

An ever so fragile recovery

By the Department of Analysis and Forecasting, under the direction of [Eric Heyer](#) and [Xavier Timbeau](#)

This text summarizes the OFCE's [economic forecast for 2015-2017](#) for the euro zone and the rest of the world.

The figures for euro zone growth in the first half of 2015 have confirmed the upswing glimpsed at the end of 2014. While the zone's return to growth might once have been taken to indicate the end of the global economic and financial crisis that struck in 2008, the turbulence hitting the emerging countries, particularly over the summer in China, is a reminder that the crisis ultimately seems to be continuing. China's economic weight and its role in world trade are now so substantial that, even in the case of a soft landing, the impact on growth in the developed countries would be significant. We nevertheless anticipate that the scenario for a recovery need not be called into question, and that euro zone growth will be broadly supported by favourable factors (lower oil prices and ECB monetary support) and by some weakening of unfavourable factors (easing of fiscal policies). But the fact remains that the situation in the developing world will add new uncertainty to an already fragile recovery.

Between 2012 and 2014, the euro zone economies stagnated at the very time that the United States turned in average GDP growth of 2%. The recovery that got underway after the sharp contraction in 2008-2009 was quickly cut short in the euro zone by the sovereign debt crisis, which led almost immediately to the uncontrolled tightening of financial conditions and the reinforcement of the fiscal consolidation being implemented in the Member States, as they searched for market credibility.

The euro zone then plunged into a new recession. In 2015,

these economic policy shocks are no longer weighing on demand. The ECB helped to reduce sovereign debt risk premiums by announcing the Outright Monetary Transaction programme (OMT) in September 2012 and then by implementing quantitative easing so as to improve financial conditions and promote a fall in the euro. In terms of fiscal policy, while in some countries the consolidation phase is far from over, the measures being taken are smaller in scale and frequency. Furthermore, growth will also be helped by the fall in oil prices, which should last, and the resulting gains in household purchasing power should in turn fuel private consumption. These factors thus reflect an environment that is much more favourable and propitious for growth.

However, it is clear that this scenario depends on some volatile elements, such as the fall in oil prices and the weaker euro. The Chinese slowdown adds another element of risk to the scenario, which is based on the assumption that China will make a smooth transition from an export-oriented growth model to one driven by domestic demand. We expect the euro zone to grow at a rate of 1.5% in 2015 and 1.8% in 2016 and 2017. The main short-term risks to this scenario are negative. If oil prices go up and the euro doesn't stay down, and if the slowdown in the emerging countries turns into an economic and financial crisis, then growth worldwide and in the euro zone will be significantly lower. This risk is particularly critical given the very high level of unemployment still plaguing the zone (11% in August 2015). Nevertheless, given the pace of anticipated growth, we expect the unemployment rate to fall in 2016-2017 by around 0.6 percentage point per year. At this pace, it will take almost seven years to bring the rate back to its pre-crisis level. So while the prospects for recovery from the 2008 crisis are uncertain, the social crisis undoubtedly has a long time to run.

Investing in the zero carbon economy in order to escape secular stagnation

By [Xavier Timbeau](#)

What the downward revisions of various forecasts ([IMF](#), [OECD](#), [OFCE](#)) presented in early autumn 2015 tell us about the euro zone is not very comforting. A recovery is underway, but it is both sluggish and fragile (see: "[A very fragile recovery](#)"). The unemployment rate in the euro zone is still very high (almost 11% of the labour force in the second quarter), and a sluggish recovery means such a slow fall (0.6 point per year) that it will take more than seven years to return to the 2007 level. Meanwhile, the European Central Bank's unconventional monetary policy is having difficulty re-anchoring inflation expectations. The announcement of quantitative easing in early 2015 pushed up the 5-year/5-year forward inflation rate [\[1\]](#), but since July 2015 the soufflé has collapsed once again and medium-term expectations are 0.8% per year, below the ECB target (2% per year). Underlying inflation has settled in at a low level ([0.9% per year](#)), and there is a high risk that the euro zone will be frozen in a state of low inflation or deflation, strangely resembling what Japan has experienced from the mid-1990s to today. Low inflation is not good news because it is triggered by high unemployment and slowly rising nominal wages. The result is real wages growing more slowly than productivity. Little or no inflation means both real interest rates that remain high, which increases the burden of debt and paralyzes investment, but also an unconventional monetary policy that undermines the ability to measure risks and which gradually loses its

credibility for maintaining price stability, i.e. to keep inflation within declared targets. At the [Jackson Hole Symposium](#) in August 2014, Mario Draghi announced that, in the face of persistent unemployment, monetary policy cannot do everything. Structural reforms are necessary (what else could a central banker say?). But a demand policy is also needed. Not having one means [running the risk of secular stagnation](#), as was formulated by Hansen in the late 1930s and recently brought up to date by Larry Summers.

Europe does not, however, lack investment opportunities. The [COP21 commitments](#), though timid, assume a reduction in CO₂ emissions (equivalent) per capita from 9 tons to 6 tons within 15 years, and investment will need to pick up pace in a big way if the change in global temperature is not to exceed 2°C. This means aiming to put an end to the use of petroleum and coal (or the large-scale development of carbon capture and storage) within 35 years. Achieving this will require investment on a massive scale, which is estimated in the [European Commission's Energy Road Map](#) at over 260 billion euros (nearly 2% of GDP) per year by 2050. The social profitability of such investments is substantial (since it helps to avoid climate catastrophe and makes it possible to meet the EU's commitments to the world's other countries), but – and this is the problem posed by our sluggish recovery – their private profitability is low, and uncertainty about future demand together with poor coordination could give pause to the “animal spirits” of our entrepreneurs. Secular stagnation results from the very low profitability of investments, particularly after taking into account the real rates anticipated and the risk of a more serious depression. To avoid this trap, the social returns on investment in a zero carbon economy need to become evident to all, and in particular they need to coincide with private returns. There are numerous tools that can do this. We can use carbon pricing and markets for trading in emission rights; we can use a carbon tax; we can develop certificates for new investments

(assuming we know how to ensure that they reduce CO2 emissions compared to an opposing counterfactual) or impose standards (if these are followed!). The difficulties of the transition and the acceptance of a relatively painful change in prices can be eased by compensatory measures (which have a budgetary cost, [see Chapter 4 of the IAGS 2015 report](#), but are part of the stimulation package). It might also be desirable to draw on monetary policy to amplify the stimulus (see [this proposal by Michel Aglietta and Etienne Spain](#)). The implementation of artillery like this to reduce emissions and boost the European economy is not straightforward and would require wrenching the institutional framework. But that's the price to pay in order to avoid sinking into a long period of stagnation which, with the inequalities and impoverishment that it would generate, would certainly break up the European project.

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Lower taxation on business but higher on households

By [Mathieu Plane](#) and Raul Sampognaro

Following the delivery of the Gallois Report in November 2012, the government decided at the beginning of Francois Hollande's five-year term to give priority to reducing the tax burden on business. But since 2015, the President of the Republic seems to have entered a new phase of his term by pursuing the objective of reducing the tax burden on households. This was seen in the elimination of the lowest income tax bracket and the development of a new allowance mechanism that mitigates tax progressivity at the lower levels of income tax. But more

broadly, what can be said about the evolution of the compulsory tax burden on households and businesses in 2015 and 2016, as well as over the longer term?

Based on data provided by the INSEE, we have broken down trends in the tax burden since 2001, distinguishing between levies on companies and those on households (Figure). While this is purely an accounting analysis and is not based on the final fiscal impact, it nonetheless gives a view of the breakdown of the tax burden [1]. In particular, this exercise seeks to identify the tax burden by the nature of the direct payer, assuming constant wages and prices (excluding tax). This accounting breakdown does not therefore take into account macroeconomic feedback and does not address the distributional and intergenerational impacts [2] of taxation.

For the period from 2001 to 2014, the data is known and recorded. They are *ex post* and incorporate both the effects of the discretionary measures passed but also the impact of fiscal gains and shortfalls that are sensitive to the business cycle. However, for 2015 and 2016, the changes in the tax burden for households and businesses are *ex ante*, that is to say, they are based solely on the discretionary measures that have an impact in 2015 and 2016 and calculated in the Social, Economic and Financial Report of the 2016 Finance Bill for 2016 [[Rapport économique social et financier du Projet de loi de finances pour 2016](#)]. They therefore do not, for both years, include [potential effects related to variations in tax elasticities that could modify the apparent tax burden rates](#). Furthermore, under the new accounting standards of the European System of Accounts (ESA) tax credits, such as the CICE, are considered here as reductions in the tax burden, and not as a public expenditure. Furthermore, the CICE tax credit is recognized at the tax burden level in terms of actual payments and not on an accrual basis.

Several major points emerge from this analysis of the recent period. First, tax rates rose sharply in the period 2010-2013,

representing an increase of 3.7 percentage points of GDP, [with 2.4 points borne by consumers and 1.3 by business](#). Over this period, fiscal austerity was relatively balanced between households and business, with the two experiencing a tax increase that was more or less proportional to their respective weights in the tax burden [\[3\]](#).

However, from 2014 a decoupling arose between the trends in the tax burdens for households and for business, which is continuing in 2015 and 2016. Indeed, in 2014, due to the impact of the CICE tax credit (6.4 billion euros, or 0.3 percent of GDP), the tax burden on business began to decline (by 0.2 GDP point), while the burden on households continued to rise (by 0.4 GDP point), mainly because of the hike in VAT (5.4 billion), the increase in environmental taxes (0.3 billion with the introduction of the carbon tax) and the increase in the contribution to the public electricity service (CSPE) (1.1 billion), together with the increase in social contributions for households (2.4 billion), mainly due to the rise in contribution rates to the general and complementary social security scheme and the gradual alignment of rates for civil servant with those for private-sector employees.

In 2015, the tax burden on business will fall by 9.7 billion euros (0.5 GDP point) with the implementation of the CICE tax credit (6 billion), the first Responsibility Pact measures (5.9 billion related to the first tranche of reductions in employer social security contributions, an allowance on the C3S tax base and a "*suramortissement*", an additional tax reduction, on investment), while other measures, such as those related to pension reform, are increasing corporate taxation (1.7 billion in total). Conversely, the tax burden on households should increase in 2015 by 4.5 billion (0.2 GDP point), despite the elimination of the lowest income tax bracket (-2.8 billion) and the reduction in self-employed contributions (-1 billion). The hike in the ecological tax (carbon tax and TICPE energy tax) and the CSPE together with

the non-renewal in 2015 of the exceptional income tax reductions of 2014 represent an increase in taxation on households of, respectively, 3.7 and 1.3 billion. Other measures, such as those affecting the rates of contributions to general, supplemental and civil servant pension schemes (1.2 billion), along with local taxation (1.2 billion), including the modification of the DMT0 tax ceiling and measures affecting tourist and parking taxes, are also raising taxes on households.

Table. Measures affecting household and corporate tax burdens - 2015 and 2016

In billion euros

	2015	2016
HOUSEHOLDS		
Income tax cut for low-income households	-2,8	-2,0
Ecology taxes + TICPE + CSPE	3,7	2,7
Change in VAT	0,5	-0,2
Local taxes	1,3	1,1
Elimination of PPE working tax credit		2,0
Old-age and CSA community autonomy tax	0,5	0,8
Other changes to social security contributions	0,8	0,1
Other measures	1,9	0,2
Reduction in self-employed contributions (Responsibility Pact)	-1,0	
Fight against tax fraud and avoidance	-0,4	-0,6
Total of measures affecting household tax burden	4,5	4,1
Total excluding fight against tax fraud and avoidance	4,9	4,7
BUSINESS		
CICE tax credit	-6,0	-0,3
C3S allowance (Responsibility Pact)	-1,0	-1,0
Elimination of exceptional IS corporate income tax (Responsibility Pact)		-2,3
Tax reduction on investments	-4,5	-3,5
Other measures affecting social security contributions	-0,4	-0,2
Other social contributions measures	1,1	1,0
Other measures	0,9	0,9
Fight against tax fraud and avoidance	0,2	-0,5
Total of measures affecting corporate tax burden	-9,7	-5,9
Total excluding fight against tax fraud and avoidance	-9,9	-5,4

Sources: PLF (Finance Act) 2016; OFCE calculations.

In 2016, the tax burden on business will fall by 5.9 billion (0.3 GDP point), mainly due to the second phase of the Responsibility Pact. Reductions in employer social security contributions on wages lying between 1.6 and 3.5 times the SMIC minimum wage (3.1 billion), the elimination of the corporate income tax (IS) surcharge (2.3 billion), the second

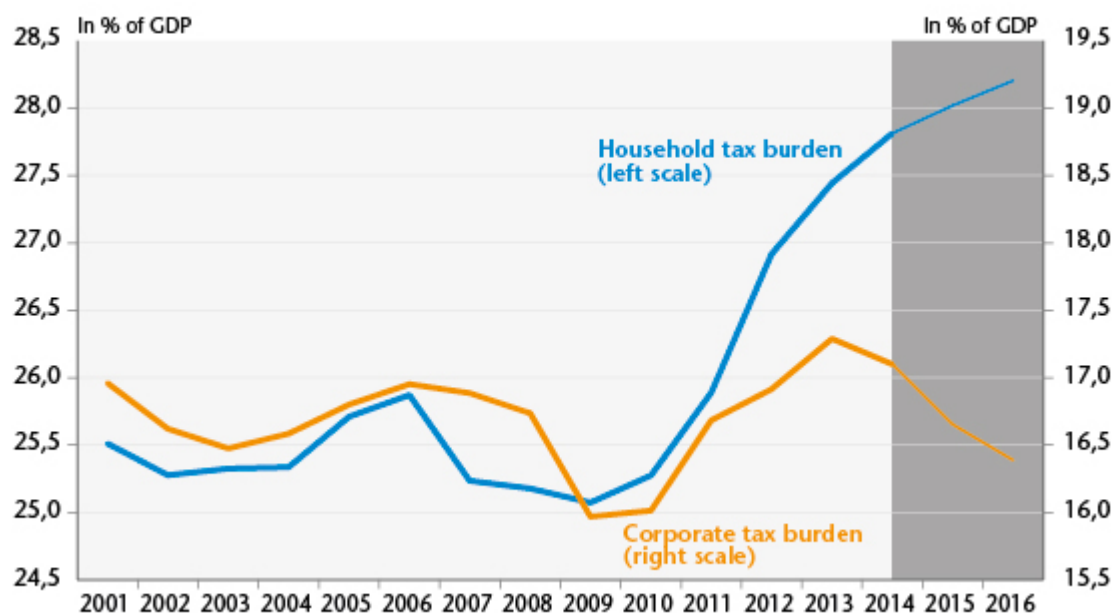
allowance on the C3S tax base (1 billion), the implementation of the CICE tax credit (0.3 billion) and the additional tax reduction on investment (0.2 billion) have been only partially offset by tax increases on business, mainly with the hike on pension contribution rates (0.6 billion). However, as in previous years, the tax burden on households will increase in 2016 by 4.1 billion (0.2 GDP point), despite a further reduction in income tax (2 billion). The main measures increasing household taxation are similar to those in 2015, including environmental taxation, with the hike in the carbon tax (1.7 billion) and the CSPE tax (1.1 billion), measures on financing pensions (0.8 billion), and the expected increase in local taxation (1.1 billion). Note that the elimination of the PPE working tax credit in 2016 will mechanically lead to an increase in the household tax burden of 2 billion^[4], but this will be offset by an equivalent amount for the new Prime d'activité working tax credit.

Ultimately, over the period 2010-2016, the household tax burden will increase by 66 billion euros (3.1 GDP points) and the burden on business by 8 billion (0.4 GDP point). The household tax burden will reach a historic high in 2016, at 28.2% of GDP. Conversely, the corporate tax burden in 2016 will amount to 16.4% of GDP, less than before the 2008 crisis. And in 2017, the last phase of the Responsibility Pact (with the complete elimination of the C3S tax and the reduction of IS corporate tax rates) and the expected CICE-related reimbursements should lead to cutting corporate taxation by about 10 billion euros, bringing the corporate tax burden down to the lowest point since the early 2000s.

The need to finance measures both to enhance corporate competitiveness and to reduce the structural deficit is placing the entire burden of the fiscal adjustment on households. Thus, the reduction in income tax in 2015 and 2016 will not offset the rise in other tax measures, most of which were approved in Finance Acts prior to 2015, and seems low in

relation to the tax shock that has hit households since 2010. However, how these recent tax changes affect growth and the consequent impact on inequality will depend on the way business makes use of the new resources generated by the massive decline in its tax burden since 2014. These funds could lead to a rise in wages, employment, investment or lower prices or to higher dividends and a reduction in debt. Depending on the way business allocates these, the impact to be expected on the standard of living in France and on inequality will not of course be the same. An evaluation of the impact of these changes on the tax burden will surely lead to future studies and debate.

Figure: Changes in the tax burden on households and business



Sources : Insee, PLF (Finance Act) 2016; OFCE calculations.

[\[1\]](#) The tax burden on households includes direct taxes (CSG, CRDS, IRPP, housing tax, etc.), indirect taxes (VAT, TICPE, CSPE, excise taxes, etc.), tax on capital (ISF, DMTG, property tax, DMT0, etc.), and salaried and self-employed social security contributions. The corporate tax burden includes the various taxes on production (value-added tax and corporate

property tax (ex-TP), property tax, C3S tax, etc.), taxes on wages and labour, corporate income tax and employer social security contributions.

[2] For example, employer social contributions for pensions are analyzed here as a tax burden on business and not as deferred wages for households or a transfer of income from assets to retirees.

[3] In 2013, 61% of the tax burden was on households and 39% on business. However, over the 2010-2013 period, tax increases were borne 64% by households and 36% by business, which was more or less their respective weights in taxation.

[4] The PPE credit will be replaced by the Prime d'activité working tax credit, in an equivalent amount, which also encompasses the RSA activité tax credit; for accounting purposes the PPE is considered as a public expenditure. However, this new measure should not change household income macroeconomically, but only the nature of the transfer. Thus, excluding the elimination of the PPE, the tax burden on households would increase by 2.1 billion in 2016.

**Financialisation and
financial crisis:
vulnerability and traumatic**

shock

By Jérôme Creel, Paul Hubert, Fabien Labondance

Since the mini-crash that took place in the Shanghai stock market in August, financial instability has resurfaced in the markets and the media and, once again, the link with financialisation has been evoked. The Chinese crisis resulted from a combination of real estate and stock market bubbles that were fed by the abundant savings of a middle class in search of high-yield investments. It feels like we've gone back almost ten years when what is considered the excessive financialisation of the US economy – with abundant savings from the emerging countries enabling the build-up of widespread US consumer debt – is treated as the cause of the financial instability and crisis that was triggered in the summer of 2007.

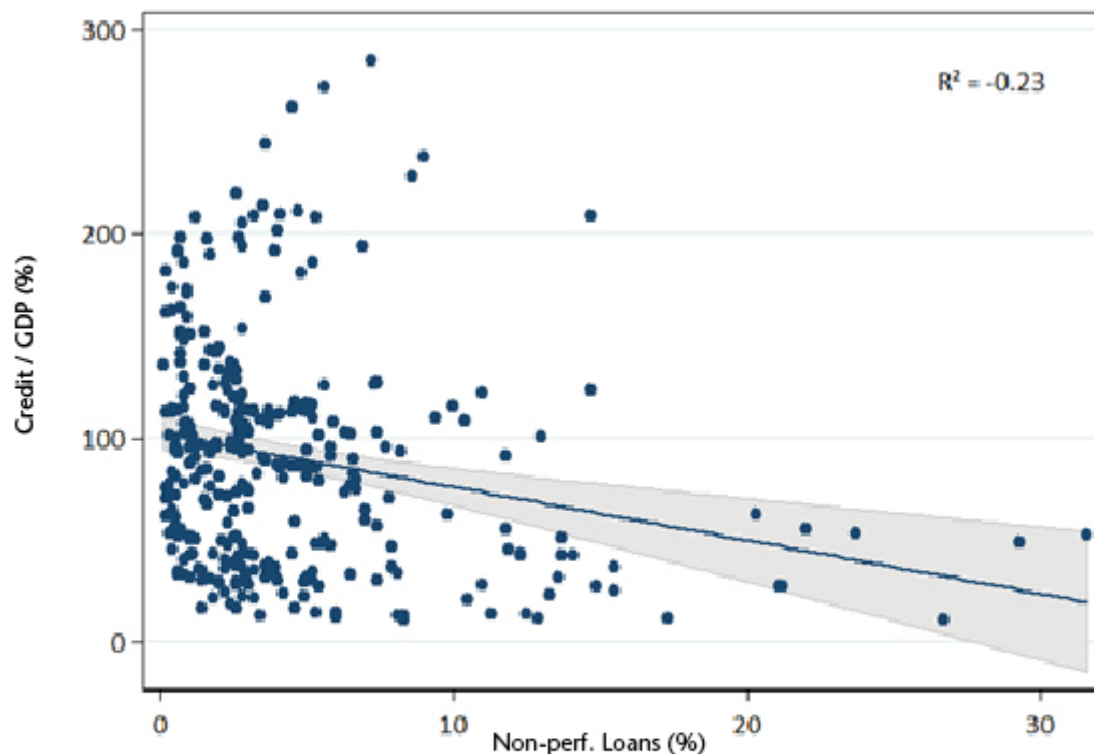
Is there really a link between, on the one side, increasing indebtedness and the great variety of financial investments, and on the other, volatile stock prices and a deterioration in the quality of bank loans? And if there is, what is the direction of the dynamics: from financialisation to financial instability, from financial instability to financialisation, or both at once? A rise in indebtedness could well lead to increasingly risky lending to agents who wind not being able to repay them, which would then lead to a financial crisis: this is one possible case. The occurrence of a crisis would change the behaviour of households and firms, causing them to reduce debt: this is the second case, in which financial instability reduces the financialisation of the economy. Depending on which is the case, the public policies needed differ. In the first, we need to monitor the degree of the economy's financialisation and target, for example, a maximum ratio of bank credit to GDP in order to prevent the rise and bursting of speculative bubbles. In the second case, there are two possibilities: to treat the causes, and thus to monitor

the quality of loans to households and business so as to ensure the proper allocation of capital in the economy; or to treat the consequences by supporting productive investment to annihilate any rationing of credit.

In the course of the debate on the links between financialisation and financial instability, and on the consequences to be drawn in terms of public policy, the European situation is interesting for two reasons: the European Union has set up a system for monitoring external imbalances, including financial ones, from 2011, and a banking union since 2014. In a recent [working paper](#), we look at this debate for several groups of countries in the European Union over the period 1998-2012.

At first glance, the relationship between these two concepts is not easy to demonstrate, as can be seen in the graph below. It shows a scatter plot that for each year and for each European country gives the levels of financialisation (approximated here by the share of credits / GDP) and of financial instability (approximated here by non-performing loans). The correlation between these variables is -0.23.

Figure. Financialisation and financial instability



Note: Non-performing loans, or bad debt, expressed as a percentage of total loans granted by banks.
Credit/GDP: total amount of bank credit expressed as a percentage of GDP.
Source : Creel et al. (2015) based on GFDD databases.

We test the two typical cases discussed above. We call the first case the vulnerability effect. As financialisation develops, it engenders a sort of euphoria that leads to granting loans that are increasingly risky, which fosters financial instability. This hypothesis derives from the work of Minsky (1995) [1]. We simultaneously test the potentially negative relationship between financial instability and financialisation, which we call the trauma effect. The very occurrence of financial instability as well as its impact encourages economic agents to take less risk and to shed debt. Our estimates show that the link between financial instability and financialisation is not uni-directional. Contrary to what is suggested by the simple correlation coefficient, the sign of the relationship is not the same when looking at the effect of one variable on the other, and vice versa. Both the vulnerability and the trauma effect have been at work in the European countries. A macro-prudential policy intended to

monitor the policy on granting bank loans, in terms of their volume and quality, therefore does indeed seem necessary in Europe.

We also tested the possibility that these effects are non-linear, that is to say, that they depend on reference values. The vulnerability hypothesis depends both on the level of financialisation (the higher it is, the stronger the relationship) and on time. This last point shows us that the positive relationship between financialisation and financial instability shows up at the moment of crisis for countries that are already heavily financialised. Finally, in the countries on the EU periphery [\[2\]](#), long-term interest rates and inflation rates greatly influence the financial instability variable. Consequently, it seems that for these countries there is a need for strong coordination between banking supervision and macroeconomic surveillance.

[\[1\]](#) Minsky H. P. (1995), "Sources of Financial Fragility: Financial Factors in the Economics of Capitalism", paper prepared for the conference, *Coping with Financial Fragility: A Global Perspective*, 7-9 September 1994, Maastricht, available at Hyman P. Minsky Archive. Paper 69.

[\[2\]](#) This group consists of Spain, Ireland, Italy, Greece, Portugal and the countries from the Eastern enlargements in 2004 and 2007. The establishment of this group is explained in the working paper.

The upward drift in senior unemployment continued in August

Analysis and Forecasting Department (France team)

The figures for the month of August 2015 published by France's Pôle Emploi job centre show a significant increase in the number of people registered as Category A (+20,000), i.e. an additional 156,000 job seekers over one year, [following two months of relative stability](#). While this figure is undoubtedly disappointing, the uncertainty surrounding monthly fluctuations in enrolment at the job centre should not be forgotten. Despite the downturn in the numbers registered in categories B and C in the last month (-11,600), the number of job seekers who have carried out an active job search has risen by nearly 332,000 since August 2014.

This figure nuances the publication of the unemployment rate as defined by the International Labour Office (ILO), which gives a less negative image of the French labour market. This statistic points to a slight fall in the unemployment rate in the first six months (-0.1 point), [largely due to shrinkage of the labor force](#) (-0.2 point).

Beyond the total figure, the data published for August confirms the divergences observed between different age groups. While up to September 2010 the number of people aged 50 or over registered in Category A at the job centre was lower than for the under 25 age group, there are now 330,000 more unemployed seniors than unemployed youth (graph). The increase in this gap since 2010 is due to several factors. The implementation of a series of pension reforms (2003, 2010), coupled with the elimination of exemptions for seniors on job-seeking, has led to a longer duration of employment and a

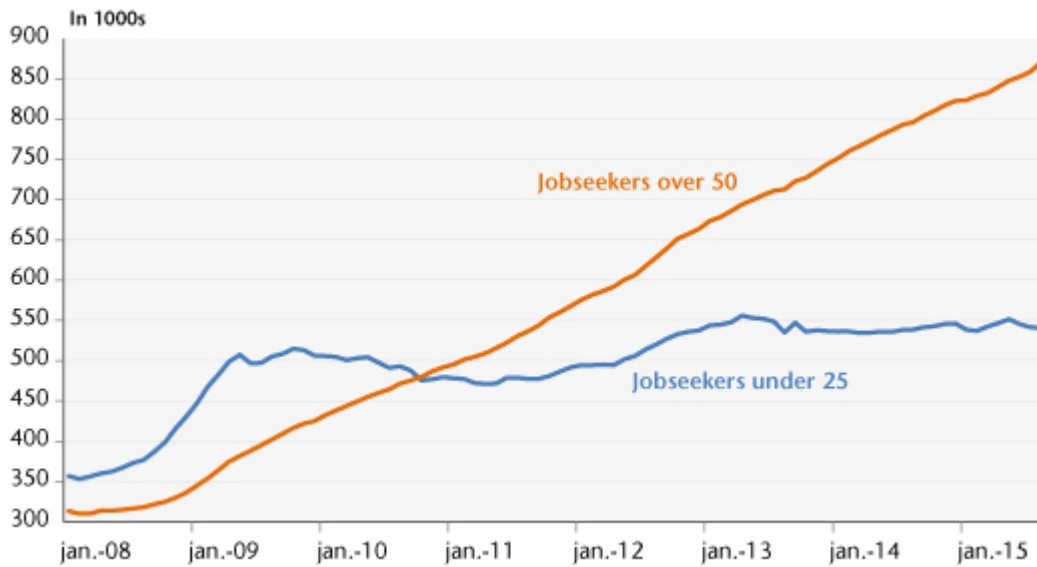
later statutory retirement age. In a context of weak growth, the rise in the rate of senior employment has been insufficient to absorb the growth in the workforce for that age group, resulting in a higher unemployment rate for the over 50s.

The weaker increase in the number of unemployed youth is the result of two main factors. First, the employment policies implemented since 2013 have targeted youth in particular, including the *emplois d'avenir* programme. Second, the weak job creation in the market sector has mainly taken the form of temporary jobs (CDD fixed-term and temporary contracts), an area in which young people are heavily represented ([34.2% of young people in employment are on CDD contracts or temping, versus 8.4% for other age groups](#)).

Finally, while seniors are unemployed less often than young people (4.6% of those aged 50-64 against 8.6% for 15-24-year-olds), they are more exposed to long-term unemployment. 62% of the seniors registered at Pole Emploi have been jobless for more than a year, against 21% of young people.

All this indicates that only a macroeconomic policy aimed at increasing the overall level of employment is capable of simultaneously dealing with unemployment among both young people and seniors. Otherwise, in a situation where employment is lacking overall, policies that are aimed at certain categories, even if effective for that specific target, may lead to adverse effects on other categories.

Figure. Jobseekers in Category A according to age



Source: Pôle Emploi.

Unemployment: a fall by temping

by Analysis and Forecasting Department (France team)

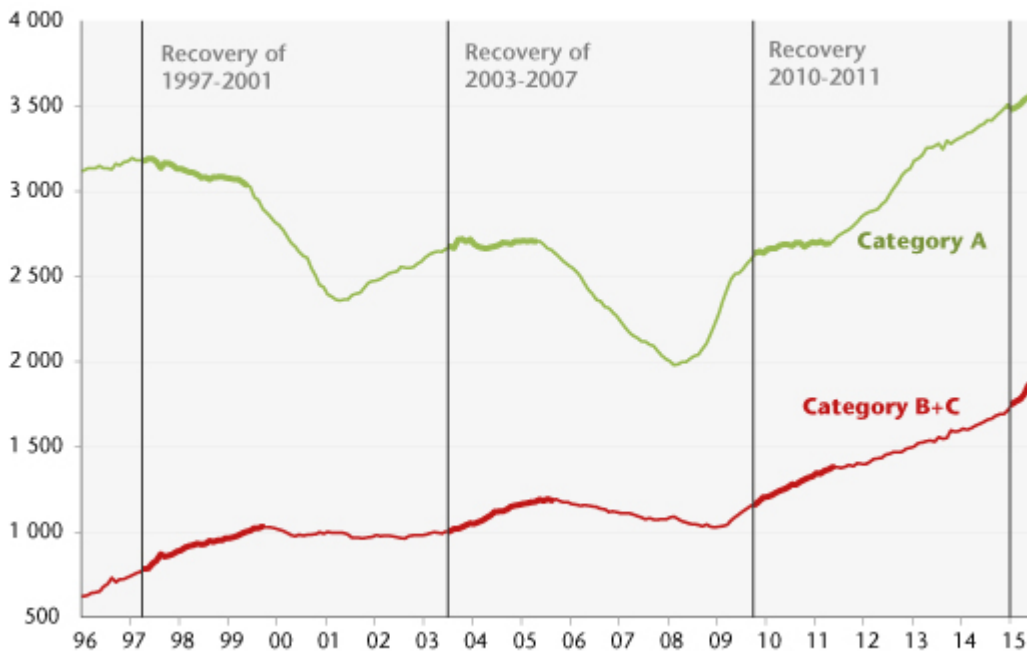
The unemployment figures for the month of July 2015 indicate a slight fall (-1900) in the number of people registering in category A. There is still too much uncertainty about monthly changes in enrolment at France's Pôle Emploi job centre to conclude that there has been a lasting improvement in the state of the labour market. However, the increase observed since January 2015 (+50,900 registered in category A) is smaller in scale than the figures recorded for this same period during the past three years (+128,500 on average for the first seven months of the previous three years). It is comparable to the situation in 2010-2011 (+44,300 on average

in the first seven months of both years), which were years of renewed growth.

Seen in the context of the first buds of recovery, this trend in unemployment is not surprising. First, the pick-up in GDP growth observed in the first six months (+0.7% according to [preliminary accounts published by the INSEE](#)) is expected to gain pace in the coming quarters. For now, [this recovery has meant a rise in salaried employment of +26,600 in the competitive sector during the first six months of 2015](#). This has been sufficient to limit the increase in unemployment, without however reversing it, as labour force numbers have increased by about 75,000 during the half year.

Furthermore, the increase in registrations in categories B and C [\[1\]](#) has been more marked than for category A (+145,600 since the year's start). This is due partly to some switching by the jobless in category A into these other categories, which reflects an increase in precarious employment that is consistent with the increase in temporary jobs in the first half year (+11,600): historically, an improvement in the labour market starts with an increase in precarious jobs (fixed term, temporary). This is also coinciding with an increase in job offers collected by Pôle Emploi, as well as with exits from the job centre due to a return to work, a figure that reflects a return to levels comparable to those observed in 2010-2011.

Figure. Enrolment in the Pôle Emploi job centre by category



Source : Pôle Emploi.

Finally, the trends differ by age group: the number of people under age 25 registered in category A is 4,600 lower than its level at year-end 2014. In fact, the young, who are over-represented in so-called temporary jobs ([34.2% of young people in work are on fixed-term CDD contracts or are temping, compared with 8.4% of those in other age groups](#)), benefit from the creation of this type of job, and from the increase in subsidized jobs that are targeted specifically at their age group. Conversely, the enrolment in category A of people aged 50 and over is rising steadily (+36,100 since the year started). 62% of those aged 50 and older have been enrolled in the job centre for over a year, versus an average of 39% for other age groups.

[1] These categories group people who have worked on reduced hours during the month, but are still registered at Pôle emploi.

Greece: When history repeats itself

By [Jacques Le Cacheux](#)

The duration of the Greek crisis and the harshness of the series of austerity plans that have been imposed on it to straighten out its public finances and put it in a position to meet its obligations to its creditors have upset European public opinion and attracted great comment. The hard-fought agreement reached on Monday 13 July at the summit of the euro zone heads of state and government, along with the demands made prior to the Greek referendum on 5 July, which were rejected by a majority of voters, contain conditions that are so unusual and so contrary to State sovereignty as we are used to conceiving of it that they shocked many of Europe's citizens and strengthened the arguments of eurosceptics, who see all this as proof that European governance is being exercised contrary to democracy.

By requiring that the creditors be consulted on any bill affecting the management of the public finances and by requiring that the privatizations, with their lengthy list dictated by the creditors, be managed by a fund that is independent of the Greek government, the euro zone's leaders have in reality put Greece's public finances under supervision. Furthermore, the measures contained in the new austerity plan are likely to further depress the already depressed domestic demand, exacerbating the recession that has racked the Greek economy in 2015, following a brief slight upturn in 2014.

Impoverishment without adjustment

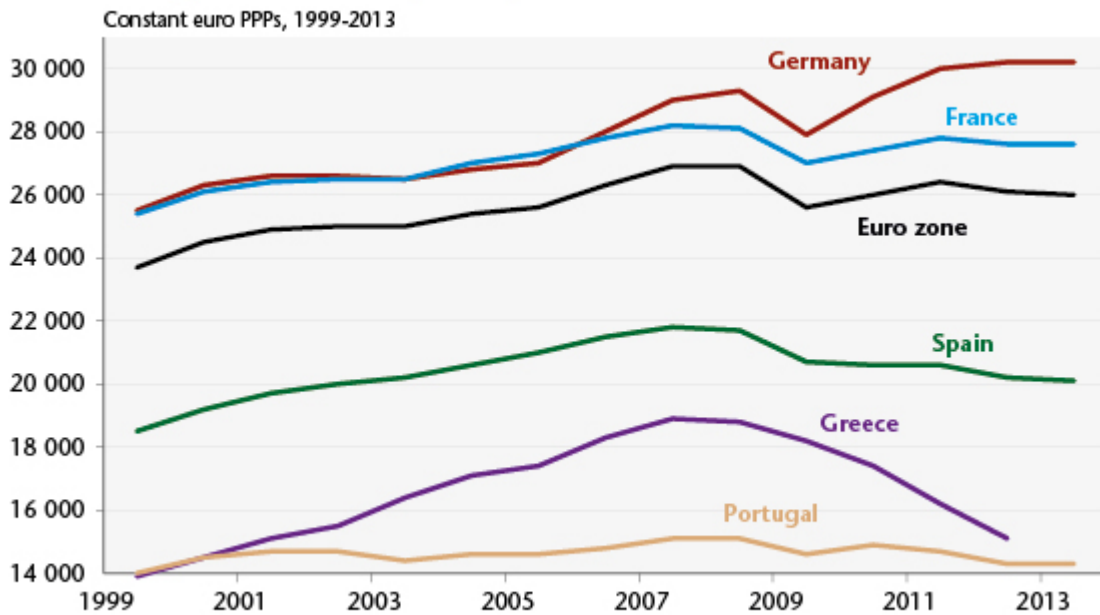
The Greek crisis, which in 2010 triggered the sovereign debt crisis in the euro zone, has seen prolonged agony punctuated by European psycho dramas that always conclude in extremis by an agreement that is supposed to save Greece and the euro zone. From the beginning, it was clear that a method based on the administration of massive doses of austerity without any real support for the modernization of the Greek economy was doomed to failure [\[1\]](#), for reasons that are now well understood [\[2\]](#) but at the time were almost universally ignored by officialdom, whether from European governments, the European Commission or the IMF, the main guarantor and source of inspiration for the successive adjustment plans.

The results, which up to now have been catastrophic, are well known: despite the lengthy austerity cure, consisting of tax hikes, public spending cuts, lower wages and pensions, etc., the Greek economy, far from recovering, is now in a worse state, as is the sustainability of the country's public finances. Despite the agreement in 2012 of Europe's governments on a partial default, which reduced the debt to private creditors – relief denied by those same governments two years earlier – Greece's public debt now represents a larger percentage of GDP (almost 180%) than at the beginning of the crisis, and new relief – this time probably by rescheduling – seems unavoidable. The third bailout package – roughly 85 billion euros, on the heels of approximately 250 billion over the past five years – will be negotiated over the coming weeks and will be in large part devoted just to meeting debt repayments.

Meanwhile, the average living standard of Greeks has literally collapsed; the difference with the euro zone average, which had tended to decline during the decade before the crisis, has now widened dramatically (Figure 1): the country's GDP per capita is now a little less than half that in Germany. And GDP per capita still only poorly reflects the reality in an economy where inequality has increased and spending on social

protection has been drastically reduced.

Figure 1. Real GDP per capita in several euro zone countries

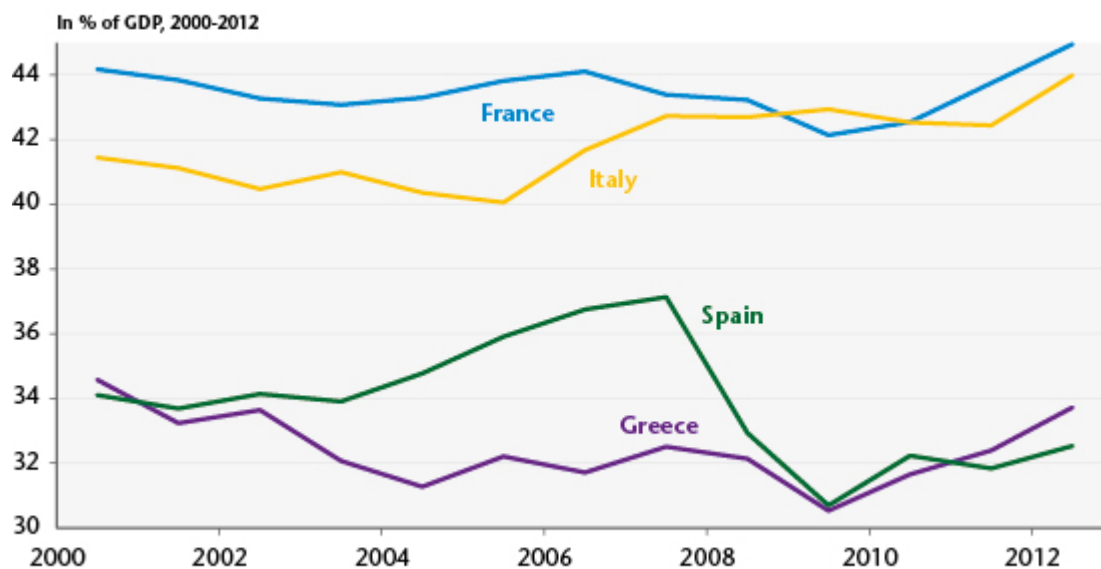


Source : Eurostat.

The new austerity plan is similar to the previous ones: it combines tax hikes – in particular on VAT, with the normal rate of 23% being extended to the Islands and many sectors, including tourism, that were previously subject to the intermediate rate of 13% – with reduced public spending, and will result in budget savings of about 6.5 billion euros over a full year, which will depress domestic demand and exacerbate the current recession.

The previous adjustment plans also featured “structural” reforms, such as lowering the minimum wage and pensions, deregulation of the labour market, etc. But it is clear that the fiscal component of these plans did not have a very visible impact on government revenue: after having declined significantly until 2009, the Greek tax burden – measured by the ratio of total tax revenue to GDP – has definitely increased, but not much more than in France (Figure 2). This does not mean, of course, that an even stronger dose of the same medicine will lead to better healing.

**Figure 2. Level of overall fiscal pressure
in several euro zone countries**



Source : Eurostat.

Does history shed light on the future?

The ills afflicting the Greek economy are well known: weak industrial and export sectors – apart from tourism, which could undoubtedly do better, but performs honourably – numerous regulated sectors and rentier situations, overstuffed and inefficient administration and tax services, burdensome military expenditure, etc.

None of this is new, and no doubt it was the responsibility of the European authorities to sound the alarm sooner and help Greece to renovate, as was done for the Central and Eastern Europe countries in the early 2000s in the years before they joined the European Union. Will the way it has been decided to do this now, through a forced march with the Greek government under virtual guardianship, be more effective?

If we rely simply on history, the temptation is to say yes. There are many similarities between the situation today and a Greek default back in 1893. At that time Greece was a relatively new state, having won its independence from the Ottoman Empire in 1830 following a long struggle supported by the European powers (England and France), which put the

country under a Bavarian king. Greece was significantly poorer than the countries of Western Europe: despite an effort at modernization undertaken after independence that was led by the Bavarian officials assembled around the Greek King Otto, in 1890 the country's GDP per capita was, according to data assembled by Angus Maddison[\[3\]](#), about 50% of the level of France, and a little less than one-third that of the UK. The analysis of Greece at that time was little better than that today:

“ ... Greece has been characterized throughout the 19th century by structurally weak finances, which has led it to default repeatedly on its public debt. According to the *Statesman's Yearbook*, in addition to significant military spending, Greece faces high expenditures on a disproportionately large number of officials for a small undeveloped state. Moreover, since part of Greece's debt is guaranteed by France and Great Britain, Greece could suspend debt service without the creditors having to suffer the consequences. The French and British budgets would be compelled to pay the coupons.

“By 1890, however, the situation had become critical. At the end of 1892, the Greek Government could continue paying interest only by resorting to new borrowing. In 1893, it obtained parliamentary approval for negotiating a rescheduling with its international creditors (British, German, French). Discussions were drawn out until 1898, with no real solution. It was Greece's defeat in the country's war with Turkey that served as a catalyst for resolving the public finances. The foreign powers intervened, including with support for raising the funds claimed by Turkey for the evacuation of Thessaly, and Greece's finances were put under supervision. A private company under international control was commissioned to collect taxes and to settle Greek spending based on a seniority rule designed to ensure the payment of a minimal interest. Fiscal surpluses were then allocated based on 60% to the creditors and 40% for the government.”[\[4\]](#)

Between 1890 and 1900, Greek per capita income rose by 15% and went on to increase by 18% over the next decade; in 1913, it came to 46% of French per capita income and 30% of the British level, which was then at the height of its prosperity. So this was a success.

Of course, the context was very different then, and the conditions that favoured the guardianship and the recovery are not the same as today: there was no real democratic government in Greece; there was a monetary regime (the gold standard) in which suspensions of convertibility – the equivalent of a “temporary Grexit” – were relatively common and clearly perceived by creditors as temporary; and in particular there was a context of strong economic growth throughout Western Europe – what the French called the “Belle Epoque” – thanks to the second industrial revolution. One cannot help thinking, nevertheless, that the conditions dictated to Greece back then inspired the current decisions of Europe’s officials[5].

Will the new plan finally yield the desired results? Perhaps, if other conditions are met: substantial relief of the Greek public debt, as the IMF is now demanding, and financial support for the modernization of the Greek economy. A Marshall Plan for Greece, a “green new deal”? All this can succeed only if the rest of the euro zone is also experiencing sustained growth.

[1] See Eloi Laurent and Jacques Le Cacheux, “Zone euro: *no future?*”, *Lettre de l’OFCE*, no. 320, 14 June 2010, <http://www.ofce.sciences-po.fr/pdf/lettres/320.pdf> .

[2] See in particular the work of the OFCE on the recessionary effects of austerity policies: <http://www.ofce.sciences-po.fr/pdf/revue/si2014/si2014.pdf> . Recall that the IMF itself has acknowledged that the

adjustment plans imposed on the European economies experiencing public debt crises were excessive and poorly designed, and especially those imposed on Greece. This *mea culpa* has obviously left Europe's main leaders unmoved, and more than ever inclined to persevere in their error: *Errare humanum est, perseverare diabolicum!*

[3] See the data on the Maddison Project site: <http://www.ggd.net/maddison/maddison-project/home.htm> .

[4] Excerpt from the article by Marc Flandreau and Jacques Le Cacheux, "La convergence est-elle nécessaire à la création d'une zone monétaire ? Réflexions sur l'étalon-or 1880-1914" [Is convergence necessary for the creation of a monetary zone? Reflections on the gold standard 1880-1914], *Revue de l'OFCE*, no. 58, July 1996, <http://www.ofce.sciences-po.fr/pdf/revue/1-58.pdf> .

[5] An additional clue: the German Finance Minister Wolfgang Schäuble insisted that Greece temporarily suspend its participation in the euro zone; in the 1890s, it had had to suspend the convertibility into gold of its currency and conducted several devaluations.

Regulating the financial activities of Europe's banks: a fourth pillar for the banking union

By [Céline Antonin](#), [Henri Sterdyniak](#) and [Vincent Touzé](#)

At the impetus of EU Commissioner Michel Barnier, on 29 January 2014 the European Commission proposed new regulations aimed at limiting and regulating the commercial activities of banks “of systemic importance”, that is to say, the infamous “too big to fail” (TBTF).

Regulating proprietary activities: a need born of the crisis

Due to banks’ particular responsibility in the 2008 economic and financial crisis, many voices have been raised demanding stricter regulation of their financial activities. This has led to two approaches: prohibition and separation.

In the United States, the “Volker rule” adopted in late 2013 prohibits banks from engaging in any proprietary trading activities as well as taking holdings of greater than 3% in hedge funds. The banks can nevertheless continue their own market-making and hedging activities. Obviously, this rule does not prohibit banks from investing their own funds in financial assets (equities, government and corporate bonds). The purpose of the rule is to prevent a bank from speculating against its customers and to minimize the use of the leveraging that proved so costly to the financial system (banks using their clients’ money to speculate on their own behalf).

The European approach is based on the Vickers Report (2011) for the United Kingdom and the Liikanen Report (2012) for the European Union. These reports recommend some separation between traditional banking activities on behalf of third parties (management of savings, provision of credit, simple hedging operations) and trading activities that are for the bank’s own account or bear significant risk, although the activities can be maintained in a common holding company. The Vickers Report proposes isolating traditional banking activities in a separate structure. In contrast, according to the Liikanen report it is proprietary trading and large-scale financial activities that need to be isolated in a separate

legal entity.

The idea of separating banking activities is not new. In the past, many countries enacted legislation to separate commercial banks from investment banks (Glass-Steagall Act in 1933 in the United States, the 1945 Banking Act in France). These laws were revoked in the 1980s due to a growing belief in the superiority of the “universal bank” model, which allows a single bank to offer a full range of financial services to individuals (loans, deposits, simple or complex financial investments) and especially to business (loans, hedging, issuance of securities, market-making activities). The crisis exposed two defects in this model: the losses incurred by a bank on its proprietary trading and other activities on the markets led to a loss in its equity capital, thereby calling into question the bank’s lending activities and requiring the State to come to its rescue in order to ensure that bank credit didn’t dry up. The universal bank, backed by the State’s guarantee and sitting on a mass of deposits, did not have sufficient vigilance over its proprietary trading activities (as was shown by the cases of Kerviel, Picano-Nacci and Dexia).

An ambitious European regulatory proposal

This proposal for bank reform is coming in a situation that is complicated by several factors:

1) The Basel 3 regulations currently being adopted already impose strict rules on the quality of counterparties of the equity capital. Speculative activities must be covered by substantial levels of common equity.

2) The banking union being developed provides that in case of a crisis creditors and large deposit holders could be called upon to save a bank facing bankruptcy (principle of “bail in”), so that taxpayers would not be hit (end of “bail out”). But there are doubts about this mechanism’s

credibility, which could cause a domino effect in the event that a TBTF bank faces bankruptcy.

3) Some European countries have anticipated reform by adopting a separation law (France and Germany in 2013) or setting prohibitions (Belgium). In the United Kingdom, a separation law inspired by the Vickers Report (2011) is to be adopted by Parliament in early 2014.

The regulatory proposal presented on 29 January is more demanding than the Liikanen Report. Like the “Volker rule” in the US, it prohibits speculation on the bank’s own account through the purchase of financial instruments and commodities, as well as investments in hedge funds (which prevents banks from circumventing the regulation by lending to hedge funds while holding significant shares in these funds, thereby taking advantage of the greater leverage).

Moreover, in addition to this prohibition the European legislator provides for the possibility of imposing a separation on an independent subsidiary for operations that are considered too risky, that is to say, that would result in taking positions that are too large. The aim is to address the porous border between proprietary trading and trading for third parties, as bankers could take risks for themselves while not covering the positions sought by their clients. With these new regulations, the legislator hopes that in the event of a bank crisis public support for the banks will benefit only depositors, not the bankers, with as a consequence an overall reduced cost.

Compared to French regulations, the regulatory proposal is more restrictive than the [law on the separation and regulation of banking activities](#) of 26 July 2013. Indeed, French law provides for the legal compartmentalization only of certain proprietary activities and highly leveraged activities in an independently financed subsidiary; strict prohibition concerns only high-frequency trading activities and speculation in

agricultural commodities. And there are numerous exceptions: the provision of services to clients, market-making activities, cash management, and investment transactions and hedging to cover the bank's own risks. In contrary, the prohibitions are broader in the regulatory proposal, as it applies to all proprietary trading. In addition, the regulatory proposal prohibits investment in hedge funds, whereas the French law permits it provided that such activities are compartmentalized.

The regulatory proposal nevertheless concerns only banks of a systemic size, *i.e.* 30 out of the 8000 found in the European Union, representing 65% of banking assets in the EU. It will not be discussed until the election of the new Parliament and the establishment of a new Commission.

A reform that doesn't have a consensus

Michel Barnier's proposed reform has already provoked sharp criticism from certain member countries and the banking community. Some have reproached it for intervening in an area where it has no jurisdiction, which clearly indicates the current complexity of the legislation governing the European banking system.

France, Germany, Belgium could object, "Why are you interfering? We have already enacted our banking reform." But the logic of the banking union is that the same laws apply everywhere. These countries have chosen to carry out a minimal banking reform in order to pre-empt the content of European law. This is hardly acceptable behaviour at European level. There is also the case of the United Kingdom (for which Barnier's proposal opens the exit door: the regulations will not apply to countries whose legislation is more stringent).

The banking union provides for the European Central Bank to oversee the large European banks and for the European Banking Agency to set the regulations and rules on supervision. The

Commission can therefore be reproached for intervening in a field for which it is no longer responsible. On the other hand, the crisis clearly showed that banking concerns more than just the banks. It is legitimate for EU political institutions (Commission, Council, Parliament) to intervene in the matter.

The proposal has encountered two contradictory criticisms. One is that it doesn't organize a genuine separation of deposit-taking banks and investment banks. From this perspective, deposit or retail banks would be entrusted with specific tasks (collecting and managing deposits; managing liquid savings and risk-free savings; lending to local government, households and businesses); they would not have the right to engage in speculative activities or trading activities or to lend to speculators (hedge funds, arranging LBO transactions). These banks would be backed fully by a government guarantee. In contrast, market or investment banks would have no government guarantee for their market interventions and equity and other above-the-line operations. Since these transactions are risky, the absence of a public guarantee would lead them to set aside a greater amount of capital and to bear a high cost for attracting capital. This would reduce their profitability and thus the development of hedging and other speculative activities. A company that was in need of a hedging operation would have to have it carried out by an investment bank and not by its regular bank, so at a higher cost. Conversely, this would reduce the risk that banks suck their clients (banks and companies) into risky investments and operations. A reform like this would greatly increase the transparency of financial activities, at the cost of diminishing the importance of the banks and financial markets. Michel Barnier did not dare take the principle of separation to this, its logical conclusion. He remains instead within the logic of the universal bank, which uses its massive size as a deposit bank to provide financial intermediary services to its customers (issuance of securities, coverage of risk, investment in the markets,

etc.), to intervene in the markets (market-making for foreign exchange and public and private securities) and to underwrite speculative activities.

The reform is nevertheless facing stiff opposition from the banking community, who would have preferred the status quo. Hence Christian Noyer, a member of the ECB Governing Council, has labelled the proposals “irresponsible”, as if the ECB had acted responsibly before 2007 by not warning about the uncontrolled growth of banks’ financial activities.

The European Banking Federation (EBF) as well as the French Banking Federation (FBF) are demanding that the universal banking model be preserved. The banks are criticizing the obligation to spin off their market-making operations (including for corporate debt). According to the FBF, this regulation “would lead to making this operation considerably more expensive,” which “would have a negative impact on the cost of financing companies’ debts and hedging their risks”. However, this obligation may be waived if the banks demonstrate that their market interventions do not require them to take on any risk. The banks could therefore continue to act as market makers provided that they set strict limits on their own positions; they could provide simple hedging operations by covering these themselves.

A fourth pillar for the banking union?

European banks have of course rightly pointed out that this reform comes in addition to the establishment of the SSM (single supervisory mechanism), the SRM (single resolution mechanism), and the ECB exercise assessing the banks (launched in November 2013). The overall system does lack cohesion; a well thought-out schedule should have been set.

However, the separation advocated by the Barnier proposal lends credibility to the banking union and its three pillars (SSM, SRM and deposit insurance). This project does contribute

to convergence in banking regulations, from both a functional and a prudential perspective. The establishment of a consistent framework simplifies control by the European supervisor under the SSM (the ECB will monitor the banks' normal activities and ensure that they are not affected by speculative activities). The separation recommended by the Barnier proposal enhances the credibility of the SRM; there will no longer be any banks that are too big to go bankrupt, and investment bank losses will not rebound onto the lending activities of deposit banks and will not have to be borne by the taxpayer. By reducing the risk that deposit banks might fail, the risk of a costly rescue plan for investors (bail-in) is also lowered, as is the risk of needing recourse to deposit insurance. In this sense, the draft regulations can be considered a fourth pillar of the banking union.

For more information:

- Antonin C. and V. Touzé V. (2013), [The law on the separation of banking activities: political symbol or new economic paradigm?](#), OFCE Blog, 26 February 2013.
 - Avaro M. and H. Sterdyniak H. (2012), [Banking union: a solution to the euro crisis?](#), OFCE Blog, 10 July 2012.
 - Gaffard J.-L. and J.-P. Pollin (2013), [Is it pointless to separate banking activities?](#), *OFCE Blog*, 19 November 2013.
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TOFLIT18: for a better understanding of the French economy

By Loïc Charles and [Guillaume Daudin](#)*

Recurrent questions on our economies are, to quote a few: Which factors and actors are key for economic development? What private and public behaviors are particularly growth-enhancing? How important are institutions and policies in shaping trade, in promoting innovations and then growth?...There are different ways of enhancing our knowledge to answer these questions. The first way consists in laboratory experiments where a small-scale environment is created in order to understand “how the different pieces of the system work and interact” This is particularly appropriate for learning on social preferences and dealing with welfare issues. But, as soon as questions related to growth – such those mentioned above – are concerned, laboratory experiments do not appear very suitable. One other way of enhancing our knowledge consists in analyzing what happens today in our country and, possibly, to carry out international comparisons in order to disentangle between what is “good” and what is “bad” for the economy. Once one is engaged in that direction, why stop at comparison across space? Analyzing what happened several decades or centuries ago and to learn from these past experiences for the current period can also be very fruitful.

The project “Transformations of the French Economy through the Lens of International Trade, 1716-1821” ([TOFLIT18](#)) follows this direction. The 4-year project, granted funding by [ANR](#), was launched on the 1st January 2014.

In few words, the project aims at analyzing the French economy during the period that laid the economic ground for the entry

of France and Europe in the modern industrial era. Its main tools are the retranscription, the use and the diffusion of French international trade statistics.

The French administrative trade statistics are the most comprehensive and coherent source of quantitative information available for the French economy at that time. These data were produced locally and aggregated at the national level by the Bureau de la Balance du Commerce from 1716 on ([Charles and Daudin ,2011](#)). Despite several administrative reshufflings, the techniques of gathering and presenting the statistics on French foreign trade went almost unchanged up to the 1820s: they provided the total value, and sometimes the unit values, of merchandise and partner-specific trade flows; we have already photographed an almost complete series of yearly statistics. These documents are unique as they provide quantitative information on several geographical levels. As such, they can be used to study the economic effects of international trade on the French economy as a whole, on the economy of a single region, of a port town as well as on the economic behaviors of individual agents, e.g. a merchant or a community of merchants from a single town/region. They can also be used to get a more accurate understanding of the interplay that existed between these different geographical levels.

The volume and dispersion of primary sources makes the process of collecting and putting them into a usable form both time-consuming and costly. Our [team](#) includes therefore social scientists with consolidated experience in the construction and management of large databases (notably [MARPROF](#), [NAVIGOCORPUS](#), [RICardo](#) and [SoundToll Registers Online](#)). They will bring their expertise to cross-test our dataset with other types of information on trade (shipping and merchants accounts). The collaboration of researchers who are currently working on similar set of foreign trade statistics for important economic partners of France at that period— Great-

Britain and the Austrian Netherlands – will allow both crosschecking and building comparative studies.

The result database will include the bilateral value (with 20-30 different partners) of trade flows at the national level from 1716 to 1821, a merchandise (600-1000 different goods) and partner breakdown from at least 1750 onward, unit values and quantities from 1771 to 1792 and regional trade data. The project will transfer this database in the public domain and make it easily useable by the research community. The collected data can partly substitute for the lack of domestic macroeconomic series.

We will use the data to improve our knowledge of the French economy and our understanding of the economic mechanisms at work, both at the national and regional level. Two main avenues of research will be privileged. First, we will investigate the evolution of French specialization, both across French regions and in comparison to other countries. How was it linked to the contrasted economic development of France and Britain? What does it tell us on the determinants of international trade? Second, we will study the effects of policy choices on the French economy: France went through several wars and politic upheavals. It also went through stark changes in its commercial policies: from mercantilism to mitigated free trade in the 1760s with its colonial empire, to a number of free-trade treaties in the 1780s, followed by the closing up of the economy under the Empire. What were the effects of these policy choices?

All these questions resonate particularly to our contemporary ears. More importantly, the answer to these questions can provide a renewed glance on the functioning of the (French) economy, both then and now.

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Is the French tax-benefit system really redistributive?

By [Henri Sterdyniak \[1\]](#)

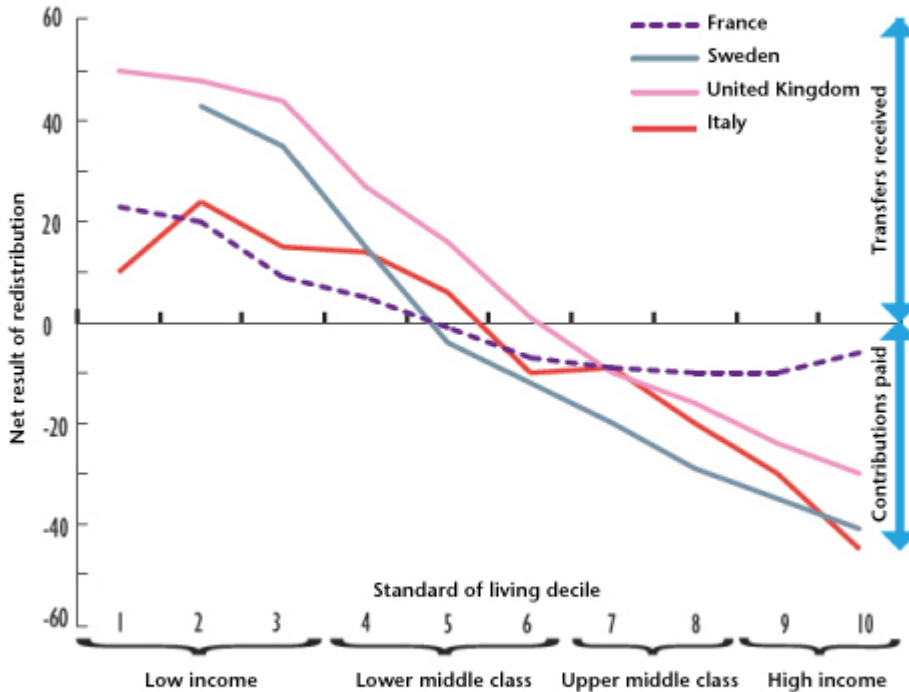
France has set up benefits such as RSA income support, PPE in-work negative income tax, CMU universal health care, the minimum pension, housing allowances, and exemptions from social security contributions for low-wage workers. From the other side, it has a tax on large fortunes; social insurance and family contributions apply to the entire wage; and capital income is hit by social security contributions and subject to income tax. France's wealthy are complaining that taxation is confiscatory, and a few are choosing to become tax exiles.

Despite this, some people argue that the French tax-benefit (or socio-fiscal) system is not very redistributive. This view was recently lent support by a study by Landais, Saez and Piketty: the French tax system is not very progressive and even regressive at the top of the income hierarchy [\[2\]](#): the richest 0.1% of households are taxed at a very low rate. But redistribution through the tax-benefit system is effected not just through taxes but also through social benefits. We must therefore look at both these aspects to evaluate how redistributive the system is. This is especially true as Landais, Saez and Piketty take into account the VAT paid on consumption financed by social benefits, but not the benefits themselves, meaning that the more a poor household benefits (and spends) from social benefits, the more it seems to lose on redistribution.[\[3\]](#)

Four researchers from Crédoc, the French Research Center for the Study and Monitoring of Living Standards, have published a study [\[4\]](#) that takes benefits into account. They nevertheless conclude: “The French tax system, taken as a whole, is not very redistributive.” The study uses post-redistribution standard-of-living deciles to review the benefits received and the taxes paid by households (direct taxes, indirect taxes and social contributions) as a percentage of disposable income, and compares France, Italy, the United Kingdom and Sweden. In France, net transfers (levies less benefits) represent only 23% of household disposable income in the first standard-of-living decile (the poorest), against 50% in the United Kingdom (see figure). At the other end of the scale, in France transfers lower the disposable income of the richest households by only 6%, versus 30% in the UK, 40% in Sweden, and 45% in Italy. France is thus considered to have the lowest level of redistribution, with little distributed to poor people and low taxes on the rich.

Figure. According to the CREDOC, the French tax-benefit system is not very redistributive

Summary of transfers received and contributions paid, as a % of disposable income, by standard of living decile



Source: Credoc calculations using data from the Luxembourg Income Study, 2006.

Note: People in the lowest standard of living decile (i.e. the poorest 10%) receive a net gain from redistribution equal to 23% of their disposable income. This net gain is calculated as the difference between their social transfers (social, sickness and pension benefits) and their contributions (income tax, social charges, indirect taxes).

Yet the French tax-benefit system is considered by international institutions as one of those that minimize inequalities the most. For instance, the OECD (2011) wrote: “Redistribution through taxes and benefits reduces inequality by just over 30% in France, which is well above the OECD average of 25%”.

The OECD provides statistics on income inequality (measured by the Gini coefficient) before and after transfers. Of the four countries selected by the Crédoc, it is France where the Gini is reduced the most as a percentage by transfers (Table 1), to an extent equivalent to the level in Sweden, and significantly greater than the reduction in Italy and the UK. Euromod winds up with a substantially similar classification (Table 2).

Table 1. Gini index of income distribution (in 2010) according to the OECD

	Before transfers	After transfers	Impact of transfers
Germany	0.496	0.286	-42.3
Denmark	0.429	0.252	-41.3
France	0.505	0.303	-40.0
Italy	0.503	0.319	-36.6
United Kingdom	0.523	0.341	-35.2
Sweden	0.441	0.269	-39.0
United States	0.499	0.380	-23.8

Source: OECD (2013). The Gini index lies between 0 (perfect income equality) and 1. The distribution of income becomes more equal as the index approaches 0.

Table 2. Gini index of income distribution (in 2010) according to Euromod

	Before transfers	After transfers	Impact of transfers
Germany	0.518	0.380	-48.1
Denmark	0.443	0.334	-54.0
France	0.483	0.349	-50.1
Italy	0.497	0.373	-36.8
United Kingdom	0.524	0.477	-38.0
Sweden	0.429	0.317	-46.2

Source: Euromod, 2012.

Table 3. Poverty rate (60% threshold)

	2005	2012
Germany	12.2	16.1
Denmark	11.8	13.1
France	13.0	14.1
Italy	18.9	19.4
United Kingdom	19.0	16.2
Sweden	9.5	14.2

Source: Eurostat, 2012.

The *Portrait social* [Social Portrait] by the INSEE provides a careful summary of how redistributive the French socio-fiscal system is (Cazenave *et al.*, 2012). It seems that inequality is reduced significantly (Table 4) in France: the inter-decile ratio (D10/D1) falls from 17.5 before redistribution to 5.7 afterwards. [5] According to the INSEE, 63% of the reduction in inequality comes from social benefits and 37% from levies, which confirms the need to take benefits into account in order to assess redistribution.

Table 4. Standard of living fractiles before redistribution according to the INSEE*

	D1	Q1	Q2	Q3	Q4	Q5	D10
Average income before redistribution	4 128	7 266	15 591	21 474	28 626	55 292	72 195
Average disposable income (DI)	9 948	11 266	15 847	20 145	25 602	44 919	56 654
Net transfers	5 820	4 000	256	-1 329	-3 024	-10 373	-15 541
Net transfers as % of DI	59	36	2	7	-12	-23	-27

* in euros per year per consumption unit. D1: the 10% of people with the lowest living standard; Q1: the 20% of people with the lowest living standard, etc.; D10: the 10% of people with the highest living standard.
Source: INSEE, 2013, Portrait social.

The vision presented by Crédoc of the redistributivity of the French tax-benefit system is thus unusual... and, to put it frankly, wrong.

The study is based on data from the *Budget des familles* [Family budget] survey that is not matched with fiscal data and which is generally considered less reliable than the Euromod survey or than the tax and social security figures used by the INSEE. This may explain some important differences between the Crédoc figures and those of the INSEE: for example, according to the INSEE, non-contributory transfers represent 61% of the disposable income of the poorest 10%, but only 31% according to Crédoc (Table 5).

Like the INSEE, the Crédoc study ignores employer national health insurance contributions (which hit high wages in France, unlike most other countries) and the ISF wealth tax (which exists only in France). Furthermore, it does not distinguish between contributory contributions (which give rights to a pension or unemployment benefits) and non-contributory contributions (such as health insurance or family contributions), which do not give rights. However, low-wage workers are not hit by non-contributory contributions in France, as these are more than offset by exemptions from social security contributions on low wages.

Table 5. Redistribution for the extreme deciles
A comparison of INSEE and CREDOC

	D1		D10	
	INSEE	CREDOC	INSEE	CREDOC
Primary income (pre-distribution)	41.5	39	127.4	93
Contributory benefits		38		32
Non-contributory benefits	60.2	31	0.6	1
Social contributions	-2.1	-8	-10.1	-16
Direct taxes	0.4	0	-17.9	-10
Total: Net disposable income	100	100	100	100
Indirect taxes	-22	-36	-10	-13
Net transfers (excl. indirect taxes)	+58.5	+59	-27.4	7
Net transfers (incl. indirect taxes)	+36.5	+23	-37.4	-6

Source: Authors' calculations based on INSEE (2013) and CREDOC (2013).

Most importantly, the study contains two errors that heavily distort the conclusions. The first methodological error is that, contrary to the INSEE, the authors include contributory transfers, in particular pensions [6], in social transfers. But for retirees, public pensions represent a very large part of their disposable income, particularly in France. Since the pension system ensures parity in living standards between retirees and active employees, then retirees show up in all the standard of living deciles and the tax-benefit system does not seem to be very redistributive, as it provides benefits to wealthy retirees. And contrariwise, if a country's pension system does not assure parity in living standards between retirees and active employees, then the tax-benefit system will seem more redistributive, as it provides pensions only to the poor.

So paradoxically, it is the generosity of the French system towards pensioners and the unemployed that makes it seem to be not very redistributive. Thus, according to Crédoc, the richest 10% receive contributory transfers representing 32% of their disposable income, which means that, in total, their net transfers represent only a negative 6% of their income. This is especially the case as Crédoc does not take into account the old-age pension contributions (*cotisations vieillesse*) incurred by businesses. If, as the INSEE does, pensions (and

more generally all contributory benefits) are considered as primary income, resulting from past contributions, the negative net transfers of the richest decile increase from -6% to -38%.

The other methodological problem is that Crédoc claims to take into account the weight of indirect taxes in disposable income (which INSEE does not). This comes to 36% for the poorest 10%, 23% in the middle of the income hierarchy, and only 13% for the best-off. The highly regressive nature of indirect taxes would make the whole tax system regressive: the poorest pay more than the rich. According to the figures from Landais, Saez and Piketty (2011), indirect taxation is definitely regressive (15% of the disposable income of the poorest, and 10% for the richest), but the gap is only 5%. According to the INSEE [\[7\]](#), the weight of indirect taxes in disposable income is 22% for the poorest, 16% in the middle income range and 10% for the richest. This difference comes from the structure of consumption (the poorest consume relatively more tobacco and petroleum products), and especially the savings rate, which increases as households earn more. In fact, the difference is undoubtedly overstated in an inter-temporal perspective: some households will consume today's savings tomorrow, so it is then that they will be hit by indirect taxation. In fact, the Crédoc study heavily overestimates the weight of indirect taxes by using an extravagant estimate of the household savings rate [\[8\]](#): the overall French household savings rate is -26.5%; only decile D10 (the richest 10%) have a positive savings rate; decile D1 has a negative savings rate of -110%, that is to say, it consumes 2.1 times its income. The poorest decile is thus hit hard by the burden of indirect taxes. But how likely is this savings rate?

National tax-benefit systems are complex and different. Comparisons between them need to be made with caution and rigour. To judge how redistributive the French system actually is, it is still more relevant to use the work of the INSEE,

the OECD or Euromod than this (too) unusual study.

[1] We would like to thank Juliette Stehlé, who provided assistance in clarifying certain points in this note.

[2] See Landais C., T. Piketty and E. Saez, *Pour une révolution fiscale* [For a tax revolution], Le Seuil, 2011.

[3] See also Sterdyniak H., “Une lecture critique de l’ouvrage *Pour une révolution fiscale*” [A critical reading of the work *Pour une révolution fiscale*], *Revue de l’OFCE*, no. 122, 2012. Note also that you cannot arrive at an overall judgment on the progressivity of the system from the case of a few super-rich who manage to evade taxes through tax schemes.

[4] Bigot R, É. Daudey, J. Muller and G. Osier: “En France, les classes moyennes inférieures bénéficient moins de la redistribution que dans d’autres pays” [In France, the lower middle classes benefit less from redistribution than in some other countries], *Consommation et modes de vie*, Crédoc, November 2013. For an expanded version, see: “Les classes moyennes sont-elles perdantes ou gagnantes dans la redistribution socio-fiscale” [Are the middle classes losers or winners from the tax-benefit redistribution], *Cahiers de Recherche*, Crédoc, December 2012.

[5] Also note that the INSEE underestimates somewhat the redistribution effected by the French system since it does not take into account the ISF wealth tax. It also does not include employers’ national health insurance, which in France is strongly redistributive as it is not capped. From the other side, it does not take account of indirect taxes.

[6] And replacement income such as unemployment benefits and sickness benefits.

[7] See Eidelman A., F. Langumier and A. Vicard: “Prélèvements

obligatoires reposant sur les ménages:

des canaux redistributifs différents en 1990 et 2010”
[Mandatory taxes on households: different channels of
redistribution in 1990 and 2010], *Document de Travail de la
DESE de l'INSEE*, G2012/08.

[\[8\]](#) Estimation from EUROMOD (2004): “Modelling the
redistributive impact of indirect taxation in Europe”, *Euromod
Working paper*, June.