# Rental housing: the CAE wants to change the ALUR …

By Pierre Madec and Henri Sterdyniak

On October 24th, the French Economic Analysis Council (the CAE) published a paper proposing a new policy on rental housing in France. This paper calls into question a number of government measures in the ALUR bill currently under discussion in Parliament, such as rent control and the universal rent guarantee (the GUL) [1]. Are these criticisms justified? The authors acknowledge that the housing market is very specific, that it requires regulation, and that the state needs to build social housing and assist poor families with housing. Their differences with the policy that the current government intends to follow are thus intrinsically limited, and are more related to means than ends. The free market does not work in the area of housing. There is a need for public intervention that should aim, as we shall see, at contradictory objectives, programmes whose structure is by their very nature subject to discussion.

## The existing rental housing stock: co-management and moral hazard

With regard to the private rental market, the authors in essence propose the introduction of a system of housing "flexicurity", akin to what has been recommended for the labour market: diversification and liberalization of leases, new rights for the landlord, more flexible conditions for terminating a lease, and the development of a system of co-management of the private rental market built around a "housing authority" whose powers would extend from setting "benchmark" rents to managing leases. This "authority", which would be jointly administered by tenants and landlords, would play a mediating role in conflicts between them, much like the

*prud'hommes* bodies for labour disputes. The main argument used by the authors to condemn a scheme such as the GUL universal rent guarantee is that it would create significant problems with moral hazard, that is to say, the guarantee would encourage those covered to take "too many risks". In this case, tenants, who would have a guarantee that any payment defaults would be covered by the fund, would be less concerned about paying their rent; they could therefore choose housing that is more expensive than what they really need. Owners would also be less concerned in their selection of a tenant. The authors also use the argument of moral hazard to defend the establishment of flexible leases: in their opinion, this would help in the fight against the deterioration of housing as well as in disputes with neighbours. The idea of tenants who are systematically "voluntary deadbeats" ready to degrade the housing they have leased seems simplistic and over the top. However, this idea is developed at some length by the authors. They seem to forget that the GUL will in particular cover tenants who are unable to pay their rent because of financial hardship (unemployment, divorce, etc.). This guarantee above all offers new protection for the owner – protection funded equally by landlords and tenants through a pooling system. In case of failure to pay rent, the landlord will be reimbursed directly from the fund. The latter will then examine the tenant's situation and proceed either with a mandatory collection or personalized support if the tenant is genuinely unable to pay. The GUL should allow landlords to rent to people who are in vulnerable situations (workers in precarious jobs, students from low-income families), without the latter needing to come up with deposits. Owners would have less incentive to seek safe tenants (civil servants, students from better-off families, employees of large companies). The State is fully within its role by covering a social risk that has been aggravated by the crisis and growing job insecurity. Isn't this worth the fantasized risk of an increase in moral hazard? The matter of the lease raises a question of substance. Should encouragement be given to the development of

individual landlords, which inevitably generates friction between on the one hand the owner's concern to freely dispose of their property and be as certain as possible that the rent will be paid and on the other hand the tenant's concern to enjoy a secure tenure and their demand for the right to housing? A household with a low or irregular income, which is thus more vulnerable, must also be able to find housing in the private sector. It may also seem preferable either to encourage institutional investors to invest in this sector or for households to make greater use of collective investment in housing and set up mechanisms such as the GUL, which can collectively address the issue of non-payment of rent. Housing is far from being an ordinary good. It is, and the authors do point this out, above all an essential need, a fundamental right. The massive casualization of housing through the establishment of a system of liberalized leases cannot be the solution. On the contrary, authors drawing on the German model, on the introduction of open-ended leases (the standard lease in Germany), constitute a major advance in terms of the tenant's security [2].

## Rent control versus the law of the market

With regard to rent control, the authors rely on a number of studies in order to demonstrate the existence of a correlation between the state of degradation of the rental stock and rent control measures. However, the ALUR law contains provisions for taking into account any renovations undertaken. There is of course a continuing risk that the stock will deteriorate, but once this has been spelled out, we should also mention the equally likely result that the stock could improve precisely due to this provision for taking renovations into account. The authors also develop the idea that control measures will lead to a significant decrease in residential mobility. While this is a real risk for programmes designed to regulate rents during the lease and not upon re-letting (the main cause of the growing inequality in rents observed in France since the

1989 Act), the rent control provisions in the ALUR law are, on the contrary, designed to lead to a convergence in rents [3]. This convergence, although modest, given the large gap still allowed (over 40%), will tend in the direction of greater mobility. In reality, the most important risk raised by the authors is that the number of dwellings available for rent might fall. Although it seems unlikely that landlords already on the market would massively withdraw their rental properties [4], rent control measures could discourage new investors in the rental market because of the resulting decline in yields. This would exacerbate the supply / demand imbalance in high-pressure areas. In practice, this seems unlikely. Even if there were a significant drop in the number of new investors, those already present on the existing market, given the lease conditions (and contrary to the authors' expectations), cannot easily sell their property, except to a new investor who in light of the fall in yields will demand lower prices. The tax incentive schemes (Duflot type) currently in force on the market for new housing suggest that landlords who invest will be only slightly affected by rent control. Some investors may nevertheless turn their backs on the construction of new housing, which, in the short term, would tend to push down property prices [5], thus encouraging homeownership and a fall in land prices. The public sector would however have to be ready to take over from private investors. Nearly one in three households in the first income quartile (the poorest 25%) is a tenant in private housing and is subject to a median housing burden, net of housing assistance, of 33%, an increase of nearly 10 percentage points since 1996. Rent control above all offers protection for these low-income households – households that, given the stagnation in social housing and the increasing difficulty in getting on the property ladder, have no choice other than to rent housing in the private sector. As the approach proposed by the Duflot Act consists of "putting in place a rent control framework to cut down on landlords' predatory behaviour. Not seeking to try to attract investors based on exorbitant rents and expectations of rising real

estate prices" does not seem illegitimate if it is actually accompanied by an effort in favour of social housing. Pressure on the housing market (where supply and demand are rigid) has permitted high rent increases, which is leading to unjustified transfers between landlords and tenants. These transfers hurt the purchasing power of the poorest, the consumer price index, competitiveness, and more. Conversely, these increases can stimulate the construction of new housing by pushing up the value of property, but this effect is low and slow (given the constraints on land). Rent control can help put a stop to rent increases, even if it undermines incentives for private investment in housing to some extent. It cannot be excluded *a priori*.

## Social housing mistreated

Even though the authors' observations seem fair – social housing does not play its full role, and the systems of construction and allocation are complex and inefficient – the solutions that they propose are less so, and are not very consistent. The debate on the role and place of social housing in France is old. Should it be reserved for poor households, thus abandoning the goal of social diversity? If this is done, should the eligibility ceilings be reduced, even though today more than 60% of the population might be entitled to social housing? Should social housing be profitable? Is there a sufficient supply of it? The idea put forward by the authors, according to which the State, through subsidized loans to housing agencies (HLMs), is to take care of housing only the poorest households, and must leave housing for the working and middle classes to competition (promoters and private investors), is open to criticism, especially in these times of economic crisis. What is needed, on the contrary, is to increase the share of social housing as well as intermediate housing at "moderate" rents that is built with public funds to house the lower classes at reasonable rents and reduce tensions in critical areas. The authors' idea that social

housing is not a right to be granted *ad vitam aeternam* seems justified. In 2006, according to the INSEE, more than one out of ten tenants in social housing belonged to the fifth quintile (the richest 20%). Unless one believes that social housing should, in accordance with the principle of social diversity, be open to all, then it is necessary to strengthen measures to encourage these households to leave social housing and direct them to the private sector, or accession needs to be tightened, as the additional rental charges currently applied are not effective enough. But the age of the occupants has to be taken into account, along with the availability of nearby housing at market rents. For housing the lower and middle classes (that is to say, “profitable” operations), the authors also suggest developing competition between private agents (developers, private builders, etc.). Once the amortization period of the loan from the Caisse des Depots et Consignations (CDC) expires, the housing thus built could change status and either switch into the private sector or be sold. This idea gives the impression that the shortage of social housing is the consequence of a lack of available funds. However, thanks to the amounts deposited in Livret A savings accounts, there is no lack of money. The brakes on housing construction are to be found elsewhere (lack of political will, lack of land, etc.). Even tType text or a website address or translate a document. hough it is necessary to fight against urban segregation and the way to do this is by “disseminating poor households throughout the urban fabric”, the proposals of the authors of the CAE note are not realistic. The index of spatial segregation proposed (see Box 10 in the working paper) would lead to no longer building social housing in areas where it is already significantly concentrated. However, given the land constraints in high-pressure areas, this is not feasible. The objective of the fight against segregation should not take priority over the goal of construction but complement it. Public funding that is rigidly conditioned on the value of one or two indicators, even the most transparent ones, as proposed by the authors,

would be extremely complex to implement. The SRU law establishing identical goals for communes with very different characteristics needs to be amended. Social housing needs to be built in accordance with need and demand. Currently, however, there is no match between supply and demand even in the less problematic areas (housing too big or too small, too old, etc.). According to the INSEE, 14% of social housing tenants are thus in a situation of over-occupation (twice the proportion seen in the private sector). Not only is entry into social housing difficult, but so is mobility within the sector. It is thus necessary to build social housing massively not only to accommodate new populations but also to house current social housing tenants in better conditions. Should the housing issue be de-municipalized? It is certainly a mistake to leave urban decision-making (and action) up to the municipalities alone, as some may be encouraged to give preference to selling off the available land to private developers rather than to housing agencies, whether this is directly for financial reasons or in an effort to attract a relatively affluent population without social problems. Housing policy thus requires strong incentives for the construction of social housing, including aid specifically for the municipalities where it is located, along with legal constraints and compensatory taxation targeted specifically at towns that have no social housing. The SRU Law is necessary. Note that proposals along these lines are difficult to get adopted at the political level. Thus, the measure to provide for inter-communal decision-making power regarding in particular the Local Urbanism Plan (PLU), a provision in the ALUR law, was largely rejected by the Senate, with the support of the Minister of Housing [6]. Similarly, the Union sociale pour l’habitat (social housing union), while deploring the lack of social mobility in the sector, regularly opposes any significant changes to the allocation process that could lead to greater mobility, with each organization striving to protect its own criteria.

## Rent and housing aid between taxation and imputation

In the CAE note, the way the tax system takes account of housing costs is the subject of questionable proposals. We agree of course with the starting point: it would be desirable to achieve a certain tax neutrality between income from financial capital and implicit rents. This is necessary from the point of view of both economic efficiency (not to overly encourage investment in housing) and social justice (given equal taxable income, a landlord and tenant do not have the same standard of living). But we believe this can be done effectively only by taxing implicit rents. It is difficult to undertake such a reform today, when substantial tax increases have already occurred. It would be difficult to introduce a new tax. This would therefore have to be accompanied by an upward translation of the tax brackets, so that, if owners pay more, tenants pay less. This could, furthermore, divert some households from building housing; the proceeds would be used in part for the construction of housing, which is inconsistent with the previous proposal to use these to reduce tenants' taxes. This would thus have to be introduced only very gradually. First the property tax bases would be re-valued. Then this database (from which landlords accessing it could deduct borrowing costs) could be used to tax the rental values at the CSG (wealth tax) or IR (income tax) rates (with some deduction). Fearing that this measure would be unpopular, the authors suggest that tenants could deduct their rent from their taxable income (with a relatively high ceiling of around 1000 euros per month). This proposal is not acceptable: – it is arbitrary: why not also deduct, still with ceilings, spending on food (no-one can live without eating) or on clothing, transportation or mobile phones (now indispensable). This could go on forever. The IR tax scales already take into account the need for a minimum income level (for a couple with two children, taxation only kicks in above a wage income of 2200 euros per month). The authors' measure would privilege housing costs over other spending, with little justification;

– the tax savings achieved in this way would be zero for non-taxable persons, and low for those near the taxation threshold: a family with two children and an income of 3000 euros per month with 600 euros in rent would pay 700 euros less tax; a wealthy family taxed at the marginal rate of 45% could save 5400 euros in tax, or 450 euros per month, that is to say, more than the housing benefit of most poor families; – the measure would be very costly. The authors do not give us a precise estimate, but lowering the taxable income of 40% of the 18 million taxable households in France (the proportion of tenants) by 10,000 euros could reduce IR tax revenue by 14 billion. In fact, this must necessarily be offset by a downward translation of the tax brackets. At the end, here, too, if the tenants pay less, the landlords pay more. Furthermore, the measure would be less effective economically than the taxation of implicit rents, since it would introduce a bias in favour of housing costs and does not take into account the value of the property occupied. The authors propose integrating the housing allowance into the IR tax and having all this managed by the tax administration, which would be responsible for developing a coherent redistributive policy on behalf of people on low incomes. While the current system of housing assistance can of course be improved, once again the authors' analysis is one-sided, and does not include all the aid given to the poorest (the "RSA socle" – basic income supplement for the unemployed; the "RSA activité" – income supplement for the working poor; and the "PPE" – in-work negative income tax). They forget that helping low-income people requires personalized support, in real time, on a monthly or quarterly basis, which the tax administration is unable to provide. In fact, they wind up with a system that is hardly simplified: the tax authorities would determine housing assistance for non-taxed households that the CAF Family Allowance fund would pay monthly and which would be adjusted by the tax administration the following year. But it is left unsaid whether the same formula would apply to the RSA income supplement. For taxable persons, the assistance would be

managed by the tax authorities. The authors tell us that, "the aid could not be less than the current housing allowance", but their proposal would greatly increase the number of untaxed households for whom it would be necessary to compare the tax savings and the allowance using the old formula. This is not manageable. It would of course be desirable to simplify the calculation of the housing allowance and to better integrate it with the RSA income supplement. This should be included in a reform of the RSA that the government needs to undertake (see the Sirugue report and the criticism of it by Guillaume Allègre), but the overall arrangement must continue to be managed by those who know how to do this, the CAF family fund, and not the tax authorities.

***Readers interested in housing-related issues should see the Revue de l'OFCE "Ville & Logement", no. 128, 2013.***

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[1] Trannoy A. and E. Wasmer, « La politique du logement locatif », Note du CAE, n°10, October 2013 and the document de travail associé [both in French].

[2] Note that the German market is very different from the French market (majority of renters, little demographic pressure, etc.), and that its rules cannot therefore be transposed.

[3] Currently, in the Paris region and more generally in all the so-called high-pressure neighbourhoods, the difference in rent between those who moved during the year and tenants who have been in their homes over 10 years exceeds 30% (38% for Paris) (OLAP, 2013).

[4] Indeed, "old" investors potentially have higher rates of return than do "new" investors.

[5] As the number of new households is tending to fall (Jacquot, 2012, "La demande potentielle de logements à

l'horizon 2030", *Observation et statistiques*, N°135, Commissariat au Développement Durable).

[6] An amendment according a low level for a blocking minority to France's "communes" during changes to the PLU (25% of communes and 10% of the population) was adopted by the Senate on Friday, 25 October – an amendment thereby reducing in practice inter-communal authority in this area.

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# No surprises from the Fed*

By Christine Rifflart

Not surprisingly, at its meeting on 29 and 30 October the Monetary Policy Committee of the US Federal Reserve decided to maintain its unconventional measures and to leave the federal funds rate unchanged. Since the end of 2012, the Fed has been making massive purchases of securities (government bonds and mortgage debt) at a rate of $85 billion per month. The aim is to put pressure on long-term rates and to support economic activity, including the real estate market.

The Federal Reserve, which is committed to a strategy of transparency and communication aimed at orienting investor expectations, also confirmed that it will hold the rate at between 0 and 0.25% so long as: the unemployment rate is greater than 6.5%; forecasts of inflation over 1 to 2 years do not exceed the long-term inflation target, set at 2%, by more than a half-point; and long-term inflation expectations remain stable. According to our forecast in October (see The United States: capped growth), the unemployment rate, which was 7.2% in September, could fall to 6.9% by end 2014. Finally, inflation, which was at 1.5% in the third quarter of 2013, should not exceed 1.8% in 2014. In these conditions, no rate

increase is expected before the second half of 2015. Policy will thus remain particularly accommodating.

There is greater uncertainty about the withdrawal of the unconventional measures than about keeping long-term rates at artificially low levels. A cessation or reduction of these measures was announced last May and is thus expected by the markets, and in any case they were not meant to last. Between May and September 2013, foreign private and public investors had anticipated the beginning of their withdrawal and began offloading some of their securities. This influx of securities depressed prices and led to a one-point increase in long-term public rates in just a few weeks. But the fragile character of growth, inadequate job creation and especially the public relations efforts undertaken by the central banks to reassure the financial markets led to putting off the actual date the purchases are to be curtailed. Long-term rates fell once again, and have continued to fall in recent weeks following the October budget crisis.

If, in retrospect, it appears that it was premature to anticipate an early withdrawal of the unconventional measures, the question of timing still remains. In its press release, the Committee stated that any decision will depend on the economic outlook as well as on a cost-benefit analysis of the programme. However, the economic situation is not expected to improve in the coming months. If Congress reaches a budget agreement before December 13, this will certainly be on the basis of cuts in public spending. This new fiscal shock will further dampen growth and penalize the labor market yet again. The issuance of new debt, which was compelled in 2013 by the statutory debt ceiling, might then grow very slowly in 2014 due to budget adjustments. Faced with this moderate growth in the supply of securities, the Federal Reserve could reduce its own purchases to the benefit of other investors. This could help maintain equilibrium in the securities market without a sharp fall in asset prices.

This normalization of monetary policy instruments should not be long in coming. But there are risks involved, and a sharp rise in long-term rates cannot be excluded. The markets are volatile, and the events of May and June have not been forgotten. But much of the movement has already been taken on board by the markets. The Federal Reserve will therefore have to beef up its communication strategy (by for example announcing in advance the date and scope of its decision) if it is to succeed the difficult balancing act of maintaining a highly accommodative monetary policy while gradually dispensing with its exceptional measures to maintain low interest rates. Let us assume that the exercise will be a success. Long-term public rates, at 2.7% in third quarter 2013, should not exceed 3.5% by the end of 2014.

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*This text draws on the study "Politique monétaire: est-ce le début de la fin ?" [Monetary policy: Is it the beginning of the end?], which is to appear soon in the OFCE 2013-2014 outlook for the global economy.

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# The euro zone quartered

By Céline Antonin, Christophe Blot, Sabine Le Bayon and Danielle Schweisguth

*This text summarizes the OFCE's 2013-2014 forecast for the euro zone economy.*

After six quarters of decline, GDP in the euro zone has started to grow again in the second quarter of 2013. This upturn in activity is a positive signal that is also being corroborated by business surveys. It shows that the euro zone

is no longer sinking into the depths of depression. It would nevertheless be premature to conclude that a recovery is underway, as the level of quarterly growth (0.3%) is insufficient to cause any significant reduction in unemployment. In October 2013, the unemployment rate stabilized at 12% of the workforce, a record high. Above all, the crisis is leaving scars and creating new imbalances (unemployment, job insecurity and wage deflation) that will act as obstacles to future growth, especially in certain euro zone countries.

Several factors point towards a pick-up in economic activity that can be expected to continue over the coming quarters. Long-term sovereign interest rates have fallen, particularly in Spain and Italy. This reflects that the threat of a breakup of the euro zone is fading, which is due in part to the conditional support announced by the ECB a little over a year ago (see Friends of acronyms: here comes the OMT). Above all, there should be an easing of fiscal austerity, given that the European Commission has granted additional time to several countries, including France, Spain and the Netherlands, to deal with their budget deficits (see here for a summary of the recommendations made by the European Commission). Driven by the same mechanisms that we have already described in our previous forecasts, a little higher growth should follow this easing of austerity (-0.4 GDP point of fiscal effort in 2013, down from -0.9 point in 2013 and -1.8 in 2012). After two years of recession in 2012 and 2013, growth is expected to come to 1.1% in 2014.

Nevertheless, this growth will not be sufficient to erase the traces left by the widespread austerity measures implemented since 2011, which pushed the euro zone into a new recession. In particular, employment prospects are improving only very slowly because growth is too weak. Since 2008, the euro zone has destroyed 5.5 million jobs, and we do not expect a strong recovery in net job creation. Unemployment could fall in some

countries, but this would be due mainly to discouraged jobseekers withdrawing from the workforce. At the same time, less austerity does not mean that there will be no austerity. With the exception of Germany, fiscal consolidation efforts will continue in all the euro zone countries. And whether this is achieved through a reduction in public spending or an increase in the tax burden, households will bear the brunt of the adjustment. At the same time, the persistence of mass unemployment will continue to fuel the deflationary pressures already at work in Spain and Greece. The improved competitiveness that results in these countries will boost exports, but at the expense of increasingly undermining domestic demand. The impoverishment of the countries of southern Europe is going to be aggravated. Growth in these countries in 2014 will again be lower than in Germany, Austria, Finland and France (Table).

As a consequence, the euro zone will be marked by increasing heterogeneity, which could wind up solidifying public opinion in different countries against the European project and making the governance of the monetary union more difficult as national interests diverge.

Table. Growth in the euro zone

In %

| | 2013 | | | | 2014 | | | | 2012 | 2013 | 2014 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 | | | |
| DEU | 0,0 | 0,7 | 0,2 | 0,3 | 0,3 | 0,4 | 0,4 | 0,4 | 0,9 | 0,9 | 1,5 |
| FRA | -0,2 | 0,5 | 0,0 | 0,2 | 0,3 | 0,4 | 0,4 | 0,4 | 0,0 | 0,1 | 1,3 |
| ITA | -0,6 | -0,3 | 0,0 | 0,1 | 0,1 | 0,2 | 0,2 | 0,2 | -2,4 | -1,8 | 0,4 |
| ESP | -0,4 | -0,1 | 0,0 | 0,0 | 0,2 | 0,3 | 0,3 | 0,3 | -1,6 | -1,4 | 0,7 |
| NLD | -0,4 | -0,2 | 0,3 | 0,3 | 0,3 | 0,3 | 0,4 | 0,4 | -1,3 | -1,1 | 1,1 |
| BEL | 0,0 | 0,2 | 0,2 | 0,4 | 0,4 | 0,4 | 0,6 | 0,6 | 0,3 | 0,1 | 1,6 |
| IRL | -0,6 | 0,4 | 0,2 | 0,3 | 0,4 | 0,4 | 0,4 | 0,4 | 0,1 | -0,5 | 1,4 |
| PRT | -0,4 | 1,1 | 0,0 | 0,2 | 0,2 | 0,3 | 0,3 | 0,3 | -3,2 | -1,7 | 1,0 |
| GRC | 1,1 | 9,6 | 0,5 | -1,1 | -3,9 | 1,2 | 1,3 | 1,5 | -6,4 | -4,1 | -0,4 |
| AUT | 0,1 | 0,1 | 0,3 | 0,3 | 0,4 | 0,4 | 0,4 | 0,4 | 0,6 | 0,4 | 1,3 |
| FIN | -0,2 | 0,2 | 0,3 | 0,4 | 0,4 | 0,5 | 0,5 | 0,5 | -0,8 | -0,9 | 1,7 |
| EUZ | -0,2 | 0,3 | 0,1 | 0,2 | 0,3 | 0,4 | 0,4 | 0,4 | -0,6 | -0,3 | 1,1 |

*Sources* : Eurostat, OFCE calculations and forecasts, October 2013.

# The crisis on a plateau

By Xavier Timbeau

This text summarizes the OFCE's 2013-2014 forecast for the world economy.

Six years after the onset of the financial and economic crisis, the acceleration in global growth expected in 2014 (Table 1) could have given hope for an end to the slump. While the sovereign debt crisis in the euro zone is of course over, and represents an important step, nevertheless aside from a few positive figures there is no indication that the crisis is at an end. Economic activity in the euro zone has reached a plateau, and the mechanisms underlying the sovereign debt crisis in the zone –in particular fear of default on public and private debt – could see the economies of the United States, Europe, the United Kingdom, and Japan plunge again at any time.

Table 1. Outlook for global growth

Annual growth rates, %

| | Share[1] of the total | Real GDP 2012 | Real GDP 2013 | Real GDP 2014 |
|---|---|---|---|---|
| EZ | 15,5 | -0,5 | -0,4 | 0,9 |
| GBR | 3,2 | 0,1 | 1,3 | 1,7 |
| USA | 20,8 | 2,8 | 1,5 | 2,4 |
| JPN | 6,3 | 2,0 | 2,0 | 1,0 |
| Developed countries | 53,5 | 1,3 | 0,9 | 1,7 |
| World | 100 | 2,8 | 2,5 | 3,1 |

1. Weighting based on 2008 GDPs and PPPs, estimated by the IMF.
*Sources*: IMF, OECD, national sources, OFCE calculations and forecasts, October 2013.

The crisis is global and has features that have been rarely if ever seen in the past. Sovereign interest rates are, for instance, exceptionally low, except in countries where the financial markets are skeptical, but which account for little in the overall mass of public debt. This indicates a situation

of a liquidity trap in which conventional monetary policy has reached its limits and where the ability of the monetary institutions to articulate a self-fulfilling future is crucial. However, as in the 1929 crisis, debate is raging about this capacity, raising numerous questions about an exit to the crisis. Monetary policy is at the heart of this uncertainty: are the extraordinary measures being taken stopping the economies from going over the brink? Would it be a good idea to lift these measures? Or is this really just an improvised makeshift with inflationary consequences that will be the source of the next crisis?

Economic activity, as measured by the GDP of the euro zone as a whole, is no longer contracting. Despite this, existing idle capacity is not being re-mobilized. Yet as long as the economies continue to be marked by idle capacity, the impact of the crisis will continue to be felt throughout the society. Wherever you look – GDP per capita, output gaps or unemployment – the indicators describe a plateau that is well below the level of 2007. The persistence of unemployment that is markedly above its equilibrium level is, for instance, swelling the ranks of the long-term unemployed, many without benefits. The high level of unemployment is undermining social cohesion and threatening societies built on integration through work. The unemployed are thrown onto family or social security benefits, which are themselves subject to fiscal cutbacks. Young people entering the labor market are facing delays in gaining access to employment and will long bear the scars of that initial period of joblessness in their wages and their careers.

But the impact of unemployment extends even further. The fear of losing one’s job or seeing one’s company close down or be relocated spreads to people with jobs whose salaries wind up being affected or who are forced to accept worse working conditions. Southern Europe for instance is engaged in wage deflation, and through the dynamics of competition, is drawing

in its neighbors.

The absence of a recovery is hardly surprising. A widespread massive programme of fiscal consolidation has been conducted in the developed countries. The total fiscal impulses from 2008 to 2013 can be used to make an assessment of the stimulation of the economies during the recession of 2008/09 and then of the fiscal consolidation that followed (Table 2).

Table 2. Fiscal Impulses 2008-2014

In GDP points

| | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2008-14 |
|---|---|---|---|---|---|---|---|---|
| DEU | 0,1 | 0,6 | 1,3 | -1,1 | -1,2 | 0,2 | 0,1 | 0 |
| AUT | -0,2 | 0,3 | 0,5 | -1,4 | -0,3 | -0,9 | -0,4 | -2,4 |
| BEL | 0,6 | 1,9 | -0,1 | 0,1 | -0,6 | -1,0 | -0,5 | 0,4 |
| ESP | 2,4 | 2,0 | -1,4 | -1,3 | -3,4 | -1,6 | -1,0 | -4,3 |
| FIN | -0,8 | 0,4 | 1,3 | -0,7 | -0,3 | -1,4 | -0,3 | -1,8 |
| FRA | -0,1 | 2,7 | -0,5 | -1,8 | -1,2 | -1,4 | -0,7 | -3,0 |
| GRC | 3,0 | 3,2 | -7,6 | -5,5 | -3,9 | -3,3 | -1,7 | -15,8 |
| IRL | 4,9 | 2,2 | -4,2 | -1,5 | -2,0 | -1,7 | -1,7 | -4,0 |
| ITA | -0,5 | 0,9 | -0,7 | -0,4 | -3,0 | -1,5 | -0,6 | -5,8 |
| NLD | -0,4 | 4,0 | -1,1 | -0,5 | -1,4 | -1,5 | -1,0 | -1,9 |
| PRT | -0,1 | 5,0 | -0,3 | -3,7 | -3,9 | -1,5 | -1,5 | -6,0 |
| EA (11) | 0,3 | 1,7 | -0,3 | -1,2 | -1,8 | -0,9 | -0,4 | -2,6 |
| USA | 3,0 | 3,8 | -0,8 | -1,3 | -1,4 | -1,5 | -0,7 | 1,1 |
| GBR | 0,6 | 2,8 | -2,7 | -3,2 | -0,5 | -1,0 | -1,0 | -5,0 |
| JPN | -0,9 | 4,8 | 0,5 | 0,5 | 0,5 | 1,9 | -1,3 | 6,0 |

*Sources* : National accounts, OFCE calculations and forecasts, October 2013.

The debate on the fiscal multipliers, using empirical analysis based on structural modeling or the systematic review of historical events, validates the causality that runs from fiscal impulses to output gaps. A large part of the output gap in 2013 is due to fiscal consolidation. There is no permanent impact of the crisis on activity, but there is the consequence of unprecedented fiscal austerity.

The developed countries have undertaken this consolidation effort under pressure from the financial markets, backed by the European authorities. The fear of facing difficulty in financing the public debt (a significant proportion of which

is renewed every year and which in the developed countries has a maturity of approximately 10 years) or of even losing access to finance altogether was reflected in higher sovereign yields and did not leave the States many alternatives. To regain credit, an ability to reduce the deficit had to be demonstrated, regardless of the price. The resulting consolidation was taken only as a preventive measure. The examples of Greece, but also Portugal, Spain and Italy, illustrate the risk of not having the public accounts in order. For some, including the economists of the European Commission, it was the massive consolidation undertaken by the Member States that made it possible to end the euro zone crisis. But there is an alternative explanation, one with heavy implications for the desirability of fiscal consolidation: the role played by the European Central Bank and the implicit commitments to solidarity on the part of the euro zone countries were more compelling than economic policies that prolonged and deepened the recession.

The reduction of public and private debt in the economies is the key to exiting the crisis. This demands a clear and reasonable strategy that combines restoring economic activity and cutting unemployment, while maintaining low sovereign interest rates and conducting fiscal consolidation at a moderate pace. This strategy requires mastery of timing, consistency in the policy adopted, and coordination between the States and between economic agents within the States. In the euro zone, this relies on a credible commitment by the Member states to fiscal consolidation in the medium term and a commitment by the European Central Bank to keep spreads at a minimum. Fiscal discipline by the markets does not work – it has to be opposed by a political commitment to economic stability.

# France: less austerity, more growth

By Eric Heyer

This text summarizes the OFCE's 2013-2014 forecast for the French economy.

In 2013, the French economy should experience annual average growth of 0.2%, which means that by the end of the year its level of production should return to the level of six years earlier, at the end of 2007. This mediocre performance is very far from the trajectory that an economy recovering from a crisis should be on.

The French economy did however have great potential for recovery: average spontaneous growth of about 2.6% per annum over the period 2010-2013 was possible and would have allowed France to make up the output gap accumulated in 2008-2009. But this "recovery" has been hampered mainly by the introduction of budget savings plans in France and across Europe. For the single year 2013, this fiscal strategy will cut economic activity in France by 2.4 GDP points.

The understanding that the fiscal multipliers were high came late, and occurred only after the austerity plans had already had a negative impact on growth. At the end of May 2013, this awareness pushed the European authorities to give additional time to six EU countries, including France, to correct their excessive deficits. The easing of the Commission's requirements provided a breath of fresh air that enabled the government to relax the austerity measures set for 2014. According to the budget presented in autumn 2013, the domestic impact of the austerity measures will be reduced by 0.5 GDP points between 2013 and 2014; since our partners are also relaxing their policies, a boost to external demand is also

anticipated. Overall, the easing of austerity will mean the addition of almost one point of growth in 2014 compared to 2013, despite the still high fiscal multipliers.

In these conditions, growth should come to 1.3% in 2014 on an annual average. By running at a rate still below its potential, the forecast growth will add to the output gap accumulated since 2008 and will continue to hurt the labour market. The unemployment rate in metropolitan France will rise slightly, reaching 10.9% by end 2014.

As a result of the easing of austerity, the public deficit will be higher than what was initially planned. It is expected to come to 3.5% of GDP in 2014, after reaching 4.1% in 2013, with gross government debt near 95% of GDP next year.

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# Is the euro area out of recession?

By Philippe Weil

At its meeting on October 9th, the Euro Area Business Cycle Dating Committee of the Centre for Economic Policy Research (CEPR) in London drew on the OFCE for this thorny issue (for the composition of this committee, which I chair, see here). The Committee's mission is to establish a chronology of recessions and expansions in the euro area, similar to what the National Bureau of Economic Research has done for the United States, dating back to 1854.

This chronology is valuable in two ways.

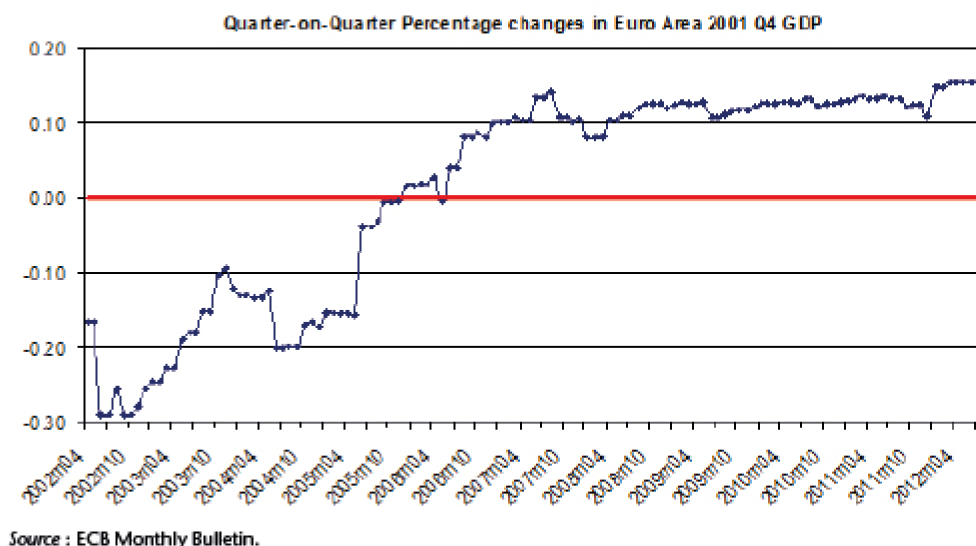
The first is that it allows economists to examine the characteristics of Europe's economic development. Do recessions tend to be short or long-lasting? Frequent or rare? Deep or mild? Is the euro area evolving in concert with the US economy? Is the slowdown in economic activity caused by the financial crisis unusual (more persistent than usual, sharper)? Without a clear definition of the timing of the ups and downs in Europe's economic activity and without a sketch of cyclical fluctuations, we cannot provide answers to these relatively basic questions.

The second advantage of this chronology is that establishing it requires an examination of all aspects of economic activity: GDP, of course, but also consumption, investment and especially employment (number of employed persons, number of hours worked). According to the CEPR's dating exercise, an expansion is a period in which every aspect of economic activity is growing significantly. It is not necessarily an episode of at least two consecutive quarters of GDP growth (much less one quarter!). For example, the CEPR Dating Committee has determined that the countries composing the future euro area were in recession during the period from the 3rd quarter of 1980 to the 3rd quarter of 1982, whereas real GDP had risen for several quarters during this time and it was higher at the end of the recession than at the beginning! The culprits were investment and employment, which fell sharply during this period.

To add to the complexity of the dating effort, the harsh reality of the world of economic statistics should not be forgotten: the statistics reach us late and are subsequently revised, sometimes significantly, over time. Unlike meteorologists who know the temperature at the top of the Eiffel Tower in real time, economists have no idea, for example, of the level of GDP for the current month or quarter. The first estimates are released only several months later (*e.g.* the first flash estimate of euro area GDP for the third

quarter of 2013 will be published by Eurostat only on 14 November 2013), and it might turn out that growth rates that seem positive based on preliminary estimates wind up after subsequent revisions to be negative – or vice versa. By examining all the determinants of economic activity (including employment), and not just GDP, the Committee is guarding against (so far successfully) the imperfections in this data so as to avoid, for instance, declaring the existence of a recession which turns out to be a statistical mirage that disappears after further review of the data. Thus, the Committee did not report [in September 2003] the existence of a recession between 2001 and 2003 even though the data showed a decrease in GDP during that time (but never, it is true, for two consecutive quarters). It concluded that there had been a prolonged pause during a period of expansion. This was a good move, as subsequent revisions of GDP cancelled these quarters of declining economic activity (see Figure 1). Its diagnosis was thus well advised.

**Figure 1. Quarter-on-quarter Percentage Changes in the Euro Area 2001 Q4 GDP (relative to the previous quarter)**




*Source* : ECB Monthly Bulletin.

So let's get back to the euro area in the state we see it in October 2013. The area hit a peak in economic activity in the 3rd quarter of 2011 and, since going into recession at that time, it experienced quarterly growth that was slightly positive in the second quarter of 2013. The first estimate for the third quarter of 2013 will not be known, as mentioned earlier, until 14 November. There are, it is true, several

corresponding indexes indicating that the cycle is in an upwards phase and that the macroeconomic outlook for 2014 is more favourable. But on 9 October the Dating Committee noted, nevertheless, that it would be premature at that time to conclude that the euro area was out of recession. Indeed, neither the length nor the strength of the putative recovery in economic activity was sufficient to conclude that the recession was already over. This judgment was not based on the absence at that point of two consecutive quarters of GDP growth because this is not the criterion that (mechanically) guides the Committee's thinking. Nor does it reflect any pessimism about the economic outlook for 2014, because the Committee is not in the business of making predictions. The Committee's assessment is based simply on a review of all the data available at the time it meets. The Committee has not excluded that the euro area is simply going through a pause in the recession it entered a year ago.

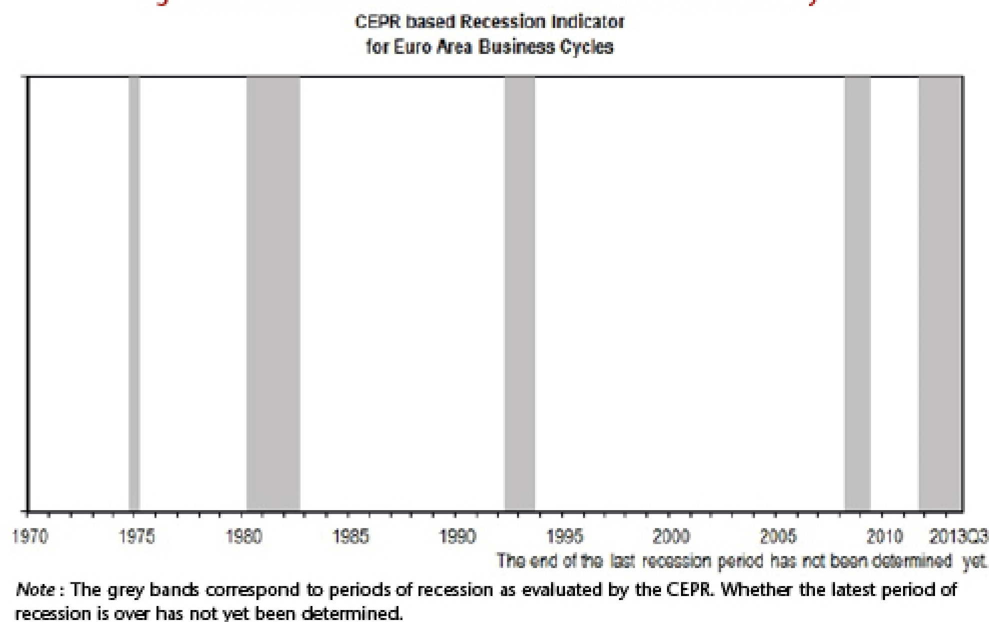



Figure 2. CEPR-based Recession Indicator for Euro Area Business Cycles

*Note* : The grey bands correspond to periods of recession as evaluated by the CEPR. Whether the latest period of recession is over has not yet been determined.

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# Why it's necessary to read Robert C. Allen: Global

# Economy History: A Very Short Introduction [1]

By Guillaume Daudin (Professor at the University of Paris-Dauphine, Researcher with the OFCE)

Robert C. Allen (born in 1947) has been Professor of Economic History at Oxford University since 2002. He defended his PhD thesis in 1975 at Harvard University. He has worked on a wide variety of topics and has received numerous awards for his publications. In 2009, his *The British Industrial Revolution in Global Perspective* was named Book of the Year by *The Economist* and the *Times Literary Supplement*. His research has focused on many aspects of the economic history of development: real wages, advances in agriculture, the sources of technical progress, the impact of imperialism, and sustainable development. He has been a key figure in the debate over the origin of divergences in development within Europe: he defends a unique position that stresses the importance of the material base (in Marx's sense) and of political choices rather than of the rest of the superstructure (culture, institutions, laws, etc.).

In 2011, he produced a very short book that was part of an English collection which resembles the "Repères" collection. It has already been translated into Italian, and may soon be available in French as part of the "Grands Repères" collection of Editions La Découverte. This book provides an excellent introduction to some of the ongoing debate on the comparative history of development in modern times. It focuses on the mechanisms for the start-up of long-term economic growth in each country.

The book's thesis can be formulated as follows. The British Industrial Revolution can be explained by the exceptional conjuncture of relatively high wages compared to the cost of

the island's capital and energy, which was due in part to the British Empire. This situation led entrepreneurs to develop technical innovations to save labour, even if this meant using production methods that were very capital and energy intensive. The modern economy was born.

The contrasting dissemination of the Industrial Revolution in the nineteenth century reflected the ability of each economy to implement the "standard model of development": the integration of the domestic market; the protection of industry from trade; the development of a banking system; and the promotion of mass education. Western Europe and North America were successful in doing this, other countries less so.

From the late nineteenth century, the technology gap between the rich and poor countries widened. Japan, the Soviet Union and Asia's newly developed countries succeeded only thanks to a determined policy on the part of the State. This involved simultaneously creating all the structures of the modern economy (steel mills, power plants, infrastructure, etc.). None of these investments would have been profitable in isolation. It was therefore necessary that the State ensure their coordination by developing policy simultaneously on every front. This is illustrated by the important role that Japan's Ministry of International Trade and Industry (MITI) played in the country's post-war development, using the example of steel. The MITI ensured that Japanese steel production was taking place on sites large enough to take advantage of increasing economies of scale; that the steel-consuming industries (*e.g.* the automotive industry) expanded fast enough to absorb the steel output; that Japanese consumers saw their wages rise fast enough to consume the goods produced (thus providing *ex post* justification for the decision to use capital-intensive production technology); and that foreign markets did not close.

This book undoubtedly provides a somewhat limited perspective on global economic history, since it is focused on

industrialization and its dissemination. It therefore leaves out a number of topics: inequality, finance, globalization, etc. It does not go very far back in history, and thus does not address the problems of development over the very long term. More fundamentally, perhaps, it is more a work on the comparative history of the economic development of nations than a work on global history *per se*. From a methodological viewpoint, it is Eurocentric in that it examines the dissemination of a European model, but this is not so much the case with regard to geographical coverage and documentation. Whole chapters are devoted to Africa and Latin America, continents that are rarely treated seriously in textbooks.

"Textbook" – so now the term is out. This book is indeed a textbook, an introduction to a broad and complex subject, and it must be judged accordingly. It is a short book that is better for not losing its focus. It defends a clear thesis, and the fact that it does not take into account the world in all its complexity has advantages. On the one hand, the thesis can be demonstrated more clearly, and it is easier to understand the dynamics. On the other hand, the reader (ultimately with guidance from the teacher) can more easily develop a perspective on the work and change their view by taking a critical approach.

The book differs from the economic history textbooks on the market in at least three ways:

- – As I have already mentioned, it has a truly global geographic coverage, whereas many textbooks focus on French or European history. This is, for instance, the book that introduced me to the adaptation of the techniques of the Japanese textile industry in an environment of low wages during the second half of the nineteenth century. This was also the book that introduced me to the role of Africans, the Krobo people in particular, in the development of cocoa farming in Ghana during this same period;

- – The book is well informed about recent advances in economic history. Currently, this field is partly dominated by Anglo-Saxon economists; their work is very rarely translated, and French historians are not very familiar with it;
- – Yet it is a very accessible book. It is illustrated by numerous tables and graphs. It is anchored in the concrete thanks to accurate descriptions of events that are unfamiliar even to specialists on the subject, as they concern national stories that to us seem distant. This can only encourage the reader to gain a better knowledge of the field.

I have taught economic history at HEC Paris, the University of Lille, Sciences Po, and now Paris-Dauphine. I wish this book had been available when I started my teaching: it would have helped me a lot. Reading in English is usually not a problem for graduate students, even if it is more difficult for undergraduates. I'm looking forward to a translation so that I can have all my students read it.

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[1] The book was published in 2011 by Oxford University Press.

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# In memoriam. Ronald H. Coase (1910-2013)

By Vincent Touzé

The American economist Ronald Coase, who died at 102 on 2 September 2013, has left us an exceptional body of work

distinguished by its simplicity and relevance.

As a pioneer of the theory of the firm, Ronald Coase believed that this type of structure had an undeniable capacity to reduce transaction costs and thus to efficiently organize economic activity outside the market ("The Nature of the firm", *Economica*, 1937). The firm's dilemma is: to do it (*i.e.* to produce directly) or to get it done (*i.e.* to use the market). In the absence of transaction costs on the markets, there would be no firms but only small autonomous production units. The transaction costs result from all the expenses associated with the purchase or sale of a product: remuneration of intermediaries, acquisition of information, search for the best price, etc. When these costs are too high, there is thus an opportunity to produce the good or service oneself. However, firms also face costs to get organized. Organizational theory was born.

As a supporter of free competition, Coase attributed market failures to the poor definition of property rights ("The Problem of social cost", 1960, *Journal of Law and Economics*, 3: 1-44). He was wary of costly regulations. He opposed Pigou (*The Economics of Welfare*, 1932, Macmillan), who recommended public intervention to deal with negative externalities. Instead, Coase called for better identification of property rights and for the role of the state to be limited to ensuring respect for these rights. This idea was synthesized as the "Coase Theorem" in 1966 by George Stigler in his book *The Theory of Price* (Macmillan). By focusing specifically on the interactions between law (the definition of property, the grounds and consequences of court decisions, etc.) and economics, Coase became one of the founding fathers of a new discipline, the economic analysis of law.

In the 1990s, the Kyoto Protocol popularized the "Coase Theorem" by proposing the establishment of trading in emission rights to regulate the amount of greenhouse gas emissions, *i.e.* the well-known "right to pollute". There were two

different approaches to controlling the emission of greenhouse gases: the sale of pollution rights, or the Pigou tax. The first approach involves assigning rights to emit gases in limited quantities. To produce the gases, one must possess rights. These rights are traded on a market where the price of gas emissions is determined by the interaction of supply and demand. The second approach is to assign an ad hoc price (Pigovian tax) to the marginal social cost of the externality. This tax is paid by the companies emitting the gas. The principle of pollution rights is often seen as more demanding (and so more constraining on companies) because the price of the gas emission is endogenous and the total quantity limited. With a Pigovian tax, the reverse is true. The price is fixed (or not very endogenous in the case of progressive taxation) and the quantity potentially unlimited.

Coase, who was devoted to simplicity in making presentations, unhesitatingly denounced the use of excessive mathematical formalism. In a profile published by the University of Chicago in 2012, he lamented that economics had "become a theory and math-driven subject". According to him, "the approach should be empirical. You study the system as it is, understand why it works the way it does, and consider what changes could be made in order to improve the system." He modestly concluded: "I've never done anything that wasn't obvious, and I didn't know why other people didn't do it. I've never thought the things I did were so extraordinary."

Coase's work won him the Nobel Prize in 1991.

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# Austerity in Europe: a change of course?

By Marion Cochard and Danielle Schweisguth

On 29 May, the European Commission sent the members of the European Union its new economic policy recommendations. In these recommendations, the Commission calls for postponing the date for achieving the public deficit goals of four euro zone countries (Spain, France, Netherlands and Portugal), leaving them more time to hit the 3% target. Italy is no longer in the excessive deficit procedure. Only Belgium is called on to intensify its efforts. Should this new roadmap be interpreted as a shift towards an easing of austerity policy in Europe? Can we expect a return to growth in the Old Continent?

These are not trivial matters. An OFCE Note (no. 29, 18 July 2013) attempts to answer this by simulating three scenarios for fiscal policy using the iAGS model. It appears from this study that postponing the public deficit targets in the four euro zone countries does not reflect a real change of course for Europe's fiscal policy. The worst-case scenario, in which Spain and Portugal would have been subject to the same recipes as Greece, was, it is true, avoided. The Commission is implicitly agreeing to allow the automatic stabilizers to work when conditions deteriorate. However, for many countries, the recommendations with respect to budgetary efforts still go beyond what is required by the Treaties (an annual reduction in the structural deficit of 0.5 percent of GDP), with as a consequence an increase of 0.3 point in the unemployment rate in the euro zone between 2012 and 2017.

We believe, however, that a third way is possible. This would involve adopting a "fiscally serious" position in 2014 that does not call into question the sustainability of the public debt. The strategy would be to maintain a constant tax burden

and to allow public spending to keep pace with potential growth. This amounts to maintaining a neutral fiscal stimulus between 2014 and 2017. In this scenario, the public deficit of the euro zone would improve by 2.4 GDP points between 2012 and 2017 and the trajectory in the public debt would be reversed starting in 2014. By 2030, the public deficit would be in surplus (0.7%) and debt would be close to 60% of GDP. Above all, this scenario would lower the unemployment rate significantly by 2017. The European countries could perhaps learn from the wisdom of Jean de La Fontaine's fable of the tortoise and the hare: "*Rien ne sert de courir, il faut partir à point*", *i.e.* Slow and steady wins the race.

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# France: why such zeal?

By Marion Cochard and Danielle Schweisguth

On 29 May, the European Commission sent the members of the European Union its new economic policy recommendations. As part of this, the Commission granted France an additional two years to reach the deficit reduction target of 3%. This target is now set for 2015, and to achieve this the European Commission is calling for fiscal impulses of -1.3 GDP points in 2013 and -0.8 point in 2014 (see "Austerity in Europe: a change of course?"). This would ease the structural effort needed, since the implementation of the previous commitments would have required impulses of -2.1 and -1.3 GDP points for 2013 and 2014, respectively.

Despite this, the French government has chosen not to relax its austerity policy and is keeping in place all the measures announced in the draft Finance Act (PLF) of autumn 2012. The continuing austerity measures go well beyond the Commission's

recommendations: a negative fiscal impulse of -1.8 GDP point, including a 1.4 percentage point increase in the tax burden for the year 2013 alone. Worse, the broad guidelines for the 2014 budget presented by the government to Parliament on 2 July 2013 point to a structural effort of 20 billion euros for 2014, *i.e.* one percentage point of GDP, whereas the Commission required only 0.8 point. The government is thus demanding an additional 0.6 GDP point fiscal cut, which it had already set out in the multi-year spending program in the 2013 Finance Act.

The table below helps to provide an overview of the effort and of its impact on the French economy. It shows the trends in growth, in unemployment and in the government deficit in 2013 and 2014, according to three budget strategies:

1. One using the relaxation recommended by the Commission in May 2013;
2. One based on the budget approved by the government for 2013 and, *a priori*, for 2014;
3. One based on an alternative scenario that takes into account the negative 1.8 GDP point fiscal impulse for 2013 and calculates a fiscal impulse for 2014 that would be sufficient to meet the European Commission's public deficit target of -3.6%.

**The different scenarios for deficit reduction in France**

In %

| | Relaxation (1) | | Approved budget (2) | | Alternative scenario (3) | |
|---|---|---|---|---|---|---|
| | 2013 | 2014 | 2013 | 2014 | 2013 | 2014 |
| Fiscal impulse | -1.3 | -0.8 | -1.8 | -1.0 | -1.8 | -0.2 |
| Unemployment rate | 10.5 | 10.6 | 10.7 | 11.1 | 10.7 | 10.5 |
| Growth | 0.2 | 1.3 | -0.2 | 1.0 | -0.2 | 1.7 |
| Public deficit | -4.3 | -3.6 | -3.9 | -3.1 | -3.9 | -3.6 |

*Source :* Authors' calculations based on the iAGS model.

According to our estimates using the iAGS model [1], the public deficit would be cut to 3.1% of GDP in 2014 in scenario (2), whereas the Commission requires only 3.6%. As a

consequence of this excess of zeal, the cumulative growth for 2013 and 2014 if the approved budget is applied would be 0.7 percentage point lower than growth in the other two scenarios (0.8 point against 1.5 points). The corollary is an increase in unemployment in 2013 and 2014: the unemployment rate, around 9.9% in 2012, would thus rise to 11.1% in 2014, an increase of more than 350,000 unemployed for the period. In contrast, the more relaxed scenario from the European Commission would see a quasi-stabilization of unemployment in 2013, while the alternative scenario would make it possible to reverse the trend in unemployment in 2014.

While the failure of austerity policy in recent years seems to be gradually impinging on the position of the European Commission, the French government is persisting along its same old path. In the face of the social emergency that the country is facing and the paradigm shift that seems to be taking hold in most international institutions, the French government is choosing to stick to its 3% fetish.

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[1] iAGS stands for the Independent Annual Growth Survey. This is a simplified model of the eleven main economies in the euro zone (Austria, Belgium, Finland, France, Germany, Greece, Ireland, Italy, Netherlands, Portugal and Spain). For more detail, see the working document Model for euro area medium term projections.