FRANCE
2023-2024 SCENARIO

GROWTH WOBBLES DESPITE DIPPING INFLATION

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WORKING EVERY DAY IN YOUR INTEREST AND FOR SOCIETY

GROUP ECONOMIC RESEARCH

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SUMMARY

GROWTH HAS STALLED AND IS STRUGGLING TO PICK UP AGAIN

Sluggish growth in France could last several more quarters. Unlike some European countries, France was able to avoid a technical recession at the beginning of the year, with positive growth of 0.2% in the first quarter after 0% in Q4 2022. But growth will slow sharply in 2023, expected to come out at 0.6% after +2.5% in 2022. Growth could start to recover slowly in 2024, reaching 1%.

Customary growth drivers are slowing down. Household consumption has already declined owing to inflation, while the raising of interest rates to combat inflation is weighing on household investment and will put the brakes on investment by non-financial companies in the coming quarters.

However, some factors are supporting economic activity and helping the French economy to withstand the unfavourable environment, so we can expect a slowdown in activity but without a significant contraction. Global value chains have returned to normal, with the end of shortages that have limited industrial production since 2021. This should support supply and contribute to lower inflation, but caution remains warranted among households. Savings are still substantial and could be drawn on in part if the decline in inflation is confirmed in the coming months. Government support for businesses is less abundant, but margins have been restored in many sectors and tax pressure continues to ease.

Yet we still see some downside risks in our scenario. Energy prices are currently lower than last year but could rise if the conflict in Ukraine further deteriorates. The trend in food prices is also uncertain, with a fresh rise potentially on the cards if companies continue to increase margins more than the cost increases in the sector, despite the decline in sales volumes. Lastly, with the rise in interest rates beginning to weigh on the investments of NFCs, the aggressive continuation of the monetary tightening cycle could curb investment and have significant repercussions on the labour market, especially as fiscal policy will now turn restrictive.

Main components of the scenario:

- **Household consumption** will not rebound after contracting at the end of 2022. While the consumption of services is holding up, the consumption of goods is sliding owing to rising prices. A slow recovery is expected in the second half of the year and in 2024 as inflation continues to decline.
- **Business investment** will be weaker than in recent years, impacted by tighter financing conditions and rising interest rates. Despite resilient margins and lower taxes, investment will slow sharply, with the momentum gained since the pandemic fading.
- **Inflation** will continue to fall. But inflation in services could be more persistent owing to domestic factors including wage increases and the rebuilding of margins in sectors such as hotels and restaurants that have so far failed to pass on cost increases to sales prices.
- After negatively impacting growth in 2022, **foreign trade is expected** to make a positive contribution in 2023. The trade deficit will be reduced by lower energy prices and import prices in general, while major export sectors still have significant recovery potential.

SUMMARY

NO STRONG RECOVERY IN GROWTH

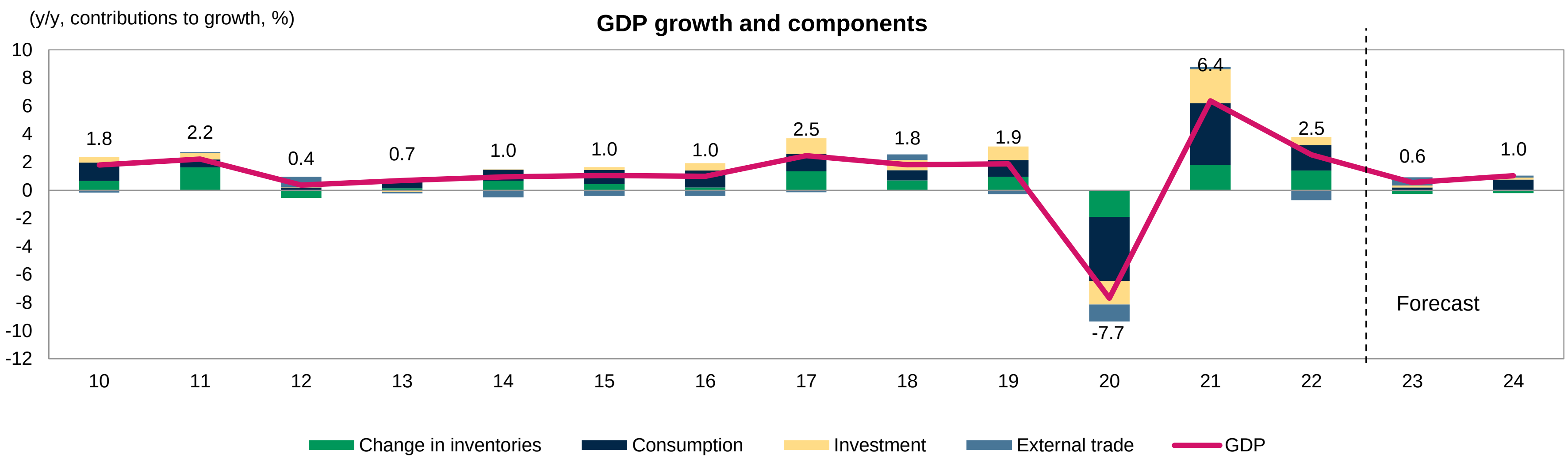
Main numbers of our outlook

France	2020	2021	2022	2023	2024
GDP	-7.7	6.4	2.5	0.6	1.0
Households consumption	-6.7	5.1	2.1	0.2	1.3
Investment	-7.0	10.2	2.4	0.5	0.6
Corporate investment	-6.8	10.4	3.9	2.1	0.5
Change in inventories*	-1.9	1.8	1.4	-0.3	-0.2
Net exports*	-1.2	0.2	-0.7	0.6	0.1
Unemployment (Insee)	7.9	7.7	7.1	7.1	7.4
CPI Insee (yoy)	0.5	1.6	5.2	5.0	3.2
Government deficit (% of GDP)	-9.0	-6.5	-4.7	-5.2	-5.0

Quarterly growth (q/q, %)

	2020				2021				2022				2023			
	T1	T2	T3	T4	T1	T2	T3	T4	T1	T2	T3	T4	T1	T2	T3	T4
GDP	-5.3	-13.1	17.4	-0.7	0.0	1.0	3.1	0.5	-0.1	0.5	0.2	0.0	0.2	0.1	0.1	0.2
Households consumption	-5.2	-11.3	17.9	-5.4	0.5	1.3	5.0	0.3	-1.1	-0.3	1.3	-1.0	0.1	0.1	0.3	0.4
Investment	-8.1	-13.0	20.4	3.7	0.3	1.7	0.1	-0.3	0.5	0.5	2.4	0.2	-0.7	-0.1	-0.1	-0.1
Corporate investment	-8.6	-11.3	19.8	1.6	1.7	1.4	0.5	-0.2	0.8	0.6	4.0	0.6	-0.3	0.0	-0.3	-0.2
Change in inventories*	0.74	0.52	-2.1	0.48	0.41	-0.35	-1.07	0.81	0.41	0.17	0.42	-0.06	-0.58	-0.1	0.0	-0.1
Net exports*	-0.5	-1.6	0.6	0.9	-0.7	0.1	0.7	-0.7	-0.2	0.5	-1.6	0.4	1.0	0.1	0.0	0.0
Unemployment (Insee)	7.7	7.0	8.8	7.9	8.0	7.7	7.7	7.2	7.1	7.2	7.1	6.9	6.9	7.0	7.1	7.2
CPI Insee (yoy)	1.2	0.3	0.3	0.1	0.7	1.4	1.7	2.7	3.7	5.3	5.8	6.1	6.0	5.2	4.5	3.8
Government deficit (% of GDP)																

* Contributions to GDP growth
Source : Crédit Agricole SA/ECO, forecast



Sources: INSEE, Crédit Agricole S.A. /ECO

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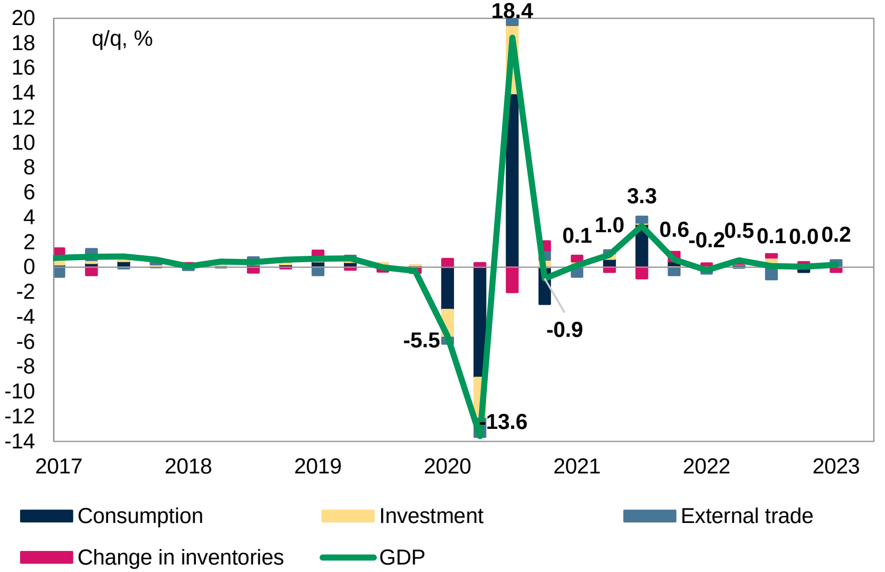
RECENT TRENDS IN ACTIVITY

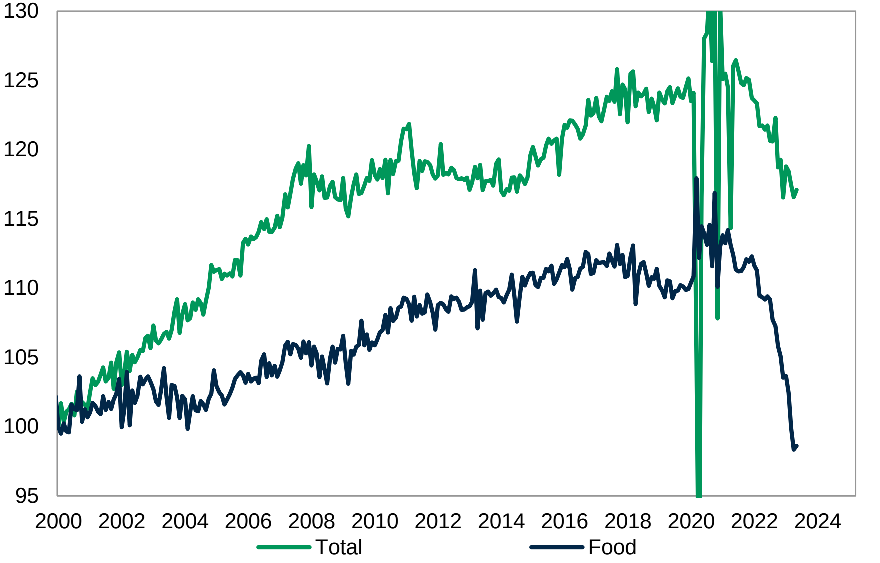
FRANCE AVOIDS RECESSION DESPITE DIPPING DOMESTIC DEMAND

GDP growth and contributions



Sources: Insee, Crédit Agricole S.A. /ECO

Household consumption of goods (volume, 100 in January 2000)



Sources: Insee, Crédit Agricole S.A. /ECO

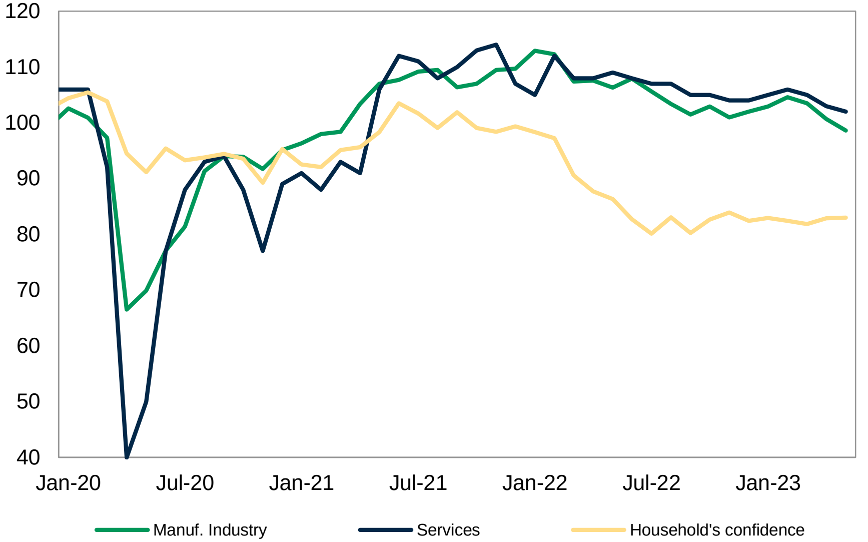
After slowing sharply in the second half of 2022, growth held up well and remained positive at the beginning of the year. This apparent robustness conceals weak domestic demand, growth in the first quarter being supported by the improvement in the trade balance.

After contracting in Q4 2022, household consumption failed to rebound, holding steady in Q1 2023 and still lower than in Q4 2019, before COVID. The consumption of goods has fallen sharply, mainly owing to the trend in food goods, down 8% year-on-year in the first quarter as food inflation reached 15%. Household investment also fell substantially for the third consecutive quarter. In addition, the effects of monetary tightening are starting to affect NFC investment, which has declined for the first time since Q3 2021. In contrast, the trade balance benefited from the sharp drop in imports at the beginning of the year (down 2.8% qoq), exports having dropped considerably less (-0.2% qoq).

RECENT TRENDS IN ACTIVITY

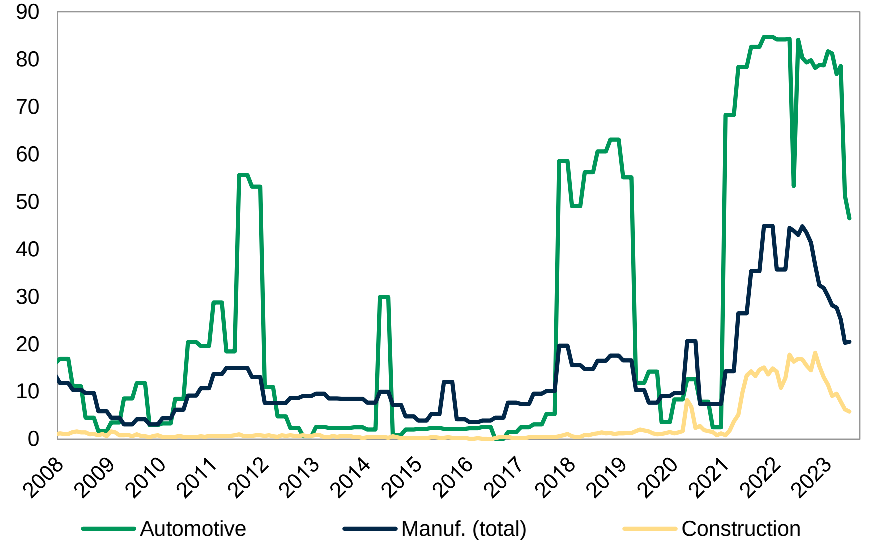
SUPPLY CONSTRAINTS EASE BUT DEMAND REMAINS SLUGGISH

Business climate and consumer confidence



Sources: Insee, Crédit Agricole S.A. /ECO

Companies whose activity is limited by supply shortages (%)



Sources: Insee, Crédit Agricole S.A. /ECO

Though supply constraints have eased, freeing up the productive capacity of manufacturing firms and reducing upward pressure on prices, the business climate continues to deteriorate in France, both in industry and services. The business climate is now trending close to its long-term average, consistent with meagre growth in activity. This is because the outlook for economic activity in the coming months is less favourable and demand remains sluggish.

Household confidence improved slightly in June but remains low. Households remain cautious even though they expect the decline in inflation initiated in May to continue in the coming months (according to the consensus on future price trends). Meanwhile, fewer businesses are looking to increase their prices in the next few months, confirming our scenario of a gradual decline in inflation that should serve to bolster consumption.

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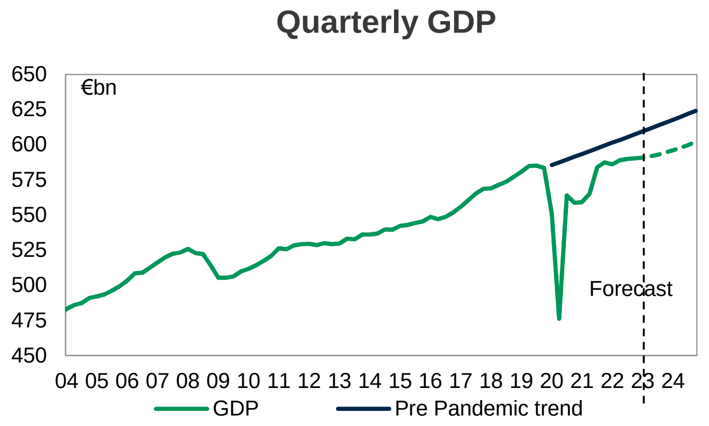
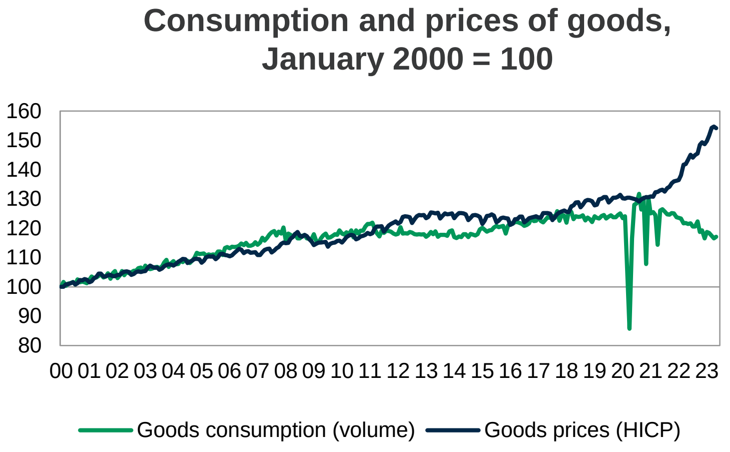
OUR SCENARIO FOR 2023-2024

FALLING INFLATION AND RISING INTEREST RATES: HEADWINDS FOR DEMAND



Sources: INSEE, Crédit Agricole S.A. /ECO



Sources: Eurostat, INSEE, Crédit Agricole S.A. /ECO

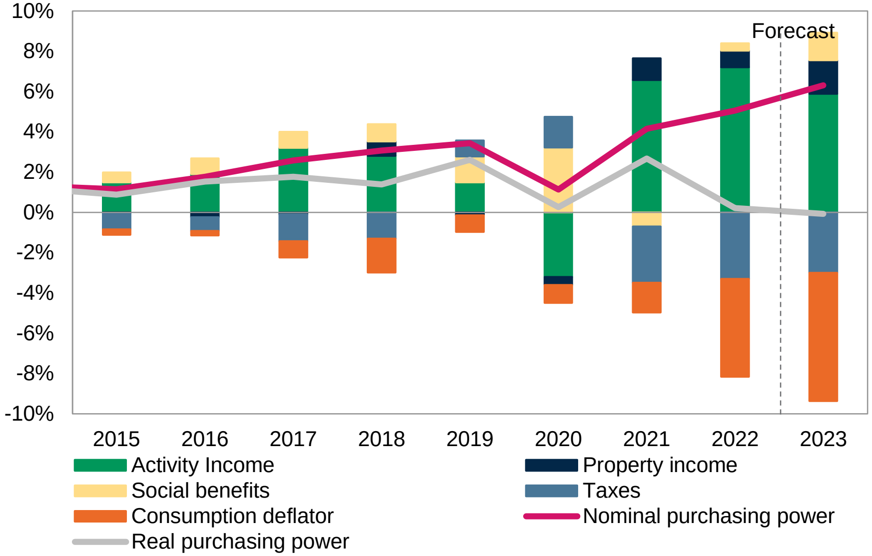
Inflation has been the number-one brake on growth since 2021, first by limiting supply through higher input costs and then by eroding demand, with businesses ultimately able to pass cost increases on to sales prices. As a result, inflation plateaued at 6% between June 2022 and April 2023. It now appears to be taking a downward trend, It fell in May and again in June, to 4.6% year-on-year, but with major contrasts from one category to the next. Food inflation remains extremely high and consumer confidence low. As a result, goods consumption has fallen in recent months. But inflation is expected to continue falling in the coming months and could lead to a recovery in consumption, especially as household savings remain high.

However, even if inflation falls, it will remain too high for the European Central Bank, which does not want the rise in prices to be fuelled by domestic factors such as wage and profit increases. Which is why it will forge ahead with its monetary tightening cycle. The ECB has increased its key rates by 4% in the last year and additional rate hikes are expected in the coming months. ECB President Christine Lagarde has also intimated that interest rates could remain high for a longer period of time. The central bank appears to be unconcerned about the consequences of tightening on the economy, mainly because labour market momentum has thus far remained strong. But it should not be forgotten that real interest rates have so far remained negative (with inflation above nominal interest rates) and that this trend is likely to reverse, with interest rates continuing to rise and inflation to fall. Furthermore, the tightening of financing conditions is not passed on immediately to the real economy. According to economic research, this process takes 12 to 18 months and could take even longer given today's high savings and cash reserves. As such, companies will feel the full effect of monetary tightening in 2023 and 2024 and investment is expected to slow sharply after three years of strong growth. The rise in interest rates has already had a visible impact on real estate, new and old properties alike. Fiscal policy, still supporting the economy in 2022 (then in contradiction with monetary policy), will also become more restrictive.

OUR SCENARIO FOR 2023-2024

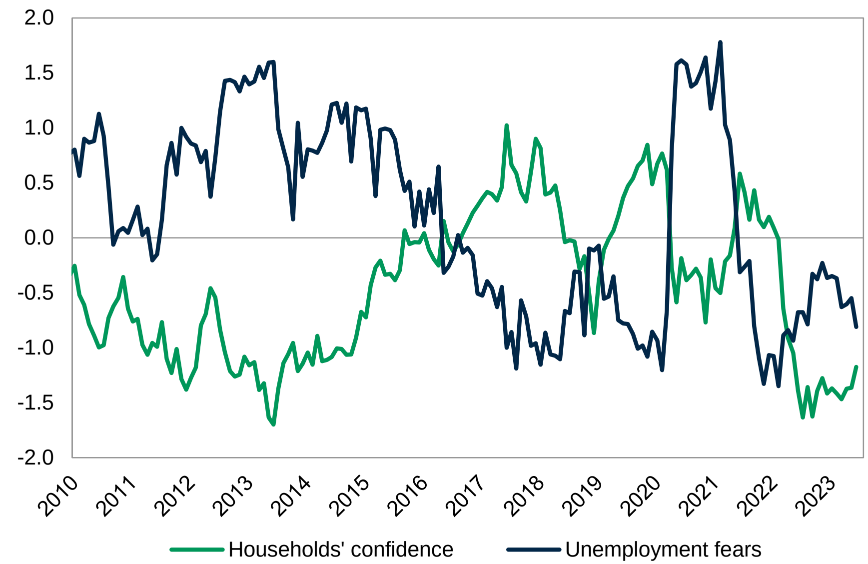
CAN LOWER INFLATION BOLSTER CONSUMPTION?

Growth in purchasing power and contributions



Sources: Insee, Crédit Agricole S.A. /ECO

Consumer confidence (normalised balance of opinion)



Sources: Insee, Crédit Agricole S.A. /ECO

The decline in inflation should keep household consumption from plummeting in the coming quarters. But inflation remains too high and real household income is expected to deteriorate in 2023. The French government is not expected to boost household income as it did in 2022 with the purchasing power law. And with inflation gradually falling, the bonuses having served to bolster household income at the end of 2022 may not be as substantial in 2023.

Households also remain highly cautious and continue to put their faith in savings. Despite a decline in purchasing power in the first quarter, the household savings rate remained extremely high, at above 18%, compared with 15% before the pandemic. This shows that households remain reluctant to draw on the surplus savings built up in recent years (with the exception of the least wealthy households).

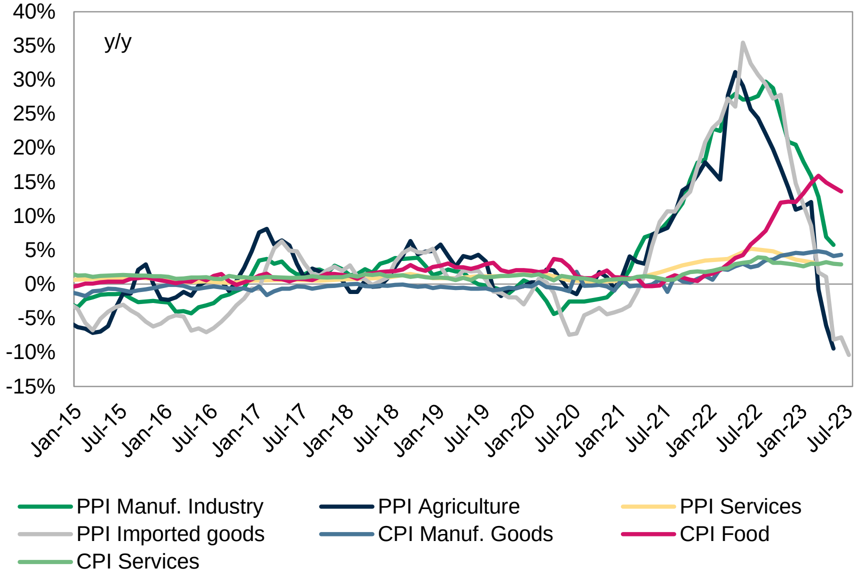
Consumer confidence may well stage a gradual recovery, but for now it is expected to remain extremely low (at 85 vs. a historical average of 100) and the decline in inflation has yet to trigger a rebound in intentions to make large purchases.

As mentioned earlier, the consumption of goods in volume terms is down sharply, but the consumption of services has held up so far, mainly because inflation is lower. Growth in household consumption came out at +2.1% in 2022 but is expected to be much more modest in 2023 (+0.2%) and recover only slightly in 2024 (+1.3%).

OUR SCENARIO FOR 2023-2024

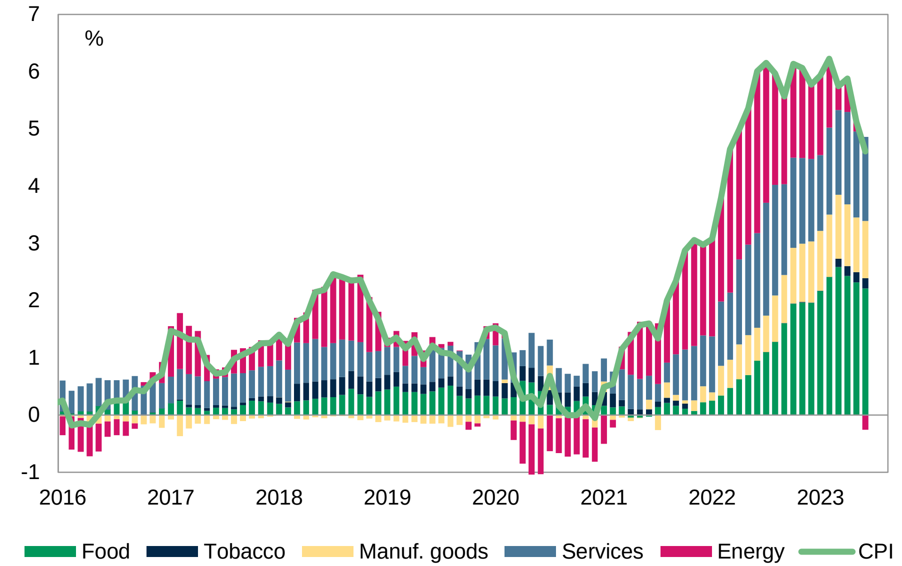
TOWARDS A SLOW DECLINE IN INFLATION

Producer price and consumer price indices



Sources: Insee, Crédit Agricole S.A./ECO

Inflation and contributions



Sources: Insee, Crédit Agricole S.A./ECO

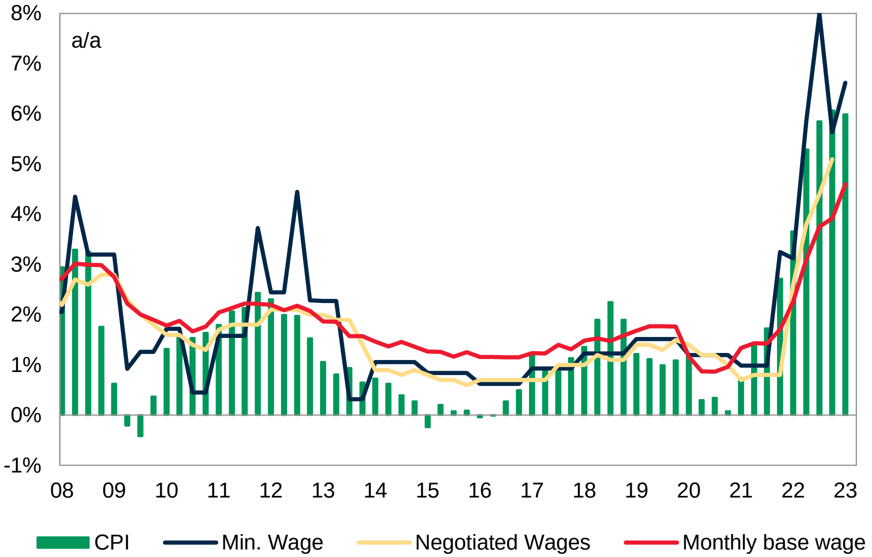
Having significantly increased production costs for businesses in 2021/2022 and gradually spread to consumer prices, imported inflation has fallen sharply in recent months. Producer prices are now down year-on-year in many sectors. With energy prices – and oil prices in particular – lower than a year ago, energy is contributing negatively to overall inflation. Food inflation, still extremely high, is starting to ebb. Price increases are now being driven by domestic inflation, which is lower. Service price inflation is hovering around 3% year-on-year and unlikely to fall in the coming months. Demand remains fairly stable in services, and some sectors, including hotels and restaurants, have yet to pass on cost increases to sales prices. In addition, cost increases remain high in services, particularly as wages are growing almost as much as prices (staff constraints). Consequently, while inflation now appears to be declining after trending at close to 6% for nearly a year, the decline will likely be gradual and we do not expect it to reach the ECB target of 2% over our forecast horizon.

After reaching 5.3% in 2022, inflation is expected to average 5.0% in 2023 and remain slightly above 3% in 2024, when the contribution of services to price trends will become predominant.

OUR SCENARIO FOR 2023-2024

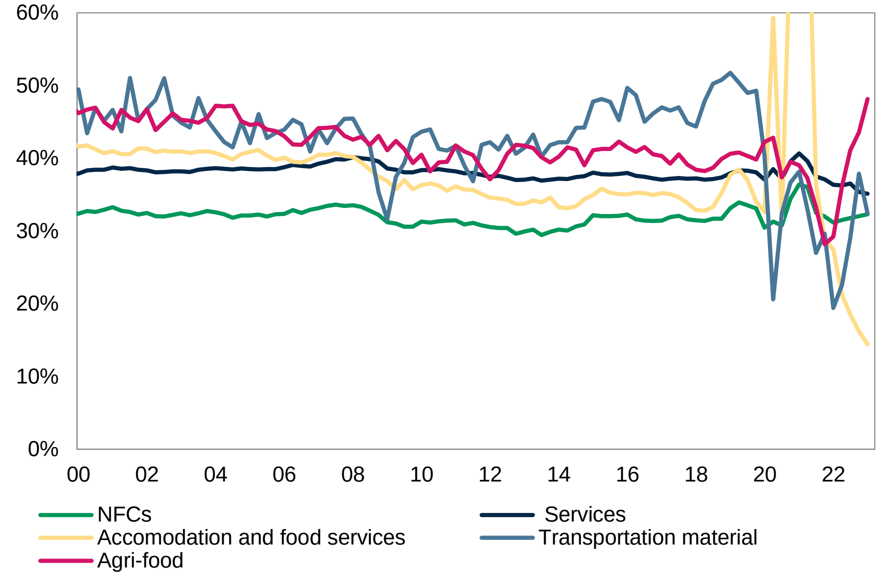
MANUFACTURING PROFITS CATCH UP, WAGES LAG BEHIND

The trend in prices and wages



Sources: Dares, Insee, Banque de France, Crédit Agricole S.A. /ECO

NFC margin rate



Sources: Insee, Crédit Agricole S.A. /ECO

Manufacturing companies have managed by and large to restore their margins after initially bearing some of the increases in production costs in 2021. Margins rebounded particularly strongly in second-half 2022 and will continue to do so in 2023 with the gradual elimination of the CVAE tax on corporate added value. Some sectors (agri-food in particular) appear to have more than passed on cost increases to sales prices, with margins now higher than in 2019.

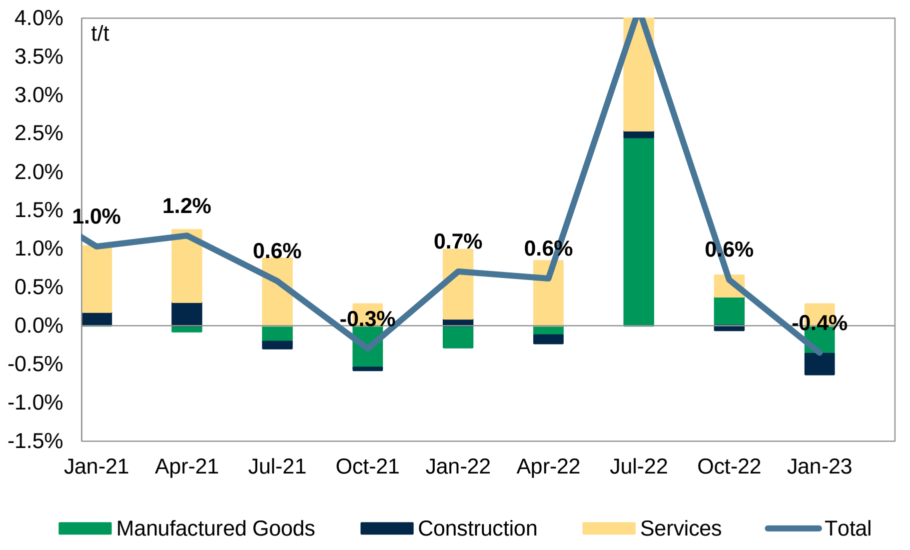
But there are limits to this pricing power, especially with the decline in the demand for goods. For as long as demand remains moderate, a price-profit loop is fairly unlikely. Demand remains more stable in services, and companies could gradually improve their margins in the coming quarters.

Meanwhile, even though wages are rising faster than the historical average, they are not increasing enough to offset inflation and thus support demand. The minimum wage is indexed to inflation and was up 6.6% year-on-year at the end of 2023. It has also caught up with, and led in its wake, some of the industry-level wage floors, which have risen faster than usual but failed to offset the increase in prices. But on average, the monthly base salary increased by 4.6% year-on-year in the first quarter, less than the 6% year-on-year increase in inflation.

These factors confirm the absence of a price-wage loop in France, despite a still buoyant labour market. While imported inflation is expected to slow, wage increases tend to lag behind and could support inflation at the end of the year and in 2024.

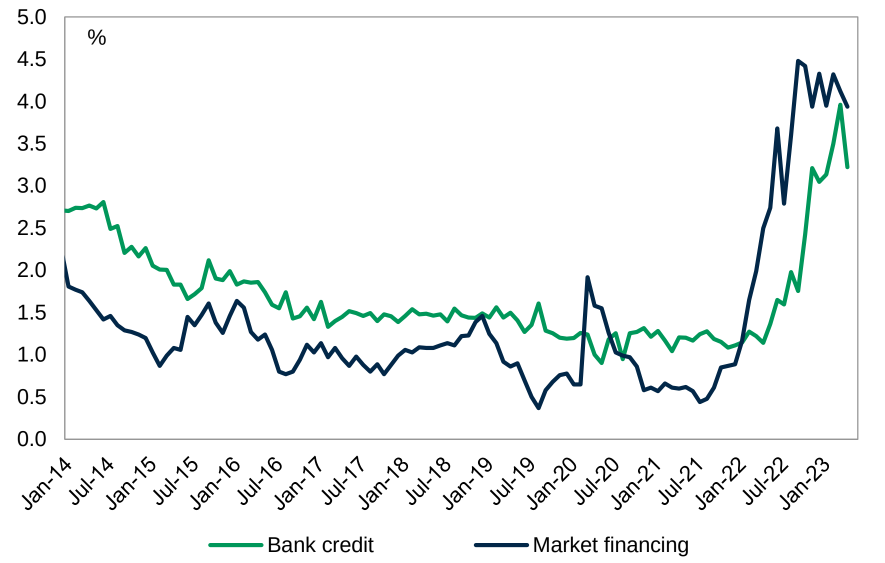
A SOFT SLOWDOWN IN NFC INVESTMENT?

Growth in NFC investment and contributions



Sources: INSEE, Crédit Agricole S.A. /ECO

Cost of financing



Sources: Banque de France, Crédit Agricole S.A. /ECO

Investment by non-financial companies remained brisk in 2022, increasing 3.8%. It was driven by the easing of global value chains, which led to a rebound in investment in manufactured goods, and by continued strong investment in services. However, the monetary tightening initiated in July 2022 is beginning to take its toll. Bank lending rates, long below market rates, have now risen, limiting the substitution of bank financing to bond financing observed in 2022 by large companies. And though industrial companies have managed to rebuild their margins, they are concerned about slowing demand, both domestically and in neighbouring European countries.

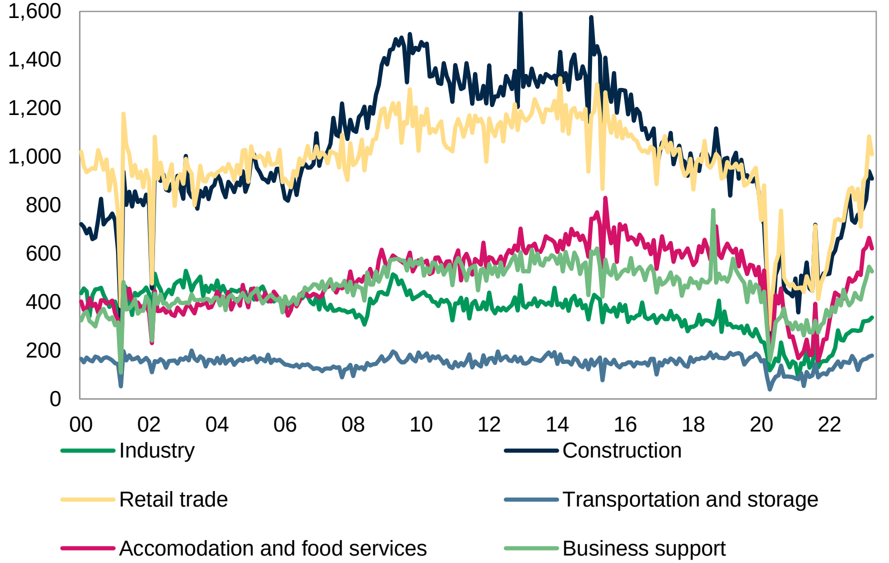
Business investment has been aided extensively since the second half of 2020 through public spending and economic stimulus plans. NFC investment is now over 8.5% higher than in Q4 2019. This means that the potential for investment growth is becoming more limited and even if the tax cuts last, direct investment support will be less abundant.

We therefore expect a significant slowdown in investment in 2023 and 2024, as monetary tightening is not over and interest rates could remain higher for longer (if they do not trigger a recession). In addition, real interest rates are likely to turn positive again as inflation slows. NFC investment is expected to increase by 2.1% in 2023, owing to consequential overhang, and by 0.4% in 2024.

OUR SCENARIO FOR 2023-2024

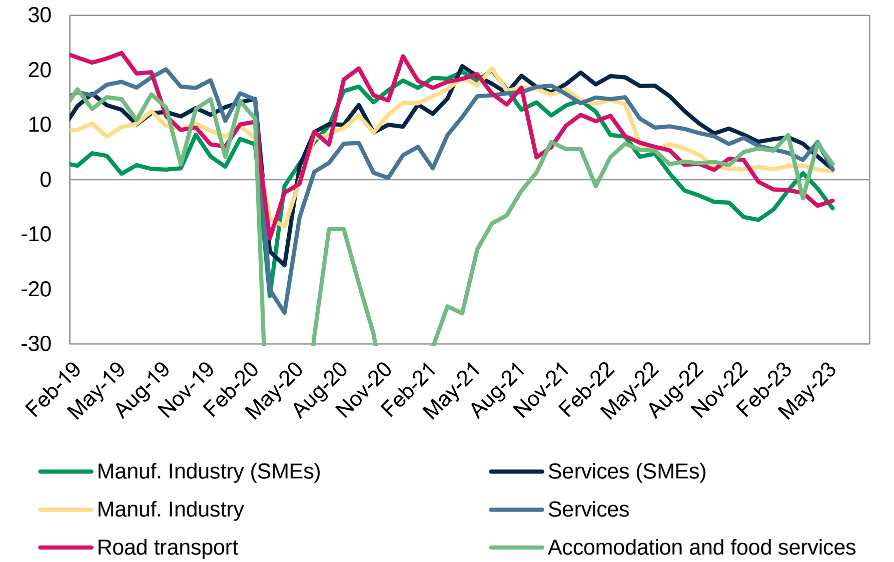
KEEPING A CLOSE EYE ON THE INCREASE IN BUSINESS FAILURES

Defaults, monthly flows



Sources: Banque de France, Crédit Agricole S.A. /ECO

Consensus on the cash position



Sources: Banque de France, Crédit Agricole S.A. /ECO

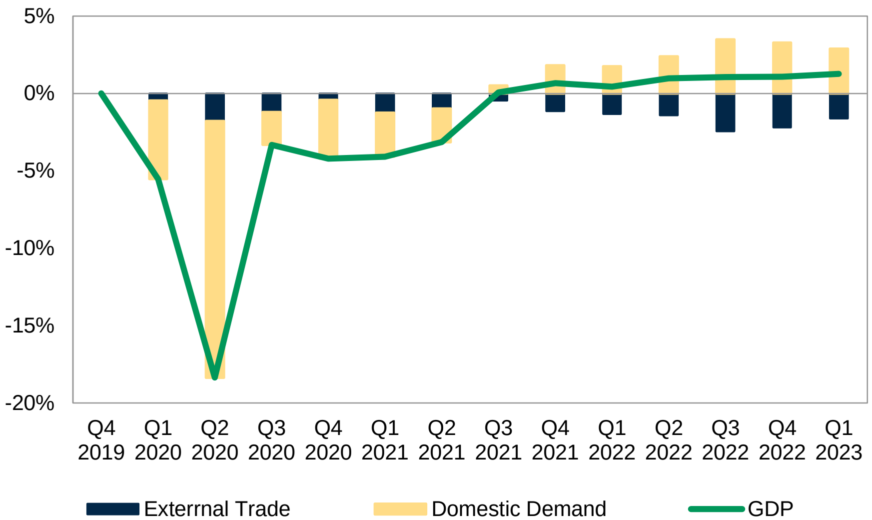
The number of business failures continues to rise, having swiftly approached pre-crisis levels. And those levels could be exceeded in the coming months, even if the increase in the number of defaults appears to have slowed since April. However, the cash position of companies remains relatively robust and, to use the words of the Banque de France, a “wall of bankruptcies” seems unlikely. The increase in defaults is above all a return to normal. The abundance of public support implemented during the health crisis and the suspension of recovery procedures in 2020 and 2021 protected all businesses without distinction, including “zombie” companies, which were artificially kept alive for two years and are now struggling. Some businesses are suffering from high inflation and tighter access to financing, and they also need to start paying back the state-guaranteed loans granted in 2020 and 2021. But the share of vulnerable companies remains relatively small.

While the risk of galloping corporate defaults appears low, a close eye needs to be kept on the rise in bankruptcies. Some sectors appear particularly exposed, particularly in services such as hotels and restaurants, where margins continue to erode and pricing power is more limited.

OUR SCENARIO FOR 2023-2024

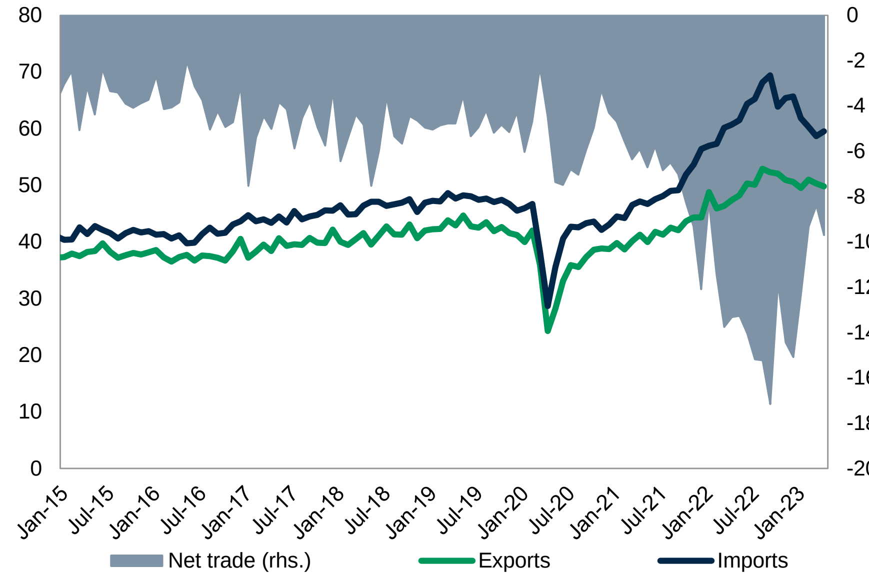
TRADE BALANCE SET TO IMPROVE AFTER RECORD DEFICITS

GDP, domestic demand and foreign trade in France (difference vs. Q4 2019 & contributions)



Sources: Insee, Crédit Agricole S.A./ECO

Trade in goods (monthly data, €bn)



Sources: Customs, Crédit Agricole S.A./ECO

Since the COVID-19 pandemic, domestic demand and, above all, investment, has recovered more strongly than foreign trade, the trade balance remaining substantially worse than in Q4 2019. The trade deficit hit a record low in 2022 owing to an increase in import prices, which contributed 55% to the deterioration, stemming in particular from the rise in energy prices. Exports were also adversely affected by the relatively slow recovery of sectors usually reporting surpluses, including tourism and aviation.

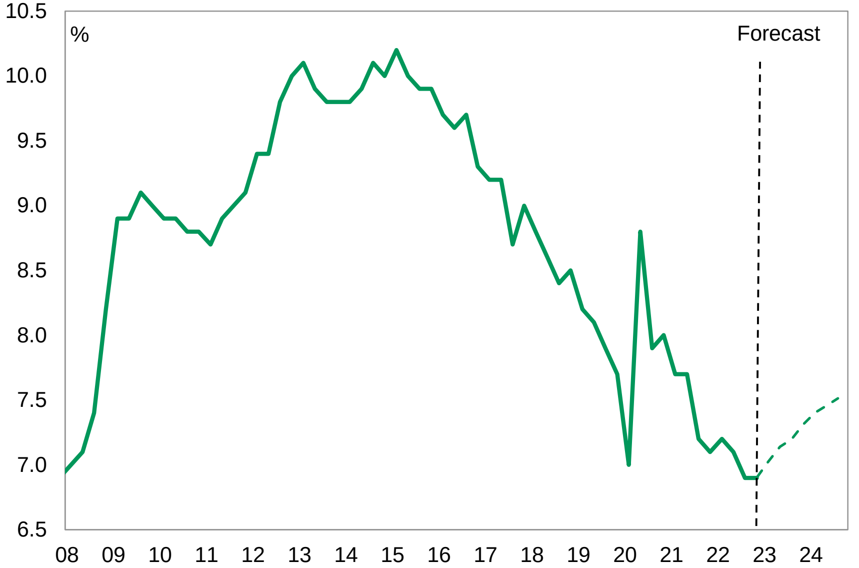
The rise in energy prices following the Russian invasion of Ukraine will nevertheless have a lasting impact on competitiveness for the Eurozone relative to other major world regions. However, while energy prices in Europe remain higher than those paid by the rest of the world, they are now down year-on-year after peaking in 2022. This helps to reduce France's trade deficit, especially as energy consumption in volume is down. Some export sectors, including aviation, should also continue to recover and contribute to this improvement.

Overall, foreign trade is expected to contribute positively to GDP growth in 2023 after a significantly negative contribution in 2022.

OUR SCENARIO FOR 2023-2024

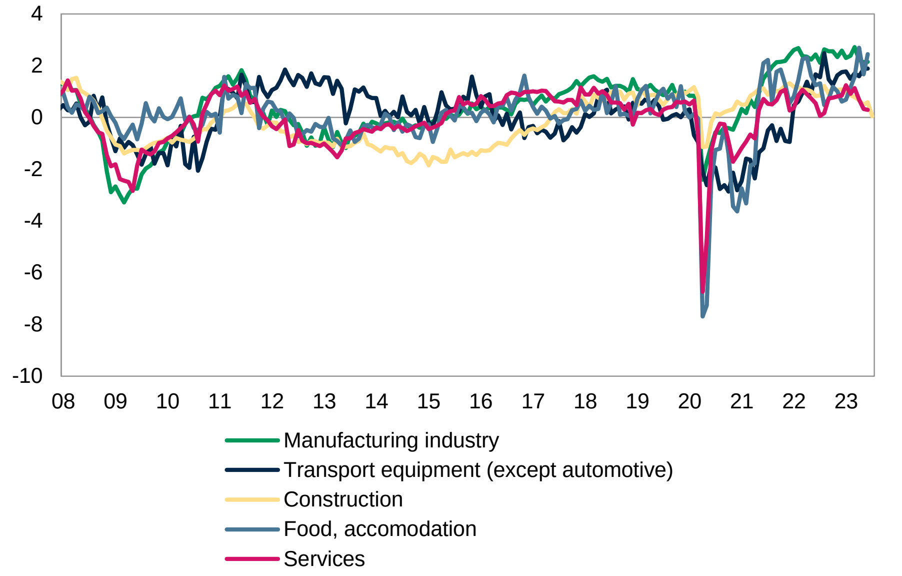
EMPLOYMENT MOMENTUM CONTINUES, BUT UNTIL WHEN?

Unemployment rate (mainland France)



Sources: Insee, Crédit Agricole S.A. /ECO

Hiring intentions (normalised indicators)



Sources: Insee, Crédit Agricole S.A. /ECO

At 6.9%, the unemployment rate remained stable in the first quarter and France now has 1.6 million more employed people than in Q4 2019. The strong momentum in job creation is driven primarily by the facilitated (and subsidised) use of apprenticeships, which, according to a recent OFCE study account for 45% of total job creations. While the reform has proved successful in accounting terms, some of these job creations appear to have replaced the creation of jobs with other statuses and may have contributed to the deterioration in productivity since the pandemic (economic activity having recovered more slowly than job creation since 2020).

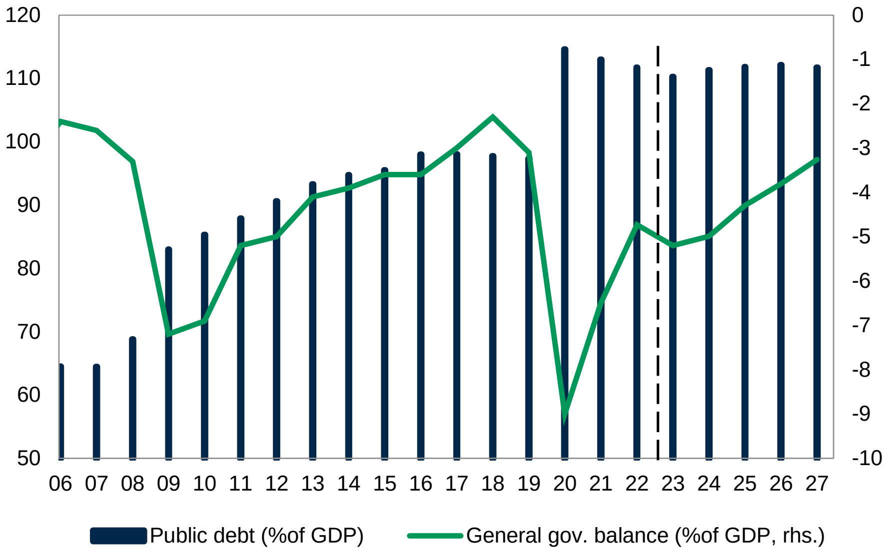
With demand waning and the government thinking about reconsidering the exceptional aid for apprenticeships introduced as part of the stimulus plan (apprenticeships cost a full €20bn for public finances in 2022), we expect job creation to slow in the coming quarters.

But because economic activity remains resilient and hiring intentions high in most sectors, the labour market is expected to remain fairly robust and any rise in unemployment should be modest. The unemployment rate is expected to remain stable at an average 7.1% in 2023 and could rise slightly to an average 7.4% in 2024, which is lower than before the pandemic.

PUBLIC FINANCES

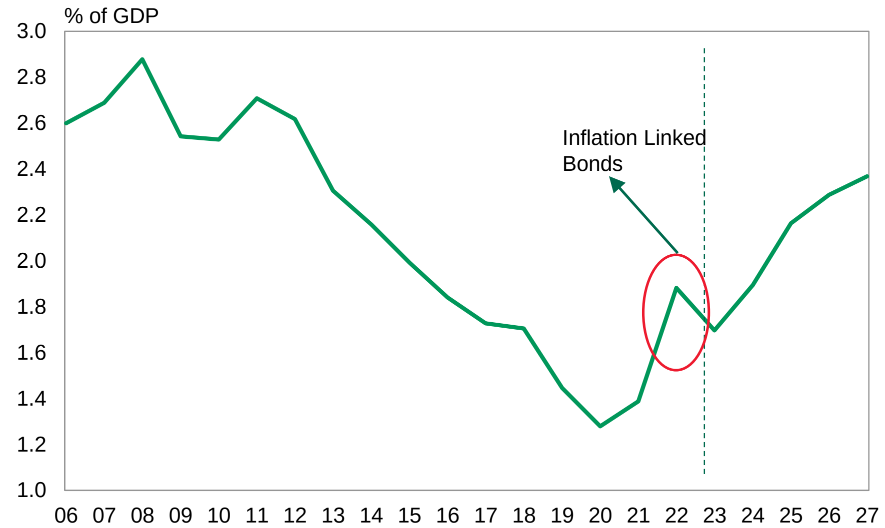
DEFICIT REDUCTION

Public deficit and debt



Sources: Insee, PSTAB 2023, Crédit Agricole S.A. /ECO

Interest expense on debt



Sources: Insee, PSTAB 2023, Crédit Agricole S.A. /ECO

After three years of fiscal support and stimulus packages, the government is waving goodbye to its "at whatever cost" policy. With interest rates on the rise and public debt nearly 15 GDP points higher than in 2019, the consolidation of public finances has become a priority once again, particularly with the return of European rules in 2024 after four years of suspension.

But support for supply will in no way be called into question and the gradual discontinuation of the CVAE tax also underlines the ongoing importance of reducing corporate taxation. The government is also maintaining support for investment, innovation and research (with the France 2030 plan and measures for the ecological transition). Savings will be generated by reducing social spending, including the second part of the unemployment insurance reform and pension reform. The government is also expected to reduce or eliminate some tax benefits on real estate investment and some healthcare spending.

However, despite the rise in interest rates, the risk for public finances is low. Although the debt stock has exploded, public debt does not cost much to public finances and the debt burden is expected to rise gradually but remain lower than in 2006, even with a debt stock twice as high and despite cautious interest rate assumptions (according to PSTAB, the 10-year OAT rate will be 3.4% from 2024 to 2027, compared with under 3% currently). All of which means that there is no "debt wall" and the risk of unsustainable French public debt remains extremely low.

But the public deficit will need to be gradually reduced to generate financing capacity and fiscal leeway in the event of a new crisis.

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Date	Title	Theme
30/06/2023	World – Macro-economic Scenario 2023-2024: normalisation plays hard to get	World
03/05/2023	Italy – 2023-2024 Scenario: 2023, the year of slowdown	Italy
02/05/2023	Spain – 2023-2024 Scenario: Sluggish growth returns	Spain
28/04/2023	United-Kingdom –2023-2024 Scenario: recession avoided, inflation persists	United-Kingdom
24/04/2023	Eurozone – 2023-2024 scenario: an unusual mix of powerful supportive and detrimental factors	Eurozone
24/04/2023	Germany – 2023-2024 Scenario: the winding path of the recovery	Germany
24/04/2023	France – 2023-2024 Scenario: activity buckles but does not break	France
07/04/2023	World – Macro-economic Scenario 2023-2024: a peculiar slowdown	World
01/02/2023	Eurozone – 2023-2024 Scenario: shock behind, shock ahead	Eurozone
30/01/2023	Italy – 2023-2024 Scenario: a year of growth despite the shock	Italy
18/01/2023	Spain – 2023-2024 Scenario: The end of the rebound	Eurozone
17/01/2023	United Kingdom – 2023-2024 Scenario: from stagnation to recession	United-Kingdom
12/01/2023	France – 2023-2024 Scenario: the economy and the challenges of inflation	France
10/01/2023	Germany – 2023-2024 scenario: towards a brief and limited recession!	Eurozone

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