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France's plans deserve to be implemented

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The new French government is planning to reduce the budget deficit from approx. 4½ % of GDP in 2013 to around 1½ % in 2017. The only cure: to curb spending. Consequently, government expenditure is scheduled to increase by around EUR 50 billion less than previously planned. This makes for an intelligent macro-economic policy.

Key points in the package:

- Freeze on central government salaries and wages and reductions in public services (EUR 15 billion).
- Reduction in future social benefits, principally by decoupling them from inflation, together with pension reforms (already passed), which include a longer working life (EUR 11 billion).
- Reform of local and regional administration (EUR 11 billion).
- Rationalisation in the health system (EUR 10 billion).

The achievement of comparative success will require annual growth and inflation rates of around 1½ % each. That is optimistic.

Measures chosen wisely

Virtually none of these measures constitutes a reduction in expenditure *as of today*. They limit growth in expenditure and liabilities *from tomorrow*. This protects current incomes and, in doing so, also protects future growth potential. The state's contribution to aggregate demand is being reduced gradually. Furthermore, continuing to adjust the minimum pension in line with inflation indicates an intention to look after those on low incomes as much as possible. Alongside these consolidation measures, there are also plans for initiating the reforms needed to strengthen competitiveness (in the labour market, for example) and to improve the regulatory framework.

The package is to be enacted over a period of three years. This is prudent. France has the confidence of the capital markets and does not have any major macroeconomic imbalances which might force it into taking action too hastily.

The French public sector is far too large. These measures will reduce it from approx. 57 % of GDP to a planned level of 53½ % – closer to the eurozone average and back to France's pre-crisis level, but still almost ten percentage points above the ratio of government expenditure to GDP in Germany (see figure). However, this will only work if the economy grows with sufficient speed at the same time. The French government's growth forecasts up to 2017 are admittedly too optimistic in this respect. Consequently, the actual result is likely to be less successful.

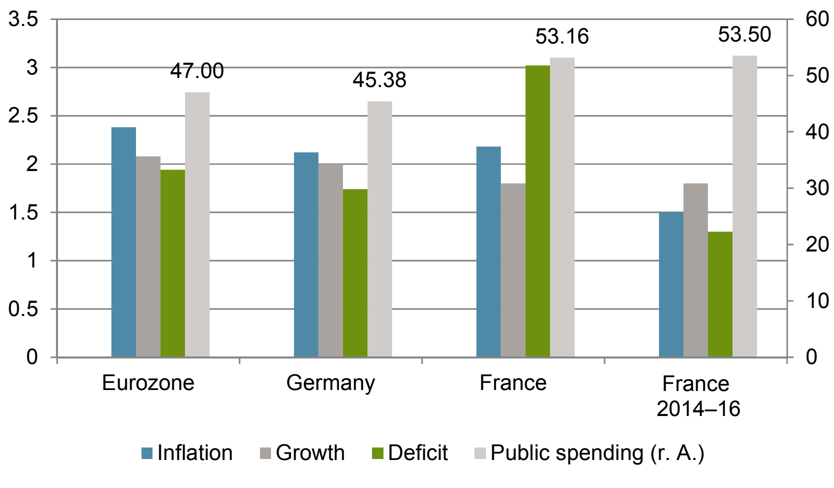
It is hoped that the package will be accepted by the French parliament. After that, the next barrier may well be resistance to regional reform from the territorial authorities. Rationalisation of the health sector could well prove difficult to monitor.

In French public debate, opinions differ on the acceptance of these reforms. The EU should therefore welcome these reform plans in the run-up to the European elections. Otherwise the plans could fall victim to a defeat for the Socialists in the elections.

Conclusion

France is heading in the right direction. In principle, the new government's consolidation package has been formulated wisely. However, it still has many hurdles to overcome; even then it is fair to assume that its actual effect will be smaller than the government is hoping. ■

Figure: Pre-crisis levels of major indicators and target figures for France
(Inflation and growth as percentages; deficit and govt. expenditure as a percentage of GDP; pre-crisis level = annual averages, 2004–2008)



Source: Eurostat