Liberté • Égalité • Fraternité
RÉPUBLIQUE FRANÇAISE
Le Gouvernement

STABILITY PROGRAMME

APRIL 2019

Index

1.

OVERVIEW

Overview

This Stability Programme provides an update of the French government's growth forecasts and targeted public finances adjustment path for the period 2019-2022. The economic context for this budgetary and fiscal programme remains upbeat, but the growth forecast has been revised down since the 2019 draft budgets were presented, notably due to a less favourable international economic environment. The updated trajectory also accounts for the measures decided on at the end of 2018 to address the pressing economic and social needs and the expectations expressed by the French population. This Stability Programme supplements the National Reform Programme, published concomitantly, which describes the government's transformation strategy.

France's public deficit was brought back below the 3% threshold in 2017 (2.8% of GDP, after 3.5% in 2016). The deficit narrowed again in 2018 to 2.5% of GDP. This outturn surpassed forecasts from six months ago and reflects France's unwavering efforts to place its public finances back on sound footing and to fulfil its European commitments. First and foremost, it demonstrates that a turning point has been reached through substantial efforts to rein in public spending. For the first time in decades, public spending declined in real terms (–0.3% excluding tax credits, +1.3% in nominal terms). This tight rein on spending will continue throughout the current five-year presidential term. These efforts have already begun to allow a decrease in the tax burden for households and businesses and will continue to do so, while also reducing the public deficit.

After growing by 1.6% in 2018, the French economy is expected to sustain robust growth of 1.4% p.a. in 2019 and 2020. Household consumption is likely to perform very well in 2019, thanks to strong support from measures to boost consumers' purchasing power (including those announced in December) and a still dynamic trend in employment and wages. Business investment, which has been very vigorous since 2015, is expected to keep growing at a strong pace despite gradually slowing due to the less upbeat international environment and the incremental rise in interest rates. As housing starts have been declining since the start of 2018, construction investment by households is set to slightly decrease in 2019, before recovering in 2020 thanks to strong gains in purchasing power and robust employment growth. Exports are set to continue to enjoy robust growth, albeit a touch below the 2018 level due to the less favourable international environment. Inflation is expected to slow to 1.3% p.a. in 2019 and 2020, after 1.8% in 2018, as energy prices level off.

Between now and 2022, the steady recovery in France's public finances will be underpinned by control of public spending, which will also enable a reduction in the tax burden. Public spending, in real terms, is forecast to grow by 0.4% in 2019[1]. On average, over the full five-year presidential term, real public spending growth is set to be just 0.2% p.a.[1], compared to a rate of 1.2% p.a. over the period 2008-2017. As a percentage of GDP, public spending is expected to decline by nearly 3 points1 between 2017 and 2022, in keeping with the objective laid out in the 2018-2022 Public Finance Planning Act.

This tight rein on spending is absolutely crucial to lower the tax burden and rebalance our public finances. The tax burden (as measured by the aggregate tax and social security contribution rate) is set to decline by 1.4 pt of GDP over the five-year presidential term1. After tax cuts in 2018, further substantial measures will be implemented in 2019: the Competitiveness and Employment Tax Credit (CICE) will be transformed into permanent cuts in employer social security contributions, the withholding-at-source system has been launched for personal income tax, and overtime pay will be exempt from taxes and social contributions. In addition, 2019 will see the full-year impact of the reduction of employees' social security contributions (in exchange for an increase in the General Social Security Contribution, CSG), as well as the exemption of the CSG hike for pensioners with net income of less than €2,000 per month. Finally, households will benefit from a second round of cuts to the residence tax in 2019. Additional measures to reduce the tax burden will be implemented until 2022, with the residence tax being eliminated for all households (apart from second homes) and the corporate income tax rate being lowered to 25%, within the EU average.

The public deficit was 2.5% of GDP in 2018. It is expected to be 2.3% in 2019 excluding the one-off double cost of converting the CICE into social security contribution cuts (or 3.1% including this one-off), then 2.0% in 2020. The public deficit is forecast at 1.2% of GDP in 2022.

By meeting these objectives, we will also begin to reduce our debt-to-GDP ratio, which levelled off at 98.4% in 2018 (unchanged vs. end 2017). This ratio is expected to decline by a little less than two GDP points by 2022.

This Stability Programme was drafted before any conclusions were issued following the Great National Debate. It therefore serves as a technical reference point prior to any decisions being made in response to this debate, notably on matters of taxation or public spending. In responding to topics broached during the Great National Debate, the government will focus strongly on ensuring the sustainability of French public finances and safeguarding the structural adjustment

1 On a like-for-like basis, not including the France Compétences vocational training scheme, which will gradually come on line and has a neutral impact on the public deficit.

2.

MACROECONOMIC SCENARIO

Macroeconomic scenario

2.1 SITUATION IN 2018 AND OUTLOOK FOR 2019 AND 2020

After growing by 1.6% in 2018, the French economy is expected to sustain robust growth of 1.4% p.a. in 2019 and 2020. Inflation is expected to decrease to 1.3% p.a. in 2019 and 2020, after 1.8% in 2018.

Household consumption is likely to perform very well in 2019, thanks to strong support from measures to boost consumers' purchasing power (including those announced in December) and a still dynamic employment and wage growth. Business investment, which has been very dynamic since 2015, is expected to grow at a strong pace despite gradually returning to its normal growth rate due to the less upbeat international environment and the incremental rise in interest rates. As housing starts have been declining since the start of 2018, construction investment by households is set to decrease in 2019, before recovering in 2020 thanks to strong gains in purchasing power and employment. Exports are expected to continue to enjoy robust growth, albeit a touch below the 2018 level due to the less favourable international environment.

These growth forecasts are similar to those of the main national and international bodies. In its March 2019 publication, the Banque de France forecasts growth of 1.4% in 2019 and 1.5% in 2020. The Consensus Forecasts of March 2019 predicts growth of 1.3% p.a. for the two years. The European Commission's growth forecasts for France stand at 1.3% for 2019 and 1.5% for 2020 (not adjusted for working days). The OECD projects growth of 1.3% p.a. for 2019 and 2020. In its January 2019 publication, the IMF (whose forecasts are not adjusted for working days) expects growth of 1.5% in 2019 and 1.6% in 2020.

PRELIMINARY DATA POINT TO ROBUST GROWTH FOR THE FRENCH ECONOMY IN EARLY 2019.

The French economy grew by 1.6% in 2018, driven by foreign trade and business investment. In 2018, both exports and investment were very resilient despite the slowdown in global economic growth. However, household consumption was less dynamic, notably due to the dampening effect of higher oil prices. Growth was not as strong as in 2017, when France's economic performance was boosted by a very upbeat international environment and a few positive one-offs (such as a very sharp increase in property transactions and a recovery in the tourism sector after terrorist attacks in previous years).

In the third and fourth quarters, the GDP growth rate (0.3% per quarter) was slightly higher than at the start of 2018 (growth of 0.2% per quarter for the first and second quarters). France's economic growth was more robust than that of the euro area in the second half of 2018. In the fourth quarter, exports enjoyed a very sharp acceleration, thanks to a large number of Airbus deliveries in December, as well as the delivery of the Celebrity Edge cruise ship in October. Business investment continued to grow, but at a slower pace than in the third quarter (which was exceptionally strong due to significant investments in vehicle fleets prior to new standards taking effect in the automotive industry on 1 September 2018). Despite a substantial boost to purchasing power from the government's measures to reduce residence tax and to cut employee social security contributions, household consumption was flat in the fourth quarter, as mild weather and the "gilets jaunes" protests dampened consumer spending.

Preliminary data point to dynamic growth in the first part of 2019. Business surveys by Insee, Markit and the Banque de France have recovered and were hovering near their medium-term averages at the beginning of the year. In March, the PMI declined, but Insee's business climate indicator improved for the third month in a row. Household confidence also increased in March for the third consecutive month, recovering to its level before the protest movement began. Growth in the first quarter of 2019 is set to be driven by household consumption, which is expected to have rebounded thanks to the set of measures implemented to boost workers' incomes. Business investment is likely to have returned to its previous robust trend, as suggested by the current strong momentum in new vehicle registrations for professional fleets, and against a backdrop of buoyant investment in services for the past several quarters. However, foreign trade is likely to provide less support due to both a slowdown in exports (following a large number of aircraft deliveries at end 2018) and a dynamic import trend (owing to a recovery in demand).

TABLE 1: MACROECONOMIC SCENARIO 2018-2022

Annual growth rate (in %)	2018*	2019	2020	2021	2022
Gross domestic product**	**1.6**	**1.4**	**1.4****	**1.4**	**1.4**
Household consumption expenditure	0.8	1.7	1.4	1.4	1.4
General government consumption expenditure	1.1	1.0	1.0	0.5	0.2
Gross fixed capital formation (GFCF)	2.9	2.1	1.4	1.2	1.6
o.w. non-financial corporations	*3.9*	*2.8*	*2.5*	*2.1*	*1.7*
Contribution to real GDP growth of changes in inventories	−0.4	−0.1	0.0	0.0	0.0
Contribution to real GDP growth of external balance of goods and services	0.6	0.0	0.1	0.2	0.2
Imports	1.3	2.4	2.3	2.3	2.3
Exports	3.3	2.4	2.7	3.1	3.1
GDP deflator	0.9	1.2	1.2	1.5	1.7
Household consumption deflator	1.7	1.3	1.3	1.5	1.75
Wages and salaries (non-farm business sector)	3.5	3.1	2.9	3.1	3.4
Wages and salaries per employee (non-farm business sector)	1.9	2.3	2.1	2.7	3.0
Employment, persons (non-farm business sector)	1.6	0.9	0.7	0.5	0.4

* Quarterly national accounts (detailed figures) for the fourth quarter of 2018

** According to Insee, the calendar effect is set to have a +0.1% effect on GDP growth in 2020, i.e. gross GDP growth of 1.5%.

GLOBAL GROWTH WAS A ROBUST 3.7% IN 2018, BUT IS EXPECTED TO SLOW TO 3.4% P.A. IN 2019 AND 2020, LED BY THE ADVANCED COUNTRIES.

The euro area slowdown is expected to continue in 2019. Apart from temporary factors, this slowdown is attributable to a slump in world demand, considerable uncertainty weighing on investment and consumption, and the end of the post-crisis catch-up effect. In 2019, growth is expected to be particularly lacklustre in Italy (0.2%) and in Germany (0.8%), which are both more affected by these factors than Spain (2.3%) or France (1.4%). Euro area GDP is seen up 1.3% in 2019, following growth of 2.5% and 1.8%, respectively, in 2017 and 2018. Thereafter, euro area growth is expected to rebound slightly in 2020 (to 1.4 %), as the economies of its major trading partners return to normal and uncertainty levels off.

US economic growth is expected to decline slightly in 2019, given pressures on the labour market and the roll-out of protectionist measures, before slowing more substantially in 2020 as fiscal stimulus tapers off. **In the United Kingdom, growth is likely to be sluggish,** with Brexit-related uncertainty dampening the growth trend. **In Japan,** growth is set to be moderate in 2019 due to a slump in Chinese demand, followed by even weaker growth in 2020 as the Japanese government raises its VAT rate.

In the main emerging economies, activity is generally expected to remain upbeat. Growth should be strong in India, but China is set for a soft landing as deleveraging measures – not to mention the trade dispute with the United States – begin to take a toll. Turkey, which is already in recession, is expected to see its GDP decline in 2019, followed by a recovery in 2020. Both Brazil and Russia should post modest economic recoveries.

Growth in world trade slowed markedly to 4.5% in 2018 (after 5.8% in 2017). It is expected to continue to slow in 2019 (world trade growth forecast at around 3% p.a. in 2019 and 2020). The slowdown in global growth and the threats to international trade agreements are both likely to continue to impact world trade. Oil-producing countries and especially China are expected to see a slump in imports. Chinese imports, in particular, will be affected by protectionist measures and a slowing economy. Weaker growth in the US is also set to have a clear impact on world trade flows. Conversely, world trade is expected to benefit from the Turkish economy recovering from recession in 2020.

World demand for French exports is expected to follow a similar trend over the forecast period. World demand for French exports is expected to slow to +2.7% in 2019 (after +3.7% in 2018), followed by a slight recovery to +2.9% in 2020. The French export sector underperformed world trade in 2018 as it was more exposed to the slump in Europe. However, in 2019 and 2020, French exports should be less exposed to the slowdown in trade in the US and Asia.

THE WORLD ECONOMY IS POISED TO SUPPORT FRANCE'S ECONOMIC GROWTH.

In 2018, foreign trade made the strongest contribution to France's GDP growth since 2012 (a positive 0.6-point effect on GDP growth). Growth of exports outpaced that of imports (3.3% vs. 1.3%), due notably to a decline in service imports. Goods exports were resilient despite the euro's appreciation in 2018; they were driven by a large number of deliveries of transportation equipment and by a recovery in farm exports after two unfavourable years for the French agricultural sector. Contrary to the other European countries, French export performance is not expected to have weakened in 2018, with this stronger export performance driving gains in relative market share.

French exports are expected to remain dynamic in 2019 and 2020 (growth of 2.4% and 2.7%, respectively), albeit less so than in 2018 due to the slowdown in global demand (+2.7% in 2019 and +2.9% in 2020 after +3.7% in 2018).

French imports are set to be less dynamic than exports and in line with their usual determinants (import growth is forecast at 2.4% in 2019 and 2.3% in 2020, after 1.3% in 2018). The acceleration expected in 2019 reflects a consumption-driven recovery in final demand (demand growth expected at 1.6% in 2019 vs. 1.4% in 2018). This forecast assumes that the service import trend gradually reverts to normal following the sharp decline in service imports in 2018.

France's trade balance is expected to improve in 2020 after being virtually unchanged in 2019, assuming flat oil prices. The continued strong momentum in global demand and the improvement in France's cost-competitiveness are set to improve the trade balance in 2020, with foreign trade contributing positively to GDP growth.

HOUSEHOLD CONSUMPTION IS LIKELY TO GATHER PACE IN 2019 AND 2020.

French households' purchasing power grew by 1.0% in 2018, and is expected to strengthen significantly in 2019 (up 2.0%). This trend is notably underpinned by tax cuts. Purchasing power will be supported by measures included in the budget bills (notably the second round of residence tax cuts and the full-year effect of the reduction in employees' social security contributions). It should also be strongly boosted by the measures announced at the end of the year: reduced CSG for pensions less than €2,000/month, zero social security contributions and income tax on overtime pay as from 1 January, and a €100/month increase in income at minimum wage level via the in-work benefit. Wages will also be buoyed by a provision whereby employers can pay an exceptional bonus, exempt from social security contributions, by the end of the first quarter of 2019. Moreover, indirect taxation measures should have a less negative effect on purchasing power than in 2018. In addition, income from work is expected to continue to be upbeat thanks to vigorous employment and wage growth, whereas oil prices should not have the same negative effect on purchasing power as in 2018. In 2020, purchasing power is expected to rise by 1.0%, similar to the growth trend, as wage growth and higher employment continue to drive income from work upward.

In 2019, household consumption is likely to grow sharply (by 1.7% after 0.8% in 2018), thanks to the strong purchasing power gains resulting from government policy. Given this sharp increase in purchasing power, households are likely to smooth their consumption somewhat, with the household savings rate rising temporarily in 2019, then returning to its 2018 level of 14.4%.

HOUSEHOLD INVESTMENT IS SET TO DIP TEMPORARILY IN 2019, THEN RECOVER.

Household investment slowed in 2018 (up 1.8% after 5.6% growth in 2017) and is expected to dip a slight 0.5% in 2019, before recovering in 2020 (up an estimated 1.0%). Housing starts are set to recover in 2019, with support from the expected purchasing power gains and employment growth. However, construction investment is not expected to recover until 2020, as construction expenditure is recorded gradually as a construction project is completed.

BUSINESS INVESTMENT IS SET TO REMAIN DYNAMIC OVER THE FORECAST PERIOD.

Despite less vigorous economic growth in 2018, business investment maintained strong momentum (up 3.9%), thanks notably to investment in services. Business investment is expected to continue to support economic growth in 2019 and 2020 (with expected increases of 2.8% in 2019 and 2.5% in 2020). The business investment rate currently stands at a record high level and is set to gradually revert to normal as interest rates rise.

HEADLINE INFLATION IS SET TO DECREASE TO 1.3% P.A. IN 2019 AND 2020 DUE TO LESS DYNAMIC VOLATILE COMPONENTS.

In 2019, core inflation is set to accelerate to 1.1% after 0.8% in 2018, driven by higher inflation in the services sector due to wage growth. Core inflation is also expected to be underpinned by higher food prices owing to the rise in commodity prices. **However, headline inflation is expected to decrease to 1.3% in 2019, vs. 1.8% in 2018,** mainly due to lower oil prices and no additional energy taxes (after contributing +0.6 pt to the CPI in 2018, the petroleum products component is expected to have zero effect in 2019). Government-controlled prices are expected to contribute +0.3 pt to inflation in 2019, less than in 2018, as tobacco price hikes will have less of an impact in 2019.

In 2020, core inflation is expected to increase to 1.2%, with a sharper increase in private-sector services prices partly offset by past food inflation fading out of year-on-year figures. This level of core inflation is consistent with French economic growth slightly above the potential growth rate. **Headline inflation is expected to be stable at 1.3% in 2020.** In the absence of energy tax hikes, petroleum prices are again expected to have a nil effect on inflation, whereas government-controlled prices are set to have a lower inflationary effect, in connection with the "100% Santé" agreement with the healthcare sector (aimed at reducing out-of-pocket health-related expenses and notably including a reduction in the price of eyeglasses).

MARKET-SECTOR JOB CREATIONS ARE EXPECTED TO GRADUALLY CONVERGE WITH PRODUCTIVITY GAINS.

Market-sector employment trends were very strong again in 2018, with an annual average of 241,000 new jobs created, continuing the strong job creation trend of the second half of 2017 and despite less dynamic economic growth.

In 2019, market-sector job creations are expected to be substantial (an estimated annual average of 145,000 new jobs), but not as strong as in 2018, as productivity gains begin to revert to their underlying trend.

In 2020, market-sector job creations are expected to total an annual average of 125,000. Labour productivity growth is expected to continue to revert to its previous level, but the job market is likely to be boosted by measures to reduce the overall tax burden and by the Skills Investment Plan (Plan d'investissement dans les compétences, PIC).

Non-market sector employment, after a slight decline in 2018 (an annual average decline of 14,000 jobs), is expected to level off in 2019 and increase very slightly in 2020 (an annual average of 10,000 new jobs). Despite the continued reduction in funding for subsidised contracts in 2018, hiring in the non-market private sector is expected to remain upbeat.

With total new job creations of 155,000 in 2019 and 145,000 in 2020, the unemployment rate is expected to continue to decline gradually.

2.2. MEDIUM-TERM OUTLOOK (2021-2022)

GROWTH SHOULD REMAIN AT A SOUND 1.4% P.A. IN 2021 AND 2022.

French GDP is expected to grow by 1.4% p.a. in 2021 and 2022. Inflation is forecast at 1.5% in 2021 and 1.75% in 2022. The negative output gap that has characterised the French economy since 2012 is expected to close in 2020. Economic growth is expected to be close to the potential growth rate in 2021 and 2022. Inflation is set to increase gradually, in line with the European Central Bank's medium-term inflation target.

THIS SCENARIO IS SUBJECT TO MAJOR UNCERTAINTIES – BOTH DOMESTICALLY AND INTERNATIONALLY.

The magnitude of the euro area slowdown, the implementation of protectionist measures in the US, the terms for Brexit, whether China experiences a soft or hard landing, the economic policy trends both in advanced countries (the US, Spain, Germany and Italy) and in emerging countries (Brazil), and financial uncertainty in the US and emerging countries – all these factors represent major sources of uncertainty. Our economic scenario assumes that oil prices and the euro's exchange rate will remain unchanged at recent levels, which may support or dampen economic activity.

There are uncertainties specific to France in addition to these international uncertainties.

The outlook for business investment in France is uncertain. In light of very favourable financing conditions, the strong business investment momentum could continue if supply-side pressures persist. The conversion of the CICE into a permanent reduction in social security contributions, which involves a double cash payment to companies in 2019, could also boost investment temporarily. This could potentially prompt companies to give pay rises, with a positive knock-on effect on consumption.

Conversely, business investment could revert to its underlying trend more rapidly than expected after several years of strong growth, given high corporate debt levels. Another factor of uncertainty is how companies and investors will react to Brexit.

Moreover, the household savings rate – which increased at the end of 2018 – might take longer than expected to revert to its normal level.

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

The Stability Programme's scenario is close to the European Commission's latest forecasts in terms of both the growth rate and growth drivers. In its February 2019 Winter Forecasts, the Commission projects growth of 1.3% in 2019 after 1.5% in 2018, followed by a slight acceleration to 1.5% in 2020[2].

According to the Commission, activity should be mainly upheld by domestic demand and investment, with the latter continuing to be above the growth rate. However, the details of the macroeconomic scenario for the Winter Forecasts have not been communicated.

The European Commission's inflation forecast, expressed in terms of the harmonised price index, stands at 1.4% for 2019, as in the Stability Programme, followed by an acceleration to 1.7% in 2020 (whereas the Stability Programme's scenario forecasts stable inflation in 2020).

BOX 2 – CALENDAR EFFECT ON GROWTH

All the growth figures used in the macroeconomic scenario are adjusted for the calendar effect. Gross GDP growth forecasts are presented before and after adjustment for the number of working days. After 2018, for which Insee has published an initial estimate, the public finance ratios in the Stability Programme are based on growth forecasts adjusted for the number of working days.

BOX 3 – DATA PRESENTED FOR 2018

The data presented for 2018 are those appearing in the Detailed Results of the quarterly national accounts for the fourth quarter of 2018, published by Insee on 26 March 2019. Because of the sequential procedure used for the provisional account, which results in public finance data being published in advance, the public demand line items in the quarterly Detailed Results differ from information relating to public finances in Insee's provisional general government account.

For example, according to the quarterly accounts, public investment appears to have increased in 2018 by 3.3% in nominal terms and by 0.9% in real terms. These figures (3.3% and 0.9%) are used in the macroeconomic scenario. However, the initial estimates of the general government national accounts, published by Insee on 26 March 2019, show an increase of 3.9% in nominal terms in 2018.

The national account data to be published by Insee in May will be fully consistent with the figures in the provisional

[2] Figures not adjusted for working days.

3.

FISCAL STRATEGY

Fiscal strategy

3.1 OVERALL STRATEGY

The general government deficit stood at 2.5% of GDP in 2018, marking the first time in more than a decade that France's deficit has been under 3% of GDP for two consecutive years. This confirms France's commitment to fiscal consolidation after exiting the Excessive Deficit Procedure in the third quarter of 2018.

The French Government adopted a series of bold measures in 2018 to meet citizens' expectations in terms of purchasing power and social justice, to address the economic and social emergency, and to maintain our transformative action (see Box 4). The measures, totalling more than €10 billion, mainly correspond to an acceleration of commitments slated for the period from 2019 to 2022. They have been partially funded by discretionary revenue measures, such as the tax on digital services and a one-year delay in lowering the corporate income tax rate for large corporations, along with savings of €1.5 billion in the current year, for a total of €4 billion. These measures do not jeopardise the government's 2019-2022 fiscal strategy. As it enters the second half of its five-year term, the Government will continue its effort to reduce the general government deficit by containing expenditure. It will also continue cutting taxes on work and investment to sustain France's long-term economic growth.

In addition to the fiscal impact of the emergency measures, the path set out in this Stability Programme factors in growth prospects that are less favourable than expected in the interest of prudence and sincerity. These macroeconomic forecasts, which assume a less favourable international environment, have a direct impact on the path of the headline deficit and debt reduction, which automatically slows down when GDP growth does. Yet, they do not alter the continuation of the government's economic reforms to boost growth and jobs.

The 2018 deficit was again under the threshold of 3% of GDP, standing at 2.5% of GDP, compared to 2.8% in 2017 and 3.5% in 2016. This good outturn stems in part from effective containment of nominal expenditure growth, excluding tax credits, which stood at 1.3%, sharply lower than the 2.4% growth posted in 2017. Real expenditure decreased by 0.3%, for the first time in several decades. The structural adjustment of +0.2 percentage points of GDP was larger than projected in the Initial Budget Act: a major effort on expenditure, which contributed 0.4 percentage points of potential GDP, improved the deficit and funded a cut of 0.2 percentage points of GDP in aggregate taxes and social security contributions, as projected in the 2018 Budget Acts.

In 2019, the deficit should stand at 3.1% of GDP, as the Competitiveness and Employment Tax Credit (CICE) is replaced by a cut in employers' social security contributions, reducing the balance in the national accounts by 0.8 percentage points of GDP. This small breach of the 3% threshold will be temporary and exceptional. **Without the replacement of the CICE, the public deficit would shrink to 2.3% of GDP in 2019, with the major containment of government expenditure growth at 1.6% in nominal terms, excluding the national vocational training authority (France Compétences), and 0.4% in real terms.** Expenditure efforts would still make a positive contribution of 0.3 percentage points of GDP, stemming in part from limited increases in pensions and certain benefits, further savings on housing benefits and subsidised employment contracts, and local governments' compliance with their contracts with central government. In addition, the Government has committed itself to producing up to €1.5 billion in savings provided for under this path, compared to the total expenditure passed in the Initial Budget Act. These savings will offset the cost of emergency measures, such as the increase in the in-work benefit. This target compares to the €4 billion in appropriations allocated to reserves under the 2019 budget and the €1.4 billion in underspending under the central government expenditure growth benchmark in 2018. Central government and general government as a whole should continue to enjoy favourable borrowing terms for debt service. **Aggregate taxes and social security contributions will continue to decrease,** even after the replacement of the Competitiveness and Employment Tax Credit, in light of this new expenditure effort, measures to eliminate taxes and social security contributions on overtime pay, the full-year effect of the switch from social security contributions on wages to the General Social Security Contribution (CSG) and the reversal of the increase in the CSG for certain pensioners, along with the second phase in the elimination of the residence tax. The aggregate tax and social security contribution rate will fall to 44.0% of GDP (43.8% excluding France Compétences), down from 45.0% in 2018.

In 2020, the public deficit should shrink by 1.1 percentage points of GDP to stand at 2.0% of GDP. Expenditure growth will be contained at 1.6% in nominal terms, excluding France Compétences, and 0.6% in real terms. This represents a further expenditure savings effort of 0.4 percentage points of GDP. Central government expenditure growth should be contained and produce a further decrease in debt service. Local government expenditure growth should slow sharply, in keeping with the local elections cycle. The national healthcare expenditure target (Ondam) should be limited to 2.3% and the unemployment insurance scheme (Unédic) should see its finances start to improve under the guidelines given to management and labour representatives. Continued containment of expenditure will make new tax and contribution cuts possible for households and corporations, including the third stage of the elimination of the residence tax for the 80% of the households with the lowest incomes. This adjustment path does not factor in the sharp increase in fuel taxes. Nevertheless, as a result of a rebound after the replacement of the Competitiveness and

Employment Tax Credit, the aggregate tax and social security contribution rate will rise back up to 44.4% of GDP in 2020 (or 44.1% excluding France Compétences).

The Government will continue its strategy to contain public expenditure and reduce taxes and contributions until 2022. The Government will continue its efforts to contain government expenditure growth to achieve an average expenditure growth rate of 0.2% in real terms between 2018 and 2022 (on a like-for-like basis), which is much lower than the 1.2% average growth rate from 2008 to 2017, after the financial crisis. The expenditure efforts will concern general government as a whole and lead to a decrease of nearly 3 percentage points in the government expenditure ratio over the government's five-year term (on a like-for-like basis, or 2.7 percentage points including the impact of France Compétences). Local governments will continue their efforts to contain operating expenditure growth, under the terms of their financial pact with central government. This pact proved to be effective in 2018. The adjustment path projects containment of healthcare expenditure growth over the government's five-year term, with a national healthcare expenditure growth target of only 2.3% up until 2022. At the same time, pending reforms of unemployment insurance and lower unemployment will improve the finances of the unemployment insurance scheme (Unédic). This reduction of government expenditure is critical, not only for making government action more effective, but also for financing cuts in taxes and social security contributions. **The decrease in the aggregate tax and social security contribution rate will continue to reach 44.0% of GDP in 2022** (or 43.8%, excluding France Compétences, representing a cut of 1.4 percentage points of GDP over the government's five-year term). The lower rate will benefit both corporations and households, especially the continuing cuts in the corporate income tax rate, bringing it down to 25% in 2022, which is the average rate in the European Union countries, and the further steps to eliminate the residence tax for all households, except for those with secondary homes.

The 2018-2022 Public Finance Planning Act set a medium-term objective (MTO) of achieving a structural deficit of 0.4% of potential GDP. The pace of adjustment had to be adapted temporarily, compared to the path set out in the Public Finance Planning Act, in order to fund the emergency measures passed. This adaptation is critical to produce positive effects for medium-term potential growth and fiscal sustainability. It is also a limited amendment: structural adjustment will remain strictly positive in 2019 and 2020, with an improvement of 0.1 percentage points of GDP, rising to 0.3 percentage points of GDP in 2021.

After remaining steady in 2018, for the first time since 2007, the government debt-to-GDP ratio will increase slightly in 2019 as a result of one-offs and then continue decreasing for the rest of the government's five-year term. The replacement of the Competitiveness and Employment Tax Credit with a permanent cut in social security contributions should bring the debt ratio up to 98.9% of GDP in 2019, with the double cost incurred in the transition year. After that, the ratio should fall until it reaches 96.8% in 2022. This would represent a decrease of 2 percentage points of GDP over the government's five-year term.

TABLE 2: ADJUSTMENT PATH

	2017	2018	2019	2020	2021	2022
General government balance and structural analysis						
General government balance	**-2.8**	**-2.5**	**-3.1**	**-2.0**	**-1.6**	**-1.2**
Nominal adjustment	*0.8*	*0.2*	*-0.6*	*1.1*	*0.4*	*0.4*
Cyclical balance	-0.3	-0.2	-0.1	0.0	0.0	0.1
One-offs (as a % of potential GDP)	-0.1	-0.2	-1.0	-0.1	0.0	0.0
Structural balance (as a % of potential GDP)	-2.4	-2.1	-2.1	-1.9	-1.6	-1.3
Structural adjustment	*0.2*	*0.2*	*0.1*	*0.1*	*0.3*	*0.3*
Main aggregates						
Government expenditure ratio (excluding tax credits)	**55.0**	**54.4**	**54.0***	**53.5***	**53.0***	**52.3***
Nominal public expenditure growth, excluding tax credits (%)	*2.4*	*1.3*	*1.9**	*1.7**	*1.7*	*1.9*
Real public expenditure growth, excluding tax credits (%)	*1.4*	*-0.3*	*0.8**	*0.7**	*0.3*	*0.1*
Tax and social security contributions rate, net of tax credits	**45.2**	**45.0**	**44.0***	**44.4***	**44.2***	**44.0***
General government debt						
General government debt	**98.4**	**98.4**	**98.9**	**98.7**	**98.1**	**96.8**
excluding financial assistance for the euro area	95.5	95.6	96.2	96.1	95.5	94.3

*Absent the impact of creating France Compétences on expenditure and revenue, with increases of €4.6 billion in 2019 and €1.5 billion in 2020, the government expenditure ratio would stand at 53.8 percentage points of GDP in 2019 and 53.3 percentage points of GDP in 2020, and the ratio of aggregate taxes and social security contributions would stand at 43.8 percentage points of GDP in 2019 and 44.1 percentage points of GDP in 2020. This restatement would lower these two ratios by about 0.2 percentage points until 2022.

At the same time, government expenditure growth in real terms, excluding tax credits, would stand at 0.4% in 2019 and at 0.6% in 2020 (or 1.6% in both years in nominal terms).

BOX 4 – EMERGENCY ECONOMIC AND SOCIAL MEASURES

The President of the French Republic announced a series of measures to address France's economic and social emergency on 10 December 2018:

- Reversal of the increase in fuel taxes;
- An increase of €100 per month in the income of households earning the minimum wage, with a €90 increase in the maximum level of the in-work benefit bonus: along with the regulatory increase in the minimum wage on 1 January 2019, this exceptional increase means that people receiving the in-work benefit and earning the minimum wage will see their monthly disposable income rise by €100 in 2019.

These two measures were passed as part of the 2019 Initial Budget Act. The exceptional increase in the in-work benefit was implemented by the Decree of 21 December 2018. Three other emergency measures, explained below, were enacted as part of the Emergency Economic and Social Measures Act, passed on 24 December 2018:

- All employees and civil servants will be exempted from social security contributions and income tax on net taxable overtime pay up to €5,000 per year, starting on 1 January 2019. For employees earning net monthly wages of €1500 and working overtime, this represents a gain of €455 per year, based on the average number of overtime hours shown by the data for 2015.
- All companies are able to pay an exceptional bonus to employees earning less than three times the minimum wage (up to €3,600 per month). The bonus is exempt from income tax and all statutory and contractual contributions. There was a time limit on this measure. Companies were required to pay the bonus by 31 March 2019.
- Reversal of the 1.7-percentage-point increase in the General Social Contribution on net retirement pensions of less than €2,000 per month for a single person (base taxable income of €22,580 for a single adult under the age of 65 with no other source of income). For the 3.8 million households concerned, representing some 5 million pensioners, the contribution rate will remain at 6.6% in 2019. All in all, nearly 70% of tax households with one or more pensioners are now exempt from the increase in the contribution rate.

These measures represent an added cost of more than €10 billion compared to the adjustment path presented in October 2018. Back in December, the government sought to offset part of the cost with a series of measures that would improve public finances by nearly €4 billion. These measures were first included in the Initial Budget Act, with further tightening of tax expenditure on capital gains realised on intragroup transfers. Other measures were included in the bill submitted by the Minister for the Economy and Finance on 6 March 2019, which will introduce a tax on digital services and amend the phased reduction of the corporate income tax rate. Finally, further savings will be achieved on the central government budget in the current year.

3.2 OUTTURN 2018

On 26 March 2019, the French national institute of statistics and economic studies (Insee) published the preliminary general government accounts, which showed a deficit of 2.5% of GDP in 2018, compared to 2.8% in 2017 and 3.5% in 2016. This improvement was made possible by containing expenditure growth at 1.3% in nominal terms, excluding tax credits, which reduced the deficit. At the same time, discretionary tax measures in the 2018 Budget Acts reduced the aggregate tax and social security contribution rate for households and corporations.

The general government deficit shrank by one quarter of a percentage point of GDP. The deficit of central government and its agencies actually grew slightly to reach a level €2.1 billion higher than in 2017, but this was more than offset by an improvement in the balance of social security funds of €5.4 billion and local government of €0.7 billion.

In real terms, government expenditure decreased by 0.3%. Strong expenditure execution by central government and slower growth of social security and local government expenditure helped to contain public expenditure growth and reduce its share of GDP from 55.0% in 2017 to 54.4% in 2018, excluding tax credits. Expenditure growth also turned out to be slower than expected when the 2019 budget was being drafted. At that time, public expenditure growth was expected to reach 1.6% in nominal terms. This slower growth was explained by the outturn under the central government discretionary expenditure benchmark, which was €1.4 billion under the figure set in the 2018 Initial Budget Act, along with slower growth of social security expenditure.

In 2018, the aggregate tax and social security contribution rate stood at 45.0% of GDP, compared to 45.2% in 2017. The lower rate is the result of discretionary revenue measures that cut taxes and social security contributions by €10 billion. This cut was partially offset by strong revenue growth that outstripped GDP growth, with aggregate tax elasticity of 1.2. This growth stemmed from increased revenue from corporate and personal income tax, as a result of strong incomes in 2017, when France's economic growth was solid.

3.3. STRUCTURAL BALANCE

The general government deficit shrank from 2.8% of GDP in 2017 to 2.5% in 2018. This change results from structural adjustment of 0.2 percentage points of GDP, stemming from an equivalent structural effort. Expenditure efforts made a positive contribution of slightly more than 0.4 percentage points of GDP. This was the result of government expenditure growth of 1.3% in nominal terms, excluding tax credits, whereas potential GDP growth was estimated at 2.2% in nominal terms[3]. Some of this expenditure effort has helped fund measures to cut the aggregate tax and social security contribution rate by up to 0.2 percentage points of GDP. The correction for the accrual-based measurement of tax credits has virtually no effect on the measurement of this effort. The contribution of variations in non-discretionary revenue to structural adjustment was neutral, since the decrease in the non-tax revenue ratio was more than offset by the effect of tax elasticity to GDP growth. This elasticity was greater than one, standing at 1.2. Finally, the actual 1.6% GDP growth rate outstripped the potential rate of 1.25%. This led to a cyclical improvement in the headline deficit of 0.2 percentage points of GDP. But this improvement should be wholly offset by the negative contribution of 0.2 percentage points of GDP from one-offs, as the exceptional corporate income tax payment set in 2017 was not renewed.

In 2019, the general government deficit should deepen by 0.6 percentage points of GDP compared to 2018, reaching 3.1% of GDP. This deterioration should be entirely attributable to one-offs, which will make a negative contribution of 0.7 percentage points of GDP. This will be only partially offset by positive contributions from cyclical developments (0.1 percentage points of GDP) and improvement of the structural balance (0.1 percentage points of GDP). One-offs should include the double cost of replacing the Competitiveness and Employment Tax Credit with permanent cuts in social security contributions, which should come to 0.85 percentage points of GDP. This cost will be counterbalanced by a positive contribution of 0.15 percentage points of GDP resulting from the end of payments linked to the 3% dividend tax dispute. Absent the impact of this replacement, the general government deficit would be equivalent to 2.3% of GDP in 2019. The cyclical balance should improve as a result of 1.4% GDP growth in real terms, compared to the potential growth rate of 1.25%. The structural adjustment of 0.1 percentage points of potential GDP should be achieved through a structural effort, which should also be equivalent to 0.1 percentage points of GDP. Expenditure growth, excluding tax credits, as restated for France Compétences, should be faster than it was in 2018, standing at 1.6% in nominal terms in 2019[4]. This faster growth stems in part from the increase in the in-work benefit. With potential growth expected at 2.5% in nominal terms, the expenditure effort should be equivalent to 0.3 percentage points of GDP. On the revenue side, discretionary tax measures (excluding one-offs), should make a negative contribution of 0.3 percentage points of GDP to structural adjustment, after restatement for France Compétences, while the variation in the correction for accrual-based measurement of tax credit refunds should make a positive contribution of 0.1 percentage points of GDP[5]. The non-discretionary component is expected to be neutral overall in terms of structural adjustment.

In 2020, the general government deficit should shrink by 1.1 percentage points of GDP to 2.0% of GDP. This will be the result of a rebound after paying the double cost of replacing the Competitiveness and Employment Tax Credit and other one-offs, contributing 0.9 points, further cyclical improvements, contributing 0.1 points, and structural improvements, contributing another 0.1 points. Structural adjustment should be achieved by means of an expenditure effort equivalent to 0.4 percentage points of GDP, after restatement for France Compétences, with growth of public expenditure, excluding tax credits, standing at 1.6% in nominal terms[6], compared to potential GDP growth of 2.5% in nominal terms. Discretionary tax measures, excluding one-offs, should make a negative contribution of 0.5 percentage points of GDP to the effort, after restatement for France Compétences. However, when measured in terms of their impact on the deficit, their negative contribution is only 0.2 points, since the correction for accrual-based measurement of tax credit refunds makes a positive contribution of 0.3 percentage points of potential GDP (see 9.2 Methodological Annex on Calculating Structural Adjustment)[7]. Nevertheless, the impact of the expenditure effort should be weakened by the effects of lower non-tax revenues in the non-discretionary component, making a negative contribution of 0.1 percentage points of GDP.

In 2021 and 2022, the structural adjustment path should be steeper than in 2019 and 2020, at 0.3 percentage points of GDP each year. The headline deficit should improve by 0.8 percentage points of GDP between 2020 and 2022, including a 0.7-point contribution from the improvement in the structural balance and a 0.1-point improvement in the cyclical balance. This means the structural deficit should be equivalent to 1.3% of potential GDP in 2022. The real

[3] Expenditure growth of 1.4%, excluding one-off expenses, along with a slightly smaller loss resulting from the 3% dividend tax dispute in 2018 compared to 2017.

[4] Or 1.9% excluding one-offs.

[5] This will be the result of the Competitiveness and Employment Tax Credit rate falling from 7% to 6% for refunds paid in 2018.

[6] Or 1.7 % excluding one-offs.

[7] By convention, expenditure one-offs are restated under expenditure efforts, while revenue one-offs are restated under revenue efforts as revenue from discretionary tax measures. However, the impact of the revenue one-off representing the replacement of the Competitiveness and Employment Tax Credit can be seen both in discretionary tax and contribution measures and in the correction for accrual-based measurement of tax credits. This means that it is the sum of the revenue effort and the effort in the correction for accrual-based measurement of tax credits that needs to be considered.

economic growth rate over this period should be steady at 1.4% and the potential growth rate should start to pick up slightly in 2021 to stand at 1.35% in 2022. Average expenditure growth in real terms should stand at 0.2% in 2021 and 2022, representing an average expenditure effort of 0.6 percentage points of GDP. This expenditure effort will make it possible to cut taxes further, in keeping with the target of lowering the corporate income tax rate to 25% by 2022 and eliminating the residence tax on primary residences. These tax cuts should lessen the pace of structural adjustment.

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

(en % du PIB)	2018	2019	2020	2021	2022
General government balance (1)	**-2.5**	**-3.1**	**-2.0**	**-1.6**	**-1.2**
Nominal adjustment	0.2	-0.6	1.1	0.4	0.4
Cyclical balance (2)	**-0.2**	**-0.1**	**0.0**	**0.0**	**0.1**
One-offs (as a % of potential GDP) (3)	**-0.2**	**-1.0**	**-0.1**	**0.0**	**0.0**
Structural balance (as a % of potential GDP) (1)-(2)-(3)	**-2.1**	**-2.1**	**-1.9**	**-1.6**	**-1.3**
Structural adjustment	0.2	0.1	0.1	0.3	0.3
Structural effort	0.2	0.1	0.2	0.3	0.3
Discretionary revenue measures	*-0.2*	*-0.1**	*-0.4**	*-0.2*	*-0.2*
Expenditure effort	*0.4*	*0.1**	*0.3**	*0.5*	*0.6*
Correction for accrual-based measurement of tax credits	*0.0*	*0.1*	*0.3*	*-0.1*	*-0.1*
Non-discretionary component	0.0	0.0	-0.1	0.0	0.0

* Absent the impact of creating France Compétences on expenditure and revenue, with increases of €4.6 billion in 2019 and €1.5 billion in 2020, the **expenditure effort** would stand at **0.3 percentage points of GDP in 2019 and 0.4 percentage points of GDP in 2020**, and the contribution of **discretionary revenue measures** to the structural effort would stand at - **0.3 percentage points of potential GDP in 2019 and - 0.5 percentage points of potential GDP in 2020**.

BOX 5 - ONE-OFFS TAKEN INTO ACCOUNT WHEN EVALUATING FRANCE'S STRUCTURAL BALANCE

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

In response to a request from the High Council on Public Finance, the report appended to Public Finance Planning Acts since the 2014-2019 Act sets out the government's rules on one-offs and proposes a set of criteria to define one-offs. This is true of the 2018-2022 Public Finance Planning Act in particular.

On the revenue side, the timing for recognition of losses stemming from exceptional tax disputes in the national accounts cannot be foreseen because it depends on the timing and outcome of the proceedings and the courts' final rulings. These losses have been classified as one-offs[8]. The on-going disputes involve refunds to foreign UCITS, refunds relating to the Ruyter[9], Stéria[10], Messer[11], Précompte disputes and the disputed 3% tax on dividends (which has been recognised as an expense rather than a reduction in revenue in Insee's provisional 2017 accounts, published in March 2018). The exceptional corporate income tax payment for large corporations in 2017 has also been included in one-offs, since it was not foreseen when the Public Finance Planning Act was drafted. Moreover, it relates to a dispute and it has a significant

8 Expenditure and revenue are recorded on an accrual basis in the system of national accounts, except in special cases, in compliance with the European System of Accounts of 2010. This means they are recorded, "when economic value is created, transformed or extinguished, or when claims and obligations arise, are transformed or are cancelled" §1.101. Consequently, losses stemming from tax disputes will be recorded in the year when the courts make their final rulings, which correspond to liabilities. On the other hand, the losses will be recorded in budgetary accounting on the basis of cash receipts or disbursements, which may occur before or after the courts hand down their final rulings.

9 Dispute concerning French social security contributions under European Union law.

10 Dispute concerning dividends received from European subsidiaries.

11 In its ruling of 25 July 2018, the CJEU found that the contribution to the public electricity service (CSPE), as it stood prior to 2016, could not have objectives of territorial and social cohesion, or administrative objectives.

impact on the balance for one year and no lasting impact in the future. Finally, discretionary revenue measures in 2019 have been restated to account for the double cost of replacing the Competitiveness and Employment Tax Credit with a permanent cut in social security contributions. This cost has been treated as a one-off.On the expenditure side, interest payments owed on dispute settlements have also been recorded as one-offs. In addition, the change in the timing of recognition of sales of mobile phone licenses is also classified as a one-off, as was the case for recognition of the EU Amending Budget No. 6 following a major change in recognition rules. The impact of sales of transmission frequencies on the general government balance has been spread out over the planning period since the second quarter of 2018 instead of recognition when new frequencies are released, as it was decided at the time when the Public Finance Planning Act was drafted.

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

(in € bn)	2018	2019	2020	2021	2022
Revenue (1)	**-0.4**	**-21.7**	**-1.9**	**-1.0**	**-1.0**
UCITS dispute	-0.3	-0.4	-0.6	-0.6	-0.6
De Ruyter dispute	0.0	0.0	0.0	0.0	0.0
Stéria dispute	-0.1	-0.1	-0.1	0.0	0.0
Exceptional corporate income tax payment for large corporations to offset the disputed 3% tax on dividends	0.1	0.0	0.0	0.0	0.0
Investment income tax dispute (*précompte mobilier*)	0.0	-0.1	-0.1	-0.2	-0.2
Withholding tax dispute	0.0	-0.1	-0.1	0.0	0.0
CVAE dispute	-0.3	0.0	0.0	0.0	0.0
Messer dispute	0.0	-0.2	-0.2	-0.2	-0.2
Deferred prosecution agreements (CJIP)	0.3				
Double cost of replacing the Competitiveness and Employment Tax Credit (*)		-20.1			
Double cost of replacing the Tax Credit for Payroll Tax (*)		-0.5			
Double cost of replacing the Apprenticeship Tax Credit (*)		-0.2			
Double cost of replacing the Energy Transition Tax Credit (*)			-0.8		
Expenditure (2)	**5.3**	**1.6**	**0.3**	**0.3**	**0.3**
Disputed 3% tax on dividends	3.7	0.2	0.0	0.0	0.0
Change in the timing of recognition of mobile phone license sales	1.0	1.1			
Interest on dispute settlements	0.6	0.2	0.3	0.3	0.3
Total effect on balance (1) – (2)	**-5.6**	**-23.3**	**-2.1**	**-1.3**	**-1.3**

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

3.4 GENERAL GOVERNMENT BALANCE BY SUB-SECTORS

After achieving a deficit equivalent to 2.5% of GDP in 2018, the effort to contain government expenditure will continue between 2019 and 2022. This effort will be shared by all general government sub-sectors: central government will contain its expenditure under the benchmark; local governments will continue to make major efforts to moderate their operating expenditure growth, under the terms of the contracts introduced under the Public Finance Planning Act (see 6.1.3. - Streamlining Local Government Expenditure). Social security funds will also take part in containing public expenditure by meeting a national healthcare expenditure growth target, which will be lowered to 2.3% per year again for the period from 2020 to 2022. This fiscal consolidation effort should reduce the public expenditure ratio by 2.7 percentage points of GDP between 2017 and 2022 (or 2.9 points after restatement for the inclusion of France Compétences).

The aggregate tax and social security contribution rate should fall by 1.1 points between 2017 and 2022 to reach 44.0% of GDP in 2022 (or 1.4 points after restatement for France Compétences). The further reduction of the aggregate tax and social security contribution rate, after sharp cuts for corporations and households in 2018, will result in 2019 from the replacement of the Competitiveness and Employment Tax Credit with a permanent cut in contributions, particularly contributions on low-wage jobs. The reduction will also be the result of further cuts in the corporate income tax rate to bring it down to 25% in 2022, which is consistent with the average rate in the European Union countries, and the next phases in abolishing the residence tax for primary homes.

These objectives, combined with a lower public expenditure ratio, should make it possible to achieve a headline deficit of 1.2% of GDP by 2022. The central government balance will be hit by the double cost of replacing the Competitiveness and Employment Tax Credit in 2019[12] and by the official transfer between central government and other central government bodies concerning the SNCF Réseau debt assumed in 2020 and 2022. If these one-offs were excluded, the balance for all sub-sectors would show steady improvement over the period.

TABLE 5: GENERAL GOVERNMENT LENDING CAPACITY (+) / BORROWING REQUIREMENT (-)[13]

% of GDP	2017	2018	2019	2020	2021	2022
General government balance, Maastricht definition	**-2.8**	**-2.5**	**-3.1**	**-2.0**	**-1.6**	**-1.2**
Of which: primary balance	*-1.0*	*-0.8*	*-1.5*	*-0.5*	*-0.1*	*0.4*
Central government	-2.9	-3.0	-3.6	-4.0*	-3.1	-3.5*
Other central government bodies	-0.2	-0.1	-0.1	1.0*	0.0	0.4*
Local government	0.1	0.1	0.1	0.2	0.5	0.6
Social security funds	0.2	0.5	0.5	0.8	1.0	1.2

Notes: The central government's assumption of €25 billion of the SNCF Réseau debt in 2020 and €10 billion in 2022 will deepen the central government deficit by the same amounts and improve the balances of other central government bodies. Absent this transfer, which is neutral for the general government balance, the central government deficit would stand at 3.0% in 2020 and 3.1% in 2022, while the other central government bodies balance would stand at a deficit of 0.1% in 2020 and balance out at 0.0% in 2022.

3.5 PUBLIC EXPENDITURE

3.5.1 GENERAL GOVERNMENT EXPENDITURE

General government expenditure grew by 1.3% in nominal terms in 2018. This was down sharply from the 2.4% growth seen in 2017 and marks a decrease of 0.3% in real terms for the first time in several decades. Efforts to contain expenditure over the forecast period should lead to growth of 0.2% in real terms over the period from 2018 to 2022 (after restatement for France Compétences, see chart). This is to be compared to average growth of 1.2% per year seen over the period from 2008 to 2017.

Nominal growth of general government expenditure, excluding tax credits, stood at 1.3% in 2018, following 2.4% growth in 2017. The slower growth stems primarily from slower growth of central government expenditure. Containment of civil service wage growth, along with savings measures targeting subsidised employment contracts and housing benefits made it possible to limit central government expenditure growth to 0.5% on a like-for-like basis (see Table 6). The slower growth of central government expenditure shown in the national accounts can also be linked to the recapitalisation of AREVA nuclear power group recognised as an expense of €4.5 billion in 2017 and, to a lesser extent, to smaller losses on refunds of the disputed 3% dividend tax, which came to €3.7 billion in 2018, compared to €4.7 billion in 2017. Local government expenditure posted strong growth of 2.4%, excluding transfers. This growth stemmed from investment expenditure patterns related to the local election cycle, but was still contained under the terms of contracts concerning operating expenditure growth. Social security funds' expenditure growth slowed slightly, with increases in the wage bill resulting from pay raises awarded in 2017 and a national healthcare expenditure growth target capped at 2.3%.

In 2019, nominal expenditure growth, excluding tax credits, should pick up slightly to 1.6%, after stripping out expenditure of €4.6 billion on France Compétences, the national vocational training authority established in 2019 and included in the general government sector. Central government expenditure growth should continue to be moderate, at 1.0%, with savings produced by reforms of the housing sector and subsidised employment contracts, along with a

[12] A transfer of some €24 billion in VAT revenue will compensate the social security funds for the cost of further cuts in contributions in 2019. Therefore, central government will bear the cost of the Competitiveness and Employment Tax Credit claims accruing in 2019 for credits accumulated in 2018 and earlier years, as well as the cost of the transfer of VAT revenue to the social security funds.

[13] The sub-sectors' respective contributions to the efforts in 2020 and 2021 are determined by convention.

savings target of €1.5 billion to help finance the economic and social emergency measures. This should partially offset the rebound in expenditure growth linked to the increase in the in-work benefit included in the Initial Budget Act. Local government expenditure growth should be slightly faster, since 2019 is the last year in the local election cycle. It should stand at 2.7%, up 0.2 percentage points compared to 2018. Most of the faster growth will stem from the resumption of the 1.2% operating expenditure growth rate under the local government contracts, which will be partially offset by slightly slower growth of local government investment expenditure. Social security funds' expenditure growth should be slightly higher, but still contained. This faster growth is related to limited increases in pensions and social benefits, which will rise by 0.3%, as well as from lower expenditure by the unemployment insurance scheme (Unédic) as the economy improves and the scheme complies with the guidelines issued.

General government expenditure, excluding of tax credits, should fall from 54.4% of GDP in 2018 to 54.0% in 2019 (or 53.8%, excluding France Compétences). Continuing efforts by all general government sub-sectors to contain expenditure in 2020 should reduce this share to 53.5% of GDP (or 53.3%, excluding France Compétences). The average growth rate of general government expenditure between 2018 and 2022 in real terms should stand at 0.2%, which should make it possible to reduce the expenditure ratio by 2.9 percentage points of GDP over the government's five-year term. This ratio should stand at 52.3% of GDP in 2022, or 52.1% excluding France Compétences.

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

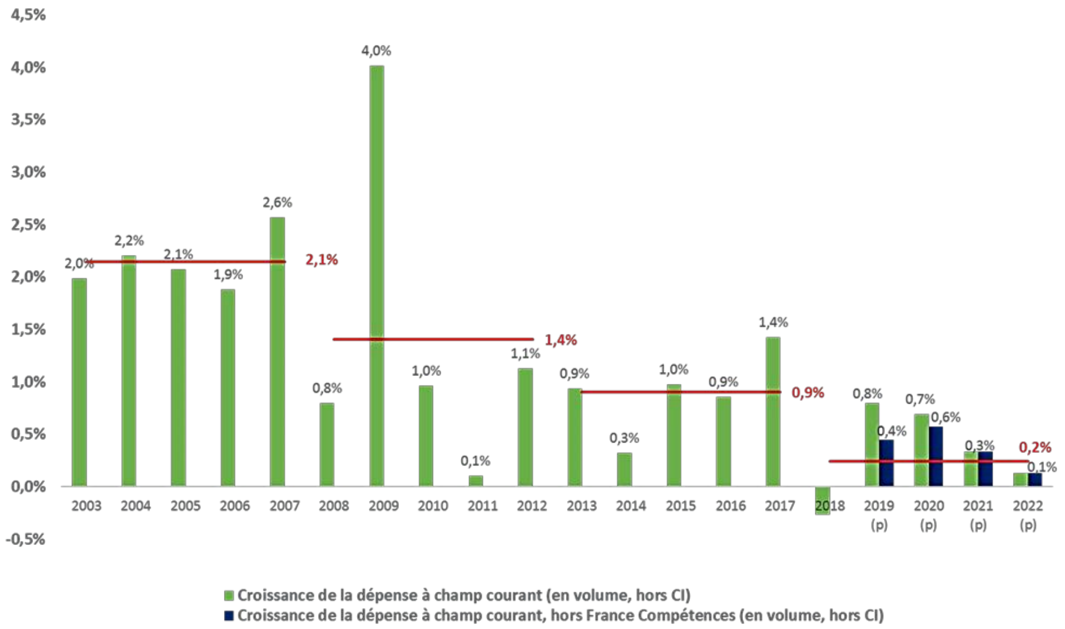
Nominal terms, excluding tax credits and transfers*	2018	2019	2020
General government, restated for France Compétences	*1.3%*	*1.6%*	*1.6%*
General government, on a like-for-like basis and excluding the 3% dividend tax dispute	1.4%	1.8%	1.6%
Central government	0.5%	1.0%	1.9%
Other central government bodies (ODAC)	0.2%	1.8%	2.2%
Local government (including investment and Société du Grand Paris)	2.4%	2.7%	0.9%
Social security funds	1.7%	2.0%	1.6%

* Nominal expenditure, excluding tax credits and transfers between general government sub-sectors.

** Restatements:

- In 2018, the expenditure of central government and other central government bodies have been corrected to account for the elimination of the solidarity fund, which had been part of other central government bodies. The relevant expenditure and revenue have been transferred to central government. Not on a like-for-like basis, other central government bodies' expenditure would decrease by 3.4% and central government expenditure would increase by 0.9%. The elimination of the solidarity fund increases central government spending by €2.5 billion and decreases other central government bodies' expenditure by the same amount. Other restatements relate to changes such as the expensing of the Energy Transition Tax Credit, which will entail a double cost in the transition year 2020.
- In 2018 and 2019, central government expenditure is restated to account for refunds of the 3% dividend tax (€4.7 billion in 2017, €3.7 billion in 2018 and €0.2 billion in 2019). By convention, these refunds were recorded as expenditure in the national accounts, whereas the other dispute settlements were recorded as reduced revenues.
- In 2019 and 2020, other central government bodies' expenditure and general government expenditure are restated to account for the creation of France Compétences. This restatement will also affect local government expenditure, since local governments have transferred some of their vocational training expenditure to France Compétences. The relevant sums are €4.6 billion in 2019 and €1.5 billion in 2020 (net of the reduced expenditure for regions).
- In 2020, other central government bodies' expenditure is also restated to account for interest expenditure related to the central government's assumption of €0.8 billion in debt owed by SNCF Réseau. Central government expenditure has also been restated to reflect this increase in interest expenditure. The assumption of the debt is automatically restated under this consolidated presentation that excludes transfers between sub-sectors.

REAL GENERAL GOVERNMENT EXPENDITURE GROWTH EXCLUDING TAX CREDITS FROM 2003 TO 2022



Expenditure growth (in real terms, excluding tax credits)
Expenditure growth, excluding France Compétences (in real terms, excluding tax credits)

3.5.2 CENTRAL GOVERNMENT EXPENDITURE

The French Government is still committed to further fiscal consolidation through targeted efforts to reduce general government expenditure, in compliance with the 2018-2022 Public Finance Planning Act. Following the major efforts made in recent years and the results obtained in 2018, **containment of central government expenditure will continue in 2019** and in later years.

In 2018, the discretionary expenditure benchmark and the total central government expenditure target (ODETE) set out in the Initial Budget Act were both met. Discretionary expenditure came in at €1.4 billion under the forecast in the Initial Budget Act. This good outturn was partially offset by expenditure under the total central government expenditure target, which ultimately stood at €425.3 billion, as opposed to the €425.7 billion originally forecast in the Initial Budget Act. After the Initial Budget Act was enacted, the levy on revenue paid to the European Union increased by €0.4 billion and the balancing contribution paid from the general budget to the central government debt and cash management account rose by €0.3 billion. The increase in transfers to local governments, which were up by €0.3 billion, also offsets the good outturn of expenditure under the discretionary expenditure benchmark. Ultimately, it reduces the compliance with the total central government expenditure target to €0.4 billion, compared to the Initial Budget Act. Compliance with the discretionary expenditure benchmark and the total central government expenditure target helped to reduce the central government budget deficit outturn, compared to the Initial Budget Act (with a deficit of €76.1 billion, compared to €85.7 billion).

In 2019, the Government announced that it will achieve savings of €1.5 billion under the central government expenditure benchmark compared to the Initial Budget Act. These savings will be used to help fund the economic and social emergency measures. The exercise to enhance the truthful representation of the €4 billion in appropriations to the contingency reserve at the start of the year will make it easier to reach this goal. This exercise entailed shifting some of contingency reserve funds for non-discretionary expenditure towards discretionary expenditure to ensure that the funds will be available in the current year.

Implementation of the reforms introduced in 2017 and 2018 will continue in 2019, with:

- Further transformation of housing policy (means-testing for housing benefits based on current income and the measure to introduce means-tested rent reductions for public housing tenants);
- Public broadcasting reform;
- Continuing reduction in the volume of subsidised employment contracts and deployment of the employment inclusion fund, which pools policy resources at the regional level for schemes to promote inclusion through employment (PEC, IAE);
- Limited increases in certain central government benefits, such as a 0.3% increase in pensions.
- Simplification of business subsidies.

As was the case in 2018, the containment of central government expenditure will still **ensure financing for the Government's priorities,** such as:

- More resources for the State's sovereign functions, with increased resources for the armed forces and job creation in the security and justice sectors;
- Boosting households' purchasing power and incentives for working, including an increase in the in-work benefit;
- Ecological transition support for low-income households, including an increase in the energy bonus, raising the average amount paid to 3.7 million households to €200 in 2019 and expanding the programme to cover the 20% of households with the lowest incomes.
- Better policy to fight unemployment with more active policies for employment, the Investment in Skills Plan and efforts to promote education;
- More effective support for the most vulnerable citizens based on a targeted social expenditure policy and a plan to fight poverty with the aim of enhancing support for entering the labour market and ensuring that the most underprivileged citizens have access to essential goods and services;
- Increased government investment in the broadest sense, with the deployment of the Great Investment Plan.

In addition, containment of the growth of total central government expenditure in 2019 will be accentuated by a decrease in debt service (see Box 6).

Implementation of savings measures and efforts to contain central government expenditure will continue in the years from 2020 to 2022. Slightly faster growth of central government expenditure will occur in 2020 as a result of a sharp increase in the levy on revenue paid to the European Union. This amount will rise by nearly €1.5 billion. The cost of debt service shown in the national accounts will also be stable, after the projected decrease of €2.5 billion in 2019.

BOX 6 – CENTRAL GOVERNMENT BORROWING COST AND INTEREST RATE ASSUMPTIONS

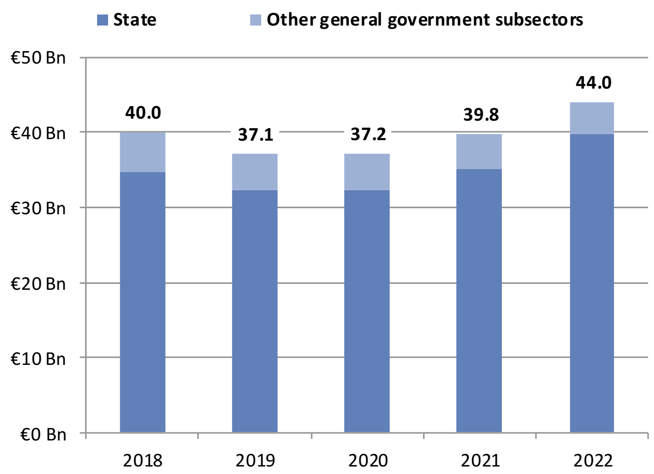
In 2018, France continued to enjoy favourable borrowing terms as a result of the European Central Bank's accommodative monetary policy and unwavering investor confidence. Yields at issue for short-term government securities were negative at -0.60% on average and yields on securities maturing at more than one year averaged 0.53%.

The interest rate path underlying the debt service cost forecast is based on the assumption that the ECB will raise its policy rates in 2020, in keeping with its forward guidance and other macroeconomic parameters applied in the Stability Programme. This means that short-term yields will start to rise in 2020. At the same time, gradual macroeconomic strengthening and the fading moderating effects of the ECB's asset purchase programme are likely to result in a rise in medium-term and long-term yields. The assumption is that the 10-year yield will rise by 75 basis points per year.

End of year levels (forecasts)	2019	2020	2021	2022
Short-term yields (3-month BTFs)	-0.20%	0.70%	1.50%	2.10%
Long-term yields (10-year OATs)	1.25%	2.00%	2.75%	3.50%

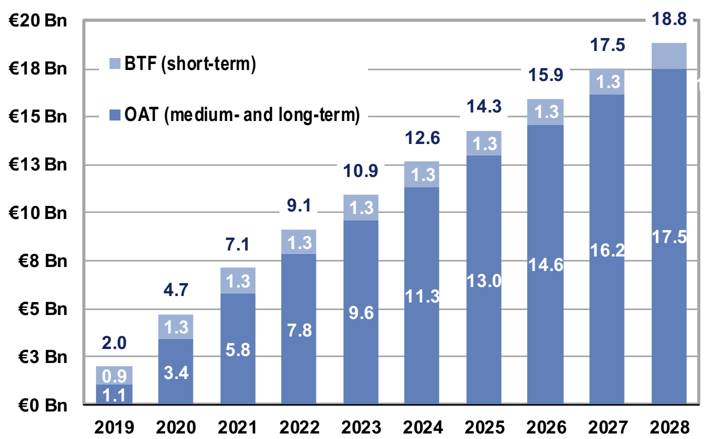
Interest expenditure should decrease for general government as a whole in 2019 and 2020, despite the increase in outstanding debt in nominal terms, as a result of refinancing at lower rates over the last few years. In 2019, the decrease could also be attributed to the 2018 base effect, since index-linking resulted in increased interest expenditure as inflation rose in 2018. Farther out, interest expenditure should increase with the expected increases in interest rates.

CHART 1: GENERAL GOVERNMENT INTEREST RATE EXPENDITUREIN THE NATIONAL ACCOUNTS



An extended rebound to higher yields than those presented above could gradually increase the cost of debt service to a higher level than that forecast in this Stability Programme. The chart below shows the impact of a shock of a 100-basis-point jump in early 2019, on the entire yield curve and for the entire forecast period, compared to the baseline scenario. The impact would be felt gradually because the debt would be refinanced in stages. For example, this shock would reduce structural adjustment by an average of 0.1 percentage points of GDP starting in 2019.

GRAPH 2: IMPACT OF A PERMANENT RATE INCREASE OF 1% ON THE DEBT SERVICE FOR NEGOTIABLE DEBT OF THE STATE



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

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

3.5.3 EXPENDITURE OF OTHER CENTRAL GOVERNMENT BODIES

In 2018, expenditure of other central government bodies, most of which are "central agencies"[14], decreased by 3.4% compared to 2017. This decrease stems mainly from the elimination of the Unemployment Solidarity Fund (FSCH) and the relevant €2.5-billion expenditure, which was transferred to the central government sector in 2018. On a like-for-like basis, without the FSCH, other central government bodies' expenditure would decrease slightly, dropping by 0.3%[15], with contrasting developments for different bodies:

- the guarantee fund for victims of terrorism and other criminal acts (FGTI) saw a big drop in its expenditure, which fell by €0.6 billion, following an increase in 2017, when large provisions were set aside for various incidents;
- expenditure for some major infrastructure projects, including the French transport infrastructure financing agency (AFITF), the Lyon-Turin Tunnel (TELT) and the Canal Seine Nord Europe (SCSNE) projects, was up by €0.2 billion;
- other central government bodies' expenditure under Invest for the Future Programmes (PIA) 1 and 2 was virtually unchanged from 2017.
- Finally, the inclusion of SNCF Réseau in the other central government bodies subsector, following the notification in October 2018, results in a conventional increase in the subsector's expenditure. In both 2017 and 2018, the SNCF Réseau deficit shown in the national accounts stood at €2.5 billion and was fully expensed.

Containment of other central government bodies' expenditure starts with closer monitoring of their resources, by means of periodic lowering of the caps on earmarked taxes, with a reduction of €0.9bn, excluding the Unemployment Solidarity Fund, and by banning these bodies from incurring debt with maturities of more than 12 months in the form of bank borrowing, in accordance with the provisions of the 2018-2022 Public Finance Planning Act. Central government agencies' expenditure for the Invest for the Future Programme (PIA) is monitored at the central level by the General Secretariat for Investment, which reports to the Prime Minister and also monitors all of the actions under the Great Investment Plan. Expenditure reported on SNCF Réseau should start to decrease with the rationalisation effort introduced by Act 2018-515 of 27 June 2018 on a new railways pact. The provisions of the Act should enable the publicly owned group to achieve economic equilibrium by the end of the Government's five-year term.

In 2019, other central government bodies' expenditure should see faster growth of 9.6%, following the creation of the new government-funded institution, France Compétences. Absent France Compétences, other central government bodies' expenditure would rise by only 1.8%[16] on a like-for-like basis. This increase would stem primarily from higher intervention expenditure on major infrastructure projects, such as the projects financed by the French transport infrastructure financing agency (AFITF) and the rollout of the "Initiatives Copropriétés" and "Habiter Mieux" programmes by the National Housing Improvement Agency (ANAH).

Other central government bodies' expenditure growth should slow slightly in 2020 to stand at 1.3%, excluding France Compétences.

3.5.4 SOCIAL SECURITY FUNDS' EXPENDITURE

In 2018, social security funds' expenditure grew by 1.9%, compared to growth of 2.0% in 2017. On a like-for-like basis, which mainly means stripping out the effects of the 2017 transfer of the funding for vocational rehabilitation centres for disabled adults (ESAT) from central government to social security funds, the latter's expenditure growth was slightly higher, at 1.9%, compared to 1.7% in 2017. The faster growth can be attributed to an increase in expenditure on benefits, which was partially offset by slower growth of expenditure on personnel.

Expenditure on benefits showed much faster growth, at 2.2%, compared to 1.7% in 2017. This was mainly attributable to faster growth of expenditure on old-age benefits, which grew by 2.7%, compared to 1.7% growth in 2017. This expenditure growth was driven by both prices and volume. Price increases contributed 0.4 percentage points to the overall increase. This contribution stems from higher inflation in 2017, and the full-year effect in 2018 of the increase in basic retirement benefits that came into force in October 2017. Meanwhile, the volume of new retirees claiming benefits was back to its usual level. The implementation of the 2010 pension reforms was completed in 2017.

At the same time, postponement of implementation of the "agreement on professional development, careers and compensation" from 2018 to 2019, the end of the impact of civil service pay raises in 2016 and 2017 and a policy to

[14] Central government agencies and other central government bodies do not cover exactly the same entities: the former are defined in budgetary terms, while the latter are listed by the French national institute of statistics and economic studies (Insee) on the basis of national accounts criteria. Some two-thirds of other central government bodies' expenditure can be attributed to entities that are also central agencies. At the same time, some three-fifths of the central agencies' expenditure can be attributed to other central government bodies.

[15] In this instance, other central government bodies' expenditure includes transfers to other general government subsectors, which is not the case in Table 6.

[16] In this instance, other central government bodies' expenditure includes transfers to other general government subsectors, which is not the case in Table 6.

contain expenditure growth meant that social security funds' wage bill growth slowed drastically from 2.4% in 2017 to 0.6% in 2018.

Moreover, the national healthcare expenditure growth target (Ondam), which was set at €195.4 billion for 2018, was met. The Government's successful management meant that healthcare expenditure growth was lower, which made it possible to reallocate €300 million to hospitals.

In 2019, social security funds' expenditure should show similar growth to that seen in 2018, standing at 2.0%, compared to 1.9 in 2018.

Expenditure on benefits should grow at the same rate of 2.2%. Growth of expenditure on old-age benefits should be slightly slower, at 2.6%, compared to 2.7% in 2018. The effect of prices should be virtually the same as in 2018: the increase in basic pension benefits should be contained at 0.3%, making it possible to reduce this expenditure. On the other hand, a further increase in inflation will boost expenditure on supplementary pensions, despite Agirc-Arrco agreement limiting index-linking to one percentage point less than inflation, excluding tobacco. This agreement will run until November 2019. Nevertheless, the growth in the volume of new retirees claiming benefits will be slightly slower, as the solidarity coefficients and financial incentives for postponing retirement introduced under the October 2015 Agirc-Arrco agreement enter into force.

The growth of expenditure on health insurance should be slightly faster as a result of the national healthcare expenditure growth target of 2.5% for 2019. This exceptionally high target covers the investment needed for the strategy to transform the healthcare system.

Expenditure on unemployment benefits will be affected by the negotiations between management and labour representatives aimed at changing the benefit rules, as provided for under the Act of 5 September 2018 on the freedom to choose one's future career. These negotiations ended in February 2019 with no agreement, which means the Government is preparing to step in. The guidelines for the negotiations set out the objectives of the reform: improving the method for calculating benefits in order to end the incentives for signing multiple short-term contracts; adapting benefits according to certain characteristics to account for the ability of each jobseeker to find a new job, expanding eligibility for benefits to workers who resign and self-employed workers (universal unemployment insurance); giving employers an incentive to limit successive terminations of employment contracts. Implementation of the new benefit rules will help reduce the debt of the unemployment insurance scheme. The guidelines included estimates of savings, which are expected to average between €1 billion and €1.3 billion per year in 2019, 2020 and 2021. The public finance forecast presented here is based on these figures, but it also acknowledges the fact that savings in 2019 could be smaller because of phased implementation.

In 2020, social security funds' expenditure growth should slow to 1.5%, compared to 2.0% in 2019. The slower growth could be attributed to slower growth of expenditure on benefits resulting from a level of savings close to that achieved in 2019. The full effects of the incentives for postponing retirement under the Agirc-Arrco agreement should also slow expenditure growth, along with further decreases is expenditure on unemployment insurance stemming from the business cycle and the growing impact of reforms.

The effort to contain social security funds' expenditure growth will continue between 2020 and 2022.

3.5.5 LOCAL GOVERNMENT EXPENDITURE

In 2018, local government expenditure growth (including transfers) stood at 2.4%, compared to 2.2% in 2017. The faster growth can be attributed to faster growth of local investment expenditure[17], with the next municipal elections two years away. Local community investment expenditure grew by 6.4%, when corrected for the specific activity of Société du Grand Paris (SGP). At the same time, the Financial Pact with central government has kept local government operating expenditure growth down to only 0.8% (as reported in the national accounts). This can be attributed to crosscutting measures to cap wage bill growth at 1.2% in nominal terms for the period from 2018 to 2020 under the terms of the contracts with 322 local governments. In the meantime, SGP's expenditure continued to rise.

Local government expenditure growth should be slightly faster in 2019, at 2.6%. The faster growth should be attributable to a resumption of 1.2% growth of local government operating expenditure under the target set in the Public Finance Planning Act, compared to 2018, when growth fell short of the target. The breakdown shows that expenditure on personnel should be sustained by the resumption of the measures introduced under the "agreement on professional development, careers and compensation", while the decline in the workforce employed under subsidised contracts should be slower. Intermediate consumption expenditure growth should be contained as price increases slow down.

Local government investment expenditure should grow by 4.9% in 2019, which is slower than the growth posted in 2018 and consistent with the previous election cycle. Local government will also undertake some exceptional asset sales in 2019. The expenditure of Société du Grand Paris will continue to grow.

[17] Includes gross fixed capital formation, investment subsidies and land purchases.

The municipal election cycle will cause a sharp slowing of local expenditure growth in 2020. Local government expenditure is expected to grow by only 0.4% in 2020. In addition to the expected 3.6% decline in their investment expenditure, local governments will continue their efforts to contain their wage bills and operating expenditure growth in order to meet the operating expenditure growth target of 1.2% set out in the Public Finance Planning Act. The path for later years assumes continued compliance with the operating expenditure growth target and an investment expenditure pattern that is consistent with previous election cycles.

3.6 PUBLIC REVENUE

3.6.1 GENERAL GOVERNMENT REVENUE

The aggregate tax and social security contribution rate fell slightly in 2018 to 45.0% of GDP, compared to 45.2% in 2017. Tax cuts more than offset the spontaneous increase in taxes and contributions that outstripped GDP growth, with tax elasticity standing at 1.2. The aggregate rate will fall more sharply in 2019 to reach a low of 44.0% of GDP as a result of replacing the Competitiveness and Employment Tax Credit with a cut in social security contributions, as well as the discretionary measures announced in December. In 2020, there should be a slight rebound in the aggregate rate to 44.4%, as a result of the fading effects of the replacement of the Competitiveness and Employment Tax Credit[18]. This forecast incorporates all of the measures passed or announced by the government, along with the usual pattern of local taxes over the local election cycle and reimbursements related to on-going tax disputes.

In 2019, the aggregate tax and social security contribution rate should fall by 1 percentage point to 44.0% of GDP (or 43.8% excluding France Compétences). Discretionary tax measures will reduce taxes and contributions by €29 billion (excluding the impact of creating France Compétences, see Table 7) and account for all of the decrease in the aggregate rate. Spontaneous growth should be in line with GDP growth, with tax elasticity equal to one. Even with the exclusion of the temporary effect of replacing the Competitiveness and Employment Tax Credit, which accounts for two-thirds of the decrease, the cut is still significant and primarily benefits households. The relief for households can be attributed to the exemption of overtime pay from taxes and social security contributions, starting in January 2019, and the cut in the general social contribution for pensioners with low incomes under the terms of the Emergency Social and Economic Measures Act, along with the second phase in abolishing the residence tax and the full-year effect of the complete elimination of employees' contributions for unemployment insurance on 1 October 2018. In addition to the replacement of the Competitiveness and Employment Tax Credit, discretionary measures aimed at corporations include the introduction of the tax on digital services and the postponement of the cut in the corporate income tax rate for corporations with sales of more than €250 million, as set out in the bill submitted on 6 March 2019. Furthermore, spontaneous growth of taxes and social security contributions should revert to matching GDP growth, after significantly outstripping it for three years. Finally, the introduction withholding at source for personal income tax in 2019 should mean that the tax burden on all French taxpayers is more closely aligned with their current income.

In 2020, the aggregate tax and social security contribution rate should rise slightly to 44.4% of GDP (or 44.1%, excluding France Compétences). Once again, spontaneous revenue growth should match GDP growth. Consequently, any variation in the aggregate tax and social security contribution rate can be attributed solely to discretionary measures. Such measures will help cut taxes and contributions by nearly €3.1 billion for households and by €2.4 billion for corporations. However, the aggregate impact of discretionary tax measures seems to lead to an increase because of the temporary rebound effect after the double cost of replacing the Competitiveness and Employment Tax Credit. The national accounts balance shows that the replacement of the Competitiveness and Employment Tax Credit is fully expensed in 2019, when the replacement occurs, but the temporary effect on the aggregate tax and social security contributions rate will last longer, as corporations' accrued tax credit claims are refunded over time. In the cash-based budgetary accounts, the measures would cut revenue by €20 billion in 2019, and by only €7 billion in 2020. In addition to these effects on the calculation of taxes and social security contributions, which do not affect the general government balance, continued efforts to cut taxes for households will include the last phase of eliminating the residence tax for the 80% of households with the lowest incomes and efforts to cut corporate taxes will include further cuts in the corporate income tax rate.

In later years, further expenditure efforts should make it possible to finance more cuts in taxes and social security contributions, lowering the aggregate rate by 1.4 percentage points of GDP between 2017 and 2022 (after restatement for France Compétences), with the elimination of the residence tax and the reduction of the corporate income tax rate to 25% for all corporations by 2022. The adjustment path through 2022 is based on spontaneous growth of taxes and contributions remaining in line with nominal GDP growth (tax elasticity equal to one).

[18] Tax credits are recorded according to budgetary accounting concepts. They are recorded as tax decreases for the amount paid. The national accounts treat them differently, recording refundable or deferred tax credits as claims reported on the government. This results in a smaller decrease of some €10 billion for 2018, 2019 and 2020.

TABLE 7: MAIN DISCRETIONARY TAX MEASURES IN 2018-2020 (RESTATED FOR THE CREATION OF FRANCE COMPÉTENCES)

	2018	2019	2020
Households	**-1.4**	**-10.6**	**-3.1**
Elimination of the residence tax for 80% of households	-3.2	-3.8	-3.1
Introduction of the Property Wealth Tax (IFI)	-3.2		
Introduction of a uniform flat-rate levy	-1.4	-0.8	0.4
Increase in supplementary pension contribution rates		1.1	-0.1
Replacement of employees' contributions with the general social security Contribution (CSG)	4.4	-4.0	-0.3
Reduction of the general social security contribution for low-income pensioners		-1.6	0.1
Tobacco taxes	0.9	0.5	0.6
Increase in energy taxes (households' share = 62%)	2.4	0.0	0.0
Extension of the Competitiveness and Employment Tax Credit to in-home service jobs	-1.0		
Expansion and extension of the Energy Transition Tax Credit	-0.3	1.1	0.1
Exemption of overtime pay from taxes and contributions		-3.0	-0.8
Corporations	**-9.0**	**0.2**	**-2.4**
Lowering the corporate income tax rate from 33% to 25%	-1.2	-0.8	-3.2
Competitiveness and Employment Tax Credit and increase in the rate from 6% to 7%*	-3.7	-0.4	0.0
Exceptional corporate income tax payment for large corporations	-4.8	-0.1	
Increase in energy taxes (corporations' share = 38%)	1.3	-0.1	0.0
Increase in supplementary pension contribution rates		0.7	
Tax integration measures (including the *Copé* exemption)		0.4	0.2
GAFA tax		0.4	0.1
Introduction of a tax credit for the tax on wages	-0.6	-0.0	0.6
Temporary effect of replacing the Competitiveness and Employment Tax Credit with a cut in social security contributions*		**-20.0**	**13.1**
Resources earmarked for *France Compétences* to finance the Invest in Skills Plan	**0.3**	**1.3**	
Total**	**-10.1**	**-29.2**	**7.5**

* Effect on tax and social security contributions rate, not the effect on the balance

** Discretionary tax measures excluding France Compétences

TABLE 8: TAXES AND SOCIAL SECURITY CONTRIBUTIONS

	2017	2018	2019	2020	2021	2022
Aggregate rate as a percentage of GDP	45.2	45.0	44.0	44.4	44.2	44.0
Excluding France Compétences	*45.2*	*45.0*	*43.8*	*44.1*	*44.0*	*43.8*
Tax elasticity to GDP growth	1.4	1.2	1.0	1.0	1.0	1.0

3.6.2 CENTRAL GOVERNMENT REVENUE

In 2018, taxes and social security contributions assessed by central government stood at 13.7% of GDP, down by 0.6 percentage points of GDP compared to 2017 as a result of discretionary tax measures and transfers. Tax cutting measures for households and corporations mainly affected central government revenue. The end of the exceptional corporate income tax payment for large corporations passed in 2017 and the payment of Competitiveness and Employment Tax Credit claims (as the rate was raised from 6% to 7% for 2017 and the claims from 2014 were paid for the first time at the 6% rate) will also reduce central government revenue. When discretionary tax measures are excluded, the growth of taxes and contributions assessed by central government stood at 4.1%, outstripping GDP growth of 2.5%. A brighter macroeconomic environment in 2017 and 2018 boosted corporations' taxable income, thereby increasing the revenue generated by corporate income taxes. In addition, revenue from personal income tax on 2017 income was also lifted by previous strong payroll growth. Strong consumption and investment growth also sustained VAT revenue.

In 2019, taxes and social security contributions assessed by central government are expected to decline by 1.1 percentage points of GDP, primarily as a result of discretionary tax measures and transfers. More specifically, central government revenue will be affected by the double cost of replacing the Competitiveness and Employment Tax Credit with a cut in social security contributions, resulting in a €20-billion cut in taxes and social security contributions. Central government's revenue will also be affected by payment of Competitiveness and Employment Tax Credit claims accrued in previous years as the same time as central government has to compensate the social security funds for their loss of revenue stemming from contribution cuts. Central government will also have to continue bearing the cost of the phased elimination of the residence tax for 80% of households. If these discretionary measures were excluded, taxes and social security contributions assessed by central government would have grown a bit faster than GDP. This growth would have been driven mainly by corporate income tax revenue boosted by sustained growth of taxable earnings in 2018.

In 2020, taxes and social security contributions assessed by central government should increase by 0.4 percentage points of GDP, rebounding after the double cost of replacing the Competitiveness and Employment Tax Credit with a cut in social security contributions. This rebound will be only partially offset by the next phase of eliminating the residence tax and the cut in the corporate income tax rate. With the exclusion of discretionary measures, taxes and social security contributions assessed by central government should post spontaneous growth that outstrips GDP growth as revenue from corporate income tax continues to be driven by sustained growth of gross operating surpluses in 2019 and even stronger growth in 2020.

3.6.3 SOCIAL SECURITY FUNDS' REVENUE

In 2018, social security funds' revenue growth was slower, standing at 2.8%, compared to growth of 3.3% in 2017. Most of the growth came from social security contributions on income from work and on investment income. The continuing strength of the economy meant that contributions grew by 3.2%, compared to 3.1% growth in 2017.

The shares of taxes and social security contributions changed in 2018. Social contributions as a share of aggregate taxes and social security contributions decreased, while the share of taxes on current income and assets increased. This change is the result of the two-step process to eliminate private-sector employees' contributions for healthcare and unemployment insurance. It is also the result of an increase in the general social security contribution, which is imposed at a lower rate than the former contributions, but levied on a broader contribution base.

As GDP growth boosted jobs and wages, the 3.2% growth of total taxes and contributions assessed by the social security funds, which are largely based on payrolls, outstripped the 2.5% growth of GDP in nominal terms. The aggregate tax and social security contribution rate assessed by the social security funds rose slightly, from 24.0% in 2017 to 24.2% in 2018.

In 2019, revenue growth should slow significantly to stand at 2.3%. The slower growth would stem mainly from the measures under the "Emergency Economic and Social Measures" Act, which will result in further gains in workers' purchasing power and better targeting of solidarity efforts for pensioners. The exemption of overtime pay from taxes and social security contributions starting in January 2019 will lower the contribution growth rate, while the exemption of pensioners with net monthly incomes of less than €2,000 from the increase in the general social security contribution will slow the growth of the relevant tax revenue.

There will also be a further change in the shares of taxes and social security contributions in revenue. Replacing the Competitiveness and Employment Tax Credit with cuts in social security contributions will lead to a significant drop in contributions, which will be offset by a greater share of VAT revenue earmarked for social security.

Aggregate taxes and social security contributions assessed by the social security funds should be equivalent to 24.1% of GDP in 2019, compared to 24.2% in 2018.

In 2020, the growth of social security funds' revenue should be faster than in 2019, standing at 2.6%. The shares of contributions and taxes will undergo further small changes, as the full-year impact of further cuts introduced on 1 October 2019, is felt in 2020 and offset by a VAT surplus. Social security funds' revenue should grow at the same pace as GDP, which means it will be equivalent to 24.1% of GDP in 2020, as it should be in 2019.

3.6.4 LOCAL GOVERNMENT REVENUE

In 2018, the growth of local government tax revenue stood at 5.6%, sustained by the introduction of a transfer of VAT revenue to regional governments in exchange for the elimination of their general operating grant. The faster growth of local taxes can also be attributed to the across-the-board increase in assessed rental values introduced under the 2018 Budget Act.

Under the terms of the Financial Pact between central government and local governments, financial support, excluding compensation for VAT paid and the share of VAT revenue earmarked for regional governments, will not be cut in 2018 or in later years. Excluding discretionary tax measures, local government revenue showed spontaneous growth of 2.2%.

In 2019, local government tax revenue should grow by 2.6% as revenue from transfer taxes stabilises, after posting strong growth in 2017 and 2018, and the 2.2% across-the-board increase in assessed rental values takes effect.

In 2020, local government tax revenue growth should slow further, falling to 1.2%, with the end of the apprenticeship tax revenue, which is now earmarked for France Compétences. Excluding discretionary measures, spontaneous growth of local government tax revenue should be virtually stable at 2.5%, as a result of lower inflation and the across-the-board increase in assessed rental values.

3.7 GENERAL GOVERNMENT DEBT AND STOCK-FLOW ADJUSMENT

The level of general government debt notified to the European Commission in 2018 stood at €2,315.3 billion, equivalent to 98.4% of GDP, which was the same ratio reached in 2017[19]. After years of major increases, the government debt-to-GDP ratio was stable in 2018. The reduction of the general government deficit to 2.5% of GDP in 2018, compared to 2.8% in 2017, made it possible to remain close to the debt-stabilising deficit balance of 2.4%. The deviation from the debt-stabilising balance ultimately contributed only 0.1 percentage points to the increase in the debt ratio (see Table 9). At the same time, stock-flow adjustments reduced the ratio slightly, with a decrease of 0.1 percentage points of GDP.

The debt ratio should increase to 98.9% of GDP in 2019 as a result of the double cost during the year of replacing the Competitiveness and Employment Tax Credit with cuts in social security contributions. This exceptional increase should be the result of a rebound in the general government deficit to 3.1% of GDP in 2019, which will be caused by one-offs, such as the replacement of the Competitiveness and Employment Tax Credit. The deviation from the debt-stabilising balance, which should be almost the same as in 2018, standing at 2.5% compared to 2.4%, is expected to contribute 0.6 percentage points of GDP to the increase in the debt ratio. Stock-flow adjustments should be neutral overall. Some of the adjustments will increase government debt. The cost of the switch to withholding income tax at source on the cash position[20] and deferred issue premiums from earlier years, which should be greater than new issue premiums in 2019, will increase the debt[21]. On the other hand, the proceeds of sales of central government equity holdings earmarked for debt reduction and the Innovation Fund should reduce the debt ratio, as should the fact that the impact of the Competitiveness and Employment Tax Credit on budgetary revenue is smaller than the amount of the outstanding claims recorded as an expense in the national accounts.

In 2020, the debt ratio should start to fall and stand at 98.7% of GDP. The deficit should shrink substantially to 2.0% of GDP and be under the debt-stabilising deficit balance of 2.5% of GDP (the same as in 2019). In this case the deviation from the debt-stabilising balance will reduce the debt ratio by 0.5 percentage points of GDP. However, the stock-flow adjustments will attenuate this reduction by contributing an increase of 0.3 percentage points of GDP to the debt ratio, resulting in part from the persistent budgetary impact of the Competitiveness and Employment Tax Credit, even though no further claims are recorded as expenses in the national accounts, and in part from deferred issue premiums from previous years.

In 2021 and 2022, the debt ratio should continue to fall from 98.1% of GDP in 2021 to 96.8% of GDP in 2022. Most of the decrease will be attributable to the growing deviation from the debt-stabilising balance, with continuing improvement in the deficit, standing at 1.6% of GDP in 2021 and 1.2% of GDP in 2022, along with the increase in nominal GDP growth as inflation rises to match the European Central Bank's long-term target. Stock-flow adjustments will slow the decrease in the debt ratio, primarily as a result of the replacement of the Competitiveness and Employment Tax Credit with cuts to social security contributions and the spreading of issue premiums and discounts over several accounting periods. In both 2020 and 2021, there will still be some outstanding Competitiveness and Employment Tax Credit claims to be paid. These claims will add to the Maastricht debt, but they will not affect the general government deficit.

[19] Figure reported to Parliament under the terms of Article 32 of the 2014-2019 Public Finance Planning Act, which was not abrogated by the 2018-2022 Public Finance Planning Act of 22 January 2018.

[20] The one-month lag in revenue resulting from the start of withholding at source on 1 January will cost some €6 billion for the budgetary balance in 2019. However, this cost is neutralised in the national accounts, which means it is a positive stock-flow adjustment.

[21] Maastricht debt is recorded at its nominal reimbursement value at maturity. Issues of securities with coupon rates that are higher than the market yields result in payment of a premium to the issuer. These premiums are recorded as negative stock-flow adjustments. The amortisation of these premiums over the life of the debt is recorded as a positive stock flow adjustment.

TABLE 9: GENERAL GOVERNMENT DEBT DEVELOPMENTS

(percentage points of GDP)	2018	2019	2020	2021	2022
Debt-to-GDP ratio according to the Maastricht definition	**98.4**	**98.9**	**98.7**	**98.1**	**96.8**
Debt-to-GDP ratio excluding financial assistance for euro area Member States	95.6	96.2	96.1	95.5	94.3
Change in debt ratio	**0.0**	**0.5**	**-0.2**	**-0.7**	**-1.3**
Deviation from debt-stabilising balance	0.1	0.6	-0.5	-1.1	-1.7
Debt-stabilising balance (excluding stock-flow adjustment)	*-2.4*	*-2.5*	*-2.5*	*-2.7*	*-3.0*
Headline balance	*-2.5*	*-3.1*	*-2.0*	*-1.6*	*-1.2*
Stock-flow adjustment	-0.1	0.0	0.3	0.5	0.4
Nominal GDP growth (%)	*2.5*	*2.6*	*2.6*	*2.9*	*3.1*

4.

SENSITIVITY ANALYSIS AND COMPARISON WITH PREVIOUS PROGRAMME

Sensitivity analysis and comparison with previous programme

4.1 SENSITIVITY TO EXTERNAL ASSUMPTIONS

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

The growth of France's exports will depend on our trading partners' economic growth. The many factors that could affect their growth include the extent of the slowdown in the euro area's growth, American protectionist measures, the terms for the United Kingdom's exit from the European Union, the severity of China's slowing growth, economic policy choices in the advanced countries, such as the United States, Spain, Germany and Italy, and in the emerging countries, such as Brazil, along with financial uncertainty in the United States and in the emerging countries.

The forecast for this Stability Programme assumes that demand for French exports will grow by 2.7% in 2019 and by 2.9% in 2020. The dollar/euro exchange rate is expected to average $1.13 in 2019 and 2020, and oil prices are expected to stabilise at $65 a barrel, with an average of $64 in 2019.

In addition to providing figures about how the baseline scenario assumptions concerning world demand for French exports, exchange rates, oil prices and interest rates will affect growth, inflation and the headline deficit (Tables 10, 11, 12 and 13), this section assesses the main upside and downside risks surrounding the forecast.

UNCERTAINTY ABOUT THE INTERNATIONAL SCENARIO

Demand growth inside the euro area has been unexpectedly weak in recent months. It could improve if business confidence improves more rapidly than expected.

The impact of Brexit still depends on the outcome of negotiations about the United Kingdom's future relationship with the European Union and the exit terms, which could affect trade between the UK and the EU.

Emerging economies still face major risks. If China's trade talks with the United States fail, the result could be a harsher slowdown for China's economy. However, the Chinese authorities have a proven track record of using powerful means to sustain growth. Turkey could see a stronger rebound if it receives budget support, but with a risk of greater imbalances. In Brazil, there are persistent doubts about the Government's ability to pass its ambitious pension reform. Political and geopolitical uncertainties constitute a downside risk for emerging countries, but the risk of massive capital outflows seems to be fading, as the Fed suspends its monetary tightening.

The risk of the Fed tightening its monetary policy more severely than expected seems to be ruled out at this point, in the absence of any significant rise in inflation. On the other hand, there is still major uncertainty surrounding American fiscal policy. Disagreements in Congress could lead to more restrictive fiscal policy if no agreement is reached on the 2020 budget.

In the euro area, easing of Italian sovereign yields by the end of the forecast period would boost growth and elections for the European Parliament and in Spain in the first half of 2019 could shape economic policy.

It is difficult to forecast changes in oil prices. They will depend on shrinking OPEC stockpiles, implementation of American sanctions on Iran and Venezuela, American supply growth and world economic growth.

BOX 7 – IMPACT OF A POTENTIALLY HARD BREXIT

The macroeconomic scenario in this Stability Programme assumes that the United Kingdom will leave the European Union under the terms of a negotiated exit agreement. The consequences of the UK crashing out of the EU without an agreement are very difficult to assess. However, preliminary estimates suggest that the impact of a hard Brexit for France would be **a loss of 0.2 percentage points of GDP** in the short-term, excluding the effects of greater uncertainty[22]. The impact could be felt through three channels:

(i) **the financial channel**, with a depreciation of sterling and the impact on risk premiums. This channel should attenuate the shock for the United Kingdom. A financial shock and an exchange rate shock similar to those seen after the referendum on 23 June 2016 would have a negligible impact on growth in France and the euro area. The scale of the shocks would depend on the Bank of England's monetary policy.

[22] The referendum results on the 23 June 2016 did not lead to an immediate and massive shock to risk premiums or stock market prices caused by economic agents' reactions to uncertainty.

(ii) **the customs duties channel**. The introduction of customs duties on goods traded between the EU and the UK would dampen demand as import prices rise. However, the short-term impact should be quite small:

- **On the British side**, the Government announced on 13 March that it would curb the impact of import duties in the United Kingdom in the event of a hard Brexit[23]. This should reduce the consequences for domestic demand in the UK, with an impact of less than 0.1%. The impact on British demand for French exports and for France's GDP should be virtually non-existent.
- **On the French side**, import duties on goods from the United Kingdom should stand at an average of 7%. Imports from the UK are equivalent to 0.8% of France's GDP, which means that the actual loss for the French economy would be less than 0.1 percentage points of GDP and domestic demand and growth would see a similar decrease.

(iii) **disruption of supply chains,** as new formalities and regulatory requirements come into play, despite the contingency measures adopted. Assuming that delivery times for imports to France range from 2 to 60 days, the impact would result in a loss of 0.1 percentage points of GDP (see table below[24]). Longer delivery times in the United Kingdom resulting from the reintroduction of customs inspections would have no direct impact on output in France.

Other institutions have published more pessimistic estimates, either because they relate to longer-term consequences or because the estimates were made before the 13 March announcement about lowering import duties in the United Kingdom in the event of a hard Brexit.

		Catégories de perturbations de l'approvisionnement				Ensemble
Degré de perturbation		Négligeable	Faible	Moyen	Important	(tous produits)
Hypothèse de délais supplémentaires de livraison depuis le R-U, par an (en jours)	(A)	2	10	30	60	~13
Équivalent en % d'une année d'approvisionnement depuis le RU	(B) =(A)/365	-0,5%	-3%	-8%	-16%	-4%
Part de cette catégorie dans les consommations intermédiaires en FR	(C)	30%	43%	12%	14%	100%
Part provenant du R-U pour les consommations intermédiaires en FR	(D)	2,1%	1,0%	2,4%	0,5%	1,4%
Impact des délais d'approvisionnement sur le PIB français	(E)=(B)*(C)*(D)	0,00%	-0,01%	-0,02%	-0,01%	-0,05%
Avec l'impact transitant par le reste du monde	(F) ≈ 2 x (E)					**-0,1%**

Source : World Input-Output Database, calculs DG Trésor

Categories of supply chain disruption — Aggregate (all goods)

Severity of disruption — Negligible — Low — Medium — High

Assumption concerning longer delivery times for imports from the UK per year (days)
Equivalent to a % of one year's supplies from the UK
Share of the category in intermediate consumption in France
Share of imports from the UK in intermediate consumption in France
Impact of delivery times on France's GDP
Including impact transiting via the rest of the world

Source: World Input-Output Database, DG Trésor calculations

ALTERNATIVE SCENARIOS PRESENTED IN THE STABILITY PROGRAMME[25]

TABLE 10: IMPACT ON FRANCE'S ECONOMY OF A 1% INCREASE IN WORLD DEMAND FOR FRENCH EXPORTS*

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

* Permanent 1% increase in export demand at the start of year n with no change in real interest rates

NB: An increase in world demand would boost exports, which would feed through to the rest of the economy, increasing business investment in particular.

[23] The British government announced the arrangements concerning the customs duties that it would apply in the event of a hard Brexit. These arrangements would exempt 87% of EU exports to the UK from duties. The average duty charged on EU exports should be less than 1%.

[24] The methodology used for this projection is similar to that used in the article in the Trésor-Eco bulletin 100 dated April 2012.

[25] The alternative scenarios in Tables 10, 11, 12 and 13 were obtained using the 2017 Mésange model. DG Trésor Working Papers (2017), "Le modèle macroéconométrique Mésange : réestimation et nouveautés," by Anne-Sophie Dufernez, Claire Elezaar, Pierre Leblanc, Emmanuelle Masson, Harry Partouche, José Bardaji, Benoît Campagne, Marie-Baïanne Khder, Quentin Lafféter, Olivier Simon.

TABLE 11: IMPACT ON FRANCE'S ECONOMY OF A 10% DEPRECIATION OF THE EURO AGAINST ALL OTHER CURRENCIES*

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

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

NB: A weak euro would boost growth in the short term by improving France's price competitiveness outside of the euro area and by stimulating the economic growth of its euro area partners.

TABLE 12: IMPACT ON FRANCE'S ECONOMY OF A $10 INCREASE IN OIL PRICES*

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

* $10 increase in the price of oil per barrel at the beginning of year n, with no change in real interest rates, no reaction from the rest of the world.

NB: With no change in exchange rates, an increase in the price of oil would have an inflationary impact. The resulting increase in consumer prices and decrease in corporate profits would weaken growth.

TABLE 13: IMPACT ON FRANCE'S ECONOMY OF A 100-BASIS-POINTS INCREASE IN SHORT-TERM INTEREST RATES LASTING FOR TWO YEARS*

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

* A 100-basis-point increase in euro area short-term interest rates lasting for two years and occurring at the beginning of year n, with its impact on long-term interest rates and no reaction from the rest of the world.

NB: An increase in interest rates would hinder growth by curbing business investment and return on capital, and by promoting savings over consumption.

Box 8: Using alternative scenarios for forecasting

The alternative scenarios presented in Tables 10 to 13 need to be handled with care. First of all, the multipliers linked to the alternative scenarios depend on the models chosen, which means that estimating them is subject to a high degree of uncertainty. For example, the alternative scenarios above are based on the Mésange modela, which is used to assess economic policy measures. They may differ from scenarios based on the Opale modelb, which is used for macroeconomic forecasting 1 to 2 years out. For instance, the impact of a 10% depreciation of the euro against all other currencies on GDP is smaller when forecast with the Opale model, at 0.7 points after three years, versus 1.3 points with the Mésange model. The impact of a $10 increase in oil prices on GDP is greater when forecast with the Mésange model, at -0.2 points after three years, versus -0.1 points with the Opale model. The alternative world demand scenarios are fairly similar in both models. An additional 1% of world demand growth leads to an additional 0.3 percentage points of GDP growth after 3 years in both the Mésange and Opale models.

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

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

(b) DG Trésor Working Papers (2017), "La maquette de prévision Opale2017," by Aurélien Daubaire, Geoffrey Lefebvre, Olivier Meslin.

4.2 COMPARISON WITH PREVIOUS PROGRAMMES

TABLE 14: COMPARISON WITH THE PREVIOUS STABILITY PROGRAMME

	2017	2018	2019	2020	2021	2022
2018-2022 Stability Programme (April 2018)						
Real GDP growth (in %)	1.8	2.0	1.9	1.7	1.7	1.7
Potential real growth (in %)	1.25	1.25	1.25	1.25	1.30	1.35
Output gap (as a % of potential GDP)	-0.9	-0.2	0.4	0.9	1.3	1.6
General government net lending (% of GDP)	-2.6	-2.3	-2.4	-0.9	-0.3	0.3
Structural balance (% of potential GDP)	-2.0	-1.9	-1.6	-1.4	-1.0	-0.6
Structural adjustment (% of potential GDP)	*0.5*	*0.1*	*0.3*	*0.3*	*0.4*	*0.4*
General government debt (% of GDP)	97.0	96.4	96.2	94.7	92.3	89.2
General government debt, excluding financial assistance for the euro area (% of GDP)	94.1	93.7	93.5	92.1	89.8	86.8
2019-2022 Stability Programme (April 2019)						
Real GDP growth (in %)	2.2	1.6	1.4	1.4	1.4	1.4
Potential real growth (in %)	1.25	1.25	1.25	1.25	1.30	1.35
Output gap (as a % of potential GDP)	-0.6	-0.3	-0.1	0.0	0.1	0.1
General government net lending (% of GDP)	-2.8	-2.5	-3.1	-2.0	-1.6	-1.2
Structural balance (% of potential GDP)	-2.4	-2.1	-2.1	-1.9	-1.6	-1.3
Structural adjustment (% of potential GDP)	*0.2*	*0.2*	*0.1*	*0.1*	*0.3*	*0.3*
General government debt (% of GDP)	98.4	98.4	98.9	98.7	98.1	96.8
General government debt excluding financial assistance for the euro area (% of GDP)	95.5	95.6	96.2	96.1	95.5	94.3

Comparison with the previous Stability Programme is delicate because of the many events that occurred since then. The economic and social emergency measures introduced in December 2018 have changed the public finance adjustment path. These changes were enacted in the 2019 Initial Budget Act and the Emergency Economic and Social Measures Act. Furthermore, the economic situation is weaker than that underlying the 2018 Stability Programme, with growth expected to stand at 1.4%, instead of the 1.7% growth up to 2022 projected in the previous Programme. The Public Finance Planning Act also updated potential growth and output gap assumptions in a scenario that is more conservative than the previous one.

The 2018 headline deficit was bigger than projected in the 2018 Stability Programme, standing at 2.5% of GDP, versus 2.3%. The larger deficit can be attributed primarily to the base effect of the 2017 deficit, which stood at 2.8% of GDP, versus 2.6%, and stemmed in part from the inclusion of SNCF Réseau in the general government sector, which increased the base deficit by 0.1 percentage points of GDP. This deviation can also be attributed to growth that was 0.4 percentage points weaker. On the other hand, structural adjustment is now slightly greater, standing at 0.2 percentage points of GDP. The headline deficit in 2019 that is larger than projected in the April 2018 Stability Programme can be largely attributed to growth prospects that are even weaker than those in the previous programme, estimated at 1.4% versus 1.9% in the previous programme, along with the emergency measures that will reduce structural adjustment, from the previous level of 0.3 points of potential GDP to 0.1 points under the current multiyear adjustment path. The 2020 headline deficit should be larger than forecast in the previous Stability Programme. Once again, the larger deficit can be attributed to weaker growth and the impact of the emergency economic and social measures. Structural adjustment should also be weaker at a level of 0.1 points of potential GDP. In 2021 and 2022, the structural adjustment path will be close to the one under the previous forecast and nominal adjustment is expected to be hampered primarily by the less favourable macroeconomic environment.

4.3 COMPARISON WITH THE EUROPEAN COMMISSON'S PUBLIC FINANCE FORECASTS

TABLE 15: COMPARISON WITH THE EUROPEAN COMMISSION'S FORECASTS

	2018	2019	2020	2021	2022
European Commission's projections (Autumn Forecast, November 2018)					
Real GDP growth (in %)	1.7	1.6	1.6		
General government net lending (% of GDP)	-2.6	-2.8	-1.7		
Structural balance (% of potential GDP)	-2.5	-2.3	-2.2		
Structural adjustment (% of potential GDP)	*0.0*	*0.2*	*0.0*		
General government debt (% of GDP)	98.7	98.5	97.2		
2019-2022 Stability Programme (April 2019)					
Real GDP growth (in %) (*)	1.6	1.4	1.4	1.4	1.4
General government net lending (% of GDP)	-2.5	-3.1	-2.0	-1.6	-1.2
Structural balance (% of potential GDP)	-2.1	-2.1	-1.9	-1.6	-1.3
Structural adjustment (% of potential GDP)	*0.2*	*0.1*	*0.1*	0.3	0.3
General government debt (% of GDP)	98.4	98.9	98.7	98.1	96.8

* No adjustment for working days

The European Commission's Autumn Forecast published on 8 November 2018 called for France's general government deficit to stand at 2.6% of GDP in 2018, followed by 2.8% in 2019 and 1.7% in 2020 (based on a "no-policy-change" scenario for 2020).

The Commission's latest forecast for 2018 does not incorporate the 2018 outturn that Insee estimated in March 2019. GDP growth was ultimately estimated at 1.6%, versus the projected 1.7% growth in the Commission's forecasts. Insee now estimates the deficit at 2.5% of GDP, versus 2.6% in the Commission's Autumn Forecast.

The Commission predicted a general government deficit standing at 2.8% of GDP in 2019 and structural adjustment of one quarter of a percentage point of potential GDP, versus the deficit standing at 3.1% of GDP and 0.1 percentage points of structural adjustment forecast in this Stability Programme. The difference between these two paths can be attributed primarily to the impact of the emergency economic and social measures introduced in December 2018, well after the Commission issued its forecasts.

The two forecasts for 2020 are no longer comparable, since the Commission's no-policy-change forecast does not include all of the discretionary tax measures and the measures to contain expenditure, particularly local government expenditure, that the Government is considering in order to reduce the general government deficit. Furthermore, the 1.6% GDP growth rate in the Commission's forecasts is higher than the 1.4% forecast in this Stability Programme and the Commission's forecast for 2020 does not consider the impact of the emergency measures introduced in 2019 either.

5.

QUALITY OF PUBLIC FINANCES

Quality of public finances

5.1 QUALITY OF PUBLIC EXPENDITURE

5.1.1 CENTRAL GOVERNMENT AND CENTRAL AGENCIES EXPENDITURE

The Government is intent on improving the effectiveness and quality of central government expenditure and that of central agencies through several means. The objective is to reduce operating expenditure and the least economically effective transfers, to contain wage bill growth and increase investment expenditure instead.

To this end, the **Government is continuing to reduce the number of subsidised employment contracts,** which have failed to prove their effectiveness in drawing people back into employment. At the same time, the Government will step up the **implementation of the employment inclusion fund,** which pools policy resources at the regional level for job skills and inclusion through employment schemes. The fund will provide regional prefects with more resources to promote better coordination of tools for providing personalised support for jobseekers and to adapt policies to local conditions.

The purpose of the Great Investment Plan is to finance implementation of structural reforms to boost the growth potential of France's economy. The Plan has an endowment of €57bn over the government's five-year term. It will finance public investment to address the four major challenges facing France's economy: i) building a knowledge society; ii) accelerating ecological transition; iii) building competitiveness through innovation; iv) building government for the digital age. In 2019, the Great Investment Plan will continue to ramp up its investment, with a total of €9.4 billion in projected investments, mainly in the central government and central agencies budget.

In addition to the Great Investment Plan, further resources will be allocated over the Government's five-year term for sovereign functions. These functions include the justice system, law enforcement and defence, and the new resources will enhance the exercise of these functions in order to meet today's challenges.

Furthermore, medium-term improvements in the effectiveness of government expenditure will result from the **reforms set out in ministries' transformation plans.** These reforms will reduce the number of public sector jobs. Fiscal tools have been created to support these reforms. These tools are devoted to implementing government transformation in the ministries. They include:

- **The public action transformation fund (FTAP):** the purpose of this fund is to finance transformation projects that aim to improve the effectiveness and efficiency of public services that are selected through calls for projects. The projects financed by the fund should provide a high return on investment in the form of lasting operating expenditure savings. Each euro invested should result in a euro in lasting savings after three years. The first allocation of €200 million euros in 2018 went to 16 winning projects that relate mainly to digital technology. A further allocation of €245 million has been opened for 2019. A total of €700 million will be invested over the Government's five-year term.
- **The interministerial human resources support fund (FAIRH):** this fund was set up by the 2019 Initial Budget Act and endowed with €50 million in 2019. It co-finances the transition costs incurred in implementing structural reforms that have a major impact on human resources. The projects selected must facilitate geographical and functional mobility between ministries and mobility between public sector employers and mobility towards the private sector.

Government transformation also relies on **modernisation of management control.** This development produced the ministerial orders of 28 December 2018, which suspended upstream budgetary audits relating to personnel expenditure temporarily. The orders also suspended upstream budget audits for other types of expenditure, in keeping with the situation of each ministry. More frequent access to information and the expansion of downstream audits will enable auditors to target their work more accurately. This will make their audits more appropriate and renew the focus on the sustainability and quality of budget accounting, which is a core management control task.

At the same time, **experimental mergers of the departments** responsible for executing expenditure will take place (shared service centres and invoice processing units). The purpose of these mergers is to reduce redundant audits by authorising officers and accountants in central government.

These different changes in government expenditure execution testify to the coordinated steps taken to reduce full audits and **promote more effective audits and more accountability.**

Moves to empower government managers and improve relationships with them took shape in 2018 and will continue in 2019, with **the signature of multiyear contracts between the Budget Directorate and central government departments or agencies** working to transform their action and/or their models. The purpose of these contracts is to provide greater clarity for managers so that they can successfully transform the structures that they manage.

The quality of public management will also be enhanced by an overhaul of the civil service. The civil service transformation bill submitted to the Cabinet on 27 March 2019 aims to enhance the effectiveness of industrial relations, expand the use of contract employees in the public sector and facilitate mobility for all employees for the sake of greater efficiency in general government.

The Government will also continue its work to make the central government budget more sincere. This effort bore fruit in 2018, when the set-aside rate was lowered to 3%, no supplemental appropriation decrees were issued during the year and the budget overruns highlighted by the French Government Audit Office in its 2017 public finance audit were resolved. This effort is continuing, with a €200 million increase in the provision for external operations compared to the 2018 Initial Budget Act.

5.1.2 CONTAINING HEALTHCARE EXPENDITURE

The strategy for transformation of the healthcare system launched on 13 February 2018 set out five major projects: quality and appropriateness of care, financing procedures, digital technology, human resources and training, local organisational structures. Consultations on the five projects were completed on 18 September 2018 when the President of the Republic presented the “My Health 2022” plan. Several of the measures under this plan have already been passed or are included in the healthcare system organisation and transformation bill submitted in February 2019. The purpose of the bill is to achieve a better organisation of the healthcare system at the local level, enhanced access to care and closer cooperation between healthcare providers and professionals, ensuring high quality and secure healthcare for everyone.

The 2018-2022 national healthcare expenditure growth target plan to support transformation of the healthcare system is fully in line with the overall medium-term framework. It lays the foundations for the transformations to be initiated to enhance the efficiency of the system and to ensure the sustainability of healthcare expenditure. Investment will play a dominant role in the modernisation and adaptation of the healthcare system.

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

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

These structural objectives will be broken down into annual targets when setting the national healthcare expenditure growth target (Ondam). The monitoring of this target has been effective as shown by the fact that it was achieved in 2018 with no increase in the hospitals’ deficit, according to the available provisional data.

5.1.3 STREAMLINING LOCAL GOVERNMENT EXPENDITURE

Under the terms of Article 13 of the 2018-2022 Public Finance Planning Act, local governments have been asked to achieve €13 billion in operating expenditure savings relative to the spontaneous growth rate over the Government’s five-year term, while maintaining their investment expenditure. The 2018-2022 Public Finance Planning Act sets out **two participatory procedures for local governments to streamline their expenditure.**

Article 13 of the Act also sets a **national operating expenditure growth target** of 1.2% in nominal terms for local governments. The 322 governments with budgets in excess of €60 million were invited to sign **finance contracts with central government.** The contracts were implemented in 2018 and will run for three years in accordance with Article 29 of the 2018-2022 Public Finance Planning Act.

Local governments’ acceptance of this approach has been high, with 229 local governments deciding to sign a contract with central government. This represents more than 70% of the 322 local governments concerned by the contracts. A further 17 local governments sought to sign a contract voluntarily, but without any binding targets. The local consultations held by the prefects and the target modulation provisions of the Act (+/- 0.45%) made it possible to tailor the efforts required of each local government to their individual situation, while still ensuring that the operating expenditure growth target of 1.2% was met at the national level.

The provisional results for 2018 are good, with significantly slower growth of aggregate local government operating expenditure, standing at 0.7% in the cash-based budget accounts. The results for the 322 local governments covered by the contract procedure were even better, with growth of 0.3%. Other local governments came close to meeting the target, posting 1.3% growth of their operating expenditure. Containment of local government expenditure can be attributed in part to containment of wage bill growth at approximately 0.8% for all local governments. On the other hand, the growth of local governments' investment expenditure, including subsidies, remained strong, at 4.2%.

PROVISIONAL 2018 OUTTURN IN THE BUDGET ACCOUNTS ISSUED AT THE END OF JANUARY 2019

Growth of actual operating expenditure	Aggregate local government	322 local governments covered by the contract procedure	Other local governments
Target	+1.2%	+1.2%	+1.2%
Outturn	+0.7%	+0.3%	+1.3%
of which wage bills	+0.8%	+0.8%	+0.9%
of which intermediate consumption	+1.2%	-0.4%	+2.7%

The Government will present the results of the provisions to contain local government expenditure growth in 2018 before the budget policy debate for the 2020 budget. A second set of results will be broken down for each category of local government and submitted in the fourth quarter of 2019. Local governments that exceeded their operating expenditure growth target will be subject to the **clawbacks provided for in the 2018-2022 Public Finance Planning Act by the end of 2019.** The clawbacks will be equivalent to 75% or 100% of the overrun, depending on whether the local government signed a contract with central government. The clawbacks are capped at 2% of actual operating revenue in the 2018 budget.

The results testify to the soundness of the Government's partnership approach. The local governments' individual presentations of expenditure growth targets during the budget policy debate help to enhance **ownership of the procedure.** It enables each local government to **compare, analyse and improve its efforts to streamline expenditure.**

At the same time, work is underway in 2019 to prepare cost guidelines to help local governments identify areas for savings and optimising local management. This work focused on education-related activities initially, but it could be expanded later to other public policies.

5.2 QUALITY OF PUBLIC REVENUE

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

The cut will reduce the tax burden on French corporations and households, which hinders demand and private-sector initiative. The decline in the aggregate tax and social security contribution rate will continue, with a cut of a bit more than one percentage point of GDP by 2022. This cut will benefit both households and corporations. The cut would be 1.2 percentage points and 1.4 percentage points after restatement for the phased integration of France Compétences. In the years covered by the Public Finance Planning Act, the aggregate tax and social security contribution rate will fall from 45.2% of GDP in 2017 to 44.0% in 2022 (or 43.8%, excluding France Compétences). This reduction corresponds to three strategic choices made by the Government. The first choice is to continue the cuts introduced in 2018 to provide immediate support for growth, promote employment and boost purchasing power by providing greater rewards for working. The second choice is to improve competitiveness and unleash enterprise, and the third is to support private-sector investment in businesses that take risks, innovate and create the jobs of tomorrow.

MODERNISING TAXATION AND REDUCING THE BURDEN FOR THE LEAST WELL-OFF HOUSEHOLDS

These tax cuts are largely for households and will primarily benefit middle-class workers and low-income households. For this purpose, private-sector employees' contributions for health and unemployment insurance have been abolished and replaced by a higher rate of the General Social Security Contribution. The latter is levied on a broader base, which makes it possible to widen the tax bases used to finance social security instead of relying solely on levies on wages. At the same time, pensioners with the lowest incomes are still protected. In December 2018, the exemption from the General Social Security Contribution was expanded to pensioners with net monthly incomes of less than €2,000. In addition to providing workers with a significant purchasing power gain, these cuts will stimulate both labour demand and labour supply by reducing the tax wedge on wages. These measures were amplified in 2019 with an exemption from taxes and contributions for overtime pay. At the same time, households will continue to benefit from the phased elimination of the residence tax, except on second homes, providing a boost for purchasing power and more equitable taxation. The implementation of withholding at source for personal income tax, starting on 1 January 2019, constitutes a major advance in terms of modernising taxation (see Box 9).

SUSTAINING THE MEASURES TAKEN TO BOOST COMPETITIVENESS AND LOWER LABOUR COSTS

Business taxes will be reduced and simplified to make France's businesses more competitive, boost growth and make France's economy more attractive. The corporate income tax rate will be cut in stages down to 25% by 2022. This cut will bring France into line with the European average and reduce the cost of capital, thereby stimulating long-term investment. The Competitiveness and Employment Tax Credit has been replaced by a lasting cut in employers' social security contributions to simplify the existing arrangement and sustain employment and the competitiveness of French businesses in the longer term. The replacement of the Competitiveness and Employment Tax Credit also provides stability for businesses, especially the smallest ones. Contribution cuts will consolidate previous efforts to help businesses restore their profitability, but they will also sustain demand for unskilled labour by targeting minimum-wage jobs more specifically starting on 1 October 2019. Support for the smallest businesses includes the elimination on 1 January 2019 of the social profit-sharing charge for corporations with fewer than 250 employees and on all employee savings plans for corporations with fewer than 50 employees, as well as support from measures under the Pacte bill, which will be introduced in 2019.

SUPPORTING INVESTMENT, ENTREPRENEURSHIP AND INNOVATION

France's wealth tax (ISF) was transformed into a property wealth tax (IFI) in 2018. The year also saw the introduction of a 30% flat tax and social security contribution rate on investment income. These moves will stimulate productive investment that is both risky and innovative. In a time of sweeping technological change, the need for capital is even greater than before and returns on capital need to be raised to promote risk-taking. The different measures are also in line with seeking greater European convergence, since French taxes on capital were particularly high compared to its European partners. In addition to helping reduce the cost of capital, these measures will channel more domestic savings into financing businesses. A digital services tax will also be introduced in 2019 to ensure that digital giants pay taxes in proportion to the value created by their customers in the French market. This provision was submitted on 6 March 2019 in the bill on taxation of large digital corporations.

Box 9 – Withholding at source for personal income tax: modernising household taxation

Since 1 January 2019, personal income tax has been withheld at source. This modernisation of tax collection was initially planned for 2018, but the launch was deferred for one year to ensure that the system is completely reliable.

This major reform will eliminate the one-year lag between receiving taxable income and paying tax on it, thereby easing problems that taxpayers may have in paying their tax bills.

For employees, withholding at source simplifies taxes for wage-earners, since it relies on tax rates applying to current income and responds immediately to changes in taxpayers' incomes and tax status in the event of marriage, births or retirement.

For employers, withholding at source will rely on the single staff reporting statement (DSN), which will simplify formalities and produce savings.

In addition, withholding at source of personal income tax complies with the founding principles of the French tax system:

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

Entities (employers, pension funds, etc.) paying wages, salaries, and income support payments such as retirement or unemployment benefits, will withhold taxes at source on behalf of the central government, using withholding rates calculated by the tax administration. Other income covered by this reform, such as self-employment income and property income, will give rise to contemporaneous advance tax payments made by the taxpayers themselves.

In order to avoid a double tax burden for households in 2019, the income subject to the new withholding at source and earned in 2018 will not be taxed. More specifically, the tax owed on recurring income earned in 2018 and subject to withholding at source from 2019 onwards will be cancelled out by a special tax credit (called Collection Modernisation Tax Credit – CIMR). Nonetheless, tax reductions and credits acquired in 2018 shall remain valid, and the taxpayers concerned received an advance of 60% of such reductions and credits in January 2019 (totalling €5.5 billion). The remaining amount will be settled when the tax assessments are sent out in the third quarter of 2019. Non-recurring income, which is by nature unlikely to be taxed twice in 2018, will still be subject to income tax and the Collection Modernisation Tax Credit for income earned by self-employed workers and company managers in 2018 will be subject to specific rules to prevent tax minimisation arrangements.

The net fiscal impact of switching to withholding at source is estimated to be neutral overall in 2019. This estimate, which may be affected by unforeseen events, incorporates the impact of demographic and macroeconomic developments, of possibilities for modulating withholding rates and of the effect the reform will have on tax collection rates. However, this estimate is still sensitive to macroeconomic developments, tax collection rates during the transition phase, the proportion of taxpayers modulating their withholding rates during the year, and potential manoeuvres by taxpayers aimed at maximising their untaxed income in 2018.

6.

SUSTAINABILITY OF PUBLIC FINANCES

Sustainability of public finances

6.1 SUSTAINABILITY OF GENERAL GOVERNMENT DEBT

6.1.1 IMPACT OF THE AGEING POPULATION ON PUBLIC FINANCES

A strong birth rate, an increasing employment rate for older workers and reforms enacted over 20 years ago have placed France in a strong position to deal with its ageing population compared to its European partners. These demographic trends make it easier to balance the pension system's finances and to ensure long-term fiscal sustainability according to the latest domestic[26] and European forecasts[27].

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

In July 2018, the Pension Steering Committee upheld its 2017 recommendations to the Government based on new expenditure projections from the Pensions Advisory Council. The recommendations deal with the measures needed to put the pension system on the path to financial equilibrium. The Pension Steering Committee did not make any new recommendations but insisted on the need to "enhance the transparency, clarity and governance" of the system.

The Government is working on a major reform project for the pension system. Several consultations have been held with citizens and with labour and management representatives. The reform should be passed in 2019. The purpose of the reform is to build a simpler and more equitable universal system. It will ensure that everyone receives the same benefits for each euro contributed, while maintaining the solidarity mechanisms. The system will be easier for workers,to understand thereby promoting professional mobility. Greater clarity will also make financial steering of the system more effective. This steering needs to consider life expectancy gains with each succeeding generation, in order to give workers new confidence in the sustainability and fairness of our retirement system. The reform framework will set out the procedures for gradual unification of the different retirement schemes.

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

On the other hand, its aging population means that France is facing an increase in the number of people needing long-term care. The French Directorate of Research, Studies, Assessment and Statistics (DREES) from the Ministry of Solidarity and Health projects that government expenditure on long-term care will increase by 1 percentage point of GDP between 2014 and 2060, rising from 1.1% of GDP to 2.1%. At the same time, total government and private-sector expenditure will increase by 1.4 percentage points of GDP, from 1.4% of GDP to 2.8%. These projections are made on the assumption of no changes to legislation or to the share of general government expenditure in total expenditure. This share stands at 79%, due to the fact that virtually all healthcare expenditure on people in long-term care is covered by social security funds.

The increase in expenditure will be strongest between 2030 and 2045, as the baby-boom generation reaches the ages when the need for long-term care is the greatest. This one-off demographic effect will be compounded by a more structural effect related to aging of the population, which is longer life expectancy. The Libault report, drafted after the "Old Age and Independent Living" consultations, makes a number of proposals for reforming the provision of long-term care. These proposals lay the groundwork for the Government's bill to be submitted in the third quarter of 2019.

The projections submitted to the High Council of Social Security Financing (HCFiPS) and the High Council of the Future of Health Insurance (HCAAM) show an increase of 1 percentage point of GDP in the consumption of medical care and goods between 2017 and 2060, in a median macroeconomic scenario based on the assumption that the elasticity of healthcare expenditure to GDP growth is equal to one. The increase in percentage points of GDP will be greater, at 1.3

[26] See Conseil d'orientation des retraites, 2018, "Évolutions et perspectives des retraites en France – rapport annuel du COR", June 2018. The next annual report will be published in June 2019.

[27] See European Commission, 2018, "2018 Ageing Report: economic and budgetary projections for the 28 EU Member States (2016-2070)", May 2018.

points by 2060, if the elasticity is greater (1.4, reverting towards 1) as a result of technological progress causing expenditure growth to outstrip GDP growth.

6.1.2 LONG-TERM SUSTAINABILITY (S2)

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

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

According to the S2 sustainability indicator calculated using the AWG's new projections up to 2070, long-term debt stabilisation will be achieved, even if the structural primary balance remains at its 2018 level in the years from 2019 to 2022. The S2 is - 0.1 points of GDP in this scenario, indicating that no additional adjustment is necessary to achieve a stable debt-to-GDP ratio in the long term. The expected favourable impact of the ageing population slightly exceeds the initially forecast deviation of the structural primary balance from the debt-stabilising balance (see Table 16).

The savings set out in this Stability Programme should allow France to improve its S2 indicator considerably. The structural effort planned for 2019-2022 should reduce the necessary adjustment related to the initial fiscal position by 0.9 percentage points of GDP. S2 should stand at -1.0% of GDP in 2022, based on the assumptions used in this Stability Programme. As from 2022, all the conditions should be in place for a substantial reduction in the long-term debt-to-GDP ratio.

Even if the years after 2060 were excluded from the calculation of the indicator, long-term debt would be nearly stable. Those years are particularly favourable for the sustainability of public finances because of the projected decrease in ageing-related costs after 2060. S2 would stand at 0.2 points if those years were excluded, with a structural primary balance maintained at its 2018 level, and at -0.6 points, if we include the savings described in this Stability Programme.

TABLE 16 - FISCAL SUSTAINABILITY GAP INDICATOR S2 (PERCENTAGE POINTS OF GDP)

Base year	Same scenario for 2019 to 2022	Stability Programme scenario
Sustainability gap (S2 indicator)	**-0.1**	**-1.0**
o.w. impact of the initial budget position	+1.5	+0.6
o.w. impact of the ageing population (as of 2022)	-1.6	-1.6

NB:

- The S2 sustainability indicator is estimated on the basis of a counterfactual scenario where the structural primary balance is assumed to be constant at its 2018 level for the duration of the programme (2019-2022), independently of the impact of the ageing population. It corresponds to the long-term fiscal adjustment that would have to be achieved in 2022 to stabilise the very long-term debt-to-GDP ratio (2070 in this case), in view of the impact of the ageing population after 2022.
- The S2 indicator is estimated on the basis of the 2022 structural primary balance expected under this programme. It corresponds to the long-term fiscal adjustment that would have to be achieved in 2022 to stabilise the very long-term debt-to-GDP ratio in view of the impact of the ageing population after 2022.
- The ageing-related expenditure projections (pensions, healthcare, long-term care, education, unemployment) are taken from the European Commission's 2018 Ageing Report, which was published at the end of the first half of 2018.

6.2 CONTINGENT LIABILITIES

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

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

Central government guarantees cover a wide range of actions to sustain or preserve economic activity or to provide financing for certain economic agents when market financing is inadequate. These guarantees are given under clear-cut agreements and they include in particular: central government debt guarantees, guarantees related to general interest functions (insurance mechanisms operated through the central reinsurance fund, guarantees to protect savings, etc.), liability guarantees (e.g. for France's share of ESM callable capital) and central government financial commitments for co-financing projects and providing development assistance. Generally speaking, the risk of such guarantees being invoked is small. The central government's role in regulating both the economy and French society also means that it is committed to providing budget-balancing subsidies, particularly to the special pension schemes.

In 2017, the aggregate outstanding central government guarantees under clear-cut agreements, meaning all central government debt guarantees, came to €204bn compared to €195bn in 2016. Some of the guarantees provided increased between 2016 and 2017. The largest increases were in the guarantees provided to the European Financial Stability Facility (up by €8 billion between 2016 and 2017), to the management company of the Guarantee Fund for Low-Income Homebuyers (SGFGAS), which was up by €3 billion, matching the increase in 2016, and to the unemployment insurance scheme (Unédic), which increased by €3.5 billion in both 2016 and 2017. These increases were partially offset by the reduction of other guarantees, such as the outstanding guaranteed debt of Caisse Central du Crédit Immobilier de France (3CIF), which decreased by €5 billion. It should be noted that the debt of the unemployment insurance scheme, which is part of general government, is already included in Maastricht debt. Furthermore, guarantees for EFSF loans under financial assistance programmes are now recognised as part of the Maastricht debt of the Member States, in proportion to the share of the guarantees they provide, following Eurostat's decision of 27 January 2011. The bilateral sovereign loans granted by the French development agency that come with explicit central government guarantees are already counted as part of the Maastricht debt.

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

France monitors these risks in three ways:

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

6.3 ONGOING REFORMS TO MEET MAJOR ECONOMIC CHALLENGES

In addition to the fiscal measures set out in this Stability Programme, France is implementing a reform strategy presented in detail in the National Reform Programme. This strategy is aimed achieving sounder, more inclusive and more sustainable growth. The strategy was rolled out in the third quarter of 2017 and is continuing in 2019. The strategy addresses four challenges: recasting our social model to build a more equitable society; unleashing the full potential of France's economy; developing tomorrow's growth model; transforming central government and balancing public finances.

RECASTING OUR SOCIAL MODEL TO BUILD A MORE EQUITABLE SOCIETY

In international comparisons, our social model ensures a lower poverty rate and a lower level of inequality by means of significant redistribution of wealth. However, our model is less able to ensure genuine equality of opportunity. Building a just society requires greater social mobility by correcting the sources of inequality. This includes ensuring access to employment and social security for everyone.

Employment should be the primary protection for individuals. For this purpose, labour laws have been reformed to adapt them to the situation on the ground and employees who resign and self-employed workers are now covered by unemployment insurance. The vocational training system has been reformed to facilitate transition between jobs. This reform has been backed up by a massive €15-billion investment in skills training through the "Building a Knowledge Society" pillar of the Great Investment Plan, with the primary focus on unskilled workers, along with reform of subsidised employment contracts, with greater emphasis on providing support for jobseekers, and the extension of the Youth Guarantee scheme.

Enhancing work through higher pay is also at the heart of our strategy. The in-work benefit was increased significantly on 1 January 2019. This increase, combined with the regulatory increase in the minimum wage on the same date, has boosted minimum wage earners income by €100 per month. Overtime pay has been exempt from all taxes and contributions since 1 January 2019. In addition, measures to promote profit-sharing and employee share ownership in the PACTE bill will give employees a greater stake in their employers' success. This movement to ensure a fairer share of value started in early 2019 with the introduction of an exceptional bonus to boost purchasing power, which is tax exempt up to €1,000. These measures complement the €20-billion cut in employees' social security contributions, which will be financed in part by an increase in the general social security contribution rate. The monthly income threshold over which the higher rate applies was increased to €2,000 to protect pensioners' purchasing power.

Our social model needs to reduce inequality of opportunity by helping everyone, regardless of circumstances or age. We need to start by ensuring more equal access to healthcare and better disease prevention (extending vaccination requirements, higher tobacco prices), by making sure everyone can afford healthcare ("100% Santé" agreement on the "zero out-of-pocket" scheme) and by promoting access to healthcare for everyone under the "My Health 2022" plan (medical school reform, creation of local community hospitals). The introduction of an equality index will provide a practical tool for fighting gender pay disparities. Finally, a systemic reform of our retirement pension system will be submitted in 2019 with the aim of making the system fairer and easier to understand, while making sure that each euro contributed procures the same benefits for everyone.

Government action is also aimed at reducing disparities between local communities including access to the Internet (Broadband Plan), access to healthcare (plan to fight medical deserts) or nationwide access to transport (Transport Planning Bill). Specific action plans target certain areas in decline, such as priority urban neighbourhoods (QPV), which will benefit from an extension of the "emplois francs" subsidies for employers hiring residents of these areas. Medium-sized cities will be eligible for specific contracts to revitalise their city centres under the "Heart of the City" action plan, and manufacturing regions will be eligible for the "Industrial Lands" initiative.

The national strategy to fight and prevent poverty will prioritise attacking the causes of poverty **to provide better protection for the most vulnerable.** The early childhood policies will be enhanced by targeting underprivileged neighbourhoods, as well as by stressing inclusion through employment and skills training. In addition, a project to overhaul minimum social benefits has started with a view to introducing a universal activity benefit (revenu universel d'activité), to replace various existing benefits. A public support service has been established to provide guidance and support for the long-term unemployed in returning to the labour force.

UNLEASHING THE FULL POTENTIAL OF FRANCE'S ECONOMY

Our country needs to seize the opportunities offered by the on-going technological revolution and by the growing interconnectedness of economies to create a more prosperous society. This means unleashing the entrepreneurial potential of France's economy through reform of the labour market, the tax system and the business environment.

Labour market reform has started, first with ordinances on strengthening labour relations, adopted back in 2017. These ordinances give company-level collective bargaining a central role. They provide more security in labour relations by introducing a fixed scale for labour tribunal awards in cases of wrongful dismissal. These reforms bring labour relations closer to workers and the real-world problems of companies. At the same time, reform of unemployment insurance rules is under way, with several goals in mind: fighting job insecurity and excessively short employment contracts, providing incentives for finding steady employment and more support for jobseekers.

Another means used to promote economic growth is tax simplification and relief, particularly with regard to taxes on capital, in order to encourage business investment and job creation (cutting corporate income tax rate to 25% by 2022, introduction of the flat tax on investment income, introduction of the property wealth tax and the replacement of the Competitiveness and Employment Tax Credit with a cut in social security contributions). The elimination of the residence tax, the introduction of withholding at source for personal income tax and the tax on digital services have made our tax system more effective and equitable.

Unleashing economic growth means improving the business environment. The action plan for business growth and transformation (PACTE) marks a significant step forward in reducing the restraints on business growth (higher thresholds) by facilitating financing (measures relating to retirement savings, life insurance, facilitating market offerings, developing equity investment vehicles), enhancing their innovative potential (measures relating to researchers) and by reforming insolvency law (cross-class cram down mechanism). Furthermore, the increase in thresholds for the certification of companies' accounts and provisions that facilitate changing supplementary health insurance providers will increase competition and make our economy more competitive. Other measures to increase competition in the service industry and boost consumers' purchasing power have been announced dealing with automotive spare parts, driving schools, building management companies, etc.

DEVELOPING TOMORROW'S GROWTH MODEL

There can be no lasting growth without the emergence of a new model that reconciles prosperity, social progress and ecology in order to address the ecological and digital challenges ahead. This will require sweeping transformations and massive public sector and private sector investment efforts.

Our entire education and training system has been revamped to make it more effective and more equitable in order to achieve a new growth model based on skills and knowledge. For this purpose, elementary school class sizes in priority education areas have been halved and the mandatory school enrolment age has been lowered from 6 years to 3 years. These changes are especially effective means of reducing education inequality at a very young age. Secondary education reforms call for a revamp of the baccalaureate examination starting in 2021. The transformation of vocational schools will provide a better grounding in the skill sets of the future and apprenticeship reforms will enhance the attractiveness of this path to excellence. Access to university education has been reformed to end admission lotteries and should make it possible to fight the particularly high failure rates for undergraduates by rebuilding the higher education curriculum.

A very bold ecology and solidarity target has been set for a sustainable growth model, with the objective of achieving carbon neutral growth by 2050. The national low-carbon strategy and the multiyear energy plan set out the means of achieving this objective. More specifically, a major public investment effort has started, with €20 billion allocated to the "Faster Energy Transition" pillar of the Great Investment Plan, including €9 billion for improving the energy efficiency of low-income housing and public buildings. Ecological transition requires a massive support effort to help the population change behaviours at every level. The various incentives have been enhanced significantly in 2019, including the energy cheque and the conversion bonus.

The growth of tomorrow will also need to be sustained by an innovation economy. For this purpose, large-scale public investment in research, innovation and product improvement has taken place. Of the €57 billion under the Great Investment Plan, €13 billion in public funds have been invested in innovative projects, particularly in the agricultural sector. In addition, an industry and innovation fund has been set up to invest in disruptive innovation. A multiyear research planning bill should be submitted to Parliament at the end of 2019 to give laboratories more predictable funding and identify the major research programmes that are strategic for France.

Transformations of key sectors of the French economy were carried out in 2018 to enhance our growth model, particularly in the rail sector (new railway sector pact), the housing sector (ELAN Act) and the agricultural sector (EGAlim Act).

TRANSFORMING CENTRAL GOVERNMENT AND BALANCING PUBLIC FINANCES

The transformation of our model must include the public sector, since public services and the social protection system are at the heart of our republican pact. Furthermore, increasing government expenditure brings with it increasing taxes and social security contributions, which are a burden for our economy and do nothing to improve the satisfaction of public service users. Therefore, we need to reform our public services and reduce government expenditure as a share of GDP.

Improving the quality of public services must start with an effort to simplify formalities and the regulatory environment for businesses. More specifically, the objective of having 100% of public services available online is still being pursued.

The way the central government operates will need to undergo sweeping change. To this end, the fund for government transformation (FTAP), with an endowment of €700 million over 5 years, will support long-term internal transformations to improve the quality of the services provided. In addition, the civil service transformation bill submitted on 27 March 2019 will improve government management through more effective labour relations, wider use of contract employees in public-sector jobs and facilitation of employee mobility. The bill will give government employees more structured and varied career paths, thereby improving the quality of public services.

The Government will continue various reforms as part of the gradual fiscal consolidation effort over its five-year term.

7.

INSTITUTIONAL ASPECTS AND FISCAL GOVERNANCE

Institutional aspects and fiscal governance

7.1 FULLY OPERATIONAL FISCAL GOVERNANCE

The Constitutional Bylaw (loi organique) of 17 December 2012 overhauled both public finance steering and its institutional framework. Changes to fiscal management include an introductory article for Budget Acts that supplements public finance steering based on the fiscal balance with targets defined in structural terms and a multi-year outlook.

Changes to the institutional framework include the creation of the High Council of Public Finance (Haut Conseil des finances publiques, HCFP), which is tasked with issuing an opinion on the macroeconomic forecasts underlying the Stability Programme, draft budgets and draft social security budgets, and their consistency with the multiyear structural balance guidelines set out in the Public Finance Planning Act. The High Council also identifies potential deviation of the budget outturn from the multiyear forecast during the debate on the draft Budget Review Act. In the event of a significant deviation, the High Council can trigger the correction mechanism, requiring the Government to set out in detail measures to correct the path in the draft budget or in the draft social security budget for the following year. The opinions issued by the High Council on these draft budgets include an assessment of these measures. **The High Council provides Parliament, the Constitutional Council and outside observers with an independent assessment of the Government's forecasts.** It has issued 28 opinions on budget bills and Stability Programmes presented by the Government since April 2013.

Alongside this new institutional framework, fiscal rules and targets set out in successive Public Finance Planning Acts have resulted in a significant improvement in fiscal governance. The main guidance and regulations for the major general government sub-sectors are as follows:

- For central government: target for discretionary central government expenditure and aggregate central government expenditure target, caps on ministries' expenditure, adjustment path for tax expenditures, ban on real-property financial leasing;
- Other central government bodies (ODAC): cap on central agencies' expenditure, ban on other central government bodies' incurring debt with maturities of more than 12 months, provisions to restrict the number and cap tax earmarks, supervision of public-private partnerships;
- For local government: ban on borrowing to cover operating expenditure, target for local government expenditure growth (ODEDEL) and introduction of contracts with local governments to contain the growth of their actual operating expenditure;
- For social security funds: national healthcare expenditure growth target (Ondam), adjustment path for reducing administration costs for basic social security schemes under the terms of objectives and management agreements, setting an expenditure target for basic social security schemes, adjustment path to reduce contribution exemptions and rate reductions, monitoring hospital wage bills, cap on social security funds' short-term borrowing.

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

7.2 STATISTICAL GOVERNANCE

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

The **semi-final and final** general government accounts, published with lags of two years and three years respectively, are compiled on the basis of detailed accounting information[28]. The main information source for the central government

[28] This means Insee will publish the semi-final 2017 accounts and the final 2016 accounts in May 2019.

is the budget outturn, supplemented by the central government's financial statements (accrual-based financial statements, which are certified by the French government audit office (Cour des comptes). Restating the budget outturn as government net lending requires a series of adjustments to correct for some time lags and for the difference in treatment of certain transactions in budgetary cash-based accounting and in the system of national accounts. Compiling the "Other central government bodies" account, which mainly covers central agencies, involves restating each of the agencies' accounts in the national accounts format. The data for the local government sector (APUL) come from the individual management accounts kept by Public Finances Directorate General accountants. The accounts of the social security funds (ASSO) are compiled from the accounts of the various funds, public hospitals and private hospitals providing public healthcare services, the unemployment insurance scheme (Unédic) and Pôle Emploi, France's public employment service agency, along with the accounts of complementary retirement scheme management bodies (such as Agirc and Arrco). Insee has revised the social security funds accounts every year since September 2013 using supplementary accounting data, ahead of the semi-final accounts.

The data available for the **provisional general government account,** published three months after the end of the year, are still incomplete. The central government budget cycle ends in mid-January of the following year (y+1) and the central government's public accounts are closed towards the middle of March of the following year (y+1). Consequently, the data published on 25 March of the following year (y+1) (26 March in 2019) are virtually final and any minor revisions made later relate primarily to the adjustments required to bring them into line with the national accounts format. The central agencies' account uses data derived directly from accounting sources that cover approximately two thirds of revenue and expenditure. The preferred sources for local governments are the data reported in the central government's accounting documents and direct, comprehensive and centralised data for regions, départements and municipalities, as well as a sampling of various local government bodies. For the March release, the social security accounts are partially based on estimates, since the different schemes have not yet produced their full financial statements, even though the general social security scheme compiles its financial statements in March. Nevertheless, a large number of accounting data (e.g. from the general social security funds, public hospitals, etc.) are used. The provisional accounts provide a good estimate of the general government balance and revisions to the balance for the final accounts are fairly minor[29].

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

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

7.3 STATUS OF THIS STABILITY PROGRAMME UNDER INTERNAL PROCEDURES

The Stability Programme was presented to Parliament on 10 April 2019.

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

On 10 April 2019, the High Council of Public Finance published its opinion on the macroeconomic forecasts underlying the Stability Programme for 2019 to 2022. This opinion was appended to the Stability Programme when it was submitted to the Council of the European Union and to the European Commission at the end of April 2019.

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

8.

APPENDIX

Appendix

8.1 STATISTICAL TABLES

TABLE 1A. MACROECONOMIC PROSPECTS

	ESA Code	2018* Amount in current € bn	2018 Annual % change	2019 Annual % change	2020 Annual % change	2021 Annual % change	2022 Annual % change
1. Real GDP	B1*g	-	1.6	1.4	1.4	1.4	1.4
2. Nominal GDP	B1*g	2,353.2	2.5	2.6	2.6	2.9	3.1
Components of real GDP							
3. Private consumption expenditure	P.3	1,271.2	0.9	1.6	1.3	1.4	1.4
4. Government consumption expenditure	P.3	546.7	1.1	1.0	1.0	0.5	0.2
5. Gross fixed capital formation	P.51	539.2	2.9	2.1	1.4	1.2	1.6
6. Changes in inventories and net acquisition of valuables (% of GDP)	P.52 + P.53	14.8	-	-	-	-	-
7. Exports of goods and services	P.6	739.2	3.3	2.4	2.7	3.1	3.1
8. Imports of goods and services	P.7	759.8	1.3	2.4	2.3	2.3	2.3
Contributions to real GDP growth							
9. Final domestic demand excluding inventories		-	1.4	1.6	1.3	1.1	1.2
10. Changes in inventories and net acquisition of valuables	P.52 + P.53	-	-0.4	-0.1	0.0	0.0	0.0
11. External balance of goods and services	B.11	-	0.6	0.0	0.1	0.2	0.2

* Seasonally and working-day adjusted data taken from the quarterly accounts (March 2019), with the exception of the nominal GDP in 2019, which corresponds to the figure from the March 2019 release.

TABLE 1B. PRICE DEVELOPMENTS

	ESA Code	2018* Annual % change	2019 Annual % change	2020 Annual % change	2021 Annual % change	2022 Annual % change
1. GDP deflator		0.9	1.2	1.2	1.5	1.7
2. Private consumption deflator		1.7	1.3	1.2	1.5	1.75
3. CPI		1.8	1.3	1.3	1.5	1.75
4. Public consumption deflator		0.1	0.5	0.5	0.9	1.1
5. Investment deflator		1.5	1.6	1.7	1.8	1.9
6. Export price deflator (goods and services)		0.9	1.2	1.4	1.5	1.7
7. Import price deflator (goods and services)		2.2	1.1	1.3	1.5	1.7

*Seasonally and working-day adjusted data taken from the quarterly accounts, March 2019.

TABLE 1C. LABOUR MARKET DEVELOPMENTS

Aggregate economy	ESA Code		2018*	2018	2019	2020	2021	2022
			Level	Annual % change	Annual % change	Annual % change	Annual % change	Annual % change
1. Employment, persons employed[1]			28,186	1.0	0.6	0.5	0.3	0.2
2. Employment, hours worked[2]								
3. Unemployment rate (%)[3]								
4. Labour productivity per person employed[4]			-	0.6	0.9	0.9	1.1	1.2
5. Labour productivity per hour worked[5]								
6. Compensation of employees (including employers' contributions)	D.1		1,251	2.9	0.8	2.2	2.7	3.0
7. Compensation per employee (including employers' contributions)				1.9	0.2	1.7	2.4	2.8

1 Occupied population in thousands, national accounts definition
2 National accounts definition
3 ILO concept
4 Ratio of real GDP growth to employment growth.
5 Real GDP per hour worked
* Seasonally and working-day adjusted data taken from the quarterly accounts, March 2019.

TABLE 1D. SECTORAL BALANCES

% of GDP	ESA Code	2018*	2019	2020	2021	2022
1. Net lending/borrowing vis-à-vis the rest of the world	B.9	-0.7	-0.5	-0.3	-0.1	0.0
of which						
- Balance on goods and services		-0.9	-0.9	-0.7	-0.4	-0.2
- Balance of primary incomes and transfers		0.1	0.4	0.4	0.4	0.2
- Capital account		0.1	0.0	0.0	0.0	0.0
2. Net lending/borrowing of the private sector**	B.9	1.8	2.6	1.8	1.5	1.3
3. Net lending/borrowing of general government***	B.9	-2.5	-3.1	-2.0	-1.6	-1.2
4. Statistical discrepancy						

* Seasonally and working-day adjusted data taken from the quarterly accounts, March 2019.
** Calculated for 2017 as the difference between national net lending from the March 2019 quarterly accounts and the public sector net lending from the 2018 notification.
*** The public sector deficit is based on the GDP figure from the March 2019 notification.

TABLE 2A. GENERAL GOVERNMENT BUDGETARY PROSPECTS

	ESA Code	2018	2018	2019	2020	2021	2022
		Level In €bn	Level % of GDP	Level % of GDP	Level % of GDP	Level % of GDP	Level % of GDP
Net lending/borrowing (EDP B9) per sub-sector							
1. General government	S.13	-60	-2,5	-3.1	-2,0	-1.6	-1.2
2. Central government	S.1311	-73	-3.1	-3,7	-3.0	-3,1	-3.0
3. State government	S.1312	-	-	-	-	-	-
4. Local government	S.1313	2	0.1	0.1	0,2	0.5	0,6
5. Social security funds	S.1314	11	0,5	0,5	0.8	1,0	1.2
General government (S.13)							
6. Total revenue	TR	1,259	53,5	52,4	52,3	52,0	51.7
7. Total expenditure	TE	1,318	56.0	55.5	54.3	53.6	53.0
8. Net lending/ borrowing	B.9	-60	-2,5	-3.1	-2,0	-1.6	-1.2
9. Interest expenditure	D.41	40	1.7	1,5	1,5	1,6	1.7
10. Primary balance[1]		-20	-0,8	-1.5	-0,5	-0,1	0.4
11. One-off measures[2]		-6	-0,2	-1.0	-0,1	0.0	0.0
Selected revenue components							
12. Total taxes (12=12a+12b+12c)		716	30,4	30,5	30,5	30,3	30.0
12a. Taxes on production and imports*	D.2	388	16.5	16,8	16,8	16.7	16.7
12b. Current taxes on income, wealth, etc.	D.5	313	13,3	13,1	13.1	13.0	12.8
12c. Capital taxes	D.91	14	0.6	0.6	0.6	0.6	0.6
13. Social contributions	D.61	425	18,0	16.8	16,7	16,7	16,7
14. Property income	D.4	15	0.6	0,6	0,6	0,6	0,6
15. Other[3] (15=16-12-13-14)		104	4,4	4,5	4,4	4.4	4.4
16=6. Total revenue	TR	1,259	53,5	52,4	52,3	52,0	51.7
NB: Taxes and contributions including tax credits (D.2+D.5+D.61-D612+D.91-D.995)[4]		1,094	46.5	45.5	45,4	45,1	44.8

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

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

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

[4] Including those collected by the European Union and including an adjustment for uncollected taxes and social contributions (D.995).

*Excluding taxes collected by the European Union

TABLE 2A CONTINUED. GENERAL GOVERNMENT BUDGETARY PROSPECTS

	ESA Code	2018	2018	2019	2020	2021	2022
		Level In €bn	Level % of GDP	Level % of GDP	Level % of GDP	Level % of GDP	Level % of GDP
Selected expenditure components							
17. Compensation of employees + intermediate consumption	D.1 + P.2	411	17,5	17,2	17.1	16,8	16,5
17a. Compensation of employees	D.1	294	12.5	12.3	12.1	12.0	11,8
17b. Intermediate consumption (including financial intermediation)	P.2	117	5.0	4,9	4,9	4,8	4,7
18. Social benefits[5] (18=18a+18b)		600	25.5	25,4	25.1	24,9	24,7
of which unemployment benefits		34	1.4	1.4	1,3	1.3	1,2
18a. Social transfers in kind supplied via market producers	D.632	142	6.0	6.0	5,9	5,9	5,8
18b. Social transfers other than in kind	D.62	458	19.5	19,5	19,2	19.1	18,9
19=9. Interest expenditure	D.41	40	1.7	1,5	1,5	1,6	1.7
20. Subsidies	D.3	63	2,7	2,7	2.0	2.0	2.0
21. Gross fixed capital formation	P.51	80	3,4	3.5	3.4	3,2	3.2
22. Capital transfers	D.9	28	1,2	1.0	1,1	1.0	1,0
23. Other[6] (23=24-17-18-19-20-21-22)		96	4,1	4.0	4.0	4.0	3,9
24=7. Total expenditure	TE1	1,318	56.0	55.5	54.3	53.6	53.0
NB: Government consumption (nominal)	P.3						

5 Includes cash benefits (D.621 and D.624) and in-kind benefits (D.631) related to unemployment benefits.
6 D.29+D.4-D.41+D.5+D.7+P.52+NP

TABLE 2B. NO-POLICY-CHANGE PROJECTIONS

	2018	2018	2019	2020	2021	2022
	level	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP
1. Total revenue with no policy change	1,258	53.5	53.5	53.4	53.4	53.3
2. Total expenditure with no policy change	1,328	56.4	56.2	55.9	55.8	55.7

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

	2018	2018	2019	2020	2021	2022
	level In €bn	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP
1. Expenditure on EU programmes fully matched by EU funds revenue	3	0.1	0.1	0.1	0.1	0.1
2. Cyclical unemployment benefit expenditure	0	0.0	0.0	0.0	0,0	0,0
3. Effect of discretionary revenue measures	-4	-0,2	-1.1	-0.1	-0,3	-0,3
4. Revenue increases mandated by law	-	-	-	-	-	-
Memorandum items (*):						
One-off revenue (ESA 2010)	0	0.0	0.0	0.0	0.0	0.0
One-off expenditure (ESA 2010)	5	0,2	0.9	0.0	0.0	0.0
(*) Methodological Annex						

TABLE 3. GENERAL GOVERNMENT EXPENDITURE BY FUNCTION

% OF GDP	COFOG CODE	2017
1. General public services	1	6.0
2. Defence	2	1.8
3. Public order and safety	3	1.6
4. Economic affairs	4	5.9
5. Environmental protection	5	0.9
6. Housing and community amenities	6	1.0
7. Health	7	8.0
8. Recreation, culture and religion	8	1.4
9. Education	9	5.4
10. Social protection	10	24.3
11. Total expenditure	**TE**	**56.5**

NB: latest available data from Insee by COFOG codes, which are not yet consistent with the update of the 2018 accounts released in March 2019.

TABLE 4. GENERAL GOVERNMENT DEBT

% of GDP	ESA Code	2018	2019	2020	2021	2022
1. Gross debt[1]		98.4	98.9	98.7	98.1	96.8
2. Change in gross debt ratio		0,0	0,5	-0.2	-0.7	-1,3
Contributions to changes in gross debt ratio						
3. Primary balance[2]		-0.8	-1.5	-0.5	-0,1	0.4
4. Interest expenditure[3]	D.41	1.7	1,5	1,5	1,6	1.7
5. Stock-flow adjustment		-0.1	0,0	0,3	0.5	0,4
of which						
- differences between cash and accruals[4]						
- net accumulation of financial assets[5]						
- privatisation proceeds						
- valuation effects and other[6]						
Memo: Implicit interest rate on debt[7]		1.8	1,6	1,6	1.6	1.8
Other relevant variables						
6. Liquid financial assets[8]						
7. Net financial debt (7=1-6)						
8. Debt amortization						
9. Percentage of debt denominated in foreign currency						

[1] As defined in Regulation 3605/93 (not an ESA concept).
[2] See item 10 in Table 2A.
[3] See item 9 in Table 2A.
[4] The differences concerning interest expenditure, other expenditure and revenue may be posted here where material or if the debt-to-GDP ratio is above the reference value.
[5] Liquid assets (currency), government securities, assets on third countries, government controlled enterprises and the difference between quoted and non-quoted assets may be posted here where material or if the debt-to-GDP ratio is above the reference value.
[6] Changes due to exchange rate movements and operations in secondary markets may be posted here where material or if the debt-to-GDP ratio is above the reference value.
[7] Calculated as the ratio of gross interest expenditure to gross outstanding debt on 31 December of the previous year.
[8] FA1, FA2, FA3 (consolidated at market value), FA511 (listed equities), FA52 (mutual fund units or shares)

TABLE 5. CYCLICAL AND STRUCTURAL DEVELOPMENTS

% of GDP	ESA Code	2018*	2019	2020	2021	2022
1. Real GDP growth (in %)		1.6	1.4	1.4	1.4	1.4
2. General government balance	B.9	-2.5	-3.1	-2.0	-1.6	-1.2
3. Interest expenditure	D.41	1.7	1.5	1.5	1.6	1.7
4. One-off measures[1]		-0.2	-1.0	-0.1	0.0	0.0
5. Potential GDP growth (%) (g)		1.25	1.25	1.25	1.3	1.35
Contributions to potential growth:						
- labour		0.1/0.2	0.1/0.2	0.1/0.2	0.1/0.2	0.1/0.2
- capital		0.4/0.5	0.4/0.5	0.4/0.5	0.4/0.5	0.4/0.5
- total factor productivity		0.6/0.7	0.6/0.7	0.6/0.7	0.6/0.7	0.6/0.7
- effect of structural reforms		-	-	-	0.05	0.1
6. Output gap		-0.3	-0.1	0.0	0.1	0.1
7. Cyclical balance		-0.2	-0.1	0.0	0.0	0.1
8. Cyclically-adjusted balance (8=2-7)		-2.4	-3.0	-2.0	-1.7	-1.3
9. Cyclically-adjusted primary balance (9=8+3)		-0.7	-1.5	-0.5	-0.1	0.3
10. Structural balance (10=8-4)		-2.1	-2.1	-1.9	-1.6	-1.3

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

TABLE 6. DIVERGENCE FROM PREVIOUS UPDATE

	ESA Code	2018	2019	2020	2021	2022
Real GDP growth						
Previous programme (2018-2022)		2.0	1.9	1.7	1.7	1.7
Current programme (2019-2022)		1.6	1.4	1.4	1.4	1.4
Difference		-0.4	-0.5	-0.3	-0.3	-0.3
General government net lending (% of GDP)						
Previous programme (2018-2022)	B.9	-2.3	-2.4	-0.9	-0.3	0.3
Current programme (2019-2022)	B.9	-2.5	-3.1	-2.0	-1.6	-1.2
Difference	B.9	-0.2	-0.7	-1.1	-1.3	-1.5
General government debt (% of GDP)						
Previous programme (2018-2022)		96.4	96.2	94.7	92.3	89.2
Current programme (2019-2022)		98.4	98.9	98.7	98.1	96.8
Difference		1.9	2.7	4.0	5.8	7.6

TABLE 7. LONG-TERM SUSTAINABILITY OF PUBLIC FINANCES*

% of GDP	2017	2020	2040	2050	2060	2070
Total expenditure						
of which age-related expenditure	**31.0**	**30.9**	**31.5**	**30.3**	**29.0**	**28.0**
Pension expenditure	15.0	15.0	15.1	13.8	12.5	11.8
of which social security pension						
of which old-age and early pensions						
of which other pensions (disability, survivors)						
of which occupational pensions (if in general government)						
Healthcare expenditure	7.9	8.0	8.4	8.4	8.4	8.3
Long-term care	1.7	1.8	2.3	2.4	2.4	2.4
Education expenditure	4.8	4.7	4.6	4.6	4.5	4.4
Other age-related expenditure (unemployment benefits)	1.6	1.4	1.2	1.2	1.2	1.2
Interest expenditure						
Total revenue						
of which property income	0.7	0.7	0.6	0.6	0.6	0.6
of which pension contributions (or social contributions if appropriate)						
Pension Reserve Fund assets						
of which consolidated public pensions fund assets (assets other than government liabilities)						
Systemic pension reforms[1]						
Social contributions paid to private compulsory pension schemes[2]	:	:	:	:	:	:
Pension expenditure paid by private compulsory pension schemes[3]	:	:	:	:	:	:
Assumptions						
Labour productivity growth	:	:	:	:	:	:
Real GDP growth	:	:	:	:	:	:
Participation rate males (aged 20-64)	:	:	:	:	:	:
Participation rate females (aged 20-64)	:	:	:	:	:	:
Total participation rates (aged 20-64)	:	:	:	:	:	:
Unemployment rate	:	:	:	:	:	:
Share of population over 65 years old	:	:	:	:	:	:

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

TABLE 7A. CONTINGENT LIABILITIES

% of GDP	2016	2017
Government guarantees*	8.7	8.9
of which granted to the financial sector	-	-

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

TABLE 8. BASIC ASSUMPTIONS

	2018	2019	2020	2021	2022
Short-term interest rate (annual average)[1]	-0.3	-0.1	0.6	1.4	2.1
Long-term interest rate (annual average)[2]	0.8	0.9	1.7	2.4	3.2
USD/€ exchange rate (annual average)	1.18	1.13	1.13	1.13	1.13
Nominal effective exchange rate	2.7	-0.9	0.0	0.0	0.0
Global GDP growth excluding EU[3]	4.0	3.7	3.8	4.0	3.9
EU GDP growth[3]	2.2	1.8	1.5	1.7	1.7
World demand for French goods	3.7	2.7	2.9	3.1	3.1
World import volumes excluding the EU	5.0	3.0	3.2	n.a.	n.a.
Oil prices (Brent, USD/barrel)	71	64	65	65	65

1 Euribor 3-month rate
2 Yield on 10-year French Treasury bonds.
3 The growth forecasts for 2021 and 2022 are taken from the October 2018 World Economic Outlook by the IMF.

8.2 METHODOLOGICAL ANNEX: CALCULATING STRUCTURAL ADJUSTMENT AND THE EXPENDITURE BENCHMARK

ROLE OF POTENTIAL GROWTH

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

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

STRUCTURAL BALANCE

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

THE GENERAL GOVERNMENT BALANCE FOR EACH YEAR CAN BE BROKEN DOWN INTO:

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

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

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

We quantify the components of the cyclical balance **on the basis of average historical elasticities (called conventional elasticities)** of these expenditure and revenue items to the output gap. The elasticities are based on an econometric estimate made by the OECD[30]. Revenue is broken down into four categories of taxes and contributions (personal income tax, including the General Social Security Contribution, corporate income tax, social contributions and other taxes and contributions) since the reaction of the tax bases to cyclical changes can vary greatly depending on the tax under consideration. **On average, the aggregate conventional tax elasticity is very close to one.**

The elasticities of the taxes and contributions under review are presented in Table 9[31]. They were updated in 2014.

TABLE 9. SEMI-ELASTICITIES TO THE OUTPUT GAP

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

Source: OECD 2014

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

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

BOX 10 - STRUCTURAL BALANCE

Y denotes actual GDP and Y* denotes potential GDP.

For each category of taxes and contributions R, the structural component Rs can be written as a function of the conventional elasticity θ to the output gap (see Table 9):

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

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

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

$$D^{cho}_s = D^{cho}(\frac{Y^*}{Y})^\varepsilon$$

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

30 See "New tax and expenditure elasticity estimates for EU budget surveillance", by R.W.R Price, T. Dang and Y. Guillemette, OECD Economics Department Working Papers No. 1174 2014.

31 More precisely, the semi-elasticity to the output gap.

STRUCTURAL EFFORT

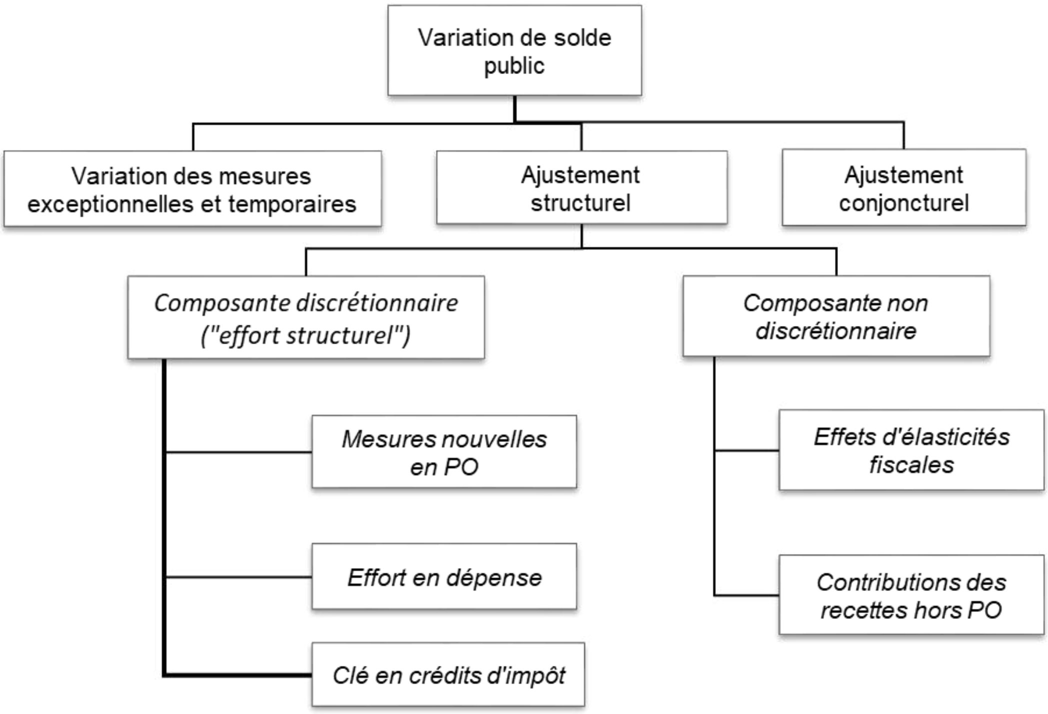
The structural balance needs to be supplemented with another public finance analysis tool: structural effort

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

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

Furthermore, the accounting conventions of ESA 2010[32] introduced in 2014, change the treatment of refundable tax credits. Tax credits reduce taxes and social security contributions by an amount equivalent to their impact on tax revenue (meaning allocations and refunds actually granted to corporations and households), but the outstanding claims acquired by taxpayers contribute to the general government balance under the accruals accounting principle. An additional term is used in this decomposition to maintain the same revenue effort and maintain its consistency with the concepts of aggregate tax and social security contribution rate and discretionary measures, which recognise tax credits as reduced revenue, as well as the expenditure effort, excluding tax credits. This term is the variation in the discrepancy between the fiscal cost and the national accounts cost of refundable tax credits (in practice, this means the Competitiveness and Employment Tax Credit and the Research Tax Credit). When the fiscal cost (under discretionary revenue measures) of the claims is less than the cost recorded in the national accounts (which affects the general government balance), this item reduces the structural effort. Conversely, when the fiscal effort measured as a revenue effort is greater than the accrued effort recorded in the national accounts, this item increases the structural effort. The correction for accrual-based measurement of tax credit refunds has been incorporated into the structural effort item in the decomposition of structural adjustment since the 2018-2022 Public Finance Planning Act. The new decomposition is warranted by the replacement of the Competitiveness and Employment Tax Credit and it will smooth its impact on structural effort without requiring any further restatement of data.

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



Change in general government balance
Change in one-offs
Structural adjustment
Cyclical adjustment
Discretionary component ("structural effort")
Discretionary revenue measures
Expenditure effort
Correction for tax credits
Non-discretionary component
Tax elasticity effects
Contribution from non-tax revenue

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

- A discretionary component called "structural effort";
- A non-discretionary component.

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

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

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

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

8.3 ADJUSTMENT PATH UNDER THE NO-POLICY-CHANGE SCENARIO

This Stability Programme presents a "no-policy-change" scenario, in accordance with the European Council Directive of 8 November 2011. This is a contra-factual scenario for 2018-2022 presenting what would have happened in the absence of the measures taken by the Government since 2017. The following assumptions underlie this scenario:

- On the revenue side, the adjustment path is not affected by any of the discretionary measures taken by the Government since May 2017, or by any prior discretionary measures that the Government maintained or assumed;
- On the expenditure side, real expenditure growth after 2017 is assumed to match the average growth rate over the last ten years. This corresponds approximately to potential GDP growth over the planning period, or 1.2% per year[33].

TABLE 10: NO-POLICY-CHANGE PATH

% of GDP	2017	2018	2019	2020	2021	2022
General government deficit under no policy change since May 2017 scenario	**-3.1**	**-3.0**	**-2.7**	**-2.6**	**-2.5**	**-2.4**
General government debt under no policy change scenario	**98.7**	**99.1**	**99.2**	**99.6**	**99.8**	**99.6**
Cumulative divergence of expenditure, excluding tax credits	0.1	0.7	0.9	1.2	1.7	2.2
Cumulative divergence from discretionary revenue measures announced (*)	0.2	-0.2	-0.5	-0.7	-0.8	-1.0
Replacement of Competitiveness and Employment Tax Credit			-0.8			
Stability Programme general government balance	**-2,8**	**-2,5**	**-3.1**	**-2,0**	**-1.6**	**-1.2**
Stability programme general government debt	**98.4**	**98.4**	**98.9**	**98.7**	**98.1**	**96.8**

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

By 2022, the cumulative divergence of expenditure would not match the reduction of the general government expenditure ratio by 2.9 percentage points of GDP, excluding France Compétences, since the ratio is also affected by cyclical developments. Similarly, the cumulative divergence of revenue would not match the reduction of the aggregate tax and contributions ratio of 1.4 percentage point of GDP, excluding France Compétences. This mismatch can be attributed primarily to the fact that the divergence incorporates the positive variation of the correction for accrual-based measurement of tax credits over the period.

In 2018, the no-policy-change scenario would correspond to a deficit of 3.0% of GDP. Discretionary expenditure measures have reduced the general government expenditure ratio by 0.7 percentage points of GDP compared to the baseline scenario. Without these measures, the debt ratio would have stood at 99.1% of GDP.

In 2019, the no-policy-change scenario would produce a deficit of 2.7% of GDP. The target adjustment path includes savings of 0.9 percentage points of GDP on the expenditure ratio, excluding tax credits. However, the cumulative cost of the discretionary revenue measures is equivalent to 0.5 percentage points of GDP. This cost stems from the emergency measures, along with the cost equivalent to 0.8 percentage points of GDP of replacing the Competitiveness and Employment Tax Credit. This means that the deficit with no policy change would temporarily be smaller than under the adjustment path in the Stability Programme. Absent the one-off impact of replacing the Competitiveness and Employment Tax Credit, the actual deficit would reach 2.3% of GDP, instead of 2.7% under the "no-policy-change" scenario.

In 2020, 2021 and 2022, the end of the double cost of replacing the Competitiveness and Employment Tax Credit will make direct explanations of the differences between the no-policy-change path and the actual path easier. Efforts to contain expenditure will continue until the end of the Government's 5-year term. The no-policy-change deficit should reach 2.4% of GDP in 2022, compared to 1.2% under the adjustment path set out in the Stability Programme. The debt-to-GDP ratio would stand at 99.6% in 2022, compared to 96.8% under the adjustment path set out in the Stability Programme.

[33] Expenditure related to the disputed 3% dividend tax is treated as part of the spontaneous adjustment path.

CONTACTS PRESSE

CABINET DE BRUNO LE MAIRE
presse.mineco@cabinets.finances.gouv.fr
01 53 18 41 13

CABINET DE GÉRALD DARMANIN
presse.macp@cabinets.finances.gouv.fr
01 53 18 45 06

ECONOMIE.GOUV.FR