

## France: Firms slowly exit the soft patch

Business confidence surveys in May show that manufacturing activity continued to improve in 2Q. But it will be harder for the service sector to exit a recent soft patch, as it relies more on domestic demand and while the government has taken measures to improve purchasing power, these have yet to be felt



Source: iStock

### French manufacturing continues to exit the soft patch

French business confidence was stable in May at 106.0. In April, it returned to its level of last summer, which was well before the “yellow vest” crisis. It remains higher than in the first quarter (103.4) which bodes well for activity in 2Q.

In manufacturing, business confidence was slightly above the 1Q level in May, rebounding from 100.8 to 104.1 on the back of lower inventories and higher order book levels. This improvement bodes well for activity in 2Q after the rebound registered in 1Q (by 1.1% QoQ after a 0.1% contraction seen in the last quarter of 2018 during the “yellow vest” crisis). In fact, despite the drop measured in March in most manufacturing sectors, we still expect industrial production to grow twice as much as the 0.4% reached in 2018, mainly supported by the continuous dynamism of corporate investments, the rebound in automobile production, and slightly more positive figures on the construction side. However, one has to remain cautious: investment good production has

been slowing down and PMI indicators for May are also indicating that industry is not out of the woods yet.

## **Inventories are getting lower and order book levels are improving**

### **Mixed signals from the service sector**

In the service sector, the PMI index for May was at its highest level since November. However, the business survey shows that future investment trends are lower than in March and April and that hiring intentions have also abated slightly after their 1Q rebound. Expected demand is only marginally better while pricing power remains a worry. This could slow down employment growth in 2Q but it is still possible that business surveys underestimate the positive impact from measures to improve purchasing power. This seems to be even more the case in retail where the last business survey showed that confidence declined in May, with lower ordering intentions. This shows that recent measures taken by the government to alleviate fiscal pressure on households have yet to reach business activity.

All in all, the May business surveys show that the French economy is exiting the 4Q18 soft patch just slowly, and is still mainly supported by external demand. We nevertheless expect domestic demand to continue recovering and support our current forecast of 1.3% GDP growth this year.