Flash Economics

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How can the French social protection system be rebalanced?

Social security (essentially health insurance) is expected to have a deficit of almost €25 billion in 2025; pension schemes are likely to have a deficit of €7 billion in 2025, rising to €15 billion in 2035 and €30 billion in 2045.

How can the social security accounts be rebalanced? There are six possibilities:

- Increasing the employment rate;
- Increase taxation on labour;
- Increase taxation on capital;
- Broaden the social protection funding base;
- Stimulate growth;
- Reduce the generosity of social protection.

The most effective approach would be to act on the macroeconomic side: increase the employment rate and stimulate growth. But this requires reforming the education system, extending the retirement age, and investing more in digital technology and research.

If the macroeconomic situation cannot be improved, we will have to rely on tax increases, on broadening the tax base that finances social protection and inevitably on a reduction in its generosity.

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Growing social protection deficits in France

A growing deficit in France's social protection systems is to be expected, due to:

- The fall in the number of pension scheme contributors relative to the number of pensioners (Table 1);

Table 1: Ratio between the number of contributors and the number of pensioners

Year	Ratio
1975	3.14
2004	2.02
2022	1.77
2050	1.50
2075	1.25

Sources: INSEE, COR

- The ageing of the population, since healthcare expenditure increases with age (Table 2).

Table 2: France: Health expenditure by age group (in euros per year)

Age group	Expenditure in euros
0-1	2135
2-16	870
17-59	1802
60-74	4195
75-79	6448
over 80	8355

Source: Sécurité sociale

Thus, it is not surprising that the social security system is forecast to have a deficit of €25 billion in 2025, and that pension schemes will go from a deficit of €7 billion in 2025 to a deficit of €30 billion in 2045.

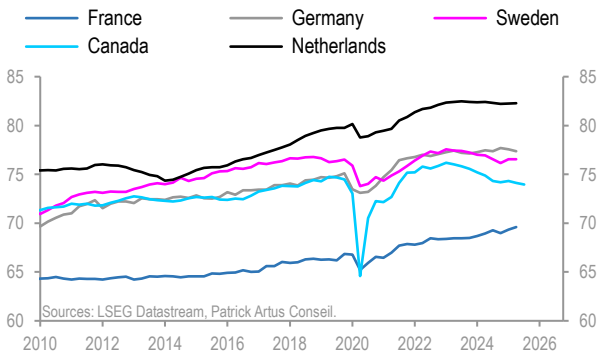
We wonder which avenues can then be pursued to bring France's social security accounts back into balance.

Six possible ways of rebalancing the social security accounts

1. Increase the employment rate

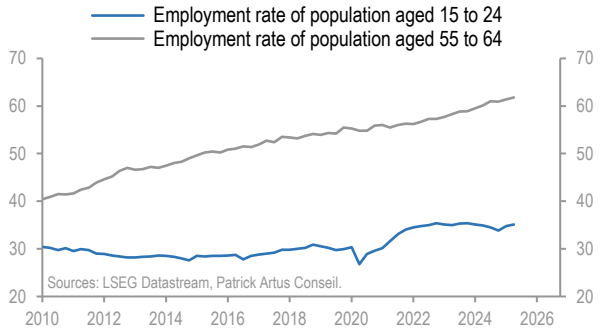
The employment rate in France is low compared with Germany, Northern European countries and Canada... (Chart 1).

Chart 1
Employment rate of population aged 15 to 64 (as %)



This is due to the low employment rate for young people and the low employment rate for the over-55s (Chart 2).

Chart 2
France: Employment rate of population aged 15 to 24 and of population aged 55 to 64 (as %)



One can see that we cannot increase the overall employment rate in France without:

- **Improving the quality of the education system** (**Table 3**);

Table 3: Results of OECD PISA surveys (overall score, by decreasing score in the 2022 survey)

Country	2022
Japan	533
Canada	506
Finland	495
Denmark	491
Germany	482
Netherlands	480
France	478

Source: OECD

- **Continuing to raise the retirement age**.

2. Increase taxation of labour

This involves **increasing employers' or employees' social security contributions**.

The problem is that **the tax wedge**, i.e. the gap between the cost of labour for the employer and the salary net of all taxes and charges received by the employee, **is already very large in France** (**Charts 3a/b**).

Chart 3A
Average tax wedge(as % of labour costs)

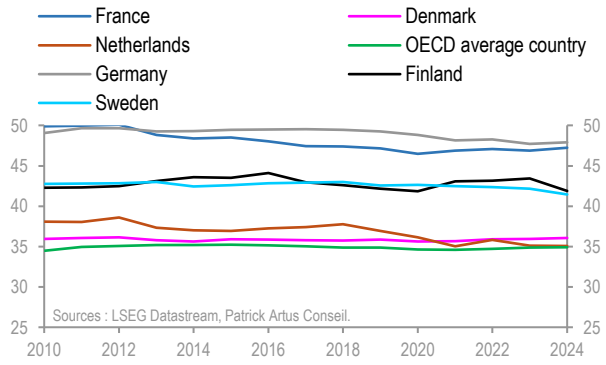
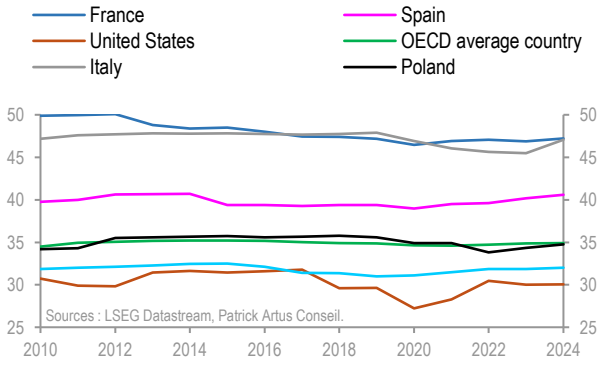


Chart 3B
Average tax wedge(as % of labour costs)



Increasing taxation on labour would lead either to a loss of competitiveness for companies or to a further reduction in take-home pay.

3. Increase taxation of capital income

Capital income is taxed at 30% in France, while the marginal tax rate on other income is as high as 49% for high earners. Increasing the 'Prélèvement forfaitaire unique' by one point would bring in around €200 and €600 million for the government, according to estimates, but the 30% rate is already higher than the average in other European countries.

4. Broaden the tax base used to finance social protection

The aim here is to move **from financing social protection through social security contributions paid by employees to financing it through a tax on all income** (including capital income).

This could involve a switch to VAT-based financing (which would include imports in the tax base for financing social protection) or CSG-based financing.

5. Stimulate growth

If France's growth were higher (it has averaged 1% a year since 2010, with 0.8% expected in 2025), **it would obviously be easier to finance social protection spending**.

The weak growth is due to **the decline in labour productivity** (**Chart 4**) and demographic ageing, **with the working-age population falling from 2023 onwards** (**Chart 5**).

Chart 4
France: Productivity per head (2010.Q1 = 100)

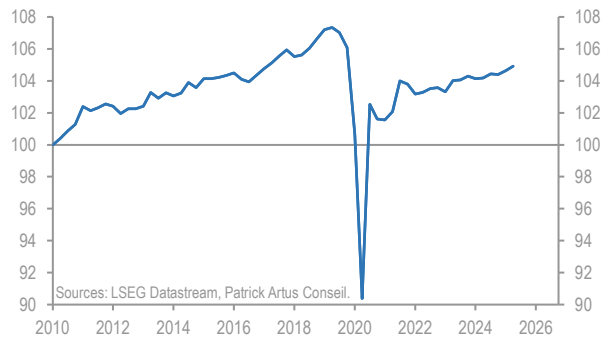


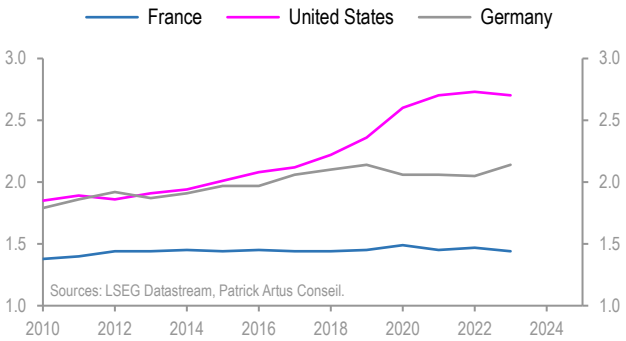
Chart 5
France: population aged 15 to 64 (annual growth rate, in %)



In reality, **France's growth only comes from an increase in the employment rate** (see Chart 1 above), and can therefore only persist in the long term if the education system is reformed and the retirement age continues to be pushed back. We know that the weakness of labour productivity is due to structural rather than cyclical factors:

- The low level of R&D spending by French companies (**Chart 6**) ;

Chart 6
Corporate R&D spending (as % of nominal GDP)



- Weak investment in new technologies (Charts 7/8).

Chart 7
Investment in information and communication technologies (in value terms, as % of nominal GDP)

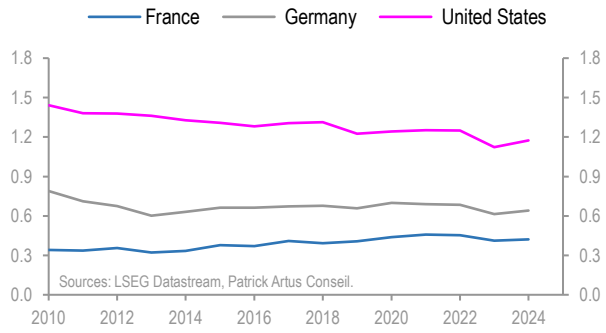
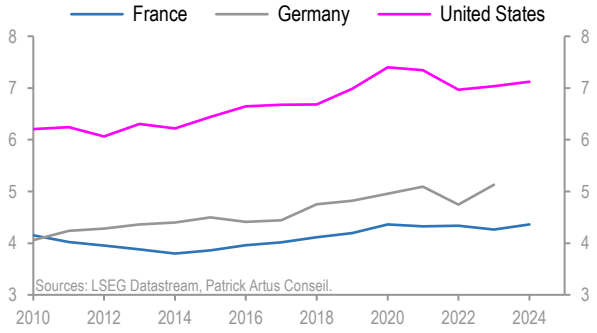


Chart 8
Gross value added of the ICT sector (as % of nominal GDP)



It would of course be desirable to correct these various weaknesses, but they have persisted for many years.

6. Reducing the generosity of social protection

If the approaches outlined above are not enough to balance the social protection accounts, **then the generosity of social protection will have to be reduced,** for example by:

- An increase in the deductible (currently 50 euros per year) on healthcare expenditure;
- Long-term under-indexation of pensions in line with prices.

Summary: how can France's social security accounts be balanced?

If nothing is done, demographic ageing will massively unbalance France's social protection accounts.

The most effective way would be to act on the macro-economy: increase the employment rate, stimulate growth. But that requires reforming the education system, extending the retirement age, and investing in digital technology and research.

If the macroeconomic situation cannot be improved, we will have to rely on tax increases, on broadening the tax base that finances social protection and inevitably on a reduction in its generosity.

Polls show that the vast majority of French people are opposed to raising the retirement age, indexing pensions to prices, making savings on healthcare costs, and raising household taxes. If we follow them, the only solution left would be to increase taxation on high incomes and wealth, which is not enough to balance the accounts of social protection.

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