

Downturn of activity in France

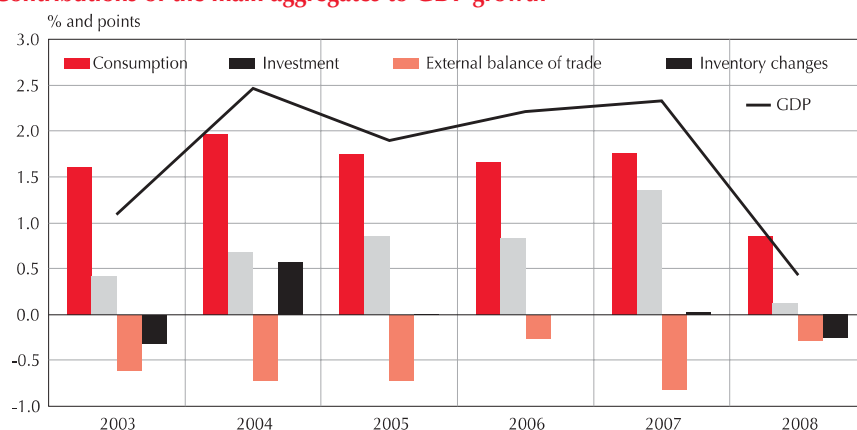
Jean-Marc Fournier and Pierre Leblanc*

Like the other industrialised countries, France suffered from the world crisis in 2008. GDP rose by only 0.4%, compared with +2.3% in 2007 [1]. This very low mean annual growth rate masked a steep decline in the course of the year: activity took a downturn from spring onwards and in the autumn this drop was accentuated still further.

Domestic demand, which had increased by almost 3% per year on average from 2004 to 2007, slowed markedly (+0.7%). Household consumer spending grew by 1.0% in 2008, compared with +2.4% in 2007. Over the last ten years, it had always increased by more than 2% per year. Total investment, which had increased markedly over the previous four years, virtually stagnated (+0.6%): household investment (excluding individual entrepreneurs) fell in 2008 for the first time since 1993 (-1.4% compared with +5.5%), general government investment well and truly collapsed (-4.4% compared with +4.5%) and investment by non-financial companies slowed considerably (+2.6% compared with +8.7%). Furthermore, non-agricultural firms ran down their stocks, which cut growth by 0.3 of a point (after zero contribution in 2007). This massive running down was concentrated at the end of the year. The worsening of the financial crisis in the autumn did indeed prompt companies to limit their cash requirements as much as possible especially as at the same time expected demand was in decline.

In addition to the slowing of domestic demand there also was the slowing of external demand. Exports fell slightly (-0.2% after +2.6%), as they were affected by the slowing of world trade. At the same time, imports improved only a little (+0.8% after +5.4%). In fact, these mean annual figures smoothed over the very violent economic reversal that occurred: between spring and summer, in the space of nine months, export and import levels dropped by 7.4 and 3.5 points respectively¹.

1. Contributions of the main aggregates to GDP growth



Source: Insee, National accounts – base 2000.

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1. Quarterly figures adjusted for seasonal variations and working days.

The slowdown affected production in all branches

In 2008, there was a considerable slowdown in practically all branches. However, it was the manufacturing industry that was most affected, particularly at the end of the year, due mainly to an exceptional drop in automobile production. Consumer goods and capital goods fared better, as demand was for the most part maintained. The situation in construction suffered a reversal, both in the building industry and in public engineering works. Activity in the service sector slowed markedly: it suffered not only the knock-on effects of the industrial slowdown, but also the effects of a reduced increase in consumption.

The manufacturing industry and particularly the automobile industry, felt the full force of the crisis

The downturn in activity in 2008 affected most sectors of the economy (*figure 2*), but manufacturing was particularly severely hit. Production stalled in the second quarter and fell heavily in the fourth quarter by 7.8%, the largest recorded drop in a single three-month period since 1949² (excluding the second quarter of 1968 which was affected by the events of May 1968). On average across the whole year, production in the manufacturing sector fell by 1.6% in volume, after a 2.2% increase in 2007.

Consumer goods and especially capital goods³ resisted relatively well (-0.5% and +4.2%), sustained because a certain level of demand was maintained (consumption of these products is still increasing, growth in manufacturing investment by companies, exports of aircraft still dynamic). On the other hand, intermediate goods, which are used in the upstream production process, and are hence upstream from the effects of cyclical downturns, saw production fall by 3.1%. It was the automobile manufacturing sector that was particularly badly affected by the crisis: production slumped by 9.3%, with a drop at the beginning of the year and a collapse of almost 30% in the autumn. This major drop in production affected all the main car producing countries (Germany, United States, Italy, Japan). On top of this pronounced cyclical movement, the sector is also currently experiencing a more structure-based crisis (cf. report on automobiles).

2. Contributions of the main branches to total value added



Source: Insee, National accounts – base 2000.

2. Quarterly series from the national accounts are now available from 1949.

3. This branch includes the construction of means of transport excluding cars, manufacture of mechanical, electrical and electronic equipment.

The construction industry ground to a halt

The construction industry has been dynamic since 2004, with annual growth in production volume of almost 4.5% on average. In particular it has been sustained by a high level of household investment, which was in turn supported by low interest rates, expectations of an increase in property prices and tax incentives (aid measures for investment in rental property and, since mid-2007, partial deductibility of interest on housing loans). The situation changed radically in 2008. First, conditions for obtaining credit, both in terms of access and rates, were much more stringent in the wake of difficulties experienced by many financial establishments. Second, after several years when prices in the property sector rose considerably, expectations of further rises began a downward trend.

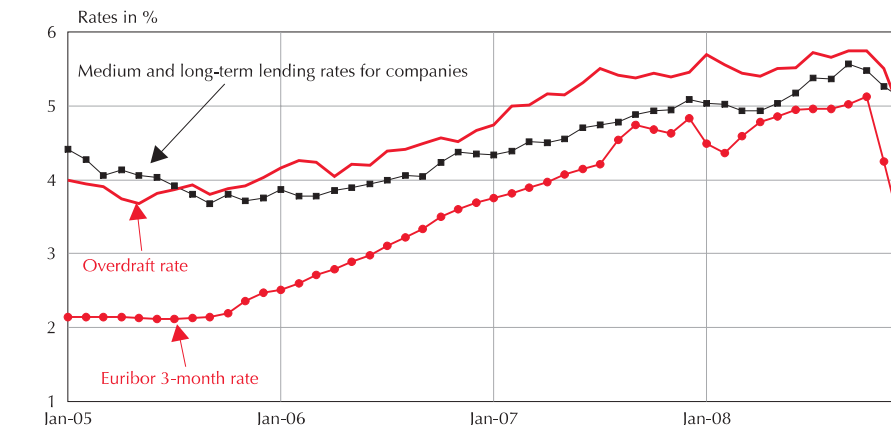
Public investment in building and major public works fell away completely, after a noticeable increase the year before, something which often happens just after local elections. On the other hand, although construction investment by non-financial companies slowed, growth remained decidedly positive (+3.7% in 2008, after +9% in 2007).

Overall, production in the construction sector came to a virtual standstill in 2008, after a rise of 5.4% in 2007. This downturn could be seen from the second quarter onwards.

The service sector resisted, but production slowed considerably

In general, the mainly non-market service sector⁴ held out slightly better (+1.5%), but production nevertheless slowed markedly compared with 2006 and 2007 (+4.2% and +3.5% respectively). As a result of the importance of this sector to the French economy, in accounting terms this slowdown accounted for most of the deceleration in total activity (figure 3), however, services to companies, which include notably activities linked with temporary posts, in fact slowed in the wake of the present industrial situation. Property development and rental services marked time, in a context where the downturn in the property market affected old and new buildings alike. Personal services suffered as a result of the slowdown in consumption, while trade and transport experienced a deceleration in demand from both households and businesses.

3. European interbank rate and credit rates for companies



Source: Banque de France

4. This sector includes Trade, Transport, Financial activities, Property activities, Services to companies and Personal services.

In 2008, the agricultural sector improved considerably (+2.9% compared with +1.5%). In particular, this sector benefited from abundant cereal harvests, boosted by improvements in yields and an increase in the amount of fallow land put under cultivation. In contrast, production in the agri-food sector fell (-0.7% after +1.4%), in a context where increased food prices led to a drop in consumption volume.

Companies had to cope with a downturn in expectations in terms of demand and prices, coupled with financing conditions that were suddenly more stringent

The downturn in demand forced companies to reduce investments and run down stocks in a massive way, especially in the automobile sector. Also, financing conditions for companies became much more stringent in 2008. The worsening of the financial crisis after the Lehman Brothers investment bank filed for bankruptcy in September made it not only harder to obtain credit but also increased the cost of credit. Indeed, the banks tried to restore balance, in a context of depreciating assets and increasing difficulty refinancing on the interbank money market.

Investment slowed ...

In the course of 2008, the drop in the number of outlets and in prospects for future activity affected company investment. The tightening of financial conditions accentuated this phenomenon at the end of the year. Overall, after a considerable increase in 2007, investment by non-financial companies slowed considerably (+2.6% compared with +8.7%). In fact this fairly moderate mean annual growth masks a sharp fall from spring onwards.

... and stock disposal caused activity to plummet in the autumn

The worsening of the financial crisis in the autumn also drove companies to minimise the demands made on their cash position. Whereas at the beginning of the year the increase in the price of raw materials was still an incentive to build up inventory upstream from the production line, these prices subsequently dropped. In a context of misguided demand forecasts, companies ran down their stocks on a massive scale at the end of the year and at the same time they reduced production. This phenomenon was noticeable in the automobile industry in particular, where many production lines were partially or completely halted, so as to clear stocks that had become excessive. Overall, by stock disposal alone, GDP was reduced by 0.8 points in the fourth quarter of 2008. Across the whole year, the contribution to growth made by inventory was -0.3 points, whereas the previous year it had been zero.

Reduced margin rates for non-financial companies, and their cash flow continued to decline

In 2008, the margin rate⁵ of non-financial companies fell slightly, to 31.3% compared with 31.6% in 2007, as in periods of economic slowdown employment is slow to adjust to activity. In fact, the increase in the gross wage bill paid by non-financial companies was greater than that of the value added that they generated (+3.8% compared with +3.0%). The increase in employers' contributions was more contained (+3.2%), thanks to the law concerning labour, unemployment and purchasing power, called the TEPA law (exemption for overtime hours). This reduced, though it did not cancel out entirely, the difference

5. The margin rate is the ratio of gross operating surplus to value added (in securities).

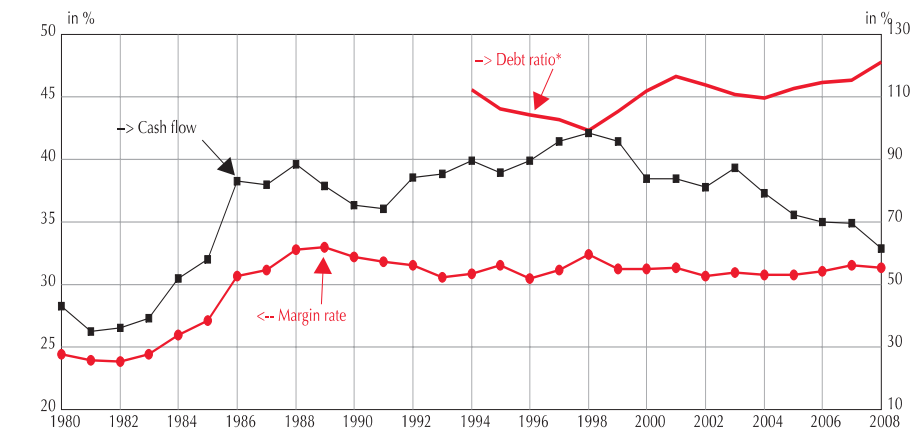
between the increase in total wages (“super gross” wage bill at +3.6%) and the increase in value added.

The decrease in margin rates, relatively moderate as an annual average, was much more marked at certain times in the year (-1.2 points between autumn 2007 and autumn 2008), a clear indication of the violence of the economic downturn.

Under the influence of the downturn in activity, the gross operating surplus (GOS) of non-financial companies slowed considerably (+2.2% after +7.4% in 2007). At the same time, the dividends paid by non-financial companies (+10.7% after +6.5% in 2007) and their corporation tax continued to increase as they were based on the good results of the previous year. The same is true for the interest from loans that had to be paid off, in a context where risk premiums were rising. In all, their savings dropped by 6.6%, whereas they had increased by almost 11% in 2007.

This decline in savings combined with the increase, although slowed, in investment resulted in a drop of more than 8 points in cash flow (*figure 4*), which has since stood at around 60%. Cash flow had dropped 37 points since 1998, and returned to the same level as in the middle of the 1980s.

4. The drop in cash flow matches the increase in the debt ratio



(*) Outstanding debt at year end added to annual value added rate

Sources: Insee, Banque de France, calculations by Insee

The activity of financial companies stagnated

In 2008, the value added of financial companies stabilised (+0.1%), after slowing in 2007 (+1.1% compared with +6.2% in 2006).

The decline in the value added of banks (credit institutions and investment companies) by -0.4% in 2008 (after +2.8% in 2007 and +3.6% in 2006) may seem very small in the context of a financial crisis. This is due to the fact that when banking activity is measured in the national accounts system neither profits nor, in fact, losses from their financial assets are included. Bank production consists of commissions received for interbank services or services billed to clients (billed services). These also include financial intermediation services indirectly measured (FISIM, corresponding to margins on deposits and credits).

In 2008, the banks' billed services were stagnating (+0.3%) after two years of substantial growth (+11% in 2007 and +14% in 2006) and FISIM increased by 2.5%, after a drop of 3.9% in 2007 (mainly due to operations with the rest of the world).

The slight reduction in the value added of banks was accompanied by a drop in staff costs (reduction in bonuses and profit-sharing schemes). Moreover, the total of received interest had increased a very great deal and both dividends and corporation tax were considerably reduced. Although these very favourable changes in income were lessened by the decrease in reinvested profits received from foreign subsidiaries, they nevertheless produced a noticeable increase in the banks' net lending. However, at the same time they must have seen a substantial depreciation in their assets.

The activity of insurance companies was stable in 2008 (value added up 0.2%, after a drop of 7.4% in 2007) as a result of two opposing movements. Life insurance declined once again in 2008 (-5.2%, after -2.7% in 2007 and +6% in 2006). Apart from the after-effects of the massive transfer of funds in 2006 away from housing savings schemes (PEL) into life insurance policies⁶, this reduction can be explained by a lack of enthusiasm on the part of households for this form of savings when the financial markets were in such strong decline, and especially when interest rates for the "Livret A" savings account had increased considerably. Thus the drop in life insurance contributions continued in 2008. At the same time, the benefits paid out (savings withdrawals) increased considerably, in a context where the return on their investments to be awarded to policyholders was very much in decline. However, the reduction in life insurance was compensated for by an increase in other insurance services.

Downturn in the labour market

Although employment had been dynamic since 2006, resulting in a decrease in the unemployment rate, it experienced a downturn in mid-2008, in line with the decrease in activity. Between the first quarter of 2006 and the first quarter of 2008, almost 470,000 salaried jobs had been created in the non-agricultural market sector⁷ (a little over 490,000 full-time equivalents⁸). Across the whole of the labour market (including agriculture and those branches that are mainly non-market), almost 600,000 jobs were created during the same period. This movement came to a halt in the spring. Although the evolution in employment lagged slightly behind the decrease in activity, the labour market was affected fairly quickly. In the fourth quarter of 2008 especially, the non-agricultural market sector lost more than 85,000 jobs, whereas for the economy as a whole the reduction was around 65,000 jobs. This downturn caused a sharp increase in the unemployment rate (cf. *infra*).

Contrasting changes in employment

The majority of job losses in the second quarter were in branches of services (*figure 5*), due mainly to the decrease in temporary work (temporary work is classified under services, even though a large proportion of temporary workers work in industry). Job losses accelerated in the manufacturing industry, while in the construction sector employment slowed.

6. Since 1st January 2006, interest on PEL accounts that were more than 10 years old became subject to social deductions (CSG, CRDS) at source instead of when the account was closed, and accounts of more than 12 years standing were subject to income tax (standard or marginal rate of personal income tax).

7. The non-agricultural market sector groups industry and mainly market services.

8. For a more accurate assessment of the workforce mobilised in the French economy, we must use the notion of "full-time equivalent", where two people working part-time are counted as one full-time equivalent. When part-time working is taken into account in this way, the number of jobs counted as full-time equivalents is less than the number counted for individual workers. On the other hand, multi-activity and corrections for undeclared employment or fraud increase the total for full-time equivalents.

5. Contribution of main sectors to total salaried work



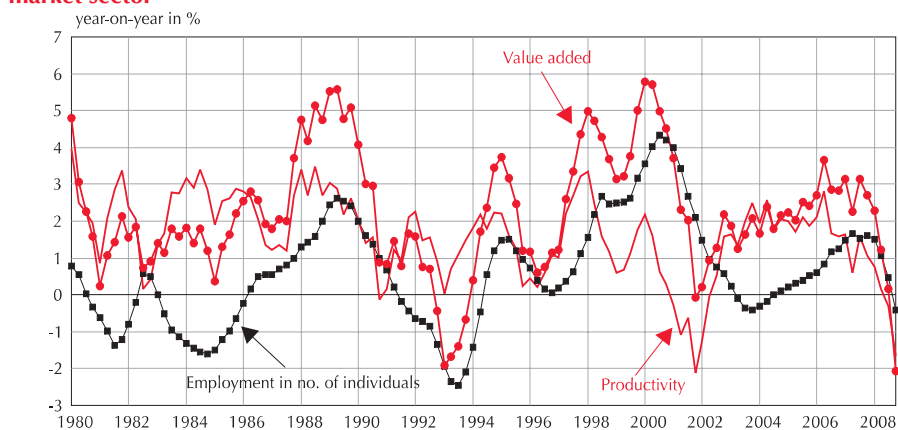
Source: Insee

The employment trend in the manufacturing branches has been falling since 2002. This decline was accentuated in the second quarter of 2008 compared with the three previous quarters. Employment in construction slowed at the end of the year, whereas it had been dynamic since 2004. In market services, there was a marked decline, whereas job creation in this branch contributed more than half of the growth in paid employment in 2006 and 2007. In the fourth quarter of 2008, paid employment in market services made a negative contribution to total paid employment, -0.3 points for a total evolution of -0.3%. Services to companies suffered most, with a drop of 1.3% in the fourth quarter of 2008. This mainly reflected the contraction of temporary work by more than 13% at the end of the last quarter, a reduction not seen since 1982. Moreover, the proportion of temporary workers in employment, which was around one per cent at the beginning of the 1980s, has quadrupled since. Also, the loss of 79,500 temporary workers observed at the end of the year is unprecedented. Personal services held out, while other market services evolved only slightly. In administered services, employment recovered in the second quarter of 2008, after near stagnation in the first quarter. This recovery was due to the halt in the decline in subsidised contracts in the non-market sector and to the increased numbers of jobs in “health and social action”.

Employment is slow to react to turning-points in activity; thus productivity, the ratio of added value to employment, is temporarily pulled down when there is a drop in activity, then revives afterwards when activity picks up again. This is indeed what we saw during 2008 (*figure 6*): across the whole of the non-agricultural market sector, labour productivity (in this case added value in relation to the number of employees) dropped by 0.1%, whereas it had grown by 1.8% on average over the previous five years. Year-on-year, it fell noticeably in the fourth quarter of 2008, for the first time since 2002.

In the manufacturing industry, apparent labour productivity dropped by 0.9% - for the first time since 1975, and in the mainly market service sector it slowed considerably. This fall in productivity should however be put into perspective. Here, productivity is defined as the ratio of value added to the number of employees in the same field of activity. However, the drop in activity over the second part of 2008 led to periods of partial unemployment for employees. These periods of partial unemployment were taken into account in the number of hours worked, but not in employment itself, whether counted as individual workers or as full-time equivalents. The fact that partial unemployment was not taken into account leads a priori to an under-estimate of apparent labour productivity.

6. Employment, value added and apparent labour productivity in the non-agricultural market sector



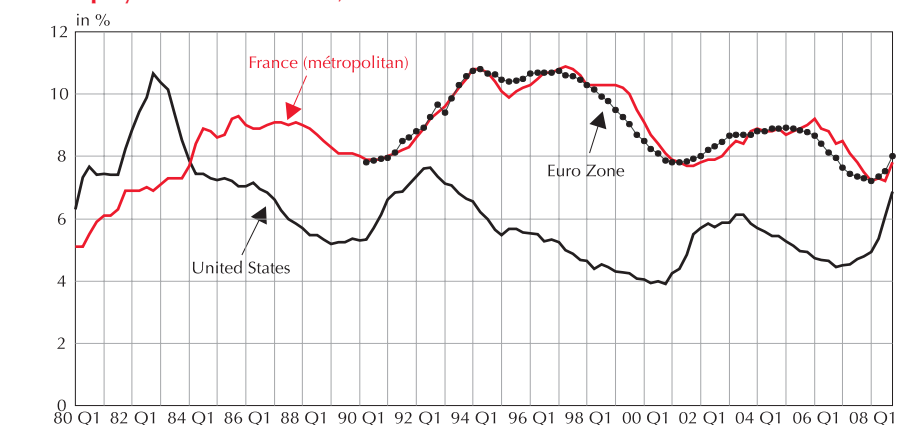
Source: Insee

The unemployment rate rose again

In the wake of the downturn in employment, the unemployment rate, within the meaning assigned by the International Labour Organisation (ILO), started to rise again at the end of 2008, after falling for two years. After peaking at 9.2 points in the first quarter of 2006, it returned to 8.4 points at the end of 2006 and was at 7.5 points at the end of 2007. However, in the last quarter of 2008 the unemployment rate was 7.8%, or almost 2.2 million unemployed persons, and 7.4% on average over the year. Taking the whole of Metropolitan France and its overseas departments into consideration, the rate finally settled at 8.2% at the end of 2008 versus 7.9% and 8.8% at the end of the two previous years.

Most of the developed countries saw a significant rise in unemployment in 2008 (*figure 7*), but in different proportions and with the notable exception of Germany, where employment seems to have reacted later. In the United States, the unemployment rate rose steeply: it went from 4.9% in the first quarter of 2008 to almost 7% in the last quarter of 2008, in other words, the highest recorded level in over 20 years. In Spain, the unemployment rate leaped almost 5 points in a single year.

7. Unemployment rate in France, the United States and the Euro Zone



Source: BEA, Eurostat, Insee.

In France, the rise in unemployment was felt particularly hard by young people aged between 15 and 24: the rate of unemployment for this group rose by almost two points between the third and fourth quarters of 2008 and jumped above the 20% mark, even though it had previously fallen by almost 6 points between the first quarter of 2006 and the first quarter of 2008.

Despite the downswing in the labour market, average per capita earnings held firm

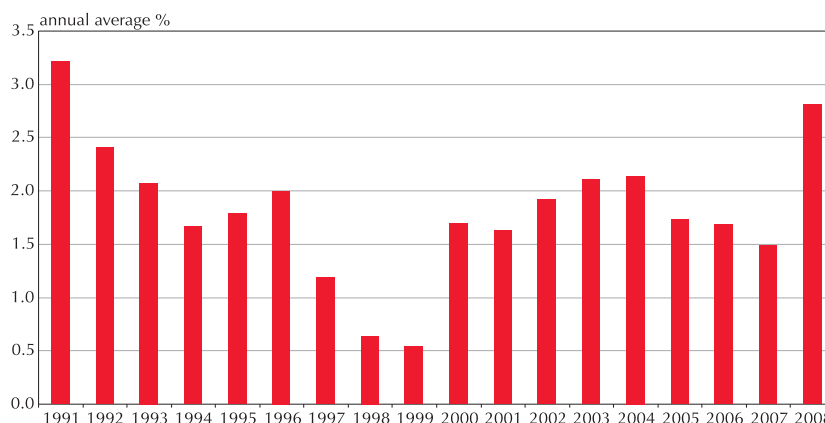
In 2008, the wage bill for the market sector increased at about the same rate as nominal value added. For non-financial companies, the increase in the wage bill had even been slightly more dynamic. The average per capita salary in the non-agricultural market sector went up 2.8% in 2008⁹. Although this was a slight slowdown compared with the two previous years (+3% in 2007 and +3.9% in 2006), this increase is compatible with the average rhythm observed since 2000.

There are several factors that can account for this progression, which remains robust, despite the reversal of the labour market in the course of the year. First of all, until the first quarter of 2008, activity remained dynamic and the unemployment rate showed a decrease. Second, the rise in inflation until mid-2008 (*cf. infra*) forced nominal wages up, thus leading in particular to a faster rate of increase than in 2007 of the SMIC, the minimum growth wage in France (+3.2% between July 2007 and July 2008), an increase that was also passed on to similar wages.

The rise in inflation contributed to the slowing of purchasing power and consumption

After inflation had been stable since 2000 at between 1.5% and 2.1%, in 2008 consumer prices accelerated. The annual average price increase was 2.8% in 2008 (*figure 8*). Nevertheless, inflation still remained well below levels observed before the disinflation of the 1980s.

8. Net rise in inflation in 2008



Source: Insee

9. In the same field, the full-time equivalent salary improved by 2.8% in 2008, after +2.9% and +4% previously.

The significant drop in the price of oil from July 2008 contributed to the fall in inflation

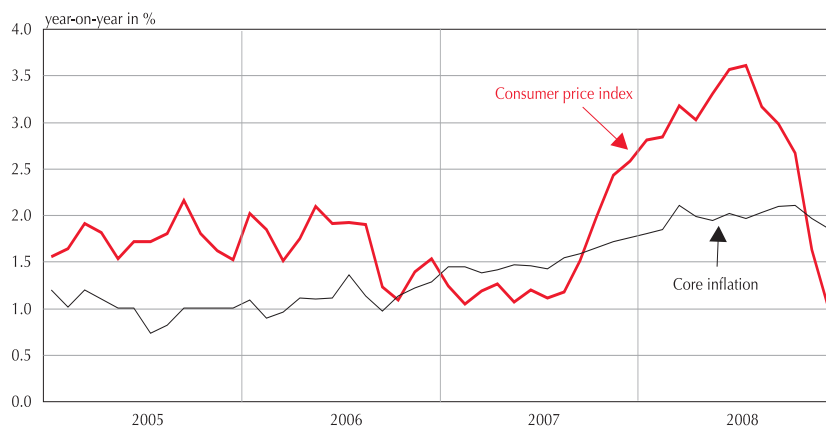
The average annual change in the inflation rate masks a sharply contrasting evolution in the course of the year. Indeed, year-on-year inflation saw a sharp rise, as much as 3.6% in July, dropping back to 1.0% in December 2008 (*figure 9*). This profile was essentially imposed by rising food and energy costs. The explosion of the dollar price of oil (+44% between January and July 2008) pushed up the price of petrol and gas, even though the 7% appreciation of the euro against the dollar over the same period made it possible to reduce this movement somewhat. Also, the surge of almost 62% in the price of food commodities between January 2007 and June 2008 caused major increases in the prices of non-seasonal food products. Since mid-2008, with the contraction in demand worldwide, these prices fell back rapidly, causing a net movement of disinflation. In particular, the price of oil in euros in December 2008 was one third of the July 2008 price and half of the December 2007 price.

On the periphery of these major movements, changes in regulations in the retailing and distribution sector contributed to the decrease in inflation, about 0.2 points off the annual average 2008¹⁰.

Core inflation nevertheless stayed at around 2%

Underlying inflation¹¹, generally more inert, remained around 2% in 2008 (*figure 9*). In fact, increases in the Brent price and the price of food raw materials filtered down only gradually and in moderation to core inflation, causing a rise from 1.8% in January to 2.1% in October. Under the effect of the reversal in the prices of oil and raw materials, excess production capacity and sluggish demand, “core” inflation was back at 1.9% in December 2008.

9. Relative stability of core inflation



Source: Insee

10. Estimate based on the file “Loi Galland and consumer prices” [3] and the research note “Consumer prices”, *Conjoncture in France*, March 2009, Insee.

11. Except public tariffs and products at volatile prices, such as seasonal food products, energy or tobacco, corrected for tax measures and seasonal variations.

After two dynamic years, purchasing power slowed in 2008

The purchasing power¹² of household disposable income slowed considerably, showing a rise of 0.6%, after 3.1% in 2007 and 2.6% in 2006. It stagnated (0.0%) per unit of consumption (box From the purchasing power of disposable income to the purchasing power of “arbitrable” disposable income per unit of consumption). In fact, nominal household income slowed in 2008 (*figure 10*), while over the same period inflation increased.

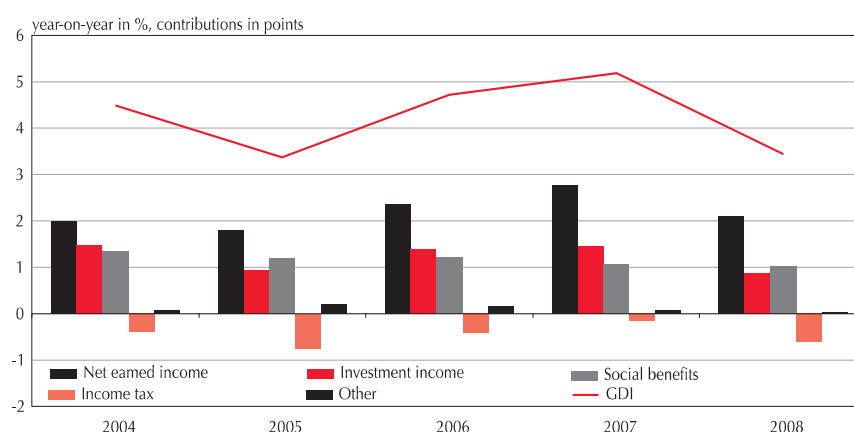
There are three main elements that account for the slowdown in households’ gross disposable income: net earned income (accounts for -0.7 of a point), investment income (-0.6 of a point) and taxes (-0.4 of a point). Social benefits increased at a rate similar to that observed in previous years.

The slowing of activity affected the gross wages received by households and the income of individual entrepreneurs. Conversely, the slowing of social contributions paid by households supported gross disposable income (at around 0.2 point), especially through new exemptions from overtime contributions¹³. In all, net earned income contributed to an increase of about 2.2 points in gross disposable income value for households, after a contribution of 2.8 points in 2007 (*figure 10*).

Moreover, investment income continued to slow. Rents (real or imputed) received by households decelerated (+3.3% compared with +5.9%) when property prices stabilised. Similarly, income from property (interest and received dividends, net of interest paid) was less dynamic in 2008, especially with the slowing of revenue from life insurance.

Lastly, all taxes on income and property (personal income tax, general social contribution, social debt repayment contribution, wealth tax, etc.) paid by households increased at a faster rate than in 2007 (+4.6% compared with +1.3%). This is the after-effect of the decrease in personal income tax the previous year, with the revised scales voted in the finance law 2007.

10. Factors contributing to changes in gross disposable income



Source: Insee

12. For an analysis of the distribution of productivity surpluses, see “Le partage des fruits de la croissance de 1950 à 2008 : une approche par les comptes de surplus”.

13. Law of 21 August 2007 regarding labour, employment and purchasing power.

The slowing of purchasing power affected household expenditure

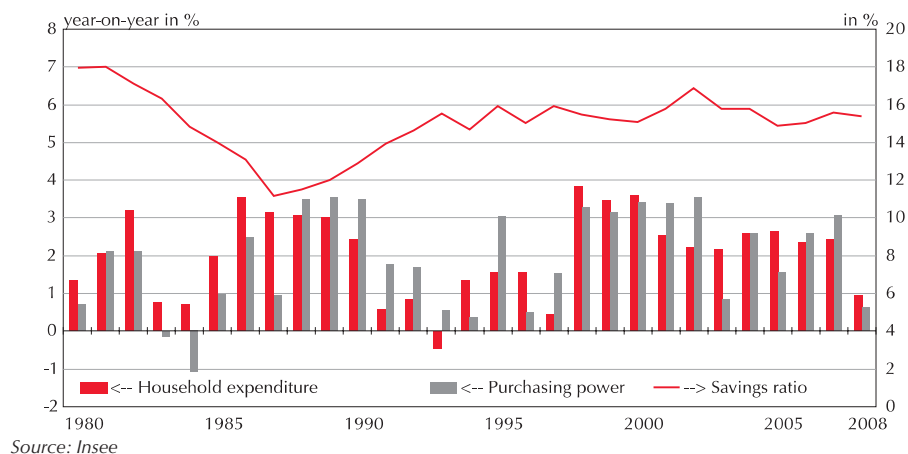
Household expenditure slowed to +1.0% in 2008 (after +2.4% in the previous two years), a rate that was virtually the same as the slowing of purchasing power. Consequently, the household saving ratio changed little: it showed a slight decrease to 15.3%, after 15.6% in 2007, and 15.1% in 2006 (*figure 11*). The relative stability of the savings ratio in French households is in contrast to the scale of the movement observed in the United States: across the Atlantic, the savings ratio increased by 3.4 points between December 2007 and December 2008.

The slowdown in household expenditure in France affected most products. Consumption of non-energy industrial goods, down 0.6% after a 4.9% increase in 2007 is always particularly sensitive to this adjustment as the purchase of many of these goods, especially durables, can easily be postponed or cancelled altogether.

Among durable goods, automobile consumption was down by 3.1% (i.e. a contribution of -0.7 points to the drop in consumption of non-energy industrial goods). The introduction of a bonus/malus scheme based on carbon dioxide emissions when buying a vehicle only served to reinforce households' preference for small cars in 2008. This downsizing led to a more marked decrease in household car consumption¹⁴, than in car registrations (-0.7%).

Consumption of agricultural and agri-food products stagnated (-0.1% compared with +1.2%), in reaction to the major increase in their prices. Energy consumption, after three years of falling prices, increased a little (+0.6%), even though winter and autumn had been colder than the previous year. Expenditure on the consumption of market services, generally not very volatile, decelerated considerably to +1.1%, after +2.2% in 2007 and +2.8% in 2006. Consumption of personal services also stagnated in 2008, after 2.1% in 2007 and 2.4% in 2006 and spending on telephone services also slowed.

11. Savings ratio stabilised



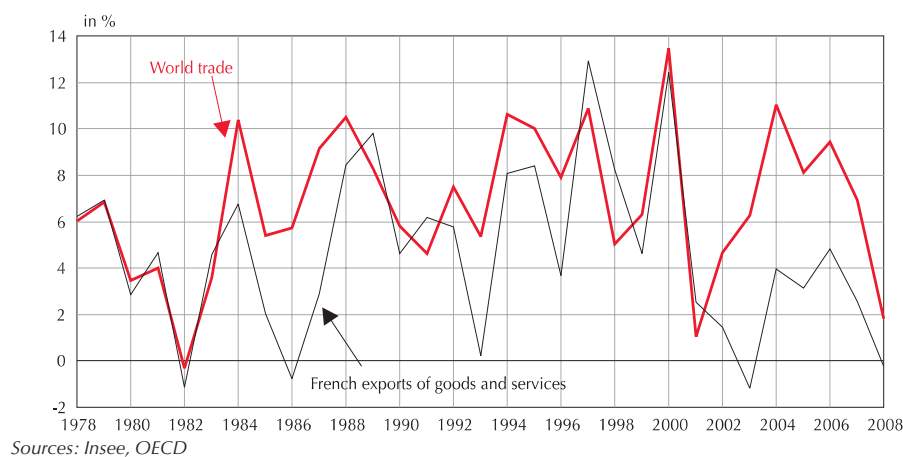
14. Car registrations group together models from the cheaper and more expensive ranges, without differentiating them, however, for the volume of household consumption cars are considered differently, with a model from a cheaper range having a lower weighting.

The dramatic slowing of world trade affected French exports

In 2008, world trade slowed considerably, after being dynamic between 2002 and 2007. This slowdown was all the more marked as the current crisis affected most countries simultaneously, in contrast to what had happened, for example, at the beginning of the 1990s. The dynamism of French exports felt the effects very strongly (*figure 12*). Moreover, the appreciation of the euro in the first part of 2008 affected the price competitiveness of French exporters. Thus all exports of goods and services fell in 2008 by 0.2%, after four dynamic years: indeed, between 2004 and 2007, exports had improved at an average annual rate of almost 4%, which was nevertheless still lower than the rate in Germany and the rest of the Euro zone.

The infra-annual profile was particularly telling in 2008. After a dynamic first quarter, exports of goods and services declined considerably in the second quarter, when world trade contracted slightly for the first time since 2001. This decline increased considerably in the fourth quarter, with import volumes from all France's trading partners shrinking dramatically.

12. Growth in French exports and world trade



Automobile exports plummeted

Most major export items were affected by the slowdown then the collapse of world trade. Exports of non-energy industrial goods dropped by 1.5%, having increased by 2.5% and 6.1% in 2007 and 2006. This decline was mainly due to the drop in automobile exports (-10.9%) and the drop in exports of intermediate goods (-3.8%). Car exports collapsed in the autumn (almost -20% between the third and fourth quarters).

Across the year as a whole, other non-energy industrial goods resisted better. However, this resistance seen in the annual average masked a considerable deterioration at the end of the year, with the exception of capital goods, because of the dynamism of the Airbus deliveries. Overall, because of their importance in the context of French exports¹⁵ as a whole, non-energy industrial goods alone accounted for the fall in exports of goods and services.

15. Exports of non-energy industrial goods represented 67% of all French exports of goods and services in 2007.

Exports from other branches showed a degree of resistance. In services, exports were still up (+2.6%), although this rise slowed. Agriculture and energy exports experienced a recovery in 2008 after two years of decline. Sales in agriculture benefited from a sustained world demand and the grain harvests were good. These sales were up by almost 18%. However, at the same time, exports of agri-food products slowed considerably (+0.5% in 2008, compared with +1.6% in 2007 and +6.3% in 2006).

Slowdown of imports and new deterioration in the trade balance

Imports in the wake of demand

The volume of imports clearly slowed, with an increase of only 0.8% compared with 5.4% in 2007. This development was largely attributable to the reversal seen in imports of manufactured products (*figure 13*). The drop in manufacturing output in particular, an important market for imports of intermediary goods, affected the demand for foreign goods. Thus, imports of intermediary goods showed a drop of 1.9%, after an increase of 5.5% in 2007.

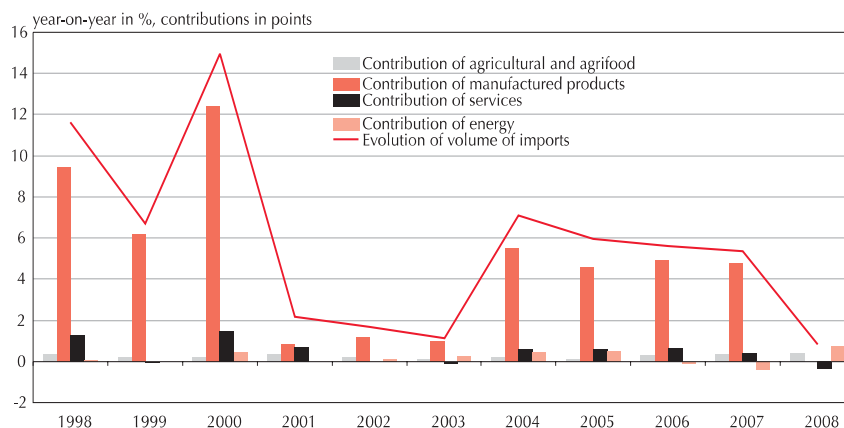
Imports of consumer goods and food products held out and imports of energy products increased considerably

On the other hand, other categories of imports continued to increase slightly. Imports of consumer goods increased by 3.0%, due mainly to a rise in the market share of importers. Imports of energy products recovered (+6.2% in volume) after falling the year before (-3.0%). In fact, the beginning of 2008 was colder than the beginning of 2007, which explains the amount spent on heating. However, the recovery of energy imports made only a small contribution to the increase in imports overall.

Trade deficits widen

With imports still growing and exports decreasing slightly, the balance of foreign trade affected activity in 2008, slicing 0.3 points from the growth of gross domestic product. This negative contribution by overseas trade was nevertheless more marked the year before, at -0.8 of a point.

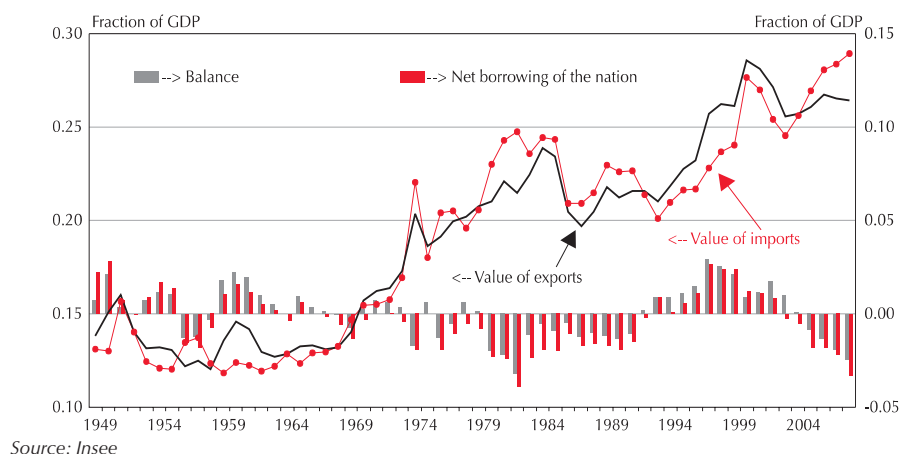
13. Sharp downturn in imports in 2008



Source: Insee

Moreover, 2008 was a year that saw a deterioration in terms of trade: in the wake of the increase in the price of oil, import prices (+4.0% on the average annual figures) rose more than export prices (+2.8% on the average annual figures). Thus the balance of the value of overseas trade increased considerably throughout 2008, extending the trend observed since the beginning of the new century (*figure 14*). The trade balance reached -48.2 thousand million euros, in other words 2.5 points of GDP, a ratio not seen since 1982.

14. Widening of the trade deficit



To the decline in the balance of goods and services was added that of the balance of current transactions: reinvested profits received by French companies from their foreign subsidiaries fell, and this affected the banks in particular. Thus the balance of profits reinvested, which was positive in 2007 (€+1.5 thousand million), became very negative in 2008 (€-10.5 thousand million).

In all in 2008, the nation's net borrowing increased by €22.8 thousand million to reach €642 thousand million, or 3.3 GDP points, a level that had not been seen since the beginning of the 1980s.

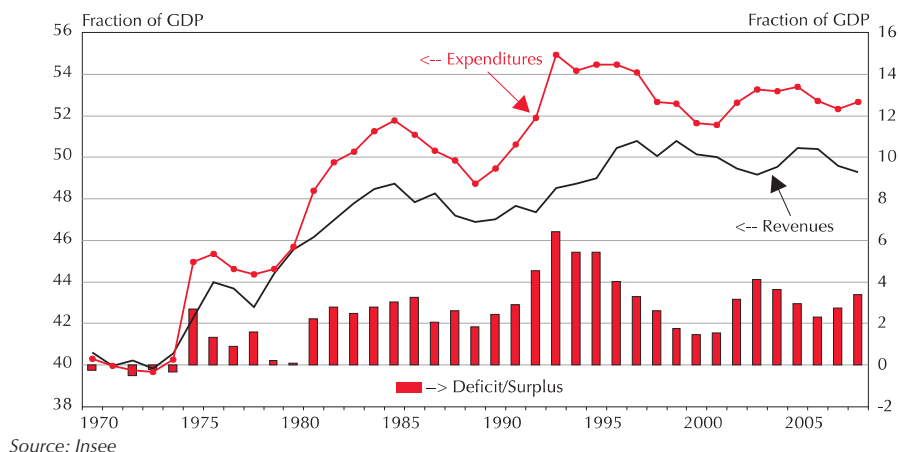
Downswing in public finances

The State deficit widened, leading to an increase in the public deficit in the sense of Maastricht.

Affected by the downturn in activity, the public spending deficit increased in 2008 to 3.4% of GDP, compared with 2.7% in 2007 [2]. This downturn of almost 15 thousand million euros can be explained essentially by a worsening of the deficit of central government. The borrowing requirements of local authorities and the social security administrations also increased, although to a lesser degree: by 0.9 and 0.6 thousand million euros respectively. The social security administrations have in fact remained close to equilibrium: deficits in the general social security scheme and hospitals have almost been compensated for by surpluses in the supplementary pension schemes, self-employed workers schemes, and unemployment insurance schemes.

Revenue increased less quickly (2.3%) than expenditure (3.6%) (*figure 15*). The widening of the public deficit that began in 2007 is therefore continuing and the slight drop in public expenditure in GDP that was started in 2006 has come to an end. The changes in this ratio

15. Net borrowing of general government



remain relatively moderate: for about ten years, the ratio of public expenditure to GDP has oscillated around 53% and the proportion of government revenue in GDP has been around 50%.

Government revenue increased in value by 2.3%

In 2008, the rate of statutory contributions and charges in general government decreased by 0.4 of a point to settle around 42.8%. While the economic downturn began to affect revenue from VAT and corporation tax, the total wage bill in the private sector remained strong, making it possible to protect the spontaneous revenue of the social security administration: without taking changes in tax and social legislation into account, statutory contributions and charges increased by 3.1%, a rate that was very slightly higher in value than the increase in GDP.

The reason for the drop in the rate of statutory contributions and charges can be found in the measures taken to relieve the tax burden. This tax relief, leading to a reduction in GDP of 0.3 of a point, derived from measures taken via the labour, employment and purchasing power law (known in France as the TEPA law). In particular, employee exemption from social contributions on overtime hours brought down social charges paid by households by 2.1 thousand million euros. Reductions on death duties and donations reached 1.5 thousand million euros. Companies also benefited from tax reductions, especially via allowances on professional and business tax.

Expenditure by public administrations increased in value by 3.6%

Central government expenditure grew by 2.6%. Wages paid by the State decreased by 1.3%, under the double impact of the decentralisation of certain posts in education and facilities (accounting for around 1.7 points) and the partial non-replacement of retiring civil servants. On the other hand, the increase in retirement pensions for civil servants remained high (+4.4%), with many opting for retirement. Lastly, interest paid by the State increased by 8.6% in 2008, forced up by the rise in inflation, which automatically increased amounts due for index-linked bonds.

The rise in expenditure was more marked at local authority level. The wage bill increased by 6.4%, partly due to the transfer of skills: comparing like with like, however, the increase remained at 3.7%, a similar rate to the increase in the private sector wage bill. The rise in

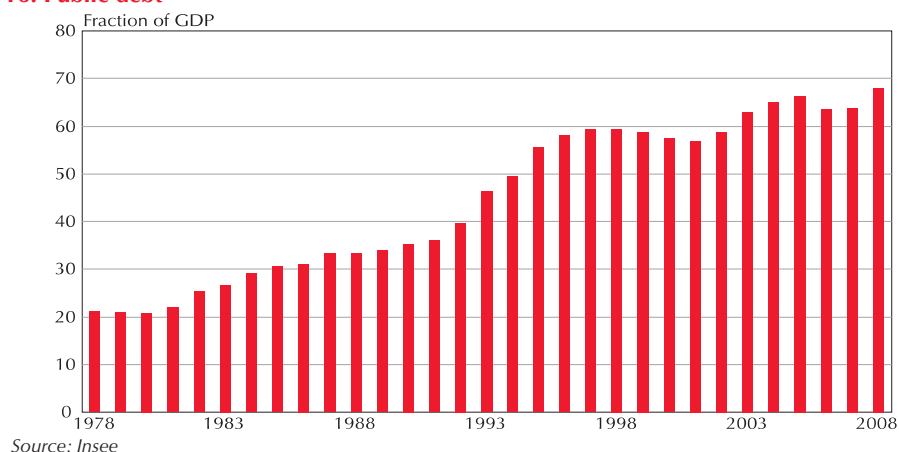
local government expenditure decelerated, however (+3.6%, after a net rise of 7.3% in 2007). Their investment expenditure in particular stabilised in value. Lastly, social security benefits paid by the administration increased by 4.1%, as in 2007. While benefits for the elderly were dynamic (+5.4%), spending on health insurance slowed (+3.4% after +4.0% in 2007) and unemployment benefit stabilised at the annual average.

The public debt was up, with the State's net borrowing combined with some exceptional measures

Public debt in the sense of the Maastricht treaty represented 68.1% of GDP at the end 2008, i.e. an increase of 4.3 points compared with the previous year. The Government's contribution to public debt had notably increased by 4.1 points of GDP, to reach 53.1 points of GDP. Over and above the State's net borrowing, the reason for this rise is the financing of the "Société de prise de participation de l'État", the state shareholding corporation, also the recovery of the debts of the fund providing social security benefits for self-employed agricultural workers (0.4 of a point of GDP) and an increase in the Government's cash-flow of around 0.6 of a point of GDP. Debts owed by various central administration bodies increased by 0.4 of a point of GDP, mainly due to the debt of around 13 thousand million euros (or 0.7 of a point of GDP) owed by the "Société de financement de l'économie française", the finance company of the French economy.

However, aid measures for the financial sector had only a marginal impact on the net public debt¹⁶. In fact, these measures increased central administration's assets while at the same time increasing their liabilities. In all, the net public debt increased rather less than the gross debt, to 61.3% of GDP at the end of 2008 compared with 59.1% at the end of 2007. ■

16. Public debt



16. The net public debt is equal to the public debt in the sense of the Maastricht Treaty minus deposits, credits and negotiable debt securities (valued at their par value) held by public administrations in other sectors.

For more information

[1] Aviat A., Houriez G., Mahieu R., " Les comptes de la Nation en 2008 ", *Insee Première*, May 2009.

[2] Brière L., Guyon T., Izzo P., Poiblanç B., Rodriguez E. Uteza A., " Les comptes des administrations publiques en 2008 ", *Insee Première*, May 2009.

[3] Guerrero G., " Loi Galland et prix à la consommation ", *Note de conjoncture Insee*, June 2008.

[4] Insee (2008), " Les salaires en France ", Collection Références, édition 2008, September.
