

Crisis, growth, stability: Evolution of the financial responsibilities of the Banque de France in the twentieth century

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Perhaps more than other central banks, the Banque de France has been the object of public debate since its founding, at the start of the nineteenth century. Since the start of the twentieth, the discussion has centred recurrently on the Bank's responsibilities, in the broadest sense, within the financial system. Bound up with the more general question of the banks' role in sustaining – or hampering – economic growth,¹ the main criticism leveled at the central bank is its supposed inability to adapt, if not too late and at the least appropriate moment, to the ever-changing needs of the economy and society.²

As a consequence, most specific histories of the Banque de France in the twentieth century have been marked by analysis of its delays, its rigidity, its archaic nature.³ Nor is there any point here in

¹ Alain Plessis, "Les banques, le crédit et l'économie" in Lévy-Leboyer, Maurice and Jean-Claude Casanova, eds., *Entre l'Etat e le marché, l'économie française des années 1880 à nos jours*, (Paris, Gallimard, 1991), pp. 331-334.

² Achille Cauphin-Meunier, *La Banque de France*, Paris, Gallimard, 1936; Alfred Pose, *La monnaie et ses institutions, histoire, théorie et technique*, Paris, PUF, 1942; François Perrous, "Les banques d'émission e l'Etat", *Revue d'Economie Politique*, vol. LIV, 1945; François Bloch-Lainé, *Profession fonctionnaire*, (Paris, Le Seuil, 1976).

³ Jean Bouvier, *Un siècle de banque française. les contraintes de l'État et les incertitudes des marchés*, (Paris, Hachette, 1973); A. Plessis, "The Bank of France from the early twentieth Century to the 1950s", in Y. Cassis, G. D. Feldman and U. Olsson (eds.), *The Evolution of Financial Institutions and Markets in Twentieth-century Europe*, (Aldershot, Scholar Press, 1995); O. Feiertag and P. Martín-Accuña, "The Delayed Modernization of the Central Banks of France and Spain in the Twentieth Century", in C. L. Holtfrerich, J. Reis and G. Toniolo, *The Emergence of Modern Central Banking from 1918 to the Present*, (Aldershot, Ashgate, 2000).

seeking to prove the contrary; all we intend to do is vary the historical perspective. The debate on the economic responsibilities of the issuing institution, in fact, takes it for granted that the Bank, commonly identified with its top management, has specific powers in the areas of monetary, exchange-rate and credit policy such that it can act in accordance with the pace and procedures of economic activity. The traditional defence of central bankers is to point out that in the final analysis the issuing institution is more passive than active. That is, it is not basically action-oriented but "is acted upon by the pressures exerted by all those who use money," in the words of Wilfrid Baumgartner, Governor of the Banque de France in the early 1950s.⁴

So posed, the alternative between self-proclaimed impotence and purported strength leaves hardly any room for analysis and reduces the history of the Bank to little but a normative chronicle of the decisions taken by its managers, sometimes converts to the new dogma of economic intervention, sometimes apostates returning to the essentially single monetary orthodoxy. Nevertheless, one can seek to examine, from a slightly different standpoint, not so much what the Bank should or could have done as its real long-term role within the French financial system and, more generally, the real evolution of its functions within the French economy during the twentieth century. For the purposes of this paper, this means paying more attention to the multifarious and ever-changing practice of the Bank than to its apparently immutable statute. We intend to contribute to the analysis of the historical dynamics of the transformation of the French financial system (not to the study of its alleged blockages).

As we know, the upheaval of the First World War put an end, for many years, in France and in the entire world, to the monetary stability that had characterized the last third of the nineteenth century. The suspension and then the abandonment of gold convertibility, more or less in concomitance with the advent of the era of inflation, inevitably altered the functions of the Banque de France, like other

⁴ W. Baumgartner, draft preface to *Distribution et contrôle du crédit*, Paris, A. Colin, 1951, Archives Wilfrid Baumgartner, Fondation Nationale des Sciences Politiques (AWB), 2BA7, Dr. 5.

central banks. The problem of the Bank's responsibilities was posed in new terms, and in a world marked by greater instability.⁵

Three key developments contributed to this evolution in the course of the twentieth century: the exponential growth and diversification of financial assets; the unprecedented growth of financial intermediation; and the increased importance of short-term international capital movements, which radically reconfigured the workings of the international money market. In this unfamiliar context, the fundamental historical problem of the Banque de France itself had to be reformulated. The objective of maintaining the franc's convertibility gradually gave way to the broader and apparently contradictory mission of safeguarding the overall macroeconomic stability of the financial system while assuring the greatest possible micro-economic efficiency.

The thesis maintained here is that the functions of the Banque de France changed so vastly in the course of the twentieth century as to transform the very notion of stability. The goal of monetary stability, i.e. the protection of the fixed value of the monetary base, can with good reason be replaced by the more complex, overarching notion of stability of the financial system. Defence of the latter's stability can be considered as the principal and permanent economic responsibility of the bank of issue, especially vis-à-vis exogenous shocks due to rapid, violent change in the international financial environment, in an ever more closely integrated world economy.

I shall examine this thesis first with a general analysis of the evolution of the Bank's financial functions, conducted by means of a study of its accounts over the long period. Then I examine the function actually performed by the Bank within the system, sharply diminished as it was by the succession of crises in the 1920s and 1930s. Next, I shall analyze the particular development of its role in the gradual construction of a debt economy from the 1930s to the 1970s. In conclusion, I shall touch on the turnaround of the 1980s and the

⁵ Richard S. Sayers, "Dagli Istituti di emissione alle Banche Centrali, 1800-1930", Istituto Internazionale di Storia Economica Francesco Datini, Prato, 21 April 1972, p 9.

general sense of recent changes within the new framework of European monetary integration and the globalization of financial markets.⁶

The Banque de France and the French financial system in the twentieth century: an overview

The position and role of the Banque de France within the financial system changed very substantially in the course of the twentieth century, but this was in no way reflected in the Bank's statute. The statutory definition of the central bank's operations remained essentially unchanged from the start of the nineteenth century until 1973. However, we should not let this normative fixity conceal the fact of the long-term adjustment of practices. Analysis of the Bank's accounts during the twentieth century – a source remarkable for continuity and relative homogeneousness – allows us to determine the extent of their quantitative and qualitative transformation.

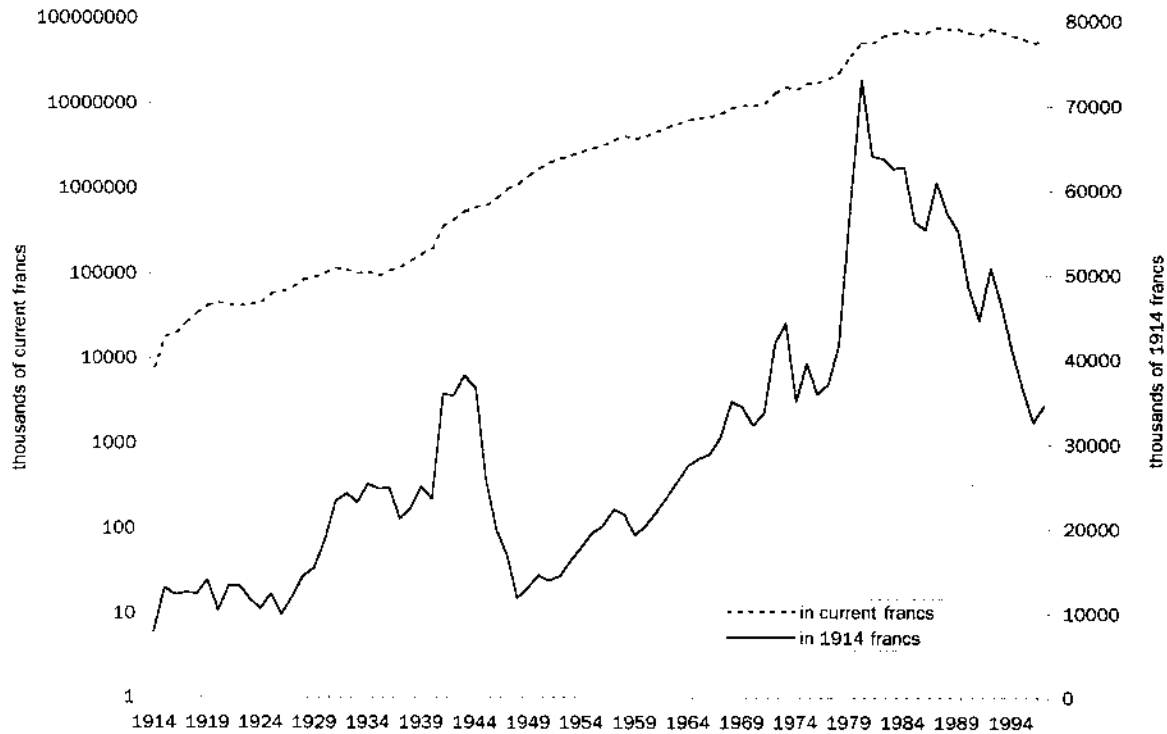
At first sight, a reasonable index of the Bank's evolving role within the monetary system is offered by the nominal size of the balance sheet. In fact, on first analysis, it is precisely through its lending – and variations therein – that the bank of issue is directly linked to the process of monetary creation. The growth of the current value of this lending during the century is a clear illustration:

The pattern of the current value of the Bank's assets from 1914 to the end of the century is, in practice, a tautological reflection of the main stages in the process of monetarization of the French economy.⁷ The long-term growth rate of the issuing institution's lending is correlated with the rate of growth of the money supply. The overall inflation of the Bank's assets can thus be read, following sound

⁶ Thus conceived, the study could use not only the published sources of the bank of issue, those most commonly used, but also its main archives, consultation of which has been easier for some years now thanks to the reorganization of the archive department of the Banque de France and the action of the "Mission historique de la Banque de France". Special thanks to their staff.

⁷ Michèle Saint Marc, *Histoire monétaire de la France, 1800-1980*, (Paris, PUF, 1983), p.109 ff.

FIGURE 1 - Banque de France assets in the twentieth century in nominal terms (semi-long scale) and in real terms (arithmetic scale)



quantitative logic as the indicator – if not the essential factor – of French inflation during the century.⁸ The historical and theoretical problem of central-bank independence, i.e. that of its monetary policy powers, is essentially grafted onto this basic correlation.⁹ Inevitably more normative than explanatory, such an approach does not enable one to grasp the reality and the evolution of the role played by the central bank within the financial system. Analysis of the Banque de France's assets provides a somewhat more adequate viewpoint.

Measuring the Banque de France balance-sheet in constant prices, like that of any other bank, is a most useful tool for assessing its *real* (not just nominal) role within the financial system over time.¹⁰ From this perspective, the similarities between the central bank and the rest of the banking system, at least until the end of the 1970s, are striking: the same overall stagnation of the balance-sheet size, more or less at its 1914 level, from the First World War until the early 1950s,¹¹ the same basic growth following the Second World War to the end of the 1970s. So conceived, the evolution of the role of the Banque de France certainly cannot be disjoined from the general trends of the French financial system. However, three exceptional episodes stand out, corresponding to the operation of real pressures on the Bank's balance sheet: the inflow of international capital from Poincaré's stabilization until 1932, the German occupation from 1940 to 1944, and entry into the European Monetary System (EMS) in 1979-80. These were three widely differing shocks, but with one element in common: all three were external to the French financial system. The impediments to the increase in the real size of the Bank's balance sheet thus underscore that its role depended both on developments internal to the French

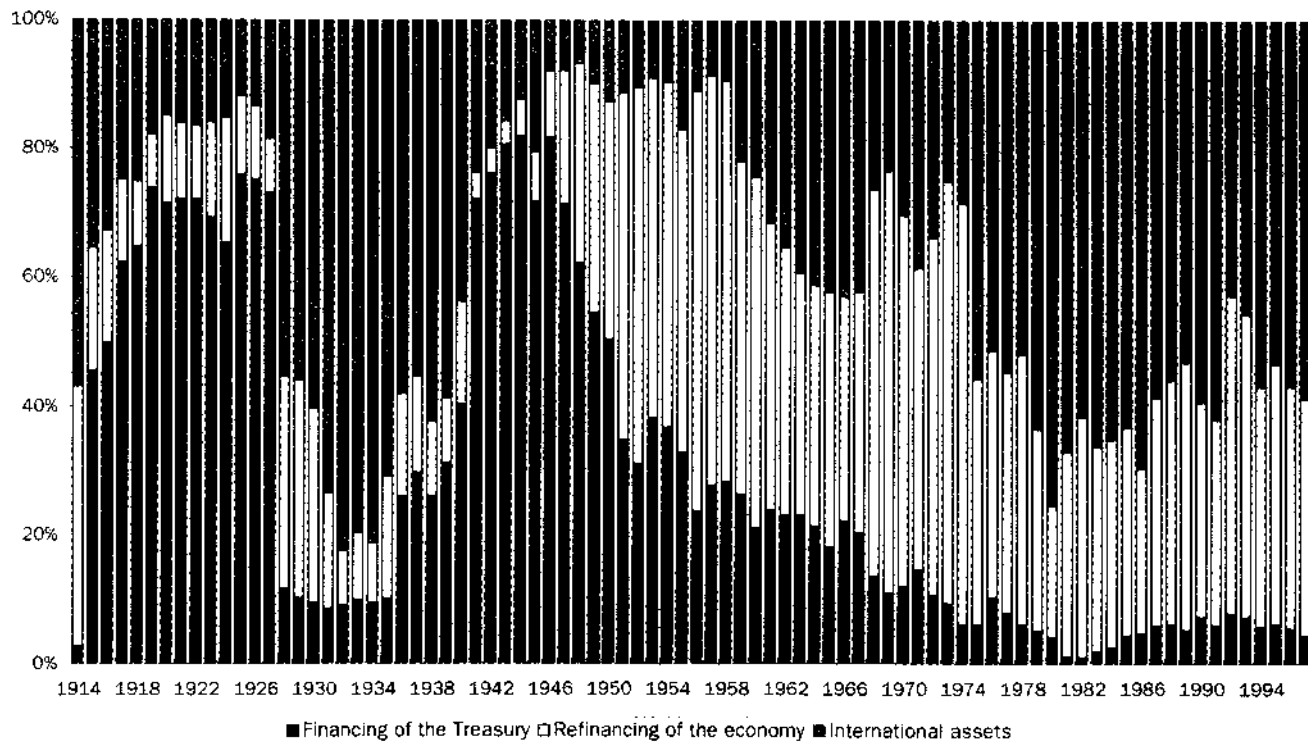
⁸ Alain Prate, *La France et sa monnaie. essai sur les relations entre la Banque de France et les gouvernements*, (Paris, Julliard, 1987).

⁹ Milton Friedman, *Inflation et système monétaires*, (Paris, Calmann-Lévy, 1969), p. 259 ff (French translation of *Dollars and Deficits*, 1968).

¹⁰ Jean Bouvier, "Pour une enquête, système bancaire et inflation au XXe siècle", *Recherches et travaux, bulletin de l'Institut d'Histoire économique et sociale de Paris I*, n° 5, 6, 7, 8, 1977-78.

¹¹ Michel Lescure, "Banking in France in the Inter-War Period", in C.H. Feinstein, ed., *Banking, Currency, and Finance in Europe Between the Wars*, (Oxford, Clarendon Press, 1995), pp. 315-318.

FIGURE 2 - The composition of the assets of the Banque de France in the twentieth century



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system and on the exogenous impact of the international financial system. At this merely quantitative level, however, the exact nature of its functions does not emerge clearly enough. A more qualitatively oriented analysis of the structure of the balance sheet during the entire century, especially on the asset side, enables us to take its measure more precisely.¹²

The changing structure of the Bank's loan assets depicts its role within the French financial system with great clarity. We find three main periods. From the First World War to the start of the 1950s claims on the Treasury were by far the most important asset item, marking a radical structural break with the pre-war period (from 1917 to 1927 such claims accounted for more than 50 per cent of the Bank's assets, and again from 1941 to 1950). The only exceptional sub-period was the decade from 1928 to 1938, with a temporary decline in claims on the Treasury in favour of reserve assets (gold and foreign exchange). In the 1950s, 1960s and 1970s refinancing the economy was preponderant, peaking in 1956-57 and 1973-74 (at more than 65 per cent of total assets). From the end of the 1970s onwards, monetary reserves become dominant, at the expense of credit to the economy, and even more so of credit to the Treasury, which fell to a tiny share of assets (under 10 per cent) from 1973 and actually disappeared in some years (1981-1983). Recent developments thus represent a reversion to the balance-sheet structure characteristic of the pre-1914 period.

Over the long run the structure of lending underscores the successive main functions within the French financial system: Treasury's bank, bankers' bank, and reserve bank. These different functions, each of which was paramount in different periods, corresponded to an evolution in the notion of financial stability itself. While there is no questioning that the tendency to inflation of the

¹² We have followed the three-part division of issuing institution assets used in the publications of the finance committee of the League of Nations beginning in the 1920s and adopted in France by the INSEE in the early 1950s (see INSEE, *Mouvement économique en France de 1938 à 1948*, (Paris, PUF, 1950), p. 168-69. The principles of aggregation of the various items used here are set forth in the methodological appendix.

assets of the Banque de France accompanied the secular devaluation of the franc, as we have seen, the overall stability of the French financial system during the century is equally clear, and in any case more pronounced than in such other countries as Germany and the United States.

This "paradox" of French financial history, observed by Jean Bouvier,¹³ lies at the centre of the twentieth-century history of the Banque de France. How was it possible that the Bank, in many respects the beneficiary of the banking system, whose ups and downs were reflected in almost mechanical fashion in the real trend of the central bank's balance sheet, became the keystone, guaranteeing *in the last resort* the overall stability of the national financial system? And above all, what role was played by the changes in the international financial system with which the issuing banks had to reckon, and brutally so, following the suspension of the gold standard and the impossibility of its restoration? The questions encapsulate the main problems for a study of the successive transformations of the Banque de France in the twentieth century.

The 1920s and 1930s: from bank of issue to central bank

The rupture brought about by the First World War in the French (and international) financial system is readily seen in the completely new pattern of the Banque de France balance sheet from the early 1920s up to 1928: sustained, unprecedented growth in the state borrowing requirement to repay the war debt and then finance reconstruction; the decline in bill discounting, which was reduced by the war and the moratorium of August 1914, attested to throughout the conflict and for the decade that followed it by bills transferred to non-liquid assets and the stagnation of the Bank's commercial bill portfolio, except during the economic crisis of 1920-21; the generalized suspension of the international gold standard and the consequent

¹³ Jean Bouvier, "The French Banks, Inflation and the Economic Crisis, 1919-1939". *The Journal of European Economic History*, vol. 13, n° 2, autumn 1984, pp. 29-90.

shift from fixed to floating exchange rates, rendered palpable in 1915 by the appearance of foreign currency loans, destined to expand sharply in the years that followed.

Subjected to rapid change in the overall architecture of the financial system, during virtually the entire interwar period the Bank pursued – more or less resolutely depending on economic and political conditions – the goal of a return to monetary stability, or the structure and operating conditions of the prewar era, namely a largely private, decentralized system with built-in adjustment machinery and in which financial intermediation still did not have a dominant role. Obviously, that system was based on the gold standard underlying the value of banknotes. In the immediate aftermath of the First World War, as in 1871, the Bank sought to restore that standard and thus to continue even after 1914 in the role that its statute had assigned it throughout the nineteenth century.¹⁴

As a result, the policy of the Bank was repeatedly criticized, beginning in the 1930s, for a failure to adapt its objectives to the new postwar financial realities.¹⁵ This rigidity has been attributed to various sources: the persistence of the Bank's private law nature or even the character of the key governors, such as Georges Pallain (1897-1920), Georges Robineau (1920-1926) and Jean Tannery (1935-1936), or of the most influential members of the board of directors, such as Edouard de Rothschild and François de Wendel, until the reform of the Bank by the Popular Front government in the summer of 1936.¹⁶ From another point of view, however, one may seek to explain the Bank's interwar difficulties by examining the way in which the war-induced transformation of the financial system made the objective of restoring monetary stability inadequate, *de facto*, and thus forced the practices of the Bank to evolve, like it or not.

¹⁴ Marcel Netter, *Histoire de la Banque de France entre les deux guerres, 1918-1939*, (Monique de Tayrac, Pomponne, 1994), pp. 39-56.

¹⁵ Bouvier, *Un siècle...*, *op. cit.*, pp. 155-160.

¹⁶ Jean-Noël Jeanneney, *François de Wendel en République, l'argent et le pouvoir, 1914-1940*, (Paris, Le Seuil, 1976).

The relationship between the Banque de France and government dominates the monetary history of the interwar period, and for good reason. During the 1920s in particular it was important, owing to the affair of the false accounts, which hastened the fall of the Herriot government in April 1925.¹⁷ The issue recurs continuously in former governor Emile Moreau's work on the monetary stabilization of 1926-28.¹⁸ Immediately after the Great War it crystallized around the problem of the Bank's advances to the Treasury both during the conflict and afterwards, to finance demobilization and the maintenance of the occupation troops. These advances totaled 27 billion francs from August 1914 to July 1919, or slightly more than 14 per cent of total public spending during the period.¹⁹

The repayment of these loans was thus at the centre of the deflationary monetary policy pursued by the Bank as the condition for a credible restoration of the stable gold parity of the prewar era. Despite solemn promises by the successive governments of the National Bloc (the François-Marsal convention of April 1920), the repayment of the Banque de France's loans to the Treasury – which depended, in practice, on the payment of German war reparations – did not take place. Indeed, the advances increased again in 1925-26 to an extent unprecedented in peacetime.²⁰ Can we read this as proof of the intransigence of a central bank still obstinately anchored to observance of contracts, blinded by the nominal illusion and the chimera of return to the old monetary regime? Perhaps. But the continuous advances to the Treasury from 1914 to 1926 are the symptom, rather than the unlikely cause, of the fact that the financial structure had been utterly changed by the war. In fact, a new function for the bank of issue was emerging.

The importance of claims on the Treasury in the Bank's balance

¹⁷ Bertrand Blancheton, *Le Pape et l'Empereur, Banque de France, Trésor et politique monétaire de la France (1914-1918)*, Paris, Albin Michel, 2001.

¹⁸ Émile Moreau, *Souvenirs d'un gouverneur de la Banque de France*, Paris, M. Th. Genin, 1954.

¹⁹ Saint Marc, *op. cit.*, p. 208.

²⁰ Netter, *op. cit.*, pp. 127-131.

sheet beginning in 1914 (and generally throughout the entire interwar period) did not lie in their share of the state borrowing requirement, which was comparatively low (14 per cent). Mainly, on a different plane these credits testified to the change in the scale of the public debt itself, which certainly marked the French financial system for the rest of the century.²¹ Central bank advances were an essential instrument in managing the State's floating debt, as in the summer of 1925 when the new advance of 6 billion francs that Caillaux sought was allocated to cover a large volume of maturing short- and medium-term paper issued in 1922 and 1923 by the Treasury and by Crédit National.²²

The fact that the public debt continued to count so heavily through 1926 is the proof – more so than the machinery of advances to the Treasury, which was merely the symptom – that the Banque de France was no longer capable of performing its statutory role within the financial system. The high level of the State's floating debt and its broad diffusion, as Jacques Rueff has emphasized, threw doubt on the Bank's ability to control the money supply by means of discount rate manoeuvres. If the rate was higher than that on Treasury paper, the holders would elect to redeem their paper rather than turn to the Bank for refinancing.²³ Even before the war the Bank had lost control of the money market owing to the unprecedented growth and the diversification of the floating debt.

The other key factor in the transformation of the issuing institution's function, in practice, was the suspension of the international gold standard. The all but universal suspension of convertibility in 1914, and even more importantly the end in 1919 of exchange-rate solidarity among the Allies, thrust the French financial system into a new international payments environment subject to considerable exchange rate variability. The Banque de France, as was recognized at the end

²¹ Robert Delorme and Christine André, *L'État et l'économie, un essai d'explication de l'évolution des dépenses publiques en France, 1870-1980*, (Paris, Le Seuil, 1983).

²² Netter, *ibid.*

²³ Jacques Rueff, "Le mécanisme de l'escompte et le taux des bons de la défense nationale", *Revue Politique et Parlementaire*, vol. CXXVIII, 1926, cited in B. Blancheton, *op. cit.*

of the war by Jules Décamps, editor of the Bank's *Etudes économiques*, then began to get acquainted, not without difficulties at times, with the basic irrationality of the foreign-exchange market and with the limits of international monetary cooperation.²⁴ Above all, the increase in short-term capital flows (both cause and consequence of the cyclical leads and lags that so heavily marked the 1920s and early 1930s) had the effect of cancelling the significance of the issuing institution's traditional function of defending the external (hence also internal) value of the national currency.

The reality of this change was demonstrated, in reverse, by the Bank's role in the exchange rate crisis of March 1924. To combat speculation against the franc, with the intermediation of the Banque Lazard committing the proceeds of loans obtained from private American and British banks,²⁵ it was forced to recognize the new dimension of the problem of monetary stability and its novel need to try to insulate the national financial system from the international context. That is, the function of bank of issue was already evolving towards those of the true central bank.

A decisive turning-point in this process was the stabilization of the franc between 1926 and 1928. The Poincaré franc, which lasted from the *de facto* stabilization in the autumn of 1926 to the legal stabilization of June 1928, was a milestone in the long-term evolution of the Bank's functions. At the end of 1928 Emile Moreau, who took over as governor following the departure of Robineau in June 1926, addressed the shareholders in the following terms: "We are faced with an event of major importance in financial history: a new franc has been created. Resigning itself, in the public interest, to an unfortunately inevitable sacrifice, the legislature has ratified the

²⁴ Jules Décamps, *Les changes étrangers, exposé général des conditions et des moyens de règlements des comptes internationaux et de la crise des changes 1914-1921*, (Paris, Librairie Félix Alcan, 1922), p. 271. Cf. O. Feiertag, "Banques centrales et relations internationales au XXe siècle", *Relations internationales*, n° 100, winter 1999, pp. 360-63.

²⁵ Raymond Philippe, *Le drame financier de 1924-1928*, (Paris, Gallimard, 1931); Jean-Noël Jeanneney, "De la spéculation financière comme arme diplomatique. À propos de la première "bataille du franc", November 1923-March 1924", *Relations internationales*, n° 13, 1978, pp. 5-27.

devaluation of our national currency. On the other hand, it has also guaranteed its convertibility into gold. After fourteen years of inconvertibility, the franc is once again a hard currency, backed just as solidly as the strongest world currencies."²⁶

The "stabilization balance sheet" published by the Bank on 25 June 1928 perfectly mirrors these radical changes. The devaluation of the franc's gold parity by nearly four-fifths meant, *ipso facto*, the accounting revaluation of the Bank's reserve assets (gold and foreign exchange), which thus suddenly came to represent the majority of the institution's assets (peaking in 1932 at 80 per cent). The windfall gain in francs resulting from the revaluation of the reserves was allocated – following a logic that would later be standard but that at the time was highly innovative – to paying off the Bank's advances to the Treasury. Apparently, as the governor explained, at the cost of a devaluation that essentially liquidated the liabilities produced by the war, the bank of issue could return to its statutory role as guardian of the currency's stability. Nevertheless, the way in which the return to stability had been achieved and the very nature of the now mixed guarantee of the franc's value betrayed the change in the Bank's functions, hence in the very substance of the notion of stability.

The most significant new element in the stabilization balance sheet, even more important than the spectacular fall in claims on the State, was the large share among the Bank's assets of foreign currency reserves, which on 25 June 1928 amounted to over 36 billion francs or more than 40 per cent of total assets, far more than the value of gold reserves proper.²⁷ Since the autumn of 1926 foreign-exchange transactions had been effected in the new legal framework created by the law of 7 August 1926, authorizing the Banque de France to intervene directly in the foreign exchange market. These interventions,

²⁶ Banque de France, *Compte rendu des opérations de la Banque de France pendant l'année 1928*, (Paris, Imprimerie P. Dupont, 1929), p. 3.

²⁷ J. Bouvier, "À propos de la stratégie d'encaisse (or et devises) de la Banque de France de juin 1928 à l'été 1932", *Recherches et travaux, bulletin de l'Institut d'Histoire économique et sociale de Paris I*, n° 13, December 1984.

long hidden in the Bank's accounts as "miscellaneous," were now brought fully to light, making explicit the fact that the value of the franc was guaranteed by a mix of assets (gold and currencies).

In an international monetary regime of variable exchange rates, and beginning from the legal changeover of 1926-28, the Bank's defence of the stability of the monetary base took on a new dimension. Domestic monetary stability presupposed that the central bank could attenuate exchange rate fluctuations both by direct intervention and through international agreements for central-bank cooperation. The international credit crisis that began in 1931 strengthened this function still further, especially with the creation, under the tripartite accords of September 1936 and on the morrow of a new devaluation of the franc, of the Exchange Rate Stabilization Fund, whose operation was naturally entrusted to the Banque de France. The Fund's role, analyzed at the time with great clarity by Charles Rist, was to insulate the national financial system from international financial fluctuations, like the "barrier of flame that surrounds Brunhilde on the pyre."²⁸

There is no doubt, then, that the twentieth-century transition from the gold standard to the gold-exchange standard also, in the end, modified the very meaning of "monetary stability". The concept came to be represented, in practice, by the relative stability of currencies in their relations with one another and gradually turned into the notion of defence of the relative stability of the national financial system within an international system marked by instability. This sea change in the operating conditions of the French financial system lies directly at the origin of the mutation of the role of the Banque de France. This was also reflected in the Bank's organization chart, with the appearance in 1926 (and steady, rapid growth continuing right down to the present) of an office for foreign exchange and external relations.

This transformation was accompanied by a slower evolution of the Bank's role within the national financial system: having become

²⁸ Charles Rist, "Les fonds d'égalisation des changes et leur action sur les prix et sur l'activité économique", *Revue d'économie politique*, 52/6, 1938, p. 1545. Cf. O. Feiertag and A. Plessis, "Conjoncture et structures monétaires en Europe à la fin des années 1930", *Revue Économique*, vol. 51, March 2000.

the lender of last resort, the Banque de France increasingly performed the function of a true *central bank*. The transition from bank of issue to central bank may have come about more slowly than in other countries, but it was essentially achieved in the 1920s and 1930s, albeit haltingly, with forced advances and retreats. The process was strictly bound up with the powerfully obstructed structural changes within the money market during a period marked by crisis and instability of both domestic and foreign origin.

The real transformation in the operating conditions of the money market provoked by the upheavals of the First World War is spotlighted by the Bank's own analyses during the stabilization years of 1926-28. Among the members of the renovated technostructure that came to head the Bank with Emile Moreau in 1926, the most lucid analyst was certainly Pierre Quesnay, a brilliant student of Charles Rist, whom he assisted on the war-reparations committee and the finance committee of the League of Nations. As he said in 1928, the evolution of financial structures since the war and especially the ever-increasing importance of the large deposit banks within the credit system ended up by eliminating all effective control over the money market by the Banque de France. The Bank's bill portfolio, which in 1913 had still accounted for nearly half the average value of the top four deposit banks' bill portfolio, had fallen to just 12 per cent in 1928.²⁹ In addition to this loss of relative weight, the large deposit banks by now had virtually renounced discounting operations with the Banque de France, which they continued to view throughout the interwar years as both judge and jury. And in fact, as the growth in its direct customers until 1935 shows, the Bank continued to engage in commercial lending. This observation prompted the drafting, between 1928 and 1930, of an ambitious plan for the reorganization and international expansion of the financial markets under the guidance of a bank of issue whose functions were to be renovated, abandoning all commercial operations and acquiring new instruments for intervention, in particular for open-

²⁹ Archives de la Banque de France (ABI) 7ème I 225, boîte 35, " Moyens d'action de la Banque sur le marché," note de Pierre Quesnay, direction des Études économiques, June 1928.

market operations on the British model.³⁰ "Regulating the amount of currency in circulation, maintaining the capability to cut down commitments sharply at any time in order to contract the volume of credit, countering the trends of the stock exchange and prices," wrote Quesnay in 1928, "are now the essential tasks of the bank of issue, in addition to safeguarding the currency."³¹ The Depression of the 1930s at first impeded and then, from 1936 to 1938, fostered this new functional evolution.

The onset of the Depression in France coincided with a succession of severe banking crises between October 1930 and November 1931, which resulted in the failure of some 230 banks. Most of these – except Banque Nationale de Crédit – were local or regional institutions, such as Adam in Boulogne-sur-Mer, Charpenay in Grenoble and the Banque d'Alsace-Lorraine. Is it true, though, that the Banque de France was passive in the face of this crisis, and even deliberately accelerated the failure of some banks to avoid having to compete with them in one financial centre or another? The dispute developed in the later 1930s, fueled in particular by the banker Charpenay himself.³² Historians have rightly studied the question mainly through the Banque de France's direct customer portfolio, i.e. the bills accepted for discounting without the intermediation of another bank.³³ It turns out that the bank of issue definitely kept up its commercial business throughout the interwar years, cultivating direct customers and actually seeking to cope with the depression-induced profit decline by increasing it; and the share of direct claims on customers in total assets reached its all-time high in 1935 at 52 per cent, just when the prolonged stagnation of economic activity reduced the volume of bills available for discounting. In any case, the banking crisis of 1930-31 made it clear

³⁰ Cf. Kenneth Mouré, *Managing the Franc Poincaré: Economic Understanding and Political Constraint in French Monetary Policy, 1928-1936*, (Cambridge, CUP, 1991), pp. 120-145.

³¹ P. Quesnay, *ibid.*

³² G. Charpenay, *Les banques régionalistes*, (Paris, Éditions de la Nouvelle Revue Critique, 1939).

³³ J. Bouvier, *Un siècle de banque...*, *op. cit.*, p. 158; Pierre-Cyrille Hautcoeur, "La Banque de France et la crise bancaire de 1930-1932", *Études et Documents*, II, 1990, pp. 295-315. Yasuo Gonjo, "La modernisation de la Banque de France (1930-1946)", *Études et Documents*, VIII, 1996, pp. 285-295.

that at that time the Banque de France was not yet performing the strictly regulatory function of a central bank serving as last-resort guarantor of the overall stability of the system. From this angle, it is clear that in the face of the Depression the reform of 1926-28 had no effect whatever.

Yet the crisis also brought to light new elements showing that the decade of the 1930s saw decisive progress in the historic transformation of the Bank's functions. The reality of the change emerges more clearly at the local and regional than at the national level, if one observes and compares the role played in the banking crisis by the various branches of the Banque de France (161 in 1930) in the individual financial centres.³⁴

At this local and regional level, three main conclusions can be drawn: (1) Direct discounting was most common in the centres (Longwy, Charleville-Mézière, Saint Quentin, Mazamet, etc.) where the local banking structure was weak or absent, or inadequate to the specific financing needs of the local economy (credit for small and medium-sized enterprises or export credits, as is shown by the fact that agricultural credit always accounted for the bulk of direct discounting). In these centres, in the 1930s the Bank was still playing the traditional role of substituting for or supplementing the activity of the commercial banks. (2) The refinancing of local and regional banks was massive, decisive to the survival of many, as in Fougères, Cognac, Limoges, Roanne, Rouen, Bordeaux, Tours and Strasbourg, all centres with a well-developed banking network where direct customers were few if any. In Grenoble, for example, following the crisis of November 1931, more than 80 per cent of the Banque de France branch's portfolio consisted of rediscounting for the three leading local banks, Banque du Dauphiné, Banque de l'Isère and Banque Charpenay. The latter in particular received 13.5 million francs in non-statutory rediscounts

³⁴ Laurence Barry, "La Banque de France et les banques régionales du Nord au cours de la crise bancaire des années Trente", *Études et Documents*, II, 1990, pp. 281-293; O. Feiertag, "La Banque de France et la crise bancaire des années 1930: une approche territoriale", in M. Lescure and A. Plessis, *Les banques locales et régionales en Europe au XXe siècle*, actes du colloque de Nanterre de novembre 2000, forthcoming.

of notes (representing an overdraft, not a commercial transaction), or 20 per cent of all the bills rediscounted to the banks in Grenoble, nearly equal to the amount of the bills of this type rediscounted to the other two banks (17 million). (3) The protraction of the crisis spotlighted the limits of discounting and its regulation under the statute as the sole instrument for controlling liquidity in the banking system. Passive by nature, discounting also proved to be lacking in flexibility and to constitute a risk for the issuing institution itself (in Cognac, for instance, the rediscount to Banque Charpentier alone, which was locked in by the collapse of cognac exports due to the devaluation of sterling, came to account for 73 per cent of the total asset portfolio of the local Banque de France branch.)

The central bank's difficulties during the banking crisis of the 1930s broadly reflect the still highly decentralized and geographically heterogeneous state of the French financial system. The concentration that was triggered by the crisis – accompanied by the increase in State agencies and financial institutions starting in 1936 and then by the Second World War – quickly transformed the system itself. At the same time the role of the Bank itself was substantially modified, along with the notion of stability.

The Banque de France and the construction of the debt economy (the 1930s and '70s)

The concept of the "debt economy" first made its appearance at the end of the 1970s in France, notably in the work of the so-called "Banque de France school," just as the reality of the phenomenon began to be called into question (a frequent coincidence in the history of economic thought).³⁵ To simplify, a "debt economy" is essentially characterized by the prevalence of bank credit within the financial system (at the expense of other forms of direct corporate finance) and

³⁵ Vivien Lévy-Garboua, "Le taux de change et la politique monétaire dans une économie d'endettement", *Annales de l'INSEE*, n° 32, 1978; Gérard Maarek, "Monnaie et inflation dans une économie d'endettement", *Revue d'économie politique*, 1/1978.

by the *compulsory* refinancing function of the central bank.³⁶ On the theoretical hypothesis of a totally closed economy, this dual configuration corresponds to the possibility of practically automatic and unlimited adjustment of capacity to the constant increase in the financial requirements of a growing economy with full employment.

This, then, is the main problem in the history of the French financial system in the second half of the twentieth century. In 1974, immediately after leaving the Banque de France and in the ominous context of the “collapse of the international monetary system,” Olivier Wormser publicly summed up the terms of the question with uncommon clarity for a central banker, albeit honorary: “To tame an inflation that is of the order of 13 per cent, we must accept sacrifices and take risks [...]. A severe and mounting inflation such as we are experiencing can only be defeated at the cost of a total halt to economic expansion.”³⁷ The long-lasting perception of these as mutually exclusive alternatives – *either* economic growth *or* monetary stability – had prompted the gradual construction of the French debt economy in the late 1930s and 1940s. This construction was intimately bound up with the transformation of the Banque de France and the financial system as a whole.³⁸

The nationalization of the bank of issue, effected in two stages in 1936 and 1945, did not alter the statute’s definition of its operations, which remained utterly unchanged until 1973 despite the political intentions first of the Popular Front and then of the Liberation government. In the meantime the role and position of the Bank had changed considerably. More and more explicitly and automatically, it was supplying the liquidity needs of a rapidly expanding credit system

³⁶ Denise Flouzat, *Économie contemporaine*, vol. 2 *les phénomènes monétaires*, (Paris, Thémis/PUF, 10th edition, 1990), pp. 67 ff.; Sylviane Guillaumont-Jeanneney, *Monnaie et finances*, (Paris, Thémis/PUF, 1998), pp. 52-56; Françoise Renverez (under the direction of), *Les systèmes financiers, Les Cahiers Français*, n° 224, January-February 1986.

³⁷ O. Wormser, “Peut-on simultanément vaincre l’inflation et favoriser l’expansion?”, *Le Figaro*, 26 May 1974, p. 7.

³⁸ Feiertag, *Wilfrid Baumgartner, biographie d’un financier public, contribution à l’étude des dynamiques historiques du système financier français au XXe siècle*, (Thesis at Université de Paris X – Nanterre, 1995) (in course of publication).

within an economy that through the 1950s was only partially open but that then returned to rapid growth within the burgeoning European Community. Usually interpreted as a loss of monetary power by the bank of issue,³⁹ this development – in the dramatically new context of sharply rising liquidity needs due to Depression, war and reconstruction – also, and perhaps even more radically, posed the problem of the overall stability of a financial system subjected to domestic and external strains that had no real precedent in the modern era.

The exceptional nature of French financial history between the 1940s and the 1970s emerges with great clarity from the largely novel structure of the Bank's balance sheet during those decades. Advances to the Treasury regularly accounted for a substantial part of total assets. These advances had reappeared in 1936, with the beginnings of rearmament, and had peaked during the war, when they financed the entire payment to Germany of the daily occupation allowance, but they always remained at more or less a quarter of the Bank's assets from the end of the war until 1967. The most striking fact, however, is the quintupling of refinancing to the banking system between 1950 and 1974. In sharp contrast to Poincaré's stabilization and more recent events, this entire period was characterized by a remarkably low share of reserve backing for the money supply in the Bank's asset structure, despite the notable improvement that, until May 1968, accompanied the return of the franc to external convertibility, decided at the end of 1958. The pattern of balance-sheet developments during the "Glorious thirties" was thus at the core of the structural transformation of the French financial system. These developments were also bound up with the more-or-less pronounced inflationary tendency that prevailed until the turnabout of the 1980s.

The diverse mechanisms that made this transformation of the French financial system possible had in common, in fact, that they had prompted the central bank to finance, if need be as a last resort through the creation of money, first the war and the Nazi occupation, then

³⁹ M. Saint Marc, *Histoire monétaire de la France*, *op. cit.*, p. 292; A. Prate, *La France et sa monnaie...*, *op. cit.*, Part III, "La Banque de France dépendante", p. 145 ff.

reconstruction and economic modernization. This occurred at times with the intermediation of a strictly controlled banking system, at times thanks to the growing integration of the central bank into the Treasury circuit, as through the automatic refinancing of the special loans of the Caisse des Dépôts et Consignations. Most of these mechanisms basically date to the Second World War. The Banking Law of 1941 first defined, within the corporative economic organization laid down by the Vichy regime, the legal framework of state control of the banks, with the centralization of banking risks under the supervision of the central bank first of all and secondarily of the Treasury.⁴⁰ Thus, at the start of the 1940s, the basis for the control and regulation of the credit system was laid, and the system, reinforced by post-Liberation reforms (the creation of the national credit council, chaired *de facto* by the governor of the Banque de France), continued to operate until the mid-1980s. This helped to transform and consolidate the structure of the financial system, which had become thoroughly hierarchical and segmented.

Within this regulatory framework bank liquidity was doubly constrained by the discount ceiling imposed on the banks in 1948 and retained until 1971 and a minimum portfolio requirement for government paper (abolished in 1967). As long as the money market was structurally managed by the central bank, above all through exchange controls, traditional management of discounting appeared to ensure the stability of the financial system, or at least its more commercial component, in that the liquidity that moved through the Treasury circuit was by definition outside the control of the market.⁴¹ Actually, this control was rendered largely inoperative by the uninterrupted growth of bank deposits over the entire period and the proliferation of exceptional procedures for liquidation of bills above the ceiling which, as the wisdom of the day had it, soon transformed the ceiling on discounts into a floor and the minimum portfolio requirement into a ceiling.⁴² The rapid growth

⁴⁰ Claire Andrieu, *La banque sous l'Occupation, paradoxes de l'histoire d'une profession, 1936- 1946*, (Paris, Presses de la FNSP, 1990).

⁴¹ Philippe Aymard, *La banque et l'État, la politique économique et l'évolution des techniques bancaires en France depuis 1945*, (Paris, A. Colin, 1960), pp. 41-60.

⁴² Henri Koch, *Histoire de la Banque de France et de la monnaie sous la IV^e République*, (Paris, Dunod, 1983).

throughout the 1950s of medium-term credits within the Banque de France portfolio is the clearest possible demonstration of this.

The Bank's acceptance of medium-term credits (2-5 years) for discounting was authorized before the end of the war by a simple decree by the Bank's general council (11 May 1944). This was the last step in a process that had begun at the start of the century if not earlier and been accelerated by the crisis of the 1930s. The machinery for liquidation of medium-term credit, apparently unimportant, was actually a radical innovation, in that for the first time it institutionalized the credit transformation cycle, financing investment through the creation of money.⁴³ Combining the various components of the postwar financial system (commercial banks, public financial institutions and the central bank), the growth of medium-term credit that could be liquidated was constant from the end of the war through the 1950s; in 1956-57 it accounted for over 20 per cent of all credit to the economy. This instrument thus was not only the essential component of finance to the nationalized corporations (Electricité de France, Renault, etc.) during reconstruction but also of credit for construction and - until recently - export credit.

The development of mobilizable medium-term credit is perhaps the best representation of the new social consensus that reigned from the 1940s to the 1970s. The result was an overemphasis on the creative function of money, at the expense, at least temporarily, of its role as standard of value. This was the main consequence of the debt economy. The role of the bank of issue was necessarily recast. Defence of the value of money was replaced, as an objective, by responsibility for the overall stability of a system whose financial needs exceeded the saving capacity of an economy which for the entire period was open to a very limited extent, especially as far as capital flows were concerned. In fact, the institution of the debt economy was ultimately justified by the fact that the financial system was relatively closed.

The opening of the system, which was increasingly pronounced

⁴³ Jean-Pierre Patat and Michel Lutfalla, *Histoire monétaire de la France au XXe siècle*, Paris, Economica, 1986, p. 122.

following the return to external convertibility in 1958 and with European economic integration, and the banking reforms of 1966-67, accompanied by the first attempt to end foreign-exchange controls, gradually remodelled the financial structure. Since the late 1970s, in the new international framework of floating-exchange rates and European monetary union, the evolution of the financial system once again redefined the role of the Banque de France.

This influence is demonstrated by the Bank's abandonment, in 1971, of the discount in favour of open-market operations as the main tool for liquidity management. Introduced in 1938, the Bank's power to intervene in the money market with purchases and sales of securities was long strictly circumscribed, as is apparent from the balance sheet (except during the war years, when bills eligible for discounting declined as economic activity itself weakened). As long as the money market remained internal to the issuing institution, there was no obvious justification for intervention in the free market outside the Bank.

After 1966, however, the powerful expansion of bank deposits caused by banking liberalization, together with the explosive growth of the eurodollar market, increased the relative importance of the money market, whose rates, greatly influenced by euromarket rates, fell below the discount rate. These developments led Olivier Wormser, governor since 1969, to make open-market operations the main tool for the Bank's regulatory action within the banking system, along the lines of the money-market reform that he himself had called forⁱⁱ and the model of most European central banks. This offers one more proof, if any were needed, that the historic transformation of the central banks in the 1970s, in France as in Germany and Italy, was strictly connected with the new conditions then emerging in the international money market.¹⁵ More generally, it radically linked the evolution of

ⁱⁱ R. Marjolin, J. Sadrin and O. Wormser, *Rapport sur le marché monétaire et les conditions de crédit*, (Paris, La Documentation française, June 1969).

¹⁵ Stefano Battilossi, "The Eurodollar Market and Structural Innovation in western Banking, 1960-1985", paper presented at the conference *Towards a Global System? European Banks within the Evolving Economy*, Warsaw, May 2000.

the banks of issue to that of the international money and financial markets, as the history of the Banque de France in the last twenty years abundantly demonstrates.

* * *

The recent history of the Banque de France – meaning since the end of the 1970s – is still largely to be written. Nevertheless, the broad outlines have been clearly traced: the virtual elimination of advances to the Treasury, a radical disengagement from the circuit of transforming credit to the economy, and a now preponderant incidence of monetary reserve assets, especially deposits with international monetary institutions. The new asset structure was the product of the collapse of the Bretton Woods system in the 1970s and the drive for regional monetary stability in the context of European monetary integration, beginning with the creation of the EMS in 1979.

This evolution was not concluded until the mid-1980s, when the French economy shifted into the protracted disinflation that still continues. In a world grown more economically interdependent and, as a consequence, more unstable, the function of the central bank was transformed yet again in response to the new demands of a modified environment, especially on the international plane. On the one hand the monetary-issue function proper will disappear, or at least be absorbed by the European System of Central Banks, while refinancing of the economy has been rendered marginal by the development of the global money market. On the other, the main responsibility of the Banque de France now seems to have reverted to the traditional defence of the value of money, as was highlighted by the Bank's achievement of statutory independence in 1993.

It is hard to determine, as yet, whether the developments of the last two decades of the century have, as is often contended, brought the Banque de France to a sort of end of (its own) history. Certainly the repeated transformations of the institution show how its responsibilities evolved in response to changes in the national and international environment, with its vicissitudes over the course of the century. Nevertheless, the Banque de France not only managed to reformulate its mission and mandate continuously and to adapt its

instruments accordingly; throughout its history, it also fundamentally always pursued a goal of stability, though to be sure the actual content of that objective was variable, not coinciding solely with the stability of the monetary base. There is every reason to think that – through this deep-rooted and broadly shared culture of stability – the Banque de France expressed a consensus within French society, which was in tacit accord with the central bank that, in the final analysis, it brought into being.

METHODOLOGICAL APPENDIX

The structure of the assets of the Banque de France in the twentieth century

All of our statistical data are drawn from the weekly accounts of the Banque de France, which form a virtually unbroken series for the entire century, interrupted on only four occasions: from 30 July 1914 to 28 January 1915; from 20 June 1940 to 7 August 1941; from 13 July to 28 December 1944 (the balance sheet for 30 November 1944 exists, separately, but was never published); and from 31 May to 20 August 1945.

In the long run, despite the incident of the false balance sheets released from March 1924 to June 1925 (or perhaps thanks to it), the question of the accuracy of the published accounts is not really an issue. Correctness is assured, furthermore, by the *de facto* statute of the institution (which explains, in retrospect, the scandal of the false balance sheets), which is that of the Banque de France in the twentieth century, since before its nationalization.

The data are brought together in the last report of each year, except for 1914 (for which the 30 July account was used). The question was whether to calculate using weekly averages or monthly averages (as the INSEE does). Tests showed that the results did not change substantially in the long run. Among the various asset items, those corresponding to fixed assets and "sundry" were not considered (which distorts the view for 1926 and 1927, when the latter rose sharply because of the foreign currency assets concealed therein). The various asset items, whose designations naturally changed over the decades, have been grouped according to three main criteria:

- monetary reserves comprise: gold reserves and gold allocated as guarantee, sight deposits abroad, guarantee deposits with international monetary and financial institutions.

- the Bank's contributions to the Treasury comprise: coins, postal current accounts, loans and temporary advances to the State, including those deriving from direct discounting of Treasury bills, the negotiable paper of the *Caisse Autonome d'Amortissement* advances to the exchange rate stabilization fund and to the Overseas Institution of Issue, and Treasury paper redeemable in gold.

- refinancing credit to the economy comprises: the bill discount portfolio, negotiable paper acquired in France (open market), advances against gold and securities, and 30-day advances on government bills.