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## **Prime rate**

Józef Djament, pen name Vir

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Decision by the Bank of Poland to lower its prime interest rate came quite suddenly. It is true that, in view of the recent lowering of the interest rates paid on deposits by the state and private banks, one expected that the current prime rate of the Bank of Poland, which remained intact since October 25 1933 when the prime rate was lowered from 6% to 5%, will adjust to the current trend of the general decrease in the cost of credit. Nevertheless, the timing of the decision by the Bank of Poland was a complete surprise.

This time, the prime rate was lowered by only half a percent. The new rate is not among the higher ones of other reserve banks. At present, the central banks of Italy, Romania, and Estonia have the rate of 4.5%. Higher prime rates are in Greece, Bulgaria (each 6%), Yugoslavia, Latvia, and Spain (each 5%). The lowest interest rate is in the United States (1%).

Lowering of the discount rate by the Bank of Poland is undoubtedly important for the economy of the country. One should not, however, overestimate its importance, and in general one should not overestimate the importance of the Bank of Poland in the Polish credit structure and in the economic life in general. In any normal country, lowering of the discount rate by the national reserve bank is an event of prime importance. This is because in those countries the central bank plays the proper role of a "bank's bank." In those countries, as a rule, the discount rate of the private banks is lower than the one of the central bank. The economic activity is primarily fueled by the private banks and the central reserve bank is the bank that plays the role of the last recourse in the credit market. In our country, it is the other way around. Bank of Poland is the first and the foremost source of credit which fuels the economic life. The private banks play the secondary role, and the ultimate reserve is played by the "street discount." For this reason, the discount rate of the Bank of Poland is the lowest, followed by the rate of the private banks, and then by street discount. This last rate is regulated by the usury laws, but in many cases it exceeds the legal limit of 12%. It is clear that because of the relatively inexpensive cost of credit in the Bank of Poland, the street cost of credit must have gone up. This is because the Bank of Poland cannot service all of the needs of the Polish economy. Only relatively few are privileged to have an access to cheap credits. The vast majority is forced to use the private banks, other state banks, or the street discount. As a result, only a few benefit from lowering of the discount rate by the Bank of Poland.

We report elsewhere in this paper that, because of the lowering of the discount rate by the Bank of Poland, the Association of the Banks took the decision of lowering, by half percent, the discount rate on the current accounts as well as on the savings. It is only because of this decision, the action of the Bank of Poland affects the second group of

borrowers. There remains the third group, not using the credits from the Bank of Poland, nor from the other institutions, which is forced to use street discount. This group will be obliged to reach a voluntary accommodation with its creditors, within the bounds of legal limits on the usury. It would be interesting to determine which of these groups the dominant one in our credit market is. I am afraid the third group is the most numerous.

The lowering of the discount rate on the deposits has an immediate effect of increasing the demand on the commercial paper market. This demand will probably not spill over to the stock market, since the movements of the prices of shares is strictly dependent on the dividend policies, and these are, in the majority of cases, determined by the profitability of the enterprise in question. The demand will, therefore, be restricted to the commercial paper, certificates of deposit, and the governmental obligations. Already yesterday the money market was very bullish.

Whether the transfer of capital from deposits to the commercial paper will cause a permanent increase in the commercial paper market will depend on the future policies of the government, i.e., whether the government will flood the market with new issues of its own obligations. Another words, will the government continue to drain the money market for the benefit of its own treasury and economic policies?