SPECULATION AND THE FUTURES TRADE

(VLEMING'S CHAPTER 12)

1. Speculation

a) *Introduction*

To discuss speculation, concentrating particularly on the role it plays in the business life of the Chinese in Netherlands India, we must begin by reminding ourselves of what speculation encompasses and the forms in which it usually occurs.

According to Professor Dr J. F. Schär in his *Handelsbetriebslehre* [*Theory of Commercial Management*], speculation has its origins in safeguarding against the future, which in business life means taking precautions to secure the future development of a certain enterprise. However, we are not used to including all these precautions under the subject of speculation, but only those taken with an eye to future price movements and the resulting profits which might be derived. So our definition restricts speculation to commercial operations within the confines of trade, because the possible advantages which lie in future price movements can be realized only through procurements and sales.

According to Professor Schär, a merchant can limit his level of speculation in those goods within his line of business as expressed by the following options:

a. he limits his involvement to core concerns, which is to say he shores against possible future price movements so as to cover future needs connected with the requirements of his business;

b. he expressly indulges in speculation but keeps sight of the actual basis of his business by limiting his speculations to those goods within his line;

c. deviating yet further from the above strictures he buys and sells goods with no intention of actually delivering them, but only to pocket the difference between his buying and selling prices. The nature of the goods has become secondary and no longer binds the merchant who instead ever expands his operations into all those commodities where his speculative mind perceives possible benefits.

In all three cases speculation shows only to two basic patterns. First, the speculator buys goods with the aim of selling them at a profit later on. In this case he speculates *à la hausse*, so he is a haussier. Second, the speculator sells goods he does not yet own with the aim of buying them cheaper prior to delivery. He speculates *à la baisse*, so he is a baissier.

Now what is the attitude of the Chinese in Netherlands India towards this speculative trade? Generally speaking it can be said that the desire to gamble has been a pronounced proclivity of these people. So not surprisingly speculation is particularly attractive to many of them, especially the type of speculation described under option c.

Very often the family relations generate tight bonds and strong mutual confidence between individuals, so it is particularly easy for members to solicit funds which can then be used as credit in their business. Nor is there much supervision, so the borrowed funds and advanced credits can be used for speculation if the borrower so desires. In fact these people can indulge in levels of speculation which may even endanger the whole trade. Several times rampant speculation has resulted in financial catastrophe, not only destroying the speculators but also reducing many *bona fide* merchants to misery.

To be reasonable, it must be pointed out that other factors have also been responsible for these financial calamities. Many of the business collapses can be attributed to the changed circumstances which have prevailed during and after the [First] World War. Furthermore we emphasize that we do not restrict our attention to the Chinese to imply that they alone are given to unsalubrious speculation. It would be superfluous to remind the reader of how other groups of people have been equally guilty of similar practices in recent years. However, it is not our business to dwell on the latter issue because this monograph is devoted solely to the Chinese business community.

The main triggers for the speculation-related debacles have been the over-extension and unscrupulous use of credit facilities, particularly on the part of European banks, brokers' officers and trading houses. Moreover, when we talk about Chinese in connection with speculation, we mean primarily the Chinese residing at the harbours along Java's north coast, especially Semarang, Surabaya and Batavia. It would be unfair to generalize about all Chinese in Netherlands India, since trade in the Outer Islands is generally based on a more solid and substantial foundation than it is in North Java.

b) *Items*

Many and various are the items which form the object of speculation of our Chinese compatriots. The big speculators with large amounts of capital dabble in real estate. They buy extensive terrains and in the cities they engage in land deals which altogether contravene the interests of the urban community as a whole. However, these large speculators are few in number and do not merit detailed discussion. Chinese speculators in stocks and debentures will also be mentioned here only for the sake of completeness. For our purposes, exports and imports which have attracted the attention of speculators are the items of prime importance.

The products which have attracted Chinese speculative interest are sugar, coffee, rice and pepper. Of these rice is an import while the rest are exports.

c) *Extended discussion*

The circumstances of war on the one hand, and natural events on the other, have provoked speculation in sugar and coffee to swell beyond its pre-1914 levels.

Mr Th. G. H. Stibbe, a senior member of the brokerage Gyselman and Steup, wrote an interesting piece called 'Termijnhandel op Java' ['The futures trade in Java'] in *Economisch-Statistische Berichten* No. 413 dated 28 November 1923. He writes:

> The character of Java's trade in its indigenous agricultural produce such as sugar, coffee and pepper, and in its importation of rice from Rangoon and Saigon, had been changing for years but more so since 1914.
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> The speculative element had hardly been absent beforehand, especially among Chinese traders in Java, resulting in occasional collapses which even then indicated the need for a regulating institution empowered to superintend transactions, mainly those involving Javan Chinese. This need is now felt more keenly than ever.
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> Two important factors have recently increased the risks for traders, particularly those dealing in sugar and coffee. First is the extraordinary scale and rapidity of the fluctuations in market values, and second the altered character of trade during the same years. These circumstances have offered the speculative trader hitherto unequalled opportunities to negotiate on an ever larger scale in increasingly less scrupulous ways.
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> The traders have been able to observe the scale of price fluctuations within short intervals according to a pattern of price hikes soon followed by steep declines, which is part of the general instability in market values for most Indies produce since 1914 (indirectly caused by the war). But if the first factor speaks for itself, the second factor may require some explanation.
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> In fact the speculator chooses to negotiate in those products which have the largest markets. Consequently the biggest turnovers can be expected and, as the speculator rightly perceives to be of most importance, the transactions can be finalized 'on delivery'. In Java the products which meet these requirements are sugar and coffee. The changed

circumstances of trade in these items will be emphasized below, not only to show how much the temptations to speculate have increased, but also to demonstrate how the risks for trade in general have been aggravated.

Presumably it is well known that the establishment of the United Java Sugar Producers (V.J.S.P) in 1918 transformed the sugar trade in Java. Previously the factories sold their own sugar under their own name, and usually without guaranteeing the time of delivery. Since the establishment of the United Java Sugar Producers, which now controls about 90% of the total sales of sugar grown in Java, the sugar is no longer sold under the name of the factory which produced it. Rather the association reserves the right to choose whatever factory it wishes, while at the same time guaranteeing a definite time of delivery as part of the sales contract. Although in some ways this procedure largely simplifies operations for the *bona fide* buyer-cum-exporter, on the other hand it grants the speculator considerable licence.

Formerly the speculator was limited in his actions to those of a haussier because, as stated above, the only contracts in circulation involved modest quantities of sugar to be provided by a specified factory. But the V.J.S.P. sold its sugar stipulating only the quantity involved and the time of delivery, without specifying the factory producing the sugar or from where it would be supplied. These conditions were sufficient for the speculator to speculate *à la baisse*, because all mechanisms had been lost for determining whether or not the trader-cum-speculator-cum-seller indeed owned the sugar he was selling.

As the primary seller, the V.J.S.P. protects itself against financial loss on long-term contracts by drawing up terms of sale which stipulate that the buyer must give a guarantee should the V.J.S.P. wish it. This is either a bank guarantee opening an irrevocable line of credit to the V.J.S.P. or some other satisfactory security.

However, such controls dissolve as soon as the transactions move on into secondary hands. Paying deposits or depositing bank guarantees are no longer required, and the pre-1918 limitations on the quantities to be bought or sold no longer apply. Secondary contract sales are no longer controlled as they should be by brokers and bankers, consequently the creditworthiness of the buyers and sellers drops below view. We hardly need to point out that last year the various second-hand traders took up direct positions within the major futures markets such as London and New York. The dangers have always existed for traders and speculators in Java, resulting in periodical debacles; but since 1918 the dangers have reached fever pitch and now threaten to wreak true catastrophe.

If difficulties have never been altogether absent, they were nevertheless rather limited in scope and affected only one or the other speculator and his small circle of sellers. This could transpire if the speculator lacked buyers for his hausse purchases, and involved financial losses which as a rule were still within reason. In 1917 a major crisis did develop among sellers, but this resulted from very peculiar circumstances related to the war. Otherwise there had been no cases of the widespread crises facing sellers which we have seen so frequently since 1918. For the last five years we have witnessed one storm drive out its predecessor, wild speculations take their toll on dozens of victims every year, with millions of guilders involved rather than the tens of thousands which used to be associated with such debacles.

The simplified business procedures created by the actions of the V.J.S.P. have indeed produced remarkable administrative benefits for *bona fide* sugar traders. At the same time, however, they opened up possibilities of hitherto inconceivable dimensions to the speculators.

So this is what happened to sugar. As regards coffee — also much beloved in Java, despite its slighter importance — a more natural course of events has changed the very nature of the product over the last ten years or so.

Formerly coffee was traded purely as a 'brand product', valued according to the virtues of the brand and the plantation which supplied it. But we have seen coffee gradually become a 'stock product'. More precisely the renowned blue Java coffee, or *Coffea arabica*, has been gradually displaced by the so called robusta coffe [*Coffea canephora*]. The latter was originally imported as an experimental plant, but it proved so ideal for the earth and climate, so capable of large yields and resistant to the known diseases, that it has come to deliver the bulk of our coffee production.

Formerly the consumer countries valued the blue Java or *Coffea arabica* by the name of the plantation which produced it, using this indication as the touchstone of satisfactory quality. But now that the stock product robusta coffee is offered, the buyer might as well have it delivered according to convenience. The only major condition made in the sales of this robusta coffee is that it must be of good average quality and that it was harvested in Java during the year of purchase.

In practice the same phenomenon described above for sugar has also beset coffee. Both cases have opened a wide field of speculation without any control over the speculators or, what is more serious, any possibility for the speculators' counterparts to protect themselves.

The contracting parties are both bound together during the entire and sometimes very long period of the coffee contract. Once the terms of contract between the parties have been fixed, both can only hope that the other will also fulfil his side of the deal. This concerns the ability of one party to deliver and the other to receive and pay for the traded goods. Given the sometimes long intervals between when the terms of the contract are decided and when the contract is finalized, both parties may trend towards unreliability, so paralleling directly or indirectly the vicissitudes of prices noted above for the sugar market.

Often one of the parties is frozen into a frightful game of patience, stealthily and uneasily watching the movements of the other party. But even in those cases where approaching danger can be anticipated, there are no prophylactic measures by which the vulnerable party can ensure that the bought goods will be delivered or that the sold goods will be accepted and paid for. The vulnerable party can only wait and see how a contract drawn up long beforehand will resolve itself.

As stated above, the element of speculation has never been absent in Java, nor of course in certain major commodity markets elsewhere. But because of the way things were, speculative institutions in Java necessarily used to be contained within certain so-to-speak 'natural' limits.

As clarified above these limits have been almost totally dissolved, so clearing the way for rampant speculation. Further, reckless speculation during and especially after the war has also swollen in the markets for pepper (black

Lampung and white Muntok) and rice, because like robusta coffee these products conform to standard qualities which facilitate their trade.

d) *Harmful Consequences*

There can be little question that the rampant speculations referred to above have had damaging consequences for the economic life and peaceful development of these regions, and that these damaging effects will continue. The following quotations from the annual reports of the Board of Commerce in Semarang clearly illustrates this issue in the context of sugar production.

> 1920: The year 1920 has been very idiosyncratic in terms of the course taken by sugar prices. They have fluctuated so extraordinarily as to be beyond compare. At the beginning of the year everything looked very bright, because the spot price for Sup. H.S.[1] was *f*35, compared against H.S. 16 at *f*32, with the remaining grades apportionately priced. Early in the year prices continually climbed with increases of several guilders a day occurring regularly. By about the second half of May prices peaked at *f*75 for Sup. H.S. and *f*70 for H.S. 16 and higher grades. This peak coincidentally presaged a horrendous fall in prices, so that by the end of July the spot price for Sup. H.S. was *f*56, with further falls to *f*50, *f*42, *f*30 and *f*25 respectively by the end of the following four months. By the end of the year the spot price was no more than *f*20.
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> The consequences of such a price bust can be readily understood. A brace of obstacles must now be overcome. The cavalcade of receiverships was led by the Java Overseas Company which went into bankruptcy with a deficit of approximately *f*15,000,000. However, in Semarang no major bankruptcies have occurred, so well did the various Chinese merchants make arrangements. . . .
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> This year the Chinese intermediary traders have played a very important role in sugar. The hausse position which they occupied from the outset appeared favourable, and although their optimism was unfounded, their line of action fed on the bull market apparent in America. Many people thought that prices would peak far down the track even when sales were as high as *f*75 for Sup. H.S.
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> The Chinese initially earned millions, but they also lost millions in the second half of the year.
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> 1921: Because the sugar market has been on a more even keel this year than last, speculation has been less rampant, but it must be pointed out that the financial situation among the Chinese has been largely responsible for this new state of affairs. Business lost its speculative character due to the huge losses suffered by most Chinese merchants last year. Consequently people were particularly interested in starting new businesses, but regrettably the government decided to raise taxes to their highest sustainable levels right at this very unfavourable juncture. . . .
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> The government had missed out on millions of war-profit tax because the State Revenue Office had not been timely in taking the appropriate measures during the period when profits were being made. But the government will probably fail to make amends

[1]*These abbreviations are not explained in the text. Sup. is short for 'superior'; H.S. is probably sh*
for Handelssuiker, *i.e. 'marketed processed sugar'.*

because, whereas tappable surpluses used to exist, these have now almost all vanished. Old established Chinese companies entered the valley of doom and have actually ceased to exist. Although the company name is retained here and there, the company no longer operates its former business.

New companies have often been established beside the old, and as a result the tax debtor has completely escaped the government's grasp.

1922: Last year was not ruinous for sugar traders; on the contrary, big losses were unheard of. This year the only companies which made money were those which adopted an optimistic stance with steadfast hope and prayers for benediction upon their enterprise. Here we refer to the 1922 sugar harvest because there was little business during the first four months [before the sugar harvest]. Those businesses which underquoted their selling prices generally took a heavy blow in their unsuccessful efforts to recover their losses by resetting their underquoted prices. There was a striking increase in second-hand trade this year compared to last year, particularly among the Chinese in Semarang.

Many people who had steered clear of sugar during the last years took it up again. This trend is particularly clear from the transactions of the V.J.S.P. and was mediated primarily through the newly established companies which had been created in response to tax pressures. It was also strikingly easy to arrange bank guarantees and to finance deposits. Flushed with capital which needed to earn interest, the banks offered more reasonable terms on securities, and this policy certainly influenced the situation.

Consequently the chances of a crisis in the sugar trade due to sudden price fluctuations have increased. But generally the second-hand trade in sugar has enjoyed a sound basis and there is no call for a craven fear of a sugar trade debacle.

The policy still held by the V.J.S.P. to guarantee its transactions is therefore also a security. A lively speculative market has existed throughout the year and presumably will increase in the years to come. However, it is striking that many traders who formerly entered the market merely for speculative purposes now try to gain entry into the world market, particularly in terms of dealing directly with consumers abroad.

1923: Price fluctuations were again marked this year and occurred throughout the period. The normalized conditions which we predicted in our last summary have not materialized at all, so that uncertainty has swollen again. After prices had stabilized between 13 and 14 guilders till the end of January, they started to rise in February by a few guilders a week, just as had happened in previous years as a result of baissiers needing to meet their pledges. This little axe cut many of them down.

The market configuration, including the pressures on sugar consumers in the far east to pay the Java price, has stimulated lively speculation. At the same time prices for sugar from the 1923 harvest rose strongly and peaked by approximately the end of April. Afterwards prices began to decline steadily because it then seemed impossible that the market could recover. This steady decline unfortunately coincided with the period of highest production so that when the prices bottomed out in August many major companies went bankrupt. Afterwards there was a steady improvement again until November when prices rocketed, again giving free reign to speculation which had been laid low for several months. The market hummed until its commitments far exceeded available local stocks which had been sharply diminished by the considerable level of exports. . . .

The export figures also promised to be large, as indeed was proved by the record amount of sugar shipped in July. But because the bumper harvest became available at a tempo which exceeded even the exportation rate, the received goods stagnated in the beginning of August, which particularly affected the Chinese circles here. Soon several major and, finally, various minor Chinese speculators postponed their payments. This directly caused bankruptcies which aggravated the sense of panic, and by mid-August the price of processed superior quality sugar had fallen to *f*13. Some large trading companies then took advantage of this ruinously low price to mop up the remaining stocks. This shows that after the forced liquidations the prices attract practically no genuine offers although they are given a boost by renewed baissier speculations.

The market then recovered within a very short time, but the damages caused by the ruthless measures which the Chinese merchants had taken against each other could not be repaired. There was no question of assistance being extended during those days of terror, rather everybody tried to save his own skin at the expense of his fellow compatriot, and in some cases people offered to lend sugar which was simply not in stock. No co-operative effort could succeed because everyone acted as if he was sufficiently endowed to finance his position, without that actually proving to be the case.

The main cause of the debacle lay in the drastic hyperspeculations and unlimited credit found among Chinese merchants in Java. A second cause must also be the boycott which the Chinese merchants stubbornly carried out against Japan for several months. The boycott disavailed the Chinese merchants of their share in the speculative position against the Japanese sugar requirements which is otherwise an annually recurring prospect, and in the end they were forced to fulfil any Japanese requests for Java sugar as a matter of urgency. For quite some time Java sugar was the cheapest sugar on all world markets, which brought about a debacle in Java itself.

1924: The past year has not been particularly advantageous for the sugar trade. Prices declined almost continuously so that at the end of the year they were below the level where they had been a year beforehand. In that there was generally less inclination to speculate *à la baisse* than *à la hausse*, speculation overall lost more money than it gained.

Trenchant difficulties were not experienced because the lessons of 1923 were not completely forgotten and also prices fluctuated less markedly this year. The course of prices during 1924 gives grounds for some satisfaction, in so far as some stability in prices was achieved. This stability, or more correctly a long gradual downward trend, made speculators more cautious and prevented any outstandingly tense situations.

On the topic of future prospects, the report remarked that the increases in beet sugar production would keep sugar prices low, a sugar shortage could certainly not be anticipated, and only low prices could maintain consumption at its current levels. We may now begin quoting the report again.

That stability for which we longed for years, and which we seemed to have reached two years ago, we can maybe look forward to now. As a result, whereas the exporters used to have much of their business hampered by unbridled speculation, they will now see an improvement in their influence over the issue.

True, exports to the west will decrease because, as has already happened in the case of America, Europe will also be lost to the Java market. Nonetheless there are still major possibilities in East Asia. These possibilities however depend on a normalized political situation in China as the *sine qua non.*

Numerous sugar speculators in Semarang failed during these years, particularly in 1923. This is shown below by the verdicts delivered by the Counsel of Justice on Chinese bankruptcies.

	Number of Bankruptcies	Assets	Debts
1920	43	*f* 108,066.98	*f* 1,605,361.13
1921	48	*f* 790,040.73	*f* 8,572,870.05
1922	122	*f* 794,726.69	*f* 5,554,311.51
1923	151	*f* 1,932,573.85	*f* 18,659,320.60

Of course not all of the bankruptcies involved sugar speculators, but we may safely assume that more or less half of the cases and two-thirds of the net outstanding debt can be subsumed within that category.

Particular attention should be directed to the passages quoted above which indicate deteriorating business ethics. In 1922 numerous businesses were created 'in response to tax pressures' or, in other words, the old businesses were abandoned to their own devices and the taxes simply went unpaid. And the 1923 report indicated that the Chinese refused to help each other weather the crisis. To our knowledge such turns of events would not have occurred during the pre-war years.

It is also worthwhile directing our attention to the report for 1922 stating that 'Flushed with capital which needed to earn interest, the banks offered more reasonable term on securities'. In this context we have heard some very reliable sources assert that in one Indies commercial town, a limited liability company (which we shall call A) operated on a capital basis of only some hundreds of thousands of guilders while turning over approximately 63 million guilders through speculation in the sugar trade. Another trading company, with a capital basis of several millions, in one year had a substantive turnover of 22 million guilders and a speculative turnover of 80 million guilders in sugar.

It cannot be disputed that the banks aided unsound speculation by financing the millions of guilders required, nor that such enormous price upheavals might raise the possibility of benefits but yet they also bring on risks which must be borne, however unwillingly. The same reliable source told us that one of the above-mentioned trading companies suffered a loss of more than twelve million guilders in one year. The following year the company was again involved in speculations to the tune of tens of millions of guilders.

Besides the limited liability companies, there are lots of companies which can be characterized as 'pure' speculators. They do nothing but buy from and sell to fellow Chinese compatriots, Arabs and British Indians. With virtually no capital basis these companies could achieve a turnover of millions, as proven by what our reliable informant had to say of a third limited liability company. Its working capital was no more than *f*400,000, yet it achieved a speculative turnover of around 70 million guilders.

We have also heard from another reliable source that some of the speculators in pepper and coffee, whose assets were worth only several thousand guilders, achieved turnovers amounting to millions of guilders.

1924 had been an idiosyncratic year for coffee, as shown by excerpts from what Mr Stibbe had to say in *Economisch-Statistische Berichten* No. 461, of 29 October 1924.

> At present, after an elapse of approximately one year, we read in the Dutch press: 'According to the *Bataviaasch Niewsblad* coffee exporters are facing great difficulties because the Chinese speculators have more than bought out the harvest. Most speculators lack capital and so several closures can be expected. The tightness of the coffee market in Europe demands that the contracted quantities be delivered and so makes the situation still more critical.
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> The Chinese Chamber of Commerce invited the Trade Association to meet with exporters so as to open up discussions with European buyers on possibly anulling some proportion of the contracts. *The Chinese merchants refused to specify their contracts so an accurate assessment of the shortfall was impossible.* The exporters tried to hammer out agreements with individual buyers but they still had their feathers singed depending on their financial resilience.'
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> Now I have italicized a sentence from this brief news item because it clearly shows how baissiers were able to go on speculating unhindered and how the *bona fide* European coffee exporters fell victim. The Chinese speculators guaranteed sales contracts beyond the harvest and hence cannot fulfil their contractual obligations. Not only can they not deliver the sold goods, they are also apparently unable to redeem their contracts at the higher price which would be required to restore such a breach of faith.
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> The most vexatious point in this whole issue is again worth highlighting. *The Chinese merchants refuse to make their position public, so an accurate assessment of the shortfall proved impossible.* This greatly aggravates the obstacles blocking some resolution to the situation. There are still no mechanisms in Java to ensure that contracts of trade guarantee delivery of the products. And so people — mainly Chinese but they are not the sole propogators of the practice — speculate with gusto on the back of the European exporter. For as Mr Th. L. wrote in the February 1924 issue of *Koloniale Studiën*, in response to my article which had appeared in November 1923, 'If all goes well people pocket the profit; if it fails people declare themselves bankrupt and will have been spared the tax burden'.

Here again the finger of accusation has been pointed at the Chinese community.

Not only coffee but pepper too has experienced a difficult year. Given business's exposure to a series of constant shocks, the time has come to regulate the various forms of trade, and thereby reign in the so far unbridled speculation.

2. The Futures Trade

a) *Introduction*

We have already explained what speculation precisely means in our Indies community, the consequences which will come into play, and the call for regulation to act as a dike against the wild commercial currents which batter our shores.

Mr Stibbe can be credited for at last and forever having woken up many sleepers. Although his articles have been attacked from many sides, they have promoted the idea of organized consultation on this issue. His article in the *Economisch-Statistische Berichten* No. 413, already referred to above, contained the following relevant passage:

> A situation has gradually developed in the so-called second-hand trade of Javan produce which must continually lead to further catastrophes and constantly place the decent *bona fide* merchant in grave danger. Can means be found to improve this situation? Are there ways which can lead to more normal relations by which the trader in produce can enjoy greater security in his undertakings?
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> To answer these questions I will pose a third. If the appropriate opportunity arises, is it possible to create in Java a supervisory body whose task is to keep a register of all second-hand and even first-hand transactions, should the parties wish to have the transaction registered or even as a mandatory requirement, under *particular* conditions?
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> I refer to the liquidating cashier, an institution which places itself between the buyer and seller such that, *under specific circumstances*, it takes over every procurement and sale as though it had carried out those transactions itself, and assumes responsibility for further liquidation of the contract between the related parties.
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> Note that I italicize the words 'particular' and 'under specific circumstances', because it would indeed be wrong to think that the liquidating cashier is involved in all transactions negotiated within the goods market. It confines itself to the so-called 'future transactions of merchandise' where it acts as the third party procuring and guaranteeing orderly expirations and liquidations.
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> So it is of utmost importantance to start by reinforcing an accurate comprehension of 'future transactions' and how they are created. This way the essential similarity between the sorts of transactions which would qualify as 'future transactions' in Javan sugar, coffee, and so on, as outlined above, can be assessed.
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> If 'future transactions' then by definition there should also be a 'futures market' and hence an exchange where the so-called futures prices are quoted. No such exchange yet exists in Java, which quite readily explains why we remain oblivious to the real picture of these 'future transactions' as they occur in Java.
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> To start with, in this context I would like to distinguish unequivocally between sales on delivery which are created by 'producers' (such as the V.J.S.P. acting as executor, owners of rubber or coffee plantations, or the Government of Netherlands India which sometimes sells the tin extracted from the Bangka operations on delivery), and 'on-delivery' transactions which take place at *second hand* in the so-called staple items such as sugar, coffee, rubber, tin and so on.

The first category of sellers are owners who have products already in stock, or who can definitely anticipate the availability of goods which they themselves produce and can immediately send to the buyer. Here there is no question of 'trading' except in the capacity of seller. Quite the reverse is true of the second-hand merchant or speculator, as explained above.

Herein lies the basic distinction between 'trade on delivery' and 'future transactions'. Those who trade on delivery deal with products which either already exist or can be produced by themselves with certainty, and which indeed can only be delivered by the seller and received by the buyer. But as for future transactions, the seller as well as the buyer can individually settle his involvement of his own accord entirely independently of the other party. So the parties can settle the transaction through the intermediation of the liquidating cashier, either by a transfer of funds reflecting the difference between the selling and buying prices, or by the sold goods actually being delivered and paid for.

Now it can be regarded as altogether impossible that sales for a future date made by producers, which indeed are better called sales on delivery, could qualify as 'future transactions' in the sense of the term used here. But whether or not the analogy with 'future transactions' can be applied to the behaviour of the second-hand merchants, it cannot be denied that their behaviour arouses insecurity. Over and above all the other hazards (dealt with previously) which can affect merchants in Javan produce, and which can be more or less compared with the risks attached to giving credit, a novel risk has arisen from the dubious behaviour of the second-hand merchants. As we have seen they feel no compulsion to trade in goods actually at their disposal, and the associated insecurity can have far-reaching consequences.

Until now trade in Java has followed the old routine despite the gradual evolution of the decidedly new trends described here. As a result the regulating mechanisms developed in Europe and America have been absent from Java. The problem looms ever larger, and whether or not interested parties hold that it is good policy to avoid a watchdog stance on the issue, the problem needs to be squarely addressed.

As explained above, circumstances in Java have gradually changed during the last few years such that basically undesirable situations have developed. In my opinion the commodities merchant in Java must be offered a reliable basis giving him the opportunity to carry on his business with certainty.

A 'liquidating cashier' in the thoroughgoing sense of the term, cannot help us at present. But the issue remains whether it would be possible to establish a similar institution carrying out comparable functions. There could be some sort of insurance business which can offer, primarily to the merchant but also to the speculator, certitude that the deals between them will be brought to a fair conclusion. I am not going to skirt around the difficulties which present themselves in view, nor deny that obstacles (maybe in the first place the speculators themselves) will manifest themselves and have to be overcome. Yet I am so totally convinced of the benefits deriving from the operations of such an institution that I wish to bring the subject to attention and plead that it be given special consideration.

As was the case under the liquidating cashier system, the right of disposition over the goods must be withdrawn from the speculator as soon as he is unable or unwilling to deposit and maintain the required security with the intermediary institution. This must be clearly expressed as the institution's foremost aim.

As can be made clear by quoting one of Mr Stibbe's statements (*Economisch-Statistische Berichten* No. 465, 26 November 1924), it has always been his intention to organize only the *on-delivery* trade in produce, rather than the *futures trade* as such.

> Meanwhile ..... I would like to point out that I have no more urged for regulation and control 'in order to reduce the risks to the contracted buyers and sellers of produce on the futures, than that the *del credere*[2] be taken wholly into the account of an established liquidating cashier or some similar arrangement in the hope that this will concurrently prevent hyper-speculation'.
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> All I have continually urged is protection for contractors, buyers and sellers in — and here lies a very important distinction — *on-delivery* produce. I have always drawn attention to the major difference between transactions in 'on-delivery produce' and 'future transactions'.
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> In Java *all* transactions in products are based on the *actual delivery* of the contracted goods. But as a matter of fact it typically occurs in 'future transactions' that *at any moment*, in *any* transaction, either party can independently settle the contract merely by compensating the other party with a sum equal to (and no more than) the difference between the price at the moment of settlement and the price stated in the contract.
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> The discussion of the idea I propose must be firmly coupled with the following principle - *the intention alluded to above that in Java all transactions in products involve the actual delivery of the traded goods.*

On the other hand, we are of the opinion that the development of an organized produce market must necessarily include a separate market for future transactions in league with the liquidating cashier, although this cannot be expected during the initial years.

To explain the matter well, it is desirable to emphasize the difference indicated by Mr Stibbe between real 'on-delivery transactions' resulting in delivery and 'future transactions'. On-delivery transactions are inherent to real trade. Here the speculative element is reduced to the time which elapses until the goods can be delivered, and the merchant will ensure that the lapse bears as little influence as possible.

The futures trade on the other hand arises directly from speculative trade. The nature of the goods is of secondary importance since the sole aim of the merchant is to take advantage of the differences in price at different junctures. Such trade has nothing to do with real trade in goods and is not involved in delivering or receiving goods, as the merchant's goods exist only in the abstract. Hence futures trade is to be regarded as *speculative trade organized within a market exchange.*

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[2] *The guarantee to the selling agent that the buyer is solvent.*

In some respects, then, the term 'futures trade' is less correct than if we talked about 'transactions on delivery' in the sense meant by Mr Stibbe.

b) *Organization*

During 1924 a great amount of discussion took place in Batavia among those involved in the goods trade, and this at last led to the establishment of the association called 'The Bureau for the Registration of Futures Trade in Products' on 12 December 1924. All the members of the Chamber of Exporters in Batavia joined this new organisation. Its role as established was to give assistance to the *bona fide* export trade and hence to find a solution along the lines indicated by Mr Stibbe. As for the sphere of activity and the initial scope of the bureau, the following comments seem apt.

For the time being the only contracts registered and carried to completion were those stipulating terms of delivery of more than eight days (in the regulation called 'future contracts') in black Lampung and white Muntok pepper and Palembang robusta coffee. All three products have a large market in Batavia. This was a sensible limitation, because too large an initial scope for the association might have increased its chances of failure.

The services of the bureau must be availed in the following circumstances:

(i) by members of the bureau in all contracts signed either by or in their name or on their behalf;

(ii) by participants (as defined in articles 12 and 13) in all contracts signed either by or in their name or on their behalf, if such registration is considered necessary (here including contracts made with third parties);

(iii) by brokerages (as listed in article 14 of endorsed brokerages) where cited as party to those contracts which must be registered, according to (i) or (ii), because the contract cites the bureau member or participant involved.

As regards the members (who also belong to the Batavian Chamber of Exporters) it must be pointed out that the obligation to register rests on all of their offices, wherever they might be located, not merely on the branches established in Batavia. They may draw up future contracts only with other parties also subject to the conditions of the regulations, i.e. the other members and the 'participants'. The regulations explain this point.

> The participants must usually be only the large, regular intermediary merchants in pepper or coffee here in the city, as well as the major European merchants in Palembang etc. The participants must register their contracts with other participants as well as their contracts with the bureau members. Participants, however, have one freedom which

> members lack, which is to conclude contracts with small traders who cannot meet the requirements for being nominated as members. Therefore the participants are generally those who purchase produce directly.
>
> The only other difference between participants and members is that the participants do not belong the Batavian Chamber of Exporters and so have no influence on the board of managers or the changes in the regulations. Participants and members are otherwise alike in all other respects such as payments, deposits, dunnings etc.

Although the mode of operations of the Dutch liquidating cashiers was initially held up as a model, only a part of their operations could be adopted owing to the very different situation in the Indies compared to the Netherlands. The most important adoptions were:

(i) that the contracting parties should negotiate a security against possible changes in market values;

(ii) as intermediary, the Registration Bureau should not liquidate a contract unless either (one or both) party could not properly settle his obligations to the Registration Bureau. This decisions allows 'the right of disposition over the traded goods to be withdrawn from any contracted party as soon as he is unwilling or unable to deposit and maintain the required security with the intermediary institution' (Stibbe), and so was a major step towards improving the recent situation.

As for (i) mentioned above, a fortunate solution was found to a major problem concerning the security. It would have been difficult to follow the Dutch system which stipulates that *f*3,000 must be deposited for each contract, because such a requirement would have frightened many peopled away from registering their contracts. Therefore people thought along the lines of countenancing the solution which the V.J.S.P. had already taken and prescribed, whereby the parties concerned provide a guarantee from one of the banks as their security to the Registration Bureau. This made it easy for merchants to have their contracts registered in the absence of large deposits. Such a measure was very important, especially for the European export houses whose systems of extending advances and guaranteeing harvests tie up most of their business credits.

Every Monday a *passage* was held. The net credit or debit balance from all of the registered contracts was calculated as though each member would decide to settle on that date against the *passage rates*. These were the spot prices for the registered products, as determined by a Passage Committee made up of five members. If they found that the available guarantees were insufficient to cover a debit passage balance, then every member or participant was obliged to cover the shortfall by increasing his guarantee the next day at the latest.

The Bureau was managed by a Council of Management consisting of five members who nominated or dismissed the Manager who would be responsible for the day-to-day administration. Whether as commissioners, brokers or merchants, individuals with interests in one or more of the registered products were ineligible for the Council of Management. Ideally they came from the banking institutions and were nominated or dismissed by the Board of the Netherlands Indies Bankers Council [Bestuur der Nederlandsch Indië Bankiersvereeniging] in Batavia. This way the impartial character of the institution was adequately safeguarded, while the banks could also supervise the new participants and by the same token look after the guarantees which they supplied. The guarantees amounted to *f*2 per *pikul* of black Lampung pepper, *f*4 per *pikul* of white Muntok pepper, and *f*3 per *pikul* of Palembang robusta coffee. These guarantees were considered sufficiently large to cover any shakeups in the marketplace.

The Registration Bureau successfuly operated for only a short period before being liquidated on 18 April 1925. According to our expert informant, the reasons were firstly (and mainly) that the Chinese stayed away and secondly the distrust which appeared among a number of the European merchants.

Regarding the second reason, we have seen that the Regulation had decided *inter alia* that the members had to register all their transactions with the bureau. So the members were prohibited from carrying out transactions except with other members and with participants. But the latter were required to register only those contracts drawn up with members and with other participants, and were otherwise free to do business with outsiders as well. Thus, as might have been anticipated, *members* donned the cap of *participants* so they could enter into contracts with outsiders, so making the regulations of the bureau ineffectual. This led to an ever growing distrust amongst the members which finally opened up as a running sore. Indeed this is one area where observers had criticized the way the bureau was established.

One of our expert informants tendered the opinion that these kinds of institutions must grow gradually so that they can take root in regular business life and wax on an organic basis. As an example he cited how an arbitration system had been established in Surabaya despite the enormous initial difficulties. The system was originally confined to specific commodities and the participants were required to call upon the arbitration of the Trade Association only as far as the quality of the commodities was concerned. After this system operated for some years, the arbitration of the Trade Association was made compulsory in specific goods. Afterwards the system was expanded to include compensation, so now the whole arbitration process (including quality and indemnification) has been absorbed by the Trade Association.

The establishment of the liquidating cashier would be the next step although the time, according to our informant, is not yet ripe. The Registration Bureau, on the other hand, which had directed trade from above through the bankers and major exporters, has collapsed altogether. Our informant saw beforehand that it must fail even though other people did not agree with him, at least not entirely. Still we hear that within the foreseeable future efforts will begin again to regulate the matter on a different basis and with more modest requirements on securities.