

# Does inequality hurt economic performance?

By [Francesco Saraceno](#)

Economic theory has long neglected the effects of income distribution on the performance of the economy. Students were taught right from Introduction to Economics 101 that the subject of efficiency had to be separated from considerations of equity. The idea is that the size of the cake had to be expanded to the maximum before it is shared. It was implicit in this dichotomy that economists should address the issue of efficiency and leave the question of distribution (or redistribution) to the politicians. In this framework, the economist's role is simply to ensure that choices about the channels for redistribution through taxation and public spending do not affect growth by interfering with the incentives of economic agents. Echoes of this view can be found both in the debate about the taxation of very large incomes envisaged by the French Government as well as in authors like [Raghuram Rajan](#) who justify inequality with references to technical progress and international trade, a view refuted by [Paul Krugman](#).

Since the work of Simon Kuznets in the 1950s, some economists have of course questioned whether excessive inequality might not inhibit economic growth, in particular by blocking the accumulation of human capital. But this has long been a minority view among economists. Indeed, the dramatic increase in inequality documented among others by [Atkinson, Piketty and Saez](#) as well as by institutions such as the [OECD](#) and the [IMF](#) failed to give rise to a deep-going reflection about the relationship between inequality and economic performance.

It was the crisis that revived this concern. Growing inequality [is now suspected](#) of being a source of increasing

household debt and speculative bubbles, leading to the accumulation of internal and external imbalances that have set off the current crisis. This is the argument developed by authors like [Joseph Stiglitz](#) and [James Galbraith](#).

Today the dichotomy between efficiency and distribution is no longer tenable. Inequality is becoming an essential theme in economic analysis, for both the short and long terms. To stimulate discussion on this topic, the OFCE and the SKEMA Business School are holding a workshop on “[Inequality and Economic Performance](#)” in Paris on 16 and 17 October 2012.

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# The crisis and market sentiment

By Anne-Laure Delatte

Fundamental factors alone cannot explain the European crisis. A [new OFCE working document](#) shows the impact of market beliefs during this crisis. In this study, we search for where market sentiments are formed and through what channels they are transmitted. What is it that tipped market optimism over into pessimism? Our results indicate that: 1) there is a strong self-fulfilling dynamic in the European crisis: fear of default is precisely what leads to default, and 2) the small market for credit derivatives, credit default swaps (CDS), insurance instruments that were designed to protect against the risk of a borrower's default, is the leading catalyst of market sentiment. This result should be of great concern to the politicians in charge of financial regulation, since the CDS market is opaque and concentrated, two characteristics

that are conducive to abusive behaviour.

What role do investors play during a crisis? If massive sales of securities reveal the weaknesses of a certain business model, then it would be dangerous to limit them: it would be killing the messenger. But if these massive sales are triggered by a sudden turnaround in market sentiment, by investors' panic and distrust of a State, then it is useful to understand how market beliefs are formed so as to better control them when the time comes.

To answer this question in the context of today's European crisis, we have drawn on work on the crisis in the European Monetary System (EMS) in 1992-93, which has many common features with the current situation. At that time investors were skeptical about the credibility of the EMS and put it to the test by speculating against European currencies (*sic*). The pound sterling, the lira, the peseta, etc., were attacked in turn, and governments had to make concessions by devaluing their currency. At first this crisis puzzled economists, as they were unable to explain the link between the speculative attacks and fundamentals: firstly, the countries under attack did not all suffer from the same problems, and secondly, while the economic situation had deteriorated gradually, why had investors decided all of a sudden to attack one currency and not another? Finally, why did these attacks succeed? The answer was that the speculation was not determined solely by the economic situation (the "fundamentals") but was instead self-fulfilling.

The same may well be the case today. If so, then the crisis in Spain, for example, would have its roots in the beliefs of investors: in 2011, as Spain had been designated the weakest link in the euro zone, investors sold their Spanish securities and pushed up borrowing rates. Interest payments ate into the government accounts, and the debt soared. Spain's public deficit will be higher in 2012 than in 2011 despite its considerable austerity efforts. The crisis is self-fulfilling

in that it validates investors' beliefs *a posteriori*.

How could this be proved? How can we test for the presence of a self-fulfilling dynamic in the European crisis? Our proposal is as follows: market beliefs must be a critical variable if, given the same economic situation, investors nevertheless require different interest rates: when the market is optimistic, the difference in interest rates between Germany and Spain is less than when the market is pessimistic.

Our estimates confirm this hypothesis for a panel consisting of Greece, Ireland, Italy, Spain and Portugal: without any significant change in economic conditions, interest rate spreads rose suddenly following a change in the beliefs of the market.

The next question is to understand where these market beliefs are formed. We tested several hypotheses. Ultimately it is the market for credit default swaps (CDS) that plays the role of the catalyst of market sentiments. CDS are insurance products that were originally designed by banks to ensure against the possibility of a borrower's default. An investor who holds bonds may guard against the non-reimbursement of their security at maturity by buying a CDS: the investor then pays a regular premium to the seller, who agrees to repurchase these bonds if the borrower goes bankrupt. But this insurance instrument quickly became an instrument for speculation: the vast majority of operators who buy CDS are not actually owners of an underlying bond (underlying in financial jargon). In reality, they use CDS to bet on the default of the borrower. It is as if the inhabitants of a street all insured the same house, but did not live in it, and are hoping that it catches fire.

However, our results indicate that it is precisely in this market that investors' beliefs vis-à-vis the debt of a sovereign country are formed. In an environment marked by uncertainty and incomplete information, the CDS market

transmits a signal that leads investors to believe that other investors “know something”. Given equivalent economic situations, our estimates indicate that investors require higher interest rates when CDS spreads increase.

To summarize, some European countries are subject to self-fulfilling speculative dynamics. A small insurance market is playing a destabilizing role, because investors believe in the information it provides. This is troubling for two reasons. On the one hand, as we have said, this instrument, the CDS, has become a pure instrument of speculation. On the other hand, it is a market that is unregulated, opaque and concentrated – in other words, all the ingredients for abusive behaviour ... 90% of the transactions are conducted between the world’s 15 largest banks (JP Morgan, Goldman Sachs, Deutsche Bank, etc.). Furthermore, these transactions are OTC, that is to say, not on an organized market, *i.e.* in conditions where it is difficult to monitor what’s going on.

Two avenues of reform were adopted in Europe this year: on the one hand, a prohibition against buying a CDS if you do not own the underlying bond – the law will enter into force in November 2012 throughout the European Union. Second is a requirement to go through an organized market in order to ensure the transparency of transactions. Unfortunately, neither of these reforms is satisfactory. Why? The answer in the next post...

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# How France can improve its trade balance\*

By [Eric Heyer](#)

Prime Minister Jean-Marc Ayrault has made a commitment to restoring France's balance of trade, excluding energy, by the end of his five-year term. Without addressing the curious anomaly of leaving the energy deficit out of the analysis of the country's trade position, as if it did not count in France's dependence on the rest of the world, we will examine the various solutions that the government could use to achieve this goal.

The first solution is to do nothing and to wait until the austerity policy that has been implemented in France through public spending cuts and higher taxes reduces consumer spending. In the face of higher unemployment and the resulting increase in household precautionary savings, the French will cut back on consumption. However, since some of this comes from outside France, this will limit imports into France from abroad and, everything else being equal, improve the country's trade balance.

This solution, it is clear, not only is not virtuous, as it relies on a reduction in employee purchasing power and rising unemployment, but it also has little chance of success, because it assumes that French exports will not follow the same path as imports and will continue to grow. However, since our partner countries are following this same strategy of a rapid return to balanced public finances, their austerity policies will result in the same dynamics as described above for France, thereby reducing their own domestic demand and hence their imports, some of which are our exports.

As a result, and since the austerity programmes of our

partners are more drastic than ours, it is very likely that our exports will decline faster than our imports, thus exacerbating our trade deficit.

The second solution is to increase our exports. In a context where our European partners, who represent 60% of our trade, are experiencing low or even negative growth, this can be achieved only through gains in market share. Lowering the cost of labour seems to be the fastest way to do this. But in the midst of an effort to re-establish a fiscal balance, the only way to lower the charges on labour is to transfer these to another tax: this was the logic of the "social VAT" set up by the previous government, but repealed by the new one, which seems to lean more towards transferring these to the CSG tax, which has the advantage of having a larger tax base, affecting all income, including capital income.

But in addition to the fact that this strategy is not "cooperative", since it resembles a competitive devaluation and thus is essentially aimed at gaining market share from our euro zone partners, there is no indication that it would be sufficient. Indeed, there is nothing to prevent our partners from adopting the same approach, particularly since their economic situation is worse than ours, and this would cancel all or part of any potential gains in our competitiveness.

The last solution consists of making the country more competitive by raising the productivity of our employees and by specialising in high value-added sectors that are not subject to competition from the emerging countries with their low costs.

This is a medium-term strategy and requires the establishment of policies to promote innovation, research and development, and training. It also means expanding the range of our traditional products such as automobiles, but also specializing in the industries of the future.

The need for a transition to an ecological mode of production that is more energy-efficient could represent this industry of the future, and therefore be the solution to our trade deficit.

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\* This text is taken from a series of reports by Eric Heyer for the programme “Les carnets de l'économie” on France Culture radio. It is possible to listen to the series on [France Culture](#).

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## Who will pay the bill in Sicily?

by [Augusto Hasman](#) and Maurizio Iacopetta

Rumors of a Sicily's possible default are in the air again. The employees of the Sicilian parliament did not receive their checks at the end of September. Another possible default of Sicily made already the international headlines in July (see the [New York Times 22/07/12](#)) due to the contagion effects it could have had on other regions. But in that occasion, the central Italian government prevented Sicily's default by providing an immediate injection of liquidity in the order of 400 million euros.

Other Italian regions are in trouble. In recent months the



provision of basic health care services has deteriorated; regions are renegotiating contracts with their creditors to obtain deadline extensions. The [figures](#) reported by Pierre de Gasquet in *Les Echos* of 02/10/2012, give a good idea of the deterioration of the Italian regional public finance over the last decade.

It will take a good deal of imagination for regional governments to come out of the impending budget crisis, not only in Italy but also in other European countries that have difficulties in managing their public debts, such as Spain, Ireland and Greece.

In recent weeks we learned that some local politicians are endowed with a good deal of creativeness, but they hardly use it to find a solution to the budget crises. The governor of the region Lazio –where Rome is located – resigned a few days ago in the midst of a political scandal due to revelations that members of the regional parliament funneled electoral funds to pay extravagant personal expenses, including car upgrades and luxury vacations.

Why don't regional governments issue their own money to finance public expenditures? It may seem absurd that now that European countries have finally accepted a common currency, regional and possibly local governments might be tempted to create some sort of fiat money. But historically it would not be the first time that local monies emerge when the central government has its hands tight.

Argentina in the early 1990s (convertibility law n° 23.928, 27/03/1991) pegged the currency on a one-to-one basis with the U.S. dollar (See Anne-Laure Delatte's [article](#) on this blog for a parallel between the Argentinean events and hypothetical scenarios for Greece.). For most of the decade, things seemed to be working well; the economy was growing at the impressive annual rate of almost 5.7%, notwithstanding (or perhaps thanks to) the fact that Argentina, in practice, gave up the monetary

policy instrument. But by 1998, the load of public debt started to become unbearable. Financing it by printing money was out of question. The IMF was called for help to prevent the panic of Argentinean savers. It granted a loan of 40 thousands million dollars but it also asked the government to impose a severe austerity plan, which had, among many effects, that of depriving provinces under financial difficulties from the prospect of being rescued by the central government.

It was at this point, in 2001, that a number of provinces began to print their own money in order to pay wages and current expenses. (Krugman's open editorial of ten years ago at the New York Times – [Crying with Argentina](#), 01.01. 2002 – gives a fresh reading on the unfolding of the events). Fifteen out of twenty-two provinces ended up using newly issued interest-bearing notes, which earned the name of 'quasi-money'. At the beginning, thanks to an agreement between provinces and large stores, quasi-money had a high level of acceptability. Indeed, competition led more and more stores to accept the quasi-money. Local trade seemed to resuscitate. In August 2002, 5 thousands million pesos of quasi-money circulated side-by-side with 12 thousands million of (real) Argentinean pesos.

Interesting, although the case of Argentina seems very surprising, the academic literature has always been puzzled of why it does not happen more often. The question is why government non-interest bearing banknotes circulate side-by-side with government bonds that promise an interest. In principle the phenomenon defies an elementary no-arbitrage principle.

One of the first to pose the puzzle was Hicks in 1935 in a famous article by the title of 'A suggestion for simplifying the theory of money'. An answer to Hicks' puzzle was offered by [Bryant and Wallace](#) (1980). Their argument is based on observation that private banks are not allowed to slice large denomination government bonds in small denomination banknotes.

If banks could issue their own small denomination notes that are fully backed by large denomination government bonds, then, competition among banks would presumably drive the return on private banknotes in line with the return on bonds. If interest rates on bonds are positive, the argument goes, the demand for non-interest bearing money should then fall to zero. For Bryant and Wallace only the legal restriction on intermediation would prevent this from happening.

But Makinen and Woodward (1986) report that, during the period from 1915 to 1927, French government treasury bonds circulated at a relatively small denomination of 100 Francs (roughly 50-60 euros of today). The bonds were issued with terms of 1 month, 3 months, 6 months, and 1 year. These bonds were continuously available to all banks (including branches of the Bank of France), post offices, and numerous local offices of the Finance Ministry. This historical episode casts some doubts on the legal hypothesis, for the Bank of France kept issuing Francs.

Why then in Argentina bonds emerged as money – albeit for a limited period? It seems to us that the key was the promise offered by the issuer to accept the regional bonds in settling a debt – typically a tax obligation. The rules on what the regions can and cannot do in Europe are different from country to country. In Italy for instance regions, provinces, and municipalities have been authorized to issue bonds by the law of ‘rationalization of public finance’, introduced in the first half of the 1990s (art. 32 of the law of 8.6.1990 n.142, for municipalities and provinces, and art.35, law 23.12.1994 n. 724). The law set several conditions for an administration to qualify to issue bonds. First, bonds can be issued only to finance investment projects. The law explicitly forbids the issue of bonds to finance current expenditures. Second, the issuer has to demonstrate a good history of balanced budgets. Third, the maturity of the bonds cannot be shorter than five years. Fourth, the bonds cannot go in direct competition with

the central government bonds, namely cannot be offered a real return above the one offered by the central government for bonds with similar maturities. Fifth, the central government is not allowed to back-up bonds of the regions who, in turn, cannot take responsibility for the bonds issued by provinces or municipalities

Is it desirable to relax these conditions? Perhaps it is useful to see the end of the story in Argentina –not particularly that of a Hollywood movie. The acceptability of quasi-money outside the region that issued it was very low. More importantly, the central government did not allow tax payers to use quasi-money for their federal taxes. Consequently, in a few months the de-facto exchange rate between the quasi-money and the national currency dropped from 1 to around 0.7 – it was somewhat higher for Buenos Aires quasi-money, for this was accepted in many other provinces.

At the beginning of 2002, a new government, presided by Eduardo Duhalde, decided to abandon the convertibility law. As a result, the exchange rate of the pesos vis-à-vis the U.S. dollar dropped from one to four. During that year, the GDP declined 10.9%.

Having gained the power of printing money again, the central government allowed quasi-monies holders to convert them into the devalued national peso. The short run benefits evaporated soon. The recession along with the depreciation slashed the purchasing power of the working class. At the end of the crisis, the national product was about a quarter lower than its 1998 level, and the rate of unemployment shot up to 24%. It appears that issuing of local money delayed the collapse of the financial system, but it is unclear whether the temporary breath gained by local administrators that issued bonds made the subsequent recession less severe. The case of Argentina suggests, nevertheless, that a major relaxation of the current constraints of regional and municipal entities is not going to help solve how to guarantee the provision of health care

service in the long run. Nonetheless, the current policy of cutting basic public services indiscriminately is the least imaginative of the solutions. Alesina and Giavazzi in an [open editorial](#) published on Corriere della Sera on Sept 27, suggested that hospitals could charge health care users directly instead of being reimbursed by the regional authorities. By doing so, they argued, not only the quality of the service would improve, but regions would need fewer resources. Although this is food for thought, in the U.S. such a system generated a colossal profit making machine that contributed to the explosion of the health care costs. Similarly, Fitoussi and Saraceno (2008) argue that the spectacular gain in income of the last three decades in China did not go hand-in-hand with similar gains in life expectancy and quality of health care, because the government opted for a health care system based on out-of-pocket expenses.

The Argentinean experience tells us that local administrators in distressed regions of Europe are going to lobby the government to give more freedom in managing their budget intertemporally – something that is already happening in Spain, and is summarized in the London School of Economics [blog by K. Basta](#) . They are also probably going to make more intensive use of ‘creative accounting’, so as to prolong their serving time in office. But this will not be the solution. A major reassessment of the national government’s priorities in combination with a sensible monetary policy at the European level is the only way out. We badly need to free up resources to revitalize the public educational system and to maintain the overall good standard of public health care services.

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# France-Germany: The big demographic gap

By [Gérard Cornilleau](#)

The divergence in the demographic trajectories of Germany and France will have a major impact on social spending, labour markets, productive capacity and the sustainability of public debt in the two countries. The implications are crucial in particular for understanding Germany's concern about its debt. These demographic differences will require the implementation of heterogeneous policies in the two countries, meaning that the days of a "one-size-fits-all" approach are over.

The demographic trajectories of France and Germany are the product of Europe's history, and in particular its wars. The superposition of the age pyramids (Figure 1) is instructive in this regard: in Germany the most numerous generations are those born during the Nazi period, up to 1946; then come the cohorts born in the mid-1960s (the children of the generations born under the Nazis). In contrast, in France the 1930s generation is not very numerous. As a consequence, the baby-boomer generation which, as can be easily understood, kicked off earlier than in Germany (starting in 1945, at a time of a baby crash in Germany that ended only in the early 1950s, with the German baby boom peaking somewhat late, in the 1960s), was limited in scale, as people of childbearing age were not numerous. On the other hand, the birth rate in France slowed much less in the wake of the 1970s crisis, and most of all it has risen again since the early 1990s. This has resulted in

the fertility rate remaining close to 2 children per woman of childbearing age, so that the size of the generations from 1947 to the present has remained virtually constant. German reunification led to a collapse in the birth rate in former East Germany, which converged with the rate in ex-West Germany in the mid-2000s (Figure 2). Overall, French fertility has generally been higher than German fertility in the post-war period, with the gap widening since the early 2000s. As a result, the number of births in France is now substantially higher than the number in Germany: in 2011, 828,000 compared with 678,000, *i.e.* 22% more births in France.

**Figure 1. Age pyramids in 2011**

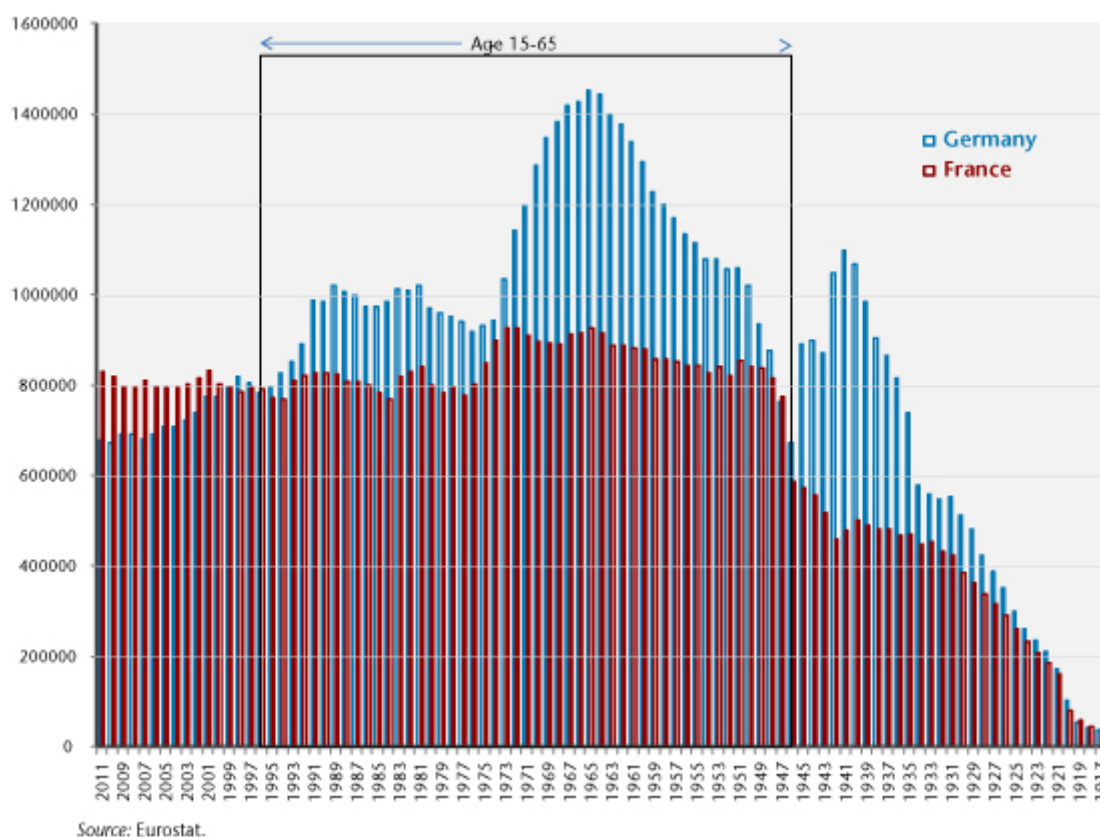
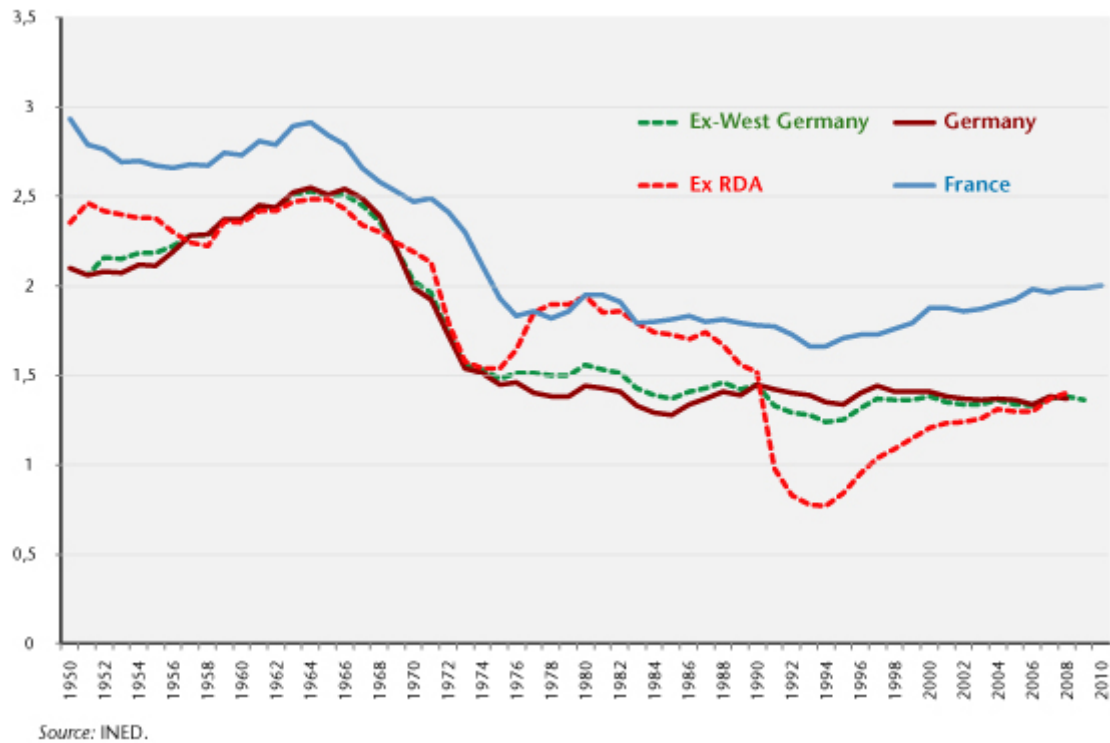




Figure 2. Instantaneous fertility indicators in France and in Germany



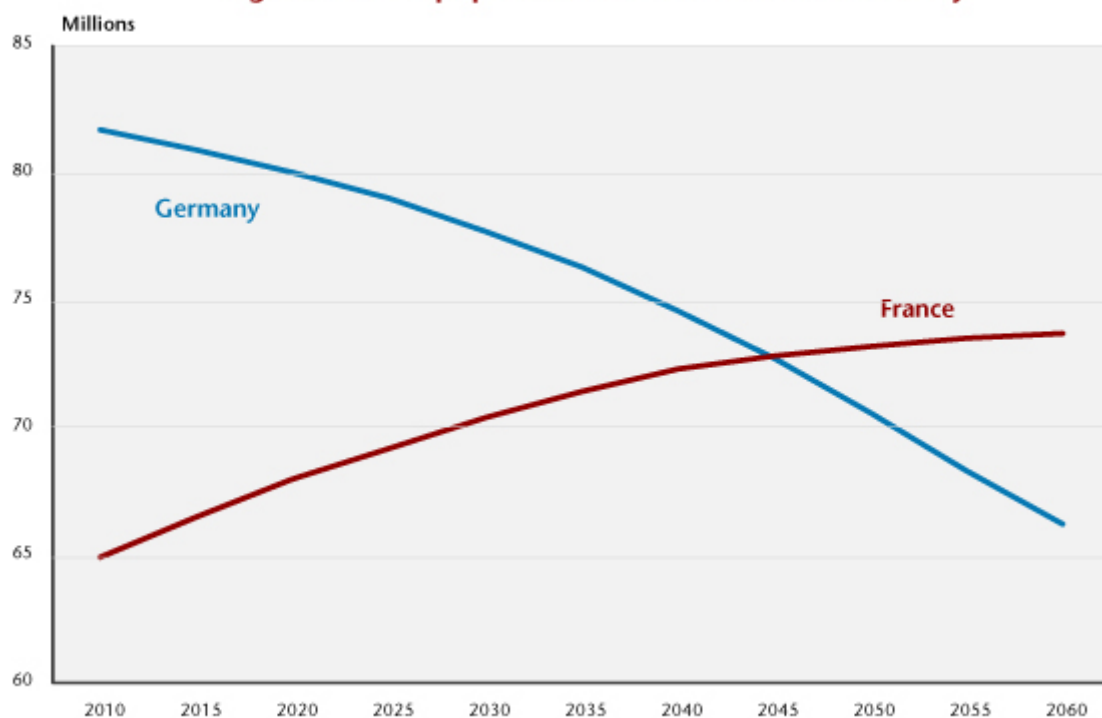
From a demographic standpoint, France and Germany are thus in radically different situations. While France has maintained a satisfactory fertility rate, almost sufficient to ensure the long-term stability of the population, Germany's low birth rate will lead to a substantial and rapid decline in the total population and to much more pronounced ageing than in France (Figures 3 and 4).

According to the population projections adopted by the European Commission [\[1\]](#), Germany should lose more than 15 million inhabitants by 2060, while France gains just under 9 million. By 2045, the populations of the two countries should be the same (a little under 73 million), while in 2060 France will have approximately 7 million more people than Germany (73 million against 66 million).

Migration is contributing to population growth in both countries, but only moderately. Net migration has been lower in Germany during the most recent period, with a rate of 1.87% between 2000 and 2005 and 1.34% between 2005 and 2010 against,

respectively, 2.55% and 1.62% in France [2]. The net migration rates adopted by the European Commission for France and Germany are similar, with a contribution to population increase by 2060 on the order of 6% in each country [3]. The UN [4] uses a similar hypothesis, with the contribution of migration growing steadily weaker in all countries. This reflects a general slowdown in overall international migration due to rising incomes in the originating countries. In this situation, Germany does not seem to have a large pool of external labour available, as it has limited historical links with the main regions of emigration.

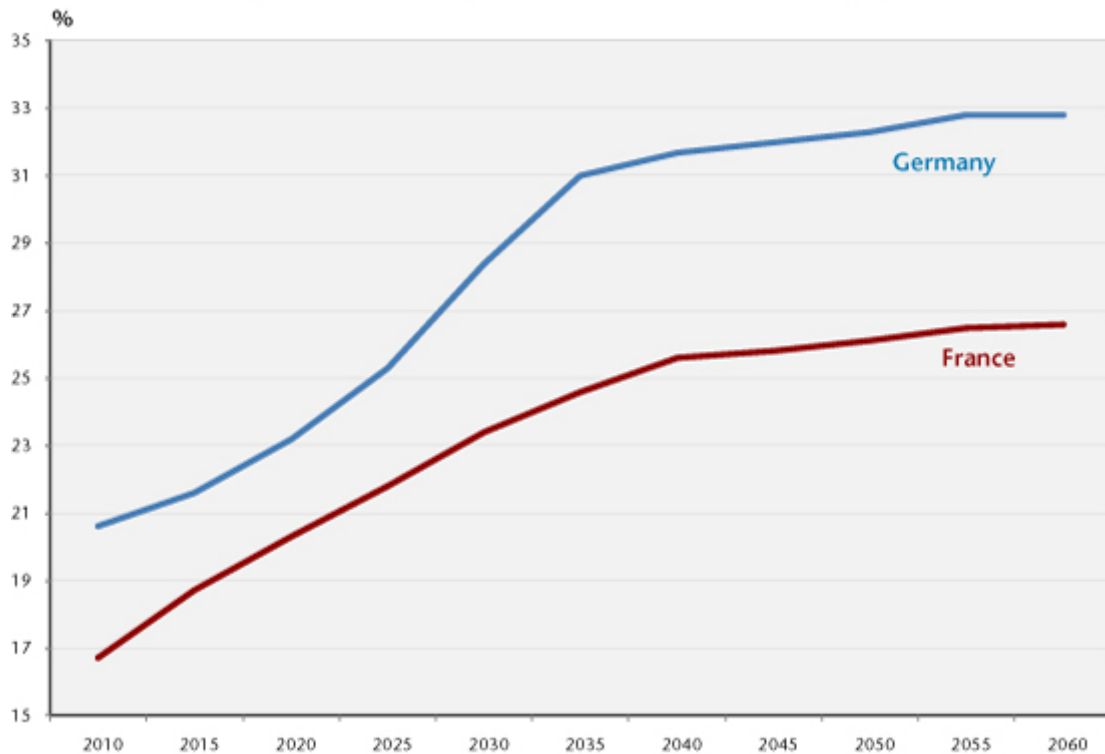
**Figure 3. Total populations in France and in Germany**



Source: European Commission, "The 2012 Ageing Report".

This inversion in demographic weight thus seems inevitable, and it will be accompanied by a divergence in the average age of the population, with considerably more graying of the population in Germany than in France (Figure 4). By 2060, the share in the total population of those aged 65 or older will reach almost one-third in Germany, against a little less than 27% in France.

**Figure 4. Share aged 65 and over in the total population**



Source: European Commission, "The 2012 Ageing Report".

As a consequence, and in light of the reforms implemented in the two countries, the share of GDP that goes to public spending on pensions would increase a little in France and a lot in Germany. According to the Report of the European Commission (*op. cit.*), between 2010 and 2060 this share would rise in France from 14.6% to 15.1% of GDP, up 0.5 GDP point, but by 2.6 points in Germany, from 10.8% to 13.4%. This is despite the fact that the German reform of the pension system provides for postponing the retirement age to 67, while the French reform postpones it only to 62.

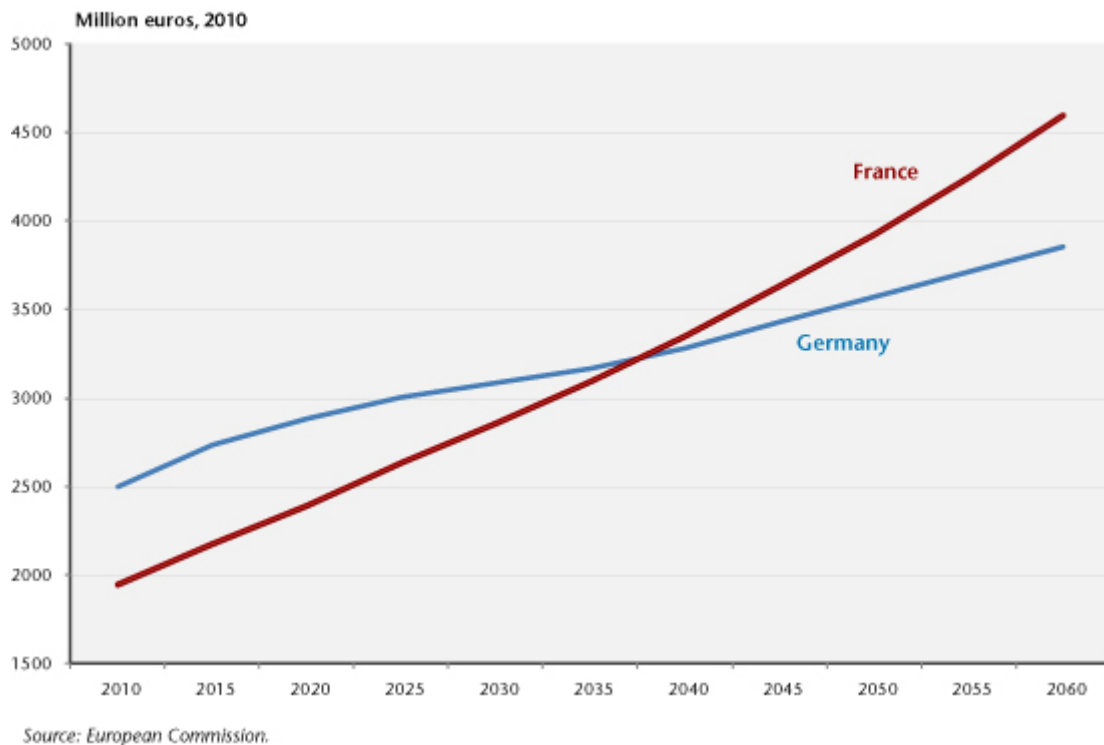
Demography also has an impact on the labour market, which will be subject to changing constraints. Between 2000 and 2011, the French and German workforces increased by the same order of magnitude – +7.1% in Germany and +10.2% in France – but while in Germany two-thirds of this increase resulted from higher labour force participation rates, in France 85% of the increase was due to demography. In the near future, Germany will come up against the difficulties of further increasing its rate. Germany's family policy now includes provisions,

such as parental leave, which aim to encourage female employment through a better reconciliation of work and family life, but female participation rates are already high, so that the problem now is more that of increasing the fertility rate than the labour supply. France, which is starting from a lower participation rate, especially because older workers leave the labour market much earlier than in Germany, has greater reserves to draw on. In recent years, the disappearance of early retirement and the increase in the working years required to receive a full pension have begun to have an impact, with the employment rate of older workers rising significantly, even during the crisis [5]. The employment of older workers has also increased in Germany, but it is not possible to continue to make significant increases in this area indefinitely. The most likely result is a long-term convergence in employment rates between France and Germany. Ultimately, then, according to the projections of the European Commission [6], the German participation rate is likely to increase by 1.7 points between 2010 and 2020 (from 76.7% to 78.4%), while the French rate increases by 2.7 points (from 70.4% to 73.1%). By the year 2060, the French participation rate will increase more than twice as much as the German rate (4.2 points against 2.2). But France's rate would still be lower than Germany's (74.7% against 78.9%), meaning that France would still have reserves to draw on.

This divergence in demographics between the two countries has major consequences in terms of long-term average potential growth. Again according to the projections of the European Commission (which are based on the assumption of a convergence in labour productivity in Europe around an annual growth rate of 1.5%), in the long term potential growth in France will be double the level in Germany: 1.7% per year by 2060, against 0.8%. The difference will remain small until 2015 (1.4% in France and 1.1% in Germany), but will then grow quickly: 1.9% in France in 2020, against 1% in Germany.

Just as for the population figures, this will result in a reversal of the ranking of French and German GDPs by about 2040 (Figure 5).

**Figure 5. GDP in France and in Germany**



The demographic situations of France and Germany thus logically explain why there is more concern in Germany than in France for the outlook on age-related social spending. This should lead to a more nuanced analysis of the countries' public debts: given the same ratios of debt to GDP in 2012, over the long term France's public debt is more sustainable than Germany's.

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[1] Cf. "The 2012 ageing report", *European Economy* 2/1012.

[2] Cf. United Nations, Department of Economic and Social Affairs, Population Division (2011). *World Population Prospects: The 2010 Revision*, CD-ROM Edition.

[3] Net migration is projected to be slightly higher in Germany than in France, at a level of 130,000 per year in 2025-2030, but under 100,000 in France. But the overall

difference is very small: in 2060, cumulative net migration between 2010 and 2060 would increase the population by 6.2% in Germany and by 6% in France (as a percentage of the population in 2010).

[4] *Op. cit.*

[5] See the summary of changes in the labour force in 2011 by the Insee: <http://www.insee.fr/fr/ffc/ipweb/ip1415/ip1415.pdf>

[6] *Op. cit.*

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# Must we choose between saving the planet and exiting the crisis?

By [Xavier Timbeau](#)

It is up to our generation and those that follow to find a way for 10 billion people to live decently and sustainably on a planet with finite resources and capacities. As a decent standard of living requires a mode of consumption closer to that of our Western societies than the deprivation that afflicts a large part of the world's inhabitants, the task is immense – but failure is unacceptable. All this requires us to curb climate change, to anticipate falling agricultural yields, to prepare for the impact of rising sea levels, to adapt, and to halt the destruction of biomass and biodiversity

while taking into account the depletion of natural resources, whether renewable or not. The list of constraints is long, and unfortunately it does not stop with these few examples (the interested reader can profit from reading the [OFCE's previous work](#) on this subject).

Yet the crisis facing the developed countries ([the Great Recession](#)) is often put in opposition to the environmental emergency, suggesting that any ethical concern for integrating human society into the limits imposed by the environment is a luxury that we can no longer afford. As we are obliged either to hope for a return to growth or to prepare the liquidation of our economies, *décroissance*, or de-growth, out of a concern for nature would be an idle fantasy, an option that only the most idealistic – and thus someone freed from the constraints of reality – could take “seriously”. How could societies that are experiencing record rates of unemployment, which need to get back to work in order to absorb the excesses of yesteryear (!), societies threatened moreover by emerging powers that will hasten the decline of anyone who fails to comply with the rules of the new world – how could they allow themselves to become absorbed in saving the planet?

The idea that these two priorities (ending the crisis, saving the planet) have themselves to be prioritized (one realistic, the other idealistic) is a very poor way of addressing the challenge of our times. It can only lead to bad policies, to increasing the future cost of the environmental realism so necessary today and prolonging the economic crisis we are going through again and again. Three arguments are often advanced that lead to neglecting environmental issues in favour of economic issues. These arguments are especially questionable.

The first argument is that the solution to the environmental issue has to be postponed – but it can't be. Indeed, and as an example, the capacity of the global ecosystem to absorb carbon dioxide has long been exceeded. Continuing to emit carbon

because oil is cheaper than other energy sources [\[1\]](#) on the pretext that there is no other choice is a dead end. Every time a gas plant is built (shale or not), it has to be worked (to be profitable) at least 50 years. But after 10 years we will take fright at the level of carbon emissions and realize that climate change is threatening not just our comfort, but the very survival of the human species, and it will be obvious that we must reduce CO2 emissions. So in addition to new investments to change the way we consume energy, it will then be necessary to add the scrapping of the still-unprofitable gas plant. Putting off doing what is needed does not save money – on the contrary, it increases the cost, simply because the environmental constraints cannot be put off. This is currently the diagnosis, for example, even of the [International Energy Agency](#), hardly a den of hard-core ecologists. To stop the planet's climate from heating up by more than 2°C (relative to the pre-industrial era), it is necessary to immediately take the path of reducing CO2 emissions by around 2t of CO2 per year per capita (down to 5 to 10 times less than current emissions in the developed countries). Not doing this today means investing in poor solutions that will have to be mothballed before they have become profitable, and resigning ourselves to limiting the increase in the planet's temperature to 3°C or even more. It therefore means paying more for a worse level of climate stabilization that will then cost even more to adapt. Making the reduction of public debt the priority on behalf of future generations is completely hypocritical if it is done at the expense of future generations. In other words, investing in the decarbonisation of the economy, if it is done well, would have a future social profitability well above interest rates on the public debt. Not doing this means impoverishing future generations. Not doing this because cash constraints prohibit it amounts to a denial that we will not be able to justify to future generations.

The second argument is that we are not rich enough to be able



to save the planet. Complying with environmental requirements and implementing solutions to reduce our impact on the environment would impoverish us, with very few exceptions, at least at first [2]. What was once cheap (e.g. producing energy with reserves accumulated underground over millions of years) would now be done with more work and more infrastructure or capital (and thus more work to produce the capital), and thus in a way that is generally less efficient. Designing products that can be recycled completely, and producing and recycling them so that the materials that compose them can be *indefinitely* reused so as not to tap into the stock of the planet's finite resources, will require more work, more energy (and thus more work) and more capital (and thus more work). Choosing to take the path of respect for the environment thus means less consumption (final consumption, or, if you prefer, fewer services from consumption or a decrease in the flow of material well-being drawn from consumption). But that does not mean a decline in production, or even less a decline in domestic production. Greater concern for the environment will mean a fall in productivity and living standards, but it will also mean job creation (this is the simple corollary). But what happens when jobs are created by reducing productivity in a situation of massive underemployment? It may, though this is not certain, reduce inequality and unemployment. The negative overall effect on income could be compensated for part of the population by the impact on inequality. Since escaping from the rarities of resources (e.g. oil) reduces (or in an extreme case eliminates) the rents associated with those rarities, a reduction in inequality means in particular the primacy of work over property. This is how we can reconcile a reduction in inequality with the environmental transition. Less wealth is consumed, but there is less unemployment, provided that we take the opportunity offered by the environmental transition to reduce inequality, and not just by means of social tariffs but also by the creation of new production.

The third argument frequently advanced is the constraint of

international competition. Since our competitors do not choose to respect the environment, their costs remain low. If we insist on burdening our companies with additional environmental costs (taxes, quotas, standards, right-to-pollute contracts), not only do we lose competitiveness and thereby destroy economic activity and employment, but furthermore, because these activities will be relocated to areas where pollution or CO2 emissions are "authorized", while the environmental degradation will not recur in our country, it will in others, and will thus ultimately increase. In short, the environmental ideal is incompatible with the harsh laws of globalization. Yet it is this argument that is deeply naive and off target, and not the environmental imperative. There are two types of possible answers, both fully compatible with globalization as it is now [little] regulated. The first involves cooperation through applying the same rules on larger and larger spaces. The European Union and its carbon market is one example. This space can be extended, as was tried by the Kyoto Protocol or as is evidenced by the recent cooperation between the European Union and Australia. But such cooperation cannot be established on a stable basis if there is no possibility of coercion. The second possible answer is thus the environmental tax on imports, which is legitimate under the WTO agreements (protection of the environment is one of the few reasons for an exception to the principle of untaxed free trade). It should be noted, for there to be no doubt about the environmental motivation for this, that the proceeds of such import taxes should be redistributed at least in part to the countries sending the imports, or even reserved for environmental investments. This would remove any suspicion that this is a protectionist tax; it would help promote environmental issues in the developing countries; it would provide a concrete response to the notion of the North's ecological debt vis-à-vis the South; and it would be neutral when establishing an environmental tax system or a market for emissions rights in the countries concerned. It would also make it possible to retain an international division of labour

(and the trade flows that go with it), which is a source of productivity and of a better allocation of capital that is still necessary to deal with all the constraints that we need to respect.

The environmental challenge and finding an exit to the crisis are issues that converge, not conflict. The first cannot be postponed without major costs or irreversible damage. The levers to act on the environment must be the same as those that will help put an end to the crisis, in particular because they reduce inequality and increase employment. There is still the issue of the public debt and the need for more manoeuvring room in the future. But submission to cash constraints (“I have to repay my debts right now or I’ll collapse”) amounts to the panic of a rabbit caught in the headlights of the car that is about to crush it. Yet this is exactly the kind of fiscal strategy that we are endeavouring to follow. And it is this that is inconsistent with the concern for future generations and for the environment.

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[\[1\]](#) Just like trying to become a little more competitive by exploiting shale gas because it is twice as cheap as average oil, while in the end, and despite the more advantageous ratio of energy to carbon emitted, it leads to more emissions.

[\[2\]](#) Subsequently, the environmental constraints will stimulate the technical progress that will ultimately raise our overall productivity again.

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# Friends of acronyms, here comes the OMT

By [Jérôme Creel](#) and [Xavier Timbeau](#)

We had the OMD with its Orchestral Manœuvres in the Dark, and now the OMT with its Orchestral Manœuvres in the [liquidity] Trap, or more precisely, “Outright Monetary Transactions”, which is undoubtedly clearer. The OMT is a potentially effective mechanism that gives the European Central Bank (ECB) the means to intervene massively in the euro zone debt crisis so as to limit the differences between interest rates on euro zone government bonds. The possibility that a country that comes into conflict with its peers might leave the euro zone still exists, but if there is a common desire to preserve the euro then the ECB can intervene and play a role comparable to that of the central banks of other major states. Opening this door towards an escape route from the euro zone’s sovereign debt crisis has given rise to great hope. Nevertheless, certain elements, such as conditionality, could quickly pose problems.

The OMT is simply a programme for the buyback of government bonds by the European Central Bank, like SMP 1.0 (the Securities Markets Programme) which it replaces but limited to States that are subject to a European Financial Stability Fund / European Stability Mechanism (EFSF / ESM) programme and thus benefiting from European conditional aid. For the ECB to intervene, the country concerned must first negotiate a macroeconomic adjustment plan with the European Commission and the European Council, and apply it. The ECB, potentially members of the European Parliament or the IMF can be a party to this (these institutions – the Commission, the ECB and the IMF – form the Troika of men in black, so famous and feared in Greece). Secondly, and more importantly, the country will be under the supervision of the Troika thereafter.

So if Italy and Spain want to benefit from the purchase of their bonds by the ECB, then their governments will have to submit to an EFSF or ESM adjustment programme. This does not necessarily imply that the plan imposed will be more drastic in terms of austerity than what these governments might have already devised or implemented (the doctrinaire approach in the management of public finances is highly contagious in Europe), but it will require the two countries to submit *ex ante* to outside scrutiny of any adjustment plan they develop and *ex post* to control by the Commission and the Council. If the country under surveillance starts *ex post* to veer away from implementing the adjustment plan, then it could, of course, withdraw from the programme, but its sovereign bonds would no longer be covered by OMTs. They would lose the support of their peers and would thus sail into the financial markets in uncharted waters. That would probably be the first step towards a default or an exit from the euro.

Furthermore, the ECB has not committed itself to absorbing all the bonds issued and thus maintains a real threat capacity: if the country were to rebel, it could be obliged to face higher rates. The OMT thus introduces both a carrot (lower rates) and a stick (to let the rates rise, sell the bonds the ECB holds in its portfolio and thereby push rates upward), upon each new issue. The OMT is therefore akin to being put under direct control (conditionality) with progressive sanctions and an ultimate threat (exiting the programme).

The ECB says that its interventions will mainly cover medium-term securities (maturity between 1 and 3 years), without excluding longer-term maturities, and with no quantitative limits. Note that short / medium-term emissions *usually* represent a small proportion of total emissions, which tend to be for 10 years. However, in case of a crisis, intervention on short-term maturities provides a breath of fresh air, especially as maturing 10-year securities can be refinanced by 3-year ones. This gives the Troika additional leverage in

terms of conditionality: the OMT commitment on securities is only for three years and must be renewed after three years. The financial relief for countries subject to the programme may be significant in the short term. For example, in 2012 Spain, which has not yet taken this step, will have issued around 180 billion euros of debt. If the OMT had reduced Spain's sovereign borrowing rates throughout 2012, the gain would have amounted to between 7 and 9 billion for the year (and this could be repeated in 2013 and 2014, at least). This is because, instead of a 10-year rate of 7%, Spain could be benefitting from the 2% rate at which France borrows for 10 years, or instead of its 4.3% rate at 3 years, Spain could have borrowed at 0.3% (France's 3-year sovereign rate). This is the maximum gain that can be expected from this programme, but it is significant: this roughly represents the equivalent of the budgetary impact of the recent VAT hike in Spain (or a little less than one Spanish GDP point). This would not alter Spain's fiscal situation definitively, but it would end the complete nonsense that saw Spaniards paying much more for their debt to compensate their creditors for a default that they have been striving arduously not to trigger.

It can even be hoped (as can be seen in the easing of Spanish sovereign rates by almost one point following the ECB announcement on Thursday, 6 September 2012, or the almost half a point reduction in Italian rates) that the mere existence of this mechanism, even if Spain or Italy do not use it (and thus do not submit to control), will be enough to reassure the markets, to convince them that there will be no default or exit from the euro and therefore no justification for a risk premium.

The ECB announced that it would terminate its preferred creditor status for the securities. This provision, which had been intended to reduce the risk to the ECB, led to downgrading the quality of securities held outside the ECB and thus reducing the impact of ECB interventions on rates. By

acquiring a government bond, the ECB shifted the risk onto the bonds held by the private sector, since in case of a default the Bank was a preferred creditor that took priority over private holders of bonds of the same type.

The ECB explained that its OMT operations will be fully sterilized (the impact on the liquidity in circulation will be neutral), which, if it is taken at its word, implies that other types of operations (purchases of private securities, lending to banks) will be reduced correspondingly. What do we make of this? The example of the SMP 1.0 can be drawn on in this regard. SMP 1.0 was indeed also accompanied by sterilization. This sterilization involved short-term deposits (1 week, on the ECB's liabilities side), allocated in an amount equal to the sums involved in the SMP (209 billion euros to date, on the ECB's assets side). Each week, the ECB therefore collects 209 billion euros in short-term fixed-term deposits. This is therefore a portion of bank deposits that the ECB assigns to the sterilization instrument, without there being sterilization in the strict sense (because this does not prevent an increase in the size of the ECB's balance sheet nor does it reduce the potential liquidity in circulation). The mention of sterilization in the OMT appears to be an effort at presenting this in a way that can convince certain states, such as Germany, that this monetary policy will not be inflationary and therefore not contrary to the mandate imposed on the Bank by the Treaty on the European Union. Currently, and because the crisis remains unresolved, private banks have substantial deposits with the ECB (out of fear of entrusting these deposits to other financial institutions), which gives it considerable flexibility to prevent the announced sterilization from affecting the liquidity in circulation (the ECB has a little more than 300 billion euros in deposits that are not mobilized for sterilization). The ECB can then probably use the current accounts (by blocking them for a week), which poses no difficulty since the ECB lends to the banks on tap through long-term refinancing operations (LTROs).

At worst, the ECB would lose money in the sterilization operation in case of a gap in compensation between the fixed-term deposits and the loans granted to banks. Sterilization could therefore lead to this kind of absurd accounting, but wind up, in a situation of monetary and financial crisis, having no impact on liquidity. On the other hand, if the situation normalizes, the constraint of sterilization would weigh more heavily. We're not there yet, but when we do get there, the ECB needs to limit lending to the economy or to accept an increase in liquidity if the OMT continues to be implemented for some euro zone members.

The deal that is now on the table places the euro zone countries in a formidable dilemma. On the one hand, acceptance of the Treaty on Stability, Coordination and Governance of the euro zone (TSCG) determines eligibility for the EFSF and the ESM [\[1\]](#), and therefore now determines eligibility for the OMT programme. Refusing to sign the fiscal treaty means rejecting in advance the potential intervention of the ECB, and thus accepting that the crisis continues until the breakup of the euro zone or until a catastrophic default on a sovereign debt. On the other hand, signing the treaty means accepting the principle of an indiscriminately restrictive fiscal strategy (the rule on public debt reduction included in the TSCG will be devastating) that will trigger a recession in the euro zone in 2012 and perhaps in 2013.

Signing the treaty also means relieving the pressure of the markets, but only to wind up submitting solely to the Troika and to the baseless belief that the fiscal multipliers are low, that European households are Ricardian and that the sovereign debt is still holding back growth. It is true that lowering sovereign interest rates, particularly those of Italy and Spain, will create some breathing room. But the main gain from lower rates would be to spread the fiscal consolidation over a longer period of time. Interest rates place a value on time, and reducing them means granting more time. The debts



contracted at negative real interest rates are not ordinary debts, and do not represent the same kind of burden as debts issued at prohibitively high rates.

It would be a terrible waste to gain new maneuvering room (the OMT) only to bind one's hands immediately (the TSCG and the Troika's blind fiscal strategy). Only a change in fiscal strategy would make it possible to take advantage of the door opened by the ECB. In short, saving the euro will not help if we do not first save the EU from the disastrous social consequences of fiscal blindness.

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[\[1\]](#) Paragraph 5 of the preamble to the Treaty establishing the European Stability Mechanism states: "This Treaty and the TSCG are complementary in fostering fiscal responsibility and solidarity within the economic and monetary union. It is acknowledged and agreed that the granting of financial assistance in the framework of new programmes under the ESM will be conditional, as of 1 March 2013, on the ratification of the TSCG by the ESM Member concerned and, upon expiration of the transposition period referred to in Article 3(2) TSCG on compliance with the requirements of that article."

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**The crisis in the automobile industry: shortcomings**                      **strategic shouldn't**

# conceal the impact of fiscal austerity

By [Jean-Luc Gaffard](#)

The crisis in the automobile industry, illustrated by the closure of the PSA site in Aulnay, reveals not only structural difficulties but also strategic errors made by the manufacturers with respect to their industrial organization and range positioning. The industry's need to restructure cannot, however, obscure the very real macroeconomic dimensions of the crisis in the short term.

New car registrations in France fell 15.5% in July on an annual basis, after adjusting for working days. In the first seven months of the year, the decline in the automotive market stood at 13.5% in unadjusted data and 14.1% in adjusted data. PSA was down 9.9% in July in terms of unadjusted data. The Renault group has seen its share of registrations fall by 11.2%, with a drop of 26.6% for the Renault brand but a near doubling of registrations for the low-cost Dacia brand. Also in July, the decline in new car sales in Spain accelerated, with a drop of 17.2%. In Italy, new car registrations plummeted 21.4%. Finally, while German production increased by 5% due to exports, new car registrations there fell by 5%.

These catastrophic figures are first and foremost the result of the collapse of aggregate demand in the countries of the European Union as a result of falling revenues combined with greater inequality in distribution. The middle class is maintaining or increasing its savings rate and either deferring purchases in time or buying lower-cost products, particularly cars, while at the same time the increase in inequality has led to growth in the market for luxury vehicles, particularly in Europe and China.

It is not surprising, in this context, that PSA, which has a mid-range positioning, recorded a fall in sales and that Renault limited the damage only thanks to sales of its low-cost brand. Nor is it surprising to see strong growth for the Asian brands, Korean in particular, which are also positioned on the low-cost segment. Finally, it is not surprising that German manufacturers racked up exceptional results, as they are strongly positioned on the top of the range: BMW, Audi and Porsche recorded sales increases in the first half-year of 8%, 22.5% and 12.3%, respectively.

This state of affairs cannot of course absolve manufacturers of their strategic responsibilities, but it should lead the government to prioritize the underlying causes and, even more, to take the measure of what is needed in the short term, even while it continues to provide long-term support for the industry.

Nobody can doubt the relevance and effectiveness of the strategy adopted by Germany's firms, which is based on the international fragmentation of their production process, the conservation and development in the home country of their technological capacity and a better analysis of market expectations in the emerging economies, first of all China. This strategy proved to be especially successful as competitive devaluations became impossible with the advent of the single currency, an impossibility that has wound up exposing the errors in the positioning of their French competitors, including PSA, in light of the reality of global markets. The intensified rivalry between firms due to the steady weakening in European domestic demand, which has recently accelerated, could only lead to widening gaps in performance in terms of sales volumes, market share and ultimately profit margins.

There is certainly no question but that the future of the French automobile industry requires a substantial effort at organizational and technological innovation together with the

internationalization of production and the strengthening of local production relationships, as well as a search for market niches to make competition less price-sensitive. Public measures aimed at strengthening the production network through a site policy and support for outsourcing respond to this strategic challenge. The emphasis on the development of electric and hybrid vehicles is, however, questionable. The electric vehicle market could well remain marginal, and this will not change as a result of heavily subsidized prices to boost sales among specific urban groups. As for the market for hybrid vehicles, this is still limited in volume, and foreign (Japanese) competition already has a solid footing. Shouldn't we worry about the fate of mid-range vehicles: while their market is clearly suffering from the crisis in Europe, might it not thrive in Europe as it emerges from the crisis and even develop in the emerging economies as a genuine middle class emerges there? In other words, a productive recovery in the automotive sector, while it must involve improvements in quality, is still a matter of demand – and demand needs to be considered at a global level, with as a consequence the corresponding strategic choices concerning the location and segmentation of production activities.

In any event, a recovery in production in one direction or another will take time, and time is likely to be lacking if in the short term there is no pick-up in demand. In other words, the immediate problem is as much if not more macroeconomic rather than microeconomic. The surest way to bury the French automotive industry, thus losing an important accumulation of human capital, is to pursue a fiscal austerity policy that merely depresses demand without addressing the issue of sovereign debt.

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# The situation on the labour market in France\*

By [Eric Heyer](#)

The French economy is facing a number of imbalances, with the two main ones being:

- a public deficit that at end 2012 is likely to come to about 4.5 GDP points, or close to 100 billion euros;
- a lack of jobs, which is leading to mass unemployment.

While the first point is the object of great attention, and while it has been and remains the main or even the sole concern of every EU summit over the last three years and is at the heart of the European strategy on the crisis, it must be acknowledged that this is not unfortunately the case for the second point. However, it is not unreasonable to ask whether the priority in a country as rich as France should actually be to reduce the deficit at all costs even if this may worsen the plight of society's most vulnerable and make it more difficult for them to access the labour market.

Since the beginning of the crisis in early 2008, the French economy has destroyed more than 300,000 jobs, and the number of unemployed as defined by the International Labour Office has increased by 755,000. More than 2,700,000 French are now without jobs, i.e. 9.6% of the active population.

And this figure undoubtedly underestimates the real situation. The French economy is currently creating only mini part-time jobs that don't last long; in the last quarter, 4.5 million job contracts were signed: 3 out of 4 of these were contracts

lasting less than one month (mostly 1 day to 1 week). Someone who signed one of these contracts and is looking for a job at the end of the same month is not counted as unemployed. Their inclusion would increase the jobless numbers and push the French economy a little further into mass unemployment.

Moreover, and this is more disturbing, the unemployed are getting older while remaining jobless – the number of long-term unemployed is continuing to shoot upwards – and thereby lose out in terms of both job skills and financially as they shift from unemployment benefits onto the social minima; in a study we conducted at OFCE for the National Observatory on Poverty and Social Exclusion (ONPES), we estimated that in France 100 additional unemployed during this crisis will lead to 45 more people in poverty in 2012. Thus, even stabilizing unemployment would not lead to halting the deterioration of people's situation – on the contrary.

It is therefore urgent to reverse current trends with respect to employment and unemployment.

The surest way to do this is to put the French economy onto a trajectory of dynamic growth: recall that low but positive growth is not enough for the French economy to create jobs again, as, given gains in productivity, the country's economy needs to grow by more than 1% in order to unleash a spiral of job creation. Moreover, given the continuation of demographic growth and the postponement of the retirement age, the labour force is increasing by 150,000 people every year. It is thus necessary to create more than 150,000 jobs in France before unemployment will begin to fall, which corresponds to growth of over 1.5%.

However, in light of the austerity policies being implemented in France and by our European partners, this level of growth seems unthinkable in 2012 and 2013.

So how can a further explosion of unemployment be stopped in

the near future?

The first step would be to change Europe's strategy by establishing, among other things, a "more moderate" austerity.

The second step would be to adopt the strategy Germany is using for the crisis, that is to say, to reduce working time by massively resorting to part-time work and to partial unemployment schemes. Remember that 35% of German employees are hired part-time, as against 17% in France. Furthermore, during the crisis 1.6 million Germans have been on a partial unemployment programme, compared with 235,000 in France. All this has helped Germany to keep unemployment down during the crisis.

The last solution is to use what in France is called the "social treatment of unemployment". As the private sector is still destroying jobs, the public sector would offset part of this by creating subsidized jobs.

The government seems to be taking this last path: 100,000 "jobs for the future" will be created in 2013 and 50,000 in 2014.

In the short term, given the economic situation, this strategy seems to be the most effective and the least expensive. However, in the medium term, it cannot replace a policy of growth.

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\* This text is taken from a series of reports by Eric Heyer for the programme "Les carnets de l'économie" on France Culture radio. It is possible to listen to the series on [France Culture](#).

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# Youth “jobs of the future”: What impact on employment and government finances?

[Éric Heyer](#) and [Mathieu Plane](#)

The bill aimed at creating 150,000 “jobs for the future” [*emplois d’avenir*] for unemployed youth will be submitted to Parliament in October 2012. These 150,000 “jobs for the future” are to be reserved primarily for young people from deprived areas. What will be the net impact on employment and public finances?

These full-time jobs, which are planned to last a maximum of five years and are paid at least the minimum wage (SMIC), will be 75% funded by the State, with the rest of the cost being borne by local authorities, associations, foundations and business. According to the Minister of Labour and Employment, Michel Sapin, the goal is to create 100,000 jobs starting in 2013.

## ***The ex-ante cost of the measure***

The gross annual cost of a “jobs for the future” contract paid at the SMIC on the basis of a 35-hour full-time week is 24,807 euros. The cost per job for the public finances is 12,831 euros for 75% of the gross wage and 4,807 euros for the exemption from employer social contributions. To this should be added the remaining cost for the employer, or 7,276 euros, when the employer is not a public entity. Based on the assumption that two-thirds of the “jobs for the future” created would be in the non-market sector and one-third in the market sector, the total average annual cost for the public



finances therefore comes to 23,015 euros per contract. When fully implemented, the cost of creating 150,000 “jobs for the future” is estimated at 3.45 billion euros a year.

### ***The impact of the measure***

By assuming the creation of 100,000 subsidized jobs in the non-market sector and 50,000 in the market sector, the impact would be as follows:

With relatively weak deadweight and substitution effects in the non-market sector (20% according to Fontaine and Malherbet, 2012), 100,000 “jobs for the future” would lead to the net creation of 80,000 jobs over the presidential term. The *ex-ante* annual cost to the public finances for 100,000 “jobs for the future” in the non-market sector would be 0.12 GDP point, but *ex post* this would be only 0.07 GDP point because of the extra income – and thus tax and social security revenue – generated by the jobs created.

The state aid (75% of the gross salary) allows a reduction in the cost of labour of 52% at the SMIC level, *i.e.* a total reduction of 71% of the actual cost of a minimum wage job if one includes the reductions in charges. With the impact of employment elasticities at a maximum labour cost at the level of the SMIC (1.2 according to a DGTPE study in 2007), the 50,000 “jobs of the future” in the market sector would generate 27,300 jobs. The *ex-ante* cost to the public finances would be 0.05 GDP point, and 0.03 GDP point *ex post*.

Ultimately, the measure would eventually create 107,300 jobs (about 25% of these in the market sector), *i.e.* an annual net creation of 72%. The *ex-ante* cost for the public finances would be 0.17 GDP point, but the *ex-post* impact of the measure on the public balance would be only -0.1 GDP point because of the extra tax and social security revenue generated by the jobs created and the consequent income gains (Table 1).

**Table 1. Impact at 5 years of the measure on employment and the public finances**

Création of...	Jobs (1 000)	Net creation (%)	<i>Ex ante</i> public balance (in GDP points)	<i>Ex post</i> public balance (in GDP points)
... 100,000 in the non-market sector	80 000	80 %	0.12	0.07
50,000 in the non-market sector	27 300	55 %	0.05	0.03
<b>Total (150,000 jobs for the future)</b>	<b>107 300</b>	<b>72 %</b>	<b>0.17</b>	<b>0.10</b>

Source : OFCE calculations.

According to statements by the Minister of Labour and Employment, two-thirds of the “jobs for the future” will be set up in 2013. To assess the impact of this measure over the presidential term, we started from the assumption that 25,000 full-time “jobs for the future” with a term of 5 years would be created each quarter from the beginning of 2013 until mid-2014.

Based on this profile for the implementation of the “jobs for the future”, the net new job creation expected in 2013 would be 71,600, with 35,700 in 2014, and then 0 from 2015 to 2017. The *ex-post* impact on the public balance would be 0.04 GDP point in 2013 and 0.06 point in 2014, *i.e.* a cumulative impact on the public finances of 0.1 GDP point over time.

**Table 2. Impact of the measure on employment and the public finances from 2013 to 2017**

	2013	2014	2015	2016	2017
Jobs for the future (1000s)	100 000	50 000	0	0	0
Net job creation (1000s)	71 600	35 700	0	0	0
<i>Ex-ante</i> annual cost (billion euros)	1.44	3.31	3.45	3.45	3.45
<i>Ex ante</i> impact on public balance (GDP pts)	0.07	0.09	0.01	0.00	0.00
<i>Ex post</i> impact on public balance (GDP pts)	0.04	0.06	0.00	0.00	0.00

Source : OFCE calculations.

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