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Monetary and Financial Co-operation in Asia: Markets and Institutions

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Introduction

Eastern Asia and South-East Asia have been at the forefront of global economic growth since the 1950s; they have also been the first in a series of several financial crises. This paper considers the monetary and financial co-operation that took place in Asia from a historical perspective.

Compared to the American and European experiences, monetary and financial co-operation in Asia demonstrates a fairly different picture. Since the end of World War II, international financial aid had been offered to the region suffering from scarcity of trade currencies, but a plan like the ‘Asian Marshall Plan’ had never been implemented. In the meanwhile, Western European countries co-ordinated reciprocal settlements through the European Payments Union (EPU). In the 1950s, ‘Hot Wars’ were fought in Korea and Vietnam. Until the 1980s, Asian governments and monetary authorities

1 This is a temporary draft and should not be used for citation. Graphs and tables will be circulated at the session.

2 In this study, ‘Asia’ refers to the region that is approximately similar to the region that is made up of the member countries of the United Nations Economic Commission for Asia and the Far East (ECAFE), including Hong Kong. Other countries in this region, like the People’s Republic of China and the Democratic People’s Republic of Korea, are not included in this geographic category. In those days, ‘China’ was represented by the Nationalist government in Taiwan.
managed economy and trade through restrictions. With regard to the banking business, the ‘American challenge’\(^3\) was more prominent in Asia than in Europe, and there were fewer opportunities for ‘co-operation’ between American international banks and the Asian banking sector. In fact, there was no concept of a single currency or economic integration in this region. However the tide of financial globalisation swept over the shores of the Asian markets, making monetary and financial co-operation a necessity.

This paper aims to present an overview of events regarding the monetary and financial co-operation in Asia from a historical perspective. More precisely, from the viewpoint of this session, the following questions require consideration.

(1) During the period after World War II and prior to the return to convertibility in Europe, intraregional trade was active among some Asian countries (ECAFE members)\(^4\). Thus, the initial condition for intraregional co-operation between Western Europe and ECAFE members in Asia was similar. What are the circumstances that led to such considerably different results in these two regions during the period following World War II?

(2) During the Bretton Woods period (1958–1973), economic development in Asia was achieved under severe government restrictions: trade barriers were high and numerous regulations controlled the exchange market. Unlike the situation in Europe, these state-led measures lasted throughout the period from 1958–1973 and even until the 1980s. Why were the Asian authorities able to maintain these measures for such a long time despite the rise of market mechanisms like the Euro-currency market?

(3) At the end of the 1960s, when the international forums began to make collaborative efforts towards maintaining the Bretton Woods adjustable-peg system, co-operation

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\(^3\) Cf. Stefano Battilossi and Youssef Cassis, eds., *European Banks and the American Challenge: Competition and Cooperation in International Banking under Bretton Woods*, Oxford University Press, Oxford, 2002. My aim in this paper is to portray the situation with regard to the American challenge in Asia in contrast to that in Europe that has been portrayed in this informative book.

took place gradually in Asia. What kind of co-operation did the international forums (BIS, IMF, G10 etc) propose to the Asian nations?

If we consider international monetary and financial co-operation from the narrow perspective, it would refer to the formal co-operation between governments and central banks. If this terminology is strictly adopted, it would imply that intraregional co-operation in Asia took place only after the 1980s. Thus, based on this definition, this paper will not present a ‘history’ but merely a ‘pre-history’ of international monetary and financial co-operation in Asia. However, from a broader perspective, this type of co-operation has existed in this region since earlier times, often in informal ways. This loose definition allows some scope for discussion on the ‘history’ of the subject in this paper.

This paper draws on the archival sources of the BIS, the Bank of Japan, and the Ministry of Finances of Japan. Some oral archives have also been referred to. Due to limited access to the archives in the Asian countries, the relevant data has been obtained from Japanese documents.

1. Intra-regional cooperation in Asia: Regional circumstances during the pre-convertibility period

Monetary and financial co-operation in Asia has long involved only a one-way transfer. This co-operation began with Anglo-American aids and Japanese reparations, and later developed into consultations and credits provided by international institutions (IMF and IBRD).  

*International transfer: Aids and reparations in Asia*

By the late 1940s and early 1950s, the dollar gap constituted a bottleneck for the Asian economies. This initial condition was similar in Western Europe but the output was quite different. European economies, initially facilitated by the Marshall

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5 Due to certain restrictions, certain testimonies are to be referred to only verbally at the session.
Plan Aid\(^7\), achieved their surplus towards the US sooner than their Asian counterparts; on the other hand, the Asian countries could not achieve the same goal until the late 1960s.

Although there was a certain transfer of liquidity in this region during the late 1940s and early 1950s, it was on a smaller scale than that in Europe. The most important transfer was that pertaining to American aid. As shown in figure 1a and 1b, the Asian-Pacific region took up approximately 16% of the economic aid distributed by the US. This sum was much less than that provided to Europe (which totalled to 74%), including the aid provided by the Marshall Plan. However, taking into consideration the ratio of the sum to the national income, the aid given to Japan and the major Western European countries was almost equal\(^8\).

Another transfer was that of Japanese reparation payments towards South-East Asia. In the San Francisco Peace Treaty that was signed in 1951, Japan agreed to pay reparations to Burma, the Philippines, Indonesia and South-Vietnam; in sum, this reparation, coupled with the development loan known as ‘quasi-reparation’, amounted to 170 million dollars. This sum was fairly small compared to the initial demand of approximately 3000 million. The payment began in 1955 and lasted until 1976 (figure 2). During this period, the transfer contributed towards establishing the economic infrastructure of South-East Asia, and of course, the Japanese export of capital goods\(^9\).

What was the contemporary opinion on the above aids and reparations? The most controversial issue in those days was the possibility of implementing the ‘Asian Marshall Plan’. In 1949, several statements referring to this plan were published in the US, including the statement made by the Secretary of State, Dean Acheson. Asian political leaders, including Premier Nehru of India, visited the US to request such aids. However, by October 1949, it was almost clear that it was impossible to implement the

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‘Asian Marshall Plan’. According to a contemporary analysis, the reasons that this plan was abandoned, were as follows: American opposition to the plan, particularly from the Republicans; the Communist victory in China, which discouraged the efforts of the plan to establish a closer intraregional trade network; the opposition of Asian entrepreneurs to the plan due to the fear that it would introduce American capital; and most importantly, the nature of the social and cultural structures in Asia that made the distribution of the fund more difficult than in Europe.\(^{10}\)

It is presumable that the absence of the ‘Asian Marshall Plan’ made international co-operation difficult in this region. However, among the various factors that instituted post-war Asian monetary regimes, the most important one from our point of view is the antagonism between the US and the UK over the key currency in this region.

*Anglo-American antagonism over hegemony in post-war Asia*

After the defeat of Japan in World War II, two great powers, the UK and US, were in conflict over hegemony in Asia. The concurrence first occurred in the field of diplomacy: the US proposed the ‘Pacific alliance’\(^{11}\), while the UK, supported by the pound-sterling, rushed to reconstruct its official and unofficial Empire.\(^{12}\)

One of the central issues in this diplomatic conflict was the view on China and Japan. In general, the UK attempted to open China as a great market, even after the establishment of the Communist power. The US, on the other hand, was more hostile towards a China that was led by Mao and proposed to make Japan a keystone in its strategy to win the Cold War. Today, it is well known, after recent historical studies, that this antagonism was more complex than it appeared. The US government had

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conflicting views on ‘China supporters’ and ‘Japan supporters’\textsuperscript{13}; Great Britain, on the other hand, was not completely hostile towards Japan, as this country was necessary in order to rebuild the sterling area in Eastern Asia\textsuperscript{14}. However, it was commonly held that the Americans gave priority to Japan, Taiwan, the Philippines as well as South East Asian countries\textsuperscript{15}.

What was the result of this antagonism? Since the details surrounding the victory of the dollar have already been established in previous studies, in this study, we only cite an archival record of the Bank of Japan, which provides a description of the contemporary situation: this intensive research paper has been entitled ‘Which should Japan belong in the future, dollar area or pound-sterling area?’\textsuperscript{16}. According to this paper, which was written in 1951, the dollar was superior to the pound from the viewpoints of ‘stability, convertibility and the possibility of introducing foreign capital’. Regarding trade balances, it was true that in those days, Japan had close trade relations with the sterling area, particularly on the export side (export from Japan to the sterling area). However, the problem was on the import side: there was an imbalance between the demand and supply of materials that Japan imported from the sterling area. In other words, the sterling area was only profitable for Japanese export but not for the import. Based on these notions, the Bank of Japan proposed to increase exports both to the US and the neutral countries that lay between the dollar and pound-sterling areas (Indonesia, Thailand, Taiwan and Korea).


**Figure 3** shows the consequence of this decision—the use of the dollar and the pound-sterling as foreign-exchange currencies in this region. It is noteworthy that the use of the pound-sterling lasted until the 1960s and carried immense weightage. In other words, despite the above observation concerning Japan, the dollar could not prevail in the Asian markets.

The abovementioned circumstances are probably well known; however, a slightly different view has been proposed by a recent testimony: despite negative conditions, Asian countries *desired* intraregional co-operation.

*‘Asian Payments Union’ rejected by Japan*

From the beginning of the 1960s, several plans to set up the ‘Asian Payments Union’ had been discussed at the ECAFE. Among those plans, one of the most influential was the proposal by Robert Triffin, theoretically inspired by the Keynes’ proposal of the International Clearing Union in the Bretton Woods Conference. The plan was to launch a multilateral payments system among Asian countries in order to encourage intra-Asian trade. In this Triffin Plan, neither dollar nor sterling was to be used as a transaction currency\(^{17}\).

Many representative ECAFE member-countries consented to this plan but Japan rejected the idea. According to former Vice Minister of Finance for Foreign Affairs of Japan, Yusuke Kashiwagi (1917–2005), who recently made an important testimony, the reason for Japan’s rejection was that ‘once that kind of framework would be set up, then Japan would be forced to offer credit to Asian countries, periodically and with no limit’\(^{18}\). In his defence, Kashiwagi provided an excuse stating

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\(^{17}\) “Roundtable discussion— Japan and Development of Asia, on Prof. Triffin’s APU Concept”, in *The Oriental Economist*, November 1968, pp.26-38.

\(^{18}\) Keikichi Honda and Tadao Hata, eds., *Kashiwagi Yusuke no Shougen, Sengo-Nihon no Kokusai Kinnyushi [Testimony of Yusuke Kashiwagi, a History of International Finances in Post-war Japan]*, Yuhikaku, Tokyo, 1998, p.28. It must be noted that Kashiwagi’s testimony has some important errors. Kashiwagi himself said that the plan for the APU was first published in the 1950s, but it was in the late 1960s that the plan has come out. Cf. Ken’ichi Odawara, “International Monetary Cooperation in Asia—some views and comments on the problem during the negotiations to conclude the Agreement establishing A.C.U.” in *Chochiku Keizai Riron Kenkyukai Nenpou*, vol.20, March 2005.
that ‘in those days, no one could predict that Japan would become the surplus country it
is today’; however, he admitted that the refusal of the ‘APU’ plan was inappropriate.
‘To tell the truth’, Kashiwagi said, ‘in the late 1950s, we have been haunted by the fear
of running short of foreign currencies, and the catch-up to Europe and America took
priority over all others. The idea of approaching to Asia has been poor’. Instead, when
Asian Development Bank (ADB) was founded in 1965, this time, Japan consented and
occupied the seat of the Governor\(^{19}\).

Although Kashiwagi made statements in defence of his stance, his judgement
was, in a sense, sound: an IMF Staff Paper reported in 1969, ‘Rarely is the currency of a
country of the region used to settle payments between two other countries of the region’.
The authors of the report, who were optimistic with regard to regional co-operation in
general, criticised that ‘there is no evidence in any of the countries (belonging to
ECAFE) of official action or intention to encourage a substantial use of the domestic
currency as a general means of settlement’\(^ {20}\).

In other words, the target of the monetary policy and exchange control in the
Asia of those days was to secure the foreign exchange reserve. However, due to difficult
trading conditions, Asia was unable to accumulate a sufficient stock of foreign reserves:
no local currency had been circulated in a wider regional area.

Eventually, the payments union plan was modified and took shape as a regional
currency union—Asian Clearing Union (ACU). It was founded in 1975, with 7 member
countries, including India, excluding Japan\(^ {21}\). Adopting Triffin’s idea, the unit of
account in this ACU area has been made equivalent to the Special Drawing Right
(SDR) of the IMF, not the American dollar\(^ {22}\).

\(^{19}\) Honda and Hata, eds., [Testimony of Yusuke Kashiwagi], op.cit.
\(^{20}\) Mookerjee, Chandavarkar and Cleary, ‘Existing International Banking and Credit Facilities in the
ECAFE Region’, IMF Staff Papers, op.cit., p.425.
\(^{21}\) Initial members were Bangladesh, India, Iran, Nepal, Pakistan, Ceylon (Sri Lanka), and Burma
(Myanmar). Butan joined the Union later in 1999.
\(^{22}\) ECAFE/RC/TF/22, “Preliminary Draft Agreement for the Asian Payments Arrangements” (Dr.
Ken’ichi Odawara), 19 February 1970.
2. State-led management of exchange market: Government restriction and market mechanism in Asia

In general, state-led growth in the Asian countries can be explained from the commonplace point of view of development. However, with regard to monetary and financial policy intervention, which hampered the international co-operation in this field, certain exceptional factors might have been influential. Two topics need to be considered at this juncture. Firstly, the European return to convertibility affects the condition of Asian trade, and government restrictions on Asian imports have become stricter. Secondly, in order to cope with the scarcity of foreign reserves, a new technique will be introduced into the exchange market (with regard to this second issue, we could only take up the Japanese case due to lack of archives).

Impact of the European return to convertibility

From 1958 onwards, the European currencies restored convertibility. With the dissolution of the EPU and the foreign exchange restriction being taken over, the countries of Western Europe entered a period of economic growth with free trade. Even though the liberalization was limited to the short-term exchange market, this ‘return to normalcy’ encouraged European trade and paved the way for economic unification. Figure 5 shows the improvement of the terms of trade for Western European countries due to the convertibility.

On the other hand, a bitter situation emerged for the Asian countries. As can be seen from figure 5 above, the terms of trade worsened for almost all the countries in the region; other indexes on figure 6a and 6b also indicate the backwardness of the Asian trade. From the figure 7a and 7b, we can observe a long term development of trade in Europe and the opposite picture in Asia.

Why were the results of the return to convertibility so different between the two regions? The reason for this can be explained from two perspectives —short term and long term. Regarding the short term, the recession that occurred in most of the developed countries in 1958 led to this difference. While the Europeans prepared the way for free trade and market unification, the Asians were passive in receiving the effect of the recession. In the late 1950s and early 1960s, most of Asia still functioned under a mono-culture economy, depending on the export of raw materials. Thus the
short-term effect of the 1958 recession appeared harsher, particularly on the export side. However, the long-term effect was more important. Due to the trade deficit resulting from a decline in exports, the Asian countries (particularly the South-East Asian nations) faced a severe scarcity of foreign reserves. In order to cope with this short-term crisis, they introduced a long-term measure—import restriction. An unpublished study of the Japanese Ministry of Foreign Affairs summed up the situation as follows: during the 1958 return to convertibility, ‘the Western European countries secured a footing towards liberalization, while the developing countries strengthened the regulation due to recession’ 23.

Finances for trade: Usance facilities

The import restriction has been combined with the regulation on the transaction of import bills. Let us now study the Japanese case. Like almost all Asian countries, Japan suffered from the scarcity of foreign exchange reserves throughout the 1950s and until the end of the 1960s. Figure 8 represents a long term movement of Japanese trade balance accounts. A chronic lack of export often led to acute crises of exchanges, almost every four years 24. In order to cope with this difficulty, the Ministry of Finance and the Bank of Japan instituted a special budget known as the ‘foreign exchange budget’. The aim of this budget was to purchase exchange bills from western banks based in Japan with an exceptionally favourable rate for the banks. The sum of the bills was then borrowed by Japanese banks and merchants from the Bank of Japan under the label of ‘Import Usance’ 25 (figure 9a).

This financial technique has its origin in the bills that were issued mainly in the New York exchange market during the interwar period. Such bills were called ‘Far

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Eastern Advance Bills’ and were issued by American banks for use in export finances that were forwarded to the Eastern Asian region. The initial aim of the bills was to secure remittances for export goods that were shipped over long distances. Later, in 1950, the Bank of Japan applied this technique to ‘Import Usance’\textsuperscript{26}. Normally, this usance facility is offered in a discount market. In fact, the Bank of England does not offer this type of bill.

However, in Japan, where the discount market was small and inactive, the central bank had to work for the usance facility, using the government budget resources. A similar system appears to have existed in contemporary West Germany and Thailand. Figure 10a and 10b indicate the amount of the usance facility offered by the Bank of Japan to the domestic banking system. By distributing this usance judiciously through the different seasons of the year, the Bank of Japan attempted to diversify the period of settlement. If not, the import of raw materials and agricultural products would lead to seasonal fluctuations of remittances, which was quite dangerous with respect to maintaining a certain level of exchange reserves. A government committee known as the Foreign Exchange Control Committee decided upon the commodities that were to be imported using this usance facility. In this context of trade deficit and exchange scarcity, state intervention was necessary.

However, it should be added that state intervention was, at the same time, profitable for certain international bankers; in fact, three American banks (the National City Bank, the Bank of America and the Chase National Bank) were particularly chosen to offer usance, not only through the Bank of Japan but also by their proper account. Under state regulation, these banks (later, also the Netherlands Bank and the Bank of Indo-China) enjoyed a position of privilege in the Japanese foreign exchange market. In 1950, the average discount rate of the usance bill amounted to 9%, of which 4% was paid by domestic Japanese banks and the remaining 5% was paid by the importers\textsuperscript{27}. So

\textsuperscript{26} Detailed explications and data on usance facilities in Japan are provided in Ministry of Finance of Japan, \textit{Showa Zaiseishi [Financial History of the Showa Era]}, vol.15, Toyo Keizai Shinousha, Tokyo, 1976, pp.148–227.

\textsuperscript{27} Bank of Japan, Investigation Bureau, ‘Sengo wagakuni no boueki kinnyuu no suii to genjou’ [‘A Retrospect and Present Stage of Foreign Trade Finance in Our Country during the Post-war Period’], August 1964, in Bank of Japan, ed., \textit{Nihon Kinnyuushi Shiryou [Selected Documents...]}, op.cit., p.29.
long as the foreign exchange scarcity continued in Japan and the state continued to intervene, ‘rent seeking’ by these foreign banks brought them high profits.

This Japanese scenario of state-led regulation combined with high profits in the international banking business presents a fine contrast with Hong Kong, where the laissez-faire principle in international finance succeeded in attracting foreign banks. In other words, both markets—Tokyo and Hong Kong—attracted international banking, but due to differing causes: the ‘state’ and the ‘market’ were conflicting in Hong Kong, whereas they were not necessarily opposing in Japan.

Finally, the Japanese authority abolished the ‘Foreign Exchange Budget’ system in 1963, following consultation with the IMF. These state-led measures were incompatible with the obligations listed for an Article VIII country. Above cited Kashiwagi, who was a high-ranking official at the Ministry of Finance in those days, said in retrospect that ‘from our viewpoint today, the Japanese policy decision of staying as an Article XIV country for more than ten years seems extremely prudent; but the contemporary authorities were equally haunted by the fear of the lack of foreign exchange’.

3. BIS and G10 cooperation efforts in Asia: The period of the downfall of Bretton Woods

During the heyday of the Bretton Woods system, financial innovations progressed in the European markets, particularly in London. In the mid-1950s, the Euro-currency market began to develop, and Euro-currency banking was first introduced. From the mid-1960s, however, the adjustable-peg system encountered

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29 Honda and Hata, eds., *Kashiwagi Yusuke… [Testimony of Yusuke Kashiwagi…]*, op.cit., p.32.


How did international co-operation at this stage of the Bretton Woods system influence Asian countries? Reconsidering the Japanese case, we shall investigate the archives of the G10 meetings as well as some contemporary oral information.

\textit{The Euro-currency market and the Japanese banking system}

During the 1960s, despite being approved by the IMF as an Article VIII country, Japan faced a chronic lack of foreign exchange reserves. In an interview, a former Bank of Japan official stated that in the autumn of 1967, the dollar reserve declined and became less than $2 billion, which was then considered as a dangerous level. Faced with a crisis, the Bank of Japan began a secret negotiation with the IMF to borrow the sum in the form of a special tranche. The response of the IMF was bitter, demanding high-threshold conditionality.\footnote{Author’s interview with Mr Y..., (29 May 2003).}

A similar picture emerges from the archival records of the Bank of Japan, reporting the BIS Governors’ meeting, which was held in Basle in July 1967. Jelle Zjilstra, the President of the meeting, announced, as follows: ‘what we need to watch carefully, besides the US and Italy, is Japan’. An official from the Bank of Japan, Daisuke Hoshino then mentioned the foreign exchange difficulty in Japan as a defence;
however, Milton Gilbert, head of the Monetary and Economic Department of the BIS, pointed out that ‘Japan has entered a stage of early warning’.

Under these circumstances, the rise of the Euro-currency market was welcomed, particularly by the Japanese banks. As mentioned in the previous section, Japan had to pay a high rate for the import usance bill. The rate of interest for the Euro-dollar had also been high in the London market but it was even lower in comparison with the Japanese domestic usance rate. Thus, Japanese banks welcomed the Euro-currency market. In fact, in early 1964, a G10 meeting referred to the Japanese borrowing of the Euro-dollar thus: ‘In Japan the Euro-dollars made up a part of the substantial foreign borrowing by Japanese banks in 1961 and have continued to be a source of credit, particularly for the finance of Japanese foreign trade, since then’. The report, written by an anonymous writer to ensure confidentiality, states that ‘the amounts involved appear to have run into several hundred million dollars, but more precise indications cannot be given because large sums were also borrowed directly from the United States’.

It should be noted that during this phase, unusually, the Japanese borrowing of Euro dollars elicited a nervous reaction from a US representative. In a Working Party 3 Meeting of the OECD, held in Paris in 1966, this American representative insisted on making the following statement: ‘a surplus country should avoid requesting the import finance abroad’. This criticism was targeted at Japan, who was rapidly increasing its use of the Euro dollar. In response to this criticism, the Japanese representative expressed disagreement, stating that ‘for a country like Japan, where the banks depend upon the foreign bankers for import finances, this kind of sudden change is not acceptable’.

Development of the swap network: Specific role of the BIS

In response to the financial innovation that took place in the 1960s, several new techniques were invented (or some old ones were revamped) in international forums like...
the G10 and the BIS. From our point of view, one of the most important techniques is
the ‘swap’ operation.

From the beginning of the 1950s, the BIS conducted a ‘swap’ operation, mainly with the Bank of England; under this operation the BIS offered dollars to this central bank and got pounds in return\(^\text{36}\). It was agreed that in case these Treasury Bills were not profitable enough, the BIS, as a commercial bank, would invest the sum elsewhere\(^\text{37}\). The BIS, with the co-operation of commercial banks in London, could have deposited up to 50 million dollars of convertible currency in the term account in these private banks\(^\text{38}\). Thus, the ‘swap’ agreement had a close relation with the Euro-currency operation, although the BIS itself was not aware of it. Later, in the published statistics, the BIS regarded its own swap operation as a constituent of the Euro-currency.

The swap operation played another important role at the beginning of the 1960s: in the agreements on international monetary co-operation\(^\text{39}\), subsequently signed in 1961, ‘swap’ became an important means to ensure co-operation between monetary authorities. Moreover, in December 1963, H. Mandel, the Head of the Banking Department of the BIS, proposed a multilateral ‘swap’ network among central banks; this was referred to as the ‘Gold-Exchange Swap’, in which the BIS was an essential agent. According to Mandel, the return of European national currencies to convertibility was ‘incomplete’ since the new system had been run by the dollar. The primary

\(^{36}\) BIS Historical Archives, 2.2, vols.3 and 4, ‘Conversation téléphonique avec la Banque d'Angleterre, Londres (MM. Preston, Bridge-O.Berntsen)’, 16 Juin 1954, 16.00h. On the use of the word ‘swap’ in the BIS, the oldest date that the author confirmed from the archives of the 15 October 1949, in the conversation of Marcel Van Zeeland, the BIS head of the Banking Department, with the French finance official François Bloc-Lainé. Archives de la Banque de France, 14892003/188, ‘Swap B.R.I. en faveur du Trésor’, 15 Octobre 1949.

\(^{37}\) According to a confidential analysis by the BIS, a certain opinion in the Bank was rather against the investments on the British Treasury Bills. Cf., BIS Historical Archives, 2.2, vols.3 and 4, DHM, ‘B.I.S. investments in UK Treasury Bills’, 5 July 1956.

\(^{38}\) BIS Historical Archives, 2.2, vols.3 and 4, Aide memoire for Monsieur Guindey, 26.2.59, confidential.

\(^{39}\) The Basle Agreement in March 1961 and the Gold Pool Agreement in October 1961.
intention of Mandel’s program was, therefore, intended to avoid a possible dollar crisis using the ‘swap’ network among the central banks and the BIS. How did the international institutions apply this ‘swap’ to Japan? An unusual proposal was made by the BIS. In November 1966, during a monthly meeting of the BIS, a Bank of Japan official held a conversation with Gabriel Ferras, the General Manager of the BIS. Ferras said that he would appreciate if the Bank of Japan would increase the deposit to the BIS in the future. Following the General Manager, the Head of the Banking Department Donald Macdonald presented the following proposals:

(1) BIS would explore transactions with consecutive central banks, following each requirement.
(2) For Japan, manipulation is sometimes inevitable to avoid excessive fluctuations in foreign reserve.
(3) In order to achieve this, the BIS and the Bank of Japan would enter into gold transactions only after booking. BIS would deposit a certain amount of gold in the Japanese account. The Bank of Japan could pay a certain interest into the BIS account.
(4) Since there would be no nominal transfer of gold in this transaction, BIS would be able to treat this transaction confidentially. Past transactions of this kind have not been leaked to the FRB.

What was the Japanese reaction to these attractive proposals? Although there is no direct evidence found in this regard, we discovered a letter of gratitude, which was written in English. Executive Director, Haruo Mayekawa, future Governor of the Bank of Japan, wrote as follows in August 1967: ‘I wish to thank you most sincerely… for your kind proposal to offer us a revolving swap facility of US$100 million against yen to enable us to head off any serious difficulties in our balance-of-payments situation’.

40 Mandel’s plan was expressed in a confidential letter addressed to a Swedish central bank manager. Cf. BIS Historical Archives, 1/3a(3), Meeting of Experts [Euro currency market], correspondence, H.H. Mandel to Gunnar Akermalm, Manager, Sverigs Riksbank, 3rd December 1963, personal and confidential.
41 Archives of the Bank of Japan, correspondence, Head of Foreign Affairs, ‘BIS Gutsureikai narabini OECD Kaigi shusseki no sai choushu shita jikou ni kansuru houkoku (1)’ [‘A report on the matters informed on the occasion of the BIS Monthly Meeting and the OECD Meeting (1)’], November 1966 [restricted document]. The report has been written in Japanese, but the word ‘manipulation’ has been written in English.
Mayekawa rejected the proposal this time, but he added that ‘I shall therefore keep in mind the proposal you have so kindly thought out for us’, and ‘I am looking forward to visiting BIS at the September meeting… I would like to talk with you further about this matter on that occasion’.  

The aim of currency swaps in the era of fixed exchange rates was ‘to enable the monetary authorities to retain control over the course of events’. The problem, however, was with the way in which the swaps were proposed. Unlike the IMF and its bitter conditionality, the BIS preferred back-door negotiation, which proved to be rather helpful for the developing countries in Asia.

However, while the BIS was welcoming Japan with simple conditions, a serious dispute ensued between the FRB and the EEC over the dollar swap network. This dispute was symptomatic of the impending dollar crisis in the 1970s.

**Dollar swap network: FRB versus EEC**

The dispute occurred at the Multilateral Surveillance Meeting held in the BIS in February 1966. At this meeting, the Western European countries presented the concept of ‘harmonisation’ of foreign reserves: since the foreign dollar surplus of the European public sector reserve displayed an upward trend, Western European countries attempted to strike a balance between the rates of the dollar and gold reserves in Europe and the US. From the European perspective, buying gold out of the dollar reserves would decrease their liquidity; therefore, they demanded that the Americans, too, support the gold market in co-ordination with the European countries. However, the US authority, represented by Coombs from FRB, rejected this idea. According to Coombs, it was the responsibility of the surplus countries to provide credit to deficit countries. Mayekawa, the future Governor of the Bank of Japan, who recorded the above debate on his memorandum, noted this antagonism to be ‘interesting’.

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42 Archives of the Bank of Japan, correspondence, Haruo Mayekawa, Executive Director, to Donald Macdonald, August 9 1967 [restricted document].


Despite the above European critique, the FRB had widened its swap network facility to as much as 4500 million dollars in September 1966 in order to avoid dollar depreciation\textsuperscript{45}. The swap operation under this scheme has not been reported publicly to the multilateral surveillance body: the swap itself was a purely independent operation, which was carried out by the closing Central Banks (and occasionally by the BIS).

At this point, a new antagonism emerged. The EEC put forth criticism of the American swap network. At the Multilateral Surveillance Meeting in December 1966, the EEC—which had gained a seat as a member—expressed its opinion that the FRB swap network was almost automatically withdrawn, mainly by the US authority; this weakened American discipline with regard to the management of its balance of payment. In response, Coombs justified the stance of the US stating that the swap operation required a bilateral agreement, which constituted a conditional liquidity that rarely exceeded the term of nine months. Coombs also stated that the objective of the American swap operation was to reverse the dollar deficit of the past, which implied no new deficits whatsoever\textsuperscript{46}.

The discussion between the Governors lasted two hours. The general impression was that even if the swap network were still useful, its size would have to be enlarged, thus altering its significance; this in turn implied that in the case of a further increase, a discussion in the BIS would be necessary\textsuperscript{47}. The essential problem pertained to the delicate relationship between the swap network and the multilateral surveillance scheme: To what extent could the international co-operation body intervene in the affairs of each central bank?

With regard to the Asian context, the FRB-EEC debate also led to debates on the ‘swap’ operation: the US built its own swap network; the Europeans criticized the US network; the BIS informally proposed a swap network to Japan; the Europeans proposed co-ordination on gold price; the US refused; and the argument continued… A thorough reconstruction of the international monetary and financial co-operation was


\textsuperscript{46} Ibid.

\textsuperscript{47} Ibid.
about to be undertaken in the 1970s, and the Asian countries would be forced to decide whether or not they wished to rely on the swap network.

Concluding Remarks

To sum up, let us answer the three questions presented at the beginning of this paper:

(1) What are the circumstances that led to such considerably different results in Europe and Asia during the period following World War II? A one-way transfer of funds and the division of currency areas prevented the Asian countries from realizing a plan of the APU.

(2) Why were the Asian authorities able to maintain these measures for such a long period, despite the rise of market mechanisms, such as the Euro-currency market? To limit our discussion to trade finance, it should be stated that balance-of-trade deficits caused a number of Asian countries to introduce exchange restrictions and state-led usance facilities. These measures lasted for such a long period because this was necessary under the worsened terms of trade after the 1960s. The weakness of the ‘Asian banking response’ towards the ‘American challenge’ allowed a certain rent-seeking behaviour into Western international banking.

(3) What kind of co-operation did the international forums (BIS, IMF, G10 etc) propose to the Asian nations? During the period of collaborative effort to maintain the Bretton Woods system, the BIS proposed the ‘swap’ agreement to Japan. Unlike the stringent conditions of the IMF, the BIS approached the prospective borrowers of the ‘gold swap’ in an informal and simple manner.

As has been summed up above, a familiar ‘state versus market’ diagram was not so clear in Asia: state-led trade finance measures were in a particular relation with international banking business. Internationally, too, back-door negotiation co-existed with market-oriented co-operation.

After the end of the Bretton Woods system in 1971 and the arrival of the floating exchange system in 1973, the dollar was no longer convertible to gold. Thus,
the Gold Pool and gold swap faded out. However, it is interesting to note that on one occasion in 1975, the Bank of Japan attempted to purchase gold in the open market. This attempt was unsuccessful because of the American objection. However, the concept of ‘reserve harmonisation’ endured informally during the 1970s, and finally bore fruit in the form of the Chinese-yuan- Japanese-yen swap agreement in the 1980s. The international monetary and financial co-operation in contemporary Asia can be assumed to have its origin in the co-operation under the Bretton Woods system, which took place between the force of market and the institutional decision-making.

48 Author’s interview with Mr X…(27 January 2003), Mr Y… (29 May 2003), Mr Z...(8 September 2003).