



BULLETIN

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Hollande Chooses the German Path —and Poses a Challenge to Poland

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President François Hollande seems to have chosen a German-style supply-side economic policy to break France's downward spiral. He is seeking balanced results from the social dialogue between employee and employer organisations, to bring long-term prospects to the country's social model. And he is looking to complement his proposed "responsibility pact" with a proper "restart" of the Franco-German tandem to address eurozone imbalances. In this context, Poland should push forward a euro-accession roadmap by the end of the year and ensure dialogue with both France and Germany to influence a long-term vision of the eurozone. Yet, besides the attendant risks, France's supply-side policy may also create opportunities for Polish entrepreneurs.

Since his election in May 2012, President Hollande has been struggling with a legacy of excessive public debt and deficit, dwindling competitiveness, and one of the worst economic conjunctures in modern history. Despite the government's strong commitment to stemming unemployment, the number of full-time job seekers rose to a record high of 3.5 million in January (Metropolitan France and Overseas Territories). A spate of misleading governmental communications and leadership failures has left the population feeling rudderless. With his new "business-friendly toolbox," François Hollande intends to break the downward spiral and provide answers to an increasingly radicalised citizenry. But this domestic resort to German solutions also requires a restart of the Franco-German tandem in Europe.

Hollande's German Toolbox. With opinion polls showing his support at its lowest ever level (20%), Hollande had no choice but to boost the reform path. With a proposal to reduce the barriers to production and investment (so-called supply-side reform) labelled a "responsibility pact," the French Social-Democrat, as the leader of the Socialist Party (PS) presents himself, seems to be embracing a focus on competitiveness through fiscal discipline, high cuts in labour costs, and increased "flexicurity" in the labour market, all of which are more usually associated with Germany. His move comes just ahead of municipal and European elections that might well boost the Front National and undermine the exceptional dominance of the PS at all political levels (presidency, government, National Assembly, and Senate).

Although most details of the reform are still the subject of laborious negotiations between state, employers and trade unions, the building blocks of this new liberal approach have already been communicated. They include a minimum of €50bn cut from public expenditure, which would, notably, finance a total cut of €30bn in social contributions for private employers by 2017 (i.e., 1.5% of GDP); shock reform aimed at simplifying administrative procedures for businesses (*choc de simplification*); financial support of up to €25,000 for selected innovative foreign start-ups; and visa facilitation schemes (*Passeport Talents*) up to four years for seven categories of migrants. This new impulse was generally welcome as a "step in the right direction" by the main opposition party (the divided Conservative UMP), and foreign partners such as Germany, the UK and the United States.

Resistance from within Hollande's Own Camp. The pact may reflect the prevalence of German standards in the public sphere, but not everyone has shown the same enthusiasm as the president. The initiative has revived dividing lines within the PS, which might yet undermine him. In a rival policy document, one-third of PS deputies reminded him of his electoral promises and denounced the lack of concessions demanded from employers. To secure the vote of

confidence scheduled by the government in spring, a balanced deal between employers and trade unions is crucial. Hollande also needs to tackle social discontent around the downgrading of the social model, and precarious employment. With 82.4% of new work contracts being fixed term, the French have good reason to worry about their future (and reduce already weak domestic consumption).

With France the least unionised of the OECD members (8% compared to 18% for Germany and 70% for Sweden), much remains to be done to address structural problems linked to the representation of employees' interests. The apparent contradiction between the proposed inclusive method of drawing up the pact and the liberal goals that it aims to achieve has proved divisive, with most trade unions coming out against the overall rationale. Notwithstanding well-founded doubts regarding job creation, the new wave of protests by the unions on 18 March demonstrates, once again, the limits of *dirigisme* in the social dialogue and economy. The divisions within the two main parties, and their failure to offer alternatives, have strengthened the Front National.

De-rusting the Franco-German Engine. Poor socio-economic prospects in both France and Southern Europe further complicate President Hollande's work. In the absence of a monetary devaluation lever, the current eurozone imbalances demand common economic policies with a redistributive element and, consequently, a *relance* of the rusty Franco-German engine. Ahead of the May European elections, a combination of factors could herald a Franco-German compromise. These may include political radicalisation in many EU Member States besides France; the embrace of domestic supply-side reforms by France and Southern Europeans; the Merkel III government's apparent return to classic pro-European tenets; and growing criticism by the EU institutions towards Germany's inaction to encourage domestic consumption and reduce its trade balance surplus.

The imperative of strengthening European Monetary Union has already been recognised, in the Hollande-Merkel declaration of May 2013, and recalled in the Franco-German Council of Ministers on 19 February 2014. However, the proposed measures (for example, completion of the banking union, a full-time Eurogroup president, and differentiation between "ins" and "outs" within the European Parliament) might prove insufficient to restore markets' long-term confidence in the euro. With the spectre of cyclical economic turmoil, far-reaching initiatives such as those proposed by the French Groupe Eiffel Europe and its German counterpart, the Glienicker Gruppe (common unemployment insurance, financing common projects, and clearer definition of the subsidiarity principle), have unusual weight, not merely as a means of restarting the tandem, but also of breaking the short-termism of the EU's crisis management.

Recommendations for Poland. Hollande has little room for manoeuvre domestically. Against the background of an intense dialogue between the social partners, not to mention deep public disillusionment and internal party struggles, the Front National looks set to undermine the PS's current dominance. Furthermore, the effectiveness of Hollande's toolbox remains in doubt without support from both Germany and the European level, and even if France has managed to keep its head out of recessionary waters for about four trimesters now, the government is currently facing pressure from the European Commission to avoid a new excessive deficit procedure in 2015.

France's domestic turnaround and a revitalised Franco-German tandem are deemed essential to break the current fatigue towards the EU. But they may also pose a challenge for Poland's influence. In order to boost its credibility in the eurozone, and vis-à-vis Germany and France, Poland should look for full association in the reform process. This will require both a hedging relationship to the EU institutions, and a euro-accession roadmap.¹ The likelihood of a decrease in EU structural funds to Poland after 2020 further requires long-term planning, and the time is ripe for reflection on domestic reforms and promotion of public awareness about how an inclusive eurozone should look.

There are already moves to give substance to the Weimar Triangle, in its economic and security and defence aspects. Warsaw should work to ensure that eurozone affairs are at the core of this. It can mobilise intellectuals and policy-planners by forming a counterpart to Germany's Glienicker Gruppe and France's Groupe Eiffel. And it can engage business in the discussion, by pointing to the way that Hollande's business-friendly approach may create opportunities for Polish entrepreneurs. Regular sectoral dialogues on potential investments could boost Poland's rising position in relation to trade with France (currently 11th as client, and 13th as provider), and further develop the quality of its political relations with France.

¹ For similar conclusions, see A. Gostyńska, R. Parkes, "Europe and Its Institutions: Towards a Renewed Polish Approach to the EU," *PISM Strategic File*, no. 2 (38), 5 February 2014, www.pism.pl.