

INTERNATIONAL MONETARY FUND
Research Department

Report on Czechoslovakia *

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January 23, 1947

1. Cooperation with Technical Staff

As instructed before my departure to London I contacted, upon my arrival in Czechoslovakia, all those agencies of the Government which, in one way or another, deal in economic matters of concern to the Fund. Except for formal visits with members of the Government, I confined my contacts to the technical people in the agencies and departments.

In the National Bank and in the Government agencies, I found a great deal of understanding for our needs. The Research Department of the National Bank assembled duplicates of all the literature on Czechoslovak economic problems available in its library and prepared it for shipment to the Fund. In this donation all the monthly and yearly reports of the bank, since its inception in 1926, are included. Similarly I arranged with the State Statistical Office to have them supply us with all its series of publications, published in the past, as well as the ones which are currently being issued by that Office. Those publications which are of immediate need in our work, I brought with me. The rest are being forwarded by mail.

2. Transportation Problem

Economic conditions in Czechoslovakia are greatly improved. The help from UNRRA has had telling effects. In the most difficult months of last winter and spring, UNRRA supplies reaching the country helped to keep the black market from undermining the economic efforts of the Government. The shipments of wool and cotton, as well as gasoline, facilitated production in industries before the Government was able to re-establish trade contacts with countries and markets which usually supply Czechoslovakia's textile industry with its raw material requirements.

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Based on a visit during November-December, 1946.

The transportation system, which, immediately after the cessation of hostilities was completely paralyzed, is restored, even though the lack of rolling stock is still one of the greatest handicaps to the intensification of domestic and the expansion of foreign trade.

By the end of the war over 1220 bridges and 38 tunnels were destroyed in addition to 75 percent of the railroad buildings and heating places and 64.5 percent of railroad switches. In addition Czechoslovakia lost 2,120 locomotives, representing 52.6 percent of her pre-war stock, 8,360 passenger cars, representing 68.3 percent of her pre-war stock and 71,734 freight cars, representing 74.5 percent of her pre-war total. During the 20 months that have elapsed since liberation, Czechoslovakia has restored its railroad network, with permanent or temporary wooden structures.

UNRRA supplied approximately 100 locomotives and over 1,000 freight cars, and this, together with recovery of 13,000 freight cars and domestic production of over 15,000 cars, has considerably eased the transportation situation. Nevertheless, the problem is still great. In July 1937, for instance, 495,752 cars were loaded, while in the same month in 1946 only 255,042 cars were loaded. Moreover, the return of cars dispatched to other European countries, is very slow. In spite of the fact that Czechoslovakia has only 53,000 freight cars, as compared to 95,000 in 1937, the number of cars abroad is much higher now than it was in that year. In turn, there are very few foreign cars in Czechoslovakia. To indicate the difficulties the Czechoslovak railroads have to contend with, it may be mentioned that only upon a written guarantee by the Red Army could Czechoslovak railroads dispatch some 300 cars to Rumania carrying goods. Since this shipment was dispatched six months have passed (on November 28th) and not even the Red Army has been able to return them. A similar situation was experienced when cars were dispatched to the Allied Zone of occupation in Germany. The U. S. Army authorities who are most anxious to have transportation function in their zone, are the greatest offenders in this respect.

Automobile transportation too is handicapped, mainly by lack of spare parts, tires and gasoline. UNRRA shipped considerable quantities of trucks but not enough tires or spare parts. Most of the trucks are of Canadian origin and Czechoslovak factories were not equipped to produce spare parts. Although Czechoslovakia has a considerable production capacity for tires, it has great difficulty in procuring rubber on the world market.

The transportation problem comes first, because it is the cause of many other difficulties with which Czechoslovak economy is grappling. The comparatively lower figures in exports for September 1946 are mainly due to lack of freight cars because these were used for the transportation of potatoes to foreign countries like Germany, Bulgaria and Austria.

Since the cold weather might have prevented shipment of this perishable item all other shipments of export goods, as well as inland transportation, were reduced to the minimum. The constant complaint of importers from Czechoslovakia that they are not being served within the time specified, is due to this handicap. This also affects the functioning of the internal market. For instance, in the eastern part of Czechoslovakia, apples were rotting, while at the same time there was a strict rationing of fruit in Ostrava and Praha regions. The authorities were fully aware of this fact but could not alleviate it because of lack of transport equipment. Officials responsible for the shipment of goods abroad were harassed because they received only 50 to 60 percent of the cars requested.

Passenger service on the other hand is close to normal. Very good sleeping cars are provided for the entire country and trains are running on schedule. This is indeed a great achievement.

In the next year Czechoslovakia will produce 290 locomotives and 16,000 railroad cars. But despite this, as long as neighboring countries continue to have transportation difficulties, the Czechoslovak problem cannot be solved. In peace time the system prevailing on the European continent was such that railroad cars of other countries could be used while a country's own cars were abroad. Now Czechoslovakia has to supply her own cars, not only for exports but as well for importing goods from abroad.

3. Production

In general the production figures achieved in Czechoslovakia during 1946 are better than was expected. High production was achieved in spite of the fact that up to November a considerable shift of population was under way throughout the country. As compared with 1938 population figures, Czechoslovakia lost 2,528,000 people, mostly Germans who were transferred to Germany. Because of this, a great many industries lost a considerable part of their labor reservoir. The percentage of Germans working in certain industries was large, for instance in mining 33 percent, in glass 45 percent, in textiles 40 percent, in the paper industry 38 percent and in others their participation ranged between 8 to 30 percent of all employees.

These losses had to be replaced. In some factories they were replaced completely. In others production was decreased. And in some instances, plants were closed entirely. In the whole of the frontier territory, where the majority of Germans lived, the industrial plants were classified by a committee of Government experts in three categories: (a) those plants whose production had to be maintained and even enlarged, (b) whose production should be maintained on a lower scale at their

present location, or transferred to some other place, (c) plants which should be scrapped, and the machinery either used as replacement in existing plants or transferred to Slovakia where new industrial units are being built in accordance with the Government plan for the industrialization of Slovakia,

The transfer of Germans, is, however, not the only element which decreased the available man power in industry. The other phenomenon, which applies, particularly to the skilled workers, is a psychological desire for a change to the white collar stratum and apparently a need for more such workers in industry. In some enterprises the number of white collar workers increased between 1939 and 1945 by as much as 75 percent. For instance in the Skoda Works it increased by 74.8 percent and in the Czech-Moravian Machine Works 36.8 percent, in the Czechoslovak-Weapon and Machine Tool Manufacturing Corporation 65.2 percent. In industry as a whole the ratio is about one white collar worker to 4 manual workers, while in 1935 this ratio was 1 to 9.

Since July of this year, however, there was a great voluntary shift of workers from Slovakia to Czech and Moravian factories. Among these were about 200,000 agricultural workers. This did not deplete the normal supply of agricultural workers in Slovakia due to overpopulation in Slovak rural areas, resulting from the restrictions on emigration abroad during the pre-war period.

These workers have to be trained, however, before their efficiency will reach the pre-war standard of their predecessors or their Czechoslovak colleagues in the plants.

Yet it was this factor (the voluntary shift of Slovak agricultural labor to Czech and Moravian factories) and the increased percentage of women in industry (from 21.9 to 27.2 between 1931 and 1946) that made it possible to replace very largely the 232,000 German workers who were eliminated in the first nine months of 1946.

On October 1st, 1946, 1,176,000 workers were engaged in Czechoslovak industry, which is about 15 percent less than the number employed in industry in 1937. (It should be noted, however, that in 1937 there were 600,000 registered unemployed in Czechoslovakia, while now there is a considerable labor shortage.)

Industry in General

The industrial production results for 1946 may be summarized as follows: The monthly average production of coal is 1,170,000 tons, or 83 percent of 1937 production. The production of lignite is 8 percent higher than the pre-war average. However, the monthly production of raw iron is 76,700 tons, which is only 54.7 percent of the 1937 production, and the monthly production of steel is 135,400 tons,

70.5 percent of the monthly average of 1937. Because of the high priority in assignment of raw materials and labor, production of locomotives and various types of railroad cars is from 2 to 10 times as large as in 1937.

In the textile industry production is still only 45 percent of the pre-war average. A similar condition of inadequate output exists in the production of certain building materials, for instance, cement 60 percent and bricks 33 percent of the monthly average of 1937.

In industry as a whole a factor which decreased efficiency to a considerable degree was the structural change in the industrial set-up of the country, which is being carried out in connection with the nationalization of the basic industries. There was a considerable shift in personnel and management, all of which did not increase in the short run the production of the plants. It will take at least another half year before the new organizational set-up of the industries and the division of functions will work smoothly enough to increase the production in the various plants.

In general it can be stated that where the Government has laid special emphasis in achieving progress because of priority needs, e.g. mining, the results attained can be compared favorably with pre-war years. In industries, however, where raw materials of foreign origin are needed there is great room for improvement, particularly in the steel, iron and textile industries. As an example, within the first nine months of 1946 Czechoslovakia did not import more than 10 percent of the quantity of cotton she used to import in pre-war years.

Iron and Steel

In iron ore the difficulties were of another nature. Since there was no Swedish ore available after hostilities ended, Czechoslovakia contracted for the importation of Russian ore. The chemical composition and quality of the latter is, however, different and much inferior to that of the Swedish ore. Moreover, it has to be transported as far as Oswieczin in Russian freight cars, then re-loaded on Polish territory into Czechoslovak cars and shipped to Czechoslovakia where it has to be re-processed by special devices so as to eliminate certain undesirable chemical ingredients. This process is a costly one.

When trade with Sweden was re-established the ore which was previously transported down the Oder River had to be shipped to Hamburg and from there down the Elba River to Western Czechoslovakia, from where it was transported by railroad some 600 miles to the furnaces in Vitkovice. Throughout the entire year there were negotiations to resume shipments through Polish territory either via Stetin or Danzig, but with

little success. In July this year the Poles agreed to permit the shipment of 30,000 tons of ore monthly instead of 70,000 as requested, claiming that there are no unloading facilities in these ports to handle such quantities. (It should be mentioned that Czechoslovakia's bargaining position, as far as concerns transit rates, has deteriorated, as compared with pre-war years, because now all the ports and river and rail communications are in Polish hands, while prior to the war Poland and Germany competed for the Czechoslovak transit trade in Swedish ore.)

Agriculture

The recovery in agriculture as compared with 1945 has made great strides. In fact, with mild rationing, Czechoslovakia should be self-sufficient in grain even though its production still reaches only 75 percent of the pre-war level (especially since there are 20 percent less people to feed on essentially the same territory). In sugar beets, production is only 13 percent lower and in potatoes, due to the unusually good crop this year, production is estimated to be 50 percent above the pre-war level.

According to the consensus of opinion among various Government officials, as well as private farmers, the average yield per ha. ($2\frac{1}{2}$ acres) is 4 to 8 percent below pre-war level. It should be noted, however, that even the pre-war yield was only about 60 percent of that achieved in countries in Western Europe.

The situation in animal husbandry is far worse. The number of cattle is about 20 percent below the pre-war years. The quality, however, has deteriorated. As a result, the quantity of milk and butter, as well as meat, is 50 percent below pre-war. The quantity of hogs is 75 percent of pre-war level. The good crop of potatoes in 1946, however, should raise production to the 1937 standard. According to Ministry of Supply figures, the quantities of meats and fats which reach the market are 62 and 40 percent of the pre-war level, respectively. However, as mentioned above, the quality of the meat is very inferior.

The small number of domestic animals reacts unfavorably to grain production as this causes a decrease in the quantity of natural fertilizer, an important factor in production methods of Czechoslovak agriculture. Agriculture, particularly in Bohemia and Moravia is also plagued by lack of labor. In the pre-war years this sector was amply supplied with manual labor. The transfer of Germans (their farms being re-settled by landless Czech and Slovak farm hands) and the great migration of people from villages to industrial centers, created, in the last few months, but particularly during the summer of 1946, a great problem for Czechoslovak agriculture. Because of the high wages which the farmers were forced to pay to their hired help only small self-sufficient farms were profitable enterprises this past year in Czechoslovakia.

To make agriculture profitable again it is necessary to mechanize it. Mechanization is, however, a slow process, particularly at this time, and in the meantime agriculture is short some 190,000 workers. An effort was made to supply these needs by importing seasonal workers from Italy, Bulgaria and Yugoslavia, but this failed completely, and the Government was forced to mobilize university students during the summer months and send them out to the farms to help bring in the crop. There are conflicting opinions about the advisability of repeating this forced measure again. It was more harmful than useful, according to some, and nobody felt that it was really a success.

4. Wage and Price Levels

Unification of Price Levels

During the war the Germans kept the price level in Bohemia and Moravia close to the pre-war level. From March 1939, through the liberation, the price level had not risen more than 60 percent. In Slovakia prices developed more freely than in Bohemia and Moravia and in the corresponding period rose by 110 percent. The black market prices were, however, in both regions, much higher, in fact four times as high as controlled prices. To eliminate the undermining influence of the black market on the morale of the population, and to bring price levels more in harmony with the proposed monetary reform, prices were adjusted by a Government decree in November 1945. In general, this adjustment doubled the increase in prices since 1939 for the whole country.

Since then, there has been a slow rise in prices. Taking as a base March 1939, in January 1946, the index of wholesale prices stood at 266.6. By October 1946, the wholesale price level rose to 292.5, mainly because of the rising prices of imported raw materials and imported goods (e.g. iron ore, copper, lead and zinc).

The cost of living index, which stood at 306.7 in January 1946, taking as a base March 1939, showed, during the whole year, a remarkably stable tendency and in October 1946, was quoted at 306.3.

At the same time, in the neighboring countries the wholesale, as well as the cost of living index, jumped considerably upwards. Were it not for the pressure of the neighboring countries where the high prices were a great inducement for people to smuggle goods across the border from Czechoslovakia, the index of wholesale prices and the cost of living index would have fallen in October. The wholesale and cost of living index for October 1946, as quoted above, reflect to a greater extent than the January figure the real situation of the country because the purchases on the black market decreased according to a survey by

the State Statistical Office to between 5 and 7 percent of total purchases. At the most people bought in the latter part of 1946, in Czechoslovakia on the black market, some fats, pork and fresh eggs, also textiles, (because of the pressure for smuggling out to Hungary and Poland, where exorbitant prices in jewelry and convertible currencies were paid for textiles). Black market operations in cigarettes ceased entirely.

Wages

The wage level index, again based on March 1939 level, slightly increased from 302.3 in January to 302.6 in October, 1946. But this slight rise in the index figures does not reflect the wages actually paid out to workers. It is computed only on the basis of an 8 hour day without taking into consideration the overtime nearly every industrial worker puts in, nor the "black wages" which skilled laborers receive to stay on the job instead of moving to other places. Many industrial managers willingly pay special bonuses to get a skilled worker into their plant. The size of the bonus is as high as the monthly wage or even higher. Another method is an arrangement whereby a worker receives for certain hours of work weekly, overtime pay for time which is not in fact worked. These black wages are paid mostly in the printing, machine tool and glass industries. On the management of an industrial enterprise has a special department entrusted with the procurement of groceries which are not on the rationed list, but yet not easily obtainable, and then sells these to the employees in the plants at a very low price or supplies them at no cost at all.

Labor morale which -- as in the whole of Europe -- was very bad in 1945 improved with the spring of 1946 (especially after the elections). The revolutionary arrangements by which Trade Union Councils dictated wage and hiring policy, in fact even management of a plant, were slowly and successfully institutionalized in a way so as not to hamper the efficient functioning of industry. The certainty on the part of the managers that the Government and public opinion would back them up if they pursued a just and equitable policy and in the course of it would fight absenteeism, eliminate unnecessary waste of production time (like the long sessions of Trade Union Councils during production hours) and apply disciplinary measures had telling results.

The Government, but above all President Benes, pointed out to the Trade Union leaders that since they asked for rapid nationalization of the economy, it was up to them to exert their efforts to make nationalization work. At the time I was in Czechoslovakia the leaders of the Trade Union Movement sponsored a great campaign whose main aim was to eliminate superfluous bureaucrats and white-collar workers, increase the efficiency of labor, and justify the extension of more responsibility and power to the managers of nationalized plants. On the whole this

campaign had results. There is in the whole country a sort of surprised and belated realization that the standard of living the country used to enjoy and hopes to achieve in the future depends on the hard work of all.

Nevertheless, productivity is still far behind what it was in pre-war years. Everybody realizes this deficiency and there are all kinds of schemes presented by every political party and every interested economic group to improve it. The Government hopes that intensive schooling of young labor, as well as capital improvements in plants, and the introduction of modern production methods will increase the productivity of Czechoslovakia labor to standards approaching those in Western Europe, if not those in the United States. The general alertness and the intelligence of Czechoslovak labor, as well as its willingness to learn, augurs well for such a "skilling" process.

The prevalent desire to emigrate and to start a new life abroad which was felt in the managerial class, as well as among the skilled and unskilled workers, has largely disappeared. "We have to make our happiness in our homeland", one skilled mechanic told me, who was in the ground forces of the R.A.F. in England during the war, and spent half a year deliberating where to emigrate. This psychological acceptance and the resulting stability in the lives of the workers and their families has greatly increased the morale of the labor force.

5. Government Finance

Eighteen months after liberation the Czechoslovakian Ministry of Finance and its subordinate revenue and customs agencies, are well organized and are functioning efficiently. At the time I was in Czechoslovakia, Parliament was discussing the budget for 1947. It was a debate in which the whole nation participated. The slogan was "economy". Under the pressure of public opinion the Government slashed expenditures by 3 billion crowns. But the public was still not satisfied and Parliament created a special committee whose function it will be to analyze every expenditure item and see to it that those expenditures which are not necessary are eliminated. In the meantime, Parliament voted the budget as presented by the Government.

From May until December 31st, 1945, the Czechoslovak Government functioned without any budget except temporary appropriations of its own. Only in March 1946 did the Provisional Parliament pass on the budget for the whole of 1946. In disturbed times like those of 1945, the collection of taxes was very lax and it was only in 1946 that revenue collecting agencies were functioning with the thoroughness they were accustomed to in pre-war years. It is because of this that the Government had to borrow 6.4 billion crowns to finance its expenditures in 1945.

The budget for 1946 called for 64 billion crowns on the expenditure side, of which 38.9 billion were intended for normal Government expenditures while 25.1 were intended for reconstruction, investment and aid to war damaged areas. The normal expenditures were to be covered by "normal revenue" of 31.4 so that there was a deficit of 7.5 billion crowns. Investment reconstruction and economic aid expenditures embodied in the extraordinary budget were to be covered for the most part by local credits (18.6 billion crowns) and in smaller part (3.5 billion crowns) from proceeds of the sale of UNRRA goods and an additional 3 billion crowns from other sources (foreign loans).

The actual expenditures in the first 9 months were smaller by 4.4 billion crowns than had been estimated. Nevertheless, there was a deficit of over 1.2 billion crowns. It was stressed, however, that this deficit will grow to a much higher sum in the last three months because the Government is committed to pay certain subsidies, which, according to the Financial Law of the country, can be paid out only in the last quarter of the fiscal year.

In the extraordinary budget for the first 9 months the Government spent only 4.6 billion crowns. The amazingly low figure (the budgeted extraordinary expenditures for 1946 were 25 billion crowns) is mainly due to the lack of materials (especially building materials, which were to be used in the reconstruction projects).

Tax collections in the first 9 months were 2.8 billion crowns, or 13.8 percent higher than the budget estimate of 22.04 billion crowns. Of this amount 2.64 billion were paid in on taxes due before the Monetary Reform was carried out and, therefore, were transferred from blocked accounts. This amount, therefore, cannot be considered as payments from current funds. By passing from blocked accounts to unblocked accounts of the Government, they swelled the money in circulation in the country. This, in fact is one of the inflationary elements in the economy. Parenthetically, one might use the sales tax as a good indicator of the growing volume of business activity. While the December income from this tax in 1945 was 179 million crowns it grew in 1946 to a monthly average of 476 million crowns. Since taxes for 1947 are payable on the basis of the 1946 business results (quarterly) and the sales tax has to be paid immediately, the above mentioned figures are good indicators that tax revenue of the Government in 1947 will be considerably higher than in 1946.

The tobacco monopoly in Czechoslovakia is considered a State enterprise. The revenue from it is not carried under the item "financial income" like that from the sugar or alcohol monopoly. Instead, like the State domains, it delivers its net profit to the Ministry of Finance (net after deductions for investments, etc.). In spite of the shortage of tobacco in 1946, up to September 30, it delivered to the State Treasury 3.3 billion crowns.

Deficit and Borrowing

To supplement this income the Government had to borrow, during 1946, a considerable sum on the money market. Early in the year it issued 6 billion crowns Treasury notes at $1\frac{1}{2}$ percent and in the autumn it issued a 3 percent loan in the total of 4.5 billion crowns. One billion crowns of the latter was used to call a portion of the first issue. In total, therefore, the credit operations for 1946 of the Government amounted to 9.5 billion crowns. The Ministry of Finance has accumulated considerable funds not all of which will be used in 1946 so that a clear picture of the financial position of the Czechoslovak Government during 1946 can be made only after all data are in.

From the first 9 months we can only say that the deficit will be considerably lower than the estimated deficit of 26.2 billion crowns.

1947 Budget

As mentioned above, in spite of the search for economies, the budget for 1947 -- as accepted by Parliament -- was set at 73.3 billion crowns on the expenditure side. On the income side the estimated revenue is 48.4 billion crowns so that 24.9 billion or $\frac{1}{3}$ of the expenditure will have to be covered by credits from domestic money market.

This is a considerable increase as compared with the 1946 budget, particularly since the Government expects the present price and wage levels to prevail and hopes to decrease the number of its employees and economize in all its departments. The reason for the increased budget is two-fold. One is the extensive investment and reconstruction program of the Government and the second the fulfilment of considerable commitments emanating from social legislation passed by the Parliament during the past year to relieve war victims and the socially weakened. Over 10 billion crowns is budgeted for social service purposes.

Investment and reconstruction expenditures which are included in the budget estimate are figures at the sum of 18 billion crowns. Of this figure 11.9 billion crowns are investments within the framework of the two-year plan. These have priority in supply of material and labor. The rest, 6.1 billion, will be carried out according to the stipulation of the Financial Law only if the status of the State Treasury will permit it. Because of this stipulation the deficit may be considerably lower than is now estimated.

State Debt

The internal debt as carried in the budget for 1947 amounts to 88.8 billion crowns. This debt can be divided into 3 parts (a) original debts of the Czechoslovak State contracted before the war (before 1939)

(b) debts during oppression (1939-45) and (c) debts contracted after liberation (1945-1946). These are:-

	<u>In Millions of Crowns</u>
(a) Original Czechoslovak debt	26,960
(b) Debt of the protectorate of Bohemia and Moravia	33,417
Debt of the Slovak State	12,548
(c) Post liberation debt	15,900
	<hr/>
Total	88,825

Of this total 18,819 million crowns is a short term debt at an interest rate of $1\frac{1}{8}$ percent to $3\frac{1}{2}$ percent. The long term debts bear interest at the rate of 3 to $4\frac{1}{2}$ percent.

The amount of interest payments is 3,061 million crowns, which would mean an average rate of 3.44 percent. This, while not high as interest rates go in Central Europe, would still be higher than what the State paid before the war.

Slightly more than half (52 percent) of this debt has its origin in time of enemy occupation and served to finance the German occupation and military needs. In spite of this it cannot be repudiated because in the largest part it represents reserves of small savings banks and insurance corporations. To lower its burden the Government decided that before it resumes interest payments, which were interrupted as of January 1st, 1946, the interest rates of all those loans which are above 3 percent will be decreased to that level resulting in a yearly saving of 400 million crowns.

The foreign debts are enumerated on the attached table.

6. Foreign Trade

Foreign trade of Czechoslovakia is developing successfully and shows indications that the country will regain the position it held before the war. During 1946 it showed an ever rising tendency. In October, 1946, exports reached the figure of 1.8 billion crowns and imports 1.3 billion crowns. In November this high level was sustained (exports 1.9 and imports 1.4). This is a noteworthy achievement. All the Ministry of Foreign Trade hoped for, in 1946, was to reach by December

the level of 1.5 in exports and 1.0 in imports. To indicate how steep a rise this is, it is necessary to mention that in 1945, for the entire 8 months following liberation exports reached 470 million crowns and imports 604 million crowns.

The trade balance for the first 11 months of 1946 shows a surplus of 3.2 billion crowns. This was achieved because many vital imports were supplied by UNRRA which, however, did not figure in the trade statistics. The outlook for 1947 is less bright. The UNRRA program is ending and the supplies which will be needed, hitherto supplied free of charge by UNRRA, are estimated to be \$163 million or 8.1 billion crowns. This will make the balance of trade passive even if the volume of exports, as is expected, will rise to a level of 2.1 billion crowns a month. Moreover, it is expected that the investment activity within the two year plan will further increase the import figures over the export figures.

Another difficulty for 1947 is emerging from the double-track nature of Czechoslovakian foreign trade which Czechoslovakia must carry on, due to her geographical location. Trade relations with South Eastern European countries, as well as the eastern countries (Poland and Russia) can be maintained for the time being only on a barter basis. The ability of these countries to supply Czechoslovakia with vitally needed goods is limited while their requirements from Czechoslovakia consist of commodities demanding a great deal of raw materials imported from the west, mostly from overseas. To secure these raw materials Czechoslovakia has to increase her exports to the west, to curtail imports from that region or to borrow convertible currencies.

In dealing with Yugoslavia, for instance, Czechoslovak trade negotiators had difficulty in committing that country to supply Czechoslovakia with non-ferrous metals. These resources have a big market in the western countries and therefore Yugoslavia intends to sell them for convertible currencies. In paying Czechoslovakia for reconstruction goods like machinery and similar items, Yugoslavia would prefer to provide wines, fruits and vegetables and similar items and to secure credits for the balance.

With the U.S.S.R. the problem is one of prices. The iron ore which is of much lower quality than that obtainable from Sweden is priced by Russia at "world prices". This is also the case with cotton and hides. On the other hand, for goods Russia imports from Czechoslovakia she is willing to pay only the lowest prices quoted on the world market.

While the foreign trade picture is very encouraging it should be noted that the long range picture of its composition and its potentialities are still unknown. The entire structure of Czechoslovak industry is

in process of reorganization. The export possibilities of the textile industry, one of the most important items on the export list of Czechoslovakia in pre-war years, are still an unknown quantity. While it is true that even during and after the depression when countries like Hungary, Rumania, Yugoslavia and Bulgaria built their own industries in this field and protected them with high tariff walls, and when, in the Far East, Japan was competing strongly, this industry maintained its own, yet the potentialities of this industry in the post-war years have to be appraised anew. One must take into consideration that during the war many specialized factories were destroyed and in others machinery was worn out. Moreover, the greatest strength of the industry was in the smaller factories producing fine linen and other specialities which found markets in the United States and other high income countries. It is these small factories that are in complete disorganization. Most of the owner-managers of the factories, and many of the skilled personnel, because of German persecution, either emigrated, or even worse, found their fate in the gas chambers of Oswiecim. Others were moved to Germany when the population transfer was completed last year. How far these branches of the textile industry, so important for export, will recover cannot be predicted. These are efforts to revive production. Not all, however, are successful.

The story in certain branches of the glass, ceramics, as well as the porcelain, industries is the same.

7. Two-Year Plan

Since the two-year plan of reconstruction was signed as a law by President Benes on October 28th, 1946, there has been a great deal of discussion among Czechoslovak economists about the possibilities and problems connected with it. The plan was popularized with great vigor, reaching even the tiniest hamlet. All political parties are committed to it and there is general agreement in Czechoslovakia that such a plan is essential in order to bring about through a concerted action a recovery which would raise production at least to the level of 1937. The two-year plan intends to increase production by 10 per cent over that figure.

Viewing objectively the economic situation and the potentialities of the country, this is indeed a modest goal and it will certainly be achieved if Czechoslovakia is able to secure a loan to procure the needed industrial equipment so as to eliminate bottle-necks in coal, steel and tool production. On the elimination of these bottle-necks hinges the success of other production goals, like railroad cars, tractors, trucks, agricultural machinery, and general consumer goods.

How much capital outlay will be required to carry out the investment projects envisaged in the plan it is difficult to say because there are no available estimates. All the planning was done in terms of units of production and the number of skilled and unskilled laborers that

a given industry will require, but there is no estimate as to the money outlay. Only in the Secretariat of the Economic Council I was told that the total investment will cost 70 billion crowns (\$1400 million). In this figure, investments of State enterprises, autonomous political bodies (provinces and municipalities) and nationalized and private industries, are included. To finance this investment plan, all the available financial resources of the country will be mobilized.

Another essential factor is the expansion of labor supply. It is estimated that 590,000 additional laborers have to be added to the productive force if the desired results are to be materialized. Of these, 270,000 are to be added to industry, 90,000 in the building trades, and 230,000 in forestry and agriculture. Moreover, this in itself will not be enough. To achieve the aimed production the productivity of the entire labor force has to increase by at least 10 per cent as compared with December 1945. Since the productivity has already increased and is still rising, the required 10 per cent will be easily surpassed.

The necessary expansion of labor in industry can be achieved if the Government carries out its publicized intention of releasing superfluous manpower from its services. Some 25,000 men are to be released from the services of the State railroads. They are all young men with technical background who can be of great value to industry. Similarly from the Security Services (greatly enlarged during the revolutionary days after liberation, when anarchy prevailed in all surrounding countries and the Government faced the problem of the transfer of Germans), an estimated 15,000 skilled people can be spared. In other Government departments too, streamlining will release manpower. These people are mostly young and will bring down the average age level of workers employed in industry (the average age in the mining industry for instance is 40 years).

An unknown quantity is the number of workers capable of returning to useful employment, who were rescued from slave labor camps in Germany and from the Todt Organization. In 1946 they were recuperating from the hardships endured during the war. By 1947 a great number of them will have returned to the productive process and become efficient industrial workers. Unknown also, as yet, is the number of Czechs and Slovaks re-immigrating from other European countries. Re-immigration is now being very strongly encouraged by the Government and its agents throughout Europe. A few thousand skilled miners returned in the latter part of October from Hungary. The problem of supplying labor for agriculture, however, still requires solution.

8. Balance of Payments

It is difficult to present a clear picture of the post-war balance of payments of the country. The following table is based on estimates prepared for 1947 by research departments of the various economic

ministries.

Preliminary Estimate of the Balance of Payments for 1947
(in millions of dollars)

	<u>Estimated Receipts</u>	<u>Estimated Payments</u>	<u>Estimated Deficit (-)</u>
1. Merchandise	590	670	-80
2. Services (Brokerage, Commissions, Insurance, Freight, Customs, Diplomatic and Business Representations, Travel, etc.)	20	68	-48
3. Remittances, Subsidies, Pensions, Gifts, etc.	2	1	/1
4. Interest, Dividends, Rentals, etc.	2	20	-18
5. Payment of debts, Transfer of Capital, etc.	1	10	- 9
Total	615	769	-154

Before the war Czechoslovakia, even though a debtor nation, was able to meet her capital commitments from the surplus of her foreign trade. In the first years after the liberation it will be difficult for Czechoslovakia to balance her payment obligation with her receipts. Her capital indebtedness abroad increased and the complete depletion of raw material stocks, as well as capital goods, will require large purchases abroad which in turn will make her balances of trade passive at least for two or three years. Some of the factors (other than trade) accounting for the less favorable post-war balance of payments are worth noting.

1. Prices of imported films have increased considerably, as compared with pre-war years, while receipts from the export of Czechoslovak films decreased to a negligible sum.
2. Patent license fees are higher than before the war and the receipts for Czechoslovak patents and licenses are much smaller.
3. There is a considerable rise in commission payments to agents abroad as compared with pre-war years. This item, although transitory, will be important in the first three or four years after the war.

4. Payments in support of international institutions established during and after the war are much higher than the contribution of Czechoslovakia to international institutions of pre-war days.
5. Czechoslovak representation abroad costs much more than foreign missions spend in Czechoslovakia.
6. The tourist trade, which was a considerable source of income for Czechoslovakia, will be negligible for the first few years.
7. Immigrant remittances which were decreasing even before the war are not only a very small sum and it is difficult to estimate how they will develop in coming years.
8. Interest payments and amortization of loans abroad will now require a higher sum than before the war. At the same time, income from investments abroad has declined or stopped altogether. Most of Czechoslovak investments were in countries which nationalized important industries or otherwise stopped payment of profits and interests (i.e. the Balkan countries).

9. Czechoslovakia's Parity Rate

While I was present in Czechoslovakia the question of the parity rate of the Czechoslovak crown was discussed. The conclusion that Czechoslovakia will stick, for the time being, to a parity rate of 50 crowns to one dollar was reached by the Government, after lengthy discussions among the leading economists of the country on the basis of a memorandum by a standing non-political committee of experts on monetary reform.

The principal argument for the maintenance of this parity rate was that while an over-valued crown might, in the long run, hinder foreign trade of the country, at present the volume of exports is limited not by prices but by physical limits of production and by problems outside of Czechoslovak borders. The committee in its memorandum anticipates that for the next three years there will be a sellers' market and under such circumstances a slight over-valuation of the Czechoslovak crown might not prove dangerous to the Czechoslovak economy.

A devaluation at this time would considerably increase, in domestic currency, the prices of raw materials and other important items which, in turn, would increase the price level in the country and force a re-adjustment in the cost-price structure. (Even now the prices of imported commodities are exerting a continuous pressure on the wholesale price level. Between January and September 1946, the wholesale price index increased by 10 per cent from 266.9 to 293.6). The reasons for this increase are mainly the higher prices of raw materials and some finished

goods imported from abroad. An analysis of the wholesale index numbers shows that 1/3 of this increase is due to an upward adjustment in prices of domestic raw material resources, while 2/3 are due to price rises abroad. The index of imported commodities rose from 293 to 361, that is 23.2 per cent, while the index of commodities of domestic origin increased only by 7.5 per cent from 264.4 to 284.

It was also felt that the change in the value of the crown at this time might shake its position as a leading currency of that part of Europe. This would, in turn, retard the re-establishment and reconstruction of the economies of neighboring countries. The Committee also argued that even a request to postpone the date for the determination of the par value of Czechoslovakian currency would be of greater harm than help. It would shake the confidence of other countries in the crown and thus hamper Czechoslovak trade relations with them. It might also start a wave of speculation among the exporters in the country itself. On the one hand they would hesitate to transfer to the National Bank their foreign claims in the hope that they will get more for them in the near future in terms of the crown and on the other hand they would wait with their sales abroad and thus slow down the recovery of Czechoslovak foreign trade. (An additional consideration was that a devaluation would mean an increased budgetary burden on the Government in meeting its obligation to amortize the foreign debt).

10. Monetary Reform

The monetary reform of the country was initiated in November 1945. At that time, by a series of decrees, the Government unified the currencies of the country by eliminating the five currencies (the Czech crown, the Slovak crown, the Reichsmark, the Pengo and the Polish zloty) from circulation and exchanged them for the new Czechoslovak crown. Simultaneously it ordered all cash to be deposited with the banks, where, together with sight and saving deposits, it was blocked, except 500 crowns per person, which was issued in the new currency. At the same time the Government decreed an average rise in prices and wages of 200 per cent, as compared with March 1939, thus putting the whole country on a unified wage and price level.

It also established a new exchange rate of 50 crowns to the Dollar and 201.50 to the Pound Sterling. By this series of actions and their amplification it was achieved that the total amount of currency in circulation decreased from 130 billion crowns in May 1945, to 31 billion in January, 1946.

Unfortunately in the law decreeing the blocking of accounts there was a loophole as far as Government agencies and autonomous bodies (district, provinces and municipalities) were concerned. These were exempted from the blocking provisions. The Government was not aware of

the large sum (some 15 billion crowns) which was involved. In the course of the year a great part of these balances was withdrawn from the banks and thus swelled the circulation. Over 2 billion crowns were transferred from private blocked accounts to the free accounts of the Government in lieu of payment of taxes due for 1945. From the 1st of January until the 1st of December 1946, when stricter regulations were put into force, 13.3 billion crowns were released from the frozen deposits. Moreover, the Government borrowed from a consortium of private banks a sum of 6 billion crowns, of which 3 billion was borrowed in turn from the Central Bank against Government securities.

These sums, together with some other balances which were de-blocked by the Ministry of Finance, to private individuals or corporations, swelled the bank notes in circulation by December 31st, 1946 to 43.5 billion crowns. The rise of 12.5 billion bank notes in circulation within a year did not bring about inflation, mostly because the population increased considerably above the pre-war level its idle cash holdings. This, together with increased production, was able to absorb the additional currency in circulation. The safe margin limit would appear to have been reached and officials of the National Bank are most anxious to prevent any additional currency expansion. The Ministry of Finance was instructed to issue new strict regulations to stop the leakages from which funds from blocked accounts passed into free circulation. As of December 1st, 1946, funds from accounts of autonomous bodies could be released only with the approval of the Ministry of Finance, taxes could be paid only from currently established balances, or with cash, and the loan policy of the National Bank of Czechoslovakia was tightened.

The commercial banks reported throughout the year a growing volume of business. The loan requests, however, were predominantly of short term nature which indicates that reconstruction was more hampered by lack of materials and labor than by financial resources. The situation in deposits is different in industrial and urban centers and in the rural sections. While in the rural sections the saving banks and the saving banks' cooperatives reported in August an equal rise in saving and sight deposits, in the large city banks the increase in sight deposits predominates, while increments to saving and time deposits are negligible.

11. Blocked Accounts

The action of the monetary reform mentioned above did not eradicate completely the inflationary legacy of the occupying power. Now that the Government was able to establish full public confidence in the new currency it has to attack the problem as to how to dispose of the blocked accounts which, on December 31st, 1945, amounted to 249.5 billion crowns.

The problem as it presents itself, is as follows:-

Blocked deposits as of December 1st, 1945.....	249.5
1. From this sum is to be deducted amounts which were not claimed by their owners or their legal heirs within the specified time limit prescribed by law and will be forfeited	21.4
2. The Parliament levy on capital and war profits, the proceeds of which will be used to finance the released blocked accounts against which there are no assets available, will bring in an estimated	30.
3. Deposits of enemy nationals	40.6
4. Some smaller items, together	<u>5.5</u>
	97.5

This total will decrease the blocked accounts to 152 billion.

Therefore, even after all these measures are carried out the Government will have to take some action on the 152 billions of deposits to prevent inflationary dangers. Of these 152 billions only 50 billions are covered by real assets held by the depository banks. For the rest there are only fictitious assets, viz, deposit claims against the National Bank, which in turn has in its books claims, of doubtful value, in the same amount on the German Reichsbank.

In an effort to find assets to cover these deposits and slowly release them to their owners the Government proposes to create a "Currency Liquidation Fund" attached to and administered by the National Bank of Czechoslovakia. The Fund would take over all the obligations on the blocked deposits from the commercial banks, together with the respective assets. Among the assets there are some good assets (e.g. claims against Czechoslovak debtors, securities of Czechoslovak firms, etc.) and doubtful ones, (German Reichsbank securities, treasury notes, claims against German nationals, etc.)

Since, however, the obligations are larger than the total sum of good assets the Liquidation Fund will be made the recipient also of proceeds of all sales of the property of transferred Germans, confiscated property of collaborators, reparation and restitution claims, as well as of some yearly donations from the State. The operations of the Liquidation Fund are envisaged so as not to disrupt the normal trade channels of the business community.

The commercial banks will not hand over to the National Bank the good assets covering the blocked deposits, but instead they will open to their full amount for the Liquidation Fund an interest bearing sight deposit account. How much of these deposits the Liquidation Fund will be able to use will depend on the liquidity of each separate bank. For the greatest portion of the deposits the Liquidation Fund is supposed to issue its own interest bearing marketable securities which it will slowly redeem. The rate of redemption will depend on the good assets the Liquidation Fund will accumulate from the above mentioned sources and on the condition of the money market. The proposed currency, Liquidation Fund and the problem of de-freezing of the blocked accounts will be dealt with in a separate memorandum.

Czechoslovak Foreign Debt

Origin of Loan	Amount in U.S. Dollars	Total in U.S. Dollars	Year Due	Amount in Original Currency
<u>I Debts taken over from Austria-Hungary:</u>				
(1) 3% franc priority privileged Austro-Hungarian Railroad Corp. Loan	\$ 25,246,359		1965	286,298,771 gold fr.
(2) 4% ditto	401,956		1965	48,852,266 F. fr.
(3) 4% Austrian gold-rent	19,017,926			72,787,533 Fl.
(4) 4½% Austrian Treasury Certif.	282,812	44,949,053		5,513,400 K.
<u>II Loans Between the Two Wars</u>				
(5) British Government loan for the repatriation of Czechoslovak Army from Siberia	1,618,000		1935	401,491 £
(6) U.S. Govt. loan to feed, equip and repatriate Czechoslovak Army from Russia	115,000,000		1987	115,000,000 \$
(7) Loan to maintain the Czechoslovak Army in France	2,138,369		1979	254,688,056 Fr. Fr.
(8) Loan to maintain the Czechoslovak Army in Italy	16,580,519		1956	41,122,321 Gold Marks
(9) Czechoslovak liberation debt according to the Versailles Treaty of Sept. 10, 1919	58,712,817	194,049,713*	1966	145,617,106 Gold Marks

*) Items 5 - 9 are the so-called political debts of the last war and their repayment fate is unknown.

Origin of Loan	Amount in U.S. Dollars	Total in U.S. Dollars	Year Due	Amount in Original Currency
(10) Czechoslovak foreign loan of 1922 dollar issue Pound sterling	1,722,400 3,861,949		1960 1960	\$ 1,722,400 953,509
(11) British loan of 1938	24,298,139	29,882,488	not determined	6,029,315 £
<u>III Loans During the War</u>				
(12) British Administrative Loan	55,790,841		not determined	13,324,221 £
(13) French Administrative Loan	221,654	56,012,495	not determined	26,400,000 Fr. Frc.
<u>IV Loans After Liberation</u>				
(14) Canadian loan for the purchase of raw materials and goods (limit 19 mill. Can. dollars)	4,008,000		1948-56	4,000,000 C. \$
(15) British loan for the purchase of commodities (limit 5 mill. £)	7,939,100		1949-53	1,970,000 £
(16) Loan of the Swedish Govt. * (limit 24 mill. Swedish Kroner)	3,338,640		1948	12,000,000 Sw. Kr.
* Was repaid in full in 1946.				
(17) Loan from the U.S. for the purchase of war surplus goods (original limit 50 mill. \$, suspended on Sept. 27/46)	7,500,000		1947-76	7,500,000 \$
(18) Loan from the Brazilian Govt. (Limit 20 mill. U.S. \$)	606,500	26,392,240	not determined	606,500 \$

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|---|--------------|
| (1) Export-Import Bank credit for purchase of cotton (limit \$20 mill) | \$15,734,525 |
| (2) Export-Import Bank credit for the purchase of tobacco (limit \$2 mill.) | 1,267,000 |
| (3) Hambros Bank Limited, London (Limit £ 1 mill.) | 788,905 |

Total \$348,285,989