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January 11, 2021

**Statement by Mr. Huh and Mr. Yoo on France
(Preliminary)
Executive Board Meeting
January 13, 2021**

We thank staff for the well-focused report and Mr. Buisse and Mr. Rozan for their insightful Buff statement. We broadly agree with the thrust of the staff appraisal. France is one of the countries hit hardest by the Covid-19 pandemic and imposed strict and recurrent containment measures at national and regional level including two rounds of lockdowns. The French economy has been severely affected by the pandemic and lockdown measures, contracting by about 19 percent in the first half of last year. We commend the authorities' comprehensive and sizeable policy actions to protect lives and livelihoods and contain the negative impact on the economy. In particular, it is noteworthy that the household income shortfall has been much less than output loss during the period of severe outbreak and liquidity pressures on firms were successfully eased by a range of support measures. **We also take a positive note that the authorities' recovery plan, "Plan de Relance", focused on green and digital transformation of the economy is on the right track and France is leading a green recovery over the world.**

The economy is expected to partly rebound next year from the sharpest contraction but remains below the pre-crisis level in the near term. The outlook is highly uncertain, and risks continue to be dominated by the evolution of the pandemic. As two lockdowns that triggered a drastic decline in domestic demand were the main driver of the contraction, we agree with staff and authorities that the economic rebound in 2021 is predicated on the assumption of no further strict lockdown. We also positively note the assessment in the Buff statement that the cost of the second lockdown has been smaller than expected. We are somewhat cautious about the view of staff and the authorities that accumulated household savings support higher domestic demand and economic recovery. In other countries' cases, savings increased mainly in the richer group who has a lower propensity to consume and people may tend to keep more precautionary savings in the aftermath of the crisis. *We*

welcome staff comment on the savings accumulation by income level and a potential shift in saving and consumption behavior, and their macroeconomic implication. We also note that the dependence of France's exports on transport equipment and tourism and European countries also contributed to the drop in output during the pandemic. We are interested to hear staff's view on the need to diversify the composition and destination of exports. Staff's comment on the near-term forecast of France's exports in the context of the Brexit and continued trade tensions with the US is also welcome.

We support the staff's policy advice that the authorities should maintain adequate support to firms and individuals in the near term and take this opportunity to reorient the French economy towards greener and more productive economy. The massive support measures should be recalibrated to be more targeted to those most affected and vulnerable as the pandemic evolves. We welcome the authorities' recovery plan, "*Plan de Relance*", announced in last September. As laid out in the Buff statement, the recovery plan is rightly focused on the green transition, the competitiveness and resilience of the French economy and employment and social cohesion. We are confident that the focus of the recovery plan on green investment and digital transformation could help limit the scarring effects from the crisis and boost the productivity of the economy. We also share the staff's concern on reshoring and reiterate that government support for reshoring should be strictly limited to addressing national security concerns.

Amidst the ongoing spread of the virus and continued high uncertainty, strong and flexible fiscal support should be maintained in the near term and a medium-term fiscal consolidation should be considered once the recovery is on firm ground given high level of debt and elevated fiscal deficit. We agree that the authorities' fiscal support during the pandemic was timely and appropriate considering the size of initial output losses. ECB's accommodative monetary stance and support from the Next Generation EU Recovery Fund help the authorities keep fiscal space and provide sufficient support to the affected firms and individuals. However, fiscal support should be more targeted and shifted towards facilitating more productive and sustainable economy as the recovery becomes durable. We welcome the significant and permanent cut in three production taxes which is expected to boost competitiveness of industrial companies including SMEs and look forward to further reform to simplify and streamline the tax system while minimizing revenue losses. We welcome the authorities' commitment to the reforms of unemployment benefit and pension system and to safeguarding public funds.

We call for staff's and the authorities' due attention to the build-up of financial sector risks and rising risks of corporate insolvency. Government guaranteed bank loans as emergency support resulted in the accumulation of gross corporate debt and some sectors such as contact-intensive service sector are likely to face profit losses and increased delinquencies when government support measures are withdrawn. In the same vein, a rise in unemployment in the aftermath of the pandemic also could increase credit risk on property loans. While taking a positive note that banking sector in France would remain sound under the baseline scenario, we underline the importance of continued vigilance on the potential

risks from corporate and household insolvency and strengthening debt restructuring mechanisms. We are supportive of more use of equity-like financing to boost investment and business dynamism and to reduce risk from excessive leverage. *However, the use of direct state equity may cause a controversy on partial nationalization and business interference. Staff comment is welcome.*

We fully agree with the staff's view that policies should aim at boosting employment, particularly among the vulnerable including low-skilled workers and the youth, by facilitating job creation in dynamic sectors. To this end, the authorities need to recalibrate the eligibility and generosity of the short-time work scheme and strengthen retraining programs once the recovery takes hold while stepping up the ongoing reforms, reduce structural unemployment and increase labor force participation over the medium term.