Prospects

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FRANCE – Political issues
Response to the Great Debate

- **The *grand débat*, or "great debate" that took place from January to March 2019 in the wake of the *gilets jaunes* ("yellow vests") crisis spawned multiple demands, the two most high profile of which were a sense of "fiscal frustration", underpinned by a desire for lower taxes and a fairer tax system, and strong demand for public services.**
- **In the face of these demands and the ongoing *gilets jaunes* crisis, the President of the Republic made a speech on Thursday 25 April. The principal economic policy choices are largely unchanged, with the reform programme to continue, especially for pensions and unemployment insurance, and a priority given to labour as a value, with the idea of encouraging French citizens to work more.**
- **However, to consider French citizens' demands, the "priority for education and fight against poverty and downward social mobility" component has been clearly strengthened. The supply-side policy is going hand-in-hand with a new raft of measures designed to stimulate demand, mainly aimed at the middle classes. There will be greater input from local elected officials and social partners in overall governance, especially as regards the topic of a more balanced distribution in local government.**
- **The new measures to stimulate purchasing power will come into force from 2020 and total around 8 billion euros. They include a reduction in personal income tax targeted at the middle classes, a re-indexation of pensions of less than 2,000 euros a month; an extension of the exceptional bonus paid by firms, net of taxes and contributions; and the recovery of unpaid alimony payments by child benefit agencies.**
- **This plan supplements a series of other tax and social security cuts rolled out in recent months in the Budget for 2019 and in last December's purchasing power support plan. By adding together the three packages, households will benefit from a "net" 13 billion euros in support measures in 2019 and 10 billion euros' worth of new measures in 2020. In this way, the gains in purchasing power will be very significant, at 2.6% in 2019 and 1.5% in 2020.**
- **Consumption looks set to pick up, but to a lesser degree. In 2019, it is expected to rise by 1.5%, given a sharp rise in the personal savings rate. Households are persisting with their precautionary savings habits and will spend the gains derived from the support plans only gradually.**
- **In its first estimate published on Tuesday 30 April by Insee, GDP growth came in at 0.3% in Q1 2019 relative to Q4 2018. Consumption was fairly sustained, up by 0.4%, but below the increase in purchasing power. Conversely, the deterioration in global growth and the sharp slowdown among our European partners (Germany, Italy) in particular, has had an adverse impact on the business climate and on activity.**
- **In the short term, this support plan will bolster purchasing power and consumption and lead to an honourable level of growth in 2019-2020, of 1.4% a year. But it is unlikely to solve the social crisis. In the mid-term, the President's aim is to continue the structural reforms, to make the French economy more competitive and more innovative, and to create a virtuous circle with stronger and more sustainable growth. He may not pull his gamble off, however. The impact of his structural reforms on growth is long drawn out and complex, while the risks looming over the international environment could compromise the process of turning the French economy round.**

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The main demands emerging from the great debate

In the wake of the *gilets jaunes* crisis, a great national debate took place from January to March 2019. The consultation brought together around 1.5 million participants in a variety of guises, notably through online contributions[1]. In the economic and social sphere, two main strands stand out in light of the 530,000 contributions analysed to date. First is a sentiment of fiscal exasperation, with a twin desire to cut taxes and to see greater fiscal justice. Second came a powerful demand for public services, even if elsewhere, the respondents preferred public spending cuts to higher taxes as a means of narrowing the deficit.

Tax cuts

Households have massively demanded tax cuts. The measure cited most often is a cut in VAT (28.2% of respondents), especially on essentials, followed by a cut in personal income tax (18.8%), local taxes (11.6%), and social security contributions (7.7%).

Eco-taxes, which ignited the *gilets jaunes* revolt, continue to be a point of contention, with 58% of respondents rejecting "punitive taxation" such as the carbon tax to encourage people to change their habits, while 55% reckon that an increase in fuel taxes or petrol would have little impact on their behaviour.

A fairer tax system

Respondents also demanded greater fiscal justice via several proposals.

- ✓ Broaden the tax base: 34.7% wanted everyone to pay personal income tax.
- ✓ Increase the contribution from those on the highest incomes (27.8%), in particular by abolishing tax loopholes (11.8%) and restoring the ISF wealth tax (10.3%).
- ✓ Overhaul corporate taxation (12%), in particular via a GAFA tax (3%) and a fairer distribution between SMEs and major corporates (6%).
- ✓ Combat tax fraud and evasion (11.3%).

Improving public services

Respondents wanted public services to be close, accessible in all parts of France, and strengthened in selected fields: healthcare, education, and the ecological transition.

Healthcare is the most-cited area requiring stronger social protection (27.8%) and where access to public services is deemed insufficient (30.4%). The avenues sketched out include measures to combat healthcare "deserts", and the creation of healthcare clusters in rural areas.

The ecological transition is a major issue. The key avenue mentioned is improving public transport networks (43%). Some 86% moreover, believe they could contribute to protecting the environment

Two other demands emerge clearly: the first is a need for local services, with a re-balancing between metropolitan areas and small and medium-sized towns and cities, more day-to-day public transport, and more front-line public sector workers. The second is administrative simplification: 49% say they have already given up applying for a benefit because of the complexity of the application process, while 86% feel there are too many administrative layers.

Control over public spending

At the same time, respondents massively said they would prefer cuts to public spending (75%) over tax increases (4%) to narrow the public deficit. Priority went to cutting state spending (56%), mainly in the spheres of defence (28%) and housing policy (22%), rather than reducing spending on local government (18%) and social security spending (16%).

The main avenues for cutting spending are a reform to social benefit allocation conditions (52%), an increase in weekly working hours (24%), and a later retirement age (22%).

Main thrusts essentially maintained, but softened by the social crisis

Faced with these multiple claims and the persistent *gilets jaunes* crisis, the French President made a speech on Thursday 25 April, setting out in detail the main lines of his economic policy, and announcing a number of measures.

The main thrusts of economic policy seem in our view largely unchanged. This policy aims to modernise the French economic and social model and to enable

[1] These contributions refer to responses to an online questionnaire. The data deriving from the questionnaires have been processed by OpinionWay.

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more robust and sustainable growth. It is structured around several main lines:

- ✓ A supply-side policy and continued efforts to improve the cost and quality competitiveness of French businesses through tax cuts, the transformation of the CICE into lower contributions, and the PACTE Act, etc.;
- ✓ Support for innovation, research and high-growth sectors;
- ✓ A redeployment of resources towards work, notably through labour law reforms and the ongoing reform of unemployment insurance;
- ✓ The priority for education and combating poverty and downward social mobility via help for education, a reform of vocational training and the apprenticeship system, and support measures for employment.

However, to take the demands of French citizens into account, the fourth of these lines has been clearly beefed up, with the idea of a restated priority for education right from the primary stage, and of a more equitable society. The supply-side policy now goes hand-in-hand with a new component featuring measures to stimulate demand aimed especially at the middle classes. Governance structures will include more locally elected officials and the social partners, especially as regards the strand of re-balancing local government coverage.

At the same time, however, the French President restated his objective of pursuing the ongoing reforms over the coming months, especially pension and unemployment insurance reforms. He also stressed the value of work and wants to encourage the French to work more.

Main measures announced

Measures to support purchasing power

Following the series of support measures for households decided last December in response to the *gilets jaunes* crisis, a new series of measures to stimulate purchasing power has been announced. These measures will come into play from 2020 and will total around 8 billion euros.

- ✓ A reduction in personal income tax amounting to 5 billion euros in 2020, aimed mainly at the middle classes. The measure could, for example, target households with baseline tax incomes below monthly levels in the range of €2,500-3,000, but the details have not yet been finalised and are due to be announced in June.
- ✓ A re-indexing of pensions of less than 2,000 euros a month in 2020 (costing around €1.4 billion) and of all retirement pensions in 2021. The level of the minimum pension to be increased to 1, 000 euros a month.
- ✓ An exceptional premium for businesses, net of tax and contributions, renewed in 2020 (costing around €1 billion).
- ✓ Recovery of unpaid alimony by child benefit agencies.

Other measures

One priority of the French President is to encourage the French to work more. This is not likely to be achieved through a further loosening of the statutory 35-hour week, but through pensions-related measures. The statutory retirement age would be kept at 62, but an incentive system would be introduced to encourage households to work longer and to encourage, but not require, a longer contribution period.

In the education sector, no class from reception to year 3 will be allowed to exceed 24 students. This would lead to the creation of around 10,000 new teaching positions.

To re-balance local government, it has been decided to halt school and hospital closures without the Mayor's agreement by 2021 and to set up "France Services" outlets that will be able to deliver a certain number of public services in each "canton" or local district. There have been 2,054 such districts in France since the 2014 restructuring, or around 20 per *département*.

These last two points would result in abandoning the target to abolish 120,000 public sector jobs over the President's five-year term.

Marked impact on household incomes

The scale of the measures announced, especially those designed to boost purchasing power, is fairly measured and falls significantly short of the demands expressed in the great debate and/or by the *gilets jaunes*. It was obviously not possible to satisfy all these numerous, disparate and sometimes contradictory demands, given the budget constraints and the government's stated priorities. Among those unmet demands are, for example, the restoration of the ISF wealth tax, a cut in VAT or an increase in the Smic minimum wage. Regarding the ecological transition, the President did not announce any practical measures but set up an "Ecological Defence Council". These announcements could, therefore disappoint. According to the opinion polls, two-thirds of French citizens say they are not convinced by the President's announcements.

We should nevertheless point out that the new income support measures announced on Thursday

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25 April supplement a significant series of tax and social security reductions rolled out in recent months via the 2019 budget on the one hand, and last December's purchasing power support plan on the other.

Among the measures included in the 2019 Budget, we can cite the second tranche of the exemption from the *taxe d'habitation* (council tax) in 2019 (€3.8 billion) and the third in 2020 (€3.1 billion), plus the reduction in employee social security contributions implemented in late 2018 and which will have its first full-year effect in 2019 (€4 billion). Conversely, the deindexing of a significant proportion of social benefits (pensions, child benefit) will have a negative impact (-2.5 billion euros in 2019).

Last December's support plan, which came in the wake of the *gilets jaunes* crisis, included tax and social security contribution exemptions on overtime worked (€3.5 billion in 2019 and €0.8 billion in 2020); an increase of around €100 a month for employees paid at Smic level through a sharp increase in the activity premium (€2.5 billion in 2019); the cancellation of a 1.7 percentage point increase in the CSG solidarity contribution on pensions of between 1.200 and 2,000 euros a month (€1.6 billion in 2019); and a one-off premium paid by companies net of tax and contributions (€0.9 billion).

Adding together the three sets of measures, households look set to benefit from a "net" 13 billion euros in support measures in 2019 and from 10 billion euros' worth of new measures in 2020. This represents a 1-point gain in purchasing power in 2019 and a 0.7-point gain in 2020. In view also of a relatively favourable uptrend in per capita wages, households' nominal income should rise sharply in 2019, by 3.6% – its largest increase since 2007 – and by 2.7% in 2020. With inflation forecast at 1% and 1.2% respectively, households' gains in purchasing power are likely to amount to 2.6% in 2019 and 1.5% in 2020.

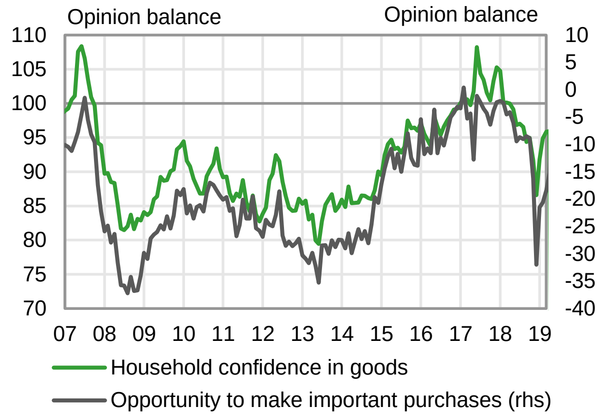
Impact on consumption and growth more uncertain

Household consumption is set to benefit from these important gains in purchasing power. Consumption is forecast to pick up, **but not as strongly as** the gains in purchasing power.

This is partly because household confidence is still fairly low. It deteriorated sharply in the second half of 2018. It picked up a little in early 2019, but at 96 over the past three months (February-April), it is still below trend level (100). More especially, the balance of opinion among households regarding their future financial situation remains low, at -11 over the past three months, compared with the trend -6. In addition, households' fears concerning trends in unemployment have strengthened in recent months. The confidence level remains fragile, therefore and could again deteriorate in view of the multiple economic and political uncertainties in France and elsewhere. It suggests that precautionary savings behaviour will persist.

What's more, the consumer durables purchasing cycle (vehicles, domestic appliances, furniture) risks entering a slowdown phase in 2019 after four years of very strong momentum (+4.2% a year on average).

France: Household confidence



Source : Insee, Crédit Agricole S.A.

Trends in recent months suggest a cautious approach. In Q4 2018, income purchasing power saw a record increase of 1.1% compared with the previous quarter due to the effect of the cut in council tax and social security contributions. But volume consumption stagnated. It was affected by the disruption generated by the *gilets jaunes* movement (demonstrations, blockages) but probably also by a marked deterioration in confidence. The household savings rate rose sharply, from 14.3% in Q3 to 15.2% in Q4.

In Q1 2019, income purchasing power should again be sustained, at +0.7%, on the strength of the support measures in the wake of the *gilet jaunes* crisis. Consumption is upbeat but lower, with an increase of 0.4% over the quarter (first Insee estimate). Consumption of goods is uneven, also, with an increase of just 0.2% in Q1. Households are keeping their savings ratio high and are not spending the surplus accumulated at the end of 2018. Consumption is forecast to grow by 1.4% in 2019, a fairly high rate, but well below the gains in purchasing power (+2.6%).

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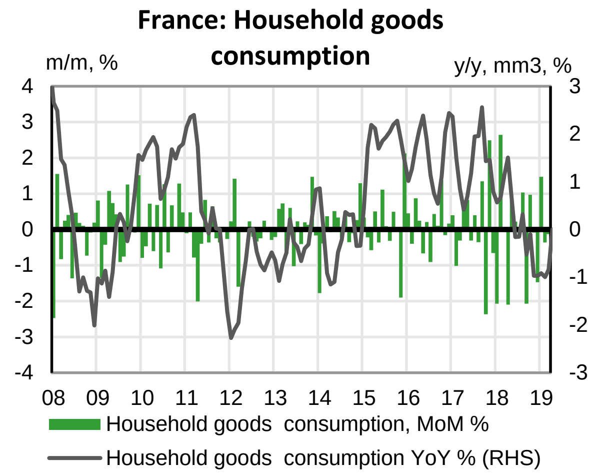

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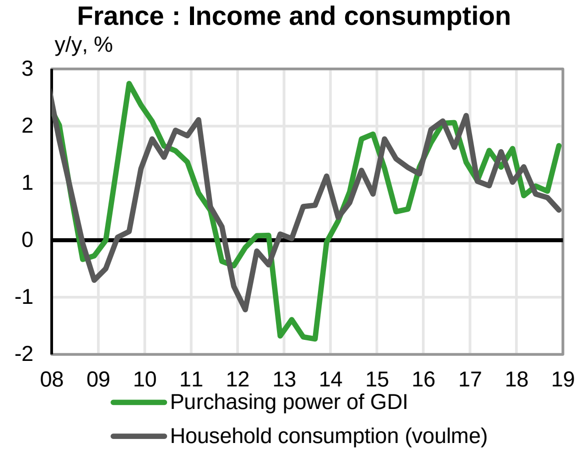

Source : Insee, Crédit Agricole S.A.

GDP increase of 0.3% in Q1 2019

In light of the first estimate published by Insee on Tuesday 30 April, GDP growth reached 0.3% in Q1 2019, relative to Q4 2018. Consumption was fairly sustained, up 0.4% as mentioned above. Conversely, the deterioration in global growth, and in particular the marked slowdown among our European trading partners (Germany, Italy), is adversely affecting the business climate and activity. Despite higher profits partly due to the CICE/contributions switch, the rebound in business investment remains measured, at +0.5%, due to the deterioration in expectations of external markets. And exports have slowed quite sharply, to +0.1% compared with +2.2% in the previous quarter. They are affected by slowing global demand and the carryover effect of large-scale aircraft deliveries recorded in late 2018. The growth carry- over for 2019 stands at 0.8%.

After 2.3% in 2017 and 1.6% in 2018, GDP growth is thus forecast at 1.4% in 2019 (the figure has been revised down slightly compared with our previous forecast of 1.5%) and 1.4% in 2020. The improvement in purchasing power is likely to be partly offset by a rise in households' saving ratio, the import content in consumer spending, and a smaller than previously forecast increase in investment. The household support measures nevertheless explain why, with a lower exposure to world trade, France will fare better than its European trading partners in 2019.

In the short term, this support plan in response to the great debate is set to bolster purchasing power and consumption and deliver honourable growth in 2019-2020. But it is unlikely to resolve the social crisis. The *gilets jaunes* movement and the demands will persist, and we cannot rule out a scenario where the "coagulation of discontent" rolls on.
In the medium term, it seems to us that the President's objectives are unchanged, namely, to carry on with his structural reforms, especially of education and the labour market, to make the French economy more competitive and more innovative, and to bolster potential growth. This could create a virtuous circle with more robust growth that will benefit all categories, a steady decline in unemployment, and an upturn in business and household confidence. But his gamble will not necessarily pay off. The impact of his structural reforms on growth will be long and drawn out. For example, the recovery in competitiveness is gradually falling into place, but so far has not led to the start of an increase in French market share. The international business climate is hardly conducive to this, given the many political, geopolitical and economic risks that could compromise the process of turning the French economy around. ■

	Yearly average (YoY, %)				
France	2016	2017	2018	2019	2020
GDP	1,1	2,3	1,6	1,4	1,4
Households consumption	2,0	1,1	0,8	1,4	1,5
Investment	2,7	4,7	2,9	2,1	2,0
Corporate investment	3,4	5,2	3,9	3,0	2,8
Change in inventories*	-0,3	0,2	-0,4	0,0	0,1
Net exports*	-0,5	0,1	0,6	-0,1	-0,3
Unemployment (Insee)	9,8	9,1	8,7	8,5	8,3
CPI Insee (yoy)	0,2	1,0	1,9	1,0	1,2
Government deficit (% of GDP)	-3,4	-2,8	-2,5	-3,3	-2,2

* Contributions to GDP growth
Source : Crédit Agricole SA, estimates

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