EUROPEAN COMMISSION
DIRECTORATE GENERAL
ECONOMIC AND FINANCIAL AFFAIRS

Brussels, 5 June 2019

# Assessment of the 2019 Stability Programme for

# France

***(Note prepared by DG ECFIN staff)***

**Disclaimer**
This is not an official Commission document and the views expressed therein do not necessarily represent the views of the European Commission.

**CONTENTS**


EXECUTIVE SUMMARY ........ 3

1. INTRODUCTION ........ 4

2. MACROECONOMIC DEVELOPMENTS ........ 4

3. RECENT AND PLANNED BUDGETARY DEVELOPMENTS ........ 6

3.1. DEFICIT DEVELOPMENTS IN 2018 AND 2019 ........ 6

3.2. MEDIUM-TERM STRATEGY AND TARGETS ........ 7

3.3. MEASURES UNDERPINNING THE PROGRAMME ........ 10

3.4. DEBT DEVELOPMENTS ........ 13

3.5. RISK ASSESSMENT ........ 14

4. COMPLIANCE WITH THE PROVISIONS OF THE STABILITY AND GROWTH PACT ........ 15

4.1. Compliance with the deficit criterion ........ 15

4.2. Compliance with the debt criterion ........ 16

4.3. Compliance with the MTO or the required adjustment path towards the MTO ........ 17

5. DEBT SUSTAINABILITY ANALYSIS AND FISCAL RISKS ........ 20

6. FISCAL FRAMEWORK ........ 22

7. SUMMARY ........ 23

8. ANNEXES ........ 25

## EXECUTIVE SUMMARY

France is subject to the preventive arm of the Stability and Growth Pact. Since France's public debt is above the 60% of GDP reference value of the Treaty, it also needs to ensure sufficient progress towards compliance with the debt reduction benchmark.

Economic activity in France is set to slightly cool down in 2019 and 2020 compared to 2018 although growth should remain above potential, being driven by domestic demand. In turn, tax revenues are expected to evolve broadly in line with economic activity although they would slow down after years of high dynamism. Private consumption should progressively regain momentum, supported by strong fiscal support to households' purchasing power, moderate inflation and rising nominal wages. Despite the prospects of a deceleration, investment should still be dynamic. According to the Commission forecast, GDP growth is set to decrease from 1.6% in 2018 to 1.3% in 2019 before reaching 1.5% in 2020. This is broadly in line with the scenario underlying the Stability Programme.

The general government deficit declined to 2.5% of GDP in 2018. The Stability programme plans the deficit to reach 3.1 % of GDP in 2019 before falling to 2.0 % in 2020, where the increase in 2019 is mainly due to the impact of a single one-off measure. The programme forecasts a limited improvement in the structural balance in 2019 and 2020. This is the result of a fiscal strategy based on the control of public expenditure to finance the reduction of the tax burden and the support of households' purchasing power. At the same time, the main effort of fiscal adjustment is backloaded. Some differences for 2019 exist between the Stability Programme and the Commission forecast with regard to the interpretation of the one-off nature of two fiscal measures. No major differences in the assessment arise concerning the impact of the measures in 2020, although the Commission forecast are based on the usual no policy change assumption. Risks to the fiscal outlook mainly stem from the effect of the announced fiscal measures following the recent nation-wide consultation (*Grand Débat*) and that might entail an overall deficit-increasing impact.

Based on the Commission forecast, France is at risk of significant deviation from the adjustment path towards the MTO both in 2019 and in 2020. In none of the two years, sufficient progress towards compliance with the debt reduction benchmark would be ensured.

In view of the planned breach of the 3% of GDP reference value in 2019 and the insufficient progress towards compliance with the debt reduction benchmark in 2018, the Commission issued a report under Article 126(3) of the TFEU in order to assess whether the launch of an excessive deficit procedure is warranted. The report concluded, following an assessment of all the relevant factors, that the deficit and debt criteria as defined in the Treaty and in Council Regulation (EC) No 1467/97 should be considered as currently complied with.

## 1. INTRODUCTION

On 26 April 2019, France submitted its 2019 Stability Programme (hereafter called Stability Programme), covering the period 2019-2022. The government approved the programme on 10 April and it was submitted to the Parliament the same day.

France is currently subject to the preventive arm of the the Stability and Growth Pact (SGP) and should ensure sufficient progress towards its medium-term budgetary objective (MTO). As the debt ratio exceeded the 60% of GDP Treaty reference value in 2017 (the year in which France corrected its excessive deficit), France is also subject to the transitional arrangements as regards compliance with the debt reduction benchmark during the three years following the correction of the excessive deficit (transitional debt rule). In this period, it should ensure sufficient progress towards compliance with the debt reduction benchmark. After the transition period, as of 2021, France will be subject to the debt reduction benchmark.

This document complements the Country Report published on 27 February 2019 and updates it with the information included in the Stability Programme

Section 2 presents the macroeconomic outlook underlying the Stability Programme and provides an assessment based on the Commission 2019 spring forecast. The following section presents the recent and planned budgetary developments, according to the Stability Programme. In particular, it includes an overview on the medium-term budgetary plans, an assessment of the measures underpinning the Stability Programme and a risk analysis of the budgetary plans based on the Commission forecast. Section 4 assesses compliance with the rules of the SGP, including based on the Commission forecast. Section 5 provides an overview on long-term sustainability risks and Section 6 on recent developments and plans regarding the fiscal framework. Section 7 provides a summary.

## 2. MACROECONOMIC DEVELOPMENTS

The macroeconomic scenario underlying the Stability Programme forecasts GDP growth at 1.4% in 2019 and 2020, after 1.6% in 2018 (calendar-adjusted). Compared to the Draft Budgetary Plan for 2019, the growth projection has been revised down by 0.1 percentage point in 2018 and by 0.3 percentage point in 2019 and 2020.

Economic activity is projected to be driven by private consumption, in line with increasing households' purchasing power thanks to significant fiscal measures and decreasing inflation. Corporate investment is expected to slow down but to remain more dynamic than economic activity in general. Moreover, exports growth is set to decrease in 2019 and only partially pick-up in 2020, reflecting the weakening of external demand. As imports are forecast to accelerate, the contribution of net exports to growth is expected to become broadly neutral. Domestic demand dynamism is set to only partly compensate the loss of net exports contribution to growth, explaining the deceleration in economic activity in 2019 and 2020 compared to 2018. IPC inflation is projected to decrease from 1.8% in 2018 to 1.3% in 2019 and 2020, due to lower oil prices and lower increases in taxes. Employment growth is expected to decrease from 1.0% in 2018 to 0.6% in 2019 and 0.5% in 2020 as productivity gains are set to increase.

Given the GDP growth projections, the output gap, as recalculated by the Commission following the commonly agreed methodology, stands at 0.3% in 2018. It is expected to increase slightly by 0.1 percentage point in 2019 and in 2020, and to widen progressively to 0.8% in 2022.

The Commission 2019 spring forecast projects a slightly lower growth in 2019 (1.3%) and the same GDP growth in 2020 (1.5% non-calendar adjusted)[1]. The composition of growth is expected to be broadly in line with the one described in the Stability Programme. However, the increase in private consumption is set to materialise more gradually in the Commission forecast, as the effects of the fiscal measures are expected to first translate into higher precautionary savings given the low levels of consumer confidence indicators. Hence, private consumption growth is forecast to be lower than in the Stability Programme in 2019 and higher in 2020. The Commission spring forecast projects lower growth in compensation per employee for 2019, by 0.2 percentage points, and slightly higher growth in 2020, by 0.1 percentage point.

**Table 1: Comparison of macroeconomic developments and forecasts**

| | 2018 | | 2019 | | 2020 | | 2021 | 2022 |
|---|---|---|---|---|---|---|---|---|
| | COM | SP | COM | SP | COM | SP | SP | SP |
| Real GDP (% change)[1] | 1.6 | 1.6 | 1.3 | 1.4 | 1.5 | 1.4 | 1.4 | 1.4 |
| Private consumption (% change) | 0.9 | 0.9 | 1.5 | 1.6 | 1.7 | 1.3 | 1.4 | 1.4 |
| Gross fixed capital formation (% change) | 2.9 | 2.9 | 2.1 | 2.1 | 1.7 | 1.4 | 1.2 | 1.6 |
| Exports of goods and services (% change) | 3.3 | 3.3 | 2.8 | 2.4 | 2.9 | 2.7 | 3.1 | 3.1 |
| Imports of goods and services (% change) | 1.3 | 1.3 | 2.5 | 2.4 | 3.0 | 2.3 | 2.3 | 2.3 |
| *Contributions to real GDP growth:* | | | | | | | | |
| - Final domestic demand | 1.4 | 1.4 | 1.5 | 1.6 | 1.6 | 1.3 | 1.1 | 1.2 |
| - Change in inventories | -0.4 | -0.4 | -0.2 | -0.1 | 0.0 | 0.0 | 0.0 | 0.0 |
| - Net exports | 0.6 | 0.6 | 0.1 | 0.0 | -0.1 | 0.1 | 0.2 | 0.2 |
| Output gap[2] | 0.4 | 0.3 | 0.5 | 0.4 | 0.7 | 0.5 | 0.6 | 0.8 |
| Employment (% change) | 1.0 | 1.0 | 0.8 | 0.6 | 0.7 | 0.5 | 0.3 | 0.2 |
| Unemployment rate (%) | 9.1 | | 8.8 | | 8.5 | | | |
| Labour productivity (% change) | 0.7 | 0.6 | 0.5 | 0.9 | 0.8 | 0.9 | 1.1 | 1.2 |
| HICP inflation (%)[3] | 2.1 | 1.8 | 1.3 | 1.3 | 1.4 | 1.3 | 1.5 | 1.8 |
| GDP deflator (% change) | 0.9 | 0.9 | 1.3 | 1.2 | 1.3 | 1.2 | 1.5 | 1.7 |
| Comp. of employees (per head, % change) | 1.7 | 1.9 | 0.0 | 0.2 | 1.8 | 1.7 | 2.4 | 2.8 |
| Net lending/borrowing vis-à-vis the rest of the world (% of GDP) | -0.7 | -0.7 | -0.6 | -0.5 | -0.7 | -0.3 | -0.1 | 0.0 |

Note:

[1] Calendar-adjustement real GDP and components in the SP.

[2]In % of potential GDP, with potential GDP growth recalculated by Commission services on the basis of the programme scenario using the commonly agreed methodology.

[3]ICP inflation in the SP.

*Source :*

*Commission 2019 spring forecast (COM); Stability Programme (SP).*

The positive output gap is increasing faster in the Commission spring forecast due to lower potential growth estimates as of 2019 (by 0.1 percentage point compared to the recalculated

[1] The Stability Program provides calendar-adjusted data but indicates that non-calendar adjusted GDP growth is expected to reach 1.5% in 2020.

potential growth from data in the Stability Programme). This difference is mostly explained by higher total factor productivity, stemming from a higher GDP growth forecast and lower employment growth in the Stability Programme.

Overall, the macroeconomic scenario underlying the Stability Programme, albeit slightly more favourable than the Commission spring forecast in 2019, is plausible. In its opinion, the High Council of Public Finances (HCFP) also considers the government's GDP growth forecast for 2019 as realistic. The HCFP welcomes the downward revision of the longer-term projections for GDP growth, now close to potential, and considers it reasonable. However, the HCFP highlights the uncertainties related to the real-time estimates of the output gap.

## 3. RECENT AND PLANNED BUDGETARY DEVELOPMENTS

### 3.1. DEFICIT DEVELOPMENTS IN 2018 AND 2019

In 2018, according to data notified to Eurostat, the general government deficit reached 2.5% of GDP, above the target of 2.3% set in the 2018 Stability Programme. This outturn is however lower by 0.1 percentage point and 0.2 percentage points, respectively, compared to the headline deficit posted in the Draft Budgetary Plan for 2019 and the one finally retained in the 2019 Budget Law adopted in December 2018.

The notified result is associated with a contraction in the fiscal stance corresponding to an improvement of 0.2 percentage points of the structural balance. Such an improvement, face to 0.1 percent point improvement and no effort foreseen, respectively, in the 2019 Draft Budgetary Plan and the 2019 Budget Law results from the combination of a better outturn deficit in 2018 and a 0.1 percent point higher deficit in 2017 compared to what anticipated.

The better-than-expected budget outcome in 2018 *vis-à-vis* the Draft Budgetary Plan is the result of a higher containment of expenditure, namely with public expenditure net of tax credits contracting in real terms, whereas revenues remained resilient. Overall, the expenditure-to-GDP ratio reached 56.0%, down by 0.3 percentage points compared to the Draft Budgetary Plan.

On the other hand, the share of total revenues in GDP reached 53.5%, compared to 53.7% foreseen in the Draft Budgetary Plan, but revenues remained buoyant, with an overall elasticity above unity.

The government plans a headline balance of -3.1% of GDP in 2019, substantially higher than the deficit posted in last year's Stability Programme (2.4% of GDP) and 0.3 percentage points higher than the one tabled in the Draft Budgetary Plan[2]. Yet, the planned deficit is 0.1 percentage point lower than the target projected in the final 2019 Budget Law. The latter indeed included the impact of the measures adopted in December 2018 to address the ‘yellow vests’ movement. After accounting for the intended offsetting measures, at the end of last year the government thus revised upwards its deficit projection by about 0.3% of GDP, adding to a further increase of 0.1% of GDP expected as base effect from 2018.

[2] The Draft Budgetary Plan did not provide explicit reasons in order to explain the change in the deficit for 2019 compared to the Stability Programme. Part of it was certainly associated with the permanent impact of the reclassification of SNCF Réseau into the general government as from 2016 for about 0.1% of GDP each year. Other likely factors explaining the change in the target could be identified in the deterioration of the macroeconomic scenario as well as the base effect from 2018.

The slight improvement in the headline deficit of the Stability Programme compared to the 2019 Budget Law is mainly the result of the positive base effect stemming from the better-than-expected deficit outcome in 2018 (by 0.2 percentage points).

As in all previous official projections, the headline deficit for 2019 contained in the Stability Programme includes the one-off impact of 0.9% of GDP stemming from the double cost of an accounting nature of the replacement of the CICE (*crédit d'impôt pour la compétitivité et l'emploi*) by a permanent cut in employers' social contributions.

The Stability Programme plans in 2019 a slight contraction in the fiscal stance, corresponding to an improvement of 0.1 percentage point of the structural balance, compared to a neutral stance previously projected in the Budget Law[3]. The improvement in the structural balance recalculated by the Commission on the basis of the information in the Stability Programme according to the commonly agreed methodology amounts to 0.2 percentage points. This compares to a neutral fiscal stance projected in the Commission spring forecast, the difference being explained by two factors. On the one hand, as indicated in section 2 above, the 2019 recalculated structural balance reflects a stronger increase of the output gap, following a stronger increase of the recalculated potential growth. On the other hand, between the two sets of projections there is a different treatment, overall worth about 0.1% of GDP, of two measures in terms of their one-off nature. Namely, the Commission spring forecast qualifies as one-off the increase of the fifth instalment of corporate income tax, while it does not so for the change of recording of sales of Hertzian licences.

The discretionary measures adopted in December 2018, being aimed at enhancing the purchasing power of the most vulnerable households, mainly acted on the revenue side. Compared to the 2019 Draft Budgetary Plan, the share of total revenues in GDP is thus expected to decrease by 0.4 percentage points, to reach 52.4%. On the other hand, after incorporating the planned savings in the budgetary execution, the expenditure-to-GDP ratio is expected to decrease by 0.1 percentage point only, to reach 55.5%.

The Commission 2019 spring forecast projects a general government deficit in 2019 in line with the Stability Programme, with only slight differences in the composition between the two sets of projections. Specifically, the Commission projects slightly higher taxes on income and wealth and lower indirect taxes compared to the Stability Programme. As for expenditure, the Stability Programme plans slightly lower interest payments.

### 3.2. MEDIUM-TERM STRATEGY AND TARGETS

The Stability Programme plans the headline deficit to decrease to 2.0% of GDP in 2020[4] and then further decrease by 0.4 percentage points both in 2021 and the year after, to reach 1.2% of GDP in 2022. The Programme therefore plans to keep the headline deficit below 3% of GDP in a durable manner. The sharp decrease of the headline deficit in 2020 is mainly the result of the fading of the one-off statistical impact of the transformation of the CICE into a permanent reduction of employer's contributions. While the measure temporarily increases the

[3] The 2019 Draft Budgetary Plan of October 2018 posted an improvement of the structural balance of 0.3 percentage points.

[4] The new measures announced by the President of the Republic on April, 25th are expected to affect almost entirely the year 2020. They are not included in the 2019 Stability Programme, nor they are in the Commission 2019 spring forecast having been announced after the cut-off date.

deficit by about 0.9% of GDP in 2019, its qualification as a one-off implies no impact in the projected change of the fiscal stance between 2019 and 2020.

Based on data in the Stability Programme the recalculated structural balance is projected to gradually improve over the years covered and to reach -1.7% of GDP by 2022. The MTO, a structural deficit of 0.4% of GDP as set in the programming law of public finances 2018-2022 of 23 January 2018, is therefore not planned to be achieved. The chosen MTO is more stringent[5] than the minimum one required by the SGP.

**Table 2: Composition of the budgetary adjustment**

| (% of GDP) | 2018 | 2019 | | 2020 | | 2021 | 2022 | Change: 2018- |
|---|---|---|---|---|---|---|---|---|
| | COM | COM | SP | COM | SP | SP | SP | SP |
| **Revenue** | **53,5** | **52,4** | **52,4** | **52,3** | **52,3** | **52,0** | **51,7** | **-1,8** |
| *of which:* | | | | | | | | |
| - Taxes on production and imports | 16,5 | 16,5 | 16,8 | 16,5 | 16,8 | 16,7 | 16,7 | 0,2 |
| - Current taxes on income, wealth, etc. | 13,3 | 13,3 | 13,1 | 13,4 | 13,1 | 13,0 | 12,8 | -0,5 |
| - Social contributions | 18,0 | 16,8 | 16,8 | 16,7 | 16,7 | 16,7 | 16,7 | -1,3 |
| - Other (residual) | 5,7 | 5,7 | 5,7 | 5,6 | 5,7 | 5,6 | 5,5 | -0,2 |
| **Expenditure** | **56,0** | **55,5** | **55,5** | **54,4** | **54,3** | **53,6** | **53,0** | **-3,0** |
| *of which:* | | | | | | | | |
| - Primary expenditure | 54,3 | 53,9 | 54,0 | 52,8 | 52,8 | 52,0 | 51,3 | -3,0 |
| *of which:* | | | | | | | | |
| Compensation of employees | 12,5 | 12,3 | 12,3 | 12,2 | 12,1 | 12,0 | 11,8 | -0,7 |
| Intermediate consumption | 5,0 | 4,9 | 4,9 | 4,9 | 4,9 | 4,8 | 4,7 | -0,3 |
| Social payments | 25,5 | 25,4 | 25,4 | 25,4 | 25,1 | 24,9 | 24,7 | -0,8 |
| Subsidies | 2,7 | 2,7 | 2,7 | 1,8 | 2,0 | 2,0 | 2,0 | -0,7 |
| Gross fixed capital formation | 3,4 | 3,5 | 3,5 | 3,4 | 3,4 | 3,2 | 3,2 | -0,2 |
| Other (residual) | 5,3 | 5,1 | 5,0 | 5,2 | 5,1 | 5,0 | 4,9 | -0,4 |
| - Interest expenditure | 1,7 | 1,6 | 1,5 | 1,6 | 1,5 | 1,6 | 1,7 | 0,0 |
| **General government balance (GGB)** | **-2,5** | **-3,1** | **-3,1** | **-2,2** | **-2,0** | **-1,6** | **-1,2** | **1,3** |
| **Primary balance** | **-0,8** | **-1,5** | **-1,5** | **-0,5** | **-0,5** | **-0,1** | **0,4** | **1,2** |
| One-off and other temporary | -0,2 | -0,9 | -1,0 | -0,1 | -0,1 | 0,0 | 0,0 | 0,2 |
| **GGB excl. one-offs** | **-2,3** | **-2,3** | **-2,1** | **-2,1** | **-1,9** | **-1,6** | **-1,2** | **1,1** |
| Output gap[1] | 0,4 | 0,5 | 0,4 | 0,7 | 0,5 | 0,6 | 0,8 | 0,5 |
| Cyclically-adjusted balance[1] | -2,8 | -3,4 | -3,3 | -2,6 | -2,3 | -2,0 | -1,7 | 1,0 |
| **Structural balance[2]** | **-2,6** | **-2,6** | **-2,3** | **-2,5** | **-2,2** | **-2,0** | **-1,7** | **0,8** |
| Structural primary balance[2] | -0,9 | -0,9 | -0,8 | -0,9 | -0,7 | -0,4 | 0,0 | 0,8 |

Notes:

[1]Output gap (in % of potential GDP) and cyclically-adjusted balance according to the programme as recalculated by Commission on the basis of the programme scenario using the commonly agreed methodology.

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

*Source :*

*Stability Programme (SP); Commission 2019 spring forecasts (COM); Commission calculations.*

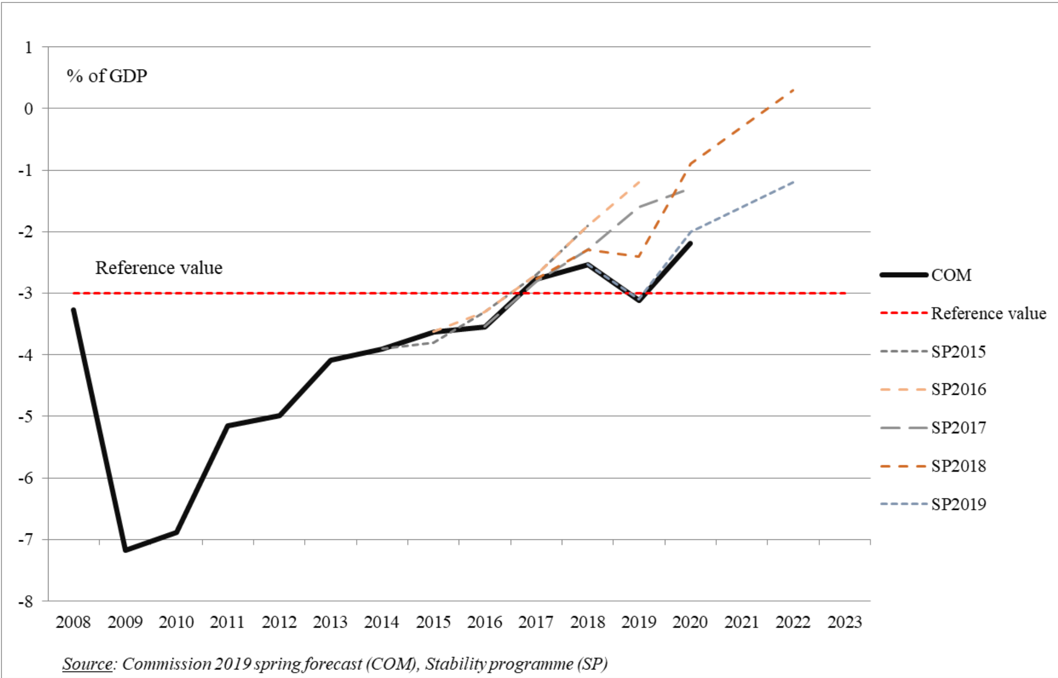
[5] The MTO selected by the Member State is more ambitious than the minimum MTO by more than 1/2 percentage point. The minimum MTOs are country-specific and calculated based on an agreed methodology.

The Commission 2019 spring forecast projects the headline deficit in 2020 to reach 2.2% of GDP. The difference with the authorities' plan arises on the expenditure side, namely concerning social payments and mainly due to the customary no-policy change assumption underpinning the Commission forecast. Based on this assumption, the Commission does not account for the savings stemming from the under indexation of pensions, as this measure was cancelled by the French Constitutional Council at the end of 2018. The different treatment of the measure under the no-policy change assumption also explains the difference between a neutral fiscal stance projected in 2020 in the Commission forecasts, compared to the 0.1 percentage point improvement in the recalculated structural balance.

No major differences appear on the revenue side, beyond slightly higher direct taxes and lower indirect taxes projected in the Commission forecast compared to the Stability Programme.

Compared to the latest official projections, the Stability Programme further revises the medium-term trajectory of public finances, both in terms of the planned headline and structural deficits. It reduces the overall consolidation objective and further postpones it towards the end of the five-year presidential term.

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




*Source: Commission 2019 spring forecast (COM), Stability programme (SP)*

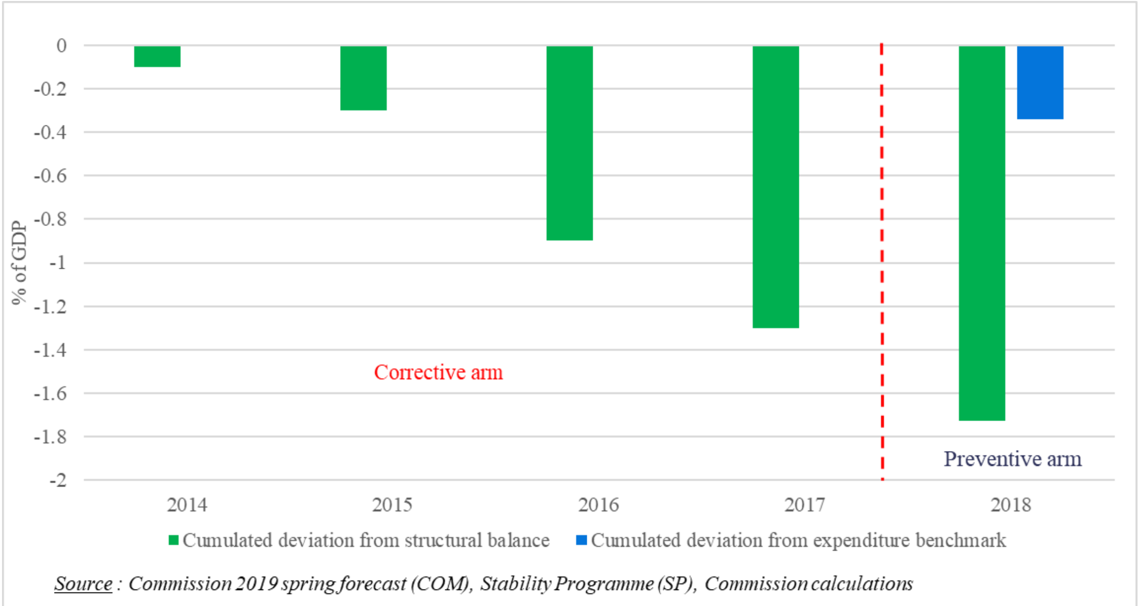
As shown in Figure 1, the deficit targets planned in successive Stability Programmes have been regularly scaled down over the last years, due to both the downward revision of macroeconomic projections as well as to the impact of discretionary measures adopted, including large one-offs.

Although with a lower level of ambition compared to past projections, the Stability Programme confirms a budgetary strategy based on continued efforts in terms of expenditure control at all levels of the general government, increasing towards the outer years, aimed at financing the progressive reduction of the tax burden. The expenditure-to-GDP ratio is planned to decrease by three percentage points, from 56.0% in 2018 down to 53.0% in 2022, with a reduction in all its components and mainly in social payments, subsidies and

compensation of employees. Such a sizeable decline is however not sufficiently underpinned by measures in the Stability Programme. In particular, specific spending review actions under the broader 'Public Action 2022' programme have not yet been specified, while further details are also needed concerning the measures already announced following the national public consultation (*Grand débat*) launched by the government at the end of 2018 (see section 3.5 below). The share of total revenues in GDP is set to decline from 53.5% in 2018 to 51.7% in 2022, mainly due to the reduction in social contributions, which took place already in 2019 (see section 3.3 below). The tax burden is planned to fall by almost 2 percentage points, to reach 44.8% in 2022.

Over the last five years, France regularly fell short of the structural effort requirements defined under both pillars of the SGP. As shown in figure 2, the cumulative deviation from the targets laid down in terms of adjustment in the structural balance consistently increased, going from 0.1% of GDP in 2014 to 1.7% of GDP in 2018. Lack of progress is observed also with regard to the limit on expenditure growth applicable since the correction of the excessive deficit in 2018. In this year, the deviation from the expenditure benchmark is 0.3% of GDP.

**Figure 2: Cumulative deviations of the preceding five years from the upper limit for net growth of government expenditure and from structural effort requirements (in % of GDP)**




### 3.3. MEASURES UNDERPINNING THE PROGRAMME

Compared to the Draft Budgetary Plan for 2019, the Stability Programme integrates a package of measures announced by the government at the end of 2018 and adopted either in the context of the 2019 Budget Law in December or via an ad hoc law approved by the parliament in April 2019[6]. These measures were taken in order to respond to the social unrest

[6] See footnote 4.

led by the so-called "yellow vests" movement and were aimed at increasing in the short term the purchasing power of the most vulnerable households. Overall, including the partially offsetting effect of some compensatory measures, the package had a net deficit-increasing impact of about EUR 6 billion (i.e. 0.3% of GDP) in 2019.

The measures from the December package reflected in the Stability Programme mainly concern the revenue side (see table below) and mainly imply the extension, amendment or reversal of previously adopted measures. In particular, the main ones with a deficit-increasing impact consist of the suspension of the planned increase in the carbon tax, diesel-gas convergence and tax increase on off-road diesel fuel (EUR 3.9 billion, 0.2% of GDP); a monthly wage increase of EUR 100 for workers at the minimum wage realised through higher in-work benefits (EUR 2.7 billion, 0.1% of GDP); the anticipation to January 2019 of the suppression of any social security contribution for extra hours and its extension to income tax (EUR 2.4 billion, 0.1% of GDP); the extension of the suspension of the increase in CSG (*Contribution Social Généralisée*) to retirees having a pension below EUR 2000 per month (EUR 1.3 billion, 0.1% of GDP). Deficit-decreasing measures, still on the revenue side, include the shift by one year and for firms with a turnover above EUR 250 million of the reduction of the corporate income tax rate from 33% to 31% (EUR 1.7 billion, 0.1% of GDP); the set up a new tax for internet groups (EUR 0.4 billion) and a reduction of the fiscal exemption on intra-group capital gains (*niche Copé,* EUR 0.2 billion). In order to further compensate for the deficit-increasing measures of the package, the authorities have also announced spending cuts by about EUR 1.5 billion (0.1% of GDP), which the Stability Programme indicates will be achieved in the context of the 2019 budgetary execution.

The main measures already included in previous programmes, with a significant incremental budgetary impact in 2019 or 2020 and confirmed in the Stability Programme, are also reported in the table below. On the revenue side, these include: the reduction of employers' social contributions associated with the transformation of the CICE (about EUR 24 billion in 2019 and EUR 3 billion in 2020, 1.0% of GDP and 0.1% of GDP, respectively); the reduction of social contributions associated with the increase of the CSG (*Contribution Social Généralisée*) (about EUR 4 billion in 2019, 0.2 % of GDP); the housing tax relief for 80% of the households (EUR 3.8 billion in 2019 and EUR 3.1 billion in 2020, 0.2% and 0.1% of GDP, respectively); the increase of the fifth instalment of corporate income tax (EUR 1.5 billion, 0.1% of GDP). On the expenditure side they include: the transformation of the CICE into a reduction in employers' social contributions (about EUR 20 billion in 2019, 1.0% of GDP); the under indexation of retirement pensions and other social benefits (EUR 3.5 billion, 0.1% of GDP); savings under the healthcare spending norm (EUR 3.8 billion, 0.2% of GDP).

Overall, most of the measures underpinning the Stability Programme are specified in sufficient detail or considered realistic and thus are included in the Commission 2019 spring forecast. As indicated in section 3.2 above, one difference concerns the assessment of savings stemming from the measure of under indexation of social payments. Based on the cancellation of the impact of the measure in 2020 by the French Constitutional Council at the end of 2018 and on the customary no-policy change assumption underpinning the Commission forecast, the latter does not consider this impact, corresponding to about 0.1% of GDP. Another difference concerns the one-off classification of the increase of the fifth instalment of corporate income tax. Opposite to the treatment adopted in the Stability Programme and in line with relevant guidelines and the treatment of similar measures in the recent past, the Commission spring forecast qualifies the former one as a one-off, while it does not so for the latter.

## Main budgetary measures included in the Programme

| Revenue | Expenditure |
|---|---|
| **2018** | |
| • Housing tax relief for 80% of households (-0.1% of GDP)<br>• Reduction of social contributions linked to CSG increase (-0.8 % of GDP)<br>• CSG increase linked to reduction of social contributions (1.0 % of GDP) | • Savings in State wage bill (0.1 % of GDP)<br>• Decrease in subsidised contracts (0.1 % of GDP)<br>• Changes in housing allowances (0.1 % of GDP) |
| **2019** | |
| • Suspension of planned increases in energy taxes (-0.2% of GDP)<br>• Suppression of social security contributions and income tax on extra hours (-0.1% of GDP)<br>• Suspension of the increase in CSG for modest pensions (-0.1% of GDP)<br>• Temporary shift of the reduction in corporate income tax for big firms (0.1% of GDP)<br>• Reduction of employers’ social contributions linked to transformation of the CICE (-1.0% of GDP)<br>• Reduction of social contributions linked to CSG increase (-0.2 % of GDP)<br>• Housing tax relief for 80% of households (-0.2% of GDP)<br>• Increase of the fifth instalment of corporate income tax (0.1% of GDP) | • Monthly wage increase of EUR 100 Euro at the minimum wage (0.1 % of GDP)<br>• Savings in budgetary execution (-0.1 % of GDP)<br>• CICE transformation into reduction in employers' contributions (-0.9% of GDP)<br>• Under indexation of pensions and other social benefits (-0.1% of GDP)<br>• Savings under healthcare spending norm (-0.2% of GDP) |
| **2020** | |
| • Reduction of employers’ social contributions linked to transformation of the CICE (-0.1% of GDP)<br>• Housing tax relief for 80% of households (-0.1% of GDP) | • Under indexation of pensions and other social benefits (-0.1% of GDP) |

Note: The table refers to the main measures included in the 2019 Stability Programme that have an incremental budgetary impact over the programme period. The budgetary impact in the table is the impact reported in the programme, i.e. by the national authorities. A positive sign implies that revenue / expenditure increases as a consequence of this measure.

### 3.4. DEBT DEVELOPMENTS

Public debt rose steadily between 2013 and 2017, from 93.4% to 98.4% of GDP, due to the cumulated high general government deficits recorded over the same period as well as low nominal GDP growth in most of the years. In 2018, the public debt-to-GDP ratio stabilised at 98.4%. The debt-increasing effect stemming from the headline primary deficit and interest expenditure was offset by economic growth, the GDP deflator inflation, both through the denominator effect, and by the marginally debt-reducing impact of stock-flow adjustments.

According to the Stability Programme, the public debt ratio is forecast to peak at 98.9% of GDP in 2019 and start to decrease in 2020 (see Figure 2). The planned increase in 2019 is mainly due to the temporary rise of the primary deficit to 1.5% due to the impact of the CICE transformation. However, once this effect vanishes, the primary deficit is forecast to narrow to 0.5% of GDP in 2020. Thereafter, the primary balance is planned to keep improving over the programme horizon, to reach a primary surplus of 0.4% of GDP in 2022. At the same time, the debt-reducing contribution by the snow-ball effect is planned to progressively strengthen until 2022, mainly due to the debt-reducing impact of real GDP growth and inflation (see Table 3). In turn, while the contribution of interest payments to the increase in public debt is projected to bottom-out in 2019 and 2020, interest payments are expected to trend up thereafter. The stock-flow adjustments are expected to be slightly negative in 2019. As of 2020, however, stock-flow adjustments are envisaged to contribute to increasing the public debt ratio, mainly due to net impact of premium on debt issuance ("prime et décote à l'émission net de l'étalement des primes passées") and the residual budgetary effects in cash terms of the CICE transformation after 2019.

For 2019 and 2020, the Commission 2019 spring forecast projects a gross debt ratio broadly in line with the Stability Programme.

**Table 3: Debt developments**

| (% of GDP) | Average 2013-2017 | 2018 | 2019 | | 2020 | | 2021 | 2022 |
|---|---|---|---|---|---|---|---|---|
| | | | COM | SP | COM | SP | SP | SP |
| **Gross debt ratio[1]** | **96.1** | **98.4** | **99.0** | **98.9** | **98.9** | **98.7** | **98.1** | **96.8** |
| Change in the ratio | 1.6 | 0.0 | 0.6 | 0.5 | -0.1 | -0.2 | -0.6 | -1.3 |
| *Contributions[2]:* | | | | | | | | |
| **1. Primary balance** | **1.6** | **0.8** | **1.5** | **1.5** | **0.5** | **0.5** | **0.1** | **-0.4** |
| **2. "Snow-ball" effect** | **0.2** | **-0.7** | **-0.9** | **-0.9** | **-1.0** | **-1.1** | **-1.3** | **-1.3** |
| *Of which:* | | | | | | | | |
| Interest expenditure | 2.0 | 1.7 | 1.6 | 1.5 | 1.6 | 1.5 | 1.6 | 1.7 |
| Growth effect | -1.1 | -1.5 | -1.3 | -1.3 | -1.4 | -1.4 | -1.3 | -1.3 |
| Inflation effect | -0.6 | -0.9 | -1.3 | -1.1 | -1.2 | -1.1 | -1.4 | -1.6 |
| **3. Stock-flow adjustment** | **-0.3** | **-0.1** | **0.1** | **-0.1** | **0.4** | **0.4** | **0.6** | **0.4** |
| *Of which:* | | | | | | | | |
| Cash/accruals diff. | | | | | | | | |
| Acc. financial assets | | | | | | | | |
| *Privatisation* | | | | | | | | |
| Val. effect & residual | | | | | | | | |

Notes:

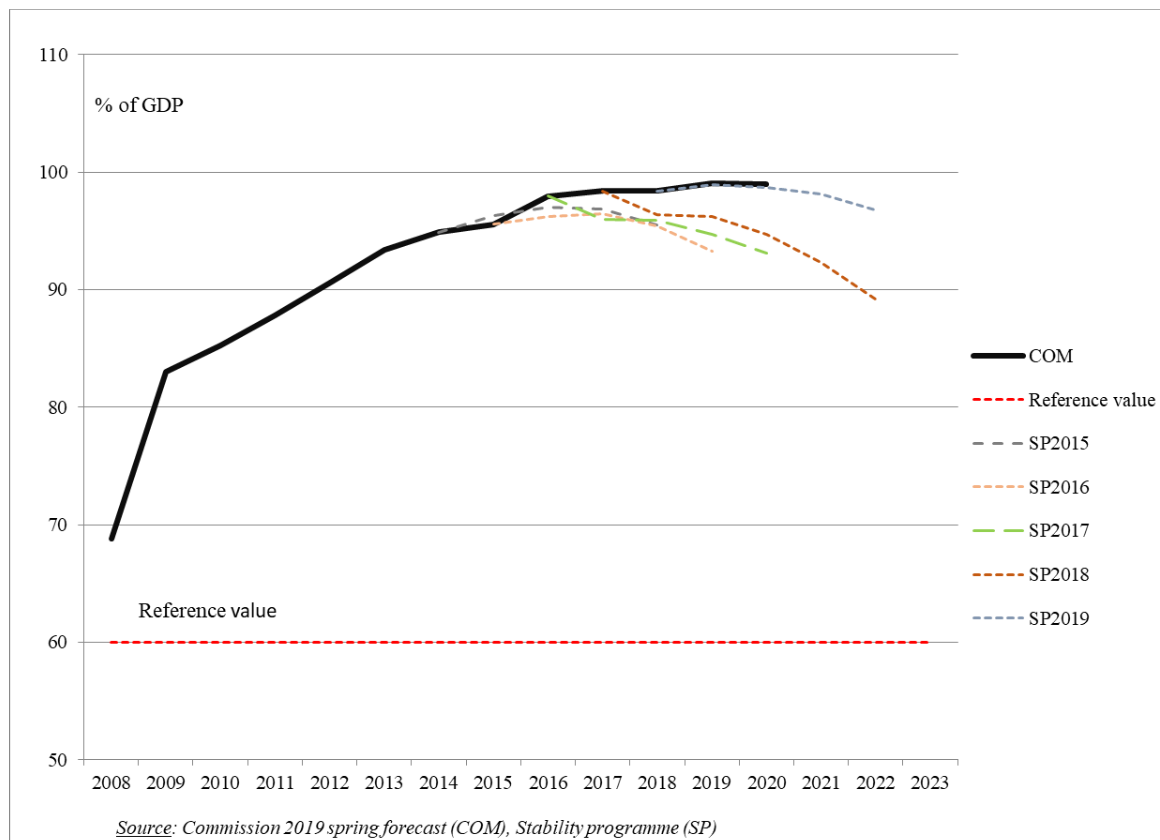
[1] End of period.

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

*Source :*

*Commission 2019 spring forecast (COM); Stability Programme (SP), Comission calculations.*

**Figure 3: Government debt projections in successive programmes (% of GDP)**




## 3.5. RISK ASSESSMENT

The headline deficit target of 3.1% of GDP for 2019 in the Stability Programme is in line with the Commission 2019 spring forecast projection for the same year, although the macroeconomic scenario underpinning the former is slightly more favourable. By contrast, the planned headline deficit in the Stability Programme is 0.2 pps. lower than in the Commission forecast in 2020, despite the expected GDP growth rate in the Programme being 0.1 pp. lower than projected by the Commission.

Regarding 2020, the main differences between the fiscal scenarios in the two sets of projections are related to the customary no-policy change assumption underpinning the Commission spring forecast projections for 2020. Specifically, the Commission spring forecast does not take on board the savings stemming from the under indexation of pensions as this measure was cancelled by the French Constitutional Council at the end of 2018. Despite the cancellation, French authorities kept this measure in the Stability Programme as they plan to reintroduce it in the 2020 Draft Budgetary Plan, thereby addressing the procedural issues raised by the Constitutional Council.

Overall, the risks to the fiscal projections for 2019-2020 appear broadly contained although somewhat tilted to the downside. Specifically, for 2019 no details have been offered yet regarding the planned expenditure savings by EUR 1.5 bn. to partly offset the deficit-increasing impact of the measures adopted at the end of 2018 in response to the “yellow vests” crisis. For 2020, details about the net impact of most measures announced on 25 April,

following the end of the "*Grand Débat National*", are still lacking. More in general, the outcome of the *Grand débat* could lead to further amendments to the overall public finance consolidation strategy, as public consensus on the economic and social priorities to address over the remainder of the presidential term will remain a key factor.

For the outer years covered by the programme, the budgetary strategy of the French government remains subject to risks. The reduction of government debt is planned to take place only in the second half of the five-year term. While the objective in terms of aggregate taxes and social security contributions is set to be attained in 2019, actions for reducing public spending, notably through a spending review process, have not been fully clarified yet. This backloads the adjustment necessary to reach the deficit and debt goals to the end of the government mandate, when electoral considerations might make these objectives more challenging.

## 4. COMPLIANCE WITH THE PROVISIONS OF THE STABILITY AND GROWTH PACT

France is currently subject to the preventive arm of the SGP and to the three-year transition period as regards compliance with the debt criterion. As such, France needs to ensure an appropriate adjustment path towards its MTO, defined as a structural deficit of 0.4% of GDP, and to make sufficient progress towards compliance with the debt reduction benchmark.

**Box 1. Council Recommendations addressed to France**

*On 13 July 2018, the Council addressed recommendations to France in the context of the European Semester. In particular, in the area of public finances the Council recommended to France "Ensure that the nominal growth rate of net primary government expenditure does not exceed 1.4% in 2019, corresponding to an annual structural adjustment of 0.6 % of GDP. Use windfall gains to accelerate the reduction of the general government debt ratio*."

### 4.1. Compliance with the deficit criterion

Based on the Commission 2019 spring forecast, the headline general government deficit in 2019 is expected to increase to 3.1% of GDP, thereby exceeding the 3% of GDP reference value in the Treaty. The projected increase of the headline deficit in 2019 compared to 2018 stems from the statistical impact of the transformation of the tax credit for competitiveness and employment (CICE) into a permanent outright reduction of employer's social contributions, which accounts for about 0.9% of GDP. This impact is considered as a one-off, therefore having no negative impact per se in the projected fiscal stance. Without this effect, the headline deficit would be projected at 2.2% of GDP.

The planned breach of the deficit criterion in 2019 suggests prima facie the existence of an excessive deficit in France in the sense of the Treaty and the SGP. The Commission has therefore prepared a report under Article 126(3) TFEU analysing whether or not France is compliant with the deficit criterion of the Treaty. The report concluded, following an assessment of all the relevant factors, that the deficit criterion as defined in the Treaty and in Council Regulation (EC) No 1467/97 should be considered as currently complied with.

### 4.2. Compliance with the debt criterion

France corrected its excessive deficit in 2017. As the debt ratio exceeded the 60% of GDP Treaty reference value in 2017 (the year in which France corrected its excessive deficit), during the three years following the correction of the excessive deficit France is also subject to the transitional arrangements to make sufficient progress towards compliance with the debt reduction benchmark. This implies that, during this period, it is required to make sufficient progress (as defined by the minimum linear structural adjustment (MLSA)) towards compliance with the debt reduction benchmark at the end of the transition period.

According to notified data and the Commission 2019 spring forecast, the change in the structural balance amounted to 0.2% of GDP in 2018, falling short of the required structural improvement of 0.7% of GDP under the MLSA. This suggests prima facie a risk of the existence of an excessive deficit in France in the sense of the Treaty and the Stability and Growth Pact. The Commission has therefore prepared a report under Article 126(3) TFEU analysing whether or not France is compliant with the debt criterion of the Treaty. The report concluded, following an assessment of all the relevant factors, that the debt criterion as defined in the Treaty and in Council Regulation (EC) No 1467/97 should be considered as currently complied with.

**Table 4. Compliance with the debt criterion**

| | **2018** | **2019** | | **2020** | |
|---|---|---|---|---|---|
| | | **SP** | **COM** | **SP** | **COM** |
| Gross debt ratio | **98.4** | **98.9** | **99.0** | **98.7** | **98.9** |
| Gap to the debt benchmark [1,2] | | | | | |
| Structural adjustment [3] | 0.2 | 0.2 | 0.0 | 0.1 | 0.0 |
| *To be compared to:* | | | | | |
| Required adjustment [4] | 0.7 | 0.8 | 0.9 | 1.4 | 1.8 |

Notes:

[1] Not relevant for Member Sates that were subject to an EDP procedure in November 2011 and for a period of three years following the correction of the excessive deficit.

[2] Shows the difference between the debt-to-GDP ratio and the debt benchmark. If positive, projected gross debt-to-GDP ratio does not comply with the debt reduction benchmark.

[3] Applicable only during the transition period of three years from the correction of the excessive deficit for EDP that were ongoing in November 2011.

[4] Defines the remaining annual structural adjustment over the transition period which ensures that - if followed – Member State will comply with the debt reduction benchmark at the end of the transition period, assuming that COM (S/CP) budgetary projections for the previous years are achieved.

Source :
*Commission 2019 spring forecast (COM); Stability Programme (SP), Comission calculations.*

Based on the plans in the Stability Programme, the annual changes in the recalculated structural balance are set to fall short of the required improvements under the MLSA. This

conclusion is confirmed by the Commission 2019 spring forecast. According to the Commission, the structural balance is forecast to barely change in 2019, thereby falling short of the required improvement of 0.9% of GDP under the MLSA. For 2020, the structural balance is also projected to remain largely stable, which implies a sizeable deviation from the required improvement of 1.8% of GDP under the MLSA. The projected deviations exceed in all years ¼% of GDP and the remaining annual structural adjustment always exceed ¾% of GDP over the transition period. Accordingly, France is currently expected to exceed the room for manoeuvre embedded in the rule.

Consequently, based on both an overall assessment of the plans in the Stability Programme and on the Commission 2019 spring forecast, France is not projected to make sufficient progress towards compliance with the debt reduction benchmark in 2019 and 2020.

### 4.3. Compliance with the MTO or the required adjustment path towards the MTO

The nominal growth rate of primary government expenditure, net of discretionary revenue measures and one-offs, exceeded the applicable expenditure benchmark of 1.2% in 2018, leading to a deviation of 0.3% of GDP in the underlying fiscal position, thus pointing to some deviation from the recommended adjustment path towards the MTO in 2018 based on the Commission 2019 spring forecast. In turn, the structural balance improved by 0.2 percentage points of GDP in 2018, thus also pointing to some deviation from the recommended structural adjustment of 0.6% of GDP towards the MTO. As the overall assessment does not show any significant discrepancy between the two metrics, based on outturn data, it points to some deviation from the recommended adjustment path towards the MTO in 2018.

For 2019, based on the information provided in the Stability Programme, the nominal growth rate of primary government expenditure, net of discretionary revenue measures and one-offs, is expected to exceed the applicable expenditure benchmark of 1.4%, leading to a gap of 0.6% of GDP, thus pointing to a risk of significant deviation from the recommended adjustment path towards the MTO. The recalculated change in the structural balance is estimated at 0.2% of GDP, falling short of the required adjustment by 0.4% of GDP, pointing to a risk of some deviation (see Table 6). This calls for an overall assessment. The overall assessment shows that the fiscal effort measured by the change in the structural balance is mainly favoured by the sizeable planned decline in interest payments, largely beyond the control of the government, and by the estimated potential growth above its medium-term average used in its calculation. Therefore, the projected nominal growth rate of primary government expenditure, net of discretionary revenue measures and one-offs, is deemed to provide a more accurate picture of the underlying fiscal effort. Accordingly, the overall assessment, based on data in the programme, points to a risk of significant deviation from the recommended adjustment path towards the MTO in 2019. Taking 2018 and 2019 together, the average deviation from the expenditure benchmark pillar amounts to 0.5% of GDP, while the average shortfall in the change in the structural balance amounts to 0.4% of GDP, thereby pointing to a risk of significant deviation in 2019 too.

These conclusions are broadly confirmed by the Commission 2019 spring forecast. More specifically, according to the Commission forecast, both metrics point to a risk of significant deviation in 2019 and also in 2018 and 2019 taken together. The lower effort estimated by the Commission in 2019 mainly stems from a different treatment, compared to the Stability Programme, of two measures in terms of their one-off nature. Namely, the Commission spring forecast qualifies as one-off the increase of the fifth instalment of corporate income tax, while it does not so for the change of recording of sales of Hertzian licences.

Based on the information provided in the Stability Programme, the nominal growth rate of primary government expenditure, net of discretionary revenue measures and one-offs in 2020, is expected to exceed the applicable expenditure benchmark of 1.2% in 2020, leading to a deviation of 0.7% of GDP in the underlying fiscal position, thus pointing to a risk of significant deviation from the recommended adjustment path towards the MTO. The recalculated change in the structural balance is estimated at 0.1% of GDP, falling short of the required adjustment by 0.5% of GDP and pointing to a risk of some deviation (see Table 6). The overall assessment shows that the fiscal effort as measured by the change in the structural balance is favoured by the different potential growth used in its calculation and the planned decline in public investment linked to the local electoral cycle. For these reasons, the projected nominal growth rate of primary government expenditure, net of discretionary revenue measures and one-offs, is deemed to provide a more accurate picture of the underlying fiscal effort. Accordingly, the overall assessment, based on data in the programme, points to a risk of significant deviation. Moreover, taking 2019 and 2020 together, the average deviation from the expenditure benchmark pillar amounts to 0.6% of GDP, while the average shortfall in the accumulated change in the structural balance would amount to 0.4% of GDP, also pointing to a risk of significant deviation from the recommended adjustment path towards the MTO in 2020.

For 2020, based on the Commission 2019 spring forecast, at unchanged policies, the nominal growth rate of government expenditure, net of discretionary revenue measures and one-offs, is projected to exceed the applicable expenditure benchmark of 1.2% by 0.7% of GDP, pointing to a risk of a significant deviation. Likewise, the structural balance is projected to barely change, falling short of the required improvement of 0.6% of GDP by 0.6 pps., also implying a risk of a significant deviation. The overall assessment does not show material differences between the two metrics. When 2019 and 2020 are taken together, the average deviation from the expenditure benchmark amounts to 0.7% of GDP and to 0.6% of GDP in the case of the structural balance. Accordingly, the two pillars point to a risk of significant deviation from the recommended adjustment path towards the MTO in 2020.

## Table 5: Compliance with the requirements under the preventive arm

| (% of GDP) | 2018 | 2019 | | 2020 | |
|---|---|---|---|---|---|
| **Background budgetary indicators**[1] | | | | | |
| Medium-term objective (MTO) | -0,4 | -0,4 | | -0,4 | |
| Structural balance[2] (COM) | -2,6 | -2,6 | | -2,5 | |
| ***Setting the required adjustment to the MTO*** | | | | | |
| Structural balance based on freezing (COM) | -2,1 | -2,6 | | - | |
| Position vis-a -vis the MTO[3] | Not at MTO | Not at MTO | | Not at MTO | |
| Required adjustment[4] | 0,6 | 0,6 | | 0,6 | |
| Required adjustment corrected[5] | 0,6 | 0,6 | | 0,6 | |
| Corresponding expenditure benchmark[6] | 1,2 | 1,4 | | 1,2 | |
| ***Compliance with the required adjustment to the MTO*** | | | | | |
| | **COM** | **SP** | **COM** | **SP** | **COM** |
| *Structural balance pillar* | | | | | |
| Change in structural balance[7] | 0,2 | 0,2 | 0,0 | 0,1 | 0,0 |
| *One-year deviation from the required adjustment*[8] | -0,4 | -0,4 | -0,6 | -0,5 | -0,6 |
| *Two-year average deviation from the required adjustment*[8] | | -0,4 | -0,5 | -0,4 | -0,6 |
| *Expenditure benchmark pillar* | | | | | |
| Net public expenditure annual growth corrected for one-offs[9] | 1,9 | 2,6 | 2,9 | 2,5 | 2,6 |
| One-year deviation adjusted for one-offs[10] | -0,3 | -0,6 | -0,8 | -0,7 | -0,7 |
| Two-year deviation adjusted for one-offs[10] | | -0,5 | -0,6 | -0,6 | -0,7 |
| ***Finding of the overall assessment*** | **Some deviation** | Significant deviation | Significant deviation | Significant deviation | Significant deviation |

***Legend***

'*Compliance*' - the recommended structural adjustment or a higher adjustment is being observed.

'*Some deviation*' - a deviation from the recommended structural adjustment is being observed, but it is below the threshold for a significant deviation.

'*Significant deviation*' - a deviation which has reached or breached the threshold for a significant deviation (i.e. 0.5% of GDP over one year, 0.25% of GDP over two years on average).

***Notes***

[1] The most favourable level of the structural balance, measured as a percentage of GDP reached at the end of year t-1, between spring forecast (t-1) and the latest forecast, determines whether there is a need to adjust towards the MTO or not in year t. A margin of 0.25 percentage points (p.p.) is allowed in order to be evaluated as having reached the MTO.

[2] Structural balance = cyclically-adjusted government balance excluding one-off measures.

[3] Based on the relevant structural balance at year t-1.

[4] Based on the position vis-à-vis the MTO, the cyclical position and the debt level (See European Commission: Vade mecum on the Stability and Growth Pact, page 38.).

[5] Required adjustment corrected for the clauses, the possible margin to the MTO and the allowed deviation in case of overachievers.

[6] Reference medium-term rate of potential GDP growth. The (standard) reference rate applies from year t+1, if the country has reached its MTO in year t. A corrected rate applies as long as the country is adjusting towards its MTO, including in year t.

[7] Change in the structural balance compared to year t-1. Ex post assessment (for 20XX-1) is carried out on the basis of Commission 20XX spring forecast.

[8] The difference of the change in the structural balance and the corrected required adjustment.

[9] Net public expenditure annual growth (in %) corrected for discretionary revenue measures, revenue measures mandated by law and one-offs (nominal)

[10] Deviation of the growth rate of public expenditure net of discretionary revenue measures, revenue increases mandated by law and one-offs from the applicable reference rate in terms of the effect on the structural balance. The expenditure aggregate used for the expenditure benchmark is obtained following the commonly agreed methodology. A negative sign implies that expenditure growth exceeds the applicable reference rate.

*Source* :
*Stability Programme (SP); Commission 2019 spring forecast (COM); Commission calculations.*

## 5. DEBT SUSTAINABILITY ANALYSIS AND FISCAL RISKS

France does not appear to face fiscal sustainability risks in the short run. Nonetheless, there are some indications that the fiscal side of the economy poses potential challenges.[7]

Based on Commission 2019 spring forecasts and a no-fiscal policy change scenario beyond the forecast horizon, government debt, projected at 99.0% of GDP in 2019, is expected to rise to 106.3% in 2029, thus remaining above the 60% of GDP Treaty threshold. Over this horizon, government debt is projected to peak in 2029. Sensitivity analysis shows similar risks.[8] Overall, this highlights high risks for the country from debt sustainability analysis in the medium term. The full implementation of the Stability Programme would lead to lower debt levels until 2029, despite being insufficient to put the debt level on a clearly declining path, thereby remaining well above the 60% of GDP reference value.

The medium-term fiscal sustainability risk indicator S1[9] is at 5.0 percentage points of GDP. Its value is primarily related to the high level of government debt, contributing 3.0 percentage points of GDP. The medium-term fiscal sustainability risk indicator S1 thus signals high risks in the medium term. The full implementation of the Stability Programme would put the sustainability risk indicator S1 at 4.5 percentage points of GDP. Based on the debt sustainability analysis and the S1 indicator, overall medium-term fiscal sustainability risks are, therefore, high. Fully implementing the fiscal plans in the Stability Programme would decrease those risks though only slightly, reflecting the insufficient planned fiscal effort by the French authorities given the high debt burden.

The long-term fiscal sustainability risk indicator S2 is at 0.4% of GDP. In the long-term, France therefore appears to face low fiscal sustainability risks, primarily related to the initial budgetary position, contributing 1.9 percentage points of GDP, which is largely offset by the projected decline in age-related expenditure, mainly in pensions. Full implementation of the programme would nonetheless put the S2 indicator at –0.7 percentage points of GDP, leading to an even lower long-term risk.[10] The debt sustainability analysis discussed above points to high risks so that, overall, long-term fiscal sustainability risks are assessed as medium for France.

---

[7] This conclusion is based on the short-term fiscal sustainability risk indicator S0. See the note to Table 6 for a definition of the indicator.

[8] Sensitivity analysis includes several deterministic debt projections, as well as stochastic projections (see Fiscal Sustainability Report 2018 for more details).

[9] See the note to Table 6 for a definition of the indicator.

[10] The projected costs of ageing that are used to compute the debt projections and the fiscal sustainability indicators S1 and S2 are based on the projections of the 2018 Ageing Report.

## Table 6: Debt sustainability analysis and sustainability indicators

| *Time horizon* | | | **Commission Scenario** | | **Stability / Convergence Programme Scenario** | |
|---|---|---|---|---|---|---|
| **Short-term** | | | **LOW risk** | | | |
| **S0 indicator [1]** | | | 0.2 | | | |
| Fiscal subindex | | | 0.4 | HIGH risk | | |
| Financial & competitiveness subindex | | | 0.2 | LOW risk | | |
| **Medium-term** | | | **HIGH risk** | | | |
| **DSA [2]** | | | HIGH risk | | | |
| **S1 indicator [3]** | | | 5.0 | HIGH risk | 4.5 | HIGH risk |
| of which | Initial Budgetary Position | | 1.6 | | 0.9 | |
| | Debt Requirement | | 3.0 | | 3.3 | |
| | Cost of Ageing | | 0.4 | | 0.3 | |
| | *of which* | Pensions | 0.3 | | 0.2 | |
| | | Health care | 0.2 | | 0.1 | |
| | | Long-term care | 0.1 | | 0.1 | |
| | | Other | -0.2 | | -0.2 | |
| **Long-term** | | | **MEDIUM risk** | | | |
| **DSA [2]** | | | HIGH risk | | | |
| **S2 indicator [4]** | | | 0.4 | LOW risk | -0.7 | LOW risk |
| of which | Initial Budgetary Position | | 1.9 | | 1.1 | |
| | Cost of Ageing | | -1.5 | | -1.8 | |
| | *of which* | Pensions | -2.0 | | -2.1 | |
| | | Health care | 0.3 | | 0.3 | |
| | | Long-term care | 0.5 | | 0.5 | |
| | | Other | -0.4 | | -0.4 | |

Source: Commission services; 2019 stability/convergence programme.

Note: the 'Commission' scenario depicts the sustainability gap under the assumption that the structural primary balance position evolves according to the Commissions' spring 2019 forecast until 2020. The 'stability/convergence programme' scenario depicts the sustainability gap under the assumption that the budgetary plans in the programme are fully implemented over the period covered by the programme. Age-related expenditure as given in the 2018 Ageing Report.

[1] The S0 indicator of short term fiscal challenges informs the early detection of fiscal stress associated to fiscal risks within a one-year horizon. To estimate these risks S0 uses a set of fiscal, financial and competitiveness indicators selected and weighted according to their signalling power. S0 is therefore a composite indicator whose methodology is fundamentally different from the S1 and S2 indicators, which quantify fiscal adjustment efforts. The critical threshold for the overall S0 indicator is 0.46. For the fiscal and the financial-competitiveness sub-indexes, thresholds are respectively at 0.36 and 0.49*.

[2] Debt Sustainability Analysis (DSA) is performed around the no fiscal policy change scenario in a manner that tests the response of this scenario to different shocks presented as sensitivity tests and stochastic projections*.

[3] The S1 indicator is a medium-term sustainability gap; it measures the upfront fiscal adjustment effort required to bring the debt-to-GDP ratio to 60 % by 2033. This adjustment effort corresponds to a cumulated improvement in the structural primary balance over the 5 years following the forecast horizon (i.e. from 2021 for Commission scenario and from last available year for the SCP scenario); it must be then sustained, including financing for any additional expenditure until the target date, arising from an ageing population. The critical thresholds for S1 are 0 and 2.5, between which S1 indicates medium risk. If S1 is below 0 or above 2.5, it indicates low or high risk, respectively*.

[4] The S2 indicator is a long-term sustainability gap; it shows the upfront and permanent fiscal adjustment required to stabilise the debt-to-GDP ratio over the infinite horizon, including the costs of ageing. The critical thresholds for S2 are 2 and 6, between which S2 indicates medium risk. If S2 is below 2 or above 6, it indicates low or high risk, respectively*.

* For more information see Fiscal Sustainability Report 2018.

## 6. FISCAL FRAMEWORK

A steady decline in public debt will depend on the government's ability to reduce spending. Since 2017, the government has put in place a new fiscal consolidation strategy throughout the five-year presidential term. Its success will depend on achieving planned spending targets for central and local governments, as well as for the health system. This relies on a full implementation of the still undefined Public Action 2022 (*Action Publique 2022,* AP2022), aiming at achieving substantial efficiency gains and savings in public spending while improving the functioning of national public administration, a process akin to spending reviews.

Based on the information provided in the 2019 Stability Programme, the past, planned and forecast fiscal performance with regard to the main applicable numerical fiscal rule in France, namely the balanced-budget rule in structural terms for the general government, appears to move away from the country-specific MTO of -0.4% of GDP, as well as from the plans set in the multiannual programming law for 2018-2022 and in the 2018 Stability Programme. As also noted by the High Council for Public Finances[11], the distance between the structural balance planned for 2022 and the MTO has widened in the successive budgetary planning documents to around 0.9 pp of GDP.

The two new expenditure ceilings introduced by the 2018-2022 multiannual programming law for public finances have reinforced budgetary control at the State level. The first ceiling focuses on a narrower definition of spending directly under the control of the government whereas the other applies to the total spending of the State. These two ceilings have replaced the former State expenditure ceilings imposing no growth for public expenditure measured in real terms and setting a ceiling on all public spending out of the perimeter of debt and pensions.

The growth ceiling for healthcare expenditure covering a third of social security spending, the ONDAM (*Objectif National de Dépenses d'Assurance Maladie*), has been increased from 2.1% in 2017 up to 2.5% in the 2019 Draft Budgetary Plan. The increase partly reflects the additional expenses to be incurred by the healthcare reform 'Ma santé 2022', whose draft law is now under discussion in the Parliament. While this reform represents an additional step to shift the traditionally hospital-centred healthcare systems towards strengthened primary care and to increase the quality of service, it does not include a revision of the growth norm for healthcare expenditure. Notwithstanding the continued respect of this ceiling, the margin with which the planned expenditure target is achieved has narrowed since 2016. For example, in 2018, the planned execution for primary care expenses (exceeding the planned target by EUR 560 million) and hospital care expenses (EUR 105 million below the planned target) highlighted a risk of surpassing the overall ONDAM target by EUR 455 million. This result had to be compensated by the mobilization of credits set aside at the beginning of the year (EUR 625 million).[12]

Since 2014, the public expenditure of the local administration in France is guided by an expenditure ceiling indicating yearly non-binding growth targets for both operating public expenditure and financing needs at local level ('Objectif d'évolution de la Dépense Locale', ODEDEL). In 2018, this ceiling has been accompanied by legally binding contract

[11] High Council for Public Finances' Opinion on the 2019 Stability Programme, 9 April 2019

[12] Les comptes de la sécurité sociale, Rapport Septembre 2018.

agreements between the state and 71% of the 322 biggest local authorities, valid in 2018-2020. This contractual approach may help to respect the spending ceiling for operational expenditure at local level, set at a rate of 1.2% up to horizon 2022. It is to be seen, however, how this approach will help the rationalisation of the local administration started in 2014 as local authorities' contribution to the savings effort remains constrained by the current structure of the local administration. Indeed, the territorial reform of 2014-2016 cut by half the number of regions but the number of communes only slightly decreased, remaining by far the highest in the EU at above 34 000.

The definition of the new approach to the evaluation of public policies launched in October 2017, Public Action 2022, remains incomplete. The programme has set 3 main objectives for this strategy, namely, the improvement of the quality of public services, the modernisation of public administration and the support to the reduction of the expenditure-to-GDP ratio by 3 percentage points by 2022. The government, however, has given clear priority to methodological and process-related aspects rather than focusing on the ex-ante and across-the-board quantification of potential savings. While this could be consistent with a complex reform process and the need to smoothen the public debate over likely sensitive issues, it also makes the quantitative assessment of the overall strategy and of its contribution to fiscal consolidation difficult.

The Stability Programme can also be considered as the national medium-term fiscal plan in line with the requirements of the Two Pack regulation 473/2013, although this document does not explicitly recall the obligations set out in Art. 4(1) according to which euro area Member States have to make public by 30 April each year their national medium-term fiscal plans, including an assessment of the expected economic returns on non-defence public investment projects having a significant budgetary impact.

*The macroeconomic forecast underlying the Stability Programme*

The High Council for Public Finances (HCPF), the independent monitoring body attached to the French Court of Auditors, released on 10 April an opinion endorsing the macroeconomic forecasts underlying the Stability Programme. In its opinion, the HCPF considers that the macroeconomic scenario underpinning the Stability Programme is realistic regarding the 2019 macroeconomic projections for GDP growth, employment and salary mass, while the inflation projections are plausible. Moreover, the HCFP also flagged that potential growth and output gap estimates, while surrounded by uncertainty, are reasonable and fall within the range of available estimates. Furthermore, the HCPF highlights the need to respect the revised targets in terms of public expenditure reduction, especially in view of the stronger reduction of tax revenues, the upward revision to the debt trajectory and the higher deficits than planned in the Draft Budgetary Plan.

## 7. SUMMARY

France registered a headline deficit of 2.5% of GDP in 2018. At the same time, France registered an improvement of the structural balance of 0.2% of GDP, which implies a deviation of 0.4% of GDP from the required adjustment path towards the MTO. In turn, the growth rate of government expenditure, net of discretionary revenue measures, exceeded the applicable expenditure benchmark rate by 0.3% of GDP. Following an overall assessment, this points to some deviation from the recommended adjustment path towards the MTO.

According to outturn data, France did not comply, prima facie, with the transitional debt rule in 2018 and thus appears to be a risk of the existence of an excessive deficit in the sense of the Treaty and the SGP. Moreover, according to the Stability Programme, the headline general government deficit in 2019 is planned to increase to 3.1% of GDP, thereby exceeding the 3% of GDP reference value in the Treaty. The Commission has therefore prepared a report under Article 126(3) TFEU analysing whether France is compliant with the debt criterion in 2018 and with the deficit criterion of the Treaty in 2019. The report concluded, following an assessment of all the relevant factors, that the deficit and debt criteria as defined in the Treaty and in Council Regulation (EC) No 1467/97 should be considered as currently complied with.

For 2019, based on the information in the Stability Programme, the overall assessment points to a risk of significant deviation with respect to the adjustment path towards the MTO in 2019. The Commission 2019 spring forecast confirms this conclusion.

Similarly, based on Stability Programme, France is at risk of significant deviation with respect to the adjustment path towards the MTO in 2020, in line with the Commission

Based on the Stability Programme, France is not expected to comply with the transitional debt rule in 2019 and 2020. This is confirmed by the Commission 2019 spring forecast.

## 8. ANNEXES

### Table I. Macroeconomic indicators

| | 2001-2005 | 2006-2010 | 2011-2015 | 2016 | 2017 | 2018 | 2019 | 2020 |
|---|---|---|---|---|---|---|---|---|
| **Core indicators** | | | | | | | | |
| GDP growth rate | 1.7 | 0.8 | 1.0 | 1.2 | 2.2 | 1.6 | 1.3 | 1.5 |
| Output gap [1] | 1.4 | 0.5 | -1.1 | -1.0 | 0.0 | 0.4 | 0.5 | 0.7 |
| HICP (annual % change) | 2.0 | 1.7 | 1.2 | 0.3 | 1.2 | 2.1 | 1.3 | 1.4 |
| Domestic demand (annual % change) [2] | 1.9 | 1.1 | 1.1 | 1.7 | 2.0 | 1.0 | 1.3 | 1.6 |
| Unemployment rate (% of labour force) [3] | 8.4 | 8.5 | 10.0 | 10.1 | 9.4 | 9.1 | 8.8 | 8.5 |
| Gross fixed capital formation (% of GDP) | 21.3 | 22.7 | 22.0 | 21.9 | 22.5 | 22.9 | 23.2 | 23.3 |
| Gross national saving (% of GDP) | 22.9 | 22.5 | 21.7 | 21.9 | 22.8 | 22.9 | 23.3 | 23.4 |
| **General Government (% of GDP)** | | | | | | | | |
| **Net lending (+) or net borrowing (-)** | **-3.1** | **-4.5** | **-4.3** | **-3.5** | **-2.8** | **-2.5** | **-3.1** | **-2.2** |
| **Gross debt** | **63.3** | **73.2** | **92.5** | **98.0** | **98.4** | **98.4** | **99.0** | **98.9** |
| **Net financial assets** | **-40.1** | **-43.4** | **-69.9** | **-82.5** | **-80.2** | **n.a** | **n.a** | **n.a** |
| Total revenue | 49.7 | 50.1 | 52.6 | 53.0 | 53.6 | 53.5 | 52.4 | 52.3 |
| Total expenditure | 52.8 | 54.6 | 56.9 | 56.6 | 56.4 | 56.0 | 55.5 | 54.4 |
| *of which: Interest* | 2.9 | 2.6 | 2.4 | 1.8 | 1.7 | 1.7 | 1.6 | 1.6 |
| **Corporations (% of GDP)** | | | | | | | | |
| **Net lending (+) or net borrowing (-)** | **1.4** | **0.9** | **0.0** | **0.1** | **-0.5** | **-0.8** | **-0.5** | **-1.4** |
| **Net financial assets; non-financial corporations** | **-85.9** | **-95.9** | **-91.9** | **-94.4** | **-97.0** | **n.a** | **n.a** | **n.a** |
| **Net financial assets; financial corporations** | **0.6** | **0.2** | **12.4** | **11.4** | **8.0** | **n.a** | **n.a** | **n.a** |
| Gross capital formation | 11.7 | 12.3 | 13.0 | 13.6 | 14.2 | 14.2 | 14.5 | 14.7 |
| Gross operating surplus | 17.9 | 17.8 | 17.2 | 17.6 | 17.4 | 17.1 | 18.0 | 17.4 |
| **Households and NPISH (% of GDP)** | | | | | | | | |
| **Net lending (+) or net borrowing (-)** | **2.7** | **3.1** | **3.3** | **2.6** | **2.6** | **2.5** | **2.9** | **2.7** |
| **Net financial assets** | **127.1** | **133.6** | **144.8** | **163.9** | **166.5** | **n.a** | **n.a** | **n.a** |
| Gross wages and salaries | 38.2 | 38.4 | 38.8 | 38.8 | 38.9 | 39.0 | 39.1 | 39.0 |
| Net property income | 4.3 | 4.7 | 4.1 | 3.5 | 3.5 | 3.6 | 3.5 | 3.4 |
| Current transfers received | 23.9 | 24.8 | 26.6 | 27.0 | 26.8 | 26.6 | 26.5 | 26.3 |
| Gross saving | 8.9 | 9.6 | 9.2 | 8.5 | 8.7 | 8.6 | 8.9 | 8.7 |
| **Rest of the world (% of GDP)** | | | | | | | | |
| **Net lending (+) or net borrowing (-)** | **1.0** | **-0.4** | **-1.0** | **-0.8** | **-0.6** | **-0.7** | **-0.6** | **-0.7** |
| **Net financial assets** | **-1.7** | **5.5** | **4.6** | **1.7** | **2.7** | **n.a** | **n.a** | **n.a** |
| Net exports of goods and services | 1.2 | -0.8 | -1.2 | -0.8 | -1.1 | -0.9 | -0.8 | -0.9 |
| Net primary income from the rest of the world | 1.5 | 2.2 | 2.3 | 2.1 | 2.5 | 2.5 | 2.4 | 2.4 |
| Net capital transactions | -0.1 | 0.0 | 0.0 | 0.0 | 0.1 | -0.1 | 0.0 | -0.1 |
| Tradable sector | 39.0 | 35.6 | 34.5 | 34.5 | 34.5 | 34.3 | n.a | n.a |
| Non tradable sector | 51.0 | 54.4 | 55.2 | 54.9 | 54.6 | 54.6 | n.a | n.a |
| *of which: Building and construction sector* | 4.6 | 5.5 | 5.2 | 4.9 | 4.9 | 4.9 | n.a | n.a |
| Real effective exchange rate (index, 2000=100) | 95.1 | 100.4 | 99.8 | 97.6 | 98.6 | 99.5 | 95.7 | 94.6 |
| Terms of trade goods and services (index, 2000=100) | 101.1 | 99.6 | 99.2 | 103.5 | 102.2 | 100.9 | 100.9 | 100.9 |
| Market performance of exports (index, 2000=100) | 112.1 | 101.4 | 104.3 | 101.2 | 100.9 | 101.3 | 101.3 | 100.9 |

Notes:

[1] The output gap constitutes the gap between the actual and potential gross domestic product at 2010 market prices.

[2] The indicator on domestic demand includes stocks.

[3] Unemployed persons are all persons who were not employed, had actively sought work and were ready to begin working immediately or within two weeks. The labour force is the total number of people employed and unemployed. The unemployment rate covers the age group 15-74.

*Source :*
*AMECO data, Commission 2019 spring forecast*

**Mandatory variables not included in the Stability Programme**

The Stability Programme did not provide non-calendar adjusted forecast for GDP components (non-calendar adjusted forecast for GDP is mentioned in a footnote). Unemployment rate forecast is also missing while the Stability Programme only provide forecast for IPC inflation, and not HICP inflation. No information is provided on investment expenditure fully matched by EU funds revenue nor on revenues increased mandated by law. Not included mandatory variables do not impede the Commission's ability to assess the Stability Programme on the basis of the Programme's assumptions.