation of three banks, namely Huabei Bank, the Beihai Bank and Xibei (Northwestern) Farmer Bank. Initially staying in the shadow of the Ministry of Finance, it was not until 17 September 1983 that the State Council took the decision (with effect from 1 January 1984) as a result of which the PBoC was to assume the role of the central bank.

[1] Central Bank of the Republic of China (Taiwan), Frequently asked questions, https://www.cbc.gov.tw/en/cp-2168-29911-D80A0-2.html#:~:text=On%20February%2021%2C%201923%2C%20Dr.%20Sun%20Yat%2Dsen%2C,of%20China%20Act%20on%20May%2023%2C%201935.

The beginnings for the PBoC in its capacity of a central bank were not easy. In the first decade (1984–1994), inflation got out of control twice (in the late eighties it reached levels close to 20% and five years later it approached almost 25%) and the renminbi was frequently devalued. The turn of the 1980s and 1990s proved to be a challenge for China as the majority of central planning economies collapsed worldwide. Under these circumstances, Deng Xiaoping made his Southern Tour (between 18 January and 21 February 1992), which is considered the turning point in modern Chinese history (Zhang, Chen 2023). For Deng it was clear that the country must embrace a new economic course. This implied, among other things, preserving the economic balance with the help of fiscal and monetary policies. An instrumental figure in this process turned out to be Zhu Rongji, who in the period from July 1993 to the end of June 1995 became the PBoC Governor (being at the same time deputy prime minister). It was during his tenure that the corruption-prone two-tier exchange rate was lifted. That is why yet another (but final) devaluation took place on 1 January 1994, contributing to the introduction of the unified exchange rate, which was set at approximately RMB 8.72 (from the previous level of RMB 5.82). And in order to keep public finances under control, Zhu resorted to the so-called Tanpai System (which goes back to the times of the Ming dynasty), as a result of which public officials were obliged to purchase certain amount of government bonds (Sieren 2013).

Such a sharp adjustment in the value of renminbi did not cause inflation pressure. One of the reasons behind it could be the Great Moderation effect. Furthermore, as Zhang and Chen (2023) point out, the degree of the adjustment was so large that it made the market believe that there would be no further depreciations. As a result of the aforementioned adjustment, China's current account surpluses continued to widen, thus creating continuous appreciation expectations. And indeed, by early March 1995, the renminbi reversed some of its losses, with the USD/RMB reaching levels below RMB 8.30. The robustness of the renminbi helped to lower (and stabilize) inflation expectations, which had been building in response to the inflation outbreaks of the late 1980s and early 1990s (Geiger, Pennings 2021).

In order to continue the momentum, changes of structural nature took place. In March 1995, the People's Bank of China Law was implemented, enshrining the PBoC's central bank mandate into law. Even if the decision made the PBoC more independent, still only two out of seven available monetary instruments did not require the consent of the State Council (Geiger, Pennings 2021). This was yet another evidence that China opted for solutions suiting its own vision.

In December 1996, China's integration into the global financial system was further deepened as China accepted obligations stemming from the IMF's Article VIII. Shortly afterwards China gained respect worldwide for its performance during the East Asia crisis. At a certain point in the second half of 1997, the sequence of events in East Asia started to resemble Beggar Thy Neighbour policies, even generating some associations with the Great Depression from the early 1930s. Only the commitment of the PBoC to its exchange rate peg helped avoid disaster. The price of this commitment was high as the bank had to face an economic slowdown in the deflationary environment. In spite of this, the PBoC remained steadfast and as sign of recognition, the world community let China join the WTO in late 2001.

In 2003, regulatory functions were detached from the central bank, as the government transferred them to China Banking Regulatory Commission (Bolton, Huang 2024). This step was preceded by efforts to commercialize banks. All these measures were aimed at improving better credit distribution. The latter was indispensable in order to halt the accumulation of non-performing debt.

In the period under review, inflation and economic growth were perceived as ultimate objectives (Xie 2004). From 1998 onward, China started to experience surpluses on both current and capital

accounts – a sort of combination which paved way to a rapid increase in FX reserves. With the PBoC having several instruments at its disposal (for example, the required reserve ratio, the rediscount window, central bank interest rates, central bank lending, open market operations on Treasury bonds, policy financial bonds and central bank bills), the last three proved instrumental in countering all the effects stemming from foreign exchange purchases (Xie 2004).

## 3. Evolution of the PBoC operational policies in the wake of GS

### 3.1. Years preceding the GS

If the East Asian crisis brought the increase in FX reserves almost to a halt, the advent of the new century heralded the beginning of drastic accumulation of these reserves. In the following six years (2001–2007) the Chinese FX reserves were almost doubling every two years. In 2006 China became the world largest holder of FX reserves. In 1993 these reserves amounted to a meagre USD 27.3 billion, thirty years later they increased to USD 3.88 trillion. While the increase in FX reserves posed a big challenge, the Chinese economy was to experience other events which highlighted the PBoC's ability to adapt to the changing environment. Those events ranged from moving gradually away from heavy industry and diminishing trade surpluses enhancing credit growth to consumption stimulating efforts. The formula of this text precludes the description of all these processes. Our attention will be focused on the PBoC's ability to respond to all these challenges by enhancing its operational toolkit.

The multiplicity of the aforementioned processes did not diminish the seriousness of all the consequences stemming from capital inflows. A number of measures were undertaken to mitigate the effect of an ever stronger growth in FX reserves. Only five years were needed to see the Chinese FX reserves double in the period stretching from early 1997 to late 200. As a result, a sharp fall in the level of interest rates was generated. If the rate on one-year loans to financial institutions amounted to almost 11% in early 1996, six years later it fell to less than 3.25%. The fall in the lending rate of commercial banks was less acute but large enough to cut it by more than half in the same timespan (from 11% to around 5.3%, respectively). The fall in the deposit rate of household savings was even more pronounced. By early 2002 they fell below 2% from levels well above 9% six years earlier (Xie 2004). Central bank interest on required rates experienced a similar fall (from 8.82% to less than 1.9%, respectively).

Such a trend in interest rates proved unable to deter investors from bringing in foreign capital, as China was attracting inflows with its economic growth potential. That is why extensive capital controls were most probably the key factor in the renminbi withstanding appreciation pressures. Another one was sterilization. While until the end of 1999 the PBoC was injecting liquidity, in 2000 (as a result of the aforementioned trends) absorption of liquidity started to prevail.

The ever stronger and continuous increase in FX reserves along with high economic growth started to raise voices demanding China to adjust its currency framework. The IMF in its Article IV consultations used the notion of exchange rate flexibility up to 42 times (IMF 2004). But the PBoC did not succumb to the pressure and opted to focus on internal issues, such as interest rate liberalization; a key decision was made on 29 October 2004, when the ceiling on loan interest rates was removed).

Such a speed of reserve accumulation had to affect money creation in China by definition. The increase in the M2 aggregate in early 2004 reached 19.4% and the monetary base rose in the whole 2004 by 12.6% (PBoC 2005a). As a result, the PBoC was quick to introduce special policies aimed to withdraw the excess of liquidity. By the end of 2003, the PBoC launched 63 issues of central bank bills alone, with a total issuance amount of RMB 722.68 billion, and the outstanding amount of RMB 337.68 billion (PBoC 2004). Just to embrace the size of monetary expansion, it makes sense to take a closer view at monetary features of the Chinese economy at that particular time. Those actions had an impact on the PBoC balance sheet. If in early 2002 foreign assets amounted to less than RMB 2 trillion, by late 2006 they surpassed RMB 8.57 trillion. As a result, the size of the balance sheet increased from RMB 4.53 trillion to approximately RMB 12.8 trillion, respectively.

Under the circumstance outlined above, the PBoC operational measures detailed at the end of the first part proved insufficient. That is why, after more than eleven years, China decided to tweak its exchange rate policy. In July 2005, the Chinese monetary authorities decided to revalue the rate of the renminbi by 2%. From then on, the PBoC opted for moving towards a managed floating exchange rate regime. As written in the *China Monetary Policy Report for Q3 2005* (PBoC 2005b), the expected outcome of the conducted reform was the following: "With the reform gradually taking effect, the new regime will serve to promote foreign trade structural adjustment, economic structural optimization, industrial upgrading, and sustainability of economic development. Meanwhile, it is worth noting that domestic demand may be more important in a large economy.".

The last sentence of the aforementioned paragraph is of paramount importance, as it can be treated as a prelude to the GS. However, the 2% appreciation along very slow crawling appreciation could only mitigate problems stemming from heavy capital inflows, not solve them.

In 2005 alone, outstanding RMB deposits of all financial institutions rose by 18.4%. As a result of tendencies of a similar kind, in 2006 the PBoC opted for a much quicker withdrawing of excessive liquidity from the banking system with the help of two instruments, namely the issuance of central bank bills and the ratio of reserve requirement. Between 2003 and 2006 approximately RMB 3 trillion were sterilized on a net basis. Another 1 trillion was withdrawn with the help of a smooth use of the Reserve Requirement Ratio (RRR). In 2006 alone, RMB 3.65 trillion worth of central bank bills were issued (an increase of 30% from a year before). During the same time period, between 5 July 2006 and 15 January 2007, the RRR ratio was raised on four occasions (PBoC 2007).

In 2007 this trend was continued with further increase in the volume of bills issued (the outstanding balance reaching RMB 3.49 trillion, while the volume of issue amounted to RMB 4.07 trillion). The PBoC also opted for relaunching 3-year central bank bills in order to enhance the freezing effect on liquidity. And the cumulative increase of the RRR amounted to 5.5 percentage points (PBoC 2008). The toolkit at the PBoC's disposal seemed to satisfy conditions aimed to preserve the monetary equilibrium in the economy. However, this state of affairs was soon to change.

The year 2008 proved to be a milestone for the PBoC because of internal and external developments. Both of them were unexpected. 2008 started with continued efforts aimed at preventing the economy from overheating. In the course of the year, however, two events changed the stance pursued thus far. They were the Wenchuan earthquake and the outbreak of the GFC. If the former was mitigated with the so-called structural policies, the latter implied far reaching changes to the PBoC operation toolkit. Both require a brief description.

Starting with the structural policies, the PBoC defines them as "monetary policy that channels fund flows to specific areas of the economy based on market-oriented resource allocation through an

appropriate incentive mechanism". Structural monetary policy not only adjusts economic structure but is also accompanied by a carefully designed incentive-compatible mechanism to link the incentive funds of the PBoC with targeted credit support to specific areas by financial institutions, thereby delivering targeted and direct support. In addition, structural monetary policy also impacts monetary aggregates through the injection of base money to maintain banking liquidity at a reasonable and adequate level and to support the steady growth of credit (BIS 2025). The PBoC resorts to this approach in response to the heterogeneity of the Chinese society, which can affect the efficiency of the monetary transmission mechanism. They reflect China's theoretical and empirical experiences in addressing the challenges of the aforementioned heterogeneity. And bearing in mind that these policies put heavy emphasis on targeting the 'three rural issues' (agriculture, rural areas, and farmers) as key areas for financial support, their origin can be sought in history (BIS 2025). After all, rice cultivation always played a fundamental role in the Chinese economy and reflected the Chinese concept of harmony (Needham 1977). In the case of the Wenchuan disaster, with the help of these policies the PBoC managed to relax credit restrictions and encouraged domestic banks to support the affected areas.

Moving toward the GFC: it presented another opportunity for the PBoC to prove its adaptability in the changing environment. Its response was versatile, ranging from adjustments to the FX regime to changes in supervisory regulations. In order to mitigate the impact of the crisis on domestic growth, the M2 growth surged in 2009 to 27.7% YoY. Initially, the PBoC opted for adjusting the pace and frequency of OMOs. A total of RMB 4.3 trillion of central bank bills was issued in 2008, with the issuance in each quarter getting smaller and amounting to RMB 1.78 trillion, RMB 1.17 trillion, RMB 981 billion, and RMB 371 billion, respectively (PBoC 2009). These bills gave way to short-term repo operations, which amounted to RMB 3.3 trillion for the full year. Similar flexibility was shown in the case of the multi-tier RRRs, as a result of which the reserve requirement ratio of large financial institutions was cut by 2 percentage points cumulatively, whereas that of small financial institutions was cut by 4 percentage points cumulatively. By the end of 2008, according to trend calculations done by the PBoC, a total of RMB 800 billion of liquidity was released (PBoC 2009). Furthermore, the PBoC resorted to window guidance with the aim of letting bank exert a stabilising role when it came to adequate distribution of credit support and risk prevention. This role proved to be essential from the point of view of preventing banks from amplifying all the potential negative effects of excessive credit creation. However, there was a flip side to this development.

Apart from a monetary stimulus, there was also an announcement of a fiscal stimulus (totalling RMB 4 trillion), which helped the Chinese economy to be among the first countries to recover from the crisis. With the launch of unconventional (and thus expansionary) monetary policies in the world major economies, China with its rather prudent monetary stance became one of the favourite destinations for capital flows. In order to halt it, the PBoC froze the yuan's appreciation, as a result of which between early 2009 and mid-2010 it traded around 6.83 USD/RMB.[2]

Once the state of the domestic economy started to improve, the PBoC opted for undertaking further measures aimed to prepare it for the approaching GS. Its toolkit was getting more and more flexible. As stated in the *China Monetary Policy Report* (PBoC 2013): "Market-based interest rate reform advanced in strides. The ceiling of RMB deposit rates offered by financial institutions to their clients was adjusted to 1.1 times of the benchmark rates and the floor of the lending rates offered by financial institutions to their clients was adjusted to 0.7 times of the benchmark rates.".

[2] https://www.researchgate.net/figure/Net-capital-flows-of-China-have-only-just-stabilised-after-declines_fig3_335161147.

In the second half of 2012, the reverse repo operations became a standard tool with the help of which the PBoC was regularly injecting liquidity. Furthermore, on 16 April 2012, the PBoC widened its maximum allowable divergence of the renminbi from its central parity from +/-0.5% to +/- 1%. Less than two years later, on 17 March 2014, the aforementioned divergence was again increased to +/-2%. As a result, the PBoC seemed to be well prepared for the GS transition.

Such a heavy interference in the domestic economy had its side effects, whose presentation goes beyond the scope of this text. Generous support for the banks created a need to enhance banking regulations. And joining the Basel Committee on Banking Supervision in May 2009, the PBoC received further impetus to strengthen its oversight of supervised banks. This regulatory stance was one of the reasons behind the rapid increase in shadow banking (which started to emerge at the turn of the century) (PBoC 2010). However, the preceding optimistic assessment of the PBoC' role was challenged in the wake of the events of 20 June 2013, when a serious setback occurred. The PBoC was trying to reduce banks' reliance upon riskier funding channels, known as wealth management products (WMPs). Because China's deposit and lending rates were fixed within narrow ranges, banks could not compete for deposits based on offering higher interest rates (Wright 2023). By offering higher returns to investors, banks received new funding. However, once the demand for WMPs subsided, banks turned to the PBoC for support. The central bank's decision to withdraw its support caused the short term repo rate to reach nearly 30%. This credit crunch temporarily stalled the transition to the GS, yet it served as a powerful incentive to ultimately accelerate the process.

## 3.2. The GS and its different perceptions

Defining exactly both the beginning and the end of a certain process is challenging. We have already given our definition of the GS in this text. However, the same notion can be explained without resorting to economic parlance. The GS can be perceived through events which took place in a span of one year. The only problem is that such a perception is subject to various biases. In the Western press, 2015 used to be perceived as the year of slowest growth in 25 years, stock exchange turbulences and currency devaluation. This stood in stark contrast to the Chinese coverage of the same year.

As broaching the issue goes beyond this text, the attention will be focused on a few discrepancies only. Even if the renminbi movements were conspicuous in August 2015, they were nowhere near the movement of the Western currencies in the same year (and the first quarter in particular). Admittedly, the renminbi's exchange rate used to be tightly managed, in a sharp departure from Western currencies; nevertheless, these movements must be perceived through the lens of an unprecedented rise in the value of the US dollar (reflecting the beginning of a tightening process by the Fed). The fall (of 44%) on the stock exchange (measured in terms of the Shanghai Shenzen CSI 300 Index) was significant and at the time of its occurrence some experts feared that it could have posed a lethal threat to the Chinese economy. There were even voices pointing at similarities with what happened in Japan in the early 1990s. And the tragedy occurring in Tianjin on 12 August 2015 encouraged some voices to draw parallels between the two events and extend almost Cassandra-like visions.

The aforementioned falls – triggered to a large extent by excessive leverage and the subsequent leverage-induced fire sales (Bian et al. 2018) – definitely posed a challenge for the authorities. Some regulatory blunders (the details of which fall beyond the scope of this text) could and should have

been avoided. Nevertheless, the doomsday scenarios did not materialize, proving that the Chinese authorities maintained their grip over the economy, with the PBoC playing its part by cutting both the level of interest rates and the RRR and thus generating much needed liquidity. It is also worth noting that during roughly the same period, the more mature German Dax index lost almost 30%. And coming back to the renminbi again, it was announced in late 2015 that from October 2016 the Chinese currency would enter the SDR basket. Had the renminbi really been in poor shape because of turbulences in the domestic economy, such an announcement would never have been made.

The Western coverage was so focused on the events in question that it almost entirely overlooked an important announcement from May 2015, regarding the Made in China 2025 strategy (MIC2025), which was then unveiled for the first time. The GS is quite closely related to MIC2025, as the former was most probably conceived (and subsequently pursued) to support the latter. Furthermore, MIC2025 offered a perfect opportunity for the PBoC to enhance the use of its structural policies.

The circumstances under which the GS was accomplished were complex. One of the key reasons was a changing external environment, with the Federal Reserve abandoning its QE in 2014 and moving gradually towards the tightening, thus reducing capital inflows to emerging economies significantly. These falling inflows were soon converted in outflows. The renminbi's appreciating trend following its resumption in June 2010 came to an end in early 2014. And in the case of China, there were also some internal elements at stake, with the domestic economy facing downward pressures as the transition period was approaching. As consumption and services were becoming the main growth engines, some traditional enterprises were facing excess capacity. Furthermore, a new trend was emerging, namely a contraction of non-regulated interbank business. This trend engineered a decline in money supply.

The GS from the PBoC's perspective can be perceived through the lens of two processes running in the banking system. The first of them consisted in a further expansion of the PBoC's toolkit aimed at improving its ability to manage liquidity even better. The second involved the central bank's continuous efforts aimed at steering credit expansion more efficiently in order to foster the restructuring process in the domestic economy.

In terms of operational policies, the early stages of the GS were manifested by the change of attitude towards the RRR – a tool with the help of which the PBoC tried to preserve liquidity in the long term. As the PBoC admits, from September 2003 to June 2011, the PBoC raised the RRR 32 times, lifting the average RRR from 6% to 20.1%. Following the GS in 2013, the PBoC subsequently lowered the RRR 29 times, reducing the average RRR from 20.1% to 6.6%, out of which four universal and five targeted cuts took place in 2015 alone (PBoC 2025). However, the burden of liquidity adjustment started to shift from the RRR toward new monetary tools to be implemented in the period in question.

In order to enhance its toolkit, the PBoC introduced new instruments aimed to manage liquidity even better. Following the introduction of the Standing Lending Facility in early 2013, new instruments were added to the toolkit. In order to encourage credit action, the Loan Prime Rate (LPR) was launched in September 2013 with the intention of converting trends taking place in the money markets to the credit market (PBoC 2014). 2014 saw further expansion of the toolkit. Among the new instruments, special attention should be paid to Pledged Supplementary Lending (PSL), which was targeted to the so-called policy banks, thus confirming China's idiosyncrasy again. Policy banks had been conceived to achieve long term goals in these areas where profit-driven banks do not find sufficient incentive to enter. Even if similar banks exist elsewhere, the uniqueness of these Chinese banks consists in their size and consequently they play a more important role in the country's more state-directed economy

(Bloomberg 2022). It is a targeted lending program that influences directly the central bank's balance sheet (He et al. 2024). Apart from the PSL, the Medium-term Lending Facility (MLF) was designed to provide medium-term base money to commercial banks and policy banks meeting macro-prudential management requirements (PBoC 2015).

In the wake of ever changing supply and demand for liquidity in the banking system, the PBoC adopted a mix of policy instruments in 2016, the most significant of which was the launch of daily OMOs with the 7-day reverse repo operation becoming its main tool (PBoC 2017).[3] However, it was not until 2024 that the bank acknowledged this rate to be its reference rate. Apart from the 7-day repo, new tenors of these operations were introduced (14-day and 28-day). The central bank started to inject liquidity (especially ahead of local holiday like the Spring Festival) through the intermediation of other instruments like the Temporary Liquidity Facility or the Contingent Reserve Arrangements (launched in January of 2017 and 2018 respectively).

In late 2018, the PBoC pivoted towards a Funding for Lending (FFL) approach by launching the Targeted Medium-term Lending Facility (TMLF). The FFL was first launched by the Bank of England in 2012 and consisted in supplying banks with very competitive lending, provided these banks were enhancing credit action among small and medium businesses. Among the pioneers of such programmes were central banks from the UK, Hungary and the Eurosystem. The launch of the TMLF was proof that the PBoC was not lagging behind the central banking vanguard.

Obviously, the time framework applied here is of a contractual nature, this is why it must be approached with caution. The beginning of the GS is associated with a significant decrease in FX reserves, which contracted approximately by a little bit more than 20%. Still, it must be borne in mind that in 2015, the PBoC utilized its FX reserves to recapitalize two of its policy banks. Apart from halting the increase in FX reserves, loans of financial institutions to the nonfinancial sector started to play an ever greater role. All the aforementioned factors were quickly translated into the structure of monetary base, thus confirming that the GS brought its first results.

As Bloomberg wrote in its report (2017), in the older era of generous inflows and trade surpluses, China used the required reserve ratio to maintain currency stability. Furthermore, the aforementioned report stated: "Now, as uncertainty over trade grows and foreign reserves have started to decrease, the MLF and other lending tools outlined above have eclipsed required reserves as the key channel to inject funds".

## 4. After the GS efforts aimed at pursuing high quality growth despite deflationary environment

If much of the second decade of the 21st century consisted of switching money creation from external to internal sources, the period from late 2010s onwards was marked by unprecedented challenges stemming from unexpected adversities. Apart from supporting the transition taking place in the

[3] The PBoC in its report for 2016 refers to the 7-day repo operation, which may be somewhat confusing. But in the same report, it states that "In addition to cutting deposit reserve requirement ratio by 0.5 percentage point to supplement long--term liquidity shortage, policy instruments such as open market operations, the Medium-term Lending Facility (MLFs), the Standing Lending Facility (SLFs) and the Pledged Supplementary Lending (PSLs) were used to provide liquidity of different maturities in a flexible way." That is why, in order to avoid any further confusion, I refer to this particular rate as the 7-day reverse repo rate. And this is in line with the majority of reports covering events in the Chinese money market in 2016.

domestic economy, the PBoC had to face an unprecedented pandemic, a bust in the real estate market, a trade war and, above all, deflationary pressures gathering pace. Out of all these factors, special attention will be put on deflation. After all, according to conventional wisdom, it is the main task of every central bank to arrest deflation. This is, however, not the case with the PBoC. In China such challenges are being faced with orchestrated economic policies, where the central voice is an important (but not the only one) component.

Even if China is currently considered a global epicentre of deflation (as yields on Chinese 30-year bonds fell in November 2024 below their Japanese equivalents), the story of deflation in China goes back to at least the late 20th century. As this article focuses on the PRoC, the deflation from early 1930s will be skipped.

Deflation hit China in the wake of the East Asian crisis. The Retail Price Index (RPI) showed price deflation in October 1997, as did the Consumer Price Index (CPI) in February 1998. When it became apparent by mid-1998 that the economy was slowing down significantly, the government began to implement monetary and fiscal measures to boost aggregate demand (Woo 2003). Initially, deflation was not perceived as something harmful for China. There were even voices claiming that China could benefit from this phenomenon (Miyakodayori 2003). Even though deflation ended in 2003, China was often accused of exporting deflation abroad. Suffice it to say that Haruhiko Kuroda, then Japan's Vice Minister of Finance for International Affairs, claimed in late 2002 that through an undervalued renminbi China was exporting deflation (Zhang, Chen 2023). Kuroda was not the only one to formulate this kind of accusations. However, not everyone shared this point of view. As China's demand for commodities started to rise, China started to face accusations of driving up global inflation. As a result, Robert Mundell perceived China at that particular time as a scapegoat, at one time being accused of exporting deflation, and at another blamed for exporting inflation (Willard, Feyzioglu 2006).

From the mid-2000s, the inflation pattern in China hardly differed from global trends. However, a more thorough analysis of the Chinese economy helped detect significant potential for deflation as early as 2015. The deflationary threat was uncovered mainly by domestic economists, whereas it was largely overlooked by international experts. For instance, the IMF wrote in its Article IV review for 2015 that with inflation expectations appearing well anchored and a still-healthy wage growth, the risk of deflation in the near-term appeared to be moderate (IMF 2015). Such verdict was surprising as the Producer Price Index (PPI) at the time when the said review was being drafted had been in negative territory for 39 consecutive months, i.e. since February 2012 (Yongding 2015).

In spite of these warnings, the PBoC did not perceive deflation as a serious threat. In its *China Monetary Policy Report. Q4 2019* (PBoC 2020), the central bank seemed to ignore the first signs of the deflationary threat, by stating: "In the meantime, with the weakening of the base figure effect, the year--on-year PPI decline has somewhat narrowed. Over the short term, factors such as the novel coronavirus epidemic are likely to affect prices, which warrant continued monitoring and analysis. However, judging by the fundamentals, China's economic performance is generally stable, and aggregate supply and demand are basically in equilibrium, providing no grounds for persistent inflation or deflation."

With a benefit of hindsight, such a statement is surprising. The fact that both nominal GDP and M2 moved in tandem in 2018 was taken as evidence for the success of efforts to preserve balance in the economy. Nevertheless, after having fallen in mid-2017 below the level of 10%, the M2 growth has never recovered this level for a prolonged period ever since. A closer look at money growth in 2018 suggests that the year saw another change in the policies pursued by the PBoC. From then on, there

was a certain kind of smoothening of the M2 growth trend with the latter oscillating at less than 10% with a 3% deviation in each direction. Furthermore, a strengthening corelation between GDP and M2 growth rates has become more and more visible. While in the period spanning 1996 to 2016, the average gap amounted to 7.5%, in the subsequent eight years it fell to 3.6%.

Another important element is the behaviour of the Chinese economy in the later stages of the pandemic.

While the reasons why inflation in China remained contained in early 2020s merits analysis, a detailed examination of this issue falls beyond the scope of this text. Nevertheless, the aforementioned ratio of M1 to overall money supply deserves some attention. Even though there are significant discrepancies between the euro area and China, as far as the definition of monetary aggregates is concerned (explained later in the text), the M1/M3 ratio in Europe reached nearly 70%. Such a high level made euro area countries more sensitive to higher price dynamic. China was not even close to such a high ratio. Furthermore, China experienced serious tensions in the real estate sector, which could have contributed to far-reaching caution when it came to releasing savings accumulated during the pandemic. It must be also borne in mind, that following the Covid and the period immediately afterwards, M2 growth saw a brief return to the double digit area, before in 2024 a downward trend in M2 resumed. In June 2024, M2 growth slowed down to 6.2% – the lowest point on record. It somewhat recovered since (data until May 2025), but it never rose above 8%.

The PBoC wrote in its report for 2022 that in order to ensure appropriate aggregate money supply it opted to maintain a stable balance sheet without constraining the growth of both AFRE (the Aggregate Financing to the Real Economy) and M2. The RRR proved to be the key to resolving this conundrum. Former PBoC Governor Yi Gang (2022) explained the mechanism in the following way: "As of end-September 2022, the PBOC's balance sheet was around $6 trillion (RMB 40 trillion). Its size has stayed relatively stable over the past five years with an average growth rate of 2.6 percent. […] Cutting the RRR increases commercial banks' excess reserves and allows them to lend more. As lower RRRs lead to higher money multipliers, we have managed to support more credit creation in the absence of significant balance sheet expansion. Since 2018, the PBOC has cut the RRR 13 times and brought the average RRR down to around 8% from its previous level of 15% and released a total of $1.5 trillion equivalent (RMB 10.8 trillion) long-term liquidity. In the meantime, the PBOC's balance sheet has stabilized at around $5.5–6 trillion equivalent (RMB 38 trillion to RMB 40 trillion). Yet, outstanding M2 has increased to over $35 trillion equivalent (RMB 260 trillion) from less than $25 trillion equivalent (RMB 170 trillion) at end-2017, which is a telling evidence of substantive monetary support for the real economy."

The problem most probably consists in the fact that the aforementioned support should be perceived from the perspective of structural changes taking place in the Chinese economy. One of the factors shaping the state of affairs was the statement issued by the General Secretary Xi Jinping in 2020 when he declared that China will strive to reach its peak emission by 2030 and to accomplish carbon neutrality in 2060. In the wake of this declaration, the PBoC was quick to react and subsequently in November 2021 it launched the Carbon Emission Reduction Facility (CERF). It consisted of RMB 200 billion worth of central bank lending targeted at supporting carbon-reduction technologies amongst others.

A few months later (in April 2022) a central bank lending for science and technology was established in order to implement another strategy aimed to construct "a scientific and technological powerhouse" (BIS 2025). Just to emphasize the importance of structural policies, it suffices to note that by mid-2024, outstanding structural monetary policy instruments stood close to RMB 7 trillion, accounting for about 15% of the PBoC balance sheet (BIS 2025).

There may be other reasons behind structural policies apart from the abovementioned factors. No matter how great the success of the enormous fiscal and monetary package in stimulating the economy, it generated some side effects. One of them was the vulnerability of the Local Government Financing Vehicles (LGFVs). In its *China Monetary Policy Report* (Q1 2024), the PBoC admitted that the economic model driven by the expansion of debt via LGFVs was hard to sustain.

As explained by the Reserve Bank of Australia – RBA (Hendy, Ryan, Taylor 2024), LGFVs served as a primary vehicle for off-balance sheet financing in the wake of the Great Financial Crisis. However, their expansion was far from transparent. The central authorities' response to the aforementioned trend was to phase out government support and expose LGFVs to a more business-oriented model. However, the conversion of LGFVs from local government off-balance sheet financing into a market oriented undertaking, according to RBA, did not go smoothly. One of the reasons were policies aimed at containing Covid 19, which undermined the launching of business models. Being backed with assets of low return, LGFVs are at the mercy of government support. That is why there are reasons to believe that the PBoC refrained from any QE out of fear that a purchase of government debt may derail efforts to restore fiscal balance in the economy.

Obviously, there are other elements of PBoC operational policy that merit further attention, but the scope of this paper precludes us from presenting them in full. In spite of all the efforts undertaken by the PBoC and presented here, the deflationary pressures started to gather pace. One previously mentioned event was symbolic, as on 12 November 2024 the yield on 30-year Chinese bonds fell below that of their Japanese counterparts.

There is no doubt that the tenure of the current PBoC Governor Pan Gongsheng will be marked by steps aimed to counter negative increase in prices. Initially, Pan seemed to follow the policies of his predecessor Yi Gang, focusing above all on avoiding massive stimuli and managing debt--driven risks. In the early days of his tenure, Pan tended to rather downplay the deflationary threat (Bloomberg 2024). Furthermore, Pan attempted to enhance transparency and, above all, to simplify PBoC operational strategy. As a result, in July 2024 he announced that the 7-day reverse repo rate will be the new reference rate (Pan 2024). Governor Pan has since opted to enhance the PBoC's operational toolkit further – for instance, by launching outright reverse repo operations in October 2024 – while simultaneously announcing more aggressive measures to combat deflation. As far as the latter is concerned, such measures were announced in September 2024 and in May 2025. The announced steps went clearly beyond the traditional scope of monetary policies (like cuts in interest rates or in the RRR). In September 2024, measures were undertaken to improve the functioning of capital markets by announcing two programmes. The first one was a swap programme sized at an initial RMB 500 billion, which ensured that funds, insurers and brokers had easier access to funding in order to buy stocks. The second was to deliver up to RMB 300 billion in cheap PBoC loans to commercial banks to enhance their funding of other entities' share purchases and buybacks (Woo, Gao 2024). In May 2025 measures aimed at providing support through relending facilities – including technological innovation, service consumption and elderly care – were announced alongside plans for further capital market boost and property market consolidation (State Council 2025).

Out of the aforementioned measures, it was the announcement of government bonds' trading which attracted the greatest interest among investors (State Council 2024). Hopes were high that this announcement would pave way to traditional QE. While, indeed, these bonds were purchased in the last four months of 2024 and in the last quarter of 2025, the scale of purchase was nowhere near the magnitude of similar actions by other central banks. This state of affairs is not surprising. In the wake

of problems related to LGFVs, launching the traditional QE in China could be risky. What is more, examples of other countries (and Japan in particular) points to a rather limited potential of QE alone in eliminating deflationary pressures.

Being aware of China's uniqueness, Chinese policy makers tend to apply policies deeply rooted in Chinese history. One of them is the set of measures aimed at tackling involution (nei-juan) in the economy. The term comes from the realm of physiology and is defined as retrograde changes in the structure and function of tissues or organs, or else as the return of an organ to its natural size after an illness or physiological functional enlargement. In other words, by countering the nei-juan, the Chinese authorities seek to curb cut-throat competition, which, among other things, exacerbates deflation.

Yi Xiong (Yi 2025) explains the concept of involution by making a comparison to the audience in a theatre. One of the seated spectators gets up just to get a better look at what is happening on the stage. However, all the other spectators stand up after him, which leads to a rather bizarre situation: everyone now sees the same thing as before, with one major difference being that while they used to sit comfortably, now everyone has to stand. The economist explains this by saying that involution involves additional effort that does not lead to the generation of any added value (or, to put it another way, to a proportional profit). Involution is therefore nothing more than additional actions to maintain the initial position on the market. This phenomenon is most easily seen in the Chinese automotive sector.

Chi Lo (Chi 2025) justifies the introduction of involution by the intensity of competition, when Chinese decision-makers had opted for a two-track strategy ('dual circulation' economic strategy). It boiled down to maintaining two circulations: internal circulation, based primarily on domestic demand, and external circulation, which was to sustain net exports. Chi Lo also wrote that manufacturers began to resort to the motto: "if a competitor has it, then I must have it too, and more importantly, I must obtain it at a lower price." It is difficult to come up with a better recipe for deflation.

At the beginning, the Chinese authorities will want to resort to persuasion (e.g. seeking to reduce the amount of overtime), and if it does not work, then specific regulations prohibiting the conduct of devastating price wars will come into force. The proposed policy is not without its flaws. Chi Lo argues that supply-side actions cannot solve the problem of deflation. In addition, anti-involution measures will create a divide between winners and losers. All the more so that the described policy is expected to lead to the introduction of consolidation measures meant to increase concentration among key market participants. This is why the policy in question will not replace actions to stimulate internal demand.

As said before, involution is deeply rooted in the history of China. In order to better understand its origin, it is worth drawing from the work of Philip Huang, whose wide range of research included, among other things, the development of agriculture in China over the centuries. Already in ancient China, one would encounter a system reminiscent of today's involution, where excessive intensification of labour inputs led to decreasing marginal profits despite the increasing total production per unit of cultivated land. As a result, the marginal product of labour was not even able to cover the daily consumption of the worker at the level of the social minimum. According to Huang, the excessive intensification of the use of labour arose as a rational response to the fact that, unlike a capitalist company, a family farm could not lay off its own members, even if the low productivity of their labour justified doing so. Therefore, it is possible to speak of sunk costs, where the inevitable outcome was to maximize the labour of all family members.

Considerations about involution touch on a much broader issue. According to Huang and Zhou (Zhou 2019), they can be a prelude to a better understanding of both the specificity

and complexity of the Chinese economy. It is the history of involution and its impact on this economy that allows us to better understand why the modernization initiated in the 19th century did not bring the same results in the Middle Kingdom as it did in Japan during the Meiji Restoration. This view almost overlaps with Needham's.

Li-An Zhou and Huang make it clear that it is impossible to understand the People's Republic of China today without a proper insight into its history and culture. They warn against evaluating economic processes in the Middle Kingdom using exclusively the Western way of thinking. At the same time, they encourage the search for a philosophy of the middle that would take into account both the scientific achievements of China and the West.

Concluding the description of the PBoC's operational policies, it must be borne in mind that Article 3 of the PBoC Law states explicitly that the objective of monetary policy is to maintain the stability of the value of the currency and thereby to promote economic growth. This is why the PBoC cannot remain indifferent to what happens to both the internal and, above all, the external price of the currency. The trade war launched by the US in 2025 does not make this task easy. Even though a floating exchange rate is far better suited for a large economy, China opted to go against the tide. Perhaps China's economy it too large to afford excessive fluctuations in the exchange rate. That is why China keeps a close lid on the external price of its currency. Although capital controls are most probably the most important tool in helping keep the exchange rate within a tight range, there are also other tools in play. One of them is the issuance of central bank bills in Hong Kong (in cooperation with the Hong Kong Monetary Authority), an arrangement highlighting China's uniqueness under the formula "two economic systems within one state".

Hong Kong seems to play an important role for Mainland China from the point of view of raising exchange rate flexibility and renminbi's internationalization. It is worth remembering here that the cooperation between the PBoC and the HKMA is not limited to the issues raised above. It is much broader and includes, among other things, cooperation in the field of digital currency and broadly understood fintech. Furthermore, Hong Kong offers Mainland China room for experimentation in the field of the latest technologies, which inherently carry various types of risks. It is therefore better to confine all such experiments in their initial phase of development to the Special Administrative Region rather than to carry them out on the Mainland. Doing so avoids exposing a population larger than those of the USA, Europe and Japan combined to potential dangers. There is no doubt that the PBoC will play a fundamental role in supporting the focus on innovation which was so strongly highlighted in the 15th Five-Year Plan, approved in March 2026 for the 2026–2030 period. All these factors combined point to the idiosyncrasy of Chinese monetary policies as derived from domestic experience gathered throughout the country's long and complex history.

## 5. Summary and conclusions

China has been subject to many misconceptions in the Western world. These misconceptions affect our perception of China today. Admittedly, Chinese economic miracle achieved in the last 47 years has generated worldwide admiration and the present text has taken upon itself to detail the role of the central bank in this undertaking along with the historical sources of inspiration for this miracle. However, the launch of the PRoC in 1949 leaves many observers under a strong impression that this

date constitutes a watershed separating today's China from its past entirely. Even if it were not, our perception of the Chinese heritage seems affected by all those scholars of times past who deliberately tried to belittle it (Spengler 1977) in order to justify the expansionist policies of the time toward the Middle Kingdom. It was only with the advent of people like Bertrand Russel and, above all, Joseph Needham, that the skewed perception of China began to be put under scrutiny. However, retrieving the lost respect for the Chinese culture and scientific achievements does not imply finding a common denominator between the Western civilization and the Chinese one. China differs not only from the West, but also from the majority of Asian states. To find differences among neighbours is no surprise. You can trace common origins for most of modern European languages and yet find that divergent paths led them towards very different end points.

The spectacular collapse of the centrally planned economies of Central and Eastern Europe cast a huge shadow on any alternative to the emerging and then prevailing Washington consensus. Anything that departed from the established economic consensus was perceived with suspicion and bred incredulity. In any case, it was seen as a fleeting anomaly and expected eventually to fail. Yet, the Chinese undertaking did not succumb to pressure. Little wonder that for a long time, in the 1990s, China was described as "the land that failed to fail" (Rudyak 2025). This perception of the Chinese economy has started to change in the last fifteen years. Embracing the Chinese past is helpful in understanding why the political system installed in 1949 in China managed to survive. A detailed analysis would find many parallels between nowadays' China and its past, not only letting us comprehend the Chinese economy better but also proving its uniqueness.

Central banking is an invention of the Western culture. While China was the first to launch paper money, the inability to create a successful debt market prevented China from being a pioneer in the field of fiat money. Efforts to catch up with the West in the first half of the 20$^{th}$ century ended badly for the Chinese economy. This is why it should not be surprising that current policymakers distance themselves from the prevailing central banking models and subsequently opt for their own solutions. Consequently, the PBoC lacks independence, functioning instead under the State Council umbrella. Monetary policy in China serves as just one tool in the toolbox for the implementation of broader economic policy (BOFIT 2024). This does not, however, prevent the central bank from drawing lessons from the past, with the story of nei-juan being a good example. Another valid illustration is the pursuit of structural policies, as such endeavours are not detached from the needs of the real economy. Unlike Western central banks, the PBoC does not shy away from state priorities. For example, it explicitly aligns its work with the country's national decarbonisation strategy (Larsen, Jackson 2025).

At the same time, the PBoC does not ignore the experience of other central banks. After all, monetary rules seem to be universal. It is just that as the central bank of the largest economy in PPP terms – with a population larger than those of Europe, the US and Japan combined – the PBoC feels entitled to pursue its own policies. These can be described as the application of universal monetary strategies enriched by the historical experience of a country with 5000 years of history to draw upon. And if to this combination, we add the political formula of "two systems within one state" (one which should in fact be redefined as two different monetary regimes within one country), we obtain a central bank with unique characteristics. Its contribution to the economic success should provide an additional incentive for further scrutiny of the policies that this bank pursues.

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## Acknowledgements

Special thanks go to Prof. Bogdan Góralczyk from the University of Warsaw, most probably the best sinologist and China enthusiast I have ever met. His valuable remarks helped me to improve the content of this text significantly. The same is true for Prof. Haizhou Huang, the member of the Monetary Policy Committee of the People's Bank of China and also affiliated at Tsinghua University, whom I met during my first ever visit to China. His words of encouragement and confidence in my work were instrumental in completing this work. Needless to add, any remaining errors and imperfections of this paper are the sole responsibility of the author.

# Wpływ historii Chin na kształtowanie polityki pieniężnej: szczególny przypadek Ludowego Banku Chin


## Streszczenie

Chińska Republika Ludowa zyskuje w ostatnim czasie spore uznanie za swoje osiągnięcia gospodarcze. Sam fakt znacznego zmniejszenia liczby ludzi żyjących poniżej granicy ubóstwa zasługuje na szacunek ze strony ekonomistów na całym świecie. Szacuje się, że w ciągu niespełna półwiecza chińskim władzom udało się wydostać z biedy około 800 milionów ludzi. Nic więc dziwnego, że coraz więcej osób zaczyna mówić o cudzie gospodarczym. Jest ewenementem na skalę światową, że system gospodarczy nadal odwołujący się do idei marksizmu i leninizmu odnalazł swoje miejsce w globalnej gospodarce. W dającej się przewidzieć przyszłości pozycja sterującej tym krajem Komunistycznej Partii Chin wydaje się zatem niezagrożona.

W niniejszym artykule podjęto m.in. próbę przedstawienia przyczyn takiego stanu rzeczy. Sam fakt, że populacja Chin liczy około 1,4 miliarda mieszkańców, każe wątpić, że Chiny mogły odwoływać się do tych samych lub nawet podobnych wzorców w zakresie polityki gospodarczej (w której skład wchodzi oczywiście polityka monetarna), co inne najważniejsze gospodarki na świecie. Chiny zdecydowały się na realizację własnej wizji zarządzania gospodarką, co w żaden sposób nie wyklucza zainteresowania chińskich decydentów tym, jak inne kraje sterują swoimi gospodarkami.

Szukanie inspiracji w innych krajach w celu znalezienia nowych i skutecznych rozwiązań jest dla władz w Pekinie ważne w kształtowaniu polityki gospodarczej. Ewentualna implementacja zależy jednak od upewnienia się, że dane rozwiązanie nie stoi w sprzeczności ze specyfiką rodzimej gospodarki.

Wspomniana specyfika opiera się na dwóch filarach. Po pierwsze, chińska władza określa prowadzoną przez siebie politykę mianem socjalizmu o chińskiej specyfice. Uwzględnienie tego wydaje się niezbędne do zrozumienia całej polityki gospodarczej. Jest to szczególnie ważne zwłaszcza w przypadku wszystkich tych krajów, które mają za sobą smutne doświadczenia w eksperymentowaniu z gospodarką socjalistyczną. Opis analizowanej tutaj specyfiki pozwoli na lepsze zrozumienie, dlaczego wspomniane eksperymenty niemal wszędzie poza Chinami nie były w stanie sprostać oczekiwaniom społeczeństw.

Drugim filarem jest spuścizna historyczna tego kraju, istniejącego od około 5000 lat. Wielu przedstawicieli świata zachodniego jest przekonanych, że powstanie Chińskiej Republiki Ludowej w 1949 r. stanowi cezurę oddzielającą obecne Chiny od ich całej przeszłości. To oraz wiele innych poglądów i stereotypów bierze się stąd, że wokół Chin narosło wiele nieporozumień w świecie zachodnim. Nasze fałszywe wyobrażenie bierze się z tego, że postrzeganie chińskiego dziedzictwa w Europie nadal kształtują obserwatorzy, którzy wręcz celowo próbowali lekceważyć dorobek cywilizacyjny Chin, aby uzasadnić – w dobie rosnącego światowego imperializmu – swoją wyjątkowo ekspansjonistyczną politykę wobec Państwa Środka.

Zmianę w postrzeganiu Chin zapoczątkowały prace Bertranda Russela, a przede wszystkim Josepha Needhama. Rodzący się szacunek dla chińskiej kultury i osiągnięć naukowych nie oznacza jednak znalezienia wspólnego mianownika między cywilizacją zachodnią a chińską. Rzecz w tym,

że Chiny różnią się nie tylko od Zachodu, lecz nawet od większości państw azjatyckich. Wystarczy odwołać się do korzeni większości języków europejskich. Nic więc dziwnego, że radzą sobie ze swoimi własnymi problemami czy wyzwaniami w sposób często niezrozumiały dla otoczenia zewnętrznego. Tekst ten jest jedynie próbą wyjaśnienia chińskiej specyfiki, która swoim zasięgiem obejmuje również gospodarkę.

Tematem przewodnim artykułu jest bankowość centralna, stanowiąca wynalazek cywilizacji europejskiej. Nie zmienia tego nawet fakt, że Chiny jako pierwsze wprowadziły papierowy pieniądz. Jednak brak zdolności do stworzenia dobrze funkcjonującego rynku długu uniemożliwił Chinom stanie się pionierem w dziedzinie pieniądza fiducjarnego. W dużej mierze przesądziło to, że w dziewiętnastowiecznej konfrontacji z cywilizacją europejską chiński model gospodarczy po prostu się nie sprawdził. Z kolei rozpaczliwe próby dogonienia Zachodu w pierwszej połowie XX w. zakończyły się klęską dla chińskiej gospodarki i niemal doprowadziły państwo do upadku.

Nie powinien więc dziwić fakt, że współcześni chińscy decydenci dystansują się od dominującego obecnie modelu bankowości centralnej i preferują własne rozwiązania. W rezultacie PBoC nie cieszy się niezależnością jak większość najważniejszych banków centralnych. Co ważniejsze, Ludowy Bank Chin podlega Radzie Państwa ChRL, która z kolei jest podporządkowana Komunistycznej Partii Chin. Prowadzona przez bank centralny polityka monetarna stanowi tylko jedno z narzędzi szerszej polityki gospodarczej. Nie przeszkadza to jednak bankowi centralnemu w wyciąganiu lekcji z bogatej historii gospodarczej tego kraju, a pojawiający się problem inwolucji (nei-juan) jest dobrym przykładem analizowanego tutaj podejścia. Innym przykładem jest odwoływanie się do szeroko rozumianej polityki strukturalnej, za pomocą której bank centralny usiłuje bezpośrednio wpływać na procesy zachodzące w sferze realnej gospodarki.

Jak wspomniano, PBoC nie dystansuje się od doświadczeń innych banków centralnych – w końcu prawa ekonomii wydają się uniwersalne. Dysponując jednak największą gospodarką (pod względem siły nabywczej) oraz populacją przewyższającą populacje Europy, USA i Japonii razem wzięte, Chiny mają chyba prawo realizować własną wizję polityki monetarnej, którą można zdefiniować jako uniwersalne strategie monetarne wzbogacone o historyczne doświadczenia kraju. Dodatkowo dzięki odzyskaniu Hongkongu mogą stosować dwa odmienne systemy gospodarcze w ramach jednego państwa, przez co ich bank centralny znalazł się w bardzo uprzywilejowanym położeniu. Rzecz w tym, że Hongkong stał się dla Ludowego Banku Chin swego rodzaju laboratorium do testowania innowacji finansowych, zanim zostaną wprowadzone w pozostałych częściach ChRL. Niewykluczone, że z tych innowacji mogą kiedyś skorzystać także inne kraje.

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**Słowa kluczowe**: gospodarka, stopa procentowa, płynność, Ludowy Bank Chin, inwolucja