

French **developments**



Review of the previous forecast

In Q3 2014, activity increased more significantly (+0.3%) than predicted (+0.1%) in the *Conjoncture in France* October issue. Consumption and investment have been a little more dynamic than expected, contributing +0.2 points to growth in Q3 (+0.1 points more than forecast). Foreign trade had a negative impact on growth (-0.2 points), whereas its contribution had been expected to be nil. On the other hand, inventory change rose by 0.3 GDP points (zero contribution forecast).

Initial employment estimates are lower than the forecasts given in the October issue: -55,000 jobs in Q3 compared to the -29,000 forecast. Headline inflation fell slightly in September (+0.2%), as expected.

The growth forecast for Q4 remains unchanged (+0.1%), although the composition of this growth has changed somewhat. As predicted in the October issue, but for slightly different reasons, domestic demand (excluding inventory) should boost growth by +0.1 points. The contribution of foreign trade should be a little more dynamic (a contribution of +0.2 points); on the other hand, inventory change should have a negative impact on growth (-0.2 points).

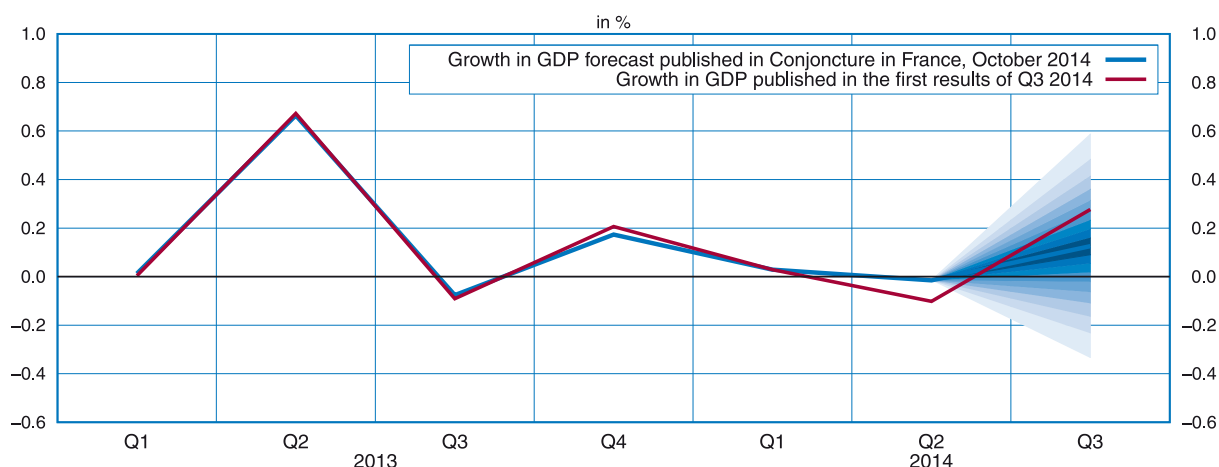
The increase in activity was slightly bigger than expected in Q3 2014

2014 Q3 saw a marked increase in activity (+0.3% after -0.1%), whereas a smaller increase had been predicted (+0.1% after 0.0%). Total production thus exceeded the forecasts, with a more dynamic performance than had been expected, both overall and within most individual activities. The rebound in manufacturing output was slightly bigger than expected (+0.5% against +0.2% in the October issue). Similarly, output from trade (+0.8% against +0.2%) and from market services excluding trade (+0.5%, compared to +0.2%) was slightly more dynamic than anticipated. Production in the energy-waste-water activity was more dynamic than expected (+2.2% and +1.0% against the forecast +1.0% and +2.1%), in line with the revisions made to the quarterly forecasts for spending on heating. On the other hand, production in the construction sector shrank by more than expected (-1.0% against -0.7% in the October issue).

Final domestic demand makes a larger-than-anticipated contribution to growth

Final domestic demand (excluding inventory) was more dynamic (contributing +0.2 points to growth) than anticipated (+0.1 points).

1- Fan chart for *Conjoncture in France* for October 2014 and growth achieved



Source: INSEE

French developments

The increase in household consumption was accurately forecast (+0.2%). However, general government consumption expenditure was more dynamic than expected, particularly individual consumption expenditures on medicines as a result of the release of a new treatment for Hepatitis C.

Investment by non-financial enterprises (NFEs) dropped off by slightly less (-0.1%) than anticipated (-0.3%). Investment in manufactured goods was more dynamic than expected. As predicted, investment in construction fell by less than it did in Q2 for NFEs (-1.0% against -0.9% in the October issue). However, the decline in household investment did not slow down as predicted (-1.7% against -0.8% forecast).

Foreign trade confounded expectations with a one-off negative contribution in Q3, offset by a positive contribution from inventory.

Exports grew by less than had been expected in Q3 (+0.5% against +0.7% forecast). In particular, sales of manufactured goods stabilised whereas they had been expected to show a clear increase (+0.9% in the October issue). This poor performance can be largely attributed to the disappointing export figures in aeronautical activity, with sales declining significantly in spite of order books which remain well-filled. Apart from aeronautics, exports were more dynamic than expected. On the other hand, total imports were more dynamic than anticipated (+1.1% against +0.7% forecast). Aeronautical activity also contributed to the acceleration in purchases of manufactured goods (+1.5% against +0.8% forecast).

All in all, for Q3, the contribution of foreign trade to GDP growth had been expected to be neutral, particularly the balance of trade in the aeronautical sector: aeronautics aside, the contribution was actually more dynamic than expected (+0.1 points), but when aeronautics are taken into account the total figure is closer to -0.2. The flipside to these fluctuations in the balance of trade is to be found in the level of inventory change, which has contributed more than anticipated (+0.3 points against a forecast of zero contribution in the October issue).

Employment declined as expected

The employment estimates are lower than the forecasts made in the October issue: -55,000 jobs in the mainly-market sectors compared to -29,000 forecast in October. The employment forecasts by activity were relatively accurate for industry (-11,000) and construction (-15,000). Services employment was disappointing (-29,000 compared with -10,000 forecast), with the reaction

to the increase in temporary employment in Q2 proving to be slightly more significant than expected (-22,000 compared with -11,000 predicted in the October issue). The rate of unemployment grew slightly more than expected in Q3 (9.9% against 9.8% forecast for Metropolitan France), the active population proving to be a little less dynamic than it had been in previous quarters.

In September headline inflation fell slightly, as predicted (+0.2%); also as expected, core inflation reached its lowest level since the beginning of the series (0.0%).

The GDP growth forecast for Q4 remains unchanged

The GDP growth forecast for Q4 remains unchanged (+0.1%), as does the forecast for 2014 as a whole (+0.4%). The business tendency surveys and activity figures currently available lead us to forecast a slight increase in manufacturing activity in Q4 (+0.2, as expected in the October issue). Household consumption expenditure should increase by just 0.1% (compared to +0.2% in the October issue). This revision comes as a result of a predicted drop in energy consumption due to the very mild weather conditions in October and November.

Corporate investment should stabilise in Q4 after falling for three consecutive quarters, whereas a slight decrease had been forecast in the October issue (-0.2%). Household investment should fall (-1.3%) by less than it did in Q3 (-1.7%), but still in excess of the previous forecasts (-0.6%): the average time lag between planning permission applications (down in 2013) and household investment was underestimated in the October issue.

The contribution of foreign trade should be positive (+0.2 points compared to 0.0 points previously), indicating a return to normal levels of activity in the aeronautical sector and reflecting the favourable impact of a fall in the exchange rate. On the other hand, the contribution of inventory should be -0.2 points (0.0 points predicted in the most recent forecast).

Mainly-market sector employment should fall by less than had been anticipated in Q4: -15,000 jobs compared to a forecast of -23,000 in the October issue. The unemployment rate should increase slightly, as forecast in October (+0.1 points).

The inflation outlook in December is slightly lower than anticipated (+0.1% against +0.4% forecast in October), and the same applies to core inflation (-0.1% against 0.0%). ■

Output

In Q3 2014, production of goods and services picked up (+0.5%) following a lacklustre H1 (+0.2% then -0.1%). GDP growth has followed a similar trajectory: +0.3% in Q3, after remaining virtually unchanged in the first (0.0%) and second (-0.1%) quarters. This acceleration in production, spread across all branches, is particularly evident in manufacturing (+0.5% after -0.8%).

In November the business climate improved across all sectors of activity, following a widespread deterioration in Q3. Returning to a level last seen in June, the composite indicator is still below its long-term average.

Production of goods and services should thus grow at a moderate rate in Q4 2014 (+0.2%), hampered by the «energy» branch in particular, then pick up pace in H1 2015 (+0.4% then +0.3%). Production of goods and services should grow by 0.6% as an annual average for 2014, with the growth overhang for 2015 standing at +0.9% at the end of H1.

Production of goods and services should see a modest increase

In Q3 2014 production of goods and services picked up (+0.5%) after a poor H1 (+0.2% then -0.1%). The business climate in France, measured by tendency surveys sent to business leaders, improved in November to make up for the gradual deterioration observed between June and October; this improvement was spread across all

sectors of activity (Graph 1). The composite indicators nevertheless remain below their long-term average levels.

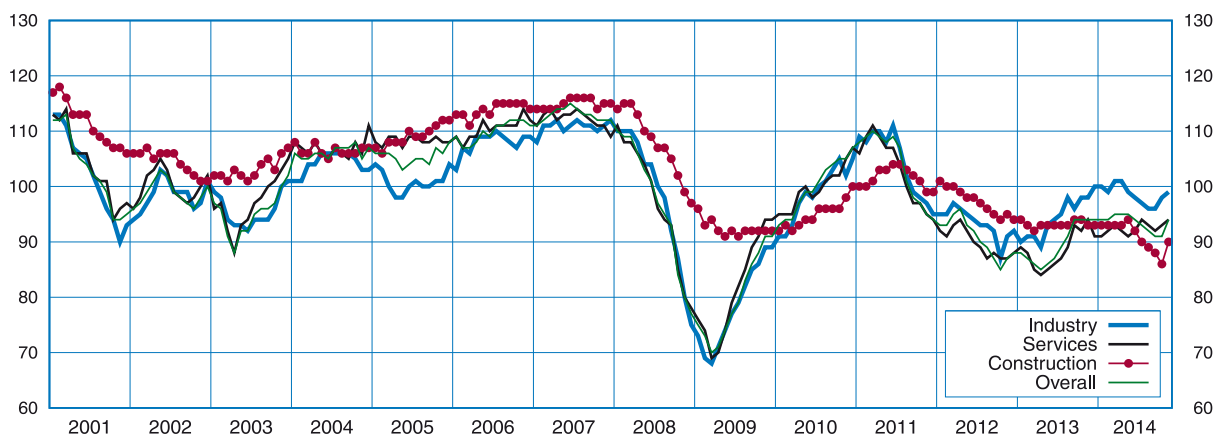
However, these surveys do not suggest that output will accelerate in the short term: production of goods and services should continue to grow at the modest rate of +0.2% in Q4, then +0.4% in Q1 2015 (Graph 2). The overall picture should be affected by the specific circumstances of the «water, energy and waste» branch, dependent on temperatures and the demand for heating. In Q2 2015, total production should increase by 0.3%. For 2014 as a whole, production of goods and services should accelerate slightly (+0.6%, up from +0.5%); for 2015, the annual growth overhang at the end of H1 should be +0.9%.

After a rebound in the summer, manufacturing output should slow

After a difficult Q2 (-0.8%), manufacturing output bounced back in Q3 2014 (+0.5%). This acceleration in activity, spread across all branches, was particularly pronounced in the coking and refining (+3.0% after -5.8%) and transport equipment (+1.7% after -0.3%) branches.

In Q4 the balance of opinion on completed production improved, accompanied by a more pronounced improvement in the outlook on future output, although both indicators remain weak (Graph 3). Manufacturing output should thus see a slight increase in Q4 2014 (+0.2%), picking up pace slightly in H1 2015 (+0.4% per quarter).

1 - Composite indicators in France: all sectors industry, services and building



Source: INSEE

French developments

Manufacturing output should grow by 0.3% for 2014 as a whole. The growth overhang for 2015 should reach +1.0% by the end of Q2.

The decline in activity in the construction sector should slow down

In Q3 2014, production in the construction sector continued to deteriorate (-1.0%, after -1.4% in Q2 2014). This decline was felt in both building and civil engineering.

In Q4 2014, production in the construction sector should continue to fall (-1.0%) based on the current state of the order books, again found to be far below usual levels in the building branch, as well as the pronounced deterioration seen in the activity forecasts derived from the sector-specific business tendency surveys (*Graph 4*). In H1 2015, this decline should continue to a lesser extent (-0.7% and -0.5% in the first two quarters), as indicated by the stabilisation in the number of applications for planning permission in 2014. Nonetheless, civil engineering activity should remain sluggish as a result of weak demand from businesses and local authorities.

For 2014 as a whole, production in the construction sector should fall by 3.1%. By mid-2015, the growth overhang for the year should be -2.6%.

After picking up pace in the summer, trade activity should slow down

Activity in the trade sector picked up pace in Q3 2014 (+0.8% after +0.2% in Q2), bolstered in particular by the performance of merchanting, which by definition is subject to volatility.¹ Assuming that growth in this sector returns to its average level, trade should slow in Q4 2014 (+0.4%), reacting to the moderate growth in the demand for manufactured goods (+0.2% in Q4 for consumption, +1.7% predicted for exports).

After a marked deterioration in the summer, the business climate indicators for the retail and wholesale sectors picked up again in the autumn but remain below their long-term average levels; the balance of opinion regarding prices remains particularly low. The balance of opinion concerning past activity remains poor in both the wholesale and retail sectors; the balance of opinion regarding business prospects for the coming months is up in both sectors, although still below average.

In H1 2015, trade should progress at a similar rate to that seen in late 2014 (+0.4% per quarter). Overall, the growth overhang for production in the trade sector should stand at +1.4% by the end of H1 2015, after growing by +1.4% over 2014 as a whole.

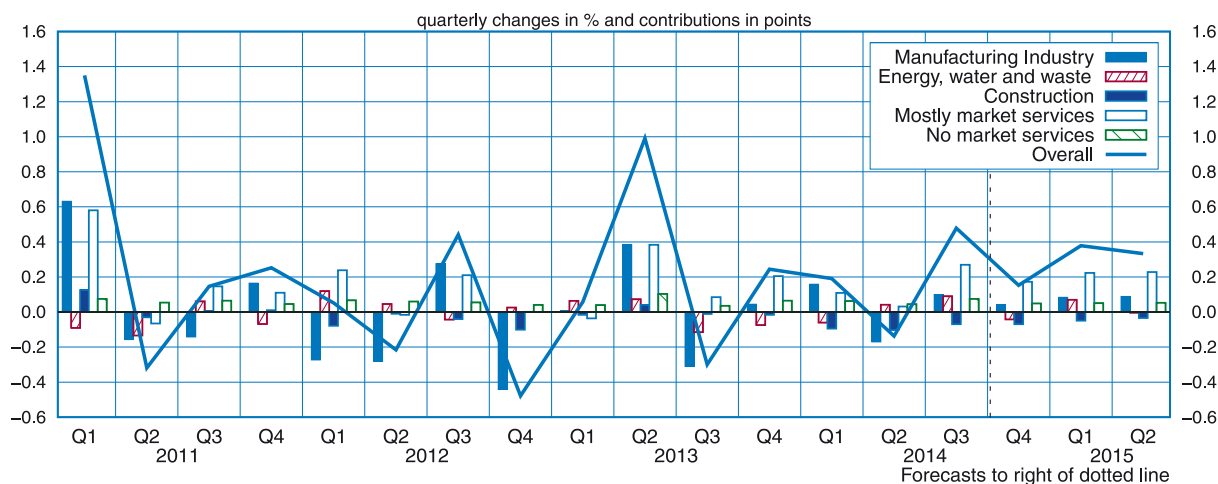
Market services excluding trade: activity should increase slightly

Production of market services excluding trade grew in Q3 2014 (+0.5%) after stagnating in Q2. Activity bounced back in accommodation and catering services (+0.4% after -0.1%) and information and communication (+0.8% after -0.1%). Activity remained dynamic in the financial services (+0.9% after +0.3%) and business services (+0.6% after +0.2%) sectors. Activity in the property sector continued to grow at a rate close to that of the preceding quarter (+0.3% after +0.2%).

In Q4 2014, market services excluding trade should continue to grow at a moderate rate (+0.3%). According to the business leaders surveyed in November, the short-term outlook has been stable for several months: the composite

(1) Merchanting refers to the commercial activity which consists of buying goods overseas and selling them on for a profit, without these goods ever entering the country.

2 - Sector contributions to growth in total production



indicator stood at 94 in November, having fluctuated around this level since September 2013, remaining below the long-term average (100). Activity should thus continue to grow at a moderate rate in 2015 (+0.4% then +0.5% for the first two quarters).

For 2014 as a whole, production of market services excluding trade should increase by 1.1%, an increase comparable to that seen in 2013 (+1.0%). By mid-2015, the growth overhang for the year should be +1.3%.

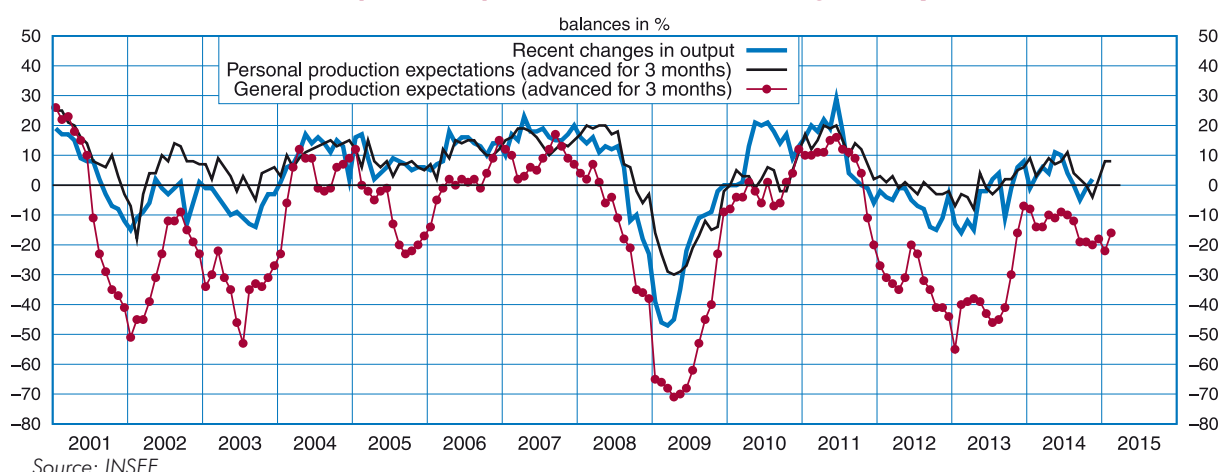
Mainly non-market services: the increase in activity should remain modest

Production of mainly non-market services increased in Q3 2014 (+0.5% after +0.3% in Q2). Production should continue to grow at a similar rate in Q4 2014 and throughout H1 2015 (+0.3% per quarter). For 2014 as a whole, production in these branches should grow by 1.6%, up from +1.5% in 2013. By mid-2015, the growth overhang for the year should be +1.2%.

After dropping off towards the end of the year, energy production should bounce back in 2015

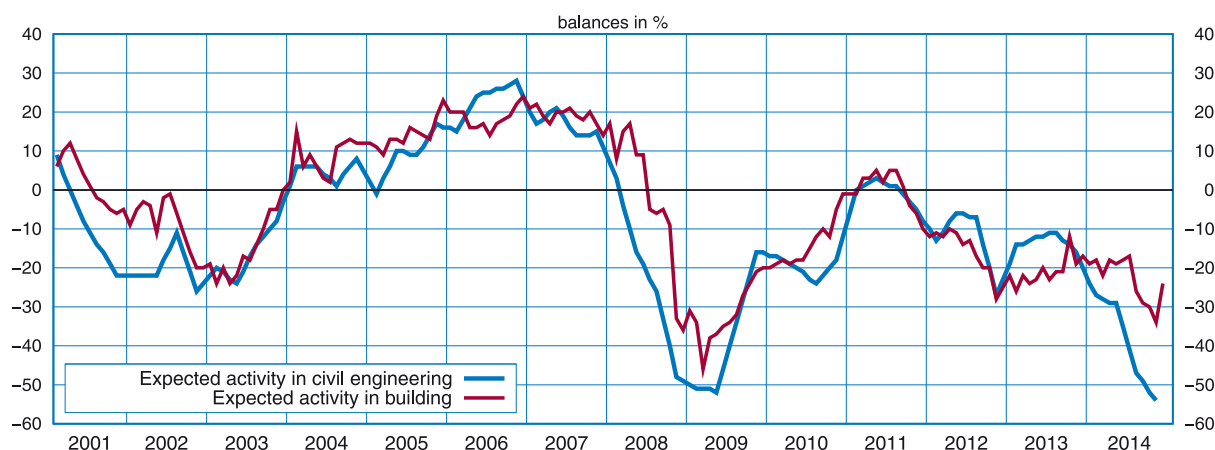
Activity in the «energy, water and waste» branch depends heavily on the demand for heating, which in turn is subject to climate factors. After falling in early 2014 (-1.4%) then bouncing back in the spring (+1.0%), production in the energy, water and waste branch accelerated over the summer (+2.2%) as spending on heating returned to normal levels. With mild temperatures in October and November, production should drop off again for the autumn (-1.0%). Assuming that heating expenditure returns to normal, energy production should bounce back in Q1 2015 (+1.7%) before stabilising in Q2 (-0.1%). The growth overhang for 2015 should thus be +2.2% by mid-year, with an overall 2.1% decline in production for 2014 as a whole. ■

3 - Opinion on production in manufacturing industry



Source: INSEE

4 - Prospects for activity in construction



Source: INSEE

French developments

Industry production at prices of the previous year chained

seasonally and working-day adjusted data, in %

	quarterly changes										annual variations		
	2013				2014				2015		2013	2014	2015 oghv
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2			
Agriculture (2%)	-0.0	0.2	0.8	0.8	0.7	0.8	0.5	0.0	0.0	0.0	0.1	2.5	0.4
Manufacturing industry (20%)	0.0	1.9	-1.5	0.2	0.8	-0.8	0.5	0.2	0.4	0.4	-0.6	0.3	1.0
Energy, Water and Waste (4%)	1.5	1.7	-2.7	-1.8	-1.4	1.0	2.2	-1.0	1.7	-0.1	1.2	-2.1	2.2
Construction (8%)	-0.2	0.6	-0.2	-0.2	-1.3	-1.4	-1.0	-1.0	-0.7	-0.5	-1.2	-3.1	-2.6
Trade (10%)	0.0	0.8	0.0	0.7	-0.0	0.2	0.8	0.4	0.4	0.4	0.6	1.4	1.4
Tradable services excluding trade (41%)	-0.1	0.7	0.2	0.3	0.3	0.0	0.5	0.3	0.4	0.5	1.0	1.1	1.3
Non Tradable services (15%)	0.3	0.7	0.2	0.4	0.4	0.3	0.5	0.3	0.3	0.3	1.5	1.6	1.2
Total (100%)	0.1	1.0	-0.3	0.2	0.2	-0.1	0.5	0.2	0.4	0.3	0.5	0.6	0.9

Forecast

Weights constructed from the annual production value in 2010.

Source: INSEE

France's International Environment

In Q3 2014 activity picked up slightly in the advanced economies (+0.5% after +0.4%), although slightly less than forecast in the October issue of *Conjoncture in France* (+0.6%). The American (+1.0%) and British (+0.7%) economies grew strongly again, while growth remained modest in the Eurozone (+0.2%), and Japanese GDP slipped back once more (-0.5% after -1.7%). In the emerging economies activity was sluggish again, although the business climate recovered somewhat. Activity slowed most notably in China, and the economic outlook deteriorated in several major emerging countries, the fundamental drivers of which are a cause for concern.

In the advanced economies, there is still a clear division between the Anglo-Saxon countries where the business climate has been high since the start of the year, signalling buoyant activity, and the Eurozone where the short-term climate remains gloomy. This decoupling should continue through to mid-2015. In Japan the VAT rise in April 2014 weighed very heavily on domestic demand, causing a sharp deterioration in activity which is only likely to recover slowly. All in all, activity in the advanced countries should continue to show a growth rate similar to that of Q3: +0.4% in Q4 2014, then +0.5% in Q1 2015 and +0.4% in Q2. Growth is likely to remain moderate in the emerging economies. As well as the Chinese

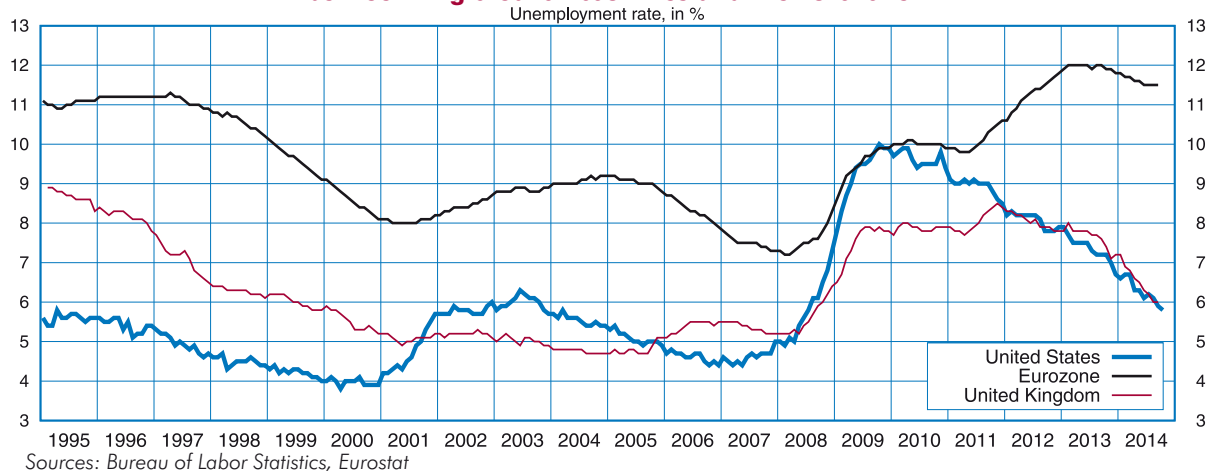
slowdown, which is marked in investment and in industrial output, the situation is likely to remain sluggish in several major emerging countries (Brazil, Indonesia, Turkey, Russia), where past monetary tightening, the sharp depreciation of currencies and the risk of new foreign capital withdrawals are likely to take their toll on activity.

Central banks adjusting their monetary policies

In the Anglo-Saxon countries, unemployment continued to fall back in Q3 and at the start of Q4 2014 (*Graph 1*). In the United States the unemployment rate stood at 5.8% in October, and in the United Kingdom it was 6.0% in September. This sharp decrease generated by the robust recovery allows an about-turn in monetary policy in these two countries. In the United States the Federal Reserve stopped its monthly bond purchases in October, bringing an end to its third quantitative easing programme. In the United Kingdom the Bank of England has maintained its accommodating monetary policy but an increase in rates seems imminent.

Conversely, in the Eurozone the European Central Bank (ECB) is confronted with a high level of unemployment (11.5% in October) and weak inflation (+0.3% in November, *Graph 2*), with the risk of deflation over the medium term. Faced with this low level of inflation and a lack of vitality in the Eurozone economy, the ECB has started to

1 - More pronounced labour-market divergences between Anglo-Saxon countries and the Eurozone



French developments

implement the bond purchasing programmes announced in summer, the first stages of which have only been a moderate success. In November it also reported the generally satisfactory results of the assessment of the quality of Eurozone banks' balance sheets that it had been conducting since the end of 2013, prior to the European banking single supervisory mechanism.

The current weakness of inflation is partly due to that of core inflation, but also to the sharp drop in energy prices since summer 2014, in the wake of the slump in oil prices. This slump has occurred at a time when a number of oil-producing countries have restored their production capacities against a backdrop of less dynamic demand. In early December the price of Brent is around \$70 per barrel (€59.60), its lowest level since September 2010.

The decoupling between the Anglo-Saxon countries and the Eurozone still in evidence

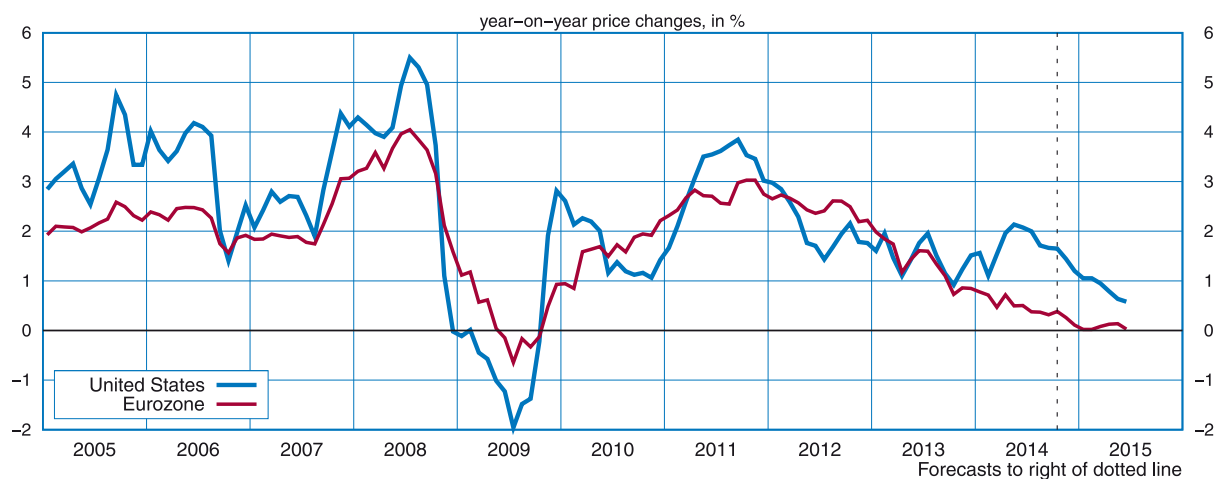
In the Anglo-Saxon countries the main obstacles in the way of demand seem to have been removed. In the United States, consumption, driven by the expected buoyancy of wages as unemployment recedes, should be dynamic, as should corporate investment, sustained by robust activity and the recovery of the production capacity utilisation rate. In the United Kingdom activity should also remain dynamic, although it is likely to slow somewhat: the unemployment rate is set to fall slightly less sharply and property prices should level off, and so household consumption is likely to benefit less from the drop in precautionary savings and the wealth effects in evidence since the start of 2013. The short-term indicators suggest that investment, in particular property investment, should be less buoyant.

In the Eurozone, growth should remain modest in Q4, as corporate investment is once again handicapped by poor demand prospects, compounded by geopolitical uncertainties. The zone should pick up a little momentum in H1 2015, particularly in Germany where the introduction of a minimum wage should generate positive income effects. Furthermore, investment should recover a little vitality, particularly in construction. However, this general context is likely to hide heterogeneous situations within the zone. In Spain the stabilisation of construction should remove the last remaining obstacle to growth and activity should pick up sharply. In Italy however, activity is likely to remain sluggish.

Slowdown in the emerging countries slowing, and lacklustre world trade

Growth has been moderate in the emerging economies since 2013, when the Federal Reserve announced it was to adopt a less expansionary monetary policy. Up until the start of 2014 this resulted in withdrawals of capital and sharp currency depreciations in several countries with fragile economies, leading certain central banks to raise their base rates and hence hamper activity. In Q2 2014, tensions have eased in the financial markets, but previous monetary tightening measures are still taking their toll on activity. The business climate in industry as compared with its long-term average is still at a far lower level than that in the advanced economies (*Graph 3*). The lack of dynamism is partly attributable to China, where growth (+1.9% in Q3) is still below its pre-crisis average (+2.5% per quarter on average between 2000 and 2007): in summer, industrial production stood still and investment, particularly in property, continued to slow. Additionally, activity remained lacklustre in several major emerging

2 - The ECB faced with weak inflation



Sources: Bureau of Labor Statistics, Eurostat, INSEE forecasts

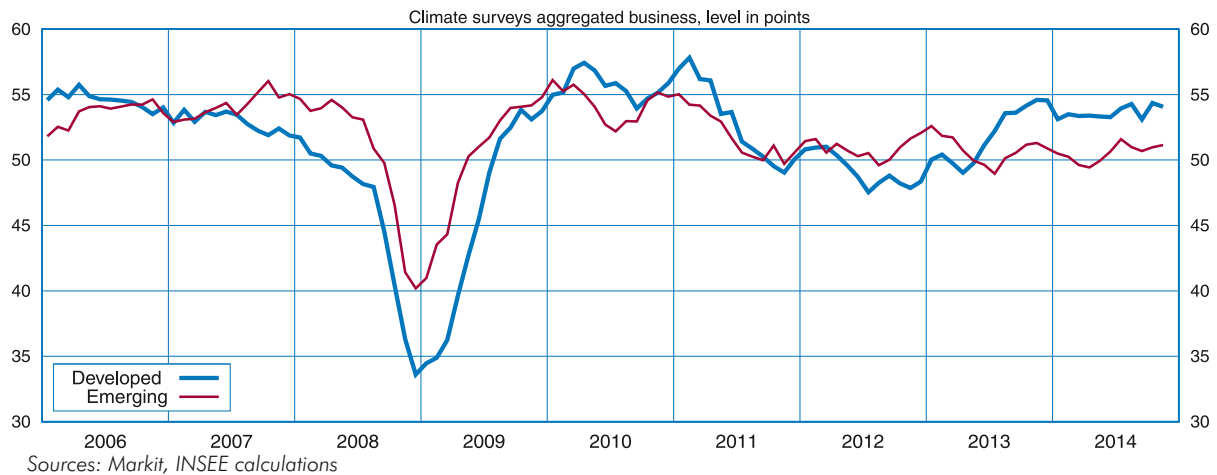
countries such as Brazil and Turkey, where domestic demand has been hit hard by monetary tightening and currency depreciations.¹

However, world trade picked up in Q3 (+2.0% after +0.7%), thanks to the rebound in imports by the emerging countries after two quarters of decline, but also to imports by the European countries. In Q4, world trade is likely to slow in reaction to this (+1.0%), and should then maintain this rhythm in H1 2015, most notably thanks to

imports by emerging countries. It should however grow at a rate below its trend (+1.6% per quarter on average between 2000 and 2007). Driven by the advanced economies, world demand for French products should also be dynamic (+1.0% per quarter). ■

(1) In general, the slowdown of the emerging countries is in part structural, linked with the gradual decrease in the processing trade.

3 - The economic climate is poor in the emerging countries



International scenario summary

	quarterly changes						annual changes		
	2014				2015		2013	2014	2015
	Q1	Q2	Q3	Q4	Q1	Q2			
GDP of advanced economies	0.3	0.4	0.5	0.4	0.5	0.4	1.4	1.8	1.5
World trade	-0.6	0.7	2.0	1.0	1.0	1.0	2.7	3.1	3.7
Imports of advanced economies	0.5	0.7	0.7	0.9	0.9	0.9	-0.3	2.7	2.8
Imports of emerging economies	-0.6	-1.0	3.5	1.1	1.1	1.1	5.8	3.7	4.3

forecast

Reading note: imports, exports and world trade data concern only goods.

Sources: National statistical institutes, Centraal PlanBureau, International Monetary Fund, INSEE forecast

The Ukraine crisis is likely to have a limited impact on Eurozone trade but may hold investment back

In reaction to Russian intervention in Ukraine, the United States and European Union imposed economic sanctions on Russia, mainly in terms of access to financing and freezing assets. The Russian government, meanwhile, decided in August to place an embargo on imports of most agricultural products from those countries that had imposed sanctions on it.

Rising tensions in this geopolitical crisis since the end of 2013 have already weighed down on economic activity in Russia: while growth stood at +0.8% per quarter on average until mid-2013, it has only been +0.3% since then, representing a cumulative difference from the trend of 3 percentage points of activity through to the end of 2014. Correlatively, the fall in

the oil price could amplify this slowdown. Consequently, Russian imports fell sharply in Q2 2014 (-7.7%) and could fall further with the effects of the mutual sanctions over the summer.

However, this sharp contraction in trade should have a relatively limited impact on the French economy, as Russia and Ukraine represent a small proportion of the destinations for French exports (2.3% and under 0.1% respectively). Russia's contribution to world demand for French products is therefore likely to stand at -0.04 percentage points per quarter in 2014, against +0.06 points on average since 2010, hence an effect on the total fall in French exports of around -0.10 percentage points per quarter.

French developments

In Germany, too, the weight of Russia (3.9%) and of Ukraine (under 0.2%) in exports is relatively limited. The contribution of the conflict can be estimated at about -0.15 percentage points per quarter on the rate of German exports. Finally, at Eurozone level, the contraction in Russian demand is weighing down on exports (-0.05 percentage points on average since Q4 2013, graph 2), but without slowing down the dynamic of growing demand for products from the Eurozone (+0.5% per quarter on average).

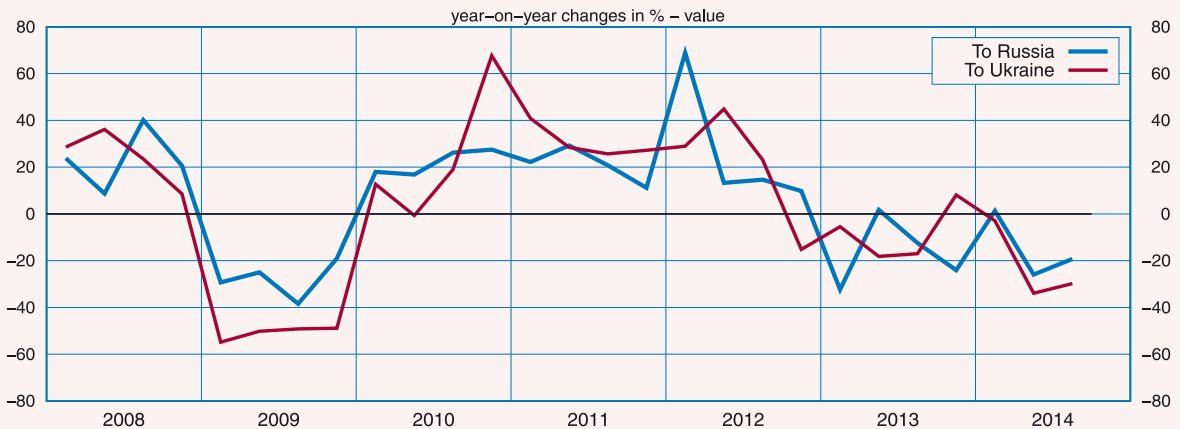
Taking account of the second-round effects of the commercial channel,¹ a fall of 3 percentage points in Russian GDP is likely to have a medium-term impact of 0.1 points on GDP in

(1) cf. model in the [...] report. This simulation considers all foreign trade between partner countries, but without taking account of exchange rate effects.

France and 0.15 points in Germany. In both cases, the direct effect is small and it is the echo effect that weighs most heavily. The latter is estimated at 0.05 percentage points of GDP for France and 0.10 points of GDP for Germany.

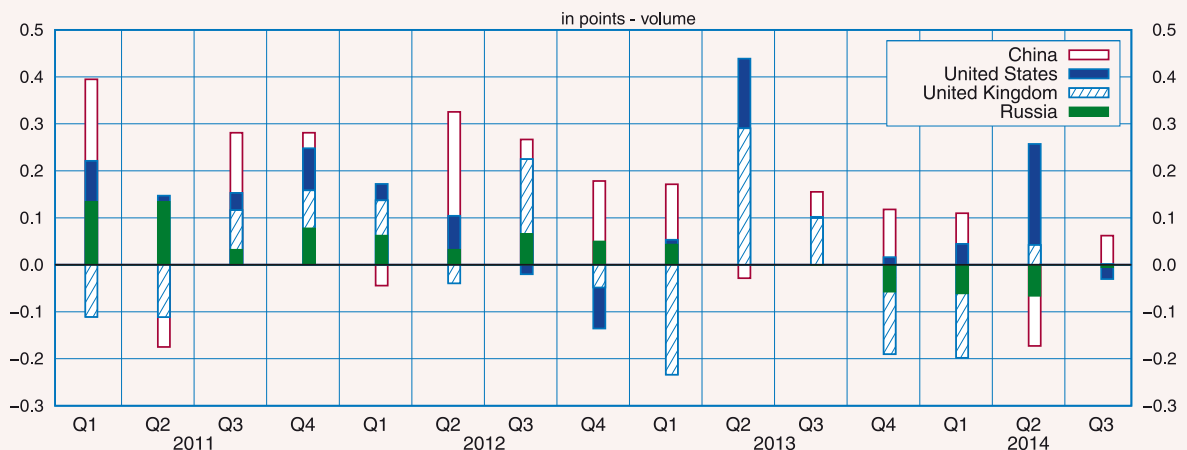
Aside from the impact on foreign trade, the Ukrainian crisis may also have had a negative impact on demand from companies (investment expenditure and inventory change), as they anticipate a deterioration in their own prospects. In Germany, the marked fall in capital expenditure (-2.3% in Q3 2014, equivalent to -0.1 points of GDP) and the very negative contribution of inventory (-0.5 points of GDP) could also partly be an indirect consequence of the Ukraine conflict, although its scale exceeds that which should result from this conflict in principle. ■

1 - Year-on-year change in French exports to Ukraine and Russia



Source: DGDDI

2 - Contributions to the non-EU exports of the Eurozone



Source: DG Tresor

Foreign trade

After a modest increase in Q3 (+0.5%), exports should pick up in Q4 (+1.4%), due mainly to a rebound in deliveries of aircraft and the recent depreciation of the Euro. They should remain dynamic in Q1 2015 (+1.1%), as the earlier depreciation of the Euro is still having an effect. However, as these favourable effects fade, exports are likely to slow a little in Q2 2015 (+1.0%). Imports are likely to slow in Q4 (+0.5% after +1.1%) due to a deceleration in purchases of aeronautical goods; after that they should increase by 0.7% in Q1 and by 0.8% in Q2 2015, following on from the upturn in domestic demand.

In all, after a negative contribution in Q3 2014 (-0.2 point), foreign trade should make a positive contribution to GDP growth in Q4 2014 (+0.2 points) then in Q1 2015 (+0.1 points) and will once again become neutral in Q2 2015.

World trade likely to be relatively dynamic through to mid-2015

In Q3 2014, world trade accelerated by +2.0% after +0.7% in Q2. Imports from the emerging countries in particular picked up after a decline in Q2.

The PMI indicators for export orders are above their long-term average level in most countries, and the first customs data available suggest an increase in world trade of around +1.0% in Q4 2014. World trade is likely to maintain this pace in H1 2015. In correlation with this, world demand for French

products is likely to increase by 1.0% per quarter over the forecasting period (see [Graph 1](#)).

Exports likely to accelerate in Q4 2014

In Q3, total exports increased moderately (+0.5% after -0.1%). Exports of manufactured goods stagnated after a 0.6% drop in Q2. In particular, sales of transport equipment contracted (-5.5% after -1.8%), especially aeronautical and naval equipment. However, the acceleration of almost all other items compensated for this decline. Sales of services accelerated (+1.0% after +0.3%), sustained by the dynamism of sales of insurance services. Energy sales remained very dynamic (+12.8% after +10.7%).

In Q4 2014, total exports should accelerate (+1.4%), sustained by relatively dynamic world demand, especially from the United States, the recent depreciation of the Euro, and the return to normal of aeronautics exports. Thus exports of manufactured goods are likely to make a particular contribution to this trend (+1.7%).

In H1 2015, exports should increase by just over 1% on average per quarter. World demand for French products (+1.0% per quarter) is likely to be sustained mainly by the advanced economies (see [Graph 2](#)). In addition, in Q1 2015, the previous drop in the real effective exchange rate (-1.7% in Q4 2014) should still occasionally favour exports of manufactured goods (see [Graph 3](#)), which are likely to increase by 1.2%, before slowing in Q2 (+1.0%). Services should progress at around their

Foreign trade growth forecast

	quarterly changes						annual changes		
	2014				2015		2013	2014	2015
	Q1	Q2	Q3	Q4	Q1	Q2			
Exports									
All goods and services	0.5	-0.1	0.5	1.4	1.1	1.0	2.4	2.2	3.1
Manufactured products (75%*)	0.6	-0.6	0.0	1.7	1.2	1.0	1.5	1.4	3.1
Imports									
All goods and services	0.7	0.3	1.1	0.5	0.7	0.8	1.9	2.9	2.3
Manufactured products (77% *)	0.6	0.3	1.5	0.3	0.6	0.7	1.3	3.6	2.2
Contribution of foreign trade to GDP	-0.1	-0.1	-0.2	0.2	0.1	0.0	0.1	-0.2	0.2

Forecast

Reading note: part of exports (resp. imports) of non-energy industrial goods in exports (resp. imports) in a whole in 2013.
Source: INSEE

French developments

usual pace (+1.3% per quarter). Exports are likely to increase by 2.2% on average in 2014, after +2.4% in 2013. The growth overhang for 2015 would then be +3.1% at the end of H1.

Imports expected to slow in Q4 2014

In Q3 2014, French imports increased significantly: +1.1% after +0.3%. Imports of manufactured goods were particularly dynamic (+1.5% after +0.3%), linked with a sharp rebound in imports of transport equipment (+5.5% after -1.4%) especially in the aeronautical and naval sectors. Energy purchases fell back once again (-0.4% after -1.2%). Imports of services decelerated slightly (+0.8% after +1.0%).

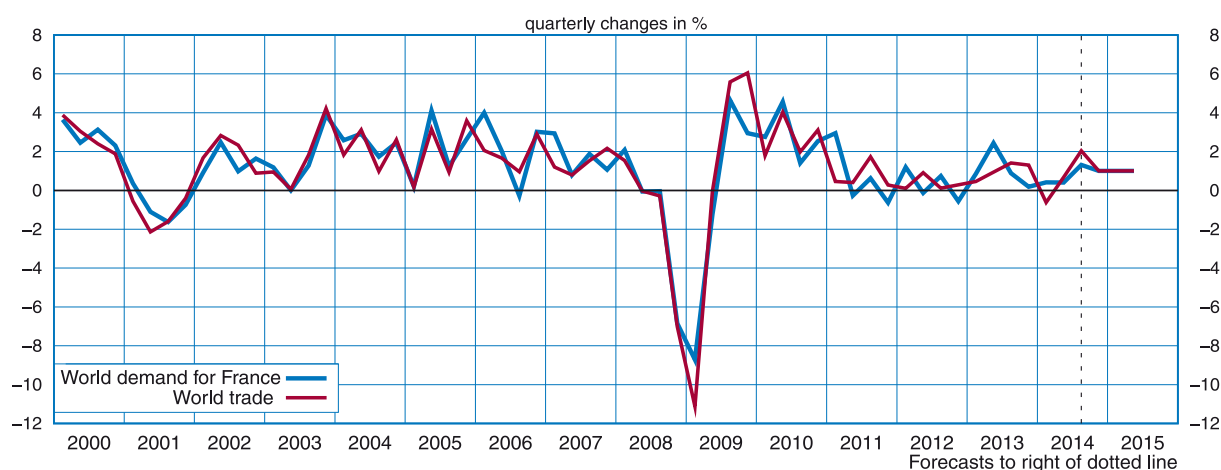
In Q4 2014, total imports are expected to slow (+0.5% after +1.1%), and the impact of the slowdown in domestic demand (+0.1% after +0.4%) should be accentuated by the return to normal of aeronautical imports.

In H1 2015, imports are likely to accelerate once again (+0.7% in Q1 and +0.8% in Q2). Purchases of manufactured goods should regain momentum (+0.6% then +0.7% after +0.3% in Q4 2014), in the wake of domestic demand. Purchases of services are set to return to their usual rate (+1.2%).

In 2014, imports are likely to increase on average by 2.9%, after +1.9% in 2013. The growth overhang for imports for 2015 at the end of H1 should be +2.3%.

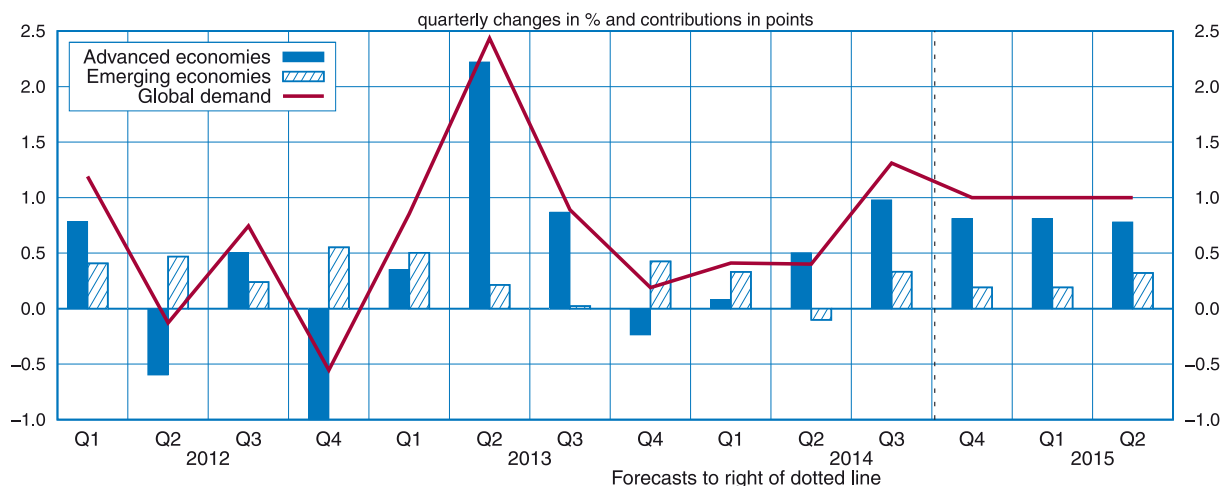
All in all, the contribution of foreign trade to GDP growth is likely to be negative in 2014 (-0.2 point). However it should be positive in H1 2015: the annual growth overhang should reach +0.2 points mid-year. ■

1 - World demand for French products and world trade



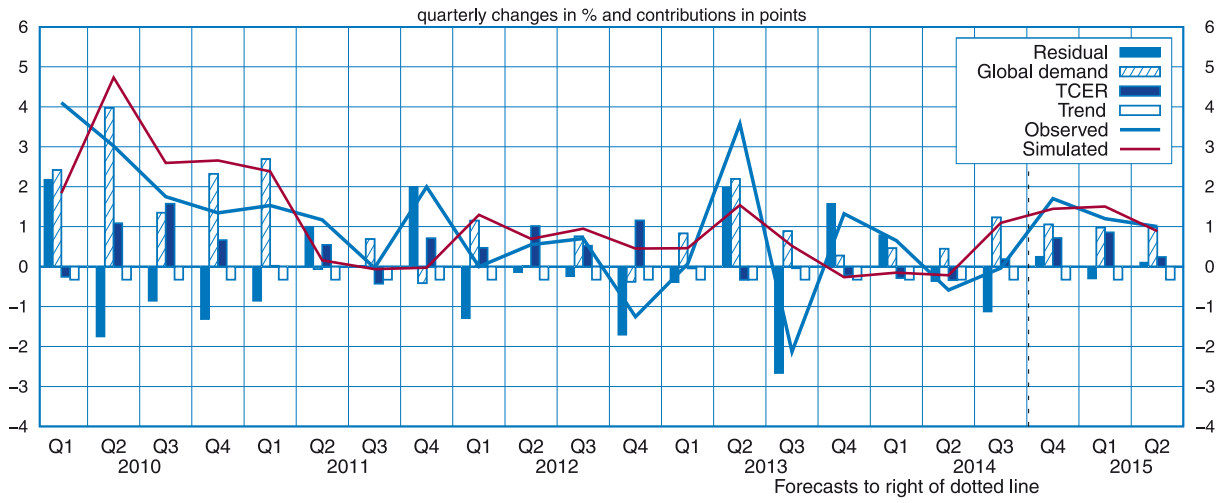
Sources: INSEE, DG Trésor, Centraal PlanBureau

2 - World demand for French products and contributions of the main partners



Sources: INSEE, DG Trésor, Centraal PlanBureau

3 - Equation of exports (goods and services) and econometric contributions



Employment

Market employment fell back in Q3 2014 (-55,000 jobs) after increasing slightly in Q2 (+7,000). During the coming quarters, a better trend in activity on the whole as well as the effects of the CICE and the Responsibility and Solidarity Pact should reduce the fall.

For 2014 overall, the fall in market employment should be slightly greater (-77,000 jobs) than in 2013 (-69,000). It should be concentrated in industry (-37,000 jobs) and construction (-43,000 jobs).

In non-market sectors, employment should continue to progress through to mid-2015, particularly due to the increased number of beneficiaries of subsidised contracts. It should increase by 58,000 in 2014 then by 19,000 in H1 2015.

All in all, employment should stagnate in 2014 (after a rise of 49,000 in 2013) and increase by 18,000 in H1 2015.

The number of employees in market sectors should decline less markedly between now and mid-2015

In 2013, market employment fell by 69,000 jobs, mainly in H1 (-74,000 employees). In 2014, job losses continued (-77,000, [Table 1](#)).

This decline is relatively in line with what the usual employment determinants would suggest ([Graph 1](#)). The slowdown in activity was partly offset by the effect of the CICE (tax credit for competitiveness and employment).

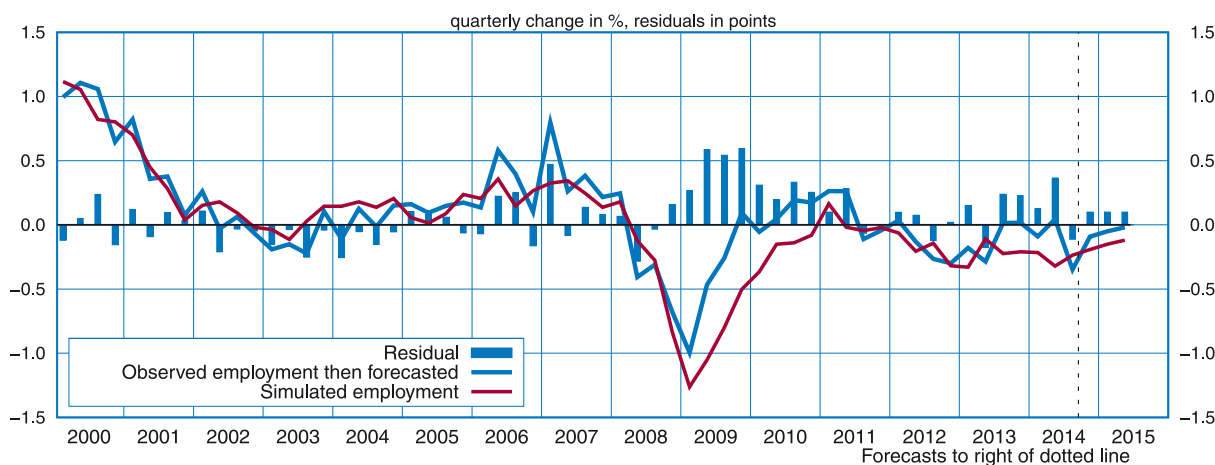
During H1 2015, the slight acceleration in activity and the cumulative effects of the CICE and the Responsibility and Solidarity Pact (see focus) should allow market job losses to be a limited a little further (-11,000 jobs).

Temporary employment should be more or less stable, and non-temporary tertiary employment should progress moderately

The fluctuations in temporary work during the last four quarters (+18,000 at the end of 2013 then -15,000; +12,000 in Q2 2014 then -22,000) have affected the profile of market employment generally. But overall, in all sectors, the rate of temporary employment remained stable year on year and should continue in this way until mid-2015. Temporary employment should therefore be more or less stable in the first part of 2015 (+8,000 jobs).

Employment in the non-temporary market tertiary sector increased in H1 2014 (+27,000 jobs). It should stagnate in H2 before rising again in H1 2015 (+14,000 jobs).

1- Employment observed in the non-agricultural market sector, simulated and residual employment



How to read it: The equation residual for employment is the spread between the observed employment growth rate and the simulated employment growth rate. A positive residual, such as that observed at the end of 2013, indicates that observed employment showed better growth than past behaviour would lead us to expect.

Source: INSEE

All in all, employment in the tertiary sector, including temporary employment, should fall in H2 2014 (22,000 jobs, mostly in the temporary sector), before accelerating in H1 2015 (+22,000 jobs).

Industrial employment should fall again

The net losses of industrial jobs were slightly reduced in H1 2014 (-17,000, after -29,000 on average per half-year in 2013). Given the decline recorded in Q3 and the prospects for industry in terms of employment, losses should increase again in H2 2014 (-20,000 jobs). In H1 2015, 12,000 jobs should be lost (Graph 2).

Employment in construction should fall back slightly more strongly

Salaried employment in construction has been in almost continual decline since 2008. The sector lost 15,000 jobs in H1 2014 and 15,000 in Q3. Given the deteriorating prospects indicated by the

(1) Since July 2014, recruitment in Integration Workshops and Projects (ACI) has no longer been carried out with CUI-CAE but on CDDIs (Fixed-Term Integration Contract). Nevertheless, in order to maintain a constant scope in the monitoring of subsidised employment, the forecasts for CUI-CAE presented here include ACI.

surveys in the building industry (Graph 3), this decline is likely to intensify: 27,000 jobs should be lost in H2 2014, then 22,000 in H1 2015.

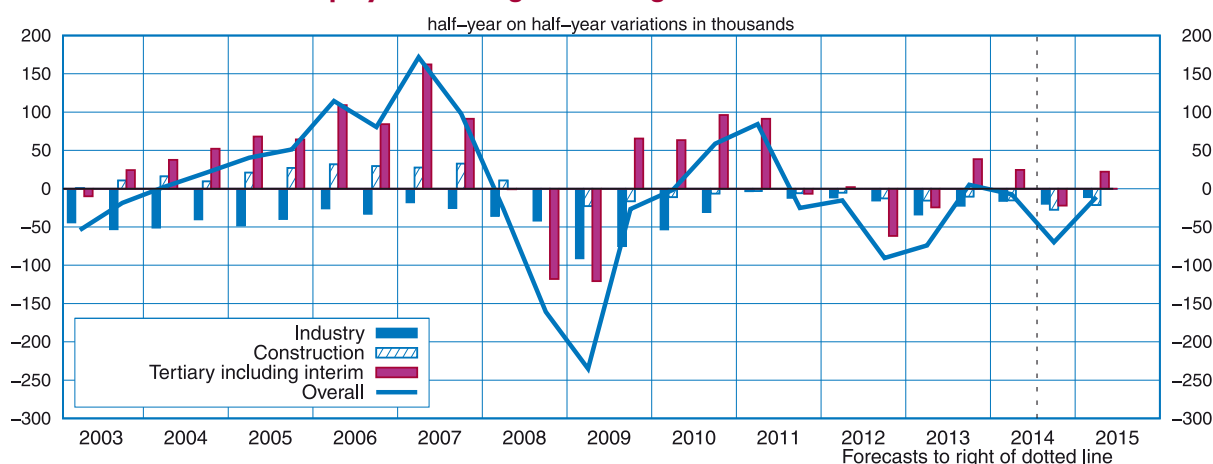
Non-market employment should progress due to subsidised contracts

Non-market employment should increase by 58,000 jobs in 2014, equally spread over the two half-years. It should slow down slightly in H1 2015 (+19,000 jobs). This slowdown should be driven by the civil service workforce excluding subsidised contracts.

In 2014, new subsidised contracts should reach almost 380,000, just over 200,000 of them in H2. These entries should then slow down in H1 2015, due to "integration" contracts (CUI-contrats uniques d'insertion – CAE-contrat d'accompagnement dans l'emploi¹). For the CUI-CAE, the numerous new contracts in late 2013 should translate into higher numbers of exits in H2 2014 and the number of beneficiaries should fall slightly. This effect should no longer be felt in early 2015. All in all, the number of beneficiaries of subsidised contracts should accelerate again, rising from +9,000 in H2 2014 to +19,000 in H1 2015 (Table 2).

Taking all sectors together, overall employment should rise very slightly in H1 2015 (+18,000 jobs) after being stable in 2014. ■

2- Employment change in non-agricultural market sectors



French developments

Table 1

Change in employment

	2014				2015		2014 S1	2014 S2	2015 S1	2013	2014	2013 *
	Q1	Q2	Q3	Q4	Q1	Q2						
Mainly non-agricultural non-market sectors (2)	-14	7	-55	-15	-8	-3	-7	-70	-11	-69	-77	15888
Industry	-6	-11	-11	-9	-6	-6	-17	-20	-12	-57	-37	3172
Construction	-5	-11	-15	-12	-12	-9	-15	-27	-22	-26	-43	1393
Temporary work	-15	12	-22	0	2	7	-3	-22	8	33	-25	543
Market services	11	16	-7	7	8	6	27	0	14	-19	27	10780
Agricultural workers	1	1	1	1	1	1	2	2	2	7	4	
Mainly non-market service sectors	14	16	16	12	14	5	30	27	19	102	58	
Self-employed	4	4	4	4	4	4	8	8	8	9	15	
TOTAL EMPLOYMENT	4	28	-35	2	11	7	33	-33	18	49	0	

Forecast

* Niveau fin (in thousands)

Note: 11,000 jobs should be destroyed in the mainly non-agricultural market sector during H1 2015. As of 31 December 2013, this sector employed 15,888,000 people.

(1) Sectors OQ (private workers)

(2) Sectors DE to MN and RU

Source: INSEE

Table 2

Change in subsidised employment in the non-market sector

in thousands

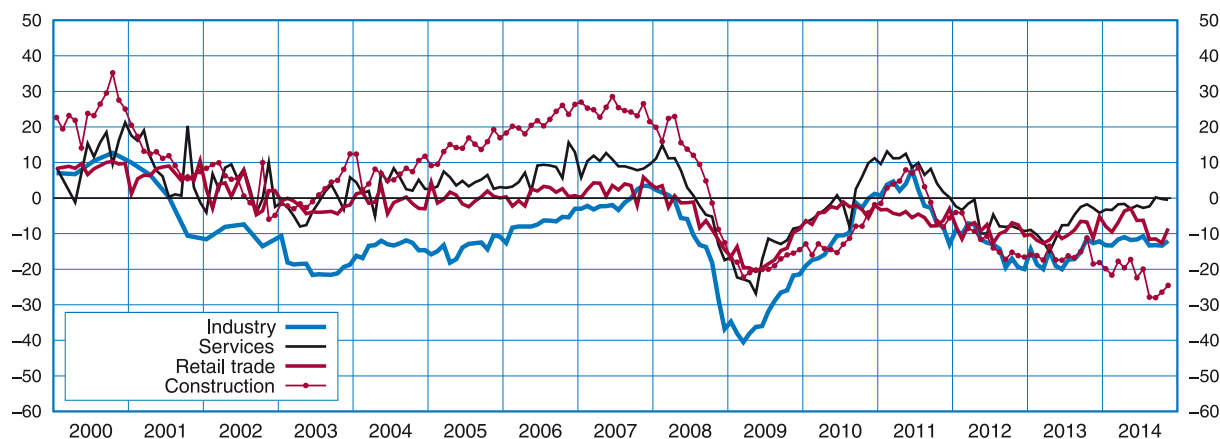
	2014				2015		2014 S1	2014 S2	2015 S1	2013	2014
	Q1	Q2	Q3	Q4	Q1	Q2					
"Emplois d'Avenir"	10	7	7	5	6	6	16	11	12	53	28
CUI-CAE (replaces CAE+CAV on 01/01/10)	10	6	3	-5	11	-4	16	-2	7	17	14
Total	20	13	10	-1	18	1	33	9	19	71	42

Forecast

Scope: Metropolitan France

Sources: DARES, INSEE calculations

3- Balance of opinion of business leaders on expected numbers



Source: INSEE, Business tendency surveys

In 2015, the CICE employment tax credit is set to ramp up and the Responsibility and Solidarity Pact (PRS) is to be introduced

The CICE employment tax credit will produce further effects in 2015 although the amount that businesses can claim will prove to be a little less than what was initially forecast

The tax credit for competitiveness and employment (CICE) introduced in 2013 is a tax benefit that applies to most businesses. The basis on which it is calculated is the gross remunerations paid in the course of the year, for wages not exceeding 2.5 times the minimum wage. On this basis, the subsidy is 4% for remunerations paid for 2013 and 6% for subsequent years.

According to the social declarations supplied by businesses to ACOSS and URSSAF, the CICE employment tax credit that could be applied for based on 2013 was €12bn in 2014. The amount of credit actually declared to the tax authorities should in theory have been the same amount. However, it is likely that it will eventually be between €10bn and €11bn from provisional data issued by the Public Finance Directorate General, and according to the 2014 report by the Committee monitoring the CICE employment tax credit. This would be only a temporary difference if it was due to late declarations (amounts that will be declared to the tax authorities in the next few years) or permanent if it was the result of deliberate choices made on the part of businesses (for fear of a tax inspection, for example). The description of the rise of the CICE proposed here uses smaller amounts than in the first ex ante estimates carried out last year¹; in particular, the theoretical annual amount of tax credit is reduced to €17bn in the long term, against €20bn in the initial estimates, and the amount is likely to be €16bn in 2015.

For 2015, at a given growth level, the CICE employment tax credit should produce 10,000 extra jobs per quarter

If the CICE employment tax credit is assimilated to a drop in social contributions applied to the lowest wages (less than 2.5 times the minimum wage), then it would directly enhance growth in employment, calculated at 15,000 extra jobs per quarter in H2 2013 and in 2014, and 10,000 extra jobs per quarter in 2015.

This effect takes into account the fact that some businesses, especially the largest ones and the smallest ones which have made use of a pre-financing mechanism, have anticipated the implementation of the tax credit system and have acted as if the tax credit were paid the same year as the remunerations on which entitlement is based, just as if there were a reduction in contributions. This factor, although neutral in the long term, must have enabled the tax employment credit to start creating jobs from 2013.

The effects of the CICE could be weakened for several reasons. First, it is applied in a context where operating margins are considerably lower than their pre-crisis levels; financial constraints may therefore play a larger part now than in the years before the crisis and companies may be eager to use the employment tax credit to improve their

financial situation, more than in the evaluations covering 1990s or 2000s, which serve to calibrate this evaluation, could lead us to expect. Also, the CICE should eventually be financed by fiscal measures (the increase in different VAT rates, in particular, had already been decided at the start of 2014), which reduces the effects of the mechanism on jobs. Also, in company accounting, the effect of the CICE is not always apparent in the company's operating account, as they may decide to record it at the bottom of the balance sheet. In this case, the link between the CICE and employee wages may not be easy to measure: thus companies' investment choices and hiring decisions may not incorporate the impact of the CICE, at least not immediately.

On the other hand, these effects could be seen to be more important if we take into account the effects of macroeconomic «closure» in addition to the direct effect of increased growth in employment.

The first measures of the Responsibility and Solidarity Pact are also likely to support employment and provide 10,000 jobs per quarter in 2015

After the CICE, the Responsibility and Solidarity Pact (PRS) is a new economic policy measure aimed at reviving growth and employment through reductions in labour costs and taxes. It is made up of two parts. The first, called «competitiveness», is aimed at businesses and will be introduced gradually between 2015 and 2020. The second, called «solidarity», will support the purchasing power of less well-off households through a reduction in income tax (removal of the first income bracket for income tax) and will come into force in 2015.

In 2015, among these measures, about €5.6bn would affect employment

Among the measures to come into force in 2015 for the benefit of businesses, two may affect employment directly:

- Labour costs are reduced via a €4.6bn reduction in employers' social contributions. Contributions to the Family branch of social security are reduced by 1.8 percentage points for wages less than 1.6 times the minimum wage. At the same time, exemptions from social contributions on the lowest wages, the «Fillon» reduction, are increased (see Graph).
- Taxation of companies is reduced via a €1.0bn decrease in the solidarity social contribution by companies (C3S). This reduction takes the form of an allowance which reduces the basis of tax assessment, i.e. turnover. When modelling this tax using the Mésange² macro-econometric model, it has been decided to transfer 70% of this reduction to labour costs and 30% to corporation tax.

All in all, these two measures can be likened to a decrease in employer social contributions of around €5.3bn, and in corporate taxes of €0.3bn in 2015.

(1) Total exemption from contributions for low wages

(2) C. Klein, O. Simon (2010) : Le modèle Mésange réestimé en base 2000. Tome 1 - Version avec volumes à prix constants.

French developments

Other measures have been taken, in particular a cut in contributions from sole proprietors and income tax reductions for modest households; however, these are more likely to have an effect on income (factored into the forecast) than a direct effect on jobs.

Reductions in the cost of labour for 2015 will focus on low wages, which will enhance the expected effects on employment

As with the CICE employment tax credit, reductions resulting from the Responsibility and Solidarity Pact will potentially affect the economy in several ways. Companies can increase their production capacity by hiring new staff or investing. They can also bring down their prices to gain market share. Finally, they can decide to improve their financial situation by taking advantage of these reductions to reduce their debt.

(3) On the profile of elasticity of labour demand against its cost, see Cahuc P. and Carcillo S. (2012), « Les conséquences des allègements généraux de cotisations patronales sur les bas salaires », *Revue française d'économie* 2012/2. and Malinvaud E., Gauron A. and Pisani Ferry J., (1998), « Les cotisations sociales à la charge des employeurs : analyse économique », *Les Rapports du Conseil d'analyse économique*, December 1998.

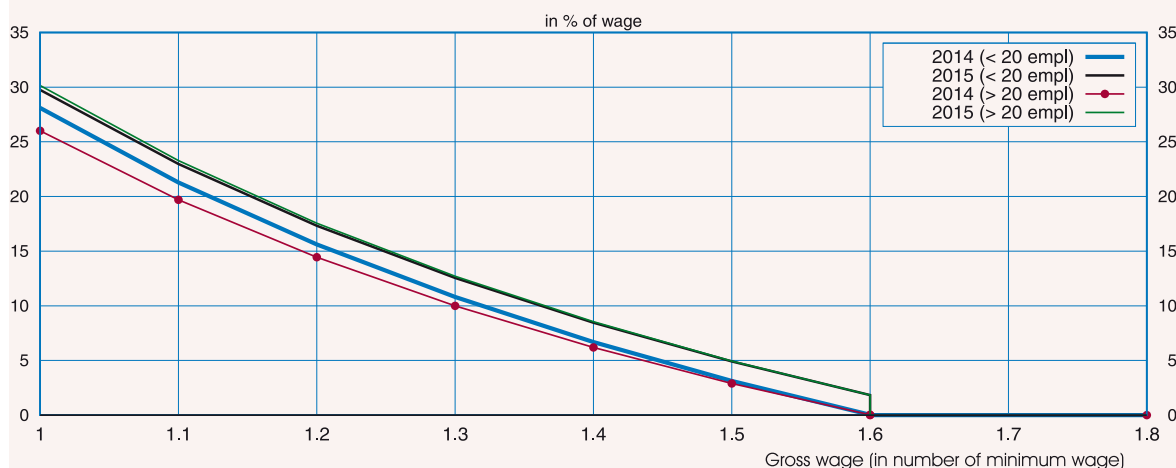
An overall reduction in employers' contributions of €4.6bn would represent a reduction of 0.6% in the average cost of labour. However, the planned reduction for 2015 covers low wages, less than 1.6 times the statutory minimum wage (see *Graph*). The effect that should be expected from this targeted measure is therefore greater than a blanket reduction of the same amount. Empirical studies are indeed in agreement that the profile of the elasticity of labour demand³ against its cost according to wage level would decrease sharply.

The extra jobs associated spontaneously with enhanced growth in employment would still be significant, and reach 10,000 jobs created or saved per quarter.

And again, as with the CICE employment tax credit, the favourable effects of the measure associated with additional activity would increase these spontaneous effects; however, effects linked with financing it would reduce them.

All in all, the effect of the two measures on enhancing the growth in employment is put at 15,000 jobs created per quarter since H2 2013 (due to the CICE) and 20,000 per quarter in 2015 (10,000 due to the employment tax credit and 10,000 due to the responsibility and solidarity pact). ■

Reductions in the cost of labour on low wages



Sources: LFRSS 2014 and PLFSS 2015. INSEE calculations

Unemployment

According to the results of the INSEE Labour Force Survey, the unemployment rate was 10.1% of the active population in Q2 2014, then 10.4% in Q3. In Metropolitan France, the unemployment rate went up from 9.7% in Q2 to 9.9% in Q3, the number of unemployed people increasing by 77,000.

During the quarters that follow, the expected slight increase in employment should not be enough to absorb the increase in the active population and the number of unemployed should increase slightly. The unemployment rate is therefore expected to rise during the coming quarters and should reach 10.6% by mid-2015 (10.2% in Metropolitan France).

In Q3 2014, the number of unemployed rose markedly

In Q3 2014, the number of unemployed increased by 77,000 in Metropolitan France, after being more or less stable in H1 (+7,000) and after a fall of 23,000 on 2013 (Table). The unemployment rate has thus increased, rising from 9.7% to 9.9% of the active population in the summer (Graph). It has thus returned to the level of one year before.

The unemployment rate for 15-24 year-olds increased by 1.0 percentage point on Q2

After a peak of 25.3% of active workers at the end of 2012, the unemployment rate for 15-24 year-olds fell throughout 2013, before stabilising at 22.7% in H1 2014. Young people benefited in

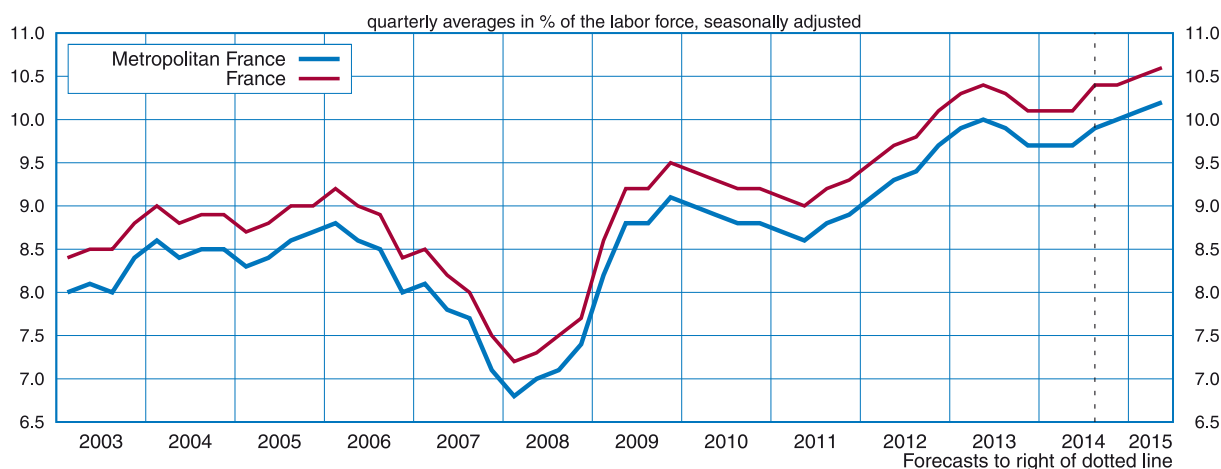
particular from the implementation of the *emplois d'avenir* programme devoted to people with no or few qualifications. Their unemployment rate, however, increased by 1.0 point in Q3 2014, settling at 23.7%. This rise may in part be due to the fall in employment in temporary work, a sector that employs mostly young people. Year-on-year, the unemployment rate for 15-24 year-olds is more or less stable (-0.1 point). The unemployment rate for 25-49 year-olds increased by 0.2 point on the previous quarter, like that for 50 year-olds and over. Year-on-year, their respective unemployment rate is stable.

The unemployment rates for men and women increased in fairly similar proportions, by 0.2 point and 0.3 point compared to the previous quarter, to 10.1% and 9.7% respectively. They are stable year-on-year.

The unemployment rate should increase again in early 2015

The active population should increase by 145,000 people in 2014 and by 64,000 people in Q1 2015. In the first place, the trend active population should increase by 68,000 people in H2 2014, then by 64,000 people in H1 2015. In addition, the growth of the active population should be stimulated by the extension of the legal retirement age to 61 years and 2 months since the beginning of 2014; it should, however, be limited by retirements for long careers, even if the effects of this reform should fade slightly in early 2015 (see «estimated effects of public policies» line in the Table).

1 - Unemployment rate in the sense of the ILO



France = Metropolitan France + Overseas Departments
Scope: Population of households, people aged 15 or over

Source: INSEE, Employment Survey

French developments

Net job creation, which should be +15,000 in H1 2015 after +34,000 in 2014, should be too low to absorb this rise in the active population and unemployment should increase again: the

unemployment rate is expected to stand at 10.0% at the end of 2014 in Metropolitan France (10.4% in France as a whole) then at 10.2% by mid-2015 (10.6% in France as a whole). ■

Changes to the active population, employment and unemployment in Metropolitan France

	quarterly changes										annual changes				
	2013				2014				2015		2011	2012	2013	2014	2015 S1
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2					
Population of the 15-64 age group	-23	-23	-22	-22	-22	-22	-22	-22	-8	-6	8	-95	-90	-89	-14
Population of the 15-59 age group	-21	-17	-14	-11	-9	-9	-9	-11	0	3	-80	-76	-63	-38	3
Labor force	17	2	-22	-26	56	5	75	11	34	31	217	210	-29	146	64
including:															
(a) Contribution of the population and the trend participation rate	30	30	30	30	34	34	34	34	32	32	165	146	120	135	64
(b) Estimated bending effects	-6	-5	-4	-4	-1	-3	-4	-7	2	-1	-6	15	-19	-14	1
(c) Other short-term fluctuations (residual)	-7	-24	-48	-52	23	-26	45	-16	0	0	57	49	-131	26	0
Employment	-29	-21	-2	46	37	16	-2	-15	6	9	166	-40	-6	36	15
Reminder: End-of-period employment (see "Employment" note)	-17	-25	22	70	4	28	-33	2	11	7	125	-51	49	2	18
ILO unemployment	46	23	-20	-71	19	-12	77	26	27	22	51	250	-23	111	49
	quarterly average										average in the last quarter of the period				
ILO unemployment rate (%)															
Metropolitan France	9.9	10.0	9.9	9.7	9.7	9.7	9.9	10.0	10.1	10.2	8.9	9.7	9.7	10.0	10.2
France (including overseas departments)	10.3	10.4	10.3	10.1	10.1	10.1	10.4	10.4	10.5	10.6	9.3	10.1	10.1	10.4	10.6

Forecast

How to read it:

- the Employment line presents variations in the number of people in employment as a quarterly average, for consistency with the other data in the table,
- employment and unemployment are not estimated here within strictly equivalent scopes: total population for employment, population of households (excluding collective) for unemployment. As the impact of this difference is very minor (the population outside of households represents less than 1% of the active population), it is neglected here for the unemployment forecasting exercise.

Source: INSEE