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SPECIFICS OF OPERATIONAL FUNDING OF ENTERPRISES UNDER CENTRALLY PLANNED ECONOMY - THEORY AND PRAXIS IN CZECHOSLOVAKIA BEFORE 1989

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Abstract:

This paper deals with the system of operational funding of enterprises in a centrally planned economy. The analysis focuses on the case of Czechoslovak Socialist Republic before 1989. A tool analyzed in the paper – credits for constantly revolving working capital – had played the main role in the planned Czechoslovak economic system. These credits for constantly revolving working capital can be described as specific frameworks for loans based on forecasts and plans of volume of production made by Czechoslovak state institutions. The system had created inefficiencies in the economy and its heritage seriously influenced processes in the period of transformation after 1989, as the paper concludes.

Keywords:

central planning, socialism, banking, corporate finance, operational funding, credits for constantly revolving stocks, inefficiencies

JEL Classification: E50, B24

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1. Introduction

The financial system was completely different in the planned Czechoslovak economy (before 1989) from what it is in a market economy. The former financial system generated special processes. An environment of centrally planned economy combined with non-democratic political system created specific features of basic economic, social and political activities. A challenge of new, post-communist democracies was to suppress these malignant heritages of communism, nevertheless many of them are still observable in behavioral patterns of individuals and institutions today. At the beginning of the transformation process changes in the financial system seemed to be easy, today it is evident that remedies have been painful and still not completed. Not only specific features of the financial system but above all a pressure on quantitative growth of the centrally planned economy are crucial when analyzing the transformation period.

The text deals with a low-quality portfolio of loans used for operational funding of enterprises in a planned economy. The major part of the portfolio was called 'credits to the constantly revolving stock', when stock de facto means working capital here. Its role was to finance working capital in enterprises, i.e. to finance permanently needed inventories and other current assets for planned level of production. Why is this topic so important? Without exaggeration, the topic can be marked as an economic and political phenomenon which completely suppressed market principles in banking sector as well as in the economy as a whole. Inefficiencies were mainly based on a logic argument for Economic Calculation Problem which economists pointed out firstly at the beginning of the 20th century; see Mises (2010) and Mises (1951) or Hayek (2009). However, the idea of centralization and planning had been criticized even earlier, for example in texts L. Trotsky. The argument of Economic Calculation Problem is still used against the concept of centrally planned economies, especially because it has not been satisfactorily refuted yet, as Boettke (2000) concludes. We can find several works analyzing soft budget constraints during transformation of centrally planned economies (e.g. Horčicová (1997), Kornai (1992) and Nove (1986, 2005, 2011a, 2011b)).

Nevertheless, specific factors of the system of operational funding of socialist enterprises are relatively poorly explained, so there are many inaccuracies and errors continuously repeated in explanations and interpretations of the system. This paper's aim is to reduce many inaccuracies and errors continuously repeated in explanations and interpretations of changes in financial system under transformation. The text describes determinants of operational funding of enterprises in a centrally planned economy through a system of constantly revolving working capital and its crediting based on legislation, and offers an economic analysis of inefficiencies that the system based on permanent, legislatively guaranteed lending to enterprises produced.

2. Main characteristics of planned economies

A basic tool of the former approach to economic policy is a plan, strongly related to the state budget. Budget breakdown to lower levels enabled state authorities to manage planning economic activities and transactions in very precise areas, i.e. in every single institution. Needs of individual institutions (operational funding related to material stocks and inventories, labor, etc.) accounted as signal for banking sector responsible for distribution of financial sources. To understand the context, firstly it is necessary to define three institutional pillars of the system: State budget, Central plan and Banking sector.

The State budget in socialist economies provided three basic functions – distribution, control and stimulation (Kyzlink 1989b). Since revealing that direct budget financing by lending from the central banking authority can create uncontrollable inflationary spiral, there was a political pressure to adjust public finance system and its funding, although Kyzlink (1989b, p. 160) states: *"The socialist state budget could end in deficit. Then, this deficit can be covered using available sources of credit to finance the needs of the state budget."*

Due to the fact centrally planned economies had only limited approach to international market with financial liquidity or securities as well as to competitive markets with international goods to trade with, balanced Budget or Budget surplus was a better solution for governments in comparison with continuous debt financing, since otherwise it would have to reduce spending (i.e. to change planned indicators) or to increase revenue (i.e. to change planned indicators or to increase tax burden) or draw credit resources from subjects willing to provided them¹. That is why the obligation of balanced Budget was legitimized. In Czechoslovakia, the fiscal reform from 1953 defined the structure of the planned Budget. In 1968, the National Assembly of Czechoslovakia passed a draft of Act No. 196/1968 which dramatically increased deductions from profits of enterprises and wages of employees to the Budget. The system was then modified with the Act No. 82/1971, governing contributions to the Budget and planned security system. This new disposition can be described as a system of indirect inflationary financing of government spending. Kyzlink (1989a, p. 33) quotes: *"The system takes resources from one group of institutions and provides resources for the other ones. It creates desirable relationships that have positive effects on fulfillment of planned quantitative and qualitative indicators and strengthen the effectiveness of the plan. By centralizing available financial resources and allocation of money to those organizations that need them for meeting tasks planned, state budget fulfills very important role of a tool that control all flows of financial resources between socialist organizations."*

The second pillar of the system was the Central plan (the Plan). In 1965, The Central Committee of the Communist Party formed a requirement for improving the system of planning, with a strong priority to set a key role of the Plan in the economy. In 1969, The Committee approved these stabilization measures: a restoration of full planning process according to the Act on the national economic planning from 1970. The State Planning Commission was authorized to manage this process. It is not surprising that this effort to plan economic interactions between supply and demand sides of the market that are normally based on spontaneous decision-making process, led to irrationalities and inefficiencies, such as that certain goods were abundant, while other required goods were scarce. The substance of this pillar was a consistency between two most important operational financial plans - the State budget and Credit plan (a.k.a. Loan plan). The Credit plan was a sovereign document from 1950 to 1970, starting from 1971 it was a part of the Monetary plan. Through this tool governments took decisions about the volume of resources reallocated through subsidies and bank loans between sectors, industries, companies and institutions.

The third pillar of the system was the Banking sector. In 1948, a number of commercial banks providing operating loans in the Czechoslovakia decreased to three institutions (Živnostenská banka, Legiobanka and Moravská banka). In the same year all credit activities merged into one institution – Živnostenská banka. On 1st of April, 1950 a monobank named the State Bank of Czechoslovakia (SBCS) was established by the

¹ With respect to the Iron Curtain limitations, of course.

Act No. 31/1950 (Kohout 1975), the law was effective from 1st of July, 1950. The SBCS was a classic monobank with a network of branches located on whole area of the state. Based on the Credit plan, the SBCS provided operating credits and loans to all institutions in the economy and also made payment clearing. Another institution Investiční banka (Investment bank) was responsible for financing investment projects, Živnostenská banka basically dealt with payments and foreign exchange settlements between domestic institutions and subjects in foreign countries. Živnostenská banka stopped operating in 1965, when Czechoslovak Trade bank was established for these purposes.

Operational funding was regulated by (see chapter 2 and 3) a special Law from 1970 that ensured the SBCS had a 100% influence and complete control of the whole financial system. It enabled to regulate financial activities and made them in full accordance with the State budget and the Central plan.

Let's focus on it more deeply: Since 1950, credit transactions within the economy were determined by the Credit plan, a part of the Central plan. Since 1970, as mentioned above, the obligation to prepare the Monetary plan for whole economy of Czechoslovakia had been put into legislation (Beneš 1970). This Monetary plan consisted in Credit plan, Cash plan (sometimes called as Treasury) and Foreign currency plan. The role of the Monetary plan was very presumptuous – to plan and control all financial transactions and cash-flow, both within the state and with trade partners abroad. The Monetary plan was a crucial tool for providing short-term and long-term credits and loans to state institutions and enterprises, for collecting savings from population, for storage and reallocation of unused resources. It was literally a balance of all available financial resources of the economy and their allocation among agents in the economy.

"Monetary plan is an essential tool for controlling operation of state banks and other financial institutions in Czechoslovakia. It builds on credit planning and its methods, it summarizes the Credit plan of the State Bank of Czechoslovakia and other financial institutions, treasury (note: Cash plan) and Foreign currency plan. That highlights the State Bank's role as a monetary institution and at the same time emphasizes the role of government taking a complete control on Czechoslovak banking system in this area." (Beneš 1970, p. 722)

3. Operational funding of socialist enterprises

The Plan built a main barrier to enterprises' managements because it limited abilities and competences of human factor in decision-making. Companies in centrally planned economy did not seek for profit, but tried to meet or overcome levels of production set up by the Plan (Kněz 1972). Both types of resources - own as well as liabilities - were actually owned by the state, and all official economic activities were defined by the Central plan. The Central plan limited the decision-making of individual managers. Discrepancy between leading role of the government (state) on one hand and personal abilities of people in enterprises' managements on the other one rose. *"And that would be a mistake."* (Kyzlink 1989a)

In 1965 two hundred companies within the economy implemented 'new elements of central planning'. All operational needs (marked as 'stocks', basically 'working capital', i.e. a part of current assets) of these enterprises were financed through special credit system managed by the SBCS. (Báča and Třetina 1981)

In 1967 the economy implemented a new monetary system and credit system operated by the state, characterized by massive loans providing operational working capital. In 1968, there was another change in the credit system methodology with the transfer of overdrafts to a brand new group of loans – ‘credits for constant need of working capital of socialist enterprise’. It demonstrates how we can understand this specific financial tool - as overdraft accounts opened by the State for an indefinite period aimed to finance continuous needs of working capital. This was the final step towards the system of credits for constantly revolving working capital.

The cornerstone of the system was cooperation between the SBCS and individual enterprises, declared by the Credit agreement. It was a unilateral act made by a branch SBCS towards an enterprise built on positive assessment of credit application before formulation of economic and financial plan. Since crediting of working capital was required by the Law, branches of SBCS or businesses did not have any choice but to do it. A relationship between local branches of SBCS and enterprises had been long-term, intensive and without substitution (Polidar 1987). Credit instruments were provided by local branches on behalf of the SBCS and had to be in accordance with Quarterly plans of working capital, through instruments called Ultimate credit commitments. The commitment was some kind of a pledge.

The system described above had to respect the annual Credit plan and its time schedule. There were usually two types of credits.

A. **Lending to the level of working capital.** This means a branch of the SBCS provides a loan with respect to the level of enterprise's working capital at a certain date. A real level of assets is taken into account. The communication between the SBCS and the enterprise went through special document named ‘Report about situation of credited subject’, alternatively supported with financial and accounting statements. How did the system work? There was some overall level of working capital evaluated in CSK (Czechoslovak Koruna). From this sum of money, assets covered by own resources of an enterprise were deducted as well as assets which couldn't be funded from the Credit plan according to the Status of SBCS (determined by legislation: low-quality products (stocks), poorly stored inventories, excessive inventories i.e. material available for higher than planned production, etc.). The rest of current assets consisted of so-called ‘free ensuring’ that the SBCS compared with a credit limit set by the Credit plan and then provided a credit equivalent to an enterprise. The credit repayment would occur only if the plan should be in accordance with the decline of credit limit, i.e. working capital needed which reflected planned production. For further relevant information, see Polidar (1987, p. 80 and p. 98).

B. **Lending to the turnover of working capital.** This method determined lending by turnover (not level nor balance) of a crucial part of current assets: operational needs (working capital actually). A branch of SBCS reimbursed all purchases of materials, stocks, etc. from special credit account, while sales from goods sold were flown to a turnover account. The credit was repaid from this turnover account to a special credit account opened in the SBCS for this purpose. Basically, we can say that operational needs were covered by loans repaid by usage (and consumption) of working capital. Sales of an enterprise were determined by the Plan, as well as operational needs (working capital) required for such level of production. This was a significant difference compared to the method described above (see A) in which operational needs were covered by an enterprise and then asked for reimbursement at SBCD. In the method ‘Lending to

the turnover', enterprises had more freedom to operate independently because the responsible branch of the SBCS did not control all transactions with respect to actual need, actual level of inventories, etc. on daily basis. Purchases of an enterprise were automatically credited from the special credit account opened at SBCS. The system operated under the condition made by law that "*organizations do not abuse this sovereignty and independence to accumulation of uneconomic, undesirable volumes of working capital (esp. inventories) and their coverage by credits from SBCS*" (Daněček et al. 1962, p. 75). Of course, the condition was absolutely unrealistic.

4. Credits for constantly revolving working capital

Operational needs could be described as a minimum level of working capital needed for meeting production Plan. This constant and continuous need was a basic element of the Plan because it was taken as a tool for forecasting distribution of economic factors of production. Since operational needs of an enterprise were taken as amount to money necessary to invest into current assets, they were closely related to level of production, technologies used, production processes, etc. They do not include short-term, temporary fluctuations of working capital influent by seasonality, fluctuations in sales, encashment irregularities, etc. (Kněz 1972)

In a centrally planned economy – in contrast to market economy – an ambition to manage consumption of operational needs is manageable thanks to short term and long term detailed quantified production processes with breakdowns on state, regional, industry or individual enterprise's level. Technical changes or production mix settings were not made spontaneously, but again with respect to directives from the Centrally Planning Committee.

The system of crediting of operational needs was being developed in 1950s through directives of the Minister of finance of Czechoslovakia and later, since 1961, via directives of the General Director (then Chairman) of the SBCS.

In 1961, the Directive of the SBCS No. 142/1960 about "Providing operating loans and implementation of sanctions" was passed. This document legislatively defined the system of crediting operational needs (previously non-codified) and in that time, the term "constantly revolving operational needs" (working capital) was defined and since that time used in official documents dealing with the topic. In 1967, results of two-year experiment – operational funding via credits – were analyzed and with respect to them, the system was changed to permanent lending on operational needs of current assets, esp. working capital. In the Directive No. 158/1975, §16, the term "constantly needed working capital" was mentioned, from which the concept of "lending on constantly revolving working capital" emerged.

Initially, standard working capital (covered by own sources and liabilities) and non-standard working capital (covered by loan) was distinguished for the purpose of communication with the SBCS about a loan. At the beginning of 1960s, as mentioned above, massive transfer of financial funds from enterprises and institutions to the State budget through taxes and levies was implied; it influenced the system of operational funding as well. The introduction of full crediting of working capital also meant obligation to cover a part of working capital with enterprises' sources. Speaking in terms of economics, the change proved to be very inefficient (Báča and Třetina 1981). After that, no significant changes in the system of operational needs' funding of enterprises

occurred and the system of crediting constantly revolving working capital from special accounts at the SBCS thus worked until 1989/1990.

Formally, the system should have respected the principles of a bank loan in a centrally planned economy, especially in terms of planning, accuracy, efficiency, material coverage, timing and return. Regardless these socialist theoretical proclamations and expectations of authors of the system, it paradoxically strengthened a perverse motivation to behave inefficiently instead of efficiency. The majority of working capital was covered by a credit provided by responsible branch of the SBCS with an interest rate set up by the government. After the implementation of the system (1965), loans crediting operational needs of working capital were provided with the interest rate at level 6 % p.a. Of course, companies could have some current assets as inventories accumulated and stored from previous periods. To avoid undesirable accumulation of current assets, these assets from the past were subject to the same interest rate burden as well (Jindra 1965). This interest limit should have naturally led to a situation where enterprises would keep only minimally required volume of assets or a volume they could afford to finance.

Implementation of the system of permanent operational need, i.e. constantly revolving working capital, was a reaction on initial difficulties with full crediting of working capital, which occurred in Czechoslovak centrally planned economy in late 1960s and early 1970s. A constant (perpetual) need of working capital (constantly revolving working capital) should be – except liabilities – funded also with own activity of the enterprise, especially with finances from profits generated by the business. In practice, however, it depended mainly on how companies and their managements were able to negotiate with representatives of state bodies, especially with employees of branches of the SBCS who participated in audits of economical use of resources in enterprises. Production volumes of individual companies were changing during the year as well as at the end of each financial year. So was working capital. For enterprises with activities non-deflected by seasonality, the need of current assets and their key part – working capital – culminated at the end of the year. To eliminate these difficulties, detailed planning of working capital were implemented, especially by setting so called ‘average working capital need’, calculated from inventory turnover indicators and performance indicators (Báča and Třetina 1981).

Therefore, credits for constantly revolving working capital were adapted to operational needs planned at the end of the year and during the year; changes were based on quarterly or monthly schedules of their use during the year (Polidar 1987). The enterprise thus had its account opened with the SBCS’s branch, on this account the amount of liabilities varied with respect to the current assets needed. As far as the Plan was quantitatively oriented, operational needs (and so working capital) increased more and more. Credit commitment of the enterprise was accumulated and rolled on to the future.

A question about repayment of credits to constantly revolving working capital was a big theoretical problem for central planners. Generally, four repayment procedures were developed and used in socialist economies (Polidar 1987):

A. The maturity date is not determined. A need of constantly revolving working capital permanently increases as centrally planned production increases. In practice, a credit involvement of enterprises at central bank increases as well. The loan repayment occurs only after accelerated turnover of working capital which caused an

absolute decline in needed current assets, or after higher participation of enterprise's resources. This methodology had been used in Czechoslovakia.

B. The repayment occurs permanently. A loan was provided for purchasing of production materials, raw materials and other inventories and was constantly repaid according to planned consumption of working capital and other specific conditions. This method had been used under the system 'lending to the turnover of working capital', for example in the Soviet Union.

C. The maturity set at the beginning of accounting period. A maturity of loan is always determined at the beginning of financial year, when organizations prepare financial plans for the next period. The central bank assesses how and in what amount a loan for working capital is provided (e.g. with regard to expected development of economy).

D. The maturity depending on the increase in profit. A maturity of loan provided for purchase of constantly revolving working capital is determined according to what level of profit (or its increase) the use of higher volume of working capital leads. Increase of permanent operational need of current assets can be considered as a kind of investment need and a process of loan providing reflected anticipation of future increase of profit. This process is very close to market-oriented lending. For example, it had been used in Hungary.

Experts differ in evaluation of the tool of credits for constantly revolving stocks. Some experts considered these financial products used for operational funding of socialist enterprises as appropriate necessity (differentiation of the SBCS credit policy), and others as outdated and wasteful, because it led to the suppression of Khozraschyot² process in companies.

The fact is that the system of operational funding through credits for constantly revolving working capital generated substantial economic inefficiencies.

5. Problems and inefficiencies of the system

Inefficiencies in centrally planned economies were, are and will be a target for criticism. Economic analysis of deficits made by the system of operational funding of enterprises within a centrally planned economy through credits on constantly revolving working capital is an inseparable part of the topic because many of these inconveniences still have an impact nowadays.

5.1 Absence of motivations

Segments of markets, where state interventions aren't observable, are characterized by certain level of competition and pressure made by that. Price mechanism leads all subjects to fair redistribution of resources, economic theory concludes. The fact is that in centrally planned economies similar principles could be find out only in the shadow economy. A high correlation between communist party affiliation and individual success was also an important part of the game.

Off course, these aspects were also observable in operational funding of enterprises within centrally planned economy, especially in terms of working capital and inventories.

² Khozraschyot = Russian acronym of the term "chozjajstvennyj rasčet". It was a planned management method which required the cost of production and the sales were both compared in monetary terms and then expenditures covered by revenues of enterprises, so a profitability of production is ensured.

Employees of such enterprises had an advantage of strong informational asymmetry about production processes compared to their regulators and other state bodies, so they could misuse it during the process of negotiation about planning of working capital needed for meeting the enterprises' plans. It is not surprising that the volume of working capital presented by enterprises' representatives to regulators and controllers was usually higher than really needed, no matter whether under condition of 100% coverage of needs by credits or with partial co-financing from own sources (Sik 1992).

Two main reasons/economic explanations of such a behavior – are offered in the following text:

Firstly, a higher amount of working capital and its turnover meant higher role of the enterprise in the economy, i.e. higher prestige of its representatives in the society with limited possibilities how to get economic sources due to the Plan. Theoretical findings of Niskanen (1971) and 'bureaucrats maximizing budget' can be applied.

Secondly, a direct conclusion of inefficient aggregation of resources enabled to consume excessive part of working capital (esp. inventories) illegally in shadow economy – to use it for your own, to sell it or to use it as an asset in very popular barter transactions (Xu and Maskin 2001).

5.2 Infant industries protection

Centralization of financial funds, i.e. removing of capital from socialist industries in which there is an 'excessive level of resources' and their reallocation to industries which fail to secure sufficient working factors' resources, in the process that goes completely against principles of market economy. Under centrally planned economy, economic development was designed by social engineering and influenced by other factors like needs of other socialist economies, compromises due to the lack of resources, personal interests of politicians and managers, etc. This caused that long-term economic processes (e.g. supply of markets with planned volume of consumer goods) didn't follow the needs of the market and its participants.

Inefficient sectors were financed at the expense of successful ones which could be sources positive economical factors, like comparative advantages and specialization or a base subsequent development of foreign trade. Centrally created plans and tables did not reflect actual development of preferences, distribution of resources (see chapter 4.3) and shares of individual market segments on domestic product. This is mainly reflected in a dramatic increase in structural unemployment after the change of communist regime (Sachs 1996).

5.3 Weak financial management of enterprises

The third important aspect of the system of operational funding of socialist enterprises is a special distribution of factors of productions. Primarily, a management of an enterprise in a market economy must ensure factors of production in sufficient quantity and quality for its business. Especially the distribution of capital through capital market is a reliable selection of efficient and inefficient market players, it doesn't matter, whether one talks about own resources from sales of products or services, or about external resources (like loans to banks, IPOs, bonds and securities offering) which are beneficial from economic reasons (leverage effect). The second task of financial management is to monitor the evolving costs related to financial resources of the company that covering the assets, with using of economic instruments such as the

Weighted Average Cost of Capital (WACC, see Kislingerová et al. (2007) or Marek (2009)).

In Czechoslovakia, however, similar processes absented. The position on the market wasn't formed by free will of consumers, but it depended on state's planning agenda and quantitative targets resulting from it. Preferences to several enterprises based on political affiliation or on fear that responsible controllers will be penalized as revenge for strict control processes to entities linked somehow to the regime were characteristic for Czechoslovak economy. For example a refusal of increase of credit for constantly revolving working capital or a critical control of working capital using in certain enterprises with friendly relationships with regime was absolutely impossible. In an environment with a lack of principles of private property and rule of law efficient motivations hadn't been spontaneously generated, but there were only strong incentives to meet or exceed the quantitative determination of plan. A relationship between real and planned production shaped financial rewards of executives (more on the issue in Matejun (2013)).³

In many enterprises, financial management totally ignored the side of liabilities of the balance sheet because it was a concern of the State and SBCS, and managers focused only on the performance of 'tangible tasks', i.e. on assets. Weaknesses in financial management was clearly evident after 1989 and contributed significantly to the fact that many businesses, until that time in a great shape, got into serious financial troubles or even bankrupted. With hindsight it can be said that the main problem in the early era of transformation was just an inability of enterprises and many managers to adapt to market principles, particularly with respect to operational funding. There was no plan secured sales from production, there was no plan secured factors of production or capital (finances) automatically got from the SBCS, there was no stable inflow to current assets; it meant that corporate managements failed to ensure money needed to finance the fixed costs of enterprises with stopped production, let alone basic production funding or securing of supplier-customer processes.

5.4 Instability of banking sector

Activities of the banking sector under centrally planned economy were completely subjected to direct control of the Communist Party and the Government. This also reflected functioning of the SBCS. Some suggestions of the SBCS are judged positively from the perspective of the current market system (e.g. interest rates, effort to reduce excess working capital in enterprises, requiring monetary and financial discipline, efforts to get loans repaid); the SBCS was just an administrative institution without real control tools. Of course, it was transmitted to other banking institutions (Kunert and Novotný 2008). This was reflected in problems during transition to a market economy. Stabilization of newly established banks, especially the low resolution of liquidity associated with subprime loans in bank balance sheets created by credits on constantly revolving working capital from centrally planned enterprises, was one of the biggest challenges central banks (not just Czech National Bank) have had after 1989.

The banking sector faced a lack of liquidity that the central bank had to cover with special redistribution loans and preferential redistribution loans. An impulse to capital adequacy ratio and to domestic banking sector as a whole was generated in March 1991, when the Consolidation Bank had been established from the decision of the

³ Off course, there were also perverse incentives to overestimate resources and redistribute them in private consumption, as mentioned above.

Federal Ministry of Finance and the State Bank of Czechoslovakia⁴. A large proportion of problematic were transferred to the Consolidation Bank, including credits to constantly revolving working capital in the volume of 110 billion CSK (CZK).

Remediation and stabilization of the banking sector, however, required additional financial packages in subsequent years (Vojtíšek 1990). For example, only in the 1991 bank capitalization increased of 12 billion CSK, and the write-off of bad old bank claims (credits on constantly revolving working capital) in total amount of 38 billion CSK were approved. During the whole 1990s, the rehabilitation of the Czech banking sector requested financial resources higher than 500 billion CZK.

6. Conclusion

Credits for constantly revolving working capital were a phenomenon linking fiscal and monetary policies of socialist governments and operational funding of enterprises within centrally planned economy, which overlapped to private sector as a result of transformation of the economy and privatization processes related to assets and liabilities from centrally planned economy.

This special method of operation funding of socialist enterprises had been used in Czechoslovakia from 1967 to 1990. Main driven factor for a development of this financial tool was aim to create environment with total state control of all production and financial processes, which had been carried out through balanced state budget (surplus) and strengthening of planning role and redistribution. The most important part of the system of operational funding, i.e. funding of current assets consisted of the loans to credits for constantly revolving (permanently needed) working capital. Essentially, it was an overdraft to credit reserves, which were necessary for meeting planned production volume of an enterprise. The volume of production varied, so did the volume of working capital needed for planned level of production. Financial needs credited via these special loans developed in time as well.

The system was not efficient and produced and accumulated many problems among which absolute absence of motivations, infant industries protection, bad financial management and instability of banking sector.

The fact that the system of operational funding of socialist enterprises in Czechoslovakia through credits on constantly revolving working capital has not been yet comprehensively analyzed in any material causes that some errors and inaccuracies are regularly repeated are subsequently taken up by other authors. Credits to constantly revolving working capital are mistakenly considered a subsidy to a socialist enterprise. Subsidies are one-time transfers provided to particular enterprise, but their characteristics are different from loans. The loan has fundamental signs which the subsidy has not - it is a specified flow, with an interest burden and enforceable obligation by the borrower to the lender. The fact that the repayment of loans before 1989 practically did not occur is based rather on the accumulation of inefficiencies, which are often criticized at centrally planned economies.

No functionality of the system has confirmed the strong objections against the socialist economies, resp. communist economies. An implementation of any market elements into non-market, centrally managed environment fails. Capital market is the cornerstone of a functioning market economy, as it provides an efficient distribution of resources.

⁴ The SBCS was split into Czech National Bank and Slovak National Bank in January 1993.

Therefore, a relevant part of the Czech and Slovak privatized enterprises in 1990s went bankrupt – many of new owners saw factories, machinery, buildings and land, but did not think about operational funding.

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