030773/EU XXV. GP
Eingelangt am 25/06/14

COUNCIL OF THE EUROPEAN UNION

Brussels, 5 June 2014 (OR. en)

9935/14 ADD 4

ECOFIN 491 UEM 144

COVER NOTE

From:	Aude Pohardy, Conseiller, Permanent Representation of France to the EU
date of receipt:	5 June 2014
To:	Carsten Pillath, Director-General, DGG-Economic Affairs and Competitiveness General Secretariat of the Council of the European Union
Subject:	Stability Programme of France for the period 2014-2017

Delegations will find attached the Stability Programme of France for the period 2014-2017 in English.

www.parlament.gv.at

FRANCE STABILITY PROGRAMME 2014-2017

23 April 2013

www.parlament.gv.at

Contents

1. OVERVIEW 4

2. MACROECONOMIC SCENARIO 7

3. PUBLIC FINANCE SCENARIO 13

3.1 Overall strategy and medium-term budgetary objective 13

3.2 Outturn 2013 16

3.3 Public finance path under the no-policy-change scenario and trend path 17

3.4 Structural budget balance 18

3.5 The government balance by sub-sector 21

3.6 Government expenditure 23
3.6.1 General government expenditure 23
3.6.2 Central government expenditure 26
3.6.3 Expenditure of other central government bodies 29
3.6.4 Social security funds' expenditure 29
3.6.5 Local government expenditure 32

3.7 Government revenue 34
3.7.1 General government revenue 34
3.7.2 Central government revenue 36
3.7.3 Social security funds' revenue 37
3.7.4 Local government revenue 37

3.8 Government debt and stock-flow adjustment 40

4. EXCESSIVE DEFICIT PROCEDURE (EDP) 44

4.1 Excessive Deficit Procedure 44

4.2 Convergence towards the medium-term budgetary objective 46

5. SENSITIVITY ANALYSIS AND COMPARISON TO PREVIOUS PROGRAMMES 47

5.1 Sensitivity analyses 47

5.2 Comparison to previous programmes 50

www.parlament.gv.at

5.2.1 Comparison with the previous Stability Programme 50
5.2.2 Comparison with the European Commission's 2014 winter public finance forecasts 52

6. QUALITY OF PUBLIC FINANCES.....53

6.1 Quality of government expenditure 53
6.1.1 Ongoing spending review process (MAP) 53
6.1.2 Public investment evaluation 57
6.1.3 Streamlining healthcare expenditure 58
6.1.4 Streamlining local government expenditure 59

6.2 Quality of government revenue 60

7. SUSTAINABILITY OF PUBLIC FINANCES.....64

7.1 Sustainability of general government debt..... 64
7.1.1 Impact of the ageing population on public finances 64
7.1.2 Sustainability gap 65

7.2 Contingent liabilities 67

7.3 Ongoing structural reforms 69

8. INSTITUTIONAL ASPECTS AND FISCAL GOVERNANCE 70

8.1 New fiscal governance structure fully in place 70

8.2 Continuing reform of European fiscal governance – the Two-Pack..... 72

8.3 Statistical governance 74

8.4 Status of this Stability Programme under internal procedures 76

9. NOTES ON METHODOLOGY AND STATISTICAL TABLES.....77

9.1 Statistical appendix..... 77

9.2 Methodological appendix: Structural analysis of government balance 83

9.3 In-year progress report on correction of the excessive deficit and compliance with the Recommendation ... 86

3

1. Overview

After remaining flat for 5 years, France's economic activity returned to its pre-crisis level at the end of 2013. The recovery has been gradual and uneven. Initiatives in the euro area helped to ease financial tensions, particularly the decisions taken by the European Council in June 2012 and the increased involvement of the ECB announced in September 2012. However, adjustments in the euro area, particularly in countries with major imbalances, put a drag on France's external environment at a time when France itself was ambitiously tackling deficits.

Consequently, the French economy posted weak growth in 2013, at a rate of only 0.3%[1]. But there were encouraging signs at the end of the year, with a recovery in investment and jobs in the private sector for the first time in two years. The annual rate of growth now stands at around 1%. The Government's concern is to foster faster growth and a sustainable increase in jobs in the private sector, in order to bolster households' purchasing power, especially the least well-off households, who are the first to suffer when the economy lacks dynamism.

The Government's two-pronged strategy is designed to:

- strengthen our economy and its capacity to create jobs, while making targeted efforts to increase the purchasing power of the least well-off;
- continue to consolidate our public finances to regain fiscal room for manoeuvre and decrease government debt, without impeding growth and while financing our priorities for the future – secondary and higher education, justice and security.

This is the whole purpose of the policies described in this Stability Programme and the National Reform Programme that goes with it.

This strategy hinges on implementation of the Responsibility and Solidarity Pact, combined with an unprecedented effort to slow spending, to achieve savings of €50 billion between 2015 and 2017.

With the Responsibility and Solidarity Pact, businesses' cost of labour, which has already fallen as a result of the Competitiveness and Employment Tax Credit (CICE), will be cut further for a total reduction of €30 billion. Starting in 2015, there will no longer be any social security payroll contributions on minimum-wage jobs, other than unemployment insurance contributions. In 2016, family allowance contributions will be reduced as well on jobs paying up to three and a half times the minimum wage. In addition, business taxes will be streamlined and reduced: the corporate social solidarity contribution (C3S), which is based on turnover and not on income, will be reduced starting in 2015 and phased out by 2017; the exceptional corporate income tax payment for large corporations will be phased out in 2016 and the standard rate of corporate income tax will decrease starting in 2017. At the same time, since there is an urgent need to boost the purchasing power of low-income

[1] Adjusted for seasonal variations and working days

households, an initial measure will be introduced in 2014 and, in 2015, smaller employee social security contributions will result in a gain of €500 per year for workers earning the minimum wage. Measures in favour of the least well-off will total €5 billion by 2017.

These efforts will allow businesses to free up new resources for innovation, investment and creating jobs, thus contributing to economic recovery and higher employment. And the households in greatest need will receive immediate support.

Based on the usual macroeconomic patterns, the Pact should boost growth by 0.6 points over the forecast period and produce 200,000 additional jobs. In practice, this impact should be amplified by the commitments made by economic and social players under the Pact and, more generally, by the positive confidence shock produced by extending and expanding reductions in spending and tax and social security contributions.

At the same time, France has confirmed its commitment to bring the deficit down to 3% of GDP in 2015 and achieve its savings target of €50 billion.

The government deficit must be reduced to stabilise and then decrease debt as a share of GDP. Reducing the deficit will also ensure that the central government continues to enjoy favourable borrowing terms which in turn will be passed on to businesses and households. Reducing the government deficit will also ensure that France continues to have its say in Europe and that the most vulnerable countries can still count on its support.

Savings of €50 billion will be needed between 2015 and 2017 to bring government expenditure growth back into line with inflation. This is an unprecedented and bold target, but it will enable us to continue cutting the deficit without introducing new taxes.

The effort will be shared equally across the whole general government sector. Central government and central government agencies' will shoulder the largest portion (€18 billion over three years) by increasing efficiency and further improving their cost controls. The other sectors will make virtually similar contributions: local government will bring expenditure growth back into line with inflation, saving €11 billion through organisational reform, the health insurance system will save €10 billion through ongoing structural reforms to ensure the quality of care and the level of coverage while keeping costs under tighter control, the social protection system will save €11 billion through reforms that have already been adopted, notably regarding pensions and family policy, and through future measures, such as efficiency gains in the management of social security funds and a stabilisation of benefits in nominal terms, except for minimum social benefits, for one year.

Civil servants will also play their part through a stabilisation of the civil service pay scale, but efforts to recruit new personnel in priority sectors will continue.

Overall, France's growth rate is expected to stand at 1% in 2014 before rising to 1.7% in 2015 and 2 ¼ % in 2016-2017. The deficit will continue to shrink to 3.8% of GDP in 2014, 3.0% in 2015 before falling to 1.3% in 2017. In keeping with our commitments, the cyclically-adjusted "structural" balance will be brought close to equilibrium by 2017 by means of an adjustment of 0.8 points per year in 2014 and 2015, followed by an adjustment of 0.5 points per year after that. All this will be achieved with no new taxes: over the period, the aggregate tax and

www.parlament.gv.at

social security contribution rate will be reduced, the share of government expenditure will shrink by 3 points of GDP and government debt will remain steady in 2015 before decreasing for the first time since 2006.

France has been making unprecedented efforts for the last two years and will take these efforts to the next level over the course of the next three. The sustained recovery of the French economy depends on it.

2. Macroeconomic scenario

After growth picked up again in 2013 to reach 0.3%[2], it is expected to climb to 1.0% in 2014 and 1.7% in 2015. Growth is bound to take strength from renewed confidence in the euro area, the initial impact of the Responsibility and Solidarity Pact on competitiveness and purchasing power, and a brighter international environment.

However, growth is unlikely to significantly exceed its potential rate before 2015 due to the euro's appreciation since the third quarter of 2012 and ongoing fiscal consolidation, albeit at a more measured pace than in previous years.

The average annual growth rate should stand at 2 ¼ % in 2016 and 2017, which will gradually close the output gap.

This growth scenario is similar to those put forward by the European Commission and international organisations, which forecast growth of around 1% in 2014 before rising in 2015 to 1.6% (OECD), 1.5% (IMF) and 1.7% (European Commission) under unchanged policies, before fiscal consolidation and before the Responsibility and Solidarity Pact.

There are still uncertainties: the pace of France's recovery hinges on that of the euro area. The growth in world trade will depend on future financial conditions in advanced economies and the capacity to control the impact that America's gradual monetary policy normalisation will have on emerging economies. At the same time, the behaviour of domestic economic agents will depend on their confidence and their expectations.

Growth resumed in the second quarter of 2013 and should continue to gather strength throughout 2014, with some quarterly variations.

Growth has been positive again since the second quarter of 2013. The current growth trend is approximately one-quarter of a percentage point per quarter, after being flat between the third quarter of 2011 and the beginning of 2013. This recovery has seen some ups and downs: after rebounding sharply in the second quarter of 2013 to 0.6%, the economy contracted slightly in the third quarter, shrinking by 0.1%, before picking up again at the end of the year with growth of 0.3%.

Growth should gather strength at the beginning of 2014, despite some potential hiccups. A temporary dip cannot be ruled out in the first quarter, given the exceptionally warm weather and certain measures that underpinned growth at the end of 2013, such as an easing of the rules to access employee savings, expectations of a stiffer penalty/bonus scheme for fuel efficiency and the VAT hike on 1 January 2014. The dip should be followed by a stronger rebound of GDP growth in the second quarter as the outlook improves and the economy bounces back from the adverse environment that existed at the start of the year.

[2] GDP growth in 2013 as stated in the quarterly national accounts which are adjusted for number of working days

www.parlament.gv.at

The recovery will accelerate as households and businesses regain confidence

Renewed confidence should lead to a recovery in business investment as the outlook for demand improves. The better business climate since the second quarter of 2013 is a sign of renewed business confidence. The shift will gather strength as the effects of the Competitiveness and Employment Tax Credit (CICE) start to be felt and the Responsibility and Solidarity Pact is implemented, reducing businesses' labour costs by a total of €30 billion and their taxes by some €10 billion by 2017. With this support, business investment, which started to recover in the last quarter of 2013, should grow by 1.8% in 2014 and by 5.2% in 2015 compared to a contraction of 2.3% in 2013. The resumption of investment should be underpinned by the continued availability of very favourable financing conditions, made possible by capital inflows to the euro area and gradual fiscal consolidation in keeping with our commitments. Furthermore, businesses should increase their inventories slightly on the back of a more promising outlook for demand, which will benefit from the measures in the Responsibility and Solidarity Pact.

After remaining soft for five years and growing by an average of 0.4% between 2007 and 2012, **household consumption will become the second domestic engine of renewed growth**, expanding by 0.8% and then by 1.6%. Purchasing power growth should also accelerate gradually from 0.3% in 2013 to 0.7% in 2014 and then to 1.3% in 2015 compared to a contraction of 0.9% in 2012. This acceleration will be underpinned by the measures in the Responsibility and Solidarity Pact, such as the reduction of payroll contributions on low-paid jobs in 2015 and tax cuts for households in the lowest income tax brackets, and by a stronger labour market. Renewed household confidence as the labour market gradually improves should lead households to reduce their precautionary savings, causing a gradual fall in the savings rate to 15.6% in 2013, 15.5% in 2014 and 15.2% in 2015. Fiscal consolidation will also underpin the decrease in households' precautionary savings.

A brighter international economic environment and measures to foster competitiveness should support exports

Demand for France's exports should rebound, growing by 4.8% in 2014 and by 6.5% in 2015.

The recovery that started in the euro area in 2013 is expected to gather strength, with faster growth, as financial tensions abate and the pace of fiscal consolidation slows down in view of the adjustments already accomplished. The euro area's growth is expected to remain moderate at this point, as a result of the large disparities that remain between Germany on the one side, and Italy and Spain, which are just emerging from two years of recession, on the other.

Developments outside of the euro area are likely to be mixed but favourable on the whole. The United Kingdom and the United States should continue to enjoy strong and rising growth. On the other hand, Japan's growth is expected to slow due to tighter fiscal policy. The growth of emerging economies should continue to be fairly strong in 2014-2015, but the long-term trend is likely to show weaker growth than during the pre-crisis period.

www.parlament.gv.at

Export growth is expected to rebound to 3.4% in 2014 and then 4.7% in 2015, in view of strong global demand and measures to promote competitiveness. This forecast factors in the reversal of France's steadily shrinking export market share since 2008 compared to the early part of the decade. This reversal stems from more balanced growth in the emerging countries and the improved non-price competitiveness of French products. In the short term, France is unlikely to derive the full benefit of strong global demand, given the recent appreciation of the euro, which undermines our price competitiveness. France's nominal effective exchange rate rose by nearly 8% between July 2012 and March 2014. On the other hand, cuts in payroll contributions and business taxes will boost competitiveness.

Foreign trade should start making a positive contribution to growth in 2015, increasing from 0.0 points in 2014 to 0.1 points in 2015 as the impact of the stronger euro fades.

Government policies should enable private sector employment to derive the full benefit of the recovery

The recovery, along with the combined effects of the Competitiveness and Employment Tax Credit and the Responsibility and Solidarity Pact should set the stage for a slight increase in private sector employment in 2014, with an annual average of 15,000 new jobs, marking a 0.1% increase, followed by much faster growth in 2015, with 160,000 new jobs for a 1% rise.

Following on from a disappointing 2013 caused by the gloomy economic climate which saw 125,000 jobs lost despite the initial impact of the Competitiveness and Employment Tax Credit and a recovery in employment in the fourth quarter, ***private sector employment*** will post a small increase in 2014, adding 15,000 new jobs. Growth should pick up gradually over the course of the year and the effects of the Competitiveness and Employment Tax Credit should be felt more strongly, leading to a recovery in employment. The growth of private sector employment should be much stronger in 2015, with 160,000 new jobs added as a result of the usual determining factors and the impetus provided by the Competitiveness and Employment Tax Credit and the Responsibility and Solidarity Pact.

Employment growth in the non-private sector should remain strong in 2014, with a net increase of 130,000 jobs, as the number of workers employed under government-sponsored contracts rises. In 2015, as this form of government support reaches maturity, employment growth in the non-private sector is expected to slow.

The primary support for the strong performance of ***non-private sector employment*** in 2014, with 130,000 new jobs, should come from proactively applied contra-cyclical employment policies in the short term to enable those furthest removed from the labour market to become participants. The number of new hires under government-sponsored contracts (CUIs-CAEs) is expected to reach 340,000 in 2014 and the Jobs for the Future programme will be phased out. Non-private sector employment should remain steady in 2015, as support from employment policies reaches maturity and renewed private sector job growth takes its place as a driving force for more jobs.

www.parlament.gv.at

An annual average of 155,000 jobs are expected to be created in 2014, followed by 175,000 in 2015 across all economic sectors. Private sector employment growth will gradually take over from the government-sponsored job schemes as a source of new employment.

Inflation will rise slightly, but be curbed by the appreciation of the euro

Inflation should pick up slightly, but very moderately, standing at 1.2% in 2014 and 1.5% in 2015, compared to 0.9% in 2013, including tobacco. The stronger euro and falling commodity prices in 2013 should continue to curb inflation in 2014 and 2015 as they are gradually passed on in consumer prices, but these effects will fade eventually. Furthermore, an end to falling oil prices and plummeting telecommunications prices should automatically lead to price hikes in 2014. The increases in the standard and intermediate VAT rates on 1 January 2014 should have a temporary impact on inflation in 2014, while the Competitiveness and Employment Tax Credit should have a deflationary impact because it will lower producers' costs. Inflation will continue to rise in 2015 as economic and employment growth gather strength.

In the medium term (2016-2017), growth should reach 2 ¼ % based on a gradual recovery scenario

The growth rate is expected to stand at 2.25% per year in 2016 and 2017, underpinned by the Responsibility and Solidarity Pact. This would mean a gradual narrowing of the output gap as government deficits are being reduced. All of the international organisations consider that the gap is very wide. This Stability Programme estimates France's output gap at -3.1% in 2015, while the OECD puts it at -3.8%, the European Commission at -2.2% and the IMF at -2.0%

Foreign trade should make a positive contribution to France's economic growth. The Responsibility and Solidarity Pact, along with all of the measures introduced as part of the National Pact for Growth, Competitiveness and Jobs, particularly the Competitiveness and Employment Tax Credit, will continue to be ramped up and will gradually have more of an impact on the price and non-price competitiveness of French products. If global demand grows in line with the long-term trend, and if the euro exchange rate remains stable, the trade deficit should gradually shrink.

Investment should continue to increase, underpinning economic growth and boosted by the Responsibility and Solidarity Pact. Further falls in the cost of labour resulting from the Pact in 2015 along with lower taxes and payroll contributions scheduled for the same year should have a favourable impact. Corporate profit margins should return to their pre-crisis level, enabling companies to maintain a high investment rate without undermining their financial soundness.

Household consumption should get a boost as purchasing power starts to rise again as a result of employment growth and measures introduced under the Responsibility and Solidarity Pact. A gradual fall in the savings rate is also expected, as precautionary savings continue to diminish against the backdrop of a steady reduction in government deficits.

www.parlament.gv.at

This forecast is still subject to many uncertainties

The current international environment features many uncertainties. The pace of the recovery will depend on global demand growth. It could turn out to be higher than expected if the euro area has a stronger recovery. There are also persistent uncertainties concerning emerging market growth. Some of these markets are particularly dependent on export demand from the advanced economies and commodity prices, as in the case of Russia and Brazil. Furthermore, renewed financial tensions linked to the external vulnerability of such countries as Argentina, Turkey, South Africa, Brazil, India, and Indonesia cannot be ruled out. Lastly, political tension could undermine investor confidence and further weaken economies that are already struggling. In addition, there is still uncertainty as to how interest rates will respond to a return to more standard monetary policy, even though central banks have enhanced their medium-term forward guidance for investors. The euro could continue to appreciate, if, for example, emerging countries' currencies drop again. Alternatively, it could depreciate, for example, if the Fed's tapering occurs more quickly than expected or if monetary policy is eased in the euro area. Based on the latest announcements made by the ECB, which is worried about the strength of the euro and the slowdown in inflation, the second hypothesis seems more likely.

There is still uncertainty in France about the behaviour of private sector economic agents. Brighter prospects for growth could lead to a stronger rebound in investment, which would entail more jobs, thereby boosting household incomes and consumption. Policies to support competitiveness and employment will have a positive impact, but the scale of this impact will depend on how businesses behave. Businesses could, for example, pass on lower labour costs in the form of price competitiveness gains that favour exports and curb domestic inflation. Alternatively, they may prefer to boost their profit margins.

Box 1 – Comparison with the European Commission's Winter 2014 Forecast

On the whole, the 2014-2015 macroeconomic scenario is in line with the European Commission scenario outlined as part of its February 2014 macroeconomic forecasts. Both scenarios forecast GDP growth of 1.0% in 2014 and 1.7% in 2015.

However, the underlying assumptions for 2015 differ. The Stability Programme scenario incorporates the positive impact of the Responsibility and Solidarity Pact on GDP and employment growth and the fiscal consolidation measures that France has planned for 2015.

The Commission's scenario forecasts faster growth in foreign trade. According to the Commission, exports are forecast to grow by 4.4% in 2014 and by 5.6% in 2015 compared to the Stability Programme's more modest growth rates of 3.4% and 4.7% respectively. The Commission also forecasts stronger growth in imports, and expects foreign trade to make a negative contribution to growth in 2015. However, it does not factor in the positive impact that the Responsibility and Solidarity Pact is expected to have on France's competitiveness.

Both scenarios give fairly similar household consumption and business investment figures. In contrast to the European Commission's scenario, the Stability Programme scenario forecasts

www.parlament.gv.at

slightly more inventory build-up by businesses and incorporates France's planned fiscal consolidation efforts.

Table 1: Macroeconomic scenario, 2013-2017

Average annual growth rate (%)	2013*	2014	2015	Average 2016-2017
GDP	**0.3**	**1.0**	**1.7**	**2 ¼**
Household consumption	0.3	0.8	1.6	2.3
General government consumption	1.8	0.4	0.8	0.3
Gross fixed capital formation	-2.1	0.2	1.3	3.3
o.w. non-financial businesses	-2.3	1.8	5.2	4.4
Contribution from inventories	0.1	0.3	0.2	0.0
Contribution from foreign trade	0.0	0.0	0.1	0.3
Exports	0.8	3.4	4.7	6.9
Imports	0.8	3.1	4.1	5.7
GDP deflator	1.1	1.2	1.5	1.7
Household consumption deflator	0.6	1.1	1.5	1.75
Wage bill (private sector)	0.9	2.2	3.5	4.3
Average nominal wage per capita (non-farm private sector)	1.5	2.1	2.4	2.8
Salaried employment (non-farm private sector)	-0.6	0.1	1.0	1.4

*INSEE quarterly accounts (adjusted for working days)

3. Public finance scenario

3.1 Overall strategy and medium-term budgetary objective

As economic growth picks up again, it must be harnessed to create more jobs. In this context, the Government is focusing on two targets: supporting growth and jobs by introducing the Responsibility and Solidarity Pact and continuing to reduce the government deficit equitably to regain fiscal room for manoeuvre, reduce the government debt burden and safeguard national sovereignty. This strategy will require, in addition to the Responsibility and Solidarity Pact, government expenditure savings of €50 billion to be made between 2015 and 2017. Lower labour costs and business tax cuts will stimulate job creation, innovation and investment, thereby boosting employment, growth and purchasing power. In the interest of social justice, the Pact will also include targeted reductions in the tax burden on the least well-off households to increase their purchasing power. Finally, the government deficit will be reduced, while maintaining funding for government priorities.

The steps set out in detail in this Stability Programme are a continuation of the recovery strategy that the government has applied since 2012.

These efforts will reduce the deficit steadily so that public finances are structurally balanced by the end of President Hollande's term in keeping with the commitments he made. Under the measures already implemented, a total structural adjustment of 2.2 points of GDP was achieved in 2012-2013, the nominal government balance improved by 1 point of GDP to 4.3 points in 2013 compared to 5.2 points in 2011. The measures presented in this Stability Programme for 2014 and for 2015-2017 build on these consolidation efforts. Fiscal consolidation was primarily underpinned by revenue measures in 2012 and 2013; adjustments will now come through government expenditure savings to stabilise the tax burden in 2014 before reducing it in 2015.

The Government will introduce further savings measures in 2014 to limit any deviations from the path set out in the third quarter of 2013. These measures will help offset the larger-than-expected drop in revenues in 2013 and 2014, which has reduced the elasticity of aggregate taxes and social security contributions. However, the targets have been revised and the 2014 deficit is expected to stand at 3.8% of GDP followed by 3% in 2015, compared to 3.6% and 2.8% respectively in the latest forecasts.

The savings plan unveiled by the Prime Minister on 16 April 2014 **will reduce the government deficit to 3% of GDP in 2015 and bring public finances into structural balance by the end of the period covered by the Programme in keeping with France's medium-term objective.**

www.parlament.gv.at

Table 2 – Multiyear public finance adjustment path

(As a % of GDP)	2012	2013	2014	2015	2016	2017
Government balance	**-4.9**	**-4.3**	**-3.8**	**-3.0**	**-2.2**	**-1.3**
Cyclical component	-0.8	-1.4	-1.7	-1.6	-1.3	-0.9
One-off and other temporary measures (as a % of potential GDP)	-0.1	0.0	0.0	-0.1	-0.1	0.0
Structural balance (as a % of potential GDP)	-4.0	-2.9	-2.1	-1.2	-0.8	- ¼
Structural adjustment	1.1	1.1	0.8	0.8	0.5	0.5
Real growth rate of government expenditure (% change)	1.2	1.3	0.3	-0.3	0.3	0.2
Aggregate taxes and social security contributions	45.0	45.9	45.9	45.6	45.4	45.3
General government expenditure	56.7	57.1	56.7	55.6	54.6	53.5
Government debt	90.6	93.5	95.6	95.6	94.2	91.9
Government debt excluding financial support for the euro area	88.2	90.4	92.4	92.5	91.2	89.0

The savings plan announced maintains our priorities, especially in relation to helping young people by creating new jobs as planned in the education, security and justice sectors. The savings will bring government expenditure growth into line with the inflation rate between 2015 and 2017, leading to a reduction in government expenditure by more than three points of GDP between 2014 and 2017 from 56.7% in 2014 to 53.5% in 2017. Initial measures implemented in 2012 and 2013 have already had an impact, as shown by central government expenditure which was €0.1 billion under its target in 2013, and by health insurance expenditure which was under its national target by €1.4 billion (so called "Ondam"). In addition, the growth of general government expenditure slowed sharply in 2013, to reach its lowest point since 1998.

Expenditure savings seen in 2013 will be consolidated in 2014 on top of the savings on unemployment insurance agreed by management and labour representatives. Combined with new measures to be announced before the third quarter, including central government budget cancellations and a one-year stabilisation of certain benefits in nominal terms, they will result in an additional net savings of €4 billion.

All of the general government sectors will share the burden and do their part to ensure the success of the €50-billion savings plan between 2015 and 2017. Central government will contribute €18 billion in savings through structural streamlining efforts, efficiency gains in IT systems, procurement, etc. and a more modest standard of living. During the previous President's term, central government agencies saw a substantial increase in their resources. Their operating expenditure and actions will be trimmed in line with those of central government. The government's wage bill will be kept in check by stabilising the civil service pay scale. Local government will contribute savings of €11 billion, bringing its expenditure growth into line with inflation. The bill clarifying France's local government structure will contribute to expenditure savings by eliminating the *clause générale de compétence* (principle by which local authorities can act in areas for which they are not responsible as of right) for *départements* and regions. The general operating grant ("*dotation globale de fonctionnement*") will be reformed to encourage better practices. The *Conseil national d'évaluation des normes* will endeavour to reduce the cost of ensuring compliance with existing regulations and will monitor the new ones.

The health insurance system will contribute savings of €10 billion through the implementation of the national healthcare strategy without decreasing the quality of care or coverage. Other social protection expenditure will contribute another €11 billion in savings. The reforms that

have already been adopted account for nearly €3 billion in savings, including measures affecting basic and supplementary pension schemes, and family policies. The March 2014 agreement between labour and management representatives on the unemployment insurance system will begin to have an impact. At the end of the period, the agreement will need to be supplemented to bring the system's finances into balance with total savings of €2 billion. The one-year stabilisation of benefits (excluding minimum social benefits), will start having an impact in October 2014, producing savings of more than €2 billion, including €1.3 billion on basic retirement pensions. Supplementary pension schemes will continue their ongoing efforts to achieve financial equilibrium, with savings of €2 billion, and family policies will be streamlined with savings of €0.8 billion. These efforts to improve efficiency by reorganising and streamlining social protection management will have an impact for all government departments, generating savings of €1.2 billion. The one-off increase in the RSA income support supplement has been upheld but deferred for one year.

Savings plan	Total for 2015-2017 in € billions
Central government	18.0
Local government	11.0
Health insurance	10.0
Social security reforms already initiated	2.9
Supplementary measures affecting benefits and social protection management	8.1
Total savings plan	**50.0**

These measures will lead to a substantial and lasting reduction in government expenditure growth in real terms. The inflation-adjusted government expenditure growth will stand at 0.3% in 2014 and average 0.1% between 2015 and 2017, compared to 1.1% in 2012 and 1.3% in 2013.

Cuts in taxes and social security contributions under the Responsibility and Solidarity Pact will lower the tax burden from 45.9 points of GDP in 2013 and 2014 to 45.3 points of GDP in 2017.

The Responsibility and Solidarity Pact combined with the growing impact of the Competitiveness and Employment Tax Credit introduced in 2012 will reduce labour costs by €30 billion. The Pact will boost the competitiveness of French companies and create hundreds of thousands of new jobs by the end of the President's term (see Box 9). The reduction in employers' social security payroll contributions is the first part of the Pact. Starting in 2015, the exemptions granted to employers on wages up to 1.6 times the minimum wage will be extended so that employers no longer pay any social contributions for minimum-wage employees other than unemployment insurance premiums, and the general scale of reductions will be reviewed.

Family allowance contributions on jobs paying up to three and a half times the minimum wage will be reduced by 1.8% on 1 January 2016 to enhance the competitiveness of French companies in export markets. All in all, the new reductions in employers' contributions will reduce labour costs by €9 billion. Self-employed workers and artisans will see their family allowance contributions cut by a total of €1 billion. The second part of the Pact deals with business taxes, which will also be reduced. The corporate social solidarity contribution (C3S) will be cut by €1 billion starting in 2015 and phased out entirely by 2017, lowering taxes by €6 billion. The exceptional corporate income tax payment for large corporations will be phased out in 2016 and

www.parlament.gv.at

the standard rate of corporate income tax will be lowered to 28% in 2020, with an intermediate cut in 2017.

Contributions will be cut for minimum-wage workers to increase their disposable income. The cuts will be degressive for workers earning up to 1.3 times the minimum wage. For minimum-wage workers, these cuts will increase their annual take-home pay by €500, which is equivalent to approximately an extra half-month's pay. **Taxes will also be cut for low-income households,** amounting to €5 billion in cuts by 2017. These measures will boost the purchasing power of low-wage workers and lead to higher consumption.

The reduction of the government deficit will stabilise the government debt ratio starting in 2015. Government debt levels will then start to shrink substantially in 2016 for the first time in more than ten years, falling to 91.9 points of GDP by 2017.

3.2 Outturn 2013

On 31 March 2014, France's national statistics institute (INSEE) published the preliminary general government accounts for 2013, showing a deficit of 4.3% of GDP in 2013 (€87.6 billion). This was €2.7 billion greater than the deficit forecast underpinning the 2014 draft budget of 4.1% of GDP, primarily as a result of the local government deficit which outstripped the forecast by 0.2% of GDP.

The 2013 outturn confirmed that expenditure was under control, with the smallest increase in nominal terms since 1998, except in the case of local government. The outturn also showed that the natural rate of growth of revenues was less favourable than expected.

The expenditure growth rate of 1.3% in real terms and 2.0% in nominal terms was around 0.5 pp lower than the draft budget forecast of 1.7% in real terms and 2.5% in nominal terms. The under-spending can be explained by lower interest expenditure in the national accounts, as well as under-spending by different general government sub-sectors, with the exception of local government.

Taxes and contributions were some €7 billion less than forecast in the draft budget. The bulk of this contraction of revenue can be attributed to corporate and personal income tax revenue, which was down by nearly €5 billion. The aggregate elasticity of taxes and contributions should stand at 0.2 in 2013 compared to the forecast of 0.4 in the 2014 draft budget.

The revised government deficit for 2013, and the concomitant downward revision of expenditure and revenue, affected the estimates for the measures undertaken to meet the deficit-reduction commitments. As explained in detail in Section 4.1, the reported data show sufficient structural adjustment, as defined by the Commission[8], to comply with the recommendation made to France in June 2013.

[8] The notion of structural adjustment computed is similar to that of structural effort, both on the expenditure and the revenue side.

www.parlament.gv.at

3.3 Public finance path under the no-policy-change scenario and trend path

In accordance with the requirements of the revised Stability and Growth Pact, this Stability Programme outlines a no-policy-change scenario, i.e. the changes in the government balance that would occur based on constant legislation and budget policy. This scenario incorporates the developments stemming from existing laws and regulations, but does not factor in the measures still to be implemented to meet the public finance targets.

This programme uses the following assumptions to construct the no-policy-change scenario.

- The scenario considers revenue and expenditure measures already passed ("no legislative change") under all legislation that has an impact on public finances and, more specifically, under previous Budget Acts, Social Security Budget Acts and Public Finance Planning Acts. For this programme, therefore, the scenario includes the effects of measures introduced by the 2013 and 2014 Initial Budget Acts, the 2013 and 2014 Social Security Budget Acts, the 2012 and 2013 Supplementary Budget Acts and previous Budget Acts, along with the expenditure rules set out in the 2012-2017 Public Finance Planning Act that Budget Acts passed since then comply with. More specifically, this Act includes ambitious objectives for central government expenditure and for expenditure covered by the national healthcare expenditure growth target (Ondam). Both have proven to be effective instruments for containing expenditure.
- The scenario also assumes no change in usual budget policies, such as index-linking of benefits (family benefits, pensions, etc.) and tax rates. It also incorporates statistically observed patterns, such as that of the local government balance over the election cycle (including capital expenditure and local direct tax rates).

In contrast to the adjustment path under this Stability Programme, the no-policy-change scenario does not incorporate measures introduced after the 2014 Budget Act, other than the changes already in place, such as the Responsibility and Solidarity Pact.

This Stability Programme also presents a **trend adjustment path** for the deficit that shows the natural growth rates of government revenue, healthcare expenditure and central government expenditure. This path is different from the no-policy-change path in that it does not factor in the efforts made to comply with fiscal requirements or the measures introduced after July 2012. When we strip these out, the deficit would stand at 5% of GDP in 2017.

www.parlament.gv.at

Table 3 - Multiyear Public finance adjustment path

As a % of GDP	2013	2014	2015	2016	2017
Trend path (before measures introduced after July 2012)	**-6.5**	**-6.7**	**-6.4**	**-5.9**	**-5.1**
Compliance with the expenditure rules	0.7	1.2	1.5	1.8	2.0
Discretionary revenue measures since May 2012 (including the 2014 Initial Budget Act and the Competitiveness and Employment Tax Credit, and excluding the Responsibility and Solidarity Pact and tax disputes)	1.5	1.4	1.3	1.3	1.2
Expenditure savings (including the 2013 retirement pension reform and agreement on supplementary pension schemes)	0.0	0.2	0.3	0.3	0.3
No-policy-change scenario	**-4.3**	**-4.0**	**-3.2**	**-2.5**	**-1.6**
Increased effort compared to the Multiyear Public Finance Planning Act and the 2014 Initial Budget Act		0.2	0.2	0.3	0.3
o.w. expenditure savings beyond the expenditure rules		*0.2*	*0.6*	*0.9*	*1.2*
o.w. Responsibility and Solidarity Pact: cuts in taxes and social security contributions		*0.0*	*-0.3*	*-0.6*	*-0.9*
Target adjustment path	**-4.3**	**-3.8**	**-3.0**	**-2.2**	**-1.3**

The 2014 no-policy-change scenario forecasts a deficit of 4.0%. The target adjustment path incorporates some €4 billion of the savings announced to ensure full compliance with our commitments.

In 2015 and beyond, the no-policy-change scenario incorporates compliance with central government expenditure rules and with the national healthcare expenditure growth target set in the 2012-2017 Public Finance Planning Act. It also includes the expenditure savings provided for in the aforementioned Act to finance the Competitiveness and Employment Tax Credit, along with the discretionary revenue measures in the Budget Acts passed since the third quarter of 2012. The target adjustment path also includes the cuts in taxes and social security contributions introduced under the Responsibility and Solidarity Pact between 2015 and 2017, along with the savings efforts made in addition to those set out in previous expenditure rules.

3.4 Structural budget balance

In 2013, the government deficit shrank by 0.6 points of GDP from 4.9% to 4.3%. The structural effort was considerably higher at 1.6 points of GDP. Most of the reduction resulted from revenue measures in the 2013 and 2014 Budget Acts which accounted for 1.4 points of GDP, and from expenditure savings which accounted for 0.2 points of GDP, corresponding to 2.0% growth in nominal expenditure which turned out to be less of an effort than expected given the very low inflation rate (the GDP price deflator stood at 1.1%). The low elasticity of revenue (contributing -0.5 points of GDP) reduced the "structural" adjustment to 1.1 points of GDP.

Furthermore, the persistently sluggish economy led to a deepening of the cyclical component of the deficit of 0.6 points of GDP as GDP growth of 0.3%[3] fell short of its potential 1.4%. One-off developments helped bring about an improvement in the government deficit of 0.1 point, as a result of no longer having to bail out Dexia (see Box 3).

In 2014, the reduction in the government deficit by 0.5 points of GDP will be achieved through a major expenditure savings effort contributing 0.7 points of GDP. This effort will rely on compliance with nominal spending rules, including stabilisation of central government expenditure excluding interest payments and pensions, and a 2.4% increase in the national healthcare expenditure growth target. Savings will also be achieved through retirement pension reform and the management-labour agreements on supplementary pension schemes and the unemployment insurance scheme, as well as further savings measures that the government will introduce before the third quarter. Measures to increase revenues will account

[3] Adjusted for seasonal variations and working days.

www.parlament.gv.at

for only a small share of the deficit reduction (0.1 points of GDP). Furthermore, ongoing tax disputes will not affect the government deficit in 2014, and the contribution of the non-discretionary component will be only slightly negative.

In 2015, implementation of a substantial portion of the €50-billion savings plan (see Box 4) will reduce expenditure by 0.9 points of GDP. This will reduce the government deficit and make it possible to finance a preliminary cut in taxes and social security contributions under the terms of the Responsibility and Solidarity Pact, contributing -0.2 points to the structural adjustment. This would produce a structural adjustment of 0.8 points of GDP and improve the deficit in nominal terms by the same margin. A slight improvement in the output gap (1.7% actual growth compared to 1.5% potential growth) will be offset by one-off developments that will strip -0.1 points of GDP from the adjustment to the government balance. These include developments in UCITS and withholding tax disputes (see Box 3)

In 2016 and 2017, the deficit is expected to fall by 0.8-0.9 points of GDP per year. Most of the reduction will come from ongoing expenditure savings equivalent to around0.6 points of GDP per year. Under the terms of the Responsibility and Solidarity Pact, taxes and social security contributions will contribute an average of -0.2 points of GDP to the net structural adjustment of 0.5 points of GDP per year. In addition, the government will take measures under the terms of the Pact that will boost growth over and above its potential (2 ¼ % per year). The cyclical component of the deficit is expected to be reduced by 0.3-0.4 points of GDP. Finally, the after-effects of the tax disputes will be favourable in 2017 (see Box 3). On the whole, the structural deficit is expected to reach ¼ points of GDP by the end of the period covered by the Programme.

Table 4 - Structural balance adjustment path and breakdown of structural adjustment

As a % of GDP	2013	2014	2015	2016	2017
Government balance (1)	-4.3	-3.8	-3.0	-2.2	-1.3
Cyclical component (2)	-1.4	-1.7	-1.6	-1.3	-0.9
One-off and other temporary measures (as a % of potential GDP) (3)	0.0	0.0	-0.1	-0.1	0.0
Structural balance (as a % of potential GDP) (1)-(2)-(3)	**-2.9**	**-2.1**	**-1.2**	**-0.8**	**-¼**
Structural adjustment	1.1	0.8	0.8	0.5	0.5
Structural effort	1.6	0.8	0.8	0.4	0.4
Discretionary revenue measures	*1.4*	*0.1*	*-0.2*	*-0.2*	*-0.2*
Effort in expenditure	*0.2*	*0.7*	*0.9*	*0.6*	*0.6*

Box 2 – Planned corrective measures

In its 5 March 2014 Recommendation, the European Commission estimated on the basis of its Winter 2014 forecast that the deviation from the recommended structural adjustment path would be approximately 0.2 points of GDP in 2013 and 2014 based on the corrected structural adjustment forecast or the "bottom-up" estimate of the fiscal effort. Since then, INSEE released exact data for 2013 on 31 March 2014. The data shows that expenditure was controlled more effectively than the Commission anticipated (see Section 4.1).

The Government decided to take additional corrective measures to achieve an additional adjustment of some €4 billion in the 2014 deficit.

The additional savings achieved in 2013 on expenditure covered by the national healthcare expenditure growth target (Ondam) will be consolidated in 2014 based on a new target that

www.parlament.gv.at

incorporates underspending, which turned out to be €0.75 billion greater than forecast in the 2014 Social Security Budget Act, or €1.4 billion underspend compared to the 2013 Social Security Budget Act. Increased expenditure savings will mean an additional effort of €0.75 billion for the health insurance system, since the Ondam passed by Parliament is stated in nominal terms. The €0.6-billion fall in expenditure on unemployment insurance benefits will also be consolidated in 2014.

In addition to these measures, all social benefits, except for minimum social benefits, will be stabilised in nominal terms for one year. The one-off increase of the RSA income support supplement by 2% more than the usual index-linked increase has been upheld, but deferred for one year. Together, these measures represent a gain of nearly €0.5 billion for public finances in 2014.

Furthermore, the Government will introduce a measure to benefit the least well-off households.

The labour-management agreement on the unemployment insurance system, along with additional savings measures focusing more specifically on central government and included in the supplementary draft budget to be submitted to Parliament before the third quarter will complete these measures and ensure compliance with the Council's June 2013 Recommendation.

Box 3 - One-off and other temporary measures taken into account when evaluating France's structural balance

France introduced a structural balance rule to implement the Treaty on Stability, Coordination and Governance. The structural balance corresponds to the government balance adjusted for direct cyclical effects and one-off developments. This rule avoids the pro-cyclical effects produced by managing government finances on the basis of the nominal government balance.

The following one-off developments and measures are not included in the structural balance under this Stability Programme in keeping with the method used in the 2012-2017 Public Finance Planning Act:

- **On the revenue side**, the amount of losses stemming from exceptional tax disputes. The year in which those losses will be recognised in the national accounts cannot be foreseen because it depends on the timing and the tenor of the courts' final rulings4. The disputes involve reimbursements to foreign UCITS and reimbursements of withholding tax on dividends paid5 (précompte mobilier).

- **On the expenditure side**, France's €2.6 billion recapitalisation of Dexia. This amount was recorded as a one-off in the 2012 government balance.

Table 5 – One-off and other temporary measures excluded from the structural balance under the national system of accounts

(deviation from baseline, in € billions)	2012	2013	2014	2015	2016	2017
Total	**-2.6**	**-0.3**	**-0.7**	**-2.7**	**-2.7**	**-0.5**
Revenue	0.0	-0.3	-0.7	-2.7	-2.7	-0.5
Withholding tax dispute (précompte mobilier)	0.0	0.0	0.0	-1.0	-1.0	0.0
UCITS dispute	0.0	-0.3	-0.7	-1.8	-1.8	-0.5
Expenditure (Dexia)	-2.6	0.0	0.0	0.0	0.0	0.0

NB: the figures given in this table do not predict the outcome of the disputes; they merely reflect the conservative approach to multiyear public finance projections. Furthermore, the figures shown are subject to change as a result of the courts' final rulings.

3.5 The government balance by sub-sector

Fiscal consolidation will be the result of joint efforts on expenditure by all general government sub-sectors over the programme period, as the economy recovers and leads to an upturn in revenue. Consequently, the government balance should improve by 3.0 points of GDP between 2013 and 2017 from -4.3% of GDP in 2013 to -1.3% of GDP in 2017.

[4] Expenditure and revenue are recorded on an accrual basis in the system of national accounts in compliance with the European System of Accounts of 1995. This means they are recorded, "when economic value is created, transformed or extinguished, or when claims and obligations arise, are transformed or are cancelled". Consequently, the loss or gain from disputes will be recorded in the year when the courts make their final ruling, whereas, in budgetary accounting, it will be recorded on the basis of cash flows.

[5] Since the previous Stability Programme, France won its case before the European Union Court of Justice concerning taxes on electronic communications. The cost of potentially losing the case, which was recorded as a one-off when the Public Finance Planning Act was drafted, has consequently been withdrawn.

www.parlament.gv.at

FRANCE STABILITY PROGRAMME 2014-2017

Table 6 - General government lending capacity (+) / borrowing requirement (-)

% of GDP	2013	2014	2015	2016	2017
Government balance, Maastricht definition	-4.3	-3.8	-3.0	-2.2	-1.3
primary balance	*-1.9*	*-1.4*	*-0.5*	*0.4*	*1.4*
Central government	-3.3	-3.2	-3.1	-2.6	-2.0
Other central government bodies	0.1	0.1	-0.1	0.0	0.0
Local government	-0.4	-0.4	-0.2	-0.2	-0.2
Social security funds	-0.6	-0.2	0.3	0.6	1.0

NB: The balances shown in this table follow the Maastricht definition

The central government (central government and other central government bodies) borrowing requirement will fall by 1.1 points between 2013 and 2017 from 3.2% of GDP in 2013 to 2.1% in 2017. The reduction will stem primarily from the rules governing the growth of central government expenditure excluding debt servicing and pensions. The central government's total effort for the period from 2015 to 2017 will amount to €18 billion. The bulk of the savings will come from efficiency gains (pooling of procurement and IT functions, moderating central government standard of living, refocusing government action and stabilising the civil service pay scale); other central government bodies will see their operating expenditure and scope of intervention trimmed. The share of central government expenditure in GDP will decline sharply. The budgets of other central government bodies will be nearly balanced by 2017.

The social security balance should improve by 1.6 points of GDP between 2013 and 2017, going from a deficit of 0.6 points of GDP to a surplus of 1.0 point of GDP at the end of the period. In addition to the impact of the revenue measures introduced in 2012 and 2013, most of the improvement will come from the consolidation and increase of the savings achieved on expenditure covered by the national healthcare expenditure growth target (Ondam), which will contribute €10 billion in reduced expenditure between 2015 and 2017, from reform of basic and supplementary retirement schemes and from reform of family benefits in 2013, as well as from the labour-management agreement on the unemployment insurance system signed in March 2014. Further reform of these sectors, with the new agreement on the unemployment insurance system to help it reach financial equilibrium, continuing consolidation of supplementary retirement schemes and reform of family policy, combined with the one-year stabilisation of social benefits, other than minimum social benefits, savings achieved by social protection bodies through reorganisation and streamlining of benefits management, will reduce social benefits expenditure, other than that covered by Ondam, by €11 billion between 2015 and 2017 (see below). On the revenue side, the issue of compensating social security funds for the cuts in social security contributions under the Responsibility and Solidarity Pact will be dealt with in upcoming budgets. Furthermore, payrolls will grow more quickly as new jobs are created under the Responsibility and Solidarity Pact.

Local government will also take part in the adjustment effort, saving €11 billion between 2015 and 2017. This effort will result primarily from a cut in central government transfers, with an initial cut of €1.5 billion in 2014 following a stabilisation in 2013. The local government deficit will shrink from 0.4% of GDP to 0.2% by the end of the programme period. This improvement will primarily be attributable to the election cycle, since newly-elected local governments usually rein in capital expenditure early in their term. In addition, their operating expenditure will fall in accordance with the Government's structural reforms. Overall, expenditure growth should be in line with inflation.

www.parlament.gv.at

3.6 Government expenditure

3.6.1 General government expenditure

Table 7 – Change in real general government expenditure by sub-sector

(annual average, in real terms and in %*)	2013	2014	2015-2017
General government	**1.3**	**0.3**	**0.1**
Central government (APUC)	-0.2	-0.4	-0.9
Local government (APUL)	2.7	0.5	-0.3
Social security funds (ASSO)	1.7	0.6	0.3

** Expenditure in real and like-for-like terms, including transfers between general government sub-sectors.*

Expenditure growth features efforts by all general government sub-sectors throughout the 2014-2017 period. Government expenditure increased by 2.0% in nominal terms in 2013, which is markedly slower than the growth of 3.0% posted in 2012. In real terms, the growth rate of government expenditure stood at 1.3% as inflation was low (as measured by the consumer price index excluding tobacco which rose by 0.7%). **As savings efforts intensify and inflation gradually picks up again, expenditure growth should slow to 0.3% in real terms in 2014 and average 0.1% per year over the 2015-2017 period.**

Expenditure growth in nominal terms slowed sharply in 2013, falling from 3.0% to 2.0%, and was slower than expected in relation to the 2014 draft budget projection of 2.5%. The savings were achieved in all general government sub-sectors, except local government. Central government expenditure was €0.1 billion less than the forecast underpinning the 2014 draft budget and expenditure covered by the national healthcare expenditure growth target grew by 2.4% from one fiscal year to the next, compared to the target of 2.7%, €1.4 billion less than the target set in the 2013 Social Security Budget Act. The factors that contributed to expenditure growth in 2013 included the local government capital expenditure cycle, even though capital expenditure grew more slowly during the 2008-2013 cycle than the previous cycle. General government interest expenditure contracted sharply in 2013, largely as a result of persistently low interest rates.

In 2014, a sharp slowdown in expenditure growth to 1.4% in nominal terms and 0.3% in real terms will stem from savings measures and spontaneous factors, including control of local government expenditure through a €1.5 cut in funding in 2014 following a stabilisation in 2013, the initial impact of pension reform and the 2013 agreement with the supplementary pension schemes. Local government capital expenditure should grow at a much slower pace in keeping with the normal pattern for election years. Lastly, additional measures in the supplementary draft budget to be submitted to Parliament before the third quarter will include labour-management agreements on the unemployment insurance system as well as supplementary savings measures which focus on central government.

Government expenditure growth between 2015 and 2017 will be virtually nil in real terms. The growth rate will be much lower than the potential growth rate because of a fiscal consolidation effort based entirely on expenditure measures. It will also be much lower than the past trend.

www.parlament.gv.at

The continuing fall in expenditure growth will result from measures already introduced and those presented in this Stability Programme, which will bring the total amount of additional savings over the programme period up to €50 billion. Local government will rein in its expenditure growth as a result of an aggregate cut of €11 billion in transfers over three years. Local capital expenditure growth will be at its lowest in 2015, the year after the municipal elections. In addition, central government savings will bring the aggregate total to €18 billion. The social security sector will make a significant contribution to expenditure savings on top of the measures relating to healthcare expenditure to be implemented in 2014. The national healthcare expenditure growth target will be capped at an average of 2.0% over the next three years, representing aggregate savings of €10 billion. Savings on benefits and operating expenses will come to €11 billion in other areas of social security expenditure (see Box 4).

Box 4 – 2015-2017 detailed plan for savings of €50 billion

In accordance with the announcement made by President Hollande on 14 January 2014, the Prime Minister presented details of the plan to reduce government spending by €50 billion between 2015 and 2017 to the Cabinet on 16 April 2014. The plan will ensure that the Responsibility and Solidarity Pact is implemented in compliance with France's government deficit reduction commitments. The savings efforts will be shared by the different sectors of general government, including central government and central government bodies, local government and social security bodies

Central government and central government agencies will contribute savings of €18 billion by stabilising the civil service pay scale, refocusing central government action and, more generally, through efficiency gains and pooling of support functions, along with a more modest standard of living for central government. A special effort to streamline the central government's real property holdings will speed up property sales and reduce related expenses. Central government agencies will do their share, with reduced human and financial resources over the programme period.

Central government transfers to local government will be reduced by €11 billion by 2017. This reduction will be backed up by structural reforms to make the cuts sustainable: reform of the general operating grant in 2015; abolition of the *clause générale de compétence*, an additional expense due to overlapping functions between *départements* and regions; reduction in the number of regions; increase in the size of intermunicipal structures and a sharp fall in the number of authorities managing them. A debate will take place regarding the future of *département* councils, and the cost of implementing regulations will also be more tightly controlled.

Health insurance savings of €10 billion will be achieved through the implementation of the national healthcare strategy, by promoting more efficient expenditure via structural reforms, such as the streamlining of treatments, greater use of outpatient care and increasing the share of generic drugs consumed. The national healthcare expenditure growth target for 2015-2017 is an average of 2.0% per year.

Other social protection expenditure will contribute €11 billion in savings. Decisions made in 2013 concerning the reform of basic and supplementary pensions and family benefits will produce savings of €2.9 billion. The one-year stabilisation of social benefits, except for minimum social benefits, will produce additional savings of €2 billion, including €1.3 billion on basic pension benefits and €0.7 billion on other social benefits. Continuing labour and management discussions to restore supplementary pension schemes to equilibrium and similar efforts in relation to other pension schemes should produce an additional €2 billion in savings.

The unemployment insurance system should achieve savings of €2 billion by 2017; the labour-management agreement signed in March 2014 has already set out the initial measures in this direction. Continuing reform of family benefits will produce savings of €0.8 billion. Social protection bodies will realise savings of €1.2 billion on operating expenditure through electronic document management and better coordination of actions between the different bodies. This will also improve service quality for users and streamline management of the social protection system.

A substantial share of the €50 billion in savings, i.e. some €21 billion, will be achieved in 2015, making it possible in that year to finance the cuts in taxes and social security contributions announced as part of the Responsibility and Solidarity Pact without deviating from the path of a steady reduction in government deficits. Aggregate savings in 2016 will reach €37 billion and the target of €50 billion will be reached in 2017.

www.parlament.gv.at

Box 5 – The Government Expenditure Strategy Council

At the same time as the budget procedure was being reviewed, a Government Expenditure Strategy Council was instituted by a decree dated 22 January 2014. The Council's task is to "propose and monitor the structural savings programme set out in France's Stability Programme".

The Council is chaired by the President of the Republic and includes the Prime Minister, the Minister for Finance and Public Accounts, the Minister for the Economy, , the Minister for Social Affairs and Health, the Minister for Employment, the Minister for State Reform, Decentralisation and the Civil Service, and the Minister of State for the Budget.

The Council has **examined all potential savings, including savings in local government and social security expenditure. This means that the structural decisions required to achieve at least €50 billion in savings by 2017, which are set out in this Stability Programme, were made at the highest level of government.**

The Council's decisions will be implemented by the Government and incorporated in the next Public Finance Planning Act as part of the public finance planning exercise. The decisions will also soon be incorporated into the preliminary budget ceiling letters sent to ministers as part of the revamped forward-looking budget procedure introduced in 2014.

3.6.2 Central government expenditure

The "zero nominal growth rule", which exempts debt servicing and pensions, has helped to control both budgeted and actual central government expenditure

The central government's budget is drawn up and executed according to the "**zero nominal growth**" rule. Article 6 of the 2012-2017 Public Finance Planning Act of 31 December 2012 upholds this rule. Under this rule, the sum of general budget appropriations, levies on revenue and revenue earmarked for third parties, excluding debt servicing and pensions, must be **stable or shrink in current euros**. This rule applies to the central government's discretionary expenditure. Furthermore, the annual increase in aggregate general budget expenditure, including debt servicing and pensions (budget appropriations, levies on revenues and earmarked revenue), must be no higher than inflation ("zero real growth" rule).

The combined effect of these two rules ensures that any fall in the cost of servicing central government debt or any savings made from pension reform are not reallocated to finance long-term expenditure but used entirely to help with fiscal consolidation efforts. On the other hand, if discrepancies in inflation, debt and pension forecasts make it impossible to meet the overall ceiling on aggregate expenditure, and even though appropriations "excluding debt servicing and pensions" might be flat or decreasing in nominal terms, the ceiling on ministries' budget appropriations will still be lowered to keep aggregate expenditure growth in line with inflation.

Total central government expenditure in 2013 was €3.4 billion lower than the target set at the beginning of the year as a result of favourable conditions for debt servicing and inflation.

The nominal target for central government expenditure of €279.4 billion was fully met despite particularly challenging conditions for budget execution. Expenditure, excluding debt servicing and pensions, came in at €0.1 billion below the target, even though the increase in France's contribution to the European Union budget strained spending limits. The €1.1 billion increase in

France's contribution to the European Union budget (excluding one-off refinancing requirements), was offset against central government expenditure savings during the fiscal year through tighter control of spending by ministries. A total of nearly €3 billion in appropriations to reserves made at the beginning of 2013 were cancelled.

Spending reductions will be intensified under the 2012-2017 central government expenditure plan to achieve structural equilibrium for public finances

For the first time, **the 2014 Initial Budget Act** includes a net spending cut of €1.5 billion excluding debt servicing and pensions.

According to the government's next three-year plan, the overall target for the 2015-2017 period is to reduce central government expenditure by €18 billion.

The revamped budget procedure (see Box 7) should lead to better and more sustainable budget planning, drafting and execution through greater involvement of the ministries in identifying potential savings and in sustainable public finances management.

The goal of an €18 billion reduction in central government expenditure will require a joint effort by the different government sub-sectors. This goal was set with a view to improving the efficiency of government expenditure wherever possible. It will be strictly enforced when drafting and executing future Budget Acts and is critical for restoring public finances to structural equilibrium.

Box 6 – Expenditure savings by central government and central government agencies

Central government and central government agencies will fully participate in the fiscal consolidation efforts. The goal is to achieve savings of €18 billion by 2017.

The planned efforts will start with structural reforms to safeguard the quality of public services.

- The savings will rely on keeping a check on ministries' operating expenditure. They will require savings to be made on real property expenses, the pooling of support functions (procurement and information systems), and a more modest standard of living for central government.

- Civil servants will contribute to the savings effort required through the continuation of the stabilisation of the civil service pay scale.

- The creation of new jobs planned in the education, security and justice systems will be upheld as part of the Government's decision to give priority to young people and the security of French citizens.

- Central government action will also be refocused for greater efficiency.

- The operating expenditure and scope of intervention of central government bodies and agencies will be trimmed following a 15% increase in their resources during the previous President's term.

Box 7 – The revamped budget procedure

Compliance with our ambitious adjustment path for public finances, which has no precedent in France's recent financial history, will require an effective budget procedure that facilitates policy decisions and choices to achieve sustainable structural savings.

www.parlament.gv.at

The previous Government decided during the preparations for the 2015-2017 three-year budget to revamp and shorten the budget timetable starting in 2014. The new budget procedure was supposed to give ministries an active role in identifying and achieving structural and sustainable savings.

The budget guidelines issued by the Prime Minister in early May will provide more specific information about the amount of the savings required by each minister in 2015-2017. It will be the ministers' responsibility to propose reforms in order to achieve the savings required, based in part on the work done as part of the ongoing spending review (*modernisation de l'action publique* or MAP) by interministerial audit teams and the French Government Audit Office (*Cour des comptes*). Joint technical work by their ministries will help them in their task. The new procedure highlights the principle of accountability and co-budgeting between ministries.

In June, after a conventional decision-making process, the Prime Minister will send budget ceiling letters to the ministers setting out the appropriations for each ministry and the guidelines for the next three-year budget. These guidelines will then be presented to Parliament at the end of June, during the public finance policy debate.

Box 8 - Yield assumptions and changes

France enjoyed very favourable borrowing terms in 2013, despite the slight rise in short-term yields seen at the end of the year and highly volatile long-term yields, which rose sharply in the second quarter. Yields at issue for short-term securities (BTFs) averaged 0.06% in 2013 compared to 0.08% in 2012, and yields at issue for securities with maturities of more than one year (OATs) averaged 1.54% compared to 1.86% in 2012.

Since the beginning of 2014, and in contrast to market expectations, the trend in short-term yields remained stable, with yields at issue close to 0.2% for BTFs. Medium-term and long-term yields fell, with yields at issue for 10-year securities dropping from 2.51% in early January to 2.15% in early April 2014.

The yield trend underlying the forecast is based on a scenario where yields gradually rise to their pre-crisis levels. Between 1998 and 2007, the 3-month BTF yield averaged 3.05% and the 10-year OAT yield averaged 4.45%. This scenario is consistent with the expected resumption of growth and a rise in inflation to a level close to the ECB's objective of 2% by 2017.

Table 8 – Yield forecasts

End of year levels (forecasts)	2014	2015	2016	2017
Short-term yields (3-month BTFs)	0.25%	0.50%	1.00%	1.50%
Long-term yields (10-year OATs)	2.75%	3.25%	3.75%	4.25%

In this scenario, short-term yields (3-month BTFs) would rise very slightly to reach 0.25% at the end of 2014, which is the current level of the ECB refinancing rate. Then, they would rise again towards the end of 2015 in the expectation that the ECB will adopt a more standard monetary policy as the euro area economy recovers. After that, they are projected to rise by 50 basis points per year.

The long-term yield (10-year OATs) of 2.75% forecast for the end of 2014 factors in the potential repercussions of a rise in long-term yields in the United States, as in the second quarter of 2013. After that, long-term yields are expected to follow the same trend as short-term yields, rising by 50 basis points per year.

www.parlament.gv.at

3.6.3 Expenditure of other central government bodies

Other central government bodies, most of which are also central government agencies[6], will contribute to efforts to control expenditure. After seeing a recent sharp rise in their expenditure[7], these bodies must present balanced annual budgets and are now more closely monitored. Consequently, their finances are almost in equilibrium. To this end, they are prohibited from borrowing money from credit institutions or issuing debt securities with maturities of more than 12 months[8]. This prohibition helps control their expenditure.

In 2015-2017, the government will take steps to streamline the central government agencies, one of the main thrusts of its programme. This is likely to result in the merger or even the closure of some establishments, a reduction in their staffing levels and appropriations (subsidies for public service provision and earmarked taxes) and, ultimately, tighter oversight of earmarked taxes or possibly their integration into the central government budget in keeping with the guidelines outlined by the tax policy council *(Conseil des prélèvements obligatoires*) in a recent report commissioned by the government[9]. At the same time, in keeping with the targets that central government sets for its own operating expenditure, the operating expenditure and scope of intervention of central government agencies will be trimmed.

In 2013, other central government bodies' expenditure was kept under control, even though the interest paid on the contribution to the cost of public service in electricity owed to the French electricity utility (EDF) was recorded as an expense in the national accounts. Indeed, central government agencies' outlays under the Invest for the Future programme have increased slowly, and various measures affecting the agencies' resources have started to have an impact, offsetting this one-off interest expenditure. **In 2014**, other central government bodies' expenditure growth will slow slightly as a result of two contradicting factors. On the one hand, expenditure will include an outlay of €1.5 billion for the Defence Industry Excellence Initiative under the second phase of the Invest for the Future programme. On the other hand, the interest expenditure on the contribution to the cost of public service in electricity will no longer have to be paid.

Expenditure growth will then slow **in 2015** and remain steady in **2016 and 2017**, as the outlays under the Invest for the Future programme stabilise (see Section 6.1.2).

3.6.4 Social security funds' expenditure

In 2013, benefits paid by the social security funds grew by 3.0% in nominal terms, which was slightly slower than their 3.3% growth in 2012. This stems primarily from the slower growth of retirement pension benefits: 2.9% compared to 4.1% in 2012. It is also the result of an increase in

[6] The salient features of central government agencies are that they provide public services, are mostly financed by the central government and are under its direct control. The purview of central government agencies and that of other central government bodies is not exactly the same: the former are included in the budget while the latter are included in the system of national accounts and listed by INSEE each year.
[7] See, for example *L'État et ses agences*, Report 2011-M-044-01 by the Inspection générale des finances, March 2012.
[8] Article 12 of the 2011-2014 Public Finance Planning Act (which has not been repealed by the December 2012 Planning Act) prohibits them from incurring debt with maturities of more than twelve months, except for the Government Debt Fund (*Caisse de la dette publique*) and the Corporation for Central Government Equity Holdings (*Société de prises de participation de l'Etat*).
[9] *La fiscalité affectée : constats, enjeux et réformes*, July 2013.

www.parlament.gv.at

the retirement age and weak inflation, which limits benefit adjustments. The growth of health insurance expenditure was also particularly moderate: the expenditure covered by the national healthcare expenditure growth target was €1.4 billion below the target set in the 2013 Social Security Budget Act and €0.75 billion below the 2014 Social Security Budget Act target. In addition, unemployment benefits, which were expected to rise in 2013 by 5.7% in the draft budget, were €0.6 billion below target.

In 2014, the growth in benefit spending should slow even further, reaching 1.7% as family allowances are adjusted in line with the 2014 inflation forecast of 1.1% and the adjustment to the inflation forecast to take into account the discrepancy between the actual 2013 inflation of 0.7% and the inflation rate of 1.2% forecast in March 2013. In line with these correction mechanisms, family allowances were raised by 0.6% on 1 April 2014. The growth of old-age pensions should also drop from 2.9% to 2.2%, as supplementary pensions are stabilised on 1 April 2014 and basic pensions are not adjusted on 1 October 2014. Growth in unemployment benefits should decelerate as the job market improves and the March 2014 agreements come into force.

Between 2015 and 2017, growth in social benefit spending should remain moderate with an average of 2.1% per year. Much of this will be achieved through slower growth in healthcare expenditure as the national healthcare expenditure growth target will average 2.0% between 2015 and 2017. Unemployment benefits should decrease in nominal terms until 2017 as a result of the improved job market and of the measures taken to improve the finances of the unemployment insurance system under the labour-management agreement on unemployment benefits signed in March 2014. Further measures will be adopted to ensure the financial equilibrium of the system by 2017.

Table 9 – Annual nominal growth rate of social benefits

(nominal growth rate, %)	2013	2014	2015-2017*
Social insurance benefits	**3.0%**	**1.7%**	**2.1%**
Old age and survivor benefits	2.9%	2.2%	2.7%
Family allowances - Housing	2.4%	0.0%	0.2%
Unemployment	5.7%	-0.5%	-1.2%
National healthcare expenditure	2.4%	2.4%	2.0%

** Average annual growth rate 2015-2017*

Healthcare benefits

In 2013, the deceleration of healthcare expenditure growth observed since 2008 continued, leading to an undershooting of the national healthcare growth target set by Parliament by €1.4 billion corresponding to a 2.4% growth rate. The reform of the governance of the national healthcare expenditure growth target, namely a reduction in the warning threshold, the introduction of a new monitoring committee and an increase in the number of actions taken by the early warning committee helped meet the target for the fourth year in a row. This result is testimony to the government's efficient management of healthcare expenditure. The government has also backed this effort with structural action to improve the organisation of the healthcare system by elaborating a national healthcare strategy.

www.parlament.gv.at

The 2014 growth rate target has been set at 2.4%. To ensure this target is met, €2.4 billion in savings measures have been taken. These measures rely primarily on lower prices for healthcare products (€1.1 billion), actions to improve medical efficiency (€0.6 billion) and hospital savings (€0.4 billion).

In view of the underspending in 2013 and the early economic data reported at the start of 2014, the target for 2014, which had already factored in the undershooting of the original 2013 target by €650 million, should be met once again, as the warning committee announced on 11 April. Furthermore, the level of underspending in 2013 will be consolidated in 2014 to ensure that expenditure growth does not exceed2.4% in 2014, compared to the final outturn for 2013.

Between 2015 and 2017, expenditure growth covered by the national healthcare expenditure growth target will continue to decline, reaching a 2.0% growth rate average. Greater efforts to increase efficiency in the healthcare sector will be required to maintain this medium-term adjustment path. The priority for the Government under the national healthcare strategy initiated in 2013 is to improve treatment through the effective regulation of healthcare supply aimed at breaking down the barriers between outpatient care, hospital care and the healthcare and social services sector. The strategy also calls for enhanced preventive care and more accessible healthcare.

www.parlament.gv.at

Old-age benefits

The adjustment path presented here, with a 2.7% average increase in benefits between 2015 and 2017, includes the 6-month deferral of the basic pension adjustment in 2014 and the stabilisation of pensions until 1 October 2015. The adjustment path for supplementary pensions includes the measures taken under the labour-management agreement on supplementary pensions signed in March 2013. This means that pensions will rise by one percent less than inflation in 2014 and 2015. These measures should be supplemented in 2016 and 2017 to ensure continued consolidation of the pension system's finances.

Other social benefits

Family allowance and housing benefits expenditure grew by 2.4% in 2013. This slower rate of growth compared to 2012 (3.0%) stems from the one-off 25% increase in the back-to-school bonus that year. The nominal value of such benefits should remain the same in 2014 as a result of the adjustment of only 0.6% on 1 April 2014, in line with the 2014 inflation forecast and the correction for actual inflation in 2013. Growth will be limited to 0.2% per year on average between 2015 and 2017 with the continuation of the family policy reform started in 2013.

After very strong growth in 2013 (5.7%), unemployment insurance expenditure should start to slow as the job market improves Furthermore, the 2014 labour-management agreement and the supplementary measures that the system managers intend to take will help restore the system to equilibrium by 2017.

3.6.5 Local government expenditure

Local government expenditure growth should start to slow in 2014. A reduction in transfers to local government and improved local public finance governance will help to reduce expenditure through greater streamlining.

After a stabilisation of central government transfers to local government in nominal terms in 2013, these transfers will be reduced by €1.5 billion in 2014 and by a total of €11 billion between 2015 and 2017. In this way, local governments are contributing fully to the fiscal consolidation effort. The planned reduction of central government transfers over the entire programme period will encourage local government to make efficiency gains to control expenditure.

Several measures will be taken to assist local government efforts. New metropolitan areas have been created and direct election of intermunicipal council members through universal suffrage is already taking place. These measures will be powerful tools for streamlining government. Other measures will be part of the planned local government reform that the Prime Minister outlined in his general policy speech on 8 April 2014: defining powers by eliminating the *clause générale de compétence*, halving the number of regions so that they can attain critical mass, drawing up a new intermunicipal map based on community catchment areas. Finally, the future of *département* councils will be debated. At the same time, structural reform of the general operating grants, which total €40.1 billion in the 2014 Initial Budget Act, will begin in 2015 to ensure the long-term sustainability of the efforts that will be required of each local authority.

www.parlament.gv.at

In addition to this change in how funding is distributed, the President of the Republic called for an expert assessment of other local government expenditure governance measures by two former budget ministers, Alain Lambert and Martin Malvy, who have been given the task of presenting "*proposals for drafting a sustainable financial governance pact with local government*" with due consideration of "*the ways and means for better control of local government expenditure*". Very specific proposals were submitted to the President of the Republic on 16 April 2014. These proposals will inform the Government's work in the coming months.

Two points need to be made with regard to local government expenditure:

- Average growth in local capital expenditure was low between 2008 and 2013, averaging 1.3% per year in nominal terms[10]. In 2013, the year before municipal elections, capital expenditure grew by 5.2%. In keeping with the election cycle, capital expenditure should contract in 2014 by 2.5% and the decline should continue with a 6.9% fall in 2015, which will be the low point in the local cycle. It will start to recover in 2016 with moderate growth. In addition to the downward trend in local government capital expenditure over recent election cycles, investment projects will be selected more carefully because of the combined effect of reduced central government transfers and improved governance measures.
- The knock-on effects of some of the savings measures announced by the Prime Minister will facilitate control of local government expenditure. This is particularly true of the stabilisation of the civil service pay scale, which is used as the basis for calculating the compensation of local civil servants.

Total local government expenditure averaged over the period from 2014 to 2017 will be flat in real terms.

[10] The underlying growth rates are calculated using Base 2010 data from year 2010 on. Data for previous years is compiled using base 2005 data.

www.parlament.gv.at

3.7 Government revenue

3.7.1 General government revenue

After increasing by nearly one point of GDP between 2012 and 2013 as a result of discretionary revenue measure, the aggregate tax and social security contribution rate should decline to 45.3% of GDP in 2017.

This forecast factors in the impact of all of the measures in the Initial Budget Act following the review by the Constitutional Council, along with the measures in the Responsibility and Solidarity Pact.

The *aggregate tax and social security contribution rate* **will be stable between 2013 and 2014 at 45.9% of GDP.** The aggregate elasticity of taxes and social security contributions should be less than one (0.9) while the impact of measures already passed but that will take effect gradually should be slightly positive at 0.1 points of GDP. These discretionary measures are designed to ensure the sustainability of France's social model, to boost competitiveness, growth and jobs, and to enhance the progressiveness of taxation and green taxes. Furthermore, under the Responsibility and Solidarity Pact, a reduction in taxes and social security contributions for low-income households will take effect in 2014.

The *aggregate tax and social security contribution rate* **will decline each year starting in 2014 to reach 45.3% of GDP in 2017.** This decline will stem from the Responsibility and Solidarity Pact, which will extend the reduction of labour costs initiated by the Competitiveness and Employment Tax Credit, lower business taxes and even eliminate some "minor taxes" that complicate life for businesses, and enhance the purchasing power of low-wage workers. The adjustment path also incorporates:

- the impact of retirement pension reform.
- the phasing in of green taxes to promote the transition to cleaner energy.
- the increase in the contribution to the cost of public service in electricity, in line with the commitment to eliminate the past deficits on this item.
- the impact of the election cycle on the rates of taxes allocated to local government.
- outlays related to tax disputes.

The adjustment path is based on a natural growth rate for tax revenues in line with GDP growth (tax elasticity equal to one between 2015 and 2017).

Furthermore, non-tax revenue should remain steady at 7.2% of GDP between 2013 and 2017.

Table 10 - Tax burden

	2012	2013	2014	2015	2016	2017
Aggregate tax and social security contribution rate (as a % ofGDP)	**45.0**	**45.9**	**45.9**	**45.6**	**45.4**	**45.3**
Elasticity of taxes and social security contributions	1.1	0.2	0.9	1.0	1.0	1.0

Box 9 – The Responsibility and Solidarity Pact

The Responsibility and Solidarity Pact was unveiled by President Hollande on 14 January 2014 and presented by the Prime Minister on 8 April 2014. It is structured around several pillars: further reducing employers' payroll contributions; streamlining the business tax system and lowering business taxes; cutting red tape; obtaining commitments regarding the quality and quantity of jobs; and introducing solidarity-based measures to enhance households' purchasing power, particularly for the least well-off.

- Further reducing the cost of labour: the Responsibility and Solidarity Pact calls for greater reductions in labour costs to meet two objectives: create more jobs and enhance our economy's competitiveness and export capacity. In 2015, the cost of minimum-wage labour will be cut by eliminating employers' social security contributions, except for unemployment insurance, and by a review of the existing exemptions on jobs paying up to 1.6 times the minimum wage. Starting on 1 January 2016, family allowance contributions will be cut by 1.8 percentage points on jobs paying between 1.6 times and 3.5 times the minimum wage. All in all, the further cuts in payroll contributions on jobs paying up to 1.6 times the minimum wage will come to nearly €4.5 billion and the cuts for jobs paying more than 1.6 times the minimum wage will also come to €4.5 billion. Family allowance contributions will also be cut by €1 billion for self-employed workers. As the impact of the Competitiveness and Employment Tax Credit grows, the cost of labour will have been reduced by €30 billion in 2017, an amount that is comparable to the cost of family allowance contributions.

- Streamlining the business tax system: the Responsibility and Solidarity Pact calls for streamlining and reducing business taxes to help encourage investment. The corporate social solidarity contribution (C3S), which is paid by some 300,000 companies, will be phased out by 2017, with a preliminary cut of €1 billion in 2015 in the form of an allowance, which means that two-thirds of the companies currently paying this tax will be exempt in the first year. Companies will save a total gross amount of more than €6 billion as a result of abolishing this tax. The exceptional corporate income tax payment for large corporations will also be eliminated in 2016 and the standard rate of corporate income tax will be lowered from the current 33.33% to 28% in 2020, with a preliminary cut in 2017. Furthermore, several dozen taxes generating only minor revenue will be abolished. This tax reform will promote growth and jobs.

- Cutting red tape faster: the move to cut red tape for businesses will be stepped up to streamline procedures and facilitate decision-making. The Enabling Act of 2 January 2014 empowers the Government to use a fast-track procedure, in particular to ease accounting requirements for SMEs. Other red-tape cutting measures will be introduced in the coming months, in accordance with the recommendations of the Administrative Streamlining Board, which will review the ten key procedures for businesses. The other task of the Board, which is co-chaired by a Member of Parliament (Thierry Mandon) and a business executive (Guillaume Poitrinal), will be to monitor progress on the red-tape cutting programme for businesses and to assess the results. On 14 April 2014, the Board presented a first set of 50 measures to make the business environment more transparent and predictable, to cut red tape faced by companies and to facilitate the hiring and training of workers.

www.parlament.gv.at

- Creating jobs and modernising industrial relations: as part of the Pact, businesses will commit to creating jobs (particularly for young people), offering job training and providing quality employment. These commitments were outlined in the labour-management agreement signed on 5 March 2014. The specifics are to be worked out in future negotiations within each industry.

- Introducing solidarity measures for the least well-off households: the Pact also calls for solidarity measures worth €5 billion to be introduced by 2017 to boost the purchasing power of the lowest-income households. Starting on 1 January 2015, a gradual reduction in employees' payroll contributions on jobs paying up to 1.3 times the minimum wage will increase minimum-wage workers' take-home pay by about €500 per year. A preliminary measure to help the lowest-income households will be introduced in 2014.

According to the MESANGE model, the major focus in 2015 on low-wage jobs, where labour demand is very sensitive to cost (see the progress report by the High Council on Public Finances on about changes in social protection financing), means that the reduction in employers' payroll contributions under the Responsibility and Solidarity Pact will lead to the creation of 35,000 new jobs as soon as the Pact enters into force. As the impact of the Pact grows, it will lead to an annual average of 65,000 new jobs in 2016 and 50,000 in 2017.

In aggregate, the Responsibility and Solidarity Pact will add 0.25 points to growth in 2016 and 2017 and help create 190,000 jobs by 2017 if we factor in the usual macroeconomic knock-on effects.

The growth momentum triggered by the climate of confidence and by the commitments made by labour and management as part of the Pact could boost its impact.

Table 11 - Responsibility and Solidarity Pact – impact on growth and employment

	2014	2015	2016	2017
Real GDP growth	0.0	0.1	0.4	0.6
Total jobs created (thousands)	0	40	120	190

3.7.2 Central government revenue

In 2014, central government taxes were 0.3 points of GDP lower than in 2013, primarily as a result of discretionary revenue measures and transfer-related decisions. The measures in the 2014 Initial Budget Act should help sustain the growth of central government tax revenue. They include an increase in the corporate income tax surcharge, a lowering of the cap on family deductions (*quotient familial*), the removal of income tax exemptions for pension increases and for employer contributions to collective supplementary pension schemes, and higher green taxes through the addition of a CO2 component to existing taxes. However, the positive impact of these measures is more than offset by the after-effects in 2014 of previous measures, such as those in the 2013 Initial Budget Act affecting business taxes (limit on the deductibility of financial expenses, calculation of taxable long-term capital gains, reform of the final corporate income tax instalment), the net impact of the Competitiveness and Employment Tax Credit and the additional transfer of VAT revenue to social security funds.

With no change in the legislation, growth of central government taxes would have matched GDP growth. The weaker growth of VAT revenue compared to GDP growth would have been offset by the automatic jump in corporate income tax revenue.

Between 2015 and 2017, the central government tax burden should decline more rapidly, primarily as a result of the growing impact of the Competitiveness and Employment Tax Credit. Tax elasticity should be slightly higher than one as economic growth picks up again.

3.7.3 Social security funds' revenue

In 2013, the social security funds' revenue increased by 2.6%. The 3.1% increase in social security contributions outstripped private sector payroll growth of 1.2% for employers paying into the central social security agency (ACOSS). The increase stems from the end of the exemption from social security contributions of overtime pay, which contributed €2.0 billion, the increase in the old-age pension contribution rate to finance the early retirement scheme for long careers, which contributed €0.9 billion, the impact of the self-employed workers package, which added €0.9 billion, and the increase in the contribution rates for the local government employees' retirement scheme.

The slower growth in tax revenue (2.4%) compared to 4.8% in 2012 stems from sluggish natural revenue growth due to the social security taxes levied on capital.

In 2014, social security revenue should grow more quickly as private sector payroll grows by 2.2%, compared to 1.2% in 2012, for employers paying into the central social security agency (ACOSS), thus maintaining a healthy growth rate in social security contributions (3.0%). The stronger growth of revenue also stems from higher contribution rates, such as the increase in the old-age pension contribution rate net of the decrease in employers' family allowance contributions, which should contribute €0.7 billion as part of pension reforms, the reform of the early retirement scheme for long careers, which should contribute €0.6 billion, the increase in the contribution rates for the local government employees' retirement scheme, which should contribute €0.6 billion, and the increase in supplementary retirement pension contributions, which should contribute €0.5 billion. Tax revenue should increase by 3.5% in 2014. This growth should be sustained by the increased transfer of VAT to social security funds to help offset the decline in family allowance contributions and to transfer the proceeds from lowering the cap on family deductions and from making premiums paid by employers for supplementary employee health benefits taxable.

Between 2015 and 2017, economic recovery and the Government's measures to promote job creation should sustain the growth of the private sector payroll, helping it to reach 3.5% in 2015 and 4.3% in 2016. The reduction in social security contributions outlined in the Responsibility and Solidarity Pact should however slow the average rate of growth to 2.7% over the 2015-2017 period (compensated over the same period).

3.7.4 Local government revenue

In 2013, growth of local government tax revenue stood at 0.6%. This increase stems from the combination of moderate tax increases in the year before an election, the fall in registration

www.parlament.gv.at

duty (DMTO) revenue owing to the weak housing market for existing homes and the decline in revenue from the contribution on business value added. Local tax revenue stood at €124.5 billion. The stabilisation of central government transfers for local government, except for the VAT compensation fund and compensation for reform of the local business tax, explain the weak growth of non-tax revenue.

In 2014, local tax increases voted by newly elected municipal and *département* councils are expected to be larger than the increases in 2013, in keeping with the usual pattern. Furthermore, *départements* will receive tax transfers to help cover their social expenditure. Consequently, growth of local government tax revenue should rise to 3.1%. On the other hand, central government funding for local government should contract by €1.5 billion compared to 2013.

Between 2015 and 2017, local tax revenue should keep pace with GDP growth. The decrease in central government funding will be greater, with a total reduction of €11 billion between 2015 and 2017.

Box 10 – Impact of cuts in central government funding for local government

The funding structure of local government was changed in 2014 to meet two objectives: to promote the streamlining of local government expenditure and to redirect funding to the local governments experiencing the most severe financial constraints.

The incentive for streamlining expenditure stems from the cut in central government transfers to local government. After being stabilised in 2013, central government funding will be cut by €1.5 billion in 2014. The cuts are spread across the various categories of local government in proportion to their operating revenues and in accordance with the guidelines set out in the Confidence and Responsibility Pact that central and local government signed on 16 July 2013. The cuts came to €0.8 billion for municipal governments, €0.5 billion for *départements* and €0.2 billion for regions.

The €1.5 billion cut in central government funding is an incentive for local government to streamline expenditure. In accordance with the "golden rule", local governments' operating budgets must balance in real terms. Operating expenditure cannot be financed through borrowing. Consequently, a decrease in operating funds means that local governments have to reduce operating expenditure.

This adjustment will continue until 2017. As announced by the Prime Minister on 16 April 2014, local government will contribute €11 billion to the €50 billion in savings planned between 2015 and 2017. The sustainability of further cuts in local government funding will be enhanced by structural reform of the general operating grant, which is the largest component of central government funding for local government, totalling €40.1 billion in the 2014 Budget Act. This long-term visibility of changes in funding will enhance the incentive for local government to keep their expenditure under control. A series of measures dealing with such matters as compensation of local civil servants, regulations and local organisational structures will help achieve this objective.

In parallel to measures affecting central government transfers, *départements* will receive new funding in 2014 to finance their non-discretionary social expenditure that has been rising in recent years because of weak economic growth. On the one hand, an amount representative of the cost of managing the property tax on developed land has been transferred to the *départements*. The total

transfer in 2014 stood at €0.8 billion. On the other hand, they have temporarily been empowered to increase registration duty rates from 3.8% to 4.5%.

Other measures have also been taken to ensure that funding is spread more evenly within each level of government. This encourages the wealthiest local governments to moderate their expenditure and redirect funds to the least well-off. For example, the National Intermunicipal and Municipal Equalisation Fund was increased from €360 million in 2013 to €570 million in 2014. Furthermore, measures to help *départements* have been combined with special arrangements to ensure that the neediest *départements* receive funds. A realignment affecting 0.35% of the registration duty tax base was introduced in 2014. The funds transferred to compensate for costs of managing the property tax on developed land are shared according to a formula that takes account of the *départements'* potential tax revenue and the net cost that each one incurs for the RSA income support supplement.

www.parlament.gv.at

3.8 Government debt and stock-flow adjustment

The government debt ratio stood at 93.5 points of GDP in 2013 compared to 90.6 points in 2012, an increase of 2.9 points of GDP compared to 4.4 points in 2012. The smaller increase stems from a reduction in the deficit and a smaller stock-flow adjustment. Adverse economic conditions, with nominal GDP growth of 1.4%, meant that the debt-stabilising balance remained high at -1.2% compared to -1.3% in 2012. Efforts to reduce the government deficit to 4.3% of GDP compared to 4.9% in 2012, helped slow the increase in the debt ratio and the deviation from the debt-stabilising balance stood at 3.0 points compared to 3.5 points in 2012. This effect has been amplified by a negative stock-flow adjustment of -0.2 points of GDP in 2013 compared to 0.9 points in 2012. Direct assistance for the euro area in 2013 stood at 0.7 points compared to 1.7 points in 2012, as lending by the EFSF slowed. On the other hand, the change in the balance on the Treasury's cash account on 31 December was a source of financing for the central government in 2013 in contrast to 2012.

Table 12 - Breakdown of changes in the government debt-to-GDP ratio

(percentage points of GDP)	2013	2014	2015	2016	2017
Debt ratio according to the Maastricht definition (1)	**93.5**	**95.6**	**95.6**	**94.2**	**91.9**
Debt ratio excluding financial assistance for euro area countries	**90.4**	**92.4**	**92.5**	**91.2**	**89.0**
Nominal GDP growth (%) (2)	*1.4*	*2.2*	*3.2*	*3.9*	*3.9*
Debt-stabilising balance (excluding stock-flow adjustment) $(3)_n \approx -(1)_{n-1} \times (2)_n$	*-1.2*	*-2.0*	*-3.0*	*-3.6*	*-3.6*
Headline balance (4)	*-4.3*	*-3.8*	*-3.0*	*-2.2*	*-1.3*
Deviation from debt-stabilising balance (5)=(3)-(4)	3.0	1.8	0.0	-1.4	-2.3
Stock-flow adjustment (6)	-0.2	0.4	0.0	0.0	0.0
Change in debt ratio (7)=(5)+(6)	2.9	2.2	0.0	-1.4	-2.3

In 2014, the debt ratio should grow more slowly, rising by 2.2 points to 95.6% of GDP. The combination of a cut in the deficit to 3.8% of GDP in 2014 compared to 4.3% in 2013, and a stronger recovery in economic growth will automatically slow the debt ratio's growth, with a deviation from the debt-stabilising balance of 1.8 points of GDP. The stock-flow adjustment in 2014 should come to 0.4 points of GDP, stemming primarily from support for euro area countries facing financial difficulties, with the final loan tranches to Greece and Portugal granted by the EFSF and last capital endowment for the ESM.

In 2015, the government debt ratio should be stable at 95.6% of GDP. The level of the government deficit, with the debt-stabilising balance at the same level, will not affect the debt ratio, and neither will stock-flow adjustment.

Continued fiscal consolidation in 2016 and 2017 and real GDP growth of 2 ¼ % should lead to a decline in the debt ratio of about 1.9 points of GDP per year on average. The deficit will be significantly lower than the debt stabilising balance of approximately -3.6%, with nominal GDP growth at 3.9%. Furthermore, the impact of the stock-flow adjustment is supposed to be neutral from 2016 on, since no new loans by the EFSF means no impact from European financial assistance plans, the capital subscriptions for the ESM end in 2014, and Ireland's and Portugal's repayments of EFSF loans are slated for after the end of the forecast period (see Box 11).

www.parlament.gv.at

Box 11 - Impact of European financial assistance plans on government debt

As tensions started to emerge on European markets in the fourth quarter of 2009, several euro area Member States in succession had to call upon Europe for financial help.

The impact of financial assistance for the euro area on France's government debt is estimated at €68.6 billion in 2014 compared to €62.9 billion in 2013.

Table 13 - Debt arising from financial assistance for the euro area (deviation from baseline)

(€bn)	2013	2014	2015	2016	2017
Government debt (Maastricht definition)	**62.9**	**68.6**	**68.6**	**68.6**	**68.6**
Bilateral loans to Greece	11.4	11.4	11.4	11.4	11.4
EFSF loans to Greece	29.2	31.4	31.4	31.4	31.4
EFSF loans to Ireland	2.6	3.8	3.8	3.8	3.8
EFSF loans to Portugal	5.4	5.7	5.7	5.7	5.7
Capital endowment to ESM	13.0	16.3	16.3	16.3	16.3

When the European Commission and Council assess compliance with the deficit and debt criteria, the Stability and Growth Pact (Article 2 of Regulation 1467/97 as amended) explicitly calls for special attention to be given to debt incurred in the form of bilateral and multilateral assistance between Member States to preserve financial stability and debt related to financial stabilisation operations during major financial crises.

Three successive financial assistance instruments were set up:

1) ***Bilateral loans***: The euro area Member States and the IMF jointly assisted Greece in the second quarter of 2010 with €110 billion in bilateral loans. The EU lent €80 billion[11] (including €16.8 billion from France[12]) and the IMF lent €30 billion.

2) ***European Financial Stability Facility***: The euro area Member States also created the European Financial Stability Facility (EFSF) to provide assistance to any euro area country that requests it. This facility has a capacity of €440 billion on top of the €60 billion in the European Financial Stabilisation Mechanism (EFSM) which is a European Union instrument backed by the EU budget and available to all 28 Member States. **The Member States' guarantees for EFSF loans are recognised as part of their gross debt under the Maastricht definition**[13] in proportion to their share of the guarantees supplied to the EFSF[14]. France's share at the beginning of 2014 stood at 21.88%.

The EFSF and the EFSM were used to support Ireland and Portugal. Ireland was the first to receive a total of €85 billion in assistance at the end of 2010, including **€17.7 billion from the EFSF**, to which **France contributed €3.8 billion** under a programme where all of the loan tranches were disbursed before December 2013. In the middle of 2011, **Portugal** received €78 billion in assistance, including **€26 billion from the EFSF, to which France contributed €5.6 billion** under a programme to finance Portugal's general government until the middle of 2014. Ireland exited its assistance programme on 15 December 2013 following rigorous implementation of a set of reforms that ensured the sustainability of a strong economic recovery.

[11] Later lowered to €77.3 billion after Slovakia refused to take part and Ireland and Portugal withdrew.
[12] Only €11.4 billion of the €16.8 billion has actually been disbursed. The remainder was incorporated into the second programme in March 2012 and financed by the EFSF.
[13] The impact in terms of debt is neutral since the amount recorded as gross debt is also recorded as a claim on the euro area Member State receiving the assistance.
[14] This share is based on the national central banks' shares in the ECB's capital, adjusted for the holdings of Member States benefitting from the withdrawal clause under the terms of a financial assistance programme.

www.parlament.gv.at

FRANCE STABILITY PROGRAMME 2014-2017

Following a deterioration in Greece's economic and financial situation in the middle of 2011, a **second financial assistance programme** was introduced in March 2012. The euro area Member States and the IMF provided further financing of €130 billion on top of the undisbursed funds from the first programme covering the period from 2012 to 2014. This financing is provided by the EFSF, which also covers the remaining tranches of the bilateral loans granted to Greece, totalling €24.4 billion, plus €9.9 billion not yet disbursed by the IMF. Given the IMF's participation, the **Member States will guarantee a total of €143.7 billion under the second programme, €31.4 billion of which will be guaranteed by France**, including the undisbursed funds from the first programme, along with the €11.4 billion already lent under the first bilateral programme.

France has therefore agreed to finance or guarantee €52.3 billion (equivalent to 2.5 points of GDP) in financial assistance for euro area countries through bilateral loans or the EFSF by the end of 2014.

None of these loans is scheduled to be repaid before the end of this Stability Programme in 2017. The average maximum maturity of the EFSF loans to Ireland and Portugal has been extended from 15 to 22 years following the decision made by the Eurogroup in March 2013. In keeping with the decisions of the Eurogroup meeting of 26 November 2012, the average maturity of loans to Greece was extended to 20 years for bilateral loans and 32.5 years for EFSF loans.

3) **European Stability Mechanism**: **the EFSF and the EFSM have stopped granting new loans**[15] **since the European Stability Mechanism (ESM) came into effect on 28 September 2012.** The EFSF was set up as a temporary institution and cannot engage in new financial assistance programmes after June 2013. At its December 2010 meeting, the European Council decided, therefore, to set up a permanent mechanism to safeguard the financial stability of the euro area. The ESM is designed to be permanent and to rely not only on government guarantees, but also on paid-in capital.

Eurostat issued an opinion on 7 April 2011 based on the characteristics described in the Conclusions of the European Council of 24 and 25 March 2011. **Eurostat has deemed that the liabilities of the ESM will not be counted as part of the Member States' Maastricht debt**[16] **and that only their borrowing to finance their subscriptions to the paid-in capital would be recognised as debt. This capital stands at €80.2 billion since Latvia joined the euro area on 1 January 2014**. **France's 20.3% share totals €16.3 billion.**

This capital will be paid in 5 instalments of €3.3 billion. In accordance with the Statement of the Heads of State and Government at the European Council meeting of 2 March 2011, France's Supplementary Budget Act of 8 February 2012 includes authorisation for €16.3 billion in commitments. France then ratified the ESM Treaty on 8 March 2012. The first two instalments were paid in October 2012, adding €6.6 billion to debt in 2012. The third was paid on 29 April 2013 and the fourth on 31 October 2013. The fifth and last instalment will be paid in April 2014.

---

[15] The EFSF is now being managed in run-off mode, which means that the Facility will continue to manage the loans already granted until they are fully repaid and that any new financial assistance will now be provided by the ESM.

[16] Since the ESM is a permanent international institution under international law with a governance structure similar to that of international financial institutions (with a board of governors, a board of directors and a managing director), and a paid-in capital of €80.2 billion. The ESM's paid-in capital must always be greater than 15% of its commitments.

42

www.parlament.gv.at

The ESM made its first disbursements to Spain for its bank recapitalisation programme, which was decided in July 2012. The amount disbursed in December 2012 and February 2013 was €41.3 billion. The programme ended in January 2014 and rigorous implementation produced a sustainable stabilisation of Spain's banking sector. After approval by the Eurogroup on 24 March 2013, €10 billion in financial assistance was also granted to Cyprus. The EMS provided €9 billion and the IMF €1 billion, of which the EMS disbursed €4.6 billion at the end of December 2013. These disbursements do not add to France's debt, as explained previously.

www.parlament.gv.at