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FM PARIS 131405Z SEPT 84

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TELEGRAM NUMBER 1042 OF 13 SEPTEMBER

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## FRANCE: DRAFT 1985 CENTRAL GOVERNMENT BUDGET

1. THE BUDGET PURPORTS TO REDEEM MITTERRAND'S PLEDGE OF A REDUCTION IN TAXES AND SOCIAL SECURITY CONTRIBUTIONS EQUIVALENT TO 1 PERCENT OF GDP AND IS PRESENTED AS A TURNING-POINT IN FRENCH FISCAL HISTORY. IT GIVES SUBSTANCE TO THE CENTRIST IMAGE OF THE FABIUS GOVERNMENT. PERSONAL AND CORPORATE TAXATION IS LOWERED AND SOME INDIRECT REVENUES ARE RAISED. THE STATE IS TO EXERCISE RESTRAINT ON ITS OWN HOUSE-KEEPING EXPENDITURE. IN TERMS OF INFLATION/DEFLATION THE BUDGET APPEARS TO BE BROADLY NEUTRAL. IT CONTAINS NO MAJOR REFORMS. THE RECEPTION ACCORDED IT BY THE PRESS (SEE MY SECOND IFT) HAS MAINLY RANGED FROM SCEPTICAL TO SCATHING.

## DETAIL

2. PUBLIC INTEREST HAS CENTERED ON THE INSTRUCTION GIVEN BY MITTERRAND THAT TAX AND SOCIAL SECURITY CONTRIBUTIONS SHOULD BE REDUCED BY AN AMOUNT EQUIVALENT TO 1 PERCENT OF GDP, LOWERING THEM FROM 44.7 PERCENT OF GDP IN 1984 TO 43.7 PERCENT IN 1985. BEREGOVY CLAIMS THAT THE BUDGET WILL ACHIEVE THIS, AND THE CLAIM APPEARS TO BE BROADLY JUSTIFIED. INCREASES IN SOME INDIRECT AND PARAFISCAL TAXES (ESPECIALLY ON PETROL) AMOUNTING TO 0.6 PERCENT OF GDP WILL ONLY PARTLY OFFSET REDUCTIONS IN OTHER TAXES AMOUNTING TO 1.6 PERCENT OF GDP. BEREGOVY ALSO CLAIMS THAT THE BUDGET DEFICIT WILL NOT EXCEED 3 PERCENT OF GDP, BUT THIS IS UNCONVINCING. ON AN UNCHANGED ACCOUNTING BASIS THE CEILING WILL BE EXCEEDED NEXT YEAR, AS THIS YEAR AND LAST.

3. THE CHIEF REDUCTIONS IN TAXATION ARE:

- A) 5 PERCENT REDUCTION IN INCOME TAX: F 10 BILLION,
- B) A REDUCTION IN THE BUSINESS TAX: F 10 BILLION, AND
- C) THE SUPPRESSION OF THE 1 PERCENT SOCIAL SECURITY LEVY ON TAXABLE INCOME: F 10 BILLION.

4. FOR THE FIRST TIME SINCE THE SOCIALISTS CAME TO POWER, STATE EXPENDITURE IS BUDGETED TO GROW MORE SLOWLY THAN GDP: 6 PERCENT NOMINAL GROWTH IN EXPENDITURE AGAINST A 7.5 PERCENT INCREASE IN NOMINAL GDP. THE TIGHTEST CONSTRAINT HAS BEEN IMPOSED ON GENERAL OPERATING EXPENDITURE WHICH WILL GROW BY 4.4 PERCENT IN NOMINAL TERMS TO ALLOW CAPITAL EXPENDITURE TO INCREASE BY 6.5 PERCENT. THE GOVERNMENT'S WAGE BILL IS BUDGETED TO RISE IN LINE WITH FORECAST INFLATION BUT THE NUMBER OF STATE EMPLOYEES IS TO BE REDUCED, EXCEPT IN EDUCATION (PARTICULARLY TECHNICAL EDUCATION) WHERE EMPLOYMENT WILL RISE. THIS IS IN LINE WITH THE GOVERNMENT'S EMPHASIS ON TRAINING AND MAY DO SOMETHING TO CONSILATE THOSE TEACHERS WHO WERE DISAPPOINTED AT THE GOVERNMENT'S RETREAT ON THE INDEPENDENT SCHOOLS ISSUE. SUBSIDIES TO PUBLIC SECTOR SERVICES, MANY OF WHICH STILL HAVE SUBSTANTIAL DEFICITS, WILL INCREASE BY ONLY 3 PERCENT IN NOMINAL TERMS.

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5. THE GOVERNMENT HAS BEEN WIDELY ACCUSED OF TAKING AWAY IN PUBLIC SECTOR TARIFF INCREASES AND PARAFISCAL TAXES WHAT IT IS CONCEDED IN REDUCTIONS IN DIRECT TAXES. WHILE THE REDUCTION IN FISCAL PRESSURE LOOKS GENUINE (PARA 3 ABOVE), THE BUDGET SHOWS THAT THE CHARGE HAS SOME FOUNDATION: FOR EXAMPLE TELEPHONE CHARGES HAVE BEEN INCREASED ON AVERAGE BY 25 PERCENT IN THE PAST 12 MONTHS.

6. PRESENTING THE BUDGET TO THE PRESS, BEREGOVY DESCRIBED IT AS NEITHER INFLATIONARY NOR DEFLATIONARY. HE REAFFIRMED HIS COMMITMENT TO ECONOMIC GROWTH BUT INSISTED IT MUST BE SOUNDLY BASED.

7. THE BUDGET IS BASED ON A FORECAST THAT INFLATION WILL FALL TO 4.5 PERCENT BY THE END OF 1985, BUT AS IN PREVIOUS YEARS THIS IS NOT SO MUCH A FORECAST AS A TARGET DESIGNED TO INFLUENCE WAGE AND PRICE FORMATION. THE FORECAST OF 2 PERCENT GROWTH IN THE ECONOMY NEXT YEAR DEPENDS HEAVILY ON A CONTINUING INCREASE IN WORLD TRADE.

8. A TABLE SHOWING THE MAIN ECONOMIC ASSUMPTIONS FOR THE BUDGET IS IN MY FIRST IFT, AND PRESS REACTION IN MY SECOND IFT.

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