CURRENCY AND BANKING REFORM IN ESTONIA

On April 29, 1927, the Estonian Government, acting upon recommendations of the financial committee of the League of Nations, passed a series of laws providing for the creation of a new currency unit, for the termination of the privilege of note issue by the State, for the unification of the currency, and for the reorganization of the bank of issue.

Currency reform.—The currency law established a new monetary unit, the kroon, which is divided into 100 cents. The kroon has a gold content of 0.40323 gram fine and is equal in value to the Swedish crown, or 26.80 cents in United States currency. The estmark, which has been stable for almost three years at the ratio of 100 to 1 Swedish krona, will be temporarily retained as the cent.

Prior to the reform there were two classes of notes in circulation—treasury notes issued by the State, against which a special reserve was held by the Government, and notes issued by the Eesti Pank. The present law provides for the amalgamation of the two forms of notes. The Eesti Pank will take over the note liability of the treasury, and the latter in exchange will turn over to the bank the reserve held against outstanding treasury notes. For that part of the note liability not covered by the reserve the bank will be compensated through the transfer of the necessary amount of Government securities or other assets.

By means of these measures the currency and the reserves held against it will be concentrated in the hands of the central bank. The notes of the Eesti Pank are made legal tender. During the period of the existence of the bank the treasury is obligated not to issue or reissue its own notes; it will, however, mint subsidiary coins of various denominations from 2 kroon to 1 cent. The 2 and 1 kroon coins will be of silver of a fineness not less than 5/10. Until these subsidiary coins are put into circulation the treasury may issue paper money of corresponding denominations. The total nominal value of subsidiary currency of 2 and 1 kroon denominations in circulation may not exceed 6 kroon per head of the population as shown by the last census; and of the cent denominations, the total may not exceed 3 kroon per head. This paper money is to be withdrawn from circulation as soon as coins of corresponding denominations shall have been issued in adequate amounts.

Reorganization of central bank.—Prior to its reorganization, the Eesti Pank was entirely under the control of the Government and functioned chiefly as a commercial bank in keen competition with the other banks. The new bank law makes the Eesti Pank completely independent of the Government and restricts its operations to those usually performed by a bank of issue. The bank is endowed with the exclusive note-issue privilege in Estonia for a period of 25 years from the date on which the law becomes effective, and its first duty is to insure the stability of the gold value of its notes. For this purpose the bank is obligated to buy and sell at its head office at a certain specified rate the legal tender currency of such foreign gold-standard countries as may be determined from time to time, in an amount not less than 5,000 kroon. The capital of the bank under the new statutes is fixed at 5,000,000 kroon, divided into 100,000 shares of 50 kroon each. The capital may be still further increased by the board of directors, subject to the approval of the Government.

The general conduct of the bank is intrusted to a board of directors, consisting of the president, who is appointed by the Government, two members of the board of management, who are appointed by the president, and seven others elected by the shareholders. Of these latter, three are to represent the Chamber of Commerce and Industry, two the Central Agricultural Society, one the Cooperative League, and one the Central Association of New Settlers. The actual conduct of the work of the bank is intrusted to a board of management consisting of the president, his deputy, and any number of other members that may be required. Provision is made for the appointment by the board of directors of a discount committee, the members to serve for two years. The function of this committee is to examine all bills presented for discount or as security for loans and advances.

The Eesti Pank is to act as fiscal agent for the Government and for the State institutions. Its loans to the Government, however, are definitely restricted. The Minister of Finance may appoint a Government commissioner, who shall have the right to attend the meetings of the board of directors but not to vote. The business operations in which the bank may engage are defined in article 51, which reads as follows:

The Eesti Pank may—
(1) Make and issue bank notes.
(2) Buy and sell gold and silver, coin or bullion.
(3) Accept money on deposit or current account.

(4) Discount and negotiate internal bills of exchange, promissory notes, or other commercial paper arising out of a bona fide commercial transaction bearing two or more good signatures and having a maturity not exceeding three months, agricultural bills not exceeding six months and timber bills not exceeding nine months, provided that the two latter categories of bills do not exceed, in the aggregate, 40 per cent of the total bill holding.

(5) Buy and sell, both at home and abroad, telegraphic transfers and checks, and bills of exchange, drafts, and treasury bills of maturities not exceeding three months, payable abroad in a currency with a stable gold value.

(6) Open accounts in foreign countries.

(7) Open accounts for foreign banks.

(8) Grant advances for fixed periods not exceeding six months, and advances on current account, against the following securities: (a) Gold coin and bullion; (b) stocks, bonds, or bills of or guaranteed by the Estonian Government up to 80 per cent of their current market value; (c) commercial paper in Estonian or stable foreign currencies bearing two or more good signatures and having a maturity not exceeding three months; (d) agricultural and timber bills (as in 4 above), provided the amount advanced on them does not exceed 40 per cent of the total advances; (e) one-name promissory notes secured by warehouse receipts against staple commodities fully insured, having broad and active markets, to an amount in each case not exceeding 60 per cent of the value of such commodities at market prices. The rate of interest charged on all advances, except those made under (11) below, shall not be less than 1½ per cent above the bank's current discount rate for three months' bills.

(9) Accept the custody and management of moneys, securities and other articles of value.

(10) Undertake on behalf of third parties the purchase and sale, collection and payment, of securities, currencies, and credit instruments at home and abroad.

(11) Make temporary advances to the Government for expenditure authorized in the annual State budget, provided that the whole of the advances outstanding at any time does not exceed one-sixth of the estimated revenue of the year, and that all advances are repaid not later than at the end of the quarter following the close of the fiscal year in respect of which the advances were made. The rate of interest to be charged on these advances shall be agreed upon between the bank and the Government.

(12) Invest an amount not exceeding the paid-up capital of the bank in securities of or guaranteed by the Estonian Government having a maturity not exceeding five years.

(13) Perform all functions incidental to the transaction of its legitimate business.

Reserve requirements.—The bank is required to maintain a reserve of not less than 40 per cent against all its demand liabilities, including notes in circulation and demand deposits. The reserve may consist of (a) gold coin and bullion owned by the bank, either in the custody of the bank or deposited in other central banks and earmarked for the Eesti Pank's account, or in any mint, or in transit to or from the Eesti Pank; (b) foreign exchange belonging to the Eesti Pank, provided that it shall at all times be convertible on demand into exportable gold at the center where the exchange is held. Subject always to this provision, the term "foreign exchange" is defined to mean (1) net balances standing to the credit of the Eesti Pank at the central note issuing bank or other bank of a foreign country; (2) bills of exchange payable in a foreign currency, maturing within three months, and bearing at least two good signatures; (3) treasury bills, treasury certificates of indebtedness, or similar obligations of a foreign government of a maturity not exceeding six months.

The amount of foreign exchange that the bank is permitted to count in its reserve must be calculated on a net basis, with allowance for offsetting items of corresponding character that figure among the bank's liabilities.

The 40 per cent requirement may be suspended by the Government at the request of the bank, subject to the payment by the bank to the Government of a progressive tax. Before applying for this suspension, the board of directors is required to raise the Eesti Pank rates for discounts and advances by not less than 1 per cent.

For the first three years after the banking law becomes operative there will be associated with the Eesti Pank an adviser nominated by the Council of the League of Nations. The adviser will work through and in consultation with the board of management. The bank is obligated to render the adviser all assistance in its power and to furnish him with any information which he may desire.

The laws will become operative on the day on which the bank receives the sum of £1,000,000, as contemplated in the protocol of the League of December 10, 1926.

Other financial projects.—In connection with the currency and banking reforms, two other measures were under consideration, namely, the establishment of an industrial mortgage bank and the flotation of an international loan under the auspices of the League of Nations. To relieve the Eesti Pank of its frozen credits, which the bank under its present statutes could not include among its earning assets, and to take over the long-term industrial credit operations hitherto carried on by the Eesti Pank, the League of Nations recommended the establishment of a mortgage bank. In addition, to provide the Eesti Pank with necessary liquid funds, an international loan was negotiated. The net proceeds of the loan, as provided in the protocol of the League, are to be £1,350,000, of which £1,000,000 will be placed by the Government at the disposal of the Eesti Pank in exchange for assets which will be turned over to the mortgage bank. The latter will receive the remaining £350,000 to be applied as its working capital.