



# **CONJONCTURE IN FRANCE**

## **December 2013**

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# A laboured recovery

*As forecast in Conjoncture in France in October, activity in Q3 2013 remained disappointing on the whole in emerging economies and dynamic in advanced economies. Foreign demand for French products decelerated, notably due to the marked slowdown in the imports of our European partners.*

*In Q4 2013, the business climate shown in the business tendency surveys continues to improve in all the advanced economies, suggesting that the upturn is likely to continue. In particular, activity in the Eurozone looks set to continue growing over the forecasting period (+0.3% each quarter), thanks to moderation in fiscal consolidation, an upturn in investment after a very marked adjustment and a fall in precautionary saving by households. In the emerging economies, situations vary but there is unlikely to be any clear improvement in growth on the whole.*

*Over the forecasting period, foreign demand for French products is likely to return to a sustained and regular rate of growth by mid-2014. However the profile of activity in France should be relatively uneven, with a progression in GDP of 0.4% in Q4 2013, then 0.2% in Q1 and Q2 2014.*

*The expected dynamism in Q4 should be driven by a combination of several effects. First of all, positive after-effects are expected in investment by companies in services and in exports of manufactured goods, which fell much more in Q3 than their determinants would have suggested. Households are also likely to bring some expenditure forward due to the release of employee-savings, the stricter terms on the automobile ecological "bonus/malus" system as of 1<sup>st</sup> January and the rise in VAT rates on 1<sup>st</sup> January 2014.*

*This expected rebound in Q4 is confirmed by the activity data available to the end of October and by the business tendency surveys: the business climate*

*improved sharply in Q3 in all sectors. However, the standstill in balances of opinion over the last two months, notably due to the downturn in personal activity prospects declared by entrepreneurs, suggests a slowdown in early 2014 as a result of the lack of dynamism of the various components of demand:*

- *the upturn in activity prospects will support investment, but its progression is likely to be held back by the absence of a recovery in construction.*

- *despite improvements on the employment front in 2014, household purchasing power is likely to be lacking in impetus. On the one hand, the rise in total employment should remain weak: the CICE tax credit for businesses should drive growth in employment but the upturn in activity is unlikely to be sufficient to allow an upturn in market-sector employment. In addition to this, the gains in real wages observed in 2013 due to the unexpected fall in inflation are likely to fade out in 2014. The result is that household consumption should barely progress in H1 2014.*

- *in H1 2014, exports should be less dynamic than foreign demand, hit by the past rises in the Euro and by the downward trend in market share, although the latter has eased since the crisis.*

*This scenario is subject to a number of uncertainties. French exports could turn out to be more dynamic, in particular if the return of confidence is confirmed among our partners in Southern Europe. On the other hand, the scale in the upturn in investment by companies is always uncertain in recovery phases. Our scenario is based on that upturn being rather slow in France, but it could even be postponed altogether due to modest growth expectations. ■*

### Activity remained dynamic in the advanced economies in Q3 2013

*Activity remained dynamic in the advanced economies in Q3 2013*

In Q3 2013, growth in the advanced economies was slightly stronger (+0.5% after +0.6%) than expected in Conjoncture in France in October 2013 (+0.4%). Activity remained dynamic in the United States (+0.9% after +0.6%) and in the United Kingdom (+0.8% after +0.7%). However, activity slowed down in Japan (+0.3% after +0.9%) and in the Eurozone (+0.1% after +0.3%).

*The end of the recession confirmed in the Eurozone*

In Q3 2013, GDP in the Eurozone progressed by 0.1%, confirming that it is emerging from recession. The slowdown compared to Q2 (+0.3%) was due to a fall in exports affecting all the countries in the zone. Private consumption also slipped, notably in Germany.

*The emerging economies accelerated slightly*

In the emerging economies, activity would appear to have accelerated, mainly in China and the CEEC. The rate of the progression in activity in emerging countries nonetheless remained below its pre-crisis level (+1.7% on average from 2000 to 2008).

### In France, activity fell back slightly in Q3 2013

*French GDP fell slightly in Q3 2013*

Activity fell back slightly in France in Q3 2013 (-0.1% after +0.5%). The fall was more pronounced in manufacturing industry (-1.0% after +2.0%), due to the sharp fall in its exports (-1.9% after +2.8%). Production of market-sector services also slipped (-0.1% after +0.7%), held back notably by the manufacturing branch. In addition to this, by a backlash after the first half of the year when lower-than-normal temperatures buoyed household spending on heating, production of energy showed a marked fall in Q3 (-1.5% after +2.1%). Finally, activity in construction continued to contract (-0.5% after -0.6%), in particular production of new buildings, while housing maintenance showed a slight upturn.

### World trade set to be dynamic and oil prices high through to mid-2014

*World trade set to be dynamic through to mid-2014*

World trade in goods accelerated sharply in Q3 2013 (+1.1% after +0.3%). While trade in advanced countries slowed down distinctly, especially in the Eurozone, trade in Asia showed an upturn. Through to mid-2014, trade should progress by 1.5% per quarter, coming close to its average pre-crisis growth as the economic situation improves in the advanced economies, particularly in the Eurozone, and the emerging economies recover some of the dynamism that was on hold in H1 2013.

*Despite a physical market low on tensions, the price of oil should remain high*

In Q3 2013, the oil price increased markedly, driven by geopolitical tensions in the Middle East, which culminated at the end of August. These tensions have largely eased and the price of Brent has returned to its springtime plateau level (\$110). In Q4, tensions should remain low on the physical market as demand declines in advanced countries. In H1 2014, despite the difficulties encountered by several OPEC countries, world oil supply should be dynamic, driven by continuing sustained production in the United States and stronger production in Russia, Central Asia and Latin America. The expected increase in oil supply (+1.3 million bpd year on year) should therefore cover the foreseeable increase in demand through to June 2014. The price per barrel is forecast to remain at \$110.

### The outlook should remain more positive in the advanced economies through to mid-2014

*The upturn should continue in the advanced economies*

In the advanced economies, the global outlook improved markedly this summer, is still positive in November and activity should remain dynamic through to mid-2014 (+0.4% in Q4 2013, +0.5% in Q1 2014 and +0.3% in Q2). In the United States, household consumption and corporate investment should continue to buoy up activity, although the rise in interest rates could trigger a slowdown in the property market and public consumption is likely to contract in Q4 under the effect of the shutdown. The Japanese economy should grow quite clearly



at the end of 2013 and beginning of 2014, but slow down in Q2: the 3-points rise in VAT on 1<sup>st</sup> April is likely to cause a fall in consumption in Q2 2014, although it should encourage households to bring some purchases forward to earlier quarters. In the United Kingdom, the recovery should remain strong: investment and consumption should show a marked upturn, thanks notably to the recovery of the property market. In the Eurozone, the easing of fiscal consolidation, improved expectations and the need to renew production capacities should allow moderate growth, despite a labour market that remains weak.

## Divergences continue between the emerging economies

Since August, according to the surveys in emerging economies, overall activity should see some impetus restored. Having said this, the divergence observed in H1 2013 is likely to continue (see Graph 1). In China, growth is set to hold up: in the short term, the easing of restrictions on lending is supporting the upturn in the property market and driving activity as a whole. The economies to the east of the Eurozone should benefit from the European recovery, meanwhile. Conversely, in the other emerging economies, according to the surveys, the outlook worsened considerably this summer and remains at a low level, in particular in manufacturing. In parallel, tighter monetary policies coupled with sharp falls in currencies in the countries with large current account deficits (India, Brazil, Indonesia, Turkey) are likely to weigh heavily on debtors who have a lot of debt in dollars, and activity should stall.

## The Eurozone should return to growth

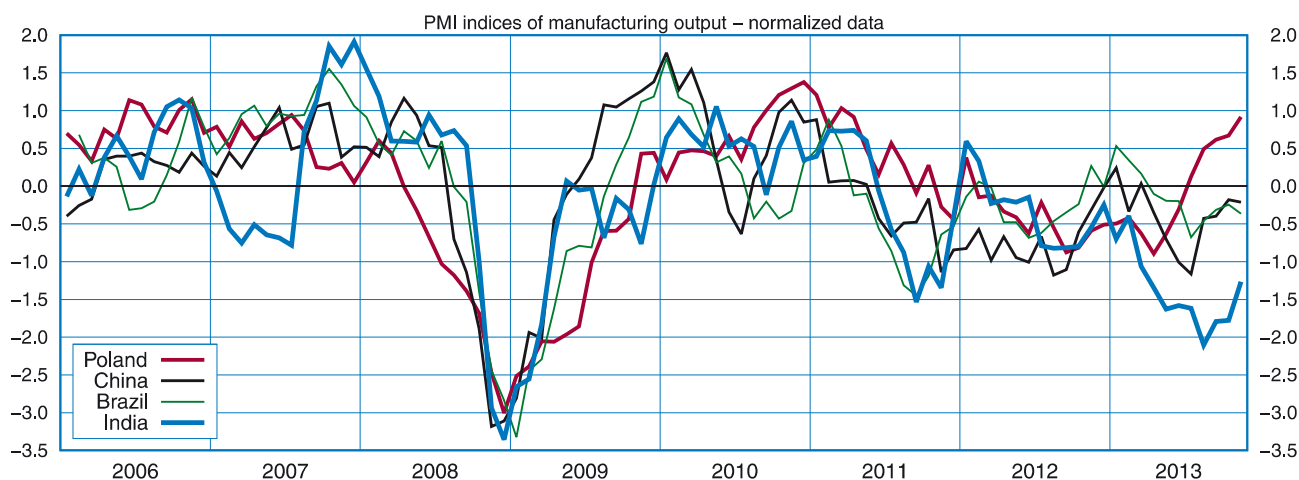
### Financial terms remain accommodating

Financial terms remain accommodating in the advanced economies. The rise in long-term rates observed over summer 2013, a consequence of uncertainty as to the continuation of US quantitative easing, has even been partially erased. While those countries that are perceived as being financially sounder continue to enjoy excellent financing terms on their sovereign debt, interest rates are falling in other countries that have known greater difficulties since the beginning of the European sovereign debt crisis (Ireland and, to a lesser extent, Spain and Italy).

### The ECB continues to support the money market

In the Eurozone, monetary policy remains expansionist in order to maintain access to liquidity for European banks. At the beginning of November, in particular in response to the low level of inflation in the Eurozone (+0.7% in October), the ECB decided to cut its main base rate by 0.25 points to 0.25%. The ECB also declared that it was ready to intervene if tensions should emerge in interbank financing, including by a further very long-term refinancing operation similar to those in December 2011 and February 2012.

**1 - Divergences among emerging countries**  
Last point: November 2013



Sources: Markit, INSEE calculations

## General outlook

*Business tendency surveys show continued improvement in the Eurozone*

In the Eurozone, according to the surveys, the outlook has been improving since mid-2013. The business climate in industry has been in the expansion zone since October (see Graph 2), for the first time since 2011. Eurozone activity should therefore see some impetus restored through to mid-2014 (+0.3% per quarter), driven in particular by internal demand against a backdrop of easing fiscal consolidation. The divergences in outlooks within the Eurozone should be reduced somewhat: activity should be dynamic in Germany and, to a lesser extent, in France, while Spain should gradually catch up with their growth rate. In Italy, however, activity should progress only weakly.

*Consumption set to increase slightly in the Eurozone*

In the Eurozone, fiscal consolidation should become less intense, the fall in employment should ease and nominal wages should progress again modestly through to mid-2014, with rises in Germany, stability in Italy and Spain (where the reintroduction of the fourteenth month of wages in the Spanish civil service is set to make wages increase sharply at the end of 2013, however). The fall in purchasing power in the Eurozone should therefore ease by mid-2014 and, as activity and employment prospects improve, households are likely to cut back their precautionary saving. All in all, consumption should increase slightly in the Eurozone.

*Corporate investment should accelerate in the Eurozone*

Tightening of lending terms has come to an end in the Eurozone since the start of 2013, except in Italy. In Spain, terms even eased for the first time since 2010. This improvement should continue and spread to Italy. In addition, the gradual acceleration in activity expected by entrepreneurs in their answers to the outlook surveys and the need to renew production capacities after a marked phase of adjustment should support the acceleration in investment.

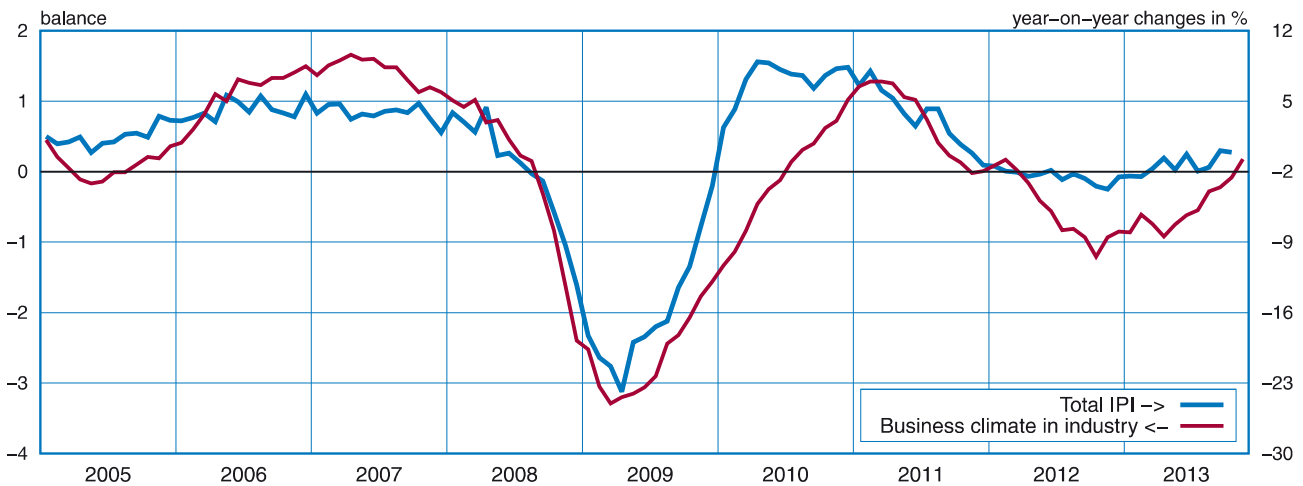
*The upturn in advanced economies should buoy up French exports*

### Moderate progression in French exports

Through to mid-2014, world trade should return to a growth rate close to 1.5% per quarter. Buoyed by the advanced economies, world demand for French goods and services should also be dynamic at +1.3% per quarter on average (see Graph 3). After a sharp increase at the end of 2013 (+2.3%) linked to an expected return to normal of aeronautics exports, French exports should only grow moderately in early 2014 (+0.7% per quarter), again hit by the past rise in the Euro and by the downward trend in market share.

## 2 - In the Eurozone, business tendency surveys have been improving since mid-2013

Last point: October for IPI and November for business climate



Source: European Commission

**In France, activity set to rebound at the end of 2013 and slow down in early 2014**

*The business climate has stabilised over the past two months and remains below its long-term average*

After a marked rebound in all sectors, the business climate in France has been stable in October and November (at 95), 11 points above its level in May but still below its long-term average (see Graph 4). This pause in the outlook surveys can be seen in industry (at 98 since August), building (94 in November and October), wholesale trade (98 in November after 97 in September) and retail trade where the compound indicator even slipped back again (95 in November against 101 in September). The improvement continued, however, in services (96 in November after 93 in October).

*Past activity judged more favourable than prospects*

More precisely, in manufacturing industry, responses on activity prospects improved clearly in October and November, announcing a rebound in production in Q4 2013. This diagnosis is confirmed by the progression in October of the manufacturing production index, showing a growth overhang of +0.4% for Q4 2013. Conversely, entrepreneurs report a downturn in their personal production prospects and their opinion of their order book levels remains negative.

*The French economy set to rebound in Q4 2013 and slow down in H1 2014*

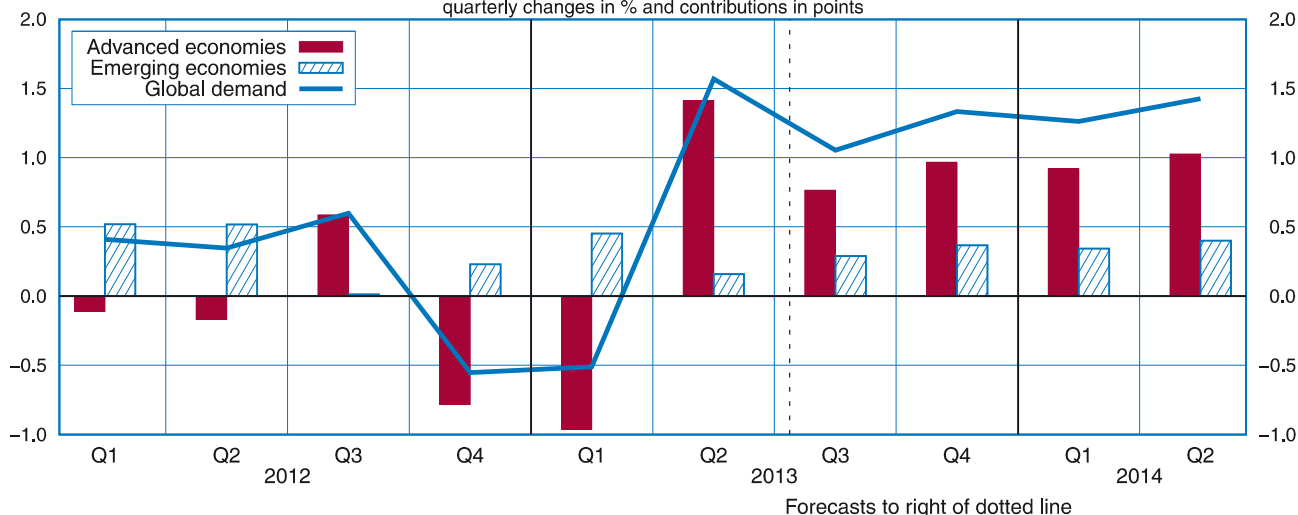
Manufacturing production should therefore rebound in Q4 2013 (+0.8% after -1.0%), before slowing down in H1 2014 (+0.2% per quarter). Activity in market-sector services should remain relatively dynamic (+0.5% then +0.3% and +0.4%), according to entrepreneurs in services surveyed in November. Energy production should fall back slightly in Q4 2013 (-0.3%), as household heating expenditure fell in October due to high temperatures. It should rebound by a backlash in Q1 2014 (+1.0%), before returning to an average rate in Q2 (+0.7%) if temperatures remain in line with seasonal norms. Finally, activity in construction should level out in Q4 2013 (0.0%). Housing starts rebounded strongly at the start of the year and some home maintenance expenditure is likely to be brought forward in anticipation of the rise in the VAT rate on 1<sup>st</sup> January 2014. The trend in building permits has been declining, however, since the start of 2013 and the number of starts fell again in Q3, suggesting a likely fall in production in H1 2014 (-0.3% then -0.5%). All in all, the French economy should rebound in Q4 (+0.4%), before slowing down in H1 (+0.2% per quarter).

*GDP to show a growth overhang of +0.7% in mid-2014*

In mid-2014, GDP is set to show a growth overhang of +0.7%, after annual growth of +0.2% in 2013 and 0.0% in 2012. The acceleration in activity expected in 2014 should be driven in particular by manufacturing industry (overhang of +1.0% in mid-2014 after +0.5% in 2013 and -2.8% in 2012).

**3 - World demand for French goods and services buoyed by the advanced economies**

quarterly changes in % and contributions in points



Source: INSEE, Tresor, Central Plan Bureau

### Total employment should progress and unemployment be close to stable through to mid-2014

*Market-sector employment set to level out through to mid-2014*

Due to the past weakness of activity, employment in the non-agricultural market sectors fell again in Q3 (-16,000). Under the effect of the return of growth and the CICE Tax Credit for Encouraging Competitiveness and Jobs, the fall in market-sector employment should gradually ease through to mid-2014 (-7,000 in Q4 2013 then -4,000 in H1 2014, *see Graph 5*).

*Total employment should progress through to mid-2014 due to subsidised jobs*

After +80,000 jobs in 2013, non-market-sector employment should continue to progress in H1 2014 (+33,000 jobs), driven essentially by subsidised contracts. Despite a fall in the number of new contracts indicated in the draft Finance Law for 2014, the increase in the average duration of integration contracts should allow a further rise in the number of beneficiaries in H1 2014 (+40,000 after +116,000 in 2013). Total employment should thus progress in Q4 2013 (+52,000), and again in H1 2014 (+36 000).

*Unemployment should be almost stable through to mid-2014*

The unemployment rate was 10.9% of the active population on average in Q3 2013 (10.5% in Metropolitan France), up 0.1 points on the previous quarter (revised downwards).<sup>1</sup> Through to mid-2014, the unemployment rate should increase by 0.1 points to 11.0%. Over the forecasting period, net job creations are unlikely to be sufficient to absorb the rise in the active population (+113,000).

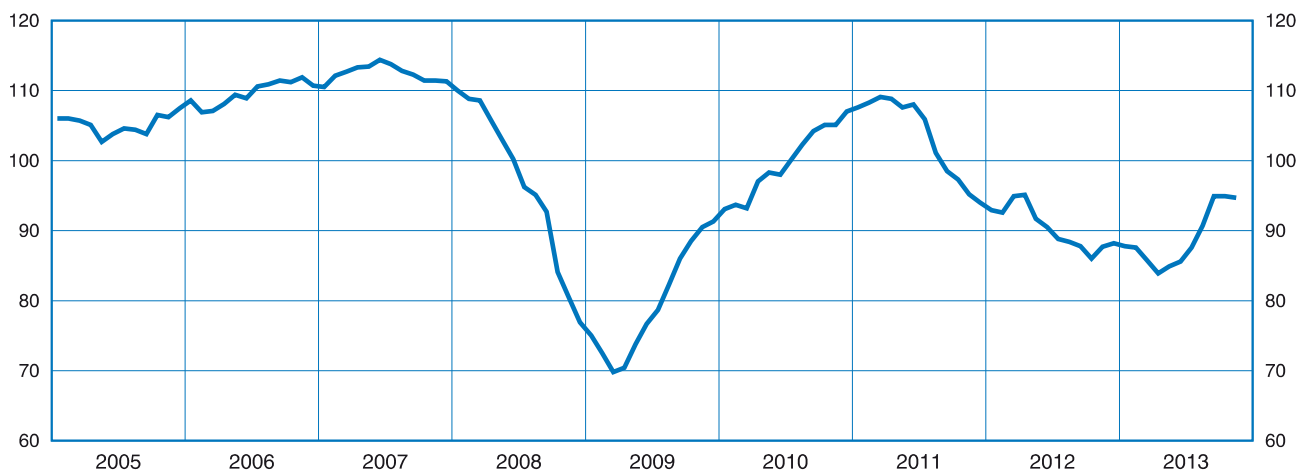
### Inflation set to rise to mid-2014

*Inflation set to rise to mid-2014*

Headline inflation should increase progressively through to mid-2014 under the effect of several one-off factors. The year-on-year change in consumer prices should thus stand at +1.1% in June 2014, after +0.7% in November 2013. The rise in VAT rates on 1<sup>st</sup> January 2014, after deducting the effect of the CICE tax credit, should contribute 0.2 points to this acceleration in prices. The upturn in telecommunications prices, which have fallen exceptionally sharply since 2012, should contribute 0.1 points. In addition, year-on-year change in energy prices should increase due to a base effect and contribute 0.2 points.

(1) The unemployment rate presented here is corrected for the effect of the new Labour Force Survey Questionnaire (see *Informations Rapides n° 203*). It is estimated that this should result in a 0.3-points reduction in the unemployment rate measured by the survey. In March 2014, new series will be published over long time periods.

#### 4 - The business climate marks a standstill in France Last point: November 2013



Source: INSEE

**Purchasing power slightly up in early 2014**

*Real wages should slow down in early 2014*

The average wage per head slowed down in Q3 (+0.4%), after the sharp rise in the previous quarter (+0.7%). On average in 2013, real wages should progress clearly (+1.1%), due to the unexpected fall in inflation. Through to mid-2014, based on the hypothesis of the minimum wage being increased without any additional boost (+1.1%), these gains in real wages should be cancelled out by the rise in inflation.

*Purchasing power should progress slightly*

In 2013, despite the slowdown in earned income (+1.5% after +1.9% in 2012), household purchasing power showed an upturn (+0.5% after -0.9% in 2012), mainly thanks to lower inflation (+0.6% after +1.9% in 2012). In addition, the social and fiscal burden was less dynamic (+4.5% after +7.4% in 2012), notably because the slowdown recorded in incomes in 2012 worked through into the income tax paid in 2013. Through to mid-2014, the profile in purchasing power is likely to be uneven, mainly due to the tax-collection calendar. It should therefore fall in H2 2013, then rise again in H1 2014. At the beginning of 2014, earned income should progress at a stable rate, while taxes, after the rises at the end of 2013 caused by income tax settlement payments, should fall back again at the very start of the year. In mid-2014, purchasing power should be 0.5% higher than one year previously.

**Household consumption set to slow down in H1 2014**

*Consumption should be dynamic at the end of 2013...*

In Q4 2013, consumption of manufactured goods should remain temporarily dynamic, buoyed by several one-off factors (release of profit-sharing schemes, bringing automobile purchases forward before the terms of the ecological "malus" scheme are tightened on 1<sup>st</sup> January 2014). Consumption of services should also accelerate slightly, with the result that total consumption should increase by 0.3%.

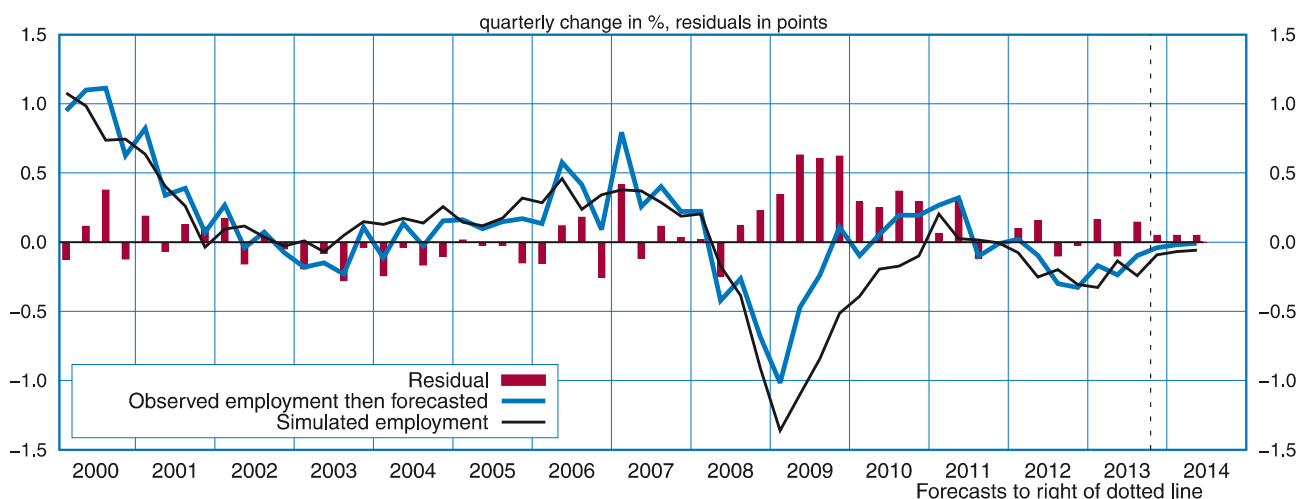
*... but should slow down in H1 2014*

In H1 2014, household consumption should be more closely in line with the trend in purchasing power and should slow down again (+0.1% per quarter).

*A new fall in construction*

Household consumption should level out in Q4 2013, after falling for seven quarters. In H1 2014, it should then fall again more sharply (-0.3% and -0.6%), due to the new drop in housing starts in mid-2013. Over 2013 as a whole, household investment should fall significantly (-3.7%) and its growth overhang should stand at -1.4% in mid-2014.

**5 - The fall in market-sector employment set to ease**



Source: INSEE

## Corporate investment should grow slightly in early 2014

### Backlash in corporate investment in services

Over the three quarters of the forecast, investment by business excluding construction should now progress at a moderate rate. Activity should improve only slowly and the margin rate of companies remain close to its low point. The CICE tax credit for businesses should represent the equivalent of 1.1 points of margin rate.

Due to the expected rebound in expenditure on services after the unusual fall in Q3 (-2.8%), corporate investment should be more dynamic in Q4 2013. Meanwhile, construction expenditure by companies should fall again through to mid-2014.

All in all, corporate investment should show a growth overhang of +0.7% at the end of June 2014.

## Main uncertainties: dynamism of French exports, investment behaviour of French companies and oil prices

### Dynamism of French exports...

In our scenario, French exports are expected to progress moderately in early 2014, at +0.7% per quarter. They could be more dynamic, notably if the return of confidence is confirmed in the Eurozone, heating up household consumption more than in our forecast.

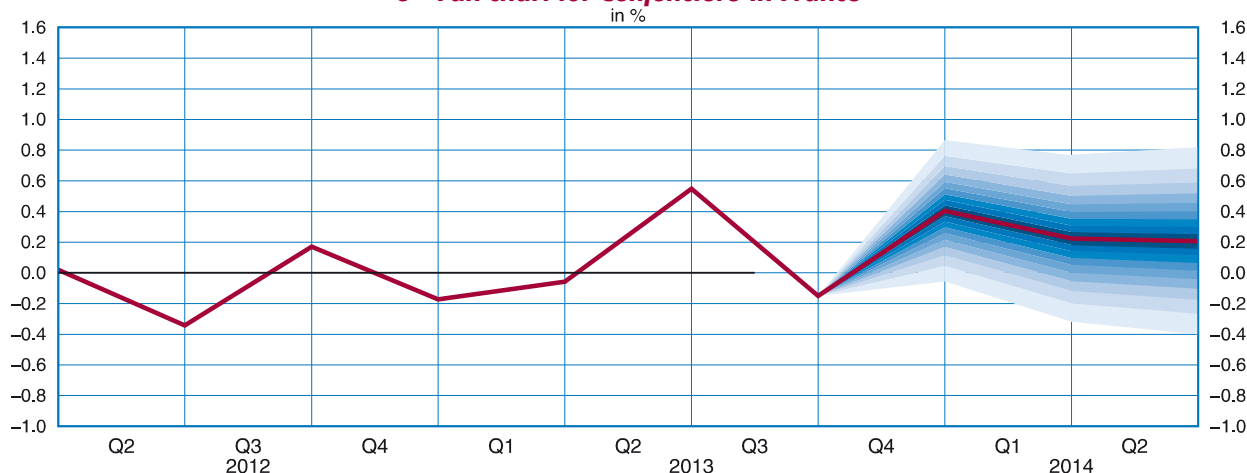
### ... investment behaviour of French companies...

In our scenario, corporate investment should grow moderately in France. The fact that it has held up in relative terms in recent years suggests that we should not expect a particularly pronounced catch-up phenomenon. The upturn in corporate investment could be even more laboured given the modest expectations of growth.

### ... and oil prices

Our scenario is based on the hypothesis of oil prices being stable through to mid-2014 at around \$110. Any further fall in OPEC production, when its additional capacities have recently been reduced by political instability in Iraq and Libya, could increase tension on the market again. Conversely, several emerging economies that are big petroleum product consumers are showing signs of fragility which, if these should be confirmed by a fall in activity, might limit their demand for oil. ■

6 - Fan chart for Conjoncture in France



How to read it: the fan chart plots 90% of the likely scenarios around the baseline forecast (red line). The first and darkest band covers the likeliest scenarios around the baseline, which have a combined probability of 10%. The second band, which is a shade lighter, comprises two sub-bands just above and just below the central band. It contains the next most likely scenarios, raising the total probability of the first two bands to 20%. We can repeat the process, moving from the centre outwards and from the darkest band to the lightest, up to a 90% probability (see *INSEE Conjoncture in France* for June 2008, pages 15 to 18). It can therefore be estimated that the first result published by the quarterly accounts for Q4 2013 has a 50% chance of being between 0.2% (lower limit of the fifth band from the bottom) and 0.6% (upper limit of the fifth band from the top). Likewise, it has a 90% chance of being between -0.1% and +0.9%. In Q1 2014, the 90% confidence intervals is [-0.3% ; +0.8%].

Source: INSEE

## Key figures: France and its international environment

seasonally adjusted / working-day adjusted data (except for prices), quarterly or annual averages, as a %

	2012				2013				2014		2012	2013	2014 ovhg
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2			
<b>International environment</b>													
Advanced economy GDP	0.6	0.0	0.2	0.0	0.3	0.6	0.5	0.4	0.5	0.3	1.4	1.2	1.5
Eurozone GDP	-0.1	-0.3	-0.1	-0.5	-0.2	0.3	0.1	0.3	0.3	0.3	-0.6	-0.4	0.9
Barrel of Brent oil (in dollars)	118	110	109	110	113	103	110	109	110	110	112	109	110
Euro-dollar exchange rate	1.31	1.28	1.25	1.30	1.32	1.31	1.32	1.36	1.35	1.35	1.29	1.33	1.35
World demand for French products	0.4	0.3	0.6	-0.6	-0.5	1.6	1.1	1.3	1.3	1.4	0.9	1.5	4.3
<b>France - supply and use</b>													
<b>GDP</b>	<b>0.0</b>	<b>-0.3</b>	<b>0.2</b>	<b>-0.2</b>	<b>-0.1</b>	<b>0.5</b>	<b>-0.1</b>	<b>0.4</b>	<b>0.2</b>	<b>0.2</b>	<b>0.0</b>	<b>0.2</b>	<b>0.7</b>
Imports	0.8	0.2	-0.1	-1.1	0.1	1.6	1.0	1.1	0.7	0.7	-0.9	1.2	2.9
Household consumption	0.2	-0.5	0.1	0.1	-0.1	0.4	0.2	0.3	0.1	0.1	-0.4	0.4	0.6
Public and NPISH consumption	0.5	0.3	0.3	0.3	0.3	0.8	0.1	0.3	0.3	0.3	1.4	1.5	1.0
Total GFCF	-1.3	-0.4	-0.7	-0.6	-0.8	-0.4	-0.6	0.4	0.0	-0.1	-1.2	-2.2	-0.1
of which: NFEs	-1.7	-0.6	-0.9	-0.5	-0.8	0.1	-0.6	0.7	0.2	0.2	-1.9	-1.8	0.7
Households	-0.7	-0.1	-0.4	-1.0	-1.3	-1.7	-0.6	0.0	-0.3	-0.6	-0.4	-3.7	-1.4
Exports	0.4	0.3	0.2	-0.6	-0.4	1.9	-1.5	2.3	0.7	0.7	2.5	0.6	2.7
Contributions (in point)													
Domestic demand excluding change in inventories *	0.0	-0.3	0.0	0.0	-0.1	0.4	0.0	0.3	0.2	0.2	-0.1	0.2	0.6
Change in inventories *	0.1	-0.1	0.1	-0.4	0.2	0.1	0.5	-0.2	0.0	0.0	-0.8	0.2	0.2
Net foreign trade	-0.1	0.0	0.1	0.2	-0.1	0.0	-0.7	0.3	0.0	0.0	1.0	-0.2	-0.1
<b>France - situation of households</b>													
Total employment	45	-21	-60	-22	-26	-16	5	52	26	10	-58	15	-
Non-agricultural market sector employment	3	-15	-48	-52	-27	-38	-16	-7	-3	-1	-112	-87	-
Unemployment rate Metropolitan France **	9.5	9.8	9.9	10.1	10.4	10.4	10.5	10.5	10.5	10.6	10.1	10.5	-
Unemployment rate France **	9.9	10.2	10.3	10.5	10.8	10.8	10.9	10.9	10.9	11.0	10.5	10.9	-
Consumer price index ***	2.3	2.0	2.0	1.5	1.1	0.8	0.9	0.7	0.9	1.1	2.0	0.9	-
Core inflation ***	1.6	1.4	1.4	0.8	0.7	0.4	0.6	0.8	0.6	0.8	1.3	0.6	-
Household purchasing power	-0.4	0.2	-0.3	-0.9	0.9	0.5	-0.1	-0.1	0.6	0.1	-0.9	0.5	0.6

Forecast

(\*) Inventory changes include acquisitions net of sales of valuable

(\*\*) For annual data, unemployment rate is that of the last quarter of the year

(\*\*\*) Year-on-year on the last month of the quarter and annual averages

How to read it: the volumes are calculated at the previous year's chain-linked prices, seasonally and working-day adjusted, quarterly and annual averages, as a %.

Source: INSEE