



France

Growth prospects and confidence

- The government maintained its growth forecast of 1.5% for both 2016 and 2017.
- This seems like an optimistic outlook given the expected dissipation of certain growth support factors while new headwinds will also emerge.
- The September INSEE business confidence surveys were rather upbeat. But they are still not on a distinctly upward trend, testifying the lack of momentum of the recovery.

At the 20 September presentation of the broad outlines of its 2017 draft budget bill, the French government confirmed that it is maintaining its growth forecasts for France at an average annual rate of 1.5% for both this year and the next. However, we are of the view that the lack of acceleration from one year to the next reflects only partly the several less favourable growth factors, and even some negative ones, in 2017 (higher inflation; the abating of the positive impact of low oil prices and the euro's depreciation; the consequences of Brexit). Maintaining such a relatively high growth rate seems to be excessively optimistic¹.

The government's estimates are, indeed, in the upper range of the consensus forecasts and of those of the international institutions (see table). The OECD has just revised downwards its forecasts as part of its September interim scenario, by 0.1 points to 1.3% in 2016 and by 0.2 points to 1.3% in 2017. In its July update, the IMF also revised its forecasts with respect to its April outlook: up 0.4 points to 1.5% for 2016 and down 0.1 points to 1.2% for 2017.

The European Commission's forecasts are higher (1.3% in 2016 and 1.7% in 2017), but they date back to May, prior to the Brexit vote. In its first assessment of the impact of Brexit², the European Commission estimated the negative impact on eurozone growth at 0.25 points in 2017, based on a "mild" scenario. We think the impact on France would be roughly the same, considering that the country's economic performances are representative of the eurozone average. We will have to wait until November for the Commission's next official outlook, which in addition to the expected negative effects of Brexit, will also integrate all of the new measures taken in the 2017 draft budget bill. Although its full scope is not known yet, the fiscal impulse is expected to be negative and will thus curb growth.

The government bases its growth forecasts on the rebound in domestic growth engines (household consumption and corporate investment), which are deemed to have been more vigorous than expected since the beginning of the year. Indeed, the upturn in the purchasing power gains of gross disposable income (+2.2% year-on-year in Q2 2016, see chart 1) has been providing substantial support

¹ The opinion of the High Council of Public Finances would have been instructive, but it was not available yet at the time we went to press.

² "The Economic outlook after the UK Referendum: A First Assessment for the Euro Area and the EU", *European Economy Institutional Papers* n°032, July 2016.

Growth forecasts for France

Average annual growth rate

	2016	2017
BNP Paribas (August 2016)	1.3	1.0
Government (Finance bill Sept 2016)	1.5	1.5
IMF (July 2016)	1.5	1.2
OECD (Sept 2016)	1.3	1.3
European commission (May 2016)	1.3	1.7
Banque de France (June 2016)	1.4	1.5
INSEE (June 2016)	1.6	
Consensus (Sept 2016)	1.4	1.2
<i>highest estimate</i>	1.6	1.8
<i>lowest estimate</i>	1.2	0.8

Table

Source: BNP Paribas

to household consumption. Similarly, corporate investment has been benefiting from the significant rebound in profit margins (see chart 2), which comes on top of the positive effects of the over-amortization scheme.

Although we also see signs of a more solid, positive feedback loop³, we do not think the recovery has enough momentum to reach 1.5% growth in 2016 or 2017. Granted, non-farm payroll employment is picking up, but these improvements in the labour market are still mild and hampered by lacklustre GDP growth. In 2017, according to our scenario, employment will not be dynamic enough to offset the negative impact of the expected increase in inflation on the purchasing power of gross disposable income (GDI). The net slowdown in GDI will drag down household consumption (from an average annual rate of 1.5% in 2016 to 1% in 2017, compared to 1.5% in 2015), barely offset by a decline in the personal saving rate (which is expected to be rather small because of the also limited expected decline in the unemployment rate). The government is more optimistic and expects household consumption to remain quite buoyant in 2017 (+1.6%).

The momentum of corporate investment is also likely to be tempered by the rather lacklustre and uncertain outlook for demand. In 2016, we expect corporate investment to grow at an average annual rate of 3.7% (after 2.7% in 2015), which is close to the government's estimate of 3.8%. In 2017, in contrast, we expect it to weaken to +1.7%, unlike the government's forecast of +3.5%.

In fact, it will be hard to meet the government's growth forecast even this year. Q1 was certainly dynamic (+0.7% q/q), but it was followed by a sharp payback. As a result, GDP has declined slightly according to the detailed national accounts (-0.1% q/q instead of the previously published figure of no growth). To reach the government's forecast of

³ Ecoweek 16-31, "France – Labour market: a mild, but virtuous improvement", 16 September 2016.



an annual average growth rate of 1.5% in 2016, it would take quarterly growth rates of about 0.6% in Q3 and Q4. We do not believe the conditions have come together yet for growth to return to such high levels in the short term. In Q3, a technical rebound is basically assured since the temporary negative factors in Q2 will no longer be at work⁴. But the monthly economic data available so far still point to another decline. Granted we only have the figures for July, but they do not bode well for now for Q3 growth: indeed, the decline in household spending on goods and in production leaves them with a strongly negative carry-over (-1% q/q and -1.3% q/q, respectively).

The INSEE business confidence survey paints a more upbeat picture, particularly the September improvement (the composite index rose 1 point to 102). This bolsters our forecast of a moderate rebound in Q3 growth, to 0.3% q/q. In particular, the industry survey unexpectedly regained 2 points to 103. The breakdown of the balance of opinions also reinforces the positive headline result, particularly the sharp improvement in business leaders' assessments of their own production prospects. In terms of sub-sectors, however, the improvement only relied on the agro-food industry and transport equipment. In the retail trade sector, the business confidence index shed another point to 102, but it regained a point in services (to 102 as well). Lastly, in the construction sector, the indicator remained flat at 95 for the fifth consecutive month. Yet the balance of opinions on expectations continues to trend up, despite some volatility from one month to the next. The sector is therefore continuing to show signs of a recovery, which is good news for growth in general.

Yet, although the global trend of the INSEE business confidence surveys is not unfavourable, it is still not distinctly favourable either (see chart 3). The composite index's turnaround indicator remains mired in the area of economic uncertainty. All of this testifies the recovery's lack of momentum that we pointed out above.

Household consumption and purchasing power

Year-on-year change

Purchasing power gains, gross disposable income
Household consumption

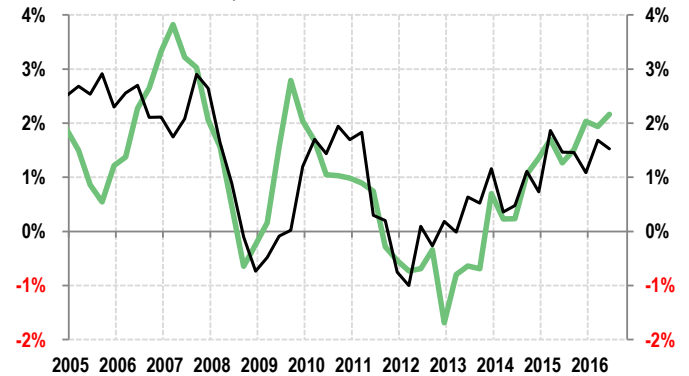


Chart 1

Source: INSEE

Corporate investment and profit margins

Corporate profit margins, % of gross value added (LHS)
Corporate investment (year-on-year, RHS)

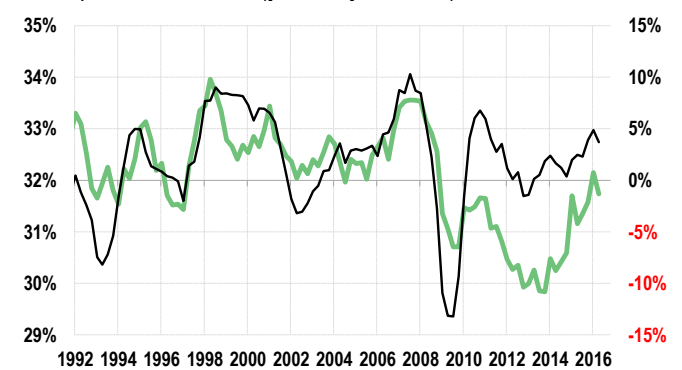


Chart 2

Source: INSEE

Business climate

Industry Retail trade Construction Services
Composite index

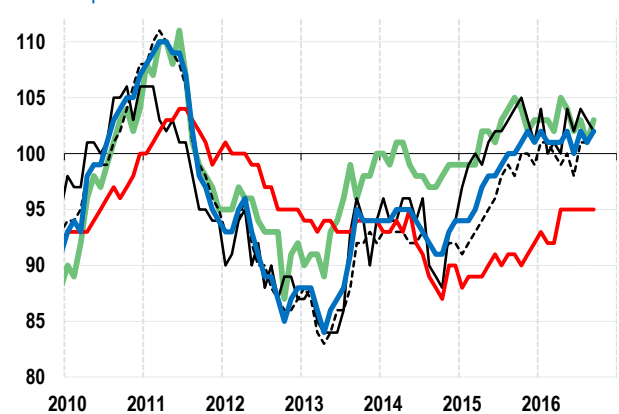


Chart 3

Source: INSEE

4 Ecoweek 16-29, "France - Growth hits another snag", 2 September 2016.