STABILITY PROGRAMME

APRIL 2018

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1.Overview

This Stability Programme outlines France's fiscal planning for 2018-2022. It updates the government's economic and fiscal guidelines for 2018-2022, which are described in the Public Finance Planning Act (LPFP) of 22 January 2018. In this way, it is a complement to the National Reform Programme, which is issued at the same time, and which lists all of the economic reforms undertaken by the government.

In 2017, the deficit was brought back below the 3% threshold and France complied fully with its European commitments, thus laying the groundwork for the country exiting the Excessive Deficit Procedure in the third quarter of 2018. Thanks to the government's ambitious cost-cutting measures, France complied with its European commitments. The overruns revealed by the French Government Audit Office (*Cour des comptes*) in its June 2017 audit have been brought under control, and the effect of the Constitutional Council ruling against the 3% contribution on dividend distributions was offset by the introduction of an exceptional corporate income tax payment that was approved in a Amending Budget Act for 2017.

In a economic environment that continues to be favourable, the macroeconomic scenario for 2019 in this Stability Programme has been adjusted upward since the LPFP was issued. Economic signs point to a continuation of the 2017 recovery, buoyed by a positive international climate, business investment, household consumption and the renewed confidence in economic circles in the wake of the May 2017 presidential election. The ongoing recovery of the euro area and robust domestic demand should be propitious for business activity during this period. Rising household purchasing power, at a time of favourable changes in the labour market and measures to support that purchasing power, coupled with an unprecedented increase in investments by business, are expected to boost private domestic demand in 2018 and 2019. Growth is predicted to reach 2.0% in 2018 and 1.9% in 2019, and there should be a particularly strong upswing in employment. Inflation, which stood at 1.0% in 2017, is expected to reach 1.4% in 2018 and then fall to 1.2% in 2019.

The fiscal consolidation measures for the period covered by this Stability Programme will rely on continuing efforts to reduce the government expenditure ratio, which will be shared by all general government sub-sectors. Real growth of public expenditure, excluding tax credits, is forecast to be 0.7% in 2018 and 0.4% in 2019, a sharp drop over 2017 (1.5%). Taken together with excellent growth prospects for the period in question, the expenditure ratio should decline by 0.7 points of GDP in 2018 and 0.9 points in 2019.

These efforts will help finance a sharp reduction in the tax burden ratio, which is expected to fall by one percentage point over the government's five-year term. This in turn will boost the French economy's long-term growth prospects. Starting in 2018, the government decided to reduce taxes by more than €10bn. This trend will continue in 2019, with further cuts in the residence tax, the replacement of the Competitiveness and Employment Tax Credit (CICE) with a permanent reduction in social security contributions and continuing efforts to lower the corporate income tax. Pursuing this path will allow France to quickly roll out measures that embody the government's stra-

tegic choices, including: *i)* unleashing the full potential of France's economy; *ii)* developing tomorrow's growth model; iii) recasting our social model in order to build a fairer and more mobile society and *iv)* transforming the central government and balancing public finances.

This strategy will make it possible to correct the structural imbalances in our public finances in a way that is compatible with investments needed to implement major structural reforms (labour market, vocational training, taxation, investment, housing, climate, etc.). The general government balance is expected to show a deficit equivalent to 2.3% of GDP in 2018, and then 2.4% in 2019 as a result of the temporary double cost of converting the CICE into a permanent cut in social security contributions. This path reflects an improvement in the structural balance (called structural adjustment) of the country's public finances, in accordance with the Public Finance Planning Act, of +0.1 percentage points of GDP in 2018, within the context of an output gap that remains wider than most of France's European partners, followed by an average annual adjustment of +0.35 points between 2019 and 2022. This would bring the country's public debt below 90% of GDP in 2022.

2. Macroeconomic scenario

2.1 SITUATION IN 2017 AND OUTLOOK FOR 2018 AND 2019

After posting growth of 2.0% in 2017[1], France's economy should again grow by 2.0% in 2018 and then by 1.9% in 2019. Inflation, which stood at 1.0% in 2017, is expected to reach 1.4% in 2018 and then fall to 1.2% in 2019.

The recovery observed in 2017 is expected to continue in 2018 and 2019, buoyed in particular by a positive International environment. The ongoing recovery in the euro area and the upswing in global demand is expected to stimulate a surge in exports and a noticeable improvement in the contribution of foreign trade to growth, which should cease to put a damper on growth starting in 2018. Rising household purchasing power, at a time of favourable changes in the labour market and measures to support that purchasing power, coupled with an unprecedented increase in investments by businesses, are expected to boost private domestic demand. Growth is expected to weaken very slightly in 2019 as a result of a minor slowdown in external demand addressed to France. This would affect exports and worsen the outlook for demand for businesses, which, combined with a gradual rise in interest rates, could lead to a falloff in business investment from the growth rates reached in 2017 and 2018.

These forecasts are similar to those of the main national and international bodies. The Consensus Forecasts of March 2018 predicts growth of 2.1% in 2018 and 1.8% in 2019. In its March 2018 publication, the Banque de France forecasts 1.9% in 2018 and 1.7% in 2019. The European Commission adjusted its forecast upwards, to 2.0% and 1.8%, respectively (Winter Forecast published on 7 February 2018, see Box 1 for a comparison of forecasts), as did the OECD, to 2.2% and 1.9% (Interim Forecast issued on 13 March 2018). The IMF will issue its new forecast on 17 April 2018.

French economic growth, which has been robust since late 2016, is expected to remain strong in the first quarter of 2018.

At 0.7%, growth in the fourth quarter of 2017 was strong – the momentum of the return to growth in the fourth quarter of 2016 picked up, with a fifth consecutive quarter of growth of at least 0.5%. Year-on-year, growth reached 2.5% in the fourth quarter of 2017, a pace that has not been seen since the first quarter of 2011. This forward momentum is consistent with the good results from business surveys since mid-2017, which indicate that business confidence is at its highest point in six years.

The uptick in activity at year's end is a reflection of the strong rise in manufacturing output (+1.5% in the fourth quarter) and **the highly positive contribution of foreign trade** (0.7 points in

[1]Growth within the meaning of the quarterly accounts, adjusted for working days. It is 1.8% within the meaning of gross annual accounts, i.e. non-corrected for working days.

the fourth quarter). On the supply side, the momentum of the production of transport equipment, capital goods and other manufactured goods contributed strongly to the quarterly increase in manufacturing output, which was at the highest point since the second quarter of 2013. On the demand side, exports rose sharply, buoyed – as in 2016 – by a number of Airbus deliveries in December and by a boost in exports of services. Business investment grew strongly, despite a slight decline in public works activity that led to a decline in investment in this sector. Similarly, household investment in this sector also slowed, in line with the weaker trend in housing starts since mid-2017. Household consumption was driven by consumption of services.

Business surveys (INSEE, Markit and Banque de France) were at very high levels in late 2017 and early 2018, well above average. Depending on the survey, these levels had not been reached since 2007 or 2011. Household confidence is stable, at a level close to its long-term average.

TABLE 1: MACROECONOMIC SCENARIO 2017-2022

Annual growth rate (in %)	2017*	2018	2019	2020	2021	2022
Gross domestic product**	**1.8**	**2.0**	**1.9**	**1.7**	**1.7**	**1.7**
Household consumption expenditure	1.3	1.6	1.9	1.7	1.7	1.7
General government consumption expenditure	1.6	0.7	0.2	-0.1	0.2	-0.4
Gross fixed capital formation (GFCF)	3.8	3.9	3.3	2.3	2.1	2.6
o.w. non-financial corporations	*4.4*	*4.4*	*3.5*	*3.4*	*3.4*	*3.4*
Contribution to real GDP growth of changes in inventories	0.4	0.0	0.0	0.0	0.0	0.0
Contribution to real GDP growth of external balance of goods and services	-0.3	0.1	0.0	0.2	0.2	0.2
Imports	4.1	4.1	4.1	3.7	3.7	3.7
Exports	3.3	4.9	4.6	4.4	4.4	4.4
GDP deflator	0.8	1.1	1.2	1.5	1.75	1.75
Household consumption deflator	0.9	1.4	1.2	1.5	1.75	1.75
Wages and salaries (non-farm business sector)	3.6	3.9	3.6	3.7	3.8	3.8
Wages and salaries per employee (non-farm business sector)	2.0	2.4	2.3	2.5	3.0	3.0
Employment, persons (non-farm business sector)	1.5	1.5	1.3	1.2	0.9	0.8

* Quarterly national accounts (detailed figures) for the fourth quarter of 2017, unless otherwise specified
** No adjustment for working days

Despite a slight slowdown, growth should remain solid in the first quarter of 2018 The contribution of foreign trade is expected to represent a fall-back compared to the end of 2017, primarily due to Airbus deliveries returning to normal after a record fourth quarter. In the same way, household consumption, particularly of services, should slow. This should also be true of total investment: for

households, this should result from the drop in housing starts in the second half of 2017 and, for businesses, from the fact that the slowdown in productive investment would not be offset by an expected upturn in public works.

After picking up sharply in 2017 (3.7%, after 3.3% in 2016), global economic activity is expected to maintain a similar pace in both 2018 and 2019 (3.8% both years), with both advanced and emerging countries contributing.

Growth should be even higher in the US, but should slow in Japan and the UK. In the US, activity is expected to pick up under the effect of expansionary fiscal measures (tax reform and the new budget passed by Congress, which will increase spending). On the other hand, growth is expected to slow in Japan – although still buoyed by the upswing in exports and domestic demand – and in the United Kingdom, under by the negative effects of the uncertainties surrounding Brexit.

Recovery in the euro area is expected to continue at a sustained pace. Growth should be driven by the forward momentum of domestic demand at a time of renewed household and business confidence, and by the upward thrust in global demand. Among the major euro area countries, growth should remain robust but show a slight decline in Spain, while remaining stable in Germany and Italy.

Growth is expected to be broadly stable in emerging economies. Vigorous growth is expected in Brazil and, to a lesser extent, India. It should remain largely stable in Russia and decline sharply in Turkey. China, on the other hand, should gradually slow over the period in question, as the country's monetary and fiscal stimuli are gradually curtailed.

Trade is expected to play a major role in world growth. After two years of moderate growth (2.0%), world trade picked up sharply in 2017 to reach 5.3%, the highest level since 2011. It is forecast to slightly slow but remain strong in 2018 and 2019 (5.1% and 4.7%, respectively). After a remarkable turnaround in 2017, imports should grow at a slower pace in Russia, China and India. In advanced countries, trade should benefit from continued momentum in the United States, but is expected to be held back in 2019 by the expected slowdown in activity in Japan, the UK (in connection with the arrival of the effects of Brexit) and in the euro area.

World demand for French exports is expected to maintain the same profile as world trade over the forecast horizon: growth should remain roughly the same in 2018 (5.0%), after 5.1% in 2017, and should achieve 4.7% in 2019. Since the 2018 Draft Budget, this figure was revised upward (by about 1 point) due to an upswing in trade in both advanced economies and the leading emerging economies.

Against a backdrop of a more positive international environment, foreign trade is not expected to dampen growth in 2018 and 2019.

In 2017, foreign trade acted as a brake on growth. Exports picked up (3.3%, after 1.9% in 2016) but did not fully and immediately benefit from the upswing in world demand (5.1%, after 3.1%), although imports remained robust (4.1%, after 4.2% in 2016), in connection with strong growth in demand areas that are import-intensive (productive investment by companies, inventories). Concurrent with robust imports and exports that fell short of average world demand, there was a positive change in inventories, particularly in transport equipment (some €4.5bn), which may have been due to slight shifts in the production chain.

Exports should be dynamic in 2018 and in 2019 (4.9% in 2018 and 4.6% in 2019), driven by robust global demand (5.0% in 2018, after 5.1% in 2017, and 4.7% in 2019) and a large number of deliveries of major export contracts (Rafale aircraft, cruise ships), and an expected return to normal for tourism and agricultural exports.

Imports are expected to continue to grow at the same rate in 2018 and 2019 (4.1%, the same as in 2017), despite a minor falloff in domestic demand (1.8% in 2018 and 2019 after 2.2% in 2017).

The trade deficit in goods deepened from €48.3bn in 2016 to €62.3bn in 2017 (based on Customs data), given the fall-off in the commercial balance excluding energy. It should remained roughly stable in 2018 (€61.8bn): rising oil prices should increase the deficit, but export volumes are expected to grow more rapidly than import volumes. The commercial balance should remain stable in 2019 (–61.1bn), under the hypothesis that oil prices will remain stable. **Finally, in 2018, foreign trade is forecast to again make a positive contribution to growth.**

Household consumption is expected to pick up speed in both 2018 and 2019.

After a strong turnaround in 2016 (1.8%), purchasing power grew at a slightly slower pace in 2017 (1.5%). It is expected to pick up slightly to 1.6% in 2018, mainly as a result of stable real wage growth in non-farm market sectors and continued strong job creation. In 2018, new direct taxation measures would buoy household disposable income and thus purchasing power, while indirect tax measures would fuel inflation and thus reduce purchasing power. In 2019, household purchasing power is expected to pick up sharply (1.9%) within a context of continuing job creation. It should be driven by new initiatives concerning aggregate tax and social security contributions (second phase of the reduction in the residence tax, full-year effect of contribution reductions, etc.) and by the acceleration of property incomes (improvement in the financial situation of businesses and a rise in interest rates), while benefiting from more moderate inflation than in 2018 (1.2%, after 1.4%).

Consumption should accelerate at the same rate as purchasing power in both 2018 (1.6%) and 2019 (1.9%). After having reached a low point in 2016 (14.0%), the savings rate rose in 2017 to 14.2%, and is expected to remain stable in 2018 and 2019.

Household investment should remain robust.

After hitting a growth peak in 2017, household investment should continue to progress during the horizon period. After increasing in 2016 (2.4%, after falling by 2.1% in 2015), household investment took a sharp upturn in 2017 (5.3%) driven both by residential investment and very high levels of real estate transactions (notary and estate agency fees are recorded as investments in service). This turnaround comes from increased purchasing power and higher employment, as well

as the sharp rise in property prices. Household investment is forecast to slow in 2018 (2.5%), and then should maintain the same rate in 2019 (2.5%). It should be sustained by the rise in purchasing power and employment but should be held back by a gradual rise in interest rates.

Business investment should slow but remain robust over the forecast horizon.

After picking up in 2017, business investment is expected to grow at a stable pace in 2018 (4.4% in 2018, the same as in 2017) and then slow down in 2019 (3.5%). Continued growth in investment should be driven by capacity utilisation rates above their historical average, tax measures to encourage investment in the 2018 Budget Act, continued low interest rates, high growth in the added value of non-farm market sectors, and a transition year in 2019 in which the CICE is shifted over towards permanent reductions in employer contributions. The expected slowdown in business investment in 2019 can be attributed to the gradual increase in interest rates and the decline in external demand.

Inflation is expected to rise to 1.4% in 2018, mainly due to an increase in tobacco taxes, before slowing in 2019.

In 2018, core inflation is expected to reach 0.7%, after 0.4% in 2017, fuelled by a rise in inflation in the services sector in connection with the gradual recovery of nominal wages. It is expected to be reined in by a fall in the prices of manufactured goods, which have been negatively affected by exchange rate increases, and by a fall in rental inflation linked to the drop in housing benefits. Total inflation should rise to 1.4% in 2018, after 1.0% in 2017, mainly due to the increase in taxes on tobacco (with a 0.3 point impact on the CPI). Higher oil prices and energy taxes should lead to a 0.5 point impact on the IPC, as in 2017.

2019 should see the gradual recovery of core inflation, to 0.9%: sluggish growth in the prices of manufactured goods, still labouring under exchange rate rises, should be more than offset by higher service prices and increased rents. This scenario is consistent with the closing of the output gap. Nevertheless, overall inflation should fall slightly in 2019 to 1.2%, as energy prices and new tobacco-related measures are expected to provide much less support for inflation.

Market sector employment is expected to remain robust in 2018 and 2019.

Market sector employment in 2017 was particularly strong (an annual average of 240,000 new jobs), buoyed by the pickup in activity and continued active support from employment policies. In 2018, market-sector employment is expected to continue its strong growth (250,000 more jobs on average per year), driven by activity within a context of less support from employment policies (a reaction to the end of the hiring bonus, the full deployment of the CICE and the Responsibility and Solidarity Pact and the decrease in the CICE from 7 to 6 %). This trend should continue in 2019 at roughly the same pace (225,000 more jobs on average): activity should be very slightly less dynamic, but converting the CICE tax credit into social security contribution cuts should help sustain employment in comparison with 2018.

Non-market sector employment is forecast to shrink in 2018 (25,000 fewer jobs on average per year), after a strong 2017 (35,000 more jobs). This contraction is explained by lower allocations for subsidised employment contracts at the end of 2017 and in 2018 (provided for in the 2018 Budget Act). The decline in non-market sector employment is expected to continue in 2019 (25,000 fewer jobs on average per year) as a result of a further reduction in subsidised contracts during this period.

2.2. MEDIUM-TERM OUTLOOK (2020-2022)

Activity should remain strong up to 2022

Starting in 2020, growth is predicted to reach 1.7%.

This prediction is based on potential growth of 1.25% for 2017–2020, 1.3% in 2021 and 1.35% in 2022. This estimate, which remains unchanged with respect to the 2018–2022 Public Finance Planning Act, is based on a lower-than-pre-crisis productivity trend, partly due to the slowdown in the effects of technical progress observed at global level.

Potential growth should increase by 2022, due to the positive effects of the structural reforms implemented during the current presidential term, particularly those intended to promote training and apprenticeships, lower the tax wedge on wages (replacing employees' social security contributions with the general social security contribution (CSG)), streamline the labour code and support productive investment (reduction of corporate income tax rate to 25%, introduction of the single flat-rate levy, replacing the wealth tax by the property wealth tax (which no longer acts as a brake on securities and risk investing) and encourage innovation (making the Research Tax Credit permanent and creation of the Industry and Innovation Fund).

After seven years of a negative output gap (2012–2018), activity is expected to continue its cyclical rebound. Thus, the output gap, which should turn positive in 2019, should continue to expand while remaining below the levels observed prior to the 2008-2009 crisis or in the early 2000s.

Inflation should gradually recover, assuming that the ECB manages to direct inflation expectations towards its medium-term target. For France, inflation is expected to converge towards 1.75% in 2022.

Major uncertainties are surrounding this forecast

If the recovery in our euro area partners is stronger than expected, global demand to France would be more robust than in our scenario, stimulating French exports to the euro area. Conversely, if political tensions materialise in Europe, this could reduce growth (for example, the magnitude of the effects of Brexit).

If protectionist measures are put in place in a comprehensive manner, for example in response to steel and aluminium tariffs in the US and the stated intentions of US authorities to place more tariffs on Chinese imports , the trade-induced slowdown could weaken the global economy.

If, out of fear of a rapid rise in inflation due to overheating in the United States, the Fed decides to raise rates more quickly, the dollar could appreciate and the euro depreciate against the dollar, which would improve France's competitiveness. The ECB could also decide to extend its unconventional monetary policy should core inflation remain low in the euro area.

Beyond these international uncertainties, those specific to France could also appear.

Reforms in recent years combined with high levels of investment by French companies could improve export performance.

The ability of French companies to invest is also uncertain. If firms felt the need to more strongly reduce their debt due to concerns about activity or higher interest rates, this would put a damper on their investments and potentially on wages, and consequently on household consumption. However, it would appear that the recent increase in non-financial corporate debt is mainly attributable to large firms that are otherwise accumulating liquidity and thus maintaining investment capacity. Finally, the measures implemented to support investment (reduction in the corporate income tax rate, introduction of the single flat-rate levy, wealth tax reform) could have a faster-than-anticipated effect on growth.

Companies in many sectors report recruitment difficulties. If these difficulties were to persist, it would mean that unemployment would be close to its structural level. Labour market tensions would translate into wage increases, but also into lower competitiveness, less expansion of production capacity on French soil, and greater recourse to imports to meet demand. Conversely, if the government's training plan produced rapid results, it would have positive effects on labour supply and thus growth.

BOX 1: COMPARISON WITH THE EUROPEAN COMMISSION'S WINTER FORECASTS

The Stability Programme's growth scenario is close to the European Commission's latest forecasts. In its February 2018 Winter Forecasts, the Commission projects growth of 2.0% in 2018 and anticipates a slight slowdown to 1.8% in 2019. These figures have been revised upwards significantly since the Autumn Forecast (1.7% in 2018 and 1.6% in 2019).

According to the Commission, activity should be mainly upheld by internal growth drivers, consumption and investment, and extended by favourable foreign trade in a positive international environment. However, the details of the macroeconomic scenario for the Winter Forecasts have not been communicated.

The European Commission's inflation forecast, according to the harmonised price index, calls for an increase to 1.5% for 2018, similar to the Stability Programme, and remains at the same level in 2019, whereas it slows by 0.2 points in the Stability Programme's scenario.

BOX 2: DATA PRESENTED FOR 2017

The data presented for 2017 are those appearing in the Detailed Results of the quarterly national accounts for Q4 2017, published by INSEE on 26 March 2018. Because of the sequential procedure between the public finance part and the real part of the economy, the public demand line items in the Detailed Results differ from information relating to public finances in INSEE's provisional general government account. The public finance and national accounts data to be published in May by INSEE will include the figures from the provisional general government account.

The macroeconomic scenario is based on data from the provisional general government account but, for the sake of consistency, it has been decided to display data for 2017 only from the quarterly accounts.

For example, according to the quarterly accounts, public investment would have increased in 2017 by 0.3% in nominal terms and -1.0% in real terms (in working-day adjusted data). It is this -1.0% change that is presented. The initial results of the national accounts, published on 26 March 2018 by INSEE, indicate an increase in nominal terms (not adjusted for working days) of +3.0% in 2017. In the figures presented here, real public investment increases from -1.0% in 2017 to +3.8% in 2018, a seemingly very strong upswing; the acceleration based on the provisional general government account is weaker.

3. Fiscal strategy

3.1 OVERALL STRATEGY

With a public deficit standing at 2.6% of GDP in 2017, France has honoured its commitment to achieve less than 3 percentage points of gross domestic product in 2017, opening the way for an exit from the Excessive Deficit Procedure in the third quarter of 2018. The government's strategy for the years from 2018 to 2022 is to maintain efforts to reduce the general government deficit by containing public expenditure. This will ensure the sustainability of public finances and make substantial tax cuts possible to boost employment, purchasing power, investment and the competitiveness of French businesses, thereby strengthening the long-term growth of our economy.

The government has maintained the structural adjustment targets set out in the Public Finance Planning Act for 2018 to 2022, which have been adapted to keep pace with ongoing reforms to transform the French economy. These structural efforts, along with better-than-expected results in 2017 and stronger growth in 2018 and 2019, mean that the **headline deficit adjustment path is faster than in the Public Finance Planning Act and the government now foresees a slight general government surplus in 2022.** The debt ratio should also start to fall in 2018, dropping below 90% of GDP in 2022.

This fiscal strategy avoids past mistakes with economic policies that were too often procyclical. The strategy puts debt on a resolutely downward path, as has been the case in practically all European countries. Continuing a deficit-reduction strategy at a pace that is appropriate for the French economy's position in the business cycle also helps to preserve tax cuts and gradually build up fiscal headroom again.

In 2017, the government's strong consolidation measures in the third quarter brought the general government deficit down to less than 3% of GDP, in compliance with our European commitments: the deficit fell from 3.4% in 2016 to 2.6% in 2017, in part because of a substantial reduction of 0.5 percentage points of GDP in the structural deficit.

In 2018, the headline deficit is expected to shrink to 2.3% of GDP, as economic conditions continue to brighten. Measures to reduce taxes and social security contributions from 45.4% of GDP to 45.0% will be more than offset by efforts to contain expenditure. The structural deficit is expected to improve by 0.1 percentage points of GDP.

Slower growth of public expenditure, excluding tax credits, with 0.7% real growth in 2018, versus 1.5% growth in 2017, will require a major effort. This would reduce the public expenditure ratio by 0.7 points of GDP, in line with the government's commitment to decrease the public expenditure ratio (excluding tax credits) by more than 3 percentage points of GDP over its five-year term.

All general government sub-sectors, including central government, local government and social security funds, will contribute to slowing expenditure growth. Following particularly strong wage growth in 2017, containment of pay increases will slow the growth of the public sector

wage bill sharply, with real growth of 0.3% in 2018, compared to 1.2% growth in 2017. At the same time the national healthcare expenditure growth target (Ondam) will be limited to 2.3%. Finally, the Financial Pact between central government and local governments aimed at capping their operating expenditure growth at 1.2% per year for five years will be implemented for the first year.

In parallel to these efforts to contain expenditure, tax cuts of more than €10 billion in 2018 will enable us to address three of the government's strategic choices. The first is to provide immediate support for growth, promote employment and boost purchasing power by providing greater rewards for work. The second is to boost competitiveness and unleash enterprise. The third is to boost private-sector investment in businesses that take risks, innovate and create the jobs of tomorrow.

The government will continue its strategy to contain public expenditure and reduce taxes and contributions in the years from 2019 to 2022.

The government plans to step up its efforts to contain public expenditure, with average real expenditure growth of 1/4% between 2019 and 2022, which is much lower than the average growth rate seen since the financial crisis (0.8% growth from 2010 to 2016). This will cut public expenditure ratio by more than 3 percentage points by 2022. The effort will be shared by all general government subsectors. The government's *Public Action 2022* reform process will identify structural savings, particularly in central government expenditure, as well as in social expenditure, related to structural reforms in the sectors concerned. Under the terms of their Financial Pact with central government, local governments will continue their efforts to contain operating expenditure. The adjustment path calls for containment of health insurance expenditure over five years, with the national healthcare expenditure growth target set at less than 2.3% from 2019 to 2022, and falling unemployment means that the unemployment insurance scheme (Unedic) should achieve financial equilibrium again by 2019. This reduction of public expenditure is critical not just to make public action more effective; it is also needed to make tax cuts credible and maximise their impact on business investment and hiring.

Taxes and contributions will continue to fall to 44.3% of GDP in 2022, for the benefit of both business and households. For businesses, the cut in taxes and contributions will be transformed in 2019, as the Competitiveness and Employment Tax Credit (CICE) is replaced with a permanent cut in social security contributions targeting low-wage jobs in particular. The corporate income tax rate will also continue falling to stand at 25% in 2022, which is the average rate in the European Union countries. For households, tax cuts will mean further cuts in the residence tax over three years and exemptions from social security contributions on overtime pay. The net decrease in taxes and contributions factors in the increase in carbon taxes, along with continuing convergence of tax rates on diesel oil and petrol to boost ecological conversion.

The faster-than-expected reduction of the headline deficit, combined with faster economic growth at the beginning of the period, means that France's general government debt ratio will fall in 2018 and should stand at less than 90% of GDP in 2022. The structural adjustment path under the Stability Programme is consistent with the commitment in the Public Finance Planning Act to use the growth dividend to reduce general government debt.

Bringing the fiscal deficit back down to less than 3% of GDP between 2017 and 2019 will open the way for an exit from the Excessive Deficit Procedure, to be ratified by the European Union Council of Finance Ministers in the third quarter. France's government will continue its fiscal consolidation efforts between 2018 and 2022 to meet the medium-term objective, in accordance

with the recommendation of the European Council, against the backdrop of a persistent negative output gap in 2018 and implementation of major structural reforms affecting the labour market, job training, taxes, investment, housing, climate change, etc. The pace of structural adjustment factors in the negative output gap in 2018 and the investment required to back up major structural reforms affecting the labour market, job training, taxes, investment, housing, climate change, etc.

TABLE 2 - ADJUSTMENT PATH

	2016	2017	2018	2019	2020	2021	2022
General government balance and structural analysis							
General government balance	**-3.4**	**-2.6**	**-2.3**	**-2.4**	**-0.9**	**-0.3**	**0.3**
Nominal adjustment		*0.8*	*0.3*	*-0.1*	*1.4*	*0.6*	*0.6*
Cyclical balance	-0.8	-0.5	-0.1	0.2	0.5	0.7	0.9
One-offs (as a % of potential GDP)	-0.1	-0.1	-0.3	-1.0	0.0	0.0	0.0
Structural balance (as a % of potential GDP)	-2.5	-2.0	-1.9	-1.6	-1.4	-1.0	-0.6
Structural adjustment		*0.5*	*0.1*	*0.3*	*0.3*	*0.4*	*0.4*
Main aggregates							
Government expenditure ratio (excluding tax credits)	**55.1**	**55.1**	**54.4**	**53.5**	**52.6**	**51.9**	**51.1**
Nominal public expenditure growth, excluding tax credits (%)		*2.5*	*1.8*	*1.4*	*1.7*	*2.0*	*1.9*
Tax and social security contributions rate, net of tax credits	**44.6**	**45.4**	**45.0**	**44.0**	**44.3**	**44.3**	**44.3**
General government debt							
General government debt	**96.6**	**97.0**	**96.4**	**96.2**	**94.7**	**92.3**	**89.2**
excluding financial assistance for the euro area	93.6	94.1	93.7	93.5	92.1	89.8	86.8

3.2 OUTTURN 2017

On 26 March 2018, the French national institute of statistics and economic studies (Insee) published the preliminary general government accounts showing a deficit of 2.6% of GDP (€59.3bn) in 2017, compared to 3.4% in 2016. The improvement stems from a 4.0% increase in public revenue (including tax credits), as economic conditions brightened. This was larger than the 2.5% increase in public expenditure (including tax credits). Regulatory measures introduced in the third quarter of 2017 and worth nearly €5bn helped contain the growth of public expenditure and led to a slight decrease of expenditure ratio from 56.6% in 2016 to 56.5% in 2017 (including tax credits). Without the one-off expense of reimbursing the 3% tax on dividends in 2017, the decrease would have been greater, with public expenditure standing at 56.3% of GDP.

In 2017, the aggregate tax and social security contribution rate stood at 45.4% of GDP, compared to 44.6% in 2016. The increase in this rate stems from exceptionally strong spontaneous growth and accounting restatements made by Insee after rebasing the system of national accounts. Strong revenue growth was sustained by the growth of total payrolls, corporate earnings, household consumption and private-sector investment as the economy recovered and by rising capital gains on property. Taxes and contributions posted spontaneous growth that was faster than GDP growth, with aggregate elasticity of 1.5, compared to the 1.3 elasticity assumption used for the 2018 Initial Budget Act. This strong revenue growth reflects a very sharp improvement in the French economy and renewed consumer and business confidence. Backward compilation of accounts by Insee after rebasing led to an increase in the aggregate tax and social security contribution rate, as a result of reclassifying the television license fee as a tax (adding €3.3bn) and the restatement of the reimbursement of the disputed 3% dividend tax as an expense rather than a decrease in revenue (adding €4.7bn).

In aggregate, the general government balance was €16.6bn smaller than in 2016, as a result of the €9.5bn improvement in the State government balance, the €7.3bn improvement in the social security funds balance and, to a lesser extent, €2bn improvement in the balance of other central government bodies. The local government balance continued to post a surplus of €0.8bn, compared to €3.4bn in 2016, despite a decline of €2.2bn.

The €9.5bn improvement in the central government balance stems from 5.4% growth of revenue (including tax credits) for a €21.7bn increase, which outstripped the 2.5% growth of expenditure (including tax credits) for an increase of €12.2bn. The main source of increased revenue was a jump of €7.9bn in VAT revenue, and €4.9bn in revenue from the exceptional corporate income tax payment for large corporations designed to offset the reimbursement of the disputed 3% tax on dividends. The increase in expenditure stems in part from strong wage growth, following the previous government's decision on a civil service pay raise, bonuses and measures introduced under the agreement on professional development, careers and compensation (PPCR).

The social security fiscal balance also improved. The social security accounts posted a surplus for the first time since 2008 as a result of revenue growth of 3.7%, which was greater than the expenditure growth of 2.4%. The revenue growth stems largely from strong wage growth of 3.5%, which produces faster growth of social security contributions, which rose by 3.5%. It also stems from a 3.3% rise in revenue from taxes on income and assets, which are based in part on payrolls. Furthermore, the growth of healthcare insurance expenditure was contained, leading to an expenditure increase of 2.2% compared to 2016, following an increase of 1.8% in 2016. This growth is consistent with the national healthcare expenditure growth target of 2.1% set out in the 2017 social security

Budget Act. The difference stems from a slight downward revision of 2016 expenditure, which does not affect the target set for 2017.

The local government balance shrank, showing a surplus of €0.8bn in the national accounts, following a surplus of €3.0bn in 2016 and a deficit of €0.1bn in 2015. Expenditure growth outstripped revenue growth as local government investment expenditure rose again, after declining for three years in a row, and wage bills increased because of the civil service pay raise in February and the reforms under the agreement on PPCR.

BOX 3 – IMPACT OF REBASING ON FORECASTS

“Rebasing" national accounts means recalculating past accounts. There are several reasons for these recalculations, the main ones being new information that affects past accounts and the objective of making different European countries’ methodological choices more consistent under the European System of National and Regional Accounts (ESA 2010). Rebasing has a minor impact on the general government balance and also affects the Maastricht debt.

General government balance (in € bn)	2008	2009	2010	2011	2012	2013	2014	2015	2016
2010 base year	-63.5	-138.9	-135.8	-105.0	-100.4	-85.4	-84.4	-78.7	-75.9
2014 base year	-65.0	-138.9	-137.4	-106.1	-104.0	-86.5	-83.9	-79.7	-75.9
Difference in € bn	**-1.5**	**-0.1**	**-1.6**	**-1.1**	**-3.6**	**-1.1**	**0.4**	**-1.0**	**-0.1**

Maastricht debt (in € bn)	2008	2009	2010	2011	2012	2013	2014	2015	2016
2010 base year	1357	1531	1632	1754	1868	1953	2038	2098	2147
2014 base year	1370	1608	1701	1808	1893	1978	2040	2102	2152
Difference in € bn	**13.0**	**77.2**	**69.4**	**54.2**	**24.2**	**25.3**	**2.4**	**3.5**	**4.9**

Source: Insee

The main recalculations of general government accounts are as follows:

- **Sales of mobile phone licenses** are spread over the period of spectrum use. Under the 2010 base, such sales were recognised as a reduction of expenditure (sale of non-produced assets) in the year of the sale. They are now recorded as rents received by central government over the 20-year license period.
- **Reclassification of soft loans from the central government to Agence française de développement** (AFD) **as central government expenditure** and, symmetrically, of loan repayments from AFD as central government revenue.
- **The estimate of uncollectible taxes and contributions** has been updated and affects taxes and contributions and the general government deficit, particularly the central government and social security fund deficits;
- Write-offs of assets and liabilities by local governments and social security funds are now recognised as revenue or expenditure, rather than financial transactions.
- Inclusion of construction costs for the high-speed rail line from Tours to Bordeaux in the central government deficit and Maastricht debt: this operation was officially sold to a private concession holder by SNCF Réseau in 2011. However, most of the costs were covered by general government in practice, either directly in the form of subsidies or indirectly in the form of loan guarantees, so all of the expenditure relating to the high-speed rail line has now been allocated to central government.
- **The reclassification of SFEF as a general government entity**. SFEF (Société de financement de l’économie française), founded in 2008, had previously been classified as a financial corporation. This reclassification increased France’s Maastricht debt in the years from 2008 to 2013.
- **Revisions of source data**. Such revisions improved the general government balance: primarily as a result of downward revisions of investment expenditure by hospitals resulting from mergers. In contrast, revisions of source data increased debt by €1.4bn in 2016.
- Furthermore, **the reclassification of the television licence fee** as a tax did not affect the general government balance, but it did simultaneously increase expenditure and the level of taxes

and contributions by some €2bn to €3bn each year, *thereby increasing the aggregate rate of taxes and contributions by more than 0.1 percentage points in the years from 2013 to 2016*.

(in € bn)	2008	2009	2010	2011	2012	2013	2014	2015	2016
Revisions of the general government balance	**-1.5**	**-0.1**	**-1.6**	**-1.1**	**-3.6**	**-1.1**	**0.4**	**-1.0**	**-0.1**
Of which recalculations following rebasing	**-1.4**	**0.0**	**-1.9**	**-1.1**	**-3.6**	**-1.1**	**-0.5**	**-3.2**	**-1.6**
Of which spreading sales of mobile phone licenses over the license period	0.1	0.1	-0.7	-0.8	-2.3	0.3	0.3	0.3	-0.3
Of which soft loans to AFD	0.0	0.0	0.0	0.0	-0.1	-0.1	-0.2	-1.1	0.2
Of which uncollectible taxes	-0.8	0.5	-0.7	0.6	-1.0	0.8	0.4	-1.2	-0.2
Of which debt write-offs	-0.5	-0.4	-0.4	0.1	-0.3	-0.6	-0.7	-0.8	-0.7
Of which Tours-Bordeaux rail line	0.0	0.0	0.0	-1.0	0.1	-1.6	-0.5	-0.8	-0.6
Of which revisions of source data	-0.1	-0.1	0.3	0.0	0.0	0.0	1.0	2.2	1.5
Revisions of Maastricht debt	**13.0**	**77.2**	**69.4**	**54.2**	**24.2**	**25.3**	**2.4**	**3.5**	**4.9**
Of which Tours-Bordeaux rail line	0.0	0.0	0.0	0.9	0.6	2.1	2.4	3.0	3.4
Of which reclassification of SFEF	13.0	77.3	69.4	53.5	23.7	23.4	0.0	0.0	0.0
Of which revisions of source data	0.0	0.0	0.0	-0.1	-0.1	-0.1	0.1	0.5	1.4

Rebasing led to increases in levels that affect forecasts. This means that it has a direct impact on the estimates for the following years. For example, the ***reclassification of the television license fee as a tax*** increased the level of taxes and contributions by €3.3bn in 2017 compared to the relevant item in the 2017 Draft Budget, marking an increase in the tax and contribution rate of approximately 0.15 points. Similarly, ***revisions of Maastricht debt at the end of 2016***, which rose by €4.6bn primarily as a result of the inclusion of the cost of the Tours-Bordeaux high-speed rail line, automatically increased the debt level at the end of 2017 by a similar amount.

For more details about the revisions, see the annex to "Information Rapides No. 79" published by Insee on 26 March 2018. The revisions will be discussed in greater detail when the Insee publishes the National Accounts on 30 May 2018.

3.3. STRUCTURAL BALANCE

In 2017, the general government deficit shrank by 0.8 percentage points of GDP to 2.6%, compared to 3.4% in 2016. The improvement stems from structural adjustment equivalent to 0.5 percentage points of GDP, primarily produced by an improvement of 0.6 percentage points of GDP in the elasticity of taxes and contributions, estimated at 1.5 in 2017. The expenditure effort made a slightly negative contribution of 0.1 percentage points of GDP, stemming from 2.2% growth of public expenditure (excluding one-off expenditures, such as the impact of the reimbursement of the disputed 3% tax on dividends) in nominal terms, compared to estimated potential nominal growth of 2.0%. This effort has been cancelled out by the contribution of the correction for accrual-based measurement of tax credit refunds and appropriations relating to the Competitiveness and Employment Tax Credit, where only the claims on the government add to the deficit[2]. In 2017, the faster growth of payments related to the Competitive and Employment Tax Credit, compared to the virtual stability of taxpayers' claims on the government, contributed the equivalent of 0.1 percentage points of GDP to structural adjustment. Other components, such as revenue efforts and non-tax revenue, made a slightly negative cumulative contribution of 0.1 percentage points of GDP to structural adjustment. The headline deficit was 0.3 percentage points of GDP smaller in 2017 than the figure forecast in the 2018-2022 Public Finance Planning Act. The deficit went from 2.9% of GDP to 2.6%. An improvement in the structural balance contributed 0.2 points to reducing the deficit, which is now equivalent to 2.0% of potential GDP, compared to 2.2% in the Public Finance Planning Act, and an improvement in the cyclical balance contributed another 0.1 points, with a deficit equivalent to 0.5% of GDP, down from 0.6%. There was no change in one-offs in the 2017 outturn compared to the Public Finance Planning Act.

The general government balance should improve by 0.3 percentage points of GDP in 2018, compared to 2017, with a deficit equivalent to 2.3% of GDP, as a result of a 0.4-point contribution from cyclical factors and a 0.1-point contribution from structural adjustment. This improvement should be partially offset by a negative contribution of 0.2 points from one-offs, such as the end of the exceptional corporate income tax payment for large corporations that offset the cost of reimbursing the disputed 3% tax on dividends in 2017. Economic growth of 2.0% in real terms, compared to potential growth of 1.25%, is expected to improve the cyclical balance. Structural adjustment of 0.1 percentage points of potential GDP is expected to result entirely from structural efforts. Expenditure growth, excluding one-offs, is expected to slow between 2017 and 2018, from 2.2% to 1.7% in nominal terms. With potential growth expected at 2.4% in nominal terms, the expenditure effort should be equivalent to 0.3 percentage points of GDP. Discretionary revenue measures, excluding one-offs such as the exceptional corporate income tax payment for large corporations, are expected to limit structural adjustment of expenditure to 0.3 percentage points of GDP. The non-discretionary component is expected to be neutral overall in terms of structural adjustment. The structural balance in 2018 is expected to be 0.3 percentage points of potential GDP greater than the adjustment path set out in the Public Finance Planning Act.

[2] The recording lag for revenue at a given aggregate tax and social security contribution rate between budgetary accounts and the national accounts has increased structural adjustment during the deployment of the CICE tax credit (see Methodological Appendix 9.2 on the structural deficit and the "correction for accrual-based measurement of tax credits" component). The difference stems from the lag between the claims on the government acquired by taxpayers and the recording of the relevant appropriations and refunds.

The general government balance is expected to decrease by 0.1 points in 2019 to show a deficit of 2.4% of GDP, as the Competitiveness and Employment Tax Credit is replaced by cuts in social security contribution rates.

The cyclical balance is expected to improve by 0.4 points, as actual growth outstrips potential growth. This improvement and the structural adjustment of 0.3 points are expected to be more than offset by one-off effects pulling the balance down by 0.7 points, primarily as a result of the replacement of the Competitiveness and Employment Tax Credit. Absent the impact of this replacement, the general government deficit would be equivalent to 1.5% of GDP in 2019. Structural adjustment will be achieved by means of an expenditure effort equivalent to 0.3 percentage points of GDP, with growth of public expenditure, excluding one-offs and tax credits, standing at 1.8%, compared to potential growth of 2.5% in nominal terms. Other effects are expected to have a neutral impact on structural effort in aggregate: discretionary revenue measures, not including one-offs, will make a negative contribution of 0.1 percentage points of GDP, which will be offset by a positive contribution equivalent to 0.1 percentage points of potential GDP from the adjustment of tax credits. The non-discretionary component is expected to be neutral in terms of structural adjustment.

In the years from 2020 to 2022, the structural adjustment path should be similar to the one set out in the 2018-2022 Public Finance Planning Act. The headline balance will improve by 2.6 percentage points of GDP between 2019 and 2022, including 0.6 points stemming from the improvement in the cyclical balance, 1.1 points from the improvement in the structural balance and 0.9 points from the elimination of the double cost of replacing the Competitiveness and Employment Tax Credit in 2019. Therefore, the structural balance should show a deficit equivalent to 0.6% of potential GDP in 2022, marking an improvement of 0.3 points compared to the figure given in the 2018-2022 Public Finance Planning Act. The real economic growth rate over this period should be steady at 1.7% and the potential growth rate should pick up slightly in 2021 to stand at 1.35% in 2022. Average expenditure growth in real terms should stand at ¼% in the years from 2019 to 2022, representing an average expenditure effort of 0.5 percentage points of GDP. This expenditure effort should make it possible to continue cutting taxes, with a reduction of the corporate income tax rate to 25% by 2022, which will limit the improvement from structural adjustment.

TABLE 3: STRUCTURAL BALANCE ADJUSTMENT PATH AND BREAKDOWN OF STRUCTURAL ADJUSTMENT

(% of GDP)	2017	2018	2019	2020	2021	2022
General government balance (1)	**-2.6**	**-2.3**	**-2.4**	**-0.9**	**-0.3**	**0.3**
Nominal adjustment	0.8	0.3	-0.1	1.4	0.6	0.6
Cyclical balance (2)	**-0.5**	**-0.1**	**0.2**	**0.5**	**0.7**	**0.9**
One-offs (as a % of potential GDP) (3)	**-0.1**	**-0.3**	**-1.0**	**0.0**	**0.0**	**0.0**
Structural balance (as a % of potential GDP) (1)-(2)-(3)	**-2.0**	**-1.9**	**-1.6**	**-1.4**	**-1.0**	**-0.6**
Structural adjustment	0.5	0.1	0.3	0.3	0.4	0.4
Structural effort	0.0	0.1	0.3	0.4	0.5	0.5
Discretionary revenue measures	*0.0*	*-0.3*	*-0.1*	*-0.5*	*0.1*	*0.1*
Expenditure effort	*-0.1*	*0.3*	*0.3*	*0.5*	*0.5*	*0.6*

Correction for accrual-based measurement of tax credits	*0.1*	*0.0*	*0.1*	*0.4*	*-0.1*	*-0.2*
Non-discretionary component	0.5	0.0	0.0	-0.1	-0.1	-0.1

BOX 4 - ONE-OFFS TAKEN INTO ACCOUNT WHEN EVALUATING FRANCE'S STRUCTURAL BALANCE

France introduced structural balance-based fiscal governance for the implementation of the Treaty on Stability, Coordination and Governance (TSCG). The structural balance corresponds to the general government balance adjusted for direct cyclical effects and for one-offs. This type of governance prevents the pro-cyclical effects produced by managing public finances based on the headline balance.

In response to a request from the High Council on Public Finance, the report appended to Public Finance Planning Acts since the 2014-2019 Act sets out the government's rules on one-offs and proposes a set of criteria to define one-offs.

On the revenue side, the timing for recognition of losses stemming from exceptional tax disputes in the national accounts cannot be foreseen because it depends on the timing and outcome of the proceedings and the courts' final rulings[3]. These losses have been classified as one-offs. The on-going disputes involve refunds to foreign UCITS, refunds relating to the Ruyter[4], Stéria[5], SERNAM[6] disputes and the disputed 3% tax on dividends (which has been recognised as an expense rather than a reduction in revenue in Insee's provisional 2017 accounts, published in March 2018). The exceptional corporate income tax payment for large corporations in 2017 has also been included in one-offs, since it was not foreseen when the Public Finance Planning Act was drafted. It relates to a dispute and it has a significant impact on the balance in one year, but no impact in the future.

On the expenditure side, interest payments owed on dispute settlements have also been recorded as one-offs. In addition, the change in the timing of recognition of sales of mobile phone licenses is also classified as a one-off, as was the case for recognition of the EU Amending Budget No. 6 following a major change in recognition rules.

[3] Expenditure and revenue are recorded on an accrual basis in the system of national accounts, except in special cases, in compliance with the European System of Accounts of 2010. This means they are recorded, "when economic value is created, transformed or extinguished, or when claims and obligations arise, are transformed or are cancelled" §1.101. Consequently, losses stemming from tax disputes will be recorded in the year when the courts make their final rulings, which correspond to liabilities. On the other hand, the losses will be recorded in budgetary accounting on the basis of cash receipts or disbursements, which may occur before or after the courts hand down their final rulings.
[4] Dispute concerning French social security contributions under European Union law.
[5] Dispute concerning dividends received from European subsidiaries.
[6] On 7 March 2018, the CJEU issued its final ruling requiring SERNAM (now known as SNCF Mobilités) to repay €0.6bn to central government for grants paid to SERNAM in 2001. The court's decision is final and the quantity is known. Consequently, central government non-tax revenue of €0.6bn has been restated and recognised as a one-off in 2018.

TABLE 4 – ONE-OFFS EXCLUDED FROM THE STRUCTURAL BALANCE UNDER THE NATIONAL SYSTEM OF ACCOUNTS

(level, in € bn)	2017	2018	2019	2020	2021	2022
Revenue (1)	**3.5**	**-0.2**	**-22.0**	**-0.8**	**-0.8**	**-0.8**
UCITS dispute	-0.6	-0.6	-0.6	-0.6	-0.6	-0.6
De Ruyter dispute	-0.1	-0.1	-0.2	-0.2	-0.2	-0.2
Stéria dispute	-0.4	-0.3	-0.1			
Exceptional corporate income tax payment for large corporations to offset the disputed 3% tax on dividends	4.9	0.4				
CVAE dispute	-0.3	-0.3				
SERNAM dispute		0.6				
Double cost of replacing the Competitiveness and Employment Tax Credit (*)			-20.1			
Double cost of replacing the Energy Transition Tax Credit (*)			-1.1			
Expenditure (2)	**5.4**	**6.6**	**1.3**	**0.1**	**0.1**	**0.1**
Disputed 3% tax on dividends	4.7	5.0				
Change in the timing of recognition of mobile phone license sales		1.0	1.1			
Interest on dispute settlements	0.7	0.6	0.1	0.1	0.1	0.1
Total effect on balance (1) – (2)	**-1.9**	**-6.8**	**-23.3**	**-0.9**	**-0.9**	**-0.9**

NB: the figures given in this table do not predict the outcome of the disputes; they merely reflect a conservative approach to multiyear public finance projections. Therefore, the figures shown are subject to change as a result of the courts' final rulings.
(*) These one-offs correspond to expenditure as defined in ESA 2010, but they are recognised as reduced revenue in the structural breakdown of the deficit. The correction for the accrual-based measurement of tax credits ensures consistency with the ESA 2010 rules. See Methodological Annex.

3.4 GENERAL GOVERNMENT BALANCE BY SUB-SECTORS

After achieving a deficit equivalent to 2.6% of GDP in 2017, in keeping with its European commitments, France will continue its efforts to contain public expenditure in the years from 2018 to 2022. This effort will be shared by all general government sub-sectors: State government, which will contain its expenditure under the benchmark and carry out the reforms included in the *Public Action 2022* programme; local governments, which will make major efforts to moderate their operating expenditure under the terms of the Public Finance Planning Act (see Box – Implementation of Local Government Contracts). Social security funds will also take part in efforts to contain expenditure, with a moderate national healthcare expenditure growth target. Fiscal consolidation efforts will help reduce the public expenditure ratio by more than 3 percentage points of GDP between 2017 and 2022.

The aggregate tax and social security contribution rate will decrease by one point between 2017 and 2022 to stand at 44.3% of GDP in 2022. These targets, combined with the lower expenditure ratio, should make it possible to post a slight headline surplus by 2022. The aggregate tax and social security contribution rate will fall sharply for businesses and households in 2018. It will continue to fall in 2019 with the replacement of the Competitiveness and Employment Tax Credit with a permanent cut in contributions targeting low wage jobs in particular. Continuing cuts in the corporate income tax rate will bring it down to 25% by 2022, which is consistent with the average rate in European Union countries. The second and third phases of abolishing the residence tax for 80% of households will also lower the aggregate tax and social security contribution rate. These cuts will be partially offset by higher carbon taxes, along with continuing convergence of tax rates on diesel oil and petrol to boost ecological conversion.

TABLE 5: GENERAL GOVERNMENT LENDING CAPACITY (+) / BORROWING REQUIREMENT (-)[7]

% of GDP	2017	2018	2019	2020	2021	2022
General government balance, Maastricht definition	**-2.6**	**-2.3**	**-2.4**	**-0.9**	**-0.3**	**0.3**
Of which: primary balance	*-0.8*	*-0.6*	*-0.6*	*0.9*	*1.6*	*2.3*
State government	-2.8	-3.0	-3.2	-1.9	-1.6	-1.2
Other central government bodies	0.0	-0.1	-0.1	-0.1	-0.1	0.0
Local government	0.0	0.1	0.1	0.3	0.5	0.7
Social security funds	0.2	0.7	0.8	0.8	0.8	0.8

[7] The sub-sectors' respective contributions to the efforts are determined by convention starting in 2019.

3.5 PUBLIC EXPENDITURE

3.5.1 General government expenditure

Nominal growth of general government expenditure, excluding tax credits, stood at 2.5% in 2017. This growth stems mainly from increases in appropriations to line ministries, higher wage bills following a civil service pay raise, bonuses and measures under the agreement on professional development, careers and compensation (PPCR), growth of expenditure under the National Healthcare Expenditure Growth Target, which stood at 2.2% in 2017, compared to 1.8% in 2016, and the increase in local governments' investment expenditure in the run-up to local elections. In addition to these factors, the reimbursement of approximately half of the 3% tax on dividends in 2017 was classified by Insee as expenditure, thereby adding 0.4 percentage points to the expenditure growth rate.

The growth of nominal general government expenditure, excluding tax credits, should slow substantially to stand at 1.8% in 2018. State and local governments should account for most of the slower growth. Containing wage increases, along with targeted savings measures, focussing in particular on subsidised employment contracts and housing, should keep the growth of State government's expenditure down to 1.7% on a like-for-like basis, and the growth of local governments' expenditure should be limited to 1.4%, despite increased investment expenditure in the run-up to local elections. Social security funds' expenditure growth is expected to slow slightly, on a like-for-like basis, as payroll expenditure growth slows down after civil service pay raises in 2017.

General government expenditure, excluding of tax credits, should fall from 55.1% of GDP in 2017 to 54.4% in 2018. Continuing efforts by all sub-sectors to contain expenditure in 2019 should reduce this share to 53.5% of GDP. In the years from 2019 to 2022, average real growth of general government expenditure should stand at ¼%, reducing the expenditure ratio by more than 3 percentage points of GDP to 51.1% in 2022.

TABLE 6: CHANGE IN GENERAL GOVERNMENT EXPENDITURE BY SUB-SECTOR

Nominal terms, excluding tax credits transfers*	2017	2018	2019
General government	2.5 %	1.8 %	1.4 %
State government	3.7 %**	1.7 %	0.4 %
Other central government bodies (ODAC)	- 0.4 %	2.4 %**	1.7 %
Local government (including investment and Société du Grand Paris)	2.5 %	1.4 %	2.2 %
Social security funds	2.1 %**	2.0 %**	1.6 %

**Nominal expenditure, excluding tax credits and transfers between general government sub-sectors, , unless otherwise specified.*
*** Restatements:*
In 2017, state expenditure should increase by 3.3% basis and social security funds' expenditure by 2.4%: the transfer of funding for vocational rehabilitation centres (ESAT) from state to social security funds increases the latter's expenditure and reduces that of central government by €1.5bn.
In 2018, other central government bodies' expenditure should decrease by 1.4%, and social security funds' expenditure should increase by 2.4%. The abolition of the Solidarity Fund increases social security expenditure by €2.5bn and decreases the expenditure of other central government bodies by the same amount.

3.5.2 State government expenditure

Right from the start of the current legislature, the government has demonstrated its determination to consolidate France's fiscal situation by containing State government expenditure.

In 2017, following an audit by the French government audit office (Cour des comptes), the government introduced tough measures in the third quarter to meet its European commitments. It cancelled unprecedented amounts of appropriations, cutting more than €4bn in the current year, and took other measures to contain expenditure, such as a first step towards a major reduction in the volume of subsidised employment contracts, which was maintained in the 2018 budget. Overall, the government's expenditure efforts affecting the current year came to more than €5bn, whereas the auditors estimated the government's capacity for regulating expenditure at €2.5bn.

In 2018, the government has opted for transparency. For example, the growth of expenditure under the State government discretionary expenditure benchmark (see below) by €5.1bn under the 2018 Initial Budget Act compared to the 2017 Initial Budget Act stems mainly from overcoming the budget shortfalls revealed by the audit. In addition, risk provisions were increased: the provision for external defence operations was increased and a new provision was set aside for the agricultural sector, which is periodically exposed to risks during the budget year. This improves the probity of the Budget Act, which makes managers more accountable and ensures compliance with the government's expenditure target.

Containment of State government expenditure in 2018 will be achieved while ensuring funding for government priorities and continued implementation of the employment and housing reforms that started in the third quarter of 2017.

- State government resources for sovereign functions will be increased, with an additional €1.8bn in appropriations for the armed forces and job creation in the security and justice sectors.

- Households' purchasing power and incentives to return to the labour market will be boosted by increasing some minimum benefits.
- Ecological transition will receive more support as other economic players participate in the most effective actions.
- The fight against unemployment will once again be at the heart of the government's action, but in a renewed format. Greater emphasis will be put on improving human capital, with the implementation of the Investment in Skills Plan rather than statistical treatment of unemployment, which traditionally relies on subsidised employment contracts.
- Housing policy will be adjusted to reinforce the resources used for urban renewal and the rationalisation of housing benefits will continue.
- Government investment as a whole will be increased and focused on the main challenges of tomorrow with the deployment of the €57bn *Great Investment Plan.*

The 2018 budget is the first annual budget in the five-year budgetary plan set out in the 2018-2022 Public Finance Planning Act. The Act upholds the principle of cutting expenditure under State government control in real terms, with a target of a 1% cut in real terms by 2020. For this purpose, the Act is based on a system with two new targets : one target for discretionary State government expenditure and another target for aggregate State government expenditure (ODETE).

The previous growth target for expenditure other than debt servicing and pensions, and the "zero real growth" rule were helpful for containing State government expenditure. However, such targets are more effective when they address expenditure that can be controlled. Therefore, the two previous targets have been replaced by:

- The **target for discretionary State government expenditure**, which corresponds to the State government expenditure where the government has the greatest capacity for taking action. For this purpose, some accounts for specific allocations and specific budgets have been included in this category, whereas levies on revenue have been excluded. These changes implement some of the recommendations made by the French government audit office. In aggregate, such expenditure accounts for €257.9bn in the 2018 Budget Act.
- The **aggregate State government expenditure target (ODETE)** is a broad-based aggregate that approximates the central government sector.

Under the target for discretionary State government expenditure, nominal expenditure will rise by €5.1bn in 2018, followed by €1.6bn in 2019 and €1.0bn in 2020, which means much slower growth for expenditure covered by the target. The increase in appropriations under the target for expenditure under the target for discretionary State government expenditure over three years stands at €7.7bn, compared to €10.4bn in increased appropriations for the same expenditure under the 2017 Initial Budget Act, compared to the 2016 Initial Budget Act.

In the years from 2020 to 2022, real growth under the benchmark for expenditure under the target for discretionary State government expenditure will be negative at 1% per year. This will be possible because of reforms set out in the *Public Action 2022* process and detailed in the 2018 ministerial and interministerial transformation plans.

BOX 5 – CENTRAL GOVERNMENT BORROWING COST AND INTEREST RATE ASSUMPTIONS

In 2017, France continued to enjoy favourable borrowing terms as a result of the European Central Bank's accommodative monetary policy and steady investor confidence. Yields at issue for short-term securities (BTFs) were negative at -0.62% on average and yields on securities maturing at more than one year averaged 0.65%.

The interest rate path underlying the debt servicing cost forecast assumes that ECB will tighten European monetary policy, in keeping with a macroeconomic scenario of stronger growth and higher inflation.

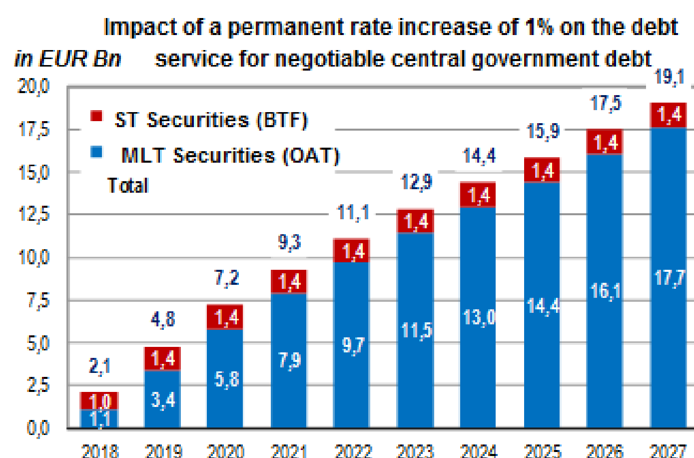
End of year levels (forecasts)	2018	2019	2020	2021
Short-term yields (3-month BTFs)	-0.10 %	0.70 %	1.50 %	2.10 %
Long-term yields (10-year OATs)	1.60 %	2.35 %	3.10 %	3.60 %

Assuming the ECB starts to raise its key rates in 2019, short-term yields should start rising gradually again in 2018. The yield on 3-month BTFs should stand at a negative 0.10% at the end of 2018. It should then increase by about 80 basis points per year.

The 10-year yield (Tec10) stood at 0.71% on 29 March 2018. Stronger macroeconomic conditions, along with the end of the moderating impact of the ECB's asset purchase programme are likely to cause a gradual rise in medium- and long-term yields. The assumption is that yields will rise by 75 basis points each year. The Tec10 index will stand at 1.60% at the end of 2018 and then 2.35% at the end of 2019.

An extended rebound to higher yields than those presented above would gradually increase the cost of debt servicing to a higher level than forecast in this Stability Programme. The impact of the shock of a 100-basis point jump in yields on the cost of debt servicing in the national accounts, compared to the baseline scenario, is shown in the chart below for the entire yield curve and for the entire forecast period. The impact would be felt gradually because the debt would be refinanced in stages. The shock would be equivalent to a negative annual adjustment of 0.1 percentage points of GDP starting in 2018.

CHART 1: IMPACT OF AN INTEREST RATE SHOCK ON THE COST OF DEBT SERVICING



Debt servicing costs are also sensitive to inflation because of the substantial share of inflation-linked bonds, which account for approximately 13% of the outstanding negotiable central government debt securities with maturities of one year or more. The shock of a positive or negative 0.1% deviation in the consumer price index (excluding tobacco) in France and in the euro area would lead to a variation of approximately €0.2bn in debt servicing costs.

Beyond these direct effects, we should point out that higher yields stemming from faster growth and/or higher inflation would, all else being equal, lead to an increase in government revenue that would offset the increased cost of debt servicing. As long as structural efforts continue for the rest of general government expenditure, the ultimate effect of this type of cyclical shock on the general government balance would be positive.

3.5.3 Expenditure of other central government bodies

Other central government bodies, which consist mostly of central agencies[8], successfully contained their expenditure in 2017, posting a reduction of 0.8% compared to 2016. This reduction stems in particularly from exceptionally high expenditure by the guarantee fund for victims of terrorism and other criminal acts (FGTI) in 2016. The Fund provides financial compensation for the damages suffered by victims of terrorism and of other offences under ordinary law..

Containment of these bodies' expenditure starts with closer monitoring of their resources, by means of periodic lowering of the caps on earmarked taxes, with a reduction of €0.3bn in 2017, and by banning these bodies from incurring debt with maturities of more than 12 months in the form of bank borrowing or debt securities, in accordance with the provisions of the 2011-2014 Public Finance Planning Act. Central agencies' expenditure for the Invest for the Future Programme (PIA) is monitored at the central level by the General Secretariat for Investment, which reports to the Prime Minister and also monitors all of the actions under the *Great Investment Plan*.

In 2018, other central government bodies' expenditure will grow by 2.4% on a like-for-like basis, compared to a contraction of 0.8% in 2017 (including transfers). The growth will stem in part from major infrastructure projects, such as the start of work on the Charles-de-Gaulle Airport Express rail link, the resumption of work on the Lyon-Turin Euralpin Tunnel (TELT) and the Canal Seine-Nord Europe (SCSNE) projects, and the implementation of the 3rd phase of the Invest for the Future Programme (PIA 3), which focuses on education, research and innovation. Final spending by other central government bodies on the Invest for the Future Programme as a whole should come to €2.2bn in 2018. Other central government bodies' expenditure will decline, as the expenditure of the Solidarity Fund, including the Specific Solidarity Allowance, will be covered by *Pôle Emploi* starting from 2018, France's public employment service agency, which is not part of other central government bodies.

[8] The salient features of central government agencies are that they provide public services, are mostly financed by the central government and are under its direct control. Central government agencies and central agencies are not exactly the same: the former are defined using a budget-based approach, while the latter are listed by Insee each year and defined by a national accounts-based definition.

The growth of these bodies' expenditure will slow down slightly to stand at 2.0% in 2019 (including transfers), as infrastructure expenditure stabilises. Final spending by other central government bodies on the Invest for the Future Programme as a whole should come to €2.6bn in 2019.

3.5.4 Social security funds' expenditure

In 2017, social security funds' expenditure grew by 2.4%, following a growth of 1.3% in 2016. On a like-for-like basis, after stripping out the effects of moving housing benefits into the central government budget in 2016 and the transfer of funding for vocational rehabilitation centres for disabled adults (ESAT) from central government to social security funds, spending growth slowed slightly from 2.2% to 2.1%. Expenditure on pensions posted slow growth of 1.7% as successive pension reforms came into full effect. Furthermore, stronger inflation had little impact on old age pensions and family benefits in 2017 as a result of the reform of methods for recalculating index-linked benefits. Moreover, the national healthcare expenditure growth target (Ondam) should be met for the eighth year in a row, with expenditure of €190.7bn.

In 2018, expenditure is expected to grow by 2.4%, as it did in 2017. However, on a like-for-like basis, social security funds' expenditure should grow by 2.0%, compared to 2.1% in 2017. The elimination of the Solidarity Fund, classified with other central government bodies, means that its expenditure on benefits will be transferred to the public employment service agency (*Pôle Emploi*) in 2018. This will increase social security funds' expenditure by some €2.5bn. The main factor contributing to the change in dynamics should be old age pensions, with benefits increasing by 2.5%, compared to 1.7%, as a result of the dual effects of prices and volume. Higher inflation in 2017 has a greater impact in 2018, since basic retirement benefits were recalculated in October 2017. Furthermore, the number of new retirees each year is back to its usual level, now that pension reforms have produced their full effects. Family benefits should decline slightly, with a 0.3% contraction, following 1.1% growth in 2017. This decline will stem from low birth rates and the impact of measures in the draft 2018 social security budget. Moreover, the delay in implementing the agreement on professional development, careers and compensation (PPCR) and fading effects of the civil service pay raises in 2016 and 2017 mean that the growth of the social security funds' wage bill should slow, contributing to slightly slower growth of social security funds' expenditure. The year 2018 also marks the start of the Investment in Skills Plan (PIC), which involves expenditure of approximately €0.5bn.

In 2019, social security funds' expenditure should increase by 1.6%. The slower growth should stem from greater efforts to contain social security expenditure, including the effects of the new measures under the Agirc-Arrco agreement on supplementary pensions of October 2015 and lower expenditure on unemployment insurance benefits.

3.5.5 Local government expenditure

Local government expenditure growth should slow sharply in 2018, following strong growth in 2017. The slower growth should stem in part from weaker growth of operating expenditure, with slower increases in wage bills, and from the implementation of the Financial Pact with central government. Investment expenditure should continue to show strong growth in the run-up to local elections.

After rising by 2.5% in 2017, local government expenditure growth (including transfers) is expected to slow to 1.5% in 2018.

This slower growth will be entirely attributable to slower growth of operating expenditure. Under the contracts required by the 2018-2022 Public Finance Planning Act (see box – Implementation of contracts with local governments), local governments will renew efforts to contain operating expenditure by holding down payrolls and intermediate consumption. Furthermore, with the civil service pay raise fully in force, the postponement until 2019 of the measures under the agreement on professional development, careers and compensation (PPCR) and the reduction in the number of subsidised employment contracts, local government wage bills should grow more slowly. All in all, the local government operating expenditure growth target of 1.2% set out in the Public Finance Planning Act should be met.

The usual pattern of local government expenditure over the election cycle indicates that investment expenditure should increase by 5.7%, which matches the growth seen in 2017.

Local government expenditure growth will continue to be contained in 2019, under the terms of the Financial Pact with central government.

Local government expenditure is expected to grow by 2.1% in 2019, following growth of 1.5% in 2018.

Wage bill growth will pick up with the reintroduction of measures under the agreement on professional development, careers and compensation (PPCR), and the reduction in the numbers of subsidised employment contracts will continue at a similar pace to that seen in 2018. However, local governments should continue their efforts on holding down payrolls and intermediate consumption, which will enable them to meet the 1.2% operating expenditure growth target set out in the Public Finance Planning Act.

Local government investment expenditure growth should be slightly slower in the last year of the election cycle.

BOX 6 – IMPLEMENTATION OF CONTRACTS WITH LOCAL GOVERNMENTS

In accordance with Article 29 of the 2018-2022 Public Finance Planning Act, contracts between central government and the local governments concerned should be signed by 30 June 2018.

For this purpose, the central administrations concerned have compiled and verified the **list of 322 local governments to be covered by the contracts, which account for 2/3 of operating expenditure**, along with financial data and the modulating factors that could be applied to them. **The practical procedures for implementing the contracts have been set out in detail in a circular sent to the parties concerned**, following a series of regular meetings between central government representatives at the local level, local offices of central government services and representatives of the local governments taking part in the experiment.

Prefects are to provide the central administration with a list of the local governments with which they are considering entering contracts. **This list must be submitted by 30 April 2018**. Prefects will then be in charge of **negotiations with each local government** under their jurisdiction and of coordination at the regional level to ensure that **all of the contracts are consistent with the 1.2% national target for real operating expenditure growth**. Prefects and local governments are free to make their own arrangements for this coordination phase, while central administration staff will monitor progress on the contracts, their content and their consistency with the contract targets set at the national level so that the overall targets set out in the Public Finance Planning Act are met. Local governments that do not choose to enter the contracts will automatically be given targets that may be less favourable under the ranges defined in the Public Finance Planning Act and, if they exceed these targets, they will be subject to clawbacks in the following year.

A monitoring meeting for each contract will be held at least once a year. However, the parties are encouraged to meet more frequently. More specifically, meetings should be held in the weeks following the publication of annual accounts in April to examine local governments' real operating expenditure growth over the previous year.

After the meeting, the Act gives the Prefect the power to initiate a clawback procedure if the annual target has been exceeded. This follows proceedings in which both parties are heard and where the local government may present any relevant information for assessing its compliance with the target. Local offices of central government services may also provide technical support in the most complex cases.

3.6 PUBLIC REVENUE

3.6.1 General government revenue

The aggregate tax and social security contribution rate rose to 45.4% of GDP in 2017, compared to 44.6% in 2016. The increase resulted from renewed economic growth and the exceptional corporate income tax payment for large corporations passed in the Supplementary Budget Act to offset the expenditure relating to the disputed 3% tax on dividends. **In 2018, this rate should fall to 45.0% of GDP as a result of the tax cuts decided by the government. It will continue to fall in 2019 and the aggregate tax and social security contribution rate should reach 44.0% in 2019 as a result of discretionary revenue measures, such as the replacement of the Competitiveness and Employment Tax Credit by social security contribution cuts in 2019 and continued phasing out of the residence tax.** This forecast incorporates all of the measures passed or announced by the government, along with the usual pattern of local taxes over the local election cycle and reimbursements related to ongoing tax disputes.

The aggregate tax and social security contribution rate should fall by 0.3 percentage points of GDP to 45.0% in 2018. Discretionary revenue measures are expected to reduce aggregate taxes and social security contributions by some €10bn, particularly with the impact of the Presidential programme to boost purchasing power, investment and competitiveness. These measures include the first phase of the residence tax rebate over three years, the creation of a property wealth tax, cutting the corporate income tax rate to 25% by 2022 and increasing energy taxes. The end of the exceptional corporate income tax payment for large corporations and the increase in the Competitiveness and Employment Tax Credit in 2017, along with the first payments of the related claims from 2014, are also expected to reduce the aggregate tax and social security contributions rate. These tax cuts should be offset somewhat by spontaneous revenue growth, which should be stronger than GDP growth in 2018 with tax elasticity to GDP growth that is slightly greater than one. Spontaneous revenue growth should once again outstrip GDP growth, with strong corporate earnings in a favourable macroeconomic environment and brisk growth of domestic demand, coming on the heels of very strong general government revenue growth seen in 2016 and, more especially, in 2017, with elasticities of 1.3 and 1.5 respectively.

In 2019, the aggregate tax and social security contribution rate is expected to fall by 1.0 percentage point of GDP, to reach a low of 44.0%[9]. The lower rate will stem primarily from the transitory effects of replacing the Competitiveness and Employment Tax Credit with social security contribution cuts (-0.8 percentage points of GDP). Aggregate tax elasticity should be equal to one.

After that, continued expenditure efforts should finance the consolidation of the cut in the aggregate tax and social security contributions rate, reducing it by a total of 1 percentage point of GDP between 2017 and 2022. The adjustment path is based on spontaneous growth of taxes and contributions coming back into line with nominal GDP growth (tax elasticity equal to one).

[9] In subsequent years, shrinking payments of Competitiveness and Employment Tax Credit claims will contribute to an increase in the aggregate tax and social security contribution rate.

TABLE 7. – TAXES AND SOCIAL SECURITY CONTRIBUTIONS

	2016	2017	2018	2019	2020	2021	2022
Aggregate rate as a percentage of GDP	44.6	45.4	45.0	44.0	44.3	44.3	44.3
Aggregate tax elasticity	1.3	1.5	1.1	1.0	1.0	1.0	1.0

3.6.2 Central government revenue

Taxes and social security contributions assessed by central government grew by 6.4% **in 2017**, compared to 3.5% growth in 2016. This growth is primarily due to particularly strong spontaneous growth of 5.4%, driven by the resurgent growth of revenue from corporate income tax as the economy recovered and the faster growth of VAT revenue driven by household consumption and private sector investment. Discretionary revenue measures and transfers contributed €3.2bn to the growth of taxes and social security contributions assessed by central government, particularly with the exceptional corporate income tax payment for large corporations that offset reimbursement of the disputed 3% tax on dividends.

In 2018, taxes and social security contributions assessed by central government are expected to decline by 0.5 percentage points of GDP as a result of discretionary revenue measures and transfers. The measures under the Presidential tax reduction programme for households and businesses will impact central government. The end of the exceptional corporate income tax payment for large corporations passed in 2017 and the payment of Competitiveness and Employment Tax Credit claims (as the rate was raised from 6% to 7% and the claims from 2014 were paid for the first time at the 6% rate) will also reduce central government revenues. Without discretionary revenue measures, the taxes and social security contributions assessed by central government should spontaneously grow by 4.5%, outstripping the expected economic growth of 3.1%. The favourable macroeconomic environment should have boosted taxable corporate earnings in 2017, thereby sustaining corporate income tax revenue in 2018, while rising consumption and investment should continue to boost VAT revenue.

In 2019, taxes and social security contributions assessed by central government are expected to decline by -0.7 percentage points of GDP, primarily as a result of discretionary revenue measures, since central government will use transfers to offset the impact to the presidential measures. More specifically, central government revenue will incur the double impact of replacing the Competitiveness and Employment Tax Credit with a cut in social security contributions. The revenue cost is €19bn and stems from payments of tax credit claims from previous years, which will continue to reduce central government revenue from corporate income tax, and the cost of offsetting the reduction in social security funds' revenue resulting from the contribution cuts. Absent these reductions, taxes and social security contributions assessed by central government would have posted spontaneous growth that was a bit faster than economic growth, with tax elasticity standing at 1.2. This faster growth would have resulted from strong corporate earnings growth and personal income tax revenue growth, which usually outstrips GDP growth during periods of economic expansion because it is a progressive tax.

3.6.3 Social security funds' revenue

In 2017, social security funds' revenue grew by 3.7%, compared to a growth of 1.6% in 2016. Most of the growth stemmed from social security contributions on income and assets, which benefited from the brighter economic situation. To a lesser extent, offsetting transfers for exemptions also contributed. These transfers now offset exemptions for professional integration workshops and work sites and for home help for vulnerable persons, which had not been offset previously. This new revenue offsets the new expenditure that social security funds now cover, such as the expenditure for vocational rehabilitation centres for disabled adults.

The actual social security contribution growth of 3.5% is consistent with the 3.6% growth of wages and salaries in the private non-farm business sector and with the 3.5% growth announced by the social security funds. Discretionary measures affecting social security contributions cancel each other out: the final stage of the deployment of cuts under the terms of the Responsibility and Solidarity Pact has been offset by successive pension reforms that have increased pension contributions.

Total taxes and contributions assessed by social security funds were virtually stable between 2016 and 2017, rising from 24.0% of GDP to 24.1%.

Revenue growth is expected to pick up substantially **in 2018**. The growth of social security funds' revenue should stand at 3.8%, excluding changes in the scope of central government transfers. This growth stems in part from wage bill growth in the non-farm business sector. Revenue has also been boosted by a change in scope: The Solidarity Fund was eliminated on 1 January 2018 and its expenditure and revenue have been picked up by *Pôle Emploi*, France's public employment service agency. This increases budget transfers to social security funds, along with the revenue allocated to funding the Investment in Skills Plan.

Social security funds' revenue growth will be slower **in 2019** after a growth of 2.2% in 2018. However, some of this slower growth will stem from sharing the burden of efforts between central government and social security funds. The percentages of revenue from taxes and from contributions will be altered at the same time. Replacing the Competitiveness and Employment Tax Credit with cuts in social security contributions leads to a sharp drop in contributions, which is offset by a greater share of earmarked VAT revenue. In 2019, the measure to eliminate employees' contributions to unemployment insurance, which is also to be offset, will continue to produce its effects and also slow the growth of social security contributions.

Taxes and contributions assessed by social security funds should stand at 24.3% of GDP in 2018, compared to 24.1% in 2017. This figure is expected to come back down to 24.1% in 2019.

3.6.4 Local government revenue

In 2017, growth of local government tax revenue stood at 3.5%, following growth of 3.6% in 2016. As was the case in 2016, tax revenue growth was primarily sustained by the registration duties on property sales (DMTO), which posted strong growth with historically high transaction volume in older properties driven by persistently low interest rates. Residence tax revenue was reduced by the take-up of exemptions for low-income pensioners. The growth of revenue from the contribution on business value added (CVAE) was slightly slower because of the new effective tax rates applied to

companies belonging to an integrated tax group, following the 19 May ruling by the Constitutional Council[10].

The decrease in financial transfers from central government passed under the previous government continued, with a €2.6bn cut in the general operating grant to local governments. All in all, local government revenue posted growth of 1.6% in 2017, compared to 0.7% growth in 2016.

In 2018, the growth of aggregate local government taxes should stand at 5.5%, boosted by the VAT transfer to regional governments. The forecast for faster revenue growth also stems from the increase in property assessments passed in the 2018 Budget Act.

Under the terms of the Financial Pact signed by central government and local government, financial assistance to regions, excluding the VAT compensation fund and the share of VAT revenue earmarked for regional government, is not expected to be cut in 2018 and the following years. On the other hand, the general operating grant from the central government to regional governments has been replaced by a share of VAT revenue. In aggregate, local government revenue is expected to increase by 2.2% in 2018.

In 2019, the growth of local government tax revenue should slow to 2.4%, mainly as a result of the residence tax exemption on primary residences.

As is the case in 2018, no cuts in financial assistance from central government are expected in 2019. Local government revenue should grow by 2.3%.

3.7 GENERAL GOVERNMENT DEBT AND STOCK-FLOW ADJUSMENT

In 2017, the debt level notified to the European Commission stood at €2,218.4bn, equivalent to 97.0% of GDP, compared to 96.6% in 2016[11]. After posting large increases in previous years, the debt-to-GDP ratio started to stabilise in 2017. The reduction of the general government deficit from 3.4% of GDP in 2016 to 2.6% in 2017, combined with faster nominal growth, made it possible to reduce the deviation from the debt-stabilising balance from 1.9 percentage points of GDP in 2016 to 0.1 points in 2017 (see Table 8). On the other hand, in contrast to 2016, stock-flow adjustments increased the debt ratio by 0.3 percentage points of GDP.

The debt ratio will start dropping in 2018, falling to 96.4% of GDP. This reduction will stem from the smaller deficit and economic growth, which will produce a deficit that is smaller than the debt-stabilising balance. With nominal GDP growth of 3.1%, the debt-stabilising deficit will be 2.9% of GDP and the actual deficit should stand at 2.3% of GDP. Expected stock-flow adjustments in 2018 should cause the debt ratio to rise slightly and will be the same as the forecast in the 2018-2022 Public Finance Planning Act, with an increase of 0.1 percentage points of GDP. The net effect of

[10] The Constitutional Council ruled that the procedures for calculating the effective tax rates applied to companies belonging to an integrated tax group were unconstitutional. This ruling meant that central government had to reimburse the plaintiffs and that the advance payments from businesses were lower in 2017.

[11] Figure submitted to Parliament for the purposes of Article 32 of the 2014-2019 Public Finance Planning Act, which was not abrogated by the 2018-2022 Public Finance Planning Act of 22 January 2018.

issuance premiums and discounts and spreading previous premiums[12] over several accounting periods should have an adverse effect on the debt ratio from now on, increasing it by 0.2 percentage points of GDP. However, this increase should be mitigated slightly by the decrease in the national motorway fund's debt, equivalent to 0.1 percentage points of GDP.

The debt ratio should continue to decline in 2019 to reach 96.2% of GDP. This is a decrease of 0.2 points, which is slightly smaller than the decrease expected in 2018. The general government balance and GDP growth are not expected to change much compared to 2018. The slower growth of debt should stem primarily from larger stock-flow adjustments. Such adjustment are expected to stand at 0.3 percentage points of GDP in 2019, primarily as a result of issuance premiums and discounts, net the spreading of previous premiums over several accounting periods, which should continue to increase debt by 0.3 points.

In the years from 2020 to 2022, the general government debt ratio should continue to shrink, falling from 96.2% of GDP in 2019 to 89.2% in 2022, for a decrease equivalent to 7.0% of GDP. The major share of the decrease (8.3 points) should stem from a general government deficit that is smaller than the debt-stabilising balance. The deficit should shrink rapidly after 2020, from 2.4% of GDP in 2019 to post a surplus of 0.3% of GDP in 2022. The debt-stabilising balance over this period should be a deficit equivalent to approximately 3% of GDP. Stock-flow adjustment will hinder the decline in the debt ratio, primarily as a result of the replacement of the Competitiveness and Employment Tax Credit with cuts to social security contributions and the spreading of previous premiums over several accounting periods. Despite the end of the Competitiveness and Employment Tax Credit in 2019, the stock of outstanding claims will increase Maastricht debt, but without affecting the general government deficit. Combined with other stock-flow adjustments, these effects should increase the debt ratio by 1.3 percentage points of GDP between 2019 and 2022.

TABLE 8. – GENERAL GOVERNMENT DEBT DEVELOPMENTS

(percentage points of GDP)	2017	2018	2019	2020	2021	2022
Debt-to-GDP ratio according to the Maastricht definition	**97.0**	**96.4**	**96.2**	**94.7**	**92.3**	**89.2**
Debt-to-GDP ratio excluding financial assistance for euro area Member States	94.1	93.7	93.5	92.1	89.8	86.8
Change in debt ratio	**0.4**	**-0.5**	**-0.2**	**-1.5**	**-2.4**	**-3.1**
Deviation from debt-stabilising balance	0.1	-0.7	-0.6	-2.1	-2.9	-3.4
Debt-stabilising balance (excluding stock-flow adjustment)	*-2.5*	*-2.9*	*-2.9*	*-3.0*	*-3.2*	*-3.1*
Headline balance	*-2.6*	*-2.3*	*-2.4*	*-0.9*	*-0.3*	*0.3*
Stock-flow adjustment	0.3	0.1	0.3	0.6	0.5	0.2
Nominal GDP growth (%)	*2.6*	*3.1*	*3.1*	*3.2*	*3.5*	*3.5*

[12] Maastricht debt is recorded at its nominal redemption value at maturity. Issues of securities with coupon yields that are higher than market yields result in payment of a premium to the issuer. These premiums are recorded as negative stock-flow adjustments. Spreading them over the life of the security is a positive stock-flow adjustment.

4. Implementation of the Stability and Growth Pact

4.1 EXCESSIVE DEFICIT PROCEDURE

As part of the Excessive Deficit Procedure started in April 2009, on 10 March 2015, the European Union Council made a recommendation to France to end its excessive deficit by 2017. The recommendation was based on a headline deficit path of 4.0% of GDP in 2015, followed by 3.4% in 2016 and 2.8% in 2017.

The 2017 deficit notified by Insee on 30 March 2018 stood at 2.6% of GDP, which is smaller than the deficit prescribed in the 2015 recommendation. This is the first time that the general government deficit has been under the 3% threshold since 2007. Furthermore, this return to under 3% is lasting. Despite the cost of the disputed 3% tax on dividends and the double cost of replacing the Competitiveness and Employment Tax Credit, the deficit should be 2.3% of GDP in 2018 and then 2.4% in 2019.

4.2 IMPLEMENTATION OF THE PREVENTIVE ARM IN 2018

4.2.1 Convergence towards the medium-term objective

The 2018-2022 Public Finance Planning Act set a medium-term objective (MTO) of a structural deficit equivalent to 0.4% of potential GDP and set out the adjustment path for achieving this objective. This structural adjustment path continues to guide this stability programme.

The Commission will assess the compliance of the fiscal adjustment path with the Stability and Growth Pact under the preventive arm rules starting in 2018, following the expected exit from the Excessive Deficit Procedure and until the medium-term objective is achieved. The progressive adjustment path set out in this programme factors in the need for investment to support the current recovery and implementation of structural reforms, even though, according to the latest European Commission estimates, France has one of the least favourable economic situations in the euro area countries, as measured by the output gap. Therefore, this path facilitates the deployment of the government's structural reforms, which will produce positive effects for medium-term potential growth and for fiscal sustainability. The reduction of the general government deficit forecast over the government's five-year term is part of the government's overall economic policy. It will make it possible to close most of the gap between the current structural deficit and the medium-term objective over this period. The compliance of this path with the European fiscal benchmarks will be assessed yearly on the basis of notified data, as part of the Commission's overall analysis, taking account of each country's economic situation. The Commission specified that, for 2018, the assessment of

compliance with the recommended adjustment path would consider the Member States' positions in the business cycle in order to account for the relative need to sustain ongoing economic recovery. Structural adjustment in 2018 should stand at 0.1 percentage points of GDP, as major structural reforms affecting the labour market, taxes, investment, housing, climate, etc. are implemented. The European fiscal benchmarks consider all of these factors when assessing the appropriateness of structural adjustment with regard to each country's economic situation and reforms. France's adjustment forecast for 2018 does not deviate significantly from the Council's recommendation. Starting in 2019, structural adjustment will average 0.35 percentage points of potential GDP each year.

4.2.2 Implementing the expenditure benchmark

The expenditure benchmark provides an additional quantitative criterion to ensure the Member States that still have not met their medium-term objective do so, and that the Member States having achieved their MTO remain on target in the long run. The purpose of the expenditure benchmark is to measure the efforts that Member States make based on an aggregate under the direct control of the government, in contrast to the headline general government balance, which is affected by the business cycle and other non-discretionary factors.

In practice, the benchmark requires real public expenditure growth (excluding interest expenditure, cyclical unemployment expenditure, and including investment expenditure smoothed over four years) to be less than or equal to a **benchmark medium-term rate of potential GDP growth, minus a convergence margin**, unless excess growth is matched by discretionary revenue measures. Under the Stability and Growth Pact, compliance with the expenditure benchmark is measured either over one year or over two years, and deviation from the benchmark must be less than 0.5 percentage points of GDP over one year or cumulatively over two years.

In 2018, actual real growth of the expenditure aggregate should reach 0.9%, compare to the reference growth rate of 0.1%[13]. This is a non-significant deviation of 0.4 percentage points of GDP from the recommended adjustment. Nominal growth of the expenditure aggregate would stand at 2.0%, versus the target of 1.2%. Most of the discrepancy with the forecast deviation of the structural adjustement indicator stems from the difference in the scope of expenditure. The local government investment pattern hinders compliance with the structural investment path. Smoothing investment expenditure under the expenditure benchmark, which is more in line with a long-term approach to investment, adjusts for this effect by 0.2 percentage points of GDP. Furthermore, excluding interest expenditure from the aggregate at a time when debt service expenditure is falling inflates the expenditure aggregate by 0.1 points.

[13] The recommendation to France in July 2017 sets a nominal growth target of 1.2% for this aggregate.

TABLE 9. EXPENDITURE BENCHMARK

(growth, in %)	2018
Real expenditure growth corrected for discretionary revenue measures	**0.9**
Growth target under the expenditure benchmark	**0.1**
Baseline growth rate (medium-term potential GDP growth)	1.2
Margin to ensure convergence toward the MTO*	-1.1

* Convergence margin calculated by the Directorate General of the Treasury on the basis of the Vade mecum on the Stability and Growth Pact. See the methodological annex for details about calculating structural adjustment and the expenditure benchmark.

4.2.3 Implementing the debt criterion

In the years from 2018 to 2020, France will be subject to a transitional rule on reducing its debt ratio.[14] Under the adjustment path (see section 3.7) set out in this Stability Programme, this rule would be less restrictive for France than the ones discussed above, since it would require minimum structural adjustment of 0.1 percentage points of GDP, which means that compliance should be achieved within the programme timeframe. After the transitional period, the public debt ratio will be locked into a decreasing path towards 60% of GDP, as is shown by the projected reduction of the ratio by nearly 8 percentage points between 2017 and 2022.

[14] The transitional period stems from a provision in the “Six Pack” of November 2011 for a transitional “debt rule” that applies to excessive deficit procedures already under way on the date the “Six Pack” was adopted. In such cases, during the three years after the deficit is brought down to less than 3% of GDP, compliance with the “debt criterion” is assessed based on the mimimum linear structural adjustment criterion that should ensure sufficient progress towards compliance with the debt criterion benchmark.

5. Sensitivity analysis and comparison with previous programme

5.1 SENSITIVITY TO EXTERNAL ASSUMPTIONS

This economic scenario assumes oil prices and the euro exchange rate will stay at recent levels. Fluctuations in either or both could ultimately boost or dampen growth. Changes in interest rates and stock market prices could also have an impact on the scenario.

The strength of France’s exports will depend on our trading partners' growth, which is subject to many risk factors (see below), such as protectionist measures, especially in the United States, which would inhibit world trade, political risks in the euro area, Brexit, the pace of rate hikes by the Fed, financial risks relating to soaring stock markets in the United States and China’s massive debt.

World demand for French exports is expected to grow by 5.0% in 2018 and by 4.7% in 2019. The euro exchange rate is expected to average $1.23 in 2018 and 2019, and oil prices are expected to reach $65 a barrel in 2018 and 2019.

In addition to providing figures about how the assumptions concerning world demand for French exports, exchange rates, oil prices and interest rates will affect growth, inflation and the headline deficit in the baseline scenario (see Tables 1 to 4), this section assesses the main upside and down-side risks surrounding the forecast.

Uncertainty about the international scenario

Protectionist measures could have a major impact on trade. More specifically, if the United States imposes 25% duties on steel imports and 10% duties on aluminium imports, as announced by President Trump in early March, it could set off a chain reaction amongst its trading partners with major escalation risks. The European Union has already said that it is prepared to retaliate. On the other hand, world trade growth could be stronger than expected if the global economic recovery gains momentum.

The outcome of Italy’s recent general elections creates some uncertainty. If Italy has a government that is sceptical about the European project, it could have a destabilising effect on the euro area by making it difficult to find a common path towards greater integration.

The direction of some countries’ economic policies is still uncertain. In the United States, there is uncertainty about the fiscal path, debt sustainability, and how quickly the Fed will raise interest rates if the economy should show signs of overheating. In Italy, there is uncertainty about the implications of the March elections. In Germany, there is uncertainty about how long it will take to implement the

coalition agreement. In China, there is uncertainty about the scale of the government's support measures. In the euro area, there is uncertainty about a decline in underlying inflation potentially forcing the ECB to defer the exit from unconventional monetary policies.

The impact of Brexit is still an unknown, with uncertainty surrounding the negotiations, the final agreement with the EU, how long the uncertainty will last, and how the markets and policy mix will react.

Emerging economies still face major risks. Financial and fiscal imbalances in China could lead to a more severe than expected slowdown. Emerging countries are also vulnerable to the Fed hiking rates more rapidly than expected, which could lead to major capital outflows. Political and geopolitical uncertainties constitute another downside risk for these countries.

Financial risks are still high in light of the price/earnings ratio[15]. American equities appear to be overpriced and European equities prices may also be too high, despite the correction in early February. Furthermore, after a period of historically low interest rates, which led to greater risk-taking, a faster-than-expected rise in interest rates could lead to renewed tension on markets.

Alternative scenarios presented in the Stability Programme:[16]

TABLE 1. - IMPACT ON FRANCE'S ECONOMY OF A 1% INCREASE IN WORLD DEMAND FOR FRENCH EXPORTS*

(deviation from the baseline scenario in %)	n	n+1	n+2
Gross domestic product	**0.3**	**0.3**	**0.3**
Total jobs created (thousands)	19	45	50
Household consumption deflator	0.1	0.2	0.3
General government primary balance (percentage points of GDP)	0.1	0.2	0.2

* Permanent 1% increase in export demand at the start of year n with no change in real interest rates
NB: An increase in world demand would boost exports, which would feed through to the rest of the economy, increasing business investment in particular.

[15] The price/earnings ratio is the ratio of the share price to net profit per share. This ratio is above its long-term average for S&P500 shares. It has been rising steadily since 2012.

[16] The alternative scenarios in Tables 1 to 4 were obtained with the Mésange 2017 model. DG Trésor Working Papers (2017), "Le modèle macroéconométrique Mésange : réestimation et nouveautés" by Anne-Sophie Dufernez, Claire Elezaar, Pierre Leblanc, Emmanuelle Masson, Harry Partouche, José Bardaji, Benoît Campagne, Marie-Baïanne Khder, Quentin Lafféter, Olivier Simon.

TABLE 2. - IMPACT ON FRANCE'S ECONOMY OF A 10% DEPRECIATION OF THE EURO AGAINST ALL OTHER CURRENCIES*

(deviation from the baseline scenario in %)	n	n+1	n+2
Gross domestic product	**0.5**	**0.9**	**1.3**
Total jobs created (thousands)	24	90	154
Household consumption deflator	0.6	1.1	1.6
General government primary balance (percentage points of GDP)	0.1	0.3	0.4

* 10% depreciation of the euro against all other currencies at the beginning of the year n, with no change in real interest rates, no reaction from the rest of the world.
NB: A weak euro would boost growth in the short term by improving France's price competitiveness outside of the euro area and by stimulating the economic growth of its euro area partners.

TABLE 3 - IMPACT ON FRANCE'S ECONOMY OF A $10 INCREASE IN OIL PRICES*

(deviation from the baseline scenario in %)	n	n+1	n+2
Gross domestic product	**-0.1**	**-0.2**	**-0.2**
Total jobs created (thousands)	-9	-38	-45
Household consumption deflator	0.3	0.4	0.4
General government primary balance (percentage points of GDP)	-0.1	-0.2	-0.2

* $10 increase in the price of oil per barrel at the beginning of year n, with no change in real interest rates, no reaction from the rest of the world.
NB: With no change in exchange rates, an increase in the price of oil would have an inflationary impact. The resulting increase in consumer prices and decrease in corporate profits would weaken growth.

TABLE 4 - IMPACT ON FRANCE'S ECONOMY OF A 100-BASIS-POINTS INCREASE IN SHORT-TERM INTEREST RATES LASTING FOR TWO YEARS*

(deviation from the baseline scenario in %)	n	n+1	n+2
Gross domestic product	**-0.1**	**-0.3**	**-0.1**
Total jobs created (thousands)	-4	-33	-37
Household consumption deflator	0.0	0.0	-0.1
General government primary balance (percentage points of GDP)	0.0	-0.2	-0.1

* A 100-basis-point increase in euro area short-term interest rates lasting for two years and occurring at the beginning of year n, with its impact on long-term interest rates, with no change in the value of the euro, and no reaction from the rest of the world. In this scenario, a rise in interest rates corresponds to an increase in production costs (user cost of capital) and has nothing to do with improved growth.
NB: An increase in central bank interest rates would hamper growth by restricting business investment and the return on capital. It would promote savings over consumption and lead to an appreciation of the euro. However, this scenario fails to account fully for the impact of the recent rise in long-term interest rates that could indicate a change in expectations regarding American monetary policy.

BOX 7: USING ALTERNATIVE SCENARIOS FOR FORECASTING

The alternative scenarios presented in Tables 1 to 4 need to be handled with care. First of all, the multipliers linked to the alternative scenarios depend on the models chosen, which means that estimating them is subject to a high degree of uncertainty. For example, the alternative scenarios above are based on the Mésange model[a], which is used to assess economic policy measures. They may differ from scenarios based on the Opale model[b], which is used for macroeconomic forecasting 1 to 2 years out. For instance, the impact of a 10% depreciation of the euro against all other currencies on GDP is smaller when forecast with the Opale model, at 0.7 points after three years, versus 1.3 points with the Mésange model. The impact of a $10 increase in oil prices on GDP is greater when forecast with the Mésange model, at -0.2 points after three years, versus -0.1 points with the Opale model. The alternative scenarios concerning export demand are relatively similar with both models. A 1% increase in world demand boosts GDP by 0.3 points after three years in both the Mésange and Opale models.

Furthermore, it is important to understand the nature of economic shocks before predicting how they will affect growth. The multipliers shown in the tables above are the figures associated with a theoretical shock that affects only a single exogenous variable and they have been estimated on the basis of shocks observed during the estimation period. However, real-world shocks rarely affect only a single variable in isolation and they may be different in nature from previous shocks. For example, we could imagine that an appreciation of the euro caused by renewed growth in the euro area could have a less adverse impact on growth than an appreciation caused by a purely exogenous factor. Similarly, an increase in oil prices stemming from a supply shock, such as a move by OPEC, could be more adverse for growth than an increase stemming from a demand shock, since, in the latter case, the negative impact would be partially offset by a positive global demand shock.

(a) DG Trésor Working Papers (2017), "Le modèle macroéconométrique Mésange : réestimation et nouveautés," by Anne-Sophie Dufernez, Claire Elezaar, Pierre Leblanc, Emmanuelle Masson, Harry Partouche, José Bardaji, Benoît Campagne, Marie-Baïanne Khder, Quentin Lafféter, Olivier Simon.

(b) DG Trésor Working Papers (2017), "La maquette de prévision Opale$_{2017}$," by Aurélien Daubaire, Geoffrey Lefebvre, Olivier Meslin.

5.2 COMPARISON WITH PREVIOUS PROGRAMMES

TABLE 10 - COMPARISON WITH THE PREVIOUS STABILITY PROGRAMME

	2017	2018	2019	2020	2021	2022
2017-2020 Stability Programme (April 2017)						
Real GDP growth (in %)	1.5	1.5	1.6	1.7		
Potential real growth (in %)	1.5	1.4	1.3	1.4		
Output gap (as a % of potential GDP)	-3.1	-3.1	-2.8	-2.5		
General government net lending (% of GDP)	-2.8	-2.3	-1.6	-1.3		
Structural balance (% of potential GDP)	-1.0	-0.5	0.0	0.0		
Structural adjustment (% of potential GDP)	*0.5*	*0.5*	*0.5*	*0.0*		
General government gross debt (% of GDP)	96.0	95.9	94.7	93.1		
General government debt, excl. support for the euro area (% of GDP)	93.1	93.1	92.0	90.4		
2018-2022 Stability Programme (April 2018)						
Real GDP growth (in %)	1.8	2.0	1.9	1.7	1.7	1.7
Potential real growth (in %)	1.25	1.25	1.25	1.25	1.30	1.35
Output gap (as a % of potential GDP)	-0.9	-0.2	0.4	0.9	1.3	1.6
General government net lending (% of GDP)	-2.6	-2.3	-2.4	-0.9	-0.3	0.3
Structural balance (% of potential GDP)	-2.0	-1.9	-1.6	-1.4	-1.0	-0.6
Structural adjustment (% of potential GDP)	*0.5*	*0.1*	*0.3*	*0.3*	*0.4*	*0.4*
General government gross debt (% of GDP)	97.0	96.4	96.2	94.7	92.3	89.2
General government debt, excl. support for the euro area (% of GDP)	94.1	93.7	93.5	92.1	89.8	86.8

Comparison with the previous Stability Programme is delicate because of the many events occurring since then. The presidential elections in May 2017 changed the roadmap for France's economy and its fiscal path. These changes were enshrined in the 2018-2022 Public Finance Planning Act passed in December 2017. The Act also updated potential growth and output gap assumptions for a more conservative scenario. Consequently, the current view of the economic situation is brighter than that underlying the 2017 Stability Programme. This revision does not affect the headline balance, but it calls for a larger structural deficit and a smaller cyclical deficit.

In 2017, the actual headline deficit turned out to be smaller, at 2.6% of GDP, than the 2.8% deficit predicted in the 2017 stability programme, whereas actual and forecast structural adjustment were in line at 0.5% of potential GDP. In 2018, this programme forecasts GDP growth of 2.0%, which is stronger than the growth forecast from the previous programme. Structural adjustment will be weaker, at 0.1 percentage points of potential GDP. This is the appropriate pace in view of the scale of ongoing economic reforms. The 2019 headline deficit is expected to be bigger than forecast in

the 2017 Stability Programme because of the replacement of the Competitiveness and Employment Tax Credit by permanent social security contribution cuts, for a deficit equivalent to 2.4% of GDP in this Stability Programme, compared to 1.6% in the 2017 Stability Programme. This effect is temporary and should fade by 2020. The headline deficit is slightly smaller in this forecast, at 0.9% of GDP, compared to the 1.3% deficit forecast in the 2017 Stability Programme. This Stability Programme forecasts structural adjustment equivalent to 0.3% of GDP in 2019 and 2020, versus the adjustment of 0.5% in 2019 and 0.0% in 2020 forecast in the 2017 Stability Programme. The 2017 Stability Programme forecast that structural equilibrium would be achieved by the end of 2019, but with a negative output gap of 2.8% of GDP, which would have meant that no further structural adjustment was required after 2020.

5.3 COMPARISON WITH THE EUROPEAN COMMISSION'S PUBLIC FINANCE FORECASTS

TABLE 11 - COMPARISON WITH THE EUROPEAN COMMISSION'S FORECASTS

	2017	2018	2019	2020	2021	2022
European Commission's projections (Autumn Forecast, November 2017)						
Real GDP growth (in %)	1.6	1.7	1.6			
General government net lending (% of GDP)	-2.9	-2.9	-3.0			
Structural balance (% of potential GDP)	-2.4	-2.7	-3.0			
Structural adjustment (% of potential GDP)	*0.2*	*-0.4*	*-0.3*			
General government gross debt (% of GDP)	96.9	96.9	96.9			
2018-2022 Stability Programme (April 2018)						
Real GDP growth (in %) (*)	1.8	2.0	1.9	1.7	1.7	1.7
General government net lending (% of GDP)	-2.6	-2.3	-2.4	-0.9	-0.3	0.3
Structural balance (% of potential GDP)	-2.0	-1.9	-1.6	-1.4	-1.0	-0.6
Structural adjustment (% of potential GDP)	*0.5*	*0.1*	*0.3*	0.3	0.4	0.4
General government gross debt (% of GDP)	97.0	96.4	96.2	94.7	92.3	89.2

** No adjustment for working days*

The European Commission's Autumn Forecast published on 9 November 2017 called for France's general government deficit to stand at 2.9% of GDP in 2017, followed by 2.9% in 2018 and 3.0% in 2019 (based on a "no-policy-change" scenario for 2019).

The Commission's forecast in 2017 does not incorporate the 2017 outturn that Insee estimated in March 2018. The Commission forecast a headline deficit of 2.9% of GDP, but the Insee now estimates the figure at 2.6%. The GDP growth forecast has since been revised from 1.7% in the Commission's forecast to 2.0% in this Stability Programme, or 1.8% with no adjustment for working days.

The latest Commission forecast called for negative structural adjustment of 0.4 points in 2018, whereas this Stability Programme predicts positive structural adjustment of 0.1 percentage points of GDP, in line with the adjustment path set out in the Public Finance Planning Act. This discrepancy stems in part from non-tax revenue, such as the dividend paid by Banque de France in 2018, and differing views about the effectiveness of savings measures (e.g. expected savings by local governments).

Finally, in 2019, the two forecasts are not comparable since the Commission’s adjustment path with no policy change does not include all of the planned measures to contain the growth of public expenditure. This choice explains the larger structural deficit in the European Commission's scenario.

6. Quality of public finances

6.1 QUALITY OF PUBLIC EXPENDITURE

6.1.1 State government and central agencies expenditure

State government and central agencies expenditure is used for the strategy to transform government. Clear choices have been made to finance the government's priorities and improve both the effectiveness and the quality of public expenditure.

An ambitious transformation of the housing sector is underway with the aim of moving away from reasoning in terms of the solvency of demand, which is inflationary, and towards increasing housing supply. It is based on current and future reforms affecting how housing benefits operate.

At the same time, the government has started to reduce the number of subsidised employment contracts, which have not proven to be effective at getting the jobless back into employment, especially during a sharp upswing in the business cycle. Reducing the number of contracts releases resources to finance an Investment in Skills Plan (PIC), which produces more decisive structural benefits in the long term. The plan aims to step up job training efforts for the groups most vulnerable to a lack of skills or rapidly out-dated skills in an ever-changing labour market. This expenditure is part of the policies financed under the *Great Investment Plan* (GPI).

In addition to addressing job skills, the *Great Investment Plan* (GPI) is designed to finance the deployment of structural reforms to boost the growth potential of France's economy. The plan has an endowment of €57bn over the government's five-year term. It will finance public investment to address the four major challenges facing France's economy: i) building an innovation society; ii) accelerating ecological transition; iii) building competitiveness through innovation; iv) building central government for the digital age.

To address the second challenge, the plan finances the climate plan policies, enabling France to accelerate its ecological transition and develop a sustainable growth model. This investment will come to more than €20bn over the five-year term of this government.

With regard to the third challenge, the plan will devote €13bn to structural actions to promote innovation and move toward higher end production in the economy. More specifically, calls for projects will finance excellence initiatives in academic research and business innovation relating to the main technological challenges. This challenge will also be addressed by €5bn in investment to promote higher end agricultural production.

The fourth challenge will be met with cross-cutting action to modernise government, relying on innovation and the spread of new technology. A €700m fund for State government transformation will support projects for new digital services (paperless procedures, automation of repetitive tasks, artificial intelligence), projects relying on new line and staff processes (setting up shared service centres, new physical workplace organisational structures) and innovative projects relating to HR and

compensation practices. The projects will be selected according to strict criteria to achieve specific transformation objectives. Investment will be initiated, monitored and assessed to measure its real impact and then stepped up or cut back depending on the outcomes.

In addition to GPI, new resources will be devoted to sovereign functions, including the justice system, police and gendarmerie, along with the armed forces, with a 2019-2025 military planning bill, for the purpose of improving the operating conditions for these functions to meet current challenges.

In the medium term, greater effectiveness of public expenditure, particularly State government and central agencies expenditure, will be the object of the reforms set out in the government transformation programme, *Public Action 2022* (see Box 8).

BOX 8 – *PUBLIC ACTION 2022*

The government has initiated a major government transformation programme called *Public Action 2022* (AP22).

This process was started in October 2017 with three objectives: (i) improving user service quality, (ii) providing a modernised working environment for civil servants by involving them fully in the definition and monitoring of transformations, and (iii) upholding the reduction of public expenditure by setting a target of cutting back more than 3 percentage points of GDP by 2022. The process encompasses all general government sub-sectors and is led at the highest level by the President of the French Republic and the Prime Minister.

The *Public Action 2022* process uses three approaches:

- **A public policy approach**, based on a review of 21 public policies that have been identified as priorities and divided into five groups: (i) Solidarity and Health; (ii) Employment, Economy and Finance; (iii) Agriculture, Ecology and Local Government; (iv) Sovereignty; (v) Education, Culture and Sports. The programme committee (CAP22) conducts the public policy review. This independent committee is made up of economists, elected officials and experts from the public and private sectors. The committee has 34 members, including 3 chairs - Ross McInnes, Chairman of the Board of Safran; Véronique Bédague-Hamilius, Secretary General of Nexity and Frédéric Mion, Director of the Institut d'études politiques de Paris. The committee's task is to conduct an in-depth review of all general government functions and expenditure (central government and central agencies, social security funds) with regard to specific public policies. The committee is communicating with the line ministries, with contributions and testimony from ministers. The committee will submit its report to the Prime Minister in the second quarter of 2018.
- **A cross-cutting interministerial project approach** examining the following five areas: (i) simplification and improvement of service quality, (ii) digital transformation, (iii) recasting the human resources framework, (iv) local organisation of public services, (v) modernising budget management and accounting. These cross-cutting interministerial projects have examined several cross-cutting public policies and will define the guiding principles for reform.
- **An approach that involves users and civil servants.** The public action forum held between 24 November 2017 and 9 March 2018 was an online consultation with several thousand civil servants and public service users.

A first set of measures, stemming in part from the cross-cutting projects was announced at the first meeting of the Interministerial Committee on Government Transformation (CITP) on 1 February 2018. These measures will create favourable conditions for the implementation of future reforms. More specifically, these measures dealt with simplification and improvement of service quality, digital transformation, recasting the human resources framework, which correspond to the interministerial projects (i), (ii) and (iii), with the following objectives:

- Initiating a new contract with civil servants: broad-based consultations have started to recast the mutual commitments of civil servants and the government
- Granting more freedom and responsibility to public managers (flexibility for hiring procedures, more management autonomy)

- Enhancing transparency with regard to the effectiveness and quality of public services in dealings with users (requirement that all administrations dealing with users publish outcome and service quality indicators by 2020).
- Stepping up digital transformation of administrations (simplification of administrative formalities for users and relieving civil servants of administrative tasks so that they can provide user support).
- Supporting government transformation (first call for projects by the Government Transformation Fund, which will raise €700m over the next five years).

The findings on the entire *Public Action 2022* process, both with regard to public policies and interministerial projects, will be submitted to the Prime Minister in early May. This will be followed by consultations and decision-making and a new meeting of the Interministerial Committee on Government Transformation will enable the government to present its roadmap for government transformation over its five-year term.

6.1.2 Containing healthcare expenditure

The strategy for transformation of the healthcare system launched on 13 February 2018 set out 5 major projects: quality and appropriateness of care, financing procedures, digital technology, human resources and training, local organisational structures. The 2018-2022 national healthcare expenditure growth target plan to support transformation of the healthcare system is fully in line with the overall medium-term framework. It lays the foundations for the transformations to be initiated in 2018 to enhance the efficiency of the system and to ensure the sustainability of healthcare expenditure. Investment will play a dominant role in the modernisation and adaptation of the healthcare system.

The strategy relies on using all of the available leverage for several priorities, including:

- **The structure of healthcare provision.** Healthcare institutions will develop innovative and more efficient treatment procedures, by expanding alternatives to hospital admissions and promoting ambulatory care, improving their internal performance through more efficient purchasing under the Hospital Performance Programme for Responsible Purchasing (PHARE), monitoring wage bills, promoting pooling of resources and management for cross-cutting activities.
- **Enhancing the appropriateness and effectiveness of prescriptions.** Efforts to contain drug and medical device prices will continue to provide a fair reward for innovation and change the structure of healthcare product consumption, including expanding the prescription and use of generic and biosimilar products in hospitals and in doctors' surgeries.
- **Enhancing the appropriateness of care.** The objective is to reduce duplicate and inappropriate treatments and care through action to monitor medical practices and adapt fee-setting procedures to technological changes.
- **Improving the effectiveness of prescriptions for transport and sick leave.** The objective is to ensure effective prescribing and contain rapid expenditure growth by making prescribers accountable and strengthening monitoring of medical prescriptions.

These structural objectives will be broken down into annual targets when setting the national healthcare expenditure growth target (Ondam). The available provisional data show that monitoring of the national healthcare expenditure growth target was effective in 2017 and that the 2.2% growth target was met. It was the eighth year in a row that the target has been met, testifying to the effectiveness of the government's monitoring of healthcare expenditure.

6.1.3 Streamlining local government expenditure

Efforts to contain local government expenditure should be continued over the next five years as part of a new approach based on contracts between central government and local governments.

Local governments' participation in fiscal consolidation efforts was announced by the President of the French Republic at the first meeting of the national conference of local governments on 17 July 2017. The government sought to take a **new approach to financial relations between central government and local governments**, based on trust and marking a break with unilateral cuts in grants.

The 2018-2022 Public Finance Planning Act of 22 January 2018 has enshrined this new approach. Article 13 of the Act sets out a national target for the growth of local governments' real operating expenditure and that of local government cooperation groups with the power to levy taxes. Article 16 sets caps on the growth of central government financing for local governments over the next five years, since the planned caps on the VAT compensation fund and the share of VAT revenue earmarked for regional government are not binding. Article 29 implements the arrangement for contracts between central government and local governments that account for the majority of local government expenditure.

In practical terms, Article 13 of the Act sets **the national target for the growth of local governments' real operating expenditure** and that of local government cooperation groups with the power to levy taxes. The target has been set at 1.2% growth per year over the next five years. There is also a **target for reducing the borrowing requirement**. **These provisions apply to all local governments and they must be considered during their budget policy debates.**

A contract-based arrangement targeting the 322 largest local governments, which account for nearly two-thirds of local government operating expenditure, has been set out in Article 29 of the Act (see Box – Implementation of Contracts with Local Governments). The contracts are signed by the central government representative in the region or department and each local community to set the targets for the growth of real operating expenditure, the reduction of the borrowing requirement and, for some local governments, the improvement of their capacity to reduce their debt. In keeping with this contract-based approach, growth targets can be modulated to suit the specific circumstances of each local government, within the limits set by law. Failure to meet the target triggers a **corrective mechanism in the form of a clawback by central government**, equivalent to 75% of the deviation from the target. For local governments that are eligible to sign a contract, but do not do so, the clawback is equivalent to 100% of the deviation from the growth target set by central government.

6.2 QUALITY OF PUBLIC REVENUE

The aggregate tax and social security contribution rate will be cut by 1 point over the five-year term of this government to promote growth and employment.

This will relieve the tax burden on French businesses and household, which hinders demand and private initiative. The reduction of taxes and social security contributions will continue with a cut of 1 percentage point of GDP by 2022 that will benefit both households and businesses. In the years covered by the Public Finance Planning Act, the aggregate tax and social security contribution rate will fall from 45.4% of GDP in 2017 to 44.3% in 2022. This reduction corresponds to three strategic choices made by the government. The first is to provide immediate support for growth, promote employment and boost purchasing power by providing greater rewards for work by introducing the cuts on 1 January 2018. The second is to boost competitiveness and cut red tape for businesses. The third is to boost private-sector investment in businesses that take risks, innovate and create the jobs of tomorrow.

Modernising taxation and reducing the burden for the least well-off households

These tax cuts are largely for households and will primarily benefit middle-class workers and low-income households. In the private sector, employees' contributions for health and employment insurance have been eliminated and are now financed by a higher rate for the General Social Security Contribution, which is levied on a broader base. This expands the tax base for financing social security so that the burden does not fall exclusively on wages. In addition to providing workers with a net purchasing power gain, these cuts will stimulate both labour demand and labour supply by reducing the tax wedge on wages and supplementing the increase in the in-work benefit. Furthermore, households will gradually be exempted from the residence tax, which will produce a purchasing power gain and more equitable taxation. Finally, a measure to exempt overtime pay from social security contributions will enter into force in 2020.

Sustaining the measures taken to boost competitiveness and lower labour costs

Business taxes will be reduced and simplified to make France's businesses more competitive, boost growth and make France's economy more attractive. The corporate income tax rate will be cut in stages down to 25% by 2022. This cut will bring France into line with the European average and reduce the cost of capital, thereby stimulating long-term investment. The Competitiveness and Employment Tax Credit will also be replaced by permanent cuts in employers' social security contributions in 2019. This date was chosen primarily to ensure that the general government deficit remains below 3% of GDP. It was also chosen to simplify the existing system and support employment and the competitiveness of French companies over time. The replacement of the Competitiveness and Employment Tax Credit also provides stability for businesses, especially the smallest ones. Contribution cuts will consolidate the efforts made up until now to help businesses restore their profitability, but they will also sustain demand for unskilled labour by being even more targeted on minimum wage jobs than they are today.

Supporting investment, entrepreneurship and innovation

France's wealth tax (ISF) was transformed into a property wealth tax (IFI) in 2018. The year also saw the introduction of a 30% flat tax rate on investment income that covers both taxes and social security contributions. These moves will stimulate productive investment that is both risky and innovative. In the midst of sweeping technological change, the demand for capital is even greater than before and cutting taxes on capital is now crucial. The different measures are also in line with seeking greater European convergence, since French taxes on capital are particularly high compared to its European partners. In addition to helping reduce the cost of capital, these measures will channel more domestic savings into financing businesses.

Accelerating ecological transition

Carbon tax increases have been stepped up to accelerate the ecological conversion of our economy and the convergence of taxes on diesel oil and petrol will be completed by the end of this government's five-year term. This will internalise the social cost of economic agents' use of fossil fuels, thereby reducing our CO_2 emissions. Consequently, France will make progress with regard to the share of revenue from environmental taxes. Fiscal measures, such as the full deployment of heating benefits (*chèque-énergie*) and the introduction of a trade-in premium for older vehicles are intended to provide ecological transition support for the most vulnerable.

BOX 9 – WITHHOLDING AT SOURCE FOR PERSONAL INCOME TAX: MODERNISING HOUSEHOLD TAXATION

As of 1 January 2019, personal income tax will be withheld at source on 98% of income. This modernisation of tax collection was initially planned for 2018, but the launch was deferred for one year to ensure that the system is completely reliable.

This major reform will eliminate the one-year lag between receiving taxable income and paying tax on it, thereby reducing tax payment problems when taxpayers' income varies or when their situation changes.

Withholding at source will simplify tax procedures for wage earners. Withholding at source will be attached to the single staff reporting statement (DSN), which will simplify formalities and produce savings for employers.

Withholding at source of personal income tax will not modify the founding principles of the French tax system, and, more specifically:

- The progressive nature of personal income tax, joint filing and income splitting for couples and families with dependent children, and the application of tax reductions and tax credits will all be maintained;
- The information used to calculate withholdings will remain confidential and the withholding rates can be individualised for different members of the same household filing jointly;
- The annual income tax return will be maintained.

Entities (employers, pension funds, etc.) paying wages, salaries, pensions and income support payments will withhold taxes at source on behalf of the central government. The withholding rates will be calculated by the tax administration using information from the taxpayers' latest tax returns. Other income covered by this reform, such as self-employment income and property income, will give rise to contemporaneous advance tax payments made by the taxpayers themselves. The withholding rate will be modified at the taxpayer's request to account for changes in his or her family situation and for variations in income from one year to the next.

In order to avoid a double tax burden for households in 2019, the income subject to the new withholding at source and earned in 2018 will not be taxed. More specifically, the tax owed on recurring income earned in 2018 and subject to withholding at source from 2019 onwards will be cancelled out by a special tax credit (called Collection Modernisation Tax Credit – CIMR). Noticeably, the tax credits and reductions relating to 2018 income will be maintained. Non-recurring income, which is by nature unlikely to be taxed twice in 2018, will still be subject to income tax and the tax treatment of the income earned by self-employed workers and company managers in 2018 will be subject to specific rules to prevent tax minimisation arrangements.

The preliminary evaluation of the reform (released in September 2016 along with the Draft Budget for 2017) estimated that its net fiscal impact would be a decrease in revenue of €0.3bn in the transition year (i.e. 2018, which has been deferred until 2019). This estimate incorporates demographic and macroeconomic effects, the possibilities for modifying withholding rates and the impact of the reform on tax collection rates. However, this estimate is sensitive to macroeconomic developments in 2018 and 2019, tax collection rates during the transition phase, the proportion of taxpayers modulating their withholding rates during the year, and possible actions by taxpayers aimed at increasing their untaxed income in 2018.

7. Sustainability of public finances

7.1 SUSTAINABILITY OF PUBLIC FINANCES

Sustainability of general government debt

Impact of the ageing population on public finances

A strong birth rate, an increasing older worker employment rate and the reforms made over the last 20 years have placed France in a strong position to deal with its ageing population compared to its European partners. These demographic trends make it easier to balance the pension system's finances and to ensure long-term fiscal sustainability according to the latest domestic[17] and European forecasts[18].

Various reforms implemented in recent years make it possible to meet the current financial challenges. The pension reforms of 2010 and 2014 and the national multisector agreement on supplementary pensions signed in October 2015 were implemented in a time of deep economic crisis and when baby-boomers were preparing for retirement. These reforms call for the burden of consolidation measures to be shared by workers, employers and pensioners.

Based on the Pensions Advisory Council's new expenditure forecasts, which appear less favourable in the short term, the Pension Steering Committee has submitted recommendations to the government for putting the pension system back on the path to equilibrium. The Committee also puts the scale of the system's financial imbalance into perspective[19]. The Pension Steering Committee also calls on the government to "improve the transparency, clarity and governance" of the pension system.

Over the course of its five-year term, the government will undertake a major reform of the pension system. The reform should produce a simpler and fairer system that factors in longer life expectancy for each successive generation, so that everyone is entitled to the same rights for each euro paid in contributions, while upholding the solidarity mechanisms in the system. The reform will make the system clearer and more predictable for everyone, providing more protection for workers when changing jobs. The reform will prescribe gradual progress towards uniformity of the calculation rules used by the different pension schemes. Greater clarity will make financial oversight of our pension system more effective and give users greater confidence in its sustainability and fairness.

[17] See Conseil d'orientation des retraites, 2017, "Évolutions et perspectives des retraites en France – rapport annuel du COR" (June 2017) and "Quatorzième rapport du Conseil d'orientation des retraites - Retraites : perspectives financières jusqu'en 2070, Sensibilité aux hypothèses, résultats par regime" (November 2017). The next annual report will be published in June 2018.

[18] European Commission, 2018, "The 2018 Ageing Report: economic and budgetary projections for the 28 EU Member States (2016-2070)" (publication pending).

[19] Half of the deterioration stems from revised assumptions.

The European projections by the Ageing Working Group (AWG), based on Eurostat's population forecasts, predict that pension expenditure as a percentage of GDP in France will increase slightly through 2040, and then fall markedly over the long term. In 2070, France's ageing-related spending (which includes, in addition to pensions, spending on healthcare, long-term care, unemployment and education) is expected to have fallen by 3 percentage points of GDP from its 2016 level. Pension expenditure alone is expected to contract by 3.3 points. France's average fertility rate is one of the highest in Europe for the years between 2016 and 2070, standing at 2.0 on average. A strong birth rate could partially offset the ageing of the population. Moreover, reforms over the last 20 years should raise the retirement age and slow the growth of pension benefits.

The long-term assumptions used for these projections are not the same as those used in the 2017 Stability Programme, which were based on the projections made in 2015. In the case of France, the differences primarily relate to macroeconomic trends, which are more sombre in the medium term. Productivity growth and the unemployment rate are now expected to take longer to attain their long-term targets. On the other hand, there is little change regarding demographic trends. Consequently, projected ageing-related costs have been revised upward around the year 2040, but should fall back to the level expected in 2015 in the longer run.

Sustainability indicator (S2)

A country's public finances are sustainable when it is able to meet its long-term financial obligations without having to cut expenditure or increase revenue. A fiscal sustainability gap is normally assessed by estimating the immediate and lasting fiscal adjustment (expressed in percentage points of GDP) that would be required to avoid a long-term increase in the debt-to-GDP ratio, with no further change in the structural primary balance (meaning the structural balance net of interest expenditure). This indicator, called the S2 indicator, is the sum of two terms:

- **The impact of the initial budget position**, which corresponds primarily to the difference between the structural primary balance and the balance that would stabilise debt in the long term.
- **The impact of the ageing population** on expenditure on pensions, healthcare, long-term care, education and unemployment benefits starting in 2020 based on a no-policy-change assumption. Work carried out by the Member States and the European Commission produced a harmonised estimate of this impact at the European level. The data used here are taken from the 2018 Ageing Report (publication pending).

According to the S2 sustainability indicator calculated using the AWG's new projections up to 2070, long-term debt stabilisation will be achieved, even if the structural primary balance remains at its 2017 level in the years from 2018 to 2022. The S2 indicator should stand at -0.4 percentage points of GDP in this scenario, indicating that no additional adjustment is necessary to achieve a stable debt-to-GDP ratio in the long term. The expected favourable impact of the ageing population exceeds the gap initially forecast between the structural primary balance and the debt-stabilising balance (see Table 12).

The savings set out in this Stability Programme should allow France to improve its S2 indicator considerably. The significant structural effort planned for 2018-2022 should reduce the necessary adjustment stemming from the initial budget position by 1.7 percentage points of GDP. S2 would stand at -2.1% of GDP in 2022, based on the assumptions used in this Stability Programme. As from

2022, all the conditions should be in place for a substantial reduction in the long-term debt-to-GDP ratio.

Long-term debt would be stable, even if we exclude the years after 2060 from our calculation of the indicator. That period is very favourable for fiscal sustainability because of the assumption of lower ageing-related costs after 2060. S2 would stand at 0.0 if those years were excluded, with a structural primary balance maintained at its 2017 level, and at -1.7, if we include the savings measures described in this Stability Programme.

TABLE 12. - FISCAL SUSTAINABILITY GAP INDICATOR S2 (PERCENTAGE POINTS OF GDP)

Base year	Same scenario for 2018 to 2022	Stab Prog scenario
Sustainability gap (S2 indicator)	**-0.4**	**-2.1**
o.w. impact of the initial budget position	+1.2	-0.5
o.w. impact of the ageing population (as of 2022)	-1.6	-1.6

NB:

- The S2 sustainability indicator is estimated on the basis of a counterfactual scenario where the structural primary balance is assumed to be constant at its 2017 level for the duration of the programme (2018-2022), independently of the impact of the ageing population. It corresponds to the long-term fiscal adjustment that would have to be achieved in 2022 to stabilise the very long-term (up to 2070 in this case) debt-to-GDP ratio in view of the impact of the ageing population after 2022.
- The S2 indicator is estimated on the basis of the 2022 structural primary balance expected under this programme. It corresponds to the long-term fiscal adjustment that would have to be achieved in 2022 to stabilise the very long-term debt-to-GDP ratio in view of the impact of the ageing population after 2022.
- The ageing-related expenditure projections (pensions, healthcare, long-term care, education, unemployment) are taken from the European Commission's 2018 Ageing Report, which will be published at the end of the first semester of 2018.

7.2 CONTINGENT LIABILITIES

General government off-balance sheet liabilities cannot be evaluated with certainty and depend on future developments. If a given event occurs, the central government's liability may be invoked. The liabilities may eventually affect public finances, and are therefore very closely monitored. More specifically, central government off-balance sheet liabilities are described in detail in the central government's General Financial Statement that is published each year and certified by the government audit office (*Cour des Comptes*). The main general government off-balance sheet liabilities are:

- liabilities for future ageing-related expenditure (pensions, healthcare, long-term care, education), where valuations depend on the demographic and macroeconomic outlook. The impact of these liabilities on debt sustainability is measured by calculating a sustainability gap indicator, the S2 indicator (see Section 7.1).
- contingent liabilities, which are liabilities that may or may not have to be paid, depending on future events. In most cases, these relate to guarantees provided by the central government and to a lesser extent by local governments.

Central government guarantees cover a wide range of actions to sustain or preserve economic activity or to provide financing for certain economic agents when market financing is inadequate. These guarantees are given under clear-cut agreements and they include in particular: central government debt guarantees, guarantees related to general interest functions (insurance mechanisms operated through the central reinsurance fund, guarantees provided on behalf of the central government by Bpifrance to support exports, guarantees to protect savings, etc.), liability guarantees (e.g. for France's share of ESM callable capital) and central government financial commitments for co-financing projects and providing development assistance. Generally speaking, the risk of such guarantees being invoked is small. Furthermore, no new central government guarantees can be given other than in a Budget Act, as stipulated in the Constitutional Bylaw on Budget Acts (Loi organique relative aux lois de finances, LOLF). The central government's role in regulating both the economy and French society also means that it is committed to providing budget-balancing subsidies, particularly to the special pension schemes.

In 2016 (latest available data), the aggregate outstanding central government guarantees under clear-cut agreements, meaning all central government debt guarantees, came to €195bn compared to €185bn in 2015. Some of the guarantees provided increased between 2015 and 2016, mainly the guarantees provided to Dexia (an additional €5bn between 2015 and 2016), the unemployment insurance scheme, Unédic (an additional €3bn) and the first-time homebuyers guarantee fund, SGFGAS (an additional €3bn). These increases were partially offset by the reduction of other guarantees, such as the outstanding guaranteed debt of Caisse Centrale du Crédit Immobilier de France (3CIF), which decreased by €1bn. It should be noted that the debt of the unemployment insurance scheme, which is part of the general government sector, is already included in Maastricht debt. Furthermore, guarantees for EFSF loans under financial assistance programmes are now recognised as part of the Maastricht debt of the Member States, in proportion to the share of the guarantees they provide, following Eurostat's decision of 27 January 2011.

The use of this type of guarantee has increased since the crisis, particularly in developed economies, but without necessarily being a long-term arrangement. It requires the central government to be more vigilant about risks that could be transferred to the public sector. The fiscal risks that the central government incurs through these guarantees, which serve a general interest purpose, must be assessed beforehand, and must be subject to ongoing monitoring and control. Parliament is also

notified each year of the guarantee authorisations granted by the government, in accordance with the terms of Article 24 of the 2018-2022 Public Finance Planning Act of 22 January 2018.

France monitors these risks in three ways:

- First, through a decision-making process, where, under the terms of Article 34 of the Constitutional Bylaw on Budget Acts (Loi organique relative aux lois de finances, LOLF), Parliament's authorisation must be obtained in the Budget Act for any new guarantee scheme. The legislation must include a precise definition of the guarantee scheme being created. When seeking authorisation from Parliament, the risks incurred must be described exactly, and, according to Constitutional Council precedent, such authorisation is not valid unless there is a guarantee limit or a mechanism to maintain financial control of the scheme. The preliminary assessments submitted are public information.
- Secondly, in conjunction with the other entities concerned during the budget-making process, off balance sheet liabilities are subject to centralised fiscal monitoring at least twice a year to assess the risk of the guarantees being invoked. In addition, more specific information, which is also publicly disclosed, is provided as part of the various draft budgets, along with many reports on specific topics submitted to the Finance Committees of both chambers of Parliament. Some of these reports are also required under the terms of the Budget Act that establishes the guarantee scheme concerned.
- Thirdly, the notes to the Central Government Financial Statements on Central Government Liabilities provide a comprehensive inventory of guarantees given and other off-balance sheet liabilities incurred by the Ministry of Finance in conjunction with the other ministries concerned.

7.3 ONGOING REFORMS TO MEET MAJOR ECONOMIC CHALLENGES

In addition to the fiscal measures set out in this Stability Programme, France is implementing a reform strategy presented in detail in the National Reform Programme. This Programme addresses four main challenges: unleashing the full potential of France's economy; developing tomorrow's growth model; recasting our social model to build a fairer and more mobile society; transforming central government and balancing public finances.

Unleashing the full potential of France's economy

France must be capable of seizing all of the opportunities provided by the growing interconnection of economies and the digital revolution in order to generate long-term growth that is stronger, as well as more sustainable and more inclusive. The government has identified three areas where fundamentally new thinking is needed to unlock growth and job creation: the labour market, taxation and the business environment.

The ordinances on enhancing labour relations, adopted in September 2017, place collective bargaining at the heart of the process, especially at the company level. They also streamline labour relations. The ordinances also provide more security in working relationships, by introducing a fixed

scale for labour tribunal awards. Furthermore, unemployment insurance benefits will be extended to self-employed workers and to workers who resign, subject to certain conditions.

Work has started on streamlining and simplifying our tax system in order to stimulate a shift in our economy to higher end production. This entails cutting the corporate income tax rate to 25% by 2022, replacing the wealth tax with a property wealth tax in 2018 and introducing a single flat-rate levy of 30% for all investment income. The Competitiveness and Employment Tax Credit will be replaced with a permanent cut in social security contributions on 1 January 2019. Finally, the advent of new ecology taxes and tobacco taxes will eliminate some of the distortions in our tax system and provide greater incentives.

The Business Growth and Transformation Action Plan (PACTE) is aimed at promoting businesses' growth so that they can innovate, export and create jobs. It is also aimed at promoting new thinking about businesses social role and giving employees a greater stake in their success. In addition, the government has introduced simplification measures and measures in favour of self-employed workers.

Developing tomorrow's growth model

The government is carrying out a sweeping transformation of France's economic model to address new challenges. This transformation is based on reforms and ambitious investment policies in every sector.

The first priority puts the emphasis on **education and vocational training**:

- On **initial education and access to university** to enable all young people to choose the path to success. The entire education system is under review, from pre-school to university admission.
- On **apprenticeships and vocational training**: the reforms introduced will address the expectations of both employers and employees. In addition, the Investment in Skills Plan will include a €14bn investment in vocational training, especially for the long-term unemployed.

The new economic model will also be built on a **fundamental ecological transformation**. The government's priorities are clear: decarbonising our economy and protecting our health. The objectives are ambitious, such as the end of internal combustion vehicles in 2040, the end of hydrocarbon mining and the gradual elimination of pesticides. At the same time, more than €20bn will be devoted to ecological transition over the government's five-year term.

A massive effort will be made to enhance **France's potential for research and innovation.** An investment of €13bn will be devoted to research and innovation. An Innovation and Industry Fund will be endowed with €10bn to support disruptive innovations.

France's central government will support the critical shift of France's **agricultural** sector to higher end products with a €5bn investment plan. In **transport**, the priority is to improve the day-to-day travel of our citizens. In **housing**, the government's action is aimed at fundamental restructuring of the sector with effective support for boosting housing supply.

Recasting the social model to build a fairer and more mobile society

The government's strategy aims to promote equal opportunities for all, by ensuring real access to essential services and social protection for all, better rewards for merit and a better strategy for fighting poverty.

The primary aim of this strategy is to make government policies in various areas more equitable. This starts with supporting the purchasing power of the least well-off with exemptions from residence tax. In the world of work, this means supporting purchasing power by replacing employees' social security contributions with the more broadly based General Social Security Contribution and by exempting overtime pay from social security contributions. In terms of access to healthcare and preventive care, the national healthcare strategy will focus on lifelong prevention for everyone and will be backed up by the introduction of full insurance coverage for certain types of basic healthcare. Finally, in terms of equity between generations, a systemic pension reform will make our system simpler, more transparent, more predictable and, most importantly, more equitable.

The reform strategy also takes care to ensure that newfound economic growth is inclusive and benefits all local communities, with the Very High Speed Network Plan aimed at providing high-quality mobile coverage for all of France, the plan to fight medical deserts and the city centre revitalisation plan.

A new strategy to fight poverty will be launched in the second quarter of 2018 with greater emphasis on children and young people, reasoning in terms of prevention and social investment starting right from early childhood. Substantial increases in the basic old-age pension and the adult disability allowance will provide support for the most vulnerable population groups. Special measures will also help those with the lowest incomes manage the ecological transition.

Transforming central government and balancing public finances

Public services and the social protection system are at the heart of our Republican pact, but the growing weight of public expenditure leads to a proportionate increase in taxes and social security contributions. At the same time, our increased general government debt is a burden for future generations and restricts our ability to respond in the event of a new economic shock. Therefore, we must reduce our debt.

In addition to introducing simplification measures and a "right to make mistakes", the "Public Action 2022" programme to transform government, which was launched in October 2017, will examine the scope and operation of public policy to identify medium-term structural savings. A fund for central government transformation endowed with €700m over five years will support implementation of a reform programme to ensure the success of these fundamental transformation projects.

The strategy for government transformation presented above will help achieve fiscal consolidation by decreasing the general government deficit and debt significantly, while redeploying government resources where they are most effective and most needed. The aim is to make public policy more agile and responsive to new challenges, while improving service quality for citizens.

8. Institutional aspects and fiscal governance

8.1 FULLY OPERATIONAL FISCAL GOVERNANCE

The Constitutional Bylaw (loi organique) of 17 December 2012 overhauled both public finance steering and its institutional framework. Changes to fiscal management include an introductory article for Budget Acts that supplements public finance steering based on the fiscal balance with targets defined in structural terms and a multi-year outlook. Changes to the institutional framework include the creation of the High Council of Public Finance (Haut Conseil des finances publiques, HCFP), which is tasked with issuing an opinion on the macroeconomic forecasts underlying the Stability Programme, draft budgets and draft social security budgets, and their consistency with the multiyear structural balance guidelines set out in the Public Finance Planning Act. The High Council also identifies potential deviation of the budget outturn from the multiyear forecast during the debate on the draft Budget Review Act. Where appropriate, the High Council may trigger the corrective mechanism in the event of a major deviation or decide whether there are any "exceptional circumstances" that could justify the deviation. The government must take this opinion into account in the draft budget for the year and the draft social security budget for the year and provide details of the corrective measures being planned. The opinions issued by the High Council on these draft budgets include an assessment of these measures.

The High Council provides Parliament, the Constitutional Council and outside observers with an independent assessment of the government's forecasts. It has issued 24 opinions on budget bills and Stability Programmes presented by the government since April 2013.

The findings of the European Commission's assessment of the transposition of the TSCG rules were published in 2017 and highlight the compliance of the architecture established in France with the European rules.

Alongside the new institutional framework, the fiscal rules and targets set out in successive Public Finance Planning Acts in recent years are now an integral part of the overall public finance strategy. The main means used are:

- *For State government:* target for discretionary State government expenditure and aggregate *State government* expenditure target, caps on ministries' expenditure, adjustment path for tax expenditures, ban on real-property financial leasing;
- *For central agencies :* cap on central agencies' expenditure, ban on other central agencies' incurring debt with maturities of more than 12 months, provisions to restrict the number and cap tax earmarks, supervision of public-private partnerships;

- *For local government:* ban on borrowing to cover operating expenditure, target for local government operating expenditure growth (ODEDEL) and contracts with local governments to reduce their deficit by slowing the growth of their real operating expenditure;
- *For social security funds:* national healthcare expenditure growth target (Ondam), adjustment path for reducing administration costs for basic social security schemes under the terms of objectives and management agreements, setting an expenditure target for basic social security schemes, adjustment path to reduce contribution exemptions and rate reductions, monitoring hospital wage bills, cap on social security funds' short-term borrowing.

France's domestic fiscal governance is finally fully integrated within the European procedure. Since the entry into force of the "Two-Pack" Regulation, the European Commission has issued an opinion on Member States' draft budgetary plans (the Economic and Social Report appended to the draft budget) in the autumn of each year. The EcoFin Council then discusses the plans. The Stability Programme is also submitted to the Commission in April, before the European Semester starts. At each of these European deadlines, compliance of each Member State's adjustment path with European recommendations is assessed, in accordance with the provisions of the Stability and Growth Pact.

8.2 STATISTICAL GOVERNANCE

France's national institute of statistics and economic studies (Insee) is responsible for publishing the national accounts, which include the main public finance aggregates in the national accounts format. A new European System of Accounts, ESA 2010, is now in force, replacing ESA 95. It has been applicable to all Member States since September 2014. Insee maintains regular contact with Eurostat to ensure that its accounts are in compliance with the new ESA 2010 rules. In 2018, Insee "rebased" France's national accounts. This rebasing entailed an update of certain items (see Box 3) when the 2017 deficit was estimated.

The **semi-final and final general government accounts**, published with lags of two years and three years respectively, are compiled on the basis of detailed accounting information.[20] The main information source for the central government is the budget outturn, supplemented by the central government's financial statements (accrual-based financial statements, which are certified by the French government audit office (Cour des comptes). Restating the budget outturn as government net lending requires a series of adjustments to correct for some time lags and for the difference in treatment of certain transactions in budgetary cash-based accounting and in the system of national accounts. Compiling the "Other central government bodies" account, which mainly covers central agencies, involves restating each of the agencies' accounts in the national accounts format. The data for the local government sector (APUL) come from the individual management accounts kept by Public Finances Directorate General accountants. The accounts of the social security funds (ASSO) are compiled from the accounts of the various funds, public hospitals and private hospitals providing public healthcare services, the unemployment insurance agency (Unédic) and Pôle Emploi, France's public employment service agency, along with the accounts of complementary retirement scheme management bodies (such as Agirc and Arrco). Insee has revised the social security

[20] This means Insee will publish the semi-final 2016 accounts and the final 2015 accounts in May 2018.

funds accounts every year since September 2013 using supplementary accounting data, ahead of the semi-final accounts.

The data available for the **provisional general government account**, published three months after the end of the year, are still incomplete. The State government's budget cycle ends in mid-January of the following year (y+1) and the central government's public accounts are closed towards the middle of March of the following year (y+1). Consequently, the data published on 25 March of the following year (y+1) are virtually final and any minor revisions made later relate primarily to the adjustments required to bring them into line with the national accounts format. The central agencies' account uses data derived directly from accounting sources that cover approximately two thirds of revenue and expenditure. The preferred sources for local governments are the data reported in the central government's accounting documents and direct, comprehensive and centralised data for regions, départements and municipalities, as well as a sampling of various local government bodies. For the 25 March release, the social security accounts are partially based on estimates, since the different schemes have not yet produced their full financial statements, even though the general social security scheme compiles its financial statements in March. Nevertheless, a large number of accounting data (e.g. from the general social security funds, public hospitals, etc.) are used. The provisional accounts provide a good estimate of the general government balance and revisions to the balance for the final accounts are fairly minor[21].

Maastricht debt is compiled using accounting data from virtually all of the general government sub-sectors, as soon as the provisional accounts are available. The debt of general government sub-sectors is consolidated based on the data gathered directly by the Public Finances Directorate General from the main holders of government securities. The transfer of the accounting data to Insee is governed by an agreement between Insee and the Public Finances Directorate General.

France's Parliament adopted the Economic Modernisation Act in July 2008. Article 144 of this Act enshrines the professional independence of government statisticians, thus ensuring the **independence of statistical output** and government statisticians. The enshrinement of this principle into law was a response to the European Statistics Code of Practice adopted by the Statistical System Committee on 24 February 2005 and reiterated in the European Commission Recommendation of 25 May 2005 on the independence, integrity and accountability of national and Community statistical authorities, which was revised in September 2011. The Code's first principle on professional independence states that the independence of the statistical authorities in producing and disseminating public statistics must be specified in law. To this end, Article 144 created a Public Statistics Authority (Autorité de la statistique publique) responsible for ensuring compliance with the European Statistics Code of Practice. It covers all entities producing public statistics.

[21] France is one of the European Union countries that make the fewest revisions to their general government balance after *the first release. (See European Commission survey: "How reliable are the statistics of the stability and growth pact?", L.G. Mora and J.N. Martins, Economic Papers No. 273, February 2007, European Commission and "Fiscal revisions in Europe" F. Castro, J.J. Pérez and M. Rodriguez-Vives, Journal of Money, Credit and Banking No. 45, September 2013).*

8.3 STATUS OF THIS STABILITY PROGRAMME UNDER INTERNAL PROCEDURES

The Stability Programme was presented to Parliament on 13 April 2018.

In compliance with the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union, the High Council of Public Finance (HCPF) was instituted by the Constitutional Bylaw of 17 December 2012 on public finance planning and governance. Article 17 of the Constitutional Bylaw stipulates that the HCPF shall issue an opinion on the macroeconomic forecasts underpinning this Stability Programme: “The government shall refer the macroeconomic forecasts underpinning the Stability Programme drawn up for the purposes of coordinating the economic policies of the Member States of the European Union to the High Council on Public Finances, which shall make its opinion public at least two weeks before the deadline for submitting the Stability Programme to the Council of the European Union and to the European Commission. This opinion shall be appended to the Stability Programme when it is submitted.”

On 13 April 2018, the High Council of Public Finance published its opinion on the macroeconomic forecasts underlying the Stability Programme for 2018 to 2022. This opinion was appended to the Stability Programme when it was submitted to the Council of the European Union and to the European Commission at the end of April 2018.

9. Appendix

9.1 STATISTICAL TABLES

TABLE 1A. MACROECONOMIC PROSPECTS

	ESA Code	2017*	2017*	2018	2019	2020	2021	2022
		Amount in current € bn	Annual % change	Annual % change	Annual % change	Annual % change	Annual % change	Annual % change
1. Real GDP	B1*g	-	1.8	2.0	1.9	1.7	1.7	1.7
2. GDP growth	B1*g	2,287.4	2.6	3.1	3.1	3.2	3.5	3.5
Components of real GDP								
3. Private consumption expenditure	P.3	1,258.3	1.3	1.6	1.9	1.8	1.8	1.8
4. Government consumption expenditure	P.3	537.5	1.6	0.7	0.2	-0.1	0.2	-0.4
5. Gross fixed capital formation	P.51	513.4	3.8	3.9	3.3	2.3	2.1	2.6
6. Changes in inventories and net acquisition of valuables (% of GDP)	P.52 + P.53	37.2	-	-	-	-	-	-
7. Exports of goods and services	P.6	682.8	3.3	4.9	4.6	4.4	4.4	4.4
8. Exports of goods and services	P.7	739.6	4.1	4.1	4.1	3.7	3.7	3.7
Contributions to real GDP growth								
9. Final domestic demand excluding inventories		-	1.9	1.9	1.8	1.5	1.5	1.5
10. Changes in inventories and net acquisition of valuables	P.52 + P.53	-	0.4	0.0	0.0	0.0	0.0	0.0
11. External balance of goods and services	B.11	-	-0.3	0.1	0.0	0.2	0.2	0.2

* Seasonally and working-day adjusted data taken from the quarterly accounts (March 2018), with the exception of the nominal GDP in 2017, which corresponds to the figure from the March 2018 EDP notification plus real and nominal GDP growth in 2017 (unadjusted data).

TABLE 1B. PRICE DEVELOPMENTS

	ESA Code	2017*	2018	2019	2020	2021	2022
		Annual % change	Annual % change	Annual % change	Annual % change	Annual % change	Annual % change
1. GDP deflator		0.8	1.1	1.2	1.5	1.75	1.75
2. Private consumption deflator		0.9	1.4	1.2	1.5	1.8	1.8
3. CPI		1.0	1.4	1.2	1.5	1.75	1.75
4. Public consumption deflator		0.5	0.4	0.6	1.2	1.3	1.8
5. Investment deflator		1.2	1.4	1.7	1.5	1.9	1.9
6. Export price deflator (goods and services)		1.4	0.9	1.1	1.5	1.6	1.8
7. Import price deflator (goods and services)		2.2	1.0	1.1	1.5	1.6	1.8

TABLE 1C. LABOUR MARKET DEVELOPMENTS

Aggregate economy	ESA Code	2017	2017	2018	2019	2020	2021	2022
		Level	Annual % change	Annual % change	Annual % change	Annual % change	Annual % change	Annual % change
1. Employment, persons employed[1]		27,892	1.0	0.8	0.8	0.8	0.6	0.6
2. Employment, hours worked[2]								
3. Unemployment rate (%)[3]								
4. Labour productivity per person employed[4]		-	0.8	1.2	1.1	0.9	1.1	1.1
5. Labour productivity per hour worked[5]								
6. Compensation of employees (including employers' contributions)	D.1	1215	3.1	3.4	1.2	3.0	3.4	3.5
7. Compensation per employee (including employers' contributions)			2.1	2.6	0.4	2.2	2.8	2.9

[1] Occupied population in thousands, national accounts definition

[2] National accounts definition

[3] ILO concept

[4] Ratio of real GDP growth to employment growth.

[5] Real GDP per hour worked

**Seasonally and working-day adjusted data taken from the quarterly accounts, March 2018.*

TABLE 1D. SECTORAL BALANCES

(% of GDP)	ESA Code	2017*	2018	2019	2020	2021	2022
1. Net lending/borrowing vis-à-vis the rest of the world	B.9	-2.9	-2.9	-2.8	-2.6	-2.4	-2.3
of which							
- Balance on goods and services		-2.5	-2.3	-2.2	-2.0	-1.8	-1.6
- Balance of primary incomes and transfers		-0.5	-0.7	-0.7	-0.7	-0.8	-0.8
- Capital account		0.1	0.1	0.1	0.1	0.1	0.1
2. Net lending/borrowing of the private sector**	B.9	-0.3	-0.6	-0.4	-1.8	-2.2	-2.5
3. Net lending/borrowing of general government***	B.9	-2.6	-2.3	-2.4	-0.9	-0.3	0.3
4. Statistical discrepancy							

**Seasonally and working-day adjusted data taken from the quarterly accounts, March 2018.*

***Calculated for 2017 as the difference between national net lending from the March 2018 quarterly accounts and the public sector net lending from the 2017 notification.*

**** The public sector deficit is based on the GDP figure from the March 2018 notification.*

TABLE 2A. GENERAL GOVERNMENT BUDGETARY PROSPECTS

	ESA Code	2017	2017	2018	2019	2020	2021	2022
		€ bil-lion	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP
Net lending/borrowing (EDP B9) per sub-sector								
1. General government	S.13	-59	-2.6	-2.3	-2.4	-0.9	-0.3	0.3
2. Central government	S.1311	-65	-2.9	-3.1	-3.3	-2.0	-1.6	-1.2
3. State government	S.1312	-	-	-	-	-	-	-
4. Local government	S.1313	1	0.0	0.1	0.1	0.3	0.5	0.7
5. Social security funds	S.1314	5	0.2	0.7	0.8	0.8	0.8	0.8
General government (S.13)								
6. Total revenue	TR	1233	53.9	53.7	52.6	52.4	52.2	52.0
7. Total expenditure	TE	1292	56.5	56.0	54.9	53.3	52.5	51.7
8. Net lending/ borrowing	B.9	-59	-2.6	-2.3	-2.4	-0.9	-0.3	0.3
9. Interest expenditure	D.41	40	1.8	1.7	1.7	1.8	1.9	2.0
10. Primary balance[1]		-19	-0.8	-0.6	-0.6	0.9	1.6	2.3
11. One-off measures[2]		-2	-0.1	-0.3	-1.0	0.0	0.0	0.0
Selected revenue components								
12. Total taxes (12=12a+12b+12c)		681	29.8	30.3	30.4	30.3	30.2	30.0
12a. Taxes on production and imports*	D.2	372	16.3	16.5	16.6	16.6	16.7	16.7
12b. Current taxes on income, wealth, etc.	D.5	294	12.9	13.2	13.2	13.1	13.0	12.8
12c. Capital taxes	D.91	14	0.6	0.6	0.6	0.6	0.6	0.6
13. Social contributions	D.61	431	18.9	18.2	17.0	16.9	16.9	16.9
14. Property income	D.4	15	0.7	0.6	0.7	0.7	0.7	0.7
15. Other[3] (15=16-12-13-14)		105	4.6	4.5	4.4	4.5	4.4	4.4
16=6. Total revenue	TR	1233	53.9	53.7	52.6	52.4	52.2	52.0
NB: Taxes and contributions including tax credits (D.2+D.5+D.61-D612+D.91-D.995)[4]		1067	46.6	46.5	45.5	45.3	45.2	45.0

TABLE 2A CONTINUED. GENERAL GOVERNMENT BUDGETARY PROSPECTS

	ESA Code	2017	2017	2018	2019	2020	2021	2022
		€ billion	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP
Selected expenditure components								
17. Compensation of employees + intermediate consumption	D.1 + P.2	404	17.7	17.3	17.0	16.7	16.4	16.1
17a. Compensation of employees	D.1	290	12.7	12.5	12.3	12.1	11.9	11.7
17b. Intermediate consumption (including financial intermediation)	P.2	114	5.0	4.8	4.7	4.6	4.5	4.4
18. Social benefits (18=18a+18b)		591	25.9	25.5	25.1	24.8	24.5	24.1
of which unemployment benefits		34	1.5	1.4	1.4	1.4	1.3	1.3
18a. Social transfers in kind supplied via market producers	D.632	139	6.1	6.0	5.8	5.8	5.7	5.6
18b. Social transfers other than in kind	D.62	452	19.8	19.5	19.3	19.0	18.8	18.6
19=9. Interest expenditure	D.41	40	1.8	1.7	1.7	1.8	1.9	2.0
20. Subsidies	D.3	59	2.6	2.8	2.6	1.8	1.7	1.7
21. Gross fixed capital formation	P.51	77	3.4	3.5	3.5	3.4	3.3	3.2
22. Capital transfers	D.9	31	1.4	1.3	1.0	1.0	1.0	0.9
23. Other[6] (23=24-17-18-19-20-21-22)		89	3.9	4.0	4.0	3.9	3.8	3.8
24=7. Total expenditure	TE1	1292	56.5	56.0	54.9	53.3	52.5	51.7
NB: Government consumption (nominal)	P.3							

1. The primary balance is calculated as (B.9, item 8) plus (D.41, item 9).
2. A plus sign denotes deficit-reducing one-off measures.
3. P.11+P.12+P.131+D.39+D.7+D.9
4. Including those collected by the European Union and including an adjustment for uncollected taxes and social contributions (D.995).
5. Includes cash benefits (D.621 and D.624) and in-kind benefits (D.631) related to unemployment benefits.
6. D.29+D.4-D.41+D.5+D.7+P.52+NP
*Excluding taxes collected by the European Union

TABLE 2B. NO-POLICY-CHANGE PROJECTIONS

	2017	2017	2018	2019	2020	2021	2022
	Level	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP
1. Total revenue with no policy change	1232.6	53.9	53.5	53.7	53.8	53.7	53.6
2. Total expenditure with no policy change	1292.0	56.5	56.1	55.6	55.3	55.1	54.8

TABLE 2C. AMOUNTS TO BE EXCLUDED FROM THE EXPENDITURE BENCHMARK

	2017	2017	2018	2019	2020	2021	2022
	in € billion	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP
1. Expenditure on EU programmes fully matched by EU funds revenue	1.9	0.1	0.1	0.1	0.1	0.1	0.1
2. Cyclical unemployment benefit expenditure	1.0	0.0	0.0	0.0	0.0	-0.1	-0.1
3. Effect of discretionary revenue measures	5.4	0.2	-0.1	-1.1	-0.1	0.0	-0.1
4. Revenue increases mandated by law	-	-	-	-	-	-	-
Memorandum items (*):							
One-off revenue (ESA 2010)	3.5	0.2	0.0	0.0	0.0	0.0	0.0
One-off expenditure (ESA 2010)	5.4	0.2	0.3	0.9	0.0	0.0	0.0

(*) Methodological Annex

TABLE 3. GENERAL GOVERNMENT EXPENDITURE BY FUNCTION

% of GDP	COFOG code	2016
1. General public services	1	6.1
2. Defence	2	1.8
3. Public order and safety	3	1.6
4. Economic affairs	4	5.6
5. Environmental protection	5	0.9
6. Housing and community amenities	6	1.1
7. Health	7	8.1
8. Recreation, culture and religion	8	1.2
9. Education	9	5.4
10. Social protection	10	24.4
11. Total expenditure	**TE**	**56.4**

NB: latest available data from Insee by COFOG codes, which are not yet consistent with the update of the 2017 accounts released in March 2018.

TABLE 4. GENERAL GOVERNMENT DEBT

% of GDP	ESA Code	2017	2018	2019	2020	2021	2022
1. Gross debt[1]		97.0	96.4	96.2	94.7	92.3	89.2
2. Change in gross debt ratio		0.4	-0.5	-0.2	-1.5	-2.4	-3.1
Contributions to changes in gross debt ratio							
3. Primary balance[2]		-0.8	-0.6	-0.6	0.9	1.6	2.3
4. Interest expenditure[3]	D.41	1.8	1.7	1.7	1.8	1.9	2.0
5. Stock-flow adjustment		0.3	0.1	0.3	0.6	0.5	0.2
of which							
- differences between cash and accruals[4]							
- net accumulation of financial assets[5]							
- privatisation proceeds							
- valuation effects and other[6]							
Memo: Implicit interest rate on debt[7]		1.9	1.8	1.8	1.9	2.1	2.2
Other relevant variables							
6. Liquid financial assets[8]							
7. Net financial debt (7=1-6)							
8. Debt amortization							
9. Percentage of debt denominated in foreign currency							

1 As defined in Regulation 3605/93 (not an ESA concept).

2. See item 10 in Table 2.

3. See item 9 in Table 2.

4. The differences concerning interest expenditure, other expenditure and revenue may be posted here where material or if the debt-to-GDP ratio is above the reference value.

5. Liquid assets (currency), government securities, assets on third countries, government controlled enterprises and the difference between quoted and non-quoted assets may be posted here where material or if the debt-to-GDP ratio is above the reference value.

6. Changes due to exchange rate movements and operations in secondary markets may be posted here where material or if the debt-to-GDP ratio is above the reference value.

7. Calculated as the ratio of gross interest expenditure to gross outstanding debt on 31 December of the previous year.

8. FA1, FA2, FA3 (consolidated at market value), FA511 (listed equities), FA52 (mutual fund units or shares)

TABLE 5. CYCLICAL AND STRUCTURAL DEVELOPMENTS

(% of GDP)	ESA Code	2017*	2018	2019	2020	2021	2022
1. Real GDP growth (in %)		1.8	2.0	1.9	1.7	1.7	1.7
2. General government balance	B.9	-2.6	-2.3	-2.4	-0.9	-0.3	0.3
3. Interest expenditure	D.41	1.8	1.7	1.7	1.8	1.9	2.0
4. One-off measures[1]		-0.1	-0.3	-1.0	0.0	0.0	0.0
5. Potential GDP growth (%) (g)		1.25	1.25	1.25	1.25	1.3	1.35
Contributions to potential growth:							
- labour		0.1/0.2	0.1/0.2	0.1/0.2	0.1/0.2	0.1/0.2	0.1/0.2
- capital		0.4/0.5	0.4/0.5	0.4/0.5	0.4/0.5	0.4/0.5	0.4/0.5
- total factor productivity		0.6/0.7	0.6/0.7	0.6/0.7	0.6/0.7	0.6/0.7	0.6/0.7
- effect of structural reforms		-	-	-	-	0.05	0.1
6. Output gap		-0.9	-0.2	0.4	0.9	1.3	1.6
7. Cyclical balance		-0.5	-0.1	0.2	0.5	0.7	0.9
8. Cyclically-adjusted balance (8=2-7)		-2.1	-2.2	-2.6	-1.4	-1.0	-0.6
9. Cyclically-adjusted primary balance (9=8+3)		-0.3	-0.5	-0.9	0.4	0.9	1.4
10. Structural balance (10=8-4)		-2.0	-1.9	-1.6	-1.4	-1.0	-0.6

[1]A plus sign denotes deficit-reducing one-off measures.

TABLE 6. DIVERGENCE FROM PREVIOUS UPDATE

	ESA Code	2017	2018	2019	2020	2021	2022
Real GDP growth							
Previous programme (2016-2019)		1.5	1.5	1.6	1.7		
Current programme (2017-2020)		1.8	2.0	1.9	1.7	1.7	1.7
Difference		0.4	0.6	0.3	0.0		
General government net lending (% of GDP)							
Previous programme (2016-2019)	B.9	-2.8	-2.3	-1.6	-1.3		
Current programme (2017-2020)	B.9	-2.6	-2.3	-2.4	-0.9	-0.3	0.3
Difference	B.9	0.2	0.0	-0.8	0.4		
General government debt (% of GDP)							
Previous programme (2016-2019)		96.0	95.9	94.7	93.1		
Current programme (2017-2020)		97.0	96.4	96.2	94.7	92.3	89.2
Difference		1.0	0.5	1.5	1.7		

TABLE 7. LONG-TERM SUSTAINABILITY OF PUBLIC FINANCES*

% of GDP	2016	2020	2040	2050	2060	2070
Total expenditure						
of which age-related expenditure	**31.0**	**30.9**	**31.5**	**30.3**	**29.0**	**28.0**
Pension expenditure	15.0	15.0	15.1	13.8	12.5	11.8
of which social security pension						
of which old-age and early pensions						
of which other pensions (disability, survivors)						
of which occupational pensions (if in general government)						
Healthcare expenditure	7.9	8.0	8.4	8.4	8.4	8.3
Long-term care	1.7	1.8	2.3	2.4	2.4	2.4
Education expenditure	4.8	4.7	4.6	4.6	4.5	4.4
Other age-related expenditure (unemployment benefits)	1.6	1.4	1.2	1.2	1.2	1.2
Interest expenditure						
Total revenue						
of which property income	0.7	0.7	0.6	0.6	0.6	0.6
of which pension contributions (or social contributions if appropriate)						
Pension Reserve Fund assets						
of which consolidated public pensions fund assets (assets other than government liabilities)						
Systemic pension reforms[1]						
Social contributions paid to private compulsory pension schemes[2]	:	:	:	:	:	:
Pension expenditure paid by private compulsory pension schemes[3]	:	:	:	:	:	:
Assumptions						
Labour productivity growth	:	:	:	:	:	:
Real GDP growth	:	:	:	:	:	:
Participation rate males (aged 20-64)	:	:	:	:	:	:
Participation rate females (aged 20-64)	:	:	:	:	:	:
Total participation rates (aged 20-64)	:	:	:	:	:	:
Unemployment rate	:	:	:	:	:	:
Share of population over 65 years old	:	:	:	:	:	:

1. Systemic pension reforms refer to reforms that introduce a switch to a multi-pillar system, including a compulsory fully-funded pillar.

TABLE 7A. CONTINGENT LIABILITIES

% of GDP	2015	2016
Government guarantees*	8.4	8.7
of which granted to the financial sector	-	-

**These are guarantees granted by the central government in budget acts under clear-cut agreements.*

TABLE 8. BASIC ASSUMPTIONS

	2017	2018	2019	2020	2021	2022
Short-term interest rate (annual average)[1]	-0.3	-0.1	0.7	1.4	2.0	2.4
Long-term interest rate (annual average)[2]	0.8	1.1	2.0	2.8	3.4	3.8
USD/€ exchange rate (annual average)	1.13	1.23	1.23	1.23	1.23	1.23
Nominal effective exchange rate	1.1	2.5	0.0	0.0	0.0	0.0
Global GDP growth excluding EU[3]	4.0	4.1	4.1	4.1	4.2	4.2
EU GDP growth[3]	2.4	2.3	2.0	1.8	1.7	1.7
World demand for French goods	5.1	5.0	4.7	4.4	4.4	4.4
World import volumes excluding the EU	5.2	5.2	4.7	n.a.	n.a.	n.a.
Oil prices (Brent, USD/barrel)	55	65	65	65	65	65

[1]Euribor 3-month rate

[2]Yield on 10-year French Treasury bonds.

[3]The growth forecasts for 2020 and 2022 are taken from the October 2017 World Economic Outlook by the IMF.

9.2 METHODOLOGICAL ANNEX: CALCULATING STRUCTURAL ADJUSTMENT AND THE EXPENDITURE BENCHMARK

Role of potential growth

Potential GDP is the level of output that can be sustained without straining factors of production and, more specifically, without putting pressure on prices and wages. This notion is used to guide the conduct of fiscal policy (medium-term growth) and monetary policy (inflation risk). Unlike GDP or inflation, **potential growth cannot be observed so it must be estimated**.

There are different methods for estimating potential growth. The first estimates potential GDP directly, using a filter. The second, more economics-based, method uses a production function that breaks GDP down into its different components (labour, capital, productivity). The latter method is generally used by international organisations and for the Public Finance Planning Act. This means that differences in the estimates stem from the different treatment applied to each component.

Structural balance

The value of the structural balance lies in the fact that it strips out the part of the general government balance that depends directly on cyclical developments. This makes it possible to measure the impact of policies on the fiscal balance, as distinct from the impact of cyclical developments. **Therefore, calculating the structural balance relies intrinsically on the definition of the business cycle and, accordingly, the gap between GDP and potential GDP.** More specifically, we observe that revenue is lower and expenditure is higher (particularly expenditure on unemployment benefits) when GDP is below its potential and, inversely, that revenue goes up and expenditure goes down when GDP is higher than its potential level.

The general government balance for each year can be broken down into:

- **a cyclical component** that captures the impact of the business cycle stage on the general government balance, i.e. the different revenue and expenditure items affected by the business cycle;
- **a structural component** that corresponds to an estimate of what the balance would be if GDP were equal to its potential;
- **one-off measures**, which have no lasting impact on the deficit and are therefore excluded from the assessment of the structural balance.

On the **expenditure** side, only expenditure on unemployment benefits is assumed to be cyclical. All other expenditure is assumed to be structural at every point in the cycle, either because it is discretionary, or because its relationship to the business cycle is difficult to measure.

On the **revenue** side, we assume that all taxes and contributions have a cyclical component, whereas other revenue (e.g. interest and dividends) is assumed to be non-cyclical.

We quantify the components of the cyclical balance **on the basis of average historical elasticities (called conventional elasticities)** of these expenditure and revenue items to the output gap. The

elasticities are based on an econometric estimate made by the OECD.[22] Revenue is broken down into four categories of taxes and contributions (personal income tax, including the General Social Security Contribution, corporate income tax, social contributions and other taxes and contributions) since the reaction of the tax bases to cyclical changes can vary greatly depending on the tax under consideration. **On average, the aggregate conventional tax elasticity is very close to one.**

The elasticities of the taxes and contributions under review are presented in Table 1.[23] They were updated in 2014.

TABLE 1. SEMI-ELASTICITIES TO THE OUTPUT GAP

Personal income tax + General Social Security Contribution (CSG)	1.9
Corporate income tax	2.8
Social contributions	0.6
Indirect taxes	1.0
Unemployment benefit expenditure	-3.2

Source: OECD 2014

In practice, France's cyclical balance is a bit more than half of the difference between actual GDP and potential GDP. This is because cyclical items account for about half of France's GDP and the average tax elasticity is about 1.

The variation in the general government balance, therefore, results from the variation attributed to cyclical changes, structural adjustment and the impact of one-off measures. Structural adjustment itself is the result of a structural effort, which measures the discretionary component of the balance controlled directly by the government and a "non-discretionary" component (see below).

[22] See "New tax and expenditure elasticity estimates for EU budget surveillance", by R.W.R Price, T. Dang and Y. Guillemette, OECD Economics Department Working Papers No. 1174 2014.
[23] More precisely, the semi-elasticity to the output gap.

BOX 10 - STRUCTURAL BALANCE

Y denotes actual GDP and Y* denotes potential GDP.

For each category of taxes and contributions R, the structural component R_s can be written as a function of the conventional elasticity θ to the output gap (see Table 1):

$$R_S = R\left(\frac{Y^*}{Y}\right)^{\theta}$$

Therefore, the aggregate structural revenue is obtained as the sum of structural revenue, calculated as R_s (for the four categories of cyclical taxes and contributions: personal income tax, including the General Social Security Contribution, corporate income tax, social contributions and other taxes and contributions), and the rest of revenue.

Structural expenditure is obtained as the difference between actual expenditure and cyclical expenditure on unemployment benefits, denoted D_{Ccho}. Structural expenditure on unemployment benefits is determined in the same way as structural revenue, as a function of the conventional elasticity of expenditure on unemployment benefits to the output gap.

$$D_s^{cho} = D^{cho}\left(\frac{Y^*}{Y}\right)^{\varepsilon}$$

The difference between structural expenditure and structural revenue is the structural balance S_s. Finally, the ratio of the structural balance to potential nominal GDP is adjusted by the GDP deflator.

Structural effort

The structural balance needs to be supplemented with another public finance analysis tool: structural effort

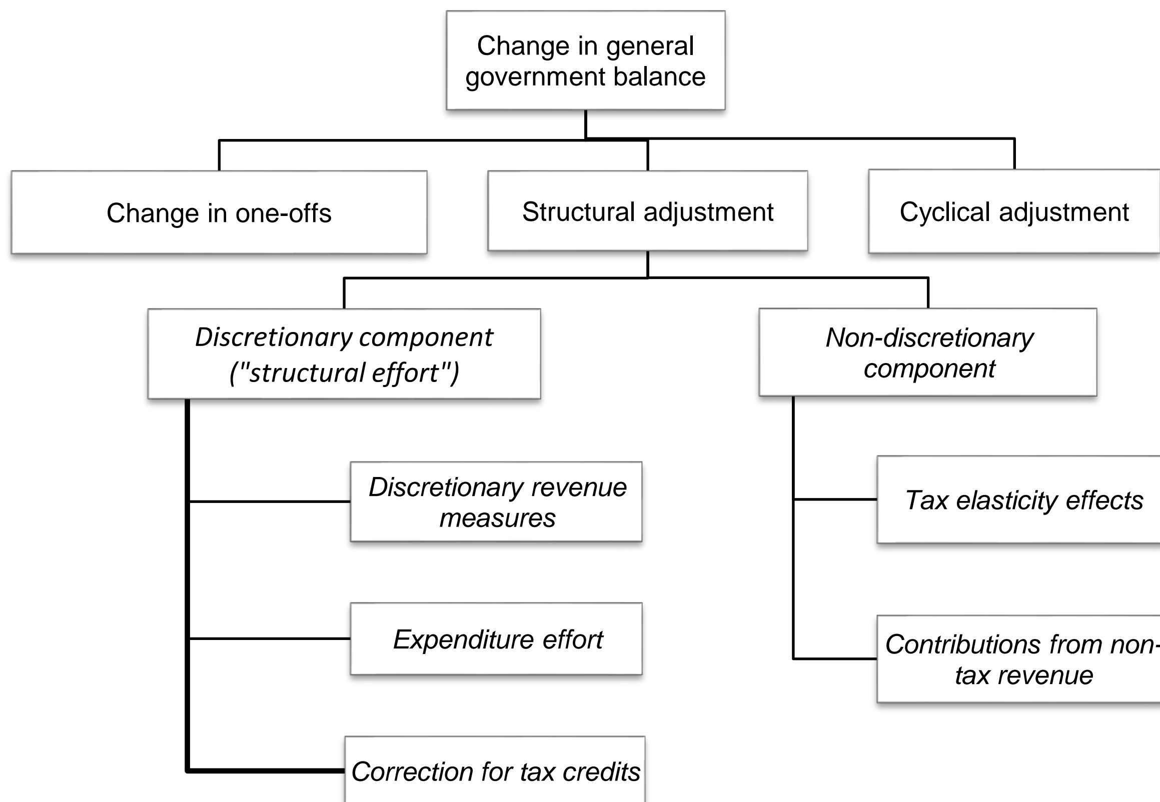
Each year, the (instantaneous) actual tax elasticities to cyclical changes fluctuate around their historical mean. Some of the fluctuations are significant. For example, in 2009, tax revenue, especially revenue from corporate income tax, dipped in an over-reaction to cyclical changes. In practice, the differential between instantaneous elasticity and conventional elasticity is passed on in full in variations in the structural balance, even though the differential corresponds to a non-discretionary component of variations in the general government balance. This means that it is beyond the control of policy-makers and yet it is still incorporated into the structural balance. Furthermore, Insee's revisions of actual growth figures may entail revisions of structural adjustment up to three years later.

To mitigate these limitations, the structural effort corresponds to the variation of the structural balance that can be attributed to discretionary factors.

Furthermore, the accounting conventions of ESA 2010[24] introduced in 2014, change the treatment of refundable tax credits. Tax credits reduce taxes and social security contributions by an amount equivalent to their impact on tax revenue (meaning allocations and refunds actually granted to businesses and households), but the outstanding claims acquired by taxpayers contribute to the general government balance under the accruals accounting principle. An additional term is used in

[24] See the Insee document from May 2014: "Les comptes nationaux passent en base 2010".

this decomposition to maintain the same revenue effort and maintain its consistency with the concepts of aggregate tax and social security contribution rate and discretionary measures, which recognise tax credits as reduced revenue, as well as the expenditure effort, excluding tax credits. This term is the variation in the discrepancy between the fiscal cost and the national accounts cost of refundable tax credits (in practice, this means the Competitiveness and Employment Tax Credit and the Research Tax Credit). When the fiscal cost (under discretionary revenue measures) of the claims is less than the cost recorded in the national accounts (which affects the general government balance), this item reduces the structural effort. Conversely, when the fiscal effort measured as a revenue effort is greater than the accrued effort recorded in the national accounts, this item increases the structural effort. The correction for accrual-based measurement of tax credit refunds has been incorporated into the structural effort item in the decomposition of structural adjustment since the 2018-2022 Public Finance Planning Act. The new decomposition is warranted by the replacement of the Competitiveness and Employment Tax Credit and it will smooth its impact on structural effort without requiring any further restatement of data.



Therefore, the **variation in the structural balance** can be broken down into:

- A discretionary component called “structural effort”;
- A non-discretionary component.

The **structural effort** can then be broken down into a revenue effort (discretionary tax and contribution measures), an expenditure effort (net of tax credits) and the correction for accrual-based measurement of tax credits.

- **Discretionary revenue measures** are decided and implemented by the government authorities.
- **Expenditure effort** is measured in relation to potential growth: an expenditure effort implies that real structural spending growth (adjusted by the GDP deflator) is lower than potential growth, and vice-versa.
- **The correction for accrual-based measurement of tax credits** makes it possible to switch from the fiscal measurement of tax credits as reduced revenue, which is included in the revenue effort, back to an accruals-based measurement.

The non-discretionary component of the variation in the structural balance corresponds to two terms:

- **The contribution of non-tax revenue**, which is assumed to be non-discretionary (equal to the variation in the ratio of non-tax revenue, excluding one-offs, to potential GDP).
- **"Tax elasticity effects"**, which measure the impact of the differential between the instantaneous and conventional tax elasticities to the output gap.

Expenditure benchmark

A supplementary indicator was introduced to make the structural adjustment target more operational. The idea of the expenditure benchmark is to measure the Member States' efforts using an aggregate under the direct control of the government, in contrast to the headline general government balance, which is affected by the business cycle and other non-discretionary factors. Annex 8 of the Vade mecum on the Stability and Growth Pact explains how to calculate the expenditure benchmark.

For this purpose, **discretionary revenue measures and one-offs used for the expenditure benchmark are not the same as those used for the structural analysis of the deficit.** The revenue effort and the expenditure effort presented in the structural analysis are based on treating tax credits as reductions in revenue, which makes it possible to show discretionary revenue measures: expenditure is shown excluding tax credits and discretionary revenue measures include refundable tax credits, as is the case for the discretionary revenue measures presented in the Statistical Appendix. The correction for accrual-based measurement of tax credits makes it possible to recognise the claims acquired through tax credits as expenditure, instead of recognising the refunds as a reduction in revenue so that the general government balance is estimated under the ESA 2010 rules, where tax credits constitute public expenditure.

The discretionary revenue measures used to offset an increase in the expenditure aggregate do not include refunds of tax credits, since the expenditure benchmark is based on the expenditure aggregate in ESA 2010. The expenditure aggregate includes tax credit expenditure and is therefore different from the expenditure effort. Under the expenditure benchmark, an increase in tax credits is treated as an increase in expenditure and has no effect on discretionary revenue measures. Tax credit one-offs related to the replacement of the Competitiveness and Employment Tax Credit and included in the expenditure benchmark aggregate are presented as expenditures in order to maintain consistency with the replacement of the tax credits in 2019.

9.3 ADJUSTMENT PATH UNDER THE NO-POLICY-CHANGE SCENARIO AND TREND PATH

This Stability Programme presents a "no-policy-change" scenario, in accordance with the European Council Directive of 8 November 2011. This is a contra-factual scenario for 2018-2022 presenting what would have happened in the absence of the measures taken by the government. The following assumptions underlie this scenario:

- No further discretionary revenue measures are introduced after September 2017, meaning that the effects of the revenue measures passed since the 2018 Budget Act would be eliminated.
- Real expenditure growth is assumed to remain at the average rate for the last ten years (i.e. 1.2% growth per year).

TABLE 1: NO-POLICY-CHANGE PATH

as percentage of GDP	2017	2018	2019	2020	2021	2022
General government deficit under no policy change scenario	**-2.6**	**-2.6**	**-1.9**	**-1.5**	**-1.4**	**-1.2**
General government debt under no policy change scenario	**97.0**	**96.7**	**96.1**	**95.2**	**93.9**	**92.2**
Expenditure, excluding tax credits		0.3	0.7	1.3	1.8	2.3
Discretionary revenue measures announced (*)		0.0	-1.2	-0.7	-0.7	-0.8
Stability Programme general government balance	**-2.6**	**-2.3**	**-2.4**	**-0.9**	**-0.3**	**0.3**
Stability programme general government debt	**97.0**	**96.4**	**96.2**	**94.7**	**92.3**	**89.2**

(*) including the net contribution of tax credits to revenue and expenditure

In 2018, the no-policy-change scenario would correspond to a deficit of 2.6% of GDP. The expenditure effort makes it possible to reduce the expenditure ratio by 0.3% of GDP. Without these measures, the debt ratio would stand at 96.7% of GDP.

In 2019, the no-policy-change scenario would produce a deficit of 1.9% of GDP. The target path includes savings of 0.7 points in the ratio of expenditure, excluding tax credits, to GDP. On the other hand, expenditure measures carry a cost equivalent to 1.2 percentage points of GDP, with the replacement of the Competitiveness and Employment Tax Credit. In this case the "no-policy-change" deficit would temporarily exceed the target path in the Stability Programme.

In the years from 2020 to 2022, this effect will fade as the double cost of replacing the Competitiveness and Employment Tax Credit comes to an end. The "no-policy-change" deficit would stand at 1.2% of GDP in 2022, compared to 0.3% on this path. The debt-to-GDP ratio would stand at 92.2%, compared to 89.2% on the Stability Programme path.

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