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FRANCE: NOTES ON PROSPECTS FOR FINANCIAL STABILITY IN 1952-53

There is no marked historical bias for inflation in France. Since 1920 (and excluding the war years) the number of years of inflation of the middle 20's, the price level of France at the beginning of the second world war was not much above that of 1920. It should not come as a shock, therefore, that France is potentially able to move swiftly from open inflation to stability or deflation, just as it did after the first world war.

The Current Situation

After the last war, each of the combattants, except the U. S. was left with a partially destroyed economy, the loss of foreign holdings, an overhang of excess money, and unsatisfied demand for consumer goods. In order to regain their prewar standards of living, these countries undertook to make large internal investments to make good their material losses and restore their prewar productivity. In such circumstances; it was not surprising that suppressed or open inflation developed in all the combattant countries, just as it had occurred after each major war. Inflation, however, begets deflation. Five years of reconstruction and rebuilding have tended to wipe out the inflationary potential in most countries and create the possibility of deflation. The position of France (along with other countries) is now balanced between these opposing forces of inflation and deflation in this transitional period.

Before examining the probable trends, it would be useful to review the economic position in which France now finds herself as revealed by widely used statistical indicators. The existing French

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economic series, however, are not complete enough to permit an analysis to rest on an examination of the statistics alone. The existing series, however, indicate that France has now reached a position between inflation and deflation.

1. Prices - The upward price trend was slowed in 1949 but not stopped. This can be seen graphically from Chart I. However, while in past years, almost all types of prices moved together and upward, indicating a basically inflationary situation, the price changes during 1949 show individual patterns based largely on changes in import prices (viz: textiles) or harvest conditions (viz: potatoes). From Table I it can be seen that, exclusive of food items, which are affected by the weather, all other items have risen less or fallen more in the past year than in the previous year. Thus, price movements lend themselves to an interpretation of a tendency toward stabilization in the basic economic forces superimposed on a rising cost structure.

2. Industrial Production - Industrial production has not been able to regain its peak rate attained in May, 1949. Prior to that month, French industrial production had advanced steadily, with breaks caused only by strikes, summer vacations, and other external factors. The summer drop in 1949 can only partly be attributed to vacations. The failure to regain the May peak indicates that marketing problems are becoming increasingly important.

3. Money Supply - The changes in money supply show that, as of February, 1950, the rate of increase at which money was being created had slowed down somewhat, and even reversed itself in 1950. Table II,

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which shows the change in the money supply, based on Table F-2 in French Data Book, indicates that the slowing down of the rate of money creation was marked in September-November 1949 and in December, 1949-February, 1950. In addition to the slowing down of money creation, there was apparently a growth in cash balances (analysed by the French in CE(50)29/05, 6th April 1950), as indicated by bank check circulation figures. While having little predictive value, the money supply figures indicate that France went through a deflationary period in the last few months.

4. Unemployment - The rise in the number of persons seeking jobs and in the number receiving unemployment relief (see Table L-6 in French Data Book) has been frequently remarked on as a forecast of bad times. The rise in the number of unfilled employment requests, however, can partly be explained by the rise in the size of the labor force and the elimination of black markets, which released manpower. The rise in the numbers of persons receiving unemployment aid may be explained partly by the growth in the number of eligibles for unemployment relief, and the rise in the number of unemployables. Part-time unemployment does not show a strong rise. The absolute level of unemployment remains very low (less than 1% of the work force). Yet, after all the qualifications, the steady rise in the number of persons seeking work indicates that the inflationary period is over.

5. Bankruptcies - The level of bankruptcies has risen steadily and now exceeds the 1938 level. (See Table F-7 in French Data Book). The comparison is not completely apt, however, since the number of

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enterprises now is far greater than in 1938, and the present period was preceded by a rash of new business startings by inexperienced persons. It is apparent, however, that some small enterprises (which are the ones almost entirely involved) are finding it profitable to close up and for the proprietor to find work elsewhere. While at present the number of bankruptices is not too useful an economic indicator, it does indicate an end to the postwar inflation.

These five indicators, while they do not completely describe the economic situation, do reveal the ending of one period of inflation. The French economy apparently began to drag in some sectors and has certainly lost vigor in others. However, statistical series have a way of reversing themselves without notice. An examination of future trends must be made by looking at the basic factors.

FACTORS AFFECTING FUTURE FINANCIAL STABILITY

The French government now has sufficient powers to cope with almost any inflationary or deflationary movements arising from domestic causes. It could not, of course, offset a world-wide depression or an inflation caused by very heavy military expenditures accompanied by a threat of war. Furthermore, there are political and economic institutions which may inhibit the full use of the government's powers. Yet, the government's powers to relieve the symptoms of a domestic depression or to restrict a domestic inflation are no longer in doubt.

The major factors which will affect financial stability in France in the foreseeable future are discussed briefly below. Together they

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indicate that aggressive and intelligent government action will be necessary to maintain financial stability (and economic growth) and that, in the absence of powerful external forces acting adversely on the French economy, the government action can be successful.

1. Investments - Although the propensity to save and to invest now appear to be in balance, there are signs that planned savings will continue to increase while investments fail to keep pace with planned savings or even fall off. If either develops a deflation will result.

Up to now the government has financed about half of gross investment in France. With most of the Monnet Plan programs nearing completion, government investment is tending to decrease. Whether private financing will fill this gap remains to be seen. The French entrepreneur is conservative in his investment policies and private investment institutions are not well developed. The uncertainty of trade liberalization program may also have depressive effect on investment until the program is completed.

The government, however, very sensitive to unemployment and demands for housing, could certainly increase the tempo of building in France if deflation developed, as there is a tremendous need for new housing and schools. Other outlets of deficit financing, some of which could be made through the nationalized industries, are available. Some deficit financing will probably be necessary to offset the increased planned savings which results when a country's economic and political position is improved.

2. Capital Flight - In the early postwar years, the flight of capital may have deprived France of as much as a half-billion dollars

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of goods yearly. It accelerated the inflation. The potential for such demoralizing capital flight exists whenever war, or political or economic crises threaten. In the present state of economic and political conditions, however, the probability of a renewed capital flight is not great, though a drastic change in world conditions could rapidly induce one in France.

3. Fiscal and Monetary Administrative Efficiency - Although budget deficits and unlimited powers of money creation by the banking system, plagued French financial stability in the early postwar years, these forces no longer are an inflationary threat.

(a) Fiscal Efficiency - The traditional weakness of the French fiscal machinery is well known. During 1949, however, the tax laws were simplified and the staff of inspectors and the quality of their work were improved, so that tax revenue is expected to increase by over 300 billion francs in 1950 over 1949.

Despite these improvements in collections, the fiscal machinery is still deficient. Very important is the fact that tax yields are largely proportional to the level of income, since the tax system is heavily dependent on sales taxes; hence the tax system has a neutral instead of a counter-cyclical effect on the level of national income. In addition, the borrowing power of the French treasury is limited by statute and by psychological resistance. Hence, if deflationary tendencies develop, the fiscal system may be too sluggish to respond by creating a large enough deficit. Up to 1952/53, however, during which time substantial government investment will continue, the fiscal system will probably be biased toward deficit financing, particularly, as the amount of counterpart

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funds released to the French treasury declines.. This should help counterbalance deflationary dangers.

(b) Monetary Efficiency - French monetary controls have been greatly improved since the imposition of quantitative and other controls on credit in September, 1948. The monetary controls operated in a flexible but logical manner. Monetary controls, however, are of little value in getting a country out of deflation. For the next few years, however, monetary controls strengthened through ECA's control of counterpart, should definitely be of value in forestalling inflation.

4. Costs - In addition to the basic forces already considered, there are several elements of the financial stability picture which operate through their effects on costs.

(a) Devaluation - The effects of the recent French revaluation of its currency have thus far worked themselves out without notably disturbing the French cost structure. With a smaller percentage of its national production directly related to world trade, France is in a more protected position than the U.K.

(b) Wage Changes - A new minimum wage of under 15,000 francs for the Paris area, and lesser minima for other areas, now being considered, may raise the average wage level by 5 percent. Since the recent wage rises have not satisfied the workers, additional demands will be made for wage increases, but these will probably be kept to moderate dimensions. Some slight price rise, as a result of these, and the previous 1950 wage rises, should be expected, but an inflationary spiral should not result under present business conditions. While workers will continue to demand wage increases in the following year, the relatively weak bargaining power of the workers compared to the power of the

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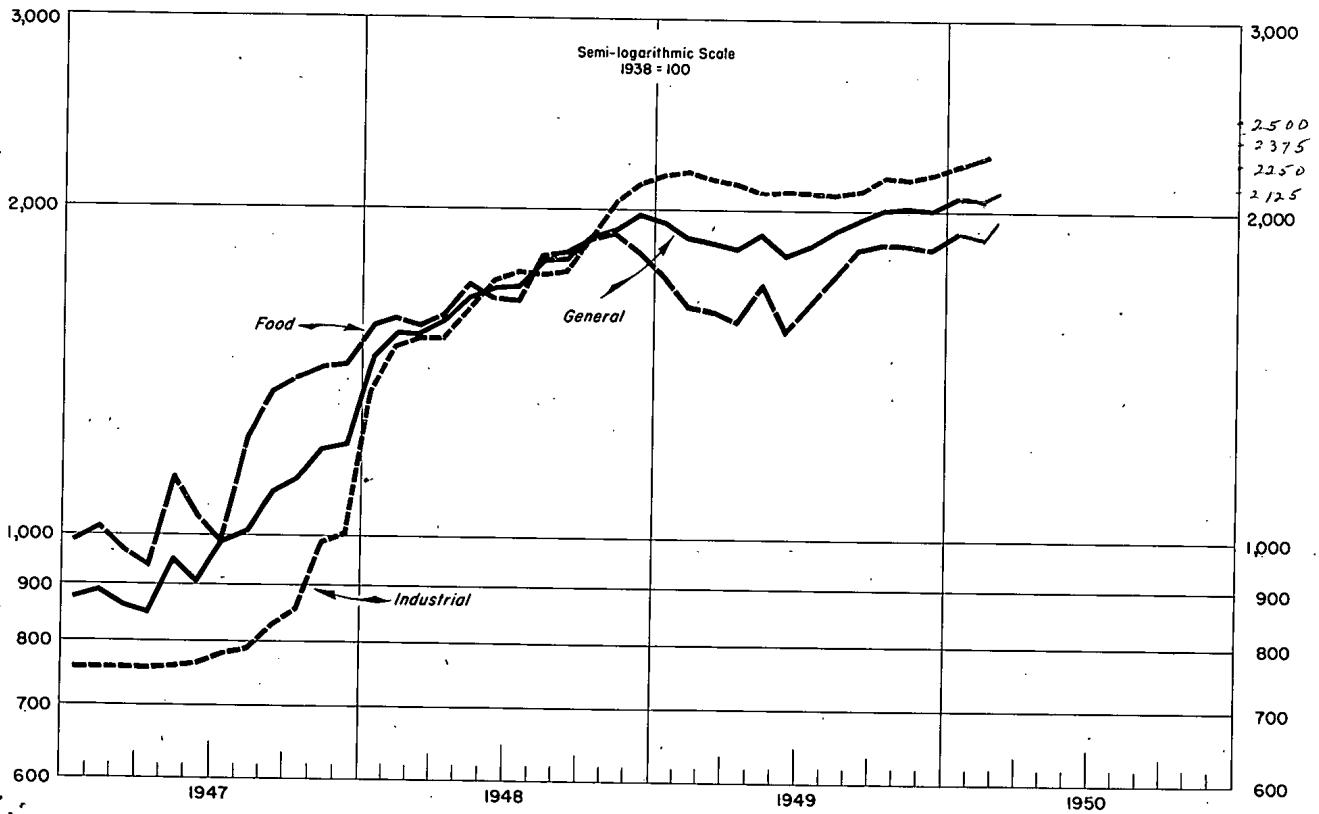
employers, and the desire of the government to maintain price stability will probably keep wages in line with advancing productivity.

5. Military Expenditures - Probable increases in military expenditures for Indo-China and more certain foreseeable increases under MDAP are not likely to be significantly large. However, French stabilization will remain provisional and capable of being upset by unforeseen increases in military expenditures.

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June 2, 1950

FRANCE WHOLESALE PRICES



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Table 1
WHOLESALE PRICES BY COMMODITY GROUP

Index 1938 = 100

	March 1948	March 1949	March 1950	Percent 1948 - 1949	Change 1949 - 1950
All Commodities	1,536	1,872	2,101	+/ 21.9	+/ 12.2
General Food	1,554	1,616	1,950	+/ 4.0	+/ 20.7
Cereals	1,014	1,271	1,338	+/ 20.0	+/ 5.3
Meat and Fats	1,925	1,925	1,695	--	- 12.0
Dairy	1,603	1,891	2,295	+/ 18.0	+/ 21.4
Other Food	1,853	1,569	2,666	- 15.3	+/ 70.0
General Raw Materials	1,533	2,127	2,315	+/ 38.7	+/ 8.8
Coal	1,585	1,989	2,035	+/ 25.5	+/ 2.3
Metals	1,780	2,069	1,975	+/ 16.2	- 4.5
Textiles	1,580	2,660	3,538	+/ 68.3	+/ 33.0
Chemicals	1,736	2,817	2,818	+/ 62.3	--
Building	1,284	1,514	1,516	+/ 17.9	--
General Semi	1,503	2,127	2,189	+/ 41.5	+/ 2.9
Metals	1,739	2,083	2,070	+/ 19.8	- 1.6
Textiles	1,667	2,950	3,301	+/ 77.0	+/ 11.9
Chemicals	938	1,157	1,198	+/ 23.3	+/ 3.5
Lumber	1,750	1,847	1,847	+/ 5.5	--

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Table II

QUARTERLY CHANGE IN TOTAL MONEY SUPPLY

(billions of francs)

1946	/	83
1947	/	80
1948	/	126
2nd	-	35
3rd	/	204
4th	/	219
1949	/	134
1st	-	17
2nd	/	128
3rd	/	239
Sept-Nov	/	23
4th	/	185
Dec.1949-Feb.1950	-	19