

# France

Nobody escapes the (downside) of convergence...  
...but you can try to delay it for as long as  
possible

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# Leading indicators signal strength, but ...

- Real GDP growth in France has increased sharply to 1.8% in 2017 from 1.1% in 2016, and the trend in industrial sector confidence signals scope for a further meaningful acceleration ahead
- While we do not want to underplay the positive effects of a strengthening recovery in the Eurozone and the US, there are a few factors that, in our view, signal a meaningful risk that French GDP performance will undershoot expectations
- **On the household sector front:** consumption has benefited from steadily falling interest rates and a recovering housing market, as well as a drop in the unemployment rate. However, with QE coming to an end and mortgage rates already very low, we suspect that consumption will no longer benefit from falling interest rates, while it may also suffer from the emerging signals of a growing appetite for savings. Also, in our view, French wages are likely to be compressed going forward – reflecting the powerful trend of convergence, which pushes up those with modest average wages, but pushes down those with wages above the European average (such as France). The increase in the minimum wage will soften this process, but cannot stop it, in our view
- Hiring appetite is high – but this does not necessarily mean higher wages: we could see a repricing of labour, as has been taking place in neighbouring countries
- **On the investment front:** capacity constraints are beginning to emerge, which is usually a good leading indicator for accelerating capex. However, much of the investment rebound is due to accumulating inventories – to the point that we doubt there will be more appetite in the near term – and, overall, in our view, the French business sector is suffering from lower profit growth (and a loss of pricing power relative to the historical performance), which could well delay a more robust investment cycle by a year, or even two

# Inflation: smoke and mirrors

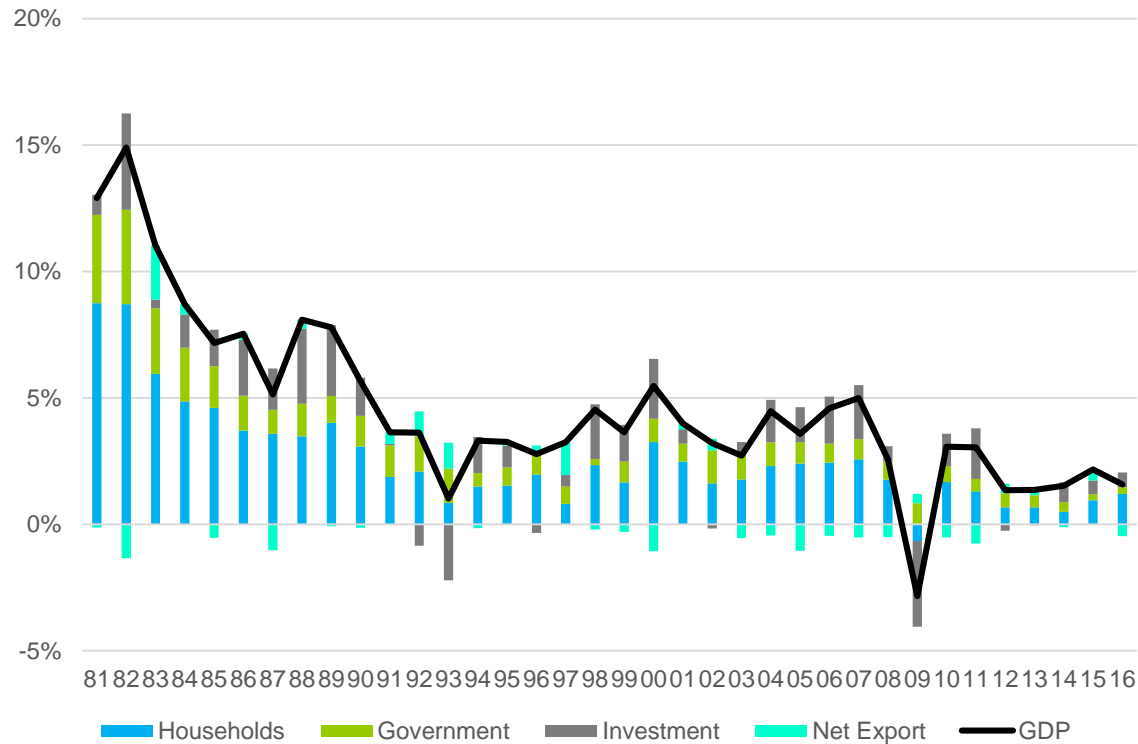
- Inflation picked up to 1.2% yoy in November 2017, up from 0.5% yoy a year earlier, but not too far from the 1.3% yoy recorded at the beginning of the year. Our inflation models signal a mild acceleration of average inflation to 1.3% in 2018E, from, 1% in 2017E, assuming that world oil prices stay, on average, around USD 60/bbl and the economy grows, on average, around 1.4% in the coming year, which would imply a steady mild widening of the positive output gap (which should, gradually, deliver higher pricing power and inflation overall)
- Business surveys suggest that inflationary pressures are indeed increasing, equivalent to what was seen last in 2006-07. Expected inflation, by consumers, has also been on an upward trend since hitting a low in 2015
- Although domestic factors are important for inflation, the speed of the recovery of CPI is also heavily influenced by commodities prices – which, for now, appear fairly mild in a historical perspective
- Equally important is the impact of the inflation, which is not evident in the CPI measure, but is felt by households nonetheless: these are, for example, housing-related costs, the higher depreciation rates of some items and services, and greater *de facto* per unit costs due to ancillary fees related to the purchase of an item/service. Inflation is also a bigger burden, if wage compensation is trending down rather than up
- Consumer surveys signal that households' willingness to save is moving up, as past savings have been trending down. A lower propensity to consume going forward may thus lead companies to partly revise down their pricing strategy over the course of the coming year

# Policy updates

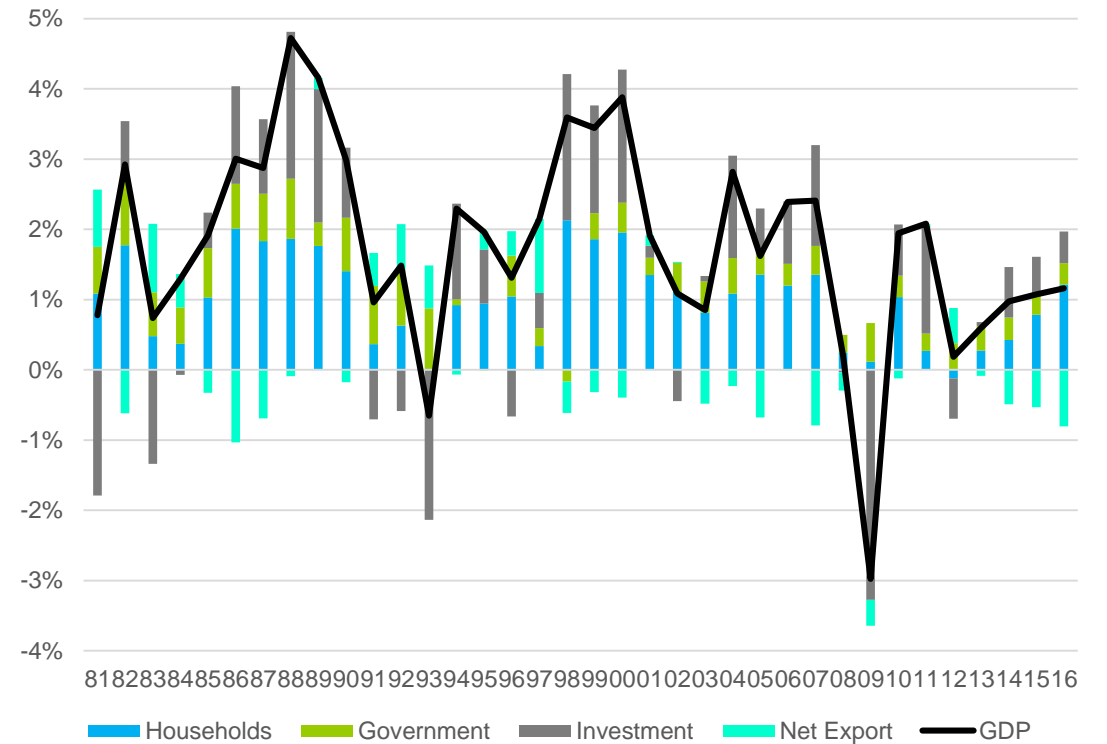
- President Emmanuel Macron's popularity has shown a strong rise in December, with 52% of respondents being satisfied with the President. This is an increase of 6ppts vs. November
- The gross monthly minimum wage in France (SMIC) is set to increase by 1.24% on 1 January, with the actual monthly increase being **EUR 18**. However, given the increase in the CSG and cuts in contributions for 2018, the net monthly increase will be around **EUR 20**. This increase will benefit about one in 10 French employees on the payroll
- The Robot Start SME programme, which was set up in 2013 to help SMEs employ robotic equipment, comes to an end in 2017, and it will not be renewed. It has been useful to around only 150 SMEs, less than half of what was targeted
- Since mid-November and throughout December, several regional and national banks have lowered the interest rates on credit, favouring the purchase of real estate. France has also witnessed a steep 15.5% yoy increase in sales volumes, the highest on record. (We will analyse the latest debt servicing costs in our next issue, when the data on regional prices have been updated.)

# Historical perspective on GDP drivers

## GDP contributions, current prices



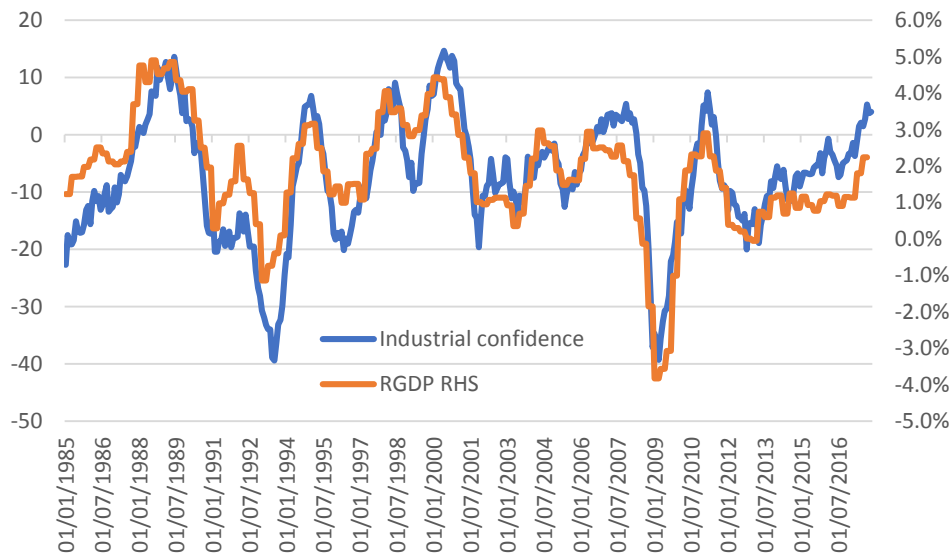
## GDP contributions, 2010 prices chain linked



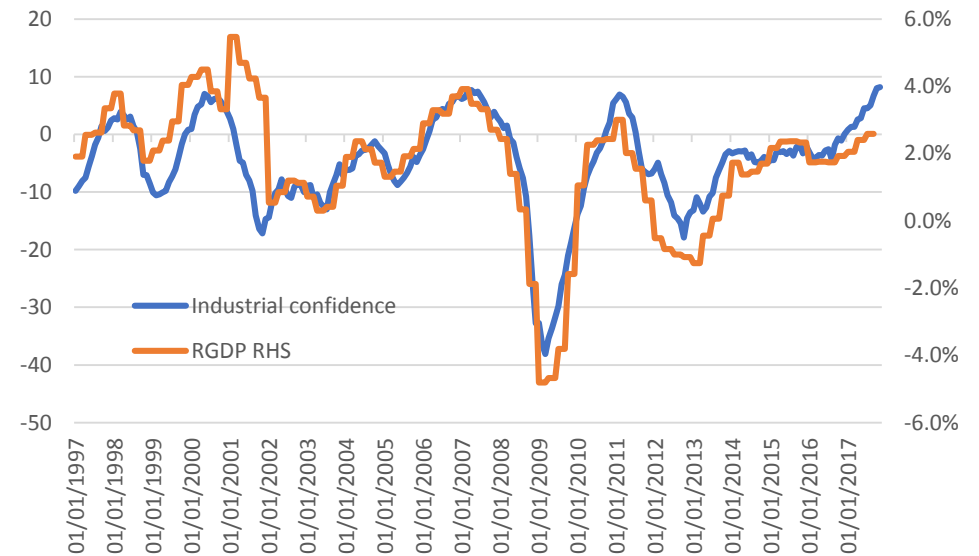
Source: CEIC, ADA Economics

# Surveys & real GDP performance historically

France: leading indicators suggest stronger GDP growth ahead



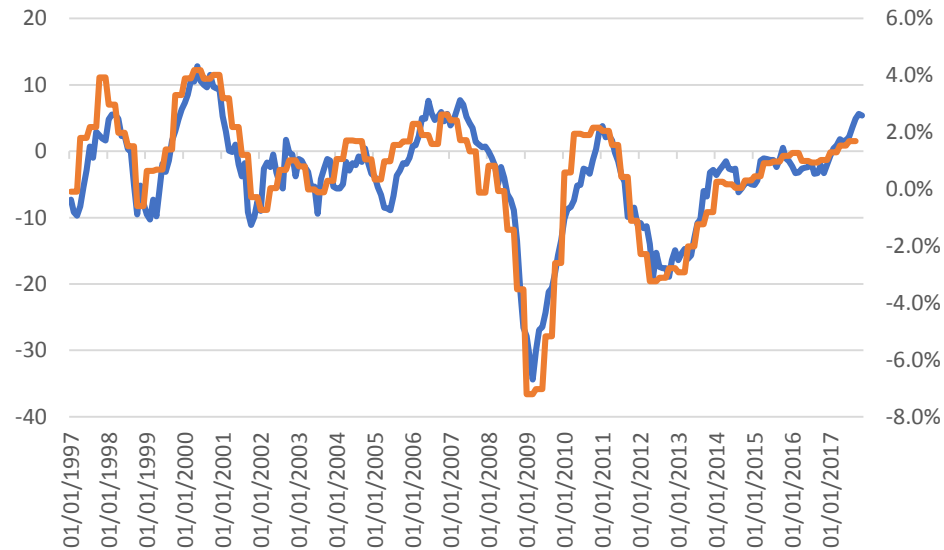
Eurozone: leading indicators point to a robust recovery



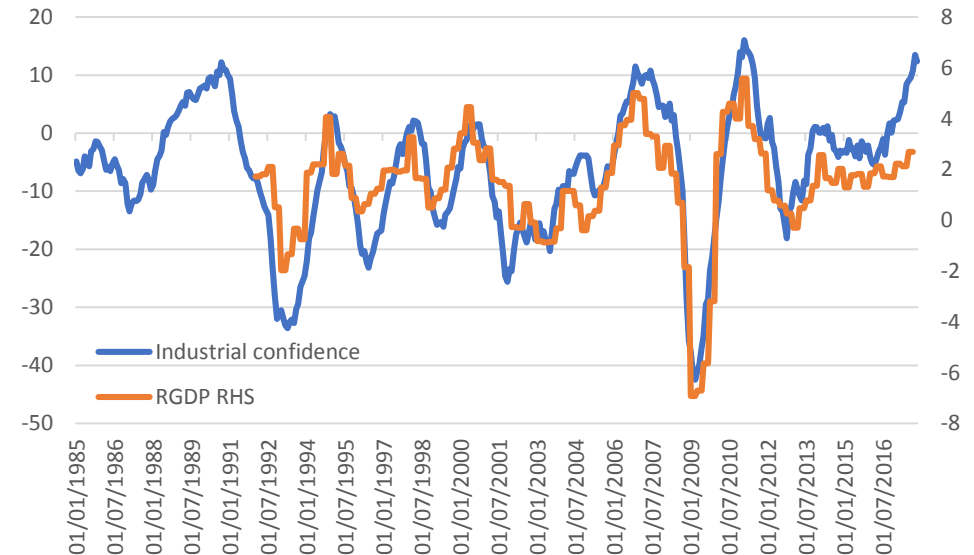
Source: Macrobond on EC survey data, ADA Economics

# Surveys & real GDP performance historically

Italy: industrial confidence signals real GDP growth pick up



Germany: industrial confidence high, but where is the GDP growth?

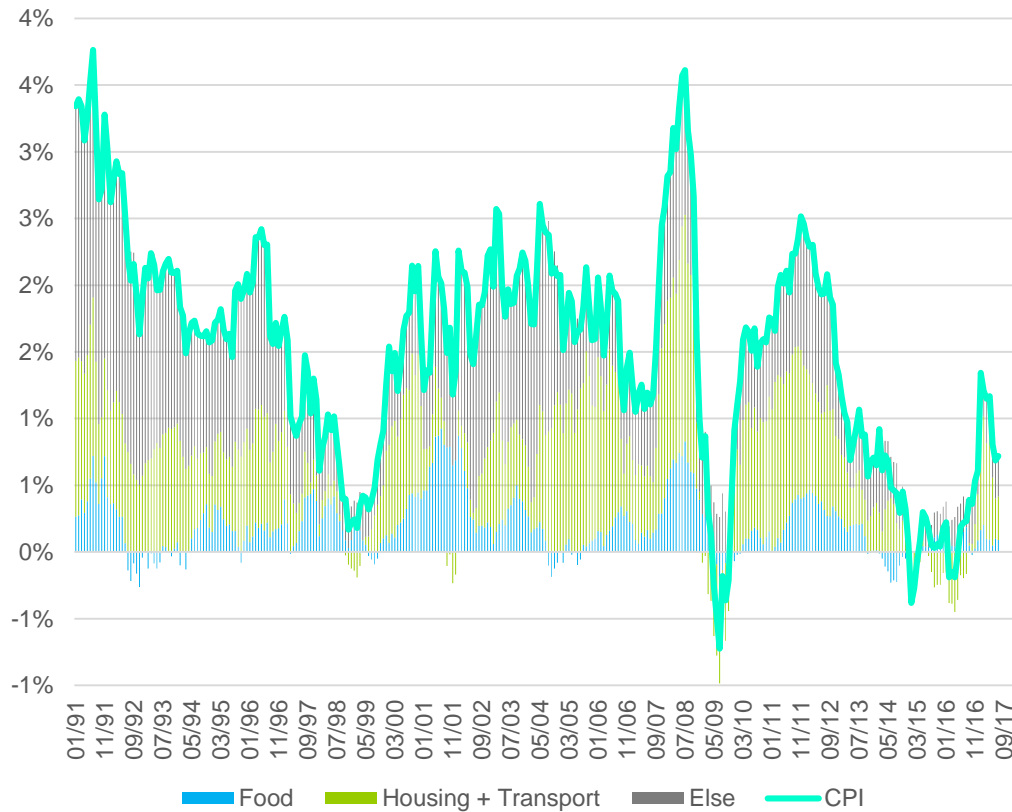


Source: Macrobond on EC survey data, ADA Economics

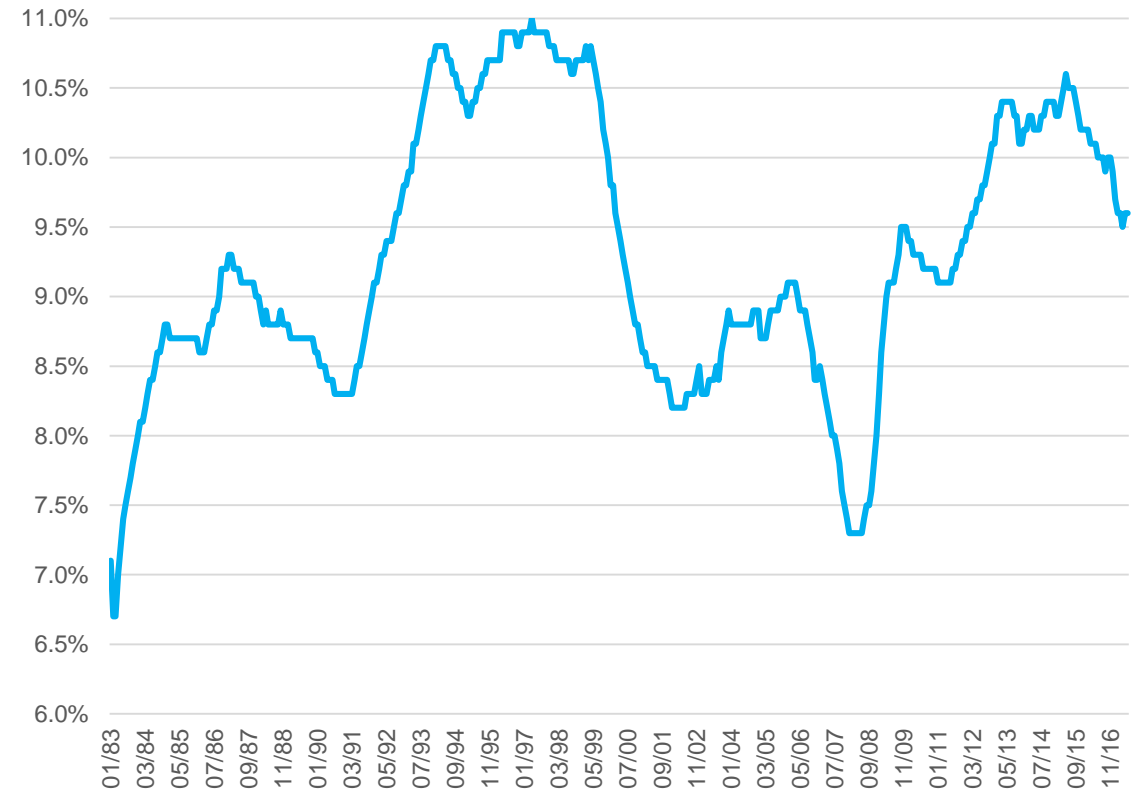


# Inflation and labour market

## Yoy CPI change



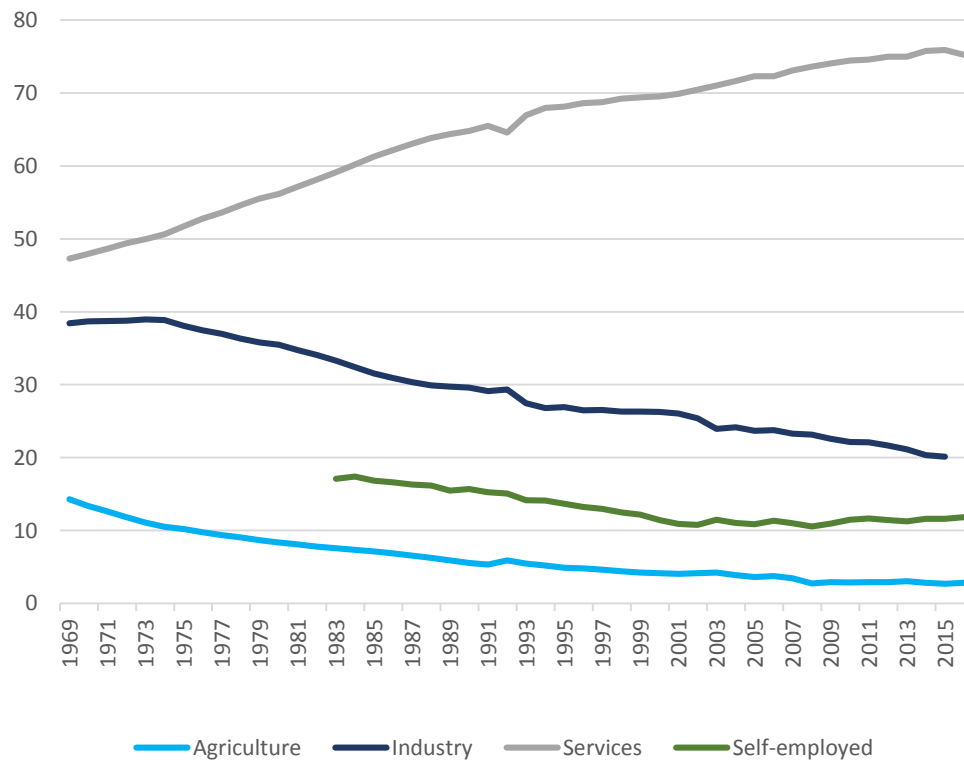
## Unemployment rate



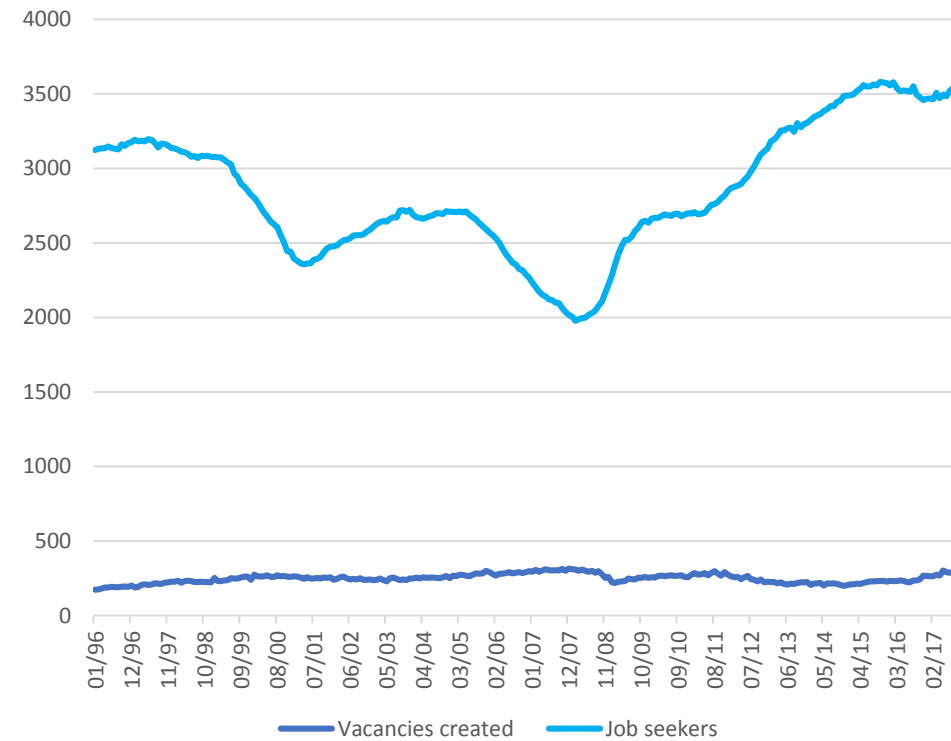
Source: CEIC, ADA Economics

# Labour market

% of total employment



Vacancies vs. job seekers (in 1,000 persons)



Source: CEIC, ADA Economics

# Employment forecasts

Despite a reduction in non-market sector employment due to less subsidised jobs:

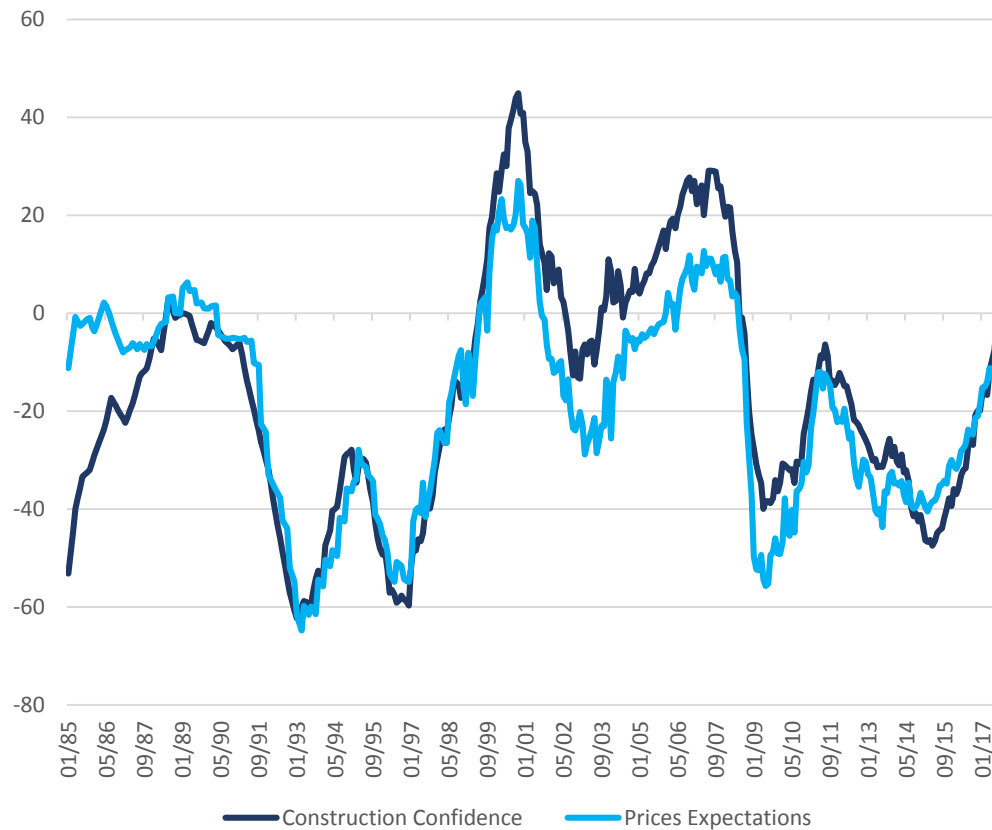
- **Non-market sector employment** should slow its progression in 2017E, and decline in 2018E (reduction of subsidised jobs)
- **Total employment** is expected to increase by 270,000 and 135,000 on average annually, respectively, in 2017E and 2018E

Variation in annual average (in 1,000s)

	2016	2017	2018E
<b>Private employment</b>	<b>170</b>	<b>235</b>	<b>160</b>
<b>Non-market sector employment</b>	<b>40</b>	<b>35</b>	<b>-45</b>
Farm employment	5	0	5
Self-employment	-5	0	15
<b>TOTAL</b>	<b>210</b>	<b>270</b>	<b>135</b>

# Construction sentiment

## Confidence and expectations



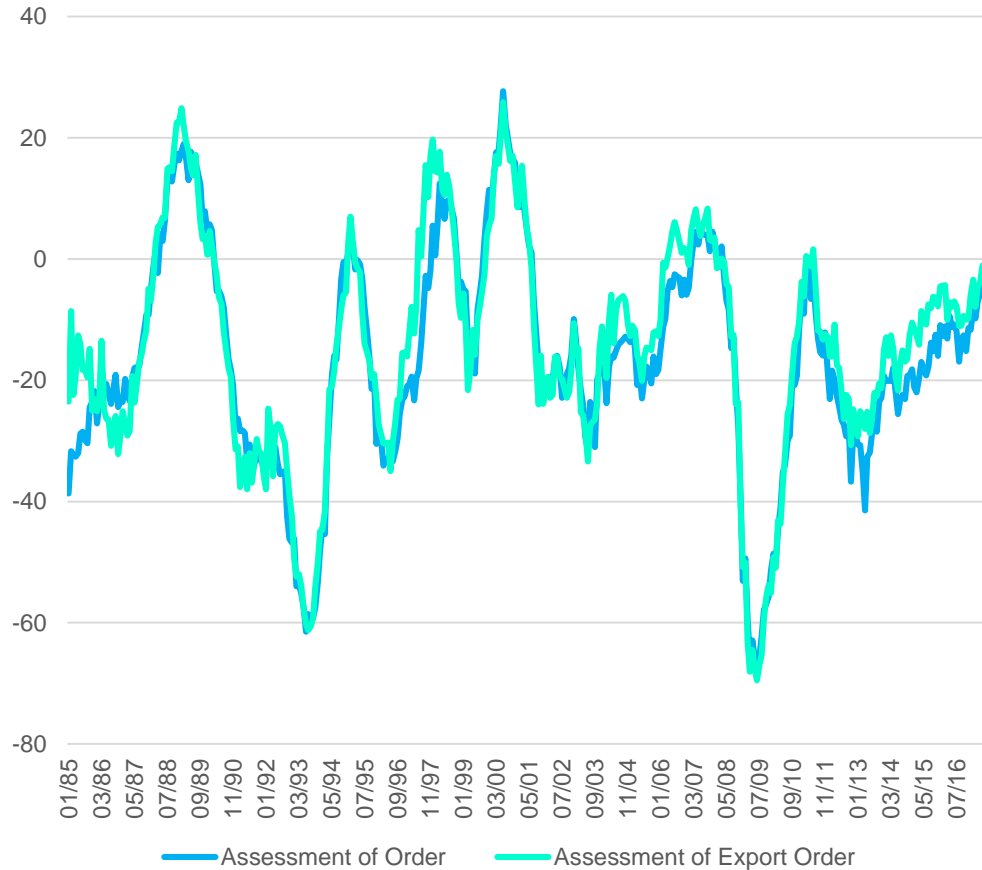
## Hiring appetite



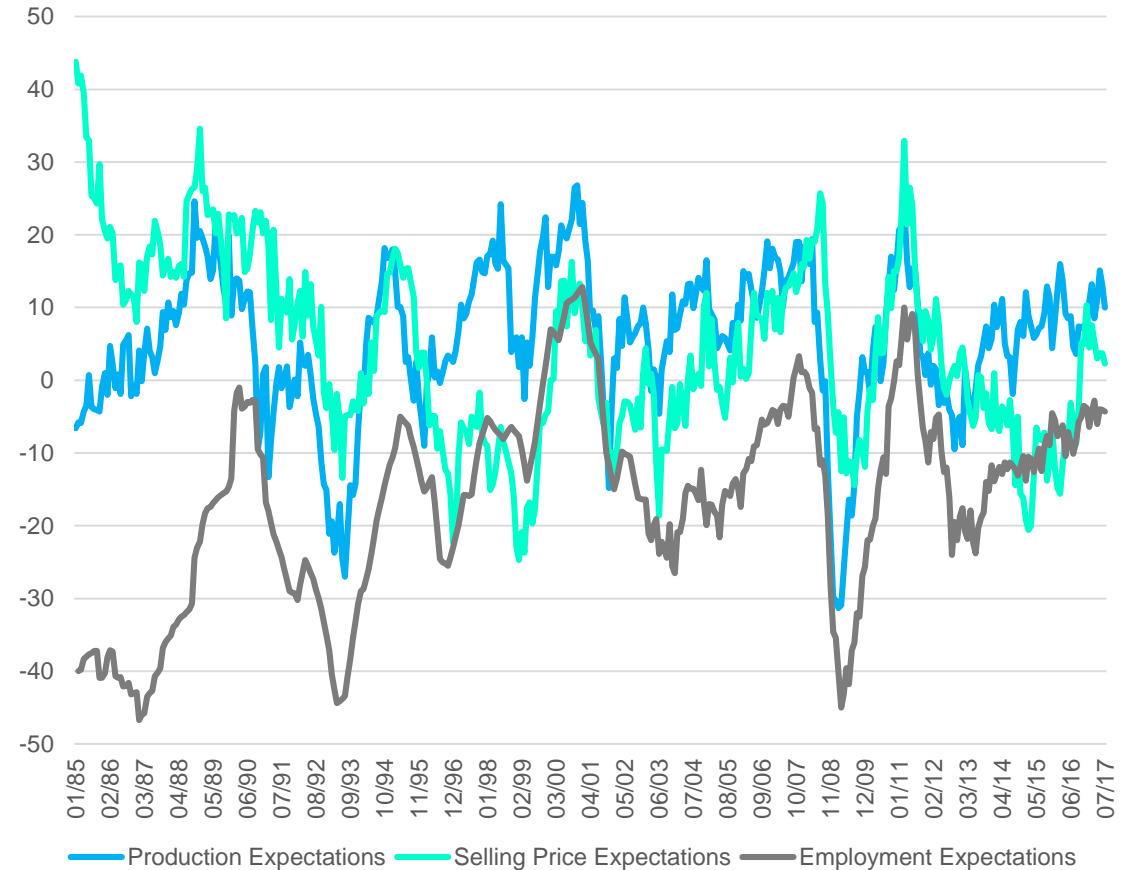
Source: CEIC, ADA Economics

# Industrial sentiment

## Assessments



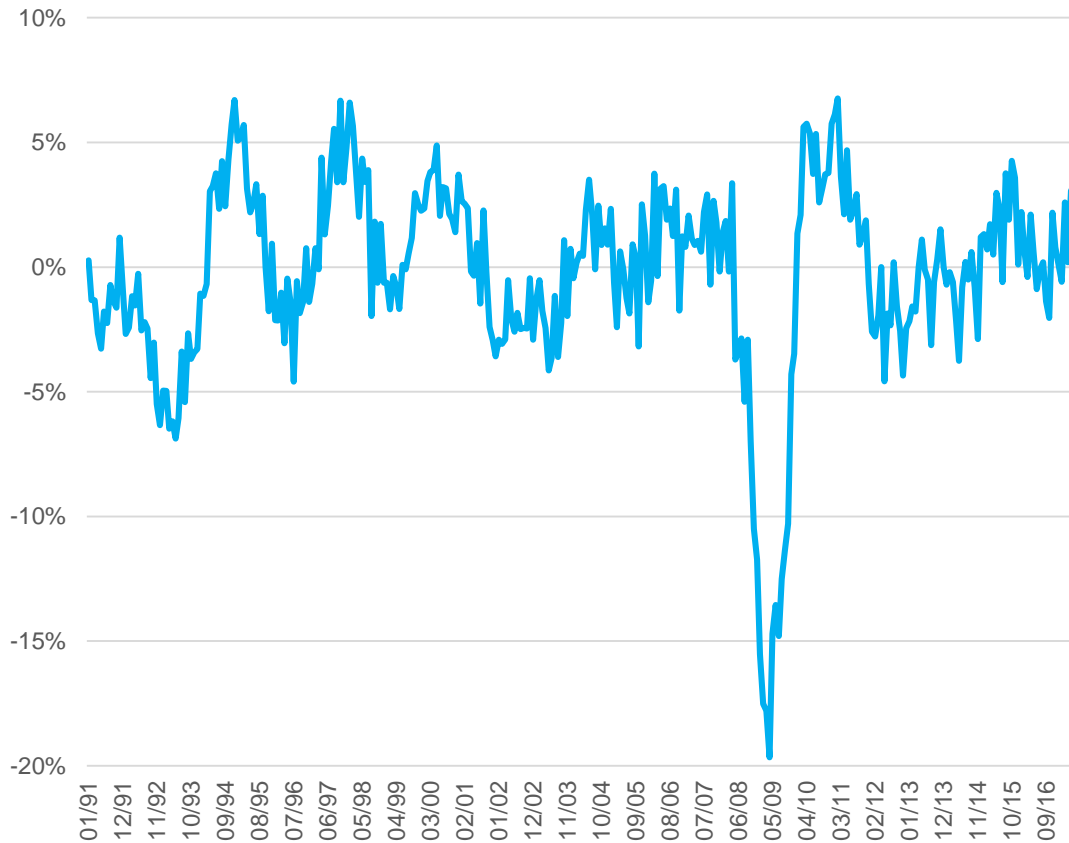
## Expectations



Source: CEIC, ADA Economics

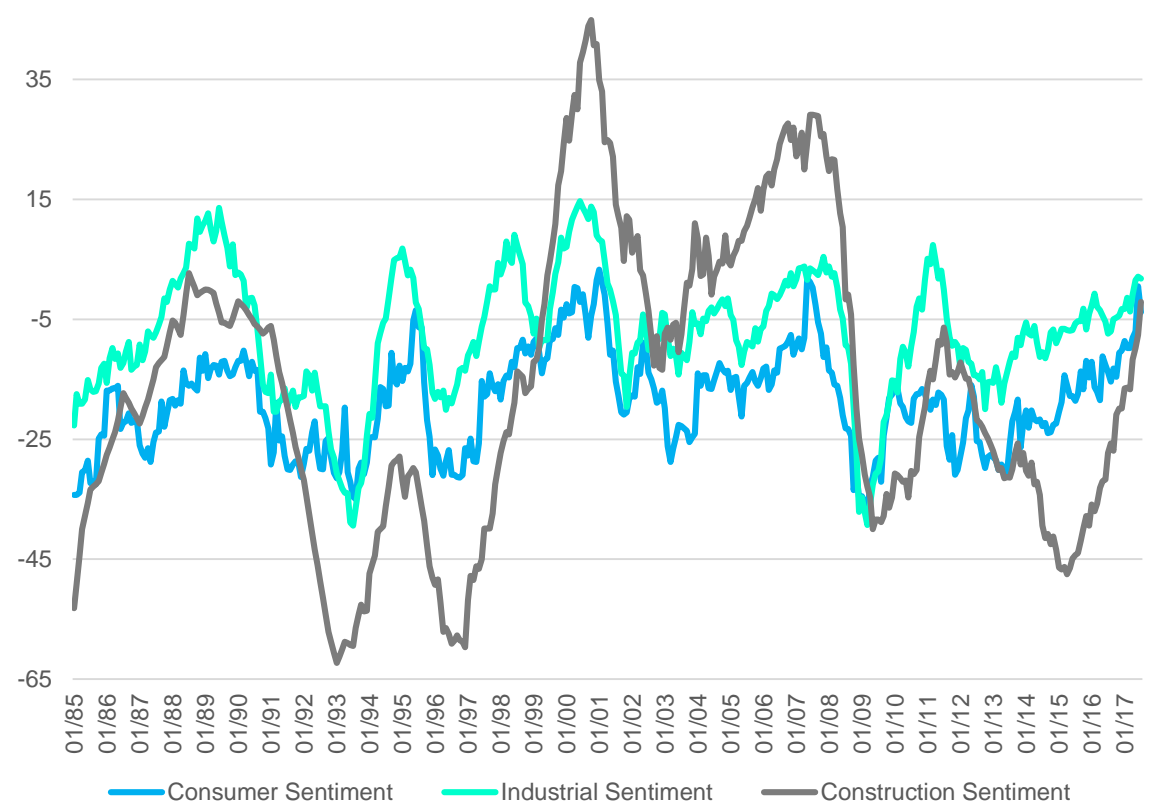
# Industrial Sector

## Yoy change industrial production



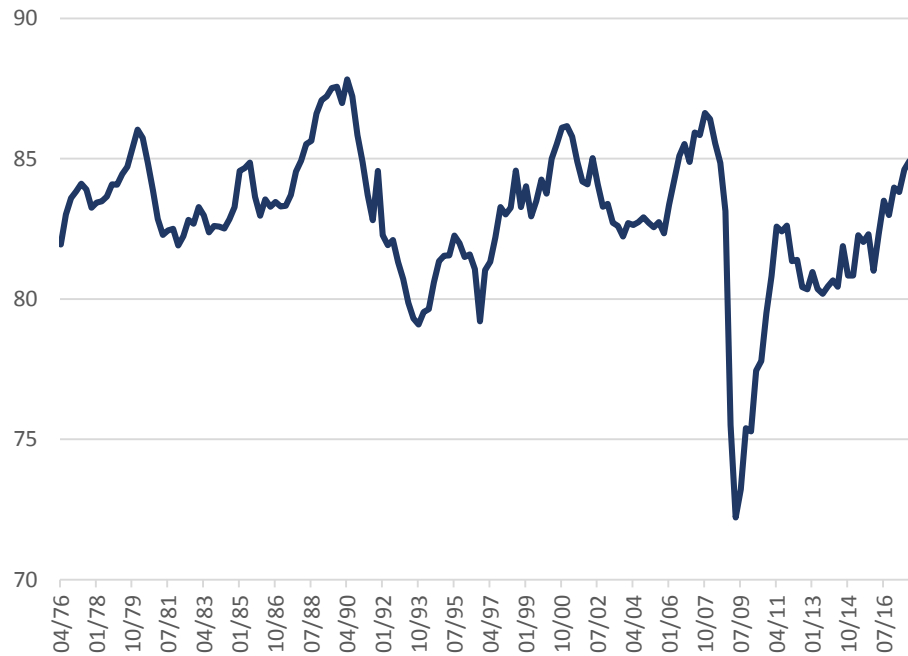
Source: CEIC, ADA Economics

## Confidence indicators

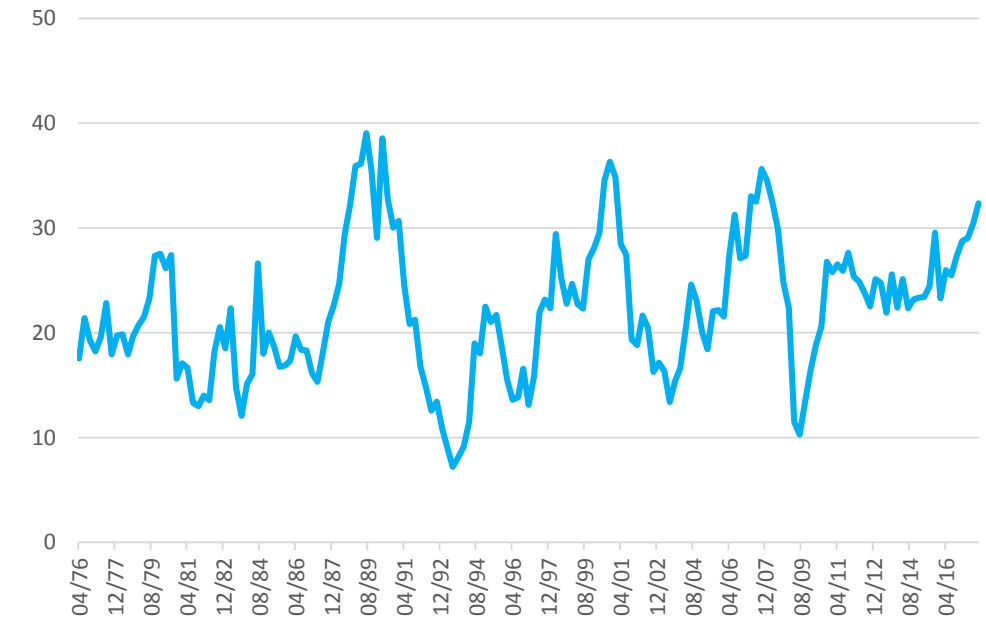


# Industrial sector

## Productive capacity utilisation rate %



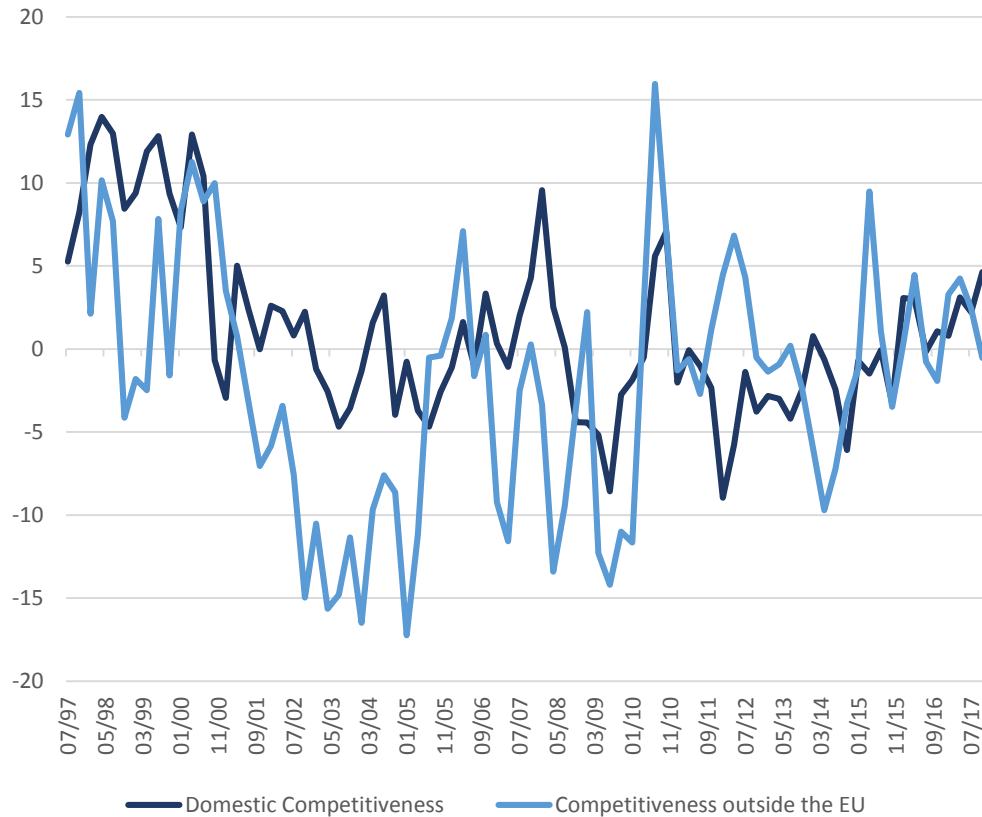
## Share of firms producing at full capacity %



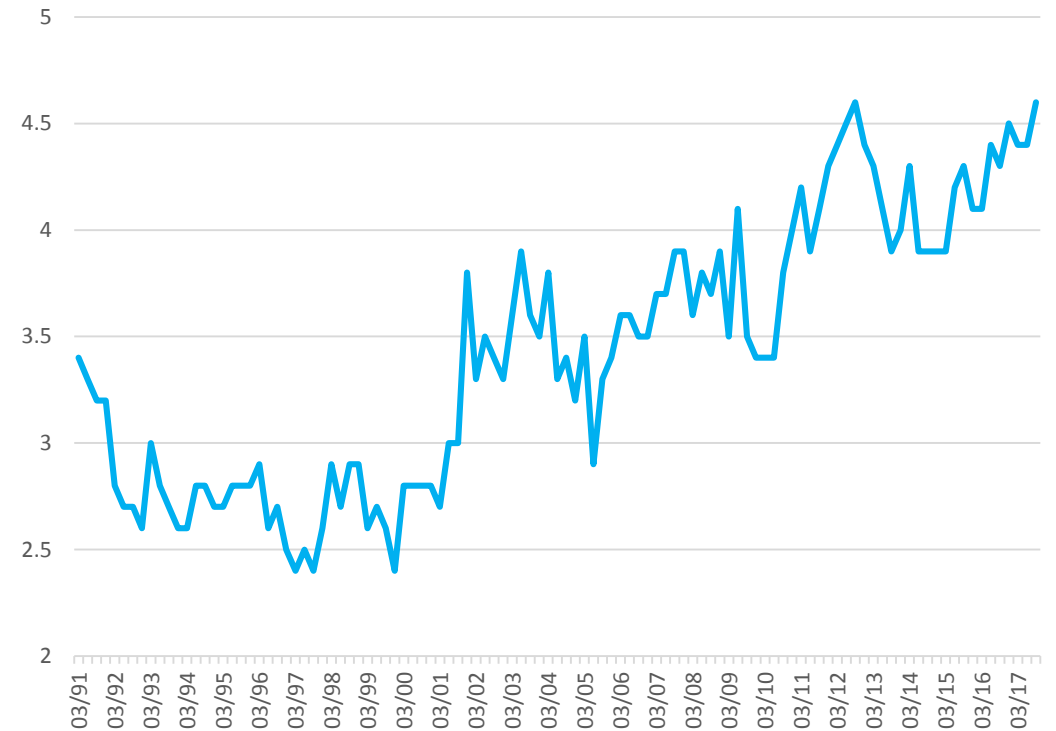
Source: CEIC, ADA Economics

# Industrial sector

## Competitiveness



## Duration of current order

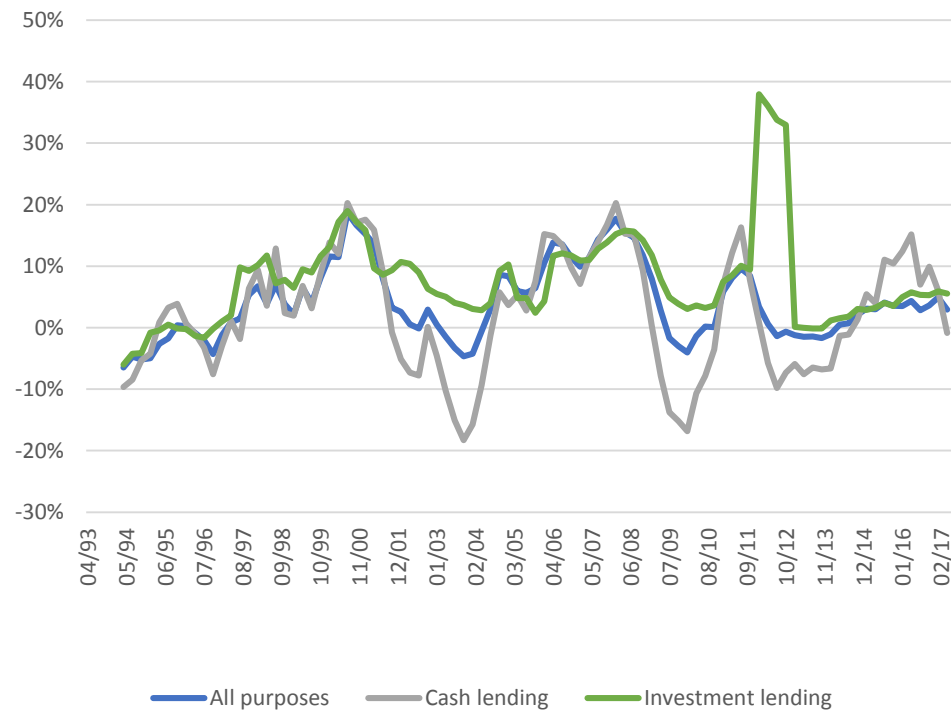


Source: CEIC, ADA Economics

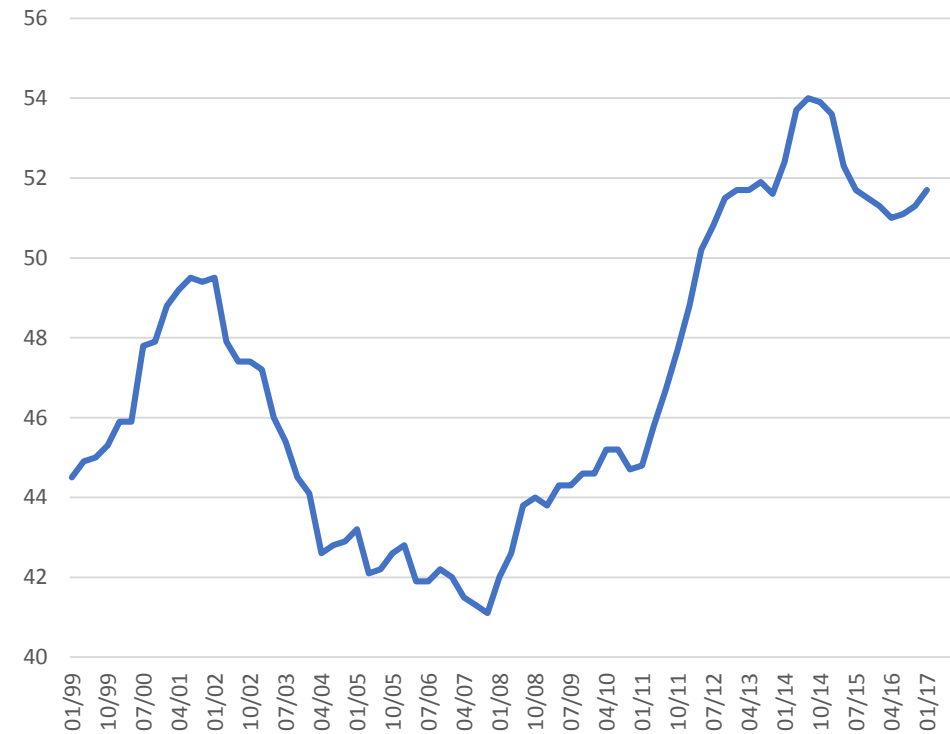


# Loans to NFCs

Loans to NFCs, yoy



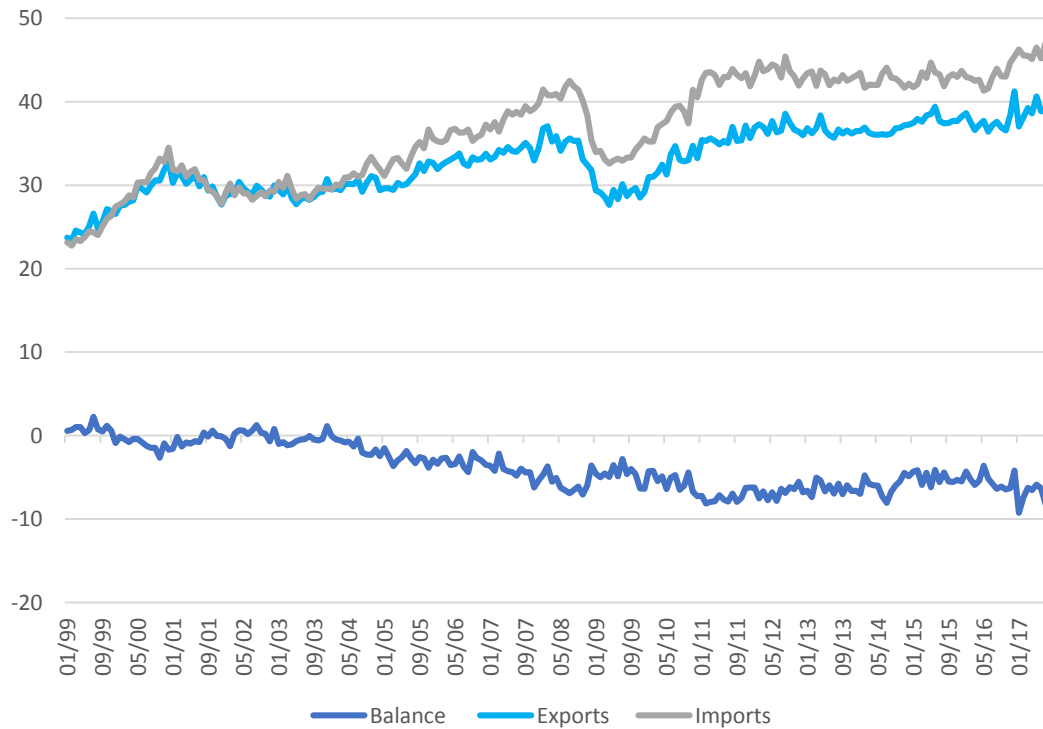
Debt service ratios, as a share of income



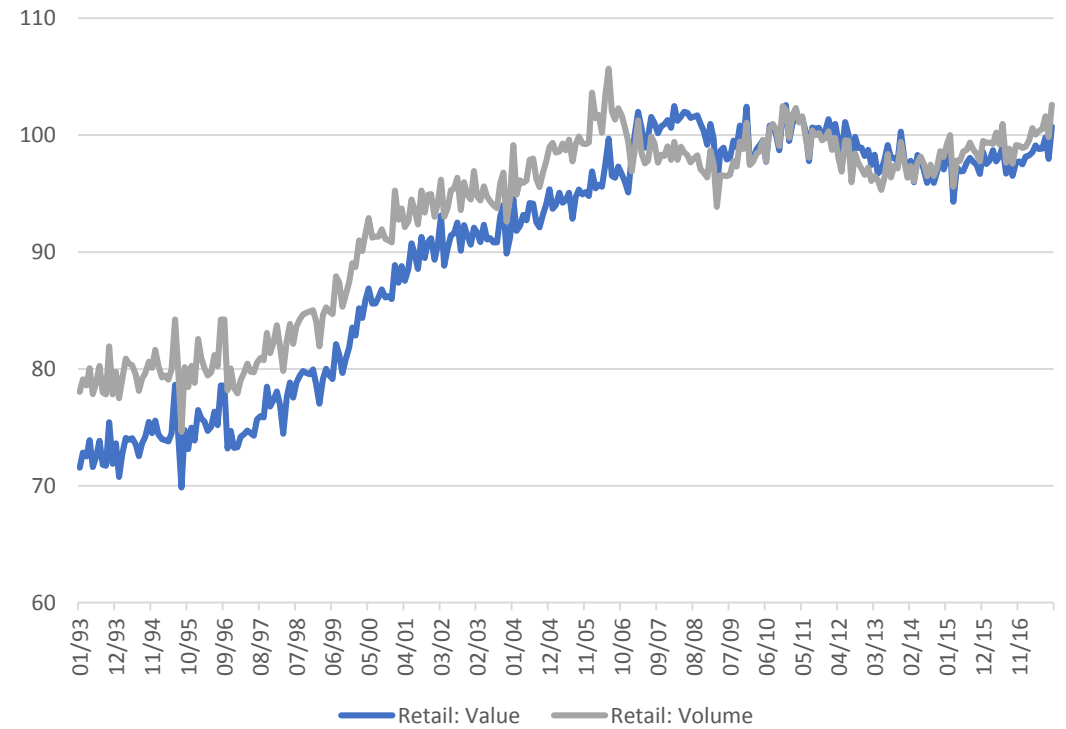
Source: CEIC, ADA Economics

# Trade

## Exports and imports dynamics, in EUR bn



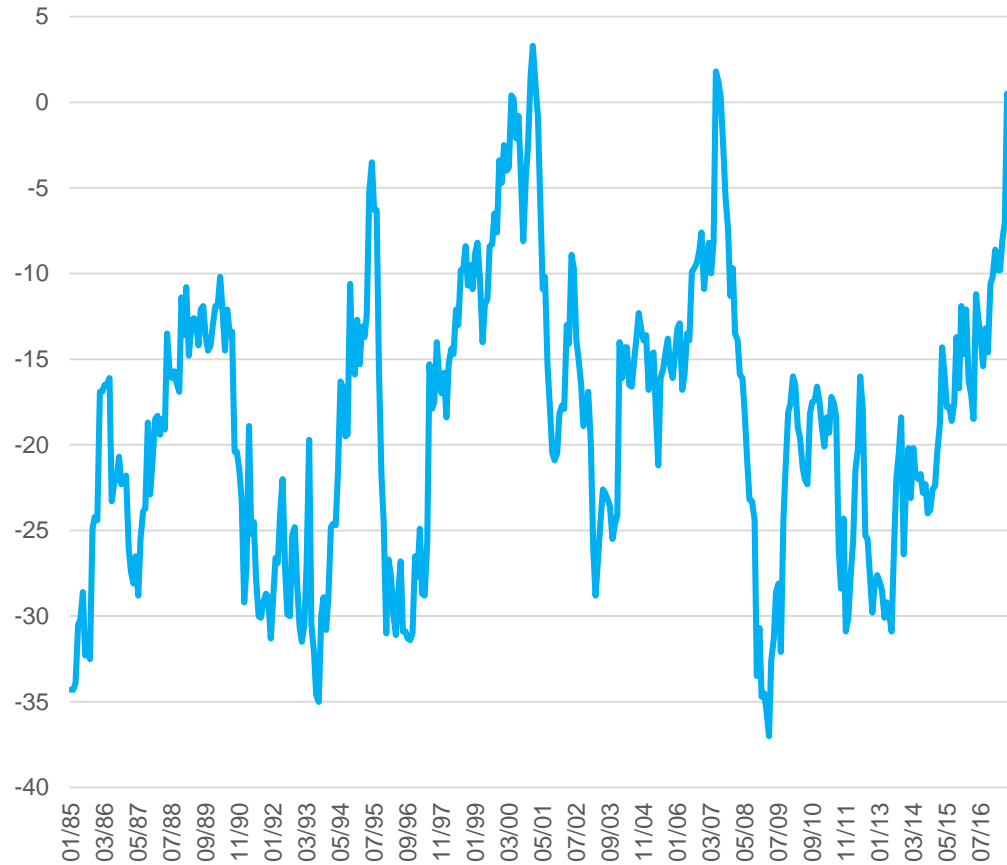
## Retail trade



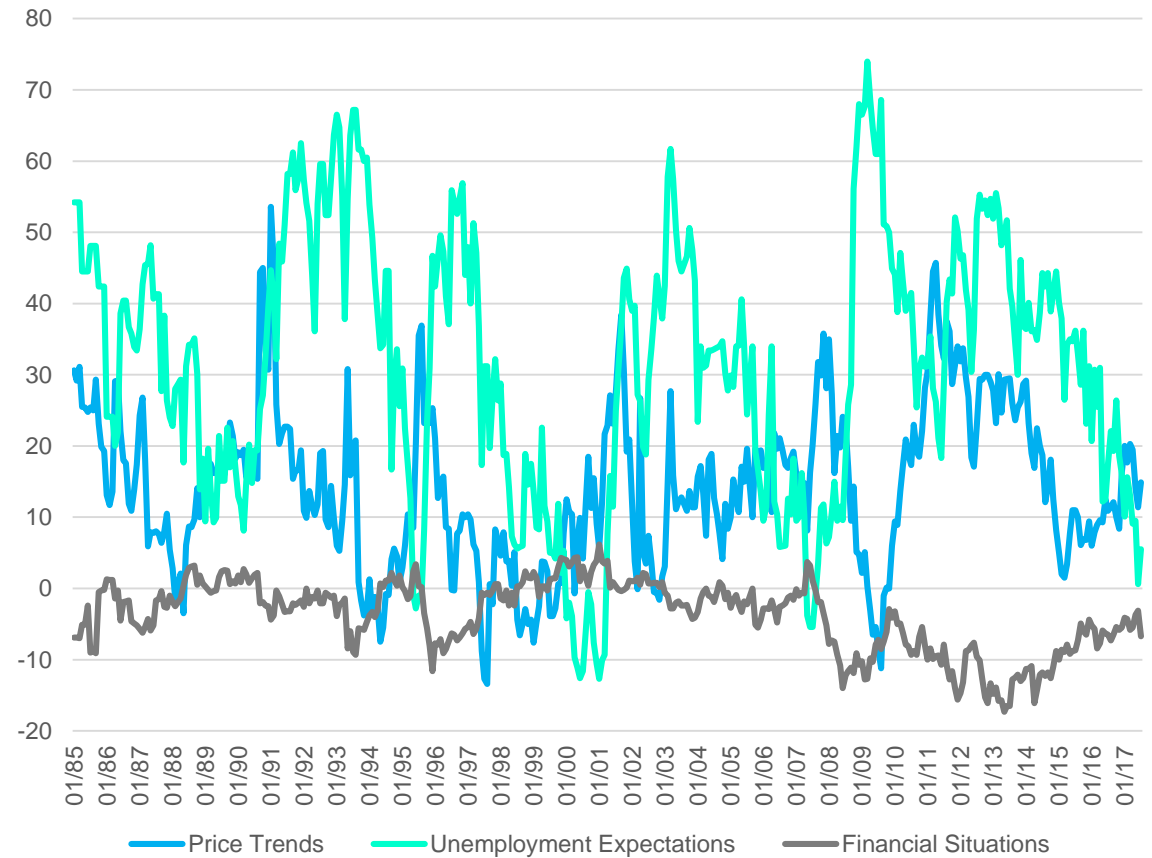
Source: CEIC, ADA Economics

# Consumer sentiment

## Total balance



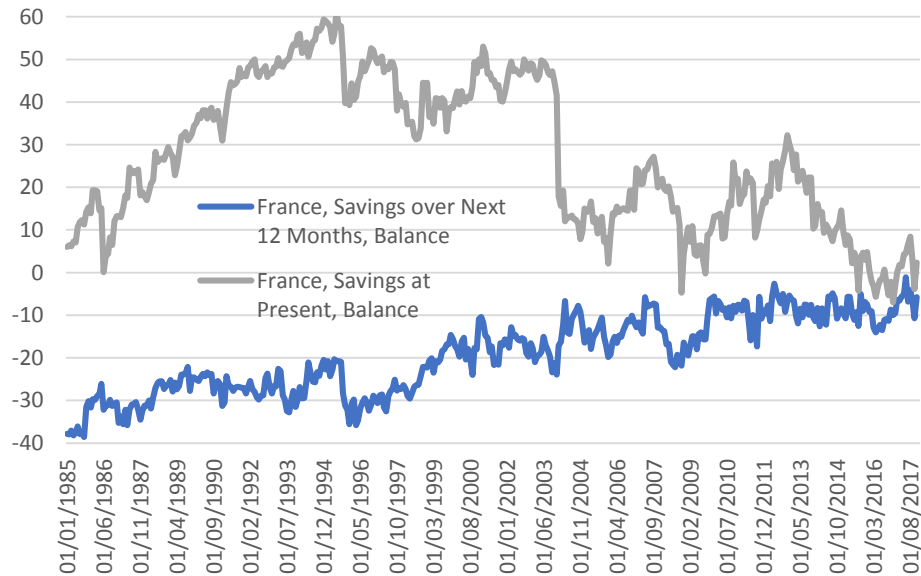
## Indicators



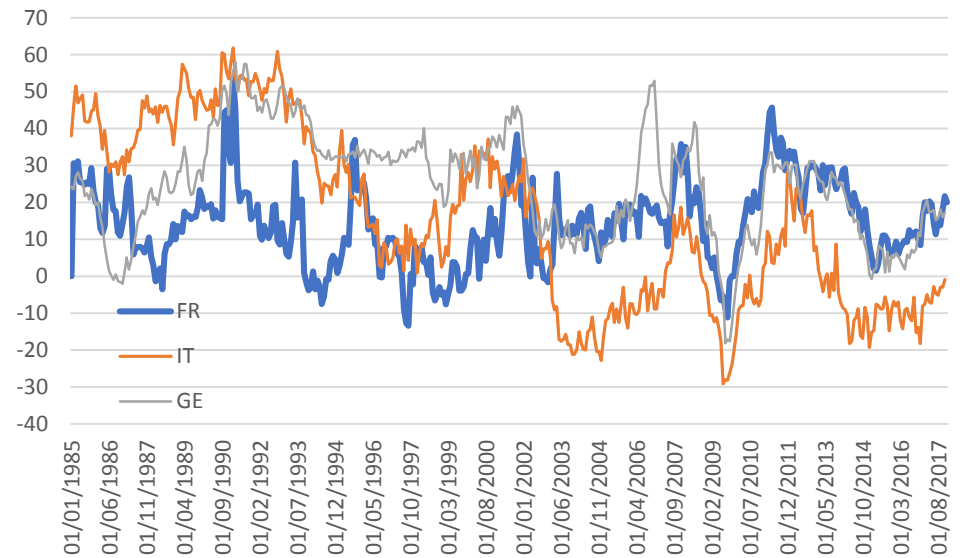
Source: CEIC, ADA Economics

# Households' concerns

Appetite for future savings is rising



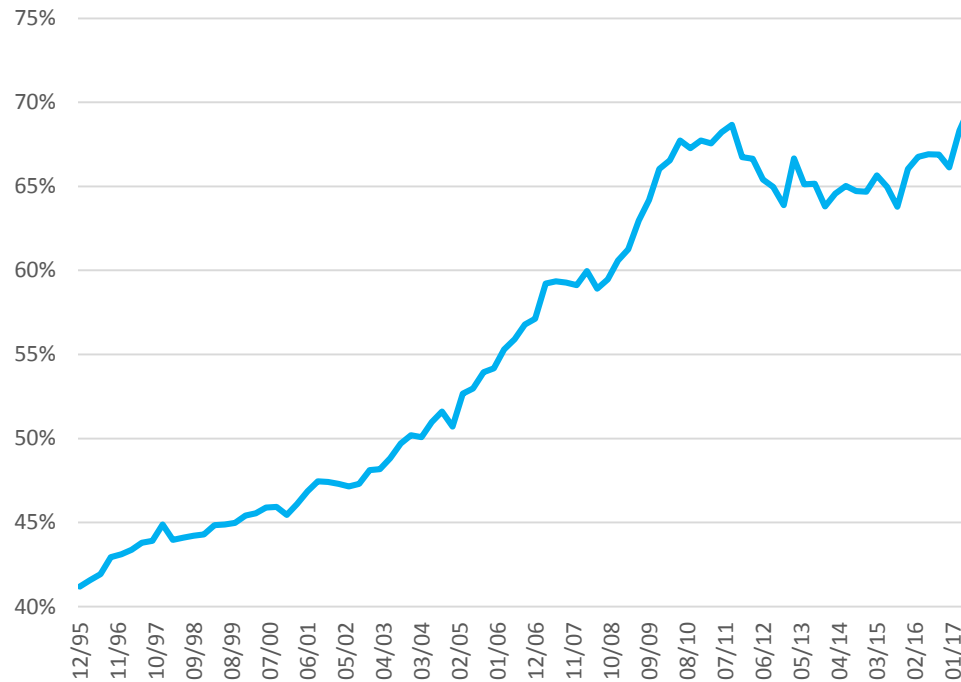
Inflation concerns are comparable to those of German Households, despite slower growth in France



Source: Macrobond on EC survey data, ADA Economics

# Household sector balance sheet

## Debt-to-GDP



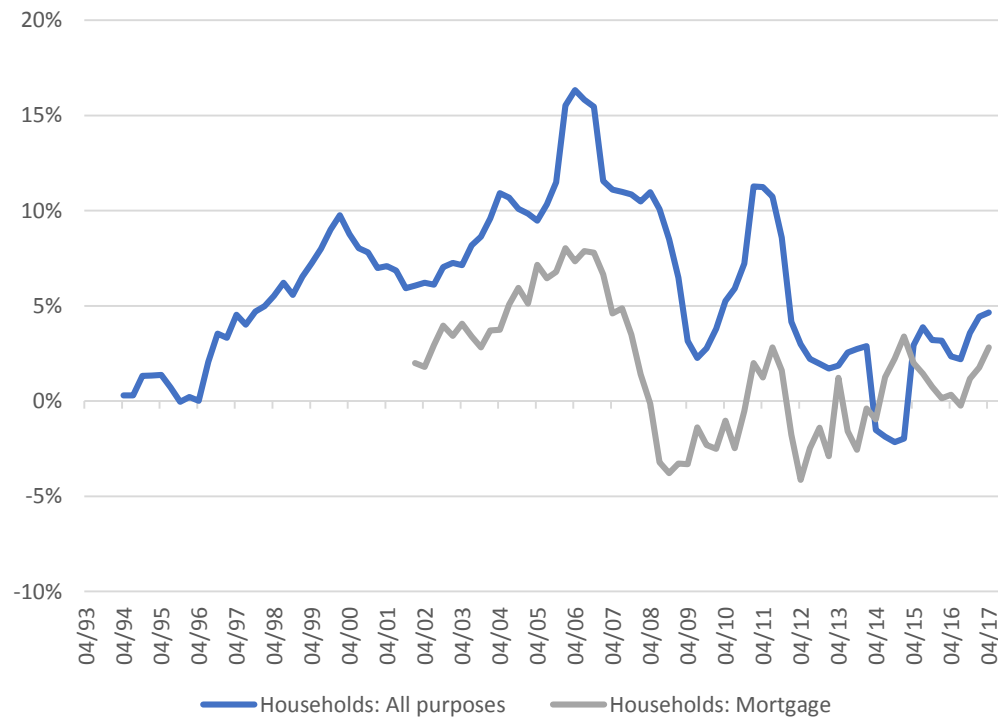
## Net assets-to-GDP



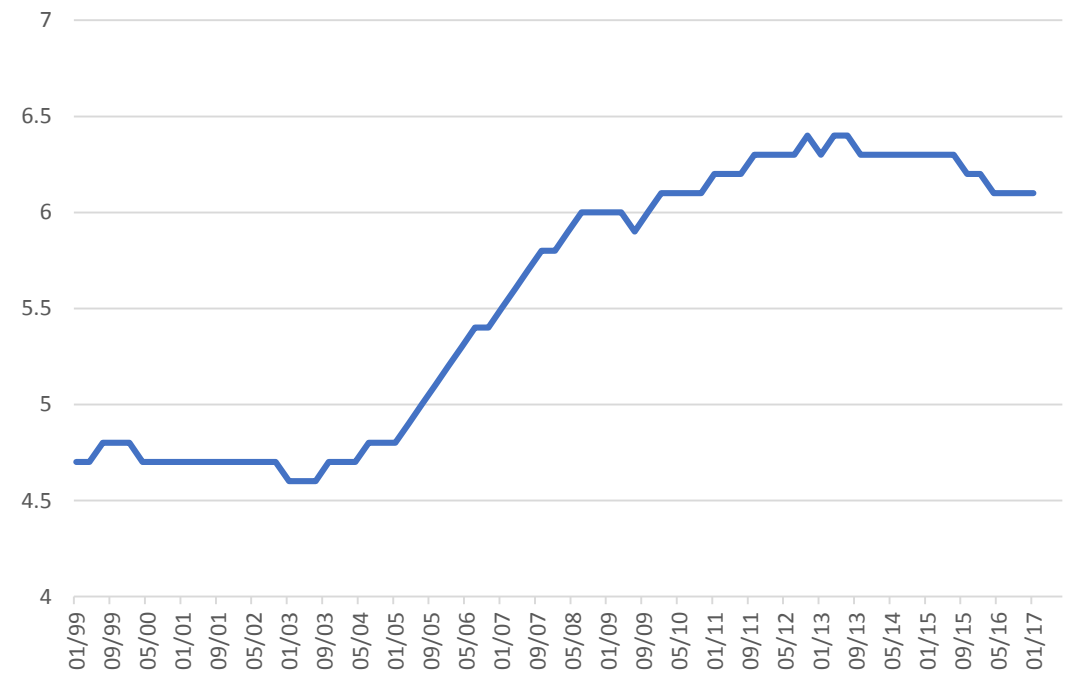
Source: CEIC, ADA Economics

# Loans to households

## Loans to households, yoy



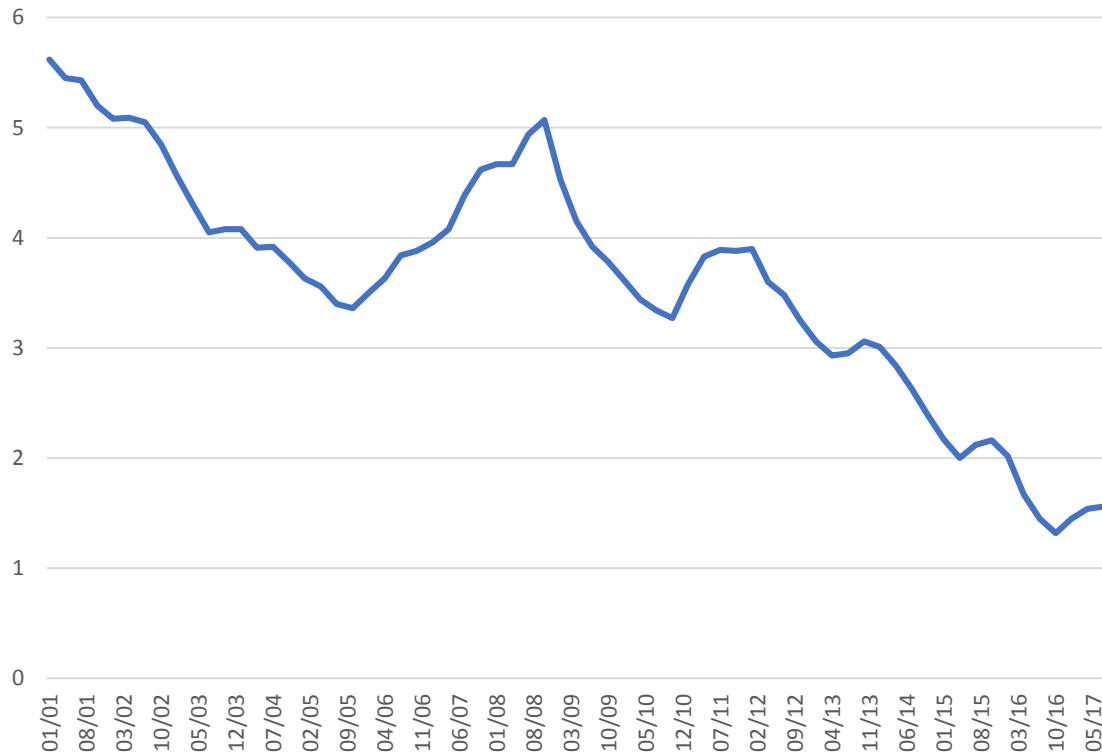
## Debt service ratios, as a share of income



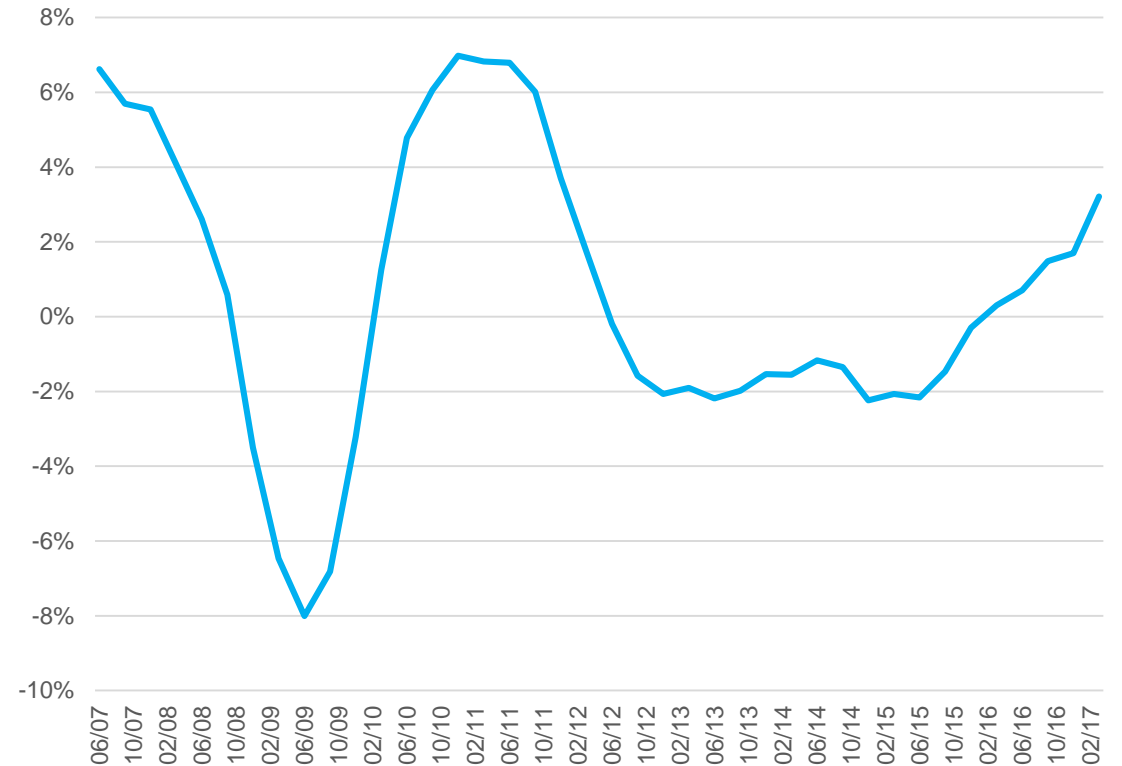
Source: CEIC, ADA Economics

# House prices

## Average interest rate on mortgages



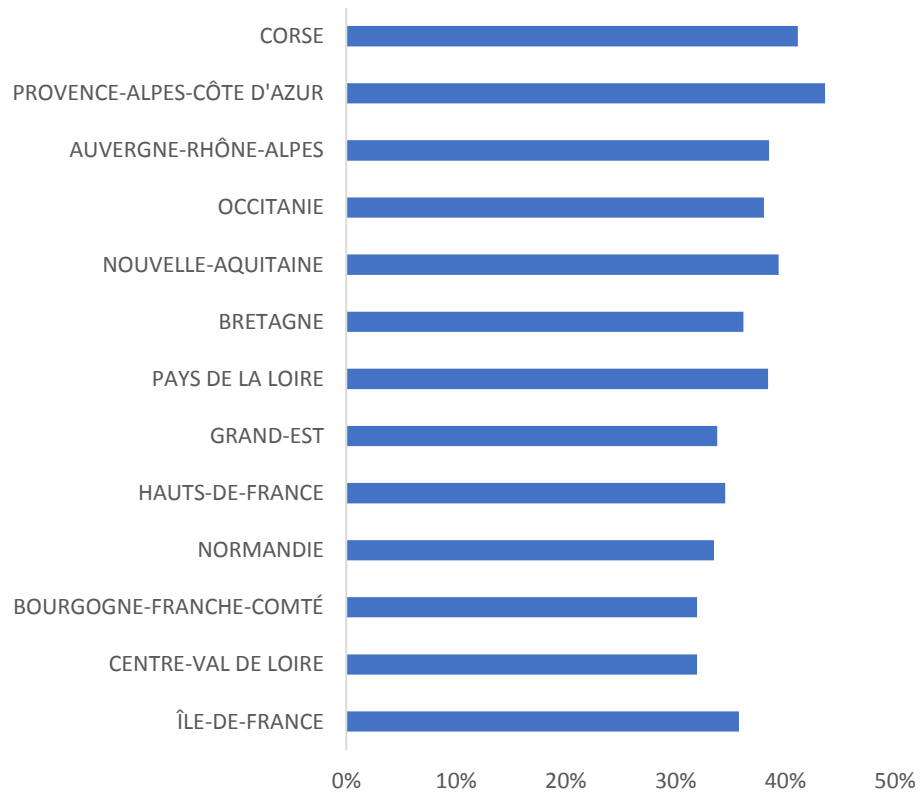
## Yoy house price changes



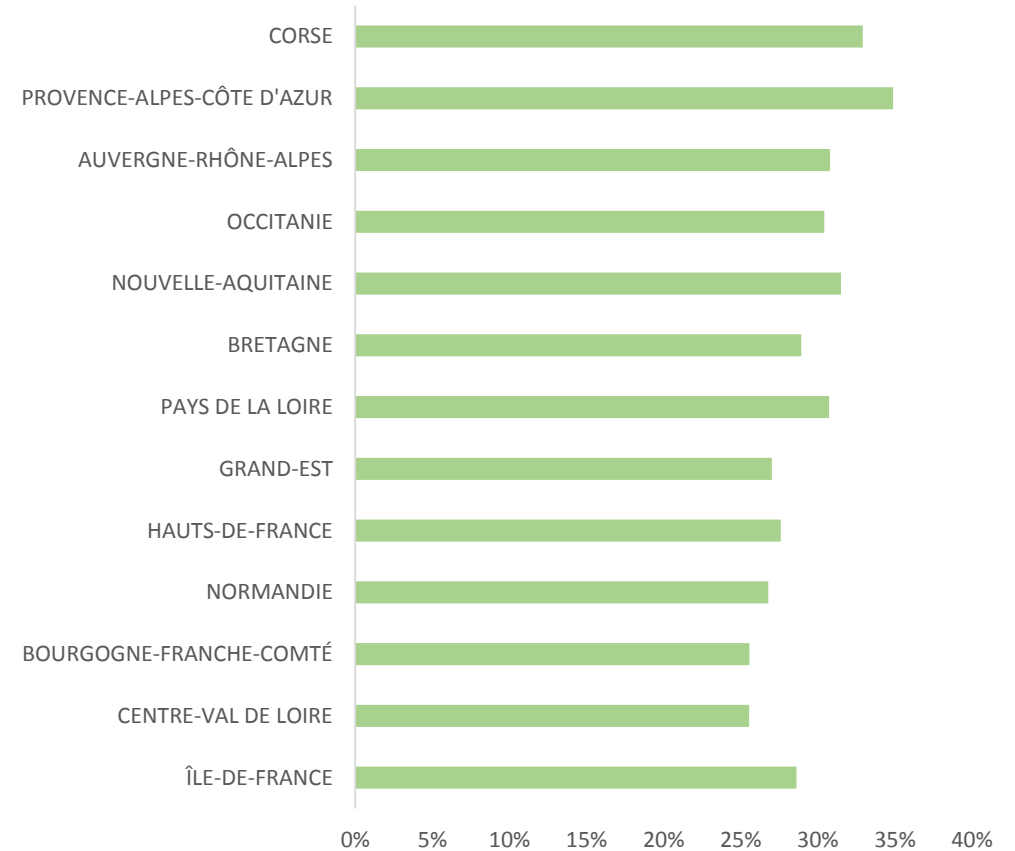
Source: CEIC, ADA Economics

# Debt servicing costs, by region

For 60m squares, 100% LTV



For 60m squares, 80% LTV

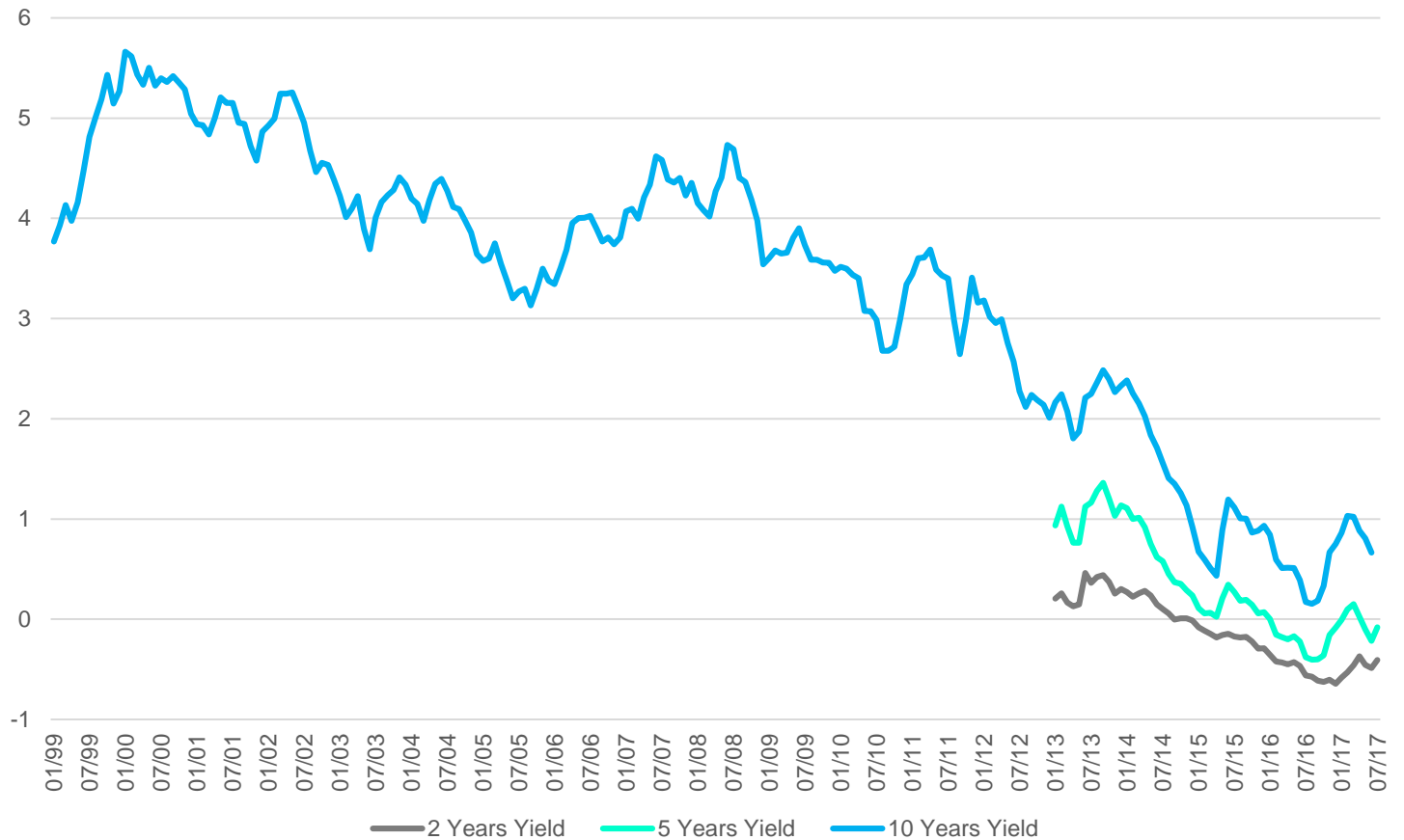


Source: CEIC, ADA Economics



# A long(ish) look at long-term borrowing costs

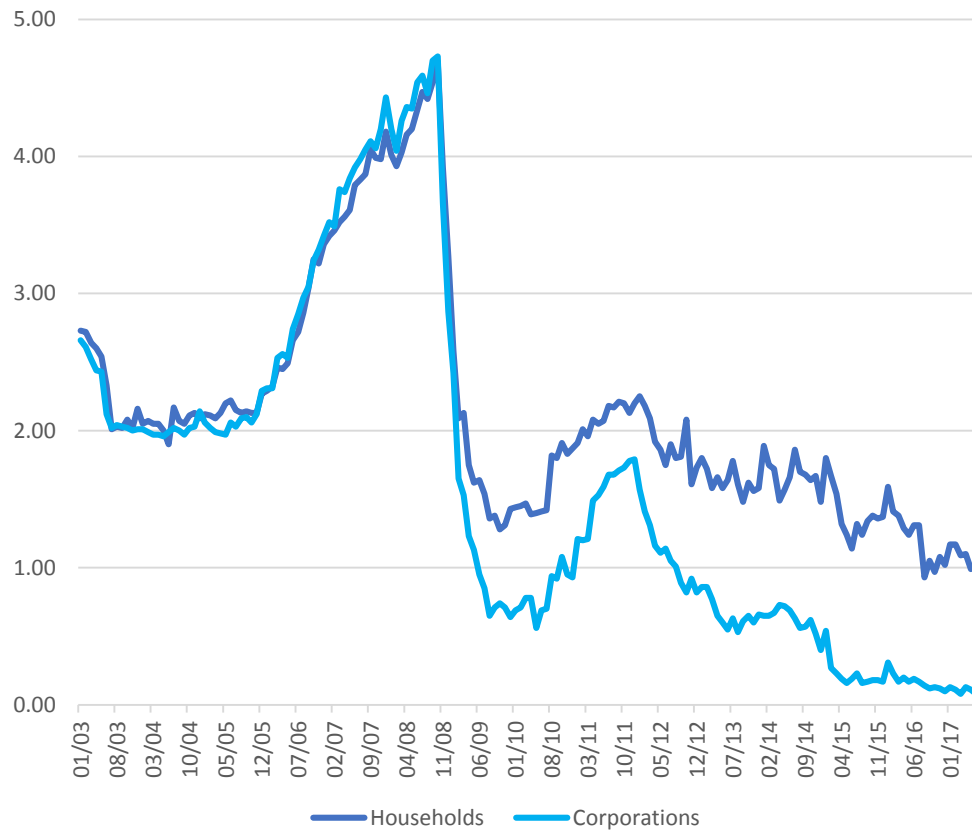
Government bond yield



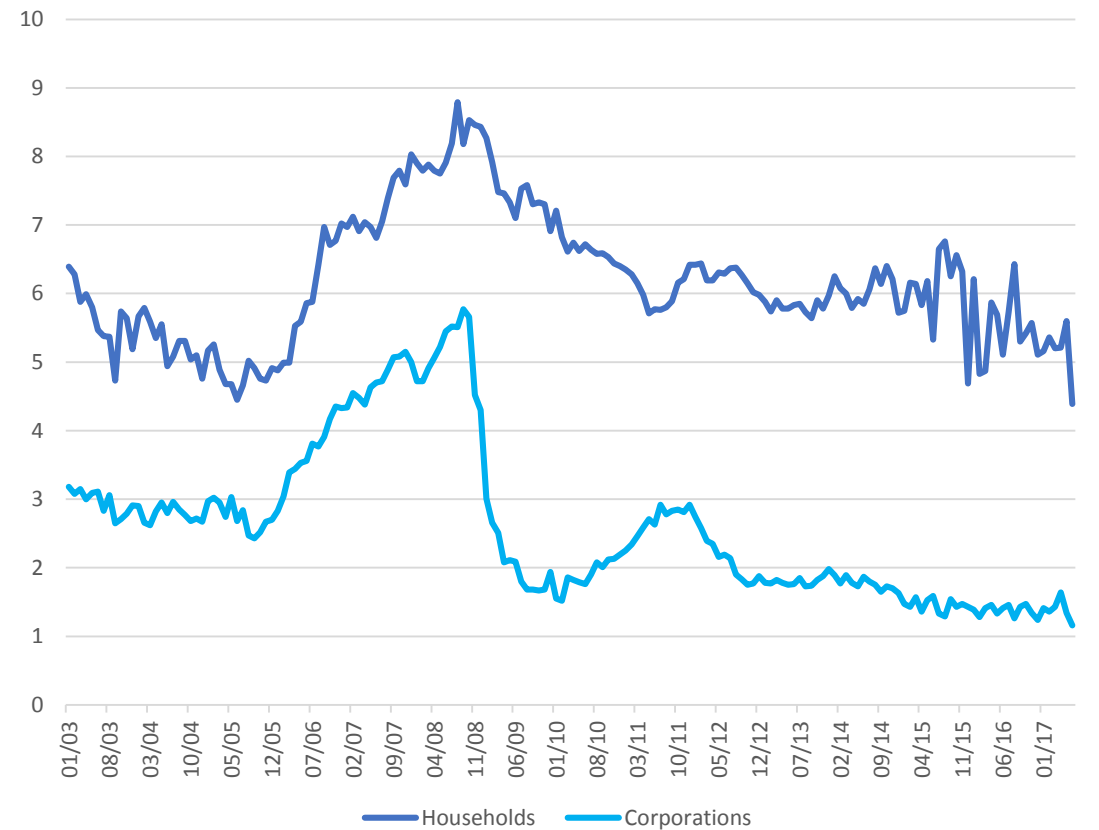
Source: CEIC, ADA Economics

# Retail borrowing costs (%)

Deposit rates, %, up to 1 year, new business



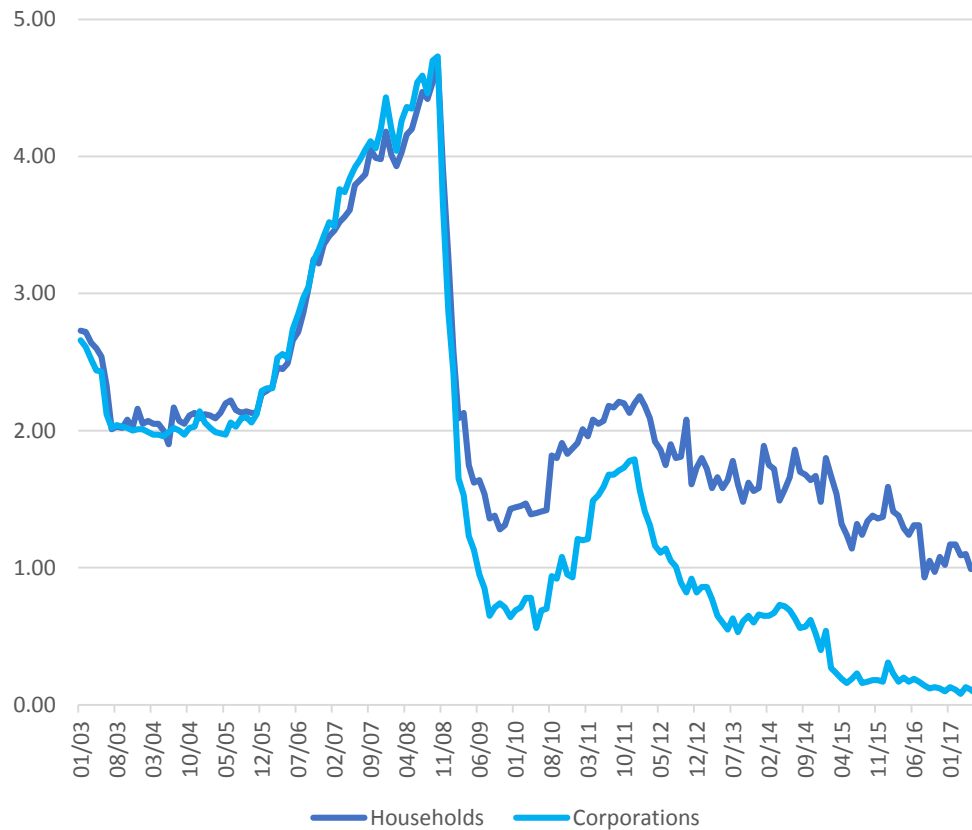
Lending rates, %, floating and up to 1 year, new business



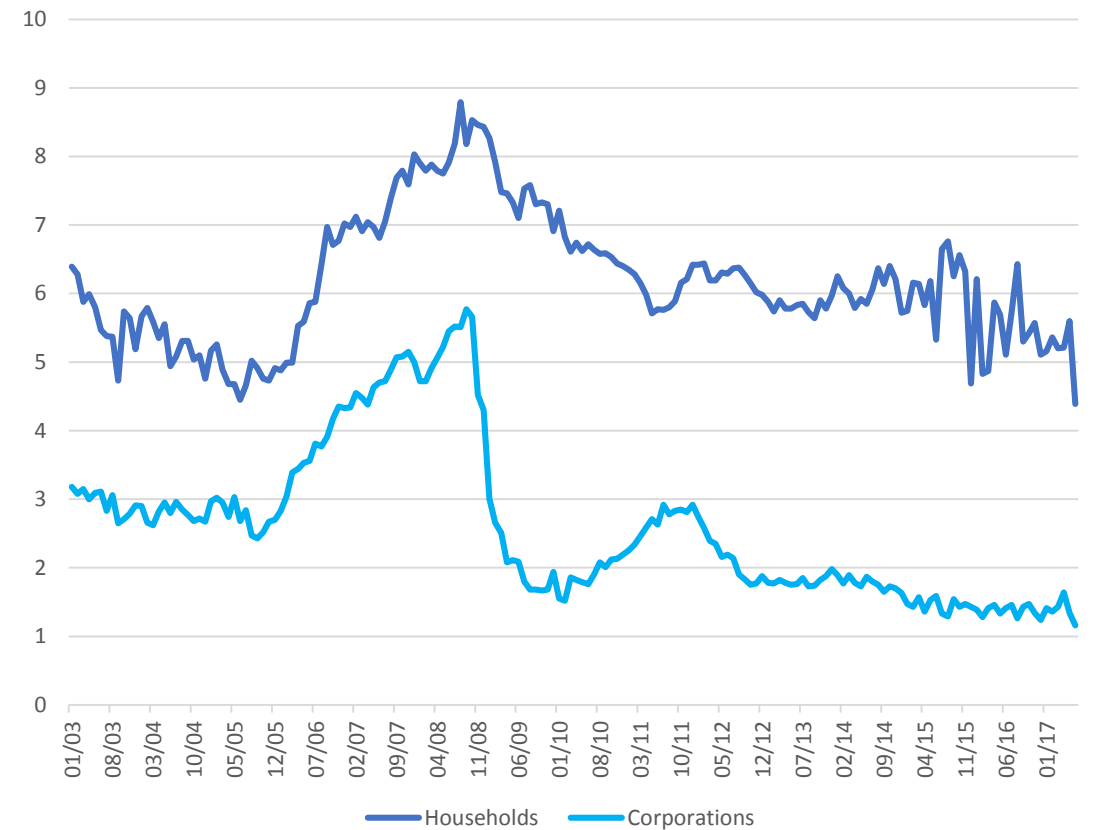
Source: CEIC, ADA Economics

# Retail borrowing costs (%)

Deposit rates, %, up to 1 year, new business



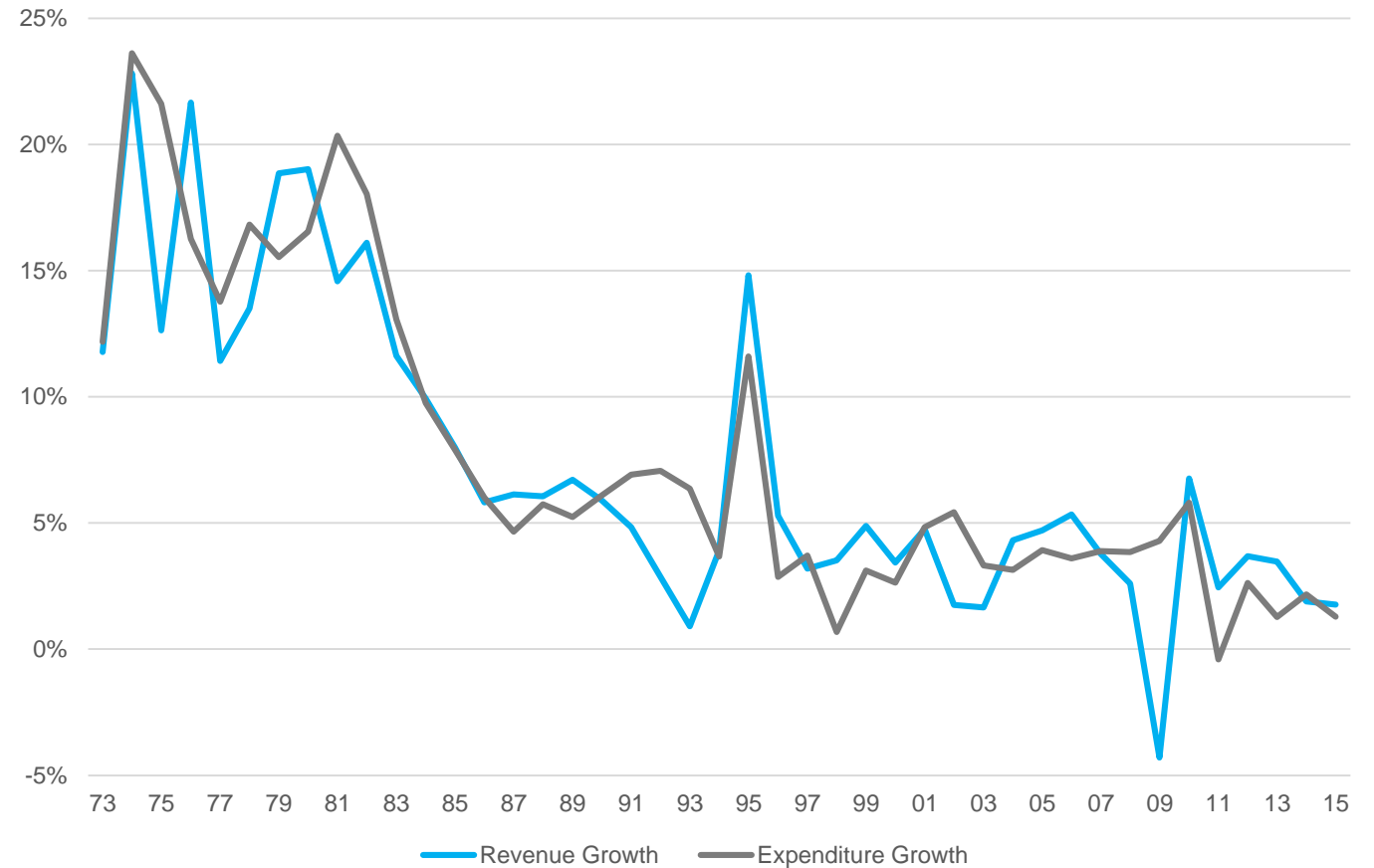
Lending rates, %, floating and up to 1 year, new business



Source: CEIC, ADA Economics

# General government non-financial account

Yoy % change  
in general government  
expenditure and  
revenue



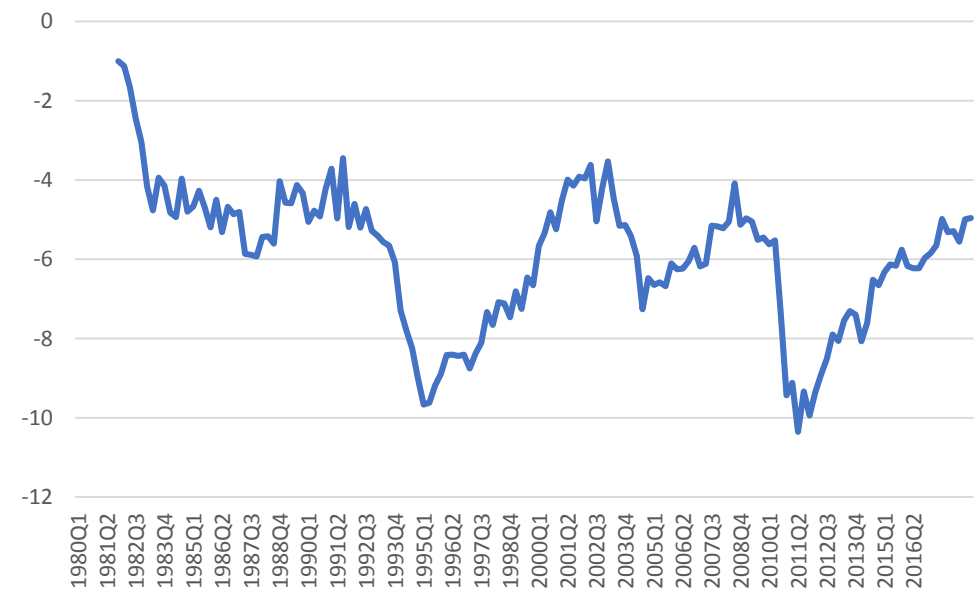
Source: CEIC, ADA Economics

# General government debt and deficit

In % of GDP, deficit on secondary axis



Primary balance, in % of the GDP



Source: CEIC, ADA Economics

# Bank of France projections

Year-on-year growth

	2015	2016	2017	2018E	2019E	2020E
<b>Real GDP</b>	1	1.1	1.8	1.7	1.8	1.6
<b>HICP</b>	0.1	0.3	1.2	1.4	1.2	1.6
<b>GDP Deflator</b>	1.1	0.4	0.6	0.9	1.3	1.5
<b>Domestic demand</b>	1.2	2	1.8	1.6	1.6	1.6
<b>Private consumption</b>	1.3	2.1	1.2	1.5	1.7	1.6
<b>Govt consumption</b>	1.1	1.2	1.5	0.7	0.7	0.7
<b>Total investment</b>	0.9	2.7	3.5	2.8	2.4	2.3
<b>Exports</b>	4	1.9	3.3	5.9	4.3	3.7
<b>Imports</b>	5.5	4.2	4.7	4.7	3.6	3.3
<b>Real HH GDI</b>	0.8	1.8	1.6	1.7	2.5	1.8

Source: Bank of France, ADA Economics

# Draft budget 2018

Economic forecasts for France, annual % change

	2016	2017	2018
Real GDP	1.1	1.7	1.7
Total CPI	0.2	1	1.1
Core inflation	0.6	0.4	0.8
Wages & salaries	2.4	3.3	3.1

Public finances, in % of GDP

	2016	2017	2018
General govt balance	-3.4	-2.9	-2.6
Tax and social contributions	44.4	44.7	44.3
Public expenditure ratio, excluding tax credits	55	54.6	53.9
Debt	96.3	96.8	96.8

Source: Agence France Trésor, ADA Economics

# ADA's deficit projections

- France's budget is based on estimated growth of 1.7% next year — the same as this year
- Macron's government hopes to reduce its public deficit to 2.6% of gross domestic product next year, so it would be under the 3% limit favoured by the European Union
- Substantial measures have been decided this summer, to lower expenditure growth
- It is expected that, if the public deficit falls below the 3% threshold, France would accordingly leave the excessive deficit procedure that was opened in 2009

	Source	2017	2018
<b>Expenditure growth</b>	Budget target	1.8	1.5
<b>Revenue growth</b>	ADA	2.3	2.8
<b>Deficit (% of GDP)</b>	Budget target	2.9	2.6
	ADA	3.1	2.4



# French state funding table

Borrowing requirements, in EUR billion

	2017	2018
Redemption of medium- and long-term debt	115.2	120.1
Redemption of other debts	-	-
Deficit to be financed	76.5	82.9
Other cash requirements	0	0.3
<b>TOTAL</b>	<b>191.7</b>	<b>203.3</b>

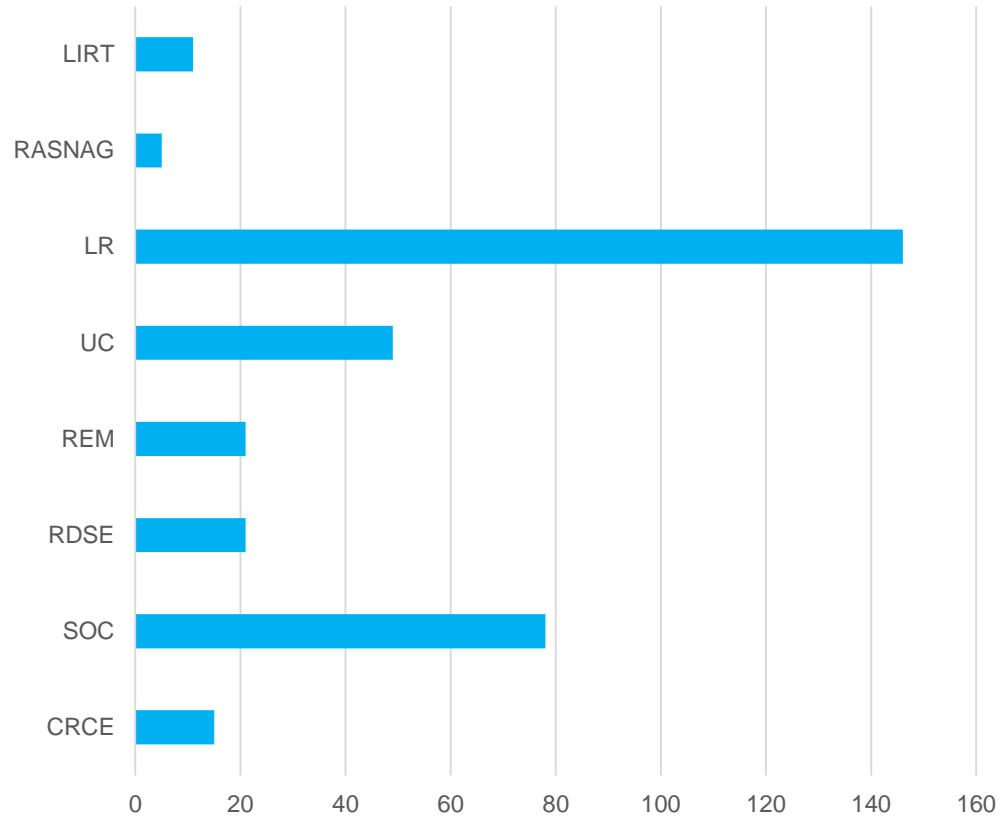
Source: Agence France Trésor, ADA Economics

# France – government set-up

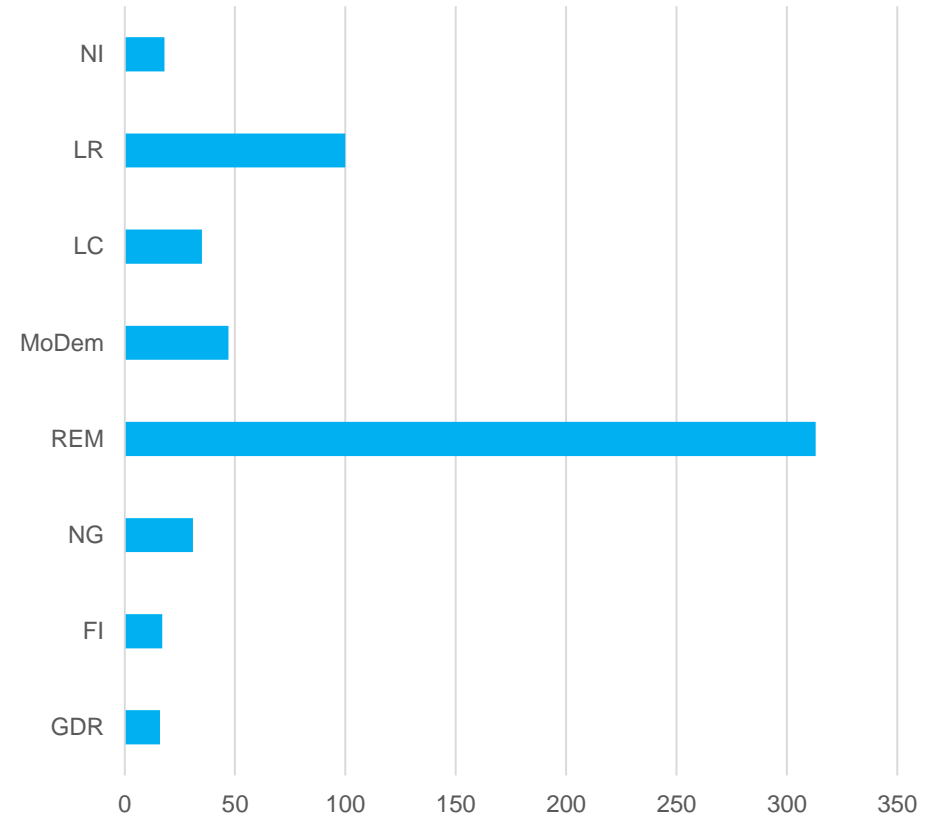
- President: Emmanuel Macron
- Prime Minister: Edouard Philippe
- President of the Senate: Gerard Larcher
- President of the National Assembly

# France – parliamentary structure

## Senate Political Groups



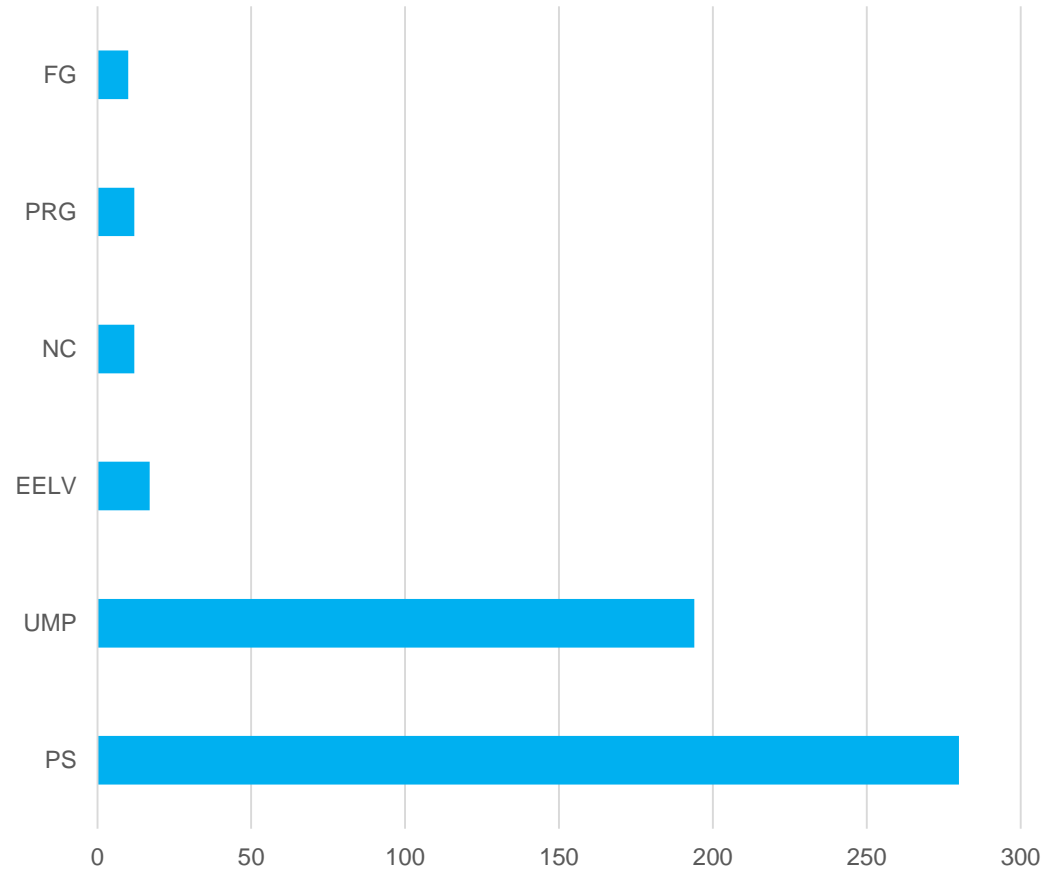
## National Assembly Political Groups



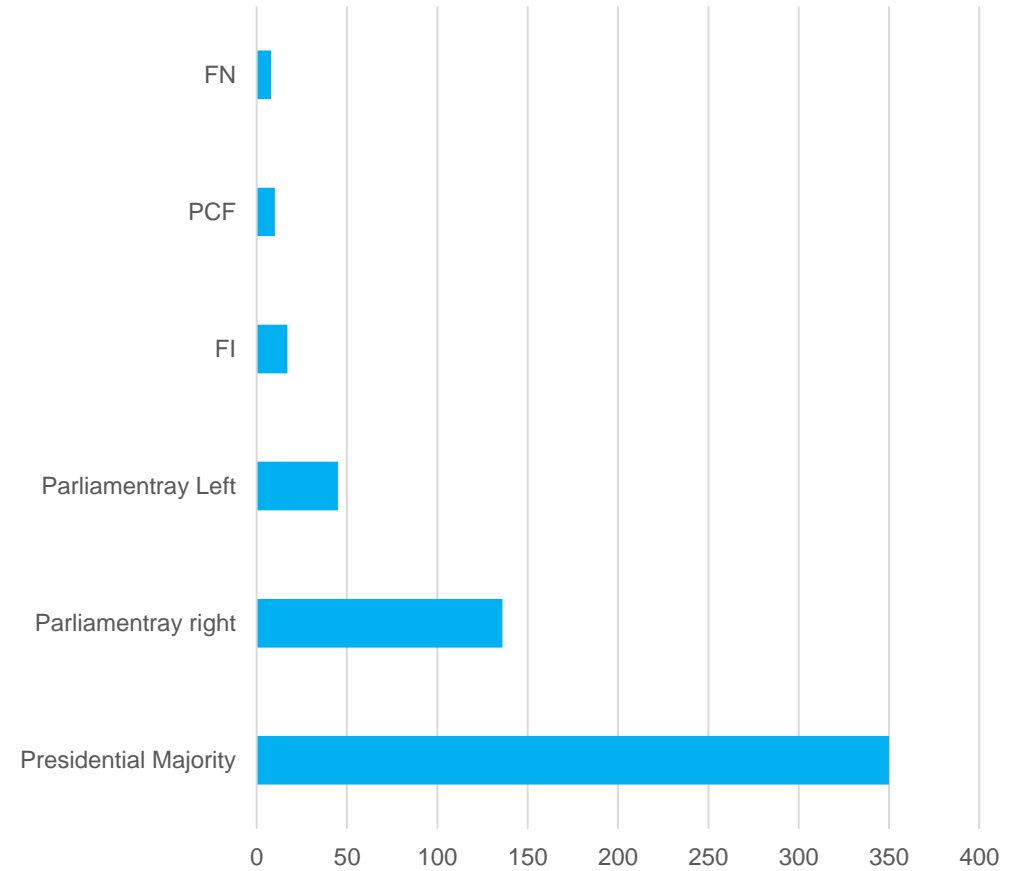
Source: ADA Economics

# France – parliamentary elections

## 2012 Elections



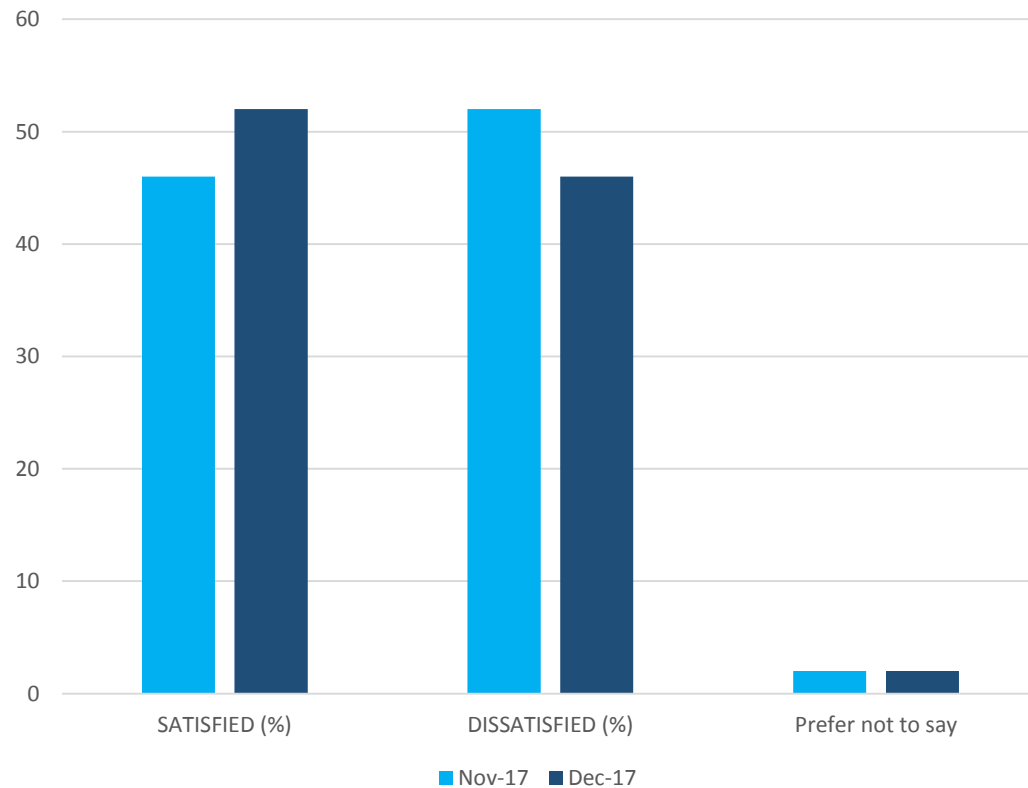
## 2017 Elections



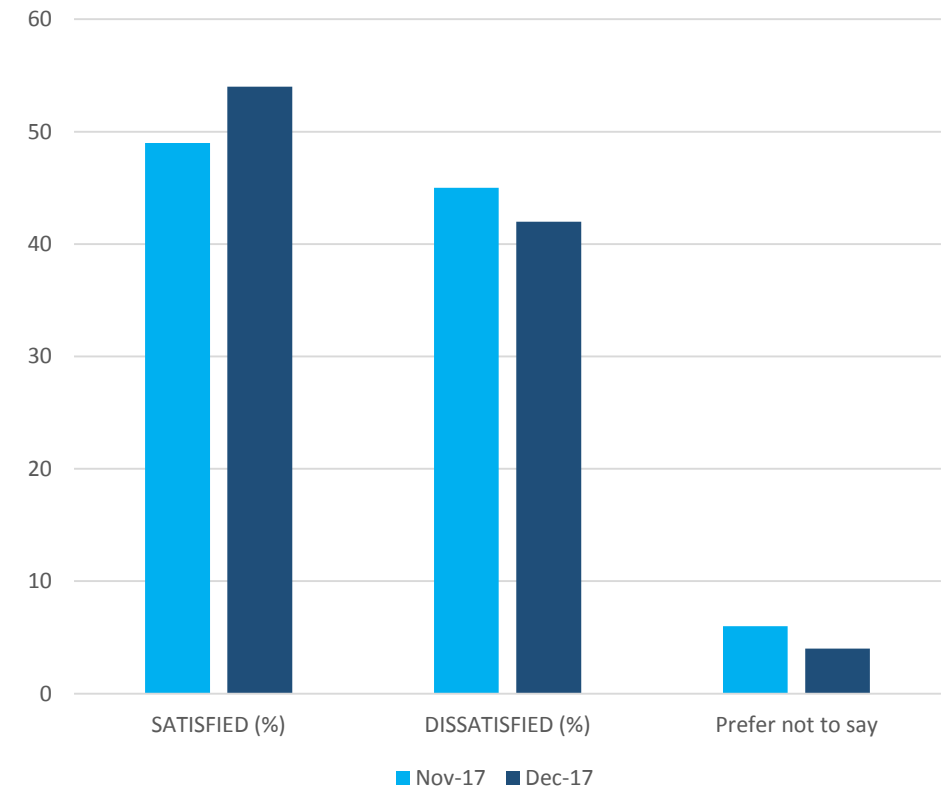
Source: ADA Economics

# Opinion polls

## Satisfied or dissatisfied with President Macron?



## Satisfied or dissatisfied with Prime Minister Philippe?



Source: Wikipedia, IFOP, ADA Economics