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**THE ECONOMIC EFFECTS OF THE  
KOREAN WAR IN FRANCE  
1950 - 1952**

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## Introduction

Five years after the end of the Second World War French agricultural production had regained its level of 1938 while industrial production had surpassed it by 25 per cent. Inflation had been brought under control. Free collective wage bargaining had been introduced in February 1950 and most prices freed from state control. Falling domestic prices had stimulated French exports so that the French current account balance was in surplus apart from with the dollar zone. Schuman's proposal in May 1950 to set up a European Community for coal and steel had crowned this economic success with international political prestige. The OEEC programme of trade liberalisation and limited convertibility of European currencies was finally proceeding after months of tortuous negotiations. European reconstruction seemed to be nearing successful completion.

## I

### French Political and Economic Initiatives after the Korean War

In the months following the Korean War European economies experienced an inflationary boom, followed by a recession and a reversal of the progress made towards liberalising trade, integrating economies and dispensing with American aid. In France the Korean War served to highlight the underlying weaknesses of the French economy which neither the Monnet Plan nor the Schuman Plan had managed to remedy. The major problem in 1950 as in 1946 was the persistent dollar deficit and French dependence on American aid. Although this deficit had declined

as French production had revived, the Ministry of Finance did not consider that it would be eliminated by 1952 when Marshall Aid was scheduled to end. In 1949/50 as much as 30 per cent of all French imports had come from the dollar zone. By 1952/53 it was estimated that these imports could be reduced from 703 million dollars to 350 million dollars but that a deficit of 200 million dollars would still remain, even after the completion of the Monnet Plan. In the view of the Ministry of Finance this dollar deficit was not due to structural problems in the French, or European economy, but rather due to the persistent trade surplus of the United States. Marshall Aid to Europe had not and would not eliminate this surplus. Efforts to cooperate with other European countries to increase investment and improve productivity were not sufficient in themselves to close the dollar gap. What was needed, it was argued, was a wider set of arrangements involving not just Europe and the United States but the rest of the world as well - an aid programme to the rest of the world under Truman's Point Four policy. This could have the effect of developing those economies, increasing their imports from Western Europe in order to balance Western European exports and increasing their exports to the United States to revive triangular trade flows. But not only did this scheme depend on further American aid (although not to Europe) but it also depended on European countries, especially Britain, cooperating rather than competing with each other in trading with the United States and with the rest of the world.<sup>(1)</sup>

The outbreak of the Korean War undermined the scheme from the start. The Ministry of Finance immediately predicted that the price of raw materials would rise as the West started to stockpile. This would benefit Britain and the Sterling Area and would make Britain independent of dollar aid and of Western



Europe. France and the rest of Western Europe, with no strategic goods to export, would become even more dependent on the United States economically - and no longer be able to rely on British support to counterbalance this dependence. Furthermore, if France did not participate in the Anglo-American rearmament effort it would become as castrated militarily and politically as Greece or Turkey. But if France did increase its defence expenditure this would either be at the expense of living standards or of financial and economic stability.<sup>(2)</sup>

Many in France were opposed to further rearmament. Already the French were devoting 7.3 per cent of their GNP to defence, over one third of which was spent fighting an unpopular war in Indochina while Britain, a country whose GNP was 20 per cent higher than that of France was only devoting 6 per cent of its GNP to defence.<sup>(3)</sup> However it made little sense to the Ministry of Finance for all European governments to expand their defence programmes separately. This would only serve to undermine all the progress made since 1945 in terms of achieving price stability and trade liberalisation in Europe.<sup>(4)</sup>

The only solution which would not mean a return to inflation and/or national economic controls was seen to lie in a co-ordinated western defence effort. The Ministry of Finance's thinking in this respect was not dissimilar to Bidault's proposal of Spring 1950. The Atlantic Council would draw up a defence plan which would then be divided up among the member states according to their national income, and resources in manpower and industrial capacity. Thus NATO would become an economic as well as a military organisation. If Germany were not to benefit from this diversion of resources to military purposes in other countries, it would have to participate in this collective rearmament. To safeguard such cooperation the Ministry of



Finance suggested that a series of steps should be taken which would make a return to national rearmament extremely difficult. These were that armaments should be standardised for a western army and not for national armies, that each country should specialise in a product which was not produced elsewhere, that strategic products for the western army should be stockpiled and paid for out of the American military budget rather than from the ERP budget. The counterpart of the "military" dollars could then be paid into a European Investment Bank (which the Ministry of Finance had been trying to set up for some time) and this Bank would then finance both civil and military investment in European countries. France should try to specialise in those military products which had the closest peacetime uses such as cars, tanks and precision instruments. On the other hand, Germany should produce those military items which had no peacetime applications, such as cannons. The diversion of German and British steel for military purposes would, it was hoped, benefit Europe's other steel producers, and especially France. The United States would also stand to benefit from cooperating in this defence effort since it would be able to continue to produce a sufficiently high level of consumer goods to avoid inflation.<sup>(5)</sup>

The British Treasury was not impressed with the French scheme. One objection was the practical one that the government was not in a position to coordinate its defence budget with that of the other members of the Atlantic Pact until parliament had voted the credits. But in view of the tedious and protracted nature of intergovernmental negotiations, the British considered it a most inappropriate mechanism for formulating defence policy in any case. They thought that it was preferable for each country to negotiate its defence expenditure individually with the United States. Both sides of the Atlantic envisaged that

this aid would be available only to cover military production and not any of the other charges arising from rearmament. This would be to the British advantage since they were more interested in increasing military production than the size of their armed forces.(6)

The scheme was not universally popular in France either. Ultimately it meant relinquishing control over the French civil and military investment programmes to an international body and implied the participation of Germany in NATO. It thus encountered the opposition in the first instance of the planners and of the Ministry of Defence who refused to submit details of the French defence programme to the Ministry of Finance. And French public opinion was extremely hostile to the idea of German rearmament in any case.

The United States was similarly sceptical of the French proposal. Its immediate interest was in an expanded defence programme in Europe and in the rearmament of Germany within the Atlantic alliance. The American view was that until all the individual NATO countries' programmes were known the economic and financial implications could not be assessed for the purposes of distributing aid. But in the meantime, the American intention was to press ahead with the creation of military divisions in Germany.(7)

It soon became clear that among the NATO countries France was the only one unwilling to give official support to German rearmament and that within the French government it was the Socialist party which opposed it. In view of this Secretary of State Acheson advised the American government to "press the French very hard in private" while being "as moderate as possible in public".(8) But under pressure the French Minister of Defence, Jules Moch, argued that his only chance of getting the



French Parliament on 17 October 1950 to agree to a defence package which included German rearmament was if they knew precisely how much aid the Americans were prepared to give and how many American divisions would be sent to Europe and when.<sup>(9)</sup> It was thus decided that all the relevant people in France and the United States should meet in Washington in October to study the financial and economic implications of the French rearmament programme and the possibility of American assistance.

These negotiations were preceded by talks in New York between General Vernoux representing the French Ministry of Defence, de Margerie from the Ministry of Finance, Alphand, the French representative on the North Atlantic Council and Spofford - the American President of the Council. Without examining the French budget the Americans made it clear that on the basis of relative prices in France and the United States it was preferable that as much of NATO's needs as possible should be produced in the United States.

Petsche and Moch who joined Alphand in Washington on 15 October rejected any such division of tasks which was based on prices rather than on resources. Moch made it clear to the Americans that the French plan to expand its military equipment programme was fully justified in view of the 15 per cent under-utilisation of French capacity since its peak in 1949. The awkward thing was that this expansion entailed running a budget deficit of about 270,000 million francs in 1951, which the French wanted the Americans to finance. However the Americans considered that if they were to put dollars into the Bank of France for use by the French government it would make no substantive difference to the French economy.<sup>(10)</sup> In effect no more goods would have been made available. So instead of agreeing to such a procedure the United States made it clear that



any aid given to France would have to be justified in terms of actual balance of payments necessities - more specifically in terms of the physical imports needed to support the French rearmament effort and maintain the stability of the French economy. They argued that the French production programme scheduled for 1951 was over-ambitious and that in view of the diversion of resources into the military programme the investment programme should be scaled down. And to boost public morale and win support for the enlarged defence programme they suggested that the budget for low cost housing should be increased.<sup>(11)</sup>

While these interministerial talks were taking place in Washington, three of Schuman's staff informed Bohlen, the American chargé in Paris, on 15 October of Schuman's latest proposal to solve the problem of German rearmament and to thwart the Ministry of Finance's plan. While saying that it had the support of Pleven and Mayer they were most insistent that no hint of the proposal was to reach Moch or Petsche in Washington since neither was likely to agree to it. Briefly stated Schuman was considering making an announcement to the French cabinet on 18 October of a plan for including Germany in a European defence community along the lines of his plan for coal and steel. This entailed setting up a common defence budget and creating a European army in both of which Germany would play a full part - provided that the European Coal and Steel Community had been ratified beforehand. The point of leaking this information to the Americans in advance was to see whether Schuman could count on their support in his anticipated battle in France and in the hope that it would influence the loan negotiations. Acheson's reaction was sympathetic but firmly non-committal and he advised that no such initiative should be made before or during the Defence Ministers' meeting of 28 October.<sup>(12)</sup>

The following day Marshall tackled Moch on the issue of German rearmament. Ignorant of developments in Paris Moch repeated his view that the French people would not countenance German participation in western defence, and would oppose any such proposal made at the meeting of Defence Ministers on 28 October. The knowledge that future American aid to Europe probably depended on such agreement did not sway Moch.(13)

Later that day the Americans announced that in the circumstances all that they were prepared to commit themselves to was the rapid delivery of end items for Indochina and credits of 200 million dollars in the American fiscal year 1950/51 which (due to the different timing of the French fiscal year) only covered six months of the French budget. At the same time they told Petsche that out of the NATO appropriations for the year as a whole they might receive a further 100-200 million dollars from the United States in the second half of 1951. But this was altogether too vague for the French. Not only was the sum involved much less than their anticipated budget deficit of about 770 million dollars, but the Americans had not specified whether it was confined to the military effort within NATO or whether it also extended to Indochina. Nor was Moch clear as to whether the dollars could be used to purchase raw materials but he was soon told that they could not.(14)

When reminded by Petsche of his scheme for a joint budget in NATO the Americans, in the light of Schuman's counter proposal, argued that it was only relevant to the continental European members of NATO. The French, it was claimed, had not given sufficient thought to the problems of coordinating national economic policies in continental Europe which was seen as a prerequisite for the successful operation of the scheme.(15)

The plan announced by Prime Minister Plevin on 24 October



1950 to include German contingents in a European army under a European defence minister with a European budget, sidestepped the entire issue of financing French rearmament within the framework of NATO. It introduced the very division between the continental European members of NATO on the one hand and Britain and the United States on the other, which the Ministry of Finance had tried to prevent and it split the French government.

## II

### The Effects of the Korean War on the French Economy

The problem of preparing the budget for 1951 remained. In November 1950 the Investment Commission which was entrusted with the task of allocating annual civil investment funds was for the first time since its creation unable to reach any agreement. The Budget Ministry argued that increases in defence expenditure would have to be made at the expense of public investment in the basic sectors since they alone had escaped earlier cuts. But opinion was very divided on the wisdom of such a policy. Roger Goetze Directeur du Budget advised the Ministry of Finance that a certain degree of inflation was inevitable in 1951 since resources would certainly not cover expenditure. Others argued quite hopelessly that the only way to maintain the existing level of economic activity in 1951 was with further American aid. Bloch-Lainé opposed an apriori decision to cut basic investment. While he agreed that any increase in public expenditure carried inflationary implications he felt that expenditure should be directed primarily into productive investment capable of increasing national income, and thereby government revenue. In



the end the committee submitted a report consisting of three different hypotheses for investment in reconstruction and modernisation.<sup>(16)</sup> As is clear from the table below the counterpart of American aid was crucial for balancing the investment budget in 1951, but the French government had less confidence in its availability than in any previous year.

Table One  
**Estimates of Expenditure in 1951**  
(thousand million francs)

	A	B	C
Plan	355	333	325
Reconstruction	267	251	245
Total	622	584	570

**Resources Predicted**

Counterpart	100	- none certain
Fiscal Receipts	215	
Interest, German reparations, etc.	50	
Medium/Long Term loans	320	
	<hr/>	
	685	- (10 reserved for PIT)
	<hr/>	
	675	million francs

Source: A.F. B 33508. Figures supplied to Ministry of Finance,  
16 November 1950

The situation was further complicated by the fact that despite repeated requests by both Petsche and Monnet in autumn 1950 for information on the increased military programme in order to gauge its importance for the civil equipment programme in terms of energy, steel, transport and so on, none was forthcoming.(17)

Yet in spite of this uncertainty and in spite of the shortfall in American credits the French pressed ahead with their military and civil investment programmes. Private investment too was stimulated by maintaining low interest rates. The results were not surprising. Consumer goods industries, which had been depressed for so long, now increased at a faster rate than producer goods industries. With the increase in production, imports of raw materials shot up. But since the price of these raw materials had escalated the government had to take several measures to mitigate the adverse effects of this imported inflation which it was felt would soon find its way into retail prices once stocks were run down. It therefore increased the corporation tax from 24 to 34 per cent, increased the production tax by one point, registration fees by 20 per cent and domestic taxes on petrol products by 15 per cent. But compared with the counter-inflationary measures taken in all other European countries, the French ones were very modest. Yet the French economy was much more vulnerable to imported inflation than either the British or the German. Even though imports were a smaller proportion of GNP in France than in the other two, the French economy was more unfavourably placed with respect to raw materials. Except for iron ore and aluminium almost the whole of French industry was dependent on imported supplies. This meant that the higher the level of national production, the greater was the level of imports.(18)



Given the low level of unemployment in the French economy the only way to achieve a substantial increase in defence production without attacking living standards seemed to lie in increasing productivity. Yet as the Ministry of Finance realised this required capital investment beyond the scope of self-financing and opened the perennial problem of capital shortage in France. Since the counterpart of American credits, which had played such a crucial part in financing long-term investment in the basic sectors, could not be counted on after the middle of 1951, some means had to be found of encouraging banks to provide medium/long term loans. Pierre Grimanelli, Director of Economic Programmes, recommended that a private institution should be set up to replace the state as the guarantor of such loans, even if its initial resources would come from public as well as private contributions. A further advantage of setting up such a body was that if the French proposals for a European Investment Bank were to be accepted by OEEC then the French would have a national equivalent already in operation and able to work with it. (19) Such ideas had little bearing on the immediate reality.

By Spring 1951 prices had begun to fall in the United States but no such trend was evident in France. Indeed, French wholesale prices increased from an index of 120 in December 1950 to 130 in February and 134 in March 1951. Under pressure the government agreed to raise the minimum wage by 11.54 per cent in March 1951. This was followed by an increase in the price of those goods still under government control, namely coal, steel and electricity. The increase was on average 15 per cent. (20) These two factors were partly responsible for the fact that inflation rates were higher in France than elsewhere in Western Europe. But they did not account for the fact that prices continued to rise in France throughout the rest of 1951 while

world commodity prices had fallen in Spring 1951.

One school of thought within the Ministry of Finance argued that inflation was mainly due to a shortfall in supply on account of the increased military expenditure and the physical obstacles to an increase in production. This had happened in spite of improvements in productivity, increases in savings and a favourable credit policy which should all have stimulated supply. Other analyses focussed on the inflationary effect of either public investment, or of wage increases.<sup>(21)</sup>

The effect on the balance of payments of trying to run a defence programme which absorbed eleven per cent of French national income, together with maintaining living standards and the civil investment programme had sucked in imports, while higher French prices had made exports uncompetitive. Whereas France had stood as a creditor of the European <sup>p</sup>ayments <sup>u</sup>nion on 31 March 1951 it then ran a deficit in every subsequent month so that by ~~the~~ 31 December 1951 its cumulative deficit was 184 million units of account. This meant that 16 million units of account had to be settled in gold. Of course domestic inflation did not altogether explain the French deficit. The fact that Germany, its main trading partner in the EPU had been forced to reduce its imports to curb its escalating deficit in winter 1950 meant that French exports suffered. A 14,000 million franc trade surplus with Germany in 1950 became a 30,000 million franc deficit in 1951. Then in November 1951 Britain began to restrict imports to cope with its balance of payments deficit, which also hit French exports. The situation with the United States was no better. Whereas the trade deficit with the United States had fallen in 1950 as a result of a cut in dollar imports, it shot up again in 1951 as the demand for imports, particularly of food, coal and raw materials increased. The French continued to place



orders in the United States in the third quarter of 1951 on the assumption that dollar aid would be continued in the fiscal year 1951-52, and were horrified to find that they had to be paid out of French reserves.(22)

It was only when American aid did not materialise in autumn 1951 that the French government really took steps to curb the inflationary pressure. Interest rates were forced up by increasing the discount rate from 2.5 per cent to 3 per cent in October 1951 and to 4 per cent in November. The minimum holdings of Treasury Bonds which commercial banks had been required to hold since 1948 were now to be enforced not only at the end of each month but throughout each month. But these measures were not very successful. Despite the increase in interest rates, borrowing for speculative purposes remained attractive when prices were rising rapidly.

Devaluation was ruled out as a solution since it was feared that this would ruin confidence in the franc and only serve to fuel inflation. Instead the government tightened up on the timing of payment for imports and in November 1951 reduced the allocation of foreign exchange to French tourists.

### III

#### American Aid, NATO and Europe

The reasons for the prolonged inflation in France cannot be found in purely domestic economic explanations. They lay in the French government's determination to increase its defence programme by increasing French production, rather than by importing end items from the United States, and without

sacrificing either domestic consumption or civil investment. The result was a budget deficit in 1951 which was almost twice that of 1950, but also an increase in real wages.

Table Two

**Indices of Import Prices, Cost of Living and Wages  
in France, Britain and the United States,  
1951 & 1952 (first half)**

(First Half 1950 = 100)

		Import Prices	Cost of Living	Money Wages	Real Wages
France:	1951 - 1st half	129	118	125	106
	2nd half	133	129	149	116
	1952 - 1st half	134	136	153	113
U.K.	1951 - 1st half	139	106	108	102
	2nd half	144	113	112	99
	1952 - 1st half	143	118	118	100
U.S.	1951 - 1st half	135	109	110	101
	2nd half	135	111	113	102
	1951 - 1st half	131	112	115	103

Source: United Nations, Governmental Policies concerning  
unemployment, Inflation and Balance of Payments, 1951-52  
(New York, 1952), pp. 20-21.

In response to a NATO questionnaire on total budgetary expenditure the French pointed to the strain which the military programme placed on the French budget and the French economy.



Table Three

Defence expenditure as % of GNP

	1950-51	1951-52 (estimate)	1952-53 (estimate)
U.K.	5.67	10.08	11.88
France	8.32	11.52	14-16

Source: F60 ter 468 Memo 28.7.51.

The average per capita income in France was only 80 per cent of that of Britain and 33 per cent of that of the United States yet fiscal charges in France absorbed 30.3 per cent of GNP compared with 32.9 per cent in Britain and 25 per cent in the United States.<sup>(24)</sup> So the option of meeting the increased defence expenditure from additional fiscal charges was considered to be unacceptable. The preferred solution, even after the unsuccessful financial negotiations with the United States in October 1950, was to reduce the ~~the~~ budgetary deficit with further American credits.

Yet judging by the changes taking place in the administration of American foreign lending the budget for 1951/52 was not expected to model those of previous years. In April 1951 Truman had given the International Security Affairs Committee, set up in January 1951, the authority to advise the State Department on the division of funds as between military end items and economic support. At the same time a Financial and Economic Board had been created within NATO which was expected to work closely with OEEC in order to allocate military production to those countries best suited economically. Whether ECA would continue to have any role was thus called into question and

following from this was the critical issue of the use of local counterpart funds. Truman in his budget message of June 1951 ignored ECA entirely. And the fact that he requested economic aid for Europe in 1951/52 to come out of funds already appropriated rather than from the 2,000 million dollars which ECA had planned for tentatively, indicated that ECA might have no further function.<sup>(25)</sup> Finally, on 10 October 1951 Congress passed legislation abolishing the Economic Co-operation Administration and replacing it with the broader Mutual Security Agency. Appropriations of 4,920,000 million dollars for military assistance and 1,022,000 million dollars for 'defence support' were approved three weeks later although the President could if necessary transfer up to 10 per cent from one fund to the other.<sup>(26)</sup>

But between June and October European governments had no idea what American assistance to expect, what the future relative roles of OEEC and NATO would be nor how the increased defence spending was to be shared. In view of this uncertainty the French government refused to make any great sacrifices in consumption or investment. Indeed in its submission to OEEC in summer 1951 it indicated that consumption was expected to rise quite considerably while the inflationary consequences of this together with increased defence spending were to be met by increased imports partly financed by the United States.<sup>(27)</sup>

This sanguine approach to the problem raised by the defence programme was not shared by Marjolin. In discussing future plans with the British Treasury he stressed that a new initiative was needed from European governments rather than from NATO. Since the United States seemed to accept that the rearmament burden would mean a vast expansion of its productive power, Marjolin was worried that European governments were still thinking in terms of



maintaining 1929 levels of production. This, he felt, could only lead to a widening of the gap between American and European economic power and further doubts about the adequacy of the European defence effort. On the other hand if European economies could grow by about four per cent per year this would enable an adequate defence programme to be implemented as well as ensuring the continued improvement of living standards within a short period. More specifically Marjolin envisaged a four or five year plan covering the whole of Europe but worked out on a country basis which would deal not only with the rearmament programme but also with other sectors of the economy such as housing, coal, steel and timber. He was opposed to making this plan dependent on a new bid for American assistance and wanted it to be a French-British initiative. (28)

The following day at a dinner given by Stikker, Schuman supported the view that rearmament had to come out of increased production rather than from living standards. While financing such production would clearly be a problem he stressed that provided such production was not excessive or unregulated the increased revenue would contribute to further investment. Petsche too was in favour of expanding production in Europe provided that it was rationalised at the same time. (29)

But as these proposals were being discussed the Fourth Republic was experiencing another of its by now fairly typical summer crises of government. This one lasted one month. In the government which Rene Pleven finally succeeded in forming on 8 August 1951, the financial portfolio went not to Maurice Petsche who had held it continuously since January 1949, but to Rene Mayer. Pleven committed his government to a vigorous programme of economic expansion and a rise in wages in line with prices.

When the French put their proposal to OEEC at the end of

August 1951 member governments agreed with the general objective of increasing production in Europe by 25 per cent over the following five years. But where opinion was sharply divided was over whether individual countries should determine the nature of their own efforts to increase production without taking account of the programmes of other countries or whether European production should be rationalised. The British declared that co-operation was impossible especially when the needs of rearmament were not known. The French supported by the Italians and the Germans in particular, argued that any declaration of OEEC should stress the advantages of a common programme in terms of increased living standards. The Swiss who were not members of NATO felt that any political role for OEEC was misplaced while the Dutch stressed that the sacrifices due to rearmament would exceed for a long time any benefits derived from economic expansion. Out of this assortment of contradictory policies a draft document emerged which was much closer to the British position than to the French one. Monnet was furious because he felt that the OEEC document lacked any constructive proposals and endangered France's European policy. Although it referred to coal and steel, it ignored the Coal and Steel Community. If the French government signed the document, Monnet feared that it would give the American government the erroneous impression that France renounced the Coal and Steel Community and the European Army.<sup>(30)</sup> Nor was Monnet alone in his condemnation of the British position. The French Cabinet European Committee found it full of contradictions. On the one hand, Britain wanted OEEC to disappear and its activities to be transferred to NATO where Britain and European countries were supposedly equal partners with the United States. But, on the other hand, even in NATO Britain was opposed to too much co-operation. It preferred to



negotiate bilaterally with the United States but at the same time was not in favour of European countries moving to political or economic union either.<sup>(31)</sup>

But the French policy too was full of contradictions. Both their plan for the Coal and Steel Community and their plan for the European army had divided OEEC and NATO and provided neither an effective political nor economic solution to the problems facing Western Europe.

However, at a meeting of the North Atlantic Council in Ottawa in September 1951 the necessity of coordinating the NATO military programmes with national economic objectives and capabilities was finally recognised. In the first instance a temporary committee of twelve men was set up to investigate how national defence contributions could be increased. On 11 October 1951 the Committee of Wise Men, as it was known, decided to appoint an executive of three to calculate each country's potential contribution to western defence. The three members were Harriman, Monnet and Plowden.

It was not until 10 December that the Three Wise Men were finally able to submit a report to the Committee of Twelve - which detailed how increased rearmament could be reconciled with maintaining living standards. The report divided the western powers into two categories - those which contributed less than the average to defence, such as Belgium, and those which committed more, such as France. The first category was recommended to increase its defence budget - by as much as 50 per cent in Belgium's case. The French were advised to increase their expenditure by 5 per cent while cutting some aspects of their naval and air programmes.<sup>(32)</sup> Overall the report recommended that European, including West German, spending on defence should be increased by 2,800 million dollars over the

period 1952-54. It was felt that this would be possible provided that GNP increased by 14 per cent over the same period. Among the other necessary conditions were adequate supplies of raw materials at stable prices, sufficient manpower, American aid, and the continuation of the EPU.(33)

The United States had promised France 600 million dollars in the financial year 1951-52 of which half was direct aid and half was to be spent in France on defence goods. However by 31 December 1951 American expenditure in France on defence was no more than fifty million dollars. So at Lisbon in February 1952 the United States revised the agreement this time promising 500 million dollars of which 200 million dollars was to purchase military equipment. The French franc counterpart of this 500 million dollars amounted to 175,000 million francs. In return the Americans wanted assurances that the French government would stabilise the economy and that the Schuman Plan and European Army would be ratified.(34)

But this American aid came too late. By February 1952 the French balance of payments position was so serious not only with the dollar area but also with EPU that their quota in the union was being used up. So on 4 and 18 February 1952 the French government took steps to suspend, at first partially, and then completely, all the measures of liberalisation of imports into France from the rest of the EPU. Then in March 1952 it reached an agreement with Belgium whereby France was to become indebted to Belgium instead of to the European Payments Union for 150 million units of account. This was to be repaid over three years and had the advantage to France of avoiding a debt to the Union involving a substantial and immediate gold payment.(35)

ECA advised the Managing Board of EPU not to accept this Franco/Belgian arrangement but to adopt a solution along the



lines of the one for Germany. But since the French were experiencing another government crisis it was not possible for them to produce a plan of action for approval by OEEC nor to offer collateral security in return for any facilities provided by the Union.(36)

On 14 March 1952 the OEEC Council decided to extend a special short-term credit of 150 units of account from the European Payments Union to France. The Managing Board of the EPU summed up the French problem in the following terms:

- the increase in world prices following the outbreak of war in Korea coupled with the fact that French industry had delayed re-stocking in the hope of a fall in prices and consequently had to buy in the worst conditions;
- the deterioration of the French terms of trade;
- the increase in military expenditure in Indochina in 1951;
- the import restrictions imposed, or maintained by a large number of countries in the EPU;
- the deterioration of the international situation and the long delay in arriving at a decision as to France's share in the rearmament of western Europe;
- the fairly rapid rate of public and private investment and the methods used to finance this investment;
- the government's policy on prices, particularly agricultural prices and on wages;
- the error of judgement regarding the nature of the equilibrium reached in France in 1949 and 1950;
- the political uncertainty prevailing (at the end of 1951) and the general belief that prices would continue to increase.

Such an analysis inclined the Managing Board to agree with the French action to end trade liberalisation but advised that

domestic action was necessary in the field of prices and wages policy, credit control and budgetary equilibrium. These they argued would be more effective than measures designed solely to control France's foreign trade and payments.(37)

#### IV

#### The 'Pinay Experiment', March-December 1952

The French government was thus now under the control of both the United States through the counterpart of military aid and the Managing Board of EPU through its emergency credit. No longer could the French refuse to sacrifice either living standards or civil investment in order to finance <sup>its</sup> rearmament programme. The course of action proposed by Faure's government in February 1952 was to raise taxes by 15 per cent in order to balance the budget. But this was opposed in the National Assembly mainly by the Gaullists and the Communists and the government fell on 29 February 1952. Paul Reynaud was subsequently unable to form a government since the socialists refused to work with the Gaullists. Pleven declined the invitation even to try to form a government and it was not until 6 March that Antoine Pinay, (who had voted for Pétain in 1940) was able to form a government.

Pinay's popular appeal was based on his pledge to balance the budget without increasing taxation. He expected that this guarantee would enable him to float a loan - the first since 1949. But his confidence proved to be ill-founded - subscriptions fell far short of expectations and in order to balance the budget he had to cut civil investment and the housing budget. Industrial production declined and the trade deficit worsened.



Whereas France's cumulative deficit in the EPU had amounted to 200 million dollars at the end of 1951, this rose to 625 million dollars by the end of 1952 and exceeded its quota by 105 million dollars. This was in spite of the drastic import restrictions imposed in February 1952. Two-thirds of this deficit was with Britain and was, in the opinion of the French government, due to the trade restrictions imposed by the British in November 1951. As a result French earnings from exports to Britain and the Sterling Area were over 200 million dollars less in 1952 than in 1951. Rather than devalue the franc to alleviate the external deficit Pinay hoped that the British would help by removing quotas on goods exported by France, would increase the tourist allowance, place more armaments orders with French industry and invite the Commonwealth countries to discriminate in France's favour. Even when the British refused to do any of these things Pinay remained reluctant to devalue the franc, since the government considered that it would lead to a loss of confidence in the currency and to a spiralling upwards of prices and wages. While it was clear from the French submission to OEEC that they predicted a large deficit on normal trade for several years they expected this to be offset by a very high level of American military off-shore procurement in France and by ordinary American defence support aid. Their policy for combatting any remaining deficit was to subsidise those exports where it was felt that a lower price would lead to increased sales. (38)

But what really undermined confidence in Pinay was the fact that industrial production stagnated in the second half of 1952. This was mainly in the consumer goods sector where a fall in wholesale prices and a fall in exports reduced business confidence. Public expenditure increased due to the rise in defence <sup>expenditure</sup> from 7.5 per cent of GNP in 1951 to 10.9 per cent in

1952, causing the budget deficit to grow. Thus when Pinay presented his budget for 1953 to the National Assembly in December 1952 it was not accepted and so Pinay resigned.<sup>(39)</sup>

V

Conclusions

The three years following the outbreak of the Korean War were not successful ones for the French economy. French industrial production increased by a mere 9 per cent between Schuman's proposal for a Coal and Steel Community and the end of 1953, while West German industrial production increased by 39 per cent over the same period. It was not until January 1955 that the French felt sufficiently confident to bring the percentage of trade liberalisation back to the level of February 1952. In the meantime the French government had lost the initiative in Europe.

But to attribute this reversal of fortune to the Korean War is to exaggerate the latter's importance. The seeds of change had been sown before Korea. On the one hand prices had begun to rise in France before June 1950 - the wholesale price index increased from 1854 in July 1949 to 2035 in June 1950, and on the other hand calls for German rearmament were circulating long before the Schuman Plan was prepared. The real weakness of French policy, it could be argued, of both the Monnet Plan and the Schuman Plan, lay in their dependence on American financial support. As tables four and five show the counterpart of Marshall Aid was quite crucial in financing the Monnet Plan.



Table Four

**Productive Investment excluding Reconstruction**  
(thousand million francs)

	current francs	fixed francs	of which public finance current francs	fixed francs	% of public finance in total investment
1948	335	546	194	316	58%
1949	499	725	311	451	62%
1950	550	715	356	462	64%
1951	699	756	307	331	44%

Source: A.F. B 33509, Monnet to Pinay, 8 March 1952.

Table Five

**Sources of public finance in productive investment**  
(thousand million fixed francs)

	Counterpart of Marshall Aid	Tax (Exceptional Levy)	Loans & resources of FME	TOTAL	Counterpart as % of total
1948	168	54	94	316	53
1949	328	--	123	451	73
1950	201	3	258	462	43
1951	53	--	278	331	16

Source: ibid.

This left the French economy vulnerable to shifts in American policy (unless the investment programme were to be abandoned before the completion of many projects) and left the French government with little possibility to influence the direction of that policy. French attempts, first by Bidault before the Korean War, and then by the Ministry of Finance to create an 'Atlantic Community', as opposed to a little European one failed. Both the 'Schuman' Plan and the 'Pleven' Plan were responses to this failure. In the short term they offered no solution to France's economic problem. But in the longer term American aid continued until 1958, the plan survived, the French economy continued to be modernised and to grow in the direction of closer integration with 'Little Europe'.



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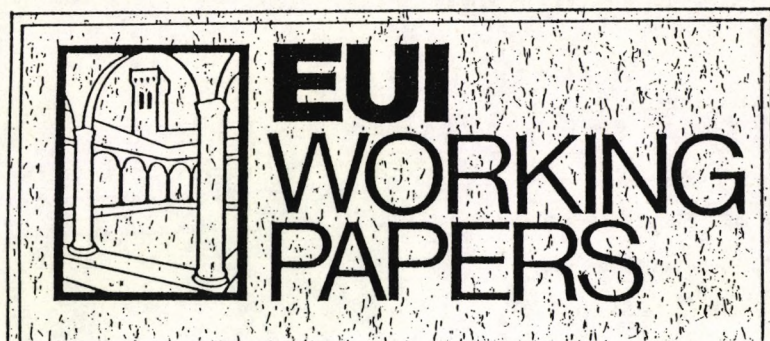
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