EUROPEAN
COMMISSION

Brussels, 20.11.2019
C(2019) 9108 final

COMMISSION OPINION

of 20.11.2019

on the Draft Budgetary Plan of France

{SWD(2019) 918 final}

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GENERAL CONSIDERATIONS

1. Regulation (EU) No 473/2013 sets out provisions for enhanced monitoring of budgetary policies in the euro area, to ensure that national budgets are consistent with the economic policy guidance issued in the context of the Stability and Growth Pact and the European Semester for economic policy coordination.

2. Article 6 of Regulation (EU) No 473/2013 requires Member States to submit annually to the Commission and to the Eurogroup a Draft Budgetary Plan presenting by 15 October the main aspects of the budgetary situation of the general government and its subsectors for the forthcoming year.

CONSIDERATIONS CONCERNING FRANCE

3. On 15 October 2019, France submitted the Draft Budgetary Plan for 2020. On that basis, the Commission has adopted the following opinion in accordance with Article 7 of Regulation (EU) No 473/2013. By letter of 22 October 2019, the Commission asked France for further information. It has taken the reply by France of 23 October 2019 into account in its assessment of budgetary developments and risks.

4. France is subject to the preventive arm of the Stability and Growth Pact. On 9 July 2019, the Council recommended France to ensure that the nominal growth rate of net primary government expenditure does not exceed 1.2% in 2020, corresponding to an annual structural adjustment of 0.6 % of GDP towards the medium-term budgetary objective of -0.4% of GDP, and to use windfall gains to accelerate the reduction of the general government debt ratio[1]. As its public debt amounted to 98.4% of GDP in 2017, the year in which it corrected its excessive deficit, France also needs to make sufficient progress towards compliance with the debt reduction benchmark in 2019 and 2020.

5. According to the Commission 2019 autumn forecast, the French economy is expected to grow by 1.3% in both 2019 and in 2020. Growth in 2020 is set to be driven by some pick-up in private consumption and still resilient, though decelerating, corporate investment. The expected pick up in private consumption would be explained by gains in purchasing power, partly due to supportive fiscal measures. In turn, the contribution of net exports to growth is projected to be broadly neutral, as export growth is expected to remain rather flat as external demand loses momentum. The macroeconomic scenario underlying the 2020 Draft Budgetary Plan forecasts GDP growth at 1.4% in both 2019 and 2020, with a broadly similar composition both years. The government expects that job creation will remain stable in 2019 and decelerate in 2020, while apparent labour productivity is forecast to decrease temporarily in 2019. Finally, inflation is set to decrease to 1.3% in 2019 and

[1] Council Recommendation of 9 July 2019 on the 2019 National Reform Programme of France and delivering a Council opinion on the 2019 Stability Programme of France, OJ C 301, 5.9.2019, p.55

to remain stable in 2020. Overall, the macroeconomic assumptions underpinning the Draft Budgetary Plan are plausible for 2019 and 2020. France complies with the requirement of Regulation (EU) No 473/2013 since the draft budget is based on independently endorsed macroeconomic forecasts. In its opinion, the High Council of Public Finances considers the government's GDP growth forecast is within reach for 2019 and plausible for 2020.

6. The Draft Budgetary Plan projects a headline deficit of 3.1% of GDP for 2019, which implies no improvement in the structural balance[2] with respect to 2018. For 2020, the deficit is planned to decrease to 2.2% of GDP, with no improvement in the structural balance. The planned deficit reduction in 2020 is mainly due to the fading of the one-off deficit increasing impact in 2019 of the transformation of the *Crédit d'impôt pour la compétitivité et l'emploi* (CICE) into an outright reduction in social security contributions by around 0.9% of GDP. The Commission 2019 autumn forecast projects headline deficits for 2019 and 2020 fully in line with the targets set out in the Draft Budgetary Plan. The projected change in the structural balance in the Commission's projections for 2019 is in line with that in the Draft Budgetary Plan. However, for 2020 the Commission projects an improvement in the structural balance by 0.1% of GDP, due to the consideration as a one-off, contrary to the French authorities, of the additional deficit-increasing liabilities linked to the CICE.

7. The fiscal stance envisaged in the Draft Budgetary Plan for 2020 is neutral. This is broadly confirmed by the Commission 2019 autumn forecast. The Draft Budgetary Plan does not target any progress in terms of fiscal consolidation. The planned reduction of the deficit is mainly explained by the fading of the one-off deficit-increasing impact of the transformation of the CICE in 2019. The tax reductions are offset by measures to control public expenditure as well as by the planned decline in public debt servicing costs. Since its initial definition in 2018, the consolidation trajectory has been repeatedly backloaded and its level of ambition has also been lowered. While the objective to reduce the tax burden by one percentage point by the end of the presidential term is mostly already achieved, the reduction of government expenditure is proving much slower compared to initial projections. On the revenue side, the main new measures include the reduction by 0.2% of GDP of the personal income tax mainly targeted to middle-income earners. Its budgetary impact is partly offset by revenue increasing measures, by less than 0.1% of GDP, that include the smoothing of the reduction of the corporate income tax for big companies, the limitation of a reduction in social security contributions to certain sectors and the suppression of the tax expenditure on the use of off-road diesel. On the expenditure side, the new measures in the Draft Budgetary Plan include the deficit-increasing cancelation of the under-indexation of lower pensions and the increase in minimum pensions, which together entail a budgetary cost of 0.1% of GDP. All those measures are specified in sufficient detail and are included in the Commission 2019 autumn forecast accordingly.

On 9 July 2019 the Council also recommended France to achieve expenditure savings and efficiency gains across all sub-sectors of the government. This included by fully specifying and monitoring the implementation of the concrete measures needed in the context of Public Action 2022 and by reforming the pension system to progressively unify the rules of the different pension regimes, with the view to

[2] Cyclically adjusted balance net of one-off and temporary measures, recalculated by the Commission using the commonly agreed methodology.

enhance their fairness and sustainability. The Draft Budgetary Plan includes a number of measures to contain public expenditure. However, it does not quantify expenditure savings and efficiency gain measures in the context of Public Action 2022 and it is unclear how this programme will contribute to the fiscal consolidation strategy. Moreover, the Draft Budgetary Plan does not put forward concrete proposals for the reform of the pension system and the announced reform has been postponed, while a public consultation is ongoing. At the same time, the new revenue measures are meant to enhance households' purchasing power, thereby supporting private consumption.

8. In 2019, for France to comply with the requirements of the preventive arm, the nominal growth rate of government expenditure, net of discretionary revenue measures and one-offs, should not exceed 1.4%, corresponding to an annual structural adjustment of 0.6% of GDP. According to the data in the Draft Budgetary Plan, the nominal growth rate of government expenditure, net of discretionary revenue measures and one-offs shows a gap of 0.7% of GDP with respect to the expenditure benchmark, which points to a significant deviation from that requirement. Likewise, the gap with respect to the required adjustment in the structural balance amounts to 0.6% of GDP, also pointing to a significant deviation. The Commission 2019 autumn forecast confirms these conclusions, showing a slightly larger gap of 0.8% of GDP with respect to the expenditure benchmark in 2019.

   In 2020, for France to comply with the requirements of the preventive arm, the nominal growth rate of government expenditure, net of discretionary revenue measures and one-offs, should not exceed 1.2%, corresponding to an annual structural adjustment of 0.6% of GDP. According to the data in the Draft Budgetary Plan, the nominal growth rate of government expenditure, net of discretionary revenue measures and one-offs shows a gap of 0.7% of GDP with respect to the expenditure benchmark, thereby pointing to a significant deviation from the requirement. The gap with respect to the required adjustment in the structural balance amounts to 0.6% of GDP, also pointing to a significant deviation. For 2019 and 2020 taken together, the same conclusion holds, unveiling a gap with respect to the expenditure benchmark and to the required adjustment in the structural balance of the same magnitude on average. Those conclusions are confirmed by the Commission 2019 autumn forecast, which points to gaps with respect to the expenditure benchmark of 0.8% of GDP for 2020 alone and on average for 2019 and 2020 taken together. The gap with respect to the required adjustment in the structural balance amounts to of 0.5% and 0.6% of GDP for 2020 alone and on average for 2019 and 2020 taken together, respectively.

9. The Draft Budgetary Plan indicates that government debt will decrease marginally from 98.8% in 2019 to 98.7% of GDP in 2020, slightly below the Commission's projection of 98.9% of GDP for both years. The Draft Budgetary Plan does not include sufficient information to assess compliance with the transitional debt rule based on the forecast and estimates of the government. Based on the Commission 2019 autumn forecast, France is not projected to make sufficient progress towards compliance with the debt reduction benchmark in 2019 and 2020, with gaps of 1.0% and 1.9% of GDP, respectively.

10. Overall, the Commission is of the opinion that the Draft Budgetary Plan of France is at risk of non-compliance with the provisions of the Stability and Growth Pact. In particular, the Commission projects a risk of significant deviation from the required

adjustment towards the medium-term budgetary objective for 2019 and 2020. Moreover, France is not projected to make sufficient progress towards compliance with the debt reduction benchmark either in 2019 or in 2020. Therefore, the Commission invites the authorities to take the necessary measures within the national budgetary process to ensure that the 2020 budget will be compliant with the Stability and Growth Pact and to use any windfall gains to accelerate the reduction of the government debt-to-GDP ratio.

The Commission is also of the opinion that France has made limited progress with regard to the structural part of the fiscal recommendations contained in the Council Recommendation of 9 July 2019 in the context of the European Semester and thus invites the authorities to accelerate progress. A comprehensive description of progress made with the implementation of the country-specific recommendations will be made in the 2020 Country Reports and assessed in the context of the country-specific recommendations to be proposed by the Commission in spring 2020.

Done at Brussels, 20.11.2019

For the Commission
Pierre MOSCOVOCI
Member of the Commission