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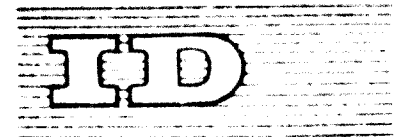
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THE FINANCING OF INDUSTRIAL ENTERPRISES IN THE PUBLIC SECTOR IN SYRIA^{1/}

by

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^{1/} The views and opinions expressed in this paper are those of the author and do not necessarily reflect the views of the secretariat of UNIDO.

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**THE FINANCING OF INDUSTRIAL ENTERPRISES IN THE
PUBLIC SECTOR IN SYRIA**

PART ONE

THE FINANCING OF THE STATE INDUSTRIAL ENTERPRISE

In the first part of our study we shall explain the investment policies of the Syrian Government regarding the public industrial sector. We shall then examine the domestic and external sources of financing for public industrial enterprises. This analysis will lead to an assessment of the cost of the capital required by these enterprises, compared with its profitability. It will also help us to identify the advantages and disadvantages of each source of finance. We shall then be in a position to indicate the criteria for establishing an order of priority among the various sources of finance available.

We think it worth pointing out that the industrial sector is of recent creation and dates from the end of the Second World War. The sector has been nationalized since 1965. The nationalized capital represents about 65 per cent of total capital invested in industry. The public industrial sector has consequently become of leading importance in the country's economy.

1. Policies regarding investment in the public industrial sector

Industrial development policy forms part of the total economic and social development policy of the régime in power. The appropriate form of industrial development has been indicated in the "Action Programme" of the "Al Baath" party^{1/} published on 22 July 1965. The main ideas are enshrined in the second Five-Year Plan (1966-1970) which is at present being implemented. All the successive Governments from 1965 to the present time have tried to give effect to the Action Programme mentioned above.

Under the 1965 Action Programme and also under the second Five-Year Plan (1966-1970), industrial investment must be aimed at the establishment of a solid

^{1/} The party in power in Syria since the "Revolution" of 8 March 1963.

industrial basis in the country, and at hastening the process of rapid industrialization. Industrial investment in the public sector will thus be approved on the basis of a strategy of industrialization and an order of priorities taking into account the following considerations:

- Facility of access to the natural resources of Syria's soil and sub-soil;
- The degree of development of the energy needed both for production and for consumption;
- The growth and development requirements of the agricultural sector;
- The expansion of exports and reduction of imports;
- The consolidation of national development potential;
- Satisfaction of the requirements of the Arab Common Market, and the achievement of economic complementarity among Arab countries.

In line with these principles, 348 million Syrian pounds, or more than 40 per cent of total State investment under the Second Five-Year Plan, were allocated for investment in the public industrial sector under the Plan.

In making these investments, the Governments in power since 1965 have been concerned with the more or less immediate profitability of projects and availability of the necessary foreign exchange. They have sought to take advantage of the country's mineral resources (phosphates, rock salt, hydrocarbons, petrochemical industries, iron, etc.) and of the possibilities of processing them locally. They have given particular priority to projects likely to result in substantial savings of foreign currency, and projects capable of providing immediate foreign exchange earnings. They have sought in this way to intensify the growth of exports of manufactures, to widen their range and to reduce the volume of imports. They have also tried to increase the production capacity of industrial enterprises in the public sector, and, in addition, to ensure their balanced development and constant improvement. They have given preference to industries employing a relatively large amount of unskilled labour and a relatively small volume of capital. They have avoided hampering projects in process of implementation on account of limitations of foreign currency reserves.

2. Sources of financing

At the present time, there is no code of financial regulations governing industrial enterprises in the public sector in Syria. However, the reorganization of the public industrial sector which took place under Decree-Law No. 21 of 1 March 1967 and the budget reform brought about by Decree-Law No. 92 of 19 July 1967 give an indication of the basic principles regarding the financing of such enterprises

In accordance with Decree-Law No. 21 of 1967, the industrial enterprises in the public sector have been grouped together in three federations ^{1/} Article 30, concerning the finances of the enterprise, provides that the profits of each enterprise shall be distributed as follows:

- 25 per cent to the workers;
- 75 per cent to the State.

The share of the State will be transferred to the federation to which the enterprise belongs. On the other hand, articles 11 to 14 of Decree-Law No. 21 of 1967, concerning the finances of the federation, reads as follows:

" Art. 11. The fixed funds of the Federation shall consist of:

- a. The share subscribed by the State to the capital of the enterprise belonging to the Federation;
- b. The amounts allotted to the Federation by the State under the allocations in its economic development budget.

" Art. 12. The Federation's investments shall be financed, within the limits of the plan and the economic development budget, from the following sources:

- a. The share of the profits of the enterprises due to the State;
- b. The reserves of the enterprises (compulsory and optional reserves);
- c. Amortization of the fixed assets of the enterprises;
- d. Foreign credit facilities;

^{1/} These federations are concerned with spinning and weaving, the food industries, and the engineering and chemical industries respectively.

- e. The amounts assigned to the Federation by the State under the development budget.

"Art. 13 The Federation shall utilize the sources indicated in the preceding article, within the limits of the State development budget, for the following purposes:

- a. Increasing the capital of existing enterprises;
- b. Creating new enterprises and participating in the share capital of these enterprises;
- c. Modernizing, replacing and expanding the fixed assets of enterprises;
- d. Covering the administrative overheads and costs of establishment of the Federation;
- e. The specific expenditures necessitated by the tasks entrusted to the Federation under the laws in force.

"Art. 14 The surplus deriving from the difference between the finance available in accordance with article 12 and the amounts utilized under the terms of article 13 shall be regarded as 'State development budget receipts'."

The legal provisions quoted above clearly do not provide solutions to all the problems relating to the financing of industrial enterprises in the public sector, or of the federations. In particular, there are no provisions regarding the sources of financing for the current operations of the enterprises, their circulating capital, their stocks, and their losses if any.

Even the text of article 12, concerning sources of finance for investments, does not by any means list all the available sources, such as medium-term and long-term credit, grants and donations of equipment, private savings, etc.

If we turn to the provisions of Decree-Law No. 92 of 1967, we note once again the incompleteness of the provisions and their ambiguity. These texts provide that the receipts and expenditures of industrial enterprises in the public sector are to appear in the budget of the federation in accordance with their financial regulations, though these do not yet exist (article 2). When the federation's

accounts show a positive balance, it is to be transferred to the State budget under the heading "receipts". In the contrary case, the State is to cover the deficit by means of a grant which appears under the entry "expenditures under the State budget" (article 5, para. 1). Allocations for the investment costs of industrial enterprises in the public sector are provided for in the general State budget with the understanding that the amortization charges of these enterprises are to be paid into the general State budget under the heading "receipts" (article 5, para. 2). What problems are posed by the interpretation of these texts and their co-ordination with many other texts on the same subject?

As there are not enough clearly worded laws and regulations on this subject, one needs a consolidated balance-sheet covering all the enterprises of the public industrial sector in order to be able to pass any judgment on their sources of financing. Such statistical data do not yet exist. We have, however, been able to obtain a sample balance-sheet for an industrial enterprise in the public sector, and this has been annexed to the present study. This sample balance-sheet will enable us to clarify certain aspects of the question of sources of financing.

We must, however, point out that, in present circumstances, the financing of enterprises is ensured in different ways from one enterprise to another and the sources and means of financing differ. The current operations of the enterprises are mainly financed by bank loans. On the other hand, investments proper are financed from a variety of domestic and external sources. We will consider in turn:

2.(a) Domestic sources

2.(b) External sources

2.(a) Domestic sources of financing

These sources can be grouped in three different sectors:

- (i) The public sector (the State and banks);
- (ii) The private sector (bond issues);
- (iii) Auto-financing (resources of the enterprise itself).

i(1) Financing of capital formation on a grant basis

The system of financing capital formation is guided by the concern to maintain balanced growth of the various branches of the public industrial sector.

The basic guidelines for development of the public industrial sector are set out in the economic development plan. In addition to this plan, a development budget is drawn up each year fixing the allocations for the public industrial sector. The allocations in the annual budget must be in conformity with the objectives and guidelines of the development plan. These funds are made available to enterprises through the National Debt Agency (Organisme de la Dette Publique), which in this regard performs the role of an investment bank. We should mention that the enterprises can utilize only the sums placed at its disposal by the National Debt Agency. Reimbursement of these sums by the enterprises is hardly ever required. The statutory allocation in this form emphasizes the system of socialist ownership of the means of production.

The conditions of financing of industrial enterprises from the State budget can thus be summarized as follows:

- Conformity of the investments: with the economic development plan;
- The investments must go towards the formation of the fixed capital of the enterprises;
- The investments must be provided for in the annual development budget;
- The credits are made available without any limitation of duration and on a grant basis;
- The profits of the enterprises are transferred to the development budget.

i(2) The financing of enterprises by bank credit

As we mentioned above, the financing of industrial enterprises in the public sector in Syria is mainly ensured through bank credit.

In addition to traditional operations, the Industrial Bank of Syria has, over the last few years, developed its direct medium-term and long-term credit facilities in order to ensure better adaptation of its loans to the needs of public enterprises and thus to help improve their financial structure.

The sample balance-sheet annexed, which is not as well set out as one would wish, shows that medium-term and long-term bank credit accounts for more than 29 per cent of the balance-sheet total. Short-term credit account for 14 per cent of the total.

Thus the total contribution from banks represents 43 per cent of the balance-sheet total and corresponds to double the capital of the enterprise (not taking into account the losses to be deducted).

A comparison of the banking contribution of the preceding year with that of the current year in the annexed statement of balance sheet reveals that the enterprise frequently diverted the short-term credits which it received from their original purpose and used them for investment. Thus, from the first year to the second, medium-term and long-term credit increased by 11 per cent at the expense of short-term credit, which fell by 22 per cent. Meanwhile, the capital of the enterprise and the fixed assets remained unchanged. These variations in volume between medium-term and long-term credit on the one hand and short-term credit on the other reflect a modification in the nature of the credit granted to the enterprise in order to enable it to improve its financial structure. In other words, the short-term credits made available to the enterprise were converted into medium-term and long-term credits.

The above-mentioned balance-sheet data cannot of course be generalized to apply to all industrial enterprises in the public sector. The volume of bank financing and the form it takes differ from one enterprise to another. However, the Industrial Bank of Syria, the only bank concerned at the present time for financing the industrial sector, has had to cope with a threefold movement since 1967: a trend towards an increase in the credits granted to enterprises, an extension of their duration and diversification of their form. According to a recent statement by the President-Director-General of this bank, 90 per cent of the loans made available are utilized by the public industrial sector.

After this brief review of the present role of bank credit in the financing of industrial enterprises in the public sector, we feel that it will be useful to consider in greater detail the existing rules of financing, the main provisions of

the proposed new regulations regarding the distribution of credit extended to the public industrial sector, and finally the difficulties which beset financing operations.

The existing state of bank financing

There are no special regulations at the present time governing bank financing for industrial enterprises in the public sector. Such regulations are currently being drafted. Up to the present time, the rules of industrial financing have been applied to the public sector and the private sector without distinction. These rules are the same as those applied in the granting of bank loans in general. Loans are approved on the basis of the solvency of the beneficiary, his capacity to repay, and the real needs of the enterprise. A ceiling and a duration are established for each category of credit. In no case is the contribution from the bank exceed 90 per cent of the net assets of the enterprise. In addition, bank credit is granted subject to a general mortgage in favour of the bank on all the fixed assets of the enterprise. Pledged goods must be deposited at the bank. Seasonal credits are granted for 300 days in order to cover the regular needs of the enterprise for circulating capital at the minimum cost. These credits can be mobilized at the Central Bank; they are repayable in monthly or semi-monthly instalments. Regular credits are granted in the form of open current account credits, or against security consisting of personal or real property, or also in the form of discount and guarantee credits. There is no control over the use made of the credits granted to the enterprise. In addition, no penalty is imposed on an enterprise in the case of failure to repay on the due date.

Since 1967, efforts have been made to introduce more flexibility in the conditions of industrial credit granted to the public sector. These efforts have taken concrete form in draft regulations on the granting of credit to industrial enterprises in the public sector. The draft has not yet been approved. In any case, it must be recognized that there is still much room for improvement in this field.

The proposed regulations on industrial credit

The committee entrusted with the task of preparing regulations on industrial credit has been concerned to link the banking operation with the production

operation itself. Thus for each stage of production there will be a category of ad hoc credit. On the basis of this principle, the various categories of industrial credit may be envisaged as follows:

- Fixed capital assets (land, buildings and construction work, plant, tools, transport vehicles, furniture, fittings and fixtures, intangible assets, etc.) will be financed from the enterprise's own capital. In cases in which the funds of the enterprise are insufficient, long-term credits could be granted. These credits will be fixed by the State in the annual plan for the distribution of credit and in the annual investment plan.
- Products in process of manufacture will be financed either from the funds of the enterprise itself or by medium-term and long-term credits. Determination of such products will be based on technical principles and take into account the production capacity of each enterprise and its own annual production plan.
- Stocks of raw materials and finished products below the technically established norms will be financed by means of short-term credits (crédits de campagne). These credits will be fixed annually within the limits of the annual plans for industrial production and distribution of credit.
- Stocks of spare parts below the technically established norms will be financed by means of medium-term credit.
- The general overheads of the enterprise will be financed by current account credits. The volume of funds will be fixed annually within the limits of the requirements of the enterprise, taking into account its financial plan and the annual plan for the distribution of credit.
- Marketing operations will be financed by discount credits.

The various categories of industrial credit indicated above naturally depend on the availability of adequate statistical data and on general economic planning. They also require qualified personnel capable of carrying out valid financial studies. These conditions are not yet satisfied. In any event, it is not the task of the present study to discuss this concept of industrial credit. We have merely described it in order to give an idea of future trends.

However, the committee responsible for drawing up the new regulations on industrial credit admitted itself that it is hardly possible at the present time to put such a concept of bank credit into practice. During the present transitional stage, the committee propose the following principles for the distribution of industrial credit:

- Bank financing will be based on the needs of the enterprise for liquidity.
- Bank financing will be granted only when the enterprise is in a healthy financial situation and can offer every guarantee of repayment of the credit on the due date.
- Bank credit will be supervised to ensure that it is not diverted from its original purpose.

To implement these principles, the committee proposed a number of measures. Thus, the needs of the enterprise for short-term credits will be determined on the basis of the annual production plan, the annual financial plan and the annual plan for the distribution of credit. The needs of the enterprise for medium-term and long-term credits will be determined according to the objectives of the economic development plan. This category of credit will be granted only for the establishment of new industries or the expansion of existing industries.

The study of the financial situation of the enterprise will be subject to the traditional rules in this regard. The study will be based on the balance-sheet of the enterprise, its profit and loss account and its financial regulations. To guarantee the possibility of repayment of the credit on the due date, certain ratios will be fixed. The situation concerning stock, current economic trends and supply and demand conditions will also be taken into account.

Control over the utilization of the credit will be effected either on the spot or on the basis of the account of the enterprise with the Industrial Bank.

Where the finances of the enterprise are not in a satisfactory state, or the enterprise has diverted the credit granted to other uses, the committee proposes that economic sanctions should be imposed.

These sanctions may take the form of an increase in the interest rate, suspension of the right to utilize the credit, cancellation of the credit and, where appropriate, legal proceedings.

In addition, the committee proposed that public enterprises should be given certain advantages over enterprises belonging to the private sector. Thus, for public enterprises there will be no limitation on the level of bank financing in relation to the capital of the enterprise. Public enterprises will also be exempted from the obligation to offer security in the form of real property or a mortgage. The guarantee of the financing to which the enterprise belongs will be sufficient. In addition, assets placed can be kept in the depositaries of the enterprise. Interest rates will be lower than those applied in the case of private enterprises.

The difficulties involved in bank financing

Several difficulties have arisen in the attempt to meet, through the formula of bank financing, the substantial requests of industrial enterprises in the public sector for loans for their various purposes. These difficulties relate especially to the procedures for cooperation on the side of the enterprise and the bank, and the conditions laid down by the bank for the granting of loans.

The first difficulty which any entrepreneur has to do with the background elements which the bank requires in order to satisfy itself as to the regularity of the operations to be financed by the credit requested. In general, the managerial staff of the enterprise are more concerned with problems of production and marketing than with those of financing.

They leave the chief accountant to solve these problems. In result, the bank does not receive the balance-sheet, trading account and profit and loss account of the enterprise until after a short or after a serious delay. It is consequently difficult to obtain documentation on the exact situation of the enterprise. On the other hand, the enterprise often requests credit at the last minute, when it finds that its funds are proving insufficient. The bank cannot take a properly based decision in such cases. It has no room for manoeuvring effectively with the enterprise. Consequently, credit is only granted because the enterprise is part of the public sector, and not because it deserves the credit requested.

A second disadvantage is inherent in the limited funds of certain enterprises. This situation is due to their steadily increasing use of bank credit, sometimes

to finance losses and often to finance investment in industrial expansion. The industrial enterprises in the public sector are resorting more and more to investment credits from the banks, because this mode of financing seems convenient and flexible. The time allowed for repayment and the guarantees required are not very exacting.

Since they share the same interests, it would be very logical for the director of the enterprise and the director of the bank to discuss their problems in a candid dialogue, in which solutions would be found to the momentary difficulties which are inevitable in the life of an enterprise, even if it is part of the public sector.

We feel that excessive recourse to bank credit, though it seems at the present time the most convenient means of financing the requirements of public industrial enterprises, could jeopardize the financial equilibrium both of the enterprises and of the banking system.

To remedy this situation, we suggest that the financing of industrial enterprises should be linked with a planned system with regard to sources of financing and the purpose of the finance. The annual investment plan could fix the total volume of bank credit, the various types of credit to be granted, their distribution by federation and by industrial enterprise, the means of controlling their proper use and the sanctions to be imposed if necessary. Bank credit could then become a valuable source of financing for industrial enterprises without undue risks.

(ii) The mobilization of private savings for the financing of the public industrial sector

Since the socialist transformation in 1963, private savings have lost their function as a source of industrial investment in Syria. Yet it was to private savings that Syria owed the establishment of an industrial sector after the Second World War. The nationalization of industries in 1965 and the failure up to the present time to reimburse the former shareholders of the nationalized companies have increased the anxieties of private capital. Any attempt to mobilize private savings would be received with very little sympathy at the present time.

Prior to 1963, the confidence of private capital was mainly based on two types of consideration. Firstly, share prices were rising steadily, this being linked

with the high dividends paid by industrial enterprises. We must also take into account the fact that the dividend rates were fixed after the setting aside of considerable funds for depreciation and auto-financing.

Secondly, the public was taught to devote some of its resources to savings rather than to consumption.

The situation has now been reversed. The public has come to show a preference for consumption expenditures stimulated by dynamic advertising on the part of merchants and by facilities for installment payments.

To safeguard future progress, however, we believe that private savings must retain their share in the financing of investment in the public industrial sector. This formula has the advantage of transferring part of the costs of industrial development which are now borne by the State and by credit institutions to traditional financial channels. It will thus be possible to absorb a not inconsiderable amount of floating liquidity and in this way to restore to private savings the role that they have lost in recent years.

The question then arises, however, whether this change is possible - in other words, whether the public will accept it and prefer the purchase of treasury bonds or bonds issued by industrial enterprises in the public sector to cash hoarding, for example, or current accounts with banks.

There seems to be several obstacles in the way of this highly desirable development. First there is the absence of any legislation on this subject. Next, we feel that it would be important to restore the confidence of private savers by reimbursing the dispossessed shareholders on a fair basis. General price trends also cause some concern, although there is no threat to the stability of the currency. Lastly, many modern schemes for mobilizing small-scale private savings, all based on a thorough knowledge of the needs and resources of private individuals, have been adopted in other countries and might as fully be introduced in Syria.

This should be the approach to the problem of mobilizing private savings for investment in the public industrial sector in Syria. The removal of mistrust and the creation of incentives may help in future to give its due place to private

capital in the financing of Syrian industry. There is no need to emphasize the necessity for bridging the gap between savings which at present are being held back and the requirements of industrial investment.

(iii) Auto-financing

In a developing economy, auto-financing is the dynamic equivalent of the static concept of financial autonomy: in particular, it is auto-financing which enables the industrial enterprise to turn to other sources for the essential supplementary financing of the investments required for its growth.

With regard to Syria, and particularly the industrial enterprises in the public sector, we should distinguish between two types of auto-financing: that adopted by the nationalized enterprises and that used by the new State enterprises recently established. In the case of the former, auto-financing is always applied in its various forms: depreciation charges, optional or compulsory reserves, investment reserves and other kinds of reserve funds or provisions.

In the case of new State enterprises, these sums are paid into the State budget. The absence of financial regulations governing industrial enterprises in the public sector is the main reason for these disparities in the auto-financing procedures of the two types of enterprises.

The sample balance-sheet annexed to this study shows that the write-offs for depreciation were made before the profit and loss account was drawn up. This element of auto-financing is included under the general overheads of the enterprise, or, one might say, the production cost. The write-off rate is not indicated, but it appears that the rate is variable and depends on the nature of the item concerned. Furthermore, the balance-sheet annexed does not indicate what value is taken as the basis for write-off, the purchase value of the asset or the present value. We are inclined to think that it is the purchase value which is considered. The components of the depreciation write-off, according to the annexed balance-sheet, are very varied: land, buildings and construction works, tools, transport equipment, furniture, installations, finished products, raw materials, doubtful debts, costs of initial establishment and costs for research and experimentation. It is not

easy to tell from the balance-sheet how the amounts written off are used. Generally, these amounts are utilized by the enterprise either to finance working capital or to finance investments in renovation and expansion.

In addition to depreciation there is the profit and loss accounts of the nationalized industrial enterprises subject to the assignment of a share of the profits to compulsory reserves (5 per cent) or rather more to optional reserves (5-15 per cent) and a third share to reserves for renovation and expansion. The distribution of the profits of the enterprises could be illustrated as follows:

- Net profits		X	
- Compulsory reserves		- 10%	
	Remainder	Y	
- Optional reserves		- 5-15%	
	Remainder	Z	
- Reserves for renovation and expansion		- 25%	
	Remainder	A	
- Income tax		- 50%	
	Profit to be distributed	B	

We see from the foregoing that a share varying between 40 and 50 per cent of the net profits of the enterprises are devoted to auto-financing, covering, above depreciation charges and contingency provisions, etc.

The newly established State industrial enterprises have not yet begun operation. Moreover, no financial regulations have yet been drawn up to govern them. We therefore have no means of evaluating the results of auto-financing. However, as the fixed assets of these enterprises are financed on current basis from the development budget, Decree-Law No. 92 of 1967 provides that the depreciation charges of these enterprises are to be transferred to the State budget accounts. The profits of these enterprises are also to be transferred to the State budget receipts. It

1/ The net profits of enterprises, according to the Ministry of Finance, consist of the difference between operating revenues and operating costs after deduction of depreciation charges and contingency provisions, etc.

It is clear from the legal provisions involved that the depreciation amounts written off and the profits earned by the new State industrial enterprises must go first of all towards reimbursing the fixed capital originally provided by the State on the basis of a arbitrary grants. Thus the chances of auto-financing in the new State enterprises are not high. It is urgent, therefore, to persuade the legislators to modify their position and give the important role to auto-financing.

A third formula could be found in the provisions of Decree-Law No. 21 of 1967 concerning the finances of the industrial federations^{1/}. We gather from the provisions of article 12 that the public enterprises must pay to the federation to which they belong the following sums:

- 25% share of the profits of the enterprises reporting to the State (75% of the profits for distribution);
- The amounts deducted from profits as compulsory and optional reserves;
- Amortization of the fixed assets of the enterprises.

Under the terms of article 13 of Decree-Law No. 21, mentioned above, the federation is to utilize the source of auto-financing referred to for the purpose of increasing the capital of the enterprises, the modernization of their fixed assets, and for other purposes.

It can be seen from what has been said that the system of industrial auto-financing is unorganized or the one and not the other. The policy of the government is not yet settled with regard to this problem. Experience and developments in the industrial sector over the coming years may lead the State to adopt a more sympathetic and realistic attitude towards auto-financing.

2. (2) Financial sources of financing

The Action Programme of the Arab Socialist party published on 23 July 1965 is regarded as the central document in Syria's political, economic, legislative and social life. We should therefore refer to this Action Programme in seeking to identify the policy of the government regarding the use of loans and facilities accorded by foreigners for industrial development in Syria.

Under the Action Programme, national savings are regarded as the basic source of financing for industrial investment under the responsibility of the State.

^{1/} See items 5 - 7 above.

However, as national savings are necessarily limited, the State will resort also to loans and credit facilities granted without conditions by third countries and by all friendly countries. Such loans must be used, however, as secondary source of financing; it is to supplement national resources, not to be attracted in specific cases, as is to be decided by the competent authorities. This foreign capital will also be subject to the laws and regulations in force in Syria and subordinated to the State. In order to deal with the steadily increasing the circumstances of each particular case, as also required, in addition to loans and credit facilities from abroad, the Action Programme also provides for the possibility of concluding trade and economic co-operation agreements with all friendly countries on the basis of mutual respect for national sovereignty. The aim of these agreements will be to ensure the supply of the equipment and plant needed for industrialization and, on the other hand, to promote exports of Syrian manufactured products.

After stating the position of the national economy, foreign investments, the Action Programme emphasized the need to introduce a "law" for private and public, Arab and foreign investments. The law should lay down the conditions relating to foreign investment, and the rights and duties of those providing funds, and also to safeguard and ensure the inflow of foreign capital.

On the basis of these principles, the Ministry of Economic Affairs and Foreign Trade prepared a draft decree-law concerning foreign investments and laying down the rights and duties of countries providing capital. Although it was drawn up in 1967, action has not yet been taken on the draft. Consequently, there is still no law dealing with foreign investments in Syria. The only regulation in force is Order number 2146 of 25 November 1960 issued by President Abdel Nasser at the time of the union of Syria and Egypt. The provisions of this Order are now reported in a dated letter.

It is the Council of Ministers, the supreme political and legislative authority of Syria, which decides on the contribution of foreign capital in each particular case. Its decision takes the form of a decree-law, statute, other agreement, a freely negotiated contract or a contract which is the subject of an international award.

External aid is also provided in the form of loans in kind (factories, capital equipment, tools, etc.), the loan of technicians, short-term and long-term credit facilities, and direct or indirect financial assistance. We shall consider in turn:

- (i) The contributions of international institutions and friendly countries;
- (ii) Contributions in the form of association between foreign and Syrian undertakings

(1) (1) The contribution of international financial institutions to industrialization programmes

Syria has not received large amounts of capital from the specialized agencies of the United Nations system or from international financial institutions for investment in its industry.

Despite its membership in the United Nations and the specialized agencies, the benefits reaped by Syria have so far been meagre. From 1963 to 1968, assistance from these institutions has taken the form of 217 experts, 50 fellowships and a contribution of US\$55,000, the cost of a few installations. On the other hand, the Special Fund has helped in the financing of the food industries project and in the establishment of an industrial management and productivity centre, an industrial research centre and the Damascus Industrial School.

We feel that Syria should take a greater interest in obtaining assistance from international financial institutions. Indeed, this is its right. To achieve this end, Syria should take certain measures of such a nature as to attract foreign capital, including:

- Preparation of a detailed plan covering its requirements for capital and foreign technicians to assist in industrial development. The plan will be kept strictly in line with the likely trends in its balance of payments over a determined period. The plan should also be designed to encourage foreign countries and international institutions to offer Syria financial co-operation;
- Providing those who request it with any documentation on the economic riches of Syria and its potential for development

- Putting an end to the false notion of "the limited capacity of Syria to absorb loans and facilities from outside" by bringing industrial projects to the attention of the world through a commercial and technical publicity campaign, and assuring contributors of capital that the requirements of national defence in Syria will in no case interfere with strict fulfilment of its commitments
- Periodical publication of statistical data on the volume of Syria's external commitments, current trends, and interest payments and capital reimbursements made;
- Simplification of the administrative and technical formalities governing the negotiation of foreign loans and their approval by the Syrian competent authorities;
- The introduction of a code governing foreign investments

(i) (2) The contribution of foreign countries to industrialization programmes

Apart from international institutions, foreign sources which can assist in the financing of the public industrial sector in Syria may be grouped as follows:

- a. The Arab countries;
- b. Other friendly countries;
- c. Foreign banks;
- d. Foreign suppliers

a. The Arab countries

Neither within the framework of the Arab League (Arab Economic Development Fund) nor of Inter-Arab co-operation (Kuwaiti Development Fund) has Syria been able so far to obtain any assistance in the financing of development projects in general and public industrial investments in particular. Syria has, however, made commendable efforts to remove the difficulties which have so far hindered the inflow of Arab capital to finance industrial projects in the public sector in Syria. The signature of an agreement guaranteeing Arab capital contributions, the establishment of an inter-Arab agency to insure Arab investments against specific risks and the establishment of an inter-Arab committee to solve differences

concerning such investments through conciliation and arbitration are all desirable steps which would, in our opinion, encourage and promote the introduction of Arab capital in Syria.

b. Other friendly countries.

During recent years, Syria has expanded its economic and technical co-operation with other friendly countries, and particularly with the USSR, Czechoslovakia and the other people's democracies. Bilateral agreements have been signed with these countries stipulating the nature of the loans granted, conditions, procedure for repayment and the rights and reciprocal duties of the two parties.

Despite the importance of bilateral agreements concluded with friendly countries, it has hardly been possible for Syria to utilize the medium-term and long-term credit placed at its disposal to the extent of more than 20 - 40 per cent. The fault lies partly with the competent authorities in Syria which have not yet properly organized the administrative offices responsible for the task of deriving all the possible benefits from the agreements concluded.

Within the framework of these agreements, it has been possible to finance several current industrial projects. Mention may be made of the nitrogenous fertilizer plant (contribution of the USSR, Czechoslovakia and Italy), the phosphate processing plant at Knafiss (American contribution), the rock-salt processing plant (Spanish contribution), the ammonia dehydration plant (French contribution), the plant for fine cotton yarn (contribution from the People's Republic of China) and the plant for the manufacture of rails (contribution of Poland). The total cost of these plants is estimated at about US\$50 million.

The main provisions of the economic co-operation agreements signed with friendly countries may be broadly summarized as follows:

- The country providing resources places at Syria's disposal a credit denominated in dollars or sterling to be utilized over a period of 3-5 years;
- The credit is to be used for the purchase of capital goods, complete plants and spare parts and for the supply of technical and other services originating in the creditor country;

- The prices for plants, equipment and supplies are to be fixed on the basis of comparative prices prevailing on the international market, taking into account quality, technical specifications and delivery date.
- A part (20-50%) of the credit used is repayable in Syrian industrial or agricultural products or in other merchandises.
- The balance of the credit used bears interest at a rate of 2-5% annually, and is repayable in 5-10 annual instalments, once the industrial project financed becomes operational.

It is under these conditions that Syria has been able, in recent years, to benefit from large scale co-operation from foreign countries.

2. Foreign banks

The contribution of foreign banks towards the financing of Syrian industrial enterprises is very limited. It is restricted to facilities for the confirmation of documentary import credit for the temporary uncovered period (travelling time) following the taking up of the documents, and especially the backing of bills payable in 3-9 months for the purpose of imports of raw materials for industry (yarn, dyes, etc.) and spare parts.

The contribution of foreign banks could have been much larger, particularly regarding short-term and medium-term financing, if Syria had made the necessary effort to obtain the support of banks with a world-wide coverage.

3. Foreign suppliers

The contribution of foreign suppliers is likewise very limited. In the sample balance-sheet annexed, the share of these suppliers in the financing of stocks of raw materials and spare parts is given as 10% of value.

It may be said in general that some foreign suppliers grant credit facilities for 3-18 months to Syrian industrial enterprises on condition that the relevant bills are backed at least by a Syrian bank. These enterprises are seeking at the present time to obtain such facilities without the intervention of a bank, and the operation sometimes takes the form of letter against products of Syrian origin, particularly cotton, petroleum and textiles.

(ii) The association of foreign capital with Syrian capital

This form of financing has not been used up to the present time in industrial enterprises in the public sector in Syria. Moreover, it will be subject to the foreign investments code which is still being considered by the Council of Ministers in the form of a draft for a decree-law, as mentioned above.

Some public sector enterprises in Syria, however, have entered into agreements with foreign enterprises for the use of their trade marks and formulas in exchange for quarterly commissions payable in foreign currency.

It is to be hoped that the future foreign investment code will find a solution to the problem of bringing together foreign capital and Syrian capital.

3. Cost of the capital required by enterprises and criteria for the choice of source

This first part of our study has shown that the sources of financing of public industrial enterprises are varied and consist of the following, in order of importance:

- Bank credits: the rates of interest charged to public industrial enterprises vary depending on the category of credit granted and its duration (short-term, medium-term and long-term). The interest rates also depend on whether it is possible to mobilize the credit with the Central Bank or not. The rates vary between 6 per cent and 7½ per cent a year.
- Fiduciary credits are made by the Government on a non-repayable basis for the financing of the fixed assets of newly established State enterprises. However, credits granted to nationalized industrial enterprises for financing new investments through the National Debt Agency bear interest at a rate varying between 3 per cent and 5 per cent a year.
- Auto-financing is the best method of financing since it is helped by the disappearance of competition between enterprises, and by a more or less steady increase in the selling prices of manufactured products. Its cost depends on the particular source of financing for which it is a substitute.

- Foreign loans and external facilities are granted at interest rates varying between 2 per cent and 5 per cent a year, leaving aside international financial institutions

The criteria for choosing between the different sources of financing mentioned above depend firstly on the purpose for which the enterprise is to use these funds and, secondly, on the capacities of the potential suppliers and their attitude towards the enterprise. We summarize this as follows:

Operations	Source of financing or instrument	Remarks
Fixed assets and investments in renovation, expansion, etc.	<ul style="list-style-type: none"> - Public - Auto-financing - Loans from abroad - Long-term credit - Private financing 	<ul style="list-style-type: none"> Grant Bond issue
Products in process of manufacture	<ul style="list-style-type: none"> - Auto-financing - Loans from abroad - Short-term credit - to banks 	
Stocks of raw materials (within technical norm)	<ul style="list-style-type: none"> - Auto-financing - Loans from abroad - Short-term credit 	<u>Credits to companies</u>
Stocks of finished products (within technical norm)	<ul style="list-style-type: none"> - Auto-financing - Short-term credit 	<u>Credits to companies</u>

Stocks of spare parts (within technical norm)	- Auto-financing - Loans from abroad - Medium-term or short-term loans	
Stocks in excess of the technical norms	- Auto-financing - Loans from abroad - Short-term credit	Current account credit
Marketing operations	- Short-term credit - Loans from abroad for imports	Discount credit
Operating costs	- Short-term credits	Open current account credit

4. Advantages and drawbacks of the various sources of financing

The investment of public funds fulfills a triple function: stabilization of the economy, ensuring optimum use of selective resources, and encouraging efficiency through deterioration of the rate of execution.

However, the rationalization of budgetary choices depends to a large extent on budget income, it is consequently limited and cannot meet all investment requirements.

Bank credit makes it possible to supplement the capital of the enterprise itself and, in some cases, to use it to considerably better advantage. This form of financing has the drawback, however, that it places the enterprise at the mercy of the bank, which could create financial difficulties for it at any moment. The most delicate point is therefore the problem of reimbursement of the credit on the due date and the sanction which will be imposed if need arises.

Auto-financing enables the enterprise to develop under more favourable conditions, and without being dependent on any outside source of funds. This procedure depends on the profits earned by the enterprise and not transferred to

the State budget, whereas in the public industrial enterprises profit margins are very small and have to go towards the reimbursement of the original outlay from the State budget.

Assistance in the form of capital and technical aid creates a new source of wealth since these contributions help to broaden the country's industrial base and increase production. However, they place a heavy burden on the recipient country in the form of interest, reimbursement charges, salaries and other costs. During a period of depression, they have a destabilizing effect in that they make the recipient country too dependent on imports from the supplier country of plant, equipment, spare parts and technicians.

Finally the effectiveness of foreign capital depends, according to some experts, on the limits to the absorption of investment capital by the recipient country.

PART TWO

THE FINANCIAL PLANNING AND ACTIVITIES OF INDUSTRIAL ENTERPRISES IN THE PUBLIC SECTOR

In the second part of our study, after a very short review of the present structure of the public industrial enterprise in Syria, we shall consider in turn:

- Planning for the financial needs of the enterprise;
- The profitability of investment on the commercial level and from the point of view of the national economy;
- Policies regarding costs, prices and profits;
- The operational efficiency of the enterprise and the means used to encourage efficiency.

1. The structure of the public industrial sector

The Syrian public industrial sector was given a new structure under Decree-Law No. 21 of 1 March 1967, which came into effect on 1 January 1968.

Centralized direction of the public industrial sector is ensured through a systematic structure with the Ministry of Industry at the top, then the industrial federation and finally the enterprise.

The individual enterprise retains its legal status as a corporate body and its financial autonomy. Its management is entrusted to a board of directors. The industrial federation, on the other hand, is governed by a council of administration. The main tasks of the federation are the planning of production and the implementation of the plans, the organization of supplies of raw materials and capital goods, the co-ordination of marketing and export operations and, lastly, the choice of methods of financing the enterprises and supervision of their liquidity.

The tasks of the enterprise, on the other hand, are to increase production and keep it in line with technical improvements and economic changes, to reduce the costs of production and operation and to increase productivity and efficiency.

The activities of the industrial enterprise are supervised by various agencies. Administrative supervision is exercised by the Ministry of Industry,

and then by the industrial federation. In the financial sphere, supervision is the responsibility of the Ministry of Finance and the Central Agency for Financial Control, apart from the supervisory role of the Federation.

Production is supervised by the State Authority for Planning and the Central Statistical Office, both of which are responsible to the Council of Ministers.

It may be observed that there is no supervision by banks and foreign capital suppliers.

We do not claim that these attempts to reorganize the sector and improve its structure have already produced positive results. The problem of the management of enterprises is still a matter of concern to the competent authorities.

2. Planning for the financial needs of enterprises

The process of planning with regard to financial requirements for the establishment of new enterprises is still in its beginning stages in Syria. We have no data whatever on the matter. Nor are there any regulations on this question. However, it is the Planning Authority, at the present time, which lays down the main guidelines for industrial development for the planning period. Objectives are adopted after their economic merit has been considered. A plan is prepared for each industrial project.

In co-operation with other competent organs, the Planning Authority submits the list of industrial investments to the Government. The importance of the projects approved is determined on the basis of negative criteria (the effect of the investment on national income, the time it will take for the investment to prove effective depending on its nature and the region in which it takes place, etc.) and some other indices (production cost, labour productivity, recovery period, saving in foreign currency, export possibilities, etc.)

This plan of investment also covers sources of financing. The total resources required are calculated on the basis of needs in terms of tangible assets, capital goods, wages and salaries and other items involving expenditures. In principle, the plan aims to ensure the optimum utilization of all available sources of financing together.

The profitability of industrial investments

It is often extremely difficult to determine the effectiveness of industrial investments and to calculate their profitability, whether in a commercial sense or from the point of view of the national economy. Firstly, it is sometimes difficult to estimate the effect of a particular investment. Secondly, some effects are not measurable.

In practice, calculation of the commercial profitability of industrial investments is based mainly on three criteria:

- (1) The period required for recovery of the capital invested - i.e., the period at the end of which the net profits expected will have offset the capital outlay.
- (2) The reduction of the market selling price, taking into account movements in demand and production.
- (3) The savings in foreign currency due to the cessation of imports of the same product.

There is little doubt that these criteria are not yet applied very satisfactorily, although they would be of considerable value to the enterprise. They enable it to assess the justification for a particular source of financing - the capital of the enterprise itself, instruments of financing, bank credit, etc. - and hence to draw up a plan for financing.

Similarly, the economic efficiency of the investment is calculated with the help of technical indices. The problem raised cannot be reduced to a choice between various opportunities, but concerns the quest for an optimum - that is to say, for the maximum increase in the national product. These indices are calculated by experts attached to the Planning Authority. The indices must enable the following factors to be measured:

- The rate of increase in annual national income;
- The degree of diversification of production and the structural transformation which it causes;

- The degree of acceleration of the process of national industrialization;
- The rate of increase in industrial workers and the migration from the countryside which could result;
- The sum of the cumulative effects in monetary and real terms;
- The coefficient of dependence in regard to international trade.

4. Policies regarding costs, prices, and profits

Production costs in industrial enterprises in the public sector have increased strikingly during recent years. This trend has affected the costs of both fixed factors and movable factors.

Could we conclude from this that there is no policy regarding costs?

In the view of those responsible, the steady increase in costs is attributable to the rise in prices of imported and local raw materials, the increase in wages and salaries and social insurance costs, and other reasons.

In principle, a cost policy must be based on "economic" accounting data in order to allow the production cost to be determined and analysed. Such accounting does not yet exist.

However, the management of the enterprises has given serious attention to the problem of production costs and their rapid upward movement. A conference will be held in August 1969 to consider the factors involved and find a satisfactory solution to the problem.

In connexion with cost policies, we may mention that the purchase of raw materials is carried out by the Public Import Agency (SINTEK), and that enterprises are not in a position to discuss prices. In addition, the purchase of local raw materials is regulated and the price is fixed by the Ministry of Supply. The taking on of labour and policies regarding wages are also controlled by the Government.

As to prices, the industrial enterprises in the public sector have tried to keep them stable in spite of the increase in production costs. In practice, a slight increase has been noted although there are no statistical data enabling us to analyse price trends. It should be added that enterprises are not free to fix sales prices themselves. These prices are determined by the Ministry of Supply.

Since it has no control over policies regarding either costs or prices, one might wonder how the enterprise can produce a profit? The profits of industrial enterprises in the public sector have indeed fallen off in recent years. However, as has been observed in this study, each enterprise is required to show a profit (the profitability principle). This profit is to be divided into three parts: one goes into re-investing (depreciation charges, reserves and provisions), one to the workers (25 per cent of the profits to be distributed), and one to the State (income tax and excess profits). Thus profit remains central in the activities of the public industrial enterprise and the criterion for judging its efficiency.

Planning with regard to costs, prices and profits is apparently to be initiated in 1970.

5. Operational efficiency and incentives

The level of efficiency of the management staff, engineers, technicians and workers in public industrial enterprises is low. They often lack the necessary technical qualifications and professional training.

In the last two years, however, an effort has been made in the direction of training managerial staff and skilled workers. This took the form of the sending abroad of 57 trainees for basic and advanced training (in 1967 and 1968). In addition, two vocational training centres have been established, one at Damascus and the other at Aleppo. Some 233 workers receive their training in these centres. Finally, the recently established Training Centre for Industrial Cadres has organized a series of seminars. These have been concerned with industrial accounting, industrial organization and structure, the calculation of production costs, means of marketing products and the raising of levels of skill.

To encourage operational efficiency and labour productivity, some incentives have recently been used. These consist of the granting of a production bonus to workers whose productivity reaches an optimum level and the awarding of a monetary grant to anyone who contributes towards increasing output or improving the quality of products. A campaign of emulation among different factories in the same branch was also organized in March 1969. The results of this campaign seem positive.

It is to be noted that the present system of incentives is not very effective and is limited to a few enterprises. Decree-Law No. 167 of 1963, fixing a maximum for bonuses of 25 per cent of wages or 200 Syrian pounds a month, further aggravates the shortcomings of the system. Much remains to be done in the field.

A N N E X

Sample balance-sheet of a State industrial enterprise
(in millions of Syrian pounds)

A S S E T S	31 December 1966			31 Dec. 1967
	Costs	Depreciation	Balance	Balance
<u>Fixed assets</u>				
Land	1.0	-	1.0	1.0
Buildings and construction work	3.8	0.7	3.1	3.3
Machinery and tools	13.9	6.0	7.9	9.1
Instruments	0.2	0.1	0.1	0.1
Transport equipment	0.1	0.1	-	-
Furniture	0.2	0.1	0.1	0.1
Goodwill	0.1	-	0.1	0.1
Security	0.0	-	-	-
<u>Total</u>	19.3	7.0	12.3	13.7
<u>Materials and Products</u>				
Raw materials	10.1		10.1	6.8
Spare parts	1.2		1.2	1.1
Goods in course of manufacture	2.5		2.5	3.2
Finished products	3.4		3.4	4.2
Waste	0.5		0.5	0.2
Goods for delivery	2.5		2.5	1.5
<u>Total</u>	20.2	-	20.2	17.0

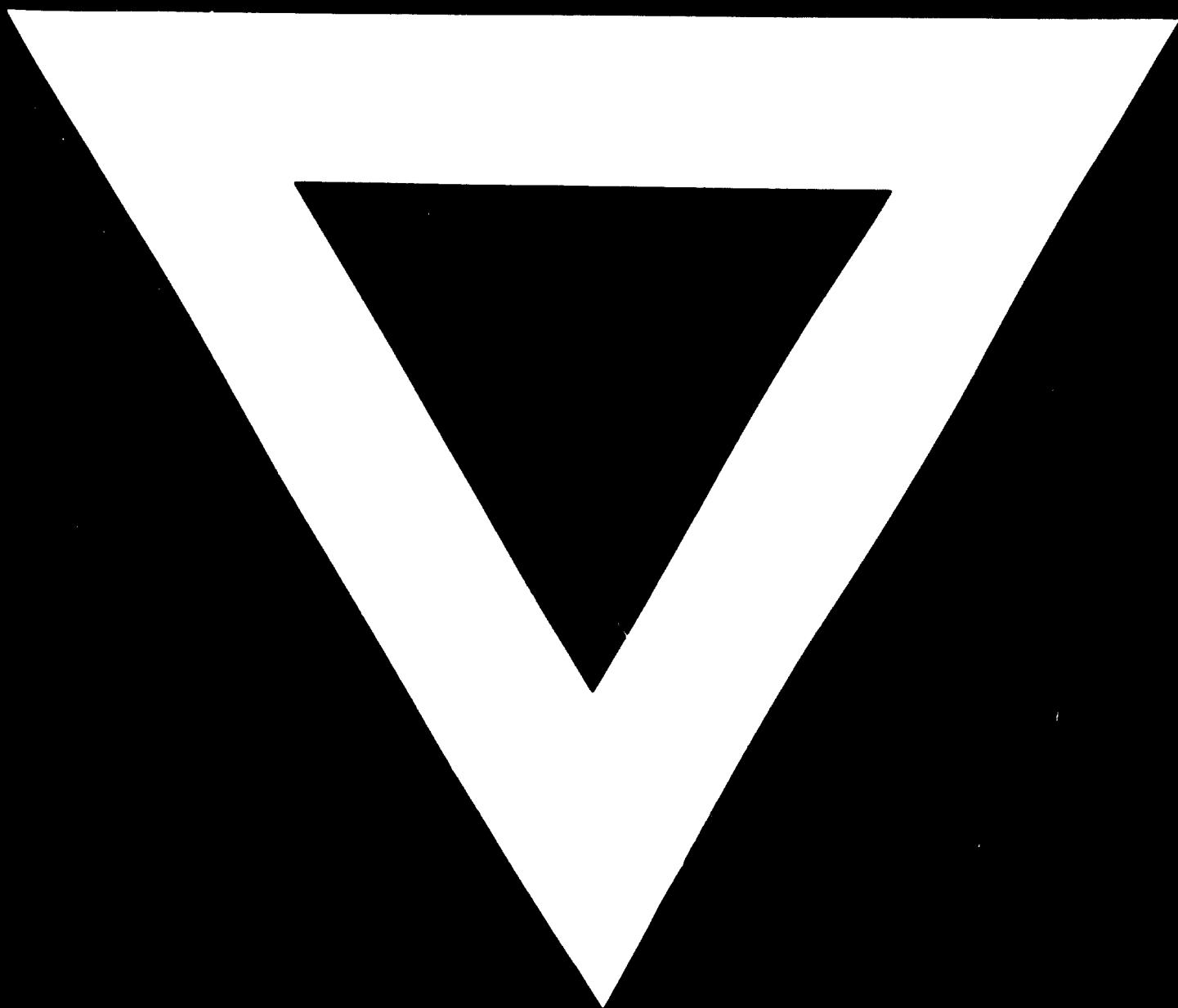
A N N E X E (continued)

<u>Debtors</u>	3 0	0.2	2 8	3.9
<u>Liquid assets</u>	0 2		0.2	0.5
<u>Short-term accounts</u>	0 1		0.1	0.2
<u>Installment debts</u>	1 2	0.9	0 3	0.5
<u>Profit and loss</u>	0 6		0 6	1.6
<u>Total assets</u>	<u>44.6</u>	<u>8.1</u>	<u>36.5</u>	<u>37.4</u>

L I A B I L I T I E S

Capital			8 0	8 0
Reserves (provisions)			1 0	0.8
Medium-term and long-term loans			10.8	9.5
Banks			5.2	7.9
Other creditors			10.8	9.8
Short-term accounts			0.7	1.4
Profit and loss			-	-
<u>Total liabilities</u>			<u>36.5</u>	<u>37.4</u>





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