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To: Members of the Executive Board

From: The Secretary

Subject: France - Liberalization of Exchange Controls
and Monetary Policy for 1987

The Secretary has received the following communication from
Mrs. Ploix:

I would like to inform the Board that my authorities have just taken new steps concerning the liberalization of exchange controls and monetary policy for 1987. These measures are described in the following statement issued by the Ministry of Economy, Finance and Privatization.

1. Liberalization of Exchange Controls

An important series of new measures to relax foreign exchange controls has just been announced by Mr. Balladur. The implementing regulations will be published shortly.

Two main types of measures have been adopted. Wide-ranging measures are being taken in areas in which the regulations that remained were hindering the competitiveness of our enterprises and banks. New measures have been adopted to extend the considerable freedom individuals have already recovered in the field of investments, travel and current transfers.

1.1 Expanded freedom for enterprises

It has been decided to abolish the control of each individual financial transfer operation connected with external trade--that is, the domiciliation at a bank of imports and exports of goods. Domiciliation at banks involved enterprises and banks in very lengthy, costly paperwork. Its abolition removes a substantial section of the bureaucratic mechanism of exchange control and reduces costs to enterprises. The obligation to declare imports and exports of goods and payments through banks is being retained as a basis for compiling the balance of payments.

1.2 Expanded freedom for banks

1.2.1 Freedom to convert into francs rescheduled foreign
currency loans to hard-pressed foreign countries

Resident banks are now authorized to convert into francs their claims on hard-pressed countries when these countries' debts are rescheduled. Since July 18, 1986, they have been

authorized to denominate in francs their loans of new money to countries experiencing difficulties. This expanded freedom eliminates the disadvantage at which our banks found themselves compared to their foreign counterparts in international financial intermediation in particularly risky operations.

1.2.2 Liberalization of franc loans to nonresidents

The banks are now authorized to grant franc loans to nonresidents up to the amount of the resources in francs received from abroad which they have at their disposal. The arrangements for this authorization will be decided on in concertation with the domestic banks so as to encourage harmonious development of the new operations. It will have no effect on the conduct of our monetary and interest rate policies; but it will make it possible to repatriate to Paris exchange operations which now take place abroad, while eliminating the distortion in international competitiveness which was detrimental to our banks. French banks will thus be able to encourage the growth of international savings denominated in francs.

1.3 Expanded freedom for individuals

The measures adopted eliminate the remaining constraints on current transactions and investment in foreign securities.

1.3.1 Freedom to use credit cards

All the ceilings imposed on use of credit cards by exchange regulations have been abolished.

Individuals will now be able to use their cards freely in settlement of purchases made abroad (purchases of goods intended for import) and expenses of travel abroad, and to withdraw unlimited amounts of cash when abroad.

1.3.2 Simplification of transfers through banks

The ceilings applicable to transfers through banks whose nature is established by substantiating documentation have been abolished. These ceilings applied in particular to transfers of assistance to relatives and to transfers for students abroad.

It will be recalled that since April 15, 1986, transfers of up to F 3,000 per transaction have been permitted without supporting documentation.

1.3.3 Freedom to buy and sell unlisted securities

Prior authorization is no longer required for investment in unlisted foreign securities. The same arrangement has been made

applicable to such investment as has been applied, since the abolition of the devise titre on May 21, 1986, to investment in listed transferable securities denominated in foreign currency.

2. Monetary Policy in 1987

2.1 The monetary target

The money supply will continue to be closely watched. The anticipated growth of GDP value in 1987 is 4.8 percent as a result of a level of economic activity that is more sustained than this year's and of a reduction in the rate of inflation to 2 percent on a through-the-year basis. Our monetary target remains the same: the upper and lower limits for M3 will be 3 and 5 percent, respectively, as they have been this year. M2 will continue to be monitored following the abandonment of a monetary policy based on control of money counterparts. Its target range will be 4-6 percent as against a through-the-year growth of 6.7 percent currently.

2.2 Abolition of credit control

The credit controls that have been in effect continuously for the past 14 years will be abolished as from January 1, 1987. France will thus join the ranks of major industrial countries which follow a monetary policy based on market forces rather than on administrative techniques.

The following specific measures will be taken:

(a) The existing system of progressive and proportional reserve requirements, based on assets, will be abolished and its elimination offset by a corresponding increase in the reserve requirements on liabilities.

(b) Required reserves will be set aside monthly and not quarterly as now; the present deadline of 20 days will be retained until July, then reduced to 15 days.

(c) Up to 75 percent--as against 90 percent today--of excess reserves may be carried forward from month to month, except the first 2 percent, of which 9 percent may be carried forward.

2.3 Money market liberalization

The Bank of France will provide the banks with liquidity or withdraw liquidity from them, in keeping with money supply targets, through auctions followed by marginal adjustments in the market. Beyond that, the market rate will be set freely by fluctuations around the Bank of France's intervention rate in accordance with changes in the banks' needs.

This new method of monetary regulation will specifically result in the following:

(a) As from December 1, fixings will be eliminated, and the Bank of France will publish each day's average rate at noon the following day;

(b) The call money rate will fluctuate freely around the Bank of France's auction rate;

(c) The seven-day pledge rate will be set at about 0.5 per-cent above the call money rate.

(d) The frequency of the Bank of France's auctions will be reduced.

(e) As from March 1, 1987, the authorized periods for the issue of negotiable treasury notes, bank certificates of deposit and treasury bills will be standardized, for maturities of ten days through seven years, subject to specific steps to be taken in order to protect savings by the public.

2.4 Overhaul of prudential rules

The enlargement of freedom and competition must not relegate to the background the rules of sound management without which our banking system cannot grow.

The Banking Commission is working on an extensive reform of the prudential rules governing credit institutions. It will involve the following elements:

(a) Redefinition of the liquidity ratio to include foreign exchange;

(b) Discontinuation of the ratio for use of stable resources and the ratio for nondiscountable medium- and long-term operations;

(c) Institution of a permanent resource ratio intended to limit transformation risk.

This information might be of interest to my colleagues on the Executive Board.

Other Distribution:
Department Heads