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SUB-COMMITTEE ON SOVIET ECONOMIC POLICY

RECENT DEVELOPMENTS OF THE COMECON BANK

NEW COMECON CONVERSION SCHEME

Note by the United Kingdom Delegation

At the meeting of the COMECON Finance and Currency Committee in Budapest in October 1965 it was decided in principle that part of the Bank's capital should be paid up in gold or convertible currencies, but no final decision was taken on the handling or use of these funds. There were a number of differing proposals from members all of which will be discussed on future sessions. The Soviet attitude to convertibility is not clear, but there have been indications recently that although agreeing in principle she might oppose any practical measures to put this into effect. The fact that little concrete happened at Budapest is substantiated by the Polish Deputy Prime Minister's statement in "Trybuna Ludu" on the 5th December. Jarowzewicz: said (a) the Polish regard the agreement (on the change in the Bank's capital structure) as a modest but constructive move in the desired direction. (b) It is by no means a move which would bring about an unsuitable improvement in the system of multilateral payments. (c) It should not be construed as a step on the path leading to the full exchangeability of the transferable rouble. (d) COMECON will be working further on this problem.

2. In the same statement Jarowzewicz indicated that in 1966 10% of the Bank's capital might well be in gold and foreign currency, made up of contributions from member countries. According to our estimates, the cost to each member would be approximately as follows, based on pro rata contributions of each country to the Bank as laid down in the Bank's charter:

	$m
Bulgaria	1.9
Hungary	2.3
Soviet Occupied Zone of Germany	6.1
Mongolia	0.3
Poland	3.0
Rumania	1.8
USSR	12.9
Czechoslovakia	5.0
	33.3

These amounts, which do not seem unduly onerous, will presumably be lost to the reserves of the countries concerned; according to the Bank's statutes, subscriptions are returnable only if a member leaves the Bank or if the Bank goes into liquidation. Yet if, as seems possible, these funds are at present to be used primarily for lending purposes, the loss may well be more than offset by greater ability to borrow convertible currencies out of bloc resources. This is likely to have an effect on the credit worthiness of individual bloc countries.

3. In our view the Polish Embassy official's statements (quoted in AC/89-WP/177/1) that part of the proposals at the Budapest meeting "provided for partial conversion of long-term surpluses, but in a strict bilateral context" suggests some form of penalty clause in inter-bloc agreements. Under this a partner country would have to settle a long-standing deficit in convertible currency once all their attempts (including presumably the COMECON clearing system) had failed. This would probably not result in payment ever being made in free exchange, since debtor countries would presumably use all other means for settlement. We have seen nothing to confirm this report and it is perhaps strange that Jarowzewicz, who was being fairly outspoken, did not mention it in "Trybuna Ludu".

4. We do not believe that the Poles (and Czechs) have given up their idea that part - and eventually all - of COMECON countries periodical net credit balances within the system should be convertible into gold and freely convertible currency. This would indeed seem to us to be the logical aim - to generate within the system outside purchasing power to the extent of net internal claims. But in present circumstances the main burden of providing the convertible currency would be bound to fall on the USSR; and the facility would tend to accelerate the current loosening of Russian ties over the direction of East European trade, at a time when large wheat purchases in the West are costing the Russian reserves sizeable sums. Another important factor is the need first to bring the COMECON system itself on to a more rational footing; considerable work has to be done on the adjustment of bloc prices vis-à-vis the outside world (and between individual bloc countries), to mention only one pre-requisite.

5. Although it is not clear why COMECON has decided now to go ahead with the change in the IBEC's capital structure without first agreeing on its purpose there are probably enough good banking reasons for making this limited change. This change was in any case envisaged in the October 1963 agreement which set up the new Bank. The Bank already does part of its business in convertible currencies. It accepts deposits of such currencies from members and re-lends them, and also conducts "operations" in convertible currencies with non-members. There is some logic, therefore, in the inclusion of these currencies in the Bank's basic capital. First, it means a more secure base, since it brings contingency reserves in convertible currencies on its balance sheet; secondly, the funds could be used towards extending present business, particularly for making currency loans to members (all under control). We do not think that the funds are required to meet incidental expenses, commissions, etc. in the West, since it can be assumed that the Bank is already making a suitable running profit on its convertible currency operations.

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