The Use of Bilateral Agreement Currencies for Trade with Third Countries

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Most trade for which payment is made through a bilateral payments agreement consists of goods originating in one partner country and destined for the other. This, clearly, would normally be expected, in accordance with the rules applying to a bilateral trade and payments relationship. During recent years, however, the payments channels between various pairs of bilateral countries (A and B) were frequently used to settle trade transactions of a different nature, involving trade between one or both of the partners with a third country (C). This situation arose if a payment through a bilateral agreement account was made from B to A either for the import of goods into B, originating not in A but in C, or for the export of goods from A, destined not for B but for C.

It is clear, however, that in both cases there had to be some further arrangement which closed the transaction. Conceivably, a direct payment was made by A to C (case 1 in Diagram 1), or, alternatively, a direct payment was made by C to B (case 2 in the diagram). In such cases, the total three-cornered transaction consisted of one direct commercial transaction and two transfers, both of which were in conflict with normal currency prescription regulations.

It is also possible that one of the bilateral partners might have acted as a commercial go-between, re-exporting or selling in transit C’s goods to the other partner (case 1a in Diagram 1), or the other partner’s goods to C (case 2a in the diagram), while itself arranging payment in either direction. Under these conditions, there would not have been any direct contacts, either commercial or monetary, between the country of origin and the country of destination of the goods concerned. The total arrangement would have consisted of a transit transaction (which might or might not have been a commercial go-between).

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1 Throughout this paper, “B” represents the bilateral country which makes, and “A” the bilateral country which receives, a bilateral payment.
not have been in accordance with the trade rules agreed between A and B), combined with two independent transfers. The problems relating to transit trade (including the complications of switch trade which might arise in that context) will not be further examined in this paper.

It is finally possible that the triangle was closed not by a payment but by a second commercial transaction (export from A to C, export from C to B). This type of transaction (case 3 in Diagram 1) normally gave rise to a so-called cheap currency quotation in a hard currency market. It consisted of two separate direct commercial transactions, settled by one payment through a bilateral payments agreement, which conflicted with normal currency prescription regulations. If the importer in B was in direct touch with the exporter in A, settlement between the two traders in C (if they were different people) had to be arranged in C’s local currency. From the point of view of C, such a transaction would have been tantamount to a three-cornered barter deal. Technically, C might have

Diagram 1
found such an exchange very difficult to organize. In practice, therefore, this type of transaction was generally carried out in a roundabout way. The exporter in C sold his goods to B against a “transit” payment of a claim under B’s bilateral agreement with A. He subsequently sold this claim to the importer in C, who used it to settle his import from A. The technical aspects of such a “transit” payment will be explained later.²

Case 3 might assume a more complicated shape, if either C’s imports or its exports were organized by one of the bilateral countries as part of a transit arrangement. Under these conditions, B would re-export A’s goods to C, and the total transaction would be a commercial switch, consisting of one transit transaction of type 2a, plus a direct commercial transaction, paid for directly. Alternatively, the accompanying direct commercial transaction might develop into another transit transaction.

It follows from the foregoing that the one common element in the transactions under consideration is the use of a bilateral payments channel to pay for trade transactions with a third country. Such a payment is made in order to settle a commercial transaction in respect of which A (the bilateral recipient) does not supply the goods which B (the bilateral payer) obtains, and/or B is not the destination of the goods which A delivers.

Two questions arise in this connection: What technical conditions must be satisfied to make it possible to use a bilateral payments agreement for indirect payments? What economic interests are involved in this type of payment? These two questions will be examined in turn.

Technical Conditions

The technical rules which govern a strictly bilateral relationship between two countries, and which must be circumvented or set aside if there is an indirect or a “transit” payment, may be summarized as follows: First, under a payments agreement, only residents of a country that is a partner to the agreement can open accounts and hold balances in the other partner country. Second, only claims and debts, in respect of mutually admitted transactions, between residents in the two partners to the agreement can be settled through the transfer of a balance held in an account opened under the payments agreement. Third, in order to qualify for settlement through the agreement, a commercial transaction between the two partners must be in respect of goods originating in one partner country and bought by the other for its own use or consumption.

² See page 180.
Several controls are necessary to supervise these conditions and to safeguard the bilateral nature of a trade and payments relationship.

If payments between A and B are centralized, there will be either one account, opened by one central bank in the name of the other, or two accounts, opened by each central bank in the other's name, depending on the type of agreement. All monetary control will then be effectively vested in the central banks.

If payments are decentralized, there will, in addition to the account(s) held by the central bank(s), be other accounts, opened by authorized banks in one country in the names of authorized banks in the other country. This arrangement necessarily delegates some controls to the authorized banks. The role played by these banks may be small if they act only as agents for the central banks. But if they are entitled to hold and handle their own currency balances, they will be more independent, although they still will function within the framework of existing exchange control regulations, and possibly be subject to specific limitations imposed by their central banks.

As long as surrender requirements are fully enforced, no private entity (other than authorized banks) can hold balances under a payments agreement. If surrender requirements are waived, private entities may be permitted or required to hold and to handle their own balances, but normally only through the intermediary of an authorized bank.

Each central bank or authorized bank, as the case may be, has to check and certify that any amounts transferred through the agreement to the partner country are paid for the account of a resident of its own country, and in respect of a transaction that has been duly authorized. The same applies to a bank which receives payment through the agreement.

Each central bank must impose prescription regulations that link the settlement of claims and debts under a bilateral agreement to transactions effected between the two countries concerned. In addition, commercial controls are necessary to ascertain the origin of the goods imported from the partner country. The exporting country may be asked to certify the origin for the benefit of the importing country. The exporting country, furthermore, may have to ascertain in its own interests whether goods exported from its territory are in fact dispatched to their alleged destination. The importing country, finally, may be requested by the exporting country to ensure that goods which it imported from the partner country are not offered for re-export.

A complicated set of controls is thus likely to be required to guarantee that both payments and underlying transactions between two countries are and remain purely bilateral. These controls are both monetary and commercial. Some of them require close cooperation between exchange
authorities and customs authorities. Part of the monetary controls may be delegated to authorized banks. The intensity of the controls may vary with the general restrictiveness of the currency regime concerned. In certain cases, the controls in one country depend on statements made by the other country, which the former may not normally try to verify.

Indirect payments through a bilateral agreement can be arranged only under one of the following conditions: (1) an ad hoc agreement between two bilateral partners to deviate from the rules of pure bilateralism; (2) general relaxation of controls in one or both partner countries, resulting in \textit{de facto} abandonment of bilateralism; (3) connivance by the control authorities in one country at practices with which the partner country does not necessarily agree; (4) circumvention of the controls by private traders.

An ad hoc agreement between two partner countries to deviate from the normal procedure of bilateralism may affect either the commercial or the monetary rules. The partners concerned may agree that, under specified conditions, all or some goods imported by one of them and paid for in accordance with the terms of the agreement need not originate in the other country, or, alternatively, that goods imported by one country and paid for under the agreement may be re-exported, or sold in transit. Or the partners may agree that a payment under the agreement shall be accepted for a commercial transaction between either of them and a third country.

A general relaxation of controls by one or both partners may involve the introduction of limited or unrestricted transferability of the bilateral balances held under various agreements. The introduction of transferability by one partner country for the benefit of others constitutes a facility which the others are welcome to use if they see fit.

Controls may be relaxed in a different way if one partner country, while officially and generally maintaining controls, allows its residents in certain cases greater freedom than would normally appear compatible with the rules of its bilateral arrangements. It may happen that the other partner country accepts these deviations, but it is also conceivable that the partner may find its interests damaged by the deviations.

Finally, private traders may succeed in dodging certain controls, especially those barring transit trade and/or prescription regulations, despite the best efforts of the authorities concerned to ensure their enforcement.

**Economic Interests**

Private traders have a commercial interest in buying and selling goods in the most advantageous markets, unencumbered by discrimina-
tory quota provisions and rules of bilateralism, which restrict their freedom of action. Their motive is to make a commercial profit. From the traders' point of view, profit possibilities are determined by the prices in various markets, recalculated at the rate of exchange between the foreign currencies concerned and their own currency. A private trader has no direct interest in particular currencies for their own sake. He has an indirect interest, however, to the extent that broken cross rates may affect his profit possibilities, and that either acceptance or availability of particular currencies may allow him to carry out certain profitable transactions that could not otherwise be concluded. This means that, in various cases (transit trade, circumvention of discriminatory restrictions, currency arbitrage through commodity transactions), private traders may see their profits increased if they can arrange roundabout transactions and/or apply unusual payments procedures. If these transactions are believed to be against a country's interests or inconsistent with its international commitments, the government may try to prevent them. But if the government has no strong negative feelings, it may not attempt to check the roundabout transactions, and it may even encourage them.

The interests that the exchange authorities themselves have in arranging, allowing, or condoning the use of bilateral balances for purposes outside the usual scope of the payments agreements involved may be of either a monetary or a commercial nature. Some governments have felt that such payments should be encouraged as a matter of general monetary policy and, therefore, have established certain conditions under which the automatic transferability of balances owed under various payments agreements is allowed. More frequently, however, the monetary considerations which prompt governments to waive the rules of monetary bilateralism are of an ad hoc nature. Those considerations arise notably when claims or debts under certain bilateral relationships have become excessive, and means are sought to correct the situation.

Normally, an excessive bilateral balance ought to be reduced by increased exports from the debtor to the creditor country, or by a payment in gold or in a third currency, but there may be reasons why a different procedure is applied. If B is the creditor in the bilateral relationship, a payment by B to A for goods imported by B from C, or exported by A to C, would likewise reduce B's excessive creditor position. For this purpose, the commercial transaction should present certain advantages for either bilateral country involved, or it should be acceptable to B—even at some sacrifice—if there is no other obvious way of reducing its outstanding claims.

Either government concerned may arrange the transaction necessary to attain the reduction of the bilateral balance (possibly, but not neces-
sarily, in agreement with the authorities of one or both of the two other countries concerned), or it may offer to its residents inducements or facilities (waiver of currency prescription, waiver of surrender requirements, import facilities outside usual quota provisions, broken cross rates, special import or export rates, etc.) that are likely to produce the desired result.

From the commercial point of view, a government may feel that its own discriminatory import policy, inspired by currency considerations, may be causing difficulties, since it deprives the country of desirable goods. Alternatively, it may find that its lack of competitiveness prevents it from selling certain export products in certain markets, although it may be eager to export those goods or to retain those markets, or both. In such situations, its aim may be to correct the trade situation by arranging or permitting indirect imports or exports (as the case may be). Since these transactions could not take place if they had to be paid for in the normal way, they have to be settled indirectly, i.e., in an inconvertible currency.

In some cases, commercial and monetary interests may run parallel. Under those conditions, a country may be able to arrange certain commercial transactions which it deems interesting and, at the same time, to correct the position of a bilateral payments agreement. In other cases, however, trade interests may prevail, and indirect payments may be used as a means to an end; the result may be that the position of the payments agreement, through which the settlement takes place, becomes more unbalanced than before, or it may be that the bilateral balance remains unaffected.

Whatever the motivation for transactions of the character described above, they may occur in three kinds of situation: First, the transaction may be commercially profitable at prevailing prices and under the existing exchange facilities; in that event, traders either will avail themselves of the opportunity without government permission, or will respond as soon as the authorities extend the necessary licenses. Second, if the special transaction can be carried out only at a loss at prevailing prices and under existing exchange facilities, the government will, if it wishes its traders to play their part, offer some kind of inducement (usually of a multiple currency nature) to compensate traders for the commercial loss they would otherwise incur. Third, if a loss is involved, the authorities themselves may decide to bear it, if they consider the transaction to be in the public interest.

If the third country does not have currency regulations, its authorities will not be involved.
Examples of cases 1 and 2 (Diagram 1) frequently arise when there are possibilities for the administrative or automatic transferability of balances from an account in one bilateral agreement to an account in a different agreement.

In the case of automatic transferability, an importer in one bilateral country can pay a supplier in another bilateral country in a third currency. The country whose currency has been made transferable will play the intermediary role which is necessary to effect the indirect payment. An export from Italy to Norway, for instance, could be paid for in sterling. Instructions on behalf of the Norwegian importer would be given to a U.K. authorized bank to debit a Norwegian sterling account and to credit the corresponding balance to an Italian sterling account.

Administrative transferability is sometimes practiced by Egypt. It may happen that Egypt wants to export cotton to, say, Japan, on which it has a bilateral claim, while at the same time it has a bilateral debt in its agreement with Greece. Such a situation would set the stage for an indirect payment through the Greek-Egyptian agreement, provided the Greeks are willing to receive and the Japanese to make an equivalent payment through the Greek-Japanese agreement. If the three exchange controls concerned give their consent, the transaction might develop in the way indicated. From the Egyptian point of view, the result would be that the cotton export to Japan does not increase its bilateral claim on Japan and helps to reduce its bilateral debt to Greece. In 1952, Sweden reduced its excessive debtor position vis-à-vis Japan by deliveries of rice from Thailand. At that time, Japan could not increase its direct rice purchases from Thailand without exceeding its quota under the Japanese-Thai trade agreement. In several cases, transactions of this type are carried out as transit transactions. For example, in order to reduce its debtor position with Brazil, Finland has re-exported to Brazil—against payments through the Brazilian-Finnish accounts—Argentine grains and commodities originating in West Germany, Sweden, and the United Kingdom.

If the transactions described above do not form a substitute for any country's right to claim gold or dollars for a balance in excess of the swing, they are likely to be carried out on a straightforward basis. This means that the commercial transaction will probably be concluded at its usual price, and that the two payments will be made at the correct

4 Illustrated by case 1, Diagram 1. For C in the diagram, read “Italy”; for B, read “Norway”; for A, read “United Kingdom.”

5 Illustrated by case 2, Diagram 1. For A in the diagram, read “Egypt”; for C, read “Japan”; for B, read “Greece.”
cross rates. The situation may be different, however, if the indirect payment through the bilateral agreement is arranged in lieu of a hard currency payment in the opposite direction, in order to reduce a balance in excess of the permitted swing.

Although many bilateral agreements provide for settlement in dollars beyond a certain point, debtor countries often do not actually pay dollars to their bilateral creditors when the need arises. This may be due to the fact that the debtor's dollar position renders it difficult or practically impossible to make such payments, while the creditor country perhaps does not want to press too hard lest it endanger its export possibilities. It may happen that, under these conditions, the two bilateral countries concerned agree upon a different procedure, which replaces the payment of dollars from A to B by a payment through the agreement from B to A, for goods imported by B from, or exported by A to, the dollar area.

In such a situation there are the following possibilities. The bilateral debtor may be willing to make dollars available for the purchase of U.S. commodities to be shipped to the creditor country, rather than pay dollars directly to the creditor country. The latter will pay for the U.S. goods through the bilateral agreement, thus reducing its excessive claim. The reason for this devious procedure may be that the creditor country is restricting its direct dollar imports, and that, consequently, dollar goods can be sold in its market at a certain premium. Under those conditions, the debtor country may be able to discharge its bilateral debt at a somewhat smaller sacrifice in dollars than if a direct dollar payment were made to its creditor. Apparently, the creditor country stands to lose, since it might have imported the same dollar goods at a lower price, if it had actually received the dollars due to it. It may, however, be willing to take this loss as the second-best possibility for reducing an excessive claim. Alternatively, the loss might be recouped if the creditor should allow the dollar goods to be resold to a third country at a profit.

Similar results may be obtained by a transaction of a different kind. The debtor country may undertake to export certain goods to the United States, the proceeds from which will be turned over to the creditor against a payment by the latter through the bilateral agreement. More usually, however, the bilateral creditor would re-export the debtor's commodities to a dollar country. Since soft currency goods exported to the United States are likely to yield less than when sold to a bilateral partner, this method is equally likely to present complications. The creditor country to which this solution is offered in lieu of a direct

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6 Illustrated by case 1, Diagram 1. For A in the diagram, read "Debtor"; for C, read "United States"; for B, read "Creditor."

7 Illustrated by case 2, Diagram 1. For A in the diagram, read "Debtor"; for C, read "United States"; for B, read "Creditor."
dollar payment would be faced with the same considerations as would arise in the previous case.

It may happen, of course, that the export from A to C is carried out with B as an intermediary, or from C to B with A as an intermediary, and not directly. If the trade transaction is arranged directly, both bilateral countries will probably be in agreement about the settlement involved. This may still be so if a transit transaction is organized, since the use of the other bilateral country as an intermediary may be purely a matter of convenience. A transit transaction may be necessary, however, because there is no agreement between the two bilateral countries concerned about the triangular transaction. One partner (either the debtor or the creditor) may take the initiative to correct a payments situation in accordance with its own convenience, but in a way of which the other bilateral country may not approve, or about which its opinion is not asked. The commercial transaction, although in reality a transit transaction, may then have to be disguised as a direct transaction.

Several cases are known in which countries have adjusted their bilateral debtor positions in excess of the swing by making special dollar allocations to their traders for the purchase of dollar commodities to be delivered to the creditor against payment via the agreement account, thereby obviating the need to settle with cash dollars the balances in excess of the swing. Arrangements of this nature have, for instance, been used in connection with excessive bilateral debtor and creditor positions vis-à-vis Japan. In the late months of 1952, West Germany and Sweden adjusted their debtor positions with Japan by selling Cuban sugar and other hard currency commodities to Japan against payment via the agreement account. The bilateral trade and payments agreement between Indonesia and Japan provides that Indonesia may offset part of its debtor position by selling to Japan dollar commodities up to US$15 million per year over the period 1952–57. Japan itself sold dollar commodities to West Germany and Sweden in late 1953, when an excessive creditor position had developed in favor of West Germany and Sweden.

During 1952 and 1953, West Germany imported approximately US$14 million of dollar goods at premium prices, paid via its agreement account with Yugoslavia, and frequently invited similar imports payable in bilateral currencies. During 1952, when the United Kingdom was making 100 per cent dollar payments to the European Payments Union, the U.K. authorities set up the “dollar commodity arbitrage scheme,” whereby U.K. merchants were authorized to purchase raw materials and foodstuffs for dollars, for resale to EPU countries against payment in sterling. The main purchasers of the dollar commodities resold by the United Kingdom appear to have been merchants in West Germany and the Netherlands. Although creditor countries seem frequently to have
agreed to the sale of dollar commodities payable through a bilateral agreement account, in some cases the creditor country refused such offers since the premium demanded by the debtor country was considered too high.

CASE 3

As has been shown above, cases 1 and 2 involve one commercial transaction (whether carried out directly or in two stages as a transit transaction), combined with two payments. Either the bilateral country receiving payment through the agreement gives up some other currency, or the partner making payment through the agreement is reimbursed in another currency. In case 3 (Diagram 1), on the other hand, two different commercial transactions are combined with only one payment. A third country imports from one bilateral partner and exports to the other, the settlement being made through the monetary agreement between the two bilateral countries.

This combination of transactions may be carried out on a prearranged basis, each country expressing its agreement about the various elements involved (type of good, price, manner of settlement). As previously mentioned, however, a different technique is more likely to be followed. The two commercial transactions are more likely to be concluded on their separate merits, the linking element being provided by the negotiation of an agreement balance in a hard currency market.

The third country involved in this type of transaction is not likely itself to have payments agreements with the other two. If it had, there would be little reason for the complications to which a transaction of this type gives rise. On the other hand, if the third country is a hard currency country, all parties involved may have an interest in the three-cornered arrangement, if the following conditions are met:

(1) Some traders in the third (hard currency) country must be interested in certain export transactions which cannot normally be concluded, since the soft currency importing country lacks the hard currency required and consequently discriminates against the commodities concerned.

(2) Other traders in the third (hard currency) country must be interested in import transactions which cannot normally be concluded, since the soft currency exporting country is not competitive at hard currency prices.

(3) The soft currency importing country must either be eager to receive the hard currency goods concerned against payment in a soft currency, or it must be anxious to reduce a net creditor position in a bilateral payments agreement and willing to import certain hard currency goods for that purpose.
(4) The soft currency exporting country must either be eager to export certain goods which it is unable to sell at hard currency prices, if necessary against payment in soft currency, or it must be anxious to reduce a net debtor position in a bilateral payments agreement and willing to forego dollar earnings for exports of certain goods to a hard currency country. This condition, however, may not apply if the commodities concerned are sold in transit without the knowledge of the exporting country.

Under a transaction of this type, a soft currency country (B) offers to buy certain hard currency goods against a “transit” payment to a dollar area exporter (usually a U.S. exporter) of a claim which it holds in a bilateral agreement concluded with country A. The U.S. exporter sells his claim to a U.S. importer, who is interested in buying certain commodities in country A. The U.S. importer then “retransfers” the bilateral balance to the exporter in the latter country, thereby canceling the original claim. The U.S. importer will be prepared to purchase B’s bilateral claim on A only at a discount, since it must be assumed that the exporting country is not competitive. The U.S. exporter will insist, therefore, that the amount in soft currency which he accepts in payment shall exceed its dollar equivalent, calculated at the official rate. As a consequence, the hard currency goods imported by B will be paid at a soft currency price and not at the (lower) hard currency price. The whole transaction, which could not have been carried out on a hard currency basis, materializes because of the sale of a bilateral balance at a discount by a U.S. exporter to a U.S. importer.

The technique of this sale must be examined more closely. A bilateral balance in a payments agreement cannot be transferred from hand to hand, like a banknote. It consists of a book entry, according to which a resident in one of the two countries holds a claim on a resident in the other, the residents concerned probably being authorized banks. There are normally only two ways in which such a claim can be passed on: it can be transferred to the name of a different resident of the country holding the claim, which leaves the status of the balance unchanged; or it can be transferred to the name of a resident of the country on which the claim is held, in payment for a transaction admitted under the agreement. This second way of passing on the claim extinguishes it as far as the bilateral agreement is concerned, since the nonresident balance (as viewed from the latter country) is thereby changed into a resident balance. In most cases, the claim will be registered in the books of the debtor country. Any transfer, therefore, requires an instruction by the

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8 Illustrated by case 3, Diagram 1. For C in the diagram, read “United States.”
9 The “debtor country” in this context, the country which owes a debt to a bilateral partner, is not necessarily synonymous with “net debtor country.” Under many bilateral payments agreements (i.e., those which provide for ac-
creditor to the debtor. Such an instruction must be compatible with the rules of the bilateral agreement. It appears extremely unlikely that under a bilateral agreement a person who is not a resident of either country could officially hold a balance in an agreement account. It follows that a balance under a payments agreement cannot be directly delivered to a U.S. exporter who might be willing to accept it in payment.

Any use of "agreement currencies" for transactions with U.S. exporters and importers, therefore, can be arranged only in a roundabout fashion. The balance has to remain outstanding in the name of a resident of the country which holds the claim, even though it is "transferred" to a U.S. exporter. The nominal holder of the balance agrees, however, to act as the agent of the U.S. exporter, and, subsequently, of the U.S. importer to whom the balance is sold at a discount. The latter can discharge his debt in soft currency only via the payments instruction which the nominal holder will give on his behalf to a bank in the debtor country. In practice, all parties may act through the intermediary of a single person, who acts as a link between the nominal holder, the U.S. exporter, and the U.S. importer.

Various dealers who act as intermediaries for this type of transaction issue lists of quotations, showing the discounts at which agreement currencies are being negotiated. In this connection, "agreement currency" stands for "a payment through the bilateral agreement between X and Y (expressed in whatever currency is used in that agreement as currency of account), payable by X to Y," or "payable by Y to X," as the case may be. "Discount quotation" stands for the percentage of discount of the clearing currency, so defined, compared with the relevant currency's official rate in terms of dollars.

It should be emphasized that an agreement currency is identified both by the contractual payments relationship between two countries and by the direction of the payment to be made. If a quotation shows a certain discount for "clearing dollars, X to Y," it means that X is importing dollar goods against payment in soft currency, while Y is similarly exporting its goods to the United States. If the quotation is for "clearing dollars, Y to X," it indicates that Y obtains dollar commodities, and X is doing the exporting. In practice, both quotations (referring to the counts to be opened in each partner country), there usually are claims and debts in both directions, the net position being determined by compensation of the accounts concerned. Although, at any given moment, there can be only one net creditor and one net debtor, each country may, at the same time, be both the other's debtor and the other's creditor with respect to individual balances before compensation.

10 It follows from the above that "the country which holds the claim" is not necessarily the net creditor.
same bilateral payments agreement, but applying to payments in opposite directions) may appear side by side. The economic significance of simultaneous quotations for payments in opposite directions will be explained later.\textsuperscript{11}

It is evident that a market where agreement currencies are traded under the above conditions cannot normally be considered a free exchange market. A clearing currency which is traded at a discount quotation is not just another quantity of effectively circulating international purchasing power; it remains a book claim locked up in a bilateral agreement, and usually inseparable from the commodity transactions which accompany it on its somewhat unorthodox excursion through a third country.\textsuperscript{12}

The conditions under which a bilateral country, B, may be willing to part with a claim on partner country, A, will be determined by the general restrictiveness of B's dollar import regime, by the type and price of the particular dollar goods which it may want to buy against soft currency, and by the position of its bilateral payments agreement with A. The last factor may exercise its influence indirectly, B being more ready to agree to the purchase of nonessential goods from C (presumably at a higher price in B's own currency) if its claim on A happens to be excessively large. The effective discount resulting from these considerations must be such as to enable a U.S. importer to buy certain commodities in A on an attractive basis. At the same time, A must be willing to approve or to tolerate the export of those goods to the United States against soft currency. Alternatively, the transaction must lend itself to being disguised in such a way as to evade A's trade or prescription of currency regulations, if A should not be willing to cooperate.

It may take considerable time and ingenuity to arrange these transactions and to bring all parties together at the right moment. Normally, C's goods will not be shipped to B, and the transaction between C and B will not be regarded as closed, unless the transfer from B to A has been effected and confirmed by the recipient bank in A. As a consequence, there is no way of foretelling whether a special transaction will turn out to be feasible, and what amounts it will involve. If one transaction has been approved or secured, the value of the other will have to match the amount of the bilateral balance used in the first transaction. In addition, traders may find it difficult to reach agreement on prices and other conditions, especially since prices will be related to the discount for the agreement currency in terms of dollars, and the latter may be determined only in the final stages of the negotiation.

\textsuperscript{11} See pages 191–92.
\textsuperscript{12} This does not apply fully to transactions with a dollar country financed in transferable sterling, since sterling balances can, in fact, circulate without hindrance among non-dollar countries.
In practice, therefore, the markets for “cheap” bilateral agreement currencies are likely to be narrow and erratic, and quotations may be intermittent. Unless information about the underlying transactions happens to be available, it is difficult to judge the economic importance of any quotation that may be published from time to time. The discount allowed on a certain inconvertible currency held in a bilateral account with another country does not necessarily reflect that currency’s real purchasing power in terms of dollars.

Furthermore, not all the discount quotations which may be obtained are “cheap currency” quotations, arising under a case 3 transaction. Some are theoretical calculations, in terms of dollars, of soft currency premiums established by case 1 or case 2 transactions, which do not involve the sale of inconvertible balances by a U.S. exporter to a U.S. importer.

From the point of view of the soft currency importing country, a case 3 transaction gives rise to a “switch import.” Since the customs officials are frequently able to check the country of origin, particularly of some staple commodities and of U.S. finished products, it seems that a soft currency country can exercise some control over these imports. In addition, it appears unlikely that an authorized bank in the importing country would “sell” a bilateral balance to a U.S. exporter (in clear conflict with the rules of the bilateral payments agreements concerned), if the central bank of the importing country were known to be opposed to such dealings. Countries may, however, permit or tolerate such imports, since they make possible the purchase of certain types of commodities for which dollars would not normally be available. Furthermore, as noted above, the authorities may tolerate, or even stimulate, these import transactions, if they are anxious to reduce large bilateral credit balances.

From the point of view of the soft currency exporting country, these transactions involve “switch exports” to the dollar area against receipts in clearing currencies instead of dollars. In exceptional cases, the authorities may be inclined to permit or tolerate such switch exports, e.g., when the transactions result in exportation of commodities which are hard to sell at prevailing prices and at the official rate of exchange. However, exports to the dollar area against payment in clearing currencies often take place against the wishes of the authorities in the exporting country. Available information indicates that the authorities have often found it

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13 This, too, does not apply to “cheap” quotations of transferable sterling.
14 The term “switch import” is used to indicate an import of dollar goods into a soft currency country against payment by the importer in a non-dollar currency, i.e., via the account of a bilateral payments agreement. Similarly, the term “switch export” denotes a transaction involving an export to the dollar area against receipt by the exporter of a clearing currency instead of dollars.
difficult to check these transactions. From the point of view of the trade and exchange control of the exporting country, the goods may be shipped to a country with which a bilateral agreement is in force; the shipping papers may indicate a port in the bilateral partner country as destination, payments being received via the clearing account with the partner country. After the goods have left the port in the exporting country, however, the original shipping papers may be revised, or replaced by new ones, to indicate a port in another country, e.g., the United States, as destination. The authorities in the exporting country may exercise some control by imposing an ex post check requiring a certificate of landing, of consumption, or of customs clearance to be sent from the bilateral partner country. This has been attempted particularly where important national exports, such as wool, coffee, or silk, were repeatedly switched to the United States. Even in such cases, ex post control may be difficult to implement, since, in order to be effective, it must be applied to many individual transactions, and since, in addition, falsification of documents is possible.

Transactions of the kind discussed here may be, but are not necessarily related to, an attempt to reduce outstanding agreement balances. In fact, as is indicated later, there appear to be many cases in which the transactions have the effect of increasing rather than reducing the agreement balance held by a net creditor country. When scarcity conditions prevail for certain dollar goods and importers in soft currency countries are willing to pay premium prices, or when U.S. exporters are trying hard to dispose of certain goods for which world market conditions are highly competitive, dollar exports may go to countries even when they are not in a net creditor position under the bilateral agreement via which the payment is made. Once clearing currencies are in the hands of a U.S. exporter, he will try to dispose of them by selling them to a U.S. importer. The U.S. importer is willing to acquire clearing currencies when the discount enables him to purchase soft currency goods at a price sufficiently competitive to make possible a sale in the U.S. market. Such cases may involve imports into the United States which would otherwise not have taken place, but the imports may actually be from countries that are already in a net creditor position under the relevant bilateral agreement.

Nature of Markets for Clearing Currencies

Since about the middle of 1952, the clearing currencies of various bilateral agreements have from time to time been quoted at a discount in dollars in a number of international trading centers. The most active
market for the negotiation of clearing currencies has probably been New York. This may be explained by the fact that, as noted above, most triangular transactions in case 3 involve hard currency countries, of which the United States is the most important. Because of the contacts between traders and intermediaries engaging in triangular operations, the quotations for clearing currencies in New York frequently apply also to transactions organized elsewhere and sometimes carried out with hard currency countries other than the United States.

Each discount quotation in the market usually arises as a result of two commodity transactions, carried out in combination by one or more traders, between the two agreement countries concerned. For instance, a discount quotation in New York for the "Argentine-West German clearing dollar, payment to Argentina" results from the negotiation of a certain amount of these clearing dollars between a U.S. exporter who has received them in payment for goods shipped to West Germany and a U.S. importer who wants to purchase them at a discount as a means of payment for imports from Argentina. The two commodity transactions—in this case the import of goods from the United States into West Germany and the export of goods from Argentina to the United States—are usually carried out at approximately the same time, unless an exchange broker is willing to take the risk of holding the clearing dollars. Thus, before the clearing currencies are negotiated, two commodity transactions must be arranged and, usually, effective payment through the agreement must have been made.\(^\text{15}\)

Although in most cases where clearing currencies are quoted at a discount the relevant negotiation takes place between traders in hard currency countries, traders in soft currency countries may sometimes be involved also; for example, when the resale to the United States of commodities originating in one partner country by traders in the other partner country is facilitated by special measures in the latter, such as a retention arrangement for the dollar proceeds from such transit sales, or a free market in which the clearing currency is negotiated at a discount. Instead of selling the commodities to the U.S. importers, the traders in the agreement country may dispose of their clearing currency balances by selling them at a discount to U.S. traders, who in turn use them to pay for commodity imports from the other partner country.

\(^\text{15}\) A discount quotation is frequently given for a clearing currency with the connotation "bid wanted" or "offer wanted." In such cases, clearing balances have not yet been negotiated at the time the quotation is published, since either the import or the export transaction with the United States still has to be arranged. However, these quotations indicate the approximate discount at which traders are willing to purchase or sell the clearing currency against dollars.
Factors Influencing Supply and Demand for Clearing Currencies Used in Trade with Hard Currency Countries

The supply of clearing currencies in the New York market, i.e., the amount of clearing balances received by or offered to U.S. exporters in payment for dollar goods, is dependent on a combination of factors, of which the general conditions favoring switch imports into non-dollar countries, and the willingness of U.S. exporters to accept such clearing balances in payment for their exports, seem to be the most important.

The effective demand for switch imports in soft currency countries is related, first, to the scarcity conditions for dollar goods prevailing in these countries, to the extent to which bilateral clearing currencies are available for making payments for such goods, and, finally, to the attitude of the authorities concerned toward switch imports. As previously stated, the authorities, when opening the door to switch imports, may be motivated either by monetary or by commercial considerations. If a country holds relatively large credit balances under some or several of its agreements, and at the same time maintains dollar restrictions, the authorities may be inclined to allow some of the holdings of clearing currencies to be used for switch imports of dollar goods, for which importers will be inclined to pay premium prices. The type of dollar import which a country can arrange on a switch basis is determined by its eagerness to divest itself of some of its bilateral claims (i.e., by the discount it is willing to accept for that purpose), and by the stringency of its restrictions on direct dollar imports. The latter factor will largely indicate what categories of dollar goods can be sold at prices whose premium corresponds with the discount at which its bilateral currency holdings can be disposed of.

When it allows switch imports, a country may, however, be looking primarily for commercial advantages, and a bilateral payments channel will then be used only as a means to that end. Under these conditions, a country may even offer to pay in a bilateral currency in which it already holds a short position, thus increasing its dollar imports at the risk of complicating, or perhaps compromising, the bilateral relationship concerned.

The willingness of U.S. exporters to accept clearing currencies in payment for dollar goods will, to an important extent, depend on their familiarity with this method of conducting business, and on their ability to dispose of the clearing balances which they obtain to U.S. importers or to middlemen. As previously explained, the transactions, although they may be profitable, cannot always be arranged promptly and smoothly. In general, the larger the discount at which clearing cur-
rencies are negotiated, the easier it is for the U.S. exporter to dispose of them, since a larger discount will enable the U.S. importer to purchase larger quantities or a greater variety of goods in the agreement countries concerned. However, even if the U.S. exporter has some difficulty in disposing of clearing balances, he may be willing to accept them when he has trouble selling abroad as a result of stringent dollar restrictions or of excess supply conditions in certain world commodity markets.

The demand for clearing currencies in the New York market arises from U.S. importers attempting to make purchases from bilateral agreement countries against payment in clearing currencies, and/or soft currency exporting countries being willing to approve or tolerate, or being unable to prevent, switch exports. When exports to the United States from the soft currency countries are overpriced, U.S. importers may be able to purchase such goods only when they receive some price concession, which may take the form of a discount against which they can purchase clearing balances to be used in import payments.

As a general rule, case 3 transactions appear to originate mainly in the bilateral importing country, either because that country has a strong demand for dollar goods, or because it wants to liquidate an excessive bilateral claim. The corresponding switch exports from the other bilateral country can, under those conditions, be arranged because the U.S. importer is being offered balances in cheap agreement currencies arising from the payment of switch imports into the country holding those balances. Although bilateral agreement countries usually oppose switch exports to the dollar area, these exports may be permitted or tolerated in order to promote the sale of overpriced exports, or, in exceptional cases, to help reduce excessive debtor balances, which the country concerned has not been able to pay off otherwise.

**Level of Discounts for Clearing Currencies**

Some idea of the actual discounts at which clearing currencies are negotiated between traders in dollar countries\(^\text{16}\) may be obtained from the quotations for various agreement currencies available in the New York market since about 1952. Clearing currencies of about 50 bilateral agreements have been quoted, some only occasionally but many others quite frequently.\(^\text{17}\) Some general conclusions may be drawn from the

\(^{16}\) Or between traders in a dollar country and a bilateral agreement country (see p. 186).

\(^{17}\) Some sources give quotations for many more bilateral agreement currencies, but those selected for study in this paper appear to be the more important ones representing most of the triangular transactions involving trade and/or payments under bilateral agreements.
quotations available on or about June 1, 1953 and June 1, 1954; the results are presented in some detail in the Appendix.

As already noted, dealings in clearing currencies are closely tied to the underlying commodity transactions. The discount quotations available for various clearing currencies should therefore be interpreted with care. Each quotation may reflect the market conditions for one or only a few commodities involved in the trade transactions concerned. They may not be indicative of the general scarcity conditions for dollar goods in the domestic market of the soft currency importing country, or of the extent to which goods from the soft currency exporting country are generally overpriced. The discount quotations for an individual clearing currency may indeed change rapidly with the market conditions for one or more of the commodities involved, or as different commodities are involved in the trade transactions which underlie the negotiation of clearing currencies.

In general, the discount for a clearing currency reflects the import premium in the soft currency country, i.e., the premium which the importer pays in his own currency for the dollar goods involved. The discount can exceed the import premium only if the U.S. exporter lowers his normal dollar price and absorbs part of the higher cost to the soft currency importer, which is the result of payment in a clearing currency. On the other hand, the import premium may exceed the discount in the New York market when importers in the soft currency country are able to make profits which are not fully absorbed by the loss on the sale of the bilateral balances involved. The discounts for clearing currencies will tend to go down when the import premiums fall. When dollar commodities in the domestic market of the non-dollar importing country become less scarce, as a result of relaxation of dollar restrictions, or of large-scale switch imports in the past, or other factors, import premiums and discounts for clearing currencies used in payments for switch imports into the country concerned will tend to decrease.

These observations are borne out to some extent by the actual behavior of the discounts for a number of different clearing currencies in June 1953 and June 1954. At both times, the discounts for clearing currencies used in payment for switch imports into countries where dollar restrictions had ceased to be very severe were considerably lower than those for currencies used in payment for such imports into countries where stringent restrictions were maintained. For instance, while discounts for clearing currencies used in switch payments by Belgium, West Germany, and the Netherlands did not as a rule exceed 5 per cent in June 1953, those for switch imports into Austria, Brazil, France, Denmark, and Yugoslavia were 10 per cent or higher. Moreover, in June 1954 discounts for clearing currencies were generally below those
for June 1953, except that the discounts for clearing currencies involved in switch imports into Brazil and Sweden were still about 10 per cent, and those for Japan increased from 6 per cent to approximately 10 per cent. Average discounts relevant for switch imports into Belgium had fallen from 5 per cent to 2.5 per cent, and those for imports into West Germany, from 6.5 per cent to 4.5 per cent.

Where more than one clearing currency is used in payment for switch imports by traders in the same country, the discounts for the various currencies frequently show considerable differences. Such differences may, of course, have no other implication than that individual transactions involved various import commodities for which internal market conditions in the soft currency country were widely different. In June 1953, however, there were a number of countries whose traders were purchasing switch imports, both with clearing currencies in which the countries had a net creditor position and with currencies in which they had a net debtor position. For practically all these countries, namely, Austria, Brazil, Finland, France, and Japan, the discounts tended to be considerably higher for currencies in which the importing country had a net creditor position than for those in which it had a net debtor position. These differences seem to indicate that switch imports against currencies of which the importing countries had a surplus involved commodities that were generally scarcer in their domestic markets than those imported against payment in currencies in which the countries had a debtor position. To some extent, this may reflect the attitude of the authorities in the countries concerned toward the use of clearing currencies in payment for imports from the United States and other hard currency countries. Where currencies in which the importing country had a net debtor position were used, the commodities involved tended to be those which were regarded as more essential and for which import premiums were lower than for luxury goods. On the other hand, where the importing countries had a net creditor position in certain currencies, the authorities concerned may have been more eager to dispose of their holdings; or, alternatively, if the bilateral debtor country was in over-all balance of payments difficulties, the authorities may have found that they could find a market for their holdings only if they agreed to accept a larger discount. As a consequence, a greater variety of commodities, including luxuries fetching relatively high premiums, tended to be imported in this manner.

Five other countries whose traders appear to have purchased switch imports with more than one agreement currency were either in a net debtor or in a net creditor position under all of the agreements concerned. The same was true for nine out of twelve countries whose traders appear to have purchased switch imports in more than one agreement currency in June 1954.
The discount for a clearing currency must also reflect the extent to which commodities sold to the United States by the non-dollar exporting country concerned are overpriced. These discounts may, indeed, reflect high cost-price levels either in individual agreement countries’ internal markets generally or in particular commodity sectors. Where an agreement country’s export commodities tend to be overpriced, a U.S. importer purchasing them against payment in clearing currencies must be able to obtain these currencies at a sufficiently high discount to make possible switch exports from the agreement country. If the discount is too low (e.g., as a result of importers in the other partner country being willing to purchase at only relatively small discounts), there will be a tendency to shift to export commodities that are more competitively priced. If that cannot be done, the transactions become more difficult to arrange, and eventually disappear.\(^\text{19}\)

If high-cost conditions are sufficiently widespread in a bilateral country, high internal prices may be expected to prevail for certain import goods, as well as for export goods. Thus, there are many individual cases in which the discounts for clearing currencies used in payment for switch exports and those relevant for switch imports (i.e., both for payments to be made to that country and for payments to be made by that country) are both relatively high. From the discount quotations for June 1954, it appears, for instance, that both switch exports from and switch imports into Brazil and Italy involved discounts of approximately 10 per cent. In most cases where discounts relevant for switch exports and imports of the same agreement country are available, they tend to be close together. In countries where cost-price conditions are generally not far out of line with those of hard currency countries, both types of discount tend to be low, e.g., in Belgium, where in June 1954 the clearing currencies involved in switch exports and imports were at a discount of approximately 2 per cent.

On the other hand, there are cases where the difference between the clearing currency discounts for switch imports and those for switch exports of the same country is relatively large. For instance, the discounts quoted in June 1953 showed such differences for Argentina, Italy, Spain, Spain.

\(^{19}\) This seems to have occurred during 1954 as a result of the decline in the discounts quoted for a number of clearing currencies in New York. It is understood that some firms specializing in this type of trade attempt to continue operations under a lower discount by combining the import and export transactions which otherwise might have been carried out by two or more traders separately. Some savings are achieved in this manner, since in this case no clearing balances are negotiated between exchange brokers and traders and the trading firms concerned do not have to pay fees to brokers. In addition, in most individual cases these so-called package deals appear to involve volumes of commodities sufficiently large to make the transactions worth while even at a smaller disparity in prices (for the goods concerned) between the United States and soft currency countries.
and Uruguay. Large variations in internal market conditions for the commodities which happen to be involved in these transactions may be responsible for the differences. Differences may also arise if, while a country's export prices are generally competitive, severe restrictions are maintained on certain luxuries, which therefore fetch relatively high premiums. Moreover, when imports into one partner country can be switched at a relatively high discount, it is possible that the clearing currencies concerned can be obtained by U.S. importers for making payment to the other partner country at a discount which does not necessarily reflect the exporting country's cost level.

Volume of Transactions and Their Effect on Bilateral Agreement Balances

Although accurate estimates are not possible, some general remarks may be made about the factors which tend to influence the total value and volume of commodity transactions involved in triangular operations. As indicated above, a decline in the discount at which a clearing currency is negotiated may make the underlying transactions more difficult to arrange. In turn, the development, on a large scale, of triangular operations involving the same bilateral agreement may bring about a fall in the discounts for the clearing currency concerned. Between 1952 and 1954, the discounts for several clearing currencies fell significantly, while the "market" for some of them tended to become less active. During that period, the underlying transactions may also have declined in total value, particularly where the credit balances held under the agreements concerned had been reduced. On the other hand, in some cases traders may have found it possible to continue the transactions, despite a decline in discounts, by organizing so-called package deals, not necessarily involving negotiation of clearing currencies (see footnote 19). The commodity transactions in these deals are essentially of the same nature as those for which clearing currencies are negotiated between traders in hard currency countries.

Despite a general downward tendency between June 1953 and June 1954, certain discount quotations remained relatively high, or even increased. This was particularly true for a number of bilateral agreement currencies of countries with relatively high domestic cost levels and/or intensive dollar restrictions. In these cases, some scope remained for the organization of switch imports and switch exports. It does not follow, however, that the clearing currencies of all bilateral agreements with high-cost countries are regularly involved in triangular operations. Those countries which have large bilateral debit balances in several pay-
ments agreements, and where internal market conditions are still relatively favorable to switch trade, do not represent a large part of the total demand and supply of commodities that may be transacted in triangular operations. For those clearing currencies that do become involved, it would seem, in fact, that periods of relatively intense market activity are frequently followed by periods in which few, if any, operations take place.

The commodity imports and exports involved in these triangular operations can be distinguished in the trade statistics of individual countries to only a very limited extent, if at all. For example, trade statistics do not specify imports (or exports) for which payments are made in clearing currencies. Only a few countries assemble statistical data on transit trade licensed by the authorities. But even where such data are available for transit trade in commodities originating in countries that are partner to bilateral agreements, they do not give an accurate picture of the scope of the triangular transactions under discussion here. These transactions are not necessarily part of transit trade, and from the point of view of individual countries they may appear as direct trade. Moreover, where transit trade in commodities purchased in agreement countries is recorded in a country’s trade statistics, the transactions represented do not necessarily involve the negotiation of clearing currencies at a discount. Finally, transit trade transactions may be carried out without the knowledge of the authorities of the countries concerned. Thus, even in the trade statistics that are available, it is virtually impossible to distinguish between transit transactions which involve “cheap clearing currencies” and those which do not.

In view of these limitations, the statistical material that is available in a few cases has to be interpreted with care. Some illustrations may be given for West Germany, whose trade statistics classify imports according to both country of origin and country to which payments are made. Imports into West Germany of goods originating in dollar countries exceeded those for which payments were made to dollar countries by $156 million in 1952 and by $173 million in 1953. Most of these dollar commodities were probably purchased against payment in EPU currencies (including sterling) and involved no clearing currency of a strictly bilateral nature. However, some of these goods may have been imported against payments via one or more of West Germany’s bilateral agreement accounts. This would seem to be supported by the fact that for five countries with which West Germany has bilateral agreements imports originating in these countries and shipped into West Germany fell short of the commercial payments which West Germany made to

20 In 1952 these countries were Brazil, Finland, Spain, Uruguay, and Yugoslavia. For 1953, Uruguay should be omitted.
them. In 1952 the difference was $26 million, or about 8 per cent of commercial payments to the agreement countries concerned; for 1953, it was $32 million, or about 11 per cent. This seems to indicate that West Germany made payments via the clearing accounts set up by the bilateral agreements with the countries concerned for significant amounts of goods not originating in the respective partner countries.21

**Effect on Countries' Bilateral Agreement Balances**

In the absence of complete information about the volume and value of triangular operations, no accurate estimates can be made of the changes which they cause in the bilateral agreement positions of the countries involved. The discount quotations in New York indicate which bilateral partner makes payments through a particular bilateral agreement, and which partner is receiving them. For instance, the transactions underlying a discount quotation for Brazilian-Italian agreement dollars payable to Italy—involving exports from Italy to the United States and imports of dollar goods into Brazil—result in a credit in favor of Italy on the Brazilian-Italian clearing account. Because of the net agreement position at the time the transactions took place, the switch exports from Italy may either have decreased Italy’s net bilateral debtor position under the agreement or increased its net creditor position. All that can be inferred from the discount quotation is the direction in which the agreement position moves as a result of the underlying transactions, the actual change being determined by the magnitude of the transactions.

In certain cases, there are simultaneous switch transactions in both directions. In the example given for the Brazilian-Italian agreement, this would be indicated by two quotations for the Brazilian-Italian agreement dollar, not necessarily equal—one for amounts payable to Italy and one for amounts payable to Brazil. Underlying the second quotation would be a transaction involving imports into Italy of dollar goods, financed with clearing currencies originating from payments for exports from Brazil to the United States. When there are two such quotations for one clearing currency, the net effect on the bilateral clearing position of each of the partner countries cannot be determined, unless the magnitudes of the transactions in opposite directions are known.

It may be remarked, incidentally, that the existence of simultaneous

21 Because of leads and lags between trade and payments, these amounts do not necessarily equal the differences of $26 million in 1952 and $32 million in 1953, recorded above. These figures would represent a minimum when goods originating in the agreement countries concerned were also purchased via third countries. It should be noted that imports originating in Argentina exceeded commercial payments to Argentina by $22 million in 1952 and $21 million in 1953.
quotations, showing discounts for payments in opposite directions under the same bilateral payments agreement, tends to indicate a lack of cooperation, or even of agreement, between the two countries concerned. From a monetary point of view, it does not appear to make sense that one partner should be reducing an outstanding balance at the same time that the other is increasing it. From a commercial point of view, the combination of two cheap currency transactions in opposite directions produces the result that each partner both imports from and exports to the United States at soft currency prices. If this result were intentional, it might have been achieved in a simpler fashion, with each country carrying out its own business. The fact, however, that the more devious and complicated procedure of executing two cheap currency transactions is resorted to supports the thesis that, generally speaking, countries are actively interested only in the import part of these transactions, and that the export part is usually organized without the knowledge of the authorities concerned.

The discount quotations of various agreement currencies, in combination with the available information about the net position of the corresponding agreements at the time, suggest that the underlying cheap currency transactions, taken together, probably have been more or less evenly divided between those tending to reduce and those tending to increase existing net agreement positions. But in June 1953, the transactions taken together probably tended to reduce clearing positions, particularly since various countries at that time were trying to dispose of excess credit balances.

In June 1953, the currencies of some 49 bilateral payments agreements were known to be negotiated at a discount in New York. For 13 of these agreements, the discount quotations indicated transactions in both directions, so that they tended, at least in part, to offset each other insofar as their effects on the existing agreement positions were concerned. The quotations for the currencies of the 36 remaining agreements indicate that transactions carried out under 17 of them tended to reduce agreement positions, while those under 12 tended to increase them. For the remaining 7 agreements, the effect on the agreement positions resulting from the transactions cannot be determined, since no information is available as to which of the partner countries held the net debtor, and which the net creditor, position.

A similar examination for June 1954 of 35 agreement currencies listed at a discount in New York shows that 20 of them were used for transactions in opposite directions, and their effects on the agreement positions of the countries concerned tended to offset each other. Transactions under 7 of the remaining agreements tended to increase agreement positions, while transactions under 8 agreements tended to decrease them.
The effect of the transactions on existing bilateral agreement positions may be illustrated in somewhat greater detail by reference to individual countries. From the discount quotations in June 1953, it may, for instance, be concluded that the underlying transactions tended to have a balancing effect on the bilateral clearing position of Argentina. Switch exports from Argentina tended to reduce its net debtor position vis-à-vis Austria, Belgium, Denmark, Finland, the Netherlands, Norway, and Sweden. However, the currencies of the agreements with Brazil, France, West Germany, Italy, and Japan were used for both switch exports from and switch imports into Argentina. On the other hand, in June 1954, Argentina’s net creditor position vis-à-vis Yugoslavia tended to be increased as a result of switch exports. Argentine traders paid for switch imports via the agreement accounts with Austria, Belgium, France, Italy, and Sweden, but the effect on Argentina’s bilateral payments position was offset at least in part by switch exports from Argentina with payments via the accounts of the same agreements. However, Argentina’s net debtor position vis-à-vis West Germany tended to be increased as a result of switch imports.

There appears to have been no general tendency in the effects which switch exports and switch imports had on the bilateral payments position of Brazil. The New York quotations in both June 1953 and June 1954 suggest that there were then 14 agreements in the currencies of which switch exports and/or switch imports took place. In June 1953, there were transactions in opposite directions (i.e., involving switch exports from and switch imports into Brazil) against payment via the agreements with Argentina, France, West Germany, Italy, and Sweden. The currencies of the other agreements were used only in payment for switch exports from Brazil, and their effect on Brazil’s existing clearing balances did not tend to be offset by payments for switch imports into Brazil. Thus, switch exports tended to decrease Brazil’s net debtor position vis-à-vis Belgium, Chile, Denmark, the Netherlands, and Spain, and to increase its net creditor position with Austria, Finland, Japan, and Yugoslavia. In June 1954, there were transactions in opposite directions under the agreements with Austria, France, West Germany, Japan, the Netherlands, Sweden, and Yugoslavia. However, switch exports tended to reduce Brazil’s net debtor position vis-à-vis Spain, and switch imports tended to decrease its net creditor position vis-à-vis Belgium and Greece. On the other hand, payments for switch imports into Brazil, made via the agreements with Belgium, Finland, Italy, and Norway, had the effect of increasing Brazil’s net debtor position vis-à-vis those countries.

Switch imports of goods into Yugoslavia are indicated by the discounts quoted in June 1953 for payments through Yugoslav agreements with Argentina, Brazil, France, Italy, and Turkey. The transactions
had the effect of increasing Yugoslavia's net debtor position vis-à-vis those countries. In June 1954, when 8 clearing currencies were listed for Yugoslavia, the effect of the underlying transactions on its bilateral agreement balances was more mixed. There were transactions in opposite directions in the currencies of agreements with Austria and Brazil. Yugoslavia's net debtor position with Argentina and the Netherlands tended, however, to be decreased by switch exports, while its net creditor position vis-à-vis Norway tended to be decreased as a result of switch imports. On the other hand, switch imports had the effect of increasing its net debtor position vis-à-vis Greece, Italy, and Turkey.

The discount quotations recorded for Finland in June 1953 indicate that switch transactions involved imports into Finland rather than switch exports from Finland. They had the effect of increasing its net debtor position vis-à-vis Brazil, France, and West Germany, and of decreasing the net creditor position existing at the time vis-à-vis Argentina. In June 1954, the discount quotations indicated that both switch imports and switch exports took place against payment in the currencies of the agreements with Belgium and France. However, Finland's net creditor position vis-à-vis Argentina was decreased by switch imports, while switch exports from Finland tended to reduce its net bilateral debtor position with West Germany. On the other hand, switch exports tended to increase its net creditor position with Brazil.

Since the middle of 1954, activity in the New York cheap currency markets has tapered off to a considerable extent. Transactions of the kind examined in this paper have become much less frequent than they were in 1953 and during the first part of 1954. As a consequence, it has become practically impossible to obtain quotations for 1955 which indicate any particular trend. A few traders continued to issue lists of quotations, but these seemed to show the levels of discount at which they would be inclined to solicit bids or offers, rather than transactions actually concluded.

Various causes cooperated to produce this decline of the cheap currency market. Fewer bilateral payments agreements were as manifestly out of balance as they had been previously and, on the whole, governments appeared less tolerant of these practices than before. The countries which used to import dollar commodities through the procedures described above had less interest in trade of this kind. In many cases, import restrictions against dollar goods had been relaxed or abandoned. In addition, import transactions financed in transferable sterling (which was traded in the second half of 1955 at less than 1 per cent discount) offered a less costly procedure for obtaining dollar goods against non-dollar payments. Since most cheap currency transactions originated in the countries importing the dollar goods involved, the declining interest on their part in this type of trade undoubtedly reduced the scope for
cheap currency deals. In particular, the organization of an “area of limited convertibility” by Brazil, and similar other arrangements, and the overhaul of the Argentine exchange system that was undertaken toward the end of 1955, contributed toward the decline of the cheap currency market.

By the end of 1955, little business in cheap currencies was being contracted. However, dealers occasionally still managed to conclude a transaction. It was felt that, if monetary conditions developed further toward normal, the cheap currency market was bound to disappear. However, its revival was possible if countries should once more find themselves in monetary difficulties.

APPENDIX

Observations on Discounts for Clearing Currencies Quoted in New York in June 1953 and June 1954

It has already been explained that there are usually two commodity transactions underlying each discount quotation of a clearing currency. Thus, in the case of a quotation for Argentine-West German clearing dollars (payment to Argentina), the underlying commodity transactions are (1) the export of Argentine commodities to the United States and (2) the export of U.S. commodities to West Germany. A 10 per cent discount for clearing dollars indicates that a U.S. exporter could sell a commodity costing US$90 for 100 clearing dollars received from West Germany. He could then sell these clearing dollars for US$90 to a U.S. importer. The U.S. importer would thus pay US$90 for an Argentine commodity costing 100 clearing dollars. When an exchange broker is involved, the discount quotation usually refers to the middle rate; at the usual broker’s fee of about 1 per cent, the U.S. exporter would receive US$89.50 for 100 clearing dollars, and the importer would pay US$90.50 instead of US$90.

The transactions underlying the available discount quotations in June 1953 involved switch imports from the United States (or other hard currency countries) into the following agreement countries: Argentina, Austria, Belgium, Brazil, Chile, Denmark, Finland, France, West Germany, Italy, Japan, the Netherlands, Norway, Spain, Sweden, Uruguay, and Yugoslavia. The same discount quotations seem to indicate that these switch imports were combined with switch exports to the United States (or other hard currency countries) from the following agreement countries: Argentina, Brazil, France, West Germany, Italy, Japan, the Netherlands, Spain, Sweden, Turkey, and Uruguay. Transactions underlying the discount quotations in June 1954 involved switch imports into the following bilateral agreement countries: Argentina, Austria, Belgium, Brazil, Finland, France, West Germany, Italy, the Netherlands, Spain, Sweden, Uruguay, and Yugoslavia; and switch exports to hard currency countries from Argentina, Austria, Belgium, Brazil, Finland, France, West Germany, Greece, Italy, Japan, the Netherlands, Norway, Sweden, Turkey, Uruguay, and Yugoslavia.

The discount quotations available for June 1953 and June 1954 have been studied (1) by comparing the discounts in June 1953, applicable to switch imports into the United States (or other hard currency countries), to those in June 1954; and (2) by comparing the discounts in June 1953, applicable to switch imports into the following agreement countries: Argentina, Austria, Belgium, Brazil, Chile, Denmark, Finland, France, West Germany, Italy, Japan, the Netherlands, Spain, Sweden, Uruguay, and Yugoslavia. The same discount quotations seem to indicate that these switch imports were combined with switch exports to the United States (or other hard currency countries) from the following agreement countries: Argentina, Brazil, France, West Germany, Italy, Japan, the Netherlands, Spain, Sweden, Turkey, and Uruguay.

22 An export commodity that is sold for 100 clearing dollars to a bilateral partner country may sometimes be offered to a U.S. importer for a smaller amount, if payment is made in effective U.S. dollars. If that price were US$95, it would still be worth while for the U.S. importer in the hypothetical case under consideration to buy the commodity concerned against a “cheap” currency.
into individual agreement countries, with those in June 1954; (2) by comparing discounts relevant for switch exports from individual agreement countries with those for switch imports into the same countries; and (3) by comparing the discounts for currencies of agreements under which the importing country had a debtor position with those under which it was in a creditor position.

(1) The available data suggest that, for June 1953 and June 1954, there were traders in at least 14 agreement countries purchasing switch imports, payments being made via the accounts of two or more bilateral agreements. In general, the discounts quoted in June 1954 were lower than those in June 1953. In 1953, there were 11 soft currency countries where importers carried out transactions involving discounts of 10 per cent or higher; these countries were Austria, Brazil, Chile, Denmark, Finland, France, Italy, Spain, Sweden, Uruguay, and Yugoslavia. On the other hand, switch imports into Belgium, West Germany, and the Netherlands involved discounts for clearing currencies in terms of dollars of 6 per cent or lower. Between June 1953 and June 1954, all discounts relevant for switch imports into these 14 countries decreased, in most cases considerably, except that for switch imports into Brazil and Sweden average discounts remained approximately 10 per cent and for switch imports into Japan the discounts increased from 6 per cent to approximately 10 per cent. In June 1954, traders in Japan, Spain, and Sweden appear to have paid import premiums of 10 per cent or more for switch imports from the dollar area. Relatively low discounts were involved in payments for switch imports into Belgium (2.5 per cent), West Germany and the Netherlands (4.5 per cent), and Uruguay (2 per cent).

(2) The June 1953 data show that the discounts relevant for switch exports from, and those for switch imports into, individual agreement countries were close together in some cases, e.g., Brazil, France, West Germany, and Japan, but relatively far apart in others, e.g., Argentina, Italy, Spain, and Uruguay. The average discount quotation for transactions involving switch imports into Brazil was 10 per cent, and for transactions involving switch exports, 11 per cent. The corresponding percentages for other countries were Argentina, 9 and 16; France, 12 and 10; West Germany, 6½ and 6; Italy, 10 and 7; Japan, 6½ and 5; Spain, 20 and 7; and Uruguay, 14 and 5.

Similar comparisons on the basis of the June 1954 data could be made for Argentina, Austria, Belgium, Brazil, Finland, France, West Germany, Italy, Japan, the Netherlands, Sweden, and Uruguay. For each of these countries, except Japan, switch imports and switch exports appear to have involved discounts for clearing currencies which were close together, the average difference in most cases being less than one point. Switch exports from and switch imports into Brazil, Italy, and Sweden involved discounts for clearing currencies of approximately 10 per cent. On the other hand, discount quotations relevant for switch export and switch import transactions with traders in Belgium and in Uruguay were approximately 2 per cent, and with those in West Germany, approximately 4½ per cent.

(3) As noted above, the available discount quotations for June 1953 indicated that traders in 14 countries purchased switch imports against payment in one or more clearing currencies. Of these 14, there were 12 where payments for switch imports took place through two or more of their bilateral agreements. Five countries (Argentina, Belgium, the Netherlands, Sweden, and Yugoslavia) were consistently in either a net debtor or a net creditor position under all of the agreements through which payments for switch imports were made. However, payments for switch imports into Austria appear to have been made through both agreements under which Austria was in a net creditor position and agreements under which it was in a net debtor position. The same applies to payments for switch imports into Brazil, Finland, France, and Japan. In all of these cases, the discounts for currencies in which the importing country had a net creditor position tended to be considerably higher than those in which it had a net debtor position.

A similar comparison could not be made for June 1954, since most of the countries (9 out of 12) for which more than two quotations were available had either a net debtor or a net creditor position in all of the payments agreements through which payments for switch imports were then being made.