

CONJONCTURE IN FRANCE

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STILL NO IMPETUS

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Still no impetus

As forecast in October's Conjoncture in France, the advanced economies accelerated slightly in Q3 2012 (+0.2% after +0.1%). This overall trend hides some wide divergences: activity accelerated clearly in the United States and United Kingdom, while it contracted again in the Eurozone and fell in Japan.

In Q4 2012, activity is likely to stall in the advanced economies (0.0%), under the effect of the return to normal in the United Kingdom and a backlash in the United States. It should contract in the Eurozone (-0.3%) and in France (-0.2%). The business tendency surveys show no clear improvement in the business climate over the last few months and the first available activity data even suggests a fall in activity, partly as a backlash after the upturn in manufacturing production in Q3.

Demand, however, both internal and external, seems to be holding up to some extent. The business tendency surveys do not suggest that there is likely to be a fall in corporate investment and the available consumption data is close to stable, seeming to confirm that the fall in household purchasing power should be softened by a reduction in their savings ratio. To meet this demand, entrepreneurs are likely to accentuate their destocking.

Demand should continue to hold up like this in France through H1 2013, enabling activity to progress again slightly in H1 2013 (+0.1% per quarter).

Exports should accelerate somewhat, under the effect of the upturn in world demand and the past depreciation of the Euro. Under the hypothesis that there is an agreement in the United States to limit the scale of the "fiscal cliff", the advanced economies should start up again gradually in early 2013 (+0.2% then +0.3% in Q1 and Q2). On the one

hand, internal demand in the Eurozone should stop falling, as financial tensions ease and fiscal policies take a less restrictive course. In addition to this, the emerging economies should accelerate slightly, due among other things to the past easing of monetary and fiscal policies.

Internal demand should again be sluggish in France, notably household consumption. After progressing sharply at the end of 2012, taxes on households should stop rising in H1 2013, but earned income should continue to slow down. The return of spontaneous productivity gains to their pre-crisis rate, which started at the end of 2011, should lead to considerable market-sector job losses (a little under 40,000 per quarter in early 2013). The fall in total employment should be a little slower, however, due to an increase in the number of subsidised jobs in the non-market sector. The unemployment rate should reach 10.9% in mid-2013 (10.5% in Metropolitan France).

Beyond its quarterly fluctuations, purchasing power should follow a downward trend (-0.2% year on year in Q2 2013), although this fall should remain sufficiently moderate for that in the household savings ratio to allow household consumption to be maintained.

There are various uncertainties that go with this scenario. The investment ratio of French companies is currently relatively high. A pronounced downward adjustment, which is not in our scenario, is therefore possible, even if nothing in the surveys suggests any advance signs of this. On the other hand, the French economy could benefit from stronger external support than expected if the acceleration underway in the emerging countries should increase its scale or if the easing of financial tensions on financial markets in the Euro Zone should defrost consumer and corporate spending behaviour quickly.

In Q3 2012, activity progressed weakly in the advanced economies

The United States on a roll

In Q3 2012, activity progressed at a modest rate in all the advanced economies (+0.2% after +0.1% in Q2 2012), with sharp contrasts between countries. For example, it accelerated significantly in the United States (+0.7% after +0.3%), buoyed by dynamic domestic demand.

An upturn in Britain, a fall in Japan

After falling for three quarters, the British economy rebounded strongly (+1.0% after -0.4%), benefitting from a one-off boost from the additional activity linked to the backlash after the Queen's Jubilee and to the Olympic Games. The Japanese economy, meanwhile, fell sharply (-0.9% after 0.0%). Household consumption fell with the end of the subsidies to buy vehicles, while Japanese exports were hit by the general slowdown in Asian trade and diplomatic tensions with China at the end of the quarter.

Activity progressed in France and Germany, but fell in Italy and Spain

In the Eurozone, activity fell slightly in Q3 2012 (-0.1% after -0.2%). Domestic demand continued to decline, but exports progressed clearly, notably in Germany and Spain. In Q3 2012, activity progressed in France (+0.2%) and in Germany (+0.2%) but fell again in Spain (-0.3%) and in Italy (-0.2%), although at a lesser rate than in the previous quarter.

World trade decrease in Q3 2012

World trade fell slightly in Q3 2012 (-0.2%), hit by sluggish conditions in advanced economies and emerging economies. The emerging Asian economies have continued to slow down over the summer and trade in the region contracted significantly between June and August 2012. It did rebound in September, however.

Advanced economies sluggish in Q4 2012

Business climate poor in Europe and Japan

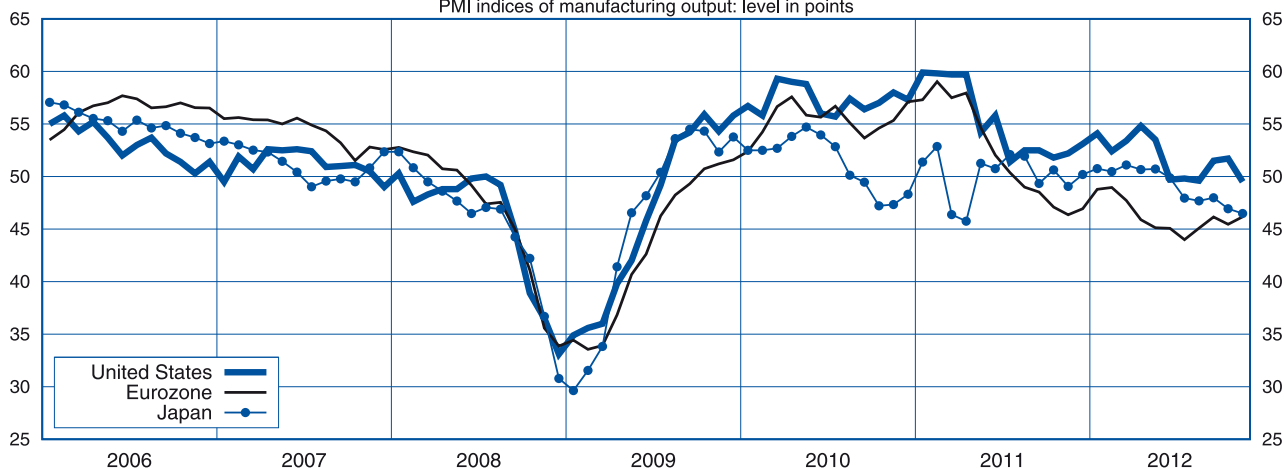
In November 2012, the business climate was still well below the expansion threshold in Japan and in the Eurozone (see graph 1). In both these economies, activity should therefore continue to slip back in Q4: -0.2% in Japan and -0.3% in the Eurozone.

The US economy hits the brakes at the end of 2012

In the United States, the business climate took a downturn in November, although it did remain at the expansion threshold. The US economy is therefore unlikely to remain at the sustained rate it had in Q3 (+0.3% in Q4 2012 after +0.7%) but it should continue to be driven by domestic factors, notably private consumption and investment in construction. Hurricane Sandy, which hit the East Coast of the country at the end of October, is likely to detract from activity in the United States.

1 - Business climate poor in the Eurozone

PMI indices of manufacturing output: level in points



Sources: Markit, ISM

Stagnating world trade

The activity of the advanced economies is likely to stall in Q4 2012 (0.0%) and world trade is unlikely to grow (0.0%). Export orders as tracked by purchasing manager surveys (PMI) remain weak, even though the emerging economies are showing signs of acceleration. In China, notably, the rate of progression of industrial production has been increasing for several months.

In early 2013, the United States should avoid the worst and world activity become more dynamic

The upturn should be confirmed in early 2013 in the emerging economies

Activity in the emerging economies should firm up in early 2013. In China, the easing of monetary policies over the last few months and public infrastructure financing programmes should provide a boost. In the wake of China, the other Asian economies are likely to accelerate in turn. Imports in the emerging economies are therefore likely to become more vigorous and progress by 1.2% per quarter in H1 2013.

A fiscal agreement in the United States?

As US legislation currently stands, tax rises and spending cuts must come into force on 1st January 2013, representing an amount of around 4.7 points of GDP. For households, the shock would represent about 4.6 points of their disposable income. However, our scenario is based on the hypothesis that the US authorities come to a compromise limiting the tax hikes to about 1 point of household income. They should also decide not to apply all the automatic spending cuts.

American activity should hold up

US households and enterprises should also show a great capacity to hold up in the face of this fiscal shock. The tax rises should mainly concern the wealthiest households which will be able to soften their effects by reducing their savings ratios. Enterprises have very high margins and should therefore offset part of the rises in payroll taxes. They should also benefit from lending conditions that remain favourable in order to increase their investment expenditure. Finally, the slowdown in inflation should boost household purchasing power and production is likely to rebound clearly in the regions hit in the previous quarter by Hurricane Sandy. Activity in the United States is therefore likely to grow in Q1 2013 at a moderate rate (+0.4%) and then to return to a slightly higher growth rate in Q2 2013 (+0.5%).

Rebound in Japan

In Japan, the fall in activity is unlikely to continue into early 2013 and the economy should progress again (+0.3% per quarter). Exports should profit from the acceleration in world trade and private demand should become more dynamic again, notably investment. The United Kingdom, after the ups and downs of H2 2012, should settle into a weak growth rate. British domestic demand should continue to be held back by continuing fiscal consolidation efforts and exports are likely to suffer from weak activity in the rest of Europe.

Eurozone: towards better days

Financial tensions have eased

With the announcement by the European Central Bank (ECB) of the launch of its sovereign debt buying programme, tensions on European sovereign debt have eased distinctly since summer 2012. Financing of private agents remains difficult, however: reduced uncertainty on the European sovereign debt market has not been passed on to the bank lending market, and lending terms tightened on the whole in Q3 in the Eurozone. The rates granted to non-financial enterprises in Spain and Italy have taken a downward turn since the summer, however. Over the forecasting period, the continued easing of sovereign debt tensions, backed by the inter-governmental agreement of 4 December 2012 on Greek debt, should lead to an improvement in financing terms in the Eurozone.

General outlook

Eurozone fiscal consolidation eases slightly in 2013

In response to sovereign debt market tensions and in accordance with their commitments, most European States are implementing major public deficit reductions. Fiscal consolidation is likely to continue in 2013, but should be less intense on the whole than the previous year for the Eurozone as a whole. In Italy, the overall tax hikes, including indirect taxes (VAT), should ease significantly in 2013. In Spain, however, consolidation is set to continue at the same rate as in 2012 and it should be stepped up in France.

Activity set to fall at the end of 2012...

Activity is set to fall again in the Eurozone in Q4 (-0.3%). According to the activity data available through to October, manufacturing production would appear to be collapsing: GDP is set to contract in the four major Eurozone economies.

... then should stabilise in early 2013

Activity should stabilise at the start of 2013 (0.0% in Q1 2013 then +0.1% in Q2 2013). On the one hand, the European economy is likely to profit from the acceleration in demand from its partners and the book contribution of foreign trade to growth should remain positive for the forecasting period. On the other, internal mechanisms should also favour a levelling out of activity. The fall in household purchasing power should be attenuated in early 2013 thanks to the easing of inflation and the fiscal consolidation effort, and household consumption is likely to stabilise in early 2013. In addition to this, after adjusting sharply since 2011, corporate investment should level out. This stabilisation should be favoured by the progressive improvement in credit access terms and by the upturn in prospects for activity.

Trajectories still diverging

The trajectories of the different Eurozone countries are nonetheless likely to remain divergent (see *graph 2*). In Germany, the domestic drivers are likely to be more powerful than in the other countries, notably household consumption and investment in construction. After falling in Q4 2012, German activity should rebound in early 2013. In Italy, activity should fall back again at the end of 2012 and beginning of 2013, but then stabilise in Q2 2013. In Spain, however, the rate of contraction of activity is unlikely to ease.

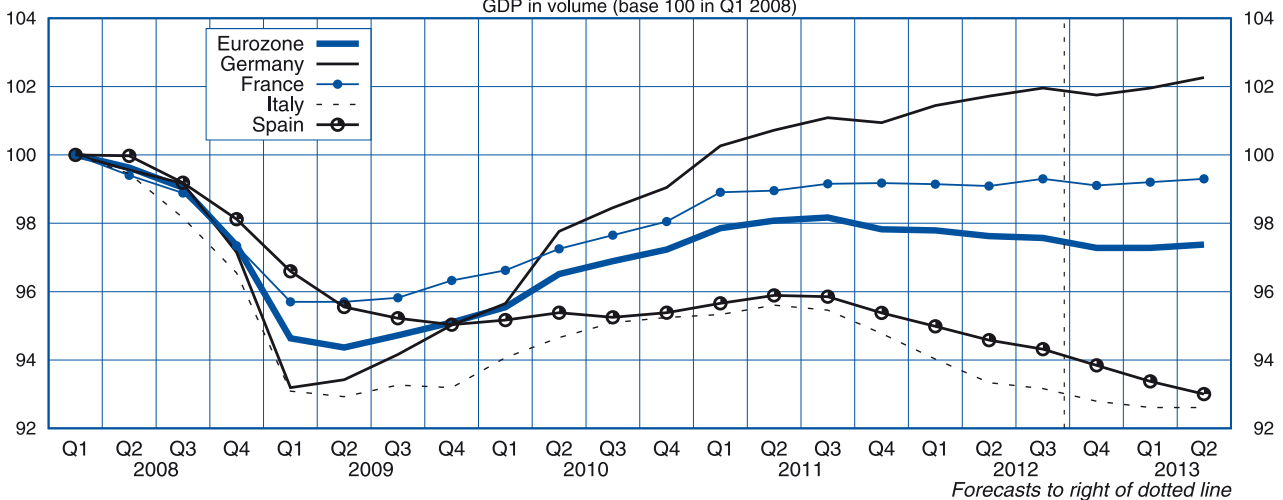
Backlash in France in Q4 2012

Activity progressed in France in Q3 2012

Activity saw an upturn in France in Q3 2012 (+0.2% after -0.1% in Q2 2012). In particular, manufacturing production rebounded distinctly (+1.0% after -1.0%), notably in the coke and refined petroleum products sector, in manufacturing of transport equipment and in that of capital goods. Driven by dynamic manufacturing activity and also sustained by the buoyancy of household

2 - Divergence in the Eurozone

GDP in volume (base 100 in Q1 2008)



Source: Eurostat, INSEE calculations

spending on services, production of market services accelerated (+0.4% after +0.1%). Activity in construction, however, only progressed slightly (+0.1% after +0.5%) and energy production fell (-1.4% after + 2.2%).

Demand firmer

On the demand side, activity was buoyed up by exports (+0.5%) and by the rebound in household consumption (+0.3% after -0.2%). Household spending on manufactured products, in particular on clothing-textiles, progressed distinctly, while their energy consumption fell. Finally, investment of non-financial enterprises fell slightly (-0.4%).

The business tendency surveys settled at a low level in November

In services and industry, the business climate remained weak in November, well below its long-term average (see graph 3). In manufacturing industry, business leaders' assessments of their personal production prospects have been stable since the summer and order books saw an upturn in November, after falling sharply in October. According to the tendency surveys, activity should remain weak.

Activity to fall at the end of 2012...

Activity should thus fall in Q4 2012 (-0.2%), notably because manufacturing production is set to fall back distinctly (-1.5%). Not only is the business climate in industry weak, but production data available through to October suggests a marked fall in manufacturing production: the growth overhang at the end of October for Q4 stood at -2.5%. This drop in manufacturing activity should have negative knock-on effects on the rest of the economy and production should fall in practically all sectors of activity (see graph 4). Like in the previous quarter, both internal and external demand should hold up to a certain extent, and business leaders are likely to step up their destocking to serve it.

... before rising in early 2013

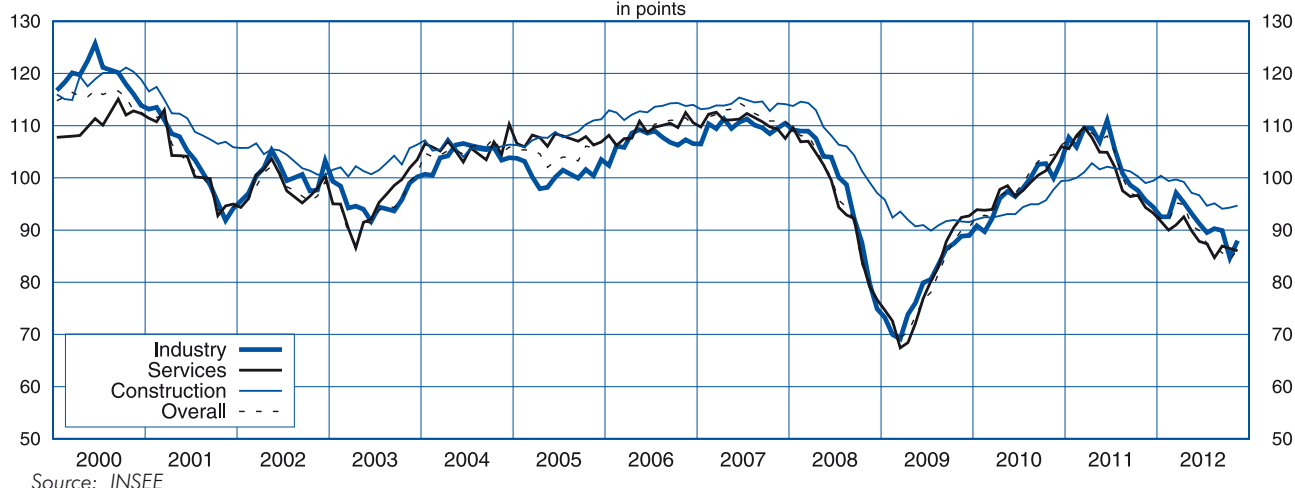
This buoyancy in demand should enable manufacturing production to level out in H1 2013 and service activity to become more dynamic. However, production in construction should fall distinctly by mid-2013. All in all, activity should progress at a modest rate in H1 2013 (+0.1% per quarter).

The labour market continues to deteriorate

Market-sector employment down sharply

Despite a slight upturn in activity in Q3 2012, employment in the non-agricultural market sectors fell sharply (-42,000). With activity weak, the situation on the employment market is likely to continue worsening through to mid-2013: on average, 40,000 jobs a quarter are likely to be lost over the forecasting period. The return of spontaneous productivity gains to their pre-crisis rate, which has been underway since the end of 2011, is likely to weigh down on employment

3 - The business tendency surveys settled at a low level
in points



Source: INSEE

General outlook

(see graph 5), but the fall in market-sector employment should be attenuated by the first effects of the tax credit for competitiveness and employment (CICE). The fall in total employment should be lower, as employment in non-market sectors should be buoyed up by an increase in the number of subsidised jobs.

Unemployment rate set to reach 10.9% in mid-2013

The unemployment rate stood at 10.3% of the labour force in Q3 2012 (9.9% in Metropolitan France). It should continue its rise over the forecasting period, reaching 10.5% at the end of 2012 and 10.9% in mid-2013 (respectively 10.1% and 10.5% in Metropolitan France).

Purchasing power to fall in 2012

Inflation at a low level

The high level of unemployment and limited degree of utilisation of production capacities should continue to hold back inflationary pressures, although the progression in food prices further to the rise in commodity prices since the start of 2012 should continue. Also, with the stabilisation of the price of Brent at around \$105, energy prices should increase little. All in all, headline inflation should be stable at 1.4% in June 2013 after 1.4% in November 2012.

Earned income should continue to slow down through to mid-2013

The deterioration in the labour market is weighing down on wage negotiations and, in the absence of a new boost, the rise in the minimum wage should be limited in January 2013. Therefore, real wages are likely to stagnate over the forecasting period and gains in nominal wages should slow down, causing a slowdown in earned income in H2 2012, then again in H1 2013.

Taxes to increase sharply in H2 2012...

The measures passed for 2012 in the initial Finance Law and Amending Finance Law induce rises in the tax burden by about 1 point of household income over the year. A large part of these measures, and notably those relating to income and wealth tax, should affect household income in H2 2012, and the taxes paid by households are therefore likely to rise sharply.

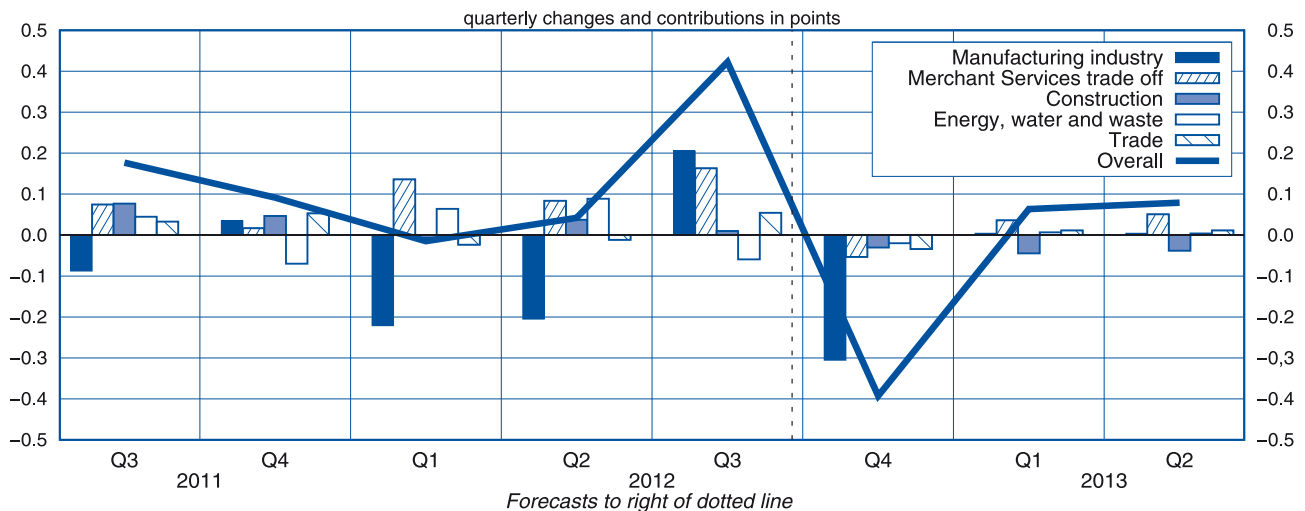
... then level out in early 2013

The new measures introduced by the draft Finance Law for 2013 should be similar in scale. But like in 2012, they will mainly come in the second half of the year and taxes should therefore level out in early 2013.

Ups and downs in purchasing power

Due to the tax payment calendar, the half-yearly profile of purchasing power will show ups and downs. It should fall in H2 2012 (-0.3%) then rise again in H1 2013 (+0.3%). Over 2012 as a whole, purchasing power should fall (-0.2%).

4 - In Q4 2012 manufacturing production is set to fall back distinctly



Source: INSEE

Household consumption sluggish

Consumer spending stable

Households tend to smooth out the consequences of ups and downs in their purchasing power on their consumer spending, and the quarterly trends in that consumer spending should therefore be much less uneven than those in purchasing power. Spending should fall slightly in Q4 2012 then level out in early 2013.

The savings ratio falls unevenly

In H2 2012, consumer spending should therefore progress more quickly than purchasing power, while the savings ratio should fall significantly. Conversely, the rebound in purchasing power in early 2013 should lead to a rise in purchasing power, standing finally at 16.1% in mid-2013, 0.4 points below its level one year previously. The new tax measures are likely to have their effect mainly on income that generally goes into short-term savings.

Investment slips slightly

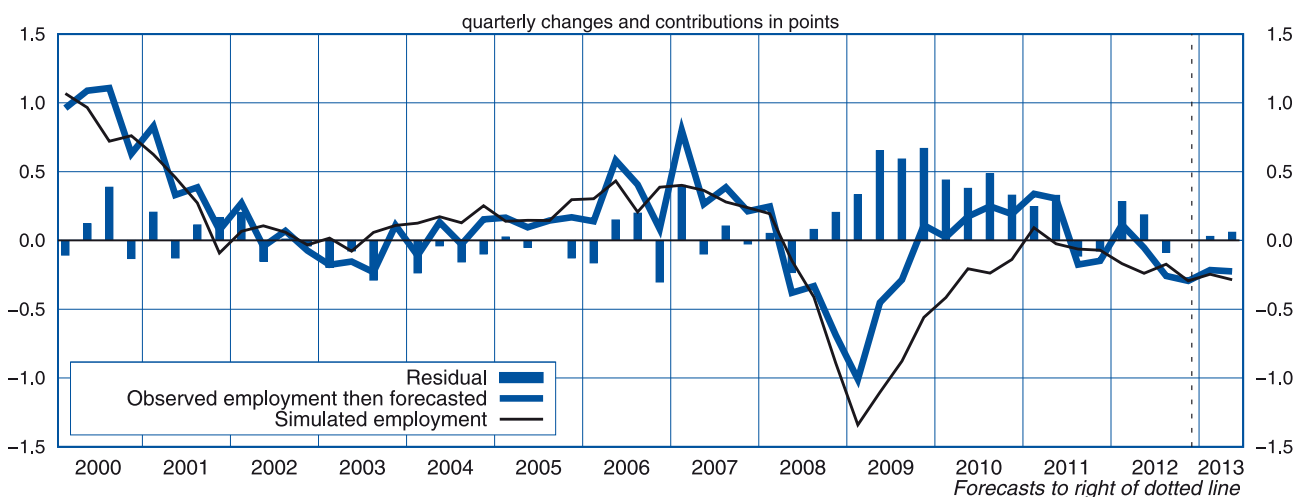
Investment in building down

Due to completion times in this sector, investment in building has been buoyed since the beginning of the year by the peaks observed in housing starts at the end of 2011. But starts in individual and collective housing have been falling since the beginning of the year and activity in building should therefore drop off from Q4 2012.

Corporate investment weak

Investment by non-financial enterprises should continue to fall in Q4 2012 (-0.3%), before stabilising gradually in H1 2013. The context should remain uncondusive towards investment: prospects for activity are poor and the utilisation rate of production capacities in the manufacturing branch is at a very low level. In addition to this, although lending terms have stabilised since the summer and private interest rates have fallen, the deterioration in the financial situation of companies is likely to hold back their investment effort.

5 - The labour market to deteriorate



How to read it: The equation residual for employment is the spread between the observed employment growth rate and the simulated employment growth rate. A positive residual, such as that observed at the beginning of 2011, indicates that observed employment showed better growth than past behaviour would lead us to expect.

Source: INSEE

Foreign trade holds up

Exports should accelerate slightly

Demand for French products should continue to be marked by the fall in activity in Spain and Italy and should therefore be less dynamic than world trade. However, it is likely to benefit from the upturn in German and extra-European demand and exports should therefore accelerate slightly through to mid-2013.

Uncertainties: corporate investment, US public finances, rebound in world trade

Corporate investment

Despite the deterioration in their financial situation (and notably the very sharp drop in their margin ratios) and uncertainty as to the duration of the crisis, the investment rate is relatively high today, at its 2007 level. Consequently, the capacity utilisation rate is well below its long-term average in manufacturing industry. A downwards adjustment of corporate investment is therefore possible, even though there is nothing in the short-term data and tendency surveys among enterprises providing any advance signs of it.

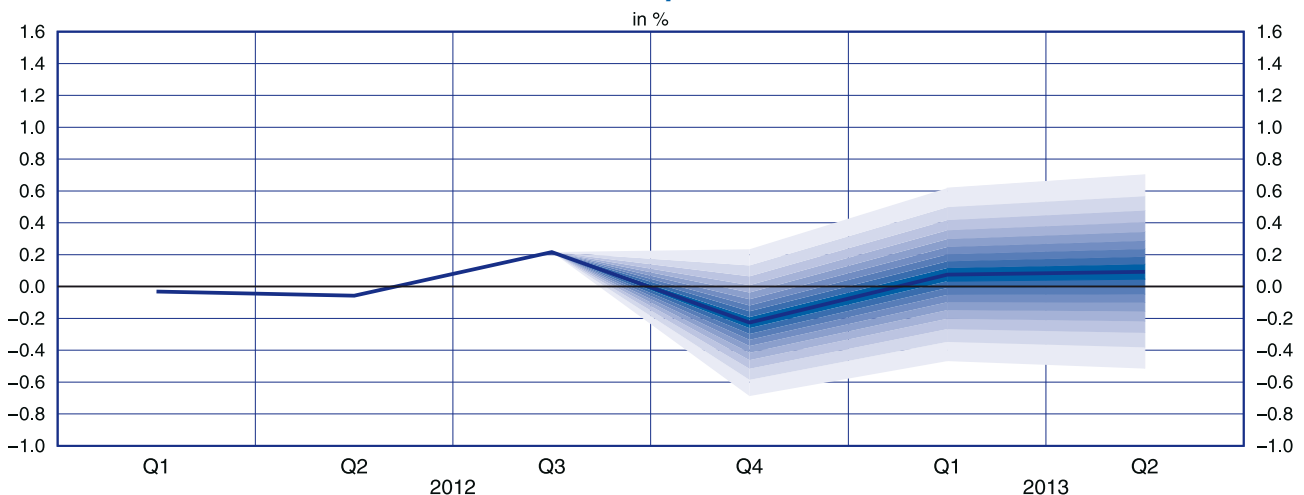
American public finances

We cannot rule out the possibility that the agreement found by the US authorities on the start-of-year fiscal shock might be less favourable to activity than that in our forecast, or there might even be no agreement at all. In this hypothesis, the US economy would be held back significantly at the start of 2013, which would have an impact on world demand for French products, thus holding back activity in France.

Rebound in world trade

Conversely, the acceleration in the emerging countries since the summer could be greater than expected. Likewise, easing tensions recorded on Eurozone financial markets since this summer could, if the trend continues, liberate spending behaviour more rapidly in the Eurozone. The French economy could then benefit from greater external support than expected here. ■

6 - Fan chart for Conjoncture in France



How to read it: the fan chart plots 90% of the likely scenarios around the baseline forecast (blue line). The first and darkest band covers the likeliest scenarios around the baseline, which have a combined probability of 10%. The second band, which is a shade lighter, comprises two sub-bands just above and just below the central band. It contains the next most likely scenarios, raising the total probability of the first two bands to 20%. We can repeat the process, moving from the centre outwards and from the darkest band to the lightest, up to a 90% probability (see *INSEE Conjoncture in France* for June 2008, pages 15 to 18). It can therefore be estimated that the first result published by the quarterly accounts for Q4 2012 has a 50% chance of being between -0.4% (lower limit of the fifth band from the bottom) and 0.0% (upper limit of the fifth band from the top). Likewise, it has a 90% chance of being between -0.7% and +0.2%. In Q1 and Q2 2013, the 90% confidence intervals is [-0.5% ; +0.6%] and [-0.5% ; +0.7%].

Source: INSEE

Key figures: France and its international environment

seasonally adjusted / working-day adjusted data (except for prices), quarterly or annual averages, as a %

	2011				2012				2013		2011	2012	2013 ovhg*
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2			
International environment													
Advanced economy GDP	0.0	0.3	0.6	0.3	0.4	0.1	0.2	0.0	0.2	0.3	1.3	1.2	0.6
Eurozone GDP	0.6	0.2	0.1	-0.4	0.0	-0.2	-0.1	-0.3	0.0	0.1	1.5	-0.4	-0.2
Barrel of Brent oil (in dollars)	105	118	113	109	118	110	109	109	105	105	111	111	105
Euro-dollar exchange rate	1.37	1.44	1.41	1.35	1.31	1.28	1.25	1.29	1.29	1.29	1.39	1.28	1.29
World demand for French products	1.6	0.4	0.8	-0.5	0.0	1.0	0.8	-0.2	0.6	0.6	5.9	1.2	1.6
France - supply and use													
GDP	0.9	0.1	0.2	0.0	0.0	-0.1	0.2	-0.2	0.1	0.1	1.7	0.1	0.1
Imports	3.5	-0.9	-0.1	-1.2	0.5	1.6	-0.6	0.3	0.6	0.7	5.2	0.2	1.4
Household consumption	0.0	-0.8	0.3	-0.1	0.1	-0.2	0.3	-0.1	0.0	0.0	0.2	0.0	0.1
Public and NPISH consumption	0.0	0.0	0.2	0.2	0.5	0.4	0.4	0.4	0.4	0.3	0.3	1.3	1.2
Total GFCF	1.5	0.4	0.3	1.3	-0.9	0.5	-0.2	-0.3	-0.4	-0.3	3.5	0.5	-0.9
of which: NFEs	2.3	-0.1	-0.3	1.7	-1.5	0.6	-0.4	-0.3	-0.2	0.0	5.1	-0.2	-0.4
Households	0.0	1.3	1.2	0.5	-0.4	0.0	-0.1	-0.6	-1.2	-1.1	3.2	0.6	-2.5
Exports	1.4	0.8	0.8	1.9	0.0	0.3	0.5	0.4	0.7	0.8	5.5	2.6	1.9
Contributions (in point)													
Domestic demand excluding change in inventories (**)	0.3	-0.4	0.2	0.2	0.0	0.1	0.2	0.0	0.0	0.1	0.9	0.4	0.2
Change in inventories (**)	1.2	0.0	-0.3	-1.1	0.1	0.2	-0.3	-0.2	0.0	0.0	0.8	-0.9	-0.2
Net foreign trade	-0.6	0.5	0.3	0.8	-0.1	-0.4	0.3	0.0	0.0	0.0	0.0	0.6	0.1
France - situation of households													
Total employment	65	50	-24	-14	39	-1	-50	-27	-26	-21	76	-39	-
Non-agricultural market sector employment	55	43	-28	-18	19	-16	-42	-47	-38	-37	52	-86	-
Unemployment rate Metropolitan France	9.1	9.1	9.2	9.4	9.6	9.8	9.9	10.1	10.3	10.5	9.4	10.1	-
Unemployment rate France	9.6	9.5	9.6	9.8	10.0	10.2	10.3	10.5	10.7	10.9	9.8	10.5	-
Consumer price index (***)	2.0	2.1	2.2	2.5	2.3	1.9	1.9	1.4	1.1	1.4	2.1	2.0	-
Core inflation (***)	0.8	1.2	1.1	1.8	1.6	1.5	1.2	0.7	0.8	0.8	1.1	1.3	-
Household purchasing power	0.0	0.4	-0.3	-0.2	0.0	0.4	-0.2	-0.6	0.6	-0.1	0.5	-0.2	0.1

Forecast

(*) Overhang

(**) Inventory changes include acquisitions net of sales of valuable

(***) Year on year on the last month of the quarter

How to read it: The volumes are calculated at the previous year's chain-linked prices, seasonally and working-day adjusted, quarterly and annual averages, as a %

Source: INSEE

Review of the previous forecast

In Q3 2012, activity progressed slightly, by 0.2%, while we had forecast that it would remain stable in *Conjoncture in France* in October 2012. Manufacturing production progressed clearly (+1.0%), while we were expecting it to be almost stable (-0.1%). It was buoyed up notably by a marked rise in production of transport equipment. In its wake, production of market services was also more dynamic than expected (+0.4% against a forecast of 0.0%). On the demand side, household consumption, notably for manufactured products, surprised by being more dynamic and rebounding more than expected. Investment, meanwhile, fell slightly, as expected. All in all, the contribution of final domestic demand excluding stocks to growth in GDP came to +0.2 points, against the expected +0.1 points. Similarly, foreign trade buoyed activity more than expected in October: imports fell as expected, but exports progressed, when we had been expecting a slight drop. All in all, the contribution of foreign trade to growth in activity stood at +0.3 points, against an expected +0.2 points. Finally, destocking weighed more on growth than had been expected in October (contribution of -0.3 points, against a forecast of -0.2 points).

Despite slightly stronger growth than expected, the employment market situation deteriorated more sharply than expected. Employment in the non-agricultural market branches fell by 42,000 jobs, against a forecast of -31,000 in October. Finally, headline inflation evolved as expected, standing at +1.9% at the end of Q3 2012.

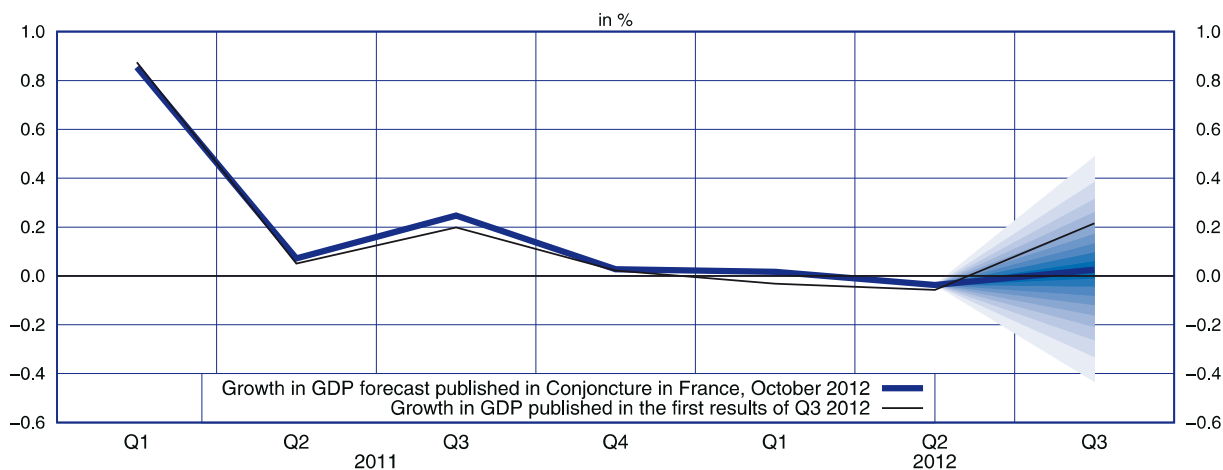
For Q4 2012, we anticipate a fall in activity, which should slip by 0.2%, while we were expecting it to be stable in October. Both domestic and foreign demand are likely to remain sluggish. Manufacturing production should fall more than expected, as a backlash after Q3, and this drop should also hold back activity in the service branches.

The employment market is likely to deteriorate more than had been expected in October: 47,000 jobs should be lost in the non-agricultural market branches in Q4 (35,000 previously forecast). Finally, inflation is likely to be more moderate than had been expected in October's *Conjoncture in France*. In December 2012 it should be 1.4%, against +1.9% forecast previously.

Activity progressed in Q3, while we had forecast stability

After a slight fall in Q2 (-0.1%), activity progressed in Q3 (+0.2%), while we had forecast that it would be stable in October's *Conjoncture in France* (see Graph 1). First of all, manufacturing production proved a surprise by progressing clearly in August (see Graph 2). While we had been forecasting a slight fall over Q3 as a whole (-0.1%), it showed a clear rise (+1.0%). In particular, production of transport equipment, buoyed by a sharp rise in exports, rebounded markedly (+3.2%). Also, production in the coke and refined petroleum products industry saw an

1- Fan chart for *Conjoncture in France* for October 2012 and growth achieved



Source: INSEE

Review of the previous forecast

upturn (+5.5%), after falling sharply at the start of the year, and that of capital goods also progressed significantly (+1.5%). Agrifood production and that of "other industrial products" remained almost stable, however.

This rise in manufacturing production buoyed up activity in market services via corporate demand. These services also benefited from the unexpected rise in household consumption of market services. Production of market services excluding retail and wholesale trade therefore progressed by 0.4% in Q3, while we had forecast it to be stable. Production in the retail and wholesale trade branch was also more dynamic than expected (+0.5% against a forecast of +0.1%), due to stronger-than-expected consumption of manufactured products.

However, energy production fell in Q3 2012, in line with our forecast in October (-1.4%, as forecast). In construction, activity slowed down markedly, as forecast (+0.1% against an expected +0.2%), with the end of the catch-up effect observed in Q2 in public works, after the delays caused by the very low temperatures in February. Finally, production in the non-market branch progressed moderately, as has been expected in October: +0.4%, against an expected +0.3%.

Consumption and exports stronger than expected

In Q3 2012, final domestic demand excluding stocks was slightly more dynamic than expected: its contribution to growth in activity came to +0.2 points, against +0.1 points forecast in October. This difference can mainly be explained by the rise in household consumption (+0.3% against a

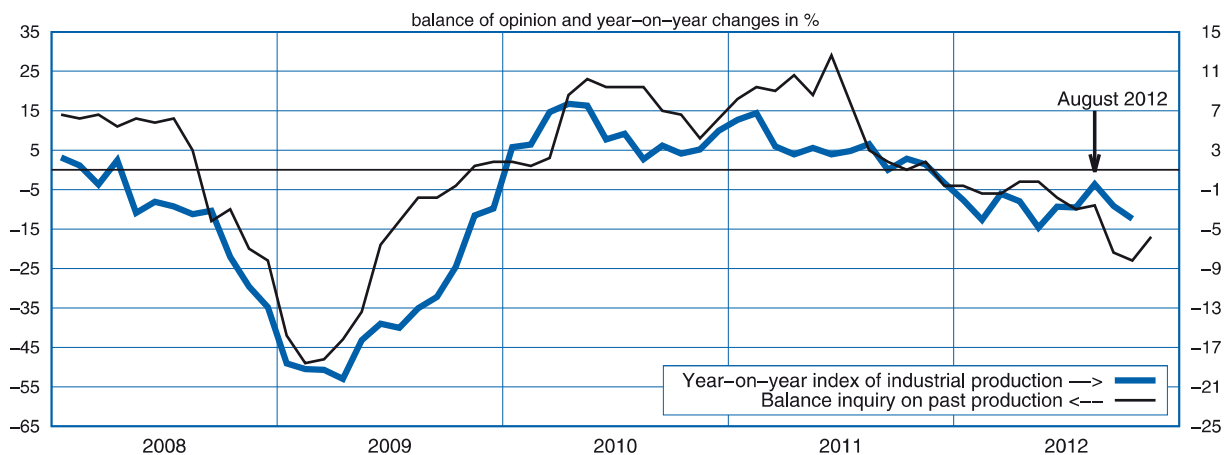
forecast of +0.1%), despite the marked drop in energy consumption (-3.8% against an expected -3.5%). On the one hand, consumption of manufactured products progressed more than expected (+0.7% against an expected +0.4%). Consumption of food and textiles-leather rebounded after a marked fall in Q2. Also, consumption of services increased slightly more than expected: consumption of market services excluding retail and wholesale trade grew by 0.2%, when we had expected it to be stable. In particular, consumption of transport services rebounded clearly, while that of accommodation-catering stopped falling.

On the other hand, investment dropped slightly, as expected. It fell by 0.2%, against an expected 0.1%. That of households slipped by 0.1% and that of non-financial enterprises (NFEs) by 0.4%, as forecast. Investment by NFEs in construction was not as dynamic as expected, but that in manufactured products fell less than had been expected.

As forecast in October, imports fell significantly in Q3 (-0.6% against a forecast of -0.8%), reflecting both sluggish domestic demand and the backlash after one-off effects in Q2 (see *Foreign Trade note*). However, the marked rise in Spanish and German imports had not been anticipated in October and French exports progressed by 0.5%, when we were expecting a 0.3% fall. In particular, exports of transport equipment were very dynamic (+7.4%). All in all, the contribution of foreign trade to growth in activity was +0.3 points, against a forecast of +0.2 points. That of variations in stock was -0.3 points, against an expected -0.2 points.

Although activity provided a positive surprise, the employment market situation deteriorated more than forecast in *Conjoncture in France*:

2 - Business tendency surveys and production in manufacturing industry



Source: INSEE

employment in the non-agricultural market branches dropped by 42,000 jobs, against an October forecast of -31,000. This difference is explained by temporary employment: it fell by 31,000 jobs, against an expected -6,000. On the other hand, employment fell a little less than expected in industry and in market services excluding temporary work.

Finally, headline inflation stood at 1.9% at the end of Q3 2012, as expected. Inflation in services fell more than forecast, however, due to a sharper-than-expected fall in telecommunications prices. Core inflation at the end of the quarter was therefore 0.1 points lower than our forecast (+1.2% against an expected +1.3%). Conversely, the fall in energy prices was less sharp than expected, and their year-on-year change therefore fell less in Q3 (+5.8% against an expected +4.8%).

Our growth forecast for Q4 2012 is revised downwards

Our activity growth forecast for Q4 2012 is revised downwards to -0.2%, against 0.0% previously. In November, the business climate measured by the business tendency surveys was at a level close to that in September, after falling in October. In industry, meanwhile, it was slightly worse than in September. The rise in manufacturing production observed in August would thus seem to have been a one-off. It had already fallen significantly in September and October (see *Graph 2*) and manufacturing production should be well down in Q4 (-1.5% forecast against -0.4% previously expected) before levelling out in early 2013. This is likely to weigh down on activity in market services excluding retail and wholesale trade, which should slip slightly (-0.1% against 0.0% previously forecast), despite resilient household consumption of services. Finally, energy production should fall: industrial activity is likely to decline and household energy consumption should also fall over the quarter. In construction, activity is set to fall, due to the drop in corporate and household investments, as forecast in the last *Conjoncture in France* (-0.4%).

Domestic demand should be slightly more dynamic in Q4 2012 than forecast in October. Investment by NFEs should decline less than previously expected, unlike that by households, which is likely to fall more sharply than had been forecast. All in all, investment should only fall by 0.3%, against an expected -0.5%. On the other hand, our household consumption forecast remains unchanged (-0.1%). It is likely to be hit notably by a fall in spending on manufactured products, offset by a slight rise in consumption of market services. The ups and downs in production should therefore not be very visible in demand excluding stocks. However, they are likely to be reflected in variations in stocks, which should make a negative contribution to growth in activity (representing -0.2 points against 0.0 points forecast previously).

In Q4, trade is set to be in line with our October forecast and therefore is unlikely to buoy up activity. Exports should progress by 0.4%, against 0.2% previously, and imports by 0.3%, as forecast in October.

In the wake of the downwards revision of activity, the deterioration of non-agricultural market employment is likely to be more marked than in our October scenario: 47,000 jobs are likely to be lost in Q4, against -35,000 expected previously. Employment should decline significantly in temporary work (-19,000 jobs, against -8,000 previously).

Finally, inflation at the end of 2012 should be lower than forecast in October's *Conjoncture in France* (+1.4% against an expected +1.9%). On the one hand, the fall in telecommunications prices was again sharper than expected in November. Also, energy inflation was less than forecast in October and November. It is also likely to be lower in December, as the price per barrel of Brent at the end of 2012 should be lower than had been expected in October. In December 2012, the year-on-year change in energy prices should therefore be lower than had been forecast in October (+3.0% against 5.3% previously). ■