Haut Conseil des Finances Publiques

Opinion n° HCFP-2022-3

on the macroeconomic forecasts associated with the Stability Programme for the years 2022 to 2027

July 26, 2022

Executive Summary

The High Council was referred to the macroeconomic forecasts associated with the Stability Programme about three months after the usual date, even beyond the electoral period in France. Despite this unusual delay, the project submitted to the High Council presents numerous weaknesses.

The High Council reiterates the assessment it made in its opinion on the first amending budget bill, according to which the Government's growth forecast for 2022 (+2.5%) is not out of reach but somewhat high. The High Council considers that this is also the case for the 2023 forecast presented in the Stability Programme (+1.4%). The inflation forecast for these two years (5.0% and then 3.2%) appears to be, conversely, underestimated. The scenario of a return of inflation to below 2% as soon as 2024 also appears ambitious.

The forecast for wage bill growth in the non-agricultural market sectors for 2022 (+8.5%) is plausible, but the forecast for 2023 (+3.7%) seems low.

The High Council considers that the assumptions for the output gap in 2022 (-1.4 points of GDP) and for potential growth (1.35% per year from 2023 to 2027) used by the Government are optimistic. These assumptions include, in particular, a forecasted increase in labor supply linked to the announcement of reforms (pension reform, unemployment insurance reform, reform of the minimum income scheme, public childcare services), the details and effects of which are not specified. The Government assumes that these effects will be significant and almost immediate, which is far from certain.

A look at the macroeconomic scenario confirms this diagnosis. The rebound in growth starting in 2023 relies on very favorable assumptions regarding the positive contribution of foreign trade and the maintenance, despite the current tightening of financing conditions, of the household and business investment rates at levels close to the very high levels reached in 2021.

Despite these very favorable growth assumptions, the public finance trajectory presented by the Government is not very ambitious in terms of reducing the deficit in light of France's European commitments, and is much slower in doing so than projected by our European partners, with the public deficit barely returning below 3 points of GDP in 2027 (2.9 points of GDP). Public debt would be nearly stable over the entire period at a high level (112.5 points of GDP in 2027). France's public finance situation would thus continue to deteriorate with respect to other comparable countries in the euro zone.

In a highly uncertain geopolitical, economic, and economic policy context, this path leaves no safety room: with lower growth than in the Government's optimistic scenario, the deficit would still be above 3 points of GDP in 2027 and the debt ratio would keep rising over the entire period.

This trajectory is also based on an assumption of an increase in the rate of taxes and social contributions through the elimination of fiscal loopholes, which experience has shown to be

difficult to implement, and on efforts to control spending on a greater scale than those implemented in the past, the timing and concrete details of which remain very vague.

*****

All in all, the High Council considers it imperative that the next public finance programming law correct these estimates by setting the output gap and potential growth assumptions on a prudent basis, taking into account the uncertainty of the period, and that it give credibility to the presented public finance trajectory through a precise description of the reforms and expenditure measures it implies.

Introductory remarks

1. Pursuant to the article 17 of the organic law n° 2012-1403 of December 17, 2012 on the programming and governance of public finances, the High Council issues an opinion on the macroeconomic forecasts on which the Stability Programme for the years 2022 to 2027 is based, drawn up to ensure the coherence of the economic policies of the European Union Member States.

2. The Stability Programme must be transmitted to the European institutions before April 30 of each year (Article 4 of Regulation (EC) No. 1466/97) and communicated to the French Parliament two weeks before (Article 14 of Law No. 2010-1645 of December 28, 2010 on the programming of public finances for the years 2011 to 2014). Given the presidential and legislative elections this spring, the submission of the Stability Programme to the European Commission was exceptionally delayed.

1- On the scope of this opinion

3. Under the terms of article 17 of the organic law of December 17, 2012, the High Council of Public Finance is referred to provide an opinion on the macroeconomic forecasts on which the Stability Programme is based.

4. Consequently, this opinion does not address the public finances scenario itself. However, considering the impact of public finances on growth, the High Council takes into account elements related to the public finances trajectory to assess the consistency of the macroeconomic scenario presented.

2- On the information submitted and the timeline

5. On July 21, 2022, the Government referred the macroeconomic framework of the draft Stability Programme to the High Council of Public Finance. This referral was supported by detailed answers to a questionnaire sent in advance to the relevant administrations.

6. The High Council notes that this referral on the Stability Programme took place more than three months later than in the previous years, even beyond the electoral period in France.

7. The projected date of referral was also changed several times. As with the first draft of the Amending Budget Bill for 2022, the final date of the referral was only communicated to the High Council at a very late stage.

8. These conditions unnecessarily complicate the exercise of the mandate entrusted to him by the organic law.

3- On the High Council's methodology

9. In order to assess the realism of the macroeconomic forecasts associated with the Stability Programme, the High Council considered the latest data and statistics available and the information provided by the Government.

10. The High Council also relied on the latest forecast from other national and international organizations: the European Commission, the International Monetary Fund (IMF), the Organization for Economic Cooperation and Development (OECD), the European Central Bank (ECB), the Institut national de la statistique et des études économiques (Insee), the Banque

de France, and economic institutes such as Rexecode and the Observatoire français des conjonctures économiques (OFCE).

11. As provided for in article 18 of the organic law, the High Council held hearings with representatives from the French Treasury and the Budget Department. As part of the preparation of its opinion on the first Amending Budget Bill for 2022, the High Council also interviewed organizations outside the finance administration (Banque de France, Rexecode and OFCE) on the medium-term outlook for the French economy.

* *

*

12. The High Council first presents its observations on the forecasts for 2022 and 2023 (I), then provides its assessment of the macroeconomic forecasts on which the Government's Stability Programme for the years 2024 to 2027 is based (II).

I. Observations on the forecasts for 2022 and 2023

1- The Government's forecast

13. According to the Government's referral, "*growth in activity in France is expected to be +2.5% in 2022, after +6.8% in 2021. Average annual inflation is expected to rise sharply in 2022, to +5.0%, and then to fall back to +3.2% in 2023.*"

14. The Government notes that "*for 2022, the macroeconomic scenario is unchanged from the scenario in the PLFR for 2022, which was referred to the HCFP on July 5.*"

15. The referral indicates that "*in 2023, the rebound would be slowed by the geopolitical situation and tensions on the supply side: the geopolitical situation in Ukraine and its consequences would only have partially normalized, slowing down the prospects for a rebound [...] Measures to support purchasing power would, however, temper this shock and household real income would continue to rise (+1.2%).*"

2- Assessment of the High Council

16. The Government's forecasts for 2022 presented in the Stability Programme are the same as those presented in the first amending finance bill (PLFR) for 2022, on which the High Council gave its opinion in opinion n° 2022-2.

17. The information published since then (a further decline in business surveys, a sharper than expected rise in the European Central Bank's key interest rates, increased financial tensions in Italy, and heightened doubts about the supply of Russian gas to the European Union) confirms the downside risks pointed out by the High Council in its opinion on the first PLFR for 2022, which should make it more difficult for the Government to achieve its forecast (+2.5%).

18. The Government's growth forecast for 2023 (1.4%) also seems somewhat high: while it stands at the same level as that of the OECD and the European Commission, it is slightly higher than the average of the July *Consensus Forecasts* (1.3%), which nonetheless takes into account

some long-standing forecasts, and those of the Banque de France (1.2%), OFCE (1.0%), the IMF (1.0 %) and Rexecode (0.3%).

19. In particular, it assumes a decline in the household savings rate, which is not given, particularly in light of the very low level of household confidence recorded in the Insee household survey. It is also subject to significant downside risks, notably the health situation, the war in Ukraine, the consequences of the European Central Bank's tightening of its monetary policy, financial tensions within the Euro Zone and the extent of current supply constraints.

Table 1: real GDP growth forecasts for France (%, annual average)

	Publication date	2022	2023
OECD	8 June	2.4	1.4
Banque de France	21 June	2.3	1.2
Rexecode	21 June	2.1	0.3
Consensus Forecasts	11 July	2.3	1.3
European Commission	14 July	2.4	1.4
OFCE	21 July	2.4	1.1
IMF	26 July	2.3	1.0
Government	**29 July**	**2.5**	**1.4**

Source: Stability Programme for 2022-2027, June 2022 OECD economic outlook, July 2022 OFCE policy brief, June 2022 Banque de France macroeconomic forecasts, Rexecode, June 2022 Insee business survey, July 2022 Consensus Forecasts, July 2022 European Commission summer forecasts, July 2022 IMF WEO Update..

20. The Government's inflation forecast for 2023 (3.2%) seems a little low: while it is close to that of the Banque de France (3.2%) and that of Consensus Forecasts (3.1%), the latter incorporating forecasts that are already a little outdated, it is clearly lower than that provided by Rexecode (3.9%) and by OFCE (4.1%). The forecast is in particular based on a +3.2% average per capita wage growth forecast for the non-agricultural market sectors, which translates into a mere stability in terms of purchasing power, without any recovery from the loss of purchasing power in 2022 (- 1.3% anticipated by the Government[1]). This rate of change therefore appears low, particularly in a context of strong recruiting pressures.

Table 2: inflation forecasts (CPI index) in France (%, annual average)

	Publication date	2022	2023
Banque de France	21 June	5.1	3.2
Rexecode	21 June	5.2	3.9
Consensus Forecasts	11 July	5.3	3.1
OFCE	21 July	5.3	4.1
Government	**29 July**	**5.0**	**3.2**

Sources: June 2022 Banque de France macroeconomic forecasts, Rexecode, July 2022 Consensus Forecasts, OFCE policy brief of July 2022, Stability Programme 2022-2027.

[1] Measured excluding the impact of partial activity.

21. The Government's growth and inflation forecasts are based on an unusual assumption of a decline in the price of oil, from $110 per barrel in 2022 to $98 in 2023, contrary to the Government's usual practice of stabilizing the price of oil at the last known level without anticipating developments that are inherently very uncertain. This unusual assumption has the effect of lowering the forecast for oil prices and inflation and increasing the growth forecast.

22. The High Council had estimated, in its opinion on the PLFR for 2022, that the growth hypothesis of the wage bill for 2022 was plausible, even if the employment forecast was weaker and that of the per capita wage higher than those of other institutions. For 2023, the employment forecast can also be considered plausible: the favorable assumption of growth would be offset by the unfavorable hypothesis of a sharp anticipated rebound in productivity.

23. As the forecast of the average wage per capita appears to be somewhat underestimated, the wage bill forecast for the non-agricultural market sectors can be considered as somewhat low in aggregate.

24. **The High Council reiterates the assessment it made in its opinion on the first amending budget bill, according to which the Government's growth forecast for 2022 (+2.5%) is not out of reach but is high. The High Council considers that this is also the case for the 2023 forecast presented in the Stability Programme (+1.4%). The inflation forecast for these two years (5.0% and then 3.2%) appears to be underestimated. The forecast of wage bill growth in the non-agricultural market sectors for 2022 (+8.5% in 2022) is plausible, but the forecast for 2023 (+3.7%) seems low.**

II. Observations on the macroeconomic scenario for the years 2024 to 2027

25. The Stability Programme's forecasts for growth and inflation up to 2027 must be examined in the light of the potential growth that France can achieve with unchanged use of production factors and the position of the French economy in the cycle. The latter is assessed on the basis of the output gap, corresponding to the difference between observed GDP and potential GDP. Potential GDP is defined as the output that would be obtained once the temporary shocks affecting the economy have been eliminated, by mobilizing the available factors of production at their equilibrium level. Therefore, when the output gap is negative, it is an indicator of the rebound capacity of the economic activity, and when positive, it hints at a slowdown.

A. Potential growth and the output gap

1- The Government's scenario

26. According to the Government's referral, *"from 2022 potential growth would return to the trend rate forecast in the Public finance programming law (+1.35%), as the productive capacity of the economy is supported by the Government's reforms and investments, which would contribute in particular to increase labor supply and achieve full employment. [...] "*

27. *"The output gap in 2022 would be -1.4 pt. Growth would be above its potential pace of 1.35 percent over the 2023-2027 period to gradually close it to zero in 2027."*

2- Assessment of the High Council

28. The Government readjusted its potential growth path compared to the Economic, Social, and Financial Report (RESF) for 2022. It now estimates that the loss in potential GDP in level due to the health crisis amounts to ¾ point compared to the 1 ¾ point in the RESF for 2022 (and 2 ¼ points in the 2021-2027 Stability Programme), but without changing its estimate of the previous potential growth path, as defined in the 2018-2022 programming law.

29. The reference of potential growth in the 2018-2022 Public finance programming law, even when adjusted to take into account an assumption of a lasting loss of GDP due to the health crisis, appears to be outdated, however, since growth in total factor productivity (TFP) has been lower since 2017 than forecast in the Public finance programming law: taking into account a weaker-than-expected change in TFP before 2022 would lead to a downward revision of the level of potential GDP and thus an upward revision of the output gap over the entire period, and in particular in 2022.

30. As a result, the Government estimates the output gap at -1.4 percentage points in 2022 instead of -0.5 percentage points previously.

31. This assessment is at the lower end of the range of international organizations (-0.6% for the European Commission, -0.9% for the IMF and -1.8% for the OECD).

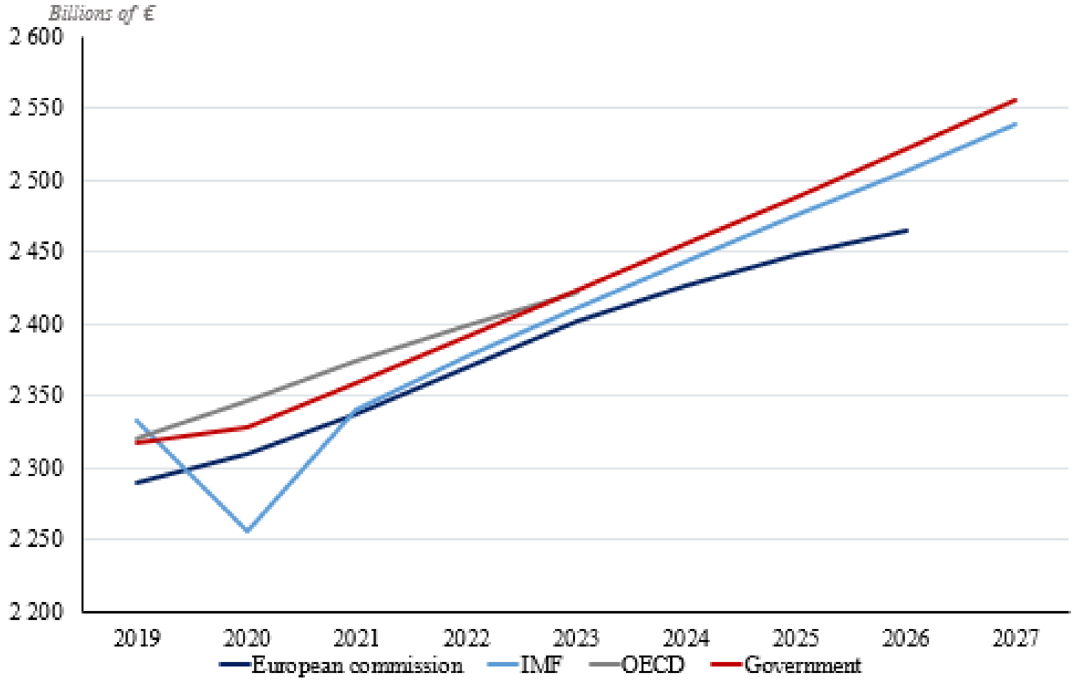
32. Moreover, such a negative output gap suggests a significant under-utilization of factors of production, which does not seem to be consistent with the proven difficulties that companies are facing in terms of skills and recruitment, difficulties that are clearly reflected in the business surveys: these difficulties are of a similar or even greater magnitude than in 2019, a period marked by a positive output gap. While the Government justifies its assessment in part by the potential for a rebound in production in certain sectors (automotive, aeronautics), the general shortage of labor supply suggests that the margins for increasing production throughout the economy are limited.

33. From 2022 onwards, the Government maintains its forecast of potential growth at 1.35 percent per year: it assumes that, once the shock of 2020-2021 has passed, potential growth will be slightly higher than its estimate for the pre-crisis period (1.25 percent per year in 2018-2019). This estimate of potential growth is close to the IMF's (1.3 %) and OFCE's (1.5 % in 2023, 1.4 % in 2024 and 1.3 % after 2025), but significantly higher than the European Commission's (1 %), the OECD's (1.0 %) and Rexecode's, which estimates potential growth below 1% after 2023.

34. The Government's potential growth forecast is also higher than the estimate, close to 1%, that can be made by replicating the methodology presented by the French Treasury at the time of the previous public finance programming law (see appendix), based on the latest Insee labor force projections and extending the pre-crisis productivity trend, while taking into account the effects of the pension reform and other reforms announced or under implementation.

35. Overall, as a result of favorable choices regarding both the level of the output gap at the beginning of the period and subsequent potential growth, the Government's potential GDP path at the end of the period is higher than the ones set by the European Commission (+2.3 % in 2026) and the IMF (+0.7% in 2027).

Figure 1: comparison of potential GDP forecasts in France (potential GDP in €bn in volume)



Source: Spring economic forecasts by the European Commission (May 2022), the OECD (June 2022) and the IMF (April 2022) and the Government's 2022-2027 Stability Programme.

36. The documents sent to the HCFP do not provide detailed figures on the respective contributions of the various components of potential growth (total factor productivity, capital, labor), nor on the impact of the various reforms announced. Nevertheless, they allow to assess that the Government's forecast is based on the increase in the labor force expected from the pension reform announced by the Government and by a marked drop in structural unemployment resulting from new reforms (reform of the minimum income scheme, unemployment insurance, transformation of *Pôle emploi*[2] into *France Travail*, extension of apprenticeship to vocational high schools, improvement of childcare facilities). The impact of these reforms appears to be clearly overestimated, since it is assumed to occur as early as 2023, whereas all comparable reforms undertaken in the past have not only required time for their formalization and implementation, but also to produce lasting effects on the population actually in employment.

37. In addition, there are still significant negative risks, common to all available assessments of potential growth, related to (i) the impact of the health crisis on the productive sector and the skill level of the workforce, (ii) the occurrence of new crises that could have a lasting impact on potential GDP, and (iii) the importance of the constraints facing the French economy in the medium term (ecological transition, public and private debt).

38. Consequently, the High Council reiterates its assessment in its opinion on the 2021--2027 Stability Programme that "the Government's assumption that potential growth will return to its pre-crisis level from 2023 onwards is optimistic".

[2] The name of the French Employment Office.

39. **The High Council considers that the hypothesis for the output gap in 2022 (-1.4 points of GDP) and the potential growth (1.35 percent per year from 2023 to 2027) used by the Government are optimistic. These assumptions include, in particular, a forecast of an increase in the labor supply linked to announced reforms (pension reform, unemployment insurance reform, minimum income scheme reform, public childcare services), for which neither the terms nor the effects are detailed. The Government assumes that the latter will be significant and almost immediate, which is far from certain.**

40. **The High Council considers crucial that the next programming law corrects these estimates by setting on cautious bases, taking into account the uncertainty of the period, the assumptions of output gap and potential growth on which the public finances strategy of the next five years will be based.**

B. Observations on the macroeconomic scenario for the years 2024 to 2027

1- The Government's scenario

41. According to the Government, *"growth [...] would gradually accelerate to an average of +1.7 % over the period 2024-2027, rising from 1.6 % to 1.8 % between 2024 and 2027. [...] The rebound in activity would be stronger from 2024 (+1.6%) and accelerate through 2027 (+1.8%), averaging 1.7% over the 2024-2027 period."*

42. *"Over the period 2023-2027, non-agricultural market wage employment would be dynamic, driven by employment measures [...] On average between 2023 and 2027, 185,000 market wage jobs would be created each year, reaching full employment by 2027."*

43. In its referral, the Government states that *"inflation [...] would be +1.9% in 2024 and then return to 1.75% from 2025, a level consistent with the European Central Bank's target."*

44. Nevertheless, the Government pointed out that *"the risks surrounding this forecast are significant. The evolution of the situation in Ukraine is the main hazard, mainly bearish. [...] The evolution of the health situation remains a risk. The activity could be affected again in the event of an epidemic wave by cautious behavior and an increase in sick leave, as well as by the impact on global supply chains of measures implemented abroad, in particular in China. In the face of these downside risks, there are factors for a rebound, but their extent is uncertain. The scenario assumes a very gradual decline in the household savings rate. [...] The recovery of the loss of export performance in goods retained in the scenario is limited, and its final extent will depend in particular on the sectoral composition of world trade in the medium term. The gradual easing of supply constraints should support production and thus allow a certain dynamism in investment and exports. »*

2- Assessment of the High Council

45. Consistent with its estimate of a negative output gap in 2022, the Government assumes that growth will be higher than potential growth after 2023, leading the level of GDP to return to its potential level in 2027: GDP growth is thus forecast at 1.6 % in 2024, 1.7 % in 2025 and 2026, and 1.8 % in 2027, compared to a potential growth forecast of 1.35 % per year over the

same period. As the High Council regularly notes, the scenario construction, which does not incorporate cyclical shocks, provides a reasonable basis for establishing a multi-year public finance path, even if, ex post, shocks, which are by their nature unpredictable, are likely to cause GDP to deviate from this path, under the condition that the initial output gap and the subsequent potential growth are correctly estimated.

46. In the Government's scenario, closing the output gap is based on the assumption that the savings rate will return to its pre-sanitary crisis level, which is plausible, even though the shocks experienced by households, particularly as a result of the sanitary crisis and the return of high inflation after two decades of low inflation, are likely to induce them to maintain greater precautionary savings than before 2020. However, a temporary, larger drop in the household savings rate, which would benefit consumer spending, is also possible, given the size of the excess savings resulting from the health crisis in 2020 and 2021.

47. This closing of the output gap is also based on a very favorable forecast of the contribution of foreign trade. The latter would be consistently positive by 2027 (0.2 percentage points on average), even though, on the one hand, foreign demand from France's European partners could be less dynamic as a result of the announced reduction in public deficits and the effects of a tighter monetary policy, and, on the other hand, French domestic demand is assumed to remain dynamic throughout the period (1.6% on average). This forecast is based in particular on an assumption of substantial gains in export market share.

48. The Government's forecast also assumes that household and business investment, which have reached particularly high levels in 2021 as a share of GDP (the highest level since 2008 and over the entire 1949-2021 period for which these data are available), thanks in particular to the very favorable financing conditions that existed until now, will not suffer from the ongoing tightening of the ECB's monetary policy.

49. All in all, these elements confirm the great fragility of the potential GDP assumption used by the Government for the period 2023-2027.

50. Moreover, the fall in inflation from 2024 below the ECB's 2% target in a context of sustained growth, above potential growth, seems particularly favorable. It is based in particular on the assumption of a further decline in the price of oil (Brent), to $85 per barrel after $98 in 2023. The High Council notes once again that the usual assumption of stabilization of oil prices at their most recent level - a conventional choice that is justified by the difficulty of predicting oil prices and that is shared by many institutions - has been replaced by the assumption of a sharp decline in oil prices.

51. **The High Council underlines that the growth scenario for the years 2024 to 2027 reflects the fragility of the potential GDP path adopted by the Government. The closing of the large initial output gap, as estimated by the Government, is based in particular on very favorable assumptions of a positive contribution from foreign trade and of maintaining, despite the current tightening of financing conditions, the rate of household and business investment at levels close to the very high one reached in 2021. The assumed scenario of a return of inflation to below 2% by 2024 also appears to be ambitious.**

C. Impact of the macroeconomic scenario on public finances

52. The Stability Programme is an obligation resulting from the membership of the Economic and Monetary Union. Required to enable the Commission and the Council of the European Union to ensure the proper coordination of economic policies and the surveillance of the effective implementation of European budgetary rules by member states, Stability Programmes must include, among other things, the medium-term budgetary objective and the adjustment path towards this objective, the projected evolution of the Government debt ratio, as well as the evolution of Government revenues and expenditures.

53. The Government's plan to reduce the public deficit in this Stability Programme is not very ambitious in the light of France's European commitments. The public deficit would remain high in 2023, at 5.0 points of GDP, with no structural adjustment. Over the period 2024-2027, it would be reduced by an average of just over half a point of GDP per year, reaching 2.9 points of GDP in 2027. The structural adjustment, i.e., the reduction of the structural balance, would be 0.3 points of GDP per year from 2024 onwards. Ultimately, the Stability Programme foresees a return of the public deficit to below the limit of 3 points of GDP set in the Stability and Growth Pact only from 2027 onwards, and this without any safety margin. While the "general escape clause" enables Member States to temporarily deviate from the adjustment path set out in the European budgetary rules, the Commission considers a return to the application of these rules from 2024.

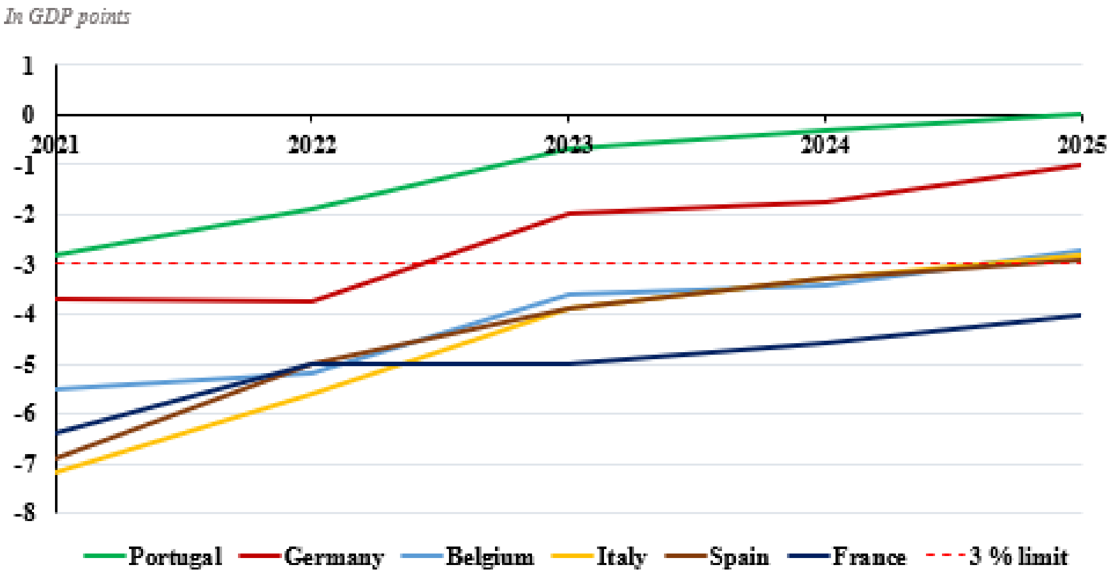
Table 3: general government balance (in points of GDP)

	2022	2023	2024	2025	2026	2027
General government balance	**-5,0**	**-5,0**	**-4,6**	**-4,0**	**-3,4**	**-2,9**
Structural budget balance (% of potential GDP)	-4,0	-4,1	-3,8	-3,5	-3,2	-2,9
Structural adjustment	0,8	0,0	0,3	0,3	0,3	0,3

Source : 2022-2027 Stability Programme

54. This unambitious path differs from those presented by other EU Member States in their Stability Programmes submitted to the European Commission in the spring. While many Member States, such as France, have deficits that currently exceed the threshold of 3 points of GDP, countries comparable to France plan to return below this limit as early as 2025.

Figure 2: public balances forecasted by Member States in their Stability Programmes submitted in spring 2022



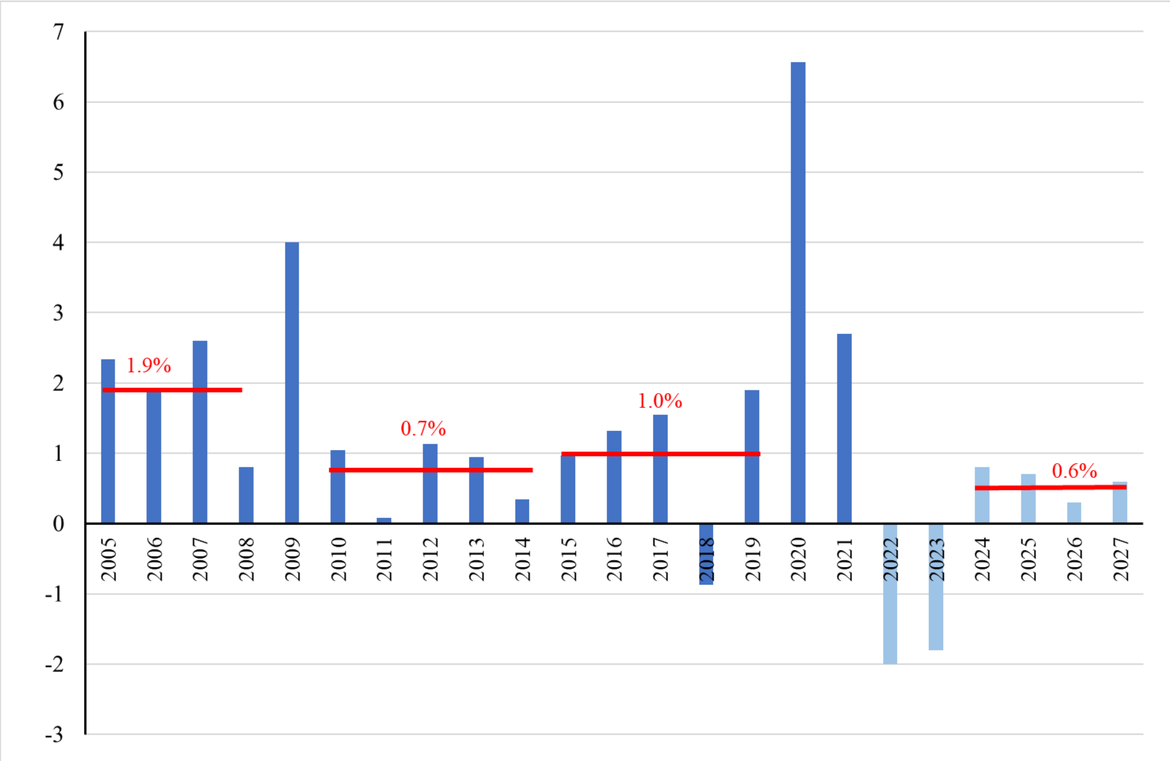
Source: Member States' Stability Programmes (European Commission website), Stability Programme 2022-2027

55. France's Stability Programme projects a reduction in the share of public spending by 3.8 points of GDP (excluding tax credits): it would fall from 57.3 points of GDP in 2022 to 53.5 points in 2027. However, the ratio of public spending to GDP would remain above its 2019 level (before the health crisis) until 2026.

56. A little less than half of the decline in this ratio would take place between 2022 and 2023, largely as a result of the phasing out of emergency support spending and anti-inflation support measures, which are assumed to be less costly in 2023. Public spending would then resume a growth path in volume terms, but at a slower pace than GDP, averaging 0.6% per year over the period 2024-2027, which is lower than the growth recorded over the previous two decades, but comparable to the period 2010-2014, which was marked by the euro zone crisis. Taking into account the expected increase in interest charges on public debt and the outlook for Government spending set out in several programming laws, this structural effort would require a strong control of, or even a reduction in, other spending, which implies a more determined action on spending than France has been able to demonstrate in the past.

57. According to the information provided to the HCFP, efforts to control spending will be based mainly on the pension reform and on expenditure reviews, for which neither the parameters nor the timetable have been communicated. Expenditure growth in volume is projected to average 0.6 percent between 2024 and 2027, but this estimate is pulled down by the supposed end of household income support measures taken in response to the energy crisis and by the impact of the municipal electoral cycle on public investment, with municipal investment spending rising sharply in the two years preceding the municipal elections, but falling well below normal in the year of the elections and the following year (that is, in this case, 2026 and 2027).

Figure 3: growth rate of public spending in volume[3] (in %)



Source: Insee, 2022-2027 Stability Programme

58. The tax and social contribution revenue[4] ratio would fall significantly in 2023, by 1.3 points of GDP compared to 2022, as its growth at unchanged policy is expected to be much lower than GDP (elasticity of 0.5) after a forecast raised to 1.5 in 2022 by the first amending budget bill for 2022. Excluding the impact of changes in legislation, taxes and social security contributions are expected to increase in line with GDP from 2024 onwards. New tax reduction measures are taken into account: the removal of the audiovisual licence fee, at a cost of €3.2bn from 2022, followed by the removal of the CVAE[5] and some other measures concerning households (lower contributions for the self-employed, others). However, the tax burden is expected to rise in 2024 and then stabilize at 44.0% of GDP, according to the Government, due to the removal of certain tax loopholes.

59. The public debt ratio would be broadly stable: after a slight increase at the beginning of the programme period, it would decrease at the end of the period, to come back to its 2021 level of 112.5 points of GDP in 2027.

60. The return of the deficit to below 3 percentage points of GDP and the virtual stability of the public debt ratio are conditional, in particular, on the achievement of the Government's favourable growth scenario: lower growth would call into question the achievement of these objectives. With unchanged fiscal policy and interest rates, a scenario with a more realistic assumption with a lower potential growth of 1.1%, where the output gap would be zero in 2022 and actual growth would consequently equal potential growth between 2023 and 2027, would result in a slower decline of the public deficit. It would still exceed 4 percentage points of GDP

[3] Emergency and stimulus measures included.
[4] net of tax credits.
[5] A tax on value-added by firms, for an impact of €7.0 billion on the general government balance in 2027.

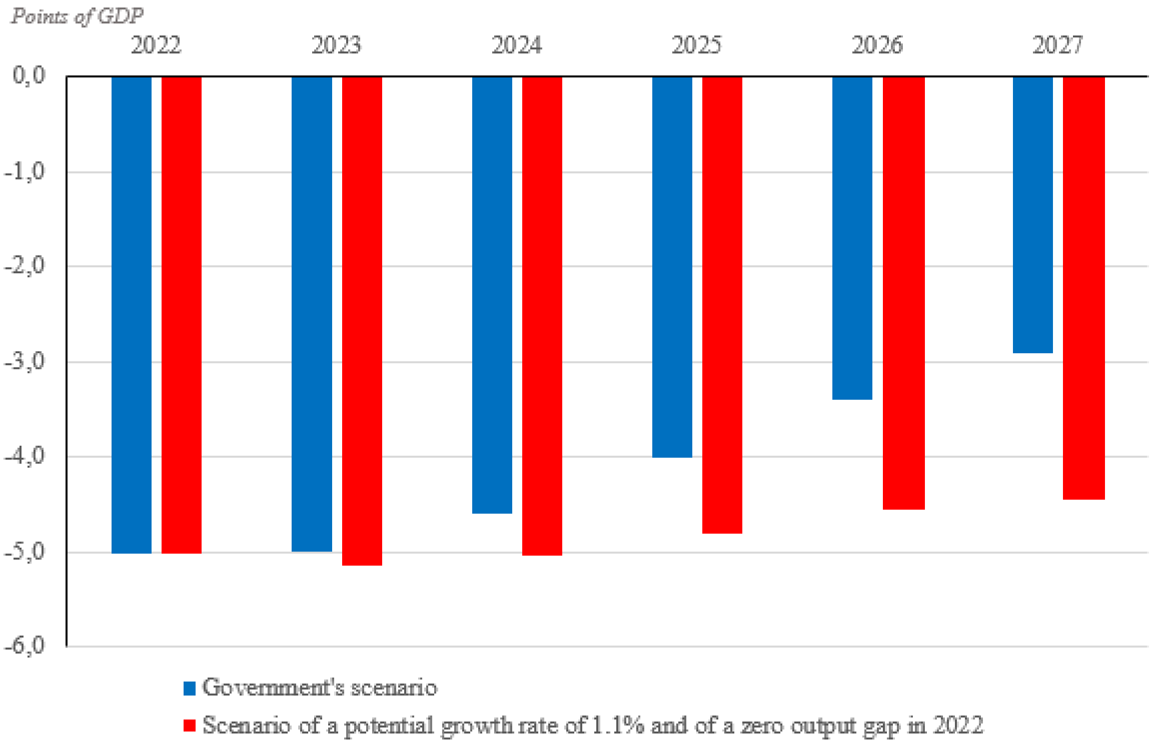
in 2027 (see Figure 4). The debt ratio would grow continuously, reaching almost 120 points of GDP in 2027 (Figure 5)[6].

61. **All in all, the public finance trajectory presented by the Government is not very ambitious in terms of reducing the deficit in light France's European commitments, and is much slower in doing so than projected by our European partners, with the public deficit barely returning below 3 points of GDP in 2027 (2.9 points of GDP). Public debt would be nearly stable over the entire period at a high level (112.5 points of GDP in 2027). France's public finance situation would thus continue to deteriorate with respect to other comparable countries in the euro zone.**

62. **This trajectory is also based on an optimistic growth assumption, without which the deficit would remain above 3 points of GDP and the debt ratio would continue to rise.**

63. **Finally, it is based on an assumption of an increase in the rate of tax and social contribution made possible by the elimination of tax loopholes, which experience has shown to be difficult to implement, and on efforts to control spending on a greater scale than those implemented in the past, for which the timetable and terms remain very vague.**

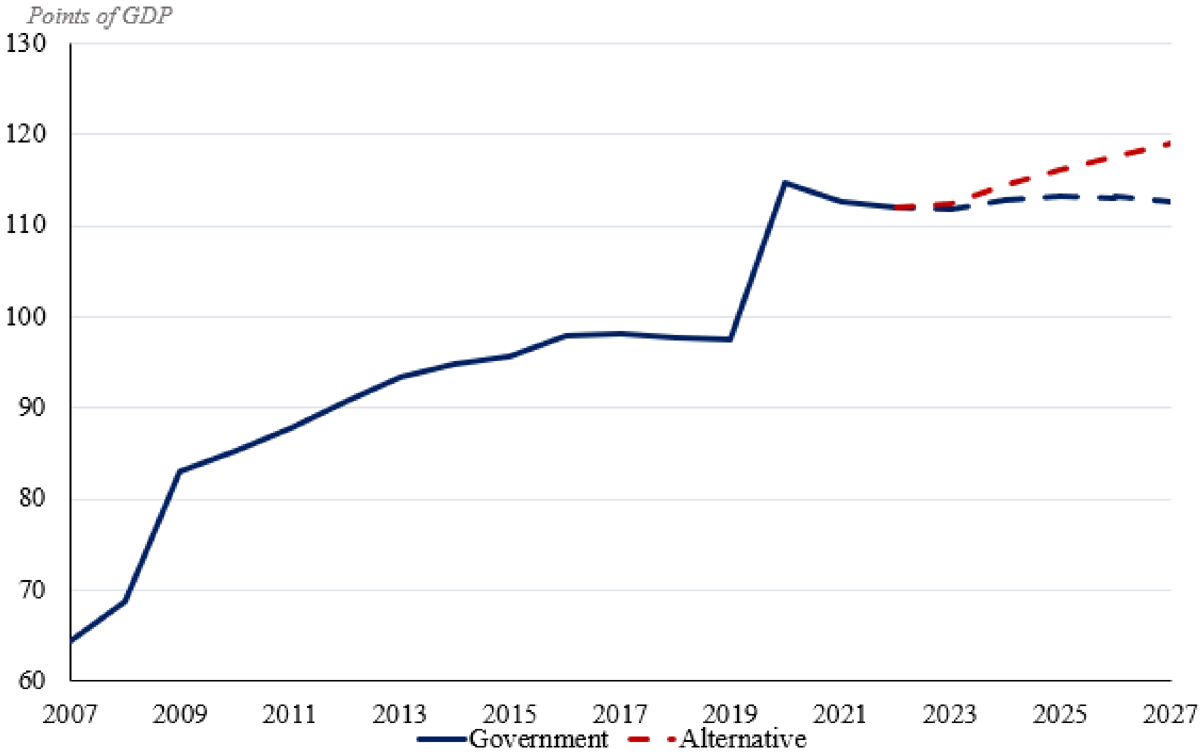
Figure 4: public deficit path according to the assumed growth assumption



Source: Government, High Council for Public Finance

[6] The deficit and debt path under these assumptions is constructed on the basis of the Government's path, assuming an unchanged tax and social contribution rate (i.e., a unitary elasticity of tax and social contribution revenue with respect to growth), taking into account the impact on unemployment benefit expenditure of a less favorable economic situation (with an expenditure elasticity with respect to the output gap equal to the one used by the Government in its calculation of the structural balance, i.e., 3.23), and the impact of the resulting increase in debt on interest charges. By contrast, other revenues and expenditures are assumed to remain unchanged, in line with the assumptions made by the Government in its structural balance calculations.

Figure 5: public debt trajectory according to the assumed growth assumption



Source: Government, High Council of Public Finance

*

* *

This opinion will be published in the *Journal officiel* of the French Republic and attached to the Stability Programme when it is sent by the Government to the Council of the European Union and to the European Commission.

Paris July 26, 2022.

For the High Council of Public Finance,
the First President of the Court of Auditors,
Chairman of the High Council of Public Finance

Pierre MOSCOVICI

Haut Conseil des Finances Publiques

APPENDIX 1

Macroeconomic scenario for the Stability Programme

	2021	2022	2023	2024	2025	2026	2027
Goods and services, real terms							
Gross domestic product	**6.8**	**2.5**	**1.4**	**1.6**	**1.7**	**1.7**	**1.8**
Private consumption expenditure	5.3	2.8	1.9	1.8	1.9	1.8	1.9
Government consumption expenditure	6.4	1.4	0.5	0.4	0.3	0.8	1.0
Gross fixed capital formation	11.4	2.9	0.8	1.8	2.0	1.1	1.4
Imports of goods and services	7.8	6.5	3.0	3.5	3.5	3.1	3.4
Exports of goods and services	8.6	7.1	3.5	4.1	4.1	4.1	4.2
Contributions to real GDP growth							
Final domestic demand excluding inventories	**7.0**	2.5	1.3	1.5	1.6	1.4	1.6
Foreign trade	**0.1**	0.0	0.1	0.1	0.1	0.3	0.2
Prices and nominal aggregates							
Consumer price index	**1.6**	**5.0**	**3.2**	**1.9**	**1.75**	**1.75**	**1.75**
Gross domestic product deflator	1.3	2.3	3.2	1.7	1.6	1.6	1.6
Nominal gross domestic product	8.2	4.9	4.7	3.3	3.3	3.3	3.4
Employment and wages							
Whole economy							
- Employment (employed persons)[7]		1.6	0.1	0.7	0.7	0.9	1.0
- Employee wages (including employer contributions)		7.3	3.8	3.3	3.2	3.1	3.1
w- Employee wages (including employer contributions) per capita average		5.6	3.7	3.2	3.0	2.9	2.8
Potential GDP growth and output gap							
Potential GDP growth (%)	**1.30**	**1.35**	**1.35**	**1.35**	**1.35**	**1.35**	**1.35**
Output gap (% of potential GDP)	**-2.6**	**-1.4**	**-1.4**	**-1.2**	**-0.8**	**-0.4**	**0.0**

Source: Ministry of the Economy and Finance (July 2022).

[7] Working population, in thousands, in the national accounts sense.

Haut Conseil des Finances Publiques

APPENDIX 2

What potential growth and output gap scenarios to adopt looking forward to 2027?

To forecast activity over a medium-term horizon, such as that of the Stability Programme, potential growth and the output gap, i.e. the difference between the level of actual and potential GDP, are essential input[8]. In the absence of a new shock, unforeseen in essence, GDP should gradually converge towards its potential level, as determined based on productivity trends and the performance of the labor market. A reasonable forecast thus consists in starting with potential growth, and then correcting it for the consequences of the gradual elimination of the output gap: a positive gap at the beginning of the period (or a negative one) leads to a forecast of growth that is lower (or higher) than potential growth[9].

Taking into account the latest labor force projections and the extension of pre-crisis productivity trends, potential growth is estimated to be around 1.0% by 2027.

The forecast of potential growth can take the latest Insee labor force forecasts[10] as its starting point as well as the extension of productivity trends observed before the health crisis.

In its latest forecasts, Insee predicts that the labour force will be stable by 2027, while it grew by about 0.3 per cent per year over the 2010 decade. Assuming a stability in hours per capita as observed before the health crisis and a stabilization of the structural unemployment rate, the labor factor, expressed as total hours worked, should therefore not contribute to potential growth at this horizon. The latter would therefore be the result of the sole increasing trend of labor productivity.

Estimating the productivity trend over the pre-crisis period is a difficult. Productivity is affected by cyclical phenomena, and by the impact, which is difficult to measure precisely, of the employment policies implemented over the period (notably CICE[11], the “Responsibility Pact”) and by the evolution of business investment, which is not automatically extended. An analysis by the Permanent Secretariat of the HCFP[12] leads to an estimate of this trend, and therefore of potential growth, of about 0.9% per year as a forecast.

This estimate carries many uncertainties however. First, Insee's labor force forecast assumes no change in the current pension legislation. Implementation of the pension reform as announced by the President of the Republic during the presidential campaign would increase the labour force and raise the potential GDP growth forecast by 0.15 percentage point per year, bringing it slightly above 1%. Other structural reforms coming into effect during the projection period or in the process of being implemented (recovery plan, France 2030, suppression of the CVAE, etc.) may also affect potential growth, but they constitute a hazard of undetermined direction: it is not possible to determine whether these reforms will have stronger or weaker effects on future growth than those implemented during the pre-crisis period which are taken into account in the estimate of the productivity trend.

---

8 See note from the Permanent Secretariat of the HCFP: *Le PIB et la croissance potentiels : déwfinition et enjeux pour les finances publiques*, September 2021, https://www.hcfp.fr/node/210 (in French).

9 Thus, in its Stability Programme, the German government expected the output gap to be positive in 2023, due to the favorable short-term dynamics of the German economy at that time, gradually returning to zero by 2026 (link: German Stability Programmeme (europa.eu)).

10 See Insee, *Projections de population active : le nombre d’actifs diminuerait à partir de 2040*, June 2022, https://www.insee.fr/fr/statistiques/6453758?sommaire=6453776 (in French).

11 A tax credit based upon the wage bill of firms, concentrated on low-paid workers.

12 See note from the Permanent Secretariat of the HCFP : *Potential growth over the medium term*, July 2022, https://www.hcfp.fr/node/224.

Additionally, this scenario is surrounded by two major negative contingencies, which are difficult to quantify: the risk of a new crisis and the effects of certain factors that could weigh on the French economy (the burden of public and private debt, the deterioration in the quality of workforce skills, the scars of the crisis on the productive sector, the consequences of the climate constraint and of the ecological transition). Conversely, the weakness in productivity observed during the health crisis[13] could, if it were partly temporary in nature and therefore expected to be reversed in the medium term, push potential growth upwards; this would be the case in particular if, in a context of increasing recruiting difficulties, companies were to devote more effort to increasing the productivity of their employees.

All in all, these factors suggest a potential growth scenario for 2027 close to 1% per year, give or take, depending on the assumption made about the implementation of the pension reform announced during the presidential campaign. Given the uncertainties surrounding this assessment, slightly different evaluations may be justified.

The Government's projection of potential growth for the 2022-2027 period is much higher, standing at 1.35 percent, unchanged from medium term trajectory set in the RESF for 2022. The Government's forecast implicitly assumes that the announced reforms (pensions, unemployment insurance, labor market reforms) would provide support for potential growth of a magnitude that appears to be clearly overestimated at this horizon.

An output gap of which the sign itself remains uncertain for 2022

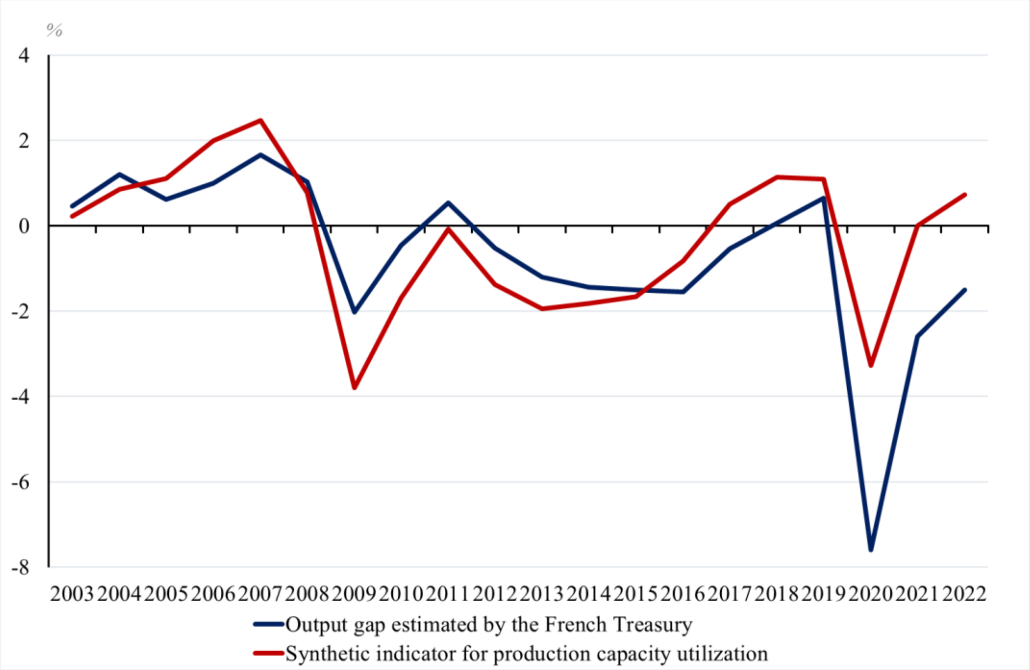
With the Government's growth forecast for 2022, both the Government's and international organization estimates of potential growth lead to a negative output gap estimate in 2022: -1.4 points for the Government; -0.6 points for the European Commission; -0.9 points for the IMF; and -1.8 points for the OECD. As the Government's actual GDP growth forecast is considered too high by the High Council, the output gap would be even slightly more negative with a more central forecast.

The magnitude of the supply constraints identified by the business surveys, which are higher than their long-term average (see graph)[14], would lead to a somewhat positive output gap estimate.

[13] See for example note 2022-01 from the Permanent Secretariat of the HCFP : La productivité du travail au sortir de la crise sanitaire, mars 2022, https://www.hcfp.fr/node/216 (in French).

[14] Business surveys are only available only June 2022, so the signal they give is not directly comparable to the Government's estimate of the output gap over the full year 2022; however, to the extent that the Government's forecast assumes growth close to potential growth over the three quarters of the 2022 forecast, the output gap can be considered to be virtually the same on average and over each quarter of 2022.

Graph: synthetic indicator of production capacity utilization and output gap estimated then forecasted by the French Treasury



Source: Stability Programme from the Government, European Commission surveys and national accounts, calculations by the Permanent Secretariat of the HCFP

Note: the synthetic indicator of production capacity utilization is calculated based on data from the European Commission's business surveys (capacity utilization rate in industry and business climate in industry, services and construction). The methodology is that of the capacity utilization business survey (CUBS) indicator that the European Commission uses to estimate potential GDP and the output gap[15]*. The indicator summarizes the surveys, taking into account the respective volatility of the sectors and their relative weight in the value added of the economy. For the second quarter of 2022, the weights are estimated based on the value added forecasts in the June 2022 Insee note de conjoncture (Table 5, page 9), and it is assumed that the indicator stabilizes in the second half of 2022 at its second quarter level.*

The difference between the Government's and international organizations' estimates of the output gap, on the one hand, and the level suggested by business surveys, on the other one, can be explained by the fact that the former assume that productivity is currently below trend and that the French economy therefore has the potential to rebound, whereas business leaders, faced with severe constraints limiting their ability to increase production (recruitment and supply difficulties, rising costs) in order to satisfy dynamic demand, do not perceive this potential for rebound.

The productivity path that will ultimately be recorded will allow to decide ex post between these two diagnosis, but their divergence makes the assessment of the actual sign of the output gap uncertain for now. As a result, it seems reasonable to consider the output gap as zero for

[15] See the document from the European Commission available at the following link: https://ec.europa.eu/economy_finance/publications/economic_paper/2014/ecp535_en.htm

the purposes of establishing a medium-term path, which, all else equal, would lead to a withdrawal of about 0.4 percentage points of growth on average per year between 2024 and 2027.