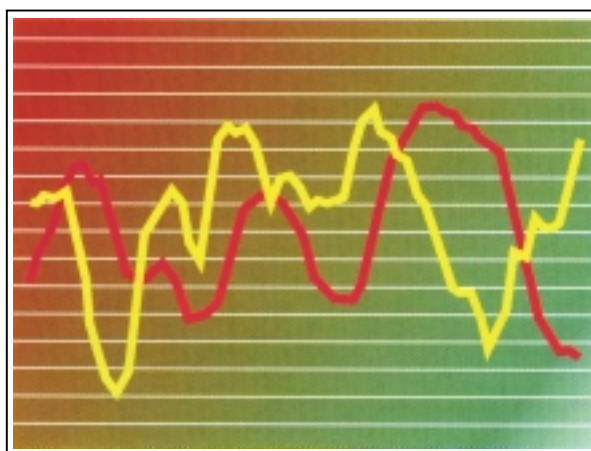


CONJONCTURE IN FRANCE

JUNE 1999



REBOUND

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REBOUND

The French economy slowed down in the past winter, in continuation of the tendency seen since the start of last year. The modest scale of the growth recorded in Q1 1999 (0.3%) was mainly due to stagnation in the industrial sector, which, after being particularly lively in the initial phase of the recovery, was then hit by the Asian crisis and its various knock-on effects. The sector was directly affected by the marked slowdown in world trade and indirectly by inventory adjustments and to a smaller extent by revisions in investment plans brought about, as in the whole of the euro zone, by the deterioration in the international climate. Throughout the period of slowdown in industry, growth was underpinned by the continuing firm tendency in domestic demand (excluding inventory changes) due mainly to brisk private consumption.

Recent months have seen the euro zone benefiting from an improved international climate. The Asian emerging economies are gradually putting the crisis behind them and giving renewed impetus to world trade. In Japan, the somewhat unexpected and probably only temporary rally in Q1 puts down the first marker of the end of recession. The United Kingdom economy, which had been slowing down considerably towards the end of last year, is reviving against a background of monetary relaxation. Growth remains brisk in United States, even if a probable downturn in consumption seems set to bring about a certain moderation.

In the euro zone, where domestic demand has shown considerable firmness in Q1, there has since April been an improvement in business leaders' expectations, especially regarding production prospects. This tendency varies in scale from country to country, with the economic situation still hesitant in Germa-

ny and Italy, but it is nevertheless general and seems justified by the firm tendencies shown by the main determinants of demand: strengthening world trade, a favourable exchange rate versus the dollar, households' expectations still positive despite a slight levelling off.

In France, the principal prop for household consumption remains growth in earned incomes linked to the expansion of employment. Employment itself, affected by the past slowdown in growth, has been rising somewhat less strongly. It is expected that 200,000 jobs will be created in the market sector this year (as against over 300,000 in 1998), corresponding to a rise of 300,000 in total numbers employed and producing a reduction of 0.4 of a point in the unemployment rate over the year. Meanwhile, purchasing power is no longer benefiting from disinflation. Because of the recovery on the commodity markets, the year-on-year price rise is expected to be 0.8% at the end of 1999, compared with 0.3% a year earlier. All in all, household consumption is expected to grow less strongly this year, reverting -- like real incomes -- to a growth rate close to 2%. This expectation is based on the cautious assumption that the saving ratio will remain unchanged. Moreover, this stabilisation would be offset by exceptionally lively investment on the part of households.

The improvement in expectations is reinvigorating corporate demand. Investment, which had never stopped rising, is gathering pace and inventory behaviour is being reversed. The result is a gradual recovery in GDP growth, from an annualised rate of slightly less than 2% in H1 to more than 2.5% in H2. On an annual average basis, GDP growth is expected to reach 2.2%.

Asia triggering a recovery in world trade

South-East Asia is gradually emerging from the crisis, although not all countries are at the same stage in the revival of activity. The recovery in output is unmistakable in Korea, slightly less so in Thailand and Malaysia. The stabilisation of exchange rates has not wiped out all the price-competitiveness gains achieved in 1997. At the same time, it has permitted an appreciable decline in inflation, which in turn has opened the way for an easing of monetary conditions. For the region as a whole, growth is expected to be of the order of 2%, compared with -6% last year. Imports into the zone, stimulated by corporate demand, are likely to gather pace as the year goes on. In Latin America, meanwhile, activity is liable to be affected by the consequences of the Brazilian financial crisis. However, the slowdown should be of limited duration and of smaller amplitude than the recessions seen in South-East Asia in 1998. Demand from the oil-producing countries could pick up again as a result of the rally in crude oil prices.

The upturn in South-East Asia should largely offset the effects of the South American slowdown on growth in world trade, of which emerging Asia and Latin America account for roughly 18% and 6% respectively. It would also be a factor tending to re-launch demand in the developed countries' export markets. The Central and Eastern European countries have been more affected by

the slowdown in the euro zone than by the crisis in Russia. The rest of the year can be expected to see a gradual revival in these countries' exports, combined with continuing firm domestic demand. In Russia, activity is liable to decline yet again this year.

Less firm growth in United States; stabilisation in Japan

American growth remained very buoyant until Q1 1999, but is expected to slow down gradually in the second half of the year, despite the recovery in exports as part of the revival in world trade. The main reason for the slowdown is that the growth factors in domestic demand are unlikely to remain as favourable as at present. Household purchasing power is set to grow more slowly than in previous years. On top of the slowdown in real earnings seen since the beginning of 1998, there is now likely to be a slowdown in employment growth as well. It is hard to see the saving ratio falling further and household consumption is therefore headed for a slowdown. These tendencies are liable to have an adverse effect on the demand outlook and corporate investment is then also likely to be less dynamic. All in all, GDP seems set to grow by around 3.5% in 1999, compared with almost 4% in 1998. However,

Gross domestic product (volume) by type of expenditure

(at 1995¹¹¹ prices, % change from previous period)

		1997				1998				1999				1997	1998	1999
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
GDP	(100%)	0.4	0.7	0.8	1.1	0.8	0.8	0.3	0.7	0.3	0.5	0.6	0.7	2.0	3.2	2.2
Imports	(23%)	0.5	2.6	4.2	3.2	2.6	1.5	0.3	0.2	-1.0	0.1	1.1	1.5	6.4	9.3	0.7
(of which merchandise)	(20%)	0.7	2.6	4.1	3.4	3.4	1.1	0.6	1.0	-0.8	0.0	1.1	1.6	6.7	10.3	1.4
Households' consumption	(54%)	0.1	0.1	0.7	1.6	0.6	1.3	0.5	0.7	0.2	0.5	0.5	0.6	0.2	3.6	2.1
General government consumption	(23%)	0.3	0.7	0.2	0.3	0.2	0.2	0.0	0.4	0.5	0.5	0.5	0.5	1.6	1.0	1.6
Total investment (GFCF)	(19%)	-1.3	1.6	1.0	1.5	0.9	1.7	1.3	1.4	2.2	0.1	1.1	1.3	0.5	5.3	5.2
Corporate sector	(10%)	-0.9	2.2	1.2	1.8	1.4	1.4	2.2	0.8	2.0	0.8	0.8	1.1	1.3	6.3	4.2
Households	(4%)	-1.7	1.4	1.4	0.2	-0.8	3.0	-1.6	2.8	3.5	0.2	1.7	1.8	0.7	2.5	7.1
Exports	(26%)	2.3	3.8	3.8	2.9	0.8	0.8	1.6	-1.4	-1.1	0.7	0.7	1.0	10.6	6.9	0.0
(of which merchandise)	(21%)	2.2	4.2	4.0	3.0	1.5	0.4	2.0	-1.4	-1.0	0.6	0.5	1.0	10.4	7.8	0.0
Domestic demand		0.0	0.4	0.8	1.2	1.2	1.0	0.0	1.2	0.4	0.4	0.7	0.8	0.9	3.7	2.4
Contributions to the growth of GDP																
Inventory changes		0.1	-0.1	0.2	-0.1	0.7	-0.1	-0.6	0.4	-0.3	0.0	0.1	0.1	0.3	0.4	-0.2
Trade in goods and services		0.4	0.4	0.0	0.0	-0.4	-0.1	0.3	-0.4	0.0	0.1	-0.1	-0.1	1.1	-0.3	-0.2
Domestic demand excluding inventories		-0.1	0.5	0.6	1.2	0.5	1.1	0.5	0.7	0.7	0.3	0.6	0.7	0.6	3.1	2.5

(1) National Quarterly Accounts evaluate growth at 1995 prices and adjusted for calendar effect. Growth rates are usually slightly different once calculated at the prices of the preceeding year.

Forecasts

the slowdown will gather pace as the year goes on, with the annualised growth rate in H2 no more than 2% -- perhaps even less in the event of a stock-market crisis.

Activity in Japan, after a first quarter whose strength has surprised observers, is unlikely to pick up other than very gradually. Excess productive capacity seems likely to prompt firms to hold back on investment and cut their workforces. The steep increase in unemployment, from a rate of 3.5% to 5% in little more than a year, and the continuing decline in earnings will hold down household purchasing power. This means that after a spurt in Q1 due to exceptional factors, consumption is likely to be lacklustre for the rest of the year. This leaves only two factors capable of propping up growth: first, public spending on construction and public works is likely to remain strong; second, exports can be expected to benefit from the strengthening in the economies of Japan's regional partners, despite the delayed effects of the appreciation in the yen which has now been going on steadily since the summer of 1998. All in all, activity is likely to be sluggish for the rest of the year, with GDP showing only a modest annual-average rise.

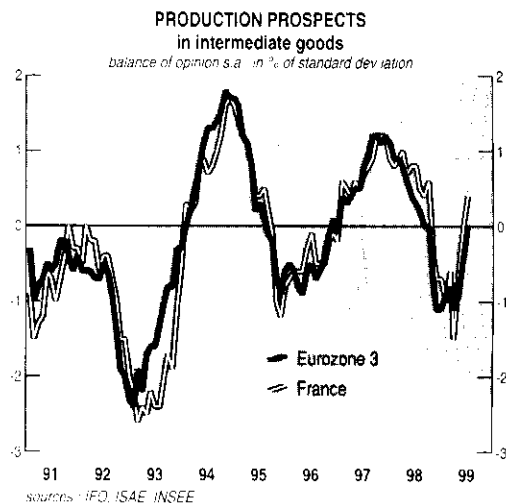
Industry reviving in the United Kingdom...

In the United Kingdom, where monetary policy has been substantially eased since October 1998, the downswing in activity seen last year seems to be coming to an end. It is nevertheless still having an adverse effect on the rate of job creation -- as a result, the unemployment rate has been stable for the past year despite a decline in the labour force. This tendency is likely to help ease the continuing strong wage pressures. At a time of renewed price rises, household consumption is expected to be less dynamic in H2. However, this slowdown in the autumn would be offset by the recovery in exports, fuelled by demand from the euro zone. Given this more favourable international environment and despite the past appreciation of sterling, business leaders' expectations have been improving again in the past few months and this should make it possible for productive investment to pick up and also encourage stock-building.

... and in the euro zone

In the euro zone, industrial activity can be expected to pick up in 1999 following the past winter's lull. This is because the acceleration in world demand during the year should breathe new life into exports, whose weakening had in mid-1998 triggered off the industrial slowdown. An additional factor favouring exports would be the more favourable exchange-rate situation since the end of 1998. The revival in euro-zone exports would in turn lead to increased inter-industry exchanges within the zone. The recent improvement in order books for intermediate goods would suggest that this upturn has already begun.

The improved export outlook would provide additional support for corporate demand. Productive investment should continue to rise. For the past few months, firms in the capital goods branch have been predicting a



"Eurozone 3" (France, Germany, Italy) stands for more than 75% of industrial output of the eurozone.

recovery in their activity. Against this background of more dynamic demand and firmer producer prices linked notably to the rally in the oil price -- firms are likely to adopt inventory behaviour that is more favourable to growth. However, stock-building is likely to be delayed in Germany, where business leaders still tend to see their inventories as being too large.

All in all, with industrial output reviving in Q2, GDP growth is expected to accelerate from less than 1.5% this past winter to almost 2.5% by the end of the year. Growth on an annual average basis should be in the range 1.5-2%.

Firm household consumption in Europe

In general, household consumption was firm until the beginning of 1999 and is expected to remain strong for the rest of the year, continuing to rise at an annualised rate of more than 2%. In Italy, however, household consumption was weak during the winter and is likely to be slow to pick up again. Italy did not benefit as much as its euro-zone partners from the industrial recovery in 1997-1998 and the situation on the Italian labour market has improved only marginally. In addition, it was temporarily affected by a deterioration in household confidence linked to the Kosovo conflict.

Employment rising somewhat less strongly in France

Growth in earned-income employment in the French market sector, which was strong early in the year despite the slowdown in activity, seems to have weakened in Q2. It should nevertheless recover again later in the year, given the improved growth outlook. The contraction in the industrial work-force that began in Q1 seems set to continue. Numbers employed in the tertiary sector, after slowing down in Q2 as the result of weaker demand for temporary-agency workers, should gradually pick up again, while the building sector is likely to accelerate recruitment. As a consequence, employment in the traded sector is expected to rise by 200,000 in 1999 (compared with over 300,000 in 1998) and total

employment by slightly more than 300,000. This would mean that the unemployment rate would continue to decline, although not as fast as in 1998 -- by 0.4 of a point, compared with the 1998 decline of 0.8 -- and reach roughly 11.1% in December 1999.

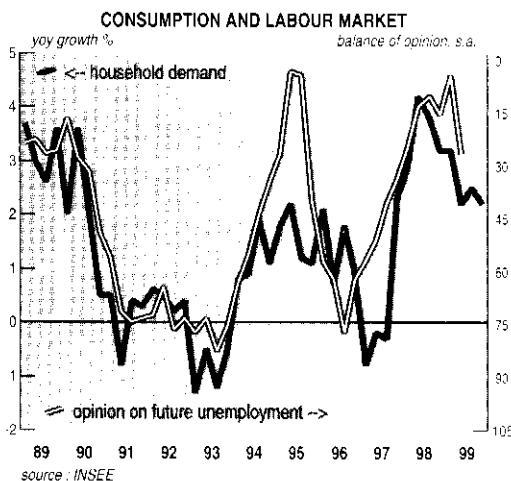
Continuing solid growth in real incomes...

Wages and salaries, given the low inflation in 1998 and the cautious behaviour on the part of firms now negotiating a shortening of working hours, are likely to follow the same path as previously. The largely unexpected disinflation seen at the end of 1998 had contributed to growth in the purchasing power of household incomes. For the year as a whole, purchasing power is likely to move much as it did last year (rising by around 2.7% on an annual average basis). However it could well now slow down gradually as a result of the levelling off in job creation and the slight acceleration in prices due mainly to the recovery in oil prices (with the year-on-year price rise increasing from 0.5% in June to 0.8% by the end of the year). In H2, growth in the purchasing power of households' gross disposable income is expected to be around 2% (annualised rate).

... and in household demand

The strength of consumption therefore has a solid underpinning. Apart from the growth in purchasing power, the general environment still seems favourable to consumption. Households remain extremely confident, heartened by the favourable situation on the labour market. One special feature is likely to be continued strong growth in purchases of computer equipment and telephones. Following weak growth in Q1, partly due to exceptional factors, consumer spending is likely to rise at an annualised rate of slightly more than 2% in the rest of the year.

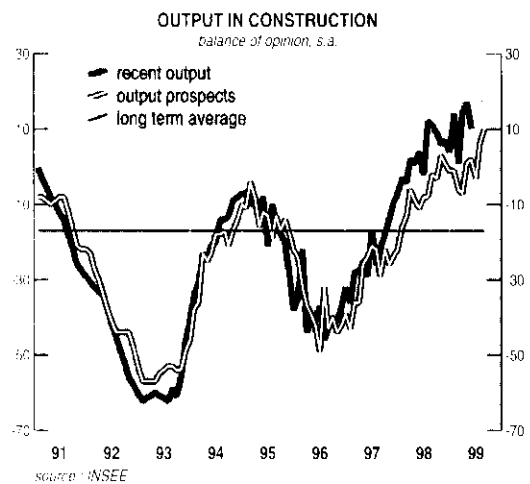
While consumption, although remaining fairly brisk, is slowing down in parallel with incomes, private investment in housing is still rising strongly following the acceleration seen towards the end of last year. With borrowing conditions extremely favourable, housing investment can be expected to grow in H2, as in the



previous half-year, at an annualised rate of well over 5%, bolstered by expectations of price rises and by the firmness of incomes.

Construction expanding strongly

The building and public works sector has therefore found strong support from housing investment in the past year, but also from corporate investment. Both construction and maintenance/renovation have posted strong growth. The outlook for H2 remains very favourable, so that output looks set to rise at an annualised rate of 5%. Investment by both households and firms can be expected to remain firm, as shown by the sharp rise in building permits.



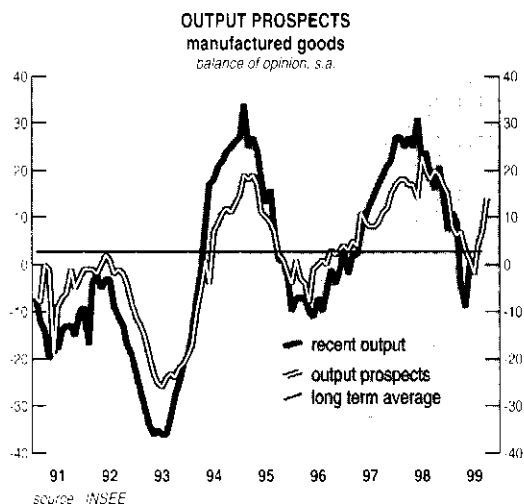
Revival in industry

In contrast to the construction sector, industry showed virtually no growth in Q1, as a result of the levelling off in inter-industry exchanges in Europe and the adjustment in corporate demand. In Q2, however, there were numerous signs indicating that industry might again be benefiting from following winds in H2. The upturn in world demand -- especially in inter-industry exchanges within the euro zone -- is likely to re-prime the growth pump. The result would be an upturn in corporate demand (inventories and investment). The stock-rebuilding would reinforce the first signs of upturns in demand and in prices now being seen in the intermediate goods sector. In the case of capital goods, production would respond to the acceleration in investment but would initially suffer from the involuntary accumulation of inventories seen in Q1. Consumer goods are likely to benefit from the firmness of consumption in France and in its principal partner countries. The car sector, after very strong activity in 1998, is likely to record less brisk growth, although still boosted by production of heavy goods vehicles. After stagnating in the winter, manufacturing output should gradually gather speed: at annualised rate, growth in output should rise from slightly over 1% in H1 to around 2.5% in H2.

In the early months of 1999, services have been affected by the slowdown in industry and, to a smaller extent, by the temporary weakness of household spending. However, signs of recovery are to be seen in the business survey for Q2. In H2, the revival in manufacturing activity should produce an improvement in the business services sector (with an annualised growth rate of almost 3%, compared with roughly 1.5% in the previous half-year). As regards services to households, the rise in activity is likely to level off (2%, annualised). Transport activity should improve in line with industry.

Revival in corporate demand

As in the rest of the euro zone, inventories can be expected to rise, in response to the steady acceleration in demand and the expectations of price rises. However, the resulting contribution to growth is likely to remain limited, given that there was relatively little de-stocking during the winter. The improvement in demand expectations seen in Q2 and the favourable borrowing conditions should permit a revival in investment, whose annualised rate can be expected to rise from less than 2% in H1 to almost 4% thereafter. Given the less favourable profit situation resulting from the rise in commodity prices and, to a smaller extent, in wage costs, the growth in investment could nevertheless remain limited.



GDP to accelerate in the second half of the year

Exports are likely to accelerate gradually, boosted by the upturn in world demand and especially in European industrial demand. The intensification of trade within the euro zone, combined with the recovery in expectations, should help corporate demand to pick up again. Household demand (investment and total consumption) is likely to remain firm. Imports would be stimulated by domestic demand. All in all, GDP growth seems set to gather speed gradually, from slightly less than 2% annualised in H1 to over 2.5% in H2. On an annual average basis, GDP growth is expected to reach 2.2%. ■