Rabobank

Monthly update France

2 March 2010

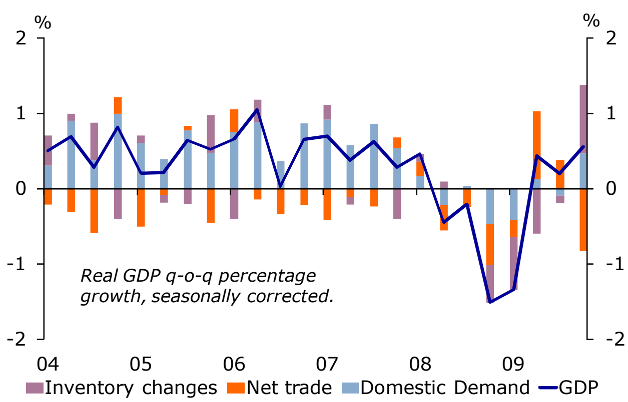
Q4 closed 2009 on an upbeat note. But now what?

year-on-year change (%)	'09	'10	'11
Gross Domestic Product	-2.2	1¼	1½
Private consumption	0.8	2¼	2
Government consumption	1.6	1	¾
Private investment	-7.5	¼	3½
Exports	-11.2	3¾	3
Imports	-9.7	6	5¼
Inflation	0.1	1½	1
Unemployment (%)	9.4	10	9½
Government balance (% GDP)	-8.3	-8¼	-7¾
Government debt (% GDP)	73.5	81½	87¼

Source: Reuters EcoWin, Rabobank

As expected, the 09Q4 GDP q-o-q growth of 0.6% was a few tenths of a percentage points higher than the 0.3% of Q2 and Q3. With that, average gross domestic production in 2009 came out 2.2% lower than that in 2008. This was the largest decline since WW2. However, within the euro zone (averaging -4%), France belongs to the group of countries that were least affected by the fallout of the financial crisis. The ray of hope provided by the relatively good growth performance in 09Q4 proved to be short-lived though. The revived consumer and producer confidence was snuffed by the growing concern, stirred up by the Greek problems, about the precarious state of public finances.

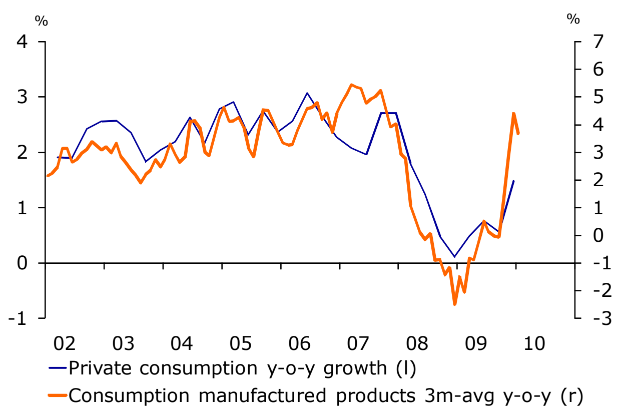
The inventory cycle saves the day



Source: INSEE

With a contribution of 0.9% to q-o-q growth in 09Q4 inventory formation came through big time. In 09Q3 France (-0.1%) lagged the rest of the eurozone (0.5%) on this point but that arrear was wiped away in 09Q4. Still, the reduction of stock levels was large in Q4 – 1.6% of GDP after 2.5% in Q3. Stocks are getting closer to the companies' desired levels so more windfalls can be expected in H1 2010. However, the German experience with inventory contribution to q-o-q GDP growth (+1.5% in Q3, -1.2% in Q4) clearly demonstrates the unpredictable nature of this factor. Its positive influence will come to an end during 2010. After that other growth drivers will have to take over the torch.

Consumers also supported growth...



Source: INSEE

With a robust growth of 0.9% q-o-q, private consumption contributed 0.5% to 09Q4 GDP growth. Consumption was strongly boosted by a run on new cars that raised car sales by 15% in Q4. This is easily explained by the 30% reduction in the car scrapping premium per 1 January. As a matter of fact, car sales dropped a stunning 16% in January. This paints a bleak picture for consumption growth in 2010 H1. Still, the underlying pattern of consumption growth was rather encouraging. Consumption of services rose slightly to 0.4%, not a bad performance in the present time. With an overall growth of 0.8% in 2009, consumption performed rather well. Also in 2010, we expect it to be the main driver of French GDP growth.

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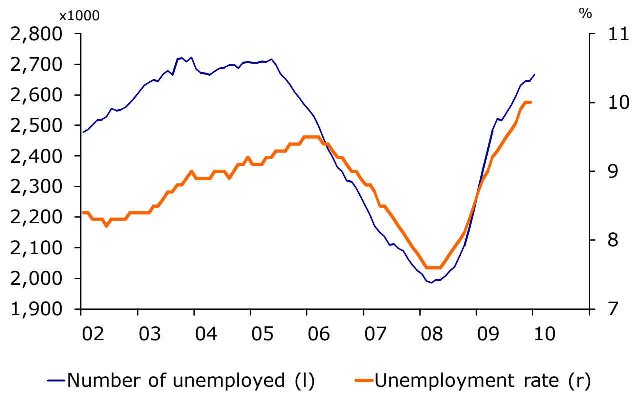
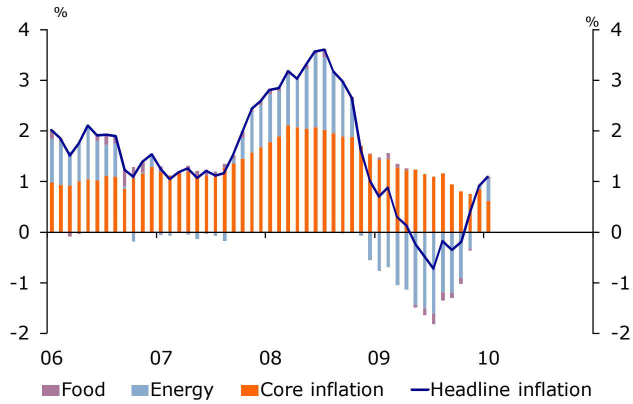
...but falling consumer confidence is a downside risk..



Source: DARES

After stabilising at the highest level in the past two years consumer confidence dropped again in February - the largest decline since October 2008. In addition to worries about the health of the country's public finances, unemployment is a major cause for this renewed pessimism. The good omens we previously distilled from unemployment statistics have all been wiped away in a recent data revision. The number of job seekers is still rising. After a minor increase in December the growth was strong again in January (+16,000). In 2009 employment in the market sectors fell by 2.5% on average. The only remaining glimmer of hope is the rise of intermediate jobs with 6% in Q4.

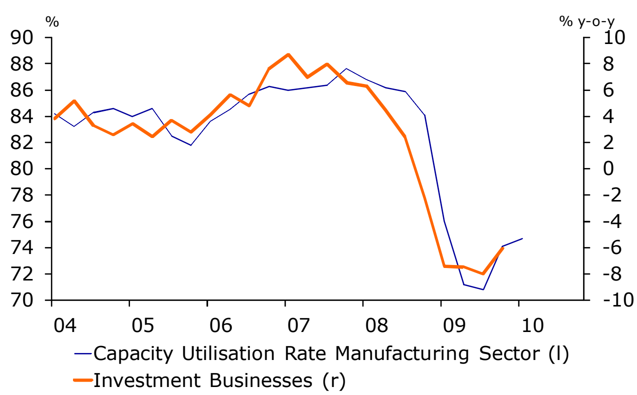
... while low inflation is a mitigating factor



Source: INSEE

Consumers will surely continue to benefit from suppressed inflation in 2010. The rise of headline inflation in January to 1.1% y-o-y, the highest point in more than a year, should be seen in perspective. It was primarily due to an energy contribution of 0.4%. Based on energy prices in the futures market, this contribution will come down quickly. Core inflation dropped to 0.6% y-o-y, again continuing its downward trend. These developments lead us to believe that inflation will hover slightly below 1% in the second half of this year. This will have a positive impact on purchasing power and consumption but it is also a worrying indicator of the business sector weakness we will turn to next.

Are leading indicators sending wrong signals?



Source: DG ECFIN, INSEE

09Q4 saw the composite PMI-index at record highs. Especially the service sector was very optimistic about the future. However, from a peak at 60.2 in November the index has fallen to 55.7 in February. Still a positive outlook on average, but it is hard to find evidence for this optimism in the actual macro figures. Industrial production growth in 09Q4 did no better than +0.1% q-o-q. Private investment fell again with 1.3% q-o-q in 09Q4. Capacity utilization rates are still at extreme lows and give little incentive for new investment. Still, a recent survey in the industrial sector showed that a 4% increase in investment is expected in 2010. Last October the same survey yielded a -3% prediction for 2010.

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