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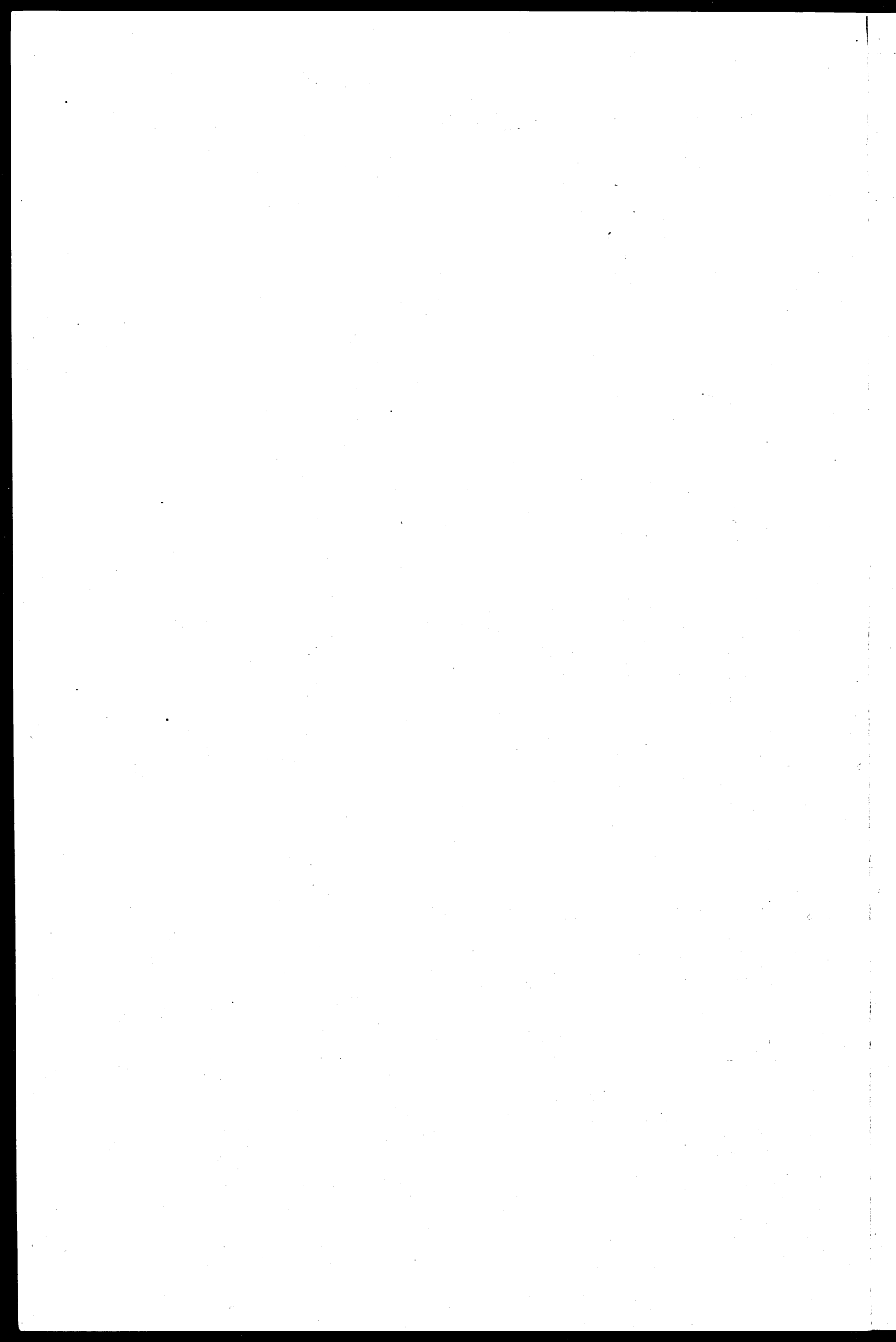
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BUDAPEST



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POINT OF VIEW OF THE DEVELOPMENT OF
COUNTRY BANKS IN HUNGARY , AND
PROPOSAL ON AN UP-TO-DATE SCHEME

by

Ádám BALOGH - Mrs. Gabriella MEMHÖLCZER KAPITÁNY

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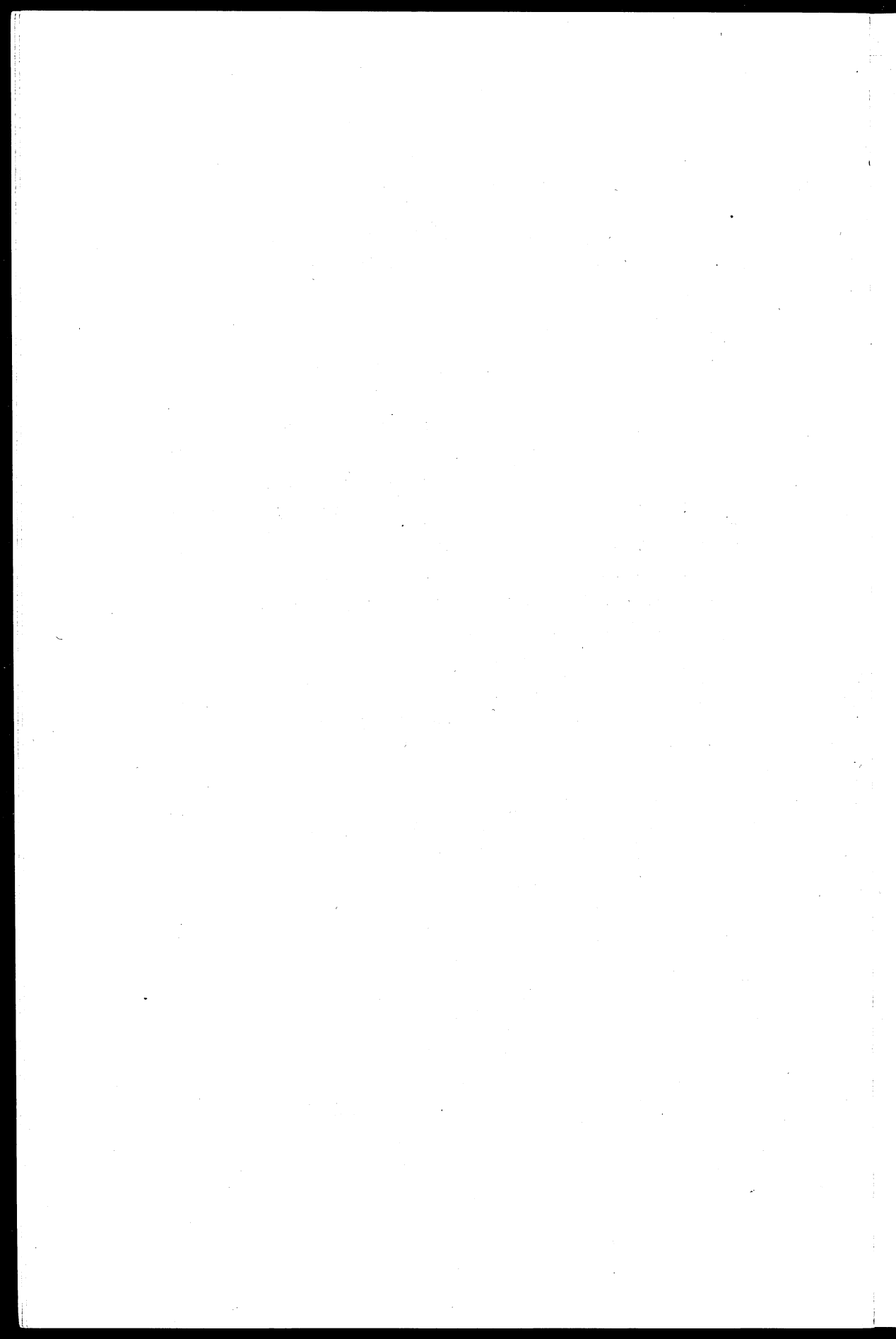
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PREFACE

As a result of the change in ownership, it is reasonable to anticipate the development of a layer of 60 to 80 thousand agricultural entrepreneurs as soon as in the coming 2 to 5 years. The appearance of independent family farms strengthening the bourgeois civilization of villages, i.e. the rural middle-class, is not conceivable without extensive financial services. To achieve this, a dense network of universal small banks is required. It is essential that they are organized on cooperative principle, that the member-owner is, at the same time, the depositor and client, of the bank, applying for credit, respectively. Thus, the revenues earned in a village will remain there and serve the interest of the local community.

The domestic savings cooperatives have a part of facilities a small bank assuming rural financing should have. However, they are very heterogenous in terms of their capital strength, professional skills, infrastructural facilities. Organizing them into a strong network can be provided by a programme allowing the weak ones to align themselves to the strong ones, constituting a change in terms of quality, without needing to give up their independent cooperative status.

By investing two and a half years of development-research work, backed up by the material-intellectual support of the Mentor Small Cooperative, we have elaborated a concept that, as we hope, is suitable for resolving the indicated mass of problems.

The project is, substantially, a service-like intervention affecting the whole environment of rural economic management which provides the interest-based coordination of farms, advisors, credit institutes and information systems, their simultaneous putting into operation.

Approach of intervention: basically the improvement of facilities.

It intends to make:

1. the entrepreneur capable of managing his activity. By this, it simultaneously obtains also the ability of being a

partner of the banking institute (crediting etc.), of the agricultural administration (regime etc.), of the budget (taxation etc.);

2. the banking institute capable of servicing the rural clientele (elaboration of information-based new crediting approaches, monitoring of credits put out); and of successful, safe surviving in form of an independent cooperative (laying the foundation of the safe operations in the money market by way of high-standard banking services).

It can make the interest representations, the agricultural administration capable of establishing the framework of the whole verticum of food production (by using correct, wide-base information) and of regulating same in the required direction (regime).

The project gives the participant a decision-tree utilizing the services and, simultaneously, it also provides the participant with the ability of deciding (information). The one (entrepreneur, banking institute etc.) joining the project enters information about his/its activity into the project and, in return for that, requires information necessary for his/its activity from the scheme (money-, capital-, product- etc. information).

The condition of information flow is the network-like operation. Its technical background is constituted by a satellite communication network for the installation of which the Mentor is ready.

The intellectual capacity of the so-called methodological centre is an essential element of the project which, by the subject-specific processing of information and by means of its consulting network, functions as a catalyzer in the scheme.

Budapest, 3 February 1993

The Authors

INTRODUCTION

The concept of establishing a network of country banks is of the same age as the regime established by the change. Both the economic management and the political sphere realized that there would be a need of up-to-date, multi-function banks having a wide network, for the regional transformation started with a change in the ownership structure. However, the worded objectives have not been implemented as yet.

There are several reasons for this unsuccess. On the one hand, it has become clear that to develop such a banking system and to prepare same for meeting the expected demands constitute not simply an issue of money and decision but also an issue of establishing and operating a number of other organizations belonging to the environments of such banks, too. On the other hand, the elaboration and completion of this difficult task take the cooperation of financial and governmental bodies (first of all the Ministry of Agriculture and the Ministry of Finance) and several socio-economic representative bodies and institutes respectively, for granted.

This Study has now been completed as a result of our research and development work we have conducted for two years, based upon the knowledge of the peculiar regional relations and interests. This Study, as for its genre, structure, train of thoughts and formal requisites do not follow the rules developed and adopted in our Institute.

We discuss the regional practice and agricultural financing developed until now only briefly, in a recapitulative manner. We have laid the emphasis on presenting the peculiar traits of the cooperative banks playing a decisive role in rendering banking services to the regions, to the changing agrarian structure and to the villages.

In the course of analysing the points on the decision tree, we discuss the tasks of savings cooperatives, with the assumption of tasks by the state and with the tasks to be done in terms of legislation.

The development concept disclosed in chapter 5 is a know-how constituting the intellectual property of the MENTOR Small Cooperative, in the elaboration of which fellow-workers of our Institute have participated as well.

As a result of our joint work, we now publish our concept in which we detail the partly vertical, partly horizontal modules of the regional banking system.

In addition to those concerned and working in the Ministry of Agriculture and in the Ministry of Finance we recommend our Study to the managers of savings cooperatives and to top-level financial, economic and interest representation experts.

1. PRACTICE OF AGRICULTURAL FINANCING DEVELOPED SO FAR AND ITS CRITICISM

1.1 Brief review of the period preceding the change of regime

Until the last, great collectivization campaign of the agriculture which began in 1959, it had only been the state farms and companies belonging to other sectors that could obtain credit. This possibility had not even been mentioned in terms of individual farmers.

The functioning ability of the formed farmer cooperatives was a matter of political prestige, therefore, credit lines were opened for them within a short period. Until 1966, they accumulated such a huge debt stock that threatened to cause a total economic and financial bankruptcy. To prevent this, the state released their credit debts. Subsequently, financing of the regions, mostly the farmer's cooperatives, was performed in a more careful manner and in a framework becoming more and more consolidated. As for the established conditions, efforts were made to allow for the nature of the agricultural sector. Development credits were made available by the country branches of the National Bank of Hungary at an extremely low interest rate, lower than that of the deposit rate. The interest rates of short-term credits financing the production was moderate, too; they exceeded the interest rate of time deposits by 1 to 3 percent points and that of the deposits on demand - by 3 to 6 percent points.

Nevertheless, with a view to the depressed agricultural prices, even this banking charge seemed to be unrealistically high but the repeated financial impossibility of performance of the large-scale agricultural farms was hindered by the extensive system of agrarian support, then by the rapid development of the more profitable industrial, commercial and servicing divisions. The showy collapse even in a "provident" economic-political medium was impeded partly by the political will, partly by the successful central and local lobbying. Several

dozens of farmer's cooperatives and state farms were granted ad hoc supports (tax-relief, extraordinary, non-refundable support, allocation of funds etc.) from year to year.

The small-scale agricultural production and other regional enterprises which, first, were tolerated then considered as desirable and worthy of support were - in practice - granted no credit within legalized frames till the early 1980s. The small-scale and private sectors had no place in the crediting that functioned in a centrally managed allocation system. The development of household farming plots which accelerated in the 1970s was mostly financed by the producers, out of their own resources, partly with the help of the large-scale farms and from small-amount agrarian loan borrowed from the savings cooperatives and from the loan borrowed from the OTP (National Savings Bank), granted for the purchase of commodities or for personal purposes, respectively. The network system of the bank was even physically unsuitable for providing the small clients with credit, as establishing and maintaining personal relations necessary for this was impossible anyway.

The division of the banking system into to stages has brought a slight change in regional financing. The commercial banks that were founded have opened their branches also in several small towns and in some more substantial large villages, after having established their city networks. However, their interest has been concentrated not so much upon the agriculture but rather upon the collection of resources and upon providing the major industrial-commercial-servicing units with credits, upon keeping their account, and the management of currency transactions. The banks' private clients have remained, disregarding the last 2 years, little in number. The population's banking relations were limited mainly to three networks:

- the OTP branches operated at larger settlements,
- the savings cooperatives and
- the Hungarian Post.

Among the commercial banks the OKHB (National Commercial and Credit Bank) has become the largest financier of the large-scale agriculture and food industry. As to their activity, the Agrobank, the Mezöbank, the MHB (Hungarian Credit Bank) and Post Bank have still had a substantial share in regional financing. The number of their independent network branches has increased to about 250 altogether. The network of the 5 banks have been established parallel to one another; they are all present in every major city. As far as the rural farmers, entrepreneurs are concerned, none of the commercial banks has come near enough to these persons, therefore no substantial relation has been established between a commercial bank and private persons either.

The agriculture and the food industry became the main loser of the inflation that started in 1979 and accelerated in the 1980s (in addition to the population). The subsidies were curtailed at a rapid pace, the interest rates on credit increased abruptly. By raising the interest rates on deposits and those of the central bank, the resource has become more and more expensive for the banks as well. The agriculture and the food industry could less and less manage to cover the more expensive credit and the price loss due to inflation. In the whole sector, the using up of production funds commenced, without refilling these funds. Nevertheless, the process resulting in the decrease of assets was not clearly stated by the company books and the banks did not pay attention to that either. The obtainment of credit did not substantially become more difficult in respect of the large-scale agriculture and food industry either, the banks did not substantially examined the actual credit coverage. They claimed strict, often non-fulfillable guarantees only from the beginner private entrepreneurs growing in number.

Due to the bank's attitude neglecting the necessary precaution, the coverage put out in the sector of food economy was, in 1990, already constituted a property which was, to a great extent, "leached" by the price scissors, by the usage, by "pre-

serving the property for posterity", in form of companies of limited liability, and by the general devaluation and it also constituted a production with a confused market demand behind it.

1.2 Change in the relation between debtor and creditor, current aspects of financing

The income- and property position of the food economy has continued to become worse for the last 2 years. In 1991, a decrease of nearly 50 billion Ft occurred in the results of both sectoral groups. The most important reason for this was the price loss caused by the inflation as the input price increase of 30 to 35 % on an average could not be included in the prices of agricultural and food industrial products. The farms of unfavourable facilities got into a particularly difficult situation.

Due to the considerable losses, the financial and income position is alarming in the meat-poultry- and conserve industry as well. The negative processes have basically left their mark on the agricultural financing.

The economic shock of the banks' agricultural partners have made crediting extremely risky. The new law on banking institutions has made the security of outlaid credits a No 1 priority. It prescribes a strict obligation to make provision for the qualified outstanding claims. These reserve funds shall be kept in form of liquid coverage. The latter ties up a resource not negotiable at an average yield and results in a fictitious loss (Annex 1).

In addition to the fact that the directives regulating the operation have become stricter, the banks' becoming more precautious, their "buttoning up" against a considerable clientele tightly correlate with the processes taking place in the agriculture, causing several uncertainties (change in ownership, transformation) and carrying negative certainties (relative and absolute devaluation). The decrease in the results

of the 800 farmer's cooperatives, 80 state farms, 200 food industrial companies alone, which constitute the food economical clientele of the OKHB within one year exceeded (in 1991) 30 billion Ft! This circumstance increasingly draws the attention to general problems arising irrespective of the banking activity which make the production of foodstuffs impossible in a wide producer's circle, in financial-economic terms.

By the exhaustion of the reserve funds and of the involvement of internal resources which resulted in the reduction, winding up of several sectors, the demand for the external financing of production increased also in terms of real value. (In this, the farmers are not guiltless either, since they put off, delayed the necessary change in produces, the deliberate processes of reducing the staff, the inevitable dismissals, etc.)

Nevertheless, at the same time, the restriction terminated the possibility of refinancing adjusting itself to the peculiarities of the agricultural and food production in an acceptable manner. The resource conditions of the commercial banks could not meet the credit demand of the food economy. The credits relying mostly on short-term resources, even today are unsuitable for financing the agricultural and food production, being reasonable in professional terms.

The credits for refilling the capital, which were made available in 1989-90 - refinanced partly by the MNB (National Bank of Hungary) - for terms over one year, in order to reduce the "lack of money", could only mitigate the insolvency of cooperatives or companies being in the worst situation. The problem of resources was significantly intensified by the fact that the prompt cash following a supply against rouble was replaced by payment (in dollars) after 60 to 110 days. The delay of revenues was one of the reasons for the vertical "circle-shaped queuing of creditors."

Now, subsequently, it can well be seen that in addition to the price losses, sales difficulties and to parsimony concerning the support of the export by the Government, the high

rate of banking interest contributed to the economic collapse of the food industrial sector as a gulf came into existence between the realizability and the interest rate levels ranging from 35 to 40 per cent.

In 1991, as a mitigation of the obvious financial troubles the conditions of obtaining credits improved in the circle of the producers and food industrial companies interested in exportation. At a more favourable interest rate, the cooperatives, companies having suitable sales contracts anyway, could obtain export pre-financing credit and currency credit. Despite the "circumvallation" with securities, the amount of the overdue debts of the agricultural and food industrial clients still grew.

In respect of the performing ability and operation of the agricultural sector, the most critical situation developed in the spring of this year. In the plants and farms being insolvent or near to insolvency and declaring bankruptcy, the financing of the springtime field works was questionable, to say the least. With regard to the operations omitted in the autumn of 1991, the possibility of the decrease in production to an already inadmissible extent and that of an accompanying nationwide economic scandal cast their shadows before. The general public, in this situation near to being "checkmated", raised - rather unambiguously - the question of the banks' responsibility, though it was obvious that the banks, alone, making efforts for a profit-oriented, safe crediting could not assume to resolve this mass of problems. The difficult situation assisted in recognizing and enforcing the fact that the banks need state guarantees and the producers need interest rate preferences to launch the putting out of credits. By the elaborated new transaction-financing construction, at a 10 per cent point interest rate allowance, the OKHB, as most important agricultural creditor, made an agricultural production credit of 1.6 billion Ft available in the spring of 1992, covered by state guarantees up to 70 per cent. This amount is extremely small in relation to the demands but the Government's inten-

tion was of indicative value. Upon the effect of favourable experience in this regard, this construction was updated also at the time of the autumn field works in 1992. However, this depicted construction assisting in performing the field works in a campaign-like manner is able only to mitigate the tension of agricultural crediting that became lingering, due to the low profitability. A permanent solution improving the relation between the producers and the banks substantially may be only that where the relations of interestedness of the agriculture and food industry get better, where the provision for internal reserve funds starts and the agricultural economy takes its position in the general appreciation, proportionate to its actual performance. To this, an internal regrouping of revenues is required among the sectors of the national economy or the fact need be taken notice of whereas the agriculture (and the food industry) needs, in lack of the latter, a continuous support, central allowance. As regards the banks, it is not the technique of the solution that is important but that the agriculture be solvent, good debtor.

Against clients being in a bad income position for an extended period, the banks get, of course, into a position that may well have resemblance to a "squirrel wheel" or to the narrowing spiral effect. Even if the resource is available at low cost, no credit may be granted to them as the real crediting loss is high. However, an expensive credit may make the production show a deficit and the debtor cannot repay the credit either. The bank encounters a loss and the process is repeated or changed into having still more unfavourable conditions.

Due to the indicated problems, the amount and share of credits over 1-year term or being explicitly long-term ones have stagnated or diminished, respectively, for the last 3 years. The uncertain, unsettled and uncalculable property-ownership status owing to privatization added to this process (Annex No 2). About one-third of the credit stock is constituted by credits put out in the framework of World Bank projects (Integrated Development Projects). Finally, the agriculture was given a long-term resource of about 1 billion Ft in the framework of inter-governmental and regional credit constructions.

In the framework of the constructions named START Foundation and Foundation for Hungarian Business Development, an amount of below 0.5 billion Ft was received by small agricultural and food economic entrepreneurs.

The MRP (Hungarian Reprivatization Project) is about to be launched. It is difficult to assess how much the credit of strongly limited use, having an interest rate of 17 per cent at present and probably 13 per cent in the near future renders a resource to create a viable business capital.

A greater interest can be observed in the Reorganization Credits allowing to buy out of the assets of farmer's cooperatives being under winding up procedure.

In addition to the aforegoing, the export competition- and capital refilling credits being hard to obtain constitute long-term resources made available by the commercial banks. By the decrease of the investment projects in the large-scale farm sector to 0, the banks' long-term credits based on their own resources were practically ceased.

In the last year, the crediting for large-scale farms and food industrial plants, as well as for individual entrepreneurs being under winding up procedure and bankruptcy proceedings became a particular form of financing (Annex No 3).

2. TASKS RELATING TO REGIONAL FINANCING

2.1 Peculiarities of regions and villages

The rural development was, not to a small extent, determined by the practice developed in the agricultural financing.

Of the country's population of 10.3 million inhabitants, about 4 million people live in villages and a further 1 million people live in small towns of or town-like large villages having less than 10 thousand inhabitants. The average population of the 2930 settlements accommodating half of the total population of Hungary amounts 1700 persons.

The feudal settlement structure that existed till World War II, then the uneven economic and social policy development that have taken place in the recent 50 years have resulted in a great backwardness in property accumulation, in the way of living and in every field of economy, culture and civilization, respectively. Both the small communities, cooperative forms of spontaneous activity and the self-supporting peasant farms, private small-scale industry and retail trade have been eliminated under the pressure of the politics. The farmer's cooperative movement and the migration and the development of shuttle labour have, as a matter of fact, made the erstwhile farmers, traders and craftsmen become wage workers. The process of achieving the bourgeois status resulting in a viable micro-economy and self-reliance has been omitted. The villages are now fully dependent on towns and they are exposed to towns at the same time. As late as in the last 5 years, the other activities and services resulting in variegated business- and personal relations have begun to be established.

Apart from the 140 towns and regional centres, the countryside has become almost the only scene of agricultural production. The problem of financing the agricultural production appears mostly along with the regional problems. To the banking institutes, the agricultural crediting means a greater problem than the financing of other sectors, due to the higher extent of seasonality, to the difficulties in servicing the units

scattered throughout the region, to the temporal congestion of cases that need to be serviced quickly, to the practice of repaying the working capital once in a year, to the lack of the duly qualified and motivated staff, to the comparatively high transaction charges, to the frequent lack of securities, the conflict between unwritten law and written law, to the difficulties in the adherence to contracts. (6)

The price policy exhausted, concentrated a great part of the income generated in the agriculture and, of this, it returned just a very little amount to the villages. Due to the lack, confusion of the trade and services, the income which was left over to the villages by the process of centralization, in form of cooperative wages and of income generated in small-scale production, could not be spent locally either. Therefore, the greater part of this income, too, passed into the towns.

Within the general confusion of the infrastructure, the provision of villages with banking institutes is especially poor.

This did not mean any problem to the large-scale farms and to the major producing and servicing companies of the villages. Based upon the size of their demands for financial services, upon the qualifications of the company management and their skill in finances, they belonged to the clientele of commercial banks. The change in ownership, taking place nowadays is not expected to destroy these relations being mutually favourable.

The atomized agricultural small-scale production - private production affect more than 1 million families on national scale. Most of them also conduct commodity production but to this, apart from a narrow stratum of entrepreneurs, no direct banking institute relation has been developed yet. The production performed without financial services is undoubtedly caused by its small extent and its natural trait but it may as well be imputed to the lack of established banking institutes and to that of services. In every other village, the Post Office constitutes the only "banking institute" which, as banking services, performs only the collection and repayment of deposits.

Nevertheless, the deposits collected here, "went away" from the villages, thus the potential credit resource, generated locally, was used in the towns, in the services, in the industry.

The external financing of agricultural private production of considerable volume are granted mostly not by banking institutes but by the so-called informal credit market. The large-scale farms (farmer's cooperatives, state farms) and other purchasing organizations provided the farmers with commodity credit in kind (fodder, livestock and various production services). The non-integrated small-scale producers perform the production practically only with the use of own resources and with the help of the families of their relatives. Their activity is accompanied, in respect of finances, by the payment in cash, however, frequently even no actual money circulation occurs either.

2.2 Development of a new ownership structure

The new legislation settling the ownership relations opens up, theoretically, the conditions of independent farming, enterprise and those of establishing a new-type livelihood for hundred thousands of rural families. The respective laws are still in the stage of execution, however it can be logically seen that the legal arrangement will not automatically develop an entrepreneurial circle operating the property. On the one hand, the typically modest volume of the acquired property, and, on the other hand, the age, place of residence, occupation of the owners exclude the possibility whereas most of the new owners may as well be entrepreneurs at the same time.

The change in the ownership and the simultaneous transition into market economy involve the intensive automatization of agricultural production and rural economy.

- A part of the village shuttle-workers losing their jobs in town will become full-time private farmers as a solution they are forced to adopt. This is, expected to be so mainly with families where the complementary household farming has been significant so far, too. Ten thousands of farmer's co-

operative members and employees are expected to decide similar to this to whom the transformed cooperative will not be able to give sufficient work to live on.

- In the event of the improvement of the financial conditions of economic management, the transformed farmer's cooperative will start to divide into smaller and smaller units. This process is expected to continue till the staff and size resulting in the actual ownership of the property develop where the issues of interestedness and responsibility will as well be clarified exactly.

- The ownership structure of villages will change in other respects, too. As soon as presently, a welcome increase is taking place in the circle of those who choose another civil occupation: they open various shops, render various services. It is anticipated that more and more family- or joint enterprises, cooperatives will be formed also for the local processing, distributing of agricultural produces. (8)

According to conservative estimates 40 to 50 thousand families are expected to appear within 5 years who will choose an agricultural way of living and who will have to provide for cultivating 5 to 60 ha of land each.

The change in the ownership-, farm- and activity structure significantly modifies the agricultural production and the requirements laid on the banking institutes financing the rural population and enterprises, respectively.

Some remarkable statements and recommendations of the Study recapitulating the World Bank's agro-financing experience gained during 15 to 20 years, in countries having heavily subdivided agricultural production and poor rural infrastructure (6):

- Aspects of allotting the credit: the securities, the timely repayment in the past, the size of landed property, the capital stock, the amount of credit applied for, the position occupied within the community, the strategic considerations, the expenses of managing the credit operation (the latter may be as high as 20 to 42 per cent in the case of small credit amount).

- The information problems existing in the rural credit markets (screening of those applying for credit, keeping track of the utilization of credits, the impossibility of forcing out the conclusion of credit contracts) raise the issue of the suitability of non-village-related financing institutes (state-owned credit allotment organizations, large banks).
- The success of a credit policy aiming at developing the optimum, market-cleaning interest rates depends, to a significant extent, on the expansion, flexibility of the informal credit market.
- The differences between the objectives of the banking institute and its employees may result in the bankruptcy of the credit market (corruption). This so-called managerial problem (i.e. the nature of the institutional arrangements) depends on the information and preference structure of the participating parties.
- Of the attempts made for resolving the problems arisen, the Study recommends two approaches for the Eastern European countries. The one is the approach of linked transactions, the point of which is that the credit operations are linked with transactions performed in other markets, e.g. in the markets of land, labour, produces. The other one is the approach of crediting for groups which, in relation to application for credit by one party, improves the bargaining position against the creditors and, by virtue of size economicalness, reduces the transaction expenses on both sides. The approach of crediting for groups gave favourable experience only in the case of groups consisting of less than 10 to 20 persons, being homogenous in respect of activity or family relation.

The task is two-sided. On the one hand, the village needs a banking institute, and only such an institute can be used as a basis which - in addition to being a real bank - is at the disposal of the village with its employees knowing the locality and the clients and being committed to the village. On the other hand, a clientele need be established, being homogenous in terms of solvency. The point of this is to allow the farmer to obtain, in the village, any information (on production means, product- and money market, technology, law, taxation, etc.) that enables him to manage his activity in respect of economics and finances.

2.3 Issues of lack of resources

Owing to the modest way of living and to the multi-life developed in the countryside, the villagers - apart from the last 2 years - have saved a higher proportion of their income than the families living in towns. (Due to the increased rate of unemployment and to the high-volume elimination of livestock farming, this process has unfortunately become reversed.) However, the amounts saved have been invested in mostly non-mobilizable, "overbuilt" dwelling houses, and the per-capita amount of savings deposits is probably less than in town (about 80 to 85 thousand Ft/person).

The more significant start-up of independent enterprises in the villages will not be possible by way of relying exclusively or mostly on own capital, similar to the situation in this regard in towns. The conditions of the agricultural family enterprise are especially unfavourable on the side of resources. This is caused partly by the considerable need of investment; as for livestock farmers; the high-rate and continuous tying up of current assets in every case; partly by the generally low profitability of production, being explicitly bad at present.

The once-only investment need of a 10 ha family farm based upon a leasehold, wage work by machine and mostly by manual work being incapable for accumulation or hardly capable of that is about 4 to 5 million Ft and a further continuous current assets financing of 1 to 1.5 million Ft is associated. To establish a more up-to-date, 30 ha livestock farm having an own landed property and own machinery an amount of as high as 15 to 20 million Ft is required and, in addition to this, there is a demand for current assets amounting to about 3 to 4 million Ft. It is obvious that the families can provide the conditions of establishment and operation from their own resources in an exceptional case only.

To establish new farms, a considerable amount of credit, granted mainly for a long term, need be made available. Such credits, in a little number, have so far been granted only by large commercial banks at general or preferential interest rates, against acceptable real securities. Nevertheless, the expected abrupt increase in the demands for credits could not be met by the large commercial banks having a thin network,

even if the resource necessary for this would, otherwise, be available.

It will be all the more this way with the short- or medium-term current assets credits providing a continuous liquidity since not only the new farms but the still existing-expanding enterprises will lodge such demands as well. Not less will depend on the development of the conditions of obtaining credit than that there will be any rural privatization or not.

3. BANKING SYSTEM OPERATING ON COOPERATIVE PRINCIPLE

3.1 Position, role of a cooperative bank in the life of the region

In Europe's countries being models for us in both economic and social respects, rural financing is performed mostly by the cooperative banking network. The Raiffeisen, the Credit Agricola, the Förenings Bank, the RABO have achieved a high position in the national, or in some cases, international hierarchy of banks. Some secrets of their 100-year successful activity are, even today, rooted just in their basic principles determining the foundation of the farmer's cooperatives.

The setting up of cooperatives started as a rural, agricultural movement. In the 80s of the last century, the appearance of the cheap American cereals in huge quantities in Europe had resulted in the market loss of small-scale family farms and in their economic frustration in large numbers. The farmers, all over Europe, so in Hungary too, had identified the setting up of cooperatives as being the way out. That time, the first credit cooperatives based upon the principles of mutual aid and reciprocity had been established.

Solidarity in the present cooperative banking institutes is not only an emotional but rather a rational factor, too. An essential peculiarity of the classical arrangement "one village, one local cooperative bank" (see the Netherlands) developed as a result of the hundred years of integral development is that the member-owner is also one of the bank's clients applying for credit. The interest relations here are quite different from those between the owner and client of a commercial bank.

Even the smallest local cooperative bank, as any other banking institute, is most profit-oriented in favour of its owners, against the non-owner clients. Nevertheless the practice "one member - one vote", constituting the main point of the operation of the cooperative form allows the cooperative, by way of a joint decision, to put out credits at preferential interest rate for the members, on account of the dividend or of the interests on deposits or to expand its acti-

vity by non-profit services that result in the improvement of the member-clients' financial position.

The members may decide to grant preferential credits for the young people, beginners or for the activities, services playing an important part in the life of the village communities, interest representations, non-profit activities (from the bank's point of views) which stabilize the material basis of the member-clients, increase their deposits, strengthen the security of credit repayment. With this purpose, in the 1970s, the cooperative banks of Europe founded a great number of subsidiaries, mainly in the field of accounting, consulting and information technique.

The real worth of the possibility of deciding assigned to the community exceeds the financial profit that can be measured in terms of forints. The position of deciding constitutes liberty in forming the image, future of the village. Such liberty of deciding is a precondition of achieving the bourgeois status by the village and, in this context, the local cooperative bank is an instrument of achieving this target.

The advantages (the solidarity, the personal knowledge of the local conditions and of the member-clientele) of the local cooperative banks enforce only till the circles of owners, depositors and credit applicants cover each other well, for an extended period. In Europe, the lower size limit is "one village - one cooperative", whereas the upper size limit is an independent local bank comprising some villages in the surroundings.

In the money market, in the competition for profit, a local bank alone represents an insignificant providedness with capital. This handicap could again be overcome by the cooperative banks by way of collaboration only; they established their joint apex banks. Every cooperative bank in Europe has been transformed into a two- or three-stage banking system in which the individual local banks, also preserving their independence, make use of all benefits of an organized banking institute well provided with capital (Annex No 6).

3.2 The network of savings cooperatives and its potential alternative

In Hungary, the credit cooperative movement had started at the same time as the similar European initiatives and, in a similar manner (rapid growth in the number of members, state support, establishment of a central bank etc.), it had become by the beginning of our century, the only financier of the small- and medium-scale enterprises in the villages, the banks of the rural regions (3).

In 1952, the political power eliminated the operation of the cooperative banking institutes, then, in 1957, permitted it again. However, this newly started, already savings cooperative movement is different from the European practice - had never been granted any state support; in fact, the operations and scope of activity of these banks were substantially restricted by the political power, by way of banking rules.

Now, in Hungary, 258 savings cooperatives operate, owned by 1.8 million members, with 1800 branches and deposit collecting counters, respectively. (Their operation and activity are described in Annex No 7). Their assets and the characteristic figures of their activity as of 31 December 1991 are as follows (4):

general balance amount	106.4 billion Ft
subscribed capital	3.9 billion Ft
deposit stock	72.8 billion Ft
credit stock	41.7 billion Ft

The rate of the savings cooperatives' profit (4.9 per cent in 1990) does not reach the level of that of the commercial banks. This difference, among others, is due to the fact that - because of the interests of members - the cooperative banks maintain their branches even in villages where the financial servicing activity shows a deficit.

About 10 per cent of the savings of the population in Hungary is managed by the savings cooperatives; this deposit stock represents 70 to 75 per cent of the resources of the cooperatives.

85 per cent of the savings cooperatives' credit stock is composed of so-called "credits granted for the population", whereas 10 per cent is composed of credits granted for small-scale and private entrepreneurs. As for the latter, the credits for agricultural purpose constitute a more significant proportion. (4)

Nearly 60 per cent of the members and clients lives in villages where only the savings cooperatives conduct banking, servicing activity.

The savings cooperatives in Hungary have all those advantages which could develop also the European credit cooperative initiatives into a strong banking network being able to complete rural banking institute's tasks. The buildings provided more or less with banking infrastructure, the officials knowing the clients and the locality and committed to the cooperative idea, are given. The two most essential obstacles to development are now the lack of well providedness with capital and of the practice in granting credits for the entrepreneurs.

In December 1991, group of international experts came, during its survey on the rural banker's activity related to retail trade, to a similar conclusion. (5)

In connection with the problems of rural financing, in professional circles, the concept of establishing a new credit cooperative network is under development. It would be the responsibility of the credit cooperatives to provide the small- and medium-scale agricultural enterprises with short- and medium-term credits. As envisaged, the bases of such a network would be the farmer's cooperative centres being vacated, whereas its professional background would be constituted by the agricultural intelligentsia having agricultural-, rural and cooperative knowledge, released from the large-scale farms.

Undoubtedly, this - in itself - reasonable initiative in the field of providing the countryside with banking institutes is still not a real alternative of the savings cooperatives. On the one hand, because it would resolve, of the wide range of financial services, only the agricultural crediting, on the other hand, because the cost of establishing a new network

would be 10 to 20-times as much as the modernization costs of savings cooperatives.

In the practice of the strong cooperative bank already referred to, the crediting for agricultural purpose represents as little as 12 to 20 per cent. This is the very reason for their being able to grant credits for their agricultural clients-members, frequently under more favourable conditions than the general conditions.

Nevertheless, it seems reasonable to involve the agricultural experts, having valuable professional knowledge, in the agro-financing development projects of the savings cooperatives, in the daily practice of financing (in specialist, consultant posts).

Simultaneously with the compilation of our Study, the coordination of the concepts of the concerned ministries and institutions (Ministry of Finance, Ministry of Agriculture, National Bank of Hungary, Banks' Supervisory Board, Bank Federation, National Federation of Savings Cooperatives, Savings Bank) on the establishment of the rural banking network is under way. It seems that the standpoints agree in that a cooperative banking network proved to be successful in Europe and not unknown in Hungary either may be suitable for this purpose. In Hungary, only the savings cooperatives meet this condition, for the time being but any other local self-organized unit, e.g. credit cooperative, farmer's cooperative centre being under transformation, too.

4. DECISION-TREE POINTS OF ESTABLISHING A COOPERATIVE BANKING SYSTEM

4.1 Task of the savings cooperatives

The savings cooperatives are banking institutes, being individually independent legal entities. Their activity is regulated by the Act LXIX of 1991 on the banking institutes and on the activity of the banking institutes as well as the Act I of 1992 on the cooperatives and by the decrees attached to these Acts. Consequently, any concept formulated by any main authority and institute for the establishment of the rural banking network may only be a recommendation for them.

The savings cooperatives, with regard to its providedness with capital, to their scope of activity, to the standard of their services are extremely different from one another, they may be treated as one group due to their organizational form.

According to expert's estimates, as few as 30 to 40 savings cooperatives are able to conduct an independent foreign trade activity in future; as for 130 to 150 cooperatives, elimination or eventual merger can be expected; the operating ability of 60 to 80 savings cooperatives constituting the middle layer can as well be maintained by using some outside support.

The heterogeneity of the group reaches a level that makes the straightforward clarification of the following basic question non-evadable:

- is the adherence to cooperative principles strong enough that the cooperatives assume their transformation into a rural banking network together and only together or

- giving up the basic principle of solidarity, those cooperatives constituting the vanguard will make themselves independent, the middle layer will collaborate and establish its two- or three-stage joint banking system, whereas the 130 to 150 weakest cooperatives will merge into the neighbouring cooperatives and continue to function as their branch offices.

In the latter case, the solidarity, the cooperative feature, may begin to decay not only among the cooperatives but also within the individual cooperatives. Of the cooperatives

having comprised 5 to 7 villages so far, being overdimensioned even now, units extending to 8 to 10 villages would come into existence.

The unfavourable experience gained in the course of the concentration of farmer's cooperatives have proven that the solidarity, readiness for association represented a significant force within a village, in some cases, however, the cohesive force - during the concentration - has diminished at a highly increased rate with the growth in the number of villages; in many villages, this force has reversed.

The clarification of the basic question would be the responsibility of the interest representation, i.e. of the OTSZ (National Federation of Savings Cooperatives). Now, the OTSZ does not seem to undertake to clarify this question.

The management of the OTSZ is fighting with the trouble of legitimation in the storm of the change of regime. This derives partly from the fact that the process of the savings cooperatives' transformation into rural banks has become the scene of the prestige fight of institutions and persons.

The savings cooperatives may undertake to complete the second task only after having considered and decided the basic question correctly; to create a programme by which they may become strong rural banks.

Several concepts have been elaborated (by the OTSZ, Savings Bank, Ministry of Finance, National Bank of Hungary) for the transformation. All of these concepts envisage to establish a network the apex organization of which is the jointly owned central bank to be set up by the savings cooperatives joining this network voluntarily (10), (11). (The basic principles regarded as a model and the description of the organization structure are included by Annex No 6.)

A substantial difference among the concepts is in what position should be given to what institutes in the new rural banking network.

In these concepts, there is no realistic alternative for the savings banks. The only chance of their survival is to join, to whatever extent their independence due to their being cooperatives be curtailed by this.

The possibility of taking an unfair advantage of their defencelessness can well be seen in one of the concepts, in the 8 points enlisted under the heading "The main rights and obligations of the joining savings cooperatives, of which 7 discuss the obligations. (Annex No 11.)

Should the savings cooperatives not adopt a uniform, jointly developed concept, they might soon get into a situation where a few people will decide on their future and instead of them.

The Study (6) of the World Bank, concerning the credit cooperatives, draws the attention to the fact that any aggressive intervention in the life of the cooperatives involves, in most cases, a failure. As a proposal, e.g. on the state's intervention with the intention to help, the Study indicates the fields of training, of the methodological development projects necessary for improving the banking activity and of the information activity serving for strengthening the membership feeling.

The responsibilities of the (so-called) apex bank can be graded, according to international experts, into four groups (a detailed description can be found in the Annex No 9) (5):

1. general coordination
2. financial centralization and commercial activity
3. supporting the regional and local banks
4. diversification of the activities by way of establishing joint subsidiaries.

A detailed and accurate description on the responsibilities of the apex bank, also suitable for consideration and analysing can be found in none of the concepts (as an example, another description can be read in Annex No 8). A still greater uncertainty concerning the description on the legal and financial relations between the apex bank and its prospective owners, i.e. the savings banks. All elaborators of this concept seem to lay the emphasis on the setting up of the institutional system, instead of stressing the "task and its accomplishment". For the savings cooperatives, it might entail consequences that are difficult to foresee if they would decide without knowing the rights and obligations, the tasks and the ways of their accomplishment and without knowing the expected results, respectively.

A similar mistake had once been made by the savings cooperatives at the time of establishing the Savings Bank. Now, though they have the majority ownership share, they have no voice in the operation of their Bank, with their deposits tied up compulsorily. The Savings Bank has not become a winner either, since it could not get the upper hand of the savings co-operatives; in practice, a stalemate situation has developed.

There is now an imperative need of resolving the problems of rural financing, already by all those concerned; practically, there is no alternative of establishing a rural banking network other than the savings cooperatives. In this light, the savings cooperatives occupy a good bargaining position today. By the exact formulation of their aims and conditions, they may be active participants in making decisions determining their own future and the rural future for an extended period of time, and not only those suffering from such decisions.

4.2 Assumption of tasks by the state

The rural development, the rural entrepreneurs' obtaining appropriate resources could be accomplished in no country in Europe, without the state's initiating, supporting attitude.

(1), (5) Due to the unprecedented load imposed on the agriculture and on the villages, in Hungary, this is not possible at all.

The World Bank Study (6) cited previously analyses the various methods of the intervention by the state in the agricultural credit markets and their success, in a detailed manner. Some remarkable statements are given herebelow:

- The intervention by the state manifested itself in granting credits at a favourable interest rate and in organizing and setting up of banking institutes conducting credit collection in rural regions and coordinating same.
- The subsidized credit fosters corruption, the flight of capital, the improductive investment projects, and at the same time it does not stimulate for savings, thus, finally, the result is not that what the Government wanted to achieve by granting preference.

- However, an interest rate higher than the market-clearing interest rate increases the moral risk (forcing the credit utilizers to enter into more risky investment projects promising, nevertheless a higher yield) and the counter-selection (increasing the share of those credit utilizers who are willing to assume risk) thereby considerably deteriorating the creditor's portfolio in respect of risk composition.
- For the rural financing banking institutes, it is especially important that their own crediting strategy be based upon a continuous methodological development.
- "First of all, we have to make an end of the misbelief whereas the intervention by the Government in the credit markets induces a growth even if the adequate infrastructure, the organizational knowledge, the favourable agricultural basis are missing. Second: we know just very little about what is still necessary for that the institutional credit project be a success, in addition to the reasonable business management, to the designing of appropriate corrective incentive mechanism, to the definite rules of execution, to the regular report required from the institutes. There are several factors that exceed the market explanations, to the scope of culture, sociology, attitude research projects ...

These features, often called as secondary explanatory factors, are much more important in our case than that we only use them in explaining the remainder values."

Based upon the analysis of the three decades' experience, the following lesson is indicated as most important for the Eastern European countries:

- "It seems that - with regard to the difference between the social and private yields, the intervention by the Government is theoretically necessary. However, the necessity is not yet enough to effectuate intervention; adequate will and ability are also necessary for achieving the intervention targets. The failure of state intervention, at least of that kind we have encountered for the recent decades, speaks against such intervention. Nevertheless, if we regard the credit as an essential element of agricultural development and of a better income distribution, we have to insist on the institutional reform, i.e. on that only banking institutes may implement granting which have adequate incentive structures, keeping track of the utilization of the credit in a credible manner, and on that the socio-economic environment should not indulge the arbitrary actions and the corruption."

The sound start-up and the operation of the private sector can only be achieved by the coordinated operation of the Government, of the competent ministries and of the apex organizations of the budgetary and financial system (National Bank of Hungary, Banks' Supervisory Board, Bank Federation) respectively.

The most important tasks and responsibilities are as follows:

a/ The possibility of crediting for mortgage on landed property need be resolved from state resource. For landed properties encumbered with a mortgage, resource coverage could be given, at the outset, by central bank credits granted at low interest rate and by other cheap resources (e.g. state reserve funds, notarial deposits etc.), while, later on by the sold mortgage-bonds. Namely, the long-term development project credits of low interest rate may usually not be granted by cooperative- or commercial banks.

b/ It is necessary to initiate and organize the process of transforming the savings cooperatives into strong, rural banks and into a strong banking network as the development "initiated from below" alone cannot produce good results.

c/ The resources that can be involved are poor and this fact necessitates the reasonable concentration of resources. Therefore, if the cooperatives, financial apex organizations as well as the concerned competent ministries have once developed a mutually acceptable concept, so systematic efforts have to be made for its implementation. The systematization of resources amplifies the positive mutual effect.

d/ The capital stock of the cooperatives need be increased by allotting funds to them in order that the developing banking network can meet the prescriptions of the Act on banking institutes, the demands for and the conditions of crediting, respectively. Its amount may be 4 to 8 billion forints, eventually in two or more stages.

e/ One of the basic conditions to the normal operation of the banking network is the establishment and operation of a uniform banking infrastructure. This, on the one hand, means a considerable once-only investment project then a smaller continuous expense for operation and development. It is reasonable that the budget (eventually from the resource of international aid projects) contributes to the implementation of the basic investment project.

f/ The income security of the agriculture and that of other rural enterprises are little and this is not necessarily the consequence of the entrepreneurs' attitude. Therefore, the state has to assume a guarantee for the credits made available. This can most reasonably be done by establishing guarantee funds and by enforcing the guarantee on account thereof.

g/ The production-political priorities appear necessarily, in compliance with the current demands of the economy. These can efficiently be enforced, by using financial means, so that such priorities are transmitted by the network to the entrepreneurs, in form of supported credits or of real supports. The credit allowance may, of course, be granted not only to the network but also to the commercial banks showing interest in target crediting.

h/ The risk of crediting is reduced to a great extent and the provision of the Government and of the financial apex organizations with correct information are significantly improved by the development and operation of the consulting service. The banking network wants to (can) pay presumably only for that information service that can be used by it directly. Therefore, the share of the consulting expenses not paid by the banks need be financed by the state.

i/ The bank's interest in a crediting at more risk than the average may be increased if they are granted tax allowance. It would be reasonable if their activity would become exempt from taxation to an extent they conduct agricultural crediting ope-

rations. It would also be a good solution if the amounts generated this way could only be used in raising the capital stock or for self-allowance purposes.

4.3 Regulatory and supervisory tasks

The savings cooperatives, if they undertake the function "rural bank", face a double task. They have to comply with the prescriptions of the Act on banking institutes (and with the related provisions) and their professional qualifications have to reach a level that allows them to act in the money- and capital market steadily.

Should the savings cooperatives decide to establish an apex bank and to adopt its concept, so the Act on banking institutes has to be amended. Within § 5 the apex (umbrella) bank need be defined as banking institute, furthermore, the recommendation of the Council of European Communities (Annex No 10) should be enacted whereas "the credit institutes connected permanently to the apex organization shall be released, among others from the provisions related to own funds." (5)

According to estimates, half (50 to 60 per cent) of the savings cooperatives cannot meet the requirements of the law and of the market even if the apex bank concept would be implemented successfully; they will either be merged or wound up. This process should by all means be avoided as hundreds of further villages will become villages without "own bank", not provided with any banking institute (the disadvantages of this have been mentioned previously herein).

In search for the solution of the problem, the demand for amending the Act on banking institutes arises mostly in the circle of weak savings cooperatives that, nevertheless, insist on preserving their independence. The problems arise in respect of the size of subscribed capital and of the rules of the banking institutes' safe operation. Also, the demands for amendment aim, in general, at these paragraphs, asking for a positive discrimination in favour of the savings cooperatives.

Yet, this is not the real solution. The compliance with a softer legal prescription does not provide the improvement of the money- and capital market position; it does not attract new members, depositors, clients.

It is not the law that need be adjusted to a weak position but the savings cooperatives have to be put in a position to meet the prescriptions of the law. They have to be provided with all those professional, methodological, informational, technical etc. facilities the large commercial banks have.

The "compensation" for the 35 years old regulation having been discriminative to the savings cooperatives could be such a programme for diminishing handicaps of this kind.

For the savings cooperatives, due to their high rate of heterogeneity, an alignment project would, by all means, result in an improvement of facilities, however to an individually different extent. This process would establish the stages of activity and decision complying with the facilities, both among the savings cooperatives and within them (e.g. deposit collecting counter - branch office - directorate).

The Act on banking institutes knows and manages the initiatives of banking institutes provided with facilities over the basic level, aiming at conducting an activity of higher level, referring them to the sphere of authority of the Banks' Supervisory Board. /§ 37 (1), (2)/. However, as for savings cooperatives weaker than the basic level, it might be necessary - practically, also within the sphere of authority of the Banks' Supervisory Board - to reduce the operations, based upon considering the guaranteeing capital and the personal and material facilities, respectively. Thus, even if with a significantly less liberty of decision, the village may continue to have its "own bank".

Should the project promoting the improvement of facilities not be a once-only intervention (e.g. putting out of computers) but being available continuously, at a level and in a pace complying with the receiving ability, so the opportunity

will be provided to each savings cooperative, that intends to remain independent and that is willing to also make effort for this, for complying, at last, with the strict prescriptions of the Act on banking institutes, by reaching higher and higher decision levels and becoming actually stronger and stronger. This, of course, may require different lengths of time, depending on the starting level. According to estimates, the joining savings cooperatives would need a grace period of about 2 to 5 years to achieve that, depending on the economic situation of the given region.

The possibility of a moratorium associated with the accomplishment of subscribed capital is provided by the Act on banking institutes, under § 22, sections (2), (4).

Of the rules related to safe operation, the performing ability concerning the index "sufficiency of capital" is - as per the standpoint of the Bank Federation - uncertain even in the case of large commercial banks. To their view, the solution requires a significant state action - also affecting the budget - and a longer or shorter grace period. (9) The savings cooperatives would need only the latter so as to provide sufficient capital.

The index "capital sufficiency" of 8 per cent take effect in the European banking security regulation in 1992, based upon the recommendations of Basel. The banks operating in the countries of the European Community have, in the course of their one-decade development, reached the level where the 8 per cent rate could be made a general norm. In Hungary, the Act on banking institutes granted just a little more than a two-year grace period and, in addition, the commercial banks founded in 1987 also inherited, from the National Bank of Hungary, a considerable portfolio of credits not repaid yet. These are expected to be settled still before the privatization of the banks or linked therewith.

5. DEVELOPMENT CONCEPT OF ESTABLISHING AN UP-TO-DATE NETWORK OF COUNTRY BANKS

5.1 Scheme and its main point

After World War II, Western Europe regrouped revenues in favour of the villages, in order to preserve the way of labour and living there, and to launch the rural development. One of the first concrete measures of the German reunification was the location of containerized branches and data telephone exchanges in the villages, for rearranging the financial processes. Hungary, in this field, seems to have lost her common sense in respect of practical steps. The half of the population lives in villages but they do not receive any practical assistance to their enterprises and to their farming activity, apart from the theoretical-legal possibility of obtaining landed property. In fact, they are unscrupulously exposed to the property- and post allotting effect of the state- and spontaneous privatization.

The environmental conditions, asserted so many times, necessary for independent farming, creation of livelihood, acquirement of property are becoming worse and worse. The diminished purchasing power, the financial policy, the communication monopoly all act against the evolvement of a business-based financial infrastructure; instead of processes supported by the state, the situation today is featured by promises, statements, budget funds running to waste.

Despite all these circumstances, a solution exists even today, however, this is not a simple crediting construction or the establishment of a bank, relying upon the promises of our existing institutes but an intervention of servicing character being simultaneous and supported by state- and non-state funds, affecting the whole environment of rural farms, new cooperatives which would create a harmony among these farms and creditors, consultants and information systems, relying on interests and provide their simultaneous operation.

The material-legal conditions of farming, the information of good quality, the marketability, the large number of solvent farmers, the standardized method of crediting, the clearness of activities are simultaneously necessary so that the rural farms come into motion.

The condition to becoming solvent is the farmer's accounting, as an elementary business accounting of family farms and small-scale farms. The farmer, in the simplest case: at home, keeps his accounts in a booklet of form type, with the help of a local advisor, at the outset. The advisors already follow the accounting of farmers associated with them, by using a computer. The advisor also renders assistance to decisions and calculations, he gives the farmer advices in respect of operation, investment, law, taxation etc. for which he can obtain background data from the computer, from the data base of the methodological centre. Thus, the advisor reasonably maintains continuous relations with 15 to 20 farmers and he organizes their participation in keeping the farmer's accounts and helps their being organized in joint utilization of credits, procurement, sales. The advisor may be assisted by a qualified administrative person in the regular entering of data into the computer, based upon manually kept accounts.

Those whose farming activity can be measured and is at good level can be financed by the local bank, thus, the local savings return in-situ, to the rural farmers, in a shorter way. The local bank is practically the savings cooperative branch of the given region, the credit granting ability of which need be improved e.g. as to allow it, as a member of a national network, to apply uniform rules in its procedure.

The savings cooperative to which the respective branch belongs will preserve its independence, it follows the uniform procedure only in respect of services associated with the local terminal. This uniform character may be more and more expanded, if required, thus, finally, the local banking institutes will be harmonized in terms of their methodology but this is not a compulsion, it is just an option with manifold advantages.

The terminals located in the savings cooperative units would connect the branches not only to the local centre but also to a national network. The closed-chain transmission facility independent from the telephone- or data network of the MATÁV (Hungarian Telecommunication Co. Ltd.) allows signal transmission of data-sound-picture simultaneously from point to point or, of course, from one point to several points. Thereby, our villages may obtain a communication facility of world standard.

The national network can be erected in a few months, by performing a nearly simultaneous installation work at all location sites, at a surprisingly low cost. The network would allow the collection of non-named data of the farmer's accounting, on national scale, then - after optional processing thereof - their return; and all this - automatically, at low cost, with daily-weekly operativity. The automatism of transmission will warrant the quality, consequently it can lay the foundation of the evaluation of granting credits, locally.

This network would also assist the advisors in their activity, in a variegated manner, as they can establish a contact with any research-training basis of the country. On the one hand, the network is able to provide the advisors with true-to-life data, and, on the other hand, their valuable professional knowledge may be spread at a low cost and recalled as required. Consequently, the information network, with its gradually developing services, adjusted to the demands of local farmers, might provide valuable data, not only in financial but also in professional terms.

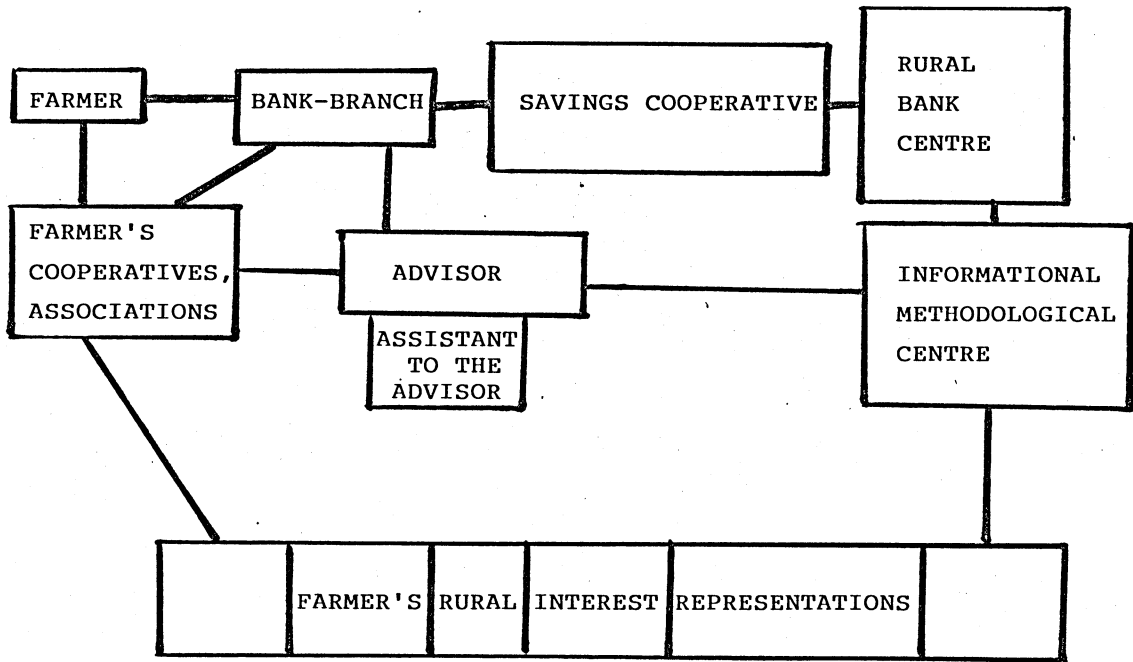
The centre of the network would be a methodological development institute that might conduct processing and development in respect of banking operations, evaluation of granting credits, management, law, projection, i.e. it might provide the local banks, branches with the best facilities. It is a great advantage that, owing to the considerable number of the latter, all this can be performed at low cost, rapidly and in a practical way, adjusted to the local conditions.

This methodological centre might provide the state administration and the professional federations with information, as well, relying on the data supplied by the partner farms. By collecting their demands, proposals, they might make the agricultural administration (agro-industrial regime) functional. More advanced farms might require a terminal by themselves through which they would have access to domestic and foreign data bases alike.

The methodological network would assist, in its operation, the background banking institute assuming the role of the apex bank. The apex banking institute performing refinancing, clearing, guarantee allotting may rely on the resources of the network. Thus, the demand for state preference resources will decrease, the utilization will be reasonable and controllable.

The money, the credit, by themselves, constitute information, too. Consequently, a well-functioning integrated system serves simultaneously the farmer, the bank, the advisor, the interest representations, the training personnel, the research workers, the state-owned institutions. This is the main point and the strong point of the concept.

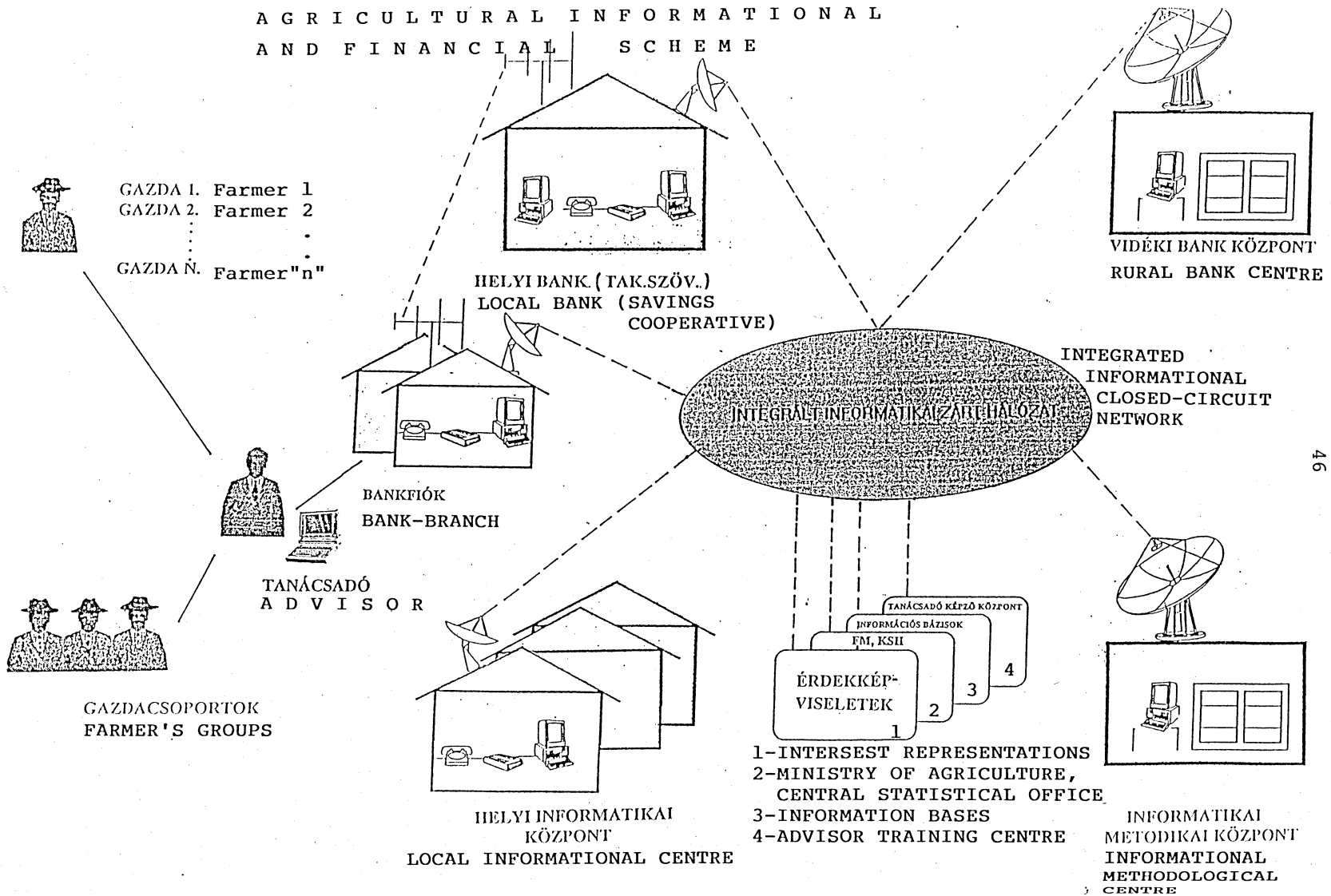
The farmer would obtain services, credits, therefore he voluntarily keeps accounts by which he supplies market data. These, after having been processed and returned, would support the local activity but they may as well be sold processed on national scale. The local and general interests would coincide. Thus, financing is possible already, too, as mostly good decisions. The system-members are developing from day to day, on both sides of the bank counter.



CONNECTION DIAGRAM OF THE R U R A L P R O J E C T

AGRÁR INFORMÁCIÓS ÉS PÉNZÜGYI RENDSZER

AGRICULTURAL INFORMATIONAL AND FINANCIAL SCHEME



5.2 Major elements and participants in the financial infrastructure of regional revitalization

5.2.1 Making farmers credit-solvent

Our democracy has, in the recent two years, made active rural population not solvent but still more insecure. The rural families being not well-informed, having no property, being in desperate straits for local or general reasons, do not know how to obtain the land promised to them, what to produce, by what and how they begin to become independent. They have no real, acceptable credit; those still undertaking to produce are awaited by the traps of usurers, sublet producers. The purchasing, processing units take an advantage of the more favourable position to an extent that the farmer's income does not even cover the production costs. Thus, the obtainment of a landed property, the transformation of the farmer's cooperative, the de-merger are not attractive. A land having a size that equals to the territory of an average-size Hungarian county lies fallow, the villages do not develop; living from hand to mouth is in prospect.

Still, there is a way out. In every village, there are initiating, optimistic individuals. They have to be supported, made solvent, by way of the crediting construction based upon farmer's accounting. The farmer may be an individual, a family but also a group of farmers which have been organized for a specific purpose. These groups might be composed of only those utilizing ad hoc production credit, relying on a joint contract and who also warrant each other but they might as well be those to whom credits are granted regularly and who are grouped around an advisor. These latter ones are already of cooperative character, whether they are new units or those de-merged from the old cooperative.

The farmer's accounting is also suitable for the business recording of the so-called "multi-legged" farms conducting several activities at a time. Therefore, the prospective partners, the individual or grouped farmers may cultivate not only

the agricultural branches interpreted in a narrow sense but they may as well be local processors, traders, servicing ones, at the same time. Consequently, the active rural population by obtaining multi-directional services, may get a new resource independent from the supporting institutes, thereby its chance of becoming independent would grow.

5.2.2 Farmer's accounting

The recognition of the aforementioned opportunity would make the keeping of accounts not a compulsion but own interest. This accounting, with its 4000 kinds of observable data renders an account of the farmer's activity on business basis. The data may not only be figures but also worded information. This accounting scheme would also manage the producing-servicing, trading, in fact, the household plot activities, too. It renders an account of the costs, incomes, of the profitability of the activities, broken down to details as required in professional and time terms but it also follows the consumption of the family and the development of the property of the farm or of the individual and makes the individual's living standard monitorable. Thus, of course, pre- and post-calculations may be made, the required date of the expense, the pace of revenues can be identified, the change in the property can be monitored.

The data that may be obtained from the farmer's accounting can be protected by using codes. The information may be separated by way of processing with statistical character, depending on whether they concern only the family, only the creditors, only the advisors or interest representations etc.

The frame of farmer's accounting has already been prepared in form of a printed booklet but the form of the software suitable for use in large networks is available as well. The basic software units adjusted to the users will assist the farmer or the credit evaluator disliking the data sheets.

The farmer's accounting combined with other software units can be used in risk analysis, cash-flow calculation of

groups, filling out tax returns etc. The farmer's accounting combined with the land register will render possibility for the manifold analysis of activities. All this, with the possibility of comparing it with the macro-economy would become a national worth, therefore it might supply data to e.g. the large information system of the Ministry of Agriculture.

5.2.3 Advisors

The advisor is a participant in the system who answers the questions of 15 to 20 other farmers which might arise during application, he organizes the local farmers to join the system, however, he belongs to the methodological centre in respect of organization structure. It helps personify the relation between the local branch and the farmers by rendering assistance partly in the family- and labour environment of the farmer, partly by resolving the eventual doubts of the creditor. Consequently the advisor is the local personifier of the relation between the farmer and the official operating the data terminal.

His individuality, his own exemplary conduct and prestige are very important, therefore reasonably, he is a farmer, too. For this reason, it is to be considered whether his activity be supported by an "assistant" who regularly collects the protected data of the farmers to the branch terminal, answers the formal questions arising in connection with keeping farmer's accounts.

The local advisors would be connected to the other large national consulting systems and anyone being the member of such a network might as well assume this task if he is a local inhabitant. Thus, the consulting programmes of different origin may coincide in one person.

It is absolutely important that the practical applications, crediting experience be recycled through the advisors into the system, for systematic processing since this is by what the network becomes quick to learn and to adjust itself to the demands.

An advisor might assist 15 to 20 farmers but the realistic figures - being different by regions, villages - will be decided by the practice. The remuneration of the advisor is reasonable to be effectuated by individual farmers and later, in proportion to the turnover; it could be accounted in the line of transaction costs. With regard to the significantly increased crediting security, to the improving insurance conditions, the return of expenditure is possible through the decreasing level of interest rate and preference.

5.2.4 The savings cooperative as local bank and branch

Today, when the revaluation of local small- and medium-scale farms is an important socio-political issue, the local savings cooperatives may as well be regarded as those belonging to this scope. Their preservation, their operation as per future demands need be supported. It is important for the rural population and for the farmers that the banking institute they maintain relations with are theirs. Therefore the concentration, the organizing into a "commercial bank", the reduction of the number of savings cooperatives (the result of the former amalgamations of farmer's cooperatives is an awful warning) are not reasonable.

First of all, the functioning ability of the savings cooperatives need be improved. The most essential initial step of this is to obtain up-to-date communication facility and, thereby, methodological assistance. The number of uniform servicing forms might continuously be expanded later. This way, by continuous transformation, they might preserve their independence and by background support of Western standard, they might learn business financing.

Accordingly, it is about the procurement of a rational service package which might start with the well-established crediting for farmers keeping (starting to keep) farmer's accounts by way of experiment. Several field- and livestock

farming branches render an opportunity for that, as early as in 1993.

The communication terminals to be installed in the savings cooperative branch would interconnect the branch and their own centre, as well as the national methodological or banking centre, respectively. Thus, putting the banking function into operation might be very rapid and wide range. The saving cooperative branches are, in terms of their location, identical with the stationary terminal points of data processing. This way, the contact with the advisors, farmers is of daily, weekly frequency and this makes the judgement of persons and activities from banking point of view highly secure.

The economic restoration of the shattered savings cooperatives (lost interbank deposits) and their integration in this system may take place simultaneously. We do not discuss here the required raise of capital since this greatly depend on the extent of the apex bank's assumption of functions.

Instead of the former coercive central measures, business-based services need be rendered, on favourable terms to the savings cooperatives intending to become a local banking institute, furthermore the solvency of farmers constituting their natural clientele need be assisted. Thus, the well-known problem of the savings cooperatives will be mitigated. They do not need to search for their prosperity in an alien commercial bank in town but they can securely increase their local investments. To launch this process they have to get an initial experience of success. They can acquire this by way of a crediting relying upon an integrated network informatics, assisted by methodological support which they grant to farmers having a judgeable administration.

The recipients of the system may involve the farmer's associations, farmer's cooperative headquarters etc. too. The savings cooperatives are natural but not exclusive entities.

The arrangement of rural revitalization aims at catalyzing the process of organization into a local independent bank,

however, without intervening too much in the spontaneous organization process. It is essential that the rendering of uniform services be realized as a common interest and introduced rapidly and widely.

5.2.5 Communication network

Due to our well-known backwardness, the up-to-date techniques are being fetishized. The application of the integrated transmission technique in our villages imply no unresolvable difficulty at all. At the same time, there is no time to wait for the MATÁV's development programme of different priority and, to adjust oneself, within that to the given facilities. A closed-circuit system need be established, constituting simply the location of antennas on the roofs or in the gardens of local branches. These antennas are capable of reaching the satellites. Thus, our villages may acquire a nearly unlimited communication facility for a price of somewhat less than 1 million Ft per location.

There is no legal obstacle to effecting two-directional data-sound-picture transmission via satellite (however, the usage of VHF is only possible after the respective legislation). Therefore, the network could be established even today.

In the centre of the communication network, the data traffic is organized behind a larger antenna, as well as the automatic establishment of contacts. Attached to this centre, or irrespective thereof, one or more data processing computers may be located at universities, research bases and other institutes. Owing to the technical facilities of the network, the location of the computers is indifferent from operational point of view.

The local terminals also allow sound contacts (conference, discussion) among any number of locations, in fact, in the Budapest Office of the elaborators of this system, picture transmission operates as well, i.e. two (later on more) co-negotiators can see one another by way of monitors and, meanwhile, data and sound are transmitted too. This technical standard, at once

will make the branches attractive in their environments. About the cost, for the sake of comparison: in the Ybl Bank, the savings cooperatives had a loss more than it would be required to establish the system in a country region.

This communication system allows the most up-to-date electronic correspondence, software transmission, invoicing, fax, financial clearing etc. to appear as a service simultaneously with the location of the system. The related facility can be purchased today and it can be introduced even under our existing conditions as well.

The detailed techno-economic condition of the system is available to the Mentor elaborating the farmer's accounting scheme, it can be seen in the Mentor's offices. Also the business plan is ready for financing by not only state funds.

The network provided with these functions, with regard to its rate of preparedness, can be put into operation within half a year (by installing the facilities in one branch a day, in 4 to 5 regions).

The putting into operation of the network implies a greater risk than not doing so as this investment project falls within the utilization fault range of the amount of 40 to 50 billion Ft decided to be given to the agriculture as support in the next year. At the same time, we - at once - obtain a facility of European standard for receiving the banking techniques, for resolving the problems related to agro-industrial (regime!) and to other administration issues, for the political negotiations etc. If we consider the chance of faulty decision by the administration alone, the size of the social surplus yield is at once sensible. A part of this may be assigned to be guarantee coverage for the investment project related to this system and as an admission support for the farmers, savings cooperatives joining the system but the establishment is feasible on business-base as well.

It is, however, to be feared that neither the Ministry of Agriculture, the Ministry of Finance, nor the political power have learnt the open cooperation with those conducting business

activity, therefore, they want to satisfy the recognized demand themselves, at a lower standard for a higher amount, more slowly, with more operational troubles, in a strict manner hardly suitable for correcting the faults. The failures of this process in the third world are well recapitulated by the World Bank study already referred to. (6)

5.2.6 Methodology centre

The data traffic of the network need be coordinated. This is a computer-aided monitoring system allowing automatic night-time data transmission in one bulk or the one- or multilateral deviation during the work. It organizes relations horizontally and vertically. It enables all this traffic only by way of hierarchic entitlements and access concessions, respectively. It is able to protect the data as the basis of the most secure money transfer system is constituted by the data transmission via satellite.

The methodological centre organizes the data processing procedures which can be performed in any computer connected to the system. Thus, the individual university-research institute capacities may be utilized, the specialization may commence. Thereby, the state consulting system may obtain support as well i.e. a cooperation may develop as required.

The centre, by adapting, testing and introducing banking techniques in Hungary and by correcting the fault, accelerates and standardizes the operation of rural branches, banks. Its utilization is not compulsory but the services directly attached to the terminal are uniform; their assisting the development anticipates joining based on interest.

The main reason for the farmers' defencelessness is their poor business management ability. By their joining the system they may get a nationally uniform but subject-specific support for improving their deciding ability, for their financial, legal security. As to the integrators being now in a superior position, the balance may be re-established within one or two years.

The methodological and information organizing background helps, in fact, forces the so-called horizontal relations. Thus, the system members may be given a business information framework which they themselves fill in and operate, without any substantial intervention. It is known how circumstantial the data maintenance is in such business records. The farmer's accounting may assist also in respect of this as the knowledge of the activities makes the market identifiable; no extra data need be entered in the system. By reducing the transmission data a single message may appear on any number of terminals - taking special care of avoiding the inflation effect caused by the too much information, of the specific access, of documented reception etc.

The methodological centre, of course, keeps relations with the apex bank, too, serving its professional needs.

In legal terms, the network and the methodological centre may as well be independent from the savings cooperative, from users. However, for the sake of stronger engagement, it is still more favourable if it is owned by them. Based upon theoretical and practical considerations, it is advisable if the partner farms become owners not in an individual manner but by way of their interest representations. In the event of the division of ownership, the financing of establishment saves money for the budget, or any budgetary source of any extent may be treated as a support granted to the interest representations, respectively.

The communication network and the processing facility allow the operation of separated, closed-circuit networks in a relationship as co-payer of overhead costs. Thus, even on national scale, a considerable organization expense and time can be saved. Thereby, the operation will be cheaper to each participant, therefore the other communication demands of the villages may be based on this network. Should it be the rural banking network that takes the first step of this kind, a several-times return can be expected on the investment.

5.2.7 Central bank

Should it be the organization of constructing from below and that of servicing that are of priority, so more time and more thorough possibility of consideration is available for setting up the background bank. The local banking institutes rendering actual services may become actual owners of the bank to be set up in their favour. Through them, the farmers will also become owners (in their capacity as owners of the savings cooperatives, credit cooperatives). This process need be elaborated in details, parallel to organizing the servicing network. In this regard, the Mentor has a financial schedule.

The arrangement related to the commercial bank function of the apex bank and to its background servicing feature do not seem favourable. The example of the Savings Bank shows that the short-term interest (selfish generation of profit) acts against the services. Only a clear, interest-owner structure can anticipate a solution allowing further development. The apex bank may not appear in the market as the competitor of its own protected members, it may not acquire any profit from its members, on account of its members. Nevertheless, it may complete the clearing and refinancing functions, it may assist, by organizing internal syndicate, by assuming larger business in the co-financing implemented with the members, also it may make decisions with the involvement of the members but only in the interest of members interested in the regional market.

It may well utilize its large bank trait "outward", in favour of the member-cooperatives, if the members get entitlements through it which, otherwise, would be possible in the case of a larger commercial bank or banks. This apex bank may maintain relations with the National Bank of Hungary, with the Banks' Supervisory Board, with the Hitelgarancia Rt (Credit Guarantee Co. Ltd.) and also this apex bank may conclude co-operation contracts with commercial banks in which the individual savings cooperatives and commercial banks may, if they so require be involved as common co-financiers. Thus the local

knowledge and the other kind of the large commercial bank's ability may advantageously meet each other, without any discrimination as to size.

The central or apex bank is able to supervise the utilization of state preferences and of agricultural supports in the crediting practice of its members and it can be a responsible negotiating partner of state institutes. The numerous small local banks, credit- or savings cooperatives may, this way have access to all those preferences which have so far been granted to commercial banks only, since the communication network anticipates a correct management of the affairs.

Of the annual amount of the financial preference granted to the agriculture, the part that has not been used in favour of the producers (as it was taken away from the farms by the strong purchasers, integrators, processors) would alone be sufficient for the whole capital demand and operating expenses of this apex bank. The calculation can be done for 1993 concretely; the above statement can be verified!

5.3 Some remarks, set-up

The chance and strength of implementation is in that not a member of the institutional system begin to develop the structure (as per the former practice) but a project team specialized for this.

A well-known way of western development is that it is not the state that resolves the tasks by its own employees but it concludes an implementation contract with one of the participants of the business life which is most suitable for this purpose. Thus, an entirely independent project (investment) team will be set up which will concentrate on this task only, the members of which will work on the basis of a lattice chart, making the time and cost data identifiable.

The complex projects are organized under one project management, with the involvement of participants specialized for a definite purpose. An existing institute is never suitable for that.

The farmer's accounting scheme is ready, its practical tests are under way, its network-targeted software version will be functional by mid-January 1993. At the same time a revised booklet and screen forms, also allowing for experience, will be produced. A quarter of a year later, the land register- and credit evaluation blocks will be available too.

The consultants employed by the Mentor direct, at present, practical application programmes at more than ten locations in the country and their experience is favourable. Its number can be expanded at any time; to this, experts of excellent capabilities are available.

In the organization and launching of the experimental programme the savings cooperatives have even so far assumed a great role. To their experience, the cooperation with several thousands of farmers may be expanded within two years. Still before or during setting up the network, the application of the farmer's accounting scheme and the consulting may commence in the target villages.

The Mentor, committed to the cause, has prepared the major modules of the scheme for arrangement, using its own resources without any state support, with the chance of the rapid development of a network. It established the engineering-servicing firm, two years ago, which is suitable for the setting up and operation of the communication network. It has appropriate licences and references. Nowadays, the PC-based video transmission technique is unique all over the world; even large communication companies do not have such a technique that provides two computers with the facility of holding a video conference, by building in only one card. This cheap and simple technique will become a publicity used videophone.

The facility of transmitting data-sound-picture via a Mentor satellite promotes the immediate use of the usable services of the large international networks. This facility will shorten the development period by years. It will enable the immediate application of e.g. the clearing, whereas the establishment of the giro centre has been under way for as long as two years.

The communication terminals can be set up at optional locations, simultaneously, therefore, the central computer and the network can be launched within half a year, at as many as 200 locations. They can be put into operation at 50 to 60 locations, as pilot ones, within four months.

The technical reliability of data transmission via satellite is higher than by conventional cable; much better and cheaper than the domestic telephone connection. In case the task of installation would be assigned to the savings cooperative, most of the computer-technical means can be applied further on, as well. The communication network and the methodological centre can as well be financed on business basis, by concluding contracts with those joining the system, on commodity supply guaranteed in advance.

The reasonable way of implementation is that the Mentor which has invested intellectual capacity and several years of preparatory work, undertakes the installation in a way that, at the outset, it exercises the ownership rights but it will gradually pass on the major share of such rights with the admission of the system-members. This is the way that anticipates the shortest time and the lowest cost.

The termination of rural defencelessness, the elimination of its backwardness by decades are in our elementary national interest. To our present knowledge, the rapidest, most successful solution to that can be granted by the up-to-date, budget-saving programme described hereabove.

In the course of our work, we have made use of the Mentor's proposals and solution constructions of business worth for which we hereby express our thank.

The Mentor has informed us whereas it intends to reserve its rights concerning the prepared farmer's accounting scheme consulting or credit organizing activity based upon the farmer's accounting scheme, the integrated market- and financial information network coming into existence by using the data resulting from the farmer's accounting, as well as the business construction related to the methodological centre being organized in connection with the mentioned network therefore in case of any related publication the Mentor insists on publishing this origin and the reservation of its right.

Recapitulative statements

- The financing of agricultural private production by the banks ceased after World War II. All source-generating institutes, that had functioned well formerly, were gradually reduced and ceased. The role of granting short-term credits was assumed, partially by the large-scale farms beginning to cooperate with the small-scale farms.

- Due to the decrease, then cease of the income content of food production, the provision of also the large-scale agriculture with credits has become questionable in the last 3 years. Due to the decrease of property, a growing proportion of credits laid out has become uncovered and this causes an about 10 billion Ft loss for the commercial banks participating in the financing. Nowadays, crediting is necessarily limited to financing the work in progress. As for the banks, their attitude still being reserved, even considering the above fact, anticipates the protraction and the non-desired distortions of the change in the agricultural ownership, respectively.

- The small-scale agricultural production affects, on national scale, more than 1 million families and most of them are performing commodity production as well. Nevertheless, apart from a narrow entrepreneurial stratum, no direct banking institute has developed for this activity. At the same time the development of independent family farms which strengthens the bourgeois civilization, the rural middle-class cannot be conceived without wide-range financial services. This is not enabled by the poor network of the commercial banks, limited mostly to towns.

- Instead of financing institutes alien to the villages and situated physically far from them, a "human-scale", dense, rural network of universal small banks is required. In accordance with the standard international practice it is important that these banks be organized on the cooperative principle; the member-owners be at the same time the depositors of the bank

and its clients applying for credit. This is the only way to achieve that the earnings produced in the village remain in-situ, serve for the interest of the local community.

- However, on the other hand the local small bank represents a low capital strength, assumes not a little risk in financing the agricultural and other private enterprises and, in general, it may get into a defenceless position in the competition in the money market.

- The mentioned disadvantage could be overcome by the Western European cooperative banks looking back upon many years of experience in a way that they established their common apex banks. Thus; preserving the major part of their independence, they can make use of all benefits of an organized banking institute and network representing a large capital strength.

- Among the domestic banking institutes, the major part of the facilities (dense network, acceptable infrastructure, trained expert team committed to the cooperative principle, having great local knowledge and personal contacts) a small bank assuming rural financing should have are owned by the savings cooperatives. It can be anticipated that a new credit cooperative network may as well be established by way of utilizing the emptied farmer's cooperative centres since the physical background and the agrarian intelligentsia released from the large-scale farms would constitute an initial basis for this. The raising of this question is, unfortunately a disputable alternative in the short term as, on the one hand it would resolve the problem of agricultural crediting only, of the wide range of financial services, whereas, on the other hand the cost of developing a functional network would use up as many as 10 to 20-times of the justified modernization expenses.

Owing to the socio-economic and political changes hardly 15 per cent of the savings cooperatives will be able to continue to operate independently and to meet the legal prescriptions and the new types of demands laid on operation. Without an alignment constituting a qualitative change, about one

quarter of them would, with external help, be able to keep their functionality, however, most of them are expected to face merger, being purchased or winding up.

- At the same time the established network of the savings cooperatives, their existing and potential clientele, deposit stock are regarded by several commercial banks, major authorities and social organizations as a good business and as a position constituting influence and power. The organization process for acquiring their network has already commenced and several concepts have been developed for their interconnection with one apex bank. The main point of these concepts is that voluntarily joining savings cooperatives would establish the jointly owned bank constituting an apex organization (this is, in general, the Savings Bank) which preserving its commercial banking function, would operate as an apex bank. The savings cooperatives in return for giving up their independence, could have the benefits of organized capital strength and central coordination representing greater security. Unfortunately, instead of "the task and its reasonably resolving" all of the referred concepts laid the emphasis on setting up the institutional scheme. A deviation is constituted only by which position the individual institutes should be assigned within the new rural banking network.

None of them anticipates a realistic alternative for the savings cooperatives. Their common feature is that the either join the central will and subject themselves to it or remain outside and fail.

- The savings cooperatives should, first of all, clarify if they consider the adherence to and solidarity with the cooperative principle as an appropriate organizing and cohesive force? If so, they can assume the task of becoming a rural network of small banks only in close cooperation with each other. If not, the majority is compelled to resign themselves to the fact that, due to personal interests, a few people decide instead of them/on their fate.

- In order that the villages may get universal banking institutional service and that the savings cooperatives may obtain a realistic perspective, we have elaborated our own concept in the course of a 2-year development-research work. The project has been managed by the Mentor Small Cooperative all along; its material and intellectual support allowed well-prepared, trained financial, agricultural, informational and telecommunication experts, bankers, economists, savings cooperative managers and practising rural entrepreneurs to participate in the work. The development concept featured herebelow in a recapitulative manner is the intellectual KNOW-HOW of the Mentor Small Cooperative.

Aim of the project: to bring the new participants of rural economy into an entrepreneurial position and to assist them in order that the rural material and human resources be utilized as efficiently as possible, increasing by all this the livelihood and material security of the rural population.

Participants in the project: the rural farmers, expectedly farmer's families, minor cooperatives, economic partnerships requiring the services to be rendered by the scheme. Their common feature is their defencelessness due to the lack of entrepreneurial experience, information, capital, enterprise managing ability.

Main point of the project: a service-like intervention affecting the whole environment of rural farms which creates an interest-based coordination among the farms, advisors, credit institutes and information systems, their simultaneous putting into operation.

The approach intervention: basically the improvement of facilities.

It intends to make the:

1. entrepreneur capable of managing its own activity. Thereby, at the same time it also requires capability of being the partner of the banking institute (crediting etc.) of the agricultural administration (regime etc.) of the budget (taxation etc.).

2. banking institute capable of rendering services to the rural clientele (information-based new crediting methods, strategies, monitoring the credits laid out), of the successful, safe survival in an independent cooperative form (laying the foundation of its safe operation in the market by means of high-standard banking services).

It can make: the interest representations, the agricultural administration capable of establishing the framework of the whole verticum of food production (by way of correct, wide-base information) and of regulating it in the desired direction (regime).

It is also an essential trait of this approach that the project does not include any compulsory prescriptions for the participant, it only provides decision alternatives for him as to what services he makes use of, however, simultaneously, it also provides decision capability for the participant (information). The harmony relying on interests will automatically be reached in the scheme. The one (entrepreneur, banking institute etc.) joining the system enters information into the system about his own activity and, in return for that it requires information (on money, capital, product etc.) necessary for his own activity. The surplus private yield resulting from the improvement of the managing ability acquired this way may provide coverage for upkeeping the system.

The condition of information flow is the network-like operation. The technical background of this is a satellite-type communication network, the Mentor is ready to install this network within half a year.

An important element of the project is the intellectual capacity of the so-called methodological centre which, by way of processing the information in a subject-specific way, works as a catalyzer in the system.

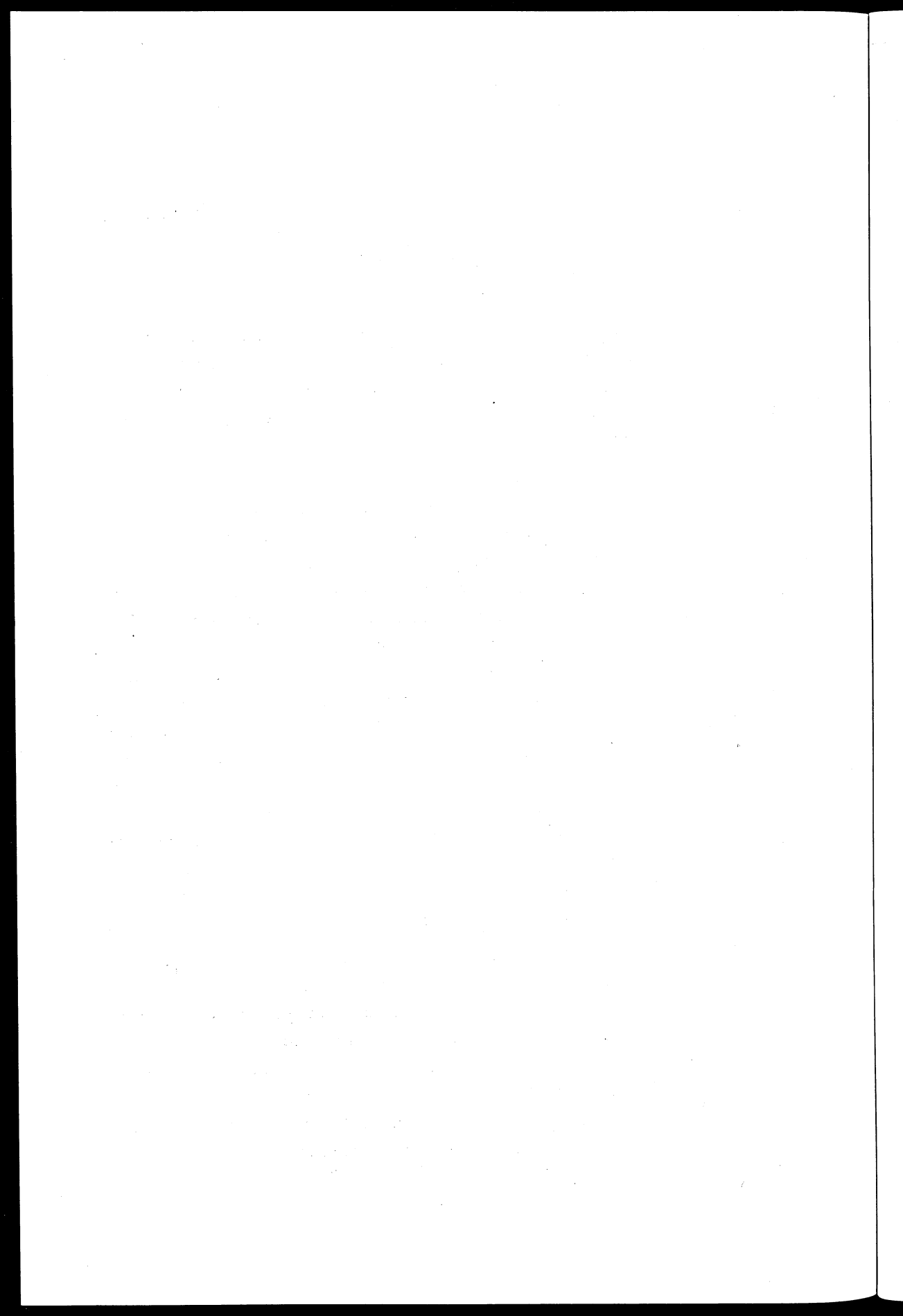
The practical success of the project assumes, of course, a calculability which is a minimum requirement in respect of the economic participant and, furthermore it also presumes an assumption of role by the state, aligned to the practice in countries regarded by us as those to be followed.

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APPENDIX



Special obligation for making provisions,
qualified outstanding claims

The activity, crediting attitude of the banking institutes and within this, the financing of the agricultural sector, too, are basically influenced by the following conditions laid down in the Act on banking institutes and in the prescriptions related to bank supervision:

1. The fact that the commercial banks have to make provision for the coverage of their qualified outstanding claims in form of a risk target reserve reduces their crediting risk, increases their demand for business profit and thereby hinders the decrease in credit interest rates expectable in consequence of the decrease of the inflation rate and that of the interest rates on the deposits, which has to be accounted as expenditure. The banking institute is liable to make a 20-per cent provision on receivables qualified as below-par, overdue between 1 and 60 days; an 50-per cent provision on doubtful debts overdue between 61 and 360 days and a 100-per cent provision on bad debts overdue over 360 days and on the total debit portfolio against debtors under winding up procedure, irrespective of what amount is included in the overdue invoice. It is a more strict regulation also constituting a loss on interest income that the amount qualified as bad debts for which provision has been made in form of target reserve has to be kept in liquid assets.

2. The investment activity of the commercial bank, the application of credit-capital conversion are limited by the Act on banking institutes, in relation to the guaranteeing capital. The bank may not hold a share in a company which is more than 15 per cent of its own guaranteeing capital and it may not hold a share exceeding 51 per cent of the own capital of an enterprise. And, the total investment made by the bank may not exceed 100 per cent of its guaranteeing capital.

From the restriction (100 per cent) on the total investment, the banks may withdraw their investments (forced investments that have been made by them in order to mitigate the loss and to eliminate same, respectively, by way of credit-capital conversion.

The aforementioned withdrawal can only be enforced if the investment has been owned by the bank for less than three years. Accordingly, the bank needs to sell its investment the profitable realization of which is very uncertain.

Following the application of the credit-capital conversion, the bank frequently becomes a co-owner of company, holding a share over 10 per cent. Subsequently, the new credit to be made available to the client will be regarded as internal credit the approval of which may be effected under limitations only.

The aforementioned statutory rules and the fact that a significant number of the companies is not able to produce a considerable dividend even by way of credit-capital conversion make the banks extremely careful and precautions.

Qualified outstanding claims

The absolute and relative worsening of the situation of food economy is well demonstrated by the fact that the qualified credit portfolio has grown to 2.6-times in the agriculture, to 2.1-times in the food industry from the 31st of December 1991, whereas it has doubled in terms of the whole clientele.

And, within the qualified outstanding claims, an unfavourable disproportion is shown in favour of doubtful and bad debts inducing an obligation of making provision to a greater extent.

Within the qualified outstanding claims, the greatest growth can be seen with the agricultural clients, in terms of both proportion and amount. The ratio between the qualified credit portfolio and the credit portfolio of the branches

under survey is somewhat higher in the food industry than that of average of the banks and it is near the bank average in respect of the agriculture. Consequently, the "frozen" credit investments made in food economic partners play a significant role in the commercial banks' obligation of making target provisions.

The impact of transformations on financing

In addition to the extremely miserable financial position of the agricultural economy and to the bankruptcies, windings-ups encountered in a large number, the transformations are making the financing difficult, to a great extent. At that, the commercial banks need to thoroughly monitor and analyse the transfer of their outstanding credits and coverages to the new owners. If the facilities and demands meet, the commercial banks are making efforts for promoting the transformations, by way of granting reorganization credits for the transformation of farmer's cooperatives at preferential interest rate and by making Existence- and Agricultural Reprivatization Project credits available to the transformation of state farms and state companies, also at preferential interest rate.

The situation is made more difficult by the frequently simultaneous appearance of transformations and bankruptcies.

The mentioned great changes make the conditions of operation and production rather insecure.

Financing of food economic clients under
bankruptcy and winding up procedure

The bankruptcies and winding-ups definitely influenced, in 1992, the financing of food economic partners.

The crediting for the concerned clients became more difficult upon the effect of the growing risk factors; in most cases the investment of new resources substantially ceased. In respect of treating these farms and companies, the re-collection of outstanding claims became a primary task.

The number of clients declaring bankruptcy increased till mid-year dynamically, then, in the 3rd quarter, the pace of growth became slower. The agricultural and food economic partners' situation being more unfavourable than the average is reflected by their higher proportion in respect of bankrupt clients than of the whole clientele and their share in the banks' portfolio of receivables is still substantially higher than that.

E.g. the agricultural clients that declared bankruptcy represent 19 per cent of those who declared bankruptcy, whereas they represent 34 per cent of the outstanding claims in bankruptcy. The food industrial clients account for 3 per cent of those who declared bankruptcy but these plants represent 10 per cent of the debts in bankruptcy against the OKHB (National Commercial and Credit Bank). These data show the indebtedness of bankrupt food economic clients being substantially more concentrated than the average. The Commercial Bank makes efforts to conclude an agreement in bankruptcy at the bankruptcy negotiations, always taking the security positions into account, by granting as less allowances as possible. Thus, it - in the course of bankruptcy arrangements - made proposals mainly on the cancellation of default interest, then on the cancellation of maximum 50 per cent of the basic interests linked with certain repayment obligations, and then on the re-scheduling of receivables.

The credit-capital conversion was applied in a few cases only, whereas the principal was not cancelled at all in any case of bankruptcy agreement with agro-economic clients.

In the case of some partners it could be experienced that they do not declare bankruptcy even despite their debt overdue by 90 days due to prestige since they are confident that their transitory insolvency problems will be resolved and they can compound with their creditors, out of bankruptcy proceedings.

In the case of some clients being in special position, it occurred that a newer credit was put out, under governmental guarantee, in order to maintain functionality.

The bankruptcy agreements where the condition of the bankruptcy agreement's coming into existence was the approval of the guarantee by the ÁVÜ (State Property Agency) or by the state may be regarded as special arrangements. Unfortunately, in certain cases, even the granting of loan under government guarantee proved insufficient to create the priority client's ability of profitable operation.

With the food industrial branches that got into a position featured by basically changed conditions, the definite concept of the competent Ministry (Ministry of Agriculture) and the ÁVÜ (State Property Agency) is missing, in respect of the forced elimination of surplus capacities. Though, the generally low rate of utilizing the existing capacities in the e.g. meat, poultry and canning industry suffering recently from basic material shortage deteriorates the chance of profitable economic management for all those concerned. The omission of decisions, the "persuasion for market mechanisms" brings namely the financing banks into a difficult situation. As a matter of fact, they make all efforts to try to save their outstanding claims by way of organizing strategic investors with promising new market opportunities and finally, even by way of acquire-

ment and of passing into trusteeship for improvement.

As for the agricultural farms, the conclusion of bankruptcy agreements and the obtainment of the resources necessary for fulfilling the obligations is feasible only by way of selling certain production units. The supply of movables and immovables, appearing in a large quantity in the individual regions, results in a considerable devaluation of assets due to the limited demand.

The large number of bankruptcy and winding up cases have compelled the commercial banks to establish - in addition to the financing that can be called traditional and to other banking operations - trading, investing, trusteeship, real estate agency- and other servicing organizations by the collaboration of which they can increase their chances concerning the re-acquirement of their outstanding claims that got into a critical situation or to relocate them into a position identified by conditions resulting in a more secure return on investment.

As a general effect, bankruptcies and winding-ups, the global devaluation of production means and real properties constituting the securities of the banks' claims can be felt which is abrupt especially after the declarations of being wound up. Being aware of this fact, also the Commercial Bank makes efforts to promote bankruptcy agreement by concluding compromises. It tends toward winding up only if securities constituting a very good position or bankruptcy offers requiring considerable sacrifices are available.

It is to be noted that the conclusion of bankruptcy agreements does not always mean the restoration of lasting functioning ability in the case of food economic clients either. For instance, the autumn revenues still calculated in agreements made formerly have not realized in the case of several cooperatives, due to the drought. If a hard-and-fast

bankruptcy management would be applied, this would automatically result in winding up but, by searching for compromises in a circumspect way, the complementary agreements are conceivable.

Opinion of the OKHB (National Commercial and Credit Bank)
on the situation and solvency of the agricultural economy

The concept of developing a subsidy-free agriculture and food industry has proven to be inappropriate. This, finally, has led to the deficit of the economic management, to the rapid decrease of production, to catastrophic using up of production bases. And, in financing the branch, the appearance of bankruptcies and winding-ups in a large number has caused forced effects to function. Consequently, business-based crediting can only be limited to financing certain combined and currency crediting operations as the normal interest rates on credits (varying in our Bank, as for e.g. short-term credits, between 30 and 35 per cent even today) cannot be borne by the profitability of the overwhelming majority of agricultural and food industrial producers.

Moreover, the considerable reduction of interest rates on credits, also acceptable for the concerned clientele, is impeded by the interest margin increasing effect of the large qualified credit portfolio. I regard, in respect of future financing, the restoration of profitability in the agriculture as being of decisive importance for which I see a realistic possibility only through the prices and by way of the harmonic adjustment of export subsidies. In addition to the foregoing, I deem necessary to stabilize the institution of interest subsidies and to increase its normativity.

As to financing the development projects which has touched the bottom in recent years, the establishment of the Land Credit Institute and the foreseen Agrarian Reconstruction Fund may play a significant role.

In financing the farmer's farms being developed, a considerable role may be assigned to a savings cooperative branch network well-provided with capital.

Development of the loan portfolio of the
Commercial Bank Co.Ltd. in the years 1990 through 1992

Composition of credits granted for
 less than 1 year

Description	Chronological credit portfolio					
	1990		1991		1992 x/	
	billion Ft	%	billion Ft	%	billion Ft	%
Agriculture	12.5	22.2	12.9	20.9	14.6	24.4
Food industry	14.0	24.9	17.3	28.0	15.9	26.5
Bank altogether	56.3	100.0	61.7	100.0	59.9	100.0

Composition of credits granted for
 over 1 year

Agriculture	15.7	25.8	17.2	28.4	15.1	28.2
Food industry	17.0	27.9	16.4	27.1	15.5	28.9
Bank altogether	60.9	100.0	60.5	100.0	53.6	100.0

Composition of all credits

Agriculture	28.2	24.1	30.1	24.6	29.7	26.2
Food industry	31.0	26.5	33.7	27.6	31.4	27.7
Bank altogether	117.2	100.0	122.2	100.0	113.5	100.0

x/ from January through 30 September.

Annex 6Major principles of operating the cooperative banks

- the mainly compulsory membership of credit utilizers (now this compulsion is being somewhat mitigated),
- the unlimited liability of the banks' members upon bearing the eventual deficits (this prescription has also become looser meanwhile),
- a good insight into the situation of credit debtors in order to prevent losses; lucidity resulting from the geographical determinedness of the banks area of operation,
- reduced profit-orientedness, appropriation of the profit by its transfer to the reserve,
- the development of the reciprocal assumption of liability by the banks, the development of a might-be cross-guarantee scheme,
- democratic structure,
- openness to admitting new members.

Structure of these cooperative banks

The local banks - having several branches (offices) and mobile branches - are coordinated, as an apex institute, by a cooperative bank that functions as an independent apex bank as well.

The apex bank is a commercial bank having full-range entitlements which coordinates the savings cooperatives as member-banks in the framework of a bank syndicate and, as being the apex bank, it performs checking and managing functions in respect of the member-banks and, in a certain circle, it also functions independently, as a commercial bank.

The cooperative banks are independent legal entities with shareholder's meeting, Board of Directors, independent business policy.

With a part of the Western European cooperative banks, regional banks are functioning which are meant for upkeeping the relations between the local level and the apex institute; elsewhere, the network is of two-stage structure only. In this latter case, they operate regional offices for consulting, support, supervision.

The apex institute is the apex bank.

The local banks subscribe a part of the apex bank's capital each; they are co-owners of the apex bank. In their capacity as co-owners, they assume liability for the obligations of the apex bank to an extent being the multiple of the capital subscribed by them. This owned share may not be appropriated by the local banks.

Functions of the apex bank:

1. Central bank of the local banks

- it performs consulting, managing functions and it manages the foreign and domestic payment circulation of the local banks and of their clients (giro), their cheque circulation, currency transactions, securities transactions, portfolio, insurance mediation, travel mediation, training of personnel,

- supervision, checking

The Bank's Supervisory Board treats the cooperative banks as separate units. (The prescriptions related to liquidity, solvency apply to the bank syndicate as a whole.)

Liquidity

The local banks are liable to appropriate a definite part of the deposits on their running accounts (it may be even 26 per cent at some locations!) by transferring it to the account of the apex bank. If the prescribed extent is not fulfilled, the credit transactions of the local banks are limited, or suspended, in an extreme case.

The apex bank, by means of the volume of the deposits kept by it and with the help of the interest rate paid thereon, has influence on the credit transactions of the local banks.

Solvency

The apex bank takes special care of the local banks whereas a sufficient provision should be available to them as a coverage for credit losses and for other business losses.

In this regard, the prescriptions within the banking network are, in several cases, stricter than those imposed by the Banks' Supervisory Board. The bank syndicate may as well establish a fund for the coverage of credit losses which fund is available to the local banks and it is maintained out of the annual contributions by the local banks.

2. Commercial banking function

In addition to the services rendered to the local banks, the apex bank conducts own banking activity as well. The apex bank renders assistance to the local banks if it has to grant a credit exceeding the local crediting level or if special skills are required in managing a transaction. The clientele not belonging traditionally to the local banks is served by the apex bank, as well. This clientele is constituted mostly by medium-scale enterprises. Consequently, the apex bank is not a competitor for the cooperative banks.

Savings Cooperative 1990

WE INTRODUCE OURSELVES

The first Hungarian savings cooperative was founded by rural citizens 35 years ago. The aim of its foundation was to render better financial services to the rural population, to the cooperative members living in the area of its operation. This aim continues to be valid even today.

The savings cooperative membership is voluntarily and open: every Hungarian citizen, who lives in the cooperative's scope of operation or who works there or has a real property there, may become a member of the cooperative. The membership comes into being in a simple way: by way of application for admission and of performing a minimal asset contribution. The membership may not be inherited but, if the inheritor is also a member of the cooperative, so the share, i.e. the property relationship, can be assigned, transferred. The 261 savings cooperatives number, at present, nearly 2 million members.

The operation of savings cooperatives is based upon the voluntary resolution made by the members, they make decisions in the meeting of shareholders (or delegates) on every substantial issue (asking for rendering account, division of profit or loss, merger, de-merger, winding-up etc.). The member is entitled to hold any elected office and, also, to obtain any information on the matters of the cooperative, on occasions other than the shareholders' meeting, too.

In the savings cooperative, one member has one voice, irrespective of his share held in the cooperative assets.

The capital of the savings cooperative consists of shares and of accumulated property which is the basic condition of its operation. The self-governing of the cooperative is enforced in the framework of the law: the most important element of this is that the member decide by themselves on issues related to the operation, economic management of the cooperative,

it formulates the Articles of Association, sets up the managing bodies, checks the officials. The operation of the cooperative is managed by elected officials (the Chairman of the Board of Directors, the Vice-Chairman and the Board Members; the Supervisory Board).

Through the Board of Directors and through the Supervisory Board, the members check the activity directly.

The savings cooperative is an independent legal entity; it can be held liable for its economic management activity by the cooperative members only. Every savings cooperative conducts a business policy complying with the peculiarities of the given region and if it otherwise is in conformity with the rules, it is only the members that may have voice in the business policy.

The interest representation of the savings cooperatives is of two-stage structure: local (regional) and national. The National Federation of Savings Cooperatives was established in April 1990, on voluntary membership basis, by the delegates of the savings cooperatives, for the purpose of interest representation and solidarity.

The major part of the savings cooperatives' activity was, in the past, composed of the collection of deposits by the population and of the crediting for the population (credits granted for housing, consumption, agricultural production purposes). Now, more and more cooperatives are getting involved in the new functions. The scope of the savings cooperatives' activity has substantially expanded; they may establish business relations with legal entities, too. This provides an opportunity for them to finance the different forms of enterprises and also to manage the finances of the local governments.

The savings cooperatives conduct the following banking institute activities:

- collection of deposits and savings deposits,
- keeping banking accounts for legal entities and private persons and managing their circulation of money,

- concluding credit contracts, loan contracts with legal entities and private persons on business basis,
- organizing the issuance of securities circulating, preserving and managing securities,
- assuming guarantee for legal entities and private persons (banker's guarantee) if the obligation undertaken is to be fulfilled by paying money and assuming bank guarantees,
- purchasing and selling of assets resulting from supplying commodities and from rendering services,
- financial managing and trusteeship services,
- issuance of cheques and credit cards,
- investment of savings on commission,
- financing instalment business,
- mediation of money-, credit-, securities- and insurance transactions (agent's activity),
- conducting other, banking institute activity on commission,
 - purchasing and selling foreign currencies,
 - other services,
 - paying the countervalue of purchased goods,
 - collecting membership fees of the automobile club,
 - receiving assignments for advertisement,
 - selling catering vouchers,
 - honouring IKKA-assignments,
 - selling football pool coupons and lottery tickets,
- in order to train the student's youth for saving, 96 savings cooperatives have established and operated a total of 180 in-school savings cooperative groups.

Source; Savings Cooperatives 1990.

Information material issued by the OTSZ (National Federation of Savings Cooperatives), pp. 5-8.

Functions of the apex bank

a/ Provision of an appropriate management, handling savings cooperative's funds deposited in the apex bank.

The apex bank also functions as a reserve fund for the savings cooperative. The surplus funds of the individual savings cooperatives are regrouped through the apex bank to savings cooperatives encountering transitory shortage of funds. At the same time, it manages transactions in the money- and capital market also for the bank syndicate as a whole. By way of appropriation by transferring to the reserve, it may as well conduct a wider commercial banking activity.

b/ Identification of the general rules of the savings cooperatives' operation.

The apex bank is liable for supervising the savings cooperatives, for ensuring the solvency of banks and for their adherence to the prescriptions of the Banks' Supervisory Board.

c/ Consulting services rendered to the savings cooperatives, its management with special regard to the identification of their annual budgets, that of the interest rates and commission fees.

This consulting affects mainly the expense-income aspect of the banking activity. It involves the product development etc.

The apex bank provides the savings cooperatives with advices also in the field of deposits, credits, credit survey etc. In the knowledge of the usual market conditions, the apex bank informs the savings cooperatives on the change in the interest rates and commission fees as well.

d/ Supervision of savings cooperatives

The apex bank conducts audits, in a number identified annually, with the savings cooperatives, in order to check the observation of the various prescriptions, for the purpose of auditing.

e/ Services rendered to the savings cooperatives

The admission to the giro system may be implemented also through the Savings Bank; the Savings Bank functions as a giro centre for the cooperatives.

f/ Operating joint information services.

g/ Establishing, maintaining foreign business relations.

Functions of the National Council of Savings Cooperatives:

a/ General representation of the bank syndicate's interests.

b/ Creating the image of the bank syndicate, popularizing the bank syndicate.

c/ Organizing, managing the communication between the savings cooperatives and the Savings Bank,

d/ Organizing training for the employees of the bank syndicate.

e/ Managing personal issues.

f/ Legal consulting.

Tasks of the apex bank of savings cooperatives

The apex bank of cooperative banks completes a great variety of tasks:

- 1) general coordination and supervision
- 2) financial centralization and commercial activity
- 3) supporting the regional and local banks
- 4) establishment of subsidiaries in cooperation with the savings cooperatives interested in collaborative enterprise.

a/ Coordination and supervision of the activity

The apex bank, as a central body, need facilitate/assure the smooth operation of local component units. This is the body that is responsible for the auditing by using legal and regulatory provisions typical of the local savings cooperatives.

Their further task is the administrative, technical and functional checking. To achieve the aforementioned targets, the apex bank needs to take all necessary steps, mainly those guaranteeing the liquidity, solvency of the network as a whole.

It is also one of the apex bank's tasks to cooperate with the local savings cooperatives in order to prevent competition within the same network.

b/ Financial centralization and commercial activity

The apex bank need assume the responsibility for being capable of rendering accounts if so required, so that the liquidity positions get under checking.

The collection of deposits is another field falling within the sphere of the apex bank's authority. It has to use the funds available to it in refinancing the long-term credits granted by the local savings cooperatives, increasing thereby the group-risk. Generally speaking, the liquidity risk

and the asset conversion are run mainly by the apex body, whereas the responsibility of assuming risk associated with granting loans is assigned to the local savings cooperatives.

The apex bank in a given case need participate in the money market transactions too, so that it can manage the deposit volume, deposited at the apex bank, with the local units. The deliberateness shown in the subject of such surplus liquidity is an essential element.

The apex banks need become key instruments in developing local savings banks if the domestic banking laws amend the basic requirements as it is the case now in Hungary.

c/ Supporting the regional and local banks

The apex bank in international terms, need foster the syndicate interests by their being involved in the foreign networks, by buying shares in foreign banks or by opening representation offices.

The apex bank also has to foster the establishment of working relations with foreign correspondents by constituting a limit surface between the banking transactions and the rendering of commercial assistance.

The apex bank need contribute to the technological development projects of its syndicate too, and it has to be the vanguard of the syndicate's large-scale technological project in full cooperation with the National Federation of Savings Cooperatives.

The apex banks are also expected to render a number of supporting and consulting services in variegated fields such as economy research, financial appraisal, legal affairs, risk analysis and appraisal, data processing, documentation, inter-clearing and credit card systems.

d/ Joint partnerships with savings cooperatives

Several subsidiaries could be established for conducting activities the local units have not conducted so far. The

main scope of the activity of such subsidiaries could be the corporate financing (by compiling standard financial packages, by subscribing shares in companies), the leasing in the commercial sectors, the capital and transferable securities (bonds and shares) etc.

In connection with the aforementioned point b/, the setting up of a central banking institute owned and audited by the member cooperatives need be thoroughly considered. Such an institute would mean a solution to the basic requirements detailed herebelow:

- 1) investment options for the surplus deposits of the members when no demand exists for them and
- 2) an immediate money resource for an unexpected withdrawal of a demand for which the member-cooperative is not prepared.

The savings cooperative may establish this central banking institute as the agricultural mutual aid fund was developed. They would keep the administrative expenses at a low level and the institute would, at the outset, grant only short-term liquidity loans. They would invite the members to send monthly financial reports to the institute which would serve for checking the solvency of the member-cooperatives applying for credit.

The setting up of a central financial institute would, in one way or another, resolve a number of problems the savings cooperatives have to encounter. This "establishment" would function as a trustee for savings deposits and it would grant credits to member-cooperatives applying for loan in excess of the volume of the available deposit stock.

Due to the low overhead expenses and investable funds, a central establishment can offer a higher return on investment in respect of the surplus funds of the member-cooperatives. The operating price margin of the centre creates a profit fund out of which the centre can offer a full range of financial services to the members.

The two major advantages of the centre is the establishment of a strong financial and liquidity system for the country's savings cooperatives and the mobilization of domestic savings. The member-cooperatives deposit their surplus funds with the centre that invests these funds and, if necessary, lends same to the member-cooperative. Those funds which would have otherwise been outside the scheme are retained for being used for the purpose of the movement. By establishing a properly capitalized institute, the movement can cope with the economic fluctuation.

The financial functions of the centre need:

- to develop financial independence by collecting the surplus funds in a joint fund as to provide the highest yield for the members;
- to concentrate the liquidity from the credit union by means of the surplus funds. This assists the member-cooperatives in complying with their members requirements for yield and liquidity and it inspires confidence in the scheme and contributes to the increase in the fund;
- to lend money to solvent member-cooperatives experiencing excessive demand for credits;
- to achieve economies of scale by collecting the resources in a joint fund so as to achieve a better return on investment and to be able to offer its credits and other services at a lower rate;
- to return the central revenues, after the expenses and the capital have been divided, to the members, in form of dividend;
- to offer a wide range of technical services, including the assistance rendered to pricing, budgeting, credit policy, economic projection, training and to developing special projects;
- to identify financial standards and to assist the members in complying with same;

- to build a permanent capital fund by way of accumulating the reserves and non-divided revenues;
- to provide for access to the money market. The centre may ask for loan funds both in the domestic and in the international money markets, providing more favourable terms than an individual unit might achieve.

The centre's Board of Director may be composed of the leaders of the National Federation of Savings Cooperatives who would be responsible for the general management of the centre's affairs.

An investment- and credit committee could audit the funds of the member-cooperatives. The supervisory board functioning mainly as an auditing committee would audit the centre at short intervals (or it would take measures for conducting such audit work) in order to assure that the centre operate in accordance with the laws, articles of association and with the sound business practice.

Directive of the Council of the European Community
on the credit institutes

4.§ a/ The credit institutes functioning at the time of publishing this Directive in the same Member-State and with a permanent trait at the given time, as subsidiaries of a central body that supervises their activity and that has been established in the same Member-State may be exempted from the requirements enlisted under the first, second and third paragraphs of the first sub-point of Article 3. (2) and under Article 3. (4) and under Article 6, till the national authorities take the measures necessary for adopting this Directive in the national code which law declares that:

- the liabilities of the central body and those of the associated institutes are joint and several or fully under the guarantee of the central body,
- the solvency and liquidity of the central body and of all subsidiaries are audited on the basis of consolidated accounts,
- the management of the central body is entitled to give instructions to the managements of the subsidiaries.

b/ The credit institutes functioning locally and which, after this Directive will have been announced, will become subsidiaries of a central body may make use, within the framework of point (a), of the opportunities offered by point a/, if they constitute a normal expansion of the network belonging to the respective central body.

The joining savings cooperatives lose a part of their independence but this may be an acceptable compromise in relation to the situation jeopardizing their survival.

Major rights and obligations of the savings cooperatives:

- they have to observe the prescriptions of the apex bank,
- the savings cooperatives are the owners of the shares of the apex bank,
- the savings cooperatives have to make a deposit on the account kept by the apex bank,
- the member-cooperatives do not enter into relations with each other directly; they participate in each transaction through the apex bank; they observe the procedures prescribed by the apex bank in this regard;
- they submit their budgets and annual accounting to the apex bank every year and they furnish the apex bank with appropriate data;
- they open any new branch, transitory office, new establishment only with the prior consent by the apex bank;
- the cooperatives refrain from conducting activities outside the border of their scope of activity, in geographical terms;
- they assure the adherence to the solvency and liquidity rules as per the prescription of the apex bank and they are liable to assist the apex bank in its taking steps for the continuous operation of other member-cooperatives.

BULLETINS ISSUED IN THE LAST TWO YEARS

Research concept for the years between 1991-1993.

(Ed. Á. Bisztray)

Budapest, 1991. 42 p.

Bulletin No. 74.

Abstracts of selected publications issued in 1990.

(Ed. Á. Bisztray)

Budapest, 1991. 101 p.

Bulletin No. 75.

The Hungarian agricultural economy and the
European Community.

(Ed. Á. Bisztray)

Budapest, April 1991. 162 p.

Bulletin No. 76.

Basic principles of the functioning mechanism and
modernization trends of the agrarian market regulation in
Hungary

(Ed. Á. Bisztray)

Budapest, 1991. 82 p.

Bulletin No. 77.

Abstracts of selected publications issued in 1991 and
research tasks for 1992.

(Ed. Á. Bisztray)

Budapest, 1992. 56 p.

Bulletin No. 78.

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