

## French economic outlook is weak amid social tensions

Against a backdrop of tense social conditions and despite a disinflationary trend that is well underway, the outlook for the French economy remains weak. We forecast 0.5% growth in 2023 and 0.6% in 2024



The strength of demand for tourism-related activities and the high level of bookings for this summer should support French economic activity in the third quarter

### The French economy has started the year better than other European countries

In the first few months of 2023, the French economy held up a little better than the other eurozone countries, with GDP rising by 0.2 in the first quarter, after a period of near stagnation in the second half of 2022. After a sharp fall at the end of 2022 against a backdrop of high inflation, household consumption has stabilised, but this stabilisation is partly artificial.

As the government reduced its support for energy consumption, public energy consumption fell, while household energy consumption was recorded as rising, offsetting the sharp fall in food consumption (to its lowest level for 23 years). At the same time, investment fell sharply, weighed down by rising interest rates. The global economic slowdown has also weighed more heavily on French exports.

## Tense social climate keeps confidence at a very low level

The first few months of the year were marked by a tense social climate, with numerous demonstrations against pension reform in the spring, followed in the early summer by riots in some localities after a young man was killed by a police officer during a checkpoint. Although the microeconomic impact of these events may be significant for some sectors at the time, the effects are generally offset later. Studies have shown that the macroeconomic impact is generally very limited, removing a maximum of 0.1 or 0.2 points from annual growth.

Nonetheless, these events monopolised attention and probably helped to keep consumer confidence at a historically low level, and the household savings rate well above its long-term average. Against a backdrop of persistently high inflation, rising interest rates and a less expansionary fiscal policy, this is contributing to weak momentum in domestic demand, which is likely to persist over the coming quarters.

Given President Emmanuel Macron's lack of a majority in parliament, a tense and divided social and political context is likely to remain the norm over the next few years and will continue to slow down or prevent the implementation of important reforms. The pension reform, which raises the retirement age from 62 to 64, will come into force in autumn 2023.

## Moderate outlook

From a sectoral point of view, the strength of demand for tourism-related activities and the high level of bookings for this summer should support French economic activity in the third quarter, but the support should diminish thereafter. At the same time, the industrial sector is suffering from weakening global demand. According to survey results, business leaders' assessment of order books has remained very weak for several months. At the same time, inventories of finished products remain high. This means that production is likely to decline over the coming months, as companies see no new orders coming in and have to clear their inventories. The PMI indices for the manufacturing sector have been in contraction territory (below 50) since January.

In short, the growth outlook for the French economy is moderate. Growth in the second quarter will be weak, with a fall in GDP remaining a risk. Growth in the third quarter should be slightly better, supported by the good health of the tourism sector, which continues to benefit greatly from the post-pandemic recovery. But this is likely to lose momentum in the fourth quarter, and the end of 2023 and 2024 look weaker, against the backdrop of a global economic slowdown and high interest rates that will have an increasing impact on demand.

We are expecting growth of around 0.5% this year. For 2024, the gradual recovery in household purchasing power thanks to lower inflation is likely to be offset by even weaker global demand. As a result, we are less optimistic than the central banks and are forecasting French GDP growth of 0.6% in 2024 (compared with a forecast of 1% by the Banque de France).

## The trend toward disinflation has begun and will continue

Inflation in France stood at 4.3% in June, compared with 5.1% in May, thanks to a fall in energy prices and slower growth in food prices. The fall in inflation is set to continue over the coming months. Growth in producer price indices has slowed markedly. In addition, business price intentions are moderating sharply: price intentions in the manufacturing sector are at their lowest since early 2021, while in the services sector they are at their lowest since November 2021. These

figures are in addition to those for the prices of agricultural products, which are falling sharply, which should lead to a sharp fall in food inflation over the coming months.

The trend toward disinflation is therefore clearly underway and will continue. However, this trend will probably be slower in France than in other countries, due to less favourable base effects for energy. The tariff shield and fuel rebates prevented a sharp rise in energy prices over the summer and autumn of 2022. As a result, energy inflation is likely to return to positive territory in France in the coming months, with energy prices for the remainder of 2023 likely to remain higher than their levels in 2022, unlike in other countries. This will probably keep overall inflation higher in France than elsewhere this autumn and at the end of 2023. But this does not change the overall picture: ultimately, although less visible than elsewhere, disinflation is well underway and will continue to be seen in France over the coming months.

While this trend is clearly encouraging, it does not mean that the problem of inflation is completely over. There is still a major risk pocket, namely services inflation, which is likely to increase in the months ahead and will probably become the main contributor to French inflation by the end of the year. The successive increases in the minimum wage, particularly in January and May 2023, which are being passed on to all wages, will continue to push up the price of services. The Banque de France estimates that negotiated pay rises will average 4.4% in 2023 (compared with 2.8% in 2022 and 1.4% in 2021), often supplemented by a one-off bonus. Salary increases are more pronounced in sectors where recruitment difficulties are greatest.

As we expect the labour market to remain tight over the coming quarters despite the economic slowdown, wage increases are likely to strengthen further. However, given the lower price intentions and sluggish demand we expect in the coming quarters, it is likely that wage increases will not be fully passed on to selling prices, weighing on margins. Therefore, inflationary pressures, including in the services sector, should eventually subside. We expect CPI inflation to average 4.6% in 2023 (5.6% for the harmonised index) and 2.1% in 2024 (3.1% for the harmonised index).

## The French economy in a nutshell (%YoY)

	2021	2022	2023F	2024F	2025F
<b>Demand and output</b>					
GDP	6.8	2.6	0.5	0.6	1.3
Private consumption	5.3	2.9	-0.4	0.7	1.6
Investment	11.4	2.2	0.1	-0.7	1.5
Government spending	6.3	2.6	0.5	0.6	1.2
Net trade contribution (% points of contribution to GDP)	-0.1	-0.8	0.6	0.3	-0.1
<b>Labour market</b>					
Unemployment rate (% eop, Eurostat)	7.8	7.3	7.2	7.5	7.6
<b>Government finances</b>					
Budget balance as a % of GDP	-6.5	-4.7	-4.9	-4.8	-4.8
Government debt as a % of GDP	114	112	112	113	115
<b>Prices</b>					
Inflation (HCPI)	2.1	5.9	5.6	3.1	2.1

Source: ING Forecasts

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