

France

Growth continues

The signs of stabilisation seen at the beginning of the year have been followed by improvements in confidence surveys. The upturn in consumer confidence has been the most marked and the most encouraging of these. The rather more mixed nature of the economic data available tempers these positive signals somewhat, and leads us to forecast stable growth in Q2, at 0.3% q/q, making this the sixth quarter in a row to see growth at around this pace. This stability, which is remarkable in and of itself, is likely to continue over the coming quarters according to our forecasts. It is a good sign of the resistance of French growth to downward pressures. Under our scenario, this resistance demonstrates a degree of effectiveness in the measures taken to support consumers and businesses.

■ So far so good

Since the beginning of 2018, although it has been slow, French growth has set itself apart by its stability, a sign of its resistance to downward pressures. In Q1 2019, real GDP rose by 0.3% q/q, in line with expectations, which we believe is good news given the rather mixed economic indicators at the time. The upward revision of the Q4 2018 growth figure (from 0.3% to 0.4% q/q) provided more good news¹, while the stability in the domestic demand contribution (0.4 percentage points in Q1 2019 as in Q4 2018) is another positive factor. This stability was driven by a small but encouraging acceleration in consumer spending (up 0.4% from 0.3% q/q) offset by a similarly small deceleration in total investment (up 0.5% from 0.6% q/q) and public consumption (up 0.2% from 0.4% q/q). From one quarter to the next there was a mirroring of the effects of the changes in inventory contribution (negative then positive to the tune of -0.2 of a point and then +0.3 of a point) and net exports contribution (positive then negative at +0.3 of a point and -0.3 of a point respectively). Payrolls gains also remained on a positive trend, rising 0.4% q/q in Q1 2019.

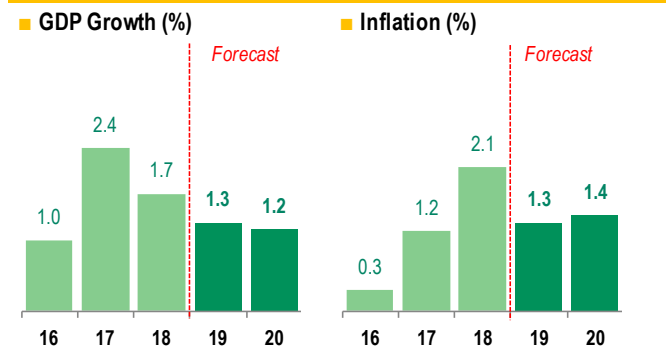
Growth prospects for Q2 are a little less mixed than in previous quarters thanks to the uptrend in confidence surveys. Their improvement remains limited and fragile. The return from slowdown to expansion territory of INSEE's new 'business confidence clock' is described as hesitant². These developments are nonetheless positive, particularly when contrasted with the less encouraging signals on the German economy. The difficulties of France's main trading partner will not be without their consequences for the French economy, but for the time being this latter is coming out quite well.

Since the trough at the start of this year, France's composite PMI has gained 5 points (having lost 11 points in 2018), taking it to 52.7 points in June. This increase has been based on improving conditions in services (up 5 points to 52.9 in June) and to a lesser extent in manufacturing (up 2 points to 51.7 in June). The fact that the German composite PMI figure is similar (at 52.6) hides a significant, unusual and unsettling divergence between the manufacturing number (45) and that in services (55.8). As far as national surveys of business confidence are concerned, the INSEE composite index is rising whilst the German Ifo is declining (the former is up 4 points since the start of the year; the latter down 2

¹ The growth figure for 2018 was also increased from 1.5% to 1.7% (swda).

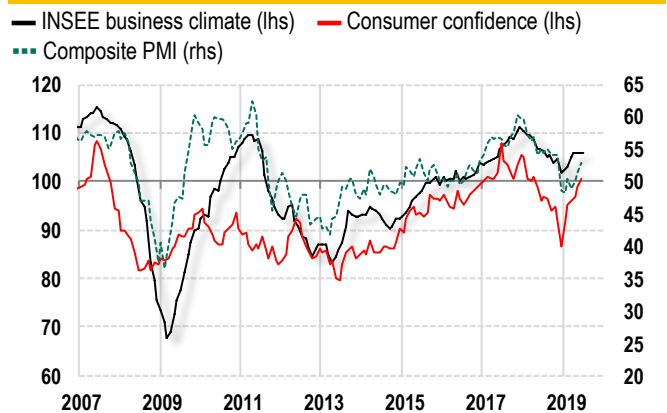
² See "France: new INSEE business confidence clock", Charts of the Week, 26 June 2019

1- Growth and inflation



Source: National statistics, BNP Paribas

2- Confidence surveys



Source: INSEE, Markit, BNP Paribas

points). At 106, the INSEE index is significantly higher than the reference average of 100. This level is consistent with a quarterly growth rate of 0.5% to 0.6%. The most encouraging improvement has come in consumer confidence: in June, after six consecutive monthly increases, total gains of 14 points took it to 101, finally moving it (just) above its reference average of 100 for the first time since April 2018.

The positive signal from surveys has been tempered by the more mixed picture from the activity data available for April and May. However, our nowcast model suggests that whether on the basis of soft data or hard data, Q2 growth is estimated at just 0.3% q/q. This fits with our forecast as well as the INSEE one while the Bank of



France has just revised down its estimate, from 0.3% to 0.2% q/q. In our scenario, growth is expected to remain stable at this rate of 0.3% q/q for the sixth quarter in a row, whilst, to continue the comparison, German growth is expected to be zero or slightly negative (from 0.4% q/q in Q1).

■ Seizing the moment

This pattern is matched by prospects for the next few quarters, with French growth expected to maintain this rate of 0.3% q/q. Average annual growth is expected at 1.3% in 2019 and 1.2% in 2020. The cornerstone of this resilience remains the expected rebound in consumer spending, dragged along by rising purchasing power. On this point, from 2019 on, the exception is likely to become the rule and consumer spending's contribution should be again greater than total investment's one, after two years where the situation has been the other way round.

However, uncertainties remain over the rebound in consumer spending, and more specifically over its scale. The upturn in consumer confidence is a good sign, but for the time being, the hard data are not showing the same vigour. We continue to believe that this is only a matter of time. The reaction of consumer spending to increased purchasing power is not immediate. And the relatively high proportion of constrained expenditure, which has little or no sensitivity to changes in purchasing power in the short term, could further slow the reaction time and limit the reaction itself³. This said, by relaxing the constraint on revenue, the additional purchasing power is likely to have a significant stimulus effect on compressible, discretionary spending.

Time is moving on, however: the rebound in consumer spending cannot take too much longer to feed through or the expected GDP growth will not materialise. The importance of the timing of this rebound refers more globally to the good timing of the measures to support households' purchasing power. We believe that these measures are well-timed and that, when combined with the ones to support businesses, their support to domestic demand should help offset, and perhaps more than compensate for, the slowdown in external demand. Even so, there is still a risk that this support will prove ill-timed, and that its benefits will pass unnoticed – all the more so if the external headwinds prove stronger than expected, making it harder to demonstrate the effectiveness of the economic policy adopted.

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³ See M. Beatriz, T. Laboureau and S. Billot, "How are purchasing power and household consumption linked in France in 2019? An analysis of the different categories of households and forms of consumption", INSEE Special Analysis, June 2019

3- Reform of the unemployment benefits system

At the end of 2018, the guidelines sent by the government to social partners to renegotiate unemployment benefit sought to rework the aggregation rules for benefits and earned income, set an approach to reduce the use of short-term contracts and aimed to produce between EUR 1 billion and EUR 1.3 billion in annual savings between 2019 and 2021. When no agreement was reached, the government took back over and presented its version of the reform on 18 June 2019. It includes 12 incentive and support measures, whose main goal is to fight job insecurity. Savings over the period are estimated at EUR 3.7 billion. Of this total, EUR 350 million are allocated to strengthening resources at the Pôle Emploi employment service. The Prime Minister has also set a target of reducing the number of jobseekers by between 150,000 and 200,000 by 2021 thanks to these reforms. We set out the measures below in the order in which they will be introduced:

1 November 2019

(1) opening unemployment benefits to people who have resigned (providing that they have at least more than 5 years' service and have a professional project) and to **(2)** self-employed people in bankruptcy proceedings (minimum revenue of EUR 10,000 per year in the two years prior to the bankruptcy).

(3) new rules on eligibility and rebuilding of rights (EUR 2.8 billion in savings). At present a claimant needs to have worked for at least 4 of the previous 28 months; this will rise to 6 of the previous 24. As far as rebuilding rights is concerned, it will now be necessary to work for 6 months rather than just 1 to create new benefit rights. The effect of these tougher terms on precariousness is debated (either an increase or a decrease appears possible). Its counter-cyclical nature should also be considered, as it (more or less) restores the rule that was in force prior to the relaxation of 2009 (6 months worked in the previous 22).

(4) tapering of benefits: -30% from the 7th month for people with previous gross monthly salaries over EUR 4,500 per month with a net minimum benefit of EUR 2,261, except employees aged 57 or over (EUR 210 million in savings). This measure aims to reduce the duration of unemployment of this specific category of workers. But as they are net contributors to the system, the measure is seen as unfair and unjustified.

1 January 2020

(5) discounts and penalties on unemployment insurance contributions for companies with more than 11 employees in the seven sectors that are the biggest users of short-term contracts: food, drink and tobacco product manufacturers; specialist scientific and technical activities; hotels and restaurants; water production and distribution; transport and warehousing; manufacturing of rubber and plastic products; woodworking, paper making and printing. If a company has a contract termination rate (giving rise to registration at Pôle Emploi) higher (or lower) than the sector average, it will pay a penalty (or get a bonus). The contribution will vary between 3% and 5% (the current level is 4.05%) and will apply to the whole payroll. The discounts and penalties will balance each other in each sector. Calculation of termination rates will be based on rolling 3-year data. Companies will start to pay penalties or receive bonuses from January 2021 on the basis of 2020 data. The restriction to seven sectors has been questioned, but after evaluation the system could be extended to the whole economy. A fixed rate tax of EUR 10 will also be applied to customary fixed-term contracts.

(6) to **(11)** a new range of support and services for new claimants, companies and workers in insecure positions.

1 April 2020

(12) new method for calculation of benefits (EUR 700 million in savings) on the basis of monthly income rather than daily pay for days worked. Benefits cannot be less than 65% of previous net monthly income, nor more than this income, as is possible in some cases at present. This should help discourage the splitting of contracts.

Source: French government, press, BNP Paribas

