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rose by three per cent, however, despite massive layoffs throughout the industry. Chrysler, for example lost 9,000 workers, almost a third of their workforce, while British Leyland cut back even more.

Unable to capitalize on the fall of the pound directly, the British Steel Corporation has carried the cheap British exports situation one step further by announcing a cut of 6 per cent in prices of hot rolled coil and sheet, specifically to undercut foreign rivals, Similarly, BSC will be increasing its stocks 800,000 to one million tons, despite recent cutbacks of 15,000 tons a week, to be able to ensure adequate supplies for orders. BSC is undertaking discussions with the government on the possibility of closing several old and inefficient steelworks to concentrate on newer works being built in other parts of the country.

Government Strategy

The Callaghan government unveiled the spearhead of its economic strategy at a meeting of the National Economic Development Council Feb. 2 which outlined proposals which promise to boost British exports by as much as £36 billion by 1980. Describing the government's proposals as "frankly experimental," Chancellor of the Exchequer Denis Healey and Industry Secretary Eric Varley laid out a program which highlights five industrial sectors for immediate development and stresses the need for increased financial and political aid to other companies to boost their exports.

Named for immediate attention were industrial engines, construction equipment, office machinery, electronic components and domestic electrical appliances on the grounds that 1) these sectors are central to export health; 2) these sectors represent world leaders in their markets and have expresse Britain'sness to expand their market performance; and 3) these are the sectors in which the government can most immediately contribute to industrial growth.

Major responsibility for implementing the government's industrial strategy is being given to the National Enterprise Board to undertake discussions with targetted companies on future investment and organizational plans. The NEB was formed in 1975 with powers to buy up troubled industries and provide financial assistance to firms considered to be critical for national economic health. Already the NEB has announced it will form a government-backed consortium for computer industry to coordinate export and product development projects for participating companies (still to be announced).

Franc Stabilized With Arab Support; Credit Crisis Looms In 1977

FRANCE

The French government has bought precious time for the national economy over the fourth quarter of 1976 and early 1977 by winning the support of its Arab trading partners in stopping the rout of the French franc on the international money markets. The political backdrop to this temporary success is the turnabout in French policy under the direction of Prime Minister Raymond Barre, who has repeatedly stated that French policy would be brought back into alignment with traditional Gaullist calls for expanded trade with the socialist sector and the Third World and for the creation of a gold-backed international monetary system. Arab receptivity to this shift has been expressed in promises of increased investment in French industry through the negotiation of trade deals and in the influx of Arab capital into French money markets. This critical margin of Arab money has played the largest part in stabilizing the franc and taking the immediate pressure off the national economy created by a collapsing currency.

French President Giscard d'Estaing's Jan. 22-26 trip to Saudi Arabia gave some indication of the levels of Arab capital accessible to the French economy. At that time, $3 billion in Saudi financing for the Egyptian-based Arab Military Industry Organization, to be constructed through joint British-French efforts, was firmed up, as well as a 3.5 billion franc housing construction contract. Rumors that the Saudis would also offer France a $5 billion loan to finance expanded trade continue to be circulated by some of Wall Street's leading oil analysts. Simultaneous with these trade-related initiatives, the Arabs have intervened on the international money markets to back the French currency. *Business Week* magazine reported in January that French banks have doubled their intake of Arab "hot money" short-term petrodollar accounts at the rate of $8 billion in new deposits in the last nine months of 1976. At the same time, Arab money has flowed into French government and corporate bonds on a large scale.

The 11 percent depreciation in the effective exchange rate of the French franc during 1976 was a continual source of inflation, resulting in a big jump in the cost of imported raw materials, and accounting for much of France's record 20.5 billion franc trade deficit. By successfully stabilizing the franc, the government has given a temporary boost to business confidence, expressed in a slight upturn of the stock market from its 1976 nadir levels, a 2.4 percent rise in industrial production in November, and a decline in unemployment from 1,041,000 in November to 1,036,900 in December. Significantly, the government was able to let up on its tight credit policies — resulting in a sharp decline of the key call money (interbank) rate from 10.25 to 9.75 percent at the end of January — since defense of the franc no longer requires as high interest rates. The declining call money rate decreases the cost of acquiring short-term

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funds for French banks, improving their profit margins, and allowing for a possible expansion in bank lending to industry.

New Monetary System Necessary

Although the French-Arab dialogue has thus provided the French economy a brief respite, the underlying reality is that, as long as there exists no international monetary framework within which to finance expanded exports, no broad-based recovery is possible. The much-touted government anti-inflation program, the Barre plan, has, since September 1976, actually tended to strangle internal consumption and capital investment. In this respect, the government's shouts of "victory" that the retail price increase was held at .3 percent for December 1976 is a pyrrhic victory which no one expects to be repeated over the next four months. Likewise the whittling of France's foreign trade deficit from 3.82 billion francs in November to 1.32 billion in December is a highly ambiguous omen, based as it is on a 2.3 billion franc cut in agricultural and energy imports.

As the situation shapes up now, the trend toward reduced internal consumption and credit starvation will probably prove to be even more difficult problems than the inflationary disease which the government claims to have solved.

The latest economic indicators from the French statistical institute, the INSEE, underline the point. Although, as noted above, overall production indices jumped 2.4 percent in November, a noticeable declining consumption trend has emerged. Retail sales volume indices declined four points in October, while orders for consumer goods plummeted 30.7 percent from October to November. Throughout 1976, retailers deliberately kept their stocks abnormally low, as a testimony to the tentative character of the consumer spending trend during the year, but from October to November, consumer goods stocks began to accumulate again. This trend was only alleviated slightly by a 2.8 percent pickup in the consumption index for November, in itself a reflection of last minute buying before the Phase One price freeze was lifted at the end of the year.

This developing trend in consumer related sectors is not a new phenomenon to the capital and semi-finished goods sectors, where order books have been shrinking since the first quarter while stocks mount. There is also some indication, according to the latest INSEE report, that a backlog of semi-finished goods stocks is developing despite the decline of activity in this sector.

For the first quarter of 1977, the immediate prospect is for a worsening of this deteriorating condition, especially in the consumer sector, which is the main target of Phase Two of the Barre Plan. Prices should begin to rise somewhat following the lifting of the fall price freeze, although this will be moderated by cutbacks in value-added taxes (VAT) from 20 to 17.6 percent for selected industrial products. The government hopes to contain overall price increases at 6.5 percent. This rising price trend will immediately intersect rising unemployment, as a new round of steel layoffs goes into effect.

Capital Credit Crunch Foreseen

The real crunch, however, will center around the availability of credit for capital investment. The government plan at present is to restrict the overall rate of increase of credit to the economy at 5 percent in 1977, as a partial means of fighting inflation and the growth of the monetary mass. What credit will be granted to industry will be highly selective "critical support" injections, tied

Sales Index 1976

(100 = 1970)

	Retail Sales	New car registrations
Jan	98.5	151.6
Feb	95	129.9
Mar	93.4	168.7
Apr	97.1	180.3
May	96.3	164.9
June	95.9	176.8
July	95.9	142.9
Aug	95	83
Sep	97.2	138.6
Oct	93.5	174.0
Nov		170

Foreign Trade Results 1976

(in bn. of francs)

	Exports	Imports	Balance
Jan	18.97	20.34	- 1.37
Feb	21.0	21.74	- .74
Mar	23.39	24.92	- 1.53
Apr	23.22	24.45	- 1.23
May	23.14	23.97	- .83
June	24.41	24.14	+ .27
July	23.43	23.75	- .32
Aug	17.41	20.14	- 2.73
Sep	22.07	26.16	- 4.09
Oct	24.66	27.21	- 2.55
Nov	24.48	28.30	- 3.82
Dec	24.71	26.03	- 1.32
1976	270.89	291.59	-20.7

Production 1976

(100 = 1970)

	STEEL/IRON	ORG. CHEM.	INORG. CHEM.	ELEC. MACH.
JAN	92	155	102	154
FEB	89	153	106	150
MAR	110	160	111	166
APR	99	145	109	174
MAY	109	152	99	165
JUNE	106	160	110	178
JULY	86	156	89	123
AUG	73	127	89	123
SEP	113	160	109	178
OCT	110	151	107	171

to rationalization schemes, thereby contributing still more to the unemployment problem. As a foretaste of the nature of the government's investment policy, a two billion franc credit has been extended to the nationalized public utilities to assist in financing their 30 billion franc deficit, in exchange for two billion francs in cuts.

Reporting from private industry is even more pessimistic. *L'Usine Nouvelle* reported in January that the rate of increase in credits to the economy peaked at 3.5 percent in 1976, and will drop to 3.1 percent for 1977. Private investments were a pitiful 2 percent for 1976 and projected at 2.4 percent for 1977. State loans to the nationalized firms, normally the biggest share of total investment, will shrink 3 percent in 1977 to a 9.5 percent rate of increase. For the steel sector, this credit situation translated into a slight 2.8 billion francs of credit in 1976, barely sufficient to cover the 2.5 billion interest due on the industry's debt. For basic industry, in particular, this reduced credit is going to debt financing and maintenance of current plant and equipment with no expansion in sight.

French industrialists are keeping close watch on the government's actions in the investment area. To date, Prime Minister Barre has won the support of the major employers' association, the CNPF, on the basis of his Phase One program to plug up the rout of the French franc and to bring inflation under control, but the question of credit to the economy, and the government's flexibility on this issue, is literally a matter of the survival of French industry. In a first test, *Les Echoes* of February 3 reported that the CNPF had appealed to the government for a 20 billion franc program of low interest credit for 1977, which has since been rejected by Prime Minister Barre as inflationary because it would set interest rates at an artificially low level. CNPF spokesman François Ceyrac quickly responded again urging the government to consider lowering interest rates to industry.

On the basis of the internal economy, the government is correct in pointing out that it cannot generate the necessary levels of credit to sustain full productive capacity. The only real means for that level of credit generation is through the development of international trade. Even limited one-shot deals, such as France has successfully negotiated with the socialist sector and the Arab countries recently, are likewise not sufficient to have widespread impact on the entire economy.

Focus on Technology

This is not to minimize the high technology orientation of France's export policy, as outlined by Prime Minister Barre at the conclusion of his mid-January trip to Great Britain. In the forefront of the government's trade program has been a concerted effort to not only ensure France's current supply of oil and related energy sources, but also to proceed with experimental work in nuclear energy. Just last week French President Giscard d'Estaing and West German Chancellor Schmidt defended European exports of nuclear technology to the Third World in the face of heavy U.S. pressure to abandon projects already in the works. As testimony to this commitment to developing nuclear energy, in the past month the Barre government has given the green light for the European project to proceed with construction of the five billion franc Super-Phenix fast breeder reactor project, and negotiated with the Saudi Arabians for construction of a nuclear technology research center.

France's nationalized oil firms, Elf Erap and CFP, have played a very important role in safeguarding France's oil supplies in the medium term until the nuclear-related projects are fully functional, and were no doubt key in the conclusion of a three-year 42 million ton oil deal with Saudi Arabia at the conclusion of President Giscard's trip Jan. 22-26. The terms of the contract agreement will reflect both the Saudi decision to restrict oil price increases to only five percent and the special terms which the French have enjoyed with the Saudi oil producers since 1974 under then Foreign Affairs Minister Michel Jobert. Under these terms, France will get the

Saudi oil for 93 percent of the actual market price. Simultaneous with this supply strategy of the nationalized firms, the government has significantly backed ELF-Erap and CFP on the domestic markets by giving them a bigger percentage cut in total distribution at the expense of Mobil and other U.S. oil multinationals.

Profiles of Key Industrial Sectors

AUTO: The auto industry had a record year in 1976, based in part on sustained consumer spending until the fourth quarter. Total production for the year was 3.4 million vehicles, reflecting a 17 percent increase in automobile production, a 35 percent increase in small utility and truck production, but a marked 21.4 percent decline in heavy trucks. Renault was number one in production with 1.365 million vehicles, followed by Peugeot at 758,000; Citroen at 679,000 and Chrysler France at 510,000. The industry as a whole was able to prevent stockpiling during the course of the year by forcibly keeping stocks low, even creating extended delivery periods when necessary. On the basis of these record production figures for the year, the newly merged Peugeot-Citroen interests showed a consolidated turnover of 35 billion francs. However, the prospects for 1977 are not bright, as auto producers are predicting a sharp curtailing of sales. Investments in 1977 for Peugeot-Citroen and Renault are projected at 2 billion francs at present to cover both improvements in productive capacity and new models.

CHEMICAL: The French chemical industry was literally saved this year by the organic chemicals wing of the sector, which will largely be responsible for the projected record turnover of 90 billion francs in 1976, an increase of 17 percent from the previous year. For chemical fibers, the leading chemical firm Rhône Poulenc suffered a 500 million franc deficit in 1976, while the entire industry had a parallel loss of 500 million francs in the mineral sector, primarily fertilizers. Fertilizers did particularly poorly in 1976, especially following the summer's drought; nitrogenous fertilizer production dropped 14 percent for the year, complex fertilizers 11 percent and superphosphates 13 percent.

The activities of the chemical engineering firm Technip stands in marked contrast to the general deterioration of this industry. In the past two months, Technip has won 6.5 billion francs in trade deals with the Soviet Union and Poland, for construction of three separate petrochemical and related refining and processing complexes. The largest deal is a four billion franc petrochemical refinery project with Poland, signed at the close of 1976. Technip has also just recently signed a one billion franc contract with Qatar for construction of a steam cracking unit which will also have spinoff facilities for production of ammonia.

STEEL: Overall steel production for the year reached 23.2 million tons, a 7.8 percent increase from 1975, but still 14 percent below the levels of two years ago. The hardest hit sector was rolled steel, reflecting the collapse in construction and housing during the year. Plant efficiency for this wing of the industry is currently only 60 percent, and weekly work hours per employee are at a low 32. Sacilor-Sollac, France's number one producer of rolled steel, had a sharp cutback in production to 6.5 million tons out of a total capacity of 9 million. The rate of decline in flat steel production was not as sharp in 1976 in part because of the sustained activity in auto. However, the industry as a whole faces a major debt financing problem in the immediate future. Total industry indebtedness equalled total turnover in 1976, or 33 billion francs. Private investments in 1976 reached scarcely 2.8 billion francs, hardly sufficient to cover 2.5 billion in interest payments due. The outlook for 1977 is even bleaker, with private investments currently projected at two billion francs. In the long term, Sacilor-Sollac and Usinor, the leading flat steel producer, have plans for eliminating close to 12,000 workers from their combined workforce of 90,000. The proposed government bailout plan for the antiquated Lorraine steel industry fits right into the vicious pattern of "rationalization" rather than expansion which will be promoted in the first quarter of 1977. Out of a projected three billion franc investment, one third will go to phasing out 14,000 jobs and the rest to modernizing plant and equipment. Because of the desperateness of the steel situation, the government has relented in backing up a total of seven billion francs in low interest loans in 1977, on the condition that this be used for make-work jobs on the spot and plant "modernization."

Italy Needs Credit Lines To Maintain Recovery

ITALY

A mild economic recovery in Italy resulted in a 12.3 per cent increase in industrial production and a 35.5 per cent increase in exports for 1976. While exports increased by taking advantage of the lira devaluation, however, the devaluation contributed to a 46 per cent increase in the cost of imports as producers were forced to pay higher prices for raw material imports.

These high import costs generated major domestic problems: Italy had the second worst trade deficit in its history; there was massive internal debt accumulation, a 1976 inflation rate of 20.5 per cent, and corresponding discontent from the trade unions in the face of a lowered standard of living.

The Andreotti government has staked everything on the expansion of foreign trade, the only way out of its present economic dilemma.

The Soviet Credit Line

In 1976, 38 percent of Italy's total credit extension was to the Soviet Union; estimates for this year (including a still-to-be-signed $650 million credit line) are that 50