Council of the European Union

Brussels, 15 June 2018
(OR. en)

9436/18

ECOFIN 519
UEM 197
SOC 333
EMPL 267
COMPET 390
ENV 373
EDUC 222
RECH 245
ENER 196
JAI 534

NOTE

From:	General Secretariat of the Council
To:	Permanent Representatives Committee/Council
No. Cion doc.:	9198/18 - COM(2018) 409 final
Subject:	Recommendation for a COUNCIL RECOMMENDATION on the 2018 National Reform Programme of France and delivering a Council opinion on the 2018 Stability Programme of France

Delegations will find attached the above mentioned draft Council Recommendation, as revised and agreed by various Council committees, based on the Commission Proposal COM(2018) 409 final.

COUNCIL RECOMMENDATION

of …

on the 2018 National Reform Programme of France

and delivering a Council opinion on the 2018 Stability Programme of France

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Articles 121(2) and 148(4) thereof,

Having regard to Council Regulation (EC) No 1466/97 of 7 July 1997 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies[1], and in particular Article 5(2) thereof,

Having regard to Regulation (EU) No 1176/2011 of the European Parliament and of the Council of 16 November 2011 on the prevention and correction of macroeconomic imbalances[2], and in particular Article 6(1) thereof,

Having regard to the recommendation of the European Commission,

Having regard to the resolutions of the European Parliament,

Having regard to the conclusions of the European Council,

Having regard to the opinion of the Employment Committee,

Having regard to the opinion of the Economic and Financial Committee,

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[1] OJ L 209, 2.8.1997, p. 1.
[2] OJ L 306, 23.11.2011, p. 25.

Having regard to the opinion of the Social Protection Committee,

Having regard to the opinion of the Economic Policy Committee,

Whereas:

(1) On 22 November 2017, the Commission adopted the Annual Growth Survey, marking the start of the 2018 European Semester for economic policy coordination. It took due account of the European Pillar of Social Rights, proclaimed by the European Parliament, the Council and the Commission on 17 November 2017. The priorities of the Annual Growth Survey were endorsed by the European Council on 22 March 2018. On 22 November 2017, on the basis of Regulation (EU) No 1176/2011, the Commission also adopted the Alert Mechanism Report, in which it identified France as one of the Member States for which an in-depth review would be carried out. On the same date, the Commission also adopted a recommendation for a Council recommendation on the economic policy of the euro area, which was endorsed by the European Council on 22 March 2018. On 14 May 2018, the Council adopted the Recommendation on the economic policy of the euro area[3] ('Recommendation for the euro area').

(2) As a Member State whose currency is the euro and in view of the close interlinkages between the economies in the economic and monetary union, France should ensure the full and timely implementation of the Recommendation for the euro area, as reflected in the recommendations below, in particular recommendations (1) and (2).

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[3] OJ C 179, 25.5 2018, p. 1.

(3) The 2018 country report for France was published on 7 March 2018. It assessed France's progress in addressing the country-specific recommendations adopted by the Council on 11 July 2017[4], the follow-up given to the country-specific recommendations adopted in previous years and France's progress towards its national Europe 2020 targets. It also included an in-depth review under Article 5 of Regulation (EU) No 1176/2011, the results of which were also published on 7 March 2018. The Commission's analysis led it to conclude that France is experiencing macroeconomic imbalances. In particular, vulnerabilities stem from high public debt and weak competitiveness dynamics in a context of low productivity growth. The risk of an adverse effect on the French economy and, given its size, of negative spillovers to the economic and monetary union, is particularly important.

(4) On 25 April 2018, France submitted its 2018 National Reform Programme and its 2018 Stability programme. In order to take account of their interlinkages, the two programmes have been assessed at the same time.

(5) Relevant country-specific recommendations have been addressed in the programming of the European Structural and Investment Funds ('ESI Funds') for the 2014-2020 period. As provided for in Article 23 of Regulation (EU) No 1303/2013 of the European Parliament and of the Council[5], where it is necessary to support the implementation of relevant Council recommendations, the Commission may request a Member State to review and propose amendments to its Partnership Agreement and relevant programmes. The Commission has provided further details on how it would make use of that provision in guidelines on the application of the measures linking the effectiveness of the ESI Funds to sound economic governance.

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[4] OJ C 261, 9.8.2017, p. 1.

[5] Regulation (EU) No 1303/2013 of the European Parliament and of the Council of 17 December 2013 laying down common provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund, the European Agricultural Fund for Rural Development and the European Maritime and Fisheries Fund and laying down general provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund and the European Maritime and Fisheries Fund and repealing Council Regulation (EC) No 1083/2006 (OJ L 347, 20.12.2013, p. 320).

(6) Following the timely and durable correction of the excessive deficit and Council Decision (EU) 2018 /…[6*] to abrogate the excessive deficit procedure, France is in the preventive arm of the Stability and Growth Pact and subject to the transitional debt rule. In its 2018 Stability Programme, the Government plans a gradual improvement of the general government balance from -2,6 % of GDP in 2017 to +0,3 % of GDP in 2022. The medium-term budgetary objective — a structural deficit of 0,4 % of GDP — is not planned to be achieved over the period covered by the 2018 Stability Programme. According to the 2018 Stability Programme, the general government debt-to-GDP ratio is expected to decrease from 97,0 % in 2017 to 89,2 % in 2022. The macroeconomic scenario underpinning those budgetary projections is plausible. At the same time, the measures needed to support the planned deficit targets from 2019 onwards have not been sufficiently specified.

(7) On 11 July 2017, the Council recommended France to ensure that the nominal growth rate of net primary[7] government expenditure does not exceed 1,2 % in 2018, corresponding to an annual structural adjustment of 0,6 % of GDP. At the same time, it was stated that the assessment of the 2018 Draft Budgetary Plan and subsequent assessment of 2018 budget outcomes will need to take due account of the goal of achieving a fiscal stance that contributes to both strengthening the ongoing recovery and ensuring the sustainability of public finances. Following the Commission's assessment of the strength of the recovery in France while giving due consideration to its sustainability challenges, carried out in the context of its opinion on France's 2018 Draft Budgetary Plan, no additional elements in that regard need to be taken into account. Based on the Commission 2018 spring forecast, there is a risk of a significant deviation from the recommended adjustment path towards the medium-term budgetary objective in 2018.

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6 Council Decision (EU) 2018/… of … abrogating Decision 2009/414/EC on the existence of an excessive deficit in France (OJ …).

* OJ: please insert the number of the Decision contained in document ST 9758/18 in the text and complete the corresponding footnote.

7 Net primary government expenditure comprises total government expenditure excluding interest expenditure, expenditure on Union programmes fully matched by Union funds revenue and non-discretionary changes in unemployment benefit expenditure. Nationally financed gross fixed capital formation is smoothed over a four-year period. Discretionary revenue measures or revenue increases mandated by law are factored in. One-off measures on both the revenue and expenditure sides are netted out.

(8) In 2019, in view of France's general government debt ratio above 60 % of GDP and projected output gap of 0,6 %, the nominal growth rate of net primary government expenditure should not exceed 1,4 %, in line with the structural adjustment of 0,6 % of GDP stemming from the commonly agreed adjustment matrix of requirements under the Stability and Growth Pact. According to the Commission 2018 spring forecast under unchanged policies, there is a risk of a significant deviation from that requirement in 2019, and over 2018 and 2019 taken together. France is prima facie not forecast to comply with the transitional debt rule in 2018 and 2019. Overall, the Council is of the opinion that the necessary measures should be taken as of 2018 to comply with the provisions of the Stability and Growth Pact. The use of any windfall gains to further reduce the general government debt ratio would be prudent.

(9) The level of public expenditure in France is the highest in the Union. The expenditure ratio is projected to reach 56,0 % of GDP in 2018, 10,6 percentage points higher than the Union average. While the consolidation strategy in recent years has mainly benefited from declining interest rates and cuts in public investment, the low interest rate environment is unlikely to prevail in the medium term and the cut in productive investment could harm future economic potential. The spending reviews since 2014 did not render significant savings and efficiency gains were limited due to a lack of appropriate follow-up and a low level of political ownership. The most recent spending review strategy has been abandoned and will be replaced by Public Action 2022 (*Action Publique 2022*), the principles of which are set out in the mandate given by the Government in October 2017. The Public Action 2022 Committee (*Comité Action Publique 2022*) is due to produce a report before Summer 2018 and to analyse what measures need to be taken. However, clearly specified measures have not been proposed yet and new savings within this framework will only be delivered from 2020 onwards. Efforts to address the current fiscal consolidation needs over the short-to-medium term would benefit from the swift implementation of expenditure-saving measures.

(10) At present, 37 different pension schemes co-exist in France. These concern different groups of workers and function according to different sets of rules. Progressively unifying the rules would improve the transparency of the system, increase intergenerational fairness, and facilitate labour mobility. Harmonising the calculation rules would also contribute to better control public expenditure. While the pension reforms already adopted are expected to bring down the level of public pension expenditure ratio in the long run, a simpler and more efficient pension system would generate further savings and help mitigate public finance sustainability risks in the medium term. According to a recent study by *La Fondation pour la recherche sur les administrations et les politiques publiques* (*iFRAP*), the alignment of different pension schemes in the public and private sectors could bring more than EUR 5 billion of public expenditure savings by 2022.

(11) The unemployment rate declined from 10,4 % in 2015 to 9,4 % in 2017 and is forecast to decrease further in the coming years, while the employment rate rose to 70,6 % in 2017. However, labour market conditions for young people, low-skilled workers and people with a migrant background (both first and second generation) remain relatively more difficult. In 2017, only 55,6 % of non-EU-born people (aged 20-64) were in employment, which is 17,0 percentage points lower than the figure for those born in France. Inhabitants of most deprived areas (*Quartiers de la politique de la ville*), including people with a migrant background, continue to face difficulties on the labour market. Notwithstanding policy action, the impact of socioeconomic and migrant background on educational performance is comparatively high and hampers labour market integration. There is also evidence of discriminatory practices in the labour market. Effective active employment support, including language training, intensive job counselling and recruitment support, and firmer action on discriminatory practices, are key to fostering equal opportunities on the labour market.

(12) The 2016 law on labour, modernising social dialogue and securing professional pathways aims to improve firms' capacity to adjust to economic cycles and reduce the share of workers on temporary contracts. While more people are being recruited on open-ended contracts, labour market segmentation remains a challenge and the transition to more open-ended forms of employment should be fostered. In this context, it is important to finalise the implementation of the ongoing ambitious reform programme, which includes the recently adopted reform of the labour law, the planned overhaul of the unemployment benefit system, and the reform of the vocational education and training system, including apprenticeships.

(13) The gradual implementation of measures to reduce the labour tax wedge have improved France's cost competitiveness since 2013, but accumulated past losses have not yet been fully recovered. At the average wage, in 2016, France still had one of the highest employers' social contribution rates as a proportion of total labour costs in the Union. Existing policy measures to reduce labour costs are expected to be further consolidated and strengthened as of 2019, with the announced conversion of the tax credit for competitiveness and employment (CICE) into a generalised reduction of social contributions for employers and the introduction of further rebates for lower wages to foster employment of the low-qualified.

(14) Since 2013, the French minimum wage has followed its indexation rule, without any *ad hoc* hikes. As a result, it has grown more slowly than reference wages (1,23 % in 2017, compared to 1,31 % for average wage), in a context of weak inflation and subdued wage growth. While the minimum wage, as compared with the average wage, is high in international terms, the cost of labour at the minimum wage has been significantly curtailed by reductions of social contributions. Such reductions will be intensified and made permanent as of 2019. While the indexation of the minimum wage is important to preserve workers' purchasing power, the current mechanism (unique in the Union) might limit wage adjustments to changing conditions, with potential negative consequences for competitiveness. A group of independent experts assesses the minimum wage annually and provides non-binding opinions on its development. In 2017, the group recommended revising the indexation rule, for example by limiting it to inflation indexation only.

(15) The current initial vocational education and training system does not sufficiently support labour market integration in particular because a significant proportion of students is driven towards pathways with limited employment prospects. Moreover, French students in vocational education and training achieve much lower educational outcomes than the Union average, while those in general education perform much better. In this context, measures to foster apprenticeships, which are associated with better employment prospects, along with measures to improve school-based results, are essential to support youth employment and promote equality of opportunity. At the same time, improving access to continuous training for the low-qualified workers and jobseekers and promoting the achievement of higher qualifications, backed by appropriate training guidance, are also important. Reflecting these challenges and in particular the need to improve the governance of the system, ensure labour market relevance, quality and access to training and secure labour market transitions, the Government presented on 27 April 2018 a draft law reforming the apprenticeship and continuous vocational education and training system. Moreover, the 2018 National Reform Programme confirms the intention to implement a EUR 14 billion investment plan for skills and opens the way for a complementary reform of the school-based initial vocational education.

(16) Overall, the social protection system delivers good results. Income inequalities after transfers are below the Union average and, despite a recent increase, the number of people at risk of poverty and social exclusion remains relatively low. However, some groups, in particular single-parent families, people not born in the Union and people living in deprived urban areas face a higher risk of poverty. Access to adequate housing for people living in poverty remains a matter of concern. Despite recent improvements, social housing shortages remain in some areas.

(17) Despite ongoing reforms to reduce the tax burden on companies and support productive investment, the French tax system continues to be characterised by a high level of complexity, with tax expenditures, inefficient taxes and taxes on production forming barriers to a well-functioning business environment. The high number of tax expenditures (tax credit, exemptions, tax reductions) puts an additional burden on businesses, and SMEs in particular, in the form of increased compliance costs and uncertainty. It also creates additional control costs for the tax administration. Tax expenditures will increase further in number and in value under the 2018 Budget Law and are set to reach EUR 99.8 billion in 2018 (4,2 % of GDP) in 2018, as compared with EUR 93 billion in 2017. In addition, around 192 taxes yielding low revenue (less than EUR 150 million a year) have been identified, but only a very limited number have been eliminated since 2014[8]. Finally, France has very high taxes on production in the Union[9] (3,1 % of GDP in 2016) which consist mainly of capital and labour taxes for which companies are liable as a result of engaging in production and regardless of their economic performance.

[8] Inspection Générale des Finances (2014), *Les taxes à faible rendement.*

[9] Taxes on production are to be understood as "other taxes on production" according to EUROSTAT (D29 category).

(18) Market services accounted for more than 50 % of value added, 40 % of employment and 20 % of the manufacturing industry's value added in exports in 2016. However, while competition in market services has an impact across the whole economy, it is still hampered by regulatory requirements and administrative burden, which also impede firms' ability to grow. If sufficiently ambitious and fully implemented, reforms in the area of services could have a significant positive economic impact. In prioritising reform efforts, it is important to take into account the economic importance and performance of the services subsectors. An indicator-based approach used to identify priority reforms in the services sectors highlights a number of business services (architectural and engineering activities, legal and accounting activities, administrative and support services), retail trade, accommodation and food services, and health. In the specific area of professional services, the Growth, Activity and Equal Economic Opportunities Act (the 'Macron law') of 6 August 2015 eased restrictions in a limited number of professions, mostly legal professions. There remains scope for further reforms in professionnal services. Further reforms could target specific entry and exercise restrictions (e.g. reserves of activity, voting rights restrictions, shareholding restrictions, multidisciplinary restrictions and numerus clausus restrictions), which are considered excessive. Reforms to address key impediments to firms' growth could include removing threshold effects linked to size-related criteria in regulations and reducing the administrative burden on businesses. Finally, improving France's coverage with fast broadband would enhance its ability to benefit from the digital economy.

(19) According to the European Innovation Scoreboard, France's innovation performance remains below that of Union innovation leaders, despite the relatively high level of public support. In particular, improving the efficiency of public support schemes including the tax credit for research and development (*Crédit d'Impôt Recherche*) would stimulate better innovation output. In this respect, the results of ongoing evaluations need to be fed into improvements to the design of public support for innovation. Knowledge transfer between public research and businesses remains a challenge and this limits the commercial exploitation of research results. Compared with other Union countries, France's performance is low in public-private co-publications and public R&D financed by businesses. There is some potential to strengthen transfer mechanisms between academia and industry by simplifying partnership research and incentivising researchers' mobility.

(20) In the context of the 2018 European Semester, the Commission has carried out a comprehensive analysis of France's economic policy and published it in the 2018 country report. It has also assessed the 2018 Stability Programme, the 2018 National Reform Programme and the follow-up given to the recommendations addressed to France in previous years. The Commission has taken into account not only their relevance for sustainable fiscal and socioeconomic policy in France, but also the extent to which they comply with Union rules and guidance, given the need to strengthen the Union's overall economic governance by providing Union-level input into future national decisions.

(21) In the light of this assessment, the Council has examined the 2018 Stability Programme and its opinion[10] is reflected in particular in recommendation (1) below.

(22) In the light of the Commission's in-depth review and this assessment, the Council has examined the 2018 National Reform Programme and the 2018 Stability Programme. Its recommendations under Article 6 of Regulation (EU) No 1176/2011 are reflected in recommendations (1) to (3) below,

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[10] Under Article 5(2) of Regulation (EC) No 1466/97.

HEREBY RECOMMENDS that France take action in 2018 and 2019 to:

1. Ensure that the nominal growth rate of net primary government expenditure does not exceed 1,4 % in 2019, corresponding to an annual structural adjustment of 0,6 % of GDP. Use windfall gains to accelerate the reduction of the general government debt ratio. Implement expenditure savings in 2018 and fully specify the objectives and new measures needed in the context of Public Action 2022, for them to translate into concrete expenditure savings and efficiency gains measures in the 2019 budget. Progressively unify the rules of the different pension regimes to enhance their fairness and sustainability.

2. Pursue the reforms of the vocational education and training system to strengthen its labour market relevance and improve access to training, in particular for low-qualified workers and jobseekers. Foster equal opportunities and access to the labour market, including for people with a migrant background and people living in deprived areas. Ensure that minimum wage developments are consistent with job creation and competitiveness.

3. Simplify the tax system, by limiting the use of tax expenditures, removing inefficient taxes and reducing taxes on production levied on companies. Reduce the regulatory and administrative burden to increase competition in the services sector and to foster firms' growth. Step up efforts to increase the performance of the innovation system in particular by improving the efficiency of public support schemes and strengthening knowledge transfer between public research institutions and firms.

Done at Brussels,

For the Council

The President