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COMMISSION OPINION

of 18.11.2020

on the Draft Budgetary Plan of France

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(Only the French text is authentic)

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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 by 15 October, presenting the main aspects of the budgetary situation of the general government and its subsectors for the forthcoming year.

3. On 20 March 2020, the Commission adopted a Communication[1] on the activation of the general escape clause[2] of the Stability and Growth Pact. In its Communication, the Commission set out its view that, given the expected severe economic downturn resulting from the COVID-19 outbreak, the conditions to activate the general escape clause were met. On 23 March 2020, the Ministers of Finance of the Member States agreed with the assessment of the Commission.[3] As indicated in the Annual Sustainable Growth Strategy 2021[4] and as communicated in the letter of 19 September 2020 from the Commission to the EU Ministers of Finance[5], Member States should continue to provide targeted and temporary fiscal support in 2021 in a context where the general escape clause is activated, while safeguarding fiscal sustainability in the medium term.

4. On 27 May 2020, the Commission put forward its proposal for the creation of a new recovery instrument Next Generation EU[6], alongside the proposal for the reinforced long-term budget of the EU for 2021-2027.[7] This proposal includes the establishment of a Recovery and Resilience Facility offering large-scale financial support for both

[1] Communication from the Commission to the Council on the activation of the general escape clause of the Stability and Growth Pact, Brussels, 20.3.2020, COM(2020) 123 final.

[2] The clause, as set out in Articles 5(1), 6(3), 9(1) and 10(3) of Regulation (EC) 1466/97 and Articles 3(5) and 5(2) of Regulation (EC) 1467/97, facilitates the coordination of budgetary policies in times of severe economic downturn.

[3] https://www.consilium.europa.eu/en/press/press-releases/2020/03/23/statement-of-eu-ministers-of-finance-on-the-stability-and-growth-pact-in-light-of-the-covid-19-crisis/

[4] Communication from the Commission on Annual Sustainable Growth Strategy 2021, Brussels, 17.9.2020, COM(2020) 575 final.

[5] https://ec.europa.eu/info/business-economy-euro/economic-and-fiscal-policy-coordination/eu-economic-governance-monitoring-prevention-correction/stability-and-growth-pact/annual-draft-budgetary-plans-dbps-euro-area-countries/draft-budgetary-plans-2021_en

[6] Communication from the Commission to the European Parliament, the European Council, the Council, the European Economic and Social Committee and the Committee of the Regions - Europe's moment: Repair and Prepare for the Next Generation, Brussels, 27.5.2020, COM(2020) 456 final.

[7] Communication from the Commission to the European Parliament, the European Council, the Council, the European Economic and Social Committee and the Committee of the Regions - The EU budget powering the recovery plan for Europe, Brussels, 27.5.2020, COM(2020) 442 final.

public investments and reforms. By contributing to the economic recovery and by providing financial support to strengthen the economy's long-term growth, the Recovery and Resilience Facility will help public finances to return to more favourable positions in the near term and will contribute to strengthening their sustainability in the medium and long term.

CONSIDERATIONS CONCERNING FRANCE

5. On 15 October 2020, France submitted the Draft Budgetary Plan for 2021. On that basis, the Commission has adopted the following opinion in accordance with Article 7 of Regulation (EU) No 473/2013.

6. On 20 July 2020, the Council recommended France[8] to take all necessary measures, in line with the general escape clause, to effectively address the pandemic, sustain the economy and support the ensuing recovery. It also recommended France to pursue, when economic conditions allow, fiscal policies aimed at achieving prudent medium-term fiscal positions and ensuring debt sustainability, while enhancing investment.

   On 20 May 2020, the Commission issued a report under Article 126(3) TFEU, as France's general government deficit in 2020 was planned to exceed the 3% of GDP Treaty reference value and France did not make sufficient progress towards compliance with the debt reduction benchmark in 2019. The report concluded that the deficit criterion was not fulfilled and that the debt criterion was not complied with. In light of the exceptional uncertainty created by the outbreak of COVID-19 and its extraordinary macroeconomic and fiscal impact, including for designing a credible path for fiscal policy, which will have to remain supportive in 2021, the Commission considered that a decision on whether to place Member States under the Excessive Deficit Procedure should not be taken.

7. According to the Commission 2020 autumn forecast, the French economy is expected to contract by 9.4% in 2020 and grow by 5.8% in 2021. According to the Draft Budgetary Plan, the French economy is expected to contract by 10.0% in 2020, with all domestic demand components except public consumption being affected, and net exports making a negative contribution to growth. In 2021, the Draft Budgetary Plan projects the economy to rebound by 8.0%, supported in particular by private consumption and investment. Net exports' contribution to growth is expected to turn positive, whereas inventories are expected to weigh on growth. Employment is set to contract, strongly in 2020 and moderately in 2021. The recovery is projected to be uneven across sectors, with the manufacturing sector resuming activity more quickly than the services sector, especially transport and food and accommodation services, where restrictions are expected to remain in place for longer. This scenario differs somewhat from the Commission 2020 autumn forecast in that the Draft Budgetary Plan projects a deeper contraction in 2020, followed by a brisker rebound in 2021.[9] While in both sets of projections private consumption and investment are expected to lead the recovery in 2021, the Commission still projects a negative, though milder contribution of net exports to growth in 2021.

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[8] Council Recommendation of 20 July 2020 on the National Reform Programme of France and delivering a Council opinion on the 2020 Stability Programme of France, OJ C 282, 26.8.2020, p 62.

[9] The cut-off date of the Commission forecast was the 22nd of October. Since then, the first Insee estimate for the third quarter turned out to be significantly better than expected by the Commission, whereas the newly announced lockdown measures to contain the spread of the pandemic will weigh on the fourth quarter more strongly than foreseen in the Commission autumn forecast.

France complies with the requirement of Regulation EU No 473/2013 since the draft budget is based on independently-endorsed macroeconomic forecasts. In its endorsement of the forecasts, the High Council of Public Finances (Haut Conseil des Finances Publiques) nevertheless mentioned that the macroeconomic projections for 2021 are upbeat.

8. For 2020, the Draft Budgetary Plan foresees the general government deficit to rise to 10.2% of GDP. This increase in the government deficit by more than 7 percentage points compared to the preceding year results from both the working of automatic stabilisers, which has led to a contraction in revenues and to an increase of cyclical expenditure, and from the discretionary COVID-19-related measures by almost 3% of GDP. According to the 2021 Draft Budgetary Plan, the deficit is expected to narrow to 6.7% of GDP in 2021, helped by the rebound in activity and the reversal of discretionary COVID-19-related measures. These plans are broadly in line with Commission's projections for 2020, but appear to be more favourable for 2021. In particular, the Commission 2020 autumn forecast projects the general government deficit at 10.5% of GDP in 2020 and at 8.3% of GDP in 2021. The Draft Budgetary Plan assumes grants of 0.7% of GDP and expenditure of 1.1% of GDP under the Recovery and Resilience Facility. These are included in the revenue and expenditure projections.

For the time being, since the submission of the Recovery and Resilience Plans and their subsequent approval are expected to take place in 2021, the Commission forecast assumes in the budgetary projections for 2021 the 10% pre-financing of Recovery and Resilience Facility grants, and treats it as a financial transaction with no impact on the budget balance, but with a public debt-reducing impact. In the case of France, the 10% pre-financing of Recovery and Resilience Facility grants is equivalent to EUR 4 billion in 2021.[10] On the expenditure side, in line with its no-policy change assumption, the Commission forecast includes expenditure related to the French recovery plan (*France Relance*) of 1.1% of GDP that is sufficiently detailed and credibly announced.[11]

The Draft Budgetary Plan indicates that the government debt-to-GDP ratio will decline from 117.5% at the end of 2020 to 116.2% in 2021, whereas the Commission projects a different profile, with the government debt-to-GDP ratio rising from 115.9% in 2020 to 117.8% in 2021. As in other countries, the government has provided public guarantees to sustain economic activity and sectors particularly hit by the pandemic. Should these guarantees be called, this will be reflected in public debt and deficits in the future.

The Draft Budgetary Plan incorporates medium-term budgetary projections until 2025. According to them, the public deficit is projected to reduce gradually to 4.9%

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10 Indicative number based on the Council Presidency compromise proposal for the RRF Regulation (11538/20) of 7 October 2020, on which the Council Presidency obtained a mandate for conducting the negotiations with the European Parliament.

11 The treatment of the Recovery and Resilience Facility (RRF) in the Commission's 2020 autumn forecast is explained in detail in Box I.4.3 of the European Commission's Economic Forecast Autumn 2020 (*https://ec.europa.eu/info/sites/info/files/economy-finance/ip136_en.pdf*). In line with the customary no policy-change assumption, the forecast only incorporates those measures that are credibly announced and sufficiently detailed in the Draft Budgetary Plans, irrespective of whether they are planned to be part of the Recovery and Resilience Plans. No financing from the RRF has been included on the revenue side of the budgetary projections. Only the pre-financing of RRF grants is included in the forecast for 2021. The assumptions on expenditure measures linked to the RRF in the Commission forecast are without prejudice to the assessment of the Recovery and Resilience Plans.

of GDP in 2022, 4.0% in 2023, 3.4% in 2024 and to 2.9% of GDP in 2025. These projections are based on a constant structural annual adjustment of 0.5% of GDP each year from 2022 onwards. In turn, public debt is envisaged to peak at 117.8% of GDP in 2024 and to only start declining in 2025, to 117.4% of GDP.

9. The Draft Budgetary Plan reports discretionary fiscal measures with a direct budgetary impact in 2020 in response to the COVID-19 outbreak and its related economic effects of 2.9% of GDP.[12] These consist of expenditure-increasing measures totalling 2.6% of GDP and revenue-decreasing measures costing 0.3% of GDP. Expenditure measures in 2020 include the funding of a partial unemployment scheme, additional expenditure to strengthen healthcare services, health insurance allowances and compensation of healthcare personnel, the creation of a solidarity fund and other support measures to provide direct support to small enterprises as well as self-employed. On the revenue side, measures in 2020 include cancelations of social security contributions and advanced reimbursements of carry-back losses in corporate income tax. The Commission 2020 autumn forecast accounts for all the measures reported in the Draft Budgetary Plan with a direct impact on the deficit. Beyond these, the Draft Budgetary Plan also includes liquidity support measures in 2020 of around 3.3% of GDP, in the form of tax and social charges deferrals for companies, accelerated refunds of tax and VAT credits, and direct support to strategic companies via equity investments and loans. Moreover, the Draft Budgetary Plan includes public guarantees of 14.2% of GDP. Based on available information, the take-up of the guarantees as of October 2020 is estimated at 5.6% of GDP. Overall, the measures taken by France in 2020 were in line with the guidelines of the Commission Communication of 13 March 2020 on a coordinated economic response to the COVID-19 outbreak.

10. Following the adoption of new lockdown measures and enhanced fiscal support, the French government presented on 4 November 2020, after the submission of the Draft Budgetary Plan and the finalisation of the Commission Autumn forecast, the fourth amended Budget Law for 2020. This amendment considerably revises downwards the macroeconomic projections contained in the Draft Budgetary Plan and the fiscal targets for 2020. In particular, GDP is now set to contract by 11%. Likewise, the general government deficit is revised from 10.2% of GDP in the Draft Budgetary Plan to 11.3%, due to the expansion of the envelope of COVID-19-related measures by around 1% of GDP. In turn, public debt is now projected to reach 119.8% of GDP compared to 117.5% in the Draft Budgetary Plan.

11. For 2021, the Draft Budgetary Plan presents a set of new measures aimed at supporting the economic recovery and targeted at the sectors hardest hit by the consequences of the COVID-19 outbreak, amounting to 1.6% of GDP. These include expenditure measures estimated at 1.1% of GDP and revenue measures of 0.4% of GDP. All these measures cover three main areas. First, the support of employment, including the extension of the partial activity scheme, the promotion of apprenticeship contracts, study-work contracts, and training programmes, especially for the youth. Second, the improvement of French competitiveness, including the reduction of production taxes and the improvement of digitalisation levels across the country. Third, the support to the green transition, including a boost to building renovation and the reduction of industrial emissions. Liquidity support will also continue to be provided to hard-hit sectors. Sectors of immediate strategic

[12] This figure is net of EUR 4.1 billion savings in healthcare expenditure execution and of the EUR 1 billion special contribution from the supplementary health insurance providers.

importance such as the public health system also benefit from measures totalling 0.5% of GDP. At the same time, some measures set out in the Draft Budgetary Plan, while supporting economic activity against the background of considerable uncertainty, appear not to be temporary or matched by offsetting measures. According to the Commission forecast, while measures amounting to 0.9% of GDP are temporary, others estimated at 0.7% of GDP are assessed as not temporary or matched by offsetting measures. These include a permanent reduction in taxes on production (0.4% of GDP) and the increase of civil servant wages mainly in the healthcare system (0.3% of GDP).

12. The Commission is of the opinion that the Draft Budgetary Plan of France is overall in line with the recommendation adopted by the Council on 20 July 2020. Most of the measures set out in the Draft Budgetary Plan of France are supporting economic activity against the background of considerable uncertainty. However, some measures do not appear to be temporary or matched by offsetting measures. Given the level of France's government debt and high sustainability challenges in the medium term before the outbreak of the COVID-19 pandemic, it is important for France to ensure that, when taking supportive budgetary measures, fiscal sustainability in the medium term is preserved. France is invited to regularly review the use, effectiveness and adequacy of the support measures and stand ready to adapt them as necessary to changing circumstances.

It is anticipated that France will submit its Recovery and Resilience Plan in 2021. The Regulation establishing a Recovery and Resilience Facility will set out how the Commission is to assess that the reforms and investments included in the Recovery and Resilience Plan are coherent with the policy priorities of the Union and the challenges identified in the context of the European Semester. This assessment by the Commission will inform the approval of the Plan by the Council and the information to the European Parliament.

Done at Brussels,

For the Commission
Paolo GENTILONI
Member of the Commission