Modern Asian Studies (2023), **57**, 918–939
doi:10.1017/S0026749X22000336

CAMBRIDGE UNIVERSITY PRESS

RESEARCH ARTICLE

Delinking 'the two rupees': The devaluation dilemma and economic divergence in the decolonized subcontinent, September 1949–February 1951

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(Received 24 January 2022; revised 7 June 2022; accepted 9 June 2022)

Abstract
By looking at the September 1949 devaluation dilemma faced by the governments of Pakistan and India, this article argues that it was an early episode of divergence between them following partition. The reasons why Pakistan did not devalue when India did so have remained largely obscured in the historiography. Deeply contested, the decision was a determining event through which the state staked its claim for economic sovereignty, internally and externally. It led to a 17-month-long official trade deadlock, especially in the eastern region of partitioned Bengal. It ended when the two governments established an exchange ratio for the two rupees, no longer at par with each other. This interactive delinking of currencies was symptomatic of the improvisational decoupling of the colonial subcontinent's post-colonial states. In tracing its trajectory, this article contributes to the inconsiderable literature on why devaluation did not happen in Pakistan, revises the rationale offered, and presents the event as a contingent exercise in economic decolonization, generative of a post-colonial sovereign difference.

Keywords: Sterling area; devaluation; Pakistan; India; trade; decolonization

Introduction

The decolonization and partition of the Indian subcontinent in August 1947 were momentous events at the intersections of old empire, new commonwealth, the Second World War just ended, and the Cold War to come. Historians have explored imperial policies, nationalist politics, regional perspectives, and the social consequences of partition in both India and Pakistan.[1] Global histories of South Asia also further this exegesis of continuity and change from colonialism to its aftermath with respect

[1]See, among others, Joya Chatterji, 'Decolonization in South Asia: The Long View', in *The Oxford Handbook of the Ends of Empire*, (eds) Martin Thomas and Andrew S. Thompson (Oxford: Oxford University

to bilateral and international relations.[2] Amid all this, early economic 'exchange relations' between Pakistan and India have received little attention,[3] perhaps because, like Indo-British financial relations, 'the complexities…of the subject make it tempting to ignore'.[4] This may also explain why there are more narratives about the new commonwealth than of the sterling area.[5] Beyond some early interest in trade and tariffs,[6] political, military, territorial, and cultural tensions have naturally attracted greater attention.[7] However, revisiting specific episodes, if not turning points, in early economic relations between India and Pakistan may enable us to form a more nuanced understanding of the 'puzzle of divergent paths' taken in the subcontinent.[8]

This article deals with one such episode at the intersection of two interrelated transitions: from imperial preference to more nationally oriented trade policies, and from a position of inter-dominion equivalence to greater differentiation in external policies and personas, which has received little attention in the literature on partition and state-making in the two countries. The episode that will be examined is the devaluation of the pound sterling against the American dollar in September 1949, which India embraced by also devaluing its rupee, but which Pakistan refused to follow. The resulting divergence between the two currencies, which until then had been practically interchangeable, turned out to be pivotal to their bilateral economic relations as well as Pakistan's relations with the rest of the world. Its immediate fallout was a trade blockade in the subcontinent that lasted until February 1951, which overlapped with parallel negotiations between India and Britain over sterling balances, and between India and Pakistan over the division of the two dominions' assets and liabilities.[9] On the face of it, this was a simple issue of divergence in the exchange rate

Press, 2018), pp. 251–275; Ayesha Jalal, *The Pity of Partition: Manto's Life, Times, and Work Across the India-Pakistan Divide* (New Jersey: Princeton University Press, 2013), pp. 1–18; Gyanendra Pandey, *Remembering Partition: Violence, Nationalism and History in India* (Cambridge: Cambridge University Press, 2000), and Gyanesh Kudaisya and Tan Tai Yong (eds), *Partition and Post-Colonial South Asia: A Reader* (London: Routledge, 2007).

2 See, for example, Paul M. McGarr, *The Cold War in South Asia: Britain, the United States and the Indian Subcontinent, 1945–1965* (Cambridge: Cambridge University Press, 2013).

3 See S. L. N. Simha, *History of the Reserve Bank of India (1935–1951)* (Bombay: The Reserve Bank of India, 1970), pp. 668–674.

4 B. R. Tomlinson, 'Indo-British Relations in the Post-colonial Era: The Sterling Balances Negotiations, 1947–49', *The Journal of Imperial and Commonwealth History*, vol. 13, no. 3, 1985, pp. 142–162.

5 See, for the most recent narration, Philip Murphy, *The Empire's New Clothes: The Myth of the Commonwealth* (London: Hurst, 2018).

6 For instance, 'Devaluation Makes Pakistan Cotton Dearer', *Economic Weekly*, vol. 1, no. 39, 24 September 1949, pp. 16–17, and N. R. Jafri, 'Pakistan's Trade with India', *Pakistan Horizon*, vol. 5, no. 2, 1952, pp. 86–96.

7 An early account is Jyoti Bhushan Das Gupta, *Indo Pakistan Relations: 1947–1955* (Amsterdam: De Brug Djambatan, 1958). A recent iteration is Pallavi Raghavan, *Animosity at Bay: An Alternative History of the India-Pakistan Relationship, 1947–1952* (New York: Oxford University Press, 2020).

8 See Philip Oldenburg, *India, Pakistan, and Democracy: Solving the Puzzle of Divergent Paths* (London: Routledge, 2010).

9 See M. De P. Abreu, 'Britain as a Debtor: Indian Sterling Balances, 1940–53', *The Economic History Review*, vol. 70, no. 2, 2017, pp. 586–604; Joya Chatterji, *The Spoils of Partition: Bengal and India, 1947–67* (Cambridge: Cambridge University Press, 2007), and Anwesha Sengupta, '"Breaking Up": Dividing Assets between India and Pakistan in Times of Partition', *The Indian Economic and Social History Review*, vol. 51, no. 4, 2014, pp. 529–548.

https://doi.org/10.1017/S0026749X22000336 Published online by Cambridge University Press

between the two currencies, but it provoked a dispute that had major consequences for the external trade of both countries, complicating India's external financial position and influencing Pakistan's membership negotiations with the Bretton Woods institutions.[10]

Why did the government of Pakistan (GoP) not follow India and almost the entire sterling area in devaluing its rupee in September 1949? The ramifications of this decision have been documented, but its rationale remains insufficiently explored. Thirty years ago, drawing on British and American government archives, Ayesha Jalal termed the GoP's 'cavalier' decision 'a remarkable show of intransigence [which] sent shockwaves through the sterling area', and categorized it as falling 'somewhere in between' Pakistan's 'assertion of its independence vis-à-vis both India and Britain' and a 'fractured economic logic'.[11] Two decades ago, Ian Talbot suggested that the decision 'underscored Pakistan's independence', but focused mainly on its implications.[12] This article, however, is interested in exploring Pakistan's rationale for refusing to devalue its rupee in September 1949, a decision that controversially punctured its payments agreement with India which had been signed in June 1948 to keep mutual remittances going without exchange rate restrictions.[13] At the time *The Economist* offered four reasons to explain Pakistan's decision:

> First, Pakistan's balance of payments…is favourable. Secondly, Pakistan…needs to import capital goods cheaply…Thirdly, Pakistan government believes that its exports have inelastic demand. Finally, Pakistan wants…a fall in domestic prices.[14]

Taking this four-fold premise as a starting point, this article draws on hitherto unutilized primary sources to plot the course of the GoP's divided ruling in September 1949 and develop a finer understanding of its motivations and compulsions. It aims to show that this rupture in the rupee ratio, which was bitterly contested by India, had major consequences for the economies of the two newly independent states and their external relationships. If the sterling area came between Britain and European integration in this period, then the severed rupee ratio was the not-so-thin end of a wedge driven into the subcontinental economy.[15] For Pakistan, it meant cutting the colonial umbilical cord and, despite the shorter-term consequences, carving out an economic sphere

[10] Aditya Balasubramanian and Srinath Raghavan, 'Present at the Creation: India, the Global Economy, and the Bretton Woods Conference', *Journal of World History*, vol. 29, no. 1, 2018, pp. 65–94, and Ehtesham Ahmad and Azizali Mohammed, 'Pakistan, the United States and the Bretton Woods Institutions: A Continuing Great Game?', in *Routledge Handbook of Contemporary Pakistan*, (ed.) Aparna Pande (Abingdon: Routledge, 2017), pp. 228–246.

[11] Ayesha Jalal, *The State of Martial Rule: The Origins of Pakistan's Political Economy of Defence* (Cambridge: Cambridge University Press, 1990), p. 96.

[12] Ian Talbot, *Pakistan: A Modern History* (London: Hurst, 1998), p. 137.

[13] Simha, *History of the Reserve Bank of India*, pp. 664, 668.

[14] *The Economist*, quoted in Raghavan, *Animosity at Bay*, p. 170.

[15] Scott Newton, 'Britain, the Sterling Area and European Integration, 1945–50', *The Journal of Imperial and Commonwealth History*, vol. 13, no. 3, 1985, pp. 163–182.

https://doi.org/10.1017/S0026749X22000336 Published online by Cambridge University Press

distinct from India.[16] While the trade crisis in the subcontinent has been examined in terms of its impact on India, its significance for Pakistan's emerging statehood and sovereignty has been largely overlooked.[17] The Reserve Bank of India (hereafter Reserve Bank) served as 'banker to the Government of Pakistan' from 15 August 1947 to 1 July 1948, before being succeeded by the State Bank of Pakistan (hereafter State Bank). This 'monetary separation', however, was softened by keeping a payment 'parity between the two rupee(s)'.[18]

This agreement was renewed in late June 1949 for another year, and it was against this liminal background that a dispute arose as a result of the GoP's September 1949 decision. This differed from the government of India's (GoI) 'defensive' devaluation, made because its trade was 'so largely a trade with sterling area countries and the price level being already high…there was no alternative to…maintaining the existing rupee-sterling rate'.[19] Hence, this article, which is organized in three parts followed by a coda, begins by reconstructing the contrapuntal motivations of Pakistan's decision-making on the rupee ratio from September 1949 onwards with considerable verisimilitude. It then relates the rapidly escalating dispute between the two dominions and Pakistan's interactions with the International Monetary Fund (IMF) and the World Bank, where the wider implications of this decision were debated. The article then focuses on the disruption in subcontinental railway traffic to illustrate the effects of the inter-dominion dispute, before underscoring the important role that the latter played in Pakistan's sovereign emergence. Throughout, the focus remains on key state actors and their motives during this three-fold episode comprising difficult consultation, its diffused communication, and, finally, its differential impact on various partition peculiarities.

Deciding on devaluation

The devaluation of the British pound in 1949, which reflected a currency in decline, is the starting point of this story.[20] Most sterling area countries followed this decision, in the range of 9–20 per cent, with the aim of increasing exports, reducing imports, stepping up production, checking inflation, and bringing in 'dollops of dollars'.[21] C. D. Deshmukh, the civil servant who became the first Indian governor of the Reserve Bank in 1943, called this decision an 'expiation of the extravaganzas of war'.[22] The first finance minister of Pakistan, Ghulam Mohamed, was informed on 16 September 1949

[16]See W. Godfrey, 'Anglo-Pakistan Trade', *Pakistan Horizon*, vol. 2, no. 4, 1949, pp. 188–198, and M. Ahmad, 'Pakistan's Economic Relations with the United States', *Pakistan Horizon*, vol. 4, no. 1, 1951, pp. 51–58.

[17]Raghavan, *Animosity at Bay*, pp. 161–182; an exception is Wayne Wilcox, 'The Economic Consequences of Partition: India and Pakistan', *Journal of International Affairs*, vol. 18, no. 2, 1964, pp. 188–197.

[18]Simha, *History of the Reserve Bank of India*, p. 668.

[19]Ibid., pp. 665–666.

[20]See Alex Cairncross and Barry Eichengreen, *Sterling in Decline: The Devaluations of 1931, 1949 and 1967* (Oxford: Basil Blackwell, 1983), and Catherine R. Schenk, *Britain, and the Sterling Area: From Devaluation to Convertibility in the 1950s* (London: Routledge, 1994).

[21]M. L. Flanders, 'The Effects of Devaluation on Exports: A Case Study UK, 1949–1954', *Oxford Bulletin of Economics and Statistics*, vol. 25, no. 3, 1963, pp. 165–198, and Henry Pelling, *Britain and the Marshall Plan* (London: Macmillan, 1988), p. 87.

[22]C. D. Deshmukh, *The Course of My Life* (Bombay: Orient Longman, 1974), p. 228.

in Washington that London had been compelled by 'American pressure and of events' to devalue the pound by 25–30 per cent.[23]

Ghulam Mohamed was visiting the United States to hold talks with the State and Treasury departments, the World Bank, the Food and Agricultural Organisation, and the IMF for development loans, technical missions, and Pakistan's application for membership. A former officer of the Indian Audit and Accounts Service, he had worked in different departments such as the railways, posts and telegraph, and supply as well as in princely states like Bhopal and Hyderabad, and had built a reputation for competence. He also had a nose for business, having co-founded the Mahindra and Mohamed steel company in 1945. He assured the Americans that, with a more favourable 'climate' for private investment, Pakistan was a 'better proposition' than India.[24] Within two years, he would be elevated to become Pakistan's third governor-general (1951–55) and help pave its pro-American path.[25]

Mohamed and Deshmukh, who was then on the executive boards of both the World Bank and the IMF, were somewhat surprised by this turn of events, as Stafford Cripps, chancellor of the British exchequer, had assured them otherwise.[26] Chips off the old, 'overdeveloped' block of the British Raj, they were resentful at the detrimental effect this would have on the subcontinent, especially the consequent liquidation of their sterling balances with London.[27] *The Pakistan Times*, the country's leading left-wing daily, would denounce the impact of London's decision as a 'severance of Indo-Pakistan trade relations [to] compel Pakistan to turn to Britain'.[28] Next door, voices in India 'feared that under [this] economic strain, Britain would unilaterally cancel the [war] debt; [their] sterling balances'.[29]

Deshmukh shared with Mohamed that he had recommended devaluation to New Delhi, as the bulk of India's trade was within the sterling area. A refusal to devalue could also lead to difficulties in getting loans from the United States. For Deshmukh, Pakistan should follow suit 'owing to the same causes…'.[30] However, as the GoP was not yet a member of the IMF, it was neither required to do so nor to make haste in doing so. The flip side to this was that 'the only standard in terms of which the value of the Pakistan rupee could be determined was sterling or the Indian rupee',[31] both of which stood devalued. Within a day, as Australia, South Africa, and India approached the IMF, some clarity emerged on the new rate of pound sterling against the American dollar. It was expected to be 2.80 and Mohamed's first concern was Pakistan's foreign exchange as,

[23] 17 September 1949, Ghulam Mohamed to Liaquat Ali Khan and Zahid Husain, File No. 53 (6) Coordination Branch (hereafter Cord)/49-50-I, National Documentation Wing (hereafter NDW), Cabinet Division, Government of Pakistan (Islamabad).

[24] 12 and 14 September 1949, Mohamed to Khan, File No. 3 (1), Prime Minister's Secretariat (hereafter PMS) 49, NDW.

[25] Talbot, *Pakistan: A Modern History*, pp. 139–143.

[26] Deshmukh, *The Course of My Life*, p. 160.

[27] Hamza Alavi, 'The State in Post-colonial Societies: Pakistan and Bangladesh', *New Left Review*, vol. I, no. 74, July/Aug 1972, pp. 59–81.

[28] 'Currency Devaluation and Pakistan-I', *The Pakistan Times*, 29 September 1950, p. 4.

[29] M. R. Carnell, 'India from Colony to Nation-State: A Re-Reading of India's Foreign Policy in Southeast Asia, c.1945–1955', PhD thesis, University of Sheffield, 2012, p. 220.

[30] Deshmukh, *The Course of My Life*, p. 161.

[31] Simha, *History of the Reserve Bank of India*, p. 669.

https://doi.org/10.1017/S0026749X22000336 Published online by Cambridge University Press

since its birth, Pakistan had 'lived on sterling and dollar releases'.[32] He then launched into an exposition of the devaluation dilemma to Prime Minister Liaquat Ali Khan.

Devaluation would set in motion inflation and importation, create an underground market, and have a 'psychological' effect. Ghulam Mohamed cautioned the prime minister against a 'sentimental or superficial' decision. Turning to trade, he listed Pakistan's main exports: jute, cotton, wool, tea, hides, skins, and bones. Among these, jute was the predominant product, and India was its largest purchaser. The risk of not devaluing here was that there would be reduced demand for jute by India; to Mohamed, it was apparent that Pakistan could not 'strike a lonely furrow'. Overall, the finance minister recommended devaluation, however 'distasteful…in concert with sterling'; this was accompanied with the foreign minister Zafrulla Khan's 'hope that US is keen to fill up gap caused by devaluation'.[33]

Within the next couple of days, as New Zealand and the then-Ceylon governments fell into the devaluation line, pressure mounted on the GoP.[34] Zahid Husain, first governor of the State Bank, who had been the vice-chancellor of Aligarh Muslim University before partition and Pakistan's first high commissioner in India after it, prepared a memorandum. Earlier, he had served as a financial adviser to regional administrations in Delhi and Hyderabad as well as in central departments such as supply and railways. In his note of 18 September 1949, Husain observed that while some devaluation of the pound had been expected, its 30-plus per cent was unforeseen. He claimed that India had been keen to devalue independently due to its worsening balance of payments situation and would have gone ahead 'had [it] been sure of similar action by Pakistan'. Deshmukh later confirmed that he was 'convinced, as a corrective to [inflation of currency in] the aftermath of the war, [of] devaluation'.[35] With the exchange rate of Pakistan's currency fixed in terms of the pound as well as the Indian rupee, in the absence of any decision, it would be devalued by default. The options were either to devalue, to not devalue at all, or to devalue to a lesser extent. However, before examining these options, Husain set the record straight on Pakistan's balance of payment position:

> It is generally believed that Pakistan has a favourable balance… [because of] the special conditions after the partition when…our imports dwindled…while our exports were maintained… [Since then] we [have] an adverse balance of payment…with the rest of the world…Owing to lack of statistics, it is not possible to measure our balance of trade with India…[36]

Husain's memorandum then moved to the first alternative of devaluing to the same extent as the pound. This meant maintaining the status quo with Britain and India, with imports of goods becoming expensive and exports likely to decrease. The second alternative was to not devalue at all. Here, the first concern was Pakistan's jute exports

[32] 17 September 1949, Mohamed to Khan and Husain, File No. 53 (6) Cord/49-50-I, NDW.

[33] 19 September 1949, Zafrulla Khan to Liaquat Ali Khan, File No. 53 (6) Cord/49-50-I, NDW.

[34] 18 September 1949, Wellington to Karachi (T. No. 19), and 19 September 1949, Colombo to Karachi (T. No. 28), File No. 53 (6) Cord/49-50-I, NDW.

[35] Deshmukh, *The Course of My Life*, p. 160.

[36] 18 September 1949, Zahid Husain's memorandum, File No. 53 (6) Cord/49-50-I, NDW.

to India. Cotton exports, on the other hand, depended more on Egypt, and with that country devaluing too, cotton prices would be reduced. As regards imports, not devaluing would mean a fall in the prices of goods resulting in some 'relief', but in terms of items that came primarily from India, like cloth, coal, and steel, the situation could reverse and require 'control'. Equally, textile products would meet Indian competition and necessitate a 'tariff'.

At the time the GoP's foreign exchange reserves were held in London (sterling) and Bombay (rupees), in addition to Karachi (GoI securities), and if Pakistan did not devalue, their book values would go down from Rs 1.5 billion to Rs 1.03 billion. With respect to India, there was a safety provision in their payments agreement that, in the event of devaluation by either, 'the rupees held by the other will be appreciated to the extent required to neutralise the effect'. The third alternative—devaluation but not to the same extent as the pound—was akin to opening a Pandora's box and Husain thus concluded:

> If we…keep in step with the United Kingdom (UK), we will strengthen inflation [and] accentuate difficulties of urban population… [On the other hand] the incomes of producers of raw products will not suffer [and] the budgetary position will not deteriorate. If we do not devalue…opposite tendencies will come in…[37]

In either case, the GoP faced 'upheaval', and its central cabinet gathered on the evening of 18 September 1949 to discuss the situation. The prime minister chaired the meeting, which was attended by five of his colleagues, the secretary-general, and Husain. They were also joined by the governor of West Punjab and premiers of Sind, the North-West Frontier Province (NWFP), and East Bengal. At its outset, Liaquat Ali Khan proposed delaying making a decision for a day or two, to 'know what course other countries were adopting'.[38] The meeting was thus devoted to an information-disseminating exercise that was started by Husain, who reiterated the salient points of his circulated memorandum.

The secretary-general Chaudhuri Mohammad Ali, a former Indian civil servant (1928–47) and a future prime minister of Pakistan (1955–56), then chimed in. He simplified the consequences of devaluation as the country earning less from exports to non-sterling area, and added that, conversely, if the GoP did not devalue, imports from the sterling area would be cheaper but it would find it difficult to buy Pakistan's raw materials. It would, therefore, benefit fixed-income earners and adversely affect the agricultural population. At this, Abdul Qayyum Khan, the premier of NWFP, opined that 'more weight' should be given to the latter. Yusuf Haroon, the premier of Sind, followed him by remarking that in Europe, devaluation had led to inflation and asked whether Pakistan was considered to be an exporting or importing country. Nurul Amin, the premier of jute-rich East Bengal, noted that the answer depended on whether India could supply jute to the world; if not, then producers of jute in East Bengal, 'would not be adversely affected from [non] devaluation'.[39]

[37]Ibid.

[38]18 September 1949, Cabinet Meeting, File No. 53 (6) Cord/49-50-I, NDW.

[39]Ibid.

https://doi.org/10.1017/S0026749X22000336 Published online by Cambridge University Press

It was at the next cabinet meeting, held on 20 September 1949, that a comprehensive list of reasons emerged as to why the GoP should not devalue, with Fazlur Rahman, the minister for commerce and education, who had served as revenue minister in the pre-partition province, taking the lead. In a detailed presentation, Rahman examined the impact of devaluation on Pakistan's exports. In the case of cotton, his officials claimed that even without devaluing, the country would be able to sell, as it grew different varieties. They argued further that if, because of the higher cost to India of Pakistani cotton, 'Indian textile prices go up, we benefit'.[40] Outside the sterling area, Japan was their principal purchaser and, since it was not devaluing, cotton exports there would not be affected. As regards jute, world consumption was estimated at 9.1 million bales, out of which Indian mills accounted for 5.6 million bales. Pakistan's current crop was forecast at six million, India's at about 2.5 million, and, after meeting its commitments to India under their trade agreement, Pakistan would still be able to export two million bales with, if necessary, reduced duty. Thus, Rahman's ministry did not anticipate a fall of more than 5–10 per cent in jute prices.

Tea was the next item of importance. Prices were regulated under Pakistan's contract with Britain, whose devaluation meant that the value of tea exports there would go up. Consequently, London would seek a revision of their contract, but Rahman did not think this would result in substantial changes. For him, on the export side, there was thus no argument for devaluation. This was ironic, considering the decision's subsequent impact on East Pakistan, where 'recession [and] economic disparity embittered the relations between the two wings'.[41] In December 1949, as the region of Bengal emerged as the epicentre of this economic conflict, prime minister Jawaharlal Nehru would confide in Dr B. C. Roy, premier of West Bengal, that 'the decision must rest with…the people of Bengal'.[42]

Insofar as imports were concerned, for Fazlur Rahman, a 30 per cent devaluation would increase the net adverse balance, but more important was the effect on prices of articles required by agriculturalists. He insisted that while there might be some deflation in the case of non-devaluation, it would benefit East Bengal. Further, he critiqued Britain's nationalization drive, wondering if it would not have to devalue again, and expressed his concern that if Pakistan followed suit now, it would be compelled to do so again. Rahman returned to Husain's memorandum in concluding that a currency appreciation would increase savings, make imports cheaper, and lead to industrial development. Devaluation, on the other hand, would lead to the 'dire consequences' predicted by Ghulam Mohamed. Rahman declared that as 'our people…*believed* that our economic position and balance of payments were good', the GoP should not give 'a cause for this to be *doubted*' [emphasis added].[43]

If this seemed like a confidence trick by Rahman, whose 'brainchild' Ayesha Jalal calls the eventual decision, then the minister for food, who followed him, continued with it.[44] He expected Indian jute buyers to buy from Pakistan even if it would cost

[40] 20 September 1949, Cabinet Meeting, File No. 53 (6) Cord/49-50-I, NDW.

[41] Talbot, *Pakistan: A Modern History*, pp. 137–138.

[42] 25 December 1949, Nehru to Roy, File No. 33, Jawaharlal Nehru (hereafter JN) post-47 (SG) Papers, Nehru Memorial Museum and Library, New Delhi (hereafter NMML).

[43] 20 September 1949, Cabinet Meeting, File No. 53 (6) Cord/49-50-I, NDW.

[44] Jalal, *The State of Martial Rule*, p. 96.

https://doi.org/10.1017/S0026749X22000336 Published online by Cambridge University Press

them more, as they could still sell their finished goods, given New Delhi's devaluation. To him, in the case of cotton, the prevailing prices were anyway 'unduly inflated'. Regarding food crops, if they did not devalue, the position in East Bengal, where rice prices were high, was expected to improve, if Pakistan could get supplies from the then-Burma. Wheat stood on a different footing, as Pakistan was in surplus here. With American and Canadian wheat being expensive and Australia being the only other exporting sterling area country, it had a decent chance of continuing to sell wheat.

The prime minister then asked Mohammad Ali to give his comments. Ali proceeded to puncture many of these ministerial presumptions. To hold that Britain would have to devalue again appeared to be unnecessary speculation to him. Like Husain, he challenged 'the assumption that our balance of payments was not so unfavourable as to call for devaluation' and cautioned that if Pakistan did not devalue, the United Kingdom might not make 'sufficient [sterling] releases'.[45] Then there was the assumption that if Pakistan did not devalue, the price of imports would 'automatically' reduce. Here, Ali argued that, in fact, there would be a rise in prices of goods produced in the sterling area. Similarly, to him it seemed erroneous to assume that any reduction in the prices of machinery would by itself promote private enterprise. Turning next to the 'psychological' aspect, Ali turned this on its head by stating that 'the world would not believe that we could stand out alone and…the decision would not be regarded as final'.[46] Instead, he sought a partial devaluation.

For Ali, the crux of the matter was whether Pakistan could sell its goods and the accompanying premise that, at least in jute and cotton, Pakistan's position was so strong that all it needed to do, was to slightly lower its prices. He thought that this argument was based on the position of an undivided India, but in fact in 1948–49, Pakistan had officially sold 1.9 million bales of jute as against six million sold by India. If Pakistan did not devalue, India's cheaper jute would be more attractive. Ali anticipated that in 1949–50, India would sell about 1.5 million bales, leaving a million of the world's demand for Pakistan. The ministers countered him here by insisting that 'steps short of devaluation' could be exercised, while challenging him on India's unlikely supply of half of the world's demand for jute. When Ali, in turn, warned them about the GoI increasing the cost of coal and steel for Pakistan, the ministers stiffened in their resolve that Pakistan 'should not be deterred' by an Indian or international belief that it would 'fall in line'.

The prime minister then returned to Zahid Husain. The State Bank governor stated soberly that if the GoP could consider devaluation 'in isolation', then it could be ignored, but could the country risk 'standing out' when the Reserve Bank financed a large part of Pakistan's jute exports? His considered opinion was that the GoP should devalue by 15 per cent, which he emphasized by underlining the scepticism that prevailed in a non-devaluing and contracting economy. Husain also informed ministers that he had discussed the matter with bankers, businessmen, and industrialists, most of whom favoured devaluation.

With his ministers in attendance arguing on one side and the officials on the other, the prime minister 'found it difficult to…lead'. However, since his ministerial

[45] 20 September 1949, Cabinet Meeting, File No. 53 (6) Cord/49-50-I, NDW.
[46] Ibid.

https://doi.org/10.1017/S0026749X22000336 Published online by Cambridge University Press

colleagues who were present, as well as the provincial premiers earlier, did not favour devaluation, he supported taking that decision. Ali and Husain were instructed to work out the new rates of exchange of the two rupees and sterling, signalling a significant moment in the making of a *national* currency. After their April 1950 agreement, Jawaharlal Nehru would pay a compliment to Liaquat Ali Khan that applies well here: 'his approach to life was that of an Oudh Taluqdar…cautious, but having [concluded], he stuck to it'.[47]

Defending non-devaluation

The GoP's discussions were, meanwhile, making its envoys abroad apprehensive. From London, high commissioner Ibrahim Rahimtoola informed the GoP that Pakistan's 'hesitation aroused great speculation' and insisted that, for the GoI to have agreed so quickly, New Delhi must have been 'assured of capital goods from sterling area'.[48] From Washington, Ghulam Mohamed reminded Liaquat Ali Khan that his recollection of the payments agreement with India was that the two rupees had to be at par, which meant that if the GoP did 'not devalue, [GoI] are entitled to pay in their [depreciated] rupees and claim payment in our rupees'.[49] Enquiries were being made regarding Pakistan's decision, which would affect its efforts to join the IMF and obtain loans from the World Bank. However, once the decision was taken, the prime minister took the lead in defending it to Mohamed and Zafrulla Khan thus:

> By a reduction in prices in jute, cotton, we should be able to sell our surpluses…Our decision is in the best interests of UK…USA also should not feel unhappy since devaluation would have raised prices of our American imports…By not devaluing we would not be exposed to inflation…[50]

Before going further, it is worthwhile embedding the prime minister's decision in a political context. Since the Commonwealth Prime Ministers' Conference in April 1949, when the soon-to-be-republic India's membership of the club was successfully negotiated, even as Pakistan's standing request for mediation on Kashmir was ignored,[51] Liaquat Ali Khan had been absorbing press criticism for being pro-commonwealth and at the same time attracting political plotting, chiefly in the province of West Punjab, which had a British governor. Altaf Hussain, the Bengali editor of the English-language daily *Dawn*, declared that 'if Liaquat goes on licking the boots of the British, I will break him'.[52] On the other hand, the Punjabi faction in his party and government was threatening his vulnerable grip on the state. Perhaps currency nationalism combined with provincial permutation came together in this declaration of sovereign intent, whatever the economic costs.

[47] 24 May 1950, Nehru's note of his meeting with Ghulam Mohamed, File No. 45-I, JN (SG) Papers, NMML.

[48] 20 September 1949, Rahimtoola to Liaquat Ali Khan, File No. 53 (6) Cord/49-50-I, NDW.

[49] 21 September 1949, Ghulam Mohamed to Liaquat Ali Khan, File No. 53 (6) Cord/49-50-I, NDW.

[50] 22 September 1949, Khan to Mohamed and Zafrulla Khan, File No. 53 (6) Cord/49-50-I, NDW.

[51] See R. J. Moore, *Making the New Commonwealth* (Oxford: Clarendon Press, 1987).

[52] Ilyas Chattha, 'Faction-building in Pakistan: Sir Francis Mudie and Punjab Politics, 1947–1949', *Contemporary South Asia*, vol. 22, no. 3, 2014, p. 236.

In the event, his economic optimism was checked within days, as the Reserve Bank announced that it was unable 'to quote any rate for Pakistan rupees' thereby setting banks free to carry out such transactions 'as they could'.[53] State Bank officials reported that prices were 'tending to rise' and goods were 'going underground', underlining the imperative of a controls policy.[54] With the cancellation of the open general licence, businessmen were stocking up on goods that the government wished them to 'dispose of'.[55] Zahid Husain and Mohamad Ali convened a meeting of the major ministries on 23 September 1949. The secretary-general started with the news that various United Nations aid organizations were sending their teams to Pakistan in winter, thereby endorsing its membership of these. This was followed, however, by an 'upset' GoI hinting at raising the cost of coal, steel, and cloth to Pakistan, so as 'to force [it] to devalue'.[56] As a result of their divergence on devaluation, Pakistan's prices for goods to India were now 44 per cent higher.

There already was an export duty on Indian steel, while Indian coal was to be exported through government channels only. GoP officials instructed the Pakistan railways to conserve coal, as they went through the list of actions that the GoI could take. These included 'stopping money orders', 'flight of capital from East Bengal…', 'restrictions on the export of mustard oil [and] sea-salt to East Bengal', halt in 'supplies of railway stores', and suspension of 'medicines, hessian and jute bags…'.[57] Pakistan officials' first response was to match this against India's wish list: jute and cotton, food and rock-salt, dried fruit, fresh fish, and cement. Such were some of the 'anomalous consequences of partition', which saw Nehru inform his provincial premiers on 2 October 1949 that 'Pakistan's refusal to devalue [brought] trade at standstill'.[58]

On food items, however, Mohamad Ali preferred not to get in India's way, as Pakistan was short of storage. The GoP was caught here between its competing desires to not take any precipitous steps and to suspend supplies. Other countries inevitably entered this equation. The GoP had learnt that Egypt had a surplus of 35,000 tons of rice, which it offered in exchange for wheat, while the GoI had an agreement for wheat supplies from Australia. Still, India needed an estimated three million tons of food grains, leaving a considerable gap for Pakistan to fill. For the rest, officials mulled over meeting India's export duties by some of their own as well as by exploring other markets. It is worth recalling that in December 1947, it was for imposing duties on jute that the GoI first termed Pakistan a foreign territory.[59] Now, almost two years later, Mohamad Ali estimated that as India had banned jute exports, its mills were able to consume a considerable quantity of its own produce (approximately two million bales) for about two to three months. In the meantime, Pakistan had the foreign market to itself. The question was how best to exploit this double-edged situation, given that

[53] Simha, *History of the Reserve Bank of India*, p. 669.

[54] Jalal, *The State of Martial Rule*, pp. 98–99.

[55] 24 September 1949, Altaf Gauhar to Mumtaz Hasan, File No. 53 (6) Cord/49-50-I, NDW.

[56] 23 September 1949, Secretaries Meeting, File No. 62 (4) Cord/49 and File No. 53 (6) Cord/49-50-I, NDW.

[57] Ibid.

[58] 2 October 1949, Nehru to provincial premiers, File No. 30, JN (SG) Papers, NMML. Also see Sekhar Bandyopadhyay, *Decolonization in South Asia: Meanings of Freedom in Post-independence West Bengal, 1947–52* (London: Routledge, 2009).

[59] Raghavan, *Animosity at Bay*, pp. 165–166.

https://doi.org/10.1017/S0026749X22000336 Published online by Cambridge University Press

the GoP's rupee appreciation had made Pakistan's jute expensive. If it now reduced prices, it would have adverse effects on either dollar earnings or on 'psychological' grounds.

For instance, although reducing export duty stimulated trade and brought down prices, it could also be construed as a sign of weakness. And so it was decided to seek alternative financing for jute, wool, hides, and skins, if 'the Marwaris in East Bengal would curtail credit' and firm up the transportation of these exports to other markets in southeast Asia, Australia, southeast Africa, and west Asia. With respect to cotton, a 30 per cent loss of the Egyptian crop meant that Pakistan could export more than expected for 1949 by reducing export duty. This left coal, the other outstanding issue with India, and in a second meeting of the secretaries held over two days, Mohamad Ali informed everyone that the GoI had formally protested that the GoP had 'infringed the payments agreement by altering the sterling rate of the rupee'.[60]

This was misleading for, after all, it was the GoI that, emulating Britain, had altered its currency rate and followed that up by declaring its 'wiliness to accept a rate of Pakistan Rs. 100=to India Rs. 143 15/16 as decided upon by the [GoP]'.[61] *The Times of India* called it the 'right decision [given] the world economic disequilibrium, obligations to the sterling area [and] to encourage American investment'.[62] This 'currency parity with the [colonial] metropole…sustained by deflationary policies' was not 'what the Indian nationalist urged'.[63] When the GoP subsequently sought from the Reserve Bank 'sterling in respect of the balances of the SBP' which it held, the GoI 'flatly refused', [64] worried, as it was by now, about Pakistan's supplies in jute and cotton. To tackle this, a conference was held at the residence of India's deputy prime minister Vallabhbhai Patel in late September 1949. It was attended by the finance and commerce ministers, Dr John Matthai and K. C. Neogy, and representatives of banking, business, and industry. They discussed buying cotton from elsewhere, while being confident that India's jute stocks would 'manage' for six months.[65]

Simultaneously, the GoI's unilateral step of raising the price of Indian coal exports to Pakistan by Rs 12 per ton worsened this state of suspension of inter-dominion trade. With the GoP deciding to apply tariffs in response, an official trade deadlock was looming and to check speculation the GoP needed an import licensing policy for countries other than India. The danger of balance of payments difficulties was also lurking, lapped up by the Indian envoy in Karachi, who reported to Patel the fear 'behind the flashy announcements…that the anticipated balance of trade may only prove a will o' the wisp'.[66] Already, Pakistan found itself in difficulty of another kind, as Ghulam Mohamed reported to Liaquat Ali Khan:

[60] 24 September 1949, Secretaries Meeting, No. 62 (4) Cord/49 and File No. 53 (6) Cord/49-50-I, NDW.

[61] Simha, *History of the Reserve Bank of India*, p. 669.

[62] 'India's Stand Vindicated', *The Times of India*, 26 September 1949, p. 6.

[63] M. S. Alam, 'Colonialism, Decolonisation and Growth Rates: Theory and Empirical Evidence', *Cambridge Journal of Economics*, vol. 18, no. 3, 1994, pp. 251–252.

[64] Simha, *History of the Reserve Bank of India*, p. 669.

[65] 'Tackling Economic Problem of India', *The Times of India*, 27 September 1949, p. 1.

[66] 2 October 1949, Sita Ram to Patel, in *Sardar Patel's Correspondence: 1945–50. Volume VIII*, (ed.) Durga Das (Ahmedabad: Navajivan, 1973), p. 68.

> Pakistan's decision not to devalue has caused considerable disappointment [at] IMF…[The] British director remarked that [it] is upsetting commonwealth economy…American financial circles are watching. If we should now devalue, it will appear…that our economy is dependent…on India's.[67]

The GoP's position in the international economic fora in the immediate aftermath of its decision was 'pretty confused', even as the official jute-cotton trade with India came to a 'standstill'.[68] By mid-October 1949, 'there were at least four different [rupee] rates prevailing in Calcutta'[69] and inter-dominion trade fell by half in that month,[70] forcing official-level talks. In these, the GoI wished for 'a free rate of exchange' for a resumption of trade, while the GoP wanted its rupee and sterling balances held with the Reserve Bank.[71] Neither side agreed and, in early November 1949, Ghulam Mohamed visited New Delhi to make it clear that 'the GoP would [not] go back…but [it was] prepared to come to [an] arrangement'.[72] His Commerce Ministry colleague Fazlur Rahman insisted that any such talks could only happen after India 'accepted the exchange ratio', otherwise it would be injurious 'to our prestige'.[73] In New Delhi, with the prime minister visiting the United States, Patel was reflecting a similar attitude of economic injury and political prestige:

> Devaluation has hit us hard…Pakistan seems upset over the stoppage of official trade…The unofficial rate has varied between 103 and 115 Indian rupees for 100 Pakistan rupees. If we can hold out sufficiently long, we might be able either to enforce parity or to settle very near parity.[74]

Meanwhile, the GoP was building up its case by obtaining a financial statement from Britain showing percentage changes in prices since devaluation there. Except for potatoes, barley, and oats, every item had registered an increase of between 10 and 30 per cent.[75] The GoP successfully reached out to neighbours like Burma to accept the new currency exchange rate,[76] and on 15 November 1949, the State Bank declared the official rate for making transactions between the Pakistan rupee and the Indian rupee as 'Rs. 143 11/16 selling and Rs. 144 3/16 buying for Pakistan Rs. 100'.[77] This rendered much of the remaining trade between the two countries as either an illegal transaction or a barter exchange in the Punjab-Bengal borderlands. These activities, which were interpreted by New Delhi 'as a preliminary to the introduction of full exchange control',[78] were soon overshadowed by news from New York, where rumours were

[67] 3 October 1949, Ghulam Mohamed to Liaquat Ali Khan, File No. 53 (6) Cord/49-50-I, NDW.
[68] 20 October 1949, Shaffi (New York) to Mohamed, File No. 53 (6) Cord/49-50-I, NDW.
[69] Simha, *History of the Reserve Bank of India*, p. 670.
[70] 'Pakistan's Foreign Trade after Devaluation', *The Times of India*, 9 December 1949, p. 7.
[71] Simha, *History of the Reserve Bank of India*, p. 670.
[72] 3 November 1949, Cabinet Meeting, File No. 53 (6) Cord/49-50-I, NDW.
[73] Ibid.
[74] 3 November 1949, Patel to Nehru, in *Sardar Patel's Correspondence: 1945–50. Volume VIII*, (ed.) Das, p. 385.
[75] 10 November 1949, Note by M. Ismail, File No. 53 (6) Cord/49-50-I, NDW.
[76] 14–16 November 1949, Karachi-Rangoon correspondence, File No. 53 (6) Cord/49-50-I, NDW.
[77] Simha, *History of the Reserve Bank of India*, p. 671.
[78] Ibid.

https://doi.org/10.1017/S0026749X22000336 Published online by Cambridge University Press

circulating that it had been decided to devalue Pakistani rupee. Denials from Karachi of 'baseless' speculations notwithstanding, these rumours persisted, with newspapers declaring that 'Pakistan will devalue…be equalised with India…Calcutta mills would obtain supplies…'.[79] Instead, in New Delhi, Dr S. P. Mookerjee, minister for industries, was exhorting Patel to 'make ourselves independent of Pakistan…agricultural economy'.[80]

Ghulam Mohamed took pains to explain to his government's envoys that this kind of talk was being spread to deter prospective buyers.[81] The GoP's Ministry of Economic Affairs procured a statement showing percentage change in prices since devaluation in India, where food articles had become costlier by almost 20 per cent, cloth by 15 per cent, and industrial raw materials by 10 per cent.[82] Yet, the London-based *Financial Times* reported on 4 March 1950 that there was 'fresh talk of devaluation of [the] Pakistan rupee'.[83] It claimed that Pakistan had delayed its budget as there was a deterioration in its balance of payments and depreciation in the prices of raw materials. The GoP certainly desired to avoid a clash between the two budgets as part of its attempt to carve out a distinct economic identity.

In November 1949, Ghulam Mohamed had suggested to the prime minister that he permit him to present his budget after the Indian budget and lay out its advantages. The GoP could then consider New Delhi's changes when framing taxation proposals; this would also have the advantage in getting attention from the foreign press which Pakistan had struggled to do.[84] Liaquat Ali Khan agreed and from 1950 onwards, the two budgets were presented on different dates, much like the two currencies were valued at different rates. These first steps on their 'divergent paths' were not easy to explain though. In December 1950, Mohammed Ali's American interlocuters urged him to establish an exchange ratio that would enable trade resumption, which might 'pave way' for the resolution of other problems. Ali had some prescient words for them:

> Devaluation's economic disadvantages outweighed benefits from resumption of trade, which would have no effect on other problems…Appeasing India in currency dispute would stiffen India's attitude…There was no barrier to trade except India's refusal to recognise exchange ratio…[85]

Inter-dominion railway and the impact of non-devaluation

Before moving on to the international proposals to end this trade deadlock, it is useful to take a closer look at one case study to examine its consequences. As a commentator pointed out, more than a 'steep deflation', it was the 'social difficulties' in their

[79] 16 and 17–27 November 1949, Mohamed-Shaffi correspondence, File No. 53 (6) Cord/49-50-I, NDW.

[80] 7 December 1949, S. P. Mookerjee to Patel, in *Sardar Patel's Correspondence: 1945–50. Volume IX*, (ed.) Durga Das (Ahmedabad: Navajivan, 1974), pp. 113–115.

[81] 30 November 1949, Mohamed to Shaffi, File No. 53 (6) Cord/49-50-I, NDW.

[82] 24 December 1949, Note by Ministry of Economic Affairs (No. III/5/P-49), File No. 53 (6) Cord/49-50-I, NDW.

[83] 7 March 1950, Salman Ali to Mumtaz Hasan, File No. 53 (6) Cord/49-50-I, NDW.

[84] 9 November 1949, Mohamed to Khan, File No. 3 (1) PMS/49, NDW.

[85] 7 December 1950, Mohamad Ali to Ikramullah, File No. 53 (6) Cord/49-50-I, NDW.

https://doi.org/10.1017/S0026749X22000336 Published online by Cambridge University Press

eastern wing that the GoP seemed to have overlooked when making its decision.[86] One can add a political dimension here. In April 1949, in a by-election held in Tangail (Mymensingh), the Muslim League was defeated, and its response was 'to postpone other by-elections'.[87] An opposition party emerged in the form of the Awami League, belying Liaquat Ali Khan's boast that he would not allow any other political outfit 'to work'.[88] The prime minister's support for Fazlur Rahman might thus also have been motivated by the need to strengthen his party in East Bengal; given the language movement there, it was already Pakistan's 'troubled province'.[89] That this support backfired was due to the GoI stopping 'transfers of Pakistan's share of the assets of undivided India, [placing] export duties on commodities… [and] suspend[ing] the supply of coal'.[90]

This section first focuses on the disrupted railway traffic between East and West Bengal and Assam from September 1949, and then dwells upon its impact elsewhere. On 22 September 1949, the day of the GoP's demurral on devaluation, the GoI instructed the East Indian Railway to refuse 'coal and parcel traffic' to Pakistan.[91] When the East Bengal Railway acted similarly regarding the traffic between Assam and West Bengal, the stoppage of coal deliveries from India exposed East Bengal Railway stocks. On the other side, the North-western Railway had enough coal stocks for 30 days and so rail traffic in Pakistan faced curtailment by a quarter. This shocked the GoP which protested to New Delhi that, post-devaluation, it expected the Indian railway to collect 'freight and fares due to Pakistan, as per [the] new exchange ratio'.[92] This, however, was a game that two could play and soon the GoP stopped jute supplies to India, pending the 'new exchange ratio', which would add seven annas per rupee to Pakistan's share.[93] Next, the East Bengal Railway stopped the transfer of rice pending a 'pre-payment' of freight in Pakistan rupees.[94]

This hold-up saw *The Times of India* predict a near-annulment of the inter-dominion trade pact by the end of the year.[95] The tussle between one side's determination to have inter-dominion traffic flow at the parity of two rupees prior to devaluation and the other side's insistence on the new differentiated exchange ratio put both sides at a disadvantage—but one side considerably more so. The GoI's decision to stop all coal traffic put Pakistan Railways in a potentially paralysing situation and, in turn, the GoP demanded a deposit of 'Rs. ten lakhs [per] month in advance in Pakistani currency with East Bengal Railway [for] cross-traffic'.[96] By the first week of October 1949, even as

[86]Josselyn Hennessy, *India Pakistan in World Politics* (London: K-H Services, 1949), pp. 76–77.

[87]A. H. Ahmed Kamal, 'The Decline of the Muslim League and the Ascendancy of the Bureaucracy in East Pakistan 1947–54', PhD thesis, Australian National University, 1989, p. 255.

[88]Ibid.

[89]See R. L. Park, 'East Bengal: Pakistan's Troubled Province', *Far Eastern Survey*, vol. 23, no. 5, 1954, pp. 70–74, and Saadia Toor, 'Containing East Bengal: Language, Nation, and State Formation in Pakistan, 1947—1952', *Cultural Dynamics*, vol. 21, no. 2, 2009, pp. 185–210.

[90]Jalal, *The State of Martial Rule*, pp. 97–98.

[91]22 September 1949, East Bengal Railway to Nizamuddin (Karachi), File No. 53 (17) Cord/49-50, NDW.

[92]23 September 1949, Karachi to New Delhi, File No. 53 (17) Cord/49-50, NDW.

[93]24 September 1949, C. C. Desai to Mohamad Ali, File No. 53 (17) Cord/49-50, NDW.

[94]26–29 September 1949, Nizamuddin-Bakhle correspondence, File No. 53 (17) Cord/49-50, NDW.

[95]'India-Pakistan Trade Pact: Annulment Threatened', *The Times of India*, 16 December 1949, p. 5.

[96]1 October 1949, Nizamuddin to Bakhle, File No. 53 (17) Cord/49-50, NDW.

https://doi.org/10.1017/S0026749X22000336 Published online by Cambridge University Press

formal inter-Bengal trade halved in quantity, New Delhi held on to the status quo and Karachi reiterated that the 'Indian Railways must collect 23 annas in Indian currency for every 16 annas in Pakistan currency', while turning its attention to the Siliguri-Haldibari sector.[97]

The terminuses of this sector were in Indian territory, but were operated by the East Bengal Railway, which charged a 'levy' that India deemed 'irregular'. Instead, it suggested a scheme in which each dominion would collect 'its own freight'.[98] This 'paid-to-pay' system was introduced from 6 November 1949.[99] But, it was one thing to agree at the national level and quite another to implement the agreement locally, where authorities introduced their own 'innovations'.[100] Ghulam Mohamed later criticized 'minor officials' on both sides, 'who did not carry out the government's policy'.[101] However, in January 1950, the GoP upped the ante by taking certain actions: behind this we can again see the hand of Fazlur Rahman. He presented the prime minister with a hopeful economic scenario, except for 'the fly in the ointment…India', urging 'full exchange control' to exert pressure on the GoI. In addition, he stated 'that membership of the IMF should be not pursued until… [this] is settled'.[102] Given that two of Pakistan's neighbours—India and Afghanistan—refused to recognize its rupee, Rahman worried about the IMF making devaluation a condition of Pakistan's membership.

For now, Karachi cancelled the booking of all railway traffic to and from East Bengal from midnight of 19–20 January. New Delhi reciprocated. At the heart of this tussle remained the triad of coal supply, 'paid-to-pay', and 'levy charge/advance deposit'.[103] Later in the year, this railway theatre was joined by customs checks and the detention of jute, which resulted in rampant smuggling across Bengal.[104] Consequently, M. Ismail, the Pakistan high commissioner in India, called on India's commerce minister K. C. Neogy in February 1950 to resolve the situation. The latter set out the following conditions for a conference: '…devaluation will not be raised…trade will be reopen[ed] without [it] …30 lac bales of jute [is] required by India…as soon as the jute reaches, coal…will be released'.[105]

Neogy, like his counterpart Rahman, was from Bengal and was feeling uneasy, as the worsening economic situation there exacerbated the deteriorating social sphere, leading to greater refugee movement across the partitioned region.[106] He felt that the GoI's decision to stop coal had 'precipitated matters' and wondered if Patel 'thought that Pakistan would fall at his feet'.[107] Now, however, Ghulam Mohamed was hopeful,

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[97] 12 October 1949, Karachi to New Delhi, File No. 53 (17) Cord/49-50, NDW.

[98] 13 and 18 October 1949, Bakhle to Nizamuddin, File No. 53 (17) Cord/49-50, NDW.

[99] 26 October–1 November 1949, Karachi-New Delhi exchange, File No. 53 (17) Cord/49-50, NDW.

[100] 14 November 1949, New Delhi to Karachi, File No. 53 (17) Cord/49-50, NDW.

[101] 24 May 1950, Nehru's note of his meeting with Mohamed, File No. 45-I, JN (SG) Papers, NMML.

[102] 12 November 1949, Fazlur Rahman to Khan, File No. 3 (3) PMS/49, NDW.

[103] 12, 23 and 31 January 1950, Karachi to New Delhi, and 18 and 21 January 1950, New Delhi to Karachi, File No. 53 (17) Cord/49-50, NDW.

[104] 25 January 1950, Ghulam Mohamed's note, File No. 3 (2) PMS/50, NDW.

[105] 5 February 1950, M. Ismail to Mohamed and 7 February 1950, Mohamed to Khan, File No. 3 (2) PMS/50, NDW.

[106] See Haimanti Roy, *Partitioned Lives: Migrants, Refugees, Citizens in India and Pakistan, 1947–65* (Oxford: Oxford University Press, 2013).

[107] 4 March 1950, Neogy to Nehru, File No. 38, JN (SG) Papers, NMML.

as Patel, mindful also of the Indian business community being hurt by the trade deadlock, had hinted to him during his recent visit to New Delhi about holding trade talks without discussing the exchange rate. One way to do this was for the GoP to trade with its funds at the Reserve Bank; the other was through their sterling reserves. The GoP's first concern was coal, given a hyperbolic campaign in the *Dawn*.[108]

In turn, *The Times of India* described Mohamed's discussions with Nehru, Patel, and Neogy as 'informal and personal', contrasting it to the GoP's 'adamant attitude' and conceding that 'as Pakistan is admitted [to] the IMF…India will agree…to Pakistan's rate'.[109] Writing 20 years later in his history of the Reserve Bank, S. L. N. Simha admitted that New Delhi had initially thought that 'the high parity of the Pakistan rupee which was not justified by the facts of [its] trade with India would itself provide the necessary check… [however] the continuance of the movement of funds despite the obvious unprofitableness showed that factors other than purely economic ones were also in operation'.[110] Away from this politicking, Ghulam Mohamed asked Zahid Husain to prepare a note anticipating the resumption of trade. Looking back at the events that had occurred since mid-September 1949, Husain, who had supported devaluation before becoming convinced by July that its absence was 'proving ruinous to Pakistan',[111] noted that, having taken that decision, the GoP was 'naturally eager to ensure that [it was] accepted…by India', because prolonged 'non-acceptance would weaken international relationship[s]'.[112]

Instead, with India's attitude complicating the application for Pakistan's membership of the IMF, the GoP was exploring the likelihood of reconciliation. The problem was that the resumption of trade without a recognition of Pakistan's exchange rate might make its ultimate recognition tougher. On the other hand, there was the possibility that persisting with the deadlock would force India to be reasonable. The promise of trading in sterling would strengthen the GoP's exchange rate and its standing with the IMF, but prolonging the deadlock in the expectation that the lack of jute and cotton would lead to Indian mills closing down meant holding the current position for at least a couple more months. By then, however, Pakistan would have a large quantity of unsold jute, a large quantity of cotton sold at unfavourable prices, stiffening inflation, shrinking foreign exchange, international pressure, and an energy crisis. In other words, the GoP was staring at absorbing all this 'to hold India under pressure for a sufficiently long period'. Husain understandably felt 'extremely uncertain'.[113]

What then of the other side of the ledger? Coal-for-jute was a formula Husain could live with, but what if the GoI made the resumption of coal exports conditional on the resumption of trade? Then, Husain would insist on regular payment by India of any liabilities. Reasonably concerned that raw materials—India's imports from Pakistan—were easier to move, unlike Pakistan's imports from India—finished products—he mulled over the high probability of balances accruing in Pakistan's

[108] 6 February 1950, Mohamed to Ismail, File No. 3 (2) PMS/50 and 12 September 1950, Mohamed to Khan, File No. 3 (21) PMS/50, NDW.

[109] 'Indo-Pakistan Disputes: Hopes of Settlement', *The Times of India*, 2 February 1950, p. 7.

[110] Simha, *History of the Reserve Bank of India*, p. 671.

[111] Jalal, *The State of Martial Rule*, p. 99.

[112] 7 February 1950, Husain's note, File No. 3 (2) PMS/50, NDW.

[113] Ibid.

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favour. Therefore, Husain was more comfortable with the limited resumption of coal-for-jute negotiations at a low-key secretaries' level, leaving the politicized exchange rate as well as larger trade negotiations for later.

In April 1950, a limited three-to-six months trade agreement on two items was reached in Karachi at the officials' level: the GoP's balances with the Reserve Bank and the exchange of mustard, groundnut, tobacco, linseed oils, cotton textiles, woollen goods, and steel from India and jute seed and wheat from Pakistan.[114] The agreement pivoted around 'a deal between the Indian jute mills' association and the Pakistan jute board for the sale by Pakistan of raw jute in Indian rupees', which were to be made available to Pakistan for its purchases in India.[115] At the political level, Vallabhbhai Patel still asserted that the exchange ratio would not be changed, 'warning the public against rumour-mongering'.[116] Indeed, for Husain's counterparts at the Commerce Ministry—Rahman and secretary A. MacFarquhar—'the risk' came from too much 'emphasis on…India' as, by September 1950, in terms of all trade, except for that with India, there was an 'adjustment to the new exchange'.[117] They were confident that when considering its review of the two economies in 1949–50, the IMF would not challenge Pakistan, but for the 'temptation' to treat '[the currency] rate as a mechanism for closing the conflict'. They then concluded with the ideological point that was the crux of this economic posture: 'Reduced economic inter-dependence between India and Pakistan [was] under way before [devaluation] and [will] continue…The maintenance of both rupees at the same value [is] unimportant.'[118]

Coda: With the World Bank and at the IMF

Meanwhile, in mid-February 1950, the IMF governors approved Pakistan's membership of the fund and George C. McGhee of the US State Department and William H. Draper of Dillon, Read and Co., an American investment bank, came visiting, with Draper offering the possibility of both countries accepting 'whatever rate of exchange the fund approves [for] trading…'.[119] Opinion on this in the cabinet in Karachi was 'divided', even on expediting membership of the IMF. Ghulam Mohamed urged his colleagues to, but others strongly expressed the opinion that this was 'not the time…because of the repercussions…on rupee'.[120] The GoP was similarly divided on the revision of the Indo-UK trade agreement, especially the imperial preferences through which British goods had enjoyed lower import duty in the subcontinent.[121] In this case, the Foreign and Commerce ministries proposed continuing these, while the finance minister pointed to the loss of revenue. London, if anything, was keener to 'increase [these] preferences by adding the differential [currency] rates…'.[122] As Ayesha Jalal wrote, the GoP's

[114] 17 April 1950, Cabinet Meeting, File No. 42-I, JN (SG) Papers, NMML.

[115] Simha, *History of the Reserve Bank of India*, p. 672.

[116] 'Exchange Ratio Not to be Changed: Sardar Patel's Assertion', *The Times of India*, 19 May 1950, p. 1.

[117] 29 August 1950, A. MacFarquhar's note, File No. 3 (4) PMS/50, NDW.

[118] 3 September 1950, Fazlur Rahman to Khan, File No. 3 (4) PMS/50, NDW.

[119] 14 and 15 February 1950, Mohamed to Khan, File No. 3 (2) PMS/50, NDW.

[120] 28 February 1950, Ispahani (Washington) to Khan, File No. 14 (8) PMS/50-III, NDW.

[121] Mir Mustafa Ali Khan, 'Pakistan and UK Trade Relations', *Pakistan Horizon*, vol. 14, no. 2, 1961, p. 140.

[122] 28 February, 1 and 22 April 1950, Mohamed to Rahman, File No. 3 (1) PMS/49, NDW.

decision not to devalue was a 'good illustration of how financial policies recoiled on politics in general'.[123]

Against this backdrop of wrangling at the apex, falling jute exports in East Bengal, rising agricultural prices in Sind, and unprecedented floods in Punjab, Pakistan became a member of the World Bank on 11 July 1950 and a World Bank mission visited the country.[124] In the same month, traders from the two Punjabs undertook an exchange that sought a 'relaxation of the permit system and resumption of road-rail traffic' by giving Jawaharlal Nehru an example of their troubles: 42,000 bales of cotton were sent from Pakistan to the then French-ruled Pondicherry on the southwest coast of India, crossing over from there to the neighbouring provinces, with spices making a similar journey in reverse.[125] The World Bank mission's visit too was overshadowed by the rupee's exchange rate and it had to clarify that this 'matter does not affect Pakistan's membership'.[126] Meanwhile, a group of Indian journalists visited East Bengal and returned with their impression that a 'revival of trade would help in decreasing the tension', while reporting that at both Calcutta and Dacca airports, they were able to 'exchange the rupee on [the old] value'.[127]

The exercise to establish a new value was undertaken by the IMF from September 1950, almost a year after the GoP's refusal to devalue. Liaquat Ali Khan, after his maiden visit to the United States in May 1950, had the worrying impression that the American attitude to the Pakistani rupee 'might be affected by their anxiety to have trade deadlock with India settled on any terms'.[128] However, Ghulam Mohamed felt that since Liaquat's trip, the attitude of the Americans had 'undergone change', reflecting the then-emerging crisis in Indo-American relations.[129] He soon confirmed that while 'the IMF and American technical group were originally in favour of both rupees being at par', they no longer held that position.[130] An encouraged prime minister now worried about the IMF suggesting postponement, as that would prolong the 'state of uncertainty'.[131] Still, this was preferable from his vantage point and on 13 September 1950, the IMF deferred by a month consideration of the Pakistani rupee's par value, overriding India's dissent.[132] In New Delhi, the feeling was that with this postponement and the expiry of the interim arrangement on 30 September, there was 'little likelihood of any trade'.[133]

The GoP now prepared for the next round in Washington. Ghulam Mohamed returned to complete the cycle that had started in September 1949. His opening gambit

[123] Jalal, *The State of Martial Rule*, p. 104.

[124] 2–6 October 1950, Mohamed-Ali correspondence, File No. 67 (14) Cord/50 and 21 November 1950, Nurul Amin to Khan, File No. 4 (3) PMS/50, NDW.

[125] 3 July 1950, Nehru's note, File No. 47-I, JN (SG) Papers, NMML.

[126] 20 October 1950, Press Communique, File No. 53 (13) Cord/49-50, NDW.

[127] 5 July 1950, B. Shiva Rao to Patel, in *Sardar Patel's Correspondence: 1945–50. Volume X*, (ed.) Durga Das (Ahmedabad: Navajivan, 1974), pp. 140–141.

[128] 6 September 1950, Khan to Mohamed, File No. 3 (21) PMS/50, NDW.

[129] 7 September 1950, Mohamed to Khan, File No. 3 (21) PMS/50, NDW. See Rudra Chaudhuri, *Forged in Crisis: India and the United States since 1947* (London: Hurst, 2014).

[130] 9 September 1950, Mohamed to Khan, File No. 3 (21) PMS/50, NDW.

[131] 12 September 1950, Khan to Mohamed, File No. 3 (21) PMS/50, NDW.

[132] 13–14 September 1950, Mohamed to Khan, File No. 3 (21) PMS/50, NDW.

[133] 'Future Trade with Pakistan: India's Stand', *The Times of India*, 17 September 1950, p. 4.

https://doi.org/10.1017/S0026749X22000336 Published online by Cambridge University Press

was that 'the economic situation had undergone a considerable change' since, a nod towards the Korean War.[134] Pakistan's trade and balance of payments position were 'improving', as exporting countries (except India) 'could now tap alternative' markets and the government could impose 'export duties'.[135] Giving the example of jute, the finance minister claimed that of the total crop of 5.5 million bales, other countries were taking '2.5 million'. For the remainder, he was confident that India was 'bound to approach' as the Indian demand for Pakistani jute was so strong that, despite the official deadlock, 'about 8 lakh bales' were smuggled, at a price that was 10 per cent less than 1949. If the GoI still refused to trade, then it could only be for 'political' reasons.[136] Indeed, at around the same time, the GoI was getting the Reserve Bank to examine whether, in the event of a further delay at the IMF, 'such exchange control measures as might be practicable should not be introduced immediately'.[137]

All this formed the prologue to the finance minister's main point, which was that Pakistan stood by its existing rate. His IMF interlocutors appreciated this assessment, but remained anxious that the subcontinental economies should continue to be intertwined. With Ghulam Mohamed stonewalling, they deferred the question for a couple of months and shook hands in the hope that the political situation might change by then. In the event, this is what happened, with the GoI and the GoP coming to an agreement in February 1951. Its terms were that for 15 months, Pakistan would supply raw jute, raw cotton, and food grains, and India would reciprocate with coal, steel, textiles, and cement, on the par value of the Pakistan rupee.[138] The following month, the IMF accepted the par value communicated by the GoP, namely, 'Pakistan Re. 1=30.225 US cents (the Indian rupee was equivalent to 21 US cents)'.[139] By then, an ailing Patel, who had lamented as late as October 1950 that Pakistan was 'drifting away from trade with India [after it] did its worst to paralyse our industry', was dead.[140] It was now left for Nehru to answer the question that if New Delhi 'had to recognise the par value of the Pakistan rupee, why did [it] not do so a year ago'? He claimed that his government was 'justified in not recognising the Pakistan rupee, which …almost led, to [its] devaluation'. But then

> The Korean war…made a great difference…It became a sellers' market [for] primary produce…Because of this, the Pakistan rupee became strong again…To continue not to recognise it would [be] unrealistic.[141]

Following this agreement, exchange control was extended to Pakistan (and Afghanistan) on 27 February 1951, and 'from that date [their] currencies were treated as foreign currencies for all purposes'.[142] By May 1951, this matter was impinging

[134] 13 November 1950, Mohamed to Khan, File No. 3 (21) PMS/50, NDW.

[135] Jalal, *The State of Martial Rule*, p. 100.

[136] 13 November 1950, Mohamed to Khan, File No. 3 (21) PMS/50, NDW.

[137] Simha, *History of the Reserve Bank of India*, p. 672.

[138] 28 February 1951, Nehru to G. M. Huggins, File No. 74, JN (SG) Papers, NMML.

[139] Simha, *History of the Reserve Bank of India*, p. 673, p. 665.

[140] 5 October 1950, Patel to Sri Prakasa, in *Sardar Patel's Correspondence: 1945–50. Volume X*, (ed.) Das, pp. 436–437.

[141] 2 March 1951, Nehru to chief ministers, File No. 76-I, JN (SG) Papers, NMML.

[142] Simha, *History of the Reserve Bank of India*, p. 673.

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upon Pakistan's debt to India, which was to be repaid 'in 50 annual instalments [of 100 million] beginning [June] 1952'. Deshmukh reasoned that this would involve either foreign currency or the transfer of goods, and both would be a gain 'whatever the par value of [Pakistan's] currency'.[143] In June 1951, India's existing agreement with Britain on sterling balances was ending, with the succeeding Colombo plan looked upon as a continuation of sorts.[144] And in August 1951, New Delhi proposed 'to supply 1, 525, 000 tons of coal/coke to Pakistan [until] June 1952, in exchange for [jute/cotton]'.[145] Before all this, they dutifully traded charges at the IMF, with India arguing that Pakistan's non-devaluation was without any economic justification and Pakistan returning the argument on India's trade boycott. At the heart of this was India's contention that the two economies were similar and therefore the reasons for India's devaluation in 1949 held good for Pakistan in 1950. The GoP's memorandum to the IMF declared against this proposition thus: 'That, India and Pakistan were parts of one country, [with] one currency…is a matter of history…hardly relevant [as] the economies of the two differ, after partition';[146] now their currencies differed too, as reflected in the Reserve Bank's buying and selling rates for Pakistan rupees (Rs 69-8-3 and Rs 69-6-6 for Indian Rs 100 respectively), and its State Bank counterparts (Rs 144-0-9 buying and Rs 143-13-3 selling for Pakistan Rs 100).[147]

Conclusion

In its annual report the IMF's executive board considered the 1949 devaluation as radiating from the Second World War. The 1940s was a decade of inflation, as the 1930s had been one of economic depression. Both caused the pound to devalue, in 1931 and 1949 respectively, but formerly the sterling area was an empire, while by the later date, some of it had transformed into a decolonized *new* commonwealth of dominions. Only one of these countries, however, looked the other way on devaluation, on the strength of 'a keen world demand for its primary products' and a 'strong monetary position' in this transitional period in the region.[148] Yet, more post-partition accounts have attended to India, while most scholarship on Pakistan has focused on its eventual military-industrial complex from the mid-1950s.[149]

As this article shows, the GoP's highly contested decision not to devalue in September 1949 and persistence with this decision until February 1951—causing, in effect, a partition of currencies—was an exhibition of sovereign intent not only to India, but to Britain and United States as well. This was part of the post-partition consolidation that the two nation-states in the subcontinent strove for. The discussions, the disagreements, the decision, and its eventual defence, were remarkable renditions of national ideology and provincial politics; mutually interacting with regional and

[143] 30 May 1951, Deshmukh to Nehru, File No. 87-I, JN (SG) Papers, NMML.

[144] Carnell, 'India from Colony to Nation-State', pp. 201–202.

[145] 3 August 1951, Nehru to Prasad, File No. 94-I, JN (SG) Papers, NMML.

[146] 7 November 1950, Anwar Ali's IMF memorandum, File No. 3 (21)—PMS/50, NDW.

[147] Simha, *History of the Reserve Bank of India*, p. 673.

[148] F. M. Innes, 'The Central Budget', *Pakistan: A Quarterly*, vol. 1, no. 1, 1949, p. 29, and J. L. Llewellyn, 'Pakistan's Tea Industry', *Pakistan: A Quarterly*, vol. 1, no. 3, 1949, p. 38.

[149] See Ayesha Siddiqa, *Military Inc. Inside Pakistan's Military Economy* (London: Pluto Press, 2007).

https://doi.org/10.1017/S0026749X22000336 Published online by Cambridge University Press

international stimuli and, in turn, creating consequences for both. It was in pursuance of a 'monetary autonomy' that this 'de-linking strategy' was followed, especially as it had 'a colonial currency', and the alternative of regional economic integration 'based on mutually supportive national currencies' was put paid to in the aftermath of partition.[150]

While this did not mean a dethroning of the economic order of the British Raj—their trading pattern was restored in February 1951—it certainly marked a constitutive break in their hitherto intersecting, and hence future, parallel trajectories, which would widen into 'divergent paths'. Before September 1949, 'more than half of Pakistan's exports went to India' but it was not so after February 1951. This was perhaps an 'unintended consequence of Patel's trade blockade', another example from these first years, when legacies of an older, singular state were untangled.[151] This article attempted one such study of the late 1940s, which rests in the cracks between the Raj and its two successor republics, when the GoP decided to adopt an appreciated rupee in its own regard. In both cases, it was difficult to estimate the exact extent to which their respective decisions were responsible for the improvement in their economies, but in both cases, by late 1950, its effect had 'neared exhaustion' and the subsequent improvement 'was largely due to the Korean war and the resultant world-wide stimulation of demand for essential raw materials'.[152]

Those early years, arguably more so for Pakistan, allow us to look closely at the trajectory of its state before it trembled with the assassination of Prime Minister Liaquat Ali Khan in 1951 and was terminated by General Ayub Khan's takeover in 1958. In-between, in August 1955, it devalued its rupee, bringing it back at par with the Indian rupee, by which time 'the estrangement of economies was almost complete'.[153] By now, the United States had replaced Britain as Pakistan's main trading partner as the world of imperial preferential tariffs gave way to global trade with its primacy of 'the need for each country to…diversify its economy'.[154] The devaluation episode from the prehistory of this trajectory allows us to see the first GoP in action, in its effort to project itself against India, Britain, and the United States: the past and the then-future of its international relationships.

Acknowledgements. I thank the reviewer and editor of *MAS* (and, earlier, of *TIESHR*) for their suggestions and support. I am grateful to Dr Pippa Virdee for sharing portions from the Liaquat Ali Khan papers, and to Professor Ian Talbot for his encouraging comments.

Competing interests. None.

[150] See, for a parallel, N. S. Sylla, 'Fighting Monetary Colonialism in Francophone Africa: Samir Amin's Contribution', *Review of African Political Economy*, vol. 48, no. 167, 2021, pp. 32–49.

[151] Shahid Javed Burki, *South Asia in the New World Order: The Role of Regional Cooperation* (London: Routledge, 2011), p. 72.

[152] Simha, *History of the Reserve Bank of India*, p. 668.

[153] Wilcox, 'The Economic Consequences of Partition', p. 194.

[154] Khan, 'Pakistan and UK Trade Relations', p. 150.

Cite this article: Ankit, Rakesh. 2023. 'Delinking "the two rupees": The devaluation dilemma and economic divergence in the decolonized subcontinent, September 1949–February 1951'. *Modern Asian Studies* 57(3), pp. 918–939. https://doi.org/10.1017/S0026749X22000336