

AGENCY FOR INTERNATIONAL DEVELOPMENT  
WASHINGTON, D C 20523  
BIBLIOGRAPHIC INPUT SHEET

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**Batch 68**

1. SUBJECT  
CLASSI-  
FICATION

A. PRIMARY

Development and economics

DE10-0000-G570

B. SECONDARY

Banking and finance--Asia

2. TITLE AND SUBTITLE

A regional payments union for south and southeast Asia

3. AUTHOR(S)

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4. DOCUMENT DATE

1965

5. NUMBER OF PAGES

45p.

6. ARC NUMBER

ARC

7. REFERENCE ORGANIZATION NAME AND ADDRESS

Wis.

8. SUPPLEMENTARY NOTES (Sponsoring Organization, Publishers, Availability)

(In Economic interdependence in southeast Asia project. Working paper)

9. ABSTRACT

10. CONTROL NUMBER

**PN-AAE-376**

11. PRICE OF DOCUMENT

12. DESCRIPTORS

Balance of payments  
Economic integration  
Payment systems  
Regional planning

South Asia  
Southeast Asia

13. PROJECT NUMBER

14. CONTRACT NUMBER

CSD-355 Res.

15. TYPE OF DOCUMENT

AID/OSD-355 RES.  
ECON. W

A REGIONAL PAYMENTS UNION FOR  
SOUTH AND SOUTHEAST ASIA

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The University of Wisconsin - AID Research Project  
"Economic Interdependence in Southeast Asia"  
Draft of Working Paper

July 1965

The decline and fall of the gold standard which was precipitated by the depression of 1929 has brought into prominence the question of mechanisms for adjusting international balances of payments. In other words, since the prime concerns of monetary policy have become the domestic objectives of full employment, growth, and stability, the almost "automatic" attainment of equilibrium that existed under the traditional price-specie-flow mechanism is no longer possible. The often-faced conflict between the objectives of growth and internal equilibrium, on the one hand, and external equilibrium, on the other, has resulted in a search for "new methods" for adjusting income and outgo--for example, trade restrictions, exchange controls, and exchange rate variations.

The use of such methods to fight balance of payments difficulties has been questioned by all those striving for international economic cooperation, whether global or regional. The balance of payments policy has become one of the liveliest issues in the growing literature on regional integration--international economic cooperation on a limited scale. In the existing framework of the European Economic Community, the European Monetary Agreement represents an attempt to create equilibrating variables that would facilitate the process of balance of payments adjustment among the participating countries. The European Payments Union (which existed from 1950 to 1958), in itself an attempt at regional cooperation, was an institutional device designed to tackle the balance of payments problem; it eventually facilitated deeper regional integration, as can be witnessed today. The regional approach to balance of payments problems taken by

the Latin American countries participating in the free trade area arrangement has also been a topic of current discussion and wide interest. And in the recent consideration of regional economic cooperation among countries of Asia, balance of payments problems have figured prominently. The Economic Commission for Asia and the Far East (ECAFE) has advocated the creation of some kind of payments union as an integral part of a free trade area arrangement or whatever other measures of trade liberalization might be adopted by the countries of Asia.<sup>1</sup> The proposal has not attracted the attention it deserves, nor is it spelled out in any detail.

This paper addresses itself to the task of examining the nature and rationale of a regional payments union and its possible application for the countries of Asia. Section II focuses its attention on some of the implications of a free trade area arrangement, particularly for the balance of payments policies of the participating countries and the experience with these problems of sections within one country. Section III discusses James Ingram's proposal for financial integration among a group of countries, which takes its inspiration from the mechanism for adjusting balance of payments among sections of a country. Section IV spells out in some detail, on a theoretical level, an alternative approach: a regional payments union. Finally, Section V examines the problem of applying a regional payments union to the countries of South and Southeast Asia.

## II

The recent literature on regional integration asserts that the broadening of the market on a regional basis leads not only to a more efficient utilization of the resources of the participating countries—the stock

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1. United Nations, "Approaches to Regional Harmonization of National Development Plans in Asia and the Far East," Economic Bulletin for Asia and the Far East (December 1964).

argument of the free trade advocate--but also to indirect and non-economic benefits<sup>2</sup> which in the long run assume greater importance. These consist of the stimulus to entrepreneurial activities, innovations, creation of new investment and new products, development of new skills, more advanced training, etc. It is these indirect effects that become the truly dynamic elements of development.

The beneficial effects (direct and indirect) of a customs union will ultimately arise from changes in the nature, scale, and geographical distribution of the region's various manufacturing and other economic activities, which can be achieved by influencing the investment decisions of its entrepreneurs. Since investment decisions are long-term in nature and are based on expectations of production for and sales to the larger regional market, entrepreneurs will need a guarantee that the customs union or free trade area, once established, will continue to exist--in other words, that the emerging pattern of intra-regional economic relations "will no more, or not for a long time, be disturbed or disrupted by trade restrictions, exchange control, or exchange-rate revision."<sup>3</sup> In the context of the European free trade area and its balance of payments problems, Meade observes that the interference of import restrictions on intra-regional trade

... with the free-trade principle is not to be measured merely by the amount of restriction of imports which actually exists at any one moment of time. The mere knowledge that trade may be restricted in this way in the future will discourage the large-scale investments that may be necessary to build up localized specialized mass production for the whole European market. The mass production of motor

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2. Scitovsky deals with the importance of these effects bearing upon "the economic behavior of governments, entrepreneurs, workers, and others." See Tibor Scitovsky, Economic Theory and Western European Integration (London: George Allen and Unwin, 1959).
  3. Ibid., Ch. II, "Theory of the Balance of Payments and the Problem of a Common European Currency." Scitovsky makes this point in the context of Western European integration.

cars in Detroit in the United States involves the investment of huge sums of capital in plant and equipment in Detroit, which is undertaken because the producer knows for certain that the whole United States market will always be freely open to him.<sup>4</sup>

The possibility of fluctuating exchange rates will also deter the producer from undertaking large-scale investments to provide for the larger regional market, because, for example, the depreciation of a member country's currency is equivalent to tariff imposition in its effects on the producer.<sup>5</sup>

Controls over international transactions in the form of trade and exchange restrictions or exchange rate variations are all means by which balance of payments difficulties may be solved. If the use of these means is to be ruled out, as has been argued above, an alternative method must be found. The gold standard technique, or the "classic monetary policy," as Scitovsky calls it, is yet another means of adjusting balance of payments. The price effects (the classical interpretation of the gold standard) and income effects (Keynesian and post-Keynesian interpretation) of changes in the money supply, arising from changes in gold flows in response to external surplus or deficit, are expected to restore balance of payments equilibrium. But the acceptance of the more important objectives of monetary policy—growth, full employment, and domestic stability—rules out the use of monetary policy solely to achieve external equilibrium. More often, policy-makers find it hard to reconcile these objectives and make the obvious choice of growth and stability.

This is not to deny the existence of automatic forces which tend to restore equilibrium in the balance of payments. Even when the money supply is not tied to gold flows, the very cause of balance of payments

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4. J. E. Meade, "The Balance of Payments Problems of a European Free Trade Area," Economic Journal (September 1957), 388.
  5. Discouraging effects of exchange rate variations on the type of investment required for larger markets are also noted by Paul Streeten, in Economic Integration—Aspects and Problems, 2nd ed. (Leyden: A. W. Sythoff, 1964), p. 73.

deficits can, in certain circumstances, release equilibrating forces. For example, a decline in exports will lead to both payments deficits and reductions in income. The latter, in turn, bring about reduced imports, through the foreign trade multiplier. However, these forces will not be strong enough to entirely bridge the payments gap. (Besides, the decline in imports will reduce the exports of other countries and may lead to declines in their income and imports.) Also, the country's income reduction is very likely to be neutralized by its stabilization program. As an alternative, the country's foreign exchange reserves, over and above the minimum required to cover the domestic money supply, can perform an equilibrating role.

The forces adjusting balance of payments operate with greater ease between various sections in one country than between countries. For example, movements of short-term funds and mobility of capital and labor are more effective in correcting temporary payments disequilibria.<sup>6</sup> The flows of commercial and financial funds and of the Treasury mainly determine a section's balance of payments. The former are comprised of receipts and payments from financing intersectional trade, a section's payments to and from the central bank, and movements of capital funds between sections. The latter include the purchase and sale of government securities, taxes, and government expenditures and assistance. Some of these flows have great equilibrating potential. Movements of marketable financial claims--for example, sales and purchases of government securities--can compensate for the loss and gain of reserves on the part of the banks in the deficit and surplus sections, without affecting their money supply.<sup>7</sup>

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6. Bela Balassa, The Theory of Economic Integration (Homewood: Richard D. Irwin, 1961), pp. 252-53; and Scitovsky, op. cit., p. 80.

7. The availability of such financial claims as government securities, however, presupposes surplus earned in the past, as is true of countries' foreign exchange reserves when they play an equilibrating role in the adjustment of international balance of payments.

Since the availability of such marketable claims will be limited, only temporary disequilibria can be financed in this way.

The same may not be true of government taxes and automatic transfers, which can exert equilibrating as well as disequilibrating influences. Should a section develop a deficit from a decline in exports, a reduction in federal taxes and increases in unemployment benefits will help it. At the same time, higher tax payments will aggravate the balance of payments problem of a thriving section whose deficit has arisen because of import surpluses originating in a rise in incomes. Nonetheless, the role of government expenditures and special assistance has great equilibrating potential. Government expenditures in Southern agricultural sections of the United States in the thirties prevented a decline in income and consumption there and helped to maintain their balance of payments equilibrium.

The policies of the federal government implemented by the financial activities of the Treasury caused their reserves to be replenished, making it possible for them to maintain a balance of payments equilibrium, and also a certain level of consumption. Without such transfers, the loss of reserves to which they would have been subject, would have forced agricultural districts to undergo a severe deflation of purchasing power and incomes at a time when they were suffering a greater deflationary pressure than the rest of the country.<sup>8</sup>

To some extent, the migration of people from agricultural to industrial sections, where real incomes were higher, also acted as an equilibrating force.<sup>9</sup>

Temporary balance of payments maladjustments among the sections of a country may also be corrected more easily under the system of branch banking on a national scale, rather than the unit-bank system. The reserve

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8. Penelope Hartland, "Interregional Payments Compared with International Payments," Quarterly Journal of Economics (August 1949), 406.

9. Ibid.

losses of banks in one section can be replenished through funds lent by their counterparts in those sections experiencing payments surpluses.

With regard to the role played by the mobility of long-term and short-term capital and of labor in maintaining equilibrium more easily in intersectional balance of payments than in international balance of payments, Hartland concludes:

... the successful operation of the interregional gold standard within the United States during the period which saw the collapse of the gold standard internationally, seems to be best explained in terms of factor mobility: the fact that people moved freely between agricultural and urban localities in this country and especially the fact that the capital was given greater mobility by the activities of the federal government. The mechanisms of adjustment available to any economic region for meeting a balance of payments disequilibrium (given fixed exchange rates) lie in an income change, a population change or a capital movement. The more the adjustment is made via factor movements, the smaller will be the necessary adjustment of income.<sup>10</sup>

A similar view is also expressed by J. C. Ingram: "... the evolution after 1900 of a large body of nationally marketable financial claims, coupled with freedom of capital movements, may have provided an important part of the easy payments adjustments in the United States."<sup>11</sup>

In the case of balance of payments adjustments between countries, foreign exchange reserves do play an equilibrating role, as noted earlier, if the disequilibria are temporary. Although it has been maintained that differences between inter-country and intra-country settlement mechanisms are observed with regard to the currency system, rules on reserve requirements, and monetary and fiscal policy,<sup>12</sup> this is not entirely true. The

10. Ibid., p. 407.

11. James C. Ingram, "A Proposal for Financial Integration in the Atlantic Community," in Joint Economic Committee, Congress of the United States, Factors Affecting the United States Balance of Payments (Studies) (Washington, 1962), p. 199.

12. Balassa, op. cit., p. 257.

fact that the sections of a country such as the United States have a common currency does not guarantee equilibrium in intersectional balance of payments. The receipts and payments of a section or country are determined by its productivity, as compared to that of other sections or countries, together with the nature and level of demand. The use of a common currency among the sections of a country does not mean that a section running a deficit will not lose reserves, any more than would the use of one currency among all the countries of the world prevent a nation with a deficit from losing reserves. As has been argued by Hartland, "For all practical purposes, so long as there is free convertibility of one currency into another, the gold standard supplies a unified currency, but this fact is not sufficient to ensure international equilibrium."<sup>13</sup>

As for the application of homogeneous monetary and fiscal policies within a country, as opposed to the lack of it among various countries, homogeneous policies imply not only that every section of the country is subject to the same policy-making authority, but also that the policy decision of that authority do not discriminate among the different sections. Hartland maintains that this is not wholly true of a country such as the United States. For example, the Federal Reserve Board, in requiring different reserves in different sections, practices a non-homogeneous monetary policy. In any event, the application of homogeneous economic policies does not affect the different sections in the same way.<sup>14</sup> On this point, Hartland cites many examples from the experience of the United States<sup>15</sup>

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13. Hartland, op. cit., p. 394.

14. Balassa admits this fact (op. cit., p. 258).

15. Most of the regulations of the Securities and Exchange Commission apply implicitly or explicitly to the New York Stock Exchange alone. Changes in these regulations thus produce far greater impact on the economy and the balance of payments of the New York Federal Reserve District than on any other. Because of different minimum reserve requirements for different sections, changes in the requirements introduced by the Federal Reserve Board would have a different impact on

and concludes that "regional equilibrium in the United States cannot be explained in terms of homogeneous economic policy, even on the national level."<sup>16</sup>

Thus, the existence of a common currency and the adoption of homogeneous economic policies do not adequately explain the differences in intersectional and international balance of payments adjustments. They can probably best be explained by the equilibrating potential of short-term capital flows, in the event of temporary disequilibria, and of higher mobility of labor and long-term capital, in the event of persistent disequilibria, among the sections of a country. Government activities, as indicated above, can favorably influence such movements and mobility as may exist. As Scitovsky points out, the contrast between intra-national and international trade is "due to political and economic institutions and mental attitudes present in the one, absent in the other case, and responsible for the existence and the functioning of these automatic equilibrating forces."<sup>17</sup> Such forces for adjusting balance of payments can be deliberately developed through institutional devices.

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various sections, such as Boston and New York. The Federal Reserve Board also pursues a non-homogeneous sectional policy with regard to regulation of discount rates. Certain percentage changes in discount rates uniformly applied on a national level will produce varying effects on different sections' balances of payments. Agricultural policy aimed at supporting the price of a certain crop will affect the sections producing that crop in one way and those buying it in another. Thus, even homogeneous (i. e., national) economic policies will give rise to different effects in different sections, and the sectional differences in policy results are sometimes a matter of degree and sometimes a matter of kind. On the other hand, economic policies are often far from homogeneous. See Hartland, op. cit., pp. 395-96.

16. Ibid., p. 395.

17. Scitovsky, op. cit., p. 80. The reference to economic institutions has nothing to do with the common currency and homogeneity of economic policies observed within a country, as is argued above.

## III

J. C. Ingram proposes such a scheme for the developed countries of the Atlantic community:<sup>18</sup> the financial integration of their capital markets,<sup>19</sup> which would mean complete freedom for individuals, firms, banks, and government agencies to trade in securities and other financial claims across international boundaries. This would permit capital movements to perform an equilibrating role in adjusting balance of payments and thus relieve the burden on gold and/or foreign exchange reserves and reduce the scope and severity of countries' balance of payments crises.

After a transitional period, during which financial integration comes into existence, the assets of various financial institutions in the several member countries would be expected to intermingle. In other words,

French insurance companies would hold sizeable amounts of United States, Italian, and Danish securities; U.S. pension funds would hold British consols and German bonds; and the assets of individuals, corporations, commercial banks and savings and loan associations, and other holders of financial assets in each nation would include securities and other claims on a variety of nations.<sup>20</sup>

The author of the scheme does not consider the transitional period in detail, focusing attention on the modus operandi of such an integration, but he points out that an intermingling of financial assets does not necessarily involve net capital movements from one country to another and, hence, gain or loss of foreign exchange reserves on the part of a given country.

18. Including the United States, the United Kingdom, France, Germany, Belgium, the Netherlands, Luxembourg, Italy, Norway, Sweden, Denmark, Switzerland, Portugal, Austria, Turkey, Greece, and Iceland.

19. Ingram, op. cit., pp. 177-207.

20. Ibid., p. 191.

Once integration is attained, capital movements of an equilibrating character and in sizeable amounts can be expected to restore equilibrium in the countries' balances of payments. A nation like the United States can cover its external deficit by selling its domestic dollar securities, which financial institutions and individuals in other countries would be willing to hold if they are made attractive, or by liquidating the financial claims on other countries which are held by U.S. government agencies, commercial banks and other financial institutions, and individuals. If domestic securities are sold, small changes in their yields, which can be brought about through adjustments in interest rates, would be sufficient to attract foreign buyers.

For national securities and bonds to become internationally acceptable claims, and for such claims to perform adequately the task of restoring equilibrium, the scheme envisages rigidly fixed exchange rates; elimination of restrictions, including de facto controls on all international transactions on both current and capital accounts; and measures to standardize quality ratings, registration procedures, and methods for service and redemption of securities. Given these conditions, suitable changes in monetary policy, i. e., in interest rates, would be required to evoke the capital movements necessary to restore equilibrium in the balance of payments. This would curtail a country's autonomy in deciding monetary policy, as it will have to be geared to balance of payments considerations, which would require the government to rely more heavily on fiscal policy to combat domestic inflation and recession.<sup>21</sup> Ingram argues that in today's world, where countries—at least the developed ones—are fairly closely tied

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21. Greater reliance on fiscal policy might lead to larger payments deficits, given the freedom of international transactions. Ingram probably considers such a possibility very remote, because the government will use its claims on foreigners before it takes drastic monetary measures to sell more of its own assets on external markets.

by trade and convertibility, they already are unable to set domestic interest rates exclusively in accordance with domestic policy. To quote him: "...under the present system, nations suffer the disadvantages of interdependence of interest rate structures, but do not enjoy the full benefits of sensitive, equilibrating capital movements."<sup>22</sup> He further asserts that financial integration does not require either a common currency or a supranational monetary authority.

In short, Ingram's proposal seeks to increase the equilibrating variables in the international balance of payments mechanism and tries to bring this mechanism closer to that prevailing in intersectional balance of payments within a country. The scheme in fact draws its inspiration from the experience of the United States with regard to adjusting intersectional balances. As he says:

The case for financial integration may be presented most succinctly by analogy with the process through which regional payments adjustments are accomplished within the U.S. common market. There we find a high degree of financial integration, complete freedom of capital movements, and scarcely any concern about the process of adjustment in a particular region's balance of payments or about the level of its external reserves.<sup>23</sup>

Elsewhere, he expresses the same view:

It...appears that the disappearance of the kind of regional payments pressures formerly experienced within the United States is the result of the development of large holdings of "generalized" claims and the attendant development of an integrated market. These developments have caused the payments position of individual states and regions to be less like that of separate nations (as usually analyzed in international trade textbooks), and more like that of parts of a fully integrated economy.<sup>24</sup>

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22. Ibid., p. 195.

23. Ibid., p. 181.

24. James C. Ingram, "States and Regional Payments Mechanisms," Quarterly Journal of Economics (November 1959), 629. The author says that extensive empirical studies on sectional adjustments in the United States are difficult to make because of the scarcity of data on intersectional transactions. He refers to the revealing experience

Can the countries of Asia use such an institutional arrangement for financial integration to cure their balance of payments ills, in the event that they form a common market or free trade area? Given the need for fixed exchange rates, freedom of trade and payments, and a willingness of the countries to adapt monetary policies to balance of payments requirements, there would have to be prompt, sensitive, and broad-based responses in the market for securities and other financial assets, in order for financial integration to work successfully. This, in turn, would require the participation of economies with "variegated structure of financial assets, such as bonds of many maturities, treasury bills, acceptances, short-term commercial paper, and deposits (demand and time); and with a wealth of experience and financial know-how in handling such claims."<sup>25</sup> Therefore, a well-developed network of financial institutions, including commercial banks, insurance companies, savings associations, and pension funds would be needed. Many countries of Asia in fact suffer from a lack of well-developed financial markets and well-diversified financial claims and from a lack of extensive and efficient use of an exchange economy.<sup>26</sup> And in the absence of adequate initial levels of foreign exchange reserves, an

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of Puerto Rico in "A Proposal for Financial Integration . . ." op. cit. A detailed empirical study of Puerto Rico is provided in his book, Regional Payments Mechanisms: The Case of Puerto Rico (Chapel Hill: University of North Carolina Press, 1962). Some empirical evidence relating to the Federal Reserve Districts of the United States, namely, Boston, New York, and Minneapolis, for the period 1919-39, is provided in Hartland, op. cit.

25. Ingram, "A Proposal for Financial Integration . . ." op. cit., p. 180.
26. Even in the Atlantic Community, as Ingram maintains, the condition of availability of well-developed financial institutions may not be uniformly met by all countries. Nations such as Greece and Turkey may not seem adequately prepared for participation in financial integration, but the Community as a whole can form an appropriate nucleus for integration.

intermingling of internationally acceptable financial claims is virtually impossible for Asian countries.<sup>27</sup>

In what other way could the countries of Asia devise a suitable institutional arrangement for dealing with their payments problems? How else could balance of payments adjustments among Asian countries be brought closer to the mechanism for adjusting intersectional balances? What other equilibrating variables could be created? What type of integration or cooperation can cure payments deficits? Can the alternative scheme of a payments union work toward the solution of balance of payments difficulties, even if the countries involved have not formed a free trade area? What conditions need to be fulfilled if the payments union is to provide an answer to these problems and lead to more trade within the region?

Earlier, we alluded to the mobility of capital funds between various sections of a country under the national branch banking system. Banks operating in a section experiencing payments deficits can rely upon their branches or head offices in a section with surpluses for the financial support required to prevent the loss of reserves and the eventuality of monetary contraction, by taking advances from them. This idea can also be applied to settling balance of payments among countries seeking to form a group based on mutual cooperation for mutual benefit. In other words, countries running payments deficits on an intra-group account could obtain short-term or medium-term credit from those countries running payments surpluses. In order to avoid numerous bilateral credit negotiations and arrangements, to make the use of credit multilateral within the group, and to inspire the confidence of the participating countries in such a credit mechanism, the device of a payments union with credit-granting powers can be fruitful, given certain conditions. Under this arrangement, deficit

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27. It is not possible, at this stage, to provide empirical evidence supporting these generalizations, but they seem to hold good.

countries on an intra-group account would obtain credit from the union, which in turn would obtain credit from the surplus countries within the group. Such a scheme, it must be emphasized, can tackle only temporary and self-correcting balance of payments disequilibria. The details are discussed below.

#### IV

In general, any regional payments union comprised of a group of countries combines two fundamental mechanisms, clearing and settlement, and is faced with two problems: multilateral clearing or offsetting of bilateral balances—surpluses and deficits arising from trade among the member countries; and settlement of each country's net balance—surplus or deficit—with the union itself, i. e., with other member countries taken as a whole. Depending upon the details of the arrangement, it may also face a third problem, namely, settlement of the group's net balance, i. e., the sum of net balances of the member countries with the rest of the world.<sup>28</sup> The first essentially involves a clearing house arrangement within the union. The second, settlement, may require the union to devise suitable credit provisions, in order that the member countries may avoid possible trade restrictions on intra-regional account because of payments difficulties. The third problem, which also involves a settlement mechanism, is concerned with interregional accounts, i. e., settlement of the region's net transactions with the outside world. The union may be required to institute a joint fund of gold and foreign exchange reserves, provided by the member countries, and this will lead to some uniformity in members' foreign exchange policies.

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28. R. F. Mikesell, "Regional Multilateral Payments Arrangements," Quarterly Journal of Economics (August 1948), 500-18.

For the multilateral clearing of bilateral balances within the region, the bilateral surpluses and deficits of individual countries with each other can be pooled together, and a single net position—surplus or deficit—can be obtained for each country vis-a-vis the union. Under this procedure, those countries running surpluses on intra-regional account would acquire claims against the payments union, rather than against the countries in their debt, while the union itself would acquire claims on the latter. This corresponds to the procedure adopted by an association of domestic banks for clearing checks; and it will raise the problem of settling net balances of those countries running a deficit with the union. This is the most crucial question for a regional payments union.

The essence of a payments union is this: the participating countries do not have to settle their intra-regional trade balances in 100 percent gold.<sup>29</sup> In other words, a country running a deficit would cover part of that deficit with credit granted by the union and part with gold payment. Similarly, the country running a surplus would extend credit to the union for part of its surplus, and part it would settle by the receipt of gold. The rights and obligations of the payments union would consist of extension of credit to it by potential surplus countries and provision of credit by it to potential deficit countries, respectively. This would make trade non-discriminatory within the region and discriminatory with the outside world.

The provision of partial credit would have the merit of enabling potential deficit countries to economize on a limited supply of foreign exchange. The avoidance of trade restrictions by the potential beneficiaries of the union would thus safeguard the trading interests of the participating countries and act as a powerful stimulus to intra-regional trade. It would aid the bringing about of a consciously attempted trade liberalization program.

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29. The term "gold" is used throughout this discussion to denote convertible currencies as well as gold.

As an alternative to partial credit, the payments union might adopt the method of granting an exclusive line of credit, whereby deficits within the lines would be settled in 100 percent credit and those beyond in 100 percent gold. This would have some disadvantages. The change-over from 100 percent credit to 100 percent gold would provide excessive facilities at the outset and might lead to a sudden need for import restrictions. Thus, the partial credit method would seem to be the most fruitful approach.

Having settled on the sources of credit and the purpose<sup>30</sup> for which it is to be utilized, there is next the question of size of credit. For determining this, the following procedure (similar to the one adopted by the European Payments Union in the later years of its existence) can be used. Each country would initially be given a certain quota, set at, say, 15 or 20 or 30 percent of the country's total visible and invisible trade with the region in a given period. The amount of the quota would basically determine the amount of trade deficit or surplus that would qualify for or be subject to partial credit and partial gold settlement. It would not designate the credit line received or granted (though it would indirectly enter into the over-all

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30. In the discussion of a possible clearing house with credit provisions for the Latin American regional market, it was suggested that clearing house credit could play a dual role, if the central bank of the deficit country receiving "payments" credit allowed the importer to share this credit. Counter to this, it was also argued that "it is difficult... to visualize how a central bank could thus commercialize its clearing credit. No facilities could be made available to importers in regional surplus countries, because the central bank itself would not receive any credit. Even in deficit countries, the central bank would not know in advance the amount of credit it was to receive..." In fact, the credit-granting operations of the clearing house do not come into existence until countries' underlying transactions are cleared and net positions are established. See F. A. G. Keesing and P. J. Brand, "Possible Role of a Clearing House in the Latin American Regional Market," International Monetary Fund Staff Papers, X, No. 3 (November 1963). Our proposal for a payments union, as indicated earlier, is based solely on balance of payments credit.

credit element). The credit line would be defined by what percentage of a given trade deficit (surplus), within the limit of the quota, is to be settled in credit. Credit can be made liberal or stringent, depending upon this percentage. The quota would set the limit beyond which the cumulative trade deficit or surplus would be settled in 100 percent gold.<sup>31</sup>

Settlement between each member and the union would be made at the end of each accounting period, say, a quarter or a month. The change in cumulative (accounting) position—deficit or surplus—would form the basis for the settlement in each period. At each settlement, a country running a deficit with the union would receive credit and pay gold in specific proportions of, say, 50 percent credit and 50 percent gold, or 60 and 40, or 25 and 75. Similarly, a country running a surplus would grant credit and receive gold in the same proportions. To make the payments union more or less self-financing, the credits obtained by debtor countries would need to be matched by those granted by creditor countries. Similarly, the amount of gold paid by debtor countries would need to correspond to the amount of gold received by creditor countries. This can be accomplished by fixing the same proportions of gold-credit settlement for both the debtor and creditor countries, since the total of intra-regional deficits would by definition equal intra-regional surpluses.<sup>32</sup>

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31. Some time limit for the repayment of outstanding debts may be necessary, so that the union's claims on debtors and creditors' claims on the union will not remain frozen for an indefinite period. Normally, interest payments by debtors would serve to prevent this possibility.
  32. All accounts and credit operations would be carried out, say, in a special payments union unit defined by its gold content. In this context, it should be noted that if the payments union is established without forming a customs union or free trade area, the member countries may be permitted to vary their exchange rates. In the event of exchange rate variations, the outstanding claims and debts of the union would not be affected, since they would be enumerated

These principles can be illustrated by the following hypothetical example. Countries A, B, C, and D are assumed to be the members of a payments union with quotas of \$100 million, \$150 million, \$50 million, and \$200 million, respectively. Settlements of deficits and surpluses are assumed to take place in gold and credit on a 50-50 basis. As in Chart 1, case 1, countries A and B have deficits of \$20 million and \$80 million, respectively, in period 1. On the other hand, countries C and D have surpluses of \$10 million and \$90 million, respectively, in the same period. Under the payments union arrangement, the deficits of \$100 million and the corresponding surpluses of \$100 million would be settled in equal proportions of gold and credit. Country A receives credit for \$10 million from the union and pays gold worth \$10 million to the union; country B receives credit for \$40 million and pays gold worth \$40 million; country C gives credit of \$5 million to the union and receives gold worth \$5 million from it; and country D gives credit of \$45 million and receives gold worth \$45 million. The receipts of gold by C and D are matched by the payments of gold by A and B, and the extension of credit to A and B are matched by the granting of credit by C and D. This procedure will be repeated for each country until its cumulative position exceeds its previously established quota.

It may be noted that adopting a change in cumulative position as the basis of settlement would enable a deficit country to receive gold by earning a surplus in a single period. For example, in case 1, country A, which runs deficits for the first three periods and thereby loses gold, earns a surplus of \$20 million in the fourth period. To settle its surplus, it reduces its debt to the union by \$10 million and receives gold worth \$10

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in a special monetary unit of specific gold content. It should be repeated that exchange rate variations would be ruled out if the countries have established a customs union or free trade area with or without the payments union, except that initial exchange rate adjustments may be permitted.

## CHART I.

**Settlements in Payments Union**  
 (Hypothetical examples with gold-credit settlement ratio of 1:1, US\$ millions)

Country, quota, and period	Surplus (+) or deficit (-) for the period (1)	Cumulative position at the end of the period surplus (+) or deficit (-) (2)	Means of Settlement Vis-a-vis the Union	
			Credit received (+) or granted (-) (3)	Gold paid (+) or received (-) (4)
<u>Case 1</u>				
<u>Country A, quota = 100</u>				
Period I	-20	- 20	+10	+10
Period II	-30	- 50	+15	+15
Period III	-40	- 90	+20	+20
Period IV	+20	- 70	-10	-10
Period V	-20	- 90	+10	+10
			+45	+45
<u>Country B, quota = 150</u>				
Period I	-80	- 80	+40	+40
Period II	-60	-140	+30	+30
Period III	+10	-130	- 5	- 5
Period IV	-20	-150	+10	+10
Period V	0	-150	-	-
			+75	+75
<u>Country C, quota = 50</u>				
Period I	+10	+ 10	- 5	- 5
Period II	+24	+ 34	-12	-12
Period III	+ 6	+ 40	- 3	- 3
Period IV	+10	+ 50	- 5	- 5
Period V	0	+ 50	-	-
			-25	-25
<u>Country D, quota = 200</u>				
Period I	+90	+ 90	-45	-45
Period II	+66	+156	-33	-33
Period III	+24	+180	-12	-12
Period IV	-10	+170	+ 5	+ 5
Period V	+20	+190	-10	-10
			-95	-95

Chart 1 (continued)

	(1)	(2)	(3)	(4)
<u>Case 2</u>				
<u>Country A,</u> quota = 100				
Period I	-20	- 20	+10	+10
Period II	-30	- 50	+15	+15
Period III	-40	- 90	+20	+20
Period IV	+20	- 70	-10	-10
Period V	-20	- 90	+10	+10
			<u>+45</u>	<u>+45</u>
<u>Country B,</u> quota = 150				
Period I	-80	- 80	+40	+40
Period II	-60	-140	+30	+30
Period III	+10	-130	- 5	- 5
Period IV	-20	-150	+10	+10
Period V	0	-150	-	-
			<u>+75</u>	<u>+75</u>
<u>Country C,</u> quota = 50				
Period I	+10	+ 10	- 5	- 5
Period II	+24	+ 34	-12	-12
Period III	+ 6	+ 40	- 3	- 3
Period IV	+10	+ 50	- 5	- 5
Period V	+ 5	+ 55	0	5
			<u>-25</u>	<u>-30</u>
<u>Country D,</u> quota = 200				
Period I	+90	+ 90	-45	-45
Period II	+66	+156	-33	-33
Period III	+24	+180	-12	-12
Period IV	-10	+170	+ 5	+ 5
Period V	+15	+185	- 7.5	- 7.5
			<u>-92.5</u>	<u>-92.5</u>

Chart 1 (continued)

	(1)	(2)	(3)	(4)
<u>Case 3</u>				
<u>Country A,</u> quota = 100				
Period I	-20	- 20	+10	+10
Period II	-30	- 50	+15	+15
Period III	-40	- 90	+20	+20
Period IV	+20	- 70	-10	-10
Period V	+12	- 58	<u>- 6</u>	<u>- 6</u>
			+29	+29
<u>Country B,</u> quota = 150				
Period I	-80	- 80	+40	+40
Period II	-60	-140	+30	+30
Period III	+10	-130	- 5	- 5
Period IV	-20	-150	+10	+10
Period V	-32	-182	<u>0</u>	<u>+32</u>
			+75	+107
<u>Country C,</u> quota = 50				
Period I	+10	+ 10	- 5	- 5
Period II	+24	+ 34	-12	-12
Period III	+ 6	+ 40	- 3	- 3
Period IV	+10	+ 50	- 5	- 5
Period V	+ 5	+ 55	<u>0</u>	<u>- 5</u>
			-25	-30
<u>Country D,</u> quota = 200				
Period I	+90	+ 90	-45	-45
Period II	+66	+156	-33	-33
Period III	+24	+180	-12	-12
Period IV	-10	+170	+ 5	+ 5
Period V	+15	+185	<u>- 7.5</u>	<u>- 7.5</u>
			-92.5	-92.5

million. Similarly, a country running a surplus and earning gold would be required to make gold payments, should it acquire a deficit in a single period. Thus, country D in our example, having a cumulative surplus of \$180 million from the first three periods, pays gold worth \$5 million and reduces its credit claims on the union by \$5 million in order to settle its \$10 million deficit in the fourth period.

The illustration given above indicates perfect matching between credits granted to debtor countries and credits received from creditor countries, as well as between gold received from debtor countries and gold paid to creditor countries, but this would not necessarily take place, as is shown in case 2. At the end of the fifth period of union operations, the union has granted a total of \$120 million credit to the debtor countries, but has received a total of only \$117.5 million credit from the creditor countries. At the same time, the union has received gold worth \$120 million from the debtors, but has paid out gold worth \$122.5 million to the creditors. This would occur when debtor countries settle their deficits within their quota limits, on a 50-50 gold-credit basis, while creditor countries accumulate surpluses beyond their quotas, so that the amount in excess of the quotas is settled in 100 percent gold.

Or it may happen, as is shown in case 3, that the union receives more gold than it pays. This would come about when a debtor country exceeds its quota and settles its excess deficits in 100 percent gold, at a time when the surplus countries do not exceed their quotas at all or by very much. Thus, the settlement of excess debts in 100 percent gold would bring more gold into the union than it paid out to creditor countries.

In order to take care of the contingency that the union might pay out more gold than it receives, some working capital in the form of gold or convertible currencies would be required. The question arises of how this capital fund<sup>33</sup> can be raised. One way of doing it is to ask the participating

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33. The capital fund would also serve as a guarantee to the creditors against possible default by the debtors.

countries for a nominal contribution in gold in proportion to their quotas, but in view of their foreign exchange difficulties, the member countries may not be able to contribute to such a fund. Alternatively, the payments union may approach the developed countries to request outright grants for this purpose. It may be noted in this connection that, with the establishment of the European Payments Union in 1950, the U. S. government provided a dollar grant of \$350 million under the European Recovery Program.<sup>34</sup> The U. S. could make a similar grant to the projected Asian Payments Union.

It would be difficult to decide a priori the size of the capital fund required for a payments union. We might note that during its eight-year existence, the European Payments Union had a capital fund of \$272 million.<sup>35</sup> This amount was subsequently raised, because of the union's net earnings, which arose from differences in interest payments received by the union from debtor countries and paid by the union to creditor countries.

The difference between interest received and paid can also be a source of liquidity for the union.<sup>36</sup> A third way in which to avoid any possible gold shortage would be the allocation of additional quotas to countries with chronic surpluses, in order to make more remote the possibility of having to settle in 100 percent gold.

It should be clear from the above that the continuing utility and success of a payments union would depend upon the self-correcting nature of the balance of payments behavior of the participating countries. If the union

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34. Bank for International Settlements, Twenty-First Annual Report, April 1950-March 1951 (Basle, 1951), p. 227.

35. The original grant of \$350 million, less \$78 million spent by the European Payments Union initially to adjust certain countries' debit and credit balances before joining.

36. This difference can be made positive by creating an interest differential on credits granted to and by the union. The interest structure should be subject to review at frequent intervals, to take into account developments in the union's credit operations.

is a close grouping with no external relations, this would mean that the participating countries must be able to restore equilibrium in their intra-regional accounts over a reasonable period of time, so that they will not have to face the problem of exhausting their quotas too soon, nor that of carrying too heavy an interest burden. As stated earlier, the payments union would be designed to provide short-term liquidity, to afford countries experiencing balance of payments difficulties a breathing spell during which they would be able to take suitable corrective measures.

In a payments union, clearing positions on intra-regional account are necessary as indicators of which countries qualify for the use of credit and which are required to extend credit. This could lead to four possible situations. (1) Debtor countries on intra-regional account might also run a deficit with outside countries. No special problem would arise, and the availability of partial credit for the settlement of intra-regional deficits would be helpful to these countries.

(2) Debtor countries on intra-regional account might earn a surplus in their transactions with outside countries, which could be used to finance their intra-regional deficits. In this case, debtor countries would not need to use the credit available to them. Furthermore, they probably would not have any incentive to accumulate their outside surpluses, while obtaining credit from the union to finance intra-regional debts, because the interest paid on credit from the union might exceed the interest earned on the outside surpluses. However, in order to avoid the possibility of their using intra-regional credit when they have outside surpluses, the union might explicitly require that, to qualify for the use of credit from the union, countries must first make use of any surpluses outside they might have earned.

(3) Creditor countries may also run surpluses in their transactions with outside countries. They would extend credit to the union, in view of their intra-regional surpluses, as well as to the outside, and no special problem would arise. (4) But a peculiar situation would arise if creditor

countries were in deficit with outside countries, for they would be required to extend credit to the union despite their over-all equilibrium (assuming their intra-regional surpluses balanced their extra-regional deficits). If the gold-credit settlement is on a 50-50 basis, then the creditor country can hope to utilize the half of its intra-regional surplus received in gold for financing the outside deficit. The other half must be financed from the country's own foreign exchange reserves.

But would a country in such a situation accept this arrangement? In the absence of credit from the surplus country to the union, and hence from the union to a deficit country, the latter might find it necessary to impose restrictions on its imports coming from the surplus country (assuming that the payments union was formed without prior commitment to free trade within the union). Consequently, the surplus country would cease to be a surplus country, or at least it would find its surplus reduced. In order to protect its export interests, the surplus country would be willing to accept the postponement of claims for part of its surplus on intra-regional account.

The implication of this argument is as follows: if countries commit themselves to a free trade area arrangement without also negotiating the creation of a payments union, incentives for potential creditors to join the union may be rather small. This provides a good reason for making a payments arrangement a necessary part of any contemplated free trade proposal.<sup>37</sup> Also, deficit and surplus positions may change, and countries

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37. An exactly similar view is expressed with regard to Latin American countries by Keesling and Brand, *op. cit.*, p. 450: "One of the considerations prompting interested creditor countries to offer credits of a certain size may be the desire to protect their export interests. In this context, it should be noted that the principle of non-discriminatory treatment of all intra-area trade has been unconditionally incorporated in the Treaty of Montevideo, without reference to the conclusion of a payments arrangement. As a consequence, the incentive for potential creditors to participate in a payments arrangement may be rather small."

which expect to run surpluses may find, in the course of time, that they run deficits, in which event they can hope to benefit from the credit mechanism of the payments union.

## V

We now turn to the question of the feasibility of a payments union for Asian countries. To begin, it is worth while to look at the trade patterns and problems and the balance of payments experience of the countries of Asia. Although they may not be of much use in assessing the long-term prospects for an Asian payments union, they can identify the possible obstacles to its formation.

The foreign exchange shortages of Asian countries and the region's import dependence on the outside world have figured prominently in recent discussions of the possibilities for regional economic cooperation, especially for the forming of a customs union or a free trade area.<sup>38</sup> Asian countries have expressed fears regarding the implications for their balance of payments difficulties of joining a customs union or free trade area.<sup>39</sup> Under the impact of the rising tempo of industrialization and economic development and growing population pressures, the region's countries have increased their dependence on the import sector for their requirements of capital goods and machinery and, in some cases, foodstuffs. The annual import average of eight developing countries of South and Southeast Asia<sup>40</sup> increased

38. See "Regional Trade Cooperation," "The Scope for Regional Economic Cooperation," and "Approaches to Regional Harmonization of National Development Plans in Asia and the Far East," in United Nations, Economic Bulletin for Asia and the Far East (June 1961, December 1961, and December 1964, respectively).

39. They are also apprehensive about the implications of a customs union for their national development plans.

40. Burma, Ceylon, India, Indonesia, the Federation of Malaya and Singapore, Pakistan, the Philippines, and Thailand.

from \$5.4 billion in 1951-53 to \$6.0 billion in 1958-60, while exports declined from \$5.7 billion to \$5.3 billion in the same period, as shown in Table 1. As a result, a trade surplus of about \$300 million in 1951-53 became a trade deficit of nearly \$700 million in 1958-60. This deterioration of \$1 billion during the 'fifties took place despite trade and exchange restrictions imposed by many countries during the latter part of the decade.

Import restrictions have naturally shown a bias in favor of capital goods and materials used chiefly for capital goods, as a result of the development programs these countries have adopted. During the 'fifties, the developing Asian countries<sup>41</sup> increased their imports by 11 percent, but this increase was unevenly distributed among various categories of goods and indicated far-reaching changes in the import structure of the group. Imports of capital goods increased by 65 percent and those of materials chiefly for capital goods by 45 percent. In contrast, imports of food and non-food consumer goods declined, the former by 2 percent and the latter by 23 percent, though imports of materials chiefly for consumer goods increased by 4 percent.

The relative share of capital goods in total imports of all fifteen developing Asian countries increased from 1951 to 1960. During 1958-60, for the group as a whole, imports of capital goods and materials chiefly for capital goods accounted for about 40 percent of total imports, compared to 28 percent in 1951-53. Non-food consumption goods and materials chiefly for consumption goods accounted for about 40 percent in 1958-60, in contrast with 50 percent in 1951-53. And food dropped to 19.6 percent in 1958-60, from 22.2 percent in 1951-53.<sup>42</sup>

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41. The phrase "developing Asian countries" refers throughout to the following group of 15 countries: Burma, Cambodia, Ceylon, China-Taiwan, the Federation of Malaya and Singapore, Hong Kong, India, Indonesia, Laos, North Borneo, Pakistan, the Philippines, Sarawak, South Viet Nam, and Thailand.
42. For further details, see United Nations, Economic Survey of Asia and the Far East, 1962.

TABLE 1.

**Intra-Regional Trade, South and Southeast Asia**  
 (Exports and imports as percentages of total exports and imports,  
 annual averages, 1951-53 and 1958-60)

	<u>Exports</u>		<u>Imports</u>	
	<u>1951-53</u>	<u>1958-60</u>	<u>1951-53</u>	<u>1958-60</u>
Burma	62.4	63.1	35.1	17.3
Ceylon	4.9	3.7	27.3	21.8
India	15.8	9.7	14.8	7.2
Indonesia	31.9	33.8	14.0	15.3
Fed. of Malaya and Singapore	16.6	16.2	41.6	43.9
Sarawak	(46.3)	42.7	(11.3)	12.2
Cambodia	(27.2)	17.0	(23.9)	11.1
Laos	(84.6)	72.7	(30.6)	22.6
South Viet Nam	(16.9)	19.4	( 9.4)	11.6
Pakistan	15.9	9.8	14.6	9.0
Philippines	0.7	0.3	6.8	9.8
Thailand	41.9	35.5	20.8	15.0
<b>Eight country total</b> (excluding Sarawak, Cambodia, Laos, and South Viet Nam)	20.8	17.8	22.1	19.4
<b>Eight country intra-</b> <b>regional trade (in</b> <b>US\$ million)</b>	1,182.4	946.3	1,196.8	1,163.8
<b>Eight country</b> <b>total trade (in</b> <b>US\$ million)</b>	5,689.1	5,339.5	5,411.2	6,012.4

**Note:** Export and import data shown in parentheses relate to annual averages for the period 1955-57 for those countries.

**Source:** United Nations, Direction of International Trade; and UN, ECAFE, Intra-Regional Trade Statistics (sixth series).

These changes in the import structure have also meant changes in the direction of imports. Since developed countries outside the region are the chief source of capital goods and materials chiefly for capital goods,<sup>43</sup> the shifts in import structure necessitated by foreign exchange difficulties have favored the exports of developed countries at the expense of those of the developing countries both within and outside the region. As was shown in Table 1, the intra-regional exports of eight South and Southeast Asian countries declined from 20.8 percent in 1951-53 to 17.8 percent in 1958-60, while intra-regional imports fell from 22.1 percent to 19.4 percent in the same period. There were some exceptions among individual countries: the intra-regional exports of Burma and Indonesia increased slightly; and the intra-regional imports of the Federation of Malaya and Singapore, the Philippines, and Indonesia registered increases. (Of those not included in the eight-country total, Sarawak showed an increase in intra-regional imports, and South Viet Nam raised its intra-regional trade both of exports and imports.) But on the whole, the trends in intra-regional trade have not been encouraging.<sup>44</sup>

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43. It should be noted that the developed countries supplied 65 percent of the total imports of \$9.23 billion of developing Asian countries in 1960. Chemicals, machinery and transport equipment, and other manufactured goods accounted for about 60 percent of this group's imports in 1960, of which the developed countries of the world (Western Europe, North America, and Japan) accounted for more than four-fifths. Ibid.
44. The share of intra-regional trade in total imports of one group of ECAFE countries (Afghanistan, Brunei, Burma, Cambodia, Ceylon, China-Taiwan, Hong Kong, India, Indonesia, the Republic of Korea, Laos, Malaysia, Nepal, Pakistan, the Philippines, Thailand, the Republic of Viet Nam, and Western Samoa) declined by about 3 percent between 1955-57 and 1959-61. The greatest drops were registered for food, agricultural raw materials, and ores and fuels, which can be generally explained by growing internal requirements for raw materials and ores, self-sufficiency drives with respect to food, and foreign exchange shortages. For details, see United Nations, Economic Bulletin for Asia and the Far East (June 1964).

TABLE 2.

**South and Southeast Asian Countries, External Transactions  
on Goods and Services Accounts, 1956-62**  
(Millions of U. S. dollars)

	<u>1956</u>	<u>1957</u>	<u>1958</u>	<u>1959</u>	<u>1960</u>	<u>1961</u>	<u>1962</u>
Burma	3.2	- 112.6	- 10.9	- 10.1	- 23.7	- 4.2	16.0
Ceylon	28.8	- 32.8	- 27.3	- 41.2	- 50.8	- 22.1	- 28.4
India	-675.8	-1,030.7	-933.6	-530.9	-881.3	-735.7	-919.1
Indonesia	-165.0	- 85.0	- 65.0	25.0	- 84.0	-521.0	-367.0
Malaysia	-	-	-	-	172.5	74.8	4.4
Pakistan	-165.8	- 172.9	-211.6	-105.9	-236.6	-271.8	-212.8
Philippines	-114.0	- 272.0	-136.0	- 75.0	-144.0	-163.0	- 12.0
Thailand	- 15.3	- 36.3	- 78.7	- 70.0	- 40.0	2.6	- 69.9
Viet Nam (S)	-323.9	- 183.5	-148.1	-169.4	-153.5	-214.2	-191.2

Notes: No sign indicates credit; minus sign indicates debit.

Burma--Figures given in kyats in original sources were converted into U. S. dollars at the official exchange rate of kyats 4.76 = \$1.00.

Ceylon, India, and Pakistan--Figures given in rupees in original sources were converted into U. S. dollars at the official exchange rate of Rupees 4.76 = \$1.00.

Malaysia--Figures given in Malaysian dollars in original sources were converted into U. S. dollars at the official exchange rate of Malaysian dollars 3.1 = \$1.00.

Source: International Monetary Fund, International Financial Statistics.

The balance of payments experience and the pattern of intra-regional trade balances of these countries is also pertinent. The most striking feature of the former is the persistent deficits on the goods and services account during 1956-62 for almost all of the countries of South and Southeast Asia, as Table 2 demonstrates. Malaysia, which started with a surplus on the goods and services account, experienced a rapid surplus deterioration during the period 1960-62. Most of the goods and services account deficit is believed to have been met by capital inflows (grants and loans)

from outside the region and by the countries' own foreign exchange reserves. A detailed picture of the geographical pattern of the countries' international transactions is not available, except on the visible trade account. But in view of their goods and services account deficits, it can be expected that the capital outflow from South and Southeast Asia would be marginal.

Tables 3 and 4 give the trade balance matrices of South and Southeast Asian countries on the intra-regional and over-all accounts, respectively. Data pertaining to 1956-62 suggest that Burma, Indonesia (1956-61), Sarawak, and Thailand were the surplus countries on intra-regional account. Of these four countries, only Indonesia and Sarawak (except for 1961) had trade surpluses on over-all account. A second group, Ceylon, the Federation of Malaya and Singapore, Laos, South Viet Nam, the Philippines, and North Borneo, had deficits on intra-regional trade account throughout 1956-62. Here Laos, South Viet Nam, and the Philippines (except for 1959) ran persistent deficits in over-all trade; Ceylon and the Federation of Malaya and Singapore had no consistent deficits, but exhibited net deficits on over-all account over the period 1956-62; North Borneo, on the other hand, had small surpluses on over-all account (except in 1962). A third category of countries—Cambodia, India, and Pakistan—had fluctuating trade balances on intra-regional account, Cambodia ending the period 1956-62 with a net surplus and India and Pakistan with net deficits. All three had deficits in each of the years from 1956 to 1962 in over-all trade. Thus, throughout 1956-62, intra-regional trade surpluses were concentrated in a few countries, namely, Burma, Indonesia, Sarawak, and Thailand, while Ceylon, the Federation of Malaya and Singapore, Laos, South Viet Nam, the Philippines, and North Borneo had deficits. Only three countries, Cambodia, India, and Pakistan, failed to have either chronic surpluses or chronic deficits on intra-regional account.

It was suggested above that, in the proposed payments union, the criterion for granting credit would be intra-regional surpluses and that

TABLE 3.

South and Southeast Asian Countries, Trade Balances Matrix on Intra-Regional Account  
(Millions of U. S. dollars)

	<u>1938</u>	<u>1948</u>	<u>1950</u>	<u>1951</u>	<u>1952</u>	<u>1953</u>	<u>1954</u>	<u>1955</u>	<u>1956</u>
Burma	74.8	128.5	51.0	87.0	95.0	65.1	98.3	52.3	84.8
Indonesia	45.6	40.2	219.4	315.5	144.9	135.2	175.3	177.9	150.8
Sarawak	8.0	40.8	-	-	-	-	42.8	52.1	58.4
Thailand	36.0	75.6	106.8	138.1	116.3	67.8	70.7	78.4	77.1
Ceylon	- 36.6	- 81.0	- 87.9	- 82.5	- 80.6	- 65.9	- 53.7	- 64.2	- 66.4
Federation of Malaya and Singapore	-119.9	-142.2	-284.1	-429.1	-229.9	-248.4	-268.9	-388.9	-374.9
Laos	-	-	-	-	-	-	-	- 7.5	- 10.2
Viet Nam (S)	-	-	-	-	-	-	-	- 1.1	- 16.4
Philippines	- 2.6	- 24.2	- 13.8	- 31.7	- 31.8	- 18.3	- 29.4	- 45.9	- 42.1
Cambodia	-	-	-	-	-	-	-	- 3.0	- 3.9
India	- 35.7	-115.8	55.8	-120.5	59.6	13.2	- 59.8	- 9.2	2.9
Pakistan	-	175.7	15.3	94.5	- 48.6	11.5	11.9	38.9	25.2
N. Borneo	-	-	-	-	-	-	-	-	- 0.9

Source: United Nations, Direction of International Trade; and ECARF, Intra-Regional Trade Statistics  
(sixth series).

Note: No sign means surplus; minus sign means deficit.

Table 3 (continued)

	<u>1957</u>	<u>1958</u>	<u>1959</u>	<u>1960</u>	<u>1961</u>	<u>1962</u>
Burma	70.2	94.4	96.8	93.2	75.4	99.7
Indonesia	245.3	203.2	209.7	186.1	157.2	-
Sarawak	60.4	47.3	55.9	50.9	34.3	35.1
Thailand	90.2	60.6	58.2	72.8	118.1	103.9
Ceylon	- 93.8	- 64.3	- 75.5	- 80.6	- 80.7	- 66.0
Federation of Malaya and Singapore	-376.9	-376.9	-449.1	-414.7	-372.5	-326.3
Laos	- 8.6	- 5.7	- 3.1	- 3.9	- 6.4	- 11.8
Viet Nam (S)	- 22.0	- 13.3	- 22.3	- 3.0	- 12.2	- 13.5
Philippines	- 54.9	- 63.8	- 54.0	- 36.9	- 47.9	- 33.6
Cambodia	2.5	3.7	- 4.0	5.2	2.0	3.6
India	- 1.8	- 44.9	29.7	- 25.2	30.5	- 12.8
Pakistan	- 20.5	- 26.4	- 4.6	4.5	- 19.7	17.3
N. Borneo	- 1.1	- 6.8	- 9.5	- 9.6	- 7.5	- 3.7

TABLE 4.

South and Southeast Asian Countries. Over-All Trade Balances  
(Millions of U. S. dollars)

	<u>1938</u>	<u>1948</u>	<u>1950</u>	<u>1951</u>	<u>1952</u>	<u>1953</u>	<u>1954</u>	<u>1955</u>	<u>1956</u>
Burma	98.0	43.8	43.3	68.7	71.8	33.9	46.8	46.2	47.4
Indonesia	111.7	- 70.1	359.3	424.6	- 12.8	66.7	237.3	314.4	28.9
Sarawak	-	34.1	-	-	-	-	9.3	11.6	7.5
Thailand	33.1	86.0	160.3	206.5	95.3	38.9	21.1	63.0	- 35.3
Ceylon	17.7	5.0	82.8	72.0	- 43.1	- 8.9	86.6	100.5	21.3
Federation of Malaya and Singapore	19.0	- 28.8	359.6	431.3	14.8	- 67.7	- 9.8	109.3	4.1
Laos	-	-	-	-	-	-	-	- 17.5	- 34.0
Viet Nam (S)	-	-	-	-	-	-	-	-194.0	-172.5
Philippines	14.4	-268.1	- 5.3	- 71.5	- 68.7	- 25.0	- 81.7	-146.9	- 55.4
Cambodia	-	-	-	-	-	-	-	- 9.6	- 19.4
India	50.2	-658.7	34.9	-168.4	-377.0	- 79.8	-113.0	-136.9	-457.6
Pakistan	-	212.6	106.0	228.7	- 77.2	80.7	34.2	111.6	- 76.1
N. Borneo	-	-	-	-	-	-	-	-	1.1

Note: No sign means surplus; minus sign means deficit.

Source: Same as Table 3.

Table 4 (continued)

	<u>1957</u>	<u>1958</u>	<u>1959</u>	<u>1960</u>	<u>1961</u>	<u>1962</u>
Burma	- 86.0	- 11.0	0.1	- 36.6	6.8	40.7
Indonesia	172.5	242.2	413.6	266.8	- 10.4	-
Sarawak	11.8	10.0	26.3	14.3	- 4.7	2.3
Thailand	- 44.2	- 85.6	- 60.0	- 40.1	- 11.4	- 87.8
Ceylon	- 45.4	- 1.3	- 65.7	- 38.7	- 4.1	23.0
Federation of Malaya and Singapore	- 68.2	-228.7	- 21.8	56.4	100.6	-304.6
Laos	- 40.6	- 25.9	- 26.1	- 10.9	- 15.9	- 23.7
Viet Nam (S)	-209.0	-176.9	-149.5	-153.9	-184.3	-206.0
Philippines	-185.5	- 65.9	20.4	- 25.8	-121.2	- 32.2
Cambodia	- 6.7	- 19.2	- 8.6	- 25.3	- 33.7	- 48.0
India	-804.2	-599.0	-555.7	-791.1	-595.1	-815.7
Pakistan	-103.5	- 98.9	- 32.9	-259.5	-242.6	-341.1
N. Borneo	1.4	0.6	7.2	8.7	1.8	- 1.0

for receiving credit would be intra-regional deficits. On the basis of these criteria and the data in Table 3, the conclusion seems obvious that Burma, Indonesia, Sarawak, and Thailand are the potential chronic creditor countries and Ceylon, the Federation of Malaya and Singapore, Laos, South Viet Nam, and the Philippines the potential chronic debtors. Also, it should be noted, out of the four intra-regional creditor countries, only Indonesia and Sarawak had over-all trade surpluses during 1951-62 (Table 4). Further, Indonesia had sizeable deficits on the goods and services account, except in 1959 (Table 2).

In view of all this, the Asian payments union proposed above would not have been very successful, had it been in existence during this period. Certainly, the debtor countries of the region would very much welcome the idea of a payments union, since they would, through the credit it would make available, be able to economize on scarce foreign exchange resources. On the other hand, the creditor countries--especially the chronic ones--would find it necessary to postpone part of their claims by granting credit. Depending upon their trading position with the rest of the world, this granting of credit might cause or aggravate over-all payments deficits. In this situation, their ability and willingness to give intra-group credit would be severely limited. And the problems experienced by debtor countries in repaying the credit given them might raise doubts about the efficient working of the payments union.

Nonetheless, there does exist a case for the establishment of an Asian payments union. The region's past intra-regional trade patterns and balance of payments behavior may not hold in the future. After all, countries' trade flows reflect domestic production structure and supply position and demand situations both within and outside the domestic market. Here we should take note of the projections, from 1960 to

1980,<sup>45</sup> of foreign trade for 15 developing ECAFE countries,<sup>46</sup> based on 12 commodities.<sup>47</sup> These commodities account for about 60 percent of total exports of these countries in 1960. The primary commodities included make up about 85 percent of total primary exports, and the

45. See "Projections of Foreign Trade of the ECAFE Region up to 1980," in United Nations, Economic Bulletin for Asia and the Far East (December 1963). As explained in the source, the projections are based on an assessment of demand prospects in the importing countries, based on postulations as to growth rates of population and gross national product (GNP) and coefficients of income elasticity and demand functions for each of the commodities included. The lower and higher estimates of the export projections for the developing ECAFE countries are arrived at by taking into account lower and higher estimates of growth rates of GNP in the importing regions. These two sets of growth rates, together with population growth, are as follows (in annual compound rates of growth):

<u>Importing region</u>	<u>GNP</u>		<u>Population</u>	<u>GNP/Population</u>	
	<u>I</u>	<u>II</u>		<u>I</u>	<u>II</u>
North America	3.1	4.4	1.8	1.3	2.5
Western Europe	4.2	5.2	0.7	3.5	4.5
Japan	6.0	7.0	0.7	5.3	6.3
ECAFE (excluding Japan)	3.6	4.9	2.3	1.3	2.5
Latin America	4.7	5.5	2.7	2.0	2.8
Other countries	4.0	5.3	2.5	1.5	2.8

Two implicit assumptions are also involved: (a) that the developing ECAFE countries' share in total world exports of each commodity will remain constant; and (b) there will be an adequate export surplus of each of the commodities in the region to satisfy the expected export demand. For details, see ibid.

46. The phrase "developing ECAFE countries" refers throughout to the following group of 15 countries: Greece, Burma, Cambodia, Ceylon, China-Taiwan, India, Indonesia, Iran, Malaya and Singapore, North Borneo, Pakistan, the Philippines, Sarawak, South Viet Nam, and Thailand.
47. Natural rubber, crude petroleum and petroleum products, tea, vegetable oils, rice, jute (raw jute and jute goods), sugar, tin (tin metal and tin-in-concentrate), wood and lumber, cotton fabrics, raw cotton, and tobacco.

manufactured commodities account for some 20 percent of total manufactured exports. No attempt is made to forecast the future trend in terms of trade, and the projections are made on the basis of average prices from 1958 to 1960.

The combined exports of these 12 commodities are likely to increase 113 percent by 1980, if conditions with respect to growth rates (of GNP) are favorable, and only 50 percent, if they are not (see Table 5). The lower estimate implies that exports will increase at an annual compound rate of about 2 percent, while the higher estimate projects a rate of increase twice as large--about 4 percent.

Mineral fuels are expected to offer the greatest export growth potential--a mean increase of 184 percent. Exports of foodstuffs and raw materials are likely to go up by about 55 percent, in view of the low income-elasticity of demand for these commodities. The 31 percent increase in the exports of manufactures, which include only jute manufactures and cotton textiles, is quite modest, since it is based on the assumption that the region's currently low share in total world exports of cotton textiles will remain unchanged.

Table 6 gives a picture of the developing ECAFE countries' export expansion vis-a-vis various foreign markets from 1960 to 1980. The region's traditional markets, North America and Western Europe, will increase their imports from it only modestly, 37 percent and 64 percent, respectively, because their accelerated growth is likely to lead to increased demands for the import of fuels and metals (in which the region is deficient) and increasing technological substitution for the kind of agricultural raw materials in which the region specializes. On the other hand, Japan, because of its high growth potential, and the region itself, because it will be passing through the transitional stage the developed world experienced in the past, are expected to provide fast-growing markets for the region's traditional exports; they are anticipated to increase their imports from

**TABLE 5.**  
**Developing ECAFE Countries,**  
**Export Projections for 1980 by Commodity Groups**  
**(Millions of U.S. dollars)**

Commodity group	1960 <sup>b</sup>	1980			Indices for 1980 (1960 = 100)		
		Low	High	Mean	Low	High	Mean
Food, beverages, and tobacco <sup>c</sup>	1,151	1,376	2,182	1,779	120	190	155
Raw materials <sup>d</sup>	2,105	2,804	3,782	3,293	133	180	156
Mineral fuels <sup>e</sup>	942	2,204	3,146	2,675	234	334	284
Manufactured goods <sup>f</sup>	293	334	435	384	114	148	131
<b>Total</b>	<b>4,491</b>	<b>6,718</b>	<b>9,545</b>	<b>8,131</b>	<b>150</b>	<b>213</b>	<b>181</b>

a. Fifteen countries as given in footnote 46.

b. 1960 refers to 1958-60 average in this table and Tables 6 and 7.

c. Includes rice, tea, sugar, and tobacco.

d. Includes natural rubber, raw jute, raw cotton, tin metal and tin-in-concentrate, wood and lumber, and vegetable oils (copra, coconut oil, palm oil, groundnut oil, and oil seeds).

e. Includes crude petroleum and petroleum products.

f. Includes jute goods and cotton fabrics.

Source: United Nations, Economic Bulletin for Asia and the Far East (December 1963).

**TABLE 6.**

**Relative Expansion in the Foreign Markets for ECAFE<sup>a</sup> Exports by 1980**  
**(1960 = 100)**

Country or region	Low	High	Mean
North America	123	151	137
Western Europe	139	189	164
Japan	220	299	260
Eastern Europe	91	147	119
ECAFE (intra-regional) <sup>a</sup>	172	294	233
Other countries <sup>b</sup>	160	221	190
<b>Total</b>	<b>150</b>	<b>213</b>	<b>181</b>

a. Fifteen countries as given in footnote 46.

b. Includes U.S.S.R., mainland China, Africa, Middle East, Oceania, and Latin America

Source: Economic Bulletin for Asia and the Far East (December 1963).

the region by 160 percent and 133 percent, respectively, between 1960 and 1980. Other countries, excluding Eastern Europe, are likely to increase their demand for Asian exports by 90 percent. As Table 7 indicates, the shares of the region itself and of Japan in total exports of the developing ECAGE countries are expected to increase at the expense of the shares of North America, Western Europe, and Eastern Europe, while the share of other countries will remain almost stable.

The prospects for intra-regional trade seem to be bright, especially if Japan's special position as a developed country is taken into account. We cannot make any predictions regarding future trade balance patterns which may emerge from the increased level of intra-regional trade, but the latter does indicate the greater need for financial arrangements of some sort. If the establishment of a customs union, with initial realignments of exchange rates, or the regional coordination of investment activities and fiscal policies on a planned basis, can bring about changes in the region's production structure and pattern which could solve structural balance of payments disequilibria, a strong case exists for the establishment of a payments union to deal with temporary and self-correcting imbalances. The payments union would function as a "stabilization fund," so that countries running payments deficits could avoid trade restrictions or deflationary policies, through their recourse to the liquidity created by the credit mechanism of the payments union. On the other hand, countries with surpluses would be prevented from indulging in inflationary policies or too liberal import policies or from holding excess earning idle, because they would be required to extend credit to the union. This would lead to stabilization of imports and domestic policies in the region. However, we are left with a more fundamental problem: regional coordination of investment and production plans and of fiscal policies.

TABLE 7.  
Direction of ECAFE<sup>a</sup> Exports in 1980

Country or region	Millions of U. S. Dollars			Percentage Distribution			
	1960	1980		1960	1980		
		Low	High	Mean	Low	High	Mean
North America	856	1,050	1,291	1,170	19	16	15
Western Europe	1,565	2,174	2,952	2,563	35	32	31
Japan	423	932	1,266	1,099	9	14	14
Sub-total	2,844	4,156	5,509	4,832	63	62	60
Eastern Europe	211	192	311	252	5	3	3
ECAFE (intra- regional) <sup>a</sup>	755	1,295	2,219	1,757	17	19	21
Other countries <sup>b</sup>	681	1,089	1,503	1,296	15	16	16
Total	4,491	6,718	9,545	8,131	100	100	100

a. Fifteen countries as given in footnote 4b.

b. Includes U. S. S. R., mainland China, Africa, Middle East, Oceania, and Latin America.

Source: Same as Table 5.

## VI

We have discussed the creation of some kind of institutional device for increasing the role of equilibrating variables in the mechanism for adjusting international balances of payments, particularly in the context of a free trade area arrangement, which would require the elimination of trade and exchange controls and exchange rate variations as weapons against imbalances. This takes its inspiration from the relatively smooth workings of balance of payments adjustments among the sections of a country. It has been shown that a payments union can deal with the problem of temporary disequilibria in balances of payments.

The available data from the recent past suggest that the prospects for a payments union among the countries of South and Southeast Asia do not seem bright at the moment, in view of (1) their high propensity to spend available foreign exchange on goods originating in countries outside the region; and (2) the concentration of intra-regional surpluses and deficits in certain countries. But these conditions may change and change radically, if these countries establish a customs union or coordinate their investment activities and production plans through deliberate planning.

Depending upon the evolution of the participating countries' balance of payments, the proposal for a payments union on the lines suggested above deserves serious consideration. If the degree of trade interdependence among Asian countries is increased through the establishment of a customs union or other trade liberalization measures, or through the increased ability of their production structures to satisfy better each other's needs, the concomitant establishment of a payments union might itself aid the process of bringing about a greater degree of trade interdependence or cooperation, provided, of course, that these countries do not run into chronic balance of payments difficulties.