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Article — Digitized Version

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Intereconomics

Suggested Citation: Hamburg Institute of International Economics (HWWA) (Ed.) (1969) : French Franc devaluation: A first step towards realignment?, Intereconomics, ISSN 0020-5346, Verlag Weltarchiv, Hamburg, Vol. 04, Iss. 9, pp. 268-269, <https://doi.org/10.1007/BF02926265>

This Version is available at:

<https://hdl.handle.net/10419/138249>

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French Franc Devaluation

A First Step towards Realignment?

Since 1968, two main points of discussion have attracted the spotlights of the international drama of the currencies: should the French Franc be devalued, and the German Mark be revalued? The first of these two points on the agenda has been wiped out overnight, when the successors of General de Gaulle lowered the Franc's exchange rate. Those who are familiar with the matter had long known of the necessity of such a step.

Necessary Devaluation

Last year's industrial strike in France, and especially in Paris, had compelled the government to make vast concessions to the strikers in the form of increased social security benefits and higher wages, which consequently drove the prices up. Advancing inflation brought with it a large adverse balance of French payments, which undermined confidence in the French currency, producing a first wave of devaluation rumours. A policy of vigorous economic expansion, some kind of "Great Leap Forward" to evade the financial aftermath of the riots, only added to the burden piled up on the shoulders of an already weakened currency. Neither the outside world nor Frenchmen themselves could believe any longer that a devaluation of the Franc could be avoided, in spite of the currency reserves hoarded under de Gaulle. The great flight of French capital from the country began. The longed-for haven which all flight capital was seeking was the DM, which

everybody suspected was on the threshold of revaluation. Veritable torrents of "hot money" from France, but also from the UK and the US, began to pour into Germany and set up an international currency crisis.

This was the reason why the Federal Government was kept under strong pressure in favour of a DM revaluation at the international currency conference convened to Bonn in November, 1968. The Federal Government stoutly refused to make the desired adjustment but, as a substitute, offered to levy an export tax on German goods and cut the turnover tax on Germany's imports, measures which were eventually adopted. This behaviour had consequences for the Franc.

Before the Bonn conference started, and during it, appearances and general expectations seemed to predict a simultaneous devaluation of the Franc and revaluation of the DM. However, General de Gaulle followed the Federal Republic's example and proclaimed the existing exchange rates as sacred and immutable.

Victory of Rationality

It is true that international credits secured a brief respite to France, but monetary equilibrium had been irretrievably lost. In May, 1969, a new breakdown in international currency relations occurred but again was not made the occasion for a general realignment of distorted exchange relations. It is true that

General de Gaulle had left the political stage, but this time Bonn found that currency relations had become a burning issue in internal German politics and the government could therefore not hammer out a rational solution of the problem.

This left only one way open to the new masters in Paris for protecting the Franc against irresistible pressure—to make their own isolated attempt to follow the dictates of economic rationality.

A Model of Tactical Wisdom

The way in which this was done compels admiration. Without giving speculators the slightest chance to cash in, the French government devalued the Franc at a moment when almost nobody expected it.

German quarters, it is true, bewailed the fact that the French had neglected to preface their momentous decision with the promised bilateral consultations the Franco-German Friendship Treaty provides for, so that the Franco-German friendship was only apparently a paper pledge. But have the critics who voice such complaints asked themselves what further consultations would have meant in terms of the danger of indiscretion—especially as Germany had long ago advocated such devaluation? The secrecy with which the French government prepared its devaluation measures has been a model of such excellence how such things ought to be done that every government

which might in future be forced to devalue could not do much better than to emulate the French procedure.

Difficulties of the Home Market

It is only to be hoped that all further steps the French government will take in the economic field will be imbued by similar wisdom, because the targets named to regain equilibrium for France's balance of payments, and even more so for its balance of trade, without a strong upward drift of prices, cannot possibly be reached, under present conditions, by simply devaluing the Franc and leaving it at that.

The full potential of increasing French exports through cutting the nominal equivalents of its prices will, at the first place, not be realised since French exporters and foreign importers will not pass on the full price cut to their clients. Secondly, any increase in French delivery volumes, even the minimum needed merely to stabilise the value of French exports after devaluation, will be hampered by the high degree of utilisation of French production capacities that has been prevailing during recent months. And thirdly, elasticity of demand, especially for durable consumer goods, is very limited and thus will enable exports to grow only sparingly, more so since other non-price-factors often have a more decisive influence than the price.

Whether the intended cut in imports can be achieved, depends also largely on whether demand is sufficiently elastic and whether prices will remain stable. However, in addition to the direct impact of inflation on French foreign trade, it is high home market demand which must be curbed before an export drive can have any chance of success. It will only then be possible to speak of a fair success of the devaluation measures if and when the government succeeds in stopping the permanent upward drift of both

wages and prices, except the prices for imported goods. The French government must at any rate avoid jumping the traces, for example, when the foreshadowed reform of its social security programme takes place, because this would create new incentives for rising imports and for boom conditions in the home market.

Farming a Separate Problem

The markets for farm produce form, as usual, a special set of problems. Prices of farm products, as is well known, have been hitched to the US \$ as a unit of accounting in the European Common Market. This is why the Franc devaluation has created confusion in the price structure.

French farmers, of course, would not object to their receiving higher prices but this would drive up the cost of living in France, which the French government intends to avoid. How this problem has been settled by the Council of Ministers of the European Community is a textbook example for the way in which a single block of interested parties, in this case the farmers, are being granted favours at the expense of the consumers and naturally also the entire European Community. For the Common Market for farm products is now to be suspended for at least two years. During this period, the products of the French farms, insofar as their marketing was regulated by Community agreement, will be untied from the former common unit of accounting, which will remain in force for the remaining five EEC member countries as a joint basis of pricing. France will thereby be compelled to react to this complicated system with a no less involved system of export taxes and import subsidies of its own.

The adjustment of the French Franc's international value has again made it blindingly clear that the European Common Market for farm products is

progressively advancing on a slippery protectionist road, which eventually will make pro-rationing of production or the fixing of harvest quotas unavoidable. With advancing time, chances that might once have existed for revising this protectionist policy are gradually growing slimmer and slimmer.

Overall Solution

But this is not so in the field of currency relations. The subject of international realignment of currency values, which had been debased, for a while, to become an exclusive subject of academic discussions at High Table, seems to have genuine chances again. The Federal Republic, for example, is by no means yet free of all its worries after devaluation by the French. Though France is Germany's most important trade partner, Germany is in surplus on trading account with France to the tune of DM 6,700 mn of which, however, only 17 p.c. are derived from straight exchanges of goods with Franc. This share is not decisively increased by adding the account Germany has with the entire Franc Zone. In order to redress the balance of payments and trade, Germany will eventually have to revalue, whether the Federal Government likes it or not, and this would be welcome support for the efforts of the French to stabilise their economy. The present official view in Germany that the rate of exchange of the DM is stabilised like the proverbial "rocher de bronze" for ever and a day, is simply untenable. If Germany lifted the exchange value of its currency, this might prompt other countries to adjust the rates at which their currencies are bought and sold, so that the "Great Currency Reform", a universal international revision and correction of mutual currency value relations, which seems indispensable, might yet be carried through. France has set the wheel in motion. ogm./ke.