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Bundesverband der
Deutschen Industrie e.V.

COUNTRY REPORT FRANCE

Competitiveness and social partnership

President Hollande's broad reform agenda

July 2015

- **France's economic situation is gradually improving.** So far, however, the pace of recovery has been slow. We expect growth of about one percent in 2015 and further strengthening in 2016.

- **Since early 2014 the government has provided a clearer direction on reforms.** It has increasingly geared many areas of economic policymaking towards growth and competitiveness. For over a decade, French companies in a number of industries have lost their competitiveness. The programme of reforms is wide-ranging; it will likely take time before positive results are seen.

- **Greater cooperation with social partners is key.** It is a prerequisite for creating a consensus for reforms in broader society. Wage policy changes are also necessary.

- **French fiscal policy still faces major challenges.** Thanks to a new extension, France is currently complying with EU set of rules. Going forward, the country needs to maintain a stable tax policy, conduct a review of state spending and carefully plan budgetary expenditures. If it fails to put growth factors on a sustainable footing, the consolidation policy will be difficult to manage.

- **The close economic relations of France and Germany are becoming more and more intertwined.** The countries are at the centre of European value creation chains. The reason for this goes beyond the countries' geographical proximity and the size of their economies.

Contents

The political situation in France

The Parti socialiste provides president and government

In May 2012, François Hollande was elected French president in a run-off vote against his predecessor Nicolas Sarkozy. The *Parti socialiste* (PS) also went on to win the majority in the elections to the *Assemblée nationale* in June 2012. Following his election as president, Hollande appointed Jean-Marc Ayrault as prime minister, who held office with a provisional government until the June 2012 elections. Ayrault was reappointed prime minister by Hollande after the elections, and his cabinet remained largely unchanged.

By contrast, the PS suffered a big blow in the March 2014 municipal elections, losing over 150 town halls – mostly to the conservative *Union pour un mouvement populaire* (UMP). The far-right Front national turned in a strong performance, gaining around 1.200 municipal council seats nationwide. Ayrault took part of the blame for the election results and subsequently resigned as prime minister. His successor was Manuel Valls, a representative of the social-democratic and reformist wing of the PS. With a cabinet reshuffle in August 2014, Valls was able to more firmly establish his reform agenda within the government. This strategy was particularly evident in his choice of Economics Minister: Arnaud Montebourg, a member of the left wing of the PS, was replaced by Emmanuel Macron, an advocator of pragmatic economic reforms.

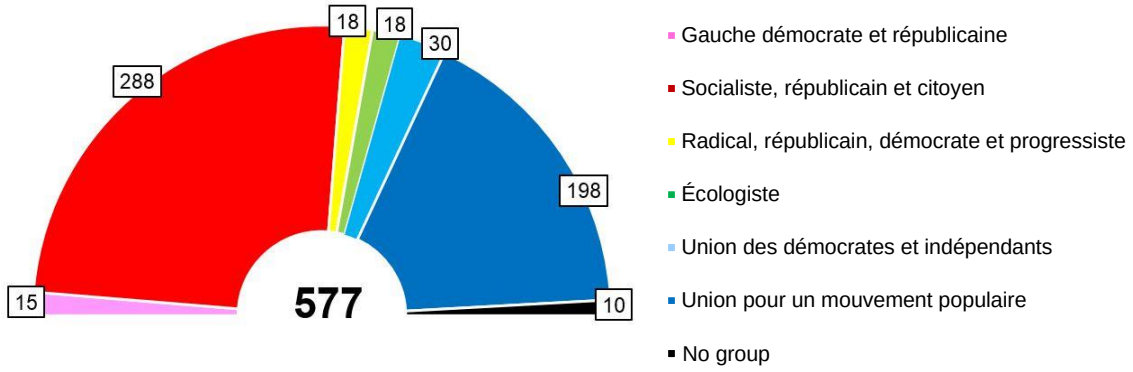
Distribution of seats in the Assemblée nationale (as of May 2015)

Parliamentary group	Most important party	Members	Apparentés	Total
Socialiste, républicain et citoyen	Parti socialiste	274	14	288
Union pour un mouvement populaire	Union pour un mouvement populaire	190	8	198
Union des démocrates et indépendants	Nouveau centre	30	0	30
Radical, républicain, démocrate et progressiste	Parti radical de gauche	18	0	18
Écologiste	Europe écologie les verts	17	1	18
Gauche démocrate et républicaine	Front de gauche	15	0	15
No group	-	10	-	10

Source: Assemblée nationale

The *Assemblée nationale* comprises a total of 577 elected *députés* organised into parliamentary groups, usually made up of representatives from a variety of parties sharing a similar political stance. A parliamentary group must include at least 15 members. *Députés* who are not official members of a parliamentary group but who are affiliated with this group are known as *apparentés*. These *apparentés* are included in the allocation of committee seats within a parliamentary group.

Distribution of seats in the Assemblée nationale (as of May 2015)



Source: Assemblée nationale

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In parliament, the PS is dependent on a coalition with the social-liberal *Parti radical de gauche* (organised in the parliamentary group *Radical, républicain, démocrate et progressiste*), with whom it holds a narrow majority just over the required 289 seats. The Greens left the coalition following the cabinet reshuffle in August 2014. With 198 seats, the main opposition party is the UMP, which, following an internal change of leadership in November 2014, is now again headed by former president Sarkozy. After Sarkozy narrowly lost to Hollande in the 2012 presidential elections, the UMP suffered a 12.4 percent drop in votes in the subsequent parliamentary elections, thereby losing a whopping 119 seats compared with the previous term. Following a temporary withdrawal from politics after his 2012 defeat, Sarkozy has recently announced that he intends to run for president again in 2017. On Sarkozy's initiative, the UMP was renamed *Les Républicains* in late May 2015.

The government is focusing its efforts on the economy

Despite the majority in the *Assemblée nationale* – and at times also in the Senate – granting Hollande the freedom to govern as he sees fit, the government's priorities over the last few years have not always been clear. With regard to economic and fiscal policy, it implemented a number of complex – and to some extent contradictory – measures. However, by appointing Valls as prime minister and with the cabinet reshuffle of August 2014, President Hollande has committed himself more firmly to a reform agenda. Increasingly, it is France's negative economic development that is of concern to Hollande's government. As far back as when he took office in 2012, Hollande pledged to kick-start a trend reversal in the labour market. Yet unemployment has since risen by more 500.000 people, reaching a record high of over 3.5 million out of work by mid-2015.

Hollande has made his own political future dependent on improving the economy during his remaining time in office. In February 2015 he confirmed that he will run for a second term in the 2017 elections only if unemployment levels have dropped by then. Since assuming the presidency, Hollande has seen his popularity plummet among the French people. By November 2013, various polls showed that he was the most unpopular president of the Fifth Republic. The popularity that Hollande and Valls gained in January 2015 following the attacks on the

French satirical newspaper *Charlie Hebdo* was short-lived; more recent opinion polls conducted found that the country's population once again felt just as dissatisfied with their president.

The rise of the Front national

Having only won two seats in the last *Assemblée nationale* elections, the *Front national* currently plays no real role on the national stage. This is in part due to the French electoral system: the plurality voting system in single-member constituencies means that *Front national* candidates often lose to candidates from the more established parties. Yet in the elections to the European Parliament in May 2014, where a proportional representation system was used, the *Front national* celebrated a landslide victory, winning 24 of France's 74 allocated seats – compared to just three in 2009 – to make it France's largest represented party on the European level.

Marine Le Pen, daughter of Front national founder Jean-Marie Le Pen and party president since 2011, has managed to gain wide acceptance in French society for the party's right-wing populist and Eurosceptic beliefs, successfully turning her father's anti-Semitic xenophobia into a tough stance on Islamic extremism and immigration.

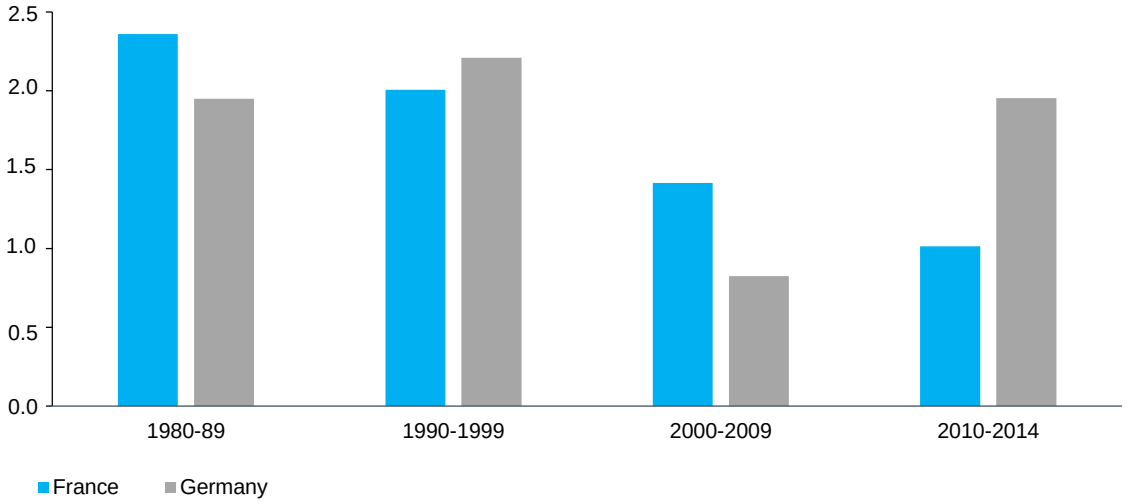
The next barometer of the public mood will be the regional elections in December 2015. These are held using a proportional representation system, thereby allowing the *Front national* to fare better than in the national elections. Furthermore, as things stand presently, Le Pen can expect to potentially make it through to the second round of voting in the 2017 presidential elections, but will in all likelihood stand no chance in the subsequent run-off vote.

Economic situation

In the three decades from 1980 to 2009 the French economy grew an average of 2 percent, though the rate of growth overall has tended downwards during these years. The upturn was particularly pronounced in the late 1980s with growth reaching 4.7 percent in 1988 and 4.4 percent in 1989. At the turn of the millennium, the French economy recorded another strong phase, growing an average of 3.6 percent from 1998 to 2000. Since 1980, there have only been two years of recession during the period under review. In 1993, the economy declined due to rising oil prices triggered by the Gulf wars, the impact of German reunification and tensions in the European Monetary System. In 2009, economic output dropped by 2.9 percent as a result of the European economic and financial crisis.

During the past decade, the French economy expanded faster than Germany's, achieving an average growth rate of 1.4 percent compared to Germany's mere 0.8 percent. This stands in contrast to growth since 2010: in the past five years, the German economy has grown at an average rate of 2.0 percent per year while France has only managed to achieve growth of 1.0 percent.

Real GDP growth of Germany and France in percent



Sources: Eurostat, Federal Statistical Office

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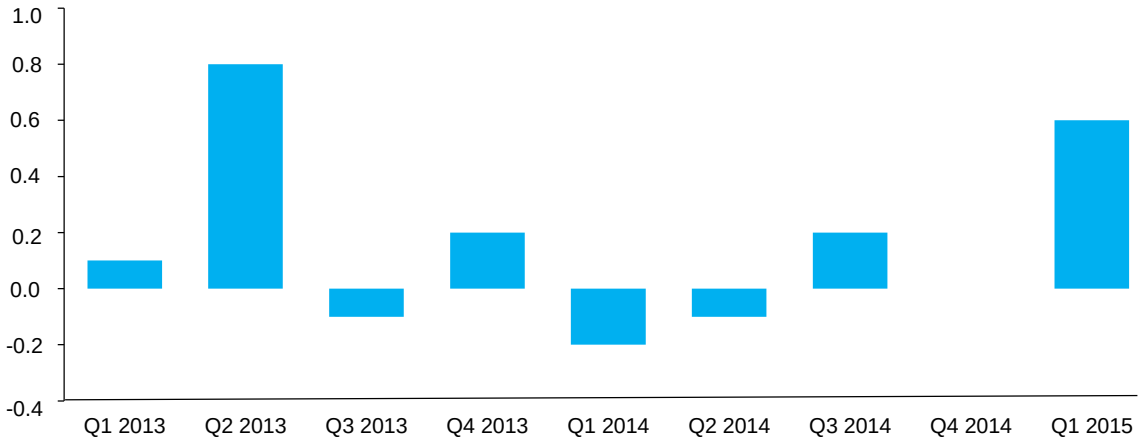
French real GDP growth quarter-on-quarter in percent



Source: Eurostat

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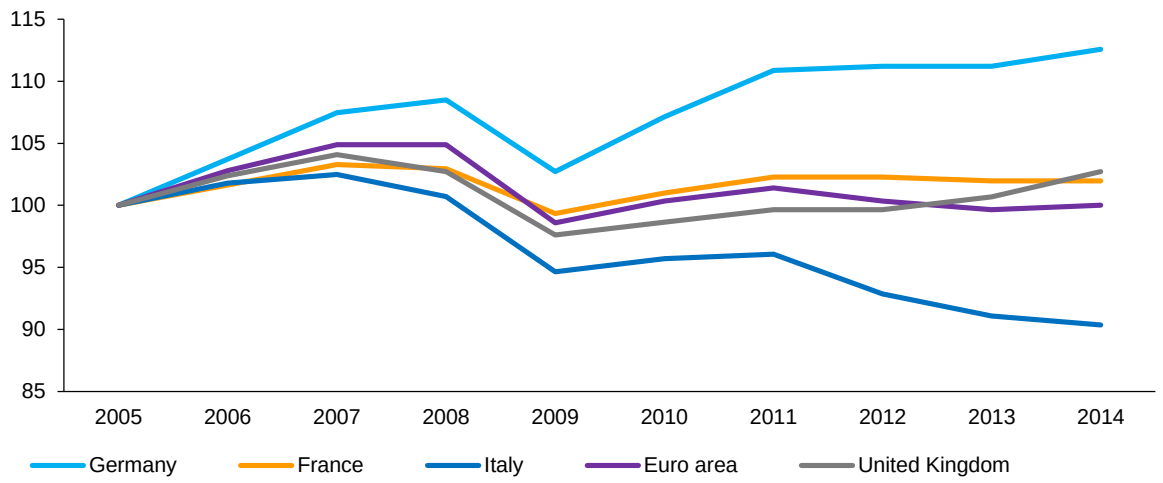
Per capita income still below 2007 levels

In 2005, per capita income in France was 30.500 euros, growing steadily to 31.500 euros in 2007. It has remained below this level since. Over the past ten years, the lowest per capita income was recorded in 2009 at 30.300 euros, levelling out at 31.100 euros in 2013 and 2014. In Germany, per capita income increased with substantially more momentum between 2005 and 2014, rising from 29.400 euros to 33.100 euros. Compared with per capita income in the UK, France is still 1.000 euros higher in absolute terms, but the UK has been catching up fast since 2012.

Real GDP per capita since 2005*



* 2005=100

Source: Eurostat

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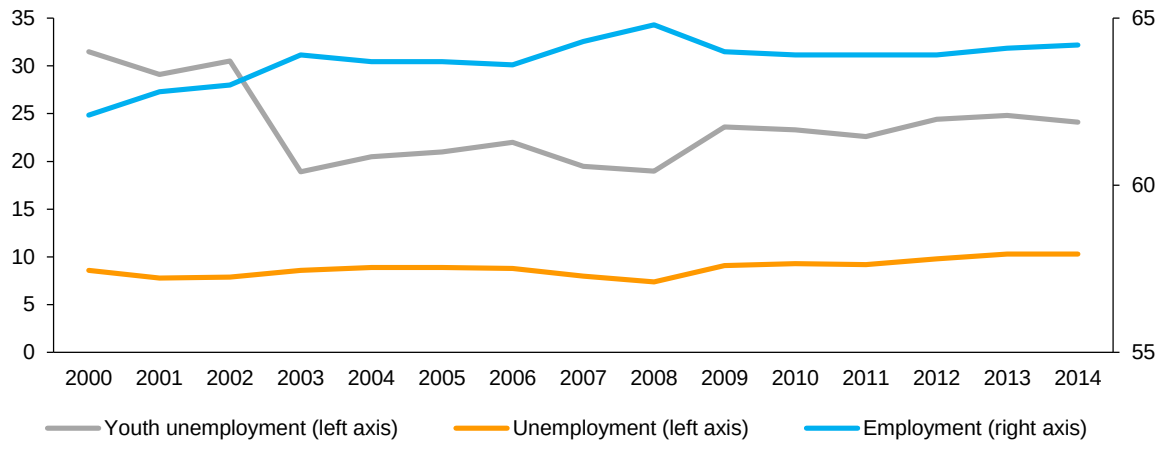
Difficult situation on the labour market

Unemployment has been on the rise since 2011, and has stayed above the 10 percent mark since 2013. With the recovery stalling in the last few years, the rate of long-term unemployed among the unemployed rose to over 43 percent by the end of 2014, which is set to have a negative medium to long-term impact on the employment prospects of the working-age population. Young and low-skilled employees from a migrant background are hit hardest by unemployment, while the low level of employment among older employees points to a structural problem (European Commission 2015a). France's labour market is fragmented and the transition rate from temporary to permanent employment is low. In 2012, this rate was at 20.9 percent, which is under the EU average of 23.9 percent. Temporary employment is particularly high among young and female employees with low qualifications.

From 2008 to 2013, the labour force aged between 20 and 64 increased by 600.000 employees. A large proportion of this growth came from employees aged 50 or over. The rate of employment among this group of employees has risen steadily over the past few years. This development is partially due to a reform in pensions in 2010 that increased the minimum and maximum age of retirement. Nonetheless, the fact remains that the employment rate for employees aged between 60 and 64 is still ten percentage points below the EU average.

Labour market performance since 2000*



* as percent of the civilian labour force

Source: Eurostat

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Economic trend: gradual recovery spurred by consumer spending

After growing a meagre 0.3 percent in both 2012 and 2013, the French economy only managed a marginally better performance of 0.4 percent in 2014. With the business climate improving slightly, the momentum of the European Central Bank's monetary policy, the substantial reduction of the external value of the euro and falling energy prices, there are many signs pointing to a slight recovery for 2015 (European Commission 2015b, European Commission 2015c).

The main factor supporting this recovery is private consumption, the traditional growth driver in France. Dynamic wage developments and low inflation combined with low electricity bills and tax benefits for low-income households are bolstering private consumption. The recovery should also fuel an increase in investments in 2015, given the favourable lending conditions. From 2016, the measures taken by the French government to reduce labour costs and the planned investment package of the European Commission should add further momentum to investments.

Foreign trade, in contrast, is not likely to contribute significantly to positive growth. In 2014, net exports reduced growth by 0.3 percentage points. This year it should add 0.2 percent to GDP due to rising global demand and the favourable exchange rate of the euro. With domestic demand gathering pace, the contribution from net exports is expected to go down again in 2016. This indicates a structural weakness in the French export sector.

In view of the slow pace of economic recovery, the government measures to reduce labour costs will only have a limited positive impact on the jobs market in the short term. In 2015 and 2016, the increase in employment will not be able to keep up with the growth of the labour force. Thus, the unemployment rate is unlikely to drop below the 10 percent mark in the next few years. Youth unemployment at 24.3 percent in 2014 was just above the EU and euro area average. The French employment rate (15 to 64 year olds) at 64.1 percent in 2013 was exactly the EU average and slightly above the average rate for the euro area, but eight percentage points below the German rate (Eurostat).

European Commission, IMF and OECD predict growth of over one percent for 2015

In May 2015, the European Commission made a slight upward adjustment to its growth forecasts from autumn 2014 for this year and the next. Reasons given by the European Commission for this adjustment were the latest monetary policy measures taken by the European Central Bank, the relatively weak euro exchange rate, sagging oil prices and the momentum of its planned investment package (European Commission 2015b, European Commission 2015c).

The International Monetary Fund (IMF) also predicted higher growth in April 2015 compared with its prognosis at the start of the year. Downward risks such as declining investment expectations, the impact of lower growth prospects in developing countries on the export sector, geopolitical tensions with Russia and a slower recovery than expected in earlier predictions for the euro area are playing a lesser role than expected (IMF 2015). The Organisation for Economic Co-operation and Development (OECD) presented a growth forecast with similar figures in June this year. For 2016, it is similarly optimistic as the European Commission.

Growth forecast of the EU Commission, IMF und OECD in percent

	Commission (May 2015)	IMF (April 2015)	OECD (June 2015)
2015	1.1	1.2	1.1
2016	1.7	1.5	1.7

Sources: European Commission 2015c, IMF 2015, OECD 2015a

The OECD puts France's potential growth for the period of 2014 to 2030 at 2.2 percent, which is almost three-quarters of a percentage point higher than for the previous period from 2000 to 2013 (OECD 2014a). The IMF has a similar assessment of the situation, forecasting potential growth of 1.9 percent for the French economy in 2020 (IMF 2015). In order to achieve such growth rates, investments in general and currently low private investments into research and development in particular have to increase. In addition, consistent structural reforms are key to raise the employment rate thereby reducing unemployment. Ongoing deindustrialisation poses a serious risk to the country's growth potential and could result in weaker productivity gains. On the other hand, France will benefit from a demographic trend that is comparatively positive.

Economic policy

The economic and fiscal policy of Prime Minister Valls's government is aimed at increasing the competitiveness of French companies, scrutinising and cutting public spending, liberalising the market for labour and goods and achieving a better balance in the social security systems. The two main cornerstones of the government's policy for reforming the French economy are the National Pact for Growth, Competitiveness and Employment (*Pacte national pour la croissance, la compétitivité et l'emploi*) and the Responsibility and Solidarity Pact (*Pacte de responsabilité et de solidarité*), which were presented in November 2012 and in early 2014 respectively (OECD 2014b).

The National Pact for Growth, Competitiveness and Employment sets out 35 individual measures. These are based on the proposals to increase French competitiveness that were prepared by Louis Gallois, the government's commissioner for investment and former CEO of EADS. Probably the most significant measure here is a

tax credit of 20 billion euros to reduce labour costs in the low-wage labour market. Other measures are geared at improving qualitative competitiveness.

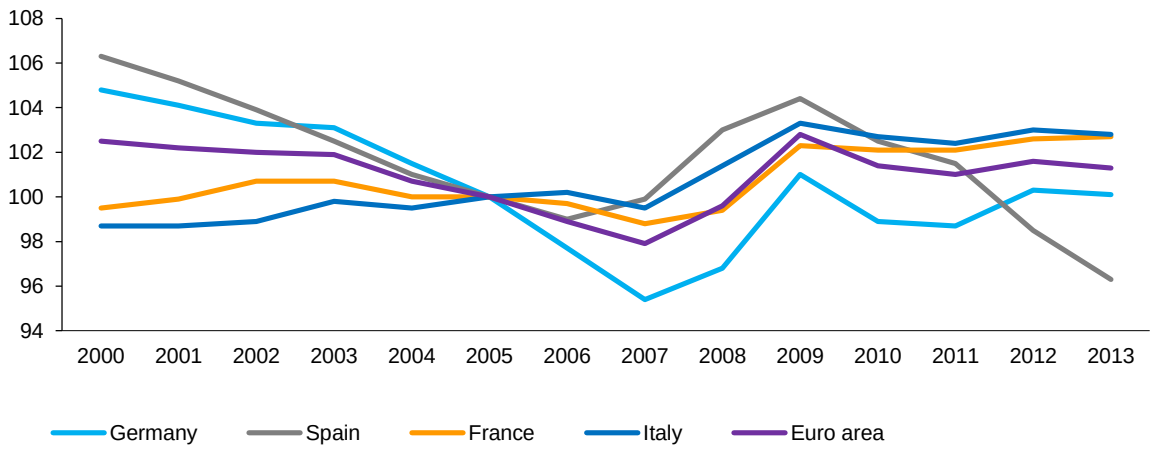
The Responsibility and Solidarity Pact is a collection of measures presented by President Hollande in January 2014. They were adopted by parliament in summer 2014 and entered into force at the start of this year. The Responsibility and Solidarity Pact consolidates the temporary measures initiated by the National Pact for Growth to reduce unit labour costs. It is also designed to improve the dialogue between employer associations and trade unions, with a view to bringing them on board for future government reforms. At the initiative of President Hollande, both sides have been meeting since July 2012 at regular intervals for the so-called *Conférence sociale*. The objective of the meetings is to establish a common understanding that can serve as a basis for moving the reform process forward.

With unemployment still on the rise, Prime Minister Valls has presented further measures in the past few months that are set to be implemented swiftly. In April 2015, he presented a package of measures to promote investment by companies and public authorities. This includes a measure that allows companies to write down for the period of one year not the usual 100 percent, but 140 percent of the value of investments. The measures also include a 2.1 billion euros increase in funding for the public investment bank Bpifrance (*Banque publique d'investissement*), which was established in late 2012. In June 2015, Valls presented an 18-point programme to strengthen small and medium-sized enterprises entitled *Tout pour l'emploi dans les TPE et les PME*. This programme includes a bonus of 4.000 euros for hiring the first employee in the next twelve months. Other points are more flexibility in extending temporary employment contracts and a period of grace of three years for companies that cross thresholds in the number of employees that would normally lead to changes in social security and tax payments. The 18-point programme is scheduled for implementation in early July 2015 (French Embassy 2015).

Labour market reforms have yet to bring about turnaround

The efforts to reform the labour market have been centred around restoring the price competitiveness of French companies, which has suffered under the upward wage trends since 2000 resulting in a sharp increase in unit labour costs.

Development of real unit labour costs*



* 2005=100

Source: Eurostat

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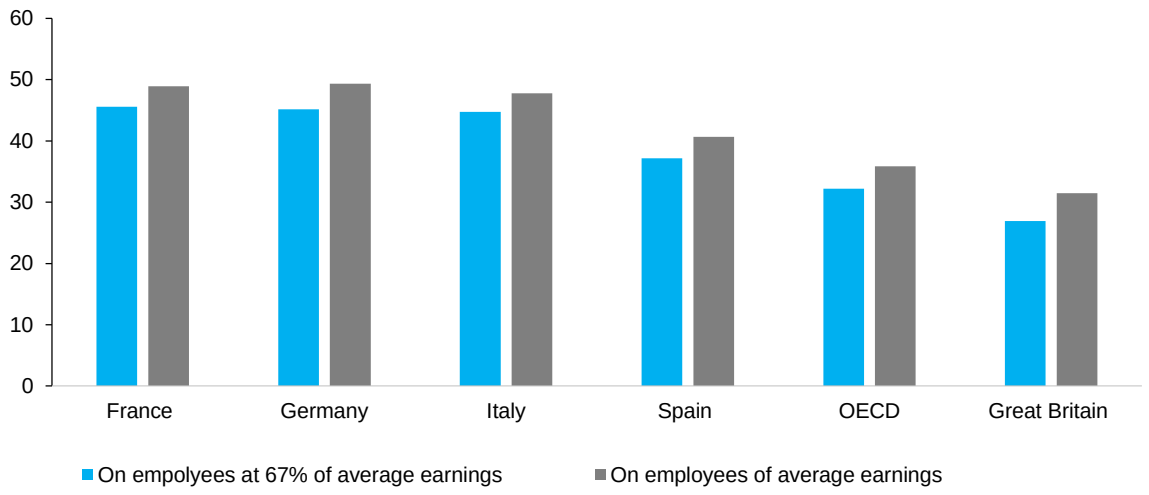
France has one of the highest labour costs per hour in the euro area. In 2014, the hourly wage in the industrial sector at 37 euros was only slightly under the German rate of 37.10 euros. Belgium was the only other country to have a higher rate, while the average for the euro area is 5 euros less. In the service sector, the difference to the euro area average was even slightly larger. Over the past 15 years, real wages in France have trended upwards with relatively high momentum despite rising unemployment. Even though rising wages may have helped bolster private consumption in the short term, it has led to structural problems in the medium term (Enderlein and Pisani-Ferry 2014). Furthermore, in a European and international comparison, the taxes on French wages are high, especially on low wages.

Tax burden on labour in 2013 in percent



Source: OECD

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To counteract this situation, the French government introduced the tax credit for competitiveness and employment (*Crédit d'impôt pour la compétitivité et l'emploi*, or CICE) in its National Pact for Growth, Competitiveness and Employment. This measure was implemented for 2013 and 2014 with the aim of reducing labour costs in the low-wage sector. The gross labour costs of employees that earn less than two and a half times the minimum wage were reduced by 6 percent through tax credits for companies; this translates into 20 billion euros in reduced costs. The Responsibility and Solidarity Pact follows on from the CICE, replacing it with a phased reduction of employer contributions to social security of 41 billion euros until 2017. Labour costs have also been reduced on a wider scale by easing the tax burden on wages up to three and a half times the minimum wage.

In the first one and a half years of his term, President Hollande also introduced the so-called secure employment law (*Loi relative à la sécurisation de l'emploi*) and a reform of pensions. The secure employment law was geared, among other things, towards increasing the flexibility of the labour market with short-time work and time-limited adjustments to wages and working hours. The pension reform adopted by parliament in late 2013 increases the contribution period necessary to benefit from a full pension by three months every three years, from 2020 to 2035 (French Embassy 2013).

Worker co-determination and social dialogue: two problem areas of key significance

In European and international comparisons, French trade unions do not have a broad membership base. At around 8 percent, France has the second-lowest level of trade union membership in all OECD states, higher only than Turkey (Germany: 18 percent) (OECD). Furthermore, worker participation is divided up between several, partially rival, trade unions. To compensate for the weak role of trade unions, the state intervenes to address remaining social concerns. Provisions in labour law, for instance, close gaps in the social partnership. On account of the active role of the state in this regard, some trade unions neglect their responsibility in the social dialogue, developing instead an attitude of protest with maximum demands.

The *Conférence sociale*, at which three employer associations and five trade unions have been meeting since 2012, is supposed to strengthen the social partnership and create a consensus for the further path of reform. Yet the search for compromise between employers and trade unions is proving difficult. The French Democratic Confederation of Labour (CFDT) is prepared to enter into dialogue with employers while some of the more radical trade union groups are attempting to boycott it. However, a compromise between the two sides is required if further reforms by the French government are to succeed. If the social partners do not support further reforms, the labour market reforms in particular could well stay stagnant on the political front until the presidential elections in 2017.

An area in which a compromise is particularly necessary as a basis for reforms is the system of worker co-determination. As the number of employees increases, a company has to set up numerous committees and is required to make more extensive social security contributions. This involves not only red tape but also means that French companies actively resist expanding their workforce. Major thresholds where employers are legally subject to increased obligations are at ten and 50 employees. As a result, there are 48 percent more companies in France that have nine employees than companies with ten employees. The number of companies with 49 employees is even 58 percent higher than the number of companies with 50 employees (European Commission 2014a).

The 'Loi Macron' to liberalise the goods and services markets

Liberalising the French goods and services markets could have a substantial positive impact on competitiveness and productivity for two reasons. First, French goods markets are relatively regulated in a European comparison. The same applies to services, including long-distance road transport, electricity markets and the retail sector. Second and more importantly, services play a major role in the French economy so that liberalising this sector can be expected to have a positive effect on other sectors as well. Services are key inputs along the whole production process in the manufacturing sector: market-based services account for 25 percent of production costs in manufacturing, and the share of services in exports is more than 50 percent already since 2009. Knowledge-intensive services account for 12.4 percent of French GDP and 13.5 percent of employment – more, in both cases, than manufacturing (European Commission 2014a, OECD 2014b).

In October 2014, Economics Minister Macron presented a draft bill with the title loi pour la croissance, l'activité et l'égalité des chances économiques, known as the 'Loi Macron'. It contains more than 200 provisions aimed at liberalising long-distance bus transport, the liberal professions (notaries and lawyers) and retail opening hours by allowing Sunday trading. The bill was presented to the Council of Ministers at the end of 2014 and discussed by parliament in January 2015. In mid-February, Prime Minister Valls invoked Article 49(3) of the French constitution, which allows adopting a law without parliamentary support. Instead, the government has withstood a vote of no confidence. Valls used this procedure, as he was unable to secure a majority in favour of the 'Loi Macron'. The left wing of the PS was particularly critical of freeing up the opening hours for shops. Article 49(3), which was last invoked in 2006, can only be used for issues involving the national budget and social security, and a maximum of once per parliamentary session for other legislative proposals.

Further reductions in red tape and administrative-territorial reform needed

In July 2013, the government announced 124 measures to dismantle and simplify bureaucracy, while further measures are being drawn up by an inter-ministerial commission. In its National Reform Programme of April 2015, the government states that measures implemented so far have cut costs by 3.3 billion euros and that half of this sum would be used to benefit companies (French Government 2015a). The 'Loi Macron' also includes further previously compiled measures to reduce bureaucracy. It is, however, unclear exactly how many of the approved measures have actually been implemented and what impact they will ultimately have on the economy. One of the most effective measures is definitely the simplification of the annual financial statements and tax filings required of small and medium-sized enterprises.

France has a uniquely complex administrative structure, accounting for 41 percent of all municipalities and boroughs in the EU. In metropolitan districts, there are 16.5 local authorities for every 100.000 inhabitants; the OECD average is 3.7. So the term *millefeuille administratif* (the administrative layer cake) sometimes used to describe this structure is not far off the mark. Until January 2016, the French government plans to reduce the French regions from 22 to 13, claiming that this will save costs of around 50 billion euros through 2017 (French Government 2015a). As well as undergoing restructuring, the regions will also be assigned additional competencies in the areas of business and infrastructure development. It has not yet been conclusively clarified to what extent this will occur and – more significantly as more politically sensitive – what competencies will have to be relinquished by other public authorities in this process.

In early 2014, another reform for the administration of metropolitan areas (*métropoles*) was adopted and is scheduled for implementation in Paris, Lyon and Marseille by 2016. This reform merges inter-municipal authorities so that they can take more coordinated action on key issues. The reform is scheduled to be extended per decree to further cities.

No lack of reform proposals from the European Commission, IWF and OECD

The European Commission and the IMF have taken a similar stance to the French national budget, both seeing an urgent need for France to tackle new and outstanding debt. In its country-specific recommendations of July 2014, the European Commission recommends seven reform areas, some of which the French government has already addressed. These include, in particular, reducing the cost of labour, simplifying the bureaucratic environment and liberalising the services sector (European Commission 2014b).

The biggest challenge facing the government is a structural reform of the labour market, which is still very inflexible and highly taxed. The French short-time work system is a good case in point. Although a new scheme has been in place since January 2013 – the *Accords de maintien de l'emploi* – it has not proved to be very useful in practice on account of the legal uncertainties involved and restrictions in its application. Companies are therefore still using the previously existing framework implemented in 2004 (European Commission 2014a). The OECD takes a similar line in its report Going for Growth 2015, released in February this year, which includes recommendations such as enhancing active labour market policies and shifting the tax burden away from labour while broadening the tax base (OECD 2015b). As an active labour market policy, the OECD recommends making sure that every jobseeker receives an employment or training offer within a few months and applying sanctions in case of a jobseeker's refusal of good offers. On this point, the IMF recommends as part of its Article IV Consultation of July 2014 to improve social dialogue as a foundation for further reform and to expand the scope of enterprise level negotiations on work and pay in order to increase the capacity of enterprises to respond to economic change (IMF 2014).

The IMF addressed the minimum wage (*Salaire minimum interprofessionnel de croissance*, or SMIC) and its negative impact, especially the costs of the potential exclusion of jobseekers from the jobs market. The level of the SMIC is fixed every year by the government, based on developments in the consumer price index and overall wages. An expert commission makes a recommendation for appropriate changes to the SMIC, but ultimately

the government can also increase the SMIC at its discretion and without prior agreement with the social partners. If inflation goes above 2 percent during the year, the SMIC is automatically adjusted by the same percent as the inflation rate once this has been determined. Compared with other large economies in the euro area – including Germany, Italy and Spain – the French SMIC is the highest in absolute terms (since January 2015: 9.61 euros per hour), has the lowest difference to the average gross monthly wage and has the most recipients measured by the proportion of employees (Eurostat).

Fiscal policy and the budget

During the European financial and sovereign debt crisis, French fiscal policy included comparatively few special measures to create economic momentum; at the same time it did not make long-term spending adjustments and only underwent minimal structural consolidation. France's fiscal policy problems are therefore not primarily the result of the crisis, but were already in evidence during the term of former President Sarkozy. A consistent structural reform of fiscal policy is required, especially in view of the weak economic recovery and high level of unemployment.

Public sector spending in France has remained above 50 percent of GDP since 1995. In the ten years from 1998 to 2007, public spending had not yet exceeded 53 percent. With the onset of the economic and financial crisis in 2008, spending compared with GDP increased on account of the crisis and slower economic growth. As a result, public spending reached a new record high last year at 57.2 percent of GDP (Eurostat).

Public budget development

As percent of GDP	95-10	2011	2012	2013	2014	2015	2016
Public spending	53.6	55.9	56.7	57.0	57.2	*not available*	
Public deficit	3.4	5.1	4.8	4.1	4.0	3.8	3.5
Public dept	64.1	85.2	89.2	92.2	95.0	96.4	97.0

Sources: Eurostat, European Commission 2015c

The 2015 budget aims to keep new debt below 4 percent

In 2014, the budget deficit was 4.0 percent of GDP, which – contary to expectations – was 0.1 percentage point below the 2013 deficit. Public revenues grew by 2.0 percent, climbing at a slower rate than in 2013 (3.3 percent). Public spending increased by 2.2 percent, primarily on account of the measures taken by the government to reduce the cost of labour. Excluding these costs, public spending slowed down. The – temporary – reduction in France's contribution to the EU budget also contributed to the low expenditure growth (European Commission 2015c).

The first draft budgetary plan for 2015 presented by the French government in October 2014 projected new debt of 4.3 percent. This draft did not yet take into account the positive impact of the low refinancing costs caused by the expansive monetary policy of the European Central Bank, which was further reinforced by the announcement in January 2015 of a large-scale purchase of government bonds and private assets. According to the European Commission, the draft would have resulted in a minimal reduction of 0.1 percentage points to the structural deficit. As this would put France significantly below the binding EU targets, the government then went back to

the drawing board and presented a revised budget in late October. This proposed a further structural improvement of 0.2 percentage points, corresponding to 3.6 billion euros. The sum comprises several items, including higher revenues from the fight against tax fraud and tax optimisation, lower debt servicing than originally planned and a reduced contribution to the EU budget.

In a working document of November 2014, the European Commission was dubious of the projected 3.6 billion euros, pointing to the fact that no further cost savings had been planned in this context (European Commission 2014c, European Commission 2014d). Government debt reached 95.0 percent of GDP in 2014, in part due to the low economic growth, and is forecast to reach 96.4 percent in 2015. The French government is planning to stabilise its debt-to-GDP ratio at 97 percent for 2016 and reduce it to 95.5 percent through 2018 (French Government 2015b).

Slimming down the public sector is a mammoth project

France's public spending ratio in 2014 of 57.2 percent of GDP was far above the euro area average of 49.0 percent. A cost-savings programme is planned for the 2015–17 period to slow down expenditure growth by 50 billion euros; this will also help ensure the financing of the Responsibility and Solidarity Pact's measures. Cost savings of 20 billion euros are already planned in for this year, including 7.7 billion euros on the national level, 3.7 billion euros on the regional level and 9.6 billion euros in the social security systems. If this endeavour succeeds, the government spending-to-GDP ratio could drop to below 55 percent by the end of 2017 (European Commission 2014d, French Government 2014). In the medium term, France will have to cut spending by a further three to five percentage points in order to achieve a balanced budget. All public expenditure is currently being scrutinised to this end. There are indications that France can also fulfil major social policy objectives through lower and more efficient public spending.

Despite France's increasing government debt ratio, the percentage of GDP used to service its debt has remained relatively stable at 2.5 percent of GDP over the past few years. Interest rates on government bonds have dropped from an average of 4.0 percent between 2000–07 to 3.0 percent between 2008–13. Yields on ten-year French government bonds have converged towards the interest rate of German government bonds after diverging during the European financial and sovereign debt crisis. The expansive monetary policy of the European Central Bank, reinforced in January 2015 with the announcement of the large-scale purchase of government bonds and private assets, has pushed down interest rates on government bonds and the difference in interest rates between the various issuing euro area members (ECB 2015).

French economic policy under EU economic surveillance

France and the Stability and Growth Pact

Since April 2009, France has been subject to the Excessive Deficit Procedure (EDP) of the Stability and Growth Pact. At the beginning of the procedure, France was initially given time to 2012to correct its excessive deficit by bringing new debt down to under 3 percent. This deadline was subsequently extended to 2013. In June 2013, the Ecofin Council decided to once again extend the deadline to 2015 on account of the unfavourable economic events (European Commission 2014c, European Commission 2014d).

France again failed to comply with the 3 percent threshold last year and presented a budgetary plan for 2015 that also initially put new debt to substantially above 3 percent. In late February 2015, the European Commission pressed for another two-year extension until 2017. The Ecofin Council agreed to this proposal. In conjunction with the new deadline, the Commission is now demanding an ambitious implementation of structural reforms and a structural adjustment this year of not 0.3 percentage points as planned by the government, but 0.5 percentage points. This figure corresponds to the benchmark specified in the Stability and Growth Pact, but is still under France's originally defined EDP target of 0.8 percentage points. The draft budgetary plan of the French

government of April 2015 factors in this structural adjustment, planning 0.5 percentage points for 2016 and 2017 as well. According to the government draft, new debt will amount to 2.7 percent in 2017 (French Government, 2015b).

MIP sees competitiveness, exports and new debt as problematic

In the course of the Macroeconomic Imbalance Procedure (MIP), the European Commission confirmed that France had excessive imbalances that required decisive policy action and specific monitoring. In the six-stage process, France is currently on the second to last stage – the last stage would result in the beginning of the actual Excessive Imbalance Procedure.

The European Commission is primarily focused on imbalances as a result of deteriorating net exports, declining competitiveness and increasing public debt. According to the Commission, France's structural reforms to increase competitiveness are set to have a positive impact on exports but will only suffice to curtail the loss of export market shares and not be enough to cause a general turnaround. Over a period of five years, the export market share has dropped to 14.6 percent, which is clearly above the threshold value for the MIP (6 percent) (European Commission 2014a).

The MIP scoreboard for France (2014)

Indicator	Threshold	Level of France
External imbalances and competitivness		
Current account balance	-4% or 6% of GDP (3-year average)	- 1.3
Net international investment position	-35% of GDP	-16.4
Real effective exchange rate	±5% change (3-year average)	- 1.2
Export market share	-6% change (5-year average)	-14.6
Nominal unit labour costs	9% change (3-year average)	3.9*
Internal imbalances		
Deflated house prices	6% y-to-y change (inflation adjusted)	- 2.0
Private sector credit flow	15% of GDP (consolidated)	1.8
Private sector debt	133% of GDP (consolidated)	137.3
Genaral government debt	60% of GDP	95.1
Unemployment rate	10% 3-year average	10.1

* 2013 data

Source: European Commission

In addition to the public debt discussed above, unemployment is also increasingly becoming a problem. The unemployment rate for this year is set to remain at 10.4 percent and only go down slightly in 2016. France was so far still under the threshold for the MIP (average unemployment of 10 percent over 3 years), but with the figures for 2014, it is now overstepping the mark.

Excursus: A look at the EU's instruments for economic policy coordination

With the **Stability and Growth Pact**, EU member states have agreed to maintain budget discipline in a long-term and sustainable manner. The Pact lays down limits for annual budget deficits (a maximum of 3 percent of GDP) and the level of debt (a maximum of 60 percent of GDP). Higher deficits are only permitted in justified cases. With a preventative arm, the European Commission together with the Ecofin Council reviews whether the budget planning of the member states will lead to a sound budgetary position in the medium term. The corrective arm includes the Excessive Deficit Procedure (EDP) that can be initiated in cases where the 3 percent limit on new debt is exceeded or where debt is not managed appropriately to be brought down to 60 percent. If the member state in question does not adhere to the corrective measures to reduce the debt, the EU can impose sanctions.

The **European Fiscal Compact** imposes stricter budgetary rules, envisaging a limit on the structural deficit of public budgets to 0.5 percent of GDP for countries whose debt is already in excess of 60 percent. An automatic correction mechanism is triggered in the event of significant deviations (German Federal Ministry of Finance 2012, Deutsche Bundesbank 2015a).

The **Macroeconomic Imbalance Procedure** (MIP) aims to avoid and correct macroeconomic imbalances. A scoreboard composed of ten indicators to determine foreign and domestic economic imbalances is designed to identify imbalances at an early stage and take corresponding action. If the indicators exceed certain thresholds the affected EU member state is subjected to a more in-depth country analysis (in-depth review). In the event that problematic imbalances are identified, the Council gives the member states in question recommendations for corresponding corrections (the so-called preventative arm) based on proposals made by the European Commission. Sanctions (the corrective arm) are possible in the last instance if a member state does not initiate corresponding corrective measures.

The **"six-pack"** is a package of secondary legislation containing five EU regulations and one EU directive. It reinforces the rules of the Stability and Growth Pact with automatically triggered sanctions and provides a basis for applying the MIP. The **"two-pack"** comprised of two further EU regulations supplements the six-pack by expanding the preventative surveillance on budgetary planning of the Stability and Growth Pact: Every year, euro area members have to submit an overview of their budget plans for the next year to the European Commission by the middle of October.

Manufacturing

France is Europe's third largest economy (after Germany and the United Kingdom) with the third most important industrial sector (after Germany and Italy). In 2014, France accounted for 11.5 percent of gross industrial value added in the EU, which corresponds to a volume of 219.4 billion euros (for comparison: Germany: 30.5 percent or 581.0 billion euros; Italy: 11.8 percent or 225.4 billion euros). In 2013, there were 2.7 million people employed in manufacturing, which is a little more than every tenth employee.

Key industrial sectors in France (2012)

NACE code	Sector	Share of gross industrial value added (%)	Number of employees
10	Food	14.8	534.063
11	Beverages	3.2	50.900
17	Paper	2.1	67.595
20	Chemicals	7.3	149.522
21	Pharmaceuticals	4.9	76.158
22	Rubber and plastics	5.2	164.649
23	Non-metallic mineral products	4.1	124.517
24	Basic metals	2.5	79.939
25	Metal products	9.5	317.560
26	Computers	5.5	141.127
27	Electrical equipment	4.0	115.694
28	Machinery and equipment	6.6	177.960
29	Motor vehicles	6.4	243.437
30	Other transport equipment	6.6	135.440

Source: Eurostat

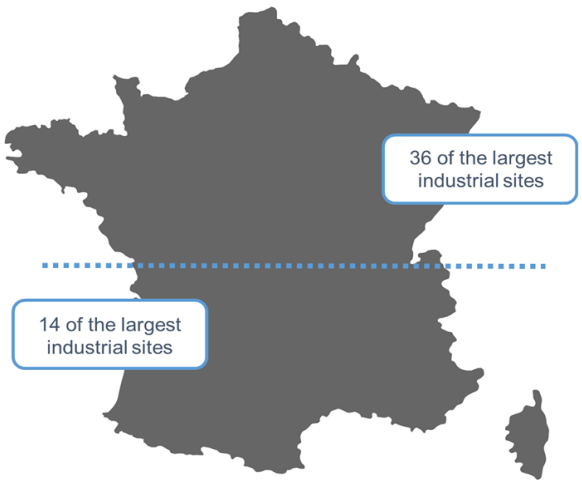
BDI

The 14 industrial sectors listed in the table account for just over 80 percent of gross industrial value added. The biggest industry is the food industry with a share of 14.8 percent of gross industrial value added and by far the most employees. These figures are higher than in Germany but not uncommon in European comparison (Deutsche Bank Research 2013). Spain's and the United Kingdom's food industry figures are similarly high with the difference that employees are employed by significantly fewer enterprises. The ratio of employees to enterprises in the French food industry is just under 10:1, while in the United Kingdom the ratio is over 58:1. Spain's food industry enterprises have four employees more on average than France's.

Compared with the other large European industrial producers Germany, Italy, the United Kingdom and Spain, the French chemical, pharmaceutical as well as rubber and plastics industries are relatively strong. Mechanical engineering and the automotive industry do not have the same significance in France as they do in Germany. The share of mechanical engineering in gross industrial value added in Germany is almost two and a half times as high as in France. The German automotive industry's contribution to national gross value added is more than twice that of the French car industry. France is, however, strong in the manufacturing of other transport equipment. The French aeronautics and space industry is particularly competitive. On a European comparison, it also has the highest production value in absolute terms. France is also extremely competitive in luxury goods, although its share of gross industrial value added is lower than the 14 industrial sectors listed above. In particular the two French luxury goods holding companies LVMH (with brands including Louis Vuitton and Dior) and Kering (with brands including Gucci and Yves Saint Laurent) generate very high turnovers in this industry.

The majority of corporate activities are concentrated in the Paris region. Of the 30 manufacturing companies listed in the French CAC 40 index, 25 are headquartered in Paris. The exceptions here are the aeronautics group Airbus based in Toulouse, automotive supplier Michelin in Clermont-Ferrand and the electrical equipment producer Legrand in Limoges (located in the French Massif Central). Steel producer ArcelorMittal and chemical producer Solvay are both listed on the French stock exchange but are headquartered in Luxembourg and Brussels respectively.

Major industrial production sites in France based on their location in relation to La Rochelle



Source: kartix|m/Fotolia

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The major centres of industrial production are mostly located in northern France. If one draws an imaginary line across France, dividing it in two at around the height of La Rochelle, the southern part only has 14 of the 50 largest production sites (Strategy Action 2015a).

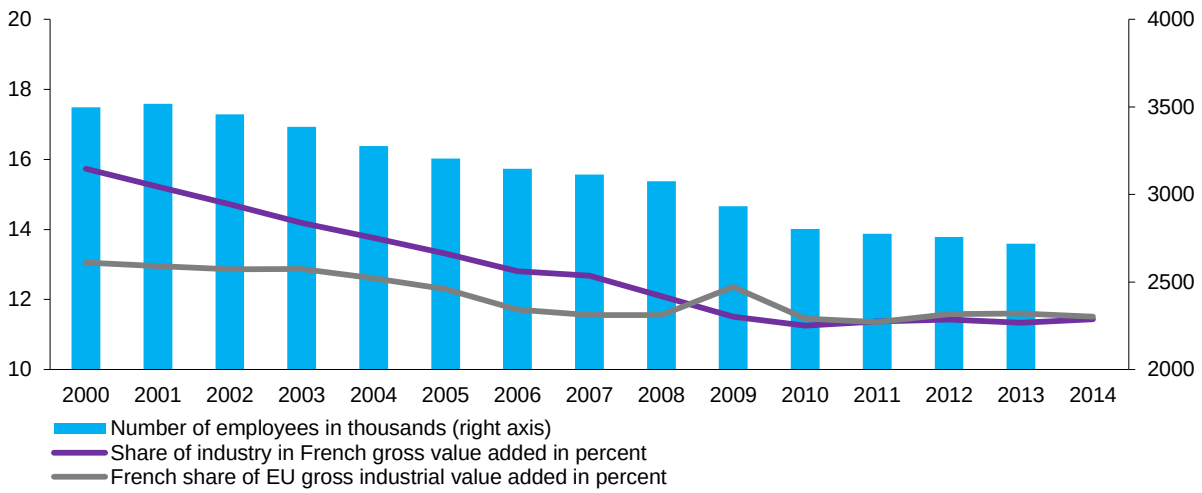
Nevertheless, some major production sites do operate in the southern half of France, including Airbus in Toulouse and Marignane near Marseilles in aeronautics, Renault Trucks in Saint-Priest near Lyon and Michelin in Clermont-Ferrard in the automotive sector, Schneider Electric Industries in Grenoble and the Dutch semiconductor producer STMicroelectronics in nearby Crolles in electrical engineering, and pharmaceutical company Sanofi in Marcy-L'Étoile near Lyon. Over half of the 50 largest production sites in France are in the automotive industry, particularly PSA Peugeot Citroën and Renault.

Creeping and continuous deindustrialisation since 2000 proving difficult to reverse

Although French industry still plays an important role in Europe and internationally, it has gradually been losing significance on a global scale in the last 15 years. The competitiveness of French industry has dropped since 2000, which has become apparent in lower corporate margins and losses on export markets. The share of industry in gross value added (GVA) of the overall economy has been falling almost continuously, from 15.7 percent in 2000 to 11.4 percent in 2014. Employment in the industrial sector has also declined, down by 779.000 employees or 22 percent.

This trend has not been caused by crises but has clearly been brought about by structural problems. In the pre-crisis period from 2000 to 2008, the contribution of manufacturing to the gross value added dropped by an average of 0.46 percentage points per year. The decrease from 2009 to 2014, on the other hand, was marginal at under one-tenth of a percentage point. Employment figures are trending similarly, with the number of employees in manufacturing in France already dropping by more than 400.000 from 2000 to 2008. This is very different to developments in Italy and Spain, where the number of employees only stagnated slightly from 2000 to 2008 before plunging as a result of the crisis.

Manufacturing in France since 2000



Source: Eurostat

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The French industry's loss of price competitiveness over the course of the last one and a half decades has coincided with a steady loss of export market shares. In addition, there have been negative developments in the area of qualitative competitiveness, including product quality, innovation, customer service and sales networks. The course of action French companies can take to operate competitively in these areas is limited as margins are falling. The gross operating surplus of the French manufacturing sector for 2013 at 29.7 percent of value added was the lowest ratio in the euro area. France has therefore suffered continuous losses in the competitiveness of its exports across all technology sectors. Especially hard hit have been the medium-technology sectors, which account for a larger export volume than the high and low-technology sectors. France lost greater shares here than its euro area competitors Germany, Italy and Spain both before the crisis from 2000 to 2008 and from 2008 to 2013 (European Commission 2015a).

In France, hopes are now high that the digital transformation and the opportunities this presents will increase the country's gross industrial added value. In May 2015, Economics Minister Macron presented an initiative called *Industrie du futur*, based on a previous project and roughly the equivalent of Germany's *Industry 4.0* scheme (French Government 2015c). It outlines nine fields in which industrial solutions are now to be developed to increase French competitiveness. The *Industrie du futur* initiative is also to be structured to have natural points of contact with Germany's Industry 4.0 platform so as to facilitate a partnership with the German counterpart, which is scheduled to start in October 2015. This partnership is part of the broader strategy of *Industrie du futur* to improve cooperation in European and international standardisation procedures.

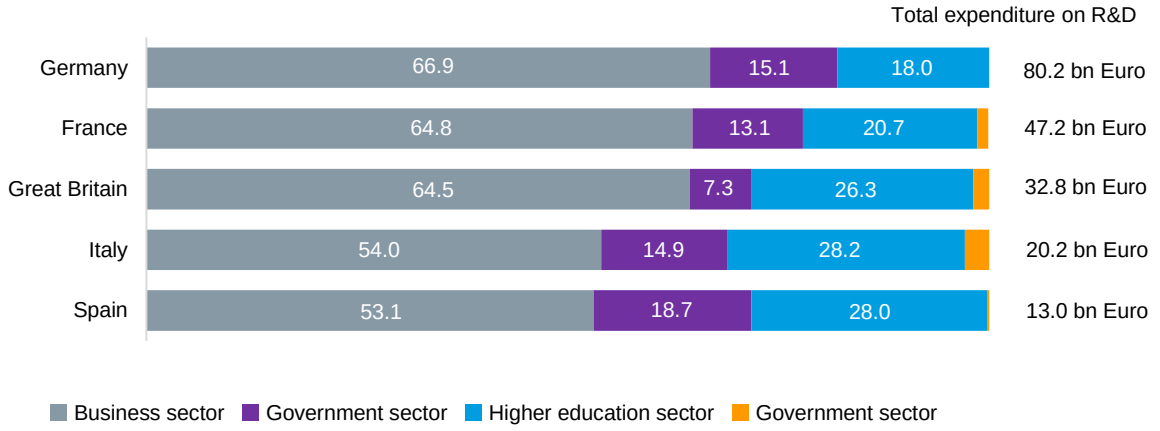
Research and development activities in France

In 2013, French expenditure in research and development (R&D) was at 2.2 percent of GDP, only 0.1 percentage points more than in 2000. Public investment in R&D measured as a percentage of GDP largely remained steady at 0.8 percent. Indirect support for private R&D spending, which should also be added to this figure, has been substantially increased since 2008, particularly through the research tax credit scheme, the *Credit d'impôt de recherche* (5.3 billion euros or 0.3 percent of GDP in 2012).

Since 2004, R&D activities have also been promoted in special competence clusters called *Pôles de compétitivité.* These clusters are regional networks of enterprises and research and educational institutions working together on a specific topic. There are currently 71 of these competence clusters with an average of 190 actors involved in each (ratio of companies to research and educational institutions is around 5:1). The French state supports the clusters with financial aid for selected cooperative projects and loans for small and medium-sized enterprises for producing and marketing the project results.

Private sector R&D spending amounted to only 1.3 percent of GDP in 2000, rising marginally to 1.4 percent in 2013, which is low compared to the highly innovative Scandinavian countries. French manufacturing has a fairly high R&D intensity; at 8 percent of value added spent on R&D it has the sixth highest percentage in the EU. This structural strength is, however, reduced by the relatively low contribution of manufacturing to the national economy. Manufacturing in France has relatively few SMEs and a comparatively small number of high and medium-technology industries. The innovation capacity of the manufacturing sector is also low on a European comparison with only 43 percent of industrial enterprises in France actively pursuing product or process innovations, 20 percentage points less than the figure in Germany (63 percent).

Share of expenditure on r&D in 2013, by sector in percent



Source: Eurostat

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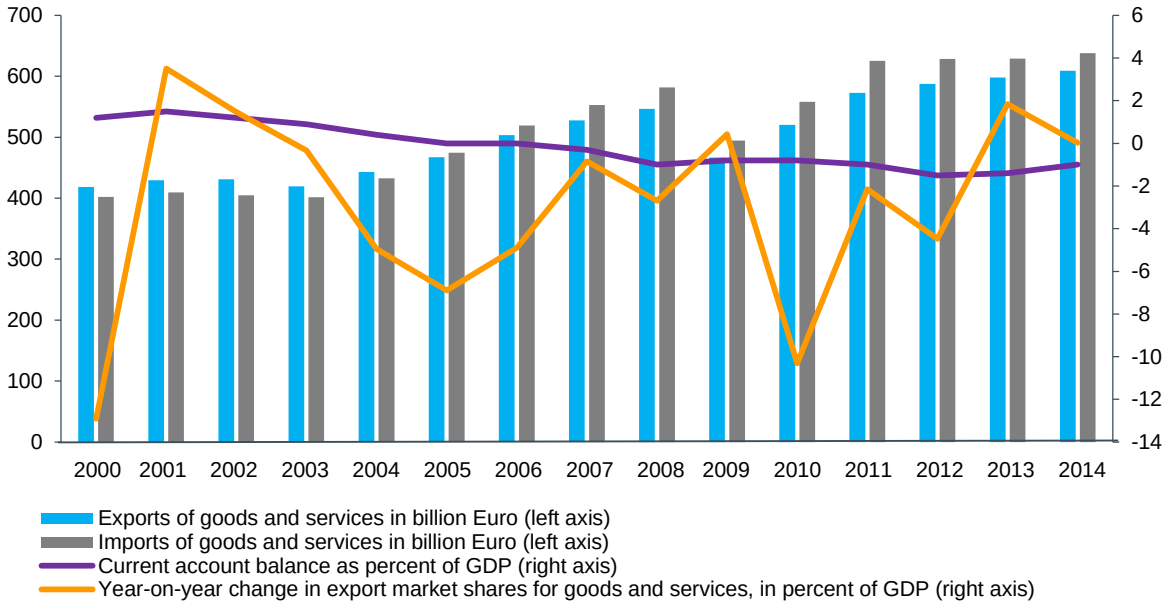
Trade and investment

In 2014, France registered an export volume of over 609 billion euros, which corresponds to 28.6 percent of GDP. Compared with 2000, exports as a share of GDP only increased marginally by 0.4 percentage points (Eurostat). About three-quarters of exports in 2014 were goods and one-quarter services. Imports in France came to 29.9 percent of GDP, with roughly the same ratio of goods to services at 3:1. Net exports have made a negative contribution to growth since 2005 on account of a deficit in the trade of goods.

Foreign trade with lower volume and focused on Europe

In 2014, France had a ratio of foreign trade (of goods) to GDP of 43.4 percent. Both Italy's and Spain's ratio was higher at 44.8 percent and 47.2 percent respectively. The difference to Germany is particularly large, with the German ratio of foreign trade to GDP for last year amounting to 69.2 percent (Eurostat). Trade with other EU countries in 2013 accounted for 58.0 percent of exports and 59.5 percent of imports, higher on both accounts than the figures for Germany and Italy (Germany Trade & Invest 2014a). The five most important supplier countries of France are all euro area members (Germany, Belgium, Italy, Netherlands, Spain), with the first third-party country the United States at sixth place. The situation is similar with the importing countries: Germany, Belgium, Italy, the United Kingdom and Spain head the list, so the focus here is also clearly on Europe. The United States takes sixth place in this ranking, too. In comparison, German trade relations are much more globally oriented, with the two third-party countries China and the United States ranking among the five most important trade partners (Germany Trade & Invest 2014b).

French foreign trade since 2000



Source: Eurostat

BDI

France's export sector is shrinking

Between 2008 and 2013, France's global export market shares for goods and services decreased by 13 percent, due mainly to reductions in the trade of goods. The global trade in goods rose by 15 percent between 2008 and 2013, while the French trade in goods during the same period dropped by 5 percent (European Commission 2015a). Two factors were mainly responsible for this development. First, the key export destinations for French goods – especially in the euro area – grew slower than the global export market, so France benefited less from the overall market momentum. Second, within these goods markets French exports increased at a much slower rate (18 percentage points) than the markets themselves. This clearly shows that competitors are responding more competitively on these markets. This trend had already emerged in the previous years. Between 2000 and 2008, France's export competitiveness in the medium-tech sector, which accounts for a large share of the export volume, dropped the most – compared to Germany, Italy and Spain – with French industry suffering export market losses of 4 percent every year.

Between 2008 and 2013, French exports differentiated according to the high-tech, mid-tech and low-tech sectors delivered a mixed performance. Competitiveness in the high-tech sector increased slightly, though only on the strength of the aeronautics and space industry. Excluding this sector, France's export competitiveness actually dropped. As aeronautics and space make up only one-fifth of the goods exported, this dynamic not enough to compensate for losses in the mid-tech and low-tech sectors. French export market shares in the mid-tech sector dropped by an annual average of 6.4 percent between 2008 and 2013, much more than in Germany, Italy or Spain. As the mid-tech sector accounts for over half of manufacturing exports, this greatly affected overall performance. The trend in the low-tech sector has also been negative, though at an annual average loss of 2.0 percentage points, the losses in the export market shares were not as high.

In France, criticism has been levelled at the euro exchange rate from many sides over the past few years, claiming that it is too high and therefore damaging to French exports. It is true that French exports, as opposed to German exports, are primarily price competitive with a large proportion from price-sensitive product categories. Changes in the effective exchange rate therefore have a larger impact on export trends than they do in Germany, for example (European Commission 2014a). According to econometric analyses, however, the direct impact of price factors on export performance is much smaller than the impact of non-price factors. Furthermore, the market share of French exports has been on the decline since 2004 and can therefore not be associated *per se* with the euro strengthening against other currencies.

Exporting SMEs in France with comparatively little importance

A structural characteristic of the French economy is the low number of medium-sized enterprises. In 2012, French enterprises employed 5.9 people on average compared with the European average of 6.4 and 12.2 in Germany. In France, only 0.9 percent of companies have between 50 and 250 employees, while the EU average is 1.1 percent and in Germany the percentage is 2.6. In manufacturing in Germany, it is as high as 8.2 percent, compared with only 3.8 percent in France. Various studies have identified a correlation between the size of companies and export performance. Put simply, French companies have competitive disadvantages compared with their competitors from other countries as they have higher fixed costs for exports when measured by company size.

In 2013, the French customs office recorded that companies with between 50 and 250 employees accounted for 4 percent of exporting companies and 33 percent of the export volume. Smaller enterprises, accounting for 96 percent of those engaged in exporting, only accounted for 23 percent of the total export volume. The proportion of companies with more than 250 employees is marginal although they do account for 44 percent of exports (European Commission 2014a).

High direct investments at home and abroad

In 2013, France accounted for 12.6 percent of all foreign direct investment within the EU. France's share has, however, been falling somewhat: in 2010 it was at 13.5 percent, with foreign investment flows showing a similar trend. In 2013, foreign investment flows were at USD 4.9 billion, comprising only 2.0 percent of all flows within the EU. Of the investments made by EU member states abroad, France accounted for 15.4 percent, which is almost exactly the share of French economic output in European GDP.

Foreign direct investment (FDI) to and from France				
By FDI flows	**2010**	**2011**	**2012**	**2013**
Inward to France				
in billion USD	33.6	38.6	25.1	4.9
Share of EU in %	8.8	7.9	11.6	2.0
Outward from France				
in billion USD	64.6	59.6	37.2	-2.6
Share of EU in %	13.3	10.2	15.6	-
By FDI stock	**2010**	**2011**	**2012**	**2013**
Inward in France				
in billion USD	990.4	973.1	1029.8	1081.4
Share of EU in %	13.5	13.0	12.8	12.6
Outward from France				
in billion USD	1516.1	1503.2	1568.8	1637.1
Share of EU in %	16.3	15.8	16.0	15.4

Source: United Nations Conference on Trade and Development

BDI

Close German-French economic ties

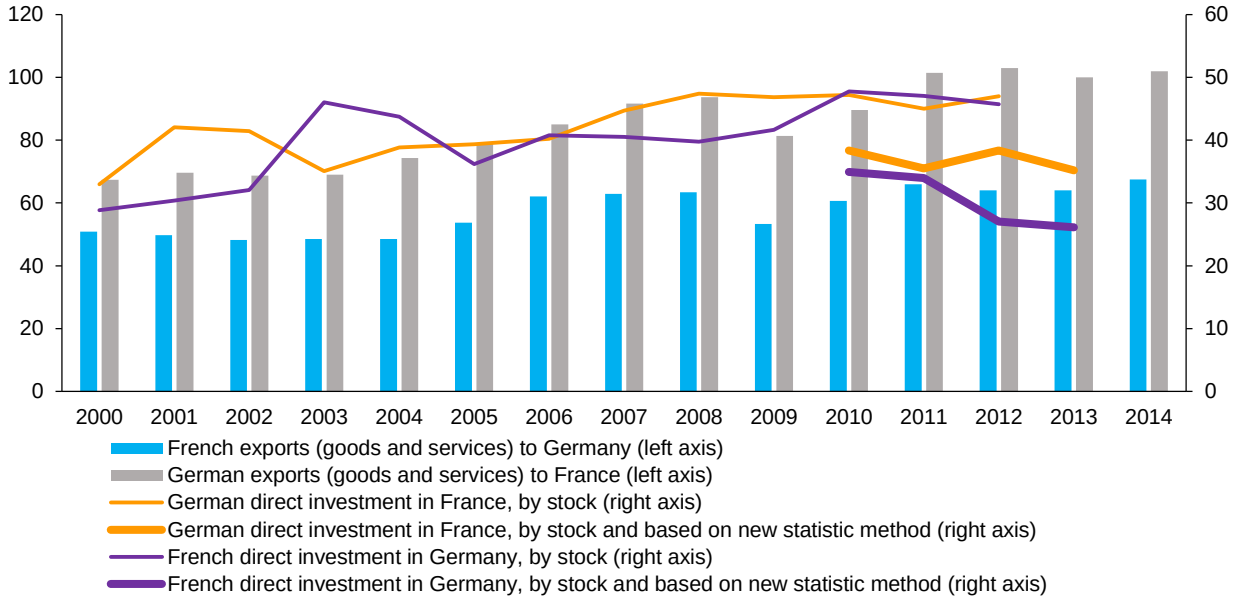
Since 2011, trade between Germany and France has been at between 167 billion euros and 169 billion euros per year. Following a slight decline in 2012 and 2013, the volume of trade increased by 3.3 percent in 2014 to 169.4 billion euros. In 2014, France's trade deficit with Germany dropped to 34.5 billion euros, which was less than the deficits recorded in 2011, 2012 and 2013. The deficit was reduced primarily by rising French exports to Germany while imports from Germany in 2014 were only around 0.5 billion euros higher than in 2011.

Last year, France was therefore the most important export destination for Germany, as it has been in the past 54 years. Conversely, France is the third most important supplier country for Germany, after the Netherlands and China. Around 9 percent of German exports go to France, and some 7 percent of German imports are from France. Germany is even more important for France. It is its top trading partner, with 16.6 percent of all French exports going to Germany in 2014. That corresponds to more than one third of French exports in the euro area. For imports from Germany, these two figures are even slightly higher.

France and Germany do not just trade final products but are heavily intertwined in industrial value chains. A look at the exchange of intermediate industrial products reveals that German-French partnership in the area of value creation chains is the most intense in Europe if measured according to the bilateral import of intermediate products (IW Cologne 2013). The key industries for the trade in intermediate products are the chemical and metal industries and, even more importantly, the automotive industry and other transport equipment, including the aeronautics and space industry.

France therefore also benefits from rising German exports – if German exports rise by 10 percent, this causes an increase of 11 percent in French intermediate exports. This percentage is lower for the other two large industrial countries in the euro area, Italy and Spain, at 10 and 7 percent respectively.

Trade and direct investment between France and Germany since 2000 (in billion Euro)



* based on new statistic method from 2010 consolidated to include financial ties

Sources: Federal Statistical Office; German Bundesbank

There are also close relations in investments between these two countries, although not quite as intense as their trade relations. French direct and indirect investments in Germany in 2013 totalled more than 26 billion euros. That is almost 6 percent of all foreign direct investment in Germany. At over 35 billion euros, the volume of direct and indirect German investment in France is almost 10 billion euros more than French investment in Germany.

Almost one-quarter of German investments are in French manufacturing – the proportion of French investments in German manufacturing is similar, despite France's relatively small industrial sector. German investments in manufacturing in France are mainly in the automotive industry, the chemical industry and mechanical engineering, which together account for almost 70 percent of all investments. With a share of 40 percent, investments in the automotive industry are particularly high.

Even if German companies in France are more numerous than French companies in Germany, German companies in France employ only 15 percent more employees than French companies do in Germany. These figures demonstrate that, to a certain extent, the German SME structure replicates itself in France, while French companies employ more workers on average.

Company activities in the partner country (2013)		
	French companies in Germany	**German companies in France**
Indirect and direct investment (in billion Euro)	26.1	35.2
in manufacturing (in billion Euro)	5.4	8.5
Number of countries in the partner country	1.203	2.265
Number of workers employed by these companies	273.000	319.000
Annual revenues of these companies (in billion Euro)	143.2	153.5

Source: German Bundesbank

BDI

In sum: right direction but a long way to go

It is difficult to accurately assess the French reform policies of the last one and a half years and to pass a final verdict on their success. Has the level of structural reform reached a critical mass? What is the combined impact of the measures that have been implemented? And what is the overall economic environment in which France can build on in its recovery?

The French government has instituted reforms in many areas since early 2014. It will be much easier to measure the success or failure of the initiatives in hindsight as reforms take time to take effect. This is why a path of reform needs long-term political commitment. And reform is urgently needed to counteract the challenges France is facing in view of the ongoing loss of export market shares, the high level of unemployment and the difficult state of public finances. It is questionable whether President Hollande will manage to reach a broader societal consensus on reforms in the time he has remaining in office, until 2017. Social dialogue will play a central role here.

The trust in the European set of rules will also depend on developments in France. The euro area members have shown their confidence in France by agreeing to extend its deadline for meeting the deficit targets under the Stability and Growth Pact. And it is in France's interests to fulfil these obligations not only for the sake of economic development – but also to prevent the jointly established rules from losing their validity.

France's future economic performance will also depend in large part on how the country deals with the upheavals brought about by the digital transformation. Digitalisation offers opportunities but these must be actively used. The companies in the CAC 40 will know how to tackle these challenges. How receptive SMEs are of digital developments will be decisive in determining whether France comes out of digitalisation as a winner. France cannot afford to fall behind in this regard as it has in terms of exports.

One of France's greatest assets is its very competitive services sector. If the services sector can use digitalisation to its advantage as part of efforts to establish closer ties with manufacturing, it would benefit more than the French industry. It would also open up new opportunities for German companies and would further increase the appeal of working with our neighbours to the west. With their plans to link up the platforms *Industrie du futur* and *Industry 4.0*, policymakers can pave the way for this to happen.

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