



**EUROPEAN
DEPARTMENT**

THE CONSEQUENCES OF THE PANDEMIC ON THE FRENCH ECONOMY: A VIEW FROM THE IMF

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Link to Report: [IMF- France 2020 Article IV Consultation](#)

OVERVIEW

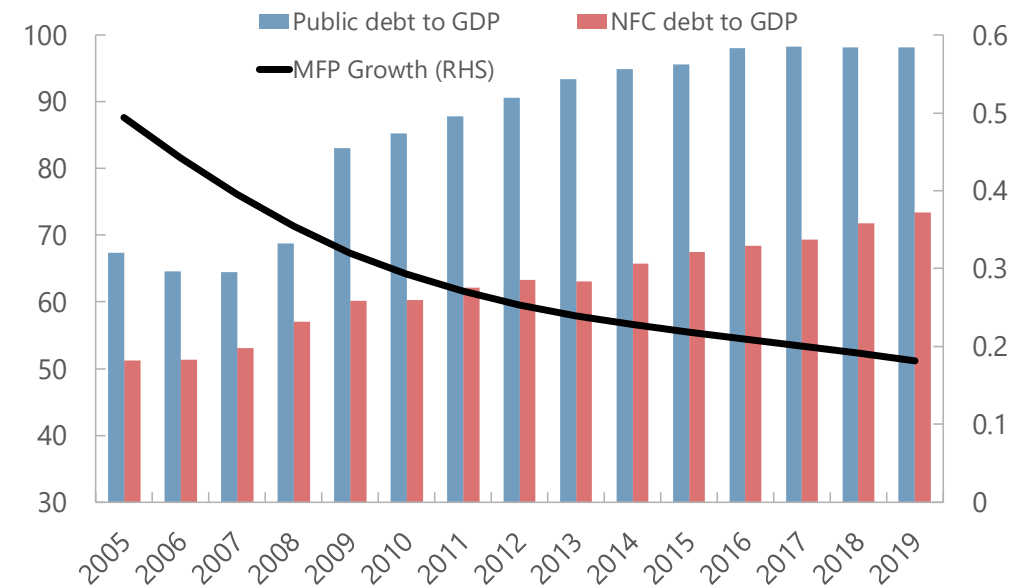
- **Pre-Covid Landscape & Covid Developments**
- **Outlook & Risks**
- **Policies**
 - *Maintaining Adequate and Sustainable Fiscal Support*
 - *Preserving Stability and Supporting Firm*
 - *Policies for a Sustained Economic Transformation*
- **Path Ahead**

A CHALLENGING PRE-CRISIS LANDSCAPE

- Slowdown in growth momentum in 2019, but labor market improved.
- Long-standing challenges, however weighed in on the pre-crisis outlook:
 - High public and private debt.
 - Sluggish productivity growth.
 - Inequality of opportunities.

Pre-Covid: Debt and Productivity

(Debt as percent of GDP; Trend multifactor productivity growth)



Sources: Haver Analytics, OECD; and IMF staff calculations.

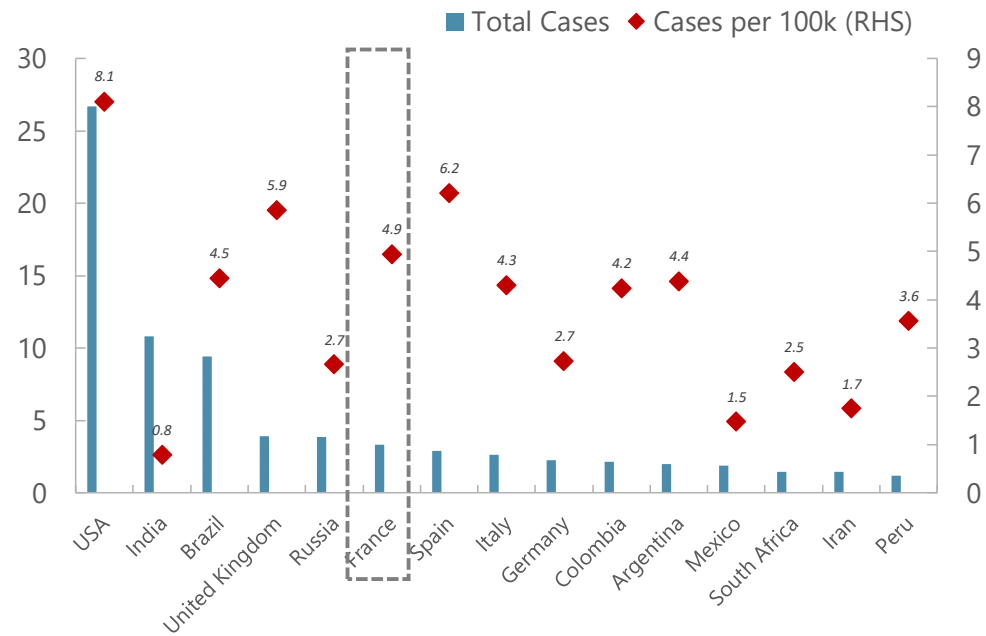
Note: NFC debt on a consolidated basis.

INTO THE STORM: IMPACT OF THE PANDEMIC

The COVID-19 infection swept rapidly and intensely through France, triggering an unprecedented health and economic crisis. France was among **the top-most affected countries worldwide**, both in terms of cases and mortality.

Covid-19 Cases in Selected Countries

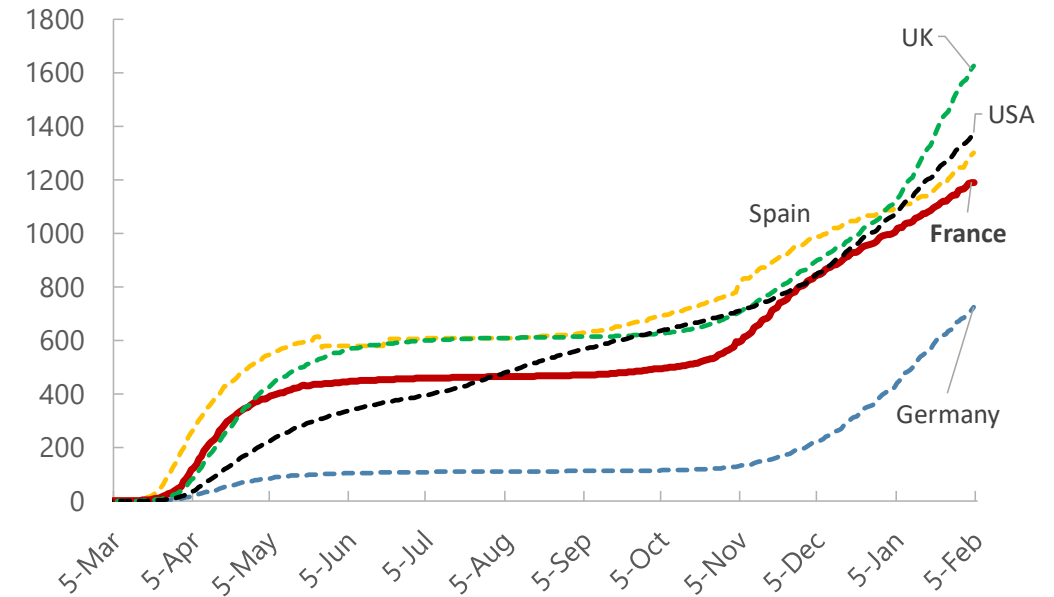
(Total cases in million on LHS and cases per 100,000 on RHS)



Sources: ECDC as February 5, 2021

Cumulative Covid-19 Deaths

(per million)



Sources: ECDC

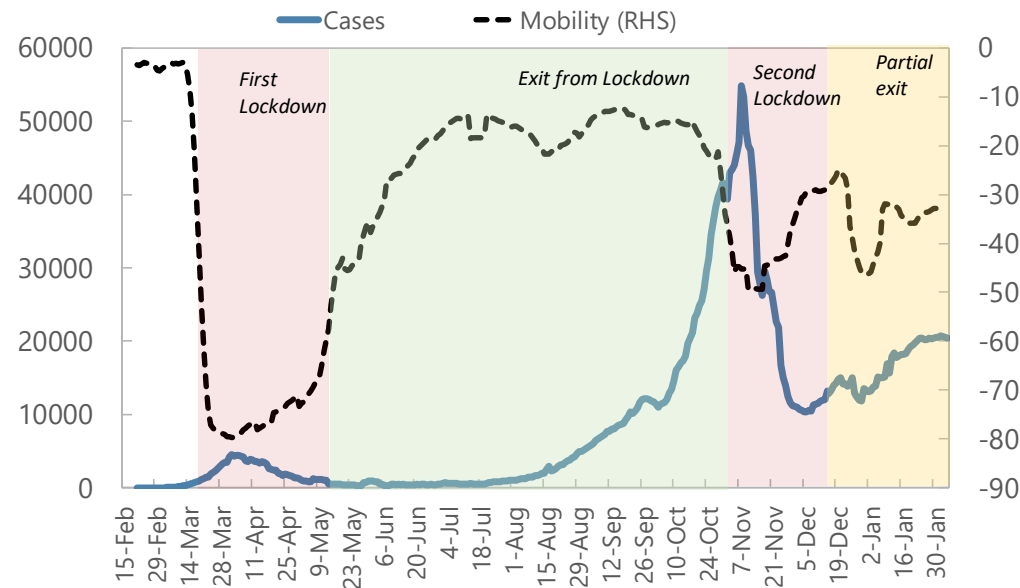
LOCKDOWN, RE-OPENING, LOCKDOWN, RE-OPENING,...

Several rounds of containment measures were instated to arrest the spread of the virus....

.... producing the deepest post-war recession, with output losses differentiated across sectors.

Covid-19 Infections and Mobility

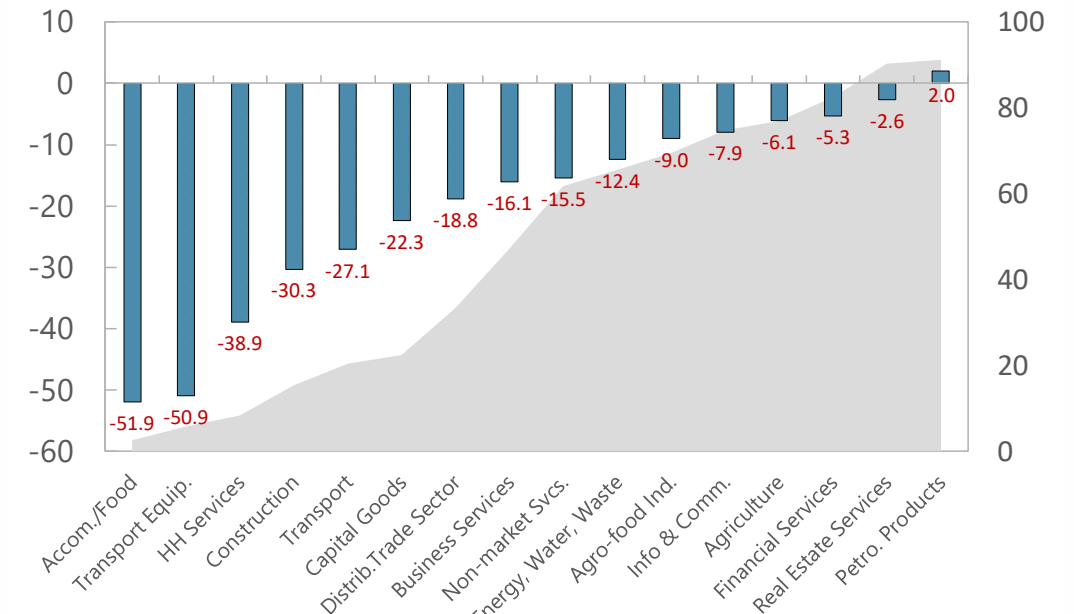
(7-day moving average of daily cases and mobility)



Source: Google Mobility (average of retail, workplace and transit), ECDC; and IMF staff calculations
 Note: Shaded area is period of lockdown (red) and phased reopening (green). Mobility is percent deviation from normal.

Change in Real Gross Value Added by Sector

(Percent change b/w 2020Q2 and 2019Q4, LHS; Cumulative GVA shares 2019, RHS)



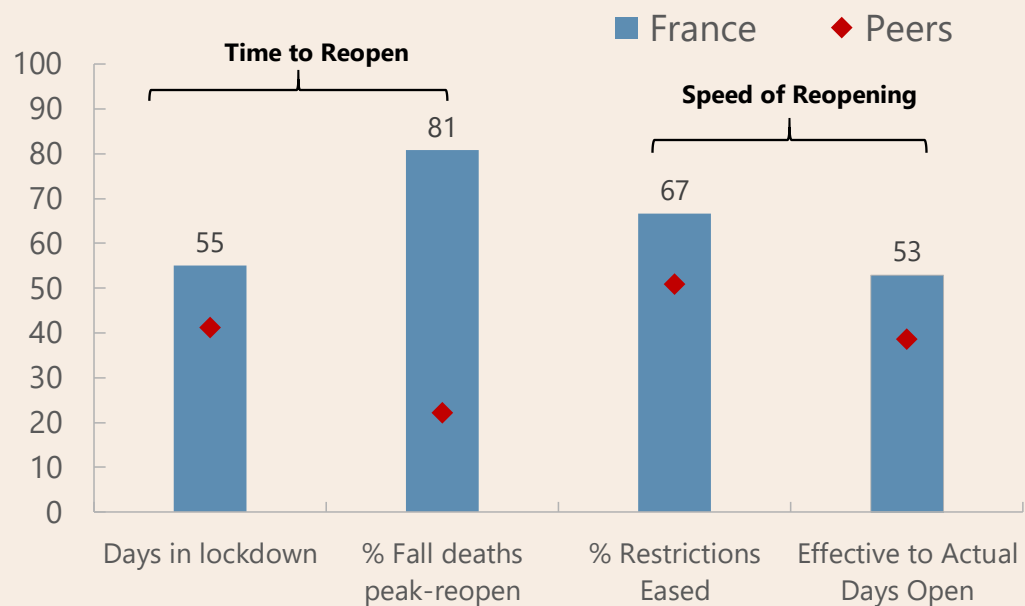
Sources: Haver Analytics; and IMF staff calculations.

ANALYSIS: HOW TO REOPEN SAFELY?

Late but fast reopening: France eased the first lockdown more rapidly than peers but waited longer to open..

.... Our analysis finds that a given reopening step is associated with worse reinfection outcomes for early & fast reopeners.

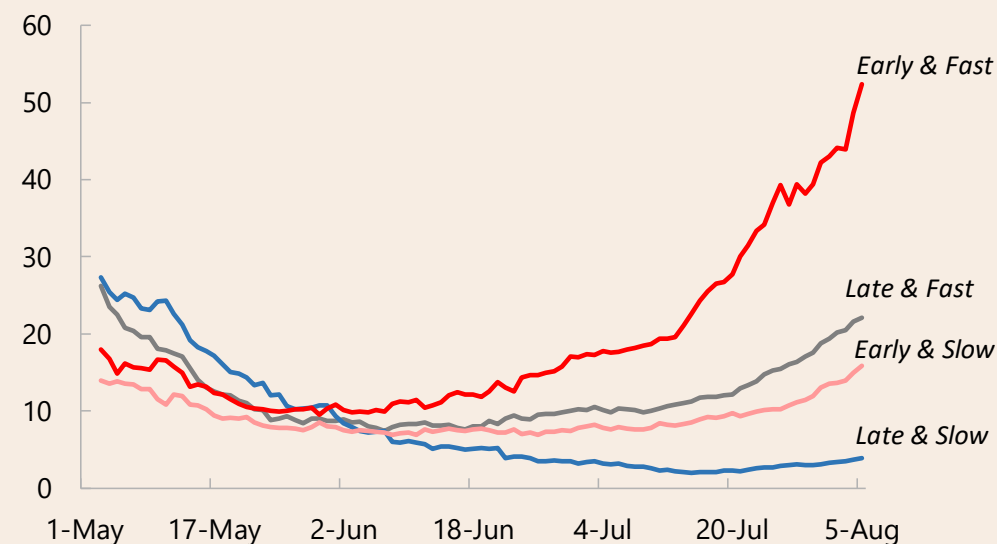
France vs. Peers: Lockdown & Reopening Strategy



Sources: IMF Staff Estimates. Peers are the sample of European countries in the reopening database by Franks et. al., 2020.

Re-infection Risk after Reopening

(predicted daily cases, 7 day moving average)



Sources: Google; Our World in Data; European Centre for Disease Prevention and Control; and IMF staff calculations.
Notes: The figures show in-sample fitted values using parameter estimates from Equation (2) in Annex 2.2 at a one-week horizon for mobility (panel 1) and a three-week horizon for daily cases (panel 2) and mean covariate values (including for reopening) for all four country groups.

See IMF WP: [Exit from Lockdowns: Early Evidence from Reopenings in Europe](#)

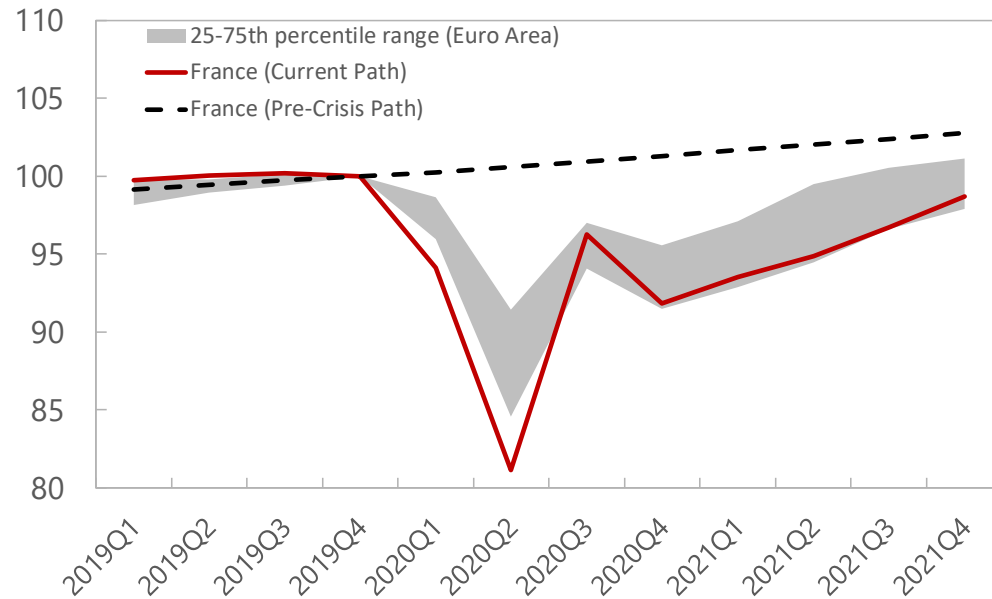
OUTLOOK & RISKS: A CLOUD OF UNCERTAINTY

We estimate recovery in 2021 to be incomplete with growth at 5.5 percent...

.... But the outlook can deviate materially from the baseline forecast depending on the virus dynamics.

Quarterly Real GDP Level - France & Euro Area

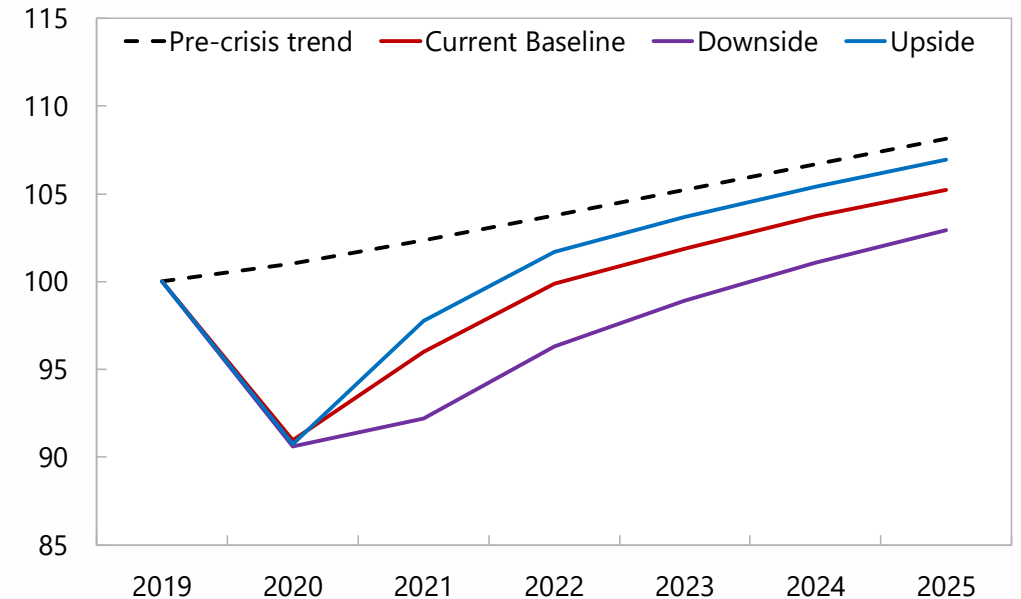
(2019Q4=100, forecasts for 2021)



Sources: WEO; and IMF staff calculations.

Annual Output Level under different Scenarios

(2019=100)



Sources: IMF staff calculations.

Policies (1)

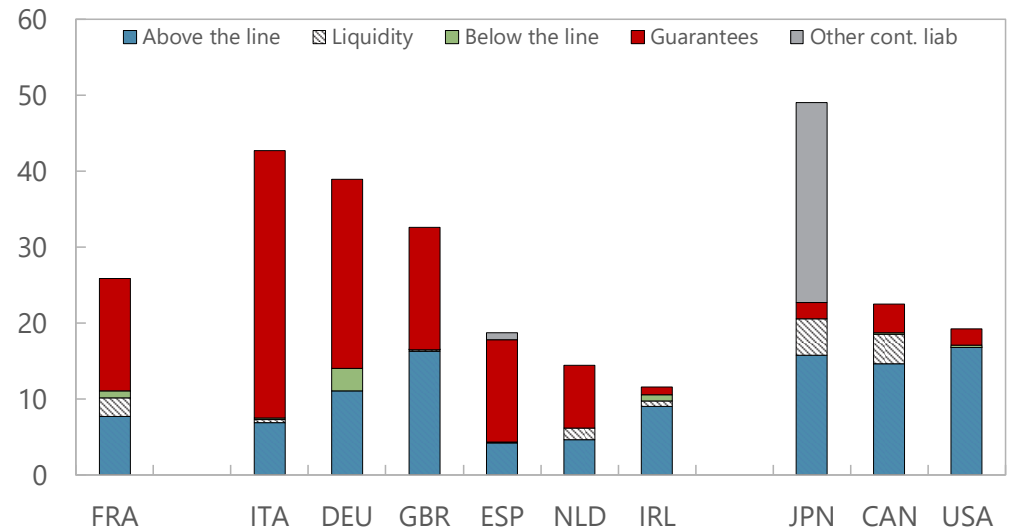
Maintaining Adequate and Sustainable Fiscal Support

FISCAL POLICIES: MAINTAINING ADEQUATE SUPPORT

- France's policy response to the crisis was **timely, flexible, and proportional** to the size of the shock.
- Support should be maintained and expanded as needed.
- As the recovery strengthens, [progressive targeting of support](#) would facilitate economic restructuring and contain fiscal costs.
- Maintaining current short-time work replacement rates for all sectors up to 2023 could be insufficiently targeted and disincentivize the reallocation of workers.

COVID-19 Fiscal Response

(Percent of GDP)



Sources: Fiscal Monitor database of Covid-19 measures (as of Nov. 6); and IMF staff calculations.

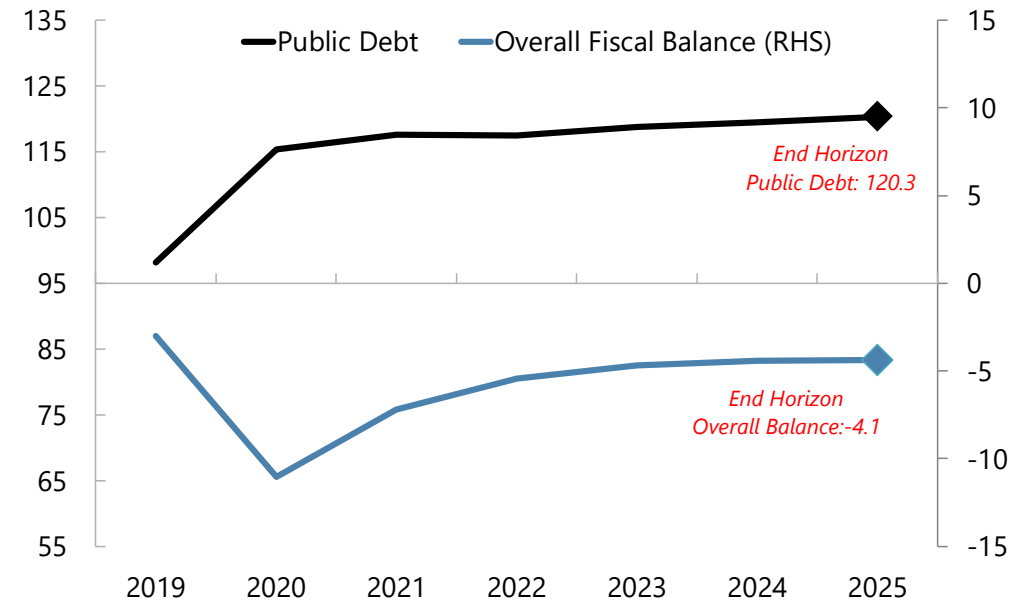
Note: Liquidity measures denote deferral of tax payments or accelerated refund of tax credits. Below-the-line measures include equity injections or asset purchases, government loans, debt assumptions, and nationalizations.

HIGH DEBT LEVELS REMAIN A CONCERN..

- Given the permanent output loss and substantial tax relief legislated before the crisis...
- .. under current policies (including EU Recovery Fund), the fiscal deficit and debt are **expected to remain elevated** over the medium term.

Annual Public Debt & Fiscal Balance

(Percent of GDP)



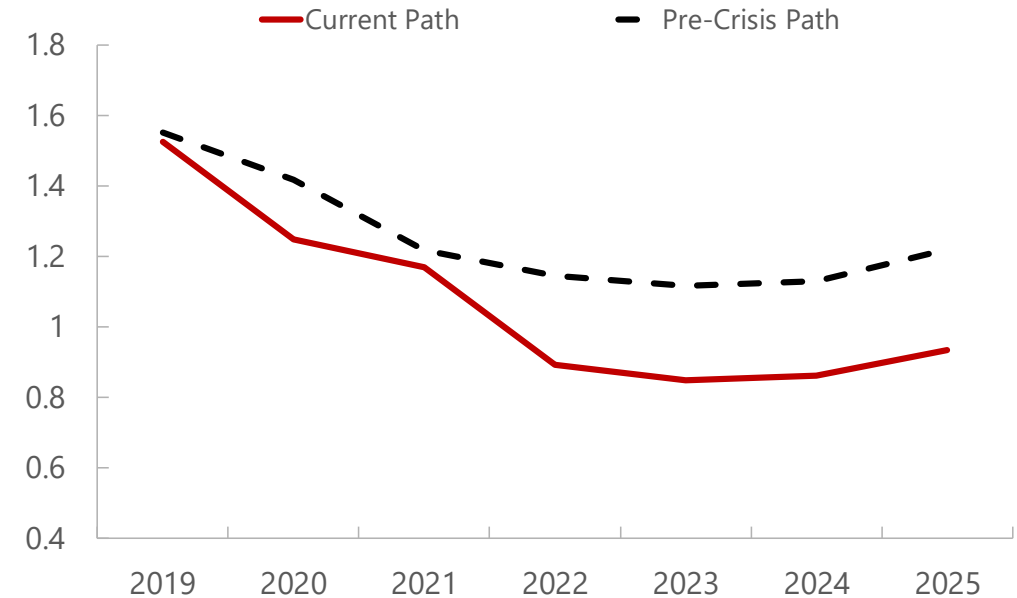
Sources: IMF staff calculations.

.. BUT “LOW FOR LONGER” OUTLOOK PROVIDES SOME BREATHING ROOM

- The exceptionally low interest rate outlook has provided some fiscal space during the crisis.
- A re-think of the appropriate medium-term objectives is warranted, including how and when to phase it in.

Effective interest rates

(Percent)



Sources: IMF Staff Calculations

FISCAL POLICIES: MEDIUM TERM SUSTAINABILITY

- An expenditure-based consolidation effort that aims to place debt on a downward path, will be needed over the medium-term:
 - The timing and pace of consolidation should remain state contingent, starting only when output has broadly recovered to its pre-crisis level and downside risks to growth have abated.
 - Planning process should start now.
 - Permanent expansionary measures should be avoided.
 - Planned reforms (unemployment, pension) should be implemented but further structural spending efforts will be needed.
- A sufficiently ambitious plan should:
 - Ensure debt remains sustainable, but also make space to reduce distortionary taxes further.
 - Provide for critical investment to reorient the economy in the post-crisis environment.

Policies (2)

Supporting Firms and Preserving Financial Stability

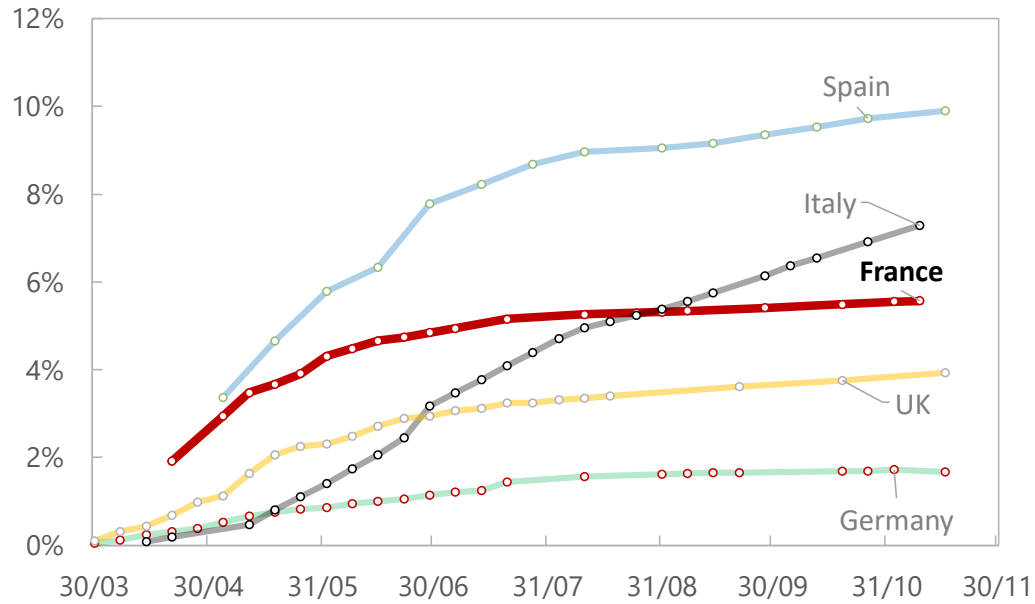
FINANCIAL POLICIES: FIRMS AT RISK

Emergency support, such as the guaranteed loan scheme, eased corporate liquidity pressures ...

.... but corporate debt spiked posing solvency challenges. Staff estimate an **equity gap equal to 1.3 percent of GDP** (~30bn euros).

Take-up of Guaranteed Loans

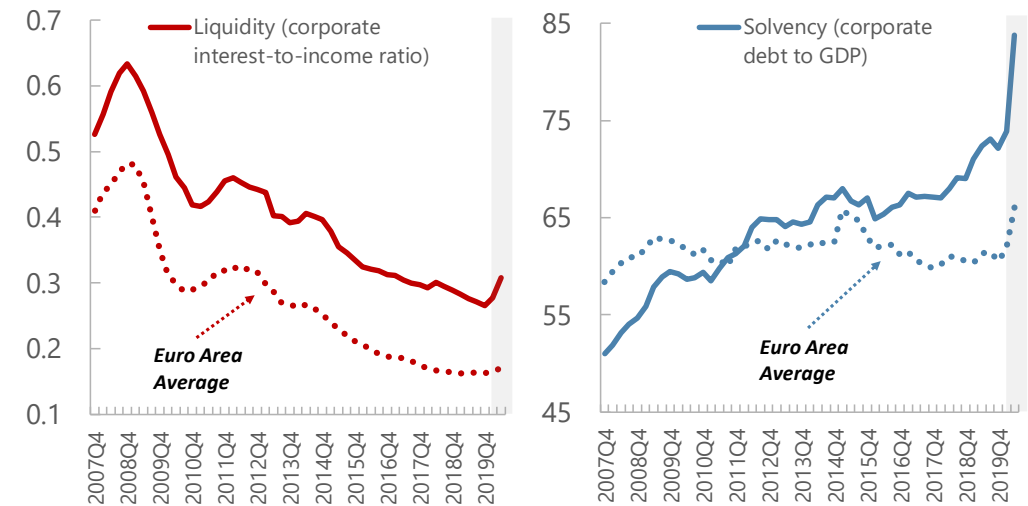
(weekly cumulative in percent of 2020 GDP)



Sources: Bruegel

Corporate Liquidity and Solvency

(Interest-to-income ratio, left panel; debt to GDP, right panel)



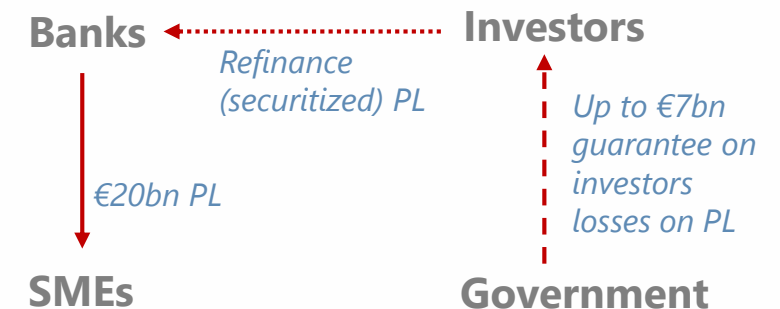
Sources: Euro Stat, Quarterly SNA. France in solid lines and Euro area average in dotted lines.

Debt is measured as net liabilities (loan & debt-securities) of NFCs; Interest-to-income is the total interest before FSIM allocation over gross disposable income (4q m.a.) of NFCs.

FINANCIAL POLICIES: SUPPORTING FIRMS

- Strengthening corporate balance sheets will be critical to the recovery:
 - Shift from liquidity support to targeted equity-like financing, as the emergency phase eases.
 - Design of equity-like support: (i) market-led selectivity (ii) well priced (iii) time-bound.
- France's *pret participatif*
 - combines desirable features of market-led selectivity and limiting the administrative burden for the government, but,
 - its complex design and pricing may preclude adequate take-up or prevent funds to go to firms with equity needs.
 - Augmented or adapt instrument if take-up is weaker than planned or equity needs persist.
- Enhance insolvency mechanisms to improve business dynamism.

France's Participatory Loan (PL) Scheme



ANALYSIS: FIRM DYNAMISM AND THE ROLE OF CREDIT

Aggregate productivity can be decomposed into the following factors:

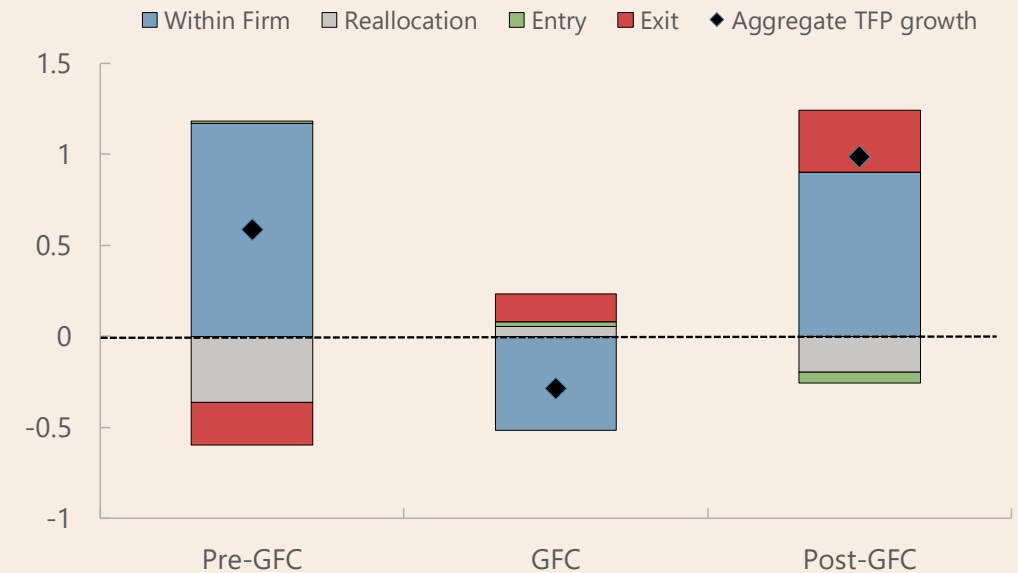
- **Within-firm adjustment effect:** Ability of continuing firms to adjust production process, incl when hit with a shock.
- **Firm dynamism:** exit of lower productivity firms and entry of higher productivity firms.
- **Reallocation:** Resources are reallocated from least to most productive firms

Firm dynamism and allocative efficiency did have a “cleansing effect” during the past crisis, but their contribution was small relative to continuing firms’ loss of productivity.

See Selected Issues Paper: [Firm Dynamism and Productivity in France: The Role of Credit](#)

Aggregate Productivity Growth: Contributors

(TFP percent change per year)



Sources: Orbis, IMF Staff Estimates

ANALYSIS: FIRM DYNAMISM AND THE ROLE OF CREDIT

We can further decompose the within-firm adjustment (main factor) into that coming from zombie vs. non-zombie firms:

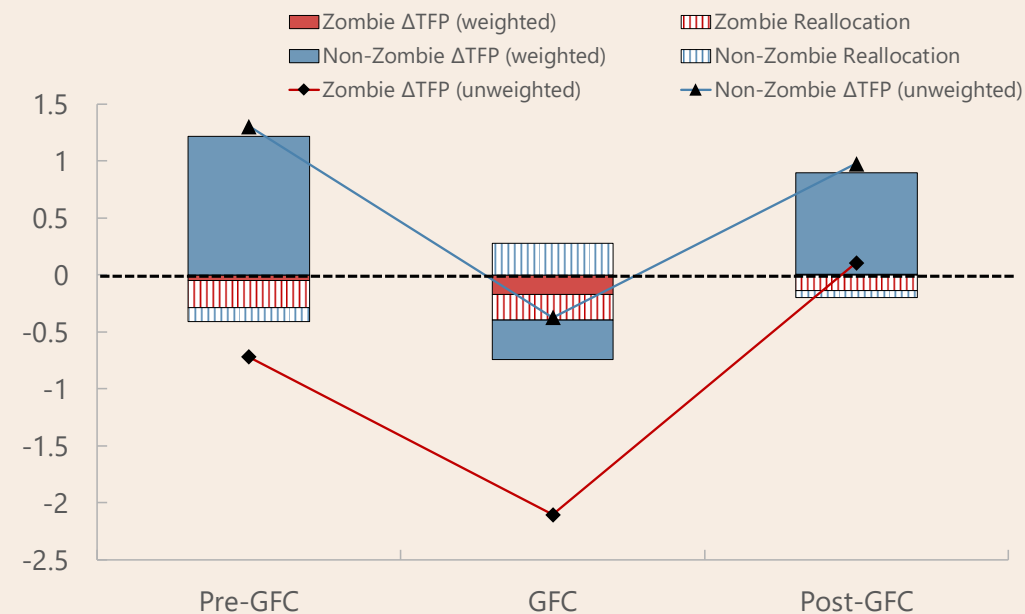
- **Zombie firms:** Firms aged 10 years and above and with an interest coverage ratio of <1.5 for three continuous years.
- Zombies represent 4 percent of continuing firms, but their mean productivity loss is six-fold lower.

Despite the small share, zombies exert a sizeable drag on aggregate productivity and can congest reallocation.

Policies should aim to expedite winding down of non-viable zombie firms, to facilitate capital reallocation and avoid long-run scarring from debt overhang.

Within Firm TFP Contribution: Role of Zombies

(TFP percent change per year)



Sources: Orbis, IMF Staff Estimates

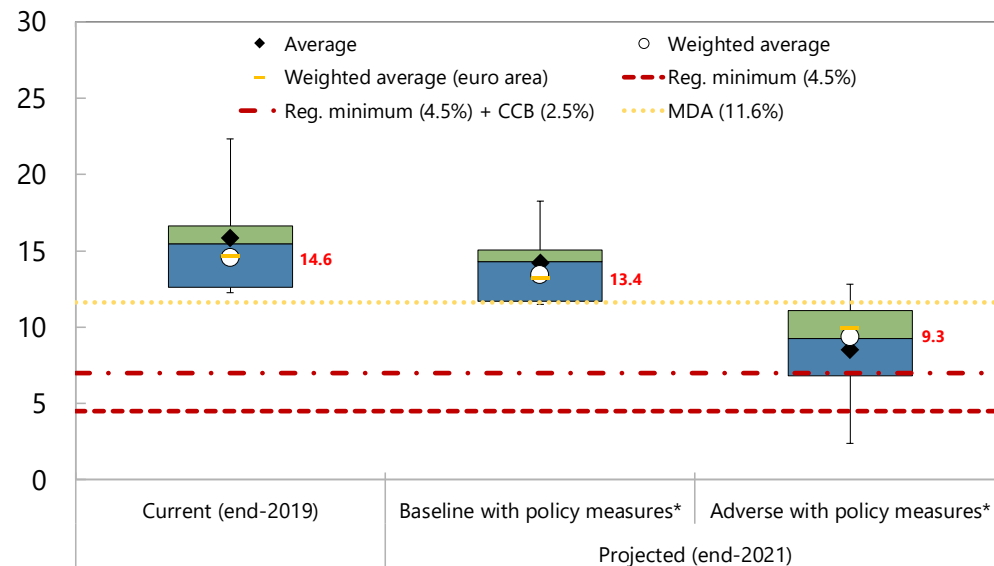
See Selected Issues Paper: [Firm Dynamism and Productivity in France: The Role of Credit](#)

FINANCIAL POLICIES: PRESERVING FINANCIAL STABILITY

Banks are adequately capitalized but may see capital depletions in an adverse scenario of slower recovery. Close monitoring of bank capital is warranted.

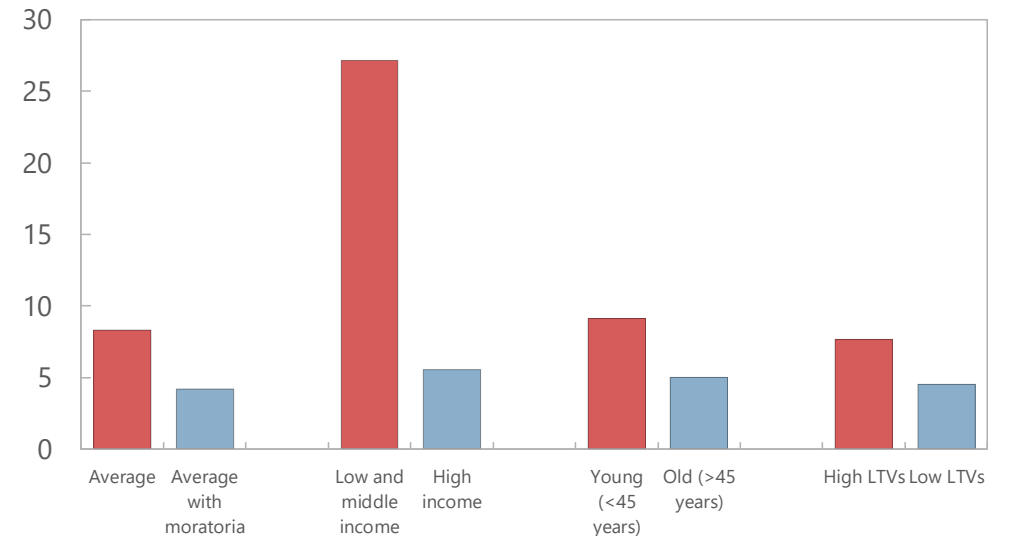
Future job losses could increase mortgage risk of low- and middle- income households.

French Banks—Solvency Stress Test (Baseline & Adverse)
(CET1 Capital Ratio, percent)



Sources: EBA; ECB; ESRB; FitchConnect; and IMF staff estimates.
Note: The blue and green boxes show the inter-quartile range with whiskers at 5th/95th percentiles. CET1=common equity Tier 1 for 8 French banks. */ Debt repayment relief (moratoria) for businesses and households as well as credit guarantees. The analysis covers all three channels affecting the capital adequacy ratio under stress: profitability, nominal assets and risk exposure.

Probability of Default on Mortgages Upon Job Loss
(Within 5 years of job loss, with unemployment insurance, percent)



Sources: ECB Household Finance & Consumption Survey 2020, OECD; IMF staff estimates.
Note: Estimates from *Household Sector Micro-Macro Simulation and Policy Analysis Amid COVID-19*, Gross and Tresselt (forthcoming).

Policies (3)

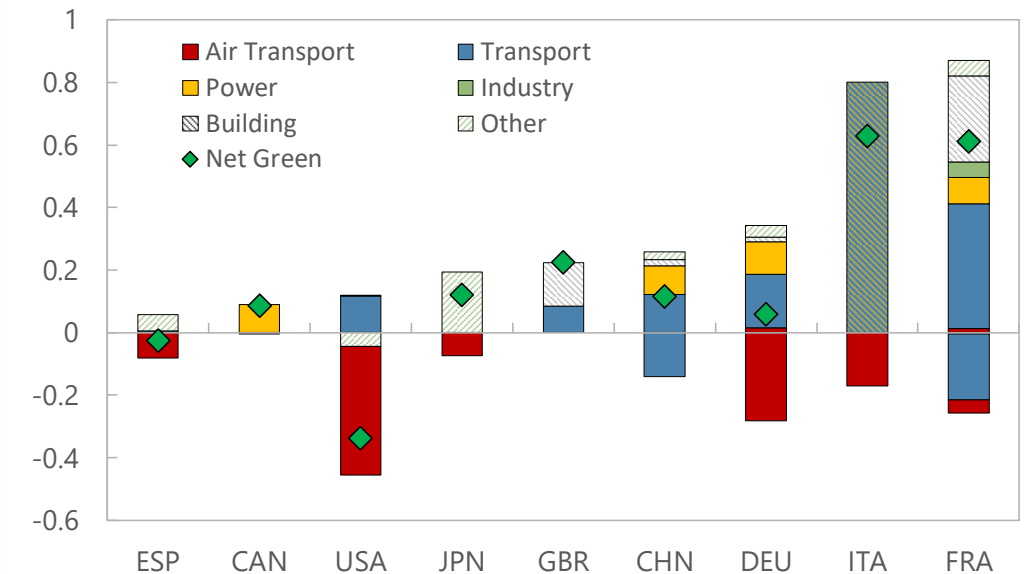
Accelerating a Sustained Economic Transformation

AIM FOR A JOB-RICH & GREEN TRANSFORMATION

- Improve productivity and boost employment by facilitating new work relationships in dynamic sectors:
 - Gradually **tightening the duration, generosity, and eligibility** parameters of the long-duration short-time work scheme.
 - Further steps to **increase competition and flexibility in product and service markets** can help boost productivity.
- France leads in incorporating climate friendly spending in recovery plans:
 - **Implement additional green policies** to reduce emissions, including by pricing carbon adequately across sectors.
 - This should be **accompanied by mitigating measures** for low-income households.

Green transition

(green(+) and climate negative(-) stimulus elements by industry, percent or GDP)



Source: IMF. 2020. Fiscal Monitor: Policies for the Recovery. Washington, October.

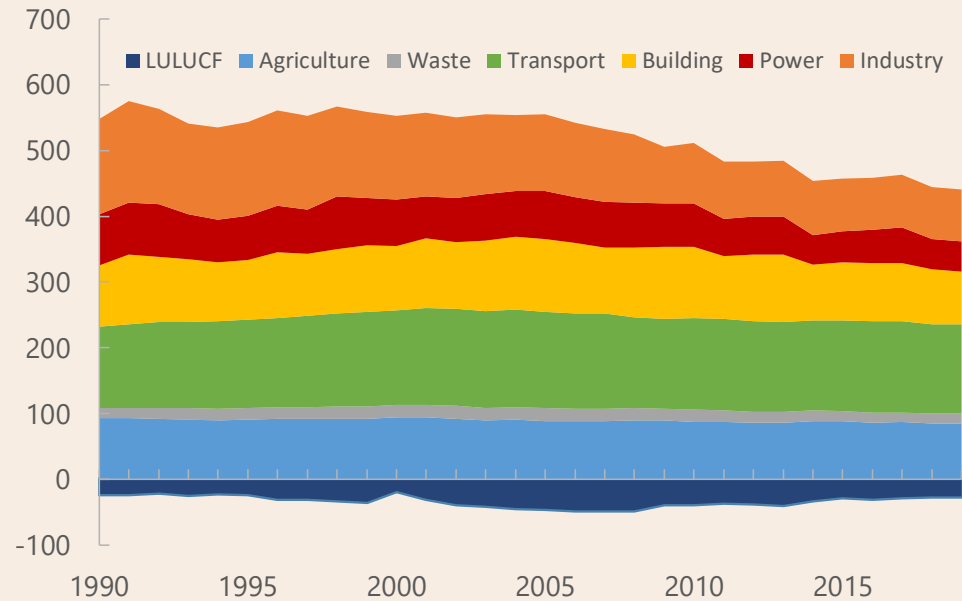
Note: Battery energy storage (R&D) investment support counted under transport.

ANALYSIS: CLIMATE MITIGATION POLICIES

Despite important progress, there remain large emission reduction potentials, especially in transport and in the housing sector.

Total GHG emissions

(MtCO₂ equivalent)

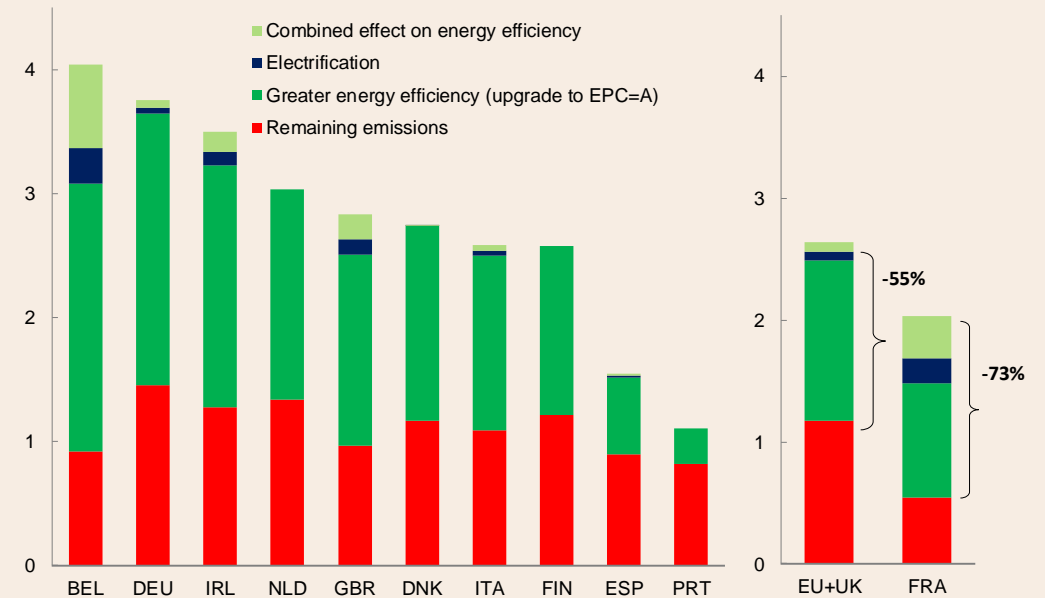


Sources: CITEPA

See Selected Issues Paper: [Climate Mitigation Policies in France](#)

Renovating the French housing stock would reduce related emissions by almost ¾ but requires support to overcome incentive and liquidity constraints.

EU+UK: Potential Emission Reduction from Renovation/Retrofitting (EPC=A) and Electrification (tCO₂ per capita, U.N. mean lifecycle emission projection per GWh)



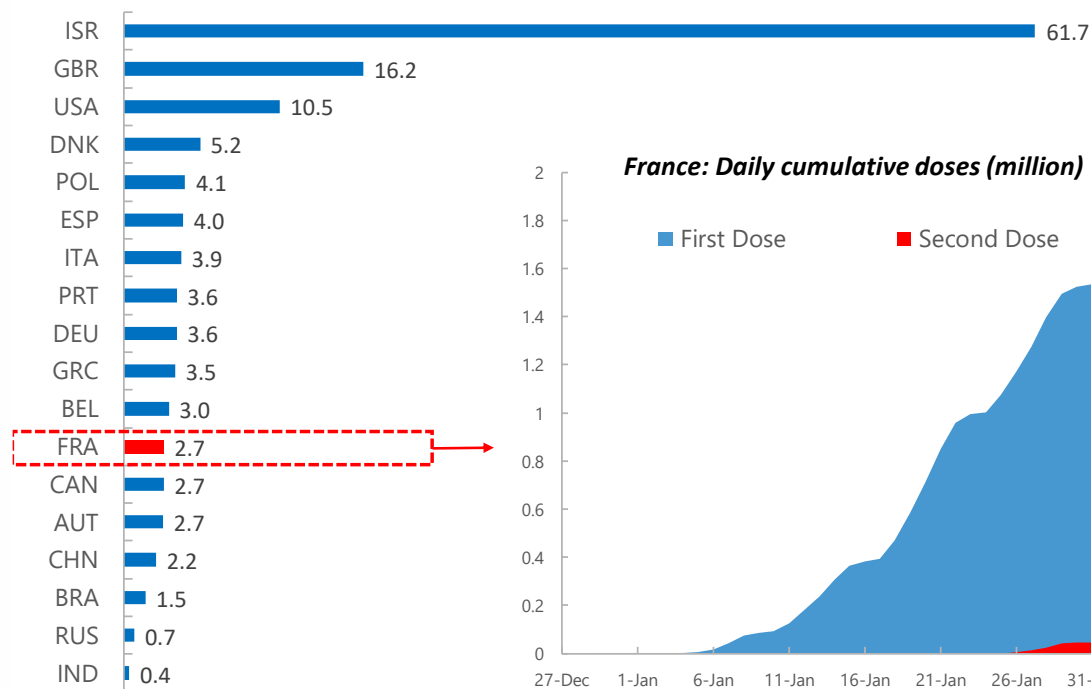
Sources: European Environment Agency; Eurostat; UNFCCC; and IMF staff

Path Ahead

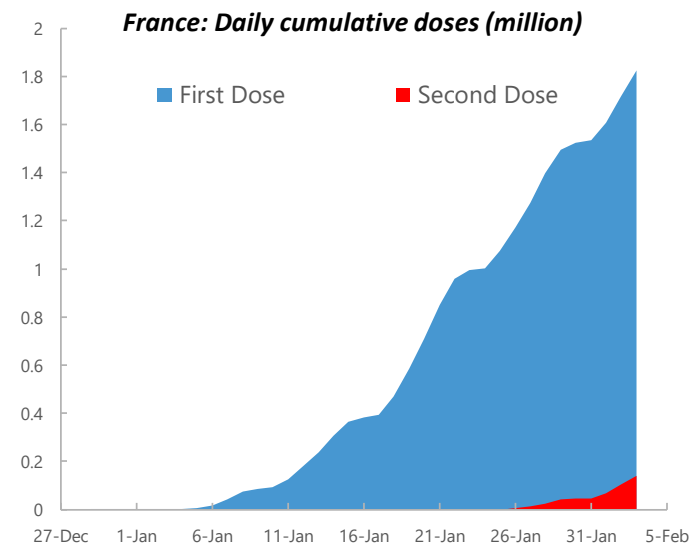
NAVIGATING HEADWINDS

- Economic outlook is highly uncertain, and risks are dominated by the virus dynamics.
 - Vaccinations tilt risk to the upside but supply bottlenecks dampen prospects.
- Continue strong policy support but reassess as needed. Once recovery gains traction:
 - Progressively target support for firms and jobs.
 - Plan for an expenditure-based consolidation now to contain high debt growth.
 - Reorient the French economy by addressing long-standing challenges, with green and job-rich policies.

Total Vaccinations Received (per 100 people)



Sources: Our World in Data



Merci!

Link to Report: IMF- France 2020 Article IV Consultation

Link to accompanying analysis: Selected Issues Papers