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FM PARIS

TO PRIORITY F C O

TELNO 023

OF 161731Z SEPTEMBER 86

INFO ROUTINE UKREP BRUSSELS, BONN, ROME, UKDEL IMF/IBRD WASHINGTON

INFO ROUTINE HM TREASURY, BANK OF ENGLAND

INFO SAVING ATHENS, BRUSSELS, COPENHAGEN, DUBLIN, LISBON

INFO SAVING LUXEMBOURG, MADRID, THE HAGUE

FRAME ECONOMIC

FRANCE: DRAFT 1987 CENTRAL GOVERNMENT BUDGET  
SUMMARY

1. FOR THE FIRST TIME IN NEARLY 20 YEARS GOVERNMENT SPENDING (INCLUDING INTEREST PAYMENTS) WILL DECREASE IN REAL TERMS. THE LARGEST REDUCTION IS IN STATE AIDS TO INDUSTRY. DEFENCE EXPENDITURE IS INCREASED. AS A PERCENTAGE OF GDP, TAXES AND SOCIAL SECURITY CONTRIBUTIONS (BUDGETTED SEPARATELY) REMAIN CONSTANT, BUT THE LOAD HAS BEEN REDISTRIBUTED, TO THE BENEFIT OF THOSE AT THE TOP AND BOTTOM OF THE INCOME TAX NET. THE DETAILED CHANGES EXPRESS THE GOVERNMENT'S POLITICAL PHILOSOPHY, BUT EXCEPT FOR PRIVATISATION RECEIPTS THE MAIN EFFECT OF THIS BUDGET FOLLOWS TRENDS SET BY THE PREVIOUS GOVERNMENT LAST YEAR.

DETAIL

2. THE DRAFT CENTRAL GOVERNMENTAL BUDGET FOR 1987 WAS APPROVED BY THE GOVERNMENT AND PUBLISHED ON 15 SEPTEMBER (FULL DOCUMENTATION BY BAG TO MATHEWS, EF2 DIVISION, HM TREASURY) IT IS SHAPED BY THE SAME PRUDENT MIXTURE OF CONTINUITY AND CHANGE THAT HAVE MARKED THIS GOVERNMENT'S ECONOMIC POLICY IN ITS FIRST SIX MONTHS IN OFFICE.

3. COMPARISON WITH BEREGOVY'S LAST BUDGET SHOWS A LARGE DEGREE OF CONTINUITY IN THE GOALS PURSUED. THE EFFORT TO REIN IN PUBLIC EXPENDITURE HAS BEEN CARRIED FORWARD, AIDED BY THE FALL IN OIL PRICE AND INTEREST RATES, TO THE POINT WHERE EXPENDITURE WILL DECREASE EVEN WHEN THE INTEREST PAYMENTS ARE INCLUDED (WHICH WAS NOT SO IN THE 1986 BUDGET). THE MAIN SAVINGS WILL COME FROM A REDUCTION IN STATE AIDS TO INDUSTRY, WHICH WERE ALSO CUT LAST YEAR. DEFENCE SPENDING WAS MADE AN EXCEPTION TO LAST YEAR'S SEARCH FOR SAVINGS, BEING INCREASED BY 2 PERCENT IN REAL TERMS, WHILE THIS YEAR IT GOES UP BY 5 PERCENT IN REAL TERMS. TRAINING AND SECURITY ARE BOTH AGAIN GIVEN PRIORITY. THE EFFORT TO UNWIND THE INCREASE IN INCOME TAX IMPOSED AT THE START OF MITTERRAND'S TERM OF OFFICE IS ALSO PURSUED. MOST HOUSEHOLDS WILL ENJOY A 3 PERCENT REDUCTION IN THEIR TAX BILL UNDER THIS BUDGET AS UNDER THE LAST. (TWO MILLION WILL BE TAKEN OUT OF THE NET).

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4. THE GOVERNMENT CLAIMS TO BE THE FIRST IN THE DEVELOPED WORLD TO HAVE CUT TAXES AND THE DEFICIT SIMULTANEOUSLY. ITS OPPONENTS HAVE NOT BEEN SLOW TO POINT OUT THAT THE INCOME TAX CUTS OF 1.5 BILLION POUNDS ARE MATCHED BY AN INCREASE IN EMPLOYEES' SOCIAL SECURITY CONTRIBUTIONS OF THE SAME AMOUNT. WITHOUT PRIVATISATION RECEIPTS THERE WOULD BE LITTLE OR NO REDUCTION IN THE DEFICIT.

5. NEVERTHELESS, THE GOVERNMENT HAS FOUND THE BUDGETARY MEANS TO DRAMATISE ITS POLITICAL PHILOSOPHY, EVEN IF THE SUMS INVOLVED ARE NOT LARGE. IT HAS ABOLISHED THE WEALTH TAX AND GRANTED UPPER INCOME GROUPS AN ABOVE-AVERAGE REDUCTION IN TAX RATES BY LOWERING THE MAXIMUM RATE FROM 65 TO 58 PERCENT, WHICH BALLADUR HAS PROMISED WILL BE REDUCED TO 50 PERCENT IN THREE YEARS. THE TAX CONCESSIONS TO COMPANIES TAKE THE FORM OF LOWER TAXATION OF PROFITS FOR ALL, INSTEAD OF SELECTIVE AIDS. MARRIED COUPLES ARE NO LONGER TO BE AT A FISCAL DISADVANTAGE COMPARED TO COMMON LAW PARTNERS. THE TAX CONCESSIONS TO LARGE FAMILIES ARE TO BE INCREASED. INHERITANCE TAXES (ALREADY MUCH LOWER THAN THE UK) ARE LIGHTENED BY PARTIAL RESTORATION OF INCENTIVES TO LIFE-TIME GIVING. THERE ARE NEW INCENTIVES TO HOME-PURCHASE AND CONSTRUCTION OF ACCOMMODATION FOR LETTING.

6. DISRESPONDING ANY IDEOLOGICAL RESERVATIONS THE GOVERNMENT HAS INCREASED FUNDING FOR SOCIAL MEASURES TO ALLEVIATE UNEMPLOYMENT.

7. THE REDUCTION IN COMPANY TAXATION (1.1 BILLION POUNDS OUT OF TOTAL TAX CUTS OF 2.7 BILLION) IS MUCH LESS THAN EARLIER SEEMED INTENDED, BUT THE GOVERNMENT ARGUES THAT IT HAS ALLOWED COMPANIES TO BE THE PRIME BENEFICIARIES OF THE LOWER OIL PRICE, BY REFRAINING FROM INCREASING PETROL TAX WHEN THE PRICE DROPPED. IN ANY CASE IT IS NOT PROFITS TAX WHICH WEIGHS MOST HEAVILY ON COMPANIES, AMOUNTING ONLY TO 1.9 PERCENT OF GDP IN FRANCE COMPARE TO 4.4 PERCENT IN THE UK (1994 FIGURES), BUT SOCIAL SECURITY CONTRIBUTIONS WHICH CAN ADD AS MUCH AS 75 PERCENT TO BASIC WAGES. THE GOVERNMENT IS PLEDGED TO MAINTAIN SOCIAL SECURITY BUT IS LOOKING FOR SOLUTIONS TO THE LONG TERM PROBLEM OF UNDERFUNDING OF OLD AGE PENSIONS.

8. THE 1987 BUDGET IS BASED ON THE FOLLOWING ECONOMIC FORECAST FOR FRANCE, EXPRESSED AS PERCENTAGE INCREASES OVER 1986:

GDP (TRADE)	2.3
CONSUMPTION	2.0
COMPANY INVESTMENT	5.0
EXPORTS	4.8
IMPORTS	4.8
RETAIL PRICES (AVERAGE)	2.0

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2 THUS, COMPANY INVESTMENT AND EXPORT GROWTH ARE EXPECTED TO TAKE OVER FROM CONSUMPTION AS THE ENGINES OF GROWTH. (INVESTMENT RECOVERED CONSIDERABLY IN THE SECOND QUARTER OF THIS YEAR AND THE GOVERNMENT WILL BE HOPING FOR ITS CONTINUATION WHILE FEARING THAT IN THE ABSENCE OF A NEW INTERNATIONAL ROUND OF INTEREST RATE REDUCTIONS, COMPANIES WILL CONTINUE TO GIVE PRIORITY TO DEBT REDUCTION OR INVESTMENT IN FINANCIAL INSTRUMENTS.) THE PERSISTENT DECLINE IN THE SURPLUS ON TRADE IN MANUFACTURED GOODS MAKES THE FORECAST FOR EXPORTS LOOK OPTIMISTIC, AND BALLADUR IS NOT HIDING HIS UNCERTAINTY OVER THE PROSPECTS FOR WORLD TRADE.  
FCO ADVANCE TO MATHEWS EF2 DIV, HMT.

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F C O PLEASE PASS SAVINGS

PCLMAN 5123

*FRAME ECONOMIC.*

*ECO(1).*

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**THIS TELEGRAM  
WAS NOT  
ADVANCED**

(REPEATED AS REQUESTED)

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