

## Industrial production in France improves to start the year, before deteriorating

Industrial production in France increased in January but remains well below pre-pandemic levels. The war is likely to weigh on industrial production and economic growth in the coming months, while inflation will rise further



Industrial production in France increased thanks to the rebound of 'other industries', mainly pharmaceuticals

### Industrial production rebounds, before the new shock

Industrial production in France increased in January by 1.6% over the month (and +1.8% for manufacturing), thanks to the rebound of "other industries" (mainly an increase in pharmaceuticals, but also in metallurgy), extractive industries, energy and water, and food industries. Nevertheless, industrial production is still well below the level it was at one year ago, but also below its pre-pandemic level (-3.9% compared to February 2020). Plagued by supply difficulties, most of the major industrial branches have not yet managed to return to their pre-crisis levels, with the exception of the food industry and coking/refining.

The situation is particularly severe in the manufacture of transport equipment, where production fell again in January and is now 27.4% below its pre-crisis level. Looking ahead, industrial production is likely to be heavily impacted by the war in Ukraine and the sanctions that have been put in place against Russia. We expect the index to fall sharply from March onwards, particularly in transport equipment manufacturing, which is likely to suffer even more from supply chains difficulties.

## The war will cost France (at least) 0.5 points of growth

In general, these data, together with the February confidence indicators, are interesting because they allow us to take stock of the situation that prevailed before the start of the new crisis that has hit the French economy: the war in Ukraine. Overall, despite significant difficulties in certain branches of industry, the French economy was still dynamic before the shock, but its growth rate was normalising. However, the invasion of Ukraine by Russia profoundly reshuffles the economic outlook. Several impacts are expected:

- A shock to household and business confidence, which will have an impact on consumption and investment and therefore on growth. This impact is highly dependent on the evolution of the situation, and in particular on the duration of the conflict.
- A shock on trade, but also on French companies present in Russia and Ukraine. Russia is France's 18th largest export partner and a sharp reduction in exports to Russia will have a significant impact on growth in France. But, above all, many French-owned companies operate in Russia. These companies will be heavily impacted by the expected sharp drop in Russian domestic demand as a result of the expected sharp recession in Russia following the sanctions. The sudden cut in economic and financial links between Europe and Russia will also lead to losses for companies with interests in this country (unpaid invoices, loss of value on assets). As a result, the investment policy of these companies could be affected, also in France.
- A new shock on supply chains will have a further negative impact on growth.
- A shock to energy and other commodity prices, given Russia's specialisation in commodity exports.

In this context, any economic forecast becomes difficult. The growth outlook will have to be revised downwards and the inflation forecast upwards. At this stage, we estimate that the war in Ukraine will cost France (at least) 0.5 points of growth. Our forecast for 2022 is therefore revised down from 3.7% to 3.2%. This may still seem high, but it should be remembered that 2022 benefits from a threshold effect of 2.4% (if economic growth was 0% in each quarter of 2022, annual growth would still be 2.4% thanks to the good economic performance at the end of 2021). At this stage, we think it is too early to already forecast a recession, assuming a scenario where things will stabilise over time with sanctions in place. The risks around the forecast are nevertheless strongly tilted to the downside and depend on the outcome of the conflict.

On the inflation front, higher expected energy and commodity prices lead us to revise our inflation forecast upwards by 0.5 points for the year 2022. We now expect inflation to remain above 2% throughout 2022, averaging 3.2% for the year. The risks here are on the upside.

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