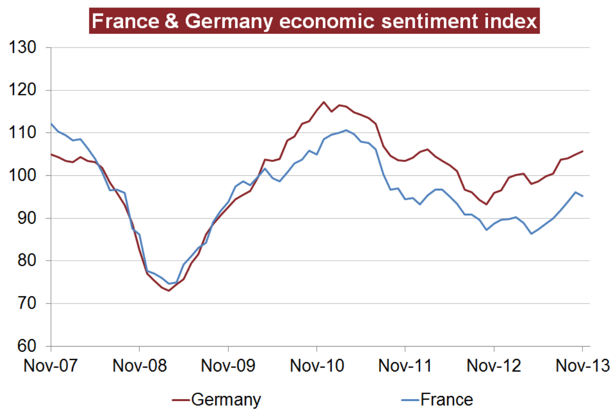
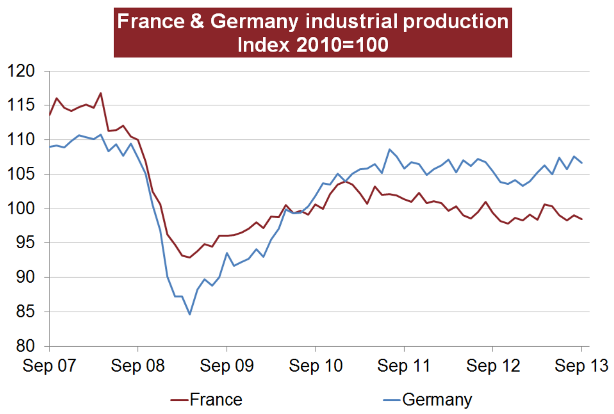
Ill blows the wind for France

- **Recent French data is generally soft**
- **Each individual series may not be bad; but the broadly-based weakness is a concern**
- **The problem now is lack of past reforms; lack of current reforms spell future problems**

November was not a good month for French data. It started with the manufacturing PMI dropping from a none-too-strong 49.8 to an even weaker 49.1 (with consensus expecting 49.4). It ends with the European Commission's Economic Sentiment Indicator easing from 96.1 in October to 95.2 in November. In between we have seen industrial production fall, France's sovereign rating being downgraded and GDP contracting in Q3. Worse, GDP growth was buttressed by a 0.5 percentage point contribution from inventories. But this was the third consecutive quarterly positive contribution from the inventories change. That would normally imply that inventories will be a drag on GDP in the current quarter as businesses attempt to adjust their stocks to the actual state of demand.





It is not that the data are so dreadful in themselves. The fall in the economic sentiment indicator was the first drop in six months and the PMI is developing in a similar manner. Rather, the problem is that the admittedly slight deteriorations are broadly based – four of the five confidence indices in the European Commission survey fell, with only the service sector confidence index bucking the trend – and that they are occurring at all. There is also a clear divergence becoming visible between French and German data. The German recovery may be sluggish and fragile, but it's there. The French recovery is hardly there at all.

Other data confirm the gloomy outlook. Euro area broad money growth slowed to a two-year low of 1.4% in the year to October. But French broad money growth (more correctly, the French contribution to EA M3), which until recently was faster than the area-wide number, is now slumping. In the year to October, it grew by 0.8%; while credit to the non-bank private sector is barely positive at 0.6% over the same period.
Even on the foreign trade side, France is showing signs of weakness. German exports (by value) troughed in May 2009 and have since risen by 48%. French exports have also recovered since their post-crisis trough (April 2009), but only by about 34%. Moreover, their trend is now sideways or even down.

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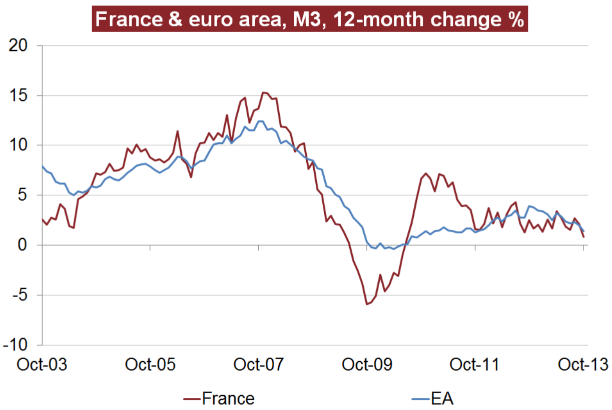
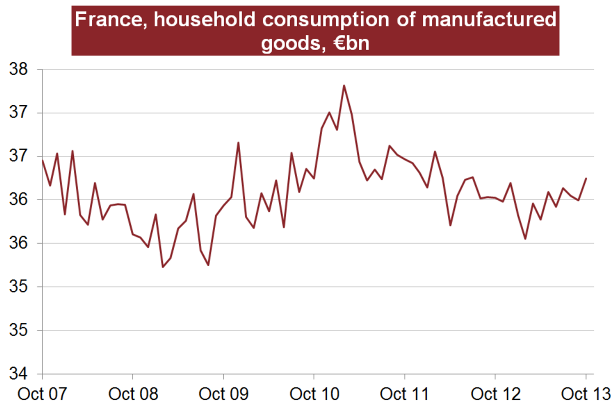
This is not surprising. The EU's harmonised competitiveness indicator shows that France improved its situation vis-à-vis the rest of the world somewhat from 2007 to 2011; but since then, there has been little or no change. By contrast, Germany has benefitted from its reforms in the early 2000s (the Agenda 2010), while the periphery countries have more recently been forced to change due to their circumstances. Some of this has been through large-scale unemployment. France has avoided the 25% unemployment rates seen in Spain and Greece. But, at close to 11%, French unemployment is not enviable either.

The problem is also that reforms take time to work through. As noted above, Germany is still reaping the rewards from reforms implemented ten years ago. France is suffering because previous governments did little or nothing to deal with the country's structural problems; meanwhile, the current government is reversing some of the reforms that actually did take place (eg, raising the retirement age) and doing little to improve France's future relative position. This raises the spectre that France will continue to underperform over the medium term.

There have been some better news. Unemployment fell in October, the first real fall since April 2011. But the number of unemployed remain near a record-high of 3.27 million (10.9% of the labour force) and much of the recent improvement is due to state-sponsored make-work schemes.

The one clearly positive indicator published this month is that household consumption of manufactured goods – a leading indicator of household spending – jumped by 0.7% in October. However, form a longer perspective, the level remains weaker than two years ago and the rise is perhaps more significant as an indicator of how far France has to go even to catch up with the general Euro area recovery – which in itself is not too great.





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