France's economic health

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Introduction

- A standard vision of France in the US: A country in decline.
- Often shared by the French. Gloom and doom. Recent bestsellers; "La France qui tombe", "Le desarroi Francais"
- Reality is (as usual) more complex:
- A country with roughly the same productivity as the US.
- But with a few serious problems, especially high unemployment, inadequate higher education. (and the problems it shares with others: aging, immigration)
- A reform process at work: Slow, frustrating, but real.

1. Basic facts. Productivity, and work

Table 1. GDP per person, GDP per hour, and Hours worked per person (U.S.=100)

	GDP per person		GDP per hour		Hours per person	
	1970	2000	1970	2000	1970	2000
US	100	100	100	100	100	100
EU-15	69	70	65	91	101	77
France	73	71	73	105	99	67

Another way of looking at the facts: From 1970 to 2000:

U.S: GDP per hour : +38%. Hours per person: +26%. GDP per person: +64%

France: GDP per hour: +83%. Hours per person: -23%. GDP per person: +60%

Not a bad performance: Higher productivity growth than the US. Spent partly on consumption, partly on increased leisure.

Too good to be true?

2. A closer look at productivity

Reasons to be skeptical:

- High minimum wage. Puts the low-skilled into unemployment. And increase the productivity of those who remain employed.
- High wage costs. Firms use more capital, and so labor productivity increases. (Hotels without personnel).
- Relevant? Yes. When adjust, true productivity (what we call total factor productivity) is lower by about 10%.
- Perhaps a bit lower than the US. but still high.

3. The decrease in hours: market failure or preference for leisure?

Decomposing the change in hours per person, from 1970 to 2000:

$$\Delta \ln(\frac{HN}{P}) = \Delta \ln H + \Delta \ln(1-u) + \Delta \ln(\frac{L}{P_A}) + \Delta \ln(\frac{P_A}{P})$$
France $-21\% = -23\% -7\% -7\% -4\% -11\% -11\% -14\%$
U.S. $+22\% = -4\% -19\% -8\% -7\% -9\%$

where H is hours worked per worker, u is the unemployment rate, L is the labor force, P_A is the population of working age, and P is population.

So main factor: a decline in hours worked per worker. Not unemployment, not aging.

Why do the French work less? (mostly low hours per year for full time workers)?

- Preference for leisure? Quality of vacations. French are better than the Americans at enjoying leisure. (Was it different in the 1970s?)
- Higher income taxes? Some evidence, across countries, that it is partly the case.
- Result of (bad) legislation: The 35 hours week, introduced in late 1990s, motivated in part by the "lump of employment fallacy." Relevant, but only a ripple.

How much of each? A heated debate.

Now turn to the problems.

1. Unemployment

- Unemployment low until the early 1970s (lower than the US)
- Increased in the 1970s and the 1980s. High since. Today (with disagreements about the exact number): 8.3%.

Not the only country in Europe with high unemployment, but.

• Unevenly distributed:

Unemployment rate for the 15-24: 22%

Unemployment rate for the 55-59: 7% (US: 2%). And low participation rate: 53% (US 69%)

• Long duration: 40% unemployed for more than one year, and 20% for more than two years. (US: 17% for more than 6 months)

Why? In response to higher unemployment in the 1970s and 1980s, more generous and inefficient social insurance.

- On the supply side: Minimum income (RMI) and (fairly) generous unemployment insurance. Partly offset by a (badly designed) negative income tax.
- On the demand side: Minimum wage (partly offset by low social contributions by firms for low-wage workers).
- On the demand side: Employment protection. A heavy administrative and judicial component.
- A perverse twist. The two-tier contract structure: CDD and CDI. Why? The result: High protection for CDI. Bad jobs and unemployment spells for the young. (And long duration unemployment for the old if they lose their job).

2. The productivity growth slowdown

More recent than unemployment. A European, not French, disease:

Total factor productivity growth: U.S., EU, and France, 1980-2004. (Percent per year)

	1980s	1990-1995	1995-2000	2000-2004
U.S.	0.6	0.5	1.1	1.7
EU-15	1.1	1.2	0.9	0.4
France	1.4	0.0	1.4	0.5

Why? and what is in store for the future?

- Across the board? No
- In manufacturing? No. Roughly similar rates in US and France.
- Appears to come largely from three sectors, retail, wholesale, and financial services.
- Use of IT? If so, why?
- Organization of firms. US multinationals more efficient than national counterparts.
- Signs of change? Recent improvements in productivity growth in Europe, including France.

3. Higher education

- A two-track system
- A "Grandes Ecoles" elite track, with early selection based on mathematics.

But students and faculty largely unconnected to research.

- A University system, with no selection (but high attrition).
 - No competition, no autonomy. Low budget. Tenure early.
 - A parking lot to avoid alternatives (unemployment).
- Cost for France? Difficult to assess, but substantial.

Plus side: Well trained elite. Highly qualified civil servants.

Minus side: Inadequate matching. Inadequate training. Brain drain of researchers. Unhappy students.

4. External trade

On the surface, fine. Balanced trade. But composition is worrisome.

Share in high-tech exports (in percent):

	Chemicals	Household	Precision inst	Transport equipmt
France	11.3	6.5	7.4	69
Germany	18.5	20.6	17.0	24

A poorly diversified portfolio. A heavy role of the state. The lack of medium-sized firms.

1. Short term prospects

A robust expansion in progress. For Europe, and for France.

- Forecast growth: 2.1% for 2007. 2.1% for 2008
- Forecast inflation: 1.5% for 2007, 1.4% for 2008
- Budget deficit: 2.7% of GDP.

Broad based growth (consumption, investment, exports). Dangers. In the short run: The appreciation of the Euro.

How long it lasts depends on reforms in goods, financial, labor markets.

2. Medium run. Reforms in the goods and financial markets

 Goods and financial markets have become much more competitive. Two forces:

The unique EU market.

Deregulation.

• Driver has been Bruxelles (the European commission). Playing the role of the bad guy. (with the result of a no to the Referendum on the European constitution).

Largely done in tradables.

• Remains: Services, "non-tradables", government. Partly outside the scope of Bruxelles. Much slower progress.

Rejection of the "Bokelstein" directive on services.

Slow rationalization of the government sector. In France, "LOLF."

Some way to go.

3. Medium run. Reforms in the labor markets

Some slow progress. But politically hard under conditions of high, long unemployment. The main directions:

- From reliance on the minimum wage (SMIC) to negative income tax.

 Negative income tax was introduced in late 1990s. (called Prime a l'emploi, or PPE). But badly designed.
- Decrease in social contributions on low wages, but largely offset by an increase in the minimum wage (SMIC)
- Introduction of fixed duration contracts, to avoid the inflexibility of permanent contracts.
 - Largely perverse. A dual labor market.
- Reform of unemployment insurance. Longer duration of benefits in exchange for the obligation to take jobs if available. But the second part of the bargain was never implemented...

What can we expect from the new government?

Keep in mind: French view of markets (at best a necessary evil), of the state (as highly competent).

Reforms in the labor market.

More flexibility in employment protection. Move to a unique, and more flexible, contract.

More emphasis on and redesign of the negative income tax.

More pressure on the unemployed to accept jobs if available.

Reforms in the goods market.

Less obvious. And a risk of interventionist "industrial policy", even of some protectionism.

Reforms of the higher education system.

More autonomy, more competition. Perilous, but likely.

Tentative bottom lines

- A country which is fundamentally doing well.
- Problems? yes (always).
 some shared with others: (aging, immigration).
 some specific: Unemployment/Participation rates of young and old.
- Worries? yes (always).
 Higher education, competitiveness.
- A country looking, often in confused fashion, for the right mix between efficiency and social protection.
- A (slow) reform process—which may accelerate.