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The Banking System of the U.S.S.R. 7 pages

Paul Gekker

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The Banking System of the U.S.S.R.*

Paul Gekker

Banking in a Soviet-type planned economy

The Soviet Union has a money using economy. With some notable exceptions, most financial devices familiar to bankers elsewhere--banks and credit, deposits, clearings, payments and collections--are also found there. Yet the use of money is severely circumscribed, largely because of the absence of arrangements under which private persons can engage in profit-making activities, but also because of technical limitations on the uses of money. The first of these limitations is inherent in a collectivist system of the "pure" type. The technical limitations are theoretically not essential to the workings of a socialist system, but they have long been a feature of Soviet money arrangements.

Limitations on the uses of money mark one area of difference between banking systems in socialist and in free market economies. A more important difference stems from the role Soviet banks play in implementing economic decisions which are determined, in all important respects, by political authorities at the highest level. This applies specifically to the State Bank, which is the heart of the system. The two other Soviet banks (the Investment Bank and the Bank for Foreign Trade) are rather specialized institutions.

The position of the State Bank reflects two features of the Soviet system. One relates to the State Bank's role in controlling the implementation of planned tasks. The other has to do with the position of the State Bank within the financial apparatus of the Soviet Government.

As part of the planned system, the State Bank participates in formulating financial plans. The Bank also implements these plans, which comprise a cash plan, a plan for credit, and a plan projecting overall balance between total incomes and expenditures of the population. On another level, the plans established for producing units contain financial criteria of successful performance such as targets for cost reductions, planned profits, and others. These financial plans may be thought of as the counterparts, in money terms, of plans governing various economic activities in real terms. The most important criterion of successful plan fulfillment is the achievement of real targets. Briefly, the priority accorded to real targets means that financial plans are to some extent subsidiary.

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*This paper has been prepared for the Journal of the Institute of Bankers of the United Kingdom. I am indebted to many associates--too numerous to single out by name--among fellow delegates to the 15th International Banking School held in Moscow (July 1962), for the opportunity of discussing with them some of the ideas developed briefly in this paper. I also welcome the opportunity of acknowledging the assistance of our hosts--officials of the State Bank of the USSR--and of expressing appreciation for the personal and professional courtesies extended to me during the sessions of the Banking School. This article reflects the author's personal opinions and must not be taken to represent the views of the Board of Governors of the Federal Reserve System.

Secondly, the Soviet banking and credit system plays only a limited role in providing the financial resources for the fulfillment of the important economic plans. In effect, the State budget is the chief financial instrument of the Soviet Government. The immense revenues collected, chiefly from indirect taxes, with individual income taxes and other items accounting for minor shares, provide the means of finance. The only slightly less imposing expenditure total (the Soviet budget is normally in surplus) covers the Government's important role in financing the economy and in supporting a wide range of educational, cultural and welfare activities. Over half the national income is channeled through the budget, which is therefore a powerful mechansim for the mobilization of financial resources, as well as for the redistribution of income. It is also the budget, rather than the banking system, which is the most important instrument for the maintenance of overall financial balance.

Basically, however, the priority of physical criteria of successful plan performance means that the State Bank's most important function is to exercise control over the activities of its clients in conformity, if possible, with the established plans. The Bank possesses some discretionary powers and an imposing array of control functions, but in the nature of the system its power to exercise independent action in the monetary field is distinctly limited.

The State and the Investment Banks

In recent years, the organizational structure of the Soviet banking system has changed somewhat, as the result of a major reorganization in mid-1959, and subsequent modifications. These changes have greatly enhanced the State Bank's powers and responsibilities. In addition, the State Bank has become more important as a consequence of institutional changes in the post-Stalin period. This is especially the case in agriculture, where a significant degree of monetization has increased the State Bank's involvement in this important economic sector.

The State Bank of the USSR--The State Bank (Gosbank)--a single, giant government bank--is a mixed institution. It exercises some typical central banking functions: the State Bank possesses the note issue monopoly, regulates the currency issue, acts as custodian of the country's monetary reserves, performs fiscal agency functions on behalf of the USSR Ministry of Finance, and organizes and manages bank clearings for the entire economy. The State Bank also performs ordinary banking functions, though these differ from banking practices elsewhere. As the source of virtually all short-term credit, the State Bank is a combined central and commercial banking institution, organized along highly centralized lines under the direction of the Bank's Administration (Pravleniya) at its Head Office in Moscow.

The State Bank is also a mixed institution in a functional sense. In addition to its traditional short-term lending activities, the Bank acquired two types of long-term functions in 1959. The State Bank now extends intermediate and long-term loans to the collective farms (it acquired authority to make intermediate-term industrial modernization loans in 1954). In 1959, the State Bank also acquired the important function of disbursing nonrepayable grants from the State budget for capital investment in State-owned agriculture and, in part, in the communal and housing sectors.

Two other organizational changes affected the State Bank. At the beginning of 1961, the Bank for Foreign Trade (Vneshtorgbank), which had for many years operated as a special department of the State Bank, conducting a limited range of foreign currency operations, acquired responsibility for all foreign trade financing activities. However, despite its greater operational independence, the Bank for Foreign Trade apparently remains under the general policy supervision of the State Bank.

The second change transferred the extensive system of savings banks from the USSR Ministry of Finance to the State Bank at the beginning of this year. In a recent article, Mr. Korovushkin, Chairman of the Board of Directors of the State Bank, noted that the change amounts to a further centralization of the banking network in the hands of the State Bank.

As a result of these changes, the State Bank system now consists of 164 main offices (in each capital of the 15 constituent republics of the USSR, plus 149 offices in other important administrative centers) almost 4,000 branches, more than 3,100 payment and collection points and agencies and, as from January 1, 1963, over 70,000 savings banks.

Finally, changes in the formal status of the State Bank are of some interest. The State Bank was an independent body for some years before the war, but was subordinated to the Ministry of Finance in 1946. Since April 1954, however, the State Bank has been independent again and, with representation on the USSR Council of Ministers, may be said to be formally co-equal with the Ministry. Moreover, with the savings bank system now under State Bank jurisdiction, and with the earlier transfer of the Investment Bank from the structure of the Ministry of Finance to an independent position, the Ministry seems to have lost all responsibility for banking functions. It is not easy to judge the importance of this development. Experience may have shown that the Ministry of Finance, which is concerned primarily with tax collection and other purely fiscal duties, was not best equipped to supervise the control functions of banking institutions under its jurisdiction.

The Investment Bank-- The All-Union Bank for the Financing of Capital Investment--the Investment Bank (Stroibank) for short--dates in its present form from the 1959 reorganization, when three separate long-term investment institutions--the Industrial Bank (Prombank), the Agricultural Bank (Selkhozbank) and the Central Communal Bank (Tsekombank)--were liquidated, and their functions divided between the new Investment Bank and the State Bank. A fourth long-term institution, the Trade Bank (Torgbank), was liquidated in 1957.

Like its predecessor institutions, the Investment Bank is primarily an agency which disburses and controls the utilization of nonrepayable budget grants which comprise the major share (over two-thirds) of investment "financing" in the Soviet economy. The Investment Bank performs this function for all State-owned sectors of the economy except agriculture--a role which the State Bank took over from the liquidated Agricultural Bank. The Investment Bank is thus responsible for all budget financing in the field of industry, domestic trade, transport and communications, and State-owned housing construction. Long-term lending for individual housing construction--which has been severely restricted in the past two years--is a function it shares with the State Bank. In general, the State Bank finances cooperative housing, and individual home construction in rural areas, and the Investment Bank takes care of all other housing finance.

As the sole exception to the State Bank's monopoly of short-term lending operations, the Investment Bank extends short-term loans to construction enterprises engaged on projects for which it handles budget investment grants.

In mid-1960, the Investment Bank had 468 separate offices and, in addition, representatives in 444 State Bank offices where no Investment Bank installation existed. In the past the State Bank always conducted a sizeable share of the financing and lending activities of the older long-term institutions, and it continues this work at the present time on behalf of the Investment Bank.

The formal status of the Investment Bank is currently in doubt. Originally it was, like the liquidated long-term banks, under the Ministry of Finance. It was removed from the Ministry's jurisdiction in December 1961 and, like the State Bank, given representation on the USSR Council of Ministers. It recently lost this position--in December 1962--but does not appear to have reverted to its previous place under the Finance Ministry. Possibly, its uncertain status is connected with the distinctly unsatisfactory record of the past few years in implementing investment plans in many sectors of the economy; and, at the recent plenum of the Communist Party Central Committee (November 1962) the Investment Bank was severely criticized for serious shortcomings in the performance of its duties.

The State Bank's short-term lending operations

In what has come to be called the "command economy," organizational questions are obviously of the greatest importance, but they are of interest chiefly to the specialist. At the same time, the ordinary operations of the State Bank have been treated in any number of excellent accounts, and the main features are fairly well understood.* It might be useful to relate this familiar material to the State Bank's position under the planned system, concentrating solely on the State Bank's important short-term lending activities. A number of interesting and important topics, such as questions pertaining to long-term finance, or the problem of inflation in the Soviet Union, must necessarily be left aside.

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*Most standard works on the Soviet economy deal adequately with the role and functions of Soviet banks. It is hoped that the present article will serve to bring the organizational and structural changes up to date. In due course, moreover, we should have at our disposal the printed version of the lectures on the Soviet banking system delivered at the 15th International Banking Summer School.

Limitations on the use of money, and the predominance of the budget as an instrument of Soviet financial policy, suggest that the State Bank's function is basically a passive one. The State Bank does not, in fact, conduct monetary policy in the usual sense--or even credit policy, except within relatively narrow limits--but what we may call a form of monetary administration, or monetary management.

This monetary management is conducted within the framework of a strict separation between cash and non-cash transactions in the economy. Hand to hand currency is of course used for almost all personal transactions; but all transactions among government organizations and producing enterprises are, with the exception of small amounts, effected by means of offsetting entries on the books of the State Bank.

As regards the cash circulation, the State Bank concentrates on recovering as promptly as possible the maximum amount of cash receipts, chiefly from retail trade outlets. In accordance with strict requirements, the Bank also limits the amounts of till money held by any establishments serving the public. The authorities are also interested in channeling as much as possible of the idle cash circulation into such forms as savings deposits and voluntary purchases of insurance, primarily in the interests of maintaining domestic monetary stability.

Control over noncash transactions is accomplished by concentrating all credit in the hands of the State Bank system. Soviet enterprises are forbidden to extend credit to one another. There is, in other words, no financing on open book account, no accounts receivables financing outside of the State Bank, or anything of that sort.

Almost all bank credit is planned to accord with the needs of producing enterprises run on a self-supporting basis. Provided the enterprise is efficiently operated, it will receive short-term bank loans, in accordance with credit plans (but with some allowance for unforeseen needs) to meet working capital requirements, to finance the movement of goods, to meet seasonal requirements, and the like. All bank loans are direct, for specific amounts and purposes, and are repayable, with interest. With the exception of a penalty interest rate on overdue loans, there is no discretionary authority exercised with respect to the application of loan interest rates. The interest rate is primarily an administrative charge.

The State Bank is supposed to ensure that the terms and purposes for which loans are granted are in strict conformity with legitimate purposes. The State Bank has some discretionary powers to limit or deny credit facilities to enterprises which violate established financial standards, and to accord favorable financial treatment to enterprises which perform satisfactorily.

The State Bank exercises its supervisory and control functions chiefly by administering what is known as "control by the ruble." This requires constant supervision to limit the liquidity of the individual enterprise to the greatest possible degree, to deny the enterprise manager any financial elbow room. This involves a formidable amount of detail. It embraces supervision of the proper division between enterprise operations financed from internal resources and those financed by bank credit; and it requires supervision to ensure the timely deposit, to appropriate accounts, of the enterprise's tax liabilities, other payments into the budget, and its depreciation reserves. Most importantly, control must ensure not only that cash disbursements and payments for the firm's accounts are consistent with the purposes set forth in the plan, but that funds designated for specific purposes are not employed to finance something else.

Banking in a system of centralized controls

Much of what we can say regarding the workings of the planned system is not new. But our grasp of the essentials has undoubtedly been sharpened by the improvement in recent years in the intellectual level--and the candor--of discussions in the Soviet economic press and periodical literature.

We know that the Soviet economy is capable of impressive accomplishments, but also that it works at great strain, in a continual struggle to accomplish ambitious economic plans. The economy therefore works with little slack, and is beset by shortages, disturbances to the system of supply and distribution, and numerous other imperfections.

The key person in this system, the individual enterprise manager, works in an atmosphere of considerable stress. He is under constant pressure from above to accomplish all sorts of assigned tasks, and to accomplish them on time. At the working level, he struggles with the shortages, the administrative machinery, and the controls. Frequently enough, he must resort to stratagems of various sorts in order to secure needed supplies, in order to obtain a certain margin of safety against the unforeseen. Despite the planning, despite the rigid controls, many "efficient" managers hoard labor, materials or equipment, and try in other ways to guarantee meeting the most important output goals. In the process, financial regulations are violated, for example, by using bank credit for unplanned or undesired uses.

The evidence suggests that, although the State Bank and the financial authorities continually thunder against these much-publicized violations, they may be tacitly tolerated just so long as the manager fulfills the real plan. Undoubtedly, the State Bank could eliminate most violations by severely limiting credit availabilities, but the real limitations to its powers here is the disruption it might cause to some essential output. Even the enterprise manager often has powerful allies to intercede on his behalf with the argument that disciplinary financial action will hobble important productive activities. Soviet financial writers have sometimes complained that their role is reduced to one of simply signalling financial irregularities to higher authorities, but with little assurance that corrective action would be taken.

The last decade has witnessed a serious effort to improve the operating efficiency of the Soviet system. The process of intermittent organizational change, which one may describe loosely as an unequal tug of war between the need for some decentralization and the compulsion to retain control in central hands, has also involved changes in Soviet banking. However, despite some devolution of decision-making powers, further centralization (or re-centralization) is now the dominant trend.

So far the authorities have reacted to problems accompanying the growing maturity of the economy, and the increasing complexity of choice, by seeking to perfect the systems of detailed control. Notions of substituting general economic instruments for control methods, or of placing greater reliance on market forces, have not made much headway. On reflection, it is hardly to be wondered that those primarily responsible for the development of the present planned system-whose entire training and experience reflects heavy emphasis on the technological and engineering aspects of the problems of economic choice--should be basically antipathetic to alternatives which appear to threaten an unwonted dilution of control powers, or that they should react instinctively against the prospect of any "atomism" or "chaos" in the economic sphere. Understandably, this point of view is shared by many Soviet financial officials.

At this writing, then, the extent to which recent further centralization of banking responsibilities represents a qualitative enhancement of the State Bank's powers in practice is uncertain, or at least debatable. The Soviet banking system was given its present form in the 1930's, and recent organizational changes cannot be said to have altered the essentials. Given the nature of the system in which it operates, we may suppose that the State Bank performs its task with fair efficiency and success, all things considered, and that the imperfections written about cannot be charged wholly to the Bank's position and operations. On the personal plane, those of us who have had an opportunity of meeting our Soviet banking counterparts little doubt their professional competence to do a job which differs so fundamentally from our own.