

The Journal of Financial Crises

Volume 3 | Issue 3

2021

Polish Fundusz Pomocy Instytucjom Kredytowym

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Recommended Citation

Oguri, Junko (2021) "Polish Fundusz Pomocy Instytucjom Kredytowym," *The Journal of Financial Crises*: Vol. 3 : Iss. 3, 570-583.

Available at: <https://elischolar.library.yale.edu/journal-of-financial-crises/vol3/iss3/26>

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Polish Fundusz Pomocy Instytucjom Kredytowym (FPIK)¹

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Yale Program on Financial Stability Case Study
November 12, 2021

Abstract

Between September and December 1925, the Second Polish Republic faced a so-called twin-crisis: the złoty,³ the Polish currency, collapsed, and the financial system faced bank runs and flights of deposits. On November 28, 1925, the Polish Government established Polish Fundusz Pomocy Instytucjom Kredytowym (FPIK), injecting over PLN 60 million capital through Bank Gospodarstwa Krajowego (BGK), a national development bank. The government-led capital injection scheme kept supporting the unstable Polish financial system during the inter-war period. Furthermore, in the 1930s, the FPIK served not only the large banks but also smaller financial institutions, and sometimes, non-financial companies. While the FPIK successfully buttressed the financial system, the scheme also contributed to the emergence of authoritarian statism, as the state took significant centralized control over the economy during the 1930s.

Keywords: Poland, broad-based, broad-based capital injection, capital injection, centralized economy, FPIK, inter-war Europe

¹ This case study is part of the Yale Program on Financial Stability (YPFS) selection of New Bagehot Project modules considering broad-based capital injection programs. Cases are available from the *Journal of Financial Crises* at <https://elischolar.library.yale.edu/journal-of-financial-crises/>.

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³ In this paper, “złoty,” as well as the currency notation “PLN,” refers to the Polish monetary unit from 1924 to 1935.

Polish Fundusz Pomocy Instytucjom Kredytowym (FPIK)

At a Glance

The Second Polish Republic (1918-39) was established as the Treaty of Versailles in June 1919 confirmed Poland's independence. After a period of hyper-inflation in 1923, a new currency, the złoty, was introduced. The new złoty notes were issued as legal tender by a newly established central bank, the Bank Polski (Smith 1936). In the summer of 1925, the so-called second inflation occurred, and the złoty became unstable. Simultaneously, both the real economy and the banking system started to crumble. Farmer-debtors faced a plunge in crop prices and became insolvent. In September 1925, the financial system started to face bank runs, and 58 percent of private banks became insolvent (Landau and Morawski 1995).

On September 4, 1925, the Bank Polski, the central bank, lent 15 million złoty to the five largest private banks (Bank Handlowy in Warsaw, Bank of the Union in Poznań, Ziemski Bank Kredytowy in Lviv, Bank Zachodni in Warsaw, and Bank United Polish Lands in Warsaw), as deposits started to flow from Polish banks. The loans were secured and paid an interest rate of 8% (lower than the usual lending rate of 12%) (Stelmach 2012; Morawski 1996).

The Bank Polski loans in September 1925 seemed inadequate to halt the panic in the financial system. However, given the simultaneous currency instability, the central bank was reluctant to offer any further aids, as it considered further funding from the central bank would lead to an increase in the money supply and risk further inflation. In other words, the central bank

Summary of Key Terms	
Purpose:	To prevent banks from bankruptcy and to avoid systemic risk (Morawski 1996, 64-70, 84).
Launch Dates	November 28, 1925
Sunset Dates	The original sunset date was the end of 1927 but was later reintroduced in 1931 (first round) (Stelmach 2012 66-67; DURP 1925 nr. 119, 859).
Program Size	PLN 65 million (first round)
Usage	PLN 63.4 million (first round, by June 1926)
Outcomes	(i) The state banking sector enjoyed much greater public confidence, and (ii) the improvement in the quality of private-sector services, forced both by the crisis and the recovery programs implemented in the banks benefiting from the assistance of the Credit Assistance Fund administered by BGK. (Wierzbicki n.d.).
Key Features	Multiple means and flexible threshold for the governmental intervention. Eventually, the facility evolved as a part of "Sanacja" (Sanation), a political movement to address perceived corruption.

decided to prioritize its mandate of currency stability over its financial-stability mandate (Komierzyńska-Orlińska 2018; Morawski 1996). Thus, the government (led mostly by the Ministry of Finance) took steps to protect the banking system (Landau 2007).

On September 21, 1925, the government established the Komitet Sanacji Banków (the Bank Sanation Committee). Given the limited fiscal capacity, the government could only grant PLN 25-28 million to the Committee, an amount met by the seigniorage from issuing new coins. The Bank Sanation Committee provided PLN 26.9 million to troubled large banks (Stelmach 2012; Morawski 1996). On October 13, 1925, the Bank Sanation Committee announced that it had completed providing immediate help to the banks and was ready to move on to the “second phase.” The second phase implied further structural changes within the Polish financial system, including liquidation of branches and potential mergers. As the central bank continued to prioritize currency stability, the government was the only actor to initiate the second phase (Komierzyńska-Orlińska 2018; Morawski 1996).

The Bank Sanation Committee was transformed into Fundusz Pomocy Instytucjom Kredytowym (Credit Institutions Assistance Fund, hereafter FPIK) on November 28, 1925, and was mandated to provide assistance to credit institutions and restructure the banking system (Landau and Morawski 1995; Wierzbicki, n.d.). The government, initiated by the Ministry of Finance, provided PLN 65 million to the FPIK (Landau and Morawski 1995). The FPIK injected PLN 63.4 million into 15 financial institutions. The capital was injected through Bank Gospodarstwa Krajowego (BGK), a national development bank which was created by a merger of three public banks from the Galicia region (Morawski 1996). Bank Handlowy SA in Warsaw received the largest injection of PLN 21.7 million, approximately one-third of the entire injected capital. Furthermore, as a part of the FPIK, guarantees were granted for foreign loans; according to Morawski (1996), the FPIK guaranteed PLN 1.0 million in foreign loans in 1925 and 0.8 million in 1926.

On May 17, 1927, the FPIK was terminated as the President of the Republic of Poland determined that the financial crisis in 1925 was over and the FPIK had fulfilled its mandate (Morawski 1996; DURP 1927 nr. 46). However, as the credit market fluctuated during the Great Depression and as the Polish financial system encountered another banking crisis, the FPIK was reintroduced. The Act of March 17, 1931, authorized the Minister of the Treasury to spend PLN 20 million for bank rehabilitation (DURP 1931 nr. 3). In 1932, FPIK was incorporated as a part of new regulation (Morawski 1996; DURP 1932 nr. 94) and continued to support the Polish financial system during the inter-war period, with minor amendments made in November 1935.

It is also worth noting that, from its establishment, the FPIK served political means. This was particularly true after the May 1926 coup d'états. The FPIK evolved as a part of “Sanacja” (“sanation,” or “healing”), a political movement to address perceived corruption, and the bill which legally established the FPIK was called the “Sanation bill.” As a result of regulation passed in 1932, BGK had new tools including debt relief, debt cancellations, guarantees, and capital injections. Following the new rule, FPIK could acquire equity in banks and private enterprises. The rule eventually enabled the government’s takeover of

targeted troubled institutions (Wierzbicki n.d.; Morawski 1996). For instance, during the 1930s, some private enterprises and state banks secured debt and capital using FPIK despite their apparent difficulties in repayment. These private enterprises were selected based on their significance for military, economic, and political reasons. The BGK, the conduit of the FPIK, took over those private enterprises under its direct management, establishing the so-called “syndicate of the Bank Gospodarstwa Krajowego,” whose shares amounted to PLN 39 million by 1935 and PLN 43.9 million by 1939 (Landau and Morawski 1995; Wierzbicki, n.d.). Meanwhile, the BGK and other state banks also benefitted from the extensive governmental support including through capital and legal privileges, like tax deduction (Landau and Morawski 1995).

Summary Evaluation

The 1925 capital injection by the FPIK was effective for those large financial institutions that could participate in the scheme; however, the scope of the FPIK was limited to large banks, as the government faced severe budget constraints. After the revival in 1931, the FPIK could inject capital not only to large banks but also to the municipal savings banks and cooperative banks (Wierzbicki n.d.). While literature evaluating the capital injection is scarce, Morawski (1996) considers the capital injection after the 1930s revival as unsuccessful compared to that of 1925 as some participating financial institutions failed shortly after the capital injection in 1931.

From a macroeconomic perspective, some consider the crisis of 1925 and accompanying policy responses, including the establishment of FPIK by the government, as having a significant impact on the Polish banking system and policies.

First, some authors have criticized the central bank’s passive approach to its financial stability mandate and its prioritization of currency stability. This is supposedly because in the wake of the hyperinflation of the early 1920s The Bank Polski continued to provide banks discounted loans from the late 1920s to 1930s, but only to an extent that would align with its interest in currency protection. This can be interpreted as a fair decision, given the Bank was only recently created in order to fight against the hyperinflation (Morawski 1996).

Second, the government became far more influential in the field of financial stability. For instance, in 1926, the government reformed the banking law, established the Banking Commissariat (Komisariat Bankowego) within the Ministry of Finance, and reshaped the banking system. In December 1926, the Ministry of Finance rigorously enforced minimum-share capital requirements and liquidated smaller banks that could not meet the requirements. Therefore, the government was committed to enforce hard stances on private banks, as it had seen how the collapse of a bank could lead to a systemic crisis, and it had spent its limited fiscal budget on the FPIK. The government viewed the fragility within the financial system as caused by small and weak banks, which were mainly engaged in currency trading activities and not much lending (Landau 2007; Morawski 1996). Landau and Morawski (1995) note that the credibility of the private banking sector

decreased after the crisis in 1925. Consequently, they stated that the “trauma persisted and became one of the premises of *étatisme*⁴ in banking in the following period,” leading to statism in Poland.

During the crisis in 1925, foreign investors took advantage of the crisis, demanding that Polish banks repay foreign currency denominated loans. The Polish banks, which could not repay the loans in time (and had little access to the governmental aids, including the FPIK), were often taken over by foreigners. Dependency on foreign capital continued and became even more prominent after the crisis of 1925. As of 1930, the total contribution of foreign capital accounted for approximately one-third of the entire banking system’s capital. Polish private banks relied on funding from foreign investors; however, most of the funding was short- and medium-term as investors were worried about the fragility of an economy situated between Germany and the Soviet Union (Morawski 1996; Landau and Morawski 1995).

Consequently, following the crisis of 1925 and the capital injection by the FPIK, the banking industry structure had changed, notably, in two ways. First, state-owned banks grew significantly while both the number and shares of private banks decreased due to governmental policies. Second, private banks became more dependent on government (state) capital and on foreign capital (Landau and Morawski 1995). The Ministry of Finance preferred to have fewer private banks. The government thought that along with state banks, several large private banks could thrive, attracting deposits and financing domestic and export trends; however, it was hard for private banks to compete with state banks, which benefitted from various governmental supports. Eventually, private banks gave up building long-term credit and focused more on short-term credit (Morawski 1996).

However, the increased dependency on foreign capital had unintended ramifications during the Great Depression and the consequent banking crisis in 1930. The significant differences between the crisis of 1925 and the crisis of the 1930s was that Polish banks, to some extent, benefitted from the credit assistance from foreign banks in 1925. In contrast, in the 1930s, Polish banks faced a significant outflow of foreign capital as the international economy went into the Great Depression (Morawski 1996).

⁴ Refers to Polish statism.

Poland Context 1996	
GDP (SAAR, Nominal GDP in LCU converted to USD)	Data unavailable.
GDP per capita (SAAR, Nominal GDP in LCU converted to USD)	Data unavailable.
Sovereign credit rating (five-year senior debt)	Data unavailable.
Size of banking system	Data unavailable.
Size of banking system as a percentage of GDP	Data unavailable.
Size of banking system as a percentage of financial system	Data unavailable.
Five-bank concentration of banking system	Data unavailable.
Foreign involvement in banking system	Prior to the independence, the financial sector was separately owned by Russian, Austrian, and Prussian banks.
Government ownership of banking system	Data unavailable.
Existence of deposit insurance	Data unavailable.
<i>Source: Morawski 1996,48</i>	

Key Design Decisions

1. Part of a package: The FPIK package included direct aid to banks as well as government guarantees for foreign loans.

The original FPIK package in 1925 also included guarantees for foreign loans (PLN 1.0 million in 1925 and PLN 0.8 million in 1926), and the government could initiate the assistance in foreign currency, if necessary (Morawski 1996).

The FPIK was established on November 28, 1925, to rescue troubled banks and prevent potential systemic risk in the Polish financial system.

FPIK was terminated in May 1927, as the scheme was considered to have fulfilled its mandate (DURP 1927 nr. 46). However, as the credit market fluctuated during the Great Depression, the FPIK was reintroduced in 1931, and was incorporated into regulation in 1932 (Morawski 1996; DURP 1931 nr. 36). The FPIK kept supporting the Polish financial system during the inter-war period.

2. Legal authority: The FPIK was established by the Sanation Bill, which was passed on November 28, 1925. Though it was terminated in 1927, the scheme was reintroduced during the 1930s crisis and was incorporated as a regulation in 1932.

In September 1925, the Władysław Grabski government drafted the “Sanation Bill.” Some believed this bill to be based on the government’s experiences in operating the Bank Sanation Committee, which performed ad-hoc capital injections between September and October 1925. After Grabski retired in November, the new government led by Skrzyński took on and submitted the bill to Sejm (the lower house). The Sanation bill passed on November 28, 1925. The bill authorized the Minister of the Treasury to assist credit institutions through the Bank Gospodarstwa Krajowego (BGK), an existing national development bank, and granted 65 million złoty to the newly established FPIK (Morawski 1996). The Sanation Bill was part of “Sanacja” (Sanation), a political movement to address perceived corruption. The Sanation movement became particularly active after the May 1926 coup d’états.

The submitted bill, DURP 1925 nr. 119, Article 6.4 authorized the following features of the FPIK:

- The sunset date of the FPIK: The end of 1927;
- The eligibility for financial institutions: Credit institutions which displayed economic need;
- The collateral conditions: The assistance was subject to appropriate collateral in the form of the (i) loans, (ii) guarantees, or (iii) “other financial operations that will prove necessary” in the liquidation of liabilities;

- The arrangements on the detailed terms of the loan (the interest rate, the method of calculating interest, the dates and manner of repayment of the principal, and others): To be determined by the Minister of the Finance;
- The size of the program: PLN 65 million.

Though the FPIK was terminated by the bill in May 1927, on March 17, 1931, a new law reinstated the program (DURP 1927 nr. 46; DURP 1931 nr. 36). The revived capital injection framework was mostly consistent with the original FPIK of 1925, but the size of the fund promised was significantly smaller. The new law in 1931 only authorized the FPIK to spend 20 million złoty for restoration of the financial system. Later critics have argued that the insufficient funds led to the failing of a few banks that had accepted assistance from the FPIK (Morawski 1996). In 1932, the FPIK, which had been implemented in the form of ad-hoc bills (with expiration dates), was finally incorporated into a regulation (DURP 1932 nr. 94; Morawski 1996). Reflecting the lessons the government had learnt from the past injections, the collateral condition was eased, including state guarantee, and the State Treasury (within a fixed quota of PLN 20 million) (DURP 1932 nr. 94). Furthermore, the regulation also newly assured more flexibilities to the Minister of the Finance, enabling receivable redemptions and any other changes in the design of the capital injection if deemed necessary.

The regulation in 1932 did not have a specified sunset date. Morawski (1996) notes that capital injections undertaken on the basis of the 1932 regulation were much more effective than those under the ad-hoc 1931 bill. He also notes that the legal framework and the operation became more complex involving a multi-level combination of reliefs, allowances, guarantees, loans, and ownership changes. The regulation was amended in 1935 (DURP 1935 nr. 85).

3. Governance: The establishment of the FPIK, as well as the earlier Bank Sanation Committee, was initiated by the government, mostly by the Ministry of Finance. By contrast, the Bank Polski, the central bank, had little involvement despite its financial stability mandate.

The establishment of the FPIK, as well as the Bank Sanation Committee, was initiated by the government, mostly by the Ministry of Finance. By contrast, the Bank Polski, the central bank, had little involvement despite its financial stability mandate.

The Governance of the Bank Sanation Committee

On September 21, 1925, the government established the Bank Sanation Committee under the leadership of the Deputy Minister of Treasury and a member of the BGK Council, Józef Karśnicki. The Committee was composed of two delegates of the Ministry of Treasury and one delegate from each of Bank Polski SA (the central bank), BGK, and Związek Banków w Polsce (ZBwP, the Polish Bank Association). Ad-hoc assistance was to be provided to eligible banks through BGK on the order of the Ministry of Treasury.

BGK

BGK was an existing government development bank which was established by a merger of three public Galician banks (Polski Bank, Krajowy Bank for Reconstruction, and Zakład Kredytowy Miejski Małopolskie) (Landau 1993). It grew significantly over the inter-war period by assisting governmental state-led economic policies (Mazur 2018).

The Governance of the FPIK

Similar to the Bank Sanation Committee, the creation of the FPIK was initiated by the government. The FPIK was operated through BGK as well (Morawski 1996).

Notably, the FPIK's capital injection was initiated by the government, not by the central bank, though the government originally argued that financial stability falls under the central bank's mandate. Two government officials, Henryk Kaden and Zygmunt Chrzanowski, strongly protested against the BGK directing the aid to banks when drafting the bill for the FPIK. In their opinion, such aid should be provided by the central bank. However, the Bank Polski refused to take on the role, and maintaining financial stability eventually fell to the government (Morawski 1996). Morawski (1996) explains and criticizes the central bank for being reluctant to participate in financial stability policies as it prioritized defending the currency.

- 4. Size: The first round of the FPIK in 1925 had PLN 65 million and 15 financial institutions had PLN 63.4 million capital injected. The second round of the FPIK in 1931 was much smaller in size: PLN 20 million.**

When the Sanation Bill was drafted in late September to October in 1925, the original intended size was 100 million złoty. However, when the bill was reviewed by the Sejm (the lower house), the amount was reduced to PLN 65 million (Morawski 1996). The FPIK injected PLN 63.34 million in capital in 15 financial institutions. In the second round in 1931, the size of the FPIK was reduced to PLN 20 million.

- 5. Timing: The bill that established the FPIK in 1925 expired in 1927, as the government determined that the capital injection scheme had fulfilled its goals. After FPIK's revival in the 1930s, it was incorporated into regulation without a specific expiration date. While the bills or regulations did not determine the timing of capital injections, most financial institutions seem to have received assistance right after the bill in 1925 passed.**

On May 17, 1927, the FPIK was terminated as the President of the Republic of Poland determined that the financial crisis in 1925 was over and the FPIK had fulfilled its goals (Morawski 1996; DURP 1927 nr. 46). In 1932, the FPIK, which had been implemented in the form of ad-hoc bills (with expiration dates), was finally incorporated into a regulation (DURP 1932 nr. 945; Morawski 1996). The regulation in 1932 did not have a specified sunset date.

While the bills or regulations did not determine the timing of capital injections, most financial institutions seem to have received assistance right after the bill in 1925 passed. Although there were no specific legal requirements of constraints in the timing of the FPIK assistance, the capital was quickly injected. The swiftness was partially due to the government's fear that if the FPIK did not intervene soon enough, foreign investors could take over private Polish banks. This concern materialized during the Great Depression; foreign shareholders in Polish banking grew as a result of taking over the share capital of credit institutions indebted to foreigners (Landau 2007).

6. Source of funds: The government had a difficult time securing the funds for the injection and met the needs with seigniorage and foreign debts.

Throughout the inter-war period, the government seems to have faced difficulty in securing the funding for the FPIK. Particularly, during the crisis in 1925 and the 1930s, the economy and the fiscal balance deteriorated significantly. For the Bank Sanation Committee established in September 1925, the government managed to grant PLN 25-28 million only from issuing new coins and raising the seigniorage (Morawski 1996). Landau (2007) suggests that part of the FPIK funding was also provided by the government's foreign debts.

According to Wierzbicki (n.d.), the long-term loans granted by BGK came from two sources. One was the BGK's own funds, while the other was the state funds received by BGK, the purpose of which was precisely defined by the government. Article 7 of the Decree of the President of the Republic of Poland of May 30, 1924, also clearly stated that "funds allocated from the state budget for credit purposes, unless they are directly available to the state authorities, may only be administered by the Bank [BGK]." In practice, however, it was quite often the case that BGK did not receive funds from the state to finance certain tasks and thus granted the state an informal loan. The government's repayment of this loan in the event of a budget deficit could vary. In the first months of its operation, BGK did not have sufficient funds to develop a long-term loan. The scale of this type of financing in the inter-war period is best illustrated by the figures. Between 1924 and 1938, BGK granted long-term loans amounting to nearly 2 billion zlotys. The majority of this sum came from deposits from the Ministry of Treasury and funds serviced by BGK from state special-purpose funds, although the exact separation of these two sources also depended on the method of accounting in balance sheets. There were cases where long-term and issue loans were booked as coming from the bank's own funds, despite the fact that these loans were partly realized through the purchase by the state of securities issued by BGK and government deposits. Thus, the majority of long-term loans granted by BGK between 1924 and 1938 came from the bank's own funds (PLN 1,095 million) and PLN 895 million from state resources.

7. Eligible institutions: Larger banks were prioritized given the limit of fiscal space in the government.

While the eligibility was only loosely defined in both 1925 and 1932 regulation on FPIK, not all financial institutions could participate in the FPIK (DURP 1925 nr. 119; DURP 1932 nr. 94). The government was selective given the limit of the available funding.

Furthermore, the government intended to leverage the scheme to increase the efficiency in the credit market, by forcing smaller and weaker banks to exit.

The first round of FPIK excluded small-credit institutions. This was due to two reasons. First, given the tight budget, the government lacked fiscal space to support all financial institutions. The government prioritized large banks over smaller ones. Second, the government hoped that the smaller and weaker financial institutions would exit from the credit market, given the over-competitive nature of the credit market (Landau 1993; Landau and Morawski 1995). The government did not intend to provide assistance to credit institutions that were not in the state's interest, focusing on providing substantial assistance to institutions that were essential for servicing the national economy (Landau 2007). Most smaller financial institutions were involved in various currency operations and were not much involved in lending or the credit market, and thus did not meet the interest of government support (Landau 1993). Figure 1 below shows the capital injection deployed by year and month, and Figure 2 below shows recipients of the capital injection.

Figure 1. Aid installments by Bank Sanation Committee and the FPIK (first round in 1925; as of December 31, 1926)

	Aid installments (in million PLN)
1925	
September	10.2
October	16.7
November	5.5
December	8.2
1926	
January-June	20.5
Total	61.1

Source: Morawski 1996.

Figure 2. Debtors of the FPIK (first round; as of December 31, 1926)

Bank Name	The Amount of the Debt (in min PLN)
Bank Handlowy w Warszawie SA	21.7
Bank Ziemiański SA w Warszawie	8.5
Polski Bank Przemysłowy SA we Lwowie	7.3
Bank Małopolski SA w Krakowie	6.9
Bank Przemysłowców SA w Poznaniu	6
Bank Związku Spółek Zarobkowych SA w Poznaniu	5.2
Ziemiański Bank Kredytowy SA we Lwowie	3.3
Polski Bank Komunalny SA w Warszawie	1
Bank M. Stadthagen SA w Bydgoszczy	0.9
Dom Bankowy T. Bunimowicz w Wilnie	0.7
Wileński Prywatny Bank Handlowy SA w Wilnie	0.6
Bank Przemysłowców Polskich SA w Warszawie	0.5
Śląski Bank Przemysłowy SA w Bielsku*	0.5
Bank Zjednoczonych Ziem Polskich SA w Warszawie	0.3
Bank Handlowo-Przemysłowy SA w Łodzi	0.1**
Total	63.4
*During the merger with Polski Bank Przemysłowy SA in Lviv.	
**Debt fully repaid by the end of 1926.	

Source: Morawski 1996.

The FPIK in 1931 and afterwards seemed to have had a similar criterion: prioritizing larger, significant private banks before the smaller ones. In 1931, the aid was granted to the following five banks: Polski Bank Przemysłowy SA in Warsaw, Bank M. Stadthagen SA in Bydgoszcz, Bank Ziemiański SA in Warsaw, Pomorskie Bank Rolnicze SA in Toruń, and Bank Ziemiański SA in Poznań (Morawski 1996). Morawski (1996) also suggests that the government increased its efficiency in capital injections and officializations, learning lessons from the capital injections in 1920s.

8. Repayment/debt restructuring plan: As well as the capital characteristics (e.g., interest rate), the Finance Minister was granted an autonomy in determining the details of repayment.

As well as the capital characteristics (e.g., interest rate), the Finance Minister was granted autonomy in determining the details of repayment (DURP 1932 nr. 94). While not much information is available on the actual repayment by banks, according to Stelmach (2012),

financial institutions started paying back as early as June 1926 after the first FPIK assistance in 1925.

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