THE FINANCIAL CRISIS OF FRANCE

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THE FINANCIAL CRISIS OF FRANCE

BY

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PREFACE

Many years ago, when in H.M. Treasury, I received instructions to prepare a report on the Public Finance of France. My report, when presented, appeared to find a certain amount of favour. For, even in those Gladstonian and economical days, it was printed, and earned the approbation of the rather formidable Chancellor of the Exchequer of that time, Sir William Harcourt.

Adventuring in the same direction I also composed some papers on the policy of the Bank of France, which *The Times* did me the good service of publishing at the close, I recollect, of 1894.

I must confess that since then I have not put pen to paper on that subject. It seemed so uninteresting for the public, so dry, technical, and strange. France fed on deficits and flourished, as the Pontic king fed on poisons and flourished too. And there were those complicated accounts, the despair of even the best French experts: *budgets extra-ordinaires*, *budgets annexes*, *budgets autonomes*, *comptes hors budget, comptes spéciaux, budgets des dépenses recouvrables.* Most of this, it is true, could be simplified into the one word, borrowing.

Nor was the subject spiced by the presence of any very commanding personalities. There was no Colbert with his *front négatif*, the face that says, no. Did not Thiers pronounce that a Minister of Finance must possess the quality of *férocité?* Did not Madame de Sévigné declare for a "man of marble"? None such was visible on the foreign scene.

And then, suddenly, at the opening of 1924, a Financial Crisis sensationally appeared. It had been, indeed, long in preparation, but, when it did come, it got to work quickly. In May 1924 it overthrew, so M. Poincaré has stated, his powerful government of the Bloc National. Not a year had passed ere it swept M. Herriot out of office, the leader of the Cartel des Gauches.

M. Painlevé, the new Prime Minister, in April 1925 conceived an inconceivable plan. He rang up Mamers on the telephone, urgently offering the post of Minister of Finance to "the best hated man in France," to the outcast who had been solemnly proscribed by the Senate five years before as a public enemy, the "protégé of Germany," the despised and detested "Catiline."

This redoubtable personage answered the trunk call with the words "Je marche." Instead of the Tarpeian rock—the Treasury!

Even from across our side of the Channel, where we have enough of our own troubles and to spare, one watched, one could not help watching, this Crisis in its development with intense interest. So much went with it for the world at large, and very specially for ourselves. It was so important that our public should realise correctly the causes of its origin, its living significance, the results which it would produce.

So I thought, I hope not too rashly, that the time had come when I might venture to go in again. I do so with many a backward glance of regard for those who, whether at *The Times* or at the Treasury, encouraged me of yore.

George Peel.

27 Belgrave Square, S.W.
September 1925.

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CHAPTER I

SUMMARY OF THE ARGUMENT

"Les nations tendent à se rapprocher. Bientôt tout ce que le sol produit, tout ce que l'industrie a créé dans les différens pays deviendra un bien commun à l'espèce humaine. Tous les peuples doivent finir par reconnoître les mêmes connoissances, par se réunir pour les progrès de la raison et du bonheur commun."—Condorcet, *Vie de Turgot*, édition de 1786, p. 308.

The argument of this book is, to start with, that at the date of the opening of the Great War the system of French Public Finance was well-nigh obsolete and needed reconstruction.

It had been, in the main, the work of the revolutionary statesmen of the Constituent Assembly, and of their mighty successor, Napoleon. But during the century from 1815 to 1914 the heirs of the heroic age, though individually distinguished, were too far steeped in the accepted tradition to be able to provide France with a financial system technically abreast of modern science, or politically fitted for the times in which we live. So, in 1914, the flames of war consumed the substance of that old order, all the quicker that its virtue had departed and its sap was dry.

Thus to the statesmen of our own hour fell the ungrateful task of raising another system amid the horrors of the worst catastrophe that men have inflicted upon one another, and amid the unutterable economic welter which ensued. Like the sage Archimedes of old days, they pursued their calculations in the thick of warfare and did their reckonings in the dust.

Yet, after as close and as impartial an examination as I am able to furnish, my conclusion will be found to be that the foundations of the reforms thus accomplished, though marred by many defects, have been well and truly laid. If that conclusion be correct, then France, for the first time in her long fiscal history, which dates from Rome and still faintly bears the hall-mark of the Cæsars, stands possessed of a taxation system which, though open to criticism in many points of assessment and of levy, is soundly conceived.

Unfortunately, while this result was being slowly attained, converse things were happening on the other side of the account. In ten years' time, from the middle of 1914 to the middle of 1924, the internal national debt of France rose from about 33 milliards to about 278 milliards. Added to this was the external debt, which, if expressed in francs at their par gold value, was approximately 36 milliards.

The service of the internal debt, and also the service of about one-seventh of the external debt, was being duly met. Even this restricted payment, however, was already absorbing a high percentage of the reorganised and expanding revenue. This ratio, which for technical reasons is capable of somewhat varying calculations, may be taken as not far from 50 per cent. In the Budget of 1913 that ratio had been only 20 per cent.

The raising of this enormous debt had been dictated and justified, of course, by the necessities of the life-and-death struggle. But unfortunately there were several avoidable financial errors—so, at least, I argue—which accompanied this process. During the war, more debt was raised than need have been, and next it was issued on terms more onerous for the State than was necessary. Thirdly, after the war was over, more debt was again raised than was essential; and lastly, the error was committed throughout of arranging the maturities of the various forms of debt in a sequence which would inevitably involve the most dangerous embarrassments in the near future.

Precisely in the middle of these operations, and perhaps because of them, a new and startling factor entered upon the economic scene. The franc, of which the average yearly rate had been 25.13 to the £ in 1914, and which was still held at the rate of 26.75 to the £ in 1918, fell thenceforward to the levels which we know.

It might seem on a narrow view that this fall of the franc might exercise a not unfavourable reaction upon the Budget. So far as the internal debt was of perpetual and long-term denominations this devaluation clearly lightened the load of the State at the expense of the holders. But this pleasant consideration was neutralised by the fact that only about 150 milliards of the debt was of this order. The remainder of the internal debt was short-term and floating, and the burden of these constantly renewable obligations of 128 milliards could not readily be alleviated that way. Besides, the burden of the external debt, being a contract in sterling and in dollars, would react in the other direction to the falling franc.

It therefore followed irresistibly that, though some decline in the gold value of the franc might be possibly acceptable, having sole regard to the perpetual and long-term debt, yet no severe or sustained fall could be conceivably contemplated with favour by the authorities of the Ministry of Finance. For such a movement could not fail eventually to upset the all-essential confidence required from the holders of the short-term and floating debt, who might if they lost faith take the course of failing wholesale to renew. Thus these latter creditors constituted the really dangerous element in the situation, an element which sooner or later could only be diminished by asking the assistance of the public in a funding operation. But no funding operation would be practicable if the franc in which such an operation would be conducted had forfeited faith. Here, then, was the crux of the situation, the *articulus stantis aut cadentis Reipublicæ*. In the words of M. Caillaux, "rien à faire tant que le franc ne se sera pas stabilisé." [1]

But, then, how was the franc to be stabilised?

The argument proceeds to examine what measures were taken in this direction from 1924 up to date, and to mark what we may perhaps be excused for considering the miscalculations made, or finally the good accomplished.

Meanwhile, behind and beyond the grave

[1] *Projet de loi ayant pour objet d'assurer le plein équilibre budgétaire*, No. 1608, 1925, p. 12 of Exposé des motifs.

problem of the internal debt towered that presented by the external debt. This debt was one-seventh "commercial" and six-sevenths "political." A Himalayan range soaring up in all, as we have seen, to 36 milliards of gold francs, or, otherwise stated, about £1,400,000,000.

This problem should have been tackled and settled in 1919. Then was the unique, the appointed hour which should have been seized for settlement. If only some Prometheus among statesmen had been there to shape into a reasonable solution the molten emotions of men! If only the genius of Lloyd George or the wisdom of Wilson had seized the flying opportunity! If only Talleyrand, if only Turgot, had been there that day! Then perhaps the nations would have seen the white light of reason, and would have forgone the accursed burden of their mutual indebtedness.

The argument proceeds to consider the existing situation created by this further entanglement, and to examine the solution of it.

Finally, I proceed to ask whether we can hope that France, in spite of the extraordinary difficulties of her situation, can attain to a revenue so reorganised and to an expenditure so adjusted as to secure for herself a bearable Budget, a debt within her compass, and a stabilised franc. My conclusion is in the affirmative.

Will that desirable end, once attained, prove a permanent settlement? Not if Christendom, which since the fall of the Roman Empire has been the scene of wars or the stage for their preparation, is still bent upon death. If we cannot substitute concert for conflict, if we still refuse to grow great in common, no financial policy, however skilful or however scientific, will avail to avert the speediest and most certain ruin, no, not if there were ten Colberts or ten Caillaux in the field.

CHAPTER II

THE PENALTIES OF BAD FINANCE

"Il est des sciences absolument sereines qui ont de l'indulgence pour leurs contempteurs et les laissent en repos. La Science des Finances n'est pas de ce nombre. Elle a une terrible façon de se venger des gouvernements qui l'ignorent ou qui la bravent."—Paul Leroy-Beaulieu, *Science des Finances*, préface de la 5e Édition, 1891, p. ix.

THE financial history of France, should it ever be written in its entirety, would be a tale of many crises. From age to age, during two thousand years, a people of marvellous industry and intelligence have seen the profits of their labour intermittently swept away. Those earnings have been claimed in turn by irresistible Imperial Rome, by the feudal barons, by mediæval and Hanoverian England, by the gay and greedy princes of Versailles, by the Germany of blood and iron, by the Russia of the Bolsheviks. This ever-recurring loss, the burden of twenty centuries, has left a profound imprint upon the French people, in matters of finance "the most sensitive and easily alarmed minds in the world." [1] How to arrest that process of misfortune for the future is still the problem for France to-day.

Rome, during her ascendancy of five centuries in Gaul, constructed a fiscal system which comprised many modern features, and which, for a considerable period, seemed well justified in its results. Serious as were the criticisms directed against it in antiquity, "we must conclude that it was not fundamentally defective, since it did not prevent the marvellous expansion of public prosperity during the first two centuries of Roman occupation, and a portion of the third." [2]

Gradually, however, that which had been judicious, or at any rate tolerable, became fraught with injustice and then with ruin. It was not that the principles of the system were so bad in theory. Rome aimed, more or less on modern lines, at a balance between direct and indirect taxation, the *tributa*, on

[1] *The Economist*, February 28, 1925, p. 398.

[2] Ernest Lavisse, *Histoire de France*, 1900, Deuxième Partie, Livre Premier, Chapitre Premier, p. 165.

the one hand, and the *vectigalia*, on the other. But what had been rooted in arbitrary power shot up presently into practices which were as unjust and as disastrous as can be conceived, a system of exemptions for the rich and strong and of corresponding impositions for the poor and weak. "Men, shut up in a circle from which there was no escape, felt their energy decay. They slackened in their toil and contracted the range of their thoughts. They lost all that sense of public interest without which there is no such thing as patriotism. They no longer sought to improve their lot. A mortal poison spread throughout the social system, stupefying the intelligence and will. The evil had many causes, but when one wants to explain that species of general stagnation which characterises the end of the Roman Empire in Gaul, we must not forget that it was due, in a distinct measure, to an unsound financial policy." [1]

The Barbarians entered, and Feudalism succeeded to the Barbarians. Through the long

[1] Ernest Lavisse, *Histoire de France*, 1900, Deuxième Partie, Livre Second, Chapitre Second, p. 289.

dark night of six centuries we can faintly discern that the fiscal system of Rome had been so solidly founded that, though broken into fragments, it disappeared not. Like some old mosaic pavement which we now unearth, it retained a recoverable life. As one of the leading statesmen and economists of modern France has written: "The system of Roman taxation survived the invasion of the barbarians. Under feudalism it crumbled but was not destroyed. When royalty, in seeking to find a basis for its power in the unity of the nation, made its great effort to acquire the power of taxation and succeeded in so doing, it was to the fiscal system of Rome that it had resort. Ages passed. Political revolutions and economic revolutions came and went. The fiscal organisation of France adapted itself to them all, but continued none the less to bear the impress of the Roman economy. Even to-day we trace that system in our methods of taxation, just as in our soil we encounter traces of the roads of Cæsar built so solidly that they seem to defy the march of time." [1]

[1] M. Joseph Caillaux, *Les Impôts en France*, 1904, Préface, p. 32.

It was indeed the fact that the unified and homogeneous fiscal system of the Emperors became parcelled out in the dark and feudal ages, private rights usurping the public right of old days. And, for centuries after, the long and weary work of the French monarchy was directed towards wresting, bit by bit, the power of taxation from localities and individuals in order to secure it for the central power of royalty. At length, in the fullness of time, the royal right itself, so long victorious in appearance, but now as much in acknowledged decay as that of the Cæsars had been, was replaced by the national right at the Revolution of 1789.

How was it, we may pause to ask, that the national right in finance did not successfully assert itself till so late an hour as the close of the eighteenth century? Why did fiscal freedom tarry for so long?

One reason was, that the French monarchy, in labouring constantly and successfully to absorb the great mediæval fiefs, steadily acquired a revenue of its own, thus rendering itself relatively independent of any popular assembly or national control. Besides that, as Guizot pointed out, the nation, spurred on by "the really intense and invincible hatred which it has always felt for the feudal system,"[1] gave far too free a hand to the monarchy, as to the sworn enemy of feudalism, in the economic administration.

Further, we must remember that, owing to the mediæval possessions and claims of England in France, there was between the two countries "a chronic state of war from 1066 to 1453, when Bordeaux, the last English possession in the south, was taken, or, if you like, until 1558, when Calais fell to the French."[2] From all this it resulted that the representatives of the French people finally resigned the key of the fiscal fortress into the hands of the French monarchs during the course of the fifteenth century, on the understanding and with the compact that their princes should rid France of the presence of England. "In 1439 the States General agree

[1] M. Guizot, *Histoire de la Civilisation en Europe*, 18th edition, 1881, p. 109.

[2] Prof. Stubbs, *Lectures on Mediæval History*, p. 362.

that the land tax should be levied on the initiative of the king, so that he may be enabled to entertain a standing army. . . . Feudalism is conquered, but the absolute monarchy is thus founded in its stead." [1]

From this time onward, with remarkably brief intervals and in spite of several short-lived attempts at reform, the financial administration can only be described as flagrant. The more enlightened efforts of Louis XI, and of Sully, the minister of Henri IV, were little more than flashes in the pan. From the death of the latter monarch at the opening of the seventeenth century up to the French Revolution there is not to be found a Budget balancing with a surplus, except some few in the time of Colbert, the great minister of Louis XIV. And, though Colbert is regarded as perhaps the most eminent Finance Minister of the old régime, yet a survey of his twenty-four Budgets shows that only eight of them balanced on the right side.

Those monarchs of old France lived on bad financial expedients. Their mediæval plan was

[1] M. Joseph Caillaux, *Les Impôts en France*, Préface, pp. 39–40.

to debase the coinage when they wanted money. Later, in the seventeenth and eighteenth centuries, they pursued the practice of pledging the revenues ahead, so as to obtain lump sums down from the agents to whose tender mercies they consigned the taxpayers. What was most serious of all, they permitted the feudal system to re-assert itself in matters of taxation and to continue to flourish, in the fiscal field at any rate, side by side with themselves.

Taine, in his work on the *Ancien Régime*, argued, with ability but with exaggeration, that, out of every 100 francs of income which a peasant might be earning prior to the French Revolution, direct taxes took 53 francs, tithes and seignioral dues 28 francs, or 81 francs in all.[1] Thus the peasant would be left, on this calculation, with some 19 francs only, out of which, in addition, he would have to defray the salt tax and the wine excise.

It must be said that modern research has reduced these scarcely credible figures. M. Marion, in his work on this subject, has

[1] *Ancien Régime*, p. 412, note 5, English translation.

calculated that direct taxes took 36 francs, and tithes and seignioral dues together 24 francs, or 60 francs out of the 100.[1]

Even if we accept the latter and lesser calculation, this weight of feudalism was heavy enough, but, as the eighteenth century proceeded, it seems that it actually tended to increase. So, at least, those writers, who have recently studied anew that period of French history, appear to have established. As one of their number has well expressed it, there was in process during the latter half of the eighteenth century "a feudal reaction" which took the form of enhanced demands for the payment of feudal dues.[2] This was indeed too much to be borne with equanimity.

Thus, as the Revolutionary age opened, the monarchy of France fell a victim to its long-concealed weakness. Those princes, for all their efforts, had never been competent to overcome feudalism, after all, so that, as De

[1] M. Marion, *Les Impôts directs sous l'ancien Régime, principalement au XVIIIe siècle*, p. 120.

[2] M. Luchitsky, *L'État des Classes Agricoles en France à la Veille de la Révolution*, 1911, pp. 102–4.

Tocqueville once wrote, "feudalism, at the opening of the French Revolution, still remained the greatest of all the civil institutions of France." Translated into financial terms this meant inequitable taxes for the many and indefensible exemptions for the few. Monarchy had thus become the accomplice, instead of the antagonist, of feudalism. It had surrendered to, or had compromised with, that very enemy which it had been chiefly commissioned to combat. That was why the knife of the guillotine fell.

How singular that the whirligig of time had come full circle after fourteen centuries! How disturbing to reflect that, on the slippery slope of the economic Gilboa, the shield of the mighty, of the Capets no less than of the Cæsars, had been vilely cast away!

CHAPTER III

THE EXPENDITURE OF FRANCE, 1789–1914

"Je vois tous les États de l'Europe courir à leur ruine. Monarchies, républiques, toutes ces nations si magnifiquement instituées, tous ces beaux Gouvernements si sagement pondérés, tombés en décrépitude, menacés d'une mort prochaine."—Jean Jacques Rousseau, 1793 edition of *Works*, Vol. II., p. 239.

WHAT was the nature of the financial policy pursued by France from the date of the Revolution of 1789 up to the outbreak of war in 1914? We will examine in this chapter the expenditure side of that policy.

A high tribute must first be paid to the zeal and goodwill of the statesmen of the Constituent Assembly, who, in the first flush of the Revolution, laboured strenuously, and partly on sound lines, to rebuild the broken economic structure of the Commonwealth. But the nature of the times absolutely forbade success, and it was impossible just then to cure the errors accumulated through many centuries. Cursed with so many evil legacies, harassed by wars without and civil chaos within, France went speedily down into bankruptcy.

According to the report of Necker, presented in 1789 to the States-General, the annual expenditure bequeathed to France by the fallen monarchy was 531 million francs, included in which sum was the annual debt charge of 207 million francs. But in 1797 this debt charge was officially pronounced to be "a sum far superior to the means of the Republic," and was drastically and disastrously scaled down by two-thirds.

Thus Napoleon, on his accession to power, was presented, on the one hand, with a great advantage in the shape of a considerably reduced expenditure, but, on the other, was faced with a great problem in the shape of an utterly ruined national credit. He soon proved himself equal to this situation, and his financial policy as regards expenditure can be summarised as follows.

First, Napoleon set his face resolutely against financing the State by means of further borrowing. He himself only made a small issue of rentes in 1813 after the Russian campaign, with the result that, at the close of his reign, the annual debt charge was no higher than 81 million francs.

Next, he realised that it is impossible to found an economical administration upon the quicksand of a debased and fluctuating currency, which he regarded, to quote the words of one of his circulars, as "the greatest scourge of nations." For this purpose among others of securing a sound monetary system as the only solid basis of all public and private transactions, he established the Bank of France in 1800. This was the achievement of which he was most proud, and from the field of Austerlitz he wrote that he was thinking more about the Bank than about the enemy.

Further, the Emperor believed that it was advisable in the interest of economy to avoid the direct participation of the State in trade. He considered, however, that the State should help in securing facilities for the smallest and humblest traders to obtain money at cheap rates and, as far as possible, at rates that did not vary. Thus he wrote to Mollien, his financial right-hand man, in 1810, that he wished that there should be inscribed over the doors of the Bank of France these words in golden letters: "What is the end and object of the Bank of France? It is to discount all the Bills of all the business houses in France at the rate of 4 per cent." That policy was sedulously followed, and one hundred years after his time the average rate of discount of the Bank of France during the fifteen years 1900–1914 was only 3.07 per cent., while there were only fourteen alterations of the rate during that period, in contrast with the seventy-five changes made during that period by the Bank of England.

His poverty-stricken years in Corsica and his military life at Auxonne had instilled into him very strict ideas of expenditure and accountancy. Hence his organisation of a regular system of tax collection, as opposed to the costly methods in vogue hitherto, and the preparation of the cadastre, or register and survey of the land of France. Hence, too, his plan for controlling the State expenditure by means of a Court known as the Cour des Comptes, the function of which was, and still is, to pass judgment on the returns of the Accounting Officers of the Budget.

Besides, this, he displayed an intense personal interest in economising in his administration. "Where did you buy that? How much did it cost?" And when he got his answer Napoleon used very often to say, "That was much cheaper when I was a Sub-Lieutenant: I won't give more for anything than anybody else."[1] Or again, he would write to General Duroc his Grand-Maréchal du Palais, "Nothing must be spent except with the direct approval of His Majesty!"[2]

Nor did Napoleon omit, in the interests of France and posterity, to found a school of trained financiers, imbued with his governing ideas and comprising such notable names as those of Mollien, Gaudin, Baron Louis, the Comte Corvetto, and de Villéle. Some of these statesmen and financiers carried forward the

[1] Mlle. Avrillon, *Memoirs*, Vol. I., p. 136.

[2] *Correspondence of Napoleon I.*, Vol. XXII., p. 419; Letter to General Duroc, August 19, 1811.

principles which they had learnt under him into the later times of the Restoration. And their tradition lasted long. Thus Baron Louis informed and inspired Thiers, who in turn handed on the torch to Léon Say.

Unfortunately, Napoleon pursued another principle of financial policy, which, however specious and attractive in appearance, well-nigh cancelled by its fateful consequences the good of all the rest. This principle was that war should be made to pay for war. The receipts thus obtained, termed *recettes extérieures*, were levied on the vassal States or on conquered enemies. But this proved a fatal lure to ever new adventures, and the last wages of his warfare were ruin, not revenue. In plain terms, the Spanish campaign began the evil process, the Russian disasters enhanced the financial troubles of the State, until with Leipzig bankruptcy began to show its face. A few weeks after that disaster Mollien could write to his master that, " It is impossible for this state of things to continue without a renewal of those disorders which cannot conceivably be allowed under the reign of Your Majesty, since it is

Your Majesty himself who remedied them once for all."

Nevertheless, it must be said that the financial system of the First Empire had been so solidly founded as to enable a very speedy recovery to be made, a recovery mainly engineered by the skill and devotion of Baron Louis and the Genoese Corvetto. After all, the task was not an impossible one. As already mentioned, the total State expenditure in 1789 had been 531 million francs. In 1815 the corresponding figure was only 931 million francs, which reflected a really modest addition to the State expenditure after nearly a quarter of a century of wars. So speedy, at any rate, was the financial recovery of France that by 1818 her public credit may be considered to have been re-established.

What was the expenditure policy pursued by France from that date onwards up to the outbreak of war in 1914?

During the course of the hundred years in question a series of powerful and well-nigh resistless forces, so resistless that they seemed to assume the strength of natural forces, operated to swell the outlays of all modern States.

One main cause of enhanced Budgets was, of course, the vast extension of State services, arising out of the new conceptions entertained of the duties of the State towards its citizens. France felt that influence as much as any other people. To take a notable example, the sum spent in the Budget on public education was quite insignificant in the Napoleonic age and only amounted to 2½ million francs in 1830. It stood at 328 million francs in 1913.

Another general cause of the growth of expenditure during that age was the increasing weight of militarism, whether incurred in past wars and represented in that case by a burdensome debt charge, or assumed by way of precaution against wars in prospect and thus represented by the direct naval and military estimates annually voted by Parliament.

Such, apart from any change in monetary values, were the main forces making in that age for increased State expenditure. How did France manage her public expenditure in view of them?

The French Budget, which was 531 millions in 1789, attained to 1 milliard in 1828, to 2 milliards in 1860, to 3 milliards in 1877, and to about 3½ milliards at the close of the century, deducting *centimes locaux*, i.e. the share of the local authorities in the Budget receipts. Hence the Budget at the close of the nineteenth century was about six times the Budget of 1789, as measured in terms of money.

Yet Léon Say, speaking in 1876, and looking backwards to the days when the Budget was only 1 milliard, argued with high authority that, during that period at any rate, the real weight of the Budget had not increased. His argument was founded on an analysis of property passing by death, from which he inferred that the real wealth of France had kept pace with the increased expenditure.[1]

At the close of the century Paul Leroy Beaulieu re-examined the matter more comprehensively from 1789 up to date. Though working by a different method he reached the same conclusion as the one arrived at for the shorter period by Léon Say. He argued that

[1] Speech in the Chamber of Deputies, December 8, 1876.

between 1789 and the date of writing the precious metals had lost half their purchasing power in France, and also that the productivity of France measured in goods and services had increased threefold. "Thus, valued in money, the production of France in 1898 is about six times as great as in 1789. Hence a Budget six times as great to-day as it was at the moment of the Revolution would not require a larger part of the revenue of our citizens than did the Budget presented by Necker."[1]

These considerations may enable us to draw the conclusion that, taking a long historic view, up to the close of the nineteenth century the national expenditure of France, though it had shown in recent years disturbing signs of expansion and irregularity, had not outrun the capacities of the French taxpayers.

Nevertheless—whether because of some inborn fallibility of financiers, or because the course of Budgets, like that of true love, never did run smooth—it unfortunately is the case that, in spite of the above general conclusion, notable signs of irregularity and disorder began

[1] *Science des Finances*, Vol. II., pp. 195–6, 6th Edition.

to manifest themselves in the financial policy of France, as the nineteenth century drew onwards. This disagreeable and unhappy truth can best be established if we notice the growth of that congenital disease of Budgets known as supplementary estimates.

In this connection, it would appear, according to a report of the Upper House in 1833, that during the period 1815–1830 the average supplementary estimates voted by Parliament were only 40 million francs. But with the growth of Parliamentary appetites a similar report, published in 1878, shows that from 1840 to 1870 that figure of supplementary estimates had grown to 250 millions on the average and that France had scarcely more than one or two Budgets that balanced on the right side. After the war of 1870–1871 a better state of things was established for a few years, and then the old evil resumed its course, not indeed on a scale such as would alarm us nowadays, but still in a manner more disturbing than before. Unfortunately, too, this tendency in expenditure continued unabated or even enhanced up to the opening of the Great War itself in 1914. The date of this new epoch can perhaps be fixed at the year 1883, so that the period of serious disorder in question extended over some thirty years.

The great disasters of 1870–1871 had been swiftly followed by years of economic recovery. The average price of the 3 per cent. rentes in 1869 had been 71; it had fallen to 54 in 1871, but had recovered to 75 as early as 1878. There had been an abounding and elastic revenue resulting in excellent surpluses. And then suddenly we read in 1883 of the financial disorder of France: "With the largest debt in the world growing rapidly, an unmanageable floating debt, a constantly increasing expenditure, and, on the whole, a slackening yield of taxes and recurring deficits of indefinitely large amounts."[1]

Following on this changing aspect of affairs, we can trace, through the writings of the economists of those days up to the close of the period now in question, a chorus of disapproving and alarmist notes.

Thus writing in 1898, Paul Leroy Beaulieu

[1] *Annual Register*, 1883, p. 231.

himself could declare: "At no epoch have we witnessed a greater prodigality. We seem to wish to endow our democratic finances with all the vices of the ancient régime . . . our Budgets are entangled one with another so much as to have lost all clearness and all exactitude with the voting of enormous supplementary credits. The indefinite delays in the clearing up of the accounts take away all precision from the public finances. The confusion between ordinary and extraordinary expenditure, between taxes and loans, which seem to serve alike for meeting expenditure, obscures everything all round. No one has any clear responsibility for the Budget, since all the world is busy adding on to it and upsetting it. In a word, after the altogether correct Budgets of the Restoration and the less correct but fairly orderly ones of the reign of Louis Philippe and the Second Empire, it seems that we are working to restore the inextricable and incomprehensible finance of the ancient régime."[1]

Accordingly, it is evident that, as the

[1] *Science des Finances*, edition of 1898, Vol. II., p. 201.

twentieth century opened, a critical hour had arrived in French finance. Nothing disastrous or irreparable had been done, so far. Expenditure had certainly not been on a ruinous scale. Still, grave signs of fiscal deterioration or disease had begun to make themselves manifest. Clearly, a more rigorous, exacting and peremptory control of expenditure, a more strict accountancy, a more abstemious policy at home, a less adventurous policy abroad, needed all to be instituted. Unfortunately, things happened otherwise.

The deciding factor which, as the twentieth century opened and proceeded, began to direct the expenditure of France into deeper channels arose from the pursuit of a great national policy in Europe and overseas alike.

Between 1871 and 1914 France was increasingly animated by a central and consuming purpose, as embodied in the successive but accordant policies of Gambetta, Jules Ferry, Rouvier, Waldeck-Rousseau and Poincaré. This policy had a twofold embodiment, but only in the sense that, partly by Colonial expansion and partly by a system of European alliances or friendships, one great purpose was aimed at, the resurrection of France as an international Power.

As regards French policy outside Europe, "These statesmen had recourse to the policy of ancient Rome. Rome, being weak in Roman citizens and rich in the number of her subjects, sought to make good her deficiency in Latin soldiers by enlisting the legionaries of Gaul, of Spain, or of Numidia in her service. Colonial expansion became the complement, or rather the buttress, of their general policy. That policy was calculated to confer on France the material power, the necessary weight, for the assertion of her rights in Europe."[1]

What reaction on the French Budget was exercised by this Colonial expansion? It was a powerful influence, and it has been sketched in vivid terms by the historian of modern France in his standard work. "The acquisition of enormous territories under diverse headings—protectorates, annexations, spheres of influence—procured for France a vast Colonial empire, peopled with natives either barbarous or else

[1] M. Joseph Caillaux, *Agadir*, pp. 6, 7.

hostile to the civilisation of France and refractory to assimilation. . . . Operations began with Tunisia, and, starting with this first step, the Ferry Ministry employed the procedure which was to characterise the Colonial enterprises of the Republic. This was to demand insufficient credits and to conceal the full meaning of the expedition in question in order to avoid alarming public opinion; to send troops "in little lots"; to engage in military operations before informing the Chambers of Parliament and to incur expenditure before having obtained credits; to involve "the honour of the flag" and "the prestige of France" up to a point at which the country could only feel itself bound to push the adventure to the issue of conquest."[1]

This policy outside Europe finally crystallised into the resolution to obtain the Protectorate over Morocco.

The Moroccan enterprise was considered as the last hope of that Colonial Empire which France had so steadily pursued for centuries.

[1] Ernest Lavisse, *Histoire de France Contemporaine*, Vol. VIII., p. 388.

Time after time in India, in Canada, in Australia, in the area now occupied by the United States, in Tripoli and in Egypt, those hopes had played her false. Here, it seemed, was the final opportunity of making good those long, traditional, and generally unfulfilled aims.

In Europe the corresponding policy culminated in the establishment of the alliance with Russia and the Entente with ourselves.

France felt that the German peril forced her to all this. It involved her in an expenditure on a rapidly ascending scale.

There was first and foremost a race for naval armaments. Suffice it to say that, during the first decade of the twentieth century, this race for naval armaments was so severe that if we take the total naval expenditure of the eight great Powers, it had swollen in that short period by no less than 56 per cent. The increase of France in that period was 37 per cent.[1]

Quickly following upon this pursuit of naval

[1] "The Growth of Expenditure on Armaments," *Quarterly Review*, 1912, p. 224.

expansion had come a similar expansion on land.

The Army policy of Germany from 1870 to 1911 had been one of quinquennial revision and re-organisation: "To this quinquennial system the German army had owed much of the homogeneity and steadiness which marked its progress in strength and efficiency."[1] The latest response of France to this growing organisation had been that, in March 1905, she established a uniform period of two years' military service for all persons without distinction, thus abolishing the very large exemptions which had been the rule since the law of 1889. The result of this was that, though Germany had in 1910 a larger army than France, France had reduced that superiority by means of the great effort in man-power which she had felt herself forced to make since 1905.

This was the situation when, in April 1911, France decided to send an expeditionary force to Morocco with a view to establishing a Protectorate in that country. As our *Annual*

[1] "The French and German Army Bills," *Edinburgh Review*, July 1913, p. 224.

Register recorded at that date, "the whole nation understood the importance of the part it had to play in North Africa, and accepted responsibility for the new attitude about to be assumed in Morocco."[1]

The answer of Germany to this proceeding was the despatch of the *Panther* gunboat to Agadir in July 1911, a date which may be taken as marking the initiation of that crisis which was consummated in July 1914. Germany, in abrupt departure from her quinquennial system, now brought forward a measure for much increasing and improving her army, and this measure became law in June 1912. This statute was quickly followed by another yet more formidable proposal which in its turn was embodied in the German Army Act of 1913.

All this naturally enough created a profound sensation in France. Accordingly, in March 1913, a solemn meeting was held in Paris of the Supreme War Council, at which it was decided that a Three Years' Service Act must be at once passed. Inquiries showed that the

[1] *Annual Register*, 1911, p. 301.

artillery was gravely defective, that the fortifications which should protect the frontier in case of an invasion were in a parlous state, and that large additional barracks were needed for the increased number of recruits who would require accommodation. Thus suddenly in the early months of 1913 all financial prospects were darkened to the gloom of night by the knowledge that immense new outlays must be provided on all manner of military material at home, in addition to the constant and heavy drain on the finances entailed by the Moroccan enterprise, which was still causing large sums to be spent by the French Treasury.[1]

This was the reason why, as the twentieth century opened and proceeded upon its way, that stern chorus of denunciation and invective upon the part of the experts, which had first arisen in the closing years of the preceding century, swelled in volume and emphasis against the expenditure system of France. The author of the standard work entitled *The Budget* wrote, for instance, in 1906: "The idea of economy constitutes the very foundation of

[1] cf. *The Economist* of July 5, 1913, and December 6, 1913.

the French mentality, but it has very little success in the bosom of the State Budget. For while private citizens accumulate savings with a fervid zeal, the representatives of these same private persons yield to the impulse of prodigality with a fervour which is scarcely less." [1]

And again a little later at the end of 1908: "Our Budgets, in spite of the strict network of formalities by which they are nominally hedged in, are swollen by irregular undertakings, by over-spent credits, by unconcealed waste and other abuses to which all the world is party." [2]

These severe strictures, if they are tested by the facts, contain a considerable element of truth, even if we view the matter from the purely technical point of view. For instance, in France the constitutional theory is that the Budget of the coming year opening on the 1st January has to be voted at latest by the day before, the 31st December. But if we recall the dates on which the Budgets were actually

[1] René Stourm, *Le Budget*, preface to the 5th edition, January 1906.

[2] *Ibid.*, 6th edition, November 1908.

voted by Parliament during the twenty years, 1895–1914, preceding the war, we shall find that sixteen of them were only voted after a delay upon the appointed time varying from two to seven months. Thus the Budget of 1913 was only passed in that August, or seven months in arrear, and the Budget of 1914 only on the 15th July of that year, or over six months in arrear.

Another technical indication of a deteriorating finance was the sinister appearance of *comptes provisionnels* and *comptes spéciaux*. The purpose and meaning of these parasitical accounts, the very curse of Budgets, was the concealment of expenditure. Having expenditure which you could not meet, you entered it in a special account and you borrowed money to defray it. Thus you withdrew that outlay from your visible Budget expenditure and you met it by increasing the floating debt. In 1914 we unearth from their concealment no less than four of these special accounts—the account for perfecting war material and the installation of military services; the account of national defence and the Morocco expedition;

the account of non-renewable expenses relative to the national defence; the account of expenses relating to the improvement in naval equipment.

This was really a series of "extraordinary" military Budgets, all fed by borrowing. These outlays could be traced only by looking at the figures of the floating debt. At the opening of 1914 the floating debt was reckoned to have reached 2,081 million francs. France was borrowing by irregular methods in order to meet her current military expenditure in time of peace.[1]

The root cause, as we have seen, of this profound economic disturbance was the rapidity of the race for armaments. If we take the military outlay of France, including the expenditure on the army, the navy, colonies, and the pensions list of the combatant forces, as it appeared in the Budget of 1913, this entailed a burden of 2,110 million francs. This was no less than 41 per cent., and over, of the Budget of 5,067 million francs. In

[1] cf. M. Germain Martin, *Les Finances Publiques de la France*, 1925, p. 47.

1873 the corresponding charges had consumed only a trifle over 25 per cent. of the French Budget.

The remarkable fact was that the "Armed Peace" which had reigned in Europe since 1873 weighed on the finances of France during the next forty years more heavily than on those of any other people. The Bankers' Trust of New York and Paris has made a most careful investigation on that point and has published most valuable figures. Its experts have calculated the total cost of the Armed Peace from 1873 to 1913 for the six great nations of the Continent, including the United Kingdom. In the calculation in question the specific cost of wars waged in that period are excluded, and only the annual and normal Army and Navy expenses are reckoned in. In absolute figures France heads the list, with Germany, Russia, Austria and Italy behind. France's figure converted into sterling is £1,713 millions, while that of Italy, the lowest, is £602 millions.[1]

How heavily, we may ask ourselves, did the

[1] Bankers' Trust of New York and Paris, *French Public Finance*, 1922, p. 2.

Budget of 1913 weigh upon the taxpayers of France?

In order to ascertain this we must not take the whole of the 5,067 million francs included in the Budget of that year, as in that case we should be including the non-tax receipts. The tax receipts were in that year 4,135 million francs, as furnished by the French Government. Thus, as the population was 39,600,000 at that date, the taxation burden in that year would be 104 francs per head, and this is, indeed, the figure as calculated officially by the French Ministry of Finance.[1]

The correctness of this calculation is, however, not accepted either by the League of Nations or by the British Treasury. Thus the Chancellor of the Exchequer stated in April 1925, in the House of Commons, that the taxation per head of France was only 84.5 francs in 1913.[2] In this he was in agreement with the League of Nations' estimate.

What was the reason of the difference in these

[1] *Inventaire de la Situation Financière de la France*, official document No. 441 of 1924, p. 106.

[2] See *Times* report, April 4, 1925.

two calculations? If we analyse the figures we can account for it, I think, as follows. The French Government runs certain monopolies or, in other words, certain industrial enterprises. In arriving at their figure they reckon into the taxation figures the gross receipts of their enterprises. The British Government, on the other hand, only reckons in the net receipts of these enterprises, and thus arrives naturally at the lower figure.

It may be considered somewhat presumptuous to call in question a calculation adopted by the French Government in regard to a technical matter of primarily domestic concern. Nevertheless, it may be considered that from the strict accounting point of view the method endorsed by the British Government would be more in accordance with the usage generally accepted.

If, then, we accept the latter calculation, the real burden on the French taxpayer was 84.5 francs in 1913, or, say, £3 7*s.* per head. For the United Kingdom at that date the corresponding figure, as officially furnished, was £3 11*s.*, omitting the pence in each case.

In order, however, to institute a fair comparison between the two countries we must bear in mind that the United Kingdom had national income at that date of £2,250 millions, or £50 per head.[1]

As regards France, the most generally accepted estimate of her national income at that date has been furnished by M. René Pupin. His estimate is a national income for France in 1913 of 37,500 million francs, or £1,500 millions, equal to £38 per head of the population.[2]

It is true that this figure has been criticised by Sir Josiah Stamp and has been rated by him only in Grade II for probability. Since then, however, the French Ministry of Finance has published its own calculation in the following terms: "Serious studies supervised and rectified by the French financial staff on the Reparations Commission have fixed, for 1913, the total of the annual revenue of private

[1] The estimate of Sir Josiah Stamp, confirmed by Professor A. L. Bowley, *Journal of the Royal Statistical Society*, July 1919, p. 491.

[2] cf. *Richesse Privée et Finances Françaises de l'Avant-Guerre à l'Après-Guerre.*

persons in France at about 35,870 million francs."[1] This would be equivalent in 1913 to £1,435 millions sterling, thus approximating to the view of M. Pupin, and would mean a national income of £36 per head.

Hence in 1913 the French taxpayer would be paying a higher ratio, about 9 per cent. of his income, than the British taxpayer, 7 per cent.

Remember, however, that this is based on an uncertain factor, the actual figure of the national income.

How did France defray, during the same period from 1789 to 1914, the weight of expenditure thus described in this chapter? Her financial policy in respect of the levy of taxation naturally falls to be considered next.

[1] *Inventaire*, 1924, pp. 107–8.

CHAPTER IV

THE SYSTEM OF DIRECT TAXATION, 1789–1914

"Tous les citoyens ont le droit de constater par eux-mêmes ou par leurs représentants la nécessité de la contribution publique, de la consentir librement, d'en suivre l'emploi et d'en déterminer la quotité, l'assiette, le recouvrement et la durée."—*La Déclaration des Droits de l'Homme*, Article 14, August 4, 1789.

WHAT, then, was the policy pursued by France from 1789 up to 1914 in regard to raising the revenues of the State? This policy is of remarkable interest and significance, especially in view of the events which were to arise at the latter date. After eliminating innumerable details, it ran as follows.

The governing and central idea of the legislators of the early days of the Revolution was that the land was the sole source of wealth, and that, in taxing it accordingly, fiscal justice would be achieved as well as social justice, since the land had fallen into fewer hands than was desirable. Hence the financial authorities of the Constituent Assembly, while seeking to limit taxation to 300 million francs, hoped to raise 240 millions of that sum by the agency of the land tax.

The subsequent history of French taxation is a movement on the whole away from that assumption and that policy. That is to say, indirect taxation ousted direct taxation from its initial predominance. Thus it was the policy of Napoleon to move quietly and steadily towards indirect taxation. If we examine his Budget of 1813, the last year when his finance was fairly normal, it appears from the figures that by that date he had reduced the proportion of direct taxation to one-third only of the total taxation receipts.

In the view of the statesman and historian of French taxation, M. Caillaux, writing in 1903, this historic tendency was of a purely reactionary nature. "The predominance of direct taxation desired by the Constituent Assembly was superseded by the predominance of indirect taxation. . . . This reaction, which quickly followed on the Constituent Assembly, began with Thermidor, developed strength under the

Directory, and proceeded under the Consulate, the Empire, and the Restoration."[1]

The opposite view of this question may be illustrated by a sentence or two taken from the work recently published by the distinguished writer, M. Marion, on the financial history of France from 1715 to 1818. In criticising "that systematic hostility which in 1790 and 1791 had nearly destroyed the indirect taxes of France," he observes that "we must do justice to that powerful movement of opinion which, in reaction against the delusions of the Physiocrats, so fashionable at the opening of the Revolution, entailed a return to the indirect taxation so unjustly repudiated on the occasion of the elaboration of the new fiscal system in 1790–1791."[2]

The real fact was that, at this critical point in her history, France could not bring herself to adopt a sound system of direct taxation. In default of this, she fell back inevitably upon other taxation. But that she did so is no matter for special eulogy.

[1] M. Joseph Caillaux, *Les Impôts en France*, Vol. I., Preface, pp. lxxviii. and lxxx.; November 1903.

[2] M. Marion, *Histoire Financière de la France depuis* 1715, Vol. IV., p. vi. of Introduction and p. 19.

The direct system of taxation as instituted at the Revolution had as its sheet anchor the land tax, *l'impôt foncier*. But throughout the period under review it was never levied fairly and accurately, and this on three accounts.

It was essential that any such tax should be based on a correct valuation. But this was never done. Napoleon, indeed, ordered a survey, "cadastre," in 1807, but this was only finished in 1850, with the result that during the nineteenth century the assessments for the land tax, whether applied to "property built on" or to "property not built on," were hopelessly at sea. It is true that under the Acts of 1890 and 1914 remedial steps were taken to assess it properly.

Next, in default of an exact assessment, this tax was left to be what is technically known as an *impôt de répartition*, i.e. a tax of which the total yield is first fixed by the Government and then is collected in rather random fashion by the local authorities. The right thing would have been, no doubt, to have organised it as an *impôt de quotité*, i.e. a tax fixed as a settled percentage on the net revenue of land and houses.

Lastly, the tax was improperly levied because it did not distinguish the *bénéfice agricole*, or the profits made out of farming, from the *revenu foncier*, or the annual value of the land as such. The tax as instituted at the Revolution did not touch the *bénéfice agricole*. It is of interest to note that when in 1907 M. Caillaux first brought forward his memorable scheme for the reform of French taxation, he based it on a division of incomes into seven categories, of which three were in respect of the existing *impôt foncier*, i.e. revenue from land built on, from land not built on, and from farming profits derived from *exploitation agricole*. But that essential principle did not prevail until the war years.

The statesmen of the Revolutionary age, however willing in theory to limit direct taxation to the land tax, could not close their eyes to the obvious fact that there were other sources of revenue derivable from direct taxation. In fact they established altogether four direct taxes, so famous in French economic history under the name of the *quatre vieilles*, i.e. the *quatre vieilles contributions*. These were, besides the land tax, the *impôt personnel-mobilier*, or personal property tax, the *impôt des portes et fenêtres*, or tax on doors and windows, and the *impôt des patentes*, or tax on licences. All these taxes lasted up till 1917; at that date the last three were repealed, so far as the State was concerned, and only remained for the local authorities, while the *impôt foncier* was already being transformed and adapted to the needs of the times.

Unfortunately, these three taxes, the supplements to the land tax, were based upon an incorrect principle of levy. What was this principle, and why was it adopted and adhered to with such strange tenacity by the enlightened statesmen of France?

The Revolutionary financiers, in resorting to direct taxation, were at once confronted with a serious difficulty. Direct taxation implies an accurate assessment of wealth, and this, in its turn, involves either investigation into private affairs by the State, or else a formal declaration and confession of wealth by the taxpayer. But the French public, which had just escaped from the fiscal injustices of the ancient régime, felt itself to be opposed to both procedures alike. The phantom Governments rushing in headlong sequence across the scene were not disposed to add one more to their innumerable troubles and accepted the fact of this antagonism.

They resorted, in fact, to an ingenious but unsound compromise which with slight modifications endured up to 1917. This compromise was that they dispensed the taxpayer both from any individual assessment by the State and also from the obligation of a personal declaration and affidavit. The ingenious plan resorted to was, in technical language, to rely on *signes extérieurs*, or outward and visible and tangible marks of wealth as a basis for assessment. For instance, there was the house which a man inhabited with its presumed rental value, with its doors and windows indicating the scale of his income; or, again, there was the professional category in which a man worked, furnishing, to some extent, the clue to his means. This compromise stood up till the War period as the governing factor in the policy of France regarding direct taxation.

M. Caillaux, writing in 1903 on these taxes and their unimportant accessory taxes, *taxes assimilées*, dismissed them with the sentence that they were then " quite out of date, ossified in their original form, and wholly out of contact with the living realities of the taxable wealth of France."[1] In verification of that verdict, a few words must be said in explanation of each of these taxes.

The personal property tax dated like the land tax from the Revolution and the year 1791. It was in theory composed of two taxes, a capitation tax calculated on the basis of three days' work and the tax on rent of the house. " The great vice of this tax," wrote the leading economist of France at the close of the nineteenth century, " is that it is a tax of repartition . . . the partitioning of it is wholly unequal as between the Departments, and in fact is quite as unjust as that of the land tax." This tax had originally been meant to be a tax on personal property balancing that on

[1] *Les Impôts en France*, Vol. I., Preface, p. xcvii.

real property, but during the course of the nineteenth century "it completely lost its primitive purpose of a tax on personal revenue,"[1] to become a fixed tax unadjusted to the conditions of the days into which it survived.

The next of the taxes in question was that on doors and windows. Enough of it to say that, "to sum up its character, the tax on doors and windows is one which it is impossible to assess equitably."[2]

The last of the "four old ones" was the tax on licences, *l'impôt des patentes*. This was initiated by the law of 1791, and perhaps no other tax underwent more frequent manipulations by the Legislature. The amending law of 1880 thus defines it: "Every individual, French or foreigner, who exercises in France a business, a trade, or a profession not comprised within the exceptions determined by the law, is subject to the tax on licences." The principle of levy for this tax was to exact a *droit fixe* and a *droit proportionnel*, the idea

[1] Paul Leroy Beaulieu, *Science des Finances*, Vol. I., pp. 439, 444.

[2] *Ibid.*, p. 426.

being to range all the occupations into distinct classes, at the same time to regulate the amount of the tax by the profits presumably realised by members of that particular occupation. It will be thus observed that it adhered to the principle of taxation by "exterior signs," since it avoided inquiries into exact profits and confined itself to the injustice of presumption.

Such, from 1791 up to 1914, was the financial policy of France in regard to direct taxation. Apart from some trifling "assimilated" taxes, it consisted of the four taxes mentioned above. In 1913, the last clear year before the war, these taxes yielded the very modest sum of 634 million francs, or about £25,000,000. Apart from any question of the total yield, this system was chaotic, unjust and antiquated. The hour had struck when it must be swept away.

Indeed, the French Ministry of Finance admitted as much in 1924 when it published its famous Inventory of the financial situation of France. In the course of that document the Ministry wrote, with a backward look at the system of pre-war finance: "Our four ancient direct taxes were based on certain outward signs of wealth. But the value of these latter, as presumption of ability to pay, was constantly decreasing, and it became daily more obvious that these taxes could not be adapted to the constant and rapid fluctuations of wealth. They could not be levied in any proportion, however distant, to the incomes of individual taxpayers."[1]

Before we leave the direct taxes proper, it should be stated that there was also a tax on securities, *valeurs mobilières*. This was a timid little direct impost, a Cinderella beside the four big elderly ones, which had dared to be born into the world in 1872. It had, however, been so pitted and ravaged with exemptions that its yield was only 138 million francs in 1913, though, to be sure, it was destined to grow to nine times that volume ten years later.

Thus the taxes on revenue proper totalled 772 million francs in 1913. This was about

[1] *Inventaire de la Situation Financière de la France*, Document No. 441 of 1924, p. 114.

19 per cent. of the total tax revenue of the State that year.

Before leaving this question of the direct taxation policy of France it would be highly unfair and misleading not to mention that there was another important class of taxes, raised throughout the period in question, which, though generally reckoned as "indirect," were quite arguably to be counted as "direct" taxes. These imposts are known as those of Registration and Stamps. It may be said of them that they were incidental to the exchange of wealth, as those hitherto mentioned were incidental to the receipt of wealth.

Léon Say, writing in 1896 and striving to define the difference between direct and indirect taxation, remarked that, "Scientifically, one calls that tax 'direct' which is specifically charged to the individual who is paying it, and that tax 'indirect' which the individual who is paying it is able to pass on to the purchaser by increasing the price payable by the latter. But in reality the same taxes are sometimes direct and sometimes indirect." [1]

[1] *Les Finances*, 1896, p. 17.

It may be added that the Ministry of Finance has never been very decided in this matter, to judge from the fact that the collection of these taxes was assigned neither to the Administration des Contributions Directes nor to the Direction Générale des Contributions Indirectes, but to the special Administration de l'Enregistrement, the task of which was to deal with " the mutations and movements of wealth."

Recently, however, it may be pointed out that, in the Inventory of 1924, the Ministry, revising its own old classification, places these taxes under the heading of imposts on capital, and elsewhere calls them *taxes sur la fortune*.

These considerations may be said to put another light upon the financial policy of France in regard to direct taxation discussed in this chapter. They appear to redress to a considerable degree the immense disparity between " direct " and " indirect " taxation. For if, as pointed out above, direct taxes on revenue amounted to 19 per cent. in 1913, and these taxes on wealth amounted to another 26 per cent. and over, then the total of what may be arguably regarded as "direct" taxation amounted to about 46 per cent. of the total tax revenue.

The taxes on Registration are of greater antiquity than their companion Stamp Duties. The former divide themselves into two main categories, falling first on property, whether real or personal, at the moment of its transmission, and secondly on certain acts incidental to judicial decisions or civil life. These duties, so far as the exchange of property is concerned, may be almost said to have been coincident with civilisation itself, for they were in full vigour in Rome, were perpetuated under the Roman Empire, and took their place among the regulations of feudalism. The monarchy greatly increased the injustice and complexity of these feudal dues. In 1790 they were swept away in the first ardours of the Revolution, but only to be re-established immediately.

It would be far too long and is really unnecessary to trace the complex evolution of these taxes during the course of the nineteenth century. Suffice it that they may be divided in the opening years of the twentieth century into three main categories : (*a*) *droits proportionnels*, which were levied mainly on property changing hands at death and also on transfers between living parties, etc. The next subdivision (*b*) was termed *droits fixes* and *fixes gradués*, e.g. fees paid to the State on the occasion of the marriage contract, etc. Lastly (*c*) a tax on the registration of mortgages, etc.

The other great branch of these duties was that of stamps. These duties were of much more recent date than the registration taxes and were instituted by Louis XIV in his Edict of 1655. But it was only in 1791 that there was initiated the modern system of stamped documents. From that time forward this system steadily increased in range and yield, and especially during the latter half of the nineteenth century. This was owing to several reasons : there was an increase in the rates of duty, more especially after the war of 1870 ; the obligation of using stamps was steadily extended ; and, especially after 1860, there was a considerable growth of national wealth involving a corresponding expansion in transactions. At the close of the nineteenth century an inquiry showed that each of these three causes had played an equal part in the growth of the yield.

Altogether, then, in 1913 the Registration duties (834 millions) and the Stamp duties (241 millions), together with a small tax (10 millions) on Stock Exchange operations, yielded in sum 1,085 million francs, or 26 per cent., and a little over, of the entire revenue derived by the State in that year from taxation.

Having thus dealt with the policy pursued by France from 1789 up to 1914 in regard to taxation on revenue and taxation on wealth, the next chapter must be devoted to the other great branch of revenue, the indirect taxes proper, or taxes on consumption.

CHAPTER V

THE SYSTEM OF INDIRECT TAXATION, 1789-1914

"Les Chambres pensèrent et sentirent comme le ministre qui les honorait en se confiant dans leur vertu. Le grand parti qui marchait sous la conduite de Sir Robert Peel, propriétaires, capitalistes, négociants, manufacturiers, aristocrates et riches de toute sorte, accepta le fardeau de l'income-tax qu'il leur imposait, et l'ordre fut rétabli dans les finances de l'État."—Guizot, *Life of Sir Robert Peel*, 1856, p. 91.

Our survey of the taxation policy pursued by France from 1789 to 1914 has so far only embraced that portion, 46 per cent., of the whole taxation which was levied on "revenue" and "fortune."

The remaining 54 per cent., if we take the figures as they finally stood in 1913, was levied on articles of consumption. This portion of the revenue was raised in several different ways and on different principles. These varieties of taxation may be most briefly and simply recounted as (*a*) taxes on drinks, *impôts sur* *les boissons* ; (*b*) taxes raised by means of State monopolies, *monopoles fiscaux* ; (*c*) taxes raised by Customs duties, Douanes; and (*d*) taxes raised internally on divers other articles of consumption or use. Each of these methods requires some explanation and account.

Under the old régime the taxes on drinks, then existing under the name of *les droits d'aides*, had been multiplied to excess and had become hopelessly illogical and intertangled. Early in 1791 the Constituent Assembly, in its primitive revolutionary ardour, swept them away.

And yet, as was so often the case in other branches of legislation, this work of abolition had no sooner been accomplished than a long and elaborate series of statutes began to revive these imposts and recalled them to a very active life. For instance, by the year 1817 a whole code re-establishing the wine duties had come into being. Beer, again, had its legislation regulated by the statutes of 1808 and 1816, statutes which were only remodelled as late as 1899. The other great category of the taxes on drinks, i.e. the taxes upon alcohol, was definitely organised and assessed by the statute of 1824, the principle of which is still in force in the twentieth century.

These taxes by the opening of the twentieth century were divided into taxes on *vins naturels*, taxes on alcohol, taxes on "artificial wines" such as vermouth, and taxes on beer. But in that long period of time since their re-institution under Napoleon and the Restoration they had not been altered in any very vital degree.

And yet, under the surface, a powerful movement of opinion had begun to ferment and had already exercised its influence upon the statute book. Faced by the increase in the consumption of alcohol, reformers, as the nineteenth century proceeded, began to demand that spirits should be more severely taxed than wines, and in this campaign they naturally enlisted the support of one of the most powerful factors in France, the interest of the numberless cultivators of the vine, who leaned readily towards a distinction in favour of the so-called hygienic drinks, *boissons hygiéniques*, i.e. wine, cider, and beer. A long list of statutes dating from 1855 bore the mark of this agitation, so that, while the rate of tax on wine, etc. fell, that on alcohol rose steadily.[1]

It is remarkable to note that out of this tendency there arose a further movement of evolution. The weightier taxation of alcohol necessitated a more vigilant system for guarding against fraudulent and illicit distillation. Hence, from being purely a tax on consumption, it tended to become a tax on production in the nature of excise. The laws of 1899, and more especially of 1900, hastened this evolution of events, and the taxation of beer was reorganised on similar lines in accordance with its alcoholic content.

As regards wine this system was found to be impossible at that date, though the existing three complicated taxes on "circulation," on retail sale, and on entry into the bigger towns, which fell upon wine in a very inequitable manner, were replaced by a uniform tax imposed on its volume as distinguished from its alcoholic content.

Next to the taxes on drinks came the Government monopolies on tobacco, on

[1] cf. M. Caillaux, *Les Impôts en France*, Vol. I., p. 12.

matches, and on gunpowder. The State manufactured these articles and taxed the public on them by means of the price which it charged on their sale. It had undertaken the manufacture and sale of tobacco since 1810 and of matches since 1890, together with that of gunpowder since 1775.

By far the most important and the most lucrative of these monopolies was that of tobacco. The French economists, despite many severe criticisms as to the methods of purchasing the raw material and the costs of production, have on the whole approved this method of taxation. "The finance of the country would have to be singularly prosperous to induce it to renounce a tax so harmless, so moral, so productive, and so easy of collection . . . if we had to classify the taxes on articles of consumption in order of merit or of harmlessness, we should conclude that the most commendable tax is that on tobacco."[1]

The third main department into which the taxes on articles of consumption can be divided was that of the Customs, Douanes.

[1] cf. *Science des Finances*, edition of 1899, Vol. I., pp. 767, 769.

The Constituent Assembly of the Revolution swept away the multitudinous mediæval obstacles to the circulation of goods within France, and created a Customs system framed on liberal lines. "The law of March 1791 established the commercial relations of France with foreign nations upon the basis of a moderate and uniform tariff."[1] But when war presently befell, war itself closed the ports, total prohibitions of entry abounded, the tariffs, if they remained, rose to dizzy heights, and the field of a real fiscal policy was left open for the legislators of the Restoration and their successors.

Unfortunately, "the Tariff Act of 1816 made it perfectly clear that, for a very long time, France would adhere to the commercial policy which she had adopted during the war."[2]

Acting on the principles of Colbert, the statesmen of the old régime had generally been opposed both to absolute prohibitions of entry and also to the taxation of raw material. But

[1] Levasseur, *Histoire du Commerce de la France*, Vol. I., p. 46.

[2] Mr. Percy Ashley, *Modern Tariff History*, 3rd edition, p. 275.

from 1814 to 1850, at any rate, the Chambers insisted on pursuing a policy in direct opposition to these reasonable principles. The economic historian of that time [1] has demonstrated that throughout that long period the Governments were constantly proposing and favouring an advance towards commercial freedom, but that the Legislature as constantly opposed and rejected those efforts. In fact, up to 1850, at any rate, the tariff history of France is the history of numerous absolute prohibitions and of exorbitant tariffs carried by the Chambers in defiance of the Executive.

Another historian of French economic history has clearly established the broad nature of the financial policy thus pursued. Its main features were the extraordinary place occupied by absolute prohibitions of entry, the taxation of almost all the raw materials essential to industry, and the inextricable and absurd complication and chaos of the tariffs.[2] It was an epoch of fiscal terror, in which the famous saying of

[1] cf. Amé, *Études sur les Tarifs de Douane et les Traités de Commerce.*

[2] cf. de Hock, *Administration financière de la France.*

Marshal Bugeaud, that he preferred an invasion of Russian Cossacks to an invasion of Hungarian cattle, found acceptance.

The first real attack on this intolerable system, which was crippling France, came from the Emperor Napoleon III. After forty years of confusion his Government made a start in 1853 by reducing duties. But the Corps Législatif would have none of it. By a bold stroke, which, however, was strictly within the terms of the Constitution, the Emperor concluded with Cobden the famous Treaty of 1860, thus achieving "the chief financial and economic reform accomplished in France since the Revolution."[1] The result was that "during the period from 1850 to 1860, when moderate reforms were being made, France commenced a rapid advance in prosperity which quickened considerably with the introduction of more sweeping changes of policy after 1860."[2] By 1870 France had become an industrial Power; her commerce, her agriculture, her manufactures were flourishing,

[1] *Science des Finances*, Vol. I., p. 673.

[2] Mr. Percy Ashley, *op. cit.*, p. 303.

and when she came to bear the burden of 1870 she astonished the world.

After thirty years of moderate tariffs opposite principles began to prevail in 1881 and triumphed decidedly in 1892. The causes in operation had been several: the need of more revenue after the disasters of 1870, the fall in agricultural prices owing to the entry of the New World into the market, and the formidable growth of trade rivals, Germany, England and America. This movement for higher rates of duty would have won its way earlier had not the whole system of Commercial Treaties, enacted according to the principles of 1860, stood in the way. But as these Treaties were gradually got rid of, the new system, that of a minimum tariff for supposed commercial friends and a maximum tariff for supposed commercial enemies, was instituted and remained in force mostly unaltered up to 1910. The scales could be altered at any time, whereas those under the Commercial Treaties could obviously not be so adjusted.

The new minimum tariff was, in reality,

much higher than the old "Conventional" tariff established by the Treaties now disposed of. For instance, even on agricultural produce the average minimum tariff was no less than 25 per cent. *ad valorem*, and it may be imagined how eagerly manufacturers would insist on corresponding rises in tariffs affecting themselves. The rates of duty of the maximum tariff were on the average about 15 per cent. higher than those of the minimum tariff. Much to the dissatisfaction of the protected parties and contrary to their expectations, it was the minimum tariff, and not the maximum, which, as the twentieth century proceeded, had come to be generally applied by France to all European countries except Portugal, and to numerous non-European countries also. All this seemed to call for a drastic revision of the duties upward, and this was accomplished, after an active agitation lasting from 1908 onwards, by the tariff of 1910, despite the almost open indifference or hostility of the French Governments holding office during that period. The principle of the new tariff, which held good up to the outbreak of the Great War, was the considerable increase in both rates of duty, the inclusion of many new headings, and a highly developed specialisation of the rates.

Looking at the matter from 1892 onwards, there was real progress in French industry, but it was nothing like so important as that which took place during the same period either in the two chief neighbouring countries of the United Kingdom and Germany, or in the United States. In the great industrial and commercial development of the last decade of the nineteenth century and the first decade of the twentieth century, France had relatively little share. "There was some progress made in the commerce and industry of France during the four years from the enactment of the tariff of 1910 to the outbreak of the European War, but it was in no way comparable to the development shown by her great industrial competitors on the East and on the West."[1] Altogether, "the tariff was one of the stiffest in the world. On British goods exported to France, early in the present century, the duties were reckoned to average 34 per cent., being, of course,

[1] Mr. Percy Ashley, *op. cit.*, pp. 340, 355.

much higher than that in many leading instances."[1]

In the year 1913 the Customs duties yielded 756 million francs to the French Budget.

The last class (*d*) of the taxes on articles of miscellaneous consumption or use was not unimportant. This was chiefly made up of taxes on sugar and salt, and a tax on transport.

Originally, at the period of the Revolution, the tax on sugar was a Customs tax levied on the entry into France of cane sugar from her colonies, but during the reign of Napoleon I the industry of extracting sugar from beet was inaugurated. This beet sugar was not taxed until 1843, and from that time forward many were the commercial and fiscal difficulties which harassed legislators upon sugar. If you taxed it low, there was the double disadvantage for the revenue that sugar from abroad would not be sent in to be taxed at the Customs and that the home tax on beet sugar would also naturally fall in yield. If, on the other hand, you taxed it high, then there arose a chorus of

[1] Mr. J. H. Clapham, *The Economic Development of France and Germany*, p. 264.

complaints from the native growers that they were being penalised for the benefit of the foreign importers and that they could not conceivably compete in the markets of the world. Between these two alternatives the yield of the tax has oscillated, sometimes up to 200 millions in 1894, sometimes down to 175 millions in 1901, and ending at 191 millions in the year before the war.

As regards the salt tax, this was the oldest tax in France, dating, it is said, from the days of Philippe de Valois in the fourteenth century and known under the name of gabelle, meaning a gift or *gabe*. This tax, it need not be said, was levied with the grossest injustice and inequality prior to the Revolution. There were regions of the great gabelle, of the small gabelle, regions redeemed of the gabelle, and regions which had always been exempt from this imposition. One of the most distinguished of French economists, writing in 1876, calculated that in France in 1788 the average daily pay of an agricultural labourer was 60 centimes.[1] From this it may be deduced that

[1] M. de Foville, article in *Economiste Français* of January 8, 1876.

the salt tax in the regions of the great gabelle was as high as one-tenth of the whole of the labourer's revenue. The Revolution, of course, abolished this tax, but it was soon re-established in 1806. By 1872 the salt tax was so modified that it was equivalent only to 1 franc per head of the population, a mere trifle.

Enough has now been said to indicate the general character of the policy pursued by France from 1789 to 1914 in respect of the taxes on consumption. As was mentioned above, these amounted in 1913 to 54 per cent. of the total revenue derived from taxation.

Though we must be disposed to consider this ratio a high one, we must remember that out of the total of 2,269 million francs yielded by the taxes on consumption in 1913, the large proportion of 966 million francs arose from duties on alcohol and tobacco, not to mention the trifling yield from gunpowder, taxes which the Ministry of Finance has recently classified under the heading of "Imposts on Articles not necessary to existence."

The balance of 1,303 million francs was

levied on articles of general use in consumption, and was equivalent to about 31 per cent. of the total tax revenue of 1913.

It may be of interest to compare the financial policy of France in respect of the relation between direct and indirect taxation with that of Great Britain for the last year of the period in question in this chapter, 1913. Speaking in the House of Commons in 1925, the Chancellor of the Exchequer stated that with us in 1913 the ratio of direct taxation was 57·5 per cent., and indirect taxation 42·5 per cent.[1] In order to make some comparison between the two countries, we may include in direct taxation in France the so-called taxes on "revenue" and the so-called taxes on "fortune." On that basis the comparable figures for France were 46 per cent. direct taxation and 54 per cent. indirect. Strictly speaking, however, the "direct" taxes of France only produced about 19 per cent., as we have seen.

Before closing this account of the revenue policy of France up to the outbreak of war, mention should be made of certain further

[1] *Times* report, May 26, 1925.

receipts realised by the French Budget which, if we take the Budget of 1913 as an example, swelled it from the 4,135 million francs of the taxation revenue up to a total of 5,067 million francs.

There were the receipts from the State Domains. The principle of the old fallen monarchy had been that no public property, once acquired, was alienable, and the famous Edict of Moulins in 1566 had formally and finally enunciated that doctrine. But when the Revolution broke out this principle was reversed, the Constituent Assembly having found at its disposal not only the domains of the extinguished régime, but also a fresh mass of properties including those of the Church and those of the *émigrés*.

Accordingly, during the succeeding hundred years there were, in fact, many alienations of these vast possessions by successive Governments, though it was found in 1878, when a summary of the matter was published in accordance with the terms of the Act of 1873, that the State still had property worth nearly 4 milliards of francs. This figure, moreover, did not include such incalculable values as those of the roads or harbours or canals, nor did it embrace the vast possessions of the local authorities in France. But for our present purpose this does not matter, for the reason that neither of these two additional items could, in their nature, provide any material revenue to the Treasury.

More than this, an important reduction has to be made even from this figure of 4 milliards, if we are to regard the question from the standpoint of the public revenue. For the figure in question comprised no less than 2,348 million francs of property which, in the technical language of the French administration, is known as *Domaine Publique*, i.e. State property of which the public user is gratuitous, or which the State employs for its own purposes without attempting to draw any direct revenues therefrom. The balance of the 4 milliards, i.e. 1,644 million francs, is, however, in a different category, and represented the value of the *Domaine Privé* at that date, which is so called because it is of the nature of private property in the sense of producing real and tangible revenue for its owner. In substance, this *Domaine Privé* consisted of the forests of the State. These forests during the period under survey were the only real property of the State furnishing any appreciable revenue. It will be seen at once how modest a contribution could accrue to the public finances from this source. At the date of the Revolution these woods and forests of France had been of the extent of 9,713,000 hectares, an hectare being very nearly two and a half acres.[1] By the opening of the twentieth century this figure had fallen to about 8 million hectares owing in part to the loss of Alsace-Lorraine, and of this area the State, as distinguished from the local authorities, possessed very nearly one million hectares.

Another of the items in question was furnished by the posts, telegraphs and telephones. During that epoch it is exceedingly difficult to discern the true facts as regards the finances of this administration. For instance, taking the accounts as they stood at the close of the twentieth century, these various undertakings

[1] M. de Foville, article in *Économiste Français*, June 19, 1875.

would appear at first sight to have been lucrative, seeing that at that date the annual gross receipts were about 220 millions of francs and the expenses about 160 millions, thus leaving a surplus of 60 million francs. But, unfortunately, it seems more than likely that this was only a budgetary illusion.

Thus there is nothing discernible in the account for interest on all the capital sunk in these enterprises, and nothing for the fact that the local authorities were bearing a considerable share of the cost of upkeep. Again, nothing was reckoned in for the cost of the pensions payable to the very numerous personnel, that figure requiring to be unearthed from its concealment among the estimates of the Ministry of Finance. Finally, the State had made agreements with the railways, and in virtue of these *cahiers des charges* the railways had to perform a vast amount of postal work free of charge on behalf of the postal authorities. But this did not seem to figure in the account. So these items, if added together, would turn the apparent surplus into a real deficit.

Another item of some importance would be miscellaneous revenue, *Recettes d'ordre*.

It may be asked whether the railways, of which the State owned some, and with all of which it had a close connection, did not assist the Budget. But here the answer must be in the negative.

When railways were first started in 1835 the State adopted a somewhat sceptical attitude. At that date, when the first concession for construction was wrung from the Government, Thiers is credited with the remark, "We must give Paris its toy, but it will never carry a passenger or a parcel." From that date forward a most sustained and ably conducted debate, lasting for many years, sprang up on the policy of nationalisation or otherwise. The policy of nationalisation found its chief advocate in Lamartine, who, echoing the principles of the revolutionary Mirabeau, claimed that the State alone should construct and possess the lines.[1] In the final result private enterprise won the day to the extent that, by the close of

[1] Guillamot, *L'Organisation des Chemins de Fer en France*, 1899, p. 7.

the nineteenth century, the State only possessed 6·7 per cent. of the total railway mileage of France. Later, in 1908, the Government felt itself compelled to buy the Western Company in addition, and incorporated it in the State system.

The principle discernible in the fluctuating policy of those days was that the State would not readily own, but was prepared to subsidise and guarantee where necessary. The financial outcome for the State, from the earliest days up to 1883, was on the whole so unfortunate that in the latter year the whole matter was definitely rearranged. The main principle then adopted was one of a State guarantee up to a fixed amount of profits. By an unexpected misfortune bad trade and low prices very shortly drove all the great companies, except the Northern, back on the guarantee. Then a turn of the wheel occurred. One after the other the railways recovered some measure of prosperity, so that in 1905, for the first time, repayments from the companies to the State of the sums which it had advanced were greater than outgoings under the guarantee scheme, except in the case of the Western, which, as already mentioned, had to be bought by the State.

At the close of the period now in question France possessed a railway network consisting of six systems all owned by private companies with the exception of one owned by the State. As regards finance, the position was that the two strongest lines were paying well and had cleared off their debts to the State, while the three weaker ones, though occasionally falling back on the State guarantee, were also in process of repaying their debts. The weakest spot was the State railway system, which was losing seriously. It seems then that by 1914 not only was there little or no profit arising to the State from the railways, but also that the State, if any catastrophe were to occur, would have a very serious liability impending in the shape of guarantees of interest. At the moment, it is true, this was of no great financial importance, but, if a war broke out, what then?

The argument of this and of the two preceding chapters is that, during the period from the Revolution up to 1914, France had not established a system of taxation duly adjusted to the incomes of her citizens. All that ingenuity could devise in the shape of indirect borrowings, of heavy Registration and Stamp duties, of heightened Tariffs, and so forth, had not availed to remedy that central defect, and, indeed, had only served to accentuate it. It was not that France was lightly taxed, it was that she was not taxed rightly. So the advent of the Armed Peace, with all that it entailed of extra effort overseas and in Europe, brought to bear upon her fiscal system a weight too heavy for a structure founded upon injustice.

CHAPTER VI

M. CAILLAUX COMES AND GOES, 1906–1914

"Il y a un bon style de finances, comme il y a un bon style littéraire."—Anatole France, *La Vie Littéraire*, p. 20.

It has been shown in the preceding chapters that, as the year 1914 drew onwards into summer, a crisis was evidently and inevitably approaching in French finance. On the one hand, the expenditure of the State had begun to rise rapidly in recent years, owing to causes uncontrollable by any Minister of Finance. On the other hand, nothing of real moment had been, or was being, accomplished to reform the State revenue system, which was antiquated and unsuitable. In consequence, there was no help for it but to borrow by concealed and irregular methods outside the four corners of the Budget.

Was it, then, true that the able and enlightened statesmen of France stood by to a man "with folded arms to view the progress of this mighty evil," in the phrase used in 1842 by Sir Robert Peel in presence of a similar crisis in our financial history? This was not wholly the case, for, from 1907 onwards, M. Caillaux had come forward with a plan for financial reform, more particularly aimed at the reconstruction of the taxation system. Singularly enough, he found his main support among the agricultural classes, who were profoundly dissatisfied with the unequal incidence of the land tax as an *impôt de répartition*, and who, besides, were firmly convinced that they were more heavily taxed than the commercial and investing classes.

It is true that, before the official entry of M. Caillaux into the matter, many persons had discoursed at large upon that subject, and that even several political banners had been inscribed with the programme of an income tax. But somehow at the crucial moment, when the trumpet had sounded for battle, those discourses had died down dumbly, and that particular ensign had been discreetly furled.

One recalls, for instance, those already ancient electoral days of 1885, when that fiery Radical of the Left, Clemenceau, inscribed on the advanced programme of his Party the *impôt progressif sur le revenu.* For, as it seemed, he wanted to abolish "the old monarchical organisation of our taxes," and to replace "the outworn system of our imposts which spares the rich and weighs down the poor."

This advanced income tax proposal was endorsed in 1886 by the Budget Commission of the Chamber, and even presently by the Chamber itself. As the Parliamentary Sessions wore on, statesman after statesman, minister after minister, nobly ranged himself in its favour. Finally, its hour of victory seemed actually to have dawned in 1896, when the Cabinet of Léon Bourgeois definitely took the plunge, and, for the first time in the history of France, brought forward a measure for a graduated income tax calculated to yield 150 million francs per year.

This was too much. This "anthropométrie fiscale" was denounced by the Opposition with such fury that the alarmed Chamber and the astounded Cabinet dropped the matter forthwith. So for the next twenty years the somewhat dry and caustic remarks of the historian of contemporary France hold good. "This conflict had a merely abstract result. Both sides condensed their proposals of fiscal reform into exact formulæ, adapted to the requirements of electoral propaganda. All agreed to condemn the ancient French system of direct taxation, which agreement, however, did not prevent it lasting for another twenty years."[1]

Nevertheless, long before that twenty years was out, M. Caillaux, as mentioned above, appeared upon the scene in 1907 in his capacity of Finance Minister, and apparently not being content merely to "condense" his plans into "exact formulæ," only suitable for electoral propaganda, he introduced a detailed measure and fought it steadily to a finish.

The plan of M. Caillaux was to catalogue and classify the revenues of all individuals under seven headings or schedules for the purpose of taxation in each case. Knowledge

[1] Ernest Lavisse, *Histoire de France Contemporaine*, Vol. VIII., p. 186.

having thus been acquired of the total revenue of each individual, a tax was to be superimposed upon it in a manner corresponding to the method of our super-tax.

All this was a profound innovation upon the conceptions handed down from the days of the Constituent Assembly, as modified in the succeeding century. Accordingly, the Chamber took two years, up to March 1909, to digest this strong meat, and then passed it on to the Senate. The Senate, in its turn, took four leisurely years to think over the disagreeable subject, and then finally turned it down in November 1913. In default of this scheme, the Ministry of that day had nothing much better to offer by way of finance than borrowing, so that M. Caillaux felt himself at length obliged to cross swords with the Government, though not on the direct issue, with the result that on December 2 this other "man of December" brought the Ministry to the ground. He himself assumed the office of Minister of Finance.

At the opening of 1914, therefore, the excitement of good citizens rose to a fever pitch when they realised the range and significance of the scheme of the Finance Minister. Apart from his income tax proposals, his further plan as regards the taxation of capital was that a man's whole property, both real and personal, was to be subject to tax. It was to be reckoned net, i.e. debts were to be deducted in estimating the assessable amount, and also 5,000 francs were to be deducted in respect of each dependent. Besides these exemptions, no fortune under 30,000 francs was to be taxed at all. On fortunes over 30,000 francs the tax was to be levied on one-fifth of the amount between 30,000 francs and 50,000; on two-fifths between 50,000 and 100,000; on three-fifths between 100,000 and 500,000, and so on. On the above-named amounts the tax was to be levied at the rate of 2½ per cent.

People had by this time become painfully aware that there was now installed in office a man whose programme was tantamount in their view to confiscation, and who, moreover, was resolutely bent on placing that programme on the Statute Book. For

M. Caillaux's plans apparently embraced not merely an income tax on the lines already described, but also an increase in the death duties, besides, worst of all, this tax on capital, *impôt sur la richesse acquise.*

So the issue, long postponed since 1791 and the days of the Constituent Assembly, came to a head at last. Never, perhaps, in Parliamentary history since the days of the Revolution had a more embittered campaign been raised against a Minister. Every charge of treachery, of treason and corruption, public and private, was hurled in crescendo at one man's head. On the other hand, "full of confidence in his talents and in his star, the Finance Minister exhibited a marvellous boldness in his manœuvres." [1] The public crowded to hear his memorable duel with the great financier Ribot, or made a ring for that tremendous battle of economic argumentation in which, on February 27, 1914, MM. Briand, Millerand, and Jaurès vied with M. Caillaux himself for the palm of victory.

But, as 1914 proceeded, the pace grew too

[1] *Annual Register*, 1914, p. 271.

hot, the stress of passion too intolerable. Amid tragic circumstances M. Caillaux fell, to the delight and ecstasy of his enemies. With him vanished that special bugbear, the Tax on Capital. Strangely enough, however, much to the joy of Jacques Bonhomme on the land, M. Caillaux, ere he fell, succeeded so far that, by the statute of March 19, 1914, the tax on land not built on, i.e. agricultural land, was made a tax of *quotité*, and also the taxation of *valeurs mobilières* was reformed. So far, everybody could feel pleased, except no doubt M. Caillaux himself. And then, by the most surprising stroke of all, M. Caillaux himself had the satisfaction of witnessing on July 15, 1914, the passing into law, though shorn of most of its schedules, of his famous or infamous income tax, *impôt global sur le revenu!*

The Income Tax Bill only passed into law after having been severely pruned by the Senate. Under its modest terms every person was made liable, if his income, after deductions for married men and for men with families, exceeded 5,000 francs.

The normal rate of the tax was only 2 per cent. of the net income; and even this was only fully applicable when the income had reached the total of 25,000 francs. For instance, it was only 0·40 per cent. on incomes from 5,000 to 10,000 francs, rising from that level by stages up to the full 2 per cent. as aforesaid.

Take, for example, the case of a married man with two children and with a net income of 30,000 francs. He would pay nothing on the first 5,000 francs; his marriage and his two children would exempt him in respect of another 4,000 francs, thus reducing his taxable income to 21,000 francs. On this the graduated tax would be 220 francs. In this shape, then, on the very eve of war, the Income Tax Bill at last found a haven for its weary, battered, and extenuated spirit on the Statute Book.

A distinguished French economist, looking back on that history, has recently asked with wonder how such an "anodyne" as the income tax measure of 1914 could possibly have aroused "debates of such intense passion, for such was certainly the character of those debates which raged round it from 1907 to 1914."[1]

The fact was that the storm in question had blown and raged so long not against the modest measure which scraped and squeezed into harbour in July 1914, but against those measures which had been originally launched in 1907, and of which this castaway was the last survivor and relic.

The basis of that proposed reform had been the analysis of personal incomes under different schedules and their taxation accordingly, completed and crowned by an *impôt global* on their sum. But this scheme had been defeated so far as the essential schedules were concerned. Apart from the *impôt foncier* the other three of the "quatre vieilles" remained with all their inadequacy and all their injustice on that statute book where the Constituent Assembly had placed them long ago. Hence a just assessment of the income tax as a whole had been rendered impossible. Finally, the *impôt*

[1] M. Germain Martin, *Les Finances Publiques de la France*, 1925, p. 72.

sur la richesse acquise had been beaten altogether off the field.

Thus, when war befell, no real reform of the French financial system had been accomplished. And what had been accomplished had come too late.

CHAPTER VII

THE CRISIS IN PREPARATION

"Il n'y a rien que la sagesse et la prudence doivent plus régler que cette portion qu'on ôte, et cette portion qu'on laisse, aux sujets. . . . Ce n'est point à ce que le peuple peut donner, qu'il faut mesurer les revenus publics, mais à ce qu'il doit donner; et, si on les mesure à ce qu'il peut donner, il faut que ce soit du moins à ce qu'il peut toujours donner."—Montesquieu, *Esprit des Lois*, Livre XIII., Chapitre II.

In the preceding chapter the financial policy of France has been described up to the very date of the outbreak of war. This chapter will be devoted to furnishing an account of the financial policy pursued by that Government during the course of hostilities.

A distinguished French economist, writing in 1919, has stated that, "for many a working or peasant family in France—for all those, at any rate, who have not had to mourn the death of a son—the Great War will have been a veritable Golden Age, the memory of which will be handed down from generation to generation as of a fabulous time, when neither taxes, nor rents, nor debts were paid, and the end of which was much to be regretted, however much one may scruple to pray for its return."[1]

The justification of such a statement may be held to be that the French taxpayers were in many cases relieved of the necessity of paying the existing taxes, the tax collectors being instructed not to prosecute in cases where mobilisation could be pleaded. Also, under the terms of the moratorium, proclaimed at the outbreak of war, mobilised rent-payers or their families were dispensed from house rent, farmers from agricultural rent, and debtors from the discharge of debts. Again, the families of mobilised men received allowances on a gradually increasing scale, with the result that a man with a wife and three children received eventually 5.75 francs a day, or 40.25 francs a week. This represented a total charge on the State of more than 2,500 million francs a year, or one-half of the total pre-war Budget.

[1] M. Charles Gide, "French War Budgets, 1919–20," *Economic Journal*, June 1919, p. 129.

As M. Métin, the Under-Secretary for Finance, expressed it, this fiscal policy was inspired by the desire, "To maintain the magnificent enthusiasm of the people by enabling their families to endure, with a constancy that has never failed, the trials imposed upon them, for the salvation of their country."

M. Gide further arrived at the conclusion that until 1917, "The French Government had performed the feat of carrying on the most expensive of all wars without requiring the French taxpayer to contribute a single penny." [1]

It is advisable that we should check such views as these by taking the Budget figures for the four years from the opening of 1914 to the end of 1917, in the first place. In 1913, the year before the war, the total revenue had been a little over 5,000 million francs. For the four years ending with 1917 the average total revenue was 4,778 million francs, so that up to the opening of 1918 the revenue was on

[1] M. Charles Gide, "French War Budgets, 1919–20," *Economic Journal*, June 1919, pp. 129–30.

the average somewhat less than before the war.

If we include the figures for 1918, when some new taxation, as will be explained presently, had begun to tell, we shall find that, even so, the average revenue for the whole five years up to the end of 1918 was only 5,219 million francs, which was thus only a trifle higher than the above-quoted figure of the revenue of 1913.

It must also be remembered in this connection that, though the franc was kept very stable during the war in relation to sterling, yet there was a certain amount of depreciation amounting at its worst to an average of 28.05 francs to the pound in 1916, as against an average of 25.13 in 1914. The bearing of this is that any depreciation of the franc would naturally tend in the direction of increasing the revenue as measured in francs.

It would seem, then, so far, that the taxation effort of France during the war was not of serious importance, as judged by its yield. In fact the French economist above quoted has laid it down, after a critical analysis of the figures, that in France "Taxation contributed practically nothing towards war expenses. The new taxes of 1917 and 1918 did no more than cover the non-payment of taxes during the years 1914 and 1916."[1]

The financial result of all this was that, whereas the total revenue of France for the five complete years, 1914–18, was 26,098 million francs, the expenditure during that same period was 169,929 million francs. The vast gap of 143,831 million francs had therefore to be filled somehow by borrowing in one shape or another. In other words, during those five years the whole of the war expenses proper were defrayed by borrowing.

In order, however, to form a closer and fairer conception of the financial methods of France during the war, let us inquire as to the taxation policy pursued, and—since reliance was placed almost wholly on borrowing in order to finance the war—as to the specific nature of that borrowing and the consequences involved.

[1] M. Charles Gide, "French War Budgets, 1919–20," note on p. 132 of *Economic Journal*, June 1919.

Taking these important matters in turn, we may omit from our survey the numerous minor manipulations of indirect taxation effected from time to time during the period in question, such as increased rates on alcohol, on postage, etc. The first really serious departure made in taxation was the War Profits Tax instituted by the law of July 1, 1916, *Contribution extraordinaire sur les bénéfices de Guerre.*

There were a number of reasons, not necessary to recite, why this tax should take long before getting into its stride. Its yield was, in fact, very modest during 1917 and 1918, and only attained its apogee of 3,313 million francs after the war in 1921. If we may anticipate events subsequent to this chapter, it may be mentioned that its total yield during its nine years of life should have been theoretically about 18 milliards. But owing to exemptions and difficulties of recovery, it will probably not work out, when the final figures are furnished, at much more than a total of 14 milliards. We must realise, too, that up to March 1924 the people were allowed to pay it in rentes securities, and gained very much thereby, as rentes depreciated. By the date when the law of March 1924 was passed prohibiting for the future this method of discharging the tax, the profiteers, who had paid up to that date 11,442 million francs, had defrayed no less than 7,254 million francs of this total in the shape of rentes.

In 1917, the next year, two further really important steps were taken in the direction of new taxation, the first of these being the tax which later developed into the Business Turnover Tax.

The aim of this statute, which became law on the last day of 1917, was to establish a very productive tax calculated to strike business transactions generally. It was termed the Tax on Payments, *la taxe sur les paiements*, and must not be confused with the later Business Turnover Tax, *la taxe sur le chiffre d'affaires.* This later tax, which was only passed into law in 1920, grew, indeed, out of the earlier tax, but was of a different character.

The 1917 tax in question levied a low tariff on all "civil" payments and on all commercial purchases done retail. Now, among these latter purchases some were classified specially as "de luxe." On this a special tariff, *la taxe de luxe*, was levied at the high rate of 10 per cent. This luxury tariff was really the kernel and centre of the whole plan, for the yield on the other parts of the tax was not important. In due course, an active campaign was organised against this luxury tax, and the Chambers of Commerce declared their preference for a tax on business turnover. The Legislature, only too glad and not a little surprised to have a tax proposed for their endorsement, gracefully yielded to these representations, and this change was duly enacted by the law of June 25, 1920, which created the Business Turnover Tax, *la taxe sur le chiffre d'affaires*.

An observer of financial events might perhaps suggest that the reason why the business community was forward in proposing this Turnover Tax, was because it cherished the not altogether illusory hope that it could pass on the charge entailed by this tax to the consumer.

The other tax measure passed on the 31st July, 1917, was of a really fundamental and epoch-making character. This measure provided a sound and scientific basis upon which to construct that adequate system of direct taxation which had hitherto been wanting in French finance.

It will be remembered that some days before the outbreak of war the income tax, *impôt général sur le revenu*, had been passed into law. But on the outbreak of war this measure was postponed until 1916, and was then again postponed until 1917. Thus it now came automatically into operation in 1917, but its yield during the war was, and could only be, slight.

According to the corrected figures, furnished in 1925 by the *Journal Officiel*, its yield yearly up to 1920 was only as follows :—

	Million francs.
1917	195
1918	359
1919	568
1920	754

But, as has been mentioned in the preceding chapter, this income tax measure was really futile as long as the various items composing each individual's total revenue had not been properly scheduled and ascertained. Without such a classification it was obviously quite impossible to assess correctly the total income of any individual. Therefore, the State now proceeded to remedy this fundamental deficiency much on the lines of the original proposals of 1907.

(1) There was first the revenue derivable from "property built on," i.e. house property. No change was required here in so far as the tax was already levied in this case on the basis of the actual amount of the assessed revenue. It was fixed at 5 per cent.

(2) There was next the revenue derivable from "property not built on," i.e. land. Here it was only necessary to put into force the law of 1914, as in No. (1). The rate was fixed at 5 per cent.

(3) There was the income derivable from the profits made in agriculture. This, as distinguished from the revenue arising from the ownership of the land as such, No. (2), had never, so far, been levied in France as a separate

tax. The profits on agriculture were now reckoned by rule of thumb as being equal to one-half of the rental value of the land in question, though this was raised later in 1920 from one-half to parity. The rate was in principle 6 per cent. apart from certain exemptions.

(4) There was the income derivable from the profits of industry and commerce. In this case the tax was fixed at the rate of 8 per cent., with exemptions.

(5) There was the income derivable from the profits of non-commercial professions, i.e. the "liberal" professions. This rate was 6 per cent., with exemptions.

(6) The next revenue dealt with was that from emoluments, salaries, and pensions, at the rate of 6 per cent., with exemptions.

(7) Lastly, there was the revenue arising from securities. This had already been dealt with, mainly under the statutes of 1872 and 1914, but it was now widened considerably in its scope.

This measure of reform entailed, of course, the abolition of the three ancient direct taxes instituted at the Revolution, i.e. the *personelle-mobilière*, the *portes et fenêtres*, and the *patentes*. Thus of the four ancient taxes only the Land Tax remained extant, so far as the State was concerned.

This series of taxes, except No. (7) tax, were known as the scheduled taxes, *les impôts cédulaires*, because they dealt with all the various categories or schedules of the revenues of the taxpayers. As this new system only began to operate in 1918, when it produced a trifling amount, if we exclude the yield of the *impôt général*, it is clear that the scheduled taxes made no contribution in substance towards meeting the problem of war finance.

The further question of great interest and moment remains to be answered. Why was so little done in the way of taxation during the period of the war? The highest French authorities have themselves been disposed to criticise this policy. We read the words of an economist and a statesman: "On the outbreak of war the fragmentary income tax, which the preceding Legislature had been induced to accept, was temporarily suspended. This event symbolised the new régime. Only after several years of war were taxes levied upon individual categories of incomes and profits, a step which ought to have been taken on the very first day of the conflict. . . . While across the Channel the financial policy, which for 150 years had always given England a free hand in the world, was being continued in force, France was sinking into a fiscal trance which paralysed the activity of the whole nation. The Government was obsessed with one idea—to make the war popular behind the lines."[1]

In mitigation of this serious criticism it can be urged that almost the whole adult male population was mobilised in the very first days of the war, indeed, more than five million men by February 1915. This profoundly upset the collection even of the old taxes, and rendered the organisation of any new taxes extremely difficult.

To illustrate the very great obstacles in the way, we must remember that Customs duties

[1] M. Caillaux, *Où va la France*, etc., English translation, pp. 87–8.

on any articles of public necessity could not suitably be increased at such a time. Indeed, some such articles were freed from existing duties, while others under the Decree of March 1917 were prohibited from entry, as being of no use to a nation at war. This course, though no doubt justifiable, was obviously prejudicial to the Customs revenue.

Besides this, there was no machinery yet in being, or which could be easily constructed, for collecting the income tax. Even after the end of the war, in the spring of 1919, the taxpayers of France, as a whole, had not generally received the demand notes for income tax relating to the incomes of 1917.

Looking at the matter from the technical point of view of the Administrative services, it may be mentioned that in 1913 the number of officials employed for the collection of taxes was 38,000. It was only in 1919 that, after the disturbances of the war period, this number was regained or somewhat surpassed.[1] There was thus a severe "crise du personnel" to account for the difficulties in the way of taxation.

[1] M. Georges Bonnet, *Les Finances de la France*, p. 326.

Last, and not least, it cannot be, of course, forgotten that France was continuously occupied by the enemy, and though, from the date of the Battle of the Marne, the extent of her territory thus occupied was only 4 per cent. of the total area, yet this included the most populous and industralised districts. These Departments are estimated to have produced 70 per cent. of the coal, 63 per cent. of the steel, 78 per cent. of the sugar, of France. They contained in their area 60 per cent. of the cotton spindles, nearly all the wool-combing mills, about 80 per cent. of the woollen yarn and cloth capacity, as well as a high proportion of the jute, chemical, and engineering factories. To look at the matter in another way, these Departments contributed to the Treasury, according to the official calculation of the French Government, about one-fifth of the total revenue receipts prior to the war.

When all the arguments have been considered on both sides with the utmost fairness, and with the most extreme desire to be reasonable, we may be permitted to range ourselves on the side of the opinion expressed by the

French Ministry of Finance itself in its "Inventory of the Financial Situation of France" issued in 1924, in connection with the proposed Budget measures for the financial year 1925. In the course of that document the following conclusion is put on record: "We are thus led to regret that on the opening of hostilities the most strenuous efforts were not made to obtain a greater yield from taxation. Whatever obstacles there may have been in the way of increasing our fiscal resources, the principles of sound policy should have forbidden the issue of new loans without securing at the same time that the necessary service of such loans was secured on permanent revenue resources. The final conclusion of our survey assigns to this initial weakness of our financial policy during the war a very large measure of responsibility for our actual difficulties." [1]

[1] *Inventaire*, 1924, pp. 10–11.

CHAPTER VIII

THE BORROWINGS OF THE STATE, 1914–1918

"Babouc conclut qu'il y avait souvent de très bonnes choses dans les abus. . . . Il trouva en une heure par leur moyen ce qu'il n'aurait pas eu en six mois par les voies ordinaires."—Voltaire, *Babouc, ou le monde comme il va*, Chapter XIII., "La Finance."

PRIOR to the war, and even on the occasion of its outbreak, many persons thought that enough money could not be found to finance it for long. They forgot that already, in the eighteenth century, "Babouc" had ascertained otherwise.

At the close of 1913 the National Debt of France stood at the figure of 32,594 million francs. As the figure of this debt increased from that time forward up to the actual outbreak of hostilities, it can be said that when France entered the war the amount of her National Debt was not very far from that figure of 35,870 million francs which, as already stated, is the official estimate of her then national income.

The service of the French Debt was 1,355 million francs in 1913. But this figure includes the service of the *Dette Viagère*, "life debt," or, as we should say, the charge for pensions. We in this country should not reckon in these pension charges as part of the National Debt. Deducting, therefore, the pension charges, the service of the French National Debt proper in that year was nearly one milliard francs, and, as the debt was on the increase, it must have been at the rate of one milliard francs when war broke out. This was about 20 per cent. of the total State expenditure.

It is not safe, however, to estimate the burden of the national debt of any country by its total figure, or even by the figure of its annual service charge. For it is possible that such debt may have been incurred for useful and remunerative national purposes, or else the money may have been wasted in war.

Viewed from this standpoint, the position of France in respect of her debt was not a favourable one. M. Caillaux has written of the National Debt of France at that date, as follows :—" The Powers of Central and Eastern

Europe, Germany above all, had railroads which compensated for their debts—reduced them, in fact, almost to nothing. Of all the countries of the world, France was the most heavily burdened. With a population of less than 40 millions, she carried a debt of more than 30 milliards, and she could put in the balance against this only minor industrial possessions, composed of a rather poor State railway system, and certain scattered forms of credit, principally the securities of railway companies." [1]

This statement of M. Caillaux, though justified from the strictly commercial standpoint, requires some modification if we would do full justice to French statesmanship, and if we would look at all the facts. Commercially, it is true, there was little direct yield from the sums which had hitherto been raised by the creation of National Debt, little, that is, which was capable of direct entry on the revenue side of a Budget. Nevertheless, it is fair to remember, and it is due to state, that

[1] M. Caillaux, *Où va la France, où va l'Europe*, English translation, p. 31.

a certain portion of the debt had been raised for the purpose of the national equipment, and was, therefore, in the fuller and deeper sense, remunerative.

If we take a more comprehensive view of the history of the French National Debt from the Revolution up to 1914, there would seem ground for the statement that one-third of it had been raised for the purpose of what may be termed the national equipment, i.e. the railways, roads, rivers, canals, harbours and schools of the country. It is true that the remainder had been raised owing to the exigencies of wars.

In the volume issued under the auspices of the Bankers' Trust Company of New York and Paris, this point has been very well stated as follows:

"To sum up the story of the debt to the close of 1913, we find that it increased from about 2,000 million francs at the close of the revolutionary period to nearly 34,000 million francs at the close of the period of Armed Peace. We find that this increase in debt may be apportioned roughly about one-third to public works, such as roads, improvement of rivers, construction and improvement of canals and railroads, to construction of docks, to works of sanitation, to building school houses, in short, to works of a constructive character which added to the health, the pleasure and the industrial status of the nation. The other two-thirds of debt was dedicated to the god of war." [1]

Such was the situation of the National Debt at the opening of hostilities. During the course of those hostilities, as has been explained in the preceding chapter, it was the policy of France to rely on borrowing rather than on taxation. The result of this policy was that the actual increase in the National Debt in the five years up to the end of 1918 was 145 milliards. Or, as the French Ministry of Finance has exactly stated it, "The weight of debt which the war period directly bequeathed to us can be estimated at about 145 milliards." [2]

The result was that whereas the annual charge for the debt was 1,355 million francs in 1913, if we choose to include the pension

[1] Bankers' Trust Company, *French Public Finance*, 1922, p. 200.

[2] *Inventaire*, 1924, p. 19.

charges, this sum had risen to 7,021 million francs in 1918, and to 7,903 million francs in 1919, including always the pension charges. This would be an increase in annual burden as measured in francs of about six times.

If we analyse this borrowing as a whole, we shall find that about 15 per cent. of it was effected by means of advances from the Bank of France, including a small amount from the Bank of Algeria; 29 per cent. was by means of National Defence Bills and similar temporary loans; 36 per cent. by means of permanent loans, i.e. the great Funded Loans, including the loans issued by the Crédit National and the State Railways, incurred expressly on the State's behalf; and finally 20 per cent. by means of Foreign Loans reckoned at the par of exchange. Hence, we may conclude summarily that the war, as far as France was concerned, was financed by borrowing as to 80 per cent. from within France, and as to 20 per cent. from outside.[1]

[1] cf. Bankers' Guaranty Trust of New York and Paris, *French Public Finance*, p. 23. These figures include the borrowings for 1919.

When the war opened, the Finance Ministry was placed in an embarrassing situation. The taxation policy of the State was not capable of swift and flexible adjustment to the urgent necessities of the hour, as would have been the case if a modernised system of direct taxation had been in force. Nor was the season favourable, as may be guessed, for big formal long-term loans, or even for the immediate raising of a large floating debt by means of short-term bills.

Thus it came about that the Government had to resort at the start to another source, different from all these. In the season of crisis they called to their immediate assistance a financial giant, the Bank of France.

This institution, founded, as has been already mentioned, in 1800 by Napoleon, had always been the favourite child, though not the spoilt child, of the great Emperor. Yet the privileges which he or his successors in Government granted to the Bank were always carefully balanced by the stipulation of corresponding duties to the public, and it was perhaps because of this essentially just basis for its operations that the Bank survived so triumphantly among all the revolutions and catastrophes which were destined successively to descend on France.

In the tragic days of 1870 the Bank, which since 1848 had enjoyed the monopoly of note issue, was authorised to suspend specie payments, but the inconvertible currency was so skilfully handled that specie payments were resumed without difficulty in 1878. It also furnished to the Provisional Government of those days a credit of 2,000 million francs, which was, however, not wholly utilised, and, at any rate, was entirely liquidated in 1877. Hence there were clear precedents for what was to happen now, though the scale was indeed gigantic compared with those days of small things.

The wise and able men who had long directed the policy of the Bank of France had pursued a very progressive and liberal policy, more especially since the year 1897, at which date the Bank's charter had been renewed until 1920. More facilities than hitherto were granted for discount, with the consequence that the number of such accounts rose from

3,387 in 1897 up to 21,426 in the year before the war. In this same period the number of its banking accounts rose from 27,304 up to 147,800. As regards its portfolio, the Bank had confined itself to commercial bills of three months' maturity at the most, and also limited its advances on collateral securities to those of a readily marketable nature. Hence the Bank was always in a very liquid position, and, thus resting on this judicious admixture of State control and private enterprise, was not only well able, when the hour struck, to meet the commercial demands for discount which for the moment increased immensely, but also could avail to tide over the crisis at the call of the Government.

If we summarise the accounts of the Bank as they ran normally in the years before the war, we shall find that it was its general policy to keep about 70 per cent. in specie and about 30 per cent. in loans and discounts against its liabilities in the shape of its note circulation and deposits. It is true that, in the critical year and a half before the actual outbreak of war, the above-mentioned ratio had somewhat fallen, so that in July 1914 the ratio of specie to circulation and deposits had fallen to 63·10 per cent. But this was not very material. What was material was that by 1918 this ratio had fallen to 18·49 per cent., and at the close of 1921, if we may look further ahead, to 14·80 per cent.

Was this prodigious change to be accounted for by the fact that the discounts and loans to the public had correspondingly risen? By no means. These had only increased by a modest figure; the real reason of the change was that advances to the State had swollen from the 3,900 million francs advanced to the Government, as at the date of the outbreak of war, up to 20,000 million francs in February 1919. Such was the measure of the assistance which had been afforded to the Government. These huge advances of the Bank took the form, broadly speaking, of an immense increase in the note circulation. The note circulation, which was 6,051 million francs at the outbreak of the war, had attained to 32,000 million francs in February 1919.

The State had obtained these advances from the Bank in virtue of nine successive statutes beginning in August 1914 and ending in July 1919. It should be mentioned that the State had stipulated originally that these advances to itself during the war should be at the rate of only 1 per cent. But in September 1914 it was further arranged that one year after the cessation of hostilities this rate should be raised to 3 per cent. This additional 2 per cent. was not to be counted in the profits of the Bank, but was allocated to a special sinking fund account for the purpose of reducing the State's debt to the Bank.

Such is the main gist and a brief summary of the financial policy pursued by the State during the war in its efforts to obtain ready money on cheap terms from the Bank of France.

The next most important means of raising money was by way of Treasury Bills, in which term is included Treasury Bills strictly so called, *bons du trésor*, and also the National Defence Bills, *bons de la défense nationale*, as the Treasury Bills were renamed after September 1914. This method of raising money from the public was decidedly popular and steadily outdid the method of advances from the Bank. But the immense increase in this means of borrowing came only in 1919, when the enormous amount of over 26,000 million francs was raised in this way. The result of this was that, taking all the war years, including 1919, the amount borrowed by Treasury Bills, etc., was about 29 per cent. of the total war borrowings. This constituted, no doubt, a very dangerous legacy of State indebtedness constantly falling due and constantly having to be renewed.

More important perhaps than either of the two sources just mentioned was a third category of debt, consisting of the great permanent loans, and the fixed term loans, including Crédit National and railroad issues, and bond issues of two years up to ten years currency.

As 1915 opened, the Government, pushing beyond its policy hitherto adopted of relying on the Bank of France and on the issue of bills, conceived the plan of issuing bonds of a short term of currency. They were known as National Defence Bonds, *obligations de la* *défense nationale*, and had a currency of ten years, but they never achieved the success of the Treasury Bills. They were preparatory to the issue of the first great War Loan of November 1915.

During the period of the war the French Government pursued the policy of issuing four great loans to the public, in 1915, 1916, 1917 and 1918 respectively. They were all made in the so-called "classic form," i.e. without a fixed maturity date, being so-called perpetual rentes, and at a discount from par.

These National Defence loans bore a rate of interest of 5 per cent. as to the first two of them, and of 4 per cent. as to the next two. They were all issued so much under par that to the investor the yield was as high as 5·73, 5·71, 5·83, and 5·65 per cent. Added to this their interest payments were free of taxation, though it should be noted that, in estimating the income subject to the *impôt général sur le revenu*, the income from these securities was not to be deducted.

It is further to be noticed that a considerable proportion of the money subscribed was allowed to be in the form of *bons*, of obligations, and of the old existing rentes, besides, of course, actual cash. Hence it happened that, of the amount of the total subscriptions of 55,762 million francs, only 24,130 million francs were in actual cash. Thus these loans might in part be considered as funding operations.

So far we have considered the policy of borrowing during the war by the agency of the Bank of France, by means of short-term bills, and by means also of long-term and funded debt.

There are two main criticisms to be made in this connection, apart altogether from the question as to whether the expenses of the war should have been so little assisted by taxation and so entirely fed by loans. The first criticism is that, short-term borrowing being itself dangerous to the borrower when on a large scale, the dates of maturity should have been most carefully distributed over the future. This was not provided for. As the Ministry of Finance has since acknowledged, the issue of short-term loans should at any rate have been accompanied by the skilful distribution of the maturities of such debt, so as to avoid entailing upon the State important repayments to the borrowers within the course of a single year. "This measure of prudence was not observed in the case of the Treasury Bills, and it can be shown that it was equally neglected in the case of the issue of the bonds of National Defence." [1]

To illustrate the accuracy of this criticism it will be found that the years 1925 and 1929 in particular were most heavily encumbered by vast maturities to be met and discharged within their course.

The other main criticism is that the big permanent loans were issued at too low a price and too favourably for lenders. Hence the large gap established between the nominal amount of the loans and the amount actually received by the Treasury. M. Caillaux as Finance Minister has definitely stated that one of the faults committed was to issue the loans at too high a rate of yield.[2]

It is time to pass from a consideration of the

[1] *Inventaire,* 1924, p. 41.

[2] M. Caillaux, speech in Chamber, June 27, 1925.

borrowings of the Government within France to the borrowings of the Government outside France. These latter proceedings are usually divided into two main classes—the "commercial" debts and the "political" debts. The first class derives its name from the fact that these loans were made to the Government of France, generally speaking, by commercial bodies in other countries. This, however, was not entirely the case. For instance, in 1919 very large stocks were arranged to be taken over by France from the United States. These stocks were purchased by French bonds, and these bonds, due to the United States Government, figure in the total of the "commercial" debt as reckoned by the French Government.

This commercial indebtedness taken as a whole might strictly be given a fourfold classification. There were the creditors in the United States and in Britain; there were advances from Japan, and added to these there were Bank credits granted to France in such countries as Holland, the Argentine, Canada, and so forth. But these two latter classes were quite insignificant compared with the borrowing by France in the United States and in Great Britain. The purpose of these commercial borrowings was principally to buy war materials and food, and any useful material left over by the war.

If we may look forward beyond the war period and may summarise the matter, it may suffice to state that by July 1924 the strictly commercial obligations of France amounted, if all the four classes above mentioned be totalled, to a sum of, in round figures, 5,150 million francs. Unfortunately, however, for France, these francs were "taken at their par value in the money of the creditor country in each case."[1]

The importance of mentioning this may be usefully illustrated by referring to a leading example of these commercial debts. After the war was over France found it advisable to take over certain large stocks from the United States, besides a considerable amount of railway material and machine tools. Putting aside the two latter items, the railway stocks were taken over at an agreed value by France

[1] *Inventaire*, 1924, p. 56.

of 400 million dollars on the 1st of August, 1919. At that date the exchange was 7.25 francs to the $. France handed 5 per cent. bonds to the United States, repayable at the end of ten years, on the 1st of August, 1929.

Looking back on this operation the Ministry of Finance in 1924 made some remarkable statements. Having pointed out that the "encaissements effectifs" realised by these stocks was only 220 million dollars as against the obligation to pay 400 million dollars, it proceeded to say: "The causes of these vexatious results are numerous. The fixing of the price of purchase was not preceded by detailed inventories and checking. The organisation of the sale could not be regularly arranged for because of the amplitude of the task which suddenly devolved on the State, and which it had summarily faced without possessing the necessary personnel and staff. The material being inadequately protected from the weather, this conduced to a rapid deterioration in value. The throwing of such a considerable mass of similar objects on the market could not but knock down the value. Finally, the Treasury had to stand all the loss of the contract, of which the charge remained fixed in a stable currency, while the receipts ran all the risks of monetary fluctuations."

After some further similar observations the Ministry goes on to make a remarkable appeal to the clemency of the American creditor. "We remain persuaded that we shall not appeal in vain to the spirit of co-operation and equity on the part of the creditor, who has not ceased to provide, for the maintenance of our finance, the most precious succour. Our American friends, we are persuaded, will be prepared to recognise the effort that we have been making since this arrangement to pay each year about 20 million dollars, i.e. 400 million francs, in respect of the interest on 400 million dollars, all the more readily since it is proved that we have not, in fact, encashed more than 220 million dollars, and that, as the labours of the experts of the Dawes Plan have shown, the transfer of these sums, added to the other sums due by us throughout the year on other loans contracted in the United States, has largely contributed to the depreciation of our exchange, thus entailing important losses for our finance and our credit." [1]

This is not the first time, or the last, that such appeals have been or will be wafted across the salt and sour Atlantic.

The other grand item in the commercial debt of France was constituted by the large borrowings effected during the war in England on the credit of Treasury Bills. This debt attained at one time to as high a figure as £73 millions, but at the date of April 1923, when an arrangement was signed regulating the whole matter, it had fallen to £55 millions. It was then settled that the capital of this debt should be liquidated by France by a series of payments extending up to and including 1930.

Without entering into further details as to this important subject of the commercial debt of France, it should be said that her policy has been to arrange and systematise the due dates of repayment of the capital involved, but not, it would seem, always with complete

[1] *Inventaire*, 1924, p. 59.

success. Taking the year 1929, for instance, the United States is owed in that year 4 million dollars in respect of the loan of 1920, together with the whole of the 400 million dollars above referred to. Then England is down to be repaid two sums totalling about £16 millions.

Nevertheless, the Ministry of Finance can claim that "the service of this interest of the loans which compose our commercial debt is, in all respects, strictly assured. The extensions of the due dates which we have asked for have been settled in full agreement with our creditors. They have had, indeed, no other end than to establish a judicious scale of repayments which in the course of the war had been confined to too short periods. . . . France, in so doing, has intended to demonstrate to foreigners that her signature has lost nothing of its worth, and that she remains ready to undergo the heaviest sacrifices to honour the engagements which she has contracted." [1]

Unfortunately, these loans appear to be entered in the Treasury accounts at one rate,

[1] *Inventaire*, 1924, pp. 63–4.

and are necessarily repaid at another according to the fluctuations of exchange. Hence embarrassed Budgets. Thus the framers of the Budget of 1924 found themselves called upon to "include, on the expenditure side, several sums totalling two and a half milliards, and corresponding for the most part to losses sustained in repaying in 1920 the Anglo-French loans in the United States."

The other great branch of French borrowing was by way of the "political" debt, constituted by huge advances from the United States and from Great Britain. This subject can be treated very summarily at this point, because the questions which it raised belong to a later period than that now dealt with, and because, during all this period, interest was not paid by France thereon.

As regards the advances from the United States to France, it is enough to say now that four successive Liberty Loan Acts were passed during the period of the war, the first of which dated from April 1917. In virtue of these Acts, four credits were opened by the United States on behalf of France.

The advances made by Great Britain to France were in each of the six years commencing with 1915.

As these obligations were constantly changing in amount owing to the accruing of unpaid interest, it would be a lengthy affair to follow the changing figures. Suffice it that at the end of the war period France owed on this "political" account £550,000,000 sterling to the United States, and £508,000,000 sterling to the United Kingdom, or a total of £1,058,000,000.

On the other hand, France was owed £355,000,000 in respect of her advances to Italy, Russia, Belgium, Jugo-Slavia, and other Allies. Of these sums the most important one individually was the £160,000,000 sterling due to her from Russia. But this, unfortunately, seemed already as good as lost.

The very serious situation in which France thus found herself at the close of the war was that she owed to her Allies more than four times the indemnity which she had had to pay to Germany after 1870, and that her assets, *per contra*, in the shape of her advances to other Governments, were of little value as a set-off.

If we may summarise the general financial situation of France at the end of the war, it may be said to have stood as follows :

France owed a vast "political" debt, as above mentioned, on which she was paying nothing, so far. All that painful problem was left over for the future.

Putting this obligation aside, France was paying in 1918, 7,021 million francs in respect of the annual service on her internal and "commercial" debt, including pensions, which, as already explained, she reckoned in to this charge. To meet this annual service alone, her total revenue for that year was 6,986 million francs, and therefore scarcely sufficed even to meet the service on a portion of her total obligations.

In other words, the position of France was that, in default of revenue, all the cost of her Civil Services, and all her Naval and Military charges, and all her outlay on special Food and Coal accounts, etc., not to mention all the cost of the restoration of her devastated areas, which had already begun to mount up—all these charges had to be met by borrowed monies. As her entire expenditure of all sorts totalled nearly 57 milliards in that year, this meant that 50 milliards of it had to be covered by borrowing in that year alone !

Surely, the hour for momentous and drastic decisions had struck on the horologe of time.

CHAPTER IX

THE CRISIS AND THE TAXPAYER, 1919–1924

A un Créancier Anglois

" Mais à vous veoir (ou l'on me puisse pendre)
Il semble advis qu'on ne vous vueille rendre
Ce qu'on vous doibt. Beau sire, ne vous chaille ;
Quand je seray plus garni de cliquaille,
Vous en aurez : mais il vous faut attendre
Un bien petit."

Clément Marot, *Rondel.*

THIS chapter will be devoted to an examination of the financial policy pursued by France during the five years from the close of hostilities up to the opening of 1924. The latter date is chosen because a new financial epoch seemed to open with it. For, as the Ministry of Finance has itself pointed out, " It was from the end of 1923 that we mark definitely a growing want of confidence on the part of those hitherto prepared to lend money to France." [1] It was then that the crisis came to a head.

[1] *Inventaire*, 1924, p. 20.

Viewed from the standpoint of accountancy this period after the war is one of considerable complexity. That hostile chorus of criticism which, as we have shown, had already raised its voice, since the closing period of the nineteenth century, so formidably against the technical methods of French finance, was now heard in more decisive and adverse volume than ever.

For instance, in his volume on the *Finances Publiques de la France*, published in 1925, M. Germain Martin, Professeur à la Faculté de Droit de Paris, comments thus on the nature of the official statistics of the years in question in this chapter :

" The truth is that the figures which we have laid before our readers must only be accepted provisionally, so variable are the statistics on which our information is based. In fact, we are faced by a mass of hundreds of milliards of expenses piled up in the past ten years which for the most part have not been submitted to any statutory audit. The figures provided by the staff of the Ministry of Finance to the Reporters of the Budget Commission are provisional figures. Not only do the figures of expenditure, as indicated, vary in the successive documents in which they are set forth, but also in the same document one finds that the figures of identically the same expenditures differ between themselves."

The author goes on to say : " To start with, what is the exact amount of our public expenditure ? From 1915 onwards one can only have recourse to the credits voted by Parliament. Thus we have only an approximation." And, making a shot at the truth, he supposes that the actual figures of State revenue and expenditure are " in the ultimate analysis, considerably less in the first case, and considerably more in the second case, than the figures given."

M. Germain proceeds : " Are we even in a position to know exactly the amount of our National Debt ? The figure has been several times communicated to the Commission of the Budget in each Chamber, and the Inventory gives a detailed table of it. . . . Recollect, however, how upset public opinion was, in 1921, when we learned that a divergence of several thousands of millions of francs existed between the totals of the Bonds of National

Defence, as registered at the Ministry of Finance, compared with the return furnished by the Paymasters-General of the Treasury. . . . This was due to the negligence on the part of the latter, who, etc., etc."[1]

Bearing in mind, then, that we must sail with caution in these uncertain and shifting currents, let us nevertheless attempt to summarise the results of the finance of the five years now in question. If we weigh the total receipts of those five years against the total expenditure, there results a deficit of over 150 milliards of francs, not to mention the coming deficit for 1924, which would carry the total deficiency to well-nigh 160 milliards. All this, of course, had to be met by borrowing in one form or another.

Thus the alarming fact was that France, with a deficit of 145 milliards contracted during the war, now had to face another deficit, bringing the total up to about 300 milliards.[2]

The question which inevitably arises at this

[1] M. Germain Martin, *Les Finances Publiques de la France et la Fortune Privée*, 1914–25, pp. 293–6.

[2] *Inventaire*, 1924, p. 21.

point is one which has been asked a thousand times in Great Britain during recent years. Given that France was obliged after the war to continue these vast outlays and to incur these huge deficits, how was it that, instead of continuing to borrow and to run so swiftly down the path of danger, France did not exert herself to the last ounce of her capacity in taxation? For it is assumed generally on this side of the Channel that French taxation still continued to be light, or, at any rate, was not properly collected.

In comment upon the above argumentation some important considerations must be adduced. It must be remembered that during the war France had reconstituted the principles of her taxation generally on sound lines, though indeed it is true that, even by the end of the war, that salutary reorganisation had as yet yielded very meagre fruits. But from the end of the war we must realise that this reorganisation of the revenue system began to yield its increase. More than this, in the year 1920 France made a very considerable effort to increase her taxation.

This effort of 1920 was, indeed, the most considerable that France had ever made in a single year. The Finance Act of June 25, 1920, aimed at producing several additional milliards of revenue, by increasing the income tax rates both on the total income and on the component, or scheduled, parts; by extending up to date the liability for the war profits tax; by increasing the inheritance and succession duties; by adding to the rate of many indirect taxes; by establishing the tax on business transactions; and by largely intensifying the Customs duties by applying a "coefficient," or multiple of increase, to the fixed Customs rates.

The net result of all this was that the total revenue from taxes, which was about 4·1 milliards in 1913, was raised to about 21·9 milliards in 1923, including the War Profits tax, but excluding all local taxes. Hence, the tax revenue had been raised over five times, measured in francs, and nearly twice, measured in sterling, if we choose to adopt for this purpose the average rate of 1923.

On what principles of financial policy had this considerable increase in revenue been raised? How far did it disturb or confirm the ratio between direct and indirect taxation, or, more exactly, between the taxation on wealth and that on consumption, which had been arrived at in 1913? An analysis of the taxation as it stood in 1923 brings out the following results:

(1) Taxes on revenue . . .	27·7	per cent. of total taxes.		
(2) Taxes on wealth and stamp duties	20·1	„	„	„
(3) Sumptuary taxes (chiefly the *Taxe de Luxe*) . . .	3·2	„	„	„
Total taxes on "wealth" .	51·0	„	„	„
(4) Taxes on "non-necessary" articles (alcohol and tobacco).	15·9	„	„	„
(5) Taxes on "consumption" (mainly on business turnover, Customs, and drinks) . .	33·1	„	„	„
Total taxes on "consumption".	49·0	„	„	„
	100	„	„	„

From this analysis we may gather a clear view of the tendencies in the taxation policy of France during those ten convulsed years. The taxes on "wealth," which had been 46 per cent. of the total in 1913, are now 51 per cent. The taxes on "consumption," which had been

54 per cent. in 1913, are now 49 per cent. Considering all the circumstances and all the traditions of France, a fair attempt at equilibrium seems to have been instituted.

But—and here again the British questioner comes in—what was the weight of this taxation as it impinged on the shoulders of the French taxpayers? Here it is inevitable that we should compare this burden with our own. We are all painfully aware of the undue burdens upon us, and nearly all of us are certain that, since the war at any rate, we have been very much more heavily taxed than the French.

It was shown in the preceding chapter that in 1913 the relative weight of French taxation was the heavier, relative, that is, to the national income. For in 1913 our neighbours were apparently paying 9 per cent. of their income in taxes, as compared with our own 7 per cent. But that, of course, does not settle the matter now in hand. For our taxes were very greatly increased during the war, so that in 1923, which is the last year under review in this chapter, our ratio of tax revenue to national income was 18·8 per cent. This would be arrived at by taking our national income in that year at £3,800,000,000, and our tax revenue at about £718,000,000. That ratio has somewhat altered since, falling to about 17.5 in 1924.

Now in France in 1923 the net taxation was 522 francs per head, according to the scale preferred by the British Government and as stated officially by the Chancellor of the Exchequer.[1] The population of France was about 39,200,000 in that year. The national income, according to the best calculations of the French Government, was 125,500 million francs, this great increase in the nominal value of incomes since 1913 being largely due to the depreciation of the franc. It follows from the above figures that the ratio of net tax revenue to national income established in France was a little over 16 per cent. Thus the real burden of taxation in 1923 was not far apart in the two countries, and is tending to increase in France to the extent of 20 per cent. to-day. A statement made by *The Economist* in 1925, that

[1] Chancellor of the Exchequer, reply in House of Commons, reported in *The Times*, April 4, 1925.

"France's burden of taxation is rising to, if it has not equalled, that of Great Britain," though not in accordance with many suppositions, seems justified by such facts as can be obtained.[1]

Nevertheless, even these considerations do not wholly dispose of the matter in issue. For, admitting that the rates of taxation had been much increased and that the burden of them in relation to the aggregate national income was already serious, it might still be held—and indeed was widely held—that the taxes were imperfectly collected, and that evasion on a great scale was practised, with the consequence that the total yield of the public revenue, though admittedly great already, might be easily rendered much more extensive by a better and stricter system of levy.

For instance, we read in a responsible journal like the *Figaro:* "If the tax on agricultural profits yields very little, it is not that the people who pay it are taxed at too low a rate. It is that 99 per cent. of the agriculturists do not pay

[1] *The Economist*, French Financial Supplement, p. 4, January 31, 1925.

up. Everyone knows it, Members of Parliament, the Minister, and the Administration."[1]

Or did not a leading French statesman describe the general income tax as "l'impôt des poires": "the tax for mugs to pay."

Has not M. Caillaux pointed out quite recently that when a tax, such as the general income tax, is "miné par la fraude," "honeycombed with fraud," then it follows, etc., etc.?

Such quotations as these chosen among many necessarily leave an adverse impression upon us. Nevertheless, the mere recital of them does not discharge us, in our search for the exact truth, from the necessity of investigating this important matter independently, always making, however, a fair and full allowance for all the untold difficulties and embarrassments of France.

Taking summarily some of the most important schedules of the income tax and starting with the land tax, we find that this tax is assessed on the actual net rental value of the lands and houses concerned. The combined results of the three statutes of 1917, 1920, and 1921 were to raise the tax by the end of 1923 from an original

[1] *Figaro*, July 1, 1925, p. 1.

rate of 5 per cent. up to a rate of 10 per cent. This tax has been fairly well collected on the basis of the existing assessments. But it must be said that these assessments, based as they are on the registers of the survey, *documents cadastraux*, are very low, so that we obtain from the French Ministry of Finance itself the following striking and significant statement: "The figures which are entered on the registers do not appear to represent more than one half of the receipts which a proper valuation would provide."[1] Hence the point to be criticised in this case is not so much the collection as the assessment.

Turning next to the income scheduled as "non-commercial profits," this consists chiefly of the revenues derived from the practice of the so-called liberal professions. In this case we come upon some avoidance of taxation, if we are to credit, as we must, a statement upon this point of the Ministry of Finance: "The abuses which have arisen from the failure of a proper system of supervision over this branch of the receipts are such that the losses of the

[1] *Inventaire*, 1924, p. 126.

Treasury to-day reach figures which cannot longer be tolerated by our sense of justice and in view of the necessities of the State." [1]

We pass to the taxation on the revenues derived from securities. The French Administration has estimated that, if we total the interest and the dividends paid by the State and by all French companies, including all the foreign securities taxable in France, the amount of this great mass of payments to the holders of these securities is about 23 milliards. Yet the proportion of this huge sum brought into tax is only about 3,700 million francs! It is true that some of this income has been expressly exonerated by statute, whether wisely or not. Nevertheless, making full allowances for this, "no one can doubt but that a very important part of the revenues arising from securities escapes the general income tax. It is certain that the escape of large revenues derived from securities opens up a very wide breach in the assessment of our taxes and withdraws an important part of the wealth of France from its fiscal obligations." [2]

[1] *Inventaire*, 1924, p. 128. [2] *Ibid.*, p. 128.

On the other hand, we may conclude that the tax on the profits of industry and commerce is more efficiently collected, and reaches almost all those persons upon whom it should properly fall. The reason of this is that this tax has taken the place of the old and well-established *impôt des patentes*, so that the collectors have had the old rolls and records to work upon. Hence "of all the new taxes this is the one which is much the most regularly established, at any rate as regards the numbers of those persons subjected to its incidence." [1]

We proceed to the tax on agricultural profits. This has been admittedly very light in yield, considering the great wealth of agricultural France. The threefold reason for this has been that agriculture, having escaped the regular taxation of its profits until now, is naturally unwilling to submit at once to the disagreeable process; that accurate assessments have proved impossible owing to the absence of farm accounts; and that the minute division

[1] cf. P. Bodin, *Les Nouveaux Impôts ont-ils fait faillite*, 1922, p. 16.

of agricultural holdings renders so many persons liable to the exonerations provided.

The principle adopted at the institution of this tax in 1917 was to take as the basis of assessment of agricultural profits the rental value as established by the "cadastral" valuation. This, to start with, was low. Next in order to arrive at the supposed agricultural profits, the rental values were multiplied by a "co-efficient," which in the years 1918 and 1919 was no more than 0·50, i.e. it was halved. It is true that in 1920 this was altered and increased to a co-efficient of 1 for arable land, to 2 for pasture, gardens, orchards, and to 3 for vineyards, etc.

For instance, in 1918 and 1919 a farm taken at an annual value of Frs. 3,000 on the registers of the Land Survey would be considered as producing only Frs. 1,500 in agricultural profits, an insignificant sum. In 1920, the co-efficient of 0·50 having been raised to 1, the profits would be taken at Frs. 3,000, the equivalent of its rental value if the land was all composed of arable. Or if, for example, it was two-thirds arable and one-third pasture, then it would be valued at Frs. 4,000 of profits (i.e. arable $= 2{,}000 \times 1 = 2{,}000$; pasture $1{,}000 \times 2 = 2{,}000$. Total 4,000 francs).

It should be mentioned, as an example of the exemptions now being established in France, that any agricultural profit under Frs. 1,500 was exempted from tax, the tax being 6 per cent., and that the fraction from Frs. 1,500 to Frs. 4,000 was counted only as half of its actual amount.

During the period now in question after the war this system of levy resulted in reducing the yield of the tax on agricultural profits to quite insignificant proportions: for instance, it merely yielded Frs. 25,000,000 as late as 1923. This was quite unimportant, as may be judged from the fact that in 1925 M. Caillaux suggested making this tax yield Frs. 100,000,000, or four times as much.[1]

A surprising fact is, and one very relevant here, that in France, where agriculturalists are numbered by millions, only 122,338

[1] *Projet de Loi ayant pour objet d'assurer le plein équilibre budgétaire*, etc., etc., Document No. 1608. Session ordinaire de 1925, p. 19.

persons made returns in 1920 in respect of their agricultural profits.[1]

On this same subject M. Compère-Morel, a Deputy, made some remarkable statements in the Chamber in February 1925. He pointed out that taking all the years from 1918 to 1923, commercial and industrial taxpayers contributed about Frs. 4,284,000,000 to the revenue; salary or wage-earners Frs. 1,035,000,000; non-commercial professions, Frs. 185,000,000; and agriculturists the relatively insignificant sum of Frs. 95,000,000. And this in a country which is one of the great agricultural nations of the world!

The Deputy went on to furnish several instances of the working of the system of assessment. One of these was the case of a wine-grower with 70 acres, whose gross income for 1924 was Frs. 244,000. His net profit was Frs. 97,200. Yet his taxable income calculated on the existing basis was only Frs. 17,175. On this taxable income his payment only came to Frs. 1,038. The Deputy argued, and does not appear to have been contradicted, that if this

[1] cf. *The Economist*, June 18, 1921, p. 1322.

man had been fairly taxed, he should have paid Frs. 13,000 to the revenue.

M. Compère-Morel went on to propose that, in all cases where the gross receipts amounted to over Frs. 100,000, the real profits should be taken as the basis of assessment. But this was rejected by 315 votes to 224.[1]

Enough has been said by way of example to establish that during the period now in question the newly established taxation of revenue was in many cases imperfectly collected and gave a yield which might be increased. As regards the *impôt général*, somewhat corresponding to our super-tax, it is perhaps enough to quote a statement of M. Caillaux in 1925: "Numbers of taxpayers declare a figure of their revenues which is notoriously under the mark. Failing proofs, or the elements of proofs, sufficient to obtain a verdict from a judge, the tax collectors find themselves utterly unable to raise the figures on the declared revenue, despite its manifest inadequacy, having regard to the style of living of the persons subject to the tax."[2]

[1] *The Times*, February 23, 1925.

[2] *Projet de Loi*, above quoted, p. 21.

It is therefore abundantly clear that the new system of taxes on revenue as organised in 1917 has yielded less than it ought.

It is true that the yield of these taxes on revenue was considerable as compared with the old abolished system of direct taxes before the war. These taxes in 1913 only yielded 722 million francs, whereas the corresponding figure in 1923 for the reorganised taxes on revenue was 5,696 million francs. This includes the *impôt général*, the *impôts cédulaires*, the tax on the interest from securities, and other trifling direct taxes.

We may here extract from the *Journal Officiel* the actual yearly figures yielded by the *impôt général.* The figures for 1917 and 1918 may be omitted, as they are quite insignificant, and have already been furnished in Chapter VII. The figures are in millions of francs.

1919	568
1920	754
1921	1,468
1922	1,269
1923	1,924
1924	2,665

Looking at the matter of taxation in its broadest aspect, the total taxation revenue from all sources had been, as we have already seen, 4,135 million francs in 1913. From this point there had been a merely nominal increase to 5,238 million francs in 1918. But from this latter point the revenue had jumped, so far as regards taxation, to 21,880 million francs in 1923.

Before quitting the subject of the new taxation policy pursued by France, it is important to draw attention to a principle of very considerable merit which was introduced during the years now in question.

To appreciate the nature of this reform, it should be explained that under the old system of taxation, whether direct or indirect, prevailing in 1914, there was no proportion maintained between the rates of tax and the revenues of individuals. Hence the taxes were not only inequitably apportioned in themselves, but also there was no method available for redressing the inequality incidental to the taxation of articles of consumption by the agency of the direct taxes. These latter were neither progressive in their rates, nor did they provide exemptions at their base for people of small incomes, nor did they furnish reductions for persons burdened with family charges. Thus they were very seriously out of date, and in actual conflict with the modern ideas of fiscal justice.

It has been the work of the French financiers of the war period and of the post-war period to remedy these defects. In their organisation of a new system of direct taxation they have pursued the threefold principle of exonerations at the base, of progression in the rate of levy, and of abatements for family charges.

For instance, as regards the rate of the *impôt général* in 1923, the last year dealt with in this chapter, all persons in receipt of a net revenue of under 7,000 francs were exempt, and this figure of exemption was increased for married persons and for those with family charges. From the point where the tax began the rate rose by stages until at 550,000 francs of net revenue the rate of 50 per cent. came into full force.

These new conceptions, which seek to adapt the weight of taxation to the resources and to the obligations of individuals, have passed from the sphere of direct taxation into that of indirect taxation. With the latter end in view a system of sumptuary taxes has been instituted, which did not exist before the war, e.g. the *taxe de luxe*, the taxes on motor-cars and theatrical performances. These are enacted for the purpose of redressing the injustice properly considered to be inherent in the taxes on articles of general consumption.

In the same line of thought it is to be observed that the prevailing principle of the "consumption" taxes before the war was that of "specific" taxation, i.e. the levy was made on the quantity of the merchandise without correlation to the value of such goods. This old conception is being discarded. The Business Turnover tax, with all its serious faults and urgent need of amendment, takes automatic account of the value of the goods affected by the tax.

The argument of this chapter may now be summarised.

The great reorganisation of the French fiscal system, chiefly embodied in the statutes of 1914, 1917, and 1920, had for its governing purpose a fairer and more scientific distribution of taxation than had obtained so far. The total burden was much increased, in itself an evil, certainly, but one unhappily made necessary by the dire situation of the State. Meanwhile, the taxes on "wealth" were increased relatively to those on "consumption."

At first, and indeed up to the close of the period in view in this chapter, there were very considerable evasions. Nevertheless, the great increase of tax revenue during the period now in question in this chapter appears to afford some proof that these grave defects were being slowly tackled.

In mitigation of the heavy burdens thus imposed on individuals there was established a humane and wise system, in accordance with modern conceptions, of exonerations at the base, of progressive rates of levy, and of allowances in respect of family obligations. And these methods were sought to be applied not only to the direct taxes on revenue but also to the indirect taxes on consumption.

So far, so good. Unluckily, as the next chapter will establish, this was not all.

CHAPTER X

THE FAILURE OF REPARATIONS, 1919–1924

" L'État, c'est à dire le pays, doit être un honnête homme, et un homme ne peut pas assister à de grandes souffrances sans éprouver le besoin de les soulager. . . . L'État a une famille, c'est la France! Il doit avant tout sauvegarder les intérêts de cette famille."—Thiers, in the Chamber of Deputies, *Journal Officiel*, November 1871.

In the last chapter, confining ourselves to the period from the close of the war to the opening of 1924, we ascertained the nature of the new taxation policy pursued by France. But, besides the revenue problem, France had to face in these years other tremendous economic issues. These must now be examined in this chapter.

For, beyond the taxation question, there was that of obtaining Reparations from Germany; that of the restoration of the devastated Departments; there was the necessity, or at any rate the desirability, of settling the thorny subject on Inter-Allied Indebtedness; and finally, complicating all the rest of France's other difficulties and entering ubiquitously to upset all arrangements, there were the persistent falls and fluctuations of the franc exchange to be overcome. A fourfold assault delivered in daily increasing strength and persistence upon her financial line of defence, a line which had already been weak even in the piping times of the Armed Peace, and which since then had been sorely battered and breached by the accumulating weight of the Great War.

It would be far beyond our present purpose to survey once more the long story of Reparations in their international aspect, so brilliantly set forth by Mr. Keynes up to December 1921. On the other hand, it is necessary to trace and explain here the reactions of the Reparation question upon the domestic financial policy of France, confining ourselves at present to events up to the opening of 1924, a date which corresponds to an important epoch in the evolution of this matter. For it will be recalled that it was on November 30, 1923, that the Reparation Commission decided to invite the Committee of Experts presided over by General

Dawes "to consider the means of balancing the Budget and the measures to be taken to stabilise the currency" of Germany.

This epoch-making Committee held its first session on January 14, 1924. Its eventual effect was finally to disperse and to discredit the Saga of the Millions which had hitherto been current in France, not to speak of that other Saga of the Millennium which had found such favour among some simple souls on this side of the Channel.

The main concern for French financiers during this period from the opening of 1919 up to the end of 1923 was to obtain money from Germany for the reparation of their devastated Departments.

The war had left behind it in the north-east of France two adjacent zones of territory where destruction had been worked. The first of these areas wound along in a band, on the average about five miles deep, gashing its path of nihilism from the English Channel towards the Swiss frontier. Here was the fixed site of the four years' struggle: it resembled the less agreeable areas of Mars or the moon. Outside this section, and to the north-east of it, stretching up to the Belgian-Luxembourg frontier, was another area which, having been in the occupation of the Germans themselves during the war, had not been systematically shelled and destroyed like the other. This comprised also some of the most highly organised industrial regions of France. Naturally, the Germans had not been concerned to deal it utter destruction as long as they themselves occupied it in strength. Nevertheless, they had stripped much of the machinery in their search for metals, as the pressure of the times went on; and, what was more important, ere their final retreat, they had blown up the power plants and the working apparatus of mines, steel works, chemical factories, breweries, refineries, etc.

In the spring of 1919 M. Dubois, speaking on behalf of the Budget Commission of the Chamber of Deputies, furnished the figure of French losses in these Departments at 65 milliard francs "as a minimum"; and M. Loucheur, the Minister of Industrial Reconstruction, stated about the same date before the

Senate, on February 17, 1919, that the reconstruction of the devastated regions would involve an expenditure of 75 milliard francs.

Six months later the Finance Minister, M. Klotz, made a further pronouncement on this subject before the French Chamber, on September 5, 1919. By this time the claim had grown to a total of 134 milliard francs.[1]

Later on, in 1921, the French Government submitted an official estimate of the losses sustained, laying it before the Reparation Commission. This estimate was for 140,607 million francs, apart from injuries to persons estimated at a further 77,834 million francs, a total, therefore, of over 218 milliards.[2]

In contrast to these claims the leading unofficial authority in France in these matters, M. Réné Pupin, estimated the losses of the devastated regions at 10 milliards to 15 milliards.[3]

Mr. Keynes, who was the official repre-

[1] cf. for above statement, *The Economic Consequences of the Peace*, Mr. J. M. Keynes, pp. 118, 120.

[2] Claim as published by the Reparation Commission, February 23 1921.

[3] Article in *Revue Bleue*, February 3, 1919.

sentative of the British Treasury at the Paris Conference up to June 7, 1919, and who also sat as deputy for the Chancellor of the Exchequer on the Supreme Economic Council, made at that date a calculation independently of M. Pupin's and without knowledge of it. Starting from the assumption that "France has the greatest claim on our generosity," he arrived at a figure half-way between the two alternative figures of M. Pupin, and was thus in substantial agreement with him as to the physical and material damage in the occupied and devastated areas of Northern France.[1]

This figure of M. Pupin's and Mr. Keynes' needed some addition to it in so far as it did not set out to cover the totality of the claims as advanced by the French. These took into account the levies and requisitions made on the occupied areas and the losses of the French Mercantile Marine, etc. Putting these at 7½ milliards and adding them to the 12½ milliards of Mr. Keynes' estimate referred to above, this makes a total of 20 milliards, which is the figure which Mr. Keynes furnished as "likely to be

[1] *Economic Consequences of the Peace*, p. 118.

criticised," but as really the closest and fairest that could be obtained.

It will be seen from the above summary that the policy of the French financiers was to reckon their losses at a high figure. This tendency had three very practical and serious reactions upon the internal financial policy of France.

For, to start with, the presumed prospect of obtaining these vast sums from Reparations dispensed French statesmen from the otherwise urgent necessity of a full "assainissement" of their economic policy. Next, as the people of the devastated Departments learnt that these sums were claimed as their due, they would naturally and inevitably hold out their hands wide to receive them from the French Treasury. And lastly, in order to obtain the satisfaction of these claims, it was imperative for France to secure at the earliest possible moment from Germany reparation payments of corresponding amount.

The consequence of all this was that a Reparation Act was enacted in France in 1919 which established the rights to compensation on a generous scale. It should be noticed that, even during the war period, some 14½ milliards had already been entered in the Budgets on that account. Presently, in 1920, there was instituted a Special Budget, known as the Budget of Recoverable Expenditure, of which the funds, derived from borrowed monies, were applicable to the work of reconstruction and reparation. The years 1920–1923 were the great years of this outlay, but from the end of the latter year the expenditure began to decline. Altogether, by the end of 1923 about 111½ milliards had been reckoned as recoverable expenditure from 1914 onwards, a sum made up partly of reconstruction proper and partly of compensation to persons.

In investigating the administration of the law of 1919, a French author, M. Lachapelle, in a work entitled *Les Finances Publiques après la Guerre*, 1924, following upon a remarkable study published in *L'Europe Nouvelle* in 1923, has given an account of the proceedings under that statute which, to quote his words, constitute "flagrant abuses" and "abuses so monstrous as to be scarcely credible."

It is preferable, however, in fairness to all parties concerned, that we should rely upon the more moderate, though unfortunately too significant, terms in which the French Minister of Finance, in his *exposé des motifs* of the Special Budget of 1923, thus refers to the matter :

"It is indispensable to put a stop to certain abuses which have flourished under cover of the law, and which, if they continue, would cause an undeniable moral prejudice to the whole body of the war sufferers, who would support all the consequences. In a work so complex as the restoration of our Departments of the north and north-east, imperfections and omissions were inevitable . . . so it has sometimes happened that, owing among other reasons to the fluctuations which have occurred during the last four years in the real value of our money, the literal applications of the law have surpassed the intentions, however liberal, of the Legislature, and have permitted the scandalous enrichment of individuals which the Legislature would certainly have forbidden if they had been thought possible. . . . In proposing various measures to check these abuses the Government is conscious of accomplishing a necessary act of conciliation between the public interest which asks for the suppression of unjustifiable expenditure and the best interests of the liberated regions, which would be the first to suffer from the smallest attack delivered on the public credit."

But, unfortunately, Parliament turned down the proposals of the Minister.

Meanwhile, what had been the policy which France pursued at Versailles and elsewhere in order to obtain from Germany the money for Reparations? Certainly, no one could complain that she did not make the most strenuous and sustained efforts to that end. But, on the other hand, she seems never to have formed a very exact conception of the practical possibilities of the situation, or, a scarcely less important matter, of the precise means of obtaining payment.

However that may be, her path from 1919 up to the opening of 1924 was simply strewn with failures, which she attributed partly to Germany, and partly to the United States, and partly to ourselves. Here it is sufficient if we mark five distinct stages of successive disappointments.

In the first place, there was the great failure associated with the date of May 1, 1921. Under the Treaty of Peace signed at Versailles, June 28, 1919, and ratified on January 10, 1920, the probability appeared to be that Germany, in order to free herself, would have to pay, during the forty-eight years following the Armistice, the fantastic annual sum of £780,000,000. But already by May 1921 this absurdity had gone overboard.

The second failure was associated with the new departure, i.e. the new assessment, announced by the Reparation Commission on April 30, 1921, and communicated to Germany in the following month. Under the provisions of Article 233 of the Versailles Treaty, the Reparation Commision now fixed at 132 milliard gold marks, i.e. £6,600,000,000, the total of the damages for which reparation was due by Germany, exclusive of War Loans made to Belgium, totalling another 6 milliards, or £300,000,000. It is known, from an article published by M. Poincaré, that the British representative was strongly opposed to the adoption of the above figure, and considered that the 132 milliards should have been no more than 104 milliards.[1]

When this second settlement, which, by the way, was only about 58 per cent. of the sums claimed, had also begun to go the way of all financial flesh, a third step was taken, as the result of meetings between M. Loucheur and Herr Rathenau, the Ministers of Reconstruction in France and Germany respectively, and an agreement known as the Wiesbaden Agreement was signed on October 6, 1921. Was this to be the means of furnishing a true solution of the reparations entanglement?

This Agreement provided in substance for the making of reparations payments by Germany to France in kind instead of in money. Germany undertook to deliver all material that France might demand for reconstruction purposes up to the limits of her capacity for production, and subject to the satisfaction of her own domestic necessities and to the quantity of raw materials at her disposal.

The scope of this Agreement, must, however, not be exaggerated. The total value of the

[1] *Revue des Deux Mondes*, May 15, 1921.

reparations in kind thus to be furnished by Germany to France between October 1921 and May 1926 was not to exceed 7 milliards of marks, i.e. £350,000,000. Further, procedure was set up by which private French firms were to acquire from private German firms all these materials without the passage of cash. But here again it must be realised that such supplies were already provided for in the Treaty of Versailles, and that the only really new feature was that the machinery of the Reparation Commission was to be replaced by direct dealings between the authorities of the two nations.

Presently, this expedient also, limited as it was in its scope, broke down chiefly before the opposition of parties whose interests lay in other directions.

The fourth attempt at settling this thorny question was that made at the Inter-Allied Conferences held in London and Paris during December 1922 and January 1923.[1]

[1] cf. the *Blue Book*, Miscellaneous, No. 3, 1923, Cmd. 1812, which contains a full account of these debates and the plans of the British and French delegates.

The immediate occasion of these renewed deliberations was the catastrophic fall of the mark, entailing, as it did, the necessity of a revision of all previous arrangements. A Committee of Experts, among whom were Mr. R. H. Brand and Mr. J. M. Keynes, appointed by the German Government to advise it on the financial situation of Germany, stated in their majority report dated November 7, 1922, that in order to avoid the " complete collapse " of Germany it was necessary to secure " an immediate stabilisation of the German mark." They clinched the matter by declaring that " so long as Germany is not relieved for a period from payments under the Treaty of Versailles, any attempt to stabilise the mark would be futile and could only result in the useless dissipation of Germany's ultimate reserves." [1] Here was a bombshell for French hopes.

In the conferences which followed upon the publication of this pronouncement, a profound and vital divergence revealed itself between France, represented by M. Poincaré, and Great Britain, represented by Mr. Bonar Law.

[1] *Blue Book*, Miscellaneous, No. 3, 1923, Cmd. 1812, p. 6.

M. Poincaré started from the position that it was not realised "how serious the French financial situation was. The French could not continue their present effort without receiving something on account of Reparations . . . it was now harder than ever to raise loans in France . . . there was no chance of raising the money to balance the Budget if nothing was done as regards Germany." He added that they could not contemplate a reduction of the debt of Germany, and that if a moratorium was necessary, "France was absolutely resolved not to give a moratorium without guarantees." [1]

In accordance with these views the French delegates at the meeting of the Inter-Allied Conference held at Quai d'Orsay in Paris on January 2, 1923, presented a memorandum, the gist of which was "that in any case the moratorium demanded by Germany is only acceptable on condition that it does not relate to the whole body of payments due from Germany, and that it is accompanied by the seizure of pledges."

[1] *Blue Book*, Miscellaneous, No. 3, 1923, Cmd. 1812, pp. 24 25, 27, 52.

The view of Great Britain as expressed by Mr. Bonar Law was in sharp contradiction to the above position. "His own view was that we should never get out of our difficulties unless some arrangement could be made which would bring the Allied debts on a reasonable basis, and fix a final amount for German reparations at a figure which the world would say that Germany could pay and which would enable Germany to obtain a loan.

"He would like to get every penny that Germany could pay, but, looking at the matter as a business proposition, he felt that it was no use making a demand based on our own needs. No really large sums could be obtained without re-establishing German credit, and this in its turn could only be accomplished by granting a moratorium and taking steps to establish the mark exchange."[1]

Naturally, with so sharp a division of opinion between the Allies, the question for the fourth time went away unsolved.

In default of agreement, the last and fifth

[1] *Blue Book*, Miscellaneous, No. 3, 1923, Cmd. 1812, pp. 35, 78.

attempt of those now in question was made in the practical shape of the military occupation of the Ruhr by France early in 1923. But this too, as need not be argued, proved a failure for the purpose in view.

What, then, was the result of all these negotiations and actions, these scurryings of statesmen, this proliferation of protocols during five long years? What had France received from Germany by the end of the year 1923? Very little, in spite of the unceasing exertions of her statesmen. Up to the end of that year France had obtained from Germany 1,804 millions of gold marks indeed. But from this had to be deducted 1,614 millions as expenses of the army of occupation and as advances to Germany under the arrangements made at Spa. Thus there only remained a balance of about 190 million gold marks as the real contribution to reconstruction to be set off against all the "recoverable" expenditure mentioned above.[1]

[1] cf. "Report on the Economic Conditions in France to June 1924," of Mr. J. R. Cahill, Commercial Counsellor, British Embassy, Paris, p. 32.

Into the causes of this stupendous disappointment or miscalculation it is not necessary to enter further. The French attributed it in some degree to Germany and the United States, but also to the action of Great Britain. One quotation out of a hundred will suffice to illustrate this. Towards the end of the period in question in this chapter, M. Louis Dubois, speaking with all the authority of one who had served as President of the Reparation Commission, declared that "if there is one fact that is well established, it is that at no time did Germany make up her mind, or make any serious attempt, to fulfil the obligations imposed upon her by the Treaty . . . it is as well to speak plainly, if the Treaty is not complied with, the fault lies, after Germany, with the British Government." [1]

On the other hand, the view held widely in Great Britain was that French statesmen not only asked impossible sums and thus constantly defeated their own purpose, but also that they never faced the very difficult but absolutely

[1] M. Louis Dubois, on the Problem of Reparation, at the Union de Commerce et de l'Industrie, June 23, 1923.

vital problem as to how these sums were practically to be obtained from Germany.

However all that might be, it is clear that up to the end of 1923 and the opening of 1924, Reparations had brought practically no tribute into the French Budget. Indeed, the false hopes of them had only served to lull and lure Parliaments and Ministers into financial courses of ever-increasing risk.

The next great issue of the time which confronted France was the settlement of the important problem of Inter-Allied indebtedness.

We have here to confine ourselves to looking at the matter exclusively from the angle of the domestic finances of France.

Dealing here with the "political" debts, as distinguished from the "commercial" debts, it would appear, as already stated on a previous page, that in 1919 France owed a total of about £1,058,000,000. On the other hand, she was owed about £355,000,000. But of these sums about £160,000,000 was owed by the defaulting Russia.

Here was no internal debt, the weight of which might be reduced as the franc fell, but, on the contrary, a debt expressed in gold dollars and in sterling. This crushing responsibility seemed to dictate imperatively a line of compromise and conciliation towards the United States and the United Kingdom, so that these Powers, in the interest of the common welfare, might abate their claims. Such a settlement seemed by no means impracticable, to judge from the temper of the time. The wonderful work carried out by Mr. Hoover of the American Commission of Relief during the first half of 1919, a work of the noblest and most disinterested good-will, of vital importance, too, at a moment when the breakdown of European civilisation itself seemed imminent, showed the spirit and possibilities of the hour. Similarly in England there was a strong current of good-will towards France available at that date for the purpose of settlement. We thought of all her sufferings, and of all her sorrows, and of all her gallant feats of arms. Her losses seemed mingled with our own. There were a thousand battle-fields on which our sons had fallen, or had won, in common. But unhappily, in order to make room for other issues, this outstanding problem was shunted out of sight.

It was impossible, however, that so immense an issue could be ignored permanently, and thus it happened that, in the course of the year 1922, the very force of events themselves began to bring it forward for consideration and settlement. The United States pressed us for payment of our debt to them. Hence the issue of the Balfour Note in the autumn of 1922, which linked the British debt towards America with the receipts to be obtained by Britain from her debtors. Also, there was the growing uncertainty as to obtaining Reparations from Germany. If these were not obtained from Germany, this would evidently react upon the capacity or the willingness of France in regard to the discharge of the sums due by her to the Allies.

Hence it was that, at the Inter-Allied Conferences held in London and Paris from December 1922 to January 1923, M. Poincaré found it advisable to explain the policy of France in this matter, and to propose a line of action.

The position of France was "very clear. The French were debtors: they recognised their debt and would do their best to pay it as soon as possible. . . . During the war the Allies had given each other help financially and economically, in order to achieve a common victory. France, who had been in the firing line from the first moment, and who for a considerable time had had to bear the first brunt of the battle, had to a great extent found it necessary to obtain supplies from her Allies. Hence these heavy war debts. . . . All had worked for a common cause and everything had been pooled. It had been believed that the Allies would, on the day when victory had been reached, demand from Germany not only the damages, but the cost of the war. Then the Treaty of Versailles had been drawn up."

M. Poincaré went on to argue that "those of the Allies who had contracted debts had found that they themselves became debtors without obtaining the cost of the war from Germany. . . . Consequently, it was true that from the Treaty of Versailles it resulted that in justice the payment of the Inter-Allied war debts ought to come only after the receipt of compensation from Germany. In fact, the principle had been recognised that the damages ought first to be paid, and that this was the first rank of payment on which the debts would be secured. Legitimately, the Allies ought to say that they would pay their debts when they themselves were at least paid their damages." [1]

This was an argument not perhaps of the most impeccable logic. The Treaty of Versailles, of which, of course, France was signatory, had not provided for the costs of the war to be obtained from Germany. The debts in question were a part of the costs of the war, and were an obligation, whether Germany fulfilled the terms of the Versailles Treaty, in regard to war damages, or not. But, though the statement of M. Poincaré might be lacking in absolute logic, there can surely be no doubt of its general force, and, to speak plainly, of its moral weight.

M. Poincaré, however, did not confine himself to this argumentation. He proposed a

[1] Statement of M. Poincaré at 10, Downing Street on December 9, 1922; see *Blue Book*, Cmd. 1812, pp. 32–3.

plan. In order to comprehend this plan we must refer to the Schedule of Payments agreed to by the Allies in 1921. As already stated, it fixed the sum due from Germany at 132 milliards of gold marks. Now, this payment was to be made in the three forms, A, B and C Bonds.

The series of A and B Bonds totalled 50 milliards—£2,500,000,000. The balance of Germany's liabilities was estimated at 82 milliards in the form of C Bonds—£4,100,000,000. The services of these three series constituted respectively a first, second and third charge upon the available funds. The service of the A and B Bonds was to cost altogether £150,000,000. The service of the C Bonds, also at 5 per cent. interest and 1 per cent. sinking fund, came next. This summary explanation will enable us to understand the bearing of the French plan now advanced by M. Poincaré.

According to this proposal, each State, after receiving its proper share of A and B Bonds, would cede C Bonds to its creditors, up to the nominal amount of its debt. France would be willing to do the same in respect of her debtor nations, and would thus be prepared to receive C Bonds from them in satisfaction of her claims. In a word, and to clinch the matter, "the French Government would be ready to deliver to Great Britain forthwith out of the French share of the C Bonds a capital nominally equal to the nominal amount of the French debt. Upon this hypothesis France would be ready to extend the benefits of an identic mode of settlement to her European debtors."[1]

These proposals were formulated more precisely in a memorandum presented about a month later by the French Delegation at the subsequent conference held in Paris in January 1923. "The Inter-Allied debts were contracted with a view to the common victory, they constitute the expenses of war, and in harmony with the principles founded on Articles 231 and 232 of the Treaty of Versailles they ought to be covered by the credit derived from Reparations. The French Government cannot either in equity or in deed pay either the capital of these debts or the interest upon them,

[1] Statement of M. Poincaré at 10, Downing Street on December 9, 1922; see *Blue Book*, Cmd. 1812, p. 33.

until it is at least indemnified by payments from Germany for the expenses incurred and to be incurred for the reconstruction of the devastated areas. These expenses correspond in the main with the French share in the A and B Bonds."[1]

This was to put the matter rather more definitely. France would not pay until Germany had paid for all the damages of the devastated Departments by liquidating the A and B Bonds. This would mean an annuity payable by Germany of an amount which in the then state of Germany was beyond practical politics. If so, what would be the value of the C Bonds which came after? Nothing.

Assuming, then, that the C Bonds would be worth nothing, the proposal of France was (*a*) to wipe out the debts due to her by Russia and the minor Allies, (*b*) to wipe out the debt due by her to Great Britain and the United States, if both these Powers accepted C Bonds, and (*c*) to scale down her future claim on

[1] Statement of M. Poincaré at 10, Downing Street on December 9, 1922; see *Blue Book*, Cmd. 1812, pp. 102–3. Memorandum Annexe II., dated January 2, 1923.

Germany to her portion, 52 per cent., of the A and B Bonds, which totalled, as is seen above, £2,500,000,000.

So the proposal for settling this thorny question stood, without action taken upon it, as 1923 ended and 1924 came.

And lastly, the franc? For the average of 1923 the franc stood at 75.74 to the £. But this average conceals the fact that during 1923 the franc began to fall seriously, and ended the year with an average exchange for December of 82.95 to the £.

This was the danger signal, and was the outward and visible sign of the finance which had been practised in the five years since the war. The broad summary of that finance was that, having to spend so much on restoration and having got nothing from Germany, France had to go on borrowing, with the result that, taking her revenue against her total expenditure, there was a net deficit of over 150 milliards of francs on the account.

The nature of the loan policy adopted had been still to rely, in some measure, upon the Bank of France. The advances by the Bank of France to the State had been 17,800 million francs at the opening of 1919. They were 23,100 million francs at the opening of 1924.

Besides drawing to some extent upon the Bank of France, the State had adopted the policy of resorting to a novel body specially created in 1919 for this purpose, the Crédit National. The full title of this organisation as fixed in October 1919 was the Crédit National pour faciliter la Réparation des Dommages causés par la Guerre. It was in reality a Company formed by a group of the chief French Banks, and its method of proceeding was to raise capital by the issue of bonds, which money was devoted to all the various forms of restoration. The bonds were guaranteed as to principal and interest by the French Government, and it was arranged that they should be met as to capital and interest by an annuity charged in the State Budget. The purpose of this method of procedure was to avoid, as far as possible, direct prejudice to, or conflict with, the issues fathered by the State itself. It is not necessary to enter into the various forms which these bonds assumed, for they were issued under very varied categories of long term, medium term, and short term debt.

The other mainstay of French finance in this respect was still the long-term direct Government loan. From this expedient the Government abstained until 1920. In the course of that year, however, the necessities of the State were so urgent that two great loans of this nature were issued at 5 per cent. and 6 per cent. respectively.

The last resort of the French Government was to a much less desirable means of raising money. This was constituted by Treasury Bills, including in that term the Treasury Bills proper, *bons du trésor*, and also the National Defence Bills, *bons de la défense nationale*. In this dangerous way the Government, whose Treasury Bill issues were a little over 23 milliards at the close of 1918, had now got outstanding at the close of the period under review in this chapter over 61 milliards of these obligations.

Thus, as 1924 opened, France, with all these great financial problems still unsettled and with her open capital account, seemed to be marching straight for the abyss.

CHAPTER XI

THE FLIGHT FROM THE FRANC, 1924–1925

"Il ne faut jamais compromettre la bonne foi d'un Gouvernement. De nos jours il n'est pas facile de tromper longtemps. Il y a quelqu'un qui a plus d'esprit que Voltaire, plus d'esprit que Bonaparte, plus d'esprit que chacun des ministres passés, présents, à venir. C'est tout le monde!"—Talleyrand: speech in the Chamber of Peers, July 24, 1821.

AT the opening of 1924 the Crisis broke. In the expressive phrase of the Ministry of Finance it was "la tourmente." It had been long in coming. We have traced the factors which produced it in their sequence from 1914 and even from remoter years. Nevertheless, when the crash befell, many voices in France were heard to ascribe it to our machinations. But really we were innocent of the declaration of "the war against the franc."

What, then, was the reason why the franc, of which the average rate was 82·95 to the £ in December 1923, fell catastrophically to nearly 120 to the £ in March, 1924?

It is probably true, or indeed certain, that, at a certain point in the proceedings, sheer speculation took a definite hand in the matter. Many persons had persuaded themselves during some four years past that the franc was sure to rise in value presently. France was so rich! A Government in penury, a people in prosperity! "L'État gêné, le pays aisé!" On this calculation they had bought francs to such an extent that it has been semi-officially estimated that 20 milliards of franc credits had been accumulated abroad, held by these astute Europeans or Asiatics in certain hope of the resurrection of the franc.

Now, at the opening of 1924, the eyes of these gentlemen, long blind, began to be opened, and their ears, long deaf, began to be unstopped. Sniffing disaster in the economic air, they sharply reversed their policy, and, like the heathen in the time of Clovis, they began to burn what they had adored. In plain terms, perceiving the realities of the economic situation, they sold for the fall with such alacrity that, at the next General Meeting of the Bank of France, the Governor could assert that in the course of the crisis "it appeared ever more clearly that the exchange market was dominated by a large movement of speculation coming from abroad." [1]

But though the speculators played a part in the crisis, it was not they who caused it. It was not they who had set the alarm bells ringing. They had only chimed in. The financial policy of France had come to trial. The people of France had for a time condemned it. The speculators were only the mob shouting "À mort!" round the tumbril of the sentenced franc.

The real cause of the sudden fall in the franc was that, as 1923 ended and 1924 began, the French people, after nearly a decade of lavish lending to their own Government, showed distinct symptoms of being averse to lending any more.

Yet, as the year 1923 was closing with the usual deficit and as the year 1924 was opening with the full prospect of another one, it was imperative to close the ever-open abyss. By

[1] M. Robineau, at the meeting of the shareholders of the Bank of France, January 13, 1925.

more borrowing? This was tried, but a Crédit National loan proved a failure. There was obviously no help to be obtained in that direction.

Or could the State borrow by means of short-term debt? But even the existing holders began to indicate reluctance to renew their bonds as they were paid off.

Then why not fall back on the trusted friend in adversity, the Bank of France? But, alas, as long ago as December 1920, the Government had entered into an engagement with the Bank of France to do the very opposite, i.e. to liquidate its debt to the Bank of France by two milliards annually. This debt at that date stood at 26,600 million francs. The distressed Treasury had had perforce to rearrange this contract in 1923.

Here then was "la tourmente," a State bent on borrowing, but with nobody in France anxious to lend to it. A "tourmente" indeed!

In order to indicate how the impossible was once more accomplished, the Ministry of Finance furnished at a later date a somewhat cryptic explanation: "Unable to procure the necessary sums by means of borrowing, our Treasury has been obliged at certain moments to have recourse to a premature discount of its future receipts."[1] What that really meant will appear eventually. Enough for the moment to notice that the Bank of France notes in issue leapt up sensationally from 37,339 million francs in September 1923, to the prodigious total of 40,266 million francs in March 1924. The crisis straightened out into a huge increase in the note circulation. Nearly 3,000 million francs were added to the circulation in a short space.

Then another issue emerged in inevitable sequence. The French public, realising what had happened so recently in Austria, in Russia, and in Germany, followed these movements of increasing volume and decreasing value in the note issue with a most acute and painful interest. They realised that the important thing in a depreciating currency is not so much the fact of its depreciation as the fact that this depreciation is always, necessarily, unequal in its incidence. What it effects most certainly is an

[1] *Inventaire*, 1924, p. 239.

immediate profit for the issuers, who make, as it were, a forced levy upon capital. On the public it inflicts a blind and irrational redistribution of wealth. The pauper and the profiteer are its twin offspring.

In these circumstances, the French public very properly demanded that prompt action should be taken by the responsible authorities, and that a remedy should be enforced. Unfortunately, the methods adopted were for some considerable time on the wrong tack, or, at least, had no effect. The Bank of France began by raising its discount rate hastily from 5 to 5½ and thence to 6 per cent., with the idea of checking speculation; while the Government with equal haste announced some fresh measures of taxation, so as to avert the deficit of the Budget. These plans, which were introduced on January 17, were calculated to produce an extra 5 milliards or more. But it was done in a half-hearted manner, there was opposition in the Chamber, and the measures were not pushed to the point of passing them into law until the end of March.

The new expedients for taxation may be

mentioned in passing. They chiefly consisted in applying a so-called double *décime*, or an increase of 20 per cent., to the general body of the existing taxes, a rough-and-ready method indeed. For instance, the effect upon the rates of the different schedules of the income tax, which were thus increased each by 20 per cent., may be illustrated as follows: The tax on agricultural profits was raised from 6 per cent. to 7·20 per cent. The tax on industrial and commercial profits similarly from 8 per cent. to 9·60 per cent. The tax on house and land property from 10 per cent. to 12 per cent.

But all was useless, and the franc still fell.

In their dismay or their despair, Ministers spread their imploring hands to the distant sky where blazed the Almighty Dollar. The French Treasury invoked Uncle Sam.

This was not the first time that France had done so in recent years. It is highly significant that they had become increasingly disposed to ask for help from across the Atlantic. There had been the loan of 100 million dollars in 1920 at 8 per cent., and another such loan in 1921 at 7 per cent. Now, after obtaining through Lazard Brothers in London a little credit of £4,000,000, they proceeded to procure a huge credit of $100,000,000 in New York, which was granted them by a consortium of banks headed by Messrs. J. P. Morgan & Co. This credit was to be used, and was used successfully, at first, to fight the decline in the franc.

As regards the British advance this was very soon liquidated, but the other one was not. Nevertheless, the special danger to France, should she operate upon the credit, was that gold in the Bank of France was pledged to the Morgan syndicate as security for the advance. As the Finance Minister admitted in the Chamber, " the whole credit of the State rests finally on the gold in its Bank of Issue," and thus such a mortgaging of the Bank's gold stock constituted an " acute danger for the whole country."[1] Therefore, something further had to be done, all the more because, as 1924 proceeded, the franc showed further signs of weakness, and another " bear " raid of a formidable character appeared to be preparing upon the

[1] Speech of M. Clémentel, *Temps*, November 23, 1924.

part of those who realised that, when the time for the credit had expired, France would be left without a "mass of manœuvre" to defend the exchange.

After considerable and critical negotiations with the American interest this difficult corner was turned by an arrangement whereby the credit was transformed into a long-term loan. Instead of a "crédit réel," i.e. a credit based upon the gold in the Bank of France, there was substituted, to use the technical word, a "crédit personnel," i.e. a loan secured on nothing but the general good faith of France. It was issued in New York at 7 per cent. interest at 94, and was repayable by France in twenty-five years at 105, on the same gold basis.

The proceeds of the loan, apart from a portion utilised by the State to defray its statutory obligations to the Bank, were to remain normally in America, invested in gilt-edged securities as a fighting fund under the auspices of the Bank, calculated to maintain the French exchange in case of further trouble. As the Finance Minister rather ruefully pointed out in the Chamber, " no doubt, as I must confess, it will be a losing transaction, as measured by the difference between the 7 per cent. which we shall pay for the money and the 5 per cent. or $4\frac{1}{2}$ per cent. at which we shall invest it in American securities. But it is worth while running this risk and this loss, as it is the way to prevent the depreciation of the franc." [1] Such were the stern uses of economic adversity.

As 1924 proceeded upon its troubled way, the situation appeared ever more embarrassed and critical. In July the British public read that " for all practical purposes, France is now at the end of her tether." [2] On the other side of the Channel, the French Prime Minister, M. Herriot, who had attained office as a result of the elections of the preceding May, exposed the situation in the Chamber in language which would have made Léon Say, or Thiers, or Baron Louis turn in their graves.

The Prime Minister declared that the financial issue had now become the master question in France, dominating all others, and that he

[1] M. Clémentel, *Temps*, November 23, 1924.

[2] *The Economist*, July 12, 1924, p. 54.

was there for nothing less than "to save the country from financial anarchy." He sternly denounced "the delays, the want of foresight, and the levity," which had hitherto been the order of the day. While not claiming to mend matters in a few months "after four years of chaos," he exclaimed that "for the first time for many a long day I shall tell the truth, however painful it may prove to be"; and he wound up this startling speech by repeating that "it is absolutely necessary to make good the deficit of 4 milliards of francs existing, or in certain prospect, for the current year."[1]

As a matter of fact it would seem that, if we take the total expenditure of the State in 1924 and compare it with the total revenue, the actual deficit was a little over 9 milliards.

It is true that the figures could be presented, and were presented, in many ways, so as to reach various conclusions.

This was rendered possible because three sorts of Budgets have figured in the post-war accountancy of France. There was, first, the normal, ordinary, "general" Budget; then

[1] M. Herriot in the Chamber, November 7, 1924.

there was the Budget of "extraordinary expenditure"; and lastly, the Budget of expenses "recoverable" under the Treaties of Peace, recoverable, that is, from Germany. The second of these Budgets was suppressed in 1922, when it was absorbed into the first. But the third of them, which was instituted in 1920, was still continuing in life. It had been mainly fed by borrowing, until the day should come when all should have been repaid from across the Rhine.

It must be said that by a salutary change of financial policy, enforced by the monetary crisis of January 1924, and by the continued absence of Reparations, an inaugural step had been taken towards suppressing the "Recoverable Budget" too. The "permanent" charges of this Budget, i.e. the interest on the monies borrowed for Reparation and Pension charges, were transferred from it and were incorporated in the ordinary Budget. This removal had involved a sum of about 6 milliards, which henceforth, of course, had to be defrayed out of the ordinary revenues. Naturally, this swelled the estimated expenses of the ordinary Budget of 1924 from its original figure of over 23 milliards to nearly 30 milliards, thus necessitating a corresponding rise in revenue, which increase was to be made good, as we have seen, out of increased taxation and so forth. Thus the figures could be turned and twisted in many ways.

If you wanted to establish that there was a surplus, then you confined yourself to the figures of the ordinary Budget. If you wanted to make out that it was a close matter one way or the other, then you took into account the newly incorporated expenditure balanced by the new taxes. If you wanted to show that there was a real deficit, then you extended your economic vision to the general finances of the State, and, embracing in your survey the remaining expenses of the "recoverable" Budget, you established that a deficit started inevitably into view.

However, all these subtle calculations were of not much avail in face of the official information, issued at the close of October 1924, as to the terms upon which the current deficit was to be met by loan.

The Finance Minister at this juncture proposed to issue what he himself described as "the first of the great Consolidation Loans." That description did not err, perhaps, upon the side of under-statement, as may be judged from the fact that it was to consist merely of ten-year 5 per cent. Treasury Bonds, the repayment of which was to begin as from the end of the fifth year after issue, with an eventual bonus to the holders totalling 50 per cent. of the nominal value. The yield was officially announced as working out at 8·50 per cent. free of tax, and the hope was expressed that investors would be attracted by the prospect of increasing their capital by 50 per cent. within ten years. But what of the State and its interests? That the State should have to borrow at such a very heavy price was another proof of financial debility, and a realisation of this other adverse factor caused a heavy drop in French rentes to a well-nigh unprecedented level.

There was yet another factor of the most serious importance which weighed upon the scene.

At the opening of 1924 it had been announced by the Minister of Finance that "on January 1, 1924, the amount still required to complete the work of reconstruction, so as thoroughly to restore the devastated Departments to their previous prosperity, is estimated at 30 milliards of francs. On the basis of present prospects it can be said that the reconstruction will practically be accomplished in three years' time. At the end of 1926 all the houses and factories and farm buildings will have been rebuilt, and the land will have been restored to the same productive conditions that it was in before the war."

From this it appeared that until the end of 1926 money would require to be borrowed at the rate of 10 milliards a year in order to finance the restorations. But how? Was it to be in cash, or in kind, in Government Stock, in ten-year bonds, or in thirty-year annuity certificates? Clearly, in the absence of cash or kind in sufficient quantities, the payments would have to be made in the latter forms.

In order to understand the issue, let us look at the most important devastated Department, that of the Nord, as it was in the middle of 1924. At that date in the Nord Department the work of restoring the factories and mines had been so well accomplished that the Prefect was able to report them at 92 per cent. of the pre-war total. On the other hand, only 56 per cent. of the buildings, which had been totally destroyed, had been replaced. The principle of payment to the war sufferers had been that the State paid one-fifth of the cost of their rebuilding operations at the start, and the rest of the money as the bills of the contractors fell due.

With the contraction in the prosperity of the State and in the pinch of money, the Government had begun to pay less and less in cash, and more and more in bonds of a ten-year currency. Thus, in the first six months of 1924 the payments in the Nord Department were 186 millions of francs in cash and 255 millions in ten-year bonds. For the second half of the year, however, the Department found itself with the prospect of receiving only 32 millions of francs in cash and 360 millions in ten-year bonds. Unfortunately, these bonds in the latter half of 1924 could only be realised at a discount of 15 to 20 per cent. of their nominal value.[1] For a time these bonds had been accepted at par by the contractors and had been absorbed. Now they were being less and less wanted, or refused altogether.

It is easy to see what serious results this might have for the war sufferers who, with contracts made, could not meet their obligations, or, with contracts not yet made, could be sure of nothing. Also, this would have a serious reaction upon the above-mentioned Government estimates of the money still needed up to the end of 1926.

Against this very serious consideration that perhaps Restoration payments would be more prolonged and more burdensome than anticipated, there might be placed, perhaps, the receipt of Reparation payments from Germany.

It will be remembered that it was at the opening of 1923 that France had marched into the Ruhr, seizing "gages productifs" in default of German payments on the agreed scale.

[1] cf. *The Times*, November 13, 1924, p. 15.

The reaction in French finance had been unexpected. It caused the entire cessation of Reparation payments by Germany. It deprived the Lorraine iron industry of its normal and necessary supplies of coke. It entailed a large direct expenditure from the French Exchequer. Worst of all, it set finally in motion in Germany the unparalleled mark depreciation, so that in April 1923 the great catastrophe had got finally under way. At last, in October 1923, France had had to reckon with a conflagration, and that other train of events opened which led to the Dawes Settlement of 1924.

" Le fantôme des Réparations ! " A phantom indeed, compared with the solid hopes raised when the Reparation Commission announced long ago that it had by a unanimous decision assessed the proper amount of German indebtedness at 132 milliards of gold marks, i.e. £6,600,000,000. Of this amount the share of France, in a well-ordered world, would have been 52 per cent. according to the ratio established at Spa in 1920.

But would not the Dawes plan of April

1924, which was accepted a little later by the Agreement of London, bring in something substantial at last to the French Treasury?

The Dawes plan proceeded upon the logical assumption that, in order to extract some of the long-lost Reparations out of Germany, it is necessary, as it were, to pump a little prosperity into that land. Or, as the Report itself stated, "the aim of the plan is to set up machinery to provide the largest annual payments from Germany." [1] This stage was prescribed to last for four years starting from 1924, being subdivided for the purpose of the plan into a Budget moratorium period of two years and a transition period of two years more. "We believe," the Report runs, "that at the end of the fiscal year 1928–29 the financial and economic situation of Germany will have returned to a normal state." [2]

By means partly of foreign loans and railway bonds, 1,000 million gold marks was to be obtained from Germany in the first year, though not all was to be taken out; in the second year,

[1] Reports of the Experts Committee, Cmd. 2105, 1924, p. 11.
[2] *Ibid.*, p. 27.

1,220 millions, arising from railway, industrial, and budgetary contributions; in the third year, 1,200 millions from the above sources, together with a transport tax; and in the fourth year, 1,750 millions from much the same sources. The standard year is reached in the fifth year with a total contribution from Germany of 2,500 million gold marks, and thereafter the same sums annually, plus a supplement computed according to an arranged index of prosperity.

How much would France receive under these prospective payments? That was a very pertinent question for the hard-pushed financiers of 1924. At first, the sum of 800 million francs only, or 10 millions sterling at the exchange of 80 francs to the £, was inserted in the Budget of 1925 as introduced in the autumn of 1924. This was raised rather speculatively to one milliard francs a little later. Speaking in November 1924, the French Prime Minister could declare that "by the Agreement of London we have secured the execution of the Dawes plan, a plan characterised both by pacification and by realism, and conceived and applied with the concurrence of the United States, a plan which has already enabled us to insert in the French Budget, even during the moratorium period, a sum totalling one milliard francs." But what was that compared with the vast sum mentioned above as already dispensed, or contracted to be paid by France, in anticipation of full Reparations?

Even in so grave and anxious a crisis it was impossible to avoid some bewilderment if one watched the extraordinary series of legislative remedies and makeshifts that poured forth in a positive cataract from the Finance Ministry during the closing period of 1924. The French Government showed itself fully alive to the situation and inspired by energy, good-will, and sound intentions. But it must also be confessed that it did not seem able to master the situation.

At one moment in October the Minister of Commerce declared that a main cause of the fall of the franc was that exporters, on receiving credits abroad for their exported goods, preferred to keep those credits in the foreign currency " as a sort of insurance against the fall of the franc." As this was prejudicial to the franc, " an organisation to regulate exchange " would have to be established, with the idea of stopping these purchases of foreign currencies. But the Minister was not very convincing as to why the exporter should consent at all to export on these terms. Or, again, was not the State expenditure too high? Doubtless; then hasten to cut down the numbers of the State employees. Accordingly, the Minister of Finance announced in November that he was reducing the staff of his own department by no less than 2,028 officials. Yet, when one looked into his plans with a critical eye, it transpired that his sweeping economy would operate only as existing officials made way from old age or in the ordinary course of service.

But above all let us hasten to reduce the cost of living! And here innumerable ingenious experiments shot like meteors of light through the darkening hours. The only trouble was that they were apt to clash fatally with each other and to descend in not very luminous dust.

First and foremost was the wheat problem and the resultant cost of bread, that article of which the great Goethe used to say that by its universal popularity it had created the unity of France itself. Bread had risen in six months by 26 per cent., from 1·15 to 1·45 francs for the kilo of 2 lbs.

Since 1913 the area under wheat cultivation had diminished by more than one million hectares, i.e. two and a half million acres, even including the new lands of Alsace and Lorraine. Besides this, the cultivation of the 5½ million hectares, or somewhat less, which remained under wheat had deteriorated. As the Prime Minister now pointed out, "the area under wheat is becoming reduced : prairie land is on the increase. This is a very grave fact, and is comparable to the movement which has modified the economic structure of Great Britain. It is a fact which might well, in becoming more widespread, upset the very balance of France, for the force of France lies in the fact that, before all and above all, she is a cultivated field. This is all the more serious since we can only buy the millions of tons which we require at the expense of our franc exchange."[1]

To meet this serious situation plans sprouted more readily than the wheat itself. It was proposed to cut down the duty on wheat. At the opening of 1924 the duty had stood at 14 francs to the quintal. At that date Parliament, under pressure from the consumers, had halved the duty at a stroke, but only until the succeeding August. In August the duty sprang back to its original figure. But if that duty was now again to be reduced or abolished in the interests of the consumers, what terrible consequences, it was said, would arise for the farming community. There was already a flight from the land. Was France to become wholly urbanised? Her population, instead of being predominantly agricultural, was now becoming divided half and half between town and country. So the agricultural interest prevailed and the duty stood.

Another bewildered and bewildering plan was to fix the price. Admittedly, it would be impossible to fix the price of wheat, which was

[1] M. Herriot: speech at Rodez, November 10, 1924.

fundamentally regulated on an international basis. But why not do the next best thing and fix the price of flour?

This was done, and the plan failed forthwith. For the millers refused to deliver flour to the bakers at the price fixed, with the consequence of a sudden rise in the cost of bread.

Then, failing the possibility of fixing a low price for flour, the Government attempted to handle the price of bread itself. An *office des céréales panifiables* was established which now issued, somewhat timidly, a "semi-official quotation" for flour after agreement with the millers, and, on the basis of this price, which was really little else than the market price of flour, the price of bread was further regulated by decree. But, as the price of flour bounded forward, so bread bounded after it, carrying the chain of official decrees dangling tamely and uselessly at its heels. In face of these irresistible forces even the creation of a special body to fight the cost of living, termed the Superior Consultative Committee for Commerce and Living, might as well lay down its arms.

At last, in November, the Government hit upon a final plan. They conceived the notion of settling the matter by introducing a Bill into Parliament, making it a punishable offence "to sell or attempt to sell above the regular market price," or to do the same "at an exaggerated price." But alas for the fallibility of human Bills! The measure was referred to a Commission of the Chamber who found almost unanimously, after mature examination, that nobody could even ascertain what "regular" or "exaggerated" meant.

Thus, as 1924 ended, the spectacle presented itself of an active and patriotic Government struggling like a Laocoön against the twining serpents of economic adversity, but all in vain.

So, as 1925 opened and proceeded, the Cartel des Gauches, the ruling combination of the parties who formed the majority in Parliament, found itself exposed to the most galling criticism directed upon its financial policy by that Bloc National which it had superseded in the preceeding May. "No reform, or improvement in any direction; on the contrary, the economic crisis grows worse and a financial crisis is threatened. Bread is going up, and the franc is going down; nothing practical has been done to reduce the cost of living, which increases daily. The Budget is in difficulties, and no one knows when it will be voted. The parties of disorder have been encouraged; traitors and deserters have been amnestied; Bolshevist propaganda has been given a free hand. In foreign affairs the Ruhr has been abandoned. The Soviet Government, now that its representative is installed in Paris, makes it clear that French investors in Russian loans are going to lose their money; and, to crown all, France's creditors are becoming more pressing." [1]

And then, as "la tourmente" swelled forth into the calculations of chaos and into arithmetic gone wild, a few words were uttered in a different key. A whisper ran from Mamers. A few words only. "The hour has come for a Great Penitence."

These words were the words of "Catiline."

[1] *The Times*, January 13, 1925.

CHAPTER XII

THE CRISIS IN FULL BLAST, 1925

"Magnifique pays que cette France, dont la prospérité répare à elle seule toutes les fautes des hommes. Ils ont beau faire; ils ne viendront pas à bout de la ruiner, et lorsque l'ouragan des folies a passé, lorsque le feu des passions criminelles s'est éteint, la voilà qu'elle ressort de dessous ses décombres aussi opulente que jamais. Son riche sol est travaillé sans cesse par l'intérêt personnel, un beau climat la vivifie, et le même sang bouillonnant qui a fait tant de vaillants soldats anime tous les genres d'industrie . . . N'abusez pas de tant d'avantages!"—Necker, *Dernières Vues Politiques*, 1802.

As the year 1925 opened and proceeded, the Financial Crisis increased in intensity.

The year 1924 had witnessed the opening of trouble in an acute shape. It could all be summarised by saying that, as the State called for more loans and as the French lenders had buttoned up their pockets, ways and means had to be sought elsewhere at all desperate costs. The year had commenced with the failure of a Crédit National Loan. Then, as more francs were issued and as their value fell, it was deemed of prime necessity to bolster up the exchange. Invocations were addressed to the American Zeus, and, at his nod in sky-scraping Olympus, golden dollars, at an extravagant rate of charge, were showered down into the lap of France. But, apart from the bolstering of the exchange, actual cash was needed to make good the current deficit, so that a costly internal "consolidation" loan was floated, the Treasury in its straits borrowing at 8·50, or more exactly 8·62, per cent. free of tax. Thus the financial history of France during 1924 could be pithily described by a French statesman as "a necrology of loans."

A more cheerful tone, however, prevailed presently when it was announced that the Government had taken steps to frame a Budget for the calendar year 1925 duly balanced with a small surplus, and, what was still more reassuring, comprehensive in its scope. This last adjective implied that all the expenses of the State were now at last actually included in the Budget. Up till now many of these had been slipped sideways into other devious and dubious accounts, which, being extraneous to the Budget, necessarily drew their surreptitious and irregular life from borrowing. Thus it could now be represented that the era of "assainissement," of purification, had dawned at last upon a regenerated financial world.

Unfortunately, however, if one scrutinised the matter with unbiased attention, this gilded colouring quickly faded away. For, to start with, though a small surplus of some millions of francs was presented by the Government, extra expenditure was speedily clapped on, long before the Budget was within sight of passing the Legislature. As the franc fell and prices rose, the public officials had demanded and obtained an extra remuneration of 900 million francs; while the war pensioners and so forth were simultaneously accorded another 800 million francs or more. With these additions to expenditure the surplus swiftly vanished away into a considerable deficit. How was this to be met? By fresh taxes or by fresh borrowing? or by a mixture of both?

From that moment there was waged one of the most amazing contests, one of the most Homeric struggles, over the body of a Budget which even France in her long acquaintance with such engagements has ever known. Five mortal times, month after month during 1925, was that forlorn Budget tossed like a pancake from Chamber to Senate, from Palais Bourbon to the Luxembourg. As it landed upside down after each dispatch, its three or four hundred clauses grew more battered and more breathless at every flight. The revenue side caught it most at one transit : then it was the turn of the expenditure side to suffer. At one moment some 160 clauses fell at a stroke before the axe of the Senate, only to be restored to life for the most part down below. Privilege was fighting. *La fiscalité bossuée par les exceptions*, that immemorial evil which in antique days had lost Gaul to the Cæsars ! *Les féodalités nouvelles*, those feudal forces, so old and so new, which in a later hour had brought the Bourbons to the scaffold, and which may yet threaten the life of the Third Republic !

This conflict was also remarkable in its strictly constitutional aspect as a tug-of-war between the Chamber and the Senate. The Senate had been gaining much financial authority in recent years, since the days, at any rate, when Thiers could define it as only "une Chambre de résistance," or when Jaurès had spoken with bitter scorn of "this senatorial wisdom, wizened, wrinkled and worn out." [1] But, as the years had gone on, the Senate had somehow furbished up its powers, and had sallied forth from the trenches to the assault.

In France the texts of the various Constitutions have consistently denied to the Upper Chamber complete equality in the financial sphere, to the extent of assigning to the Chamber of Deputies the right of "priority." Such was the plain intention of the Charter of 1814, of the Constitution of the July Government, and of the Senatus Consultum of May, 1870. Similarly, in 1875, the National Assembly in framing the new Constitution of the Third Republic ordained that, while the Senate and the Chamber should be generally equal in legislative power, "nevertheless, laws of finance must, in the first instance, be presented to the

[1] Speech in the Chamber, June 12, 1911; *Journal Officiel, Débats*, p. 2348.

Chamber of Deputies and voted thereby." This reserved "priority" for the Chamber, but, if tested and analysed, was vague and indeterminate.

Driving a coach and pair through these limp statutory expressions, the Senate has gradually won back very practical powers in finance. It was much helped in this by the Republican attitude which it adopted during the Boulangist crisis of 1889 and the Nationalist movement of 1900. Besides, it gathered much prestige among the rentiers for its long opposition to an income tax from 1907 to 1914. The war furnished it with fresh opportunities. In 1920 it went to the length of establishing its right to raise the rate of taxes submitted to it,[1] and from that time forward it has asserted its financial power with considerable energy and success.[2]

The proposed expenditure of the Budget Bill was a little over 33 milliards, and its proposed revenue was the same, with a trifling

[1] cf. Rapport Doumer, June 18, 1920, No. 250.

[2] cf. Gaston Jèze, *Cours de Science des Finances*, 6th edition, 1922, p. 246.

surplus of some 13 million francs. But, to the detriment of human hopes and of ministerial declarations, this long-debated Budget was not "comprehensive," or nearly so, after all. Indeed, the Rapporteur Général of the Budget in the Senate had to declare that "between the Treasury and the Budget there is still a difference of several milliards." In plain terms, though the Budget scheme seemed to balance satisfactorily, it was really in deficit by several milliards, and the apparent surplus had been merely obtained by the old, old plan of transferring a number of expensive items out of it. These could only be defrayed, meanwhile, by the established expedient of borrowing.

By borrowing? But how borrow? By what possibility could the State successfully renew those applications to the French public which had proved either so futile or so immensely onerous in 1924? This was the problem which presented itself, regardless of the delays of the Legislature, from the very start of the year 1925.

To alleviate the critical situation, it was announced in February 1925 that yet another huge loan of $100,000,000 was being negotiated in America. But this too time-honoured expedient was presently abandoned.

So another policy had to be launched by the hard-pressed Ministry, and a whole litter of financial measures, five of them at once, was brought forward, one more original and ingenious than the next. They were chiefly aimed at accelerating the collection of taxes and at reducing debt.

As an instance of these novel proposals, there was a measure for expediting the collection of the arrears of the War Profits Tax. The firms with such arrears to their debit were to be authorised to issue debentures under State guarantee, the product of such debentures to be employed in payment of the tax arrears. This strange inversion of a tax might obviously end in the result that, if a firm failed to meet its debentures, the loss would fall on the State itself, so that the State would be paying out instead of gathering in.

Another remarkable proposal of the Ministry was the establishment of an *Office National* for the liquidation of debt, a laudable idea indeed, but somewhat paradoxical at a time when the great object of the hour was to find fresh ways and means in order to cope with the deficit. However, the memorandum introducing the measure made it clear that, apart from 800 million francs normally allotted already to meet certain debt payments falling due, no budgetary contribution for this purpose would be made during the current year. It was adumbrated, however, that future Budget surpluses, whenever they might appear, would be appropriated to this fund. Finally, it was proposed that, from 1926 onwards, 20 per cent. of the Dawes annuities received by France should be used for its endowment.

Thus the scheme for the repayment of debt melted swiftly into the thin air of the future, in company with the American loan.

While such measures were thus being taken, or suggested, in order to meet or mitigate the present need of money, other plans were being adopted which would actually cut the other way. The famous Bordereau des Coupons, or list of customers' securities, kept by the Banks for submission to the revenue authorities, was abolished.

This Bordereau had been established in March 1924, with the excellent object of repressing frauds on the revenue on the part of those who drew such dividends, but prudently refrained from declaring them. Under the provisions of this law, persons cashing dividends on their bearer bonds were first obliged to sign a declaration to that effect for the information of the revenue authorities. This inquisitorial enactment had convulsed the financial and investing world. It was declared on authority that at least 20 milliards of such securities had forthwith been transferred abroad out of reach of the fiscal authorities, while other bond-holders had actually preferred to leave their coupons uncashed rather than run their heads into the official noose.

The Prime Minister now announced surrender to the storm. In the technical phraseology of France, *la mise au nominatif des titres au porteur*, i.e. the registration of bearer bonds, for that was the practical effect of the Bordereau, was swept away. Mélanie, the cook, standing possessed of certain securities, was to have the right henceforth of drawing her dividends without the obligation of writing her name ![1] So Mélanie, the cook, not to mention the bigger people upstairs in the drawing-room, would be safe from the clutches of the tax collector.

It was only too apparent, therefore, that no successful attempt to grapple with the crisis in its broadest aspect was in contemplation. So the franc, the sign and symbol of all things financial, which since the spring of 1924 had exhibited a relative stability in relation to gold, now began to display renewed symptoms of most alarming weakness.

At this moment, not yet too late, there flashed across the brain of some unknown inventor yet another device of singular ingenuity and, as it seemed to some, of positive genius. If people would not lend adequate sums to the State, and if even such methods of tax collection as the Bordereau must be abandoned, why not borrow in the last extremity from the taxpayers themselves ?

[1] M. Herriot, in Chamber of Deputies, February 17, 1925.

The method now adopted in order to compass this extraordinary end was the so-called *chèque-contribution*, or taxes cheque. The idea was to provide ready money for the Treasury by offering a cash premium to any taxpayer who was prepared to defray his direct taxes before even receiving his demand notes. The tax-payers were to be enabled to purchase special taxes cheques proportionate to the total direct taxes paid by them in the preceding year. These cheques were to be sold to the taxpayer at a discount on their nominal value, but were to be utilisable by the holder to the full extent of that value for the purpose of paying the direct taxes when due. By this method, it was estimated, the immediate crisis could be turned, and a large yield from taxes could be anticipated. Suppose, for instance, that a tax-payer purchased a taxes cheque on April 1 in order to pay taxes which would be due on November 1. In that case he would secure a discount which would work out at 8·55 per cent. interest on his advance.

It is not difficult to discern two drawbacks inherent in this notable invention. The payment of direct taxes in France, as elsewhere, has the demerit, from the Treasury point of view, of being distributed irregularly throughout the year. The new method in question would tend to accentuate that inconvenience. But, what is more important, the rate of borrowing thus inflicted upon the Treasury was immensely heavy. The great danger to the State was the incidence and volume of the short-term debt, of which, indeed, no less than 130 milliards was now in existence, and which was falling due in an especially large volume in the course of 1925 itself. But, as the National Defence Bonds carry interest at different rates which vary up to 5 per cent., it was obvious that the taxes cheques would impose a much heavier burden on the national finances than the instrument in vogue. Thus the new taxes cheques were in reality nothing more than a disguised form of short-term bond of a very embarrassing and costly character. Yet in the stress and confusion of the hour the measure passed.

All in vain, however. As February lapsed onwards and March arrived, the British public looking across the Channel could only observe with concern "a perfect tornado of protest from all parts of the country," arising against the various proposals,[1] and could only accept the sombre forecast and conclusion of *The Times*, that "French finance is gradually but surely moving towards an unhappy climax."[2]

That climax was not long delayed.

At the opening of April, long ere the Budget could be passed into law, an economic thunderbolt fell in the political arena and destroyed the Ministry. This destructive missile came from the arsenal of that venerable Titan, born long ago in 1800 from the brain of the mighty Bonaparte.

A confession on behalf of the Bank of France was now issued in the Senate, that it had been in the practice of presenting deceptive balance sheets under the stress of Government compulsion. This statement was accompanied by a corrected balance sheet which showed that, whereas the authorised statutory maximum of bank notes issued to the public was 41 milliards,

[1] *The Economist*, March 21, 1925, p. 547.

[2] *The Times*, leading article, February 20, 1925.

the number issued in reality was 43 milliards. To a critical eye even this seemed to savour of under-statement. At any rate, it was evident that the Government, in its search for ready money, had been squeezing more funds from the Bank than the law allowed.

The Minister of Finance defended himself with vigour and ability. He said that, as long ago as December 1923, the legal limit of advances by the Bank to the Treasury, which, as it stood at that date, constituted a considerable portion of the total authorised issue, had been exceeded by about 1,200 million francs. In June 1924, some days after he himself had come into office in the newly-formed Government of M. Herriot, these "hidden" advances amounted to no less than 2,325 million francs, of which 1,085 millions came direct from the Bank of France, while 1,240 millions had come from other banks. And then he recited impressively all the imperative demands made upon himself since that date for finding money where none was. He did not add, but the Opposition added for him, that he had increased these "hidden" borrowings of the Treasury to over 3 milliards in 1925.

The only practicable measure to be taken now was to introduce and pass a law raising the total legal limit of issue from 41 to 45 milliards, and correspondingly the limit on the advances to the Treasury from 22 to 26 milliards, "with the sole object of regularising the actual facts of the situation."

How was it, we may pause to ask, that this revelation was vouchsafed at this particular juncture of April 1925, and not before? Was it at the promptings of sheer financial virtue, and of the love of abstract economic truth? Do doctored returns sometimes feel remorse in their consciences? Can the soul of Double-Entry experience twinges of that honest doubt which, as Tennyson has told us, is better than half the creeds?

Or, failing such moral considerations, must we suppose that the authorities of the Bank of France, conceiving that a climax of State bankruptcy was imminent, and alarmed in consequence for the security of their extra-legal advances, "blew the gaff"?

In avoidance of so drastic an inquiry into the foibles of financiers or into the bluff of balance sheets, let us ask ourselves whether the Bank of France was not more sinned against that sinning, and was not in substance the victim of unsound financial methods which were not its own.

The State, it may be remembered, had fixed the maximum of the Bank's total note issue at the sum of 41 milliards. This provision, made in 1920, seemed for some years to be sufficient, since, according at any rate to the Bank's returns, the circulation stood considerably below that figure for some time. Thus the year 1923 closed with a circulation a little under 40 milliards. But from that time forward strong pressure began to be exercised upon the Bank for more notes, so that the limit of 41 milliards was being constantly threatened, even according to the published returns.

The reason for this pressure upon the Bank of France was due to two quite separate, and even mutually opposed, forces, acting for the nonce in the same direction. One of these was the great activity of French trade, as manifested during 1924 in a large balance of exports over imports, such as had not been witnessed since 1875. Obviously, active business needed proportionately more of the medium of exchange.

The other force at work was the heavy depreciation in the international value of the franc. Both these influences combined to produce demands for more francs, as indeed the Governor of the Bank himself explained at the opening of 1925. "The general development of production and of business has inevitably provoked demands for currency, of all the more urgency in that the level of prices within France has necessarily risen parallel to the influence exerted by the pressure of the exchange." [1]

It may be added that there was yet a third factor always exerting pressure upon the Bank in the same direction. It was estimated at this date by the best authorities that the French people, with their ingrained habit of hoarding, had stored away 6 milliards out of the total

[1] M. Robineau, address at the General Meeting of the Bank of France, January 1925.

issue. This habit diminished, of course, the effective currency and rendered an increase of it more defensible.

In face of this triple pressure upon it, the Bank had displayed much energy and good-will. It had instituted an active campaign for encouraging the use of cheques in the hope of economising the note issue; it had arranged to withdraw its circulation from the Saar and Madagascar, so as to restrict the circulation outside France and thus to increase it inside without adding to its total; and, lastly, it had raised its rate of discount at the close of 1924 up to 7 per cent., in contravention of the sage maxim of its founder, who had hoped to see inscribed in golden lettering over its doorway that it would discount the bills of all men at 4 per cent. This last act was taken by the Bank with great reluctance. "We had to resign ourselves to it," the Governor explained.

So, as 1925 proceeded, the Bank was increasingly involved in a complicated position. Production and trade legitimately demanded more notes. The Treasury, always in deficit, and unable to borrow otherwise, demanded more notes also. Rather than check trade by a rigid insistence on the legal maximum of 41 milliards, rather than bring the Treasury to bankruptcy by refusing notes above the legal maximum of 22 milliards, the Bank gave way. The unsound requirements of a State in deficit, the sound requirements of a nation in business activity, combined to induce the Bank of France to violate the unsound system of a limited currency imposed upon it by law. A sore imbroglio truly for an old Titan of untarnished repute!

Looking at the matter in another light, the French Treasury, it may be said, had become by gradual degrees the business competitor of the Bank of France. "The Treasury acts, in fact, as an enormous Deposit Bank, absorbing the savings of the public as they are made."[1] And this bad banker was acting on unsound lines.

In order to exhibit as clearly as possible the dangerous character of the Treasury's banking operations, let us summarise its figures for the first six months of 1924. That period is

[1] *The Economist*, April 11, 1925, p. 710.

chosen because it was then that the forces which were now at a climax were gathering head, and indeed were creating the crisis already in being in 1924.

Treasury Receipts for the first half-year of 1924.

	Million francs.
Normal receipts (i.e. State Revenue)	11,911
Exceptional receipts (War Profits, Reparations)	1,144
Borrowed monies	2,901
Extraordinary receipts	282
Total Treasury Receipts	16,238

Treasury Expenses for the first half-year of 1924.

Budgetary expenses	11,856
Special Accounts	235
Advances to Railways	429
Payments to Crédit National	1,381
Miscellaneous charges	1,060
Repayments of National Defence Bonds	126
Repayments of Crédit National Bonds	1,691
Sinking Fund payments, Bank of France	347
Total Treasury Expenses	17,125

Here is an apparent deficit of 887 million francs. Add the balance of former deficits and a small amount for working expenses, and the total deficit was 1,250 million francs.

This summarised statement may enable us to gauge plainly the full danger of the normal

Treasury situation. The Treasury, without any Reserve Fund or working capital of its own, is vulnerable at five points. If the Budget is in arrears or in deficit, the Treasury has to find the money. If there are extra-budgetary Special Accounts, the same applies. If the Railways have to call upon the State for its guarantee, the story repeats itself. Payments to the Crédit National in respect of its advances on behalf of the devastated Departments must be met somehow. If the Bonds of the short-term or floating Debt, as they fall due, exceed the new Bonds subscribed, the Treasury must defray the difference.

We can, then, readily understand how the Ministry of Finance could point out at the end of that particular half-year that "this was the situation which brought about the Crisis at the opening of the year 1924,"[1] and also, it can be confidently added, the consecutive Crisis in 1925.

And it was on the Bank of France, in default of all other succour, that the brunt of this bad banking business fell. True, the Bank of

[1] *Inventaire*, 1924, p. 239.

France could put up its rate of discount in order to check the demand for advances upon the part of the public, and thus increase its capacity for helping the Treasury. But the danger involved in such an action was that the holders of the short-term debt would be then disposed not to renew their advances to the Treasury, if they could obtain a higher rate with the Bank of France. So, by that course of action carried too far, the Bank of France might bring the State itself into bankruptcy.

In the circumstances, as the crisis had deepened, the Bank of France, torn between its patriotic duty to the State, on the one hand, and, on the other, its obligation to the Legislature not to issue notes above the legal limit, chose to infringe the law and to serve the nation. Let us believe that it made its avowal and went to the confessional not merely in order to save its own immediate interests, but also in order to draw the attention of the entire public once for all to the absolute necessity of a new finance.

We touch here at the very core and heart of the Financial Crisis of France.

So, on April 3, 1925, at an all-night sitting of the French Cabinet, the resignation of the Minister of Finance was accepted. At 3 a.m. before dawn on April 4, M. de Monzie was urgently aroused out of slumber, and, two hours later, had accepted to fill the vacant post. This long interval of two hours had been filled by an anxious discussion as to his views on the right official relations between the French Government and the Vatican. For the new Minister had his scruples—he would not be " un Monsieur qui se renie "—even with the golden apple of the Hesperides within his grasp. Must we conclude from this incident that in France statesmen have somewhat softer and more sensitive consciences than our own? For instance, it is not recorded that Mr. Churchill, in accepting the post of Chancellor of the Exchequer, boggled for two hours before dawn as to his exact relations with the Archbishop of Canterbury.

But the Ministry as a whole was doomed. The Financial Crisis of France had broken it, even as, according to M. Poincaré's own admission, it had broken that puissant statesman and his dominant Bloc National on the wheel of the Elections of May 1924.

Nevertheless, the adage that the ruling passion is strong in death never came more true than now. The Government of M. Herriot, and this was vastly to its credit, had always insisted that finance was the master problem, the all in all issue of the day. In Napoleonic parlance, they had always marched towards the sound of the economic guns. The Prime Minister had never ceased to emphasise that necessity with sincere and noble eloquence. Speaking time and again of "these problems which cause anguish to us all," he had insisted that "I shall never allow my country to be swept down the slope which has carried Germany and Austria away." [1]

Coupled, however, with so wise and patriotic a purpose, that Government evinced also a strange proclivity. It cherished a passion, not paralleled by any recorded Ministry, for instantaneous and snapshot fiscal remedies. It was as handy with its infallible cures as a cash chemist at his counter. It effervesced

[1] Speech in Chamber, April 13, 1925.

with potions for its patient, the State. Did the price of bread rise? Then pass an enactment to put it down again. Did the lending public button up its pockets? Then borrow from the Bank. Did the Bank prove restive? Then by all means raise a loan in America. Were the American terms too exacting? Then raise the wind from the taxpayers themselves. Were the taxpayers too backward in coming forward? Then, presto, a volley of five Government measures whizzed past the ears of the distracted Legislature.

It was the same thing even now at this final hour when, even in the austere atmosphere of the Senate, the Ministers on arrival could be greeted as "ces messieurs de la famille," in grim allusion to the formalities observed at funerals.

In plain terms, in accordance with this ruling passion, the Government now tabled their ultimate Bill. One final measure more! The measure in question provided for a Capital Levy, of sorts. It was the Socialist Party, then, who had carried their point in this hour of convulsion, who had rushed the pass, and who had worked their triumphant will upon an expiring Administration.

This measure, which was presented on April 7, began by announcing innocently the opening of subscriptions to an issue of rentes at par carrying 3 per cent. interest. This, so far, was mild enough. But the Bill went on to say, Clause 10, that those income tax payers who did not subscribe to this issue up to a tenth part of their wealth would be subjected to "an exceptional contribution, of which the amount would be equal to that fraction of this tenth part which was not covered by the subscription in question." Delinquency on the part of anyone was accordingly to be made good by a Capital Levy spread over twenty quarterly instalments, the proceeds to be allotted to the reduction of the National Debt.

The Senators, who by this time had been apprised by the Bank of France of its irregular complicity with the Government, and who were further scandalised at the prospect of a Capital Levy, registered a hostile vote against the Government. The Government fell.

Thus the swift torrent of the Financial Crisis had swept away yet another Ministry.

The substance of the matter was that Ministers, after trying all other expedients known or unknown, had hoisted ere they sank something akin to the Red Flag. This anomalous particoloured ensign braves the tempest for a moment. Then, it, too, is sucked under by the stormy mill-race surging along.

CHAPTER XIII

THE RETURN OF M. CAILLAUX, 1925

"Certains politiques n'aperçoivent pas que la pharmacopée financière est infiniment plus réduite que le vulgaire ne l'imagine. C'est vainement qu'on y chercherait un élixir permettant aux peuples de recouvrer en quelques instants la santé que leurs erreurs ont compromise. Il n'est, sur les rayons de la boutique symbolique, qu'un ou deux médicaments, toujours les mêmes, très simples, pénibles à absorber, qui ne donnent de résultats qu'autant que le patient s'y résigne de bon cœur et qu'il se soumet en même temps au régime qui conditionne leur efficacité.

"Travail, économie, voilà le régime! Contributions multiples, imposition terrible de tous les revenus sans exception ni distinction, taxation inexorable de l'opulence, tels sont les remèdes!

"Hors d'eux, tout est chimère."—M. Caillaux, Introduction to Wellhoff's *L'Emprunt Forcé*, 1923.

In his novel *Coningsby* Lord Beaconsfield described the character of Sidonia.

Sidonia was by hereditary talents "prescient of the great financial future of Europe, confident in the fertility of his own genius, in his original views of fiscal subjects, and in his knowledge of national resources."

Besides this, Sidonia was endowed with "a penetrative intellect which, matured by long meditation and assisted by absolute freedom from prejudice, permitted him to fathom, as it were by intuition, the depth of questions apparently the most difficult and profound. He possessed the rare faculty of communicating with precision ideas the most abstruse, and in general a power of expression which arrests and satisfies attention."

This was not all, however, in the complex composition of this occult personage. "There was not an adventurer in Europe with whom he was not familiar. No Minister of State had such communications with secret agents and political spies as Sidonia. He held relations with all the clever outcasts of the world. The catalogue of his acquaintance, in the shape of Greeks, Armenians, Moors, secret Jews, Tartars, Gypsies, wandering Poles, and Carbonari, would throw a curious light on those subterranean agencies of which the world in general knows so little, but which exercise so great an influence on public events."

Suppose France possessed a Sidonia! Would it not be worth while recalling him from exile now that so many recognised financiers had fallen by the way? At any rate, it was useless to enlarge for ever upon the obvious fact of a "crise de confiance," or on the patent necessity for an "assainissement." That something must be done somehow, and that somebody must somewhere be discovered—these were platitudes worn out.

The harsh reality was, that, owing to the compelling stress of the financial crisis, two Finance Ministers had tumbled in a week, and that a powerful Prime Minister with a great majority behind him had vanished likewise, after hoisting a flag which, if not exactly red in colour, was much of that complexion.

The year 1925 was rolling on without a Budget, and the franc was bowing down before sterling. There was a conflict over finance between the Chamber and the Senate. The public, instead of renewing their National Defence Bonds and their Crédit National Bonds as they fell due, were requiring their money. Vast maturities were imminent and impending in the future. The United States and Great Britain were asking for a settlement of the French indebtedness. A huge increase had occurred in the authorised amount of the currency, and the cost of living was rapidly mounting up. The index figure for the price of wholesale articles was 554 for June 1925 as against 100 for July 1914. The returns of national revenue for that same month revealed the lowest total since the preceding August. Meanwhile, the Socialist leader, M. Rénaudel, was repeating the refrain of his lugubrious anthem : " We will take the money where we can find it," " on prendra l'argent où il est."

On our side of the Channel, many a British paterfamilias, who had invested in French rentes, as a nest-egg, you know, for the eldest boy at Eton, was staggered, while discussing his more reliable eggs at breakfast, to read in his *Times* that " statesmen and business men in close touch with the situation are aware that French finance is on the verge of a catastrophe."[1] Such, indeed, was the fact.

How was it that France, the master key to whose politics is generally assumed to be her sense of national danger and her fear of Ger-

[1] June 3, 1925.

many, had not realised, so far, that her financial courses might presently imperil her position in Europe? It was not for want of being told so by her statesmen. Here was M. Herriot himself, the apostle of national reconciliation, speaking, in his capacity as Prime Minister, of France ever living "with a poniard poised at a centimetre from her heart"! Here he was declaring that "monetary peace, financial peace, is the indispensable condition of political peace. If you do not attend to it, beware one day of difficulties which may well result in acts of war."[1]

The usual English reply to so natural an inquiry is that France is essentially a self-contained country, and that purely financial crises do not, for that reason, affect her very much. But this view is based on an incorrect assumption. If we analyse the imports of France during the five years prior to the war, it will appear that no less than 76 per cent. of those imports consisted of food and raw materials. If we bring that calculation up to date, that same ratio increased to no less than 85 per

[1] Speech at the American Club of Paris, March 13, 1925.

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cent. in 1923, and to 87 per cent. in 1924. We must remember, for one thing, that whereas the average number of hectares under all cereals in France during the thirty years before the war was 14,280,000, to-day, even counting in Alsace and Lorraine, it is only 9,590,000 hectares, an immense drop.[1] For another thing, as French industries increase, so France has to buy abroad more cotton, wool, silk, and flax.

So any argument founded on the general idea that France is a self-contained country must be abandoned.

The real reason why financial impolicy has been allowed such headway until now is that its practical result, the devaluation of the franc, has impinged with very different intensities on the various organisms which compose the national economy. In order to make this clear, let us look at the three leading organisms in question. Agriculture heads the list; then in point of numbers comes the State service: while the textile industry, which in all its

[1] Department of Overseas Trade, *Report on Economic Conditions of France*, by Mr. J. R. Cahill, 1924, p. 111.

branches employs about 900,000 workers, constitutes, after agriculture and the State service, the third most important single source of employment in France.

To the agricultural population the policy of constant State borrowings has been by no means disagreeable. Instead of hoarding their money and getting nothing for their pains, they have been able to invest it very readily in National Defence Bonds, and so forth, at a fair rate of interest.

Besides this, it was not unpalatable to them that purchases of food-stuffs by France abroad, in competition with their own produce, should be rendered expensive by the falling franc. Here was an automatic Protectionist tariff devised, if not on their behalf, at least to their advantage, by a wise Providence. True that overhead in the branches they could hear the rushing of new fiscal statutes, a mistral wind of laws. But that would only hurt the townsmen, and, in the Provençal parlance, it was "lou bon vent" for the dwellers on the soil. They did not perceive that even on themselves eventually new "rôles" would be "émis," and that hitherto unheard-of "coefficients" would begin one day to patter down in hail.

The fall in the franc reacted in an opposite manner upon the second great body, that of the State employees, high and low. In France, it is said, these do not have salaries, but only *pourboires.*

In England our legal luminaries cannot live in proper comfort, so they tell us, on their salaries, and even our Prime Ministers must spend their capital, so they aver. But in France the head of the Judicial hierarchy, the First Président of the Cour de Cassation, gets only £350 a year, as does the Procureur Général. In France there are twenty-five Courts of Appeal: the First Président of a provincial Court of Appeal and its Procureur Général get £250 each. Judges of first instance hope in their dreams to attain to the red robe of Councillors, though that position only carries £130 a year.[1] And things are on the same scale all through.

So in silence, but not in satisfaction, the

[1] M. Barthelémy, *Le Gouvernement de la France*, 1924, pp. 187–9.

functionaries of France nibbled at the crumbs of their dwindling emoluments.

Pass now to the textile industry. How did the Financial Crisis act upon it?

The strength of French industrial life arises from the fact that she has never endured a sudden Industrial Revolution, that thing so far more terrible in its permanent effects upon the life and happiness of a people than a Great War. In the middle of the nineteenth century, nearly 100 years after our Industrial Revolution had begun, the population of France was still three-quarters rural and only one-quarter urban. From that date onwards up to 1914 the townward movement was very slow, though uniform, so that each succeeding decade witnessed a gradual transfer of 3 per cent. of the population in that direction. Accordingly, France has been as prudent in industrial change as she has been precipitate in politics.

Besides this, the figures of her Industrial Census of 1896, not repeated since, exhibit another significant fact. At that date out of a total of 575,000 "Industrial Establishments" in France, no less than 534,500 had each less than ten employees, so that France remained the home of the small workshop, of the atelier, of the artist in manufacture.[1] At the outbreak of war only a small fraction of the textile trades was in the form of joint stock companies; the rest were family businesses producing goods of an extreme diversity, high quality, and a beautiful specialisation, which the world will have and is prepared to pay for.

It is true that, since that date, considerable advance has been made in the organisation of joint stock companies in the textile industries, and in each case, whether of cotton, of wool, of silk or of flax, there is a strong central trade organisation. Thus industrial France seized the auspicious moment, as in battle her Foch or her Joffre might do. Her textile industries, already enjoying all the cellular strength derived from family life, have added the organic strength derived from modern organisation.

At the date when the Financial Crisis got under way at the end of 1923, the textile industry was obtaining on its exports, we may

[1] Mr. J. H. Clapham, *Economic Development of France and Germany*, 1815–1914, p. 258.

calculate, about eight times the price that it was getting in 1913 for equal quantities of goods. We arrive at this figure by taking the respective metric weights of the goods exported in 1913 and 1923 and by combining this with the values received as measured in francs. But the franc in 1923 averaged 75.74 to the £. Thus for a given piece of goods in that year France was obtaining from the foreigner eight times more than in 1913, in francs worth each one-third of their former value. This means, in other words, that, in spite of the Financial Crisis and the already serious fall of the franc, the textile industry was obtaining for its exported goods nearly 27 pence sterling for every 10 pence sterling before.

As against this, however, something important must be set. In 1913 the value of the textile raw materials imported was 1,732 million francs. In 1923 that figure was 6,923 million francs.

On the whole, the greatest of French exporting industries, in spite of serious misgivings, had found no acute discomfort in the falling franc.

But by the spring of 1925 other considerations had come into play. Agriculture was losing on its hoarded notes and the value of its short bonds was shaky. The State services were more restless and dissatisfied than ever. The great productive industries, though prosperous, looked with dismay at the lessons of inflation as taught by Germany and Austria. In the words of Dr. Johnson, addressed to Mr. William Drummond on the subject of an Erse Bible, "the efficacy of ignorance has long been tried, and has not produced the consequence expected. Let knowledge, therefore, take its turn."

Such was the opinion of France. Such, at any rate, was the opinion of M. Painlevé, the new Prime Minister, who declared that the country was now faced with the possibility of "an economic catastrophe." The essential business of the hour was to avoid the fall of the franc and to avert that consequential peril, "the amplitude of the floating debt. At each maturity the holders of these bonds can exercise a veritable plebiscite." [1]

[1] M. Painlevé, speech at Autun, August 3, 1925.

So there was a trunk call on the telephone. The Capital rang up Mamers. A voice answered. There was a moment of hesitation, and then the voice replied, "Je marche." Quickly, a big grey car set forth eastwards for Paris. An exiled statesman was coming back.

In order that we should precisely appreciate the nature of the Financial Crisis as it confronted M. Caillaux that April day on his accepting the office of Minister of Finance in the Government of M. Painlevé, let us compare his financial outlook with that which met Sir Robert Peel on accepting office in the autumn of 1841.

Four years after the close of the Great War in 1815, Sir Robert had secured the passing of "Peel's Act" establishing the gold standard, and thus had already earned for himself at the age of thirty-one the praise inscribed upon the tomb of Elizabeth: "Moneta in justum valorem redacta." But that measure had not been sufficient to restore us. Industry, indeed, was stricken, one person out of every eleven was a pauper, and deficits in our national

Budgets were returning as regularly as the swallows.

Sir Robert Peel felt that situation acutely. He decided at length that the crisis could only be met by measures relieving industry of the innumerable fiscal restrictions that shackled it. But primarily, of course, this would only accentuate the deficits by forfeiting revenue. Hence it was essential to impose an income tax. The income tax, if modestly framed, would reap much from acquired or otiose capital, and industry would benefit much on the whole. So in 1842 he struck upon the rock of the national resources. He touched the dead corpse of industry, which sprang upon its feet.

It must be said that the party, which for a season followed him in this departure, was not united at heart. In days gone by, it had applauded Eldon, and had voted the Budgets of Vansittart. But now it realised that all other solutions had been exhausted, and that the strength of England was running out. Here was a statesman who had already decided the monetary question, had established public order by his police, had resolved the immemorial

Anglo-Catholic tangle, and had reorganised the whole range of the penal statutes. So they followed, with murmuring and misgiving, and with footsteps often faltering, him, their indispensable chief. When he appealed to them "not to consent with folded arms to view the annual growth of this mighty evil," the ayes had it.

The economic situation, which confronted the brain of M. Caillaux as he sped eastward in the big car of the Government, was in substance inverse to that presented of old to Sir Robert Peel.

The crisis of France was financial, not industrial, at least so far. But take care. The economic life of a nation cannot permanently proceed in separate compartments. Diseased finance, healthy industry—these are incompatibles.

The French crisis, then, was distinctively financial, and, more, it was monetary, the last phase of bad finance. In 1925 the financial straits of France were as severe as were the industrial straits of England in 1841. Still, financial trouble is, on the whole, a lighter evil than industrial trouble, for, if industry is sound, finance can be made to conform to it, but not vice versa.

But, against this consideration of optimism, there were to be set the most serious anxieties. That special bolt of M. Caillaux, the income tax, had been shot long ago. It was not now a resource in reserve, as it had been to Sir Robert. Something else must be thought of. Yonder in the north-east those once devoured, and now devouring, Departments were needing 25 milliards still.[1] That meant more borrowing.

Further away, beyond the sea, the United States and Great Britain were maintaining their astronomical claims, those constellations boding ever more ominously as the financial night fell. There was the threatening short-term debt now amounting to 130 milliards. There was the franc exchange, the playground of every speculator in the world.

Besides all this, Sir Robert Peel in his day had been the only man of the hour, and his the only policy. Not so now. In France there were others—the Socialists, for instance,

[1] cf. speech of M. Caillaux at his banquet, February 20, 1925.

who had a constructive plan in readiness, the Capital Levy. They were even members, nominally, of the Cartel des Gauches, that combination of four parties upon which the Government itself reposed. *La valse des porte-feuilles !* Perhaps this was only another turn in that eternal dance.

Past Rambouillet, past Versailles the grey car flashed and flew to the gates of Paris. One remembered the phrase of M. Clemenceau, " Caillaux se croit Napoléon." But, after all, what the grey car carried was only a black coat, not a " redingote grise."

The statesman who had so suddenly attained office had experienced a singular career. Born in 1863, he was the son of a distinguished financier, his father having been Minister of Finance in the Broglie Government. Trained in the French financial administration, M. Caillaux had quitted it in 1898 for the Chamber, where he quickly became, next year, Minister of Finance in the Waldeck-Rousseau Administration, a position which he occupied till 1902. Moving from the Centre to the Left he had occupied the same post in

M. Clemenceau's Ministry of 1906 to 1908. The rest of his career we know : his persistent advocacy of fiscal reform : his Premiership in 1911 : his fall in 1912 : his return to the Ministry of Finance in 1913 : his fall in 1914.

Arrested for treason at the instance of M. Clemenceau in 1917, he was acquitted of that charge by the Senate in April 1920, but was convicted at the same time of communicating with the enemy and condemned to three years' imprisonment and the loss of civil rights. He could quote a letter addressed to him by Anatole France denouncing the iniquity of this sentence; and, getting his own back on his arch-enemy, he had summarised M. Clemenceau's policy at Versailles as having secured "the minimum of peace and the maximum of anarchy." A gross scandal, M. Millerand declared, that this "chief of *défaitisme*," that this "protégé of Germany" should now be made, in substance, head of the Government of the Republic.[1]

But, finally, the tide had turned when Marshal Foch had sensationally deigned to

[1] Speech of April 24, 1925.

shake hands with M. Caillaux in public; and so, with this imprimatur upon him, precisely five years after his condemnation, he was again, and for the fourth time, Minister of Finance.

As so often happens in human affairs, and perhaps rather specially in Paris, a considerable sensation is followed by a considerable reaction. Dull things began to cloud the day. The mist of financial facts and figures began to spread. The Budget of 1925, not yet passed, inconveniently insisted upon attention. Even Chartered Accountants emerged, like the Minister, from their exile, and Double Entry, that banished bivalve, crept out of its shell.

It was deadly disappointing to find that, in order to meet the urgent necessities of the hour, the maximum note issue, which early in April had been raised from 41 to 45 milliards, was now stupendously increased in June to no less than 51 milliards, a rise of about £60 million sterling, chiefly in order to provide 6 milliards more for the Treasury, which henceforth could borrow up to 32 milliards from the Bank of France. All this in face of the old stipulation of 1920 that the advance of the Bank to the State was to be annually reduced by 2 milliards!

This was not all. All sorts of disagreeable revelations were now produced in regard to the Budget, still floating up and down the tidal constitutional stream. This much-vaunted Budget, which M. Caillaux had inherited, with its small surplus and its presumed inclusion of all the heads of State expenditure, proved on cross-examination to be really in deficit to the tune of 4 milliards. For it included on the receipts side the Dawes payments, which was improper. It excluded from the expenses side substantial payments for War Pensions and for Posts, Telegraphs, and Telephones, which was more improper still. Bad also that it excluded necessary outlays required by the railway system. Altogether, then, to the eyes of the calculators, that tribe so detested by Edmund Burke, the "balanced" Budget of 1925, so joyously acclaimed at birth by the Ministry of Finance as making "a complete 'assainissement'" and as constituting "a final return to the principle of unity and budgetary equilibrium,"[1] was something of a sham.

The new Minister of Finance tried at first to reconstruct and renovate. But it was too late. The Budget was already four months in arrear. So it must quickly be pushed through the Chambers anyhow, patched up with the presumed Dawes receipts of 1,275 million francs inside it, and sprinkled over with a miscellaneous assortment of new taxes, such as higher levies on agricultural profits and 20 per cent. on the total net revenue of insurance companies.

But it was all highly unsatisfactory. The franc very naturally went on falling. Paterfamilias in London telephoned to his broker to cut his loss on his French nest-egg, and in more epigrammatic Paris people smiled cynically over "a magician without a wand."

Meanwhile, to make matters worse, the very existence of the Government itself began to be threatened. The army of the Government, the Cartel des Gauches, began to break and quit. This was due to the secession of the

[1] *Inventaire*, 1924, p. 21.

Socialists. M. Caillaux himself was a Radical, or, if you like, a Republican of the Left.[1] But a Socialist he was not, and he declined to accept the adoption of a Capital Levy of 10 per cent. on capital, to be used for the redemption of debt, as was urgently pressed upon him by that party in the Cartel. In consequence, as the summer of 1925 proceeded, the Government was in daily and hourly peril, all the more that the Chambers could not, and would not, agree even to pass the Budget such as it was. There was not much of the "redingote grise" in all this, assuredly.

It was in these apparently hopeless circumstances that the resolution and the resource of M. Caillaux shone out in full. Rushing down the crestfallen ranks of his supporters, he encouraged, he argued, he compromised, he suggested, he appealed. He sped like Mercury from the Finance Commission of the Chamber to the Finance Commission of the Senate: from the Chamber to the Senate and vice versa he flew, conquering time and distance,

[1] cf. M. Caillaux's speech at Le Mans, July 11, 1925.

and occupying four places at once. From above he scattered epigrams like superfluous ballast on the heads below. "The financial situation is better than people say, but much more serious than people think." He was like Nicias, as described by Thucydides in the despairing hour of the Syracusan expedition, who, ill and weary himself, having done and said everything, still felt that all that he had done was nothing, and that he had not said half enough.

At the end of June, after thirty-six hours of sleepless exertion, during which he attended a long Ministerial Council, appeared before the Finance Commissions of both Houses, and piloted an important measure not merely through the Chamber but also through the Senate, he was away that Sunday morning to rouse his constituents in a brilliant speech! Incidentally, he put through a contested election for the Senate, and won by an immense majority.

These extraordinary energies, this dauntless demeanour, this aggressive assault on his assailants, began to have their Parliamentary effect.

M. Painlevé, the Prime Minister, waiting in reserve, began secretly to recover political health and strength. If the Socialists would not have him, well, he would move from the Left towards the Right. He would chip off some sections from the old Bloc National, and would renew his plaster with this new cement. And indeed, as July went onward, while the Socialist benches seethed with increasing interruptions, the Moderates of the Right began to steal abashed approving glances at M. Caillaux, and even, with downcast eyes, uttered embarrassed *applaudissements*.

The hour had struck, therefore, for a forward movement, and for constructive finance.

By way of preliminary clearance the system of cheque contributions was abolished, that singular method recently adopted for raising revenue by borrowing from the taxpayer at an exorbitant rate of interest.

Next, a circular was sent to the amazed Ministries warning them to cut down their estimates for 1926, and conveying the unprecedented news that " I have to inform you that it will be impossible for me to agree to your estimates unless they are inspired by a real effort of economy." Such language had scarcely been heard in financial circles since the time when the great Colbert insisted on substituting his "maxime de l'ordre" for the existing "maxime de la confusion."

The next step taken was to reduce the Bank rate from 7 per cent. to 6 per cent. This action, it must be said, met with a certain amount of criticism here. A reliable authority reported accurately that it caused in London "surprise and comment in the market." Our experts considered it to be merely a "political" act of "propaganda," arguing truly that there had been already a considerable rise of the note circulation, and drawing the conclusion from this, not so accurately, that this process should have been checked by a high rate.[1]

The note issue had increased, certainly, but if we study the accounts of the Bank of France they show that the note issue was 44,493 million francs, which was much below the authorised limit of 51 milliards. It must also

[1] cf. the report in *The Economist*, July 11, 1925.

be remembered that a high Bank rate at once creates special difficulties in French finance. For the holders of the maturing debt forthwith apply in large numbers to be paid off by the Treasury, and do not renew, in order to obtain the higher market rate. By this interplay more notes have, after all, to be made available, and thus the raising of the Bank rate is defeated of its purpose. Indeed, this is exactly what happened when the Bank rate was raised at the close of 1924. But besides this consideration there was another. Suppose that it were advisable to raise a loan in order to fund the short-term debt. In that case, as actually was envisaged, it was clearly politic to lower the Bank rate.

The last and most important measure now adopted was to mark down for treatment that old standing enemy, the short-term debt. A loan was authorised to be raised on a novel plan. It was to be in the form of 4 per cent. rentes at par, the subscribers, as at first arranged, to be confined to the existing holders of National Defence Bonds.

These rentes, on the old but very doubtful principle, were to be exempted from taxes, including the general tax on revenue. They were to enjoy a "garantie de change," i.e. in so far as the exchange goes over 95 francs to the £ the holders are recouped the difference in the value of their interest receipts. They are similarly guaranteed as to capital. This was a first step, it seemed, towards a return to the gold standard, and also a long step, if the loan succeeded, towards the diminution of the huge short-term debt. "Courage creates confidence" was the maxim constantly on the lips of the Finance Minister. The dangerous demand for the repayment of maturing National Defence Bonds was suddenly reversed. Rentes went upwards. The loan was acclaimed as judicious. As July ended it was written: "M. Caillaux does seem to have given a touch of the magician's wand to the financial situation in France."[1]

Meanwhile, in that same month, the Minister at last carried into law the Budget of 1925 with its stupendous 321 clauses. It took him till 6 a.m. in the morning of July 13, the

[1] *The Times*, July 31, 1925.

last round being fought over the issue as to whether small traders should be exempt, as proposed by the Socialists, from the Turnover Tax.

For weeks past M. Caillaux had now endured and sustained a continuous fourfold debate on the Budget before the two Finance Commissions and in the two Chambers. At length, he was fairly exhausted, and was dropping with fatigue. Yet ever, as he struggled and staggered to the Tribune, his fighting spirit reasserted itself: his voice reappeared: his fire reopened: and he stoutly carried on into the dawn of day and of victory.

But the "dismal" Science, in her search for economic truth, does not count personalities among her repertory, and, in her jargon, classes them all as "imponderables." She reminds us that in France the life even of the ablest and most useful Minister is a short one: *breves et infaustos Populi Romani amores.*[1]

So Science asks only for facts and figures. Let us provide them, and adjudge them.

In the calendar year 1925 the expenditure

[1] Tacitus, *Annals,* Book II., cap. 41.

of the French Budget, so far as settled by the statute of July, will be, in round figures of francs and in its most summary form, as follows :

	Francs.	Per cent.
Public Debt Services	18,574,000,000	56
State Services, Army, Navy, Civil, etc.	13,214,000,000	40
Expenses of State Monopolies and Revenue collection	1,349,000,000	4
Total	33,137,000,000	100

Notice here that under the heading of Public Debt is included the *dette viagère*, i.e. charges for pensions, both war, civil, naval and military. This constitutes to-day 20·4 per cent. of the whole Public Debt service.

The charge for the internal debt is 73·5 per cent. of the Public Debt charge. The serious feature here is the immense proportion due for National Defence Bonds, Treasury Bonds of over one year, Treasury floating debt, and the Crédit National Bonds. But let us hope that this is a decreasing danger.

The remaining 6·1 per cent. of the Public Debt Service is paid in respect of external "commercial" debt, and is mainly remitted to America.

As regards the second item, State Services, etc., the 12 Civil Ministries account for about 8000 million francs of it. The remaining 5000 million francs go to the Army and Navy Departments, which include the Air Force. Thus, at the present rate of exchange, France is paying £50,000,000 for defence.

If we reckon that this latter figure is an insurance premium paid to safeguard the national income, and that this national income, as estimated for 1924 by the Ministry of Finance, is 125,500 million francs—then it follows that this insurance premium is at the rate of 4 per cent.

Turning to the other side of the national accounts, we may summarise the receipts for 1925 as follows:

	Francs.	Per cent.
Taxation	25,381,000,000	77
State Monopolies and Domain .	3,018,000,000	9
Exceptional Resources . . .	1,605,000,000	5
"Dawes" Receipts, etc . . .	1,275,000,000	4
Sundry Receipts	1,871,000,000	5
Total	33,150,000,000	100

Towards the figure of over 25 milliards supplied by taxation, "direct" taxes contribute about 6 milliards. About half of this 6 milliards is reckoned to come from the impôt général sur le revenu, and most of the balance from its component taxes cédulaires.

These latter taxes, as now officially classified in the Budget, consist of the land tax, in its two branches of "property built on" and "property not built on," the tax on industrial and commercial profits, the tax on agricultural profits, the tax on salaries, pensions, etc., and the tax on non-commercial professions. By far the most important of these taxes in yield is the tax on industrial and commercial profits, which provides over 1·8 milliard francs. Next comes the land tax, yielding altogether about 600 million francs; while the tax on agricultural profits is much the lowest on the list. The important tax on securities, *valeurs mobilières*, yielding about 1·8 milliard is not entered as a direct tax, but figures under a separate heading of its own.

The remainder of the taxation owes its main yield to registration, stamps, and Stock Exchange operations, 6·5 milliards, to the great Business Turnover tax, about 4·4 milliards, and to the Customs and indirect taxes, about 6·4 milliards.

As these taxes are in course of collection, it will be useless to give more exact figures. Nevertheless, those furnished above practically account for the main taxes as estimated, and enable us to observe the general trend of taxation up to date.

This Budget of 1925 has two weak features. On the expenditure side its drawback is that it does not include some items of charge which, as already noted, are included in other accounts.

On the receipts side of the Budget its weakness consists in the last three items, which are all more or less of an uncertain nature. For instance, if we analyse the Exceptional Resources, they are constituted by the Special Tax on War Profits, by the liquidation of War Stocks, and by the excess revenues calculated as likely to accrue over the Budget estimates.

This Budget, looked at as a whole, constitutes a serious burden upon France. The proportion of the national income absorbed by taxation has already been discussed. But the latest inquiry, founded on the computations of the United States National Industrial Conference Board, is as follows :[1]

	Per cent.
France	20·9
Italy	19·2
United States	11·5

Observe that these computations all rest on an uncertain factor, i.e. the total national income in each case. So we must receive them with caution. Did not Thiers say that statistics only enable you to state exactly what you do not know?

Grave and momentous as were the financial problems already crowding upon the attention of the French public, they were rivalled or outstripped, as the year 1925 passed into autumn, by the question of Inter-Allied Indebtedness.

On this latter issue, indeed, depended the whole future of French Finance.

[1] cf. "The Index" of July 1925, quoted in *The Economist*, August 8, 1925, p. 226.

CHAPTER XIV

THE FUTURE OF FRENCH FINANCE

"L'impartialité de l'histoire n'est pas celle du miroir qui reflète seulement les objets. C'est celle du juge qui voit, qui écoute, et qui prononce. Des annales ne sont pas de l'histoire. Pour qu'elle mérite ce nom, il lui faut une conscience."—Lamartine, *Histoire des Girondins*, Tome I, Livre I, Section I, edition of 1847.

WRITING just before the Revolution, Necker declared that French Public Finance was so complicated that only one or two persons in a generation could understand it. Unluckily for us, a fresh complication—the international one—has been added to it since then.

This we may realise if we recall to memory *The Wealth of Nations*. Towards the close of that work, which Adam Smith published in 1776 and revised last in 1786, the most famous of our economists dealt with the Financial Crisis of France of his day. He argued that wrong taxation was at the root of the evils from which that nation was suffer-ing, and he produced a scheme of fiscal reform for the future. But in his remarkable diagnosis there was no international factor to be taken into reckoning. We are not so fortunate to-day.

Let us, therefore, attempt to weigh in the balance not only the national, but also the international, factors which will decide the future here. Grave and weighty as are the adverse factors, I think that it can be shown that they will be outweighed, in the long run, by the favourable ones.

Prior to the war, France not only possessed great investments abroad, but also was steadily adding to those investments. It may be estimated that, during the twenty years prior to 1914, these increased at the rate of about 1·2 milliard francs on the yearly average. The result was that, when war broke out, France had about 40 milliards invested abroad. From this she was drawing an income of about 2 milliards a year.

Unhappily for France, 11 milliards, or a little over, of this 40 milliards was invested in Russia, and a further substantial amount in the Balkan States, as well as in Austria and in Germany. For the French investor, usually so cautious at home, relishes his "flutter" abroad, like so many other people. Most of this investment has "gone west," or, more geographically, "gone east," in spite of numerous negotiations up to date.[1]

Besides this, France found it necessary to sell some 3·5 milliards of her remaining good foreign securities owing to the exigencies of the war, with the total result that, instead of drawing 2 milliards of revenue from abroad, France now draws, or was drawing very recently, not more than 250 or 300 million francs a year from this source.[2]

The blow that has thus befallen her is that, for the present, her property totalling about £1,600 millions has largely disappeared, or, at any rate, has ceased to yield revenue beyond a small amount. This means a loss to her of upwards of £80 millions a year.

If we would appreciate all that this means, we may recall that we ourselves are about

[1] Return prepared by French Government, per Decree of January 1919.

[2] Calculation authorised by American Institute of Economics, in *Agriculture and the European Market*, by E. G. Nourse.

£80 millions worse off than before the war, in relation to the United States. This is to be accounted for by adding the full eventual charge of the Baldwin Settlement to the loss which we have sustained from selling our £800 millions worth of American securities.

These losses have proved, naturally, a heavy blow for France, and, besides this forfeiture of her external pre-war fortune, we must reckon in the advances which her Government made, as already referred to, to foreign Governments, and which, generally speaking, have not yet been repaid to her.

We must, however, not suppose that these losses will permanently cripple France. Her Finance Minister, on the occasion of the arrangement of the Morgan loan in 1924, wrote as follows: "France has turned to the development of her foreign trade. . . . This effort has been most successful. The recent development of France's export trade is in a large measure due to the return to productivity of the great industrial centres devastated during the war."[1] These observations have been

[1] Letter of M. Clémentel, November, 1924.

amply borne out since then by the surpluses established in France's visible trade balance. To them we must add such sources of invisible income as shipping receipts and tourist net receipts. From this we can infer that France is already engaged in slowly reconstituting her external investments. It is true that some authorities hold that the favourable trade balance is partly due to the influence of her falling exchange, the argument being, of course, that the decline of the franc constitutes a premium for her exporters. While we may make allowance for this factor, we must still conclude that the opinion above quoted of her Finance Minister holds the field, and that this favourable trade balance arises in substance from her industrial reconstruction.

The next main factor which for seven long years has compromised and embarrassed the future prospects of France is her indebtedness to Great Britain and the United States. According to the French official statement issued at the end of 1924, this consisted of 30,815 million gold francs of "political" debt, and 5,149 million gold francs of "commercial" debt, or a total of about £1,438 millions. Of this over £600 millions was owing to Great Britain and over £800 millions to the United States. This grew as time went on and as unpaid interest was added to the principal.

If we get down at once to bedrock, it may be said that there are two divergent views taken of this problem which, though it may be temporarily adjusted, cannot fail to harass the world for a long time.

The first of these conceptions found its practical expression in the Baldwin Settlement, with its principle that these borrowings constitute plain and unavoidable obligations, and must be paid in full, the sooner the better.

On behalf of this solution it has been most authoritatively urged by the present Chancellor of the Exchequer that "it has placed us in an extraordinarily strong position . . . we are entitled to rest ourselves with confidence upon the position of freedom and independence which we have regained." And Mr. Churchill went on to claim it as "the indispensable forerunner of that consolidation and increasing establishment of our credit throughout the world on which our world-wide trade depends." [1]

Pass we now to the other view of this indebtedness. This is the French view, and here we must have recourse not to the expressions of any statesman or publicist, however eminent, but to the formal argument advanced by the French Ministry of Finance in its Inventory of 1924.

The substance of this argument is that France recognises these obligations of hers to the United States and to Great Britain, and that "her signature will always be sacred in her eyes." But justice and morality imperatively demand that it should be recognised that all these borrowings were made for one common purpose, and therefore "should be apportioned among the Allied States relatively to the wealth of each, and without taking account of the particular engagements imposed by the necessities of the moment. Thus only

[1] Mr. Churchill, House of Commons, December 10, 1924, *Hansard*, pp. 261–2.

can be realised an equality of sacrifice as between all concerned." [1]

Besides, there is an indissoluble connection, so France feels, between what Germany pays by way of Reparation, and what France can and should pay to her creditors. "Public opinion in France will not admit of our consenting, without a legitimate and corresponding reduction in the settlement of the Inter-Allied debts, to any reduction in that established system of repayment to the initial execution of which the Dawes plan has confined itself." [2]

This fundamental French view that all was done and all these debts incurred for a common purpose had already found its most notable expression in the Balfour Note itself, written two years earlier. "Can the present world situation be looked at only from this narrow financial standpoint? It is true that many of the Allied and Associated Powers are, as between each other, creditors or debtors, or both. But they were, and are, much more. They were partners in the greatest international effort ever made in the cause of free-

[1] *Inventaire*, 1924, pp. 73–4. [2] *Ibid.*, p. 74.

dom; they are still partners in dealing with some, at least, of its results. Their debts were incurred, their loans were made, not for the separate advantage of particular States, but for a great purpose common to all, and that purpose has been, in the main, accomplished."[1]

We may, then, resolve the fundamental French view, whatever may be the terms of any immediate settlement, into the following propositions: (*a*) All these Inter-Allied debts, including the debt of Great Britain to the United States, are technical entries made during the terrible exigencies of a common effort; (*b*) nevertheless, as the French signature has been given to her debts, there is an obligation to pay; (*c*) the extent of this payment upon the part of France must hinge fundamentally upon the operation of the Dawes settlement. For the Dawes receipts must regulate the capacity of France to pay in the future; and also, from the point of view of equity, it would be intolerable that, if Germany failed to make the Dawes payments, Germany, the aggressor, should go free, while France, the victim,

[1] Aug. 1, 1922, Miscellaneous Paper, No. 5, 1922, p. 3.

should continue to pay her debts incurred by her in the common interest of civilisation.

It seems, then, that the future of French finance, in this department of it, is inextricably involved with the Dawes plan, and that therefore France will always hold herself morally free to associate her payments to her Allies with her receipts from Germany.

Now, if we inspect the Dawes plan, we shall find weighty reasons for supposing that it will not produce all that it sets out to furnish.

These reasons may be reduced to two, each stated very briefly. First, the solution of the really critical question as to whether the Allies can transfer these sums from Germany, without upsetting the new currency settlement, is not yet in sight. This difficulty at present is partially veiled by the fact that the moneys needed to defray the cost of the Armies of Occupation and the costs of administering the various Dawes schemes do not require to be sent out of the country. This consideration reduces the extent of the problem without, however, removing it.

The second reason is even more fundamental. Germany has a debit balance on her visible foreign trade, and her invisible exports are small, as compared with old days, to set against that deficiency. Thus we shall be faced eventually with the old difficulty as to how to get all the money out. This problem, no doubt, finds its mitigation in the provisions for payments in kind and in the operation of the Reparation Recovery Acts—a mitigation, but not a solution. Surely, the only real solution will be found to lie in the expansion of world-trade, carrying along with it an increase in Germany's exports, or, more precisely, in a renewal of international demand for the coal, iron, steel and shipping of Germany. But what is that prospect? Ask the coal, the iron, the steel, and the shipping magnates of Great Britain and Germany, who are alike in the same market. Add to this the consideration that Germany's budgetary deficits are apparently on the increase.[1]

It is true that Lord Bradbury has pronounced the receipts under the Dawes plan

[1] cf. *The Times*, City Notes, July 27, 1925.

to be "a very hopeful asset,"[1] but that is not tantamount to saying that they will be discharged in full. And, indeed, he has further expressed the opinion that "it would be unsafe, in view of both economic and political uncertainties, to treat our share of German Reparation as worth more than 50 per cent. of what we should receive if the Dawes annuities were paid and remitted in full."[2]

Further, we must remember that, though the Protocol of the London Agreement was only signed on August 30, 1924, the year had not ended ere our Chancellor of the Exchequer informed the House of Commons that "the Dawes hopes may not be fulfilled for many years."[3] Following this up, the Note of the British Government sent to France in February 1925, on the subject of French debt, lays it down that we must not assume "the full normal yield of the Dawes annuities."

Suppose, therefore, that the Dawes plan only yields 50 per cent. of the full annuities

[1] Speech at Manchester, *The Manchester Guardian*, May 2, 1925.

[2] Letter to *The Times*, May 28, 1925.

[3] Mr. Churchill, House of Commons, December 10, 1924, p. 264.

in 1929 and after. This will be £62½ millions a year. Deduct £11 millions for prior charges. Balance £51½ millions, of which the share of France, under the terms of the London Agreement, would be nearly £27 millions.

If France could obtain that sum, she could balance it against annuities totalling £27 millions payable to ourselves and the United States with due moratoria.

The third danger threatening French finance in the future is the enormous debt charge, equal to about 56 per cent. of the total Budget of 1925, if, on the French plan, we include the *dette viagère*, i.e. annuity debt, consisting of civil and military pensions, etc., and constituting about one-fifth of the total debt charge of 1925. Even this ratio will be swollen if, as is contemplated in the Budgets of the future, all the war pensions charges are to be included. The question of the future is how to diminish this burden, all the more in view of the fact that it includes nothing for the service of the "political" debts of France to Great Britain and the United States.

In 1924 the Ministry of Finance wrote on this subject as follows: "No country could long support so heavy a mortgage on its resources, a mortgage which absorbs the greater part of our present activities in order that the past may be liquidated. The consolidation and extinction of our public debt will become an imperious necessity which we shall have to face. No doubt a start has been made, and some chapters of the Budget allow for the partial liquidation of loans which we have raised. We have shown that the payment in rentes of the tax on war profits has enabled us to make a repayment of about 7 milliards of capital. Our debts to the Crédit National, to the groups of war sufferers, and to the railway companies also provide for a service of annuities which imply an annual repayment of capital. But this effort is totally insufficient, and we should pursue and intensify it with tenacity and vigour."[1]

This excellent resolution has since then been reaffirmed in 1925 by the new Government of M. Painlevé, whose Ministerial declaration on taking office contained a pledge to diminish

[1] *Inventaire*, 1924, p. 254.

the national debt, "which is at present insupportable for a great country desiring to have strong and sound finances." [1]

This aspiration has found its latest expression in the plan announced for the Budget of 1926. According to this scheme a *caisse d'amortissement*, a redemption fund, is to be established. This fund is to be supplied with moneys from two sources, i.e. the Dawes annuities, and the product of "an exceptional revision of the indemnities paid for war losses which can be reckoned to be of the nature of excessive profits." These resources will be used to finance the final reconstruction of the devastated Departments, and to meet the annuities due to the Allies. The bearing of this plan upon any reduction of the debt charge is negative rather than positive. That is to say, the Inter-Allied debt annuities and any fresh charges needed to complete the restoration of the devastated Departments will, under this arrangement, not require to be added to the budgetary debt charge. But no funds will be available at present from this source

[1] Declaration by M. Painlevé, April 21, 1925.

for the reduction of the ordinary internal debt of the State.

We must, however, realise that, as indicated in the above quotation from the Ministry of Finance, there is a certain amortisation of the French debt always in process. It may be considered one of the most difficult problems presented by the French finance accounts to ascertain how much debt repayment is normally in process within the four corners of the ordinary Budget. Nevertheless, it is indispensable to clear up the matter, all the more as it would indicate the lines on which future efforts should proceed.

The process of redemption may first be considered in connection with the "consolidated" and "amortisable" debt. Here the statutory sinking funds have been at work upon the amortisable debt; next, the State from time to time has made purchases of small amounts; then, considerable amounts of these securities have been tendered by way of subscription to new loans; lastly, the proceeds of the War Profits Tax have been used in part for redemption purposes, and also various small lots have occasionally passed into the hands of the State. If we summarise from this angle the French finance accounts during the period of ten years from the outbreak of war, it seems that, owing to these various processes, debt which would have been costing the State to-day an annual charge of 6½ milliards, is now costing it 5 milliards. Of course this process is entirely concealed from view by the enormous simultaneous increase in the debt charge. But it has existed, nevertheless.

A careful examination, however, will warn us not to exaggerate the future effects of this complicated process. For, if we inspect the action of the five factors mentioned above, we shall find that much the most important were provided by subscriptions to new loans and by the redemptions effected by the War Profits Tax. But these factors will presumably cease to operate, let us at least hope so, in the future.

Turning now to the next method of debt redemption involved in the Budget figures, this consists of the annuities payable (*a*) to the Crédit National, (*b*) to the *sinistrés*, war sufferers, (*c*) to the various bodies who have advanced moneys to the State, and (*d*) to the railways.

Much the most important of these are the obligations due by the State to the Crédit National. This institution, it will be remembered, was established in order to take the place of the State in paying a portion of the war damages. To this end it raised moneys by issues of which the interest and capital are made good to it by annuities charged in the State Budget. But if we analyse these annuities so as to ascertain the capital involved in them, as distinguished from the interest, it appears to work out as an annual capital sum, charged in the Budget, of not more than 98,000,000 francs. For these annuities have been largely arranged to run for very long terms, up to 1994 and 1995. Of course there does not enter into consideration here any of the short-term Crédit National issues, a reduction of debt being only available in this case out of Budget surpluses, which have not existed hitherto.

As regards the war sufferers, the State, under the terms of the law of 1920, made an arrangement similar to that with the Crédit National. The war sufferers financed themselves and receive an annuity of 721,400,000 francs voted in the Budget in discharge of those outlays. This runs for thirty years.

The next important class (*c*) consists of a great variety of annuities scattered through the Budget under the various votes, and generally termed *annuités servies par l'État*. These arise from very numerous contracts arranged with different bodies, in order to free the State from the obligation of finding important capital sums, by substituting regular fixed annuities comprising interest and sinking fund against the debt so contracted. Finally, (*d*) there are the railway annuities, which are comprised mainly in the accounts of the Ministry of Finance and of the Ministry of Public Works, involving annuities payable to the railways, most of which are of a long-term nature and terminate in 1950 and 1960.

The conclusion to be drawn here is, that as these annuities mostly run for long terms, no early relief will arise for the Budget from their termination. The capital outstanding in 1924 in respect of each of these classes was in the case of (*a*) about 18½ milliards, of (*b*) about 8¼ milliards, of (*c*) about 12⅓ milliards, and (*d*) about 12¼ milliards.

The next method of debt redemption which has been sometimes operative consists in the repayment by the State of the advances made to it by the Bank of France. But, as already explained, this has broken down in recent years in view of the necessities of the State, so that the Convention of 1920 for the repayment of the State's debt to the Bank at the rate of 2 milliards a year has not been carried out, though there is a small sinking fund normally in operation for this purpose.

Passing to the *dette viagère*, this has been exposed to contradictory influences, as best can be illustrated and explained by a practical example. Between March 1922 and January 1924 the annual charge for these various pensions was, in one direction, diminished mainly owing to the decline in war pensions, and was, in another direction, simultaneously increased mainly by supplements voted in order to meet the increased cost of living. On balance there was a net fall, so it happened. But who can say how future changes in the cost of living may presently operate on this charge?

The last method of redemption practised in current Budgets is that in respect of the "commercial" foreign debt, amounting to about 5,150 million gold francs in July 1924. By the end of 1930 it seems that this sum of about £206 millions will be reduced to about £33 millions. If, however, the intention of the Ministry, as it indicated towards the close of 1924, should be acted upon of reckoning the losses on exchange involved in these payments "among the operations of the Treasury and by the means of the opening of a special account," i.e. if the Government borrows in order to substantiate these losses, then the operation would take on a different aspect from that of a substantial repayment of debt.[1]

How much debt is being actually repaid under the headings just reviewed? The Rapporteur Général report of the Finance Com-

[1] *Inventaire*, 1924, p. 65.

mission of the Senate, in dealing with the figures of the 1924 Budget, stated that in his estimation the capital repayments of debt in 1924 amounted to a little over 2 milliards.[1] This of itself would not be unsatisfactory if we did not remember that in that same year there was a deficit, all things included, as follows : ordinary Budget deficit, plus advances to the Crédit National, plus annuity payments for war losses, totalling about 9 milliards. Also, as the above argument has tended to show, even in this modest repayment of debt there are several unstable factors which cannot assure us of its continuance in the future.

On the whole, it must be concluded under this heading, in words recently written by M. Caillaux, that " no serious effort has been made, no considerable plan has been formulated, for the progressive and bold reduction of the liabilities of the State."[2]

In the future, however, these meagre measures bid fair to be accelerated by a plan

[1] Report of speech in *Temps*, February 22, 1925.

[2] Projet de Loi, etc., document No. 1608, Chamber of Deputies, p. 3.

adumbrated, but not yet fully formulated. Speaking of the intended eventual return to the Gold Standard, the Finance Minister has announced that in that event "lenders to the State will then find their advantage in a lesser but more certain return, which diminution will be exclusively used for the reduction of debt and also for the restoration of the public credit, as well as of that of all other enterprises. There will be operations which will be supplemented by the rearrangement of the Succession duties on a new model, and in which we hope that all persons with property great or small will cooperate." [1]

From the above observations on this important branch of French finance the following conclusions seem to emerge : the normal operations of the French Budget comprise a considerable number of annuity payments which imply debt reduction. These reductions have hitherto made no impression because of the large borrowing simultaneously indulged in. But, as soon as a new amortisation fund can be established and endowed with moneys derived

[1] Projet de Loi, etc., document No. 1608 of 1925, p. 12.

from the Dawes annuities and from levies on the profiteers of the restored Departments, these funds can be employed in avoidance of new borrowing. In that case the annuities will begin to tell. Besides that, the idea seems to be to reorganise the Succession duties and to assign the proceeds thus realised to debt reduction. Add to these methods the difference accruing to the State between its present rate of borrowing and its future rate of borrowing, once it has established the Gold Standard.

There is a fourth and definite danger which in the future might conceivably compromise the public finance of France. It has been shown, in a preceding chapter, that it was the weight of the Armed Peace prior to the war of 1914 which had already begun to break down the fiscal system. The danger now is that the Armed Peace reigning in our day, not to mention the effects of colonial warfare, may exercise a similarly adverse influence on the present structure.

To-day, there are twenty-five European nations who maintain armies. Of these twenty-five, five have adopted, mostly under the compulsion of the Peace Treaties, the voluntary system; six adhere to the militia, or Swiss, system; while the remaining fourteen, France, of course, among them, maintain the compulsory system of army organisation.

France feels, no doubt, that in so unstable and dangerous a Europe she must still rely on the most complete system available; but, subject to that determination, she does not appear disposed to allow the consequent financial obligations to overweight her financial strength. In 1913 she had 766,000 Frenchmen serving in the army; in 1925 that figure can be taken at 435,000. This is because the term of service was reduced from three years to one and a half years, with the promise of carrying the effective reduction to one year. She has aimed at supplementing this decline in her forces by securing less costly troops: 228,000 from North Africa and other of her colonies, not to mention 12,000 of the Foreign Legion.[1] We are told on authority that "military experts consider that the establish-

[1] cf. article by General Sir F. Maurice, "The Armies of Europe in 1925," *Foreign Affairs Review*, July 1925, p. 618.

ment of the French metropolitan army will in the end not be more than 250,000, including the permanent cadres."[1] For economy, no less, perhaps, than military science, seems to dictate the advisability of relying more and more upon a small, but highly trained, metropolitan army. It is calculated that the full realisation of twelve months' service will lead to the reduction of the army from thirty-two to as low as twenty-two divisions.

The fifth, and last, great danger threatening French finance is the uncertain value of the franc. If any of the four dangers hitherto analysed in this chapter were to take charge of the situation, that is, if the favourable trade balance were to be reversed, or if the annuities payable to the United States and to Great Britain were to prove too burdensome, or if the service of the debt or the military charges were, either of them, to break down the Budget, then the franc would be in danger once more. And if the franc were to fall again sharply and seriously, then, to mention

[1] *The Times*, article on "Army Changes in France," November 7, 1924.

no other results than those purely fiscal, the consequential rise in the cost of living would react once more upon the amount of the annuity debt and upon all salaries defrayed from the Budget, and also would, if too accentuated, threaten the renewals of the short-term debt.

Then why not, it may be asked, at once establish the Gold Standard, so as to eliminate this last and comprehensive danger? There is an answer to be made to this proposition. If the dangers recited in the above paragraphs are genuine, and if they threaten the exchange now, will they not equally threaten the exchange on the establishment and proclamation forthwith of that excellent institution, the Gold Standard? For even in the Gold Standard there is no innate magic. It postulates, but does not produce, sound finance; it is the crown, rather than the cause, of financial stability.

In May 1925 M. Caillaux wrote as follows on this subject: "Once the budgetary problem regulated, once the country freed from the task of reconstruction in the liberated Departments, once the problem of the Inter-Allied debts settled—in a word, once all the debit accounts, as yet unsettled, have been cleared up, we shall find ourselves in presence of a crushing internal debt: 150 milliards of consolidated, and 130 milliards of obligations of short, and very short, currency. Nothing to be done, so long as the franc is not stabilised. Everything to be done, from the day that it is stabilised. And stability will not be attained until all the great preliminary operations, which we have sketched out, have been accomplished. Once the franc is stabilised, that entails the possible, the necessary, return to gold." [1]

From this we may gather how it is proposed to regulate the course of events. Although nothing can really be secured till the franc is stabilised, this stabilisation itself can only be attained as a result of the achievement of considerable preliminary reforms. Then the Gold Standard will follow upon the stabilisation of the franc. Thus the order of events will be, financial reform producing stability in the

[1] Projet de Loi, etc., document No. 1608, pp. 11–12.

exchange, and stability in the exchange enabling, in its turn, the establishment of the Gold Standard.

Nevertheless, though this is the avowed aim, it must be certain that France suffers in her credit from this slow advance towards the Gold Standard. Take, for instance, the price to-day of the 5 per cent. ten year Treasury Bonds issued in 1924 and repayable at a premium of 50 per cent. by drawings, which start on a small scale in 1930 and continue crescendo till completed by a large repayment in 1934. The amount of the issue in question is somewhat less than 5 milliards and the bonds are free of all taxes in France. Yet the quotation for this apparently attractive Government Bond is only about 453 francs per 500 franc bond. Here is a bond which, after yielding you well over 5 per cent. free of tax, is repaid to you at the latest in nine years' time with a premium of 50 per cent. Clearly, the cause of the extremely low price resides in the exchange, which, by rendering the value of the franc so doubtful in the future, militates against the attraction provided by the security, and thus is prejudicial to the credit of the issuing Government.

But we must not be peevish with those who serve the people. They have obviously begun to take steps on the upward path by making the Budget of 1926 *un Budget de vérité*, by the early completion, let us hope, of the work of restoring the liberated Departments, and by the settlement, let us hope also, of the Inter-Allied debts. Besides this, there is the more specific measure of utilising American credit for the stabilisation of the franc, and, above all, there is the favourable balance of trade. That France can establish the Gold Standard in the future is surely not in doubt. That the task is arduous is not less certain.

So far, this chapter has reviewed in turn the five great dangers which threaten the public finance of France in the immediate future. Nevertheless, our analysis has led to the conclusion that none of these difficulties should prove too much for France, that all are accompanied by mitigating factors, and that therefore with time and courage they can all be overcome.

Advancing, then, from this position, let us endeavour to estimate how a French Budget can best be framed for the future.

Founding ourselves for that purpose upon the proposals soon to be discussed by the Chambers in regard to the 1926 Budget, we observe that it is proposed to augment it, by "a policy of audacity and considered prudence," to a level of 36 milliards, as opposed to the 33 milliards of the 1925 Budget.

This considerable increase is necessitated by the final incorporation in the Budget of all the charges for war pensions, by similar action as regards Posts, Telegraphs and Telephones, and by allowing for increases due to the rise in prices and to the execution of new undertakings already authorised by law. Thus we are promised a Budget of a really comprehensive character.

Meanwhile, in face of this increased expenditure, the anticipated revenue for 1926 is to be diminished by the exclusion of any Dawes annuities, and by the diminishing yield of the War Profits Tax.

Thus the expenditure, totalling about 36 milliards, set against the decreased revenue will result in an anticipated deficit of 3,460 million francs.

It seems that it has been impossible to cut down expenditure any more at present. As it is, the Minister has knocked off two-thirds of all increases in the estimates presented by the various Departments of State. Thus an imperative necessity prescribes more taxation to the extent of about £34 millions, as francs are measured at the exchange of the time.

To the critic it will be obvious at once that this Budget excludes two items of vast importance, and that therefore it forfeits once more its title to be termed all inclusive of the total outlays of the State. Where are entered the costs of restoring the devastated Departments? And where the annuities, to be arranged, presumably, with the United States and Great Britain?

These outlays are to be set down in a new amortisation fund, which looks not so very unlike that old discarded friend, the Budget of Recoverable Expenditure. Happily this new subsidiary Budget, if we must call it so, is to be fed by more genuine receipts than those which "the phantom of reparations" once flashed in the eyes of a dazzled and deceived Europe. These receipts are to come from the Dawes annuities and from the profiteers of the devastated Departments themselves. A bold, a meritorious, a drastic proposal indeed!

But how is the deficit on the ordinary Budget to be made good? Practically entirely by increases in direct taxation.

In the first place, the effective rate of the general income tax, *impôt général sur le revenu*, is to be progressively increased. Next, there is to be a uniform increase in scheduled taxes on income, *impôts cédulaires*, except in the case of small incomes. The principle aimed at in this case is that taxation shall fall at the rate of 10 per cent. on incomes derived from labour, after an exemption point has been reached; 15 per cent. on incomes derived partly from labour and partly from capital, and 20 per cent. on incomes derived from capital alone.

For instance, take the case of an income derived solely from French securities, even though, technically, this tax is not usually ranked among the so-called scheduled taxes. At present the tax is at the rate of 10 per cent., though the operation of the double décime carries that rate up to 12 per cent. Henceforth it is proposed to abolish the double décime, but to carry the rate up to 20 per cent. This applies to French securities and to foreign securities "abonnées" in France. For foreign securities not "abonnées" the rate would be 25 per cent. This is an example of how the rate will strike incomes derived from capital alone.

Another of the scheduled taxes is that on wages and salaries of a certain amount. Here the rate of tax will be not 20 per cent. but 10 per cent., an example of the effort made to discriminate according to the quality of the income as distinguished from its quantity.

Yet another new principle is sought to be instituted in the taxation of *biens oisifs*, unproductive capital values, such as jewels or collections of rare objects. This is calculated to reach those who to avoid taxation invest in such directions. One plan for assessing this tax is to base it on the insurance premiums paid for such articles.

We are now in a position to state the governing principles which will probably dominate future French Budgets: (1) To meet the added needs of the future, direct taxation is to be resorted to rather than indirect taxation. (2) Generally speaking, it seems to be recognised that a revenue of 7,000 francs constitutes a minimum for existence, though it does not appear from a study of the various scheduled taxes that this limit is strictly recognised throughout. (3) Next to this basic principle of "abattements" comes that of deductions allowed off the taxed income for a wife, 3,000 francs, for each child, 3,000 francs, and for each dependant, 2,000 francs. This is the general principle adopted, if with some variations. (4) Apart from these abatements and reductions, the taxation of scheduled revenues is to be regulated by the amount of personal labour involved in producing them. To some extent this principle is in being already, but it is to be extended and systematised. (5) The taxation of the general revenue, roughly corresponding to our super-tax, will be rendered more generally progressive, and, in fact, more productive than at present. The fixed rate of tax is now applied to different fractions, which increase as the income rises, and thus the progressive nature of the tax, in spite of its fixed rate, is preserved. But this principle of progression has in the past been materially disturbed by the provision whereby the tax paid in the preceding year is deducted from the income submitted to tax in the next.

This serious infringement of the yield of the tax has been well stated by the Rapporteur Général of the Finance Committee of the Chamber in 1924. After pointing out that, when an income attains 550,000 francs per annum, it becomes subject to the total 50 per cent. rate under the statute of 1920—or even 60 per cent. if the double décime of 1924 is counted in—the Rapporteur proceeded : "This system is obscure, it is a matter of very complex calculation to ascertain the real charge imposed upon a given revenue."

Assuming that the 50 per cent. rate is

charged, then the annual effective rate on an income of one million francs, when all family allowances, etc., have been deducted, may be established at, say, 47·5 per cent. for 1924. In the immediately succeeding years the most bewildering fluctuations occur in the rate of tax paid, even though the rate is the same, the income the same, and the family deductions the same. The rates for the first few years of tax paid will be approximately as follows:

1924	47·5 per cent.
1925	19·1 " "
1926	36·0 " "
1927	25·9 " "
1928	32·0 " "

These singular fluctuations are due, of course, to the provision of the law authorising the deduction from a year's revenue of the tax paid in the year before.

It is therefore obvious that in future the yield of the *impôt général* can be regularised and increased.

(6) The taxation of unproductive property in the nature of valuables is to be instituted.

(7) Apart from the direct taxes and the tax on securities, no very important increase of

yield is in immediate prospect from the other ten heads into which the taxes are divided in the Budget accounts, i.e. the assimilated taxes, registration duties, stamp duties, tax on Stock Exchange operations, tax on insurance companies, the *taxe de luxe*, the business turnover tax, the customs duties, the *contributions indirectes*, mainly composed of taxes on drinks and on railway travel, and the taxes on sugar and saccharine. These ten heads of taxation, together with the two heads of direct taxes and the tax on securities, make up the twelve heads of taxation as entered in the Budget. Nor can the State Monopolies, the State Domain, the Miscellaneous Receipts, or the Extraordinary Receipts, be relied upon for any material increase of yield.

It is for this reason, and on these principles, that resort is to be had to direct taxation.

(8) The expenditure side of the account is practically occupied by the service of the debt in all its branches, by the naval and military outlays, and by the costs of the remaining Departments of State.

As regards the latter class of expenditure it seems that, though the Ministry of Finance has made all the cuts possible at present in the 1926 estimates, it has in mind to undertake in future a comprehensive reduction and reorganisation in expenditure. If so, this will assist in some degree the great object which must command the attention of French financiers in the future, the reduction of the burden of the national debt.

In this direction several lines of future advance can be discerned. If the Dawes annuities yield in a satisfactory manner, any surplus over the annuities paid to Great Britain and America might suitably be applied to the reduction of the debt; if the death duties are to be reorganised, some of that yield is to be applied, it seems, to the same purpose; if the Gold Standard can be established and the rate of interest reduced, then the consequent diminution in the interest charges of the short-term debt could be appropriated similarly; and lastly, there is, as already explained, a scattered and miscellaneous debt reduction always in process by the agency of the annuities charged in the Budget votes, and by the operation of the regular statutory redemption of the amortisable loans.

France, whose Parliament found difficulty in accepting the Budget of 1925, and whose people has submitted to the new burdens enacted in 1920 and 1924, may well feel the strain of endorsing these additional, but necessary, calls upon her resources.

Let us, at any rate, even amidst all the anxieties that assail us, seek diligently to comprehend the magnitude of her problems and the way to solve them, animated with all that sympathy which we should feel for a sister people, and with all that confidence in her future which will, I believe, facilitate the accomplishment of her task.

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