Haut Conseil des Finances Publiques

Opinion n° HCFP-2024-1
on the general government structural balance presented in the budget settlement bill for 2023

15 April 2024

Executive Summary

The general government deficit amounts to 154.0 billion euros in 2023, or 5.5 points of GDP. This is 28.2 billion euros and 0.7 points of GDP higher than in 2022, and much worse than the forecasts in the initial Budget Laws for 2023 and 2024 and in the public finance programming Law (LPFP) of 18 December 2023-2027, which estimated the deficit at 4.9 points of GDP. This deterioration increases the divergence of France's public finances from those of our main European partners and reflects a worrying situation.

In its opinion issued on 17 March 2020 on the first Amending Budget Bill for 2020, the High Council of Public Finance noted, at the Government's request, that the health crisis and its economic and financial repercussions constituted unusual events beyond the Government's control and therefore fell within the "exceptional circumstances" referred to in Article 3 of the Treaty on Stability, Coordination and Governance (TSCG).

In accordance with Article 62 of the Organic Law on Budget Laws of 1st August 2001, it took this into account in its opinions on the Budget Settlement Bill for the years 2021 and 2022 and therefore did not trigger the correction mechanism, even though the structural balances recorded for these two years differed by more than 0.5 points of GDP from those forecast in the public finance programming Law for the years 2018 to 2022 in force at the time.

In application of the same provisions, the High Council has now been presented with the general government structural balance presented in the budget settlement bill for 2023.

In this opinion, the High Council notes that economic conditions, which were severely affected in 2020 and 2021 by the health crisis and then by the energy crisis in 2022, have improved significantly in 2023.

Consequently, pursuant to the provisions of II of article 5 of law no. 2023-1195 of 18 December 2023 on public finance programming for the years 2023 to 2027, the High Council hereby notes that the exceptional circumstances identified in 2020 no longer exist and must not be considered in the examination of this bill.

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The structural component of the 2023 deficit amounts to 4.6 points of potential GDP, as estimated by the public finance programming Law (LPFP) of 18 December 2023, to which the Haut Conseil des Finances Publiques must refer. The structural balance has deteriorated by 0.5 points of potential GDP between 2022 and 2023.

This deterioration is explained by the sharp fall of tax revenues as a proportion of GDP. Indeed, even though public spending grew in current euros, it fell in volume terms, due in particular to the phasing out of some of the emergency and stimulus measures adopted in the context of Covid-19 and a fall in the interest burden on inflation-indexed bonds as a result of the decline in inflation. However, this structural adjustment on the expenditure side was more than offset by the fall in revenues as a share of GDP, which is itself due much more to a shortfall in compulsory levies than to newly implemented measures.

Under the terms of Article 62(I) of the amended Organic Law No. 2001-692 of 1st August 2001 on Budget Laws, the High Council has to issue an opinion on the difference between the structural balance recorded and that forecast for the same year by the current LPFP. This gap amounts to 0.5 points of potential GDP in 2023. However, it is partly the result of a methodological change linked to the switching of the national accounts to the 2020 base between 2022 and 2023. Adjusted for this rebasing of national accounts, the difference between the structural balance observed in 2023 and that forecast in the LPFP is less than 0.5 points of potential GDP. It is therefore not "significant" within the meaning of II of the aforementioned Article 62. Under these conditions, there is no need to trigger the correction mechanism for 2023.

However, the fact that the correction mechanism has not been triggered should not obscure the fact that the structural deficit is very high and has deteriorated sharply compared to the objectives of the recently enacted LPFP, whose 2023-2027 trajectory was deemed optimistic and fragile by the High Council.

The structural deficit is now a long way from the medium-term objective (MTO) that France set itself in the 2023-2027 Programming Law, i.e. a structural deficit of less than 0.4 points of potential GDP, whose compliance has been put off to a distant future.

Against a backdrop of rising debt charges, the high level of the structural deficit is delaying the necessary reduction in the debt-to-GDP ratio and could hamper France's ability to cope with any economic shocks and to commit to new spending, particularly for the ecological transition. A significant reduction in the deficit requires, as a priority, resolute action on public spending and a reassessment of the planned tax cuts.

I- Introductory remarks

1- On the subject of this opinion

1. The Haut Conseil des Finances Publiques (High Council for Public Finance) was asked by the Government, pursuant to Article 62(I) of the amended Organic Law on Budget Laws No. 2001-692 of 1st August 2001, to provide an opinion on the introductory article of the general government structural balance presented in the budget settlement bill for 2023. Article 62 stipulates that "*the High Council for Public Finance shall issue an opinion identifying, where appropriate, any significant differences [...] that emerge from a comparison of the results of the past year with the multi-year structural balance guidelines defined in the public finance programming law*". Under the terms of II of the same article, a deviation is considered to be significant when the structural balance presented in the budget settlement bill is at least 0.5% of GDP lower than the public finance programming law in force in a given year or at least 0.25% of GDP per year on average over two consecutive years.

2. The Organic Law also specifies that the structural balance must be calculated in relation to the potential GDP trajectory set out in the report appended to the Public Finance Programming Law. The identification by the High Council of a significant deviation triggers the *"correction mechanism"* within the meaning of Title VI of the Organic Law.

3. In this opinion, the High Council refers to Law 2023-1195 of 18 December 2023 on public finance programming (LPFP) for the years 2023 to 2027.

4. The opinion issued by the High Council pursuant to Article 62(I) of the amended Organic Law no. 2001-692 of 1st August 2001 must also cover compliance with the general government's expenditure targets mentioned in article 1A of the aforementioned Organic Law of 1st August 2021, with regard to the results of the past year's implementation.

2- On the information submitted and the decision timeframe

5. The Government referred the matter to the High Council on 8 April 2024. This referral includes the introductory article of the general government structural balance presented in the budget settlement bill for 2023, including its summary table which presents the nominal balance and the structural balance of general government for 2023 (Appendix 1). It was accompanied by the answers to a questionnaire that had previously been addressed to the relevant government departments.

6. Pursuant to IX of Article 61 of the aforementioned Organic Law, the High Council held a joint hearing with the French Treasury and the Budget Department on 10 April 2024.

II- Remarks on the exceptional circumstances clause

7. In its opinion of 17 March 2020 on the first bill of the Amending Budget for 2020, the High Council decided, upon request of the Government, that the health crisis and its economic and financial repercussions fell within the scope of the exceptional circumstances referred to in Article 3 of the Treaty on Stability, Coordination and Governance (TSCG), which states in paragraph b that "*'exceptional circumstances' refers to the case of an unusual event outside the control of the Contracting Party concerned which has a major impact on the financial position of the general government or to periods of severe economic downturn as set out in the revised Stability and Growth Pact, provided that the temporary deviation of the Contracting Party concerned does not endanger fiscal sustainability in the medium-term.*"

8. It took account of these exceptional circumstances in its opinions on the Budget Settlement Bills for the 2021 and 2022 financial years by not triggering the correction mechanism, even though the structural balances recorded for these two financial years differed significantly from those forecast by the public finance programming Law for the years 2018 to 2022.

9. Law no. 2023-1195 of 18 December 2023 on public finance programming for the years 2023 to 2027 added to the procedures for lifting this clause. In accordance with the provisions of Article 5(II), the High Council may note, at the request of the Government or in its opinion on the draft law relating to the results of management and approving the accounts for the year, that exceptional circumstances have ceased to exist.

10. The High Council notes that the conditions for economic activity, which had been severely restricted from 2020 to 2022 by the health crisis and then by the consequences of the war in Ukraine, improved significantly in 2023; in particular, energy prices and the tensions that had led to fears of disruptions in the supply of energy products began to ease from the end of 2022 and the risks of shortages did not materialise. The High Council also notes that the European Commission announced in March 2023 that the general derogation clause, which allows EU Member States to derogate from the obligations applicable under the European budgetary framework, would be deactivated at the end of 2023, and announced its intention to propose to the Council to open excessive deficit procedures based on the deficit in spring 2024 on the basis of actual data for 2023, in accordance with the legal provisions in force.

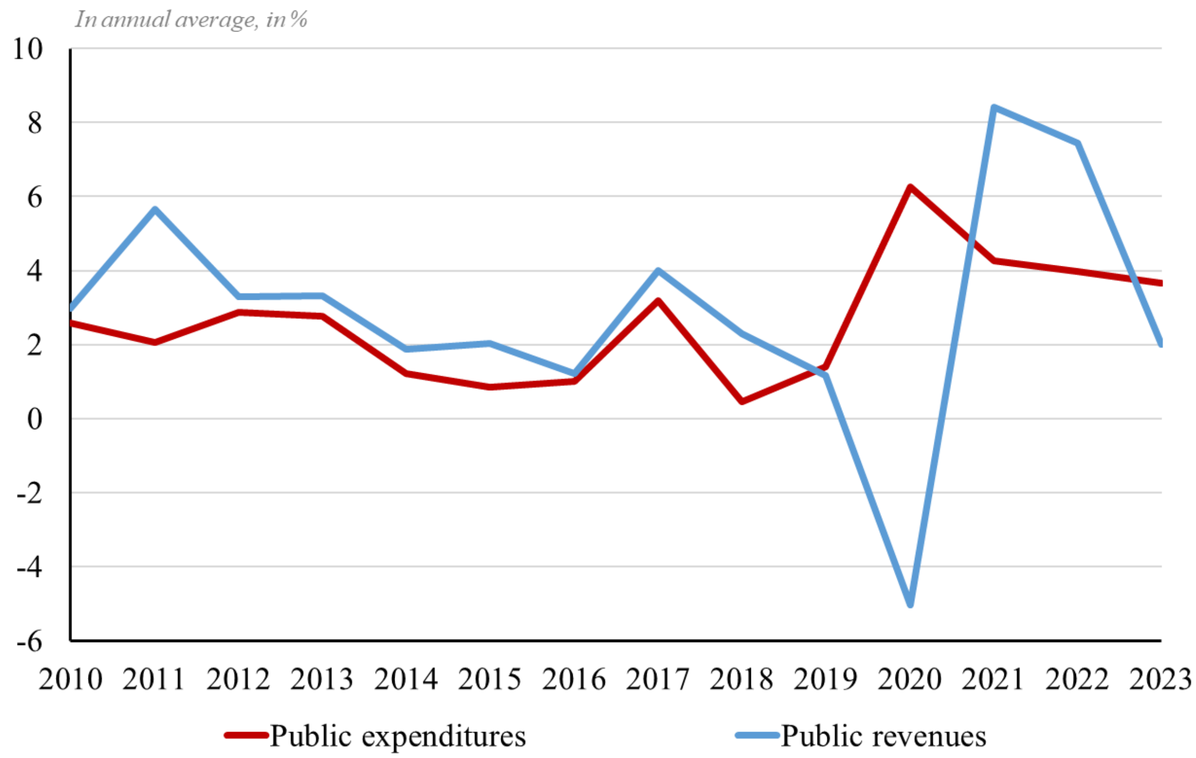
11. Consequently, in accordance with the provisions of Article 5(II) of Law no. 2023-1195 of 18 December 2023 on public finance programming for the years 2023 to 2027, the High Council hereby assesses that the exceptional circumstances identified in 2020 ceased in 2023 and should not be considered in the examination of this bill.

III- Remarks on the evolution of the nominal and structural public deficits in 2022 and on the deviations from the programming law

1- Change in effective public and structural deficits between 2021 and 2022

12. According to INSEE, the public deficit reached 154.0 billion euros in 2023 (5.5 points of GDP), up sharply on 2022 (€125.8bn, or 4.8 points of GDP). The increase in expenditures (+€56.7bn) markedly exceeds that in revenue (+€28.5bn). Despite a marked increase in GDP (+6.2% in value terms, after +5.5% in 2022), revenues have grown much more slowly in value terms than in 2022 (+2.0%, after +7.4%) and have even contracted in volume terms (-1.1% excluding tax credits). In current euros, revenue growth is lower than expenditure growth (+3.7% after +4.0%).

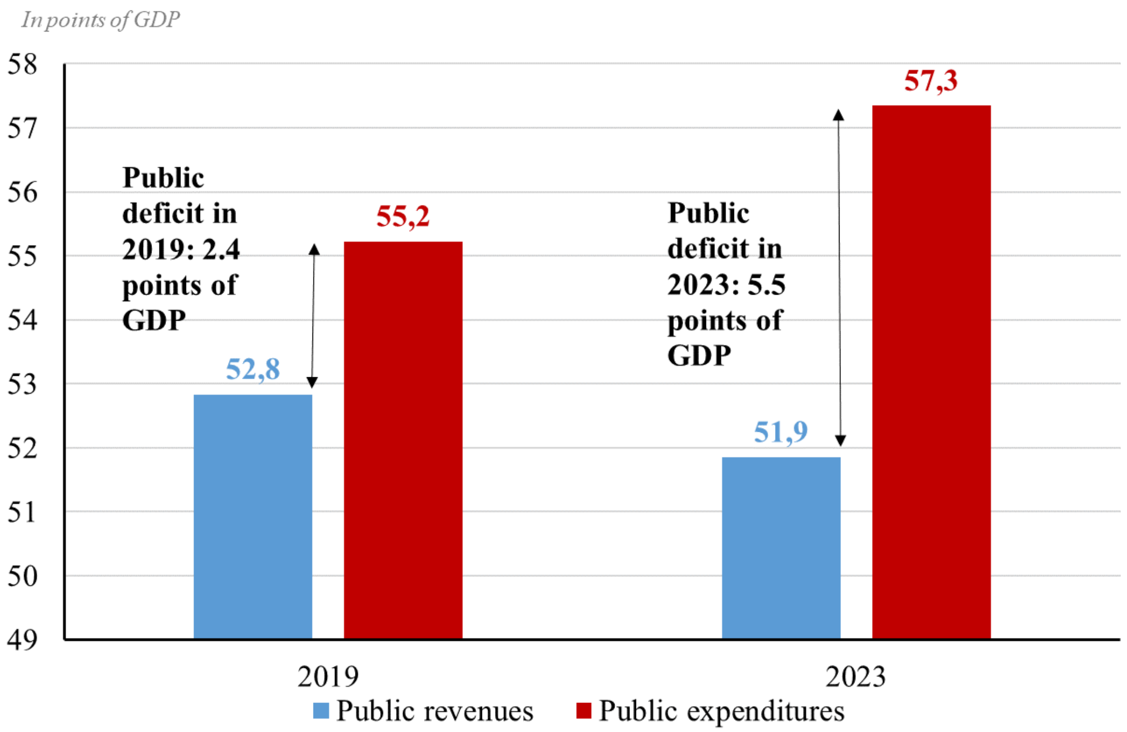
Figure 1: growth rate of public revenues and expenditures (in value)



Source: INSEE

13. The public deficit remains well above its level prior to the health crisis, both in terms of value (€154.0bn in 2023 compared with €58.2bn in 2019) and GDP points (5.5 points compared with 2.4 points). The ratio of public spending to GDP (57.3 points) is lower than in 2022 (58.8 points), mainly due to the end of the emergency and stimulus measures adopted in the context of Covid-19 and the fall in the interest burden on inflation-linked bonds as a result of the decline in inflation[1]. However, it is 2.1 points higher than in 2019, while the ratio of public revenue to GDP (51.9 points in 2023) is 1.0 point lower than in 2019. At 43.5 points of GDP, compulsory levies ratio is 0.3 points lower than in 2019. The fall is slightly greater (-1.1 points) compared to the plateau reached between 2012 and 2018, when the compulsory levies ratio averaged 44.6 points of GDP.

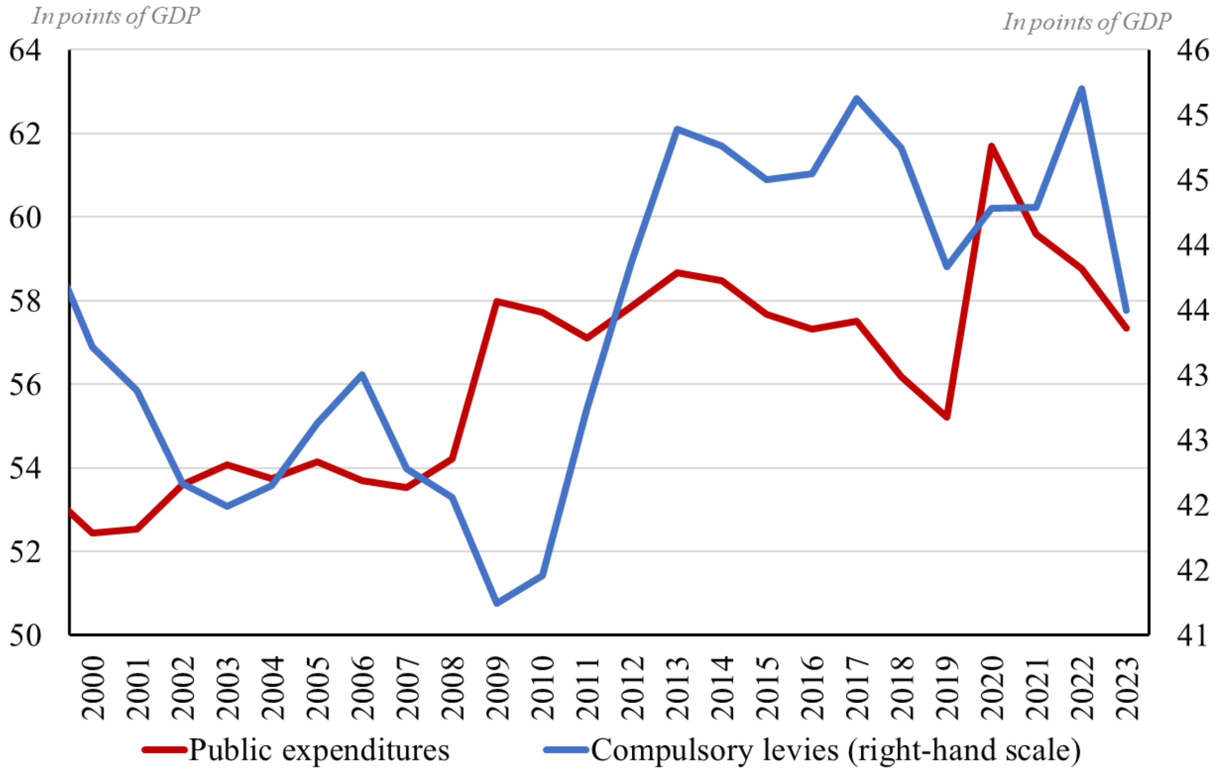
Figure 2: public revenues, expenditures and deficit in 2019 and 2023 (% of GDP)



Source: INSEE

[1] In national accounts, the interest expense on index-linked bonds includes interest due for the year, but also a provision for indexation of the capital due at maturity of the securities.

Figure 3: public spending and compulsory levies (in percentage points of GDP)



Source: INSEE

Box – Revision of public finance ratios due the switching to the 2020 base of national accounts

As part of the switching from the "2014 base" to the "2020 base"[2], INSEE has revised general government expenditure and revenue, as well as public debt in the Maastricht sense. The revisions made to the national accounts series in base 2020 are mainly the result of a change in the scope of the general government sector as defined in the national accounts, as well as the application of a new version of the European manual on public debt and deficit published in 2023.

The two most significant factors in the revision of the balance in 2019 and 2020, the years in which the general government account is "rebased", are the bringing forward by one year of expenditure on the tax credit for employment and competitiveness, and the reclassification of the Additional pension scheme for civil servants (ERAFP) outside general government.

In 2022, revisions to the change of base associated with the ERAFP and the recording on an accrual basis of replenishments of the concessional windows of the multilateral development banks worsen the general government balance by €3.4bn[3].

[2] Periodic changes of base are made by national accountants to take account of developments in national accounts sources and methods, as well as in the concepts and nomenclatures used to present the results. In accordance with Eurostat's recommendations, most European Union countries will change base in 2024. For more details, consult the INSEE website.

[3] However, the effect of the change of base is not limited to these two main factors.

In 2023, the impact on the public balance is mainly due to the removal of the ERAFP, which has a surplus, from the scope of general government. This reclassification leads to a €2.6bn deterioration in the public balance in 2023. The total effect of the rebasing on the public balance is estimated by INSEE at around -€4bn.

The GDP series used to calculate public finance ratios as a percentage of GDP continues to be evaluated using the concepts of the 2014 base.

14. The cyclical deficit amounts to 0.8 points of GDP in 2023, 0.3 points higher than in 2022. The sharp slowdown in activity has caused GDP growth (+0.9% in volume terms, after 2.5% in 2022) to fall below the potential growth rate as estimated by the Government (+1.35% in volume terms, after +1.25% in 2022) and the output gap to widen from -0.9% of potential GDP in 2022 to -1.4% of potential GDP in 2023.

15. The balance of one-off and temporary measures retained by the Government stands at -0.1 percentage points of potential GDP, as in 2022 (see Table 1). These include the impact of the losses on guaranteed loans to companies (PGE) (-1.8 billion euros) and elements not related to the health crisis (tax disputes).

Table 1: One-off measures in €bn

	2022	**2023**
Revenue measures	**0.5**	**0.7**
Health crisis - Premiums on State-guaranteed loans	0.5	0.7
Spending measures	**2.6**	**2.9**
Litigation interest	0.2	0.1
Serial tax litigations	0.9	1.0
EIB default rate	0.0	0.0
Default rate of state-guaranteed loans	1.5	1.8
Balance effect	**-2.1**	**-2.2**
Effect on potential GDP in percentage points	**-0.1**	**-0.1**

Source: Government

16. The structural balance is derived from the actual balance by neutralizing the effects of the economic cycle as well as one-off and temporary measures.

Box - Calculation Method of the Structural Balance[4]

The methodology used for calculating the structural balance has been simplified in the Public Finance Programming Law (LPFP) for the years 2023 to 2027. It is now close to that used by the European Commission.

The cyclical component now results from applying a constant coefficient to the output gap over the entire period covered by the programming law. The value chosen from 2023 to 2027 is 0.57 and is based on:

i. Elasticities estimated by the OECD. Specifically, the cyclical portions of revenue and public expenditure are assessed as follows:
   - On the revenue side, only compulsory levies are assumed to be cyclical;
   - On the expenditure side, only those related to unemployment compensation are assumed to be dependent on the economic cycle.

ii. The average weight of taxes in total revenue over the period 2008-2017, the weight of unemployment expenses in total expenditure, and those of total revenue and total expenditure in GDP over the same period are considered.

This calculates the cyclical component of the deficit. This component is subtracted from the actual balance to obtain an estimate of the structural balance. A final adjustment is made to the structural balance to exclude certain events or measures that, due to their exceptional nature, do not have a lasting impact on the public balance.

17. The structural deficit thus stands at 4.6 percentage points of potential GDP in 2023, up by 0.5 points compared to 2022. The significantly lower elasticity of mandatory levy revenues (-1.6 percentage points of potential GDP) was partially offset by a positive structural effort (+1.5 percentage points of potential GDP): the expenditure effort (+1.7 percentage points), which corresponds to the reduction[5] of the ratio between expenditure in value and potential GDP in value, is counterbalanced by new measures of reductions in compulsory levies composed of the completion of the abolition of the residence tax on primary residences and the halving of the value-added contribution of companies (-0.2 percentage points). Once the extinction of emergency and stimulus measures adopted in the context of Covid-19, the reduction in support measures against the energy shock, and the decline in debt burden due to the decline in inflation are neutralized, the expenditure effort amounts to 0.5 percentage points of potential GDP.

[4] The steps for its estimation are detailed in Appendix 2.

[5] Its increase when it is negative.

Table 2: Decomposition of structural adjustment

In percentage points of potential GDP	**2022**	**2023**
Structural balance	-4.2	-4.6
Structural adjustment (change in structural balance)		-0.5
Structural effort		1.5
Including new measures in compulsory levies		*-0.2*
Including expenditure effort		*1.7*
Non-discretionary component		-2.0
Including revenues outside of compulsory levies		*-0.4*
Including the elasticity effect of mandatory levies		*-1.6*

Source: Government

Note: Since the numbers are rounded to the tenths, there may be slight discrepancies in the result of the operations (structural adjustment of 0.5 percentage points of GDP when the displayed difference between the structural balances of 2022 and 2023 is only 0.4 percentage points of GDP).

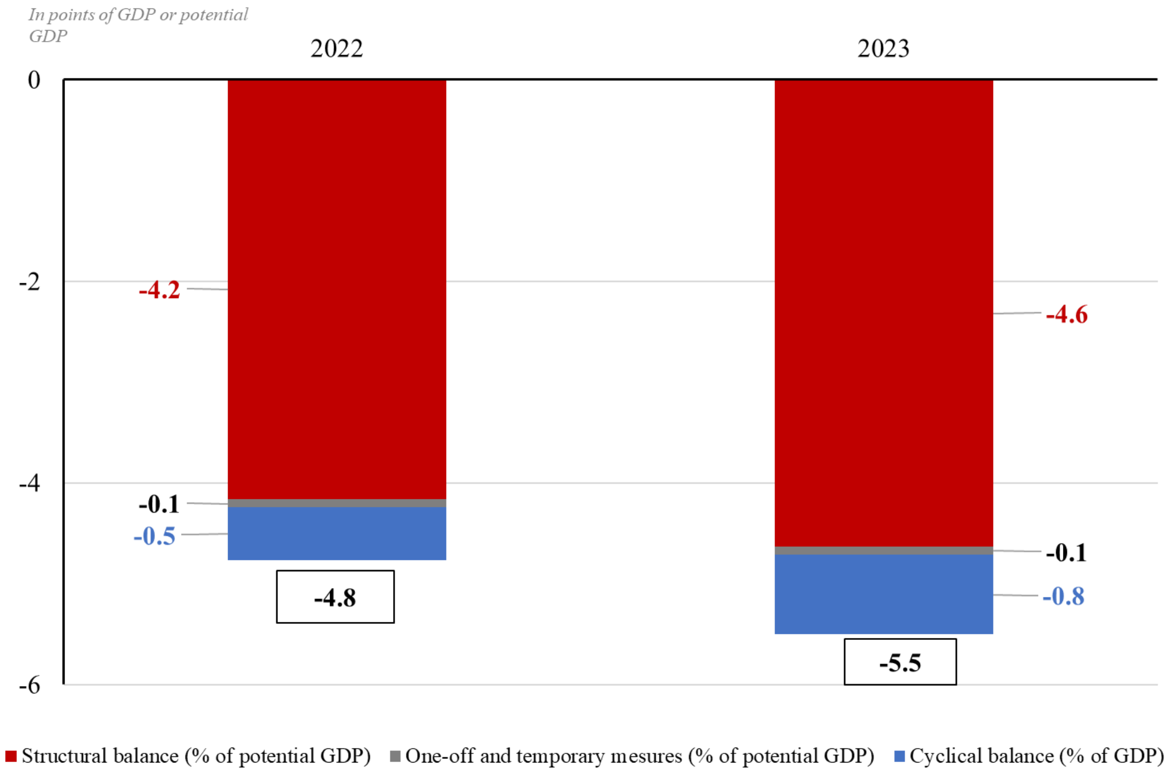
18. At 4.6 percentage points of potential GDP, the structural deficit is now very far from the medium-term objective (MTO) set by France in the 2023-2027 programming law, which aims for a structural deficit of less than 0.4 percentage points of potential GDP.

19. While the primary structural balance worsened in 2023, the future European budgetary rules resulting from the trilogue agreement between the Parliament, the Council, and the Commission in February 2024 foresee a primary structural adjustment of at least 0.25 percentage points of GDP per year for Member States, such as France, with a public debt ratio exceeding 60 percentage points of GDP.

20. **The general government deficit stands at €154.0 billion in 2023, equivalent to 5.5 percentage points of GDP. Its structural component is estimated at 4.6 percentage points of potential GDP as specified in the Public Finance Programming Law (LPFP) of December 18, 2023, to which the High Council of Public Finances must refer.**

21. **This deterioration is explained by the significant decline in compulsory levies as a proportion of GDP. Indeed, even though public expenditures are increasing in current euros, they are decreasing in volume, notably due to the expiration of part of the emergency and stimulus measures adopted in the context of Covid-19 and a decrease in interest charges on inflation-linked bonds due to the decline in inflation. However, this structural adjustment in expenditures is more than offset by the decrease in revenues as a share of GDP, which is primarily due to a shortfall in compulsory levies rather than to newly implemented measures.**

Figure 4: public balance decomposition



Source: Government

2- Observations on deviations from the Public Finance Programming Law

22. The public deficit recorded in 2023 (5.5 percentage points of GDP in terms of the 2020 base) is 0.6 percentage points higher than the one projected in the Programming Law of December 2023 (4.9 percentage points of GDP).

23.

Table 3: Deviation from the 2023-2027 Programming Law

(% of GDP or potential GDP)

	2022	**2023**		
		LPFP (Dec. 2023)	**PLRG 2023 (April 2024) in terms of the 2020 base**	***Gap***
Actual balance (1)	**-4.8**	**-4.9**	**-5.5**	***-0.6***
Cyclical component (2)	-0.5	-0.7	-0.8	*-0.1*
One-off and temporary measures* (3)	-0.1	-0.1	-0.1	*0.0*
Structural balance* (1)-(2)-(3) *	-4.2	-4.1	-4.6	*-0.5*

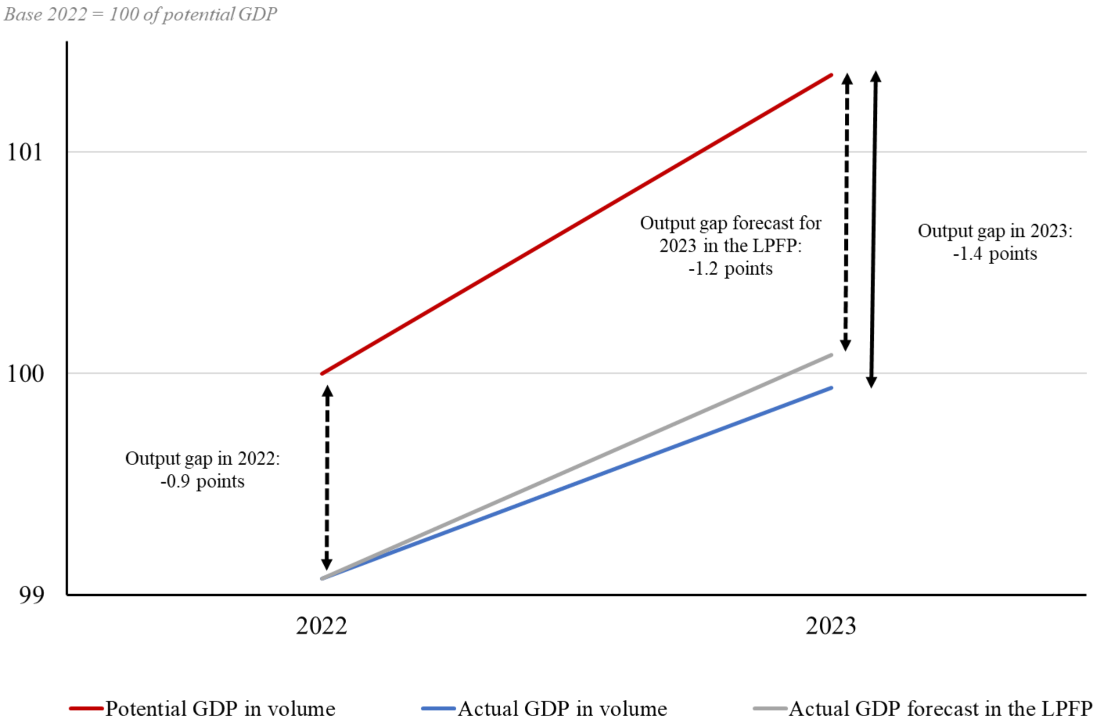
** In percentage of potential GDP*

Note: Since the figures are rounded to the tenths, there may be slight discrepancies in the result of the operations.

Sources: Law No. 2023-1195 on public finance programming of December 2023 and budget settlement bill for 2023.

24. According to the government's breakdown, this difference is explained to a small extent (0.1 percentage point) by its cyclical component because, due to a slightly weaker GDP growth in volume in 2023 (0.9%) compared to what was expected in the LPFP (1.0%), the output gap is slightly wider than anticipated. Real GDP remains 1.4% below the potential GDP set in the 2023-2027 LPFP, while it was projected to be 1.2 percentage points below potential GDP in 2023 according to the LPFP. As a result, the cyclical deficit is deteriorated by 0.1 percentage point compared to what was set in the LPFP[6].

Figure 5: the trajectory of potential GDP (basis 100 in 2022) as set out in the LPFP and the observed GDP (on an annual average and in volume).



Sources: INSEE, LPFP 2023-2027 of December 2023

25. The largest part of the difference (0.5 percentage point) is attributable to the structural balance, estimated at 4.6 percentage points of potential GDP based on 2020, compared to a forecast of -4.1 percentage points of potential GDP in the LPFP.

26. The opinion rendered by the High Council in accordance with Article 62(I) of the amended Organic Law No. 2001-692 of 1st August 2001 must also cover the compliance with the spending objectives of general government mentioned in Article 1A of the Organic Law of 1st August 2021, in relation to the execution of the past year. The methodological changes associated with the switching to the 2020 base of the national accounts have significantly affected the level of public expenditures and do not allow for a comparison between the trajectory set in the LPFP and that of the past year without accounting adjustments. Growth

[6] The cyclical component results from applying a coefficient of 0.57 to the output gap (see box presenting the calculation method of the structural balance). Therefore, a widened output gap of 0.2 percentage points leads to a deterioration of the structural balance of about 0.1 percentage point.

rates in public expenditures in value and volume are more comparable, although they not fully (see Table 4).

27. Public spending excluding tax credits, based on 2014, was expected to increase by 3.4% in value in 2023 according to the LPFP. In the results established by INSEE, it is at 3.6%. In volume, adjusted for the Consumer Price Index excluding tobacco as in the LPFP, it decreased by 1.2% compared to an expected decline of 1.3% in the LPFP. Overall, these differences, which may be slightly affected by the rebasing, are not significant.

Table 4: Forecasted and actual growth of public spending in value and volume in %

	LPFP	**PLRG**
The evolution of public spending excluding tax credits in value	3.4	3.6
The evolution of public spending excluding tax credits in volume (adjusted for CPI excluding tobacco)	-1.3	-1.2

Sources: INSEE, Law No. 2023-1195 on Public Finance Programming of December 2023, budget settlement bill for 2023.

3- Assessments regarding the gap between the structural balance and that of the public finance programming law

28. In accordance with Article 62(I) of the amended Organic Law No. 2001-692 of 1st August 2001 relating to Budget Laws, the High Council pronounces on the consistency of the observed structural balance trajectory with that of the current programming law, specifically that of December 18, 2023, for the years 2023 to 2027.

29. The assessment of the structural deficit presented by the Government for 2023 is 0.5 percentage points of potential GDP higher than the forecast included in the Public Finance Programming Law of December 18, 2023.

30. As mentioned above, however, the objectives of the LPFP were defined based on the 2014 national accounts, while the levels of public deficit and debt were established by INSEE using the concepts of the 2020 base. This rebasing, which is methodological in nature, affects the calculation of the difference between the structural balance presented in the LPFP and that included in this draft law, notably due to changes in the scope of public administrations. The High Council takes these methodological changes into account in its assessment.

31. Adjusted for the rebasing, the difference between the observed structural balance in 2023 and that forecasted in the LPFP is less than 0.5 percentage points of potential GDP. Therefore, this difference cannot be considered significant within the meaning of Article 62(II) of the Organic Law of 1st August 2021, and there is no need to trigger the correction mechanism provided for in Article 62(III) for the year 2023.

32. **The High Council notes that the structural balance of general government deteriorated by 0.5 percentage points compared to the forecast in the LPFP (-4.1 percentage points of potential GDP). However, part of this difference results from a methodological change related to the switching of national accounts to the 2020 base between 2022 and 2023. Adjusted for the rebasing, the gap between the observed structural balance in 2023 and that forecasted in the LPFP is less than 0.5 percentage points of potential GDP. Therefore, it is not considered 'significant' within the meaning**

of Article 62(II) mentioned above. Under these circumstances, there is no need to trigger the correction mechanism for the year 2023.

33. **In a context of rising debt burden, the high level of the structural deficit delays the necessary reduction of the debt-to-GDP ratio and could impair France's ability to cope with potential shocks or to undertake new expenditures, particularly in favour of ecological transition. Reducing the deficit requires prioritized action on public spending, which remains over two percentage points higher relative to GDP than its pre-health crisis level, and a reassessment of planned tax cuts.**

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This opinion will be published in the *Official Journal of the French Republic* and sent to Parliament.

Paris, 15 April 2024.

For the High Council of Public Finance
The First President of the Cour des Comptes,
President of the High Council of Public Finance

Pierre MOSCOVICI

APPENDIX 1

Introductory article of the draft budget settlement bill for 2023
Structural balance and effective balance for all general government for 2023

The structural balance and the actual balance of general government resulting from implementation, general government expenditure resulting from implementation expressed in billions of current euros, changes in general government expenditure resulting from implementation over the year expressed in volume, compulsory levies, general government expenditure and debt resulting from implementation and the main general government expenditure for 2023 considered as investment expenditure within the meaning of the last paragraph of Article 1 A and Second of Article 1 E of the Organic Law No. 2001-692 of 1 August 2001 on Budget Acts, as well as these same aggregates entered in the Initial Budget Act for 2023 and for the year 2023 in the Public Finance Programming Bill for the years 2023 to 2027 are as follows:

In % of GDP unless otherwise stated	2023 result	Budget law 2023		Public finance programming law 2023-2027 for 2023	
Total general governement		Forecast	Gap	Forecast	Gap
Structural balance (1) (in points of potential GDP)	-4.6	-4.0	-0.6	-4.1	-0.49
Cyclical balance (2)	-0.8	-0.8	0.0	-0.7	-0.10
Balance of one-off and other temporary measures (3) (in points of potential GDP)	-0.1	-0.2	0.1	-0.1	0.02
Actual balance (1+2+3)	-5.5	-5.0	-0.5	-4.9	-0.57
Maastricht debt	110.6	111.2	-0.5	109.7	1.0
Rate of compulsory levies (included EU, net of tax credits)	43.5	44.9	-1.5	44.0	-0.6
Public expenditure (excluding tax credits)	56.7	56.9	-0.2	55.9	0.8
Public expenditure (excluding tax credits, €bn)	1 589	1 572	17	1 575	14
Change in public spending excluding tax credits in volume (%) [1]	-1.1	-1.1	0.0	-1.3	0.2
Main capital expenditure (€bn) [2]	25	25	0.0	25	0.0
1 At constant field. 2 Within the meaning of the Public finance programming law for 2023-2027.					

Explanatory statement:

This article implements the provision set out in Article 1 of Organic Law No. 2001-692 of 1 August 2001 on Budget Laws, by comparing the difference between the actual and structural balances resulting from implementation for 2023 based on national accounting conventions between, on the one hand, those provided for in Finance Law 2022-1726 of 30 December 2022 for 2023 and, on the other hand, the balances for 2023 defined in Public Finance Programming Law 2023-1195 of 18 December 2023 for the years 2023 to 2027.

On 26 March 2023, INSEE published the first results of the national accounts for general government. The public deficit is estimated at 5.5% of GDP in 2023, compared with 4.8% in 2022 and 4.9% forecast in the 2023 Budget Bill (LFG) and the 2023-2027 Public Finance Programming Law (LPFP).

The structural breakdown of the 2023 public balance presented in the introductory article and below is based on the potential growth assumptions of the 2023-2027 LPFP. For the purposes of the law relating to the results of management and approving the accounts for the year (PLRG 2023), the potential growth of the programme remains the reference, as stipulated in article 62 of the organic law relating to finance laws.

Compared with 2022, the increase in the deficit in 2023 (+0.7 points of GDP) is explained for +0.3 points of GDP by the deterioration in the cyclical balance. Although real GDP growth has held up well in 2023 (+0.9%), it increases at a lower rate than potential growth (+1.35%).

The increase in the deficit compared with 2022 is also explained by a fall of almost -0.5 points of potential GDP in the structural balance, which amounts to -4.6% in 2023. This deterioration in the structural balance is the result of weak revenue growth, mainly due to:

- the spontaneous growth in compulsory levies, which is significantly lower than the growth in GDP in value terms, which has contributed to a deterioration in the structural adjustment of -1.6 points of potential GDP;

- new measures on compulsory levies (completion of the abolition of the residence tax on main residences and abolition of half of the contribution to added value of companies) which weighed down the structural adjustment by -0.2 points of potential GDP.

These impacts were largely offset by the gradual phasing out of the emergency and support measures put in place during the health crisis (+0.6 points), as well as by the lower cost of measures to combat rising energy prices (+0.3 points) and by the decline in the cost of debt linked to inflation-indexed securities (+0.3 points).

Compared with the multi-year guidelines of the 2023-2027 LPFP, which also correspond to the forecasts underlying the 2024 PLF, the structural balance recorded in the introductory article of the 2023 PLRG is -0.49 points of potential GDP lower than that shown for 2023 in the 2023-2027 LPFP.

This difference is explained to the tune of -€4bn by the change in methodology associated with the switching of the national accounts to the 2020 base. This impact on the public balance is mainly due to the removal of the Additional pension scheme for civil servants (ERAFP), which has a structural surplus, from the scope of general government. This reclassification alone has led to a deterioration in the public deficit of around €2.6bn in 2023.

The changeover to the 2020 base for the national accounts also leads to methodological changes that significantly affect public finance ratios without impacting the balance, in particular with a much higher level of public spending and revenues excluding compulsory levies. There are two main reasons for this increase: (i) the inclusion of SNCF Réseau's full account (for which only the balance was previously recorded), resulting in an increase of around €10 billion in revenues excluding compulsory levies and in expenditure, and (ii) a new treatment of adjustments relating to research and development, resulting in an increase of around €4 billion in revenues excluding compulsory levies and in expenditure. Thus, with regard to spending in particular, it is the effects of the rebasing that largely explain the significant differences in the amount in billions of euros and in the share of GDP of public spending between the results of the 2023 implementation and the objectives of the 2023-2027 LPFP. Expenditure growth between 2022 and 2023 is slightly more dynamic than expected; in particular, it is affected by a drop of €3bn in expenditure estimated in national accounts for 2022, linked to measures to fight rising energy prices. Excluding these effects, spending in 2023 is broadly in line with the objectives of the 2023-2027 PSSA, as shown by the decline in real public spending (-1.1%).

This rebasing, carried out independently by INSEE under the supervision of Eurostat, can be considered as an unusual event beyond the control of the Government and having a significant effect on public finances without any effect on the sustainability of France's public finances, which could not have been anticipated at the time the 2023-2027 LPFP was adopted. Thus, it is more appropriate to compare the structural balance resulting from the 2023 implementation with that of the LPFP by correcting for the effects of the change in the basis of the national accounts, in order to compare the results in the same national accounting frame of reference. As a result, **the difference in the structural balance to be considered in relation to the objectives of the LPFP is -0.35 points of potential GDP**.

The difference between the balance recorded in the 2023 PLRG and that recorded in the 2023-2027 LPFP totals -€15 bn. Excluding the estimated effect of the change in the national accounts base, it therefore amounts to -€11bn.

This difference of -€11 bn is mainly due to a reduction in tax revenues (approximately -€21 bn). In addition, spending by local authorities was more dynamic than anticipated in the LPFP (-€4bn effect on the public balance). Conversely, spending on the State budget was lower than expected (approximately +€6bn impact on the public balance) and on the other central government bodies (+€2bn impact on the public balance). In addition, revenues excluding compulsory levies were higher than forecast (around +€5bn for general government as a whole, not including the effects of the base change).

APPENDIX 2

The calculation of the structural balance

To assess the trajectory of public finances, it is usual to consider the structural balance, which corresponds to the **general government balance corrected for the direct effects of the economic cycle and exceptional events**. The general government balance is thus separated into two:

- a **cyclical component** representing the impact of the economic cycle on general government expenditure and revenue;
- a **structural component** corresponding to what the general government balance would be if the economy were at its potential level.

The identification of the cyclical and structural components of the public deficit is fundamentally based on the estimation of potential GDP. Potential GDP represents the level of output that the economy can sustain over the long term without putting pressure on the factors of production, capital and labour.

The methodology for calculating the structural balance has been simplified in the Public Finance Programming Bill (PLPFP) for the years 2023 to 2027. It is now close to the one used by the European Commission.

The cyclical component is now the product of the output gap and an apparent semi-elasticity to the output gap, set at an average value over the entire period covered by the programming law[7]. The value used for the period 2023-2027 is 0.57 and is based on:

- the elasticities estimated by the OECD. In concrete terms, the cyclical shares of public revenue and expenditure are evaluated as follows:
    - **On the revenue side,** only compulsory levies are assumed to be cyclical;
    - **On the expenditure side,** only unemployment compensation expenditure is considered to be cyclical[8].

- the average weight of taxes in total revenue over 2008-2017, the average weight of unemployment expenditure in total expenditure, and the average weight of total revenue and total expenditure in GDP over the same period.

The cyclical component of the deficit is thus calculated. **This component is deducted from the actual balance to obtain an estimate of the structural balance**.

A final adjustment is made to the structural balance in order to exclude certain events or measures which, because of their exceptional nature, do not have a permanent impact on the general government balance. This adjustment was originally introduced to neutralise the effect of the sale of UMTS licences at the end of the 1990s and the various payments received by the State (IEG, La Poste, France Telecom) which contributed to an exceptional increase in revenue.

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[7]The method used for the 2018-2022 programming law required a new calculation of the apparent semi-elasticity of the cyclical balance to the output gap each year.

[8] As regards other expenditure, either it is discretionary or no clear and reliable link with the business cycle can be demonstrated.

However, there is no precise definition of exceptional measures and their identification is partly a matter of interpretation. While stressing that the one-off and temporary nature of the measures must be assessed on a case-by-case basis, the Government is proposing a set of criteria to help understand the concept in an annex to the programming law.

The composition of the structural adjustment

The change in the structural balance from one year to the next is called the “structural adjustment”.

To analyse the fiscal policy stance, **the change in the structural balance can be broken down** as follows:

- **Structural effort, which measures the share of the structural adjustment attributable to "discretionary" factors. *i.e.* factors that can be controlled by policymakers:**

    - **the expenditure effort,** which compares the growth rate of public expenditure in volume (deflated with the price of GDP) with the potential growth of the economy. It contributes to a positive structural adjustment when spending increases less rapidly than the potential GDP;
    - the quantum of **new measures in compulsory levies.**

- **The "non-discretionary" part** of the structural adjustment, which takes account of **changes in revenues excluding compulsory levies.**