Creditreform Sovereign Rating

Creditreform Rating

Rating Object	Rating Information	
FRENCH REPUBLIC	Assigned Ratings/Outlook: **AA /stable**	Type: Monitoring, unsolicited
Long-term sovereign rating Foreign currency senior unsecured long-term debt Local currency senior unsecured long-term debt	Initial Rating Publication Date: Rating Renewal: Rating Methodologies:	26-08-2016 05-06-2019 "Sovereign Ratings" "Rating Criteria and Definitions"

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Rating Action

Neuss, 05 June 2019

Creditreform Rating has affirmed the unsolicited long-term sovereign rating of "AA" for the French Republic. Creditreform Rating has also affirmed France's unsolicited ratings for foreign and local currency senior unsecured long-term debt of "AA". The outlook is stable.

Key Rating Drivers

1. Very large, wealthy and resilient economy, displaying very high productivity levels; solid GDP growth set to remain in place in 2019/20, supported by purchasing power gains of households and a further decrease in unemployment; while labor markets continue to strengthen, challenges persist
2. Sovereign continues to exhibit a high-quality institutional framework, and benefits from integration in the European Union and the euro area; government has demonstrated its willingness to address structural shortcomings, and we expect broad adherence to the enshrined reform path
3. Budget deficit continued to narrow in 2018, driven by expenditure constraint; largely due to one-offs, we expect a temporary rise in the headline deficit this year before budget consolidation should resume in 2020
4. Elevated debt-to-GDP ratio should peak this year but decrease only slowly thereafter; fiscal sustainability risks arising from high spending on age-related expenditures tempered by favorable redemption profile and refinancing conditions
5. Limited external vulnerabilities stemming from moderately negative current account balance and net international investment position

Reasons for the Rating Decision

The French Republic's very high creditworthiness reflects its favorable institutional and macroeconomic performance profile, as well as solid fiscal and external metrics.

Macroeconomic Performance

The sovereign's credit ratings continue to be underpinned by the economy's favorable macroeconomic performance profile. While we continue to view the French economy's significant size and high income and productivity levels as major credit strengths, structural challenges related to the business environment and the labor market persist.

In our view, France can rely on its very large economy, which enhances its economic resilience against external shocks. At the latest count, France was the sixth largest economy in the world, with a gross domestic product totaling USD 2.76tr in current prices (IMF data). Thanks to its large and prosperous domestic market, France displays a relatively low exposure to cyclical swings in global economic activity. In 2018, exports made up for merely one third (31.3%) of economic output, which compares low to the euro area as whole (47.9%) and also to its largest trading partner Germany (47.0%). This partly reflects the sectoral composition of gross value added (GVA) in the French economy. Financial services and manufacturing activities, which we consider as rather cyclical, play only a minor role, accounting for 3.5 and 11.1% of total GVA respectively in Q4-18 (Eurostat data). On the other hand, the presence of a large service sector, which made up for 79.0% of GVA at the end of last year (EU-28: 73.3%), stabilizes the economy in times of weakening external demand. In this context, we note that the service sector is dominated by high value-added activities. At the latest count, the GVA share of ICT services stood at a high 5.4%, while real estate and business services together contributed more than a quarter (27.2%) to GVA – the highest proportion observed in the EU-28. As a result, productivity per hour worked exceeded the EU-28 level by 23.1% in 2017.

What is more, French citizens enjoy very high levels of prosperity by both global and European standards. Last year, French GDP per capita stood at USD 45,775 (PPP terms) according to IMF estimates, placing it in the top 15% of countries worldwide. As compared with AA-rated peers, we note that income levels are broadly on par with e.g. Finland (USD 46,430) and the UK (USD 45,705) but considerably lower than in Austria (USD 52,137).

Turning to France's growth record in the recent past, the moderate upswing we have observed since 2013 continued last year, albeit at a slower pace. After growth had hit a ten-year high of 2.3% in 2017, it softened to 1.7% in 2018. Thus, growth was still slightly above its 5y-average of 1.2% (2013-17) but continued to lag behind the euro area as a whole (1.9%) for the fifth consecutive year.

Last year's slowdown in GDP growth was entirely due to weaker domestic demand, which contributed 1.3 p.p. to economic expansion (2017: 2.1 p.p.) In particular, growth in gross fixed capital formation shifted into a lower gear. Following an exceptionally strong 2017, investment growth halved from 4.7% to a still robust 2.8% in 2018. While manufacturing investment held up well, with the growth rate rising from 1.1 to 2.0% in 2017-18, gross fixed capital formation in other sectors such as ICT and business services moderated. At the same time, the recent cooling of the housing market was mirrored by softer investment in construction, having increased by 1.5% in 2018, down from 5.0% a year before. From a sectoral point view, there are signs that NFCs postponed some investment activity to 2019 in view of rising domestic and external uncertainties (2018: 3.8%, 2017: 4.7%).

Moreover, 2018 witnessed lackluster growth in private consumption. The overall increase in consumer spending of 0.9% (2017: 1.4%) appears in particular weak against the background of further improving labor market fundamentals. A stronger expansion of private consumption was prevented by temporary factors such as railway strikes, and weakening consumer confidence translating into higher household savings. Moreover, sharply increasing HICP inflation limited purchasing power gains. While the savings rate rose slightly from 13.9 to 14.2% in 2018, the pick-up of inflation was more pronounced. Edging up from 1.2 (2017) to 2.1%, inflation hit a six-year high mainly due to rising energy prices and excise duty hikes. As a result, growth in household's disposable income eased from 1.4 (2017) to 1.2% in 2018. According to latest INSEE data, consumption appears to have proven resilient towards the end of the year, despite headwinds from weak car sales in the run-up to the increase of the scrappage premium (prime a la conversion) and the "yellow vest protests". By contrast, net exports strengthened markedly, making a growth contribution of 0.7 p.p. (2017: -0.1 p.p.), as import growth was curtailed by easing domestic demand, decelerating from 3.9 to 1.2%. Supported by vividly rising transport and textile exports towards the end of the year, export growth proved remarkably resilient in light of softening global trade (3.5%, 2017: 3.9%).

Anticipating real GDP growth of 1.4 and 1.5% in 2019 and 2020 respectively, we expect the French economy to retain its current growth momentum over the next two years. However, the economic expansion should be less broad-based than in 2018. Growth should be primarily driven by domestic demand, while net exports are unlikely to make a positive contribution. Our expectation is underpinned by latest quarterly national accounts data, according to which economic growth remained stable at 0.3% in this year's first quarter (Q3-18 and Q4-18: 0.3 and 0.4% respectively), with solid consumer spending and buoyant investment offsetting weaker exports. Given our expectation that economic growth in France's key trading partners (Germany, Italy, and the US) is facing a cyclical slowdown, export dynamics are likely to soften over the coming two years. At the same time, import growth should decelerate to a lesser extent in view of strengthening domestic demand.

First and foremost, private consumption is set to rebound strongly in 2019. With the scrappage premium for old cars being lifted up to EUR 2,500 in January 2019, new car registrations have recovered, coming in at 2018 levels in Q1. In general, household spending should be fostered by easing inflationary pressures due to somewhat lower oil prices and the cancellation of previously envisaged energy tax increases, as well as by notably rising household incomes. Apart from a minimum wage increase and sustained nominal wage growth in the private sector, the implementation of emergency economic and social measures (MUES) should be conducive to private consumption. Responding to the social protests, the government enacted a set of measures in December 2018 aimed at facilitating the purchasing power of low-wage earners and pensioners (see below). Drawing on Banque de France estimates, MUES alone may lift household's purchasing power by 0.7 p.p. in 2019. Going forward, household spending will presumably receive a further boost from the measures announced more recently at the end of April following the so-called Grand Debate (see below). As the vulnerable groups addressed by the measures typically have low savings rates and a high propensity to consume, we expect that a significant share of income gains will be used to expand consumption in 2019/20. We also note that the announcement of the policy package coincided with a turnaround in consumer confidence. After the EU commission's consumer sentiment indicator had deteriorated throughout 2018, it has steadily increased since December, with household's concerns about their personal finances gradually abating.

Notwithstanding our assumption that external demand will gradually slacken going forward, we are cautiously optimistic on investment. Government plans to ramp up public investment related to the implementation of the "Big Investment Plan 2018-22" should partly compensate for moderating, but solid private sector activity. Early indicators suggest that residential construction is unlikely to emerge from its soft patch soon. In March 2019 (-6.0% y-o-y), authorized dwelling permits declined for the thirteenth month in a row. Meanwhile, capacity utilization in the manufacturing sector is still consistent with solid growth in business investment, although it has eased somewhat from 85.9 (Q2-18) to 84.8% in Q2-19 amidst slowing external demand, ongoing trade tensions, and looming Brexit uncertainties. Capacity utilization was thus broadly aligned with its long-term average (1991-2018 avg. 83.3%), pointing to limited investment needs. On the other hand, recent monetary policy decisions should provide some support for investment in the near term. At its March meeting, the governing council decided to keep the refinancing rate at its present level (0.0%) at least until the end of 2019. Hence, we expect financing conditions for French NFCs to remain extraordinarily low, which should bode well for corporates' propensity to invest. Since the beginning of 2016, NFC rates on loans with maturity up to one year (ECB new lending, AAR) have been oscillating around 1.5%.

Solid GDP growth should be complemented by further improving labor market conditions in 2019/20. Thanks to sustained employment growth throughout the year (2018: +291,000 persons), the French unemployment rate fell from 9.2 to 8.8% in the year to the first quarter of 2019, the lowest reading since the beginning of 2009 (Q1: 9.1%). Nevertheless, unemployment still compares high to most euro area peers. At the end of 2018, only three euro area members, namely Italy (10.6%), Spain (14.5%) and Greece (18.5%) posted higher unemployment rates. Also, persistent labor market segmentation continues to present a challenge to the French labor market. Immigrants from outside the EU-28, as well as the young and low-skilled population, remain disproportionately affected by high unemployment. Simultaneously, job vacancies are on the rise, pointing to skill-mismatches. Since mid-2015, the number of vacancies in corporates with at least ten employees has more than doubled from 89,179 (Q2-15) to 186,511 in Q4-18. With regard to job security, we continue to observe significant differences between age groups. While the share of fixed-term contracts in total employment (15-64y) accounted for a moderate 14.8% in 2018, the majority (56.2%) of young employees (15-24y) was hired on a temporary base and transition rates to permanent contracts remained low.

Despite our expectation of solid growth in 2019/20, we assess France's medium-term growth prospects to be rather modest. As illustrated by AMECO data, private investment has been remarkably strong in recent years, with the investment-to-GDP ratio climbing from 18.1 to 19.5% over the last three years. Hence, France is one of few countries in the EU where private investment activity has exceeded its pre-crisis level (2007: 19.2% of GDP).

By contrast, lackluster TFP and labor productivity dynamics continue to weigh on the economy's growth potential.

Also, France has scope to improve conditions for doing business. According to the latest Doing Business report compiled by the World Bank, the country occupies only a middle ranking position in terms of business friendliness within the EU, and the distance to AAA peers remains considerable. The latest edition of the World Economic Forum's Global Competitiveness report confirms this view. Ranking 17th out of 140 countries (2017: rank 18) France remains in the first quintile of all countries assessed but continues to fare worse than European frontrunners Germany (rank 3), the Netherlands (rank 6), and the UK (rank 8). While France's infrastructure and innovation capability receive high scores, a high tax burden and extensive labor market regulations were identified as hampering business activity.

While accelerating FDI inflows in the recent past (2018: +36.3%) signal an improvement in competitiveness, export market shares and real unit labor costs (ULC) rather suggest a stabilization of France's competitive position. From a cross-country perspective, France's ULC adjustment is still mild by comparison, with real ULCs stagnating in 2012-18. At the same time, we observed improvements in the euro area as a whole (-1.7%), as well as in other major euro area economies such as Spain (-2.9%) and Italy (-2.3%). In the same vein, France's global export market share remained broadly unchanged in 2012-18, but the economy has not recovered from losses incurred between 2003 and 2010 when the export market share plummeted from 5.22% in 2003 to 3.83% in 2010.

To overcome these weaknesses, France is undergoing a process of far-reaching reforms pertaining to taxation, labor markets and its business environment. Although it is too early to assess the effectiveness of the government's reform agenda, we acknowledge that policymakers have started to decisively address the aforementioned shortcomings. More recently, the OECD estimated that ongoing supply side reforms could lift French GDP per capita by more than 3 percentage points over a 10-year period. Among others, French authorities lowered the labor tax wedge by the introduction of the tax credit for competitiveness and employment (CICE), promoted wage bargaining at the firm level, and revamped dismissal procedures to provide companies with greater legal certainty. While these reforms mainly focused on lowering labor costs to restore cost competitiveness, authorities have recently stepped up their efforts to foster labor market inclusiveness. Since mid-2018, ambitious educational reforms have been undertaken. Upper secondary and tertiary education was reformed in order to lower drop-out rates, while the apprenticeship and vocational training system was overhauled by the implementation of the "Career Choice Act" (Aug-18). By the end of the year additional measures will enter into effect, geared towards aligning school curricula with labor market needs and to reduce the impact of the socioeconomic background on educational attainment.

Alongside the ongoing implementation of labor market reforms, the government started to lower corporate income tax rates, which are currently the highest among OECD members. The statutory CIT-rate slightly decreased from 33.3 (2018) to 31% in 2019 (OECD data) and the French administration envisages a further reduction to 25% by the end of its term in 2022. Also, CICE tax credits were converted into a lasting reduction in employers' social security contributions at the beginning of 2019, which should have a dampening effect on labor costs going forward.

Furthermore, policymakers forged ahead with initiatives to strengthen the corporate sector's non-cost competitiveness by reducing red tape. On 11 April 2019, parliament adopted the Action Plan for Business Growth and Transformation (PACTE), a comprehensive set of pro-business reforms. The main objective of PACTE is to unlock the corporate sector's growth potential in order to stimulate job creation. In particular, the legislation aims to remove obstacles to doing business by simplifying business creation, supporting SME exports, and easing obligations concerning workforce thresholds.

Fiscal Sustainability

On the fiscal front, we note that the situation of public finances has notably improved in recent years and further progress was made with regard to budget consolidation in 2018. Decreasing from 2.8% of GDP in 2017 to 2.5% of GDP last year, net borrowing has steadily fallen since 2010 (6.9% of GDP). However, due to a softer macroeconomic backdrop and the inclusion of SNCF Réseau in the general government sector, the sovereign slightly missed the deficit target (2.3% of GDP) foreseen in the 2018 stability program.

In this context, it has to be highlighted that the government continued to follow its expenditure-based approach to budget consolidation. Primary spending increased by 1.9%, comparing favorably with nominal GDP growth of 2.5%. Most importantly, the state kept growth of its largest expenditure items in check. Spending on social benefits and public employees, which account for two thirds of budgetary expenses, increased by 1.8 and 1.1% respectively. As a result, the French expenditure-to-GDP ratio continued on its downward trajectory, falling from 56.4 (2017) to a still high 56.0% in 2018. Sustained expenditure containment was particularly important in view of bottoming interest expenses. After a cumulative decline by some 70% between 2012 and 2017, debt service costs remained broadly flat at EUR 40bn last year. Moreover, 2018 saw slowing revenue growth, which clocked in at 2.3%, down from 3.8% in the previous year. While VAT revenues expanded by a robust 4.3% on the back of employment growth and solid private consumption, property income (-0.5%) and corporate taxes (-5.2%) detracted from revenues, mirroring a reduction in the CIT rate, the repeal of the 3% distribution tax, and lower housing taxes.

Notwithstanding the progress that has been made with regard to budget consolidation in the recent past, French government debt remains among the highest in Europe and, apart from Belgium, significantly higher than in any other AA- or AAA-rated sovereign. On a positive note, the rise in government debt came to a halt for the first time since 2007 last year, with the debt-to-GDP ratio stabilizing at 98.4% of GDP. In September 2018, INSEE reclassified SNCF Réseau as a government entity, leading to a slight upward revision of 2016 and 2017 debt levels. With the envisaged fiscal loosening, we anticipate the sovereign's debt-to-GDP ratio to peak at around 99% of GDP this year. Beyond 2019, we expect that moderate economic growth and sustained primary deficits will allow for only very gradual debt reduction.

Risks arising from high public debt are somewhat mitigated by a low interest to revenue ratio of 3.2% (2018). Furthermore, French authorities continue to take advantage of the beneficial interest rate environment, engaging in sound debt management. The average weighted maturity was extended to 7.9 years by March 2019, climbing from 7.5 years at the end of 2016, and the share of short-term debt in total outstanding negotiable debt was reduced from an already low 8.3 to 6.0% over the same period (AFT data). Long-term bond yields remain close to historical lows, buttressed by ongoing reinvestment under the ECB's asset purchase program and strong investor appetitive for French government bonds. Since our last review, yields on French 10y bonds have fallen from an already low 0.8 to 0.3% (10-05-2019).

This year, we expect the budget deficit to temporarily spike to 3.2% before falling back to 2.3% in 2020. Most importantly, the conversion of CICE tax credits in the amount of EUR 20bn into a permanent social security contribution in 2019 should result in a 0.9 p.p. deterioration of the government's headline balance. Secondly, measures adopted in December 2018 to allay the yellow vest movement will lead to an increase in the deficit. President Macron announced a bundle of measures with a gross budgetary impact of approx. EUR 10bn, geared towards improving the living standard of low- and middle-income earners. The government thus decided to exempt overtime pay from certain payroll taxes, to lower social security contributions (CSG) for pensioners that are under EUR 22,580 a year, the repeal of the energy tax increase, and higher in-work benefits. To be sure, authorities envisage to partly counterfinance the policy package. A new tax on digital services, a one-year postponement of the corporate tax cut for large companies and savings in the public sector are envisaged to generate EUR 4bn. These measures were followed by another package of policies, outlined by President Macron after the conclusion of the Grand Debate at the end of April, which should have a gross budgetary impact of another EUR 7bn from 2020 onwards. The government tabled plans to cut the household income tax, increase the minimum retirement pension, and reinstate inflation-indexation for pensions below EUR 2,000. While the President reiterated the government's strong commitment to keep the budget in check, e.g. by improving tax collection, spending cuts, and an increase in hours worked, these plans need further specification. To be sure, the headline deficit is likely to remain well below 3% of GDP. Still, the most recent package carries some downside risks to the fiscal outlook.

Against this backdrop, compliance with the healthcare and local spending ceilings appears key to maintaining fiscal consolidation. We note that the healthcare spending norm (Ondam) has seen some upward revisions in the recent past and was set at 2.5% p.a. in the latest budget, up from 2.3% in 2018. Meanwhile, the ceiling for operating expenditures of local public administrations (Odedel) was set at 1.2%. In this regard, we view it as positive that the three quarters of the country's 322 largest local authorities have contractually committed themselves to fiscal discipline by signing a legally binding agreement with the central government for the first time in 2018.

In the same vein, the successful implementation of the public sector and unemployment insurance reform could generate some savings. To lower the public wage bill, the government launched a public sector reform in March 2019 that envisages the loss of 120,000 jobs over the next three years. Last year, the public wage bill (general government level) totaled 12.5% of GDP – the highest reading in the euro area. Furthermore, the current system of unemployment benefits is relatively generous. As evidenced by OECD data, the net replacement ratio of unemployment benefits stood at 68% in 2018, comparing high to an OECD total of 59%. After negotiations between unions and employers had failed this February, the government announced it would come up with a new proposal. Although we have limited visibility on the eventual shape of the reform, as well as on the timeline of implementation, officials have hinted that any reform will likely include a reduction of the maximum payout, currently set at a high EUR 7,700 per month.

Meanwhile, demographic challenges related to France's ageing population are comparatively moderate in a European context, as its working-age population is projected to diminish by only 3.7 p.p. of the total population by 2030 as compared to an average decline of 4.2 p.p. in the EU-28. However, age-related expenditures are already putting pressure on public finances. Total age-related expenditure made up for 31.0% of GDP in 2016 (EC 2018 Ageing Report), the highest share in the EU-28, and latest projections suggest that costs may rise further over the next decade, reaching 31.5% of GDP by 2030. Even though this estimate does not account for the forthcoming pension reform, we believe the envisaged measures are rather unlikely to result in significant cost savings. In October 2018, the government outlined the main reform strands to make the pension system more equitable. A cornerstone of the reform is to align the retirement systems in the public and private sectors by merging the current 42 retirement schemes into a single system; yet the statutory retirement age will be kept unchanged at a low 62 years, as attempts to raise the legal retirement age met fierce opposition in the past.

With regard to the financial sector, we believe that there are no imminent risks which could have an adverse impact on public finances in the near term, as French banks with assets totaling 315.8% of GDP in Q3-18 continue to display notable capital buffers and strong asset quality. In the year to Q4-18, banks' CET1-ratio remained stable at 14.2% (Q4-17: 14.3%), broadly in line with EU-28 levels (14.7%). Concurrently, the NPL-ratio has continued to decline since our last review, falling from 3.1 (Q4-17) to 2.8% at the end of 2018 (EU-28: 3.2%). Risks associated with vivid credit growth, which has been accompanied by rising private debt, should be vigilantly monitored. Three months into 2019, growth in bank loans continued to outpace GDP, which may result in increasing banking sector vulnerabilities if sustained over a longer period of time. Loans outstanding to NFCs grew at a rate of 5.6% y-o-y in March 2019, comparing high with most euro area members. At the same time, credit to households continued to expand in the 5-6% range. In particular, consumer credit, which increased by 5.0% in March, has accelerated notably since spring 2015, primarily driven by automobile financing.

As a result, debt accumulation in the private sector continued. As illustrated by ECB data, household's debt-to-disposable income ratio has increased by some 20 p.p. since the end of 2008, reaching a high 95.6% in Q4-18 (Q4-17: 93.3%). Edging up from 87.6 (Q4-17) to 89.1% of GDP in Q4-18, NFC debt also continued on its longer-term upward trajectory. Accordingly, NFC debt not only stood well above the euro area median of 74.9% of GDP, but was also higher than in the other major European economies. Although the latest increase in French NFC-debt was partly driven by lending to foreign subsidiaries and the build-up of cash buffers, which increased from 26.8 to 27.7% of GDP in the year to Q4-18, it has prompted regulatory authorities to implement additional macroprudential rules.

To prevent the build-up of financial stability risks, the French High Council for Financial Stability ordered the country's six biggest banks to limit their credit exposure to the most indebted companies to 5% of their capital. Moreover, regulators set the countercyclical capital buffer on risk-weighted assets from currently 0.25 to 0.5%, as loan growth is showing no sign of slowing down.

Institutional Structure

The sovereign's rating continues to be supported by the high quality of its monetary and political institutions.

In general, we believe that the French economy benefits from EU integration and euro area membership, which entails broader and deeper capital markets as well as advantages related to the euro as a reserve currency. Monetary policy is conducted by the highly credible and accountable ECB. Since the adoption of the euro, we have not observed any sizeable interest rate differentials, and consumer prices have moved broadly in line with the EA-19 average. The lack of monetary flexibility is somewhat offset by the size of the French economy. Given that France is the second-largest member of the currency union, accounting for 20% of the euro area's economic output in 2018, we believe that economic developments in France will continue to have a notable impact on the ECB's monetary policy stance.

Our institutional assessment also incorporates the country's longstanding track record of high governance standards. While France's performance on the World Bank's Worldwide Governance Indicators (WGI) lags somewhat behind AA-peers Finland, Austria and UK, we believe that the country's credible and effective institutions represent a key credit strength. While the quality of public services is high, perceived corruption is low and the constitution provides extensive checks and balances to power. These characteristics are mirrored by favorable rankings along all dimensions of the World Bank's World Governance Indicators (WGI), as France is ranked 26th, 23th, and 27th on the sub-indices for government effectiveness, rule of law and control of corruption, comparing well to the respective euro area median (33, 32, 41).

In general, the strong role which the French constitution assigns to the President in policy-setting, coupled with a comfortable parliamentary majority, should be conducive to cohesive policy-making going forward. After the 2017 general elections, president Macron's La République en Marche claimed 308 out of 577 seats in the national assembly. Looking ahead, however, we believe a swift and decisive implementation of structural reforms has become more challenging in light of the emergence of heavy resistance among some segments of the population. To soothe the protests, Macron made some concessions, and popular support has somewhat recovered more recently. Against this backdrop, we expect the government to remain broadly committed to its reform agenda, but social considerations are likely to play a more prominent role related to scope and timeline of implementation of future reforms.

Foreign Exposure

Risks pertaining to France's external position appear contained, as we see no major imbalances at the current junction. The country has run moderate current account deficits averaging at -0.7% of GDP over the last decade, but we note that the current account was close to balance more recently. Last year the current account deficit slightly narrowed from 0.6% (2017) to 0.3% of GDP on the back of strengthening trade and income balances. Up from 2.3 to 2.4% of GDP, the primary income surplus reached its highest level since 2011. Concurrently, the trade balance improved from -0.9 to -0.7% of GDP.

Looking ahead, the French economy should continue to operate at a small current account deficit as robust domestic demand continues to support import activity. At the same time, we expect exports to lose momentum against the backdrop of a cooling global economy. Alongside the current account balance, France's net international investment position (NIIP) should also remain in negative territory for the foreseeable future, mirroring the government and financial sector's external liabilities. In 2018, the NIIP ticked up from -20.1 (2017) to -11.4% of GDP on the back of improving net FDI and portfolio investment balances.

Rating Outlook and Sensitivity

Our Rating outlook on France's sovereign ratings is stable, as we assume that the risk situation underlying the key factors affecting sovereign credit risk – including macroeconomic performance, institutional structure, fiscal sustainability, and foreign exposure – will remain fundamentally unchanged in the next twelve months.

We could raise the French Republic's sovereign rating to AA+ if medium-term growth outperforms our expectations, or if public finances improve significantly and sustainably. We view a comprehensive implementation of the government's ambitious structural reform program as imperative for a rating upgrade, as the far-reaching structural reforms may boost the economy's competitiveness and improve the still impaired fiscal metrics.

By contrast, we could lower the rating if we observe significant fiscal slippages resulting in further increasing government debt, if medium-term growth prospects fall short of our baseline scenario, or if competitiveness deteriorates significantly. In the same vein, downward pressure on the ratings could arise if we observe significant delays or failure in implementing the envisaged reforms or, worse, if we perceive backtracking on already adopted structural reforms.

Primary Analyst
Johannes Kühner
Sovereign Credit Analyst
j.kuehner@creditreform-rating.de
+49 2131 109 1462

Chair Person
Benjamin Mohr
Head of Sovereign Ratings
b.mohr@creditreform-rating.de
+49 2131 109 5172

Ratings*

Long-term sovereign rating	AA /stable
Foreign currency senior unsecured long-term debt	AA /stable
Local currency senior unsecured long-term debt	AA /stable

*) Unsolicited

Economic Data

	2013	2014	2015	2016	2017	2018	2019e
Real GDP growth	0.6	1.0	1.1	1.1	2.3	1.7	1.4
GDP per capita (PPP, USD)	40,031	40,966	41,687	42,525	44,168	45,775	46,978
HICP inflation rate, y-o-y change	1.0	0.6	0.1	0.3	1.2	2.1	1.3
Default history (years since default)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Life expectancy at birth (years)	82.4	82.9	82.4	82.7	82.7	n.a.	n.a.
Fiscal balance/GDP	-4.1	-3.9	-3.6	-3.5	-2.8	-2.5	-3.2
Current account balance/GDP	-0.5	-1.0	-0.4	-0.8	-0.6	-0.3	n.a.
External debt/GDP	193.8	209.1	209.2	213.5	210.8	217.3	n.a.

Source: International Monetary Fund, Eurostat, own estimates

Appendix

Rating History

Event	Publication Date	Rating /Outlook
Initial Rating	26.08.2016	AA- /stable
Monitoring	28.07.2017	AA- /positive
Monitoring	01.06.2018	AA /stable
Monitoring	05.06.2019	AA /stable

Regulatory Requirements

In 2011 Creditreform Rating AG (CRAG) was registered within the European Union according to EU Regulation 1060/2009 (CRA-Regulation). Based on the registration Creditreform Rating AG is allowed to issue credit ratings within the EU and is bound to comply with the provisions of the CRA-Regulation.

This sovereign rating is an unsolicited credit rating. The Agence France Trésor (AFT) participated in the credit rating process as the AFT provided additional information and commented on a draft version of the report. Thus, this report represents an updated version, which was augmented in response to the factual remarks of AFT during their review. However, the rating outcome as well as the related outlook remained unchanged.

The rating was conducted on the basis of CRAG´s "Sovereign Ratings" methodology in conjunction with its basic document "Rating Criteria and Definitions". CRAG ensures that methodologies, models and key rating assumptions for determining sovereign credit ratings are properly maintained, up-to-date, and subject to a comprehensive review on a periodic basis. A complete description of CRAG´s rating methodologies and basic document "Rating Criteria and Definitions" is published on the following internet page: www.creditreform-rating.de/en/regulatory-requirements/.

To prepare this credit rating, CRAG has used following substantially material sources: International Monetary Fund, World Bank, Organization for Economic Co-operation and Development, Eurostat, European Commission, European Banking Authority, European Central Bank, Banque de France, Agence France Trésor, INSEE, Ministère de l'Économie et des Finances.

A Rating Committee was called consisting of highly qualified analysts of CRAG. The quality and extent of information available on the rated entity was considered satisfactory. The analysts and committee members declared that the rules of the Code of Conduct were complied with. No conflicts of interest were identified during the rating process that might influence the analyses and judgements of the rating analysts involved or any other natural person whose services are placed at the disposal or under the control of Creditreform Rating AG and who are directly involved in credit rating activities or approving credit ratings and rating outlooks. The analysts presented the results of the quantitative and qualitative analyses and provided the Committee with a recommendation for the rating decision. After the discussion of the relevant quantitative and qualitative risk factors, the Rating Committee arrived at a unanimous rating decision. The weighting of all risk factors is described in CRAG´s "Sovereign Ratings" methodology. The main arguments that were raised in the discussion are summarized in the "Reasons for the Rating Decision".

As regards the rating outlook, the time horizon is provided during which a change in the credit rating is expected. This information is available within the credit rating report. There are no other attributes and limitations of the credit rating or rating outlook other than displayed on the CRAG website. In case of providing ancillary services to the rated entity, CRAG will disclose all ancillary services in the credit rating report.

The date at which the credit rating was released for distribution for the first time and when it was last updated including any rating outlooks is indicated clearly and prominently in the rating report; the first release is indicated as “initial rating”; other updates are indicated as an “update”, “upgrade or downgrade”, “not rated”, “affirmed”, “selective default” or “default”.

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Creditreform Rating AG

Creditreform Rating AG
Hellersbergstrasse 11
D - 41460 Neuss

Phone	+49 (0) 2131 / 109-626
Fax	+49 (0) 2131 / 109-627
E-Mail	info@creditreform-rating.de
Internet	www.creditreform-rating.de

CEO: Dr. Michael Munsch
Chairman of the Board: Prof. Dr. Helmut Rödl
HRB 10522, Amtsgericht Neuss