

## French companies expect just a short-lived economic slowdown

Today's PMI and business climate indices are the first sentiment data for French companies this year. They indicate that an economic slowdown is underway, but companies are saying it may only be short-lived. We are more cautious and believe that a near-stagnation of activity over the year as a whole is likely



France's manufacturing sector is recovering but services remain a drag

### First glimpses of business sentiment in 2023

Since the beginning of the year, good weather and a drastic drop in global energy prices have led to widespread optimism and an upward revision of the growth outlook by consensus opinion. The question was, therefore, whether this renewed optimism was shared by the real economy and especially by companies. Today's publication of the PMI and business climate indices for January allows us to make an initial diagnosis.

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*The manufacturing sector is recovering*

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The composite PMI index fell slightly in January for the third consecutive month and stood at 49 compared to 49.1 in December. It is the services sector that is dragging the overall index down, given the context where the boom linked to the end of health restrictions is being brought to an end. The services PMI hit a 22-month low of 49.2 in January, down from 49.5 in December. At the same time, thanks in particular to the improvement in the global energy situation, the manufacturing sector is recovering and the index for the sector has risen above the 50 mark, reaching a 7-month high of 50.8. Overall, the PMI survey indicates a deterioration in the demand faced by French companies: new orders are falling and sales are decreasing. At the same time, companies are optimistic for the coming months. Their business and hiring prospects are improving. All in all, the PMI survey indicates that French companies are expecting an economic slowdown but that this is expected to be short-lived before we see an upturn.

The surveys carried out by INSEE show a slightly more contrasted situation between the various sectors. The overall business climate remained stable at 102 in January for the fifth consecutive month, but the sectoral situation differs markedly. In wholesale trade, both the assessment of current and expected demand weakened. At the same time, industrial companies are revising upward their assessment of current demand and their outlook for the future is stable. Companies in the services sector are much more optimistic about current demand but are less positive about the overall outlook. Finally, the assessment of past and expected future sales is revised upwards by companies in the retail trade.

All this data suggests the French economic outlook is uncertain but far from dramatic; it's not leaping into recession. Moreover, companies indicate that the employment outlook remains very positive in all sectors.

## Near stagnation of activity expected in 2023

We expect 2023 to be characterised by near-stagnation in the French economy in all quarters of the year. Given inflation, the evolution of real purchasing power will remain very weak, which will slow down the dynamism of private consumption. Given the uncertainties, the expected (albeit small) rise in the unemployment rate and the low level of household confidence, the household savings rate will remain high and above its historical average. Household investment in housing is likely to stall, weighed down by inflation, higher commodity prices and rising interest rates.

In addition, industrial production should continue to see supply difficulties ease but would face much weaker global demand and would still be at risk of a further significant rise in global energy prices. We expect GDP growth to be 0.2% for the full year 2023. 2024 could see a little more dynamism thanks to a more pronounced fall in inflation, although this will remain moderate. We expect 1.1% growth in 2024.

## Inflation higher in 2023 than in 2022

While most European countries have already seen inflation peak, inflation in France is expected to rise further in the first quarter of 2023. The revision of the tariff shield will lead to a 15% increase in household energy bills, compared to a 4% increase in 2022. The PMI survey indicates in January that, while inflation in production costs is falling, inflation in invoiced prices is still rising. This is particularly the case for the services sector, where the prices forecast by the January INSEE survey are at their highest level since 1988, but also in retail trade. If we add to this the fact that many prices are only reviewed once a year at the beginning of the year, we can expect a clear rise in underlying inflation at the beginning of 2023.

In addition, rising production costs should continue to support food and manufacturing inflation. Many companies are facing the first upward revision of their energy bills, which will push up costs. In addition, the four indexations of the minimum wage to inflation in 2022 will continue to lead to increases in all wages, which will push up inflation, particularly in services, significantly in 2023.

Ultimately, average inflation in 2023 will probably be higher than in 2022 (we expect 5.5% for the year, and 6.3% for the harmonised index), but the annual profile will be fundamentally different, with a peak above 6.5% in the first quarter, then a gradual decline from the summer onwards. At the end of 2023, inflation will probably still be above 4%, a level higher than the European average. The deceleration of price developments should continue in 2024 but will still be slow, averaging 2.6% over the year (3.5% for the harmonised index).

## Author

### Charlotte de Montpellier

Senior Economist, France and Switzerland

[charlotte.de.montpellier@ing.com](mailto:charlotte.de.montpellier@ing.com)

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