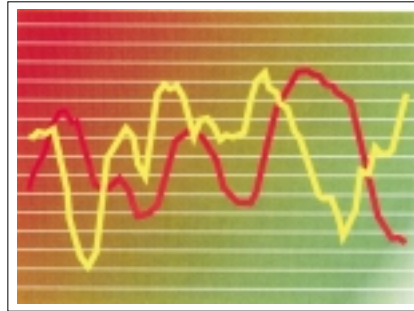


CONJONCTURE IN FRANCE



An autumnal slowdown

The annualised growth rate of around 1.5% posted by the French economy in the first half of the year is well down on the annual rates of between 3% and 4% that had prevailed in the three preceding years. The number of dependent jobs created in the private sector fell by a half in Q2 and the decline in unemployment was halted. This marked change in tendency is linked to the rapid adjustment of corporate demand to the worsening of the international climate and the contraction in world trade, through de-stocking and cuts in investment programmes. On the other hand, household consumption has continued to rise at a rate of close to 3%.

The whole of the euro zone has followed a similar pattern. Japan has fallen into recession. The United States economy has continued to grow very slowly, with household demand increasingly hard put to make up for the weakening of investment. At the end of Q3, the whole of the world economy was suffering virtual stagnation, and this seemed set to continue until the end of the year. The dramatic events of 11 September have added an acute downside risk, quite apart

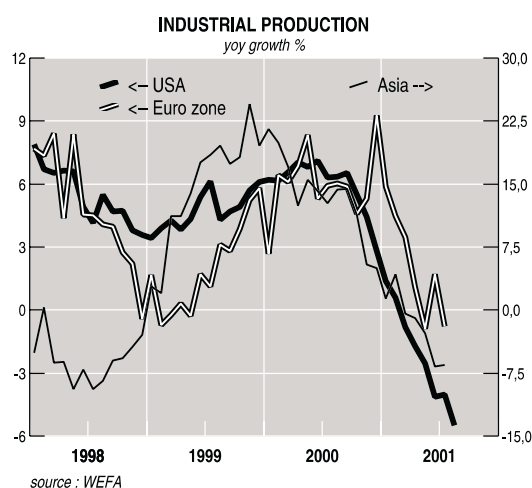
from the immediate weakening effect on certain sectors. This additional risk consists mainly of a possible reduction in United States household consumption, triggering an additional adjustment for the whole of the world economy.

In France, the rise in purchasing power in H2 will make it possible for consumption to continue to grow. On the other hand, the slowdown in investment is intensifying. Assuming that the above-mentioned risk fails to materialise—and, given the difficulty of assessing this, it is not taken into account in the figures shown below—modest growth, comparable to that seen in H1, is highly probable for H2. This would give an annual growth rate of 2.1% for 2001. In these circumstances, the rise in dependent employment in the private sector (240,000 in 2001) would mean a virtually unchanged unemployment rate for the year as a whole. Even allowing for a slight rise in underlying inflation, the year-on-year price increase should remain moderate (1.8% in December), and this, in combination with the fall in interest rates, should leave the door open for a subsequent upturn in activity.

The downturn in American activity has now spread to the whole of the world economy

The severe downturn in the American economy, which has now lasted for more than a year, was triggered off by an overinvestment crisis, combined with a marked deterioration in corporate accounts. The bursting of the NASDAQ bubble in March 2000, signalling a sharp downward revision in the profit expectations founded on the surge in the new technologies, coincided with a downturn in productive investment, which, after rising by 8 to 10% a year for almost eight years, has been in free fall since the summer of 2000. The recession in the high-tech sector rapidly spread to the whole of American industry, helped by substantial de-stocking in H1 2001. Even before the dramatic events of 11 September, unease was spreading to household demand, which, despite slowing down, had previously been helping to underpin activity. American firms, however, have started to adjust their demand for labour, so that the decline in dependent employment in the private sector is now holding back the growth of the total wage bill. Faced with a simultaneous rapid rise in unemployment and negative wealth effects due to the falls on the stock markets, there was already a substantial risk that American consumers might show greater prudence and save part of the tax cuts introduced by the Bush administration. In these circumstances, there was little chance of the American economy getting out of the rut by the end of the year.

The downturn in activity in the United States in mid-2000 dealt a severe blow to the world economy. First in line were America's principal trading part-



Note:
For Asia, average of Malaysia, Thailand, Taiwan and Corea.

ners (Canada, Mexico), as well as countries specialising in high-tech products (Southeast Asia, Japan). However, contagion spreading through the channels of world trade gradually affected all the economic zones.

Euro-zone growth still weak

The euro zone has not come off unscathed. The run-down in external demand starting at the beginning of 2001 came at a time when activity in the zone had already started to weaken. Consumption by European households had levelled off in H2 2000 under the impact of the higher oil price. The tax cuts introduced

FRANCE : GROSS DOMESTIC PRODUCT (volume) BY TYPE OF EXPENDITURE

(at 1995 prices seasonally and working-day adjusted data, % change from previous period)

		1999				2000				2001				1999	2000	2001
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
GDP	(100%)	0.9	0.8	0.9	1.1	0.7	0.7	0.8	0.8	0.4	0.3	0.3	0.3	3.0	3.4	2.1
Imports	(27%)	0.1	2.0	2.0	3.1	5.0	4.2	3.8	2.1	-1.7	-1.3	0.0	0.5	4.2	15.2	1.8
(of which merchandises)	(24%)	0.4	2.1	2.4	3.7	5.3	4.4	4.1	2.2	-1.9	-1.5	-0.3	0.3	5.2	16.7	1.5
Consumption	(54%)	0.4	0.9	1.2	0.9	0.5	0.4	0.8	0.2	1.2	0.3	0.8	0.5	3.1	2.7	2.7
Public consumption	(24%)	1.0	0.4	0.5	0.8	0.4	0.7	0.6	0.6	0.3	0.4	0.7	0.6	2.1	2.4	2.1
Investment	(20%)	2.2	1.7	0.7	1.2	1.8	2.1	1.2	1.8	0.6	0.0	-0.1	0.1	6.2	6.2	3.1
of which:																
Non financial corporated and unincorporated enterprises	(11%)	2.4	1.6	0.9	1.1	1.6	2.5	2.2	2.5	0.3	0.4	-0.4	-0.1	5.9	7.1	4.0
Households	(5%)	2.8	2.7	0.0	0.9	2.4	1.3	-0.4	0.0	0.5	-1.1	0.0	0.4	7.6	4.6	-0.1
Exports	(29%)	1.1	2.4	3.6	1.0	4.3	4.7	2.2	2.9	-0.1	-1.9	0.0	-0.1	3.9	13.4	2.8
(of which merchandises)	(24%)	0.7	2.7	4.6	1.0	4.4	4.9	1.9	2.4	0.2	-2.7	-0.3	-0.3	4.0	14.0	1.7
Contributions to growth																
Internal demand excluding inventory changes		0.9	0.9	0.9	0.9	0.7	0.8	0.8	0.6	0.9	0.3	0.6	0.4	3.4	3.2	2.6
Inventory changes		-0.3	-0.3	-0.4	0.7	0.1	-0.3	0.3	0.0	-0.9	0.2	-0.3	0.0	-0.4	0.3	-0.8
Net foreign trade		0.3	0.1	0.5	-0.5	-0.1	0.2	-0.4	0.3	0.4	-0.2	0.0	-0.2	0.0	-0.1	0.3

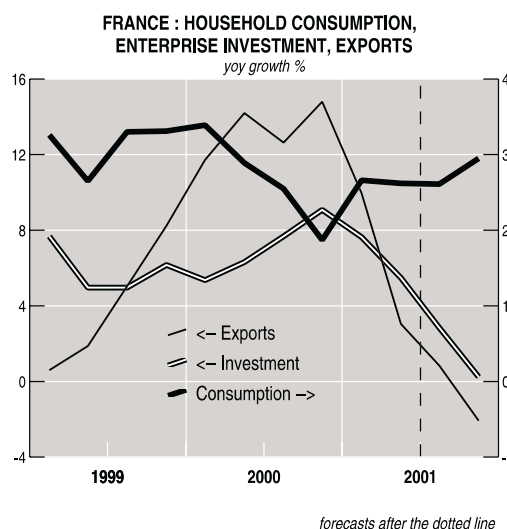
Forecasts

in the leading European countries gave room to hope that a re-acceleration in household demand would cushion the negative shock from outside the zone. However, this tendency was slightly slower in coming than had been expected⁽¹⁾, probably as a result of the further price increases that occurred early in the year. In these circumstances, European business confidence weakened and this had a major restraining influence on inventory and investment behaviour. The slowdown has been very sharp, with the euro zone close to stagnation in Q2. Looking ahead to the end of the year, even if the deterioration on European labour markets induces a slowdown in the total wage bill, the current consolidation of consumption should be strengthened by the marked decline in inflation in the zone, from a peak of 3.4% last May to 2.3% in Q4. All in all, activity in the euro zone seems set to remain weak, with growth at an annual rate of close to 1% in H2.

Firms holding back

The French economy in 2001 has moved in line with its main European partners. The growth rate weakened in the early part of the year under the impact of the sharp external slowdown and the rapid adjustment on the part of firms to the new situation, reflected in their behaviour regarding stocks, investment and imports. This adjustment is all the more remarkable in that the upturn in consumption in H1 was faster and slightly more distinct than in the euro zone as a whole. Indeed, the acceleration in household income came somewhat earlier still, with the first wave of reductions in compulsory contributions taking place in Q4 2000. In addition, France enjoyed a more marked decline in inflation than the euro zone as a whole in Q1 2001. This apparent paradox suggests that demand behaviour on the part of French firms is now more dependent on the economic situation in Europe as a whole, and perhaps even in a broader area. At a time of economic slowdown, it is also possible that the steady decline since 1999 in French firms' profit ratios (excluding the energy sector) also played a part in leading to the freezing of certain investment projects.

In H2 2001, in view of the lasting deterioration in the international environment, French exports of manufactures are set to decline still further. As regards corporate behaviour, the watchword seems likely to continue to be "wait and see". Views regarding order books worsened distinctly in September in the capital goods branch and the large industrial firms were reporting at the end of July a very marked deterioration in their investment outlook. Having stagnated in H1 2001, productive investment is thought to have declined in H2. This decline is being accompanied by a similar fall in construction investment. Private



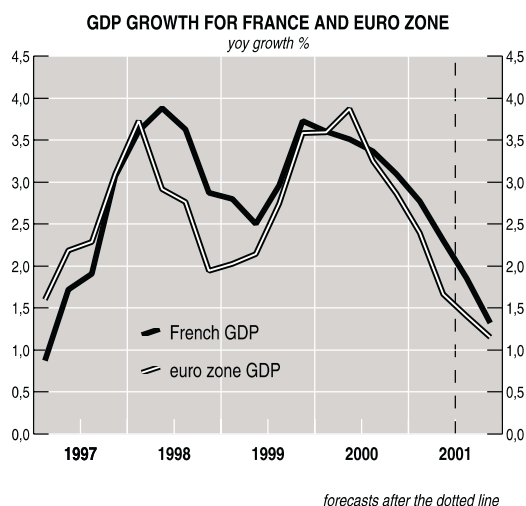
housing investment seems to have stabilised at a high level, while public works activity is slowing down, after a particularly brisk period.

French firms have also begun to reduce their demand for labour. Because of the lags inherent in the productivity cycle, job creation admittedly remained high in Q1 2001, but Q2 saw a distinct slowdown and this is likely to intensify, with the six-monthly change in private dependent employment, which was still as high as 1.3% in H1, apparently no more than 0.3% in H2. This would mean a total of 280,000 jobs created in the year as a whole, compared with last year's record figure of 600,000. The decline in unemployment came to a halt in Q2 and the unemployment rate is likely to be around 9% at the end of the year.

Household consumption continuing to prop up activity

Meanwhile, wages seem to have maintained their modest acceleration. The year-on-year change in the average wage per head is likely to be around 3% at the end of the year. This means that wages are adjusting after a certain delay to earlier-occurring declines in unemployment and price rises. All things considered, the total wage bill seems set to slow down substantially during the year under the impact of reduced job creation. Even so, the momentum built up in the period to Q1 2001 means that the annual average increase would again be strong.

(1) Admittedly, the latest national accounts for the euro zone show a marked upturn in household consumption in the early part of the year (a rise of 0.8% in Q1 2001). However, 0.3 of a point of this stems from revisions in the German national accounts, with the estimation of growth in German consumption in Q1 2001 raised from +0.1% to +1.0%. However, this upward revision in the Q1 growth rate was due above all to a downward revision in the level of consumption in 2000 and it would therefore appear that the acceleration in German consumption dates rather from Q2 2001.



On top of this rise in the wage bill there have also been, as of last autumn, falls in compulsory contributions (declines in the rates for the lowest two income-tax tranches, cuts in local taxes, abolition of car licence fees) and these enabled household income to accelerate. The further tax cuts seen following the summer break (declines in all income-tax tranches, the special “employment premium”) are underpinning the momentum acquired by income by the end of last year.

Having eased earlier in the year thanks to the decline in oil prices, French inflation moved up again in Q2, under the impact of a marked acceleration in food prices due to the strength of meat prices as the result of sanitary problems (BSE, foot-and-mouth disease) combined with a surge in the price of fresh produce in Q2 and early Q3. This latter shock, the consequence of the impact on the crops of bad weather in April, began to fade out in August. Movements in food prices and in energy prices (assuming a stabilisation of the oil price at around USD 25/barrel and of the EUR/USD exchange rate at around 0.90) should now help to reduce inflation (to 1.8% in December). At the same time, underlying inflation is expected to continue its slow growth and reach 2%. It would thus complete the incorporation of the past rise in the oil price and fall in the euro and also react to the slight acceleration in wages. The prospect of the move to a 35-hour working week for small firms, as well as the introduction of the euro, could also be the occasion for marginal adjustments in the prices of certain

goods and services. Even so, the rise in underlying inflation should come to an end, given the weaker economic situation.

With incomes rising strongly and low average inflation over the year, household purchasing power can be expected to rise sharply in 2001, by 3.8%. In these circumstances, in both halves of the year it is household consumption that will have been the mainstay for growth, rising at a rate of close to 3%. This rise in expenditure has been accompanied by an increase of the order of 3/4 of a point in the saving ratio between 2000 and 2001, mainly as the result of the usual economic determinants, smoothing out the strong increase in incomes. However, at a time of deterioration on the labour market, some renewed precautionary saving behaviour cannot be ruled out.

The events of 11 September have introduced additional uncertainties into an already weakening tendency

All things considered, following three years of growth of better than 3%, French GDP is expected to rise by 2.1% in 2001. The economy will probably continue to post the slower growth rate seen in H1. In an international climate that remains weak, firms are likely to adopt a “wait-and-see” attitude. Household consumption would then provide the minimum platform for growth.

The new climate created by the terrorist outrages in the United States on 11 September clearly introduce major uncertainties into the scenario described here. In the short term, the most important of these clearly lies in the behaviour of American households, with these dramatic events liable to impair the capacity of consumption to hold up for long. A similar risk cannot be totally ruled out in the euro zone, although this seems less likely. Above all, however, an additional blow to the American economy could intensify the restrained attitude adopted by European firms. On the other hand, the rapid and clear-cut reaction already seen from the monetary authorities and the relaxation of fiscal discipline, notably in the United States, mean that there is still the possibility of an up-turn next year. ■