COUNCIL RECOMMENDATION

of 12 July 2011

on the National Reform Programme 2011 of France and delivering a Council opinion on the updated Stability Programme of France, 2011-2014

(2011/C 213/03)

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Articles 121(2) and 148(4) thereof,

Having regard to Council Regulation (EC) No 1466/97 of 7 July 1997 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies [1], and in particular Article 5(3) thereof,

Having regard to the recommendation of the European Commission,

Having regard to the conclusions of the European Council,

Having regard to the opinion of the Employment Committee,

After consulting the Economic and Financial Committee,

Whereas:

(1) On 26 March 2010, the European Council agreed to the Commission's proposal to launch a new strategy for jobs and growth, Europe 2020, based on enhanced coordination of economic policies, which will focus on the key areas where action is needed to boost Europe's potential for sustainable growth and competitiveness.

(2) On 13 July 2010, the Council adopted a recommendation on the broad guidelines for the economic policies of the Member States and the Union (2010 to 2014) and, on 21 October 2010, adopted a decision on guidelines for the employment policies of the Member States [2], which together form the 'integrated guidelines'. Member States were invited to take the integrated guidelines into account in their national economic and employment policies.

(3) On 12 January 2011, the Commission adopted the first Annual Growth Survey, marking the start of a new cycle of economic governance in the EU and the first European semester of ex-ante and integrated policy coordination, which is anchored in the Europe 2020 strategy.

(4) On 25 March 2011, the European Council endorsed the priorities for fiscal consolidation and structural reform (in line with the Council's conclusions of 15 February and 7 March 2011 and further to the Commission's Annual Growth Survey). It underscored the need to give priority to restoring sound budgets and fiscal sustainability, reducing unemployment through labour market reforms and making new efforts to enhance growth. It requested Member States to translate these priorities into concrete measures to be included in their stability or convergence programmes and national reform programmes.

(5) On 25 March 2011, the European Council also invited the Member States participating in the Euro Plus Pact to present their commitments in time to be included in their stability or convergence programmes and their national reform programmes.

(6) On 3 May 2011, France submitted its 2011 stability programme update covering the period 2011-2014 and its 2011 national reform programme. In order to take account of the interlinkages, the two programmes have been assessed at the same time.

(7) France was relatively less affected than other Member States by the economic and financial crisis, with a decline of 2,7 % in GDP in 2009, partly due to sizeable economic stabilisers and the resilience of household consumption. The banking sector also proved to be resilient. In 2010, the economy recovered and, overall, GDP growth came out at 1,5 %. However, the economic crisis has substantially impacted France's public finances. Due to the automatic stabilisers and discretionary fiscal stimulus, the general governement deficit rose from 3,3 % of GDP in 2008 to 7,5 % in 2009. Similarly, the crisis has exacerbated the insufficient utilisation of labour and the structural weaknesses of the French labour market, where there was a relatively high level of unemployment of 9,7 % in 2010. In addition, the trade balance of goods has gradually deteriorated during the last decade, highlighting the challenges of French companies in terms of cost and non-price competitiveness.

(8) Based on the assessment of the updated stability programme pursuant to Regulation (EC) No 1466/97, the Council is of the opinion that the macroeconomic scenario underpinning the budgetary projections is

[1] OJ L 209, 2.8.1997, p. 1.
[2] Maintained for 2011 by Council Decision 2011/308/EU of 19 May 2011 on guidelines for the employment policies of the Member States (OJ L 138, 26.5.2011, p. 56).

favourable, especially as expected growth levels remain well above the potential growth in later years. After a better-than-expected deficit of 7 % of GDP in 2010, the stability programme plans to bring it down to 3 % of GDP in 2013, which is the deadline set by the Council for correcting the situation of excessive deficit, and to continue consolidation thereafter. Starting from a debt of 82 % of GDP in 2010, the debt ratio is set to increase until 2012 (86 %), after which it will decline slightly. The deficit and debt adjustment paths are subject to risks, which include the possibility of a macroeconomic scenario that could turn out to be less favourable, the fact that the measures are not sufficiently specified to reach the targets from 2012 onwards, and the fact that targets have often been missed in the past, notwithstanding the better-than-expected outcome in 2010. Therefore, it cannot be ensured that the excessive deficit will be corrected by 2013 unless further measures will be taken as needed. The medium-term objective of a balanced budget in structural terms will not be reached within the stability programme period. The average annual fiscal effort over the 2010-2013 period as recalculated by the Commission services according to the commonly agreed methodology is slightly below what was included in the Council Recommendation of 2 December 2009 ('above 1 % of GDP').

(9) Implementation of fiscal consolidation remains a major challenge. Avoiding expenditure slippages by means of a strengthened fiscal effort based on fully specified measures is vital to re-establishing a sustainable fiscal position, especially since the 2013 target does not provide any safety margin below the 3 % of GDP threshold. Moreover, as specified in the 2011-2014 Multiyear Public Finance Planning Act voted in December 2010 it would be appropriate to use all windfall revenues to accelerate the deficit and debt reduction. According to the Commission's latest assessment, the risks with regards to long-term sustainability of public finances appear to be medium. To improve the long-term sustainability of public finances, France adopted a new pension reform in 2010. The planned measures, including the gradual increase in the minimum retirement age from 60 to 62 and in the statutory retirement age from 65 to 67, as well as the phasing out of early retirement schemes, should have an impact on the low employment rate of older workers. Moreover, the pension system is expected to be in balance by 2018. A deficit is likely to appear thereafter unless further measures are taken. The latest pension reform has also created a new public body, the 'Comité de pilotage des régimes de retraite', which is in charge of presenting annual assessments of the budgetary situation of pension accounts and, if there is any likelihood of a deterioration, of proposing corrective measures.

(10) The current employment protection legislation is still too strict: the conditions for economic dismissals are subject to legal uncertainty. This is leading to labour market outcomes where workers on indefinite labour contracts (the majority of the labour 'stock') benefit from a relative degree of security and workers on temporary labour contracts (the majority of the inflow into the labour market) are exposed to uncertainties. Hence, the share of temporary contracts is significantly higher for young workers, and there are few transitions from temporary contracts to permanent contracts. This segmentation also applies to access to vocational training. There is consequently a high turnover and a limited accumulation of human capital in these workers. Young workers and the low-skilled are therefore exposed to disproportionate risks in the labour market. The aim of the Renewal of Social Dialogue Act and of the 2008 Labour Market Modernisation Act was to modernise social dialogue and to address the issue of labour market dualism. The latter Act notably introduced a new procedure for terminating permanent contracts by mutual agreement (*rupture conventionnelle*) which is now increasingly used.

(11) The French unemployment rate was slightly above the EU average in 2010 and long-term unemployment is on the rise (3,9 % in 2010 versus 2,9 % in 2008). In this context, public employment services should play an important role in supporting the unemployed in their search for a job. In France, the new one-stop shop public employment service *Pôle Emploi* has so far shown mixed results. In 2009-2010, in the context of the crisis and of a significant increase in the number of job seekers, its main objective was mainly focused on the merger of the two pre-existing administrative entities. Outsourcing of placement services has so far yielded mixed results in achieving the return to work targets set by *Pôle Emploi*. At the same time, *Pôle Emploi* resources dedicated to individualised support of job seekers remain underdeveloped (71 full-time equivalents per 10 000 unemployed, which is significantly below the levels recorded in some peer countries).

(12) The French current account deficit has gradually deteriorated during the last decade, reflecting the decline in the trade balance of goods, partly due to a decrease in labour cost competitiveness after the single minimum wage was reintroduced in the 2003-2005 period (the previous reform of the 35 hours working week had resulted in five different minimum levels). Some improvements have been made to the indexation procedure (creation of an advisory commission of independent experts, elimination of discretionary hikes) leading to a moderation of the increase in the minimum wage. As a result, the proportion of employees that are paid the minimum wage has decreased substantially, enabling better wage differentiation. The French minimum wage is still among the highest in the EU when compared to the median salary even if the tax-wedge is much lower than for the average salary due to cuts in employers' social security contributions.

(13) France has one of the highest tax and social security burdens on labour in the EU, while the tax on

consumption remains relatively low. Moreover, environmental tax revenues as a share of GDP are also below the EU average. Rebalancing the tax system, including for example by switching taxation from labour towards consumption and the environment, is likely to have a beneficial effect on jobs as well as on environmental objectives.

(14) Tax and social security exemptions (including *niches fiscales*) in France are very high. In addition, understanding and exploiting the benefits of the system requires firms and households to invest in extensive expertise. While tax expenditures are used to implement a given economic policy, there has not been so far a systematic assessment whether they have managed to fulfil the objectives pursued although a review is planned to be carried out in 2011 according the 2009-2012 Multiyear Public Finance Planning Act. In the past, their substitutability with public expenditures has allowed the French authorities to formally meet existing spending rules, although further shifts are no longer possible as stated in Article 9 of the 2011-2014 Multiyear Public Finance Planning Act. A discretionary increase in tax revenue (mainly through the reduction of tax expenditures) by around 0,75 % of GDP over the period 2011-2013 is foreseen by the French authorities. The precise tax expenditures to be abolished have only been partly identified as from 2012.

(15) Competition in the retail sector is still hampered by administrative restrictions on the opening of large retail outlets, and a ban on resale below cost. In the services sector, there are still barriers to competition for several regulated professions, which could be tackled either by reviewing the entry conditions, or by gradually doing away with certain quotas (*numerus clausus*) and the exclusive rights that these professions hold.

(16) France has made a number of commitments under the Euro Plus Pact. On the fiscal side, France has undertaken to swiftly implement the 2010 pension reform. With a view to strengthening fiscal sustainability, France will also change its constitution to introduce binding multiannual budget planning. To increase labour participation, various measures are being considered to increase active labour market policies (e.g. apprenticeship to ease the school-to-work transition of younger workers, additional childcare facilities by 2012 to improve female employment prospects, strengthening of the public employment services for jobseekers). The competitiveness measures focus on improving the higher education system and promoting research and development (R&D) and innovation (*investissements d'avenir*), as well as reducing the administrative burden by implementing a comprehensive programme of administrative simplification. These commitments refer to three of the four areas of the Pact, leaving out the financial sector. Although they are taken in those areas where the main challenges lie, many of them (particularly those concerning fiscal governance or support to higher education and R&D) are confirmations of existing public policies/reforms. The reform agenda does not seem fully consistent with the extent of the macroeconomic challenges faced in the labour market or the business environment. In addition, the envisaged constitutional reform is subject to political uncertainty. These Euro Plus Pact commitments have been assessed and taken into account in the recommendations.

(17) The Commission has assessed the stability programme and national reform programme, including Euro Plus Pact commitments for France. It has taken into account not only their relevance to sustainable fiscal and socio-economic policy in France but also their conformity with EU rules and guidance, given the need to reinforce the overall economic governance of the EU by providing EU-level input into future national decisions. In this light, the Commission considers that the fiscal consolidation strategy needs to be made more specific, for 2012 and beyond, in order to ensure that the excessive deficit is corrected by 2013 and the debt is brought onto a downward path. Any windfall revenues should be used to accelerate the deficit and debt reduction, as specified in Article 11 of the 2011-2014 Multiyear Public Finance Planning Act. A shift from labour towards environmental and consumption taxes, and a streamlining of tax expenditure, would bolster fiscal and environmental objectives and improve the business environment. Further steps in 2011-2012 should focus on adapting the employment protection legislation to reducing the dualism of the labour market, and on strengthening public employment services in order to provide comprehensive support to jobseekers. Existing policy on minimum wage moderation should be pursued. Competition should be fostered in regulated professions and retail trade.

(18) In light of this assessment, also taking into account the Council Recommendation under Article 126(7) of the Treaty on the Functioning of the European Union of 2 December 2009, the Council has examined the 2011 update of the stability programme of France and its opinion [1] is reflected in particular in its recommendation 1 below. Taking into account the European Council conclusions of 25 March 2011, the Council has examined the national reform programme of France,

[1] Foreseen in Article 5(3) of Regulation (EC) No 1466/97.

HEREBY RECOMMENDS that France take action within the period 2011-2012 to:

1. Ensure the recommended average annual fiscal effort of more than 1 % of GDP over the period 2010-2013 and implement the correction of the excessive deficit by 2013, in line with the Council recommendations under the EDP, thus bringing the high public debt ratio on a downward path, and ensure adequate progress to the medium-term objective thereafter; specify the necessary corresponding measures for 2012 onwards, take additional measures if needed and use any windfall revenues to accelerate the deficit and debt reduction as planned; continue to review the sustainability of the pension system and take additional measures if needed.

2. Undertake renewed efforts, in accordance with national practices of consultation with the social partners, to combat labour market segmentation by reviewing selected aspects of employment protection legislation while improving human capital and upward transitions; ensure that any development in the minimum wage is supportive of job creation.

3. Encourage access to lifelong learning in order to help maintain older workers in employment and enhance measures to support return to employment. Step up active labour market policies and introduce measures to improve the organisation, decision-making, and procedures of the public employment service to strengthen services and individualised support provided to those at risk of long-term unemployment.

4. Increase the efficiency of the tax system, including for example through a move away from labour towards environmental and consumption taxes, and implementation of the planned reduction in the number and cost of tax and social security exemptions (including 'niches fiscales').

5. Take further steps to remove unjustified restrictions on regulated trades and professions, in particular in services and the retail sector.

Done at Brussels, 12 July 2011.

For the Council

The President

J. VINCENT-ROSTOWSKI