FRANCE

THE GRASSHOPPER AND THE ANT

The French economy is characterised by a dichotomy. Household spending – consumption and investment – has decreased in volume (-1.4% and -6.6% in Q2 compared to Q4 2021), while corporate investment has increased (+6.7% between Q4 2021 and Q2 2023). This factor, combined with the reduction in constraints on the production of transport equipment, has enabled high growth in Q2 (0.5% q/q). While these factors should continue to support economic activity in the medium term, growth may be constrained in the coming quarters by the fall in demand against the background of high household savings.

French growth was surprisingly up in Q2 2023, reaching 0.5% q/q. This performance comes from exports in the transport equipment sector (automotive, aviation and naval) and corporate investment (+0.5% q/q in Q2). Conversely, household consumption and investment contracted, affected by still-high (albeit falling) inflation and persistently high interest rates. This divergence, observed since the beginning of 2022, between a part of demand that is holding up and another that is shrinking, has weakened growth without, however, making it disappear. This has also enabled job creation to continue, although at a slower pace (21,000 net new jobs in Q2, compared with an average of almost 94,000 over the previous four quarters). The erosion of existing resilience factors should weigh on both GDP and employment growth in the second half of the year.

INCOME GROWING FASTER THAN GDP

The dynamics of sectors' accounts, whether households or non-financial companies, were rather positive in the first half of 2023.

Households suffered a fall in purchasing power in the first half of 2022, as income increases came afterwards: the EUR 20 billion from the law on purchasing power passed in July 2022 and pay rises (other than the minimum wage) in the second half of 2022 (first bonuses, then pay rises in early 2023). However, in Q2 2023, nominal gross disposable income (GDI) growth (+9.1% y/y) far outstripped that of the consumption deflator (+7% y/y). While net compensations have not yet made up all the lost ground (+6.6% y/y), it is income from capital (+20.8% y/y) and income from redistribution (benefits are growing faster than taxes) that are boosting purchasing power (+2% y/y).

Q2 2023 also saw the margin rate of non-financial companies rise to 33.2% (above their long-term average: 32%). This reflects the ability of these companies to pass on rising costs to selling prices.

Overall, income momentum improved and could have generated higher growth. But while companies are investing, household spending is still missing out.

COMPANIES CONTINUE TO INVEST

Corporate investment has been one of the most consistent supports for French growth in recent quarters. The investment rate reached 26.1% of gross value added over the past 12 months; in the 90s, it was only 20%. More than half of the difference can be explained by the increase in investment in information and communication: from 16% of the total investment in 2000 to 26% over the past twelve months. An acceleration in construction and machinery & equipment investments is the second driver (from 2016-17). This enabled the French economy to stabilize its industrial production capacity after the decline observed as from 2000.

At the beginning of 2023, companies' sound financial capacity also enabled them to self-finance part of their investment, limiting the impact of rising interest rates. However, the latter is weighing on demand (particularly that of households). Lower new orders should therefore ultimately lead to fewer investments.

GROWTH & INFLATION

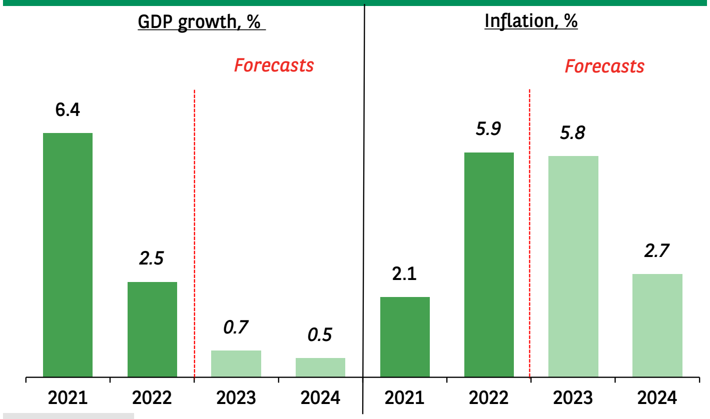

CHART 1 SOURCE: BNP PARIBAS GLOBAL MARKETS

PENT-UP DEMAND FROM HOUSEHOLDS? NOT RIGHT NOW

In Q2, household savings reached 18.8% of GDP, the highest level since 1979 (excluding the Covid-19 period). This high level of savings could be a sign of pent-up demand. However, since the end of the pandemic-related restrictions, the savings rate has never returned to its pre-Covid level.

For a household, savings have two purposes: investing in housing or building up financial savings. However, the former has been declining for several quarters: at 9.8% of GDI in Q2 2023 (4 points below its 1979 level). According to our estimates, financial savings will account for around 8% of GDI on average in 2023, a quite unprecedented level (excluding the Covid period): never before the proportion of the GDI spent by households was so low.

In the 70s, wage growth (and purchasing power) was high (indexation clauses), which encouraged households to take on debt (despite the very high interest rates at the time). In fact, the growth in their income quickly reduced the burden of monthly repayments on their GDI. However, we are not seeing anything like this at the moment. The dynamic of household purchasing power since the end of 2021 has been very different from that of the 1970s: the proportion of debt repayment in household budgets should not reduce as significantly as it did then.

In addition, the high level of interest rates is holding households back on their purchases of durable goods. This, along with the limited supply of electric vehicles and their price, means that saving is not a choice but the result of a lack of opportunities. Demand could free up later, but not in the short term: according to our forecasts, the downturn in household investment will not end before 2025, while household consumption should return to normal growth (of around 0.3% q/q per quarter) in 2024, but without any catch-up effect compared with 2022-23.

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