

French industrial production rebounds on the back of strong corporate investments

The story is still looking positive for French industrial production, especially when compared to other European countries. So far, France seems to be resisting the growing discrepancy between services and the industry



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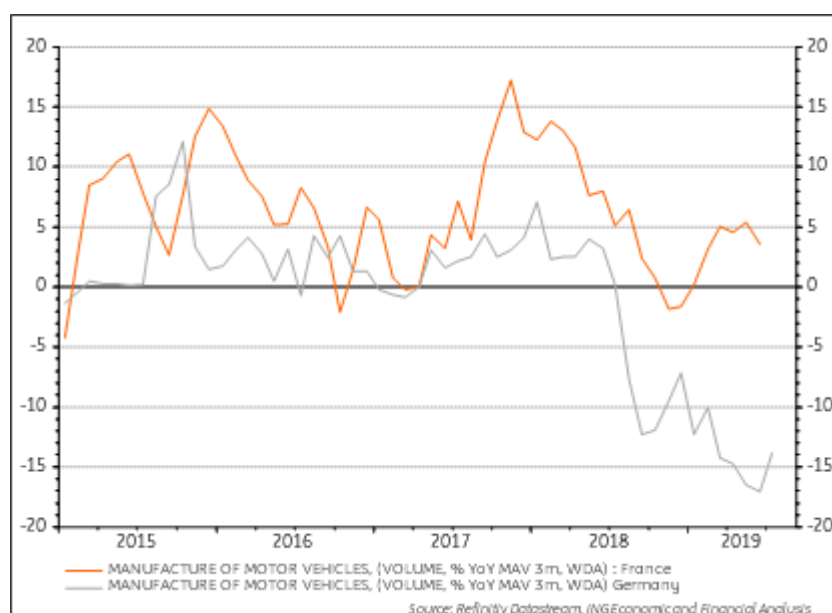
French manufacturing production was still growing in July

Industrial production rebounded by 0.3% month on month in July, starting the third quarter on a strong footing.

Given that manufacturing dipped slightly last year, it was a pleasant surprise to see it increasing by 0.3%. This rebound was mainly due to investment goods production which recovered by 1.2% MoM after the 2.7% drop registered in June. Other subsectors showed production declines, especially construction which declined by 4.2% and is now down by 1.2% on the year. After the 1.4% decline registered in 2Q19, the trend remains weak despite record-low mortgage interest rates on new residential housing.

The fact that French automobile sector is in better shape than Germany's where the impact of slowing world trade is being felt much more significantly, has undoubtedly helped industrial production

Consumer goods production, which rebounded significantly in 2Q19 (+3.7% QoQ) after the “yellow vest” crisis and three weak quarters, declined by 0.8% in July. The fact that the French automobile sector is in better shape than Germany's where the impact of slowing world trade is being felt much more significantly, has undoubtedly helped industrial production in recent months. It is still well above last year's levels and seems to have recovered after the emissions saga last year in the summer.



Source: Thomson Reuters Datastream

Is France escaping Germany's fate?

The dichotomy currently observed in Europe between the manufacturing and service sectors is a concern for activity growth in the eurozone in coming months.

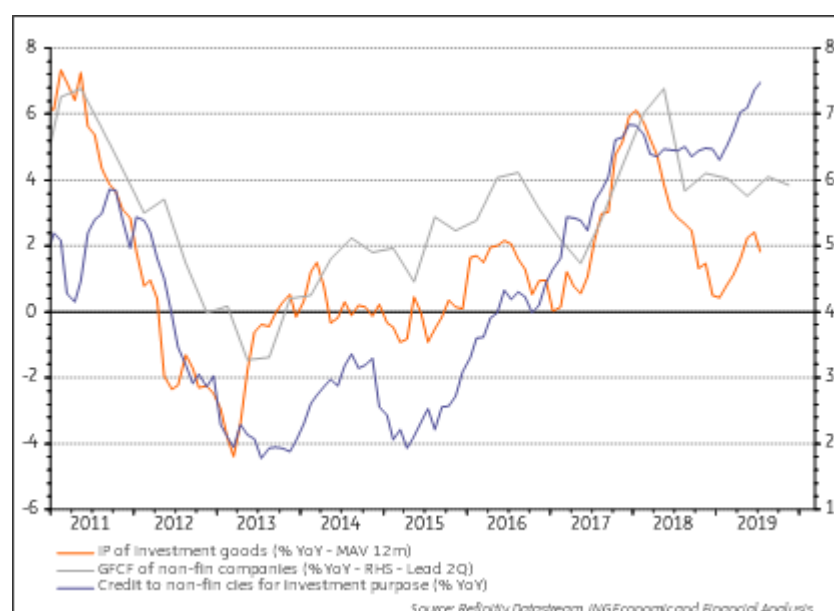
Activity indicators have indeed contracted much quicker in the industry than in services and the question is how long can this be sustainable for without triggering a slowdown in the other. Lower industrial activity generally lowers demand for services, triggers a slowdown in employment growth which in turn also affects services. So far, France seems to have been spared by this phenomenon. Firstly because the industry, and related services, are worth less than 20% of GVA. And secondly, because the French industry has slowed less than in other countries for the time being. One of the reasons for that is a robust investment dynamic.

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Indeed, with sky-high credit growth, French companies keep investing (gross fixed capital formation was France's main growth engine in 2Q19) which maintains demand for investment goods. This explains why today's figures show that investment goods were over-performing other manufacturing sectors in July.

However, the recent trend in production has not been positive, with 2Q19 production figures showing a 1.2% drop. On the year, the trend is also less positive, which could mean that companies are reducing their production plans as they forecast less demand. If this is the case, we will probably see lower investment figures in the second half of the year, despite strong credit growth.



Source: Thomson Reuters Datastream

The story is still positive for French industrial production, especially when compared to other European countries. Production rebounded in the first two quarters of the year after the “yellow vest” crisis. Looking at the most recent figures though, it could be that the catching up effect is already over and that the trend for business investments – while still positive – is slowing down.

That does not mean industrial production figures will turn negative in the coming months. We still expect industrial production to grow twice as fast as it did in 2018, supported by the continuous dynamism of corporate investments and the rebound in automobile production.

This should confirm the French economy growing near its potential, or 1.3%, in 2019 as a whole.

