

« The French Economy - 2015 Edition »

Summary Press Kit

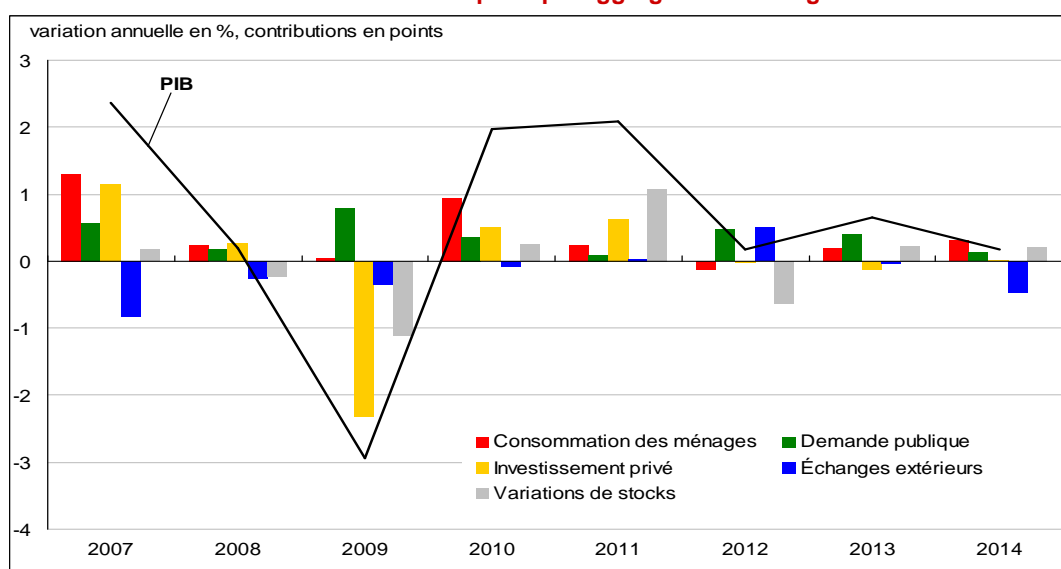
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General outlook – Growth faltered in 2014

Growth is still being held back by the sluggishness of domestic demand and export performances

After picking up pace in 2013 (+0.7% after +0.3% in 2012), the rate of growth of the French economy did not exceed +0.2% in 2014, in spite of various favourable factors including a very low inflation and the depreciation of the Euro. **Household purchasing power nonetheless increased (+0.8%)** for the first time since 2011, stimulated by a relatively sustained increase in nominal wages, the moderate increase of taxes and social security contributions after several years of steep hikes, and the sharp slowdown in prices. **And yet household consumption expenditure saw only a slight increase (+0.6% in volume after +0.4% in 2013), even though the decline in automobile sales has finally been reversed.** Nevertheless, the other components of demand remain unpromising: exports are picking up pace (+2.4% in volume, up from +1.7%), but are still growing more slowly than global demand for French products. **In volume, imports have bounced back strongly (+3.8% after +1.7%), growing much more rapidly than domestic demand.** For the first time since 2007, the contribution of foreign trade to GDP growth is now clearly negative (-0.5 points). Finally, the downturn in investment was accentuated in 2014 (-1.2% in volume after -0.6% in 2013).

Contribution of the principal aggregates to GDP growth



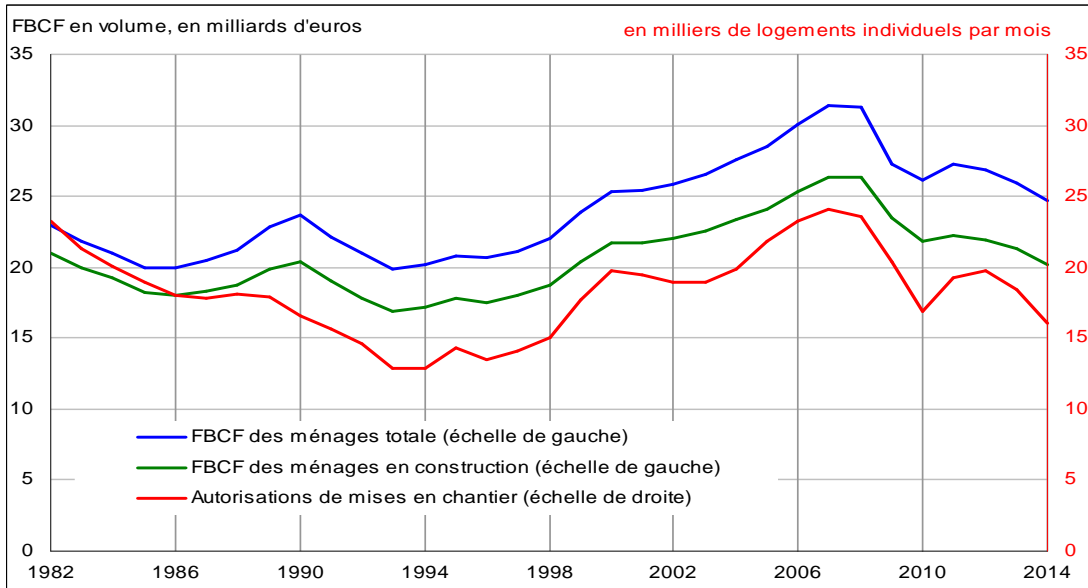
Source : Insee, National Accounts, 2010 base.

Construction still struggling

The overall contraction of investment in 2014 conceals substantial variations from one sector to the next: investment excluding construction, primarily the preserve of non-financial corporations (NFCs), grew by 0.8% in volume terms after a poor 2013 (-0.6%). The rate of investment by NFCs also increased by 0.3 points to reach 23.1%. On the other hand, **investment in construction continued to fall (-3.4% in 2014)** and the value added of the construction sector shrank by 4.0% in volume.

Housing and civil engineering projects were hit particularly hard. Civil engineering suffered from the sharp decline in investment by local government (-9.6% in value terms) after a good year in 2013 (+5.2%). Local investment usually slows down after the municipal elections, but the drop-off seen in 2014 was the biggest on record, reflecting the impact of budgetary constraints. The housing sector, meanwhile, was hindered by the fall in the number of building permits issued, which has been on the slide since mid-2013. Household investment in property thus declined more rapidly in 2014 (-5.9% in volume after a fall of -3.1% in 2013): this investment has now returned to the levels recorded in the late 1990s, well below the peak of 2007-2008. In early 2015, the composite indicator for the business climate in the building sector remained at a very low level.

Household investment in property



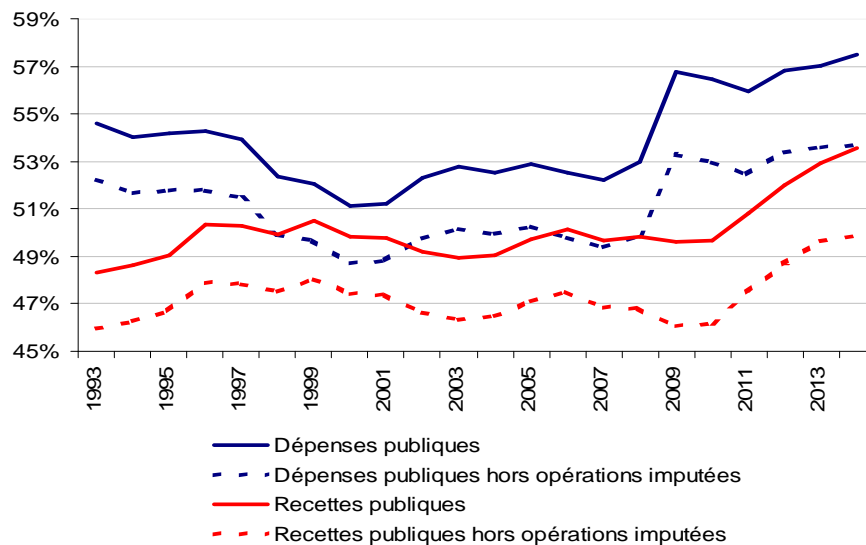
Sources : Insee, Comptes nationaux, base 2010 ; SoeS.

The increase in public spending as a proportion of GDP can be attributed to the introduction of the CICE tax credit

The public deficit shrank slightly in 2014 (4.0% of GDP, after 4.1% in 2013): public spending and revenue both grew proportionally to GDP (0.5 points and 0.6 points respectively). Tax credits are considered as expenditure in the national accounts, although as a general rule they take the form of a reduction in the sums demanded of taxpayers. The introduction of the tax credit for encouraging competitiveness and jobs (CICE) thus increased public spending as a proportion of GDP by 0.4 points, accounting for the majority of the increase recorded for this indicator in 2014. **If we exclude imputed operations (and particularly the impact of processing tax credits), public spending remained virtually stable as a proportion of GDP.**

France's public spending as a proportion of GDP remains particularly high when compared with other European nations of similar size: in 2013 it was almost 11 points higher than the average calculated for Germany, Spain, Italy and the United Kingdom. **Closer analysis of the breakdown of this spending reveals that two-thirds of the disparity observed can be attributed to expenditure on healthcare and social protection, with much less substantial differences in other areas of public spending.**

Variation in public spending and revenue



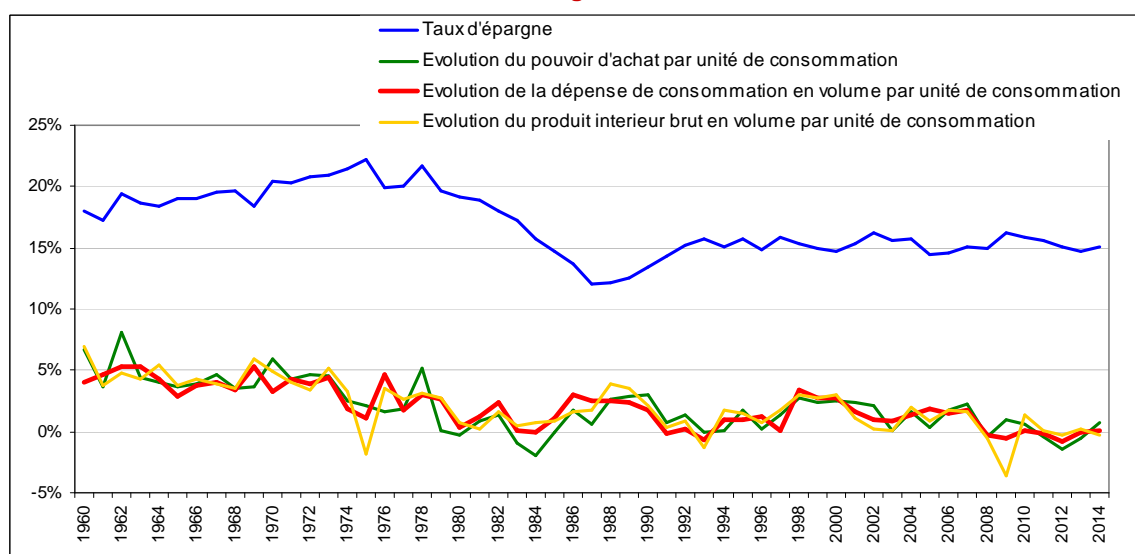
Source : Insee, Comptes nationaux, base 2010.

Dossier 2

Since the crisis of 2008, households have cut down on those goods and services purchases which are easiest to postpone or do without

The economic crisis of 2008 has had long-lasting consequences for consumption expenditure: purchasing power slowed, despite the very slight increase in effective consumer prices. This hindered the progress of consumption expenditure, which actually shrank in 2012. The sharp slowdown in consumption was spread unevenly across different categories of consumption, with households reducing their spending on those goods and services purchases which are easiest to postpone or do without.

Variation in volume of GDP, consumption expenditure and consumption per consumption unit, and the savings ratio



Source: INSEE, national accounts, 2010 base.

Spending on housing and food little affected by the crisis

Spending on immediate priorities (food and housing) is difficult to moderate in the short term, and such spending has slowed down only slightly if at all since the onset of the crisis.

Housing, which remains the largest item of household expenditure, has remained dynamic in value. Although spending on rentals in volume tends to be immune to short-term shocks, and energy spending is generally stable, the evolution of these items in value is determined by increases in rental and energy prices. Indeed, the increase in the price of rentals has been more substantial than the increase in the consumption deflator. This trend can be explained by the tensions observed on the housing market, partly as a result of the downturn in property transactions. As for energy prices, with the exception of a pronounced fall in 2009 and another decline from mid-2014 onwards, they have continued to grow at a keen pace as a result of the increase in gas and home heating oil prices, as well as electricity prices, which have remained highly dynamic since 2011. As such, **the cost of housing as a proportion of actual household consumption has risen further over the past few years** (an average of +0.13 points per annum between 2007 and 2014, compared with an annual average of +0.14 points between 1960 and 2007).

Similarly, **spending on food** has suffered little from the slowdown in purchasing power. Structurally settled into a regular, very moderate pace of growth, household spending on food consumed at home increased by an average of 0.4% per annum in volume between 2007 and 2014, down slightly from the annual rate of +0.6% recorded between 2000 and 2007. As growth in food prices has been noticeably more dynamic than the development of consumer prices in general, the importance of food spending as a proportion of total consumption increased between 2008 and 2013. This increase represents an inversion of the downward trend which had been prevalent since the early 1960s. Nonetheless, this proportion declined once more in 2014.

Other forms of expenditure are suffering the effects of the crisis, particularly spending on transport, clothing, communications, culture and leisure activities

The adjustment of consumption habits in response to the pronounced slowdown in incomes has thus been most keenly felt by those forms of expenditure which do not represent immediate priorities, and can thus be postponed or cut out. Purchases of durable goods (cars, furniture), semi-durable goods

(clothes, textiles) and certain services (hotels, restaurants, publishing) have thus clearly suffered from the slowdown in incomes, with sales falling or slowing dramatically.

Household spending on transportation has thus decreased in volume since 2008 (falling by an average of 1.3% per annum), hit by the contraction of vehicle sales (-2.7% p.a.) and usage expenditure (-1.6%). Easily postponed, particularly vehicle purchases, this expenditure has also been hit by the rising prices of both fuel and maintenance and repair services. The implementation of the environmental bonus-malus scheme in January 2008, followed by the introduction of a scrappage bonus scheme between December 2008 and December 2011, provided only a passing boost to the automobile market. Transport services continue to grow in volume (+1.5% p.a.), but at a slower pace than that seen in the pre-crisis years.

Easy to postpone in the short term, **household consumption of clothing and footwear** has been falling since 2008 (-1.0% per annum in volume), despite bouncing back in 2014. The introduction of flexible sales periods in 2008 and the arrival of new technological innovations have not been sufficient to turn around this decline in consumption. Consumption has also been penalised by price rises which have been more significant since the onset of the crisis.

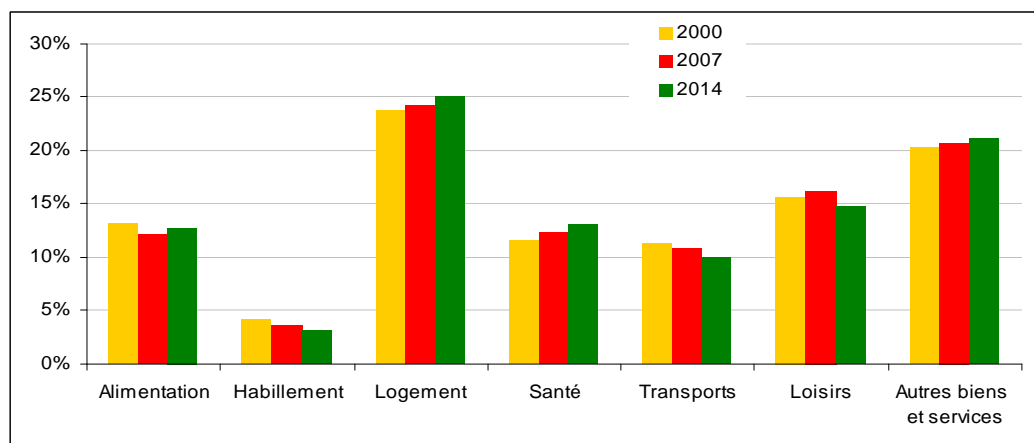
Since 2008, **household consumption of communication services, leisure activities and culture** has grown by 1.2% per annum in volume terms, after growing at an annual rate of over 5.0% during the 2000s. With prices falling, such expenditure accounted for 14.7% of total household expenditure in 2014, the lowest proportion since 1998. These developments primarily reflect the fate of technological goods and services which, in addition to the effects of the crisis, have suffered from a high rate of technological saturation in French households. Technological innovation and a sharp reduction in prices have not succeeded in restoring the dynamism of overall consumption in this sector. Nonetheless, mobile telephones and communications services continue to prop up spending on technological goods and services. On the other hand, the publishing sector has contracted sharply, largely as a result of the dissemination of information via free publications and online. Other forms of spending classified as leisure and culture expenditure (hotels, cafés, restaurants, holidays, gambling etc.) have remained stable or decreased.

Consumption of health and social services has been underpinned by substantial public spending

Expenditure borne largely by the public sector (healthcare and social services) is a different matter. Such expenditure is not directly affected by the slowdown in the purchasing power of income. But, faced with the slowdown in resources available to fund it, the public authorities take measures to restrict the growth of spending in these areas. **In terms of healthcare**, these measures have largely succeeded in stabilising prices, which were still growing by +1.7% per annum in the early 2000s. As such the actual consumption of healthcare products and services, three-quarters of which are borne by general government, has slowed in value, but continues to grow significantly in volume, at the same pace observed between 1994 and 2007 (+2.8% p.a after +2.9%).

Actual consumption of **social services** (crèches, childcare assistants, retirement homes, home help etc.) grew more slowly in volume between 2007 and 2014 than it had done in the early 2000s, but this rate of growth remains higher than that observed for actual consumption as a whole (+1.8% p.a. compared with an overall average of +0.8%). The prices of social services continue to rise steadily, although dropping from an annual increase of 3.2% between 2000 and 2007 to 2.4% in more recent years.

Categories of expenditure as a proportion of effective household consumption in 2000, 2007 and 2014



Source: INSEE, national accounts, 2010 base

Dossier 3 - GDP and well-being in Europe over the past twenty years

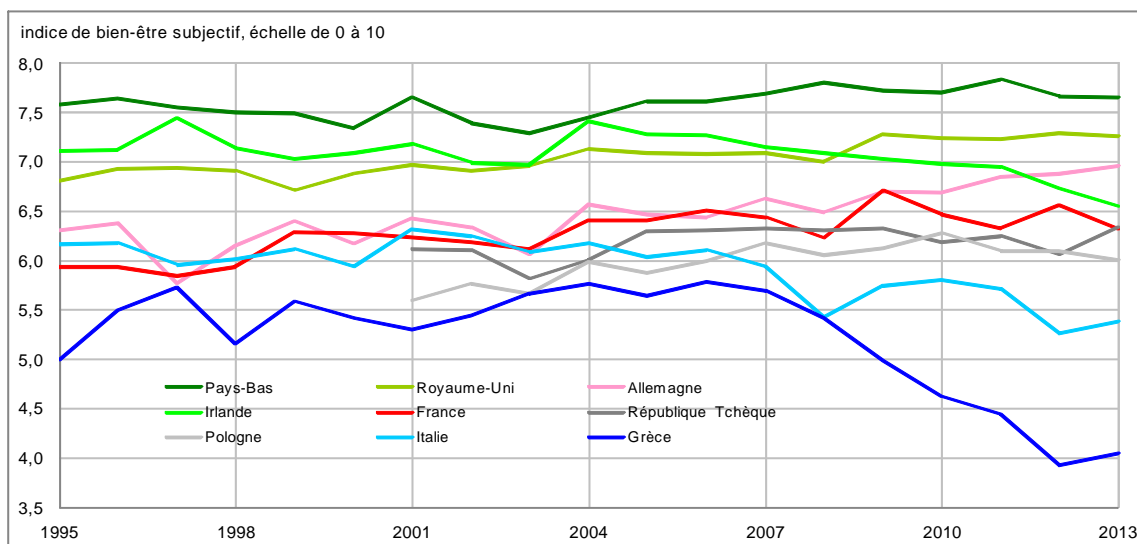
Between 1995 and 2007, GDP per capita grew by an average of around one third in Europe. Since the onset of the crisis, Europe's national economies have followed highly divergent trajectories. By 2013 a majority of European nations had returned to levels of GDP per capita similar to those recorded in 2007, but several Southern European economies had suffered a significant contraction. Germany, meanwhile, was one of the few economies to have exceeded its 2007 level. Nevertheless, the development of a nation's economic income does not necessarily reflect the well-being of households, as the Stiglitz-Sen-Fitoussi report makes clear.

Subjective well-being: three groups of countries

There are several ways of measuring people's well-being. One such method is the subjective well-being indicator, measuring how people actually feel by questioning them on their level of life satisfaction.

Between 1995 and 2007, subjective well-being increased less rapidly than GDP per capita. In most countries it stagnated or, at best, grew slightly. This phenomenon is known as the 'Easterlin paradox'. **Since the crisis, subjective well-being has declined or, at best, stagnated.** **Three distinct groups of countries emerge:** Southern European nations (Greece, Italy, Portugal, Spain) where well-being has declined significantly; Eastern European nations (Poland, the Czech Republic and Slovakia) where well-being has seen a more moderate decrease; and finally the other European nations, including France (this group is also referred to as 'North-Western Europe') where well-being has remained generally stable.

Life satisfaction since 1995



Source: Veenhoven, R., *World Database of Happiness*, Erasmus University Rotterdam.
Key: the average degree of satisfaction in France in 2013 was 6.3/10.

Nonetheless, **these measurements of subjective well-being** have their limits: they depend upon the psychology of the respondents (phenomena of social comparison and adaptation), the scales used are bounded (unlike other measurements such as household consumption, for example) and different survey sometimes yield very different results.

Measuring individual utility

In addition to our assessments of GDP and subjective well-being, we can also turn to economic theory to enrich our consumption measurements and obtain something approaching a measurement of the economic utility of individuals. This is the approach adopted in this *dossier*, used to construct a measurement of utility which takes into account the appreciation of leisure time and the effect of household size on the pooling of collective consumption costs. Certain forms of expenditure do not increase proportionally with the size of the household. However the trend has been for a decrease in the number of people per household in the majority of countries, which serves to bolster fixed costs and has a negative impact on the purchasing power of individuals.

A comparison of the two periods 1995-2007 and 2007-2012 allows us to demonstrate that the development of utility is dependent upon structural factors (household size, leisure time) as well as one factor which is sensitive to the impact of the crisis (per capita consumption).

Median annual average growth rate (evolution by sub period)

	Parameter in the utility calculation	1995-2007	2007-2012	Variation between the 2 periods
Actual per-capita consumption	0.45	2,3	-0.1	-2,4
Household size	0.225	-0.4	-0.3	0.1
Leisure	0.55	0.2	0.2	0.0
Utility	///	1.0	0.0	-1.0
GDP per capita	///	2,4	-0.6	-3,0

Source: OECD and the authors.

In the period of growth which stretched from 1995 to 2007, the median growth rate of utility was 1.0% per annum, half of the median growth rate of GDP (2.4% p.a.).

On the one hand actual consumption is growing at the same pace as GDP, which is conducive to an increase in utility. But on the other hand, the growth of consumption contributes just 45% to the development of utility. Utility is thus 55% dependent upon leisure time. Furthermore, the downward trend observed in household size is holding back utility by limiting the economies of scale possible within households.

Since the onset of the crisis, utility has stagnated while GDP per capita has dropped off more noticeably (-0.6%). This trend is indicative of the less cyclical nature of household consumption (-0.1%). The rise in independent living arrangements is thus contributing to the decrease in utility. On the other hand, the continued increase in leisure time (+0.2%) is making a positive contribution to utility.

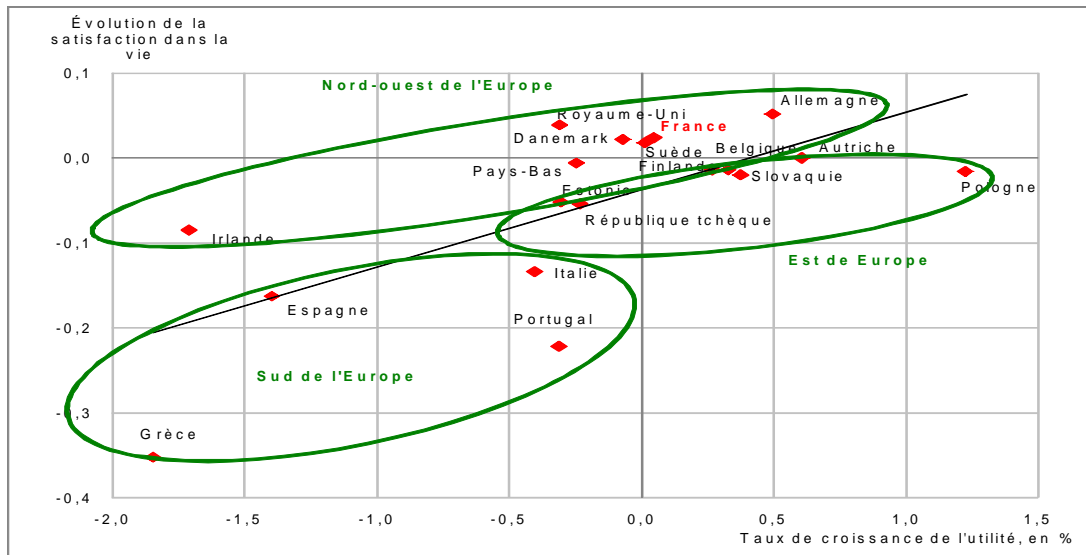
In all, over both periods, the progress of leisure time and household size has been reasonably steady. Leisure time grew by 0.2% per annum throughout both periods, with the average household size shrinking by 0.4% per annum in the first period and 0.3% p.a. in the second. **These two variables combine to make utility less sensitive than GDP to the fluctuations of the economic cycle.**

GDP, utility and life satisfaction before and after the crisis

Between 1995 and 2007, if we replace GDP per capita by utility, the correlation with subjective well-being becomes clearly positive, but remains weak. **Taking into account actual consumption, household size and leisure time allows us to more accurately represent the development of subjective well-being.**

Since the 2008 crisis a clearer relationship has emerged between subjective well-being and utility. Nevertheless, this general trend conceals a variety of different circumstances. In those Southern European nations which saw the most dramatic drop in utility, satisfaction has clearly decreased. This decrease is much more substantial than would be expected in light of the relation observed across all European countries (the Southern European nations are thus below the regression line). In Eastern Europe, median utility grew by 0.4% per annum while satisfaction actually decreased by around 0.02 points. As with the previous group of countries, the progress of satisfaction is less positive than utility would lead us to expect. Finally, in the other European nations ('North-Western Europe'), the increase in satisfaction is greater than the development of utility would lead us to expect.

Utility and satisfaction with life, variation between 2007 and 2012



Source: OECD, Veenhoven, R., *World Database of Happiness*, Erasmus University Rotterdam, auteurs