French business climate resilient despite social unrest

Latest business climate figures show French companies in most sectors remained undeterred by recent social unrest. Sensitivity to consumer demand seems high but there's certainly no sense of panic

Recent transport strikes have caused misery for many, especially in Paris

Business climate remains positive in both manufacturing and services

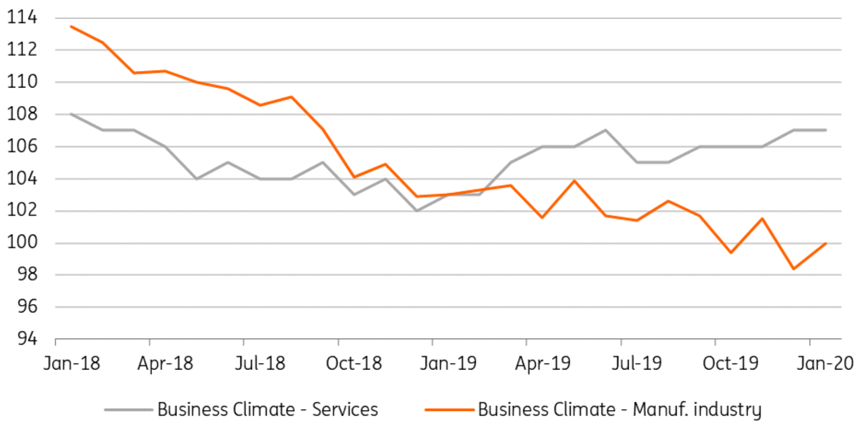
The main business climate indicator decreased slightly from 105 to 104.5 in January. Considering it is a 10-month low, it could be taken as bad news. However, given the period of social unrest that France, and especially its capital region, endured between mid-November and mid-January, this figure is a positive sign that business was far from being disrupted.

There are encouraging signs for future activity

In manufacturing, sentiment bounced back to its long-term average in December; recent output was higher than expected. Although business sentiment as far as the general outlook is concerned hit a one-year low for the second month in a row, there are encouraging signs for future activity: confronted with lower order books since last summer, companies managed to slash inventories which should lead to higher rates of capacity utilisation should new orders recover.

In the service sector, sentiment remained stable in January at 107, and well above its long-term average. If it were not for business worries about the general outlook (a component that deteriorated in January on the back of social unrest), sentiment would have increased thanks to additional hiring and more investment intentions. As for that, almost half of the companies surveyed reported having hiring difficulties. There is also generally no sign of weakening demand, but some sectors do show signs of softness, notably hospitality which was more affected than others by recent transport strikes Overall, the survey shows that if there were weaknesses, they should be temporary.

French business climate



Source: Refinitiv Datastream

Sensitivity to consumer sentiment remains high across sectors

Retail led to a slight decline in the overall business climate in January. However, looking at the figures in absolute terms, it seems that sentiment there is merely adjusting from a local peak in December. It seems that despite the street protests, mainly in Paris, retailers did not have a bad end to the year - recent sale levels in the January survey were very high and retail sales were up 1% in 4Q19 - but they are now adjusting their expectations and moderating orders. They may be right as we also noted a drop in consumer sentiment in December, with the main indicator dropping from 105 to 102, its lowest level since July. The main factor behind the drop was the consumers' assessment of the economic situation, which also affected their confidence as to their future financial situation. Fears of unemployment remain contained and the survey did not show a large impact on their purchasing intentions.

Retailers did not have a bad end to the year

All in all, today's figures confirm our initial assessment of the first effects of the pension reform protests that hit the railways and brought thousands of protesters back on the streets. The impact on industry is mild: companies continue to invest, fueling demand for investment goods while consumer good producers are taking steps to reduce their inventories in times of uncertainty and lower retail optimism. The impact on the service sector seems to be one of caution rather than any panic. Worried by the dire consequences of last year's "yellow vest" crisis, companies in this sector are showing they are ready to adapt to lower demand at the first signs of consumer retreat. That is why any sign of weakening consumer confidence is so worrying: even if consumer confidence remains high, and by any measure well above last year's levels, service companies are likely to be very sensitive in their hiring and investment plans to any new kind of uncertainty. Today's data shows that did not happen in January.

We expect all this will not have impacted 4Q19 activity which should show a small rebound compared to the third quarter. But if consumer confidence continues to be affected by the current political atmosphere, activity's elasticity to it could be unusually high in the first quarter. We remain cautious and keep our 1% GDP growth forecast for 2020.