Haut Conseil des Finances Publiques

Opinion n° HCFP-2021-5

on the second amending budget bill for 2021 and on the revised budget bill and social security financing bill for the year 2022

29 October 2021

Summary

The Government has changed its macroeconomic and public finance forecasts for 2021 and 2022. This scenario takes notably into account significant new measures that were not included in the budget bill when it was introduced. The Government has therefore referred to the High Council the revised 2022 budget bill at the same time as it referred the second amending budget bill for 2021.

The High Council welcomes this new referral, that it called for in light of the macroeconomic and public finance scenario presented in the previous referral, and which allows for a more informed opinion on the 2022 budget bill (PLF).

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For 2021, the High Council considers that the Government's growth forecast (+6¼%), revised upwards by a quarter of a point compared to the initial PLF for 2022, should be exceeded, in view of the much better-than-expected results of the quarterly accounts for the third quarter that were released after the referral. For 2022, the growth assumption (+4.0%), unchanged from the initial PLF, remains plausible. The new developments since September - new measures to support purchasing power and investment and the deterioration of the international economic environment - work in opposite directions.

The High Council considers the Government's inflation forecast for 2021 to be plausible, but the forecast for 2022, which is unchanged despite the rise in energy prices and the marked improvement in the labour market since the initial PLF, seems too low. The employment and wage bill forecasts for 2021 and 2022, although revised upwards, also remain cautious in the light of the most recent data.

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The High Council considers that the Government deficit for 2021 presented in the amending budget bill (PLFR) could be slightly lower than forecast, notably due to an underestimation of the revenues based on the wage bill. For 2022, the dynamics of employment and of the wage bill also suggest higher public revenues, but the degree of uncertainty surrounding the expenditure forecast is important given the significant movements in new public spending. Their timing, pace and amounts remain to be specified at this stage. Overall, on the basis of the available information, the Government deficit forecast for 2022 can nevertheless be considered plausible.

The structural balance presented by the Government for 2022 would be -4.0 points of GDP by applying the potential GDP assumption of the current programming law (LPFP), and would thus be 3.2 points lower than that set out in this law, that is a significant deviation as defined by the organic law of December 2012. Nevertheless, the High Council considers that the exceptional circumstances clause, triggered in spring 2020, may still justify deviations

from the programmed path in 2022.

However, the current LPFP is an outdated reference for assessing the public finance trajectory. The structural balance calculated on the basis of the Government's latest estimate of potential growth, revised to take account of the consequences of the health crisis, stands at -5.0 points of GDP, which is a deviation of more than 4 points from the medium-term budgetary objective (MTO) for public finances that France has set to itself in the LPFP and a deterioration of 2.5 points in the structural balance compared with 2019.

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The High Council notes that the decline in the debt ratio for 2022 in the revised PLF compared to the initial draft is stronger than expected (-1.8 points to 113.5 points of GDP, instead of -1.5 points). However, this decrease is not the result of a reduction in the general Government deficit but of Government cash management operations.

The High Council notes that, contrary to what it had advised in its opinion of 17 September 2021, the expected increase in revenue is not devoted to public debt reduction, but is, on the contrary, more than offset by increased spending or tax relief measures. It stresses once again that the medium-term sustainability of the public debt, forecast to increase by 16 points of GDP in 2022 compared to 2019, calls for the utmost vigilance.

1. The Government referred to the High Council on October 22, 2021, pursuant to Article 15 of the Organic Law No. 2012-1403 of December 17, 2012 on public finance programming and governance, to give an opinion on the macroeconomic forecasts as well as on the consistency on the multi-year trajectory of the structural balance associated with the second amending finance bill (PLFR) for 2021.

2. In the same referral, pursuant to Article 16 of the aforementioned Organic Law No. 2012-1403, the Government referred to the High Council a revision of the draft Budget bill for 2022 including a revision of the macroeconomic assumptions on which these drafts were based.

3. This double referral is accompanied by responses to questionnaires sent by the High Council to the competent administrations.

4. As permitted by Article 18 of the Organic Law of 2012, the High Council heared representatives of the Treasury and Budget Department on October 25, 2021.

5. The High Council drew on the latest economic information and forecasts produced by a range of international and national organizations and institutions. In addition, it took into account the publication by Insee on October 29 of the first estimate of the third quarter accounts and the provisional results of the October consumer price index.

6. After deliberation at its meeting on October 29, 2021, the High Council adopted this opinion in response to this double referral.

1. The macroeconomic scenario

7. The High Council successively assesses the new assumptions for activity growth, inflation, employment and private sector wage bill for 2021 and 2022.

a) Activity growth

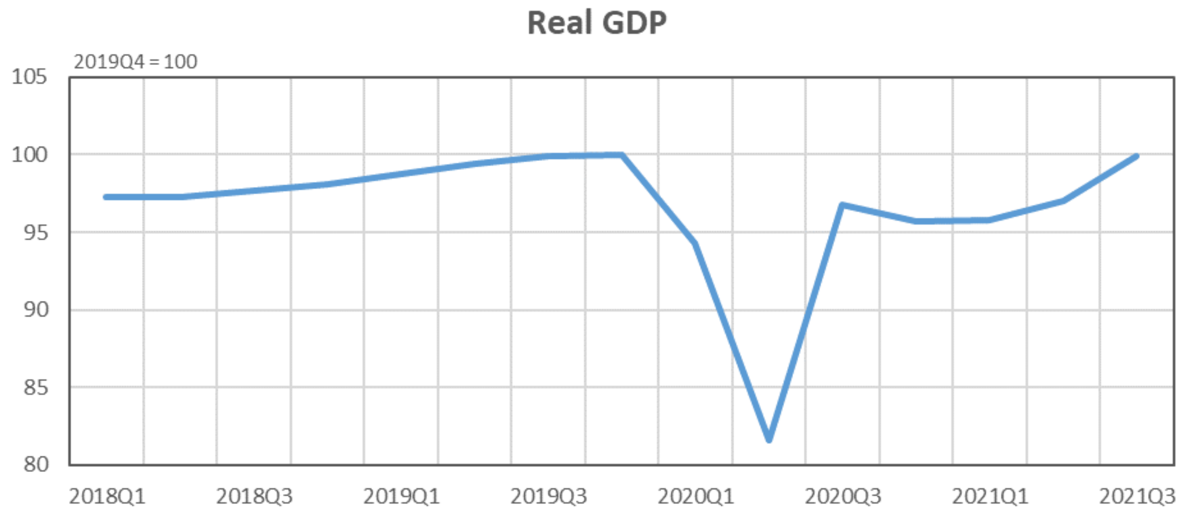
8. For 2021, the Government projects real GDP growth of 6.75%, revised up a quarter point from the 2022 budget bill, and 4.0% in 2022, unchanged from the PLF.

GDP growth forecasts for 2021-2021

	France			Euro Area		
	2021	**2022**	**2022/2019**	**2021**	**2022**	**2022/2019**
Government (PLF 2022 - September 2021)	**6,0**	**4,0**	**1,4**	**4,9**	**4,4**	**2,4**
Banque de France (September 2021)	6,3	3,7	1,5	5,0	4,6	2,7
OECD (September 2021)	6,3	4,0	1,7	5,3	4,6	3,0
IMF (October 2021)	6,3	3,9	1,6	5,0	4,3	2,5
Observatoire français des conjonctures économiques (OFCE) (October 2021)	6,3	4,1	1,9	5,1	4,8	3,0
Rexecode (October 2021)	6,3	3,5	1,2	5	3,9	2,1
Consensus Forecasts (October 2021)	6,1	3,8	1,3	5,1	4,4	2,6
Government (revised PLF 2022 - October 2021)	**6,25**	**4,0**	**1,7**	**4,9**	**4,4**	**2,4**

Source: HCFP based on forecasts from international organizations and business and consumer organizations. The columns '2022/2019' feature for each forecast the level of GDP reached in 2022 compared to the level observed in 2019.

9. In its opinion on the PLF and PLFSS for 2022, the High Council considered that the Government's growth forecast for 2021 could be deemed as prudent in the light of the latest Insee and Banque de France forecasts. In fact, the Government's new forecast for 2021 has been revised upwards by a quarter of a point and is now close to that of these two organizations. However, the publication by the Insee of the quarterly accounts for the third quarter on October 29 – after the Government's referral – leads expect this estimation to be exceeded. The GDP carry-over from the third quarter of 2021, that is the growth rate that would be recorded over the whole of 2021 if GDP were stable in the fourth quarter, is already 6.6%. GDP has thus in the third quarter of 2021 almost returned to its level in the fourth quarter of 2019.



Source: Insee

10. The Government has not changed its growth forecast for 2022, which remains at 4.0%. The High Council considered this estimation plausible in its opinion on the PLF and PLFSS for 2022. Since then, the Government has taken into account various new measures to support purchasing power and investment that are likely to boost activity growth in 2022. Conversely, French growth is likely to suffer from the deterioration of the global economic environment, marked by persistent supply difficulties. In addition, energy prices have continued to rise. Altogether, this led to a loss in dynamism of the global economy, as evidenced by weaker than expected economic results (third quarter GDP in the US, the UK China and Germany). Inflationary pressures have led some central banks (notably the Fed, the Bank of England and the Bank of Canada) to announce an earlier-than-expected tightening of their monetary policy. These announcements are pushing up interest rates and could lead to tensions in financial markets. Overall, these opposing elements lead the High Council to believe that the Government's growth forecast for 2022 remains plausible.

11. **The High Council considers that the Government's growth forecast for 2021 (+6¼%), revised upwards by a quarter of a point compared to the initial PLF for 2022, should be exceeded, in view of the much better-than-expected results of the quarterly accounts for the third quarter that were released after the referral. For 2022, the growth assumption (+4.0%), unchanged from the initial PLF, remains plausible. The new developments since September - new measures to support purchasing power and investment and the deterioration of the international economic environment - work in opposite directions.**

b) The rise in consumption prices

12. The Government has not changed its forecast for the increase in consumer price index for 2021 and 2022: +1.5% on yearly average in 2021 and 2022, after +0.5% in 2020.

Consumer price index (CPI)

Variations in %	Government's forecast (yearly average)			
	2019	**2020**	**2021**	**2022**
Aggregate index	1.1	0.5	1.5	1.5
Core inflation index	0.8	0.6	1.1	1.5

Source: revised Budget bill for 2022

13. In its opinion on the PLF and PLFSS for 2022, the High Council considered the Government's inflation forecast for 2021 and 2022 realistic. However, energy prices increased sharply since then, which all else being equal, should lead to an upward revision of the forecast for 2022. The price of a barrel of Brent crude oil was in October 2021 about 15$ above the level used by the Government in its estimation (84$ against 69$). Thus, according to the simulations presented by the Government in the April 2021 Stability Program, this could lead to an increase in prices of nearly 0.5 percentage points in 2022 (see box below), should the barrel price remain at this level over the entire forecast horizon. The higher growth forecast and the stronger improvement in the labor market than expected in the initial forecast associated to the PLF for 2022 are also likely to increase underlying inflation in 2022 relative to that forecast. The publication by Insee of the provisional results of the consumer price index on October 29, after the referral, confirms the upward trend in inflation and raised the risk of a slight overshoot of the inflation forecast for 2021.

14. **The High Council considers the Government's inflation forecast for 2021 to be plausible, but the forecast for 2022, which is unchanged despite the rise in energy prices and the marked improvement in the labour market since the initial PLF, seems too low.**

What impact on the forecast of higher oil prices?

Oil prices are a salient parameter in macroeconomic and budgetary forecasts. A change in the price of oil has a direct impact on public finances through energy taxation, and an indirect one through its effect on the behavior of economic agents (household consumption, especially of fuel, costs and prices of firms, etc.).

When preparing its economic forecasts, the French Treasury usually assumes that oil prices will stabilize at their most recent level. This conventional choice results from the difficulty in predicting the evolution of oil prices and is shared by many institutions.

The Government has not changed its inflation forecast in the revised macroeconomic framework for the Budget bill for 2022, and in particular kept the oil prices assumption underlying the initial framework presented in September 2021, at $69 per barrel of Brent, corresponding to the average level in August. However, oil prices have averaged around $84 per barrel since the beginning of October, that is almost $15 more[1].

It is possible to estimate, all other things being equal, the impact that adjusting oil prices to their October level would have on the government's forecast. This can be done based on the simulations presented in the April 2021

[1] The euro/dollar change rate also influences the economy, but it has been almost perfectly stable between August and October 2021.

stability program, which detail the consequences for the government's scenario of a different oil price assumption, using the Mésange model developed by Insee and the Treasury[2].

The effect on the major macroeconomic aggregates, although modest, is not negligible. All else being equal, updating the oil price scenario would lead to a 0.5 point increase in inflation in the first year, a 0.2 point decrease in GDP growth and a 0.1 point increase in the public deficit related to the GDP loss. The new measures, incorporated in the revised PLF for 2022, designed to offset the effects of energy inflation on household purchasing power, mitigate somewhat its impact on GDP, but increase the public deficit.

The impact of an average increase in oil prices over the year of $15 per barrel

	$15 increase
Effect on GDP	-0.2
Effect on inflation	+0.5
Effect on the primary balance	-0.1

Note: impacts computed from "$10 oil price increase" variant over the first year, rounded to the tenth.
Source: Stability program, April 2021

c) Private sector employment and wage bill

15. The private sector wage bill is a salient determinant of government revenue. In its opinion on the PLF and PLFSS for 2022, the High Council considered the employment and wage bill forecasts for 2021 too low. They did not take into account the latest available information. The Government has indeed raised significantly its forecast for the wage bill in the non-agricultural market sector in 2021, from 6.2% to 7.2%.

16. However, this new forecast of wage bill growth still appears low in view of its recent dynamics, as evidenced by recent data from the Acoss[3]. In its financial forecast for 2021-2023 published on October 22, 2021, the Unedic for example assumes a 8.0% growth of the wage bill for 2021, for a very similar field. The Acoss data do not provide a breakdown between employment and wages per capita beyond the second quarter. Nonetheless, they suggest that employment, and perhaps the average wage per capita, will rise more strongly than expected by the Government in 2021.

Non-agricultural private sector wage bill (evolution in %)

	2020	**2021**	**2022**
Private sector employees	-1,5	1,9	1,1
Average wage	-4,9	5,2	4,7
Wage bill	-6,2	7,2	5,9

Source: revised Budget bill for 2022 forecasts

17. For 2022, the Government has revised downwards its forecast for average wage growth by half a percentage point (4.7% against 5.2% in the PLF for 2022), due to the assumption – unchanged from the initial PLF – that value added sharing will return to its 2019 level in 2022.

[2] Bardaji J., B. Campagne, M-B. Khder, Q. Lafféter, O. Simon, A.-S Dufernez, C. Elezaar, P. Leblanc, E. Masson, H. Partouche, *Le modèle macroéconométrique Mésange : réestimation et nouveautés*, Insee, Working paper, N°G2017/04, May 2017.

[3] Total payroll was +3.5% higher in July 2021 compared to July 2019 and +3.9% higher in August 2021 compared to August 2019. A continuation over the remaining months (September to December) of the difference recorded in July 2019 compared to the same months in 2019 (the last year in which the payroll profile is not disrupted by the effects of the health crisis) would lead to a wage bill growth of more than 8%. September's hiring intentions and the high level of employment sentiment in Insee's business surveys lend credence to this assumption, although lower year-end bonuses than in 2019 could limit this increase somewhat.

However, the economic situation on the labor market (the drop in unemployment rate, greater recruitment difficulties, even labor shortages in certain high pressures occupations) and the dynamics of imported inflation weaken that assumption. Average wage could thus be higher in 2022 than forecasted by the Government.

18. The Government has left its forecast for net job creation in 2022 generally unchanged (60,000 between the end of 2021 and the end of 2022 against 64,000 in the initial PLF). This scenario is possible, but is not a foregone conclusion given recent employment dynamics. It assumes a partial recovery of the productivity loss because of the crisis recorded so far, compared to a pre-crisis productivity trend estimated by the Government at 1.2% per year. In an unchanged growth scenario, job creation would be higher in 2022, if the productivity trend were lower, as some institution estimate.

19. Overall, the Government forecast for the growth of the total payroll in 2022 is subject to rather upwardly oriented contingencies, both for the evolution of the average wage and for that of the employment.

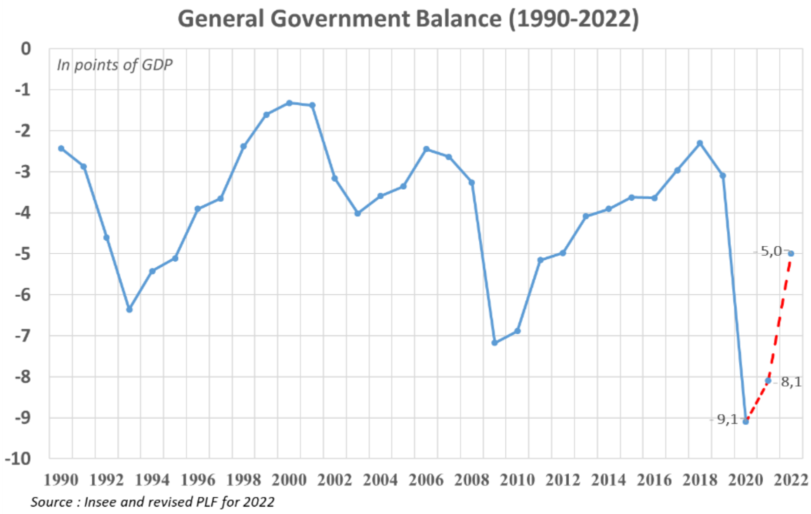
20. **The High Council considers that the employment and wage bill forecasts for 2021 and 2022, although revised upwards, remain cautious in the light of the most recent data.**

2. Remarks on public finances forecasts for 2021 and 2022

21. The High Council assesses the risks to the public balance, then examines the consistency of the structural balance[4] with the multi-year targets of the public finance programming law and finally discusses developments in the public debt.

1- Assessment of risks to the public balance

22. The government has revised downwards its public deficit forecast[4] for 2021 by €6.9bn (that is almost 0.3 points of GDP, from 8.4 to 8.1 points of GDP) in the context of the amending budget bill, and upwards by €4.8bn (i.e. 0.2 points of GDP, from 4.8 to 5.0 points of GDP) for 2022.



a) The public balance for 2021

23. In 2021, the overall increase in expenditure excluding tax credits is estimated at 4.8% in value (or 4.3% in volume[5]), after an increase of 6.8% in 2020. Expenditure would thus represent 59.7 points of GDP in 2021, a ratio lower than the level reached in 2020 (60.8 points), but still 5.9 points higher than in 2019 (53.8 points of GDP). Compared with the forecasts in the initial 2022 budget bill, total expenditure by the public sector is revised downwards by €1.2bn. New expenditures, the "inflation allowance" (€1.5bn[6]) and "other measures to preserve purchasing power" (€0.5bn), as well as a higher-than-expected debt burden (€0.3bn), are more than offset by the removal of the allowance for accidental and unforeseeable expenditure (€1,5bn)[7], lower charges for the public electricity service due to higher energy prices[8] (-€1.5 bn), an expected under-execution of solidarity fund expenditures (-€0.2bn) and lower expected unemployment compensation expenditure (-€0.2bn).

[4] The structural balance is defined as the public balance adjusted for the direct effects of the economic cycle and exceptional events (see Annex 3).
[5] Deflated by GDP prices.
[6] The total announced amount of €3.8bn would be partly paid in 2021 (€1.5bn) and partly in 2022 (€2.3bn).
[7] The allocation for accidental and unforeseeable expenditure (DDAI) is a programme intended to cover unforeseen expenditure during the year when the finance law is voted. The public finance scenario associated with the budget bill for 2022 considered that this programme would be mobilised by the end of 2021 to cover unspecified expenditure. In fact, some new expenditure (the "inflation allowance" and other measures to preserve purchasing power) has been approved but it is subject to new appropriations rather than a replenishment from the DDAI.
[8] See the deliberation of the Energy Regulatory Commission of 7 October 2021.

24. Government spending in budgetary accounting is broadly stable compared to the September forecasts: the total spending target (Odete) stands at €535bn that is €0.4bn above the level expected in the initial 2022 budget bill. The amount of this expenditure is still subject to uncertainty, particularly because the mechanism for implementing the "inflation allowance" - which will influence the distribution of its cost between the 2021 and 2022 fiscal years - has yet to be specified.

25. Concerning social security administrations, the expenditure forecasts are very similar to those of September, with a slight downward revision of unemployment benefit expenditure, linked to the increased dynamism of employment. Expenditure under the Ondam[9] is expected to rise by 7.4% in 2021, the same rate as that forecast in the 2022 Social Security financing bill.

26. Local authority spending forecasts for 2021 are unchanged from those of September. They are consistent with the accounting data available up to September.

27. The government has revised upwards its forecast for compulsory levies for 2021 by €4.5bn. This revision mainly reflects, for €2.9bn, the impact on social security contributions and levies of the revision of the wage bill and the inclusion of better-than-expected accounting data for transfer taxes (+€0.8bn) and VAT (+€1.6bn).

28. On this basis, the growth in VAT revenue (+11.8%) continues to diverge from that of the corresponding tax base (+8.4%), as reflected in the government's macroeconomic forecasts, although the latter has also been revised upwards in line with the growth in activity. However, the latest data from Insee's quarterly accounts suggest an increase in the growth of the tax base, and thus some reduction in this gap; given the accounting data for the first nine months of the year, the Government's forecast can be considered reasonable.

29. The forecast for the corporate tax remains, at this stage of the year, one of the major sources of uncertainty and has not been revised since the initial budget bill for 2022. The gross operating surplus (GOE) of companies could be stronger than forecast in the budget bill, with the impact of higher-than-expected value added, as suggested by the quarterly accounts, more than offsetting the upward revision of both the wage bill and energy input prices. The government's forecast implicitly assumes a revenue of the fifth instalment, which is based on the results of the current year, consistent with the rebound in activity.

30. Finally, the upward revision of revenue from social contributions and levies is probably insufficient, due to the likely underestimation of the wage bill.

31. **The High Council considers that the Government deficit for 2021 presented in the amending budget bill (PLFR) could be slightly lower than forecast, notably due to an underestimation of the revenues based on the wage bill.**

[9] The Ondam (“objectif national des dépenses d’assurance maladie”) is a target set for a big part of healthcare expenditure.

b) The public balance for 2022

32. For 2022, the government has revised upwards its forecast for public spending, excluding tax credits, by €5.3bn compared to the initial budget bill. This increase is the result of new spending of €7.8bn, including in particular measures to support purchasing power for €3.5bn (inflation allowance, compensation to energy suppliers for the freezing of their prices)[10] and new intervention spending for €4bn (France 2030 public investment plan, measures for the development of skills and integration into employment, new active measure for young people). This new spending is partially offset (€2.6bn) by lower public spending resulting from the rise in energy prices (lower public service charges for electricity)[11] and a larger drop in unemployment benefit spending than was anticipated in the initial budget bill.

33. In total, public spending would amount to €1 444bn, that is 55.7 points of GDP in 2022, down by 4 points compared to 2021 but up by 1.9 points compared to 2019. While some of the new spending is not intended to be permanent, particularly the measures to support purchasing power, some of it will continue over time (France 2030 plan, measures to develop skills and promote integration into employment).

34. This additional expenditure is mainly borne by the State budget. Thus, the drop in Government spending in national accounts, expected in 2022 due to the reduction in support and stimulus spending, would no longer be 7.9% as announced in the initial budget bill but 6.4%. In national accounting terms[12], State spending (excluding tax credits and transfers) would increase by €5.7bn, from €402.7bn to €408.4bn.

35. There is still considerable uncertainty about the evolution of State spending in 2022. Firstly, the distribution of the cost of the "inflation allowance" between 2021 and 2022 remains unclear. In addition, other State expenditures evolve according to energy market prices (electricity utility charges, compensation to gas suppliers for the freezing of their prices) and their amount is therefore uncertain. In addition, the rate of disbursement of the France 2030 plan is subject to the risks of delays in implementation that may have affected previous investment plans. Finally, the piling up of schemes for investment in skills and support for young people creates implementation risks.

36. Social benefits are revised slightly downwards by €0.6bn in 2022 compared to the September forecast (€0.3bn on pensions, due to the decision by the Agirc-Arrco to revalue pensions by 0.5% below inflation and €0.2bn on unemployment benefits due to an upward revision of employment levels). Expenditures to face the health crisis within the scope of the Ondam are forecasted at €5bn, after €14.8bn in 2021, although this amount is subject to uncertainties.

37. Local government spending forecasts remain unchanged from the September forecast.

38. The Government has revised its forecast of compulsory levies for 2022 slightly downwards (-€0.9bn). This decrease can be broken down into three main components: the decrease in the domestic tax on the final consumption of electricity (TICFE) for €5.9bn, the

[10] The total revenue and expenditure from the measures that support purchasing power and mitigate the impact of increasing recent price in the 2nd amending budget bill for 2021 and the revised 2022 budget bill are estimated at €11.4bn.

[11] These charges are mainly intended to compensate operators for the additional costs associated with the development of renewable energies. Thus, they decrease when market prices increase.

[12] In budgetary accounting, expenditure under the State's controllable standard would increase by €2 billion compared to the 2022 budget bill. The High Council of Public Finance has not been informed of the revised Odete (total expenditure target) for 2022.

impact on 2022 of the revision of compulsory levies in 2021 (+€4.8bn), and the impact on 2022 revenues alone of the revision of macroeconomic forecasts for 2021 (+€0.3bn).

39. A stronger increase in energy prices than expected by the Government could weigh on corporate earnings and thus on corporate tax revenues. However, the prospect of better earnings in 2021 than anticipated by the Government leads the High Council to consider the corporate income tax forecast as prudent. In addition, the Government does not include the positive effect on the 2022 income tax balance that would be expected from the upward revision of the wage bill in 2021.

40. Finally, payroll taxes (contributions, CDG, CRDS) are affect by the probable underestimation of the wage bill.

41. **For 2022, the dynamics of employment and of the wage bill suggest higher public revenues, but the degree of uncertainty surrounding the expenditure forecast is important given the significant movements in new public spending. Their timing, pace and amounts remain to be specified at this stage. Overall, on the basis of the available information, the Government deficit forecast for 2022 can nevertheless be considered plausible.**

2- Assessment of consistency with the multi-year structural balance orientations

42. Under the terms of the organic Law of December 17, 2012, the High Council must rule on the consistency of the structural balance trajectory used in the Budget bill for 2022 with that of the current programming law of January 22nd, 2018 for the years 2018 to 2022. Given the changes to the public balance and the level of GDP in 2022, the High Council also assesses the year 2022.

43. According to the same organic law, a structural balance deviation is considered significant when it represents at least 0.5% of GDP in a given year or at least 0.25% of GDP per year on average over two consecutive years.

44. The High Council must therefore refer to the potential growth as established by the programming law in force. Thus, the structural balance is computed in the Budget bill for 2022 with the same potential growth (1.25 % in 2020, 1.30 % in 2021 and 1.35 % in 2022) as in the programming law.

Public balance decomposition submitted by the Government

In points of GDP	**Revised PLF for 2022 (Oct. 2021)**			*LPFP (January 2018)*		
	2020	**2021**	**2022**	***2020***	***2021***	***2022***
Public balance	**-9.1**	**-8.1**	**-5.0**	***-1.5***	***-0.9***	***-0.3***
Cyclical component	-5.0	-2.3	-0.8	*0.1*	*0.3*	*0.6*
One-off and temporary measure	-2.8	-0.1	-0.2	*0.0*	*0.0*	*0.0*
Structural balance	**-1.3**	**-5.7**	**-4.0**	*-1.6*	*-1.2*	*-0.8*
Difference with the LPFP	***+0.3***	***-4.5***	***-3.2***			

Note: figures are rounded up to the nearest tenth, small errors may result from it. Source: Draft revised budget bill for 2022, programming law of 2018.

45. With these potential GDP data from the public finance programming law, the structural balance would deteriorate between 2020 and 2021 by 4.4 points of PIB, before restoring between 2021 and 2022 by 1.7 points. These staggered trends are due both to the exceptional nature of the changes in revenues and expenditure caused by the health crisis and to the methods used by the government[13] to calculate the structural balance. Compared with the draft budget bill presented in September, the structural deficit is improved by 0.1 point in 2021 and worsened by 0.3 point in 2022. The structural balance deviation from the January 2018 public finance programming law, which is still in force today, amounts to 4.5 points of GDP in 2021 and -3.2 points in 2022, and is therefore significant in the sense of the 2012 organic law.

46. The Government has maintained, in the revised macroeconomic framework of the 2022 budget bill, the estimate of the loss of potential GDP that it had retained in September 2021 for the 2022 budget bill. Thus potential GDP would be 1.75 percentage points lower in 2022 than in the public finance programming law path, and then grow at the same rate as in the public finance programming law (+1.35% per year). The downward revision of potential growth compared to the public finance programming law assumption would, all other things being equal, lead to an improvement in the cyclical balance of almost one point in 2021 and 2022 and a corresponding increase in the structural deficit. In 2022, the structural balance would thus be at -5.0 points of GDP instead of -4.0 points of GDP with the potential growth of the public finance programming law.

47. The government's assessment of the level and growth of potential GDP in 2021 and 2022 is surrounded by particularly high uncertainties due to the assumptions that are needed about the impact of the health crisis, which is still difficult to assess. The assessment of the resulting structural deficit is thus likely to be revised when this impact will be better assessed.

48. As the High Council noted earlier, the structural balance estimates presented by the government in the revised 2022 budget bill can only be interpreted in a relevant manner for the

[13] In 2020, the choice was made to record the emergency measures (of the order of 3 points of GDP) as temporary expenditure, leading to an improvement in the structural balance in 2020, even though the government provided very significant budgetary support for economic activity. In 2021, these emergency measures are no longer considered as temporary measures and are therefore integrated into the structural balance. This contributes to the very sharp deterioration of the structural balance observed in 2021, which therefore does not reflect the real evolution of the public finance situation.

year 2022 in comparison with 2019. This is due to the analytical difficulties associated with the exceptional economic situation and the choices made by the government in terms of the registration of support measures. In total, the structural deficit would deteriorate by around 2.5 points of GDP between 2019 and 2022 with the revised potential GDP, including 1.2 points of GDP of measures from the support and recovery plans, which are not long-lasting, but 1.3 points of more permanent deterioration. In this framework, the output gap would be slightly positive in 2022 and the public deficit (-5.0 points of GDP) would then be entirely structural in nature.

Public balance decomposition with the actualized potential growth hypothesis

In points of GDP	**2019**	**2020**	**2021**	**2022**
Public balance	**-3.1**	**-9.1**	**-8.1**	**-5.0**
Cyclical component	0.4	-4.3	-1.3	0.2
One-off and temporary measures	-1.0	-2.8	-0.1	-0.2
Structural balance	**-2.5**	**-1.9**	**-6.6**	**-5.0**

Source: Revised budget bill for 2022

49. **Under the terms of the Organic Law of 17 December 2012, the High Council must give its opinion on the consistency of the structural balance path with that of the current programming law of 22 January 2018 for the years 2018 to 2022.**

50. **The High Council notes that the structural balance presented by the Government for 2022 would be -4.0 points of GDP by applying the potential GDP assumption of the current programming law (LPFP), and would thus be 3.2 points lower than that set out in this law, that is a significant deviation as defined by the organic law of December 2012. Nevertheless, the High Council considers that the exceptional circumstances clause, triggered in spring 2020, may still justify deviations from the programmed path in 2022.**

51. **The High Council recalls that the current LPFP is however an outdated reference for assessing the public finance trajectory. The structural balance calculated on the basis of the Government's latest estimate of potential growth, revised to take account of the consequences of the health crisis, stands at -5.0 points of GDP, which is a deviation of more than 4 points from the medium-term budgetary objective (MTO) for public finances that France has set to itself in the LPFP and a deterioration of 2.5 points in the structural balance compared with 2019.**

3- The public debt

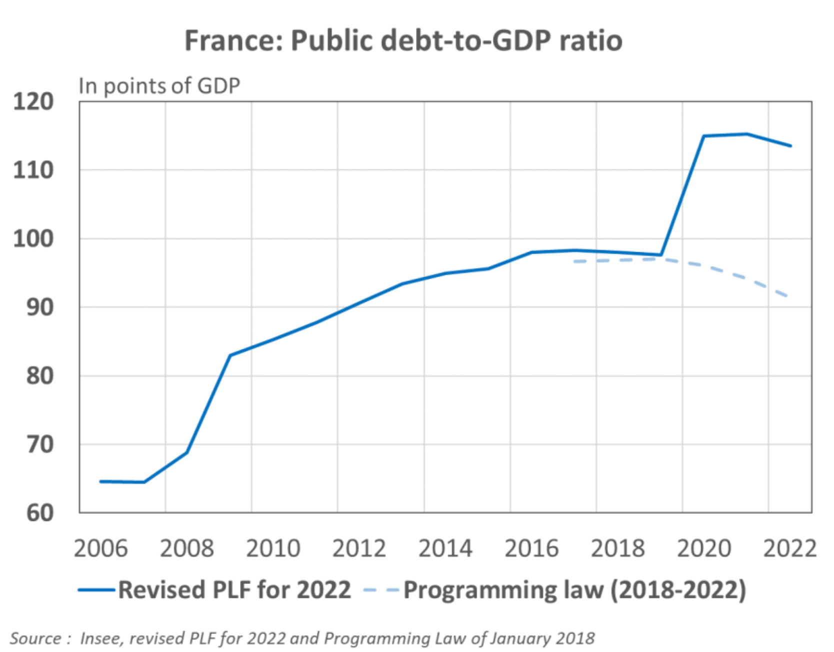
52. According to the Government’s forecast, the public debt ratio would be almost stable in 2021 at 115.3 points of GDP, and would fall by 1.8 points in 2022, to 113.5 points of GDP. As a result of high growth, the debt-stabilizing deficit (-6.0 points of GDP) would in fact be higher than the expected deficit (-5.0 points of GDP).

53. The decrease in the public debt ratio in 2022 is slightly higher in than in the PLF of September (-1.8 points against -1.5). This larger decrease is not the result from a reduction in the public deficit, but of an assumption of a larger consumption of government cash in 2022. The public debt forecast for 2022 is also affect by the uncertainties surrounding the deficit.

Public debt and deficit

In points of GDP	**2020**	**2021**	**2022**
Public balance	-9.1	-8.1	-5.0
Public debt	115.0	115.3	113.5

Sources: Insee and revised Budget bill for 2022



How the combined large scale evolutions of public finances and GDP shape the dynamic of the public debt ratio between 2020 and 2022

Public debt as a share of GDP increased sharply in 2020, from 97.5 points of GDP in 2019 to 115 points of GDP in 2020. According to the Government, the debt ratio would be almost stable in 2021 before declining by 1.8 points to 113.5 points of GDP in 2022.

The significant increase in the public debt ratio in 2020 can be broken down into four factors, all of which contribute to the increase of the ratio that year:

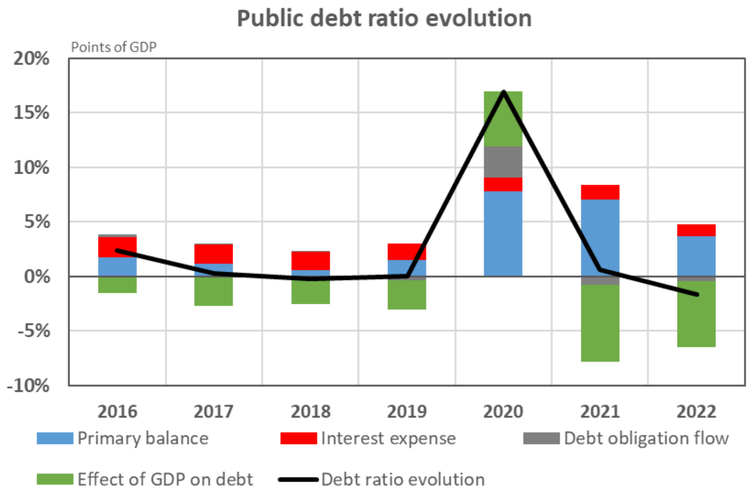
- a higher interest burden of 1.3 points of GDP;
- a primary deficit, i.e. excluding interest charges, of 7.8 points of GDP;
- factors that affect debt and the Government balance differently in national accounts (so called “debt-flows”), reflecting in particular the sharp rise in the Government’s cash position in 2020, amounting to 2.8 points of GDP;
- the contraction in the value of GDP in the denominator of the ratio (-5.5%), which increases the debt burden inherited from the past by around 5 points of GDP.

In 2021 and 2022, the evolution of the debt ratio reflects the effect of factors working in opposite directions. The public deficit still contributes to the increase in the debt ratio, but this effect is largely offset by the recovery of GDP in value terms, which reduces the burden of the debt inherited from the past.

In 2021, the public debt ratio estimated by the Government would slightly increase:

- the significant rebound of GDP in value terms would reduce the burden of the debt inherited from the past by around 7 points of GDP;
- debt flows would contribute to reducing the debt burden by 0.5 points of GDP;
- but the primary deficit would still increase the debt by 6.7 points of GDP;
- and, as in 2020, interest charges would contribute to increasing the debt by 1.3 points of GDP.

In 2022, the projected decrease in the debt ratio (-1.8 points of GDP) is due to the increase in real GDP (+5.5%). This dynamic reduces the debt inherited from the past by 6 percentage points, more than offsetting the public deficit, which, although decreasing significantly, still increases it by 5.0 percentage points[14]. Debt flows also contribute to a slight decrease in the ratio in 2022 (-0.8 points of GDP).



Sources: HCFP, Insee and revised Budget bill for 2022

Beyond its direct impact on the debt burden inherited from the past, the decline in GDP in 2020 also indirectly affects the evolution of the debt, via its impact on the primary deficit in relation to GDP.

- First, as with the debt, the decline in GDP increases the ratio of the nominal primary deficit to GDP trough a “denominator effect”. This effect is usually negligible becomes significant when there are large changes in GDP, as in 2020;

- In addition, the health and economic crisis the caused the decline in GDP is leading to an increase in some public expenditures and a decline in revenues. This impact is difficult to assess, however, particularly because the measures to support activity have a knock-on effect on revenues of uncertain magnitude[15], while some spending may have been prevented by the sanitary situation.

In 2021 and 2022, the sharp increase in GDP, in contrast, should reduce the primary deficit, but again in proportions that are difficult to assess.

54. **The High Council notes that the decline in the debt ratio for 2022 in the revised PLF compared to the initial draft is stronger than expected (-1.8 points to 113.5 points of GDP, instead of -1.5 points). However, this decrease is not the result of a reduction in the general Government deficit but of Government cash management operations.**

55. **The High Council notes that, contrary to what it had advised in its opinion of 17 September 2021, the expected increase in revenue is not devoted to public debt reduction, but is, on the contrary, more than offset by increased spending or tax relief measures. It**

[14] The public deficit breaks down to a primary deficit of 3.9% and interest charges of 1.1% in 2022.
[15] See the study note no. 2021-01 of the Permanent Secretary of the High Council of public finances, *Le coût net des mesures économiques et sociales exceptionnelles en 2020*.

stresses once again that the medium-term sustainability of the public debt, forecast to increase by 16 points of GDP in 2022 compared to 2019, calls for the utmost vigilance.

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This opinion will be published in the *Official Journal* of the French Republic and submitted to the National Assembly.

Done in Paris, October 29, 2021.

For the High Council of public finance,
The first president of the Court of Auditors,
President of the High Council of public finance

Pierre MOSCOVICI

Annex 1: Macroeconomic scenario attached to the second PLFR for 2021 and the revised PLF for 2022

Actualized economic forecasts for France *(difference with the 2022 Budget bill)*	2020		2021		2022	
Goods and services in volume						
Gross domestic product (wda)	**-8.0**	(0.0)	**6.25**	(0.25)	**4.0**	(0.0)
Households final consumption	-7.2	(0.0)	4.5	(0.4)	7.0	(0.0)
Government final consumption	-3.2	(0.0)	6.4	(-0.1)	-1.5	(0.0)
Gross fixed capital formation	-8.9	(0.0)	12.6	(0.2)	4.7	(0.0)
Of which : Non-financial corporates	*-8.1*	(0.0)	*12.2*	(0.0)	*5.1*	(0,0)
Public administrations	*-4.4*	(0.0)	*13.0*	(1.0)	*1.6*	(-0,7)
Households (excluding individual entrepreneurs)	*-12.2*	(0.0)	*15.8*	(0.1)	*3.5*	(0,4)
Imports	-12.2	(0.0)	9.2	(0.2)	10.4	(0.0)
Exports	-16.1	(0.0)	8.6	(0.0)	10.0	(0.0)
Contribution to GDP growth in volume						
Private domestic demand (excluding stocks)	-5.8	(0.0)	4.8	(0.3)	4.8	(0.1)
Public demand	-0.9	(0.0)	2.1	(0.0)	-0.3	(0.0)
Inventories	-0.2	(0.0)	-0.3	(0.0)	0.0	(0.0)
External trade	-1 1	(0.0)	-0 3	(0.0)	-0 4	(0.0)
Prices and nominal aggregates						
Consumer price inflation index	**0.5**	(0.0)	**1.5**	(0.0)	**1.5**	(0.0)
Core inflation	0.6	(0.0)	1.1	(0.0)	1.5	(0.0)
GDP deflator	2.5	(0.0)	0.5	(0.0)	1.4	(0.0)
Nominal gross domestic product (wda)	-5.7	(0.0)	6.7	(0.2)	5.5	(0.0)
Productivity, employment and wages						
Market sector excluding agriculture :						
- Effective labor productivity	-8.1	(0.0)	4.9	(-0.1)	3.6	(-0,3)
- Salaried employment (natural persons)*	-1.5	(0.0)	1.9	(0.4)	1.1	(0,3)
- Salaried employment (AA.in thousands)*	-259	(0.0)	325	(80)	195	(52)
- Salaried employment (y-o-y. in thousands)*	-356	(0.0)	458	(131)	60	(-4,0)
- Average per capita wage (APCW)	-4.9	(0.0)	5.2	(0.4)	4.7	(-0,5)
- Purchasing power of the APCW	-5.3	(0.0)	3.6	(0.4)	3.1	(-0,6)
- Wage bill	-6.2	(0.0)	7.2	(1.0)	5.9	(-0,2)
Total employment (AA, in thousands)*	-0.6	(-0.3)	1.5	(0.3)	0.8	(0.1)
Total employment (y-o-y, in thousands)*	-263	(90)	492	(115)	101	(-29)
Non-financial corporates' accounts						
Markup rate (GOP/AV)	**31.8**	(0.0)	**34.4**	(-0.3)	**33.2**	(0.0)
SAving rate (savings/AV)	21.9	(0.0)	24.9	(-0.3)	24.1	(0.0)
Investment rate (GFCF/AV)	24.6	(0.0)	25.7	(-0.4)	25.5	(-0.4)
Self-financing rate (savings/GFCF)	89.1	(0.0)	96.9	(0.5)	94.6	(1.6)
Housholds' accounts						
Gross disposable income (GDI)	1.0	(0.0)	4.1	(0.4)	2.4	(-0.1)
Purchasing power of the GDI (consumption deflator)	**0.4**	(0.0)	**2.6**	(0.4)	**0.9**	(-0.1)
Saving rate (savings/GDI)	21.4	(0.0)	20	(0.0)	15.1	(-0.1)
Operations with the Rest of the world						
Trade balance FOB-FOB (Douanes figures, in points of GDP)	-2.8	(0.0)	-3.5	(0.0)	-3.7	(0.0)
Trade balance FOB-FOB (Douanes, €Bn)	-65	(0.0)	-86	(-0.9)	-96	(-1.0)
International context						
Global demand addressed to France	-6.8	(0.0)	10.4	(0.0)	4.9	(0.0)
Euro-dollar exchange rate	1.14	(0.0)	1.19	(0.0)	1.17	(0.0)
Oil prices (Brent baril in dollars)	42	(0.0)	68	(0.0)	69	(0.0)

Employment in the sense of employment estimations (Estel)

Annex 2: Introducy article of the PLFR II for 2021

The forecasts of the structural and actual balance for all public administrations for 2021 are as follows:

In points of potential GDP* of the LPFP framework	**2020 execution**	**2021 forecast**
Structural balance (1)	-1.3	-5.7
Cyclical balance (2)	-5.0	-2.3
One-off and temporary measures (3)	-2.8	-0.1
Actual balance (1 + 2 + 3)	-9.1	-8.1

(*) Amounts in this table are rounded to the nearest tenth; errors between the actual balance and the sum of its components can result from this principle.

Explanatory statements

This article presents, in accordance with Article 7 of the Organic Law n°2021-1403 of December 17, 2012 relating to the programming and governance of public finances, the forecast of the structural balance and the effective balance of all public administrations for 2021.

The public balance forecast for 2021 is now -8.1% of GDP, compared with -8.4% of GDP projected in the 2022 Budget bill.

Public finance forecasts have been updated to account for the following elements:

- The upward revision of 0.25 points of GDP growth in volume (from +6.0% to +6.25%) and its consequences on revenues, the latter having also been revised to take into account the latest accounting data;
- Measures taken to address inflation, particularly in the energy sector;
- The 2021 end-of-management plan underlying this second revised Budget bill (PLFR) of the year.

The improvement of the 2021 public balance compared with the 2022 Budget bill results from the following elements:

- 0.2 point of GDP increase in revenues due to the upward revision of GDP and the wage bill (social contributions and levies). This revision also takes into account tax receipts at the end of September, which confirm that certain revenues (notably VAT and DMTO) have held up well beyond the simple revision of the level of activity;
- +0.1 point of GDP of other new information, notably in revenues excluding compulsory levies.

The structural balance in 2021 would be -5.7% of GDP, compared with -5.8% in the Budget bill for 2022. The structural decomposition of the current article relies on potential growth hypothesis from the programming law (LPFP) 2018-2022. One-off and temporary measures excluded from the structural balance are those described in the programming law, as well as the loss experience of the EIB and “state secured loans” guarantees.

Methodology:

The magnitude of the crisis makes certain methodological issues related to the decomposition of the public deficit significant, and clarifications can be made to the figures presented in this article.

Potential growth corresponds to the path of activity that is sustainable without tensions in the economy. Assumptions on the computation of potential GDP are described in the programming law of January 22, 2018. The discrepancy between the real level of output (effective GDP) and the potential level is called the “output gap”. It indicates the position of the economy within the cycle. In 2020 and 2021, this gap is negative and unusually large due to the crisis.

Each year, the public balance can be decomposed as:

- A cyclical component (reflecting the impact of the position within the economic cycle on public balance);
- One-off and temporary measures that are excluded from the evaluation the structural cycle, as they do not have any long-term effect on deficit;
- A structural component.

The public balance is measured in relation to actual GDP in 2021, i.e. €2,457.8 bn. This is the ratio referred to in Article 126 of the Treaty on the Functioning of the EU.

The structural balance and the balance of one-off and temporary measures are measured in terms of points of potential GDP, i.e. €2,557.0 bn. Thus, the structural balance in points of potential GDP is the ratio that would be observed once GDP returned to its potential, and after eliminating the effects of one-off and temporary measures. This property would not be verified if it were related to actual GDP. These concepts stem from European budgetary rules, the Growth and Stability Pact, and the Treaty on Stability, Coordination and Governance, whose organic law of December 17, 2012 on programming and governance of public finances applies in domestic law.

Between the deficit expressed in actual GDP points, the structural balance and one-off and temporary measures expressed in potential GDP points, the last component is a balance: this is the cyclical component presented in the introductory article. Thus, the differences between actual and potential GDP play out within the cyclical component, which is legitimate because the difference between these two quantities is cyclical in nature.

Annex 3: estimating the general government structural balance

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 growth[16];
- **On the expenditure side**, only the unemployment compensation expenses are considered dependent on economic conditions[17]. Their cyclical share is estimated, as for revenue, based on their elasticity to the output gap and the amounts observed.

The structural balance is computed 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.

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[16] This effect is evaluated on the basis of the average "elasticities" of each tax category with respect to the output gap. The elasticities used are those estimated by the OECD.

[17] As for other expenditures, they are either discretionary in nature or no link with the economic situation can be clearly and reliably identified.

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**.