France in 2021: Growing crises make recovery uncertain

France will end the year with contracting GDP growth. 2021 looks uncertain, with any economic recovery taking place amidst a complicated political environment

A few ups but a lot of downs

After the terrible shock of the lockdown, which led to a historic GDP contraction in France (-13.8% QoQ in 2Q20 and -5.9% in 1Q20), the recovery appeared to be particularly dynamic.

In the third quarter, France posted the highest growth rate in the eurozone (18.2% QoQ or 95.4% in annualised QoQ). Unfortunately, the fourth quarter will be synonymous with a new contraction in activity due to another lockdown implemented in France in November. Although less strict than that in spring, the new one means all bars, restaurants, non-essential shops, sports, tourist and cultural places are now closed, and non-essential travel is prohibited too. As a result, a drop in activity of around 15% over the month is to be expected, which implies that GDP should fall by 5% QoQ in the fourth quarter and 9.5% over the whole year; the contraction of GDP would amount to 9.5%.

The risks are still skewed to the downside. Indeed, President Emmanuel Macron has warned people that the lockdown could be extended if the number of cases does not fall to 5,000 per day (compared to 45,000 per day at the beginning of November). There is, therefore, a high probability that this target will not be achieved in early December and the lockdown will be extended. As December is an extremely important month for shops, the economic impact could be even higher than in the previous month. An extended lockdown for the whole month of December would probably mean a decline in GDP of more than 10% in the fourth quarter and an annual contraction of more than 1 percentage point additionally.

Political risks

Nonetheless, it is not clear that President Macron and his government will dare to opt for an extension of the lockdown for the whole of December. Indeed, public support for the measures has fallen sharply compared to the spring. Clearly, they are difficult to accept and "corona fatigue" is being felt. There is also anger about the closure of small shops which are deemed to be non-essential while all schools remain open and workers continue to go to their workplaces.

> *France is facing three crises at the same time*

Politically, the situation is very complicated for French officials. Social unrest could be on the horizon, reminding Macron of the painful "yellow vests" period. France is facing three crises at the same time: a health crisis, an economic crisis, caused by Covid-19, and a security crisis given the various attacks that have taken place on French territory in recent weeks.

This is a difficult time for Macron given that he is coming to the end of his presidential term and will, in 2021, begin his campaign for re-election the following year. The current situation doesn't give him much chance of making progress on the major reforms he promised, including on pensions and public governance. The only advantage for him at the moment is that no other candidate for the Presidency seems capable of showing that they could have managed the health crisis any better.

Currently, polls predict a tie between Emmanuel Macron and Marine Le Pen, from the far right, for the next presidential election. Given the very complicated security context, Macron will have to please right-wing voters, otherwise, they risk being lured by Le Pen, while at the same time being seen not to abandon left-wing voters. It's a decidedly delicate balance not least because there are so few certainties about the economic recovery next year.

An uncertain 2021 with consumers in focus

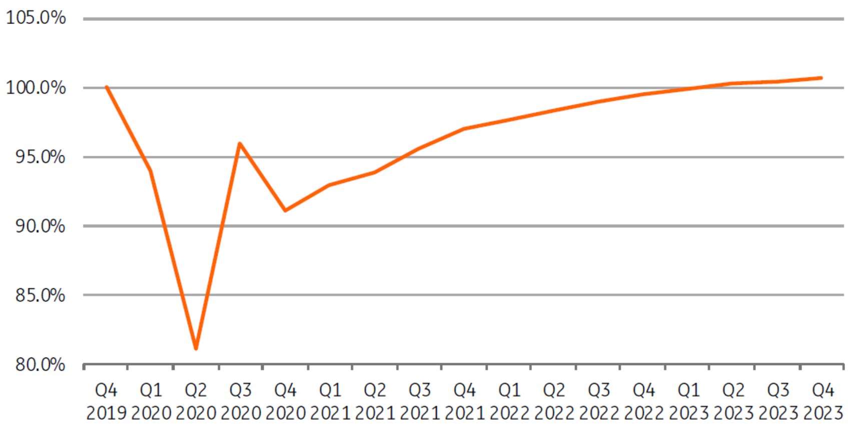
After a fall in GDP of at least 9.5% in 2020, the year 2021 should be synonymous with economic recovery. A rebound can indeed be expected in the first quarter of 2021 after the current lockdown, but it is highly unlikely to be as dynamic as that observed in 3Q20, after the initial one. Firstly, winter and indoor activities seem to be more conducive to the spread of the virus than summer, which raises fears of a more gradual easing of lockdown measures than the first time. Secondly, because the message is now clear: as long as there is no vaccine or treatment, the coronavirus will remain and fears of a third outbreak of the pandemic and the restrictive measures that follow will still be present. Unfortunately, neither households nor businesses will be able to exclude a third lockdown from their future prospects. As a result, there's likely to be more caution when the second lockdown ends and that could well hamper the recovery.

Of course, the French government has put in place a whole series of measures to try to mitigate the worst of the economic problems that the country is facing and it is hoping that the economy can bounce back pretty quickly. Although there's a system of temporary unemployment, subsidies to closed companies, loans and state guarantees, these emergency measures alone will not restore confidence.

Consumers are likely to adopt more cautious behaviour

In particular, household consumption will need to be monitored. This had contributed strongly to the rebound of the economy after the first lockdown and was only 2.3% below its pre-crisis level at the end of September. One reason for this is that the labour market, and thus household purchasing power, was not too badly affected thanks to the temporary unemployment mechanism that avoided redundancies. Nevertheless, as the crisis deepens and the overall economic situation deteriorates, consumers are likely to adopt more cautious behaviour. Declining consumer confidence and rising fears about jobs are worrying. Business investment is also likely to remain sluggish for a long period. And French exports are likely to remain impacted in 2021 by the crisis, because they are concentrated in sectors dramatically hit by the health crisis, including aeronautics and international tourism, which will take time to recover.

French GDP expectations (4Q19 =100%)



Source: INSEE data up to 3Q20 and ING forecasts afterwards

It looks as though only a vaccine against Covid-19 will bring a real recovery in the French economy. Consequently, we can hope for a more dynamic recovery in the second part of 2021 than in the first half if those vaccine trials are successful. The bright spot is that the French government's recovery plan should give a boost to activity, with an estimated impact of around 1 to 1.5ppt on GDP growth in next year. We're forecasting GDP growth of around 4.7% in 2021. The rest of the economic recovery will probably take place in 2022, where that plan will continue to play an important role, with a return to the level of activity that prevailed before the crisis forecast for 2023.

The French economy in a nutshell

	2019	2020F	2021F	2022F
GDP growth (%)	1.50	-9.50	4.70	4.00
Headline CPI (%)	1.10	0.30	0.80	1.40
Unemployment rate* (%)	8.50	7.60	10.40	9.20
Budget balance as % of GDP	-3	-11	-7	-5
Government debt as % of GDP	99	120	118	118

Source: ING forecasts

*Eurostat definition

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