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OVERVIEW

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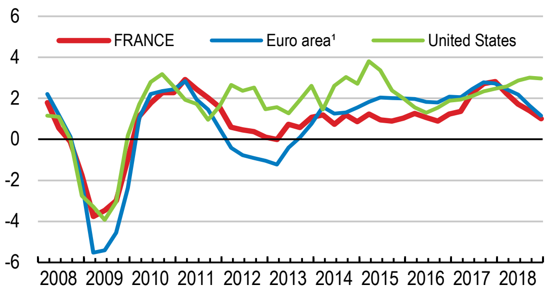
This Overview is extracted from the Economic Survey of France. The Survey is published on the responsibility of the Economic and Development Review Committee (EDRC) of the OECD, which is charged with the examination of the economic situation of member countries.

Executive summary

The French economy is slowing down

Economic growth has slowed down after a gradual recovery. Global economic conditions, monetary policy and structural reforms have supported exports and investment in recent years. However, global uncertainties and the effects of social unrests weighed on activity in 2018. Employment rates remain low and the fiscal situation has not recovered. Real wage growth and productivity gains have not returned to pre-crisis levels, despite a slight rebound in 2017-18.

Figure A. Growth has slowed



1. Euro area member countries that are also members of the OECD (17 countries).
Source: OECD (2019), *OECD Economic Outlook: Statistics and Projections* (database) and updates.

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Consumption and growth will benefit from a boost in households' purchasing power. GDP growth is expected to remain around 1.3% in 2019-20. The expected slowdown among France's main trading partners will weigh on exports and business investment (Table A). On the other hand, employment gains, increasing real wages, lower taxes and oil prices will support household consumption. Social measures taken at the end of 2018 will also increase disposable income and consumption of retirees and low-wage earners.

The main risks surrounding these forecasts are downward. A stronger-than-expected slowdown in growth in advanced economies, particularly in Europe, would reduce exports and investment. In addition, recent social unrests have highlighted the need to fully integrate the redistributive effects of reforms to support their social acceptability and smooth the implementation of the measures needed for more inclusive and sustainable growth. The latest social protests had little impact at the end of 2018, but their persistence could create uncertainty and would weigh on the economic outlook.

Table A. Growth will have a broader base

% change	2018	2019	2020
Gross domestic product (GDP)	**1.6**	**1.3**	**1.3**
Private consumption	0.9	1.5	1.4
Government consumption	1.0	0.9	0.4
Gross fixed capital formation	2.9	2.1	2.0
Exports of goods and services	3.3	2.3	2.7
Imports of goods and services	1.3	2.6	2.7
Unemployment rate	9.1	8.7	8.5
Consumer price index	2.1	1.4	1.5

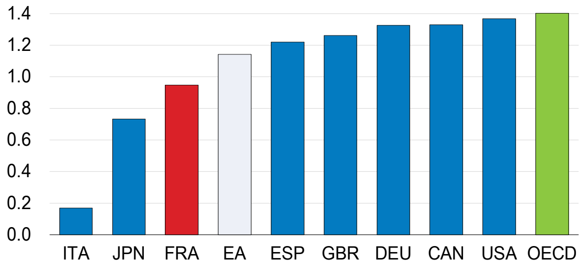
Source: OECD Economic Outlook.

Sluggish growth and job prospects weigh on well-being, while the level of public spending is high

Slowing productivity gains and weak employment rates have reduced GDP per capita growth (Figure B). Productivity growth has decreased over the past ten years, as in most other OECD countries. The employment rate is still one of the lowest among OECD countries, especially for the low-skilled, youngsters and older workers, despite its historically high level. Too many workers have skills that do not match labour market needs and educational outcomes are highly dependent on family background. Unequal access to training has made difficult the professional integration of the youth. Finally, until recently, growing public spending has kept taxes high, weighing on disposable income. As a result, the public debt-to-GDP ratio has increased to close to 100% (Maastricht definition), and has not yet started to decline.

Figure B. Income gains per inhabitant are slow

GDP per capita[1], average annual % growth rate, 1998-2018



1. At constant 2010 USD PPPs.

Source: OECD (2019), *OECD National Accounts Statistics* (database).

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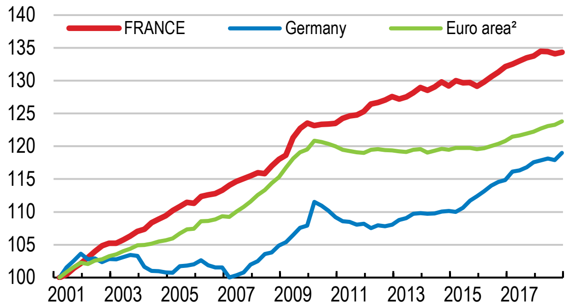
Public spending has grown rapidly. Expenditure control objectives have not made it possible to sustainably reduce the level of public spending, which remains high, despite a recent inflection (Chart C). To reduce the share of public spending in relation to GDP, it will be necessary to review the allocation, the targeting and, if necessary, the amount of some expenditures, to improve the distribution of responsibilities between local governments and to increase the efficiency of their expenditures. Some spending, such as local government operational expenditures and health expenditures, have grown rapidly, despite their recent slowdown. In addition, some expenditures have not had the expected results: educational outcomes largely reflect family background and low-skilled workers have benefitted little from professional training until recently. The government's reform programme to control public spending and improve its allocation through expenditure reviews should be implemented more rapidly. The proposed merger of welfare programmes and housing benefits would also help better steer social assistance. In addition, pension expenditures are sizeable, and new measures to raise the effective age of labour market exit will be needed.

Figure C. Public spending has grown rapidly

Real public spending[1], index 2001-Q1=100



1. Deflated by the GDP deflator.
2. Euro area member countries that are also members of the OECD (17 countries).

Source: OECD (2019), *OECD Economic Outlook: Statistics and Projections* (database) and updates.

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Streamlining the tax system would support economic activity. A number of narrow-based low-revenue taxes affect businesses and should be reviewed to simplify the tax system. VAT exemptions and reduced rates are sizeable and some of them benefit too little low-income households. Limiting these exemptions would promote economic activity and a more redistributive tax structure, while allowing to reduce the tax burden. Environmental taxes must also better reflect environmental and social costs. Their social acceptance will require gradual changes, without increasing the tax burden, and compensation measures to promote equity.

Competition-enhancing reforms to regulatory settings would raise productivity and innovation. An ambitious business simplification programme could ease firm entry and growth. Moreover, entry and conduct regulations remain stringent in several professional services – such as accountants, notaries and pharmacists – weighing on productivity and employment. To ensure such regulations are in the public interest, reviewing existing regulations from a competition perspective would be helpful.

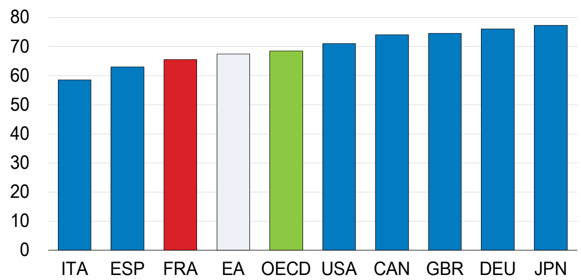
Stronger and more inclusive growth will require ambitious reforms. Improving labour market outcomes, increasing competition, limiting public spending and eventually reducing tax rates should be priorities. Measures currently being implemented by the authorities could increase GDP per capita by 3.2% after 10 years and those proposed in this *Survey* would increase that gain to 5.1%. The gains from these reforms would be concentrated in the middle and lower-middle categories of the income distribution. The implementation of these reforms will need to put in place adequate compensation mechanisms, ensuring they are perceived as a means to promote equal opportunities.

Labour market reforms must foster more and better jobs

Employment rates remain low in international comparison (Figure D), despite a recent increase. The low-skilled, young and older workers have particularly low employment rates. The low level of qualification of part of the labour force combined with tight labour market regulations have reduced access to employment. Support and training measures still need strengthening, particularly for the long-term unemployed, low-skilled and young people, as foreseen in the Youth Guarantee programme, the Skill Investment Plan and the antipoverty strategy. The government is continuing to lower labour cost and increasing wage top-ups for low-wage earners which will help improve their situation on the labour market and their disposable income.

Figure D. Employment rates are low

15-64 year-olds, % of the population, 2018-Q4 or latest available



Source: OECD (2019), *OECD Short-Term Labour Market Statistics* (database).

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Ensuring supply of the right skills would boost jobs and productivity. Businesses report increasing skill shortages, while the share of young people who are not in employment, education or training is persistently high, despite a recent improvement. Professional training programmes have so far had low returns on investment. The government has initiated welcome reforms to improve access to up-skilling and re-skilling programmes and their quality and the apprenticeship reform could allow reducing mismatches between educational programmes and firm needs. Regularly evaluating vocational training and subsidised job programmes, as planned, will improve their quality. Programmes that have been found to have a positive impact on the employment prospects of participants should be expanded. Ongoing reforms also aim to develop apprenticeship. However, for these reforms to reach their full potential, it will be necessary to strengthen relationships between firms and the educational system and to continue to reduce dropout rates.

Productivity and income gains would benefit from easing labour market transitions. Recent reforms promote a more flexible labour market, through lower uncertainty about separation costs and the development of firm-level bargaining. However, short-term contracts have rapidly increased. Containing the use of short-term contracts would require increasing the relative cost of short-term hiring and reforming the unemployment insurance system so that it does not encourage recurrent short-term employment periods and unemployment spells. The authorities foresee to take measures in this direction. Moreover, favouring workers' mobility would help match job offers and job seekers. Better public transport and lower housing transaction costs would increase the efficiency of local labour markets.

Public investment should support stronger, more sustainable and inclusive growth

Public investment in France should concentrate on the maintenance and upgrading of the capital stock in some sectors. The stock of public capital is extensive (Figure

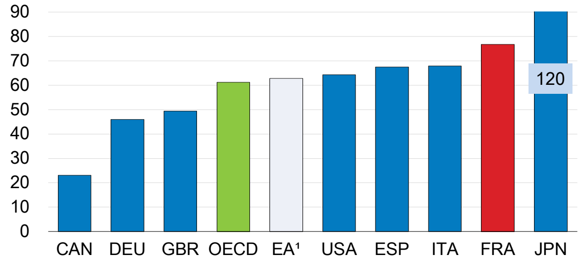
E) and the perceived quality of infrastructure is high. Yet, in some sectors such as rail transport or health care, a lack of maintenance has hampered the efficiency of existing infrastructure. Promoting socio-economic efficiency in project selection would help make the most of new investments and concentrate investments where they are the most needed.

Improving the efficiency of public investment will rely in large part on local governments, as they represent the majority of public investment. Continuing efforts to streamline local governments and clearly allocating responsibilities across administrative levels will help achieve economies of scale and scope. Moreover, revising intergovernmental transfers to better tackle disparities in tax-raising abilities and costs faced would ensure that local resources match local needs. This would also help contain public expenditures.

Transport and energy investments need to better tackle environmental challenges. The transport sector accounts for a large share of pollution and emission reductions have been slow, while urban pollution remains high in some cities. Infrastructure planning needs to better reflect health and environmental costs and be consistent with government's targets for reducing greenhouse gas emissions. The increase in the shadow price of carbon used in socio-economic analyses goes in this direction.

Figure E. The stock of public capital is high

% of GDP, 2015



1. Euro area member countries that are also members of the OECD (17 countries).

Source: IMF (2017), *Investment and Capital Stock Statistics* (database), International Monetary Fund, Washington, D.C.

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Continuing reforms that give universities more autonomy will help reap the full benefits of investment plans. A selected increase in funding for public research should go along with reforms to raise universities' autonomy over their human resource policies. Channelling additional funding through competitive processes and fostering a closer involvement with the private sector will also be key to foster innovation and knowledge diffusion.

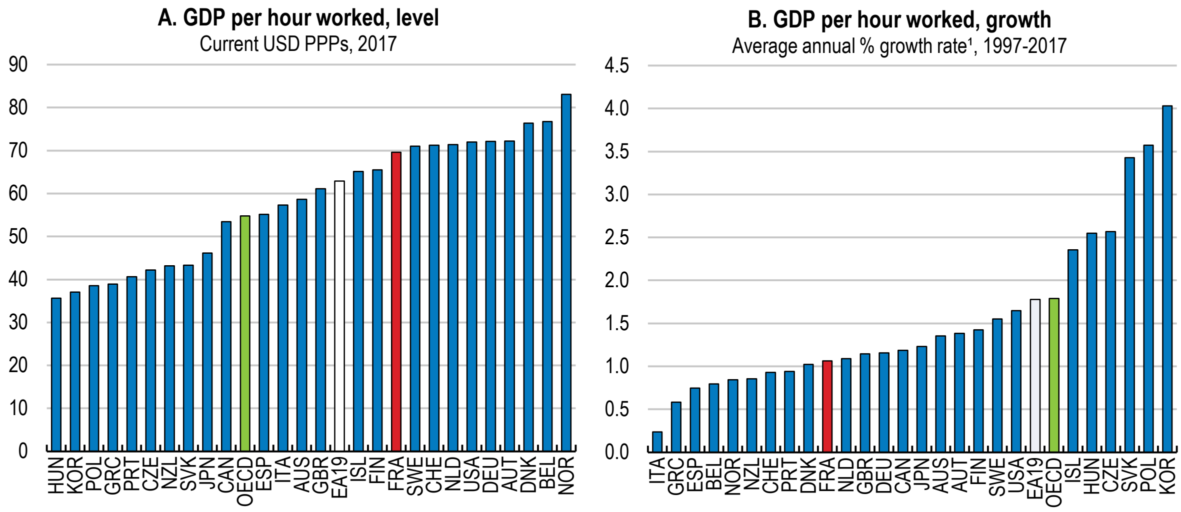
The quality of the digital infrastructure could improve significantly. Broadband penetration and internet speed are lagging relative to best performing countries. Efficient, reliable, and widely accessible digital infrastructure will be key to reap the full benefits of digitalisation. Investments in digital public administration will also help achieve productivity gains in public administration and contribute to increase public spending efficiency.

MAIN FINDINGS	KEY RECOMMENDATIONS
Developing a long-term strategy to boost growth and reduce the fiscal deficit and public debt	
Structural reforms are needed to increase growth. However, these reforms may have a social cost in the short run, limiting their acceptability.	Continue reforms conducive to more inclusive and sustainable growth and promote their acceptability by minimising and/or offsetting their potential short-term negative effects on selected population groups.
Public debt is high and elevated public spending requires high taxes that weigh on economic activity. The government is undertaking targeted public expenditure reviews to identify gains in spending efficiency.	Continue fiscal consolidation durably to ensure a gradual decline in the debt-to-GDP ratio. Announce precise targets for reducing public expenditures in spending reviews.
VAT exemptions and reduced rates are important and some of them benefit little low-income households. Tax expenditures are sizeable and some have been reinstated (such as overtime tax deduction) despite weak evidence of being beneficial.	Simplify the tax system by reducing the use of exemptions and reduced rates that do not benefit the lowest-income households, and reduce tax rates. Systematically review tax expenditures after some years of implementation and phase them out if not deemed helpful.
The pension system is fragmented and pension spending elevated. The effective retirement age is low.	Review pension penalties and bonuses to encourage an increase in the effective retirement age and gradual retirement.
Existing infrastructure may have suffered from a lack of maintenance and upgrading in some sectors (rail transport, hospital and tertiary education). The health sector has set up a committee to help prioritise investment projects.	Continue to extend the investment selection framework in place in the health sector to other sectors. Strengthen the share of infrastructure maintenance spending in public investment.
Fostering employment to make growth more inclusive	
The long-term unemployment rate remains high and employment rates are weak, notably for the low-skilled people.	Mainly focus employer social security contribution exemptions on low wages.
The skills of the population aged over 24 are lagging. The quality of lifelong training programmes is unequal.	Ensure access to transparent information and effective monitoring of the quality of lifelong learning programmes through additional evaluations and strengthened counselling.
The use of short-term contracts is recurrent and widespread. Some unemployment insurance rules can encourage an excessive use of short-term contracts.	Restrict the possibility of receiving unemployment benefits during repeated periods of temporary employment and the reloading of rights over short employment spells. Modulate labour costs to reduce the excessive use of short-term contracts.
School to work transitions are difficult, notably for low-skilled youth. Intergenerational mobility is weak. The poorest households would benefit most from access to childcare, as it raises women's employment.	Strengthen apprenticeship in secondary vocational schools, and social and economic integration programs for inactive youth. Speed up the development additional childcare services for low-income households and in poor neighbourhoods.
The take-up of some social programmes and follow-up measures is weak.	Merge welfare programmes and in-work benefits (*Prime d'Activité*), taking into account housing benefits and public housing in overall household resources.
Improving productivity and competitiveness	
Despite some progress, barriers to entry and competition in services remain high. Business regulation can be unduly restrictive.	Engage an independent institution to conduct a thorough review of all existing and proposed regulations affecting firms.
Science-industry collaboration remains weak, as is the share of competitive project financing of public research.	Continue to increase universities' autonomy over their programmes and human resource policies, while taking into account their public service function. Continue to increase the budget of the National Research Agency.
The low flexibility of housing supply hinder access to housing for the poor and prevent greater residential and labour mobility.	Encourage a more flexible rental market by developing shorter contracts and the use of rental guarantees. Lower transaction costs on housing, notably real estate transfer taxes.
Recalibrating the economy for greener growth	
The pricing of the environmental costs of fossil fuels is uneven. The transport sector is responsible for much of the greenhouse gas emissions and air pollution. However, diesel taxes do not reflect all of the negative effects of its use on the environment and health. Joint increases in diesel taxes and the carbon tax have not been socially accepted.	Better take into account environmental externalities in transport taxation and develop flanking measures for the most affected populations over the short term.
France is a major consumer of pesticides posing significant risks to health and the environment.	Strengthen the risk assessment of phytosanitary products, notably the effect of their interaction, and contribute to European research to gradually replace the substances identified as the most harmful.

Key policy insights

The French economy has a high productivity, ensuring standards of living in line with the OECD average (Figure 1, Panel A). This good economic performance is underpinned by a well-rated infrastructure, a dynamic working-age population, long life expectancy in good health, and a tax and transfer system that significantly reduces income disparities and poverty rates (Figure 2, Panel A). Moreover, from 2015 to end-2017, monetary policy, the global economic upturn and structural reforms have bolstered a gradual economic recovery.

Figure 1. France's productivity is high, but its growth lags peers



1. At constant 2010 USD PPPs.
Source: OECD (2019), *OECD Productivity Statistics* (database).

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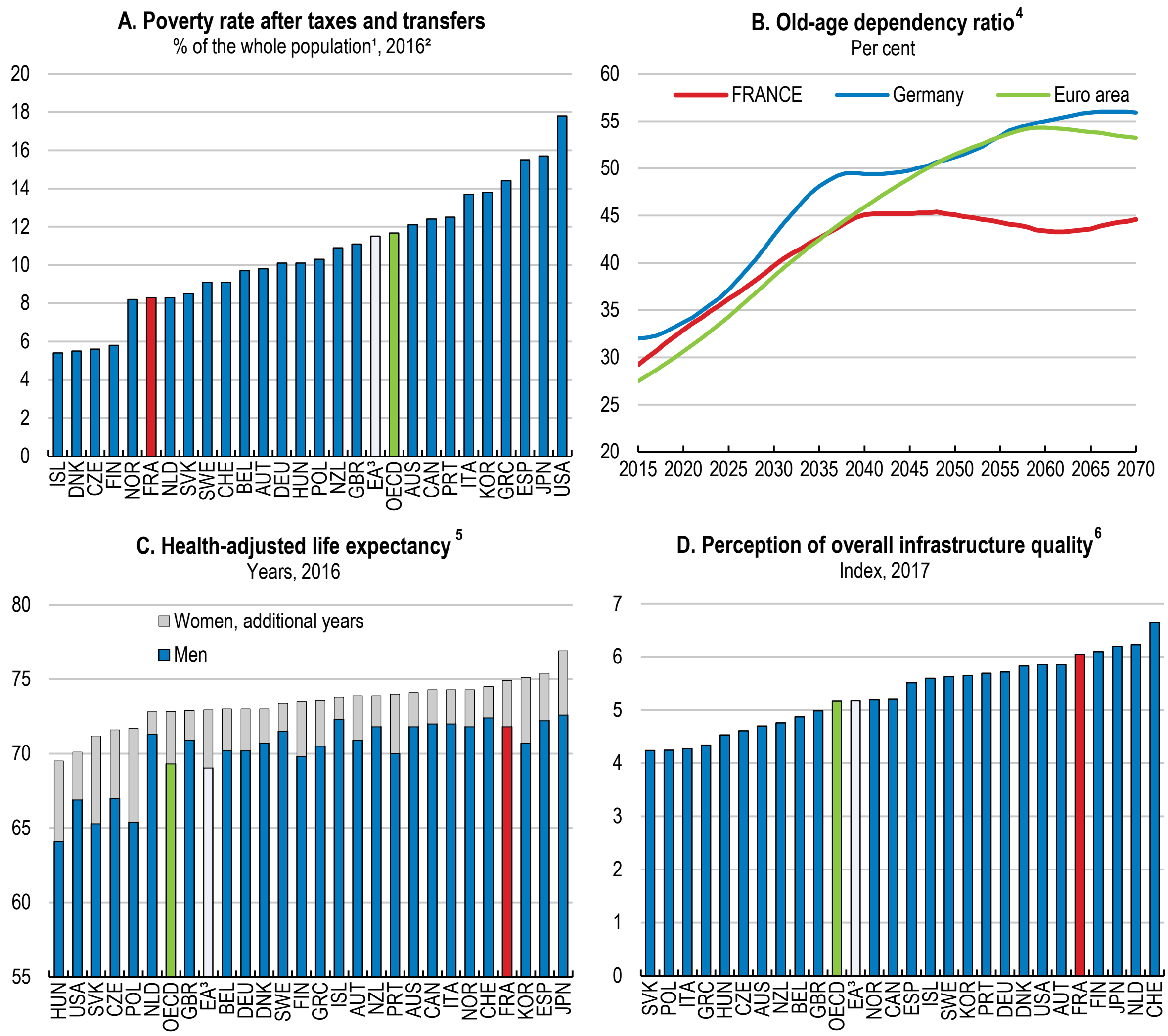
However, growth slowed in 2018 and economic performance has disappointed over the medium term. Material living standards, as measured by GDP per capita, are constrained by slowing productivity growth, as in most other advanced economies (Figure 1, Panel B), and employment rates are relatively low (Figure 3). Despite growing real wages, households' purchasing power per unit of consumption, a better measure of living standards, has stagnated over the past ten years (INSEE, 2018). Too many low-skilled and young people are excluded from the labour market, and unequal educational outcomes weaken inter-generational mobility. Elevated public spending, while contributing to lower income disparities through extensive social expenditures, requires high taxes that limit firms' ability to create jobs, and reduce incentives for people to work. This has pushed the public debt-to-GDP ratio close to 100% of GDP (Maastricht definition). Regional GDP per capita disparities have also increased, even though regional disposable income inequalities have decreased over the long term.

Figure 2. France has many assets



1. At 50% of household's median equivalised income.
2. Or latest available year.
3. Euro area member countries that are also members of the OECD (17 countries).
4. Ratio of the population 65 and over to population 15 to 64 years according to Eurostat (2018)'s baseline projections.
5. Average number of years that a new-born infant can expect to live in full health by taking into account years lived in less than full health due to disease and/or injury (HALE). The countries are ranked according to women's life expectancy.
6. Index from the lowest perceived quality (0) to the highest (7) based on the assessment of business leaders operating in the country.

Source: OECD (2019), *OECD Income Distribution and Poverty Statistics* (database); Eurostat (2018), "Baseline projections: Demographic balances and indicators", *Eurostat Database*; WHO (2018), *Global Health Observatory data repository* (database), World Health Organisation, Geneva; WEF (2018), *The Global Competitiveness Report 2017-2018* (database), World Economic Forum, Geneva.

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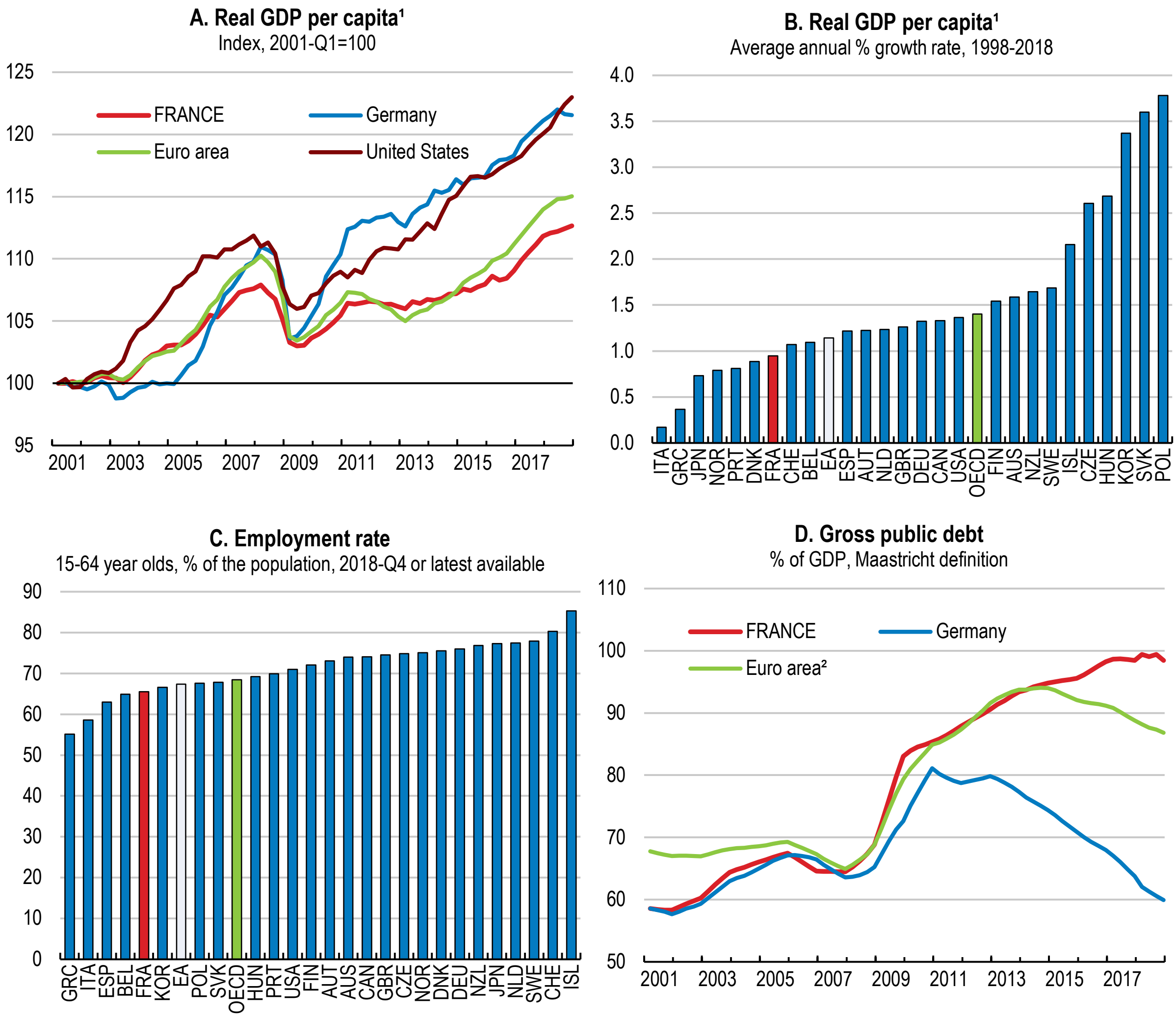
The government has undertaken a series of pro-growth and pro-inclusiveness structural reforms to boost medium-term economic activity and put public finance on a firmer footing (Box 1). Comprehensive labour reforms, lower business and labour taxes and a welcome productivity-enhancing public investment plan should help raise medium-term growth and boost employment. Environmental considerations have also been a concern, although targets for improvement have been set at a relatively distant future. The 2017 Climate Strategy foresees a net zero carbon footprint by 2050, the ban of sales of fossil fuel vehicles from 2040 and a steady increase in the carbon tax (i.e. the carbon component of domestic consumption taxes). However, the government decided to cancel the foreseen 2019 hikes in energy taxes following the "gilets jaunes" protests. Spending reviews and a planned pension reform are set to increase the effectiveness of public expenditures and make room for tax cuts, while preserving public investment. OECD estimates, covering a broad part of ongoing reforms, show that they could boost GDP per capita by 3.2% at a ten-year horizon and would mostly benefit middle- and lower-middle income households (Box 1).

Figure 3. Slow income gains, low employment and high public debt are key challenges



1. At constant 2010 USD PPPs.
2. Euro area member countries that are also members of the OECD (17 countries).
Source: OECD (2019), *OECD National Accounts Statistics*, *OECD Short-Term Labour Statistics* and *OECD Economic Outlook: Statistics and Projections* (databases) and updates.

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Box 1. Key measures from the government's 2017-22 reform agenda

- **Labour market reforms** (Chapter 1): the aim of the 2017 *Ordonnances* is to facilitate collective bargaining and firm-level negotiations, as well as to reduce legal uncertainty surrounding dismissals for permanent contracts and to regulate the administrative extensions of sector-level agreements by setting up an independent committee to evaluate the economic and social effects of administrative extensions. New unemployment insurance rights are open to some self-employed workers and to resigning employees subject to conditions.
- **Measures to promote initial education and adult learning** (Chapter 1): A 2018 law (*loi pour la liberté de choisir son avenir professionnel*) reforms the apprenticeship system to boost its take-up by the youth and bring it closer to firms' needs. This law also reforms the vocational training system and aims to strengthen the quality of training by simplifying its funding to make it more attractive. Moreover, a new training plan (*Plan d'investissement dans les compétences*) is increasing funding for access to training for young low-skilled workers and long-term unemployed. A 2018 law (*loi sur l'orientation et la réussite des étudiants*) has engaged a global reform to raise individualised support and counselling for students, notably to reduce failure rates during undergraduate university studies.
- **Anti-poverty strategy** (Chapter 1): the government has increased in-work benefits – *Prime d'activité* – to support low-income workers. The government plans to boost access to early childhood education and care in poor neighbourhoods.
- **Pension reform:** the government plans to move to a single pension system to improve transparency, foster labour mobility, lower management costs, and ensure the long-term financial sustainability of the pension system. Discussions about this reform started in 2018 and the reform should be voted in 2019.
- **Healthcare reform**: the 2022 healthcare plan ("Ma Santé 2022") aims at improving prevention and co-ordination among care providers. This plans also reforms medical studies in order to better tailor the number of doctors to social needs. Moreover, the plan "100% santé" aims to provide access to all for optical, hearing and dental care.
- **Education reforms:** Following a 2019 law (*loi "Pour une école de la confiance*"), education will be compulsory for three year olds (instead of six year olds) from the 2019 school year school to better address educational inequalities that start building up from early ages. At the primary level, class size in grade 1 and grade 2 in poor neighbourhoods was halved to improve knowledge transmission and reduce socio-educational inequalities by targeting the most vulnerable groups.
- **Effectiveness of public spending** (Chapter 2): the government targets to reduce the weight of current public expenditure by three points of GDP over 2017-22. Specific spending reviews aim at cutting current expenditures.
- **Tax reforms:** An increase in the proportional personal income tax (*contribution sociale généralisée*, CSG) allowed for a reduction in employee social contributions in 2018. The wealth tax (*impôt sur la fortune*) was focused on real estate assets only (*impôt sur la fortune immobilière*), and the taxation of capital was set to a flat rate of 30%. The headline corporate income tax rate will decrease to 25% in 2022. A permanent reduction in employer social contribution rates replaced the tax credit for competitiveness and employment (*crédit d'impôt pour la compétitivité et l'emploi – CICE)* in 2019. The government is phasing out the residency tax (*taxe d'habitation*) for middle-income households (80% of the

population) by 2020. By contrast, taxes on tobacco will continue to increase substantially, and environmental taxation increased in 2018.

- **Business environment and product market reforms:** the draft PACTE bill announced in 2018 smoothed some regulatory thresholds to boost firm growth. The reform of the national railway company (SNCF) also aims to prepare the opening up of domestic rail passenger transport to competition and foresees that the government will take back EUR 35 billion of SNCF's debt by 2022.
- **2017 Climate Strategy** (Chapter 2 and below): The National Low Carbon Strategy (*Stratégie Nationale Bas-Carbone*, SNBC) describes France's roadmap for achieving carbon neutrality by 2050. It sets targets for reducing greenhouse gas emissions in the medium term by setting carbon targets not to exceed every five years. The Multiannual Energy Plan (*Programmation pluriannuelle de l'énergie*, PPE) presents a strategy to decarbonise France's energy mix for the next ten years: the share of renewable energies will have to reach 32% of final energy consumption by 2030.
- **Transport and mobility** (Chapter 2): the 2018 draft bill on mobility (*loi d'orientation des mobilités*) plans to reduce car dependency by ensuring that the entire territory is covered by local authorities organising mobility. The bill also includes a program of investments in transport infrastructure for the period 2019-27, prioritising daily transport.

Source: République Française (2018), National reform programme 2018; République Française (2018), Projet de loi de finances pour 2019.

Looking forward, France should capitalise on this reform agenda and take further measures to improve public spending efficiency and increase high-quality jobs, two of the main issues discussed in this Survey. The main OECD recommendations in this Survey could raise GDP per capita by an additional 2 percentage points at a ten-year horizon and reduce the public spending to GDP ratio by 2 points in the long term. To do so, productivity growth across the business sector must be revived through policy settings that facilitate the expansion of high potential enterprises and exporting firms. This would help address France's long-standing export share decline, even though it has stabilised in recent years.

These reforms would address the social challenges of long-term unemployment and inactivity, difficulties in accessing the labour market, in particular for low-skilled youth, and significant inequalities of opportunity that result in low equity in access to quality education and very low intergenerational mobility. The ongoing national debate (*Grand débat national*) is an opportunity to effectively communicate the gains of these reforms and could avoid a political polarisation and the risk of legislative impasse that could lessen the chances to make changes (Alesina, Ardagna and Trebbi, 2006). To be socially acceptable and politically feasible, the reform agenda will need to be introduced without completely eliminating acquired rights. This implies to strike a balance between a partial recognition of acquired rights, to the extent that public finances can accommodate it, possible compensations of the aggregate impacts of reform packages, along with mechanisms to support the population in the reform process (OECD, 2015).Against this background, the main messages of this *Survey* are:

- Continuing pro-growth reforms, in line with recent measures, is key to further reducing unemployment. However, short-term negative impacts on some categories of the population should be compensated to ensure the social acceptability of the reform process.

- Reducing public spending in relation to GDP is needed to improve the fiscal position, and lower tax rates in the long run, particularly on labour. Government spending policies should focus on ensuring investment and social spending are well targeted raising and public administration efficiency.
- Raising well-being will depend on strengthening skills and greater inclusion of low-skilled workers in the labour force. This requires increasing the quality of education, reforms to ensure high-quality training programmes benefit everyone and measures to reduce the use of short-term contracts, as the government wishes.
- Continuing to reduce administrative barriers to entry and unduly restrictive regulations will raise competitive pressures and ensure favourable conditions for young and dynamic firms. This would boost productivity gains and innovation.

Economic growth has peaked

The economic outlook has weakened, but remains positive

GDP growth is expected to be around 1.3% in 2019-20. While in 2017 a solid rebound in exports and investment by businesses and households pushed growth to a level of 2.3% unprecedented over the past ten years, it stood at 1.5% in 2018. Exports and household investment slowed down. Household consumption was also disappointing as the savings rate increased. Yet, business confidence remains above its historical average, although it fell sharply in 2018. Relatively accommodating monetary conditions, corporate tax cuts, and the ongoing recovery in profit margins are stimulating business investment, despite slowing external demand (Table 1 and Figure 4).

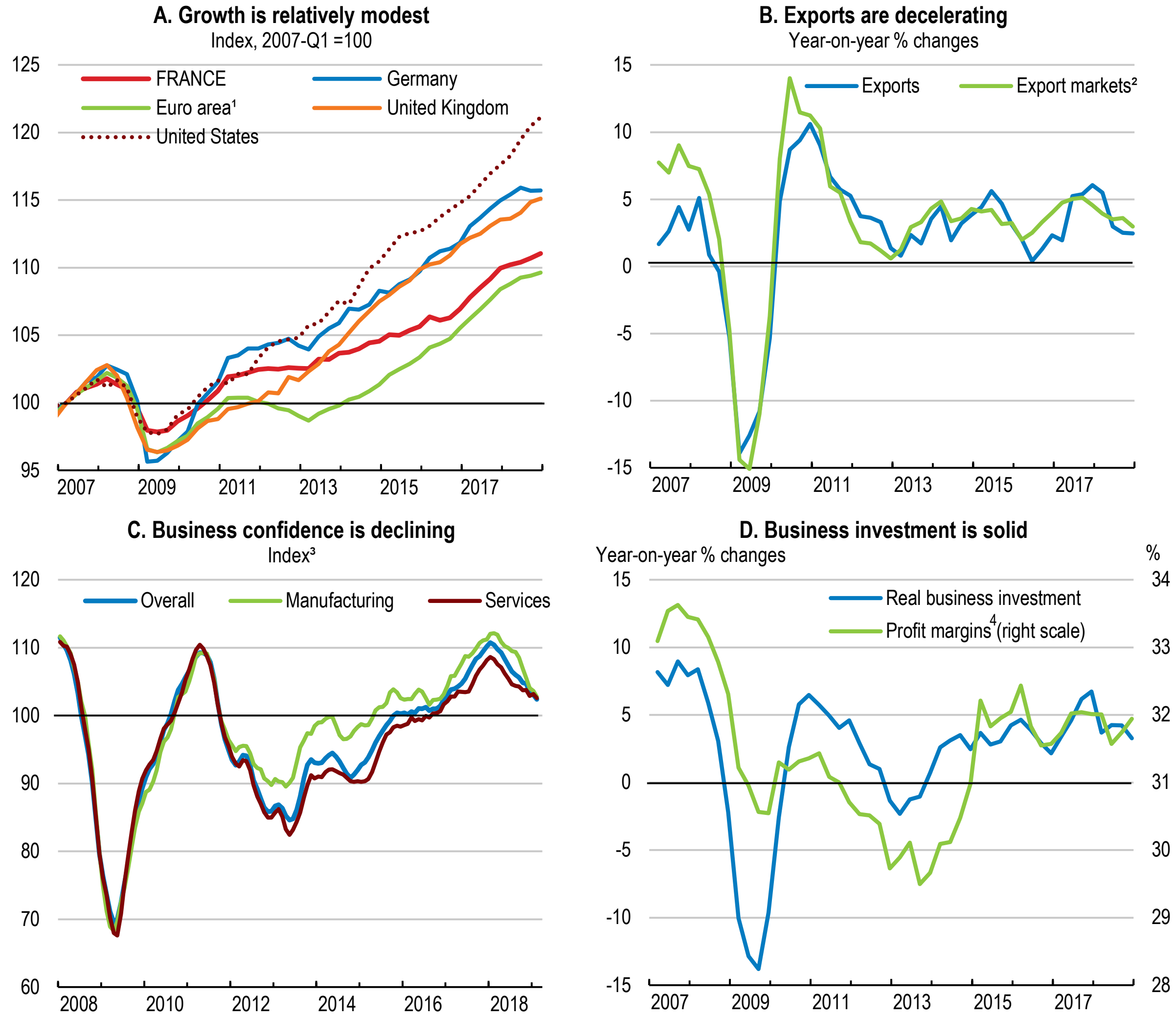
Table 1. Macroeconomic indicators and projections

	2015	2016	2017	2018	2019	2020
	Current prices EUR billion	Percentage changes, volume (2014 prices)				
GDP	2198.3	1.1	2.3	1.6	1.3	1.3
Private consumption	1188.5	1.9	1.2	0.9	1.5	1.4
Government consumption	523.4	1.4	1.4	1.0	0.9	0.4
Gross fixed capital formation	472.6	2.7	4.7	2.9	2.1	2.0
Of which: Residential	113.0	2.8	5.4	1.8	-1.2	0.4
Non-residential	284.7	2.7	4.5	3.3	3.1	2.5
Final domestic demand	2184.5	2.0	2.0	1.4	1.5	1.3
Stockbuilding1	26.4	-0.4	0.2	-0.4	-0.1	0.0
Total domestic demand	2210.9	1.6	2.2	0.9	1.4	1.3
Exports of goods and services	672.2	1.5	4.7	3.3	2.3	2.7
Imports of goods and services	684.8	3.1	4.1	1.3	2.6	2.7
Net exports1	-12.6	-0.5	0.1	0.6	-0.1	0.0
Other indicators (% change, unless otherwise specified):						
Potential GDP	-	1.1	1.1	1.3	1.3	1.3
Output gap[2]	-	-1.9	-0.7	-0.5	-0.5	-0.5
Employment	-	0.6	1.1	0.9	0.5	0.5
Unemployment rate[3]	-	10.1	9.4	9.1	8.7	8.5
GDP deflator	-	0.2	0.7	0.9	1.4	1.4
Consumer price index	-	0.3	1.2	2.1	1.4	1.5
Core consumer prices	-	0.6	0.5	0.9	0.7	1.1
Household saving ratio, net[4]	-	8.3	8.5	8.6	9.1	9.0
Trade balance[5]	-	-0.8	-1.1	-0.9	-1.0	-0.8
Current account balance[5]	-	-0.8	-0.6	-0.7	-0.7	-0.5
General government financial balance[5]	-	-3.5	-2.8	-2.5	-3.2	-2.3
Underlying government financial balance[2]	-	-2.2	-2.1	-2.6	-2.3	-2.4
Underlying government primary balance[2]	-	-0.5	-0.4	-0.5	-0.8	-1.0
General government gross debt[5]	-	125.6	124.3	124.8	125.9	125.4
General government debt, Maastricht definition[5]	-	98.0	98.4	98.4	99.8	99.7
General government net debt[5]	-	82.6	80.1	80.7	81.8	81.3
Three-month money market rate, average	-	-0.3	-0.3	-0.3	-0.2	0.2
Ten-year government bond yield, average	-	0.5	0.8	0.8	1.0	1.2

1. Contributions to changes in real GDP, actual amount in the first column.
2. As a percentage of potential GDP.
3. As a percentage of the labour force.
4. As a percentage of household disposable income.
5. As a percentage of GDP.

Source: OECD (2019), OECD Economic Outlook: Statistics and Projections (database) and updates.

Figure 4. Growth has peaked



1. Euro area member countries that are also members of the OECD (17 countries).
2. Export market growth with destination markets as of 2010.
3. Standardised index, with average 100 and standard deviation 10; 3-month moving averages.
4. Non-financial corporations, as a percentage of their gross value added.

Source: OECD (2019), *OECD Economic Outlook*: *Statistics and Projections* (database) and updates; INSEE (2019), "Indicateurs de climat des affiares" and "Comptes nationaux trimestriels", *INSEE databases*; INSEE (2018), *Point de conjoncture - Octobre 2018*.

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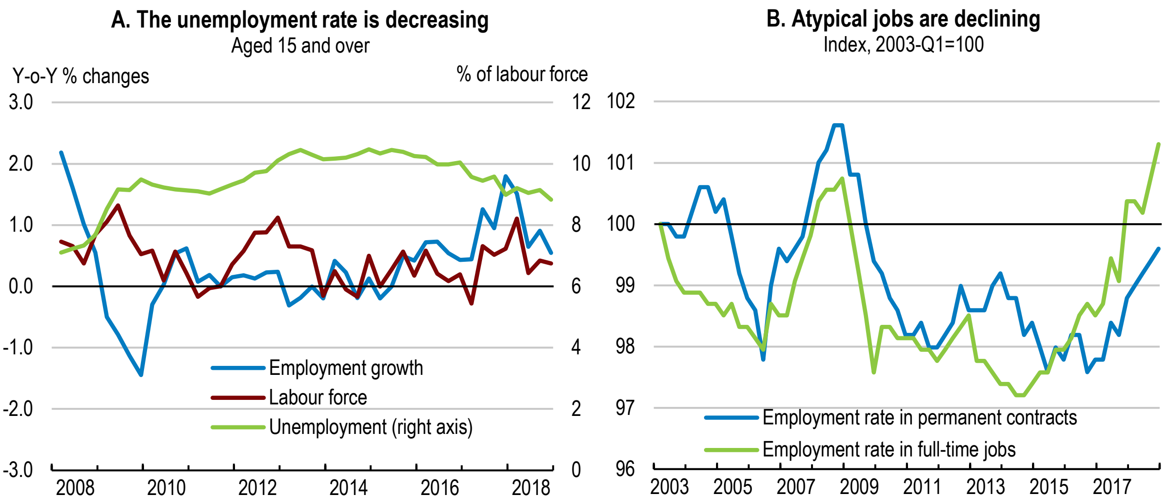
In the context of slowing global growth and France's main European partners, exports and business investment would gradually slow down. However, France appears more resilient than its main partners. Consumption would rise strongly in 2019, supported by the current improvement in the labour market, some tax cuts, the decline in oil prices and the fading negative effects of the end-2018 social protests (Figure 5 and Figure 6). The new social measures, taken at the end of 2018 and designed to promote disposable income following the "gilets jaunes" movement, represent around 0.4% of GDP in 2019, which would also stimulate consumption from pensioners and low-wage workers. In addition, the still favourable financing conditions and the relatively low level of household debt, while on the upward trend, will support household investment.

Figure 5. The labour market is improving



Source: OECD (2019), *OECD Economic Outlook: Statistics and Projections* (database) and updates; INSEE (2019), Enquête emploi 2019.

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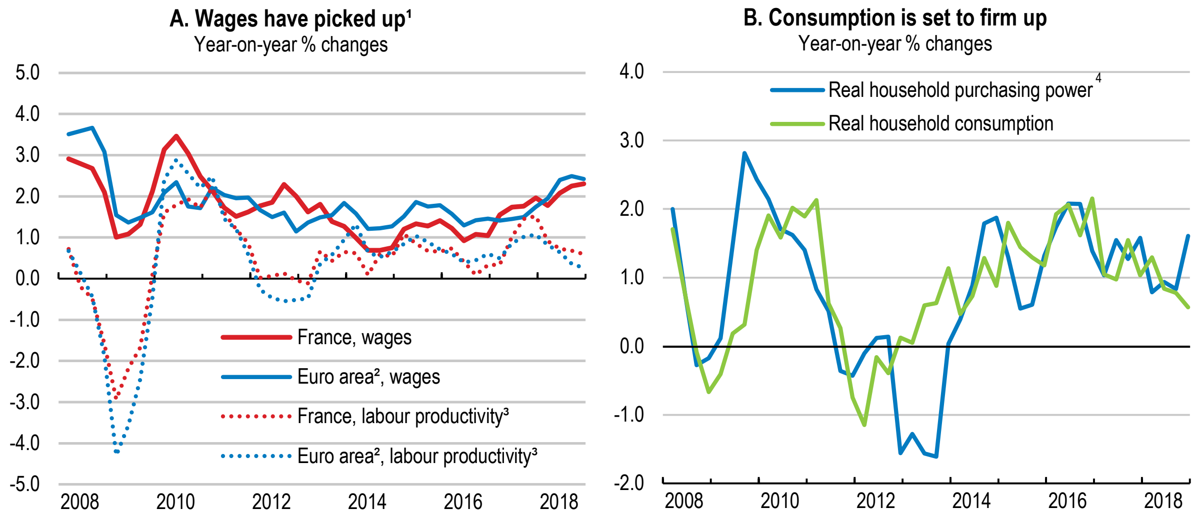
Figure 6. Rising wages support household income and consumption



1. Nominal wages per employee.
2. Euro area member countries that are also members of the OECD (17 countries).
3. Productivity per person employed.
4. Gross household disposable income deflated by the private final consumption expenditure deflator.
Source: OECD (2019), *OECD Economic Outlook: Statistics and Projections* (database) and updates.

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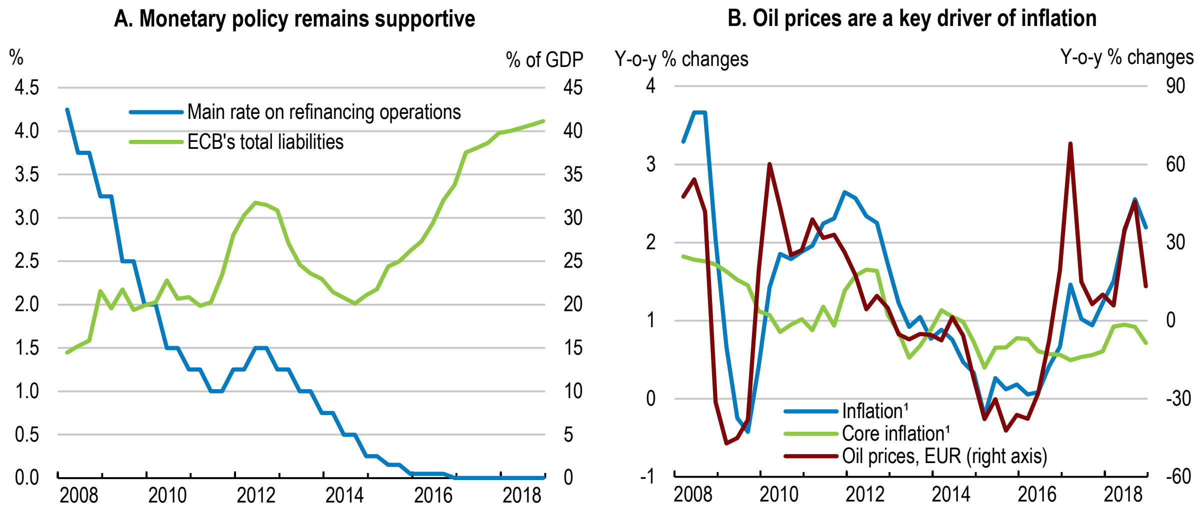
After a temporary rebound in 2019, the fiscal deficit is expected to decline substantially in 2020 (Table 1). A large one-off business tax reduction – the tax credit for competitiveness and employment (CICE), Box 1 –, lower-than-expected consolidation efforts related to social unrest and the cancellation of environmental tax increases will push the deficit upwards in 2019. However, the deficit is set to be close to 2.3% of GDP in 2020, reflecting the transitional costs of the CICE reform in 2019 amounting to nearly 1% of GDP and efforts to reduce public expenditures. Public debt will remain at a historically high level, close to 100% of GDP (Maastricht definition).

Core inflation will increase modestly (Figure 7). Ongoing economic growth, although it is slowing, will support a moderate improvement in the labour market situation. A gradual pick-up in wages along with still accommodative monetary policy conditions are supporting a gradual increase in underlying inflation. However, headline inflation is projected to slow down in 2019-20, reflecting the decline in oil prices at the end of 2018.

Figure 7. Core inflation remains subdued



1. Harmonised indices.

Source: OECD (2019), *OECD Economic Outlook: Statistics and Projections* (database) and updates; INSEE (2019), *"Prix du pétrole et des matières premières importées", Information Rapides, N° 46;* ECB (2018), *"Financial Market Data: Official Interest Rates"*, Statistical Data Warehouse, European Central Bank, Frankfurt.

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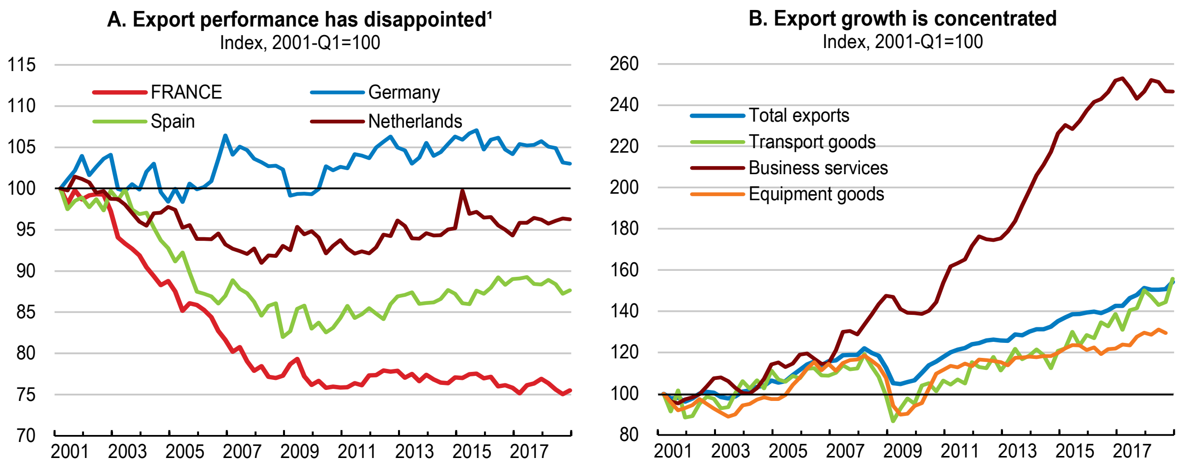
In the near term, risks to this outlook are significant. A more severe slowdown than expected in advanced economies, particularly in Europe, would have adverse effects for exports and investment. Moreover, disruptions related to ongoing social protests, particularly those of the "gilets jaunes" could, if they worsened, reduce economic activity in the short run as well as consumer and business confidence. Consumption growth might turn out stronger or weaker than expected, as the impact of ongoing tax changes, such as the move to a withholding personal income tax, on consumer confidence and saving behaviour are hard to predict. A number of large possible shocks could also alter the economic outlook significantly (Table 2).

Table 2. Low probability events that could lead to major changes in the outlook

Vulnerability	Possible outcome	Possible policy action
A steep rise in protectionism globally markedly reduces trade and the demand and prices for France's exports.	A large and prolonged reduction in export production activity leads to lower investment and job losses, harming incomes and government revenues.	Continue to work (in the context of international collaboration) towards free markets and improvements to the rules-based trade system. Strengthen the economy's resilience and workforce adaptability to changes in the global economy.
Disorderly exit of the United Kingdom from the European Union.	A disorderly exit of the United Kingdom from the EU, a major trading partner for France, could severely hurt consumer and business confidence, resulting in lower investment. This could also lead to severe congestion in some seaports. At the same time, the relocation of some financial services could support economic activity in France.	Set up contingency plans as planned. Work for a close economic relationship between the UK and the EU while maintaining the integrity of the EU's internal market.
Prolonged and heightened social unrests.	Prolonged and heightened social protests would hurt private consumption and business investment as well as exports through weaker tourism. The authorities' ability to reform would also be adversely affected.	Intensify consultation efforts with all stakeholders during the *Grand débat national*. Better involve the population in the reform process by outlining the expected effects. Offset the potential short-term negative impacts of certain reforms.

Trade performance is a vulnerability for the French economy. Despite a positive growth contribution from net exports in 2017-18 (Table 1), and a contribution from sectoral specialisation that is more favourable relative to its European peers (Camatte and Gaulier, 2018), France's foreign trade performance is unsatisfactory (Figure 8, Panel A). Goods exports growth has relied on relatively few sectors, particularly aeronautics, transport equipment and agriculture (Panel B and Figure 9). Yet, the share of services has been growing strongly, reaching close to 30%, second in Europe only to the United Kingdom. Non-price competitiveness is hampered by weaker innovation than in the best performing economies, whereas research spending is mostly directed at industries that are in decline in terms of their share of value added (see below). However, French exports also partly reflect the internationalisation strategies followed by French companies, which have focused on multiplying production sites (Emlinger, Jean and Vicard, 2019). The current account deficit thus remains moderate at 0.7% of GDP in 2017.

Figure 8. Export performance is disappointing



1. Difference between export growth and export markets' growth, in volume terms (with export markets as of 2010).

Source: OECD (2019), *OECD Economic Outlook: Statistics and Projections* (database) and updates; INSEE (2019), *Quarterly national accounts* (database).

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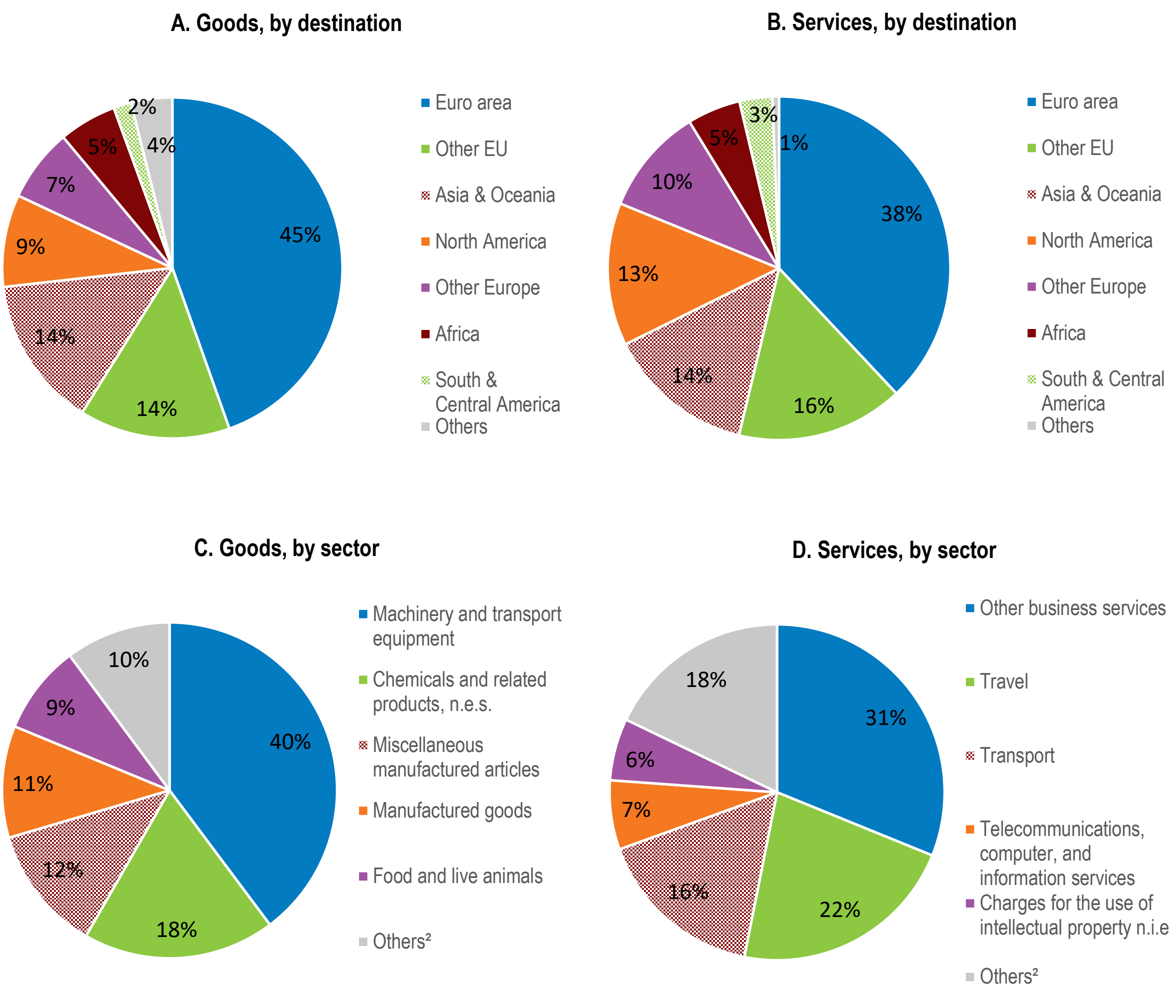
Figure 9. Structure of exports

Per cent, 2017



1. In Panel C, others include animal and vegetable oils-fats-waxes, non-elsewhere classified commodities, crude and inedible materials (except fuels), mineral fuels and lubricants, beverages and tobacco; in Panel D, others include financial services, manufacturing services, insurance and pensions services, maintenance and repair, personal cultural/recreational services, construction and public administration services.

Source: OECD (2019), *International Trade Statistics* (database).

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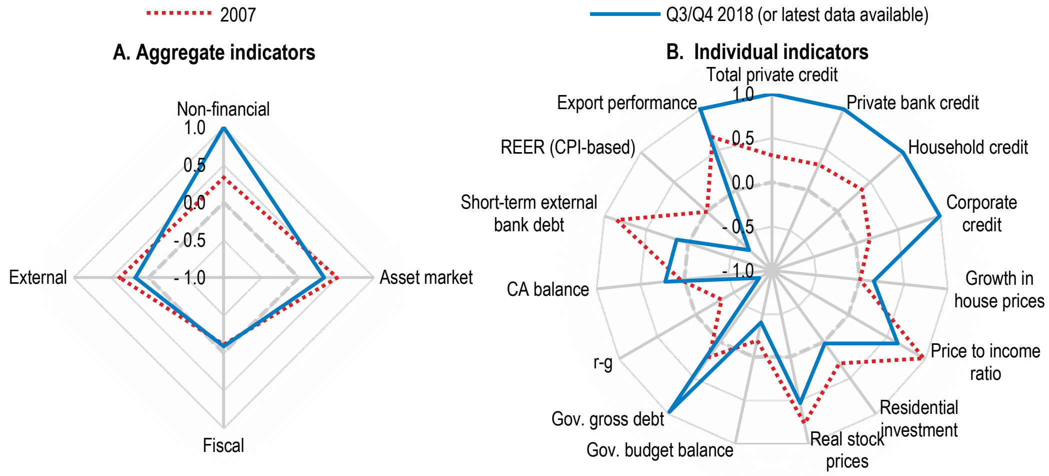
Financial risks

Some macro-financial vulnerabilities appear to have worsened relative to 2007, in particular public and private sector debts are near historical highs (Figure 10). The debt of non-financial corporations reached 73% of GDP in the second quarter of 2018, noticeably higher than the euro-area average (Figure 11). However, this increase has been accompanied by a rise in the liquid assets that non-financial corporations hold, mitigating risks (Khder and Rousset, 2017). Against this background, the authorities lowered the maximum exposure of banks' lending to the most indebted large corporates in July 2018, and the counter-cyclical buffer will increase to 0.25% of banks' capital in July 2019, which is expected to lower annual outstanding credit growth by up to 0.5 percentage point (Haut Conseil de stabilité financière, 2018). In March 2019, they also proposed to raise this buffer to 0.5%. The authorities should continue to use macro-prudential policies pro-actively to prevent the build-up of imbalances.

Figure 10. Evolution of macro-financial vulnerabilities

Index scale of -1 to 1 from lowest to greatest potential vulnerability, where 0 refers to long-term average, period since 1970.



Note: Each aggregate macro-financial vulnerability dimension is calculated by aggregating (simple average) normalised individual indicators from the OECD Resilience Database. Individual indicators are normalised to range between -1 and 1, where -1 to 0 represents deviations from long-term average resulting in less vulnerability, 0 refers to long-term average and 0 to 1 refers to deviations from long-term average resulting in more vulnerability. Non-financial dimension includes: total private credit (% of GDP), Private bank credit (%of GDP), household credit (% of GDP) and corporate credit (% of GDP). The asset market dimension includes: growth in real house prices (year-on-year % change), house price to disposable income ratio, residential investment (% of GDP) and real stock prices. Fiscal dimension includes: government budget balance (% of GDP) (inverted), government gross debt (% of GDP) and the difference between real bond yield and potential growth rate (r-g). External dimension includes: current account balance (% of GDP) (inverted), short-term external bank debt (% of GDP), (real effective exchange rate (REER) (relative consumer prices) and export performance (exports of goods and services relative to export market for goods and services) (inverted).
Source: Calculations based on OECD (2019), *OECD Resilience Statistics* (database).

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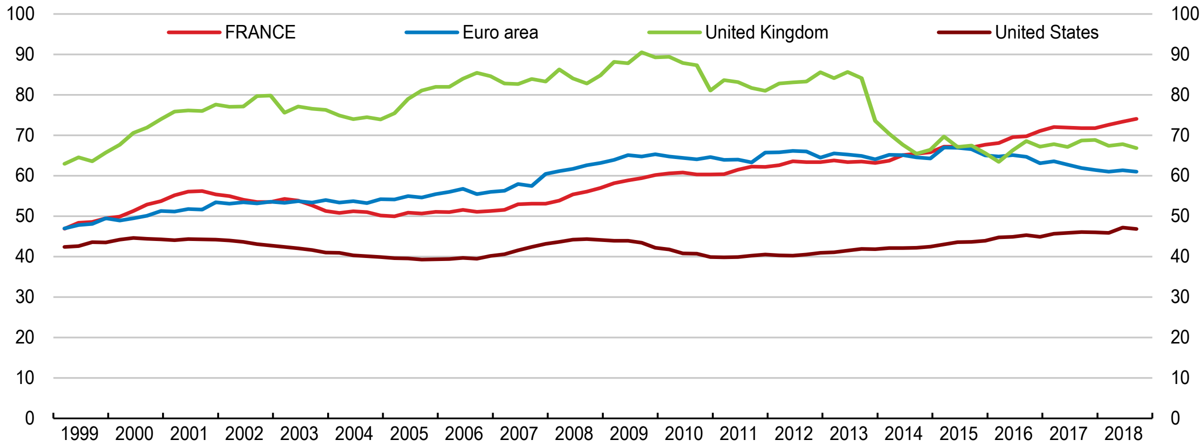
Household credit has reached historically high levels. However, risks appear overall contained according to the central bank (Banque de France, 2018a). The nature of mortgage loans that are primarily at fixed interest rates – 93% of the outstanding mortgage market in 2017 (Autorité de contrôle prudentiel et de résolution, 2018) – is a factor of resilience for household solvency. However, a sharp increase in banks' financing costs would adversely impact the profitability of their mortgage stock. Moreover, a sharp repricing of households' assets (particularly housing) or a drop of their income (in case of a recession) would make households less solvent. A close monitoring of risks related to residential real estate is thereby necessary. The increase in real house prices since mid-2015 is modest relative to euro-area and OECD developments (Figure 12, Panel A). Price to rent and price to income ratios remain below the average OECD country and have moderated from their highs in

2011 (Panel B). Yet, price increases in some large cities such as Paris and Lyon have been stronger than at the nationwide level, suggesting that local developments should be carefully monitored, and that appropriate macro-prudential tools should be used if needed (European Central Bank, 2017).

Figure 11. Non-financial corporate debt has continued to increase

As a percentage of GDP[1]



1. The non-financial corporate debt is consolidated by subtracting assets from the non-financial corporate sector's liabilities.
Source: Banque de France (2019), "Endettement des agents non-financières : comparaisons internationales", Webstat database.

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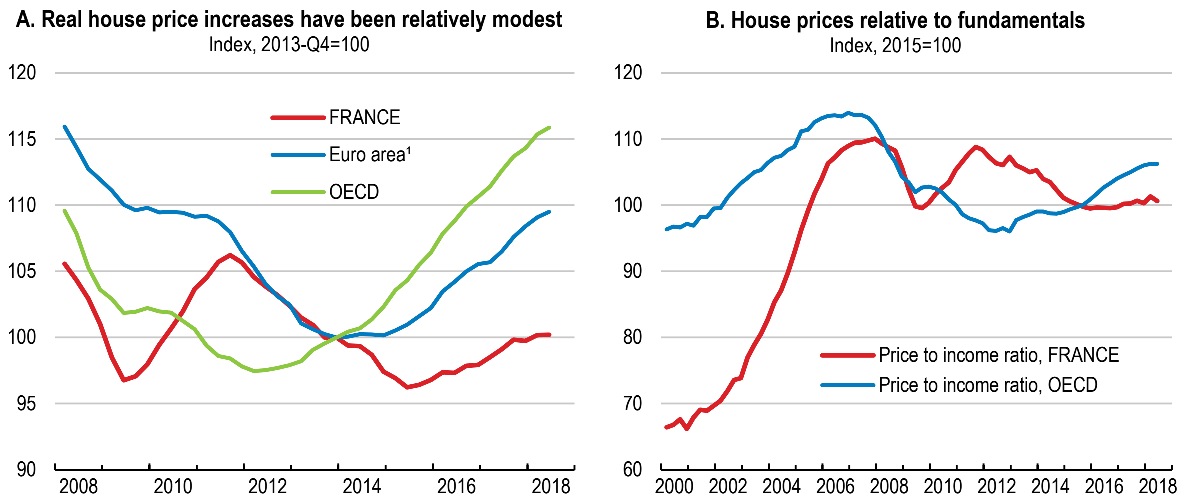
Figure 12. Housing market developments



1. Euro area member countries that are also members of the OECD (17 countries).
Source: OECD (2019), *Analytical House Price Indicators* (database).

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The valuation of commercial real estate requires careful monitoring as France is the most expensive market among large European countries (Banque de France, 2018b), and commercial property valuations can signal vulnerabilities in the housing sector as a whole. Enhancing data collection efforts to gauge price dynamics would be a good move, since the quality of existing data is poor (European Systemic Risk Board, 2016). The systemic consequences of steep price falls on this market appear, however, limited as direct exposures from the insurance sector and large banks to commercial real estate stand below 5% of their balance sheets. Moreover, these institutions seem to be resilient to steep price falls in the office segment of commercial real estate (Haut Conseil de stabilité financière, 2017).

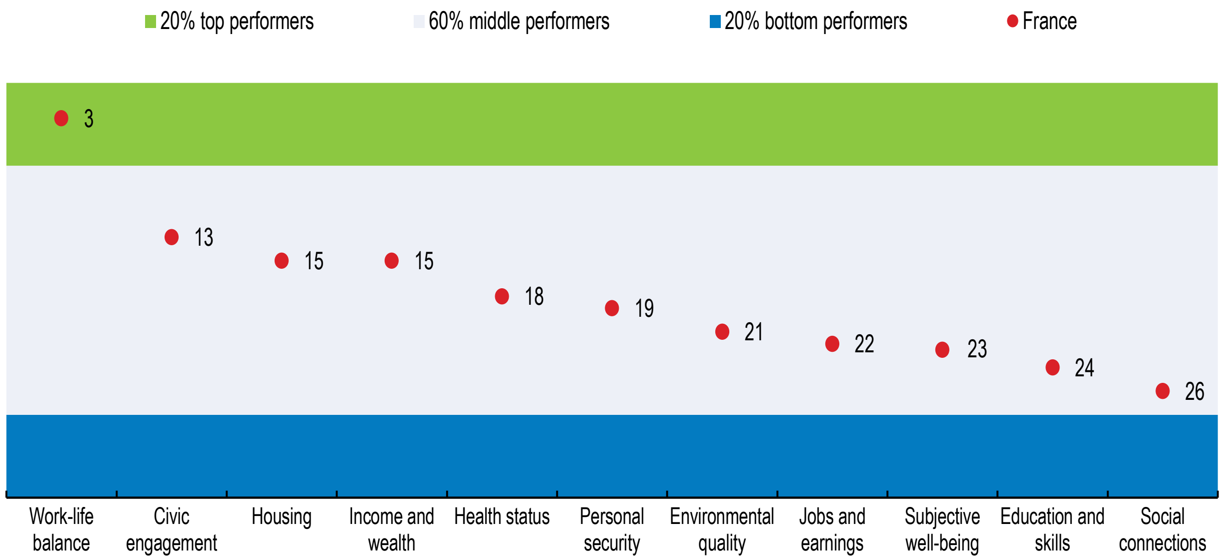
Better use of public spending to boost growth and well-being

Key economic and social challenges remain

France's well-being indicators are mixed. France is above the OECD average on indicators concerning income and wealth, housing conditions and work-life balance (Figure 13). Monetary poverty is low in international comparison (Figure 2). Income and wealth disparities appear moderate (Figure 14) and they have been broadly stable over time, even in the upper tail of the income and wealth distribution (OECD, 2014a; Balestra and Tonkin, 2018). Over the past twenty years, the real disposable income of the poorest household has increased significantly faster than the median household and the top deciles (Argouarc'h and Picard, 2018).

Figure 13. Well-being indicators are mixed

Better Life Index, country rankings from 1 (best) to 35 (worst), 2017[1]



1. Each well-being dimension is measured by one to four indicators from the OECD Better Life Index set. Normalised indicators are averaged with equal weights.

Source: OECD (2017), *OECD Better Life Index*, www.oecdbetterlifeindex.org.

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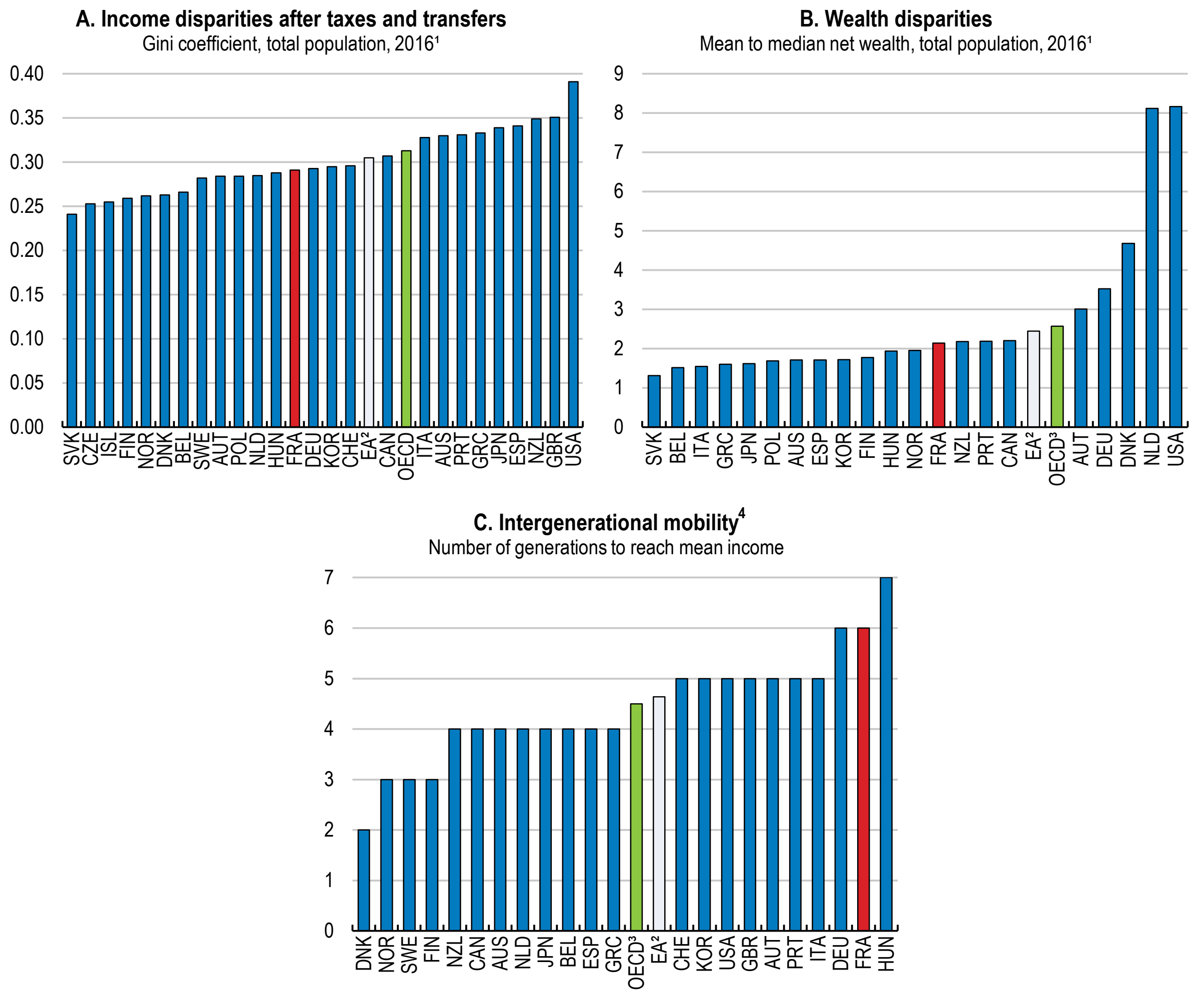
Figure 14. Income and wealth disparities are contained but social mobility is weak



1. Or latest available year; for France, 2014 in Panel B.
2. Euro area member countries that are also members of the OECD (17 countries), excluding Lithuania in Panel B, as well as Luxembourg and all other Eastern European euro area countries in Panel C.
3. Unweighted average across countries with available data (27 and 24 countries in Panels B and C, respectively).
4. Expected number of generations it would take the offspring from a family at the bottom 10% to reach the mean income in society.

Source: OECD (2019), *OECD Income distribution and Poverty Statistics* and *OECD Wealth Statistics* (databases); OECD (2018), *A Broken Social Elevator? How to Promote Social Mobility*, OECD Publishing, Paris.

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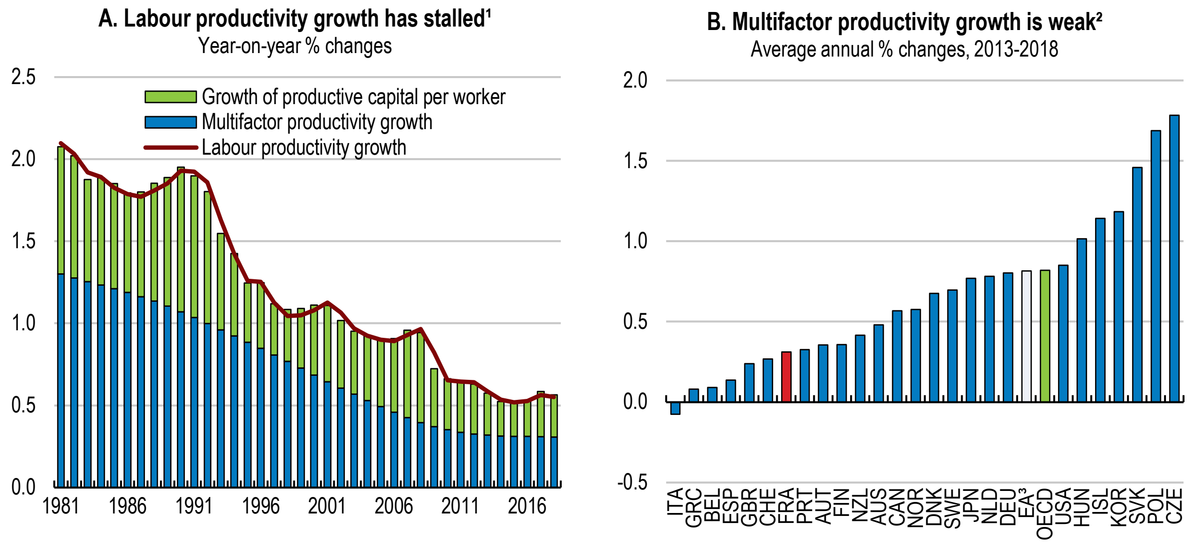
Employment rates, although back to levels not seen since the early 1980s, remain low in international comparison. The importance of long-term unemployment and the high proportion of fixed-term contracts concentrate the economic and social difficulties on certain households. Many low-skilled workers and labour market entrants are excluded from the labour market, implying a particularly high poverty rate before taxes and transfers. Long-term inactive and unemployed workers cumulate significant difficulties that tend to concentrate over space (OECD, 2017a) and be reproduced across generations. Inter-generational social mobility appears weak (OECD, 2018a) and the link between family background and schooling results is excessively strong in France. Access to housing and health could also improve further.

Productivity growth has been sluggish and declining for the past 25 years (Figure 15, panel A). Capital accumulation per worker has substantially declined well before the crisis, as for most comparable economies. Multifactor productivity, which is more closely related to innovation, also decelerated and appears low in international perspective (panel B). Raising multi-factor productivity growth is needed to maintain sustainable and inclusive growth going forward. The productivity gap between French firms and best performing global firms has widened, notably in services sectors, suggesting that policies that can increase diffusion and spillovers are key (Andrews, Criscuolo and Gal, 2016; Berlingieri, Blanchenay and Criscuolo, 2017; Cette, Corde and Lecat, 2017). Policies to boost skills, innovation and digitalisation will also be needed to boost growth potential, job creation and reduce socio-economic disparities (Chapters 1 and 2).

Figure 15. Labour productivity growth has steadily declined



1. Trend labour productivity per employee.
2. Annualised trend multifactor productivity growth.
3. Euro area member countries that are also members of the OECD (17 countries).
Source: OECD (2018), *OECD Economic Outlook: Statistics and Projections* (database).

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Ongoing reforms could help reignite productivity growth. If fully implemented, those reforms would have a meaningful impact on growth and equity in the medium term (Table 3 and Table 4). The estimated impact of selected reforms (for which there is sufficient empirical evidence) on potential GDP per capita is of the order of 3.2 per cent at a ten-year horizon. Moreover, additional simulations use OECD empirical evidence on the long-term distributional effects of structural reforms based on the experience of similar reforms in OECD countries (Causa, Hermansen and Ruiz, 2016; Akgun, Cournède and Fournier, 2017) to illustrate the potential distributional effects of this reform package. The simulated results suggest that the long-term income gains of ongoing reforms would be concentrated around the average household and in the lower- and lower-middle parts of the income distribution (Table 4 and Figure 16).

Table 3. Potential impact of some ongoing reforms on GDP per capita after 10 years[1]

	GDP per capita	Through employment	Through productivity
2017-18 labour market reforms			
- Higher targeted spending on lifelong training	0.6	0.4	0.1
- Lower administrative extension of branch-level agreements[2]	0.7	0.7	0.0
- Reduced uncertainty around dismissal costs	0.3	0.2	0.1
Tax measures			
- Reduced tax wedge[3]	0.2	0.2	0.0
- Reduction of capital taxation[4]	0.8	0.0	0.8
- Steady increase in in-work benefits (*Prime d'activité*)[5]	0.5	0.5	0.0
Product market and simplification measures			
- Simplification of bankruptcy procedures, smoothing of firm-size related thresholds and incentives for employee-participation schemes[6]	0.4	0.2	0.2
Total (Ongoing reforms)	3.2	2.1	1.1

1. All figures are rounded to the nearest decimal point. The estimates assume full implementation of the reforms.
2. This estimate assumes a drastic change in the dynamics of extension of collective agreements, as well as an ambitious mobilization and implementation of the recommendations of the expert group that may assess the benefits of extending branch-level agreement. It assumes that the difference between the union membership rate and the coverage rate of the extended agreements would fall by 10 percentage points (from 90% to 80%).
3. Reduction of social contributions and increase of the proportional personal income tax (*contribution sociale généralisée*, CSG).
4. Reduction of the corporate income tax rate and transformation of the wealth tax.
5. This estimate shows a decline in the effective tax wedge after transfers averaging 2.8 percentage points for low-income workers
6. These estimates are based on De Williencourt et al. (2018).
Source: OECD estimates based on Balázs Égert and Peter Gal (2017), "The quantification of structural reforms in OECD countries: A new framework", *OECD Journal: Economic Studies*, Vol. 2016/1 and Akgun, O., B. Cournède and J-M. Fournier (2017), "The effects of the tax mix on inequality and growth", *OECD Economics Department Working Papers*, No. 1447, OECD Publishing.; De Williencourt, C, Faci, A. and S. Ray (2018), "Quel effet macroéconomique du PACTE ? Premiers éléments de réponse", *Trésor-Eco*, No. 226.

Speeding up reforms – while compensating, if necessary, their overall potential negative short-term impact on selected categories of population and continuously evaluating their implementation – could boost productivity growth and gains among low-income households in the medium run. Increasing competition in markets that are still protected, such as regulated professions and retail trade, raising innovation and business dynamics, and reducing administrative barriers will be key to boost productivity growth.

The reforms proposed in this *Survey* would lift growth, raise productivity and strengthening incentives to invest. This would complement the ongoing reforms. Illustrative simulations suggest that the total estimated total impact of the ongoing and recommended reforms is of the order of a 5.1 per cent increase in potential GDP per capita at a ten-year horizon (Box 2). The illustrative long-term income gains of the overall reform package would be tilted towards the lower and average parts of the income distribution (Figure 16).

Box 2. Impact of some OECD recommended reforms on growth and inclusiveness

The estimated impact of some key structural reforms proposed in this *Survey* are calculated using historical relationships between reforms and growth in OECD countries (Table 4). These estimates assume swift and full implementation of reforms.

Table 4. Potential impact of some reforms proposed in this Survey on GDP per capita after 10 years[1]

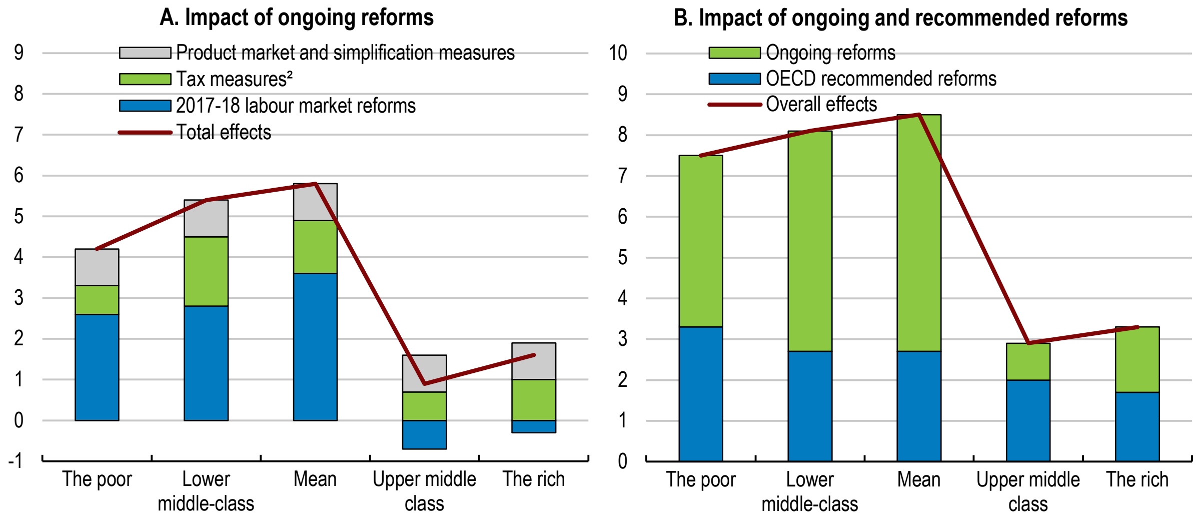
	GDP per capita %	Through employment (percentage points)	Through productivity (percentage points)
Labour market reforms			
- Improved social dialogue[2]	0.4	0.4	
- Higher effectiveness of activation policies	0.2	0.1	0.1
- Gradual increase in the effective retirement age to 64 by 2025	0.5	0.3	0.1
Product market and simplification measures			
- Further simplification of business regulations and opening up of regulated professions	0.1		0.1
Tax and public spending measures			
- Increase in digital investment (0.1% of GDP)[3]	0.3		0.3
- Increase in public spending for R&D (0.1% of GDP)	0.2		0.2
- Shift taxes away from production (0.5% of GDP)	0.2		0.2
Total (recommended reforms)	1.9	0.8	1.0
Total (ongoing reforms)	3.2	2.1	1.1
Total (recommended and ongoing reforms)	5.1	3.0	2.1

1. All figures are rounded to the nearest decimal point. The estimates assume full implementation of the reforms.
2. Estimates are based on the assumption that the measures to reform social dialogue described in Chapter 1 could reduce the difference between the union membership rates and the coverage rate of collective agreements by an additional 5 percentage points.
3. The output effects from a 0.1% of GDP permanent increase in digital investment are scaled using the range of models used to estimate the long-term GDP gains from an increase in public investment reported in A. Mourougane, J. Botev, J-M. Fournier, N. Pain and E. Rusticelli (2016), "Can an Increase in Public Investment Sustainably Lift Economic Growth?" OECD Economics Department Working Papers, No. 1351, OECD Publishing, Paris.

Source: OECD estimates based on based on B. Égert and P. Gal (2017), "The quantification of structural reforms in OECD countries: A new framework", *OECD Journal: Economic Studies*, Vol. 2016/1; Akgun, O., B. Cournède and J-M. Fournier (2017), "The effects of the tax mix on inequality and growth", *OECD Economics Department Working Papers*, No. 1447, OECD Publishing, Paris.

Figure 16. Illustrative gains of some structural reforms along the income distribution

% increase in real disposable income over the long term[1]



1. All figures are rounded to the nearest decimal point. The estimates assume full implementation of the reforms. The reforms used for this illustrative exercise correspond to those described in Tables 3 and 4, except for two measures due to the estimates presented in Causa et al. (2016) and Akgun et al. (2017). On the one hand, the effect of reducing uncertainties surrounding redundancy costs (Table 3) is not taken into account here. On the other hand, a stronger decentralisation of wage bargaining (a change in the index used by Causa et al. (2016) from 5 to 4.65) was taken into account in the context of the labour market reforms in Panels A and B. However, a quantification of the expected effects on GDP per capita over a 10-year horizon is unavailable.
2. These estimates are based on De Williencourt et al. (2018), and assume equal long-term gains over the income distribution, as with most product market reforms in Causa et al. (2016) and Akgun et al. (2017).
Source: OECD estimates based on Balázs Égert and Peter Gal (2017), "The quantification of structural reforms in OECD countries: A new framework", OECD Journal: Economic Studies, Vol. 2016/1 and Akgun, O., B. Cournède and J-M. Fournier (2017), "The effects of the tax mix on inequality and growth", *OECD Economics Department Working Papers*, No. 1447, OECD Publishing.; De Williencourt, C, Faci, A. and S. Ray (2018), “Quel effet macroéconomique du PACTE ? Premiers éléments de réponse”, *Trésor-Eco*, No .226.

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Reducing public spending and improving their efficiency

France has made some progress in reducing public deficits since 2012. The budget deficit has declined to 2.6% of GDP in 2018 from 5.0% in 2012. On the basis of current government plans, the fiscal deficit will increase in 2019, following a large one-off spending due to the transformation of the CICE in lower social security contributions for employers (Box 1) and, to a lower extent, due to exceptional measures to respond to the “gilets jaunes” protests. However, the headline deficit should be below 3% in 2020 (Table 5). This fiscal path will provide support to economic activity in 2019, but, overall, fiscal policy is expected to be broadly neutral in 2019-20. The debt-to-GDP ratio is expected to stabilise at around 100% by end-2020.

Despite this progress, France’s fiscal consolidation pace has lagged those of its neighbours following the fiscal easing in response to the Great Recession of 2007-08. Many euro-area countries that reached fiscal deficits higher than France in 2010-11 have now smaller deficits, such as Spain or Portugal. In fact, all France’s direct neighbours had smaller fiscal deficits in 2017 (Figure 17, panel A). This owes in big part to the ability of those countries to reduce their ratio of public spending while France has not been able to do that following the steep increase in 2008 (panel B). For example, from their 2007 peak, Spain, Belgium and Germany have reduced their public spending ratios by 6.9, 4.2 and 3.7 percentage points, respectively. During the same period, French public spending was reduced by only one percentage point, implying that most of the fiscal deficit adjustment was on the revenue side.

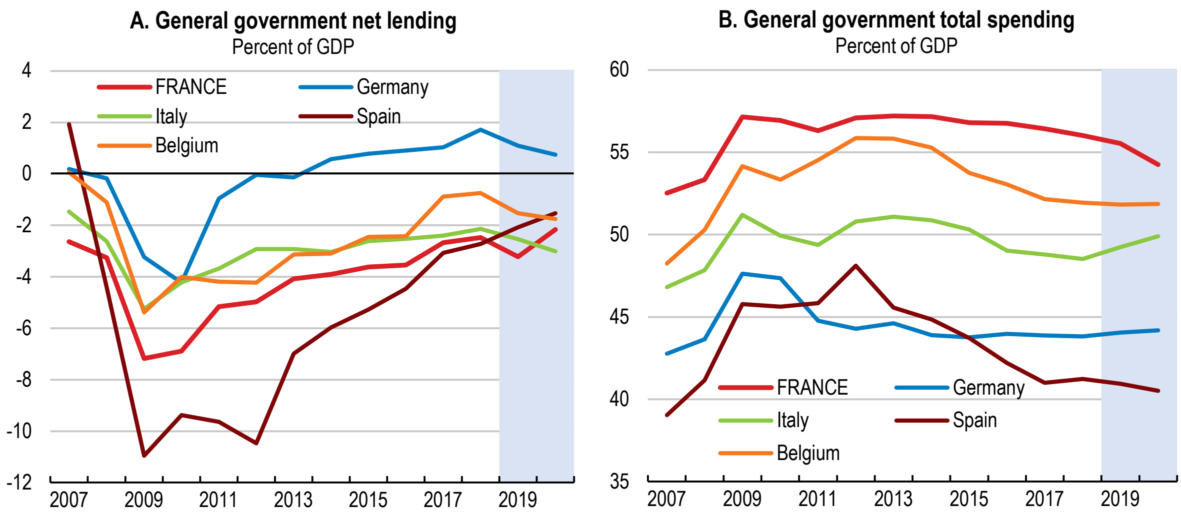
Table 5. Fiscal indicators

As a percentage of GDP

	2012	2013	2014	2015	2016	2017	2018[1]	2019[1]	2020[1]
Spending and revenue									
Total expenditure	57.1	57.2	57.2	56.8	56.6	56.4	56.0	55.5	54.2
Total revenue	52.1	53.1	53.3	53.2	53.0	53.6	53.5	52.3	52.1
Net interest payments	2.4	2.2	2.1	1.9	1.8	1.7	1.6	1.5	1.5
Budget balance									
Fiscal balance	-5.0	-4.1	-3.9	-3.6	-3.5	-2.8	-2.5	-3.2	-2.3
Primary fiscal balance	-2.5	-1.9	-1.8	-1.8	-1.8	-0.9	-1.0	-1.8	-0.9
Cyclically adjusted fiscal balance[2]	-4.1	-2.9	-2.7	-2.4	-2.3	-2.2	-2.3	-2.9	-2.0
Underlying fiscal balance[2]	-4.1	-2.9	-2.7	-2.5	-2.2	-2.1	-2.6	-2.3	-2.4
Underlying primary fiscal balance[2]	-1.7	-0.8	-0.7	-0.7	-0.5	-0.4	-0.5	-0.8	-1.0
Public debt									
Gross debt (Maastricht definition)	90.6	93.4	94.8	95.6	98.0	98.4	98.4	99.8	99.7
Net debt	68.5	67.6	75.2	77.2	82.6	80.1	80.7	81.8	81.3

1. Projections.
2. As a percentage of potential GDP. The underlying balances are adjusted for the cycle and for one-offs. For more details, see OECD Economic Outlook Sources and Methods.
Source: OECD (2019), *OECD Economic Outlook: Statistics and Projections* (database) and updates.

Figure 17. The French public deficit and spending remain high



Source: OECD (2019), *OECD Economic Outlook*: *Statistics and Projections* (database) and updates.

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Empirical research shows that consolidation through the control of expenditures tends to be more sustainable (Guichard, Kennedy and André, 2007). To assess the drivers of the improvement of the French fiscal balance, an analysis has been made by decomposing the different factors behind the changes in the structural balance in order to better assess the discretionary component of public finances following a method proposed, among others, by Duchêne and Levy (2003). As shown in Table 6, no significant expenditure effort was achieved after 2009, expect in three years, from 2013 to 2015. The continuous improvement of the structural fiscal balance since 2010 owed much to new tax measures (especially in 2011-13; see Table 6) and non-discretionary factors, such as higher tax elasticities (most likely the case in 2016-17).

Reducing the fiscal deficit through public spending restraint is key to putting the debt-to-GDP ratio on a declining path. This will entail a stronger control over public spending. Tax revenues are already high, leaving no room of manoeuvre from increasing tax revenues. Indeed, the heavy tax burden will eventual have to decline, since it is detrimental for economic activity and because the social acceptance of additional taxes seems to have reached a limit.

Table 6. Fiscal consolidation efforts since 2007

Per cent of GDP

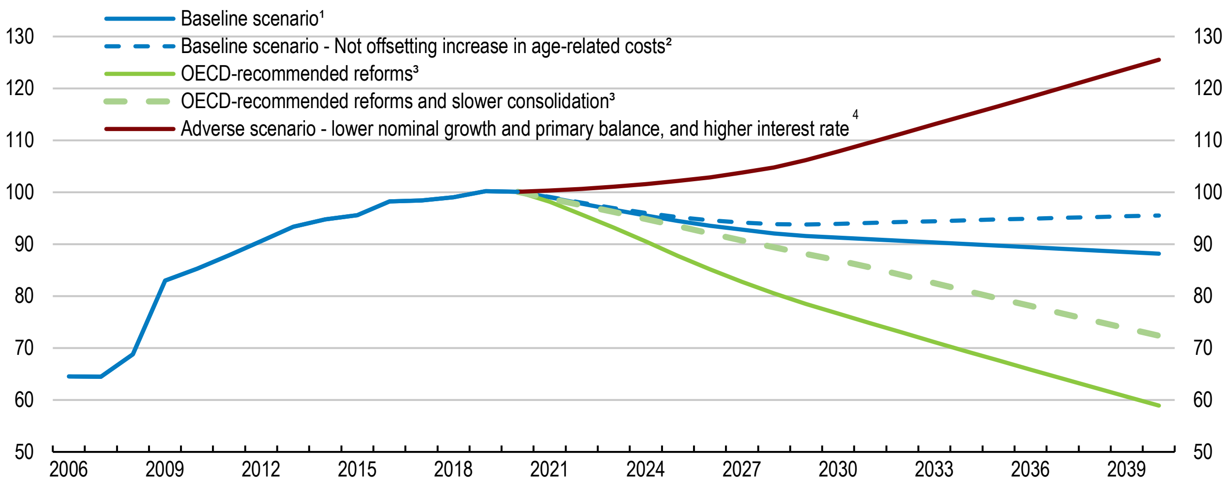
	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
General government financial balance	–2.6	–3.3	–7.2	–6.9	–5.2	–5.0	–4.1	–3.9	–3.6	–3.5	–2.8	–2.5
Change in the general government financial balance (A=A1+A2)	–0.2	–0.6	–3.9	0.3	1.7	0.2	0.9	0.2	0.3	0.1	0.9	0.1
Cyclical component (A1)	0.5	–0.8	–2.5	0.5	0.7	–0.4	-0.3	0.0	0.0	0.0	0.8	0.2
Cyclically-adjusted component (A2=B1+B2)	–0.7	0.2	-1.4	–0.2	1.0	0.6	1.2	0.2	0.3	0.1	0.1	–0.1
Discretionary effort (B1=C1+ C2)	–0.5	–0.5	–2.4	–0.1	1.1	0.7	1.4	0.3	0.3	–0.2	–0.1	–0.2
New measures affecting the tax burden (C1)	*–0.3*	*–0.5*	*–0.8*	*0.1*	*1.1*	*1.1*	*1.3*	*0.2*	*–0.1*	*–0.2*	*0.2*	*–0.2*
Effort in controlling nominal expenditure growth[1] (C2)	*–0.1*	*0.0*	*–1.6*	*–0.2*	*0.0*	*–0.4*	*0.1*	*0.1*	*0.4*	*0.0*	*–0.3*	*0.0*
Non-discretionary component (B2)	–0.2	0.7	1.0	–0.1	-0.1	-0.1	–0.2	-0.1	0.0	0.3	0.2	0.1

Note: Computed using the difference between the growth of expenditure and potential GDP (Duchêne and Levy, 2003). Public spending includes the CICE (tax credit for competitiveness and employment).
Source: OECD and French authorities; OECD computations.

According to OECD projections, France's public debt – Maastricht definition – will slowly decrease but still reach 90% of GDP by 2040 (Figure 18). This central scenario assumes that the increase of ageing costs is fully offset by compensatory measures. If this is not the case, the debt-to-GDP ratio would be 5 percentage points higher than in the baseline scenario by 2040. This would heighten risks to fiscal sustainability, especially if by that time the level of interest rates has returned to level seen before the 2007 financial crisis.

Figure 18. Structural reform and further consolidation are necessary

Simulations of gross government debt as a percentage of GDP, Maastricht definition



1. The baseline scenario builds on Table 1 for 2019-20. It assumes a potential growth that increases to 1.7% in 2030, based on the measures described in Table 3, and remains stable thereafter. The primary balance and GDP deflator are set at -0.3% of GDP (from 2022) and 2.0% (from 2021), respectively, while the effective interest rate increases progressively from 1.7% in 2021 to 3.0% in 2030 and remains stable thereafter.
2. The "Not offsetting increase in age-related costs" scenario includes the European Commission projections of total ageing-related public expenditures (pensions, long-term care, health and education). These projections suggest ageing-related costs will add 0.5 percentage points of GDP to annual government spending, compared to the baseline scenario.
3. The "OECD-recommended reforms" scenario adds the estimated effects of the reforms recommended in this Survey (Box 2) and Table 10. This scenario assumes that the primary balance would go from -1.0% of GDP in 2020 to 1.2% of GDP in 2025 and would stay stable thereafter. In the alternative scenario "OECD-recommended reforms and slower consolidation" the primary balance progressively reaches 0.8% of GDP in 2032 and remains stable afterwards.
4. The adverse scenario is similar to the baseline simulations but real GDP growth is set at 1%, the primary deficit is set to stabilise at 1.2% of GDP over 2021-40 and the effective interest rate increases progressively from to 1.7% in 2021 to 3.5% in 2030 and remains stable thereafter.
Source: Adapted from OECD (2018), *OECD Economic Outlook: Statistics and Projections* (database), *June and November;* and European Commission (2018), "The 2018 Ageing Report - Economic and budgetary projections for the 28 EU Member States (2016-2070)" Directorate-General for Economic and Financial Affairs.

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To put the debt-to-GDP ratio firmly on a declining path, further efforts to control expenditures are needed. At this stage, the foreseen spending cuts only broadly compensate planned tax cuts (Table 7), and a stronger control over public spending will be necessary to sustainably lower taxes, while reducing the public deficit. A welcome committee mandated by the government (Comité Action publique 2022) has identified potential efficiency gains to reduce public spending. However, detailed performance objectives on the quality of public services or budget savings are not yet available. A quantitative tracking of the implementation and outcomes of spending reviews will be important to ensure their effectiveness (OECD, 2017b).

Table 7. Main government tax and spending structural measures

Estimated effect on the fiscal balance in 2022, per cent of GDP

Containment of local-government spending	0.7%
Partial indexation of social benefits to inflation in 2019-20	0.3%
Containment of health-care spending	0.2%
Cut in subsidised contracts	0.1%
Housing spending reform	0.1%
Cut in the number of civil servants	0.1%
Total spending cuts	1.4%
Cut in the statutory CIT rate	-0.4%
Increase in environmental and tobacco taxes	0.2%
December 2018 fiscal package	-0.2%
Lower taxation on capital income and wealth tax reform	-0.2%
Full repeal of the housing tax on main residences	-0.7%
Total tax measures	-1.4%
Total effect on the fiscal balance	0.0%

Note: The estimated fiscal impacts are relative to a no-change scenario relative to GDP in spending and tax revenues from 2017, and assume full implementation. This includes both legislated and anticipated reforms. The increase in environmental tax includes the 2018 carbon tax hike only. The December 2018 fiscal package corresponds to the tax cut for low- and middle-income pensioners, the increase in in-work benefits (*prime d'activité*) and tax exemptions for overtime work.
Source: OECD calculations based on the *2019 Rapport économique social et financier*, *Évaluation des voies et moyens Tome II Dépenses fiscales 2019*, and *Programme de Stabilité 2018-2022* (all reports are from the Ministère de l'Économie et des Finances).

A strategy to reduce public spending in France should include improving its efficiency, particularly those related to local governments and tax expenditures, lowering the public-sector wage bill, and reducing pension spending in relation to GDP. Moreover, health-care spending represents about 14% of public expenditures, and public and private health-care expenditures are high in international comparison. There remains scope to implement past Survey recommendations to reduce the foreseen increase in costs by boosting the health system's efficiency (OECD, 2017a). As in other areas of reform, the expected costs and benefits of measures will need to be clearly communicated. Voters and other stakeholders will need to be convinced of the need for reform and the costs of no action (OECD, 2010a).

Containing local government spending

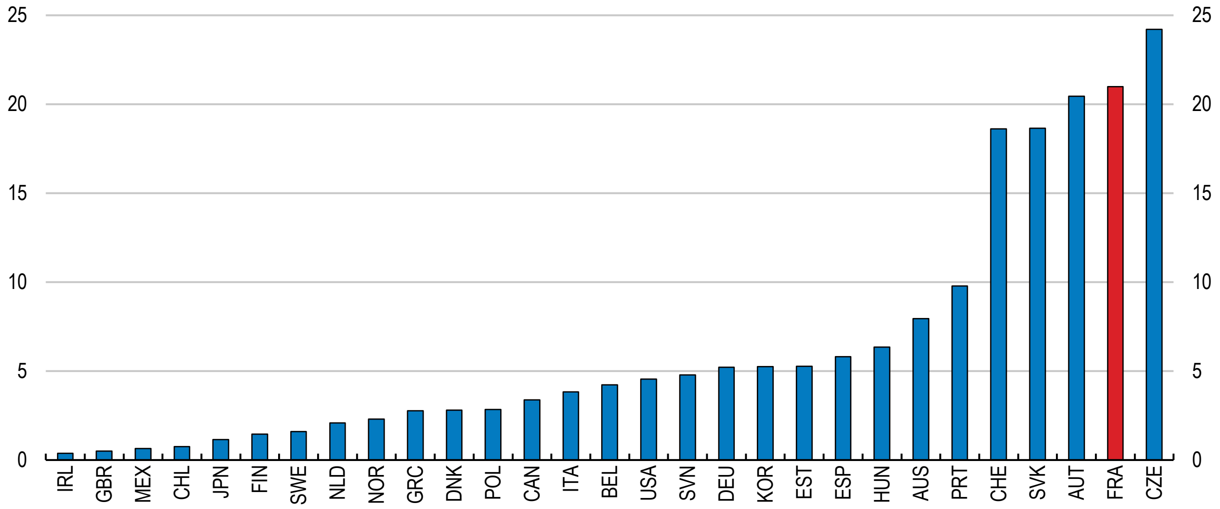
Local governments represent roughly 20% of public spending. The 2018-22 budget programme foresees that local governments will achieve sizeable spending reductions relative to a no-change scenario (Table 7). A contractual approach with a system of penalties (and investment subsidies for municipalities) has been set up to foster compliance to the targets set out by the central government. These contractual agreements have been signed by 71% of the 322 large local governments subject to these requirements (Gourault and Dussopt, 2018). Local governments that have not signed such an agreement will also be subject to a control of their operating expenses, and may be subject to penalties if they exceed their targets, which have been notified to them by the State representative in each *département*.

Simplifying the multiple layers of sub-central governments – the so-called *mille-feuille* – could serve to make spending more efficient and, in due course, realise substantial savings. The 2014-15 territorial reforms reduced the number of regions in metropolitan France from 22 to 13 and increased the size of inter-municipal co-operation structures. They also created new governance bodies for large urban areas (*métropoles*). Yet, they lacked detailed objectives, and early indications suggest that cost savings in the short run have been limited in that the amalgamations of regional administrations were either partial or done based on the most attractive conditions. These reforms also did not fully streamline the allocation of responsibilities between different levels of local governments, suggesting significant room for efficiency gains in this area (Cour des comptes, 2017a).

Continuing efforts for streamlining small municipalities would help achieve further efficiency gains. French municipalities are small in international comparison and French metropolitan areas are among the most administratively fragmented in the OECD (Figure 19). Small municipalities make it more difficult to internalise spatial spillovers in terms of urban planning, environmental and congestion costs or public services provision. They also compound co-ordination problems by spreading expertise more thinly. Asymmetric arrangements, in which responsibilities for municipalities are differentiated based on population size or urban/rural criteria, could be further developed in that respect (Allain-Dupré, 2018). The differentiation of responsibilities depending on the category of inter-municipal cooperation structures is a step in that direction. Pilot experiments, as done in Denmark as part of the “Free municipality” programme, would also be helpful to identify asymmetric arrangements with the strongest benefits. Moreover, ensuring that regulations applying to local governments are proportional and tailored to them would help limit their effects on public spending (Lambert and Boulard, 2018).

Figure 19. French metropolitan areas are fragmented

Unweighted average number of municipalities per 100 000 inhabitants[1], 2014



1. Metropolitan areas includes functional urban areas with a population of 500,000 or more; see OECD (2012), Redefining “Urban”: A New Way to Measure Metropolitan Areas, OECD Publishing, Paris http://dx.doi.org/10.1787/9789264174108-en.
Source: OECD (2018), *OECD Cities statistics* (database), https://stats.oecd.org/Index.aspx?DataSetCode=CITIES.

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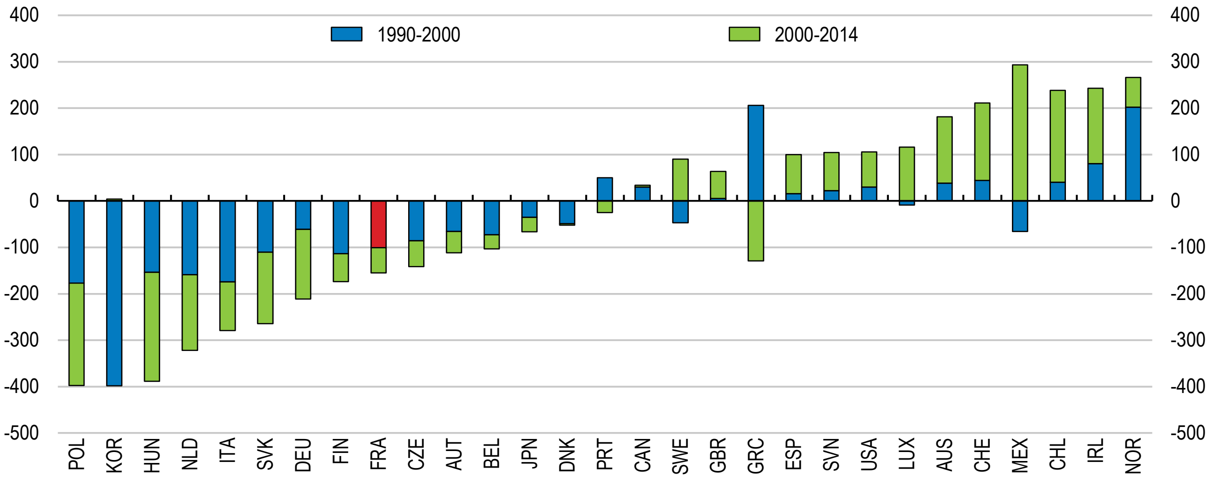
Intergovernmental transfers need to put a stronger focus on standard unit cost approaches to better reflect spending needs of local governments and contribute to contain public spending. The main central government transfer to the municipal sector (*dotation globale* *de fonctionnement,* DGF) is complicated as it includes multiple layers, including several equalisation components that benefit to nearly all municipalities. Moreover, the lump-sum component of the DGF tends to perpetuate past spending patterns that can lead to sizeable inequalities across jurisdictions (Cour des comptes, 2016). Giving a stronger role to cost-based approaches by defining a basic set of collective goods and services to be delivered by local governments would help better reflect actual spending needs of municipalities.

Moreover, increasing further horizontal equalisation, which corresponds to transfers within the same level of local government, would be helpful in that horizontal transfers have hitherto remained modest in France. Horizontal equalisation tends to achieve better results than vertical equalisation (OECD, 2013), which typically corresponds to transfers from the central government to local governments. Avoiding earmarking further national taxes to local governments is also preferable as earmarked taxes are already largely used in France, and these lead to budget rigidities and incentives for excessive spending (Moretti and Kraan, 2018).

Urban sprawl increases the cost of providing collective goods and services and puts upward pressure on local government spending. French urban areas have noticeably sprawled over 1990-2014 (Figure 20), with significant environmental, economic and social consequences (OECD, 2018b), as well as risks to underuse infrastructure. As recommended in previous *Surveys* (OECD, 2017a; OECD, 2011), the lowest level of land-use planning should be the inter-municipal co-operation structure, which should exclusively be in charge of delivering building construction permits and of the development of business parks (*zones d'activités économiques*). Reviewing building restrictions in local land-use plans would also help achieve more sustainable urban development patterns. Moreover, removing exemptions to the development impact fees (*taxe d'aménagement*) for public amenities and commercial buildings would ensure that local tax incentives are fully effective.

Figure 20. Evolution of average urban population density by country

Change in average urban population density[1], inhabitants/km², 1990-2014



1. Urban population density refers only to population density in functional urban areas (FUAs): small cities not forming part of a functional urban area are not considered in the analysis. The full list of FUAs for France is available here: http://www.oecd.org/cfe/regional-policy/functional-urban-areas-all-france.pdf.

Source: OECD (2018), *Rethinking Urban Sprawl: Moving Towards Sustainable Cities*, OECD Publishing, Paris.

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Reforming the pension system

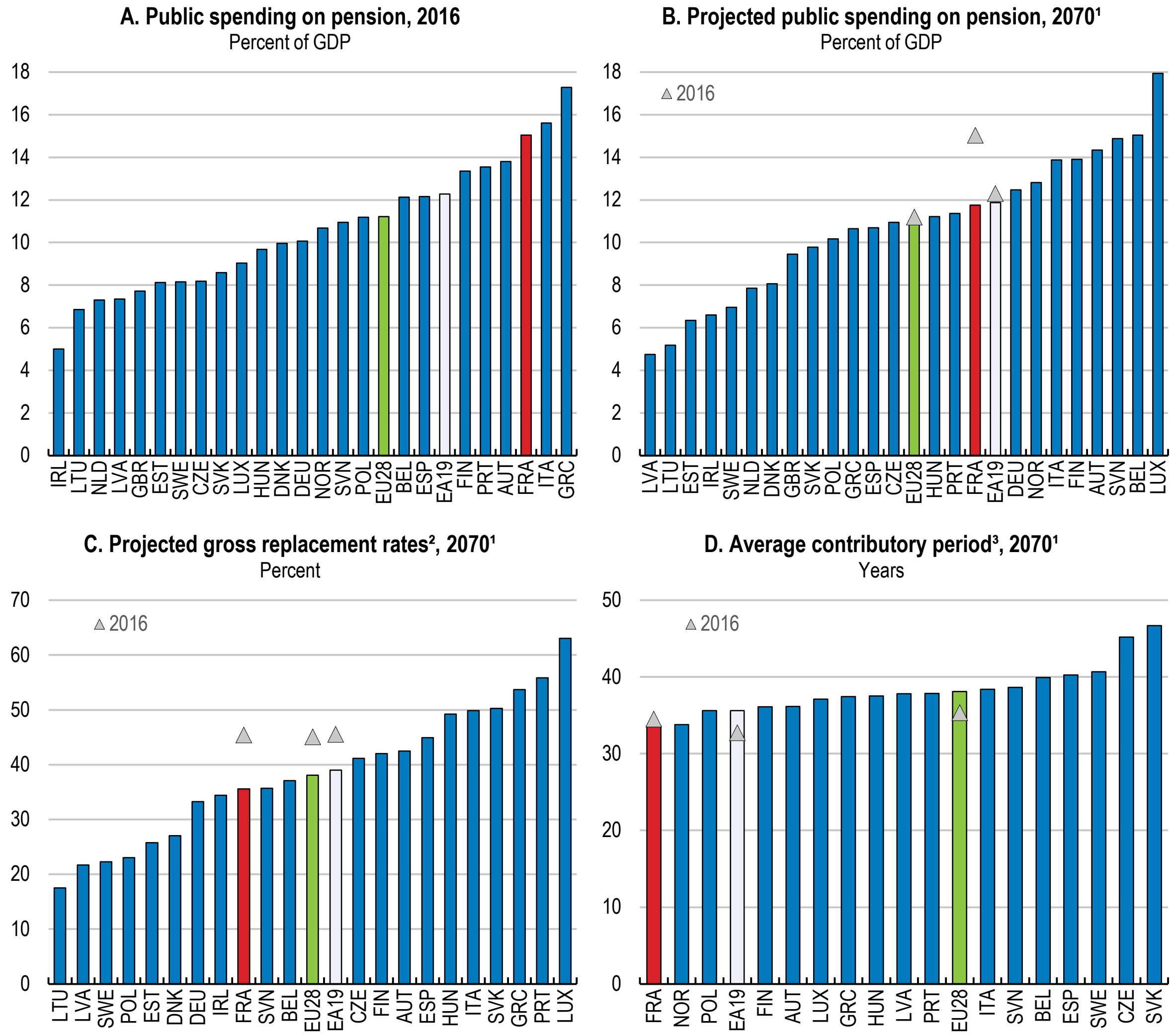
Public expenditures on pensions appear high but broadly under control. Public pension spending is among the highest in the OECD area at about 14% of GDP (Figure 21). However, under the current legislated rules, public expenditures on pensions are set to remain broadly stable until 2040 and would decline rapidly thereafter according to the projections from the European Commission (European Commission, 2018). The financial sustainability of the pension system has been ensured by a decrease in replacement rates which, in the absence of an improvement in the labour market, are expected to decline rapidly (Figure 21), as is the average pension measured as a proportion of the average wage (European Commission, 2018). According to these projections, in 2070, projected public expenditures would be close to the euro-area average.

However, the pension system suffers from numerous weaknesses. The low adjustment rule of past earnings - based on inflation rather than wages (COR, 2018; Cour des comptes, 2018) - could heighten poverty risks for some pensioners in the long run. It could also increase inequalities between pensioners and the employed population Moreover, the complex structure of the pension system – 42 different pension regimes coexist – prevents workers to anticipate their future pension rights. The coexistence of multiple schemes with different rules also undermines labour mobility, contributes to inequities, and fosters a sense of mistrust in the pension system. These weaknesses are amplified by the labour market situation. The effective contributory period to public pension are among the lowest in the European Union (Figure 21). Weak employment rates and labour market challenges, as well as low effective exit age of the labour market reduce contribution periods and undermine pension rights (Chapter 1).

The plan to move to a single point-based pension system goes in the right direction to improve labour mobility. The design of adequate contributions and solidarity mechanisms will be key to successfully move to a single pension system (Boulhol, 2019). Under the current pension system, workers with incomplete careers due to late entry or career breaks have limited benefit losses in international comparison (OECD, 2017c; COR, 2018b). The 2019 reform will need to ensure a better visibility of future pension levels. To avoid creating inequities between workers and retirees, it will also be necessary to review the rules for adjusting past earnings based on wages and adjust the other parameters to ensure the sustainability of the pension system (Boulhol, 2019).

Several measures would be desirable. A revision of bonuses could make gradual retirement more attractive (OECD, 2017d). An alternative solution would be to abolish contributions for those who have reached full pension entitlements and continue to work. Raising the statutory retirement age, eventually by indexing it to life expectancy, could also help accelerate the increase in effective retirement age (OECD, 2017a). Similarly, survivor pension schemes could be reviewed to increase incentives to work and reduce their costs (OECD, 2018c). Finally, it will be important to ensure the convergence of the parameters of the special pension regimes (COR, 2016). Family-related pension benefits also appear outdated. They are heterogeneous across pension schemes and the third child top up tend to benefit more men than women and affluent families (Vignon, 2018).

Figure 21. Public spending on pension is set to decline together with replacement rates



1. European Commission projections (2018).
2. Gross replacement rates are measured as the very first pension benefit relative to the last wage before retirement.
3. Average contributory period for new pensions. Contributory periods can increase for several reasons, such as, for example, rising statutory retirement ages that force employees or higher employment rates.
Source: European Commission (2018), "The 2018 Ageing Report - Economic and budgetary projections for the 28 EU Member States (2016-2070)", Directorate-General for Economic and Financial Affairs.

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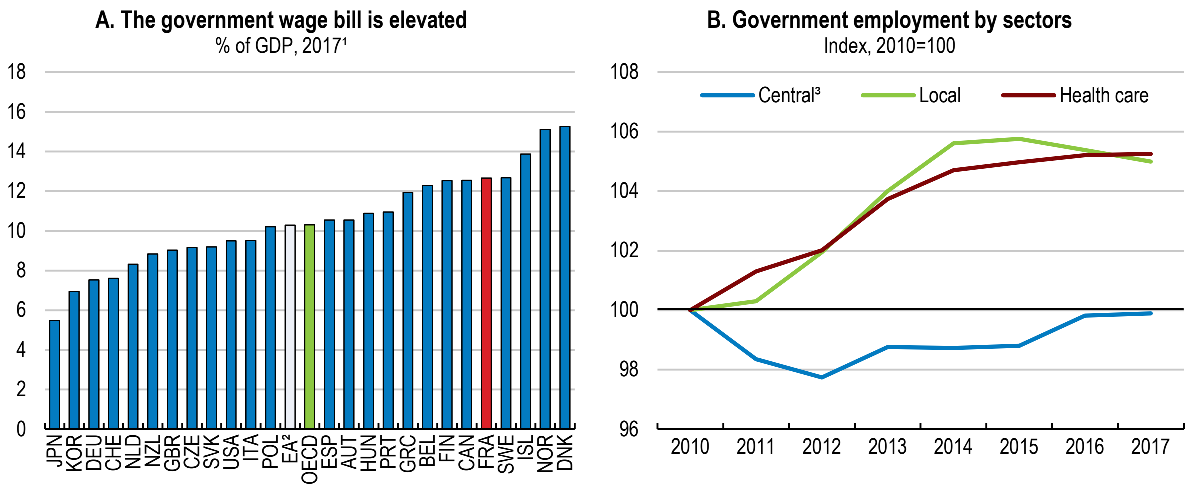
Containing health care spending

France's health care system offers high quality care, but as part of a long-term strategy to reduce public spending, there is a need to improve the efficiency of public health spending, as foreseen in the government plan "Ma santé 2022". To contain the ongoing rise in health expenditures, it is particularly important to encourage health practitioners to adopt more efficient behaviours and stem the rise in pharmaceutical spending. The development of capitation payments to remunerate health professionals for the prevention and treatment of chronic diseases would limit excessive medical intervention, drug sales and improve the prevention and monitoring of chronic diseases (OECD, 2017a). In addition, the share of generics in the reimbursed drug market is low in international comparison. Targeted information for hospitals and primary care providers should be strengthened to improve the relevance of prescriptions, and to apply reimbursement ceilings to a wider range of drugs.

Reforming the delivery of public services to improve their efficiency

Operating and personnel outlays are high and increased rapidly in some sectors (Figure 22). The authorities intend to reduce the number of civil servants by 120 000 by 2022, which corresponds to cuts of the central government and local government workforces by 2.0% and 3.5%, respectively. To meet these targets, they reorganise further the tax administration and deploy a new voluntary departure programme. The authorities are also considering an increase in the civil servants' working time in local governments to align it with the legal working time.

Figure 22. The public sector wage bill is high



1. Or latest available year.
2. Euro area member countries that are also members of the OECD, excluding Lithuania (16 countries).
3. Civil servants from the central government (fonction publique d'État), local governments (fonction publique territoriale), and health care (fonction publique hospitalière) accounted for 44%, 35% and 21% of total civil servants, respectively in 2017. All categories include subsidised contracts (emplois aidés).

Source: OECD (2018), *OECD National Accounts Statistics* (database); INSEE (2018), L'emploi dans la fonction publique en 2016, *INSEE Première* nº 1691 et mises à jour (*Informations rapides* nº 325, 2018).

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Using digital investment to mutualise the face-to-face delivery of public services would be a good move. Mutualisation can lower costs and promote job mobility across government functions without jeopardising the quality of public services. OECD countries that restructured the way public service is delivered to boost productivity through economies of scale and scope include Canada that merged multiple agencies into a consolidated public service organisation in 2005 (Service Canada) or Norway that established in 2006 a unified labour and welfare organisation (NAV). France could consider following the one-stop-shop delivery model of public services based on the results of the experiments currently conducted. However, the large-scale implementation of a one-stop-shop system for public services would require significant preparation to avoid the undesirable effects of hasty mutualisation.

Table 8. Past OECD recommendations to reduce public spending and boost its efficiency

Main OECD recommendations	Summary of actions taken since the 2017 *Survey*
Move towards a single pension system to improve labour mobility and lower management costs. Then, gradually increase the minimum retirement age in line with life expectancy.	Discussions with stakeholders to move to a single pension system started in 2018, and the reform will be voted in 2019.
Reform public employee job-mobility rules, and reduce the number of civil servants through a targeted approach, redefining the duties of government, for example with the help of an external audit.	The authorities announced quantitative objectives to reduce the number of civil servants in central and local governments by 2022.
Increase health practitioners' remuneration for prevention and treating complex chronic diseases, which will help reduce the level of medical intervention, the number of prescriptions and drug sales. Facilitate insurance schemes' contracting with groups of providers. Expand electronic health records to improve health-care co-ordination.	The 2022 healthcare plan aims at improving prevention and co-ordination among care providers, notably by reforming doctors' education. The authorities also target to increase the take-up of generic drugs and develop bundled payments for some long-term diseases.

Reducing inefficient tax expenditures

Tax expenditures (excluding the CICE) are large at about EUR 80 bn in 2018 (3.4% of 2018 GDP) and can be gradually streamlined to improve the effectiveness of the tax system and its redistributive effects.The broadening of tax bases will have to go along with lower tax rates, particularly the progressivity of the tax wedge on low- and middle-income households, to strengthen social cohesion.

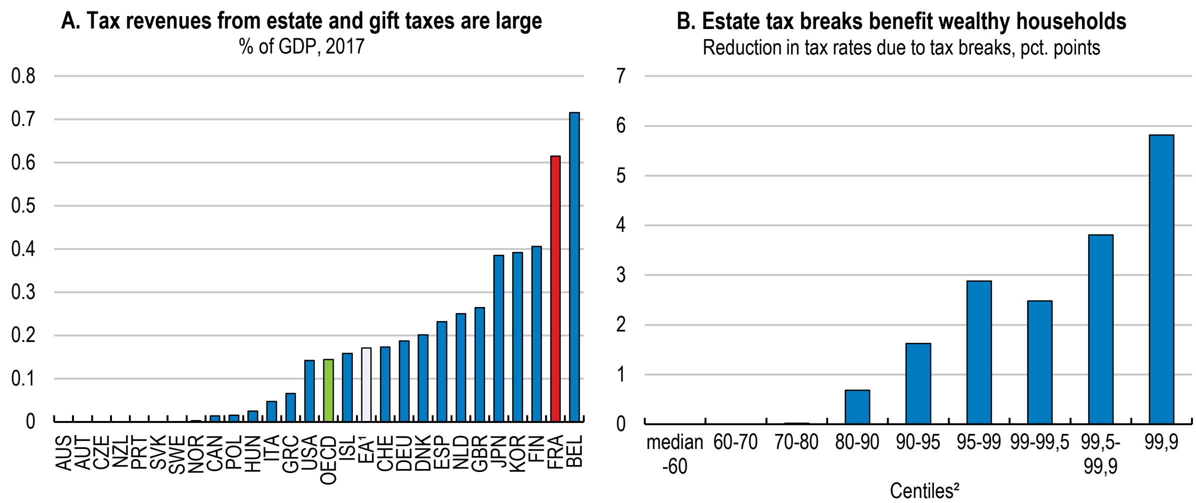
Thorough regular evaluations of tax expenditures have room for improvement, and the authorities are introducing new tax expenditures such as tax-free overtime work, which can have adverse effects on hiring and entails significant dead-weigh costs. The benefits of tax expenditures should be systematically evaluated after a few years of implementation. Such reports should be made public and if some tax expenditures are deemed inefficient, the government should phase them out or explain why it wishes to maintain them.

Moreover, the case for removing tax preferences in favour of the housing sector is strong, as they can result in a misallocation of capital, away from unsubsidised business activities that are more productive (Arnold et al., 2011). Estimated tax expenditures for the housing sector are sizeable (about 0.7% of GDP in 2019), and the main expenditures do not primarily benefit low-income households, such as the reduced rates for the value added tax (VAT) in the construction sector and personal income tax breaks for housing investment. Moreover, their efficiency is undermined by the weak responsiveness of housing supply (Caldera Sánchez and Johansson, 2011; OECD, 2017a).

There are also many tax expenditures on households' savings vehicles – at least 126 in 2016 amounting to about 1.0% of GDP (Conseil des prélèvements obligatoires, 2018). In particular, there is an unusually large number of personal savings vehicles that benefit from a preferential tax treatment ranging from share savings plans to life insurance savings products and savings deposits, and households' savings are heavily tilted towards such financial products. Reducing these tax expenditures would help ensure neutrality of the tax system and promote a fairer tax system, since capital income is more unevenly distributed than labour income.

Reducing tax exemptions on the inheritance and gift taxes would help tackle wealth inequality with knock-on effects on equity and intergenerational mobility. Wealth inequality in France is broadly in line with the average OECD country and tax revenues from estate and gift taxes are large in international comparison (Figure 23, Panel A). However, the progressivity of the inheritance and gift taxes is limited as tax breaks mostly benefit wealthy households (Panel B), which can fuel a feeling of an unfair taxation system among the population. Yet, a well-designed inheritance tax may be a more efficient and less administratively costly way of addressing wealth inequality than a net wealth tax (OECD, 2018d). For example, eliminating the distinct tax treatment for estate purposes of life insurance savings vehicles for large life-insurance contracts would be welcome.

Figure 23. Tax breaks for the estate tax are large



1. Euro area member countries that are also members of the OECD (17 countries).
2. Distribution by centile of inheritances received by children; Panel B shows that the top 0.1% legacies which amount on average to EUR 5.5 million obtain a roughly 6 percentage point tax rate cut due to tax breaks. Calculations are reported in (Dherbécourt, 2017).
Source: OECD (2018), *OECD Revenue Statistics* (database); Dherbécourt, C. (2017), *"Peut-on éviter une société d'héritiers ?"*, https://www.strategie.gouv.fr/sites/strategie.gouv.fr/files/atoms/files/na_51-transmissions-ok_0.pdf.

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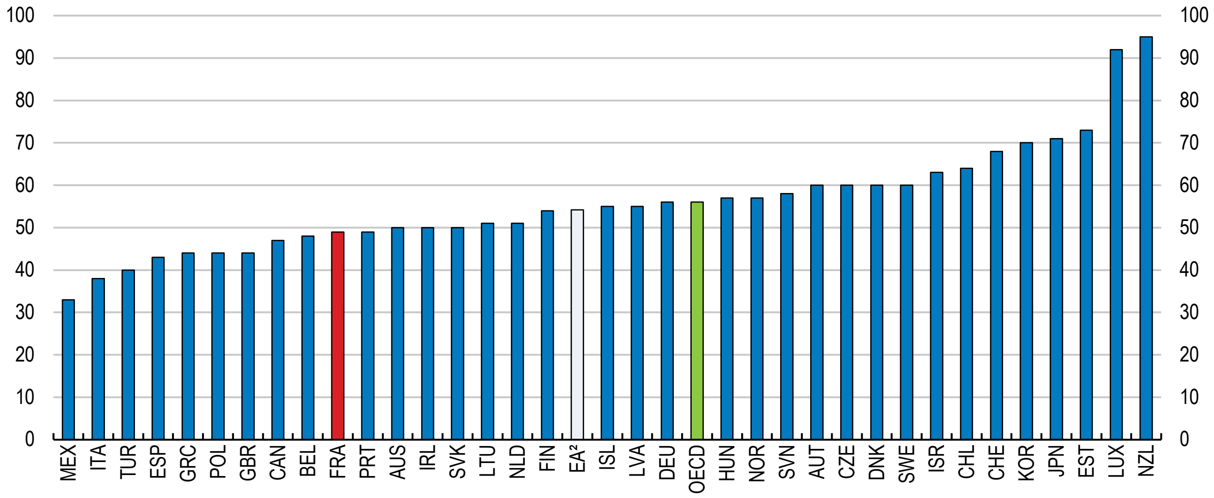
The VAT tax system is complicated by the use of many reduced rates on selected items and exemptions, leading to substantial VAT revenue shortfalls (Figure 24; Table 9). Social policy targets are more efficiently reached through targeted social transfers or the personal income tax (PIT) than through reduced VAT rates. The employment gains of reduced rates on selected sectors such as hotels and restaurants also seem limited in that the benefits appear to have largely benefitted to hotel and restaurant owners (Benzarti and Carloni, 2018), and such reduced rates tend to benefit to the most affluent households. Removing some of the VAT tax breaks, particularly those that benefit the wealthiest households, would be less distortive, and would give room to sustain efforts to lower the taxation on households or businesses (see below).

Figure 24. VAT revenue shortfalls are large

VAT revenue ratio[1] (VRR), 2016



1. The VRR is an indicator of the loss of VAT revenue as a consequence of exemptions and reduced rates, fraud, evasion and tax planning. It measures the difference between the VAT revenue actually collected and what would theoretically be raised if VAT was applied at the standard rate to the entire potential tax base in a "pure" VAT regime and all revenue was collected.
2. Euro area member countries that are also members of the OECD (17 countries).
Source: OECD (2018), *Consumption Tax Trends 2018 - VAT/GST and Excise Rates, Trends and Policy Issues, Consumption Tax Trends,* OECD Publishing, Paris. https://doi.org/10.1787/ctt-2018-en.

StatLink https://doi.org/10.1787/888933949782

Table 9. Past OECD recommendations for a tax system promoting sustainable growth

Main OECD recommendations	Summary of actions taken since the 2017 *Survey*
Withdraw reduced rates for VAT.	No action taken.
Reduce registration fees, and increase taxes on immovable property.	No action taken. Conversely to increasing taxes on immovable property, the repeal of the housing tax runs against an increase in taxes on immovable property.
Use lower social contributions as an opportunity to give a bigger role to the progressive income tax by lowering the basic allowance. Remove personal tax breaks on capital income, and lower the tax rate.	The cut in employees' social contribution was compensated by an increase in the proportional income tax (*contribution sociale généralisée*). The taxation of capital income was reduced to a flat rate of 30%. The tax base of the wealth tax was narrowed to real estate assets only. Some tax breaks applying on large life-savings contracts were removed in 2018.

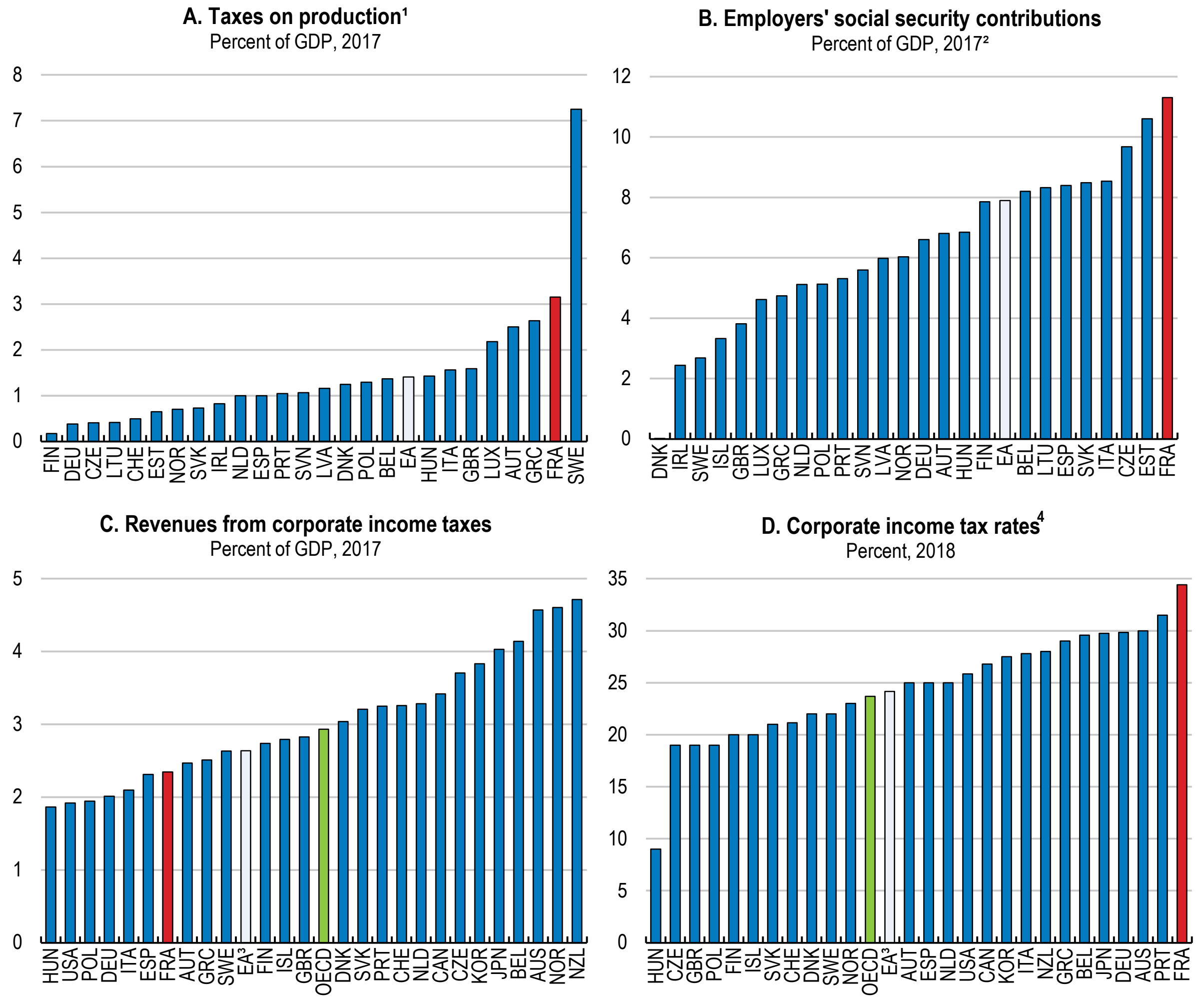
Making taxes more favourable to employment and productivity

The tax burden on businesses is hefty

The large number of taxes levied on businesses go along with frequent changes to exemptions and tax credits. This can be a barrier to firm entry and productivity growth, particularly taxes on production that affect companies regardless of their economic situation. Taxes on production stand at 3.2% of GDP the second highest in the EU (Figure 25, Panel A). Taxes on production include taxes collected by local governments such as the contribution on the firms' value added, the property tax on businesses and a tax to fund public transport. Employers' social security contributions also weigh heavily on businesses (Panel B). Moreover, government revenues derived from the corporate income tax, net of tax credits, are low despite high statutory tax rates (Panels C and D).

Overall, taxes on production consist of about 40 taxes levied by the central government, and, for the most part, by local governments on capital and labour. Efforts to eliminate low-yield taxes on businesses are a first step in reducing the tax burden of businesses. This should go along with efforts to reduce the distortions induced by some tax bases. Eliminating tax expenditures on businesses, particularly those related to reduced VAT rates, would also give room to cut taxes on production, promoting a more efficient tax system.

Figure 25. Business taxation is hefty



1. Taxes on production exclude taxes on households.
2. Employers' actual compulsory social security contributions, including governments. In France, employers' social security contributions excluding public administration reached 8.1% of GDP in 2016. The employers' contributions-to-GDP ratio is expected to decrease by 0.9 percentage point as of 2019 following the transformation of the CICE in lower employers' social security contributions.
3. Euro area member countries that are also members of the OECD (17 countries).
4. Combined central and sub-central (statutory) corporate income tax rates - as of 2018 - given by the central government rate (less deductions for sub-national taxes) plus the sub-central rate. Where a progressive (as opposed to flat) rate structure applies, the top marginal rate is shown.

Source: European Commission (2018), *AMECO Statistics* and *Taxation trends in the European Union* (databases); OECD (2018), *OECD Global Revenue Statistics* (database).

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France legislated a gradual decline in the top statutory rate of the corporate income tax (CIT) from 33.3% to 25% in 2022. Ongoing efforts to broaden the CIT tax base include stricter rules governing the tax consolidation regime for cross-border transactions and a change in the patent box regime to align it with the OECD's Base Erosion Profit Shifting (BEPS) rules. As in other OECD countries, the corporate tax system continues to favour debt over equity (Hanappi, 2018), even though measures were introduced in 2019 to limit the benefits of interest payments deductions. These deductions can also be used by multinational enterprises in their profit-shifting strategies to locate debt in higher-tax rate jurisdictions (Sorbe, Johansson and Bieltvedt Skeie, 2017). Removing entirely the tax bias in favour of debt would rebalance financing incentives, while reducing corporate leverage and enhancing resilience

The property tax system has room for improvement

Policies promoting residential mobility would reduce skills mismatch with positive effects on productivity and employment (Adalet McGowan and Andrews, 2015). High transaction costs can create barriers to labour mobility that heighten skills mismatch (Caldera Sánchez and Andrews, 2011). Transaction fees (*droits de mutation à titre onéreux*) are onerous in France and there is evidence that recent increases have reduced the number of transactions, particularly in non-tense markets (Bachelet and Poulhes, 2017). Elevated transaction fees can also create incentives to purchase undeveloped land to build a new house rather than an existing building in a more central area to lower the tax burden, aggravating urban sprawl.

Lowering registration fees for real estate transactions and reforming recurrent taxes on immovable property (see below), which are less distortionary would therefore be welcome. Replacing the tax break on capital gains from the sale of immovable property by an inflation correction based on consumer prices could also foster residential mobility.

The gradual repeal of the housing tax (*taxe d'habitation*) risks undermining the ability of local governments to set tax rates and bases, which is favourable for public investment and growth (Kim and Dougherty, 2018). The authorities plan to compensate the repeal of the housing tax by reallocating other local direct taxes and by increasing central government transfers. France currently has a recurrent tax on both the owner of an immovable property (*taxe foncière*) and on the occupant of an immovable property (*taxe d'habitation*). The *taxe foncière* is a tax on capital whose receipts go to both the municipality and the *département,* while the receipts from the *taxe d'habitation* go to the municipality only.

The housing tax amounted to EUR 22.3 billion in 2017 (1.0% of 2017 GDP), or roughly 25% of the operating expenses from the municipal sector in 2017. The rationale for the gradual repeal of the housing tax is that it is viewed as being unfair, since it tends to be regressive as it overlooks the taxpayers' ability to pay (Conseil des prélèvements obligatoires, 2010), and its tax base relies on outdated notional rental values.

Updating the cadastral rental values and reforming the *taxe foncière* is a priority to ensure efficiency and fairness of property taxation. The cadastral values used for the property tax levied on households (both for the *taxe d'habitation* and *taxe foncière*) are based on an assessment of property values dating back from 1970. Cadastral values are adjusted uniformly each year – based on consumer price inflation – regardless of spatial variation in property prices so that property values used for taxation purposes differ markedly from market prices. A revised property tax based on updated cadastral values would also make up for some of the loss in revenues from the housing tax repeal. Phasing-in this reform gradually as currently done in the case of the property tax levied on businesses would smooth tax liabilities and likely reduce reform opposition.

Illustrating the effects of OECD-recommended reforms

The proposed tax and spending reforms give the government a choice of options to reduce public spending in the medium run. These options would also make room in the longer term to increase spending on growth-enhancing investment, for example, public expenditures on R&D. This is quantified in an illustrative manner in Table 10.

Table 10. Illustrative fiscal impact of OECD-recommended reforms

Estimated change in the fiscal balance in 2022, per cent of GDP

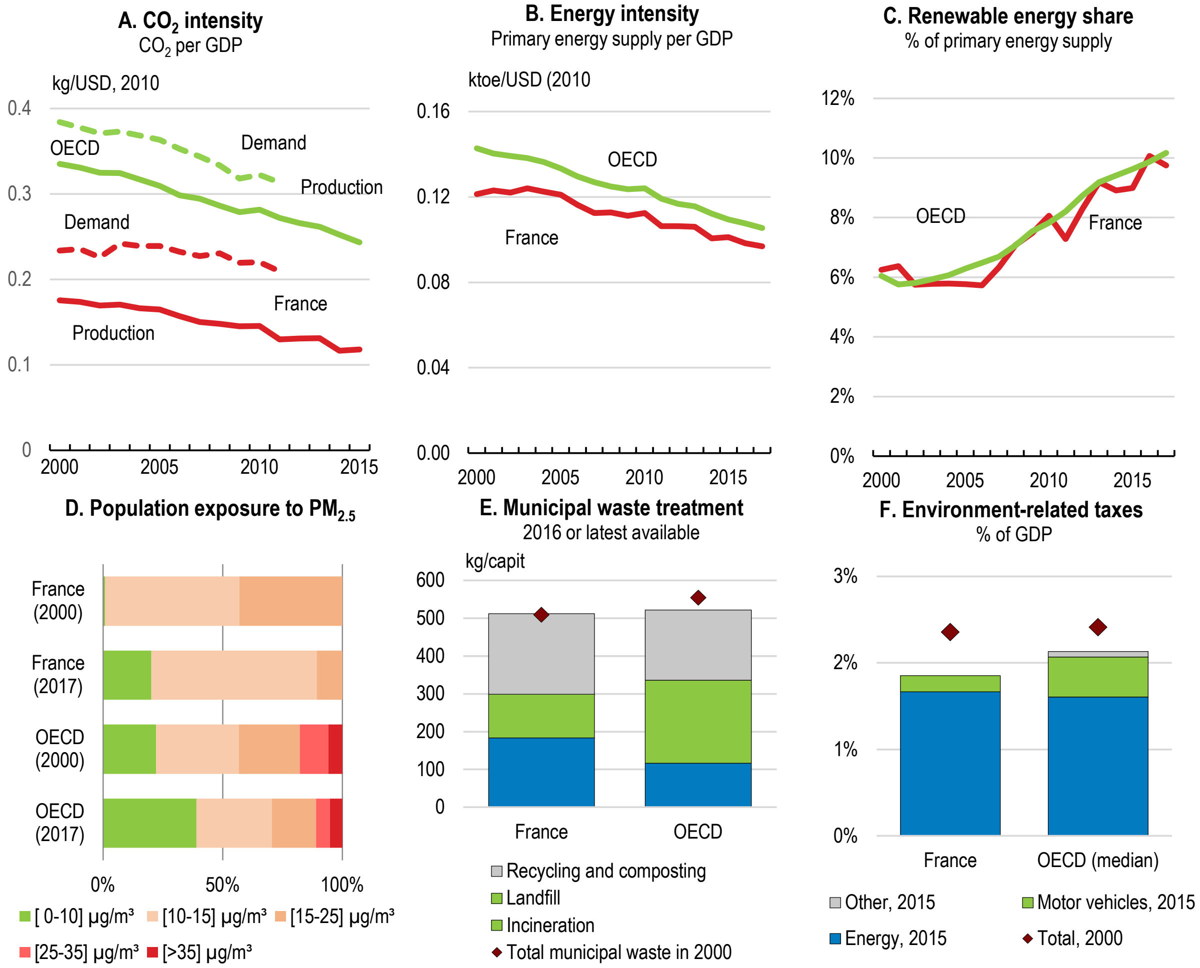
Removing the reduced VAT rate on hotels and restaurants:	0.1%
Remove tax breaks on households' savings	0.2%
Cut taxes on production	-0.5%
Total tax measures including government plans presented in Table 7:	-1.6%
A gradual increase in the effective retirement age to 64 in 2025	0.9%
Broad-based spending review	0.5%
Accounting effects of the OECD-recommended reforms after 4 years through higher GDP growth (Box 2)	0.4%
Increase in public spending for R&D	-0.1%
Total spending cuts including government plans presented in Table 7:	3.1%

Note: The estimated changes in the fiscal balance are static estimates that abstract from behavioural responses that could be induced from policy changes. These estimates are only reported for illustrative purposes. OECD-recommended structural reforms through higher GDP growth in Box 2 would lead to higher GDP by 1.9%, abstracting from population growth. The public-spending-to-GDP ratio of 56.5% in 2017 would be lowered to (56.5/(1.019x4/10))% over 4 years and, assuming a tax revenue to GDP elasticity of one, the estimated effect on the fiscal balance would be 0.4%. For the increase in the effective retirement age, the pension simulator from the *Conseil d'orientation des retraites* is used (http://www.cor-retraites.fr/simulateur/). The outcomes of the broad-based spending review are scaled using the proposals of the *Action Publique 2022* committee related to health care (improved balance of EUR 5 bn), housing (improved balance of EUR 3 bn), mutualisation of purchases of goods and services by public entities (improved balance of EUR 3bn), central administration and local government reforms (improved balance of EUR 1 bn each). A 0.2% reduction in tax breaks on households' savings could be achieved by removing the favourable tax treatment for housing investment and for the sale of immovable property (Conseil des prélèvements obligatoires, 2018). For the fiscal benefits from removing reduced VAT rates, estimates available in the *Dépenses fiscales volume II* of the *Evaluation des voies et moyens* of the 2019 budget draft bill are used.
Source: OECD calculations.

Ensuring environmental sustainability

France's environmental policy is proactive and ambitious, but the main challenge for France is to fulfil its commitments (OECD, 2016a). The 2017 Climate Plan is a welcome step in that respect (Table 11). France's CO_2 emissions per unit of GDP are among the lowest in the OECD, owing to its predominantly nuclear electricity generation capacity and relatively strong electrification (Figure 26, Panel A). Yet, progress with lowering the energy intensity of production and raising the share of renewable energy has been modest in recent years (panels B, C). On current trends, France will not reach its greenhouse gas emission reduction targets. Transport accounts for around 35% of emissions, and it will be important to concentrate transport infrastructure investment towards zero-carbon transport. Policies to support investment in energy efficiency and renewables have room for improvement (see Chapter 2).

Figure 26. Green growth indicators - France



Source: OECD (2019), *OECD Green Growth Indicators* (database).

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Air quality has improved and population exposure to small particles is lower than in most OECD countries (panel D). Nonetheless, air pollution is estimated to cause 48 000 premature deaths in France, mostly by small particles and around 50% of mortality may be due to road transport (Santé publique France, 2016). Urban sprawl has contributed to an increase in car dependency and traffic congestion. Policies to limit urban sprawl, discussed above, would help contain pollution, energy consumption and CO_2 emissions, with positive effects on biodiversity (OECD, 2016a). Higher taxes on car purchase, modulated according to cars' pollution performance, in particular NOx emissions, could also lower pollution in the absence of taxation directly related to car use and related adverse externalities. Better taking into account environmental externalities in transport taxation and developing an efficient pricing of road infrastructure, combined with targeted social support measures, would make it possible to reduce environmental externalities. Combined with measures to tackle congestion and develop public transport, such as congestion charges, this approach would make significant progress in reducing air pollution.

A more even taxation of fossil energy use would improve the effectiveness of the pricing of carbon emissions in terms of emission reduction. Some industrial emitters are subject to both the European Union's emission trading system (ETS) and energy taxes, others only to either taxes or ETS. In 2015, 15% of industrial emissions (not including emissions from biomass) were not priced at all (OECD, 2018e). Natural gas and coal are taxed less, in terms of carbon content, than petrol, in the manufacturing and construction sectors (OECD, 2018f). Overall 42% of emissions from energy sources were priced at EUR 30 per ton, a low-end estimate of current climate-related costs of carbon (OECD, 2018e). However, France considerably strengthened its carbon tax over 2015-18 for the sectors not included in the EU's ETS system, and the carbon tax reached 44.6 euros/tCO_2 in 2018. However, there remain many exemptions and scope for base broadening.

Additional communication and using tax revenues to compensate the most vulnerable households and improve environmental outcomes could foster citizens' support and make such taxes fairer (CEV, 2017). How environmental tax revenues are used has a substantial impact on their acceptance (OECD, 2010b). In particular, the use of revenues could help offset the negative real income and distributional effects of higher taxes on fossil fuels (Douenne, 2018; Simon and Thao Khamsing, 2016). For example, OECD evidence on heating fuels shows that using a third of the revenues of environmental taxes on domestic energy to raise income-tested cash transfers for low-income households would improve energy affordability (Flues and van Dender, 2017). The planned discussion about the revenues of environmental taxes and their use during the yearly budgetary debate from 2020 is a good move, since it could lead to define future flanking measures along with the planned increases of environmental taxes (Peyrol and Bureau, 2018).

France could make more use of economic incentives to avoid waste and recycle more. The volume of household waste remains large, while its recovery rate remains lower than in Germany and Belgium (panel E). Landfill taxes are lower than in other European high-income countries (European Environment Agency, 2016), and France has no mandatory separate collection of biowaste. The development of pay-as-you-throw schemes linking waste management fees to the amount of waste produced by each households, with higher charges for unrecycled waste could be developed further (European Environment Agency, 2018; Ministère de l'Écologie, du Développement durable et de l'Énergie, 2014). The planned increase in the tax rate of the waste component of the general tax on polluting activities (TGAP, *taxe générale sur les activités polluantes*) is an important step in this direction.

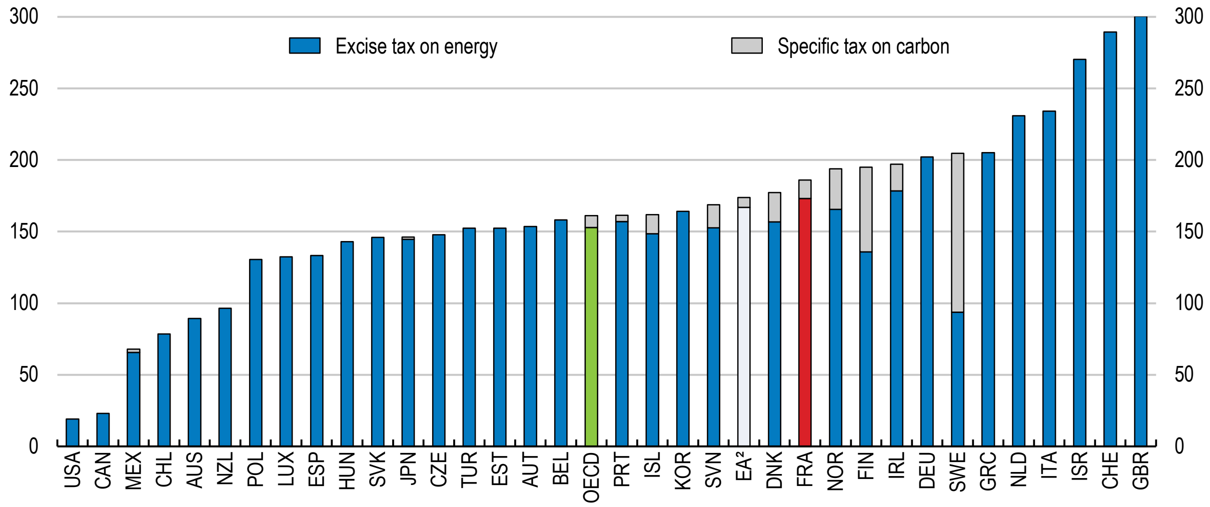
Moreover, France is one of the main consumers of pesticides, which creates risks for the environment and biodiversity (OECD, 2016a). Incorporating environmental impact assessment into all agricultural product authorisation procedures at national and European level would lead to environmental and public health gains. This involves strengthening the risk assessment of phytosanitary products, in particular those of their interaction effects, and to increase the consideration of their impact on the functioning of ecosystems in socio-economic evaluations. Contributing to European research would enable gradually replacing the substances identified as the most harmful. Moreover, accelerating the transition towards sustainable production methods (agroecology), outlined in the "ecophyto" and biodiversity plans (Table 11), would be positive.

Table 11. Past OECD recommendations to improve environmental performance

Main OECD recommendations	Summary of actions taken since the 2017 *Survey*
Air. Adopt and implement the national plan for the reduction of atmospheric pollutants to ensure that standards for the protection of human health are respected; promote the creation of restricted traffic zones and trial the use of urban road tolls.	The national plan for the reduction of atmospheric pollutants was adopted in 2017.
Waste. Strengthen measures to raise awareness and provide information on waste prevention and recycling; step up the pace of implementation of incentive pricing.	No action taken. Incentive pricing remains little used.
Agricultural inputs. Continue to increase the diffuse pollution charge and introduce a similar charge for mineral nitrogen fertilisers; assess the results of the savings certificates scheme for plant protection products.	The diffuse pollution charge is increasing in 2019.
Step up the pace of reform of energy and vehicle taxation for better internalisation of damage related to climate change and air pollution.	The trajectory of the carbon tax hike was steepened in 2017, but the increase in the carbon tax has paused in 2019.
Add quantified objectives, indicators and financing perspectives to the National Biodiversity Strategy.	The biodiversity plan announced in 2018 aims at a net zero land take, and set up a 4-year financing perspective to support biodiversity.
Promote agroecology with information, training, research and financing to facilitate the transition to sustainable modes of production	The biodiversity plan unveiled a series of measures to promote agroecology.

Figure 27. Average effective tax rates in the road sector have increased

Average effective tax rates from excise taxes and specific taxes on carbon[1], EUR per tCO2, 2015



1. Effective tax rates are calculated including the carbon emissions from biomass.
2. Euro area member states that are also members of the OECD, excluding Latvia and Lithuania (15 countries).
Source: OECD (2018), *Taxing Energy Use 2018*, OECD Publishing, Paris.

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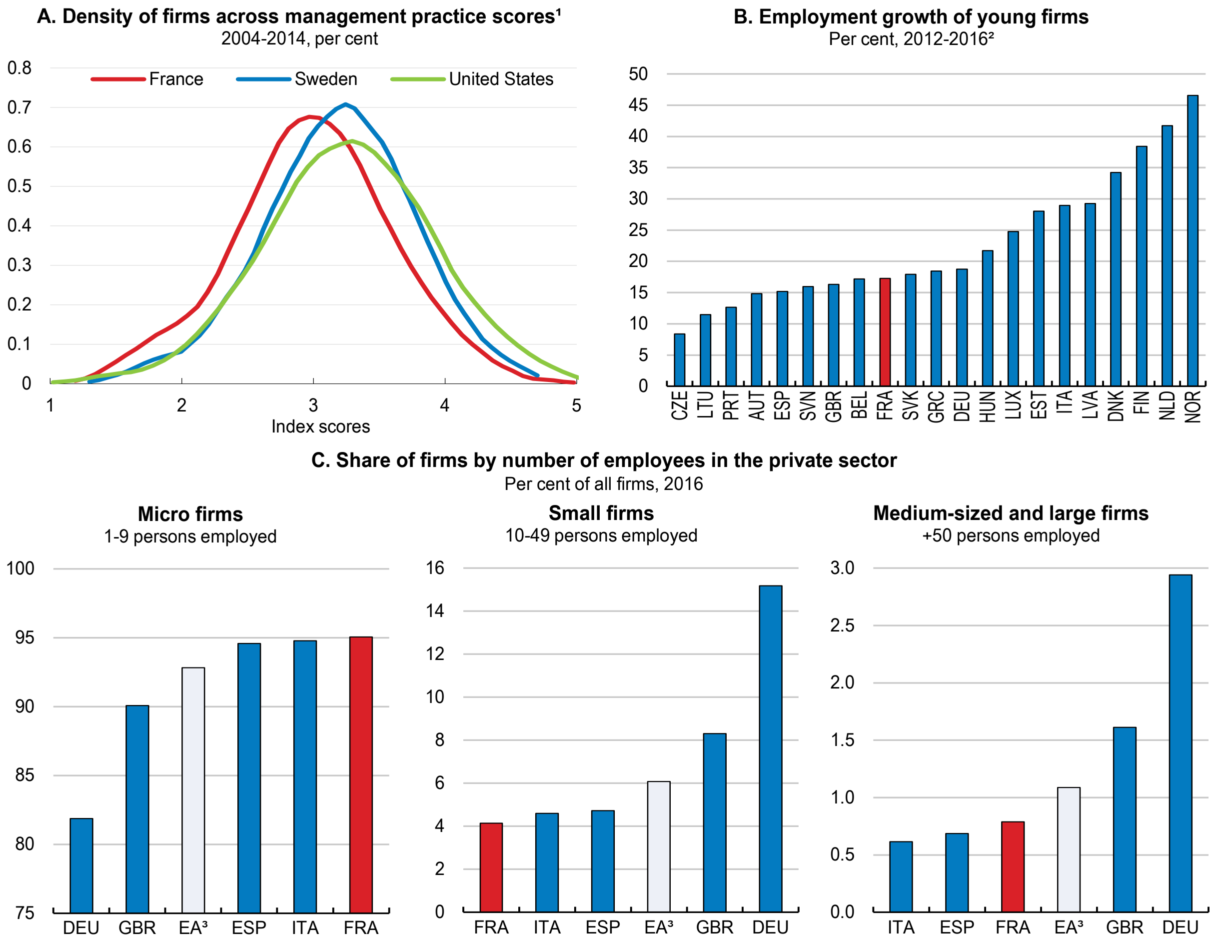
Improving productivity, employment and social mobility

Product and services market reforms would boost growth

Complementary product- and service-market reforms will generate synergies and boost competitiveness and long-run growth. The PACTE bill is expected to encourage firm growth, support competition and raise export performance (De Williencourt, Faci and Ray, 2018; Box 1). However, many services sectors are partly sheltered from competition, and business regulations remain complex. Compared to the United States and Sweden, France has a higher proportion of companies with poor management and human resources practices (Figure 28), which explains more than half of its shortfall in total factor productivity vis-à-vis the United States (Bloom, Sadun and Van Reenen, 2016).

Figure 28. The distributions of management quality and firms size are skewed



1. Index scale from 1 (worst practice) to 5 (best practice), manufacturing sector.
2. Young firms are those less than 2 years old (conditional on survival); average of available years.
3. Euro area member countries that are also members of the OECD (17 countries).
Source: World Management Survey Database; OECD (2018), *OECD Business Demography Statistics* (database).

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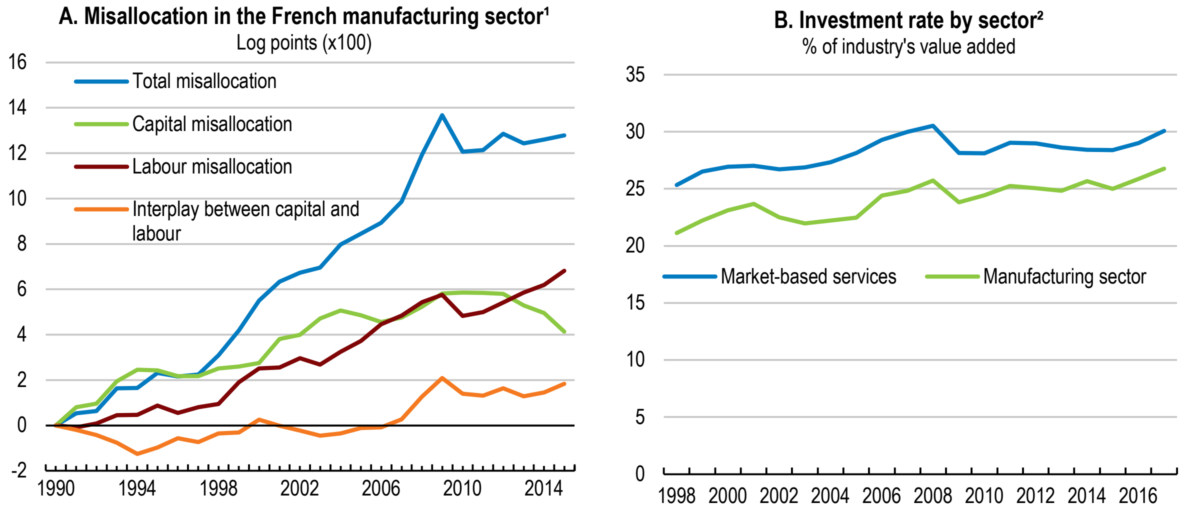
The difficulty for young firms to survive and grow and France's skewed firm distribution, where small businesses are numerous, also explain weak total factor productivity. This skewed firm distribution is partly explained by the self-employed ("*auto-entrepreneur*") regime. However, poor management skills and smaller firm size also strongly relate to the low share of exporting firms (Bacheré, 2018) and disappointing innovation and export performance, notably along the price-competitiveness dimension (Bloom et al., 2018).

Many regulations have hindered firm entry and growth, as well as more efficient resource allocation (Andrews and Cingano, 2014). After 2008, the reallocation of labour and capital towards the most productive firms slowed markedly (Libert, 2017; Figure 29). Even though factor reallocation towards firms whose productivity has increased remained dynamic (Ben Hassine, 2017), reforms of labour and product markets and housing regulations would enhance competition, skills matches and productivity (Figure 30). Regulations on start-ups and those in services sectors that hinder firm entry, competition and productivity are stricter than in many other OECD countries (Bourlès et al., 2013).

Figure 29. Resource misallocation has increased, while investment disappoints



1. Loss in multi factor productivity that can be imputed to misallocation of resources, as computed in Libert (2017).
2. Gross fixed capital formation as a percentage of gross value added, by industry.
Source: T. Libert (2017), "Misallocation Before, During and After the Great Recession", *Banque de France Working paper*, No. 658; INSEE (2018), *Annual national accounts* (database).

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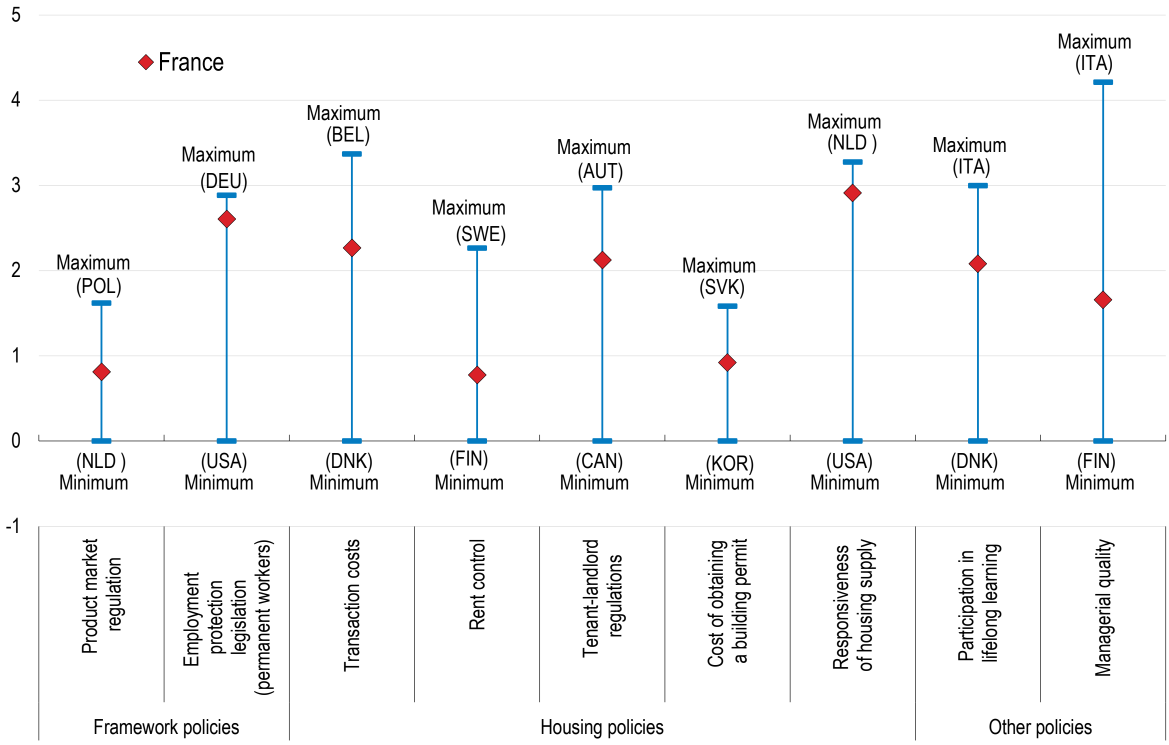
Housing and labour market reforms also hold significant potential to ease reallocation of workers and firms (Chapter 1). Past simplification schemes have insufficiently eased the regulatory burden (Lambert and Boulard, 2018). In particular, the regulatory framework lags more transparent and competitive regulatory alternatives in services (Figure 31). This setting weighs particularly on SMEs and potential exporters, in goods and services sectors, as larger firms are better equipped to succeed in complex regulatory environments and benefits of economies of scale to absorb overhead costs (Rouzet, Benz and Spinelli, 2017). More effective stakeholder engagement in the development of primary laws and subordinate regulations could help raise the effectiveness of regulations. France has a well-developed system of *ex-ante* impact assessments of regulations, but firms and households' engagement play a less important role than in best performing countries (OECD, 2018g).

Easing unduly restrictive regulations would also increase competition and stimulate innovation. Multiple regulatory and tax thresholds may still be a barrier to firm growth, as small firms may shy away from growing beyond them. Studies estimate the cost of such regulations at between 0.3 and 4% of GDP (Garicano, Lelarge and Van Reenen, 2016; Gourio and Roys, 2014), depending on the degree of downward wage rigidity, although older research implies only a small impact on the firm-size distribution (Ceci-Renaud and Chevalier, 2011). Despite significant recent measures to smooth some of these thresholds included in the PACTE bill (Table 12), the new regulatory environment has tended to concentrate them on 11 and 50 employees and new labour-law regulations introduced differentiated treatments by firm size.

Figure 30. Estimated labour productivity gains from policy reforms reducing skill mismatch

Per cent increase in the level of labour productivity associated with aligning policies to best practice



1. *Estimates are based on*: i) logit regressions of probability of mismatch controlling for age, marital and migrant status, gender, education, firm size, contract type, a dummy for working full-time and working in the private sector; and ii) OLS regressions of labour productivity on skill mismatch.
Source: Adalet McGowan, M and D. Andrews (2015), "Skill Mismatch and Public Policy in OECD countries", *OECD Economics Department Working Paper*, No. 1210. http://dx.doi.org/10.1787/5js1pzw9lnwk-en.

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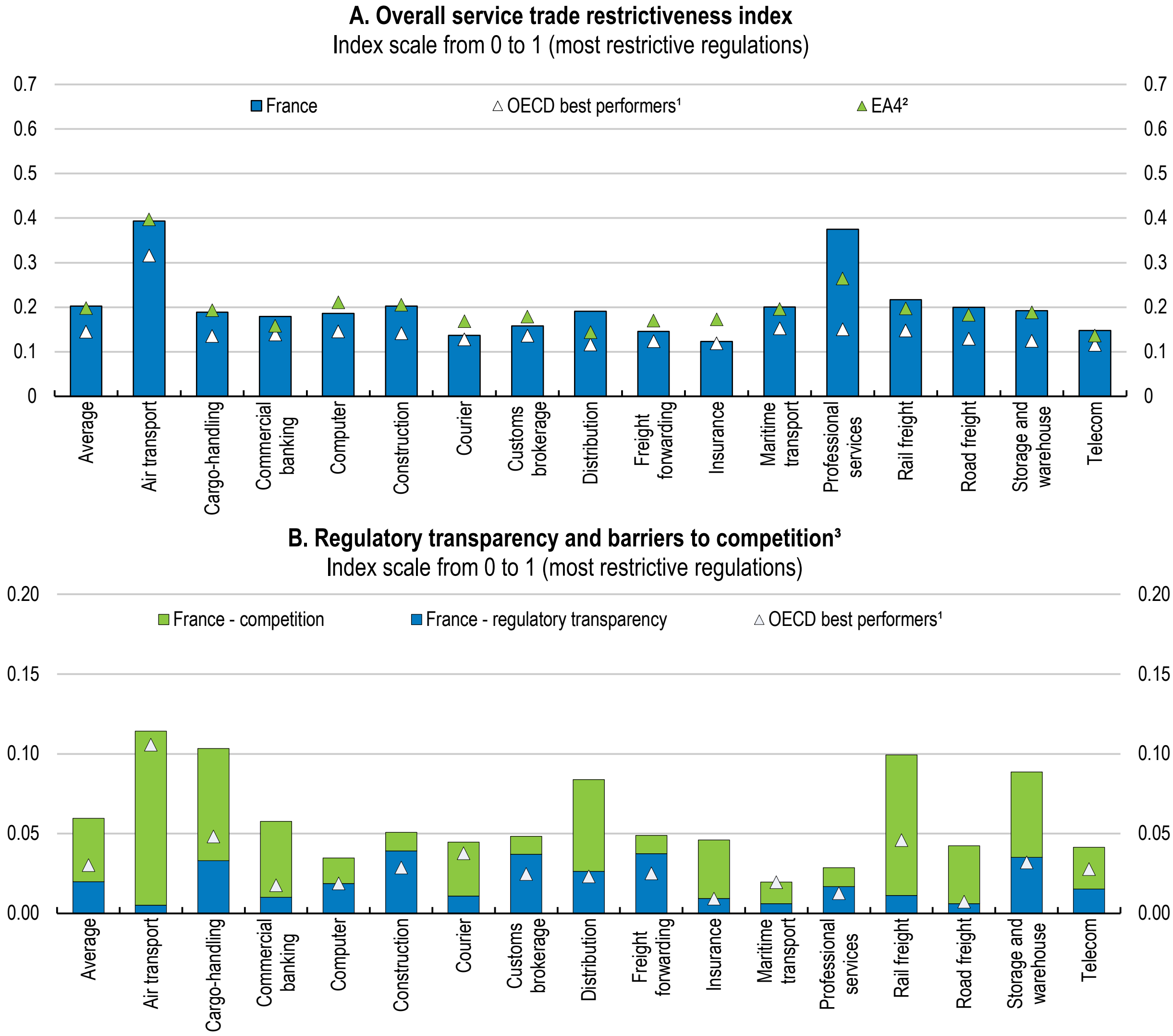
Services play a key role in the economy, accounting for 68% of GDP, 75% of employment in France and 61% of gross exports (OECD, 2018h) without taking into account the growing output of services by manufacturers (Crozet and Milet, 2017). As, in most OECD countries, many professional services are subject to a raft of regulations (in the form of self-regulation and/or government-imposed regulation), some of which have a direct impact on entry include education requirements (such as minimum number of years of study) or practices (such as price controls or reserved tasks). In France, about 1.1 million persons works in a regulated profession. If France's regulations appear more conducive to trade in most services sector, this is not the case in professional services (Figure 31).

Figure 31. Service trade barriers remain important in some key sectors

Services Trade Restrictiveness Index, 2018



1. The OECD best performers is the average of the five OECD countries with the regulations the most conducive to trade.
2. EA4 is the unweighted average of Germany, Italy, the Netherlands and Spain.
3. Most of the measures recorded as barriers to competition and issues related to regulatory transparency apply equally to domestic and foreign firms.
Source: OECD (2019), *Services Trade Restrictiveness Index* (database).

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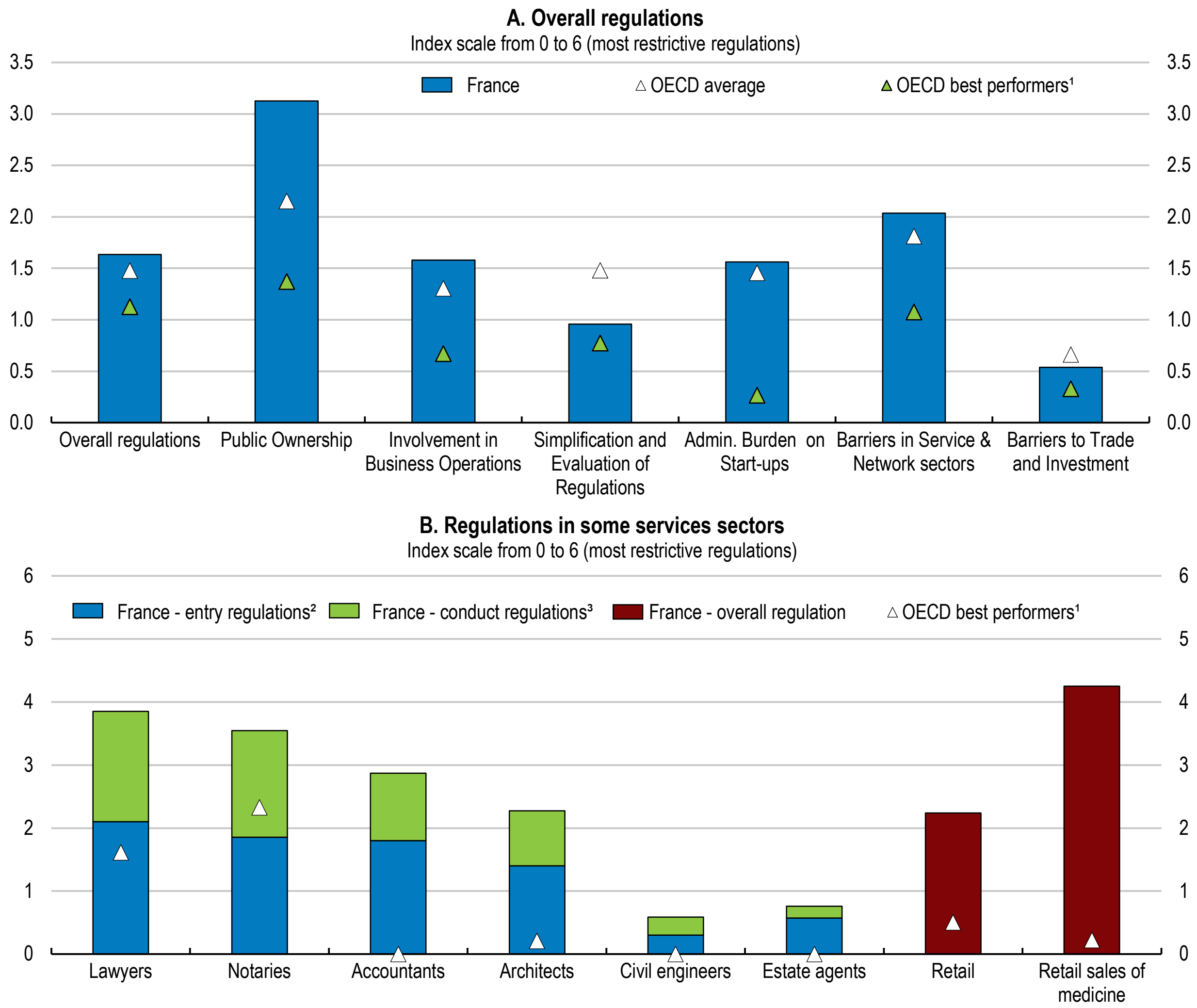
The 2014 Law on Consumer Affairs, the 2015 Law on growth, activity and equal economic opportunity and the 2018 PACTE bill currently in legislative process have tried to strike a better balance between consumer protection and competition. However, for notary, architectural, accountancy, real estate and legal services, barriers to entry and controls on practice in France remained among the highest in the OECD (Figure 32) suggesting that it should be possible to reach a better balance between quality control, integrity and competition. For example, the regulatory framework of accounting services limits the ownership of auditing firms to licenced auditors, while in architecture services, the majority of shares in an architectural firm must be owned by licensed architects (OECD, 2017e).

Figure 32. Product market regulations remain stringent in some sectors, 2018



1. The OECD best performers is the average of the 5 OECD countries with less distortive regulations.
2. Entry regulation refers to the regulation of new entrants in the profession.
3. Conduct regulation refers to the regulation of the conduct of existing professionals.
Source: OECD (2019), *Product Market Regulation database* (Preliminary).

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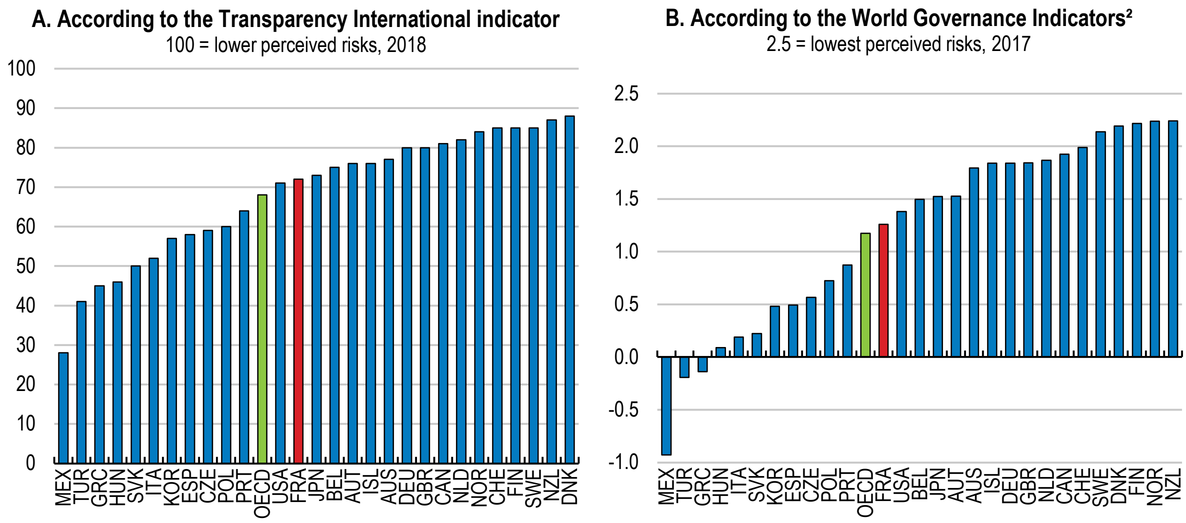
More generally, a further opening of the capital of selected professions would ease new entry and allow economies of scale and scope. For example, France stands out as the country with the most restrictive regulations of retail sales of medicines (Figure 32; Autorité de la Concurrence, 2016). Pharmacies continue to retain a monopoly on the sale of basic drugs and are subject to strict restrictions on ownership and size, capital, distribution chains, and on-line sales. In addition, drivers of cabs and private-hire vehicles (VTC) have to hold some specific diploma to be able to transport passenger that are not justified by safety considerations (Autorité de la concurrence, 2017).

Continuing the efforts to prevent corruption

Continuing efforts to fight corruption is important. Corruption can distort competition, damage the business climate and divert the use of public resources from the public interest, as well as foster a sense of mistrust towards public institutions. Transparency International's Corruption Perceptions Index and the World Bank's Corruption Control Indicator placed France around the median of OECD countries in 2017-18 (Figure 33), even though these indicators are subject to high uncertainty.

Figure 33. Perception of corruption risks



1. Transparency International's Corruption Perceptions Index.
2. Corruption Control index from the World Bank's World Governance Indicators.
Source: Transparency International (2019), *Corruption Perception Index 2018*; World Bank (2018), *World Governance Indicators* (database), The World Bank Group, Washington D.C.

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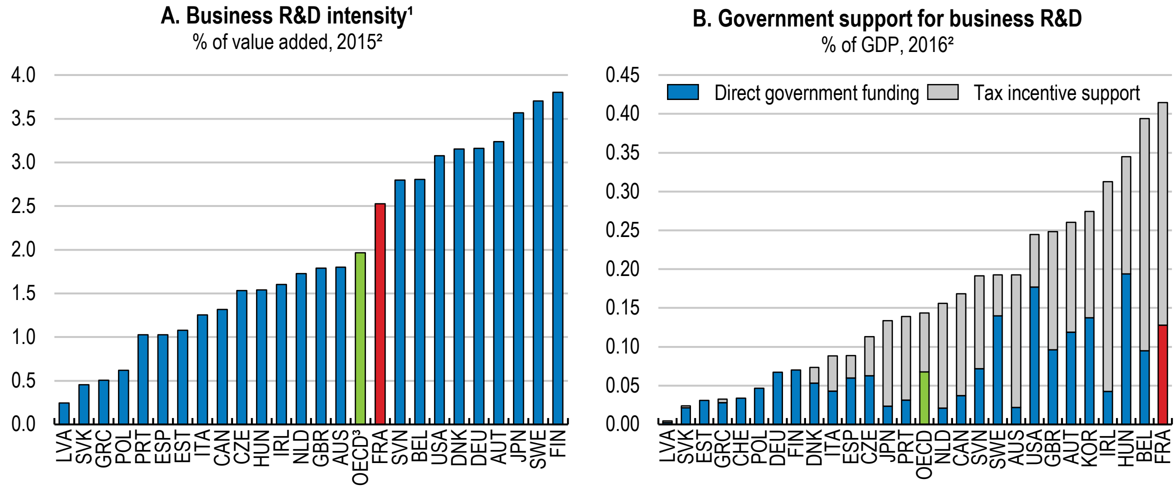
In recent years, France implemented significant reforms to contain the risks of corruption. Based on the recommendations of the OECD Working Group on Bribery, a 2016 law ("*loi relative à la transparence, à la lutte contre la corruption et à la modernisation de la vie économique*") introduced new procedures to criminalise influence peddling of foreign public officials and reinforced the resources allocated to the fight against transnational corruption (Table 12). It also imposed the creation of corruption prevention programmes for businesses and created the French Anti-Corruption Agency (AFA) to support them. In 2016, another law ("*loi relative à la déontologie et aux droits et obligations des fonctionnaires*") also provided a framework, at the national level, to better monitor the risks of conflicts of interest (IMF, 2017). Moreover, a public procurement office at the central-government level (*direction des achats de l'État*) was set up in 2016 with the aim of professionalising public buyers. There is room to improve the knowledge of anticorruption mechanisms within small local governments (AFA, 2018), and thereby to further professionalise public procurement processes at the local level (Chapter 2).

Boosting innovative business investment

Investment in R&D lags behind the OECD's top performers. This also holds for innovation output, particularly among SMEs, the quality of scientific publications and science-industry collaboration (OECD, 2018i; Figure 34). This is partly related to the sectoral mix of the French economy, in which the more R&D-intensive high and especially medium-high tech sectors are under-represented in comparison with the most innovative economies such as Germany.

Figure 34. Business investment has stagnated, despite generous R&D support



1. R&D investment as a percentage of value added in all activities, except for real estate activities, public administration and defence, compulsory social security and education, human health and social work activities and activities of households as employers.
2. Or latest available year.
3. Unweighted average across 30 countries with available data.
Source: OECD (2018), *OECD Science, Technology and Innovation Outlook*, OECD Publishing, Paris; OECD (2018), *OECD R&D Tax Incentive Indicators* (database).

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France has a high rate of support for business R&D relative to countries with a similar business R&D-to-GDP ratio, at 0.4% of GDP in 2016, the second highest in the OECD. Support for R&D mostly takes place through two tax instruments: a volume-based tax credit whose increased significantly in 2008 and social security contribution exemptions targeted at young and innovative firms, while numerous grant schemes are available (CNEPI, 2016; OECD, 2018j). Moreover, a specific investment fund for supporting radical technological innovation (*Fonds pour l'innovation et la rupture*, FII) was created in 2018. In parallel, a new innovation council was set up in 2018 to provide guidance on innovation policies, including a review of existing measures with an objective of simplification.

Despite this significant progress, numerous measures could still improve innovation support. Young an innovative firms enjoy a good access to bank financing and a rapidly increasing venture capital market (Banque de France, 2018c; OECD, 2018k). However, delays to benefit from the refundable R&D tax credit are long for young and smaller firms (Kallenbach et al., 2018).

Leveraging the potential of cryptoassets to finance innovative business investment

Blockchain technology can potentially provide large benefits for the settlement of securities, international payments, and trade finance (Landau and Genais, 2018). Given the lack of EU regulation, the French authorities are in the process of finalizing a legal framework related to the primary (issuers of initial coin offering, ICOs, Box 3) and secondary (i.e., exchange) markets for cryptoassets. As technology evolves fast, there is a need to periodically review the legislation framework as foreseen in the PACTE bill. Moreover, to address the risks of regulatory competition, promoting an EU-wide approach to cryptoasset regulation appears warranted.

Box 3. Initial coin offering

ICOs allow start-ups to issue their own coins (also called tokens) to raise funding through blockchain technology and without an intermediary. They can be divided in three categories depending on their function:

- *Payment tokens* (often called cryptocurrencies) are mostly used for payments. Unlike official currencies, they are not backed by a central bank.
- *Security tokens* are similar to an initial public offering (but only on a blockchain). As such, they are regulated as traditional securities (Prospectus and MiFID Directives).
- *Utility tokens* represent a new form of funding: they offer the owner different future services or products in exchange for a payment (e.g., access to software, the use of storage space on a computer, or voting rights).

While reliable data about the total funds raised by ICOs is missing, the AMF – France's Financial Markets Authority – has information about 15 French ICOs that raised EUR 89 mln from November 2016 to October 2018 (compared to USD 185 mln in the UK and USD 547 mln in Switzerland over a similar period according to ICOWatchlist.com). In the first half of 2018, ICOs amounted to roughly 5 percent of equity capital raised by French firms, and 68 issuers were conducting or planning to conduct an ICO in France as of November 2018 (Le Moign, 2018).

The AMF should be transparent about its methodology for granting visa for utility tokens and provide comprehensive data about tokens that apply for a visa to attract investors. The PACTE bill offers the possibility for issuers of utility tokens to obtain a visa from the AMF based on the AMF's analysis of the ICO's information document (white paper), and this visa can be withdrawn if the issuer does not respect its commitments.

Evaluating the need to apply EU securities regulation for utility tokens would be welcome. According to the AMF, utility tokens cannot be considered as securities because they do not offer its owner the right to participate in the issuer's return (through dividends or fixed income) and do not represent an ownership title (AMF, 2017). However, utility tokens are typically used as investment products. They are issued by start-ups to raise funding and are afterwards traded on specialized cryptoasset exchanges. Since their future value is highly uncertain, they give rise to risks that are very similar to risks on other capital markets in terms of investor protection and market abuse (ESMA, 2018).

Table 12. Past OECD recommendations to improve the business environment

Main OECD recommendations	Summary of actions taken since the 2017 *Survey*
Task an independent institution to conduct a thorough review of all existing and proposed regulations affecting firms, applying the OECD Competition Assessment Toolkit principles.	No action taken.
Continue to streamline burdensome permit procedures for large new stores. Eliminate restrictions on loss-leader selling, dates of discount sales and opening hours (for which time-off and salary compensation should be negotiated).	The 2017 ordonnances streamlined workers' representations for larger firms and required industry-level labour agreements to take into account the needs of smaller firms. By contrast, sale periods have been restricted.
Continue to liberalise the regulated professions by: reducing entry requirements to those needed to protect the public; narrowing professions' exclusive rights; eliminating regulated tariffs in potentially competitive activities; and gradually abandoning quotas.	The 2018 PACTE currently in legislative process aims to simplify firm entry requirements and reduce entry barriers in craft occupations. Quotas are to be eliminated for doctors.
Ensure non-discriminatory access to the rail network. In particular, modernise the process of allocating service slots for rail freight, and separate the rail infrastructure manager from the station manager. Pool regulatory powers for the various modes of transport under a single land transport regulator.	The 2018 reform reorganised the railway sector to open up the passenger-transport sector to competition.
Obtain an independent assessment of the impact on competition of laws and regulations, and increase dialogue on this subject between the competition authority and the Ministry for the Economy during the decision-making process.	No action taken.
Continue efforts to comply with the OECD convention on Combating Bribery of Foreign Public Officials in International Business Transactions.	The law of 9 December 2016 strengthened the anti-corruption framework. A new body, the French Anticorruption Agency, was set up in 2017 to identify and prevent corruption.

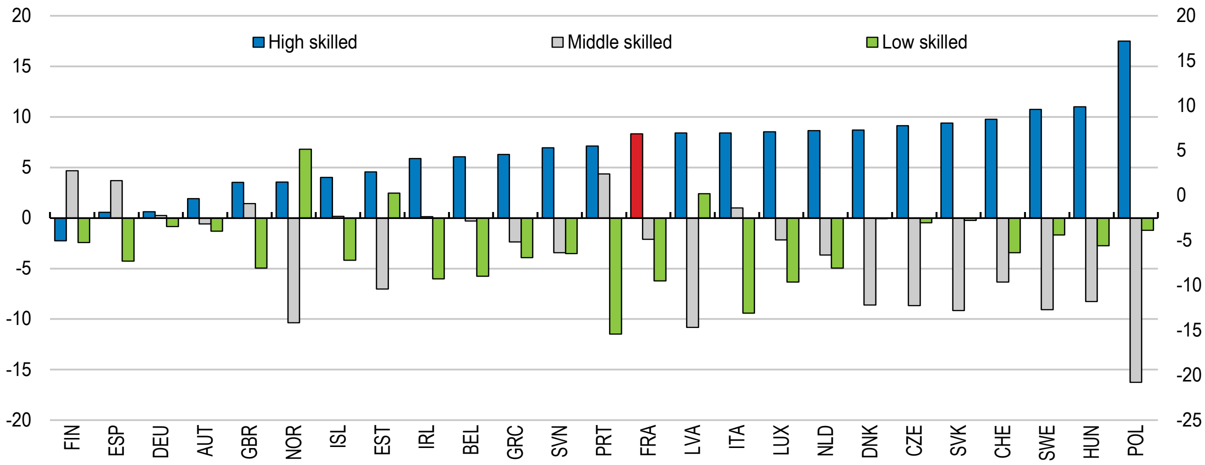
Strengthening skills through initial education

The labour market is continuing to shift towards higher-skilled employment (Figure 35). This reflects that over the past decades, the service sector has expanded and industry has moved from heavy industries to higher value added production that links into global value chains, leading to an increase in medium and high technological intensive manufacturing, although manufacturing accounts for a rapidly decreasing part of employment. These changes are taking place as firms increasingly search for skilled workers. Thus, to sustain growth it is becoming increasingly important to adjust and enhance skills, improve allocation of labour and mobilise all underutilised labour resources (Chapter 1).

France does not strike the right balance in spending per pupil across education levels to best address inequalities in educational outcomes. Relative to the OECD average, spending per student is comparable to this average in tertiary education, above for upper secondary education (OECD, 2018l), but below for pre-primary and primary education levels (Figure 36). Moreover, children's academic performance heavily depends on parents' socio-economic background, hampering social mobility (OECD, 2016c), even though intergenerational mobility in terms of educational attainments has increased for the most recent generations. There is also extensive evidence that teachers are more inexperienced, more often on temporary contracts, and that staff turnover is stronger for schools in poor neighbourhoods (CNESCO, 2018).

Figure 35. The shift towards high skilled employment is expected to continue

Change in share of total employment between 2015 and 2025, in percentage points[1]

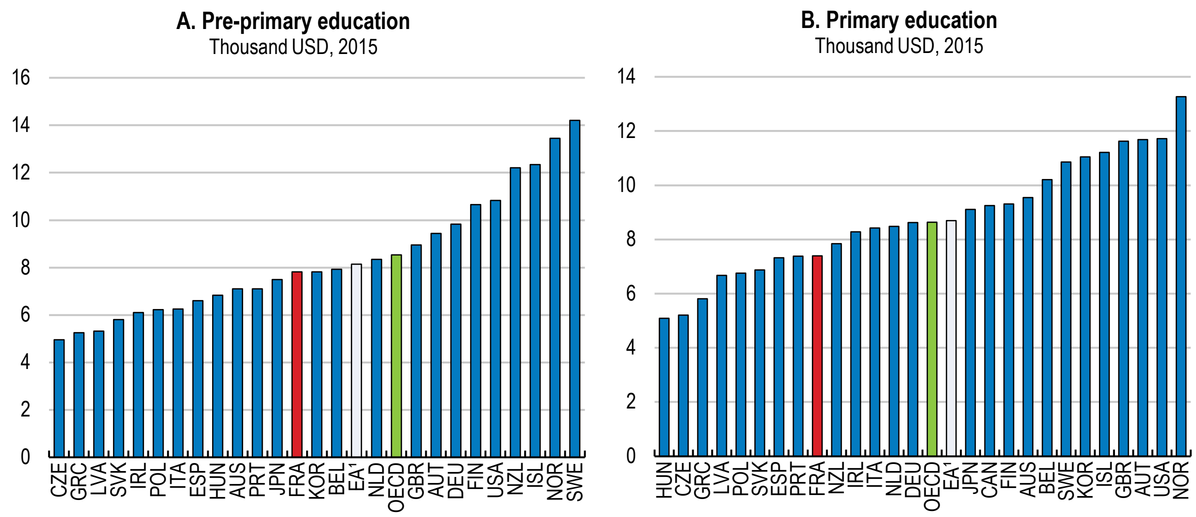


1 High-skill occupations include jobs classified under the ISCO-88 major groups 1, 2, and 3. That is, legislators, senior officials, and managers (group 1), professionals (group 2), and technicians and associate professionals (group 3). Middle-skill occupations include jobs classified under the ISCO-88 major groups 4, 7, and 8. That is, clerks (group 4), craft and related trades workers (group 7), and plant and machine operators and assemblers (group 8). Low-skill occupations include jobs classified under the ISCO-88 major groups 5 and 9. That is, service workers and shop and market sales workers (group 5), and elementary occupations (group 9). The ISCO-88 major group 6 for skilled agricultural, forestry and fishery workers is excluded.
Source: CEDEFOP (2017), "Forecasting skill demand and supply", European Centre for the Development of Vocational Training, http://www.cedefop.europa.eu/en/events-and-projects/projects/forecasting-skill-demand-and-supply/.

StatLink https://doi.org/10.1787/888933949991

Figure 36. Expenditures on pre-primary and primary education are low

Annual expenditure per child in PPPs-converted USD



1. Euro area member countries that are also members of the OECD (17 countries), excluding Estonia in Panel A.
Source: OECD (2018), *Education at a Glance 2018*, Tables B2.3a and C1.1, OECD Publishing, Paris.

StatLink https://doi.org/10.1787/888933950010

To address some of these concerns and to better tackle inequalities in education that start building up from early ages, pre-primary education will be compulsory for three year olds from the 2019 school year (loi "*pour une école de la confiance*"), class sizes are being halved in grade 1 and grade 2 in priority education of primary school networks (*Réseau d'éducation prioritaire*, REP), and the salary bonus for staff in those schools is increasing (Table 13). Yet, the number of teachers per child is low in pre-primary education in international comparison (23 children per teacher – 8 children more than the OECD average), even though assistants in pre-primary schools intervene along with teachers. One of the challenges for improving the quality of pre-primary education is to improve the initial training of assistants in pre-primary education. As early educational interventions for disadvantaged children are more efficient relative to interventions taking place at later stages (OECD, 2018m), the authorities could consider increasing staff at the pre-primary education level in disadvantaged neighbourhoods. Going forward, beyond a reduction in class sizes in poor neighbourhoods, efforts should also concentrate on professional-development policies to attract and develop high-quality educators and teachers where the challenges are the greatest.

Table 13. Past OECD recommendations to improve learning outcomes of disadvantaged children

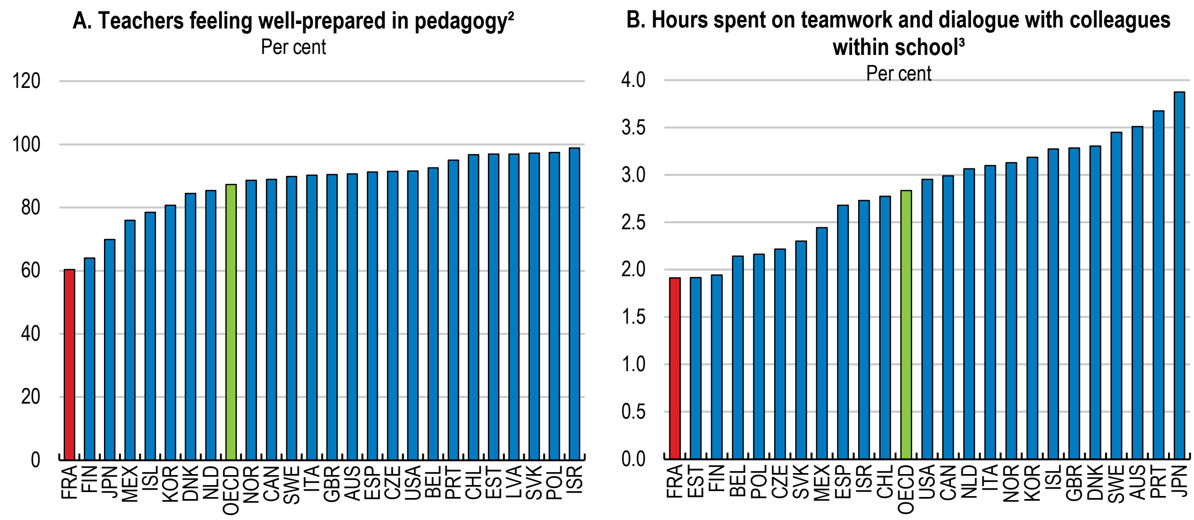
Main OECD recommendations	Summary of actions taken since the 2017 *Survey*
Offer attractive salaries and career prospects to teachers in schools with many pupils from disadvantaged backgrounds.	The annual salary bonus for staff in priority school networks is increasing by 3000 euros in steps.
Promote an innovative range of different practices in teacher training in order to meet the different needs of pupils.	The authorities strengthened teachers' initial training by setting up new institutes (*Instituts nationaux supérieurs du professorat et de l'éducation*)
Bring schools' human resource budgets into line with the number of their students, with top-ups for poor and foreign-language children. Publish both budgets and underlying formulae.	The reform of priority education and the revision of budget allocation rules in 2018 strengthened the role of social criteria in schools' funding.
Better target public spending at transportation, childcare services and face-to-face public services in poor neighbourhoods.	The class size in grade 1 and grade 2 in priority primary education school networks is being halved to 12 pupils.

In higher education, the public funding advantage per student enjoyed by students preparing the entry exam of highly competitive elite schools (the *grandes écoles* and their preparatory classes, CPGE) is significant. Given the overrepresentation of children from privileged backgrounds in these courses (OECD, 2013b), measures (e.g., "*cordées de la réussite*") aim to introduce greater equity in access to these programs. Moreover, less than half of students complete their undergraduate studies (*licence*) in three years. A reform of access to higher education was initiated with a 2018 law (*loi relative à l'orientation et à la réussite des étudiants*). This reform aims to foster social and geographical mobility, and tackle school dropout in undergraduate studies, particularly in universities. It also customises guidance services through dedicated means.

Stepping up efforts to improve initial and ongoing career training of teachers is needed, as envisaged in a 2019 law (loi "*pour une école de la confiance*"), which sets up new institutes for teachers' initial training. Professional training is only compulsory for primary education teachers, and teachers tend to feel underprepared in pedagogical training and show little co-operation relative to other OECD countries (Figure 37). Putting in place teacher-appraisals mechanisms, for example by introducing an annual training review as currently done for other categories of civil servants, will be helpful to foster teachers' continuous improvements (Cour des comptes, 2017b). Moreover, granting greater autonomy to school principals in the teachers' hiring decision, teachers' performance appraisal and pay, could also help attract the most talented teachers to the most challenging classrooms (OECD, 2018n). This will also entail better training for school principals to these new responsibilities. Moreover, the planned development of teachers' job openings for specific profiles ("*postes à profil*") should lead to a better match between the skills and the position of teachers.

Figure 37. Pedagogical training and teacher teamwork are weak

Teachers in public lower secondary education, 2013[1]



1. Belgium, Canada and the United Kingdom refer to, respectively, only Flanders, Alberta and England.
2. Share of lower secondary education teachers who feel well or really well prepared in the pedagogy of subjects being taught.
3. Average number of 60-minute periods that lower secondary education teachers report having spent on the mentioned activities during the most recent complete calendar week (not shortened by breaks, public holidays, sick leave, etc.)
Source: OECD (2013), *OECD Talis Statistics* (database).

StatLink https://doi.org/10.1787/888933950029

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