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FRANCE: MACRO FISCAL ASSESSMENT

AN ANALYSIS OF THE FEBRUARY 2010 UPDATE OF THE STABILITY PROGRAMME

The Stability and Growth Pact requires each EU Member State to present an annual update of its medium-term fiscal programme, called 'stability programme' for countries that have adopted the euro as their currency and 'convergence programme' for those that have not. The most recent update of France's stability programme was submitted on 1 February 2009.

The attached technical analysis of the programme prepared by the staff and under the responsibility of the Directorate-General for Economic and Financial Affairs (DG ECFIN) of the European Commission, was finalised on 17 March 2010. Comments should be sent to Pierre Ecochard, Samuel de Lemos Peixoto and Fabrizio Melcarne (pierre.ecochard@ec.europa.eu, samuel.de-lemos-peixoto@ec.europa.eu and fabrizio.melcarne@ec.europa.eu). The main aim of the analysis is to assess the realism of the budgetary strategy presented in the programme as well as its compliance with the requirements of the Stability and Growth Pact. However, the analysis also looks at the overall macro-economic performance of the country and highlights relevant policy challenges.

The analysis takes into account (i) the Commission services' autumn 2009 forecast, (ii) the code of conduct ("Specifications on the implementation of the Stability and Growth Pact and guidelines on the format and content of stability and convergence programmes", endorsed by the ECOFIN Council of 10 November 2009) and (iii) the commonly agreed methodology for the estimation of potential output and cyclically-adjusted balances.

Based on this analysis, the European Commission adopted a recommendation for a Council opinion on the programme on 17 March 2010. The ECOFIN Council is expected to discuss the opinion on the programme on 16 April 2010.

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All these documents, as well as the provisions of the Stability and Growth Pact, can be found on the following website:

http://ec.europa.eu/economy_finance/sgp/index_en.htm

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1. INTRODUCTION

This document assesses the February 2010 update of the France's stability programme, which was submitted on 1 February 2010 and covers the period 2009-2013.

This assessment is structured as follows. Section 2 discusses the key challenges for public finances in France. Section 3 assesses the plausibility of the macroeconomic scenario underpinning the public finance projections of the stability programme against the background of the Commission services' economic forecasts[1]. Section 4 analyses budgetary implementation in the year 2009, the budgetary plans for 2010, and the medium-term budgetary strategy. It also assesses risks attached to the budgetary targets. Section 5 reviews recent debt developments and medium-term prospects, as well as the long-term sustainability of public finances. Section 6 discusses institutional features of public finances. Finally, Section 7 concludes with an overall assessment of the programme. The annex provides a detailed assessment of compliance with the code of conduct, including an overview of the summary tables from the programme.

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[1] This assessment uses the Commission services' 2009 autumn forecast, as published on 3 November 2009, as a benchmark. However, more recent information that has become available has also been taken into account to assess the risks to the programme scenarios.

Table 1. Comparison of key macroeconomic and budgetary projections

		2008	2009	2010	2011	2012	2013
Real GDP (% change)	**SP Feb 2010**	**0.4**	**-2.25**	**1.4**	**2.5**	**2.5**	**2.5**
	COM Nov 2009	0.4	-2.2	1.2	1.5	n.a.	n.a.
	SP Dec 2008	*1.0*	*0.2-0.5*	*2.0*	*2.5*	*2.5*	*n.a.*
HICP inflation (%)	**SP Feb 2010**	**3.2**	**0.1**	**1.3**	**1.6**	**1.75**	**1.75**
	COM Nov 2009	3.2	0.1	1.1	1.4	n.a.	n.a.
	SP Dec 2008	*3.3*	*1.5*	*1¾*	*1¾*	*1¾*	*n.a.*
Output gap[1] (% of potential GDP)	**SP Feb 2010**	**0.8**	**-2.9**	**-2.9**	**-2.1**	**-1.2**	**-0.4**
	COM Nov 2009[2]	0.8	-2.5	-2.5	-2.4	n.a.	n.a.
	SP Dec 2008	*-0.6*	*-1.8*	*-1.6*	*-1.1*	*-0.4*	*n.a.*
Net lending/borrowing vis-à-vis the rest of the world (% of GDP)	**SP Feb 2010**	**-3.3**	**-2.5**	**-2.8**	**-2.8**	**-2.7**	**-2.7**
	COM Nov 2009	-3.3	-2.3	-2.3	-2.3	n.a.	n.a.
	SP Dec 2008	*-3.4*	*-2.6*	*-2.5*	*-2.4*	*-2.4*	*n.a.*
General government revenue (% of GDP)	**SP Feb 2010**	**49.3**	**47.7**	**47.6**	**48.6**	**49.1**	**49.8**
	COM Nov 2009	49.3	47.0	46.8	47.1	n.a.	n.a.
	SP Dec 2008	*49.8*	*49.6*	*50.0*	*50.0*	*50.2*	*n.a.*
General government expenditure (% of GDP)	**SP Feb 2010**	**52.7**	**55.6**	**55.8**	**54.6**	**53.7**	**52.8**
	COM Nov 2009	52.7	55.2	55.1	54.8	n.a.	n.a.
	SP Dec 2008	*52.7*	*53.5*	*52.7*	*52.0*	*51.3*	*n.a.*
General government balance (% of GDP)	**SP Feb 2010**	**-3.4**	**-7.9**	**-8.2**	**-6.0**	**-4.6**	**-3.0**
	COM Nov 2009	-3.4	-8.3	-8.2	-7.7	n.a.	n.a.
	SP Dec 2008	*-2.9*	*-3.9*	*-2.7*	*-1.9*	*-1.1*	*n.a.*
Primary balance (% of GDP)	**SP Feb 2010**	**-0.6**	**-5.4**	**-5.5**	**-3.2**	**-1.7**	**-0.1**
	COM Nov 2009	-0.6	-5.5	-5.4	-4.7	n.a.	n.a.
	SP Dec 2008	*0.0*	*-1.1*	*0.1*	*0.9*	*1.7*	*n.a.*
Cyclically-adjusted balance[1] (% of GDP)	**SP Feb 2010**	**-3.8**	**-6.5**	**-6.8**	**-4.9**	**-4.0**	**-2.8**
	COM Nov 2009	-3.8	-7.0	-7.0	-6.5	n.a.	n.a.
	SP Dec 2008	*-2.6*	*-3.0*	*-1.9*	*-1.4*	*-0.9*	*n.a.*
Structural balance[3] (% of GDP)	**SP Feb 2010**	**-3.8**	**-6.5**	**-6.8**	**-4.9**	**-4.0**	**-2.8**
	COM Nov 2009	-3.9	-7.0	-6.6	-6.5	n.a.	n.a.
	SP Dec 2008	*-2.6*	*-3*	*-1.9*	*-1.4*	*-0.9*	*n.a.*
Government gross debt (% of GDP)	**SP Feb 2010**	**67.4**	**77.4**	**83.2**	**86.1**	**87.1**	**86.6**
	COM Nov 2009	67.4	76.1	82.5	87.6	n.a.	n.a.
	SP Dec 2008	*66.7*	*69.1*	*69.4*	*68.5*	*66.8*	*n.a.*

Notes:

[1]Output gaps and cyclically-adjusted balances from the programmes as recalculated by Commission services on the basis of the information in the programmes.

[2]Based on estimated potential growth of 1.5%, 1.2%, 1.2% and 1.4% respectively in the period 2008-2011.

[3]Cyclically-adjusted balance excluding one-off and other temporary measures. One-off and other temporary measures are 0 all over the period covered (2008-2013) according to the most recent programme and 0.1% of GDP in 2008 deficit-reducing and 0.4% of GDP in 2010 deficit-increasing according to the Commission services' November 2009 forecast.

Source :

Stability programme (SP); Commission services' autumn 2009 forecasts (COM); Commission services' calculations.

2. KEY CHALLENGES IN THE ECONOMIC DOWNTURN AND THE POLICY RESPONSE

This section describes recent economic and budgetary developments for France, which form the background against which the current programme assessment should be viewed, and outlines the key challenges to be addressed by future economic policies.

The global financial crisis dragged France into a deep recession. GDP, which had been growing relatively robustly for several years, lost its dynamism in the course of 2008 and declined sharply in the fourth quarter and in the first quarter of 2009 (falling by 1.5% and 1.4%). From the second quarter of 2009, it picked up again, supported by stimulus measures in France and in neighbouring countries. Although the French banking system has been resilient, mainly due to the predominance of retail banking and relatively sound balance sheets in the corporate sector and the financial sector, the crisis has entailed a tightening of liquidity and lending conditions. Moreover, the free fall in world trade has taken its toll on the French economy. All in all, however, the recession has been less steep than in many neighbouring countries and the euro area as a whole, due mainly to the resilience of private consumption, the relatively small degree of openness of the economy and the limited size of the manufacturing sector. Fiscal policy has aimed at containing the economic downturn and has added to the sizeable impact of automatic stabilisers. Specifically, a recovery plan with a budgetary impact of 1.1% of GDP in 2009 and 0.35% of GDP in 2010 has been implemented, consisting mainly of public investment and support to firms. Furthermore, cuts in VAT in the catering sector and in the local business tax have been adopted. In addition, the French authorities have announced an investment programme financed through a public loan ("*Emprunt national*") and aimed at stimulating potential growth by "investing in the future".

The starting position of public finances before the crisis was not good in spite of robust growth in the previous years. Since 2002 the deficit in France has been high and either above or close to the 3% threshold which was essentially a reflection of the insufficient consolidation efforts. Already in April 2003, an excessive deficit procedure had been initiated by the Commission[2]. After it was abrogated in January 2007 by the Council, nominal and structural balances deteriorated again in 2007. In the light of the expected further deterioration of the nominal and structural deficits in 2008, the Commission issued in May 2008 a policy advice highlighting the risks that the 3% threshold could be breached and recommending France, among other things, to carry out the necessary consolidation of public finances in order to support the reform process. Following the notification of a deficit above the 3% threshold in 2008, a new excessive deficit procedure was opened in February 2009, in the framework of which the origin of this excessive deficit was not considered to be the global crisis, contrary to the increased excess in 2009. Whereas the Council recommended to France in April 2009 to bring an end to the excessive deficit by 2012, it issued revised recommendations in December 2009, in view of the economic downturn and the significant budgetary consequences, essentially postponing the deadline by one year[3]. Complying with these recommendations and correcting the excessive deficit will be a challenge for the economic policy in the coming years. France will also have to further reform its pension system with a view to cushion the impact on public finances of increasing age-related costs, thereby improving the long-terms sustainability of public finances. Another challenge for the French economy is related to competitiveness: net trade has hampered French growth significantly over the last years. This is not due to a single factor but rather to a series of weaknesses on the supply side. The combination of a sustained domestic demand, translating into relatively dynamic imports, and declining market shares, could lead to increasing external imbalances and, therefore, a sluggish recovery. This could be avoided through reforms aiming at alleviating supply-side weaknesses. A third key challenge to be addressed by public policies is the historically insufficient utilisation of labour, which is widely seen as one of the main weaknesses of the French economy. Poor labour market functioning in France manifests itself in a rather low participation rate at both ends of the age spectrum (young and older workers), a high unemployment rate, and a low number of average hours worked. Addressing this

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[2] All the necessary documents can be found at: http://ec.europa.eu/economy_finance/sg_pact_fiscal_policy/excessive_deficit9109_en.htm

[3] See Box 1 in section 4.1 for more information on the excessive deficit procedure.

situation would help the economy to enter a virtuous circle by stimulating economic activity and alleviating the burden on public accounts.

3. MACROECONOMIC OUTLOOK

Against the background of the current macroeconomic situation and the main policy challenges set out in the previous section, this section makes an assessment of the plausibility of the macroeconomic scenario underpinning the public finance projections of the programme.

The programme forecasts GDP to resume growing in 2010 by 1.4%, after a contraction of 2¼% in 2009. In this scenario, activity is driven by domestic demand (contribution of 0.9 pp.) and especially private consumption, while changes in inventories contribute to a lesser extent (0.5 pp.). From 2011 onwards, growth is projected to increase to 2.5% per year on average, mainly as a consequence of strong domestic demand, which is projected to contribute 2.3 pp. of GDP each year. Throughout the programme period, imports growth stemming from a strong domestic demand would be compensated by high exports growth in a favourable international environment[4], leading to a contribution of net trade to GDP growth equal to zero. As recalculated by the Commission services' based on the information in the programme following the commonly agreed methodology[5], the output gap is projected by the programme to close gradually, from -2.9% in 2009 to -0.4% in 2013. GDP growth is forecast to be around potential in 2010 and 0.8 pp. above potential on average from 2011 to 2013.

The Commission services' autumn GDP growth forecast for 2010 (identical to the February 2010 Interim forecast) is relatively close to that of the programme: 1.2% against 1.4%. It should be mentioned however that there are differences in the composition of growth between the two projections: in the Commission services' forecast, change in inventories rather than private consumption is the main growth engine. Differences are much wider as far as 2011 is concerned: the Commission services' forecast projects growth at 1.5%, against 2.5% in the programme. This is due to a much smaller contribution of domestic demand (1.2 pp. against 2.3). For 2012-2013, the growth assumptions of the programme are significantly higher than the Commission services' estimate of potential GDP growth for 2009-2011 (2.5% against 1.3%). Throughout the programme period, domestic demand appears to be on the high side. Indeed, the backlash of the phasing out of the car scrapping premium and the high unemployment rate are set to weigh on private consumption, while public investment will suffer from the phasing out of the recovery package. Additionally, the uncertain demand outlook and the underutilisation of production capacities, combined with widespread declines in profits and the need for firms to strengthen their balance sheets, do not bode well for productive investment. The consolidation of public finances foreseen by the programme itself (1.4 pp. of GDP per year on average after 2011) will also limit the dynamism of domestic demand, which might not be fully reflected in the macroeconomic scenario of the programme. All in all, when assessed against the Commission services' autumn 2009 forecast, but also taking into account more recent information, the growth assumptions of the programme can be considered as slightly favourable for 2010, and markedly favourable for 2011-2013.

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[4] The external outlook of the programme is more optimistic than the external outlook in the Commission services' autumn 2009 forecast, especially as regards extra-EU trade.

[5] The reported potential growth figures are different from those recalculated by the Commission for 2012 (1.9% against 1.6%) and 2013 (1.9% against 1.7%).

The programme projections reflect the traditional lag between activity and employment: employment is forecasted to shrink by 0.7% in 2010 (0.9% in the Commission services' forecast), before recovering, growing by 0.5% in 2011 (0.4% in the Commission services' forecast) and 0.7% in 2012 and 2013. The employment projection for 2009 (-1.2%) is significantly different from that of the Commission services' forecast (-1.8%), which is fully explained by the developments on the labour market since the publication of the Commission services' forecast. Compensation of employee per head is on the high side, which is coherent with the programme's optimistic outlook for consumption from 2011, at 3% in 2011 (against 1.5% in the Commission services' forecast), and 3.3% thereafter. The programme's projections for HICP inflation are close to those of the Commission services' forecast (1.3% against 1.1% in 2010; 1.6% against 1.4% in 2011; 1.75% in the outer years). They appear plausible in light of the latest developments in commodities prices and exchange rates.

Table 2: Comparison of macroeconomic developments and forecasts

	2009		2010		2011		2012	2013
	COM	SP	COM	SP	COM	SP	SP	SP
Real GDP (% change)	-2.2	-2.25	1.2	1.4	1.5	2.5	2.5	2.5
Private consumption (% change)	0.8	0.7	0.8	1.4	0.8	2.5	2.9	3.0
Gross fixed capital formation (% change)	-6.2	-5.8	-1.6	-1.3	2.2	4.5	3.2	3.2
Exports of goods and services (% change)	-10.9	-11.1	2.8	3.7	3.4	4.8	6.5	6.5
Imports of goods and services (% change)	-9.5	-9.9	2.2	3.6	3.7	5.0	6.1	6.1
Contributions to real GDP growth:								
- Final domestic demand	-0.6	-0.4	0.4	0.9	1.2	2.3	2.3	2.3
- Change in inventories	-1.4	-1.7	0.8	0.5	0.4	0.3	0.2	0.1
- Net exports	-0.1	-0.1	0.1	0.0	-0.1	-0.1	0.0	0.0
Output gap[1]	-2.5	-2.9	-2.5	-2.9	-2.4	-2.1	-1.2	-0.4
Employment (% change)	-1.8	-1.2	-0.9	-0.7	0.4	0.5	0.7	0.7
Unemployment rate (%)	9.5	n.a.	10.2	n.a.	10.0	n.a.	n.a.	n.a.
Labour productivity (% change)	-0.4	-0.5	2.1	1.8	1.1	1.9	1.8	1.8
HICP inflation (%)	0.1	0.1	1.1	1.3	1.4	1.6	1.75	1.75
GDP deflator (% change)	1.9	1.0	1.2	1.1	1.7	1.5	1.75	1.75
Comp. of employees (per head, % change)	1.2	n.a.	1.5	n.a.	1.5	n.a.	n.a.	n.a.
Net lending/borrowing vis-à-vis the rest of the world (% of GDP)	-2.3	-2.5	-2.3	-2.8	-2.3	-2.8	-2.7	-2.7

Note:

[1]In percent of potential GDP, with potential GDP growth according to the programme as recalculated by Commission services.

Source:

Commission services' autumn 2009 forecasts (COM); Stability programme (SP).

4. GENERAL GOVERNMENT BALANCE

This section consists of four parts. The first three parts discuss the budgetary implementation in the year 2009, the budgetary plans for 2010 and the medium-term budgetary strategy in the programme. The final part analyses the risks attached to the budgetary targets.

4.1. Budgetary implementation in 2009

According to the February 2010 update of the stability programme, the general government deficit is expected to have reached 7.9% of GDP in 2009, compared to 3.4%

in 2008. This deterioration essentially reflects the working of automatic stabilisers as a result of the economic downturn as well as the impact of fiscal stimulus measures in line with the EERP estimated at 1.1% of GDP. Although increased from the original plan of 0.8% of GDP, the overall size of these measures can still be considered as broadly appropriate given France's limited fiscal space.

Table 3 compares the projected outcome for the general government balance, revenue and expenditure (as a percentage of GDP) in 2009 as presented in the new stability programme with the targets from the previous update of the programme. Differences between outcome and targets (excluding the impact of the unanticipated GDP developments which may have affected the ratio, referred to as the ‘denominator effect’) are decomposed in the impact of a base effect stemming from a different starting position (i.e. the outcome of 2008 may also have been different from what was anticipated in the previous programme update) and the impact of differences in the revenue / expenditure growth rate from the planned growth rates[6].

Compared to the December 2008 update of the stability programme, the general government deficit in 2009 is 4pps. of GDP higher, which is largely explained by the effect of negative surprises as regards both revenue and expenditure. To a lesser extent, this difference stems from the starting position by end 2008, which turned out to be more negative than anticipated in the previous stability programme by 0.5 % of GDP.

The decomposition between revenue and expenditure surprises clearly highlights the prominence of the former over the latter in the explanation of the expected deterioration of the general government deficit. As nominal GDP growth in 2009 turned out to be significantly lower than anticipated in the previous programme (nominal growth was projected to increase by a range of [0.2 ; 0.5]%, whereas it actually contracted by 2.2%), it seems advisable to eliminate this large "denominator effect" to correctly interpret revenue and expenditure surprises.

Once corrected for the denominator effect, the revenue surprise explains 3.7 pps of a total difference of 3.9 pps. The negative surprise in revenue is essentially a consequence of the impact of the economic downturn, particularly on corporate tax receipts and, to a lesser extent, on VAT, which also suffered to some extent from an unexpected decrease of its tax base linked to composition effects. In addition, the impact of revenue measures in the framework of the recovery plan (notably alleviating firms’ liquidity constraints) was 0.3% of GDP higher than expected at the time of the submission of the previous programme.

As regards the expenditure side, a negative surprise of 0.2% of GDP excluding denominator effect is expected, notably linked with higher-than-expected functioning of automatic stabilisers. There were no unscheduled one-off measures in 2009 that played an important role in the deviations from the target set in the previous programme.

Overall, the revision of GDP growth in 2009, from a projected [0.2; 0.5]% in the previous stability programme, to -2.2% has raised the deficit by around 1 ¼ pp. The 2009 deficit outcome indicates that, on top of a larger impact of the recovery measures in line

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6 Mathematically, the difference in the revenue ratio in Table 3 can be expressed as:

$$\rho^{o}-\rho^{p}=\underbrace{\frac{1+r^{p}}{1+g^{p}}\Delta\rho_{-1}}_{\text{Base effect}}+\underbrace{\frac{\rho_{-1}^{o}}{(1+g^{o})(1+g^{p})}\Delta r}_{\text{Revenue growth effect}}-\underbrace{\frac{\rho_{-1}^{o}}{(1+g^{o})(1+g^{p})}\Delta g}_{\text{Denominator effect}}+\underbrace{\frac{\rho_{-1}^{o}\left(r^{o}g^{p}-r^{p}g^{o}\right)}{(1+g^{o})(1+g^{p})}}_{\text{Residual}}$$

where r is the growth rate of revenue and g is the growth rate of GDP. The subscript -1 refers to the previous year’s value. Superscripts o and p refer to the outcome and the planned value respectively. Similar for the expenditure ratio.

with the EERP, the economic downturn had a sharper budgetary impact than could have been expected when applying standard elasticities.

Table 3: Budgetary implementation in 2009

	2008		2009	
	Planned SP Dec 2008	Outcome SP Feb 2010	Planned SP Dec 2008	Outcome SP Feb 2010
Government balance (% of GDP)	-2.9	-3.4	-3.9	-7.9
Difference compared to target [1]	-0.5		-4.0	
Difference excluding denominator effect [1,2]			**-3.9**	
Of which : due to a different starting position end 2008			-0.5	
due to different revenue / expenditure growth in 2009			-3.3	
p.m. Residual [3]			-0.1	
p.m. Nominal GDP growth (planned and outcome)			*2.3*	*-1.3*
Revenue (% of GDP)	49.8	49.3	49.6	47.7
Revenue surprise compared to target [1]	-0.5		-1.9	
Revenue surprise excluding denominator effect [1,2]			**-3.7**	
Of which : due to a different starting position end 2008			-0.5	
due to different revenue growth in 2009			-3.1	
p.m. Residual [3]			0.0	
p.m. Revenue growth rate (planned and outcome)			*1.9*	*-4.5*
Expenditure (% of GDP)	52.7	52.7	53.5	55.6
Expenditure surprise compared to target [1]	0.0		-2.1	
Expenditure surprise excluding denominator effect [1,2]			**-0.2**	
Of which : due to different starting position end 2008			0.0	
due to different expenditure growth rate in 2009			-0.1	
p.m. Residual [3]			-0.1	
p.m. Expenditure growth rate (planned and outcome)			3.9	4.1

Notes:

[1] A positive number implies that the outcome was better (in terms of government balance) than planned.

[2] The denominator effect captures the mechanical effect that, if GDP turns out higher than planned, the ratio of revenue or expenditure to GDP will fall because of a higher denominator. Although the denominator effect can be very significant for revenue and expenditure separately, on the balance they usually largely cancel against each other.

[3] The decomposition leaves a small residual that cannot be assigned to the previous components. The residual is generally small, except in some cases where planned and actual growth rates of revenue, expenditure and GDP differ significantly.

Source : Commission services

Box 1: The excessive deficit procedure (EDP) for France

On 27 April 2009, the Council adopted a decision stating that France had an excessive deficit in accordance with Article 104(6) of the Treaty establishing the European Community (TEC)). At the same time, it addressed a recommendation to France under Article 104(7) TEC specifying that the excessive deficit should be corrected by 2012. On 2 December 2009, the Council, following a recommendation by the Commission, considered that action had been taken in accordance with the recommendations, but unexpected adverse economic events with major unfavourable consequences for government finances had occurred after the adoption of the recommendation, and issued new recommendations to correct the deficit by 2013. In particular, growth in 2009 was revised down from -1.8% to -2.2% while the expected deficit was revised up from 5.4% of GDP to 8.3% in view notably of the larger budgetary impact than an application of standard budgetary elasticities would have implied.

In particular, the French authorities were recommended to implement the deficit-reducing measures in 2010 as planned in the government proposal for the budget in 2010 while avoiding a further deterioration of public finances, and to implement and strengthen the fiscal effort from 2011 onwards above the consolidation measures already planned. In order to put an end to the present excessive deficit situation, France should ensure an average fiscal consolidation of above 1% of GDP over the period 2010 – 2013, which should also contribute to bringing the government gross debt ratio back on a declining path that approaches the reference value at a satisfactory pace by restoring an adequate level of the primary surplus. The French authorities were also recommended to 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 and budgetary conditions turn out better than currently expected. In addition, the French authorities should 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. The Council established the deadline of 2 June 2010 for the French government to take effective action to implement the fiscal measures in 2010 as planned in the government proposal for the budget law for 2010 and to outline in some detail the consolidation strategy that will be necessary to progress towards the correction of the excessive deficit. The assessment of effective action will take into account economic developments compared to the economic outlook in the Commission services' autumn 2009 forecast. The French authorities should report on progress made in the implementation of these recommendations in a separate chapter in the updates of the stability programme which will be prepared between 2010 and 2013.

4.2. The programme's budgetary strategy for 2010

The February 2010 stability programme expects the general government deficit in 2010 to further deteriorate by 0.3% of GDP when compared to 2009 and reach 8.2% of GDP in 2010. This deterioration occurs both on the revenue side, which is set to deteriorate by 0.1% of GDP, and on expenditure side, which would increase by 0.2% of GDP.

Taken at face value, the budgetary target for 2010 driven by the measures presented in the programme can be considered as broadly consistent with the latest recommendations under article 126(7) TFEU addressed to France; the country has implemented the deficit-reducing measures in 2010 as planned in the government proposal for the budget law for 2010 while largely avoiding a further deterioration of public finances, with the exception of the decision on the public loan that will have a negative budgetary impact of around 0.1% of GDP in 2010 (and an additional impact of 0.1% of GDP each following programme year).

The deficit projection for 2010 is 0.3% of GDP better than the one presented in the draft budget for 2010 submitted to Parliament on 30 September (and adopted in December), where the authorities projected the general government deficit to reach 8.5% of GDP in 2010. The anticipated better 2009 deficit outcome is expected to create a positive base effect for 2010 amounting to 0.2% of GDP and the revision of growth projections by the French authorities would translate into an additional 0.3% of GDP improvement of the general government deficit in 2010. However, the target was only revised down by 0.3% in view of the suspension of the environmental tax by the French Constitutional Court as well as the introduction of measures stemming from the previously mentioned public loan (see box 2), which would together, for the time being, deteriorate the general government deficit by around 0.2% of GDP compared to plan (but this deterioration could be limited to 0.1% of GDP in case an amended version of the environmental tax is eventually implemented). The latter two elements changed the balance of discretionary measures from around +¼% of GDP at the time of the Council recommendation to broadly neutral in the programme. Compared to 2009, the recovery measures for 2009 in line with the EERP, reaching 1.1% of GDP, are partially phased out and reduced to 0.35% of GDP in 2010, and there are some further consolidation measures of 0.1% of GDP (notably the increase in taxes included in the social security budget), bringing total compensation measures to 0.8% of GDP. However, these consolidation measures are offset by new deficit increasing measures included in the original budget for 2010 amounting to 0.7% of GDP, notably the reform of the local business tax (around 0.6 % of GDP) and the decrease in VAT for the catering sector (0.1% of GDP), as well as by the measures related to the public loan amounting to around 0.1% of GDP.

Box 2: The public loan to invest in the future

On 22 June, in a speech to the Congress, President Sarkozy announced the launching of a public loan (*emprunt national*) "to invest in the future". The revised draft budget for 2010, sent to Parliament on 20 January, formally makes provisions for the public loan in the Budget. The loan reaches € 35 bn (around 1.7% of GDP); 60% of it (€ 22 bn, or around 1% of GDP) would be used for capital injections or loans for firms, therefore impacting gross public debt but not the ESA deficit. The remaining 40% (€ 13 bn, or around 0.7% of GDP) can eventually be spent over the next years and will be mainly transferred to public agencies. These agencies are in charge of using the funds for investments in the fields identified in President Sarkozy's speech on 14 December 2009, i.e. higher education and training; research; industry and innovative SMEs; sustainable development; digital technology.

According to the French authorities, the impact of the public loan on the budget will amount to 0.1% of GDP in 2010, excluding interest payments that will be compensated by expenditure cuts elsewhere. The latter are estimated to reach € 0.5 bn (less than 0.1% of GDP) in 2010, compensated by expenditure cuts. For the following years, the impact on the budget is expected to increase by 0.1% of GDP each programme year and will have to be addressed, on top of the consolidation measures that will be required to reduce the deficit.

All in all, taken at face value, the budgetary target for 2010 driven by the measures presented in the programme can be considered as broadly consistent with the latest recommendations under article 126(7) TFEU addressed to France; the country has implemented the deficit-reducing measures in 2010 as planned in the government proposal for the budget law for 2010 while largely avoiding a further deterioration of public finances, with the exception of the decision on the public loan that will have a negative budgetary impact of around 0.1% of GDP in 2010 (and an additional impact of a similar magnitude in each following programme year).

Looking at the breakdown of the expected deficit for 2010 by sub-sectors of general government, the central government deficit would be reduced by 0.3% of GDP when compared to 2009 to 5.9% of GDP, driven notably by the improvement of the macro-economic situation. The social security deficit would substantially increase by 0.6% of GDP attaining 1.9% of GDP, notably due to the continued rise in unemployment benefits related to the worsening situation on the labour market. This assumes that the increase in health expenditure (*Objectif National des Dépenses d'Assurance Maladie*, or ONDAM) would be limited to 3% in 2010 (after 3.4% in 2009) thanks to efficiency improving measures in hospitals or targeted decrease in the reimbursement rate of certain medicines, are described in a comprehensive way, although not quantified in terms of budgetary impact on savings. The deficit for local authorities would also slightly deteriorate in

2010, reaching 0.5% of GDP, after 0.4% of GDP in 2009, notably due to the increase of social benefits they are in charge of.

In 2010, the structural deficit, i.e. the cyclically-adjusted deficit net of one-off and other temporary measures calculated by the Commission's services on the basis of the programme figures according to the commonly agreed methodology, would deteriorate by ¼ pp. and reach 6¾% of GDP. When taking into account the transitory impact of anticipated reimbursements for firms of 0.4% of GDP in the context of the implementation of the reform of the local business tax, a one-off measure but not considered as such in the programme, the structural deficit would slightly improve by 0.1 pp in 2010 to 6½ % of GDP[7].

Looking only at 2010, the planned structural adjustment envisaged in the programme is substantially below the "above 1% of GDP" recommended for the average annual structural adjustment over 2010 – 2013 as foreseen in the Council recommendation of 2 December to France and should there be an improvement of the macroeconomic situation without concomitant improvement in the fiscal balance there would be even no structural adjustment at all. This suggests that even substantially higher efforts would be needed in the following years.

Table 4. Main budgetary measures for 2010

Revenue measures[1]	Expenditure measures[2]
• Acceleration of government payments to corporations (in line with the EERP) (-0.1% of GDP) • Other revenue measures in line with the EERP (among which cut in employers' social contributions for very small firms) (-0.1% of GDP) • Reform of the local business tax (-0.6% of GDP) • Decrease in VAT for the catering sector (-0.1% of GDP) • Increase in taxes in the social security budget (0.1% of GDP)	• Additional public investment (in line with the EERP) (0.1% of GDP) • Social measures in favour of employment and professional training (in line with the EERP) (0.1% of GDP) • Expenditure measures stemming from the public loan (0.1% of GDP)

Notes:

[1] Estimated impact on general government revenue
[2] Estimated impact on general government expenditure

Source: Commission services, Budget law and Social security law.

4.3. The programme's medium-term budgetary strategy

This section describes the medium-term budgetary strategy outlined in the programme - and how it compares with the one in the previous update - as well as the composition of the budgetary adjustment, including the broad measures envisaged.

[7] In case an amended version of the environmental tax is eventually implemented, the structural balance could be improved by another 0.1% of GDP.

The main goal of the programme's budgetary strategy is to bring the general government balance below the 3% of GDP reference value by 2013, the deadline set in the Council recommendation of 2 December 2009.

The programme considers that the medium-term objective (MTO) is a balanced budget in structural terms (see also box 3). The programme does not mention a target year for achieving the MTO. It indicates that, in order to meet this objective, a working group on balanced budget rules has been set up on 28 January 2010

Box 3: The medium-term objective (MTO) for France

As noted in the Code of Conduct[8], the MTO aims to (a) provide a safety margin with respect to the 3% of GDP deficit limit; (b) ensure rapid progress towards fiscal sustainability; and (c) allow room for budgetary manoeuvre, in particular taking into account the needs for public investment. The MTO is defined in cyclically adjusted terms, net of one-off and other temporary measures. On 7 July 2009, the ECOFIN Council took note of a new methodology for setting MTOs, ensuring that implicit liabilities (costs related to ageing populations, in particular projected healthcare and pension expenditure) are also accounted for.

Specifically, the country-specific MTOs should take into account three components: (i) the debt-stabilising balance for a debt ratio equal to the (60% of GDP) reference value (dependent on long-term potential growth), implying room for budgetary manoeuvre for Member States with relatively low debt; (ii) a supplementary debt-reduction effort for Member States with a debt ratio in excess of the (60% of GDP) reference value, implying rapid progress towards it; and (iii) a fraction of the adjustment needed to cover the present value of the future increase in age-related government expenditure. This implies a partial frontloading of the budgetary cost of ageing irrespective of the current level of debt. In addition to these criteria, MTOs should provide a safety margin with respect to the 3% of GDP deficit reference value and, for euro area and ERM II Member States, in any case not exceed a deficit of 1% of GDP.

As communicated by the authorities, the MTO of France is a balanced budget in structural terms. In view of the new methodology and given the most recent projections and debt level, the MTO of France more than adequately reflects the objectives of the Pact.

The consolidation strategy outlined in the programme would rely on measures aimed at curbing expenditure growth at all sub-government levels, on top of the complete phasing out in 2011 of the measures in line with the EERP.

At the central government level, measures to streamline expenditure are expected to be unveiled in April by the Ministry of Budget and should be included in the new three-year budget to be presented to the Parliament in autumn. Additionally, the programme indicates that central government expenditure would decrease by around 0.1% in real terms on average each year throughout 2010 – 2013 notably backed by the implementation of the reforms in line with the General Review of Public Policies (*Révision Générale des Politiques Publiques*, or RGPP). Against this background, the

[8] "Specifications on the implementation of the Stability and Growth Pact and guidelines on the format and content of stability and convergence programmes", endorsed by the ECOFIN Council on 10 November 2009, available at: http://ec.europa.eu/economy_finance/sgp/legal_texts/index_en.htm

central government deficit is expected to decline from 5.9% of GDP in 2010 to 2% of GDP in 2013.

As regards social security spending, the programme foresees that, after an increase by 3% in 2010, the rise in national health spending (ONDAM) would be below 3% on average from 2011 to 2013, which would lead to a reduction in the social security deficit from 1.9% of GDP in 2010 to 1% of GDP in 2013. Whereas the measures backing the expenditure objective set in 2010 are described in a comprehensive way, this is not yet the case for the following years. According to the programme, new measures designed to meet the objective assigned for the 2011 – 2013 period will be unveiled in April. Moreover, regarding specifically pension expenditure, the stability programme states that a new reform of the pension system will be presented in 2010.

Concerning local authorities, the programme anticipates a subdued increase in their expenditure over the programme period, which would reduce the deficit from 0.5% in 2010 to 0.1% in 2013. This expenditure constraint is supposed to come notably from the implementation of the reform of local authorities, currently debated at Parliament and aimed at improving their efficiency. Additionally, new measures to curb the increase of spending at local authorities' level would be presented in April.

The consolidation strategy presented in the programme would also be supported by measures on the revenue side. The French authorities intend to further reduce the budgetary impact of existing tax exemptions by around 0.1% of GDP each year starting in 2011. The programme does not indicate which tax exemptions would be targeted.

Overall, from 2011 onwards, the consolidation strategy relies on measures not yet specified.

Regarding the time profile of the adjustment path, the programme anticipates that the general government budget deficit increases from 7.9% of GDP in 2009 to 8.2% in 2010; thereafter it is expected to decline and reach 6% in 2011, 4.6% in 2012 and 3% in 2013. From 2010 to 2013, the expenditure ratio would decrease by 3% of GDP, which incorporates a negative denominator effect of around 6 ½ pps. Over the same period, the revenue ratio would increase by 2.2% of GDP, taking into account a decrease stemming from a denominator effect of around 5 ¾ pps. Adding to the previously mentioned measures on expenditure and revenue, those targets would be supported by an elasticity of fiscal revenue to GDP reaching 1.2 in 2011-2013 according to the programme.

The primary balance is foreseen to follow a somewhat similar path. The structural deficit, as recalculated by the Commission's services according to the commonly agreed methodology, would deteriorate from 6.5% in 2009 to 6.8% of GDP in 2010. When taking into account the impact of the 0.4% of GDP one-off previously mentioned and related to anticipated reimbursements in the context of the implementation of the reform of the local business tax, the structural deficit would slightly improve to 6.4% of GDP. The structural deficit would further diminish in 2011 to reach 5% of GDP in 2011, 4% in 2012 and eventually 2.8% in 2013.

The average annual fiscal effort, based on the evolution of the structural balance as recalculated by the Commission's services according to the commonly agreed methodology would reach 0.9% of GDP on average each year from 2010 to 2013. It is therefore below what was requested in the recommendation, which recommended the French authorities to ensure an average annual fiscal effort of above 1% of GDP over this period, and builds on the favourable assumptions that growth will be relatively strong and elasticities above historical average.

Table 5: Composition of the budgetary adjustment

(% of GDP)	2008	2009		2010		2011		2012	2013	Change: 2009-2013
	COM	COM	SP	COM	SP	COM[1]	SP	SP	SP	SP
Revenue	**49.3**	**47.0**	**47.7**	**46.8**	**47.6**	**47.1**	**48.6**	**49.1**	**49.8**	**2.1**
of which:										
- Taxes on production and imports	14.8	14.4	14.7	14.5	14.2	14.4	14.6	14.7	14.9	0.2
- Current taxes on income, wealth, etc.	11.4	9.9	9.7	10.1	10.4	10.7	10.9	11.2	11.5	1.8
- Social contributions	17.9	17.4	18.2	17.0	17.9	16.8	17.9	18.0	18.0	-0.2
- Other (residual)	5.1	5.3	5.1	5.2	5.1	5.2	5.2	5.2	5.4	0.3
Expenditure	**52.7**	**55.2**	**55.6**	**55.1**	**55.8**	**54.8**	**54.6**	**53.7**	**52.8**	**-2.8**
of which:										
- Primary expenditure	49.9	52.5	53.1	52.2	53.2	51.8	51.8	50.8	49.8	-3.3
of which:										
Compensation of employees and intermediate consumption	17.7	18.3	18.5	18.2	18.5	18.1	18.0	17.6	17.1	-1.4
Social payments	23.3	24.6	25.0	24.8	25.3	24.6	24.9	24.5	24.3	-0.7
Subsidies	1.4	1.5	1.5	1.4	1.4	1.4	1.3	1.3	1.3	-0.2
Gross fixed capital formation	3.2	3.5	3.4	3.3	3.4	3.3	3.2	3.2	3.1	-0.3
Other (residual)	4.3	4.5	4.8	4.4	4.6	4.4	4.3	4.2	4.1	-0.7
- Interest expenditure	2.8	2.8	2.5	2.9	2.6	3.0	2.8	2.9	3.0	0.5
General government balance (GGB)	**-3.4**	**-8.3**	**-7.9**	**-8.2**	**-8.2**	**-7.7**	**-6.0**	**-4.6**	**-3.0**	**4.9**
Primary balance	**-0.6**	**-5.5**	**-5.4**	**-5.4**	**-5.5**	**-4.7**	**-3.2**	**-1.7**	**-0.1**	**5.3**
One-off and other temporary measures	0.1	0.0	0.0	-0.4	0.0	0.0	0.0	0.0	0.0	0.0
GGB excl. one-offs	**-3.5**	**-8.3**	**-7.9**	**-7.8**	**-8.2**	**-7.7**	**-6.0**	**-4.6**	**-3.0**	**4.9**
Output gap[2]	0.8	-2.5	-2.9	-2.5	-2.9	-2.4	-2.1	-1.2	-0.4	2.4
Cyclically-adjusted balance[2]	-3.8	-7.0	-6.5	-7.0	-6.8	-6.5	-4.9	-4.0	-2.8	3.7
Structural balance[3]	**-3.9**	**-7.0**	**-6.5**	**-6.6**	**-6.8**	**-6.5**	**-4.9**	**-4.0**	**-2.8**	**3.7**
Change in structural balance		*-3.1*	*-2.6*	*0.4*	*-0.3*	*0.1*	*1.8*	*1.0*	*1.2*	
Structural primary balance[3]	-1.1	-4.2	-4.0	-3.7	-4.2	-3.5	-2.1	-1.1	0.2	4.2
Change in structural primary balance		*-3.2*	*-2.9*	*0.5*	*-0.2*	*0.2*	*2.0*	*1.1*	*1.3*	

Notes:

[1]On a no-policy-change basis.

[2]Output gap (in % of potential GDP) and cyclically-adjusted balance according to the programme as recalculated by Commission services on the basis of the information in the programme.

[3]Structural (primary) balance = cyclically-adjusted (primary) balance excluding one-off and other temporary measures.

Source:

Stability programme (SP); Commission services' autumn 2009 forecasts (COM); Commission services' calculations

4.4. Risk assessment

This section discusses the plausibility of the programme's budgetary projections by analysing various risk factors. For the period until 2011, Table 5 compares the detailed revenue and expenditure projections in the Commission services' autumn 2009 forecast, which are derived under a no-policy change scenario, with those in the updated programme. However, although the assessment uses the Commission services' forecast as a benchmark, it also takes explicitly into account all available information about more recent developments.

As far as 2010 is concerned, the deficit target appears to be rather plausible and even leaves some room for a better performance in case the environmental tax is eventually implemented in an amended form. The budgetary projections are subject to significant downside risks from 2011 to 2013. As regards 2010, the Commission services' autumn 2009 forecast anticipated the general government deficit to reach 8.2% of GDP, after 8.3% in 2009. However, due to the cut-off date of the forecast, data on budget implementation in 2009 as well as new information that became available after the adoption of the original budget for 2010 were not taken into account. The better budgetary outcome for 2009, translating in 2010 into a positive base effect of 0.2% of

GDP, would be compensated by the impact of measures related to the public loan and the suspension of the environmental tax.

Based on the information provided in the programme, meeting the medium-term targets is subject to significant downside risks that could jeopardise the correction of the excessive deficit by 2013 as recommended the Council recommendation of 2 December (see Box 1).

The most significant downward risks are linked to the macroeconomic scenario. As discussed in section 3, the composition of growth of the programme's forecast for 2010 is slightly more favourable from a fiscal point of view than that of the Commission services (with a bigger contribution of domestic demand and notably private consumption, and a smaller contribution of inventories). More importantly, from 2011 to 2013, the programme's projections are markedly optimistic. In the sensitivity analysis provided in annex 2 of the programme, average GDP growth is lower by ¼ pp. from 2011 to 2013 (2.25% instead of 2.5%). In this case and according to the programme, the deficit would be 4% of GDP in 2013, and the 3% threshold would be reached only in 2014. This – still rather optimistic – alternative scenario illustrates the high sensitivity of the deficit projections to growth. A cumulative loss of ¾ % of GDP would therefore translate in 2013 into a deficit increase of 1% of GDP. All in all, it appears that if, as is to be expected, growth is significantly lower than projected in the programme from 2011, then budgetary outcomes will be significantly worse than targeted and the excessive deficit would not be corrected in time.

The deficit targets could also be negatively affected by possible expenditure slippages rather optimistic assumptions regarding the projected evolution of revenue, once the above-mentioned effect of the macroeconomic scenario have been accounted for.

Regarding expenditure, as already mentioned in the previous section, the consolidation strategy outlined in the programme would notably rest on measures aimed at curbing expenditure growth at all sub-governments levels. In this regard, the programme expects public expenditure, excluding recovery measures in line with the EERP as well as measures stemming from the public loan, to increase by 0.9 % in volume terms on average each year from 2010 to 2013, and even by 0.6% over 2011 – 2013, compared to an average increase of 2% over 1991 – 2008. However, the removal of the impact of the public loan is questionable as it hides certain expenditure that will weigh on the deficit and debt and will need to be compensated by other savings measures.

For the correction in the public expenditure trend compared to the historical trend the programme refers to measures that are not yet specified but are supposed to be unveiled in the coming months.

More specifically, public spending at the central government level would decrease by 0.1% in volume terms on average from 2010 to 2013. Expenditure restraint is expected to stem notably from measures that would be identified as a result of the RGPP as well as from additional measures that would be made public in April. No information is provided concerning their budgetary impact as well as their implementation schedule. Additionally, the public loan will eventually increase public debt by around 1% of GDP overall therefore putting a drag on interest payments. While in 2010 cuts in expenditure aiming at compensating for their budgetary impact are specified in the programme, no measures are announced for the outer years.

Social security spending would increase by 0.9% in volume terms on average each year from 2010 to 2013. Healthcare expenditure and pensions account for around 4/5 of social security spending. Since the evolution of pensions is largely determined by demography, the uncertainty in the evolution of social security spending lies mainly in healthcare expenditure. The programme expects the national health insurance spending objective (*Objectif National des Dépenses d'Assurance Maladie*, or ONDAM) to reach 3% in 2010 and below 3% afterwards. The evolution of the ONDAM is notably driven by health facilities spending. In this regard, the programme refers to measures aimed at improving their efficiency. However, their budgetary impact is not provided. Moreover, reaching the target set for the outer years will be possible, according to the programme, thanks to further measures yet to be unveiled. Eventually, given France's past track record (ONDAM was only reached once in twelve years), there is a risk that healthcare expenditure could turn out to be higher than projected in the programme. As regards the pension system, the programme refers to a reform expected in 2010. No measures have been announced yet.

The growth rate of local authorities' spending is projected to reach 1.6% in volume terms on average from 2010 to 2013. This rather subdued increase would be linked to the implementation of the reform of local authorities, notably aimed at increasing their efficiency. This reform is currently debated at Parliament; it is expected to be progressively implemented, starting soon after the law is passed, and to be achieved in 2014, therefore after the programme horizon. Its budgetary impact is not assessed. Additionally, the programme indicates that reaching the spending target for local authorities would be possible with further reforms, which will be unveiled only in the forthcoming months.

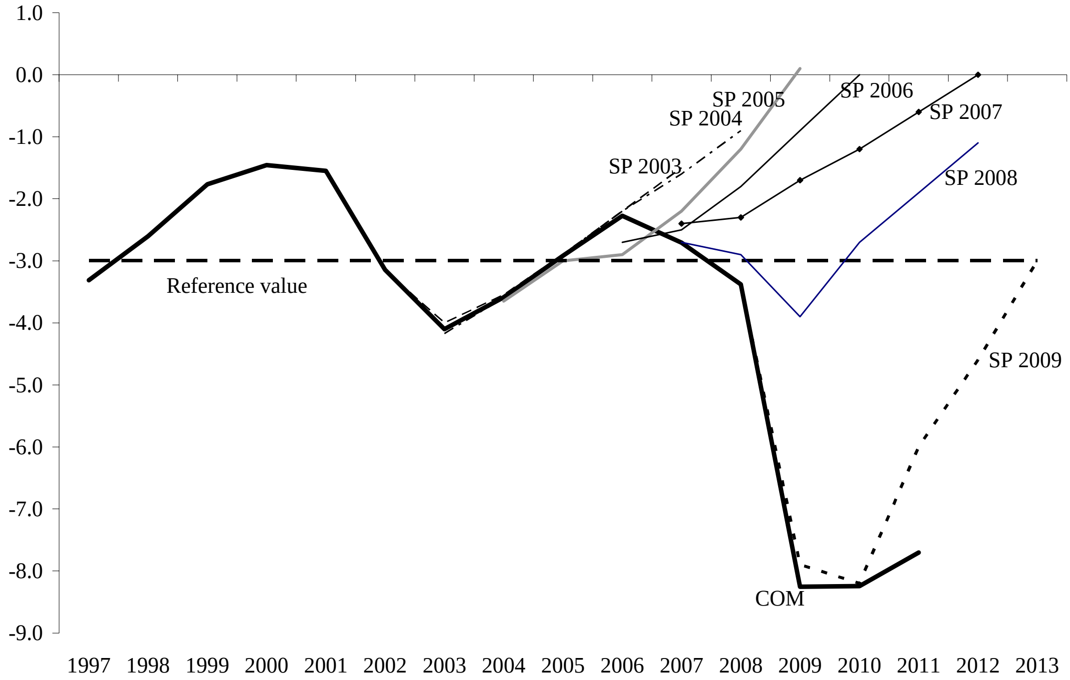
The overall development of the revenue ratio is also subject to substantial risk. From 2011 to 2013, the tax-to-GDP elasticity would reach 1.2, which is rather high when compared to its remarkable stability over the past 30 years at around 1. The programme indicates that tax exemptions would be reduced by around 0.1% of GDP each year as of 2011. However, the programme does not specify which exemptions would be removed and what is the timing that would back this decrease in tax exemptions. Moreover, as indicated by a recent report from the French Court of Auditors[9], while the first three-year budget adopted in February 2009 for the 2009 – 2012 period included rule to compensate for any increase in the budgetary impact of tax exemptions, this rule has not been observed in 2009 and their overall budgetary impact increased by € 1.2 bn (less than 0.1% of GDP). The Court anticipates that this impact will raise the deficit by a further € 2.2 bn (around 0.1% of GDP) in 2010 if not compensated by other measures. The objective set in the programme on the evolution of tax exemptions therefore raises some doubts.

Finally, France's overall track record when it comes to respecting its budgetary targets is rather poor as illustrated in figure 11; long-term (more than two-year) budgetary projections have always been missed since 2000.

Overall, the assessment based on the information presented in the programme and given the above analysis suggests that there are substantial risks that the deficit outcomes for the 2011 – 2013 period may be worse than targeted in the programme and therefore that the excessive deficit is not corrected in 2013, the deadline set in the Council recommendation of 2 December.

[9] *Finances publiques: au-delà de la crise, l'aggravation du déficit structurel,* February 2010

Figure 1: Government balance projections in successive programmes (% of GDP)



Source: Commission services' autumn 2009 forecast (COM) and successive stability programmes

5. GOVERNMENT DEBT AND LONG-TERM SUSTAINABILITY

This section is in two parts. A first part describes recent debt developments and medium-term prospects, including risks to the outlook presented in the programme. A second part takes a longer-term perspective with the aim of assessing the long-term sustainability of public finances.

5.1. Recent debt developments and medium-term prospects

5.1.1. Debt projections in the programme

The debt-to-GDP ratio almost stabilised in 2007 and rose in 2008 to 67.4% of GDP, notably due to a deficit exceeding 3% of GDP but also as a result of several government operations including those to stabilise the financial system. In 2008, the French authorities established two funds: the first one to increase the capitalisation of banks in order to bolster their solvency and the second one to boost bank liquidity and compensate for the dysfunctional interbank market. Capital injection by the government reached around 0.6% of GDP in 2008 and thus affected public debt. At the end of 2008, the total amount raised by the latter fund (SFEF – *Société de financement de l'économie française*) for lending to the banks with central government guarantees reached around 0.7% of GDP but was not accounted for in the public debt as Eurostat clarified on 15 July 2009 that debt issued by "other central bodies" (to which SFEF belongs) in support of the financial sector would not be included in the general government debt.

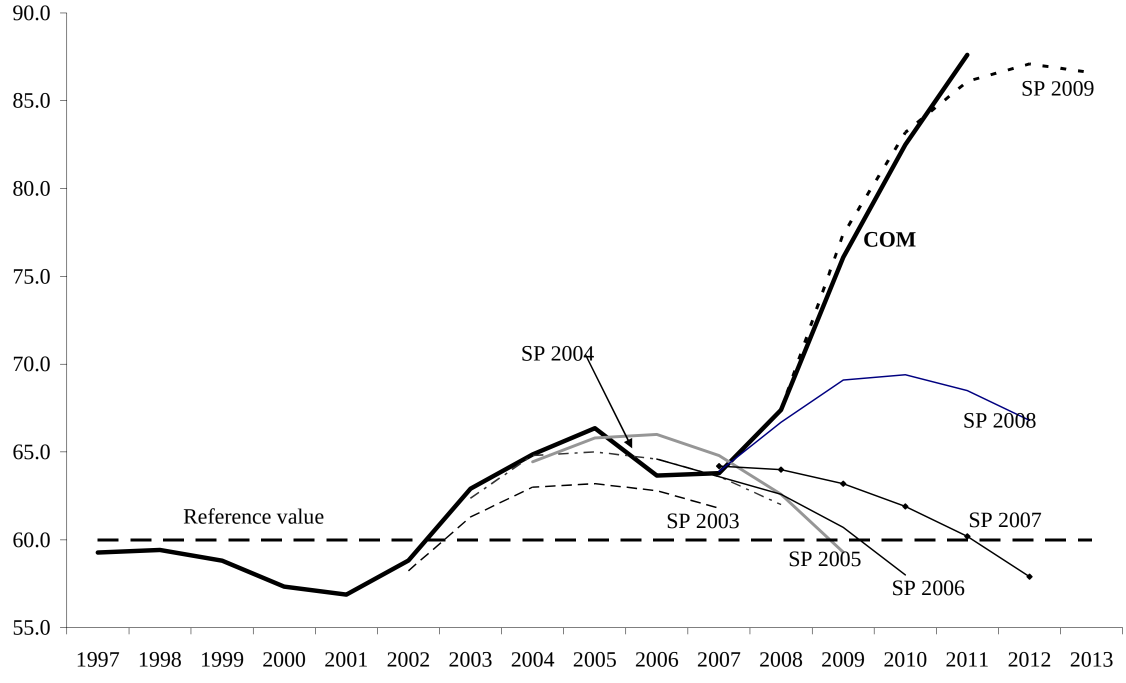
The programme expects the debt-to-GDP ratio to have further increased to 77.4% of GDP in 2009, notably as a result of a high deficit. This compares to 76.1% of GDP in the Commission services' autumn forecast. The gap mainly stems from a 1 pp. difference in stock-flow adjustment in 2009. Most importantly, at the cut-off-date of the autumn forecast, banks had reimbursed 0.7% of GDP of government capital injection, and the government eventually decided to use the 0.7% of GDP reimbursements to finance the public loan. The remaining difference stems notably from an increase in financial assets of pension funds. The total amount of guarantees provided to SFEF for lending to banks and not accounted in the public debt reached around 4% of GDP at the end of 2009.

In 2010, the debt-to-GDP ratio is expected to further increase to 83.2% of GDP, mainly attributable to the high government deficit. The public loan is expected to increase the general government debt by another 1/4 of GDP (including the 0.1% of GDP impact on the deficit).

In the outer years, the debt-to-GDP ratio will continue to increase until 2012; it would reach 86.6% of GDP at the end of the programme period. The public loan is expected to increase the general government debt by around 0.2% of GDP each year (including the 0.1% of GDP impact on the deficit).

In the past, the debt targets of the successive stability programmes have regularly been revised upwards and often missed (see Figure 2 below), notably due to deficit revisions.

Figure 2: Debt projections in successive programmes (% of GDP)



<u>Source</u>: *Commission services' autumn 2009 forecast (COM) and successive stability programmes*

Table 6: Debt dynamics

(% of GDP)	average 2003-07	2008	2009		2010		2011		2012	2013
			COM	SP	COM	SP	COM	SP	SP	SP
Gross debt ratio[1]	**64.3**	**67.4**	**76.1**	**77.4**	**82.5**	**83.2**	**87.6**	**86.1**	**87.1**	**86.6**
Change in the ratio	1.0	3.6	8.7	10.0	6.4	5.8	5.1	2.9	1.0	-0.5
Contributions [2] :										
1. Primary balance	**0.4**	**0.6**	**5.5**	**5.4**	**5.4**	**5.5**	**4.7**	**3.2**	**1.7**	**0.1**
2. "Snow-ball" effect	**0.2**	**1.0**	**3.0**	**3.4**	**1.0**	**0.8**	**0.4**	**-0.4**	**-0.6**	**-0.7**
Of which:										
Interest expenditure	2.7	2.8	2.8	2.5	2.9	2.7	3.0	2.8	2.9	2.9
Growth effect	-1.2	-0.3	1.5	1.5	-0.9	-1.1	-1.2	-2.0	-2.1	-2.1
Inflation effect	-1.3	-1.5	-1.3	-0.7	-0.9	-0.8	-1.4	-1.2	-1.4	-1.5
3. Stock-flow adjustment	**0.4**	**2.0**	**0.2**	**1.2**	**0.0**	**-0.5**	**0.0**	**0.1**	**-0.1**	**0.1**
Of which:										
Cash/accruals diff.	0.1	0.2		n.a.		n.a.		n.a.	n.a.	n.a.
Acc. financial assets	0.3	1.8		n.a.		n.a.		n.a.	n.a.	n.a.
Privatisation	-0.4	0.0		n.a.		n.a.		n.a.	n.a.	n.a.
Val. effect & residual	0.0	0.0		n.a.		n.a.		n.a.	n.a.	n.a.

Notes:

[1]End of period.

[2]The snow-ball effect captures the impact of interest expenditure on accumulated debt, as well as the impact of real GDP growth and inflation on the debt ratio (through the denominator). The stock-flow adjustment includes differences in cash and accrual accounting, accumulation of financial assets and valuation and other residual effects.

Source :

Stability programme (SP); Commission services' autumn 2009 forecasts (COM); Commission services' calculations

5.1.2. Assessment

In the programme, the debt-to-GDP ratio in 2010 is 0.7% higher than in the Commission services' autumn 2009 forecast. This difference is partly explained by a difference in the starting position in 2009: the debt-to-GDP ratio in the programme is 1.3% higher than in the Commission services' autumn 2009 forecast. Additionally, the programme states that the cash-flow transactions would generate a negative stock-flow adjustment of 0.5% of GDP, not taken into account in the Commission services' autumn 2009 forecast.

Risks to the debt scenario are clearly on the upside, mainly related to the above-mentioned risks to the deficit targets. The debt ratio is on an increasing path and above the Treaty reference value over the entire programme period.

5.2. Long-term debt projections and the sustainability of public finances

5.2.1. Sustainability indicators and long-term debt projections

This section presents sustainability indicators based on the long-term age-related government spending as projected by the Member States and the EPC in 2009 according to an agreed methodology[10].

Table 7 shows that age-related spending is projected to rise by 2.2 percentage points of GDP between 2010 and 2060, below the EU average (4.6 pps.). Sustainability indicators for two scenarios are presented in Table 8. 'The 2009 scenario' is based on a no-policy-

[10] Economic Policy Committee and the European Commission (2009), '2009 Ageing Report: Economic and budgetary projections for the EU-27 Member States (2008-60)', *European Economy* No. 2/2009. European Commission (2009), 'Sustainability Report 2009, European Economy No. 9/2009. European Commission (2008), 'Public finances in EMU – 2008', *European Economy* No. 4/2008..

change assumption and the 2009 structural primary balance as a starting year, while 'the programme scenario' takes into account the consolidation planned in the programme up to 2013 and is based on the projected 2013 structural primary balance as a starting position. Assuming that the structural primary balance remained at its 2009 level and including the increase in age-related expenditure, the sustainability gap (S2)[11] would amount to 7.1% of GDP; about 3½ percentage points more than in last year's assessment, which is due to a lower estimated structural primary balance in the starting year, while the rise in age-related expenditure is lower in the 2009 projection than in the previous one. The starting budgetary position is not sufficient to stabilize the debt ratio over the long-term and entails a risk of unsustainable public finances even before considering the long-term budgetary impact of ageing.

The "programme scenario" foresees a significant improvement in the structural primary balance and thus shows a smaller sustainability gap. If the budgetary consolidation planned in the programme was achieved, risks to long-term sustainability of public finances would be mitigated.

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Table 7: Long-term age-related expenditure: main projections

(% of GDP)	**2007**	**2010**	**2020**	**2030**	**2040**	**2060**	**Change 2010- 60**
Total age-related spending	**28.4**	**29.0**	**29.4**	**30.5**	**31.3**	**31.2**	**2.2**
- Pensions	13.0	13.5	13.6	14.2	14.4	14.0	0.6
- Healthcare	8.1	8.2	8.6	8.9	9.2	9.4	1.1
- Long-term care	1.4	1.5	1.6	1.8	2.0	2.2	0.7
- Education and unemployment benefits	5.9	5.8	5.6	5.6	5.5	5.6	-0.2
Property income received	0.8	0.8	0.7	0.7	0.6	0.6	-0.2

Source: Economic Policy Committee and Commission services.

Table 8: Sustainability indicators and the required primary balance

	2009 scenario			**Programme scenario**		
	S1	**S2**	**RPB**	**S1**	**S2**	**RPB**
Value	7.2	7.1	3.0	2.9	2.9	2.9
of which:						
Initial budgetary position (IBP)	5.2	5.3	-	1.0	1.0	-
Debt requirement in 2060 (DR)	0.6	-	-	0.4	-	-
Long-term change in the primary balance (LTC)	1.4	1.8	-	1.4	1.8	-

Source: Commission services.

Based on the assumptions used in the projection of age-related expenditure and the calculation of the sustainability indicators, Figure 3 displays the projected debt-to-GDP ratio over the long-term.

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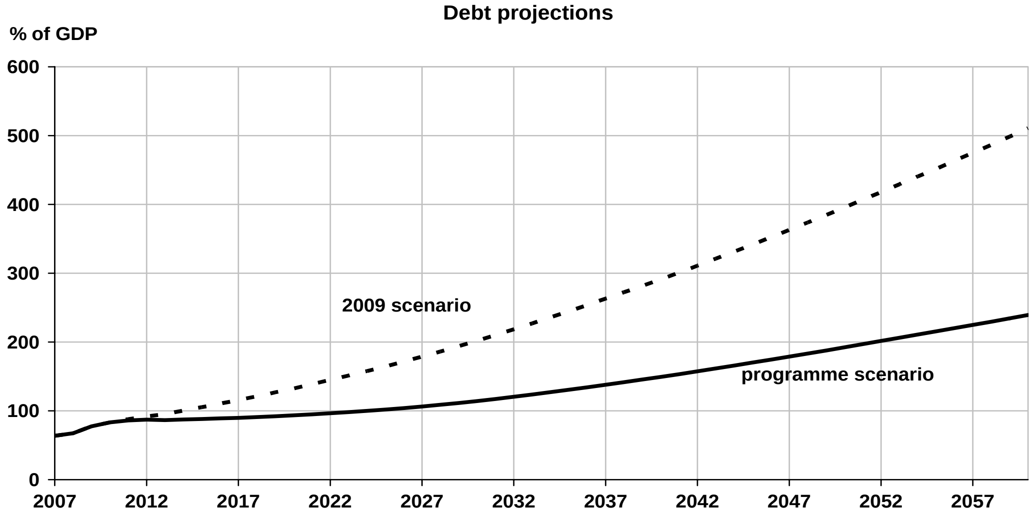
[11] The S2 indicator is defined as the change in the current level of the structural primary balance required to make sure that the discounted value of future structural primary balances (including the path of property income) covers the current level of debt.

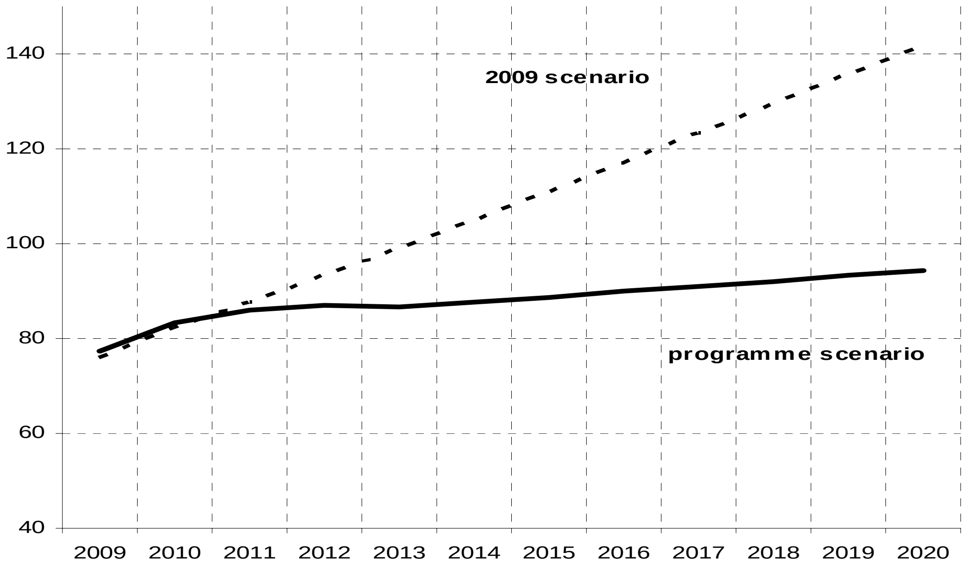
Figure 3: Long-term projections for the government debt ratio



<u>Source</u>: *Commission services calculations*

Based on the alternative assumptions of economic developments presented in the Commission services' autumn 2009 forecast publication[12], Figure 4 shows projected medium-term trajectory of the debt-to-GDP ratio. The projected debt trajectories reveal significantly different paths under both sets of assumptions: while, based on the programme scenario, the increase in the debt-to-GDP ratio would be relatively subdued and remain below 100% over the projection period, in the 2009 scenario it would increase at a much faster pace and eventually reach around 140% of GDP in 2020.

Figure 4: Medium-term projections for the government debt ratio



<u>Source</u>: *Commission services' calculations*

[12] Section 3.5 in European Commission (2009), 'European Economic Forecast – autumn 2009', European Economy No. 10/2009. This economic scenario assumes that the output gap caused by the crisis will be closed by 2017.

5.2.2. Additional factors

For an overall assessment of the sustainability of public finances, other relevant factors are taken into account (Table 9). As indicated in Table 9 none of these factors have an impact on the overall long-term sustainability assessment.

Table 9: Additional factors for the assessment of long-term sustainability risks.

	Impact on risk
Debt and pension assets	na
Decline in structural balance until 2011 in COM Autumn 2009 forecast	-
Alternative projection of cost of ageing	na
Strong decline in benefit ratio	na
High tax burden	na
Difference between S1 and S2	na

Note: '-': factor tends to increase the risk to sustainability, '+': factor tends to decrease the risk to sustainability.
'na': not applicable.

Alternative projections are often presented in the programmes, whose assumptions often diverge from the common method. Projections currently discussed in the Economic Policy Committee but not yet published, are for the time being also considered "unofficial.".

An explanation on these factors can be found in chapter V of: European Commission (2009), Sustainability Report 2009, European Economy No. 9/2009.

Source: Commission services.

5.2.3. Assessment

The long-term budgetary impact of ageing is clearly lower than the EU average, with pension expenditure showing a more limited increase, as a result of the pension reforms already enacted. The budgetary position in 2009, as estimated in the programme, which is significantly worse than the starting position of the previous programme, compounds the budgetary impact of population ageing on the sustainability gap. Ensuring primary surpluses over the medium term would contribute to reducing the high risks to the sustainability of public finances.[13] The current level of gross debt is above the Treaty reference value. Medium-term debt projections until 2020 that take account of more recent economic developments and projections on the potential growth show that the budgetary development envisaged in the programme is not enough to stabilise debt in the medium term but would increase it to the level of around 95 % of GDP by 2020.

6. INSTITUTIONAL FEATURES OF PUBLIC FINANCES

6.1. Fiscal framework

As regards its medium-term budgetary framework, France ranks in the first quartile among European countries, according to the DG ECFIN database on fiscal governance.

[13] In the Commission's 2009 Sustainability Report the risks to the sustainability of public finances were assessed as medium.

France's medium-term budgetary strategy is based on the setting of multi-annual objectives for the increase in general government real expenditure. Until 2008, these objectives were set in the annual updates of the stability programmes and were not adopted by the Parliament. Given that the objectives were rarely reached, reforms were introduced to further improve the overall budgetary framework. They include the reform of the Constitution on 23 July 2008 where a balanced budget objective, although non-binding, was introduced for public administrations. Additionally, on 9 February 2009, the first multi-year public finance planning act was adopted by Parliament, setting out expenditure targets at all general government sub-sectors. It also notably lays down the principle of budgetary neutrality for the creation of new tax exemptions, whose aggregate cost must be fully offset. However, as was previously mentioned, a recent report from the French Court of Auditors states that this principle has not been met in 2009 and the overall budgetary impact of tax exemptions increased by € 1.2 bn (less than 0.1% of GDP). The Court anticipates that it could increase by a further € 2.2 bn (around 0.1% of GDP) in 2010 if not compensated by other measures.

Regarding fiscal rules, France ranks in the second quartile among European countries, according to the DG ECFIN database on fiscal governance. The annual budgetary framework in France is notably comprises expenditure norms set for general government sub-levels. A first rule, the so-called "zero volume increase expenditure rule", is set at the central government level. It has been formally adhered to in recent years. In the past, changes in the perimeter of the rule have helped to respect it. For instance, some fast growing expenditures, such as the *Revenu Minimum d’Insertion* (RMI - minimum integration income), were removed from the perimeter of the rule (when it was decided that the local authorities should be in charge of it). In addition, some expenditure were substituted into tax exemptions, equivalent in deficit terms but facilitating the respect of the rule. Recently, the perimeter was broadened with the aim of achieving a better control of central government expenditure and the rule has been adhered to. The national health insurance spending objective (*Objectif National des Dépenses d’Assurance Maladie*) is aimed at controlling healthcare spending; still, it has been reached only once, the year it was introduced. Finally, local authorities' expenditures are not allowed to raise debt to finance operational expenditures and the increase of funds transferred by the central government cannot exceed the rate of inflation. However, the objectives set in the stability programmes have rarely been reached, notably due to expenditure slippages linked to the dynamism of the payroll.

The government intends to further reform the fiscal framework. A conference on public finances, gathering notably representatives from social security and local authorities, was organised on 28 January 2010 with the aim of addressing the significant deterioration of French public finances and on how to implement budgetary consolidation. Several working groups were set up to propose new reforms to be unveiled in April and notably aiming at further curbing the evolution of healthcare spending, or at better controlling local expenditures. A working group on balanced budget rules was also set up. The programme also indicates that new measures aimed at reducing central government spending will be presented in April.

6.2. Quality of public finances

At 52.7% of GDP in 2008, France's expenditure-to-GDP ratio is the highest in the euro area. The rise in public expenditure over the past decades has contributed to high deficits and debt levels, which have affected the long-term sustainability of French public finances. Assessing the breakdown by functions of public expenditure highlights the relative importance in France, compared to the euro area, of social protection, education and healthcare expenditure. However, as regards education and healthcare, relatively high public spending in those two functions does not match with results, when looking at PISA scores for education, or life expectancy and infant mortality for healthcare.

The French authorities launched in 2007 the General Review of Public Policies (*Revue Générale des Politiques Publiques*, or RGPP) with the aim of identifying ways of making government expenditure more efficient. It is led by a dedicated body, the *Conseil de la modernisation des politiques publiques*, rather than Ministries, and benefits from external expertise. Moreover, this process does not only address the efficiency of public policies but it also calls into question their relevance on the basis of assessment tests. More than 300 measures have been identified so far (with the aim to achieve savings of around 0.3% of GDP which has been rather modest compared to the global amount of public expenditure, exceeding 50% of GDP). About ¾ have been implemented and for example made possible the non-replacement of one out of two retiring civil servants in the central government sub-sector. The government announced in the budget law for 2010 that the RGPP would be extended to other central bodies. Additionally, the programme states that further reforms in the context of the RGPP will be announced in autumn. Regarding the pension system, the programme refers to a further reform expected in 2010, following the reform of 2003. No measures have been announced so far.

7. OVERALL ASSESSMENT

Taking into account the risks attached to the budgetary targets discussed above, this section assesses the appropriateness of the fiscal strategy in relation to the Council Recommendations under Article 126(7) of 2 December 2009 with a view to correcting the excessive deficit and the budgetary objectives of the Stability and Growth Pact, against the background of the current economic situation, the debt and long-term sustainability position of the country, and the institutional features of its public finances.

As far as 2010 is concerned, the recommendations under Article 126(7) state that the French authorities should implement the deficit-reducing measures as planned in the government proposal for the budget law for 2010 while avoiding a further deterioration of public finances. The programme expects the general government deficit to slightly improve to 8.2% of GDP, compared to 8.5%, the official forecast at the time of the Recommendation. The recovery measures in line with the EERP would be partially phased out but replaced by other stimulus measures. Overall, in 2010 the budgetary strategy set out in the programme is broadly consistent with the Council recommendations under Art. 126(7) although the authorities decided to raise a public loan which is expected to have a negative impact of 0.1% of GDP on the budget in 2010 (and an additional impact of a similar magnitude in subsequent years covered by the programme). On the other hand, additional revenues from the new version of the environmental tax, as mentioned in the programme, should eventually help achieving a better result.

The recommendations under Article 126(7) TFEU also state that the French authorities should put an end to the excessive deficit situation by 2013. Specifically, to this end, the French authorities should ensure an average fiscal consolidation of above 1% of GDP over the period 2010 – 2013, which should also contribute to bringing the government gross debt ratio back on a declining path that approaches the reference value at a satisfactory pace by restoring an adequate level of the primary surplus. The French authorities were also recommended to 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 and budgetary conditions turn out better than currently expected.

The programme anticipates the nominal budget deficit to decrease from 2010 to 2013, when it would eventually reach 3% of GDP, therefore leaving no safety margin for the correction of the excessive deficit. As regards the evolution of the structural balance over the programme period, as calculated under the commonly agreed methodology, it would only slightly improve in 2010 to 6.4% of GDP (by 0.1% of GDP), when taking into account a 0.4% of GDP one-off, and it would further better thereafter at 5% of GDP in 2011, 4% in 2012 and eventually 2.8% in 2013. The average annual fiscal effort, based on the evolution of the structural would reach 0.9% of GDP, therefore below what was requested in the recommendation (above 1% of GDP).

There are significant downward risks associated with the budgetary targets presented in the programme raising doubts that the excessive deficit can be corrected on time. First, from 2011 to 2013, the macroeconomic scenario is markedly optimistic and in particular significantly higher than the Commission services forecast on which the recommendations were based. The programme explicitly states that the budgetary targets over the programme period are highly sensitive to growth projections: indeed, if growth is lower by ¼ pp. from 2011 to 2013 (2.25% instead of 2.5%), the deficit would reach 4% of GDP in 2013, which is a reflection of the fact that the strategy for bringing the deficit to an end by 2013 is too much dependent on high growth and not sufficiently on structural adjustment. Second, the consolidation strategy outlined in the programme would notably rest on measures aimed at substantially curbing expenditure growth at all sub-governments levels. However, the measures that should support the control of public expenditure are not specified in the programme and are only expected to be announced in the coming months. Third, the evolution of the revenue ratio is also subject to substantial risk. The tax-to-GDP elasticity assumed at 1.2 over the 2011 – 2013 period is above its historical values (around 1). As mentioned in the Council recommendation of 2 December 2010, some better-than-expected revenue surprises partially mirroring the negative surprises of previous years cannot be excluded; however, it would be more prudent to consider such a development a positive risk rather than include it in the baseline. Moreover, the measures backing the reduction in tax exemptions by around 0.1% of GDP each year starting in 2011 are not specified.

Overall, taking into account the risks, the budgetary strategy from 2011 on does not seem to be consistent with the Council Recommendation under Art. 126(7). Using windfalls related to an improvement of the macro-economic and fiscal outlook, as well as the implementation of all envisaged tax measures would accelerate deficit reduction and the decline of the gross debt ratio back towards the 60% reference value. The fiscal consolidation may need to be strengthened to ensure a correction of the excessive deficit by 2013. Further consolidation measures, in particular for 2011 and beyond, may be needed, in case risks related to the fact that the macroeconomic scenario of the programme is more favourable than the scenario underpinning the Article 126(7) Recommendation materialise. Moreover, the measures necessary to ensure an average annual fiscal effort of above 1% of GDP over the period 2010 - 2013 and to achieve a correction of the excessive deficit by 2013 need to be further specified. Finally, the recommendations under Article 126(7) TFEU also state that the fiscal consolidation should also contribute to bringing the government gross debt ratio back on a declining path that approaches the reference value at a satisfactory pace by restoring an adequate level of the primary surplus. In this regard, the budgetary strategy may not be sufficient to bring debt back on a downward path and would benefit from a strengthening of the consolidation effort.

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ANNEX. COMPLIANCE WITH THE FORMAT AND CONTENT REQUIREMENTS FOR STABILITY AND CONVERGENCE PROGRAMME

This annex provides an assessment of whether the programme respects the requirements of Section II of the code of conduct (guidelines on the format and content), notably as far as (i) the model structure (Annex 1 of the code of conduct); (ii) the format data provisions (Annex 2 of the code of conduct); and (iii) other information requirements is concerned. It also assesses to what extent France followed up on the Council's recommendation to report on progress made in the correction of the excessive deficit, in a separate chapter of the programme.

(i) Model structure

The update broadly adheres to the code of conduct as far as data requirements are concerned. The missing data did not impede the assessment. Most compulsory data have been provided except assumptions on short- and long-term interest rates (Table 8).

(ii) Data requirements

Part of the optional data is missing. Tables on general government expenditure by function and on long-term sustainability are partly filled (Table 3: all data are missing for 2013; Table 7: total expenditure, social security pension, old-age and early pensions, other and occupational pensions, interest expenditure, total revenue composition and all assumptions are missing). Employment-hours worked and labour productivity-hours worked are missing (Table 1.c labour market development); net lending/borrowing of the private sector and statistical discrepancy (table 1.d sectoral balances); government consumption (nominal) (Table 2 general government budgetary prospects); stock-flow adjustment composition (for 2009-2012) and privatisation proceeds (for 2008-2012), liquid financial assets and net financial debt (Table 4 general government debt developments) are missing as well. In addition, figures for 2008 are not provided for real GDP and change in inventories (Table 1a) and labour productivity persons (Table 1c).

The tables on the following pages show the data presented in the February 2010 update of stability programme, following the structure of the tables in Annex 2 of the code of conduct. Compulsory data are in bold, missing data are indicated with grey-shading.

(iii) Separate chapter on progress made in the correction of the excessive deficit

In its recommendation under article 104/126(7) of 2 December 2009 with a view to bringing the excessive deficit situation to an end, the Council also invited France to report on progress made in the implementation on the Council's recommendations in a separate chapter in the updates of the stability programme. France complied with this recommendation by outlining the steps it plans to take in this respect.

(iv) Other information requirements

The table below provides a summary assessment of the adherence to the other information requirements in the code of conduct.

* * *

The SCP…	Yes	No	Comments
a. Involvement of parliament			
… mentions status vis-à-vis national parliament.		X	
… indicates whether Council opinion on previous programme has been presented to national parliament.	X		
b. Economic outlook			
… (for euro area and ERM II Member States) uses “common external assumptions” on main extra-EU variables.	X		The external assumptions used for the international environment are very close the ones used in the COM forecasts
… explains significant divergences with Commission services’ forecasts[1].		X	Despite quite close external assumption (only divergence is about oil prices in 2011 where in the programme are lower (77$) compared to 80$ in COM forecast) growth profiles are different, mainly for 2011.
… bears out possible upside/downside risks to economic outlook.	X		
… analyses outlook for sectoral balances and, especially for countries with high external deficit, external balance.			Not applicable as external deficit remains limited at around 2% of GDP.
c. Monetary/exchange rate policy			
… (CP only) presents medium-term monetary policy objectives and their relationship to price and exchange rate stability.			Not applicable
d. Budgetary strategy			
… presents budgetary targets for general government balance in relation to MTO and projected path for debt ratio.	X		The programme does not specifiy the deadline for reaching the MTO. However, on 3 February, the French Prime Minister said in an interview that the French authorities intend to meet the MTO in 2020.
… (in case new government has taken office) shows continuity with respect to budgetary targets endorsed by Council.			Not applicable
… (when applicable) explains reasons for deviations from previous targets and, in case of substantial deviations, whether measures are taken to rectify situation (+ provides information on them).			Not applicable
… backs budgetary targets by indication of broad measures necessary to achieve them and analyses their quantitative effects on balance.	X		The target for 2010 is underpinned by measures; for 2011 onwards the programme states that measures will be announced in the forthcoming months
… specifies state of implementation of measures.	X		
e. “Major structural reforms”			
… (if MTO not yet reached or temporary deviation is planned from MTO) includes comprehensive information on economic and	X		

The SCP…	Yes	No	Comments
budgetary effects of possible 'major structural reforms' over time.			
… includes quantitative cost-benefit analysis of short-term costs and long-term benefits of reforms.	X		
f. Sensitivity analysis			
… includes comprehensive sensitivity analyses and/or develops alternative scenarios showing impact on balance and debt of: a) changes in main economic assumptions b) different interest rate assumptions c) (for CP only) different exchange rate assumptions d) if common external assumptions are not used, changes in assumptions for main extra-EU variables.	X X X X		 Not applicable
… (in case of "major structural reforms") analyses how changes in assumptions would affect budget and potential growth.			Not applicable
g. Broad economic policy guidelines			
… provides information on consistency with broad economic policy guidelines of budgetary objectives and measures to achieve them.	X		
h. Quality of public finances			
… describes measures to improve quality of public finances, both revenue and expenditure sides.	X		
i. Long-term sustainability			
… outlines strategies to ensure sustainability.	X		
… includes common budgetary projections by the AWG and all necessary additional information (esp. new relevant information).	X		
j. Other information (optional)			
… includes information on implementation of existing national budgetary rules and on other institutional features of public finances.	X		

Notes: SCP = stability/convergence programme; CP = convergence programme
[1]To the extent possible, bearing in mind the typically short time period between the publication of the Commission services' autumn forecast and the submission of the programme.

Source:
Commission services

Tables from Annex 2 of the code of conduct

Table 1a. Macroeconomic prospects

	ESA Code	2008 Level	2008 rate of change	2009 rate of change	2010 rate of change	2011 rate of change	2012 rate of change	2013 rate of change
1. Real GDP	B1*g	*n.a.*	0.4	-2.25	1.4	2.5	2.5	2.5
2. Nominal GDP	B1*g	*1950.1*	2.9	-1.3	2.5	4.0	4.3	4.3
Components of real GDP								
3. Private consumption expenditure	P.3	*1114.1*	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. Changes in inventories and net acquisition of valuables (% of GDP)	P.52 + P.53	*n.a.*	0.3	-1.5	-1.2	-0.9	-0.7	-0.6
7. Exports 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 real GDP growth								
9. Final domestic demand		-	1.0	-0.4	0.9	2.3	2.3	2.3
10. Changes 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 developments

	ESA Code	2008 Level	2008 rate of change	2009 rate of change	2010 rate of change	2011 rate of change	2012 rate of change	2013 rate of change
1. GDP deflator		*n.a.*	2.5	1.0	1.1	1.5	1.75	1.75
2. Private consumption deflator		*n.a.*	2.8	-0.2	1.3	1.5	1.75	1.75
3. HICP[1]		*n.a.*	3.2	0.1	1.3	1.6	1.75	1.75
4. Public consumption deflator		*n.a.*	2.1	1.8	1.2	1.5	1.75	1.75
5. Investment deflator		*n.a.*	3.9	0.0	1.3	1.3	1.75	1.75
6. Export price deflator (goods and services)		*n.a.*	2.9	-3.4	1.9	1.6	1.1	1.1
7. Import price deflator (goods and services)		*n.a.*	4.0	-6.6	2.4	1.1	1.1	1.1

[1] Optional for stability programmes.

Table 1c. Labour market developments

	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]		*25841*	0.5	-1.2	-0.7	0.5	0.7	0.7
2. Employment, hours worked[2]		*n.a.*	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
3. Unemployment rate (%)[3]		*n.a.*	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
4. Labour productivity, persons[4]		*n.a.*	0.2	-0.5	1.8	1.9	1.8	1.8
5. Labour productivity, hours worked[5]		*n.a.*	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
6. Compensation of employees	D.1	*1015.8*	3.2	0.1	1.0	3.5	4.0	4.0
7. Compensation per employee		*n.a.*	n.a.	n.a.	optional	optional	optional	optional

[1]Occupied population, domestic concept national accounts definition.

[2]National accounts definition.

[3]Harmonised definition, Eurostat; levels.

[4]Real GDP per person employed.

[5]Real GDP per hour worked.

Table 1d. Sectoral balances

% 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
of which : - Balance on goods and services		-2.5	-1.7	-1.8	-1.8	-1.8	-1.7
- Balance of primary incomes and 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	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
3. Net lending/borrowing of general government	EDP B.9	-3.4	-7.9	-8.2	-6.0	-4.6	-3.0
4. Statistical discrepancy		n.a.	optional	optional	optional	optional	optional

Table 2. General government budgetary prospects

	ESA Code	2008	2008	2009	2010	2011	2012	2013
		Level	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP
Net lending (EDP B.9) by 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	*n.a.*	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
4. Local government	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 (S13)								
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
11. One-off and other temporary measures[3]		*n.a.*	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Selected components of revenue								
12. Total taxes (12=12a+12b+12c)		*n.a.*	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
12a. Taxes on production and imports	D.2	*287.9*	14.8	14.7	14.2	14.6	14.7	14.9
12b. Current taxes on income, wealth, etc	D.5	*223.1*	11.4	9.7	10.4	10.9	11.2	11.5
12c. Capital taxes	D.91	*7.9*	0.4	0.4	0.4	0.4	0.5	0.5
13. Social contributions	D.61	*349.5*	17.9	18.2	17.9	17.9	18.0	18.0
14. Property income	D.4	*17.2*	0.9	0.8	0.8	0.8	0.8	0.8
15. Other[4]		*75.2*	3.9	3.9	3.9	4.0	4.1	4.1
16=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+D.91-D.995)[5]		834.3	42.8	41.0	41.0	41.9	42.4	43.0
Selected components of expenditure								
17. Compensation of employees + intermediate consumption	D.1+P.2	*345.1*	**17.7**	**18.5**	**18.5**	**18.0**	**17.6**	**17.1**
17a. Compensation of employees	D.1	*n.a.*	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
17b. Intermediate consumption	P.2	*n.a.*	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
18. Social payments (18=18a+18b)		*n.a.*	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
18a. Social transfers in kind supplied via market producers	D.6311, D.63121, D.63131	*111.3*	5.7	6.1	6.1	6.0	5.9	5.9
18b. Social transfers other than in kind	D.62	*342.1*	17.5	18.9	19.2	18.9	18.6	18.4
19=9. Interest expenditure	EDP D.41	*54.3*	2.8	2.5	2.6	2.8	2.9	3.0
20. Subsidies	D.3	*27.3*	1.4	1.5	1.4	1.3	1.3	1.3
21. Gross fixed capital formation	P.51	*62.4*	3.2	3.4	3.4	3.2	3.2	3.1
22. Other[6]		*84.3*	4.3	4.8	4.6	4.3	4.2	4.1
23=7. Total expenditure	TE[1]	*1026.7*	52.7	55.6	55.8	54.6	53.7	52.8
p.m.: Government consumption (nominal)	P.3	*247.7*	12.7	13.2	13.1	12.9	12.6	12.3

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

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

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

[4] P.11+P.12+P.131+D.39+D.7+D.9 (other than D.91).

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

[6] D.29+D4 (other than D.41)+ D.5+D.7+D.9+P.52+P.53+K.2+D.8.

Table 3. General government expenditure by function

% of GDP	COFOG Code	2008	2013
1. General public services	1	7.1	n.a.
2. Defence	2	1.8	n.a.
3. Public order and safety	3	1.2	n.a.
4. Economic affairs	4	2.8	n.a.
5. Environmental protection	5	0.9	n.a.
6. Housing and community amenities	6	1.9	n.a.
7. Health	7	7.8	n.a.
8. Recreation, culture and religion	8	1.5	n.a.
9. Education	9	5.8	n.a.
10. Social protection	10	21.8	n.a.
11. Total expenditure (=item 7=23 in Table 2)	TE[1]	52.7	52.8

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

Table 4. General government debt developments

% of GDP	ESA Code	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
of which:							
- Differences between cash and accruals[4]		0.2	n.a.	n.a.	n.a.	n.a.	n.a.
- Net accumulation of financial assets[5]		1.8	n.a.	n.a.	n.a.	n.a.	n.a.
of which:		-	-	-	-	-	-
- privatisation proceeds		0.0	n.a.	n.a.	n.a.	n.a.	n.a.
- Valuation effects and other[6]		0.0	n.a.	n.a.	n.a.	n.a.	n.a.
p.m.: Implicit interest rate on debt[7]		4.5	3.6	3.5	3.5	3.5	3.5
Other relevant variables							
6. Liquid financial assets[8]		22.2	n.a.	n.a.	n.a.	n.a.	n.a.
7. Net financial debt (7=1-6)		45.2	n.a.	n.a.	n.a.	n.a.	n.a.

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

[2]Cf. item 10 in Table 2.

[3]Cf. item 9 in Table 2.

[4]The differences concerning interest expenditure, other expenditure and revenue could be distinguished when relevant.

[5]Liquid assets, assets on third countries, government controlled enterprises and the difference between quoted and non-quoted assets could be distinguished when relevant.

[6]Changes due to exchange rate movements, and operation in secondary market could be distinguished when relevant.

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

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

Table 5. Cyclical developments

% of GDP	ESA Code	2008	2009	2010	2011	2012	2013
1. Real GDP growth (%)		0.4	-2.25	1.4	2.5	2.5	2.5
2. Net lending of general government	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 and other temporary 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 factor productivity		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 budgetary component		-0.2	-2.1	-2.4	-2.0	-1.7	-1.4
8. Cyclically-adjusted 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 update

	ESA Code	2008	2009	2010	2011	2012	2013
Real GDP growth (%)							
Previous update		1.0	0.2/0.5	2.0	2.5	2.5	n.a.
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	n.a.
General government net lending (% of GDP)	EDP B.9						
Previous update		-2.9	-3.9	-2.7	-1.9	-1.1	n.a.
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	n.a.
General government gross debt (% of GDP)							
Previous update		66.7	69.1	69.4	68.5	66.8	n.a.
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	n.a.

Table 7. Long-term sustainability of public finances

% of GDP	2000	2007	2010	2020	2030	2050
Total expenditure	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Of which: age-related expenditures	n.a.	28.4	29.0	29.4	30.5	31.3
Pension expenditure	n.a.	13.0	13.5	13.6	14.2	14.2
Social security pension	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Old-age and early pensions	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Other pensions (disability, survivors)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Occupational pensions (if in general government)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Health care	n.a.	8.1	8.2	8.6	8.9	9.3
Long-term care *(this was earlier included in the*	n.a.	1.4	1.5	1.6	1.8	2.2
Education expenditure	n.a.	4.7	4.6	4.6	4.7	4.7
Other age-related expenditures	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Interest expenditure	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Total revenue	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Of which: property income	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Of which : from pensions contributions (or social contributions if appropriate)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Pension reserve fund assets	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Of which : consolidated public pension fund assets (assets other than government liabilities)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Assumptions						
Labour productivity growth	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Real GDP growth	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Participation rate males (aged 20-64)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Participation rates females (aged 20-64)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Total participation rates (aged 20-64)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Unemployment rate	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Population aged 65+ over total population	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.

Table 8. Basic assumptions

	2008	2009	2010	2011	2012	2013
Short-term interest rate[1] (annual average)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Long-term interest rate (annual average)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
USD/€ exchange rate (annual average) (euro area and ERM II countries)	1.47	1.40	1.48	1.48	1.48	1.48
Nominal effective exchange rate	113.5	114.0	115.7	115.7	115.7	115.7
(for countries not in euro area or ERM II) exchange rate vis-à-vis the € (annual average)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
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
Growth of relevant foreign markets	1.6	-13.0	5.5	6.2	6.6	6.6
World import volumes, excluding EU	2.8	-12.9	9.5	7.6	7.7	7.7
Oil prices (Brent, USD/barrel)	97	62	77	77	78	79

[1]If necessary, purely technical assumptions.