

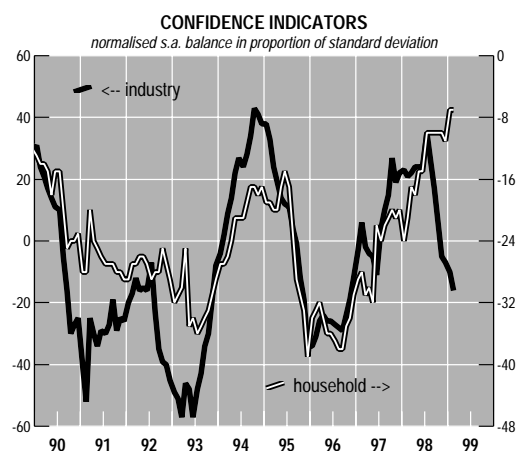
# 1998 in retrospect

*Despite the Asian crisis, 1998 prolonged the upswing begun in mid-1996 and produced the best results of the decade to date: 3.2% growth, 400,000 job creations (including 300,000 in the market sector) accompanied by a fall of almost one point in the unemployment rate.*

The growth in activity was based entirely on domestic demand, in contrast to 1997, when foreign trade had contributed more than half the year's growth. Household consumption turned out to be particularly lively, thanks to a purchasing-power rise of more than 3%. The impact of the Asian crisis was to be seen not so much in the yearly average as in the pattern over time during the year, marked by a gradual slowdown reflecting the appreciable levelling off in industry. But the year 1998 had other exceptional features, partly the secondary effects of the Asian crisis:

- the price rise reached an historic low: 0.3% year-on-year for 1998 as a whole at consumer-price level (1.1% in 1997). From this standpoint, the last two years differ markedly from previous upswings by reason of the absence of inflation. Over and above the impact of the fall in commodity prices -- and especially fuels -- what was seen was stability for underlying inflation at an annual rate of close to 1%;
- short-term and long-term interest rates returned to historically low levels. This evolution was linked both to the slowdown in prices and to the flow-back of capital due to the Asian crisis. These falls in rates, which were favourable to domestic demand (notably for housing), like the disinflation, which increased purchasing power and hence consumption, cushioned the direct impact of the Asian crisis on French growth.
- the direct and indirect effects of the Asian crisis are to be seen in the divergent evolutions for individual sectors. Industry, which had been the first to profit from the upturn, steadily lost momentum in 1998, whereas distribution and services saw growth accelerate between one year and the next, while construction showed continuous acceleration, returning in H2 1998 to distinctly positive growth;
- the final particularity of 1998 -- one that had already been seen the previous year -- was the scale of job creation in the market sectors and the relatively small rise in labour productivity. This meant that the decline in unemployment that had begun the previous year continued, despite a substantial rise in the labour force.

Before going on to describe in more detail the sequence of events during the year, it should be noted that French growth was slightly above the average recorded by its euro-zone partners. This was due to a more substantial increase in household consumption in France. It should also be noted that the deterioration in industrial leaders' expectations took place somewhat later in France, per-



haps because French exporters were less exposed to the Asian crisis -- and later the Russian crisis -- than their Italian or German counterparts.

## Gradual slowdown in industrial activity

Growth in manufacturing output, which was of the order of 6% at annual rate early in the year, fell back to 2% in H2 1998. As in the previous year, the annual average increase in production was 5%. However, the rise in value added in manufacturing industry (4.0%) no longer contributed more than one-fifth of the growth in French activity, compared with two-fifths in 1997. The slowdown in industrial output was due, first of all, to the levelling off in exports, whose year-on-year increase eased from 16% in 1997 to 3% in 1998. Indeed, the external-trade contribution to growth turned negative as of early 1998. The slowdown is also linked to the levelling off in corporate domestic demand from the summer on. While the contribution of investment to growth remained substantially positive, that of inventory changes turned out to be slightly negative on a year-on-year basis over the year. Business surveys show that the overall slowdown in manufacturing output as a whole masked widely-differing sectoral tendencies. For example, the intermediate goods sector was from the start of the year severely affected by the deterioration in the international climate. In contrast, for the consumer goods industries the fall in orders took place only in the summer, and only in Q4 in the case of capital goods. Meanwhile, the car sector, buoyed up by the revival of new registrations on the French market, maintained its upward momentum throughout the year.

The non-industrial sectors, whose recovery had taken place after that of industry in 1997, made substantial progress last year. Output in both distribution and

non-financial services rose by 5.0% in 1998, compared with 2.3% and 2.8%, respectively, in 1997. 1998 also saw a return to substantial growth in output from the construction sector (2.1%, as against -0.4% the previous year) that was particularly marked in H2. The continuing expansion of private investment in housing, which in 1997 had mainly produced a fall in existing stocks, finally led to an increase in starts, all the more so as the outlook remained favourable, with interest rates still low.

### A record year for job creation

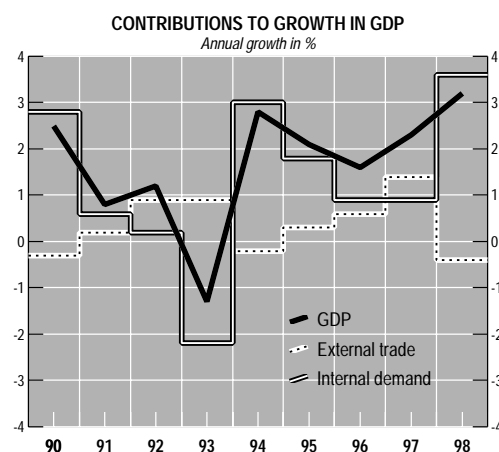
Dependent employment, which had profited at an early stage from the upturn, continued to expand in 1998, the pattern over time tracking that of activity: particularly strong in H1 (170,000 jobs created in the market sector), and then a slight slowdown in H2 (130,000) with the ending of net job creation in industry. 1998 turned out to be particularly productive in terms of job creation, with total employment rising by around 400,000 (net). This result was considerably aided by job creations in the non-market sector, due notably to the special youth-employment programme. Given this exceptionally favourable tendency in numbers employed, unemployment naturally continued the downward movement begun at the end of 1997. A steady decline brought the rate down from 12.2% in December 1997 to 11.5% in December 1998, the main beneficiaries being the under-25s.

### Growth shielded by household consumption

In accounting terms, the 3.8% rise in household consumption contributed three-quarters of overall growth in 1998. By favouring sectors that create substantial numbers of jobs, it participated in a virtuous spiral which kept activity going despite the Asian crisis. The rise in consumption in 1998 took its origin first from a very steep increase in purchasing power (3.5%) linked to the expansion of earned income and disinflation. It was also helped by a slight fall in the saving ratio, attributable to the steady improvement in household opinion regarding the economic situation and especially the future evolution of unemployment. It also benefited, however, from two one-off factors: a marked upturn in the car market following the period depressed by the ending of the car-scrapping bonus, and the World Cup, which had a direct impact on sales of "brown goods". Lastly, consumption also benefited from the spread of innovative products (mobile phones, PCs) to a wider public.

### Rising investment

Corporate investment rose by 6% in 1998 (compared with 0.1% in 1997). The growth rate was particularly strong in H1 (of the order of 8%) but was then halved in H2. Investment in H1 was all the stronger because



in 1997 it had responded only after a certain time-lag to the upturn in activity. Thereafter, the deterioration in businessmen's expectations limited the implementation of new investment projects. This tendency was particularly felt in industry. However, the downturn was only moderate, thanks to the maintenance of satisfactory conditions for the financing of investment, in terms of both interest rates and the level of self-financing. As a result, investment in industry rose by 8% in 1998 after stagnating in the two previous years. This movement can be linked to a distinct rise in the productive capacity utilisation rate, which throughout the year 1998 moved back closer to its long-term average.

### Sharp reduction in inflation

1997 had already been atypical in that the marked acceleration in activity had not been reflected in an upturn in inflation. The year 1998 presents an even more paradoxical picture. The strongest annual growth this decade was accompanied by a fall in the year-on-year consumer price rise to the historically low level of 0.3% (1.1% in 1997). This fall was linked to the collapse in commodity prices and especially that of oil, which is a direct consequence of the recession in Japan and in the emerging countries of Asia and Latin America. Meanwhile, underlying inflation remained stable at around 1%. Despite the strength shown by consumption, the year-on-year price rise for manufactured goods remained close to zero. Granted, industrial firms' selling prices have been steadily declining. Only the prices of private services and rents showed increases and even these were modest. In the first case, the year-on-year rise levelled off at 2%; in the second, there was a slight increase from 1.6% at the end of 1997 to 2.1% in December 1998, most of the acceleration taking place in H1. ■