

French public finances: Chronicle of an announced overrun?

France slid into recession in the spring of 2008¹. There have in fact been four consecutive quarters of contraction in GDP since the second quarter of 2008, plunging France into the worst recession in its post-Second World War history². And the crisis is not over. Even though the "severe" stage of the recession now seems to be over (GDP has declined by 2.6% in six months³), the hypothesis of a cyclical recovery from next year onwards still seems very fragile. For our part, we expect a gradual levelling-off in activity during the summer (i.e. an annual contraction in GDP of approximately 2.7%) in our main scenario, linked to a large extent to the concomitant growing weight of the economic stimulus packages decided on a global scale⁴. In 2010, activity is likely to remain listless overall (+0.0%), under the effect of a new weakening of domestic demand (household consumption) and the fact that the support measures for activity in France and other countries will gradually run out of steam.

Against such a backdrop, it is not surprising to see a surge in fiscal deficits (6.7% of GDP in 2009, 7% in 2010, according to our forecasts). The better French performance expected this year (compared with the euro zone⁵) is, besides, intimately linked to the weight of the main fiscal stabilisers, which differ from one economy to the next within the union (taxes, welfare transfers, civil service employment). The government's stance on this issue - that the deficit makes it possible to dampen the crisis - is in our view absolutely justified in this respect. On the other hand, what is less justified is the persistent asymmetry when it comes to the role that the budget is to play during the cycle (counter-cyclical called for during economic downturns, pro-cyclical sought during economic upturns), and which explains why France will probably still rank at the top of the list of the least virtuous countries in the budgetary field in 2012.

In this respect, the Versailles statement revealed the French penchant for not complying with the European commitments - which it, furthermore, helped define and draw up. Whereas a number of member countries in the union⁶ have already announced austerity measures to reduce their deficits in the wake of the crisis, France is an exception by not undertaking to take any measures to improve the situation. Whereas a hike in the tax burden clearly seems to be out of the question, the only options considered to enable a (hypothetical) return to equilibrium actually remain the sacrosanct "keeping government spending in check" and the eternal hope that growth will outpace potential growth for an extended period of time. In this respect, while we believe it is wishful thinking to expect growth to rapidly return to its full potential, it seems to a large extent illusory⁷ to fuel hopes of cyclical surpluses in the longer term - surpluses that are supposed to make it possible to absorb the level of the post-crisis deficit. On the other hand, while we do not doubt the government's stated resolve to cut government expenditure, we nevertheless remain relatively sceptical about the efforts currently made, by using this single measure, to achieve a balanced budget⁸ in the near future. In other words - unless France definitively reneges on the commitments that link it to its main partners (Stability and Growth Pact) - a hike in the tax burden in the near term is in our view absolutely inevitable.

Jean-Christophe Caffet

¹ And not during the autumn, as INSEE's first GDP estimates could indicate.

² The crisis in the 1930s ended in a contraction in French GDP of nearly 15% in four years.

³ From October 2008 to March 2009.

⁴ See Flash no. 2009-274: "Are cycles lagged in the G7?"

⁵ We expect a 4.2% contraction in GDP in the euro zone this year.

⁶ Ireland, Spain, the Netherlands, Germany, etc.

⁷ See in particular Flash no. 2009-286: "Crisis and potential production (and destruction of capacity)" and Special report no. 2009-193: "The worst in a crisis: The shortfall in potential GDP drives both the structural fiscal deficit and the structural unemployment rate upwards"

⁸ In a context where, moreover, welfare spending is set to increase (pensions, healthcare, etc.).