

Review of 1999

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With the strength of the rebound observed following the “air pocket” that struck during Q1 1999, the robustness of the expansion phase in progress for three years was apparent during that year. The impression of a slight downturn, year-on-year, resulting from the 2.7 percent increase in GDP on an annual average (as against 3.2 percent in 1998) should be considered in light of the GDP yoy growth rate of 3.2 percent, which exceeded each of the two preceding years in this recovery phase. This approach enables us to understand the exceptional strength of job creation (370,000 in the trade sector, and a total of 465,000) and the subsequent reduction in employment of nearly one point.

As is true for the prior year, the increase in economic activity, analysed through accounting contributions to growth, was almost totally based on domestic non-inventory demand. Household consumption remained dynamic—indicative that France has once again outperformed its neighbours in cultivating the virtuous cycle of employment, consumption, and growth. Of particular interest is the housing sector, in which vigorous demand, generated by attractive interest rates and economic policy measures, sustained activity throughout the year. Even with its continued low average contribution to growth, foreign trade was the main factor in the accelerated activity that began in Q2, with an increase in exports of nearly 10 percent per annum. Further, entrepreneurs' expectations were stimulated by the perceived end of the world trade slowdown. Accordingly, the rapid world trade recovery is therefore the first response to the question that comes to mind when reviewing 1999: why didn't the slowdown during H2 1998, accompanied with a vigorous reversal in expectations, lead to a substantial economic slowdown as it did in 1995? Or why did the Asian crisis result in a mere air pocket?

Two types of arguments can be developed: first, with its direct damping effects on interest rates and inflation, the Asian crisis entailed factors to stimulate demand in developed countries that offset the more visible effects—primarily the world trade slowdown—on the industrial apparatus. According to the second argument, the creation of the euro zone made Europe more

resistant to external shocks. During earlier crises, slowed growth was amplified by exchange rate fluctuations between European currencies, and perhaps further accentuated by interest rate increases intended to limit such fluctuations.

This bulletin includes a detailed account of 1999. The year ended has three distinguishing features:

- First, a strong rebound of economic activity that made it possible to restore an annual growth rate of over 3 percent from Q2;
- Second, as discussed, substantial job creations—with 465,000 new jobs, 1999 marks the best performance in the past 50 years; and
- Third, the revival of inflationary pressures. Although these pressures are still moderate (except in construction and public works), 1999 marks a return of the upward trend in physical pressures, inflation, and interest rates.

Vigorous recovery in economic activity

Contrary to the preceding year, the profile for 1999 shows accelerated activity, with a growth rate of just under 4 percent per annum from mid-year. This trends reflects developments in manufacturing production: up slightly during Q1 (as an extension of H2 1998), with resumed growth of just under 6 percent per year during Q2, primarily as the result of increased exports, as well as a substantial increase in non-inventory domestic demand (particu-

larly consumption) since the beginning of the year. It is true that the Asian crisis never did affect household expectations, as the French only seem to be sensitive to decreased unemployment and increased purchasing power generated by imported disinflation. Further, enterprise investment only reversed slightly at the beginning of the year, as if entrepreneurs had always believed that the slowdown would not last long. We observe similar indications in job creation trends. Contrary to the situation registered in 1998, the contribution of foreign trade is slightly positive, with a somewhat faster resurgence in exports than in imports. Another factor of symmetry in respect of the preceding year, the inventory contribution to growth is negative in 1999. There are two possible explanations for these findings. At the beginning of the year, low input price levels and less dynamic demand led to a rundown on inventories; while the negative contribution of inventories during the second half of the year seems to be associated with vigorous development in demand, particularly in connection with exports.

The non-industrial sectors (services, trade) generally registered accelerated activity during the year, with their sensitivity to the spill-over effects from industry. The construction and public works sectors, which had an excellent year, merit special mention. Housing demand, already active in 1998 as the result of lower interest rates, was clearly bolstered by the full implementation of the Périssol scheme, which required a purchase by end-August 1999 to qualify. The rise in demand was reflected by a wave of housing starts reaching 310,000 for the year. Construction activity during H2 was strengthened by VAT reductions.

New record year for job creations

From Q1 on, growth in employment evidenced surprising strength, seemingly unfazed by the "air pocket." This growth increased at the end of the year, and for 1999 as a whole, appears to be exceptional: 465,000 jobs created (as against 385,000 in 1998), including 370,000 in the business sector. Most (320,000) of these jobs are situated in the tertiary trade sector. However, positive trends were also registered in construction—as the result of its sustained activity and industry—despite its dip at the beginning of the year. Growth in employment in 1999 resulted primarily from strong economic performance, while H2 was characterised by the first appreciable effects of the reduced work schedule. We should also point out the continued low level of apparent labour productivity (an annual average of 0.6 percent, 0.9 percent year-on-year, in the trade sector).

Of course, despite a greater increase than the preceding year in labour supply, 1999 was also an exceptional year in terms of reducing unemployment. With regard to unemployment as defined by the International Labour Office, the decrease was 256,000 unemployed for the year—primarily benefiting young persons under 25 years of age.

A return of inflationary pressures

1999 is a milestone in the cycle that began at end-1996, as 1999 is the year when pressures become more evident and inflation begins an upward trend—a classic characteristic of the maturation phenomenon. However, the levels reached at

end-1990 in these two areas are not sufficient to affect the continued expansion phase in the short term. In fact, the only sector registering real pressures is construction, where production bottlenecks have increased substantially, particularly as the result of recruitment problems, with levels comparable to those registered during the early 1990s. We can therefore rule out the short-term existence of a constraint on the level of activity in the sector. In addition, the pressures in the construction sector are clearly reflected by accelerated housing prices. In industry, only the automotive sector faces production bottlenecks. Despite a highly active market, prices do not appear to be accelerating. The only repercussion of the pressures is a vigorous increase in investments in the sector in 1999 and, according to builders' projections, in 2000. Considering industry as a whole, the production capacity utilisation rate—up for the year as a whole—at end-1999 is approximately two points above its average long-term level; however, it is also two points below its peak in early 1990.

Annual consumer price drift increased from 0.2 percent in January to 1.3 percent in December. This acceleration reflects the recovery of oil prices, with underlying inflation stabilised in the vicinity of 0.7 percent. Trends in 1999 should therefore be no cause for concern with regard to short-term inflationary trends, to the extent that oil prices are likely to stabilise. However, the strength of world activity has also bid up the prices of other industrial inputs. The outlook of medium-term inflation resulting from the combination of rising import costs and pressures has promoted a gradual increase in long-term rates, as well as enhanced vigilance on the part of the monetary authorities. ■