

Inflation, debt and stabilisation in the 1920s France : underpinning the Poincaré's Miracle

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Coping with a french myth

The french myth of
Raymond Poincaré (1860-1934)
as the « savior of the franc » in
1926-1928

- return of confidence (and capital)
- sound public finances
- stabilization on 25th June 1928 of the value of the money to the 1/5th of its pre-1914 gold parity (125 FF/1£)



1. Reassessing the Poincaré's Miracle

The end of the great inflation of wartime and after ?



« The Masterpiece of the Cartel : the daily life more and more expensive »

Borrowing to finance the war...

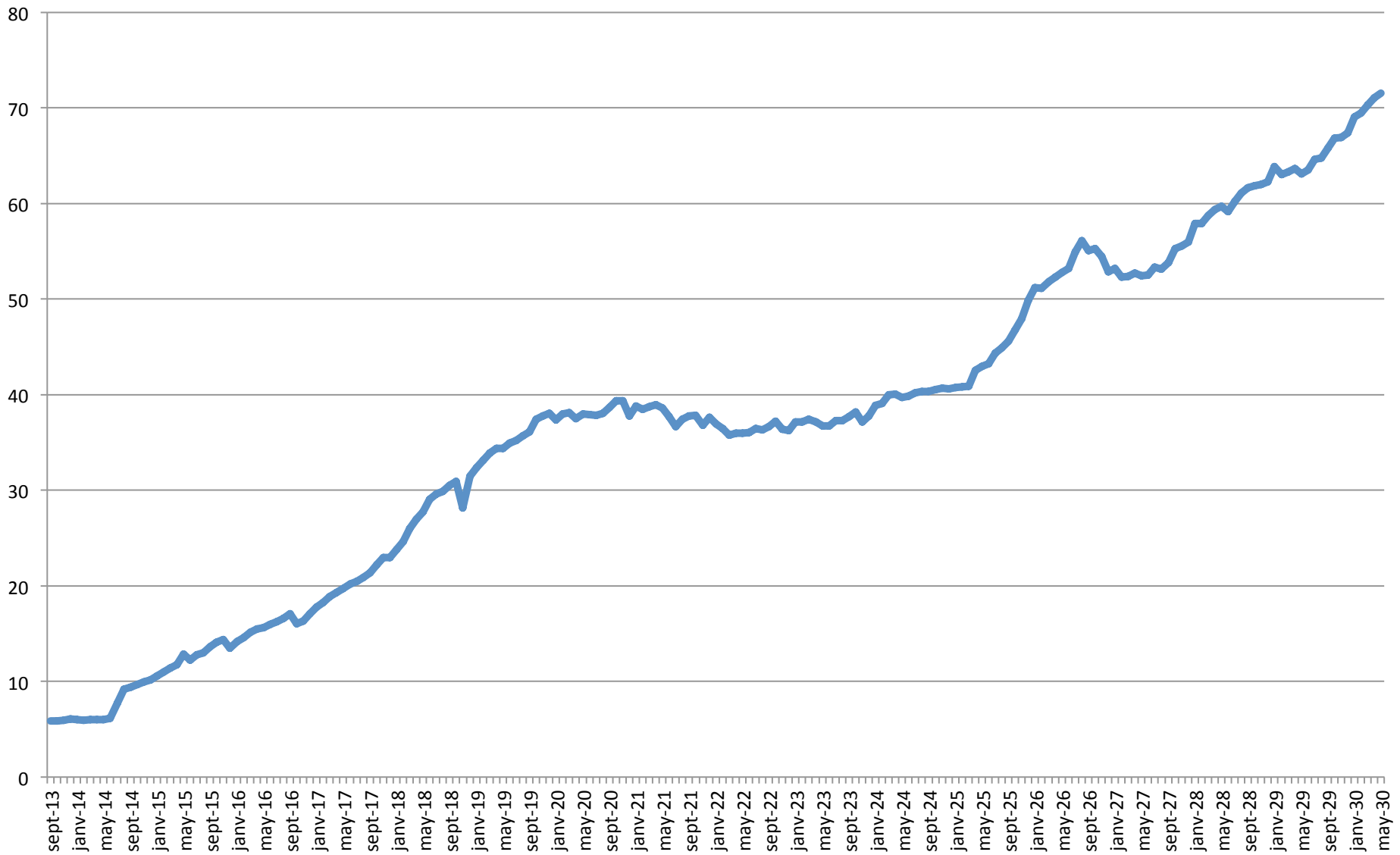


and to finance the
peace...

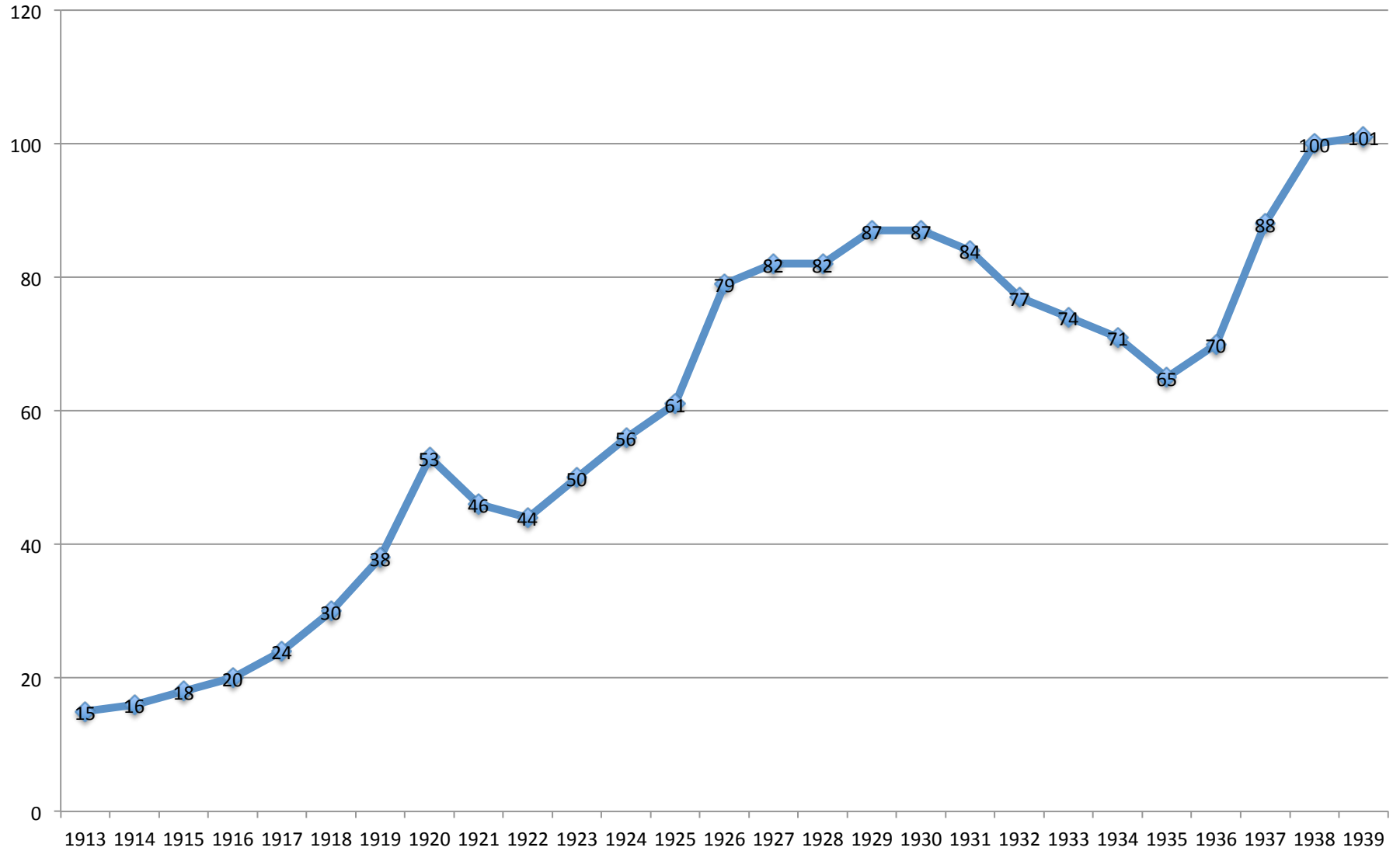
(poster for the
reconstruction loan
1920)



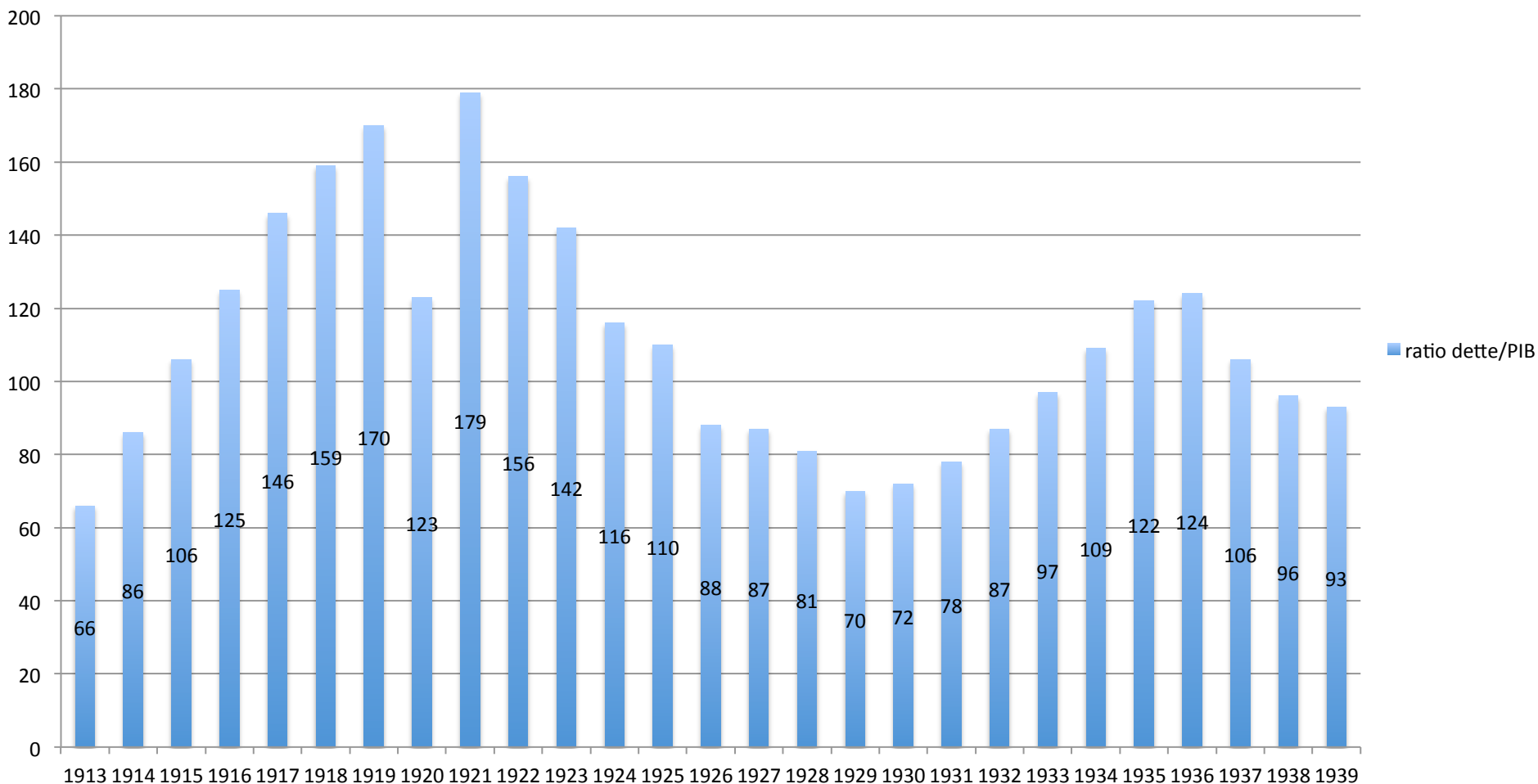
Amount of Bank of France notes in circulation



Price Level (1938=100)



French Debt-GDP ratio (1913-1939)



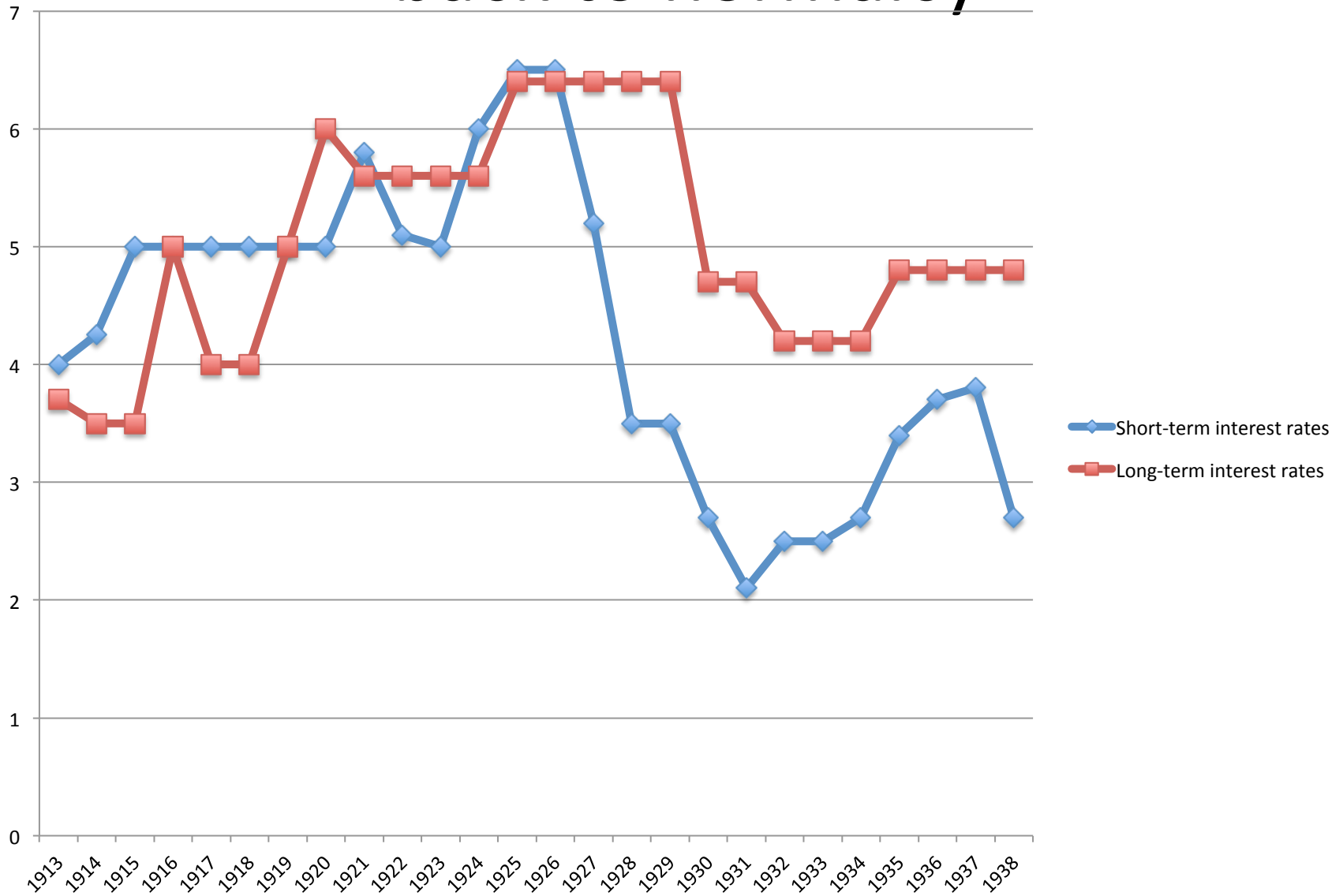
Franc/US Dollar rate, 1919-1927 (1 dollar = x franc)

(Special thanks to K. Yago for providing us the chart from his pHd)



出所: *Annuaire statistique de la France, 1919-1929.*
より作成.

Nominal Interest rates : back to normalcy



The limits of austerity

Examining the classical (and neo-classical) view of Poincaré's stabilization: the credibility and the austerity as credibility vector (Bordo and Hautcoeur, 2003)

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- **policy of austerity?**
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- Budgetary compression ?
- If we consider the ratio public expenses-GDP, we state indeed a drop from 17,6% in 1925 to 15,2 %in 1926, but it established already at 16,3% in 1927...and 15,9% in 1928...
- The measures of austerity were broadly symbolic...(closing of 104 “sous-préfectures”, see Nicolas Verdier, 2010)
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- **Fiscal policy ?**
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- the increase of taxation is counterbalanced by measures of alleviating :
- Doubles the tax on income from securities, but reduction of the general level of tax-income from 60 to 30% of the maximum rate...
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- Finally : the ratio tax-DGP does not increase significantly : it rose from 12,6% in 1925 to 14,6% in 1926, 15,6% in 1927 and stabilizes at 16% in 1928.

2. Underpinning the Miracle : the key-role of new market institutions

- The redesign of Bank of France (1926-1928)
- The new deal of the Caisse des dépôts et consignations
- « Created in 1816 to restore confidence following the financial crisis after the Napoleonic Wars »

Redesigning the Bank of France : toward a central bank (1926-1928) :



- New management : independance from the Treasury and end of competition with commercial banks
- New tools : « regularization » of the foreign exchange market (outside) and conversion to open market policy (inside)
- New missions : ensuring monetary and financial stability

Managing the Exchange market

- From December 1926, Bank of France buys (according to the law of 7 august 1926) all the pounds, without ceiling, at 124,02 Francs et sells them at 124,10 Francs. However, foreign exchange flowing into France because they speculate on a soon strong revaluation of the franc. The BoF issue thus a ever larger amount of money. It is estimated that the money supply increased by 25 billions !
- The abundant liquidity is further enhanced by the slowdown of business, due to the increasing exchange rate of the franc which inhibits exports.
- the money market is soon congested by unemployed liquidities, contributing to the decline of interest rate.

The new role of the central bank on domestic money market expressed by Pierre Quesnay, head of the Research Departement of the Bank of France

- « Contrary to what is happening in all countries where the Bank of Issue ensures the functioning of the money market, the Bank of France has practically no immediate influence on the various segments of the market... »
- « To have control over money in circulation, to be able at all time to reduce its commitments sufficiently to lower the volume of lending, to regulate the capital market, to counteract a general inflationary tendency on the stock market or in prices, these are the bank of issue's main task today, beyond the job of protecting the currency » (Memos of Pierre Quesnay, head Dpt Research of the BoF, 1926-1928, Bank of France Archives)

Fostering the money markets :
the hidden face of the Poincaré's Miracle
the new deal of the Caisse des dépôts et consignations



Jean Tannery :
CEO Caisse des dépôts et
consignations from 1925 to 1935

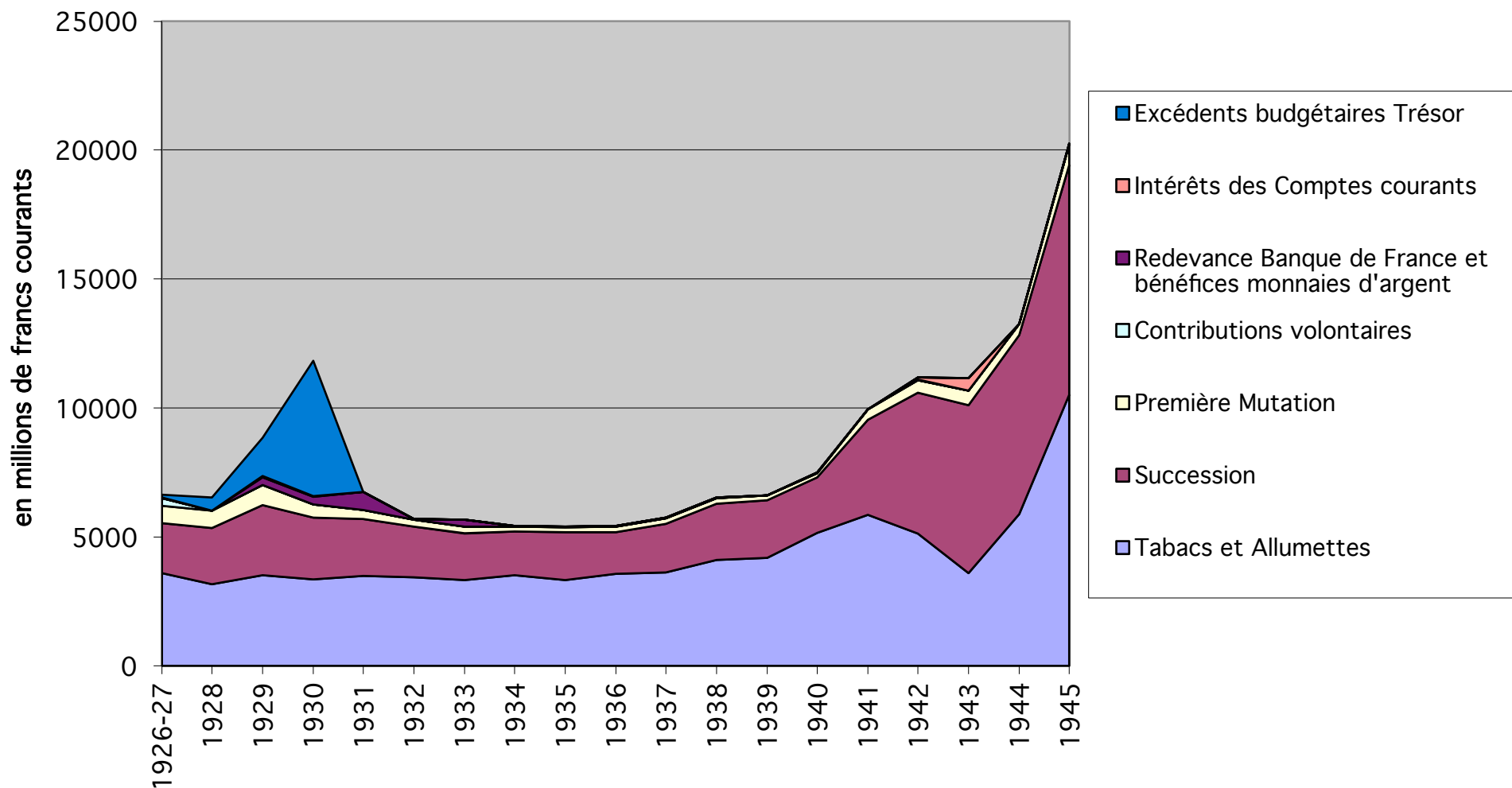


The decisive lever :

The Caisse autonome (CA)

- **The launching of the Caisse autonome d'amortissement (Autonomous Sinking Fund)**
- The entire name was in 1926, in application of the law of the 7th August 1926 : *Caisse autonome de gestion des bons de la défense nationale, d'exploitation industrielle des tabacs et d'amortissement de la dette publique.*
- The creation of the Fund was actually the centrepiece of the recovery plan of Poincaré.
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- **The first Golden Rule**
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- The autonomy of the Fund is guaranteed in the constitutional law voted by the Congress (held in Versailles), on 10th August 1926. This legal disposition remains in force until the end of the Third Republic in 1945.

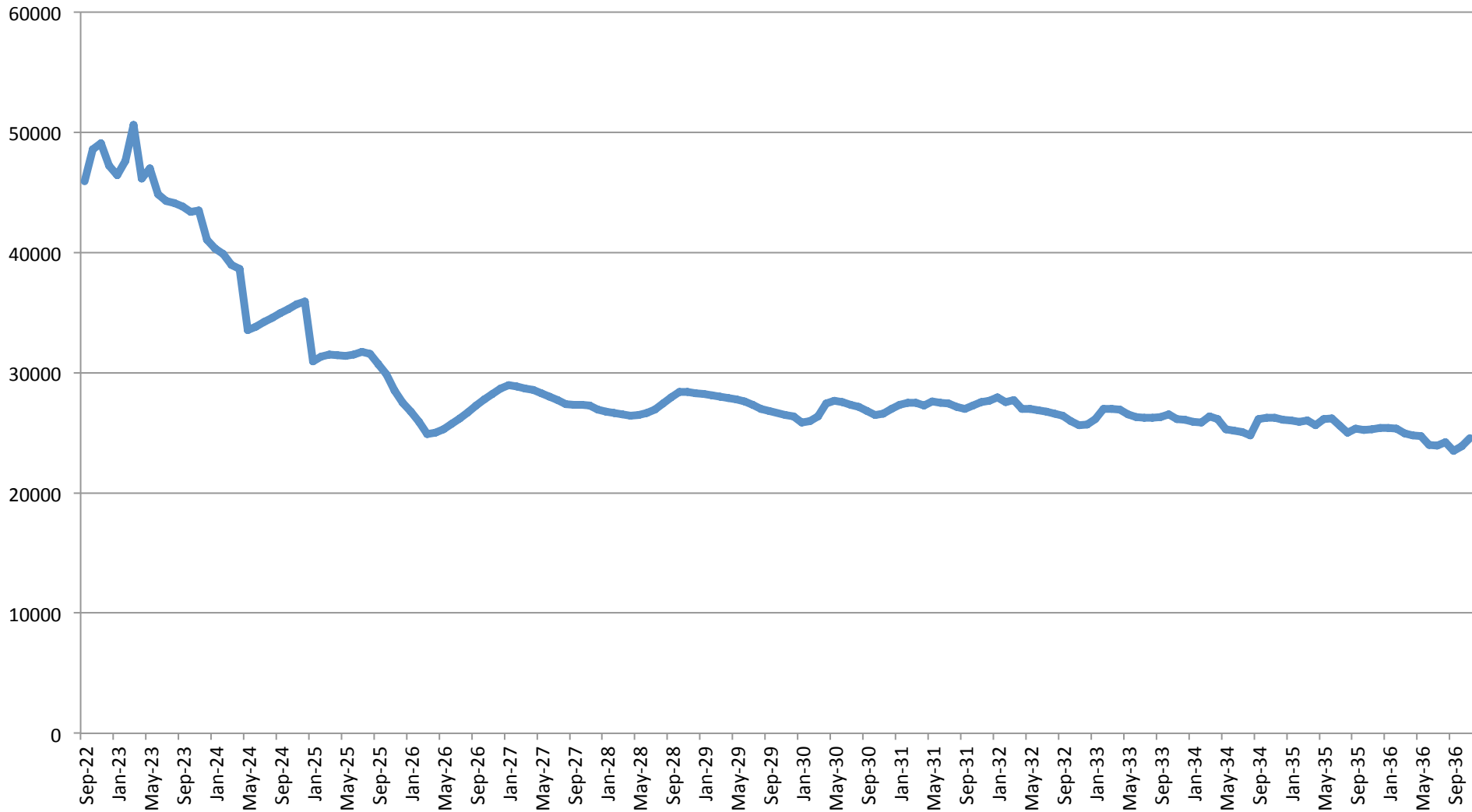
The Resources of the Caisse autonome (1926-1945)



The policy of the Caisse autonome : amortization or consolidation ?

- The deleveraging by the Caisse
-
- From 1st January 1927: issue of two-year bonds, bearing interest at 6%, while the very short term bonds bear saw lower interest rate, from 5,5 to 3%.
- End 1927, the very short term debt is reduced to an amount of 18MM and the total amount of the 2-years bonds reached 25 billions.
- On 3th June 1928, the floating debt mounts 38 billions.
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- 1month bills : cancelled on 16 december 1926
- 3 month bills : cancelled on 15 janvier 1927
- 6 month bills : on 30 janvier 1927
- 1year bills : on 3 juin 1927
- First january 1927 : first issue of 2 years bills
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- But the politics of the CA faces the reality of the French money market – or rather the absence of a real money market in France, comparable to the London money market. The French economy is flooded with cash
- This situation is due to the policy of the de facto monetary stabilisation of the exchange rate of the franc. This explains the stabilization of the Bons de la Défense nationale in circulation from 1930 to a bearing of about 25 billions of FF.
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- On 25th JUNE 1928, the franc is de jure stabilized. At 125,21 for one pound. Nogaro proved it was the right level regarding the debt-income ratio. The stabilization increases the savings deposits : 4 billions in excess in 1927 and 1928.
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- A second stage begins for the CA
- 23th October 1928, Milan proposed to extend legally the operations of the CA to the whole assets of the domestic public debt : the consol- state securities (la “rente”), the Crédit National Bonds...
- This is adopted by the law of the 30th December 1928.
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- The action of the body gives depth to the transactions on the money market. It constitutes doubtless a regulatory factor

The stabilisation of the money market the amount of the bills of nationale defense (1926-1940) in millions of Francs



3 concluding remarks

- « Confidence » is doubtless the key-variable, but confidence is ever based on institutions.
- The Poincaré Miracle originated a “financial system” – CDC, BOF, Crédit national, Saving banks...commercial banks which existed until the french big bang of the 1980s and 1990s.
- The level of the sovereign debt (and of inflation) is related to the degree of national cohesion and most determinant is the share of foreign holders of the public debt. More generally, the sustainability of a sovereign debt is always related to a certain international regime. There is no doubt that the settlements of the german reparations by the Dawes Plan (1924-1928) and the Young Plan (1929-1930) had been a important factor of the “Poincaré’s Miracle”. The issue of the management of the sovereign debt could thus not be solved in just one country. It is always an international issue. It is not the less pessimistic lesson from this past history.