

**FOR
INFORMATION**

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January 23, 2023

To: Members of the Executive Board

From: The Secretary

Subject: **France—Statement by the European Central Bank Representative**

Board Action: Executive Directors' **information**

Additional Information: For the Executive Board discussion on France to be held on Wednesday, January 25, 2023.

23 January 2023

**Statement by Rasmus Rueffer (ECB Representative) and Maddalena Perretti (Advisor) on
France – 2022 Article IV Consultation
IMF Executive Board Meeting**

25 January 2023

We would like to thank Messrs. Buissé, Grossmann-Wirth, Benac, and Ms. De Waziers for their informative Buff statement and Staff for their balanced Report. We broadly agree with Staff and share many of the main findings, in particular those related to the challenges facing the French economy and priorities ahead. We associate ourselves with the statement of Mr. Pösö and would also like to highlight the following items for emphasis.

While the IMF estimate for 2022 GDP growth is closely aligned with our assessment, the Staff projections for 2023 and 2024 appear slightly more optimistic. The December 2022 Eurosystem staff projections entail weaker growth for both 2023 and 2024 than IMF staff (0.4 percentage points lower than IMF figures in each year). The size and persistence of the current energy shock can affect the level of potential output through the capital and productivity channel. In fact, this shock can further disrupt value chains, reduce investment and R&D, reduce human capital accumulation, increase uncertainty and reduce business activity and dynamism. ECB staff generally agrees with IMF staff's assessment of the inflation outlook but would also emphasize that upside risks may come from wage pressures. Hourly compensation of employees remains the most elevated in the eurozone. Further, while short-term risks to activity are tilted to the downside, ECB staff would also add that medium-term risks to the growth outlook seem to be more balanced. Finally, energy shortages not mentioned in the Staff report could pose some risks, as energy supply over the coming months is highly uncertain.

We broadly concur with the thrust of the fiscal assessment by Staff, with significant risks to both the short- and the medium-term outlook. ECB staff agrees with IMF staff that fiscal policy should begin reducing the deficit in 2023. Eurosystem staff projections of the deficit ratio are very close to those by IMF staff. The expansionary fiscal measures implemented over the last few years have limited fiscal space, making very prudent policies going forward necessary.

We share the view that it would be desirable if measures cushioning the impact of high energy prices were better targeted than was the case in 2022. One reason for this is the need to put public finances on a more sustainable footing against the backdrop of increasing risks. While the measures implemented by the government from end-2021 were efficient in reducing the inflationary impact, they have been very costly to the budget. Any energy support measures still in place this year should therefore be temporary and targeted to the most vulnerable households and companies. They should also be tailored to preserving incentives to consume less energy and thus not eliminate the important price signal coming from a lack of supply of clean energy. Fiscal measures falling short of these principles are likely to exacerbate euro area inflationary pressures.

ECB staff agrees that medium-term fiscal consolidation efforts should take place mainly on the expenditure side. The consolidation strategy should rely on a strong commitment and clear specification of measures to control the evolution of public expenditure; this requires further reprioritization. The pension reform that is under discussion at this point would be instrumental, but would likely have to be complemented by other measures.

IMF staff's risk and policy assessment for the financial sector is broadly aligned with that of ECB staff. The IMF appropriately notes that systemic risks in the financial sector need to be monitored. This is particularly true as a worsening economic outlook can adversely impact corporate and household balance sheets on the back of accumulated vulnerabilities, related in particular to high and increasing levels of corporate indebtedness. Amid signs of still positive but decelerating mortgage lending and also real estate price growth, the monitoring of residential real estate risks is warranted in the context of household indebtedness stabilizing at levels above the average for the euro area.

ECB staff agrees with IMF staff on the appropriateness of the recent decision to increase the CCyB rate to 1%, given accumulated vulnerabilities and available capital headroom. In addition to preserving and strengthening resilience in the banking sector, additional capital buffers give the authorities greater leeway to release the buffers if adverse developments materialize.

The suggestion by IMF staff to explore a sectoral systemic risk buffer directed at corporate exposures should take into account the existing limits on large individual exposures of French systemically important institutions towards highly indebted large firms under Art 458 of the Capital Requirements Regulation. Finally, ECB staff is also of the view that the current borrower-based measures addressing risks in the residential real estate sector are appropriate.