



# France

## Could growth be stronger in 2017 than in 2016?

- The business climate deteriorated slightly in January (-1 point) after December's strong showing (+3 points).
- After an expected robust Q4 2016 performance (+0.5% q/q), growth prospects in Q1 2017 are also looking upbeat for now (+0.4% q/q).
- The positive carry-over automatically raises our full-year 2017 forecast. According to our estimates, growth should accelerate slightly this year, to 1.3% from 1.1% in 2016.

In 2016, we estimate that French growth held at roughly the same pace as in 2015, at an average annual rate of just over 1%. The lack of acceleration is disappointing in the light of the favourable combination of low oil prices, interest rates and euro exchange rates. The situation can be explained in part by the troubles encountered in the grain industry, hard hit by poor weather conditions, and in aeronautics, due to supply problems and shipment delays. Once these problems have been ironed out, activity should benefit from a catching up effect.

Although full-year growth lacked a dynamic drive, 2016 seems to have ended on a positive note. According to the latest economic indicators, it looks like Q4 growth will be robust, buoyed by strong momentum, which also augurs well for Q1 2017 (we estimate growth at 0.5% and 0.4% q/q, respectively).

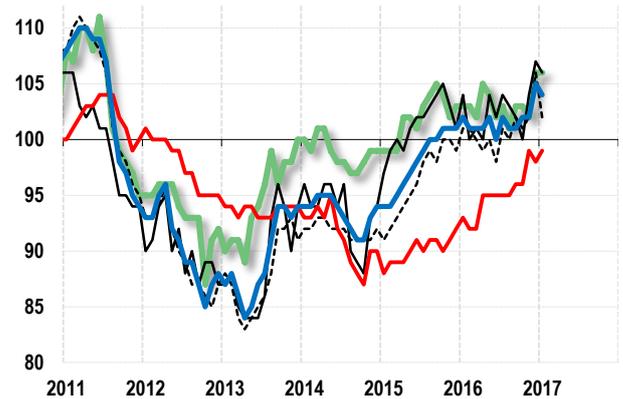
In December, the INSEE composite business confidence index improved significantly, gaining 3 points to 105. This is much higher than the long-term average benchmark of 100, and is consistent with quarterly growth of 0.3-0.4%. After such a strong performance, it is understandable that the index backtracked in January, and yet it shed only 1 point. In construction, the business climate rose to 99, regaining the point it lost in December, while industry preserved its strong gains and held at a high 106. In services and retailing, in contrast, December's big improvement was followed by a correction in January (-4 points to 102 and -1 point to 106, respectively), which dragged down the overall index.

The decline in the overall index masks several favourable factors, such as another improvement in the business leaders' assessments of their foreign order books and of personal and general production prospects. The quarterly economic survey on industry, also released on 25 January, contained some good news too: the production capacity utilisation rate has picked up to 83.7% -- higher than the long-run average of 82.9% -- which augurs well for investment; and export prospects have improved significantly.

Although the beginning of the year is looking rather upbeat, the year 2017 has no shortage of obstacles. The biggest is the current upturn in inflation in the wake of higher oil prices. This will erode household purchasing power gains and, in turn, consumer spending. The expected slowing of UK growth following the Brexit vote is also likely to curb exports. Numerous political uncertainties, at both the national

### Business confidence

— Industry — Retail trade --- Services — Construction — Composite index



Chart

Source: INSEE

level and in the rest of the world, also risk undermining growth. All of these factors could dampen corporate investment.

Under these conditions, how can we expect French growth to accelerate even slightly in 2017, to 1.3%? First, it is mechanically supported by a positive carry-over. Second, exports should benefit from an expected stronger growth in the United States. And if the euro were to weaken against the dollar, which seems justifiable, then that would serve as another support factor.

Lastly, French growth is becoming more solid thanks to signs of a healthier job market. Although the number of registered category A job seekers picked up in late 2016 (+0.7% m/m in December), this followed on a 3-month decline. The year-on-year decline was 3%. For the full year, the average decline was not as strong (-1%), but it was nonetheless the first one since 2008. Growth has also become more solid thanks to the upturn in the construction sector (12-month cumulative housing starts rose 11% in the year to November); the decline in the number of corporate bankruptcies (-6% in the year to November); and the increase in business creations (+6% in the year to December). Various government measures to reduce labour costs and boost supply also came into play.

French growth continues to be torn between contrasting forces. Until now, hopes for even a mild acceleration have led to disappointment, but there is a small chance that growth will be on target in 2017. There are numerous risks, but on the whole they seem to be well balanced between upside and downside risks.