

FRANCE

YEAR ZERO

The figure zero should define French growth in 2023. The carryover should be zero, due to a second half-year 2022 in which the positive performance observed in the third quarter should be cancelled out by negative growth in the fourth quarter (with a key contribution of a further drop in household consumption). The quarterly growth momentum recorded in 2023 is not expected to provide any further support. A further contraction in GDP is expected in the first quarter, mainly due to a further acceleration in inflation and the probability of lower inventories in companies. The upturn expected to occur from the second quarter should be moderate, limited to offsetting the drop in the first quarter. There should be average growth of zero, which therefore includes a period of recession, at the turn of 2022–23, but an atypical recession. French corporates should continue to suffer from supply-side constraints, which in turn should support investment expenditure.

HIGH ACTIVITY IN Q3

In the third quarter, French growth benefited both from post-Covid catch-up effects and from the anticipation of production in the event of a difficult winter, which enabled it to continue to rise beyond what conditions at the time suggested (0.2% q/q in the second quarter, after already +0.5% q/q in the second quarter).

The first set of factors supported the production of services (from the second quarter), in particular those associated with households' tourism and leisure spending. This materialised in part as a substitute for other expenditure due to purchasing power constraints. Thanks to the reduction of supply difficulties, these catch-up phenomena also prompted an increase in automotive production, as well as of machinery and equipment, enabling a recovery in corporate investment (+3.1% q/q).

The second series of factors led to the anticipation of production (industry and building) and supplies (energy), increasing stocks. Thus, the contribution of stocks (0.3pp) was greater than GDP growth in the third quarter.

A FIRST ASSESSMENT OF GROWTH IN 2022

According to our forecasts, over the year as a whole, inventories constituted the main dynamic, with corporate investment coming second (chart 2¹). The inventory rebuilding estimated in 2022 fully compensates for the cumulative negative contribution in 2020 and 2021. Other items, in particular household consumption and public consumption, above all contributed through their carryover to GDP growth.

In other words, although household consumption was higher in 2022 than in 2021, it was mainly due to health restrictions which penalised the latter in spring 2021, while its own dynamic was negative in 2022. This aspect can be explained mainly by the impact on purchasing power suffered in the first half of 2022 and was not offset by the upturn in the latter from the third quarter onwards (household consumption was stable in the third quarter). Another factor explaining the poor performance of consumption is the fact that some of it remained constrained by supply problems, particularly car purchase.

A TECHNICAL RECESSION

We expect a recession, i.e. two consecutive quarters of negative growth, in the fourth quarter of 2022 and in the first quarter of 2023. This anticipation is firstly based on the gradual diffusion of a new inflationary impact (chart 3). The latter comes from two causes, one associated with the drought of the summer of 2022 and its consequences for food inflation, the other corresponding to a further rise in energy prices.

¹ The carryover's calculation uses the figures observed in Q4 2021 for each demand item and keep it constant throughout the whole 2022 year.

GROWTH & INFLATION

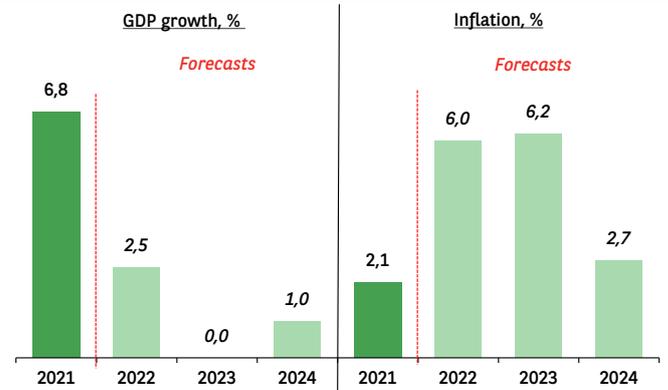


CHART 1

SOURCE: BNP PARIBAS GLOBAL MARKETS

CONTRIBUTIONS TO 2022 GROWTH: CARRYOVER AND DYNAMICS RELATIVE CONTRIBUTIONS

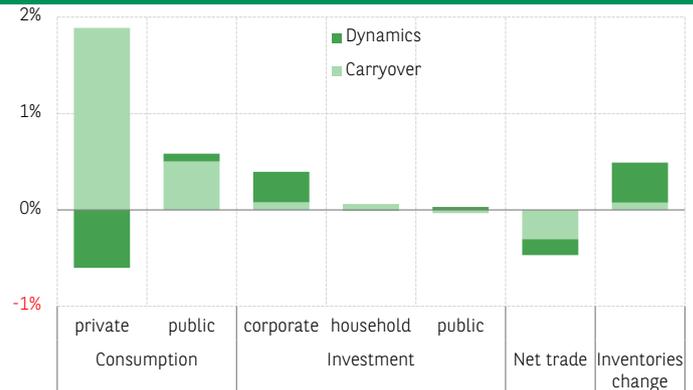


CHART 2

SOURCE: BNP PARIBAS

The rise in food prices is very substantial (+12.2% in November y/y) and is reflected in the development of household consumption in goods in October, which was very negative (-2.8% m/m). Thus, per capita food consumption is at its lowest since 1988. The drop in energy consumption also contributed to the sharp drop in consumption in October and



appears to have continued thereafter, according to RTE data. These two elements should bring the French economy closer to a contraction in GDP in the fourth quarter.

The rise in regulated gas and oil prices by 15% at the beginning of 2023, as well as the withdrawal of the fuel discount, should lead to a further increase in energy inflation. At the same time, the rise in the wholesale price of electricity suffered by companies is leading prices of manufactured goods and services to rise, in particular those adjusted on a calendar basis on January 1st (especially transport services) or at the end of the annual negotiations on prices with large retailers.

All these elements should be combined to increase inflation above 7% at the beginning of 2023 (6.2% year-on-year in November 2022). The result will be declines in purchasing power (-0.6% q/q in the first quarter and -0.4% in the second quarter, after +1% q/q in the 3rd quarter according to our scenario) and household consumption (-0.4% q/q in the fourth quarter, then -0.2% q/q in the first quarter 2023), against a background of rising saving rate (17.2% on average in 2023, after 16.7% in 2022). The production that companies seemed to have anticipated in the third quarter could lead to a subsequent downward adjustment and therefore to continued negative growth in the first quarter. In fact, inventories appeared to be much higher than their average level in INSEE's latest economic surveys in industry. The indicator of the survey on past production deteriorated in November, but to a moderate extent. In fact, the precise timing of the setback largely depends on the speed with which stocks are being cleared, as well as the ability of companies to continue their production under good conditions for longer than expected (as autumn was milder than expected and so did not create any strain on energy supply): clement conditions that benefited to the construction sector. At the same time, the automotive sector saw its supply difficulties shrink, allowing production to fill some of its backlog on demand (which was reflected in high order intake and delivery times), particularly ahead of Black Friday. However, demand indicators (opportunity to make significant purchases in the household survey, order books in the business climate in industry) remained lower for several months than at the beginning of 2022. These elements reinforce the hypothesis of a downward adjustment of industrial production in the middle of winter.

A "PHONY RECESSION"

A recession is therefore our central scenario. Beyond this, 2023 should subsequently be penalised by significant growth restrictions, in particular due to the continued rise in interest rates, which is why we are anticipating zero growth over the year as a whole.

The recession we expect looks quite different to its precursors. The very clear predominance of supply difficulties in industry and the very low level of demand shows strong originality (figure 4), a trend already present in the French economy but which the recession recorded at the time of Covid increased. The upcoming recession is unlikely to fundamentally change the characteristics of the French economy: the various challenges, in particular the green transition or full employment, have in common that they highlight the need for supply side transformation. Thus, 2023 should remain, like its precursor, a year of particularly high corporate investment (with an investment ratio of 26%, close to the record level of 26.3% reached in the third quarter of 2022).

FRANCE: CONSUMER PRICES CUMULATIVE CHANGES

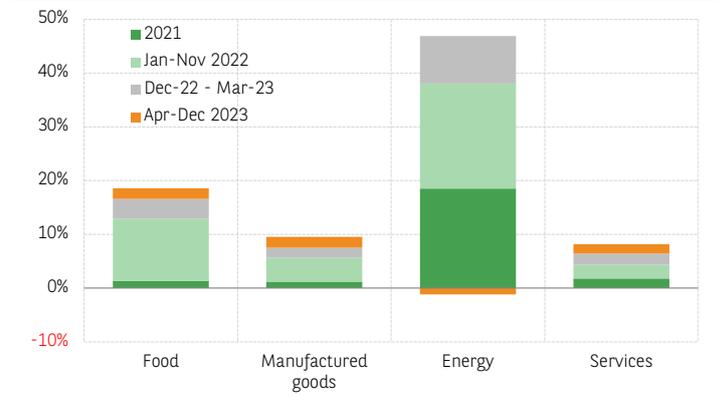


CHART 3 SOURCE: INSEE, BNP PARIBAS CALCULATIONS AND FORECASTS

FRANCE: MANUFACTURING SECTOR, DIFFICULTIES OF SUPPLY AND/OR DEMAND

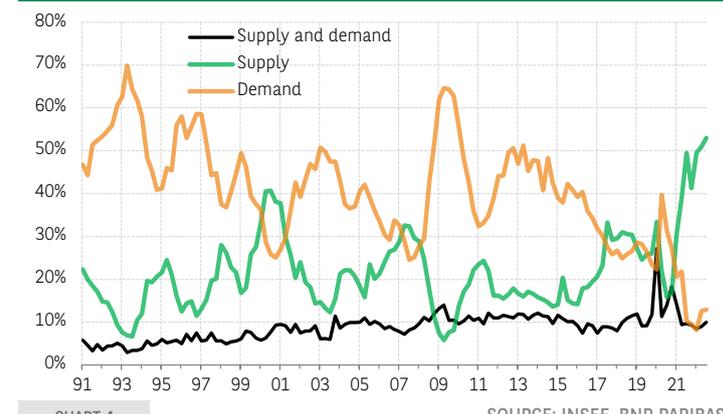


CHART 4 SOURCE: INSEE, BNP PARIBAS

Furthermore, the labour market will remain relatively tense. Employment should formally erode under the effect of the economic slowdown (predictable impact in construction and on temporary employment in particular) and the gradual weakening of the post-Covid job creation dynamic (in particular in catering and leisure). However, continued high recruitment pressures argue for job retention, even in the event of a recession. This aspect should be combined with the ongoing wage negotiations to favour faster wage growth in 2023 (5% compared to 3.4% in 2022). Faster wage growth may lengthen the disinflation process and should drive nominal GDP growth in 2023 (3.9%).

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