

## The French economy is in recession and inflation has not yet peaked

A double whammy for the French economy: inflation continues to rise and reached 5.2% in May, while first-quarter GDP has been revised down. We believe the French economy is currently in recession and we are revising down our growth forecast for 2022



### Inflation will continue to rise

As expected, French inflation continued to rise in May, reaching 5.2% according to the national measure, up from 4.8% in April. Inflation according to the harmonised index, which is important for the ECB, reached 5.8%. As in previous months, inflation is primarily driven by energy prices, up 28% year-on-year, mainly due to higher oil prices. However, inflation is clearly becoming a widespread phenomenon, with food prices up 4.2% year-on-year, manufactured goods up 2.9% and services up 3.2%. In all major categories, inflation is therefore now above the ECB's 2% target.

The question for the next few months is when will inflation peak and how fast will it fall? We believe that inflation has not yet peaked, but is not far off. If oil and gas prices on the international markets do not increase too much more, inflation should start to decrease as early as this summer, but the decrease will be very slow and inflation will probably still be above 3.5% at the end of the year. We expect inflation to average 5% for the year, which will have a lasting impact

on household purchasing power.

## The French economy is in recession

In addition, GDP figures for the first quarter have been revised downwards significantly. Instead of the previously estimated stagnation, GDP actually contracted by 0.2% in the first three months of the year. The contraction is explained by a strong decrease in household consumption (-1.5%), particularly in transport equipment and manufactured goods. Despite the dynamism of investment (+0.6%), domestic demand contributed negatively to economic growth, to the tune of -0.6 points. The contribution of inventories (+0.2 points) and foreign trade (+0.2 points) cannot compensate enough to pull the French economy out of contraction. This bad news is compounded by the downward revision of annual growth for 2021 to 6.8% from the previously estimated 7%. This new profile leads to a marked revision of the carry-over effect for the rest of 2022: at the end of the first quarter, it now stands at 1.9%, compared to 2.4% at the time of the previous estimate.

Looking ahead, the news is not very encouraging. The data on consumption in volume of goods for the month of April, published by INSEE this morning, indicate a further decline in household consumption, of -0.4%. Both food consumption and consumption of manufactured goods are down over the month (-1.1% and -0.3% respectively). Only energy consumption increased (+0.7%), as a result of the more unfavourable weather conditions in April. The second quarter has thus started very badly for the consumption of goods. While the consumption of services is probably much more dynamic, it is likely that household consumption will again contribute negatively to growth in the second quarter, given the inflationary context and the decline in confidence. Consequently, a further contraction of GDP in the second quarter is expected. It means that, in our view, the French economy is currently in a de facto recession.

For the second half of the year, we expect a slight recovery. The third quarter should see a significant increase in tourism activity against the backdrop of the end of health restrictions and the return of foreign tourists, which should help to achieve quarterly growth of around 0.4%. The fourth quarter will probably be a little less dynamic. Given the various downward revisions, we are now expecting growth of 2.1% for the year as a whole (compared with 2.7% previously). This is therefore a significantly lower figure than the expected 4% that was used by the executive to establish the 2022 budget. With the recession, inflation at 5% and rising interest rates, the first months of the new government are likely to be more complicated than expected.

### Author

#### Charlotte de Montpellier

Senior Economist, France and Switzerland

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

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