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France: soft crisis, hard recovery – eroding influence in Europe?

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France: soft crisis, hard recovery – eroding influence in Europe?

Abstract: The objective of this paper is to examine why the French economy, having done quite well during the period of global financial crisis, has been unable to head off to the path of sound economic growth again, while at the same time the German economy, by European standards, has been flourishing. Is it related to the specificities of French capitalism (centralisation, rigidities, delays in structural reforms, etc.) or some EU policies (pre-eminently the monetary one) are to blame? A thorough examination of this issue is of the utmost importance considering that a permanent shift in the balance of power between France and Germany might prove detrimental to the European integration process at large.
Keywords: France, Germany, economic performance, balance of power

Introduction

Having done quite well during the period of the global financial crisis, the French economy has been unable to regain a dynamic pace of growth, and France is increasingly lagging behind Germany. A thorough examination of this issue is of the utmost importance considering that a permanent shift in the balance of power between France and Germany might prove detrimental to the European integration process at large. To address this issue the paper debunks the common myth of the dirigiste French state interfering in domestic economy. We examine the evolution of the role of state and civil servants in a historical perspective, pointing out that the neoliberal agenda has not left French economic thought intact and current economic policy is not far from that of 'liberal' EU member states. We also point out that the common conservative cultural background of the French financial elite prevented them from engaging in riskier investments before 2008 and therefore the financial crisis took a milder toll on state coffers in France than elsewhere in the EU. The state's modest recapitalization efforts however led to further procrastination regarding deep structural reforms. The slow pace of these reforms are to blame for France lagging behind Germany in economic terms. European monetary policy is also responsible since the common currency boosts German export competitiveness and compels periphery countries (including France) to resort to inner devaluation. In the end, we shortly draw two possible scenarios in an effort to evaluate Macron's neoliberal reforms. The argument is structured as follows. First the evolution of the role of the state in French economic thought is examined. Against this backdrop the implications of the global financial crisis for the French economy and its resilience are discussed. Section three offers a thorough insight into the dynamics underlying the French economy capacity to catch up. Conclusions follow.

1. Evolution of the role of state in France

Like in any other country having a significant impact on world development, certain beliefs and prejudices are associated also with France regarding the special role of state. One such stereotype relates to excessive state intervention in domestic economy, suggesting that France "is a capitalistic country with a socialist outlook".[1] This means that although in everyday practice the French believe in market and economic fundamentals of capitalism, they do not necessarily trust the self-correcting capacity of the market and, therefore, consider it important that the state interferes in the economy. Like all stereotypes, this one is also based on a morsel of truth, and while it might have been true for centuries, it has fundamentally changed by now.

Regarding the historical evolution of the state's economic intervention, France was already quite centralized in the 15th century, and the centralization of resources was further intensified by the establishment of absolutism and Colbert's mercantilism. Ever since the nomination

1 S. Pendergast and T. Pendergast, *Worldmark Encyclopedia of National Economies Volume 4 – Europe*, Detroit: Gale Group/Thomson Learning, 2002, p. 144.

of Sully for finance minister (to Henry IV.), the incumbent government of France have nurtured close links with businesses, and this relationship has traditionally been marked by state interventionism.[2] Accordingly, and contrary to the general European (e.g. British or German) practice where the economic role of the state has changed based on political winds, a godfather-like 'big government' has become a permanent feature of French capitalism.[3]

The emergence and evolution of this tradition cannot, however, be understood as a simple linear development. Resource-centralization cannot be identified as an exclusive perversion of the French, or a process of common consent of the people of France. As an illustration, we can mention that indirect taxes on colonial goods (sugar, coffee, tobacco, calico) from the second half of the 17th century made these goods so difficult to obtain that the fast strengthening of black economy (in the form of tax evasion and smuggling) was an inevitable consequence. In an attempt to roll back the growing underground, the efficiency of the General Farm (*Ferme générale*), the then largest paramilitary force in Europe, was boosted by scaling it up to some twenty thousand guards and a brutal hardening of the penal code entered into force against smuggling, encompassing punishments out of proportion.[4] Widespread dissatisfaction about government policy trying to regulate the consumption of colonial goods – first, by introducing heavy taxes on them, then, when this led to large-scale smuggling, by punishing people cruelly – was one of the most important reasons for the outbreak of the French Revolution. In this respect, it is revealing that the revolution itself did not begin with the storming of the Bastille on 14 July 1789. Three days earlier, a mob of professional and part-time smugglers, tradesmen, craftsmen, workers, and unemployed attacked and sacked the circa 40 customs gates encircling Paris which had been set up in the 1780s to break down the illegal wine and tobacco trade.[5]

2 F. Chevallier, *Les entreprises publiques en France* [State owned enterprises in France], Paris : La documentation française, 1979, p. 16.

3 C. Meisel, 'The Role of State History on Current European Union Economic Policies', *Towson University Journal of International Affairs*, *Fall Issue*, vol. XLVII, no. 1, 2014, p. 81.

4 M. Kwass, 'Global Underground: Smuggling, Rebellion, and the Origins of the French Revolution', in: S. Desan, L. Hunt and W.M. Nelson (eds), *The French Revolution in Global Perspective*, Ithaca, NY and London: Cornell University Press, 2013, pp. 27-28.

5 Ibid.

In spite of their dissatisfaction with tax policy, French revolutionaries mostly blamed the aristocracy and the Catholic Church for the country's economic woes rather than the widely respected public servants. And here we come to the fundamental characteristics of French capitalism in terms of the state's economic involvement, which can be summed up in two points. The first one originates in the traditional respect for state officials: senior administrators of the so-called Grand Corps[6] hold their positions longer than ministers, thus ensuring a certain degree of continuity in economic policy. The second is a conviction of historical origin, linked to the Revolution: people have the right to happiness, liberty or fair (equal) treatment.[7]

If anything, this special French interpretation of public service explains why the belief in state intervention is still high. According to the French legal interpretation, public services should be governed by constitutional principles such as continuity (which means uninterrupted service, as there is a strategic social need to satisfy), equality (i.e. equal access to service which implies different tariffs for different social strata and geographical areas), and adaptability (ensuring services are constantly adapted to demand, both in quantity and quality).[8] In this concept, the ultimate goal of public service provision is to serve the broad public interest, including the facilitation of social and territorial cohesion.[9]

However, even the French were influenced by the neoliberal economic philosophy during these last more than three decades. As a result of successive privatization waves since the shift in economic policy in 1983, the weight of public ownership, constituting the main asset for state intervention, has decreased significantly (Figure 1).

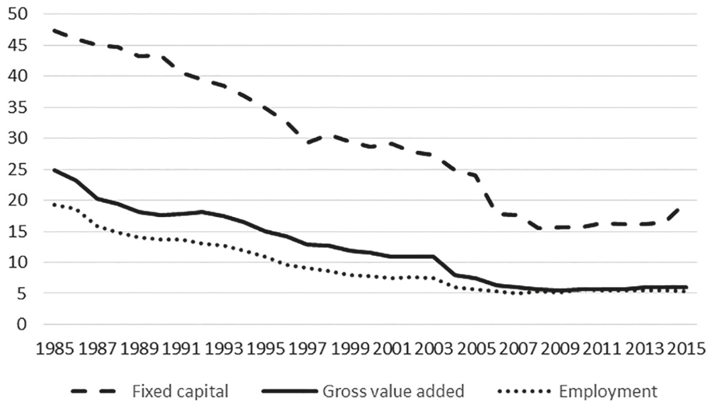
6 Powerful public bodies special to France, established by Colbert, and modernised under Napoléon I.

7 S.C. Kolm, 'History of public economics: The historical French school', *The European Journal of the History of Economic Thought*, vol. 17, no. 4, 2010, p. 690.

8 E. Brillet, 'Le service public "à la française": un mythe national au prisme de l'Europe' [Public service 'à la française': a national myth through European prism], *L'économie politique*, no. 4, 2004, p. 10.

9 P. Musso, 'La dérégulation des télécommunications ou « la finance high-tech »' [Deregulation in telecoms or high-tech finances], in: D. Benamrane, B. Jaffré, F-X Verschave (coord), *Télécommunications, entre bien public et marchandises* [Telecoms: public good or mechandise?], Paris : ECLM, vol. 148, 2005, p. 104.

Figure 1. Changing importance of the public sector in French economy (1985-2015), %

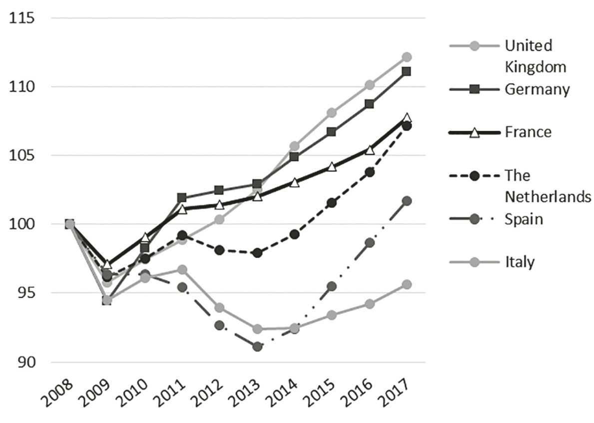


Source: INSEE, 'Entreprises publiques' [State owned enterprises], *Tableaux de l'économie française, Édition 2018*, https://www.insee.fr/fr/statistiques/3303570?sommaire=3353488 [2018-06-26].

2. The French economy and the crisis

The 2008 global financial crisis has led to a less pronounced growth slowdown in France than its most important European competitors. In 2009, real GDP fell by a mere 2.9 per cent, against 4.2 per cent in the United Kingdom, 5.5 in Italy, and 5.6 in Germany. Even the relatively smaller economies of Spain or the Netherlands experienced a more important decline (-3.6% for each) than France (Figure 2).

Figure 2. Cumulative GDP growth in the largest EU economies (2007 = 100)



Source: Eurostat, 'Real GDP growth rate – volume, Percentage change on previous year', http://ec.europa.eu/eurostat/tgm/table.do?tab=table&init=1&plugin=1&language=en&pcode=tec00115 [2018-06-27].

The relative resilience of the French economy was mainly due to the fact that the banking system – thanks to its regulatory and structural characteristics – was not exposed to extreme shocks from the international financial markets. Following the neo-liberal shift in 1983 and the subsequent waves of privatization, commercial banks were listed on the stock exchange, while financial institutions could turn their core business into a profitable direction and become universal banks. It is not the transformation itself that matters, but the way it was carried out. As a result of the privatization process, centred on a handful of national banks, a system of financial institutions and big corporations was created. These were interconnected in a complex though short-lived cross-shareholding network. What proved to be more permanent and therefore decisive was the fact that members of the boards of directors and supervisory boards of this system were senior officials with similar backgrounds (i.e. with similar career path), having completed their studies at the same French elite universities (HEC, ENA, Polytechnique) and gained professional experience in various positions of the same large bodies (e.g. ministry of finance or banking supervision) of the French administration.[10]

The common conservative educational/professional background prevented bank managers from venturing in overly risky transactions, or, more precisely, from extremely risky investments gaining too much importance in the activities of the organizations they managed. Unlike German and British banks, specializing mostly in investment banking and corporate lending, French banks used financial liberalization to broaden the scope of their activities towards the relatively less risky retail banking area, both at home and in Southern Europe, considered to be their second homeland.[11] Similar moderation could also be observed concerning derivatives, as French banks specialized in equity, interest and exchange rate derivatives, rather than riskier credit derivatives.[12]

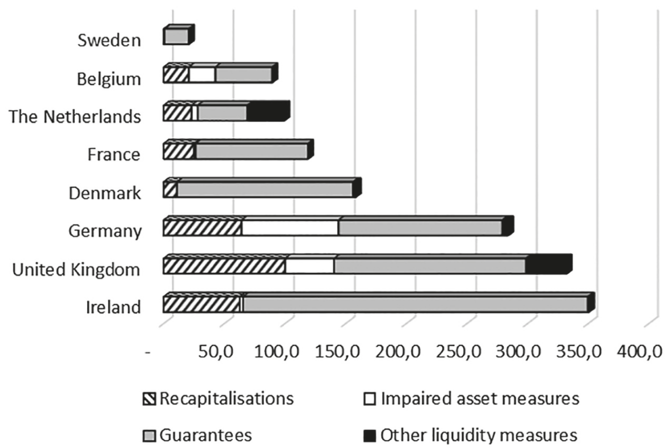
10 V. Schmidt, 'French capitalism transformed, yet still a third variety of capitalism', *Economy and Society*, vol. 32, no. 4, 2003, p. 542.

11 I. Hardie and D. Howarth, 'Die Krise but not La Crise? The financial crisis and the transformation of German and French banking systems', *Journal of Common Market Studies*, vol. 47, no. 5, 2009, p. 1020.

12 D. Howarth, 'The Legacy of State-led Finance in France and the Rise of Gallic Market-Based Banking', *Governance*, vol. 26, no. 3, 2013, p. 376.

Prudent banking management has paid off during the global financial crisis, given that the French had to spend relatively little money (and most of it in the early years of the crisis) on saving their banks. Figures 3, 4 and 5 show the absolute and relative magnitude of state aid granted to the financial sector over the 7-year period from 2008 to 2014[13]. We have tried to compare the allegedly 'dirigiste' France with those member states of the EU where liberal economic policy dominates. It is already apparent from Figure 3, showing absolute values, that France is outpaced by far smaller economies (Ireland, Denmark). Belgium or the Netherlands, countries with respectively less than a fifth or a third of the GDP of France, spent amounts almost as important as France to bail out their banks.

Figure 3. State aid effectively spent on rescuing banks from 2008 to 2014 (€ Bn)



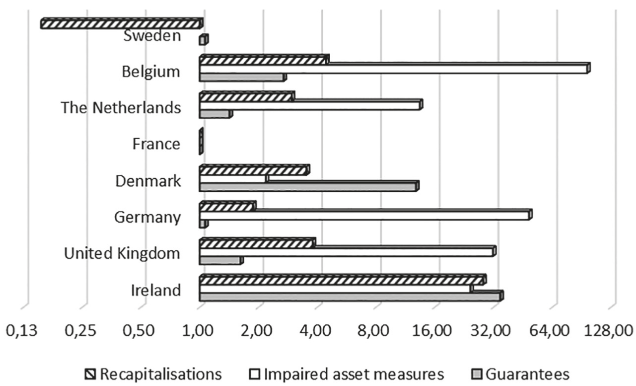
Source: Own calculation based on European Commission, DG Competition, 'Aid in the context of financial and economic crisis', *State Aid Scoreboard 2015*, http://ec.europa.eu/competition/state_aid/scoreboard/financial_economic_crisis_aid_en.html [2016-04-30].

For the sake of better comparison, Figure 4 shows how significant the amount of the various types of state aid (each country granted to its banks) is in comparison to French data, taking into account coun-

13 In this chapter, investigation covers the period for which data were available. In this paper, time series, in general, start from 2006, the year considered to be a turning point from which point onwards economic growth rate in Germany is noticeably higher than in France.

tries' economic performance (GDP). Now, it is definitely true that 'dirigiste' France, with the only exception of Sweden, spent much less on rescuing banks than the so-called liberal member states. Most 'liberal' countries spent about three to four times (even Germany spending almost twice) more on recapitalisations than France. The British spent more than 30 times, the Germans almost 50 times, the Belgians almost 100 times more than the French recapitalizing impaired assets . As for guarantees, the UK and the Netherlands spent one and a half time, Belgium two and a half times, Denmark 13 times, and Finland 35 times more than France.

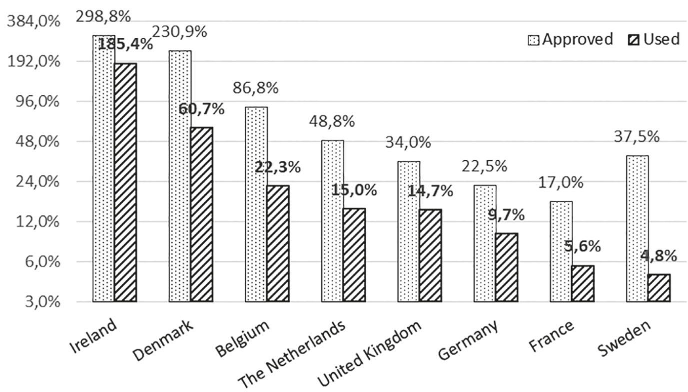
Figure 4. Relative size of state aid effectively spent on rescuing banks from 2008 to 2014 (the data for France compared to French GDP = 1)



Source: Own calculation based on European Commission, DG Competition, 'Aid in the context of financial and economic crisis', *State Aid Scoreboard 2015*, http://ec.europa.eu/competition/state_aid/scoreboard/financial_economic_crisis_aid_en.html [2016-04-30].
Example: UK's GDP is 1.06 times of that of France's, while it spent on recapitalisations of their banks four times more money than France did. So, it spent (4/1.06=) 3.78 times more, taking into account its economic size.

Finally, in Figure 5, we compared the approved and used state aids to GDP. The French spent € 119 billion or 5.6% of their GDP to bail out their banks, a rather low ratio compared to those of the 'liberal' countries. Effectively, only the Swedes spent less than the French. GDP-wise, the Germans spent more than 1.7 time, the British and Dutch more than 2.6 times, the Belgians four times, the Danish 11 times, and the Irish 33 times more than the French.

Figure 5. State aid effectively spent on rescuing banks from 2008 to 2014 (as a percentage of GDP)



Source: Own calculation based on European Commission, DG Competition, 'Aid in the context of financial and economic crisis', *State Aid Scoreboard 2015*, http://ec.europa.eu/competition/state_aid/scoreboard/financial_economic_crisis_aid_en.html [2016-04-30].

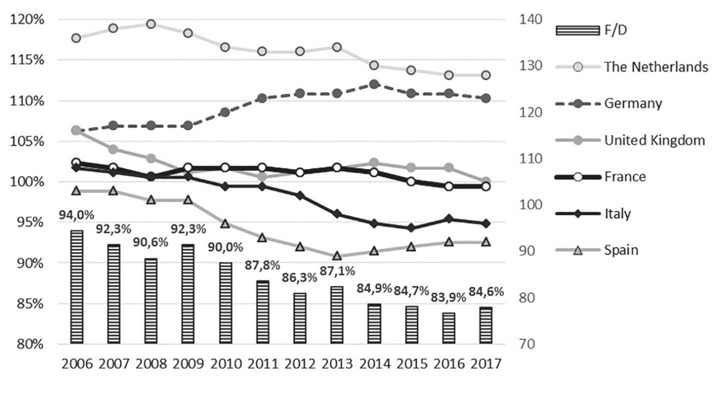
Eventually, the cost of state aid granted to the French financial sector in connection with the global financial crisis was kept at a relatively acceptable level, at least in international comparison or in taxpayers' eyes. On the other hand, because of the relatively small decline in growth, constraints on structural change in the economy were also weaker in France than in many competitors. This delay in structural reforms, in turn, most probably played a role in the fact that – after a relatively fast recovery from a modest recession in 2009 – the French economy has found itself on a slower growth trajectory than some of its main partners. Especially the diverging economic development trend of the two most important Eurozone members (i.e. Germany and France) could become cause for concern.

3. Doomed to lag behind Germany? – the French economy capacity to catch up

For many, the history of the European integration is the story of the ever-tightening Franco-German relationship. They tend to speak of a Paris-Berlin axis and consider the governments of these two countries as the engines of the EU: when their relationship is good and balanced, the integration process accelerates; when problems prevail, it slows down. One thing is for sure: without their consent, there can be no meaningful reform in Europe.

Based on the above, there is a general assumption arguing that these two countries can cooperate well when they are in the same 'weight group'. In GDP terms, they have never been in the same 'weight group' for the last 50 years. But while this postwar difference was 'balanced' partly by the division of the German nation, and the French military-political superiority (permanent membership in UN Security Council, possession of nuclear arsenal), the situation changed radically after the German reunification. Once the Cold War was over, the importance of France's military-political advantage has declined, while that of Germany's economic advantage – due to its higher population and twice export volume of France – has gained importance. Although from 1995 through 2005, France's economic growth rate exceeded that of Germany every single year, this trend has been totally reversed since.[14] In addition, due to differences in demographic tendencies, France lagging behind Germany is even more evident in terms of per capita output (Figure 6).

Figure 6. GDP per capita in PPS from 2006 to 2017 (EU28 = 100)



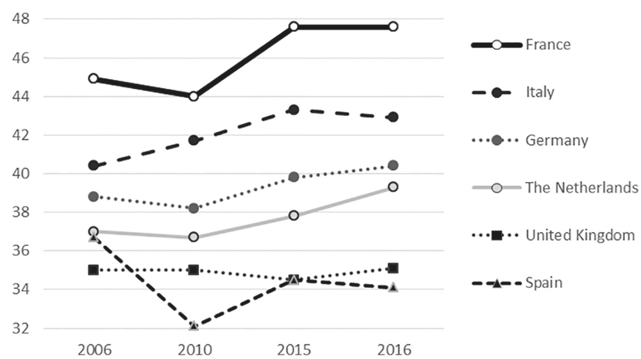
Source: Own calculation based on Eurostat, 'GDP per capita in PPS', *Index (EU28 = 100)*, http://ec.europa.eu/eurostat/tgm/table.do?tab=table&init=1&language=en&pcode=tec00114&plugin=1 [2018-07-01].

14 USDA ERS (United States Department of Agriculture – Economic Research Service), 'International Macroeconomic Data Set', *Real GDP (2010 dollar) Historical*, https://www.ers.usda.gov/data-products/international-macroeconomic-data-set/international-macroeconomic-data-set/#Historical%20Data%20Files [2018-07-01].

Many fear that this trend will be permanent and the shift in the balance of power between France and Germany will ultimately harm European integration.[15] Concerns are further enhanced by the fact that while Germany successfully implemented structural labour market (so-called Hartz) reforms in the early 2000s, in France such reforms have only recently (under Macron's presidency) been initiated, and with limited content.

The situation is further exacerbated – and the French government's room for maneuver is further narrowed – by the country's equilibrium problems. As a result of the global financial crisis, France was among the first, within the Eurozone, to undergo an excessive deficit procedure, and is among the last – to be precise, the last but one (before Spain) – whose procedure is now being closed.[16]

Figure 7. Total tax revenues from taxes and social contributions



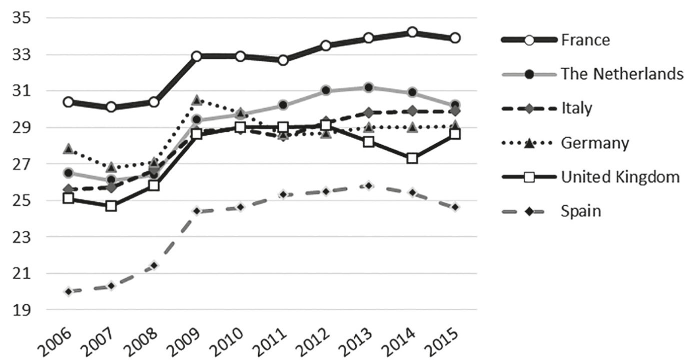
(as % of GDP)
Source: Own compilation based on Eurostat, 'The tax-to-GDP ratio slightly up in both the EU and the euro area', News-release, 187/2017, http://ec.europa.eu/eurostat/documents/2995521/8515992/2-07122017-BP-EN.pdf/0326ff22-080e-4542-863f-b2a3d736b6ab [2018-07-03].

15 This is even more so as, with Brexit looming, not only the EU's second largest economy but also a powerful counterweight to German influence is about to withdrawing from the integration and its decision-making system.

16 The Council set the 2012 deadline for bringing the general government deficit below 3 percent of GDP on 27 April, 2009. The deadline was later modified three consecutive times (2013, 2015, and 2017 mentioned as new deadlines), given the slow recovery of the French economy. Finally, French deficit dropped to 2.6 percent of GDP in 2017, and on 22 June, 2018 the Council closed the excessive deficit procedure against France. Source: European Commission, 'Excessive deficit procedures – overview', *Most recent decisions and updates*, https://ec.europa.eu/info/business-economy-euro/economic-and-fiscal-policy-coordination/eu-economic-governance-monitoring-prevention-correction/stability-and-growth-pact/corrective-arm-excessive-deficit-procedure/excessive-deficit-procedures-overview_en [2018-07-01].

French struggle with macroeconomic imbalances has its origins in the centralization of incomes and expenditure on social protection (Figure 7, 8). An economic research institute which is close to the employer's side (with a board of directors coming from large banks, MEDEF, and large corporations) found that the comparatively high tax-to-GDP ratio (i.e. sum of taxes and net social contributions as a percentage of GDP) played an important role in France's diminishing share of Eurozone exports (dropping from 17 to 13.4 percent between 2000 and 2015).[17]

Figure 8. Expenditure on social protection (as % of GDP)



Eurostat, 'Expenditure on social protection – % of GDP', *Social protection*, http://ec.europa.eu/eurostat/tgm/table.do?tab=table&init=1&language=en&pcode=tps00098&plugin=1 [2018-07-03].

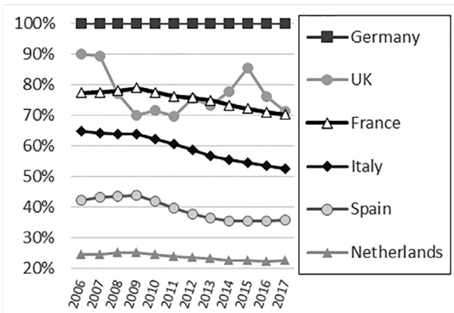
To 'defend' the French, two remarks should be made. First, although a lot of assets are centralized, a significant part of those are spent on human capital. In this way, while wages paid to full-time employees in industry, construction and market services are higher in Germany, when it comes to disposable income of households per capita in PPS (i.e. money available for spending and saving, a better proxy for standard of living than earnings), France ranks third in Europe, slightly

17 Coe-Rexecode, 'Perspectives 2017 et analyse des freins qui brident le redémarrage de l'économie française' [Outlook 2017 and analysis of the brakes that are holding back the recovery of the French economy], *Document de travail*, no. 60, September 2016, pp. 3-5.

ahead of Germany, and preceded only by Luxemburg and Austria.[18] Moreover, in the mid-2010s, the proportion of people living at risk of poverty (i.e. below 60 percent of median income after social transfers) was by several percentage points lower in France (13.6%), than in Germany (16.7%).[19]

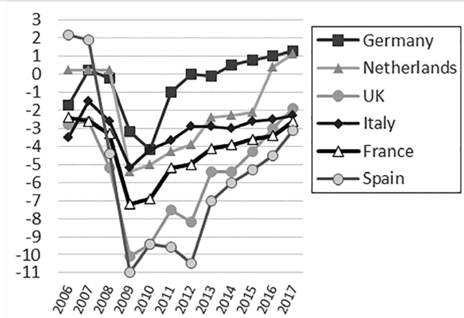
Figures 9-12

GDP at market prices (Germany = 100)



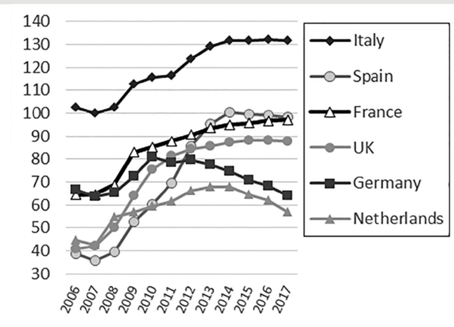
Source: Own compilation based on Eurostat, 'GDP and main components (output, expenditure and income)' http://appsso.eurostat.ec.europa.eu/nui/show.do?dataset=nama_10_gdp&lang=en [2018-07-04].

General gov. deficit/surplus (% of GDP)



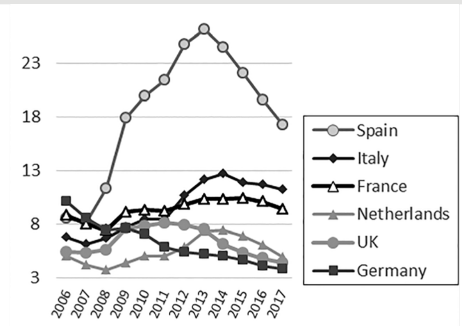
Source: Own compilation based on Eurostat, 'General government deficit/surplus', *Percentage of GDP*, http://ec.europa.eu/eurostat/tgm/table.do?tab=table&init=1&language=en&pcode=tec00127&plugin=1 [2018-07-04].

General gov. gross debt (% of GDP)



Source: Own compilation based on Eurostat, 'General government gross debt', *Percentage of GDP*, http://ec.europa.eu/eurostat/tgm/table.do?tab=table&init=1&language=en&pcode=sdg_17_40&plugin=1 [2018-07-04].

Unemployment rate (% of labour force)



Source: Own compilation based on Eurostat, 'Unemployment by sex', *Percentage of the labour force*, http://ec.europa.eu/eurostat/tgm/table.do?tab=table&init=1&language=en&pcode=tesem120&plugin=1 [2018-07-04].

18 INSEE, 'France, portrait social – Édition 2017' [France, social portrait – 2017 edition], https://www.insee.fr/fr/information/3280892 [2018-07-03], p. 226.

19 M. Dancer, 'L'Allemagne, un modèle économique inimitable pour la France' [Germany – an economic model France cannot copy], *La Croix*, 2 October 2017, https://www.la-croix.com/Economie/Economie-et-entreprises/LAllemagne-modele-economique-inimitable-France-2017-10-02-1200881273 [2017-12-03].

It is also to be noted that France's situation is not at all unique within the European Union. From figures 9 to 12 it is clear that not only France but – apart from the Netherlands – practically all the major economies of Europe are lagging behind Germany. Moreover, France is not in the worst position: Italy and Spain are further down the list.

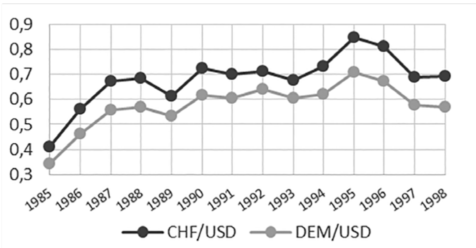
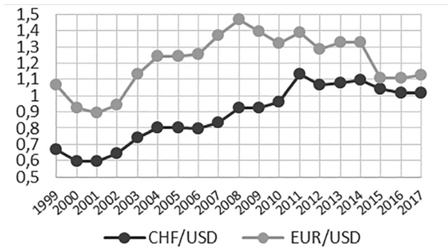
If, within an integration, development and healthy economic indicators are concentrated on just a few countries, while the majority of members is constantly underperforming (even their own earlier achievements), it is possible that the blame is not to be put solely on those lagging behind. 2016 regional unemployment statistics give us food for thought: except for Germany and countries/regions closely linked to the German economy (e.g. Austria, the Benelux, or Bratislava Region) unemployment is below 6.5 percent almost exclusively in the regions of those countries (e.g. Scandinavia, the British Isles, Switzerland and Central and East European countries) where the euro has not yet been introduced. Of course, the two groups of countries (those with German orientation and those being outside the Eurozone) may overlap (e.g. see the case of Switzerland or Czechia).[20] Apparently, the common currency is too strong for the peripheral economies (France included), and too weak for Germany and its affiliated economies. If there is any doubt about the truth of this statement, we can consider the following.

Figures 13, 14, and 15 suggest that, in the period of 1985-1998, the German mark and the Swiss franc tended to move parallel to each other against the US dollar. There was, however, no parallelism in the move of the exchange rate of the Swiss franc and the euro against the dollar from 1999 to 2017. In the latter period, the franc tended to become stronger, while the euro, following a temporary strengthening, ended up at its starting point. Assuming the euro and the Eurozone had not been created, and the German mark and the Swiss franc would have moved parallel against the dollar in 1999-2017 (like they did in 1985-

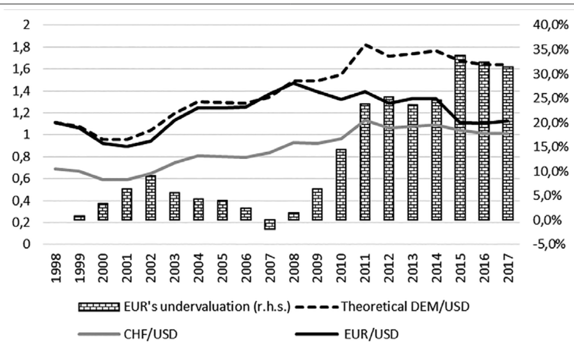
20 Another characteristic feature is that, while, in 2016, 7 of the 10 regions with the lowest unemployment rates in Europe (9 in the 15-24 age group) were located in Germany, one could only find Spanish, Greek, French and (in the 15-24 age group also) Italian regions among the top 10 with the highest rates. Source: Eurostat, 'Unemployment in the EU regions in 2016', *Newsrelease*, 72/2017, pp. 1-2, http://ec.europa.eu/eurostat/documents/2995521/8008016/1-27042017-AP-EN.pdf [2017-12-03].

1998), the German national currency would be 30 percent stronger than actually is. This would obviously have a negative impact on German exports' competitiveness.[21]

Figures 13-15.

Evolution of the exchange rate of the Swiss franc and the German mark against the US dollar	**Evolution of the exchange rate of the Swiss franc and the euro against the US dollar**
	

Demonstration of the evolution of the exchange rate of a theoretical German mark against the US dollar, and the undervaluation of the euro versus this theoretical German mark.



Source: Own compilation based on FXTOP, 'Historical exchange rates from 1953 with graph and charts', http://fxtop.com/en/historical-exchange-rates.php [2017-11-26].

Of course, we do not pretend that countries of the EU periphery (including France) should not introduce economic policy reforms to improve public spending or make the labour market more flexible.

21 It is no wonder that for the 3-year backward moving average of the current account balance (as per cent of GDP) – one of the headline indicators covering the most relevant areas of the so-called EU macroeconomic imbalance procedure scoreboard (for which there is an asymmetry in thresholds: -4%/+6%, which favours Germany) the latter has, since 2012, been unable to comply with EU rules. What's more, the indicator is trending upward (!): 6.2% in 2012; 6.6% in 2013; 7.1% in 2014; 7.7% in 2015; 8.3% in 2016; and 8.5% in 2017. Source: Eurostat, 'Current account balance – 3 year average', *Percentage of GDP*, http://ec.europa.eu/eurostat/tgm/table.do?tab=table&init=1&plugin=0&language=en&pcode=tipsbp10&tableSelection=1 [2018-07-05].

It should, however, be noted, that the German economy, which was already quite competitive in itself, has been given further impetus by the undervalued single currency, which in turn has unequivocally deteriorated the standard of living of the people of these countries. Unable to devalue their currencies, the latter were hence compelled to resort to internal depreciation (i.e. to reduce wages and profits) in order to regain competitiveness on world markets. In view of the above, reforms should not be limited to the periphery, but should also be extended to the core states of the euro area.

It has become fashionable to compare German and French economies and jump to the conclusion that Paris should learn lessons from Berlin. But differences in economic and social structure, as well as in geography and history do significantly limit the potential for copying. Due to differences in traditions between the federalist Germany and the highly centralized France, while the culture of mutual trust and compromise between social partners can be traced back to the board of directors of businesses in the former, the culture of confrontation prevails in the latter.[22] It is also unlikely that the French would be able, at least in the near future, to establish their own *Mittelstand*, this fabric of family-owned small and medium-sized businesses of Germany, which could, by expanding its suppliers' contacts, take advantage of the proximity of cost-effective Central European sites.[23]

It should be emphasized, however, that France has its own assets – geographic and demographic situation, high-quality education and training, stable banking system, relatively homogenous society[24] – which can be exploited to accelerate growth and close the gap with Germany. Circumstances having allowed the German economy to reach today's high level of competitiveness, may also change which

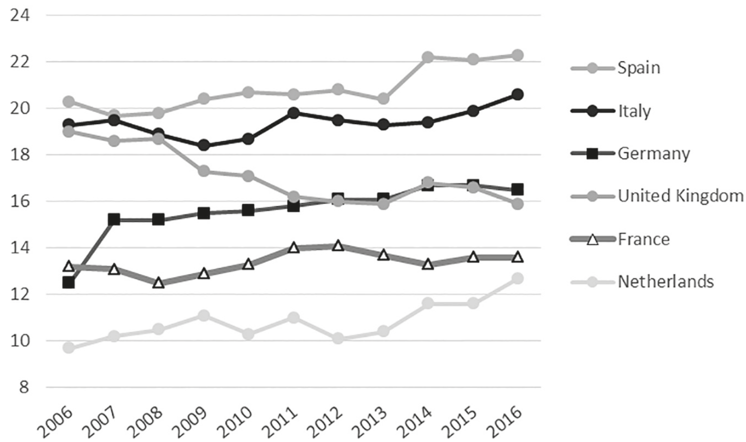
22 This attitude is far from being peculiar to workers' organisations. The overall thrust of Macron's labour reforms, often passed through decrees to avoid the parliamentary route, is to facilitate layoffs and decentralise collective bargaining. These changes will inevitably weaken workers' rights and protection, but, if the goal had really been to copy Germany, they could have been coupled with the introduction of a German-type model for workers' participation in management and supervision of the companies they work for (*Mitbestimmung*).

23 Dancer, op. cit.

24 Homogeneous in the sense of income distribution – at least compared with the USA, Britain or even Germany (T. Piketty, *Capital in the 21st Century*, Cambridge, Mass. and London, England 2014, The Belknap Press of Harvard University Press, online database, Tables 8.1; 8.2; 9.1; 9.2 and 9.4).

could lead to tensions with its partners already in the medium term (e.g. in the field of international finances) or the formation of bottlenecks (e.g. in infrastructures), the removal/elimination of which would inevitably result in a (probably temporary) reduction of Germany's competitive advantage.

Figure 16. At risk poverty rate (cut-off point: 60 % of equalised median income after social transfers)



Eurostat, 'At-risk-of-poverty rate by poverty threshold, age and sex', *EU-SILC survey*, http://appsso.eurostat.ec.europa.eu/nui/submitViewTableAction.do [2018-07-07].

As far as the German economy is concerned, the phenomenal increase of international competitiveness has a price: domestic poverty (the ratio of losers of the system) is growing (Figure 16), and so is anti-German sentiment, spreading in some EU member states. Both processes could be slowed down or even reversed if Germany was willing to change its economic policy trajectory.

As far as the French economy is concerned, the relatively moderate reforms – which were launched during the previous presidential term, fully implemented since 2017, and aimed at reducing employers' social security contributions (for their low and medium wage employees) – have not yet or only to a very limited extent led to the creation of the half a million jobs, promised in return for the cost reduction in the so-called Responsibility and Solidarity Pact.[25] Although hundreds of thousands of new jobs have been created in the private sector since the Pact was announced, most of them offer only temporary, often fixed-term contracts, the most common form being the very short-term (less than one month) contract. This is because French companies, rather than reducing their producer prices (to increase their price competitiveness) which would probably have increased the number of real, lasting jobs – do use the government's 'gift' to restore gross margin (profitability). From the employers' point of view, the emphasis is naturally on investing to increase non-price competitiveness.[26]

The new president has now launched a drive to speed up reforms – not just for the labour market but also social security and education – which he, in the absence of sufficient public support, is trying to achieve by circumventing the parliament via presidential decrees. Among the reforms one of the most important happens to be the reduction of taxation on capital and wealth, in the hope of giving an impetus to job creation and domestic investment. However, since the entry into force of the Maastricht Treaty "all restrictions on capital movements and payments across borders" was removed (and prohibited),[27] there is no guarantee, therefore, that savings in capital income will necessarily be invested in France.

In any case, the implementation of an overtly neoliberal policy agenda poses serious risks, regardless of whether it is successful or not. If it is successful – i.e. the majority of society accepts it and adapts to the new situation – more and more people may find themselves in worsening working conditions, poverty may further increase and the French can say farewell to the relatively homogeneous income distribution within their society. If it is not successful – because most people reject the reforms – it may enhance political radicalization and extremism in France.

25 French government, 'Responsibility and solidarity pact for employment and purchasing power', *Service d'information du gouvernement*, https://www.gouvernement.fr/sites/default/files/locale/piece-jointe/2014/09/frenchresponsabilitypact-en.pdf [2018-07-07].

26 Coe-Rexecode, op. cit., p. 4.

27 European Commission, 'Capital movements', *Overview*, https://ec.europa.eu/info/business-economy-euro/banking-and-finance/financial-markets/capital-movements_en [2018-07-08].

Conclusions

Contrary to the old stereotype whereby France's competitiveness gap with Germany stems from too much centralisation, i.e. the excessive and damaging interference of the state in economy, today's French model of capitalism does not fundamentally differ from that of other developed countries of Europe. This does not mean that there are no special features of the French system. Some of them, like the common educational background of the managerial elite or the strict financial supervision, may also have beneficially contributed to the country's relatively minor downturn in the global financial crisis.

France's economic performance however has for the last 10-12 years increasingly been lagging behind that of Germany. Although the responsibility for this lies mainly with France's internal economic policy deficiencies (e.g. the eternal procrastination of deep structural reforms), some blame can also be attributed to the Eurozone monetary policy which exacerbates France's competitive disadvantage versus Germany. In case Macron's overtly neoliberal reforms did not work out – i.e. pulling France closer to Germany in economic policy sense – and Brexit happened to be too hard in the end, then the balance of power within the European Union, especially between France and Germany, would inevitably undergo fundamental change and harm the integration itself.

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