FRANCE

STABILITY PROGRAMME 2013-2017

April 2013

Contents

1. Outline

Action by Governments and the European Central Bank (ECB) has eased fears about the future of the euro, but the recovery of the real economy still has not started. Since June, Governments have taken initiatives to promote growth (Growth Pact) and greater integration of the euro area (banking union), and the ECB has announced new measures as well. Despite the gradual strengthening of investor confidence, Europe's domestic demand is still depressed as a result of the on-going process to reduce public and private debt and the slowdown in world trade. In countries facing tensions, the effects of accommodative monetary policy are not being fully transmitted to the real economy and financing terms for private economic agents are still tight. The unemployment rate in the euro area has reached its highest level since the introduction of the single currency.

However, the situation of the euro area as a whole is similar to that of other areas in the global economy, and even better in many cases, as regards government and private debt. European and national initiatives to promote sustainable improvements in growth and jobs are paving the way for a gradual recovery starting in the second half of 2013. The effects of the Growth Pact, of the emerging banking union, of stabilisation actions in countries in crisis and of the European Central Bank's new instruments will be felt gradually. At the same time, the Member States have committed themselves to implementing policies to balance their current accounts, by improving competitiveness in countries with current account deficits and by boosting domestic demand in countries with current account surpluses.

This gradual recovery is what international organisations and the European Commission are expecting. In France, the average annual growth rate should remain low in 2013, because of weak growth at the end of 2012 and a poor start to the year in 2013, but it should gather strength in the coming months, and the economy should start creating jobs again in the second half of 2013, bringing the unemployment rate down again towards the end of the year. **The Government predicts that gross domestic product (GDP) will grow by an annual average of 0.1% in 2013, followed by 1.2% in 2014 and then 2.0% per year, starting in 2015.** The recovery will stem from an improvement in the international environment and the effects of reforms implemented by the Government to promote jobs and competitiveness.

The Government's objective is to implement ambitious structural reforms to foster stronger, more balanced and more inclusive growth. Restoring the competitiveness lost over the last ten years will require lower labour costs and support for productive investment: business finance reform, streamlining regulations, tax reform to favour SMEs and intermediate-sized enterprises, as well as innovation, sector reforms to stimulate the growth of priority sectors. Fighting unemployment, job insecurity and inequality calls for both urgent measures to support the purchasing power of the least well-off and sweeping reforms to reduce labour market segmentation, improve job security, promote jobs for young people and older workers, make job training more effective and promote gender equality at work.

The strategy to consolidate government finances presented in this Stability Programme will contribute to achieving this goal of economic recovery. The strategy is based on the principles of social justice and economic efficiency. It aims to underpin domestic demand in the short term while maintaining potential growth in the long term through a large-scale modernisation of public action.

Starting in May 2012, France's new Government made the necessary decisions to honour the commitments that had been made, whereas the previous measures had not been sufficient to ensure that these commitments would be met. The Government implemented structural adjustment on an unprecedented scale with the amended 2012 Budget Act in July and with the Initial Budget Act and Social Security Budget Act for 2013. The government deficit was reduced to 4.8% of GDP in 2012, following a deficit of 5.3% in 2011, despite zero growth. This represents a structural adjustment of 1.2 point of GDP, as scheduled in the multiyear Public Finance Planning Act.

In 2013, structural effort should be equal to 1.9 point of GDP, as scheduled in the multiyear Public Finance Planning Act. In the four years from 2010 to 2013, France will have achieved structural adjustment of 4.6 points of GDP, with two-thirds of the progress being made in the last two years. With the sharp deterioration of the economic outlook for 2013, the nominal government deficit should stand at 3.7% of GDP in 2013. If France adopted further measures, it would tip into recession while the euro area is on average already in a recession. For this reason, the French Government has argued to its partners that its efforts should be acknowledged and that the return to a nominal deficit of less than 3% of GDP should be deferred until 2014.

The government deficit will then be lowered to 2.9% of GDP in 2014 by means of a structural effort estimated at 1.0 point of GDP, followed by structural equilibrium in 2016. After primarily relying on increases in revenue in 2012 and 2013, the Government will focus adjustment efforts on expenditure savings in 2014 and beyond, making sure that it improves government expenditure efficiency. This is a valid strategy in a difficult economic context. Furthermore, the most recent and in-depth studies of the impact of fiscal consolidation on growth show that increasing government revenues is less harmful for growth and jobs in the short term, while the most sustainable adjustments that do the most to boost growth in the medium term are adjustments that rely on curbing government expenditure and making government management more efficient.

Maintaining the structural balance trajectory will require efforts by all subsectors of general government. The French Government has initiated an ambitious endeavour to modernise public action with the objective of evaluating all of the public policies implemented by the various Government departments and agencies by 2017. The process will rely on a close partnership with the users and agents of these policies to determine their effectiveness. This will promote ownership of the process and its success, thereby contributing to the containment of government expenditure. Central government expenditure, excluding debt and pensions, will decrease by €1.5 billion in 2014, while expenditure on the Government’s priorities of promoting jobs and fighting poverty is financed by redeploying resources. Grants to local governments will be reduced by €1.5 billion in 2014, and then by another €1.5 billion in 2015. Social security funds will also take part in the effort to contain government expenditure. In addition to the efforts already announced on health insurance, employers’ and labour representatives have reached an agreement on supplementary pension schemes that will help consolidate public finances and these parties will renegotiate the agreement on unemployment insurance by the end of 2013. Work has also started to achieve equilibrium of the old-age pensions and family benefits sections of the social security system in the medium term (Fragonard Task Force and Moreau Commission). Measures regarding the tax burden will be taken to offset the declining return in 2014 from the measures introduced in 2013, which has already been embedded into the trajectory used for the Multiyear Public Finance Planning Act. These measures will also offset the lower-than-expected revenue from the Tax on Financial Transactions and the measures overturned by France's Constitutional Council. They will reduce tax exemptions, in line with the objective of stabilising such exemptions in nominal terms set out in the Multiyear Public Finance Planning Act, and step up the fight against tax fraud and evasion.

The strategy to consolidate public finances also relies on renewed governance. The Constitutional Bylaw of 17 December 2012 on public finance planning and governance, which establishes a management of public finances through the structural balance, sets up a correction mechanism to remedy significant deviations from the multiyear structural balance trajectory set out in the Public Finance Planning Act for 2012 to 2017. An independent body, the High Council on Public Finances, is now responsible for producing a public notice concerning its opinion of macroeconomic forecasts underlying the budget bill and social security finance bill as well as on the consistency of the bills with the structural balance trajectory contained in the Public Finance Planning Act. The macroeconomic forecasts underlying this Stability Programme have been submitted to the High Council for its opinion.

2. Macroeconomic scenario

2.1 Situation in 2012

France's economy was affected by worsening conditions in the international environment in 2012, but it did better than the euro area as a whole, posting 0.0% growth versus a decline of 0.5%[1].

After a recovery in 2010, the global economy slowed in 2011 and 2012, at first because of rising commodity prices and the earthquake in Japan, then, during the third quarter of 2011, because of bad news from the United States, with a downwards revision of growth estimates and the downgrade of the country's sovereign credit rating. In addition to these factors, there were specifically European developments: growing fears about sovereign debt and the future of the euro in the third quarter of 2011, combined with synchronised tightening of fiscal policies.

In this gloomy international environment, France's economic growth slowed sharply in the third quarter of 2011 and was stagnant in 2012.

French exports slowed down significantly, but the dip was smaller than the decline in global demand for French exports, in particular thanks to the depreciation of the euro in 2011 and early 2012.

Weak export markets and a poor outlook for demand caused firms to draw down their inventories and cut back their investment slightly, despite an easing of financial tensions following statements by the Governor of the European Central Bank in July 2012. However, on the whole, France's business investment was firmer than in most of the other leading euro-area countries.

Household consumption did not slip, despite job cuts and higher unemployment, which affected purchasing power. The sluggishness of consumption and the decline in the savings rate in the second half of the year stem from support measures for the most vulnerable households and tax hikes that target the most well-off households. The slight increase in average annual investment in housing actually obscures a downturn in the construction market at the start of the year.

2.2 Outlook for 2013 and 2014

As the euro-area recession persists in 2013, France's growth would remain flat at 0.1%.

After a particularly difficult winter, France's economy should gradually start to recover, according to the forward-looking indicators from business surveys, but job growth will not resume until the second half of the year.

The initial economic data available for the first months of 2013 point to an improvement in the international environment for the euro area, particularly in the United States and Japan. Yet, these external sources of growth are unlikely to be enough to bring the euro area out of the recession in the very short term. The adjustment of private-sector balance sheets in troubled economies and fiscal consolidation will continue to affect the euro area economy, with an aggregate structural adjustment of nearly one point of GDP in 2013. The ECB's continuing accommodative monetary policy is not being fully transmitted to the real economy because of the efforts to clean up banks' balance sheets in some vulnerable countries. All in all, global demand for French exports should pick up only gradually in 2013.

Renewed economic growth in France in the second half of the year should be driven by an improving international environment and by Government measures to boost jobs, competitiveness and housing construction, especially in the social housing sector.

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[1] Data adjusted for working days.

Export sales should become firmer again, with measures to support exporting industries and the early effects of the National Pact for Competitiveness, Growth and Jobs. Business investment should take off again gradually over the year, with brighter prospects for markets, measures to support short-term financing for businesses (Cash Plan, pre-financing of the Competitiveness and Jobs Tax Credit – CICE, etc.) and streamlined regulations. However, average annual business investment is still likely to decrease slightly because of the downturn at the end of 2012. Inventories should continue to make a negative contribution to growth for the year as a whole, but, once again, primarily because of a carryover effect, following drawdowns at the end of 2012.

The French economy should start creating jobs again in the second half of the year, and the unemployment rate should start decreasing again in the last quarter, as growth gradually resumes and the effects of the many measures to boost jobs introduced over the last ten months start to be felt. These measures include such initiatives as the Jobs for the Future, Generation Contracts, the Competitiveness and Jobs Tax Credit and the National Inter-Sector Agreement on Job Security. However, average annual employment should fall slightly. Wage growth should also slow down with high unemployment and lower inflation, which is expected to stand at 1.3%[2] for 2013. This means growth of competitive sector payrolls should slow from 1.8% in 2012 to 1.3% in 2013. The carryover effect from the end of 2012 should cause average annual purchasing power to post a further slight decline in 2013. However, the automatic stabilisers should mitigate the impact of slower payroll growth and tax hikes on households, since the hikes are more closely targeted on the most well-off households than those introduced in 2012. Household consumption should also be boosted by a decline in the savings rate, helped by the composition of fiscal adjustment and the return of confidence. Households' investment in housing in 2013 is likely to be held back by the decline in housing starts seen in 2012, given the time it takes to complete construction. However, the emergency housing investment plan should make a significant contribution to reversing the trend over the year.

The recovery will start to take root in 2014 (+1.2%).

Growth should be sustained by the Government's structural reforms and the pick-up in global demand for French exports, which should grow by 6.5%.

The impact of continuing consolidation of public finances in France and in much of Europe on aggregate demand will probably be offset to some extent by efforts to correct imbalances and support domestic demand in countries with current account surpluses, in compliance with the new Macroeconomic Imbalance Procedure.

Business investment should pick up again as the international environment improves and companies should stabilise their market shares in global competition thanks to business financing reform, with the creation of the Public Investment Bank, banking reform, and the impact of cuts in labour taxes. Household investment should also pick up again, with the increase in available land and the elimination of structural impediments in the construction industry.

Renewed growth and policies to boost employment should enable the French economy to create some 80,000 jobs in the competitive sector in 2014. The growth rate of competitive sector payrolls should bounce back up to 2.4%, which is lower than the GDP growth rate, as is typical of the productivity cycle during a recovery. Consumption is likely to be firmer, driven by increases in purchasing power, as employment and wages start rising again and as consumers tap into employee savings plans. Domestic

[2] As measured by the Consumer Price Index.

demand, however, should not be as dynamic as export demand, which means that the trade balance should continue to make a positive contribution to growth.

This scenario is shrouded in uncertainty. More specifically, this outlook relies on continuing easing of financial tension in the euro area. Furthermore, the growth forecast for 2014 is lower than the potential growth rate, which means that the output gap should continue to widen. At the same time, the pace and scale of the recovery in our trading partners' economies, especially in the euro area, will determine the pace of export growth, as will future changes in the euro exchange rate. Finally, changes in commodity prices, especially oil prices, will also be a risk to household consumption and businesses' profit margins.

The European Commission's winter forecasts saw the French economy grow by 0.1% in 2013, picking up more speed to grow by 1.2% in 2014. These are the same growth forecasts as in this Stability Programme. The Commission and the Government both forecast that France's growth rate will be higher than the growth rate for the euro area in 2013. On the other hand, as fiscal consolidation continues, the Stability Programme scenario implies softer domestic demand than in the European Commission's scenario, but this would be offset by the capacity of the French economy to benefit from a global economic recovery, in view of its competitiveness gains.

2.3 Medium-term outlook (2015-2017)

The economic scenario used for multi-year planning is based on a growth rate of 2.0% per year in 2015, 2016 and 2017. This is a conservative figure, since it is only slightly higher than potential growth. It relies only on a partial narrowing of the output gap that has opened up with the crisis, which will stem in part from the structural reforms implemented by the Government. This means that the French economy has strong potential to rebound. Potential growth should stand at around 1½% between 2015 and 2017, after declining during the crisis. Productivity declined sharply during the crisis, but over the last several quarters, its growth has been more in line with the previous trend. In addition, France's National Statistics Institute, INSEE, forecasts that the labour force will grow by slightly less than ½% per year.

This scenario assumes that the adjustment of public finances will continue, that the household savings rate will decline and that the global economy will recover. Household debt levels are lower than in other countries, which means that household consumption should underpin growth as the savings rate continues to decline. Such a decline in the household savings rate would be made possible by the particularly high current savings rate and the brighter outlook on the labour market. Furthermore, export growth should be somewhat stronger than the growth trend of global demand for French exports. Exporting businesses should derive the full benefits of the Competitiveness and Jobs Tax Credit and other measures under the National Pact for Growth, Competitiveness and Jobs, which should boost their competitive strength. Net foreign trade should make a positive contribution to growth and the balance of trade in goods and services should improve gradually over the forecast period. The scenario also assumes that businesses' profit margins will improve: payrolls should grow by an average of 4.0% per year, which is less than the increase in market sector value added.

Table 1: Macroeconomic scenario, 2012-2017

Average annual growth rate, in %	2012*	2013	2014	Average 2015-2017
GDP	**0.0**	**0.1**	**1.2**	**2.0**
Household consumption	-0.1	0.2	0.9	1.9
General government consumption	1.4	1.2	0.6	0.3
Gross fixed capital formation	0.0	-0.8	1.2	2.4
o.w. non-financial businesses	*-0.5*	*-1.0*	*2.4*	*3.1*
Contribution from inventories	-1.0	-0.4	0.1	0.0
Contribution from net foreign trade	0.7	0.3	0.2	0.3
Exports	2.5	2.0	4.5	6.7
Imports	-0.3	0.8	3.5	5.3
GDP deflator	1.6	1.5	1.75	1.7
Household consumption deflator	1.7	1.3	1.75	1.75
Wage bill (non-farm market sector)	1.8	1.3	2.4	4.0
Average nominal wage per capita (non-farm market sector)	2.0	1.9	2.2	2.9
Salaried employment (non-farm market sector)	-0.2	-0.6	0.2	1.1

** INSEE quarterly accounts (adjusted for working days)*

3. Public finance scenario

3.1 Overall strategy and medium-term budgetary objective

The Government's objective is to reduce debt as a share of the national wealth and reach structural fiscal balance in the medium term. To achieve this, special attention is paid to the structural effort, with measures that preserve growth and mostly concern expenditure.

The multiyear public finance trajectory described in this Stability Programme distinguishes between two phases in achieving this objective, in accordance with the recommendations of the ECOFIN Council of 2 December 2009 (see Section 4) and the Public Finance Planning Act promulgated in December 2012:

- **In the first phase, the nominal government deficit will be reduced to less than 3% of GDP.** This means that substantial consolidation measures applying to 2012 and 2013 were passed starting in July 2012 to sustain the structural trajectory as the macroeconomic outlook worsened. A major effort will still be needed in 2014 to bring the deficit down to less than 3%. The effort in 2014 will be equivalent to approximately 1 point of GDP, among which 70% will involve savings on expenditure.

- **In the second phase, the medium-term budgetary objective of structural fiscal balance will be achieved. This will lead to a rapid reduction of debt as a share of GDP, leave more leeway for Government action and protect growth by allowing the automatic stabilisers to operate.** The public finance trajectory will be the result of continued expenditure savings under the rules set out in the Public Finance Planning Act and the effects of the modernisation of public action (MAP). Consequently, the structural deficit will be close to 0 in 2015 and reach it in 2016. Efforts to contain expenditure that are deployed over time will provide some leeway for reducing the tax burden, since a heavy tax burden could eventually undermine France's growth potential.

The Government's strategy over the period as a whole relies firstly on a major effort to contain expenditure and on targeted tax measures. In view of the already high level of taxation, a choice was made to avoid any across-the-board tax increases. Achieving structural balance in 2016 will subsequently make it possible to reduce the tax burden as the expenditure savings efforts gradually start to produce results, following an initial increase that is needed to ensure that the objectives are reached. **Consequently, the expenditure ratio is to be cut by 3 points of GDP between 2013 and 2017, whereas the tax burden will remain stable overall, before declining towards the end of the period.**

Containment of government expenditure throughout the programme period will make it possible to finance the Government's priorities. The effort to contain expenditure will continue until 2017, leading to a gradual decrease in government expenditure as a share of GDP. In real terms (excluding special accounting treatment of certain items[3]) expenditure growth will be limited to 0.5% on average over the period from 2013 to 2017, which is much lower than the historic trend of slightly more than 2%. The effort will be shared by all general government entities. The French administration has launched an ambitious initiative to modernise public action with the objective of carrying out an evaluation of all the public policies implemented by the various Government departments and agencies by 2017. The process will rely on a close partnership with the user, staff and agents of these policies to promote ownership of the process and its success, thereby contributing to containment of government expenditure. Central government expenditure, excluding debt and pensions, will decrease by €1.5 billion in 2014 and the

[3] The massive proceeds of spectrum auctions in 2012, standing at €2.6 billion, compared to €0.9 billion in 2011 and zero in 2013, are recorded as a fall in expenditure. In addition, military spending is recorded in the system of national accounts at the time of delivery and not the time of payment, which can lead to major discrepancies in Government expenditure. The recapitalisation of Dexia had an impact of €2.6 billion on Government expenditure in 2012.

Government's priorities of promoting jobs and fighting poverty will be financed by redeploying resources. Transfers to local governments will be reduced by €1.5 billion in 2014, and then by another €1.5 billion in 2015, representing a cut of €3 billion compared to 2013. Social security funds will also contribute to the effort to balance public finances. In addition to the efforts already announced on health insurance, management and labour representatives have reached an agreement on measures concerning the second-pillar pensions in the private sector that will help consolidate public finances. The same parties will also renegotiate the agreement on unemployment insurance by the end of 2013. Work has also started to balance the budgets of the old-age pensions and family benefits sections of the social security system in the medium term (Fragonard Task Force and Moreau Commission).

The aggregate tax and social security contribution rate should stabilise in 2015 and then decline towards the end of the period, after increasing up until 2014 to help bring the deficit back down to less than 3%. The higher tax burden in 2013 and 2014 will reflect the measures already called for in the Public Finance Planning Act: (i) impact of new measures for 2012 and 2013; (ii) supplementary measures to be implemented in 2014 to offset the lower return in 2014 on the measures taken for 2013 (the trajectory in the Planning Act already takes these new measures into account); (iii) measures to offset lower-than-expected returns (tax on financial transactions primarily) and measures overturned by the Constitutional Council; (iv) measures to achieve the objective set out in the Public Finance Planning Act to keep tax exemptions stable in nominal terms. In addition, revenue will be affected by the Agirc-Arrco pension agreement between labour and management representatives to increase contributions to supplementary retirement schemes in order to consolidate the system. The measures that still need to be documented include the efforts to step up the fight against tax fraud and tax evasion, and continued reductions in tax and social security contribution exemptions and other potential measures to help balance the budgets of retirement schemes in the medium term (Commission chaired by Ms Moreau).

The aggregate tax and social security contribution rate should decrease at the end of the period as the Competitiveness and Jobs Tax Credit starts to produce its effects, and as continued efforts to contain expenditure and achieve structural balance in 2016 provide some leeway to reduce the tax burden.

This strategy, which is based on a combination of reforms to boost growth, set out in detail in the National Reform Programme and sustainable containment of government expenditure, will lead to a decline in the government debt ratio starting in 2015.

This structural adjustment strategy will be implemented **for the purpose of enhancing the efficiency of public finances**. This will be achieved by continuing efforts to rationalise expenditure, and, more specifically, through the modernisation of public action (see Section 6.2.1) and redeployment of Investments for the Future (see Section 6.2.2), to focus expenditure on investments producing high social and economic returns and enhance the leverage of Government action. With regard to revenues, the continuing reduction of tax expenditures and the least effective social security contribution exemptions, along with the Competitiveness and Jobs Tax Credit worth nearly €10 billion in 2014 (see Section 6.3.2), will help streamline the tax system in favour of policies that generate more growth and jobs.

At the same time, **the Government will implement the enhancement of public finance governance passed in 2012**, in compliance with the European Treaty on Stability, Coordination and Governance in the Economic and Monetary Union, the European Budgetary Frameworks Directive and the latest European Regulations (see Section 8).

Table 2 – Multiyear public finance trajectory

(% of GDP)	2012	2013	2014	2015	2016	2017
Government balance	**-4.8**	**-3.7**	**-2.9**	**-2.0**	**-1.2**	**-0.7**
Structural balance	-3.7	-2.0	-1.0	-0.2	0.2	0.5
Structural adjustment (% of potentiel GDP)	*1.2*	*1.8*	*1.0*	*0.7*	*0.5*	*0.2*
General government expenditure	56.6	56.9	56.4	55.5	54.7	53.9
Real growth rate of expenditures (%)	*1.0*	*0.9*	*0.4*	*0.2*	*0.4*	*0.6*
Real growth rate of expenditures excluding special items (%)*	*0.7*	*0.9*	*0.5*	*0.1*	*0.4*	*0.6*
General government revenues	51.8	53.2	53.5	53.5	53.5	53.2
Government debt (Maastricht definition)	90.2	93.6	94.3	92.9	90.7	88.2
Government debt excluding financial support for the euro area	87.8	90.6	91.1	89.8	87.8	85.3

** Proceeds of spectrum sales, military expenditure, Dexia recapitalisation and changes in the accounting treatment of levies on revenues for the European Union*

3.2 The trajectory of public finance at "unchanged policy"

In accordance with the revised Stability and Growth Pact, this Stability Programme presents a scenario at unchanged policy, *i.e.* the spontaneous developments in the government balance that would occur with no changes to legislation or budget practices. The scenario at unchanged policy incorporates the developments stemming from the laws and regulations already in force, which distinguishes it from a "trend-line" trajectory. It does not consider the further measures to be implemented in order to meet the public finance targets.

This programme uses the following assumptions to construct the scenario at unchanged policy.

- The scenario considers revenue and expenditure measures already passed ("no legislative change" concept) under all legislation that has an impact on public finances and, more specifically, under Budget Acts, Social Security Budget Acts and Public Finance Planning Acts. For this Programme, therefore, the scenario includes the effects of measures introduced by the 2013 Initial Budget Act, the 2013 Social Security Budget Act, the Supplementary Budget Act of December 2012 and previous Budget Acts, along with the rules that future Budget Acts must comply with set out in the 2012-2017 Public Finance Planning Act. More specifically, the Multiyear Planning Act includes ambitious fiscal objectives for expenditure, which will be met by reducing and then stabilising central government expenditure in nominal terms (excluding pensions and interest expense) and by moderating the increase in the National Healthcare Expenditure Growth Target (Ondam), which have proven to be effective instruments for containing expenditure.

- The scenario also assumes no change in budget usual practices, such as index-linking of benefits (family allowance, pensions, etc.) and of taxes. It also incorporates statistically observed patterns, such as the pattern of the local government balance over the election cycle (including capital expenditure and local direct tax rates).

On the other hand, unlike the Stability Programme scenario, the scenario at unchanged policy does not incorporate planned measures still to be passed.

This Stability Programme also presents a **"spontaneous trajectory"** for the deficit that shows the spontaneous growth rates of government revenue, healthcare expenditure and central government expenditure. This trajectory is different from the trajectory at unchanged policy, because it does not consider efforts to meet fiscal requirements and measures introduced after July 2012. Without the efforts in the programme, the deficit would stand at 5½% of GDP in 2013.

Table 3 – Trajectory at unchanged policy

(% of GDP)	2013	2014	2015	2016	2017
Spontaneous trajectory (before measures introduced after May 2012)	**-5.9**	**-6.1**	**-5.7**	**-5.3**	**-5.2**
Compliance with the expenditure rules	0.6	1.1	1.5	1.9	2.3
New tax and social security contribution measures (as defined in the multiyear Public Finance Planning Act, excluding CTCCE*)		1.5	1.5	1.4	1.1
Competitiveness pact		0.0	0.0	0.0	0.0
of which CTCCE net of the VAT hike and environmental taxes*		*-0.2*	*-0.4*	*-0.4*	*-0.4*
of which expenditure saving measures		*0.2*	*0.4*	*0.4*	*0.4*
“Unchanged policy” scenario	**-3.7**	**-3.5**	**-2.7**	**-2.0**	**-1.8**
2013 Agreement on supplementary retirement pension schemes, rebalancing of social security funds’ budgets, reduction of tax exemptions and fighting tax fraud, stepping up efforts to contain government expenditure	0.0	0.5	0.7	0.9	1.1
Target trajectory	**-3.7**	**-2.9**	**-2.0**	**-1.2**	**-0.7**

** Corporate Tax Credit for Competitiveness and Employment*

The 2013 scenario at unchanged policy is based on a deficit of 3.7%, which is the same as the Government's target, since all of the expenditure and revenue measures have already been passed.

Box 1 – Balancing the social security funds’ budgets

The Government is determined to preserve the French social security model, while modernising it, at the same time. Therefore, efficiency needs to be improved to ensure financial equilibrium and sustainability.

Two task forces were created for this purpose.

As part of the modernisation of public action, Bertrand Fragonard was tasked with reviewing the architecture of family benefits with a view to reforms to balance the family benefits budget and enhance the targeting of benefits, while contributing to the fight against poverty. The objective is to make net savings of €1 billion in 2014, to start bringing the family benefits budget back into balance, while still providing financing for measures included in the five-year poverty reduction plan and for a major effort to provide services to parents (including infant care). The task force has just submitted its report to the Prime Minister and the measures that the Government decides to implement will be included in the 2014 Social Security Budget Bill.

According to the timetable drawn up at the labour-management conference in July 2012, a commission on the future of retirement benefits, chaired by Yannick Moreau, former Chair of the Pensions Advisory Council, was tasked with coming up with proposals to ensure the medium-term and long-term equilibrium of retirement schemes by June. In accordance with the timetable and methodology defined at the labour-management conference in July 2012, consultation will start with a view to recommending reforms in 2013. The public finance trajectory incorporates a gradual return to equilibrium for retirement schemes by 2020 at the latest, with a shift starting as early as 2014.

In 2014 and the following years, the scenario at unchanged policy incorporates the compliance with central government expenditure requirements and with the National Healthcare Expenditure Growth Target as set in the Public Finance Planning Act passed in December 2012. The scenario also includes the expenditure savings called for in the Planning Act to finance the Competitiveness and Jobs Tax Credit and the revenue measures anticipated in the Planning Act to offset the expected decline in the return on the measures introduced in 2013. The efforts needed to bring the deficit down to less than 3% of GDP in 2014 and to close the gap between the trajectory at unchanged policy and the target trajectory have already been identified. First of all, management and labour representatives reached an agreement on the two second-pillar pension schemes – the General Association of Pension Institutions for Managerial Staff (AGIRC) and the Association of Supplementary Pension Schemes (ARRCO). The other efforts will primarily be achieved through the savings produced by the modernisation of public action, measures to keep tax expenditures steady in nominal terms, the expected returns from stepping up the fight against tax fraud and efforts to balance social security funds' budgets (see Box 1).

3.3 Evolution of the structural balance

The measures implemented by the Government since July 2012 have increased the structural adjustment achieved over the period from 2010 to 2013 to 4.6 points of GDP[4]. The recommendation made by the ECOFIN Council at its meeting on 2 December 2009 called for structural adjustment of at least 4 points of GDP over this period (see Section 4). **In 2014, our estimates show that the deficit will be reduced to less than 3% of GDP by means of a structural effort of 1 point of GDP.** Under the Commission's very conservative potential growth assumption, this corresponds to a structural adjustment of more than ¾ point of GDP. **Structural adjustment will be more moderate in 2015 and 2016, but still significant**, at 0.6 point per year on average, to return to our medium-term budgetary objective (structural balance). Once structural equilibrium has been achieved, it will provide some leeway to reduce the tax burden, while maintaining the effort to contain expenditure. All in all, a slight structural adjustment will carry on the decline in the nominal deficit.

In 2012, the reduction of the deficit by 0.5 point of GDP (from 5.3% to 4.8%) was achieved despite one-off events that hampered improvement of the government balance, such as the recapitalisation of Dexia and the aftereffects of the fine imposed on France Télécom and recorded in 2011, and despite a very gloomy economy, with stagnant growth that deepened the cyclical deficit component by 0.5 point of GDP. The reduction of the deficit actually came from substantial structural adjustment of 1.2 point, as called for in the 2012-2017 Planning Act, with 1.3 points resulting from consolidation measures concerning revenue (1.1 point) and expenditure (0.2 point, which could have been 0.2 point more if not for adverse price effects for public finances[5]). The structural adjustment is slightly smaller than the efforts made, because of spontaneous developments in non-tax revenue, which failed to keep pace with growth (more specifically, a sharp decline in dividends paid to the Government).

Table 4 – Multiyear structural balance trajectory

(% of GDP)	2012	2013	2014	2015	2016	2017
Government balance (1)	-4.8	-3.7	-2.9	-2.0	-1.2	-0.7
Cyclical balance (2)	-1.0	-1.6	-1.8	-1.6	-1.4	-1.2
One-off measures (3)	-0.1	-0.1	-0.1	-0.1	0.0	0.0
Structural balance (1)-(2)-(3)	**-3.7**	**-2.0**	**-1.0**	**-0.2**	**0.2**	**0.5**
Change in the structural balance	1.2	1.8	1.0	0.7	0.5	0.2
Structural balance of the multiyear Public Finance Planning Act	*-3.6*	*-1.6*	*-1.1*	*-0.5*	*0.0*	*0.0*

In 2013, the deficit will shrink by 1.1 point, from 4.8% to 3.7%, which is a greater decline than in 2012, despite the persistent gloom in the economic environment. This result reflects a strong structural effort,

[4] Hereinafter, structural adjustment is estimated using the same potential growth rate as in the Public Finance Planning Act (*i.e.* 1.2% on average from 2010 to 2013 and 1.5% in 2014).

[5] The GDP price growth was sluggish at 1.6%, compared to consumer prices (excluding tobacco), which rose by 1.9%, creating adverse terms of trade at a time when oil prices are rising.

equivalent to 1.9 point of GDP, with even greater efforts than in 2012. The effort will be equivalent to 1.9 point, compared to 1.3 point in 2011 and 2012. As was the case in 2012, the effort will stem from new tax and contribution measures (1.5 point), as well as continuing containment of expenditure (0.4 point). However, some of these efforts will be neutralised by persistently sluggish growth, which will reach only 0.1%, far less than the potential growth rate. This can be seen not only in the deepening of the cyclical deficit component by 0.6 points, but also in structural adjustment, as a result of spontaneous growth of tax revenue that is weaker than GDP growth (elasticity effects of -0.1 points). One-off measures should have a neutral effect on the government balance, since the aftereffect of the recapitalisation of Dexia will be offset by the cost of exceptional tax disputes (see Box 2). The gap compared to the structural balance in the Public Finance Planning Act stands at 0.3 point[6]. This gap falls below the 0.5-point threshold triggering the correction mechanism mentioned in the Constitutional Bylaw 2012-1403 of 17 December 2012 on public finance planning and governance.

Table 5 – Breakdown of structural adjustment

(% of potential GDP)	2012	2013	2014	2015	2016	2017
Structural adjustment	1.2	1.8	1.0	0.7	0.5	0.2
Structural effort	1.3	1.9	1.0	0.6	0.5	0.3
Discretionary tax measures	*1.1*	*1.5*	*0.3*	*0.0*	*0.0*	*-0.2*
Effort in expenditure	*0.2*	*0.4*	*0.6*	*0.7*	*0.5*	*0.5*
Non discretionary component	-0.1	-0.1	0.0	0.1	-0.1	0.0

In 2014, the reduction of the deficit by 0.8 point will be entirely structural (1.0 point) in view of growth that is expected to be closer to potential growth (a negative cyclical component of 0.2 point only). The expenditure requirements expressed in nominal terms for the central government and health insurance system, along with the commitments to contain expenditure above and beyond these requirements by cutting government expenditure to finance the Competitiveness and Jobs Tax Credit, in particular, and the preliminary savings made on expenditures for the purpose of balancing the budgets of social security and supplementary retirement pension schemes all mean that the main effort in 2014 will focus on expenditure (0.6 point) despite the assumption that interest rates will rise and increase interest expense. Measures to increase revenue will account for only a minor share, equal to 0.3 point of potential GDP growth, in order to offset the decline in returns in 2014 – from measures implemented in 2013, which is already anticipated in the Planning Act trajectory, lower-than-expected returns, from the financial transactions tax in particular, and measures overturned by France's Constitutional Council – and to stabilise tax exemptions in nominal terms and to step up the fight against tax fraud. Revenue measures also include the revenue aspects of the management and labour representatives' agreement on supplementary retirement pensions. Furthermore, it is estimated that tax disputes will have just as much impact on the government balance as in 2012, which means it will be neutral in terms of change in the government balance. Ultimately, 70% of the structural effort should rely on expenditure savings in 2014.

Between 2015 and 2017, the average annual reduction of the deficit by ¾ point of GDP stems from the business cycle (0.2 point), since real economic growth is greater than potential growth, thereby reducing the domestic output gap gradually, from structural adjustment (0.5 point) and the rest from the end of the losses related to tax disputes (see Box 2). Structural adjustment in 2015-2017 stems almost entirely from

[6] 2.0 points of GDP in the Stability Programme trajectory, compared to 1.6 point of GDP in the Public Finance Planning Act.

continued efforts to contain expenditure in all general government sub-sectors, which will provide leeway for measures to reduce the tax burden at the end of the period.

Box 2 – One-off and temporary measures considered in the evaluation of France's structural balance

France introduced a structural balance rule for the implementation of the Treaty on Stability, Coordination and Governance. This corresponds to the government balance adjusted for the direct effects of the business cycle and one-offs. This rule prevents the pro-cyclical effects produced by a management of government finances based on the nominal balance.

The following one-off events and measures are not included in the structural balance under the Stability Programme, in line with the method used in the Public Finance Planning Act:

- **On the revenue side**, the losses stemming from exceptional tax disputes whose recording year in national accounts cannot be foreseen because it depends on the year and outcome of the proceedings and the courts' final rulings[7]. This involves reimbursements to foreign UCITS and reimbursements of withholding tax (*précompte mobilier*).
- **On the expenditure side**, France's €2.6-billion recapitalisation of Dexia. Following a decision by Eurostat, this amount is exceptionally recorded in the 2012 government balance.

Table 6 – Assumptions concerning tax disputes

(deviation from baseline, in € bn)	2012	2013	2014	2015	2016	2017
Total	**0.0**	**-2.8**	**-2.7**	**-2.8**	**0.0**	**0.0**
Withholding tax dispute (*précompte mobilier*)	0.0	0.0	-1.0	-1.0	0.0	0.0
UCITS dispute (*OPCVM*)	0.0	-1.5	-1.8	-1.8	0.0	0.0
Electronic communications tax dispute	0.0	-1.3	0.0	0.0	0.0	0.0

NB: *the figures given in this table do not predict the outcome of the disputes; they merely reflect the conservative approach to multiyear public finance projections. Furthermore, the figures shown are subject to change as a result of the courts' final rulings.*

3.4 Evolution of the government balance by sub-sector

Consolidation of public finances will be the result of joint efforts by all general government sub-sectors over the planning period, as the economy recovers and leads to a spontaneous increase in revenue. This will improve the government balance by 4.1 points of GDP between 2012 and 2017, from a deficit of 4.8% of GDP in 2012, to a deficit of 0.7% of GDP in 2017.

The central government borrowing requirement (central government and other central government bodies) **will fall by 2.8 points between 2012 and 2017**, from 4.1% of GDP in 2012 to 1.3% of GDP in 2017). This reduction will stem primarily from stabilisation, followed by a cut, in central government expenditure, excluding pensions and debt service. This represents a cut of €1.5 billion in central government expenditure, excluding pensions and debt service, in 2014. The reduction will rely on reforms

[7] Expenditure and revenue are recorded in the system of national accounts on an accrual basis. According to the European System of Accounts of 1995, this means, "when economic value is created, transformed or extinguished, or when claims and obligations arise, are transformed or are cancelled". Consequently, the impact of disputes is recorded in the year when the courts make their final ruling, whereas, in budgetary accounting, the impact is recorded on the basis of cash flows.

and savings and streamlining measures defined by the ministries, particularly within the framework of the modernisation of public action. The share of central government expenditure in GDP will decline sharply, providing leeway for measures to reduce revenue towards the end of the period. Combined with the effects of the Competiveness and Jobs Tax Credit, such tax cuts will reduce the tax burden following the tax hikes related to the consolidation measures passed since July 2012.

Table 7 – General government lending capacity (+) / borrowing requirement (-)

(% of GDP)	2012	2013	2014	2015	2016	2017
Government balance, Maastricht definition	-4.8	-3.7	-2.9	-2.0	-1.2	-0.7
o.w. primary balance	*-2.3*	*-1.3*	*-0.4*	*0.7*	*1.6*	*2.1*
State	-3.9	-2.8	-2.2	-1.9	-1.5	-1.2
Other central government bodies	-0.1	-0.1	-0.1	0.0	0.0	0.0
Local governments	-0.2	-0.2	-0.2	0.0	0.0	0.0
Social security funds	-0.6	-0.6	-0.5	-0.1	0.3	0.6

The budgets of other central government bodies will be nearly balanced over the period, with slight fluctuations owing to the timing of expenditure under the Invest for the Future programme (expenditure growth should widen the deficit temporarily, peaking in 2014).

The social security balance, excluding the social security debt redemption fund (CADES) and the pension reserve fund (FRR), should improve by 1.2 point of GDP between 2012 and 2017, going from a deficit of 1.1 point of GDP to equilibrium at the end of the period (the balance including CADES and FRR will go from -0.6% of GDP to +0.6% of GDP). In addition to the revenue measures introduced in 2012 and 2013, this improvement will stem mainly from the limited increase in the National Healthcare Expenditure Growth Target (Ondam), the implementation of the March 2013 agreement on supplementary retirement pensions and from measures that will follow the review of family policy and retirement schemes. The measures adopted following the Fragonard Report to balance the family benefits budget will be incorporated into the 2014 Social Security Budget Bill. The commission chaired by Ms Moreau will submit proposals for reform to the Government in June to ensure balanced retirement scheme budgets in the short, medium and long term. In accordance with the timetable and methodology defined at the labour-management conference in July 2012, consultation will start on these proposals with a view to recommending reforms in 2013.

Local governments will also do their share, since their balance should move from a deficit of 0.2 point of GDP in 2014, to financial equilibrium at the end of the period. This will be achieved primarily through expenditure reductions as central government transfers are reduced by €1.5 billion in 2014 and by a further €1.5 billion in 2015. An improving economy and a smaller deficit in the first years of the election cycle will also contribute to this improvement.

3.5 Evolution of government expenditure

3.5.1 Expenditure of general government

Table 8 – Change in general government expenditure

(annual average, in real terms and in %*)	2012	2013	2014	2015-2017
General government	**1.0**	**0.9**	**0.4**	**0.4**
Excluding proceeds of spectrum sales, military expenditure, Dexia recapitalisation and changes in the accounting treatment of levies on revenues for the European Union	***0.7***	***0.9***	***0.5***	***0.4***
Central government (APUC)	0.0	-0.4	-0.5	-0.3
Local governments (APUL)	1.1	1.3	0.2	0.5
Social security funds (ASSO)	1.2	1.8	0.8	0.7

** Expenditure in real and like-for-like terms, including transfers between general government sub-sectors.*

Major efforts to contain expenditure will be made throughout the planning period and by each of the general government sub-sectors to reduce expenditure as a percentage of GDP by 3 points from 56.9% in 2013 to 53.9% in 2017.

Government expenditure will grow by an average of 0.5% in real terms between 2013 and 2017, which is much lower than the long-term average of 2.1%[8] and much lower than potential GDP growth. Sustainable containment of government expenditure will come from a steadfast joint effort by all of the general government sub-sectors: dropping in 2015, and then stabilising in nominal terms for central government expenditure (for aggregate spending, excluding debt service and pensions); local government spending will be limited, because of the stabilisation in nominal terms and then cuts in central government transfers in 2014 and 2015; savings achieved through the modernisation of public action; compliance with the National Healthcare Expenditure Target, whose growth rate will decline gradually; the effects of the management and labour representatives' agreements on supplementary retirement funds (which will start to be felt in 2013 both in terms of expenditure and revenue); and the measures to be adopted following the review of family policies (task force chaired by Mr Fragonard) and the retirement pension system (commission chaired by Ms Moreau).

In 2012, government expenditure showed little growth, once exceptional events are excluded, rising by 0.7%, compared to a 0.9% increase in 2011. Aggregate expenditure growth in 2012 was driven by exceptional events that were not provided for in the 2013 Budget Act, such as the recapitalisation of Dexia, which counts as expenditure and not a financial transaction (this measure cost €2.6 billion, accounting for more than 0.1 percentage point of expenditure growth) and special treatment of military expenditure[9] in the national accounts and the payments made in early 2013 under the 2012 European Amending Budget, which will contribute nearly 0.2 point. When these measures are excluded, State and healthcare expenditures subject to the rules of the Planning Act were lower than expected, which points to the effectiveness of expenditure management. The deviation from the 0.5% real growth forecast (excluding exceptional events) in 2012 set out in the 2013 Budget Bill is due in part to lower-than-expected inflation (excluding tobacco prices), standing at 1.9% instead of 2.0%, and slightly stronger growth of local government expenditure.

[8] The average annual real growth rate of Government expenditure from 2000 to 2011.

[9] Military expenditure is recorded in the system of national accounts at the time of delivery and not at the time of payment, which can lead to major discrepancies in Government expenditure.

In 2013, aggregate expenditure (as well as expenditure excluding exceptional events[10]) should grow by 0.9% in real terms, which is faster than its growth in 2012 (0.7% excluding exceptional events) **reflecting a sharp drop in inflation** (from 1.9% to 1.2%), which is not incorporated into State and healthcare expenditure targets expressed in nominal terms.

Expenditure growth should be weak between 2014 and 2017, averaging 0.4%. This should primarily reflect the continued efforts to meet the budgetary rules for State and healthcare expenditure under the Public Finance Planning Act, as well as the growing savings from the modernisation of public action and the additional effort to cut State expenditure, excluding debt service and pensions, by €1.5 billion in 2014 on top of the savings called for in the Public Finance Planning Act and under the agreement on supplementary retirement pensions in 2013, which has already been signed by management and labour representatives. The reforms carried out in 2013 to balance the budgets for old age pensions and family benefits (task force assigned to Mr Fragonard and commission chaired by Ms Moreau) will contribute to containment of social security fund expenditure. Finally, a dip in local government capital expenditure is expected in 2014 and 2015, because of the elections calendar. Expenditure under the Invest for the Future programme should gradually slow after peaking in 2014.

3.5.2 State expenditure

The State's general budget is drawn up and executed according to the "zero nominal spending growth" rule. The 2012-2017 Public Finance Planning Act of 31 December 2012 upholds this rule. At the most, the rule calls for stabilising the sum in current euros of appropriations under the general budget, levies on revenues (made on behalf of the European Union and local governments) and allocations of revenue to third parties, excluding debt service and civil service pension expenditure.

If we add debt service and pensions to these appropriations (total general budget expenditure), the annual increase in budget appropriations and levies on revenues should not exceed the inflation rate.

The freeze on nominal expenditure, excluding debt service and pensions, is particularly effective. More specifically, this rule has ensured that all of the savings on debt service in 2012 stemming from lower interest rates have been used entirely for structural consolidation of our public finances and not to finance other expenditures.

Furthermore, although discrepancies in inflation, debt and pension forecasts make it impossible to meet the overall ceiling on aggregate expenditure, and despite the fact appropriations "excluding debt service and pensions" might comply with the "zero nominal growth" rule, the ceiling on ministries' budget appropriations will still be lowered to keep aggregate expenditure growth in line with inflation.

In 2012, State expenditure was cut substantially, both in the initial budget and in the outturn

Compared to the 2012 Budget Bill tabled in October 2011, which called for stabilising expenditure in 2012 at the level of the 2011 Initial Budget Act under the "zero nominal growth" rule, the target that was ultimately applied in 2012 was tightened up twice: once during the Parliament's examination of the Initial Budget Act for 2012, when the target was cut by €1.2 billion, and again during the vote on the first 2012 Supplementary Budget, when the target was cut by a further €1.2 billion, bringing the total reduction to

[10] The aftereffect of recapitalising Dexia and the accounting treatment of payments made under the European budget, which hold down 2013 expenditure growth compared to 2012, are offset by the aftereffect of the proceeds of spectrum auctions received in 2012 and by the adjustment for military expenditure recorded in the system of national accounts.

€2.4 billion compared to the 2011 Initial Budget Act. Given the particularly rigorous environment for executing the budget, with the Court of Auditors reporting the risk of overruns to the order of €2 billion back in July 2012, the Government introduced preventive measures to ensure that the expenditure target was met. Following the independent audit of public finances that it commissioned from the First President of the Court of Auditors, the Government decided to freeze a further €1.5 billion of the appropriations made to ministries for 2012.

In the outturn, State expenditure, excluding debt service and pensions, were ultimately perfectly contained, coming in under the lower target by nearly €100 million. All in all, State expenditure, including debt service and pensions, posted a historic decline of €0.3 billion in nominal terms, compared to the 2011 budget outturn.

"Aggregate expenditure", including debt service and civil service pensions, met the target initially set with some room to spare because of the efficient execution of expenditure subject to the zero nominal growth rule and favourable circumstances for debt service, where savings of €2.5 billion were made compared to the Initial Budget Act. Strict control of State expenditure planning in 2013 and the following years is critical for achieving balanced public finances.

The 2013 Initial Budget Act was drafted with the same exacting rules (zero nominal expenditure growth, excluding debt service and pensions, and aggregate expenditure growth that cannot exceed the inflation rate). A further €2 billion in appropriations was frozen back in January, in addition to the usual amount put into reserves, raising the Government's precautionary reserve to nearly €8 billion. The purpose of this reserve is to promote containment of State expenditure and even to create further savings if conditions during the fiscal year permit.

The 2012-2017 Public Finance Planning Act calls for State expenditure to remain stable in nominal terms over the period as a whole, which will constitute an unprecedented effort.

Compliance with this trajectory will require new discipline in the management of State expenditure. The Prime Minister's Circular dated 14 January 2013 on the "rules for responsible management of government expenditure" defines this new discipline, which is built on three main principles: self-insurance, which means that each ministerial department must cover the risks it incurs; financing all new expenditure through savings on expenditure, and a ban on substituting tax expenditures for budget expenditures.

Furthermore, half of the drop in revenue caused by the Competitiveness and Jobs Tax Credit will eventually be covered by expenditure savings. The State will contribute by cutting expenditure covered by the "zero nominal growth" rule by €1.5 billion in 2014.

Compliance with this ambitious trajectory will rely on reforms and savings and streamlining measures to be identified as part of the modernisation of public action process (see Section 6.2.1). More specifically, this approach will endeavour to identify overlaps and redundant actions, modernise ministries' operations in order to contain their operating expenditure and target expenditure more effectively.

Debt service is expected to increase over the period, but the growth of aggregate expenditure still will not exceed the inflation rate because of the decline in nominal terms of expenditure excluding debt service and pensions.

3.5.3 Expenditure of other central government bodies

Other central government bodies, in their capacity as "central government operators"[11], will contribute to the effort to reduce expenditure. Most of these operators maintain fairly balanced budgets. They are not allowed to borrow from credit institutions or issue debt securities with maturities of more than 12 months[12], which helps contain their expenditure. Furthermore, a parity principle means that central government operators will comply with the same requirements that the central government places on its own expenditure.

This means that the expenditure growth of other central government bodies over the planning period can primarily be attributed to the Invest for the Future programme, which causes faster expenditure growth at the start of the planning period, followed by stabilisation and then a reduction of expenditure at the end of the period (see Section 6.2.2.), and compensation for the cost of public service in electricity. The contribution to the cost of public service in electricity pays the French electricity utility EDF for the growing cost of public services in electricity, such as the purchase of electricity from renewable energy sources (solar power) and lower electricity rates implemented as part of the plan to fight poverty[13]. The central government operators' expenditure also reflects the Greater Paris Corporation's investments. This corporation (Société du Grand Paris) was founded in late 2010 to organise financing for the two automated métro loops around Paris, which are planned to start services between 2020 and 2030. In addition to continuing its preliminary studies and land acquisitions, the start of construction will lead to an increase in the Corporation's expenditure.

This means that other central government bodies' expenditure should grow at an average annual rate of ¾% in real terms from 2012 to 2017, both as a result of the central government operators' major efforts to reduce operating costs and, for others, their role as public investors. These bodies account for approximately half of the capital expenditure by central government.

3.5.4 Expenditure of the social security funds

In 2012, benefits paid by the social security funds grew by 3.5% in nominal terms, which was slightly faster than their 3.1% growth in 2011. This growth is primarily attributable to the impact of the one-off €0.4-billion increase in the back-to-school bonus on family benefits, which grew at a 2.8% rate, following 1.4% in the previous year, and the increase in expenditure of unemployment benefits, which rose by 5.3%, following a decline of 0.6% in the previous year. This increase was caused by economic conditions, with zero growth of the economy in 2012, after a 1.7% growth rate in 2011. On the other hand, healthcare expenditure decelerated, as consumption turned out to be lower than initially budgeted (see below).

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[11] The salient features of central Government operators are that they carry on public service activities, are mostly financed by the State and are under the State's direct control. The purview of central Government operators and that of other central Government bodies are not exactly the same: the former are considered from the point of view of the budget and the latter are considered from the point of view of the system of national accounts and listed by the National Statistics Institute each year.

[12] Article 12 of the 2011-2014 Public Finance Planning Act (which has not been abrogated by the December 2012 Planning Act) prohibits them from incurring debt with maturities of more than twelve months, except for the Government Debt Fund and the Corporation for Central Government Equity Holdings (*Société de proses de participation de l'Etat*).

[13] The means-tested limit for the supplementary health insurance benefit was raised and its recipients are entitled to lower gas and electricity rates.

In 2013, benefits will grow slightly less rapidly, rising to3.3%, mainly as a result of slower growth regarding old-age benefits (growth rate of 3.4% compared to 4.0% the previous year). Basic pensions were raised by only 1.3% on 1 April 2013, following a raise of 2.1% in 2012. The smaller raise was due to the lower inflation rate. The growth of family benefits will also be slower, at 2.0%, compared to 2.8% in 2012 due to a one-off increase in the back-to-school bonus. In contrast, unemployment benefits will continue to grow significantly, rising to 6.1%, following a 5.3% growth rate in 2012. The 2013 National Healthcare Expenditure Target was voted at a 2.7% growth rate, a slight increase compared to the 2.4% growth observed in 2012 meant to boost investment in hospitals. The growth rate should be lower than 2.7% for the rest of the period.

Between 2014 and 2017, the growth of most social benefits should substantially slow down, leading the overall growth of social benefits to fall to 2.4%. Pension expenditures should continue to grow more moderately in real terms with the National Inter-Sector Agreement, signed on 13 March 2013, which will let index-linked supplementary pensions fall behind inflation. The measures to come from the work conducted by Mr Fragonard and the commission chaired by Ms Moreau in 2013 on balancing the budgets of the social security old-age pensions and family benefit systems in the medium term should also help contain expenditure growth. Expected improvements in the labour market should also greatly reduce the growth of unemployment benefits.

Table 9 – Change in expenditure of the social security funds

(nominal growth rate, %)	2012	2013	2014-2017*
Social insurance benefits	**3,5**	**3,3**	**2,4**
Old age and survivor benefits	4,0	3,4	3,1
Family-Housing	2,8	2,0	0,8
Unemployment	5,3	6,1	0,4
National Healthcare Expenditure Growth Target	2,4	2,7	2,5

** Average annual growth rate, 2014-2017.*

NB: The 2014 growth rate of the National Healthcare Expenditure Target is 2.6% and it will fall to 2.5% in 2015 and onwards.

Healthcare benefits

The slowing down of healthcare insurance expenditure growth that started in 2008 continued **in 2012** and made it possible to comply with the National Healthcare Expenditure Target adopted in the Social Security Budget Act. The reform of the governance of the National Healthcare Expenditure Target: namely, the reduction of the warning threshold, the introduction of a new monitoring committee and the increase in the number of actions taken by the early warning committee, helped meet the target for the third year in a row. The latest accounting data available even show that the outturn is far below the initial target by some €0.9 billion. This result is testimony of the Government's efficient management of healthcare expenditure. The Government has also backed this effort with structural actions to improve the organisation of the healthcare system by elaborating a national healthcare strategy.

The 2013 target is set for a 2.7% growth. All in all, an effort of €2.5 billion in cost oriented measures has been decided to slow expenditure growth in order to meet the target, including €1.8 billion for the private medical practice sector. These measures consist mainly of €0.9 billion in savings on healthcare products, such as brand-name and generic drugs and medical devices. They also rely on continuing efforts to moderate prescriptions and improve medical efficiency (savings evaluated at €0.6 billion). The savings measures also concern €0.2 billion in outpatient care expenditures, with lower fees for certain medical specialties, and laboratory work and improved expenditure efficiency on patient transportation in accordance with the remarks made by the Court of Auditors. Savings of some €0.7 billion have been made in the hospital sector.

From 2014 to 2017, the National Healthcare Expenditure Target for the latest Public Finance Planning Act is 2.6% in 2014 and then an average of 2.5% per year after that. Compliance with this medium-term trajectory will rely on persistent efforts to improve the efficiency of the market for healthcare products and services. The heart of this quest for greater efficiency is the improvement of treatment through effective regulation of healthcare supply aimed at breaking down the barriers between outpatient care, hospital care and the medical and social sector. This will be a priority for the Government as part of the national healthcare strategy initiated in 2013. Furthermore, these growth targets do not incorporate the impact of the Competitiveness and Jobs Tax Credit on the healthcare sector, which will reduce healthcare production costs, thereby positively affecting the expenditure trajectory.

Old-age benefits

In accordance with the priorities that the Government defined during the social conference in July 2012, and following the publication of the report by the Pensions Advisory Council in December 2012, a commission chaired by Ms Moreau has started to work on balancing the budgets of the retirement funds in the short, medium and long run (see Section 7.1.1). The trajectory shown here, which incorporates the effects of the 2013 agreement on supplementary retirement pension schemes, is in line with this process.

Other social benefits

Family and housing benefits grew by 2.8% in 2012. This growth results from the opposing effects of the 1% increase in family benefits by the previous Government, instead of an increase matching inflation, and the one-off increase of 25% in the back-to-school bonus in September 2012. These benefits should grow by 2.0% in 2013 with the resumption of the linking of benefits to inflation, these stood at 1.2% on 1 April 2013. Incorporating the conclusions of the work on balancing the budget for family benefits assigned to Mr Fragonard, such as linking family benefits to income, as announced by the President, should slow their growth to an estimated average of 0.8% per year between 2014 and 2017.

After showing a sustained growth in 2012 and 2013, expenditure on unemployment insurance benefits should grow more slowly as the economy improves. As part of the renegotiation of the unemployment insurance agreement for 2014 and 2015, management and labour representatives will have to redefine the framework of the unemployment insurance benefits, taking into account the financial trajectory of the system. The trajectory presented here assumes a gradual return to a balanced budget for the unemployment insurance system by the end of 2017.

3.5.5 Expenditure of local governments

The local government balance should be close to equilibrium from 2013 to 2017, because local government expenditure growth has slowed down from the pace observed from 2000 to 2010.

The local investment momentum seen in 2011 and 2012 should continue in 2013 in the run-up to the 2014 municipal elections. Given the declines in local governments' capital spending seen in 2009 and 2010, its growth should be weak at an average of 0.6% in nominal terms over the 2008-2013 election cycle. Local capital spending should shrink in 2014 and 2015, followed by gradual growth up until 2017, in keeping with the pattern observed in previous election cycles.

Current expenditure growth should be contained over the planning period because of fiscal restraint made necessary by a reduction of the nominal amount of central government transfers for local governments, with a €1.5-billion cut in 2014 and a further €1.5-billion cut in 2015. In 2013 and 2014, social expenditure and operating expenditure should be affected by the deteriorating economic situation, with an increase in spending on the social inclusion benefit (*RSA socle*). Local governments will also share some of the cost of implementing employment policy as the Jobs for the Future programme takes effect. They will share the cost of implementing school-year reform, with a financial support made available for local governments that lack resources. As the economic outlook becomes brighter and with the achievement of the stepping-up of certain social security benefits, such as the Disability Compensation Benefit (PCH), current expenditure should grow more slowly in the second part of the planning period.

3.6 Evolution of government revenues

3.6.1 Revenues of general government

After a period of growth (2011-2014) due to measures aimed at bringing the fiscal balance below 3% of GDP, the aggregate tax and social security contribution rate (the "tax burden") will subsequently decline to 46.3% of GDP in 2017, equalling its 2013 level.

This projection incorporates the effects of all of the measures promulgated; the commitment made in the Public Finance Planning Act to offset the diminishing returns in 2014 of measures introduced in 2013; new measures to be introduced to offset lower-than-expected returns from certain measures, such as the Financial Transactions Tax, and measures overturned by the Constitutional Council, along with measures to stabilise tax exemptions in nominal terms; and to step up the fight against tax fraud. The trajectory also incorporates the impact on revenues of the agreement between management and labour representatives on supplementary retirement schemes.

In 2015-2017, the stepping-up of the Competitiveness and Jobs Tax Credit will help reduce the tax burden, half of its cost being financed by savings on expenditure. The leeway to lower the tax burden opened up by maintaining efforts to contain expenditure will be used to reduce taxes, once structural balance has been achieved.

The elasticity of the aggregate taxes and social security contributions to nominal economic growth is expected to be slightly less than 1 in 2013 and 2014. In 2013, this will be because central government revenue over-reacts on the downside, notably the corporate income tax, and in 2014, it will be because social security contributions are less dynamic than economic activity (wage bill growth will lag behind GDP, due to the productivity cycle). After that, elasticity will average 1.0 from 2015 to 2017.

Table 10 – Aggregate tax and social contribution rate

	2011	2012	2013	2014	2015-2017
Aggregate tax and social security contribution rate (as a % of GDP)	**43.7**	**44.9**	**46.3**	**46.5**	**46.5**
Elasticity in taxes and social security contributions	1.1	1.1	0.9	0.9	1.0

In 2013, the aggregate tax and social security contribution rate will increase by 1.4 points, rising from 44.9% to 46.3%. This reflects a major effort to reduce the deficit in a persistently adverse economic environment. Much of this effort is the result of measures introduced by the 2013 Initial Budget Act and Initial Social Security Budget Act and the effects of measures introduced by the July 2012 Supplementary

Budget Act. In addition to these measures, 0.2 point of the increase comes from new measures introduced before 1 July 2012, primarily by the 2012 Budget Acts and by the Social Security Budget Act. All of these measures increase the aggregate tax and social security contribution rate by 1.4 point of GDP, whereas its spontaneous increase would be slightly less than GDP growth.

From 2014 to 2017, the increase in the aggregate tax and social security contribution rate should be much more moderate in 2014, rising from 46.3% of GDP to 46.5%, before returning to 46.3%. The increase in 2014 will reflect measures to offset lower-than-expected returns in 2013, from the Financial Transaction Tax in particular, and the measures overturned by the Constitutional Council. It will also reflect the reduction in tax and social security contribution exemptions and the stepped-up fight against tax fraud, as well as the impact on revenue of the agreement signed by management and labour representatives on supplementary retirement schemes. The trajectory also incorporates the conventional pattern of local taxes in relation to the election cycle and the increase in the levy to compensate electricity distributors for additional costs entailed by their public service obligations, in accordance with the commitment to cover the past shortfall. At the end of the planning period, the tax burden will be reduced with the leeway for lowering taxes, once structural balance has been achieved, and with the stepping-up of the Competitiveness and Jobs Tax Credit (see Section 6.3.2.). Half of the cost of the tax credit is financed by savings on expenditure. It will help reduce the tax burden by more than €10 billion by 2017.

Furthermore, non-tax revenues as a percentage of GDP should be unchanged at 7.2% between 2014 and 2017.

3.6.2 State revenues

In 2013, State taxes will rise sharply compared to 2012. The increase stems primarily from the Government's tax consolidation strategy, which leads to a positive impact of new measures on revenue. The main new measures are:

- ***Measures aimed at households:*** a new 45% tax bracket, a lower ceiling on the "*quotient familial*", taxing investment income at the same rates as labour income, re-introducing progressive rates for the wealth tax, and, at the other end of the income scale, an increase in the exemption for the least well-off households.

- ***Measures aimed at businesses:*** a cap on the deduction for financial expense when calculating the taxable corporate income, a reform of the deduction for expenses and fees from capital gains on sales of equity securities, tighter limits on carrying forward past losses, a reform of the final corporate income tax payment instalment, a two-year extension of the exceptional contribution worth 5% of corporate income tax owed by large corporations and the exceptional contribution owed by insurance companies in 2013 only.

Several measures introduced in the August 2012 Supplementary Budget Act also increased revenues in 2013, such as the creation of a 3% contribution on dividend payments, a set of anti-abuse measures regarding corporate taxation aimed at eliminating certain tax planning arrangements, reducing inheritance tax deductions and bringing back taxes on overtime pay.

With no change in legislation, central government taxes would have increased by only 1.6% in 2013, which is lower than the expected 1.7% growth of nominal GDP. The low spontaneous growth of corporate income tax and value-added tax explains most of the weak increase in revenue.

In 2014, the spontaneous increase in central government taxes should be slightly greater than the 3.0% nominal increase in GDP. New measures, such as the measures introduced in July 2012, in the 2013 Budget Act, and in the future 2014 Budget Bill, which will step up the fight against fraud, reduce tax and social security contribution exemptions and offset the downwards-revised returns on measures such as the Financial Transactions Tax and the expected decline in the returns on certain 2013 measures provided for in the 2013 Budget Act, will contribute to an increase in the tax burden, after adjusting for the impact of the Competitiveness and Jobs Tax Credit.

From 2015 to 2017, spontaneous growth of central government taxes is expected to mirror the nominal GDP growth rate very closely. At the same time, the effects of the Competitiveness and Jobs Tax Credit and the leeway for cutting taxes that opens up at the end of the planning period, once structural balance has been achieved, should lead to a reduction of the tax burden.

3.6.3 Revenues of social security funds

In 2012, the revenues of the social security funds increased by 3.4%. The 3.0% growth of social security contributions outstripped the 2.2% growth of private sector wage bill; partly as a result of the suppression of the exemption from contributions on overtime pay. The increase in contribution rates intended to finance the early retirement scheme for long-serving employees also produced extra revenues in 2012. New measures also underpinned the 4.7% increase in tax revenues. The increase in taxes on production stems primarily from two increases in the minimum tax on social security exempt benefits paid by employers ("*forfait social*"), first from 6% to 8% in the 2012 Social Security Budget Act, and then from 8% to 20% in the Second 2012 Supplementary Budget Act. The 2-point increase in the social security levy on capital income also increased tax revenues. Other measures implemented earlier, such as the reduction of the flat-rate Generalized Social Contribution ("*CSG*") exemption for professional expenses to take into account work related expenses or the elimination of the partial exemption from the special tax on insurance policies for "inclusive and socially responsible" contracts, also contributed to the increase in social security revenues in 2012.

In 2013, social security revenues should slow down primarily because of slower growth of private sector wage bill, which will decline from 2.2% to 1.3%. This slower growth will be reflected in the spontaneous growth rate of social security revenues. These revenues will be affected by several new measures, such as the full-year impact of the elimination of the exemption of social contributions for overtime pay (and the reallocation to the central government of a basket of taxes then allocated as compensation for the exemption), an increase in contribution rates for the National Retirement Fund for Local government Employees (CNRACL), the National Retirement Fund for Self-Employed Professionals (CNAVPL) and the "work accidents and occupational illness" branch (AT-MP) of the general social security fund, measures affecting the contributions of self-employed workers, increases in taxes on tobacco and beer, the welfare contribution for elderly people living alone levied on retirement pensions, an extension of the tax base and creation of an additional top bracket for the payroll tax ("taxe sur les salaires"), the spill-over effect in 2013 of the 2012 increase in the "forfait social" and the increase in the social security levy on capital income

In 2014, the private sector wage bill growth should rebound gradually, rising from 1.3% to 2.4%, which will boost social security revenue. The growth of this revenue is also affected by the increase in supplementary retirement fund contributions agreed between management and labour representatives, and by the discussion on how to ensure a balanced budget for retirement funds in the short, medium and long run.

From 2015 to 2017, as the economic recovery gains strength, private sector wage bill should grow by 4.0% annually and sustain the growth of social security contributions, which are the main source of social security revenue.

3.6.4 Revenues of local governments

After growing slightly faster than GDP in 2012, local government tax revenue should spontaneously match GDP growth in 2013. Revenue from real property transfer taxes ("*DMTO*") is expected to be down compared to 2012, because of the sluggish real property market, but this decline in revenue should be offset by stronger growth of the business value added contribution and by direct local taxes which are not very sensitive to cyclical fluctuations. There will be low local direct tax hikes. Furthermore, transfers from the central government to local governments (excluding the VAT compensation fund) will remain unchanged in nominal terms compared to 2012.

In 2014, the spontaneous increase in local tax revenue will be closely aligned on GDP growth, as in 2013. Central government transfers to local governments will decrease in nominal terms: in addition to the €750-million cut included in the Public Finance Planning Act, a further €750-million cut will be made as part of the joint effort to contain general government expenditure.

From 2015 to 2017, local taxes will increase in line with GDP growth, with an average elasticity close to 1 over the forecast period. Increases in local tax rates will be larger in 2015 and 2016, reflecting the election cycle. With a further cut of €1.5 billion in 2015, the cumulative cuts in central government transfers between 2013 and 2015 will amount to €3 billion.

3.7 Government debt and stock-flow adjustment

In 2012, a large – albeit reduced – deficit, along with a flat economic growth and the impact of European financial assistance mechanisms, pushed up government debt by 4.4 points of GDP to 90.2% of GDP (87.8% of GDP when excluding the financial support for the euro area, see Box 3 below). The public balance showed a deficit of 4.8%, which is 3.5 points lower than the government debt stabilising point, the latter being particularly high in 2012 (at -1.4% of GDP) because of adverse economic conditions, with nominal GDP growth of only 1.6%, compared to 3.3% in 2011. In addition, the stock-flow adjustments contributed 0.9 point to the increase in the debt-to-GDP ratio. Financial support for the euro area had a major impact, increasing the debt-to-GDP ratio by 1.7 point in 2012, with more loans by the European Financial Stability Facility in the framework of the second bailout plan for Greece and the support for Portugal and Ireland[14]. The capital subscriptions[15] of the European Stability Mechanism (ESM) were significant (€6.5 billion out of a total of €16.3 billion to be paid in instalments until the end of 2016) so that the ESM can rapidly start full-scale operations. These items were only partially offset (for nearly 1 point) by the decrease in general government cash net holdings, and, more specifically, the decrease in the cash holdings of the social security debt redemption fund (CADES) and low interest rates which yielded issuance premiums.

[14] Eurostat decided that the EFSF loans should be recorded directly as debt by the Governments providing the guarantees, in proportion to their guarantees (which correspond to key for subscription of the ECB's capital, once excluded Greece, Ireland and Portugal).

[15] ESM liabilities are not recorded as Government debt under the Maastricht definition, but the financing for the subscription to the ESM capital is recognised as debt if it is borrowing.

Table 11 – Breakdown of variations in the government debt-to-GDP ratio

(% of GDP)	2012	2013	2014	2015	2016	2017
Government debt (excluding support for the euro area)	**87.8**	**90.6**	**91.1**	**89.8**	**87.8**	**85.3**
Government debt	**90.2**	**93.6**	**94.3**	**92.9**	**90.7**	**88.2**
Change in government debt	4.4	3.4	0.7	-1.4	-2.2	-2.6
Differential from debt stabilising fiscal balance	3.5	2.2	0.2	-1.4	-2.1	-2.6
Government balance	*-4.8*	*-3.7*	*-2.9*	*-2.0*	*-1.2*	*-0.7*
Government debt stabilising fiscal balance	*-1.4*	*-1.5*	*-2.7*	*-3.4*	*-3.3*	*-3.3*
Stock-flow adjustment	0.9	1.2	0.5	0.0	-0.1	0.0

In 2013, the government debt ratio should increase less rapidly, rising by 3.4 points of GDP to 93.6% of GDP, as the deficit shrinks. Adverse economic conditions will persist, with nominal GDP growth of 1.7%, meaning that the debt stabilising fiscal balance will remain high at -1.5%, compared to -1.4% in 2012. Efforts to reduce the government deficit to 3.7% of GDP (after 4.8% in 2012), should help slow the increase in debt ratio: the differential from the stabilising point will stand at 2.2 points, compared to 3.5 points in 2012. However, this effect will be attenuated by a larger stock-flow adjustment than in 2012, contributing 1.2 point of GDP, compared to 0.9 point in 2012, despite the smaller share arising from support for the euro area, which should contribute 0.7 point, compared to 1.7 point in 2012, as the EFSF grants fewer loans and the ESM capital subscriptions remain at the same level as in 2012. The stock-flow adjustment should be higher than in 2012 on the assumption of no increase in cash holdings, in contrast to 2012, and the €1.6-billion capital subscription to the European Investment Bank (EIB).

In 2014, the deficit should be brought back down to the debt stabilising point, leading to a very moderate increase in the debt-to-GDP ratio, which should rise by 0.7 point to 94.3%, after a rise of 3.4 points in 2013. **The increase will still be driven by the European financial support programmes.** The combination of a big cut in the deficit, from 3.7% of GDP in 2013 to 2.9% in 2014, and a recovery in economic growth will automatically slow down the debt-to-GDP ratio, with a differential from the debt stabilising point of 0.2 point of GDP. The stock-flow adjustment expected in 2014 comes to only 0.5 point of GDP, primarily because of support for euro-area countries facing financial difficulties (final loan tranches to Ireland, Greece and Portugal granted by the EFSF and last capital subscription for the ESM).

From 2015 to 2017, once structural balance of public finances has been achieved and economic growth stands at 2% in real terms, the debt-to-GDP ratio should start falling by 2 points per year on average. The deficit will be significantly lower than the debt stabilising point of approximately -3.3%, with nominal GDP growth at 3.7%. Furthermore, except for the impact of European financial assistance plans, the stock-flow adjustment is supposed to be neutral from 2015 on. If there are no new loans from the EFSF and with the capital subscriptions for the ESM ending in 2014, the only stock-flow adjustment would be from the start of Ireland's and Portugal's repayments to the EFSF[16] (see Box 3).

[16] Discussions are under way about possibly extending the maturities of loans to Ireland and Portugal, which could result in them coming due after the end of the Stability Programme.

Box 3 – Impact of European financial assistance plans on government debt

As tensions started to emerge on European markets in the fourth quarter of 2009, three Member States of the euro area successively had to call upon European solidarity to finance their debts since markets were demanding excessively high yields.

Ultimately, the impact of financial support for the euro area on government debt will be €67.5 billion by 2017, of which €62.5 billion as soon as 2013.

Table 12 – Debt arising from financial support for the euro area (deviation from baseline)

(€ bn)	2012	2013	2014	2015	2016	2017
Government debt (Maastricht criterion)	**48,1**	**62,5**	**68,7**	**68,7**	**67,5**	**67,5**
of which bilateral loans to Greece	11,4	11,4	11,4	11,4	11,4	11,4
of which EFSF loans to Greece	23,6	29,1	31,6	31,6	31,6	31,6
of which EFSF loans to Irland	2,6	3,8	3,8	3,8	3,1	3,1
of which EFSF loans to Portugal	4,0	5,1	5,6	5,6	5,1	5,1
of which capital endowment to ESM	6,5	13,0	16,3	16,3	16,3	16,3

During the evaluation of compliance with the deficit and debt criteria by the Commission and the Council, the Stability and Growth Pact (Article 2 of Regulation 1467/97 as amended) explicitly calls for special attention to be given to debt incurred in the form of bilateral and multilateral support between Member States to preserve financial stability and debt related to financial stabilisation operations during major financial disturbances.

Three successive financial assistance instruments were set up:

1) Bilateral loans: The Member States belonging to the euro area supported Greece in conjunction with the IMF in the second quarter of 2010. This support took the form of €110 billion in bilateral loans scheduled until the middle of 2013. The EU put up €80 billion[17] (of which €16.8 billion came from France[18]) and the IMF put up €30 billion.

2) European Financial Stability Facility: The Member States belonging to the euro area also created the European Financial Stability Facility (EFSF) to provide assistance to any euro area country that requests it. This facility has a capacity of €440 billion, on top of the €60 billion in the European Financial Stabilisation Mechanism (EFSM), a European Union instrument backed by the EU budget and available to all 27 Member States. **The Member States' guarantees for the EFSF loans are recorded as part of their Maastricht debt** in proportion to their central banks' subscriptions to the ECB's capital (20.39% for France, but since the Member States benefitting from the programmes do not participate, France's share is 21.83%).

The EFSF and the EFSM were used to support Ireland and Portugal. **Ireland** was the first to receive a total of €85 billion in support at the end of 2010, with **€17.7 billion from the EFSF, of which France's share was €3.8 billion**, under a programme running until the end of 2013. In the middle of 2011,

[17] Later lowered to €77.3 billion after Slovakia refused to take part and Ireland and Portugal withdrew.

[18] Only €11.4 billion of the €16.8 billion have actually been disbursed. The remainder was incorporated into the second programme in March 2012 and financed by the EFSF.

Portugal received €78 billion in support, with **€26 billion from the EFSF, of which France's share was €5.6 billion** under a programme to finance Portugal's general government until the middle of 2014.

Following a worsening of Greece's economic and financial situation in the middle of 2011, a **second financial assistance programme for Greece** was introduced in March 2012. The Member States belonging to the euro area and the IMF provided new financing worth an additional €130 billion on top of the undisbursed funds from the first programme covering the period from 2012 to 2014. This financing will be provided by the EFSF, which will also cover the remaining tranches of the bilateral loans granted to Greece, totalling €24.4 billion, plus €9.9 billion not yet disbursed by the IMF. Given the participation of IMF, **the Member States will guarantee a total of €144.6 billion under the second programme, of which €31.6 billion will be provided by France** (including the undisbursed funds from the first programme).

Thus, France has agreed to finance or guarantee €52.4 billion (2½% of GDP) in financial support for the peripheral countries through bilateral loans or the EFSF by the end of 2014.

The first tranches provided to Portugal and Ireland should be repaid by the end of this Stability Programme (2017)[19], for a total of €5.8 billion, which translates into a reduction of €1.2 billion in France's debt. The other tranches of the loan mature after the end of the Stability Programme planning period. The EFSF loans to Ireland and Portugal have a maximum average maturity of 15 years, in keeping with the decision made on 21 July 2011. After the Eurogroup meeting of 26 November 2012, the average maturity of loans to Greece was extended to 20 years for bilateral loans and 32.5 years for EFSF loans.

3) European Stability Mechanism: **The EFSF and the EFSM have stopped granting new loans[20] since the European Stability Mechanism (ESM) came into effect on 28 September 2012.** The EFSF was set up to be a temporary institution and cannot engage in new financial assistance programmes after June 2013. At its December 2010 meeting, the European Council decided, therefore, to set up a permanent mechanism to safeguard the financial stability of the euro area. The ESM is designed to be permanent and to rely not only on government guarantees, but also on paid-in capital.

Eurostat issued an opinion on 7 April 2011, based on the characteristics described in the Conclusions of the European Council of 24 and 25 March 2011, **deeming that the liabilities of the ESM will not be counted as part of the Member States' Maastricht debt[21] and that only their borrowing to finance their subscriptions to the paid-in capital (€80 billion, which works out to €16.3 billion for France or 20.4% of the total) would be recognised as debt.**

This capital will be paid in 5 instalments of €3.3 billion. In accordance with the Statement of the Heads of State and Government at the European Council meeting of 2 March 2011, France's Supplementary Budget Act of 8 February 2012 includes authorisation for €16.3 billion in commitments. France also ratified the treaty establishing the ESM on 8 March 2012. The first two instalments were paid in October 2012, adding €6.6 billion to debt in 2012. The next three instalments should be paid every six months starting in April 2013.

[19] Talks are under way about possibly extending the maturities of loans to Ireland and Portugal, which could result in them coming due after the end of the Stability Programme.

[20] The EFSF is now being managed in run-off mode, which means that the Facility will continue to manage the loans already granted until they are fully repaid and that any new financial assistance will now be provided by the ESM.

[21] Since the ESM is a permanent international institution under international law with a governance structure similar to that of international financial institutions (with a board of governors, a board of directors and a managing director), and a paid-in capital of €80 billion (15% of its commitments during the capital building period).

The ESM made its first disbursements to Spain for its bank recapitalisation programme, which was voted in July 2012. The amount of €41.4 billion disbursed in December 2012 and February 2013 had no impact on France's debt. With the consent of the Eurogroup, given at its meeting of 15 and 24 March 2013, the principle of providing €10 billion in financial assistance to Cyprus was also passed. The first disbursement by the ESM for Cyprus should be made by the end of April. It will not have any impact on France's debt either.

4. Compliance with the Stability and Growth Pact

4.1 Excessive Deficit Procedure (EDP)

4.1.1 Structural adjustment targets in the Council recommendations

Efforts to ensure compliance with the Council recommendations

On 2 December 2009, the Ecofin Council issued a recommendation to France with a view to ending the excessive government deficit observed in 2008. The recommendation called for structural adjustment of more than 1.0 point per year on average over the 2010-2013 period.

Following the 2010-2013 Stability Programme submitted in January 2010, **the Ecofin Council conclusions of 13 July 2010 deemed that France had complied with its recommendation. Since then, the adjustment procedure has been suspended. When France's current Government took power in the second quarter of 2012, it introduced the measures needed to ensure compliance with the structural adjustment target of more than 1.0 points per year between 2010 and 2013 set out in the December 2009 recommendation.** As asked by the Council in its 10 July 2012 recommendation, France has endeavoured to enhance its strategy to consolidate public finances.

The measures introduced in July 2012 ensured compliance with the structural targets, in addition to rigorous management of central government and healthcare expenditure.

The structural effort in 2013 is at a historic level of 1.9 point. The adjustment stems primarily from the effects of measures introduced in the second 2012 Supplementary Budget Act and in the 2013 Budget Act and Social Security Budget Act.

These cumulative efforts in 2012 and 2013 will ensure a 1.6 point reduction in the nominal deficit from 5.3% in 2011 to 3.7% in 2013, despite virtually stagnant economic growth in real terms over two years, which increases the cyclical deficit by 1.2 points, and despite tax disputes that increase the deficit by 0.2 points of GDP in 2013, compared to 2011.

The effort to be made in 2013 has been split between revenue and expenditure to avoid undermining growth, with an emphasis on revenue measures that target large companies and the most well-off households.

A major effort will be made to contain expenditure in 2012 and 2013. Real government expenditure growth (excluding special accounting treatment of certain items[22]) will be limited to 0.8% over the period from 2012 to 2013, which is much lower than the historic trend of slightly more than 2%. All public administrations are contributing to this effort. Central government and Social Security expenditure is governed by the rules in Public Finance Planning Act: zero nominal growth of general budget expenditure, excluding debt service and pensions and the Healthcare Expenditure Growth Target. The operators will contribute to the global effort through contained State transfers and lower allocated tax revenues. Local government will contribute through a freeze in nominal terms of central government transfers.

The measures taken for 2012 and 2013 ensure that the structural adjustment between 2010 and 2013 is greater than 4 points of GDP, in accordance with the recommendation that the European

[22] The proceeds of spectrum auctions, standing at €2.6 billion in 2012, compared to €0.9 billion in 2011 and zero in 2013, are recorded in national accounting as a fall in expenditure. In addition, military spending is recorded in national accounting at the time of delivery and not the time of payment, which can lead to significant variation in Government expenditure. Finally, the recapitalisation of Dexia had a temporary impact of €2.6 billion on Government expenditure in 2012.

Council made to France in December 2009. At the same time, France has confirmed its commitment, under the terms of the Public Finance Planning Act, to achieve structural balance before the end of the current legislature (see Section 3).

Box 4 – Public finance consolidation measures for 2012 and 2013 introduced since the previous Stability Programme

From the day it took power, the Government has faced a difficult economic environment and the prospect, pointed out by the Court of Auditors in its report on the Situation and Outlook for Public Finances, that tax revenues will fall short of the projections of the 2012 Budget Act and the April 2012 Stability Programme. Consequently, the Government quickly introduced revenue and expenditure measures to prevent public finances from deteriorating.

August 2012 Supplementary Budget Act

The August 2012 Supplementary Budget Act included €14 billion in new revenue measures, with €7 billion taking effect in 2012. These measures were the first phase of the tax reform. They primarily targeted the most well-off households and large corporations or the financial sector in order to protect investment and jobs.

Some of the main measures include:

- Smaller allowable deductions for inheritance tax and donation duties. The deduction for inheritance tax will be reduced to €100,000, and the interval between donations will be increased from 10 years to 15 years. However, 88% of inheritances will still be exempt from taxation;
- Doubling the financial transaction tax rate to 0.2% Pending a more radical reform, in keeping with the on-going negotiations in the European Union, the revenue from this tax has been increased;
- A set of measures to combat business tax abuse by restricting the possibilities for tax planning arrangements;
- An increase in the tax on stock options from 14% to 30% for companies and from 8% to 10% for the beneficiaries;
- An increase in the minimum tax on Social Security-exempt benefits paid by employers ("*forfeit social*") from 8% to 20%;
- Elimination of the exemption on overtime pay, except for employers' contributions in SMEs with fewer than 20 employees that benefit from a flat-rate reduction;

The Supplementary Budget Act also introduced temporary measures for 2012, such as the corporate income tax payment on 2012 taxable income for large corporations, the wealth-tax payment on assets in excess of €1.3 million, which is a temporary measure pending wealth tax reform, the contribution on the value of petroleum product inventories, which was introduced to make oil companies contribute to the consolidation effort.

At the same time, the Government introduced expenditure saving measures to address the major risks identified in the Court of Auditors' public finance audit report published in July 2012 and estimated at between €1.2 billion and €2.0 billion. A further €1.5 billion in central government expenditure was frozen. This strict control of expenditure was upheld by the November Supplementary Budget Act, in which any new appropriations to cover overruns were fully offset by cancelling other appropriations. At the end of 2012, the appropriations cancelled and set aside in reserves reached the very high figure of €2.7 billion, which is twice as much as in 2010 and 2011. Ultimately, the measures introduced in 2012 produced a historical tightening of central government expenditure: excluding debt service and pensions, expenditure met the objective, which had been lowered by €2.4 billion compared to the 2012 draft Budget Bill, and was even under target by €0.1 billion. Expenditure including debt service and pensions posted a historical decline of €0.3 billion compared to 2011, in contrast to an average increase of €5 billion to €6 billion per year over the previous five years.

The provisional figures regarding the 2012 Healthcare Expenditure Growth Target indicate that expenditure was nearly €1 billion under target in 2012, which testifies to the progress achieved in containing expenditure since the target was introduced in 1996. These results are testimony to the Government's determination to contain long-term healthcare expenditure growth and to the effectiveness of the new governance framework with greater involvement of the Early Warning Committee.

The 2013 Budget Act and the 2013 Social Security Budget Act

The 2013 Budget Act and the 2013 Social Security Budget Act have continued the consolidation effort, with an adjustment of €30 billion in 2013, split between €20 billion in revenue measures and €10 billion in cuts in central government expenditure, along with the savings made possible by a Healthcare Expenditure Growth Target that is much lower than the historical trend.

Additional levies on companies introduced in 2013 are mainly targeted at large corporations, so as to strike a better balance of taxation in favour of SMEs and intermediate-sized enterprises. The main measures are as follows:

- A cap on deductions for financial expense, which corrects the previous rules, which were excessively favourable for debt financing. This measure spares SMEs, since it only applies when net financial expense exceeds €3 million;
- Limits on the exemption for long-term capital gains accruing to companies selling equity securities;
- Changes to the arrangement for carrying losses forward for companies subject to corporate income tax, by lowering the rate at which taxable income can be offset by losses carried forward;
- Changes in the rules on end-of-year advance payment of corporate income tax, with a lower turnover threshold of €250 million at which the advance is compulsory.
- Introduction of a tax on insurance companies' capitalisation reserves.

Measures targeting households are designed to make personal income tax more progressive:

- A new 45% tax bracket for income in excess of €150,000, adjusted for family composition (*"quotient familial"*);
- A cap on the "*quotient familial*" lowered at €2,000;
- Taxing dividends and fixed-income yields at progressive rates, along with capital gains on equity holdings, which means that capital income is now taxed in the same way as labour income;
- A larger income tax deduction for the least well-off households;
- A lower overall cap on tax exemptions of €10,000 (down from €18,000 plus 4% of the household's taxable income);
- Wealth tax reform with more progressive rates.

In addition to these increases in revenue, the 2013 central government budget calls for a reduction of more than €10 billion in expenditure.

A savings of €10 billion will be achieved, with €9 billion to offset the trend in expenditure growth and €1 billion to offset new measures, such as hiring teachers, subsidised contracts as part of the Jobs for the Future programme and civic service programmes. These savings rely on a series of measures. A reduction of the appropriations for all ministries' operating costs and no change in payrolls produce savings of €2.8 billion. Defence expenditure will be €2.2 billion less than estimated in the Military Planning Act and central government capital expenditure will be reduced by €1.2 billion by postponing or cancelling projects that are not priorities and by streamlining investment in transport infrastructure. Improved targeting and stricter guidelines for central government intervention will produce savings of €2 billion. Central government operators and local governments will also take part in the consolidation effort, contributing savings of €1.8 billion through stabilisation or reductions in transfers and reductions in the tax revenue allocated to them.

In addition to this effort to contain expenditure growth, the €837-million increase in the levies on revenue allocated to the European Union under the Supplementary Budget Act passed at the end of 2012 will be offset during the year.

Securing the structural effort in 2013

All measures giving rise to new expenditure will be offset by savings on other items in accordance with the commitments that the Prime Minister made in the Circular dated 14 January 2013 entitled "Rules for Responsible Management of Government Expenditure". The Circular explains the principle of self-insurance for programmes (see Section 3 on central government expenditure) and the principle that any new expenditure must be matched by equivalent savings, and that no expenditure can be financed by increasing revenue. Nor can new taxes or increases in existing taxes be used to justify an increase in expenditure.

Furthermore, management and labour reached an agreement in March 2013 on a flat-rate increase of supplementary retirement benefits that is lower than inflation in 2013, and equal to inflation minus 1 point in 2014 and 2015. They also agreed to increased contribution rates in 2014 and 2015.

4.1.2 Governance and quality of public finances

Furthermore, in accordance with the Ecofin Council's recommendation, France will continue to implement measures aimed at:

- Improving the quality of public finances, especially through the "modernisation of public action" (MAP) process (see Section 6);
- Improving public finance governance by transposing the "Budgetary Framework" Directive, ratifying the Treaty on Stability, Coordination and Governance and enforcing the Constitutional Bylaw on Public Finance Planning and Governance (see Section 8);
- Improving the long-term sustainability of public finances through fiscal consolidation measures, backed up by structural reforms to stimulate growth and the on-going talks to restore the sustainability of France's retirement system (see Section 7);
- Containing government expenditure, by making spending more cost-effective in particular (see Section 6.2.4);
- Simplifying the tax system by reducing tax loopholes (especially exemptions that tend to favour debt financing), and shifting tax pressure from work to other forms of taxation that weigh less on economic growth (see Section 6.3).

4.1.3 Structural adjustment in 2014

Given the deterioration of the macroeconomic environment, France requested that the return to a deficit under 3% of GDP be postponed until 2014 and is planning for this purpose a major structural adjustment of 1.0 point of GDP.

France's efforts between 2010 and 2013 comply with the Council's recommendations, but do not enable France to achieve the nominal target of 3% of GDP in 2013 because of the sharp downturn in the macroeconomic environment.

To ensure that the nominal target of 3% is met in 2014, the Government will achieve a structural adjustment of 1.0 point of GDP in 2014. Under the Commission's very conservative potential growth assumption, this corresponds to a structural adjustment of more than ¾ point of GDP.

4.2 Compliance with the Preventive Arm of the Stability and Growth Pact

The budgetary framework set out in this document should enable France to exit the Excessive Deficit Procedure in 2015, with the notification of the 2014 deficit. After that, the rules of the preventive arm of the Stability and Growth Pact[23] would apply: In addition to the main structural adjustment criterion that applies as soon as exiting the Excessive Deficit Procedure and as long as the medium-term budgetary objective has not been attained, there is a rule on growth of government expenditure net of discretionary revenue measures in the preventive arm of the Pact[24], and the debt criterion now defining the entry into the corrective arm[25] of the Pact along with the 3% criterion for the Maastricht deficit.

4.2.1 Progress towards the medium-term budgetary objective

The 2012-2017 Public Finance Planning Act sets structural balance of public finances as the medium-term budgetary objective and describes the trajectory for achieving this objective. This trajectory is the benchmark for this Stability Programme. It complies with the requirements of the preventive arm of the Stability and Growth Pact.

Once a country exits the Excessive Deficit Procedure and, as long as the medium-term budgetary objective has not been attained, the Growth and Stability Pact requires structural adjustment of at least 0.5 point of GDP per year[26].

The structural balance trajectory described in this Stability Programme is compatible with these requirements, since it describes structural adjustment in excess of 0.5 point per year in 2015 and 2016, after bringing the deficit back down under 3% in 2014 (see Section 3.3). It also leads to achieving our medium-term budgetary objective of structural balance in 2016.

[23] The reform of the Pact was completed in October 2011 when the Council and the European Parliament adopted the set of five Regulations and one Directive usually called the "six pack". In particular, Regulations 1466/97 and 1467/97 were amended by Regulations 1175/2011 and 1177/2011.

[24] Regulation 1466/97 amended by Regulation (EU) No 1175/2011 of the European Parliament and of the Council of 16 November 2011.

[25] Regulation 1467/97 amended by Regulation (EU) No 1177/2011 of the European Parliament and of the Council of 8 November 2011.

[26] Article 5 of Regulation 1466/97 as amended.

4.2.2 Compliance with the expenditure benchmark net of discretionary revenue measures

Under the preventive arm of the Stability and Growth Pact, the real growth of general government expenditure, net of new revenue measures, should not, depending on the country's position with respect to its medium-term budgetary objective "*exceed a reference medium-term rate [or for countries that have not yet reached their medium-term budgetary objective a rate below a reference medium-term rate] of potential GDP growth, unless the excess is matched by discretionary revenue measures*."[27]

This rule is part of an overall assessment that uses the structural balance as a benchmark. It makes it possible to focus on the components of structural adjustment that are under the direct control of lawmakers: expenditure excluding interest, and discretionary revenue measures.

Therefore, it is similar to the notion of structural effort used in Section 3.3, with the main difference being the exclusion of interest expense. However, the presentation is different. It is expressed as an expenditure growth rate net of new revenue measures for comparison to the medium-term reference GDP growth rate.

Compliance with this rule under the preventive arm is assessed as follows.

- The variable considered is general government expenditure, excluding interests and the cyclical component of unemployment benefit expenditure, and net of discretionary revenue measures. In addition, investment, which may be a very volatile component of expenditure, especially for small countries, is averaged over three years.
- Real government spending growth is calculated using the GDP deflator.
- The reference GDP growth rate is the Commission's average potential growth rate, set at the start of 2013 for the three years 2014, 2015 and 2016.
- The rule requires real spending growth, net of discretionary revenue measures, to be slower than the reference GDP growth for countries that have not achieved their medium-term budgetary objective. The difference should ensure a structural adjustment of 0.5 point per year.

In the case of France, the Commission's reference growth rate of 1.1% for 2015 to 2016, along with the weight of primary expenditure (*i.e.* expenditure excluding interest expense) in GDP, mean that real expenditure growth, net of new revenue measures, would have to be around 0.2% to be compatible with a structural adjustment of 0.5 point. Once the medium-term budgetary objective has been met, the expenditure growth rate that maintains the objective will be the potential growth rate. Thus France will comply with the expenditure benchmark, with real expenditure growth (excluding interest expense) net of discretionary revenue measures around 0.2% in 2015 and 2016, therefore providing a contribution of 0.5 point to structural adjustment[28].

4.2.3 Compliance with the debt criterion under the corrective arm of the Pact

The debt criterion has now been added to the deficit criterion for triggering or exiting an excessive deficit procedure. The debt criterion is aimed at ensuring that the debt-to-GDP ratio returns to the 60% threshold at a satisfactory pace. Under Article 126 of the Treaty on the Functioning of the European

[27] Regulation 1466/97 as amended.

[28] The contribution would be about 0.7 point per year, taking the 2015-2017 Public Finance Planning Act average potential growth as the reference growth rate.

Union, the Commission shall monitor whether the ratio of government debt to GDP exceeds the 60% reference value "*unless the ratio is sufficiently diminishing and approaching the reference value at a satisfactory pace*". The corrective arm of the Pact as amended by the "Six-Pack" calls for the difference between the current debt-to-GDP ratio and the 60% target to be reduced by an average of one twentieth per year over three years[29].

Given France's level of government debt, an average reduction of 1.5 percentage point of GDP per year is required to meet the criterion, whereas the average reduction planned between the end of 2014 and the end of 2017 is around 2 percentage points of GDP per year. The trajectory for a return to structural balance of public finances in the medium term produces a deficit that is much smaller than the debt stabilising point, which, with 3¾% of nominal economic growth, stands at around -3% of GDP. In this context, **the public finance trajectory described in this Stability Programme complies with the debt criterion between 2015 and 2017**.

However, for countries that were in the Excessive Deficit Procedure in November 2011, as was the case for France, there is a 3-year transition period after exiting the current Procedure in which the debt criterion does not apply, but these countries must achieve enough progress during the transition period to ensure that they comply with the rule at the end of the 3 years. According to the Commission's latest calculations, France needs to achieve structural adjustment of at least 0.2 point per year starting in 2014 to meet the criteria as of 2017[30]. This is less than the minimum structural adjustment required to converge to the medium-term budgetary objective of structural balance. The trajectory in the Stability Programme produces more than enough structural adjustment to ensure compliance with the debt criterion in 2017. In fact, compliance will be achieved in the period 2015-2017.

[29] Article 2 of Regulation 1467/97 as amended by Regulation (EU) No. 1177/2011 of the European Parliament and of the Council of 8 November 2011.

[30] During the transition period, Member States are required to comply with a minimum linear structural adjustment. The Commission defines this adjustment by defining a linear adjustment trajectory for the structural balance that would result in compliance with the benchmark at the end of the transition period. The "minimum" trajectory would consist of (i) deviating by no more than 0.25% of GDP from the defined structural adjustment, and (ii) not being more than 0.75% off the adjustment target in aggregate. If either of these criteria is not met, the Commission will deem that progress is "insufficient".

5. Sensitivity analysis and comparison to the previous programme

5.1 Sensitivity to external assumptions

The international scenario on which the projections are based is as follows:

- Oil prices remain at $114.00 per barrel after 2013[31];
- It is conventionally assumed that the exchange rate between the euro and the dollar will be US$1.31[32] during the entire period under review;
- The growth rates of the global economy and world trade will gradually return to their long-term average. Demand for France's exports should grow by 6.5% per year starting in 2014, which is consistent with its average growth over the last 25 years, following growth of 0.8% in 2012 and 2.6% in 2013.

The assumptions outside the European Union are very similar to those used by the Commission for its winter forecasts. However, the latest oil prices and exchange rates are more in line with the figures given above. The Stability Programme sets out below the estimated average expected impacts of stronger growth of demand for France's exports, rising oil prices, a depreciation of the euro and a temporary rise in interest rates. The effect of symmetrical shocks (weaker growth of export demand, etc.) can be derived by changing the sign.

5.1.1 Impact of stronger demand for France's exports

Virtually all of the impact of an increase in world demand for French goods and services would be passed on to exports, after which it would spread to the rest of the economy, primarily through increased business investment.

Assuming constant nominal interest rates, a permanent increase of 1% in world demand would boost growth by about ¼ point of GDP and generate about 40,000 extra jobs after three years. With no change in exchange rates, the impact on inflation would be low[33].

This shock combines a substantial increase in growth with an improvement in the job market, with relatively little effect on inflation. Stronger growth of tax bases and payrolls would have a positive impact on government revenue (VAT, personal income tax, social contributions and other taxes). The slight impact of this demand shock on inflation will cause little change in expenditure growth, which will be slower than revenue growth. Ultimately, the government’s net lending would rise by approximately 0.1 percentage points of GDP starting in the second year.

[31] A technical assumption is also made that the price of oil in euros and in dollars will increase at a rate of 1.75% per year starting in 2015.

[32] US$1.32 on average in 2013 on the basis of the exchange rates observed at the beginning of the year.

[33] In this variant, the price of oil is considered exogenous and thus unresponsive to changes in demand for France’s exports.

Table 13 – Impact on the French economy of a 1% increase in world demand for French goods (*)

(deviation from the baseline scenario in %)	n	n+1	n+2
GDP	0.2	0.2	¼
Total payroll employment (thousands)	9	27	40
Household consumption deflator	0.0	0.1	0.1
Net government lending/borrowing (in % points of GDP)	**0.0**	**0.1**	**0.1**

(*) Sustained 1% increase in export demand at the start of year n with no change in real interest rates.

5.1.2 Impact of higher oil prices

Higher oil prices increase imported inflation and raise consumer prices directly, at constant exchange rates. In addition to this automatic price rise, the inflationary impact of dearer oil also stems from the resulting rise in businesses' production costs and labour costs, as wages quickly adjust to higher prices. Higher consumer prices, combined with the weakening of corporate profits, have a negative impact on growth. This impact would also be felt in other countries that are net oil importers, leading them to contribute less to the demand for France's exports. On the positive side, the fact that France's producer prices are less sensitive to oil prices than those of its main trading partners results in price competitiveness gains for France. In addition, higher oil prices sustain the growth of net oil exporters by increasing their oil revenues.

A macroeconomic equilibrium model with the rest of the world suggests that a sustained $20 increase in the price of a barrel of oil would lead to a reduction of growth by 0 to 0.1 percentage points at constant real interest rates or exchange rates. It would also increase consumer prices by 0.3 percentage points in the first year compared to no change in oil prices. After three years, the impact would be a reduction of growth by 0.2% and the loss of some 60,000 jobs.

Table 14 – Impact on the French economy of a $20 increase in oil prices (*)

(deviation from the baseline scenario in %)	n	n+1	n+2
GDP	-0.1	-0.2	-0.2
Total payroll employment (thousands)	-3	-28	-62
Household consumption deflator	0.3	0.8	1.2
Net government lending/borrowing (in % points of GDP)	**0.0**	**-0.1**	**-0.2**

(*) $20 increase in the price of a barrel of oil at the beginning of year n, with no change in real interest rates, endogenous reaction of the rest of the world.

Higher oil prices would have mixed consequences for government revenue. On the one hand, a drop in economic growth would have a negative impact on general government tax revenues until the third year, especially revenue from corporate income tax. On the other hand, revenues that vary with inflation and wage increases, such as the VAT, personal income tax and social security contributions, would show an increase in nominal terms. The overall net impact on revenue would be slightly positive. In contrast, faster spending growth, primarily as a result of higher inflation and job losses, would start to be felt in the second year and would continue into the third year. Consequently, the government balance would deteriorate by 0.1 percentage points of GDP in the second year and by 0.2 points in the third year.

5.1.3 *Impact of a depreciation of 10% of the euro vis-à-vis all other currencies*

If the value of the euro depreciated against all other currencies, it would automatically improve France's price competitiveness compared to countries outside of the euro area and boost growth in the other euro area countries. The increase in exports would create more growth and jobs. As in the rest of the euro area, inflation would be increased by a depreciation of the effective exchange rate.

A macroeconomic equilibrium model with the rest of the world shows that, at constant real interest rates, a 10% depreciation of the euro against all other currencies would increase growth by 0.6 percentage points and raise consumer prices by 0.5 percentage points in the first year compared to a situation with no depreciation in the value of the euro. The impact after three years would be a 1.2-point contribution to growth, 150,000 new jobs and a 1.2-point rise in consumer prices.

Table 15 – Impact on the French economy of a 10% depreciation of the euro against all other currencies (*)

(deviation from the baseline scenario in %)	n	n+1	n+2
GDP	0.6	1.0	1.2
Total payroll employment (thousands)	30	85	149
Household consumption deflator	0.5	0.7	1.2
Net government lending/borrowing (in % points of GDP)	**0.2**	**0.4**	**0.6**

(*) A 10% depreciation in the value of the euro against all other currencies at the beginning of year n, with no change in real interest rates, endogenous reaction of the rest of the world.

A depreciation of the euro would have a positive impact on most taxes and therefore on public finances due to faster growth and inflation. A lower exchange rate would also increase social security contributions (which are based on total payrolls). This impact would be only partially offset by an increase in expenditure stemming from higher inflation. All in all, the government balance would improve by 0.4 percentage points of GDP in the second year and by 0.6 points in the third year.

5.1.4 *Impact of a temporary 100-basis-point rise in the ECB's key rates*

A temporary rise in the European Central Bank's key interest rates, in response to an economic recovery, for example, and the consequent increase in long-term interest rates would hamper growth in three main ways.

- Productive investment would be affected by an increase in interest rates, since higher interest expenses would weaken solvency and lower profitability of capital.
- Higher rates would promote savings at the expense of consumption by virtue of the substitution effect. They would also make home loans more expensive and thus discourage investment in housing.
- Higher interest rates would strengthen the euro and hinder growth through a loss of competitiveness vis-à-vis countries outside the euro area.

A 100-basis-point increase in short-term interest rates in the euro area lasting two years would reduce growth in France by 0.2 percentage points of GDP in the first year and by 0.3 points in the second year.

The negative impact would be attenuated starting in the third year, as interest rates and exchange rates return to their pre-shock levels. However, consumer prices would still be 0.2 percentage points lower in the third year and the negative impact on employment would be strongest in the third year, with 45,000 job losses.

These evaluations take into account the effects of macroeconomic equilibrium with the rest of the world, and, in particular, the negative impact on France's economy caused by weaker demand from France's partners in the euro area suffering from the same interest rate increases.

Table 16 – Impact on France's economy of a 100-basis-point increase in short-term interest rates for two years (*)

(deviation from the baseline scenario in %)	**n**	**n+1**	**n+2**
GDP	-0.2	-0.3	-0.1
Total payroll employment (thousands)	-10	-36	-45
Household consumption deflator	-0.1	-0.1	-0.2
Net government lending/borrowing (in % points of GDP)	**-0.1**	**-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 that has an impact on long-term interest rates and on the value of the euro and endogenous reaction of the rest of the world.

An increase in interest rates would adversely affect public finances in two ways. First, general government debt service would increase because the cost of financing the deficit and refinancing the stock of debt would rise. Secondly, slower growth would cause a deterioration of public finances.

In the first two years, lower demand and the deflationary impact of an interest rate shock would automatically reduce revenues from taxes and social security contributions. At the same time, job losses would increase expenditure on unemployment benefits and the temporarily higher interest rates would increase the cost of debt service. The impact of lower inflation on other government spending would only partially offset this effect, since some of such expenditure is determined by rules set in advance in nominal terms: central government expenditure, excluding debt service and pensions, and the National Healthcare Expenditure Growth Target. The negative impact on the government balance will be weaker in the third year, but it will still be significant because payrolls will still be smaller than in the baseline scenario.

5.2 Comparison with the previous Stability Programme and the Commission's forecasts

Table 17 – Comparison of the 2013-2017 Stability Programme with the European Commission's forecasts and the 2012-2016 Stability Programme

	2011	2012	2013	2014	2015	2016	2017
2013-2017 Stability Programme (April 2013)							
Real GDP growth*	1.7	0.0	0.1	1.2	2.0	2.0	2.0
Government balance (% of GDP)	-5.3	-4.8	-3.7	-2.9	-2.0	-1.2	-0.7
Structural balance (% of potential GDP)	-4.9	-3.7	-2.0	-1.0	-0.2	0.2	0.5
Structural adjustment (% of potential GDP)		*1.2*	*1.8*	*1.0*	*0.7*	*0.5*	*0.2*
Government debt (% of GDP)	85.8	90.2	93.6	94.3	92.9	90.7	88.2
Government debt, excl. support for the euro area (% of GDP)	85.1	87.8	90.6	91.1	89.8	87.8	85.3
European Commission's Winter Forecasts (February 2013)							
Real GDP growth	1.7	0.0	0.1	1.2			
Government balance (% of GDP)	-5.2	-4,6**	-3.7	-3.9			
Structural balance (% of potential GDP)	-4.5	-3.3	-2.0	-2.2			
Structural adjustment (% of potential GDP)		*1.2*	*1.3*	*-0.2*			
Government debt (% of GDP)	86.0	90.3	93.4	95.0			
2012-2016 Stability Programme (April 2012)							
Real GDP growth	1.7	0.7	1.75	2.0	2.0	2.0	
Government balance (% of GDP)	-5.2	-4.4	-3.0	-2.0	-1.0	0.0	
Structural balance (% of potential GDP)	-3.7	-2.6	-1.2	-0.4	0.4	1.2	
Structural adjustment (% of potential GDP)	*1.9*	*1.2*	*1.4*	*0.8*	*0.8*	*0.8*	
Structural adjustment recalculated using the potential growth rate from the Public Finance Planning Act	*1.6*	*1.0*	*1.2*	*0.8*	*0.7*	*0.8*	
Government debt (% of GDP)	85.8	89.0	89.2	88.4	86.4	83.2	
Government debt, excl. support for the euro area (% of GDP)	85.1	86.6	86.5	85.4	83.3	80.4	

** quarterly accounts, unadjusted data   ** excluding recapitalisation of Dexia, which has been recorded as an expenditure*

5.2.1 *Comparison with the 2012-2016 Stability Programme from April 2012*

In 2012, the government deficit according to the Maastricht definition was held down to 4.8% and structural adjustment was in line with the previous Stability Programme. To meet this target, the government managed expenditure very rigorously, which enabled it to offset the central government expenditure overruns estimated at some €2 billion and identified by the Court of Auditors. The Government also introduced consolidation measures in July 2012 that yielded more than €7 billion. Without these measures, the structural adjustment called for in the 2012-2016 Stability Programme would not have been achieved. On the other hand, the 0.4-point reduction of the nominal deficit was smaller than the 0.8-point reduction called for in the April 2012 trajectory. The deviation stems from one-off events, such as the recapitalisation of Dexia, and an economic downturn that caused revenue to fall short of the April 2012 forecasts. The April 2012 Stability Programme assumed that GDP would grow by 0.7% in 2012. France's national statistics institute, INSEE, is now estimating that GDP growth was 0.0%. This economic downturn has deepened the government deficit, largely as a result of automatic stabilisers, with slower revenue growth and higher expenditure on unemployment insurance benefits. These effects were exacerbated in 2012 by a sharp drop in capital income, especially dividend income.

In 2013, the effects of the measures introduced in July 2012 and the measures introduced in the 2013 Budget Act and the 2013 Social Security Budget Act have greatly stepped up the structural efforts compared to the programme set out in April 2012. Therefore, the main reason for the smaller improvement in the nominal government balance (1.1-point versus 1.4-point in the previous Stability Programme) is the sharp economic downturn in the economy, with 2013 growth expected to be 0.1%, compared to an estimate of 0.8% in October 2012 and an estimate of 1.75% in April 2012.

Box 5 – Revision of the structural balance level since the last Stability Programme

The 2011 structural deficit has been revised upward since the April 2012 Stability Programme, from 3.7% of GDP to 4.9%. This reflects the downward revision of the output gap in 2011, which reduces the cyclical component of the deficit and increases the structural component. Furthermore, potential growth in the following years has also been revised downward, which reduces the structural adjustment for a given economic growth rate and a given reduction of the deficit in nominal terms.

These revisions stem primarily from an upward revision of the magnitude of the shock caused to potential GDP level by the 2008-2009 crisis and through its impact on total factor productivity growth. This shock of approximately 2.5 points has been revised upward since the release of the previous Stability Programme, in conjunction with the revision of the national accounts following the publication of the provisional 2011 accounts in May 2012. The revision reduced the output gap in 2011.

Furthermore, in view of the uncertainty and dispersion of potential growth estimates, the Government decided to use a conservative conventional assumption of gradual recovery in total factor productivity growth and, consequently, a gradual increase in the potential growth rate starting in 2011. This rate should rise from 1.1% in 2011, to 1.6% in 2017, thanks to the reforms to be introduced during the current legislature and the gradual convergence with the long-term trend of labour productivity growth.

On the other hand, actual growth has not been as strong as expected, which has increased the output gap for a given potential growth rate.

Ultimately, the negative output gap at the start of the period is smaller than what was assumed for the last Stability Programme, because of the revision of the shock to total factor productivity growth during the crisis. However, the gap is virtually the same in 2016, since actual growth between 2012 and 2014 has also been revised downward.

	2011	2012	2013	2014	2015	2016	2017	Average 2011-2016
2012-2016 Stability Programme (April 2012)								
Effective growth rate	1,7	0,7	1,75	2,0	2,0	2,0		1,7
Potential growth rate	1,7	1,7	1,7	1,7	1,7	1,7		1,7
Output gap	-2,8	-3,7	-3,6	-3,3	-3,0	-2,7		
2013-2017 Stability Programme (April 2013)								
Effective growth rate	1,7	0,0	0,1	1,2	2,0	2,0	2,0	1,2
Potential growth rate	1,1	1,3	1,4	1,5	1,5	1,6	1,6	1,4
Output gap	-0,8	-2,0	-3,3	-3,6	-3,1	-2,7	-2,3	

The outlook for growth **in 2014** has been revised downward from 2.0% in the previous Stability Programme to 1.2%. The reduction of the government deficit from 3.7% of GDP to 2.9% between 2013 and 2014 will nonetheless be in line with the reduction in the previous Stability Programme (0.8 point versus 1.0 point) thanks to a greater structural adjustment.

The government debt ratio (excluding loans to euro-area countries facing financial difficulties) will start to decline in 2015, which is one year later than called for in the previous Stability Programme, as a result of the impact of slower growth on the government debt ratio: the nominal deficit will be larger because of the cyclical component, and, for a given level of nominal debt, the debt stabilising point is higher when growth is flat.

5.2.2 Comparison with the European Commission's 2013 winter public finance forecasts

In its winter forecasts published on 22 February 2013, the European Commission forecasted that France's government deficit would stand at 4.6% of GDP in 2012, 3.7% in 2013 and 3.9% in 2014, under its usual no-policy-change assumption and with **growth rates in 2012, 2013 and 2014** that are identical to the ones used by the Government in this Stability Programme.

Under these assumptions, the deficit projections are **very similar in 2012 and identical in 2013**. The small discrepancy in 2012 stems largely from the recognition of the recapitalisation of Dexia as an expense, whereas the Commission had not made this change, pending Eurostat's ruling. **In 2013**, the growth forecasts are identical, as are the deficit forecasts.

In 2014, the 1.0-point differential in the deficit forecast (2.9% of GDP for the Government and 3.9% for the Commission) stems primarily from the European Commission's usual no-policy change assumption. More specifically, the Commission's forecasts do not incorporate the commitment made in the Public Finance Planning Act to offset temporary measures in 2013, the measures that the Government will introduce to offset the lower-than-expected returns on certain measures, such as the Financial Transactions Tax, and Constitutional Council's overturning certain measures, such as the one-off tax on very high income. In addition, the Commission's forecasts do not include some savings measures at this point, such as the expenditure cuts planned to finance the Competitiveness and Jobs Tax Credit. Nor do they include the effects in 2014 of the agreement between labour and management on supplementary retirement schemes (Agirc and Arrco) signed on 13 March 2013, after the Commission's forecasts were published. The Commission's forecasts also don't take into account the reduction of tax exemptions and the stepped up fight against tax fraud and tax evasion (see Section 6.3).

6. Quality of public finances

6.1 General strategy

Restoring the balance of public finances goes hand in hand with attention to the quality of public finances both on the expenditure side and on the revenue side.

The Government launched a crosscutting modernisation of public action process on 18 December 2012 in order to improve the economic efficiency and targeting of government expenditure. During the course of this legislature, running from 2012 to 2017, all public policies will be evaluated, including policies implemented in partnership with social security funds and with local governments. Evaluation of a first series of 40 policies starts in the first half of 2013, focussing on support for businesses (direct individual grants, organisation of local economic development players), family benefits, vocational training and local level of housing policy. The modernisation of public action will help reduce expenditure while improving services to users. The Interministerial Committee for modernisation of public action (CIMAP) meeting in April 2013 added 9 policies to the list to be evaluated in the second half of 2013.

In addition, a comprehensive investment strategy has been defined, with a redeployment of the Invest for the Future Programme appropriations. This strategy emphasises the priorities in the National Pact for Growth, Competitiveness and Jobs, and, as far as governance is concerned, the prioritisation of public investment projects. Pursuant to Article 17 of the 2012-2017 Multiyear Public Finance Planning Act passed on 31 December 2012 investments by the central government and government agencies (including healthcare institutions) will be subjected to systematic social and economic evaluations in order to concentrate funds on the projects that are most useful for the community. When investment amounts exceed a certain threshold, an independent counter evaluation will be conducted under the aegis of the General Commission for Investment, which answers directly to the Prime Minister.

In addition to this crosscutting process, Social Security and local government expenditure will also be optimised. Social security funds will curb their operating expenditure and aim at rationalising healthcare expenditure and reforming social benefits, in particular family benefits, so as to target the groups that need them most. The bills submitted to the Council of Ministers on 10 April on decentralisation and Government reform will promote containment of local government expenditure.

The National Pact for Competitiveness, Growth and Jobs also contributes to the quality of public finances, both on expenditure and revenue sides, by cutting the labour costs through the Competitiveness and Jobs Tax Credit and enhancing the companies' competitiveness. Savings on general government expenditure will finance half of the cost of this tax credit.

Revenue efficiency is also a priority, with efforts to reduce exemptions from taxes and social security contributions, to fight tax fraud and to increase the tax system's fairness and economic efficiency.

6.2 Quality of government expenditure

6.2.1 The modernisation of public action

The modernisation of public action is a bold initiative to enhance the efficiency of public services while consolidating public finances. It requires all players to make efforts to be more efficient and spend less.

The modernisation of public action process covers all aspects of public expenditure to achieve compliance with the financial trajectory that France has chosen in order to restore structural balance by 2016. It uses a new method to evaluate all public policies with input from all of the stakeholders. An Interministerial

Committee for modernisation of public action (CIMAP) chaired by the Prime Minister meets once every three months. It is the decision-making and monitoring body for modernisation. A Secretariat-General for modernisation of public action (SGMAP) that reports to the Prime Minister is responsible for preparing and examining the decisions made at the quarterly meetings.

After the Committee's first meeting on 18 December 2012, the Government initiated the four main projects that make up the modernisation of public action programme. The first two projects are evaluations of public policies and Ministerial Modernisation and Streamlining programmes. They should make a direct contribution to compliance with the trajectory for consolidating public finances that the Government has committed to, in addition to making appropriate and crucial improvements to service quality. The other two projects to streamline the administrative environment and speed up the digital transition will help build more efficient public services that are more attuned to users' needs and less of a burden for taxpayers.

The first major project is the systematic evaluation of the efficiency and costs of public policies that involves all of the stakeholders. The involvement of all of the stakeholders, in keeping with the new European guidelines on public finance coordination and governance, is the key to the success of this process, which aims to rethink public intervention in order to produce sustainable and structural savings. Each meeting of the Interministerial Committee should be an opportunity to announce a new series of evaluations. The first series was launched in January 2013 and focuses on 27 public policies affecting all aspects of expenditure, including expenditure of central government and central government agencies, local governments and social security funds. The policies being evaluated account for 20% of total government expenditure. The second series saw the launch of 13 more evaluations and, following the second meeting of the Committee in April 2013, 9 new evaluations were announced, including support for young people entering the job market, coordination between unemployment benefits and welfare benefits, optimisation of military maintenance procurement and location of research units, and the possibilities for pooling resources with universities. The choices are made in consideration of different criteria: the prioritisation of policies in the Government's agenda by virtue of the issues involved; the number of tools and structures that require clarification; the size of the budgets involved and the potential for improving efficiency and effectiveness. Each ministry will see at least one of its public policies evaluated in 2013.

The scope and operating procedures for evaluations are defined for each ministry in accordance with the specific features of their policies and their objectives. There is no single evaluation method or uniform set of objectives. Some policies may be improved by promoting organisational improvements or streamlining.

Other public policies will require structural reform to produce savings without affecting their effectiveness. **Three main types of policies are primarily concerned: support for businesses, vocational training and family benefits.**

There are more than 7,000 Government schemes in place to support businesses. This number makes access to support very complex. In addition, not all of the schemes have proven to be efficient. This explains why the evaluation of support for businesses should contribute to compliance with the trajectory for consolidation of France's public finances set out in the Multiyear Public Finance Planning Act of 31 December 2012 and produce savings of €2 billion by 2015.

Evaluation of vocational training and financial support for apprenticeships has also started with the aim of targeting the groups that need the most support more effectively.

In another area, since more than half of government expenditure goes to Social Security, it is crucial to ensure that the benefits system is efficient and fair. Family benefits play an important role in meeting the costs related to rearing children, but the targeting of these benefits is not always appropriate and the persistent deficit of the family branch of Social Security leads to unsustainable borrowing to finance permanent costs. Therefore, the evaluation of this aspect of public policy should review the overall system architecture, the efficiency of the benefits and the targeting of family allowances in order to curb expenditure substantially, starting in 2014, in order to bring the family benefit system back into balance, without affecting the lowest-income families.

The second project deals with Ministerial Modernisation and Streamlining programmes and specifically covers central government and central government agencies. It has two aspects. The first focuses on improving service quality for users and citizens and the second deals with improving the organisational structures and operations of Government departments. These programmes should also identify the savings in terms of job cuts and appropriations that are necessary to meet the three-year budget guidelines.

Under the third and fourth public action modernisation projects, each ministry is given the task of contributing to rationalisation of their organisational structures and operations by achieving a significant reduction in the actual and perceived complexity of administrative formalities. A permanent arrangement for consulting with businesses and an interministerial group to coordinate streamlining of formalities for businesses have been set up to identify businesses' priorities and to seek, develop and oversee streamlining measures. Quarterly meetings are held with business representatives.

Seven structural streamlining measures were launched in January 2013:

- "Tell us once", so that businesses no longer have to provide the same information to multiple agencies;
- The introduction in the first half of 2013 of the Déclaration Sociale Nominative (DSN), a single form for reporting corporate employment information;
- Streamlining and acceleration of procedures applying to business real-estate;
- Opening of a single web portal for business support schemes;
- Fighting "over-transposition" of European legislation into French law to avoid pointless complexity that exceeds the requirements of European legislation;
- A test to evaluate the impact of new rules on very-small, small and medium-sized enterprises;
- Reduction of the export obstacles for very-small, small and medium-sized enterprises;

These seven streamlining measures will be supplemented with proposals from the ministries based on businesses' priorities. The proposals will be included in the Ministerial Modernisation and Streamlining Programmes. The preliminary version of these proposals was drafted for the April 2013 meeting of the CMPA. Further streamlining measures for business will include speeding up the introduction of one-stop service for customs formalities, the future creation of a "platform for corporate legal notices" in the form of a public interest grouping and online filing procedures for environmental protection declarations relating to listed sites and the extension of the streamlined approval system.

The modernisation of public action also incorporates crosscutting initiatives run by interministerial bodies:

- A project to rationalise the structure and governance of operators and agencies;
- A project to rationalise procurement, with procurement savings of €2 billion by 2015 for the central government and central government agencies, to be achieved by strengthening the Public Procurement Department (SAE). The decree instituting the Department will be recast to enhance its oversight and extend its jurisdiction to central government agencies. Hospitals are now engaged in a similar process called the Programme for Responsible Hospital Procurement (PHARE), which should produce procurement savings of €910 million by 2014;
- A project to rationalise State property management;
- Work to improve and rationalise the financial function, especially the expenditure chain;
- And, finally, the establishment, under the aegis of the General Commission for Investment (CGI), of a systematic preliminary evaluation procedure for investments, with an independent second

opinion for the largest investments to ensure that the best and most efficient choices are made (see below).

6.2.2 Strategy for research, innovation and investment

Redeployment of Investments for the Future to priority sectors

The Invest for the Future programme helps improve the quality of public finances by concentrating government expenditure on investments with high social and economic returns. Total appropriations of €35 billion have been initially allocated for investment in higher education and training (€4 billion), research (€15 billion), manufacturing and SMEs (€6.5 billion), sustainable development (€5 billion) and digital economy (€4.5 billion).

In order to stick to stakeholders' needs and to Government priorities, €2.4 billion have already been redeployed. Furthermore, Prime Minister announced in January 2013 that another €2.2 billion would be redeployed. The first redeployment of the Invest for the Future programme mainly aimed to support the creation of the Public Investment Bank (BPI)[34], the increase in excellence laboratories appropriations and the establishment of a national seed capital fund. The second one is targeting the National Pact for Growth, Competitiveness and Jobs' five priorities (see Section 6.3.2). These are innovation and industry support, development and dissemination of enabling technologies, energy transition, development of the life sciences and health care industries.

The focus on the most growth-oriented expenditure reflects the Government's determination to rationalise Government action and make it more effective. This programme is co-financed by the private sector and will benefit from a major leverage. It will stimulate France's growth potential.

A rigorous investment selection process will be maintained. Projects are selected by panels of top international experts, based on scientific excellence, profitability and expected impact on potential growth. After the agreement between the central government and its operators and following the first calls for projects in 2010, 2011 and 2012 were dedicated to selecting projects, launching new calls for projects and negotiating contracts. The selected projects involve the "higher education, research and job training" priority (laboratories of excellence, biotechnology, facilities of excellence), as well as sustainable development (fourth-generation nuclear reactors, "*EcoCités*" mass transit), manufacturing (aeronautics, space, and automotive industries) and the digital economy.

An assessment phase was included from the outset. Governance of the Invest for the Future programme is based on assessing public action. Each project is monitored by the General Commission for Investment, which is responsible for running the programme under the authority of the Prime Minister. The operators responsible for implementing the projects are closely monitoring them, and, under the control of a supervisory committee and in partnership with specialised audit teams, conduct periodic assessments of the scientific, economic, social and environmental effectiveness of the initial appropriation.

Systematic social and economic evaluation of government investments, with an independent second opinion for the largest ones

The constraints on public finances now make it all the more necessary to prioritise government investment projects to select the ones that offer the best cost-benefit performance for the community. For

34 Back in June 2012, the Government started working on founding the Bank, and some of the endowments initially allocated in 2013 through *Oséo* and the *Caisse des Dépôts et Consignations* were used to capitalize the Public Investment Bank's capital.

this purpose, it is critical that social and economic evaluations be carried out using a consistent method and as impartially as possible. Article 17 of the 2012-2017 Public Finance Planning Act marks a major step forward by making social and economic evaluations systematic for all major civilian investment projects backed by the central government and Government institutions, public healthcare institutions and healthcare cooperation bodies, and by introducing an independent second opinion for the largest investments. The second opinion requirement will improve evaluations. Plans also call for the second opinion to be submitted to Parliament.

The General Commission for Investment (CGI), which answers directly to the Prime Minister, will oversee the second-opinion process. The Government tasked Louis Gallois, the General Commissioner for Investment, with coming up with the proposals and, more specifically, with the thresholds at which an independent second opinion becomes mandatory and the way to integrate this opinion into the Government decision-making process. The ministries, working with the General Commission for Investment, will submit the operational details of the procedure to the next meeting of the Interministerial Committee for modernisation of public action (CIMAP) in the third quarter of 2013.

At the same time as this change in governance, a Commission from the Strategic Analysis Centre, led by Emile Quinet, will submit proposals for improving the social and economic evaluation method in the transport sector and contribute to the development of similar methods for other sectors. Defining the method is an important step towards enforcing the preliminary evaluation requirement.

6.2.3 Optimising healthcare expenditure

Constant improvements are being made to expenditure management tools to enhance healthcare delivery performance and make healthcare expenditure more efficient. As part of its national healthcare strategy, the Government has called on all stakeholders and all the instruments at its disposal to modernise the healthcare system. This means promoting more efficient care procedures (outpatient surgery, etc.), fighting waste in all areas (pointless procedures and prescriptions, unwarranted hospitalisation). These objectives will be achieved with new compensation and pricing methods that are less inflationary and by better coordination of hospital care with private practice and the medical and social sector, under the aegis of regional healthcare agencies.

Furthermore, the procedures for building and monitoring the annual National Healthcare Expenditure Growth Target ensure consistency between the long-term changes in healthcare delivery and the short-term need to meet the target. They have shown that they can produce the expected efficiency improvements and, at the same time, allow for rapid implementation of the savings measures required for infra-annual management of expenditure.

The heart of this quest for greater efficiency is improvement of care through effective regulation of healthcare delivery aimed at breaking down the barriers between private practice, hospital care and the medical and social sector. This will be one of the Government’s priorities. It is why the Prime Minister decided to implement a National Healthcare Strategy. A major effort will be undertaken in 2013 to set up local teams of different healthcare professionals in order to facilitate outpatient care and to enable hospitals to concentrate on treating the most acute and complex cases.

6.2.4 Decentralisation and public action reform

Containment of local government expenditure will be facilitated by decentralisation and public action reform. This reform will strengthen cooperation between municipalities and help clarify the powers of the different levels of local government, by upholding the notion of “lead entities” and “blocs of competences" to reduce the main sources of inefficiency in local government while improving the service provided to the public.

Three bills are being proposed for this reform:

- **The modernisation of local public action and the Metropolis Affirmation Bill** institute a local government conference in each region, chaired by the President of the Regional Council. The elected officials attending the meetings of this new body will draft the Local Governance Pact, which is a tool for coordinating local powers under the aegis of a lead entity.
- **The Regional Mobilisation for Growth and Jobs and Promotion of Equality between Local Areas Bill** makes the regions the lead entities for economic development and support for businesses. The Bill also makes regions major players in policies for jobs and young people, giving them full powers over vocational training and apprenticeships and giving them a role in coordinating and running public career guidance services. This second aspect of the reform also makes *départements* the lead entities for local solidarity, by giving them the task of working with the central government to develop a plan to improve access to public services within their territories. The Bill also expands the technical services that *départements* can offer municipalities, ranging from roads, to land use planning and housing. It calls for community centres for public services to be developed.
- **The Local Solidarity and Democracy Development Bill** establishes the High Council of Local government, which is a forum for on-going dialogue between local government representatives and central government. It strengthens the powers of each category of public establishment for cooperation between municipalities, broadens the requirements for exercising local petition rights and enhances the transparency of local government action.

At the same time, central government transfers to local governments will be frozen in nominal terms in 2013, and then cut in 2014 and 2015, to ensure local governments participate fully in the effort to consolidate public finances and to provide an incentive for local elected officials to rationalise local government expenditure. A parallel and unprecedented equalisation effort will be made to reduce inequalities between local areas.

All of the measures concerning local governments will be covered in a Confidence and Responsibility Pact negotiated with them. The Pact will now provide the framework for dealings between central and local government. It will make it possible to involve local governments more closely and more effectively in the public finance strategy.

6.3 Quality of government revenues

6.3.1 Consolidation efforts in 2012 with concern for a fair and effective tax system

The different Budget Acts put forward by the Government in 2012 were part of a fiscal consolidation strategy relying on new targeted efforts to make the tax system fairer and more effective, in keeping with the Council of the European Union's recommendations to France in July 2012.

The measures in the Budget Acts passed in 2012 targeted the most well-off households and large corporations **aiming at rendering the tax system more progressive**.

The most well-off households are being asked to pay more than the others, making fiscal consolidation an equitable process with a limited impact on consumption. The August 2012 Supplementary Budget Act introduced an exceptional wealth tax for 2012 and amended the inheritance tax reductions introduced by the previous majority. Taxes on capital income, which accrues mainly to the most well-off households, were increased with higher social levies on income from assets and investment products. The measures were supplemented by further measures in the 2013 Initial Budget Act, which includes measures to make personal income tax more progressive (with an additional 45% bracket and a lower cap on family deductions "*quotient familial*"), an alignment of taxes on capital income with taxes on labour income (the flat-rate withholding tax in discharge of all other taxes has been eliminated) and restoring fair taxation of assets with a return to progressive wealth tax rates. The social security contributions for self-employed workers have been aligned with those for payroll employees, including the elimination of the cap on health insurance contributions and the end of the deduction for business expenses from the compensation of company directors with majority holdings.

Box 6 – Details of the main recent measures to reduce tax expenditures and social security contribution exemptions

The second 2012 Supplementary Budget Act raised the minimum tax on Social Security-exempt benefits paid by employers from 8% to 20% and ended the tax and social security contributions exemptions for overtime pay.

The effort to reduce tax exemptions and tax breaks was stepped up in the 2013 Budget Act, affecting households, with an overall cap of €10,000 on personal income tax breaks and a lower cap on family deductions at €2,000 per dependant, instead of €2,336, and affecting businesses, with a cap on loan interest deductions and a recasting of the capital gains tax on corporate sales of equity securities. Several exemptions from social security contributions have also been reduced. Starting in 2013, individuals with employees will be required to contribute on the basis of the actual wages paid to their employees, since the possibility of paying contributions based on a lump-sum wage has been eliminated. Local elected officials will contribute to financing Social Security on their compensation in excess of €18,186 per year in 2012, under the same requirements as those applied to payroll employees. Social security contributions for freelance entrepreneurs will be increased to the same level as other self-employed workers.

The effort for businesses falls mainly on large corporations and on the financial sector, in order to narrow the implicit tax rate gap between large and small businesses. The August 2012 Supplementary Budget Act doubled the tax rate on systemic banking risk, imposed an exceptional corporate income tax payment for large corporations in 2013, increased contributions on stock options, introduced measures to fight corporate tax abuse and imposed an exceptional tax on the oil sector. The 2013 Initial Budget Act lays the emphasis on reducing the least effective tax exemptions for large corporations. This reduction limits the impact of tax increases on growth and enhances the coherence of the tax system by restricting fiscal optimization. More specifically, two tax planning arrangements have been restricted: the deduction of loan interest from taxable corporate income is now capped and the capital gains tax exemption for sales of equity securities has been reduced by an increase in the tax rate and a new way of calculating the deduction for fees and expenses. These two measures should help narrow the implicit corporate income tax rate gap between small and large businesses, since large corporations have a much lower implicit tax rate. There are also tighter restrictions on companies' carrying earlier losses forward to offset future income: the minimum corporate income tax rate has been raised to 50% of earnings, with a deduction of €1 million for small businesses. The payment deadlines for corporate income tax have also been reformed to bring the tax payment closer to the time of the chargeable event. This has been achieved by lowering the threshold that makes payment of the fifth prepayment instalment mandatory. Finally, the 10% exit tax introduced in 2010 on funds invested in insurance companies' capitalisation reserves has been increased by means of an exceptional supplementary contribution.

Special emphasis has been placed on eliminating ineffective tax and social security contribution exemptions, in accordance with the Council of the European Union's recommendations to France in July 2012. The effort to reduce tax and social security contribution exemptions has consequently continued (see details in the box below), with the end of tax exemptions on overtime pay and the measures mentioned above, such as the cap on deductions for loan interest expense, which **reduces the bias in favour of debt financing** in accordance with the Council's recommendations.

Box 7 – The fight against tax fraud

This fight is imperative for fair taxation and a priority for the Government.

The back taxes and penalties assessed under tax audits increased by nearly €2 billion in 2012 to a total of €18 billion. The Supplementary Budget Act from the end of 2012 gives tax audit staff **new legal instruments** to ensure that further progress is made in 2013. These new instruments to fight tax fraud include more specialized police resources, easier access to computerised bookkeeping registers and bank accounts, adaptation of search powers to computerised systems and the end of the so-called "double" rule that meant that taxpayers did not have to provide any justification for unexplained bank deposits unless they were at least double the declared amounts. Supplementary measures under the Bill for Transparency in Public Life and the Fight against Tax Fraud and, more specifically, the organisation of prosecution of tax fraud, along with the measures already announced as part of the 2014 Budget Bill, particularly the measures relating to transfer pricing, will have a greater impact on revenue growth in 2014.

The Social Security Budget Act contains several measures that will increase the return on audits:

- Principals will bear more liability when a sub-contractor is found to have used undeclared labour: Principals may lose their exemptions if they are found to be negligent with regard to their subcontractors' practices.
- Assessments for unpaid social security contributions may be increased for repeat offenders;
- The procedures for sharing and using information between investigation units have been expanded.

The results are expected to be in line with the previous upward trend:

- Assessments made by the Social Security contribution collection office (URSSAF) following audits of contributions have been growing rapidly: they increased from €458 million in 2008 to €1,029 million in 2011 (€933 million, excluding unemployment insurance). This was achieved on the strength of the expanded investigative powers of the collection office with regard to unemployment insurance premiums and improvements in the organisation of the investigation function under the on-going development of the collection office's regional network. Further progress should be made as the regional network is deployed.
- The fight against undeclared labour has made dramatic progress. Assessments for unpaid contributions increased from €33 million in 2003 to €220 million in 2011.

France has also followed the Council's recommendations concerning **the distribution of the tax burden to different tax bases.** Implementation of the Competitiveness and Jobs Tax Credit (see Section 6.3.2.) reduces taxes on labour. Half of the cost of the tax credit has been financed by expenditure savings and the other half by an overhaul of VAT rates and the introduction of new environmental taxes in 2016.

Measures to increase taxes on tobacco and alcohol were also included in the 2013 Social Security Budget Act.

In addition, the **fight against tax fraud** has been stepped up (see Box 7). The Third 2012 Supplementary Budget Act introduced several measures worth €1 billion: (i) measures to strengthen the administration's resources in the fight against fiscal fraud (extension of the procedure for blatant cases of tax fraud, the scope of the court-ordered investigation procedure, modernisation of search procedures); (ii) measures to fight tobacco smuggling; (iii) a measure to facilitate prosecution of VAT fraud involving the sale of used cars.

6.3.2 National Pact for Growth, Competitiveness and Jobs

The Prime Minister presented the National Pact for Growth, Competitiveness and Jobs on 6 November 2012. It is a comprehensive strategy for rebuilding our economy's production structure, combined with improved management of public finances. The measures announced are aimed at enhancing France's attractiveness and the international stature of our companies, developing training for young people and workers, fostering a shift to producing high-end products and services by stimulating innovation and stabilising the main tax measures applying to businesses.

The Competitiveness and Jobs Tax Credit is one of the main components of the National Pact. Its cost will be €20 billion when it is fully operational and its effects will be similar to those of a cut in employers' social security contributions. It will lower the cost of labour of all of the employees of the businesses concerned and should become fully operational over two years[35]. Half of the cost will be covered by cuts in general government expenditure and the other half will be covered by increasing taxes that are deemed to cause little distortion. The new tax measures include simplification of VAT rates[36] and the introduction of environmental taxes[37]. The tax credit will provide businesses with leeway to improve their price competitiveness by lowering their selling prices and to improve their non-price competitiveness by increasing their investment, in addition to stimulating job creation.

The macroeconomic effects of the tax credit are expected to be very substantial. It is expected to create 300,000 jobs and to increase GDP by 0.5 percentage points by 2017. The positive effect on jobs is expected to be seen as soon as 2013, since the tax credit will be paid in 2014 on the basis of payrolls in 2013 and pre-financing can be arranged. The Competitiveness and Jobs Tax Credit targets low and median wage jobs, which means it will have a major impact on employment and also on industries that are most exposed to international competition.

The National Pact also enhances discipline when it comes to managing public action, by asserting that "all new expenditure must be financed by savings on expenditure; that using new revenue to finance new expenditure will no longer be possible, since tax increases must not be used to promote new expenditure; and that any reforms initiated by the Government must include measures to optimise government expenditure". At the same time, it calls for simplification of the taxes concerned, based on

[35] The Competitiveness and Jobs Tax Credit represents a reduction of labour costs that is equivalent to a 4% reduction in gross payroll expense for employees earning less than 2.5 times the statutory minimum wage. In 2014 and beyond, the reduction will be 6%.

[36] The three current VAT rates of 5.5%, 7% and 19.6% will be changed to 5%, 10% and 20% respectively on 1 January 2014, producing a return of €6.1 billion in the first year. Approximately half of the return will come from the increase in the reduced rate from 7% to 10%.

[37] Environmental taxes will consist of a new revenue measure worth at least €3 billion by 2017. A Committee for Environmental Taxes, with representatives of all stakeholders and chaired by Professor Christian de Pertuis, is currently working on proposals.

the principle that no earmarked tax can be introduced without the simultaneous elimination of an equivalent or greater tax (Decision 29). The 2012-2017 Public Finance Planning Act calls for a reduction of earmarked taxes allocated to operators in 2014 and 2015, and a comprehensive review of all earmarked taxes by 30 June 13. The Circular of 14 January 2013 on "Rules for Responsible Management of Government Expenditure" defines the procedures for implementing the rules in the National Pact and, more specifically, the principle of self-insurance for programmes (see Section 3.5.1) and the principle of matching any new expenditure with an equivalent savings on expenditure, and no financing of new expenditure by increasing revenue. Also, no new taxes or increases in existing taxes can be used to justify an increase in expenditure.

6.3.3 Outlook

The reduction of the least effective tax expenditures and social security contribution exemptions will continue beyond 2014, with enhanced governance under the 2012-2017 Public Finance Planning Act:

- Article 14 restricts the annual increase in tax exemptions in nominal terms by introducing a cap.
- Article 16 states that any new legislation introducing tax expenditures or social security contribution exemptions must stipulate a limited term for the application of the new measures.
- Article 18 calls for annual evaluation of one fifth of tax expenditures and exemptions from social security contributions and systematic evaluation of all exemptions one year before their term expires. This provision of the Public Finance Planning Act gives the Government and Parliament an instrument for assessing the relevance of tax expenditures and exemptions from social security contributions, leading to a reduction in real terms.

This governance will be enhanced by holding interministerial **tax conferences**, as implemented by the Prime Minister's Circular dated 5 April 2013. The conferences will be held before Budget Bills are drafted so that each ministry can propose reductions to tax and social security contribution exemptions.

The Government has also initiated many projects to streamline France's tax system:

- The report by Members of Parliament Karine Berger and Dominique Lefebvre, which was submitted to the Prime Minister on 2 April 2013, will be the basis for the **upcoming reform of taxes on savings**, aimed at reinforcing savers' confidence and providing greater incentives for longer-term, higher-risk investments to meet the financing needs of small, medium-sized and intermediate-sized enterprises and the housing sector.
- The task force led by Member of Parliament Christophe Sirugue on **reform of the in-work income supplement** (RSA activité) in coordination with the **earned income tax credit** (PPE) will submit its findings in May 2013. These two instruments are intended to produce similar effects and they could be improved to enhance the purchasing power of low-paid workers and to provide better support for returning to employment. This measure parallels European efforts in accordance with the Council Recommendation adopted last February that calls for a Youth Guarantee to be established throughout the European Union.
- The **Environmental Tax Committee** is expected to present its preliminary proposals in June 2013. This Committee chaired by Christian de Pertuis was set up to provide an opinion on the roadmap drafted by the Environmental Conference for Ecological Transition. The roadmap sets out tax measures for reducing consumption of resources, greenhouse gas emissions and pollution. Another objective of the **Environmental** Tax Committee is to propose new ecological revenues

of €3 billion or more by 2017 to finance part of the Competitiveness and Jobs Tax Credit (see Section 6.3.2).

- The Government gave the French Digital Council the task of holding consultations on the findings of the report by Nicolas Colin and Pierre Collin, in order to propose **tax reforms in the digital sector**, with particular emphasis on the issue of the collection and use of personal data.
- Finally, the **Entrepreneurship Conference**, which opened on 14 January 2013 and will present its findings by the middle of 2013, is going to identify areas for reform to make France a more welcoming country for entrepreneurs and to reconcile the imperatives of growth and competitiveness with the social and human dimensions of enterprise.

Discussions will also start on expanding the base for **corporate income tax** and introducing modulated rates. France's corporate income tax features a high rate and a narrow base, even though the latter has been expanded by recent reforms (see above). The objective is to achieve European convergence on corporate income taxes.

7. Sustainability of public finances

7.1 Sustainability of general government debt

7.1.1 Impact of the ageing population on public finances

In the medium-to-long term, the ageing of the population will affect European countries' public finances. France will be less affected than most Member States of the European Union because of its high birth rate and the gradual effects of the retirement pension reforms already under way. A report by the Pensions Advisory Council (COR) submitted in December 2012 shows that the financing requirement for the pension system will start to diminish in 2030 in the baseline scenario, but that it will be substantial nonetheless.

In the short term, France will see large numbers of baby-boomers take retirement. This will increase expenditure by retirement pension schemes, despite the recent changes to the pension system, including the two-year increase in the age for automatic full retirement benefits. Furthermore, weak economic growth is still affecting the retirement pension schemes' revenue.

Against this background, the Government and other parties attending the labour-management conference in July 2012 identified consolidation of retirement pension schemes as one of the priorities for strengthening the Social Security system. For this purpose, the Government is holding a **"Rendez-vous 2013" on retirement pensions** with the primary objective of ensuring the short-term and long-term sustainability of retirement pension schemes. A roadmap has been drawn up to define the working method and the objectives.

The preliminary diagnostic phase was completed and two reports were submitted by the Pensions Advisory Council. One of the reports, submitted in December 2012, stresses that a balanced retirement system budget will not be achieved in the near future, despite the impact of recent changes to the retirement system on public finances. The financing requirement for all retirement pension schemes taken together will stand at approximately 1 point of GDP by 2020. The second report, submitted in January 2013, offers a detailed picture of the current state of the French retirement system.

After this groundwork was completed, the Prime Minister established a "**Pension Reforms Committee**," made up of 10 independent experts and chaired by Ms Moreau, on 27 February 2013. The Committee's task is to consult with all stakeholders and put forward proposals for reform in June 2013 that will ensure the short-term, medium-term and long-term equilibrium of retirement pension schemes. In particular, the Committee must identify the changes needed to achieve the following objectives simultaneously: (i) preserving the pay-as-you-go retirement system; (ii) making the system fairer; (iii) making the system easy to understand to ensure free choice; (iv) building confidence in pay-as-you-go retirement systems by providing a sustainably balanced financial framework; and (v) improving management of the retirement system. Improving the level of employment, particularly for older workers, is a major focus of the Committee's work.

Based on the proposals that the **Pension Reforms Committee** will make, a final consultation phase between the Government and management and labour representatives will take place and legislative changes will be produced in the second half of 2013.

7.1.2 Sustainability gap

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. The deviation of public finances from a sustainable path is conventionally assessed by estimating the immediate and lasting fiscal adjustment (in percentage points of GDP) that would be required to avoid a long-term increase in the government debt ratio with a constant structural primary balance (meaning the structural balance excluding interest expense). This 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 evolution for pensions, healthcare, long-term care and unemployment benefits starting in 2017 at unchanged policy. Work by the Member States and the European Commission produced a harmonised estimate of this impact at the European level[38].

In France, the adjustment measures already in place for 2013 and the measures stemming from this Stability Programme for 2014 to 2017, which incorporate the objective of short-term, medium-term and long-term equilibrium of retirement pension schemes set for the Pension Reforms Committee, will make it possible to restore the overall sustainability of public finances. The structural primary balance should stand at 3.3% of GDP in 2017, which is 2.2 percentage points of GDP more than the primary balance that stabilises debt in the long term. This would reduce debt in the medium term and provide enough flexibility to finance the rising costs related to the ageing of population after 2017.

Table 18 – Public finance sustainability gap indicator S2 (percentage points of GDP)

Base year	2012	2017
Sustainability gap (S2 indicator)	**3,6**	**-1,0**
o.w. impact of the initial budget position	2,6	-2,0
o.w. impact of the ageing population (as of 2018)	1,0	1,0

Note:

- *The 2012 S2 indicator is estimated on the basis of a counterfactual scenario, where the structural primary balance is assumed to be constant for the duration of the programme (2012-2017), independently of the impact of the ageing population: it corresponds to the long-term fiscal adjustment that would have to be made in 2018 to stabilise the debt-to-GDP ratio in the very long term, in view of the impact of the ageing population after 2018;*
- *The 2017 S2 indicator is estimated on the basis of the 2017 structural primary balance expected under the present programme. It corresponds to the long-term fiscal adjustment that would have to be made in 2018 to stabilise the debt-to-GDP ratio in the very long term, in view of the impact of the ageing population after 2018.*
- *The data on ageing-related expenditure (pensions, healthcare, long-term care, education, unemployment) and expenditure on unemployment benefits underlying the calculation of the S2 indicator are taken from the Fiscal Sustainability Report by the European Commission (published in January 2013[39]).*

On the other hand, with no reduction in the government deficit (constant structural primary balance from 2012 to 2017), long-term structural adjustment of 3.6 percentage points of GDP would have to be achieved in 2018 to stabilise debt in the very long term, in view of the expected increase in expenditure

[38] See European Commission, 2012, "2009 Ageing Report: Economic and budgetary projections for the Eu-27 Member States (2010-2060)", European Economy, 2/2009.

[39] See European Commission, 2012, “Fiscal Sustainability Report 2012,” *European Economy*, No. 8/2012

related to an ageing population. The discounted additional cost is estimated at 1.0 percentage points of GDP between 2018 and 2060.

7.2 Contingent liabilities

General government off-balance sheet liabilities cannot be evaluated with certainty and depend on future developments[40]. They may affect public finances eventually, and are **very closely watched by the Government and Parliament**. 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[41]. This financial statement is certified by the Court of Auditors.

The main general government off-balance sheet liabilities are:

- **liabilities for future ageing-related expenditure** (pensions[42], healthcare, long-term care, education), where valuations depend on the demographic and macroeconomic outlook. The impact of these liabilities on the sustainability of debt is measured by calculating a sustainability indicator (see Section 7.1).
- **contingent liabilities** 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 intervention to support economic activity or to obtain financing for certain economic agents without access to market financing. They include guarantees provided under clearly defined agreements, along with guarantees related to the general-interest functions (insurance arrangements through the Central Reinsurance Fund, guarantees provided to COFACE to support exports, guarantees to protect savers, etc.) Generally speaking, the risk of such guarantees being invoked is small. Furthermore, to prevent excessive use of this type of instrument, **new central government guarantees can only be granted under the terms of a Budget Act**[43].

In 2011, total central government loan guarantees came to €124 billion. The main new guarantee that the French Government provided was for Dexia in December. It was granted in coordination with Belgium and Luxembourg as part of the bank's restructuring. In addition, France, along with the other euro-area Member States, has provided financial support for euro area States facing financial difficulties, by guaranteeing the securities issued by the EFSF. Following a decision by Eurostat on 27 January 2011, the funds that the EFSF lends to these countries are recognised directly as part of the Maastricht debt of the Member States providing guarantees, proportionately to their guarantees (see Section 3.7).

In 2012, the main new central government loan guarantees or amendments to central government guarantees concerned Peugeot PSA, CIF and Dexia. Central government guarantees may cover debt securities issued between 1 January 2013 and 31 December 2016 by Banque PSA Finance (for outstanding

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[40] In the State accounting system, off-balance sheet liabilities are defined as contingent liabilities, meaning potential liabilities or else liabilities remaining at the end of the year that are not likely or certain to lead to a disbursement of funds.

[41] Articles 27 and 54(7) of the Constitutional Bylaw on Budget Acts of 1 August 2001. See http://www.performance-publique.budget.gouv.fr/fileadmin/medias/documents/ressources/Comptes/2011/Compte_General.pdf

[42] These pension liabilities incorporate central Government liabilities for civil servants' pensions, as well as the liabilities of all Social Security administrations.

[43] Article 34 of the Constitutional Bylaw on Budget Acts of 1 August 2001.

loan principal of up to €7 billion[44]). The central government guarantee for loans to Dexia, first set up in 2011, was amended in 2012. The guarantee can now apply to funds raised by Dexia SA and Dexia Crédit Local SA between the publication of the Supplementary Budget Act of 2 November 2011 and 31 December 2012, as well as to debt securities issued by Dexia Crédit Local SA that were already reported on its balance sheet when the Supplementary Budget Act of 2 November 2011 was published. The guarantee will cover a maximum outstanding amount of €38.76 billion[45].

7.3 Continuation of structural reforms

As explained in detail in the ***National Reform Programme***, the Government is determined to carry out a bold reform agenda to return to **stronger, more balanced and more inclusive growth**, and to reverse the unemployment trend before the end of 2013 by unleashing dynamism **at the European level and at the national level**.

In addition to the **consolidation of public finances** described in this Stability Programme, which is based on the principles of social justice and economic efficiency, and on the determination to sustain aggregate demand in the short term while supporting potential long-term growth through sweeping modernisation of public action, the Government's economic policy has two other aims at the national level, which are explained in detail in the National Reform Programme:

- **Restoring the competitiveness** lost over the last ten years relies on lowering labour costs and supporting productive investment: business finance reform, streamlining regulations, tax reform to favour SMEs and intermediate-sized enterprises, as well as innovation, sector reforms to stimulate the growth of priority sectors.
- **Fighting unemployment, job insecurity and inequality** calls for both urgent measures to support the purchasing power of the least well-off, action to prevent abuse and indecently high compensation, and sweeping reforms to reduce labour market segmentation, improve job security, promote jobs for young people and older workers, and promote gender equality at work. The 11 January 2013 Agreement on Job Security, which is now being made into law by the Parliament, will make a huge contribution.

[44] See Supplementary 2012 Budget Bill (19 December 2012).

[45] See Supplementary 2011 Budget Act (Act 2011-1416 of 2 November 2011) and the Supplementary 2012 Budget Bill (19 December 2012). This guarantee must be invoked jointly with the guarantees provided by the Kingdom of Belgium and the Grand Duchy of Luxembourg and for up to 45.59% of the eligible amounts.

8. Institutional aspects and governance of public finances

8.1 Transposition of the Directive on "budgetary frameworks"

The Council of the European Union adopted a Directive on requirements for budgetary frameworks for the Member States on 8 November 2011. This Directive is one of the six instruments in the "Economic Governance Package," or "Six-Pack," adopted to supplement and strengthen multilateral surveillance of economic and fiscal policies in Europe.

The Directive calls for improved production and dissemination of public finance data prior to the release of national accounts statistics, more thorough documentation of economic and fiscal forecasts, setting quantified budget rules for general government, implementation of medium-term budgetary frameworks providing multiyear public finance planning and, finally, transparency and coordination of general government sub-sector forecasts.

Many of the provisions in the Directive already existed in French law. Measures were taken to complete the adaptation of national law to the provisions of the Directive in accordance with the commitment by the Member States to transpose the Directive by the end of 2012.

- **The budgetary and public accounting systems already cover France's entire general government sector and France is the only euro-area country where central government and social security funds' financial statements are certified.** The statements are subject to internal budgetary and accounting audit procedures, independent audits, including the yearly certification of the central government's financial statements, as well as the verification of the social security funds' financial statements by the Court of Auditors and the regional audit bodies' audits and opinions of local governments' financial statements. Furthermore, a new Decree on fiscal management and public accounting was published in November 2012. It will harmonise the fiscal and accounting rules for the structures covered by the notion of general government in the system of national accounts[46].
- **The infra-annual dissemination of budget outturn data from the public general accounting system or the cash-based accounting system will be enhanced.** Budget outturn data for the central government sector are now published monthly. Preparations are now under way to publish infra-annual data on local government and Social Security finances. The first publication is scheduled for the beginning of 2014, with quarterly publications for local government and monthly publications for Social Security.
- **The Economic, Social and Financial Report already covers the main items required under the Directive with regard to the transparency and coordination of public finance forecasts and it will be expanded.** Under the terms of Article 50 of the Constitutional Bylaw on Budget Acts promulgated in August 2001, the documents that are currently appended to Budget Bills already include a presentation of the assumptions underlying the macroeconomic scenario chosen, a comparison with the scenarios presented by other forecasting organisations and an analysis of sensitivity to different scenarios. These forecasts have already been compared to the Commission's

[46] Central government, local government, local public establishments, public healthcare establishments, other public units included in the general government sector, private corporations included in the general government sector, and with the consent of the Minister for the Budget and if their articles of association so provide, public corporations that are not part of the general government sector, unless their articles of association exempts them.

forecasts in the April 2012 Stability Programme and in this Programme. This comparison will be appended to future budgetary documents.

- **The medium-term budgetary framework has been in place since 2008, with Multiyear Public Finance Planning Acts that cover at least four years[47]. This framework has recently been enhanced.** The French Constitution provides for a special category of legislation to give lawmakers the tools they need for managing public finances over several years. This legislation takes the form of Public Finance Planning Acts. These Acts define the "multiyear guidelines for public finances" and must be in line with the "objective of balanced public finances". The content of the Public Finance Planning Acts is currently defined by the Constitutional Bylaw on Public Finance Planning and Governance of December 2012 (see below). Furthermore, the implementation of the Public Finance Planning Acts and their consistency with annual Budget Acts are monitored. The Government is required to report to Parliament on the enforcement of the Multiyear Public Finance Planning Act rules each year in the preparatory report for the public finance policy debate[48]. The Court of Auditors also produces a special report for the public finance policy debate. In accordance with the requirements of the Constitutional Bylaw on Public Finance Planning and Governance, the reports appended to the multiyear public finance plans include public finance trajectories at unchanged policy, in compliance with the relevant provisions of the Directive.

- **The current coordination of public finance forecasts for general government sub-sectors was recently enhanced:** the public finance policy debate, which is held in June each year, presents the public finance strategy for the general government as a whole. During this debate, the Parliament examines the enforcement of the Multiyear Public Finance Planning Act for the current year and how it applies to different sub-sectors. The annual Initial Budget Act and Social Security Budget Act are drafted to be consistent with the multiyear framework. The application by sub-sector is updated in the fourth quarter in the Economic, Social and Financial Report appended to the Budget Act. The Constitutional Bylaw on Public Finance Governance reinforces this coordination by calling for an introductory article in the Budget Bill passed by Parliament that presents the general government budget balance forecasts underlying the Budget Act and the Social Security Budget Act.

- **Public finance governance relies on several quantified fiscal rules that are monitored independently, as required by the Directive.** The Public Finance Planning Act sets specific expenditure and revenue requirements: a requirement for central government expenditure (see Section 3.5.2), a healthcare expenditure target (ONDAM) with an early warning procedure in the event of a serious threat of an overrun, spending caps for basic Social Security coverage and a floor for new tax and social contribution revenue measures. Each year, the Public Finance Planning Act requires the Government to report on compliance with these requirements during the public finance policy debate, where the Parliament can call on the Court of Auditors for assistance with the outturn for the year, in accordance with Article 48 of the Constitution. In addition, the Early Warning Committee monitors healthcare expenditure independently. Furthermore, in response to the European Treaty on

[47] Three planning acts have been passed since 2008. The one currently in force was passed on 31 December 2012 and covers the period from 2012 to 2017.

[48] This monitoring is documented in the preparatory report for the public finance policy debate in accordance with Article 29 of the 2012-2017 Public Finance Planning Act: "Each year, the Government shall submit a report on the enforcement of this Act to Parliament, after consulting with the Local Finance Committee and before the public finance policy debate. It shall also present an explanation of any discrepancies between the commitments made in the previous Stability Programme submitted to the European Commission and the forecasts in the present Act. The report shall be made public and presented in a single document, with the opinion of the Local Finance Committee appended to it."

Stability, Coordination and Governance in the Economic and Monetary Union, a new structural balance requirement was incorporated into French national law and is monitored independently by the High Council on Public Finances (see Section 8.2). A "golden rule" now applies to local government budgets as well. Loan repayments must be covered by cash flow, "operating" budgets and "capital" budgets must be balanced, and borrowing is only allowed to finance capital expenditure. Compliance with this requirement is supervised by the Prefects and the Regional Court of Auditors.

- **Various documents ensure transparent public finances.** The reports and appendices attached to the Budget Bill provide detailed information about taxes and social security contributions, central government equity holdings and the off-balance sheet liabilities of the central government and its operators in order to meet the requirements of the Directive. The Court of Auditors certifies the central government's financial statements in accordance with Article 27 of the Constitutional Bylaw on Budget Acts, which establishes the principle that the "central government's financial statements must be lawful, faithful and give a true and fair view of its net assets and financial situation." The Court of Auditors also certifies the financial statements of the social security funds.

- **Macroeconomic forecasts are submitted to the High Council on Public Finances for its opinion:** the Constitutional Bylaw on Public Finance Planning and Governance of 17 December 2012 set up the High Council on Public Finance, which is an independent body that is responsible for giving an opinion on the economic forecasts in all financial bills, as well as the economic forecasts in the proposed Public Finance Planning Act and Stability Programme (see below).

8.2 Enhanced governance with the Constitutional Bylaw on Public Finance Planning and Governance, following the entry into force of the European Treaty on Stability, Coordination and Governance in the Economic and Monetary Union and the agreement on a new Regulation on Strengthening Public Finance Surveillance

The European **Treaty on Stability, Coordination and Governance in the Economic and Monetary Union (TSCG)** was signed by 25 Member States of the European Union on 2 March 2012, at the end of a process that the European Council had initiated on 9 December 2011. The requisite number of ratification instruments were deposited and the Treaty came into force on 1 January 2013. Consequently, the Member States have one year, up until 1 January 2014, to implement the provisions of Article 3(1) on **establishing a national rule for the general government structural balance**.

At the same time as the discussions on the Treaty on Stability, Coordination and Governance were taking place, the Commission presented two further Regulations on 23 November 2011, jointly referred to as the "Two-Pack". These Regulations have not been adopted officially as of the date on which this Stability Programme is being presented, but a political agreement on them was reached at the European level on 20 February 2013. One Regulation deals with strengthening economic and budgetary surveillance of Member States experiencing or threatened with serious difficulties with respect to their financial stability in the euro area. The second Regulation sets out **common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficit of the Member States in the euro area**. The second Regulation aims at the following public finance objectives:

- **Ensuring consistency between the European Semester focusing on the Stability Programme (or "national medium-term fiscal plan"), which ends in July with recommendations from the Council of the European Union to Member States, and the National Semester focusing on preparing Budget Bills.** Therefore, each Member State must submit its draft budgetary plan for the coming year to the European Commission by 15 October. The plan must set out the main parameters of the general government balance forecast, in accordance with the Stability Programme and the Council's recommendations, and the macroeconomic forecast on which it is based. If the examination of the proposed budgetary plan shows a significant deviation from the fiscal requirements set out in the Stability and Growth Pact, the Commission may request a revised budgetary plan. The proposed Regulation stipulates the information that must be included in the draft budgetary plan. It stipulates that independent organisations must be made responsible for monitoring fiscal requirements at the national level, particularly the structural balance requirements, in accordance with the relevant provisions of the Treaty on Stability, Coordination and Governance. The proposed Regulation also calls for the macroeconomic forecasts that financial legislation and medium-term fiscal plans are based on to be produced or approved by independent bodies.

- **Strengthening the surveillance of the fiscal policies of Member States subject to an Excessive Deficit Procedure.** The proposed Regulation calls for Member States with excessive deficits to submit an "economic partnership programme" to the Commission and the Council that describes the measures and structural reforms to be used to bring the government deficit back down under the reference value in the long term.

France ratified the Treaty on Stability, Coordination and Governance by legislation enacted on 22 October 2012. France brought its national legislation into compliance with the Treaty and the future provisions of the proposed Regulation on Strengthening Surveillance of Public Finances with the **Constitutional Bylaw on Public Finance Planning and Governance**, adopted on 17 December 2012, and the **2012-2017 Multiyear Public Finance Planning Act. These two pieces of legislation consolidate and enhance the existing budgetary framework.**

- **The Constitutional Bylaw governs Public Finance Planning Acts**, requiring a content which is consistent with the requirements under the Directive on Budgetary Frameworks of 8 November 2011. Therefore, the Multiyear Public Finance Planning Acts must define multiyear fiscal targets over more than 3 years and present public finance forecasts at unchanged policy (see above). The Constitutional Bylaw also ensures that Public Finance Planning Acts comply with the rules under the Treaty on Stability, Coordination and Governance (see below).

- **It incorporates a new rule on the general government structural balance into the Public Finance Planning Acts.** As provided for in the Treaty and the Two-Pack, compliance with the Constitutional Bylaw is subject to opinions made public by the High Council on Public Finances and a correction mechanism is automatically triggered in the event of a major deviation. The Constitutional Bylaw defines a major deviation of the structural balance as a deviation of more than 0.5% of gross domestic product in a given year, or 0.25% of gross domestic product averaged over two consecutive years, in accordance with the European principles. The Constitutional Bylaw requires the Government to respond to the deviation in the next Budget Bill or the next Social Security Budget Bill at the latest. **The Public Finance Planning Act sets the parameters for the correction mechanism, notably the time allowed for returning to the planned trajectory**, in the event of a deviation from the structural trajectory defined in the Multiyear Public Finance Planning Act: the Government is required to present a report proposing corrective measures to return the structural balance to the trajectory defined in the Multiyear Public Finance Planning Act within two years of the end of the year in which the deviation occurs.

- **The Constitutional Bylaw enhances Parliament's oversight of the public finance targets for the entire general government sector.** Parliament receives more information about the forecasts for the entire general government sector under the terms of an introductory article in the Budget Act and Social Security Budget Act that reports the public finance forecasts and outturns for the previous year and enhances the coordination mechanisms within the sub-sectors of general government.

- **The Constitutional Bylaw sets up the High Council on Public Finances**, which is an independent body established under the aegis of the Court of Auditors.
    - As stipulated in the Treaty on Stability, Coordination and Governance, the High Council on Public Finances publishes **an opinion that identifies any major deviations of the previous year's outturn from the trajectory defined in the Public Finance Planning Act**. Its opinion is given before the budget review act is presented to Parliament. The High Council also gives its opinion about any exceptional circumstances, as defined in the Treaty, that warrant a temporary deviation from the structural balance requirement.
    - **The High Council on Public Finances, which is an independent body**, provides ex-ante opinions on all draft financial legislation, as well as on the Public Finance Planning Bill and the proposed Stability Programme, and on the realistic character of **macroeconomic forecasts** (in accordance with the provisions of the Directive on Budgetary Frameworks). Its opinions will be taken into consideration by the Constitutional Council if Budget Acts are referred to it for review.
    - The High Council's opinion issued before the presentation of Budget Bill and Social Security Budget Bill drafts also focuses on **the consistency of the structural balance forecasts for the entire general government sector with the Multiyear Public Finance Planning Act, and the consistency of this planning with France's European commitments.**

8.3 Statistical governance

France's national statistics institute (INSEE) is responsible for publishing the national accounts, which include the main public finance aggregates in the system of national accounts. The national accounts are compiled in accordance with the European System of Accounts, ESA95. INSEE maintains regular contact with Eurostat to ensure compliance. In May 2011, the national accounts methods and concepts were recast. They were rebased and 2005 is now the new base year for macroeconomic data. INSEE will switch to the "2010 base" when it publishes the national accounts in May 2014, implementing ESA 2010, which will replace ESA 95[49].

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. The main information source for the central government is the budget outturn, supplemented by the central government's Financial Statement published by the Public Finances Directorate General. The restatement of the budget outturn as government net lending requires a series of adjustments to correct for some time lags and different treatment of certain transactions in budgetary accounting and in the system of national accounts. The construction of the "Other central government bodies" account, which mainly covers central government operators, relies on treating the individual accounts of all these bodies and converting them into the system of national accounts. The data for the local government sector come from the individual management accounts kept by Treasury accountants. The accounts for the social security funds are based on the accounting data from the different funds, public hospitals and hospitals providing public healthcare services, the unemployment insurance agency and Pôle Emploi, France's public employment service agency, along with the supplementary retirement scheme management bodies.

[49] See Proposal for a Regulation of the European Parliament and of the Council on the European system of national and regional accounts in the European Union (COM/2010/0774).

The information used for the **provisional general government account**, published three months after the end of the year, is not as complete. The closing of the central government's fiscal year is in mid-January of the following year and the central government's public accounts are completed towards the middle of March. Consequently, the data released on 1 April are liable to be revised slightly, mainly because of the adjustments needed to enter them into the system of national accounts. The operators' account data is derived mainly from accounting sources, which cover approximately two thirds of revenue and expenditure, with the rest of the data coming from forecasts. 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 virtually all municipalities. For the 1 April release, the social security fund accounts are partially based on estimates, when the funds' financial statements are not yet public. Nevertheless, a large number of provisional statements (General Social Security funds, unemployment insurance benefits, 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[50].

Government debt under the Maastricht definition is compiled for the provisional account using accounting data from nearly all general government sub-sectors. The debt of general government sub-sectors is consolidated by means of the "securities survey" conducted by the Banque de France and the information that the Public Finances Directorate General gathers directly from the leading holders of Government securities.

The transmission 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 production.** The enshrinement of this principle into law was a response to the European Statistics Code of Best Practices, adopted by the Statistical Programme 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 specifies that the independence of the statistics authorities in producing and disseminating public statistics must be made into law. To this end, Article 144 creates a Public Statistics Authority responsible for ensuring compliance with the European Statistics Code of Best Practices. It covers all entities producing public statistics.

8.4 Status of this Stability Programme under internal procedures

Stability Programmes are debated and voted on by Parliament by virtue of Article 14 of the 2011-2017 Multiyear Public Finance Planning Act of 28 December 2010. This Article, which has not be abrogated by the 2012-2017 Public Finance Planning Act of 31 December 2012 stipulates: "The Government shall send the draft Stability Programme to the Parliament at least two weeks before it is sent to the European Commission for the purposes of Article 121 of the Treaty on the Functioning of the European Union. The Parliament shall debate the draft programme and vote on it".

[50] France is one of the European Union countries that make the fewest revisions to their 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).

In 2012, the suspension of the Parliament's work on 7 March because of the presidential elections held on 22 April and 6 May, and the general elections held on 10 and 17 June, meant that the draft Stability Programme was examined on 11 April by the Finance Committees of the upper and lower chambers.

In 2013, the High Council on Public Finances, created by the Constitutional Bylaw of 17 December 2012 on Public Finance Planning and Governance, received the macroeconomic forecasts underpinning the draft Stability Programme from the Government on 8 April. The High Council published its opinion on these forecasts on 16 April.

The present Stability Programme has been voted by the National Assembly on April 23th 2013 and debated at the Senate on April 24th 2013.

9. Annex

Statistical tables

Table 1a. Macroeconomic prospects

	ESA Code	2011 Level (Mn€)	2011 Rate of change	2012 Rate of change	2013 Rate of change	2014 Rate of change	2015 Rate of change	2016 Rate of change	2017 Rate of change
1. Real GDP	B1*g	-	1.7	0.0	0.1	1.2	2.0	2.0	2.0
2. Nominal GDP	B1*g	2 001.4	3.3	1.6	1.7	3.0	3.7	3.7	3.7
Components of real GDP									
3. Private consumption expenditure	P.3	1 151.3	0.3	-0.1	0.2	0.9	1.8	1.9	1.8
4. Government consumption expenditure	P.3	489.3	0.2	1.4	1.2	0.6	0.4	0.1	0.4
5. Gross fixed capital formation	P.51	401.2	3.5	0.0	-0.8	1.2	1.8	2.5	2.9
6. Changes in inventories and net acquisition of valuables (% of GDP)	P.52 + P.53	10.9	-	-	-	-	-	-	-
7. Exports of goods and services	P.6	538.2	5.3	2.5	2.0	4.5	6.7	6.7	6.7
8. Imports of goods and services	P.7	594.3	4.9	-0.3	0.8	3.5	5.3	5.3	5.4
Contributions to real GDP growth									
9. Final domestic demand		-	0.9	0.3	0.2	0.9	1.5	1.6	1.7
10. Changes in inventories and net acquisition of valuables	P.52 + P.53	-	0.8	-1.0	-0.4	0.1	0.1	0.0	0.0
11. External balance of goods and services	B.11	-	0.0	0.7	0.3	0.2	0.3	0.3	0.3

NB: *The nominal GDP stock and flow data for 2011 and 2012 correspond to the March 2013 release, but the breakdown of GDP in 2011 is taken from the national accounts published in mid-May 2012 and the breakdown of GDP in 2012 is taken from the quarterly accounts published in March 2013.*

Table 1b. Price developments

	ESA Code	2011 Level (Mn€)	2011 Rate of change	2012* Rate of change	2013 Rate of change	2014 Rate of change	2015 Rate of change	2016 Rate of change	2017 Rate of change
1. GDP deflator		-	1.3	1.6	1.5	1.8	1.7	1.7	1.7
2. Private consumption deflator		-	2.1	1.7	1.3	1.7	1.7	1.7	1.7
3. ICP		-	2.1	2.0	1.3	1.8	1.7	1.7	1.7
4. Public consumption deflator		-	1.4	0.7	1.0	1.1	1.1	1.1	1.1
5. Investment deflator		-	2.9	2.1	1.7	2.1	2.0	2.0	2.0
6. Export price deflator (goods and services)		-	3.2	1.4	0.8	1.1	1.5	1.5	1.5
7. Import price deflator (goods and services)		-	5.4	1.8	0.5	1.0	1.5	1.5	1.5

** GDP components adjusted for seasonal variations and working days (from the quarterly accounts, March 2012)*

Table 1c. Labour market developments

	ESA Code	2011 Level	2011 Rate of change	2012* Rate of change	2013 Rate of change	2014 Rate of change	2015 Rate of change	2016 Rate of change	2017 Rate of change
1. Employment, persons[1]		26 891	0.5	0.0	-0.2	0.6	0.9	0.9	0.9
2. Employment, hours worked[2]									
3. Unemployment rate (%)[3]									
4. Labour productivity, persons[4]		-	1.2	0.0	0.4	0.6	1.1	1.1	1.1
5. Labour productivity, hours worked[5]									
6. Compensation of employees	D.1	1 077.6	3.4	2.0	1.6	2.5	3.5	3.5	3.5
7. Compensation per employee			2.9	2.1	1.9	1.9			

[1]Occupied population, domestic concept national accounts definition
[2]National accounts definition
[3]ILO definition
[4]Real GDP per person employed
[5]Real GDP per hour worked
** GDP components adjusted for seasonal variations and working days (from the quarterly accounts, March 2012)*

Table 1d. Sectoral balances

% of GDP	ESA Code	2011	2012	2013	2014	2015	2016	2017
1. Net lending/borrowing vis-à-vis the rest of the world	B.9	-2.6	-2.2	-1.8	-1.3	-1.0	-0.6	-0.2
o.w. balance on goods and services		-2.8	-2.2	-1.8	-1.5	-1.1	-0.7	-0.3
o.w. balance of primary incomes and transfers		0.2	0.0	-0.1	0.1	0.0	0.0	0.0
o.w. capital account		0.0	0.0	0.1	0.1	0.1	0.0	0.0
2. Net lending/borrowing of the private sector	B.9							
3. Net lending/borrowing of general government	EDP B.9							
4. Statistical discrepancy								

Table 2a. General government budgetary prospects

	ESA Code	2012 Level (Bn€)	2012 % of GDP	2013 % of GDP	2014 % of GDP	2015 % of GDP	2016 % of GDP	2017 % of GDP
Net lending (EDP B.9) by sub-sector								
1. General government	S.13	-98.8	-4.9	-3.7	-2.9	-2.0	-1.2	-0.7
2. Central government	S.1311	-82.6	-4.1	-2.9	-2.3	-1.9	-1.4	-1.3
3. State government	S.1312							
4. Local government	S.1313	-3.1	-0.2	-0.2	-0.2	0.0	0.0	0.0
5. Social security funds	S.1314	-13.1	-0.6	-0.6	-0.5	-0.1	0.3	0.6
General government (S13)								
6. Total revenue	TR	1052.3	51.7	53.1	53.5	53.4	53.5	53.2
7. Total expenditure	TE[1]	1150.5	56.6	56.8	56.4	55.4	54.6	53.9
8. Net lending/borrowing	EDP B.9	-98.2	-4.8	-3.7	-2.9	-2.0	-1.2	-0.7
9. Interest expenditure	EDP D.41	51.6	2.6	2.4	2.5	2.6	2.7	2.8
10. Primary balance[2]		-46.6	-2.3	-1.3	-0.4	0.7	1.6	2.1
11. One-off and other temporary measures[3]		-2.5	-0.1	-0.1	-0.1	-0.1	0.0	0.0
Selected components of revenue								
12. Total taxes (12=12a+12b+12c)		567.0	27.9	28.9	29.1	29.0	28.9	28.6
12a. Taxes on production and imports	D.2	314.0	15.4	15.6	16.3	16.3	16.3	16.2
12b. Current taxes on income, wealth, etc	D.5	243.4	12.0	12.8	12.4	12.2	12.1	11.8
12c. Capital taxes	D.91	9.6	0.5	0.5	0.5	0.5	0.6	0.6
13. Social contributions	D.61	387.0	19.0	19.3	19.4	19.5	19.6	19.7
14. Property income	D.4	13.4	0.7	0.7	0.7	0.7	0.7	0.7
15. Other[4]		85.0	4.2	4.2	4.3	4.2	4.2	4.2
16=6. Total revenue	TR	1052.3	51.7	53.1	53.5	53.4	53.5	53.2
p.m.: Tax burden (D.2+D.5+D.61+D.91-D.995)[5]		913.5	44.9	46.3	46.5	46.5	46.5	46.3
Selected components of expenditure								
17. Compensation of employees + intermediate consumption	D.1 + P.2	381.6	18.8	18.8	18.5	18.1	17.7	17.4
17a. Compensation of employees	D.1	267.7	13.2	13.2	13.1	12.8	12.6	12.4
17b. Intermediate consumption	P.2	113.9	5.6	5.6	5.4	5.3	5.1	5.0
18. Social payments (18=18a+18b)		528.7	26.0	26.4	26.3	25.9	25.7	25.4
of which Unemployment benefits[6]		28.4	1.4	1.5	1.4	1.4	1.3	1.3
18a. Social transfers in kind supplied via market producers	D.6311 D.63121 D.63131	125.1	6.2	6.2	6.2	6.1	6.0	5.9
18b. Social transfers other than in kind	D.62	403.5	19.8	20.2	20.1	19.8	19.7	19.5
19=9. Interest expenditure	EDP D.41	51.6	2.6	2.4	2.5	2.6	2.7	2.8
20. Subsidies	D.3	30.5	1.5	1.5	1.5	1.5	1.5	1.5
21. Gross fixed capital formation	P.51	63.7	3.1	3.2	3.1	2.8	2.7	2.7
22. Capital transfers	D.9	17.4	0.9	0.7	0.7	0.6	0.6	0.6
23. Other[7]		77.1	3.8	3.9	3.8	3.7	3.6	3.5
24=7. Total expenditure	TE[1]	1150.5	56.6	56.8	56.4	55.4	54.6	53.9
p.m.: Government consumption (nominal)	P.3							

[1]Adjusted for the net flow of swap-related flows, so that TR-TE=EDP B.9

[2]The primary balance is calculated as (EDP B.9, item 8) plus (EDP D.41, item 9)

[3]A plus sign means deficit-reducing one-off measures

[4]P.11+P.12+P.131+D.39+D.7+D.9

[5]Including those collected by the EU and including an adjustment for uncollected taxes and social contributions (D.995), if appropriate

[6]Includes cash benefits (D.621 and D.624) and in kind benefits (D.631) related to unemployment benefits

[7]D.29+D.4-D.41+D.5+D.7+P.52+K.2+D.8

Table 2b. Breakdown of revenue

	2012 Level (Bn€)	2012 % of GDP	2013 % of GDP	2014 % of GDP	2015 % of GDP	2016 % of GDP	2017 % of GDP
1. Total revenue at unchanged policies	1052.3	51.7	53.1	53.5	53.5	53.6	53.5
2. Discretionary revenue measures[1]		0.0	0.0	0.0	0.0	-0.1	-0.3

[1]As supplementary measures

Table 2c. Expenditure to be excluded from the expenditure benchmark

	2012 Level (Bn€)	2012 % of GDP	2013 % of GDP	2014 % of GDP	2015 % of GDP	2016 % of GDP	2017 % of GDP
1. Expenditure on EU programmes fully matched by EU funds revenue							
2. Cyclical unemployment benefit expenditure	1.9	0.1	0.2	0.2	0.1	0.1	0.1
3, Effect of discretionary revenue measures	22.3	1.1	1.4	0.4	0.0	0.1	-0.2
4, Revenue increases mandated by law							

Table 3. General government expenditure by function

% of GDP	COFOG code	2011	2016
1. General public services	1		
2. Defence	2		
3. Public order and safety	3		
4. Economic affairs	4		
5. Environmental protection	5		
6. Housing and community amenities	6		
7. Health	7		
8. Recreation, culture and religion	8		
9. Education	9		
10. Social protection	10		
11. Total expenditure (=item 7=23 in Table 2)	TE[1]		

[1]Adjusted for the net flow of swap-related flows, so that TR-TE=EDP B.9

Table 4. General government debt developments

% of GDP	ESA Code	2012	2013	2014	2015	2016	2017
1. Gross debt[1]		90.2	93.6	94.3	92.9	90.7	88.2
2. Change in gross debt ratio		4.4	3.4	0.7	-1.4	-2.2	-2.6
Contributions to changes in gross debt							
3. Primary balance[2]		-2.3	-1.3	-0.4	0.7	1.6	2.1
4. Interest expenditure[3]	EDP D.41	2.6	2.4	2.5	2.6	2.7	2.8
5. Stock-flow adjustment		0.9	1.2	0.5	0.0	-0.1	0.0
of which:							
Differences between cash and accruals[4]							
Net accumulation of financial assets[5]							
o.w. privatization proceeds							
Valuation effects and other[6]							
p.m.: Implicit interest rate on debt[7]		3.0	2.7	2.8	2.9	3.1	3.2
Other relevant variables							
6. Liquid financial assets[8]							
7. Net financial debt (7=1-6)							
8. Debt amortization (existing bonds) since the end of the previous year							
9. Percentage of debt denominated in foreign currency							
10. Average maturity							

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

[2]Cf. item 10 in Table 2

[3]Cf. item 9. in Table 2

[4]The differences concerning interest expenditure, other expenditure and revenue could be distinguished when relevant or in case 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 could be distinguished when relevant or in case the debt-to-GDP ratio is above the reference value.

[6]Changes due to exchange rate movements, and operation in secondary market could be distinguished when relevant or in case the debt-to-GDP ratio is above the reference value.

[7]Proxied by interest expenditure divided by the debt level of the previous year.

[8]AF1, AF2, AF3 (consolidated at market value), AF5 (if quoted in stock exchange; including mutual fund shares).

Table 5. Cyclical developments

% of GDP	ESA Code	2012	2013	2014	2015	2016	2017
1. Real GDP growth (%)		0.0	0.1	1.2	2.0	2.0	2.0
2. Net lending of general government	EDP B.9	-4.8	-3.7	-2.9	-2.0	-1.2	-0.7
3. Interest expenditure	EDP D.41	2.6	2.4	2.5	2.6	2.7	2.8
4. One-off and other temporary measures[1]		-0.1	-0.1	-0.1	-0.1	0.0	0.0
5. Potential GDP growth (%)		1.3	1.4	1.5	1.5	1.6	1.6
contributions:							
- labour		0.3	0.3	0.3	0.3	0.3	0.3
- capital		0.6	0.6	0.6	0.6	0.6	0.6
- total factor productivity		0.4	0.5	0.6	0.6	0.6	0.6
6. Output gap		-2.0	-3.3	-3.6	-3.1	-2.7	-2.3
7. Cyclical budgetary component		-1.0	-1.6	-1.8	-1.6	-1.4	-1.2
8. Cyclically-adjusted balance (2 - 7)		-3.9	-2.1	-1.1	-0.3	0.2	0.5
9. Cyclically-adjusted primary balance (8 + 3)		-1.3	0.3	1.4	2.3	3.0	3.3
10. Structural balance (8 - 4)		-3.7	-2.0	-1.0	-0.2	0.2	0.5

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

Table 6. Comparison to previous update

	ESA Code	2011	2012	2013	2014	2015	2016	2017
Real GDP growth (%)								
Previous update		1.7	0.7	1.7	2.0	2.0	2.0	-
Current update		1.7	0.0	0.1	1.2	2.0	2.0	2.0
Difference		0.0	-0.7	-1.6	-0.8	0.0	0.0	-
General government net lending (% of GDP)	EDP B.9							
Previous update		-5.2	-4.4	-3.0	-2.0	-1.0	0.0	-
Current update		-5.3	-4.8	-3.7	-2.9	-2.0	-1.2	-0.7
Difference		-0.1	-0.5	-0.7	-0.9	-1.0	-1.1	-
General government gross debt (% of GDP)								
Previous update		85.8	89.0	89.2	88.4	86.4	83.2	-
Current update		85.8	90.2	93.6	94.3	92.9	90.7	88.2
Difference		-0.1	1.2	4.3	6.0	6.6	7.5	-

Table 7. Long-term sustainability of public finances*

% of GDP	2010	2015	2020	2030	2040	2050	2060
Total expenditure							
Of which: age-related expenditures	31.4	31.1	31.1	31.7	32.5	32.5	32.2
Pension expenditure	14.6	14.4	14.4	14.9	15.2	15.1	15.1
Social security pension							
Old-age and early pensions							
Other pensions (disability, survivors)							
Occupational pensions (if in general government)							
Health care	8.0	8.3	8.5	8.9	9.3	9.4	9.4
Long-term care (this was earlier included in the health care)	2.2	2.2	2.1	2.0	2.3	2.2	2.0
Education expenditure	5.0	4.9	4.8	4.7	4.6	4.6	4.6
Other age-related expenditures	1.7	1.4	1.3	1.2	1.1	1.1	1.1
Interest expenditure							
Total revenue							
Of which: property income	0.8	0.8	0.9	0.8	0.7	0.7	0.7
Of which: from pensions contributions (or social contributions if appropriate)							
Pension reserve fund assets**							
Of which: consolidated public pension fund assets (assets other than government liabilities)							
Systemic pension reforms[1]							
Social contributions diverted to mandatory private scheme[2]	:		:	:	:	:	
Pension expenditure paid by mandatory private scheme[3]	:		:	:	:	:	
Assumptions							
Labour productivity growth	:		:	:	:	:	:
Real GDP growth	:		:	:	:	:	:
Participation rate males (aged 20-64)	:		:	:	:	:	:
Participation rates females (aged 20-64)	:		:	:	:	:	:
Total participation rates (aged 20-64)	:		:	:	:	:	:
Unemployment rate	:		:	:	:	:	:
Population aged 65+ over total population	:		:	:	:	:	:

[1]Systemic pension reforms refer to pension reforms that introduce a multi-pillar system that includes a mandatory fully funded pillar.

[2]Social contributions or other revenue received by the mandatory fully funded pillar to cover for the pension obligations it acquired in conjunction with the systemic reform.

Pension expenditure or other social benefits paid by the mandatory fully funded pillar linked to the pension obligations it acquired in conjunction with the systemic pension reform.

*Source: 2009 Report on Ageing by the Ageing Working Group, updated to adjust for the impact of the 2010 pensions reform.

**In 2009, the unconsolidated financial assets (except for FA7) of supplementary pension schemes (Agirc, Arrco, CNAVPL, ERAFP, Ircantec, RSI) and the Pension Reserve Fund (FRR) stood at 8.1 percentage points of GDP. Their consolidated assets stood at 7.8 percentage points of GDP.

Table 7a. Contingent liabilities

% of GDP	2011	2012
Public guarantees*	6.2	
Of which: linked to the financial sector		

**These are guarantees granted by the State in Budget Acts under clearly defined agreements*

Table 8. Basic assumptions

	2011	2012	2013	2014	2015	2016	2017
Short-term interest rate (annual average)[1]							
Long-term interest rate (annual average)[1]							
USD/€ exchange rate (annual average)	1.39	1.29	1.32	1.31	1.31	1.31	1.31
Nominal effective exchange rate	110.6	107.5	109.8	109.8	109.8	109.8	109.8
World excluding EU, GDP growth	4.3	3.8	4.1	4.4	4.2	4.2	4.2
EU GDP growth	1.5	-0.3	0.1	1.5	1.9	1.9	1.9
Growth of relevant foreign markets	6.2	0.8	2.6	6 1/2	6 1/2	6 1/2	6 1/2
World import volumes, excluding EU	9.0	3.4	4.7	7.9	7.9	7.9	7.9
Oil prices (Brent, USD/barrel)	111.0	111.8	113.7	113.7	115.6	117.6	119.6

[1]Si nécessaire, hypothèses purement techniques