

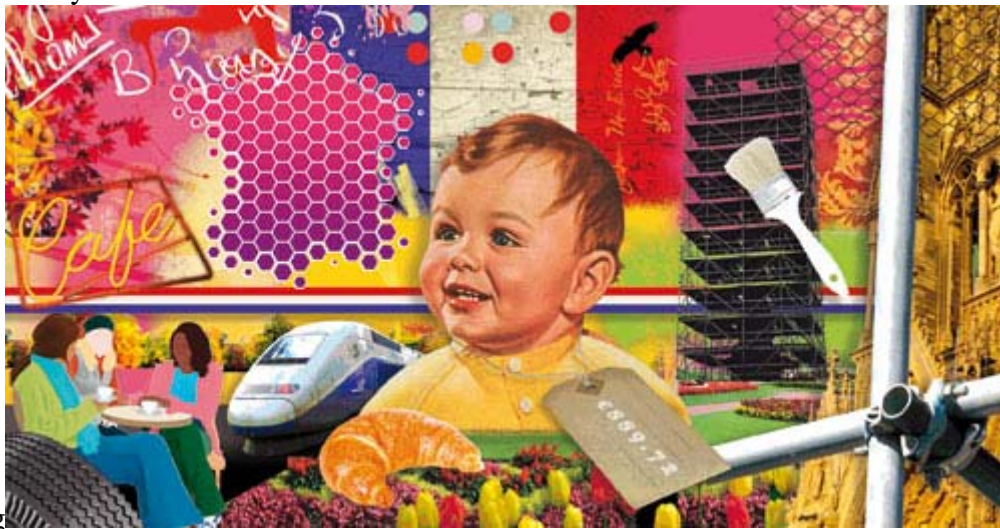
# The French model

## Vive la différence!

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### The French way of doing things looks pretty good—at least in these troubled economic times

Illustration by Matt



Herring

OVER 60 metres (nearly 200 feet) above the ground in the Picardy town of Beauvais, fiscal stimulus *à la française* is under way. With tiny paintbrushes and sandblasters, artisans perched on scaffolding are painstakingly scraping away at the damaged façade of the towering 14th-century gothic cathedral. The €2m (\$2.7m) restoration is one of 1,000 projects put in place by the French government as part of its €26 billion stimulus plan. Along with more conventional schemes, such as upgrades to motorways, ports and the TGV high-speed train network, France's boost includes the scrubbing up of a host of its historic cathedrals and churches.

Even in a crisis, the French do things differently. Despite calls from the Americans to do more to lift consumer demand, their stimulus plan relies heavily on front-loading investment in infrastructure, cathedrals included, in line with their *dirigiste* tradition. A strong beneficent state, with heavy taxation, regulation and protection, is common to many continental European countries. But nowhere is it more pronounced or entrenched than in France, where it reaches back to the construction of roads, canals and industrial mammoths under Jean-Baptiste Colbert, Louis XIV's minister of finance and industry.

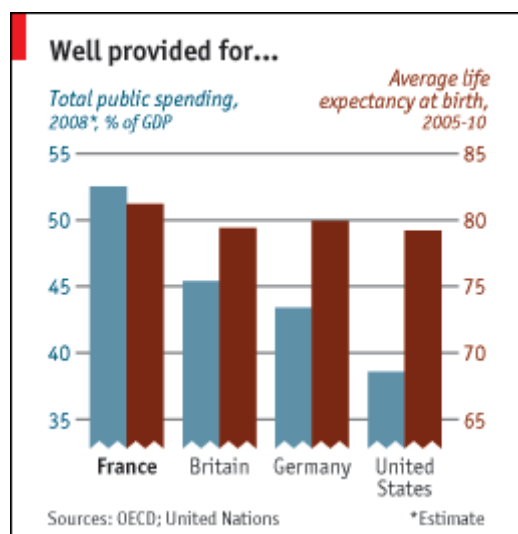
In recent years, before the financial crash, what is loosely known as the French model came in for fierce criticism, chiefly for failing to generate enough growth or jobs. Its detractors have not only been *les Anglo-Saxons* but have also included Nicolas Sarkozy

himself. He may be better known now for proclaiming the end of laissez-faire capitalism. But he was elected France's president partly by arguing that the French model was moribund, and picking out the British and American models for praise.

Before him, a string of government-commissioned reports, written by such authors as Michel Camdessus, a former IMF managing director, and Michel Pébereau, chairman of BNP Paribas, laid bare the failings and costs of the system. France's public spending accounted for 52% of GDP in 2007, next to 45% in Britain and 37% in America. Yet in 1997-2007 its annual rate of GDP growth was below the OECD average.

To be sure, the French economy has been battered by the global recession like any other. Firms are cutting output and shedding jobs. Unemployment reached 8.6% in February. There have been regular mass rallies across France in protest at job cuts. More sinisterly, there has been a wave of "boss-napping", a form of kidnapping in which managers are kept by workers overnight in their own offices.

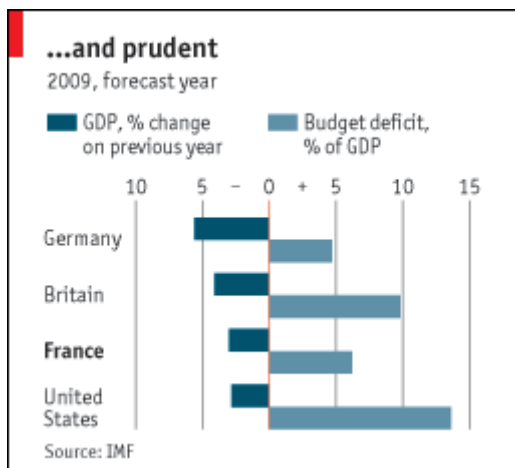
Yet France's economy has been less hard hit than many. Its GDP is expected to shrink by 3% this year, according to the IMF, against 4.1% in Britain, 4.4% in Italy and 5.6% in Germany (see charts). It is less dependent on exports than Germany, and consumer spending in the first quarter of 2009 was up on the same period last year. The government, usually reprimanded for profligacy, is set to have a deficit in 2009 (6.2% of GDP) well below those in America (13.6%) and Britain (9.8%).



The French are great savers and most have not taken out unaffordable mortgages or spent heavily on credit. Household debt as a share of GDP is less than half that in Britain or America. The prospect of nationalising banks may give Americans nightmares about turning French. In fact the French government has not yet had to rescue any big French bank from collapse, let alone nationalise one. Though there is outrage at bonus payments in firms laying off workers, bosses' pay in France is not that extravagant, and the income gap between the top 10% and the bottom 10% is far smaller than in Britain or America.

Indeed, with a mix of amusement and self-satisfaction, the French have watched *les Anglo-Saxons* start to sound, well, increasingly French. Barack Obama says he wants Americans to save more and consume less, to make real things rather than short-term

paper profits, to redistribute more wealth and provide health care for all. When he dropped in on Strasbourg, in eastern France, a town now linked by the TGV to Paris in little over two hours, he asked enviously: “Why can’t we have high-speed rail?” *Time* ran an article entitled “How we became the United States of France”. *Newsweek* published one claiming that “The last model standing is France”. When Christine Lagarde, France’s finance minister, appeared recently on Jon Stewart’s “The Daily Show”, an American comedy programme, she joked that “maybe you are moving in our direction.”



In Britain, Gordon Brown has declared—like Mr Sarkozy—that “laissez-faire has had its day”. Business chiefs clamour for Britain to get itself a proper industrial policy and stop relying on the mirage of finance. Howard Davies, head of the London School of Economics, wrote in praise of “French lessons on the state’s new role”. Even Peter Mandelson, a former European trade commissioner whom the French regard as a high priest of economic liberalism, recently turned up in Paris to learn more about what he calls industrial activism. “We have something to learn from continental practice,” he said, identifying French long-term strategic planning in such sectors as energy and transport.

To French ears, all this is rather pleasing. Mr Sarkozy hailed the G20 London summit as the end of the Anglo-Saxon model of capitalism. *Le Monde*, a leading daily, wrote: “In the crisis, the French model, formerly knocked, finds favour once more.”

## Croissants and car tyres

Behind the loose terms and caricature, however, what exactly does the French model consist of? Does it work? As governments try to work out the best balance between the market and the state, have the French got that balance right after all?

The low-lying region of Picardy in northern France has been as battered by the global slump as any other. Workers at Continental, a tyre manufacturer, recently trashed an administrative building when the courts upheld the closure of a factory at Clairoux, with the loss of 1,120 jobs—a crushing blow to employees who had agreed to work a longer week in return for a promise to keep the site going. In nearby Beauvais, Bosch closed its factory last year, putting 240 people out of work. Now there are worries about the future of a sponge factory in the town.

Yet at lunchtime on a warm spring day, tables at the pavement cafés in the town centre, near the scaffolding-clad cathedral, are all taken. Municipal flowerbeds, where cornflower-blue lupins nestle next to ornamental cabbages, are well stocked and tended. The car park at the local hypermarket is packed. Traffic at the nearby low-cost airport, a big employer, is still busy. And local electronics and perfume factories are holding up well. “This is not a rich town,” says Caroline Cayeux, the centre-right mayor. “But having the French social system enables people to keep their heads above water.”

Beauvais, the administrative capital, captures the cushioning effect of the French model in recession, and its strong egalitarian ethos. On the one hand, there is widespread fear of job losses. On the other, there is a sense that the economy is propped up even in bad times by the public sector and the welfare system. Fully 43% of the town’s residents live in rent-subsidised social housing. The town hall itself is a big employer. Some 130 gardeners, for example, toil away in its flowerbeds year-round, digging, weeding and planting. It also distributes all manner of direct help to families, such as vouchers for children’s holidays or after-school activities. It has devised a special scheme for the 4,500 “working poor”, who fall outside other national welfare safety-nets.

Across France, 5.2m workers, or 21% of those with jobs, are employed by the public sector. If you count others whose incomes or jobs are not exposed to the economic cycle, 49% of those either in work or retired are only moderately vulnerable to the recession, according to Xerfi, an economics consultancy. Add to that layers of social protection, including unemployment benefits that can reach up to 75% of previous salary, and a raft of direct payments for families, such as €89.72 for newborn babies, and the French are relatively sheltered from market downturns.

Moreover, France’s health system, a mix of private and public provision, manages both to guarantee universal coverage and produce a relatively healthy population for half the cost per person of America’s, and with shorter waiting lists than Britain’s somewhat cheaper version. The French have higher life expectancy than both the British and Americans. Through means-testing, the state covers those without the top-up private insurance needed to complement the public scheme.

All these “automatic stabilisers”, argues Ms Lagarde, help to support demand and should be counted as part of the fiscal stimulus package. Indeed, the finance ministry has received many recent visits from other governments’ officials interested in the French system. “The difference is that the French model provides shock absorbers that were already in place,” she comments. “We haven’t had to reinvent our unemployment, health or welfare systems.”

A central feature of the French model is the state’s role as provider, cushioning citizens, redistributing wealth and propping up demand in hard times. But it has two other functions: planner and regulator.

## **The ghost of Colbert**

The French finance ministry is housed in a vast modern structure that juts out on pillars into the Seine in eastern Paris. The finance minister also has use of the Hôtel de Seignelay, an elegant 18th-century riverside mansion in the capital’s fashionable heart. Outside the minister’s parquet-floored office stands a fine bust of Colbert, whose

grandson lived in the house. Colbertist state planning helped to reconstruct France after the second world war, delivering the *trente glorieuses*, or 30 years of post-war economic growth. Until recently an official “planning commission”, in charge of strategic four-year plans, still operated. The official body has gone, but the spirit, like the bust, lives on.

Long-term planning of public infrastructure is the best example of where it works well. London’s first fast-link cross-city underground line, Crossrail, is not due to open until 2017, but Paris boasts a network of five such RER lines, first launched in the late 1960s. Mr Sarkozy has just unveiled the latest step: a ten-year project to build an automated metro loop around the city outskirts, linking the main airports. France’s TGV network, whose first tracks were laid in 1974 under Georges Pompidou, continues to spread. The construction costs are heavy, with debt now hived off into a separate rail-network entity. Yet with average speeds of 300km per hour (190mph), the trains provide a viable and ecological alternative to air and road travel. Many businessmen use the TGV for daily trips between big French cities.

Or take the nuclear industry. The French government decided to push nuclear power in a big way back in the 1970s, in response to the oil shock and the country’s lack of fossil fuels. Nuclear energy now generates 78% of all French electricity, and the country is a net electricity exporter. In EDF and Areva, it has two of the world’s leading nuclear companies. France is now pioneering the construction of the latest-generation, missile-proof, earthquake-proof power plant, the EPR, with other countries set to adopt the same design.

Such French strategic planning is not only about long-term vision and infrastructure; it is also about putting in place the industrial supply chain needed to get there. The French state has either created companies (EDF, Areva) or bailed-out troubled private ones (Alstom, the manufacturer of the TGV train) in order to keep the supply side going. Such planning extends to education too. France has a world-class layer of engineering, business and public-administration schools, known as *grandes écoles*, which churn out a technically skilled elite to run such firms. It is no coincidence that the bosses of EDF (Pierre Gadonneix), Alstom (Patrick Kron), and Areva (Anne Lauvergeon, see [Face Value](#)) are all graduates of *grandes écoles* in science or engineering.

The impulse to control, which underpins the French model, extends to the third function of the state too, that of regulator. The French are champion rule-makers. There are rules about how many pharmacies any one pharmacist can own (one), and how many taxis there are on the Paris streets (15,300). There are rules about when lorries can use motorways (not on Sundays), or when shops can hold sales (twice a year, on dates set by officials). New rules allowing shops to pick freely another two weeks have been greeted as a revolution. “To have cut-price discounts in April without waiting for the June sales is unheard-of!” exclaimed *Le Parisien* newspaper. Some of these rules seem absurd. But, in the financial sector, France’s regulatory urge has served it well in the current crisis.

France’s big banks may have lost plenty of money, but they have certainly performed better than their British or American peers, and most are still in profit. One reason is tighter regulation. Take the mortgage market. French banks have generally been far more wary about lending to homebuyers. In 2007 French mortgage debt represented

only 35% of GDP, according to the European Mortgage Federation, less than in Germany (48%) and way off that in the housing-bubble economies of Britain (86%), Ireland (75%) and Spain (62%). French house prices did rise strongly. But the Bank of France argues that this was as much because of demographic growth, higher real disposable income and limited housing supply as speculative buying.

How far all this is due to regulation is hard to measure precisely. One leading French official reckons the answer is half thanks to a tradition of cautious borrowing, and half thanks to stricter rules. France applies tighter rules on bank capitalisation than international standards dictate. The regulator also recommends that banks should not make loans on which interest payments represent more than a third of the borrower's income. Banks are under a legal obligation not to push borrowers into more debt than they can manage, and cases are regularly brought to court. So caution is built into the system.

## Now for the flipside

If the French model has broadly sheltered its people from credit-fuelled excess, kept demand buoyant and inequalities manageable, and delivered well scrubbed buildings and blooming flowerbeds to boot, does this mean that the model works? Or what is the catch? The answer lies in a generally disappointing macroeconomic performance, with low growth and high unemployment, and is explained by the flipside of each of the three roles the French model allocates to the state.

First, as a provider, the government taxes employers and employees with such heavy social-security contributions to pay for all the health and welfare that it ends up deterring firms from creating jobs in the first place. One reason why French workers are more productive per hour than Americans is that firms employ so few of them. Many make widespread use of rotating interns and temps. One fast-food boss says that he staffs the same restaurants in France with two-thirds of the numbers hired in Britain. France's jobless rate (8.6%) may now be the same as America's (8.5%). But, unlike America's, it never falls much below 8% even in good times.

The upshot is a split employment market. On one side, decent permanent jobs, protected by industry-wide conventions negotiated by the unions. On the other, unprotected short-term work—or none at all. The young are particularly shut out: joblessness for the under-25s is 21%. On some housing projects in the heavily Muslim *banlieues*, the rate is double that.



Illustration by Matt Herring

The state as planner has its flaws too. French industrial policy has evolved, and is no longer just about big planes, trains and cars. There is, for instance, a generous new research tax credit for companies, designed to boost innovation in industry particularly in the carbon-light and high-tech sectors. A new “auto-entrepreneur” system to encourage self-employment, and run on the basis of “no profit earned, no tax due”, has lured a massive 145,000 people since it was launched in January, well ahead of official expectations. “Anybody who says that the French just want to be civil servants and not entrepreneurs hasn’t got it,” declares Ms Lagarde.

But, as a senior French official points out, the Colbertist engineering culture is on the whole much better at devising and managing big planned projects than it is at dealing with bottom-up ideas and uncertain markets. France lacks start-ups, and its small firms have difficulty growing. Hardly any of the biggest companies listed on the Paris bourse were founded in the past 50 years. Moreover, the old-style policy of picking national champions has had, at best, a mixed record. Transport and utility firms may be one thing. In other sectors, including computers (remember Groupe Bull) or banking (think of Crédit Lyonnais under state ownership), it has been a disaster. Even the French have been unwinding public stakes in private enterprise over the past 15 years. There has been no widespread nationalisation for more than a quarter of a century.

Nor is the egalitarian impulse necessarily a guarantor of quality, as French universities demonstrate. In reality, France has two-tier higher education: its world-class *grandes écoles* cater to a tiny elite, and its broadly second-rate universities fail the masses. Tuition at universities is free. There is no undergraduate selection at entry. Recent reforms have begun to inject an element of competition, and could produce centres of excellence in time. But, for the rest, a virulent distrust of competition and selection has led to overcrowded amphitheatres, an oversupply of philosophy and sociology students and high drop-out rates. In the Shanghai Jiao Tong University’s world ranking, not one French university makes it into the top 40.

As for the state as regulator, it may have protected the French economy from extreme volatility, but that goes for the upside too. A more stable economy in a recession also means a less dynamic, less innovative economy in good times. For all its positive elements, the French model has not yet not incorporated enough flexibility, leaving it

with the task of ensuring solidarity, but not the dynamic growth needed to sustain it in the long run.