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July 2014

2014 ARTICLE IV CONSULTATION—STAFF REPORT; PRESS RELEASE; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR FRANCE

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2014 Article IV consultation with France, the following documents have been released and are included in this package:

- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on July 1, 2014, following discussions that ended on May 15, 2014, with the officials of France on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on June 17, 2014.
- An **Informational Annex** prepared by the IMF.
- A **Press Release** summarizing the views of the Executive Board as expressed during its July 1, 2014 consideration of the staff report that concluded the Article IV consultation with France.
- A **Statement by the Executive Director** for France.

The following document has been or will be separately released.

Selected Issues Paper

The publication policy for staff reports and other documents allows for the deletion of market-sensitive information.

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INTERNATIONAL MONETARY FUND

FRANCE

STAFF REPORT FOR THE 2014 ARTICLE IV CONSULTATION

June 17, 2014

KEY ISSUES

Context and Outlook. The economy has shown resilience through the crisis, but faces a slow recovery. Three years of significant fiscal adjustment have dampened activity. We project growth of 0.7 percent this year and 1.4 percent in 2015, driven by stronger external demand, improvements in profitability and investment, and a lesser fiscal drag. Inflation is projected to stay just above one percent. Apart from cyclical weakness and a structural fiscal imbalance, the economy faces employment and competitiveness gaps. Supply side measures and structural reforms are expected to improve economic performance over the medium term.

Risks. Volatile and uneven leading indicators point to the risk of a stalled recovery. Continued stagnation would, in turn, make it more difficult to meet fiscal objectives. Financial stability risks, and related outward spillovers, have abated considerably, as banks have rebuilt capital and liquidity buffers at a brisk pace, although exposure to wholesale funding remains high.

Policy Recommendations. Despite substantial adjustment, mostly on the tax side, the government deficit still stood at 4.2 percent of GDP in 2013, and debt rose to 92 percent in 2013. The April 2014 Stability Program lays out a path of fiscal adjustment, tax cuts and reform aimed at closing the structural fiscal deficit over the medium term while boosting the economy's growth potential. The targeted pace of adjustment is right—about ½ a percentage point a year. The simultaneous pursuit of tax cuts and deficit reduction rests on an ambitious program of expenditure reduction (2.2 percent of GDP). The emphasis should go to structural measures to ensure that spending growth is curbed permanently. Tax cuts and regulatory simplification are welcome measures to encourage investment. The impact of supply-side initiatives would be boosted by better functioning labor and product markets: reforms should aim to expand competition in services and to deepen labor market reforms with a view to creating more room for enterprise-level negotiations over working conditions. Indexation of the minimum wage should be reformed to limit the adverse impact on low skilled employment. Stronger liquidity and capital buffers in banks, and an improved European bank resolution framework, will better shield the economy and public finances from banking shocks. Banks still face adaptation to the evolving regulatory framework, and it will be important to ensure that the uneven taxation of financial instruments does not constrain the key intermediation role of banks.

Approved By
Jörg Decressin and Mark Flanagan

Discussions took place in Paris from April 29 to May 15, 2014. The staff team comprised Messrs. Gardner (head), Hallaert, Mses. Pérez Ruiz, and Kongsamut (all EUR). Mr. Decressin (EUR) joined for the last four days of the mission. The team was supported from headquarters by Ms. MacKinnon and Mr. Mason (both EUR). France Executive Director Mr. de Villeroché and Mr. Guyon (OED) participated in the Discussion. Staff met with Ministers Sapin (Finance), Montebourg (Economy), Eckert (Budget), Rebsamen (Labor), Bank of France Governor Noyer, other senior officials, and representatives of the financial and private sectors, parliament, employers and trade union federations. The mission held a press conference at the conclusion of the mission.

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CONTEXT

1. **The mission took place before the European Parliament elections, in which the far-right party registered large gains at the expense of the socialist and center right parties.** These electoral results came in the wake of a similar rebuke at the local elections in April, following which the President nominated a new government, headed by PM Valls. Discussions with the authorities centered on the policy program of the new government, as described in the Stability Program and National Reform Program. European Parliament elections have no immediate implications for policies: the government can count on a comfortable socialist majority in parliament until Presidential and Parliamentary elections in 2017; and, in reaction to the electoral results, both the President and the PM vowed to stay the course. Nonetheless, the popular discontent voiced during these elections could make the reform and adjustment process more arduous.

2. **Through the crisis, the economy fared better than other large euro area economies, except Germany, but it is also behind others in the recovery cycle** (Figures 1 and 2)**.** Investment in particular remains depressed and the output gap widened to -2.2 percent in 2013, with unemployment stuck above 10 percent. Demand has been constrained by a weak external environment and the drag caused by structural fiscal adjustment of nearly 3 percent of GDP over three years (2011–13). Resilient wage growth helped sustain consumption; but, combined with faltering productivity growth, it also compressed profit margins. Falling profitability, in turn, appears to have amplified the contraction of investment in response to flagging demand.[1] Long-standing structural and competitiveness problems have compounded these negative factors.

3. **Private consumption has been an important factor of resilience in the French economy.** During the crisis, the private saving rate did not react as procyclically as in other economies (notably the United States and the United Kingdom), and consumption growth remained positive, except for a small dip in 2012—real consumption was 2.5 percent higher in 2013 than at the pre-crisis peak, and the household saving rate has been relatively stable around 15½ percent in the last decade. The stability of consumption, even as disposable incomes were squeezed by rising taxation, reflects extensive social safety nets and sustained real wage growth.

4. **The stability of private consumption also reflects weak exposure to asset price changes.** The absence of observable wealth effects in consumption, which have amplified the recession in other advanced economies, owes to conservative financial holdings (mostly bank deposits and life insurance products which have built-in shock absorbers) and inability to monetize real estate wealth because of rigid lending standards—these are based on capacity to repay rather than collateral. Thus, in the absence of over-leveraging, the gradual correction of real estate prices which is underway—real prices are 9 percent below pre-crisis peak—has had no discernible impact on consumption.

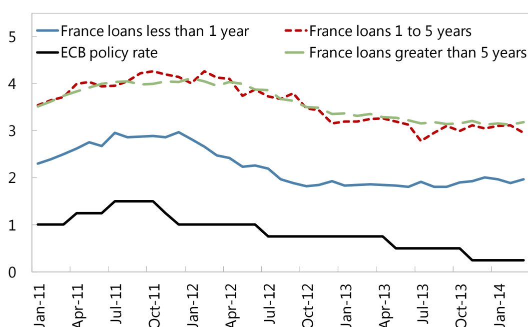
[1] See Selected Issues: "The Drivers of Business Investment in France: Reasons for Recent Weakness."

5. In the wake of disinflationary pressures that began in 2012, inflation has stabilized around 1 percent. The slowdown in inflation (from 2.3 percent in 2012Q2 to 0.9 percent in 2014Q1) originates from declining core, energy, and food inflation in about equal proportions (Figure 3). Core inflation bottomed out mid–2013 driven by the continued compression in profit margins, pass through of lower import prices into manufacturing products, and the significant drop of telecom prices following the entry of a fourth operator. As some of the temporary factors waned, core inflation has edged up to just over 1 percent.

6. Monetary easing has been transmitted into domestic interest rates, but monetary conditions have tightened since 2012. Despite the low level of nominal lending rates, falling inflation expectations have led to an increase in real interest rates. Balance sheet restructuring by banks was achieved mostly by shedding non-core foreign activities while preserving the core lending business. Domestic credit growth has thus remained positive through much of the crisis, although in 2013 the only growth was in mortgage lending. Corporate and household debt levels have increased, but they remain moderate by international comparison (Figure 4).

Though nominal interest rates have remained broadly stable,

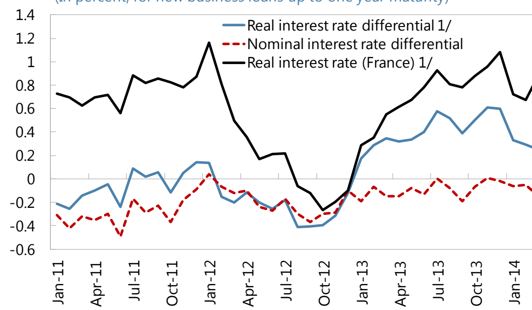
France: Lending Rate for New Business Loans
(In percent)



Sources: Haver Analytics, IMF Staff calculations.

real interest rates have risen as inflation has come down.

France: Real Lending Rate and Differential Relative to Germany
(In percent, for new business loans up to one year maturity)



Sources: Haver Analytics; Consensus Forecasts; and staff calculations.
[1] Nominal rates deflated using CPI consensus forecasts.

7. Notwithstanding the significant adjustment already achieved, the government deficit was still 4.2 percent of GDP in 2013 (2.8 percent in structural terms). The persistence of structural fiscal deficits stems from the fact that public expenditure has tended to outrun GDP growth over decades, including through the fiscal stimulus of 2009. The resulting accumulation of deficits since 1975, even in good times, has reduced fiscal space and limited the ability of governments to sustain demand as the economy slowed down in 2012-13 (Figure 5).[2] Fiscal space is also constrained by contingent liabilities, which declined from 152 percent of GDP end 2012 to

[2] As the structural deficit in 2012-13 diverged significantly from the multi-year fiscal law of 2012, the fiscal council triggered the corrective mechanism in May 2014 (for details see Box 1 of the Staff Report for the 2013 Article IV Consultation, Country Report No. 13/251). In response, the government said it will take additional spending measures (0.2 percent of GDP) this summer; and it will likely send to Parliament, in the fall, a new multi-year fiscal law targeting structural balance in 2017 rather than in 2016 (consistent with the April 2014 stability program).

134 percent of GDP in 2013 (slightly more than half is related to pensions). Despite the increase in debt, government borrowing rates have stabilized at historically low levels (the 10-year yield has declined from 4.7 percent in June 2008 to less than 1.9 percent in May 2014).

8. The fiscal policy strategy was to divide the adjustment equally between revenue and expenditure measures but to front-load the revenue measures because of their lower (expected) multiplier. The tax burden increased by 2.8 percent of GDP from 2007 to 2013. Fiscal adjustment shifted from tax increases to expenditure containment in 2013, but growth of spending was still 0.9 percent in real terms. The strategy has encountered a number of challenges, including a political backlash against taxation, falling tax buoyancy and inflation, expenditure slippages at the level of local governments, and rising social spending. In the event, the social insurance system which has contributed to the economy's resilience has become more difficult to sustain financially and to reconcile with deficit reduction.

9. Loss of competitiveness has weighed on growth. The competitiveness gap is evident from export market share and unit labor cost developments (Figure 6). The evidence based on price competitiveness is less clear, because narrowing profit margins have compensated for the loss of cost competitiveness. At the same time, EBA model estimates suggest that the 2013 current account was 1 to 3 percent of GDP below its cyclically-adjusted norm. Based on all of these considerations, staff considers that the real exchange rate in 2013 was 5-10 percent higher (i.e., overvalued) relative to medium term fundamentals and desirable policy settings. Export performance appears weak even when correcting for the fact that France is less integrated in the Global Value Chains, which tend to gross up both imports and exports.[3] Non-cost factors weighing on competitiveness are related to rigidities in the economy. The recent narrowing of the current account deficit—from 2.1 percent of GDP in 2012 to 1.3 percent in 2013—reflects to a greater extent weak domestic demand than a rebound of export growth. The net international investment position has deteriorated since the outset of the crisis to -20 percent of GDP. However, its size and trajectory do not raise sustainability concerns.

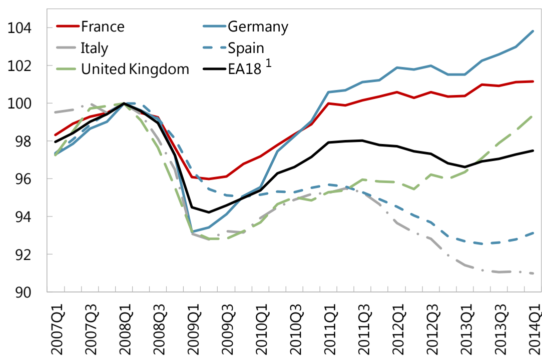
10. Financial sector indicators show continued improvements, but banks remain exposed to wholesale funding risks. Banks have made significant progress in building capital and liquidity buffers, drawing from increased profitability and adjustments in their funding structure. These improvements have been reflected in rising price-to-book ratios (Figure 7). Despite a further reduction in the loan-to-deposit ratio (to 115.9 percent in 2013 for the six large banking groups), banks face gaps relative to future net stable funding ratio requirements. And, although the large groups have met the CRD-IV fully loaded minimum CET1 capital requirement, many peers have gone further. Deleveraging has continued, with total assets of the five large banking groups down 7.5 percent in 2013. Non-performing loans have risen to 4.5 percent in 2013 (Table 5), but continue to be well provisioned.

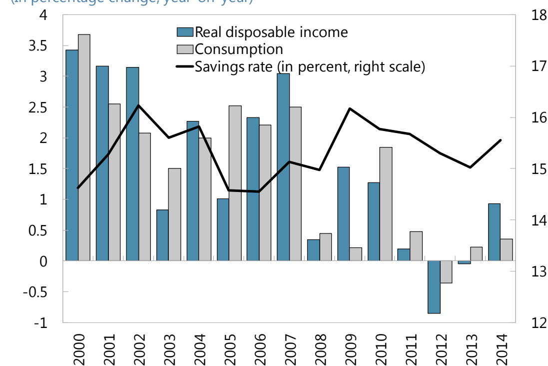
[3] See Selected Issues: "France in the Global Value Chains: Revisiting the Competitiveness Loss."

Figure 1. Real Sector Developments, 2007–19

The French economy weathered the crisis relatively well compared to peers....

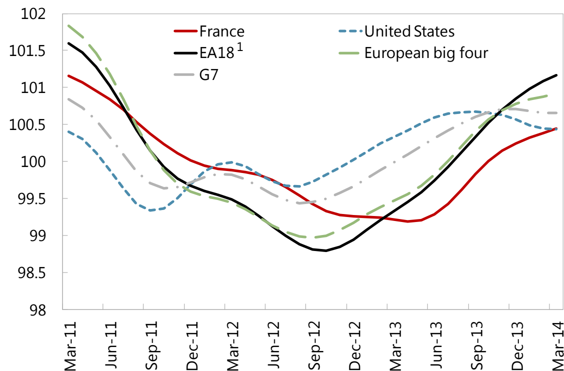
....supported by the resilience of private consumption

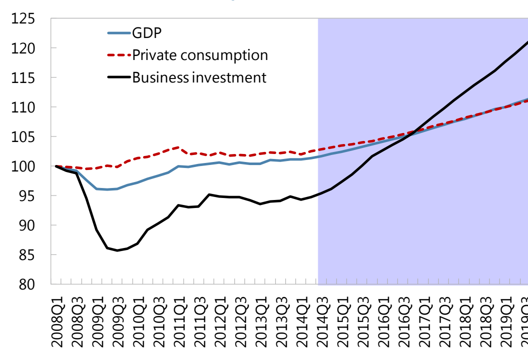




Composite leading indicators point to a lag in the recovery in France compared to other large economies ....

....which should be followed by steady medium-term growth, as investment recovers lost ground.





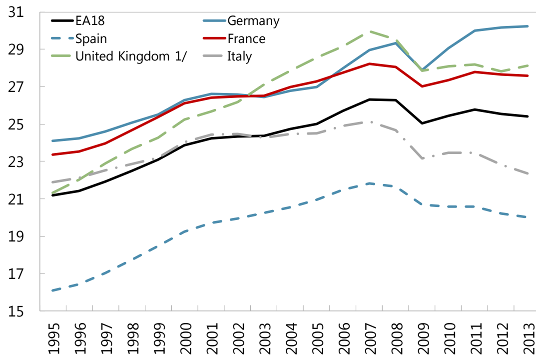
Sources: OECD, Haver Analytics, and IMF Staff calculations.

[1] Comprises Austria, Belgium, Cyprus, Estonia, Finland, France, Germany, Greece, Ireland, Italy, Latvia, Luxembourg, Malta, Netherlands, Portugal, Slovakia, Slovenia, and Spain.

Figure 2. Per Capita Income 1995–2013

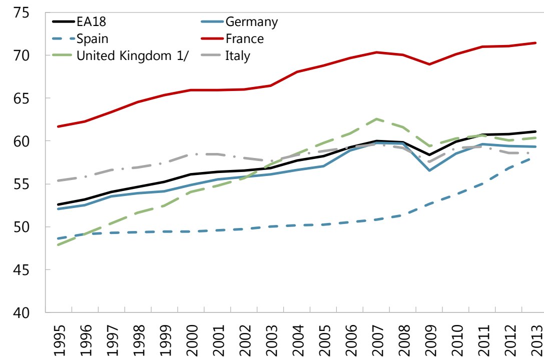
Real GDP per capita in France has grown in line with the euro area average and remains below the pre-crisis peak.

Real GDP per Capita
(In thousands of 2005 euros)



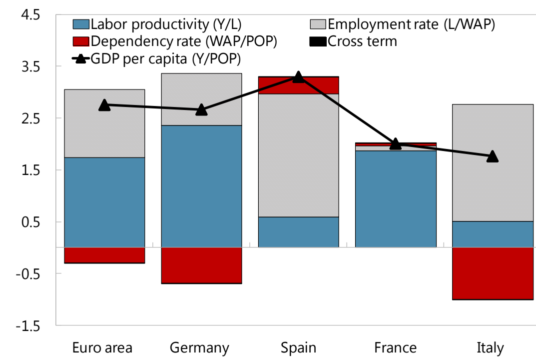
Income growth in France has been sustained by a highly productive labor force, while employment rates have remained lower than in other countries.

Real GDP per Person Employed
(In thousands of 2005 euros)



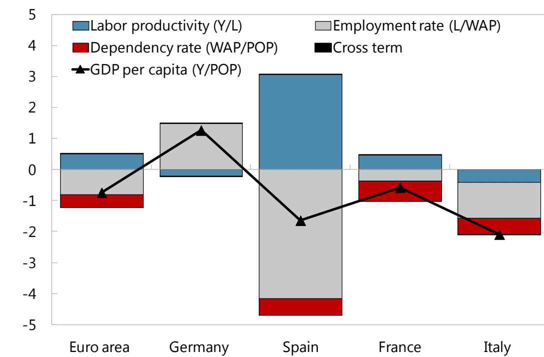
The growth of real per capita income in France prior to the crisis was driven essentially by labor productivity growth, with virtually no contribution from increase in the employment rate. This contrasts with the observed increases of the employment rates in peer countries.

Growth of Real GDP per Capita, and Components, 2000-07
(In percent change, and percentage point contributions)



Since the outset of the crisis, the loss of real per capita income in France reflects both rising dependency rates and falling employment rates, although to a lesser extent than in peer countries (with the exception of Germany).

Growth of Real GDP per Capita, and Components, 2008-13
(In percent change, and percentage point contributions)



Sources: AMECO, Haver Analytics, and IMF Staff calculations.

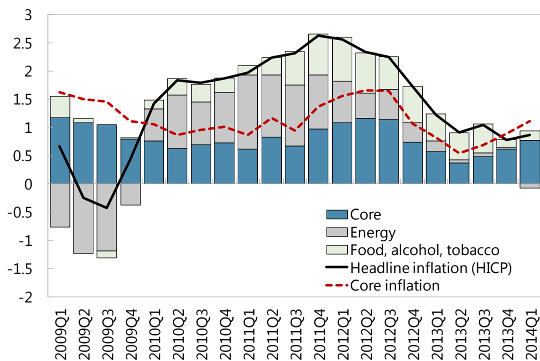
[1] Converted into Euros using the average exchange rate for 1995-2013.

Figure 3. Inflation Developments, 2009–13

Inflation has fallen rapidly since 2012, and ….

Headline and Core Consumer Prices (HICP)

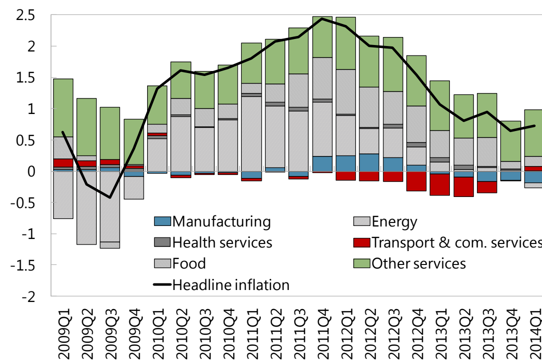
(In percent change, year-on-year; bars in contribution to total)



….with waning temporary factors, inflation has stabilized around 1 percent.

Contributions to Headline Inflation by Items

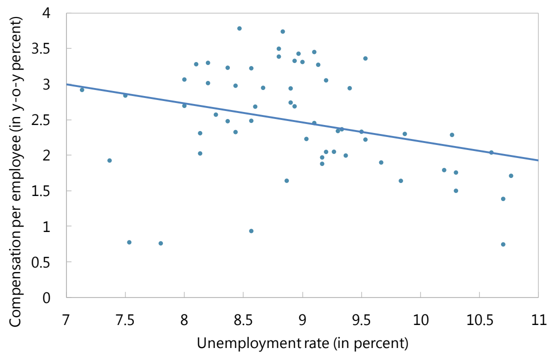
(In percent change, year-on-year; bars in contribution to total)



Longstanding labor market rigidities have rendered wages relatively unresponsive to unemployment conditions….

The Phillips Curve

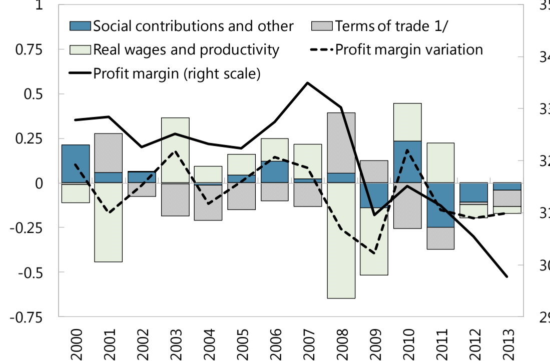
(1999Q1-2013Q3)



…and profit margins have been squeezed by real wage growth and the deterioration in the terms of trade

Contributions to Profit Margins

(In percent change, year-on-year; bars in contribution to total)

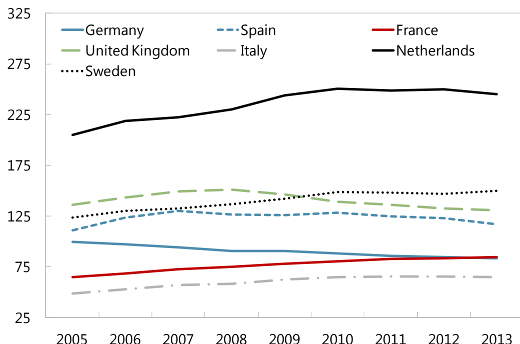


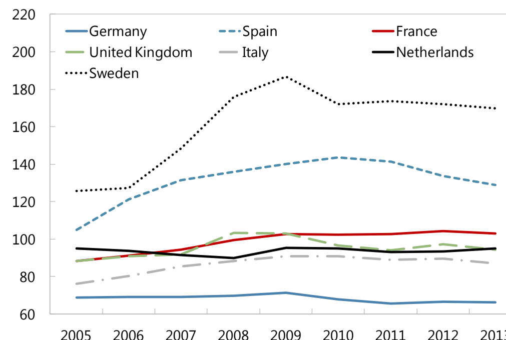
Sources: INSEE, Haver Analytics, and IMF Staff calculations.

[1] Ratio of value added deflator to consumption deflator.

Figure 4. Debt and Financing Conditions for Non-Financial Private Sector

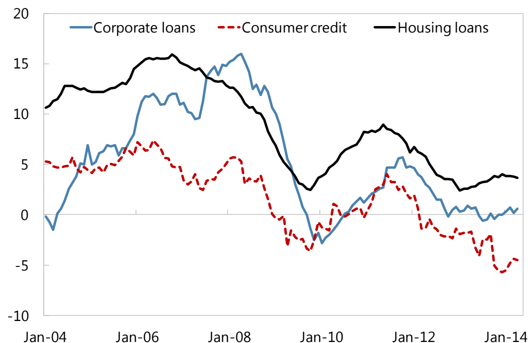
Household and corporate debts are moderate relative to peers.

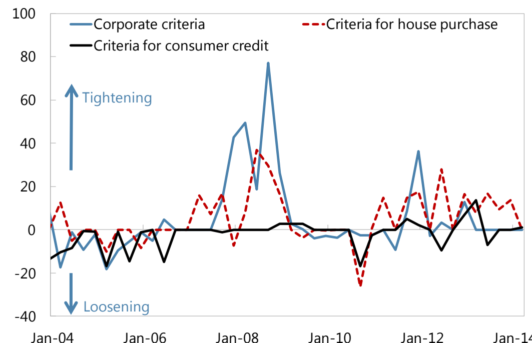




In the past year, positive credit growth has been driven by mortgage lending....

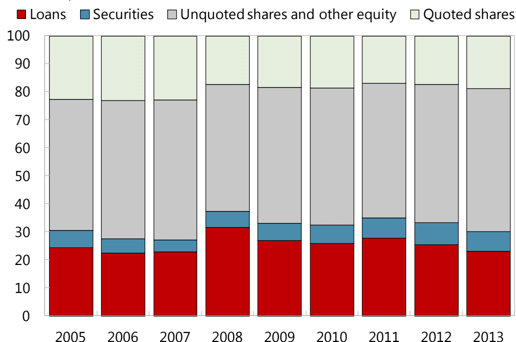
...even as credit standards for mortgages were tightened.

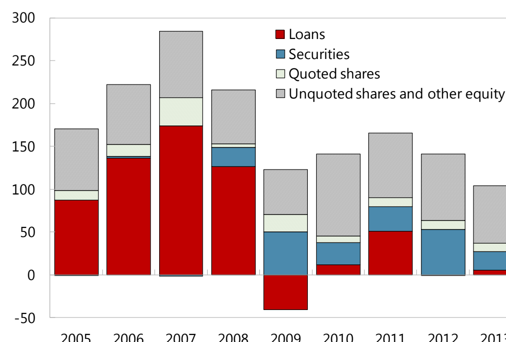




Bank loans remain central to enterprise debt financing ...

.... even though the share of market financing has been growing in recent years.



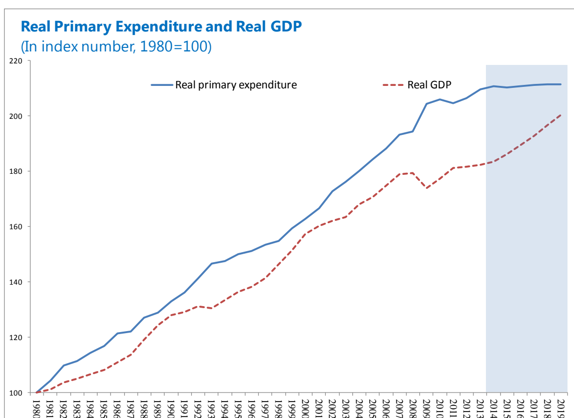


Sources: ECB, Haver Analytics, and IMF Staff calculations.

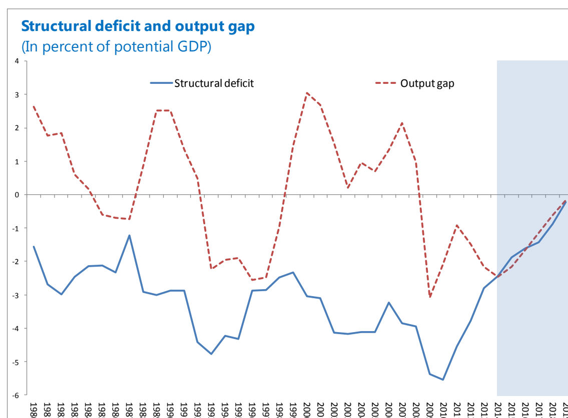
[1] The difference between consolidated and non-consolidated NFC debt in these countries was a maximum of 21 percent of GDP in 2012 for France; no consolidated data exist for the UK.

Figure 5. France: Fiscal Developments and Adjustment Scenario

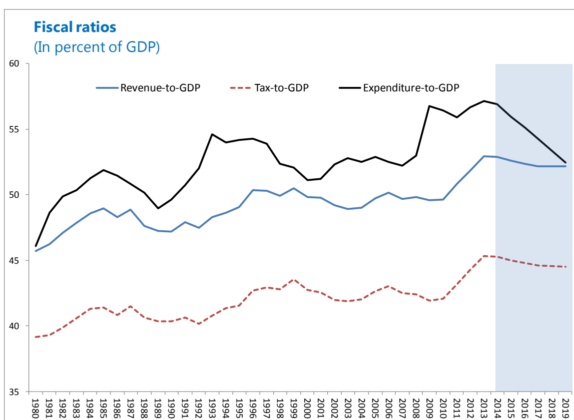
Spending has outpaced GDP…



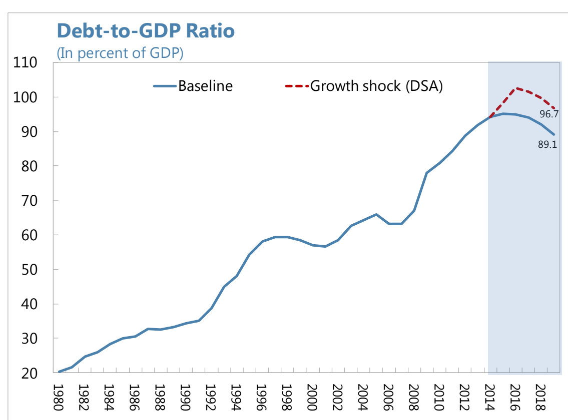
… making it difficult to close the structural deficit even in good times,….



… despite a ratcheting up of taxes.



The result has been a steady erosion of fiscal buffers.

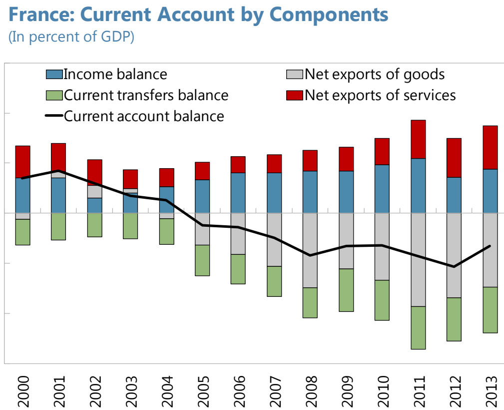


Sources: French Authorities, INSEE, and IMF Staff calculations.

Figure 6. External Developments, 2000–13

The steady deterioration in the current account….

France: Current Account by Components
(In percent of GDP)

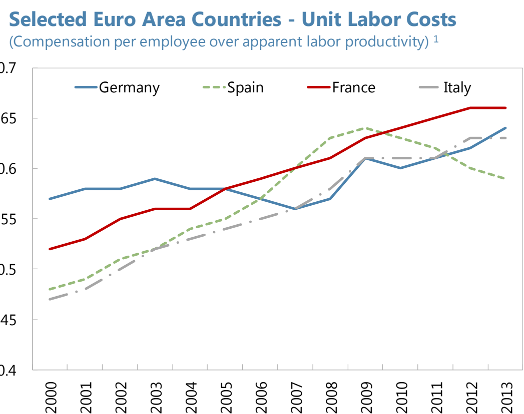


….is mirrored by weak export performance

Share in Exports of Goods and Services, 1997-2013
(In percent change)

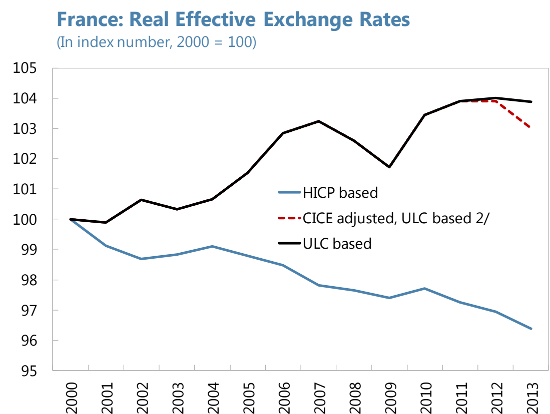
More recently, external competitiveness has been undermined by losses in cost competitiveness relative to some peers…

Selected Euro Area Countries - Unit Labor Costs
(Compensation per employee over apparent labor productivity) [1]



….which exporters have offset by squeezing profit margins so as to preserve price competitiveness.

France: Real Effective Exchange Rates
(In index number, 2000 = 100)



Sources: European Commission, IMF WEO Statistics, IMF BOP Statistics, Haver Analytics, and IMF Staff calculations.

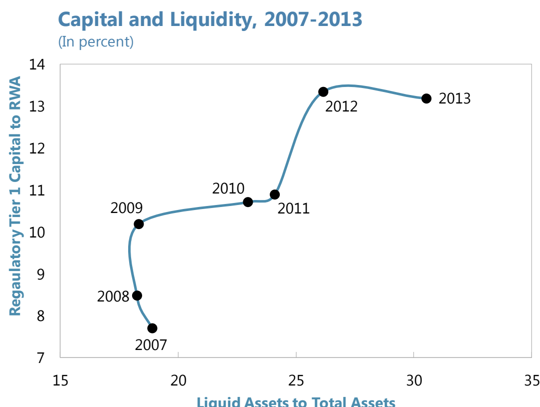
[1] Compensation in current Euros divided by apparent labor productivity measured in 2005 Euros.

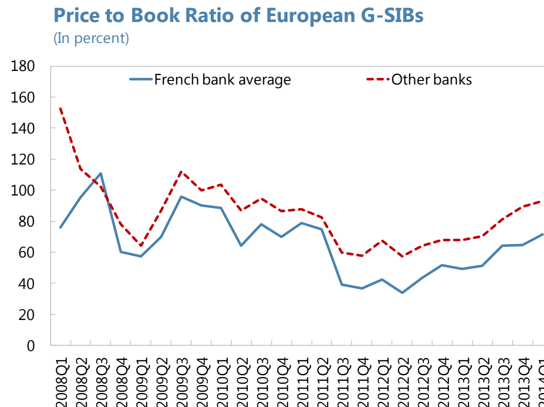
[2] Adjusted by imputing the CICE tax credit (0.9 percent of GDP) to lower labor costs.

Figure 7. Banking Sector Developments

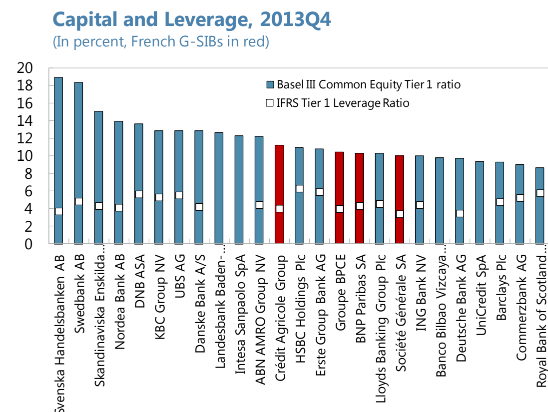
System capital and liquidity ratios have improved …

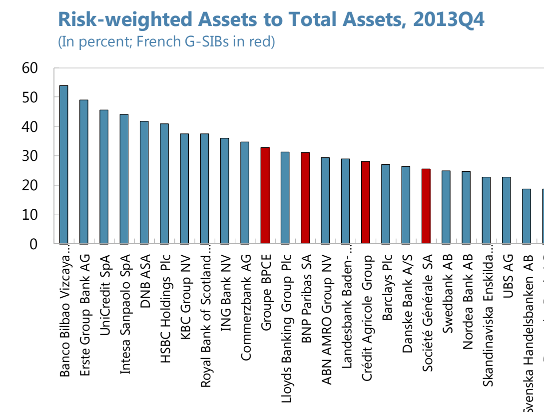
… and markets have responded positively.





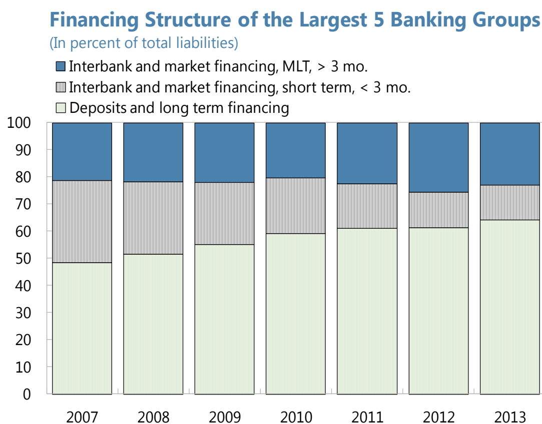
In the French systemically important banks, capital ratios meet fully-loaded Basel III requirements; leverage ratios are in the low range, reflecting relatively low risk-weights.

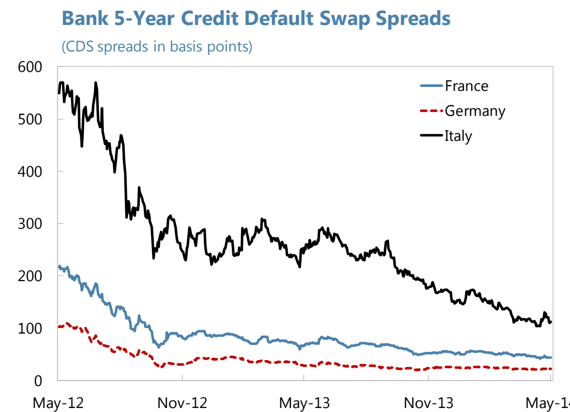




Stable financing sources have increased, but wholesale funding remains large.

Market conditions have been favorable.





Sources: Banque De France, ACPR, SNL Financial, Bloomberg, and IMF Staff calculations.

OUTLOOK AND RISKS

11. The recovery faces a difficult take off. On the back of a weaker than expected first quarter, staff revised growth projections relative to the April WEO, to 0.7 percent in 2014 and 1.4 percent in 2015. The expected gradual recovery rests on stronger external and domestic private demand (from gains in real disposable income and gradual improvements in profit margins), and a lesser fiscal drag. Supply side measures are expected to gain in strength over the medium term. Following 2 years of net job destruction, the private sector should become a source of net job creation this year, but the unemployment rate should begin to come down measurably only in 2016.

12. Inflation is expected to remain around 1 percent, rising only very gradually over the medium term. The inflation projection is predicated on moderate wage inflation related to the slack in the labor market and the need of enterprises to restore profit margins. However, there are non-negligible downside risks to the inflation outlook. While so far wage growth has declined very slowly in response to labor market slack, it could decelerate more rapidly in a context of continued slow output growth. In particular, downward pressures could develop as falling inflation feeds into wages through the indexation of the minimum wage.

13. The 2014 budget was prepared on the basis of prudent macroeconomic assumptions, reflecting the moderating role of the fiscal council. The authorities project a deficit of 3.8 percent of GDP based on additional saving measures to be adopted this summer. Staff projects a deficit of 4.0 percent reflecting the downward revision to growth and lower tax buoyancy. Structural adjustment would be 0.4 percent of GDP, the bulk of it coming from expenditure containment.

14. The authorities' medium-term scenario envisages a somewhat stronger and faster response of the economy to supply side measures. The Stability Program, prepared prior to the release of the poor Q1 results, envisaged growth of 1 percent this year and 1.7 percent in 2015, rising to 2.25 percent by 2016. It also assumed higher price and wage inflation and a more rapid decline of the unemployment rate. The newly created fiscal council assessed the growth and employment projections to be realistic for 2014, possible but subject to the "realization of several positive assumptions" in 2015, and optimistic for 2016-17.

15. Delivery of planned supply side and fiscal policies should help correct the external imbalance. In the staff's baseline scenario, the current account deficit is projected to close over the medium-term in tandem with the fiscal deficit. This would bring the external position to a level consistent with fundamentals and desirable policy settings. This adjustment is to be facilitated by internal depreciation induced by the implementation of the authorities' policy program of public expenditure containment and labor tax reductions, and by wage moderation. These policy actions are aligned with those recommended by staff to close the external gap.

16. Risks around the baseline scenario remain substantial, reflecting uncertainty about the timing and strength of the cyclical turnaround and the impact of popular discontent on policy resolve. Slower global growth and financial market volatility are the main external risks (see Risk

Assessment Matrix). The main domestic risk is a stalled recovery of investment in the face of an uncertain outlook—some leading indicators remain below average. A negative spiral of low growth and falling inflation, and its effect on real interest rates, would have additional adverse effects on investment and the fiscal deficit. Lower-than-expected growth could also fuel popular discontent and could undermine fiscal resolve. However, the fiscal responsibility framework would likely kick in to limit backtracking on fiscal policy. Public debt is particularly sensitive to a lower growth scenario (DSA in Appendix II). On the upside, staff could be underestimating the rebound, given the well-known difficulties in projecting cyclical turnarounds. The main financial sector risks stem from the banks' continued reliance on wholesale funding, even though the maturity of debt has been lengthened; medium-term risks relate to the ability of French banks to adapt to changes in the regulatory environment (see policy discussion). Legal risks associated with their global operations (e.g., investigations into market manipulation, compliance with international sanctions) could also weigh significantly on some banks, particularly if penalties were to curtail some of their international activities.

17. The potential for outward spillovers from France appears to have abated since the crisis, particularly with respect to financial linkages. Recent research shows that, whereas credit and funding shocks to French banks could have induced banking failures in more than ten countries in 2008, as of 2012 significant outward spillovers would have been limited to Belgium, Italy, and Ireland, reflecting lower cross-border exposures.[4] Other research shows that, under deteriorated liquidity conditions, cutbacks in interbank lending were the first line of defense of French banks, and that banks with higher capital ratios were able to maintain higher rates of lending to the foreign non-financial sector.[5] By implication, the generalized improvement in capital ratios since the crisis should help limit outward spillovers to the real sector in the event of renewed liquidity stress. With respect to trade linkages, France continues to exercise strong demand effects especially on small neighboring countries. A recent study highlights the strong outward spillovers of business investment in particular, given its large import component.[6] In all, with investment set to recover gradually, and with banks' capital and liquidity positions strengthened and direct financial inter-linkages reduced, large adverse spillovers from France appear less likely.

[4] Kim and Mitra, "Real and Financial Vulnerabilities from Crossborder Banking Linkages," IMF Working Paper, forthcoming.

[5] Bussière, Camara, Castellani, Potier and Schmidt, 2014, "Shock Transmission Through International Banks – Evidence From France," Banque de France Working Paper No. 485.

[6] Bussière, M., G. Callegari, F. Ghironi, G. Sestieri, and N. Yamano, 2013, "Estimating Trade Elasticities: Demand Composition and the Trade Collapse of 2008-2009," American Economic Journal: Macroeconomics, vol. 5(3).

France: Risk Assessment Matrix[7]

Source of Risks	Relative Likelihood	Impact on France if Realized
Surges in global financial market volatility (e.g., related to geopolitical tensions, revised market expectation, UMP exit)	**High** Market volatility and higher-than-expected increases in long-term rates.	**Medium** Inward spillovers from global financial market volatility have been limited in recent years, but could affect interest rates in the future.
Protracted period of slower growth in advanced and emerging economies	**High** Weak demand could take a toll on productive capacities. Risk of deflation in Europe has increased.	**Medium** Impact from trade and investment links mitigated by automatic stabilizers in the short run, but domestic growth would suffer eventually. Entrenchment of high structural unemployment and limited fiscal space would make it difficult to exit low growth trap.
Risks to financial stability from incomplete regulatory reforms (medium term)	**Medium** Global risks from regulatory uncertainty offset in part by convergence to banking union in the euro area, which reduces the risk of fragmentation.	**Medium** French banks are vulnerable to a globally systemic closure in funding markets. Pressures to meet stricter leverage ratios on a short horizon could trigger further deleveraging and, in turn, erode profits.
Housing price correction	**Medium** Housing prices supported by strong fundamentals but empirical estimates suggest 10-20 percent overvaluation.	**Low** Limited impact on banks due to sound lending standards, but possibly larger impact from a concomitant shock to income and employment.
Weak implementation of fiscal and structural policy commitments.	**Medium** Political resolve for reform may wane in the face of protracted low growth and popular discontent.	**Medium** Reversal of commitments could undermine investment and growth, and aggravate the external imbalance enough to trigger adverse market reactions.

[7] The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relative likelihood of risks listed is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability of 30 percent or more). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly.

POLICY DISCUSSIONS

18. *A comprehensive policy program to address structural imbalances.* Persistent fiscal deficits have eroded fiscal space to the point where there may not be enough room to counter effectively possible future shocks without putting fiscal credibility at risk. Underutilization of labor resources, with an employment rate of youth and seniors among the lowest in the OECD, has not only lowered potential GDP but also impacted social spending, with adverse effects on the fiscal balance and taxation. Overlaying these challenges is a competitiveness gap which has further undermined potential growth. This diagnostic, shared by the authorities, is the motivation behind the ambitious course of adjustment and reform laid out in the April 2014 Stability Program and National Reform Program. At the core of the strategy are a very sizeable correction in public expenditure and measures to increase the supply response of the economy.

19. *Steady and more moderate fiscal adjustment going forward.* The Stability Program targets structural fiscal adjustment averaging about ½ a percent of GDP a year, until (structural) fiscal balance is reached. Staff and the authorities agreed that this objective adequately balances the need to restore fiscal space against the risk of undermining the recovery. Staff noted that no additional measures should be taken this year, beyond those already planned, given the fragility of the recovery. The authorities project to converge to structural fiscal balance by 2017 (the horizon of the Stability Program). Under the staff's more conservative macroeconomic scenario, fiscal adjustment would need to continue at the same pace until 2019 to reach balance (see staff baseline scenario in the tables).

20. *Adjustment anchored by an expenditure reduction plan.* Because of simultaneous tax cuts (see below), the strategy relies on sizable expenditure reduction (relative to trend). The expenditure effort (2.2 percent of GDP over three years) is distributed across all sectors, including local governments and social security where expenditure growth has been the strongest in recent years. Expenditure cuts at the local government level will be backed by institutional reforms aimed at rationalizing overlapping structures which have contributed to overspending. This institutional reform should begin in the next couple of years. In all, real expenditure would remain roughly constant over the next three years, compared to growth of 0.5 percent in 2011-14. The areas of adjustment have been identified, and the underlying measures are in various stages of preparation. The authorities plan to provide greater clarity on the specific measures in the multi-year finance law in the fall (Box 1).

21. *Still, sizeable implementation risks ahead.* Given the scale of the effort, resistance to expenditure tightening is likely to build up as specific measures are put up for discussion with social partners and for parliamentary approval. Staff also noted that institutional reform that will help contain local government spending will only come into effect over the medium term. In the meantime, there is a risk that local governments would react to reduced transfers from the central government by cutting productive investment, raising taxes, or increasing debt. This would undermine the government's strategy.

22. ***Careful piloting needed to mitigate these risks.*** The authorities recognized the difficulty of piloting this program over the next three years, but emphasized the strong political will behind it, as reflected in the decision to obtain parliamentary endorsement. With such endorsement, the authorities believed they could pursue the necessary measures, even if concessions may need to be

Box 1. The Spending Containment Package

Announced expenditure containment of €50 billion, relative to trend, over 2015-17 implies an effort of 2.2 percent of GDP and would result in a stabilization of real spending over the three years. By comparison, the expenditure effort planned for 2014 is €19 billion (including €4 billion in extra cuts added in supplementary budgets).

The cuts are frontloaded: €21 billion in 2015, €16 billion in 2016, and €13 billion in 2017. Cumulatively, they represent about 4 percent of spending for each level of government (central, sub-national, and social security). The cuts are distributed as follows:

- **Central government**: €18 billion. To be achieved through spending rationalization, pooling of purchases and ICT spending across ministries, reduced funding of state agencies, and extension of the wage freeze introduced in 2010 combined with stabilization of the number of civil servants.[1] Discussions are under way on how to distribute the burden across ministries consistent with government priorities.

- **Local governments**: €11 billion cut in transfers from the central government, expected to lead to equivalent cuts in spending. These cuts follow a freeze in 2012 and a €1.5 billion cut in 2014. Because of their fiscal independence, local authorities could, within limits, compensate for lower transfers by raising taxes and debt.[2] To ensure that the cut in transfers will translate in spending reductions, the government has launched plans to reduce the number of sub-national governments over the medium term. The plan also includes elimination of the general competency clause which has spurred duplication of spending by allowing the various layers of government to operate in the same areas of competence.

- **Health spending**: €10 billion. Measures have been largely identified, and they are mostly structural: development of ambulatory surgery (€1 billion), rationalization and pooling of hospital spending (€1 billion), cut in medicine costs notably through promotion of generics (€3.5 billion), elimination of ineffective medical procedures (€2.5 billion). Additional savings would come from the public sector wage freeze and from fighting fraud.

- **Social protection**: €11 billion. €2.9 billion comes from recent reforms of family allowance and pensions; €4 billion from de-indexation of pensions, family, and housing allowances—expected to be adopted in 2014; and €2.8 billion from additional reform of unemployment insurance and family allowances—yet to be defined. The remaining €1.2 billion in savings would come from reduced administrative costs.

The proposed savings are at different stages of identification. The wage freeze, de-indexation of social benefits, and impact of recent reforms in social benefits are well identified. Central government savings (outside of wage and employment freeze) have yet to be announced, but the central government has the means to deliver. Savings in health spending are identified and rationing mechanisms are in place to ensure execution, although health spending is subject to factors that fall outside the control of the authorities. Of the social spending saving, about €4 billion depends on reforms of social protection programs, which will need to be decided in consultation with social partners, who are ultimately responsible for these programs. As for local governments, they have the means to realize savings by reducing employment through attrition, and by containing other current and capital spending. The degree to which there will be leakage into higher taxes or higher debt is uncertain.

[1] The base wage freeze applies to all levels of government.

[2] The potential for tax increases is limited by the narrow own tax base (6 percent of GDP). Local governments can only resort to debt financing for capital projects, so debt could increase only by shifting the financing of such projects from own resources to debt.

made at the margins. As for the effort required of local governments, they noted that it was doable without disorderly adjustment or leakages into higher taxes or debt, since it only implies a stabilization of real spending (compared to a reduction of about 1 percent per year for the central government). Nonetheless, the authorities were seeking to develop coordination mechanisms to guide and monitor the actions of local governments through the consolidation phase. They also thought that raising taxes was no longer politically viable for local elected officials**.**

23. *Supply side measures to reinvigorate investment and job creation.* The package of supply side measures includes: (i) tax cuts for enterprises (2 percent of GDP in 2014–17), comprising the CICE[8] tax credit scheme introduced in 2013, and the various tax breaks under the Responsibility and Solidarity Pact (RSP) announced by the new government; and (ii) an enhanced program of regulatory simplification conducted in consultation with enterprises. The intention behind the tax cuts, which are mostly in the form of lower labor taxes, is to restore profit margins and thus the capacity of enterprises to invest, and to enrich the employment content of growth. The authorities also planned to ease regulatory thresholds which create additional costly regulatory requirements beyond 10, 20, and 50 employees, hampering enterprise growth and development. Though the bulk of tax cuts will benefit firms, the authorities also plan to reduce taxes paid by household by about 0.25 percent of GDP over 2015-17, which should more directly support demand.

24. *Potentially significant impact of the tax cuts, but over an uncertain horizon.* The authorities have estimated that the tax reductions of the RSP would create about 200,000 jobs. Staff has estimated that the reductions in labor taxes under the CICE and the RSP (about 1.4 percent of GDP in all) would create at least 600,000 in the long run, after the capital stock has fully adjusted.[9] However, both sets of estimates are derived from models that neglect demand side constraints, which would affect the time it takes to realize these gains. For the authorities the gains can be realized in full by 2017, while staff considered it would take longer.

25. *Slow product market reform has left the economy with unrealized potential gains.* The gradual product-by-product approach to liberalization pursued until now has had mixed results, as reforms have been limited and often thwarted or watered down by vested interests, notably in services. Indeed, the OECD Product Market Regulation (PMR) indicator shows no progress over the last five years (Figure 8). Estimates of the gains from product market liberalization vary considerably.[10] A recent study estimated that a move by France to the OECD frontier in terms of the PMR indicators could increase productivity by 3 percent after 5 years.[11] A 2014 staff study estimated that a 1 percent productivity gain in regulated services accounting for less than 30 percent of GDP

[8] Crédit d'impôt compétitivité emploi.

[9] Espinoza R. and E. Pérez Ruiz, 2014, "Labor Tax Cuts and Employment: A General Equilibrium Approach for France," IMF WP 14/114, Washington DC: International Monetary Fund.

[10] See Hallaert, J.J., 2013, "Gains from Services Sector Reform," France Selected Issues, Country Report No. 3/13.

[11] Bourlès, R., G. Cette, J. Lopez, J. Mairesse, and G. Nicoletti, 2010, "The Impact on Growth of Easing Regulation in Upstream Sector," CESifo DICE Report, vol. 8(3).

(distribution, transport and storage, and other business services)) could raise GDP by 0.8 percent after two years.[12]

26. *A more decisive approach to product market reform going forward.* The authorities said they would pursue product market reform more proactively by stressing the purchasing power gains that can accrue from eliminating rents. The chosen methods of reform are reducing barriers to entry in regulated professions and/or changing price setting mechanism of regulated services. The competition authority has also gained a more visible role, and has stressed, for instance, the significant costs caused by constraints on competition in the transport sector. At the same time, the authorities have restated the importance of state intervention in product markets to steer the economy toward sectors with growth potential. Such intervention would come mostly in the form of seed money provided by the state to leverage private initiative. Staff underscored the large potential employment benefits of liberalizing opening hours in the retail sector and of the authorities' plans to simplify urban planning rules which currently stifle construction.

27. *A more adaptable labor market needed to complement supply side measures.* Rigidities in labor regulations and high and unpredictable dismissal costs have been a hindrance to hiring and labor mobility (Figure 9). The law on job security and flexibility sought to increase adaptability by easing cumbersome collective dismissal procedures and giving enterprises and their workers room to renegotiate, within bounds, labor market conditions when faced with restructuring needs.[13] This option has been used sparingly so far, perhaps because of its limitations. Meanwhile, other measures have been adopted to improve labor market functioning, including better targeted professional training and the introduction of rechargeable unemployment rights which should reduce inactivity traps.[14] The unemployment insurance system is scheduled for review by 2016. Staff noted that this is an opportunity to increase work incentives (for instance by revisiting degressivity rules and the high ceiling on benefits) and to align contributions of employers to their job turnover.

28. *Improved social dialogue as a foundation for reform*. Staff recommended expanding further the scope for enterprise level negotiations over work and pay, in order to increase the capacity of enterprises to adapt and take risks. The authorities supported the idea but noted that the process needs to overcome a history of conflictual labor relations. Observers suggested that it was because of this mistrust that state intervention had grown into a complex labor code and reliance on the judicial system to settle disputes. In this regard, the authorities underscored that the decision to involve social partners in the labor market reforms pursued since 2012 had already improved the quality of the social dialogue; and that the law on job security and flexibility may not have resulted

[12] Fernández Corugedo E. and E. Pérez Ruiz, 2014, "The EU Services Directive: Gains from Further Liberalization," IMF WP 14/113, Washington DC: International Monetary Fund.

[13] See Box 2 of the Staff Report for the 2013 Article IV Consultation, Country Report No. 13/251.

[14] Under the previous system, an unemployed person who took on a job would forfeit whatever remaining unemployment benefits he/she had accrued. This reduced incentives to take on risky jobs that could end before new unemployment eligibility is established. Under the new "rechargeable unemployment rights", unused unemployment benefits would be preserved if a new job is accepted and could be reactivated in case of loss of the new job.

in many successful negotiations, but it had spurred a welcome increase in discussions at the enterprise level.

29. ***The challenge of raising job prospects for the less skilled.*** A side effect of the minimum wage (EUR 1,445.4 per month) has been to limit job creation for the low skilled—the unemployment rate for workers with education up to a lower secondary degree was 16.2 percent in 2012, against 9.9 and 5.7 percent for those with intermediate and tertiary education, respectively. The authorities' approach to limit the rationing effect of the minimum wage has been to eliminate labor taxes at and near the minimum wage, and to expand subsidized job schemes and alternative job entry paths (apprenticeships and work-study schemes). Targeted labor tax cuts are, however, costly (around 1 percent of GDP already in 2012, before the new set of tax cuts) and could create low-wage traps.

30. ***The role of the minimum wage.*** Staff suggested that the objective of ensuring, through the minimum wage (SMIC), that work pays a living wage should also be balanced against the cost of exclusion from the labor market. It proposed that the indexation system of the SMIC include the unemployment rate of the low skilled. The authorities considered that the SMIC was too central to the social contract to contemplate any changes, and said they would continue to focus on facilitating job placement through subsidized jobs, apprenticeships and by improving skills.

31. ***Increased financial resilience and transition to banking union.*** The authorities underscored the progress made in the various building blocks of the banking union, with preparations for the Single Supervisory Mechanism well underway. Banks and the supervisor expected that the comprehensive assessment would validate the quality of the loan portfolios. Even so, they noted that surprises on the need for additional provisioning could not be ruled out, and banks could face additional changes, as the ECB will likely try to harmonize the validation of bank's risk models across countries.[15] The authorities also pointed to the actions taken to reinforce the resolution framework at the national level first (new banking law) and at the euro area level. A single resolution mechanism at the European level would, in time, address the problem of cross-border resolution which has contributed to national ring fencing and fragmentation. In all, banks and the supervisor believed that reinforced capital, liquidity and loss absorption buffers adequately mitigate too-big-to-fail (TBTF) risks. By contrast, they were concerned that the uncoordinated multiplication of regulatory safeguards (GLAC, MREL) could have unintended effects on financial intermediation. GFSR analysis has found that implicit subsidies for systemically important banks remain sizeable, suggesting that TBTF risks remain important, although regulatory reforms may have reduced them.

32. ***Adapting to changing global regulatory standards.*** The French financial system, with banks at the center of credit provision and life insurance at the center of savings mobilization, has left banks with a structural funding gap which they have filled through the wholesale market.[16] This has resulted in relatively high loan-to-deposit ratios and elevated liquidity risk. Under pressure

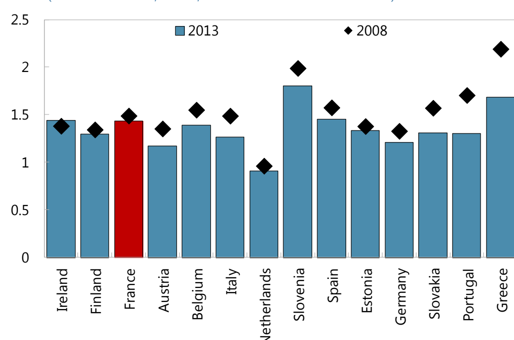
[15] Banks could also be required to hold additional buffers against legal/operational risk (see ¶16.)

[16] Tax advantages attract household savings to life insurance and regulated savings deposits which go in large part to the Caisse des Dépôts et Consignations (CDC), the public institution in charge of financing social housing.

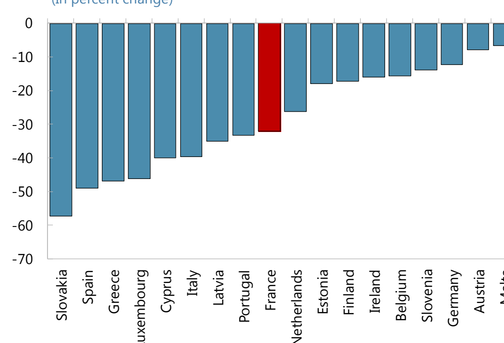
frommarkets and regulations to build larger liquidity buffers, banks have reduced their loan-to-deposit ratios considerably since 2011, helped in part by weak credit demand and low long-term rates which have made life insurance products less attractive.[17] However, under more stringent liquidity requirements, banks' deposit raising capacity may not be able to keep up with loan demand in a more buoyant environment. The authorities believed two factors would reduce this risk: increased securitization of bank loans and reliance of firms on market financing. Although these alternative financing channels have grown in recent years, they remain limited. Given uncertainties over their development, staff underscored that a reform of financial savings taxation might also become necessary to level the playing field, for instance by taking a maturity-based rather than a product-based approach to tax incentives.

Figure 8. France: Scope for Product Market Reform

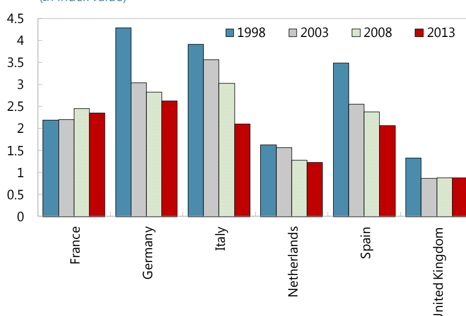
Product market reforms have been limited since 2008, as measured by the OECD.....



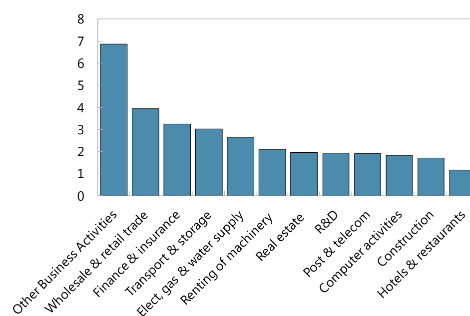
... even though some progress has been made in reducing barriers in the services sector.



Barriers to competition in regulated services remain high and raise the cost of these services...



..with an adverse impact on overall competitiveness since services are important inputs for other sectors.



Sources: OECD, Monteagudo and others (2012), and IMF Staff Calculations.

[1] Reduction in barriers to establishment of domestic and foreign providers.

[2] High index values indicate strict regulation.

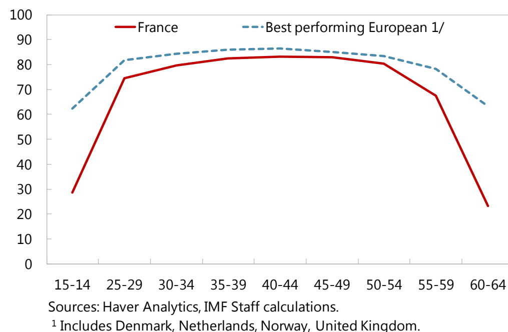
[3] Chart shows output rise in each sector due to a unit increase in final demand of all other sectors (forward linkages).

[17] They were also helped by the decision in 2013 to reduce the share of regulated saving deposits directed to the CDC for the financing of social housing. The decision shifted 30 billion Euros from the CDC to bank deposits (equivalent to 1¾ percent of non-bank private deposits).

Figure 9. Labor Market Features

Employment rates for youth and senior workers are low when benchmarked against best performers

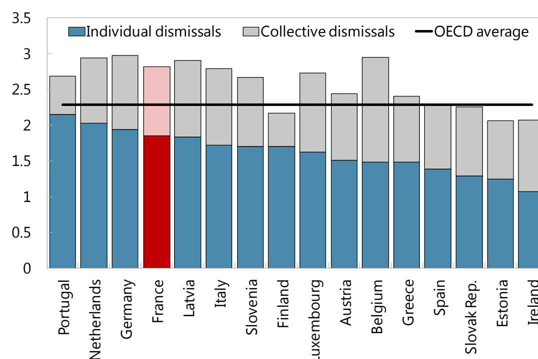
Employment Rates by Age Group, 2013
(In percent of population age group)



Sources: Haver Analytics, IMF Staff calculations.
[1] Includes Denmark, Netherlands, Norway, United Kingdom.

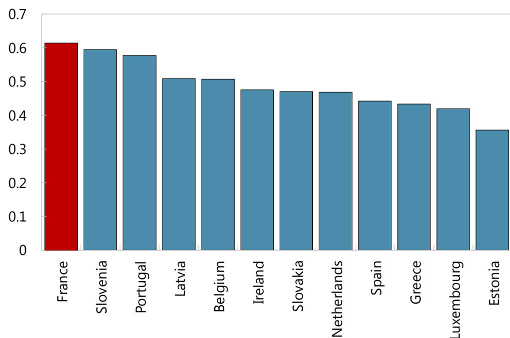
Dismissal rules are among the tightest in the OECD…

Protection of Workers Against Dismissals, 2013
(In index number)



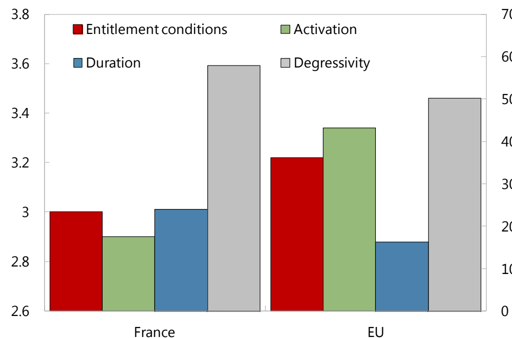
The gap between the minimum wage and the median wage is smallest in France.

Minimum Wages, 2012
(Ratio of minimum to median wage)



Unemployment benefits are more generous than the EU average, but activation policies are also less strict.

Entitlement, Activation, Duration, Degressivity
(In index number, number of months, and ratio)[1]



Sources: Eurostat, OECD, Stovicek and Turrini (2012), and IMF Staff calculations.

[1] Entitlement and activation index from 1 to 5, where 1 is less strict (left scale). Duration is equal to months of benefits for an unemployed worker with 22 years of contributions (right scale). Degressivity is equal average net replacement rate in years 2 to 5 as percent of net replacement rate in year 1 (right scale).

STAFF APPRAISAL

33. The strategy laid out by the authorities for the next three years holds the promise of placing the French economy on more solid foundations over the medium term. Economic policies may have appeared as lacking a clear direction in recent years, but they have gelled into a coherent package based on an accurate understanding of the challenges. Furthermore, the objectives are backed by well-identified policies. The strategy is ambitious and so naturally subject to risks; and it could be boosted by deeper structural reforms.

34. The chosen pace and instrument of fiscal adjustment are right. After three years of substantial adjustment, the more moderate pace of adjustment chosen under the Stability Program is appropriate given the weakness in the economy. Most importantly, the decision to anchor adjustment by an explicit expenditure target addresses the fundamental structural weakness of public finances. While simple expenditure containment will necessarily be part of the approach, the emphasis should go to structural measures to ensure that the rate of growth of spending is curbed permanently. On that score, important structural decisions have been taken, notably to rationalize local government layers and to contain the growth of health spending.

35. Both political and economic risks weigh on the strategy. Pressures to dilute the program could increase as difficult reforms are introduced. These pressures should be resisted as there is little room to deviate from the chosen course if both tax cuts and deficit reductions are to be pursued simultaneously. The medium-term budget to be presented to parliament in the fall is an opportunity to lock in specific measures underlying the adjustment, and thus reinforce the strategy. On the economic front, a delayed recovery poses the greatest risk. If growth threatens to disappoint projections by an appreciable margin, the pace of adjustment could be eased by moving forward or accelerating proposed tax cuts. However, this should not be a reason to postpone structural spending measures.

36. Monetary conditions have been insufficiently supportive of adjustment and restructuring of the economy. France did not suffer from financial fragmentation and lending rates remain at record low levels. However, monetary conditions have arguably become tighter owing to the strengthening euro and the fall of inflation and its impact on real interest rates. Such tightening does not appear appropriate for France's cyclical position.

37. Supply side measures to restart investment and job creation are welcome and should be boosted by reforms of labor and product markets. The proposed tax cuts will give breathing space to enterprises whose squeezed profit margins have impeded investment. Regulatory simplification is equally welcome. But these initiatives will not durably improve potential growth unless they are supplemented by better functioning labor and product markets. The renewed focus on fighting rents is a powerful guiding principle to spur reform and should be pursued by opening protected sectors to greater competition. This process of labor market reform should be broadened, with a view to giving enterprises and their workers more flexibility to negotiate working conditions. This also requires the establishment of a more cooperative social dialogue. The minimum wage is a

legitimate instrument to ensure that work pays a living wage, but its level should also be set with a view to limiting the exclusion effect it has for the low skilled. The authorities' efforts to enhance employment opportunities for the low skilled through job subsidies, apprenticeships, and work-study programs are welcome, but these schemes are unlikely, by themselves, to close the employment gap for this group.

38. The economy and public finances are better shielded today from the risks of banking shocks, but the evolving regulatory framework may require continued adjustments for banks. Higher liquidity and capital buffers, enhanced loss absorption capacity, and a strengthened European resolution framework will help mitigate too-big-to-fail risks. At the same time, the balance sheet adjustments needed to meet these requirements could reduce the intermediation role of banks in the French economy. While there are benefits to diversifying financing channels, these will take time to develop and they are subject to risks. In this context it will be important to ensure that, as banks adapt to the new environment, their financing role is not constrained by distortions in the taxation of financial instruments.

39. It is proposed that the next Article IV consultation take place on the standard 12-month cycle.

Table 1. France: Selected Economic and Social Indicators, 2009–19

	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
						Projections					
Real economy (change in percent)											
Real GDP	-2.9	2.0	2.1	0.3	0.3	0.7	1.4	1.7	1.8	1.9	1.9
Domestic demand	-2.6	2.1	2.0	-0.3	0.2	0.7	1.0	1.4	1.6	1.7	1.7
Nominal GDP (billions of euros)	1939	1998	2059	2091	2114	2156	2215	2284	2359	2442	2530
CPI (year average)	0.1	1.7	2.3	2.2	1.0	1.0	1.2	1.3	1.4	1.5	1.6
Unemployment rate (in percent)	9.1	9.3	9.2	9.8	10.3	10.3	10.2	10.0	9.7	9.4	9.3
Gross national savings (percent of GDP)	20.0	20.6	21.5	20.6	20.4	20.8	21.1	21.6	22.1	22.5	23.0
Gross domestic investment (percent of GDP)	21.3	21.9	23.2	22.7	22.0	22.4	22.1	22.2	22.3	22.4	22.7
Public finance (percent of GDP)											
Central government balance	-6.0	-6.1	-4.4	-3.9	-3.3	-3.2	-3.1	-2.6	-2.1	-1.3	-0.5
General government balance	-7.2	-6.8	-5.1	-4.9	-4.2	-4.0	-3.4	-2.7	-2.1	-1.2	-0.3
Structural balance (percent of potential GDP)	-5.4	-5.5	-4.5	-3.8	-2.8	-2.4	-1.9	-1.6	-1.4	-0.9	-0.2
Primary balance	-4.9	-4.5	-2.6	-2.4	-2.1	-1.9	-1.3	-0.7	0.0	0.9	1.9
General government gross debt	78.0	80.8	84.4	88.7	91.8	94.3	95.1	95.0	94.0	92.0	89.1
Money and interest rates (in percent)											
Money market rate 1/	0.7	0.5	0.8	0.1	0.0	0.1	…	…	…	…	…
Government bond yield 1/	3.6	3.1	3.3	2.5	2.2	2.3	…	…	…	…	…
Balance of payments (in percent of GDP)											
Exports of goods	17.9	19.6	20.6	20.9	20.5	19.8	19.7	19.7	19.8	19.9	19.9
Volume growth (in percent)	-11.3	9.0	6.9	1.1	2.2	3.4	4.8	4.6	4.6	4.6	4.6
Imports of goods	20.1	22.3	24.3	24.3	23.5	22.8	22.2	21.9	21.8	21.7	21.5
Volume growth (in percent)	-9.4	8.9	6.3	-1.3	1.7	3.1	3.2	3.5	3.8	3.9	3.9
Trade balance	-2.2	-2.7	-3.7	-3.4	-2.9	-3.0	-2.5	-2.2	-2.0	-1.8	-1.6
Current account	-1.3	-1.3	-1.7	-2.1	-1.3	-1.5	-0.9	-0.5	-0.2	0.0	0.3
FDI (net)	-3.1	-1.2	-0.7	-0.5	0.3	0.0	-0.2	-0.4	-0.6	-0.8	-1.0
Official reserves (US$ billion)	46.6	55.8	48.6	54.2	50.8	…	…	…	…	…	…
Fund position (as of December 31, 2013)											
Holdings of currency (percent of quota)	80.8	79.7	73.1	69.6	74.2	…	…	…	…	…	…
Holdings of SDRs (percent of allocation)	95.9	96.1	95.5	93.6	90.6	…	…	…	…	…	…
Quota (SDRs million)	10739	10739	10739	10739	10739	…	…	…	…	…	…
Exchange rates											
Euro per U.S. dollar, period average	0.72	0.75	0.72	0.78	0.75	…	…	…	…	…	…
Nominal effective rate, ULC-styled (2000=100)	104.8	102.4	102.4	100.1	102.1	…	…	…	…	…	…
Real effective exchange rate, ULC-based (2000=100)	103.6	104.3	105.4	104.8	109.1	…	…	…	…	…	…
Potential output and output gap											
Potential output	1.1	0.9	0.9	0.9	1.0	1.0	1.1	1.2	1.3	1.4	1.5
Output gap	-3.1	-2.1	-0.9	-1.5	-2.2	-2.5	-2.2	-1.7	-1.1	-0.6	-0.2

Social indicators

Per capita GDP (2006): US$35,471; Life expectancy at birth (2009): 77.7 (male) and 84.4 (female);

Poverty rate (mid-2000s): 14.1 percent (60 percent line), 7.1 percent (50 percent line);

Income distribution (ratio of income received by top and bottom quintiles, 2004): 4.2.

Sources: French authorities; IMF staff estimates and projections.

1/ For 2014, January-March.

Table 2a. France: General Government Statement of Operations, 2009–19
(In percent of GDP, unless otherwise indicated)

						Projections					
	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	49.6	49.6	50.8	51.8	52.9	52.9	52.6	52.4	52.2	52.2	52.2
Tax revenue	41.9	42.1	43.2	44.3	45.3	45.3	45.0	44.8	44.6	44.6	44.5
Nontax revenue	7.7	7.6	7.6	7.5	7.6	7.6	7.6	7.6	7.6	7.6	7.6
Expenditure	56.8	56.4	55.9	56.7	57.2	56.9	55.9	55.1	54.3	53.4	52.4
Expense	54.3	54.3	53.9	54.6	56.6	56.5	55.5	54.7	53.9	52.9	52.0
Compensation of employees	13.1	13.0	12.8	12.8	12.9	12.8	12.6	12.3	12.1	11.8	11.5
Use of goods and services	5.1	5.1	5.1	5.1	5.2	5.1	5.0	4.9	4.7	4.6	4.4
Consumption of fixed capital	2.6	2.6	2.6	2.7	3.6	2.8	2.8	2.7	2.7	2.6	2.6
Interest	2.4	2.4	2.6	2.5	2.3	2.2	2.2	2.2	2.2	2.2	2.3
Subsidies	1.6	1.6	1.4	1.5	1.4	1.4	1.4	1.4	1.4	1.4	1.4
Grants	0.7	0.7	0.7	0.8	0.8	0.8	0.8	0.8	0.8	0.8	0.8
Social benefits	24.8	24.8	24.8	25.3	25.8	25.8	25.7	25.6	25.4	25.3	25.1
Other expense	3.7	3.7	3.6	3.9	4.5	5.4	4.9	4.8	4.5	4.2	4.0
Net acquisition of nonfinancial assets	0.9	0.6	0.5	0.4	0.6	0.4	0.4	0.4	0.4	0.4	0.4
Acquisitions of nonfinancial assets	...	...	...	...	...	...	...	...	...	...	...
Disposals of nonfinancial assets	...	...	...	...	...	...	...	...	...	...	...
Consumption of fixed capital	-2.6	-2.6	-2.6	-2.7	-3.6	-2.8	-2.8	-2.7	-2.7	-2.6	-2.6
Gross Operating Balance	-3.9	-3.8	-2.0	-1.6	-0.1	-0.8	-0.1	0.4	1.0	1.8	2.7
Net Operating Balance	-6.4	-6.3	-4.6	-4.3	-3.7	-3.6	-2.9	-2.3	-1.7	-0.8	0.1
Net lending (+)/borrowing (–)	-7.2	-6.8	-5.1	-4.9	-4.2	-4.0	-3.4	-2.7	-2.1	-1.2	-0.3
Net acquisition of financial assets	2.6	-0.9	1.6	2.5	...	...	...	...	...	...	...
Monetary gold and SDRs	0.0	0.0	0.0	0.0	...	...	...	...	...	...	...
Currency and deposits	0.9	-0.9	0.8	-0.3	...	...	...	...	...	...	...
Debt securities	-0.3	0.1	0.0	-0.2	...	...	...	...	...	...	...
Loans	0.4	0.1	0.3	1.3	...	...	...	...	...	...	...
Equity and investment fund shares	0.6	-0.5	-0.2	1.0	...	...	...	...	...	...	...
Insurance, pensions, and standardized guarantee schemes	0.0	0.0	0.0	0.0	...	...	...	...	...	...	...
Financial derivatives and employee stock options	0.0	0.0	0.0	0.0	...	...	...	...	...	...	...
Other accounts receivable	1.0	0.2	0.7	0.6	...	...	...	...	...	...	...
Net incurrence of liabilities	9.9	5.9	6.6	7.2	...	...	...	...	...	...	...
SDRs	0.0	0.0	0.0	0.0	...	...	...	...	...	...	...
Currency and deposits	-0.1	0.0	0.3	0.4	...	...	...	...	...	...	...
Debt securities	8.5	4.6	5.9	3.9	...	...	...	...	...	...	...
Loans	1.0	0.9	-0.4	1.7	...	...	...	...	...	...	...
Equity and investment fund shares	0.0	0.0	0.0	0.0	...	...	...	...	...	...	...
Insurance, pensions, and standardized guarantee schemes	0.0	0.0	0.0	0.0	...	...	...	...	...	...	...
Financial derivatives and employee stock options	0.0	0.0	0.0	0.0	...	...	...	...	...	...	...
Other accounts payable	0.6	0.4	0.7	1.2	...	...	...	...	...	...	...
Memorandum items:											
Structural balance	-5.5	-5.7	-4.6	-3.8	-2.9	-2.5	-1.9	-1.6	-1.4	-0.9	-0.2
Structural balance (in percent of potential GDP)	-5.4	-5.5	-4.5	-3.8	-2.8	-2.4	-1.9	-1.6	-1.4	-0.9	-0.2
Structural primary balance 1/	-3.4	-3.5	-2.2	-1.7	-1.0	-0.7	-0.2	0.2	0.6	1.2	2.0
Central government net lending/borrowing	-6.0	-6.1	-4.4	-3.9	-3.3	-3.2	-3.1	-2.6	-2.1	-1.3	-0.5
General government Maastricht balance	-7.2	-6.8	-5.1	-4.9	-4.2	-4.0	-3.4	-2.7	-2.1	-1.2	-0.3
Gross debt (Maastricht definition)	78.0	80.8	84.4	88.7	91.8	94.3	95.1	95.0	94.0	92.0	89.1

Source: GFS yearbook, INSEE, French authorities, and IMF staff estimates and projections.
1/ Excludes cyclical effects.

Table 2b. France: General Government Integrated Balance Sheet, 2003–12

(In percent of GDP)

	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
STOCK POSITIONS:										
Net worth	...	...	...	...	...	...	...	...	...	...
Nonfinancial assets	...	...	...	...	...	...	...	...	...	...
Net financial worth	-45.2	-45.9	-44.0	-38.1	-34.6	-44.4	-50.6	-55.5	-61.0	-68.4
Financial assets	27.8	28.8	32.5	33.6	36.1	32.3	38.1	37.0	35.9	37.9
Monetary gold and SDRs	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Currency and deposits	3.2	3.4	3.1	1.3	1.3	2.1	3.1	2.2	2.9	2.6
Debt securities	1.5	1.3	1.3	1.6	1.8	2.5	2.4	2.4	2.3	2.0
Loans	2.1	2.1	1.9	1.7	1.6	1.5	1.8	1.9	2.2	3.5
Equity and investment fund shares	13.1	14.9	18.7	21.4	23.5	18.2	21.3	21.1	18.7	20.0
Insurance, pensions, and standardized	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Financial derivatives and employee stock	0.0	0.0	0.0	0.0	0.0	0.1	0.1	0.1	0.1	0.1
Other accounts receivable	7.9	7.0	7.5	7.5	7.9	7.9	9.2	9.2	9.6	9.6
Liabilities	72.9	74.6	76.5	71.7	70.8	76.7	88.7	92.5	96.9	106.3
Monetary gold and SDRs	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Currency and deposits	1.0	0.9	0.9	1.1	1.2	1.3	1.2	1.2	1.5	1.8
Debt securities	54.6	57.6	59.4	54.5	52.9	58.8	69.2	72.2	76.6	83.3
Loans	9.7	9.5	9.6	9.4	9.7	9.5	10.7	11.3	10.5	12.0
Equity and investment fund shares	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Insurance, pensions, and standardized	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financial derivatives and employee stock	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other accounts payable	7.7	6.6	6.6	6.7	7.1	7.0	7.6	7.8	8.3	9.1
Memorandum items:										
Debt (at market value)	72.9	74.6	76.5	71.7	70.8	76.7	88.7	92.5	96.8	106.3
Debt at face value	69.0	69.6	71.2	68.8	69.3	73.1	84.6	87.6	91.6	96.8
Maastricht debt	62.6	64.3	65.9	63.2	63.2	67.0	78.0	80.8	84.4	88.7
OTHER ECONOMIC FLOWS:										
Change in net worth from other flows	...	...	...	...	...	...	...	...	...	...
Nonfinancial assets	...	...	...	...	...	...	...	...	...	...
Net financial worth	0.7	0.9	3.2	6.2	4.4	-7.4	2.4	0.5	-2.1	-4.0
Financial assets	0.5	2.0	3.6	4.1	3.3	-4.9	2.3	0.9	-1.6	0.1
Monetary gold and SDRs	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Currency and deposits	0.0	0.1	-0.1	0.0	0.0	0.0	0.2	0.0	0.0	0.0
Debt securities	0.1	-0.1	0.0	0.0	0.0	0.1	0.1	0.0	0.0	0.2
Loans	-0.3	0.0	-0.1	0.0	0.0	0.0	-0.1	0.0	0.0	0.0
Equity and investment fund shares	0.7	2.1	3.8	4.2	3.2	-5.0	2.0	0.9	-1.6	0.0
Insurance, pensions, and standardized	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financial derivatives and employee stock	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other accounts receivable	0.0	0.0	0.0	0.0	0.1	0.0	0.1	0.1	0.0	-0.1
Liabilities	-0.2	1.1	0.5	-2.1	-1.0	2.5	-0.1	0.5	0.5	4.1
Monetary gold and SDRs	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Currency and deposits	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Debt securities	-0.2	1.1	0.3	-2.1	-1.1	2.4	0.1	0.4	0.5	4.0
Loans	0.0	0.1	0.2	-0.1	-0.1	0.0	0.0	0.0	0.0	0.0
Equity and investment fund shares	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Insurance, pensions, and standardized	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financial derivatives and employee stock	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other accounts payable	0.0	0.0	0.0	0.0	0.1	0.1	-0.2	0.0	0.0	0.1

Source: GFS yearbook.

Table 2c. France: General Government Accounts, 2009–19
(In percent of GDP, unless otherwise indicated)

						Projections					
	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
General government											
Revenue	49.6	49.6	50.8	51.8	52.9	52.9	52.6	52.4	52.2	52.2	52.2
Tax revenue	41.9	42.1	43.2	44.3	45.3	45.3	45.0	44.8	44.6	44.6	44.5
Nontax revenue	7.7	7.6	7.6	7.5	7.6	7.6	7.6	7.6	7.6	7.6	7.6
Expenditures	56.8	56.4	55.9	56.7	57.2	56.9	55.9	55.1	54.3	53.4	52.4
Primary exp.	54.4	54.1	53.3	54.1	54.9	54.7	53.7	52.9	52.1	51.1	50.2
Debt service	2.4	2.4	2.6	2.5	2.3	2.2	2.2	2.2	2.2	2.2	2.3
Balance 1/	-7.2	-6.8	-5.1	-4.9	-4.2	-4.0	-3.4	-2.7	-2.1	-1.2	-0.3
Primary balance	-4.9	-4.5	-2.6	-2.4	-2.1	-1.9	-1.3	-0.7	0.0	0.9	1.9
Structural balance 2/	-5.4	-5.5	-4.5	-3.8	-2.8	-2.4	-1.9	-1.6	-1.4	-0.9	-0.2
Central government balance 1/	-6.0	-6.1	-4.4	-3.9	-3.3	-3.2	-3.1	-2.6	-2.1	-1.3	-0.5
Social security balance 1/	-0.7	-1.2	-0.6	-0.6	-0.6	-0.4	0.1	0.1	0.1	0.2	0.2
Local government balance 1/	-0.3	-0.1	0.0	-0.2	-0.4	-0.5	-0.3	-0.3	-0.2	-0.1	-0.1
ODAC balance 1/	-0.1	0.5	0.0	-0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Gross debt 3/	78.0	80.8	84.4	88.7	91.8	94.3	95.1	95.0	94.0	92.0	89.1
Memorandum items:											
Nominal GDP (in billion of Euros)	1,939	1,998	2,059	2,091	2,114	2,156	2,215	2,284	2,359	2,442	2,530
Potential nominal GDP (in billion of Euros)	2,001	2,041	2,078	2,123	2,160	2,210	2,264	2,323	2,387	2,457	2,534
Real GDP growth (in percent)	-2.9	2.0	2.1	0.3	0.3	0.7	1.4	1.7	1.8	1.9	1.9
Real expenditure growth (in percent)	4.0	0.7	-0.2	0.7	0.9	0.5	-0.2	0.3	0.3	0.2	0.2
of which: primary	5.2	0.8	-0.7	0.9	1.5	0.6	-0.3	0.3	0.2	0.0	0.1
of which: structural primary	4.5	0.6	-0.5	0.8	1.1	0.9	-1.1	0.8	0.0	0.1	0.1

Sources: French authorities; IMF staff estimates and projections.

1/ Maastricht definition.
2/ In percent of potential GDP.
3/ The debt figure, based on Maastricht definition, does not include guarantees on nongeneral government debt.

Table 3. France: Balance of Payments, 2011–19

(In percent of GDP)

	2011	2012	2013	2014	2015	2016	2017	2018	2019
						Projections			
Current account	-1.7	-2.1	-1.3	-1.5	-0.9	-0.5	-0.2	0.0	0.3
Net exports of goods	-3.7	-3.4	-2.9	-3.0	-2.5	-2.2	-2.0	-1.8	-1.6
Exports of goods	20.6	20.9	20.5	19.8	19.7	19.7	19.8	19.9	19.9
Imports of goods	-24.3	-24.3	-23.5	-22.8	-22.2	-21.9	-21.8	-21.7	-21.5
Net exports of services	1.5	1.6	1.7	1.7	1.8	1.9	2.0	2.1	2.1
Exports of services	8.2	8.0	8.4	8.3	8.3	8.3	8.3	8.4	8.4
Imports of services	-6.7	-6.5	-6.7	-6.6	-6.5	-6.4	-6.3	-6.3	-6.3
Income balance	1.5	0.7	1.0	1.0	0.9	0.9	0.9	0.8	0.8
Current transfers	-1.7	-1.7	-1.8	-1.8	-1.8	-1.8	-1.8	-1.8	-1.8
Capital and financial account									
Capital account	0.0	0.0	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Financial account	2.6	3.5	1.2	1.4	0.8	0.4	0.1	-0.1	-0.3
Direct investment	-0.7	-0.5	0.3	0.0	-0.2	-0.4	-0.6	-0.8	-1.0
Portfolio investment	11.1	1.9	4.7	6.1	5.4	5.0	4.6	4.2	3.9
Debt securities	2.5	2.6	2.7	2.8	2.8	2.8	2.7	2.7	2.6
Other investment	-8.7	1.6	-5.0	-4.8	-4.5	-4.1	-3.8	-3.5	-3.3
Reserve assets	0.3	-0.2	0.1	0.0	0.0	0.0	0.0	0.0	0.0
Errors and omissions	-0.9	-1.4	0.5	0.0	0.0	0.0	0.0	0.0	0.0

Source: IMF, Balance of Payments Statistics; and Direction Générale des Douanes et Droits Indirects for goods exports and imports.

Table 4. France: Vulnerability Indicators, 2006–12

(In percent of GDP; unless otherwise indicated)

	2006	2007	2008	2009	2010	2011	2012	Est. 2013
External Indicators								
Exports (annual percentage change, in U.S. dollars)	9.1	13.7	10.5	-12.5	6.3	15.3	-5.7	4.3
Imports (annual percentage change, in U.S. dollars)	14.2	15.4	15.5	-33.1	12.1	17.0	-5.2	-3.6
Terms of trade (annual percentage change)	-1.5	1.2	-0.6	2.6	-1.4	-2.4	-0.3	1.2
Current account balance	-0.6	-1.0	-1.7	-1.3	-1.3	-1.7	-2.1	-1.3
Capital and financial account balance	1.4	1.7	0.9	1.2	1.3	2.6	3.5	1.3
Of which								
Inward portfolio investment (debt securities, etc.)	8.2	4.4	6.2	16.2	4.3	3.0	1.6	7.1
Inward foreign direct investment	3.1	3.6	2.2	0.9	1.3	1.3	0.9	0.2
Other investment (net)	9.2	8.2	3.2	-7.6	-4.5	-8.7	1.6	-5.0
Total reserves minus gold								
(in billions of U.S. dollars, end-of-period)	42.7	45.7	33.6	46.6	55.8	48.6	54.2	50.8
Euros per U.S. dollar (period average)	0.8	0.7	0.7	0.7	0.8	0.7	0.8	0.8
Market Indicators								
Financial Markets								
Public sector debt 1/	63.2	63.2	67.0	78.0	80.8	84.4	88.7	91.8
3-month T-bill yield (percentage points, eop)	3.5	3.8	1.9	0.4	0.5	0.1	0.1	0.1
3-month T-bill yield in real terms (percentage points, eop)	2.0	1.3	0.9	-0.5	-1.3	-2.2	-1.3	-0.6
US 3 month T-bill	4.8	3.1	0.0	0.1	0.2	0.0	0.1	0.1
Spread with the US T-bill (percentage points, eop)	-1.4	0.7	1.9	0.3	0.3	0.1	0.0	0.1
5- to 8-year government bond (percentage points, eop)	3.8	4.4	3.5	3.5	3.3	3.2	2.0	2.3
10-year government bond (United States)	4.6	4.1	2.4	3.6	3.3	2.0	1.7	2.9
Spread with US bond (percentage points, eop)	-0.8	0.3	1.1	-0.1	0.1	1.2	0.3	-0.6
Yield curve (10 year - 3 month, percentage points, eop)	0.3	0.5	1.6	3.1	2.8	3.0	1.9	2.2
Stock market index (period average, 1995=100)	273.1	306.2	232.0	178.6	200.3	192.1	179.0	211.1
Real estate prices (index, Q1-10=100, period average)	98.6	105.1	106.0	98.5	103.5	109.7	109.1	106.8
Credit markets (end-of-period 12-month growth rates)								
Credit to the private sector	11.0	13.4	6.2	-0.7	5.6	4.4	2.0	0.5
Bank credit to households	11.4	10.7	5.7	2.9	6.0	5.8	2.1	2.4
Housing Loans	15.1	12.8	7.5	3.7	8.2	6.2	3.0	4.0
Bank credit to nonfinancial enterprises	9.7	14.1	10.6	-2.1	1.4	4.7	-0.2	-1.1
Sectoral risk indicators								
Household sector								
Household savings ratio	14.6	15.1	15.0	16.2	15.8	15.6	15.2	15.1
Household financial savings ratio	4.0	4.4	4.2	7.1	6.5	6.1	5.6	5.8
Real estate household solvency ratio (index, 2001=100) 2/	97	97	101	102.0	99.4	100.9	98.2	98.5
Corporate sector								
Profitability of business sector (financial margin)	39.4	40.0	39.5	37.3	37.9	37.4	36.8	36.0
Investment ratio	19.8	20.9	21.6	20.0	20.4	21.0	21.0	20.9
Savings ratio	18.4	19.4	16.8	16.7	18.9	18.2	17.3	17.0
Self-financing ratio	85.4	85.8	72.1	77.7	85.6	80.3	76.3	75.5
Banking sector								
Share of housing loans in bank credit to the private sector	37.3	37.1	37.6	39.2	40.2	40.8	41.2	42.6
Share of nonperforming loans in total loans	3.0	2.7	2.8	4.0	3.8	4.3	4.4	0.0
Ratio of nonperforming loans net of provisions to capital	6.8	6.6	10.3	19.3	17.2	20.8	19.4	0.0
Liquid assets to total short-term liabilities	146.7	150.3	128.3	93.1	76.2	87.6	91.4	0.0
Return on assets	0.6	0.4	0.1	0.3	0.6	0.4	0.3	0.0
Return on equity	14.0	9.8	3.6	7.2	12.0	8.3	9.8	0.0
Regulatory capital to risk-weighted assets	10.9	10.2	10.5	12.4	12.7	12.3	14.3	0.0

Sources: French authorities; INSEE; BdF; ECB; Haver; Credit Logement; IMF, International Financial Statistics; and Bloomberg.

1/ The debt figure does not include guarantees on non-general government debt.

2/ This index combines the effect of real disposable income, repayment conditions for loans, real estate prices, and interest subsidies.

Table 5. France: Core Financial Soundness Indicators, 2006–13

	2006	2007	2008	2009	2010	2011	2012	Estimate 2013
Deposit-taking institutions 1/								
Regulatory capital to risk-weighted assets 2/	10.9	10.2	10.5	12.4	12.5	12.2	14.0	15.1
Regulatory Tier I capital to risk-weighted assets 2/	8.2	7.7	8.5	10.2	10.7	10.9	13.3	13.2
Nonperforming loans net of provisions to capital 3/	6.8	6.6	8.2	10.8	10.0	9.2	10.7	11.5
Bank provisions to nonperforming loans 3/	170	158.3	131.0	109.5	112.0	115.3	106.7	106.7
Nonperforming loans to total gross loans 3/	3.0	2.7	2.8	3.6	3.5	3.5	4.0	4.5
Sectoral distribution of loans to total loans, *of which*								
Deposit-takers 3/	30.6	32.2	33.6	5.0	36.5	40.2	40.7	39.2
Nonfinancial corporation 3/	18.6	18.1	18.3	17.5	20.5	19.2	18.8	19.0
Households (including individual firms) 3/	26.6	24.8	24.1	24.5	30.5	28.7	28.9	30.3
Nonresidents (including financial sectors) 3/	4.2	4.7	4.7	4.6	6.1	5.9	5.6	5.4
ROA (aggregated data on a parent-company basis) 3/	0.6	0.4	0.0	0.4	0.3	0.0	0.2	0.4
ROA (main groups on a consolidated basis) 2/	0.57	0.35	0.1	0.3	0.6	0.4	0.3	0.5
ROE (aggregated data on a parent-company basis) 3/	14.0	9.8	-1.0	8.2	7.9	1.2	5.5	10.1
ROE (main groups on a consolidated basis) 2/	17.2	13.3	3.8	6.4	11.8	8.2	6.6	8.1
Interest margin to gross income 3/	28.2	25.3	40.4	34.9	49.4	51.5	41.4	44.0
Noninterest expenses to gross income 3/	62.4	68.4	84.2	63.1	65.7	67.4	63.2	66.6
Liquid assets to total assets 3/	19.9	18.9	18.3	18.3	23.0	24.1	26.2	30.5
Liquid assets to short-term liabilities 3/	146.7	150.3	139.6	150.1	144.4	136.3	164.0	165.2

Sources: Banque de France, ACPR

1/ These may be grouped in different peer groups based on control, business lines, or group structure.
2/ Consolidated data for the seven main banking groups (2005, IFRS).
3/ All credit institutions' aggregated data on a parent-company basis.

Table 6. France: Encouraged Financial Soundness Indicators 2006–13
(In percent, unless otherwise indicated)

	2006	2007	2008	2009	2010	2011	2012	Estimate 2013
Corporate sector								
Total debt to equity	59.3	55.1	87.6	78.5	76.6	84.5	80.9	72.2
Return on equity	8.9	8.6	12.3	8.3	8.5	8.5	7.4	6.7
Interest paid to financial firms 1/	9.7	11.5	13.7	9.9	8.8	10.1	n.a.	n.a.
Corporate net foreign exchange exposure to equity	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Number of enterprise bankruptcies (thousands)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Number of enterprise creations (thousands)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Deposit-taking institutions								
Capital (net worth) to assets	4.5	4.1	4.2	4.5	4.6	5.5	4.8	4.7
International consolidated claims of French banks, *of which* (BIS data, as percent of total international claims)								
Advanced countries	85.1	84.0	84.2	83.3	79.8	79.4	78.0	78.7
Developing Europe	3.2	4.0	4.3	4.6	5.7	6.0	7.1	7.1
Latin America and Caribbean	0.9	1.0	1.1	1.2	1.4	1.4	1.5	1.4
Africa and Middle East	2.6	2.6	3.1	3.5	4.4	5.1	5.2	4.3
Asia and Pacific Area	2.5	2.9	2.6	2.9	4.0	3.6	4.1	4.3
Offshore Financial Centers	5.6	5.5	4.7	4.4	4.7	4.6	4.1	4.2
Gross asset position in financial derivatives to capital	337.0	235.0	633.2	362.7	286.2	388.8	346.2	205.8
Gross liability position in financial derivatives to capital	293.0	227.0	616.3	361.9	286.7	388.0	346.0	206.8
Large exposures to capital	1.4	4.7	3.1	4.1	14.1	26.9	7.6	6.9
Trading income to total income	26.0	16.8	-63.9	16.4	10.3	-13.2	6.4	11.0
Personnel expenses to noninterest expenses	54.0	53.3	51.6	61.1	44.9	42.1	36.0	27.2
Spread between reference lending and deposit rates	226	232	218	237	246	227	219	216
Spread between highest and lowest interbank rate	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Customer deposits to total (noninterbank) loans	80.5	77.4	78.0	85.3	79.5	78.4	67.9	92.6
FX loans to total loans 2/	11.4	11.3	10.5	10.4	9.8	8.9	8.4	7.6
FX liabilities to total liabilities	18.6	18.1	16.8	15.3	16.4	15.4	13.9	14.3
Net open position in equities to capital	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Market liquidity								
Average bid-ask spread in the securities market 3/	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Average daily turnover ratio in the securities market	7.0	7.7	5.4	3.4	4.3	n.a.	n.a.	n.a.
Other financial corporations								
Assets to total financial system assets	20.9	20.6	19.7	20.5	20.4	19.0	19.8	19.7
Assets to GDP	201.3	211.1	191.8	210.7	212.4	199.2	211.5	214.7
Households								
Household debt to GDP	44.6	47.1	49.3	53.1	54.6	55.6	55.9	56.3
Household debt service and principal payments to income	14.5	12.1	11.7	12.3	13.2	12.9	12.3	12.7
Real estate markets								
Real estate prices (in percent change)	10.0	5.5	-3.8	-4.2	7.6	3.8	-2.1	-1.4

Sources: Banque de France ; ACPR ; BIS ; Ministère des Finances

1/ In percent of financial firms' gross operating surplus.
2/ Data cover interbank and customer lending to residents and nonresidents on a metropolitan basis.
3/ Or in other markets that are most relevant to bank liquidity, such as foreign exchange markets.

Appendix I. Main Recommendations of the 2013 Article IV Consultation and Authorities' Actions

Fund Recommendations	Policy Actions
Fiscal Policy	
"Many Directors saw merit in allowing for a smoother pace of adjustment than envisaged in the [2013] Stability Program to support the hesitant recovery. Many other Directors advised the authorities to persevere with the consolidation plans under the program, noting that it already allows automatic stabilizers to operate. While Directors welcomed the shift to structural deficit targeting, a number of them noted that nominal targets should not be neglected."	In the face of another growth shortfall and weakening revenue performance, the deficit targets set in the 2013 Stability Program were missed: by 0.5 percent of GDP in 2013 and by a projected 0.8 percent of GDP in 2014 (authorities' projections).
Rebalance fiscal adjustment toward expenditure containment, including in the areas of social security and local spending	Rebalancing is taking place: expenditure measures accounted for 35 percent of structural adjustment in 2013, and an expected 86 percent in 2014.
Financial Sector Policy	
Better align tax incentives on financial products with regulatory objectives, including by removing tax disincentives against deposits and phasing out regulated interest rates.	The 2013 reform rebalanced tax incentives provided to life insurance savings toward equity investments in SMEs. No other reform is being considered, as banks do not presently appear constrained in their ability to provide credit.
Structural Reforms	
Reform pensions in a way that increases labor market participation rather than contribution rates.	The pension reform of 2013 relied in the short term on higher contribution rates, and starting in 2020 on lengthening the contribution period to reach full pension
Pursue deeper labor market reforms to increase employment of the young and low-skilled	Subsidized job programs were increased with a target of 340,000 new hires in 2014; apprenticeship and work-study programs were also expanded.
Open the product and services markets to greater competition.	The following sectors were opened to greater competition: pregnancy tests, prescription eye-glasses, auto insurance, and veterinary services. The consumer law of March 2014 opens the door to collective action.

Source: IMF Staff.

Appendix II. France: Public Debt Sustainability Analysis

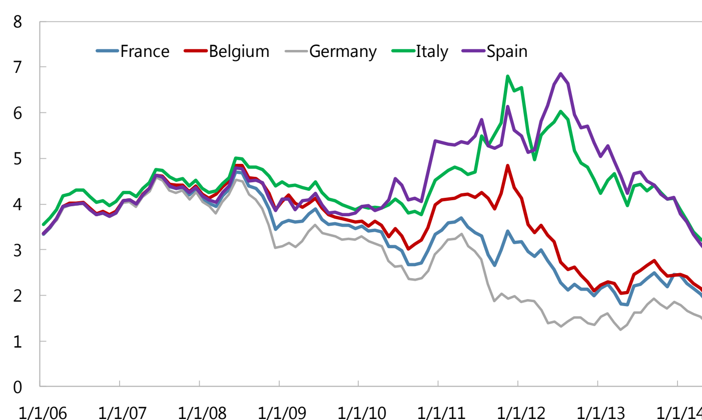
Under the baseline scenario, the debt-to-GDP ratio is projected to peak at 95.1 percent in 2015 and to decline to 89.1 percent by 2019 as economic recovery gains traction and the primary balance shifts to a surplus starting in 2018. Due to the maturity structure of the French debt, gross financing needs would increase substantially in 2015, to 12.3 percent of GDP, but decline thereafter. The debt ratio would be bumped up significantly in the event of protracted stagnation. The impact of lower fiscal consolidation and higher interest rate remains comparatively more limited. None of the standard stress tests would result in unsustainable debt dynamics.

Background. The combined effect of low growth over several years and the persistence of high fiscal deficits, augmented by the fiscal stimulus of 2009, have increased the debt-to-GDP ratio by almost 29 percentage points in six years to 91.8 percent in 2013. Despite ongoing fiscal consolidation, the debt ratio is projected to continue to increase in the short term peaking at 95.1 percent of GDP in 2015 and decline thereafter.

Currently, yields on French debt are at historically low levels. The benchmark yield (10 years) has declined from 4.7 percent in June 2008 to 1.85 percent in May 2014. The spreads over German Bunds, which had increased to almost 190 basis points in November 2011, were back to 40 basis points early-June 2014.

10 Year Sovereign Yields

(In Percent)



Source: Thomson Financial/Datastream.

Owing to the sharp decline in interest rates, the rising debt has had a limited impact on the debt service. Interest payments were at the historically low level of 2.3 percent of GDP in 2013.[1]

Baseline. Staff projects that the debt-to-GDP ratio will peak at 95.1 percent in 2015 and then decline to 89.1 percent in 2019. Interest payments would remain low averaging 2.2 of GDP during the projection period because: (1) fiscal consolidation leads to a primary surplus starting in 2017; (2) interest rates are expected to increase slightly during the projection period; and (3) given the maturity structure of the debt (average maturity of 7 years as of end March 2014), the expected small increase of interest rates starting in 2014 has a slow pass-through to implicit interest rate and the budget.

[1] The drop in inflation also lowered the 2013 debt service as part of the French debt is indexed to inflation.

- **Macroeconomic assumptions.** Recent growth performance has been affected by the weak external environment and the drag caused by structural fiscal adjustment of 2.8 percent of potential GDP over three years (2011-13). After two years of quasi stagnation, the economy should grow by 0.7 percent in 2014. The growth rate is expected to rise steadily to 1.9 percent in the end of the projection period, with the output gap almost closed in 2019.

- **Fiscal outlook.** The pace of structural adjustment is expected to slow from 0.9 percentage point per year in the past three years to about ½ a percentage point per year during 2014-19. Structural balance would be almost reached by the end of the projection period. Primary balance would shift to a surplus in 2018 and would be above its debt-stabilizing level starting in 2016. The constant primary balance scenario at its projected 2014 level should be seen as a tail risk triggered by a more widespread crisis in Europe.

- **Debt levels and gross financing needs.** France's high level of debt calls for using the higher scrutiny framework.[2] The gross financing need, despite the expected increase in 2015, remains below the threshold. Part of the increase in the debt ratio reflects financial support to other Euro area countries which grew from 0.2 percent of GDP in 2010 to 3.1 percent of GDP in 2013.[3] This support is expected to increase to 3.2 percent of GDP by 2014 before declining.

Realism of Projections. The median forecast error for real GDP growth during 2005-13 is -0.82 percent suggesting there is a slight upward bias in the staff projections. The median forecast bias for inflation stands at -0.01 percent suggesting that staff projected inflation accurately. At 0.08 percent, the median forecast error for primary balance is small and staff projections have been slightly conservative.

The projected fiscal adjustment appears feasible. The reduction in the cyclically-adjusted primary balance would average 0.6 percent per year during the projection period. This is smaller than the averaged 0.9 percent reduction per year achieved during 2011-13. Cross-country experience also suggests that fiscal adjustment projections are realistic. The projected adjustment and level of the CAPB are below the thresholds that would cast doubt on the feasibility of the adjustment, based on high debt country experience.[4]

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[2] The peak in the gross financing needs 2015 is in part triggered by the amortization of the large amount of debt issued at the beginning of the crisis. For advanced economies that (i) have a current or projected debt-to-GDP ratio above 60 percent; or (ii) have current or projected gross financing needs-to-GDP ratio above 15 percent; or (iii) have or are seeking exceptional access to Fund resources; staff uses an extended set of tools to identify and assess specific risks to debt sustainability. For these "higher scrutiny" cases, staff produces a standardized summary of risks in a heat map and prepares a write-up to discuss risks, including any country-specific considerations.

[3] Bilateral loans (direct and through the EFSF to Greece, Ireland, and Portugal) and contributions to the ESM increased from 0.2 percent of GDP in 2010 to 3.1 percent of GDP in 2013.

[4] More specifically, at 2.3 percent of GDP, the largest projected adjustment over any three years during the projection is below the threshold of 3 percent of GDP. In addition, the maximum average level of the cyclically-

(continued)

Heat map. Risks levels from the debt level are deemed high given that the relevant threshold to which France's values are compared is 85 percent and this threshold is breached under baseline and all stress test scenarios. In contrast, France's gross financing needs remain below the benchmark of 20 percent of GDP in the baseline and all stress test scenarios. The debt profile remains below relevant thresholds except for the share of public debt held by foreigners. Following a steady decline from mid-2010 when foreigners held 70.6 percent of French debt, that share has been increasing in 2013 and reaches 65.1 percent.

Shocks and Stress Tests. The DSA framework suggests that France's government debt-to-GDP ratio remains below 105 percent and its gross financing needs remain below 16 percent of GDP under different macroeconomic and fiscal shocks.

- **Growth shock**. Under this scenario, real output growth rates are lower by one standard deviation over 2015-2016, i.e., 1.7 percentage points relative to the baseline scenario. The assumed decline in growth leads to lower inflation (0.25 percentage points per 1 percentage point decrease in GDP growth) and the interest rate is assumed to increase 25 basis points for every 1 percent of GDP worsening of primary balance. Under this scenario, the debt-to-GDP ratio would increase to almost 103 percent of GDP in 2016 and declines thereafter.

- **Primary balance shock**. This scenario examines the implications of a dual shock of lower revenues and rise in interest rate, leading to a cumulative 2.0 percent deterioration in the primary balance over 2015-2019. Under this scenario, the debt-to-GDP ratio would increase to 95.6 percent of GDP in 2015 and declines thereafter.

- **Interest rate shock**. This scenario assumes an increase of 238 basis points increase in the cost of debt throughout the projection period. The deterioration of public debt and gross financing needs are back-loaded as old debt gradually matures and new higher interest rate debt is contracted. In 2019, the impact on the gross financing needs is 1 percent of GDP and 2 percentage points for the debt-to-GDP ratio.

- **Real exchange rate shock**. This scenario assumes 13 percent devaluation of the real exchange rate in 2015 and examines the impact on debt through the inflation channel. Under this scenario, the debt-to-GDP ratio would be marginally smaller (0.4 percentage point) than in the baseline.

- **Combined macro-fiscal shock**. This scenario aggregates shocks to real growth, the interest rate, the exchange rate, and the primary balance while taking care not to double-count the effects of individual shocks. Under this scenario, debt would reach almost 103 percent of GDP in 2016 and decline to 100 percent of GDP in 2019. The gross financing needs would

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adjusted primary deficit for any consecutive 3-year period during the projection horizon reaches is 2.94 percent of GDP, well below the threshold of 3.5 percent of GDP.

peak at 14.9 percent of GDP in 2016, which remains below the 20 percent benchmark considered by the heat map.

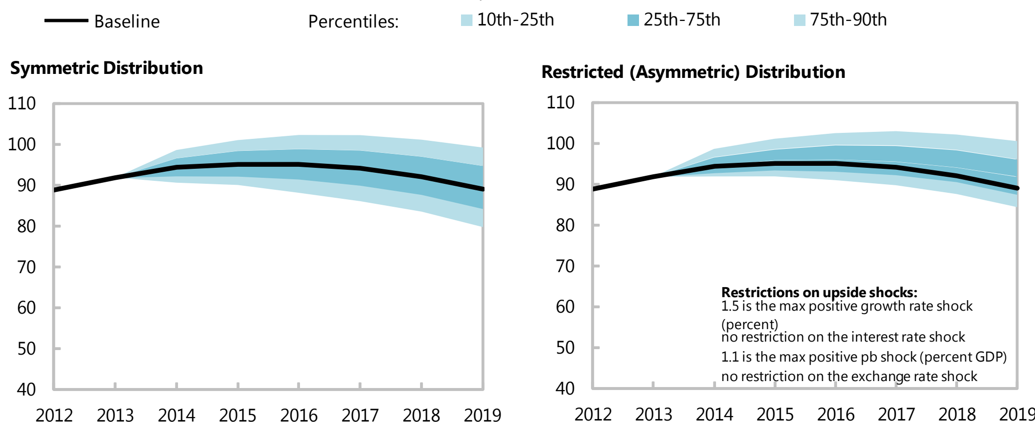
France Public DSA Risk Assessment

Heat Map

Debt level [1/]	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability shock
Gross financing needs [2/]	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability Shock
Debt profile [3/]	Market Perception	External Financing Requirements	Change in the Share of Short-Term Debt	Public Debt Held by Non-Residents	Foreign Currency Debt

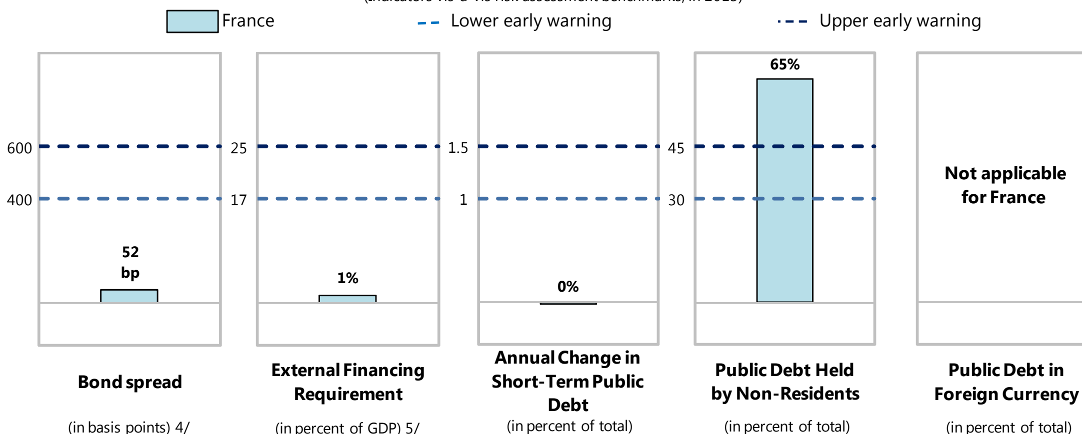
Evolution of Predictive Densities of Gross Nominal Public Debt

(in percent of GDP)



Debt Profile Vulnerabilities

(Indicators vis-à-vis risk assessment benchmarks, in 2013)



Source: IMF staff.

1/ The cell is highlighted in green if debt burden benchmark of 85% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

2/ The cell is highlighted in green if gross financing needs benchmark of 20% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

3/ The cell is highlighted in green if country value is less than the lower risk-assessment benchmark, red if country value exceeds the upper risk-assessment benchmark, yellow if country value is between the lower and upper risk-assessment benchmarks. If data are unavailable or indicator is not relevant, cell is white.
Lower and upper risk-assessment benchmarks are:

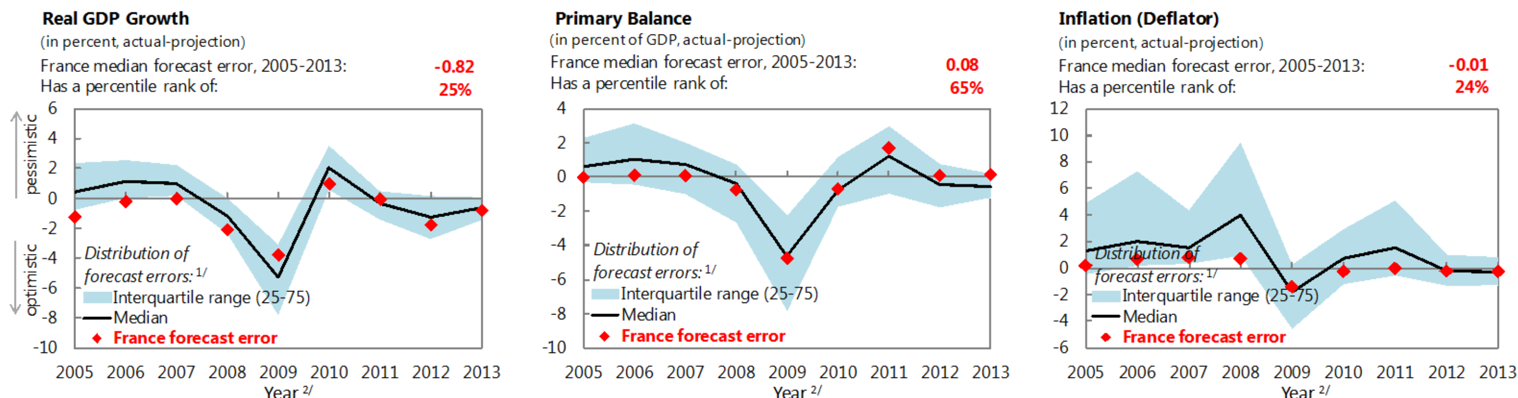
400 and 600 basis points for bond spreads; 17 and 25 percent of GDP for external financing requirement; 1 and 1.5 percent for change in the share of short-term debt; 30 and 45 percent for the public debt held by non-residents.

4/ Long-term bond spread over German bonds, an average over the last 3 months, 13-Feb-14 through 14-May-14.

5/ External financing requirement is defined as the sum of current account deficit, amortization of medium and long-term total external debt, and short-term total external debt at the end of previous period.

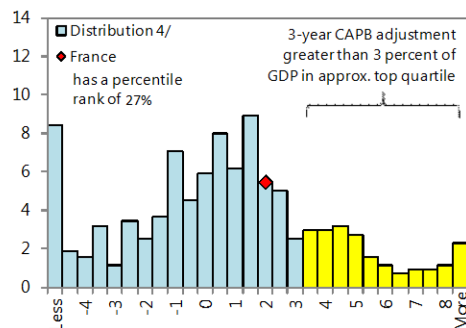
France Public DSA – Realism of Baseline Assumptions

Forecast Track Record, versus surveillance countries

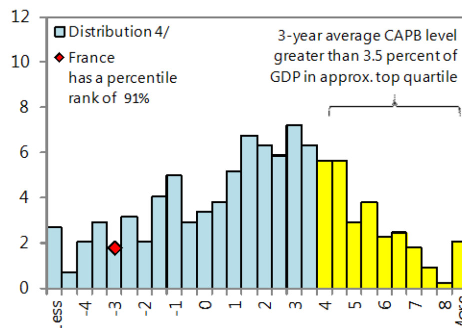


Assessing the Realism of Projected Fiscal Adjustment

3-Year Adjustment in Cyclically-Adjusted Primary Balance (CAPB)
(Percent of GDP)

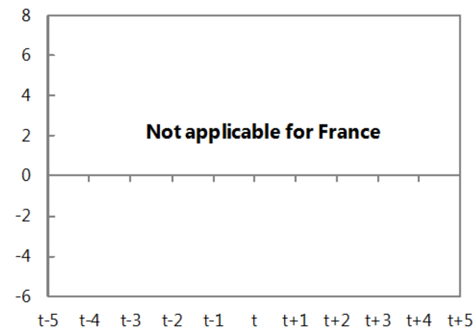


3-Year Average Level of Cyclically-Adjusted Primary Balance (CAPB)
(Percent of GDP)



Boom-Bust Analysis [3/]

Real GDP growth
(in percent)



Source : IMF Staff.

1/ Plotted distribution includes surveillance countries, percentile rank refers to all countries.

2/ Projections made in the spring WEO vintage of the preceding year.

3/ Not applicable for France, as it meets neither the positive output gap criterion nor the private credit growth criterion.

4/ Data cover annual obervations from 1990 to 2011 for advanced and emerging economies with debt greater than 60 percent of GDP. Percent of sample on vertical axis.

France Public Sector Debt Sustainability Analysis (DSA) - Baseline Scenario

(in percent of GDP unless otherwise indicated)

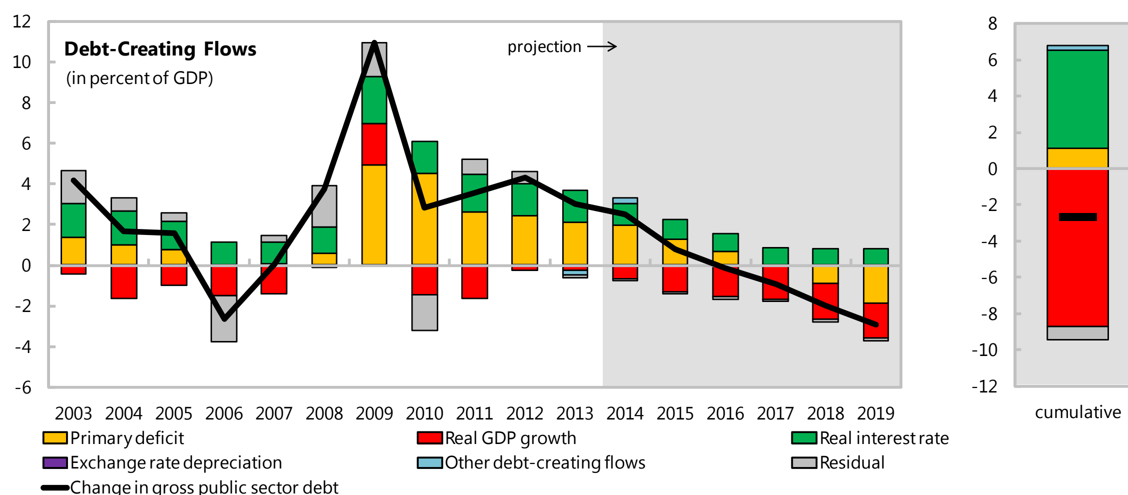
Debt, Economic and Market Indicators [1/]

	Actual			Projections					
	2003-2011 [2/]	2012	2013	2014	2015	2016	2017	2018	2019
Nominal gross public debt	69.9	88.7	91.8	94.3	95.1	95.0	94.0	92.0	89.1
Public gross financing needs	8.2	9.6	8.4	8.8	12.3	11.5	10.0	7.9	4.8
Real GDP growth (in percent)	1.2	0.3	0.3	0.7	1.4	1.7	1.8	1.9	1.9
Inflation (GDP deflator, in percent)	1.6	1.2	0.8	1.2	1.3	1.4	1.4	1.5	1.6
Nominal GDP growth (in percent)	2.9	1.5	1.1	2.0	2.8	3.1	3.3	3.5	3.6
Effective interest rate (in percent) [4/]	4.0	3.1	2.6	2.5	2.4	2.4	2.4	2.5	2.6

As of May 14, 2014		
Sovereign Spreads		
EMBIG (bp) 3/		44
5Y CDS (bp)		42
Ratings	Foreign	Local
Moody's	Aa1	Aa1
S&Ps	AA	AA
Fitch	AA+	AA+

Contribution to Changes in Public Debt

	Actual			Projections							
	2003-2011	2012	2013	2014	2015	2016	2017	2018	2019	cumulative	debt-stabilizing primary balance [9/]
Change in gross public sector debt	2.9	4.3	3.0	2.5	0.8	-0.1	-0.9	-2.0	-2.9	-2.7	
Identified debt-creating flows	2.5	3.7	3.2	2.6	0.9	0.0	-0.8	-1.9	-2.8	-1.9	
Primary deficit	1.8	2.4	2.1	1.9	1.3	0.7	0.0	-0.9	-1.9	1.1	-0.9
Primary (noninterest) revenue and gra	49.5	51.7	52.8	52.8	52.5	52.3	52.1	52.1	52.1	313.6	
Primary (noninterest) expenditure	51.3	54.1	54.9	54.7	53.7	52.9	52.1	51.1	50.2	314.8	
Automatic debt dynamics [5/]	0.7	1.3	1.3	0.4	-0.3	-0.7	-0.8	-0.9	-0.9	-3.3	
Interest rate/growth differential [6/]	0.7	1.3	1.3	0.4	-0.3	-0.7	-0.8	-0.9	-0.9	-3.3	
Of which: real interest rate	1.6	1.5	1.6	1.1	1.0	0.9	0.8	0.8	0.8	5.4	
Of which: real GDP growth	-0.8	-0.3	-0.3	-0.7	-1.3	-1.6	-1.7	-1.8	-1.7	-8.7	
Exchange rate depreciation [7/]	0.0	0.0	0.0	…	…	…	…	…	…	…	
Other identified debt-creating flows	0.0	0.0	-0.2	0.3	0.0	0.0	0.0	0.0	0.0	0.3	
Net privatization proceeds (negative)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Please specify (2) (e.g., ESM and Euro	0.0	0.0	-0.2	0.3	0.0	0.0	0.0	0.0	0.0	0.3	
Residual, including asset changes [8/]	0.4	0.6	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.7	



Source: IMF staff.

1/ Public sector is defined as general government.

2/ Based on available data.

3/ Long-term bond spread over German bonds.

4/ Defined as interest payments divided by debt stock (excluding guarantees) at the end of previous year.

5/ Derived as $[(r - \pi(1+g) - g + ae(1+r)]/(1+g+\pi+g\pi))$ times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

6/ The real interest rate contribution is derived from the numerator in footnote 5 as $r - \pi(1+g)$ and the real growth contribution as -g.

7/ The exchange rate contribution is derived from the numerator in footnote 5 as $ae(1+r)$.

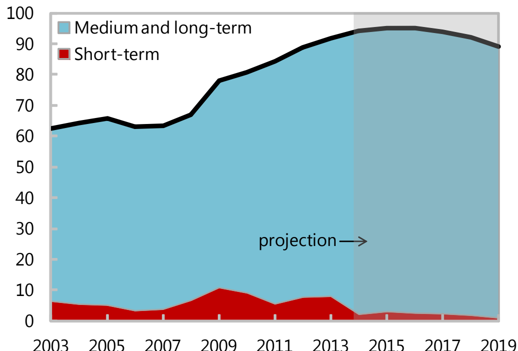
8/ Includes asset changes and interest revenues (if any). For projections, includes exchange rate changes during the projection period.

9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

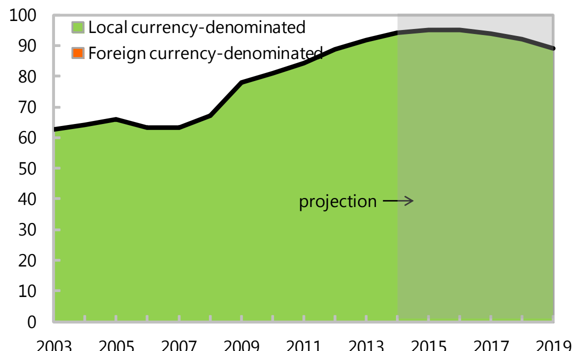
France Public DSA - Composition of Public Debt and Alternative Scenarios

Composition of Public Debt

By Maturity
(in percent of GDP)



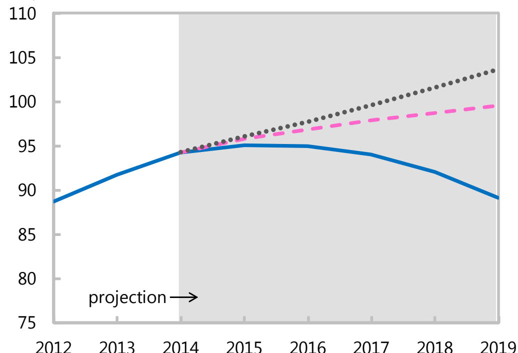
By Currency
(in percent of GDP)



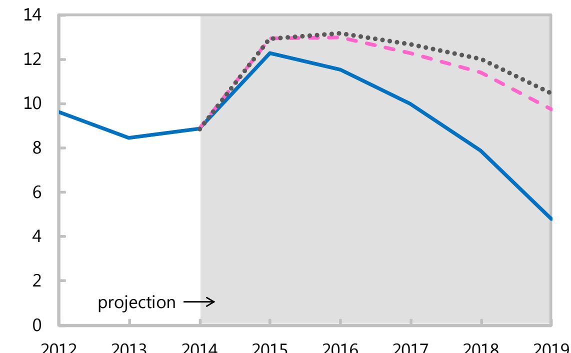
Alternative Scenarios

Baseline　Historical　Constant Primary Balance

Gross Nominal Public Debt
(in percent of GDP)



Public Gross Financing Needs
(in percent of GDP)



Underlying Assumptions
(in percent)

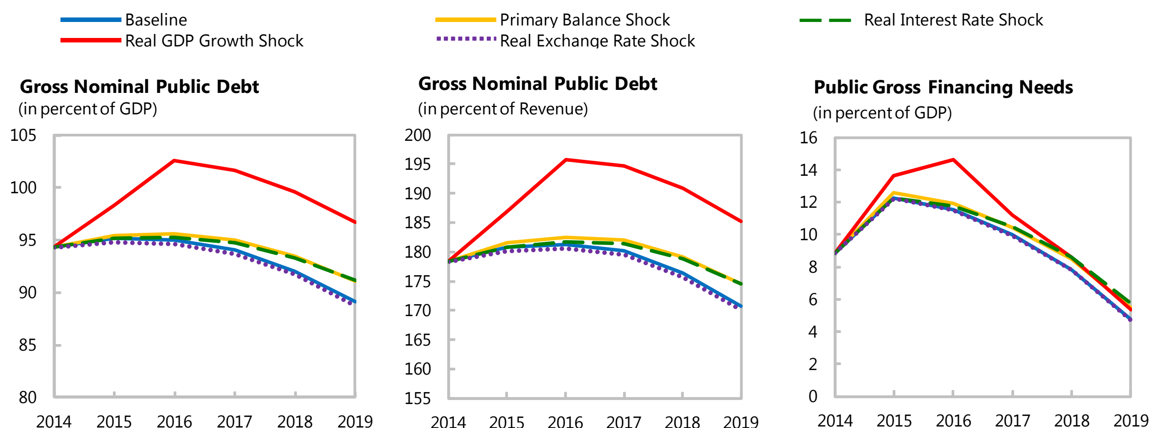
Baseline Scenario	2014	2015	2016	2017	2018	2019
Real GDP growth	0.7	1.4	1.7	1.8	1.9	1.9
Inflation	1.2	1.3	1.4	1.4	1.5	1.6
Primary Balance	-1.9	-1.3	-0.7	0.0	0.9	1.9
Effective interest rate	2.5	2.4	2.4	2.4	2.5	2.6
Constant Primary Balance Scenario						
Real GDP growth	0.7	1.4	1.7	1.8	1.9	1.9
Inflation	1.2	1.3	1.4	1.4	1.5	1.6
Primary Balance	-1.9	-1.9	-1.9	-1.9	-1.9	-1.9
Effective interest rate	2.5	2.4	2.4	2.4	2.5	2.6

Historical Scenario	2014	2015	2016	2017	2018	2019
Real GDP growth	0.7	1.1	1.1	1.1	1.1	1.1
Inflation	1.2	1.3	1.4	1.4	1.5	1.6
Primary Balance	-1.9	-1.9	-1.9	-1.9	-1.9	-1.9
Effective interest rate	2.5	2.4	2.5	2.6	2.8	3.1

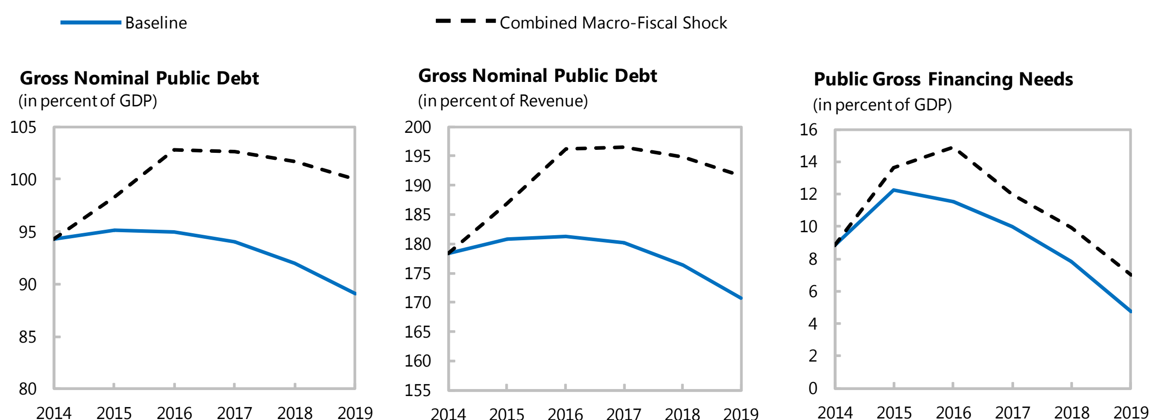
Source: IMF staff.

France Public DSA - Stress Tests

Macro-Fiscal Stress Tests



Additional Stress Tests



Underlying Assumptions

(in percent)

	2014	2015	2016	2017	2018	2019
Primary Balance Shock						
Real GDP growth	0.7	1.4	1.7	1.8	1.9	1.9
Inflation	1.2	1.3	1.4	1.4	1.5	1.6
Primary balance	-1.9	-1.6	-1.0	-0.4	0.5	1.4
Effective interest rate	2.5	2.4	2.4	2.4	2.5	2.6
Real Interest Rate Shock						
Real GDP growth	0.7	1.4	1.7	1.8	1.9	1.9
Inflation	1.2	1.3	1.4	1.4	1.5	1.6
Primary balance	-1.9	-1.3	-0.7	0.0	0.9	1.9
Effective interest rate	2.5	2.4	2.6	2.9	3.1	3.4
Combined Shock						
Real GDP growth	0.7	-0.3	0.0	1.8	1.9	1.9
Inflation	1.2	0.9	1.0	1.4	1.5	1.6
Primary balance	-1.9	-2.4	-3.0	-0.4	0.5	1.4
Effective interest rate	2.5	2.4	2.6	2.9	3.2	3.5

	2014	2015	2016	2017	2018	2019
Real GDP Growth Shock						
Real GDP growth	0.7	-0.3	0.0	1.8	1.9	1.9
Inflation	1.2	0.9	1.0	1.4	1.5	1.6
Primary balance	-1.9	-2.4	-3.0	0.0	0.9	1.9
Effective interest rate	2.5	2.4	2.4	2.5	2.6	2.7
Real Exchange Rate Shock						
Real GDP growth	0.7	1.4	1.7	1.8	1.9	1.9
Inflation	1.2	1.7	1.4	1.4	1.5	1.6
Primary balance	-1.9	-1.3	-0.7	0.0	0.9	1.9
Effective interest rate	2.5	2.4	2.4	2.4	2.5	2.6

Source: IMF staff.

Appendix III. FSAP Update: Status of Main Recommendations

Recommendations and Authority Responsible for Implementation	Priority (H/M)	Timing (S/M) 2/	Status
Overall Financial Sector Oversight			
Enhance public disclosure of financial institution conditions and risks.	H	S	***No New Action.*** The authorities consider availability and comparability of financial information for the main banking groups as adequate and no new initiatives are expected (e.g., the publication of bank-by-bank data by ACPR, including prudential returns). In 2013, the AMF conducted a review of public documents of listed banks to ensure information quality, and made recommendations to individual banks. The authorities will continue to report on financial sector developments in the context of BdF and ACPR annual and other reports, BdF annual thematic Financial Stability Review and AMF *Cartographie des Risques*.
Give serious consideration to modifying MoF participation in the Boards of ACP and AMF to support independence of the supervisory process.	M	M	***No New Action***. There are no plans to modify MoF participation in ACPR or AMF Boards. The authorities reiterated their disagreement with the FSAP evaluation.
Eliminate limits on headcount for ACP, AMF, and H3C.	M	M	***No New Action.*** The authorities indicated that they have sufficient margin of maneuver to accommodate the higher resource needs related to additional responsibilities given to ACPR by the 2013 banking law. The removal of headcount limits is not expected in the near-term given pressure not to expand budgets. Furthermore, the BdF can provide supplementary resources to ACPR if needed.
Banking Supervision			
Continue monitoring banks' funding position and availability of collateral to access liquidity through the secured debt market and/or central bank facilities.	H	H	***Done.*** ACPR monitors on an ongoing basis the liquidity position of French banks. At regular intervals, ACPR specifically reviews the preparedness of the main banking groups in meeting new regulatory liquidity ratios.
Give ACP powers to assess the suitability of Board members (of both banks and insurance companies) and to require removal of all unsuitable Board members.	H	M	***Done.*** The law of separation and regulation of banking activities of July 26, 2013 contains provisions amending the Monetary and Financial Code to extend the ACPR's authority to assess the fit and proper requirements for membership to the Board of Directors , the Executive Board or any other body performing equivalent functions for: - Credit institutions, upon appointment and throughout their tenure and in case of emergency; -Insurance firms, throughout their term, with the ability to suspend when requirements of sufficiently good repute and competence are no longer met and in case of emergency.
Give ACP powers to ensure it receives prior notification of major acquisitions and is, therefore, able to consider them ex ante.	H	S	***Partly Done***. The 2013 banking law has strengthened ACPR's capacity to review major acquisitions by banks. No other legislative initiatives on the matter are expected in the near term. The authorities indicated that granting ACPR formal approval powers for acquisition of EU financial institutions would be inconsistent with EU law (*Directive 2007/44/EC*).
Require full and consistent disclosure of the	H	S	***No New Action***. The authorities reiterated their disagreements with the FSAP evaluation and noted that

Recommendations and Authority Responsible for Implementation	Priority (H/M)	Timing (S/M) [2/]	Status
capital treatment in place and the related financial interactions within complex groups.			practices are fully consistent with European rules and Basel standards for cooperative groups. As for *bancassurance* groups, the exemption allowing the more lenient EU capital treatment lapsed at the end of 2012. Practices are now aligned with CRDIV and the conglomerate directive. There are no plans to revise disclosure requirements in regard to related financial interactions within complex groups.
Insurance Supervision			
Introduce enforceable legal and regulatory corporate governance requirements.	H	M	***Partly done.*** The Monetary and Financial Code requires the nomination and renewal of executives to be reported to the ACPR, who may oppose if fit and proper and experience conditions are not met. Governance requirements in line with international norms are expected to be imposed in the context of the transposition of the Solvency II directive, to be completed by March 31, 2015.
Require insurance companies to have internal audit and actuarial control functions.	H	M	***Ongoing.*** The entry into force of these requirements is expected in the context of the transposition of the Solvency II directive, to be completed by March 31, 2015.
Enhance insurance companies' disclosures, including on valuation of technical provisions; risk exposures and concentrations; risk management; corporate governance; and sensitivity results from forms of stress testing.	H	S	
Securities Regulation			
Establish stronger conflict-of-interest arrangements to govern industry participation in the AMF Board.	H	M	***No New Action***. There are no plans to modify the composition of AMF Board. The authorities reiterated their disagreement with the FSAP evaluation.
Strengthen AMF's supervision of investment service providers and financial advisors by increasing onsite work, including inspections.	H	S	***Partly Done***. AMF has reviewed all the associations of financial investment advisors (CIF) between 2012 and early 2013 to assess their capacity to inspect and control their members. Under the strategic plan for 2013-16, AMF is working to further strengthen CIF supervision. In particular, a specific methodology for control is being developed which could be used from 2014.
Provide greater enforcement powers to the H3C and increase its staffing levels.	M	M	***Ongoing***. H3C is expanding the number of staff dedicated to supervision of *commissaires aux comptes* and this trend is expected to continue in the near-term. European laws were adopted in April 2014 and are to be transposed within 2 years.
Resolution Framework			
Modify composition of Fonds de Garantie des Dépôts (FGD) Board to limit the potential for conflict of interest.	H	M	***No changes to the FGDR Board.*** The 2013 banking law which put in place a resolution authority (ACPR) stipulates that the Director of the FGD is a member of the resolution college at the ACPR. Changes to the composition of the FGDR are not envisaged.
Expand FDG's powers in the resolution process, so as to assume assets and liabilities from a failing bank.	H	S	***Partly Done.*** The 2013 banking law allows the FGD to be involved in bank resolution under the new name of FGDR (*Fonds de Garantie des Dépôts et de Résolution*), in association with the renamed banking supervisor, ACPR (*Autorité de Contrôle Prudentiel et de Résolution*).

Recommendations and Authority Responsible for Implementation	Priority (H/M)	Timing (S/M) [2/]	Status
Central Counterparties			
LCH.Clearnet SA should measure its exposures continuously throughout the business day.	H	S	***Partly Done***. The central counterparty is able to calculate multiple intra-day margin calls as prices and positions change. For fixed-income instruments, one automatic intraday margin call is calculated. For CDS, a margin call is done upon initiation of the operation independently of all netting. Margin calls are manually triggered for cash& derivatives. Collateral is re-valued daily, with haircuts applied meant to cover extreme but plausible market movements with a 99.7 percent confidence interval.
Carry out annually an external audit of LCH.Clearnet SA business continuity plan, including that of the in-sourcing company.	H	M	***Ongoing.*** In compliance with the authorization process under European Market Infrastructure Regulation (EMIR), ACPR will conduct an audit of LCH.Clearnet SA's business continuity plan. Consistent with EMIR obligations, internal rules of LCH.Clearnet SA will require an annual external audit of the BCP. Moreover, contractual arrangements with the providers of business continuity services were modified to allow for the possibility of external audit at any time.
AML/CFT			
Strengthen the implementation of AML/CFT measures in the overseas territories.	H	M	***Partly Done***. An agreement covering the financial aspects of the December 19, 2011 agreement between ACP and the overseas issuance institutes (IEDOM and IEOM) was signed on September 10, 2012. These agreements enlarge the mandate of the institutes to cover AML/CFT, including provision of assistance to the ACPR's onsite controls. On November 23, 2012, the Ministry of Justice released two circulars to remind prosecutors (including in overseas departments and territories) to be vigilant and deepen exchanges with TRACFIN. Various meetings and training sessions have been convened for overseas departments.
Complete legislation to enable the authorities to seize laundered property.	H	M	***Done***.

2/ H/M: indicates high or medium priority level. S/M: indicates the time span in which the recommendation could be implemented (short or medium term).

INTERNATIONAL MONETARY FUND

FRANCE

June 17, 2014

STAFF REPORT FOR THE 2014 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

Prepared By The European Department

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FUND RELATIONS

(As of April 30, 2014)

Membership Status: Joined December 27, 1945; Article VIII.

General Resources Account:	SDR Million	Percent of Quota
Quota	10,738.50	100.00
Fund Holding of Currency (Exchange Rate)	8,055.42	75.01
Reserve Tranche Position	2,683.20	24.99
Lending to the Fund		
New Arrangements to Borrow	2,506.82	

SDR Department:	SDR Million	Percent of Allocation
Net Cumulative Allocation	10,134.20	100.00
Holdings	9,287.05	91.64

Outstanding Purchases and Loans: None

Latest Financial Arrangements: None

Projected Payments to Fund (SDR million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2014	2015	2016	2017	2018
Principal					
Charges/Interest	0.83	1.17	1.17	1.17	1.17
Total	0.83	1.17	1.17	1.17	1.17

Implementation of HIPC Initiative: Not applicable

Implementation of Multilateral Debt Relief Initiative (MDRI): Not applicable

Implementation of Post-Catastrophe Debt Relief (PCDR): Not applicable

Exchange Rate Arrangements:

- France's currency is the euro, which floats freely and independently against other currencies.

- France maintains an exchange system free of restrictions on the making of payments and transfers for current international transactions, except for exchange restrictions imposed solely for the preservation of international security. These restrictions involving certain individuals and entities and which target specified countries have been notified to the Fund pursuant to Executive Board Decision No. 144-(52/51). In accordance with the relevant EU regulations and UNSC resolutions, certain restrictions are maintained on the making of payments and transfers for current or military international transactions with respect to Belarus, the Democratic Republic of Congo, the former Government of Côte d'Ivoire, the Islamic Republic of Iran, the former government of Iraq, the Democratic People's Republic of Korea, Guinea (republic of), Guinea Bissao, the former Government of Liberia, the former Government of Libya, Myanmar, the former Government of Tunisia, Transnistria (the independentist region of Moldova), Eritrea, the former Government of Egypt, Somalia, Sudan and South Sudan, Syria, certain individuals associated with the murder of former Lebanese Prime Minister Rafiq Hariri, and Zimbabwe.
- Measures have been taken to freeze accounts of listed persons and entities linked to terrorists pursuant to the relevant EU regulations (n°881/2002, n°2580/2001 and n°753/2011) and UN Security Council resolutions (resolutions 1267 and 1373 and subsequent resolutions).

Article IV Consultation:

The last Article IV consultation was concluded on July 29, 2013. The associated Executive Board assessment is available at http://www.imf.org/external/np/sec/pr/2013/pr13295.htm and the staff report at http://www.imf.org/external/pubs/ft/scr/2013/cr13251.pdf. France is on the standard 12-month consultation cycle.

FSAP Participation and ROSC:

France–Report on the Observance of Standards and Codes (ROSC): Module I–Fiscal Transparency	October 17, 2000
Fiscal Transparency—Update	IMF Country Report No. 01/196, 11/05/01
Fiscal Transparency—Update	IMF Country Report No. 04/345, 11/03/04

Summary: The report found that France has achieved a high level of fiscal transparency and has introduced a number of improvements in coverage and presentation of fiscal information. Notable areas of progress include the development in the final accounts publication to include more complete information on government assets and liabilities as well as disclosure of contingent

liabilities. Accounting standards have been changed to reflect accruals principles in a number of areas, and these standards are clearly explained. The staff suggested that further steps could be taken to identify and report quasi-fiscal activities in the budget presentation, provide a more consolidated picture of fiscal activity outside the appropriation process, and improve the reconciliation of stated policies with outcomes at the general government level.

These issues have been addressed in the *Loi organique aux lois de finance* (LOLF), which has become fully effective on January 1, 2006. In addition to the annual appropriations, the first multi-annual fiscal framework law was adopted in January 2009, and contains fiscal objectives for the period 2009–12. The budget is organized along missions and provides details on the level of appropriations for each mission and performance indicators by which the expected results of the mission will be assessed ex post. The State Audit Office has been given the new assignment of certifying the public accounts, and implementation of accruals basis accounting has been confirmed. Parliamentary oversight powers have been strengthened.

France–Report on the Observance of Standards and Codes (ROSC): Module II–Transparency in Monetary and Financial Policies	October 2000, corrected: 2/15/01
Transparency in Monetary and Financial Policies—Update	IMF Country Report No. 01/197, 11/05/01
Transparency in Monetary and Financial Policies—Update	IMF Country Report No. 02/248, 11/13/02

Summary: The 2000 ROSC noted that transparency of financial policies is accorded a high priority by all financial agencies assessed, and they are in observance of the good practices of the *Code of Good Practices on Transparency in Monetary and Financial Policies*. The major agencies disclose their objectives, their legal and institutional frameworks, and have open processes of policymaking and regulation. The principles of transparency are observed by dissemination of relevant information to the public and in the agencies' arrangements for internal conduct, integrity, and accountability. However, the staff noted that the framework for supervision and regulation applicable to mutual insurance firms is not as well defined and suggested to improve its transparency. The transparency of monetary policy was not assessed by the Fund team as the *Banque de France* is a member of the European System of Central Banks and no longer conducts independent monetary policy.

Subsequently, the framework for supervision and regulation applicable to a specific group of mutual insurance firms was modified in a number of steps. In August 2003, legislation created a single supervisory body, the *Commission de Contrôle des Assurances, Mutuelles et Institutions de Prévoyance* (CCAMIP) by merging the regular insurance supervisor (CCA) and mutualities' supervisor (CCMIP). Coordination with the banking sector supervisors was strengthened and the powers of the supervisory authorities extended. In 2010, supervision of the banking and insurance sectors was

unified under the *Autorité de contrôle prudentiel (ACP)*, which subsequently also was granted resolution powers and was renamed the *Autorité de contrôle prudentiel et de résolution (ACPR)*.

France–Report on the Observance of Standards and Codes (ROSC): Data Module	IMF Country Report No. 03/339, 10/2903
Data Module—Update	IMF Country Report No. 04/345, 11/03/04
Data Module—Update	IMF Country Report No. 05/398, 11/07/05

Summary: The report found that France is in observance of the Fund's Special Data Dissemination Standard (SDDS). In particular, the mandate of INSEE and the *Banque de France* for the production of the six macroeconomic datasets is clearly defined, with the reporting burden and the confidentiality provisions given special consideration notably through the CNIS. Professionalism is central to the statistical operations of the two institutions, internationally and/or European accepted methodologies are generally followed, the degree of accuracy and reliability of the six datasets is remarkable, statistics are relevant and provided on a timely basis, and they are accessible to the public.

The report made a number of suggestions for further improvements: the responsibility of INSEE as the producer of government finance statistics should be clarified; data sharing between the *Banque de France* and the rest of the French statistical system improved; classification and valuation methods in balance-of-payments statistics reviewed; consistency between the current account of the balance of payments and the goods and services account in the national accounts improved; the timing of revisions in the quarterly and annual national accounts aligned; and identification of data production units of INSEE facilitated.

France continues to implement several of the 2003 ROSC Data Module recommendations, including by promoting a broader understanding of statistical data revisions, making greater use of firm-level data to improve the measurement of changes in stocks, and intensifying work on portfolio investment income with the objective of starting to record those transactions on an accrual basis.

***France–Financial System Stability Assessment* (FSSA)**	IMF Country Report No. 04/344, 11/03/04
FSAP Assessment and Reports on ROSCs	IMF Country Report

	No. 04/345, 11/03/04
FSAP Assessment	IMF Country Report No. 05/185, 06/08/05
Publication of FSAP—Detailed Assessment of Observance of Standards and Codes	IMF Country Report No. 05/186, 06/08/05
***France–Financial System Stability Assessment* (FSSA)**	IMF Country Report No. 12/341, 12/07/12
France: Financial Sector Assessment Program—Detailed Assessment of Observance of Standards and Codes	
Basel Core Principles for Effective Banking Supervision	*IMF Country Report* *No. 13/180, June 2013*
Insurance Core Principles	*IMF Country Report* *No. 13/181, June 2013*
IOSCO Objectives and Principles of Securities Regulation	*IMF Country Report* *No. 13/182, June 2013*
Securities Settlement Systems and for Central Counterparties	*IMF Country Report* *No. 13/183, June 2013*
Financial Sector Assessment Program—Technical Notes	
Housing Prices and Financial Stability	*IMF Country Report* *No. 13/184, June 2013*
Stress Testing the Banking Sector	*IMF Country Report* *No. 13/185, June 2013*

Summary: The 2004 report concluded that France's financial sector is strong and well supervised. No weaknesses that could cause systemic risks were identified. The strength of the system is supported by the financial soundness indicators and the strong conformity to the supervisory and regulatory standards approved by the Basel Committee, IAIS, IOSCO, FATF, and CPSS. The degree of observance of the transparency code is high in all relevant areas. The French banking sector has been modernized and restructured over the past two decades and is well capitalized. Systemic vulnerabilities in the important insurance sector are well contained. Securities markets are large and sophisticated.

The FSAP Update undertaken in January and June 2012 confirmed the resilience of France's financial system to severe market pressures but also identified challenges faced by the system. While its structure has contributed to solid profit generation, the crisis exposed the risks posed by the banks'

size, complexity, and dependence on wholesale funding. The larger banks have been actively restructuring their balance sheets—moving to more stable sources of funding; reducing their cross-border presence; and building up capital. They remain, however, vulnerable to sustained disruptions in funding markets and reduced profitability, which would cause delays in meeting capital-raising plans.

The 2012 report confirmed that the regulatory and supervisory regime for banks, insurance, and securities market was of a very high standard. Areas for improvement that emerged from the FSAP Update included greater de jure independence of supervisory authorities; disclosure of the capital treatment and related financial interactions within complex banking groups; a move toward a more economic risk-focused approach to insurance regulation and supervision; and enhanced supervision of investment service providers and financial advisors.

The 2012 report also found disclosure-related shortcomings. French banks and listed companies, more generally, make extensive public financial disclosures under IFRS, and as a result of bank regulations (Pillar III of Basel II). Nonetheless, disclosure of financial sector data falls short of international best practice and enhancements would be highly desirable. Market discipline would benefit from the publication of regular and comparable data on an institution-by-institution basis, as well as detailed official analyses of financial sector developments in France.

STATISTICAL ISSUES

The economic database is comprehensive and of high quality, and data provision to the Fund is adequate for surveillance. The authorities regularly publish a full range of economic and financial data, and calendar dates of main statistical releases are also provided. France subscribes to the Fund's Special Data Dissemination Standard. The transmission of data in electronic form from INSEE (*Institut national de la statistique et des études économiques*) and the profusion of data from various institutions (*Banque de France*, INSEE, ministry of finance, ministry of labor and solidarity) have helped to build an infrastructure, in which all data can be easily accessed through the Economic Data Sharing System. A data ROSC mission conducted an assessment of the statistical system in March 2003, and the report was published in October 2003. A factual update to the main report was published in November 2004.

France's monetary and banking statistics methodology conforms with the European Central Bank framework, which provides comparable details as the Standardized Report Forms developed by STA. Statistics for *International Financial Statistics* on banking institutions and monetary aggregates are prepared on a monthly basis and are timely. Monetary data are also disseminated in the quarterly *IFS Supplement* on monetary and financial statistics. France follows the European System of Integrated Economic Accounts 1995 (ESA95). Data for GDP and its expenditure components are available from 1978 onwards. Both annual and quarterly accounts provide reliable information, although estimates from the two accounts differ slightly before the quarterly accounts are revised to be aligned to the annual ones. In 2014, national accounts estimates were rebased to 2010 prices and the methodology changed leading to an upward revision of the level of GDP and to a revision of public finance data.

Government finance statistics have been strengthened recently. Both central and general government data are presented in a more comprehensive fashion than previously and the data for 2006 and 2007 also reflect the various impacts of recent budgetary reform. Although the source data is collected by the Ministry of Economy and Finance, INSEE is principally responsible for the compilation and dissemination of fiscal data in a framework that is consistent with ESA95. INSEE's website has recently been enhanced; in particular, it includes expenditure tables and government revenues by subsector (central government, miscellaneous central government agencies, local governments, and social security administration).

Starting in January 2014, balance-of-payments statistics are published monthly using the guidelines set out in the sixth edition of the Balance of Payments Manual. Greater coherence between the external current account and the rest of the world account in the national accounts is needed. In this regard, work with promising early results has been undertaken on the transportation account.

TABLE OF COMMON INDICATORS REQUIRED FOR SURVEILLANCE

(As of May 2014)

	Date of Latest Observation	Date Received	Frequency of Data	Frequency of Reporting	Frequency of Publication
Exchange Rates	04/14	04/14	Monthly	Monthly	Monthly
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	03/14	05/14	Monthly	Monthly	Monthly
International Investment Position	2012	Q1:2013	Annual	Annual	Annual
Reserve/Base Money	04/14	05/14	Monthly	Monthly	Monthly
Broad Money	04/14	05/14	Monthly	Monthly	Monthly
Central Bank Balance Sheet	04/14	05/14	Monthly	Monthly	Monthly
Consolidated Balance Sheet of the Banking System	04/14	05/14	Monthly	Monthly	Monthly
Interest Rates[2]	04/14	05/14	Monthly	Monthly	Monthly
Consumer Price Index	04/14	05/14	Monthly	Monthly	Monthly
Revenue, Expenditure, Balance and Composition of Financing[3]—General Government[4]	2013	05/14	Annual	Annual	Annual
Revenue, Expenditure, Balance and Composition of Financing[3]—Central Government[5]	03/14	05/14	Monthly	Monthly	Monthly
Stock of Central Government Debt	04/14	05/14	Monthly	Monthly	Monthly
Stock of Central Government-Guaranteed Debt	Q1:2012	04/14	Quarterly	Quarterly	Quarterly
External Current Account Balance	03/14	05/14	Monthly	Monthly	Monthly
Exports and Imports of Goods and Services	03/14	05/14	Monthly	Monthly	Monthly
GDP/GNP	Q4:2013	05/14	Quarterly	Quarterly	Quarterly
Gross External Debt	Q4:2013	05/14	Quarterly	Quarterly	Quarterly

[1] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[2] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
[3] Foreign, domestic bank, and domestic nonbank financing.
[4] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.
[5] This information is provided on a budget-accounting basis (not on a national accounts basis).

Press Release No.14/326
FOR IMMEDIATE RELEASE
July 3, 2014

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Concludes 2014 Article IV Consultation with France

July 1, 2014, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation[1] with France.

The economy fared better than most other large euro areas economies through the crisis, reflecting the resilience of private consumption, lack of financial fragmentation, and lower levels of household and corporate debt. Banks' financial position has also been strengthened. But after two years of near stagnation unemployment remains high. A loss of competitiveness has also weighed on growth, and compressed profit margins have constrained investment.

The outlook is for a gradual recovery, with GDP growth projected at 0.7 percent in 2014 and 1.4 percent in 2015, based on stronger external and domestic private demand, reflecting gains in real disposable income and improved profit margins. Inflation is expected to remain subdued at around 1 percent. These trends should allow the private sector to become a source of net job creation this year.

Fiscal adjustment has been very substantial over the past three years, but the deficit was still 4.2 percent in 2013. The authorities' program targets continued adjustment with a view to closing the structural fiscal deficit over the medium term, based on a program of expenditure containment. It also contains supply side measures, including tax reductions to reinvigorate investment and job creation.

Executive Board Assessment[2]

Executive Directors noted that the French economy has shown resilience during the global financial crisis, but the pace of recovery has been slow. Going forward, Directors welcomed the authorities' economic strategy outlined in the Stability Program and the National Reform

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

[2] At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: http://www.imf.org/external/np/sec/misc/qualifiers.htm.

Program, noting that the policies and objectives are well aligned. They concurred that an ambitious adjustment and reform agenda is critical to address structural imbalances, guard against future shocks, address the employment and competitiveness gaps, and boost the economy's growth potential. In view of the implementation risks of this ambitious agenda, Directors considered that the strategy needs to be backed by comprehensive upfront measures in the fall budget, and could be boosted by deeper structural reforms.

Directors endorsed the authorities' plan to undertake a steady and more moderate pace of fiscal adjustment, focusing on expenditure measures. They welcomed the progress made in reducing the fiscal deficit during difficult economic times. Looking ahead, they noted that the proposed pace of adjustment strikes an appropriate balance between the need to restore fiscal space and support recovery. Further, they considered that anchoring the adjustment on expenditure addresses the structural weakness of public finances, and urged the authorities to rely on structural measures to ensure a permanent slowdown in spending growth. Recognizing that these measures could be politically difficult to implement, they welcomed the authorities' resolve to remain steadfast in pursuing the reform program, as there is little room for deviation if both tax cuts and deficit reduction are to be pursued simultaneously.

Directors welcomed the supply-side measures to revive investment and job creation, and encouraged further reforms to labor and product markets. They supported the renewed focus on fighting rents as a guiding principle to spur reform, and called for stronger effort to open protected sectors to greater competition. Directors encouraged the authorities to build on the labor market reforms taken since 2012 and to make the labor market more adaptable. They stressed the importance of enhancing the scope for enterprise-level negotiation based on a more cooperative social dialogue. Directors welcomed the efforts deployed to reduce unemployment among the low skilled, but also suggested that the minimum wage could be set with a view to increasing their job opportunities.

Directors observed that the economy and public finances are better shielded from banking shocks thanks to the efforts made by banks to build stronger liquidity and capital buffers and to an improved bank resolution framework. However, they noted that the regulatory framework is still evolving, and that additional adjustment will be needed on the part of banks to meet prudential requirements. Directors encouraged the authorities to ensure that banks' key financing role is not constrained during this process, and to facilitate it by leveling the playing field in the taxation of financial instruments.

France: Selected Economic and Social Indicators, 2009–19

	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
						Projections					
Real economy (change in percent)											
Real GDP	-2.9	2.0	2.1	0.3	0.3	0.7	1.4	1.7	1.8	1.9	1.9
Domestic demand	-2.6	2.1	2.0	-0.3	0.2	0.7	1.0	1.4	1.6	1.7	1.7
Nominal GDP (billions of euros)	1939	1998	2059	2091	2114	2156	2215	2284	2359	2442	2530
CPI (year average)	0.1	1.7	2.3	2.2	1.0	1.0	1.2	1.3	1.4	1.5	1.6
Unemployment rate (in percent)	9.1	9.3	9.2	9.8	10.3	10.3	10.2	10.0	9.7	9.4	9.3
Gross national savings (percent of GDP)	20.0	20.6	21.5	20.6	20.4	20.8	21.1	21.6	22.1	22.5	23.0
Gross domestic investment (percent of GDP)	21.3	21.9	23.2	22.7	22.0	22.4	22.1	22.2	22.3	22.4	22.7
Public finance (percent of GDP)											
Central government balance	-6.0	-6.1	-4.4	-3.9	-3.3	-3.2	-3.1	-2.6	-2.1	-1.3	-0.5
General government balance	-7.2	-6.8	-5.1	-4.9	-4.2	-4.0	-3.4	-2.7	-2.1	-1.2	-0.3
Structural balance (percent of potential GDP)	-5.4	-5.5	-4.5	-3.8	-2.8	-2.4	-1.9	-1.6	-1.4	-0.9	-0.2
Primary balance	-4.9	-4.5	-2.6	-2.4	-2.1	-1.9	-1.3	-0.7	0.0	0.9	1.9
General government gross debt	78.0	80.8	84.4	88.7	91.8	94.3	95.1	95.0	94.0	92.0	89.1
Money and interest rates (in percent)											
Money market rate 1/	0.7	0.5	0.8	0.1	0.0	0.1	...	...	...	...	...
Government bond yield 1/	3.6	3.1	3.3	2.5	2.2	2.3	...	...	...	...	...
Balance of payments (in percent of GDP)											
Exports of goods	17.9	19.6	20.6	20.9	20.5	19.8	19.7	19.7	19.8	19.9	19.9
Volume growth (in percent)	-11.3	9.0	6.9	1.1	2.2	3.4	4.8	4.6	4.6	4.6	4.6
Imports of goods	20.1	22.3	24.3	24.3	23.5	22.8	22.2	21.9	21.8	21.7	21.5
Volume growth (in percent)	-9.4	8.9	6.3	-1.3	1.7	3.1	3.2	3.5	3.8	3.9	3.9
Trade balance	-2.2	-2.7	-3.7	-3.4	-2.9	-3.0	-2.5	-2.2	-2.0	-1.8	-1.6
Current account	-1.3	-1.3	-1.7	-2.1	-1.3	-1.5	-0.9	-0.5	-0.2	0.0	0.3
FDI (net)	-3.1	-1.2	-0.7	-0.5	0.3	0.0	-0.2	-0.4	-0.6	-0.8	-1.0
Official reserves (US$ billion)	46.6	55.8	48.6	54.2	50.8	...	...	...	...	...	...
Fund position (as of December 31, 2013)											
Holdings of currency (percent of quota)	80.8	79.7	73.1	69.6	74.2	...	...	...	...	...	...
Holdings of SDRs (percent of allocation)	95.9	96.1	95.5	93.6	90.6	...	...	...	...	...	...
Quota (SDRs million)	10739	10739	10739	10739	10739	...	...	...	...	...	...
Exchange rates											
Euro per U.S. dollar, period average	0.72	0.75	0.72	0.78	0.75	...	...	...	...	...	...
Nominal effective rate, ULC-styled (2000=100)	104.8	102.4	102.4	100.1	102.1	...	...	...	...	...	...
Real effective exchange rate, ULC-based (2000=100)	103.6	104.3	105.4	104.8	109.1	...	...	...	...	...	...
Potential output and output gap											
Potential output	1.1	0.9	0.9	0.9	1.0	1.0	1.1	1.2	1.3	1.4	1.5
Output gap	-3.1	-2.1	-0.9	-1.5	-2.2	-2.5	-2.2	-1.7	-1.1	-0.6	-0.2

Social indicators

Per capita GDP (2006): US$35,471; Life expectancy at birth (2009): 77.7 (male) and 84.4 (female);

Poverty rate (mid-2000s): 14.1 percent (60 percent line), 7.1 percent (50 percent line);

Income distribution (ratio of income received by top and bottom quintiles, 2004): 4.2.

Sources: French authorities; IMF staff estimates and projections.

1/ For 2014, January-March.

Statement by Hervé de Villeroché, Executive Director for France
July 1, 2014

We would like to thank staff for a very clear, balanced and interesting set of papers that broadly validates both my authorities' diagnosis on the French economy and the strategy that is being put in place as a response. My authorities would also like to thank the Article IV mission team for the open, thorough and candid discussions that took place in Paris during the first half of May.

1. Economic outlook

General context and relative performance

So far, the global recovery has been gradual and uneven. Initiatives in the euro area helped to ease financial tensions, particularly the decisions taken by the European Council in June 2012 and the increased involvement of the ECB announced in September 2012. However, adjustments in the euro area, particularly in countries with major external and fiscal deficits, and the appreciation of the euro exchange rate, put a drag on France's external demand and price environment at a time when France itself was restoring its macroeconomic balances.

In this difficult external environment, the French economy's resilience has been remarkable over the past years. As shown by the Figure 1 in the report, when compared to pre-crisis levels, French economy GDP lays almost 4 points over the euro area average. Staff's views that France is now "behind other countries in the recovery cycle" is based essentially on the OECD leading indicators, which did not capture the relative performance of the French economy within the euro area over the past two years, and could therefore have been handled differently. In particular, France is one of the countries where business investments resisted most during the crisis.

Recent developments

There were encouraging signs at the end of the year 2013, with a recovery in investment and jobs in the private sector for the first time in two years. The annual rate of growth now stands at around 1 percent. The slowdown in Q1 2014 was caused by temporary factors such as mild weather conditions which caused a decrease in energy expenditure, after-effect of the exceptional possibility given to employees to unlock the savings invested in their company at the end of 2013 and an increase in the tax rate on polluting vehicles. Regarding demand, indicators such as manufactured goods consumption and commercial vehicles or based-on VAT indicators of investments are encouraging. A rebound in consumption and investment is then highly likely for Q2.

Macroeconomic forecasts

The French stability and growth program expects GDP growth to stand at 1 percent in 2014 before rising to 1.7 percent in 2015 and 2¼ percent in 2016-2017. Those forecasts were broadly in line with staff projections at the time of their release. In the meantime, staff

revised its forecasts down due to a disappointing Q1 growth. The latest economic indicators confirm that uncertainty remains high. My authorities will wait for the Q2 figure's release in mid August before deciding whether or not to revise the macroeconomic scenario for the draft budget law.

Engines of growth

Overall, underlying macroeconomic scenarios and expected engines of growth are quite similar in staff and authorities forecasts. The economic climate is expected to recover in 2014-2015 thanks to increased business and household confidence as well as the implementation of structural reforms, notably the Responsibility and Solidarity Pact. As a consequence, 2014-2015 should see a pick-up in corporate investments and in consumption; France should also benefit from the ongoing recovery in the Eurozone and in advanced economies, which would be materialized by an increase in exports. In a medium and long run perspective, strong demographics, rising innovation efforts by French companies, highly qualified and productive workforce, excellent infrastructure and a stable investment rate during the crisis are factors bound to support France's growth prospects.

2. Fiscal policy

My authorities intend to provide full support for the economic recovery by carrying out a bold plan of reforms. The Responsibility and Solidarity Pact (*Pacte de responsabilité et de solidarité*) is the keystone of the Government's strategy, which aims to support jobs and competitiveness through labor-management dialogue and in consultation with all stakeholders. The Pact also includes solidarity measures to support the purchasing power of low-income workers. The entire package will be financed through an unprecedented effort to reduce public spending.

Fiscal adjustment pace

The fiscal adjustment pace had been carefully calibrated in order to continue an ambitious and still needed fiscal consolidation, but in a growth-friendly manner and while financing priorities were identified for the future – secondary and higher education, justice and security. The deficit will then continue to shrink gradually from 5.1 percent of GDP in 2011, 4.8 percent in 2012, 4.2 percent in 2013 to 3.8 percent in 2014 and 3.0 percent in 2015. In keeping with our European commitments, the structural balance will be brought close to equilibrium by 2017 by means of an adjustment of 0.8 point per year in 2014 and 2015, followed by an adjustment of 0.5 point per year after that. We welcome the staff's appraisal that this pace is the "right" one.

Fiscal adjustment composition

Consistently with staff recommendations, the fiscal adjustment will rely exclusively on the expenditure side, with an unprecedented target of €50Bn expenditure savings relative to trend; this effort corresponds to a freeze in real expenditures (compared to growth of 1½ percent over the 2000 decade). Those savings will be used to close the structural deficit and

to reduce the aggregate tax and social security contribution rate, with a view to stimulate competitiveness and household's purchasing power.

The savings effort will be shared equally across the whole general government sector:

- Central government and central government agencies' will shoulder the largest portion (€18 billion over three years) by increasing efficiency and further improving their cost control;
- Local government will bring expenditure growth back into line with inflation, saving €11 billion through cuts on state transfers to local governments and the progressive savings expected by a deep organizational reform (halving the number of *régions* by 2017, strengthening *intercommunal* structures, clarifying the division of powers by eliminating the *clause de competence générale* and by eliminating the *département* councils by 2021);
- The health insurance system will save €10 billion through ongoing structural reforms to ensure the quality of care and the level of coverage while keeping costs under tighter control;
- The social protection system will save €11 billion through reforms that have already been adopted, notably regarding pensions and family benefits, and through future measures, such as efficiency gains in the management of social security funds and a stabilization of benefits in nominal terms, except for minimum social benefits, for one year;
- Finally, civil servants will also play their part through a stabilization of the civil service pay scale, but efforts to recruit new personnel in priority sectors will continue.

The supplementary budget bill presented on June 11th includes several extra savings amounting to €4 bn while providing a break totaling €1.1 bn on income tax paid by middle and low-income households (the cost of this measure will be compensated by the increased revenues generated by the anti-fraud service - STDR).

Tax cuts - Responsibility and solidarity pact.

With the Responsibility and Solidarity Pact, French labor costs, which has already fallen as a result of the Competitiveness and Employment Tax Credit (CICE) by €20 Bn, will be cut further for a total reduction of €30 Bn (1 ½ percent of GDP), in order to boost employment and restore firms profitability. By 2016, there will no longer be any social security payroll contributions on minimum-wage jobs, other than unemployment insurance contributions. Family allowance contributions will be reduced as well on jobs paying up to three and a half times the minimum wage.

The Pact also includes a "fiscal side" that will imply business taxes to be streamlined and reduced: the corporate social solidarity contribution (C3S), which is based on turnover and not on income, will be reduced starting in 2015 and phased out by 2017; the exceptional corporate income tax payment for large corporations will be phased out in 2016 and the standard rate of corporate income tax will decrease starting in 2017, bringing it down to 28 percent by 2020.

At the same time, measures in favor of low-income workers will total €5 Bn by 2017, including a reduction in the employee social security contributions for workers earning the minimum wage.

Macroeconomic impacts

Based on the usual macroeconomic patterns, the Responsibility and Solidarity Pact will add half a percentage point to growth and create nearly 200,000 additional jobs in the medium term. In practice, this impact should be amplified by the commitments made by economic and social players under the Pact and, more generally, by a positive confidence shock. This assessment is broadly consistent with IMF staff's own estimates of the total long term impact of recent actions taken to lower the labor cost (including the CICE tax credit), which would create at least 600,000 additional jobs.

3. Structural reforms

Labor market

Several structural reforms have already been undertaken over the past two years to improve the functioning of the labor market, beyond the pro-employment tax policy:

(i) The law on *sécurisation de l'emploi*, which transposed the national multisector agreement on January 11, 2013, has created a framework for agreements to protect jobs when a company's economic situation deteriorates, while securing workers' careers, especially for the most vulnerable;

(ii) The Act, established on March 5, 2014, on *vocational training* which also transposed a former agreement at the national multisector level, provides for individual and transferable rights to training (individual training accounts) and greatly simplifies the existing system. It expands the scope of the training available, particularly for the most vulnerable individuals (including the unemployed and young people); it also aims to ensure that training meets the economy's need for skills in the short and medium term;

(iii) Staff rightly emphasizes the structural impact of the introduction of "rechargeable" unemployment benefit entitlements, which is part of the broader social partners' agreement, established on March 22, 2014, on *unemployment benefits*; this scheme will reduce uncertainty for unemployed person to re-enter the workplace, by preserving unused benefits if a new job is accepted.

On the minimum wage, my authorities do not endorse the staff's recommendation to include the unemployment rate of the low skilled in its indexation rule. A reform of the indexation rule took place in 2013, precisely in order to better guarantee the purchasing power of the low-income workers; a decrease in the minimum wage in bad times would have unacceptable social consequences and an unclear macroeconomic effect (positive effect on labor demand but negative impact on aggregate revenue). Moreover, it should be borne in mind that thanks to existing tax and social exemptions, the tax wedge at the minimum wage is already within international standards; together, the CICE tax credit and the Responsibility and Solidarity

Pact (by decreasing employers *and* employees contributions, notably at the minimum wage level) will further reduce the tax wedge for the less skilled workers, supporting labor demand and labor supply. These schemes seem simpler, more efficient, and more direct than modifying the indexation of the minimum wage to support employment.

Product markets

France implemented several structural reforms of the product markets in order to simplify administrative burden and red tape, fight economic rents and boost purchasing power and competitiveness, in line with staff recommendations.

The Consumer Act, established on February 13, 2014, contains measures that promote competition and consumers' interests. It creates a class action procedure for consumer disputes under French law, particularly in the case of anti-competitive practices in services. The provisions of the Act enhance competition in services, particularly in the healthcare sector (opticians, chemists) and in the financial sector (banking and insurance). The measures under this Act will have a significant impact on households' purchasing power, estimated at €1.5bn in all. My authorities intend to take further steps, particularly in the healthcare sector, with further reform of the market for certain so-called “borderline” products, which are currently sold exclusively by chemists and greater price transparency in the distribution of certain medical devices, such as prostheses and optical products.

Other measures will increase competition in services. The Act, established on January 2, 2014, eliminated restrictions in the legal and accounting professions in order to develop the business of notaries, lawyers and accountants. Other changes to legislation are being considered, such as a more cost-based approach to pricing in some of these professions. Consultations will be held with professionals that may also cover the organization of certain services with a view to achieve greater economic efficiency.

In addition, a large program for the simplification of administrative burden was launched in July 2013. More than 200 measures were put forward, among them more than half are directly linked to firms’ routine. To increase the impact of the program, the government has been granted the right to speed up the process and has created a council for businesses’ simplification, which has already designed 50 new measures. From May 2014 onward, 10 new simplification measures will be decided upon each month.

By the end of the year, the Businesses Simplification Committee is scheduled to review the rules governing access and permission to exercise certain professions, and submit proposals to the Government. In June 2014, the French minister of the Economy asked the French Competition Authority to issue an opinion on the fixation and revision of tariffs of specific regulated professions (notaries, bailiffs, clerks of Commercial Court, etc.)

4. Financial sector

Staff’s report rightly underlines that French banks have made significant progress towards meeting Basel III requirements. They meet the CRD-IV fully loaded minimum CET1 capital

requirement, and have strongly reduced their dependence to short term wholesale funding, which only represents around 10 percent of total liabilities in 2013, compared to 30 percent pre-crisis. It is certainly too early to assess their position relative to future net stable funding requirements at this point in time, as the precise definition and calibrations of the NSFR ratio are still under discussion by the BCBS; we however strongly believe in French banks' capacity to meet the new requirements, if published in a not-too-distant future, in a timely manner as they already did with the other CRD-IV capital requirements. Finally, it is likely that the various regulatory and supervisory measures implemented so far at the national (notably the *loi de separation et de regulation des activités bancaires* established on July 26, 2013 and European level, in particular the setting-up of the single supervision and resolution mechanisms, as well as significant efforts made by banks to strengthen their resilience, have decreased the systemic risks posed by a potential failure. The ongoing asset quality review and the stress test will also be key to provide additional clarity on the banks that will be subject to the ECB's direct supervision.

My authorities remain confident that the financing needs of the economy will continue to be satisfied when the demand for funding will become more buoyant, despite the evolving regulatory framework. Recent reforms will help finance firms' growth and development following a two-pronged approach by providing them with the means to diversify their financing instruments and sources. On one hand, French authorities have been working in close liaison with all relevant market participants to ease market access of firms large enough to benefit from market financing (the euro private placement workstream) and restarting a robust and viable loan securitization market; this should allow all French firms to find solutions when their demand for funding will gain further momentum. On the other hand, work has been done to diversify potential sources of funding through reforms in the insurance sector (reform of life insurance products, adjustment in the prudential treatment of the simplest securitized products invested in loans to corporate) and the introduction of a dedicated SME bucket in savings plan (PEA-PME).

5. Risk assessment

Uncertainty remains high, mainly stemming from international developments. The pace of France's recovery hinges on that of the euro area. The recent actions taken by the ECB to tackle the risk of a low inflation period are welcome, notably because monetary conditions have become tighter over the past months, as staff's report emphasizes.

There are also more specific risks. In particular, there is still uncertainty about the behavior of private sector economic agents. Brighter prospects for growth could lead to a stronger rebound in investment, which would entail more jobs, thereby boosting household incomes and consumption. Policies to support competitiveness and employment will have a positive impact, but the scale of this impact will depend on how businesses behave. Businesses could, for example, pass on lower labor costs in the form of price competitiveness gains that favor exports and curb domestic inflation. Alternatively, they may prefer to boost their profit margins which could boost non price competitiveness.

Finally, while we broadly share the staff's assessment of risks, we cannot agree on the risk of a political resolve lessening. My authorities have repeatedly expressed a very strong commitment to stay the course of reform and the method based on social dialogue allowed significant achievements, notably on the labor market reform.