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Mitterrand's policy: an inflationary crunch

by Dana Sloan

What French President François Mitterrand was doing in Saudi Arabia Sept. 26-29 had less to do with furthering his own political objectives for the Middle East region than with convincing the Saudi regime not to pull the rug out from under the French economy.

Having lost the political credibility that his predecessors built over the years with Saudi Arabia and countries like West Germany, Mitterrand is reduced to the role of beggarman. Whether the French economy has even the smallest chance of surviving the fourth quarter of 1981 depends largely on Saudi good will.

Early in September when the warning signals began flashing, French Treasury director Jean-Yves Haberer went to Saudi Arabia to ask for a $2 to $3 billion loan to help finance France's trade deficit with Saudi Arabia, which is currently at about double that amount. Haberer was told that the most he should expect would be in the order of $750 million—a small sum considering the value of French-Saudi trade. Within the first three months after Mitterrand's election, Arab investors began a pullout from the French economy, to the minimum tune of 1 billion francs. When the French government recently floated a $1.4 billion bond issue at extremely attractive interest rates of 17 percent, only 10 percent of it was bought up with Arab capital, compared to past rates of 20 percent or more.

Since the West German central bank, the Bundesbank, has been less than eager to spend its own reserves in an attempt to keep the franc within acceptable parity-reach of the deutschemark in the European Monetary System snake, the Banque de France has had to dip into its own reserves to an astounding degree. Since the end of July more than 46 billion francs, or slightly more than $8 billion, has been spent in this effort to avoid an official devaluation. During the course of a single day, Sept. 18, the Banque de France had to spend between 5 and 10 billion francs to support the national currency, in what amounts to one of the single largest interventions anywhere in recent history.

Despite these and other emergency measures to support the franc, characterzed by one leading French banker in New York as "artificial interventions" intended to postpone a devaluation of the franc in the EMS, that devaluation will not be long in coming anyway.

During the weekend that followed that massive intervention, Economics and Finance Minister Jacques Delors announced two additional measures intended to prevent capital flight from the country. Taking his cues from Paul Volcker at the Federal Reserve, Delors jacked up the rate at which the central bank lends short term from 17.5 to 20 percent. The French twist however is that—unlike in the United States—the government of France has demanded that the banks which then lend out this money stick to a basic 14.5 percent prime rate. Only a few weeks before, Delors had forced the banks to lower their prime rate by warning that heads would roll in the large—and soon to be larger—nationalized banking sector.

In addition, Delors slapped down a series of strict, Italian-style exchange-control measures, which prohibit importers of foreign goods from buying foreign currencies at the time they contract to buy the goods; the currency has been used later for payment on their purchases. Delors' measures mean importers will now be unable to protect themselves from unfavorable currency fluctuations. Importers will have to purchase foreign currencies at the time they settle their transactions, potentially at exchange rates vastly different from those that prevailed at the time the purchase was made.

The exchange controls were immediately challenged by the European Community and might, like similar Italian measures taken last May, have to be reversed within a few months. But the effect of the overall package was short-lived in any case. Although the franc temporarily rose to 5.3 to the dollar, in contrast to the near-record 6.1 rate of a month ago, it was still well below the 4.5 mark that prevailed before Mitterrand's election in May. By the end of this week, the Banque de France was again forced to intervene massively to keep the franc from falling below acceptable levels vis-à-vis the deutchemark. Within a few days, the French interest rate is expected to be jacked up another notch, and an official devaluation may follow soon after, despite all the emergency measures.

Marriage of Keynes and monetarism

There is more involved here than just a general reaction in the capitalist world to the presence of four Communist ministers in the French government. They, after all, do not make Mitterrand's policies. The French government itself reduced the value of the franc to an increasingly worthless piece of paper by its decision to use billions of francs, not to create new wealth, but to manage and spread the poverty. As Jacques Delors,

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reputed to be the "moderate" in the cabinet, has put it, the government wants to take the "best" aspects of Keynesianism and of monetarism and roll them up into one. This borrowing from two equally bankrupt forms of economic policy is a sure prescription for disaster.

This year's budget deficit will already be near $17 billion. By next year, that figure will skyrocket as a result of the nationalization program and hiring policies that will add 50,000 functionaries to the state payrolls. The nationalization program alone will cost the state a minimum of 35 billion francs (or about $6.5 billion) in compensation to stockholders. In addition to the large, relatively healthy conglomerates such as Pechiney Ugine Kuhlmann, Saint Gobain, Compagnie Générale d'Electricité, the 36 banks and two arms manufacturers that will become state-owned at the beginning of next year, the government is also taking over two large steel companies fighting for their very survival.

Bankruptcies are now occurring at a rate of 2,000 a month, almost 30 percent higher than at this time last year. Unemployment, poised to break the 2 million mark by the end of the year, has accelerated at a pace of 27 percent annually. The inflation rate for the month of August was 1.2 percent, a record rate for that month which guarantees that the annual inflation rate will be at 15 percent by year's end.

The social security system is expected to register a 7 billion-franc deficit by the end of the year, a figure which is expected to increase to 23 billion by 1982. The unemployment insurance fund, Unedic, is also 7 billion francs short this year, with predictions of a 15 billion shortage by next year. For the first time in its history, Unedic was forced to borrow the majority of funds needed to compensate unemployed workers at the end of August.

Spreading poverty

The French government has made much ado about its intentions to stimulate consumption through an increase in buying power. After increasing the minimum wage rate, however, the government announced a series of tax increases which will offset any positive impact on consumption the minimum wage increase might have had. Two new taxes have been announced: The first, a tax on "fortunes" in excess of 3 million francs ($550,000), with provisions for a 2 million-franc abatement on what is termed "professional equipment." The small businessmen who can't afford to pay the tax will just have to sell their businesses to those who can. The second tax is being called the "solidarity tax" and will affect about 2 million middle-income households. Its proceeds are to be channeled into Unedic in an effort to make up for half of next year's projected deficit. Ironically, the tax will hit the whole section of middle-income working people who normally vote conservative and who had swung in large numbers to Mitterrand in the last elections hoping to improve their economic positions. A couple with two children, earning a combined income of 12,000 francs a month ($2,200), would be typical of the taxpayers hit hard by the new tax.

This "solidarity tax" is only one example of the vicious form of Malthusian economic thinking that has taken over since the change in government. In a government that now contains a specially created "Minister of National Solidarity," this concept of sharing the wealth, i.e., distributing the poverty, has become pervasive. A day does not go by when some minister, in talking about either the domestic economic policy or policy toward the developing-sector countries, does not use the term "solidarity." "Social justice" is another preferred phrase heard in the hallways of ministries these days in Paris. All it signifies is that France's national energies will be channeled into parceling out already-existing wealth, instead of creating new wealth for further progress and development.

Return of Pétain

This zero-growth mentality was illustrated with a vengeance when Prime Minister Pierre Mauroy laid out his plan to fight unemployment—not through the creation of new productive jobs, but through the sharing of already-existing jobs. So shocking was the Mauroy program, so reminiscent of the solidarism that prevailed during the days of Marshal Pétain's wartime Vichy regime—in which Mitterrand served—that a well-known Gaullist party member, Robert Vivien, greeted the announcement of the program with cries of "we're back with the Marshal."

Mauroy's program contains the following points:

- financial incentives for business to reduce the workweek to 39 hours;
- lowering of the retirement age to as early as 56 years of age;
- institution of "part-time retirement" in which individuals nearing retirement age would first work only 30 hours a week, and then only 20; a younger worker would come in to work for the duration of the freed-up hours;
- a "civil service" job program for youth in which young people leaving school would go to work for one year to "fight pollution," or to maintain forests and national parks in exchange for room, board and a $200 a month allowance;
- "solidarity contracts" in the newly nationalized sector, which employs several hundreds of thousands of people; these contracts will reduce working hours to the level of part-time work, with corresponding pay cuts.

When solidarism comes to France in full force, the French economy can't be a long way from the Polish "model."