



Which Reforms for France? The CAE's Recommendations

Les notes du conseil d'analyse économique, no 15, July 2014

Economic policy in France is faced with three main challenges: tackle the employment situation in the context of high and lasting unemployment, improve the country's public finances which are faced with significant debt and a high level of social charges, and restore the competitiveness of exporting companies so as to curb the recurring loss of market shares. Faced with the scale and duration of the crisis, the opinion of the *Conseil d'analyse économique* (CAE, French Council of Economic Analysis) concerning public policy, based on assessments made in France and elsewhere, is that there is significant room for improvement in both effectiveness and equity. This Note is a compendium of some of the CAE's recommendations in key areas such as employment, housing, health, energy policy and modification of the regulations that apply to certain sectors. The majority of these have appeared in recent CAE publications since 2013, with some coming from earlier reports.

Structural reforms have a negative image in France –they tend to be perceived as having no positive short-term effect and even as an impediment to economic growth by reducing employment in those sectors affected by changes in regulations. However, not all reforms carry the same impact. Whereas the benefits from certain reforms are legitimately expected over the medium to long term, other measures are likely to have a rapid and positive impact both on employment and on household purchasing power. In addition, a proper evaluation of the impact of econo-

mic reforms needs to take into account their effects on all sectors and all players at the same time (households, companies and the public administration). For example, a lower product or service price in the reformed sectors means increased purchasing power for the average household, whose members can then reallocate this purchasing power towards other sectors of the economy.

The question of a turnaround in France's public finances cannot be overlooked. It is not merely a European commitment. It is first and foremost the requirement to equip the Nation with the necessary room for manoeuvre so as to be able to invest in growth, to be able to intervene effectively, to limit tax pressure so as not to discourage innovation and talent, whilst at the same time maintaining a high level of social protection and, finally, to help the most vulnerable sections of society face up to the structural changes underway. The essential requirement is to set public finances on a sustainable track, even if the short-term effects are not spectacular. The current reform of France's administrative organisation is exactly in line with this objective. The reforms proposed in this Note also move in this direction –they enable tackling various facets of public activity where there is scope for more effective action and their aim is primarily to liberate the capacity for job creation and areas of growth potential which the French economy so desperately needs.

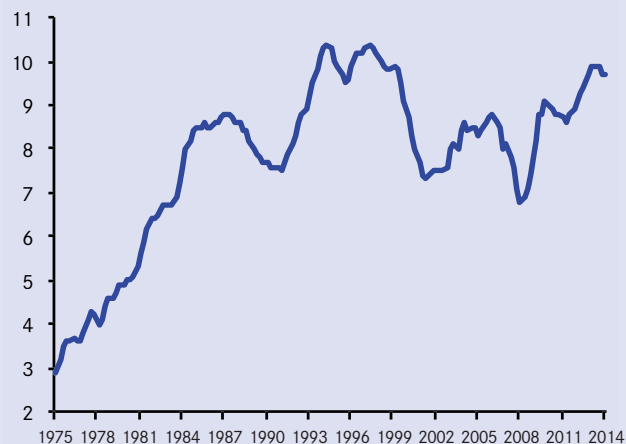
Employment policies and labour market functioning

France is confronted with a persistently high level of unemployment – it stood at 9.7% in metropolitan France in the first quarter of 2014, with no real prospects of an improvement during the year. In the past twenty years, unemployment has fluctuated in line with the economic situation, but with the level hovering between 7% and 10.5% there is clearly a strong element of structural unemployment when compared with the thirty year post-war period (see chart 1). Certain categories are particularly affected – in the age range 15 to 24 the unemployment level stood at 22.9% at the beginning of 2014. Over the past twenty years the rate for this category has never fallen below 15%. Even though, overall, the unemployment rate in France is a little less than the average in the euro zone (itself affected by the situations in Greece and Spain), it is nonetheless high compared with the other OECD countries. This is despite the high level of active and passive expenditure to support employment in France. In 2011, direct expenditure represented 2.3% of GDP (compared with 1.4% of GDP on average in the OECD countries), to which were added close to 2 points of GDP for general expenditure favouring job creation (a general lowering of social contributions for low wage-earners, tax-exemption for overtime hours, etc.)¹. The disappointing results obtained by the employment policies adopted in France argue in favour of tackling the structural problems that continue to weigh heavily on the labour market. The CAE's work in this area has concentrated on three key questions: the employment contract, the cost of employing low-paid workers and the means of leading unskilled youngsters into the job market.

Correcting the malfunctioning parts of the labour market

Despite the reforms in the job market undertaken since 2007, the very marked difference between the highly-protected permanent employment contract, (CDI, for *contrat à durée indéterminée*), and the short-term employment contract (CDD, for *contrat à durée déterminée*), which is very insecure and which covers the overwhelming majority of job flows, continues to inhibit the smooth running of the labour market. The CDD system creates a duality in the job market, between those who have been hired with a permanent contract and who are thus less inclined to move, and the others who are only ever

1. Unemployment rate in metropolitan France, in %



Note: Provisional data for 2014.

Source: INSEE (The French Statistical Institute).

offered a CDD, given that companies use them to get round the rigidity implicit in the CDI. This system is the source of notable inequalities: it hinders a good match being found between employees and jobs and, for those people on a CDD, discourages employers from investing in their human capital. This segmentation hampers the young unskilled population far more than any other category of employee. The mechanisms in the 2013 National Inter-professional Agreement point in the right direction. Among other aspects, there was a reduction in the legal insecurity engendered by collective lay-offs, and an attempt to discourage very short CDDs by imposing a surcharge on social contributions, but overall they were too timid to have a deep long-lasting effect. The CAE's Note no 4 recommends that the termination of CDI contracts for economic reasons be consolidated, with judges no longer required to determine whether the business reason is well-founded or not in relation with the company's performance.² To prevent excessive contract breaking and to incite employers to act responsibly, employer contributions would be adjusted on the basis of the volume of jobs destroyed – in effect linking them to the cost that the company imposes on the unemployment insurance scheme, irrespective of the type of contract involved.³

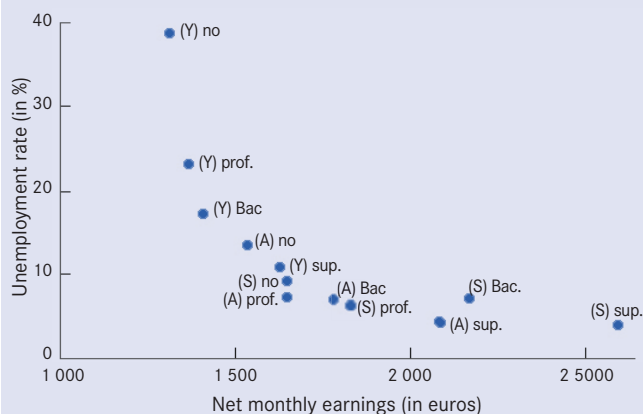
This collective Note has been collated and edited by H el ene Paris, General Secretary of the CAE, who is to be warmly congratulated for her sense of synthesis.

¹ Cf. DARES (2014): "Les d epenses en faveur de l'emploi et du march e du travail en 2011", *DARES Analyses*, February.

² Cahuc P., S. Carcillo and K. Zimmermann (2013): "L'emploi des jeunes peu qualifi es en France", *Note du CAE*, no 4, April.

³ See also Blanchard O. and J. Tirole (2003): *Protection de l'emploi et proc edures de licenciement*, *Rapport du CAE*, no 44, La Documentation fran aise, which recommends a tax on lay-offs to 'internalise' the social costs linked to job losses, in exchange for judges interfering less in redundancy procedures. In the same spirit, Artus P., A. B enassy-Qu er e, L. Boone, J. Cailloux, J. Delpla, E. Farhi, P-O. Gourinchas, J. Tirole and G. Wolff (2003): "Compl eter l'euro", *Note du CAE*, no 3, April, propose that the European Union adopts a genuine labour market policy, coupled to a Europe-wide unemployment insurance scheme. Practical implementation of this system would entail the creation of a European permanent employment contract, armed with flexible lay-off criteria, and subject to a lay-off tax (bonus/malus) in order for companies to internalise the social cost of their decisions. Such a contract would automatically grant the right to receive European unemployment benefits. Employers would be legally obliged to offer the employee the choice between a national employment contract and the European one. Thus, having a European employment contract would be the result of a personal choice by the employee. Funding the European unemployment benefits by Member States would be calculated so as to avoid any permanent transfer.

2. Average monthly earnings and unemployment rate by age range and education level average 2010-2012



Interpretation: (Y) = young people: 15-29 year-olds; (A) = adults: 30-54 year-olds; (S) = seniors: 55-65 year-olds. Educational level: no = neither qualification nor school-leaving certificate; prof. = CAP or BEP (Professional Aptitude Certificate or Professional Training Diploma; Bac = Baccalauréat (school-leaving certificate); sup. = 2 or more years of higher education).

The unemployment rate among unqualified youngsters was 39% in 2010-2012; those in work earned an average of 1,311 euros net per month for full-time employment.

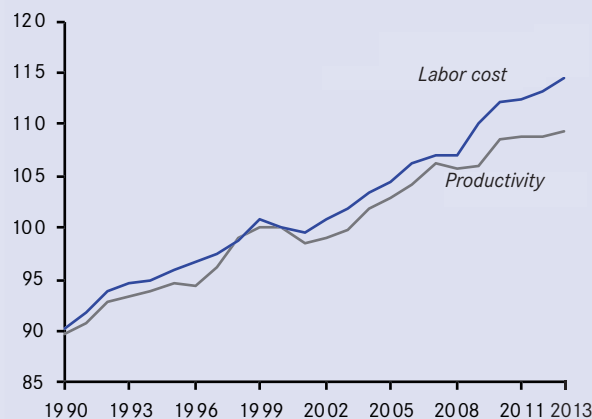
Source: Employment Survey, INSEE (The French Statistical Institute).

Making employment costs rise in relation to productivity gains

Employment costs for people on the lower end of the wage scale create difficulties for young and unskilled people to obtain jobs. Chart 2 shows that the unemployment rate for people capable of commanding a net monthly salary greater than 1,650 euros is only 5.8%. On the other hand, the average earnings for youngsters with no qualifications but in work are very close to the level of the minimum wage, whereas 38% of such unskilled youngsters are jobless. *The CAE's Note no 4* highlights the importance of closely managing the employment cost at the level of the minimum wage in order to reduce the unemployment level among the most disadvantaged sections of the population. The authors of this *Note* thus recommend specifically targeting reductions in social security contributions on the low wage sector, as any such reductions involving higher salaries tend to result in salary increases with scant effect on the level of employment.

The *CAE's Note no 5* highlights the uncoupling, since 2006, of labour productivity from labour cost (see chart 3).⁴ This phenomenon does not come from a large increase in the minimum wage (which has not been boosted by any special increase), nor from an increase in social contributions (at

3. Apparent productivity and real labour cost in the private sector, index base 100 in 2000



Scope: Financial and non-financial companies.

Interpretation: Apparent productivity is measured as the added value per full-time equivalent employee and the fully-loaded salaries per full-time equivalent. The deflator used is the consumer price index.

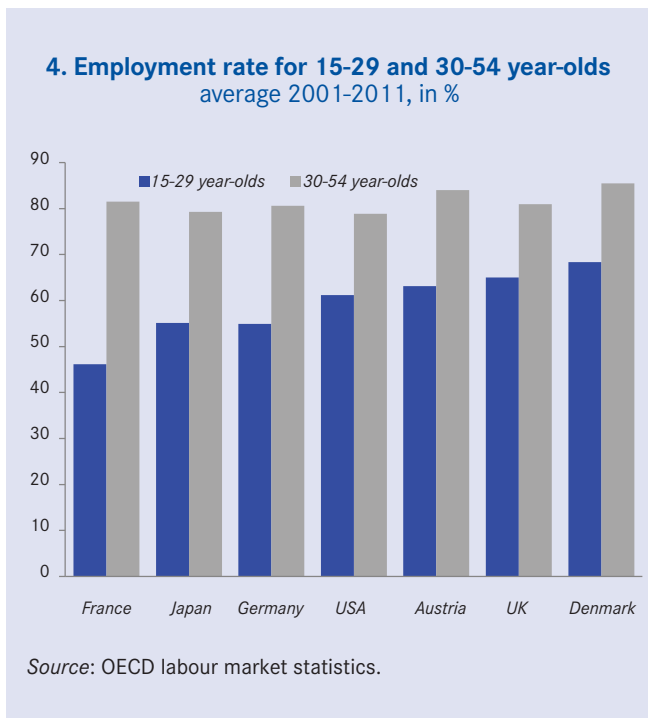
Source: National accounts base year 2010, INSEE.

least until 2011), but is mainly caused by the natural dynamics of take-home pay – a surprising effect in a period of a significant increase in unemployment. Although labour costs can be seen to be an obstacle for the young in entering the job market (*see above*), for the higher salaries the challenge is more the international competitiveness of French companies. The authors of the *Note* recommend much greater recourse to the special relief clauses in the branch collective agreements. This is based on the observation that such collective agreements played a role in maintaining this momentum since the beginning of the crisis. These exemption clauses would apply to companies in difficulty subject, for example, to any specific company agreement; they could also cover new companies during the first few years of their existence. The authors also recommend basing social security financing much more closely on a tax base by integrating social deductions in the tax schedules. In this way there would be a better shared perception of the levels of remuneration between employers and employees.

Improving training and assistance for young unskilled people to enter the job market

France has a specific problem when it comes to youth unemployment, with the rate of employment for the 15-29 year-olds being noticeably lower than that found in other OECD countries (see chart 4). This is explained by a lower level of paid employment by those still completing their education, and a very high level of youths who are simply unoccupied. To help these young people get started with their working life, training and accompaniment need to be improved.

⁴ Askenazy P., A. Bozio and C. García-Peñalosa (2013): "Dynamique des salaires par temps de crise", *Note du CAE*, no 5, April.



Although the system of alternating formal education and genuine remunerated employment increases the chance of someone finding a job at the end of formal education, it is not yet fully developed and still difficult for young French people with no other qualifications to enter. The authors of the *CAE's Note* no 4 recommend that public funding be more focused on the young with no qualifications by subsidising this dual system in the market sector and by financing full-time training in so-called second chance programmes. The authors of this *Note* insist that state-financed employment contracts in the non-market sector are not an effective insertion mechanism for these young people. In addition, they recommend a targeted strengthening of the means made available to employment offices, particularly for the least skilled youngsters, focusing on local missions and external service providers, with a real oversight being maintained on performance. To ensure that these youngsters are guided towards training and employment support measures, the authors propose to implement a specific allowance, a '*Revenu de solidarité active-jeune*' ('Active Solidarity Income-youth') or '*RSA-jeune*', which would be subject to very strict conditions concerning enrolment and course attendance, backed up by an intensive monitoring process. This *RSA-jeune* would be differentiated from the one introduced in 2010 which had such strict conditions attached (it demanded two years of full-time work in the three years preceding the request for the allowance) that it found very few takers⁵ and which offers no specific oversight for helping to

secure long-lasting employment. The current experimental youth 'guarantee' is a move in the right direction, but its success will depend on setting up a tight monitoring system, with specialised advisers and the possibility of being steered towards a dual system of education and training.

Stimulating competition in the markets for goods and services

Solving the unemployment problem in France is not just a question of reforming the labour market. A key challenge for employment lies in freeing up the purchasing power and potential pool of job opportunities by targeted reforms in certain goods and services sectors. Despite considerable efforts in recent years, there is still room for improvement for France in the regulation of the market for goods and services (see chart 5). France performs better than Germany in the areas of retailing or professional services but lags behind in the openness of the network sectors. In all areas, continental Europe has far more regulation than exists in the United Kingdom.

The idea here is not to remove the regulatory requirements that concern professional qualifications or the limiting of public risks. However, excessive barriers to entry and anti-competitive regulations have a negative impact on growth –such rules protect current technologies and production methods, generate rents and stifle innovation. It is therefore absolutely essential to severely curtail the number of regulations in force. France has made progress in this area, yet a lot remains to be done relative to our partners. The CAE Reports nos 72 and 100 insist on the necessity of correcting two types of rigidity.⁶

Releasing the pent-up employment opportunities in certain professions

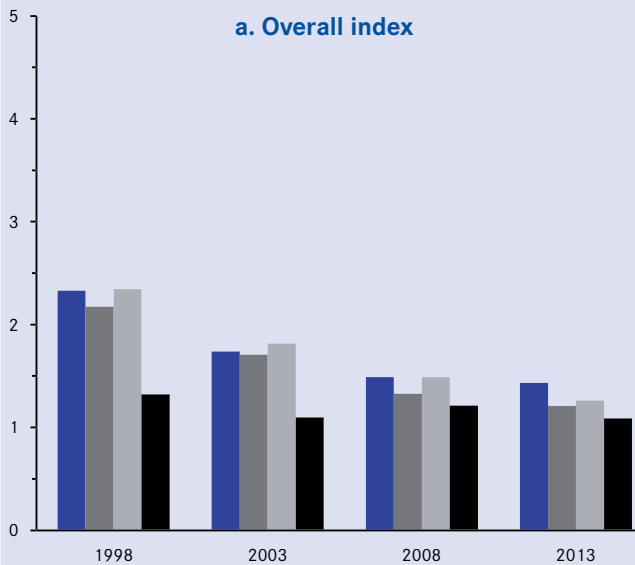
The authors of these two reports recommend loosening the barriers to entry into certain regulated professions (taxis, notaries, accountants, craftsmen, etc) or even removing them altogether, without in any way dispensing with the requirements for appropriate qualifications. Although specific consideration should be given to certain medical professions, the general principle is to facilitate the entry into certain professions and to create competition whilst, at the same time, better responding to the demands of users and consumers. The terms of opening up each profession need to be handled profession by profession, without unnecessary harm being done to those in place and without unreasonable cost to the taxpayer (see Box).

⁵ Some 8,000 households were receiving minimum income (RSA) benefit at the end of 2013, the allowance being granted at the household level based on the combined income of all those comprising the household. However, the majority of young people receiving the benefit (85% of the total households involved) were living alone; See *Caisse nationale d'allocations familiales* (CNAF, National Family Allowance Offices).

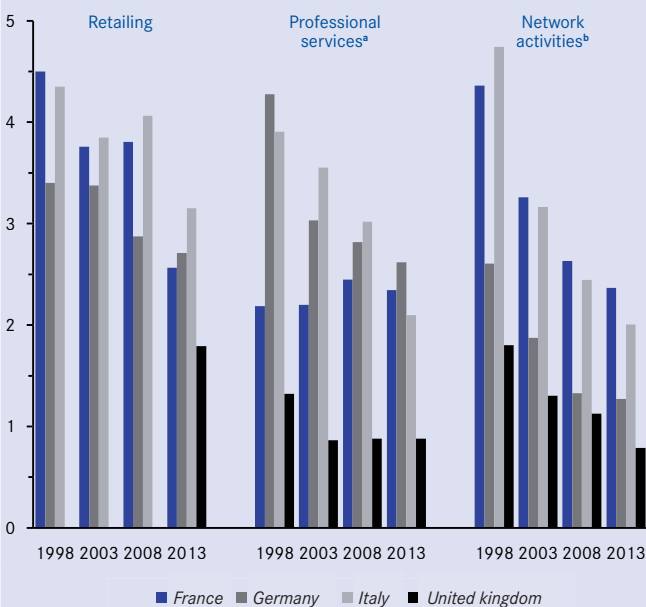
⁶ Cf. Aghion P., G. Cette, É. Cohen and M. Lemoine (2011): *Crise et croissance: une stratégie pour la France*, Rapport du CAE, no 100, La Documentation française and Aghion P., G. Cette, É. Cohen and J. Pisani-Ferry (2007): *Les leviers de la croissance française*, Rapport du CAE, no 72, La Documentation française.

5. Regulation index for the goods and services market

a. Overall index



b. Retailing, professional services and networked activities



Notes: ^a Accounting, legal, architectural and engineering services, and services provided to companies; ^b Energy, transport, communications.

Source: OECD.

Increasing competition in the non-manufacturing sectors

Softening the rigidity of the goods and services sectors is a means of increasing consumers' purchasing power and of achieving productivity gains. Judging by the detailed OECD indicators, France still has a greater set of restrictive regulations in place than many other OECD countries notably in the network

Regulated professions^a

A regulated profession is an administrative category encompassing occupations subject to specific rules and certain legal and regulatory protections which come in addition to those in place for the general category of occupations. Such professions are subject to, or benefit from, one or more of the following: a legal monopoly, entry barriers (required qualifications, *numerus clausus*, mandatory contributions on assets), and regulated pricing grids. They are to be found in a wide variety of sectors –law, medicine, crafts trade, architecture, urban planning. A number of these professions operate exclusively within a monopoly, others have in addition a certain level of competition, whilst others still operate within a normal competitive framework.

Leaving aside the medical profession, there are two broad categories, distinguished by the respective economic issues they warrant:

- craft trades: taxi-drivers, hairdressers, driving instructors for example are professions where barriers to entry prevent the creation of additional employment possibilities. The first reason is training, with qualification conditions (*CAP* and *Brevet*) which are at times unsuitable, be it because of a shortage in training supply or because of inappropriateness relative to exercising the profession (hairdressing). A second reason is the *numerus clausus*. The example of taxis is frequently in the news. Faced with competition from a new breed of taxis –minicabs hired through the Internet– official taxi drivers called upon the public authorities for protection. Blocking the attribution of taxi licences and forbidding “electronic cruising” by minicabs, i.e. the geo-localisation of the nearest vehicle, as the Thévenoud Report^b is proposing will not help promote employment in a sector where there appears to be a shortage of supply. As for driving schools, the lack of transparency in prices charged, and the limited number of places for instructors to obtain their licence, hold the sector back and this translates, in practice, into increased difficulty in obtaining a driving licence;
- the legal and auditing professions: in this sector, professions such as notaries, solicitors, bailiffs, accountants, court registrars, etc. benefit from monopolies and protected incomes, frequently opposed to ‘open professions’ such as lawyers, the legal community’s reference profession which is more innovative and competitive. Although several restrictions have been lifted by the rulings authorised by the law of 2nd January 2014 (especially the ability to have salaried notaries), the core problems still remain, with licensing schemes, service provision arrangements and access to certain professions all needing to be reviewed.

^a Cf. Jamet J-F. and X. Piccino (2009): “Peut-on réformer vraiment les professions réglementées ? Le rôle déterminant de l’Europe”, *Annales des Mines*.

^b Thévenoud T. (2014): *Un taxi pour l’avenir, des emplois pour la France*, Mission de Concertation Taxis/VTC, Avril.

industries (transport and energy in particular)⁷ and in retailing, two sectors in which productivity in France is poor compared with other sectors of the economy.

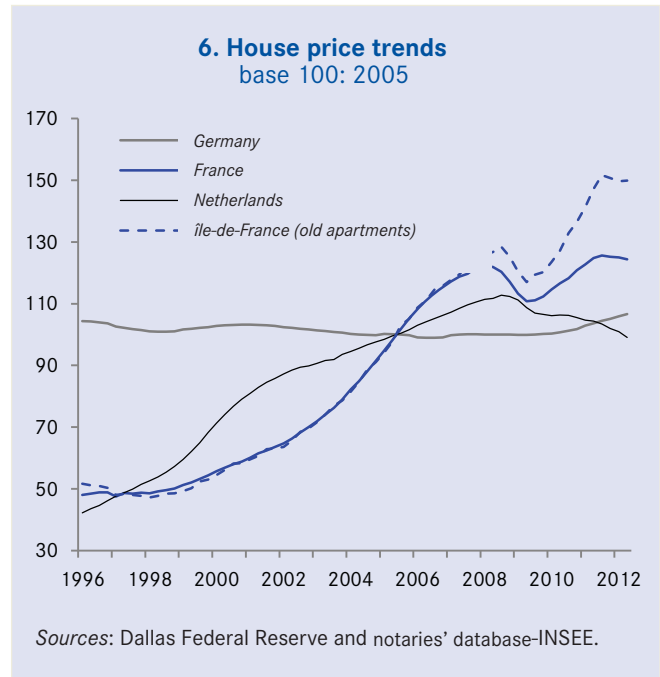
In the retail sector, for example, the CAE authors recommend reforming the rules for siting supermarkets and *hard discounters* but also for those trades where entry is regulated (hotels, etc.) by putting them out to tender for tenures that are long-term yet not permanent with decisions being based on competitive considerations. Although certain advances have been enabled by the 2008 law on modernising the economy, market structures are still heavily influenced by commercial town planning rules and restrictions placed between retailers and suppliers. For example, a special authorisation is still required to open a shop with a footprint exceeding 1,000 m². There is no longer any reason to forbid sales at a loss since, for companies in a dominant position, competition law already outlaws the practice. In reality, this prohibition deprives consumers of potential benefits and restrains competition by preventing retailers, especially those just getting started, from using their own pricing policy for establishing their place in the market. The arrival of new players and genuine competition among retailers would enable a lowering of prices for the consumer, but could also create jobs and increase production, as has been demonstrated by the development of supermarkets in a number of countries. The authors also recommend allowing all non-prescription drugs and medicines to be sold elsewhere than in pharmacies, and keeping the current restrictions only for those products with a public health justification.

Rationalising housing policies and making them more effective

The rise in house prices that France has witnessed since 2000 (see chart 6) has been a powerful factor in increasing inequalities. It has also brought in its wake certain economic inefficiencies such as increasing commuting distances, a lower degree of worker mobility, investment in likely over-valued property or even a loss of competitiveness when the price of housing translates into increased salaries or an increase in the cost of commercial property. Still, the public financing to help the housing sector has been really significant –around 45 billion euros per year if one adds up support to house-buyers and to developers.

Stimulating supply and facilitating market flows

The CAE's Note no 2 proposes to combine measures to stimulate supply, offset demand-side market distortions and facilitate market flows.⁸ To stimulate supply, the proposal is to improve land/real estate management by systematically



transferring the responsibility to the level of the so-called inter-communalities and by introducing a specific exemption mechanism in the immediate Parisian suburbs. To reduce construction costs, the proposal is mainly to start removing some of the least important rules and standards concerning urban planning (simplification of the rules governing insulation, anti-earthquake standards, etc.).⁹ To grease the wheels of the market and to make property tax more equitable, the authors' proposals are to progressively abolish transfer taxes and to reform the property tax system on buildings, by basing the tax on the market value of the property less any associated outstanding loans. Such a reform would be budget neutral and would be complemented by a tax on latent capital gains on vacant land, which would encourage the sale of such land when planning permission is secured. These reforms presuppose that notaries will rapidly step up to their legal obligation to complete the land registry databases. In parallel, the authors recommend the gradual phasing-out of all state aid for home buyers, measures which are costly (more than 4 billion euros in 2012) and which tend to inflate prices with very limited results for first time home-owners.

Optimising rented accommodation policies

State subsidies for rented accommodation are huge, but they fluctuate frequently and are often inconsistent. In order to reduce geographic disparities concerning subsidised housing, the CAE's Note no 10 suggests opening up to competition the market for building and managing council accommodation and to allocate subsidies based on simple indicators

⁷ According to the OECD's summary indicators, France ranked 22nd out of 31 countries in 2013.

⁸ Trannoy A. and É. Wasmer (2013): "Comment modérer les prix de l'immobilier?", *Note du CAE*, no 2, February.

⁹ The law enacted on the 11th June 2014 is on the right track concerning the accessibility standards for disabled people. It updates the 2005 law and allows a staged implementation for such accessibility, removing the targeted cut-off of 2015, and simplifying certain standards to be met.

that measure the tension between demand for, and supply of, housing.¹⁰ The rules for attribution of council accommodation would be clarified by the use of a points system catering to each broad category of social housing objective. Moreover, mobility would be encouraged by using a mechanism of super-rents applied as a function of occupancy time and earnings level. Finally the *Note's* authors propose to ensure the consistency of housing subsidies with social redistribution as a whole by including them in the income tax schedule and in the minimum income mechanism. This reform would reduce the advantage of the beneficiaries of social housing relative to those renting privately who have suffered the most from recent price trends. It would also reduce the risk of private owners effectively pocketing the housing subsidies.

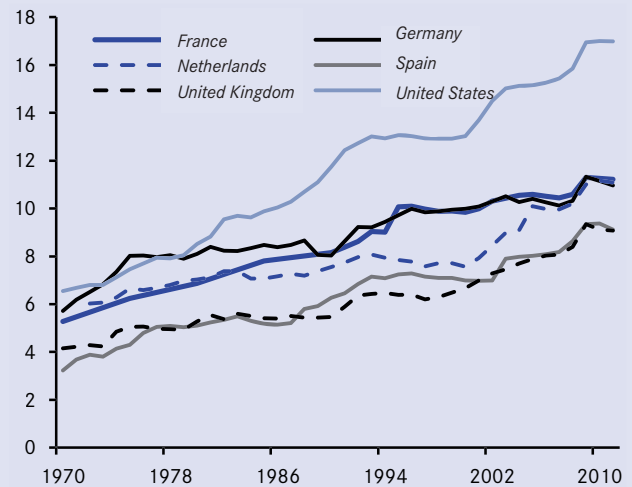
Improving both effectiveness and equity in the health system

France spends much more on health than many other developed countries (11.6% of GDP in 2011, versus 9.3% of GDP for the OECD average, see chart 7) and, for the public expenditure part, more than the European Union average (around 9% of GDP). The French system produces good results in strictly health terms, but with significant social inequity, a clear lack of coordination over the control of expenditure and structural financing issues. Several ideas for reform are proposed by the CAE to improve the overall effectiveness of the nation's health system.

Defining the scope of involvement with a "solidarity healthcare package"

The *CAE's Note* no 8 proposes breaking with the current system which consists of limiting the overall Social Security expenditure by both lowering reimbursement rates and increasing compulsory contributions. The idea is to define a "solidarity healthcare package" available to all irrespective of financial means and health condition.¹¹ This package would contain all medicines, drugs and acts –both preventive and curative– carried out in hospital and as outpatient care, which would be fully covered for clearly defined pathologies. Its scope would be systematically and openly updated based on a classification of treatments available according to their demonstrated effectiveness in relation to their costs. This implies setting up a sustainable system of medico-economic evaluation, and the political will to follow the recommendations thus produced. All treatments not contained in the basket would not be reimbursed –not even partially– by the social security system. In the very near term, the authors of the *Note* recommend to no longer reimburse medicines currently giving rise to a 15% refund rate, revise the current

7. Running costs for public health as % of GDP, 1970-2011



Source: OECD (2013).

list of reimbursable items and introducing a single reference tariff for the reimbursement of each molecule. Putting in place an effective, contract-based oversight mechanism for healthcare supply

With its mixed public/private system of health insurance, involving the national social security and complementary insurers, France is an exception among developed countries. Such an organisation engenders duplication in management costs (estimated respectively at 7 and 6 billion euros) and hampers effective cost control within the overall health system. The current regulations for the complementary insurers also encourage selecting the risks to be covered, a situation that produces inequities in both access to certain healthcare items and insurance coverage. For this reason, the *CAE's Note* no 12 recommends in the long term a complete rethink of the system by ending the dual system of health insurance and replacing it with a single unified system of healthcare coverage. This would be done either with a decentralised public system (using the Regional Health Authorities), or through regulated competition between the various health insurance providers.¹² In the short term, it would be necessary to at least improve the current system by creating a situation of genuine competition in the market for complementary insurance based on a standard contract, to abolish the social contribution exemptions in collective contracts, to respect the principle of a ceiling for patients' contribution and to have the complementary insurers involved in the conclusion of contractual arrangements with care providers.

¹⁰ Trannoy A. and É. Wasmer (2013): "La politique du logement locatif", *Note du CAE*, no 10, October.

¹¹ Askenazy P., B. Dormont, P-Y. Geoffard and V. Paris (2013): "Pour un système de santé plus efficace", *Note du CAE*, no 8, July.

¹² Dormont B., P-Y. Geoffard and J. Tirole (2014): "Refonder l'assurance-maladie", *Note du CAE*, no 12, April.

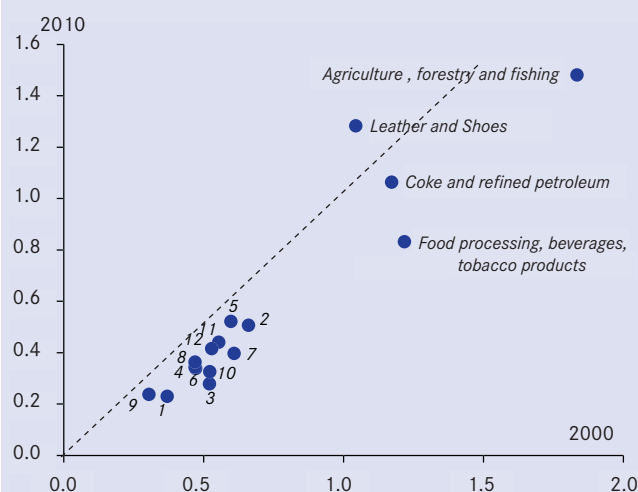
In the medium term, conditions need to be put in place to move towards comprehensive contractual relations with healthcare providers. The Regional Health Authorities (RHA), or the public health insurance offices in regulated competition, would be funded globally, based on the estimated requirements of the population under their care and with contributions proportional to income. They would have latitude in splitting their funding between hospitals, outpatient care and the medico-social services. They would also have the responsibility of determining the contracts and methods of payment for the totality of the medical profession in their area. Giving the RHAs or the health insurance offices the responsibility for overseeing health expenditure would be the most effective way of ensuring that the offer best meets the needs of the population concerned and will be a real incentive to an effective use of healthcare funds.

The impact of public policies on competitiveness: the example of energy policy

France's market shares in exports have dwindled over the past ten years and this is most clearly evident when compared with Germany's performance (see chart 8). With the exception of the leather and shoe sector, boosted by luxury brands, the comparison between Germany and France shows the latter's marked deterioration in the past few years. The CAE's *Note* no 6 broaches the question of competitiveness from the point of view of the cost of electricity, which is lower in France than in her main competitors.¹³ The *Note* shows that a 10% increase in the price of electricity in France would reduce the value of exports by about 2%. It is clear that the effect is significant, and will obviously be all the more so in those industries which are energy-intensive. Energy prices, because they are a short-term cost, are an important factor in competitiveness. But they are also a long-term signal. High energy prices, or the expectation of high prices, is a wake-up call to consider investing in new technology or new products.

The tension between these two requirements –the need to be competitive today whilst preparing to be competitive tomorrow– demands that all the players in the economy receive the right signals. It is for this reason that the *Note's* authors propose that a credible and gradual increase in energy prices be announced so as to enable the various economic actors to confidently amend their forecasts. The government's communications policy on electricity prices needs to be as clear as possible. The very specific situation in France –heavy labour taxation combined with low energy taxation (see chart 9)– leads the authors to recommend progressively increasing the taxation on energy in order to reduce labour costs. Given the significant short-term impact that electricity prices have on the country's industrial exporters, the *Note's* authors recommend

8. Global market shares for France compared with those for Germany by sector in 2000 and 2010



Interpretation: In 2000, France's global agricultural market share was almost twice that of Germany. Ten years later, it was only one and a half times that of Germany.

Legend: 1. Extractive industries; 2. Textile-clothing; 3. Timber and associated industries; 4. Paper, cardboard, printing and reproduction industries; 5. Chemicals, pharmaceuticals; 6. Rubber, plastics; 7. Other non-metallic mineral products; 8. Metallurgy, metallic products (excluding plant and machinery); 9. Plant and machinery (not included elsewhere); 10. Electrical and optical equipment; 11. Transport equipment; 12. Other manufacturing industries, recycling.

Source: Calculations based on BACI-CEPII.

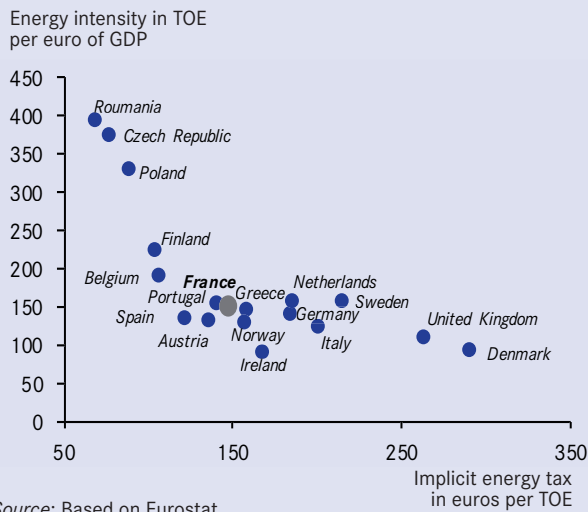
that considerable prudence be exercised in the rate of decommissioning the ageing nuclear power stations, the cost per kWh of which is particularly competitive. Given the particular sensitivity to electricity prices of the competitiveness of the energy-intensive industrial sector, they also suggests that public service costs (including financing the development of renewable energies) be charged differently depending on the industry's energy intensity. This selective charging may go beyond the existing ceilings, as is currently the case in Germany.

Energy policy is an example of a public policy with significant cost impact on exporting companies, and thus on their competitiveness. The other public policies analysed above (housing, labour costs, training, health and competition in the market for goods and services) may also have an impact on French competitiveness even when this is not their main focus. The CAE believes that the impact of new public policies on competitiveness should be systematically taken into account by the nation's decision-makers. The CAE's *Note* no 11 shows that a 1% reduction in French prices compared with trading partners outside the euro-zone, or a 1% depreciation of the euro, produce a similar rise in the country's manufactured exports.¹⁴ French competitiveness is thus decided as much in Paris as in Frankfurt.

¹³ Bureau D., L. Fontagné and P. Martin (2013): "Énergie et compétitivité", *Note du CAE*, no 6, May.

¹⁴ Bénassy-Quéré A. P-O. Gourinchas, P. Martin and G. Plantin (2014): "L'euro dans la 'guerre des monnaies'", *Note du CAE*, no 11, January. Lower prices will provide the additional advantage of improving France's competitiveness with respect to our Eurozone partners.

9. Energy taxation and energy intensity in Europe 2010



Overall consistency

Structural reforms have a negative image in France –they tend to be perceived as having no positive short-term effect and even as an impediment to economic growth by reducing employment in those sectors affected by changes in regulations. This view needs changing for several reasons. Not all reforms are the same

The reforms discussed earlier do not all have the same short-term effect. For example, it is reasonable to assume that abolishing the 15% reimbursement rate currently in place for a number of drugs or unifying the reimbursement rate according to the molecule would have a negative short-term impact on employment in the pharmaceutical sector. And a progressive reduction in the level of building subsidies would likely have a short-term negative impact in the construction sector. Thus, the benefits from certain reforms would be expected in the medium to long term, with little hope of any immediate results, and even with a short-term negative impact on employment and economic activity. But on the other hand, liberalising ground transport, simplifying construction norms or opening up certain regulated professions could well have a rapid and positive effect on employment and on households' purchasing power.

Assessing reforms in general equilibrium

To arrive at a correct assessment of the economic impact of structural reforms, one needs to think in terms of gene-

ral equilibrium, i.e. take into account the overall effect of such reforms on all sectors and on all players in the economy (households, companies, public administration).¹⁵ For example, lower prices in the reformed sectors means increased purchasing power for the average household, whose members can then reallocate this extra disposable income towards other sectors of the economy. It is worthwhile noting here that certain households spend up to 8% on complementary health insurance, and that housing costs take up some 18.5% of French peoples' income. Even small gains in these two areas (not to mention transport or food) can have a substantial effect on disposable income and thus on consumption. Moreover, gains in the public sector (for example, as a result of lower medication prices) can mean re-allocating the saved-up expense to others areas or reducing the level of mandatory levies.

Reforms and consolidating public finances

In 2013, even with historically low interest rates, the interest payments on the national debt amounted to 2.3% of GDP, i.e. roughly the same size as the revenues from corporation tax and far more than state expenditure on higher education and research. Improving France's public finances is not merely a European commitment. It is first and foremost the requirement to equip the Nation with the necessary room to manoeuvre so as to be able to invest in growth, to be able to intervene effectively, to limit tax pressure so as not to discourage innovation and talent, whilst at the same time maintaining a high level of social protection and, finally, to help the most vulnerable to face up to the structural changes underway. From a purely accounting point of view, reducing debt levels helps limit the exposure to an increase in interest rates. In terms of sovereignty, such discipline will prevent the nation being suddenly forced, in case of a reversal of market sentiment, to sell off public assets to which the country may be particularly attached or at less than market values. Finally, from the point of view of macroeconomic management, a gradual return to financial equilibrium will provide the nation with the renewed ability to intervene to support the economy if, and when, there is a cyclical slow-down.

In a period where it is difficult to kick-start activity, the key emphasis needs to be on the structural measures required to consolidate public finances. The main objective is to put them onto a sustainable trajectory, even though such a turnaround is hardly spectacular in the short term. The reform of the nation's administrative structure is perfectly in line with this objective. The possible avenues for reform outlined above also move in this direction, especially those affecting housing and health.¹⁶

¹⁵ Members of the CAE (2013): "Évaluation des politiques publiques", *Note du CAE*, no 1, February.

¹⁶ The topic of pensions, which constitute a sizeable proportion of public expenditure (close to 14% of GDP), is deliberately not handled in this Note, as it come under the aegis of the *Conseil d'orientation des retraites* (COR, Pensions Guidance Council).

Taking account of future expectations

There is an abundant literature which has tried to assess the effect of reducing public expenditure on economic activity and on the level of employment. Some authors stress the importance of market expectations in the process. A reduction in expenditure felt to be long-lasting could have a lesser negative effect on short-term activity because it would improve long-term expectations concerning economic growth and the sustainability of public finances. In the same vein, the signal given by structural reforms is likely to attenuate the negative Keynesian effect of a short-term budget contraction because it improves the income perspectives in the medium and long terms.

Accompanying structural reforms with renewed industrial policies

The structural measures recommended above aim to improve the effectiveness of the nation's productive and social protection systems. But the next challenge is to go even further and boost the growth potential by targeted public support for research and innovation. Without rejecting this idea out of hand, the *CAE's Note* no 13 recommends that public decision makers focus on high added-value activities rather than traditional industry, the boundaries of which are difficult to define today.¹⁷ In addition to creating an environment favourable to innovation and employment, the aim ought to be to support business restructuring and technological development by giving priority to the mobility of factors of production (capital, labour, know-how and experience) and correcting market failures, for example in the area of research. Public support and intervention will need to be accompanied by powerful watchdogs capable, in particular, of cutting short unsuccessful projects.

¹⁷ Fontagné L., P. Mohnen and G. Wolff (2014): "Pas d'industrie, pas d'avenir ?", *Note du CAE*, no 13, June.

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