Regulating for Legitimacy: Consumer Credit Access in France and America

Introduction

Why do we regulate markets? Theories of regulation in the public interest have emphasized the role of governments either in fixing market failures to promote greater efficiency, or in restricting the efficient functioning of markets in order to pursue public welfare goals.[1] In either case, features of markets serve to justify regulatory intervention. I argue that this causal logic must sometimes be reversed; that, for certain areas of regulation, its function must

[1] Because I am interested in regulation in the public interest, I set aside theories of regulation based on regulatory capture by narrow economic interests in order to limit or control market access by competitors, as well as cases of "reverse capture" in which regulatory agencies attempt to dominate a sector. Giandomenico Majone, "From the Positive to the Regulatory State: Causes and Consequences of Changes in the Mode of Governance," *Journal of Public Policy* 17/2 (2008), p 162; Steven K. Vogel, *Freer Markets, More Rules: Regulatory Reform in Advanced Industrial Countries* (Ithaca: Cornell University Press, 1996), p 15; Daniel Carpenter, *Reputation and Power: Organizational Image and Pharmaceutical Regulation at the FDA* (Princeton: Princeton University Press, 2010), pp 38-39.

be understood as making markets legitimate.[2] Based on a comparative historical study of consumer credit markets in the United States and France, I examine the sources of national regulatory divergence. In France, usury and data privacy laws restricted lenders' ability to offer credit to riskier borrowers. In the United States, a different set of regulations—including centralized credit rating, liberal pricing policies, and liberal bankruptcy provisions—promoted broad access to credit for the American public. What is important about these regulatory responses was the role they played in legitimizing what had historically been at best a marginal economic activity. Although the regulatory outcomes were different, in each country, a series of regulatory interventions by the state transformed a formerly disreputable small lending sector into a legitimate economic activity.

Among the advanced industrialized countries, France and the United States represent nearly opposite poles in consumer credit use. Americans have been heavy users of consumer credit since the interwar period; the French have relied relatively little on consumer credit. In 1955, non-mortgage consumer debt averaged 15% of household disposable income in the United States, compared to 0.3% in France. Fifty years later, in 2005, US non-mortgage household debt had risen to 33% of disposable income.[3] French household debt at the time was still below 15%

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[2] Daniel Carpenter, "Confidence Games: How Does Regulation Constitute Markets," in Edward J. Balleisen and David Moss, eds., *Government and Markets: Toward a New Theory of Regulation* (Cambridge: Cambridge University Press, 2010).

[3] From the late 1990s, households began rolling over consumer credit into home equity loans. The 33% figure includes 25% credit card and installment debt, plus an additional 8% of extracted equity used to pay off existing debt or make new consumer purchases. Alan Greenspan

of disposable income. (See figure 1.) This difference is puzzling in part because of the technical skill and economic success of French lenders. The consumer finance companies that emerged in postwar France were quick in assimilating new lending techniques developed in the United States. From the late 1980s, when consumer use of credit grew more common across Europe, the French company Cetelem emerged as the dominant player.[4] Consumer lending rates were also roughly the same in both countries. Given comparable know-how in originating consumer loans, and similar lending rates, why were American and French consumer credit markets so different?

<Figure 1 about here>

Using records from lenders and regulators, I argue that differences in credit practice derive from the ways in which consumer credit markets came to be legitimated in the two countries. In the United States, a coalition of non-governmental organizations (NGOs) and commercial lenders helped to construct the market for consumer credit as a legitimate response to an evolving set of societal problems. Over the course of nearly a century, politicians on the left and right supported policies that promoted credit access as a form of social welfare. In France, NGOs were less active and commercial banks stayed away from consumer lending. Lending instead came to be dominated by dedicated consumer finance companies that were required to operate under close regulatory scrutiny. If American policies emphasized the value of consumer access, the French response emphasized the value of consumer protection. In both cases, the point of government regulation was to construct credit markets as socially and politically legitimate. Once established, these different approaches to consumer credit became

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and James Kennedy, “Sources and Uses of Equity Extracted from Homes,” *Oxford Review of Economic Policy* 24/1 (2008), pp 120-144.

[4] In 2008, Cetelem was renamed BNP Paribas Personal Finance.

locked in over time. Hence, when France briefly experimented with deregulated consumer credit markets in the mid-1980s, social activists on the left and right demanded that the government step back in to re-regulate the market. In the United States, rising personal bankruptcy rates tied to consumer over-indebtedness in the 1990s and 2000s failed to elicit a regulatory response from policymakers on the left or right despite the clear social costs. The financial crisis of 2008 traces its roots in part to the resulting regulatory void.

This process of legitimation by regulation is not unique to consumer credit. Other market sectors, including life insurance and genetic technologies, have relied on regulatory interventions in order to shed prior public opprobrium.[5] If this legitimating function of regulation is pervasive, it suggests that the study of regulation might benefit from a strong dose of historical institutionalism.[6] Rather than focus on the functional logic of market failure or the welfare politics of market externalities, we might better explain existing national differences by studying the specific historical contexts in which new market sectors come to be perceived as legitimate in society. To the extent that different strategies of legitimation become locked in over time,

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[5] Viviana A. Rotman Zelizer, *Morals and Markets: The Development of Life Insurance in the United States* (New York: Columbia University Press, 1979); Julia Black, "Regulation as Facilitation: Negotiating the Genetic Revolution," *The Modern Law Review* 61/5 (1998): 621-660.

[6] See, for example: Daniel Carpenter, *Reputation and Power: Organizational Image and Pharmaceutical Regulation at the FDA* (Princeton: Princeton University Press, 2010); David Moss, *When All Else Fails: Government as the Ultimate Risk Manager* (Cambridge: Harvard University Press, 2004).

historical institutions may play a critical role in explaining variation in contemporary regulatory outcomes.

The article is organized as follows. The first section introduces the two cases that are to be compared. It presents two sets of theories that are commonly evoked to account for regulatory differences, then proposes an alternative theory based on the role of regulation in legitimating markets. The second section applies this alternative framework to explain patterns of consumer lending in the two countries. The third addresses sources of national differences in consumer credit rating. The final section traces the historical evolution of the link between credit and welfare in the two countries.

Existing Theories of Credit Regulation

The rise in consumer credit use across the advanced industrialized countries, together with a growing interest in institutions that promote credit access in developing countries, has focused academic attention on the sources of cross-national differences in credit use. Two kinds of explanations have dominated the debate. One sees credit markets as beset by problems of adverse selection that lead to an under-serving of risky borrowers.[7] This strain of research has

[7] Faced with a combination of honest-but-risky borrowers and dishonest borrowers who did not intend to repay, the latter group would be less price sensitive and thus over-represented among applicants. Joseph E. Stiglitz and Andrew Weiss, "Credit Rationing in Markets with Imperfect Information," *American Economic Review* 71/3 (1981): 393-410;

emphasized the importance of information sharing among lenders to limit non-payment losses.[8] Credit research has accordingly focused on credit rating agencies as a driver of credit extension, and on the use of credit data to select borrowers and set interest rates. [9] In micro-finance and other social lending institutions, social ties have been seen as an alternative means to overcome the problem of adverse selection.[10] Yet the perceived riskiness of consumer borrowers was, historically, largely a myth. During the Great Depression, consumer loans showed higher repayment rates than any other class of borrowing.[11] In France during World War I, lenders in the industrial northeast that closed their doors during German occupation were able to collect on most of the debts after the war ended. And when the United States enacted a liberal consumer bankruptcy policy in 1978, including a provision for automatic discharge of debts, lenders appear not to have worried about its impact on non-payment rates, and raised no objections. Observers frequently but mistakenly attribute the high cost of consumer credit to the risk associated with unsecured personal loans, but the reality is more mundane. Consumer loans were expensive

[8] Tullio Jappelli and Marco Pagano, "Information Sharing, Lending and Defaults: Cross-Country Evidence," *CSEF Working Paper,* no. 22, 1999; Tullio Jappelli and Marco Pagano, "Information Sharing in Credit Markets," *Journal of Finance* 48/5 (1993).

[9] Akos Ronas-Tas, "Consumer Credit in Transition Economies," in Victor Perez-Dias, ed., *The European Experience in Comparative Perspective* (London: Berghahn Books, 2009).

[10] Asif Dowla, "In credit we trust: Building social capital by Grameen Bank in Bangladesh,“ *Journal of Socio-Economics* 35/1 (2006), 102-122.

[11] Michel Schlosser and Gérard Tardy, *Les cartes de crédit* (Paris: Dunod, 1971).

(25%-40% was typical in the early postwar period) primarily because of the unusually high administrative costs associated with writing, tracking, and collecting small loans.[12]

The second kind of explanation focuses on the potential social costs associated with liberal credit access. The general proposal is that governments intervene in markets to manage an inherent trade-off between market efficiency and social equity.[13] In a range of markets, including labor, capital and product markets, governments regulate in order to curb the socially unacceptable externalities that unfettered markets would generate.[14] How much different states are willing to compromise efficiency in order to promote equality depends in turn on institutional

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[12] Archives of the National Consumer Council of the Banque de France (BdF CNC), 1427200301, box 283, Comité national du Crédit, Comité du crédit a court terme, December 1953-June 1961, Meeting of the Comité du crédit à court terme, June 19, 1961, p 21.

[13] Joseph E. Stiglitz, "Government Failure vs. Market Failure: Principles of Regulation," in Edward J. Balleisen and David Moss, eds., *Government and Markets: Toward a New Theory of Regulation* (Cambridge: Cambridge University Press, 2010), p 22.

[14] Jonas Pontusson, *Inequality and Prosperity: Social Europe versus Liberal America* (Ithaca: Cornell University Press, 2005); André Sapir, "Globalization and the Reform of European Social Models," *Journal of Common Market Studies* 44/2 (2006), pp 369-390; Guandomenico Majone, "From the Positive to the Regulatory State: Causes and Consequences of Changes in the Mode of Governance," *Journal of Public Policy* 17/2 (2008), p 162; Gosta Esping-Andersen, *Three worlds of Welfare Capitalism* (Princeton: Princeton University Press, 1990).

and political features that are distinctive to their political and historical context.[15] In consumer credit markets, the problem was that credit access appeared to be regressive in its consequences. In general, the interest paid on outstanding credit reduces borrowers' purchasing power over time. But, because the administrative costs of making loans was high and fixed, smaller loans faced higher interest charges. To the extent that the working class and poor borrowed smaller amounts, they tended to reduce their purchasing power more. This effect implied that countries focused on the welfare of the poor and working classes should have an interest in regulation that limited credit access. Such regulation could take a variety of forms: usury ceilings, restrictions on downpayment and repayment periods, direct quantitative limits on extended credit, restriction on advertising and collections practices, limitations on data sharing and collections practices, and liberal bankruptcy provisions that weakened the contractual claims of lenders. Each of these regulations has been interpreted as limiting the supply of credit in order to limit the social costs of free credit markets.[16]

The problem with this efficiency-versus-equity argument as it relates to consumer credit markets is that neither American nor French policymakers believed that such a trade-off existed. In the United States, policymakers on the left and right came increasingly to see consumer credit as *supporting*, rather than undermining, social welfare. In their view, more efficient consumer credit markets were welfare enhancing. In France, early postwar regulators restricted credit not

[15] André Sapir, "Globalization and the Reform of European Social Models," *Journal of Common Market Studies* 44/2 (2006): 369-390; Jonas Pontusson, *Inequality and Prosperity: Social Europe versus Liberal America* (Ithaca: Cornell University Press, 2005).

[16] Theresa A. Sullivan, Elizabeth Warren, and Jay Lawrence Westbroook, *As We Forgive our Debtors* (Washington, DC: Beard Books, 1999).

primarily out of concerns about its distributional effects, but because they felt that consumer credit was an inefficient allocation of capital. France's restrictive policy with respect to consumer credit was grounded in the understanding that free markets offered neither welfare benefits nor efficiency. It is this cross-national difference in perception of the social and economic implications of consumer borrowing that needs to be explained.

The Puzzle: Explaining Demand for Credit

The adverse selection theory and the equity-versus-efficiency theory share a common focus on the supply side. Both assume a large, unmet demand for consumer credit, then focus on explaining differences in the degree to which that demand is being met. Yet a core puzzle of consumer credit is that demand for it exists at all. After all, consumer credit works over time to *reduce* household purchasing power. While borrowing allows a household to move its consumption forward in time, it also reduces its total consumption by the amount of the interest payments on the loan. Unlike business borrowing, in which debt creates a corresponding new stream of income out of which it can be repaid, household borrowing is a pure liability.[17] Interest payments must come out of the budget for future consumption. The effect is to reduce household purchasing power. Given this, why have households borrowed to finance consumption, and why has that borrowing increased over time?

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[17] An estimated 30% of consumer credit actually finances business investment. Some small businesses rely on consumer loans to finance inventory and investments. They may devote household savings to business investments while financing consumption through credit. Educational borrowing is typically also understood as an investment. I am interested in household borrowing that finances pure consumption.

Researchers have offered three explanations for this seemingly irrational behavior. The earliest explanation, formalized in the life-cycle savings model introduced by Franco Modigliani, suggested that credit could be used to could smooth consumption so as to increase overall household utility.[18] Assuming a diminishing marginal utility of consumption, households expecting a higher future income might borrow in order to move some of their consumption forward. The problem with the life-cycle theory is the very high cost of consumer borrowing. Households would have to expect extraordinary wage growth in order for a typical 15%-20% real interest rate to increase their household utility. Moreover, real wage growth had declined or even stagnated by the early 1980s, at the time when borrowing began to escalate. This pattern of wage growth and credit use is difficult to explain in terms of life-cycle consumption smoothing.

A second explanation has focused on the role of credit contracts in imposing discipline on households.[19] By contracting for a loan, households received a regular bill that bound their hands and forced them to pursue "systematic savings."[20] A third and related explanation focuses on the use of credit as a form of insurance. In this view, households faced with shocks to income and expenses used credit in order to maintain a minimum level of savings that they would need to carry themselves through hard times. The problem with both the discipline and the insurance

[18] Franco Modigliani and Robert Brumberg**, "**Utility analysis and the consumption function: An interpretation of cross-section data," in Kurihara, ed., *Post-Keynesian Economics* (New Brunswick, NJ: Rutgers University Press, 1954).

[19] Lendol Calder, *Financing the American Dream: A Cultural History of Consumer Credit* (Princton: Princeton University Press, 1999).

[20] Robert L. D. Morse (RLDM) Archives, Kansas State University, Box 148, folder 16, JC Penney Company, "100% Down and Nothing a Month for the Rest of your Life," c 1968.

arguments is that they no longer made sense once revolving credit had become the dominant form of unsecured consumer borrowing. Revolving accounts, which had by the 1960s become a dominant form of lending in the United States, gave consumers unusual flexibility in making repayments. This flexibility was attractive for lenders, who discovered that it allowed them to reduce non-payment rates, but it also eliminated the discipline of repayment for consumers. Further, because revolving accounts offered households a line of credit up to a predetermined credit ceiling, customers had access to liquidity without actually borrowing. Had consumers been using credit as insurance, we would expect them to establish revolving credit accounts, and then hold them unused in preparation for future need. This was not the pattern that banks observed.

Without better explanations, economists have embraced the idea that consumers possess a steep near-term discount rate that leads them to prioritize current consumption.[21] This emphasis on near-term consumption makes households accepting of even very high interest rates for short-term loans. Yet the insight that consumers are short-sighted does not explain differences in policy that we observe across countries. Consumers also exhibit high demand for gambling, alcohol and drugs—how countries have responded to regulate their access to these markets has depended on the historical context in which they came to be regulated.[22] Even if consumers share an irrational short-term bias, the status of the market that serves that demand is set through the regulatory processes that need to be explained. By focusing on the role that national regulation

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[21] David Laibson, "Golden Eggs and Hyperbolic Discounting," *The Quarterly Journal of Economics* 112/2 (1997), pp 443-477.

[22] Paulette Kurzer, *Markets and Moral Regulation* (Cambridge: Cambridge University Press, 2001).

plays in legitimating markets, I argue that we can begin to explain both the supply and demand for consumer credit.

An Alternative View: Regulating for Legitimacy

Historically, consumer borrowing was viewed with deep skepticism in both France and the United States. At the turn of the 20th Century, social critics saw it as exploitative of the working classes, an unproductive use of capital, and in contravention of religious dictates against charging interest. In both countries, activists from the religious right and the labor left spoke out strongly against the problem of usury. In the United States, high interest rate lenders seemed to pray on the working classes. Loans secured against salaries drove unlucky workers into a cycle of poverty and unemployment that eventually left them destitute. In France, early itinerant lenders were seen as promoting profligacy, undermining morality, and taking advantage of housewives while their husbands were away at work. Yet, by the 1960s, societal attitudes toward credit had changed. Although interest rates had not fallen significantly in either country, consumer loans had been reconceived as a legitimate tool for household financial planning. Formerly marginal economic activities had gained political and social legitimacy. How this transformation occurred, and the role of government regulation in the process, is central to understanding persistent national differences in credit practice.

In the United States, an evolving coalition of progressive social groups and business interests united around credit as socially advantageous. In the interwar period, legitimate consumer loans were promoted as an alternative to the scourge of high-rate salary lenders. In the early postwar period, both industrialists and organized labor supported credit as a means to drive scale in production, raising productivity, profits and wages. By the late 1960s, a new coalition had emerged that saw credit as a tool for extending economic citizenship to formerly excluded groups, including women and urban blacks. These ideas would influence the ‘third-way’ politics that promoted credit access during the 1980s and 1990s. Whether or not they were right, American interest groups on the left and right came together around the idea that credit access was a tool for social and economic equality. In France, this coalition of social progressives and business leaders never emerged. Labor unions argued that the interest paid on loans lowered worker purchasing power; economic planners warned that credit would drive inflation and hurt exports; commercial banks saw consumer lending as undignified and unprofitable. The legitimacy of consumer credit in France had its origin instead in a close collaboration between lenders and government regulators. The resulting policies emphasized a strong regulatory framework of borrower protections rather than the idea of credit access as a right. These different logics of market legitimacy—access in the United States and protection in France—in turn drove the regulatory divergence that continued to dominate the sectors through the turn of the century. Lenders played a role in forging this regulatory divide, but so did government policymakers and social activists. Through processes that were in part historically contingent, French and American policymakers and their constituencies came to fundamentally different conclusions about the credit interests of consumers, about the nature of market failures, and about the very social and economic purpose of regulation.

The process of defining a legitimate role for consumer credit was shaped by two specific institutional differences between the two countries. First, the role of banks was critical. American banks moved quickly to offer consumer credit, while French banks delayed. The participation of commercial banks in consumer lending in the United States gave the activity legitimacy. It also created the conditions under which revolving credit and electronic payments would be combined in the same instrument: the modern credit card. In France, banks did not enter consumer lending in force until the mid-1980s. Without the legitimacy lent by the participation of commercial banks, consumer lenders in the early postwar period enjoyed legitimacy through close regulatory oversight by the French state. By the time banks did begin making consumer loans, France's *carte bleue* debit card system had already established electronic payment and consumer credit as fundamentally different products. Second, the role of non-governmental organizations (NGOs) was critical. In France, the interest of certain family associations in increasing access to credit was offset by objections from both religious groups on the right and organized labor on the left. In the United States, by contrast, a range of NGOs across the political spectrum organized to advocate for credit extension as a tool for economic self-reliance and social inclusion.

The case of consumer credit evokes the importance of interactions between different societal actors in generating legitimacy for new market activities. In the United States and France, different legitimacy coalitions emerged to support consumer lending. In the United States, NGOs and commercial banks formed a legitimacy coalition that supported credit extension. In France, commercial banks did not engage in consumer lending, and few NGOs supported credit extension. The legitimacy of consumer lending found a different basis: in a close interaction between national regulators and consumer lenders that defined consumer credit as an area of active consumer protection. If consumer credit in the United States was desirable as a form of social policy, consumer credit in France was acceptable because the state worked closely with lenders to mitigate its potentially negative societal impact. These different approaches to credit would in turn affect consumer perceptions of the value of credit. American consumers were taught that consumer credit would improve their economic status, and their high level of borrowing reflected that belief. French consumers were taught a different lesson. For them, consumer credit was acceptable but risky—more akin to gambling than to an investment in future prosperity. French consumers borrowed, but they also supported government policies that placed careful restrictions on the scope and extent of lending practice.

Explaining Lender Behavior: Seeking and Finding Legitimacy

The central fact of early postwar consumer credit was that it was largely unprofitable. The problem had little to do with the riskiness of individual borrowers, as later theories of adverse selection would suggest. In fact, most early consumer credit was working class credit, and the regular wage of workers made them reliable repayers. Small lenders did take pains to reduce non-payment rates. In the United States, consumer lenders found ways to control non-payment risk even before local credit bureaus became common in the 1940s and 1950s. Early Morris Plan banks that pioneered unsecured small lending in the 1910s and 1920s required that each borrower be joined by two co-makers.[23] French postwar retail lenders employed either door-to-door collections, or relied on the judgment of retailers who were familiar with their customers. In most cases, non-payment rates remained below 1%.

The high cost of consumer credit derived mainly from the small size of each loan. For any lending transaction, the basic administrative cost—including loan application, credit check, bill mailings and reminders, and the associated bookkeeping—were largely invariant. This meant that small loans were relatively costly to administer, in proportion to the size of the loan. A study by France's National Credit Council in 1961 estimated that while the cost of an average commercial loan came 75% from interest and 25% from administration, the cost of an average

[23] *The Morris Plan of Industrial Loans and Investments* (New York: Industrial Finance Corporation, 1915), p 19.

consumer loan came 45% from interest and 55% from administration.[24] To earn a profit on small loans, banks had to charge high interest rates. In the United States in the 1910s, the Russell Sage Foundation estimated that lenders could not make loans “on a business-like basis” unless they were allowed to charge up to 42% annually (3.5% per month). By the 1960s, large lenders estimated that consumer loans below 18% could not be made profitably. The problem for banks was that they relied heavily on their reputations, and loans at such high rates were generally considered to be ethically questionable. The high interest rates that would be needed to make consumer lending profitable could damage their profitable lines of business with commercial clients. Non-bank lenders who focused exclusively on consumer borrowing did not have these reputational concerns.

In France, this moral economy of consumer lending led banks to steer clear. In fact, the French government periodically encouraged banks to enter the consumer lending field, in the hope that added competition would reduce consumer borrowing rates. In 1962, and again in 1972, banks dabbled with making personal loans, but quickly withdrew. Alongside concerns about reputation, France’s commercial banks also discovered that they were unable to make small loans efficiently. Dedicated consumer finance companies in France had since the 1950s been investing in automation that allowed them to process small loans at relatively low cost. At Cetelem, a consumer lender formed in 1954, the staff-to-loans ratio had by the late 1970s reached 1:1,000, higher even than its American counterparts at the time.[25] Commercial banks, by

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[24] BdF CNC, 1427200301, box 283, Comité national du Credit, Comité du crédit a court terme, December 1953-June 1961, Meeting of the Comité du crédit à court terme, June 19, 1961, p 21.

[25] *Forum International*, July 10, 1979.

contrast, were accustomed to making loans on the basis of personal relations with clients. These personal relationships imposed higher administrative costs, and yielded less reliable repayment. Critically, French banks at the time were making strong returns on industrial lending in the context of indicative planning by the French government. By comparison, consumer lending was a risky, low-margin activity that threatened to eat away at a bank's credibility. Revolutions in computerization, telecommunications and deregulation from the early 1980s would eventually change the economics of consumer lending. During the same period, a decline in economic planning and the rise of capital markets as an alternative source of industrial finance began to eat away at the traditional profit center for France's commercial banks. By the mid-1980s, French banks were moving aggressively into the consumer lending segment. By that time, many American banks already had thirty or more years of experience with consumer lending.

The relatively late move by French banks into consumer lending had a lasting impact on both public policy and on public attitudes toward consumer credit. Because banks did not participate in consumer lending, they were at best indifferent to government policies that restricted consumer credit access. In the United States, banks argued vehemently for the abolition of Regulation W, a restriction adopted during the Korean War that limited the downpayment and repayment terms for consumer loans; in France, similar qualitative and quantitative restrictions on consumer lending went unopposed by commercial banks. Had banks been actively involved in consumer lending, it is likely that the regulatory treatment of the sector would have been less restrictive. More generally, consumer lending never gained the early legitimacy that bank participation in the sector might have conferred.

The absence of banks in the consumer lending sector in France during the mid-1960s also influenced the way French consumers would learn to think about the relationship between credit and payment. In 1965, dedicated consumer finance companies in France began offering credit cards that combined electronic payment with a revolving credit facility. The first of these, called *Crédit en poche* (pocket credit), was provided by Cetelem; other finance companies quickly followed.[26] For banks, which were not engaged in consumer lending at the time, these cards seemed to threaten the traditional role of banks in managing the private payment system. In 1967, with support from the French government, a coalition of French banks countered the threat by creating their own electronic payment network, called Carte bleue. Like modern debit cards, Carte bleue offered an efficient electronic payment system that drew directly from one's savings account. Critically, there was no link to a credit facility.[27] Heavily subsidized by France's main banks, Carte bleue had by the early 1980s become the universal card-based payment system in France. Only in 1986, with the launch of Cetelem's Carte aurore, would French consumers would begin to associate electronic card payment with access to credit.

The factor that distinguished the American consumer lending sector from its French counterpart, and from the lending sector in virtually every other advanced industrialized economy, was the early move by US banks into consumer lending. The first US bank to have a large consumer lending branch was National City Bank, in 1924. American banks in the Northeast issued their first credit cards in mid-1950s. Bank of America created the first inter-bank payment network in 1968. By 1972, 2,000 different banks were offering credit cards affiliated with one of the two major credit networks. The central role of banks in consumer lending would profoundly shape attitudes toward credit. In general, banks brought deep

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[26] Cetelem's competitor Sofinco followed with a similar revolving credit card called Carte d'argent. *Le Figaro*, June 14, 1968.

[27] Quoted in Schlosser and Tardy (1971), p 55.

legitimacy to consumer borrowing. If banks were willing to make consumer loans, then consumers could assume that they were useful. More specifically, the early move by banks into lending meant that credit access and electronic card-based payment became inextricably connected. Debit cards that separated payment from credit would not become common in the United States until the 1990s.[28]

Why did American banks enter consumer lending when their French counterparts did not? The willingness of American banks to offer consumer credit had two sources. First, many banks had learned how to make small consumer loans during the interwar period. In 1934, the Title I program created under the new Federal Housing Act provided federal insurance for consumer loans intended for home improvement. By removing uncertainty associated with repayment, and by setting a federally-mandated interest rate on consumer loans (set at 10%), the Title I program induced many banks to experiment with consumer lending. What they learned was that consumers were reliable borrowers.[29] One industry observer noted in 1937: “Banks realize today that even in the absence of a government guarantee they can finance loans…with safety and at a good profit.”[30] By 1950, many American banks had developed the specialized skills—including standardized risk assessment, automated filing and billing, work specialization, and prompt collections—needed to make consumer loans efficiently. And, for reasons described

[28] Travel and leisure cards like Carte Blanche, Diners Card and American Express were the exception, but they were used primarily by business people.

[29] Carter McFarland, “An Economic Evaluation of FHA’s Property Improvement Program,” *The Journal of Land and Public Utility Economics* 23/4 (November 1947), p 399.

[30] Morris Bernhard, “Personal Loan Departments in Banks,” *Bankers’ Magazine* 134/4 (April 1937), p 320.

below, banks were spared the reputational costs that otherwise might have kept them from moving into consumer loans.

Still, American banks could not escape the basic economic reality that small loans were essentially unprofitable. A survey of consumer lenders in 1972 found that most banks that had launched credit cards in the 1950s and 1960s had lost money on them.[31] Banks nonetheless flooded the consumer market with credit. The reason had to do with the fragmentation of the postwar banking sector. In 1950, the United States had 14,000 banks. Most were unit banks that were restricted by state regulations from having branches. They were also bound by Regulation Q under the Federal Reserve Act, which banned interest on demand deposits (checking accounts) and capped interest on time deposits (savings accounts). What banks discovered in the 1950s and 1960s was that consumer credit, and especially the new revolving credit card accounts, was a powerful lure for attracting new depositors. Drawn by the prospect of a loan, borrowers would open savings accounts and provide a source of new capital for lending. The credit card business also attracted new commercial customers, since retailers who agreed to accept early credit cards also typically moved their banking operations to the same bank. More than the free toasters that banks occasionally offered as an inducement, credit was the inducement that banks used to attract new depositors.

The final ingredient that boosted both the supply and the reputation of credit in the United States was the role of retailers. Up until the 1950s, virtually every product and process

[31] JC Penney Corporate Collection (JCPCC), Southern Methodist University, Credit Matters, July 1971, “The Role and Functioning of Consumer Credit,” A Report by the Sub-council on Credit and Related Terms of Sale of the National Business Council for Consumer Affairs, March 13, 1972, p 37.

innovation in consumer credit—including installment lending, the credit card itself, and the revolving credit account, plus automated equipment for making and collecting loans—had its roots in the retail sector. In the period of postwar prosperity, large retail chains like Sears, JC Penney and Montgomery Ward offered credit in order to increase sales. Initially, their credit activities were purely a tool for promoting merchandising.[32] The interest rates they charged, typically 1% per month, almost never covered the actual cost of credit, which had to be subsidized out of general revenue. It was only in the late 1970s that JC Penney and Montgomery Ward began to make a profit on their credit services. Because the goal of early retail credit was to increase sales, retailers almost never pursued aggressive collections. Until the 1980s, JC Penney had a policy of writing off consumer debts more than six months past due.[33] It was in part the leniency of retail creditors that taught Americans to see consumer credit as economically benign. Retail credit was not accessible to everyone, but for customers whose applications were approved, they learned to see credit as convenient and non-threatening.

Historical Roots of Regulatory Divergence: Credit Rating and Data Privacy

The different roles of commercial banks in the United States and France had one final effect that, though unintended, would have a lasting impact on the institutional context of consumer lending. Much attention has been paid to the role of credit rating agencies in

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[32] JCPCC, Oral History Interview with William Batten, Session 1, Document #1071L, July 16, 1987, Interviews 1-2, p 2-7.

[33] JCPCC, Updates on Credit – WM Batten Speeches, 1962-1964, Remarks of William M. Batten, President, J.C. Penney Company, at the Annual Shareholders' Meeting, May 15, 1962, pp 3-4.

promoting access to consumer credit, and the French and American cases appear to affirm this link.[34] The United States had history of consumer credit bureaus dating to the interwar period, and the broad availability of credit in American has been attributed in part to the ability for lenders to use credit rating data to distinguish reliable from unreliable credit risk.[35] Conversely, the lack of centralized credit rating data in France has been described as one reason for the relatively low credit extension in the 1990s and 2000s.[36] French lenders shared only "black" non-payment data, not positive "white" information about credit-relevant factors including assets, outstanding liabilities, income, and credit and employment history. Foreign lenders like Egg and Capital One reported staying out of the French market in the 1990s specifically because of the lack of useful credit rating data.[37]

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[34] Tullio Jappelli and Marco Pagano, "Information Sharing, Lending and Defaults: Cross-country Evidence," *Journal of Banking and Finance* 26 (2002), pp 2017-2045; Tullio Jappelli and Marco Pagano, "Role and Effects of Information Sharing in Credit Markets," in Bertola Guieppe, Richard Disney and Charles Grant, eds., *The Economics of Consumer Credit* (Cambridge, Mass.: MIT Press, 2006), 347-371; Margaret Miller, ed., *Credit Reporting Systems and the International Economy* (Cambridge, Mass.: MIT Press, 2003).

[35] Alya Guseva and Akos Ronas-Tas, "Uncertainty, Risk, and Trust: Russian and American Credit Card Markets Compared," *American Sociological Review* 66 (2001), pp 623-646

[36] *Libération*, December 7, 1988.

[37] Catherine Maussion, 'Crédit: tout le monde dans le même fichier?' *Libération*, October 5, 2002.

In the United States, where tens of thousands of small lenders were offering credit, retailers and banks had long relied on chambers of commerce and other for-profit credit information services to track creditworthiness. Given the high mobility of the US population, these agencies frequently contacted each other in order to access the past credit records of new arrivals. Many sponsored Welcome Wagons as a way to assess the credit needs and creditworthiness of new arrivals.[38] In 1950, the United States had 1,500 independent rating agencies. By the early 1970s, these had consolidated into four main for-profit groups: TRW (Experian), Retail Credit Company (Equifax), Associated Credit Bureaus (Innovis), and TransUnion. As lenders began making revolving loans, they contracted with credit bureaus to track their clients' creditworthiness over time. Once consumer lending began to become profitable, in the late 1970s, consumer lenders began incorporating aggregate credit scores into their own credit risk models, and using these models to guide direct marketing campaigns to attract new customers.

Why did France not develop a similar system of centralized credit reference data collection? The problem was not a lack of know-how. In 1900, the Parisian retailer and lender Georges Dufayel had already accumulated a credit database of over 3.5 million French citizens—probably the largest rating database of its kind in the world at that time.[39] Yet early postwar lenders never created a centralized credit rating bureau. There were two reasons for this. First, consumer lenders were relatively few in number. In 1955, France had 70 registered consumer

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[38] Louis Hyman, *Debtor Nation* (Princeton: Princeton University Press, 2010).

[39] Jacques-Bernard Voirin, "Les Aspects Financiers et Economiques du credit a la consummation: etude comparative et evolutive," Doctoral Thesis in Economics, University of Paris, March 1959, p 40.

lenders, and many of these were regionally focused. This meant that lender activities did not heavily overlap, and the advantages of sharing data were not great. More importantly, the way in which they assessed credit was different. In the French system, lenders made loans indirectly, through retailers, and those retailers took responsibility for assessing credit-worthiness of borrowers. When borrowers did not pay, retailers shared in the loss. If non-payment rates rose too high for a particular retailer, it was dropped from the lender's portfolio. The system was highly effective, and non-payment rates were regularly below 1%. But it meant that consumer lenders focused on repayment by retailers rather than by individual consumers. In 1974, the four largest consumer lenders in France did begin sharing non-payment data, but they never moved to share the sort of positive data that was used to assess borrower riskiness in the United States.[40]

In the 1980s, consumer lending in France shifted from indirect sales credit to direct-to-consumer lending. This shift in practice drove demand for a new credit data service. In 1988, the Banque de France advocated adopting a centralized “white" credit data depository to which all French lenders would contribute. Coming at a time when household debt and nonpayment rates were both rising, policymakers, as well as many consumer lenders, hoped that better data on household debt levels would help target loans to more reliable borrowers.[41] The project would almost certainly have passed, had it not been for objections from France's powerful data privacy agency, the National Commission in Information and Freedom (CNIL). CNIL argued that any centralized collection of private consumer credit data would unduly infringe on the consumers'

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[40] Gérard de Chaunac-Lanzac, *La vie m'a fait crédit* (Paris, 2001), 237.

[41] Pierre-Laurent Chatain and Frédéric Ferrière, *Surendettement des particuliers* (Paris: Editions dalloz, 2000), p 188.

right to privacy, and was therefore illegal under France's data privacy law.[42] Thus, France's lack of centralized credit rating would appear to reflect different national approaches to personal privacy.

In reality, the historical roots of data privacy policy the United States and France trace their roots to early postwar consumer lending practice. In 1968, authorities in both the United States and France were drafting legislation to introduce the principle of data privacy. The trigger in each case was an initiative to unify all government-held data into a single electronic database that could be used to optimize public policy. Consumer and labor advocates in both countries pushed for lawmakers to limit the collection and sharing of private data. The focus of the legislation was on the activities of the government, but each country also had to decide how to regulate data collection and sharing by companies. In the United States, data privacy legislation became the focus of intensive lobbying by the big-three credit rating agencies, which were in the midst of digitizing their collections. Coming at a time in which policymakers were pushing lenders to offer loans to traditionally marginalized borrowers, the credit rating agencies easily convinced policymakers that the collection and sharing of private credit data promoted fair credit access. US privacy legislation was therefore limited to government-held data. In France, there was no credit rating sector to push back against a comprehensive conception of data privacy that applied the same restrictions to private companies as to the government. Without opposition from the private sector, France's privacy legislation gave CNIL a broad mandate to regulate the

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[42] Bertrand Bissuel and Anne Michel, "Les établissements de crédit accusés de favoriser le surendettement, *Le Monde*, 28 April 2005; Sylvie Ramadier, "La bataille du crédit à la consummation," *Les Echos*, 21-22 January 2005, p 8.

exchange of private data among corporations.[43] In this way, the early structure of postwar lending in France set a legal trajectory that continued to shape the sector forty year later.

Explaining Demand for Credit: The Rise of Socially Acceptable Credit

Supply conditions alone cannot explain the different patterns of consumer credit use we observe in the United States and France; we also need to understand differences in demand. Both countries harbored deep traditional concerns about the impact of consumer credit on society. In France, the Catholic prohibition against usury, combined with a history of exploitative door-to-door textile traders that offered sales on credit, had given consumer lending a bad reputation. This kind of apprehension was if anything stronger in the United States. The roots were partly religious, as in France, but also economic and social in emphasis. Almost every US state had strict usury laws on their books limiting interest rates to between 6% and 8% per year. Most were enacted in the wake of financial crises in the 18th and 19th centuries that had been attributed at least in part to credit-financed speculation. More generally, policymakers worried that consumer credit amplified the natural economic cycle, with liberal lending during periods of growth and scarcity during down cycles. By the turn of the 19th century, social progressives and worker advocates had also become concerned about sales credit. Door-to-door sellers, discount retail chains (dubbed “Borax houses”) and company stores all had the reputation of offering credit to induce their customers to purchase shoddy products.[44] Consumer lending was frequently

[43] Gunnar Trumbull, “Between Global and Local: The Invention of Data Privacy in the United States and France,” in Kirsten Bruchweh, ed., *The Voice of the Citizen Consumer* (Cambridge: Cambridge University Press, 2010).

[44] Calder, *Financing the American Dream*, p 56.

exploitative. Small salary lenders, the forebears of 21st century check traders, regularly charged 20% to 40% per month, secured against a worker's future paycheck. Yet, from this common state of popular apprehension, different attitudes toward consumer credit emerged in United States and France. This transformation occurred through a regulatory process in which this formerly disreputable activity came be seen as economically and socially legitimate.

In France, consumer lending became publicly acceptable through a close interaction with and supervision by regulators. From 1953 until 1984, France's National Credit Council (CNC), in consultation with the *Banque de France* and the French finance ministry, set the terms and volumes of credit that could be offered by consumer lenders.[45] In order to grow, consumer lenders had to behave in ways that gave the CNC reason to support them. From 1966, the CNC also set usury caps that limited the price lenders could charge. Unlike in the United States, where lenders resorted to a range of creative pricing schemes to evade the highly restrictive state usury caps, the French caps were genuinely enforced. In one sense, this sort of skepticism about markets is familiar to the French political economy. The surprise is the silence from consumer, labor and minority groups that would become strong advocates of liberal access to credit in the United States. When France did finally experiment with a liberal credit regime, between 1984 and 1989, rising debt and non-payment rates drove a backlash that placed the lending sector under new forms of government control. The result has been an approach that takes consumer credit as a legitimate economic activity so long as it is closely managed by the state.

In United States, the legitimation of consumer credit followed a different path. Although the sector remained tightly regulated at the state level until the late 1970s, a loose and evolving

[45] Albert O. Hirschman and Robert V. Rosa, "Postwar Credit Controls in France," *Federal Reserve Bulletin* 35/4 (1949), p 349.

coalition of lenders and progressive non-governmental organizations (NGOs) had from the very beginning of the 20th century begun to push for greater access to consumer credit as a response to social ills. Those NGOs included welfare societies and charitable foundations in the 1910s and 1920, labor unions in the 1950s, and women and civil rights movements of the late 1960s and 1970s. Each argued for greater access to credit on less restrictive terms in order to improve the welfare of marginalized groups. At the same time, industrialists and employers saw consumer credit as a private-sector response to social stresses that could take the place of government-managed welfare policies. It is from this coalition of interests, supported by the lending practices of banks and retailers, that an American ideal of credit as a means to economic prosperity took root.

The US Case: Harnessing Credit for Social Policy

The idea that credit might become a form of self-help for the poor and working classes emerged at the turn of the nineteenth century. At that time, a set of religion-based social reformers in Boston and New York began exploring the idea of a rigorous approach to welfare, what they called "scientific philanthropy," that would avoid the problems caused by direct welfare support. As Lewis Edwin Theiss, one of the movement's early founders, explained: "Relief, given in love, begets a degenerate craving for more."[46] Scientific philanthropy advocated modern prison reform, the policy of "friendly visiting" that became the inspiration of modern social work, as well as the idea of inexpensive credit for workers. Their model was a French institution, the mont-de-piété, or charitable pawn shop (see below). The first of these, founded by welfare reformers in New York in 1894, was the Provident Loan Society. By 1915,

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[46] Ibid., p 318.

there were 40 similar institutions across the country.[47] They made loans at 1% per month, and raised capital by issuing bonds whose return was capped at 6% per year. The idea was to offer workers and the poor a low-cost alternative to loan sharks, and many of the country's charitable foundations invested in their bonds. For the many philanthropic industrialists who helped finance the effort, charitable pawn looked like a market-based alternative to the sort of expansive welfare states that were emerging in Europe.

The problem with charitable pawn was not that it didn't work—most were highly successful—but that it was not enough. Especially in the wake of the financial crisis of 1906-7, demand for credit was so high that charitable pawn could not keep pace.[48] If enough credit was going to be made available, it would have to come from the private sector. The problem was that the high cost of making small loans meant that lenders were forced to deceive borrowers about their interest rates in order to operate below low state usury caps. In 1910, two institutions were created that would propose two very different solutions to this conundrum: the Morris Bank, and the Russell Sage Foundation. Together, they would set the trajectory of American policy toward consumer credit.

In 1909, Arthur Morris, a lawyer from Virginia, began making small unsecured loans at rates that were "reasonable to the borrower and yet fairly remunerative to capital."[49] His bank, and the network of Morris Plan banks that was founded around the country, was based on two

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[47] Shelly Tenenbaum, *A Credit to Their Community: Jewish Loan Societies in the United States, 1880-1945* (Detroit: Wayne State University Press, 1993), p 97.

[48] Morris R. Neifeld and Stuart Bruchev, *Cooperative Consumer Credit* (Manchester, N.H.: Ayter Publishing, 1979), pp 2-3.

[49] Industrial Finance Corporation, Articles of Incorporation, 1914.

innovations. First, all loans required two co-signers, who were legally liable if the borrower did not repay. This system, what Morris called “character as the basis of credit,” resulted in default rates averaging 0.25% over the duration of the Morris Plan, from 1910 to 1952.[50] The second innovation was based on some legal sleight of hand. For every $100 loan, Morris deducted $6 for interest and $2 as a processing fee. Although relatively cheap for lending at the time, this was still far above state usury laws, since the loan was repaid in weekly installments, and interest on the declining balance was closer to 13%. Morris’s solution was to channel installment payments to the purchase of investment securities that were then used to repay the loan at the end of the term. Since the loan was not technically being repaid until the end, interest on the loan was 6%, and therefore below state usury caps. Morris justified the system as a tool for encouraging thrift. Morris Plan borrowers learned to save, “in the first instance as a condition of a loan advanced by us, and afterwards and permanently, for investment.”[51] Even more important, Morris repeatedly made the case that his system would reduce class tensions, giving workers a dignified means to help themselves.[52] By 1930, there were over 140 Morris Plan banks around the country.

The other solution to the problem, proposed by the Department of Consumer Credit Studies of the Russell Sage Foundation, was to legalize higher interest rates. From 1914 to 1928, Russell Sage fought state-by-state legislative battles to enact special laws covering small loans.

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[50] AJM, Box 17, Scrap Book 1952, *San Francisco News*, March 27, 1952.

[51] Russell Sage Foundation Archives (RSF), Rockefeller Archives Center, Box 25, Folder 191, Letter from Clark Williams, President of Industrial Finance Corporation, to Robert W. deForest, vice president of Russell Sage Foundation, May 28, 1917.

[52] Elgin R. L. Gould, “The Meeting Ground of Business and Philanthropy,” in Lindsay Russell, ed., *America to Japan* (New York: Putnam’s Sons, 1915, p 136.

Under these small loan laws, lenders who registered with state regulators and disclosed the full cost of their loans as an annual interest rate (on the declining balance) were allowed to charge up to 42% annual interest. Although expensive, Russell Sage calculated that this was what small loan companies would need to charge in order to make loans profitably and legally. Early consumer advocates, as well as the loan sharks that profited from illegal lending, accused Russell Sage of promoting usurious interest rates. Eventually 26 state legislatures were won over and passed small loan laws modeled on the Russell Sage Foundation model. Loan sharks in these states disappeared virtually overnight.[53] Between Russell Sage, the Morris Bank network, and the growing number of charitable pawn shops, social progressives in the interwar period came to see personal credit on reasonable terms as a boon to working-class Americans.

In the wake of World War II, the logic of public support for consumer credit shifted to organized labor. When the Federal Reserve, under direction of the Treasury Department, imposed restrictions on downpayment and repayment periods for installment loans under Regulation W during the Korean War, the American Federation of Labor fought it vociferously.[54] It argued that restricted credit would reduce demand, and that this in turn would cause unemployment. It also supported state legislation to liberalize usury restrictions for bank and retail lending in order to extend credit access for workers.[55] There were two reasons for labor support. First, employers and organized labor both saw credit as feeding a virtuous cycle, in

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[53] RSF, Box 24, Folder 186, Letter from Shelby M. Harrison, RSF, to Jeremiah Milbank, President of the Provident Loan Society of New York, April 25, 1935.

[54] *Wall Street Journal*, December 9. 1950.

[55] J. Albert Woll, "Organized Labor Views of the Loan Shark Problem," *Law and Contemporary Problems* 19/1 (1954), p 99.

which higher demand drove manufacturing scale, productivity, and wages. Higher wages in turn drove new demand. Moreover, credit gave workers access to the benefits of new household products after years of wartime thrift. Second, labor unions in the early 1950s relied on credit to finance strike actions. During the wave of Appalachian mine strikes of the late 1940s and 1950s, workers primarily relied on credit from retailers and finance companies to hold out. In some cases, labor unions pre-negotiated lines of credit or moratoria on interest payments in preparation for a strike. For creditors, strikers to secure long-term wage contracts made workers even more reliable repayers. Even company stores almost always extended credit to striking workers.[56] Credit financing had one critical drawback. Workers were serious about repaying their debts, and unions quickly realized that they could not call a new strike before debts from the previous strike had been settled.

By the late 1960s, trade unions had become far less enthusiastic about the merits of credit for their workers. They now supported more restricted credit policies, and fought in state-level campaigns to lower usury caps. But public attention in the credit debate had by that time already shifted to issues of credit access for previously marginalized groups. Women's and civil rights advocates in particular embraced the idea of credit access as a basic right. Most prominent of these was the National Welfare Rights Organization (NWRO), an advocacy organization targeting single, mainly black mothers on welfare. In 1969, the NWRO launched a national campaign to get retailers to extend credit to their membership. When Sears refused, on the grounds that welfare mothers did not meet their risk criteria, the NWRO launched a 2 year boycott against them. Other large retail chains, including Montgomery Ward, Gimbels and

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[56] Edward J. Lally, "Coal Strikers," *Wall Street Journal*, October 31, 1949.

Federated Department Stores, all signed nationwide agreements with the NWRO.[57] The NWRO campaign, and a range of similar private and public efforts to extend credit to poor urban blacks, had been inspired in part by the findings of the Kerner Commission investigation into the sources of urban riots that had been plaguing most major inner cities in the late 1960s. The Kerner Report argued that racial tensions could be alleviated in part by greater financial access. "Rather than rejecting the American system, [the rioters] were anxious to obtain a place for themselves in it."[58] The NWRO and similar movements laid the groundwork for subsequent credit-access policies, including the 1977 Community Redevelopment Act and federally-supported low income credit unions.

As the NWRO campaign was coming to an end (repayment rates had proven disappointingly low), women's advocacy groups began to focus on credit access for white, middle-class women. The National Organization for Women (NOW) spearheaded a campaign to bring their plight into the light. As documented in thousands of testimonial letters, the greatest problems afflicted married and divorced women. Married women could only get credit in their husband's name; women's salaries were either not recognized or heavily discounted in home mortgage applications, on the grounds that they were likely to have kids and quit their jobs; many lenders requested so-called "baby letters" from doctors ensuring that a woman was infertile or on birth control. Once divorced, women had no credit rating of their own, and even

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[57] *Wall Street Journal*, December 9, 1969; *New York Times*, May 9, 1970.

[58] Kerner Commission, *Report of the National Advisory Commission on Civil Disorders*, 1968, p 7.

professional women were unable to get credit.[59] The NOW campaigns led to further legislative reforms, including the 1974 Equal Credit Opportunity Act[60] banning discrimination based on sex or marital status, and an Amendment to the 1970 Fair Credit Reporting Act requiring credit agencies to keep separate records for married women. The message was clear: to be a functioning member of society required credit, and that meant that credit access must be treated as a right, not a privilege.

The French Case: Credit and Consumer Protection

The United States was by no means unique in interpreting credit as a strategy for improving social welfare. France had been experimenting with social credit long before it was discovered in the United States. Earliest of these was the charitable pawn shop, or mont-de-piété.[61] The first mont-de-piété was opened in by the Franciscan monk Théophraste Renaudot in 1637, though it lasted only 7 years. The idea was revived in 1777 by Jacque Necker, Louis XVI's liberal finance minister. For most of the next two centuries, France's monts-de-piété enjoyed a monopoly on the domestic pawn market in return for helping the poor. They served the poor in

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[59] Archives of the National Organization for Women (NOW), Schlessinger Library, Box 211, File 41. Billie Venable Sessoms, Suzanne Nelsen, and Patricia Smith, "A Preliminary Report on Women and Cedit," National Organization for Women, Durham, North Carolina Chapter, October 15, 1973, p 11.

[60] ECOA antidiscrimination provisions were extended to include race and color in 1977.

[61] American reformers regularly traveled to Europe to study the small lending institutions there. These included Arthur Morris, founder of the Morris Plan Banks, Edward Filenes, who advocated for the founding of credit unions, and at least one Congressional research team.

two ways: offering low-interest (9% to 15%) loans at a time when personal credit was available only on exorbitant terms, and transferring excess interest income to charitable hospitals. Until World War I, the monts-de-piété had functioned independently of the state. That changed with the onset of war. Under partial German occupation, non-payment rates rose, and the government placed a ban on auctions of unclaimed pawn. This drove the monts-de-piété into insolvency. With the end of the war, and amid great social dislocation, the government began for the first time to offer direct financial aid to recapitalize the monts-de-piété. The effect was to make consumer lending a function of state welfare policy. Following World War II, the functions of the monts-de-piété were enlarged. They began offering low-cost salary loans to public employees, and, later, provided advances on welfare payments. In order to shed the social stigma that had traditionally been associated with the monts-de-piété, the institutions were rebranded as "municipal credit unions," and they continued to function as a part of France's formal welfare system.

Two features of France's early experiments with social credit differentiated its experience from the United States. First, the direct involvement of the French state painted credit in a very different light. If credit in America was seen as an alternative to an expansive welfare state, French social credit became an integral (if relatively small) function of the welfare state. And because lending by the monts-de-piété and municipal credit unions was explicitly state-sponsored, the idea of credit as socially beneficial never fully extended to private credit markets. Credit could be beneficial, in some cases, but the conditions under which it was offered had to be carefully controlled.

The second difference in the French experience was a general hostility of organized labor toward credit. If American labor saw credit as a means to fight loan sharks, finance strike actions and secure the fruits of industrialization for workers, French labor leaders saw it as mainly negative in its effect. At a minimum, they complained that high interest charges on consumer credit reduced worker purchasing power.[62] There was also a strong perception that credit contributed to the de-radicalization, or *embourgeoisement*, of the working class.[63] Leftist commentator René Creussol warned in 1956: "Employers hope that the need for regular repayment will cause workers to lose their combativeness and even, at the limit, their class consciousness, since they have to allocate a share of their salary at the end of each month toward paying their debts."[64] Concretely, he observed that workers with debts to pay were more reluctant to strike. France's communist party (CGT) was even most strident in its critique. For them, the interest paid on credit was simply another means to exploit workers once employers had reached the limits of wage restraint. "The challenges of increasing [worker] exploitation have made it necessary to resort to indirect means to recover salary payments."[65] With concerted opposition from labor, and with no other societal groups pushing actively for greater credit access, the idea of credit as socially progressive simply never took root.

Debates about consumer credit in postwar France instead focused on its implications for economic reconstruction. Officials at the *Banque de France* worried that free access to consumer credit would have two especially negative effects: that retailers would compete on providing credit rather than on price, resulting in inflation, and that consumer credit would reduce the

[62] Max Léon, "Rien à Payer," *Humanité*, July 3, 1956.

[63] René Sédillot, *La vie Française*, February 5, 1954.

[64] René Creussol, "Le Developpement des ventes a crédit," *Economie et Politique* 22 (1956), pp 78-9.

[65] CGT, *Le crédit à la consommation: facilité ou contrainte* (CGT: May 1978), p 113.

capital available for industrial investments.[66] What is striking about each of these objections is that they had very little to do with concerns about individual welfare. Early consumer finance companies worked hard to address these concerns. They argued repeatedly that credit drove scale in production, and that this led to lower prices for consumers, while also helping French exports.[67] They also repeatedly argued that consumer credit *encouraged* savings. Their idea was that regular installment payments taught consumers discipline, and that they would continue to restrain their consumption even after the loan was paid off. Rather than crowding out industrial investment, French lenders argued that consumer credit would increase savings and thus make *more* capital available for industrial investment.[68] Cetelem, one of France's early general-purpose sales finance companies, made this point clearly with their logo of a house depicted as a change bank, with a coin poised over a slot in the roof. Their case for consumer credit was not that it was good for workers or for the poor, but that it was good for France as a whole.

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[66] BdF CNC, 1427200301, Box 111: Crédit à la Consommation et vente au Crédit; Gilbert Mathieu, "Le gouvernement fixera-t-il un taux d'intérêt maximum pour les crédits consentis aux acheteurs ?" Le Monde, January 4-5, 1953.

[67] Jean Chicoye, "Les achats a credit," *Revue de l'action populaire* 140 (July-August 1960), p 794; Pierre Locardel, "L'extension du credit à la consummation sera reserve à certains articles utilitaires," *Le Figaro*, 14 April 1953.

[68] Cetelem Historical Archives, Promotional material for launch of Cetelem, "Note d'information concernant le CETELEM," September 1953, p 2.

Conclusions

Market regulation has conventionally been justified in terms either of the public interest in correcting market failures or of the social welfare interest in restricting market functions. Each kind of account relies on features of markets to justify regulation. The case of consumer credit suggests that the historical context in which markets have been constructed as legitimate matters for the way in which they are regulated. For consumer credit, the goal of early regulation was to define a logic of consumer lending and borrowing that differentiated legitimate new practices from historically exploitative practices. The basis for that legitimacy proved to be very different in France and the United States, and those historical differences went on to shape the conditions of credit market regulation over the longer term.

Two features of the historical context proved consequential for the way in which credit came to be legitimated. The first was the role of banks. The core challenge of early consumer lending was not repayment risk—workers were in general reliable repayers—but instead the high administrative costs of making small loans. These costs, coupled with restrictions on how much lenders could charge, made consumer lending a largely unprofitable business. It was the fragmented and highly competitive banking sector in the United States that led banks to offer credit, and especially revolving credit, as an inducement to attract new depositors. American retailers also provided credit, subsidized out of sales, to attract new customers. And because the goal of these loans was to attract and retain customers, the terms of lending tended to be humane. In France, banks were making profitable industrial loans to projects that were being supported through coordinated government policies. Despite periodic pressure from the state to enter the consumer lending business, most banks stayed away. Without the legitimacy that would have accompanied bank participation, French lending continued to be viewed with public skepticism.

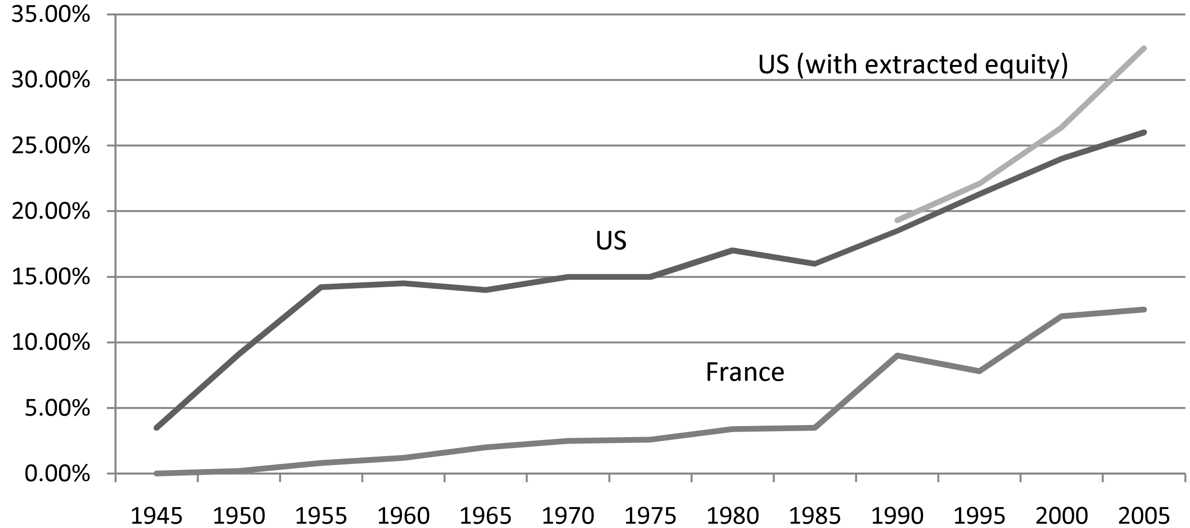
The second feature that set France and the United States on different trajectories was the divergence in attitudes about credit of progressive non-government organizations, including trade unions and other welfare and rights groups. In France, the relationship between credit and welfare was contested. France was a pioneer with early forms of social credit, including charitable pawn, but these forays into credit-based welfare were managed directly by the French state. This lent consumer credit a limited sort of legitimacy: so long as it was carefully regulated, it could provide benefits, but those benefits did not automatically emerge with free credit access. The labor left was generally opposed to consumer credit, which they saw as reducing worker purchasing power, and also potentially reducing worker militancy. Nor did other advocacy groups push credit access for socially marginalized groups. France's tradition of republican citizenship implied equal treatment by the state, but not universal access to all products and services in the marketplace. In particular, the idea of "positive discrimination" in promoting market access was antithetical to the republican ideal.[69]

In the United States, an evolving coalition of lenders and non-profit societies pushed the idea of credit access as welfare improving: from anti-loan shark campaigns in the 1920s, to early postwar credit intended to give workers access to new household products, to campaigns in the 1970s to extend credit to urban blacks and middle-class women. The center-left "third way" movement of the 1990s continued to embrace expanded credit access as a means to improve the welfare of the worst-off in society. In a sense, it is hardly surprising that American consumers came to perceive consumer credit as a path to prosperity. For nearly three generations, coalitions

[69] Luc Matray, Director General of the Credit Municipal de Paris, "Introduction," *La Bacarisation des nouveaux marchés urbains,* a study commissioned of the US credit markets, 2004, p VI.

of progressive activists and conservative industrialists assumed that access to credit generated positive social outcomes.

Figure 1. Non-mortgage household debt in France and United States (share of disposable household income).



Sources: United States Federal Reserve Bank; Banque de France; Alan Greenspan and James Kennedy, “Sources and Uses of Equity Extracted from Homes,” *Oxford Review of Economic Policy* 24/1 (2008), pp 120-144.

Note: Home equity extraction contribution to consumer spending and debt reduction estimated at 80% of total home equity extraction, assuming that 20% of extracted equity was shifted to other assets. Based on Kennedy and Greenspan, 2008. France experienced no significant home equity extraction.