

25 May 2023
Snap

French business climate decline shows warning signals ahead

France's business climate has deteriorated to its lowest level in over two years, signalling a clear turning point and an expected slowdown in the second quarter. Inflationary pressures are moderating substantially



Signs of a worsening outlook have been accumulating for several months, but until now, they haven't overshadowed the outlook

Signs of a worsening outlook emerge

The business climate in France deteriorated in May, falling by two points to 100 – its lowest level in over two years. The decline is notable in the services sector, as well as in industry, retail and wholesale trade. Both the assessment of the current situation and the assessment of business prospects are falling everywhere.

Signs of a worsening outlook have been accumulating for several months, but until now, they haven't overshadowed the outlook. With PMI indices published yesterday, the May data are now very clear: a slowdown in French economic activity is to be expected in all sectors, starting in the second quarter. And this slowdown is beginning to have an impact on the labour market, which means that it's likely to continue for several quarters. The employment climate fell sharply in May to 106 – its lowest level since September 2021 – due to a more negative assessment of employment developments in the services sector.

Given these early signs of labour market weakness, a weaker outlook according to business leaders, persisting high inflation, expected weak global growth and the impact of monetary tightening being felt in a more meaningful way, we expect GDP growth to be weak in the coming quarters. This should bring 2023 growth to 0.6%

and 2024 growth to 0.7%, with risks tilted to the downside. While France escaped recession last winter, today's indicators are a reminder that a recession in the coming months cannot be ruled out.

Divergence in Europe

With this generalised weakening, France is an exception from its neighbouring countries. In other European countries, the divergence between the manufacturing and service sectors increased in May as the global economic slowdown weighed down industry, while services benefited from the gains in purchasing power linked to lower energy prices and higher negotiated wages. In France, this divergence is not quite as significant – and more importantly, the slowdown is visible everywhere, including the services sector.

The difference between France and its neighbouring countries is likely due to differences in the inflation context; French inflation increased again in April, while it continues to decrease elsewhere. The biggest inflation shock on purchasing power occurred in 2023 in France but took place in many other European countries last year.

From an inflation perspective, the report brings good news, with business price expectations falling in all sectors. The decline is particularly pronounced in the industrial sector, where the expected trend in sales prices has fallen back below its long-term average. This is a clear sign that inflationary pressures have diminished significantly. In services, the decrease is less pronounced, but expected selling prices have returned to their November 2021 level.

Forecast prices are also down in trade and construction. This good news should be greeted with relief by the European Central Bank, as it indicates that inflation in France should begin a fairly clear descent in the coming months.

Charlotte de Montpellier

Senior Economist, France and Switzerland
charlotte.de.montpellier@ing.com

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. (“**ING**”) solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies)*. The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice. The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions. Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements. Additional information is available on request. For more information about ING Group, please visit <http://www.ing.com>.