

## French domestic demand remains strong

In France, GDP growth (0.26% quarter-on-quarter) was disappointing in 3Q19. The rebound in private consumption was not entirely on track, but business investments continued their upward trajectory. We maintain our growth forecast of 1.3% in 2019, but expect a slowdown in the first half of 2020.



Source: Shutterstock

# 1.2%

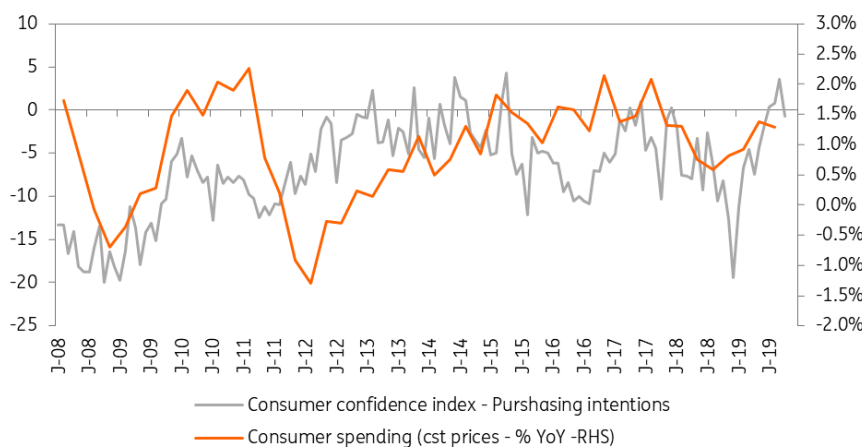
Business investments stronger than expected in 3Q19

Better than expected

### Businesses the main driver of domestic demand

GDP growth in the first quarter of 2019 was slightly lower than ING expectations. The rebound in private consumption did not completely meet expectations. Nevertheless, domestic demand was robust in Q3, particularly related to business investment.

Household consumption recovered from growth of 0.2% QoQ in 2Q19 to 0.3% in 3Q19, still below the levels reached at the beginning of the year. Consumer spending ended the summer badly (today's data shows that it contracted by 0.4% month-on-month in September). That said, September and October consumer confidence was at some of its highest levels since the financial crisis. The large decline in the unemployed population in Q3 (the sharpest quarterly decline in more than a decade), combined with the end of "yellow vest" crisis effects and the first effects of tax incentives, has contributed to a decline in unemployment fears and an – albeit slow - rise in purchasing intentions. We expect this to materialize even more in Q4. Private consumption was up only 1.3% year-on-year in Q3, which should lead to growth in 2019 that is barely higher than the 0.9% achieved in 2018. We expect 1.2%.



Source: Thomson Reuters

Household investment in new construction saw a very weak quarter after the rebound recorded in 2Q19 (+0.1% QoQ in 3Q19 after 1.6% in 2Q19). That said, it should be noted that the fall in rates after 2014, even if it took time to have an impact, has allowed investments to rebound since the beginning of 2016: here growth since then has averaged 3.3% per year. However, the catch-up seems to be over and the 2019 average should be 1.7%.

By contrast, business investment continued to perform well in the third quarter. With growth of 1.2% QoQ, this was above expectations. Indeed, even if no decline was expected, capacity utilization has declined in recent months, particularly in industry (where confidence indicators indicate a stagnation in activity and a mix of rising inventories and falling order books). On the other hand, it seems that investment is still robust in the service sector, where indicators remain positive. We expect a slowdown in the last quarter of the year, but for 2019 as a whole, business investment growth should nevertheless reach 3.9%, as in 2018.

Growth in public investment continues to contribute positively to GDP growth. After several years (2013–2016) of negative contributions, this boosted growth by 0.3ppt in 2018, a figure that is expected to double this year. So, after growth of 2.4% year-on-year in 2018, this should grow by nearly 4% in 2019 - but still 4% below the 2008 level.

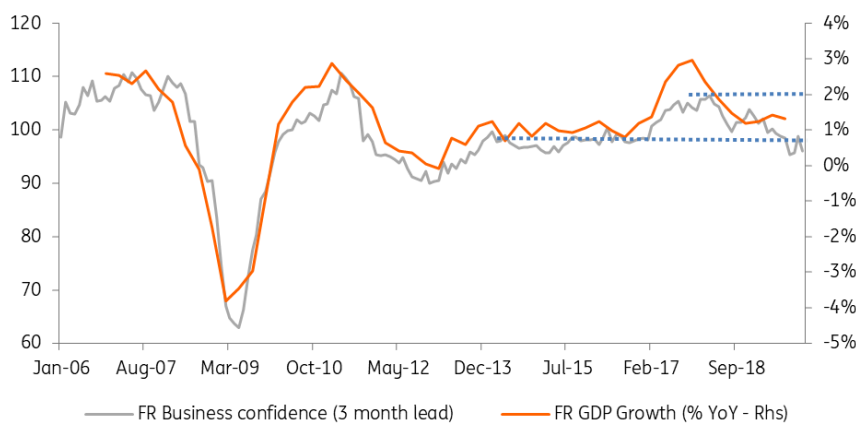
## French exports were slightly more dynamic in 3Q19

After a weak first semester, exports rebounded slightly in 3Q19, by 0.3%. This was not enough to offset the effect of imports on growth, as these grew faster with the recovery in private

consumption. This leaves a very negative contribution by foreign trade to GDP growth in 3Q19, -0.4pp.

The first detailed figures from last summer tend to show that it is mainly demand from France's main partners in the Eurozone (Germany and Italy in particular) that is dragging, while the rest of the world continues to post strong contributions to French growth. This is mainly due to a strong dollar, a situation that will have marked, as expected, most of 2019. Weak European demand is expected to remain a key factor in the dynamics of foreign trade in Q4, so we expect a slightly negative contribution from foreign trade in 2019, at -0.2%.

## Growth is expected to slow in 2020



Source: Thomson Reuters

## The French economy could resist the ambient gloom for longer

While this does not mean that it will be able to avoid it completely, the recovery in domestic demand that is currently supporting French growth is a largely domestic phenomenon. Apart from for industry, surveys continue to show high levels of confidence. Hiring intentions in the service sector allow us to be optimistic that employment figures will hold up well in coming quarters. This should enable growth to reach 1.3% in 2019, after 1.7% in 2018.

As the French economy is more dependent on services than on industry, which accounts for around 15% of value added (half of its share in German value added), we believe that the French economy should resist the current global slowdown for longer than the rest of the eurozone. However, the latest official projections for 2020, at 1.2%, already seem optimistic given the decline in economic activity in neighboring countries and some leading indicators (Chart 2). Other factors, primarily domestic, could stop the engine earlier. The transportation sector strikes announced in Q4 on the back of pension reform talks, if they were to affect the holiday season as in 2018, could already affect growth at the end of the year.

We therefore expect growth to slow down in the first half of 2020, which would limit GDP growth to 1.0% next year. As for the unemployment rate, while its decline is expected to accelerate by then (to levels below 8.0%), we believe this should stop with the slowdown in growth from around mid-2020.