Haut Conseil des Finances Publiques

Opinion n° HCFP-2020-4

on the third amending budget bill for 2020

8 June 2020

Main Conclusions

The high level of uncertainty resulting from the health crisis caused by the Covid-19 epidemic leads to frequent revisions of macroeconomic forecasts and of the Government's policy and fiscal responses. The High Council is thus asked, for the third time in less than three months, to give an opinion on a draft amending budget bill (PLFR) for 2020.

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The High Council notes that the Government's scenario, contrary to the one presented in the previous PLFR, is no longer assuming a rapid return to normal activity, but forecasts that activity in the second half of the year will remain well below its level at the end of 2019.

Therefore, it considers the Government's forecast of an 11% decline in activity in 2020 to be cautious. Continued favourable trend in the health situation and a higher utilisation in the second half of the year than assumed by the government of the constrained savings accumulated by households could lead to a less pronounced recession.

The High Council estimates that employment could be slightly higher than the Government's forecast, but inflation, on the contrary, could be slightly lower.

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The High Council notes that the Government's deficit forecast stands at 11.4 points of GDP, a level not seen since the end of the Second World War. The deterioration of the deficit compared to the previous PLFR is the result of new spending, a sharp revision of the macroeconomic assumptions and more realistic forecasts for some previously decided public expenditures.

The High Council points out that more favourable macroeconomic developments could limit the widening of the general government deficit. On the contrary, it highlights that some of the measures presented as cash flow measures could finally have an impact on the deficit as early as this year and that not all the measures announced by the Government to support activity, in particular some sectoral stimulus packages, have been included in this PLFR.

It points out that the structural deficit for 2020, as estimated by the Government, would be identical to the one in 2019 (2.2 points of GDP) and would deviate significantly from the programming law. The structural deficit could moreover turn out to be higher than forecast in this third PLFR. Indeed, some of the expenditure related to the health crisis, considered as temporary by the Government, could be extended beyond 2020. Besides, there is a risk that the estimation of potential GDP could be revised downwards due to possible losses of human capital caused by the rise in unemployment and the consequences of the foreseeable increase in business bankruptcies and the decline in investment on productive capacity, as well as the impact on productivity of the lasting implementation of health protection measures.

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The High Council notes that the forecast of the government debt-to-GDP ratio is revised upwards by more than 5 points compared to the previous PLFR and by 22 points compared to the initial finance act. This ratio would thus exceed 120 points of GDP at the end of 2020. This massive increase, which comes on top of an almost uninterrupted increase over the past ten years, weakens the medium-term sustainability of France's public finances and calls for careful vigilance.

Introductory remarks

1. The High Council adopted the following opinion after discussions at its meeting on June 8, 2020.

1. On the scope of this opinion

The Government referred to the High Council of Public Finances on June 4, 2020, pursuant to article 15 of organic law n ° 2012-1403 of December 17, 2012 relating to the programming and governance of public finances, the introductory article of the third amending finance bill (PLFR) for 2020 to give an opinion on the associated macroeconomic forecasts as well as on the consistency of this bill with the multi-year trajectory of structural balance defined by the programming law of public finances of January 2018 (LPFP).

2. On the method used by the High Council

3. In order to assess the realism of the macroeconomic forecasts associated with the amending finance bill, the High Council relied on the latest available statistics and on the information communicated by the Government, in its referral and in the responses to the questionnaires which they addressed the High Council.

4. The High Council proceeded, as permitted by article 18 of the organic law of 2012, to hear the representatives of the competent administrations (Directorate General of the Treasury, Directorate of the Budget and Directorate of Social Security) following the initial referral. He also heard from representatives of Insee, the Research, Studies and Statistics Department (Dares), the Banque de France, Rexecode and the French Economic Observatory (OFCE). The High Council also drew on the work of the European Commission, the European Central Bank and the International Monetary Fund (IMF), which have recently produced forecasts or analyses of the economic effects of the measures taken to combat the pandemic Covid-19 coronavirus.

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5. As the High Council noted in its previous opinions relating to the first two PLFRs for 2020[1], the health crisis results in uncertainties on an unprecedented scale which make any

[1] Opinion n ° HCFP-2020-1 of March 17, 2020 and n ° HCFP-2020-2 of April 14, 2020.

economic forecasting exercise difficult and in shocks which prompt budgetary responses of unusual scope.

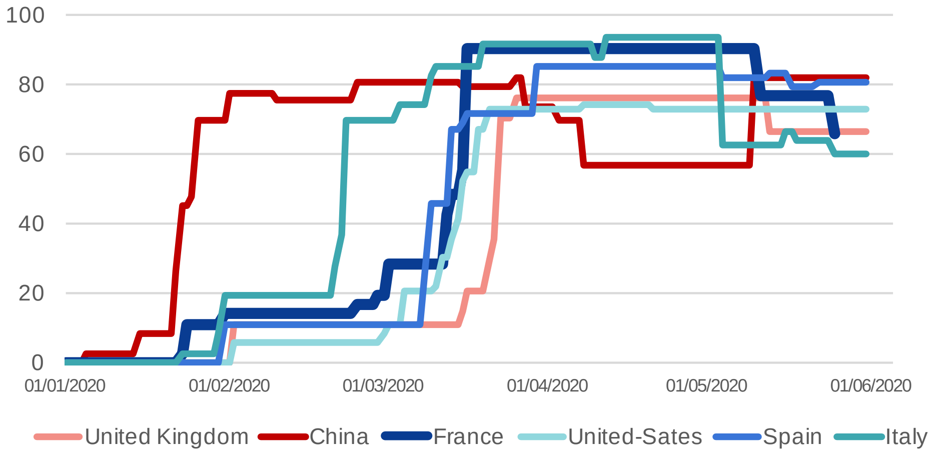
6. As in its opinion on the second PLFR, the High Council notes that this third PLFR does not carry out a full review of government expenditures and revenues and that it probably does not mark the end of the process of adjustment to the consequences of the health crisis. The High Council notes that the Government has also not presented an amending social security financing bill, despite the planned increase in health expenditure and the considerable deterioration in the financial situation of social security.

7. After presenting the general context (I), the High Council expresses its assessment on the one hand on the macroeconomic forecasts on which the amending finance bill is based (II) and on the other hand on the associated public finance forecasts (III).

I. An unprecedented global economic crisis

8. The health crisis caused by the Covid-19 epidemic has affected the entire world. The implementation of containment measures to curb the epidemic has restricted the activity of many economic sectors and led to a recession of an unprecedented magnitude since the Second World War. While the main world economies have today emerged from the period of tight travel and economic restrictions, activity is only gradually returning to normal.

Index of health restriction measures taken against Covid-19

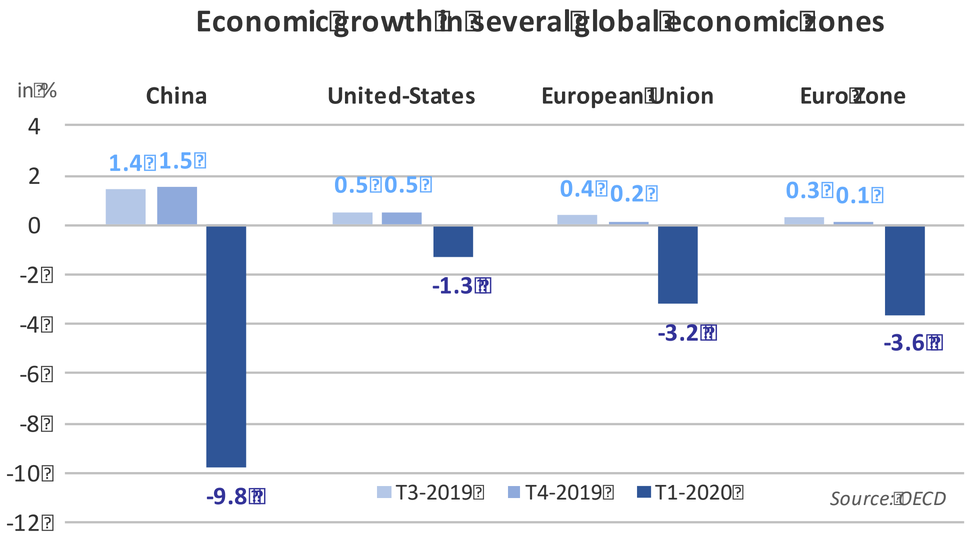


Source: Oxford COVID-19 Government Response Tracker, Oxford University

Note: the Oxford COVID-19 Government Response Tracker (OxCGRT) is a project to monitor the progress of measures put in place by governments during the period of the spread of the Covid-19 epidemic. It consists of a composite index measuring the rigor of these responses based on a series of indicators (school closings, travel restrictions, etc.).

9. Most economies around the world have been hit hard by the crisis since the start of the year. Its impact began to be felt in the first quarter, with GDP drops of 9.8% in China, 1.3% in the United States and 3.2% in the European Union compared to the fourth quarter 2019. The impact on economies relates both to the productive system whose functioning is hampered by

health restrictions and to the demand addressed to businesses, in a context of great uncertainty felt by economic actors.

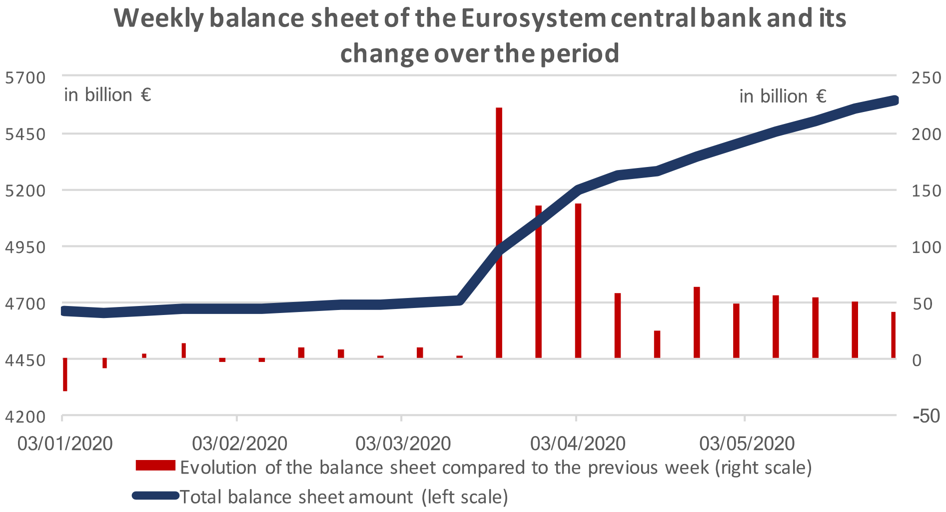


10. The entire euro area experienced a very sharp contraction in its GDP in the first quarter of 2020, with a 3.6% drop in GDP compared to the previous quarter. The drop in activity shows great heterogeneity between countries. Possible differences in the collection and processing of existing data by statistical institutes weaken current comparisons. However, some countries such as Germany and the Netherlands, less affected by the pandemic and not having implemented as strict health restrictions as in other countries, seem to have experienced less severe recessions than countries like Spain, France or Italy more affected by the epidemic and where containment measures have been more stringent.

11. The fall in GDP is expected to be much stronger in the second quarter in most countries with the shutdown of large parts of the economy, particularly in April. In addition, activity has only recovered gradually since the restrictions began to be lifted.

12. A rebound in activity is expected by all forecasters in the second half of the year, but overall activity should experience a very marked decline over the whole of 2020. In its June forecast, the European Central Bank estimates for instance that the GDP of the world outside the euro zone will contract by 4.0% over the whole of 2020 and that of the euro zone by 8.7%.

13. The economic consequences of the crisis in the Eurozone countries were, however, cushioned by the massive and rapid reaction of economic policies. The European Central Bank, whose monetary policy was already very accommodating before the crisis, adopted in March new support measures, which it further increased in early June (increase in the size of its programs purchase of assets, strengthening of liquidity provision to banks through targeted long-term refinancing operations ...).



Source: Weekly Financial Statement, European Central Bank(ECB)

14. Fiscal policies have been overwhelmingly expansionary across all EU member states, far beyond the effect of automatic stabilizers alone. In addition to the national responses, the European Union has decided to create funds of € 540 billion in loans to the Member States, in particular for the financing of partial unemployment. In addition, the European Commission has proposed the creation of a financial instrument for economic recovery of € 750 billion, including € 500 billion in direct subsidies to the Member States and sectors most affected by the crisis, which would be integrated into the next multiannual financial framework 2021-2027 (*Next Generation EU*).

15. The path out of the health crisis in all countries remains uncertain at this stage. Many additional hazards could materialize. In particular, the vulnerability of many emerging countries to the massive decline in external funding caused by the health and economic crisis, reinforced for some by the low prices of raw materials, could become more acute in the months to come. The rise in protectionism could accentuate these risks. Conversely, in the Eurozone, the measures intended to maintain to a large extent the employees' pay have led to the creation of significant constrained savings, which could be consumed in the coming months, thus allowing a sharper rebound, but on a scale that remains very difficult to anticipate.

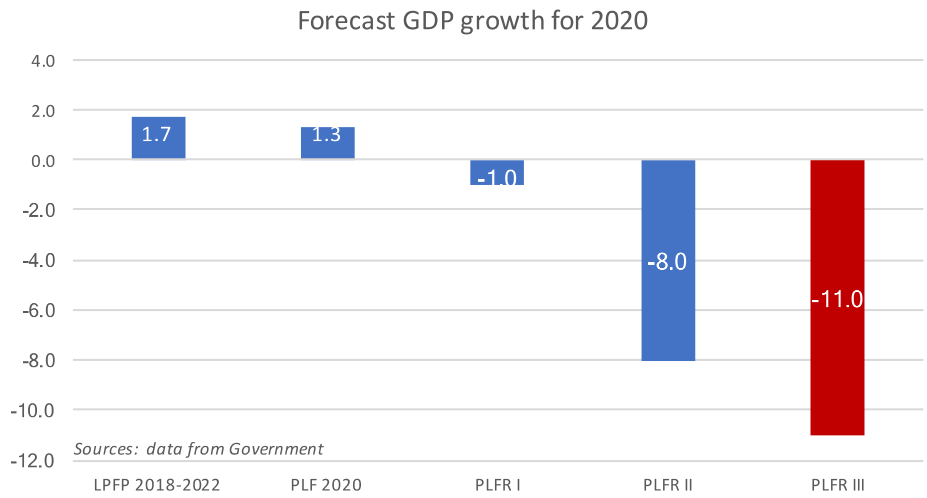
II. Observations on the macroeconomic forecasts for 2020

1. Government forecasts

16. According to the referral from the Government, "*GDP would be down 11% in 2020. The health restriction measures in force in France since mid-March ended on May 11, after a total duration of 8 weeks. The rebound to trend levels has been observed since May 11 and should continue beyond June 2 [...].*

17. *Household consumption is expected to decline sharply over the whole year. [...] It would not completely return to its usual level at the end of 2020 due to health constraints in certain sectors. The investment in construction would be penalized by an almost general closure of*

sites during containment. Productive investment would suffer from the high uncertainty and the decline in activity. Tourist flows would be very reduced in 2020 and would not return to their previous level by the end of 2020. Exports would decrease in line with the decline in activity among our partners in the euro zone and in the rest of the world. However, imports are also expected to fall sharply in line with the fall in domestic demand. [...] Inflation, as measured by the CPI, would decrease to + 0.4% in 2020 after +1.1% in 2019, due to the health crisis and the low prices of energy".



2. Assessment of the High Council

18. The third PLFR for 2020 takes into account the very sharp drop in GDP which is expected in the second quarter (almost 20% according to Insee in its latest economic outlook), after the 5.3% drop recorded in the first quarter.

19. The government's scenario is based on the end of the state of health emergency on July 10 and a gradual lifting of restrictions on international travel. It includes a gradual and partial return to normal during the second half of the year, in France and among its main partners: given the drop expected in the second quarter by Insee in its latest economic outlook, the Government's forecast is consistent with activity in the second half still on average 7% below its level at the end of 2019.

20. The High Council also reckons, like all the forecasters it has consulted, that a rebound in activity will occur in the second half of 2020 but that it should not allow the return by the end of the year to its level at the end of 2019 and notes that major uncertainties continue to affect the extent of this rebound.

21. In the short term, the favorable development of the health situation allows a gradual lifting of most of the travel and activity restrictions, but certain sectors will continue to be affected by the persistence of targeted restrictions (air traffic, tourist activities, accommodation, catering, etc.) and by maintaining prudent behavior. The risk of a resurgence of the epidemic occurring and weighing on the exercise of certain activities, thus causing a further decline in activity, is impossible to quantify today, but cannot be entirely discounted.

22. The support measures which have been taken in the context of successive PLFRs for 2020 should make it possible to limit the impact of the crisis on the productive apparatus and

to preserve to a certain extent the real income of households. However, forecasts from international organizations as well as from institutes that the High Council has heard show that they should not prevent the financial situation of many companies from deteriorating, leading to more bankruptcies and an investment deficit. In addition, the necessarily progressive nature of the reallocation of production capacity from the sectors of activity durably affected by the crisis towards those which have become more promising will limit the rebound capacity of the economy.

23. Travel restrictions are expected to affect tourism receipts from foreign visitors, and the lack of a full return to normal activity for our partners will weigh on all of our exports of goods and services.

24. Particular uncertainty weighs on the behavior of households, in France as with our main European partners. On the one hand, their incomes should suffer in 2020 from the drop in employment and activity of the self-employed. On the other hand, the support mechanisms put in place (partial unemployment, support fund for the self-employed, exemption from contributions for certain sectors directly linked to tourism) will cushion their consequences and households have a large amount of constrained savings built up during the containment (€ 100 billion according to the 3rd PLFR). The government anticipates a mere return to normal of the saving behavior of households, without any use over the forecast horizon of these extra savings, which thus limits the magnitude of the rebound in consumption. The High Council considers that the savings rate could be lower than the exceptionally high level forecast by the Government for 2020 (23.2% against 14.9% in 2019), and therefore the consumption higher.

25. The fall in inflation presented by the government in its forecast (0.4%, compared to 1.1% in 2019) essentially reflects the fall in petroleum products but also that of core inflation. Available data[2] indeed indicate that core inflation would decrease in 2020 as a result of lower commodity prices, lower employment and lower aggregate demand, phenomena that today tend to outweigh the impact of the additional costs entailed by the drop in productivity and the implementation of health protection measures. The High Council considers that the Government's inflation forecast, although revised down from the previous PLFR, could prove to be a little too high in 2020. On the contrary, it would be compatible with a recovery in activity much more stronger than expected by the Government.

26. The 3rd PLFR forecasts a significant decline in total employment (-2.8%, corresponding to the net loss of 0.8 million jobs on average in 2020), but much more limited than activity (-11%). The partial unemployment scheme in fact made it possible to cushion the impact of the drop in activity in the first half. The Government's forecast, however, assumes a continuation of decline in employment in the second half of the year, resulting in a significant adjustment of employment to activity (1.2 million jobs lost at the end of 2020 compared to at the end of 2019). The High Council therefore considers that the level of employment could be a little higher than expected by the Government.

27. **The High Council notes that the Government's scenario no longer assumes, unlike that presented in the previous PLFR, a rapid return to normal of activity, but forecasts that activity will remain in the second half of the year significantly below its level of the end of 2019.**

[2] The lack of trade in certain services that have been temporarily banned and the lack of data collected by statistical institutes for certain goods makes current measures of inflation more fragile.

28. **Consequently, he considers the Government's forecast of an 11% decline in activity in 2020 to be prudent. Continued favorable development in the health situation and stronger use in the second half than retained in the Government's assumptions the constrained savings accumulated by households could lead to a less marked recession.**

29. **The High Council estimates that employment could be a little higher than expected by the Government, but inflation, conversely, a little lower.**

III. Observations on public finances

1. Government forecasts

30. According to the Government's scenario, *"The forecast of public balance for 2020 is revised down sharply, to -11.4% of GDP, against - 2.2% forecast in the LFI for 2020, and -9.1% in the LFR n ° II adopted on April 25 (and - 9.0% in PLFR2). The structural balance would amount to - 2.2% of GDP, as in 2019, and the structural adjustment to 0.0 point of GDP, as in LFI 2020 as well as in LFR n ° I and n ° II. The potential growth used in PLFR III is the same as that of the 2018-2022 public finance programming law, and the scope of exceptional and temporary measures deducted from the structural balance has been extended to measures to combat the Covid-19 epidemic. [...] because of the very one-off nature of these measures and the evolution of their cost. This cost went from 0.5 point of GDP in LFR n ° I and 1.9 point of GDP in LFR n ° II, to 2.6 points of GDP in PLFR n ° III [...].*

31. *The deterioration in the balance compared to LFI 2020 is explained by the deterioration in the economic situation and the effect of the exceptional and temporary measures. [...] The spontaneous growth rate of compulsory levies would thus stand at -9.6%, in line with nominal GDP growth of -9.7%, that is a unitary elasticity. [...] The public expenditure ratio would be revised up sharply, supported by the measures adopted in response to the epidemic and due to the denominator effect linked to the fall in GDP. It would stand at 63.6% of GDP, excluding tax credits. Public spending would thus increase by 6.4% in value in 2020, after 2.3% in 2019. [...] The public debt ratio in the sense of Maastricht would increase very sharply, reaching almost 121.0 points of GDP, due to the widening of the deficit as well as to the sharp contraction in GDP".*

2. Assessment of the High Council

32. The third PLFR for 2020 revises the trajectory of public finances to take into account the deterioration in macroeconomic assumptions and the new support measures decided. This PLFR also raises the estimated amount of certain support measures already implemented, of which the High Council had noted the risks of being exceeded in its previous opinion (partial unemployment, solidarity fund).

a. Tax revenues

33. In the continuation of the second PLFR for 2020, which had carried out a large-scale revision of the public finance scenario, the revenue forecasts are once again significantly lowered.

34. Under the effect of the change in macroeconomic scenario, the spontaneous evolution of compulsory levies (that is measured with constant legislation) has been revised downwards. The Government forecasts that their decline will be equivalent to that of GDP, which therefore corresponds to an elasticity equal to 1.0, a value comparable to that observed during the 2009 crisis, against 1.1 in the previous PLFR.

35. If this forecast is achievable, it occasionally appears to be surrounded by negative uncertainties in income tax and social security contributions, the forecasts of which have not been revised for this 3rd PLFR. In addition, as noted by the High Council in its opinion on the 2nd PLFR, the forecast of spontaneous growth in compulsory contributions makes the strong assumption that the postponement of a few months of fiscal and social deadlines will not give rise to significant debt forgiveness in 2020, even though many companies affected by these deferrals will be weakened by the fall in their activity due to the health crisis.

36. The third PLFR includes, for a total amount of € 3 billion, contribution exemptions decided within the framework of the tourism plan announced on May 14 by the Government. However, these only represent around 10% of the tax and social deferrals requested by companies.

37. Furthermore, the Government's scenario is based on a slight drop in revenue excluding compulsory levies (-1.2%), which could turn out to be a little more marked than expected, the health crisis likely to cause a significant drop in non-tax resources of local communities, hospitals and state operators.

b. Expenditures

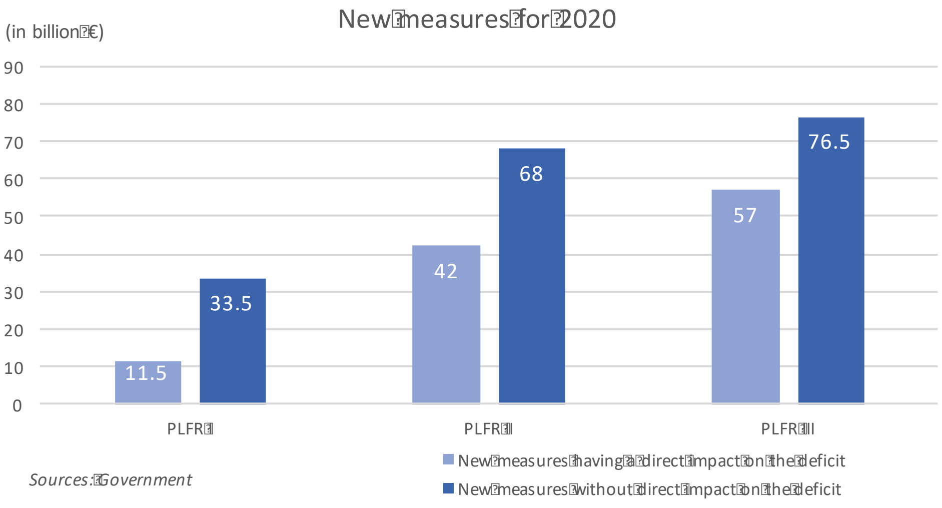
38. The forecast increase in the value of public expenditure amounts to 6.4%, i.e. growth of 1.2 points higher than that used in the 2nd PLFR[3] (+ 5.2%). The ratio of public expenditure to GDP would increase by 9.6 points in 2020 and reach 63.6%[4], a level never reached in the past 70 years.

39. The 3rd PLFR revises upwards the amount of exceptional expenditure, which goes from € 42 billion[5] to € 57 billion.

[3] Against 1.7% at constant scope in the initial finance law.

[4] This increase in the ratio of expenditure to GDP is partly linked to the shock to activity, and therefore to the denominator of the ratio, but also to an increase in expenditure in response to the health crisis.

[5] And € 44 billion in amending finance law adopted by Parliament.



40. This additional expenditure is a component of the overall plan of € 133.5 billion presented by the Government, which includes € 76.5 billion of measures which, according to the Government, should have no impact on public balances and should only weigh in cash. Besides, government support for the economy also takes the form of loan guarantees for businesses of up to € 327 billion.

Estimation cost of support measures by the 3rd PLFR (in billion€)

	Measures	Estimation of cost of measures (in billion€)
Measures having an effect on the public deficit	Partial unemployment	30,8
	Solidarity fund for companies (share of APU)	7,95
	Exceptional health expenditure, in addition to Ondam at 2,45%	8
	Tourism plan: exemption from contributions (revenue)	3
	Opening of credits in PLFR III (including automotive plan)	2,5
	Additional emergency credits carried by the State	1,6
	Income support for the self-employed[6]	0,9
	Social inclusion and protection of people	0,9
	Postponement of Unedic measures planned for April 1 and extension of rights	0,4
	Advances repayable to SMEs	0,5
	Credits for non-surgical masks from the state budget (LFR2)	0,3
	Carry back of deficits	0,4
	TOTAL	**57,2**
Non-deficit measures	Tax and social deferrals from March to June 2020	32,5
	Early repayment of tax credits and tax claims benefiting businesses	23
	Capital contributions from the special account State financial investments	20
	Addition to the Economic and Social Development Fund (FDES)	1
	TOTAL	**76,5**

41. The third PLFR brings spending from the general state budget to € 392 billion, up € 11.5 billion compared to the second PLFR. This increase reflects the opening of credits in favor in particular of partial unemployment (of the order of an additional € 5 billion from the State, for a total of € 20.5 billion[7]), targeted devices on certain business sectors (automotive, culture and press, for € 2.5 billion) and the solidarity fund for businesses (+ € 1.2 billion).

[6] See the press release n ° 2119/1009 of the Government of April 10, 2020 on the creation by the Council of social protection of the self-employed (CPSTI) of exceptional aid intended for all the craftsmen and tradesmen.
[7] The 3rd PLFR provides funding for partial unemployment measures for a total of € 31 billion, divided between the State (€ 20.5 billion) and the Unedic (€ 10.5 billion).

42. The State also supports local authorities by granting some of them repayable advances aimed at compensating part of their loss of revenue, for an amount of € 2.7 billion. These measures correspond to transfers from the state to other categories of public administration and are therefore neutral for the public deficit[8].

43. This 3rd PLFR does not reexamine the consequences on the public deficit of capital contributions for companies in difficulty, authorized by the 2nd PLFR for an amount of up to € 20 billion and which should be made from the special account “State financial investment”. The Government makes the conventional assumption that each of these financial investments will meet the requirements for these investments not recorded as public expenditure in national accounts (that is to say that the State acts as a “prudent investor”).

44. The High Council also notes that the Government is assuming that none of the guarantees granted by the State on bank loans to businesses will be called in 2020.

45. Concerning social security administrations (ASSO), this PLFR revises unemployment insurance expenditure upwards (beyond the increase of € 2 billion in credits linked to partial unemployment to be borne by the Unédic) and leaves unchanged the forecast of expenditure in the Ondam field compared to the previous amending finance bill[9]. In addition, this 3rd PLFR for 2020 takes into account the support measures for craftspeople and tradespeople which were recently announced by their complementary pension funds.

c. The effective public deficit

46. The public deficit would reach 11.4 points of GDP, that is, a deterioration of 9.2 points of GDP compared to the initial finance law and 2.3 points compared to the 2nd amending finance law. Due to the triggering of the general escape clause of the Stability and Growth Pact (see Annex 4), this massive increase in the deficit does not violate European rules in 2020.

47. All in all, upside and downside risks relate to general government revenue and expenditure. On the one hand, more favorable macroeconomic developments could lead to increase public revenues and thus limit the widening of the public deficit. On the other hand, the measures to support activity announced by the Government, in particular sectoral recovery plans, have not all been taken into account in this PLFR and part of the measures which the Government considers to have no direct effect on the balance, of an amount estimated by the 3rd PLFR at € 76.5 billion, could ultimately have an impact on the deficit this year.

d. The structural deficit

48. The structural deficit is estimated by the 3rd PLFR at 2.2 points of GDP in 2019 and 2020, against 2.0 points in the previous PLFR over these two years.

49. The government takes into account the modification made by Insee to the GDP estimation for the years 2017 to 2019. The structural deficit is thus revised up 0.2 point in 2019,

[8] They could allow the local authorities concerned to finance expenses which they would otherwise have had to forgo.

[9] The High Council notes that the alert committee on the development of health insurance expenditure considered necessary, "if the hypothesis of a bill of corrective financing allowing the rapid vote of a new Ondam was not retained, [..] the presentation in the coming weeks, for example on the occasion of the next Social Security Accounts Committee, of an updated financial framework for health insurance expenditure which would be communicated to Parliament. "

to 2.2 points of GDP (see box). Cumulative over the years 2018 and 2019, the structural deficit is *in fine* slightly less than 0.4 point above the objective which had been set in the programming law. This difference remains below the threshold for triggering the correction mechanism, but higher than that estimated in the draft regulatory bill for 2019 which the High Council has judged[10].

Consequences of national accounts revisions on structural balance assessments

The publication of annual national accounts by Insee on May 29 resulted in revisions to GDP estimates over the past three years, as it does every year. Although modest this year, the revisions lead to an increase in GDP growth of 0.1 point in 2018 and 0.2 point in 2019 compared to the estimates on which the budget review law was based. The public balance is almost unchanged (downward revision of less than € 100 million in 2019).

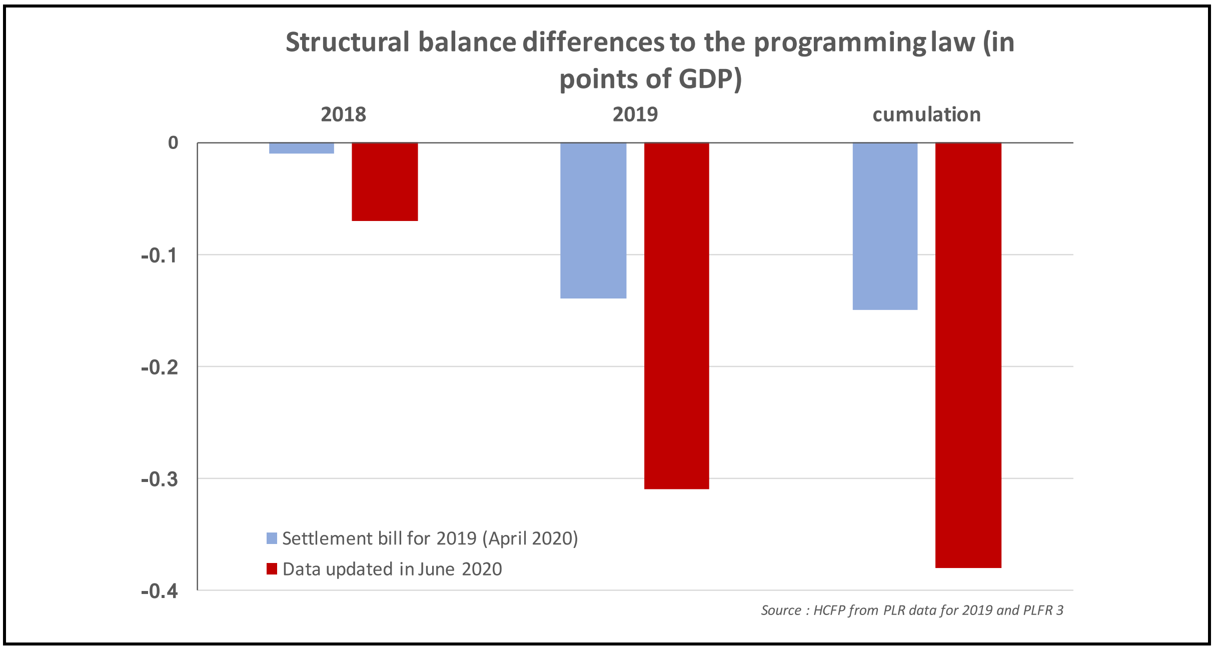
With potential GDP unchanged, these upward revisions to GDP lead to a larger share of government revenues being attributed to the impact of the economic situation and therefore to improve the cyclical balance, slightly in 2018, but by almost 0.2 point of GDP in 2019. On the other hand, the structural balance deteriorates by the same amount and moves in 2019 from a deficit of 2.0 points of GDP to a deficit of 2.2 points of GDP.

As the Government considers that the entire deterioration in the effective balance in 2020 is linked either to the economic situation or to exceptional and temporary measures, the structural deficit of 2020 is therefore also revised up, in the Government's forecast, to 2.2 points of GDP in this PLFR against 2.0 points in the previous PLFR.

Cumulative over the years 2018 and 2019, the structural deficit is *in fine* slightly less than 0.4 points above the objective which had been set in the programming law against slightly more than 0.1 points in the budget settlement bill (graph below): this difference remains below the threshold for triggering the correction mechanism, but significantly higher than that estimated in the settlement law.

Compared to the settlement law, the structural adjustment is also revised downwards, mainly in 2019. With these new estimates, the structural adjustment is now equal to zero in 2019.

[10] See opinion n ° HCFP-2020-3 on the structural balance of public administrations presented in the 2019 budget draft law.



50. For 2020, the Government considers, as in the previous two PLFRs, that all of the measures taken (2.6 points of GDP following this PLFR against 1.9 points after the previous one) are exceptional and temporary measures. Besides, the government assumes that potential GDP and therefore the structural balance are not affected by the health crisis. The cyclical balance is thus estimated by difference at -7.0 points of GDP, down 1.7 points from the previous PLFR[11].

51. In the Government's scenario, the structural balance would deviate in 2020 by 0.6 point of GDP from that recorded in the programming law of January 2018. Such a difference, if it were confirmed during the examination of the budget settlement bill of the 2020 by the High Council in the spring of 2021, would then lead it to trigger the correction mechanism set out in article 23 of the organic law of December 17, 2012.

[11] This procedure of calculating the cyclical balance as a residual is completely unusual and opposite to that usually used by the Government or that still used by the European Commission. Actually, the usual method consists firstly of evaluating the output gap, then, using an estimate of the elasticity of income and expenditure from unemployment benefits to employment, to deduce the cyclical balance and finally, after deduction of exceptional and temporary measures, to deduct the structural balance (see appendix 3). The method chosen by the Government can be justified by the exceptional nature of the changes in public finances brought about by the health crisis, but in particular has the drawback of increasing the sources of divergence with the estimates of the European Commission.

Breakdown of the public balance presented by the Government

In GDP points	**PLFR n° 3 for 2020 (June2020)**			*LPFP (January 2018)*		
	2018	**2019**	**2020**	***2018***	***2019***	**2020**
Public balance	**-2.3**	**-3.0**	**-11.4**	***-2.8***	***-2.9***	***-1.5***
Cyclical balance	0.0	0.2	-7.0	*-0.4*	*-0.1*	*0.1*
One-off and temporary measures*	-0.1	-1.0	-2.3	*-0.2*	*-0.9*	*0.0*
Structural balance*	**-2.2**	**-2.2**	**-2.2**	*-2.1*	*-1.9*	*-1.6*
Deviation from LPFP	***-0.0***	***-0.3***	***-0.6***			

Note the figures being rounded to the tenth, this may result in slight differences in the result of the operations. The public finance data for this PLFR has been modified compared to the finance bill for 2020 and compared to the previous PLFR due to the inclusion of data published by Insee at the end of May. These revisions led to revise the chronicle of deficit for the years 2017 to 2019 and in fact of structural deficit.
**: In potential GDP point.*
Source : 3rd amending financing bill for 2020, January 2018 programming law.

52. The High Council stresses that this forecast of the structural balance by the Government is based on two strong assumptions. On the one hand, it assumes that none of the additional expenditure, compared to the forecasts of the initial finance law, linked to the management of the health crisis will be extended beyond 2020 and can therefore be considered as extraordinary and temporary measures, even though the strong sectoral impacts of the crisis will probably call for long-term responses.

53. On the other hand, it is based on an assessment of potential GDP unchanged compared to the programming law of January 2018. However, it is likely that the health crisis will have adverse consequences on potential GDP, in particular because of possible losses of human capital caused by the rise in unemployment and because of the consequences of the foreseeable rise in company bankruptcies and the fall in investments on production capacities, as well as the impact on productivity of the implementation of the measures aimed at health protection. In this respect, in its spring forecasts, the European Commission has already lowered its estimate of potential growth for the year 2020 by 0.4 points. Consequently, the structural deficit could turn out to be significantly higher than expected by the Government and what is estimated before the crisis.

e. The public debt

54. Finally, the High Council notes that the 3rd PLFR revises the forecast of public debt compared to GDP by more than 5 points compared to the previous PLFR and by 22 points compared to the initial finance law.

Evolution of public debt and deficit forecasts

as a percentage of GDP	**PLF for 2020**	**PLFR 1 for 2020**	**PLFR 2 for 2020**	**PLFR 3 for 2020**
Public balance	-2.2	-3.9	-9.0	-11.4
Public debt	98.7	102.9	115.2	120.9

Source: initial and amending budget bill for 2020.

55. After a total increase of more than 30 percentage points of GDP in the decade following the 2008-2009 financial crisis, the level of debt should once again increase very sharply in 2020, to exceed 120 percentage points of GDP. Since the creation of the euro in 1999 and until last year, such a level of debt had only been reached in the euro area by very few countries. This trajectory of public debt, which weakens the medium-term sustainability of public finances in France, calls for particular vigilance.

56. The High Council notes that the government's deficit forecast stands at 11.4 points of GDP, a level never reached since the end of the Second World War. The deterioration of the deficit compared to the previous PLFR results from new spending, the sharp revision of macroeconomic assumptions and more realistic forecasts for certain expenses decided previously.

57. The High Council notes that more favorable macroeconomic developments could limit the widening of the public deficit. On the contrary, it stresses that part of the measures presented as cash flow measures could ultimately have an impact on the deficit as of this year and that all the measures to support activity announced by the Government, in particular certain sectoral plans for stimulus, have not been translated into this PLFR.

58. He noted that the structural deficit for 2020, as estimated by the Government, would be identical to that of 2019 (2.2 points of GDP) and would deviate significantly from the programming law. The structural deficit could also turn out to be higher than expected in this 3rd PLFR. Indeed, some of the expenses linked to the health crisis, considered temporary by the Government, could be extended beyond 2020. In addition, the assessment of potential GDP may be revised downwards due to possible losses of human capital brought about by the rise in unemployment and the consequences of the foreseeable rise in corporate bankruptcies and the fall in investments in production capacities, as well as the impact on productivity of the sustainable implementation of health protection.

59. The High Council notes that the forecast of the ratio of public debt to GDP is revised by more than 5 points compared to the previous PLFR and by 22 points compared to the initial finance law. This ratio would thus exceed 120 points of GDP at the end of 2020. This massive increase, which adds to an almost uninterrupted growth for 10 years, weakens the medium-term sustainability of public finances in France and calls for vigilance particular.

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In Paris, the 8 June 2020.

For the High Council of public finance,

The President of the Court of Auditors,

The President of the High Council of Public Finance

Pierre MOSCOVICI

Annex 1: Macroeconomic scenario associated with the 3rd PLFR for 2020

France economic forecasts		
	2019	2020
Goods and services, real terms	**Annual percentage change**	
Gross domestic product	**1,5**	**-11,0**
Households final consumption	1,5	-10,0
Final public consumption	1,7	-0,3
Grossd fixed capital formation	4,3	-19,3
Of which: Non-financial firmss	3,7	-24,2
Public aministrations	ND	ND
Households (excluding individual entrepreneurs)	1,8	-19,5
Imports	2,6	-15,5
Exports	1,8	-15,5
Contribution to real GDP growth	**As a percentage of GDP**	
Private domestic demand (excluding inventories)	1,5	-9,9
Public demand	0,7	-0,1
inventories	-0,4	-1,1
External Trade	-0,3	0.0
Price and nominal aggregates	**Annual percentage change**	
Consumer prices inflation index	**1,1**	**0,4**
Core inflation	0,8	0,4
Gross domestic product deflator	0,8	1,4
Nominal gross domestic product	2,5	-9,7
Productivity, employment and wages	**Annual percentage change**	
Market sector (excluding agriculture) :		
- Productivity	ND	ND
- Salaried employment	1,5	-4,1
- Average salary	2,0	-5,8
- Payrolls	3,5	-9,7
Total employment	1,0	-2,8
Non-financial corporate account	**Annual percentage change**	
Value Added	4,1	-12,5
Gross operating product	9,9	-20,6
Markup rate	33,2	30,1
Saving rate	23,2	21,6
Investment rate	24,5	21,4
Self-financing rate	94,6	101,0
Households account	**Annual percentage change**	
Total wage bil	2,9	-7,0
Gross disposable income	3,1	-1,4
Real gross disposable income	2,1	-1,4
Saving rate	14,9	22,3

Operations with the rest of the world	Annual percentage change	
Trade balance FAB-FAB (customs data)	-2,4	-1,3
Trade balance FAB-FAB (in billions of euros)	-58	-28
International context	**Annual percentage change**	
France export market	1,0	-12,8
Euro-dollar exchange rate	1,12	1,10
Brent Oil price (per baril in dollars)	64	33

Annex 2: Introductory article to the third amending finance bill for 2020

La prévision de solde structurel et de solde effectif de l'ensemble des administrations publiques pour 2020 s'établit comme suit :

En points de produit intérieur brut (PIB)	Exécution 2019	LFI 2020	Prévision 2020
Solde structurel (1)	-2,2	-2,2	-2,2
Solde conjoncturel (2)	0,2	0,1	-7,0
Mesures exceptionnelles et temporaires (3)	-1,0	-0,1	-2,3
Solde effectif (1 + 2 + 3)	-3,0	-2,2	-11,4

Exposé des motifs

En 2019, le déficit s'est élevé à 3,0 % du PIB, soit un ratio légèrement moindre que les 3,1 % prévus en sous-jacent de la LFI pour 2020 mais conforme à celui révisé en deuxième loi de finances rectificative pour 2020. À la suite de la publication des comptes de la Nation 2019 par l'INSEE révisant la croissance 2019 à la hausse de 1,3% à 1,5%, le solde structurel s'établit à -2,2 % du PIB en 2019 comme en 2018, contre -2,0% en sous-jacent de la LFR II. L'écart à la LFR II sur 2019 résulte uniquement de la révision des comptes nationaux publiée fin mai par l'INSEE.

En 2020, la crise sanitaire inédite que traverse la France et ses répercussions économiques et financières constituent des « circonstances exceptionnelles » au sens de l'article 3 du Traité sur la Stabilité, la Coordination et la Gouvernance, ainsi que l'a estimé le Haut Conseil des Finances Publiques dans son avis n°HCFP-2020-1 relatif au premier projet de loi de finances rectificative pour l'année 2020. Dans ce contexte macro-économique fortement dégradé, la prévision de solde public pour 2020 est revue en baisse, à -11,4 % du PIB, contre -2,2 % prévu dans la LFI pour 2020, -3,9 % dans la LFR I et -9,1 % dans la LFR II. Le solde structurel serait stable en 2020 (-2,2 % comme en 2019). En effet, la dégradation du solde par rapport à la LFI s'explique essentiellement par la dégradation conjoncturelle et l'effet des mesures exceptionnelles et temporaires prises face à la crise du Covid-19. Dans le détail le solde 2020 est affecté par :

(i) La révision en baisse de la croissance de l'activité en raison du contexte de crise sanitaire et de l'impact économique du confinement. L'estimation de la croissance de l'activité a été revue à -11,0%, contre +1,3% dans la LFI pour 2020 et -8,0% en LFR II, dans le contexte de crise déclenchée par l'épidémie de Covid-19, ce qui affecte les recettes d'impôts et de cotisations. Le solde conjoncturel passe ainsi de +0,1 % du PIB en LFI 2020 et -5,3% en LFR II à -7,0 % du PIB.

(ii) Les mesures de lutte contre l'épidémie de Covid-19 et ses conséquences économiques et sociales, détaillées ci-après, pour 57 Md€ de dépenses maastrichtiennes, soit -2,6 points de PIB effectif et -2,3 points de PIB potentiel, traitées comme mesures exceptionnelles et temporaires. Le total des mesures exceptionnelles et temporaires s'élève à -2,3 points de PIB potentiel, et inclut notamment en sus une convention judiciaire d'intérêt public importante datée de janvier 2020. Ce total s'établissait à -1,7 point de PIB potentiel en LFR II.

Les 57 Md€ de dépenses exceptionnelles maastrichtiennes face à la crise sanitaire, économique et sociale comprennent :

(i) Le financement des mesures exceptionnelles d'activité partielle pour 31 Md€, dont 20 ½ Md€ à la charge de l'État et 10 ½ Md€ à la charge des administrations de sécurité sociale (Unedic).

(ii) Des crédits supplémentaires pour financer les exonérations de charges prévues par le plan tourisme, à hauteur de 3 Md€ et d'autres dispositifs d'urgence pour faire face à la crise, notamment le plan en faveur du secteur automobile, pour 2½ Md€ de plus.

(iii) Le financement public du fonds de solidarité pour les entreprises pour 8 Md€, ainsi que le versement d'une prime pour les indépendants par la CPSTI pour 1 Md€.

(iv) Des dépenses exceptionnelles supplémentaires d'ONDAM estimées à 8 Md€ incluant les dépenses nécessaires à l'achat de matériel et de masques, les mesures sur les indemnités journalières, ainsi que les rémunérations exceptionnelles du personnel soignant et d'autres surcoûts liés à la crise.

(v) 1 ½ Md€ de crédits supplémentaires d'urgence portés par l'État.

(vi) 1 Md€ en faveur de l'inclusion sociale et de la protection des personnes fragiles ainsi que ½ Md€ au titre du décalage de la réforme de l'assurance chômage et la prolongation de droits pour les demandeurs d'emploi.

(vii) ½ Md€ d'avances remboursables pour soutenir les PME et ½ Md€ de crédits pour masques non chirurgicaux.

(viii) ½ Md€ pour l'utilisation immédiate des reports en arrière des déficits sur l'assiette de l'impôt sur les sociétés (« carry-back »).

Annex 3: The methods for estimating the structural balance of public administrations

The structural balance estimate

To assess the public finance path, the structural budget balance is usually considered. The structural balance is the **public balance adjusted for the direct impact of the economic cycle and exceptional events**. The public balance is thus divided into two components:

- A **cyclical component,** which reflects the impact of the economic cycle on public administrations' expenditure and revenue;
- A **structural component,** being what the public balance would be if domestic production were at its potential level.

The calculation of the cyclical and structural components of the public balance is based on the potential GDP estimate. Potential GDP is the "sustainable" output, i.e. the quantity that can be produced without having positive or negative impacts on inflation. The cyclical component of the public balance results from the cyclical variations in public revenue and expenditure, considered as follows:

- **On the revenue side**, only compulsory levies are assumed to be cyclical. The cyclical parts of the income tax, corporate income tax, social security contributions and other mandatory contributions are calculated separately based on the observed levels, the estimated output gap and the elasticity of each tax category to GDP growth3;
- **On the expenditure side**, only the unemployment compensation expenses are considered dependent on economic conditions. Their cyclical share is estimated, as for revenue, based on their elasticity to the output gap and the amounts observed.

The structural balance is calculated as the difference between the nominal public balance and the cyclical component estimate. Given the fact that compulsory levies and cyclical expenses account for about half of GDP and that their average elasticity is close to one, the cyclical component of the public balance is equal to just over half the output gap (for France). **A final correction is made to the structural balance in order to exclude certain events or actions** that have no lasting impact on the public balance. **However, there is no comprehensive definition of one-off and temporary measures and their assessment is partly based on interpretation.**

The components of the structural adjustment

The variation of the structural balance is known as "structural adjustment". A positive structural adjustment reflects a budgetary policy directed towards the medium term objective (-0.4 % for France as set by the programming law), when there initially is a deficit. Conversely, a negative structural adjustment reflects an expansionist budgetary policy, increasing the structural deficit.

In order to assess more sensibly the budgetary policy, the **structural adjustment is divided into two components**.

- **The structural effort, which measures the discretionary part of the structural adjustment, i.e. controlled by public decision makers, is made of**:
    - **the expenditure restraint**, which compares the public spending real growth(calculated with the GDP deflator) to the economy's potential growth. It has a positive contribution to the structural adjustment when public spending grows slower than potential GDP;
    - the new measures on compulsory levies.
- **The non-discretionary part** takes into account:
    - the impacts of **changes in revenue elasticities**: since the cyclical component of the public balance is based on average elasticities, the structural balance includes the effects of elasticity fluctuations around the long-term average value;

- the **changes in revenues other than compulsory levies.**

Annex 4 : The triggering of the general escape clause of the Stability and Growth Pact

In the health context linked to the Covid-19 epidemic and on a proposal from the Commission, the Council of the European Union announced on March 23, 2020 the triggering of the "general escape clause". Introduced in 2011 as part of the reform of the Stability and Growth Pact, this clause can be activated in the event of “an unusual circumstance beyond the control of the Member State concerned which has appreciable effects on the financial situation of public administration or in a period of severe economic recession affecting the euro area or the whole of the Union”[12].

This clause does not suspend the procedures of the Stability and Growth Pact. Nevertheless, it allows Member States and the European Union to take and coordinate budgetary measures necessary to cope with the "unusual circumstance" by departing from the budgetary requirements normally applicable. In the case of the preventive arm of the Stability and Growth Pact, States are thus "authorized to temporarily deviate from the adjustment trajectory with a view to achieving the medium-term budgetary objective [...] provided that the medium-term budgetary sustainability is not jeopardized”[13]. Furthermore, within the framework of the corrective arm of the Pact[14], the clause allows the Council of the European Union in particular to revise a recommendation addressed to a member state and to “extend, in principle by one year, the period provided for the correction excessive deficit”.

[12] Article 5 du règlement n°1466/97 du Conseil du 7 juillet 1997

[13] Article 6 du règlement n°1466/97 du Conseil du 7 juillet 1997.

[14] Article 3 et 5 du règlement (CE) n°1467/97 du 7 juillet 1997.