

## France: Industrial production points to better second half

Industrial production increased by 0.7% in July. The figures reflect a better outlook for corporate investment. Confidence indicators still point to a decent second half, although late 2017 peaks are not likely to be repeated



House construction in Orleans, France

### Manufacturing production seems to have peaked

Industrial production rebounded by 0.7% month on month in July, after 0.7% in June. This adds to previous signs that industrial production growth could now be stabilising at levels just below 2% year on year. After declines of 1.3% and 0.3% quarter on quarter in the first two quarters of the year, we should witness a small rebound in 3Q18. Manufacturing production increased by 0.5% in July, but only investment goods production increased (by 2.3% MoM) while both consumer durables and intermediate goods saw declines.

Overall, the July reading is in line with our expectations. Indeed, as investment goods production rebounded in July, it is now 1% above its peak of 4Q17, reflecting an improvement in the investment environment for non-financial companies, which was shown in the 2Q18 GDP figures.

The situation is however much worse for durable consumer goods, of which production is now 7.5% below its 4Q17 peak, also reflecting weak consumer spending.

There are signs of stabilisation though, mostly in recent surveys which show that, even if sentiment might not be as bullish as at the end of 2017, there is no pessimism yet, at least compared to where it was only 18 months ago. Business sentiment has stabilised just above its long term average in the industry, at 100.9, a notch below its 12-month average of 103.9 in June, indicating that the current downward trend in manufacturing production growth could stabilise just below 2% YoY in the third quarter.

We still believe that the second half of 2018 could be stronger than the first. It will be insufficient to lift GDP growth above 2% in 2018 but is certainly a sign that the current phase of the cycle is not over yet. In our view, the second half of the year could still benefit from relatively high sentiment levels and from the abating negative effects of strikes. This should not hide the fact that the 2017 surge will have been short-lived: industrial production has been growing at a rate of 1.8% YoY so far this year, down from 3.6% in the second half of 2017.

**-0.1%** Small decline in construction activity so far in 2018

## Construction activity continues to point to a maturing house price cycle

Construction activity, which grew by 2.9% in 2017, stabilised in 2018 (-0.1% YoY so far this year). This had been confirmed by household investment growth in 1H18 GDP figures (it increased by a mere 0.2% QoQ in 1Q18 and declined by 0.1% in 2Q18, the lowest rate since 2015). While this sector has been recovering since 2015, we continue to see the first signs of the housing market cycle. As long as interest rates remain supportive, we do not believe in a hard landing, but construction activity figures since May are a sign that the housing market could be cooling down somewhat. In July, construction activity declined again, by 1.8% MoM, its fourth month of declines so far this year. As this came despite very high confidence in the sector and record high capacity utilisation, labour market shortages are part of the explanation. This explains why we still think that house price growth should not plummet either. We still expect 2.7% house price growth in 2018 after 3.2% in 2017.