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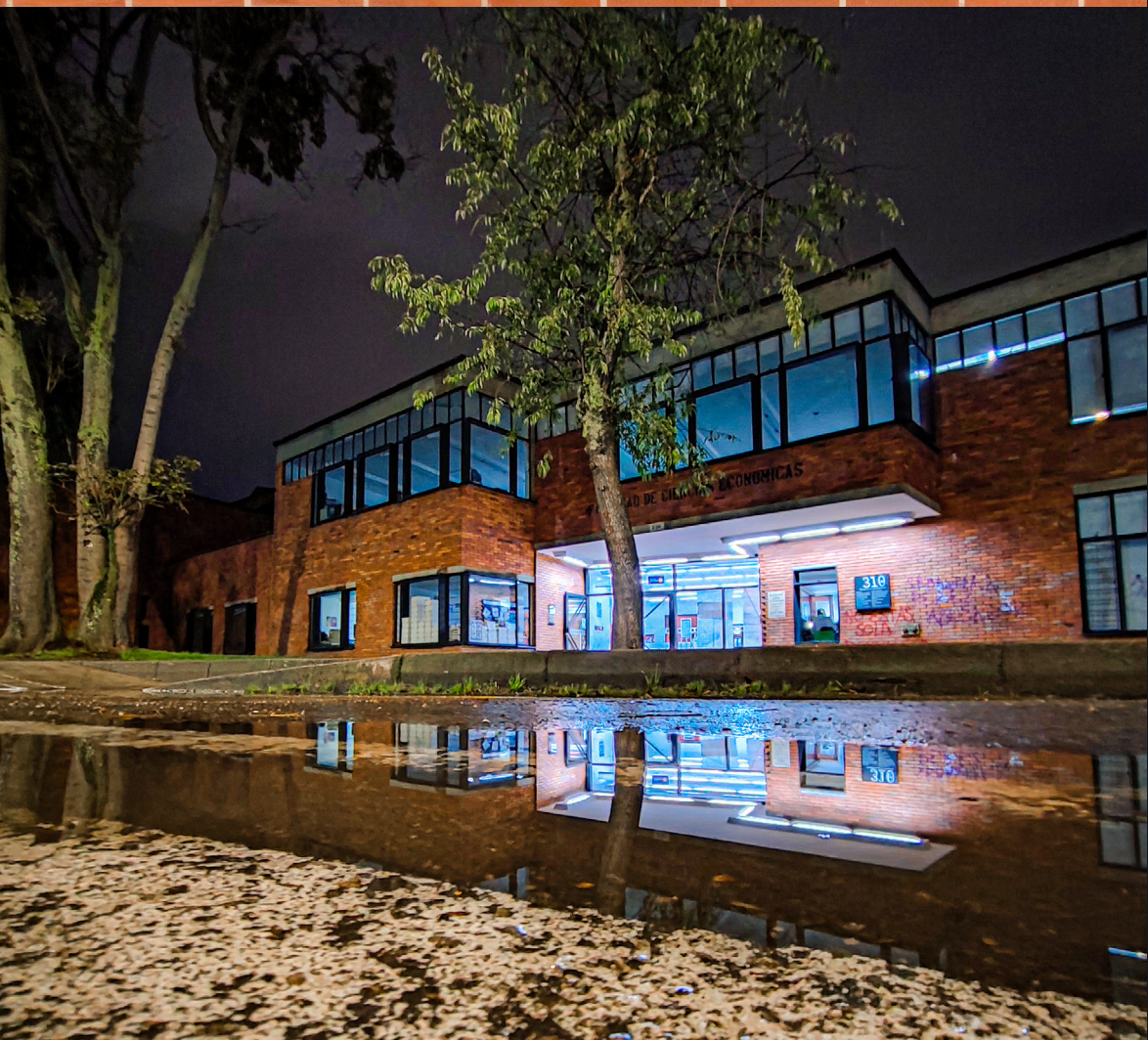
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REGIONAL PAYMENT AGREEMENTS: AN ALTERNATIVE TO CURRENCY CONVERTIBILITY?

Marcelo Bruchanski
Andrea Molinari

Bruchanski, M., & Molinari, A. (2023). Regional payment agreements: An alternative to currency convertibility? *Cuadernos de Economía*, 42(88), 23-41.

Regional Payment Agreements (RPAs) replicate, on a regional scale, John M. Keynes's proposal at the Bretton Woods Conference, based on the recording and subsequent clearing of transactions. The analysis of the three "founding" RPAs from the Golden Age (Finland-USSR, European Payments Union and the LAF-TA-LAIA Agreement on Reciprocal Payments and Credits) suggests that, in

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general, these agreements fulfilled their objectives: saving foreign currency and promoting trade. Hence, RPAs would present an alternative to currency convertibility for current account transactions.

Keywords: International monetary arrangements and institutions; International institutional arrangements; Keynes; Keynesian; Post-Keynesian; Modern monetary theory; International economic order and integration.

JEL: F33, F55, E12, F02.

Bruchanski, M., & Molinari, A. (2023). Los Acuerdos Regionales de Pagos: ¿una alternativa a la convertibilidad monetaria? *Cuadernos de Economía*, 42(88), 23-41.

Los acuerdos regionales de pagos (ARP) replican a escala regional la propuesta de John M. Keynes ante la Conferencia de Bretton Woods, sobre la base del registro y posterior compensación de las transacciones. El análisis de los tres ARP “fundacionales” de la Edad de Oro (Finlandia-URSS, Unión Europea de Pagos y el Convenio de Pagos y Créditos Recíprocos de ALALC-ALADI) sugiere que, en términos generales, estos acuerdos cumplieron con los objetivos propuestos: el ahorro de divisas y la promoción del comercio, por lo cual se infiere que los ARP presentarían una alternativa a la convertibilidad monetaria para las transacciones corrientes.

Palabras clave: instituciones y acuerdos monetarios internacionales; acuerdos institucionales internacionales; Keynes; keynesianos; post-keynesianos; teoría monetaria moderna; orden económico internacional e integración.

JEL: F33, F55, E12, F02.

INTRODUCTION

The widespread adoption of currencies convertible to the US dollar was one of the major trends in the late twentieth century. Towards the end of the 1950s, Western Europe began using convertible currencies for current transactions, and peripheral countries also moved in this direction, albeit more slowly. Furthermore, after the dissolution of the Union of Soviet Socialist Republics (USSR), even former socialist countries integrated into international payments through currency convertibility (Braga de Macedo et al., 1996).

One of the best-known theoretical alternatives to currency convertibility for current transactions was the International Clearing Union (ICU), designed by John M. Keynes, submitted by Great Britain to the Bretton Woods Conference in 1944. Although the US plan prevailed and the ICU was not implemented, the main ideas emerging from Keynes' proposal could be contrasted at a regional level through Regional Payment Agreements (RPAs).

From a historical perspective, RPAs predate the ICU, since their use grew in the 1930s thanks to the key role played by Germany. At the end of the Second World War, within a context of hard currency shortage, RPAs increased exponentially, both among capitalist countries and between capitalist and socialist nations. Conversely, the International Monetary Fund (IMF), led the currency convertibility paradigm, advising countries to remove any kind of discrimination from current payments, such as RPAs (de Vries, 1969).

After the collapse of the Bretton Woods Agreements (in 1971), financial deregulation caused many balance-of-payments and foreign exchange crises, mostly manifested during the 1990s. This resulted in extensive literature concerning financial account regulations and macroprudential policies. However, current account convertibility has not received the same academic attention. The present international context, where countries such as China or Russia use their own payment systems and domestic currencies for international trade, represents a major challenge to the currency convertibility trend. Peripheral, and particularly Latin American, countries should evaluate these changes carefully. In addition, different macroeconomic theories, such as the "Dominant Currency Paradigm" (Gopinath & Itskhoki, 2021) or the "Currency Hierarchy" (de Paula et al., 2017), study the reasons why the predominance of the US dollar in international transactions can be problematic. This paper assumes that RPAs are an alternative to currency convertibility, and that these agreements have historically served to promote trade within a context of hard currency shortage.

Apart from this introduction, the paper includes six sections. The first one describes the objectives and the operation of the main precedent of RPAs: the Keynes Plan, while the subsequent section characterises the main attributes of RPAs. Sections three to five summarise the background, historical context and main objectives and operation of the three cases that we consider to be the "founding" RPAs: Finland-USSR, the European Payments Union (EPU) and the Reciprocal Payments

and Credits Agreement (CPCR, in Spanish) of the Latin American Free Trade Association (LAFTA) and the Latin American Integration Association (LAIA). The choice of these RPAs was based on three criteria: (i) historical context, since all of them were signed during the so-called “Golden Age” of capitalism (a period between the second post-war and the fall of the Bretton Woods Agreements); (ii) diversity of the countries considered, since the first agreement links a socialist economic system with a capitalist one, the second one includes mainly central capitalist countries, and the third one involves peripheral capitalist nations; and (iii) economic and geopolitical importance of participating countries.¹ Finally, the sixth and final section concludes by comparing the agreements assessed.

THE KEYNES PLAN

RPAs are considered an extension of the British proposal prepared by John M. Keynes for the 1944 Bretton Woods Conference (Aragão, 1984; Fritz et al., 2014; Kaderbeck, 2019; Kregel, 2017; UNCTAD, 2011; Varela Parache, 1966). The so-called “Keynes Plan” proposed the establishment of an International Clearing Union (ICU) to register, clear and settle all international payments.

After the war, Keynes refused to return to a freely convertible gold standard, primarily due to the fact that such a system would lead to a contraction in global aggregate demand (Keynes, 1980). Under a *laissez faire* framework, the burden of adjusting external imbalances would fall only on deficit countries and capital flows would cause financial instability, preventing the implementation of sovereign economic policies to expand aggregate demand.

The ICU proposed by Keynes was based on three components: the adoption of the “banking principle”, the expansive adjustment of chronic external imbalances, and the control of speculative financial flows. Since the banking principle uses the clearing house as an alternative payment system, it dispenses with money as a means of payment and restricts bank operations to bookkeeping customer accounts. In other words, banks are limited to offsetting assets with liabilities and credits with debits. Thus, a bank loan would be the exchange of a current debit for a future credit (Keynes, 1980; Kregel, 2017).

At an international level, the ICU would use a common unit of account (called “Bancor”), with a fixed parity to gold (which could eventually be changed). The central banks of member countries would keep an account in the ICU to settle their bilateral balances at a fixed parity defined in terms of the Bancor. Countries running a surplus with regards to the rest of the world would have a creditor position

¹ Other relevant RPAs are, for example: the Central American Clearing House, the Asian Clearing Union, the SUCRE (Unified System for Regional Compensation) among ALBA countries, the SML (Local Currency Payments System) between MERCOSUR countries, or the REPSS (Regional Payments and Settlement System) of the Common Market for Eastern and Southern Africa.

in the ICU, whereas those running a deficit would have a debit balance (Keynes, 1980).

In other words, based on the banking principle, the ICU enables trade between countries without using an international currency (and currency convertibility). External surpluses would result in credits extended to the ICU. However, given that the Bancor was only conceived as a unit of account, it could not be bought or sold. Moreover, an exchange market or the hoarding of international reserves by central banks for transactional or precautionary motives would not be necessary (Kregel, 2017).

In addition, as those credits extended within the system would be automatic,² in order to avoid chronic imbalances, it was necessary to tackle the excessive accumulation of credits and debits, without placing the burden of such adjustment only on deficit countries. That is the reason why each country would receive an annual quota based on the volume of its international trade. Keynes proposed charging an interest rate for both creditors and debtors.³ If a creditor country exceeded half of its quota, it would have to apply several measures (such as appreciating its exchange rate with respect to the Bancor or reducing its import tariffs) to restore the balance (Aragão, 1984; Keynes, 1980). This adjustment scheme, in line with Keynes' (1936) ideas regarding effective demand, encouraged deficit countries to expand their exports to surplus countries, instead of restricting their imports.

Last, but not least, the Keynes Plan would ease (both incoming and outgoing) capital controls (Keynes, 1980), although this would not end international investments with "legitimate purposes". For that reason, Keynes suggested distinguishing long-term credits from capital flight and regulating short-term speculative financial flows.

Regardless of the Keynes Plan, the design of the post-war international monetary system ended up following the aspirations of the new hegemonic country, the United States, represented in the Bretton Woods Conference by Harry D. White, whose plan succeeded in establishing the US dollar as the international currency. It created a stabilisation fund to assist participating countries with liquidity problems (the IMF), fixed the exchange rates to the dollar and the dollar to gold, and (in coincidence with the Keynes Plan) regulated capital flows (Eichengreen, 2008; Serrano, 2003). Since the brand-new IMF sought to promote a multilateral payment system based on currency convertibility for current transactions, it recommended member countries to minimize or abolish any exchange restrictions or discriminatory payment agreements (de Vries, 1969).

² This means that deficit countries do not have to request a credit, since they are only left with a debit balance against the ICU.

³ In addition, when the debtor's balance exceeds 25% of the quota, credits would cease to be automatic and, in case it exceeds 50%, the ICU could request the delivery of gold or hard currency as collateral and the devaluation of the currency.

A BRIEF DESCRIPTION OF REGIONAL PAYMENT AGREEMENTS

RPAs,⁴ also known as regional clearing systems or payment unions, are institutional mechanisms designed to facilitate the clearing and settlement of payments among member countries. RPAs replicate, regionally and to a certain extent, several of the characteristics of the Keynes Plan: the central banks of participating countries (or any other institutions specially assigned to this purpose) operate as a clearing house, which manages regional trade payments recording them in a unit of account, and extends automatic credits to deficit countries (Aragão, 1984; Fritz et al., 2014; Kaderbeck, 2019; Kregel, 2017).

The main difference between the Keynes Plan and the RPAs is that the latter are regional (or limited to a few countries). The former aims at establishing a single multilateral general agreement (or for as many countries as possible), whereas in an RPA a country with a regional surplus might not necessarily have the same position in global terms (Aragão, 1984; Keynes, 1980).

RPAs operate at two offsetting levels. At a national level, each country's central bank is in charge of two tasks: paying in domestic currency to local companies exporting to another member country, and collecting domestic currency from those companies that have imported from other members of the agreement. As a counterpart, on a regional scale, each central bank records credits and debits in relation to the other central banks. Hence, some of them would run surpluses and others deficits with respect to the remaining RPA members. During the "accounting period" (set by each RPA), each central bank records the transactions made through the system. The "settlement time" begins at the end of such period, when deficit countries pay and surplus countries receive net balances (unless the RPA defines another type of arrangement).⁵

There are two interdependent reasons why a country may decide to establish and participate in an RPA. First, to promote intra-regional trade with the other member countries, given that importing intra-regionally is relatively more convenient than doing so from the rest of the world. This discrimination resembles a free trade area (FTA). Second, to save hard currency, as member central banks have lower daily liquidity requirements of foreign exchange for transactional and precautionary motives. Both objectives are interdependent, since a country with a hard currency shortage will foster intra-regional trade, while the more trade is diverted into the region at the expense of the rest of the world, the higher hard currency savings will be.

⁴ RPAs are identified here as "regional" regardless of whether they cover one or more regions, in contrast to global agreements.

⁵ This is another difference with the Keynes Plan, where the lack of a "settlement time" forced countries to find the way to resolve imbalances through the operation of the system itself. In other words, payments in hard currencies or gold would be more the exception than the rule.

RPAs promote intra-regional trade by reducing transaction costs for payments made under the agreement. This is because companies in member countries do not need to access the foreign exchange market or send money abroad to trade with their peers in another member country. In fact, they can pay in home currency and incur in financial costs that are comparable to those of a domestic transaction.

Regarding hard currency savings, given that the balances settled in a RPA are determined by the difference between debits and credits recorded during the accounting period, countries would end up requiring less foreign exchange than if each transaction were paid individually. Moreover, automatic lending in a RPA allows central banks to settle payments only at the end of the accounting period. Thus, the volume of daily foreign exchange liquidity needed for transaction motives decreases. In other words, hard currency savings result from settling the exact net balances and only at the end of the accounting period (Chang, 2000; Fritz et al., 2014). In addition, central banks might not require foreign exchange at the settlement time, increasing hard currency savings even more (Fritz et al., 2014). This would be the case when central banks settle balances at the end of the accounting period (even partially) in domestic currencies (or in a unit of account specially created for this purpose), or if imbalances are outweighed by expanding the exports of deficit countries.

As will be seen below, the empirical cases analysed in this paper suggest that there are many differences among RPAs, both in terms of their operation and their objectives.

REGIONAL PAYMENT AGREEMENT BETWEEN FINLAND AND THE USSR (1949-1990)

Cold War geopolitics and Finnish neutrality

This RPA is rooted in Finland's war reparations to the USSR between 1946 and 1952, which in turn helped to develop the installed capacity of the former's metallurgical and naval industries. Given the full closure of Western Europe markets, once the reparation payments were completed, Finland was eager to find new markets to place its production (Oblath & Pete, 1985).

The neutral foreign policy adopted by Finland during the Cold War allowed the country to link economically to both the Western and socialist worlds: while holding a RPA with the USSR and other socialist countries, it also joined the IMF (in 1948) and the Organisation for Economic Co-operation and Development (OECD, in 1969), and signed trade agreements (General Agreement on Tariffs and Trade (GATT), in 1950, and with the European Economic Community, in 1974) (Laurila, 1995; Oblath & Pete, 1985).

Thus, Finland found an amicable environment in the multilateral organisations and treaties signed among capitalist countries (such as the IMF, the GATT or the

European Free Trade Association), which strongly fought against protectionism, trade discrimination and current account inconvertibility. In addition, the IMF did not request that Finland eliminate its RPA with the USSR (unlike the conditionalities imposed on other countries) and “tolerated” its dual position in its trade ties (Matala, 2020).

Furthermore, this RPA would allow the USSR to oversee Finnish trade and keep this country under the Soviet area of influence. In return, Finland rejected aid from the Marshall Plan and did not take part in the EPU. However, during the 1950s and 1960s, the degrees of freedom gained by the Nordic country with respect to the USSR suggest that its continuity in the RPA was clearly its own decision. Despite the economic size difference between the two countries, Finland was able to negotiate and assert its position (Matala, 2020).

Finland signed its first bilateral RPA with the USSR in 1949 (for the period 1951-1955) as a complement to a trade agreement that established quotas for the volume and structure of bilateral trade. This agreement, albeit with different amendments, was renegotiated every five years (synchronously with Soviet planning cycles) until its termination in 1990. During the period 1945-1990, the USSR share of Finnish trade averaged 16%, reaching 19% in the 1980s, whereas Finland accounted for 10% of the USSR trade with Western countries.

Regarding the RPA operation, payments between the two countries were made through accounts denominated in rubles held with the Bank of Finland and the USSR Foreign Trade Bank (VEB). When Finland received a payment, the funds were deposited in a special account with the VEB and became part of Finnish international reserves (although these funds could only be used to make payments to import goods and services from the USSR).⁶ On the companies’ side, the process resembled the payment of imports using convertible currencies. The RPA stipulated that all bilateral trade-related payments had to be made with clearing rubles, which were inconvertible to any other currency. In other words, Finnish foreign exchange regulations prohibited the use of hard currency to pay for imports from the USSR.

Initially, payments through the RPA were feasible only when there were funds available for such purpose in the specially created bank accounts. Later on, the system began to operate with overdrafts and a credit limit, thus allowing payments regardless of the availability of funds. In fact, the established credit limits were frequently exceeded, showing that they were conservative. All in all, the fact that the creditor country did not receive interest payments from the debtor reflected that the RPA did not aim at restricting bilateral trade.

The use of this RPA was mandatory, both for the trade of goods and services between the two countries and for any related expenses. Since the framework within which payments could be channeled was relatively flexible, it was also pos-

⁶ The account with the Bank of Finland fulfilled the same role, but from the USSR perspective.

sible to make some non-commercial payments. Finally, the goods and services traded were valued at international market prices and/or were subject to negotiations between importers and exporters.

The challenge of sustaining the external balance and expanding aggregate demand without using hard currency

From the outset, given that this RPA was envisaged to maintain the balance-of-payments equilibrium in order to avoid, as far as possible, the clearance with hard currency, it was necessary for both countries to have similar export quotas on an annual basis. However, given that many prices could not be fixed *ex-ante* (as they were subject to negotiations between companies or to international market fluctuations), it was not possible to ensure that trade balances would remain in equilibrium. In fact, between 1961 and 1965, the USSR had to pay only 5% of its current account deficit with Finland in hard currency to cover the import content of Finnish exports under the RPA. This ratio fell to 3.9% (and 1.6% of Soviet sales) during 1961-1990 (Holopainen, 1983; Laurila, 1995).

The RPA had various instruments to resolve trade imbalances that exceeded the credit limits originally set. First, countries had to negotiate to balance trade between them, to prevent the credit country from suspending its exports or requesting hard currency for the surplus balance. However, overall, credit limits in this RPA were frequently exceeded and bilateral asymmetries were addressed by offsetting the trade balance without restricting business (that is, increasing exports from the deficit country). This allowed both countries to minimise their hard currency payments (Holopainen, 1983).

Although the hard currency shortage motivated the beginning of this RPA at the end of the War, this situation cannot account for its relatively long duration. In 1957 Finland signed the Helsinki Club Agreement with the OECD, which promoted its gradual shift to multilateralism and current account convertibility (on a par with other Western European countries), while in 1967 Finland opposed the Soviet proposal to terminate the RPA and keep trading with convertible currencies. The RPA had fostered the aggregate demand expansion in key sectors whose competitiveness required economies of scale, research and development efforts, and financing (such as the shipbuilding, capital goods, or construction industries). In addition, the five-year agreements ensured a stable demand for long-term investments. In the 1960s, since some Finnish exporting companies received their payments in advance, financing through this RPA was one of the main reasons to avoid shifting USSR trading to convertible currencies. Finally, the RPA was also useful as an argument to account for Finnish trade discrimination practices within the GATT (Matala, 2020).

The large imbalances in this RPA started after the two international oil crises (in 1973 and 1979), which increased Finland's trade deficit with respect to the USSR. It was possible to briefly offset said imbalance by increasing Finnish

exports, mainly incorporating light industries (such as food and clothing), through an expansion of aggregate demand (similar to the Keynes Plan). There were no impediments for Finland to expand its exports, and the USSR had both the capability and the need to absorb them (Matala, 2020).

This situation was reversed when Finland began to run a surplus, with the falling oil prices in the early 1980s. For this reason, a special account was created in 1982 to include part of the Finnish credit balance, with funds that, unlike ordinary overdrafts, did earn interests. Furthermore, in 1986 Finland called for the start of negotiations due to the substantial expansion of the USSR's debt balance. At the Soviet request, the Bank of Finland created a credit facility to expand its imports from the USSR, although this attempt failed to restore the bilateral trade balance (Laurila, 1995; Oblath & Pete, 1985).

The end of the Agreement was decided by the USSR following its disintegration in the early 1990s, although Finnish diplomacy made several attempts to continue it, even after the clearing agreements among the Council for Mutual Economic Assistance countries were terminated.

THE EUROPEAN PAYMENTS UNION (1950-1958)

From bilateralism to multilateralism through the EPU

The post-war period showed that it was necessary to import capital goods and inputs as well as recovering intra-European trade to promote the reconstruction of countries. However, within a context of US dollar and gold shortage, European inconvertible currencies, and deficit balances of payments with respect to the US, it was necessary for governments to restrict imports through licenses and direct management of foreign purchases.

The institutions created at the Bretton Woods Conference lacked the necessary funding and were not ready for a post-war context of currency inconvertibility (Eichengreen, 2008; Kregel, 2017; Triffin, 1961). Intra-European trade had decreased even more than the trade with the rest of the world,⁷ prompting the establishment of a payment mechanism that was able to restore trade regardless of the dollar shortage. The first of these agreements was signed in 1943 by the (exiled) Benelux governments, a model that was then implemented for the over 200 bilateral RPAs signed in the following four years.

In 1947, the Benelux, France, and Italy (and later West Germany) signed the First Multilateral Monetary Compensation Agreement, with the objective of easing bilateralism limits through the multilateralisation of RPAs. Thus, a European country would be able to offset its bilateral debit balances using the credit balances with European third parties. Nevertheless, the scope of this agreement was

⁷ In 1947, European exports to the rest of the world accounted for 78% of the pre-war level, *vis-à-vis* 56% of intra-European exports (Varela Parache, 1966).

limited, especially due to Belgium's strong creditor position and the few participating countries.

At that time, the IMF limited its involvement in the establishment of the European RPA and did not appoint representatives for the first multilateral agreement.⁸ Therefore, the Bank for International Settlements (BIS) acted as a clearing agent and maintained this role when the EPU was established. The erratic position of the IMF regarding payment problems in Europe began to shift by the mid-1950s. While some of its authorities (both from the Executive Board and the staff) believed that a multilateral RPA in Europe was consistent with the organisation's objectives, others feared that the creation of new means of payment would postpone the currency convertibility of European current accounts (de Vries, 1969).

In 1948, the 16 member countries of the Organisation for European Economic Cooperation (OEEC) joined the system under the Intra-European Payments Agreement (IEPA). This RPA also allowed for a first-level multilateral clearing, but this could cause problems due to the chronic deficits of some countries. In addition, the IEPA operated with the Marshall Plan's hedge for creditor positions that could not be outweighed. Although in 1949 the IEPA was reviewed to adopt a more multilateral approach⁹, the shift to the EPU began shortly after its signature.

The EPU became operational in September 1950. Integrated by the 17 OEEC member countries,¹⁰ it was monitored by a committee of that organisation. As in the case of the IEPA, the BIS was the clearing and settlement agent. The EPU expressly stated its objective of helping member countries to shift from bilateralism to current account currency convertibility. Originally, this RPA would last for two years and would then continue operating among those countries that agreed to its renewal (as long as they accounted for, at least, half of the total initial quotas), and from 1952 onwards it would be renewed annually.

Each central bank recorded its transactions with the other EPU members, having to notify the BIS about the balances of the accounts opened by other RPA members, and the EPU oversaw the multilateral clearing of such operations. In a bilateral RPA, a country is encouraged to import goods and services from those countries with which it has a surplus trade balance (and to avoid buying from those countries with which it is running a deficit). Instead, the EPU eliminated the need of intra-European trade to "buy from whoever buys from us" (Triffin, 1961). The balance of each country at the end of the established accounting period (that is, monthly) was a debit or a credit with respect to the whole EPU. It was mandatory

⁸ Although in the first draft of the RPA the IMF was originally listed as the clearing agent, since it did not appoint any representative for the 1947 meeting (in Paris), the BIS ended up taking its place (de Vries, 1969).

⁹ This mainly implied incorporating the possibility that a debt could be paid with the credit provided by a third country.

¹⁰ Austria, Belgium, Denmark, France, The Federal Republic of Germany, Greece, Ireland, Iceland, Italy, Luxembourg, Norway, the Netherlands, Portugal, the United Kingdom, Sweden, Switzerland, and Turkey.

to use this RPA, and operations included the whole balance of payments and were not limited to the trade of goods and services. Given that the EPU employed a unit of account with a fixed exchange rate with respect to gold, operations could be carried out even when a currency was inconvertible.

The Marshall Plan and the management of intra-European imbalances

The EPU was introduced as an intermediate stage between a RPA with no hard currency settlement (such as the Finland-USSR Agreement) and monetary convertibility to gold and US dollars. Each country was allocated a quota,¹¹ as proposed by the Keynes Plan. Depending upon the utilisation rate of such quota, a part of the surpluses and deficits was settled with gold or US dollars (or possibly another agreed-upon convertible currency) at the end of the accounting period, while the remainder became a credit extended from creditors to debtors through the RPA.

The arranged payment scheme set a mechanism that partially replicated the Keynes Plan for the ICU, since it punished imbalances. Debtors had to pay a progressively larger part in gold as their deficits increased, whereas creditors received only half of their surpluses in gold and only when their credit balance exceeded 20%.¹² The objective was to prevent EPU members from solving dollar shortage problems through surpluses with other European countries. The payment scheme was asymmetric between debtors and creditors, as the former received more financing than that extended by the latter. Therefore, this RPA was not entirely a zero-sum game, and the operating funds that financed such mismatch (which reached USD 350 million) were provided by the United States through the Marshall Plan (Triffin, 1961; Varela Parache, 1966).

The contribution of the Marshall Plan was not limited to closing the gap between payments and receipts within the EPU. It also helped to establish “initial credit balances”, which benefited members with a substantial deficit. Thus, those imbalances at the beginning of the RPA would not hinder its operation. By contrast, countries with structural surpluses conceded their “initial debit balances” in exchange for a conditional aid in US dollars. It is important to note that if a country had a credit balance *vis-à-vis* the EPU, it did not mean that it had a solid external position in global terms.

By mid-1951, the United States replaced all initial (debit or credit) balances with “special resources” in US dollars so that the EPU could allocate them to debtor countries, and then it began to gradually reduce its financial assistance, which ended in 1954. Consequently, around 1952 the EPU had to modify its payment and

¹¹Corresponding to 15% of its trade in goods and services in 1949.

¹²The EPU did not specify what would happen when a credit balance exceeded 100% of the quota, as a way to avoid excessive accumulation of credit balances (Triffin, 1961).

credit scheme to increase payments in hard currency to the EPU and cope with its commitments at the expense of the credit for deficit countries, and later (in 1954 and 1956) changed its payment scheme in the same direction.

Overall, since 1952 the imbalances among the EPU countries had narrowed and only Germany continued to run chronic surpluses, while the remainder of the countries tended to reverse their position with respect to the RPA. Despite the tightening of the EPU payment rules, trade liberalisation continued due to the accumulation of US dollar and gold reserves for the whole region.¹³ Between 1949 and 1955, intra-European trade doubled (*vis-à-vis* a 37% growth in gross domestic product). By the end of 1956, all quantitative restrictions had been removed from 89% of intra-European imports, and the OEEC launched a consultation process to reduce tariffs among participating countries.

The EPU sought to create a transition towards current account convertibility through the amortisation of accumulated credits and the strong increase in gold and US dollar payments. Meanwhile, the exchange market was liberalised, and central banks only intervened to maintain a floating exchange rate band. This further complicated the automatic credit operation within the EPU¹⁴ and fostered a system of non-automatic credits through the creation of the European Fund. By 1958, most of the countries participating in the EPU had established currency convertibility, terminating the RPA and allowing the European Monetary Agreement (EMA), created three years earlier, to fully function. The EMA did not extend automatic credits, and its member countries authorised their commercial banks to freely carry out foreign exchange transactions.

RECIPROCAL PAYMENTS AND CREDITS AGREEMENT

Latin American structuralism and the need to establish a RPA

Debates on complementing regional integration with schemes that facilitate payments among Latin American (LA) countries date back to 1948, when, at the request of the Economic Commission for Latin America and the Caribbean (ECLAC), the IMF concluded that a regional multilateral clearing system would be cumbersome and barely positive for the region. On the contrary, freer convertibility of Latin American domestic currencies would only require minor adjustments (Economic Commission for Latin America and the Caribbean [ECLAC], 1949; Siegel, 1964).

Towards the end of the 1950s, with the LAFTA under construction, the ECLAC resumed the idea of creating a payment and credit system in the proposed Free

¹³From USD 8.4 billion (in 1949) to USD 17.2 billion (in 1956).

¹⁴A country could borrow from the EPU and, at the same time, accumulate foreign currency outside the system.

Trade Area (FTA). Its purpose was to manage a payment clearing mechanism among member countries, multilateralising bilateral payments, and to provide a credit system to balance trade among forthcoming FTA members. However, when the Montevideo Treaty created the LAFTA in 1960, it did not provide any solutions to the potential payment problems, mainly due to the opposition by the IMF and the United States to the establishment of a RPA in LA (Siegel, 1964).

In the context of the establishment of a FTA, the governments of seven South American countries¹⁵ called a meeting of central banks to analyse the payment problem and asked the ECLAC and the IMF for available solutions. These countries considered that the proper functioning of the FTA would require that all trade-related payments be made on a uniform basis and within the same area. Moreover, special credit facilities related to intra-zone trade would help to dispel the concerns and mistrust inevitably created with any trade liberalisation programme, thus contributing to ensure the reciprocity of trade concessions and their advantages. Therefore, signing a RPA was considered essential for the proper functioning of the FTA (ECLAC, 1959; Siegel, 1964).

The main criticisms of the IMF and the United States to the ECLAC proposal can be summarised along three lines. First, a RPA would go against the IMF's aims to broaden convertible currencies. The second criticism pointed to the fact that credits would be received (or granted) based on the debtor (or creditor) country's position in the region, without considering the global position of its balance of payments. Finally, like any FTA, this agreement would generate trade diversion, "artificially" modifying trade patterns (Siegel, 1964).

On the contrary, according to Prebisch (1960), it was necessary to create a payment system that could meet the FTA requirements, considering the need to foster trade among member countries as much as possible. Given that Latin American progress towards import substitution required the development of increasingly complex industries, countries would need larger markets than the national ones. In other words, the idea was to create an additional intra-zone trade flow to boost economic development, but this would not necessarily imply decreasing trade with the rest of the world.

The CPR and regional integration of Latin America

The Mexico Agreement (September 1965) created the Multilateral Compensation System for Reciprocal Payments and Credits (SCMPCR, in Spanish), which came into force in May 1966. In 1969, this Agreement was complemented with the Santo Domingo Accord, which provided reciprocal financial support to help countries dealing with temporary liquidity deficiencies. The result obtained reflected not only ECLAC's position (in favour of automatic and semi-automatic credits),

¹⁵Argentina, Bolivia, Brazil, Chile, Paraguay, Peru, and Uruguay.

but also the IMF's perspective, since many Latin American countries had signed Stabilisation Programmes with this institution.

Thus, instead of establishing a clearing house such as the EPU, the central banks created a multilateral clearing system, based on reciprocal credit lines negotiated bilaterally. These credits were devised to finance those transactions channeled through the system during the accounting period. The accounting period initially lasted for two months, but it was then gradually extended to a four-month duration (since May 1972). Nevertheless, amounts could still be settled every two months for less developed creditor countries (Ossa, 1975).

The SCMPCR established ordinary bilateral credit lines between central banks, denominated in US dollars and with a cap. The clearing house calculated the bilateral balances, which were then offset multilaterally. Those central banks with a deficit had to pay the Central Reserve Bank of Peru (through the correspondent bank, the Federal Reserve Bank of New York) in US dollars. Although, in the beginning, the credit was bilateral, in 1968 a system of partial multilateralisation was introduced, whereby a country that exceeded its credit line with a partner could resort to the unused part of the bilateral credit that a third central bank had extended, as long as the three countries agreed (Aragão, 1984).

Although payments through the system were, at first, voluntary, the central banks often made them compulsory with their own regulations. The agreement included trade of goods, services and related expenses (Aguirre et al., 2016; Pérez Caldentey et al., 2013). If ordinary credit was exceeded, it had to be paid immediately, although it was also possible to use non-automatic financing. The latter was considered an extraordinary credit and was established as a proportion of the former. In addition, in 1969 the Santo Domingo Accord created a support mechanism for temporary imbalances, to hedge debit balances within the RPA that could not be settled (Aragão, 1984; Latin American Integration Association [ALADI], 2009; Ossa, 1975).

Furthermore, every central bank guaranteed to the others the irrevocable acceptance of the debts of the importing country, hence eliminating commercial risk. In other words, the exporting company did not need to get an export credit insurance and the importer could have access to the exporter's credit on better terms. Therefore, central banks assumed a private risk to promote regional trade (Pérez Caldentey et al., 2013).

With the Montevideo Agreement (signed in 1980), LAFTA was replaced by LAIA and the agencies in charge of ensuring the operation of the Mexico and Santo Domingo Agreements ceased to function. In 1981, the Santo Domingo Accord was modified, incorporating two new support mechanisms for countries with liquidity deficiencies. A year later, the Mexico Agreement was amended, creating the CPR, now within LAIA's framework, which continues to be in force (ALADI, 2009).

Initially (from 1966 to 1981), this RPA managed to incorporate new members and improve relations among partners, with 64 (out of 66 possible) bilateral credit lines accomplished. From channeling 10% of intra-regional trade in 1966, it reached 76.5% in 1981, within a growing trade context. In 1982, the CPR suffered its first setback following the Latin American external debt crisis, when Argentina and Mexico were excluded from the operation and the mechanisms provided in the Santo Domingo Accord proved insufficient. Although the proportion of operations channeled through the CPR increased, intra-regional trade dropped by 37% between 1981 and 1986.

By 1987, a new stage had begun with an exponential increase in Latin American trade, but since 1990 the proportion of transactions channeled through the CPR began to fall abruptly (from 90.9% in 1989 to 1.5% in 2003). Within a context of financial deregulation and strong capital inflows into the region, prepayments¹⁶ increased from 10% (in the 1980s) to over 90% (in the mid-1990s). In short, the end of capital controls, the spread of currency convertibility in the 1990s, and the decision of central banks to limit credit lines (all measures promoted by a surge of neoliberal governments), led the CPR to become irrelevant, although, in formal terms, it remains in force. Although after 2003 its use increased slightly (reaching 9.8% in 2007) and then decreased again, such increase was entirely accounted for by the Venezuelan decision to use the system (Aguirre et al., 2016; ALADI, 2017).

CONCLUSIONS

The study of the three RPAs analysed in this article suggests that they may provide a regional alternative to current account currency convertibility. Like the Keynes Plan, RPAs are based on the recording and subsequent clearing of transactions. This implies the provision of automatic credit, at least during the accounting period. In the cases reviewed, the IMF opposed or maintained a trivial position regarding their implementation: in the Finland-USSR RPA it tolerated the neutrality of the Nordic country, in the EPU it avoided getting involved, and in Latin America it strongly discouraged its creation and development.

The end or the decline of the three RPAs studied was due to a decision made by some or all of their member countries (and only when it was feasible to move towards currency convertibility), but it was never accounted for by intrinsic problems in their operation. The RPA between Finland and the USSR ended because of the disintegration of the latter and despite Finland's intention to continue it. By contrast, while the EPU could have continued operating, it was its success that paved the way for the gradual restoration of convertibility in Western Europe (Triffin, 1961). Finally, the CPR stopped being massively used due to the strong capital inflow (as part of neoliberal financial deregulation and the Brady Plan in the early 1990s), which eased the hard currency shortage.

¹⁶That is, the voluntary settlement of credits before the expiration date.

Overall, RPAs succeeded in compensating external imbalances by expanding aggregate demand, in the way that Keynes had envisaged the ICU to work. In the 1970s, when the price of oil rose, Finland managed to increase its exports to the USSR. For their part, most of the countries participating in the EPU managed to reverse their external position *vis-à-vis* the region in the early years of the Agreement. In Latin America, the greatest difficulties arose in the 1980s following the debt crisis, and the response of the countries was to increase the transactions channeled through the CPR. Thus, the impact of the crisis would have certainly been much worse without this RPA.

Regardless of the technical features of each RPA (namely the duration of the accounting period, the extension of extraordinary credit, or the mechanisms designed to reverse regional imbalances), geopolitics played a key role in their operation. Thus, the Cold War influenced the first two RPAs: the Marshall Plan was key for offsetting the European balance of payments and for preventing the liquidity provided by the United States from leaking into the dollar area, whereas in the 1970s the USSR avoided leaving oil out of the RPA, thereby improving the Finnish aggregate demand.

Based on the above, it is possible to conclude that, as an alternative to current account currency convertibility, RPAs are a feasible tool for easing external constraints, both in countries that suffer from frequent devaluation pressures and in those which, having accumulated international reserves for a precautionary motive, pay a high opportunity cost for their hoarding. In addition, RPAs could be used as an instrument that contributes to the development of more sophisticated regional value chains through intra-regional trade, which is likely to increase export diversification and the added value of local production. Both issues (easing of external constraints and regional integration) are especially important for peripheral countries (in general) and for Latin America (in particular).

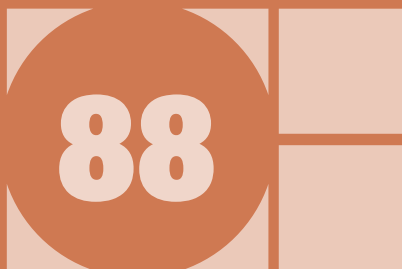
This article paves the way for the future research agenda in three directions: incorporating other RPAs into the analysis, assessing RPAs as a complement to regional trade agreements and as a tool for greater regulation of international payment systems by peripheral states, and lastly, by investigating why the CPR did not regain some momentum after the setback of neoliberal governments in the 2000s.

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