

## FRANCE

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## LOW GROWTH IS EXPECTED TO CONTINUE

The energy crisis was less severe than initially feared during the autumn and winter. This prevented negative growth during Q4 2022 (+0.1% q/q) and provided grounds for relative optimism, as reflected in the rise in the INSEE business climate indicator from December to February. While the growth carry-over naturally led us to revise our growth forecast for 2023 upwards, growth is still low and reflects the sustained downturn in demand, particularly in household investment. In addition, while inflation is expected to decrease, it is still being buoyed by food prices, which, in turn, is adversely affecting household consumption.

Three factors should be considered when assessing the state of France's economy as a whole. Firstly, there was the pleasant surprise of an economic contraction being (narrowly) avoided during Q4 2022, as the risk of energy shortages affecting growth did not materialise. This could give a misleading view that the fundamentals of the French economy are stronger than they actually are. The second factor is other shocks, which are being felt more and more widely across the economy and are weakening its fundamentals. Despite expectations of no further inflation increases, price increases are coming one after another: our expected average inflation of 5.9% y/y for 2023 follows average inflation of 5.9% in 2022, which has hit household consumption hard (-1.2% q/q during Q4 2022). At the same time, rising interest rates are already affecting household investment, which decreased during the second half of 2022. This trend is expected to continue. Finally, the third factor is barriers to growth gradually lifting, which could help to prevent a recession. These include, in particular, semiconductor shortages easing and the Chinese economy reopening, which should ultimately provide a boost for the aeronautics, tourism and luxury sectors.

## 2022: MANY FACTORS CONTINUED TO SUPPORT GROWTH

2022 saw a number of post-Covid catch-up elements boosting growth, but these are expected to be less active in 2023. Services production bounced back and closed the gap with its pre-Covid trend, boosted by operations returning to normal in the tourism and accommodation and catering sectors. The labour market also erased the shock observed during the pandemic. As a result, employment also closed the gap with its pre-Covid trend, resulting in the unemployment rate dropping to nearly 7% for the first time since 2008. Companies were able to replenish their inventories, resulting in a 0.6 percentage point (pp) contribution of inventory changes to growth in 2022. Companies also increased their investment (contribution of 0.5 pp to growth), taking advantage of supply constraints starting to ease, particularly in the car industry, during the second half of the year.

Growth figures do not entirely reflect this dynamism within the economy, with the rising energy imports preventing shortages, despite electricity production falling by 20% y/y during the second half of the year. Higher gas inventories and additional electricity imports accounted for almost half of foreign trade's negative contribution of 0.8 pp to growth in 2022: growth would have hit 3.0% rather than 2.6% if it had not been for these unusual trends on the energy markets.

## 2023: CLEAR LOSS OF MOMENTUM, BUT A RECESSION SHOULD BE AVOIDED

One popular sentence is «when the construction industry is doing well, so does the economy», and the opposite is often true as well. However, the current economic climate in France has flipped the script on this adage. According to the French National Institute of Statistics and

## GROWTH &amp; INFLATION

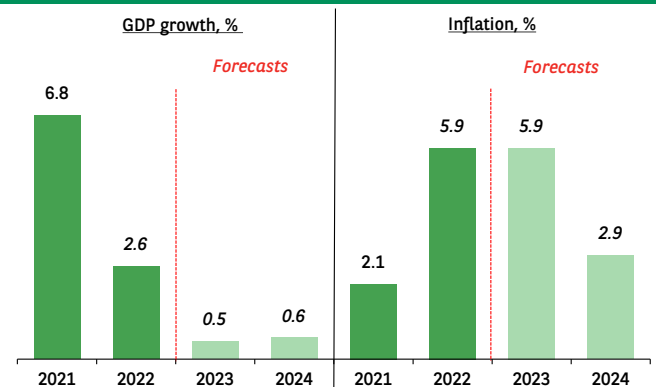


CHART 1

SOURCE: BNP PARIBAS GLOBAL MARKETS

Economic Studies (the INSEE), while 12% of households had stated in January 2022 (a record) that they were considering buying a home within the next two years, this figure fell to 8% in February 2023. This is still higher than the record low (5%) last hit in November 2014. Nevertheless, this is a significant drop and is reflected in a 1.2% contraction in household investment between the first and second half of 2022, and an anticipated fall of 2.5% in 2023. Interest rate hikes, which are expected to continue, are helping to drive this trend. However, it should be noted that other building sectors are still enjoying more positive dynamics, such as new non-housing construction and, in particular, building improvement and maintenance.

However, the downturn in new housing alone does not sum up the state of the French economy. Supply constraints are still a major factor in the economic picture. Even though falling demand should eventually ease these pressures, it is still relative as things stand. Admittedly, order books for the manufacturing industry fell from 7.3 months in February 2022 to 6 months one year later, based on our estimates (which is close to their average level between 1990 and the present day). However, the easing of supply constraints and the reopening of markets (China) should benefit the transport equipment sector, which is still operating at far below its pre-Covid levels.

Wage increases, which are higher in 2023 than in 2022, should also boost growth. In addition, the energy price caps should protect purchasing power and help to keep household consumption at around the level recorded during Q4 2022, and therefore prevent a further drop. This stabilising factor is likely to ultimately prevent a recession.

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