Haut Conseil des Finances Publiques

Opinion n° HCFP-2022-5

On the public finance programming bill for the years 2023 to 2027

21 September 2022

Executive Summary

The draft public finance programming bill for the years 2023 to 2027 is based on a macroeconomic scenario that is almost identical to the one of the Stability Programme for the years 2022-2027, even though the High Council considered it necessary to correct several elements in its opinion n°2022-3 of the 26th July 2022. In particular, the High Council called for a revision of the assumptions of the output gap and potential growth on a more prudent basis.

Consequently, the High Council reiterates its assessment that, on the one hand, the assumptions of the output gap in 2022 (-1.1 percentage points of potential GDP) and, on the other hand, of potential growth (1.35% per year from 2022 to 2027) are optimistic, in particular because the latter assumes significant and immediate effects of reforms (of the minimum income scheme, pensions, unemployment insurance, apprenticeship…) of which neither the modalities, nor the impacts, nor the timetable are documented.

As already pointed out in its opinion on the Stability Programme, the High Council notes that the detailed macroeconomic scenario for reaching the expected level of potential GDP in 2027 is based on very favourable assumptions of a continued decline in the household savings rate resulting in supporting consumption, a persisting high rate of business investment and a positive contribution of foreign trade to growth over the entire period.

The Government expects inflation to return to a level consistent with the ECB's target from 2026, along with a moderate rise in interest rates, even though the rate hike needed to curb inflation remains highly uncertain.

The High Council of public finance considers that the public finance trajectory presented by the Government is unambitious especially with respect to France's European commitments. The draft programming law does not aim a rapid return towards the medium-term objective of balanced public finances, to which France has committed itself, and the planned change in the debt trajectory is limited and late, even though the growth assumptions are optimistic. Moreover, the effort to contain expenditures and the planned increase in certain revenues (as elimination of loopholes, fight against fraud) included in the programming law are only partially documented.

To ensure the sustainability of its public finances, France, which is among the most indebted countries in the euro zone and has a high tax and social contribution rate, needs a solid programme to contain expenditure.

Introductory remarks

1- On the scope of the following opinion

1. In application of Article 61 – III of the amended organic law n° 2001-692 of the 1st of August 2001 relating to budget bill, the High council gives an opinion on the macroeconomic forecasts and on the estimate of potential gross domestic product on which the public finance programming bill is based, as well as on the consistency of the planned path with the medium-term objective adopted and with France's European commitments.

2- On the information submitted and the timeline

2. On September 15, 2022, the Government referred the macroeconomics forecasts, the estimate of potential gross domestic product and the information needed to assess the consistency of the planned programme with the medium-term objective and France's European commitments to the High Council of public finance in order to issue an opinion on September 21, 2022. On September 16, the Government also presented the elements of the programming bill and its annexed report which were missing from the initial referral. The High Council pointed out that the -already short- one-week deadline set by the organic law to issue its opinion was not met.

3- On the High Council's methodology

3. In order to assess the realism of the macroeconomics forecasts associated with the public finance programming law, the High Council based itself on the latest available statistics as well as on the information provided by the Government.

4. The High Council have also relied on the latest forecasts produced by a range of international and national institutions: the European Commission, the International Monetary Fund (IMF), the Organisation for Economic Co-operation and Development (OECD), the European Central Bank (ECB), the French National Institute for Statistics and Economic Studies (Insee), the Banque de France and several economic institutes such as Rexecode and the French Economic Observatory (OFCE).

5. The High Council held hearings with representatives of the Treasury, the Budget department and the Directorate of social security. The High Council also interviewed organisations outside the finance administration (Insee, Banque de France, Rexecode and OFCE) on the outlook for the French economy.

The role of public finance programming laws in the governance of public finances

Introduced into the national legal order by the 2008 constitutional revision, the main function of public finance programming laws (PFPL) is to define the multi-year orientations of public finances with the objective of balanced public accounts.

Their role in the governance of French public finances has been gradually strenghtened and formalised. In this way, the organic law of December 17, 2012, which transposes the Treaty on Stability, Coordination and Gouvernance (TSCG) into national law, stipulates that PFPL shall set the medium-term objective for public administration provided for by this treaty and determine a multi-year trajectory for the public balance in order to achieve this objective. It also creates the High Council of public finance, which is reponsible for assessing the consistency of the draft budget bill and social security financing bills with the multi-year structural budget balance guidelines defined in the PFPL. In addition, the High Council of public finance has to identify whether there are “significant deviations” between the execution of the past year and these multi-annual guidelines. In this case, the Government must present corrective measures to return to a structural balance path of public accounts. PFPL cover a minimum period of three years. They may include rules relating to the management of public finances and to the information and control of Parliament. The purpose of these rules may be to control expenditure, revenue and the balance or use of public debt.

The framework of the public finance programming laws has been clarified and completed by the organic law of December 28, 2021, which also integrates the organic provisions governing PFPL into the organic law of August 1, 2001 regarding budget bills.

Although the creation of PFPL marked an undeniable progress in the governance of public finances by placing their management in a multi-year framework, and although their role has continued to be strenghtened in law, they are not sufficient, on their own, to ensure the control of public finances. Since their introduction into the public finance governance framework, five programming laws have been adopted (2009-2012, 2011-2014, 2012-2017, 2014-2019 and 2018-2022). Their objectives are non-binding, based on generally optimistic and quickly obsolete assumptions and have rarely been achieved. Since 2008, the situation of French public finances has clearly deteriorated, contrary to the objectives constantly stated in the programming laws.

*   *
*

6. The High Council first formulates its observations on the estimate of potential GDP (I), then on the macroeconomic forecasts on which the public finance programming law for the year 2023 to 2027 is based (II), before commenting on the consistency of the public finance multi-year path with the medium-term objective adopted by the bill and France’s European commitments (III).

I. Observations on the estimate of potential GDP

7. The High Council must give its opinion on the estimate of potential GDP took on by the Government in the draft programming law. This estimate plays a fundamental role in the construction of the macroeconomic scenario.

8. Indeed, potential GDP is defined as the output which would be obtained once the temporary shocks affecting the economy have been eliminated, by mobilising the available factors of production at their equilibrium level (i.e. without causing inflationary or deflationary pressures): in the absence of any knowledge of the shocks that will affect the economy in the future, it is therefore the level towards which actual GDP can be expected to converge over the horizon of the programming law. Effective growth over the period under consideration therefore depends on potential growth, which is itself the result of the expected growth of production factors (capital and labour) and that of their productivity, on the one hand, and of the closing of the initial gap between observed GDP and potential GDP, known as output gap, on the other hand: when this gap is negative, expected growth should be higher than potential growth and in return, when it is positive, lower than the latter.

1- The Government's forecast

9. According to the Government's referral file, "*From 2022, potential growth would be 1.35%, a level similar to that forecast for this horizon in the 2018-2022 public finance programming law, with the economy productive capacity supported by government's reforms. The latter would contribute to increasing the labour supply and achieving full employment by 2027.*"

10. *"The output gap calculated is +0.9 pts in 2019, -1.1 pts in 2022 and 1.4 pts in 2023. Effective growth over the period 2024-2027 would be higher than its potential rate of 1.35% and the output gap closed in 2027. Growth would set up at 1.7% over 2024-2027, with a slightly higher rate at the end (1.8% in 2027) than at the beginning of the period (1.6% in 2024), reflecting the gradual dissipation of pressures related to the health crisis and the conflict in Ukraine."*

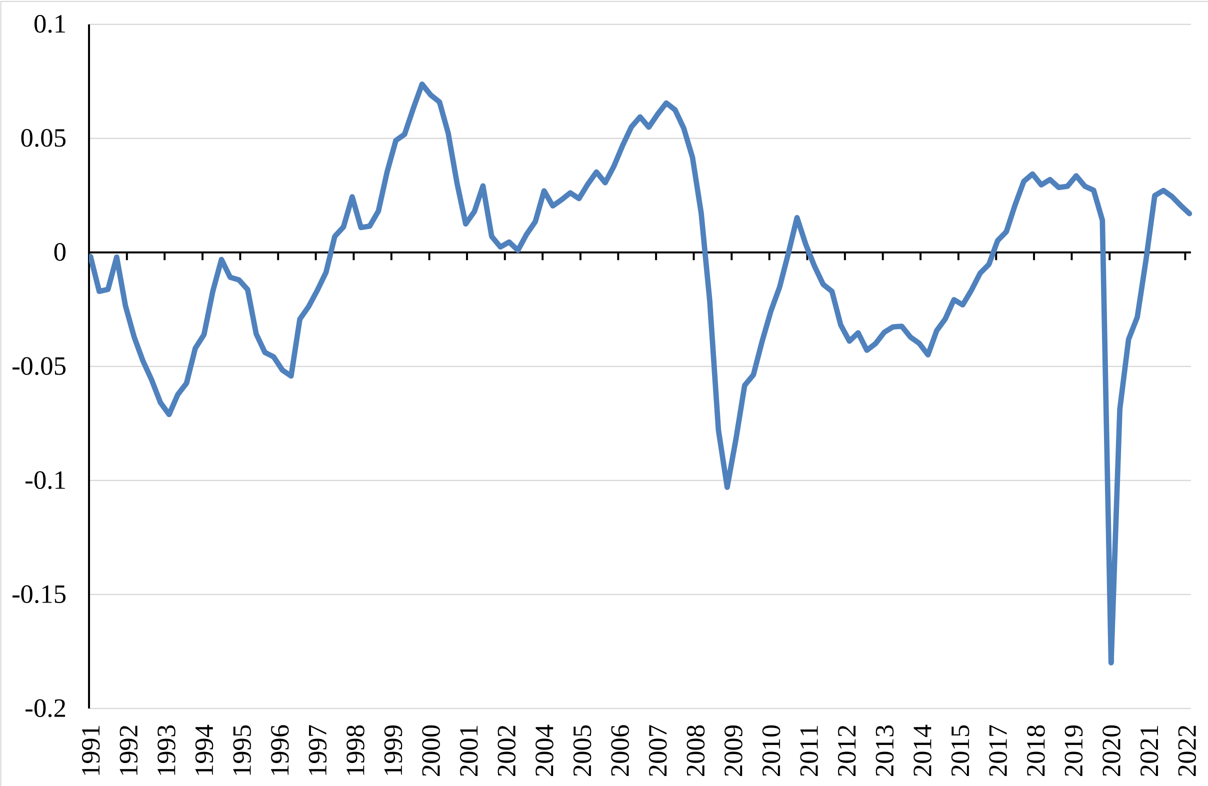
2- Assessment of the High Council

11. The government adopted the same potential GDP scenario than the one presented in the 2022-2027 Stability Programme. The loss of potential GDP due to to the health crisis is estimated at ¾ points compared to 1 ¾ points in the Economic, Social and Financial Report (ESFR) for 2022, and potential growth is estimated at 1.35% over the years 2023-2027.

12. The only change, at the margin, compared to the 2022-2027 Stability Programme comes from a revised estimate of the level of potential GDP in the past. The latter is now calculated so as to obtain a zero output gap on average over the period 1993-2019, which includes two full economic cycles. The resulting output gap is +0.9 points in 2019 (compared to +0.7 points in the Stability Programme). The output gap would be -1.1 points in 2022, widen to -1.4 points in 2023 and then gradually close to zero in 2027.

13. The Government estimates the output gap in 2022 at -1.1 points. This estimation is at the lower end of the range of international organisations (-0.4% for the European Commission, -0.7% for the IMF and -1.6% for the OECD). The significant underuse of production capacity that this figure implies seems inconsistent with the companies' answers to business surveys (see graph 1.), as well as with the extent of recruitment difficulties.

Figure 1: synthetic indicator of production capacity



Source: European Commission surveys and national accounts, calculations by the High Council of Public Finance Permanent Secretariat

Note: the synthetic indicator of production capacity utilisation is calculated from the European Commission's consumer and business survey data (industry capacity utilisation rate and business environment in industry, services and construction). The methodology is that of the capacity utilisation business survey (CUBS), indicator that the European Commission uses to estimate potential GDP and the output gap. The indicator synthesises the surveys taking into account the respective volatility of the sectors and their relative weight in the value added of the economy. Its average is zero over the period 1993 - 2019.

14. The Government's potential growth forecast, set at 1.35% over the entire 2022-2027 period, is identical to the one adopted at the end of the period by the 2018-2022 PFPL. The decomposition of the contributions to the potential growth of 1.35% from 2022 onwards takes into account the slowdown in total factor productivity (TFP) observed before the health crisis. The contribution of TFP thus falls from 0.6-0.7 points in the previous PFPL to 0.4-0.5 points in the current draft, an estimate consistent with trends prior to the health crisis.

15. In contrast, the contribution of labour is expected to increase from 0.1-0.2 points before the health crisis to a range of 0.3-0.4 points between 2023 and 2027 in the draft PFPL. The government assumes that the impact of a series of reforms (the minimum income scheme, pensions, unemployment insurance, apprenticeships, etc.) will more than offset the sharp slowdown in the active population projected by Insee. As stated in its opinion on the Stability

Programme, the High Council considers that the impact of these reforms, on which the government has not provided more information than in the Stability Programme, is overestimated, particularly in the first years of the period considered since, even assuming that they are implemented quickly, these reforms should only have a gradual impact.

16. Similarly, the contribution of capital is expected to rise to 0.5%/0.6%, 0.1 points above its pre-crisis trend, even though financing conditions, which were exceptionally favourable before the crisis, are now tightening.

17. The Government's assessment of potential growth is close to that of the IMF (1.3%) and OFCE (1.5% in 2023, 1.4% in 2024 and 1.3% after 2025), but significantly higher than the European Commission (1.0%), the OECD (1.0%) and Rexecode, which estimates that potential growth will be below 1% after 2023. A replication of the methodology used by the Government would lead to an estimate close to 1%, based on the latest Insee labour force projections and taking into account the effects of a gradual increase in the legal retirement age.

18. At the end of the programming period, the potential GDP forecast of the Government is higher than that the forecast of the European Commission (+2.1% in 2026) and the IMF (+0.5% in 2027).

19. There are also significant downside risks to all potential growth estimates: the possible impact of the health crisis on the productive fabric and on the skills of the workforce, new crises that could have a lasting impact on potential GDP, and the costs of the ecological transition and of curbing public and private debt.

20. **The High Council therefore reiterates its assessment that, on the one hand, the assumption for the output gap in 2022 (-1.1 GDP points) and, on the other hand, that for potential growth (1.35% per year from 2022 to 2027) are optimistic, notably because the latter assumes significant and immediate effects of reforms (of the minimum income scheme, pensions, unemployment insurance, apprenticeship, etc.) for which neither the modalities, nor the impacts, nor the timetable are documented.**

21. **The High Council considers that these assumptions make the public finance path presented by the Government for the period 2023-2027 particularly fragile.**

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

1- The Government’s scenario:

22. According to the Government's referral: “*Actual growth over the period 2024-2027 would be higher than its potential rate of 1.35% and the output gap would thus be closed in 2027. Growth would average 1.7% over 2024-2027, with a slightly higher rate at the end (1.8% in 2027) than at the beginning of the period (1.6% in 2024), reflecting the gradual dissipation of the constraints linked to the health crisis and the conflict in Ukraine*.”

23. “Inflation would gradually fall back to its estimated long-term level of 1.75% as the transmission of past commodity price increases ends and supply tensions dissipate. It would return to +1.75% in 2026 in the CPI sense, a level consistent with the ECB's target of 2% for the euro area in the HICP sense.”

2- Assessment of the High Council:

24. The observations relating to the Government's macroeconomic forecasts for the years 2022 and 2023 are presented in detail in Opinion No. 2022-4 in the Budget bill and Social security financing bill for 2023.

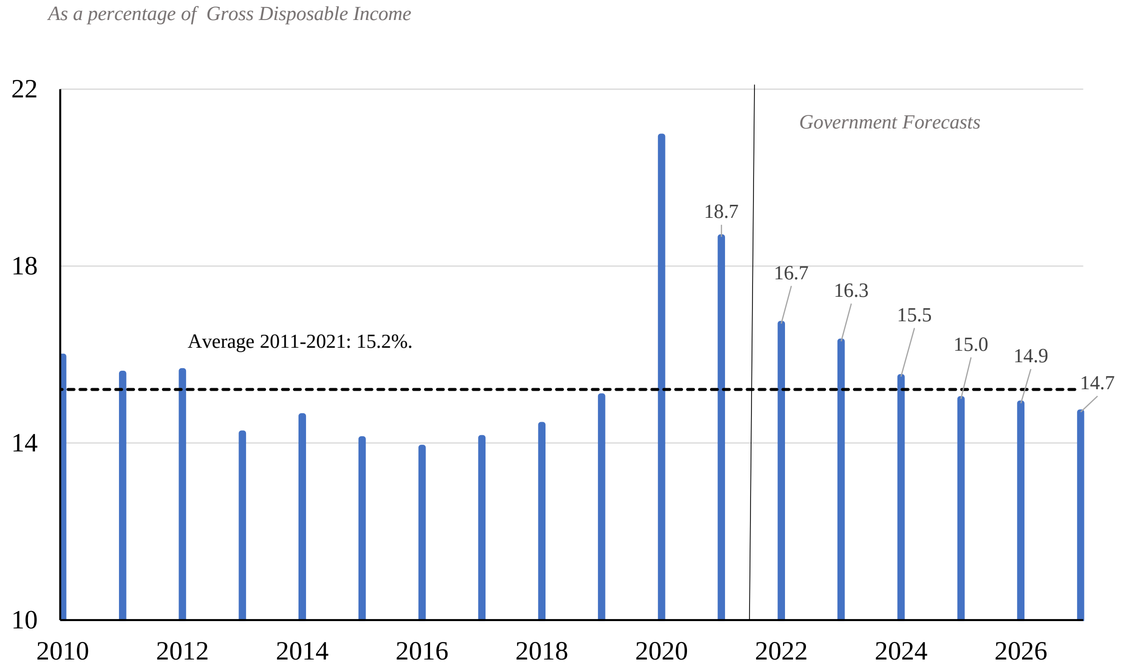
25. The macroeconomic scenario adopted by the Government for the years 2024 to 2027 presented in the draft PFPL is very close to the one included in the 2022-2027 Stability Programme, on which the High Council gave its opinion in Opinion No. 2022-3.

26. The assumptions for GDP growth from 2024 to 2027 are unchanged from those in the Stability Programme. The Government expects growth to exceed potential growth from 2024 until 2027: GDP growth is expected to be 1.6% in 2024, 1.7% in 2025 and 2026, then 1.8% in 2027, compared with potential growth estimated at 1.35% per year over the same period. In this context, the output gap is estimated at -1.1% of potential GDP in 2022 and would gradually narrow and be closed in 2027.

27. This closure of the output gap over the period is based on an anticipated drop in the household savings rate, the maintenance of a high level of the business investment rate and a positive contribution from foreign trade each year until 2027. None of these assumptions can be excluded a priori, but they are all surrounded by downside risks, so that the scenario presented by the Government is based on a combination of favourable assumptions.

28. The household savings rate is expected to drop throughout the period. Its decline would even be slightly stronger in 2024 and 2025 than anticipated in the Stability Programme. The new geopolitical and health risks that emerged in recent years may, however, encourage households to maintain increased savings over the long term compared with the previous period; the erosion of the purchasing power of their assets as a result of the high inflation in 2022 could have the same effect. Nevertheless, a temporarily larger decline in the household savings rate is also possible, given the excess savings accumulated in 2020 and 2021 and the possibility that households draw on their savings to maintain their consumption.

Figure 2: households savings rate in France

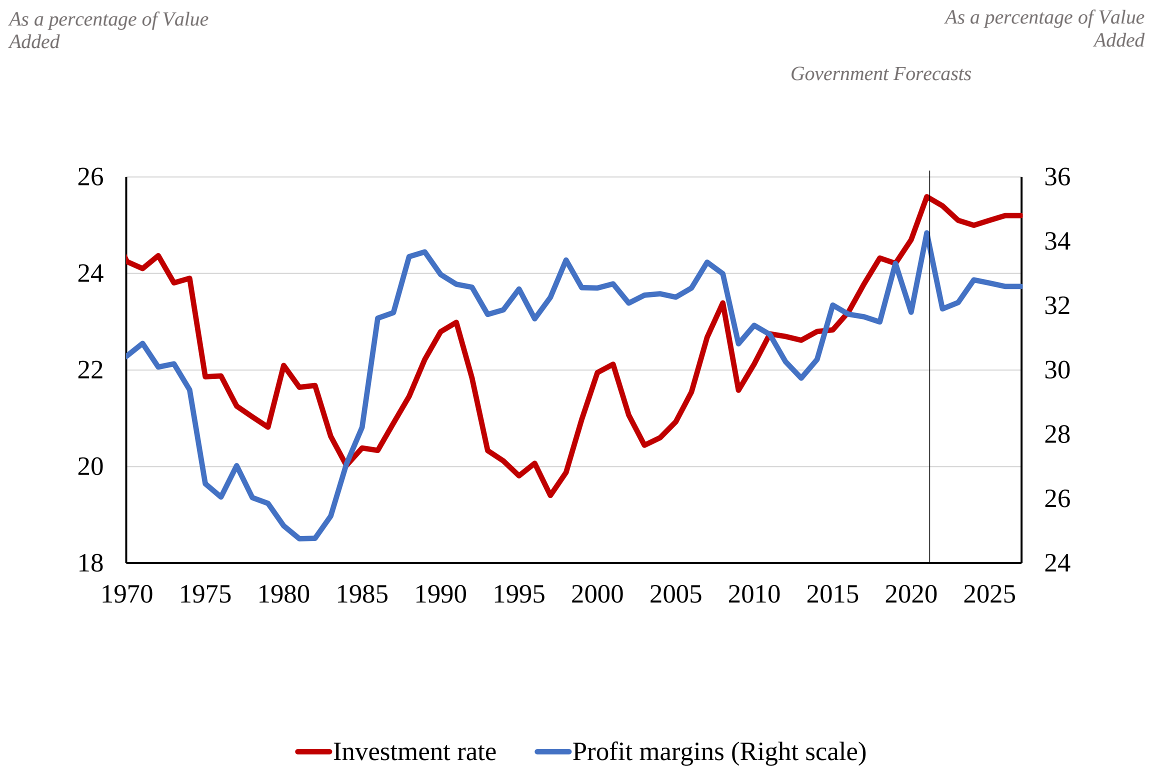


Sources: Insee[1], Public Finance Programming bill

29. The assumption of a business investment rate remaining at a historically high level (above 25% throughout the period) also seems optimistic, since the ECB has engaged in a cycle of monetary policy tightening in the euro area, financing conditions are becoming less favourable, and the operating results of non-financial companies in many sectors (energy and shipping being the exceptions) will have suffered from only partial transmission of their higher input prices and labour costs to selling prices.

[1] French National Institute of Statistical and Economic Studies

Figure 3: investment rate and profit margins of non-financial corporations in France



Source: Insee[2]*, Public Finance Programming bill*

30. The Government forecasts a positive contribution of foreign trade to growth every year from 2024 to 2027. This forecast assumes that world trade will remain strong over the entire period, despite the high level of uncertainty associated with the combination of geopolitical, financial and health risks and the need for central banks to curb demand in order to control inflation. It also assumes significant gains in the export market share of the French economy, a development that is possible, notably because of the gains in competitiveness due to the devaluation of the euro against the dollar and the lower inflation recorded by France thanks to the "energy shield" measures, but which would mark a strong break with the trend observed since the beginning of the 2000s.

31. The Government's GDP growth forecast for the period 2024-2027 appears to be subject to essentially downward risks, even in the absence of unforeseeable shocks such as the health crisis or the war in Ukraine, which have led to macroeconomic and public finance results that are much less favourable than forecasted in the previous programming law (see box). Moreover, the near-stability of public spending in volume terms over the period 2023-2027 would mark a

[2] French National Institute of Statistical and Economic Studies

significant change from past trends and should weigh on activity in the short term, even though it is insufficient to ensure a reduction in the public deficit to well below 3 points of GDP.

32. The government expects inflation to ease to an annual average of 3.0% in 2024 (revised upwards by 1.1 percentage points from the Stability Programme), 2.1% in 2025, 1.75% in 2026 and 2027. The dissipation of supply tensions and the end of the transmission of past commodity price increases could effectively dampen price increases in the medium term. Conversely, the expected decline in inflation may seem rapid, especially with the chosen scenario of sustained, above-potential growth and in a context where inflation has consistently surprised forecasters for the past two years.

33. **As it has already pointed out in its opinion on the 2022-2027 Stability Programme, the High Council notes that the closure of the output gap during the years 2024 to 2027 is based on very favourable assumptions of a continued decline in the households savings rate supporting consumption, a continued high level of business investment and a positive contribution from foreign trade over the entire period. The resulting growth scenario is optimistic.**

34. **The Government's inflation forecast assumes a return to a level compatible with the ECB's target from 2026 onwards, with a moderate rise in interest rates, even though there are major uncertainties surrounding the rise in rates needed to control inflation.**

Review of the PFPL 2018-2022 and lessons for programming laws

The comparison of macroeconomic and public finance results with the path adopted in the previous programming law sheds light on the scenario adopted for the present draft programming law:

Less favourable macroeconomic results than foreseen in the PFPL, due to major crisis (health crisis, then war in Ukraine)

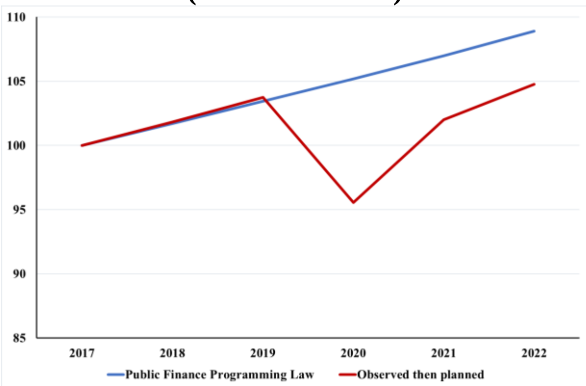
Real GDP followed closely the path planned by the PFPL until 2019, in a favourable economic context, then deviated significantly from 2020 onwards (up to -9 points that year) under the effect of the health crisis and then the war in Ukraine.

The health crisis has deeply affected the functioning of the economy from February 2020 due to the precautionary behaviours it has caused and to the restriction measures taken by public authorities, in France and among our trading partners. In 2022, the health crisis continues with less marked effects on activity, but the latter is penalised by the disruption of global supply chains and by the rise in commodity prices, especially energy prices, in particular since the war in Ukraine.

In 2022, the GDP deficit compared to the PFPL forecast should remain substantial at almost 4 points.

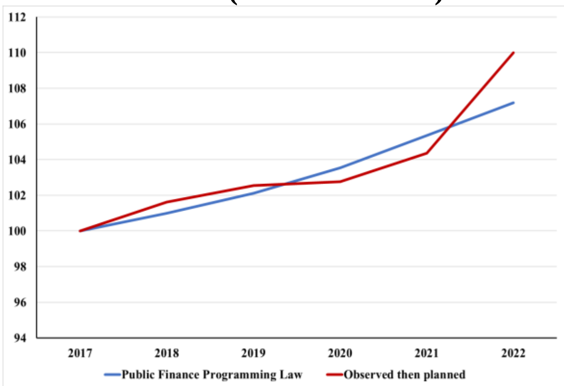
Consumer Price Index deviated little from the PFPL path until 2021: 0.5 points above it on average in 2018 and 2019 in a favourable economic context, and 0.8 points below it on average in 2020 and 2021, during the health crisis. In 2022, however, CPI accelerate sharply, bringing the deviation from the PFPL path to around 2.6 points, in a context of pressure on productive supply and of an unexpected rise in world commodity prices.

Figure: GDP in volume (base 100 = 2017)



Sources: Insee, Public Finance Programming Law 2018-2022

Figure: Consumer prices index excluding tobacco (base 100 = 2017)



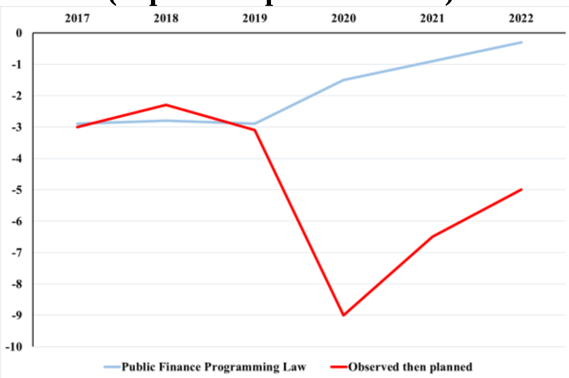
Sources: Insee, Public Finance Programming Law 2018-2022

A deterioration in the public balance and debt relative to the objectives of the PFPL from 2020 onwards

In the 2018-2022 PFPL, the public balance, estimated at -2.9 points of GDP in 2017, was supposed to return to close to balance by 2022, at -0.3 points of GDP. The public debt, starting from 96.7 points of GDP in 2017, was supposed to increase slightly until 2019 (97.1%), before falling back to 91.4% of GDP in 2022.

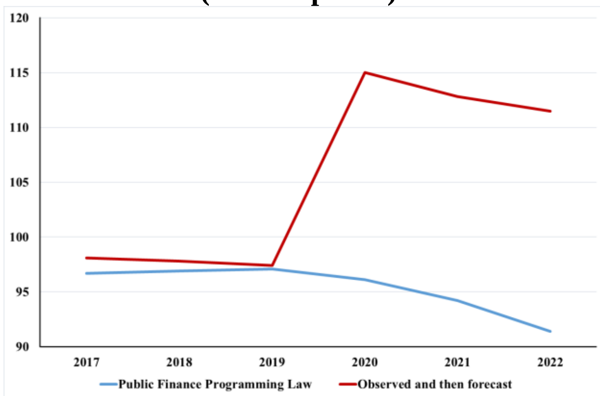
Both the public balance and the public debt followed fairly closely the path set out in the PFPL in 2018 and 2019, allowing France to emerge from the excessive deficit procedure as early as 2018 as planned. However, it deviated significantly from 2020 onwards.

Figure: General government balance (in points of potential GDP)



Sources: Government, Public Finance Programming Law 2018-2022

Figure: Public debt (in GDP points)



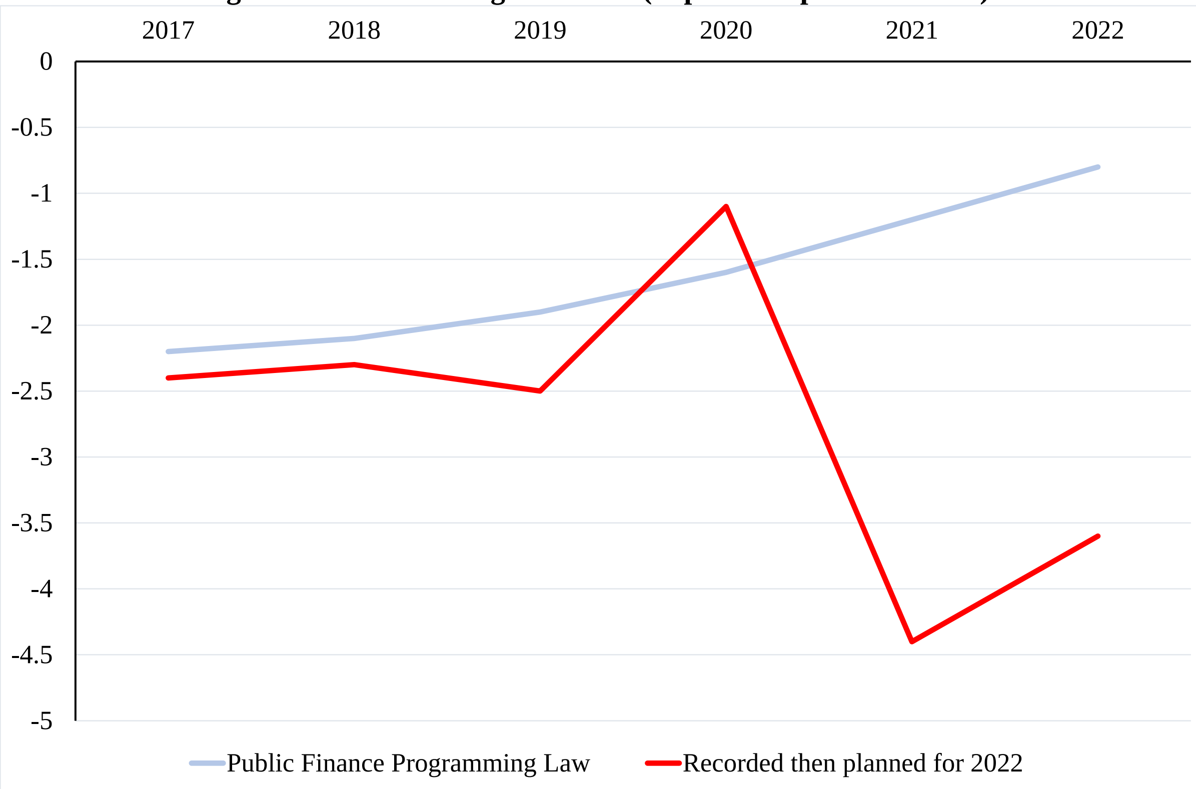
Sources Insee, Public Finance Programming Law 2018-2022

A deterioration of the structural balance

The deterioration in the public balance compared to the PFPL in 2022 (4.7 points of GDP) partly reflects the impact of less favourable activity, which has affected public revenues, but also results from measures to reduce taxes in addition to those planned in the PFPL (by almost one point of GDP) and from increases in expenditure (support measures during the health crisis, measures in favour of hospitals staff and investment, recovery plan, France 2030 public investment scheme, etc.).

The structural balance, which neutralises the effect of the economic situation, is thus 2.8 points of GDP worse than in the PFPL[3] according to the estimate given in the Amending budget bill for 2022[4].

Figure: Structural Budget Balance (in points of potential GDP)



Sources: Government, Public Finance Programming Law 2018-2022

* the structural balance is here calculated with the potential framework of the PFPL 2018-2022

This comparison illustrates once again the asymmetrical nature of the budgetary policy consistently pursued in France, which leads to a tendency for public debt to grow contrary to the intentions stated in the programming law: very expansive in an unfavourable economic phase, but on the other hand little, if at all, restrictive in a favourable economic phase.

III. Observations on the public finance programming

1- The Government's scenario:

35. Organic Law No. 2001-692 of August 1, 2001 on finance laws, as amended by the Organic Law No. 2021-1836 of December 28, 2021 on the modernisation of public finance management, states that "the High Council shall assess the consistency of the planned

[3] Part of the deviation of the structural balance from the PFPL path results from the inclusion of certain support measures, which are a priori temporary, in the structural balance. This effect, which is significant in 2021, should be more marginal in 2022 as most of the emergency support measures linked to the health crisis come to an end.
[4] Since the Amending budget bill for 2022, growth in 2022 has been revised slightly upwards (from 2.5% to 2.7%) and the public balance is unchanged (-5 points of GDP), which means that a higher gap of around 0.1 points of GDP is expected.

programme with the medium-term objective (MTO) adopted and with France's European commitments".

The European Rules

The European rules governing public finances are set out in the EU Treaties, in the Stability and Growth Pact, which brings together several regulations and directives, and in the rules stemming from the Intergovernmental Treaty on Stability, Coordination and Governance signed by France in 2012.

In March 2020, the Commission triggered the general escape clause of the Stability and Growth Pact,which allows Member States to deviate from the normally applicable requirements due to the exceptional circumstances resulting from the health crisis, *"provided that medium-term fiscal sustainability is not put at risk".*

The Commission has launched a review of the European economic governance with a view to proposing adjustments to current budgetary rules, which were considered even before the health crisis to be too complex, sometimes pro-cyclical, and not taking sufficient account of the specific situation of each Member states. The Commission is expected to make its proposals shortly.

The European rules should be fully applied again from 2024 onwards, probably with some changes, which could give more weight to a rule on the growth of public spending. However, the rules laid down in the Treaties, particularly in terms of the actual balance, will probably not be changed.

As the texts currently stand, the main provisions applicable to France are as follows: the actual government balance must be above -3 points of GDP and the government debt must be approaching the 60 points of GDP threshold at a sufficiently rapid pace.

Member States must set a medium-term objective (structural balance) of at least -0.5 points of GDP. Convergence towards this objective must be "rapid". For Member States such as France with a debt-to-GDP ratio above 60 points, this convergence must be based on a structural adjustment of more than 0.5 points of GDP per year.

Moreover, as France has not reached its medium-term objective, the growth rate of public spending must be lower than a reference rate, lower than the potential growth rate of the economy, unless the excess spending is offset by tax increase measures.

The European rules are applied with margins of flexibility, related to unfavourable economic conditions, public investment expenditure or structural reforms.

36. The effective deficit path in the public finance programming bill for 2023-2027 is almost identical to the one presented in July 2022 in the Stability Programme. The actual public balance, projected at -5.0 points of GDP in 2022, would be stable in 2023 and then gradually brought back to -2.9 points of GDP in 2027. The structural balance path is also almost identical to that in the July Stability Programme: it is expected to be a bit lower in 2022, to -4.2 points of potential GDP (instead of -4.0 points in the Stability Programme), and then to improve gradually over the rest of the programme period, returning to -2.8 points in 2027. The medium-term objective is set at -0.4 percentage points of GDP.

37. The High Council observes that the public finance path set out in the draft programming law leads, after five years, to a deficit that is far from the medium-term objective set out in the same draft law.

Table 1: path of the effective, cyclical and structural balance between 2022 and 2027

	2022	2023	2024	2025	2026	2027
Effective balance (in GDP points)	**-5.0**	**-5.0**	**-4.5**	**-4.0**	**-3.4**	**-2.9**
Cyclical balance (in GDP points)	-0.6	-0.8	-0.7	-0.5	-0.3	0.0
Temporary measures (in potential GDP points)	-0.1	-0.2	-0.1	-0.1	0.0	0.0
Structural balance (in potential GDP points)	-4.2	-4.0	-3.7	-3.4	-3.1	-2.8
Structural adjustment	***0.9***	***0.2***	***0.3***	***0.3***	***0.3***	***0.3***

Source: Draft PFPL 2023-2027

2- The consistency of the public finance path with France's European commitments

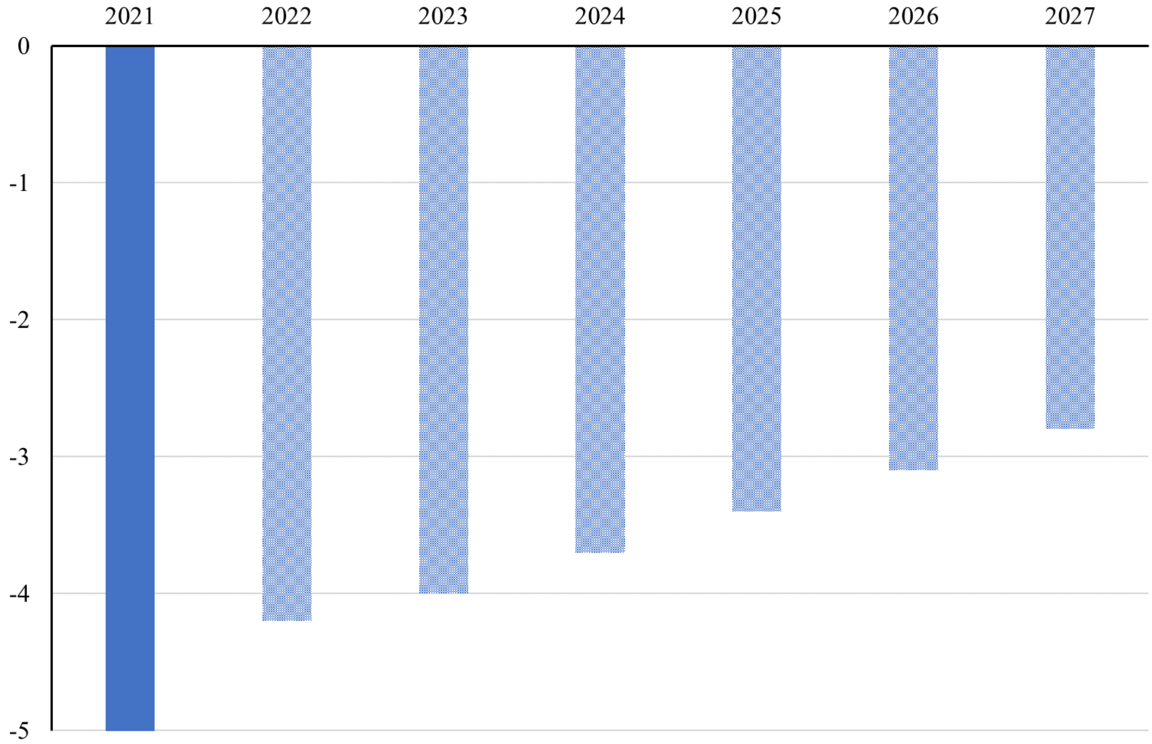
38. In March 2020, the Commission triggered the general escape clause of the Stability and Growth Pact due to the exceptional circumstances resulting from the health crisis. This clause allows Member States to deviate from the normally applicable budgetary requirements until the end of 2023. The European budgetary rules should apply again from 2024 onwards, possibly with adjustments to be proposed by the Commission in the coming months (see box above).

39. The High Council already pointed out in its opinion on the 2022-2027 Stability Programme that the actual balance path is not very ambitious with respect to France's European commitments and the trajectory is much slower than the one planned by our European partners, with the French public deficit barely falling below 3 points of GDP in 2027 (2.9 points of GDP).

40. The level of the medium-term objective (MTO) (-0.4 points of potential GDP), which is identical to that used in the last two programming laws, is in line with the TSCG. However, in the Government's scenario, the structural balance would only return to -2.8 points of potential GDP by the end of the programming period, and with a very significant gap with the MTO. The public accounts are significantly more deteriorated at the beginning of the programming period than when the previous PFPL was drawn up, which may explain a slower convergence towards the MTO. Nevertheless, the envisaged structural adjustment path can hardly be considered to be in line with the provision of the TSCG according to which "the contracting parties shall ensure rapid convergence towards their medium-term objective" (Article 3).

41. The expected structural adjustment, i.e. the change in the structural balance, would be of 0.9 points of GDP in 2022. This high level of adjustment is not explained by a structural effort but exclusively by exceptionally favourable growth in tax revenues and the gradual phasing out of emergency and support measures in response to the health crisis (accounted for in the structural balance). The structural adjustment would amount to 0.2 points of GDP in 2023, a year covered by the general escape clause of the Stability and Growth Pact, and then to 0.3 points of GDP each year from 2024 to 2027.

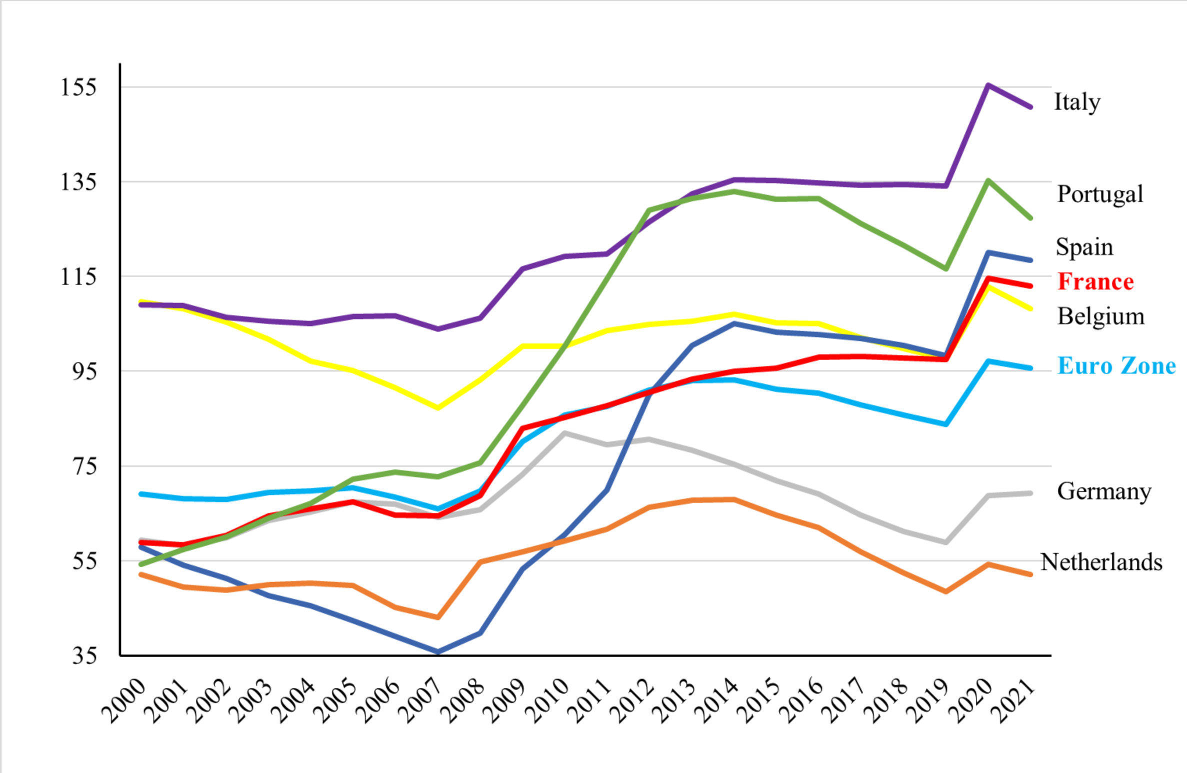
Figure 4: General Government structural balance (% of potential GDP)



Source: Public Finance Programming Bill for the years 2023 to 2027

42. At less than 0.5 percentage point of GDP per year, this adjustment in the planned structural deficit does not a priori comply with the provisions of Article 5 of EU Regulation 1466/97 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies. However, when examining a Member State's budgetary situation, the European Commission and the Council may take into account the implementation of major structural reforms or other elements of flexibility foreseen by EU rules that can allow a temporary deviation from the adjustment path towards the medium-term objective (MTO).

Figure 5: public debt paths (% of GDP) in the euro area



Source: Eurostat

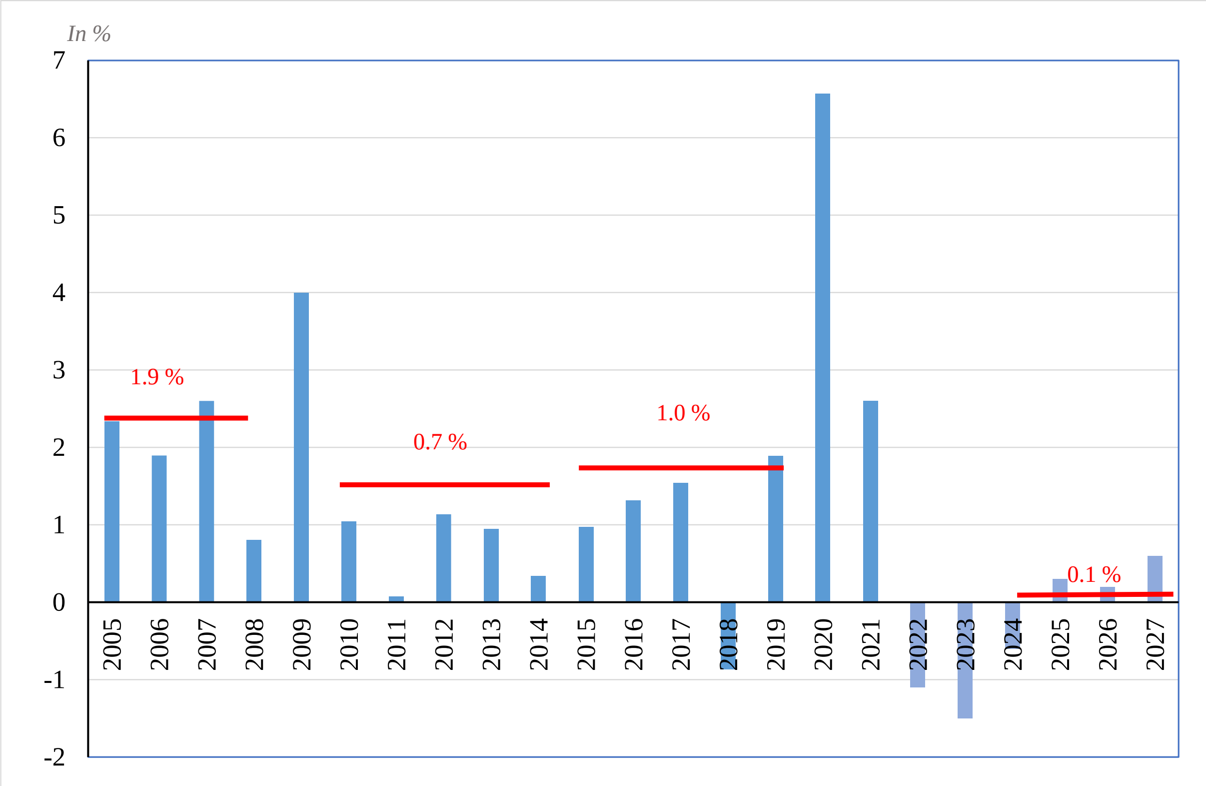
43. The Government debt ratio would decline by more than one point of GDP in 2022 to 111.5 points of GDP and then remain almost stable before declining again at the very end of the programme period to 110.9 points of GDP in 2027. France's indebtness situation has deteriorated in relative terms across euro area Member States. Indeed, it is now one of the seven countries in the euro area with a debt above 100 points of GDP, while 11 of them have a debt ratio under 80 points of GDP. A comparison of the Stability Programmes submitted in the spring by the other Member States shows that, if the planned trajectories are respected, France will continue to see its relative debt position deteriorate.

3- The High Council's assessment

44. According to the Government, public spending will decrease in volume terms in 2022 and 2023 (by 1.1% and 1.5% respectively), in particular due to the decline in emergency and support expenditures needed during the health crisis, but less than forecasted in the Stability Programme. Public spending will be virtually stable (+0.1% in volume on average per year) over the period 2024-2027.

45. This expected control of public spending would be unprecedented and would lead to a drop of 4.6 points between 2021 and 2027 in its weight in the GDP. It would reach 53.8 GDP points at the end of the period, *i.e.* its level in 2019, seven years after the start of the health crisis.

Figure 6: growth rate of public expenditure in volume (in %)



Source: Public finance programming bill for the years 2023 to 2027

46. This stability of public spending in volume results in particular from the planned reduction in local public operating expenditure of 0.5% in volume per year between 2023 and 2027. Achieving this objective, which is more ambitious than the one set by the previous programming law, would be made possible by a new contractualisation mechanism with local authorities. It assumes not only that this mechanism is strictly implemented, but also that local authorities will not adjust their investment effort to the resulting increase in their savings. The increase in the financing capacity of local governments (0.5 point of GDP in 2027) included in the draft programming law thus seems fragile.

47. This stability in volume also assumes strong control of social security administration expenditure. Health insurance expenditure within the scope of the national health insurance expenditure target (+2.7% in 2024 and 2025, then 2.6% in 2026 and 2027) is projected to grow significantly slower than GDP (+4.1%, then +3.5%, 3.3% and 3.4%), which rarely happened in the past. This implies resolute action to curb spending, particularly on office pratice, despite the increasing impact of an ageing population and technical progress, the details of which are not documented in the draft programming law. Furthermore, the trajectory does not reveal any additional costs related to old-age dependency spending despite an ageing population. Finally, the features and timetable of the pension reform have not been specified. In any case, the resulting savings would be gradual and limited over the programming period.

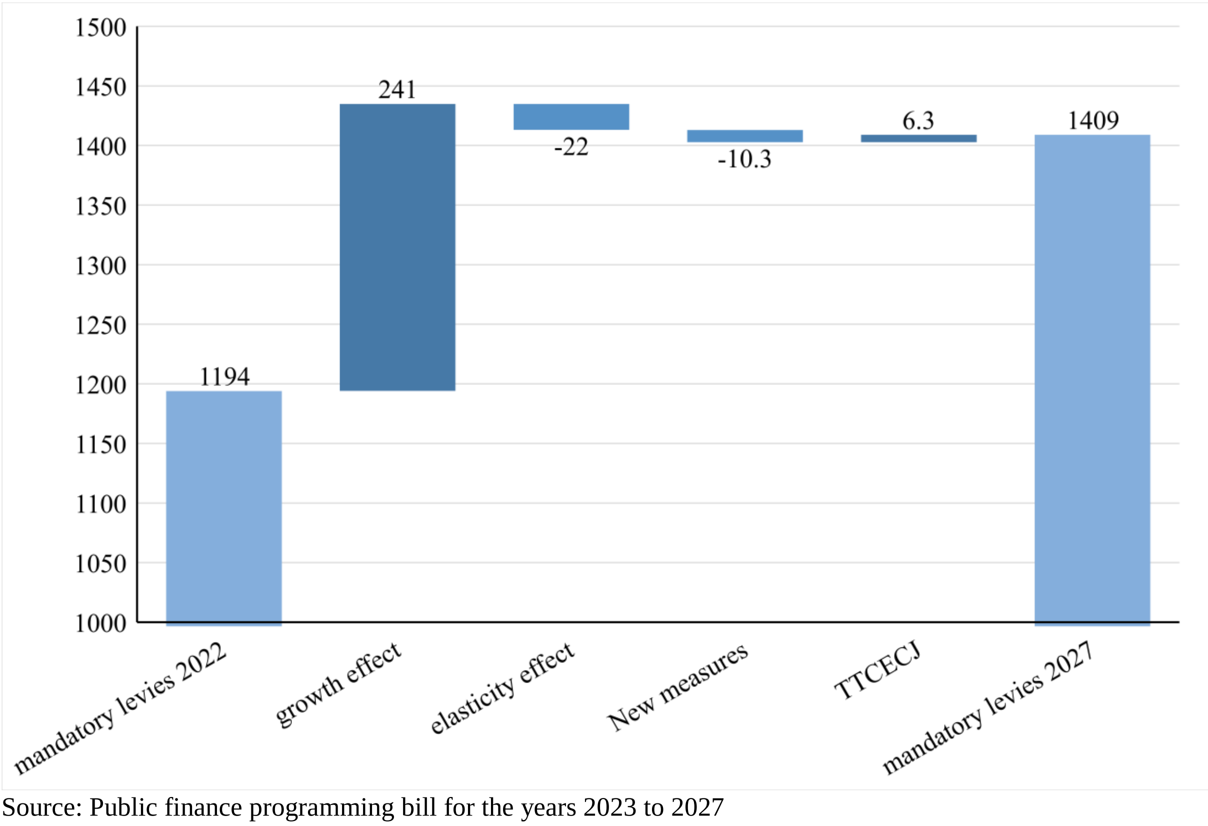
48. The public finance programming bill also provides for an ambitious path for controlling State spending. Within the new definition of the perimeter of State spending introduced by the bill, spending should fall by 0.7% in volume per year on average between 2023 and 2027. This path will be all the more difficult to achieve as the appropriations included in the sectoral

programming laws (defence, interior, research) will make State spending more rigid over the period, implying a very marked reduction in the spending of all other 'non-priority' ministries.

49. This path for public spending (+0.1% in volume on average per year over the period 2024-2027) appears all the more ambitious as it will be set against a context of an expected rise in interest rates which will have an impact on the debt interest expenditures.

50. After an expected decrease in 2023 and 2024, mainly due to a growth of tax revenues that is slower than activity in 2023, the tax rate is expected to remain stable from 2025 onwards at 44.3% of GDP. This trajectory results from the combination of a unitary elasticity (equal to 1) of taxes and social contributions to activity from 2024 and of new measures whose effect is less than 0.1 point of GDP. While this trajectory makes provision for €3.5bn tax cuts on households, it assumes on the other hand the removal of the tax loophole on non-road diesel fuel, that has been postponed several times (€0.9bn). Above all, it relies on a return of €9.2bn from the reduction of tax and social security loopholes, without specifying which ones, and from the fight against tax and social security fraud. It will be difficult to achieve these objectives, which have often been stated in the past but never reached with such magnitude in practice.

Figure 7: evolution of taxes and social contributions between 2022 and 2027

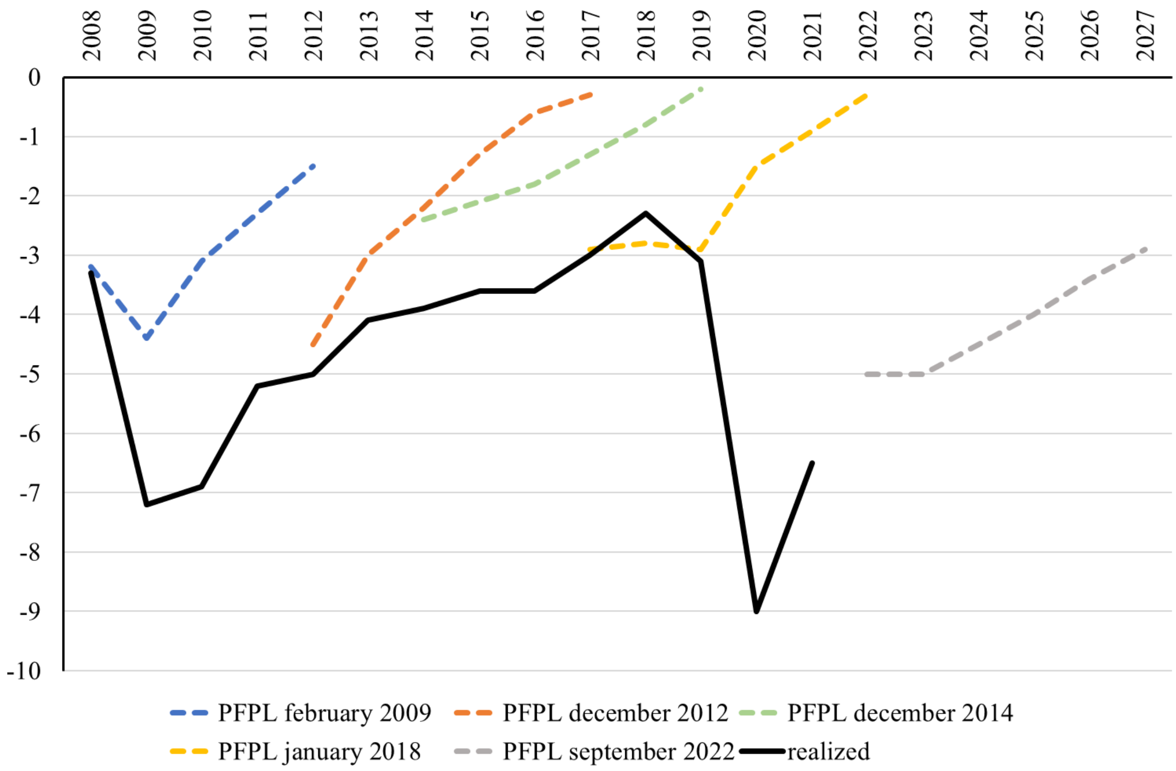


Source: Public finance programming bill for the years 2023 to 2027

51. The combination of favourable assumptions on economic growth, on the control of public spending and on the increase in taxes and social contributions makes this public finance trajectory particularly fragile. Contrary to what was observed during the implementation of previous programming laws, the latter assumes a determined implementation of reforms from the start of the period, which have yet to be fully explained, and the ability to adjust the

expenditure and revenue targets in the case of a growth rate lower than expected, as the High Council fears.

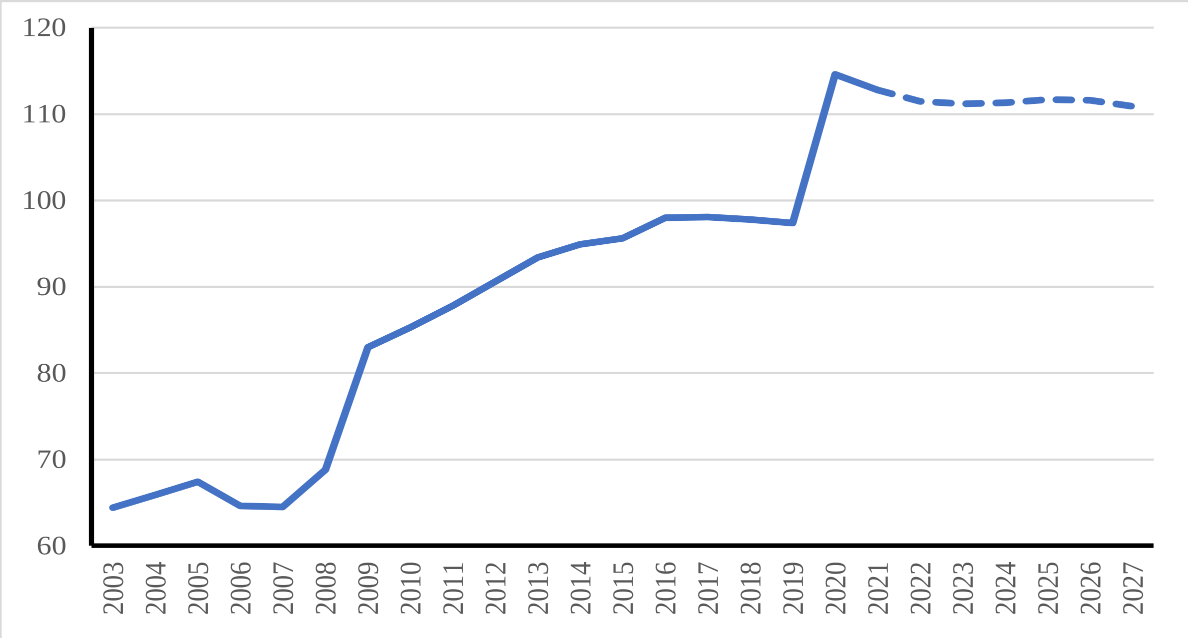
Figure 8: actual general government balance (% of GDP)



Sources: Insee, previous Programming Laws, Public Finance Programming Bill for years 2023 to 2027

52. As a proportion of GDP, the public debt would be stable overall between 2022 and 2026 at around 111.5 points and would only really start to decline in 2027, with the public balance moving away from the balance that stabilises the weight of the public debt in that year by 0.8 points. As indicated by the High Council in its opinion on the Stability Programme, this scenario of a modest and delayed decline in the public debt ratio is based on an optimistic growth scenario: lower growth than expected by the government would, on the contrary, lead to an increase in the debt ratio at this horizon. This would also be the case if the spending target or the increase in taxes and social contributions were not respected.

Figure 9: public debt path



Source: Insee, public finance programming bill for the years 2023 to 2027

53. **The HCFP considers that the path presented by the Government is not very ambitious, especially in light of France's European commitments. The draft programming law does not provide for a rapid return to the objective of balanced public finances, to which France has committed itself, and the targeted decline in the debt ratio is modest and late, even though the growth assumptions are optimistic. Moreover, the unprecedented effort to control expenditure and the planned increase in certain taxes and social contributions included in the programming law are only partially documented.**

54. **To ensure the sustainability of its public finances, France, which is one of the most indebted countries in the euro area and has a high tax rate, needs a solid expenditure savings programme.**

*

* *

This opinion will be published in the Official Journal of the French Republic and attached to the public finance programming bill for the years 2023-2027 when it is submitted to Parliament.

Etablished in Paris on 21 September 2022.

ANNEX 1

Macroeconomic scenario of the public finance programming bill 2023-2027

Main assumptions of the 2022-2027 macroeconomic scenario*						
	2022	2023	2024	2025	2026	2027
GDP (*)	2.7	1.0	1.6	1.7	1.7	1.8
GDP deflator	2.8	3.6	2.4	1.8	1.6	1.6
CPI excluding Tabaco	5.4	4.3	3.0	2.1	1.75	1.75
Private sector wage bill (**)	8.6	5.0	3.9	3.6	3.4	3.4
Potential growth	1.35	1.35	1.35	1.35	1.35	1.35
Potential GDP (in billions€ 2010)	2,390	2,422	2,454	2,488	2,521	2,555
Output gap (in % of GDP)	-1.1	-1.4	-1.2	-0.8	-0.5	0.0

Note: Data expressed as annual growth rates, unless otherwise specified

(*) Data adjusted for working days.

(**) Non-agricultural market sectors

ANNEX 2
Public finance scenario of the public finance programming bill 2023-2027

Growth in public spending, excluding tax credits

	2023	2024	2025	2026	2027
Growth rate in value	2.8	2.3	2.3	2.0	2.4
Growth rate in volume	-1.5	-0.6	0.3	0.2	0.6
Inflation excluding tobacco	4.3	3.0	2.1	1.75	1.75

Growth of public expenditure by sub-sector, excluding tax credits, at constant scope, excluding transfers, in volume

	2023	2024	2025	2026	2027
General Government	-1.5	-0.6	0.3	0.2	0.6
Central Government	-2.6	-2.5	-1.1	0.4	1.6
Local Government	-0.6	0.1	0.4	-1.3	-1.1
Social Security funds	-1.0	0.5	1.2	0.7	0.6

Government balance (expressed according to national accounting conventions)

	2023	2024	2025	2026	2027
Public balance	-5.0	-4.5	-4.0	-3.4	-2.9
Structural balance (in points of potential GDP)	-4.0	-3.7	-3.4	-3.1	-2.8
Structural adjustment	0.2	0.3	0.3	0.3	0.3

Expenditure and revenue (expressed according to national accounting conventions)

	2022	2023	2024	2025	2026	2027
Public expenditure ratio (*)	57.6	56.6	55.6	55.0	54.3	53.8
Taxes and social contributions ratio (including EU)	45.2	44.7	44.2	44.3	44.3	44.3
Revenue ratio excluding taxes and social contributions	7.4	7.2	7,1	7.0	6.8	6.8
Tax credit key	0.2	0.0	0.0	0.0	0.0	0.0

(*) Excluding tax credits

Change in structural balance 2022-2027

	2022	2023	2024	2025	2026	2027
Change in structural balance (structural adjustment)	0.9	0.2	0.3	0.3	0.3	0.3
Structural effort	-0.2	1.3	0.3	0.4	0.5	0.3
Input of new measures in tax and social contributions	-0.3	0.0	-0.5	-0.1	0.0	0.0
Spending effort (including tax credits)	0,1	1,3	0,8	0.5	0.5	0.3
Non-discretionary component	1.0	-1.1	-0.1	-0.1	-0.1	0.0

Elasticity of tax and social contributions 2022-2027

	2022	2023	2024	2025	2026	2027
Elasticity of taxes and social contributions (non-EU)	1.5	0.6	1.0	1.0	1.0	1.0

Debt by sub-sector 2021-2027

	2021	2022	2023	2024	2025	2026	2027
Public debt (in GDP points)	112.8	111.5	111.2	111.3	111.7	111.6	110.9
Central Government's contribution	92.0	92.2	93.2	94.6	96.3	97.8	99.0
Local public Government's contribution	9.8	9.4	9.1	8.9	8.6	8.1	7.4
Social Security funds'w contribution	11.0	9.9	8.9	7.7	6.7	5.7	4.5

Interest expense and primary balance 2022-2027

	2022	2023	2024	2025	2026	2027
General government balance	-5.0	-5.0	-4.5	-4.0	-3.4	-2.9
Interest expense	1.8	1.6	1.8	1.9	2.0	2.1
Primary balance	-3.2	-3.4	-2.7	-2.1	-1.5	-0.8