

# French inflation picks up as the economy stalls

Inflation has rebounded in France, as expected, while first-quarter activity data is deteriorating sharply. Taken together, this highlights a very real stagflation risk, directly linked to the Middle East conflict



A view of Paris from the Eiffel Tower

## Inflation rebounds

As anticipated, consumer prices rebounded in France in March, rising by 1.7% Year-on-Year after 0.9% in February. The harmonised index, closely watched by the ECB, stood at 1.9%, compared with 1.1% the previous month. This renewed increase in inflation is unsurprisingly linked to the situation in the Middle East. In the wake of higher oil prices, energy inflation jumped to 7.3% YoY, after a decline of 2.9% in February. The increase in gas prices is not yet reflected in consumer prices due to the structure of gas contracts.

Excluding energy, French inflation remains contained. Food price inflation slowed to 1.8% YoY from 2% the previous month. Prices of manufactured goods continue to decline, falling by 0.6% after a 0.2% decline in February. Services inflation edged up slightly to 1.7%, from 1.6% the previous month.

Overall, the conflict in the Middle East represents a major shock to the global economy and, by extension, to the French economy. The exact magnitude of the shock remains uncertain and will

depend on the duration and intensity of the conflict. But one thing is clear: each passing day increases the risks to both growth and inflation. The figures published today confirm that a first inflationary wave is already underway. After fuel prices, second-round effects via transport costs and certain industrial goods should not be long in coming. The key question now is whether this will remain a temporary shock or mark the beginning of broader-based inflation, with de-anchoring of inflation expectations and stronger wage demands.

## The risk of an inflationary wave is limited in France

The risk of an inflationary spiral nevertheless remains more limited in France than in the rest of the euro area. The starting point for inflation is lower than in most other European countries. The French economy is characterised by a large share of administered prices or prices negotiated in a centralised manner, particularly in large-scale retailing, which slows the pass-through of cost increases to consumer prices. In addition, economic conditions prior to the conflict were already weak, with constrained demand.

The labour market remains fragile: hiring intentions are low and net job creation has been negative for several quarters. Wage negotiations for this year do not incorporate this new inflationary shock. In this context, wage growth should remain more moderate than elsewhere, limiting price pressures, particularly in services. Even in the case of a “one-off” inflationary shock, however, French inflation should average around 2% in 2026, compared with a forecast of 1.3% for the harmonised index prior to the conflict.

## Economic activity engines are already under strain

Other data released today confirms that the risks weighing on French activity are significant. The year 2026 started on a slightly more optimistic note, but on fragile foundations. The first activity data for the beginning of the year is disappointing. Services production fell by 0.6% Month-on-Month in January. Retail sales volumes stagnated. Household consumption contracted sharply in February, down 1.4% on the month after an increase of 0.4% in January.

These indicators point to a weaker-than-expected first quarter and an already fragile starting point, even before the economic effects of the conflict fully materialise. Growth could therefore surprise on the downside as early as the first quarter, while the conflict will weigh on consumption, investment and production in the quarters ahead. In this context, GDP growth well below expectations at the start of the year now appears likely. Our March forecast of average growth of 0.7% for the full year (compared with 1% expected at the beginning of the year) now already looks optimistic.

At a time when the government was targeting a budget deficit close to 5% this year, based on GDP growth of 1%, this new shock risks once again weighing on tax revenues and further deteriorating public finances. Limited fiscal space significantly reduces the likelihood of large-scale support measures to cushion the rise in energy prices, unlike what happened in 2022.

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