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Structural trends of financial systems and
capital accumulation : France, Germany, Italy.

Giangiaco^o NARDOZZI *

Internal paper



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ABSTRACT

This paper analyzes the evolution of the French, German and Italian financial systems from the mid 1960s until the present day. The analysis concentrates on the structural aspects of the question. References to monetary policy are limited to the minimum necessary to understand the functioning of the three systems. The aim of the paper is to provide a contribution to the evaluation of the three systems' ability to finance capital accumulation. The point of departure is the debate during the 1960s on European financial markets. The results derive from the identification of certain structural distinctions between the three systems. These have then been used to cast light on subsequent developments which are interpreted country by country.

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I. INTRODUCTION

Objectives and Method of Research

A financial system can be considered from a number of different points of view owing to the fact that it performs various different functions.

The present report is primarily concerned with the accumulation of capital. There are two good reasons for this choice. The first arises from the fact that, particularly during the mid 1960s, the three countries to which reference is to be made had had a relatively short history of capitalist development (compared to that of the U.S. and the U.K.). They were therefore characterised by a much higher capacity and need for accumulation. The second derives from the existence of the crisis that has hit, albeit with differing intensities and modalities, all the industrialised countries during the 1970s. The needs of productive restructuring within these countries, require an especial response in the field of investment. The attention of academics and other specialists has consequently been turned to the question of the role that financial system can perform in sustaining this dynamic process of resource reallocation, the central mechanism of which is the investment decisions made by firms.

In recent years, therefore, there has been a return to some of the issues which had received particular attention, in Europe, around the mid-1960s when a number of important studies analysed the relation of financial systems to problems of economic growth (Lamfalussy (a), OECD (a), EEC).

The present report takes the situation pertaining at that period and the results of these studies' contributions as its point of departure. There is a two-fold objective in doing so. In the first place, it is intended to see whether or not the evolution of the three

financial systems has proceeded in the directions that were considered desirable during the second half of the 1960s. And if the paths taken in the three countries have had divergent results, then it is also intended to ask whether this differentiation affects to any appreciable measure the way in which each system places itself in relation to the financing of investment.

In the second place, it is intended to provide a critical contribution to evaluating the points of strength and weakness in the three financial systems' ability to fulfill the functions necessary for sustaining the accumulation process.

* The achievement of these two objectives obviously presupposes a particular "interpretation" of the functioning and evolution of the three systems. In reality it is this that determines the report's conclusions and therefore constitutes its principal part. A more rigorous approach would have required the delineation of a theoretical schema which would have provided the means for describing and interpreting the facts. However, it has been preferred to follow a more pragmatic approach starting with certain general premises and then, in the light of these, modelling the analysis around the characteristics, presented by each of the three systems in the mid 1960s. A reconstruction of the evolution of the three financial systems is derived from this approach, centring on different aspects of each system: the effects of anti-inflationary policy in Germany, the manner in which the credit system has sustained exceptional industrial development in France, the effects of the peculiar position of the Italian banks in financial intermediation.

These three aspects of these three financial systems are considered essential to an understanding of the internal logic underlying the ways in which they function. The resulting analysis applies at a more general level than that which could have been derived from an examination of the specific problem of investment financing. It has

been decided not to attempt to compare the pattern of firms' indebtedness in the individual countries considered. The reason for this is that companies' financial accounts reflect their relations with financial intermediaries and are therefore the result of the broader logic which regulates the functioning of each individual system. At the same time there are theoretical difficulties in defining an 'optimal' mix of financial resources available to firms on the basis of which to evaluate experience in these different countries. The statistics show, furthermore, that there exist significant structural differences between patterns of firms' indebtedness in the various O.E.C.D. countries.

Other aspects of the question have here been ignored. It will be noted for example that there is no mention of interest rates. Perhaps it is opportune to make explicit at this point that it has been a hypothesis of this report that it is not realistic to retain as a basic assumption any reference to the level of the medium-to-long term rate of interest (nominal?, real?) as a significant means for comparing the relationship between different financial structures and capital accumulation. Needless to say, this means neither that variations in interest rates do not influence accumulation nor that study of the ways in which interest rates are formed through the working of financial intermediaries and the markets could not also be important. But both these aspects may be considered as products of the functioning of a financial system; a system which already, of itself, influences the accumulation process.

The justification for these, and other, gaps in this work lies in the approach chosen in this particular comparative analysis (1), the aim being to propose a central core of ideas and hypotheses which,

(1) Other comparative studies of possible interest to the reader include: E. V. Morgan-R. Harrington, Bank for International Settlements, J. Carrington-G. Edwards, B. Bayliss-A. Butt Philip, Economists Advisory Group (see References).

in so far as they are at all valid, will provide a basis at a later stage for an analysis of those aspects of financial systems neglected in the present work.

Anglo-American and European Financial Structures

A financial system consists of a combination of intermediaries and markets. In the context of the accumulation of capital, the system operates as the creator of new purchasing power (credit for the production of new commodities) and as the means whereby those responsible for managing the savings generated by investments and those responsible for managing investment itself are brought into contact. The first function is performed by the banking system, the second can be performed not only by the banks but also by non-bank financial intermediaries and by the capital market. The parameters of the first function vary in accordance with the rate of growth of the economy; whilst those of the second depend upon the share of savings that remain within firms in the form of profits; that is, they depend upon the distribution of income given the rate of growth. A financial structure is defined by the weight obtaining to the different intermediaries and capital markets in the recomposition of the dissociation between saving and investment.

The financial structures of the three countries which interest us had, in the first half of the 1960s, a common characteristic that distinguished them from those of the Anglo-Saxon countries: namely, the relatively greater significance of the banking system. This was due to the limited existence, within the European financial structures, of non-bank financial intermediaries and in particular of the so-called "institutional investors" on the capital market (Table I.1). Hence the preferences of holders of financial wealth were relatively concentrated in but two types of financial asset: on the one hand, deposits by the banking system and, on the other, bond- and shareholding. This characteristic was accompanied by a market for shares

and bonds having apparently contradictory features. The Euro-continental market's absolute size was considerably smaller (both in terms of the value of outstanding securities and of the number of firms quoted) in comparison to those of the United States and of United Kingdom but was able, nevertheless, to supply a higher level of financing not only in relative, but also in absolute, terms in some cases (Tables I.2 and 3).

The European markets lacked that "fluidity" which, as is stated by O.E.C.D. report (O.E.C.D. (a)), is "a combination of characteristics difficult to classify, which comprise active competition between financial intermediaries, a broad gamut of instruments for placing of issues and providing finance available for savers and users of capital, the mobility of funds from one sector to another, broad access to information, etc." but which certainly is in relation to the dimensions of the secondary market. The lack of these conditions did not prevent firms from raising relatively large funds by means of the issue of shares and bonds (many of which were purchased directly by households) but limited the stability of the market (namely its function of rendering capital goods into more liquid form) and its degree of adaptability to the needs of new firms.

The economies which are the object of our attention also had in common a 'real' connotation that distinguished them from the Anglo-American economies: high demand by firms for external financing. This was due, as Lamfalussy has demonstrated, not so much to lower profitability in comparison to firms across the Atlantic or across the Channel, but rather to a greater propensity to invest (younger industrial structures rejuvenated by the war).

High external financing requirements together with the dominant role of the banking system could well have generated disequilibrium in the industrial development of the European economies.

Table I.1 : Resources of consolidated financial sector

	US (1960-64)	UK (1962-65)	France (1960-64)	Germany (1960-64)	Italy (1964-65)
Debtor sectors					
1. Capital Market	11	- 9	15	19	22
2. Banking system	31	35	41	51	58
3. Public sector (securities excl.)	9	9	18	- 2	-
4. Other financial intermediaries (securities excl.)	49	65	26	15	20
5. Others	-	-	-	17	-
	100	100	100	100	100

Source: OCDE Etudes sur les marchés de capitaux

Table I.2 : Value of outstanding securities (billions dollars)¹

		1964	1980
US ²	shares	633	1516,2
	bonds	114	490,4
UK ⁴	shares	72,9	160,8
	bonds	11,0	18,9
France	shares	20,9	60,9
	bonds ³	10,4	92,0
Germany	shares	11,2 ⁵	48,5
	bonds	15,5 ⁵	287,0
Italy	shares	13	64,0
	bonds	13,1	91,6

1. Market value of domestic and foreign securities issued by private and public enterprises and by financial institutions.
 2. Private sector only. 3. Private and public sector (Central Government excluded). 4. Foreign securities held by households are excluded. 5. Year 1969.

Source: OCDE Financial Accounts
 OCDE Etudes sur les marchés de capitaux

Table I.3 : Securities issues (% of GDP)

	60-65			76-80		
	shares	bonds	total	shares	bonds	total
US	0,41	2,87	3,28	0,63	6,51	7,14
UK	0,91	2,29	3,2	0,58	5,02	5,6
France	1,02	1,42	2,44	0,63	2,28	2,91
Germany ¹	0,71	3,05	3,76	0,44	5,16	5,6
Italy	1,67	3,8	5,47	1,05	6,93	7,98

1 Bonds-issues: including Debt Certificates (loans against borrower's notes and other non-bonded loans granted by insurance companies).

Source: OCDE Financial Statistics; OCDE National Accounts

It was this problem of the European financial markets which was the subject of discussion in various places during the 1960s. The most frequently proposed solution was the strengthening of the bond and share market. However, the experience of the Anglo-Saxon countries demonstrated that where this market was well-developed and "fluid", firms' requirements for external financing were very limited. This association, regardless of the direction of causality, indicates the objective limits of the capacity of the capital market to provide firms with funds. Even if one were able to transfer, by magic, the American financial structure into the European continental economies one would still be unable to meet all firms' needs (Lamfalussy(a)).

The solution which logically presented itself was that of marrying the superior financial capacity of the European countries with the greater "liquidity" of the Anglo-American stock markets. This would have permitted a solution of firms' financing problem which while providing risk capital would not at the same time shift their financial equilibrium to a higher level of indebtedness. In

fact, this solution was indicated in the past by Lamfalussy when he hypothesised a massive intervention of the banking system and of medium-long term financial institutions on the stock markets.

Today we can confirm that this path has been followed in none of the three countries. Perhaps this was because the proposal did not give due regard to the motives for which the industrial development of these economies had not already led to the creation of stock markets with Anglo-American characteristics. In all three countries the banks have strengthened their role in comparison to the mid 1960s (Table I.4). On the other hand there is no doubt that industrial development has continued in these economies at a high, though differing, rate. How they might have been able to reconcile the two trends, how in other words the three systems might have found their own solutions to the problem of financing of firms, is the basic issue to which this report addresses itself. To do so it will reconstruct the recent history of the German, Italian and French financial systems.

Table I.4 : Structural coefficients

	A		B		A x B	
	$\frac{\Delta \text{Fin. assets of fin. int.}}{\Delta \text{Fin. liab. of non fin. sectors}}$		$\frac{\Delta \text{Fin. assets of banks}}{\Delta \text{Fin. assets of fin. int.}}$			
	65-67	78-80	65-67	78-80	65-67	78-80
US	80,9	85,4	43,8	34,5	35,6	29,4
UK	n.a.	88,1	32,1 ³	69,4	35 ³	61
France ¹	85 ³	92,9	48,2 ³	55,1	41,0 ³	51,2
Germany ²	81,2	95	80,7	82,3	65,6	78,5
Italy	94,9	83,2	74,5	78,3	70,8	64,9

1. Including "Credit Agricole" but excluding Saving Banks.

2. Including banking special institutions.

3. 1960-1964: OCDE Estimates

Source: OCDE Financial Accounts

Banking Legislation

Whilst the three countries shared common characteristics so far as the centrality of the banking system was concerned this commonality did not extend to the legislative-institutional field. Here, instead, the operation of the three systems was different. Some reference to the banking legislation is necessary not only to explain the working mechanisms of each system but also to isolate the specific problems and illuminate them in such a way that we can interpret the evolution of the period 1965-1980.

Today, of the three banking laws presently in force the Italian is the oldest and also the only one which has not been modified recently. The Italian banking law of 1936 is also the only one of the three which still shows the mark left by the Great Depression.

The banking crisis experienced by France during the 1930s was much less severe than those in the other countries, did not involve the larger and more prestigious credit organisations, and did not prefigure the introduction of reforms in the area of credit legislation. Current legislation is based on laws and decrees from the years between 1941 and 1946 and on the modifications introduced during the period 1966-1973. This legislation distinguishes three types of banks which are obliged to register with the "Conseil National du Crédit" and are thus known as the "banques inscrites". These are deposit banks, "banque d'affaires" and medium-long term credit banks. These categories of banks were obliged to follow extremely strict rules loosened by the 1966-68 reform determining their respective fields of specialisation.

Germany, in contrast, experienced a banking crisis of more than modest proportions in the early 1930s, but this did nothing to shake legislators' conviction as to the utility of the mixed bank which indeed has recently been re-affirmed by the Gessler Report.

The banking law promulgated in 1934 maintained the credit structure based on the mixed, so-called, "universal" bank and the law of 1961 (which, with the modifications added in 1976 is still in force) did not introduce substantial changes leaving the institutional or organisation of credit to the initiative of the bankers.

Italian banking law is again somewhat different, belonging to a series of measures (the creation of I.M.I. in 1931 and of I.R.I. in 1933) aimed at definitively eliminating the distortions generated by the transformation of the 'mixed' banks into 'holding' banks. It thus constituted the crowning stage of a movement to radically alter the regulations affecting the credit system. The banking law of 1936, which with the modifications introduced in the post-war era is still operative, in effect constitutes a set of norms for assigning powers to direct and control credit. With these norms one cannot define the precise shape of the banking system as in the French case in which one observes a distinction between deposit banks, medium-long term credit banks, and "banques d'affaires" (besides the 'établissements financiers'); nor is it stated that the normal exercise of banking activity may include the purchase of equity and the granting of medium-long term credit (as in the German case). On the other hand, the law does not establish an absolute prohibition against the banks entertaining relations with firms that go beyond short-term credit arrangements. What is sanctioned however is the principle that the credit system requires external regulation. The law derogates to the monetary authority the task of regulating, both through active intervention and passive consent, the ways in which bank credit should be granted. It is therefore understandable that, in order to describe those banking practices compatible with Italian law, it is "... preferable to avoid the distinction between British, or short-term, "commercial" banks and mixed banks. It is preferable to resort to the single notion of the ordinary

credit bank on the understanding that it is the bankers, and if necessary the monetary authorities, which define the limits which at any given moment have to be observed in the use of deposits by the banks." (Saraceno). This notion of "ordinary credit" is a good illustration of the flexibility of Italian banking law and of the key role attributed to the central bank. In short, it is the central bank which determines what it deems to be an optimal financial structure in any given period (Ciocca).

The importance of the role attributed to the central bank in Italy derives from motives which are different from those which make German law attribute to the DBB an equally important role. In the German case the accepted principle is that the institutional organisation of credit must be left to the initiative of the bankers. The exercise of controls, which is very limited, and the supervision are entrusted not the central bank but rather to a special body nominated by the government. The central bank's main task on the other hand is to undertake the function of being the issuing bank which, by acting absolutely independently, guarantees the general conditions for the functioning of the credit system and especially monetary stability. Whilst, therefore, in Italy the importance of the central bank derives from the recognition of the necessity for public regulation of the credit system, in Germany the DBB draws its authority from the opposite philosophy: that of guaranteeing the conditions for the exercise of self regulation.

Unlike the Italian and German cases, in which the spirit underlying credit legislation has hardly changed over the last fifteen years, in France there has been a significant shift in the "dirigiste" approach which the legislation of the 1940s took towards the credit system. The decrees of 1966-68 constituted a

genuine reform of the system aimed at reducing the importance of the Treasury in the supply of medium-long term credit and decentralising decision-making. The law of 1973 concerning the Bank of France constituted a decisive step in attributing to it independent responsibilities for monetary policy. Under the preceding legislation, the Bank had been in a position of mere executor of the decisions taken by the government.

II. CHARACTERISTICS OF THE THREE FINANCIAL SYSTEMS IN THE FIRST HALF OF THE 1960s

France

The French financial system of the mid 1960s had three characteristic features: the so-called "cloisonnement" of the financial circuits; the reduced role of the banking profession (as defined by the laws of 1941-46) and the dominant position of the public sector in the management of credit flows.

On the whole, the banking system had a considerably greater weight in the French financial structure than those in the Anglo-Saxon countries but a lesser importance compared to those in Italy and Germany (Table I.1). The difference in respect to these two countries was due to the exceptional importance of the state's intermediation activity. This intermediation is based upon the "Treasury circuit". This consists of three channels for raising funds: deposits and Treasury bonds, deposits with the Post Office and, especially, the funds deposited by the savings banks with the Caisse Dépôts et Consignations (C.D.C) (2). Together, these three channels accounted for a flow of funds to the Treasury which was not much below the total volume of funds which flowed to the "banques inscrites" and "special statute" banks put together (Table II.1).

State intermediation was focussed most of all in the field of "non-mobilisable" medium-long term credit. Side by side with the intervention of the Treasury was that of the "special institutes" (Credit National, Credit Foncier, Caisse Nationale des Marchés de l'Etat, etc.), which are institutions of a public and semi-public nature relying largely for the supply of funds on the purchase of their bonds by the C.D.C.

(2) From a legal point of view Savings Banks do not belong to the French banking system.

Table II.1 : France: funds raised by financial intermediaries¹
(percentage distribution)

	1966	1974	1981
Banques "inscrites"	37,4	44,2	35,9
Banques "à statut spécial"	15,5	20,4	24,3
Post office accounts	8,6	6,5	4,6
Saving banks (Caisses d'Epargne)	26,6	24,8	29,7
Treasury bills	11,1	3,9	2,2
Others	0,8	0,2	3,3
	100,0	100,0	100,0

¹ Sight, term and savings deposits, "bons de caisse", and Treasury bills, Stock data.

Source : Rapport du CNC various years.

The majority of medium-long term credit was therefore supplied through the direct or indirect intervention in the state (Table II.2). Despite the presence of a category of banks specialised in medium-long term credit the significance of the banks in this sector was extremely limited and confined almost exclusively to "mobilisable" credit (3). Even the very weak market for fixed-income bonds was dominated by the Treasury and by the "special institutes".

With exception of the "banques populaires", the special statute banks, the other large segment of the French financial system, benefitted from tax exemptions and privileges on interest payments to depositors. These banks, and in particular the forceful and dynamic Crédit Agricole, could thus develop behind barriers protecting them from the competition of the "banques inscrites".

(3) This peculiar kind of credit may be rediscounted by the Banque de France on authorization by the special credit institutions or the C.D.C.

Table II.2 : France: credits to the economy by maturity and institutions (bill. FF and % distribution)

	1966	%	1974	%	1980	%
Short term	103	100	286,8	100	509,1	100
- Banque de France	15,4	15,05	65,9	22,9	-	-
- Banques inscrites	85,4	82,9	203,2	70,7	385,9	75,8
- Banques "à statut spécial"					92,6	18,2
Medium term "mobilisable"	36,8	100	80,3	100	147,4	100
- Banque de France	7,9	21,5	24,5	30,5	-	-
- Banques inscrites	22,2	60,3	43,6	54,3	111,0	75,3
- Banques "à statut spécial"					21,6	14,6
- Special Credit Institutions	6	16,3	12,1	15,1	11,3	7,7
Medium "non mobilisable" and long term	152,4	100	566,4	100	1416	100
- Banques inscrites	12,9	8,5	190,2	33,6	333,2	23,5
- Banques "à statut spécial"					298,0	21,0
- Special Credit Institutions	94,9	62,3	326,4	57,6	679,6	48,0
- Treasury	44,6	29,3	48,9	8,6	31,1	2,2

Stock data. Source: Rapport du CNC, various years.

The latter constituted the third part of the system and was an expression of genuine finance (not included in the sphere of public administration or in that of corporative interests). This segment was, one could say, "overwhelmed" by the privileged circuits (savings banks, Crédit Agricole and Crédit Mutuel) and it disposed, during the mid 1960s, of little more than a third of the entire value of funds collected by the intermediaries. The reduced importance of the "banques

inscrites" is a structural problem in the French financial system, dealt with but not resolved, as we shall see, by the reform of 1966-1968. Here it should be added that the four large nationalised deposit banks (three since the 1966 merger between the Banque Nationale pour le Commerce et l'Industrie with the Comptoir National d'Escompte) while belonging de jure to the public sector, de facto pursued their activities on lines very similar to those of a private bank. Often, in fact, they had common interest with private "banques d'affaires" (Morin).

In the last analysis, the "cloisonnement" of the financial system and the limited role of the banking profession were the logical consequence on the one hand of social groups (particularly the farmers) with sufficient power to organise their own privileged circuits, and on the other of a particularly high level of public intervention.

Halfway through the 1960s, the French financial system presented itself therefore as a highly structured system of banking and non banking intermediaries (much more so than the Italian system in which there existed neither "banques d'affaires", financial credit banks, nor even the "etablissements financiers") but suffering from "cloisonnement" and a level of public intervention such as to suggest to some commentators that it would have been better adapted to a socialist economy rather than to a capitalist one. It was especially on this latter aspect of the question that the debate preceding the reforms begun in 1966 was concentrated.

At first glance, the extraordinary importance of the public sector in the credit system can be ascribed to objective factors of a "real" character. The high rate of inflation experienced on a continuous basis in France from the end of World War Two until the beginning of the 1960s could explain the two peculiar phenomena that have conditioned the French financial system: namely, the low level

of the propensity to save and the high propensity of families to hold cash ("Rapport Lorain") (Table II.3). The appearance of these phenomena in a country already historically oriented towards an extensive participation of the state in the economy, and endowed by a centralised and efficient public administration, could explain the importance of public intervention as a guarantor of the rational utilisation of available savings and to make possible a massive "transformation" of liquidity into financial credit.

Table II.3 : Households financial assets (percentage distribution)

	France ¹		Germany		Italy	
	1960-65	1976-80	1960-65	1976-80	1964-65	1976-80
- Cash and bank deposits	53,5	43,0	54,4	46,6	46,7	62,3
. cash and sight deposits	49,2	15,1	8,4	5,1	19,6	32,0
. other deposits	4,3	27,9	46,0	41,5	27,1	30,3
- Securities	18,3	9,1	19,5	14,8	17,7	20,3
- Other	28,2	47,9	26,1	38,6	35,6	17,4
	100,0	100,0	100,0	100,0	100,0	100,0

1 Saving banks excluded

Source: OCDE Financial Accounts; OCDE Etudes sur les marchés de capitaux; Banca d'Italia: Attività e passività finanziarie del paese

A more fundamental investigation shows however the effects that the legislation of 1941-45 and the credit policy in the following twenty years have had on the distribution of deposits between the three sectors and on their liquidity. This allows us to understand more fully the reforms "raison d'être" and the problems that even now continue to exist in the French financial system.

The various constraints on the "banques inscrites" included, for deposit banks, the imposition of upper limits on the maturity and remuneration of deposits. These, jointly with a tight policy on the opening of new branches, had prevented the large deposit banks from effectively competing with the "privileged" circuits in the acquisition of more stable resources. As a result, the function that these banks could have performed in changing the preferences of the public towards deposits of longer-term maturity was reduced. On the other hand, the "banques d'affaires" and the medium-long term credit banks did not have sufficient size or geographical coverage to collect term deposits or savings deposits in competition with the Saving Banks and with Credit Agricole. At the same time, the issuing of fixed-interest bonds was practically reserved to the Treasury and to the special institutes.

The massive intervention of the state in the financing of investment was therefore not due so much to an objective shortage of non-liquid funds arising independently of the behaviour of the financial intermediaries, but rather to their distorted distribution in favour of the Saving Banks and the "special statute" banks. Such an important role of the state in the collection of funds could not be considered, at a political level, necessary for channeling resources towards the investments defined by the Plans as of priority. The logic that had animated the nationalisations of 1945, public control of the centralisation of capital and of industrial sectors was lost with the reduction of power of the Left, and it left behind only its legislative shell. In reality, from the period of reconstruction onwards, the effective use that was made of public intervention in the financial system was notably below that which was potentially feasible. And even under Gaullist "dirigisme" the extension of public intervention was on a level above that genuinely required by planning.

The basic motive for the Debré reform (1966-68) was that, despite a lack of coherent political support, the institutional pattern was still conceived in the interests of a highly-developed form of public intervention. The main consequence of this contradiction between the institutional framework and the policy conducted within this framework was that the financing of investment took on a public character even when it was not strictly necessary. The existence of specialised banks in this field, medium-long term credit banks provided for by the legislation, were not sufficient to significantly involve the banking system in financial credit. The "banques d'affaires", while clearly performing an important role in the interpenetration between finance and industry that characterised the major private groups, also had limited importance in financing credit for the private sector, which had easy access to the funds placed at their disposal by the public financial circuit.

The 1966-68 reform of the credit legislation, preceded and accompanied by a succession of expert investigations (Lorain, Commission Leca, Marjolin-Sadrin-Wormser), was based on the conclusions of the Commission de l'Economie Générale et du Financement of the 5th Plan according to which it was deemed necessary to offer the banks the possibility of playing a more important and active role in the financing of investments, while at the same time reducing on to an equal footing the intermediation activity of the Treasury. Given that the deposit banks were those most concerned by this new line of policy at the beginning of 1966 a decree significantly reduced the differences between their statutes and those of the "banques d'affaires". In particular, the former became like the latter in so far as they were allowed to receive medium-long term funds.

There was thus a reduction in the protection enjoyed by the privileged circuits, especially the Savings Banks, vis à vis the competition from the "banques inscrites". This competition was also

stimulated by the abolition of the regulations (a "legal cartel") fixing maximum rates paid to depositors and minimum rates offered on loans for the "banques inscrites", and by the liberalisation of the opening of new branches.

A further series of measures aimed at steering the competition of the "banques inscrites" to the privileged circuits towards medium-long term operations: prohibition of remuneration of sight deposits, liberalisation of interest rates on fixed term deposits, removal of the upper limits on returns to savings deposits. A reform of the methods of issue and placing of fixed-income bonds aimed at the same objective and considerably reduced the relative weight of the Treasury. Furthermore, in order to allow the deposit banks to widen their activity in equity participation, one previously the dominant preserve of the "banque d'affaires", there was an increase in the maximum limits of participation with respect to their own capital and also that of the other businesses in which they had holdings.

In addition to a group of measures aimed at modernising the technical operations affecting short-term credit there followed a thorough-going reform of bank re-financing by the Bank of France. This reform was based on the proposals of the Marjolin-Sadrin-Wormser report. This reform aimed at bringing about the creation of an effective monetary market that would substitute for the direct activity of the central bank in the area of re-discounting. A crucial motive for these changes was to adapt the domestic system to those of other countries with a view to opening up the French financial system.

Germany

The German financial system, in contrast to those of Italy and of France, is characterised by the dominant presence of the universal bank.

It is a well-known fact that the universal bank offers the entire array of banking services (acceptance of all type of deposits, granting of both commercial and financial credit, purchase and sale of securities, and maintains strong ties with non-financial businesses. The latter ties take a number of forms such as the acquisition of shares, the exercise of the depositors' voting rights and the presence of the banks' representatives on the Boards of Directors of such firms. One is not dealing here with a specific category of "banking firm" defined by law, as in the case of the "banques d'affaires" in France. German banking law, in fact, neither sanctions nor defines the possibility of a classification of banks. Hence, the existence of the universal bank, results from the behaviour of the banking profession within a legislative framework which does not define a specific pattern of specialisation. This does not mean however that there do not exist, within the German banking system, specialised credit institutions which offer only particular services. Nor does it mean that one will not also find within the operations of the universal banks a certain degree of specialisation. Such specialisation however derives from the choices made by management and not from constraints produced by law.

Credit firms belonging to private Commercial Banks, Savings Banks and Credit Co-operatives sectors are all considered to be universal banks. Although they all supply the entire gamut of banking services, these three groups of banks may be differentiated, not only in relation to their respective legal forms and administrative organisations but also by business structures.

The private commercial banks (by which one understands the large banks, the regional banks, the private bankers, and the foreign banks) have dominated the market for short-term loans since the 1960s (with about a 54% market share) and on the side of liabilities, also that for deposits 'on demand' (about 42%) (Tables II.4 and 5). Furthermore, the private commercial banks were and still are, especially the three largest banks (Deutsche, Dresdner and Commerzbank), closely tied to the foreign banks; together they own the largest part of the shares that were in the portfolio of the German banking system (Immenga).

Even if the direct presence of the commercial banks on the market for medium-long term credit was modest (10% in 1965), it should be remembered that they also operated (and continue to operate) indirectly in this market through private mortgage banks (the main activities of which are the provision of medium-long term credit and whose form of re-financing consists of the issuing of bonds). In addition, they also used, and continue to use, financial institutions specialising in medium-long term industrial credit (the main shareholders are the large banks and the most important Insurance companies).

The Savings Banks, together with their central institutions (Girozentralen), which also operate directly, had by the mid 1960s a leading position in granting medium-long term credit (about 42%) and also in receiving savings deposits (about 64%). Furthermore, they owned over half of the bonds held by the German banking system (above all, of debentures issued by the public administration) and they were also the permanent holders of shares in non-banking companies.

The other group of banks with an universal approach to credit is the credit co-operatives, whose "de facto specialisation" consisted of granting short- and medium-term loans.

Table II.4 : Germany : deposits of banking groups from non-banks, by maturity (percentage distribution)

	68			74			81					
	Total	Sight dep.	Time dep. < 4 years	Saving & time dep. > 4 years	Total dep.	Sight dep.	Time dep. < 4 years	Saving & time dep. > 4 years	Total dep.	Sight dep.	Time dep. < 4 years	Saving & time dep. > 4 years
Commercial Banks	27,3	42,6	65,2	14,4	26,4	39,2	51,9	14,9	23,7	34,8	45,1	13,3
Big Banks	14,7	23,5	35,1	7,6	13,7	20,6	24,8	8,3	12	18	21,3	7,2
Regional Bank	10,4	15	24,2	6	10,4	14	22	5,9	9,8	12,7	19,9	5,4
Branches of foreign Banks	-	-	-	-	0,5	1,2	1,1	0	0,4	1,1	0,5	0,2
Private Bankers	2,2	4,1	5,9	0,8	1,8	3,4	4	0,7	1,5	3	3,4	0,5
Central giro Inst.	4,7	4,6	13,6	2,7	5,2	4,7	9	4,2	4,8	4,9	5,7	4,5
Savings Banks	38,7	31,8	11,4	47	36,8	32,3	19,3	43,4	34,2	33,1	23,2	38,3
Cooperative Sectors	12,3	13,8	5,6	13,4	16,6	16,8	14,4	17,3	20,1	19,7	22,1	19,5
Mortgage Banks	9	0,2	1,1	13,3	7,3	0,2	1,3	11	8,4	0,3	1,6	13
Instalment sales financing inst.	0,2	0	0,9	0	0,4	0,2	1,3	0,2	0,6	0,5	1	0,4
Banks with special functions	4,4	1,3	2,2	5,9	3,6	0,6	2,8	4,8	4,6	0,8	1,3	6,7
Postal giro and postal savings bank offices	3,4	5,7	0	3,3	3,7	6,2	0	4,2	3,6	5,9	0	4,3
	100	100	100	100	100	100	100	100	100	100	100	100

Stock data Source: Monthly Report of Deutsche Bundesbank

Table II.5 : Germany : Lending by banking groups to non-banks, by maturity (percentage distribution)

	68		74		81				
	Total	Short-term	Medium and long-term	Total	Short-term	Medium and long-term			
Commercial Banks	20,8	55,5	11,3	22,2	50	13,8	20,7	41,7	15,8
Big Banks	8,7	23,6	4,6	9	19,4	5,8	8,3	15,5	6,7
Regional Banks	10	24,1	6,2	10,3	20,8	7,1	10,1	17,7	8,3
Branches of foreign Banks	-	-	-	1,2	4,4	0,3	1,1	3,8	0,4
Private Bankers	2,1	7,8	0,5	1,7	5,4	0,6	1,2	4,7	0,4
Central giro Inst.	13,4	6,6	15,3	17,6	8,5	20,3	16,5	7,9	18,5
Savings Banks	23,3	18	24,8	22,5	20,2	23,2	23	25	22,5
Cooperative Sectors	8,4	17,1	6,1	10,7	17,5	8,7	13	22,1	10,6
Mortgage Banks	23,8	0,3	30,3	17,8	0,7	22,8	19	0,6	23,2
Instalment sales financing Inst.	1,4	1,5	1,3	1,6	1,6	1,7	1,5	1,8	1,5
Banks with special functions	7,6	1	9,3	6,4	1,5	7,9	5,2	0,9	6,6
Postal giro and postal savings bank offices	1,3	-	1,6	1,2	-	1,6	1,1	-	1,3
	100	100	100	100	100	100	100	100	100

Stock data Source: Monthly Report of Deutsche Bundesbank

By the middle of the 1960s the three banking groups which constituted the system of universal banking had total assets equal to 70% of the entire banking system. If, furthermore, one takes into consideration the aspects of banking services which do not appear in their accounts and also the "subsidiary relations" existing between banks with a universal approach and specialised credit institutions (mortgage banks, banks for financing hire purchase, and banks with special functions), the dominant position of the universal banks within the German banking system appears self-evident. This position is reflected in the absence of a system of special credit institutions comparable to those which exist in Italy or even in France. In 1965, banks with special functions, which included the credit institutions in charge of financing industrial investment, granted only 7% of the medium-long term credit awarded by the banking system so that this item constituted only 32% of their assets, while a greater proportion (42%) consisted of loans to banks. One can see confirmed in this a situation in Germany which is opposite to that of the Italian one of "double intermediation". The credit institutions with special functions were (and still are) operational instruments in the hands of the banks, a situation considerably different to that in Italy where, despite the existence of subsidiary relations, there has not been a similar relation of subordination between banks and special credit institutions.

Even public intervention in the credit arena involved, and continues to involve, the banks. The Kreditanstalt für Wiederaufbau, the most important credit institution in the management of governmental financing programmes in favour of industry, has a procedure for granting credit which allows for the intervention of the banks, to whom the requests for financing have to be addressed. What one is dealing with here is a form of open collaboration with the banks which does not influence their relative competitive positions and

ensures that the Institute does not undertake operations that other credit firms would be able to undertake on their own. A greater significance is attributable to public intervention in the form of guarantees, obtainable from the Federal Government, from the Lander and from local authorities. It is these guarantees for example that have allowed the emergence of industrial credit guarantee syndicates, set up on the initiative of the association of German industrialists. These syndicates do not grant credit as such. Rather, they play an intermediary role in so far as it is the banks which turn to the syndicates with requests for guarantees for advancing loans. The Government and the Lander then grant a "re-guarantee" equal to 80% of the commitment assumed by the guarantee syndicate. The investment companies for small- and medium-sized industry, while remaining private institutions, also operate with a certain amount of public support, partly in the form of financing but more frequently as guarantees underwritten by the Government and Lander.

All this demonstrates that public intervention in the credit field did not extend to the direct management of financial flows, as occurred in France and, to a lesser degree, in Italy, but took, and continues to take, indirect forms through banks receiving support on those investment projects which are deemed by them to be of considerable risk.

Although family savings have become relatively highly-concentrated in two groups of non-bank financial intermediaries (Insurance companies and Savings Associations for Housing Finance) and also in the housing market this has only led to a marginal degree of competition in relation to the banks. The German securities market was (and still is) practically dependent on the banking system. As far as the share market is concerned, though the banking system's purchasing of shares is kept within strict limits (average 1960-65: 8,8% of total share purchases), the banks have always had a preponderant role in

the floating of public quotations, which in Germany requires the involvement of a bank, in order to manage underwriting of new issues and their sale to investors. The issuing syndicate is normally composed of a group of banks (especially large private banks and also the central institutions of the savings Banks) which sell a large proportion of the shares underwritten to their own clients. The fixed-income bond market was (and still is) dominated by banking debentures (70% of the debentures in circulation) (Table II.6).

Table II.6 : Germany : Bonds by issuers and holders (percentage distribution)

	France ¹		Germany		Italy	
	1964	1980	1965 ²	1980	1964	1980
<u>Issuers</u>						
- Public sector	83,0	78,0	21,7	23,9	43,1	59,4
. Gen. Gov.	23,3	15,9			25,1	49,5
- Non fin.priv.enterpr.	17,0	22,0	7,1	0,8	10,4	0,8
- Banks and other fin.int.			71,2	75,3	46,5	39,8
	100,0	100,0	100,0	100,0	100,0	100,0
<u> Holders</u>						
- Banks	n.a.		45,3 ³	40,1	28,6	57,5
- Other fin.int.	n.a.		12,6	15,6	3,2	2,7
- Rest of the world	n.a.		3,1	4,1	} 48,2	} 18,3
- Non fin. enterpr.	n.a.		3,9	5,0		
- Household	n.a.		22,8	23,9		
- Other	n.a.		12,3	11,3	20,0	21,5

1. Public sector includes issues of special credit institutions. Private sector includes issues of financial institutions with public statute. 2. Source: Monthly Report of DBB. 3. 1971

Stock data Source: OCDE Financial Accounts

During the mid 1960s measure were taken against the inflow of foreign capital seeking to acquire German bonds. It was at this time that it became evident that although the foreign sector had the ability to guarantee a degree of stability on the German housing market, the market for bonds was highly dependent on the banking system. In other words what was lacking was a network of investors willing or able to guarantee stability.

The mild competition from the Insurance companies and the Savings Associations towards the banking system in regard to their financing of housing is demonstrable by analysing the actual relations existing between them and the banks. The largest investments by the Insurance companies consist of loans in return for bonds issued both by firms and by banks (DBB, Monthly Report Jan. 72). Since it is only large industrial firms which have direct relations with the largest Insurance companies, whilst to a large extent industrial bonds are distributed by the banks, the Insurance companies end up being clients of the banks themselves; not only because of their accounts with the banks, but also because of their purchases of banking and industrial bonds as well as of shares. If, moreover, one also consider the fact that over two-thirds of the bonds held are banking bonds, then it becomes evident to how high a degree the Insurance companies perform the task of channeling funds to the banking system.

The Savings Associations for Housing Finance also had (and have) close ties with the banking system, not only because "banking deposits" had not inconsiderable weight in their asset structure (almost 30%), but also because a large number of these institutions were (and are) departments of the Girozentralen, of the Savings Banks and of various mortgage banks that the Bundesbank defines as "parent institutions" (DBB, Monthly Report Dec. 1966).

One can add that by the middle of the 1960s the three large banks and some other commercial banks began to supply "personal mort-

gage loans", which were more easily obtainable than those offered by the Savings Associations for Housing Finance, who required a minimum sum of savings and a short time period in which to determine whether or not to allocate a loan to an applicant; procedures which effectively limited the competitive capacity of such Associations in comparison with the banking system that can supply the full array of services.

As far as the competition within the banking system itself is concerned, the universal approach to credit practice, together with the existence in law of free access to credit activity, have been the cause of intense competition between the banks which since 1967, following the complete abolition of controls on the rate of interest, has become acute.

Italy

The distinctive character of the Italian financial system, as it appeared in the middle of the 1960s, without doubt consisted of the credit specialisation which assigned the task of providing investment finance almost exclusively to the "special credit institutions". This specialisation constituted the pivot for diversification between intermediaries. The range of different kinds of intermediary was thus narrower than that existing in France, where alongside the "special institutions", organised on similar lines to those in Italy, there also existed various other kinds of bank and "établissements financiers". In effect, the Italian system was based solely on two types of intermediary: the banks and the "special credit institutions". The first kind include, it is true, various different categories of banks (National Interest Banks, Public Law Credit Institutes, ordinary banks, popular banks and co-operatives, savings banks, etc.) that are distinguished in terms of their ownership, legal status and geographical

coverage, but much less in terms of their specialisation. All of them in fact, with some differences, are substantially deposit banks and "ordinary credit" banks.

Not even the fact that the largest banks belong to the public sector (Public Law Credit Institutes) or to the system of state participation (the three National Interest Banks, COMIT, CREDIT and Banco di Roma) implied substantial differences in behaviour.

The "special credit institutions" are non-bank intermediaries specialised in medium-long term industrial finance (IMI, Mediobanca, Efibanca, Centrobanca, Mediocredito, Isveimer, Irfis, CIS, etc.), housing finance, agricultural finance and public works. They are mostly publicly-owned, or controlled by credit firms which in their turn belong to the public sector or the state participation sector. The legislation did not define other forms of intermediary such as investment banks, finance companies and investment funds.

Between these two types of intermediary defined by the law codifying credit specialisation, banks had a dominant position in the collection of deposits (Table II.7). This role was accentuated in the post war period. The total number of credit firms remained virtually unchanged between 1947 and 1965; what has altered is the relative weight of individual categories. The direction taken by the monetary authorities in the post war years had the effect of reducing the significance of the three National Interest Banks and of encouraging competition in the relations between these and other banks. One can see this trend in Table II.8, where, in particular, the development of savings bank deposits should be noted. Although the Italian savings banks are public law institutions whose presidents are nominated by the Treasury Minister, they do not belong to the state finance circuit as is the case in France. Rather, the growing importance of the savings banks has to a significant extent been at the expense

of the state's own collection of funds via the Post Office, and thus in competition with the Treasury circuit which, as in France, includes postal deposits and "Cassa Depositi e Prestiti" (a parallel institution of Caisse Dépôts et Consignations).

The development of the banking system as a whole privileged some categories of bank at the expense of others. The category that was sacrificed, namely the Banks of National Interests, was, for reasons of tradition (ex-mixed banks) and geographical concentration, in close contact with the productive sphere and in particular, the industrial sector of the economy. The banks which received privileged treatment with regard to their opening of branches were more "deposit-oriented" than "credit-oriented". Funds raised in excess of the lending capacity were channeled into the purchase of bonds or onto the inter-bank market which, as a result, expanded rapidly (De Cecco).

This "deposit oriented" attitude was to remain a constant tendency in the Italian banking system; a tendency not hindered or prevented by the monetary authorities and intensified by the behaviour of individual credit firms which were always oriented, at least until recently, to maximising deposits by means of reciprocal competition on interest rates offered to depositors.

Already by the beginning of the 1960s, the contradiction which was becoming evident in the Italian financial system was that existing between, on the one hand, the dominant position of banks in the financial assets of the public and, on the other, the limitations imposed on the use of their assets, in particular, as medium-long term credit. In large part this contradiction was resolved by the characteristics assumed by the system of special credit.

The shape of the special credit system, as it presents itself today, was nearly completely formed during the period from the

end of the war up until the beginning of the 1960s. With the exception of I.M.I., the institutions operating predominantly in the field of industrial financing were nearly all founded during this period. But the large part of them was set up to favour public intervention. At the same time their number was very much higher than in the other two countries. The existence of a large number of these credit institutions, which still continues today, was due to overlapping between the policy lines decided by the state, on a geographical and sectoral basis, and the company growth targets of the individual banks interested in expanding their activities.

The importance of public intervention in the activities of the special credit institutions can be confirmed from the weight of subsidised credits in the total value of their lending (Table II.9) and also from the geographical distribution of credit employed in the years (1962 and 1963) of high investment activity by firms in the "industrial triangle" of Northern Italy. During this period credits advanced in north west Italy were not more than 40% of the total. This comparison shows that the supply of credit by the special credit institutions was determined not by demand (concentrated in the industrial triangle) but by the steering of funds towards the targets of the public intervention. Moreover a major part of the non-subsidised credit was directed to large-sized, private or state-owned, enterprises, as a result of the natural propensity of large credit institutions (such as IMI and Mediobanca) to favour big investment projects and corporation restructuring.

One can therefore conclude that the medium-long term credit system that had been established during the period of maximum accumulation of industrial capital left largely unsatisfied the demand for non subsidised credit arising from that group of small- and medium-sized firms that had been the principal actors in the industrial development process. This demand naturally turned to the banks operating

in the areas of industrial development which, by tradition, were inclined to entertain relations with the business world and which were also able to supply assistance for companies engaged in foreign trade. These banks largely satisfied these financial needs by granting credit advances that were 'working capital' only in a formal sense.

Thus the concept of "ordinary credit" came also to include finance for investment (Mattioli, Confalonieri). The banks substantially filled the gap which had been formed in the supply of non-state-backed loans.

A further consideration emerges from the analysis of the sources of funds of special credit institutions. Only a minor proportion of funds were raised by term deposits. The biggest proportion of funds was raised through the issue of bonds. The placement of bonds, whilst competing with firms' sales of direct issues - which in Italy as in the other two countries have always been rather limited - did not compete with bank deposits. Instead, with respect to the banks the bonds issued by the special credit institutions were an important form of employment of funds. In effect, in 1965, the special credit institutions derived about 40% of its funds directly from the public, about 35% from banks and the remaining 25% from the public administration.

Credit specialisation was thus consistent with the maintenance of a key role for the banking system; this being made possible by the two-way relationship that tied the special institutions to the banks. On the one hand, the banks supplied funds to the credit institutions by acquiring bonds; on the other, the supply of credit of these institutions was such as to allow the banks to provide a portion of finance for investment.

This consistency was made possible by the special meaning that bankers and the central bank attributed to "ordinary credit".

Here one already sees the importance of the role of the Bank of Italy. Not only are its powers much broader than in the other two countries, but at the same time its discretionary powers allow it to establish those models of banking practice which in Germany result from the "free" behaviour of the banks and in France (particularly before the Debré reform) from credit legislation.

Table II.7 : Italy: Funds raised by financial intermediaries¹
(% distribution)

	1965	1974	1980
Banks	69,6	76,2	71,9
. sight dep.	(45,5)	(55,7)	(52,5)
. other dep.	(54,5)	(44,3)	(47,5)
Special Credit Inst.	11,4	11,9	4,15
. dep. & dep. cert.	(20,2)	(26,2)	(45,0)
. bonds	(79,8)	(73,8)	(55,0)
(<u>bonds held by banks</u> <u>bonds held by public</u>)	(0,77)	(1,84)	(6,6)
Post Office Accounts	14,0	9,4	8,6
Gov. bonds and Tr. bills	5,0	2,5	15,35
	<u>100,0</u>	<u>100,0</u>	<u>100,0</u>

¹ Sight, term and saving deposit, deposit certificates, bonds and Treasury bills held by households and not financial enterprises.

Stock data. Source: Banca d'Italia: Attività e Passività Finanziarie del Paese.

Table II.8 : Italy: Deposits and credits by categories of banks
(% distribution)

	1947		1965		1981	
	dep.	cred.	dep.	cred.	dep.	cred.
Public Law Credit Inst.	23,1	24,9	22,5	25,1	19,1	19,1
National Interest Banks	23,9	24,1	18,2	22,4	12,1	14,9
Ordinary banks	22,2	22,2	22,1	22,0	25,1	28,9
Popular & cooperative banks	11,2	9,9	11,4	10,4	16,0	14,5
Savings banks	19,6	18,9	25,8	20,1	27,7	22,6
	<u>100,0</u>	<u>100,0</u>	<u>100,0</u>	<u>100,0</u>	<u>100,0</u>	<u>100,0</u>

Source: Banca d'Italia, Bollettino

Table II.9 : Italy : Credits to the economy of banks and special institutions (% distribution)

	1965	1974	1981
Banks	62,1	58,3	63,3
. short-term	(87,2)	(87,2)	(81,9)
. medium-long term	(12,8)	(12,8)	(18,1)
Special Credit Institutions	37,9	41,7	36,7
. industry & public works	(60,0)	(71,05)	(65,0)
of which - subsidised	(39,1)	(39,1)	(31,6)
. others	(40,0)	(28,95)	(35,0)
	<u>100,0</u>	<u>100,0</u>	<u>100,0</u>

Source: Banca d'Italia, Bollettino e Relazione del Governatore

III. REAL TRENDS IN THE THREE ECONOMIES

Before giving consideration to the evolution of the three financial systems it is useful to recall the three economies' principal trends.

The most important common characteristic was the transition from a phase of strong growth to one of constrained and unstable growth, during the 1970s. The fall of the average rate of growth of investment has not, to any dramatic extent, diminished the proportion of G.D.P. devoted to accumulation. The latter has, in all three countries, remained at a level higher than that in the U.S.A. and in Great Britain (Table III.1). Firms' profit margins have everywhere shown an initial fall followed by a recovery after 1975; public spending as a share of G.D.P. has everywhere increased.

If one considers various other questions however, the general trend of the three economies differs. Observing the trend of investment, one notes an almost uninterrupted phase of expansion in France between 1965 and the beginning of 1974. In Italy, there was an interruption in 1969-70 followed by an extremely rapid recovery between 1972 and 1974. Germany witnessed extraordinary growth in the period 1968-71, but the recession began earlier than elsewhere, in 1972. The three countries became synchronised during the deep depression of 1975. The subsequent recovery was slower in Italy and France, faster in Germany. Here there are three main distinctive features of the three economies: the rate of inflation which was particularly high in Italy and low in Germany; the uninterrupted surplus of the German current balance of payments between 1966 and 1979 and the massive capital inflows from abroad; the structural negative savings position of the public sector in Italy.

These phenomena have had a notable influence on the conditions in which the three financial systems have worked. Above all else,

the amount of intermediation has expanded. On the one hand, at least until 1976, the fall in the share of profits has been faster than the fall in the rate of accumulation. On the other, there has been the problem of financing the public debt: in Germany and France there has been a transition from a situation of substantial equilibrium to one of deficit: in Italy the deficit has expanded.

Table III.1: Investments as a percentage of G.D.P. (constant prices)

	1965-70	1970-75	1975-80
United States	19.4	18.4	17.1
United Kingdom	20.7	20.5	18.1
France	23.3	24.1	21.9
Germany	23.7	23.0	22.5
Italy	23.9	22.6	19.3

Source: OCDE National Accounts

In all three countries the conditions in which intermediation activity has to be carried out have become more critical. In short, the degree of uncertainty has increased in the face of sharp exchange rate and raw material price fluctuations, crises of certain industrial sectors and reconversion difficulties and major fluctuations in stocks, the most volatile component of investment. Risks of financial instability have increased with banks failures, both in Germany where the central bank has adopted a very severe monetary policy and in Italy where it has taken a softer line.

The comparison of financial balances shows (Table III.2) the extraordinary volume of families' financial savings in Italy (equal to nearly three times those in the other countries). The financial deficit that, obviously, has to counter-balance this surplus mainly arises not in firms but, rather, in the public sector. The share of this deficit in G.D.P. is anomalous compared to the position in other

countries. The reasons for this particularity of the Italian financial system are hence to be found largely in the relationship between the public sector and the family sector. Public expenditure in Italy largely consists of current expenditure which contributes to families' disposable income. The inadequate level of revenue from direct taxation has brought into being a mechanism whereby the public sector's current deficit is largely covered by families' financial assets. The increase in interest rates has turned this mechanism into a vicious circle continually raising the burden of debt service.

Table III.2 : Financial balances (% of G.D.P.)

	1965-67			1970-72			1977-79		
	D	F	I	D	F	I	D	F	I
Households	3.5	3.2	9.3	4.6	4.0	11.7	3.7	5.0	14.6
Corporations	-2.8	-3.9	-2.5	-4.6	-4.2	-4.3	-0.9	-4.3	-3.0
Public Sector	-0.6	0.8	-4.1	-0.1	0.9	-6.9	-2.9	-1.5	-9.9
Rest of the world	-0.3	-0.2	-2.6	-0.4	-0.4	-1.3	-0.7	0.3	-1.7

Source : National Accounts.

The tendency for the public sector financial deficit to grow is common to all three countries. In contrast, in Germany and Italy, firms' deficits registered a fall during the last three years considered in the Table. This, however, took place in Germany together with a rate of capital accumulation (I/Y) averaging a level equal to that of the three years 1970-72, whereas in Italy this fell by nearly 4%. In France there was no significant reduction in firms' financial deficit despite a drop in the rate of accumulation.

IV. THE MAIN FEATURES AND EVOLUTION OF THE THREE FINANCIAL SYSTEMS OVER THE LAST 15 YEARS

IV.1 France: Reform of the Credit System and Support for Industrial Development

Sustained and stable growth and the "rupture" of 1974

There are three "real" characteristics regarding trends in the French economy which it is helpful to recall before examining changes in the financial system.

In the first place, France began a phase of accelerated capital formation after 1965 which continued until 1974, the year of what the French call "la rupture", after which private investment entered a phase of stagnation that is still continuing today. France was "late" in comparison to Germany and Italy, which during the 1950s had already experienced a process of accelerated growth. This "late" development in France was notably stable. The trend in French investment was characterised neither by the long cycle experienced by Germany between the second half of the 1960s and the early 1970s, nor by the short and frequent Italian cycles.

In the second place, during the 1960s France had an average rate of inflation considerably higher than in the other two countries and in the 1970s this rose although not, as in the Italian case, dramatically. With respect to Germany, France, which was used to inflation, felt the inflationary shock less.

The accelerated growth and the stability of the French economy during the first phase (ie. until 1974) was not the fruit of fortuitous circumstance. Rather, this was the key objective of economic policy both under De Gaulle and Pompidou. According to the political philosophy of the General, industrial modernisation was supposed to serve France by bringing her into a competitive position on the world market and by developing strategic sectors of her domestic economy,

both of which conditions were necessary in order to sustain the primary role that the country had assumed in international politics. In Pompidou's more liberal approach it was intended to use a rapid growth in productivity to maintain the Government's social consensus and to limit domestic social conflict (Gigliobianco - Salvati).

Even though De Gaulle's philosophy implied a large element of "dirigisme", the acceleration of industrial development was not meant to be based on an extension of the public sector. The state's influence was supposed to be exercised through the planning process. This was intended to induce private enterprise to collaborate in achieving the growth targets defined at a political level.

The collapse of "pure" Gaullism was subsequently translated into a decisive orientation towards free enterprise. This was entrusted the task of investing according to the usual market criteria. With the Barre Government this orientation acquired particularly more vigour.

Support for capital accumulation without an extension of the public sector is therefore the lowest common denominator linking the three administrations (De Gaulle, Pompidou, Giscard), during the period from 1965 to 1981.

In the financial field, structural changes arising from the reforms of 1966-68 accompanied this political will to sustain the development of productive investment. In a certain sense these reforms constitute the "liaison" between the "real" and the financial aspects of the system. It is therefore convenient to analyse the evolution of the financial system in the light of these reforms.

Reforms of the Financial System

We have already mentioned the motives for the 1966-68 reforms. Around the middle of the 1960s the objective that emerged was mainly that of reducing the Treasury's intermediation in order to leave more

space to the banks. The 5th Plan expressly provided for a diminution of medium-long term credit awarded through the Treasury and an expansion of the bank's role in this sector. In the financial arena it thus carried out a liberalisation which preceded by some years those that the Pompidou administration was to promote on the "real" front.

In relation to this target, the reforms showed themselves to be extraordinarily effective. Within six years the share of "non-mobilisable" credit awarded by the banks quadrupled, rising to about 35% of the total, the relative weight of the Treasury being accordingly reduced. In this period therefore a good proportion of investment financing was outside the Treasury circuit, decentralised to the banks, and in particular the "banques inscrites" (Table II.2).

Important structural modifications affecting the banking profession accompanied this development in the field of medium-long term credit. For many "banques d'affaires", this legal status, which carried with it a number of special obligations (for example, surveillance by a government official) was no longer advantageous given that in terms of the business which the banks were authorised to handle they were now in the same position as the deposit banks. For this reason there was a drastic fall in the number of "banques d'affaires" in the years following the reform (Fournier). On the other hand, the nationalised deposit banks had moved closer to the model of the bank "à tout faire", moving through relations with the special institutions and through the acquisition and development of specialised banks.

Large nationalised, and private, banks thus operated in the same area, and where this was worthwhile, collaborated. Nevertheless, important differences remained. These, as will be seen, are fundamental both to understanding both monetary policy and the motives for nationalisation. The private banks did not have, in their origins as "banques d'affaires", a sufficiently wide base of deposits to raise

the funds that they were in a position to lend. Despite a decisive strategy of deposit expansion (Paribas and Indo Suez assumed, by the end of the 1960s, control of two banks holding many branches, Credit du Nord and Credit Industriel et Commercial) the private banks remained net borrowers on the money market whilst the opposite took place in the case of the nationalised deposit-banks. Moreover, the latter continued to be reluctant to purchase equity participations in non-financial firms thus only making partial use of the opportunities which the new legislation offered. The reform provided a stimulus to competition, specially from the "banques inscrites" vis à vis "special statute" banks. The former have profitted abundantly from the new liberal regime concerning the opening of branches. As this liberalisation was accompanied by the prohibition of the remuneration of "sight" deposits, competition was brought to bear through the acquisition, by the "banques inscrites" of various other forms of deposits. However, it is only from the Savings Banks that the "banques inscrites" succeeded in winning a further market share: in fact, the Treasury, in correspondence with the reform's objectives, performed a voluntary retreat vis à vis acceptance of deposits. The "banques inscrites" lost ground however in relation to the special statute banks and, in particular, to Credit Agricole (Table II.1).

As far as the "banques inscrites" liabilities are concerned, there was therefore a strong shift from "sight" deposits to term and saving deposits. In this respect, the reform has also had success in inducing that consolidation of deposits that ought to accompany the expansion of medium-long term banking activity. However, a more detailed examination reveals that the effective duration of the more widespread forms of deposits was relatively short and that, given the banks' failure to develop issues of bonds, the "burden of transformation" was relatively high (Gaudichet, Conseil National du Crédit 1976 and 1977). On the other hand, one can see that the banks succeeded, on the whole, in securing a high and sufficiently stable

supply of medium-long term credit to firms. This means that monetary policy has made these two phenomena compatible.

Monetary policy has thus been constrained in its attempts at stabilisation, by the need to avoid critical situations in the banks' accounts and by that of guaranteeing the regularity of financial flows.

Monetary Policy

Of the two variables, money supply or interest rates, which in line of principle a central bank can use to exercise its control, the Bank of France has emphasised the latter (Raymond, OECD (b), Coutière).

Two reasons can be used to explain this behaviour: the first, that we will not investigate here in any detail, is that of maintaining a stable rate of exchange; the second derives from the structure of the financial system.

From the financial balances it can be seen that, in France, intermediation arises substantially between only two sectors: families and firms. The credit system is thus dominated by firms' financing requirements which, to a large extent, are met through the banks. Before 1971, the latter refinanced themselves through rediscounting with the Central Bank, whilst after this date the money market began to be substituted for direct re-discounting.

On the whole, the banks' supply of liquidity from the French money market is based on transactions with the Central Bank (and with the C.D.C.) and not primarily with the public as is the case in countries where there exists a wide circulation of public securities. To a large extent the French market consists of bills admitted for discount by the Bank of France, bills representing "credit mobilisable" as well as Treasury bonds and securities issued by the special

institutions (4). The French monetary authority considers that in such a system a rigorous and direct control of money supply would be impossible without making the system highly unstable (Raymond, Couitière).

Given that the banks cannot recover liquidity by selling securities to the public on the money market any reduction of re-financing by the Central Bank would make it difficult for them to satisfy their reserve obligations. Wide interest rate variations, on the other hand, would not be compatible with the heterogeneity of the French banking system in which, as has been noted already, many banks are structurally dependent on the money market for the collection of funds. Sharp interest rate movements on the money market would generate effects of different signs and intensity for different banks which would rebound on their incomes (Joffre-Strauss Kahn, House of Commons). Moreover strong interest rate variations were considered by the French monetary authority as unwanted shocks that impede the capital accumulation process.

Not being able, therefore, to control monetary expansion directly through bank liquidity nor indirectly by means of major shifts in interest rates, the French monetary authorities have combined an interest rate policy with control of the principal determinant of monetary expansion, namely bank credit provided to the public. When control based on the interest rate no longer helped to relieve inflation monetary expansion was controlled through "l'encadrement du crédit", instrument introduced on a temporary basis on various occasions from the end of the 1950s on, and which became permanent after 1972.

In the years between the Debre reform and the Barre Plan, French monetary policy has been based on a "fine tuning" aimed at

(4) Since 1973 the money market has been organised into two departments. The first is the Banque of France department where transactions are carried between the central bank and financial institutions. The second relates to intra financial institutions transactions.

sustaining a steady growth path and containing inflationary pressures. This policy, that has achieved a relatively high rate of growth of investment paying a relatively low cost in terms of inflation, has required a series of regulations which have been accompanied by some reform.

In the field of credit control, "l'encadrement", introduced on a temporary basis in 1969-70, was to be re-adopted in 1972 with a "corset" regime based on the constitution of obligatory reserves to match credits granted in excess of the monthly limits on credit expansion fixed by the Bank of France. This instrument has been employed in a selective manner in order to limit, or exclude, effects on investments and exports.

With regard to the question of bank re-financing, a large part of the Marjolin-Sadrin-Wormser report's suggestions have been put into effect. This has allowed a considerable reduction in the practice of the Central Bank rediscounting in favour of the development of a money market with a strong secondary component. This transition from rediscounting to negotiation of securities and titles to credit on the money market has been encouraged by the practice followed by the Bank of France in maintaining its intervention rate below the discount rate. In order to prevent access to the money market from leading to an undesirable expansion of those banks structurally indebted to this market, and in order to assimilate the position of these banks to that of those with a high deposit/credit ratio, in 1971 obligatory reserves on credits were introduced, alongside those on deposits.

Finally, it is necessary to recall that, thanks to the influence that the three large nationalised deposit banks have on the Association Française des Banques, the French monetary authorities have available to them a special channel through which to limit the repercussions of interest rate fluctuations on the cost of bank credit. On a number of occasions when there has been a strong increase of the rate on the money market the bank base rate has been

kept below this through the actions of "moral suasion" on the nationalised banks by the Ministry for the Economy. In early summer 1982 the difference between the two rates was, for example, about 2 points.

"A Financial Road To Growth ?"

One can, therefore, arrive at the conclusion that, so far as concerns the period 1965-74, capital accumulation in France has been encouraged by structural transformations of the credit system and by a monetary policy highly attentive to firms' credit requirements. Nevertheless, it remains to be seen whether this policy orientation aimed at providing support to accumulation through the manipulation of credit has forced the French economy into what, in the Italian case, has been called "the financial road to growth" (Andreotta). This consists in forcing economic growth towards an "artificial" process of accumulation that has the ultimate effect of inducing firms into a position of increased financial disequilibrium.

At first sight, it would seem that this has also been the case in France. As has already been shown, the period from the second half of the 1960s until the present day can be subdivided into two phases. The first, one of accelerated accumulation, continued until the beginning of 1974; the second, which began in 1974, was marked by a critical situation in firms' financial accounts and by stagnating investment (Table IV.1).

Nevertheless, with a more thorough investigation this "first sight" impression shows itself to be unfounded. As a result of the sustained process of capital accumulation, that had made it possible to achieve continual gains in productivity, firms' profitability did not fall appreciably until 1974. The drop in profits was registered concomitantly with the depression of 1974-75.

Table IV.1 : France: Operating accounts of private non-financial corporations (% on value added)

	1965	1968	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979
Wages + social security contr.	60,5	61,8	63,9	64,3	64,0	64,4	66,0	68,5	69,1	68,8	68,9	68,3
Indirect taxes (net of subsidies)	13,3	8,9	7,5	7,2	7,1	8,0	6,9	6,8	6,4	6,8	6,9	7,4
Gross operating	26,2	28,3	28,6	28,4	28,8	27,6	27,1	24,7	24,5	24,4	24,2	24,3
. net interest payments	2,7	3,6	5,1	5,6	5,5	5,6	6,9	6,1	5,7	5,6	5,2	5,0
. gross saving	14,5	15,9	14,5	14,1	14,4	12,3	10,2	10,1	10,4	10,2	11,2	11,8

Source: INSEE, Comptes de la Nation

On the other hand, the structure of firms' financing was kept in equilibrium until 1974 by a contribution of self-financing approaching 50% and of medium-long term liabilities of about 25%. This indicates that the financial system had not worsened firms' indebtedness nor had it oriented such indebtedness towards short-term borrowing. Firms' financial equilibrium broke down in 1974 when, at the beginning of the recession, firms proceeded to massive speculative stocking. Falling profits provoked by the recession led to very heavy recourse to short-term banking indebtedness. Entering into the heart of the recession (1975) in conditions which were already critical vis à vis indebtedness with the banks, firms drastically reduced the level of investment and began a process of financial stabilisation by substituting medium-long term credit for bank overdrafts (INSEE 1976). The policy of reflating the economy, initiated in the autumn of 1975, stimulated demand through the manipulation of the Budget and support for family incomes helping to re-equilibrate firms' accounts. However, this policy was not maintained for a sufficiently long period to give results because of the productive capacity created by the preceding expansion.

By the end of 1976 Barre's deflationary policy took place. The ensuing "freeing" of prices enabled profits to recover but did not succeed however in stimulating a resumption of investment. What has been called the "rupture of 1974" in the French accumulation process was caused by the same factors that affected the other advanced economies. The financial system seems to have adapted itself to the requirements of the high level of industrial growth, experienced between 1965 and 1974, without provoking "feedback effects" on firms' behaviour.

Monetary and financial policy during Barre's government

The 1974-75 crisis in France hit an economy whose experience of sustained and stable growth was rather exceptional among the O.E.C.D.

countries. The economic policy imposed by the Barre government derived from an awareness of this peculiarity and from that of the necessity to reabsorb the effects of the "oil shock". At the basis of the turnabout of economic policy introduced in 1976, there were substantially two orders of consideration. The first referred to the capacity of the French economy to return to the rates of growth and accumulation which had been experienced previously. In effect, it was hardly thinkable to return and stick to the pre-crisis growth path, notwithstanding the optimistic forecasts of the 7th Plan (Bloch-Lainé); this not only because of the constraints arising from foreign payments balances but also, and most importantly, because of the dimensions already reached by the national productive apparatus. The second order of considerations related to the fact that the consolidation of France's economic position in international competition required a stable exchange rate. To this end, re-balancing of external accounts was essential and therefore became a primary target. In order to achieve this target Barre chose an internationally credible policy instrument capable of sustaining France's international credit: the fixing and publication of monetary expansion "targets", according to what was rapidly spreading as economic orthodoxy, particularly in Germany, the economically strongest country in the E.E.C.

The readjustment of another set of accounts, namely those of public finance, is probably better to be considered as a complement to the declared monetary orthodoxy rather than as a primary objective. The "exceptional" public sector deficit that Barre programmed to reduce did not exceed 2,5% of G.D.P. and was largely justified by the adverse trend in revenues owing to the collapse of the level of activity following the crisis. On the other hand, the Barre government, while it reduced direct state intervention in accumulation, allowed public investment to expand at a relatively sustained rate (almost 14% per annum in the period 1975-80), especially through the contribution of nationalised firms. Despite what the ideology proclaimed

by Barre would have us believe, there has been no significant "rupture" in the previous tradition of support for accumulation not by means of a budget deficit but through the composition of public spending.

Within this framework, the slogan of the Barre government, the struggle against inflation, is to be seen primarily in relation to the external balance. The emphases put on the social effects of inflation constituted rather a means to promote the internal acceptance of the new course of policy.

The Barre policy's liberal character, that emerged in the so-called "second phase" of application of his programme (price controls were abolished in 1978 after twenty-five years of application), was based on confidence in the resumption of private investment following a rise in profitability. It is precisely this assumption which has been the real failure of the programme: the attainment of the third readjustment (balancing of firms' accounts after the balancing of foreign accounts and of public budget, did not lead to a resumption of accumulation. This drove the government to make a whole series of stimulatory interventions to which, on the whole, there was no significant response and which often contradicted the "liberal" spirit of the programme.

What have been the effects of Barre's policy on the French financial and credit system? To what extent can one speak of an effective change of course in comparison to previous experience?

At the level of monetary policy the change is more apparent than real. The financial structure remained unchanged and policy has therefore continued to be based on control of credit demand rather than on that of supply (OECD (c), Fröchen-Maarek). Even before the autumn of 1976, when it was decided to publish monetary targets, monetary policy required forecasting of the expansion of money supply in order to fix the maxima for the "encadrement du credit". With the

Barre programme these forecasts were made public to exploit the "publication" effect, especially at an international level. Nevertheless the preoccupation with preventing sharp fluctuations in the rate of interest remained, even though, in conformity with the objective of readjusting foreign balances, the conduct of monetary policy was oriented less towards "fine tuning" and more towards medium-term stabilisation.

Interventions relative to the functioning and structure of the credit system can be reduced without excessive exaggeration to a single aim: the re-launching of private accumulation in competitive conditions. With the Barre government one registers a systematic challenge to the previous industrial growth policy and to the relationship between this policy and the credit system. Symptomatic in this respect is the draft of the Hannoun report. This was based on a retrospective analysis of the privileged credit concessions given to priority sectors. It strongly argued the advantages of moving from a sectoral industrial growth policy to the creation of conditions in which the most efficient firms could emerge spontaneously and in which it would be the capacity to produce competitively, rather than the choice of product, that would be rewarded. The multiple initiatives (in 1978, in 1979 and in 1980) aimed at stimulating the creation of new firms and the development of the small and medium-sized ones, were part and parcel of this project. Regional development objectives were also oriented towards private initiative, stimulated and assisted by public and semi-public institutions. To this end, the "Mayoux report" puts forward evidence for the necessity to review the policy of the banking system (and in particular of the nationalised banks). These, it argued, are inclined to use local branches only for deposits while transmitting decisions relative to lending to Paris, even for relatively modest credits. The consequent centralisation of credit, both geographically (in the principal financial centres and, especially, in the Paris area) and by sector

(the privileged position of large firms) is accused of being an important obstacle to the promotion of regional development via the activity of smaller companies. The "Monory law" ("Measures for orienting savings towards the financing of firms" in 1978) was directed to the strengthening of firms' self-financing, again with the objective of stimulating investment.

As a result of legislative intervention between 1966 and 1972 the French financial and credit system appeared, on the eve of the 1981 nationalisations, very different in comparison to fifteen years before. The main guidelines on which this structural intervention policy was built were the opening of a much wider possibility for action by the three large state banks, a stimulus to competition within the banking system, a reduction of the Treasury's intermediation role and, more generally, "de-provincialisation" of the whole system. Some results were achieved rapidly, others remained as permanent problems.

In the field of medium-long term credit the reduction in the Treasury's intermediation role in favour of the "banques inscrites" was extremely rapid. So far as deposits were concerned, however, while initially the "banques inscrites" gained ground in comparison to the Savings Banks, the latter subsequently re-asserted themselves. This was also true of Credit Agricole which, thanks to dynamic management, continued to exploit its privileges. In the summer of 1978 the Association Française des Banques sent a strongly-worded memorandum to the Government with regard to the "privileged circuits" and, in particular, Credit Agricole (AFB). It underlined, amongst other things, the fact that this bank's privileges enabled it to achieve a level of deposits well above the needs for credit of the category of borrowers that it served; furthermore, it allowed of the existence of a double intermediation circuit that exploited the "banques inscrites" requirement for funds through the placement of the excess deposits on

the money market. An accord was reached in November of the same year, and approved by the Cabinet, on the basis of which two-thirds of Credit Agricole's profits were subjected to the same company taxation as that paid by the banks. In return, Credit Agricole was allowed to enlarge its field of operations, operating in conditions closer to those of the "banques inscrites". Even after this initiative however the "cloisonnement" of the credit system remained one of the main structural problems inherited by the Mitterand administration.

Despite this last characteristic there cannot be any doubt that, during the 1970s, the French financial system has been "de-provincialised" by means of a considerable opening up of the system in its relations with abroad. The principal channels for this internationalisation process, furthered by certain French foreign policy initiatives, were the development of export credits and increased recourse of large firms to credit on the xeno-currency markets.

The Mauroy government's nationalisations

The transformations induced by the policy followed towards the French financial and credit system appeared to be dominated by the objective of adapting it to the need to sustain a high level of capital accumulation. This, as we have seen, was a constant preoccupation of governments in the period that we have examined. The Barre government, that tempered a monetary policy aimed at sustaining France's international prestige with various initiatives aimed at promoting investment, was no exception to this rule. The French financial and credit system has thus gradually moved towards a structure which, with respect to the 1960s, was intended to be virtually independent of Treasury intermediation and to be based on the co-existence of a mixed bank system with public special institutions, decentralised so as to collect and develop entrepreneurs' energies wherever they appeared. According to the Mauroy government's official declarations, the intention of the nationalisations was to encourage this tendency.

The nationalisation of the banking system has brought under the state's control about 90% of the "banques inscrites" branches accounting for 88% of their deposits and 78% of their loans. The Government's slogan of "banalization et decentralization" signifies a commitment to continuing to work for a unification of the conditions in which the "banques non-inscrites" and the "banques inscrites" operate. (The A.F.B. thus has a new reason to ask for protection from the privileged circuits, namely that of representing state property). Decentralisation of credit functions is also implicit in the vast governmental programme of regionalisation.

One of the ideas guiding bank nationalisation is that of stimulating investment financing. It is believed that the expansion of the mixed banks, already encouraged by preceding policies, can be accelerated by means of the "state mixed banks". The pressures on the banks to assume participation in firms, exercised in the spring of 1982, should be understood in this context. The coupling of the state mixed bank with large state-owned industry (which itself has been expanded by the nationalisation of large private industrial groups) is intended, according to the logic underlying nationalisation, to increase capital accumulation eliminating the uncertainties concerning reinvestment of profits and availability of external financing. The long phase of stagnation of private investment, the main failure of Barre's policy, is thus expected to end. If, in this respect, the Mauroy government's nationalisation objectives are the same as traditional French policy over the last fifteen years, the question about their efficacy still remains.

From the strictly economic point of view the question is simply that of the coherence between the socialist government's economic policy and the shape of the credit system. To the thesis according to which the credit system inherited from the preceding administration was incoherent with the new economic policy one can oppose an evaluation of the experience of the last fifteen years. This experience does

not testify in favour of the necessity of nationalising the banking system. There do not seem to have been structural constraints on capital accumulation either during the strong previous expansion or during the following phase of stagnation. The latter can be explained by two causes: the restrictive impact of economic policy and the presence of a large, recently-created productive capacity in French industry.

In order to stimulate investment a reflationary strategy using the classic (in France) instruments of public investment programmes financed by public intermediaries might have been just as successful as nationalisation. There is some reason to believe that the path followed by the Mauroy government is less effective in stimulating accumulation than the former alternative. In the short term, the nationalisations have certainly been an element in reducing the international acceptability of France's "against-the-stream" policy of reflation. Being exposed on many fronts, and particularly in the field of structural reforms, loss of international credibility has prevented the socialist government from succeeding in adopting the kind of "Keynesian" policy, used during many turbulent periods of the 1970s; a policy which even the Barre government abandoned only in part.

At the structural level one may only advance hypothetical considerations. In the period that we have examined, the French economy has been managed by a highly integrated public and private power elite operating in both industry and finance. The Mauroy government's nationalisations have obviously affected this. If, in the short term, this élite were to be transformed so as to force accumulation there would then be the risk of entering a "financial road to growth" analogous to that experienced in Italy. If, on the other hand, the government abandoned a use of the reforms for short term political objectives, while they would have little immediate effect they would nonetheless constitute a decisive turning-point in the approach of the French credit system to a "finance - industry" model that could have the positive characteristics of a mixed bank together with the guarantees constituted by a state ownership.

IV.2 GERMANY : THE FINANCIAL SYSTEM AND ANTI-INFLATIONARY POLICY

A hypothesis on the motives for anti-inflationary policy

German economic policy is distinguished from those of the other two countries by its decisively anti-inflationary imprint which, for the entire period from the mid 1960s until today, has allowed Germany to achieve one of the lowest rates of inflation in the world. During this same period Germany has assumed an hegemonic role in the world economy which is, without doubt, connected to the fact that German industry has become the world's largest exporter and that the current payments balance has, for a long time, accumulated a major surplus.

The characteristics which the German economy has assumed in the last fifteen years raise questions about the conditions that have enabled the achievement of remarkable results and the possible motives underlying the particular emphasis attributed to the struggle against inflation. Re-examination of the particular conditions that lie at the base of the German growth model are outside the terms of reference of the present report. As far as concerns the motives for anti-inflationary policy it is possible to make three important observations. The first is related to the high degree of concentration in German industry and to the weight of the largest industrial groups in total exports. The second refers to the interpenetration between banks and industry, which can be described as "... the headquarters of large industrial and banking capital that represents a powerful centre of monopolistic control over the German economy" (Dal Bosco). The third observation is in reality a hypothesis, namely, that relative price stability is one of the principal conditions for the functioning of the German universal banks.

As concerns liabilities, universal banks receive both short- and medium-long term funds. As for assets, they offer the entire range of financing needed by firms, from working capital to equity shareholding.

With a high rate of inflation there is inevitably a shortening of maturities on the side of liabilities that necessarily imposes, in a prudential sense, modification in management criteria by the banks. In Germany this could have brought about the birth of new financial intermediaries, or public intervention in the management of financial flows (House of Commons). One is thinking here of France or Italy, where the high inflation rate has hindered institutions financing investments from raising medium-long term funds from the public and where the problem of transformation of maturities has been resolved through the direct or indirect intervention of the state (France), or by means of the double intermediation circuit, functioning thanks to banking administrative regulation by monetary authorities (Italy).

If this hypothesis is reasonable, it is possible to sketch an analysis in which the primary role assumed by the German economy is closely tied to the working of a restricted group of industrial firms, tied in its turn to the universal bank system which functions to deter inflation delegating the essential maintenance of monetary stability to the central bank. This particular structure of bank - industry relations contains, however, a contradiction, at least as far as monetary stability is concerned. If, as he happened, safeguarding of price stability requires a strongly restrictive monetary policy this can hinder the growth both of industry and of the banks.

Monetary policy

The low rate of inflation which has characterized the German economy has been obtained by means of a compression of demand which led to a slowing-down of growth. During the period 1973-77 German GDP grew at an average rate lower than that of the other countries though in 1978 there was a significant recovery. In the period 1973-77 the ratio of gross fixed capital investment to GNP, which until 1972 had been at a level higher than in France and Italy, fell sharply,

while in the last four years it has recovered achieving higher levels even than France. German economic policy has run ahead of that of the other countries. A deflationary line was adopted earlier and with greater firmness.

The German monetary authorities have been called the "hard money men from the continent". The main justification for this renown lies in the severity of the restrictions which monetary policy has applied in the struggle to achieve or maintain monetary stability. This is first element which distinguishes German from Italian or French monetary policy.

During the period of concern to us here the years in which the Deutsche Bundesbank (DBB) took the firmest line on monetary restrictions were 1966, 1973 and 1981.

In 1966, a year in which rapidly rising domestic demand has led to a rise in prices, the DBB imposed severe restrictions on the banks' free reserves. Given that the banks were entirely dependent on these reserves for their liquidity this intermediate goal enabled the DBB to control bank credit.

From 1970 onwards it was clear that the national and international monetary markets had developed to such an extent that the banks were relying less on their free reserves and had strengthened the role of inter-bank relations outside the control of the central bank. Although the volume of reserves had been reduced to a level which had previously been regarded as "critical", credit continued to expand at a rapid rate. It was in 1973-74 however that the DBB made the changes necessary to achieve accurate control of the supply of bank credit. Faced with the way in which the banking system had adapted its behaviour to the development of the monetary market, in 1973 the DBB almost completely soaked up the banks' free reserves using the traditional tools at its disposal in the most restrictive way possible. In order for the monetary authorities to succeed they had to halt the huge inflow of

capital from abroad which in spite of the DM revaluation in Oct. 1969 and the free float vis à vis the dollar in May 1971 had made the central bank's effort to control the growth of bank liquidity ever less effective. To this end the central bank imposed obligatory reserves equivalent to 100% of the growth of non-resident deposits; on the insistent advice of the DBB the Government revalued the DM and took a series of further measures including the prohibition of interest payment on non-residents' deposits and a requirement that purchases of German securities should be subject to authorization. Direct flows of capital to German firms in the form of financial credit granted by the Luxemburg subsidiaries of German banks were countered by making it obligatory to deposit 50% of the credit in a non-interest-bearing account with the DBB.

Having blocked the inflow of capital from abroad and eliminated the possibility of refinancing the banks, the central bank was able to adopt a highly restrictive monetary policy. At the same time it prepared itself to exert direct control over the creation of central bank money (CBM) defined as the sum of currency and of the reserves covering the banks' domestic liabilities. Given that the discount "ceilings" had already been nearly fully used and that normal lombard loans had been suspended, the DBB continued until the spring of 1974 to supply the banks' marginal requirements for CBM on a discretionary basis at rates of interest higher than discount rate. In order to anticipate and counteract large-scale fluctuations in interest rates, the bank had provided itself, during 1973, with a number of tools of "fine tuning" capable of being used in an arbitrary and unforeseeable way. In December 1974 as part of this policy the DBB publicly announced its growth target for CBM which for 1975 and the three following years was fixed at 8% per annum.

The combined effect of the severe credit squeeze of 1973 and the publication of the target for monetary expansion led to a substantial reduction in the rate of inflation. During the period 1975-1978 mo-

netary policy was moderately expansionary while the effective increase in money supply was consistently in excess of the goals fixed.

Between the early months of 1974 and the spring of 1975 the gradual suspension of the measures taken by the government in 1972 and 1973 led to a renewed capital inflows from abroad. These speculative flows were discouraged by the DBB by an increase in minimum reserves, proportional to the growth of deposits by non-residents. As a result demand for credit by major firms was shifted onto the Euromarket. Every time that the obligatory reserves mechanism tended to hinder flows of Eurocapital towards national banks the excess supply of capital on the Euromarket tended to push down eurointerest rates. This reduction increased the differential with respect to rates of interest on the national money market which thus became less attractive for German firms seeking finance (Matthes). The difference in interest rates and the behaviour of the German banks which in these circumstances encouraged firms to contract Eurocurrency loans via their foreign subsidiaries, led to a shift in the flow of foreign capital directly towards firms. In this way companies were allowed to satisfy their requirements for external finance without creating tensions on the national credit market. De facto this led to an expansion of CBM in excess of the published targets. Given that this expansion derived from increasing demand for credit needed to sustain an expansion of production it was nonetheless compatible with stabilization.

Although compatible with anti-inflationary policy the fact that the growth of money supply consistently exceeded the targets announced endangered the credibility of the figures published. The DBB was thus led to fix its targets as a range explicitly defining the circumstances in which expansion would proceed at a lower or higher rate (DBB, Monthly Report, Jan. 1979). In this way the flexibility of monetary policy was placed on an institutional footing.

The early months of 1979 saw the beginning of a new period of restrictions. In February 1981 these became more severe; the DBB, having suspended for the second time "normal" lombard loans to the banks, for a number of days did not even grant "special" loans. As in 1973 this led to a sharp increase in interest rates. During the last months of 1979 and 1980 the situation was the opposite of that between 1972 and 1974; now the DBB aimed to neutralize, at least in part, the pressure on bank liquidity deriving from the massive withdrawals by non-residents due to the high level of international with respect to German interest rates and the uncertainties on the external value of the DM.

Since the autumn of 1981 the DBB has used "fine tuning" to bring about an increase in bank liquidity and thus a gradual but persistent decline in both short and medium-long term interest rates.

One can thus identify a second distinction between German monetary policy and French and Italian policies. We have seen that in order to achieve its targets the DBB uses market-oriented policy tools. Following the abolition (1967) of control on the interest rates on deposits and loans, with rare exceptions, the German authorities aim to influence the relative profitability of different options by the credit institutions and thus by savers and investors rather than substituting official for private decisions. Thus, the DBB's controls change the environmental conditions in which decisions are taken rather than acting directly as would be the case with ceilings on loans. As has been observed by the DBB itself (House of Commons) the justification for this behaviour lies in the fact that direct action on the assets of individual banks would change the competitive positions of the different banking groups, a view confirmed by Italian and French experience.

On the contrary to the policy adopted by the Bank of Italy and the Bank of France, which for a decade now have been using administrative controls not only to achieve a more timely regulation over credit but also to influence its composition (by size of loan and by economic

sector) the German central bank has restricted its action to the determination of the macro-economic conditions in which the banks operate, leaving the latter free to select credit as they see fit.

Further on we will see the conditions under which the severe and non-discriminatory behaviour of the German monetary authorities has succeeded in avoiding excessively negative repercussions on the capital accumulation process.

The rationale of monetary policy

The constitutional significance of the maintenance of monetary stability gives German monetary policy a key role in general economic policy. During the period examined here the DBB has ended up by shaping much of German economic policy. Here the German experience is clearly very different from that of France or Italy even though in this latter case central bank policy was also extremely important in influencing the formulation and the conduct of economic policy. In France monetary policy has "accompanied" government policy on economic growth. In Italy monetary policy acquired exceptional importance during the period 1965-75 when it took upon itself the "anomalous" objective of creating the conditions for (rather than merely accompanying) capital accumulation. In Germany on the other hand monetary policy, while pursuing the "orthodox" target of monetary stability, has never lost its awareness of the effects on capital accumulation and industrial growth.

According to the argument advanced earlier the policy of the DBB is influenced by the need to maintain the universal bank system. The objective of maintaining monetary stability is held to be a particularly significant consequence of this fact. What has been assumed here is that the German banking system is particularly sensitive (more than the Italian or French systems) to variations in the rate of inflation sufficiently large to induce the owners of financial wealth

to shift their preferences from medium-long term to monetary assets. It is obvious that these variations should be measured with respect to the "normal" rate of inflation in any given period.

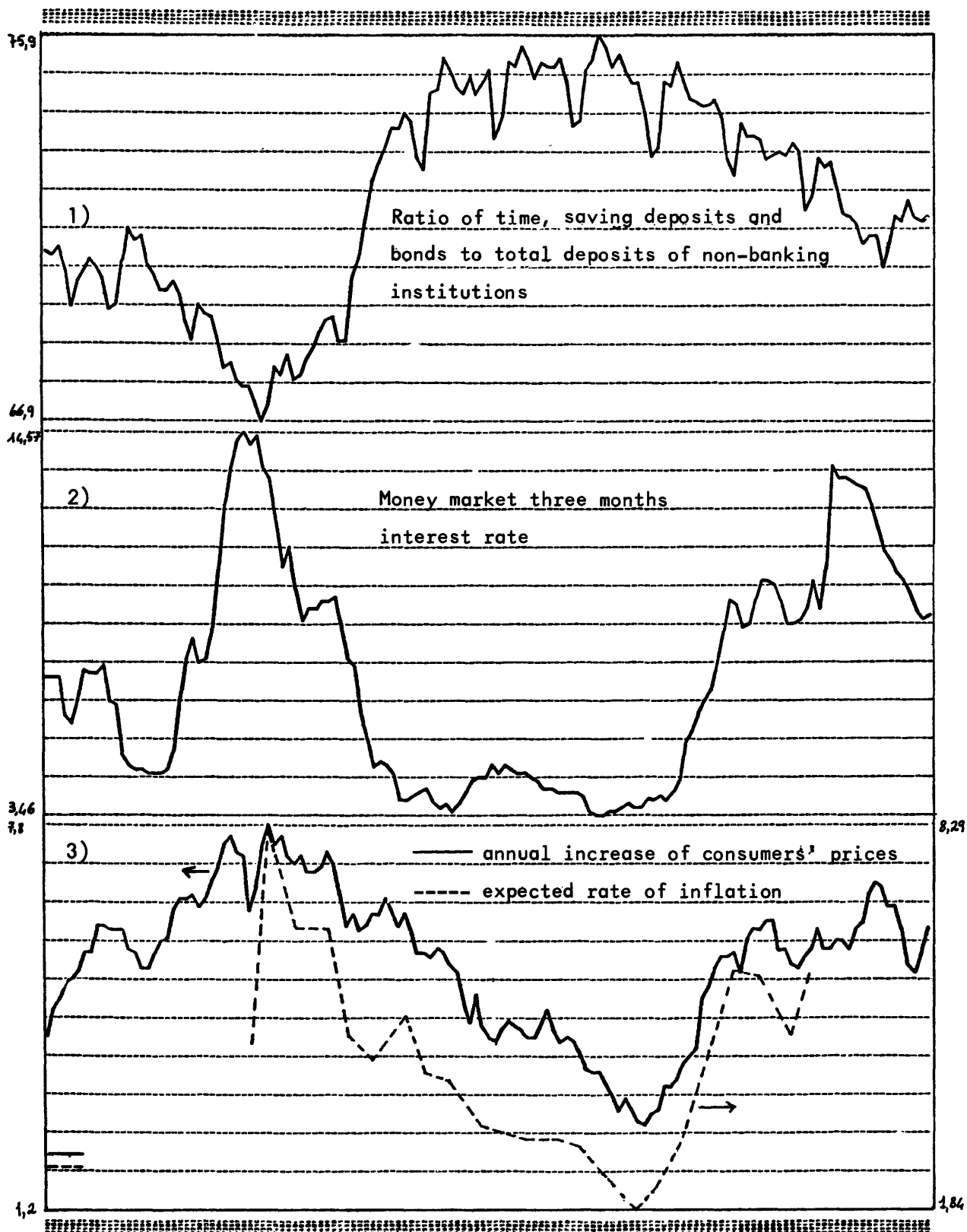
The logic followed by the DBB in the conduct of monetary policy seems to confirm this argument and the hypothesis on which it is based. The two periods since 1970 in which tight monetary restrictions were imposed (1973 and 1981) were both preceded by a fall in the importance of long term bank liabilities (Graph IV.1).

In both cases the policy adopted by the DBB led to drastic increases in money market interest rates. In both cases, intervention by the bank was extremely firm and lasted only a very limited period of time. No longer able to re-finance themselves from the central bank, the banks increased the pressure on the money market and sold bonds. In this way the increase of money market rates was immediately transmitted to those on financial markets. Interest on bank deposits adapted to these rates. The end result of this adjustment was in both cases a change in the composition of the banks' liabilities and an increase in the share of their medium-long term liabilities (this effect is less visible in 1981). The fact that this result was obtained was obviously due to the credibility of the signal from the central bank showing its firmness in the struggle against inflation. In practice monetary policy seems to have been based on changes in the public's inflationary expectations rather than on actual trends on prices (see Graph IV.1). It is the former which determine the public's options with respect to the composition of its financial portfolio.

The credibility of the DBB's policy has been strengthened by the tough approach taken towards monetary restrictions. Here we discover one of the reasons why the DBB has always opposed any form of indexation. Indexation would end up by neutralising the effects induced by changes in portfolio composition by the owners of financial wealth (Matthes (b), Andreas). Although the policy lines adopted by

the central bank for the control of the stock of money imply extremely volatile interest rates (as is also the case in the USA) the DBB has preferred to concentrate sharp changes in interest rates in a very short period of time after which fluctuations are maintained at a relatively limited level. There are two motives which justify this extremely rigorous approach when it is necessary to break inflationary expectations and the pragmatic line taken during normal times. The first is the need to guarantee the effectiveness of the mechanisms used to control the composition of the public's financial assets; the second is that frequent fluctuations in rates would damage banks primarily committed to medium-long term loans bearing a fixed rate of interest. By adopting a line of rare, yet drastic, intervention the central bank limits the negative effects on bank profits to a limited number of short periods.

The monetary policy followed by the DBB has not only limited the negative effects of deflationary policy on the banks but has also exerted a positive influence on their growth. As far as foreign business is concerned, the prospect of revaluation of the DM, together with a generally "market-oriented" attitude (with occasional corrections) to capital movements, has made it possible for the banks to internationalise, enormously expanding their foreign operations. The market for DM bonds, largely fed by issues by the banks and completely controlled by the banking system, has reached significant proportions. During the 1970s the foreign subsidiaries of German banks, particularly in Luxembourg, have rapidly increased in number. Domestically, a large proportion of the growing volume of resources required to finance the public debt, especially since 1979, has been obtained using medium-long term bank loans. In this way the financing of the public sector has been achieved without reducing the role of the banks, as has occurred in Italy.



GRAPH IV.1 : Germany: Structure of bank's liabilities, interest rate and inflation (1971-1981)

Source : 1. DBB Monthly Report
2. DBB Monthly Report
3. DBB Monthly Report and F. Papadia, V. Basano

Competition and Financial Stability

Although the growth of the German banking system has not been damaged by anti-inflationary monetary policy, and although it has met with little competition from the capital market or from other financial intermediaries, competition within the system itself has sharpened. Since the early 1970s there has been a structural change in the system which has pushed it towards further "despecialisation" (DBB, Monthly Reports Apr. 1971, May 1974, Aug. 1978). This has occurred at two different levels: on the one hand, within the system taken as a whole, on the other within individual banking groups. Compared with the situation in the first half of the 1960s the specialised credit institutions have suffered a reduction in their share of the market. This has particularly affected the "mortgage banks", specialised in long-term credit, and the special institutions, engaged in providing credit for industries in crisis, backward regions, and small- and medium-sized enterprises. There has also been a slowing down in the growth of the "private bankers" who, depending particularly on the money market, have suffered severely during periods of restrictive monetary policy. An increased market share on the other hand has been taken by credit cooperatives (whose credits, since 1974, have no longer been restricted to cooperative members) and by the central institutions of the savings banks. There has also been a slight increase in the share of the big banks and the regional banks. It is these three groups of banks (the credit cooperatives, the savings banks and the commercial banks) which have shifted the composition of their activities towards further despecialisation. As a result, their respective fields of operation have moved closer together, so far in fact as to reverse the previous pattern of market domination in the granting of short term credit, where it is no longer the big banks but the savings banks which hold the largest share. Credit cooperatives and the savings banks have also been increasingly active in the syndicated issuing of shares by firms, although this activity is still do-

minated by the big banks. On the other hand, it has been mainly the big banks which have intensified their activities on the international money and capital markets, to a large extent through the activities of their foreign subsidiaries (DBB, Monthly Report 1978). The internationalisation of the banking system, the fluctuations of prices and exchange rates on world markets, the intensification of competition among the banks and the severity of the monetary squeezes imposed by the DBB have revealed the potential for financial instability implicit in a relatively unregulated system. It is this which led to the only "structural" credit policy measures taken in Germany during the period under examination.

In 1973 and 1974, when monetary restrictions were extremely tight, Germany witnessed the collapse of ten banks. The German authorities responded introducing modifications to the 1961 banking law, the least restrictive of those in the three countries. The changes approved in 1976 were motivated by concern over the stability of financial institutions. As well as abolishing those credit institutions legally classified as "individual banking companies", the new banking law provided the authorities with increased powers of control allowing inspections of credit institutions even if there is no special reason for them and no longer, as established by the 1961 banking law, only those inspections for which there are "well-founded motives". It should be observed that the new banking law also provided for a deposit guarantee fund which replaced the old "emergency fund" which had covered only certain kinds of deposit up to a fixed ceiling. The new guarantee of deposits is on a voluntary basis and takes account of the specific differences between the savings banks, the credit cooperatives and the commercial banks.

A further important change in the banking law concerned the reduction of the overdraft limits for large loans, that is, for individual loans to a value in excess of 15% of the assets of the credit

institution. Not only was there a reduction in the maximum volume of credit which could be granted to an individual client; at the same time the formula of the law was changed from a recommendation to an explicit prohibition. It is of interest to quote the dissenting opinion, limited to this latter modification, expressed by the "Central Credit Committee", which includes the representatives of the business associations of the various different forms of credit institution. According to the Committee, the change in the overdraft ceilings could not only exert a significant effect on the economy as a whole, but could also "push many credit institutions towards medium scale, and thus relatively riskier, operations", while at the same time "inducing an acceleration in the phenomenon of concentration with negative effects on the structure and on the level of competition of the system (Lovato).

This reaction by the banks to the changes in the regulations on overdraft ceilings raises the question of the relations between the universal bank and industry and can only be understood if one bears in mind the scale of firms within the sectors least damaged by the restrictive monetary policy.

Contrary to what one might expect, the use of market-oriented policy tools has allowed monetary policy to achieve a degree of selectivity during restrictive periods. This fact constitutes one further justification for the DBB aversion to the administrative regulation of credit, as applied in France and Italy. Market-oriented policy tools have not only left relative competitive positions within the banking system unchanged; at the same time they have made it possible to be selective in the granting of credit.

During periods of monetary restrictions this selectivity has operated in favour of large firms. The main channel through which it has operated has been the behaviour of the banks and especially of the three big banks and the central institutions of the savings banks which have a very close relationship with large companies.

Except during the period of the compulsory deposit on foreign credits, funds from abroad guaranteed large German companies' the external finance they required. During the 1970s this foreign channel for finance, which on account of the nature of the operations involved and of their scale was a monopoly of large firms, provided on average more than 20% of external financing of non financial companies. This selectivity of monetary policy has been explicitly confirmed by Helmut Schlesinger, the former vice president of the Bundesbank, who has stated that when the central bank's market-oriented policy tools are employed to restrictive ends it is particular sectors of the economy and especially small and medium-sized companies which suffer. According to Schlesinger, although the DBB is not unaware of this discrimination the only way for it to take a more selective approach would be to encroach on the area of policy making reserved to parliament and the government (Schlesinger). If one also bears in mind the reduction in the market share of the special credit institutions, the majority of whose role is to channel credit to small and medium-sized firms it becomes clear how far the supply of credit to these companies has been rationed. The de facto selectivity of German monetary policy is fully coherent with Germany's industrial structure, specialised in those export sectors dominated by large enterprises. One may thus understand the concern expressed by the Central Credit Committee as regards the reduction of the overdraft ceilings on large credits. These, the committee believed, could induce the credit institutions to engage in smaller scale operations involving small and medium-scale enterprises hit by restrictive monetary policy and therefore implying a higher risk element than credits to large companies.

The way in which small enterprises have been hit is confirmed by the increase in the number of insolvencies during the 1970s. "Since 1970 the number of insolvencies has increased very rapidly ... from an average of 500-600 cases per year during the 1960s to 1861 cases in

1973 and 1652 in 1977. It is interesting to note that during the 1970s more than two thirds of all insolvencies were of firms which had been on the market for at least 8 years" (Dal Bosco). This latter observation shows one of the limitations in German industrial strategy: the way in which this strategy inhibits innovation by new firms.

The existence of a privileged relationship between the banks and large enterprises is closely tied to the way in which the banks can control the latter. As is well known the universal bank owns industrial shares, exercises the voting rights deriving from the shares deposited with the bank by its clients (the "Depotstimmrecht") and has its representatives on company boards.

This "triple" influence of the banks on industry and above all their right to own shares in industrial companies has given rise to heated debate and to various proposals for reform. The motive for this concern is on the one hand the acceleration of industrial concentration with an increase in mergers and a consequent reduction in competition, to which German law assigns a "decisive role in regulating and stimulating the economic process", on the other the possibility that the credit system could abuse its power to dominate industry in the way described by Hilferding in "Finance Capital".

According to the "anti-monopoly commission" set up as a result of the new "law against restrictions on competition" passed in 1974, the credit institutions' holdings in firms in non-financial sectors distort competition both among firms, - firms in which the banks have holdings receive preferential treatment - and among the banks themselves. Here it is the large banks with their role as major holders and purchasers of industrial shares which find themselves in a privileged position. The commission thus recommend that banks should not be allowed to purchase more than a 5% holding in non-banks, except in sectors assimilated to banking or when such holdings are ne-

cessary in order for the banks to fulfil their proper function (as in the case of company recovery programmes).

These recommendations were limited to the banks' direct holdings which in German manufacturing industry as a whole account for only 2,8% of the total capital of companies (although the banks holdings are at a higher level in certain specific sectors such as brewing). What the commission did not consider were the shares deposited with the banks (50% of the total amount of shares in 1974) and for which the latter exert voting rights (Immenga). Given that only an insignificant proportion of share-holders give instructions prior to meetings it becomes clear how the influence deriving from this "right" is even greater than that due to the direct ownership of shares. This is confirmed by the extent to which the Board Chairmen in the main companies are representatives of the three big banks.

The "Study Commission on Basic questions concerning credit" (Gessler) set up in 1974 by the Minister for Federal Finance made even blander proposals for reform. The commission expressed the view that the purchase of holdings, the exercise of proxy voting rights and the nomination of representatives on company boards did not imply that the banks were following a policy of concentration outside the banking sector nor that they had succeeded in reducing competition within the banking system. It went on to propose that holdings should be limited to 25% plus one share of a company's capital, excluding shares purchased in the public interest (as in the case of company recovery programmes) or on a temporary basis; that permanent voting rights should be abolished and replaced by a system in which proxies have to be renewed every 15 months; that the banks should be obliged to request individual instructions from their clients before all important company meetings and finally that the names of the members of company boards should be made public (Gessler).

These proposals derived from an analysis, encouraged by superficial criticism from political circles hostile to the universal bank, foundered in a bog of minor detail without facing up to the key problem raised by the Federal Banking Supervisory Office of the relationship between the universal bank and financial stability. Insofar as concerns the peculiar relationship in Germany between banks and companies, the Gessler Commission recognized the possibility that the former might exert a degree of influence over the latter. The majority of the Commission did not believe however that this actually occurs. One thus sees confirmed both the conpenetration of finance and industrial capital and the desire not to change the underlying financial structure. This does not mean that in Germany today industrial capital is dominated by finance capital. What it does mean is that any discussion of the ability of the German financial system to meet the requirements of the economy requires this point to be clarified looking for the limits of a model of growth based on a highly concentrated industrial and financial structure.

IV.3 ITALY : THE CONCEPT OF "ORDINARY CREDIT" AND THE EVOLUTION OF THE FINANCIAL SYSTEM

The flexibility of banking legislation and the importance of the central bank

Over the last twenty years the Italian business cycle has been marked by short, yet intense, periods of expansion followed by prolonged periods of recession. On the basis of the usual indicators it is practically impossible to identify any consistent or dominant trend for the whole period. Up until the late 1960s Italy benefitted from a high degree of price stability; from 1973 onwards the rate of inflation has been one of the highest in the OECD with annual price rises consistently in the two figure range. In a very short period of time the unusually large surpluses on external current account which marked the years between 1964 and 1972 had been replaced by dramatic deficits (1973-1976) followed by a spectacular recovery (1977-1979).

This unstable, "neurotic" performance makes it impossible to trace the evolution of the financial system to a consistent trend in the economy itself or in economic policy. It is true that there has been much use of monetary policy and a diversification of the policy-tools available in this field, surrogating for the lack of an effective fiscal policy. It is also true that this has affected the Italian financial structure. Nonetheless there exist basic features of the Italian financial system which are a cause rather than a consequence of monetary policy. The growing demand for finance from the public sector, while undoubtedly influencing the functioning of the credit system seems equally inadequate as a point of departure : some of the characteristics of the system are in fact independent of this phenomenon.

A good point of departure is the peculiar position in which Italian legislation places the banks vis à vis those in France or in Germany; this is obviously a prior consideration to monetary policy or to the financial requirements of the public sector. As has already been noted, the peculiarity of the Italian banking system is the following: that the law, while failing to define "prototypes" of banking activity, as in France, does not leave this to the initiative of the bankers, as in Germany. On the one hand, this law establishes the principle of the separation of banking activity from that of firms - absent in the legislation of the other two countries - on the other it leaves it to the monetary authorities to determine the structure of the banks' assets, either through active intervention or by tacit consent. As a result, a description of banking activity as contemplated by Italian legislation requires the concept of the "ordinary credit bank" (see page 11). It is the monetary authorities which have the responsibility for determining the forms which this may assume and thus what they deem to be the optimal financial structure for the system; no changes in legislation are required. It is this flexibility that explains the longevity of Italian banking law.

As a first step it is thus necessary to identify the main characteristics of the financial structure which the monetary authorities, and particularly the Bank of Italy, have forced or allowed the system to adopt. It will then be necessary to ask how far these characteristics have proved themselves adequate to the requirements of economic growth.

It was only at the end of the 1970s that the statistics began to show signs of a reduction in the intermediation activity of the banks and thus of a change in the structure of the Italian credit system. Nonetheless the change in attitude of the monetary authorities began several years earlier, between 1975 and 1976, the period in

which P. Baffi took G. Carli's place at the end of the latter's fifteen years as governor of the Bank of Italy. On the other hand, as early as the 1963 credit squeeze, the Bank of Italy began to develop rather a clear view of what it saw as the desirable structure of the Italian credit system, of the roles of the various intermediaries and markets and of the duties of the central bank. It thus seems legitimate, in the reconstruction of the development of the Italian financial system from the mid 1960s to the present day to define two distinct financial structures: the structure which characterized the period 1965-1975 and that of the period up to the present day.

The period 1965-1975

In order to understand the characteristics of the financial system which emerged during this period it is necessary to recall the two alternatives which were opened to the monetary authorities. They could limit the banks' importance in the field of pure commercial credit thus adopting the "strong" version of the principle of credit specialization; alternatively they could allow the bankers to extend, directly or indirectly, their activities into the field of medium-long term credit. In 1958 the Bank of Italy had opted for the first of these alternatives. Given the novelty represented by the Balance of Payment surplus on current account the central bank embarked on a decidedly expansionary policy avoiding the sterilization of the additional monetary base created and lowering the discount rate. Given that the level of economic activity was depressed these measures supplied the system with additional liquidity which, according to the central bank's intentions, should have favoured the development of the capital market (Marconi). In the period between the end of 1957 and the end of 1959 there was in fact an exceptional expansion in net issues on the securities markets both by the special credit institutions and by public and private corporations.

The monetary authorities' attempt to create a financial structure based on a low level of banking intermediation failed. The extraordinary economic expansion during the period 1959-1962 was financed to a large extent by the banks which expanded their lending also providing "false short term" loans to medium and small-sized firms ill-served by the special credit institutions. One of the reasons for which the capital market did not compete effectively with the banks was that major private enterprises failed to profit from the favorable situation on the stock market to develop it further (Filippi).

During the period immediately following the crisis of 1963 the monetary authorities gradually defined a different conception of what constituted the desirable financial structure. This time they no longer attempted to develop the capital market in contrast with bank intermediation; rather they attempted to reconcile the two. In 1965 the Bank of Italy launched a policy aimed at strengthening the market for bonds. While the banks were granted authorization to cover a proportion of their obligatory reserves with long term bonds the central bank intervened to stabilize prices on the market.

Although the adoption of a monetary policy aimed at stabilizing the rate of return on bonds stimulated the interest of the public, at the same time it provided the banks with an investment opportunity which was almost devoid of risk. This was a powerful incentive to increase interest rates on deposits, thereby attracting new funds. It was this line of conduct in fact which allowed the banks to limit the effects of the competition due to the massive issueing of bonds and which led them to increase the share of bonds in their portfolios. This behaviour was authorized by the Bank of Italy.

It was this approach adopted during a period when the lines of development of the Italian economy and of public intervention were under reconsideration at a political level, that determined the form

taken by the credit system and the objectives of the central bank during the period 1965-1975. It is not intended in the present work to pass judgement on the motives underlying this policy. It is worth noting however that the alternative of keeping bank intermediation low would have required the "spontaneous" development of a whole series of financial intermediaries acting as projection onto the market of companies' financial requirements. At the same time this alternative line of policy would have required a rationalization and improved organization of the financing of the public administration. It is true that even in the absence of these conditions the Bank of Italy could still have "forced" the system to adopt this solution. It is also true, however, that such a policy would not only have been of doubtful efficacy but would also have proved less than beneficial to good relations between the central bank and the banks.

These two conditions, namely the "autonomous" organization of both the public and private sectors, were not to be fulfilled until at least after 1975. Even the elite of the private enterprise system failed to produce financial institutions capable of competing with the banks or with the special credit institutions. At the same time the public administration not only did not develop a financial circuit of its own but consented to the decline of those institutions, modelled on French lines, of which it actually disposed.

The solution adopted was thus the second alternative. This occurred without any change in banking law, using the freedom granted to the bankers and the monetary authorities to determine what is to be meant by "ordinary credit". The evolution of the Italian financial system can therefore be identified to a large extent with that of the concept of "ordinary credit".

Bank intermediation and "ordinary credit"

In the structure which the Italian financial system gradually assumed between 1965 and 1975 the banks succeeded in attracting a growing proportion of households' financial assets. During this period the banks' share of family financial savings doubled and by 1975 has almost reached 75%. A further reason for the increased raising of funds was that the share of household financial balances on national income increased over this period by a good 50%. To an ever greater extent the bridging of the growing gap between savers and investors was entrusted to the bank. As a result, despite a sharp drop from 1979 onwards, the period from 1965 to 1980 witnessed a high average increase of bank deposits. Obviously this reflected the composition and volume of households' financial assets. This does not mean however that the banks simply reacted passively to a shift in households preferences. On the contrary the banks were extremely active in influencing household behaviour. The collection of funds has been the main area of competition within the banking system, a form of competition centred primarily around the interest rates on deposits. The monetary authorities, although they had the power to regulate interest rates on deposits, entrusted these to the self-regulation of the banking system, recognizing the agreements "cartels") among the banks (for further information see Biscaini Cotulla). Throughout the period there were difficulties in the application of this self-regulation, frequently referred to in the Governor's Annual Reports.

The banks thus acted as a permanent factor distorting household's preferences towards bank deposits, regardless of lending opportunities (Cingano). In this way they not only competed with the capital market, but also encouraged the public's preference for highly liquid forms of asset. This latter phenomenon, which represent a peculiar feature of the Italian system, should be viewed in the light

of the differences between the Italian banks and those of the other two countries. At least until recent times the limited volume of what are viewed formally as medium-long term lending has failed to provide a sufficient incentive for the consolidation of bank's liabilities.

Compared to the volume of funds raised by the special credit institutions the performance of the banks differs significantly between the periods 1963-1972 and 1972-1980 (Table II.7). During the former period the volume of funds collected by the special institutions grew faster than that of the banks. This was due to the issuing of a massive volume of bonds, whose sale was encouraged by the Bank of Italy's policy of stabilizing their return. The banks resisted the competition from bonds by increasing the volume of deposits to a greater extent than the volume of lending, investing the excess funds in the bonds issued by the special credit institutions. From the mid 1960s onwards there thus developed a "double intermediation" circuit which reconciled the banks' propensity to attract deposits with the need to increase the flow of medium-long term finance.

In order to identify the concept of "ordinary credit" which defines the financial structure during the decade from 1965-1975, it is useful to see the outlets found by the banks for the massive volume of resources they now administered. Bonds provided a highly important contribution to banks' assets. The share of bonds in the banks' portfolios increased continually throughout the decade. Above all however it was in the period 1964-1968 that the banks became accustomed to investing their assets in fixed-income securities and that double intermediation became a structural feature of the Italian financial system. The introduction of the portfolio constraint in 1973 institutionalized the tendency by the banks to increase the volume of their deposits regardless of the existence of lending opportunities relying on the spread between the return on bonds and the

rates on deposits. The distribution of bank credit by sector shows both the range of the credit requirements satisfied by the banks and the instability of their relations with the different categories of clients. The Italian banks have distributed funds to an extremely heterogeneous clientèle (not only various different-sized private companies, but also state participation companies, public corporations, local authorities, social insurance agencies, hospitals, etc.). At the same time however, lending has shown patterns of instability which cannot be explained in terms of normal cyclical behaviour. As has been pointed out by Onado, there is a similar lack of stability in the relationship between particular categories of clientèle and specific kinds of bank (a specific size of bank or banks with a specific form of legal status). Much of this instability - how much cannot be quantified - is due to the fact that bank credit has been used not only to supply working capital but also, in practice, to differing extents at different times, as medium to long term credit or as surrogate risk capital for public enterprise. At the same time banks lending has substituted the revenue from the tariffs on public services as well as the funds which the chaotic public finance circuit fails to distribute. One may thus observe that, despite the institutional limits on their lending, the Italian banks in practice have satisfied a range of financial requirements comparable to that met by the banks in the other two countries. In these countries the banks' choice of clientèle can be interpreted as a result of action by the legislator (France) or of a development strategy by the banks. In Italy, on the other hand, given the lack of a clear legislative definition of their role, the banks seem to have continuously shifted their priorities in line with changing opportunities.

To test the hypothesis that the variable composition of lending and assets depends on the lack of an adequate development strategy, it would be necessary to examine individual cases. Nonetheless,

considering that there existed a high degree of variability even before the introduction (1973) of administrative constraints as a permanent tool of monetary policy, it does not seem unreasonable to suppose that this was a sign of a lack of encouragement for the banks to clearly define their policy. As can be seen from Table IV.2, IV.3, the period 1963-1968 witnessed a shift of the banks' assets towards bonds and the financing of the public administration. It is true that during this period there was a change in the composition of aggregate demand in which exports and public expenditure substituted investment by private companies and by the state participation sector. The only way however in which it is possible to explain the new structure of bank lending in terms of this "real" aspect of the economic system would be to suppose the demand for credit given with respect to supply. During this period this may have been true for the state participation sector (which had just completed major blocks of investment) and for major private enterprises (which had increased its productive capacity during the boom of 1959-1963). At the same time however the boom had been due to a large extent to the investment deriving from the creation and expansion of small-scale firms, precisely the component in accumulation which disappeared in the period 1963-1968. This is the kind of demand for credit which cannot be considered as being independent of the behaviour of the banks. It is probable that the investment opportunities supplied to banks by bonds led to a rationing of credit to these firms and in particular to a lack of help for new clients. The rationing of credit to the less attractive categories of clientèle is however only one of the possible effects of the shift of the financial system towards a structure characterized by a growing role for the banks and a reduction in their entrepreneurial drive. Here one immediately notes the differences with the situation in France, where the expansion of the "banques inscrites" led to them assuming increased responsibilities in investment financing.

Table IV.2 : Italy: banks' lending and bonds holding

	1963-68	1968-72	1972-74	1974-76	1976-80
1. Total lending ($\Delta\%$)	61,6	76,4	43,1	39,7	72,7
2. S.C.I. bonds ($\Delta\%$)	133,6	101,3	195,1	25,1	80,1
3. 2/1	2,2	1,32	4,5	0,63	1,1

S.C.I. = Special Credit Institutions. Stock data.

Source: Banca d'Italia, Bollettino

Table IV.3 : Italy: banks' lending elasticity¹

	1963-68	1968-72	1972-74	1974-76	1976-80
Lending to:					
Companies					
. Large private	0,64	0,88	0,63	0,51	0,63
. Public ²	0,69	1,99	1,49	1,81	0,48
. Other	0,95	0,93	1,3	1,3	1,83
Public Admin.					
. Local Authorities	1,84	1,67	0,63	1,1	-0,71
. Soc. Sec. Inst.	n.a.	4,5	0,84	0,7	0,7
. Hospitals	n.a.	n.a.	4,4	0,29	-0,62

¹ Ratio between the share in banks' lending during the period and that of the starting year (stock data).

² From 1972 only state participation companies.

Source: Banca d'Italia, Bollettino.

In the French case the banks were able to expand their role in intermediation via their commitment to satisfying firms' requirements for finance and by lengthening the maturities of their liabilities. In Italy, on the other hand, the banks achieved the same end

by purchasing bonds and by trusting in the guaranteed solvency of the public sector (on the role of the state as direct or indirect guarantor, see Carli, Monti, Padoa Schioppa).

During the period 1964-1968 the Italian financial system thus assumed a form in which the high level of bank intermediation depended on two basic factors: on the one hand the banks' freedom to fix the rates of interest paid on deposits, on the other the outlets for their assets provided by the opportunity to purchase bonds bearing a very low risk and the methods used by the public sector to satisfy its requirements for fiancae. The high level of bank intermediation did not correspond to a similar level of responsibility in the maintenance of relations with the borrowers. The system lacked mechanisms capable of stabilizing the structure of banks' assets. As a result it was possible for the banks to interrupt the flow of credit when other forms of investment proved more advantageous, thereby altering the allocation of assets between bonds and lending and the distribution of the latter to different categories of clientèle. In the former case the banks, by purchasing bonds issued by the special credit institutions did actually finance capital formation by firms. At the same time however, given that they had no direct relationship with these the flow of funds could be interrupted at any time, without this explicitly affecting relations with the clientèle. In the latter the possibility of investing in institutions whose solvency was almost guaranteed and whose attitude to conditions was relatively undemanding deflected funds away from less attractive and more demanding clients. In the absence of mechanisms capable of stabilizing the banks' asset structure it became necessary for the central bank to intervene so as to avoid unwanted interruptions and distortions.

The financial structure, which emerged during the "quiet period" of the mid 1960s, continued to survive in the presence of the disturbances which characterized the system from 1969 onwards. After

an attempt to return to the policy of stabilizing the rate of return on bonds, which had been suspended at the beginning of 1969, 1973 saw the introduction of the constraints on banks' portfolios. During the same year ceilings were imposed on the expansion of credit. These were defined in such a way as to take account of the importance of the role assumed by the banks in financing certain sectors of the public administration. As a result the ceilings did not apply to the railways, the hospitals, the Electricity board etc.

These measures limited the banks' freedom to define the composition of their assets. Now it was the central bank which determined what composition best responded to any given situation. While the "deresponsibilization" of the banks assumed an institutional character the central bank became increasingly involved in the regulation of flows of credit. At the same time however there was no challenge to the central role played by the banks. Rather the contrary these were able to expand their intermediation activity as a result of the public's falling propensity to hold securities, of the initial impact of inflation on company accounts and of the irrational management of the financial requirements of the public sector.

Investment financing: the "financial road" to growth

The attitude to capital accumulation of the credit system and of economic policy decision-makers during the period which lasted until the mid 1970s has been called the "financial road" to growth (Monti, Cesarini, Scognamiglio). What is meant is the use of monetary and credit policy to force the rate of accumulation with more regard for the aggregate volume of investment than for the efficiency of its allocation. This expression implies a substantially negative evaluation of past experiences which is widely shared in Italy

This negative evaluation is largely based upon the distortions created by the system of subsidized credit. There can be no

doubt that this system of subsidies and incentives, in a political-institutional framework characterized by the "appropriation" of the state and its institutions by the political parties, did effectively distort the accumulation process, benefitting firms which should not have invested or which would have invested even without subsidies. Even disregarding however the distortions introduced by economic policy there are other elements in the financial structure which seem to justify a substantially negative judgement. One may note the contradiction between the importance attributed by the central bank to a high level of accumulation and a certain reduction in the entrepreneurial role of the banker, brought about by economic policy. As far as the banks are concerned it has already been seen how the structure of the credit system conceived by the Bank of Italy following the 1963 crisis contained few incentives for an efficient allocation of credit. Undoubtedly the opportunities provided by the purchase of bonds and by the financing of the public sector have had anything other than a stimulatory effect on the banks' responsiveness to firms' requirements. At the same time the banks, in their relations with firms, have suffered from the lack of a clear definition of their function (being neither pure commercial banks nor mixed banks). In the majority of cases this has led them to withdraw from one of the key roles of "finance" vis à vis "industry": that of "guaranteeing a balanced technical, financial and market basis for firms' expansion (Confalonieri (a), (b)). As far as the special industrial credit institutions are concerned here too one notes a process of dequalification. As those responsible for the administration of public intervention these institutions have seen their role reduced to that of verifying whether the firms applying for credit possess the prerequisites established by law. In the collection of funds any incentive to assume a more entrepreneurial attitude has been largely removed by the banks' purchases of their bonds.

In these conditions there have been very few stimuli to technical innovation in the credit field. To a large extent innovation by individual banks have been replaced by financial engineering on the part of the monetary authorities. At the same time there has been very little pressure to improve operative efficiency.

It seems legitimate to argue that a financial system of this type is likely to favour rather than to oppose the public's preference for liquid assets. Whereas in Germany and France it has been in the interest of the banks to match the maturities of their liabilities to those of their assets, in Italy this has been less so. This explains why Italy is the only country among those considered in which there has been an increase in the share of sight deposits in banks' liabilities.

A system as liquid as this is exposed both to financial and to cyclical instability. The former risk has been minimized by the state's role as ultimate guarantor resort. The latter, deriving from the system's sensitivity to external shocks and to the corrective monetary policy measures which these make necessary, have led to a discontinuity in the flow of credit mainly hitting those firms relying for credit on the renewal of overdrafts.

These features of the Italian financial system during the period 1965-1975 meant that the system was ineffective to satisfy the demand for credit by "normal" unsubsidized medium-sized firms. Such firms could turn to two kinds of intermediary, both of whom however were ill-suited to their requirements. On the one hand there was the "omnibus" bank (Cingano) which tended to avoid forms of involvement with firms which lay outside what is considered its field of activity. On the other there were the special institutions whose structure was such as to impede access.

The weak points we have seen in the Italian banking system are not to be attributed to weak management. For countries as similar as those considered here comparisons of entrepreneurial ability are somewhat meaningless. Financial institutions, however, to a far greater extent than firms are influenced by the environment in which they operate. The argument developed in this paper is that the conditions in which Italian credit institutions have operated have failed to stimulate the development of an effective system of industrial credit.

Lastly a note concerning the central bank. The financial structure built up by the Bank of Italy during the period of the "financial road to growth" attributed an important, broad-ranging role to the bank itself in the management of credit flows. In the exercise of this responsibility the bank was constrained however by the position in which it found itself. The Bank of Italy was neither the executor of government economic policy, as in France, nor a counter-vailing power as in Germany. Rather it was a key participant in the process whereby the government formulated Italian growth policy (Carli).

Towards a new financial system

Until the emergence of "new developments" during the second half of the 1970s, Italy's financial structure implied that policy "tools" were more important than market credit "mechanisms" (Ciocca). This was due to more than just the range of public intervention in subsidizing investment credit and the way in which this credit was managed by the special institutions. Quite apart from these aspects of the system and from the necessity for intervention created by inflation it can be argued that the structure assumed by the credit system could not have survived without continual intervention by the monetary authorities. In this way the Bank of Italy ended up by as-

suming responsibility for decisions concerning the allocation of credit. Around 1975 however there was a change in the Bank of Italy's attitude to economic policy and to the role of the Central Bank. There was a clear shift in the conduct of monetary policy towards the pursuit of the "normal" objectives of this policy and in particular the balancing of the country's foreign accounts. At least in part as a result of this change a number of measures were taken as a response to the public sector's growing financial problems and several new developments emerged. These initiated a gradual transformation of the financial system whose new characteristics are today beginning to appear.

In March 1975 the Ministerial Committee for Credit and Savings approved a number of changes in the method of issuing Treasury bills including authorization for non-bank dealers to participate in the auctions. This was a first important step towards the creation of non-banking channels for the financing of the public sector. The figures showing the gradual increase in the share of these assets in the public's portfolio prove that this measure has made a decisive contribution to reducing the role of banks intermediation. At the same time however the scale of the treasury's financing requirements is still such as to make the involvement of the banks inevitable.

A second series of measures aimed at rationalizing financial circuits within the public sector. These included both the measures taken at the end of 1976 and the beginning of 1977 blocking and consolidating local authorities' indebtedness with the banks and the more recent decisions, obliging public institutions to deposit their liquid balances with the Treasury. The blocking and consolidation of the local authorities' indebtedness closed one of the outlets through which the banks' could expand their assets. The concentration of public institutions assets in the hands of the Treasury reduced bank intermediation on the deposits side. It was thus possible to block a

distorted financial circuit in which "the Treasury emits bills and forces the central bank to create money to provide funds to be transferred to other public institutions while the latter find it advantageous to deposit these with the banks, which in their turn invest in Treasury bills" (Cavazzuti).

A third series of measures concerned the medium to long-term credit sector. Here the monetary authorities adopted two specific lines of action: on the one hand decentralization towards the banks, on the other the break of the tie between credit and subsidies which characterized the Special Institutions (Relazione del Governatore, Banca d'Italia 1981). The first line of action implied a number of decisions: the authorization (1976) for banks existing in the form of public companies and for cooperatives to grant 15% of their liabilities in the form of medium-term loans (this reinforced a similar authorization granted in 1972); the loosening of the portfolio constraint from 1978 onwards and the exclusion from this constraint of the bonds issued by industrial credit institutions. These measures were more than just a response to the need to consolidate credits already granted; rather they constituted a stimulus to replace the banks' indirect links with firms via the special credit institutions with a direct relationship. As a result the role of the banks in the medium-term sector has expanded considerably (Cesarini (a)).

The second line of action is that implied by the proposals to reorganize the system of credit subsidies and incentives. These proposals imply that in the medium-long term credit sector the banks should coexist with the special institutions. The former would be allowed to finance investment projects on a limited scale vis à vis the turnover of the firm applying for credit. The latter would finance larger projects. The banks would thus be given a more clearly defined and more responsible role in the supply of credit to industry, thereby compensating the reduction in the range of possibilities open for

their lending to public institutions. The special credit institutions, for their part, would lose their role as administrators of public intervention.

The effectiveness of these measures in modifying Italy's financial structure has been amplified by a number of new developments within the productive system. The particularly sharp "stagflation" experienced during the 1970s has led to changes both in industrial structure and in the composition of the entrepreneurial class. These in their turn have produced significant quantitative and qualitative effects on relations between banks and firms. The violent fluctuations in raw materials and energy prices, the rigidity of the labour market, restrictive economic policies and the consequent rise in interest rates initially had the effect of unbalancing major enterprises' financial accounts, particularly, as in other countries, in those sectors worst hit by the crisis. This led to an expansion of indebtedness with the banks which reached its high point in 1974. This was followed by a gradual return to financial equilibrium achieved via a recovery in profits and, at least up to 1979, by a drastic cut in investment. At the same time liquidity was managed more rationally. In this way companies were able to reduce their requirement for credit per unit of turnover while public enterprise benefitted from a major increase in capital contributions by the state.

Meanwhile inflation and technical innovation, together with the characteristics of the labour market have led to the development of a sector of medium to small scale entrepreneurs, responsible in fact for the majority of industrial investment. As in the years from 1955 to 1963 industrial development has been "from the bottom up", has been largely extensive in nature and has been concentrated in certain specific regions. The consequent renewal of the entrepreneurial class, encouraged by the crisis of a number of major companies

and groups which has made it possible for new entrepreneurs to join the private industrial élite, has encouraged a change in attitude towards the banks, a more demanding approach and a willingness to develop non-banking channels of finance.

The second half of the 1970s thus witnessed a whole series of "novelties" affecting the structure of the financial system and reducing the importance of the two main factors underlying the previous structure, namely the weakness if not the absence of independent financial circuits for the public sector and for private firms.

These changes, although due to a large extent to short term economic difficulties were in fact structural in nature. Already they have led to changes in the Italian financial and credit system, encouraging a higher degree of rationality and a more adequate response to the financial requirements of capital accumulation. Although this seems something of a paradox the shift of the Bank of Italy's goals from the promotion of capital accumulation to domestic and external stability have ended up by encouraging the credit system's responsiveness to firms' financial needs.

The recent changes in the attitudes of financial intermediaries and their despecialization have prepared the ground for a global redefinition of the fields of operation reserved for the banks and the special institutions. Many of the preconditions now exist for a reform of the Italian financial and credit system which could bring Italy closer to the other two countries examined.

V. CONCLUSIONS

During our research we have developed for each of the countries considered, an interpretation of the evolution of their respective financial systems. Given that the characteristics of the three countries differ these interpretations also differ. In view of the impossibility of defining an "ideal" model of financial system what we have primarily tried to do is to identify the specific features of each system and to evaluate their internal coherency. It remains true however that our interpretation is based on a common "problématique" (dating from the 1960s), namely the need to reconcile a high level of external financing of capital accumulation with structure of financial systems centred on the banks.

Regardless of the hopes often expressed in conferences and studies on this question in none of these countries has the "European financial markets problem" been resolved through a strengthening of the stock markets. In all three the proportion of non-financial sectors' liabilities absorbed by the banking system has increased. As a result their financial structures have failed to move towards the Anglo-American model, taken as a touch-stone by the studies of the 1960s. Rather the contrary it appears that the Anglo-American systems (in particular the British system) have moved towards the "continental" model.

In all probability the failure of continental Europe to develop financial systems similar to those in Britain or North America is due to deep historic reasons. However much importance one may attach to specific factors such as the tax regime for financial assets, social security systems, or the existence of efficient organs of control these are not enough to provide a full explanation. In the last analysis all these factors depend on decisions taken by governments, decisions which cannot be regarded as completely independent of the interests of financial institutions and of firms.

The history of economic development shows that the Anglo-American capital markets, which economists tend to assume as their model for an ideal financial system are in fact an exception to the general rule. At the same time there can be little doubt that in continental Europe the paths taken to high economic growth were different from those which characterized the precocious development of Britain and the United States and the corresponding structure of financial markets. The characteristics of the Anglo-American markets can be explained not so much as a result of these countries' level of development when they were first organised, but rather as a consequence of the period in which they emerged. This also explains their relatively limited capacity for channelling funds from the public to firms. The development of the major European economies has been based on financial systems biased towards intermediaries rather than the market. With respect to these intermediaries capital markets have played a complementary rather than a competitive role. The reasons for the failure to put Lamfalussy's suggestions into practice are to be found in the lack of interest, on the part of the banks, in developing a broader capital market. Nonetheless it is very doubtful whether it is in the banks' interest to replace their direct relationship with firms with holdings in investment funds (as Lamfalussy suggested) (Cesarini (b)). Both in Germany and France major firms have a relatively close relationship with the financial system. Our research shows no evidence that finance capital has dominated the industrial system. It thus seems unlikely that there have been any significant limitations on firms' willingness to look for risk capital. In Italy where this interpenetration between the banks and major industry hardly exists, firms have received far from negligible benefits from the subsidized credit system.

Our analysis of the evolution of the three systems from half way through the 1960s until the end of the 1970s has shown the diffe-

rent ways in which it has been possible to satisfy the need for external finance for the accumulation process. In France, the only country in which there has been a genuine reform of the credit system the financial system has moved closer to the German banking model. The latter has continued to be centred around the universal bank whose role has been further expanded as a result of bank despecialization. Italy's financial structure, from the 1960s until recently, has reconciled the central role of the banking system with a form of credit specialization in which medium-long term credit is reserved for non-banking institutions. As a consequence she has taken a different path from that followed by the other two countries.

While French industrial growth has been accompanied by a "decentralization" of investment financing from the Treasury to the banks, Italian development has been based on the "financial road to growth". Decisions concerning investment financing have been centralized. As a result, at least until recently, the increased role of the banks in financial intermediation has failed to bring with it an increase in their responsibilities vis à vis industrial credit.

This low level of responsibility (with respect to the banks' importance), affects the banks' attitudes both towards the owners of financial wealth and towards inflation. The Italian banks have not the German and French banks' same interest in consolidating their liabilities. As a result there has been no attempt to hinder the owners of financial wealth from opting for liquid assets; rather the contrary the policy of granting a high return on current account deposits has encouraged this tendency. This distinguishes the Italian case from the situation in Germany or France, where even in the presence of a relatively high rate of inflation the banks have succeeded in shifting a proportion of their deposits towards longer maturities. The Italian banks' attitude of relative indifference towards the ma-

turities of their liabilities and their limited involvement in medium-long term credit help to explain why the Italian banking system has failed to emulate the German system in deterring inflation. The negative effects of inflation have been felt not by the banks but by the special credit institutions whose role in the forming of a consensus around government economic policy is far less important.

As far as capital accumulation is concerned the Italian financial system is in a contradictory position. On the one hand it has attempted to force the process along; on the other it has proved inadequate to meet its requirements.

The Italian credit system's structural insufficiency to meet the need for non-subsidized financing mainly affects small and medium-sized firms.

The financing of these firms has also given rise to concern and state intervention in the other two countries considered (as well as elsewhere). The difference between the Italian situation and that in Germany or France is that in these latter countries special credit institutions and intervention by government have been grafted onto a system in which medium-long term credit was already a normal part of the banks' activities. If one is to evaluate the role of the credit system in selecting between different entrepreneurs one also has to bear in mind that the German discrimination in favour of large firms was the result of an economic policy implying revaluation of the DM, a policy which put their entrepreneurial capabilities to a severe trial. In France this same discrimination fitted in with an industrial policy in which large companies had been encouraged to commit themselves to large highly innovatory projects. In both cases the problems which arose in the financing of minor enterprise derived not so much from the behaviour of the credit system as from the underlying rationale of development policy. This rationale, while

working to the advantage of the major industrial groups, also asked for something in return. In Italy on the other hand, where there was no such policy of stimulating major companies, it was primarily the credit system which had to select firms worthy of receiving finance and where necessary encourage innovation. At the same time how ever the very structure of the system made this an almost impossible task.

In recent years there have been structural changes in the Italian financial system which have brought the Italian banks closer to the model of the other two countries. This appears desirable not because the French and German models represent some kind of ideal but rather as a coherent alternative to the Anglo-American model which has difficulty in taking roots in continental Europe and which today is even less of a model than in the past.

Last but not least one further result of our investigation concerns the relationship between the central bank and the financial system. The analysis of the characteristics and development of the three financial systems examined has provided evidence against the idea of the central bank's policy as an exogenous variable. This problem has recently been studied from the point of view of the relationship between the central bank and government (Wooley). What emerges from our research is the importance of a further problem, namely that of whether the central bank's behaviour is exogenous with respect to the structure of national financial system. A likely hypothesis to explain the DBB's monetarism is that this is a consequence of the role of the universal bank in the German financial system and of the way in which this influences the behaviour of the central bank. We have also considered the constraints on monetary policy imposed by the structure of the French banking system in the case of the policy adopted by Barre. Finally, as far as Italy is concerned, we have emphasized

the importance which the banking law grants the central bank in determining the optimal structure for the financial system and the way in which in this case too the central bank has been influenced by the banking system. This evidence from the three countries examined thus tends to confirm the importance of the problem raised which could provide an interesting topic for future research.

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