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REGIONAL PAYMENTS AND CO-OPERATION PROBLEMS OF LATIN AMERICAN CENTRAL BANKS

INTRODUCTION

The Latin American Centre for Monetary Studies (CEMLA) submitted the following working documents for examination at the seventh Meeting of Central Bank Technicians of the American Continent which was held at Rio de Janeiro in October 1963 and in which some 70 experts representing most countries of the western hemisphere participated. The questions of Latin American payments and of the measures to be taken to establish real co-operation between the Central Banks of the region were among the most important on the agenda of that meeting. They had been given high priority for despite the continued progress of the Latin American Free Trade Area, results so far obtained with respect to regional arrangements for payments and financial and monetary co-operation have been fairly slight.

According to its final report, the results achieved by that meeting represent the first positive measures towards the negotiation, in a relatively near future, of a regional Latin American payments system. The participants agreed on the main characteristics of such a system. They agreed that any Latin American payments system will have to be optional both as regards membership of the countries of the region and the use to be made of the system for clearing purposes and that in the present situation the operation of the mechanism should depend on the general balance of payments position of member countries and should not supply automatic credits to balance payments.

The most interesting feature of the Rio de Janeiro meeting was the acknowledged importance of the need to use the regional payments institution as a permanent organization for the gradual co-ordination of monetary and financial policies in the region. The participants were generally agreed that the real purpose of a regional payments system goes beyond clearing and payments operations and that progress in regional economic co-operation calls urgently for co-ordination of the policies of the central banks.

It should also be pointed out that the observer for the International Monetary Fund stated that if necessary the IMF would give favourable consideration to any concrete system which the Latin-American members of the Fund might drawn up.

The Meeting requested CEMLA to examine with the IMF and the Economic Commission for Latin America the possibility of establishing regional clearing and credit machinery and a regional institution responsible for co-ordinating financial and monetary policies in Latin America.

PROBLEMS OF A PAYMENTS UNION FOR LATIN AMERICA^{1/}

An outline will be given here of the main features of the two ECLA schemes and of the Triffin proposal for possible payments and credit systems in the free trade area. This brief review will make it possible to distinguish fundamental opinions and matters of detail. This distinction will in turn introduce the examination of the chain of events which in both systems lead to divergent consequences.

A. Review of Projects

ECLA Projects

1. The two systems offered by ECLA have a number of important points in common and are distinguished only by the ways and means of liquidating surpluses and deficits within the area.
2. Care is taken to secure the co-existence of bilateral payment agreements, to the extent that they are maintained or would be re-established, and relationships between countries making settlements in convertible currency.
3. Whatever the final liquidation machinery, provision is made for:
 - (a) An agency responsible for the periodic liquidation of surpluses and deficits;
 - (b) The establishment of a dollar (money of account) account per country;
 - (c) Periodic liquidations at intervals of 60 or 90 days;
 - (d) A decentralization of operations in each country, the Central Bank establishing the external operations balance of approved banks;
 - (e) The establishment of a fund available to the agency to bridge the gaps between net payments in convertible currency it should receive and those it should make;

^{1/} Abridged version (parts II and III) of a document drafted by Mr. Pierre Uri, Director of the Atlantic Institute, Paris, for the Latin American Centre for Monetary Studies (CEMLA) and submitted by that Institute to the Central Bank Technicians of the American Continent at their seventh session (Rio de Janeiro, October 1963).

- (f) The establishment of quotas by country, estimating both the credits they are willing to make or entitled to receive.

Failing the immediate and integral multilateralization of balances, two progressive ways of introducing bilateral agreements into the system are suggested:

- (a) The establishment of a limit to bilateral credits, the surplus being transferred to the agency for multilateralization
- (b) The transfer to the agency, at the end of each accounting period, of a percentage of the balances, in such a way that finally they would be transmitted in full to the agency for multilateralization purposes, in successive fractions.

4. The principle of multilateral credits is that each country shall receive payments in convertible currency only in excess of the credit quota it grants and shall pay in convertible currency only in excess of the credit to the same amount, from which it benefits.

5. These credits may be administered in two different ways depending upon whether the a priori (or preventive) or a posteriori technique is followed.

6. In the first, settlements in convertible currency are not made until the end of the liquidation period. In the second, settlements in convertible currency are made from day to day and dollars thus received or paid, and the amount of which remains within the credit margins granted or obtained, have to be reimbursed to, or by, the agency.

7. Within each country the differences occur in the relationship between approved banks and the central bank. In the a priori credits system, the central bank constantly establishes the balance of the approved banks. In the a posteriori credits system operations are effected between banks and centralization by the central bank is merely statistical.

Triffin Proposal

8. The Triffin proposal in its turn provides for:

- (a) An agency which might be the Inter-American Bank or the International Monetary Fund;
- (b) The establishment with the clearing house of an account for each country in a unit of account, the dollar or the Latin-American peso;
- (c) Inter-country payments by adding to or deducting from their accounts;
- (d) The purchase from or sale to their residents by the central banks for payments to be received or made in their relations with residents of another participating country;
- (e) A monthly liquidation period, with settlement in gold or in convertible currencies of net creditor or debtor positions with the clearing house;
- (f) Credit systems which could be established gradually and which include:
 - i) The carry-over at the end of the month of settlements, except that a monthly credit line is defined for each country which, if exceeded during the month, gives rise, in one direction or another, to a settlement of the surplus of claims or debts;
 - ii) Credits, of limited amount and duration, making it possible to defer the end of month settlement and gain time, pending negotiations for more general credits of a non-automatic nature, such as those the International Monetary Fund may grant and to which they could if necessary be added;
 - iii) Special credits also non-automatic, granted by the clearing house itself;

- (g) The constitution, to meet stand-by credits, of a fund to which contributions could be made by institutions outside Latin America or by the member countries by a percentage of their reserves, i.e. by deposits in gold or convertible currency the amounts of which would vary with that of the reserves themselves.

9. It will be seen that in the ECLA and Triffin schemes loans are borrowed from quite different parties than in the case of the European Payments Union. The Triffin project, for example, has borrowed the unit of account and interim finance, due to the carry-over at the end of the month, which also appears in the European Monetary Agreement. The technique of making transactions in units of account and of replenishing a fund by a percentage of the sum of reserves held by Member States at any time is linked to the reform projects suggested by Professor Triffin for the international monetary system, for the European Economic Community and other groups.

10. The main features of the combination of credits and payments in gold or convertible currencies depending on the regional balance position of each Member State, which characterized the European Payments Union, are to be found in the ECLA project.

B. Basic options and matters of detail

11. Certain practical methods and the main orientations must be distinguished in a clearing system. Arguments of convenience may be advanced regarding the former and finally the decision results from the result of negotiations, from arguments or interests put forward by the participants or from practical compromises which take shape. The basic options, on the other hand, must be decided in terms of the economic effects of one system or another and more particularly of its adequacy in respect of an existing situation or an evolution which must be promoted.

12. The first category of questions cover the following points:

- duration selected for the period of liquidation. If settlements are made daily, as in the Central American Clearing Fund, the credit element is nil. The more spaced out the liquidations the longer the duration, if effective settlements in gold or convertible currencies are - unless the balances exceed certain sums - carried over to the date of liquidation. This is the case with a priori credits in ECLA project I, and with interim financing in the Triffin project. On the other hand, in ECLA project II - that of transfers of convertible currencies by those who have earned too many or to those who have lost too much - the longer the period of liquidation the weaker the credit element.
- Definition of a money of account. This in any case is a necessary means for the reduction to uniform units of debts and claims which may appear in a number of different currencies. Whether the dollar or a unit equivalent to the dollar is chosen is a matter of political presentation; in this case the guarantee of stability is equal to that of the dollar. If on the other hand the unit is defined, as was that of the European Payments Union, its stability may be greater: in this case, the unit of account was as stable as the least devalued national currency in Europe or the United States.
- Fixed value or spread. The translation of national currencies into a unit of account at a single rate is an obvious simplification. This was the system of the European Payments Union. The Triffin project proposes the same system. Clearings may however be organized despite the existence of a gap between the sale and purchase prices of foreign exchange: this formula was accepted in the European Monetary Agreement. The rate at which claims or debts are settled must then be defined.

The Monetary Agreement distinguishes several cases:

- i) Acquired balances by a central bank, operating on the market, for repurchase by the debtor country: they are settled at the sale price of the dollar in the debtor country;
- ii) Balances resulting from interim financing: they are settled at the purchase price of the dollar in the lending country;
- iii) In the case of bilateral payments agreements, balances are settled at the rate provided in those agreements.

It is noted that in the first two cases the rate is the most disadvantageous for the debtor.

- Fixing of limits to loan facilities. The limit may be fixed in relation to the value of exchanges in a near period or in relation to the value of settlements between a given country and the clearing house. Triffin proposes to begin with the first formula and pass on to the second according to the experience gained.

13. On the other hand, the replies to the following points, which are interconnected, must be regarded as basic options:

- Automatic or discretionary credit. The system proposed by ECLA is based on an automatic credit, although no formula is given as regards the equal amount which each country may obtain or must grant. Automatism figures in the Triffin system only for interim financing resulting from the carry-over of the settlement to the end of the month. Short-term credits which may obviate payment at the end of the month may be classified as semi-automatic: they are of the nature of a relay. On the other hand, any large credit granted outside the two preceding categories, either internationally or through the resources of the clearing house, must be based on examination of a situation and a stabilization programme.

Two factual observations clarify the matter.

14. The aim of a clearing system is to eliminate or at least reduce purely bilateral settlements and reproduce them in a group consisting also of countries accustomed to settlements in convertible currencies. The latter will no doubt find advantage in machinery which facilitates payments and at the same time their own exports. It is hard to imagine, on the other hand, that, if they are creditors, they will be ready to grant automatic credits for periods that may be indeterminate.

15. This would amount in effect to forgoing means of payment which they need elsewhere for it is a fact that nearly all Latin American countries suffer from persistent deficits in their external balances.

- Regional or global balance. An automatic credit through a clearing fund cannot be based on a regional balance, not knowing whether the country which shows a surplus in the region does not show a deficit elsewhere, whether the country which shows this deficit in the area does not offset it by surpluses with the rest of the world. The consequence may be that a country will be led to transfer - in the ECLA II system, for example - a posteriori credits, dollars earned in the area and used for payments to be made elsewhere: it will have to borrow them to refund them to the fund. ECLA accepts this consequence, maintaining that a country must not earn dollars at the expense of its partners in an effort at reciprocal liberation. Triffin, on the other hand, affirms that a country may be obliged to achieve a global balance but not a regional balance.

16. The obtaining of credits, followed by their exhaustion and immediate settlement, cannot govern the economic and financial policy of a State, and determine the moment when austerity cannot be avoided, in the case of a trade which includes but a fraction, equal to 20 per cent in the highest case and to 10 to 15 per cent on an average, of the total trade of the countries concerned: such today is the role of inter-regional trade in Latin America.

- Compulsory centralization of operations or not. The ECLA project adopts no position on this matter. During the discussion in Mexico, Triffin stated that his project did not exclude direct settlements between banks.

This point implies essential consequences.

The Monetary Fund experts emphasize in their paper that a clearing system results almost of necessity in inciting countries to centralize all their operations, i.e. to maintain exchange controls or even establish them where they do not exist, and finally to eschew convertibility. The argument is as follows:

17. Take two countries A and B, one of which requires its residents to effect all their settlements through a clearing office while the other allows its residents a choice. If country A receives a fraction of the settlements due to it outside the clearing fund it will be able in the accounts to make its debit situation appear larger than it really is. On the other hand, country B's credit position in the books may exceed its net position. The result would be that A would be entitled to larger credits and B would have to grant larger credits than was justified by the real relationship of their balances in the area.
18. It must be pointed out at once that these observations are not valid in the case of the ECLA II system: settlements are all effected in accordance with ordinary banking methods and are statistically carried over at the periodic settlements by the clearing house. Nevertheless, the difficulty of accurate stock-taking is obvious.
19. But that is not the real issue. The objection of the Monetary Fund experts is valid only to the extent to which the clearing house administers automatic credits. If only interim financing for an average duration of 15 days is involved the point loses all its importance. If the other credits granted by a regional organization are discretionary or short-term, there is nothing much to gain by showing in the clearing account credit or debit

situations which do not correspond to the total amount of the transactions, but only to those channelled through this system. This provides an analogy with the evolution of payment methods and the currency situation which caused the development of the European Payments Union and finally its replacement by the European Monetary Agreement. The possibilities of direct arbitrage, causing a part of the transactions to evade clearing, do not basically change credit needs: the net positive or negative balance is the same whether a fraction of the transactions is cleared directly and another transmitted to the clearing house. Much more important is the possibility of obtaining the currency of other members on the free market and causing at will variations in the creditor or debtor position transmitted to the clearing house. As soon as that facility was offered, the European Payments Union had to try to eliminate automatic credits based on a combination of payments by credit and settlements in gold or in dollars within the limits of a cumulative situation carried over to a quota. It had to adopt the integral settlement of balances together with simple interim financing and completed where necessary by non-automatic credits.

C. Logical sequences

20. The very brief analysis of the projects, the review of purely practical options or on the contrary of options of principle which must be taken up, make it possible to summarize the logic of the systems proposed, the sequence which leads from an initial position to a series of solutions or perhaps difficulties.

The ECLA system is based on the principle of reciprocity regarded as the condition for regional integration.

The regional balance, but not the global balance, is therefore taken into account. Reciprocity requires, and consideration of the regional balance permits, that credits should be automatic. They imply the establishment of quotas according to country, defining the global credit which countries may receive or must grant. Repayment of credits obtained is effected only by transfer of the cumulative position of the Member State involved.

The automatism of credits leads Member States to channel their transactions and if necessary to re-establish appropriate controls in this way. In any case, a Fund is necessary as in the European Payments Union: the gold and convertible currencies paid in by some are not automatically transferred to others. Inversely, the creditors may be entitled to such settlements without the debtors being obliged to effect them since the rights and obligations depend on the credit situation carried over to the quotas. The Fund bridges the gaps between the situations of the various parties.

21. The sequence of events resulting from Professor Triffin's premises is entirely different.

The objective is not reciprocity but the saving of foreign exchange by the use of a money of account, the establishment of guarantees facilitating both trade development and the credit of the Latin American countries in their relationships with the outside world and finally a co-ordination of economic and monetary policies.

Consequently, there can be only very limited automatism of credits. The month's transactions are all settled in gold or in foreign exchange at the time of settlement, except relay credits which must be redeemed over a limited period.

The exclusion of any large-scale automatism prevents the exclusiveness of the system: it is compatible with the method of settlements between banks and of arbitrages; there are only inducements to use the money of account to the extent that it saves foreign exchange.

The system therefore implies no re-establishment of controls where they do not exist or tightening of controls where they do exist.

A Fund is not a sine qua non, for settlements are effected in gold or a convertible currency. It is, however, a very useful complement to reinforce the guarantees constituted by the unit of account system and to ensure credits. It is proposed that, apart from foreign contributions, the Fund's supplies should be based not on fixed quotas but on the reserves situation of each country.

22. It emerges from this brief comparison that the objections to centralization, the abandonment of banking settlement procedures, the disruption of trade flows, and the return to controls cannot be raised in general and in the abstract against all clearing house systems: on the contrary, systems may be established which escape them entirely, while at the same time strengthen the flexibility of settlements, the solidarity of States and the credit of the region.

23. The Commission has also

24. The Commission has also

25. The Commission has also

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27. The Commission has also

SPECIAL PROBLEMS

23. A certain number of determinations appears necessary for the completion of multilateral settlement projects; a certain number of difficulties frequently cited must be either overcome by reasoning the case or removed by the rules of the game. This is due to the consequences resulting from the diversity of the monetary systems in force in Latin America.

A. Replenishment of a fund

24. There are two questions - in great measure inter-connected - relating to the extent of resources necessary and the sources from which they may be derived.

25. It is to be hoped, of course, that foreign funds will facilitate the establishment of any settlements system set up by Latin America. In so far as the resources which could be derived from the area itself are concerned, it is not a good argument to say that the total of the available means would not be increased thereby. For that total may be much more efficiently used either because temporary surpluses, rather than remaining idle, facilitate the development of another country or because credits are better distributed to allow of more economic trade.

26. The extent of resources obviously depends on the function of a fund at the disposition of a clearing house. Its function in a system such as that of ECLA, in which it would resemble the capital which the European Payments Union needed, is different from its function in a system under which net settlements are made in gold and convertible currencies.

27. Under the first system, the fund must make it possible for the gap between the entitlements to payments in gold or dollars of some and the entitlements to payments in gold or dollars of others to be bridged. On this point the ECLA document contains certain calculations and Professor Triffin compares the volume of trade to be financed in Latin America with that for which the European Payments Union assumed responsibility.

28. An a priori determination of the sums necessary under the various systems and assumptions is practically impossible. It must be remembered, that if settlements through clearing agreements are not exclusive, other credits may be added to them in inter-bank relationships or by taking a round-about way through American banks. Export credits are beginning to be organized in Latin America with a view to developing trade in industrial products within the area. There is a special difficulty with respect to trade in agricultural products, which may fluctuate considerably depending on the harvest in one country or another. Even if bilateral payments agreements, covering all inter-country transactions, must be abandoned for the sake of multilateralization, no one considers it necessary that a country should be forbidden to combine a credit with a delivery from a surplus harvest which might, the following year, be followed by an import to offset a deficient harvest.

29. The size of a fund, therefore, is not measured by the totality of transactions but rather by the specific tasks assigned to it, whether it serves as cash in hand ensuring flexible adjustment of members' claims and debts, or to honour guarantees, or is the basis of credits of less than a year or of longer-term additional and discretionary credits.

30. It is practicable therefore to seek a formula which may be added as an experiment without constituting a real burden for those countries which have to contribute. This argument pleads in favour of a fund in which the Member States would deposit a fraction of their reserves, varying with the level of these very reserves.

31. What are involved, of course, are gross reserves from which short-term commitments have not been deducted. The net reserves method would lead to many countries, including the United States and Great Britain, showing a negative figure. When these commitments fall due the reserves will be reduced and contributions reduced in proportion. There is no need therefore to discount in advance a hypothetical reduction of the resources available to a country for its payments.

32. The system of contributions fixed as a percentage of reserves gives rise to certain misunderstandings. The following is a quotation from another work by the author of this report:^{1/}

"Some critics expressed concern about the automatic granting of credits which the system seems to imply. But this criticism is founded on a confusion. It is true that funds would automatically become available as a result of an increase in Members' reserves. But, apart from marginal sums at short terms, the granting of joint credits should remain a purely discretionary matter linked to a programme for restoring the payments balance to be discussed by the deficit country with the countries providing collective aid.

Secondly, it is feared that there may be difficulties in collecting contributions from Member States. It is true that - as opposed to the International Monetary Fund's system of fixed quotas governing the amounts both of subscriptions and of permissible withdrawals - the connexion between the facilities available and the obligations assumed would here appear to be broken; and it is further stressed that it is the prospect of receiving facilities that prompts countries to make the required contributions. This observation, however, though it may hold good of the member countries of the Monetary Fund as a whole, ceases to apply when the only countries in question are advanced countries with a long financial tradition. Moreover, it is essentially incompatible with the refusal to admit any sort of automatism in the credit system; for if there is no automatic credit, there can be no link between rights and obligations.

Again, it is argued that States prefer fixed obligations to variable contributions. That is, of course, true in so far as they seek to prevent an increase in available funds from resulting in an increase in their obligations. But the reverse is equally true: it is difficult to meet fixed obligations when available funds fall off. It appears, therefore, that an adjustable system involves on the whole less risk.

^{1/} "Dialogue des Continents" - Plon Editeur, Pages 133 and 134.

Lastly, it is objected that the criterion by which contributions are fixed in terms of reserves does not correspond to the real resources of a country - its wealth and its income. This criticism also misses the point. A private person's savings in cash or at the bank are not always in strict proportion to his total property or his income. Nevertheless, they constitute a fund of credit which, by his own decision, he makes available to others. In the same way a country which hoards gold or foreign currency is in fact, by that very decision, granting credits to other countries. It is simply a question of recognizing the fact and of bringing it to the notice of the country concerned - and not of imposing a tax on such a partial assessment basis. Moreover, this contribution of a fraction of its reserve carries certain advantages: it is interest-bearing and may be covered by a guarantee".

33. It would seem, therefore, that this system is preferable to a system of quotas. Its particular advantage lies in the fact that creditor countries recover their liquidity when it is needed to effect payments. The practical solution is to fix the contribution required of member States in a more or less arbitrary manner at some moderate figure, while at the same time establishing a procedure by which it may be raised in case of need and, above all, providing an incentive to make voluntary deposits above the required minimum by arranging for interest to be paid and by providing solid guarantees.

B. Monetary practices

34. Another group of problems arises from the variety of monetary systems in existence, that is to say, from the extent to which these diverge from the system of free and stable exchanges.

(a) Exchange Control

Exchange control would not appear to constitute a real obstacle to the introduction of a clearing system, which may indeed provide an effective method of co-operation between monetary authorities. The Central American Clearing House receives from countries operating exchange control only cheques or payment orders which have been stamped by the State concerned to confirm that they comply with its exchange regulations.

Under the ECLA II system, under which countries pay or withdraw foreign currencies, the problem of exchange control remains a purely internal matter for each country.

Under the machinery proposed by Professor Triffin, whereby States sell rights of withdrawal to their residents, the States themselves are entirely free to limit such sales to legal transactions, whether on current or on capital account.

- (b) The problem of multiple currencies at first sight appears more complicated. In reality, however, this is only the case when a State is in a position to obtain from another State in respect of certain transactions or certain products the payment either of a large sum of the latter's currency or of a quantity of convertible currencies. In other cases, multiple exchange rates are essentially an internal matter governing the rates at which currencies are bought or sold for different types of transaction to residents of a country.

In the present situation on world markets, the first problem has very little topical interest. In any case, it can be adjusted by export duties. At the worst, the situation resembles that when a country demands, for certain markets, direct payment in gold or in "hard" currency. If payments through a clearing fund are covered by satisfactory guarantees of exchange or convertibility, whilst deposits or credits carry interest, even this temptation is removed. In any event, it has been shown that a clearing system can operate effectively even if it does not cover all transactions, so long at least as it does not involve substantial automatic credits granted for indefinite periods and repayable only by a debtor country becoming a creditor.

The essential point about a system of multiple currencies is that residents buy or can sell foreign currencies at different rates according to the transaction for which they are needed. In the simplest case, differential rates are fixed for commercial and

for financial transactions. The next degree of complication is when differential rates are fixed for different categories of exports and imports; thus traditional exports may be given a less attractive rate, while the currency thus obtained is devoted to essential imports at favourable rates; higher rates are fixed to encourage new types of export and to impose restraint on non-essential imports. The situation becomes still more complicated if rates are differentiated for various types of product, and particularly in those systems under which available stocks of foreign currency are allotted to various types of import and where the allocation for a given product is sold by competitive bidding. Systems of that kind are equivalent to import and export taxes or subsidies; but they do not prevent a country from fixing a single rate at which its transactions with foreign countries are liquidated. The real question is whether that rate is effective, or whether the official market is not short-circuited by another market on which residents consent to pay a considerably higher price for foreign currency and on which non-residents can obtain the currency of the country in question at a discount.

The consequence of a system of multiple currencies in a clearing system based on a unit of account is that - to the extent to which such practices in a given State are permitted by the Monetary Fund - that State has the right to sell to or buy from its residents rights of withdrawal on the clearing fund at different rates of exchange.

(c) Fluctuating rates

Mention must be made of the rapid variations in the exchange rates of a certain number of Latin American currencies. The problem inevitably arises as to how far variations are compatible with the introduction of a clearing fund.

These fluctuations may affect all transactions indifferently or else some transactions may be conducted for a time at a fixed rate pending the fixing of a new rate, while the remainder - whether they are commercial or capital transactions - are left to

the workings of the free market, which may or may not be subject to government intervention. In the latter case, exchange fluctuations and multiple rates are combined in the simplest manner: that of two markets.

A fluctuating rate is only the extreme form of periodical adjustments of exchange rates, and regulations have to be devised for cases in which the rate of a currency changes during a liquidation period. It is obvious that solutions will differ according to the length of the liquidation period and the clearing machinery.

If balances are cleared daily and settlements are made in gold or in convertible currencies, the problem of fluctuating rates is virtually negligible, even if the transactions themselves and not the balances are passed through the clearing system, and even if the unit of account is only an intermediate calculating device to enable the different currencies to be added and subtracted, and is not actually used in settlements. That, in broad outline, is what happens in the Central American Clearing House.

If liquidation occurs only at intervals - at the end of the month, as in the European Payments Union, the European Monetary Agreement and in the Triffin proposal, or every sixty or ninety days as under the ECLA schemes - an adjustment in the rate of one of the currencies during a liquidation period necessitates a separation of accounts, at least in so far as the currencies of different countries are actually used for settlement. With fluctuating exchange rates the problem may become inextricable if the transactions concluded in the various currencies of the participating States are passed to the clearing house in the form in which they have been made.

It is precisely the fear of variations in exchange rates that is one of the reasons for quoting transactions in a third currency, usually the dollar. In these circumstances, operators in the

country manipulating its currency receive, in exchange for their foreign currencies, amounts of their national currencies which vary either with the official rate or with the free-market rate.

The real purpose of clearing machinery may be to avoid a fluctuation of rates producing international repercussions, while limiting recourse to the use of gold or international currencies.

In this connexion, it may be interesting to describe the course of operations under the Triffin proposal.

At the beginning of the month, a country is credited with certain rights of withdrawal in the unit of account: it does not have to buy them with its own currency; it may, however, expand its account by purchasing additional rights with gold or with currencies convertible outside group. Its account is debited with the payments it makes and credited with those it receives. The various national currencies so far play no role in the system and their respective rates are only relevant to transactions between the national monetary authority - in practice, the Central bank - and the nationals of the country in question whose payments or withdrawals in units of account are settled at the current rate.

When balances are calculated at the end of the month they are in principle paid to the creditor country or by the debtor country in gold or in currencies convertible outside the group. Thus, the clearing system is not affected by rate fluctuations.

The stand - by credits made to participants - like their debts and their arrears of interest - are also expressed in the unit of account which is independent of any fluctuation in the exchange rate of their national currencies.

C. Balances outside the system

35. Mention must be made of the problems which may arise for a multilateral clearing system from the existence or appearance of balances outside the system.

36. When the European Payments Union was set up, the problem of accumulated balances made itself felt, particularly in connexion with Great Britain which was well aware of the leverage which an accumulation of sterling holdings by other European countries gave in the development of its exports. A compromise was reached in that Great Britain was compensated for the additional losses in gold occasioned by priority being given to some of its claims on Union fund by the liquidation of certain agreements resulting from the creation of the Union.

37. It is to be noted that a similar problem has been avoided in Latin America by the elimination of bilateral agreements. In any case, the problem would not have been so serious as in the case of a world currency like the pound, substantial quantities of which might be held for long periods in other countries.

38. The other problem which has been of particular concern to ECLA is that of the relationship between countries which make their mutual payments in gold or in convertible currencies and countries linked by bilateral agreements. The purpose of multilateral machinery, of course, is to get rid of such agreements and the distortion of exchange rates which they produce. ECLA proposed either that a ceiling be set to bilateral agreements, and that the parties should agree to the multilateralization of any sums in excess of the ceiling; or that successive blocks of bilateral balances be transferred to the clearing system. It is impossible to suggest that all bilateral credits should disappear, especially if they are linked with large orders for goods. Such cases are provided for under the European Monetary Agreement, which allows them to be settled by the clearing arrangements on condition of previous notification; they are cleared at the rate laid down in the agreement.

39. Once again it should be noted that the introduction of accumulated balances or of bilateral balances arising from special agreements between countries into a clearing system creates no genuine difficulties unless the net credit position of the countries affected by these balances triggers off a system of automatic credits. The position is quite different if the credits based on the balance within the regional system are of very short-term and if the assistance offered jointly by the member States of a clearing house is designed, as part of the operation of an agreed programme, to avoid a situation arising in which the global balance of one of the partners compels it to apply restrictions to the common market area that is being created.

CONCLUSION

Administrative organization and relationship with other institutions

40. The administrative organization required by an international clearing fund may be extremely small provided that only balances and not transactions are centralized, and that it works in conjunction with the Central banks.
41. Banks traditionally work for each other's account without charging for their reciprocal services. Centralized operations should be conducted at the Central banks. The operating costs of the European Payments Union, and of the resulting European Monetary Agreement, can be regarded as negligible; apart from salaries for staff and the cost of equipment, the bulk of the expenditure consists of the constant telephone calls and, when necessary, telegrams.
42. It should be perfectly apparent that there is no incompatibility between the establishment of a clearing house or of a Payments Union in Latin America and the fact that most of the countries concerned belong to the International Monetary Fund. The supplementary aid which a Payments Union can give is in no way restrictive: with the present situation in regard to capital resources in Latin America, it is indeed normal to have recourse, first of all, to external sources of capital and, in particular, to credits from the Monetary Fund. The multilateral credits between States belonging to the Union should be regarded as supplementary and as serving to avoid obstacles to the development of trade within Latin America.
43. Triffin suggests that the Monetary Fund might act as cashier in the same way as the Bank for International Settlements acts as cashier to the European Payments Union. And, just as the Treaty of Rome provides for mutual support between member States and a common approach to international organizations, particularly those capable of granting credits, so the Latin American States could express a common opinion regarding the needs of one of their number and any programme it intends to adopt. It would be advantageous for organizations such as the International Monetary Fund to deal with a body capable of analyzing and stating a case. It must, however, be decided what limits to set to the group of countries constituting the proposed Payments Union.

44. In any case the question will arise whether in order to facilitate effective implementation of the Montevideo Treaty, or even go beyond it, in the sense of setting up a real common market, the clearing machinery should be limited to countries which are members of ALALC or whether the system should be wider so as to promote the trade of all Latin America countries generally.

45. The ECLA schemes are based essentially on the establishment of a free trade area; the system of automatic credits should encourage States whose balances have been rendered positive by the policy of liberalization to speed up the abolition of obstacles to importation, and to provide incentives to preferential purchases within the zone, even at inferior conditions of price or quality. It has been shown that the first objective was limited to the full realization of a common market, and that the second was tantamount to a systematic organization for the diversion of trade. A system for avoiding hold-ups in the development of trade, involving discrimination in the form of special help given by a group of countries to one of its members, is only legitimate if it removes some obstacle to a process of economic integration and of combined development. This principle of mutual aid, therefore, is based not on an attempt to achieve a balance within the region, but on the desirability of preventing restrictions motivated by disequilibrium in the global balance of payments from extending to the whole region in process of integration. This second, more flexible and more economical conception leads equally to the conclusion that the establishment of a Fund capable of providing supplementary aid is a legitimate corollary to the Latin American free trade area.

46. Such a conception would not rule out a proper clearing arrangement embracing all Latin American countries, in units of account with interim payments in connexion only with end of month settlements.

47. The situation of the Central American States poses another problem for they are linked both by a common market and by a clearing house designed, as has been shown, to meet a different situation and whose machinery differs from the kind that would be needed for the wider scope of Latin America. It would, however, be perfectly conceivable that this Central American clearing house as such in place of the States it represents should be a member of clearing system covering Latin America.

48. This would lead to the idea of a payments union centred on ALALC with funds for stand-by credits or, if resources increase, for discretionary longer-term credits. In addition to full members, participating in clearing arrangements and in maintenance and administration of the funds as well as in the profit derived from them, there would be associate members comprising States temporarily outside ALALC, and the clearing house of Central American countries. These flexible links would make it possible to reconcile the efficiency and the generality of the system while at the same time taking to its limit the economic logic it has to serve.

CENTRAL BANKS AND REGIONAL AGREEMENTS ON
INTEGRATION IN LATIN AMERICA^{1/}

49. The fact that monetary co-operation is explicitly recommended in the General Treaty of Central American Economic Integration, but only referred to indirectly in the Treaty of Montevideo, is due in part to the differing purposes of the two treaties. At the same time it must be admitted that prior to the signing of the Treaty of Montevideo all efforts to reach at least one positive solution to payments problems in the contemplated free trade area had failed and that it had been relatively easy to secure the co-operation of the monetary authorities in Central America where currency was convertible and there was monetary stability. Thus in Central America efficient machinery exists for official and multilateral co-operation, whereas in the case of ALALC, national monetary authorities take only unilateral action in implementing the programme for integration.

50. Up to the present time the ALALC Central banks have taken the following, rather secondary, steps towards the objectives of Latin American economic integration:

- (a) participation by the central banks in the State bodies responsible for carrying out the obligations of the Treaty of Montevideo;
- (b) technical assistance for staff of issuing houses in preparing for the multilateral negotiations on tariff concessions, and for the actual negotiations which take place annually at the time of the conference of the ALALC contracting parties;
- (c) elimination of bilateral payments agreements in force in the area, or revision of those agreements in accordance with the spirit and the letter of the Treaty of Montevideo;

^{1/} Abridged version of a document submitted by Mr. Miguel S. Wionczek, Director of the Department of Information of the Latin American Centre for Monetary Studies, (CEMLA) to the Central Bank Technicians of the American Continent at their seventh session (Rio de Janeiro, October 1963).

- (d) monetary and exchange measures to promote trade in the area, or suspension of restrictive monetary and exchange measures introduced since the signature of the Treaty; and
- (e) establishment of agencies or branches of central banks in certain member countries of the Association.

51. The central banks of the member countries of the General Treaty of Central American Economic Integration have achieved much more solid success than those in the zone of ALALC; this is apparent from the efficient functioning of the Central American clearing house and by a certain measure of co-ordination of exchange policies operated by the various countries. It should be emphasized that in the view of participating countries, the clearing house has been a dynamic force in the area's accelerated progress towards the expansion of trade between Central American countries and towards the common market.

52. Nearly four years after the signature of the Treaty of Montevideo progress towards a solution of the payments problem and towards monetary, exchange and financial co-operation in the ALALC area may be described as negligible. In contrast to this stagnation, however, are the considerations relating to the theory of economic integration, the precise proposals formulated by experts of international repute and the growing concern of the governments of the area and of the private sectors in the member countries of the Treaty of Montevideo.^{1/}

^{1/} See, in particular, the joint declaration of the Presidents of Brazil and Chile (Santiago, 24 April 1963) which recommends member States of ALALC "to set up payments systems which, without impairing the convertibility achieved by member countries of ALALC, will promote the extension of intra-regional trade, the progress of measures for lifting restrictions and industrial co-ordination". See also the agreements of the Association of Chilean exporters (Santiago, 27 March 1963) and the Sixth Brazilian Conference on External Trade (Belo Horizonte, July 1963).

53. In any event, the view is emerging in certain quarters^{1/} that, in view of the extremely efficient international private banking systems which exist and of the fact that convertibility has been re-established in the area any multilateral payments agreement for Latin America would be useless; that, moreover, such an agreement would be detrimental to Latin America's financial relations with the rest of the world and to the situation of the ALALC members themselves, for it would automatically limit the convertibility of their currencies. It is worth noting that those who are opposed to the adoption of a regional payments agreement also seem to fail to grasp the need for monetary co-operation and co-ordination in Latin America.

54. These negative opinions will not be discussed in detail here. Another document submitted at the Rio de Janeiro Meeting by a well-known European expert^{2/} on economic integration problems shows that it is impossible to claim, in the abstract, that the idea behind any regional compensation system would be centralization and the abandonment of traditional banking methods, or to submit that its purpose would be to upset trade flows or to seek to reinstitute a policy, of control. On the contrary, according to this same expert it should be possible to envisage a system which could improve the fluidity and efficiency of regional payments, strengthen regional economic and financial co-operation and Latin America's situation in relation to the rest of the world, without having an adverse effect on the zone or on its relations with third countries.

1/ See for example the statement by Peru at the meeting on commercial policy and the Central Bank (Bogota, 1-6 April 1963) and contained in the document entitled Peru, Organizations taking part in the formulation and execution of commercial policy (ALALC/PG/I/di/16).

2/ Pierre Uri, The Problem of a Payments Union in Latin America (document submitted by the Latin American centre for Monetary Studies at the seventh meeting of Central Bank technicians).

55. The manifest absence of progress is due to a variety of causes. First of all, the Treaty of Montevideo, because it is the result of efforts to find a common denominator for the particular positions of the countries which negotiated it, can be interpreted in a number of ways - for example, as a commercial preferential treaty with very limited effects. Then, the proposals for solving regional payments problems which were made prior to signature of the Treaty of Montevideo, and which are still the centre of attack, were made in anticipation of a much more ambitious regional treaty than the Treaty of Montevideo. Moreover, most monetary authorities in the zone are preoccupied by urgent and difficult short-term problems. Last, and by no means less important, the ALALC machinery with its obligations and weaknesses has emerged in a region lacking experience in economic co-operation, composed of countries whose economies, independent of each other, have very long been linked with the economies of the world industrial centres. These factors may well explain the present situation, which is characterized by the fact that most of the ALALC monetary authorities refuse to define their position with regard to payments problems and monetary co-operation. The theory that the lack of progress in the direction desired, is probably due to the "wish not to adopt an idea which could be interpreted as a disagreement with international arrangements on monetary policy".^{1/} After all, the establishment of the European Payments Union did not provoke any irreparable crises in the relations of its member countries with international organizations, nor did the establishment of the Central American Clearing House and the monetary co-operation between its members have any adverse effects on the relationship between these countries and international bodies.

56. Now, in view of the fact that the obligations of the Treaty of Montevideo are only a starting point and not the final goal of the participating countries, that throughout the region there is increasing pressure to speed up the free-trade programme, that co-operation embraces industrial

^{1/} ECLA, Realizaciones y perspectivas en el proceso del mercado regional (E/CN.12/668), 18 April 1963, p.86.

policy and economic development policy and that the executive bodies of the Latin American Free Trade Association is gaining strength it can be asserted that if those objectives are to be achieved, a regional monetary system will have to be created. Such a system is necessary not only to facilitate payments for existing commercial transactions but also to protect the region from the possible danger of a reversion to bilateralism to make more rational use of the limited hard currency resources on which Latin America as a whole depends, and to establish a permanent institution in which the monetary authorities can collaborate in solving the problems of internal and external monetary policy, or at least exchange information on proposed measures which might impede attainment of the purposes of the Treaty of Montevideo and subsequent complementary agreements.

57. It would be a complete misunderstanding of the kind of problem facing Latin America to assume that the convertibility of currency achieved at the end of the last decade is permanent, or that it is guaranteed by supplementary liquidities obtainable from international sources. On the contrary, the external situation of Latin America as a whole^{1/} is still deteriorating; it can be gauged by the absolute level of gold reserves and foreign currency, by its share of total international reserves and by the proportion of its net external debt, which has returned very nearly to the levels reached between 1930 and 1940.^{2/}

58. It is obvious that such serious problems cannot be solved by the establishment of regional payments machinery, anymore than they can be solved by the co-ordination of monetary and financial policies. Nevertheless, whatever may be done to stimulate the ordered progress of development on a regional scale, Latin America's external position will have to be strengthened.

^{1/} Between 1953 and 1962 the participation of America (excluding Cuba and Venezuela) in world gold and currency reserves fell from 4.5 to 2.8 per cent. Simultaneously, the relationship between the reserves of the 18 Latin American Republics and their annual exports fell from 47.3 to 26.1 per cent.

^{2/} See the document "Recent changes in the external public debt of Latin American countries" submitted to the Rio de Janeiro meeting by Mr. Bardi Rao of the IBRD and ECLA document "External financing in Latin American development" (E/CN.12/649), Mar del Plata, May 1963, pp.211-234.

59. The extreme precariousness of convertibility in the region is illustrated by the extent and persistence of all sorts of monetary and exchange restrictions, which do not appear to be temporary, since they are now greater than when convertibility was restored in the region at the end of the nineteen fifties. As has been mentioned in the first part of this paper, the monetary authorities of the ALALC countries are certainly striving unilaterally to protect intra-regional trade against the effects of these restrictions. The measures adopted would however be far more effective if recourse could be had to sub-regional consultative machinery incorporated in a clearing system, whatever particular techniques that machinery might employ.

60. The extent to which the member countries of a regional payments system could make more rational use of their international reserves than they do at present would depend, of course, on the characteristics of the system and, in particular, on the intervals at which and the method by which clearing is carried out, on the extent and nature of credit facilities, and on the source and volume of the financial resources at the system's disposal. Even the most rudimentary clearing system, however, would make possible an undoubted saving of currencies within the area and would enable the stocks of currency now held by the Latin American Bank outside the region to be used for purposes other than the financing of intra-regional trade. Even if a very simple system were set up, based on monthly clearings in dollars or in gold, the advantages of such a system would be apparent, particularly in situations such as are caused by the seasonal fluctuations in commercial payments within ALALC which coincide with pressure on the reserves due to speculative movements.

61. Apart from the direct effects of a regional payments system, we must repeat once again that, in the absence of some such machinery, it will be practically impossible to achieve co-operation and co-ordination of the monetary and financial policies of member countries, a goal which can hardly be achieved by means of non-institutional contacts. It seems that the ALALC countries are on the way to attaining their first objective - closer contacts between monetary authorities in the region - thanks to the

establishment in May 1963 of the Consultative Commission on Monetary Affairs as an organ of the Standing Executive Committee of the Association. For the moment, however, apart from the fact that the executive organs of ALALC are in general very weak, the competence of the new Consultative Commission seems exceedingly limited, since it consists exclusively in carrying out "studies relating to the financial and monetary sectors of common interest to the contracting parties" and in preparing "such meetings as the Standing Executive Committee may convene".^{1/} The terms of reference of the ALALC Consultative Commission on Monetary Affairs do not even reflect the recommendations of the first ALALC Meeting on Commercial Policy and Central Banks held at Bogota in April 1963, at which it was stated that "effective formulae for the appropriate co-ordination of financial systems in the area so as to ensure the adequate and rapid economic development of the region are lacking".^{2/} Since, to achieve monetary and financial co-ordination, contacts must be established between the monetary authorities at the highest level, it is hard to imagine that a consultative technical commission can be an appropriate instrument for such co-operation.

62. In the light of the above, it seems that a regional payments system capable of speeding up the Latin American economic integration programme should be optional, in respect both of membership and of recourse to the facilities it offers. The machinery, however should remain open to other

^{1/} See Resolution 33 of the ALALC Standing Executive Committee (23 May 1963).

^{2/} See Agreement No.3 of the Bogota Meeting of the Latin American Free-Trade Association, Informe de la Primera Reunion Comercial y de Bancos Centrales y Similares, Doc. ALALC/P/I/dt 4, 5, April 1963, p.21.

members of the Association and even to Latin American countries which have not yet signed the Treaty of Montevideo. That Treaty provides for the conclusion of various types of agreement, and in particular, agreements on industrial co-ordination, which do not necessarily include all the countries in the region; so that an agreement between only three central banks of member countries for the multilateral clearing of payments would conflict neither with the letter nor with the spirit of the obligations undertaken by the ALALC countries. In this way, the problem arising from the fact that there are in the region a certain number of central banks which are interested neither in a given payments system nor in any other form of co-operation, could be overcome.

63. Secondly, admitting that the radical solution of the ALALC payments problem lies in setting up a suitable structure within which monetary authorities can collaborate more effectively on other aspects of the integration programme, perhaps the best starting point would be the establishment of a clearing system on the simplest possible lines.^{1/} The unhappy experience of the past leads one to think that the present impasse is, to some extent, the consequence of attempting to set up a very complex structure at the very outset.

64. Mutatis mutandis, the present situation in the matters discussed in this paper, is identical with that existing in the region prior to the signature of the Treaty of Montevideo - when Latin American economists were invoking theoretical arguments to demonstrate the necessity of achieving a regional agreement which, from the very start, would lay the solid foundations of a Latin American Common Market. However, as the situation was not then ripe for such a regional enterprise, a compromise formula

^{1/} Mr. Rodrigo Gómez, General Director of the Bank of Mexico, has recently proposed the extension of machinery similar to that of the Central American Clearing House to the whole region (see his statement at the third annual conference of Heads of Organizations organized by the Peruvian Institute of Business Management, Paracs, Peru (29 August - 2 September 1963)).

was found: The Treaty of Montevideo. As already stated, this Treaty is a long way from being an effective instrument of integration, but at the time it offered more promising results than the more ambitious formulae which were then unacceptable to most members of ALALC. Three years after its signature, the Montevideo Treaty is proving its utility. There are few people in Latin America now who predict its disappearance, but many who are convinced that it will be gradually transformed into an effective and dynamic instrument.

65. Those who think that integration cannot go forward without some form of payments system and some machinery for co-operation between the monetary authorities of the region, should bear in mind the lessons of the negotiations preceding the creation of ALALC and seek the simplest possible formula which any group of ALALC member countries can accept, and not allow themselves to be imposed upon by totally negative attitudes which, since they are negative, are incapable of leading to any compromise. To adopt such an attitude might appear cowardly, but it is nothing of the kind; it is merely to propose tactics capable of surmounting existing obstacles and to assume that, in one way or another, regional economic integration programmes for Latin America will continue to progress.

THE TACTICS OF FINANCIAL CO-ORDINATION^{1/}

66. There are excellent economic arguments in favour of Latin American integration which has on several occasions been described as the sine qua non of the continent's full development. There is no need to dwell on these arguments which are sufficiently well-known.

67. The best way of advancing along the road to integration is to establish a set of machinery to promote it, for regional trade liberalization is not on its own a sufficient stimulus. Of the many aspects of integration the financial is one of the most important. If, for instance, a country experiences balance of payments difficulties it may have to contrive to reduce its trade with the other countries of the region, to their detriment, thereby perhaps compromising integration itself; if these balance of payments difficulties arise despite the application of sound policies, those countries which really want to be integrated with the country concerned must help it financially. Even if there are no balance of payments difficulties, for trade to be buoyant there must, by definition so to speak, be abundant and easy institutional financing, which may be encouraged by co-ordination of the region's financial practices and machinery, by the harmonization or unification of financial legislation, etc. Co-ordination of the amount, orientation and localization of investments in the region is just as important, and co-ordination of policies and unification of the criteria applied by international financing organizations or other regional groups are equally essential; what the European Economic Community has already adopted must be applied in Latin America.

68. The problem of financing may be distinct from that of co-ordination, but the Latin American countries are so unaccustomed to co-ordinating their policies that it would seem wise to encourage them to do so by a financial system. Hitherto, when applying to the IMF, for example, Latin

^{1/} Abridged version of a document submitted by Dr. Javier Marquez, Director of the Latin American Centre of Monetary Studies the Central Bank technicians of the American continent at their seventh session Rio de Janeiro, October 1963).

American countries have used their own contributions to that fund or foreign capital in the region, so that bad use of these resources affects the drawer country or the (non-Latin American) countries whose capital is used. It is utopian to believe that any Latin American central bank would be willing to relinquish any of its reserves if it thought they might be put to ill-considered use. Thus, while balance of payments equilibrium is desirable - or essential - it would be easier to apply the requisite policy if the means of financing deficits were derived to a greater or lesser extent from the Latin American countries themselves and if those same countries also decided how those means were to be apportioned, for prudence in financial management would result in the borrowers being required to apply policies favourable to long-term stability ensuring the viability of regional economic integration.

69. It is interesting to note that in international liquidity the United States is now resorting to arguments hitherto invoked by Latin America only. Thus, a study made by the Brookings Institution at the request of the economic advisers of the President of the United States concludes that the only way to ensure that full employment is not subordinated to balance of payments considerations is to set up a new international financial system, for the discipline of the traditional system imposes restrictions even when the domestic situation calls for expansion. (If the word "employment" is replaced by the word "development" and the words "United States" are replaced by the words "Latin America" similar ideas can be found in many Latin American writings and speeches).

70. Nobody denies that the resources of the IMF are more than adequate to meet the short-term needs of Latin America's balances of payments; the difficulty does not lie in the volume of financial resources. The IMF would also have sufficed for the European countries, but they nevertheless established the European Payments Union, whose justification lay in the manner and ease with which it was able, at any time, to supply essential foreign exchange. Member countries' balances of payments have not yet required this machinery to be put to full use but the possibility of a state of affairs necessitating wider recourse to it is not excluded.

Finally, the fact that one institution possesses financial resources is not sufficient reason for refusing to establish others, for it might be advantageous to be able to apply to several lenders. When the establishment of the Inter-American Development Bank (IADB) was being discussed some people maintained that the IBRD was sufficient to finance all deserving Latin American projects. The IADB was established however and was followed by the Central American Bank for Economic Integration, and Latin America was able to obtain long-term loans from all these institutions which, in the case of multiple projects, quite legitimately apply different criteria.

71 The establishment of new financing machinery doubtless reduces, to a certain extent and in a certain sense, the relative importance of existing institutions, a fact which perturbs all those who think that only the existing institutions are capable of stimulating a sound policy and that the establishment of new institutions is liable to give rise to trouble. This might be the reason for the attitudes adopted when there is talk of a new payments machinery in Latin America.

72. The establishment in Latin America of clearing houses, with provisions concerning credit, or of payments unions is a subject charged with emotion. As a matter of fact, opposition to this idea is so stubborn and so passionate (however moderately it may be expressed) that technical arguments will not on their own prevail against it. Some people do not want the question even discussed while others want it buried as deeply as possible and covered with a thick layer to prevent it re-surfacing. When, despite all, the subject does re-surface - which happens suspiciously often - those who want it to remain buried argue that the idea is completely valueless and that the history of similar systems proves conclusively that some of its features - features which it does not contain - are dangerous. This opposition group never stops to wonder whether it might not be possible to improve the proposed machinery or in what form it might be useful; they ask rather in what circumstances, under what aspects and in which technical details a concrete project is useless or harmful and hence vulnerable to attack. One and the same person has sometimes been

heard to say that such machinery would serve no purpose, that it would not work and that it would, moreover be harmful. It is, however, hard to imagine how it could be harmful if it did not work. The important thing is to attack the idea.

73. There is indeed too great a tendency to imagine that what is intended is a certain type of machinery which, inevitably it appears, springs to the mind of many people who, quite rightly, reject it. In other words, it is thought that the payments union is machinery for automatic and solid credits, that its use inevitably leads to exchange control, in which some countries are always debtors and others quite unwillingly always creditors and that it is a means of securing "reciprocity", i.e. balanced trade and payments within the region. If indeed this were the sort of system a payments union implied the idea would be very hard to defend. To the extent that it is impossible to avoid associating the idea of a payments union with such a monstrosity, those in favour of a separate payments machinery would do well to seek another name.

74. A recent study by the IMF secretariat, which has been submitted to this meeting, sets out the results of an enquiry made in Latin America and shows that in our region the above-mentioned association is very widely accepted, that in many Latin-American quarters there is a manifest lack of understanding of the subject and that in consequence the task of defining the ideas is considerable. It is hard to know which is the more incredible, the incomprehension of those in favour of the idea or the incomprehension of those opposing it.

75. I am interested (for several reasons already mentioned) in such a system mainly, but not exclusively, as a co-ordinating body. No one will accuse me of wanting capital to be granted to Latin America to re-establish a balance of payments the disequilibrium of which is the inevitable result of an unconsidered financial policy or a policy of inflation (whether it be structural or cost). I do not want these additional resources, which add to the region's or countries' external debt without contributing to development, to come from the IMF or from a specific Latin American organization; but I do believe that we can obtain from a new organization as

much (although perhaps of a different kind) prudence as the IMF wishes to introduce while at the same time establishing or proposing an extremely desirable financial co-ordination machinery if a part of the resources to be employed were Latin-American.

76. Finally, one of the facts most favourable to a meeting leading to co-ordination is that the countries are motivated by a financial interest, either as borrowers or as lenders. Although conditions are not yet ripe for achieving co-ordination through an organization for payments or for the financing of temporary balance of payments deficits by means, in part, of the resources of the countries involved, such an organization is by no means the only financial machinery to set in motion a process of financial co-ordination in Latin America. That is why I am interested in some of the misunderstandings which have come to light about the setting up of clearing houses or payments unions in our region.

77. I am thinking more particularly of the fact that some people seem to be convinced that machinery designed to increase international liquidity or facilitate payments also increases directly or through central banks, the volume of resources (foreign currency) available to exporters, importers and commercial banks. Certainly, neither clearing houses nor payments unions have this effect, but would machinery which, to a certain extent, had this effect and which in addition rendered other services be cumbersome?

78. There is an organization in which, from this point of view, I am extremely interested: the Bank for International Settlements (BIS). In July 1944 the final declaration of the Bretton Woods Conference recommended its liquidation. After hostilities, however, it was decided that it should be maintained because it was recognized that it would not duplicate the work of the IMF or the IBRD but rather usefully complement those two institutions since the IMF and the IBRD are universal in character while the BIS is a purely European institution.^{1/}

^{1/} Which does not exclude working relations with countries outside the European region.

79. This, in other words, is an institution which works with central banks, which is independent, which is useful, which does not embarrass the IBRD or the IMF for it neither obviates their functions nor restricts their powers, which affords financial assistance of various sorts to its member countries and which, in particular, is a meeting centre and an instrument of co-operation for central banks.^{1/}

80. An interesting point in this connexion is that the BIS charter is vague so that it can extend its activities or adapt them to circumstances or the requests of its members; it may also serve them as "joker", this obviating the establishment of new institutions for purpose which, if independent of each other, would only develop international bureaucracy without contributing any advantage. What it has done and what it is doing merit brief if not detailed mention.^{2/}

81. In principle and technically its operations are short-term. Sometimes, however, it effects operations of considerable scope with more than short-term maturities, but it always jealously guards its statutory liquidity, mainly through the long-term deposits entrusted to it. From its early days it has granted "emergency credits", particularly during the great economic crisis (to Hungary, Austria, Germany and Yugoslavia). It has organized central bank syndicates in which it participates financially.

82. The centralization in it of a part of the international reserves of central banks allows it to make payments by simple ledger entries, resorting as little as possible to markets so as not to disturb their equilibrium.

1/ The close co-operation existing today between the IBRD and the BIS is evidenced by the fact that the latter has contributed to raising the former's first loan in Swiss francs and, if necessary, discounts the maturing securities held by the IBRD as a result of its loans. I have never heard that there was any friction between the IMF and the BIS following the intention to abolish the latter.

2/ The following paragraphs are based on the study by Roger Auboin entitled The Bank for International Settlements, 1930 - 1955, Essays in International Finance, Princeton University, No.22, May 1955, and on the annual reports of the BIS.

It was even hoped to establish what was called "a foreign exchange clearing system" and an attempt was made to unify the various currencies quoted for operations involving different currencies. The bank may grant commercial loans, by means of credits obtained from a central bank in the currency of that bank, compensated by credits in gold or in another currency. These credits offer a commercial financing method combined with a foreign exchange guarantee, contributing to make up for the absence of a forward market for a large number of monetary relations. In reality the BIS methods are directed towards a foreign exchange arbitrage increase mainly in the form of sales of gold or cash foreign exchange combined with forward purchase liabilities. These methods are explained by the fact that in most cases the BIS's operations are the consequence of seasonal imbalances, of the need to revise maturities, or of other temporary situations.

83. In the annual reports of the BIS, there are chapters on the Bank as Trustee and financial agent for public international loans (which was its initial function), on the Bank as agreed third party under the trusteeship agreement concluded with the High Authority of the European Coal and Steel Community, and the Bank as agent for the European Organization for Economic Co-operation and Development (European Monetary Agreement). This clearly shows the variety of roles which the Bank may fill.

84. The creation of the IMF has not, of course, reduced the value of the BIS to European countries, and the very favourable balance of payments position of many of those countries has not restricted, but rather increased, the transactions of BIS with central banks whose reserves are growing. The BIS is seldom referred to as a financial power; nevertheless, at the end of March 1963, European central banks had Fr. Sw. 4.057 million on deposit with it and other clients Fr. Sw. 504 million. No European central bank has ever regarded those deposits with the BIS as being in the slightest danger, although BIS conducts operations with countries which have never been regarded as models of financial virtue. At the date mentioned above, its investments amounted to Fr. Sw. 2,429 million.

85. It follows that the BIS is a very active institution and that its activity does not depend on the existence of balance of payments difficulties. Would it not be possible for European countries (or their central banks) to carry out the same operations without the BIS? Certainly it would - provided that non-European countries carried them out. But it is convenient for countries to have recourse to specialized international machinery even if their external accounts cause them no worry. The Director of a European central bank once made some interesting remarks: Too much publicity, he said, was given to the operations of IMF; too many people were informed, which sometimes led to speculations which were not justified by the operation contemplated, and the same situation could arise if a central bank were operating directly on the national or international market; but if such an operation were carried out by the BIS, or by its intermediary, it would remain absolutely secret, since the BIS acts like a bank in the strictest sense of the word. The annual reports and balance sheets published by the BIS make no mention of the source of deposits or of the beneficiaries of its operations. Moreover, very short-term operations, like those of the IMF, are very costly owing to the 1 per cent commission which, under the Statute, has to be charged on all transfers.

86. Far from being harmful, the great financial activity of the BIS has been favourable to its function as an instrument of co-ordination between European central banks. Would not the introduction of a similar system be a good start in setting up co-ordinating machinery in Latin America - apart from the advantages it would provide as a supplementary source of finance for Latin American trade?

87. On the basis of experience with the BIS, it would be impossible and undesirable to attempt to foresee the precise financial functions that a similar institution in Latin America might perform; in the same way, it would be undesirable to invest such an institution at the outset with all the functions that might be foreseen for it, even if it were evident that some of them already existed. A concrete example is supplied by the fund set up by the Inter-American Development Bank to finance Latin

American exports of capital goods at medium-term. There is no doubt that the reason why this fund was set up within the IADB was that it was the only existing financial institution which could do the job and which possessed the resources. Nevertheless, that was a role quite foreign to the purposes of the IADB.^{1/} Nothing, of course, would have justified the establishment of a new institution to take over the medium-term financing of Latin American exports of capital goods, but if what is required is an organization for co-ordinating policies involving several (or very many) types of financial operation, this medium-term financing might well be one of them.

88. Other such functions could be imagined; the proposed institution might support various sectors of export market. I have in mind the protests of the less-developed countries of the region, which are themselves exporters of various types of goods, when the machinery just referred to was set up. They wanted it to cover other types of export, if necessary at shorter term. Could not our proposed co-ordinating institution also play a role in creating a market for bank acceptances in Latin America? This idea is prompted by those protests to which I have just referred, since a bank acceptance is an ideal instrument for the short-term financing of foreign trade. The creation of such a market has already been suggested and the subject will shortly be studied at the Bankers' Conference which CEMLA is to convene at Bogota, to examine methods of stimulating the relationships between Latin American banks. The working document

^{1/} In a lecture given at the University of Chile on 22 May 1963, Mr. Felipe Herrera, President of IADB, commented that: "Originally, the Bank would have preferred that a new fund, specially designed for this new activity on which IADB is about to launch, be set up. But in view of the difficulties and servitudes involved in obtaining the necessary resources, I think that, all in all the step which has been taken offers excellent prospects of success. But in employing this machinery for stimulating the export of capital goods, one must never lose sight of the fact that the Bank is an investment bank, a development bank, and not a foreign trade bank"..

on which the examination of this point will be based, and which contains many valuable ideas as to how the scheme might be carried out, also suggests that the banks in each country, with the participation of the Central Bank, create a joint fund or "pool" of capital for the purchase of first-class acceptances. I see no reason why this idea should not be extended to Latin America, with a capital pool centred in an organization of the type we have been discussing, which would become a centre for the re-discount of acceptances originating in intra-Latin-American trade.

89. A wealth of ideas for an analogous Latin American organization is to be found in the types of administration and investment operation now conducted by the Basle Bank (BIS) and other banks, which would serve as a basis - or, if you prefer, as a pretext - for Latin American financial co-ordination which I regard as a sine qua non if integration is to be developed on solid foundations.

Summary

90. Integration can mean more rapid development for the Latin American countries; but there can be no integration without the co-ordination of policies, and in particular of financial policies, at all levels. Financial co-ordination would be facilitated if embodied in organic systems which necessitate it.

91. Though it can be argued that co-ordination and international finance can be separated, co-ordination is more likely to be achieved if the two functions are united for certain financial operations in an international organization. Financial operations can stimulate co-ordination if the latter is dependent on them and, above all, if some of the means of finance are themselves Latin-American. In other words, if financing is to any extent carried out with regional financial resources, and if the countries supplying them must decide when, to whom, and to what amount loans are to be given, it is probable that they will apply pressure to borrowers to adopt "sound" policies, so that risks may be reduced.

92. The international organizations which exist today and provide for the financing of temporary deficits in payments balances - i.e., above

all, the IMF - possess more than adequate resources to meet the legitimate needs of Latin American countries in this field. But it by no means follows that it might not be valuable to possess, in addition, special machinery with different, but equally sound, criteria, and which might increase the resources actually supplied by IMF, while applying the same or different criteria.

93. It is very probable, however, that the situation in Latin America is not yet ripe for the establishment of financial collaboration on the scale which would be desirable; it is therefore a question of finding other financial functions of interest to the region which, at the same time, would serve to stimulate co-ordination. That this is possible is shown by the many types of operation by which economic relations between Latin American countries are now financed, which have nothing to do with balance of payments difficulties, which involve no exceptional risk even where such difficulties exist, and which may, to some extent, contribute to relieving them by expanding trade. The operations of the Basle Bank for International Settlements show that these other methods of financing are convenient, whatever the balance of payments position of a country may be; they also give some indication of the variety of possibilities for regional financing in Latin America.

94. The transfer to a co-ordinating organization of the function, at present undertaken by the Inter-American Development Bank, of providing medium-term finance for the export of capital goods can be regarded as an immediate possibility. Similarly, one can imagine that such an organization should adopt the idea recently put forward of the creation of a market for bank acceptances in Latin America, by creating a fund to absorb bank acceptances for which national banking organizations do not wish to take responsibility.

95. Experience and the progress of integration would certainly open the way to further activities, and the mutual confidence created by the establishment of such an organization and the desire that would be aroused to extend possibilities of having recourse to it would bring about the co-ordination which is indispensable to integration.