FRANCE

STABILITY PROGRAMME 2010-2013

JANUARY 2010

Introduction

The French Economic Recovery Plan launched in 2009, was timely, targeted and temporary, and consistent with the European Economic Recovery Plan framework. France's plan emphasised support for investment, and contained measures for supporting the purchasing power of those households that were hardest-hit by the crisis.

France's Recovery Plan curtailed a serious recession as of the second quarter of 2009, and the drop in GDP is expected to be half that of the euro area. Employment policies sharply curbed growth in the number of job-seekers between the first and the final quarters of 2009. Finally, consumption has not decreased throughout the crisis, and this resilience is an encouraging sign for the recovery in 2010.

In 2010, in line with the strategy adopted by the G20 countries, and with the recommendations of international organisations, France will progressively withdraw its support for growth. The recovery is still fragile, and a few recovery measures from 2009 will be carried over into 2010, on an adapted and strictly temporary basis.

Beyond 2010, the French government will considerably strengthen its efforts to consolidate public finances. The seriousness of the crisis placed great pressure on automatic stabilisers, and significant adjustments to the budget will be needed in the coming years. Additionally, the country's ageing population will put increasing strain on social spending, and far-reaching reforms are required to ensure sustainable public finances.

The Government's strategy involves pursuing structural reforms that encourage growth and – rather than raising taxes – reducing public spending.

In terms of structural reforms, and in line with the measures put in place since 2007, the goal will be to continue lowering firms' production costs to make them more competitive, and to boost total factors productivity. In 2010, the suppression of the local business tax and the introduction of the future-oriented investments consistent with the Lisbon Strategy are two examples of how France is pressing on with structural reforms, despite the difficult economic situation.

In terms of revenue, the Government is committed to not increasing the tax burden – already among the highest in Europe – in order not to hurt growth. Nevertheless, starting in 2011, the plan for consolidating public accounts calls for reducing tax expenditures and social contribution exemptions.

When it comes to spending, the goal will be, in large part, to apply what the State has learned in terms of managing expenses to local authorities and social security funds. Following the first meeting of the National Conference on the Public Deficit on 28 January 2010, the President of the Republic appointed various working groups, which have been asked to come up with concrete proposals before the next meeting in April.

During the Conference, President Sarkozy made it clear that he wants France to adopt a rule that will ensure that the whole general government budget is balanced. A working group led by Michel Camdessus, the former Managing Director of the IMF, will make proposals about how this rule could be implemented.

Containing expenditures growth and providing impetus for potential growth are also watchwords when it comes to reforming France's pension system, which will be examined and implemented by year's end. The timeline for this reform will be discussed with the social partners starting on 15 February 2010.

Cyclical conditions permitting, France's deficit would be brought back to 3% of GDP by 2013 with a tax burden of 43% of GDP at the end of the programme period, i.e. lower than it was in 2007.

France's Stability Programme for 2010–2013 provides a detailed, multiyear framework for a budgetary policy that combines a gradual end to crisis-related measures, greater containment of every aspect of public spending and continued structural reforms.

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1. Macroeconomic scenario

1.1. Current situation and short-term outlook (2009-2010)

Like every one of its partners, starting in September of 2008, France was affected by the global crisis that followed the bankruptcy in September 2008 of the American financial-services firm Lehman Brothers. Faced with a drop in world trade and tightening credit conditions, companies put off their investment projects and reduced considerably their inventories. Simultaneously, falling stock markets, diminishing house prices and increased joblessness meant that household consumption slowed in most countries.

GDP shrank by 2.25% in France in 2009. However, this decline, though sizeable, was relatively restrained compared with those of France's main partners. The Commission's autumn 2009 European Economic Forecast estimated a 4% drop in GDP for the euro area in 2009. France's somewhat better performance is due in large part to its sizeable automatic stabilisers and the Government's recovery measures. Household consumption has been resilient, and has not fallen since the start of the crisis.

In the spring of 2009, France was one of the first countries to climb out of recession, posting a 0.3% increase in GDP in the second and third quarters of the year. The improved situation in the manufacturing industry, confirmed by a marked rise in industrial production in November and in end-of-year car sales, leads us to expect a further increase in economic activity for the fourth quarter.

France's economy would continue to improve in 2010, buoyed by the effects of the recovery plan, and within an increasingly robust international environment, which would help French exports.

Nevertheless, the recovery would be progressive, both in France and abroad. Household consumption would pick up, thanks to a higher income growth within a context of restrained inflation (assuming a stabilisation of oil prices), but would be hampered by a still depressed labour market as employment tends to lag behind the pace of economic activity. After a sharp drop in 2009, business investment would stabilise. The need to reduce corporate debt, the slack in capacity utilisation and weak demand do not, at this stage, point to a dynamic upswing. Residential investment would not pick up at the end of the year, as the effects of favourable lending conditions and support for household investments (such as the zero-interest loan) begin to appear. An upturn in inventories would also contribute to growth.

France's GDP would grow by 1.4% in 2010. This is identical to the IMFs forecast, and to the *consensus forecast* of January 2010.

Unknown factors could influence – positively or negatively – this progressive growth scenario in the short term. For several weeks now, business surveys around the world have come up with mixed signs. On the other hand, a faster end to inventory reductions would contribute to greater growth in 2010, and bring down unemployment more rapidly than expected.

1.2. Medium-term outlook (2011-2013)

This central economic scenario underlying the multiyear estimates assumes an annual growth of 2.5% for 2011 to 2013. This assumption is consistent with the sizeable output gap existing in 2010, even factoring in uncertainties concerning the level of potential GDP. It also corresponds to the continuation of the cyclical rebound that would begin in 2010. Under this scenario, the output gap would not be fully closed by 2013.

The first rebound factor would be an increased job creation rate. The adjustment of employment to the fall in activity during the 2008–2009 recession would come to an end, and wages would resume their progression after the slowdown in 2009 and 2010. This momentum in earned income, in connection with falling unemployment, should bring the savings rate back to its pre-crisis level. This scenario is strengthened by France's relatively low level of household debt. In addition, this fall in savings can be accompanied by short- and long-term measures aimed at reducing the general government deficit.

Growth would also be helped by a rebound in business investment, within a context of strengthening domestic and external demand. Companies would take advantage of investment support initiatives that the Government put in place starting in 2007. In addition, these measures (including an increase in the research tax credit, the suppression of the local business tax and the future-oriented investments) would be beneficial for potential growth (see Section 5.2).

The outlook described above constitutes our central scenario. Nevertheless, financial crises sometimes have long lasting negative effects, and these could exert a dampening effect. This is why a more moderate growth scenario is also presented in Annex 2. In that scenario, average annual growth for 2011–2013 has been estimated at 2.25%, with expenditures and new tax and social security measures identical to those in the main scenario.

A more forceful upturn in global demand would also improve the outlook for French businesses in a cyclical manner. Investments would increase more sharply, reducing unemployment even further, and bringing the savings rate back down to its pre-crisis level faster than expected.

Table 1: Macroeconomic scenario, 2010-2013

	2009	**2010**	**Average 2011-2013**
GDP	-2.25	1.4	2.5
Domestic demand excluding inventories	-0.4	0.9	2.2
Household consumption	0.7	1.4	2.9
General government consumption	2.0	1.4	-0.3
Gross fixed capital formation	-5.8	-1.3	3.6
o.w. non-financial businesses	-7.6	0.6	4.8
Contribution from inventories	-1.7	0.5	0.2
Contribution from foreign trade	-0.1	0.0	0.0
Exports	-11.1	3.7	6.0
Imports	-9.9	3.6	5.7
GDP deflator	1.0	1.1	1.7
Household consumption deflator	-0.2	1.3	1.7
Primarily market branches (non-agricultural)			
Wage bill	-0.8	0.3	4.5
Real average wage per capita (deflated using consumption defl.)	2.0	0.6	2.1
Salaried employees	-2.6	-1.6	0.7

2. General government balance and debt

2.1. Public finance objectives and overall strategy

The Government's Medium-Term Objective (MTO) is to restore the structural balance of public finances.

To ensure the respect of this objective, the President of France made it clear, during the meeting of the National Conference on the Public Deficit on 28 January 2010, that he wants France to adopt **a rule that guarantees that the whole general government budget is balanced**. A working group led by Michel Camdessus, the former Managing Director of the IMF, will make proposals about the implementation of this rule.

By the end of the programme period (2013), the Government's goal is to carry out a structural adjustment representing more than 4 points of GDP. This will bring the deficit back down to 3% of GDP by 2013. The public finance trajectory is thus consistent with the recommendations of the Ecofin Council of 2 December 2009 (see Part 7).

This structural adjustment, which is primarily focused on public expenditures, will begin in 2011. In 2010, budgetary policy will be neutral vis-à-vis 2009 so as not to endanger France's return to growth. The adjustment will be carried out within the framework of an overall strategy, the linchpin of which will be a heightened containment of public expenditures throughout the general government sector. This will be complemented by a policy of reducing tax expenditures and social contribution exemptions by some €2 billion per year (out of a total of €70 billion of tax expenditures alone). In addition, the gradual disappearance of the temporary measures taken in 2009 and 2010 (measures for dealing with the economic and financial crisis and the temporary cost of reforming the local business tax in 2010) will also help improve public finances.

This general strategy responds to the long-term challenges facing the French economy:

- Given France's ageing population, a progressive return to structural equilibrium is a powerful lever for ensuring the long-term sustainability of public finances. This equilibrium will complement ongoing structural reforms to the pension system – reforms that will become even more wide-ranging following France's 2010 Pension System Review (*Rendez-vous sur les Retraites*). Thus, the structural adjustment achieved by 2013 will place public finances on the path to debt reduction (see Part 5).
- Lowering public expenditure without raising taxes in order to make the French economy more competitive and increase its growth potential.

Future-oriented investments (see Box 1), which are part of this long-term approach, will – thanks to their knock-on effect on private-sector investment – stimulate growth (see Section 5.2).

Table 2: Multiyear public finance trajectory

	2008	2009	2010	2011	2012	2013
Public balance (% GDP)	-3.4	-7.9	-8.2	-6.0	-4.6	-3.0
Public debt (% GDP)	67.4	77.4	83.2	86.1	87.1	86.6

Box 1: The impact of future-oriented investments on the general government balance

Future-oriented investments are financed by a €35 billion budget, €13 billion of which comes from repayments of loans granted to banks under the financial rescue plan. Starting in 2010, this will add €2–2.5 billion to the deficit annually[1], or about 0.1 points of GDP.[2]

In addition to co-financing certain projects with private-sector players, the moderate cost to the public finances is the result of strategic decisions to finance those investments that are favourable to potential growth in the medium term, while limiting their impact on public expenditure:

- €15.6 billion are non-consumable appropriations deposited in the Treasury's account. For example, €7.7 billion will be used to build between five and ten "Campuses of Excellence" that will bring together universities, schools and research teams. These campuses will be allocated a certain capital; each year, they will draw down the interest generated by this capital, thus ensuring a permanent source of revenue independent from annual budgeting. These additional expenses will have no impact on the deficit, since the interest paid by the Treasury account will be secured by reductions in operating expenditures in the State budget.

- €6.5 billion will be allocated for loans, purchase of securities and equity financing. These will not negatively affect the State's net financial assets, as the general government will, as a well-advised investor, acquire financial assets at their real value. For example, the State will grant loans to private operators that are developing high-speed broadband networks. These investments, which are considered to be financial transactions under national accounting rules, will have no impact on the public deficit.

- €2.9 billion will be given out in the form of repayable advances – loans for which repayment is based on the success of a specific project, but which may entitle the government to collect fees over and beyond the principal and interest. If a project is successful, and independently of how it is considered in the national accounts – as expenditure or financial transaction – the long-term impact of this method of financing is neutral, since the advances granted at the start of the project are revenue-generating.

- In order to ensure France's long-term competitiveness, €10.1 billion will be used for subsidies or consumable appropriations in strategic sectors. Subsidies will be granted for research in cutting-edge areas such as nano- and biotechnologies, which will, over time, result in lucrative patents and competitive industrial applications. The government will pay out all of these subsidies in 2010, but the impact on the public deficit will be staggered: beneficiaries outside the general government (such as ANDRA) will receive the total amount of their allocations immediately, but for other entities it will take place over time, based on when they draw down funds.

The fact that the Maastricht definition of debt is not net of financial assets held by general government explains why future-oriented investments have a slightly greater impact on the debt than on the deficit – about €5 billion the first year and an annual average of €3.5 billion over the following four years. The requirement for government agencies which will receive funds to deposit them into the Treasury account ensures that they are consolidated, as long as they are not drawn down.

[1] These estimates do not include the expected returns on investments (interest, dividends and additional revenue produced by more dynamic growth), which is a conservative assumption for the programme period.

2.1.1. Structural balance trajectory

Table 3: Multiyear structural balance trajectory

	2008	2009	2010	2011	2012	2013
Structural balance (% potential GDP)	-3.1	-5.8	-5.8	-4.0	-2.8	-1.6
Change in structural balance (% potential GDP)	0.0	-2.6	0.0	1.8	1.2	1.2

In 2009, the consequences of the economic crisis brought about a sharp downturn in the structural balance (–2.6 points). Slightly more than one point of GDP of this loss can be attributed to measures for managing the crisis, primarily the budgetary recovery plan voted within the framework of the European Economic Recovery Plan (EERP). A negative overshooting of tax revenues, particularly from the corporation tax, was responsible for the loss of an additional 1.5 points; the drop in activity had a much more marked effect on these than the conventional elasticities would suggest.

The structural balance would be stable **in 2010**. Yet, this stability includes temporary deterioration factors connected to the suppression of the local business tax, as well as new factors involving support for economic growth: future-oriented investments. Without these two elements, structural balance would be up by 1/2 point of GDP for 2010. This short-term stabilisation in budgetary policy would prevent a too-early consolidation from jeopardising recovery efforts, while offering medium- and long-term support for the growth needed to create sustainable public finances.

Starting in 2011, the structural adjustment would be more pronounced, due to the combined effect of government-wide efforts to contain public expenditures and, to a lesser extent, a reduction in tax expenditures and social contribution exemptions. Moreover, after their negative overshooting during the crisis, tax and social security contributions – and tax revenues in particular – should progressively return to normal, slightly outpacing GDP in the medium term (elasticity of 1.2). In this way, they are expected to gradually make up for revenues lost during the crisis. Excluding the impact of new measures introduced between 2008 and 2013, tax and social security contributions should remain at roughly the same percentage of GDP as they were in 2007.

In all, **the structural balance should improve by an average of approximately 1.4 points per year for the period 2011–2013**. For 2011, the above-mentioned effects will be complemented by the disappearance of two temporary factors that will have contributed to the degradation of the balance in 2010. These are the extinction of measures for managing the economic and financial crisis (0.3 points of GDP) and the disappearance of temporary costs associated with reforming the local business tax (0.4 points of GDP).

Given our cautious macroeconomic scenario for the programme period (which assumes that the sizeable output gap that appeared in 2008 and 2009 will not be entirely closed), the public deficit in 2013 will still be partially cyclical.

[2] On the other hand, future-oriented investments will have a significant impact in 2010 on balances by sub-sector: appropriations will be fully paid out in the first year (negative impact on the State balance), mostly to State operators in the ODAC sub-sector. The balance of these ODACs will improve, since the appropriations will not be fully used the first year, or will be used for financial transactions.

2.1.2. Public debt trajectory

In 2009, the debt ratio is expected to have gained some 10 points of GDP, basically due to highly unfavourable economic conditions – given a nominal growth rate of –1.3%, stabilising the debt ratio required a general government surplus of 0.9 points of GDP. With the public deficit at 7.9 points, the stabilising balance gap contributed to an 8.7 points rise in the debt burden.

In addition, stock-flow adjustments will raise the debt by 1.3 points of GDP. This is primarily due to the various crisis management measures, such as loans to automobile manufacturers, which had no effect on the deficit from a national accounting standpoint, but which contributed to the public debt according to the Maastricht definition. Surpluses from the supplementary pension schemes and the Pension Reserve Fund (*Fonds de Réserve pour les Retraites* – FRR) were used to acquire financial assets, thus contributing to the gross debt according to Maastricht. Finally, the Maastricht debt definition is consolidated of intra-governmental claims. Therefore, even though the balance of the Treasury account was, at the end of 2009, close to the amount recorded one year earlier, reduced holdings of commercial paper purchased from Acoss and the Government Debt Fund (*Caisse de la Dette Publique* – CDP) with respect to the end of 2008 have added to the public debt.

In 2010, the debt ratio should increase by 5.8 points of GDP – a slower rate than in 2009, despite a slightly higher deficit. Indeed, nominal growth in activity should, to some extent, rein in debt ratio growth, and the drop in the State's cash position over the end of 2009 would explain the negative stock-flow adjustment expected in 2010 (–0.5 points of GDP). The total impact of future-oriented investments on the public debt should be only around €5 billion in 2010; between €2 and €2.5 billion of this will be registered as part of the deficit in the national accounts, and the remainder as financial transactions that, under the Maastricht definition, will add to the Maastricht public debt but will not affect net public debt (see Box 1).

Starting in 2011, net financial asset acquisition flows are assumed to be nil, and the debt ratio is expected to progressively slow under the effect of stronger growth and reduced deficits. It should reach 87.1 points of GDP in 2012 and begin to fall off in 2013, thanks to the public balance returning to a level above the stabilising point (see Table 2).

2.1.3. Public finance trajectory by sub-sector of the general government

Each sub-sector should help reduce the general government borrowing requirement through 2013.

Table 4: Lending capacity (+) / borrowing requirement (-) of the general government (% of GDP)

	2008	2009	2010	2011	2012	2013
General government	-3.4	-7.9	-8.2	-6.0	-4.6	-3.0
Central government	-2.9	-6.2	-5.9	-3.9	-3.0	-2.0
o.w.: State	*-2.8*	*-6.3*	*-7.6*	*-4.0*	*-3.1*	*-2.1*
o.w.: Other government bodies	*-0.1*	*0.1*	*1.7*	*0.0*	*0.1*	*0.1*
Local governments	-0.4	-0.4	-0.5	-0.4	-0.2	-0.1
Social security funds	0.0	-1.3	-1.9	-1.7	-1.3	-1.0

- The general government borrowing requirement would decrease by about 4 points of GDP from 2010 to 2013, thanks to the State's complying with the "zero real-term expenditure" growth rule ("norme zero volume"), and the spontaneous "catch-up" effect of tax revenues that dropped to abnormally low levels during the crisis. The extinction in 2011 of the various crisis management measures and the disappearance of the temporary cost of reforming the local business tax – both of which were financed by the State – should also play a role in this decrease.

- The breakdown of the central government balance into the State's balance and that of the ODAC (*Organismes Divers d'Administration Centrale* – other government bodies) was noticeably affected by the State's 2010 grants to the organisations responsible for future-oriented investments, most of which are ODACs (including the ANR, ADEME and the CEA[3]).

- Expenditure containment should enable local governments to reduce their deficit progressively by around 0.1 points of GDP per year from 2010 to 2013, allowing them to reach a balance close to equilibrium at the end of the programme period. This could be facilitated by setting a local expenditure target. During the National Conference on the Public Deficit meeting, a working group was mandated to discuss this topic. It will be co-chaired by Gilles Carrez, Chair of the Local Government Finance Committee, and Pierre-René Lemas, prefect, and will report on its findings in April.

- Finally, the balance of the social security funds – which includes the "Régime Général" as well as the complementary pension schemes and unemployment insurance – should begin to recover in 2011 thanks to ongoing spending containment efforts, particularly on health insurance spending (with an expenditure target – ONDAM – that is set to increase by less than 3% per year). Recovery will also be helped by spontaneous decreases in expenditures on unemployment benefits and a better outlook for the private-sector wage bill as the economic situation improves. By 2013, the social security funds' deficit should be nearly half of what it was in 2010.

2.2. Alignment with the National Reform Programme

The goal of the National Reform Programme is to create the conditions for a long-term increase in potential growth and thus restore the structural balance of public finances in the medium term. The effects of the structural reforms that the Government has pursued since 2007 will increasingly make themselves felt. The priorities for this programme period include continuing to modernise the French economy, structural reforms of the labour market, support to make French businesses more competitive and streamlining public policies and tax and social security contributions. These priorities were factored in when this Stability Programme was defined. In particular, they include major reforms concerning the elimination of the local business tax, which was weighting on productive investments. Future-oriented investments are also part of the Reform Programme (see Section 5.2).

[3] ANR: French National Research Agency (*Agence Nationale de la Recherche*); ADEME: French Environment and Energy Management Agency (*Agence de l'Environnement et de la Maîtrise de l'Energie*); CEA: Atomic Energy Commission (*Commissariat à l'Énergie Atomique*).

3. Analysis of sensitivity and comparison with the previous programme

3.1. Sensitivity to external assumptions

The international scenario underlying the projections is as follows:

- Oil prices will settle at US$77/bbl from winter 2009 through 2011, and subsequently maintain this level in real terms (i.e. the nominal price per barrel will rise by 1.75% p.a. from 2012 to 2013);
- It is conventionally assumed that the exchange rate between the euro and the dollar will be US$1.48 during the entire period under review;
- Global activity and world trade will begin to return to their medium- to long-term average as of 2011. World demand for French goods and services would increase by 6.6% per year starting in 2012, i.e. its average during the period from 1987 to 2007.

Overall, these assumptions are close to those of the Commission. It is nevertheless possible to evaluate the effect of unforeseen economic developments on the French economy. Below, we will examine the impact of greater world demand for French goods and services, higher oil prices and an increase in the exchange rate and the interest rates.

a) Impact of a stronger increase in world demand for French goods and services [4]

An increase in world demand for French goods and services would pass almost entirely on exports, after which it would spread to the rest of the economy, primarily through increased corporate investment.

Assuming constant nominal interest rates, a permanent increase of 1% in world demand would improve activity by about 1/4 points of GDP and generate about 40,000 extra jobs after three years. The impact on inflation would be low at constant exchange rates[5].

To illustrate the point, a 1% increase in world demand for French goods is equivalent to a temporary increase in US growth of about 1 point, given the importance of the American market in French exports of goods (8%) and the spill-over effects for the world economy. Should global demand slow, the orders of magnitude would be almost exactly the same, but in a negative direction.

Table 5: Impact on the French economy of a 1% increase in world demand for French goods and services (*)

(deviation from baseline scenario as a %)	**2010**	**2011**	**2012**
GDP	0.2	0.2	1/4
Total employment (thousands)	9	27	40
Consumer prices	0.0	0.1	0.1
Public net lending (in points of GDP)	0.0	0.1	0.1

(*) Permanent increase of 1% in world demand occurring in early 2010.

[4] The world demand variant and the oil variant have been revised to reflect the most recent evaluations based on the MESANGE France model.

[5] In this variant, the price of oil is considered to be exogenous and thus unresponsive to changes in world demand.

This shock would be the result of a significant increase in activity, an improved labour market and relatively low rate of inflation. Increased momentum of taxable jobs and payroll income would have a positive impact on tax revenue (VAT, corporation tax, personal income tax, social contributions and other taxes). The slight effect on inflation triggered by this demand shock would have little impact on expenditure growth, which would speed up less quickly than revenue. In all, public net lending would improve by about 0.1 point of GDP as of 2011.

b) Impact of higher oil prices

A rise in oil prices would increase imported inflation, which in turn would directly increase consumer prices at constant exchange rates. This automatic effect would be strengthened by the induced change in production costs and increases in wages to offset – in whole or in part – higher prices, which would add to the inflationary impact. The rise in consumer prices and the weakening of corporate profits would then converge to curb activity. These effects would also be felt in other net oil importing countries. By contrast, rising oil prices would add to the activity of net oil exporting countries, due to the increase in revenues that would result.

Our models incorporating an endogenous response by the rest of the world suggest that a lasting 20% increase in oil prices – rising from US$77 to US$92 bbl, for example, and at constant real interest rates and exchange rates – would bring about a drop in activity of 0.1 points and raise consumer prices by 0.3 point after one year.

Table 6: Impact on the French economy of a 20% increase in oil prices (*)

(deviation from baseline scenario as a %)	**2010**	**2011**	**2012**
GDP	-0.1	-0.1	-0.2
Total employment (thousands)	-4	-26	-50
Consumer prices	0.3	0.6	0.9
Public net lending (in points of GDP)	0.0	-0.1	-0.15

(*) A 20% rise per barrel at the start of 2010, exogenous real interest rate, endogenous response by the rest of the world.

The increase in oil prices would have a mixed impact on public revenue. On one hand, the drop in economic activity would have a negative impact on general government tax revenues through 2012, particularly from the corporation tax. Additionally, revenue sensitive to inflation (such as VAT) would increase in nominal terms. The net impact on revenue would be roughly neutral. By contrast, the impact of increased spending, largely due to higher inflation and a less robust labour market, would already be felt in the second year. As a result, the public balance would deteriorate by 0.1 point of GDP in the second year and 0.15 point of GDP in the third year.

c) Effects of a 10% appreciation of the euro against all other currencies without an economic policy response

A 10% appreciation of the euro against other currencies would reduce activity in France by about 0.7 point in the first year as it would make France less competitive on the export market and depress activity in other countries of the euro area. The fall-off in exports would be amplified by the accelerator effect and the Keynesian multiplier effect. Employment would also be affected by this slowdown.

As in the rest of the euro area, inflation would be moderated by an appreciation of the effective exchange rate.

Table 7: Impact on the French economy of a 10% appreciation of the euro against all other currencies (*)

(deviation from baseline scenario as a %)	**2010**	**2011**	**2012**
GDP	-0.7	-0.8	-0.8
Salaried employment (thousands)	-40	-114	-131
Consumer prices	-0.6	-1.4	-2.4
Public net lending (in points of GDP)	-0.2	-0.3	-0.5

(*) A 10% appreciation of the euro against all other currencies, at constant nominal interest rates.

An appreciation of the euro would have a negative impact on most taxes and therefore on public finances due to its adverse influence on activity and inflation. Moreover, a higher exchange rate would reduce social security contributions (which are based on the total wage bill). The resulting loss of revenue for the general government would amount to 0.3 point of GDP from the first year onwards. This phenomenon would be partially offset by a drop in expenditure in connection with lower inflation (about 0.1 points of GDP for the first year).

d) Impact of a 100-bp interest rate increase

A faster than expected recovery would lead to an earlier hike in interest rates in the euro area. An upward adjustment of both short and long-term interest rates would penalise activity in three ways:

- Productive investment would be affected by an increase in interest rates since higher interest expense would weaken solvency and lower profitability of capital.
- More expensive credit would also depress housing investments; moreover, rate hikes would encourage savings instead of consumption (substitution effect).
- If the euro appreciated as a result of such rate increases, the euro area would be less competitive vis-à-vis other countries, which would dampen activity.

At constant exchange rates, a 1% rise in short and long-term interest rates in the euro area would reduce activity by 0.2 point of GDP during the first year and 1/2 to 1 point of GDP during the second and third years. Inflation would register a mild decrease.

These evaluations take the macroeconomic balancing effect within the euro area into account. In other words, decreased demand in other euro-area countries would have a negative impact on the French economy.

Table 8: Impact on the French economy of a 100 bp rise in short and long-term interest rates in the euro area(*)

(deviation from baseline scenario as a %)	**2010**	**2011**	**2012**
GDP	-0.2	-0.5	-0.8
Total employment (thousands)	-10	-60	-100
Consumer prices	0.0	-0.1	-0.2
Public net lending (in points of GDP)	0.0	-0.2	-0.4

(4) Lasting 100 bp increase in short and long term interest rates at the start of 2010 at constant exchange rates.

Public finances would be negatively affected in two ways by a drop in interest rates. First, the cost of general government debt would rise due to higher financing and refinancing costs. Secondly, public accounts would deteriorate owing to weaker activity.

Decreasing growth would automatically push down tax and social security revenue. In addition, nominal expenditure would rise due to a depressed labour market and higher interest expense, although this would be slightly attenuated by its sensitivity to inflation.

3.2. Comparison with previous programme

Table 9: Comparison of 2009–2012 and 2010–2013 programmes

	2008	**2009**	**2010**	**2011**	**2012**	**2013**
2009-2012 Programme						
GDP growth rate (%)	1.0	0.2-0.5	2.0	2.5	2.5	
Public balance (% of GDP)	-2.9	-3.9	-2.7	-1.9	-1.1	
Structural balance (% of pot. GDP)	-2.4	-2.7	-1.4	-0.7	0.0	
Public debt (% of GDP)	66.7	69.1	69.4	68.5	66.8	
2010-2013 Programme						
GDP growth rate (%)	0.4	-2.3	1.4	2.5	2.5	2.5
Public balance (% of GDP)	-3.4	-7.9	-8.2	-6.0	-4.6	-3.0
Structural balance (% of pot. GDP)	-3.1	-5.8	-5.8	-4.0	-2.8	-1.6
Public debt (% of GDP)	67.4	77.4	83.2	86.1	87.1	86.6

Comparing the present Stability Programme with the one submitted in December 2008 highlights the consequences of the economic and financial crisis on both growth and the public balance.

Deterioration of the public balance in 2009 was roughly 3 1/2 points of GDP worse than had been forecast in the previous Programme. This can be explained by the following factors:

- **Growth forecast was revised downward sharply**, from 0.2-0.5% in the previous programme to –2.25%. This fall-off had a direct impact on the 2009 deficit – about 1 1/2 points of GDP.
- **Revenues reacted more strongly** than average elasticities (estimated on previous business cycles) had suggested. For example, once corrected for regulatory changes, the corporate tax dropped by an exceptional 39%, and VAT revenue fell by 1.9%, more than the drop in growth (–1.3% in nominal terms).

- **The fiscal stimulus package was completed**. Additional measures for supporting consumption were adopted within the framework of a second supplementary budget act (“loi de finances rectificative”). Some tax measures, including accelerated reimbursement of the research tax credit and the corporation tax carry-back, were more popular than expected. In all, the recovery measures voted in December 2008 and February 2009 represented, for 2009 alone, about 1.1 points of GDP.

For 2010, the current Stability Programme expects that the public balance will worsen by 0.3 points of GDP over 2009. This is due to the following factors:

- **Measures taken by the Government in 2009 to pave the way out of the crisis and to improve the French economy's long-term growth potential**. Thus, the reform of the local business tax will have a negative impact of 0.6 points of GDP on the deficit, 0.4 points of which are temporary implementation costs that will disappear in 2011. Spending on future-oriented investments will add about 0.1 points of GDP to the 2010 deficit (see Box 1). Despite their higher cost in 2009, the impact of the stimulus package measures on the variation of deficit between 2009 and 2010 would remain the same. This is due to the carryover of unused appropriations from 2009 and the continuation of certain measures, such as early reimbursement of the research tax credit and the Social Investment Fund (*Fonds d'Investissement Social* – FISO).
- **A downward revision of growth forecast**, which is now estimated to be 1.4% for 2010, compared with a forecast of 2.0% in the previous Programme, which explains the loss of 0.3 points in the 2010 balance compared with last year's Programme.
- **A magnified productivity cycle**. The crisis will have a strong effect on the productivity cycle in 2010, and the private-sector wage bill should increase at a much slower rate than GDP (0.3% in nominal terms, against 2.4%). This was not the case in the previous Programme, and should lower social security contributions and revenues from the CSG[6].

Over the medium term, the general government balance will improve at a faster rate than planned in the previous Programme, by about 0.7 points of GDP per year. This is due to:

- Even tighter containment of public spending throughout the general government sector, which will be possible thanks notably to:
    - A wide-ranging action plan for reducing State expenditures. It will be introduced in April 2010 by the Minister for the Budget and Public Accounts, as requested by the President of the Republic.
    - The efforts of several working groups that were set up in the wake of the first meeting of the National Conference on the Public Deficit on 28 January 2010. Based on their findings, measures will be decided on in April 2010.

  A more ambitious national healthcare expenditure target (ONDAM) will also play a part. In last year's Programme, increase in spending was capped at 3.3% per year, compared with less than 3% in the current Programme.

  Moreover, the timeline for pension reform will be discussed with the social partners during the social agenda meeting on 15 February 2010.
- A policy for reducing tax expenditures and social contribution exemptions, which will save €2 billion annually starting in 2011
- Increase in tax revenue, which will slightly outpace GDP growth (elasticity greater than unity). This is the result of a catch-up phenomenon following the negative overshooting in revenues observed during the crisis. We now forecast that the tax and social security rate

[6] Contribution Sociale Généralisée – General Social Security Contribution

will return to its 2008 level in 2013 (after correction of any new measures introduced in the intervening period).

- Elimination of one-time crisis-management expenses incurred in 2010 (0.3 points) and the temporary cost of reforming the local business tax (0.4 points).

The adjustment of the public debt trajectory reflects the updated deficit and nominal growth forecasts together with a higher stock-flow adjustment in 2009 but a lower one in 2010. The previous Programme used a standard assumption of null stock-flow adjustment starting in 2009.

4. Change in general government expenditure and revenue

4.1. General government expenditure

Table 10: Change in general government expenditure

(average per year in real terms, excluding transfers between general government sub-sectors[7])	**2010-2013**
General government	**0.9%**
Central government (APUC)	-0.1%
Local governments (APUL)	0.9%
Social security funds (ASSO)	1.6%

Bringing the deficit down to 3% of GDP by 2013 will require tight spending containment by every general government sub-sector. For the 2010–2013 programme period, this implies a growth in public expenditure at half of its past trend rate.

4.1.1. State expenditure

After neutralising the effects of changes in perimeter, the impact of the stimulus package in 2009–2010 and future-oriented investments, changes in State expenditure will be limited to, in nominal terms, 1.2% in 2010, 1.5% in 2011 and 1.75% in 2012 and 2013, which implies a stability in volume for the Programme period 2010-2013. Spending in 2009 remained within the cap stipulated in the Initial Budget Act (“loi de finances initiale”, excluding economic recovery spending). This was possible – despite the economic crisis and the corresponding increase in expenditure – thanks to spending control in areas unaffected by the economic situation and lower interest charges on the public debt. The State's remaining debt to Social Security was paid off.

The Initial Budget Act for 2010, the second year in the 2009–2011 three-year budget, contains several objectives:

- To accompany and strengthen the country's emergence from the economic and financial crisis, by not withdrawing support for growth too soon, and by highlighting a limited set of long-term priorities.

[7] Changes in general government expenditure by sub-sector between 2010 and 2013 do not include transfers between general government sub-sectors. In the national accounts, change in expenditure by sub-sector is blurred by one-time variations in the transfers between the State and local authorities in connection with the reform of the local business tax (transfers from the State to these authorities in terms of revenues collected by the State but earmarked for local authorities and minor management fees paid by the authorities to the State).

- To continue spending containment efforts with a stable budget in real terms, while strengthening the effectiveness of that spending.

Full implementation of the recovery plan in 2010 will allow France to complete its 2009 investment programmes and to continue its support for growth and jobs. Appropriations in the 2010 Initial Budget Act (€4.1 billion) will be combined with recovery plan appropriations carried over from 2009 (€1.3 billion).

The 2010 Initial Budget Act places emphasis on a limited set of priorities, such as higher education, research and sustainable development. It also maintains the goal of increasing the effectiveness of public spending while holding spending growth to the projected rate of inflation. The spontaneous increase in social expenditure during the crisis, the growing number of pensioners and the increasing number of levies on revenue for the benefit of the EU means that additional efforts must be brought to bear on controlling spending in other areas.

Such efforts are made possible by the reforms adopted within the context of the General Review of Public Policies, which allow the State to replace only one out of every two retiring civil servants. This rule, which will be applied each year, will eliminate 33,749 positions in 2010.

The 2010 Supplementary Budget Bill that the Government presented on 20 January 2010 concerns future-oriented investments. It introduces €35 billion in additional appropriations into the State budget, to be used to finance investments that will encourage France's growth potential. These allocations will be paid out during 2010 to various organisations (including public establishments, funds, societies, etc.), and used for the sole purpose of financing projects with high potential for the economy. These projects are in the sectors of higher education and research, technology transfer and SMEs, sustainable development and the digital economy.

These appropriations are spread among various newly-created programmes within the existing missions of the State's general budget. This ensures that the government's policies are clear, that the allocations are kept completely separate from other general budget expenditures, and that their use can be optimally tracked.

Future-oriented investments will introduce a one-time, €35 billion increase in the budget deficit in 2010, but they will not affect the budget balance in subsequent years. The impact of the public balance on the national accounts should be between €2 and €2.5 billion annually (see Box 1). Given their exceptional and one-shot nature, appropriations will be monitored outside of the State expenditure rule. On the other hand, the supplementary interest charge connected with the borrowing is covered by the expenditure rule, and is thus fully offset by an equivalent reduction in the State's current expenditure. This effort is part of a forward-looking policy of reducing the State's current expenditure.

Multiyear budgeting has improved the quality of the budgeting process and of State budget management. Therefore, for 2011–2013, the Government will present a second three-year budget in the fall of 2010.

For this three-year period, strict compliance with the so-called "zero real-term expenditure" growth rule will be enforced, which will require strenuous efforts in every part of the budget. This is because:

- Expenditure inherited from the past is rising faster than before and absorbing a growing proportion of the State's room for manoeuvre. In particular, the retirement of the baby-boomers will increase pension expenditures for civil servants.

- The predicted rise in the State indebtedness will incur a corresponding rise in debt servicing charges.

In sum, for the period 2011–2013, pensions and debt servicing will absorb almost all of room to manoeuvre provided by the pegging of spending increases to the rate of inflation.

The General Review of Public Policies will result in additional savings during the 2011–2013 budget period. A new phase of the project was introduced in the fall of 2009, which, among other measures, will continue the policy of replacing only one out of every two retiring civil servants.

Special emphasis will be placed on support functions, both for the State and its operators, with the goal of significantly lowering spending in this area over the next three years. To achieve this, cross-departmental projects will be set up to address spending on IT, logistics, communication, training and examinations. Taking into account ongoing actions dealing with procurement, real estate and payroll, by the end of the programme period, the State will have streamlined all of its support functions.

Finally, in line with the French President's statements during the first meeting of the National Conference on the Public Deficit, the Minister for the Budget, Public Accounts, the Civil Service and State Reform will, at the April meeting of the Conference, present a wide-ranging action plan for reducing government spending. A detailed description of how this will be implemented will be included in the upcoming three-year budget.

4.1.2. Expenditure of central government bodies

Central government bodies that are considered as State operators will be very directly involved in the State's effort to control expenditure[8]. To accomplish this, on 3 December 2009, the Minister for the Budget, Public Accounts, the Civil Service and State Reform introduced new governance rules that should help streamline the way in which these bodies function. The goal is to bring the operators' management efforts in line with those of the State.

In particular, this will mean that, starting in 2011, operators will replace only one of every two retiring civil servants, so that their workforce reduction effort matches that of the State. As for the State, this is an overall objective that will be adapted to each operator's specific situation, specifically in terms of demographics. In addition, operating expenditures will be reduced, in particular thanks to a policy of pooling resources, both between operators and between operators and government departments.

These rules of conduct and governance for State operators are in addition to the tools implemented to upgrade supervision of the overall sub-sector of central government bodies (ODACs).

4.1.3. Expenditure of the social security funds

Benefits paid out by the social security funds increased substantially in 2009 (+5.2%), due to rising unemployment claims as a consequence of the economic crisis. They are expected to continue to

[8] The salient features of State operators are that they carry on public service activities, are mostly financed by the State and are under the State's direct control. The concept of operator nevertheless reflects other criteria than those found in the national accounting. Many State operators fall outside the ODAC sub-sector – some fall within the social security funds (ASSO) or local government (APUL) sphere – or even outside the perimeter of the general government. These non-ODAC entities represent about 10% of operator expenditure.

rise by 3.8% in 2010, despite a lesser growth in unemployment and the fact that family benefits were not re-indexed for inflation on 1 January 2010. For 2011–2013, the upward trend in benefits should be moderate (3.1% on average), thanks to an improved labour market and the implementation of ambitious objectives concerning control of healthcare benefits.

Healthcare benefits

Following a 3.5% rise in 2008, the national healthcare expenditure target (ONDAM) for 2009 was almost respected and should total 3.4%. This is still less than an average annual trend of 4.5% without efforts to control spending. This moderate growth in healthcare spending is the combined effect of actions by the conventional partners to control unnecessary prescriptions, lower prices (of pharmaceuticals, radiology and biological testing, in particular), and an increase in copayments (from 50% to 70%) for patients not under managed care.

In 2010, efforts to control spending via the ONDAM will be stepped up, with a more ambitious goal (3%) than for 2009. Every sector will be called on to play a part: similar growth rates will be set for both private practice and hospital treatment, and the medico-social institutions will have a growth target that is lower than that for 2009.

With respect to private practice, efforts to control unnecessary prescriptions are the continuation of actions carried out in 2008 and 2009. In 2010, these will be complemented by measures designed to boost the efficiency of the care-giving system, including lower prices for certain drugs and reduced fees for certain medical specialties (biological testing and radiology). Finally, a new reimbursement rate of 15% will be introduced for drugs whose usefulness is deemed to be limited.

In terms of hospital spending, the provisions of the Hospitals, Patients, Healthcare and Territorial Organisation Act should bring about considerable improvement. The creation of Regional Healthcare Agencies (*Agences Régionales de Santé* – ARS) will introduce unified management of France's regional healthcare system. This will create better synergies between private practitioners, hospitals and medico-social institutions, and will help streamline the healthcare system.

In addition, a €2 increase in the flat-rate charge in medical, surgical and obstetrics departments, as well as for follow-up care and rehabilitation will result in approximately €0.2 billion in savings. Under the terms of the action plans of the Ministry for Health and the Economic Committee on Healthcare Products, efforts to control prescriptions and hospital prices will be stepped up. There will be better oversight of spending on products in the *liste en sus* (supplementary list of high-cost innovative treatments), while nationally-fixed rates for various types of treatments will more closely correspond to observed costs.

The **Multi-year Public Finance Planning Act** of 9 February 2009 set a 3.3% cap on increases in healthcare spending. For 2010, given the need to curb public spending even more sharply, the report published prior to the public finance policy debate in June 2009 called for this target to be adjusted downward. The 2010 Social Security Budget Act thus set the national healthcare expenditure target at 3.0%. New and ongoing efforts to control spending should keep this target under 3% for the period 2011–2013. A working group was set up in the wake of the National Conference on the Public Deficit to identify any additional regulations that need to be put in place to meet this objective.

Old-age benefits

Demographic changes in France, as the initial baby-boomers reach retirement age, mean that old-age benefits will continue on an upward trend throughout the programme period. They will increase by 4.3% in nominal terms in 2011-2013, against an average of 4.2% in 2009–2010.

This relative stability in nominal growth indicates a slowdown in real terms. This is partially explained by the early-retirement scheme that was put in place in 2003 for those who started working at an early age. Its gradual introduction fed the growth in benefits through 2008. After this, stricter entry requirements and a drop in the number of eligible workers – due to the introduction of a higher minimum school-leaving age for those born in 1953 and after – has kept the number of beneficiaries down.

In recent years, two reform efforts have been launched to ensure the long-term survival of France's old-age insurance system.

Under the terms of the reform of 2003, the insurance period required to be entitled to a full pension will be lengthened, based on a shared approach to increased life expectancy. Thus, the period will increase to 41 years in 2012 (for the generation born in 1952), and to a possible 41.5 years in 2020. Additionally, for the first time, retirement schemes for the civil service were reformed, in order to bring them gradually into line with the private sector. The insurance period was increased from 37.5 years to 40 years in 2009, and then will evolve along with the private sector, with the introduction of a premium and penalty system (*décote*/*surcote*) and price inflation indexing.

To create a more equal retirement system, the reform of special pension schemes in late 2007 was part of efforts to bring pensions in line with private-sector rules. The same set of parameters used to calculate special pensions are now used in all pension schemes, including progressively extending the insurance period to 40 and then 41 years, a penalty system and price inflation indexing.

The Social Security Budget Acts for 2009 and 2010 include additional measures with respect to seniors receiving the lowest-level pensions (a 25% increase by 2012 in the solidarity allowance for the elderly - *allocation de solidarité aux personnes âgées* – ASPA). They also maintain the allocation of supplementary pension years to mothers.

Employment for older workers is another priority for the government, and a series of measures have been taken. These include more flexible rules on combining earned income with a pension, the elimination of forced retirements, and increasing the rate used to calculate pension premiums to 5%. In addition, civil servants whose job classification (*catégorie active* – for positions considered risky or physically arduous) grants them early retirement may continue working if they so desire. The "Older Worker Agreements" in the 2009 Social Security Budget Act encourage businesses with more than fifty employees to put such agreements in place, or to create an action plan to do so. Failure to comply will result in a penalty equivalent to 1% of the company's wage bill as of 2010.

As announced by President Sarkozy, 2010 will witness a significant pension reform. The goal is to ensure the long-term sustainability of France's pension system, which has been weakened by demographic changes and the economic downturn. This reform will encompass both the public and private sectors, and a no-holds-barred approach will be taken to restore equilibrium. Decisions will be handed down and enacted before the end of the year.

Other social benefits

Family and housing benefits are expected to rise by 1.8% in 2010, compared with 3.6% in 2009. The difference is partly due to indexation of family benefits, which belatedly included adjustment for inflation in past years. Over the course of 2011–2013, the aggregate should return to a trend comparable to the previous programme period, i.e. an average annual increase of 2.6%.

Unemployment benefits should also return to their pre-crisis levels. After very strong growth in 2008 and 2009, they are slated to level off in 2010. The expected upturn in the labour market will then bring them down by 5% per year for the period 2011–2013.

Table 11: Change in expenditure of the social security funds between 2011 and 2013 (in nominal terms)

	2008	2009	2010	2011-2013*
ONDAM	3.5%	3.4%	3.0%	<3.0%
Family-Housing	3.9%	3.6% |	1.8%	2.6%
Old age	5.3%	4.5%	3.9%	4.3%
Unemployment	-0.6%	18.5%	7.4%	-5.4%
Total expenditure	4.1%	5.2%	3.8%	3.1%

** Average annual growth rate, 2011-2013*

4.1.4. Expenditure of local governments

The Programme foresees limited growth in local expenditure, which is compatible with a gradual return to equilibrium in the balance of local governments. Local authorities will play an active role in consolidating general government budgets.

Several factors can be expected to help slow local spending in the medium term. The Regional and Local Government Reform Bill, presented by the Government in the fall of 2009, should help streamline local expenditure. The bill is based on the work of the Balladur Committee, and is designed to redefine local institutional structures, simplify and strengthen inter-municipal structures ("intercommunalité"), modernise local taxation and clarify areas of competency of local governments. By addressing the problems caused by organizational complexities, it should help local authorities eliminate unnecessary expenses and inefficiencies, while at the same time improving the quality of public services.

Moreover, with the full implementation of certain benefits, such as the Attendance Allowance (*Allocation Personnalisée d'Autonomie*) and the Disability Compensation Benefit (*Prestation de Compensation du Handicap*) social expenditure should slow. Besides, the next cycle of local investment will be less dynamic than its predecessor, which was characterised by a marked rise in construction costs. This slowdown in medium-term investment will be all the more marked due to the anticipation of investments within the context of the Recovery Plan, thanks to early payments from the VAT Compensation Fund in 2009 and 2010.

The effort to streamline local expenditure will be taken up with a working group on containing local spending that was set up during the National Conference on the Public Deficit. The group, co-chaired by Gilles Carrez and Pierre-René Lemas, will examine various ways to keep local spending down, and will report on its findings in April 2010. It will review the factors that led to increased local expenditure starting in 1980, and will evaluate the impact of State-fixed norms. The group will then make detailed proposals to cushion this impact and will study how local spending objectives could be introduced.

4.2. Public revenues

4.2.1. The Government's tax strategy

Given France's high aggregate tax and social security rate, the Government will not raise taxes as a means to restore the balance of public finances. Nevertheless, to boost the attractiveness and competitiveness of the country's economy, adjustments may be made to the tax and social security structure, but without, modifying the overall rate over the programme period vis-à-vis its pre-crisis level.

The government's tax policy will focus on three major areas. An initial series of reforms were already carried out in these areas during the first years of the President's term in office. They include:

- **Economic effectiveness to put taxation at the service of competitiveness, investment, growth and employment**. Special emphasis is placed on SMEs, including a threefold increase in the research tax credit, a Wealth Tax reduction for individuals who invest in SMEs, the tax measures introduced in the Economic Modernisation Act (in particular the creation of the freelance entrepreneur status). This area also includes reforms for making work more attractive and boosting purchasing power via making overtime hours tax-free, tax credits for home buyers, compensation in lieu of supplementary time off, early access to employee savings plans and reform of profit-sharing schemes. The gradual disappearance of the annual flat-rate corporation tax and the elimination of the local business tax in 2010 will also contribute to making France more attractive for businesses.

- **Environmental effectiveness to put taxation at the service of sustainable and environmentally friendly growth**. The "sustainable development" tax credit will be reformed and the "green" component of tax credits for the acquisition of a primary residence and interest-free loans will be strengthened. The cap on the amount of tax-deductible interest on loans for highly-energy-efficient houses.

- **Justice and fair taxation:** the 2009 Budget Act included a series of measures to cap tax expenditures, in order to put an end to the most unfair situations. Moreover, in line with the elimination of the local business tax, the Government has announced its desire to go forward with efforts to eliminate inappropriate transfers between authorities, thus providing regional and local authorities with fairer, more modern and more effective property taxes.

These priorities are reflected in the measures provided for in the Budget Bill for 2010.

The local business tax, which was assessed on productive investments, will be eliminated as of 2010. This reform will shore up efforts already underway in favour of private investment. This reform is driven by an economic need to make France more attractive by giving businesses a freer hand to invest, recruit and conquer new markets. An additional impact of the reform will be to allocate new tax revenues to local authorities, including the new contribution based on value-added produced by companies and the flat-rate tax on *entreprises de réseaux* (large, energy-grid dependent firms), which is established at the national level.

To meet the challenge of climate change and honour France's commitments in this area, the Government has proposed the creation of a carbon tax (on oil, gas and coal, based on their CO_2 content). This helpful economic instrument will allow France to meet its emission targets at a minimal cost to society. Eco-taxation should help encourage energy savings, reduce the country's oil and gas expenditures and give a boost to the development of green technologies. The Constitutional Council's ruling of 29 December 2009 has delayed the entry into force of the carbon tax, but this has not blunted the Government's desire to press on with this reform, as the tax's ultimate objectives were not called into question. A second bill will be presented during the course of the year with the idea of instating the carbon tax for 1 July 2010.

Additionally, in the second half of 2009, the Government began efforts to evaluate the effectiveness of various tax expenditures and social contribution exemptions, with the goal of sharply cutting them back. During the National Conference on the Public Deficit on 28 January 2010, the President of the Republic stated his desire to go forward with efforts to dismantle and, if need be, reduce these schemes. For the upcoming programme period, we thus expect to reduce the cost of tax expenditures and social contribution exemptions by €2 billion annually starting in 2011 (out of a total of €70 billion in annual revenue losses in tax expenditures alone).

4.2.2. A gradual catching-up of tax and social security contributions after their steep decline during the crisis

After falling off sharply in 2009, the aggregate tax and social security rate is expected to make up for crisis-related losses and start climbing again in 2011. It should reach 43% of GDP by 2013, thus close to its pre-crisis level (43.2% of GDP in 2007).

This is based on the assumption that elasticity of these contributions will be slightly positive (1.2 between 2011 and 2013), which would gradually make up for the drastic drop in revenue, particularly the corporation tax, observed during the crisis.

This is consistent with the assumption that growth will pick up again in 2011, after two years (2008/2009) of far below potential growth and a one year (2010) slightly under par. Over the long term, the elasticity of taxes and social security contributions to growth is close to unity but may experience cyclical fluctuations. Thus the elasticity of taxes and social security contributions, especially taxes collected by the State, may be slightly above unity when growth is strong and the wage bill is catching up.

Above all, the good indications concerning tax revenues that were observed in late 2009 following the presentation of the 2010 Budget Bill appear to confirm our medium-term scenario, and lead us to expect that the situation will return to normal faster than we had originally anticipated.

The programme period also includes the full set of tax and social security contribution-related measures that have been enacted since 2007. In 2010, the positive effects of the country's economic recovery plan (early reimbursement of the research tax credit and the corporation tax carry-back, payment of VAT reimbursements in monthly instalments, a two-thirds reduction in taxes owed by six million households in the lowest tax category) will be offset by the temporary cost of the reform of the local business tax. The disappearance of this one-time cost will account for 0.4 points of GDP in the growth of tax and social security contributions in 2011. For the whole period, the aggregate tax and social security rate will rise by nearly two points to reach a level lower than that of 2007 (43.2% of GDP).

4.2.3. Change in revenue per sub-sector

a) State revenue

In 2010, the State's net tax revenue is expected to rise noticeably, for four reasons:

- The positive effects of the recovery plan, which cost was mainly concentrated in 2009. One-time measures (reduced income taxes and payment of VAT reimbursements in monthly instalments) and an early reimbursement policy (research tax credit and corporation tax carry-back) will induce a growth of €14.8 billion of the Stat’s net tax revenue.

- Suppression of the local business tax. In 2010, the State will temporarily be allocated revenues that will, in 2011, be assigned to regional and local authorities (the business property contribution, a second contribution based on value-added produced by companies and the flat-rate tax on *entreprises de réseaux* (large, energy-grid dependent firms).

- The introduction of the carbon tax, expected for mid-2010.

- The economic upturn starting in 2010 will automatically result in net tax receipts that outstrip growth; revenues will be boosted by the corporation tax, which fell off sharply in 2009 and should begin to recover in 2010, despite an assumption that taxable profits would drop in 2009. Other tax revenues will be less dynamic, because some of them are based on 2009 assessments (such as the income tax).

Starting in 2011, revenues will rise, stoked by:

- **More favourable economic conditions** which should, by the end of the programme period, restore the State's revenues to their 2008 levels, barring any new legislation

- **The Government's efforts to reduce tax expenditures and social contribution exemptions** by some €2 billion annually (out of a total of €70 billion in annual revenue losses in tax expenditures alone). This re-evaluation of certain exemptions, which was confirmed by President Sarkozy on 28 January 2010, will be based on in-depth examination by the Government of the effectiveness of such measures.

b) Revenues of social security funds

After holding up well in 2008 (+3.8%), social security contributions were hard-hit by the economic crisis, and shrank by 0.4% in 2009. The marked drop in the private-sector wage bill (-1.6%[9]) is expected to put particular strain on the tax base and thus lower social security contributions and revenues from the CSG. The social security funds have benefited from new measures for cushioning the drop in revenue, particularly a tax on supplementary social security schemes (€1 billion) and the creation of a flat-rate social security levy on wage savings (€0.4 billion).

In 2010, growth in social revenues will be slow (1.2%), as the private-sector wage bill will remain sluggish (0.3%). Nonetheless, they should receive a boost by the introduction of new measures in the 2010 Social Security Budget Act, particularly a doubling of the flat-rate social security levy on wage savings (*forfait social sur l’épargne salariale*), which will net €0.4 billion. Another important measure is a one-time levy on supplementary social security schemes (*taxe sur les organismes*

[9] As defined by Acoss. The drop is 0.8% as defined by the national accounts.

complémentaires), which will ensure that every part of the country's healthcare system helps finance efforts to fight the flu pandemic (€0.2 billion).

By the end of the programme period, the improvement of the economic situation would allow the private-sector wage bill to grow significantly. This is expected to result in higher social security contributions. Growth rates (corrected for unusual occurrences) should thus return close to their pre-crisis levels, or an average of 4.2% for the period 2011–2013, against 4.1% for 2006–2008.

c) Revenues of local governments

To factor in the low spontaneous dynamism of tax bases in the past, the elasticity of local taxes is assumed to be slightly less than one during the 2011–2013 programme period (0.9 on average). In particular, we assume that tax revenues related to housing transactions (*droit d'enregistrement sur les mutations à titre onéreux* – DMTO) will only partially catch up after their sharp drop-off during the crisis. This is based on a standard assumption that local tax rates will increase during the programme period in line with past observations.

5. Sustainability of public finances

5.1. Continuation of structural reforms

Despite a severe worldwide recession, France went ahead with structural reform efforts that it began in 2007. Its goal is to maintain and encourage employment, and to support investment and boost the country's competitiveness in order to increase the French economy's growth potential and hasten the consolidation of public finances.

This reform programme is wholly in line with the European framework of the Lisbon Strategy for Growth and Jobs.

A. Labour market reforms

The array of labour market reforms enacted in recent months, combined with those introduced in 2007 and 2008[10], should stimulate both supply and demand, as well as improve supply/demand synergies. The goal of streamlining the labour market and improving the qualitative and quantitative aspects of working is expected to increase employment rates and thus improve public finances.

France adapted its employment policy to the crisis in order to limit job losses and sustain growth, particularly via short-time working, eliminating employer contributions for very small enterprises and actions in favour of apprenticeships and the young.

The new Pôle Emploi, operational since 1 January 2009, offers better synergies between the needs of firms and of jobseekers. Pôle Emploi is the result of the merging of the French National Employment Agency (ANPE) and the Unemployment Benefits Funds (ASSEDIC), but maintains the existence of a joint unemployment insurance scheme. This reform has a twofold object. The first

[10] These include the Work, Employment and Purchasing Power Act of 21 August 2007; the Labour Market Modernisation Act of 25 June 2008; the Act of 1 August 2008 concerning the rights and obligations of jobseekers; and the Act of 20 August 2008 reforming workplace representation and working hours.

is to streamline procedures for users – companies and jobseekers alike – by means of a nationwide network of multi-purpose offices providing a complete range of recruitment and placement services. The second involves providing a wider set of services offered to all users of public services and improving the functioning of the labour market.

In terms of unemployment benefits, a new benefits payment scheme was introduced on 1 April 2009. The idea is to create a clearer, more transparent and fairer system offering a more direct correlation between the contribution period and the extent of benefits. The waiting period for access to benefits has been reduced from six months to four, making the system more responsive. This is of particular benefit to young people and those whose professional careers have been less than smooth.

Professional training reform was introduced with the law of 25 November 2009. It represents an important step forward in improving the mobility and employability of active workers, particularly via the creation of the Joint Fund for Securing Career Paths and the setting aside of training-related funds collected from SMEs and VSEs. The reform alters the existing structures so that training funds can more easily be directed to those most in need of training. It also provides fresh impetus to the training system, simplifying it and adapting it to individual needs.

Labour demand should benefit from the June 2009 introduction of the Working Solidarity Benefit (*Revenu de solidarité active* – RSA). The RSA was designed to encourage professional activity by ensuring that a return to work means higher revenues in the long term, thanks to the combination of earned income and benefits. The RSA replaces the Minimum Integration Income (RMI), the Single Parent Allowance (API) and several other temporary lump-sum payments such as the Back to Work Bonus (*prime de retour à l'emploi*). By the end of November 2009, more than 1.3 million requests for benefits had been filed with the Local Family Benefits funds.

Controlling labour costs will continue to encourage those with lower skills to find work. The National Minimum Wage (SMIC) was not adjusted in 2009 (except for inflation), which encourages the hiring of low- and unskilled workers. Among other measures, the law of 3 December 2008 concerning earned income established an expert committee tasked with providing an economic point of view on adjustments to the National Minimum Wage. In its first report, submitted on 1 June 2009, the committee recommended that the National Minimum Wage not be adjusted that year. With the committee's decision handed down on 30 November 2009, the minimum wage will increase by 0.5% on 1 January 2010.

Finally, to encourage the creation of new businesses, the Economic Modernisation Law of 4 August 2008 called for the creation of the freelance entrepreneur status, which entered into force on 1 January 2009. As a result, more than 500,000 requests for the new status were registered in 2009.

B. Goods and services market reforms

In terms of the goods and services market, the Economic Modernisation Act (LME) of 4 August 2008 introduced wide-ranging reforms to certain structures of the French economy, and is expected to provide sustainable impetus to its growth potential.

A number of the LME's measures were designed to encourage SME activity, via three means: improved access to financing by SMEs (boosting the equity of French SMEs and easier access to credit thanks to the public agency OSEO); improved access by SMEs, particularly innovative ones, to public procurement contracts and international markets (with the help of the Ubifrance agency); and the creation of a more SME-friendly regulatory environment (a reduced administrative burden thanks to a "one-stop shop" approach to business registration, and procedures for making it easier to pass on a business).

The Economic Modernisation Act introduced strict rules, which came into force on 1 January 2009, designed to reduce payment times between companies. It caps the times stipulated in a contract, in order to reduce the number of businesses that fail due to cash flow problems.

Significant efforts are underway to encourage innovation and productivity gains resulting from technological progress. The research tax credit has been extended, in order to provide continuing support for companies' R&D programmes.

The LME also created the Competition Authority. It began work on 2 March 2009 and is now fully operational. It has jurisdiction over cases of anti-competitive practices (redefined by the Ordinance of 13 November 2008) as well as over mergers. On 16 December 2009, the Authority issued a set of new merger-related guidelines that integrate the full set of changes introduced by the LME.

In the telecommunications sector, France's Telecommunications and Posts Regulator (*Autorité de Régulation des Communications Electroniques et des Postes* – ARCEP) awarded Free a license to operate a 3G licence in metropolitan France, following a call for tender launched on 1 August 2009. The arrival of a fourth operator on the market should increase competition and result in lower prices for consumers.

LME reforms in the retail sector[11] are already beginning to bear fruit. Listing fees fell sharply, from 30–35% of product prices in 2008 to 5–10% in 2009. The law also fostered competition between major retailers by reforming licensing arrangements in order to facilitate the creation of new retail shops. In the first half of 2009, permits were granted for 359 shops with sales areas over 1,000 sq. metres, or a total of 1.425 million sq. metres.

C. Streamlining tax and social security contributions and public policies

Streamlining tax and social security contributions is a key part of France's structural reforms, within the context of the General Review of Tax and Social Security Contribution System (*Revue Générale des Prélèvements Obligatoires* – RGPO) that was set up in the summer of 2008. Two major reform efforts got underway in 2009: the reform of the local business tax and the introduction of a carbon tax.

The share of the local business tax on equipment and movable property, which represents a burden on company productivity, has been eliminated. This will provide impetus for economic effectiveness and firms' competitiveness. Investment by businesses is expected to increase, thanks to a drop in the marginal cost of capital. Lower production costs should result in lower production prices.

The creation of a carbon tax, which is slated to come into effect on 1 July 2010, should improve environmentally-oriented taxation.

Public policy changes were also introduced within the context of the General Review of Public Policies (RGPP), which began in the summer of 2007 with the goal of increasing the effectiveness of public action. Every ministry is concerned, and because of the Review's very wide scope, a ground-breaking structure for implementing and monitoring reforms was put in place. To ensure

[11] Including the freedom to negotiate prices, greater ease in opening new retail spaces and changes to the structure of *département* commissions responsible for issuing site licences.

that these reforms are long-lasting, the full set of measures decided upon within the framework of the RGPP were integrated into the State's 2009–2011 three-year budget, presented as part of the Multiyear Estimates Act.

High-profile reforms were carried out. In April 2008, the General Tax Directorate was merged with the Public Accounting General Directorate. The new structure, the Public Finances General Directorate (DGFiP), with its 130,000 employees, will make life easier for taxpayers, as well as improve the efficiency and performance of State services. Placing the National Gendarmerie under the authority of the Minister for the Interior, which took place on 1 January 2009, will make France's security forces more effective, and the pooling of support functions will result in substantial savings. A reform of France's judicial jurisdictions has eliminated 62 labour relations boards, 55 commercial courts and 6 district courts. Finally, reform of the State's decentralised administrations is expected, by 2011, to reduce the number of State services at region and *département* level.

5.2. Future-oriented investments will stimulate growth

Stimulating potential growth is one of France's main priorities. The goal of future-oriented investments is to improve productivity through targeted and financially viable projects in the areas of research, innovation, industry, higher education, training and sustainable development.

For more than two decades, various economic studies have shown the extent of the economic and social returns linked to investments in technology sectors and in human capital. State intervention is necessary for financing some of these high-potential projects, which are too large for the private sector alone, and which will generate substantial returns for the economy.

Future-oriented investments are in line with the Lisbon Strategy for Growth and Jobs. They represent two of the Strategy's three pillars – the economic pillar (investments in the digital economy, innovative industrial processes, SMEs, higher education, training and research) and the environmental pillar (investments in renewable energies, the nuclear energy of tomorrow, transport and sustainable urban planning, and green building renovations).

These types of investments were designed to encourage large-scale knock-on effects for private-sector investment. Specifically, capital allocations mechanisms ensure steady revenue, which is essential for sustaining long-term partnerships with businesses. Every year, these allocations provide fresh impetus for investments in R&D, innovation and the production of human capital in higher education.

As an illustration, a 2007 report by the Economic Analysis Council (CAE)[12] suggested that allocating 1.5% of GDP to French higher education will stimulate growth by 0.4% per year at the end of ten years. Using the CAE's orders of magnitude, and factoring in capital allocation schemes that encourage partnerships with the private sector, we expect the effect on growth to be an average nearly 0.1% of GDP per year over ten years – and this solely for those future-oriented investments that are connected to investments in higher education.

[12] Aghion P., G. Cette, E. Cohen and J. Pisani-Ferry, *Les leviers de la croissance française*, Report by the Economic Analysis Council, La documentation française, 2007.

5.3. Structural reforms to improve the long-term sustainability of public finances

Sustainability indicators (see Box 2) reveal a sizeable sustainability gap for 2009, of around 5.2 points of GDP[13]. This is largely attributable to the effect of the economic crisis on public finances. Indeed, the negative overshooting of tax revenues weighed heavily on the structural balance in 2009. However, this will presumably be largely compensated in a spontaneous manner in the coming years as the macroeconomic situation improves.

The structural adjustment goal of more than 4 points until 2013 should put our public finances on a virtuous debt-reduction trajectory and thus substantially improve their sustainability. By 2013, the sustainability gap is expected to shrink to no more than 1.6 points of GDP (see Box 2). It will remain positive only due to the long-term cost of the country's ageing population.

The 2010 pension reform should bring this cost down by deepening previous pension reforms and thus further improving sustainability.

Box 2: Evaluation of the S2 sustainability indicator for France

To assess the sustainability of public finances, the European Commission and the ECOFIN Council use the S2 indicator, which measures immediate and lasting improvement of public finances required to ensure that current debt is covered in the long term by future surpluses (the so-called *sustainability gap*).

The sustainability gap consists of two parts. The first reflects the initial public finance situation that, if negative, is liable to generate an explosive snowball effect. The second takes account of the expected dynamism of age-related expenditure.

In this box France's S2 indicator is evaluated using two public finance scenarios:

- In the first ("2009 scenario"), we assume that the structural balance component (excluding interest expenses, property income and age-related expenditure) is constant and will remain equal to its 2009 level until 2060. Besides, the 2009 balance has been adjusted to eliminate temporary measures linked to the economic crisis, which reduced it by more than one point of GDP, but which will have no further impact on the public balance after 2011.

  In this scenario, the sustainability gap is estimated to be 5.2 points of GDP, including 3.4 points stemming from the initial situation of public finances in 2009 and 1.8 points due to additional age-related expenditure. The scenario nevertheless tends to overestimate risks related to public finance sustainability, in that a large part of the degradation of the structural balance in 2009 was caused by a negative overshooting of tax receipts during the economic crisis, which is expected to be largely corrected in a spontaneous manner in coming years.

- In the second scenario, which is based on the assumptions of the current Stability Programme, the sustainability gap would be only 1.6 points of GDP, reflecting a generally positive contribution by the initial public finance situation (0.2 points of GDP), covering part of the age-related expenditure (1.8 points of GDP).

[13] Excluding the cost of temporary crisis-related measures.

Table 12: Calculation of the S2 public finance sustainability indicator

In points of GDP	S2	Of which impact of the initial budgetary position	Of which impact of future changes in age-related expenditure
Base year 2009 (*)	5.2	3.4	1.8
Base year 2013	1.6	-0.2	1.8

(*) Excluding temporary crisis-related measures taken in 2009.

6. Governance of public finances

6.1. The first meeting of the National Conference on the Public Deficit

On 28 January, the President of the Republic assembled the main actors concerned by public finances for the first meeting of the National Conference on the Public Deficit.

A shared diagnosis of the situation of France's public finances will be prepared by Paul Champsaur and Jean-Philippe Cotis. They will examine the evolution of public finances over the past thirty years, and in the outlook for the coming decade. The report will be made public, and will serve as the starting point for the second meeting of the Conference, scheduled for April.

President Sarkozy also announced that he wants France, over the medium term, to adopt a **balance rule for the whole general government sector**. A working group led by Michel Camdessus, a former Managing Director of the IMF, will make proposals about how this rule could be implemented.

In addition, three working groups were tasked with discussing the various ways to restore the situation of France's public finances:

- A group on **containing local expenditure** will examine ways to bring down spending by local authorities

- A group on **improving management of healthcare spending** will propose rules to ensure compliance with the annual national healthcare expenditure target set by the Parliament

- A **Social Debt Commission** will propose long-term solutions for handling the social security debt that built up during the crisis

In addition, at President Sarkozy's request, the Minister for the Budget, Public Accounts, the Civil Service and State Reform will, at the April meeting of the Conference, present **a wide-ranging action plan** for reducing State spending. Every option for doing so will be examined, particularly measures concerning tax expenditures and social contribution exemptions. The decisions will be finalised within the framework of the upcoming three-year budget.

6.2. Initial evaluation of the 2009–2011 three-year State budget

The 2009–2012 Multi-year Public Finance Planning Act of 9 February 2009, which was adopted following the constitutional revision of 23 July 2008, represented a major step forward in France's vision of its public accounts and how to consolidate them.

Although the worsening economic crisis in the first six months of 2009 called into question the public finances trajectory established in the Act, the rules established under the Act did – despite the crisis – guide budgetary policy decisions in 2009 and 2010, in particular the three-year perspective on State expenditure.

As it turns out, the State's first three-year budget remained an essential point of reference in 2009 and 2010. An initial evaluation of the budget has been drawn up:

- Despite the economic and financial crisis, the goal of limiting growth in State spending to the estimated rate of inflation (excluding recovery measures) was achieved in 2009, and confirmed in the initial 2010 Budget Act

- The initial 2010 Budget Act respects, in large part, the programme for missions established in the three-year budget

- A three-year budget for the State provides public managers with greater visibility of the resources at their disposal for carrying out reforms and implementing public policies. It also offers a means for dealing with the increasing rigidity of a budget shaped by the weight of expenditures inherited from the past.

- Finally, the three-year budget offers a coherent link between budget planning and the wide-ranging structural reforms underway in the various government departments.

As a result, the Government has decided to adopt a multiyear approach to budgeting for State expenditure, and is in the process of drawing up a new three-year budget for 2011–2013, which will be presented to Parliament in 2010.

6.3. Choosing the most effective national budgetary rules to support budget consolidation efforts

By providing effective support for introducing reforms to ensure the sustainability of public finance, budgetary rules should help achieve budget policy objectives.

In addition to public finance rules incumbent on France due to its membership in the Economic and Monetary Union, the country has introduced a certain number of national budgetary rules, some of them dating back to the mid-1990s. The current rules provide a framework for:

- The government balance and/or debt. For example, the "Golden Rule" of local authorities, and the rule concerning allocation of resources in case debt is transferred to the Social Security Debt Amortization Fund (CADES).

- Growth in spending. For example, the "zero real-term" growth rule for State expenditure (“norme zéro volume”), and the annual national healthcare expenditure target (ONDAM) set by Parliament.

- Revenue levels. For example, the tax expenditure and social contribution exemption compensation rule, part of the Multi-year Public Finance Planning Act, requires compensatory measures for any measures that negatively impact tax and social security contribution revenues. The allocation rule assigns any surplus tax revenues to debt reduction.

In order to provide active support for future budget consolidation, the President of the Republic also announced that he wants France, over the medium term, to adopt a **balance rule for the whole general government sector**. A working group led by Michel Camdessus, a former Managing Director of the IMF, will discuss the best way to calculate the cyclical share of the deficit, how to coordinate the various general government deficits within the context of such a rule, as well as its legal and governance structures.

6.4. More vigilant governance for State operators

The State acknowledges the managerial autonomy of its operators, given their activity and status. However, it has set itself the goal of providing more strategic leadership for them, by more clearly defining their missions, strategies and resources, and by more systematically overseeing the results obtained. Existing dashboard tools will be tightened up and put into widespread use. For example, assignment letters will be systematically sent to managing directors. For the seventy largest operators, there will be standardised performance contracts, which will be closely monitored.

6.5. Specific governance for future-oriented investments

Implementing future-oriented investments has been assigned to the General Commissioner for Investment, who is mandated with coordinating inter-ministerial efforts under the authority of the Prime Minister.

A specific governance structure has been set up within each organisation in charge of managing appropriations. Management agreements between each organisation and the State define how funding is to be used, as well as assessment rules and indicators for measuring results.

In addition, a Future-Oriented Investments Oversight Board will be established, which will focus on *ex post* monitoring and assessment of the various investment projects. It will consist of MPs and qualified experts. The General Commissioner for Investment will submit regular progress reports. The social partners will be included within the scope of the work. The Oversight Board will draft an annual public report.

To select projects, each organisation in charge of managing appropriations will issue calls for projects based on a set of specifications that have been validated at ministerial level. These specifications will stipulate the process and criteria for selecting projects, how financing will be applied, how funds will be used and how to monitor that use. As often as possible, outside consultants, such as economic experts (including those from outside France), will be brought in to evaluate projects in terms of their relevance, profitability and impact on potential growth.

6.6. Statistical governance

INSEE, France's national statistics institute, is responsible for methodological matters involving the compliance of French national accounting statistics practices with the European System of Accounts (ESA95). INSEE maintains regular contact with Eurostat about these matters. Within the framework of the Treaty and specific regulations, the sources and methods used to evaluate national general government accounting data have been inventoried.

The **semi-final and final accounts** are prepared in the light of detailed information, particularly for the State and the central government bodies (ODAC). For the State, the main accounting reference is the Central Government General Account (CGE) published by the Public Finances General Directorate (DGFiP). Restatement of the final outturn of budget acts as government net lending requires a series of corrections (timing differences, different treatments of certain transactions in the budgetary accounting and in the national accounting, etc.). The method used to evaluate the central government bodies' accounts is to restate the accounts of all these bodies. The consolidated account produced for the national accounts is prepared after transcription of the accounts of the individual central government bodies in the national accounting. Production of the local government accounts (S13131) is based upon the individual cash-based accounts kept by the public accounting officers. The documents used to prepare the accounts of local government bodies (S13132) are not homogeneous due to the number of different legal statuses. The accounts of the social security funds (ASSO) are based upon different accounting plans (social security scheme, general social security scheme, hospitals).

Information is less complete for the **provisional account**. For the State, the accounting year ends at the end of January in year n+1. The "public" accounts of the State are finalised towards the middle of March in year n+1, which means that the information used for notification purposes on 1 April of that year is likely to be reviewed, particularly the corrections needed to switch to accrual basis accounting. The central government bodies' accounts are partly based on projections. The accounting sources cover about 70% of revenue and expenditure. For the local governments, the accountants use information recorded in the accounting documents of the State and, since 2003, "direct" figures, which are exhaustive and centralised for the regions and *départements* and based upon a sample for the communes. This is complemented by a certain number of estimates and forecasts. Finally, for the first notification, the accounts of the social security funds are essentially based on estimates since the accounting figures of the regimes are not yet known. Nevertheless, the availability of many - still provisional - accounting figures (benefits for the UNEDIC and the general regime, sample of hospitals, etc.) makes it possible to prepare the accounts of the main organisations with some reliability.

Finally, at the Government's initiative, in July 2008 the French Parliament adopted Article 144 for the Modernisation Act, which grants legal recognition to the professional independence of public statisticians. This recognition reflects the European Statistics Code of Practice adopted by the Statistics Programme Committee on 24 February 2005 and included in the European Commission's recommendation of 25 May 2005 on the independence, integrity and accountability of national and Community statistics authorities. The Code's first principle on professional independence specifies that the independence of a statistics authority 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 Practice, whose powers embrace anyone producing public statistics.

7. Implementation of the Ecofin Council's recommendations to France

On 2 December, the Ecofin Council issued a recommendation to France with a view to bringing an end to the situation of an excessive government deficit observed in 2008 (see Box 3). **The consolidation strategy in the present Stability Programme is in line with the Council's recommendation.**

The following paragraphs detail how the recommendation is being implemented, along three major lines:

- Implementation of budgetary consolidation measures for 2010

- Implementation of a structural adjustment of more than 4 points of GDP for 2010–2013, which will bring the public deficit down to 3% by 2013

- Implementation of reforms aimed at improving the effectiveness and the governance of public finances, boosting potential growth, improving monitoring of public spending and introducing pension reform.

Box 3: Selections from the Ecofin Council's recommendations to France

Under Article 126(7) of the Treaty on the Functioning of the European Union, on 27 April 2009, the Ecofin Council addressed a recommendation to France with a view to bringing an end to the situation of an excessive government deficit observed in 2008. This recommendation was revised by the Ecofin Council on 2 December 2009.

This revised recommendation postpones the date for eliminating excessive deficit to 2013 and recommends that France:

(i) implement the deficit-reducing measures in 2010 as planned in the government proposal for the 2010 Budget Act while avoiding a further deterioration of public finances, and implement and strengthen the fiscal effort from 2011 onwards above the consolidation measures already planned

(ii) ensure an average annual fiscal effort of above 1% of GDP over the period 2010-2013

(iii) specify the measures that are necessary to achieve the correction of the excessive deficit by 2013, cyclical conditions permitting, and accelerate the reduction of the deficit if economic or budgetary conditions turn out better than currently expected

(iv) seize opportunities beyond the fiscal effort, including from better economic conditions, to accelerate the reduction of the gross debt ratio back towards the reference value

(v) continue implementing reforms with a view to enhancing the efficiency and governance of public finances and raising potential GDP growth. Increase enforceability of expenditure control, notably in the areas of healthcare and local authorities

(vi) further reform the pension system as planned which would contribute to long-term fiscal sustainability

7.1. Implementation of deficit-reducing measures in 2010

As the Council recommended, the French government is implementing all the consolidation measures planned for 2010.

Public expenditure should increase at a much lower pace in 2010 than in 2009, thanks to efforts to control spending by every general government sector. In particular, the State's compliance with the "zero real-term growth", and efforts to keep down rising healthcare costs (the national healthcare expenditure target will grow by 3.0% in 2010) are expected to contribute to reining in public expenditure in 2010.

Thus, efforts introduced in 2010 to contain public spending are in line with measures in the 2010 Budget Act, with two differences:

- Unused appropriations from the 2009 recovery plan (€1.3 billion) will be carried over into 2010; they will thus reduce public expenditure in 2009, but increase it by the same amount in 2010. This shift between the two years is neutral over the long term, since appropriations for the "Economic Recovery Plan" mission are intended to disappear at the end of 2010.
- Future-oriented investments, intended to boost the French economy's potential growth, are expected to add €2 to €2.5 billion to public expenditure in 2010 (see Box 1). For 2010, the slight impact on expenditure was obtained through €500 million in supplementary savings on the State's current expenditures. Future-oriented investments also are designed to support the return to growth in 2010, but will not jeopardise the structural adjustment programme for 2011–2013, as they will be compensated by additional deficit-reducing measures between 2011 and 2013.

In terms of revenue, the measures stipulated in the initial 2010 Budget Act will be implemented. Despite the Constitutional Council's ruling on 29 December 2009 concerning the carbon tax, the Government's plans to introduce green taxation for fighting climate change remain unchanged. A new bill will be submitted to Parliament during the course of the year.

In addition, the public deficit will be reduced by the introduction of an exceptional bank bonus tax. This scheme, which should collect some €360 million in all, was included in the Supplementary Budget Bill in January 2010. Any increases in tax revenue will be used to reduce the budget deficit, and thus the debt, as stipulated by Article 9 of the 2009–2012 Multi-year Public Finance Planning Act of 9 February 2009.

In all, the January 2010 Supplementary Budget Bill calls for a deficit of 8.2 points of GDP in 2010, against 8.5 points in the initial Budget Act, an improvement representing some €5 billion.

7.2. Implementation of deficit-reducing measures as of 2011

In addition to implementing measures already called for, as of 2011, the Government plans to increase its efforts to **bring about a structural adjustment of more than 4 points of GDP for the period 2010–2013 –** or more than 1 point of GDP annually. Given that the structural balance will remain constant in 2010, in order to allow the recovery to take fully place, this represents an average annual structural adjustment of 1.4 points of GDP between 2011 and 2013.

This adjustment will be made possible through additional efforts to control public expenditure that will involve every general government sub-sector, and that will bring average annual increases in spending down to 0.6% in real terms between 2011 and 2013.

Adopting a general government balance rule, as the President announced during the meeting of the National Conference on the Public Deficit on 28 January 2010, should help in this effort to control spending. A working group led by Michel Camdessus will examine how this rule could be implemented, and will submit its proposals in April.

President Sarkozy has also asked the Minister for the Budget, Public Accounts, the Civil Service and State Reform to present a wide-ranging action plan for reducing government spending at the next meeting of the Conference. A detailed description of how this will be implemented will be included in the upcoming three-year budget.

The second phase of the General Review of Public Policies (RGPP) was launched in the fall of 2009. In particular, it focuses on State operators, who are being asked to identify ways of keeping costs down.

The social security funds will also play a part in efforts to reduce expenditure, and increases in the national healthcare expenditure target will be capped at less than 3% per year starting in 2011.

In addition, a schedule for reforming France's pension schemes will be discussed with the social partners at the social agenda meeting on 15 February 2010.

Structural adjustment will also be made possible by a policy of reducing tax expenditures and social contribution exemptions by some €2 billion per year starting in 2011, or a total of €6 billion by 2013 (out of a total of €70 billion in annual revenue losses in tax expenditures alone).

Finally, two additional elements will spontaneously contribute to reducing the deficit:

- The complete phasing-out in 2011 of recovery measures and the disappearance of the 2010 temporary cost of reforming the local business tax;
- After their negative overshooting during the crisis, tax and social security contributions should spontaneously outpace GDP between 2011 and 2013 (elasticity of 1.2). As in 2010, any increases in tax revenue will be used to reduce the budget deficit.

Taken together, these measures should bring France's deficit down to 3% of GDP by 2013, in line with the recommendation of the Ecofin Council on 2 December 2009.

7.3. Reforms to improve the effectiveness and governance of public finances, and to raise potential growth

A. Effectiveness and governance of public finances, controlling public spending

With respect to local public finances, **the project for reforming regional and local authorities, currently being debated in Parliament, is expected to extend efforts to streamline expenditure**. A strengthened, simplified approach to intercommunal relations, and improvements to how local governments share authority – which will be the subject of a new legislation in 2010 – will result in better pooling of public expenditure.

Effort to streamline local spending will be deepened in the context of a working group, which was set up during the National Conference on the Public Deficit. The group, co-chaired by Gilles Carrez and Pierre-René Lemas, will examine various ways to keep local spending down, and how a local spending target might be set. It will report on its findings in April 2010.

Moreover, the second phase of the General Review of Public Policies (RGPP) focuses on introducing new governance rules for State operators, which are being asked to implement rules governing human resources, performance-based pay, sharing of support functions, real estate policy and transparency of accounts. These rules are already in force at central government level. The RGPP is also focused on **improving service quality and relations with users**. Greater emphasis will be placed on remote "one-stop shops", and case treatment times will be reduced.

In the area of healthcare, recent efforts to control spending will be stepped up. An ambitious national healthcare expenditure target (ONDAM) will keep spending growth to 3.0% in 2010, and below 3.0 % as of 2011 (instead of the 3.3% called for in the 2009 Multi-year Public Finance Planning Act). To this end, implementation of the Hospitals, Patients, Healthcare and Territorial Organisation Act should considerably improve the effectiveness of the hospital sector. The creation of Regional Healthcare Agencies (*Agences Régionales de Santé* – ARS) will introduce unified management of France's regional healthcare system. This will create better synergies between private practitioners, hospitals and medico-social institutions, and will help streamline the healthcare system. A working group headed up by Raoul Briet aims at ensuring the credibility of this approach and report on its conclusions in April 2010.

B. Boosting potential growth

With the future-oriented investments (See Section 5.2), the French Government is investing in order to improve the economy's potential growth.

In terms of governance, France has entrusted the execution of its future-oriented investments to a General Commissioner, whose services will be responsible for evaluating – both *ex ante* and *ex post* – the profitability of these public investments. More generally, the Commissioner will have the authority to ensure the consistency of the full range of investments made by the public authorities each year.

Finally, as per the Council recommendations, a monitoring committee for investments financed by the National Loan has been set up. This oversight will also contribute to making public expenditure as a whole more efficient, and to making project assessment more a part of government culture.

C. Sustainability and pension reform

France is aware of the long-term implications of an ageing population (See Section 6).

This is why, discussions concerning France's pension system, originally scheduled for 2012, **have been moved up to 2010**. The goal is to ensure the long-term viability of the country's contributory scheme, which has been weakened by an ageing population and the recent economic crisis. This reform will concern both public- and private-sector pensions, and no area will be excluded from consideration. A timeline for this reform will be discussed with the social partners starting on 15 February 2010. Major decisions will be adopted and voted on before the end of 2010.

Annex 1: Statistics tables

Table 1a. Macroeconomic forecasts

	ESA code	2008	2008	2009	2010	2011	2012	2013
		Level	Rate of change	Rate of change	Rate of change	Rate of change	Rate of change	Rate of change
1. Real GDP	B1*g	-	0.4	-2.25	1.4	2.5	2.5	2.5
2. Nominal GDP	B1*g	1,950.1	2.9	-1.3	2.5	4.0	4.3	4.3
Components of GDP								
3. Private consumption expenditure	P.3	1,114.1	1.0	0.7	1.4	2.5	2.9	3.0
4. Government consumption expenditure	P.3	451.6	1.2	2.0	1.4	-0.4	-0.3	-0.3
5. Gross fixed capital formation	P.51	427.2	0.6	-5.8	-1.3	4.5	3.2	3.2
6. Change in inventories and net acquisition of valuables (% of GDP)	P.52 + P.53	-	0.3	-1.5	-1.2	-0.9	-0.7	-0.6
7. Export of goods and services	P.6	515.6	-0.2	-11.1	3.7	4.8	6.5	6.5
8. Imports of goods and services	P.7	563.8	0.8	-9.9	3.6	5.0	6.1	6.1
Contributions to GDP growth								
9. Final domestic demand excluding inventories		-	1.0	-0.4	0.9	2.3	2.3	2.3
10. Change in inventories and net acquisition of valuables	P.52 + P.53	-	-0.3	-1.7	0.5	0.3	0.2	0.1
11. External balance of goods and services	B.11	-	-0.3	-0.1	0.0	-0.1	0.0	0.0

Table 1b. Price trend

	ESA code	2008	2008	2009	2010	2011	2012	2013
		Level	Rate of change	Rate of change	Rate of change	Rate of change	Rate of change	Rate of change
1. GDP deflator		-	2.5	1.0	1.1	1.5	1.75	1.75
2. Private consumption deflator		-	2.8	-0.2	1.3	1.5	1.75	1.75
3. Harmonised index of consumer prices (HIPC)		-	3.2	0.1	1.3	1.6	1.75	1.75
4. Public consumption deflator		-	2.1	1.8	1.2	1.5	1.75	1.75
5. Investment deflator		-	3.9	0.0	1.3	1.3	1.75	1.75
6. Export price deflator (goods and services)		-	2.9	-3.4	1.9	1.6	1.1	1.1
7. Import price deflator (goods and services)		-	4.0	-6.6	2.4	1.1	1.1	1.1

Table 1c. Labour market

	ESA code	2008	2008	2009	2010	2011	2012	2013
		Level	Rate of change	Rate of change	Rate of change	Rate of change	Rate of change	Rate of change
1. Employment, persons[1]		25,841	0.5	-1.2	-0.7	0.5	0.7	0.7
2. Employment, hours worked[2]		:	:	:	:	:	:	:
3. Unemployment rate (%)[3]		:	:	:	:	:	:	:
4. Labour productivity, persons[4]		-	0.2	-0.5	1.8	1.9	1.8	1.8
5. Labour productivity, hours worked[5]		:	:	:	:	:	:	:
6. Compensation of employees	D.1	1,015.8	3.2	0.1	1.0	3.5	4.0	4.0

[1] Economically active population in the meaning of the National Accounts (in thousands)

[2] National accounts definition

[3] ILO definition

[4] Real GDP per person employed

[5] Real GDP per hour worked

Table 1d. Sector balance

as a % of GDP	ESA code	2008	2009	2010	2011	2012	2013
1. Net lending/borrowing vis-à-vis the rest of the world	B.9	-3.3	-2.5	-2.8	-2.8	-2.7	-2.7
o.w.: - Balance of goods and services		-2.5	-1.7	-1.8	-1.8	-1.8	-1.7
- Balance of primary incomes and current transfers		-0.8	-0.8	-1.0	-1.0	-1.0	-0.9
- Capital account		0.0	0.0	0.0	0.0	0.0	0.0
2. Net lending/borrowing of the private sector	B.9	:	:	:	:	:	:
3. Net lending/borrowing of the public sector	EDP B.9	-3.4	-7.9	-8.2	-6.0	-4.6	-3.0
4. Statistical discrepancy		:	:	:	:	:	:

Table 2. General government budgetary prospects

unit: € bn	ESA code	2008	2008	2009	2010	2011	2012	2013
		Level	as a % of GDP	as a % of GDP	as a % of GDP	as a % of GDP	as a % of GDP	as a % of GDP
Net lending (B9) per sub-sector								
1. General government	S.13	-65.9	-3.4	-7.9	-8.2	-6.0	-4.6	-3.0
2. Central government	S.1311	-56.4	-2.9	-6.2	-5.9	-3.9	-3.0	-2.0
3. State government	S.1312							
4. Local governments	S.1313	-8.6	-0.4	-0.4	-0.5	-0.4	-0.2	-0.1
5. Social security funds	S.1314	-0.9	0.0	-1.3	-1.9	-1.7	-1.3	-1.0
General government (S.13)								
6. Total revenue	TR	960,8	49,3	47,7	47,6	48,6	49,1	49,8
7. Total expenditure	TE[1]	1026,7	52,7	55,6	55,8	54,6	53,7	52,8
8. Net lending/borrowing	EDP B.9	-65,9	-3,4	-7,9	-8,2	-6,0	-4,6	-3,0
9. Interest expenditure	EDP D.41	54,3	2,8	2,5	2,6	2,8	2,9	3,0
10. Primary balance[2]		-11,7	-0,6	-5,4	-5,5	-3,2	-1,7	-0,1
Key components of revenue								
11. Taxes on production and imports	D.2	287.9	14.8	14.7	14.2	14.6	14.7	14.9
12. Taxes on income and wealth	D.5	223.1	11.4	9.7	10.4	10.9	11.2	11.5
13. Capital taxes	D.91	7.9	0.4	0.4	0.4	0.4	0.5	0.5
14. Social security contributions	D.61	349.5	17.9	18.2	17.9	17.9	18.0	18.0
15. Property income	D.4	17.2	0.9	0.8	0.8	0.8	0.8	0.8
16. Other revenue (16=17-11-12-13-14-15)		75.2	3.9	3.9	3.9	4.0	4.1	4.1
17=6. Total revenue	TR	960.8	49.3	47.7	47.6	48.6	49.1	49.8
p.m.: Tax burden (D.2+D.5+D.61-D612+D.91-D.995) [3]		834.3	42.8	41.0	41.0	41.9	42.4	43.0
Key components of expenditure								
18. Compensation of employees and intermediate consumption	D.1+P.2	345.1	17.7	18.5	18.5	18.0	17.6	17.1
19. Social transfers in kind	D.6311. D.63121. D.63131	111.3	5.7	6.1	6.1	6.0	5.9	5.9
20. Social transfers in cash	D.62	342.1	17.5	18.9	19.2	18.9	18.6	18.4
21=9. Interest expenditure	EDP D.41	54.3	2.8	2.5	2.6	2.8	2.9	3.0
22. Subsidies	D.3	27.3	1.4	1.5	1.4	1.3	1.3	1.3
23. Gross fixed capital formation	P.51	62.4	3.2	3.4	3.4	3.2	3.2	3.1
24. Other expenditure (=25-18-19-20-21-22-23)		84.3	4.3	4.8	4.6	4.3	4.2	4.1
25=7. Total expenditure	TE1	1026.7	52.7	55.6	55.8	54.6	53.7	52.8
p.m.: Compensation of employees	D.1	247.7	12.7	13.2	13.1	12.9	12.6	12.3

[1]Adjusted for the net interest flows connected with swaps, 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]Including taxes collected by the European Union and adjustment for uncollected taxes and social security contributions (D.995) if appropriate.

Table 3. Government expenditure by function

% of GDP	COFOG code	**2008**	**2013**
1. General public services	1	7.1	:
2. Defence	2	1.8	:
3. Public order and safety	3	1.2	:
4. Economic affairs	4	2.8	:
5. Environmental protection	5	0.9	:
6. Housing and community amenities	6	1.9	:
7. Health	7	7.8	:
8. Recreation, culture and religion	8	1.5	:
9. Education	9	5.8	:
10. Social protection	10	21.8	:
11. Total expenditure (= line 7 of Table 2)	TE[1]	**52.7**	**52.8**

[1] Adjusted for the net interest flows connected with swaps, so that TR-TE=EDP B.9.

Table 4. Change in public debt

as a % of GDP	ESA code	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**
1. Gross debt[1]		67.4	77.4	83.2	86.1	87.1	86.6
2. Change in gross debt ratio		3.6	10.1	5.8	2.8	1.0	-0.5
Contributions to changes in gross debt							
3. Primary balance[2]		-0.6	-5.4	-5.5	-3.2	-1.7	-0.1
4. Interest expenditure[3]	EDP D.41	2.8	2.5	2.6	2.8	2.9	3.0
5. Stock-flow adjustment		2.0	1.3	-0.5	0.0	0.0	0.0
o.w.: - Differences between cash and accruals		0.2	:	:	:	:	:
- Net accumulation of financial assets		1.8	:	:	:	:	:
o.w.: *- privatisation proceeds*		0.0	:	:	:	:	:
- Valuation effects and other		0.0	:	:	:	:	:
p.m.: Implicit interest rate on the debt[4]		4.5	3.6	3.5	3.5	3.5	3.5
Other relevant variables							
6. Liquid financial assets[5]		22.2	:	:	:	:	:
7. Net financial debt (7=1-6)		45.2	:	:	:	:	:

[1]As defined in Regulation 3605/93; the concept is not part of the European System of Accounts (ESA).

[2]See item 10 in table 2.

[3]See item 9 in table 2.

[4] Interest expense divided by debt outstanding the previous year.

[5]AF1, AF2, AF3 (consolidated at market value), AF5 (excluding non quoted shares).

Table 5. Cyclical changes and cyclically-adjusted data

as a % of GDP	ESA code	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**
1. Real GDP growth (%)		0.4	-2.25	1.4	2.5	2.5	2.5
2. Public balance	EDP B.9	-3.4	-7.9	-8.2	-6.0	-4.6	-3.0
3. Interest expenditure	EDP D.41	2.8	2.5	2.6	2.8	2.9	3.0
4. One-off measures[1]		0.0	0.0	0.0	0.0	0.0	0.0
5. Potential GDP growth (%)		2.0	1.7	1.5	1.7	1.9	1.9
contributions:							
- labour		0.2	0.0	0.0	0.0	0.2	0.2
- capital		0.9	0.7	0.6	0.7	0.7	0.7
- total productivity of production factors		1.0	1.0	1.0	1.0	1.0	1.0
6. Output gap		-0.8	-4.6	-4.7	-4.0	-3.4	-2.9
7. Cyclical balance		-0.2	-2.1	-2.4	-2.0	-1.7	-1.4
8. Cyclically-adjusted public balance (2 - 7)		-3.1	-5.8	-5.8	-4.0	-2.9	-1.6
9. Cyclically-adjusted primary balance (8 + 3)		-0.4	-3.3	-3.1	-1.2	0.0	1.3
10. Structural balance (8 - 4)		-3.1	-5.8	-5.8	-4.0	-2.9	-1.6

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

Table 6. Divergence from previous programme update

	ESA code	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**
GDP growth (%)							
previous update		1.0	0.2 / 0.5	2.0	2.5	2.5	
current update		0.4	-2.25	1.4	2.5	2.5	2.5
Difference		-0.6	-2.75 / -2.45	-0.6	0.0	0.0	
General government net lending (as a % of GDP)	EDP B.9						
previous update		-2.9	-3.9	-2.7	-1.9	-1.1	
current update		-3.4	-7.9	-8.2	-6.0	-4.6	-3.0
Difference		-0.5	-4.0	-5.5	-4.1	-3.5	
Public debt (as a % of GDP)							
previous update		66.7	69.1	69.4	68.5	66.8	
current update		67.4	77.4	83.2	86.1	87.1	86.6
Difference		0.7	8.3	13.8	17.6	20.3	

Table 7. Long-term sustainability of public finances (source: EPC, 2009 Ageing Report)

as a % of GDP	**2007**	**2010**	**2020**	**2030**	**2040**	**2050**	**2060**
Total expenditure	:	:	:	:	:	:	:
o.w.: age-related expenditure	28.4	29.0	29.4	30.5	31.3	31.3	31.2
Pension expenditure	13.0	13.5	13.6	14.2	14.4	14.2	14.0
o.w.: General regimes	:	:	:	:	:	:	:
Old-age and early pensions	:	:	:	:	:	:	:
Other pensions (survivors, disability)	:	:	:	:	:	:	:
o.w.: Employer's regimes (if in the general government)	:	:	:	:	:	:	:
Healthcare expenditure	8.1	8.2	8.6	8.9	9.2	9.3	9.4
Long-term care expenditure	1.4	1.5	1.6	1.8	2.0	2.2	2.2
Education expenditure	4.7	4.6	4.6	4.7	4.6	4.7	4.6
Other age-related expenditure (unemployment)	1.2	1.2	0.9	0.9	0.9	0.9	0.9
Interest expense	:	:	:	:	:	:	:
Public revenue	:	:	:	:	:	:	:
o.w.: property income	:	:	:	:	:	:	:
o.w.: pension contributions (or social security contributions if appropriate)	:	:	:	:	:	:	:
Financial assets of supplementary pension schemes and FRR (*)	:	:	:	:	:	:	:
o.w.: consolidated financial assets of supplementary pension schemes and the FRR	:	:	:	:	:	:	:
Assumptions							
Labour productivity growth rate	:	:	:	:	:	:	:
Real GDP growth rate	:	:	:	:	:	:	:
Participation rate of man (aged 20-64)	:	:	:	:	:	:	:
Participation rate of women (aged 20-64)	:	:	:	:	:	:	:
Participation rate (age 20-64)	:	:	:	:	:	:	:
Unemployment rate	:	:	:	:	:	:	:
Population aged 65 and over in the total population	:	:	:	:	:	:	:

(*) in 2008, the non-consolidated (resp. consolidated) financial assets of the supplementary pension schemes (Agirc, Arrco, CNAVPL, ERAFP, Ircantec and RSI) and the FRR came to 9.0 points of GDP (resp. 8.2 points of GDP)

Table 8. Basic assumptions

	2008	2009	2010	2011	2012	2013
Short-term interest rates (annual average)[1]	:	:	:	:	:	:
Long-term interest rates (annual average)	:	:	:	:	:	:
USD/€ exchange rate €/$ (annual average)	1.47	1.40	1.48	1.48	1.48	1.48
Nominal effective exchange rate (basis 100 in 1995)	113.5	114.0	115.7	115.7	115.7	115.7
World excluding EU, GDP growth	3.2	-0.1	4.0	4.3	4.0	4.0
EU GDP growth	0.7	-3.5	1.2	1.5	2.4	2.4
World demand addressed to France	1.6	-13.0	5.5	6.2	6.6	6.6
World trade excluding the EU	2.8	-12.9	9.5	7.6	7.7	7.7
Oil prices (Brent/bbl in USD)	97	62	77	77	78	79

[1]If necessary. Purely technical assumptions

Annex 2: The public finances trajectory under a different growth scenario

In addition to the central growth scenario described in the present Stability Programme, this annex provides a second scenario and an accompanying public finances trajectory. Under this alternative scenario, growth in activity for 2009 and 2010 remains the same as in the original scenario, but is less dynamic starting in 2011 (2¼ % per year instead of 2½ %). In comparison with the central scenario, household savings rate would go down more slowly and investment by businesses would be held back by a stronger debt-reduction effort.

The assumption that tax and social security contributions would automatically catch up after their negative overshooting during the crisis is adjusted consequently.

Efforts to reduce expenditure and new measures in terms of tax and social security contributions would remain identical to the central scenario.

Under this alternative scenario, the public deficit would come down to 4% of GDP by 2013, and then to 3% in 2014. Trends in public spending would be identical to the central scenario, with the exception of unemployment benefits, which would decrease less quickly. On the other hand, growth in tax and social security contributions would be slower, and their aggregate rate would remain under their pre-crisis levels even in 2014 (around 42½ %).

Higher deficits and a weaker denominator would mean a higher debt ratio than in the central scenario form 2011 on. It would reach a high point of 89.0 points of GDP in 2013, and then begin to decline the following year.

Table 13: Simulated illustrative multiyear public finances trajectory

	2008	**2009**	**2010**	**2011**	**2012**	**2013**	**2014**
Public balance (% GDP)	-3.4	-7.9	-8.2	-6.3	-5.2	-4.0	-3.0
Public debt (% GDP)	67.4	77.4	83.2	86.6	88.4	89.0	88.6
Structural balance (% potential GDP)	-3.1	-5.8	-5.8	-4.2	-3.2	-2.2	-1.4
Change in structural balance (% potential GDP)	0.0	-2.6	0.0	1.6	1.0	1.0	0.9