

**ISSUES IN FRENCH-AMERICAN ECONOMIC RELATIONS**  
**Memorandum for presentation to the French-American Chamber**  
**March 3, 1988**

**I. Background: Current Conditions in French economy.**

- A. GDP growth: 1987 1.5% (OECD est., French government est. 2.1%) ; 1988 projection, 1.5% (OECD est., French government, 2.2%).**
1. Chirac government committed to opening up economy through program of privatization, financial market deregulation, tax reductions, budget control, and labor market reforms.
  2. Should promote stronger growth over medium to long term, but economy faces structural problems in short term.
  3. Interest rates remain high, though discount rate has been lowered several times in past few months.
    - a. constrained by West German monetary discipline;
    - b. French ability to reduce domestic rates is limited by DM/franc exchange rate developments within the EMS and interest rate movements in Germany.
  4. Current account balance suffers from EMS ties, particularly lack of significant expansion in Germany, France's largest trading partner.
    - a. French domestic demand has grown relative to Germany's.
    - b. This causes France to import too much from Germany.
    - c. Current accounts have deteriorated from surplus in 1985 to probable deficit last year.
    - d. France (and Italy) replacing U.S. in supplying Germany's trade surplus.
- B. Inflation: 1987, 3.3%; will probably taper off to just below 3% in 1988.**
1. Chirac government has made fight against inflation top priority;
  2. has phased out price controls, but maintains strict wage controls in private sector.
- C. Unemployment: about 10.4% end of 1987, expected to rise to around 11% in 1988.**
1. large supply of new entrants into labor market;
  2. large supply of long-term unemployed.

#### D. Trade with U.S.

1. In 1986, the U.S. was fifth among the countries receiving French exports (7.4% of total exports) and fourth among exporters to France (also 7.4%).
2. U.S. is leading supplier of analytical and scientific instruments (32% of market), computers (52%), computer software and services (46%), electronics (38%), especially semi-conductor assembly machines, wafer fabrication equipment, equipment for testing components. Also important: engines and aircraft.
3. Principal U.S. imports: aircraft and parts, engines, motor vehicle parts, and wine.
4. U.S. investment in France has dropped over last four years for which figures available from \$9.1 billion in 1981 to \$7.8 billion in 1985, but U.S. remains France's most important foreign investor.

#### II. Issues in U.S.-French Economic Relations

##### A. In general, there seems to be more agreement than disagreement between the two countries on trade issues.

1. A number of key sectors in France's economy are dependent on foreign sources for industrial products, technology, and basic raw materials.
2. Thus, France is committed to concept of free trade, is a vigorous supporter of GATT.
3. France shares an interest with the U.S. and other industrialized economies in getting services included in GATT.
4. France is moving toward income rather than price supports for agricultural subsidies and is thus in accord with overall U.S. desires.
5. In U.S.-EEC relations, France has been "friendly partner" of both the U.S. and West Germany:
  - a. When U.S. pushed Germany to expand its economy, France supported U.S.;
  - b. but also supported Germany in criticizing U.S. agricultural policies.

##### B. The chief area of contention in recent years has involved French "buy national" policies that discriminate against foreign producers.

1. In order to foster the development of certain industries--electronics, aerospace, nuclear power generation and weaponry--France continues to subsidize them.
2. Has been challenged on these grounds by the European Community commission and also by the U.S.

3. "Buy national" policies are implemented by government agencies and state-owned corporations not covered by GATT through use of short tendering procedures or developments of specifications which favor domestic products.
4. U.S. intervenes on behalf of U.S. companies treated unfairly (e.g., current issue involving manufacturers of large electrical equipment), has had reasonable success in achieving market access in other cases.
5. U.S. seeking removal of "buy national" policies as part of the GATT government procurement code renegotiations and is conducting bilateral meetings with French government.

C. Other problem areas

1. Lack of intellectual property protection.
  - a. piracy of video cassettes; inadequate protection of software
  - b. U.S. pressing for broad discussions of intellectual property protection at GATT.
2. French government support for commercial aircraft.
  - a. May, 1987, French government announced it would provide \$975 million in support of the Airbus A330 and A340 commercial transport aircraft programs in addition to billions in support already provided.
  - b. Competes directly with Boeing and McDonnell Douglas; estimated loss of 150 sales.
  - c. U.S. questions whether Airbus is economically viable under normal criteria and consistent with GATT agreements on aircraft.
  - d. Some evidence that French officials have intervened in foreign country sales by offering political and economic inducements to promote Airbus over U.S. aircraft.
  - e. Negotiations with Airbus partner governments (U.K., Germany, France) and with GATT, little progress.
3. Export subsidies.
  - a. France--and other OECD countries as well--in some instances have tied aid credits to agreements to purchase domestic products (between \$500 million and \$1 billion for France in recent years).
  - b. OECD reached agreement in March of 1987 to control this practice in two stages ending July 1988.

III. You might be asked to comment on French Finance Minister Edouard Balladur's essay on "Rebuilding an International Monetary System," Wall Street Journal, 2/23 (attached).

- A. Balladur considers floating exchange rates a failure, discusses three possible approaches to world monetary policy coordination he considers preferable.
- B. Louvre system lacks automatic mechanisms and sanctions with enforcement beyond the control of individual governments.
- C. Suggests possibility of worldwide exchange mechanism similar to EMS.
  - 1. Would need monetary reference unit (suggests SDRs);
  - 2. automatic mechanisms that require members to adhere to margins of fluctuation around central rate;
  - 3. and sanctions--each government would be forced to intervene and draw down exchange reserves (a form of sanction in itself) in order to maintain value of currency.
  - 4. Flaws: no built-in guarantees against inflationary drift of all currencies; would probably contain asymmetries similar to Bretton Woods.
- D. A more objective system would be one organized around a standard that would play role of world reserve asset.
  - 1. Rejects gold for a number of reasons.
  - 2. Suggests possibilities of Baker's basket of commodities including gold or a basket of currencies including gold.
  - 3. Notes studies by the Committee of Twenty (IMF, 1972) considered how to devise a reserve instrument with constant real value (i.e., revised every year on basis of world inflation).
  - 4. Automatic mechanism: make each nation convert its currency into world currency at fixed rate; make settlements among central banks payable in world currency.
  - 5. Sanctions built into automatic mechanism--no country could remove itself from external constraint, since all countries would have to maintain their solvency in world currency.
- E. Doesn't decide among these choices, ends instead with a plea for the international community to "entrust a small group of distinguished people of unquestionable moral authority--who have proven their economic, monetary, and financial competence--with the task of lighting our way."