



CONJONCTURE IN FRANCE

March 2015

© Insee 2015

- Editorial director
Jean-Luc Tavernier

- Chief editors
Vladimir Passeron
Laurent Clavel
Bertrand Marc
Aurélien Fortin

- Contributors
Vincent Alhenc-Gelas
Franck Arnaud
José Bardaji
Anne-Juliette Bessonne
Stéphane Boucher
Clément Bortoli
Jocelyn Boussard
Guillaume Chanteloup
Stéphanie Combes
Véronique Cordey
Jeanne-Marie Daussin-Benichou
Vincent Dortet-Bernadet
Yannick Fendrich
Charles-Julien Giraud
Morgane Glotain
Yaëlle Gorin
Julie Goussen
Jorick Guillaneuf
Elodie Lalande
Quentin Laffeter
Thomas Laurent
Kevin Milin
Allaoui Mirghane
Pierre-Damien Olive
Mathilde Pak
Cécile Phan
Julien Pramil
Alain Quartier La Tente
Sophie Renaud
Catherine Renne
Sébastien Riou
Marie Sala
Anne-Marie Stoliaroff-Textier
Camille Sutter

- Editorial and pagesetting secretariat
Myriam Broin
Moussa Blaibel
Jacqueline Courbet
Denise Maury-Duprey

- Secretariat
Nathalie Champion

- Translation
Hancock Hutton

The issues of *Conjoncture* in France along with a glossary of economic outlook terminology are available as soon as they are published on the INSEE web server. in the "INSEE conjoncture" section of the website www.insee.fr

ISSN 1152-9776
Printed from supplied documents by
JOUVE - PARIS

Completed on 26 March 2015

A DROP OF FUEL TO DRIVE CONSUMPTION AND MARGINS

GENERAL OUTLOOK 7

SPECIAL ANALYSIS

- New advances in the use of INSEE's business tendency surveys to analyse the short-term economic outlook. 21
- Contribution from Google Trends for forecasting the short-term economic outlook in France: limited avenues 43

FRENCH DEVELOPMENTS

- Review of the previous forecast 59
- Output 61
- France's international environment 64
- Foreign trade. 67
- Employment 72
- Unemployment 77
- Consumer prices 79
- Wages 82
- Household income. 84
- Household consumption and investment 88
- Entreprises' earnings 91
- Corporate investment and inventory 93

INTERNATIONAL DEVELOPMENTS

- Oil and raw materials 99
- Financial markets. 102
- Eurozone. 107
- Germany. 110
- Italy 113
- Spain 114
- United Kingdom 117
- United States 118
- Japan 121
- Emerging economies 122

FOCUS

- The depreciation in the Euro and the fall in oil prices buoy up activity in France in early 2015. . . 16
- What are the consequences of the sharp rise in the Swiss Franc in early 2015? 69
- Subsidised contracts in 2014 75
- The ECB's quantitative easing policy should support the recovery underway in the Eurozone. . . 105
- The Greek risk for the French economy and the Eurozone 109
- German productivity should recover in H1 2015 111
- Corporate investment is the source of the Spanish recovery 115
- The stagnation of the import penetration rate in America since 2011 can be linked to the decline in oil product imports. 119

COUNTRIES ACCOUNTS 125

STATISTICAL FRENCH APPENDIX 129

A drop of fuel to drive consumption and margins

The end of 2014 was in line with expectations: the advanced economies became more dynamic while the emerging countries continued to slow down. In H1 2015, growth is likely to ease further in the latter: the Chinese economy in particular should slow down again, while Brazil and Russia are likely to be in recession. In the advanced economies, however, growth should firm up. It should remain robust in the USA and the United Kingdom and accelerate slightly in the Eurozone: +0.4% per quarter, after +0.3% at the end of 2014.

In fact, the Eurozone economies are benefitting from a combination of tailwinds, notably the fall in oil prices. The oil countershock underway since the summer of 2014 is boosting household purchasing power and consumption. The latter is also being stimulated by the slowdown in taxes and social contributions which are now less of a burden on the dynamics of their income. Eurozone exports are also benefitting from a substantial fall in the Euro, which fell to its lowest level against the dollar since 2003 in mid-March. The business tendency surveys do show, however, that the different European economies do not seem to be benefitting from these positive factors in the same way, in particular as regards corporate investment behaviour. In Germany, growth is set to remain sustained as the introduction of a minimum wage at the start of the year stimulates consumption in the short term, and investment in production should be driven by demand prospects. Spain is likely to confirm its dynamism, driven both by consumption and corporate investment. The recovery in Italy, however, should be very slow, after three years of falling activity.

Growth in the French economy is likely to be close to the Eurozone average, with contrasting components of demand. Like their European neighbours, households are set to consume at a more sustained rate, reaching +1.5% year-on-year by mid-2015, driven by purchasing power. However, the business tendency surveys show a continuing wait-and-see attitude among companies, with their prospects appearing to gain little from these new winds: the

business climate has progressed only slightly since November and still remains below its long-term average. This being the case, companies are likely to be little inclined to accelerate their investment expenditure which is expected to be flat, despite enjoying favourable financing terms at present: with the ramp-up of the Tax Credit for Competitiveness and Employment (CICE) and the start of the Responsibility Pact, their margin rate should rise significantly in H1, to its highest since early 2011. Household investment, meanwhile, should continue to fall back.

All in all, GDP should accelerate to +0.4% in Q1 2015, driven by a one-off rebound in energy production after the mild autumn, and then progress in Q2 by 0.3%. Year-on-year, the rise in activity should reach +1.1% by mid-2015, its highest rate since the end of 2011.

The upturn in activity and policies to boost growth-driven job creations are unlikely to be enough to halt the fall in market-sector employment, although it should be less pronounced in early 2015 than it was in 2014. Total employment is likely to progress slightly (+20,000 in this half year, after -17,000 in the previous half), driven once again by subsidised employment contracts in the public sector. As the labour force is still growing significantly, unemployment is likely to continue increasing from 10.4% at the end of 2014 to 10.6% in mid-2015.

This scenario is subject to several uncertainties. In particular, recent fluctuations in oil prices show that the market is still in search of its equilibrium price. If Brent falls again or rises, the expected effects will either be reinforced or limited. Also, the current gap between the perception of agents, in particular companies, and the expected effect of the positive winds blowing on the French economy is a source of uncertainty. If this gap is narrowed in an upwards direction by a brightening of the business climate, activity and investment could provide a positive surprise, while if it is narrowed "downwards", any take-off in growth may be postponed once again.

At the end of 2014, the emerging economies slowed down while the advanced economies accelerated

The emerging economies slowed again in Q4 2014

In Q4 2014, the short-term outlook remained relatively poor in the major emerging economies. China, for example, slowed down again (+1.5% after +1.9%), posting growth of +7.4% in 2014, its lowest since 1990. Likewise, growth stalled in Brazil under the combined effects of the fall in commodity prices and past moves to tighten monetary policy, while Russia is suffering from the fall in oil prices and economic and financial sanctions.

Growth in the advanced economies remained buoyant

In Q4 2014, the advanced economies slowed down only slightly (+0.5% after +0.6%), posting slightly stronger growth than forecast in *Conjoncture in France* in December 2014 (+0.4%). After two quarters of very strong expansion, activity slowed down, while remaining buoyant, in the US (+0.5% after +1.2%) and the UK (+0.5% after +0.7%). The Japanese economy, meanwhile, grew moderately (+0.4%, as forecast), after two quarters of recession in the wake of the VAT hike on 1st April 2014.

GDP accelerated moderately in the Eurozone

In the Eurozone, GDP accelerated moderately again (+0.3% after +0.2%), mainly driven by Germany (+0.7% against a forecast of +0.2%), where consumption surprised by its vigour, and Spain (+0.7% against a forecast of +0.6%). As expected, growth was sluggish however in France (+0.1%) and Italy (0.0%). In the Eurozone as a whole, household consumption continued to progress quickly (+0.4%) and investment rebounded, both in equipment (+0.2% after -0.3%) and construction (+0.4% after -0.6%).

In France, activity progressed little in Q4 2014

As expected, activity progressed little in France at the end of 2014

In Q4, activity grew only slightly in France (+0.1% after +0.3%), as expected in *Conjoncture in France* in December 2014. The slowdown was partly due to the marked fall in energy production (-2.5% after +1.7%), under the effect of the mild autumn temperatures. Manufacturing output fell back slightly (-0.1% after +0.6%), notably due to transport equipment (-2.8%), while activity was dynamic in capital goods (+1.5%). Output barely slowed in market services (+0.4% after +0.5%) and in trade (+0.5% after +0.9%). Construction activity, however, contracted again sharply (-0.8% after -1.0%).

World trade and the fall in oil prices set to buoy up activity through to mid-2015

World trade should be relatively dynamic in H1 2015

After a rebound in Q3 (+1.9%), world trade slowed down in Q4 (+1.3%), notably due to imports in the emerging countries (+1.9% after +3.6%). In H1 2015, the first available quantitative indicators and the business tendency surveys suggest that world trade should remain on the same rate of growth (+1.0% per quarter), distinctly less than its pre-crisis progression (+1.6% per quarter between 2000 and 2007).

The oil price fell sharply through to January

The fall in oil prices since June 2014, when Brent stood at \$111.8 (€82.2) per barrel on average, continued through to January 2015, when it reached \$48.4 (€41.6), its lowest level since May 2009. This fall is mainly driven by the easing of tensions on the physical market, with world supply exceeding demand; it would also seem to be the result of a downward revision in expectations of demand, especially in China and the emerging countries. But the market is in search of a new equilibrium price: in February, the price rose again to \$57.9 (€51.0), notably after the announced reductions in drilling in the US and lower investments by the large oil groups, before levelling out at around \$55 (€50.8) in March. In the scenario detailed in this issue of *Conjoncture in France*, the oil price is fixed at this level.

The short-term outlook should remain favourable in the advanced economies in H1 2015

The emerging economies set to slow down further

The business tendency surveys show no sign of improvement in the short term in the emerging countries, where the slowdown is set to continue in H1 2015. In China, consumption should progress modestly and investment continue to slow down, despite first signs of improvement in real estate. For Brazil and Russia, it is the risk of entering recession that dominates: high inflation is weighing down on the purchasing power of households whose confidence is falling, the drop in commodity prices and slowdown in the other emerging countries are reducing export revenues and, finally, successive monetary tightening measures are holding back investment.

Growth in the advanced economies should remain sustained

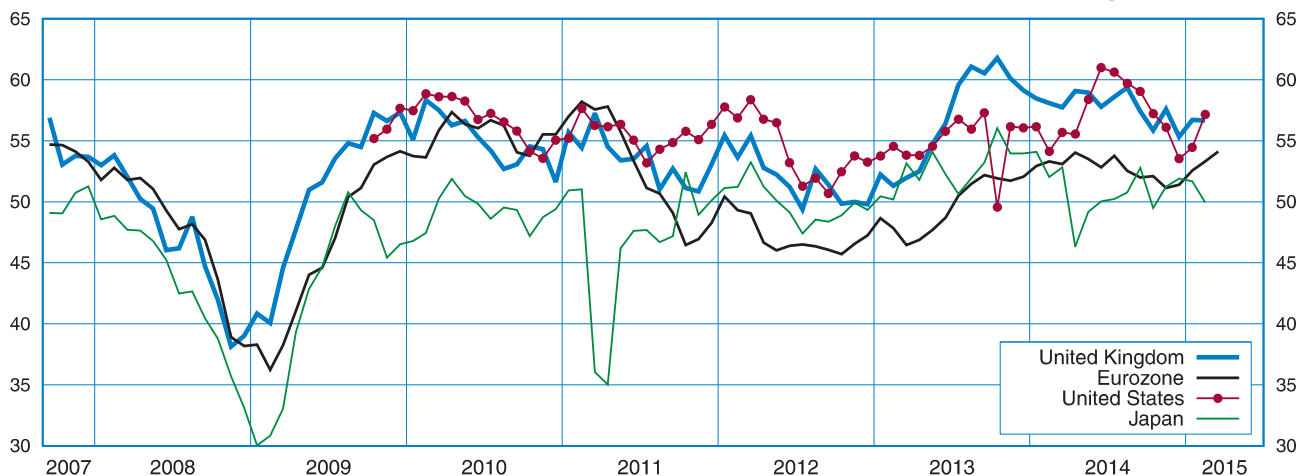
In the advanced economies, the short-term outlook remains favourable in early 2015 and even improved slightly in March (Graph 1). Activity there is likely to post a comparable growth rate to that in H2 2014 (+0.5% in Q1 then +0.6% in Q2). In the United States, growth should remain sound even though activity slowed down in Q1 due to the harsh winter (+0.4% then +0.7%), despite the rise in the Dollar and thanks to robust private demand: consumption should continue to benefit from the fall in unemployment and buoyant purchasing power, while investment should remain dynamic, supported by positive demand prospects. Likewise, British domestic demand should buoy up growth which is unlikely to weaken (+0.5% per quarter, as in Q4). The Japanese economy is likely to continue recovering in H1 2015 (+0.8% then +0.6%), notably thanks to combined support from the improving labour market, falling energy prices and a new fiscal stimulus. Among France's main partners in the Eurozone, activity should be favoured by the drop in oil prices, which is driving household purchasing power, and by the falling exchange rate, which boosts the competitiveness of companies.

In H1 2015, the Eurozone should continue to accelerate slightly

The ECB in turn has launched a quantitative easing programme

After the end of quantitative easing, a rise in base rates in the USA and the United Kingdom would seem to be approaching as the return of growth is confirmed. However, the new fall in inflation resulting from the drop in oil prices and rise in currencies has once again postponed the prospect, and in the light of inflation expectations, the Bank of England and the Fed are likely to keep their interest

1 - The short-term outlook remains favourable in the advanced economies in early 2015



Source: Markit

rates and balance sheets unchanged through to mid-2015. In the Eurozone, faced with the fall in present and expected inflation, the ECB started implementing quantitative easing in early March, which is likely to increase its balance sheet substantially, to return to its 2012 level by mid-2016.

Quantitative easing should stimulate the Eurozone credit market

In the Eurozone, quantitative easing should stimulate credit, the contraction in which should gradually ease in the southern European countries. Weak credit is partly due to demand factors (non-financial private agents are continuing to reduce their debt), but also to difficulties in the transmission of the ECB's accommodating monetary policy. A large proportion of European banks are continuing their refinancing with the ECB thanks to the liquidity it is lending in its very long-term refinancing operations, especially in the peripheral countries, where the financial institutions remain fragile. Expectations of the ECB's various measures to ease monetary policy have also led to a marked fall in the Euro since summer 2014. The Euro thus fell from \$1.37 in May 2014 to less than \$1.10 in March 2015. The effective real exchange rate has therefore fallen significantly (for France: -3.1% in Q1 2015, after -0.5% at the end of 2014).

Eurozone activity should continue to accelerate slightly

In the major Eurozone countries, the business climate as shown in the business tendency surveys has returned to a level close to its long-term average, in industry and services alike. Stimulated by the fall in oil prices and the Euro, activity is set to continue accelerating slightly in the Eurozone and its rise should reach +0.4% per quarter in H1 2015. Despite common supporting factors (oil, exchange rates), divergences continue in the outlook within the Eurozone: Spain (+0.7% per quarter) and Germany (+0.6% then +0.4%) are likely to grow more strongly, thanks to vigorous domestic demand, while Italy should return to as yet very moderate growth (+0.1% then +0.2%).

Eurozone consumption likely to grow at a more sustained rate

The fall in oil prices is stimulating European household purchasing power and therefore expenditure. Consumption should thus grow at a more sustained rate in the Eurozone (+0.7% then +0.5% in Q1 and Q2 2015 in the Eurozone as a whole), especially in Germany (+0.9% then +0.7%), thanks to the additional income provided by the introduction of a minimum wage, and in Spain (+1.0% per quarter) where the upturn in employment is strong.

Investment to remain sluggish in the Eurozone

Despite this favourable context and the ECB's quantitative easing which should allow a gradual improvement in financing terms, investment should remain sluggish in the Eurozone in H1 2015 (0.0% then +0.2%). The fall in investment in new housing has come to an end in Spain and should ease in France. Corporate investment, however, should barely progress and even continue to fall in Italy (-1.0% then 0.0%).

French exports likely to be buoyed up by the recent fall in the Euro

French exports boosted by the recent fall in the Euro

Driven by the relative dynamism of world trade, world demand for French products should progress by 0.8% in Q1 then by 1.1% in Q2. After the sharp rebound in aeronautics exports at the end of 2014, exports should slow down, however, due to a backlash effect in Q1 2015 (+0.8%), before accelerating slightly (+1.2% in Q2), buoyed by the fall in the Euro (Focus).

The French economy should return to stronger growth in H1 2015

The business climate in France has progressed only slightly since November

After deteriorating in summer 2014, the business climate in France improved again in November, returning to the same level as in H1 2014. The business climate in France has progressed only slightly since then, to a level (96 in March 2015) that is still below its long-term average (100). Looking at the different

sectors (*Graph 2*), the composite indicators are close to their long-term average in manufacturing industry (99 in March) and above it in retail trade (104). They are lower in services (93) and building construction (89).

Manufacturing output should accelerate moderately in H1

In manufacturing industry, production prospects among business leaders have been on a more positive trend since September and the corresponding balance of opinion is back above its long-term average. Manufacturing output should therefore accelerate in Q1 (+0.4%), as confirmed by the growth overhang in industrial output at the end of January (+0.5%). Manufacturing output should then progress at almost the same rate (+0.3%) in response to accelerating foreign demand.

The French economy should accelerate a little in H1 2015

According to business leaders in services surveyed in March, the business climate still remains relatively morose and activity in market-sector services should progress in H1 at a rate close to its average since 2010 (+0.4% per quarter on average). After a sharp fall in Q4 2014 (-2.5%), when mild autumn temperatures reduced heating expenditure, energy production should rebound considerably in Q1 (+2.9%), before returning to a rate closer to its trend in Q2 (+0.6%). Finally, the fall in activity in construction should barely ease in H1 2015 (-0.7% then -0.6% after -0.8% at the end of 2014): investment in new housing should fall less in H1 2015 than in 2014, but the continuing fall in building permits for non-residential buildings provides no sign of any clear improvement.

The annual growth overhang should reach +0.8% by mid-2015

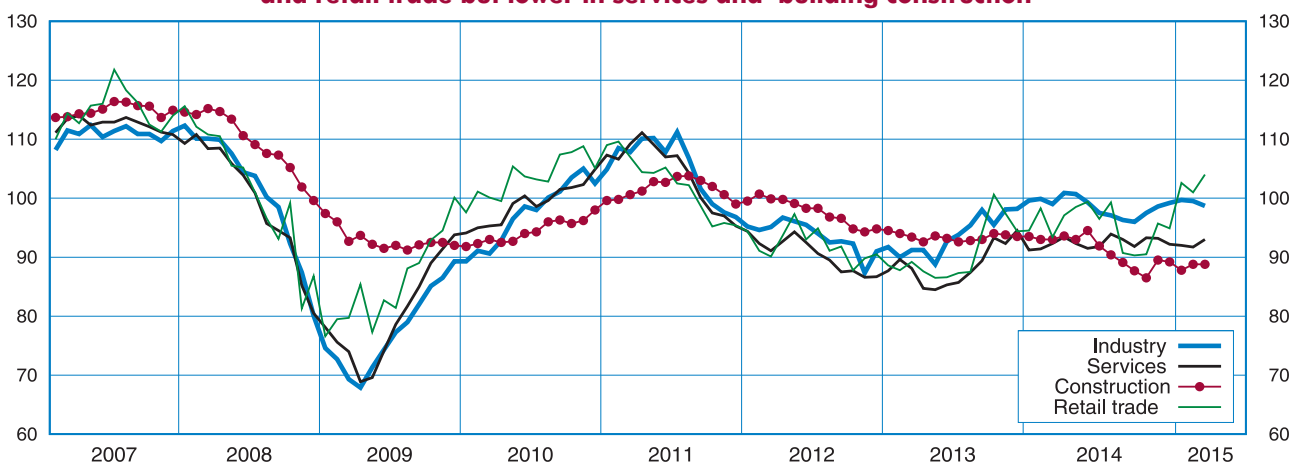
All in all, GDP should accelerate significantly in Q1 2015 (+0.4% after +0.1%). The upturn in growth should be driven by the upturn in energy production (contribution of +0.2 percentage points to the acceleration). As this effect fades out in Q2, activity should slow down, although remaining at a higher rate (+0.3%) than the average since spring 2011 (+0.1%). By mid-2015, the annual growth overhang should be +0.8%, after three very sluggish years (+0.4%).

Total employment set to progress and unemployment to increase slightly in H1 2015

The CICE and Responsibility Pact should buoy up market-sector employment in H1 2015

After a sharp downturn in the previous quarter, interim employment rebounded in Q4 2014 (+24,000 jobs after -22,000), almost allowing market-sector employment to level out (-1,000 jobs), despite further falls in industry and construction. Market-sector employment is set to fall again in H1 (-13,000 jobs): the slight acceleration in activity and the support provided by the cumulative

2 - The business climate is close to its average in industry and retail trade but lower in services and building construction



Source: INSEE

General outlook

effects of the Responsibility and Solidarity Pact and the ramp up of the Tax Credit for Competitiveness and Employment (CICE) should make for a smaller fall than in H2 2014 (-61,000 jobs).

Total employment to start rising again slightly in H1 2015 driven by subsidised employment contracts

In 2014, employment in the non-market sector progressed significantly (+65,000), largely due to subsidised employment contracts (+49,000), of which the number of beneficiaries grew over the year as a whole. It should be the same in H1 2015: non-market employment is likely to increase by 23,000, of which 20,000 subsidised jobs. Total employment should therefore start rising again in H1 2015 (+20,000 jobs, after -17,000 in H2 2014), this acceleration being the result mainly of the lesser fall in market-sector employment.

The unemployment rate should reach 10.6% in mid-2015

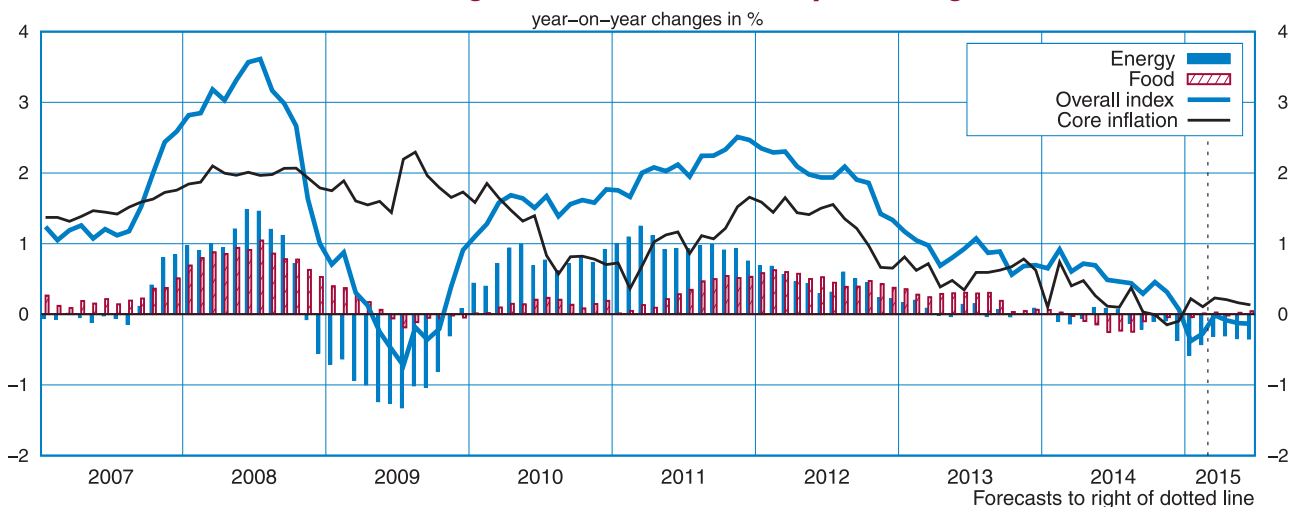
In Q4 2014, the unemployment rate stood at 10.4% of the labour force on average (10.0% in Metropolitan France), after 10.3% in the previous quarter. In H1 2015, the expected slight rise in employment is unlikely to be enough to offset the growth in the labour force and the number of unemployed should rise slightly. The unemployment rate should increase again and could reach 10.6% by mid-2015.

Inflation likely to remain very low through to mid-2015

Inflation likely to remain very low through to mid-2015

In January and February 2015, headline inflation was negative year-on-year for the first time since 2009 (-0.4% and -0.3% respectively). It should remain very low through to mid-2015, at -0.1% in June 2015 (*Graph 3*). In particular, on the assumption that the barrel of Brent remains stable at \$55 (€50.8), the year-on-year change in energy prices would remain very negative, at -4.3% in June 2015. Core inflation should remain very moderate: the core inflation indicator calculated by INSEE, excluding volatile products and the mechanical impact of modifications in indirect taxation, should show growth that is close to zero year-on-year in June 2015 (+0.1%), as the impact of the VAT hike on 1st January 2014 and its effects almost fade out.

3 - Inflation to remain negative and core inflation very low through to mid-2015



Source: INSEE

Purchasing power to accelerate through to mid-2015, buoyed by disinflation

Wages likely to slow down in H1 2015

Average wage per capita in the market-sector branches was slightly more dynamic in 2014 (+1.7%) than in 2013 (+1.5%). It did slow down however in the course of the year, at +0.6% in H2 after +0.8% in H1. Under the effect of the past fall in inflation, a moderate rise in the minimum wage on 1st January 2015 (+0.8%, making 0.3 points less than in 2014) and rising unemployment, nominal wages should slow down again in H1 2015 (+0.3%). In real terms, wages should also slow down (+0.3% in H1 2015, after +0.8% in H2 2014).

Household purchasing power should accelerate, buoyed by disinflation

After stagnating in 2013, household purchasing power showed a marked upturn in 2014 (+1.1% annual average), due to the acceleration in earned income (+1.3% after +0.9%) and, above all, less dynamic taxes and social contributions (+2.1% after +4.2%). In H1 2015, it should accelerate further (+1.6 year-on-year in mid-2015 against +0.7% one year earlier), notably due to the sharp fall in inflation (Graph 4).

Household consumption to accelerate significantly in H1 2015

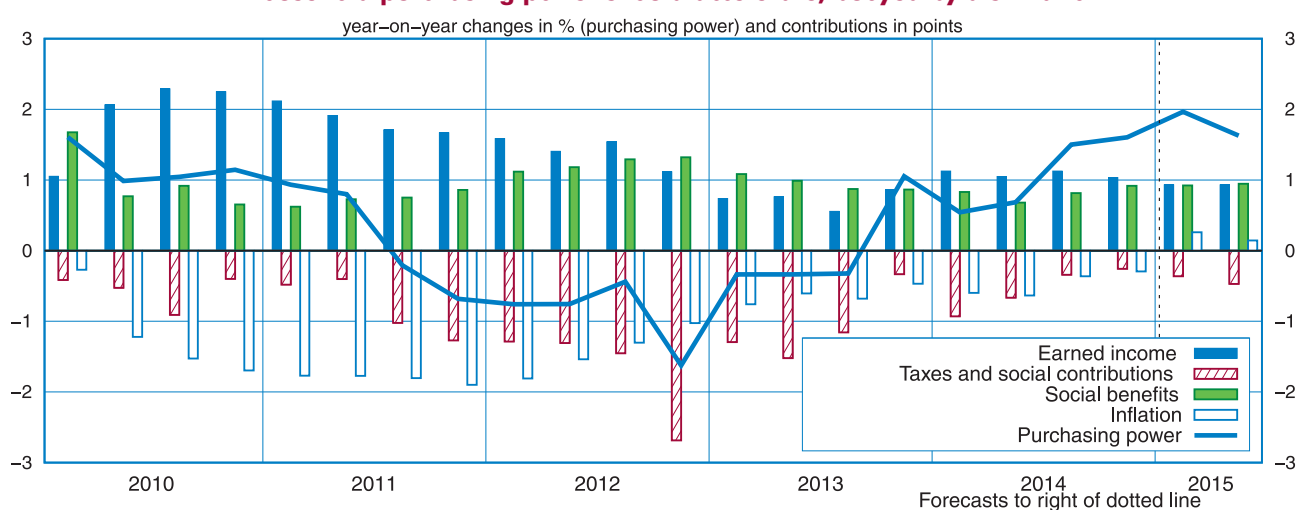
Household consumption should increase sharply in Q1

After a slowdown in Q4 2014 (+0.2%), due to a marked fall in heating expenditure caused by the very mild autumn, household consumption should rebound in Q1 2015 (+0.6%) as energy expenditure returns to normal. The first quantitative information also indicates that purchases of manufactured products should remain dynamic (+0.5% after +0.6%).

In H1 2015, consumption should remain sustained by dynamic purchasing power

In Q2, the effects of the climate on consumption should fade out and consumption slow down. It should remain at a dynamic level (+0.3%), however, compared to its trend in recent years (quarterly average of 0.0% between 2011 and 2014), driven by the acceleration in household purchasing power. Smoothing out this extra purchasing power over time, households are likely to increase their savings ratio slightly, to 15.6% in mid-2015 against 15.4% one year earlier.

4 - Household purchasing power should accelerate, buoyed by disinflation



Source: INSEE

Corporate investment to be almost stable

The fall in household investment set to ease a little

After levelling out in the course of 2014, the number of building permits decreased again at the start of the year, for both individual and collective housing. Expenditure on home maintenance and improvement is likely to remain on a downward trend. All in all, household investment should fall a little less in H1 2015 (-1.0% per quarter) than in H2 2014 (-1.6% then -1.5%).

The corporate margin rate should improve significantly in H1 2015 but corporate investment is likely to remain almost stable

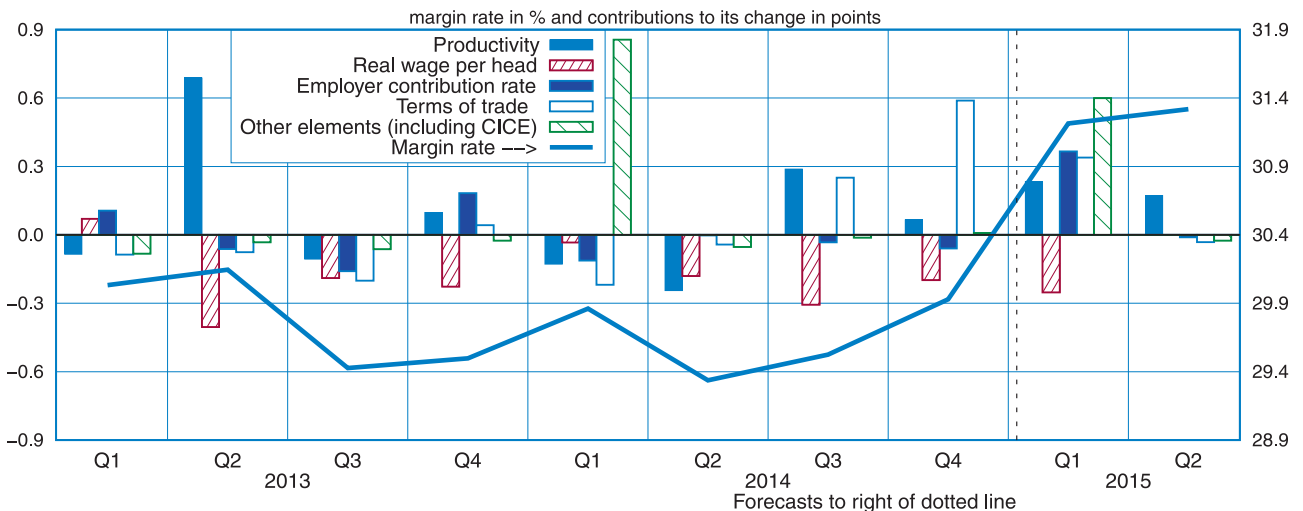
Many of the conditions are now fulfilled for corporate investment to accelerate. First, the corporate margin rate should improve significantly in H1 (Graph 5), thanks to the combination of three factors beginning in Q1: the ramp up of the CICE, implementation of the Responsibility and Solidarity Pact and the continuing improvement in terms of trade driven by the fall in petroleum product prices. Next, companies are also benefitting from much more accommodating financing terms than in past years. Finally, domestic and foreign demand prospects are now more favourable. However, the business tendency surveys, in particular in services, indicate that business leaders are likely to continue with their wait-and-see attitude and will be little inclined to accelerate their investment significantly. Corporate investment is likely to be almost stable in H1 2015, with a further fall in investment in construction (-0.4% per quarter) offsetting the slight rise in other expenditure overall.

Uncertainties: oil price and confidence

Oil price

In our scenario, the oil price is forecast to stay at its recent level (\$55), thereby allowing household consumption to benefit to the full from the fall over the past year. However, in a context where supply outstrips demand and stocks are already large, the fall in oil prices that came to a halt in January could resume. If that were to be the case, it would support household purchasing power and the financial situation of businesses even further. Conversely, renewed geopolitical tensions (over the Iranian nuclear programme, for example) or a further downward revision in expectations of supplies could lead to a new correction upwards.

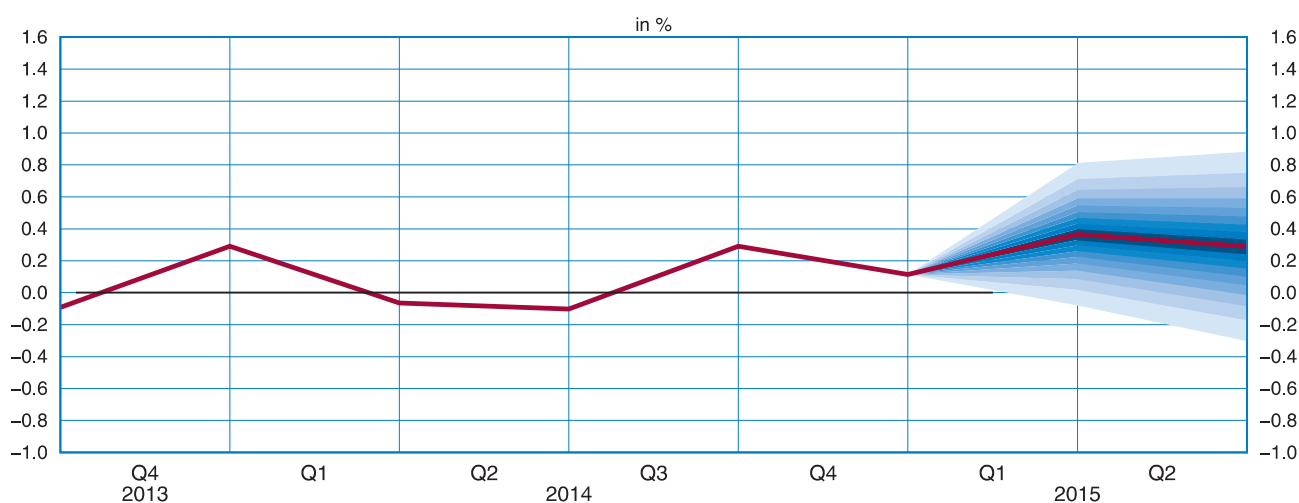
5 - The margin rate of non-financial corporations should its a very marked upturn in early 2015



Household confidence and business climate

In our scenario, household consumption accelerates in France and its European partners, in particular thanks to the additional purchasing power provided by the fall in energy prices. In early 2015, French households declare themselves to be a little more confident as to the financial situation, although at a level that is well below the long-term average. However, investment by French corporations is likely to remain sluggish in H1 2015, despite the presence of many factors that should drive a more significant acceleration. There is therefore a gap between the perception of agents, and in particular companies, and the boost provided by the fall in oil prices, the fall in the exchange rate and the more accommodating policy mix in the Eurozone. This gap could be narrowed in an “upwards” direction if it is a sign of great caution towards the first signs of improvements in demand: in this case, growth could gradually become more dynamic and turn out to be stronger than expected. The gap could also be reduced “downwards” if it is a sign of structural difficulties preventing French companies from benefitting fully from this favourable environment: growth would thus be held back and disappoint once again. ■

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 Q1 2015 has a 50% chance of being between +0.2% (lower limit of the fifth band from the bottom) and +0.5% (upper limit of the fifth band from the top). Likewise, it has a 90% chance of being between -0.1% and +0.8%. In Q2 2015, the 90% confidence intervals is [-0.3% ; +0.9%].

Source: INSEE

The depreciation in the Euro and the fall in oil prices buoy up activity in France in early 2015

In *Conjoncture in France* in December 2014, the cumulative effect of the fall in the exchange rate and in the oil price in H2 2014 was estimated at an extra 0.4 percentage points of GDP growth between Q4 2014 and Q2 2015, of which 0.3 points in the first two quarters of 2015.

This estimate must now be updated to take account of the changes in oil prices and in the exchange rate from the December hypotheses. For example, the actual oil price was lower than that used for December's forecast: \$76.8 per barrel in Q4 2014 instead of \$79.5 per barrel; \$55.1 on average in Q1 2015 instead of \$70 in *Conjoncture in France* in December 2014. For Q2, the assumption is \$55 per barrel instead of \$70. On the other hand, the fall in the real effective exchange rate was less (-0.6%) than expected in Q4 (-1.7%), partly due to the sharp fall in the Ruble and, to a lesser extent, in the Yen. In Q1 2015, however, the Euro fell again against the Dollar (to \$1.13 on average, making a fall of 9.6%), resulting in a substantial fall in the real effective exchange rate (-3.1%). For Q2, the exchange rate has been set at a lower level than in the previous *Conjoncture in France*, notably against the Dollar, with a forecast at \$1.08 for €1, against \$1.23 for €1 previously.

The fall in oil prices and in the Euro should therefore have a more favourable overall effect in this period than in the previous *Conjoncture in France*, even though some of those effects will come into play after the time horizon of this forecast. The cumulative effect of these two positive shocks is now estimated at an extra 0.4 percentage points of growth in GDP over the first two quarters of 2015.

A simultaneous fall in oil prices and the exchange rate never seen before in the Eurozone

Between June 2014 and February 2015, the price per barrel of oil in Dollars fell by 48%, from an average of \$111.8 per barrel to \$57.9, after reaching a low of \$48.4 in January. At the same time, the Euro fell sharply against most other currencies,

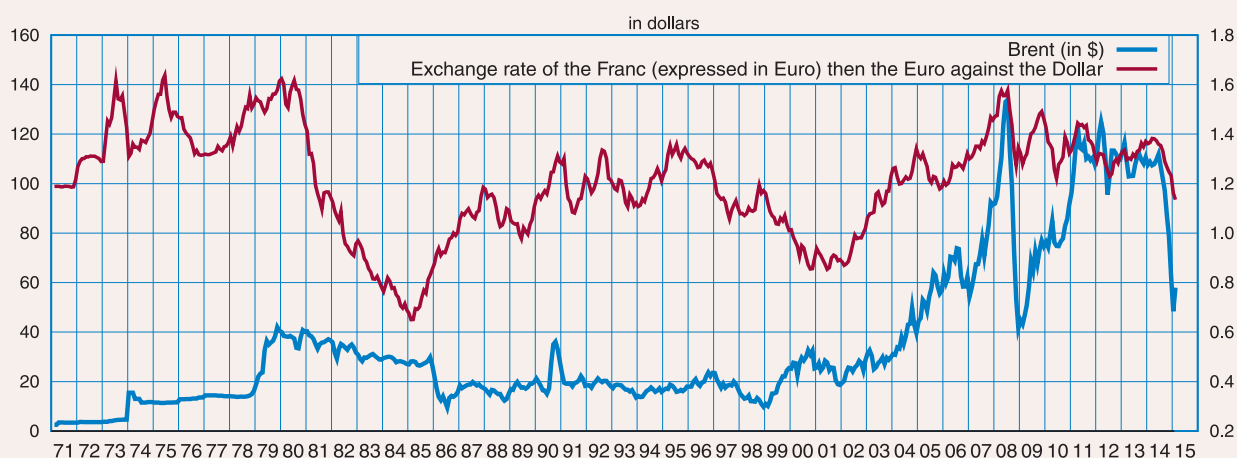
especially against the Dollar (from \$1.36 to \$1.13 for €1, representing a fall of 16.5%). Over the period, the real effective exchange rate fell by 4.8%. Such a simultaneous fall in oil prices and exchange rates has never been seen before since the creation of the single currency (*Graphs 1 and 2*).

Over the longer term, with the exception of the sharp fall in oil prices in the great recession of H2 2008, the last sharp fall in the price per barrel of Brent dates back to 1985 and 1986. That first "oil countershock" was triggered by an increase in Saudi output. At that time, the price of Brent fell from \$29.8 per barrel on average in November 1985 to \$9.6 in July 1986, a fall of 68%. However, today's oil countershock comes in a context that is different in a number of ways. First of all, the share of household consumption dedicated to energy has decreased (9% in 2013 against 11% in 1985, in value), thereby reducing the positive impact of the fall in oil prices on purchasing power. Likewise, France's energy dependence on oil has decreased, further reducing the positive impact of such a fall on the economy: the share of oil in household energy consumption has fallen from 71% in 1985 to 62% in 2013. The combination of the different shocks was also different: the 1986 countershock was accompanied by a sharp rise in the Franc against the Dollar, amplifying its effect on household purchasing power but reducing the positive effect on GDP, as French exporters lost market share, with the fall in the Dollar boosting the competitiveness of the United States and also of many emerging countries whose currencies were pegged to the Dollar at the time.

The falls in the Euro and oil prices since the summer should increase French growth by about 0.4 percentage points in H1 2015

For an oil-importing country like France, a pronounced fall in the price per barrel leads to a fall in inflation in the short term, thereby allowing an increase in household consumption via the rise in the purchasing power ("first-round" effects). The difference in energy

1 - Changes in the price of Brent and the exchange rate since 1971



Sources: FMI, Federal Reserve

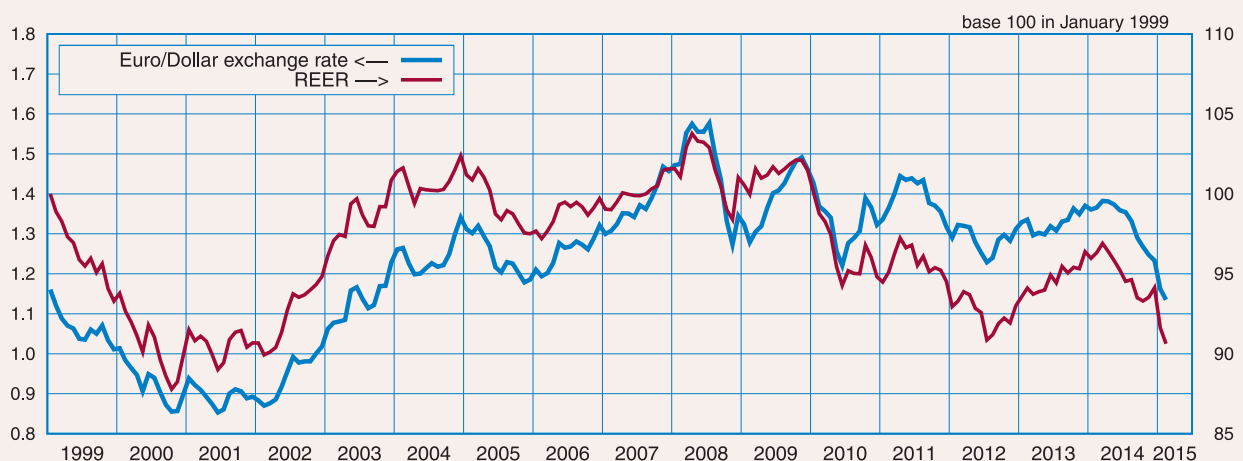
inflation between Q2 2014 and Q1 2015 should therefore contribute 0.4 percentage points to the increase in household purchasing power between these same two quarters (+1.3points, Graph 3). As a comparison, the slowdown in taxes and social contributions contributed 0.8 percentage points to the rise in income between Q3 2013 and Q3 2014.

The additional purchasing power provided by the fall in oil prices is being passed on progressively to consumption and then GDP. The fall in oil prices is also working through into producer prices via intermediate consumption, and to wages via the price-wages loop ("second-round" effects). In so doing, it increases corporate margins by improving terms of trade. Foreign effects are added to these domestic mechanisms: the oil-exporting countries are suffering from a decline in their resources and in their demand for French products. Conversely, additional activity in the other oil-importing countries which are benefitting from the fall in oil prices is leading them to increase their imports. In the light of the structure of France's foreign trade, it is this second effect that

prevails: French exports are increasing in volume, driven by more dynamic world demand. All in all, the effect of the fall in oil prices is estimated to represent about an extra 0.3 percentage points of growth in GDP in H1 2015. However, the positive effects of the fall in oil prices on world demand for French products are being lessened by the new slowdown in several emerging countries, notably China, Russia and Brazil.

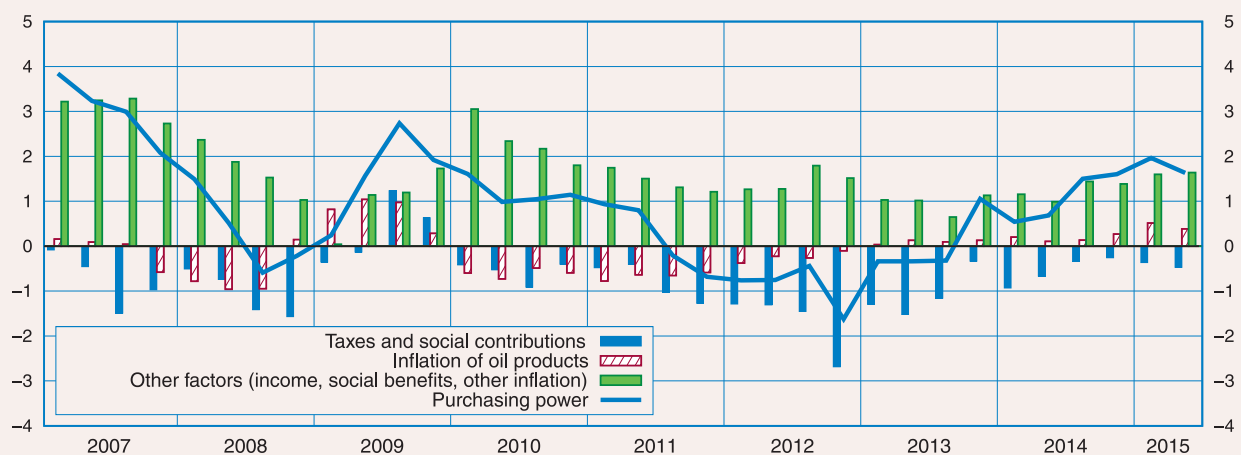
Likewise, the fall in the Euro against most currencies that started in summer 2014 was accentuated in Q1 2015, notably due to the announcement and then implementation by the ECB of its quantitative easing programme. This fall in the Euro should buoy up activity by an extra 0.1 percentage points of growth in GDP in H1 2015, all other things being equal, on account of the mechanisms presented in the box entitled "What are the effects of the recent falls in the Euro and oil prices?" in *Conjoncture in France* in December 2014. All in all, the cumulative effect of the fall in the Euro and in oil prices should therefore be about an extra 0.4 percentage points of growth in GDP in H1 2015. ■

2 - Changes in the Euro/Dollar exchange rate and the real effective exchange rate since 1999



Sources: INSEE, DG Tresor

3 - Year-on-year change in purchasing power and contributions



Source: INSEE

Key figures: France and its international environment

	2013				2014				2015		2013	2014	2015 ovhg
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2			
International environment													
Advanced economy GDP	0.4	0.5	0.7	0.6	0.2	0.4	0.6	0.5	0.5	0.6	1.4	1.8	1.7
Eurozone GDP	-0.4	0.3	0.2	0.3	0.3	0.1	0.2	0.3	0.4	0.4	-0.4	0.9	1.1
Barrel of Brent oil (in dollars)	112.6	103.5	109.6	109.4	108.1	109.7	103.8	76.8	55.1	55	108.8	99.6	55
Euro-dollar exchange rate	1.32	1.31	1.32	1.36	1.37	1.37	1.33	1.25	1.13	1.08	1.33	1.33	1.09
World demand for French products	0.9	2.5	0.9	0.1	0.8	0.4	1.6	0.6	0.8	1.1	3.1	3.3	3.0
France - supply and use													
GDP													
Imports	-0.1	0.7	-0.1	0.3	-0.1	-0.1	0.3	0.1	0.4	0.3	0.4	0.4	0.8
Household consumption	0.4	2.0	1.0	0.2	0.8	0.7	1.7	1.7	0.8	0.8	1.9	3.9	3.8
Public and NPISH consumption	0.2	0.2	0.0	0.5	-0.3	0.4	0.3	0.2	0.6	0.3	0.3	0.6	1.3
Total GFCF	0.5	0.7	0.3	0.5	0.3	0.4	0.6	0.5	0.4	0.5	1.9	1.8	1.6
of which: NFEs	-0.4	0.2	0.0	0.1	-0.7	-0.8	-0.6	-0.5	-0.3	-0.3	-0.8	-1.6	-1.4
Households	-0.8	0.5	0.3	1.2	-0.3	-0.2	0.0	-0.2	0.0	0.1	-0.6	0.7	-0.2
General government	-0.2	-0.5	-1.0	-1.7	-1.7	-1.6	-1.6	-1.5	-1.0	-1.0	-3.1	-5.9	-4.0
Exports	0.3	0.5	0.2	-0.8	-0.8	-1.7	-1.7	-0.1	-0.5	-0.5	1.1	-3.3	-2.2
Contributions (in point)	0.3	3.1	-0.8	0.9	0.6	0.2	1.0	2.5	0.8	1.2	2.4	2.9	4.1
Domestic demand excluding change in inventories *	0.1	0.4	0.1	0.4	-0.2	0.1	0.2	0.1	0.4	0.2	0.5	0.4	0.8
Change in inventories *	-0.1	0.0	0.4	-0.3	0.3	-0.1	0.4	-0.2	0.0	0.0	-0.2	0.3	-0.1
Net foreign trade	0.0	0.3	-0.5	0.2	-0.1	-0.2	-0.2	0.2	0.0	0.1	0.1	-0.3	0.1
France - situation of households													
Total employment	-20	-28	23	78	0	27	-41	25	1	19	52	11	
Non-agricultural market sector employment	-32	-49	3	12	-19	6	-60	-1	-18	5	-66	-74	
Unemployment rate Metropolitan France **	9.9	10.0	9.9	9.6	9.7	9.7	9.9	10.0	10.1	10.2	9.6	10.0	
Unemployment rate France **	10.3	10.4	10.3	10.1	10.1	10.1	10.3	10.4	10.5	10.6	10.1	10.4	
Consumer price index ***	1.0	0.9	0.9	0.7	0.6	0.5	0.3	0.1	0.0	-0.1	0.9	0.5	
Core inflation ***	0.6	0.4	0.6	0.5	0.4	0.1	0.0	-0.1	0.2	0.1	0.6	0.2	
Household purchasing power	1.2	0.3	-0.2	-0.3	0.7	0.5	0.6	-0.2	1.0	0.1	0.0	1.1	1.4

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

GDP: Gross Domestic Product

GFCF: Gross Fixed Capital Formation

NFE: Non-financial enterprise

NPISH: Non-profit Institutions Serving Households

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