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FRANCE– REVIEW OF PROGRESS ON POLICY MEASURES RELEVANT FOR THE CORRECTION OF MACROECONOMIC IMBALANCES

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Executive summary

This is the fourth specific monitoring report under the Macroeconomic Imbalance Procedure (MIP) for France, which was identified as experiencing excessive imbalances in the 2016 European Semester. As pointed out by the 2016 Country Report, these imbalances are related to the large public debt and the deteriorated cost and non-cost competeiveness of the French economy. France being a large economy in the euro area, the vulnerabilities associated with its macroeconomic imbalances are of cross-border relevance. This report hence reviews the most recent developments in France's macroeconomic imbalances and the policy actions taken by the authorities to tackle them, as called for by the 2016 country-specific recommendations addressed to France. The cut-off date for this report is end-November 2016.

After three years of weak economic activity, GDP growth reached 1.3% in 2015. According to the Commission's 2016 autumn forecast, economic growth in France is projected to continue at a moderate pace at 1.3% in 2016 and 1.4% in 2017. The recovery in investment is expected to rebalance growth, making it less dependent on private consumption. However, net exports are set to remain a significant drag on growth. The substantial improvement in export performance in 2015 has proved short-lived and the current account, close to balance in 2015, is expected to deteriorate significantly over the coming years. Cost competitiveness is stabilising but has not yet regained past losses. The labour market shows signs of recovery with employment increasing strongly in the first half of the year, but remains segmented. The need for deleveraging is expected to remain contained for the private sector with the level of private debt stabilising around the threshold of the alert mechanism scoreboard.

Efforts to strengthen the budgetary strategy have remained modest. Public debt remains on an increasing path despite the gradual deficit reduction, highlighting the need for additional consolidation efforts in the next years to put the debt on a firm downward path. The budgetary strategy is largely nominalist and its success relies on the better-than-expected deficit outcomes in 2014 and 2015, the improving cyclical conditions and the low interest rates environment. At the same time, the ambition of the consolidation strategy on the expenditure side has been scaled down and tools to rein in spending growth such as spending reviews and public policy evaluations have only been marginally strengthened and have so far made only modest contributions to the streamlining and prioritisation of public expenditures.

The tax system remains complex. Corporate taxes on production and profits in 2017 will be reduced less than initially announced, while the Tax Credit for Competitiveness and Employment (CICE) will be increased from 6% to 7%. On the simplification side, the government only plans to introduce the withholding personal income tax reform as of 1 January 2018.

Despite reform efforts, the business environment continues to be characterised by a heavy regulatory burden. Although competition has improved in some services sectors, notably legal professions, retail trade and passenger transport services, barriers to activity persist in business services and regulated professions. Evaluations of innovation support schemes are not systematic and the innovation support system remains complex. Meanwhile, given the limited scope and temporary nature of some of the past measures and the absence of new initiatives, size-related regulatory thresholds will continue to weigh on firms' growth.

Action has been taken to improve cost competitiveness and to reduce the labour market segmentation. The Labour Act of 8 August 2016 paves the way for a comprehensive review of the Labour Code and is expected to have positive effects on the degree of segmentation of the labour market. Measures targeted at SMEs have also increased incentives to hire on longer-term contracts. Recent evaluations have shown the positive impact of the CICE on employment and firms' profit margins, while its effects on investment, R&D and exports are expected to materialise in the medium term. However, no details are available yet on its transformation into a permanent reduction of employers' social security contributions announced by 2018. While the recent minimum wage developments have been in line with productivity and average wage developments, they have not reduced the compression at the bottom of the wage scale. Steps have been taken to improve the vocational training system, but the education sector is not yet fully linked with labour market needs.

Overall, since February 2016, reform efforts have been pursued and progress has been achieved in certain policy areas, but further action is warranted. Actions were taken to improve the functioning of the labour market, to foster competition in a number of services sectors, and to reduce the regulatory burden of firms. Also, the introduction of the withholding personal income tax, planned for 2018, can help modernise the tax system. However, as regards public finances, the budgetary strategy does not guarantee a long-lasting correction of public finances, also because the spending reviews and public policy evaluations were not significantly reinforced. The taxation system continues to be characterised by high complexity and to be more focused on production than consumption. Concerning the labour market, no revision of the minimum wage indexation mechanism has been undertaken and the reform of the unemployment benefit system is still pending. Barriers to activity in business services and regulated professions persist and threshold effects in business regulations continue to hamper firms' growth.

Key findings on the implementation of economic policy reforms

On track	Wait-and-see	Action wanted
• reform of legal professions • collecting the personal income tax at the source • reform of the labour law • simplification of companies' administrative, fiscal and accounting rules under the simplification programme	• sustainability of the measures to reduce the cost of labour • reform of the vocational training system • reform of health professions • reform of passenger transport services (taxis, vehicles with a driver, rail transport) • simplifying and improving the efficiency of innovation policy schemes	• reinforcing the budgetary strategy • reinforcing the annual spending reviews • reinforcing the independent public policy evaluations • reform of the minimum wage indexation mechanism • reform of the unemployment benefit system • further removal of barriers to activity in business services and regulated professions • removing regulatory impediments to firms' growth • shifting the tax burden away from production to consumption • simplifying the tax system

Note: The table classifies reforms under review on the basis of their respective adoption and implementation process and their credibility and level of detail. "On track" are measures for which the legislative or implementation process has been completed or is progressing well according to the foreseen timeline, and which are expected to be sufficiently effective. "Wait and see" are measures for which the legislative process is on-going, but is still in a relatively early phase, or measures for which there is still uncertainty on the complete implementation and effectiveness. "Action wanted" are measures for which limited or no action has been taken, or measures that have been announced but which are not sufficiently detailed yet to be assessed.

1. Introduction

On 26 November 2015, the European Commission presented, in the context of the Macroeconomic Imbalances Procedure (MIP), its fifth Alert Mechanism Report to underpin the selection of Member States requiring an in-depth investigation into the existence and extent of macroeconomic imbalances. The subsequent Country Report on France – published on 26 February 2016 − examined the nature, origin and severity of macroeconomic imbalances and risks in France.[1] In its accompanying communication,[2] the Commission concluded that France was experiencing excessive macroeconomic imbalances. The high level of public debt, coupled with deteriorated productivity growth and competitiveness, constitute vulnerabilities, with cross-border relevance. Despite policy measures to reduce the labour tax wedge and a stepping-up of policy commitments, the Commission pointed to the need for an effective structural reform implementation regarding, in particular, the wage setting system, regulatory impediments to firms' growth, and the ambition of spending reviews.

On 13 May 2016, the Commission proposed a set of five country-specific recommendations (CSRs) for France, which were subsequently adopted by the Council on 12 July 2016. The CSRs stress the main policy gaps in France and propose policy actions that aim *inter alia* to ensure sound and sustainable public finances, to favour competitiveness and employment, to improve the business environment and to simplify the tax system. Moreover, the first recommendation which was addressed to all euro-area Member States[3] calls for the pursuing of policies that support the recovery, foster convergence, facilitate the correction of macroeconomic imbalances and improve the adjustment capacity.

This report presents the results of the specific monitoring by assessing the latest main policy measures taken by France since the publication of the 2016 Country Report. In order to underpin the findings of this document, a specific monitoring mission took place on 26-28 October 2016. The present report assesses the latest key policy initiatives[4] undertaken by the French authorities also in the light of the findings of the monitoring mission. The content of this document reflects the content of France's 2017 Draft Budgetary Plan, transmitted on 15 October, as well as the Commission's 2016 autumn forecast. In order to avoid an overlap of surveillance processes, this report does not provide an assessment of France's revised fiscal targets, as presented in the 2017 Draft Budgetary Plan (DBP) (submitted to the Commission in October 2016). The latter assessment can be found in the Commission's opinion on France's Draft Budgetary Plan,[5] taking into account the outcome of the Commission's 2016 autumn forecast. The report includes information up to end-November.

[1] European Commission (2016), Country Report, France 2016 – Including an In-Depth Review on the prevention and correction of macroeconomic imbalances, http://ec.europa.eu/europe2020/pdf/csr2016/cr2016_france_en.pdf

[2] 2016 European Semester: Assessment of progress on structural reforms, prevention and correction of macroeconomic imbalances, and results of in-depth reviews under Regulation (EU) No 1176/2011. COM(2016) 95 final/2, http://ec.europa.eu/europe2020/pdf/csr2016/cr2016_comm_en.pdf.

[3] http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32016H0311(01)&rid=2

[4] Details on the policy measures can be found in the overview table in the Annex.

[5] See Commission Staff Working Document on the 2017 DBP, http://ec.europa.eu/economy_finance/economic_governance/sgp/pdf/dbp/2016/fr_2016-11-16_swd_en.pdf.

2. Outlook and recent developments on imbalances

Recent economic developments and outlook

After three years of weak economic activity in France, GDP growth reached 1.3% in 2015 supported by favourable external factors, in particular reduced oil prices and the euro's depreciation. Following strong growth in the first quarter of 2016, economic activity contracted slightly in the second quarter due to several temporary factors and grew modestly by 0.2% in the third quarter. Overall, growth continued to be primarily driven by private consumption and investment. Since the 2016 Country Report, growth prospects have somewhat weakened, especially for 2017, given the weaker external outlook, an environment of increased uncertainty as well as new consolidation measures included in the 2017 draft budget. The new scenario for the economic outlook is one of a continuation of moderate growth in which a recovery of investment is set to rebalance growth, making it less dependent on private consumption. However, net exports are set to remain a significant drag on growth. According to the Commission's 2016 autumn forecast, French GDP is projected to grow by 1.3% in 2016, 1.4% in 2017 and 1.7% in 2018. Inflation has started to recover and is expected to average 0.3% in 2016 before picking up substantially to 1.3% in 2017 and to 1.4% in 2018 on the back of increasing oil prices and pressures from rising wages. The labour market shows signs of recovery with employment increasing strongly in the first half of the year. Over the forecast horizon, the unemployment rate is set to decline continuously to 9.6% in 2018 supported by economic growth and by policy measures aimed at encouraging job creation (the Tax Credit for Competitiveness and Employment, the Responsibility and Solidarity Pact, and the Hiring Subsidy).

The general government deficit is expected to decrease to 3.3% of GDP in 2016 and is projected to decrease further to 2.9% of GDP in 2017. At unchanged policy the deficit is projected to increase to 3.1% of GDP in 2018. The structural balance is projected to improve by only 0.1% of GDP in 2016 and by 0.2% of GDP in 2017 suggesting an overall slow pace of fiscal adjustment. General government debt stood at 96.2% of GDP in 2015 versus a euro area average of 92.6% and is expected to increase further to 97.1% of GDP in 2018.

Developments as regards imbalances

In March 2016 France was found to be experiencing excessive macroeconomic imbalances (see Section 1). These imbalances related to a deteriorated competitiveness and a high and increasing public debt, in a context of low inflation and productivity growth. While competitiveness showed some signs of stabilisation in 2015, the latest developments point to a renewed deterioration in export performance in 2016. As already described above, the general government debt is projected to increase, albeit at a relatively slow pace, suggesting that the slow pace of public deleveraging is continuing.

<u>Competitiveness</u>

Export performance improved substantially in 2015, supported by the euro's depreciation as well as the exceptional performance of certain sectors. In the first three quarters of 2016, however, exports stalled in part due to delivery delays in the aircraft sector and in a context of weaker world trade. For 2016 as a whole, exports are forecast to fall short of the expected export market growth leading to a deterioration of export performance.

The prospects for current account developments have significantly deteriorated since the 2016 Country Report. The current account was close to balance in 2015 (-0.2% of GDP) thanks to oil price and exchange rate developments, but the latest available data point to a strong deterioration in 2016 (-1.1% of GDP over the first nine months). In the medium term, the current account balance is expected to further deteriorate, as imports remain more dynamic than exports and as oil prices rebound.

The recent improvement in cost competitiveness remains insufficient to regain past losses. Wage moderation continues, but ULC developments remain inflated by low productivity growth. In 2015, unit labour costs increased by 2.5% over three years, and 0.9% once the Tax Credit for Competitiveness and Employment (CICE) is taken into account, less than in the rest of the euro area (2.1%). Productivity picked up slightly, but remained below both long-term trends and the euro area average. A part of the decline in productivity growth, however, can be explained by the measures aimed at boosting employment growth.

Substantial improvements in non-cost competitiveness are not yet visible. Non-financial corporate profit margins have somewhat recovered since 2013, but remain below their pre-crisis level.

Public and private debt

While public debt dynamics do not improve, the other internal sector indicators are gradually improving. Financial sector liabilities are slowly declining, private sector credit has stabilized at moderate positive levels and real house prices are slowly correcting. Some deterioration is noted when it comes to the private sector debt indicator which reached 145% of GDP in 2015, just above the threshold of the alert mechanism scoreboard, although its growth rate has stabilized and its level is even projected to start declining in 2016. The debt-to-GDP ratio is projected to increase further and reach 97.1% in 2018 implying a growing divergence in indebtedness vis-à-vis the euro area.

The structure of public debt financing in terms of maturity and diversity of the investor base does not give rise to short-term risks. The rating outlook for French government debt is since recently AA stable for the three major rating agencies. The average maturity of debt issued has increased to nearly 7.5 years which reduces the refinancing risks related to an increase in short-term rates. Holdings by foreign investors have slightly declined to 60% of total French debt, but investor appetite is still high as French debt is an investment sought for capital and liquidity requirement reasons and diversification purposes.

Although the French public debt is not among the highest in the euro area and its growth rate has decelerated more recently, it remains a major vulnerability, especially if seen in combination with the high private sector debt, the slow adjustment pace of the deficit and taking into account the current context of still weak (potential) growth and low inflation. Indeed, France's debt burden may give rise to negative feedback loops to the real economy and the financial sector should a new macro-economic shock materialise and could translate into negative spillover effects for the rest of the euro area.

Adjustment issues: unemployment

The employment rate of the population aged 20-64 years old increased to 69.5% in 2015. Also, the unemployment rate decreased to 10.0% in the third quarter of 2016, after 10.4% in 2015 as a whole. This decrease was due both to a stronger-than-expected employment growth and to an unexpected slight decrease in the activity rate, related to the emergency plan for employment which has shifted some unemployed persons out of the labour force into training (see Section 3.3). However, the long-term unemployment rate continued to increase (at 4.3% in 2015 against 3.7% in 2012).[6] The labour market segmentation remains high, with a stable share of very short-term contracts (*i.e.* contracts lasting for less than a month) − at 69.2% of total hires in the first three quarters of 2016 − and significantly low transition rates to open-ended contracts. The unemployment rate remained higher in the second quarter of 2016 for more vulnerable groups, being at 17.4% for workers having less than a lower secondary education diploma and at 19.7% for unemployed workers having a migrant background.

3. Policy implementation and assessment

3.1 Improving public finances and taxation

This section reviews the latest developments in the budgetary strategy, the fiscal framework and taxation in the light of the country-specific recommendations (CSRs) addressed to France on 12 July 2016. Specifically, France was recommended to step up efforts to increase the amount of savings generated by the spending reviews and to reinforce the independent public policy evaluations. Moreover, the Council recommended France to reduce the taxes on production and the corporate income statutory rate while broadening the tax base on consumption, to remove inefficient tax expenditures and taxes that are yielding little or no revenue and to adopt the withholding personal income tax reform by the end of 2016.

The Commission's assessment is that the 2017 Draft Budgetary Plan is broadly compliant with the provisions of the Stability and Growth Pact, as the headline deficit target is projected to be met, although the fiscal effort is expected to fall significantly short of the recommended level. On November 16, the Commission adopted its opinion on the 2017 Draft Budgetary Plan (DBP) assessing compliance with the Stability and Growth Pact (SGP) and with the Council Recommendation of 10 March 2015 to correct the excessive deficit. Overall, the Commission is of the opinion that the 2017 DBP is broadly compliant with the provisions of the SGP, as the Commission's 2016 autumn forecast projects that the deficit will be slightly below the threshold value of 3% of GDP in 2017, although the correction would not be durable in 2018 under a no policy change scenario.

There is no specific mechanism in place to reconcile divergent views between the High Council of Public Finance and the Ministry of Finance. Since the creation, by the organic law of 17 December 2012, of the High Council for Public Finances (HCFP) as an independent fiscal body mandated to provide an endorsement of the government's macroeconomic forecast underpinning the draft budget, the risk of overoptimistic macroeconomic forecasts has receded. On 24 September 2016, the HCFP issued a more critical opinion on the macroeconomic scenario underpinning the 2017 DBP than in previous years.[7] However, there is no specific mechanism in place in the French legislation and practice to reconcile divergent views of the independent body and the Ministry of Finance on the main variables of the

[6] The AMR 2017 introduced three new employment indicators in the MIP scoreboard, notably the 3-year percentage change in the activity rate, in the youth unemployment rate, and in the long-term unemployment rate.
[7] Haut Conseil des finances publiques (2016), Avis n°2016-3 relatif aux projets de lois de finances et de financement de la sécurité sociale pour l’année 2017, 24 Septembre 2016.

macroeconomic forecast underpinning the DBP, which points to a shortcoming in the fiscal framework.

The budgetary strategy as reflected in the 2017 DBP is more revenue-oriented than in previous years. Compared to the April 2016 Stability Programme and the National Reform Programme, the last tranche of the Responsibility and Solidarity Pact (RSP) has been replaced by a reinforcement of tax credits in 2017 and corporate tax cuts in 2018. This would translate into 0.2% of GDP additional revenues in 2017 and an equivalent increase of expenditure in 2018.[8] For 2017, the last phase of the RSP had planned the abolition of the Companies Social Solidarity Contribution (C3S), a tax on turnover, and a reduction in corporate income taxes. Other consolidation measures consist in the upward revision of the yield of certain measures or dividends and the inclusion of a number of non-recurring revenue measures, such as changes in the payment modalities of some taxes (see Commission Staff Working Document Analysis of the 2017 DBP of France, Section 3.3).[9] Overall, the quality of the consolidation on the revenue side can be questioned as it shifts the cost of some measures to 2018, relies on the upward revision of the yield of certain measures decided previously and on non-recurring revenue measures.

On the expenditure side, the consolidation measures in the 2017 DBP have been scaled down compared to the April 2016 Stability Programme and some tools to keep expenditure growth in check have been relaxed or abandoned. The savings package of EUR 50 bn (2.2% of GDP) over 2015-2017 will not be fully realized as the amount of savings has been sharply reduced to EUR 40.5 bn (1.8% of GDP) in the 2017 DBP. At the same time, the norms and tools that have allowed the authorities to keep in check expenditure growth until 2016 have been relaxed: the civil servants' wage freeze was discontinued in 2016; in the 2017 DBP the spending norm for the State and the healthcare spending norm (ONDAM) have been increased while the cut in transfers from the State to local authorities has been reduced compared to the Stability Programme. Overall, the DBP includes EUR 9 bn new deficit-increasing measures for 2017. Moreover, as flagged by the High Council for Public Finances,[10] the risks to the achievement of expenditure growth targets in 2017 are higher than in previous years, notably due to the unrealistic nature of the planned savings on the unemployment benefit scheme, to the large scale savings planned on the ONDAM and to the evolution of spending by the State and local authorities.

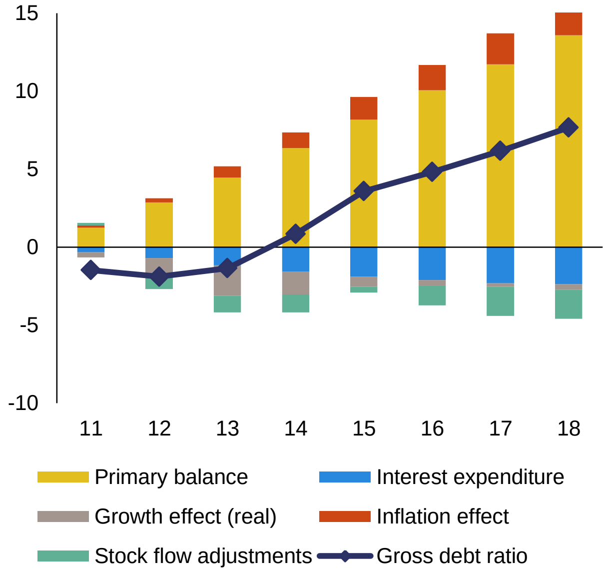
Debt dynamics between France and the rest of the euro area continue to diverge although the increase in French debt is decelerating. According to the Commission's 2016 autumn forecast, the general government debt in France is projected to reach 97.1% of GDP in 2018 under a no-policy change assumption, i.e. about 8 pp above the level in the rest of the euro area. The slower deficit reduction in France explains most of this difference, while real economic growth, interest expenditure and stock-flow adjustments have partly compensated for the higher primary deficits in recent years. Since 2011, the lower interest expenditure has had a significant contribution to the deficit and debt reduction (Figure 1). However, this trend is expected to reverse once interest rates and inflation normalize. Therefore there is scope for strengthening the consolidation strategy as it currently relies on elements outside the control

[8] The ESA 2010 accounting treatment of tax credits delays their budgetary impact by one year
[9] See Commission Staff Working Document on the 2017 DBP, Section 3.3, http://ec.europa.eu/economy_finance/economic_governance/sgp/pdf/dbp/2016/fr_2016-11-16_swd_en.pdf.
[10] Haut Conseil des finances publiques (2016), *ibidem*.

of the authorities such as the benign economic environment and the persistently low interest rates.

The spending review process was scaled back in 2016 and still does not foresee a mechanism to ensure that the savings and recommendations identified in the spending review are translated into actions, especially at the local government level. The first wave of spending reviews in 2015 had identified EUR 453 mn potential savings and had led to a final amount of EUR 325 mn. The second wave of spending reviews included in the 2017 DBP has not identified new savings but has announced that measures of the first round of spending reviews − on housing allowances, medical devices and the dematerialization of the electoral material − would continue to yield additional savings of EUR 400 mn in 2017. One explanation for the lower amount of savings in 2017 could be linked to the nature of the second wave of spending reviews, of which more than 50% concerned spending by local governments, autonomous by Constitution in managing their budgets. Also, the spending reviews of the second wave were only ready starting from end-June onwards which is relatively late to include them in the 2017 DBP. While the publication of the first wave of spending reviews in April 2016 increased transparency, the planned improvement of the process, namely the *ex-ante* specification of a savings target as foreseen at the launch of the 2016 spending review, did not take place. The 2018 spending review is foreseen to cover 13 new expenditure areas targeting mainly spending by local authorities. This casts doubt on the potential for improving and reinforcing this third wave of spending reviews.

Figure 1: Difference in debt dynamics between France and the euro area (% of GDP)



Source: European Commission, 2016 autumn forecast

Local governments are expected to contribute further to the consolidation effort in 2017, but the underlying savings have not been specified in the DBP. The consolidation effort of local authorities has been driven by the cut in transfers from the State (EUR 6.8 bn in 2015 and 2016 cumulatively). The cut in transfers has led to a reinforcement of the traditional local investment cycle culminating in a decrease in local investment by -10.2% in 2015. At the same time, the cut in transfers has also translated into lower growth of operational spending in 2015 (+2.1%) which is projected to decline further on the basis of in-year execution data and low hiring intentions at local level.[11] Also, the *Note de conjoncture*[12] published by La Banque Postale confirms that efforts on operational expenditure will be pursued, but adds that it would require taking structural measures. In this regard, the indicative expenditure norm for local authorities (ODEDEL) should facilitate keeping track of the evolution of expenditure at this administrative level, although no correction mechanism or alert committee such as the one existing for the expenditure norm for healthcare (ONDAM) is foreseen in case of expenditure overruns. Compared with the ONDAM, there are also considerably more actions involved and the financial autonomy of the local authorities is larger which makes it more difficult to enforce the ODEDEL.

The rollout of the local government reform is being pursued. The new inter-municipal agreements will be implemented in 2017 and the transfer of competencies (i.e. non-urban and school transport transferred from departments to regions, transfer of powers from departments to new metropolitan areas from 2017 on) will be pursued as foreseen in the Local Administration Reform Act (NOTRe) of 7 August 2015. However, the implementation of the territorial reform over 2016-2020 could increase spending in the short run and would lead to efficiency gains only in the longer term, notably through spending rationalization and mutualisation of services. A new development is the creation on 18 October 2016 of the O*bservatoire des finances et de la gestion publique locales* introduced by the law NOTRe to replace the former *Observatoire des finances locales*. The missions of this new body would be to analyse and to disseminate data and statistics relative to local authorities in order to promote best practices and to evaluate local public policies. It is not clear at this stage how this observatory would interact with the *Secrétariat Général de la modernisation de l'action publique* (SGMAP) which also covers local authorities.

A meta-evaluation to measure the quality and impact of the public policy evaluations is ongoing. The public policy evaluation process started in 2012 is ongoing with 68 assessments out of 80 launched being already completed as of September 2016. The 59 such evaluations launched between 2013 and 2014 have generated limited savings, amounting to 0.3% of GDP according to the authorities. The public policy evaluations do not have an *ex-ante* savings objective and have often led to recommendations of a qualitative nature. Moreover, no mechanism exists to ensure that the recommendations are implemented, in particular when the policy is shared by different administrations (often the State and local authorities). A positive development in this area is the launch by the SGMAP of a meta-evaluation (evaluation of evaluations) which was delegated to third parties. Its objectives are to measure the quality of the evaluation process currently used by SGMAP and to assess the impact of the public policy evaluations that have already been completed. It is expected that the results of this evaluation will be made public at the end of 2016.

Corporate taxation will be further cut in 2017, with somewhat reduced numbers as compared to earlier announcements. The *Rapport Economique, Social et Financier* (RESF) accompanying the 2017 DBP provides for EUR 39.5 bn tax cuts in favour of companies in 2017, which represents a reduction of EUR 1.5 bn of the figure announced for the same year in last year's RESF. This can be partly explained by the authorities' choice to strengthen the Tax Credit for Competitiveness and Employment (CICE) in 2017, which will only have a budgetary effects in 2018 (see Section 3.3 for further details), but to abandon the phase-out of

[11] Randstad (2016), *Baromètre Ressources Humaines des collectivités locales 2016. Les collectivités toujours plus nombreuses à envisager une réduction de leurs effectifs*.
[12] La Banque Postale (2016), *Note de conjoncture, Les finances locales*, November.

the last tranche of the turnover tax (*C3S*) for the 20 000 businesses still liable to it (which would have reduced the corporate tax burden by EUR 3.5 bn in 2017).

Furthermore, measures aimed at reducing the corporate tax bill are being refocused on SMEs. In addition to the non-phasing out of the last tranche of the C3S which now weighs exclusively on larger companies, the reduction in the corporate income tax statutory rate will benefit SMEs in 2017, for an amount of EUR 330 mn. As of 2017, all SMEs will immediately benefit from a rate of 28% up to EUR 75 000 of profits (while the reduced rate of 15% remains unchanged). Up to the EUR 38 120 profit ceiling, the reduced rate of 15% will continue to apply, making the 28% an additional, intermediary rate. The 2017 DBP then includes a roadmap to gradually reduce to 28% the statutory rate of the tax on corporate profits by 2020.

The tax base on consumption has not been broadened. The 2017 DBP does not introduce any proposal in this respect, leaving inefficient VAT reduced rates and exemptions untouched.

Efforts to simplify the tax system are mixed. The income tax system will be modernised through the introduction of the withholding personal income tax reform (*prélèvement à la source*) which will be implemented as of 2018 if adopted by Parliament. However, little has been done to streamline the tax system. The scrapping of taxes yielding little or no revenue continues to progress at a slow pace. The 2017 DBP plans the suppression of two further taxes out of the 192 identified by the General Inspection of Finances in 2014, keeping the pace of 2016 unchanged. Tax expenditures keep increasing in number and in value, and are set to reach EUR 89.9 bn in 2017 (up from EUR 85.9 bn in 2016), exceeding the maximum of EUR 86 bn set for 2017 in the 2014-2019 multiannual budgetary framework. The higher-than-previously forecast cost of the CICE in 2017 and the increase in tax expenditures linked to environmental taxation can only account for 1.1 bn of the increase on 2016. Indeed, the 2017 DBP provides for a net creation of 5 tax expenditures (14 new ones will be introduced, while only 4 are to be suppressed and 5 to come to an end).

In conclusion, since February 2016 some reform efforts have been made in the areas of public finances and taxation. Efforts to reduce the headline deficit are being pursued in line with the EDP recommendation but the ambition of the consolidation strategy on the expenditure side has been scaled down compared to the latest Stability Programme and the structural effort is well below what is needed to reduce the high debt burden. The second wave of spending reviews included in the 2017 DBP has not identified new savings compared to the first round, although the process is now embedded in the budgetary process. In the area of public policy evaluations, a meta evaluation of the public policy evaluations conducted since 2012 is ongoing, reflecting the increased awareness that the process could be improved. The main initiative taken to simplify the tax system is the planned introduction of the withholding personal income tax reform as of 1 January 2018, while the reductions in corporate taxes on production and profits foreseen in the 2017 DBP are more limited than previously announced.

3.2 Measures to support the business environment and innovation

This section describes policy measures to improve the business environment in France in line with the related country-specific recommendation (CSR 4). This recommendation notably calls for further actions to remove barriers to activity in the services sector, in particular in business services and regulated professions and to simplify and improve the efficiency of innovation policy schemes. France is also invited to further reform by the end of 2016 the size-related criteria in regulations that impede companies' growth and to continue to simplify companies' administrative, fiscal and accounting rules by pursuing the simplification programme.

Recent reform efforts have helped increase competition in a number of services sectors. The Macron law[13] of 6 August 2015, affecting in particular legal professions, retail trade and passenger transport services, is almost fully implemented. Out of the 116 measures that required an implementation decree, 108 measures (93%) were already in effect on 23 October 2016. As regards legal professions, four decrees were adopted on 29 June 2016 easing practice requirements for a number of them, including lawyers, notaries, bailiffs and court-appointed auctioneers, while on 16 September two additional decrees further eased establishment requirements for notaries by identifying 247 free set-up areas (out of a total 307 areas in France). Ownership rules for certain legal and accounting professions, architects and surveyors were also relaxed through the decrees of 29 June and 1 July 2016. Decrees of the Macron law, which are still pending publication, relate *inter alia* to the financing of railway infrastructure and to the reform of Labour Courts (*justice prud'homale*). Furthermore, 21 ordinances have been adopted and two are still pending issuance. Yet, the scope of the Macron law remains limited and its effectiveness in some areas may be hindered by other factors. For instance, although the establishment of free zones could allow for the setting up of 1 650 additional notaries during the next two years, the application process is strictly framed by several rules that render the process rather complex.[14]

Access to professions and services in the healthcare sector is not optimal. While the Healthcare law of 26 January 2016 allowed *inter alia* for an extension of the remit of certain professions which are restricted by the law (such as midwives, and medical and dental assistants), it extended reserved activities for others (such as orthoptists and opticians).[15] The regulatory framework for home-care services was also reformed through the law of 28 December 2015 on Ageing Society.[16] Yet, the role of local authorities will be crucial to ensure full implementation of the new common regime in order to prevent any discrimination between existing and newly-authorised providers. Finally, there are currently no government plans to revise the quotas on medical students (*numerus clausus*) in a way that would adequately address future needs, although their levels have been increased somewhat.

A number of passenger transport services are currently being reformed, but not rail services. The Macron law has opened to competition long-distance domestic coach services, which, together with car-sharing services, has increased the offer of transport services in France. A reform affecting the sectors of taxis and vehicles with a driver is also under discussion and is expected to be adopted in autumn.[17] In line with the French authorities' will to define rules for intermediaries and active providers in the collaborative economy, this reform aims to review the regulatory framework of taxis and vehicles with drivers and to generalise the use of digital platforms, which is currently favouring the latter. Nevertheless, the impact of this law will depend on its final design and implementation. France does not

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[13] *Loi pour la croissance, l'activité et l'égalité des chances économiques*

[14] For example, a lottery procedure is envisaged in case the number of applications exceeds the number of available places and there is no possibility to put an order of preference on the zones that candidates apply for.

[15] *Loi de modernisation du système de santé*

[16] *Loi relative à l'adaptation de la société au vieillissement*

[17] *Loi relative à la régulation, à la responsabilisation et à la simplification dans le secteur du transport public particulier de personnes (Loi Grandguillaume)*

envisage liberalising regional passenger rail transport before the deadline set by the fourth European railway package (end-2023 at the earliest). However, the government and the association of French regions have agreed on setting up a legal framework to allow regions to introduce competition in passenger rail transport on an experimental basis.

Despite these reform efforts, barriers to activity remain in the services sector, in particular in business services and regulated professions. As regards business services, despite recent reforms, a number of regulatory barriers to activity remain in place, including the restrictive application of authorisation requirements and the compulsory membership of chambers (e.g. in the case of architects), although deontology codes are now supervised by the Competition Authority. Concerning the crafts sector, the initial version of the Sapin II law intended to ease some qualification requirements, but most of these provisions were withdrawn during the parliamentary process.[18]

Some preliminary steps are being taken to rationalise the innovation support system, but a lot remains to be done. The first report of the National Commission on Assessment of Innovation Policies[19] (CNEPI) sheds light on the complexity of the innovation support system and calls for stepping up evaluation efforts. Evaluations of several individual schemes are ongoing, but their scope is somewhat limited. While the tax credit for research (CIR), the largest state-financed innovation support scheme, is subject to several ongoing studies,[20] other smaller schemes have not been evaluated yet. Some recommendations of the mid-term stock-taking report of the Investment for the Future programme (*Programme d'Investissements d'Avenir*) have been taken on board in the third phase of the Programme, launched in June 2016. In particular, repayable advances to companies will be replaced by equity financing, including in risky projects. Finally, the Court of Auditors has identified some design weaknesses of the competitiveness clusters (*pôles de compétitivité*), but it is unclear how exactly the authorities plan to implement the recommendations included in the Court's report. A reform should be announced before the end of the year.

Limited action has been taken to soften the impact of size-related requirements on firms' growth. Some initiatives have been taken in recent years (2015 Social Dialogue law, 2016 budget law), but their impact is hampered by their limited scope, and the temporary nature of some measures. More recently, the Sapin II law provides for a streamlining of the different legal forms of firms by making it easier to switch from the 'sole trader'[21] status to another status, notably the 'limited liability sole proprietorship'[22] status or the 'single-member private company'[23] status. Although these measures could facilitate the transition of small businesses to a status that is more adapted to recruiting employees, the overall legal framework governing businesses in France continues to be rather complex. In the same vein, the Sapin II law attempted to offer the possibility to auto-entrepreneurs crossing certain turnover-related thresholds to keep a simplified tax regime, but this provision was withdrawn during the

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[18] *Loi relative à la transparence, à la lutte contre la corruption et à la modernisation de la vie économique*

[19] Commission Nationale d'évaluation des politiques d'innovation (2016), *Quinze ans de politiques d'innovation en France*, January.

[20] France Stratégie has launched a tender for a study on the CIR, and the Research Ministry publishes a yearly evaluation report. The last edition was published earlier this year: Ministère de l'Education nationale, de l'Enseignement supérieure et de la Recherche (2016), *Le crédit d'impôt recherche en 2013*, April.

[21] A sole trader is a type of business entity that is owned and run by one natural person and in which there is no legal distinction between the owner and the business.

[22] Limited liability implies that a person's financial liability is limited to a fixed sum, most commonly the value of a person's investment in a company or partnership.

[23] A single member company is a private limited company where one single person holds the entire share capital issued.

legislative process. As there are currently no plans to review and permanently reform where needed size-related criteria in business regulations, threshold effects will continue to weigh on firms' growth.

Some effort is being made to simplify firms' administrative, fiscal and accounting rules. A new batch of 49 measures was announced on 24 October 2016 under the so-called simplification programme (*'choc de simplification'*), bringing the total number of business-oriented measures to 415 with an expected annual benefit of around EUR 5 bn for firms. The implementation of the *Declaration Sociale Nominative* (that would represent 3 bn EUR of annual benefits for firms) is expected to be operational early 2017. Elsewhere, the programme is progressing as planned, although implementation is uneven with 262 measures affecting firms (63%) currently in effect. With a view to facilitating business creation, the Sapin II law of 8 November 2016 also eased training requirements prior to starting a business and removed the requirement for micro-entrepreneurs to open a second bank account at least during the first year of business.

Overall, despite the aforementioned reform efforts, the business environment in France continues to be characterized by a heavy regulatory burden. [24] Some 89% of the French SMEs responding to a 2016 Commission Survey found that the complexity of administrative procedures is a problem for doing business in France (EU average: 62%).[25] There is also scope to further increase competition in the services sector which could translate into productivity and competitiveness gains for the whole economy. Tax reforms and improvements in public innovation policies could amplify these effects. Meanwhile, France needs to address threshold effects on a permanent basis by reviewing and reforming where needed size-related criteria in business regulations. Last but not least, simplification efforts are pursued but they have not improved yet the perception of business actors in France.

3.3 Labour cost and labour market

This section describes policy measures to improve the cost competitiveness of firms and the functioning of labour market in France, as called for by the related country-specific recommendations (CSRs 2 and 3). In particular, these recommendations urge the authorities to sustain the policies to reduce the cost of labour, ensure that minimum wage developments are consistent with job creation and competitiveness, reform the labour law to provide employers with more incentives to hire on open-ended contracts, and reform the unemployment benefit system in order to ensure its budgetary sustainability while providing more incentives to return to work.

Studies using firm-level data for the period 2013-2014 have pointed to the positive effect of the *'crédit d'impôt pour la compétitivité et l'emploi'* (CICE) on profit margins and employment, while the effects on investment, R&D and exports are expected to take time to materialise. Three groups of researchers have analysed firm-level data for the period 2013-2014 (see box below for further details) in the context of the annual evaluation of the impact of the CICE. In brief, the CICE is found to have a positive impact on employment and firms' profit margins. The CICE has instead had no impact on average wages, while some impact on wages was found by one team of researchers within certain firms. Moreover, no effect on

[24] 2017 World Bank Doing Business Report, 2016-2017 Global Competitiveness Report, 2016 European Commission Small Business Act.

[25] 2016 European Commission Small Business Act Fact Sheet on France, http://ec.europa.eu/growth/smes/business-friendly-environment/performance-review_en#sba-fact-sheets.

investment, R&D and exports has been found yet given the too short time horizon for which firm-level are available at the moment.

Box: New assessments of the impact of the *crédit d'impôt pour la compétitivité et l'emploi* using firm-level data

Three studies using firm-level data have assessed the effect of the '*crédit d'impôt pour la compétitivité et l'emploi*' (CICE) on firms' behaviour over the period 2013-2014. In September 2016, the first evaluations of the *crédit d'impôt pour la compétitivité et l'emploi* (CICE) based on firm-level data for the period 2013-2014 were published.[26] The studies were conducted by the *Observatoire français des conjonctures économiques* (OFCE), the Laboratory for Interdisciplinary Evaluation of Public Policies (LIEPP) and the *Fédération de Recherche CNRS Travail Emploi et Politiques Publiques* (TEPP). The results of these evaluations are summarised in the 2016 report of the *Comité de suivi du crédit d'impôt pour la compétitivité et l'emploi*.[27] While the OFCE study assesses only the effects of the CICE on exports through a calibrated theoretical model, the other two studies empirically assess the effects of the CICE on wages, employment, firms' profit margins, exports and investments.

These studies find a positive impact of the CICE on employment and firms' profit margins, while the effects on investment, R&D and exports are expected to take time to materialise. First, the LIEPP and TEPP studies have found that firms have used an important part of the CICE to rebuild their profit margins. However, this increase in firms' profit margins has not yet translated into any significant effect on investment, exports or R&D expenditures because these effects will take time to materialise, as also pointed out by the OFCE study. Second, the two studies have found some effects of the CICE on wages and employment, although with some diverging results. On the one hand, the TEPP study found that the CICE allowed creating or maintaining between 45 000 and 115 000 jobs. This effect on employment did not increase with time, as firms being more exposed to the CICE showed no additional impact of the CICE on employment in 2014, when the CICE rate was increased from 4% to 6%. In addition, the TEPP study found no effect of the CICE on wages. By contrast, the LIEPP study found no positive effect of the CICE either on employment or wages per capita, while a positive effect was found on hourly wages. The difference between the two studies as regards the effect of the CICE on employment disappears when the assessment is based on an econometric model specified in the same way. By contrast, the difference between the two studies as regards wages could not be reconciled, as the TEPP study referred globally to the impact of the CICE on the evolution of the average wage, while the LIEPP study evaluated the evolution of wages within firms, pointing to the fact that some firms used the CICE to increase wages.

The transformation of the CICE into a reduction in employers' social security contributions by 2018, as announced in the 2016 NRP, could lead to a simplification of

[26] Gilles, F., Bunel, M., L'Horty, Y., Mihoubi, F. and X. Yang (2016), "*Les effets du CICE sur l'emploi, les salaires et la R&D: une évaluation ex post*," TEPP Rapport de Recherche, No 2016-09, September 2016. Carbonnier, C., Malgouyres, C. and G. Rot (2016), "*Evaluer les impacts du crédit d'impôt pour la compétitivité et l'emploi*," LIEPP Policy Brief No 27, September 2016. Guillou, S., Sampognaro, R., Treibich, T. and L. Nesta (2016), "*L'impact du CICE sur la marge intensive des exportateurs*," Rapport d'évaluation pour France Stratégie, OFCE, 26 Septembre 2016.

[27] Comité de suivi du crédit d'impôt pour la compétitivité et l'emploi (2016), "*Rapport 2016 du Comité de suivi du crédit d'impôt pour la compétitivité et l'emploi*," France Stratégie.

the existing set of measures to reduce the cost of labour. The CICE credit rate has been increased from 6% to 7% in the 2017 DBP, while its transformation into a reduction in employers' social security contributions is foreseen by 2018 according to the latest NRP. This measure could take into account the outcome of the evaluation of the general reductions in employers' social security reductions (*exonérations générales de cotisations)* currently conducted by the *Comité de suivi des aides publiques aux entreprises et des engagements* and expected to be completed in early 2017. The transformation of the CICE into a permanent reduction in employers' social contributions would represent a first step towards the simplification of the set of measures to decrease employers' social security contributions (i.e. the *allègements généraux des cotisations sociales patronales,* the CICE, and the employers' social security exemptions contained in the Responsibility and Solidarity Pact). Such a simplification might reduce the budgetary costs of these measures, secure over time the tax breaks of the different categories of income and decrease social contributions at the level of median income earners who are subject to high tax wedge.[28]

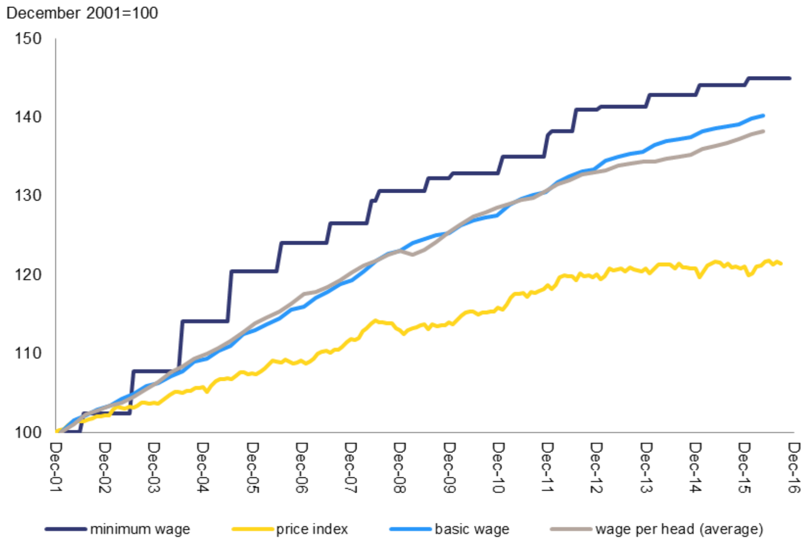
While increases in the minimum wage continued to be moderate in 2016, with no discretionary hikes by the government, wage compression at the bottom of the wage scale and its impact on employment outcomes for the low skilled remains an issue of concern. The level of the minimum wage in France remains relatively high, as the gross minimum wage represented 62% of the median wage in 2015, the highest rate in the EU.[29] Such a high level is due to minimum wage dynamics that have been historically faster than inflation, basic wage[30] or average wage per head growth (Figure 2).[31] More recent developments in the minimum wage have been instead more moderate, resulting from the automatic minimum wage indexation mechanism without discretionary hikes by the government. In January 2015, the minimum wage increased by 0.8% in nominal terms and by 0.7% in real terms, below labour productivity (0.9%) and basic or average wages (respectively at 1.1% and 1.3% in real terms). In January 2016, the minimum wage increased by 0.6% in nominal terms and by 0.3% in real terms, in line with the growth rate of labour productivity (0.2%) and below basic or average wages (respectively at 0.9% and 1.1% in real terms). Despite the recent moderation in the minimum wage developments, there is still wage compression at the bottom of the wage scale, with potentially harmful consequences for the employment of the most vulnerable workers. As a result, beyond the absence of ad-hoc increases in the minimum wage, a revision of its automatic indexation mechanism would help correct past excessive increases in the minimum wage and increase job opportunities for the workers at the bottom of the wage scale.

The Labour Act of 8 August 2016 (also called El Khomri law) may reduce the degree of segmentation of the labour market. The El Khomri law aims at revising the Labour Code to extend the role of collective bargaining and to shift, towards the firm, the predominant level of collective bargaining in France. In particular, the law requires the revision of the whole Labour Code by August 2018, so as to categorise the norms into: (i) public order rules, (ii) norms to be fixed through collective bargaining at firm or at branch level, and (iii) norms that can be applied in the absence of a collective agreement. This revision (except for the

[28] OECD (2016), Taxing Wages 2016, OECD Publishing, Paris.
[29] As shown in the 2016 Country Report, even in net terms the cost of labour at the minimum wage in France remains the fifth highest in the EU.
[30] The evolution of basic wages is calculated on the basis of the '*indice des taux de salaire horaire des ouvriers dans l'ensemble des secteurs non agricoles*'.
[31] See also the 2016 Country Report on France for an in-depth description of the functioning of the French minimum wage.

provisions on working time already re-transcribed by the Labour Act itself) needs to be made by a committee of experts to be appointed by the end of the year. Moreover, the law contains measures to increase the effectiveness of collective bargaining, notably through the reduction in the number of branches,[32] the introduction of the majority principle for the adoption of collective agreements, the reform of rules underpinning the denunciation and revision of collective agreements, and the introduction of firm-level agreements that firms can use to adjust wages and working time arrangements while maintaining or increasing the level of employment. Lastly, the law adds two new definitions of 'economic dismissal', following the case-law of the French Court of Appeal, to the two definitions already codified. This redefinition, together with the firm-level agreements to maintain or increase the level of employment, is expected to allow employers to substitute shorter with longer-term contracts, hence reducing the segmentation of the labour market.

Figure 2: evolution of minimum and average wage, France



Source: Insee, Dares, enquêtes Acemo.

The implementation of the Labour Act and the appropriation by social partners of the flexibility it offers will be key in determining its impact on the cost of labour and labour market segmentation. Most of the implementing decrees are planned to be adopted by the end of the year. However, already as of end-November 2016, not all decrees have been adopted according to the planned timeline. Among the decrees to be adopted, two seem the most important for reducing the segmentation of the labour market; notably the decree defining the perimeter of the 'compensation' upon which social partners could bargain for the adoption of a firm-level agreement for maintaining or increasing the level of employment and the one providing the definition of a drop in a 'firm's turnover' required for triggering an economic dismissal. Moreover, social partners may require time to fully make use of the new and extended possibilities for developing the social dialogue within firms that have been granted by the El Khomri law. For example, the law allow company-level agreements to decrease the overtime premium from the default rate (25% for the first 8 overtime hours

[32] The restructuring of the first 100 branches was acted by the 'committee for the restructuring of branches' on 15 September 2016. It mainly concerned branches that did not sign any new collective bargaining for more than twenty years.

worked over a week and then 50% for the following hours) down to the minimum set by law (10%). If used by companies, this provision may create 15 000 jobs under the assumption that it would decrease the cost of labour by 0.5% for 6 millions of workers.[33] In this respect, the evolution of social dialogue within firms and branches will determine the success of the law, especially for companies employing less than 50 employees where firm-level collective agreements still require several preconditions (such as the *mandatement syndical*). As a result, it is too early to assess what the actual impact of the El Khomri law will be, which, as mentioned above, also needs to be followed by a comprehensive review of the Labour Code.

The incentives to hire on longer-term contracts have helped to address the labour market segmentation in smaller firms. The SME recruitment incentive programme (*prime à l'embauche PME*) allows for an annual, lump sum, bonus of EUR 2000 paid quarterly over a two-year period to companies with fewer than 250 employees, which have hired new employees on an open-ended or fixed-term contract of more than 6 months between 18 January and 31 December 2016 for wages up to 1.3 time the statutory minimum wage. This initiative has been merged with the bonus for recruiting the first employee introduced by the decree 2015-806 of 3 July 2015 and prolonged for the year 2017. As of 22 October 2016, the number of hires that have benefited from this subsidy were about 670 000. Two-thirds of these hires concerned open-ended contracts, while the remaining third concerned fixed-term contracts of a length of 6 or more months.

No reform of the unemployment benefit system has been agreed yet, with a view to ensuring the financial balance of the system and favouring sustainable forms of employment. In September 2016, the deficit of the unemployment benefit system was estimated at EUR 4.4 bn in 2015 and projected to slightly decrease to EUR 4.3 bn in 2016 and EUR 3.8 bn in 2017. This would further increase the system's debt from EUR 25.8 bn in 2015 to EUR 30.0 bn in 2016 and EUR 33.8 bn in 2017. The current rules for the benefit calculation favours a succession of short-term full-time jobs over long-term part-time jobs and creates incentives for employers to offer short-term employment to be complemented by in-work benefits, weighing on the fiscal balance. Moreover, the design of the unemployment benefit system, notably as regards eligibility conditions and the generosity of the system, may weaken incentives to return to work.[34] A first round of negotiations among social partners took place last spring, without reaching any agreement though and no clarity on the next steps of the process to reform the unemployment benefit system.

Overall, despite ongoing reform efforts, further actions are necessary to improve cost competitiveness and the functioning of the labour market. The first evaluations of the CICE using firm-level data covering the period 2013-2014 have shown a positive impact on employment and firms' profit margins. This increase in profit margins has not yet translated into any significant effect on investment, R&D and exports and further evaluations will be needed to have a complete picture of the effects of the CICE. While the CICE credit rate will be increased from 6% to 7% in 2017, the modalities of its announced transformation into a permanent reduction in employers' social security contributions have not been specified yet.

[33] COE-Rexecode (2016), 'L'impact sur l'emploi du projet de loi "Travail",' Documents de travail, No. 58, May 2016.

[34] Brigitte Dormont, Denis Fougère et Ana Prieto (2001), "L'effet de l'allocation unique dégressive sur la reprise d'emploi", Insee, Economie et statistique, No. 343, 2001-3. Bruno Coquet (2016a), "Dette de l'assurance chômage: quel est le problème?", Les Notes de l'OFCE, No. 60, 10 March 2016. Bruno Coquet (2016b), "Dégressivité des allocations chômage: une réforme ni nécessaire ni efficace", Policy Brief OFCE, No. 4, 4 October 2016.

Recent developments in the minimum wage have been in line with labour productivity and average wage developments, but have not alleviated wage compression at the bottom of the wage scale, hampering job creation for the low skilled. While the Labour Act is expected to have positive effects on the segmentation of the labour market and paves the way for a reform of the Labour Code, its actual impact on the labour market segmentation and the labour cost will depend on the quality of social dialogue at firm-level. Finally, there is no clarity yet on the future reform of the unemployment benefit system.

3.4 Education and life-long learning

This section describes policy measures to improve the link between the labour market and the education system, as suggested by CSR 3. This recommendation calls on the authorities to reform the apprenticeship and vocational training systems, putting more emphasis on the actions targeted to the low-skilled.

The reforms of the vocational training system are on-going. The 2014 reform intended to improve the suboptimal allocation of resources among active population sub-groups, such as low-qualified/highly qualified, unemployed/employed, SMEs/big firms. The Personal Training Account (*compte personnel de formation, CPF*) introduced in January 2015 by the 2014 reform of the vocational training system (Sapin law) is gradually increasing its take-up, with over 3.3 mn accounts created and over 500 000 trainings, 60% of them for jobseekers. As part of the Labour Act of 8 August 2016, additional training rights will be made available for non-qualified employees and early-school leavers, while the CPF will be merged into the newly created Personal Activity Account (*compte personnel d'activité, CPA*). However, the quality of training actions proposed in the context of the CPF is not in line with a proper individual and independent career-building tool. Moreover, the emergency job plan of 18 January 2016 increased by 500 000 the number of trainings for jobseekers. 75 % of these trainings are currently under implementation or scheduled, although not much information is available on the nature of trainings (qualifying, non-qualifying) provided. Also, 2016 has been the first year of implementation of the companies' contribution for financing vocational training introduced by the 2014 reform. This contribution aims at increasing funds for SMEs' employees and unemployed, but no data to assess its effects are available at this stage, while a gradual increase of trainings funds for jobseekers can already be observed. Beyond these measures, the improvement of the governance of the vocational training system, both at national and regional level, remains key to ensure the alignment of training offer with labour and economic needs.

The on-going vocational training reforms are underway but little has been done to reform the initial vocational training system. The transition from school to work remains challenging and the least qualified young people are the most affected. Apprenticeship presents better labour market integration results than school-based vocational training. On the back of a premium introduced in June 2015 for less than 11 employees companies hiring a minor apprentice and an increase in the State commitment to hire apprentices, apprenticeship figures stabilised to 405 000 at the end of 2015, after having dropped over the period 2013-2014. To sustain this positive trend, the Ministry of Labour opened 85 apprenticeship diploma and reviewed the school-based vocational training system, to open 500 new vocational training pathways and to reshuffle the initial training offer towards sectors with better employment prospects. As school-based vocational training represents three-quarters of young people engaged in vocational training, its efficiency plays a predominant role to ensure proper labour market integration for young people who are enrolled in technical education.

Overall, the links between the education system and the labour market remain suboptimal and the relevance of trainings offered is not sufficiently in line with labour market needs. Notably a better coordinated system of governance for the vocational training system, both at national and regional level, would be able to ensure that training courses match labour market needs, increase access to training of different categories of active workers, while a reform of the initial vocational training system would address the weaknesses of the school-based vocational training offer in parallel with a consolidation of apprenticeship.

Annex I: Overview of MIP-relevant reforms

MIP objective: ensuring compliance with SGP, improving public finances			
Public finances			
SGP compliance			
Announced measures	*Adopted measures*	*Implemented measures*	*Sources of commitment*
Expected by end 2017: the Projet de loi de Finance *(PLF)* 2017 and the Projet de loi de financement de la sécurité sociale *(PLFSS)* 2017 include new initiatives, mainly on the expenditure side, with a total cost of EUR 9 bn. The PLF and PLFSS also identify consolidation measures for a total of EUR 14 bn to compensate these new initiatives as well as the EUR 5 bn in additional measures announced in the Stability Programme. For a more detailed description of the new initiatives and the compensatory measures, the reader is referred to the Staff Working Document of the Commission opinion on the Draft Budgetary Plan opinion. The PLF scales back the ambition of the EUR 50 bn consolidation package over 2015-2017 announced in the *Loi de Programmation des Finances Publiques 2014-2019 (LPFP)*. Over the same period only EUR 40.7 bn savings would now be realised.		**2015 and 2016:** EUR 30.5 bn consolidation measures would be realised over the period 2015-2016 according to the PLF 2016 compared to the EUR 35.5 bn measures initially planned in the LPFP. The savings are calculated compared to trend expenditure growth, with trend expenditure growing by 2.4% in value over 2013-2017. These savings were realised by the strict control of expenditure under the expenditure norm of the state; the introduction of the local government expenditure growth target (ODEDEL) and the cut in dotation to local authorities of EUR 6.8 bn over the period 2015-2016 and a contained growth of healthcare expenditure with a growth target (ONDAM).	CSR (1) – 2016: "Ensure a durable correction of the excessive deficit by 2017 by taking the required structural measures and by using all windfall gains for deficit and debt reduction. …"

Spending review			
Announced measures	*Adopted measures*	*Implemented measures*	*Sources of commitment*
Expected by end 2017: a new round of spending reviews was launched on 12 new areas and published on 24 October 2016. Out of these spending reviews, four relate to local government. The spending reviews of 2015 and 2016 allow documenting EUR 400 mn savings in the PLF 2017 according to the government. **Expected by end 2018:** the third phase of the spending reviews has been launched, set out in the yellow background budget document annexed to the 2017 DBP.		**In 2015 and 2016:** the results of the 2015 and 2016 spending reviews were published as annexes to respectively the PLF 2016 and 2017. The 2015 spending reviews allowed planning savings with an expected yield of nearly EUR 500 mn in the *Loi de Finance Initiale* (LFI) 2016. In the course of 2016 the individual spending reviews were also made public.	CSR (1) – 2016: "… Specify the expenditure cuts planned for the coming years and step up efforts to increase the amount of savings generated by the spending reviews, including on local government spending, by the end of 2016. …"
Independent public policy evaluations			
Announced measures	*Adopted measures*	*Implemented measures*	*Sources of commitment*
Expected in 2017: In the framework of the Modernisation de l'Action Publique (MAP) six new assessments have been started in 2016 to enable further savings to be made in 2017. **Expected by end 2016:** a meta-assessment is expected by the end of 2016. This meta-assessment focuses on the methodology used and monitors the effects of the public policy assessments carried out since the end of 2012 in the framework of the MAP.		**Between 2012 and 2016:** 80 public policy evaluations were rolled out since December 2012 in the framework of the MAP. Out of these 80 assessments, 68 were completed as of September 2016. In terms of savings generated, the 59 assessments launched in 2013-2014 generated savings of EUR 7.1 bn according to the government.	CSR (1) – 2016: "… Reinforce independent public policy evaluations in order to identify efficiency gains across all sub-sectors of general government."

Taxation			
Shifting taxation from production to consumption			
Announced measures	*Adopted measures*	*Implemented measures*	*Sources of commitment*
As of 2017: the DBP reduces to 28% the corporate income tax rate for all SMEs above EUR 38 120 and up to EUR 75 000 of profits. By 2020, the aim is for the 28% rate to be extended to cover all businesses, regardless of profit levels.		**Until 14 April 2017**: 40% additional tax break for productive investments. This represents an extension of a similar measure in force since 15 April 2015.	CSR (5) – " Take action to reduce the taxes on production and the corporate income statutory rate while broadening the tax base on consumption, in particular as regards VAT. … "
Simplification of the tax system			
Announced measures	*Adopted measures*	*Implemented measures*	*Sources of commitment*
As of 2017: the 2017 DBP eliminates two low-yield taxes for an amount of EUR 249 mn. Tax expenditures continue to increase in number and in value, and are set to reach EUR 89.9 bn in 2017. **In 2018:** the 2017 DBP introduces withholding personal income taxation as of 2018.		As part of the implementation of the 2014-2019 multiannual budgetary framework providing for a mandatory assessment of tax expenditures three years after their creation, the 2016 spending review includes an assessment of free trade zones for 2017.	CSR (5) – " Remove inefficient tax expenditures, remove taxes that are yielding little or no revenue and adopt the withholding personal income tax reform by the end of 2016. "
MIP objective: improving the business environment			
Business environment			
Remove barriers to competition in the services sector			
Announced measures	*Adopted measures*	*Implemented measures*	*Sources of commitment*
The regulatory framework of taxis and	The law on Transparency, Anti-	Out of the 116 measures of the Macron	CSR (4) – " Remove barriers to activity

vehicles with a driver is currently being reviewed and a law reforming these sectors should be adopted in autumn (Grandguillaume draft law).	Corruption and Economic Modernisation (Sapin II law) of 8 November 2016 eases somewhat qualification requirements for craft professions. The Healthcare law of 26 January 2016 eases somehow access to professions and services in the healthcare sector. The law of 28 December 2015 on Ageing Society reformed the regulatory framework for home-care services.	law that required an implementation decree, 108 measures (93%) were already in effect on 23 October 2016. Four decrees were adopted on 29 June 2016 regarding a number of legal professions (barristers before the *Conseil d'Etat* and the Court of Cassation, lawyers, notaries, bailiffs, court-appointed auctioneers and valuers, and court-appointed administrators and receivers). Further on legal professions, two orders were adopted on 16 September 2016 identifying 247 free set-up areas for notaries and specifying the list of documents required to apply for a notary nomination. Ownership rules for certain legal and accounting professions, architects and surveyors were relaxed through the decrees of 29 June and 1 July 2016. Twenty-one ordinances required by the Macron law were adopted by 23 October 2016.	in the services sector, in particular in business services and regulated professions. … "
Reform size-related criteria			
Announced measures	*Adopted measures*	*Implemented measures*	*Sources of commitment*
	The law on Transparency, Anti-Corruption and Economic Modernisation makes it easier for a business to swift from the sole trader status to another		

	status, notably the Limited Liability Sole Proprietorship status or the Single-Member Private Company status.		
Simplification of business environment			
Announced measures	*Adopted measures*	*Implemented measures*	*Sources of commitment*
	Since 2013: The simplification programme is ongoing with 262 out of the total 415 announced measures in effect on 24 October 2016, The Transparency, Anti-Corruption and Economic Modernisation law eases training requirements prior to business start-up and removes the requirement for micro-entrepreneurs to open a second bank account at least during the first year of business.		
Innovation policy			
Announced measures	*Adopted measures*	*Implemented measures*	*Sources of commitment*
Under the hospices of the National Commission on Investment of Innovation Policies (CNEPI), France Stratégie is conducting two studies on innovation policy schemes: • One on the economic impact of the competitiveness clusters (*pôles de compétitivité*) for which a preliminary working document has been published in March 2016. The final report remains to be published (expected by en 2016).	**In March 2016:** A mid-term stock-taking report of the Investment for the Future programme (*Programme d'Investissements d'Avenir*) coordinated by France Stratégie was published in March 2016. **In June 2016:** the third phase of the Investment for the Future programme has been launched. **In July 2016:** Publication of a scorecard on innovation in France in July 2016 by	The Education and Research Ministry publishes a yearly report on the research tax credit (CIR). The last edition was published in April 2016.	CSR4 – "Take steps to simplify and improve the efficiency of innovation policy schemes."

• Another one on the research tax credit (CIR) for which the tendering process has been launched in June 2016. Expected by end 2016: The Economy Ministry is conducting a qualitative study on the impact of the specific tax arrangements applying to young innovative companies (Jeunes Entreprises Innovantes).	the Ministry of Education and Research.		
MIP objective: improving the functioning of the labour market			
Labour market			
Labour cost reductions			
Announced measures	*Adopted measures*	*Implemented measures*	*Sources of commitment*
In 2017: as part of the 2017 DBP, the Competitiveness and Employment Tax Credit (CICE) will be increased from 6% to 7% of payrolls for wages up to two and a half times the statutory minimum wage. **In 2017:** the programme for hiring new employees on an open-ended or fixed-term contract of more than 6 months will be extended to cover hires included between 1 January and 31 December 2017.		**In 2016:** the CICE and the reduction in employers' social security contributions contained in the Responsibility and Solidarity Pact have been kept unchanged in 2016. **In 2016:** the SME recruitment incentive programme (*embauche PME*) allowed for an annual, lump sum, bonus of EUR 2 000 paid quarterly over a two-year period to companies with fewer than 250 employees, which have hired new employees on an open-ended or fixed-term contract of more than 6 months between 18 January and 31 December 2016 for wages up to 1.3 time the	CSR (2) – 2016: "Ensure that the labour cost reductions are sustained..."

		statutory minimum wage. This initiative englobed the bonus for recruiting the first employee introduced by the decree 2015-806 of 3 July 2015.	
In 2017: no extra rise (*coup de pouce*) has been announced for 2017, in addition to the increase in the minimum wage implied by the automatic mechanism of minimum wage revaluation.		**In 2016:** through the decree 2015-1688 of 17 December 2015, the government raised the minimum wage by 0.6% in January 2016, offering no extra rise (*coup de pouce*) in addition to automatic mechanisms of minimum wage revaluation.	CSR (2) – 2016: "... and that minimum wage developments are consistent with job creation and competitiveness."
Reform of the labour law			
Announced measures	*Adopted measures*	*Implemented measures*	*Sources of commitment*
	In 2016: the Labour Act (El Khomri law) introduces company-level agreements for maintaining or increasing employment, through which working conditions can be reviewed (including those concerning work duration and compensation). The implementing decrees were expected by October 2016. **In 2015:** an indicative scale for unfair dismissals was introduced by the Macron law. Implementing decrees have not been undertaken yet. **Starting from 2017:** the Labour Act introduces the majority agreement rule for company-level agreements: as from 1 January 2017 for company-level agreements concerning working hours and agreements for maintaining or increasing employment; as from 1	**August 2016:** the Labour Act redefines the economic dismissal procedure.	CSR (2) – 2016: "Reform the labour law to provide more incentives for employers to hire on open-ended contracts."

	September 2019 for all agreements. **Expected by August 2018:** the Labour Act requires that a committee of experts will re-draft the Labour Code (except for the provisions on working hours already re-transcribed by the Labour Act itself) by the end of 2018, so as to increase the scope of company-level agreements. Hence, the new Labour Code will define how different bargaining levels articulate, notably by setting the fields in which company-level agreements may pre-dominate sector-wide agreements, subject to compliance with statutory standards (working hours, minimum wage). **Expected by August 2019:** the Labour Act requires the restructuring of professional branches from around 700 to around 200 occupational sectors by 2019. The restricting of the sectors that have not signed any collective agreements for the last fifteen years or whose geographic scope is merely local or regional is planned by the end of 2016.		
Reform of unemployment benefit system			
Announced measures	*Adopted measures*	*Implemented measures*	*Sources of commitment*
Expected by end 2016 – beginning 2017: a reform of the current unemployment benefit system is expected by end 2016 – beginning of			CSR (3) – 2016: "… By the end of 2016, take action to reform the unemployment benefit system in order to bring the system back to budgetary sustainability

2017. In the absence of an agreement, the government announced to take responsibility for adopting a decree regulating unemployment insurance conditions.			and to provide more incentives to return to work."
MIP objective: improving the link between the education system and the labour market			
Education and social policies			
Vocational training and apprenticeship			
Announced measures	*Adopted measures*	*Implemented measures*	*Sources of commitment*
In 2017: opening of 500 new vocational training pathways towards sectors with better employment prospects. **In 2017:** implementation of the State-Regions platform including mixed school-apprenticeship pathways, experimental extension to 30 years of eligibility to apprenticeship.	**In 2016:** The emergency job plan of 18 January 2016 created almost 500 000 additional places to get people into jobs, including 360 000 places for training job-seekers, 50 000 for vocational training contracts, 10 000 skills certification actions and heightened support for 70 000 new business projects (Training plan). **In 2016:** the eligibility criteria for the Youth Guarantee Scheme (*Garantie jeunes)* were broadened for 2017 by Article 46 of the Labour Act. **Expected as of 1 January 2017:** set up of the Personal Activity Account (CPA), established by Article 39 of the Labour Act. **In 2016**: training rights to access a first qualification for early-school leavers and increased training rights for non-qualified employees granted by article 39	**Since 2014**: implementation of the 2014 vocational training reform, including creation of new governance entities (CNEFOP and CREFOP) and since 2016 implementation of the "1% continued vocational training" contribution for companies. **Since 2014**: reform of the apprenticeship-financing tax increasing the discretionary share granted to Regions and aiming to increase support towards first qualification levels. **Since 2015:** Personal Training Account in place with currently over 3.3 mn accounts created and over 500 000 trainings provided, 60% of them targeted to jobseekers. **Since 2015:** Small companies apprenticeship hiring premium of EUR 4 400 for a minor apprentice.	CSR (3) – "Improve the links between the education sector and the labour market, in particular by reforming apprenticeships and vocational training, with emphasis on the low-skilled. … "

	of the Labour Act. **In 2016**: opening of access to 85 first professional titles to apprenticeship (to be followed by others) through decree.		