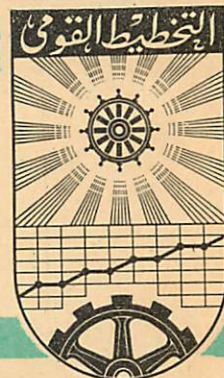


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Financial Mechanism of a
Socialist Economy

(on Poland's Example)

by

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I. Financial system of a socialist economy.

1. The structure of the financial system.

The socialist economy is composed of many units, which are economically independent, such as socialist (i.e. state and collective) enterprises, private enterprises, individual consumers etc. This economy is managed in a planned manner, which imposed a certain limitation on the independence of the economic decisions taken by separate units. The instruments of limiting the freedom of economic decisions are of different types, as for example the general ~~prescriptions~~ ^{instruct-}ions of the civil law, the direct orders given by upper organizations (National Planning Office, Ministries etc.) and the indirect instruments stimulating directions of decisions according to the objectives of the general plan. The financial system is playing an important part among these instruments. All economic decisions - in order to be effective - must be connected with the means sufficient to put them into execution. This means that the plan regulating the monetary revenues and expenditures of the independent economic units may be an efficient instrument of managing their economic activity. The planned regulation of monetary revenues and expenditures is the main objective of socialist financial system.

This system is composed of the following main parts:

- a) The financial system of the socialist enterprises which includes the state enterprises and the collective ones, both being in general very similar, but different in some important questions, as well as the industrial, commercial, agricultural and others enterprises, each of them having its own branchial characteristics).
- b) ^{the} The state budget, which serves in general as an instrument of appropriating the financial means among all the branches of the national economy and as an instrument of financing the activity of the state in non-productive sectors, such as education, public health, administration, national defence etc.

- c) The insurance financial system, which is practically reduced to the financial activity of one state organisation of "general insurance", dealing with material goods, Social insurance being included into the state budget.
- d) The financial system of banking and credit.

There does not exist a separate financial system for the population (individual consumers) and private enterprises, as a result of their independence of the state. The ^{pre}scriptions, regulating financial relations between individuals and socialist organisations (state budget, enterprises, banks, insurance company) are included in their respective sectors financial systems.

2. Financial system of socialist enterprises (a short outline)

The most important source of monetary revenues of enterprises is the sale of goods and services. The sale is effectuated at prices fixed by the state organs, save exceptional cases in which the price of individually commanded and produced goods may be fixed by contract between sellers and buyers (this is the case of very special investment goods). The industrial enterprises sell their products at so-called industry sale prices, the whole-sale commercial enterprises sell them at wholesale prices (industrial sale prices increased by wholesale margin), the retail commercial enterprises sell them at retail prices (wholesale prices increased by retail-margin). The retail prices are fixed by the state organs at the presumed equilibrium level of supply and demand, and wholesale prices and industry sale prices are deducted from retail prices.

As a rule, the industrial sale prices cover not only planned average costs of production (the use of capital equipment included) but also give a surplus, which is called "monetary accumulation" (gross benefit). This is the main source of financing state expenditures: both productive and non-productive ones. The management of the gross benefit of the socialist enterprises is one of the most important problems of the financial system.

The gross benefit of each enterprise must be divided between centralized funds (state budget among them) and the decentralized ones, in order to

allow to finance both centralized expenditures (big investments, all non-productive expenditures of the State), and decentralized expenditures (small investments decided by enterprises themselves, participation of workers in, net benefits, bonuses etc.). The instrument of dividing the gross benefits is the turnover tax.

In most cases the rates of the turnover tax are calculated individually for each commodity. These rates are calculated as the difference between industry sale price and the so-called "plant price" of each good. The "plant price" includes:

- average planned costs of production.
- rate of net profit.

Average planned costs of production are calculated for all enterprises putting out a given kind of goods. Of course, each of these enterprises may produce this kind of goods at different costs, according to differences in capital equipment, productivity of labour, natural conditions, etc. But the turnover tax is fixed at equal rates on this good unit from every enterprise, regardless of these differences. This means that the rate of profit included in the "plant price" is also an average one, and that in reality the rates of profit in each enterprise of the same branch of industry are different. In some special cases, when the differences in individual costs of production of single enterprises are extremely high (and it happens especially in mining, where the influence of natural conditions of production on costs level is very great) some of the enterprises have deficits instead of benefits. In such cases, the trust (Union of enterprises of the same branch) organises the repartition of benefits among enterprises, in order to cover the deficits of those working in unfortunate natural or economic conditions, by the over-average benefits of the other ones, working in better conditions.

The turnover tax flows directly to the State budget. The rest of the "gross benefit" of the enterprise after deduction of the turnover tax is called its profit.

It is necessary to underline that the rates of profit, included in "plant prices" of different commodities are equal, or differentiated deliberately,

when it seems advantageous in order to stimulate or to limit the output of certain commodities. When it happens (rather seldom), that the "plant price" is higher than industry sale price of certain good, - the rate of turnover tax gets a negative value, meaning that the producer of such a commodity instead of paying the tax receives an allowance from state budget for every unit sold. It is also necessary to underline that the turnover tax system (of positive and from time to time negative payments to the State budget) plays the regulating role only on the level of an industrial branch (trust, Union of enterprises) not on the level of single enterprises. The trusts being responsible for inter-branch economic policy, must look after repartition of benefits among their enterprises.

The profit of an enterprise is further divided. In state enterprises one part of the profit forms the so-called "bonuses fund" another part forms "fund of development" - and the rest is transferred to the trust. The rules of forming these funds are rather complicated. In general, a proportion is maintained between the bonuses fund and the loan fund and the increase of the benefit (as compared to the last year). The percentage rate of the share of the fund of development in the total benefit is fixed by the ministry of finance for the trust, and the trust is fixing it for each enterprise. These rates must be fixed for a period of no less than five years, in order to give the necessary perspective in planning self-financed development in every trust and enterprise.

The rest of the benefit has to be transferred by the enterprise to the trust's account. The trusts are obliged to transfer a fixed amount of these payments to the State budget, and are using the rest of them (a) for covering the planned deficits of other enterprises (b) for increasing the reserve-fund of the trust.

To summarize the system of formation and allocation of state enterprises gross benefits may be outlined as follows:

Enterprise's Financial System

	Revenues from the sale of goods	R	
	(at industry sale prices)	-	
less	Costs of production	C	
equal	gross benefits	= A	
less	turnover tax (and allowances)	- T	state budget
equal	profit (or deficit)	= B+E	+GL
less	"Fund of bonuses" formation	- C	
less	"Fund of the development" formation	- D	
equal	Transfer of profit to the trust	= F	
	<u>Trust's financial system</u>		
	Transfers from rentable enterprises.	F	
less	Allowances covering planned deficits and funds formation in deficitary enterprises	- E	
less	Trust's reserve fund formation	- G	
equal	Trust's payments to the state	= H	state budget
	The fund of development of an enterprise is devoted to cover:		
	a) The expenditures connected with capital investments.		
	b) The expenditures connected with increasing stocks.		

Every state enterprise is equipped by the state with its own capital whose amount is equal to the value of a) capital equipment being at the disposal of the enterprise, b) standard amount of floating capital, i.e. value of standard stocks of raw materials, unfinished production, finished goods etc. The initial equipment of a new-organized enterprise is financed from budgetary funds. The main source of increasing the own capital ("own means" as it is called in order to avoid the word "capital") of existing enterprises is their fund of development. Only general reconstructions of existing enterprises, or creation of new plants within existing enterprises, may be financed from budgetary funds.

So, the rate of development of existing enterprises is regulated through the regulation of their rentability (price policy and turnover tax) and of the share of the fund of development in the net benefit.

The re-investment (renewal of existing capital equipment) being financed by amortisation fund, the fund of development is devoted chiefly to self-financing of new investments. But in practice, the amortisation fund and the part of development fund, devoted for investments, are unified in one fund called "the fund of investment and reconstruction". It may happen that this fund of investment, accumulated in a given year by a given enterprise, does not cover the amount of expenditure included by the enterprise in its financial plan. In such a case, the enterprise may apply for a bank investment credit. The investment credits are reimbursed from the accumulation of the investment fund in coming years.

The increase of standard stocks is planned by the enterprise independently. No directives are given in this area. But the enterprise is obliged to cover first the increase of the standard stocks from the fund of development, and only then is authorized to transfer the rest of this fund on account of the investment fund. This means that there is a competition between the needs for increasing standard stocks and the needs for new investments within an enterprise.

Standard stocks are planned, including permanent stocks of raw materials, unfinished production and finished products, needed in order to run normal activity. They do not include season or special stocks - these being financed exclusively by bank short-term credits. The bank short-term credits cover also the claims of enterprises emerging from the delay in settling the transactions in goods and services. The average period between the date of furnishing goods and the date of monetary settlement is of 12 days, so in the average, the bank credits granted to this purpose amount to 12 - days turnover.

The annual financial plan of an enterprise includes a summary table, which has the form of a balance-sheet of monetary revenues and expenditures. It is divided into 4 chapters as follows:

Financial plan for the year

(Simplified)

EXPENDITURESREVENUESChapter I: Gross Benefit & Net Benefit

1. Costs of sold goods and services	1. Revenues from sale of goods & services.
2. Turnover tax	2. Budgetary allowances
3. Net benefit	3. Net deficit
TOTAL	TOTAL

Chapter II: Repartition of the Benefit and Financing Deficit.

1. Net deficit	1. Net benefit
2. Bonuses fund	2. Allowances from the trust
3. Development fund	
4. Transfer to trust	
TOTAL	TOTAL

Chapter III : Own Circulating Fund

1. Increase of standard stocks	1. Part of development fund
2. Reimbursement of bank credit.	2. Bank credit
3. Transfer on investment fund.	3. Reduction of standard stocks.
4. Others	4. Others
TOTAL	TOTAL

Chapter IV : Financing Investments.

1. Costs of investments and renewal	1. Part of development fund ..
2. Reimbursement of credits	2. Amortization fund..
3. Others	3. Budgetary allowances
	4. Bank credits ..
	5. Others.
TOTAL	TOTAL

The annual plan does not include needs for the formation of over-standard stocks, or bank credits granted in order to cover them. This kind of financial operations is estimated only in quarterly plans.

In order to prepare their financial plans (year plans), the enterprises get some directive indicators from upper organisations. As a rule, these indicators include the amount or the rate of increase of the gross benefit (as compared to the previous year), the share of the fund of development in the net benefit), the budgetary allowances for investments (if any centralized investments are planned). The enterprise has to keep these directive indicators in its plan, or to establish its objectives above (when they indicate minimum revenues), or respectively under (when they indicate maximum expenses) their level. The enterprise's financial plan is not approved by anybody other than the director of the enterprise and the workers' council. But - as far as the financial needs of an enterprise have to be covered by bank credits - financial plans must be discussed with bank's office representative and the credit requests must be approved by the bank.

In quarterly plans enterprises estimate the fulfilment of annual plan's targets, especially of the formation of the benefit and their own funds, in order to correct the requests for credits formerly granted by the bank (credits of standard stocks, investment credits), and, besides, they calculate their needs of credit on over-standard stocks and of settlement-credits.

3. The financial activity of the population and private enterprises.

The planning of financial activity of the population and private enterprises, i.e. planning of their monetary revenues and expenditures, serves above all, as an instrument of maintaining equilibrium on the market of consumption goods and the production goods which are furnished to private producers (mainly small farmers). The inclusion of private production and individual consumption in the same financial plan - theoretically wrong - is in practice unavoidable as a result of the difficulties emerging from the separation of individuals' expenditures on consumption from their expenditures on production. For the purpose of analysis, of course, separate plans of individual consumption, of private agriculture (which in the only important private kind of production) and other private economic activity are

prepared but for operational work only one plan is drawn up, containing all financial relations between the socialist sector and particulars.

The main sources of monetary revenues of individuals are:

- a) Wages, salaries and other kinds of remuneration paid by socialist enterprises, organizations, institutions etc.
- b) pensions, allowances, scholarships etc. paid by the State budget (which now includes formerly existing separate social insurance fund),
- c) revenues from the sale of agricultural and others products to the socialist enterprises,
- d) indemnifications from estate insurance company,
- e) Bank credits,
- f) others
- g) reduction of monetary savings : a) on accounts,
b) in cash.

The main kinds of monetary expenditures of individuals are:

- a) Purchase of goods and services from socialist enterprises.
- b) Taxes and other payments to the State budget.
- c) Payments to insurance company.
- d) Reimbursement of bank loans.
- e) Others.
- f) Insurance of monetary savings : a) on accounts
b) in cash.

The balance-sheet of monetary revenues and expenditures of the population, whose main positions are given above, is not addressed to any special institutions as a target or directive for fulfilment. It serves as an instrument of coordination of different targets, included in different and separate plans, but on the basis of this balance-sheet even very important changes of directives given to different institutions may be imposed. For example, if it occurs that the estimated purchasing power of the population is not in accordance with estimated supply of goods and services (at fixed prices) - some measures must be taken in order to

equilibrate both quantities. It does mean, that or the estimated revenues, or expenditures of the population have to be corrected, and not only in this balance-sheet, but also in enterprises financial plans, state budget, credit plan etc. The analysis of the market equilibrium and the financial measures serving to its maintaining are a special problem, which will be separately treated.

Wages are planned on the basis of planned amount of employment and average wages. Every enterprise and office gets from its upper organisation a directive, indicating the maximum loan fund, which dare not be exceeded without authorisation. The upper organisation, e.g.) trusts and ministries, dispose of some reserve loan fund, which may be used in order to raise the given limits in emergency cases. Besides, during the year when new opportunities arise, due to overfulfilment of production plans, additional loan fund may be admitted in order to raise the average wages above the formerly planned level, or in order to exceed the planned amount of employment (but only on condition of keeping the planned level of labour productivity, which means that over-planned employment must be in proportion to over-planned production). As a rule, enterprises producing consumption goods are automatically authorised to surpass their planned loan fund in proportion to the over-planned output, while enterprises producing investment goods and all non-productive organisations may surpass the planned loan fund only upon explicit authorisation. The rigid control over the loan funds is executed by the banks.

The pensions, social allowances, scholarships etc., being paid from budgetary funds, are planned, within the planning of State expenditures, on the basis of demographic estimations (pensions, family allowances), statistical data on illness cases and accidents, prescriptions regulating amounts of indemnities etc.

Revenues from the sale of agricultural and other products, provided by the individual formers and other private producers, are planned within the financial plans of commercial enterprises, buying these products from private suppliers. These revenues are planned on the basis of estimation of agricultural production (less self-consumption and increase of stocks in farms and less direct supplies of these products to the town-population) and fixed prices.

The indemnities for losses of estate, paid by State insurance office, are planned also on the basis of statistical data, by insurance companies.

Bank credits granted to the population and private producers, are of four different kinds : a) investment ~~and~~ short-term credits for private farmers b) investment and short-term credits for others branches of private production c) investment credits for private house construction d) consumption credits, including credits granted to commercial enterprises in order to cover their claims arising from sale by instalments. Each kind of these credits, playing a different role in economic activity, is separately planned within the credit plan.

Other monetary revenues, received by the population, are of small importance and must not be treated in a detailed way. This item of the balance-sheet includes for example revenues such as gains from the State lottery etc.

The purchase of goods and services by the population-though as the first item of the expenditures part of the balance-sheet, is planned at the end, after all others.

The payments to the State budget, imposed on the population and private producers, are composed mainly of such as the tax on wages and salaries , income tax and turn-over tax (concerning only private producers and dealers except farmers) and land tax. The tax on wages and salaries is a progressive one, with rates growing from 0,5 % up to 15% of earnings. Exemptions are granted to numerous families, war invalides etc. The turn-over tax received from private producers and dealers is taken at small, constant (regardless of the amount of turnover) rates from 1 up to 5%. Income tax is progressive, with rates growing from 5% up to 65% of net benefit . Small handicraft enterprises, employing no labour power, except the owner, his family members and up to 2 pupils - are exempt from normal turn-over and income taxes but they pay combined turnover-income tax expressed in absolute rates. These rates depend on the kind of profession, the number of population in the locality where the enterprise is situated etc. The land-tax is imposed on the basis of estimated (not realised) income of the

farm, this income being calculated according to standards fixed for 1 hectare land in different amounts, according to (a) economic area (the whole country is divided into three areas, according to the level of economic development), (b) economic zone where the farm is situated (there are five zones, distinguished for the purpose of land taxation: big towns, near to town zones, country zones distant country zones), (c) Kind of land (plough land, pastures and meadows, forests) and finally (d) the class of land (there are distinguished 6 classes of plough land and 5 classes of pastures and meadows, according to their fertility, all forests belonging to only one class). The relation between the lowest and the highest standard of income from 1 hectare land is about 1 : 40. The rates of land-tax are progressive, growing from 5 up to 36% of estimated income, but many exemptions and alleviations are granted in different cases. It must be underlined, that all income above the standard level is free of taxation, what has for purpose to incite private farmers to intensification of their production. In practice the standards of income, used for taxation, are rather far below realized income level from 1 hectare, so the real burden of the land tax is estimated on the level of the half only of its nominal rates.

The payments to the insurance company result^{*)} from the contracts concluded between this company and private firms and persons. There are many kinds of insurance contracts, some of them being obligatory (for example insurance against the risk of fire for private farmers). These payments are planned by the state insurance company on the basis of statistical forecasting.

The payments resulting from the reimbursement of bank loans, formerly granted to the private sector (and to the state and cooperative shops as reimbursement of claims emerging from the sale on instalments) are planned in the four formerly mentioned groups within the credit plan. In some cases a part of credit indebtedness of private farmers and persons may be reduced

*) Beside taxes and duties, the payments to the state budget include also fees for different services executed by State organs, as for example rents for flats in nationalized houses, fees for medical services (paid only by persons, not participating in social security organization, what is the case of private farmers) and so on.

without reimbursement, by using budgetary funds. It is one of the ways of promoting by the state the development of agriculture and housing construction.

The planning of increase of population's monetary saving-either on saving bank accounts or in cash-is based on statistical data and functions of propensity to saving are established for different groups of the population. These functions relate savings with the absolute monetary income's level (in real terms), with the relative increase within the planned period, with seasonary factors (influencing especially monetary expenditures) etc. The forecasting of the increase of monetary savings is one of the parts of credit planning.

All monetary revenues of the population less the increase of monetary savings, and such expenditures as payments to the state budget, to insurance company, reimbursement of bank loans, forms so-called population's purchase fund and are compared with estimated supply of goods and services from the socialist sector. The equalisation of monetary demand (expressed as purchase fund) and supply of good and services is a main purpose for which the balance-sheet of monetary revenues and expenditures of private sector is established. This problem, being of exceptional importance in the whole mechanism of socialist economy, will be elsewhere separately treated.

4. State budget.

The main sources of budgetary revenues are:

- a) Gross benefit of socialist enterprises, flowing into the budget as turnover tax from socialist enterprises, and a part of the net benefit of state enterprises and income tax from co-operative enterprises. Some additional budgetary revenues are taken from socialist enterprises as duties and fees, added to the cost of production (and thence not considered as a part of the gross benefit, though their economic nature is identical). The most important kind of these duties are the payments to social insurance, established on the level of 15% of the loan fund.

The budgetary revenues from socialist enterprises actually amount in Poland up to 80% of the total sum of budgetary revenues. The relative share of the turnover tax is of about 60%. From total gross benefit of socialist enterprises a little more than 10% left to their disposal, nearly 90% being interpreted by the State budget.

- a) The monetary revenues of the population. The tax on wages and salaries, local taxes and fees for services taken from the population bring about 12% of total budgetary revenues, amounting at the same time to 11 - 12% of total monetary revenues of the population. But the amount of budgetary allowances, paid directly to individual persons (pensions, rents, social allowances etc.) is surpassing largely the amount of budgetary revenues, taken from them.
- b) The monetary income of private producers and dealers. The turnover tax, the income tax, the land tax and other budgetary revenues, brought by the private sector, given 6% of total budgetary revenues. However, their share is declining as a result of consecutive socialisation of the national economy and changes in its structure.
- c) Other sources, as for example treasury loans (in part from domestic financial institutions, in part from abroad) etc. Their share in total budgetary revenues in Poland amounts in the average to about 2%.

The main direction of budgetary expenditure in Poland are:

- a) Expenditures on the development of the national economy. For this purpose is devoted in the average a little more than 50% of total resources. This part of budgetary expenditures involves mainly centralized investments in state enterprises, in infrastructure and in geological researches, then subsidies to deficitary enterprises and others.
- b) Expenditures on so-called social and cultural services i.e. on education of all degrees, on subsidies to cultural institutions (museums, theatres etc.) on science and research work, allowances granted to editors, expenditures on medical services, social insurance, pensions, rents etc. The average amount of these expenditures is of about 27% of total budgetary funds.

- c) Expenditures on administration, both central and local, on internal security, on law administration etc. - take on the average about 8% of total budgetary funds.
- d) Expenditures on national defense take on the average about 10% of budgetary funds.
- e) Other expenditures, including interests on public indebtment and its partial reimbursment, amount in the average to 5% of total expenditures.

As a rule, the budgetary revenues, both planned and realized, exceed budgetary expenditures. In budgetary plans the surplus is divided into two parts: one of them forming the reserve at the disposal of the government, the other being treated as undistributable and is devoted to increase treasury deposits at the National Bank.

According to the organization of State authorities and administration, the State budget is divided into two parts: the central budget and the local budgets. The central budget includes the means at the disposal of central authorities; about 75% of total budgetary resources, while the rest of them is included in the local budgets. The local budgets are constructed by a ladder-like method, the budgets of communities being included into districts budgets, and these, in their turn into the budgets of wojewodztwa (provinces). All including, the general State budget is voted by the parliament. The representative authorities of lower degrees ("national councils") dispose of some autonomy in detailed planning of expenditures limited by parliamentary act, and in voting over-planned expenditures based on over-planned revenues got during the period of implementation of their budgets. The relations between central and local budgets, the limitations of competences between them, the division of revenues and expenditures, are questions of a great importance, especially in connection with general tendencies to decentralisation of the whole system of planning and management.

The monetary side of State budget's implementation is left to the National Bank, which receives on budgetary accounts all budgetary revenues and performs all expenditures on orders given by authorised organs. The treasury neither disposes of its own network of cash-services, nor is authorised to issue treasury notes.

5. State insurance company.

Insurance is regarded as a means of recovering losses in material assets entailed by unexpected accidents. The insurance system covers the losses in an automatic way, and hence is considered as adoptable to all the assets of private sector and to circulating capital of the public sector, its capital equipment being exempted from the insurance system. The reason for this exemption is that the reconstruction of reduced economic capacities should not be decided automatically as the reconstruction of just the same plant on just the same place, because in many cases more efficient way of recovering damaged capacities is either the construction of a new plant elsewhere or supplementary investments in other existing plants. To the purpose of extra-planned investment expenditures, connected with reconstruction of damaged capital equipment, reserves are held within the state budget.

The participation in the insurance system is in some cases obligatory, as for example for private farmers in the insurance against fire risks. The payments to insurance fund are calculated on the basis of statistical data and the probability accounting. There is a very developed system of payment reductions in connection with measures taken by interested parties in diminishing dangers of risks (for example fire-proof constructions, vaccination of cattle-stocks against epidemics etc.)

The expenditures of the State Insurance Company include indemnities for occurred losses, administration costs and costs of preventive actions against risks. The surplus of payments above expenditures is divided into two equal parts, a part being paid to the state budget as its participation in the benefit, and the second part is added to the reserve fund of the company. The reserve fund is lent to the state budget as termless and interestless loan.

6. The system of Banking.

In all socialist countries the most important place in the banking system belongs to the state central bank. The main functions of the state central bank are:

a) the issue of bank-notes and change for circulation b) granting short-term and investment credits for state, collective and private enterprises in industry, commerce, and other branches of the national economy, with the exception of construction and agriculture¹⁾ c) granting re-financial credits to special banks d) execution of budgetary and treasury operations e) execution and supervision of foreign-exchange operations.

The special banks are: The Investment Bank (in all socialist countries with exception of Czechoslovakia), the Agricultural Bank (existing in Poland, Hungary and German Democratic Republic) and the Bank for the Foreign Trade (in all countries with exception of Czechoslovakia).

The Investment Bank deals with the finance of centralised investments, i.e. the execution and control of that part of the state budget which contains investment expenditures. Besides, as the physical implementation of the investment program is executed by construction enterprises, the Investment Bank grants credits to these enterprises and executes the whole bank-control over them.

The Agriculture Bank grants short-term and investment credits to the private farmers, as well as to the state and cooperative farms. In Poland, this Bank is collaborating with a network of saving and credit country cooperatives, which distribute credits granted by this Bank among private farmers and grant also own credits on the basis of accumulated savings.

The Investment Bank and the Agriculture Bank, receive re-financial credits from the central bank (in Poland - the National Bank of Poland) when these credits are needed for fulfilment of their credit plans.

The Bank for the Foreign Trade executes mainly the settlements bound with the foreign trade in correspondance with the foreign banks. It grants also credits to export and import companies using - if necessary - refinancial credits from the Central Bank. Exchange operations are performed

1) In most countries. In some cases, however, (for ex. in Czechoslovakia) the State Central Bank is fully monopolistic, and hence is granting credits to all branches of the national economy.

either by offices of the Central Bank, and Bank for Foreign Trade or by specially authorised institutions (hotels, sea-going ships, travel offices etc.).

A special function in the banking system is performed by ~~saving-banks~~. Their main target is to receive deposits on saving-book and accounts and perform cheque operations for private persons and firms. In some countries (for ex. in Poland and Hungary) they grant also consumption credits.

In socialist countries the commercial credit between enterprises is forbidden. Enterprises have no right to issue or to draw bills of exchange, or to receive from other enterprise advances on future supplies. All credit operations and settlements within the socialist sector have to be concentrated in banks in order to make possible planned distribution of financial means and bank control over their use.

The main kinds of short-term credits, granted to state and cooperative enterprises are:

- a) Credit on standard stocks. It is granted in the cases when the increase of standard stocks cannot be covered by the increase of enterprise's own circulating fund as a result of shortage of the development fund. This credit, granted for the term of one year or more, has to be reimbursed from the development fund either of the running or of the next year. In some cases the bank is permanently participating in standard stocks of an enterprise in percentage share, established by the Ministry of Finance (for example in retail commerce enterprises the share of permanent bank credit in standard stocks is established on the level of 70% of their value in retail prices). For this purpose, is adopted also the credit for standard stocks, reimbursable only in cases when the value of real stocks kept by the enterprise falls below the standard.
- b) Credit on over-standard stocks. The over-standard stocks are stored for seasonal and special (for example as reserve stocks) needs, and also in connection with over-fulfilment of production plans, the level of standard stocks being calculated strictly

on the basis of planned output. The credit on over-standard stocks may be granted up to their value, reduced by legal (i.e. within the legal period of payments) indebtedness towards suppliers, and if the bank office decides so - by the value of stocks not needed for enterprise's economic activity. The term of reimbursement of this kind of bank credit is established in connection with the term of storage of over-standard stocks.

- c) credit on monetary settlements. The receivers of goods are obliged to pay bills in a term of 5 up to 15 days after delivery. The claims, emerging from delivered and not yet paid goods are the most important subject of credits on settlements. The claims emerging from the sale on instalments are also covered by the credits on settlements. The claims towards buyers have permanent character and thence the credit on monetary settlements is not reimbursable in practice; only its level is submitted to periodical regulations, in connection with changes in average daily turnover and conditions of payment.
- d) credit on urgent payments. This credit is granted in emergency cases, on a term up to 10 days, when an enterprise - having to cover urgent payments - disposes temporarily of no monetary means on its accounts and has no grounds to apply for another kind of short-term credit.

The techniques of granting credits, used in socialist countries, are different. In most cases separate credit accounts are kept for each kind of short-term credit. In Poland's practice, all short-term credits are granted together as a limit of the overdraft on the current account. The calculation of the credit limit is based on enterprise's applying form, which includes following datas :

Simplified example

	(real)	(planned)	
I. <u>Credit on stocks.</u>	on 31. III ...	on 30. VI ...	
1. Stocks value	10.000	12.000	
2. Stocks of bad quality, not needed etc.	500	-	
3. Standard stocks	8.000	9.000	
4. Over standard stocks	2.000	3.000	
5. Planned amount of own circulating fund and permanent indebtedness	8.000	8.500	
6. Credit on standard stocks (3 - 5)	-	500	term applied 30. IX
7. Overplanned own circulating fund	-	-	
8. Legal indebtedness (less planned permanent level)	300	400	
9. Credit on overstandard stocks (4 - 2 - 7 - 8)	1.200	2.600	31. XII
II. <u>Credits on settlements.</u>	on 31. IV	on 30. VI	
10. Daily average turnover (less turnover tax)	500	500	
11. Average period of settlements (days)	10	10	
12. Amount of claims from sale	5.000	5.500	
13. Credit on settlements	5.000	5.500	
III. <u>Other short-term credits.</u>			
14.			
15.			
IV. 16. General amount of short-term credits (6+9+13+14)	6.200	8.600	
17. Increase of the credit-limit as compared to the previous quarter of the year		+2.600	500 30. IX 2100 31 XII.

The application form has to be submitted to the bank office together with a copy of the balance-sheet, and the bank is authorised to request additional documentation from the enterprise if it appears necessary in order to clear the enterprise's request.

The bank may reject the enterprise's application for credits, especially in cases when the enterprise does not gain the planned amount of profit, and therefore does not dispose of planned amount of own circulating fund. In such cases, enterprises are obliged to apply to the trust for an allowance from its reserve fund in order to recover the lacking circulating fund, or may apply for the trust's guarantee for their indebtedness towards the bank. The bank may also reduce the amount of credits granted below the level applied by enterprises, if it appears justified by the results of an analysis of enterprise's targets and needs. Instead of diminishing the amount of requested credits - when the bank's control detects the existence of not needed over-standard stocks in an enterprise - higher rate of interests may be imposed as a means of bank's sanction. Normal rate of interest on bank short-term credits is established in Poland at 4% p.a. The banks are authorised to increase this rate up to 10% p.a. The rate of interest on indebtedness resulting from not reimbursed in due term credits is established at 12% p.a.

Investment credits for socialist enterprises may be granted either on planned investment expenditures, or on over-planned ones. The implementation of investment plan of an enterprise may start only upon bank's approval. (Even in the cases when no investment credit is requested). The banks approve investment plans on the basis of an analysis of economic efficiency of planned expenditures, and - if necessary - grant credits up to the level of the difference between planned expenditures and planned accumulation of the investment fund. These credits are granted at the beginning of each year. During the year supplementary investment credits may be granted on investments of extremely high economic effectivity which are not included in the annual plans. The term of reimbursment of investment credits on planned investments may be fixed up to 8 years (for collective enterprises up to 15 years) and on non-planned ones up to 3 years. The rate of interest on investment credits is fixed at 3% p.a.

The amount of investment credits granted to the socialist enterprises as well as the amount of all kinds of credits granted to the private sector, are limited by the credit plan. The short-term credits for the socialist enterprises may be granted by bank offices without limitation.

7. The financial system of the foreign trade.

Export and import operations are performed by specialized foreign trade companies. Their settlements with domestic customers (suppliers of exported and receives of imported goods and services) are based on internal prices, sometimes a little risen above normal level, when - especially by exported goods - exceptional performance is required. The settlements between foreign-trade companies and their outside customers (buyers of exported and sellers of imported goods and services) are based on current world-market prices, with the exception of the trade within European socialist countries, members of the Economical Aid Council (EAC) where more stable agreement prices (established as average on the world market during a longer period) are adopted.

World market prices, expressed in Polish currency at the normal exchange rate (24 Polish zlotys = 1\$ USA) very often differ from home-market prices. As a result, a special system of equalisation of monetary revenues and expenditures of foreign trade companies is required. It is organised on the so-called "budgetary differences" system. World market prices, expressed in Polish currency at basic¹⁾ exchange rate and increased by the margin for foreign trade companies, are compared with home market prices. The positive differences are paid to the state budget, the negative ones are paid by the budget to the foreign trade companies. In most numerous cases, the negative budgetary differences are connected with exported goods, while positive with imported ones, both mainly in trade with hard-currencies area.

The balance-sheet of foreign claims and payments is established first in transferable zlotys (it means in foreign currencies, all revaluated into Polish zlotys at the basis exchange rate), and then in current zlotys

1) It is adopted to all transactions with foreign currencies, tourism included, but at the sale of foreign currencies to tourism purposes, Polish citizens have to pay a duty to "Tourism fund", which amounts up to 15% of the exchange rate.

i.e. after including "budgetary differences". The balance-sheet established in transferable zlotys is divided into parts, each one corresponding to special foreign settlements system (The multilateral clearing within the EAC, the bilateral clearing with other countries, the settlements in hard currencies). Every part of the balance-sheet is further divided into three chapters : Turnover of goods and services, other settlements, and credit operations. The chapter of credit operations is balancing surpluses and gaps, occurring in the two preceding chapters and indicates either the increase of claims, or of indebtments towards foreign countries, within a given period of time.

In the balance-sheet, illustrating the monetary activity of foreign trade companies within the home market, no particularities about different settlement methods are given, but "budgetary differences" are included, in order to establish financial bounds between the foreign trade and others institutions of the financial system.

II. Monetary flows, uniting different economic units in a socialist economy.

In the description of the financial system of the socialist economy (on Poland's example) many lines, uniting its different parts have been mentioned. In order to get a more transparent picture of the financial mechanism of a socialist state, we must use an input-output table of the Poland's national budget. This table though elaborated on the basis of actual data and documentation, was specially prepared for illustrative purposes, mainly by simplifications and consolidation of different accounts.

In this table, six sectors are distinguished as follows:

- 1) Productive enterprises (PE) i.e., socialist (state and cooperative) enterprises dealing in all branches production recognized as "material" ones (agriculture, industry, transportation, construction etc.) Private farming is not included here.
- 2) Foreign-trade enterprises (FT). The table does not include their settlements with foreign customers.

- 3) Home trade enterprises (HT). This sector includes figures relating to the wholesale commerce and to the retail commerce as well.
- 4) Population. (P) here are included figures relating not only to households of individual consumers, but also to private farmers and other kinds of private producer and dealers.
- 5) State budget (SB). In this sector are included consolidated operations of all parts of the State budget (it means of the central budget and of local budgets as well). The operations within the budgetary system have been excluded.
- 6) Banking (B). In this sector, against the general rule, are included figures showing not gross flows, but only the changes of the indebtedness towards the bank and deposits held on bank accounts. This method was adopted in order to show the final results of banking activity. I.e. the increase of the monetary means in circulation and the share of bank credits in financing the development of the national economy.

Monetary revenues of every sector are expressed in horizontal lines, monetary expenditures in vertical ones (Attention, please, because in many countries an inverse method is adopted in input-output tables of national budgets.) The table of national budget, serving here as a specimen showing monetary flows, has been established for the year 1957, in billions (1.000.000.000) Polish zlotys, billion Polish zlotys being equivalent to 41.666.667 \$ or to 18.185.000 Egyptian pounds.

THE BALANCE-SHEET-OF POLISH ECONOMY

(1957, in billion zlotys)

Revenue from Expenditures to	PE	FT	HT	P	SB	C	Total
P.E.							
Sale	307,9	28,9	176,9	-	15,7	-	529,4
Allowances					63,8		63,8
Credit						9,0	9,0
							602,2
F.T.							
Sale	38,6		1,1				39,7
Allowances					25,5		25,5
							65,2
H.T.							
Sale	45,7		135,0		14,0		365,0
Allowances					1,4		1,4
Credit					6,4		6,4
							372,8
P.							
Wages & Salaries	100,1	1,0	8,8	18,8	34,2		162,9
Allowances					18,5		18,5
Sale of products			41,0				41,0
Credit					6,2		6,2
							228,6
S.B.							
Sale of services				21,7			21,7
Taxes and others	99,4	35,7	9,7	12,2			157,0
							178,7
C.							
Money on accounts	10,5	-0,4	0,3	3,4	5,0		19,4
Cash				2,2			2,2
							21,6
TOTAL	602,2	65,2	372,8	228,6	178,7	81,6	1469,1

This balance-sheet, including only monetary flows, does not include therefore parts of the national income, consumed directly by the private