

Economic outlook

7 September 2022



The backdrop to global economic activity is still very much affected by a combination of several exogenous shocks (health, geopolitics, climate) which are causing persistent tensions for production conditions and helping to fuel inflation.

In France, government policies to limit energy prices should help maintain the change in consumer prices year-on-year at around 6% in September-October. However, this level could reach around 6.5% in December, mainly due to the continuing rise in food prices.

The business tendency surveys suggest that French activity has remained relatively resistant this summer, in services in particular. Growth is therefore expected to be slightly positive (+0.2% forecast) in Q3. There is more uncertainty surrounding the end of the year and activity could come to a standstill (0.0% forecast), against a background of monetary tightening and concern over energy supply chains. Annual growth is therefore expected to stand at 2.6% for 2022, but the growth overhang for 2023 is likely to be modest.

Tensions over production persist, in line with an unprecedented accumulation of exogenous shocks

The international economic environment is still affected by the cumulative weight of exogenous shocks, which are likely to hamper activity and fuel inflation. The Covid-19 epidemic continues and, as a result, there are still lockdowns in parts of China. The war in Ukraine has sparked a major geopolitical crisis between Russia and Europe and is now raising fears of an energy crisis. Finally, this summer's drought notably affected some agricultural production and limited navigability on the river Rhine, Europe's most important trade artery.

All in all, supply difficulties would seem to be significant over the long term in most major sector of activity (► **Figures 1 and 2**). Since mid-2021, they have far outstripped demand difficulties. In July 2022, more than one in two industrial companies, and more than one in three in services, reported in the business tendency

surveys that they were facing supply difficulties only (but no demand difficulties). These are unprecedented levels since the series began (apart from the very particular situation in services during the first lockdown).

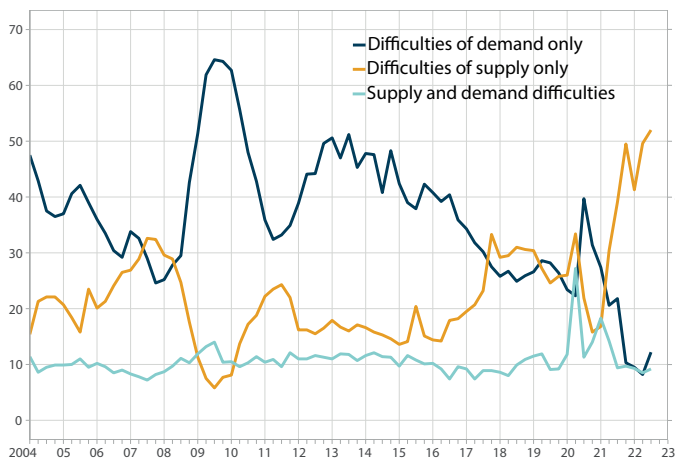
These supply difficulties can take several different forms: supply chain problems, lack of equipment, but also sometimes a lack of staff. Hiring difficulties have also reached unprecedented levels, in a recent context of momentum in payroll employment. Such tensions in the labour market are not just affecting France, they are felt even more strongly in the United Kingdom, for example, in the context of Brexit.

Production prices continue to increase in industry, in agriculture they are easing a little while remaining very high, and they are starting to accelerate in services

The unprecedented accumulation of supply constraints, combined with the strong demand seen just after the

► 1. Supply and demand difficulties in the manufacturing industry

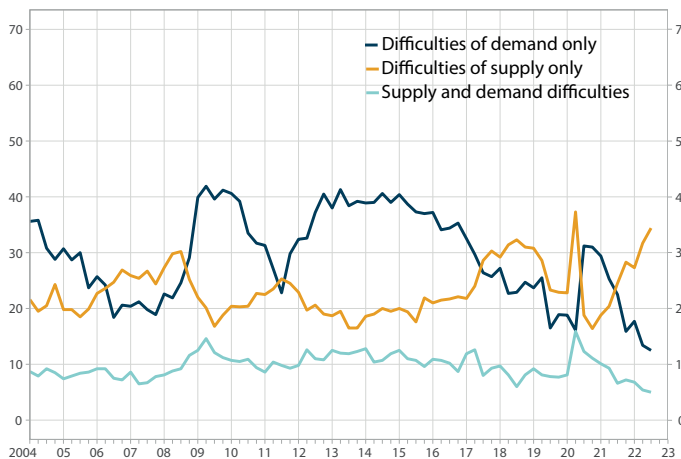
% of companies reporting such difficulties



Note: results are weighted by turnover.
Last point: July 2022.
Source: INSEE, quarterly business survey in industry

► 2. Supply and demand difficulties in services

% of companies reporting such difficulties



Note: results are weighted by turnover.
Last point: July 2022.
Source: INSEE, business survey in services

most acute phase of the health crisis, has led to soaring production prices in industry and agriculture (► **Figure 3**) and in construction too. Thus in two years, between July 2020 and July 2022, production prices increased by a little over 20% in industry (excluding energy), and just over 35% in agriculture. In the case of services, which are less directly exposed to the rise in world prices, the increase was less (around +7% between Q2 2020 and Q2 2022), with nevertheless some very sharp increases, in sea and coastal freight water transport, for example, where production prices more than doubled in two years.

The production prices of some agricultural products (cereals, oilseed) have eased markedly in recent months, however, with the unblocking of Ukrainian exports. They remain buoyant in industry, and they are beginning to accelerate in services, exceeding those of maritime transport. In most services, these prices depend above all on wage costs, where change is mainly linked to negotiations at branch and company level and to increases in the minimum wage.

Finally, regarding energy, oil prices have fallen back, affected by fears of recession, but still bolstered by concerns over energy supply chains due to geopolitical tensions, and recently these tensions have caused gas and electricity spot prices to soar on the European markets.

In the business tendency surveys there are still high expectations for change in selling prices in the next three months (► **Figure 4**). In industry, however, the corresponding balance of opinion has recently slowed after reaching its highest point last May.

Although substantially eased by price limitation measures, inflation looks set to remain high through to the end of the year

In August 2022, consumer prices in France increased overall (+0.4% compared to July) according to the provisional estimate. However, prices fell back slightly year-on-year (+5.8%, after +6.1% in July) for the first time since July 2021, due mainly to the fall in oil prices. Inflation in France thus remains high, but is among the lowest in the Eurozone.

Price changes over the coming months will depend on several factors: movements in international energy and commodity prices, the value of the euro on the foreign exchange market, the speed and degree of transmission of past increases in producer prices (including their wage component) to consumer prices, government price limitation policies, especially related to energy.

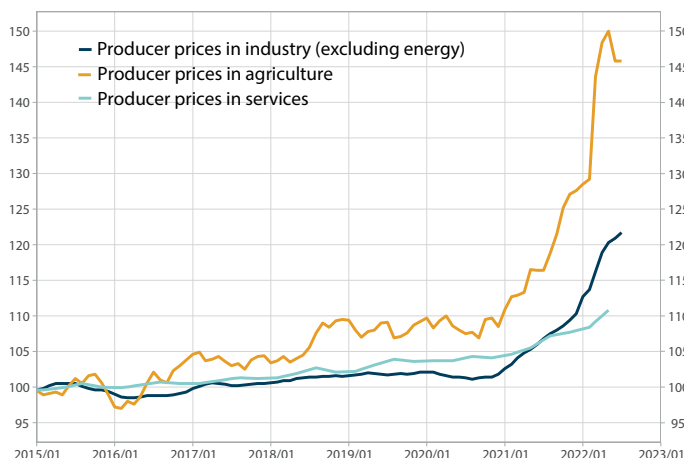
In this forecast, the price of Brent is assumed to be \$100 per barrel (i.e. also €100, assuming that parity is maintained between the euro and the dollar until the end of the year). The strengthening of the “reduction at the pump”, combined with the continuing tariff shield on gas and electricity prices, is expected to help bring down energy inflation in September-October. This reduction is then likely to be smaller in November-December and energy prices could then increase year-on-year at the very end of 2022, driven by a “base effect”, as oil prices fell at the end of 2021 with the emergence of the Omicron variant.

Inflation in services is unlikely to accelerate overall between now and the end of the year, due partly to the abolition of the television and radio licence fee which is likely to bring down prices under the heading “Television and radio licence fees and subscriptions” in the consumer price index.¹

¹ Note that in the national accounts, this cut is not counted in the household consumption deflator but in their disposable income.

► 3. Producer prices in industry (excluding energy), agriculture and services

base 100 in 2015

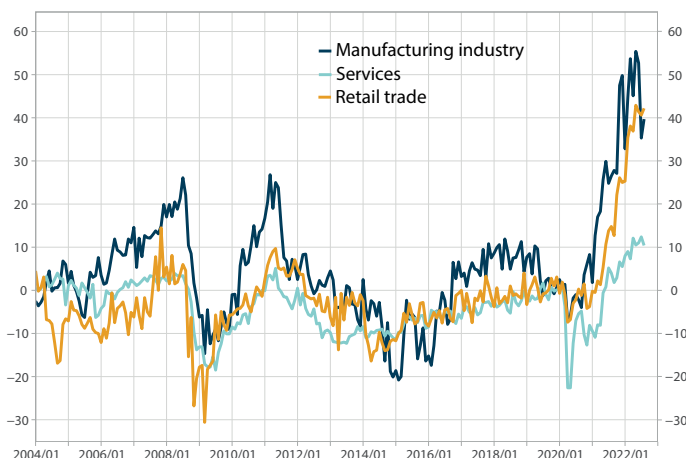


Note: monthly data in agriculture and industry (last point: July 2022), quarterly data in services (last point: Q2 2022). SA data in agriculture series but raw data in other sectors.

Source: INSEE

► 4. Balances of opinion on expected change in selling prices for the next 3 months

opinion balances, in points, SA



Last point: August 2022

Source: INSEE, business surveys

Finally, it is likely that the year-on-year shift in consumer prices will continue to increase for manufactured goods (around +5% year-on-year forecast for December 2022) and especially for food (around +12% forecast). Overall in our scenario, inflation is expected to stabilise at a little below 6% year-on-year in September-October, then rise to about 6.5% in December (► **Figures 5 and 6**). Core inflation, which does not take the most volatile prices into account, is expected to exceed 5% by the end of the year. Tariff shields and reductions at the pump should help to ease headline inflation directly by about 2.5 percentage points in September. However, this estimate is basically a lower bound of the overall impact of these measures, as the impact also includes the indirect effect coming through the productive system (see *Insee Analyses*, n°75, September 2022).

Signals relating to demand are mixed

The purchasing power of household gross disposable income (GDI) contracted substantially in the first half of the year: -1.6% in Q1 then -1.1% in Q2, respectively -1.8% and -1.2% per consumption unit (CU), notably due to the effect of the acceleration in prices. It is expected to bounce back in H2 however (at least +1.5% in Q3 then at least +0.5% in Q4), as a result of a sharp acceleration in nominal income in Q3. Over the whole of 2022, there is unlikely to be an increase in purchasing power compared to 2021 (about 0% forecast) and it is expected to decline by about 0.5% per CU.

In Q3, earned income is expected to benefit from the buoyancy of wages, notably from the latest increase in the minimum wage on 1st August, the increase in the civil service index point and the value sharing bonus (PPV),

► 5. Past and projected headline inflation

year-on-year change in % in consumer price index

	July 22	August 22	Sept. 22	Oct. 22	Nov. 22	Dec. 22	2021	2022
	year-on-year change						annual average	
Headline inflation	6.1	5.8	5.9	5.8	6.3	6.6	1.6	5.3

Provisional

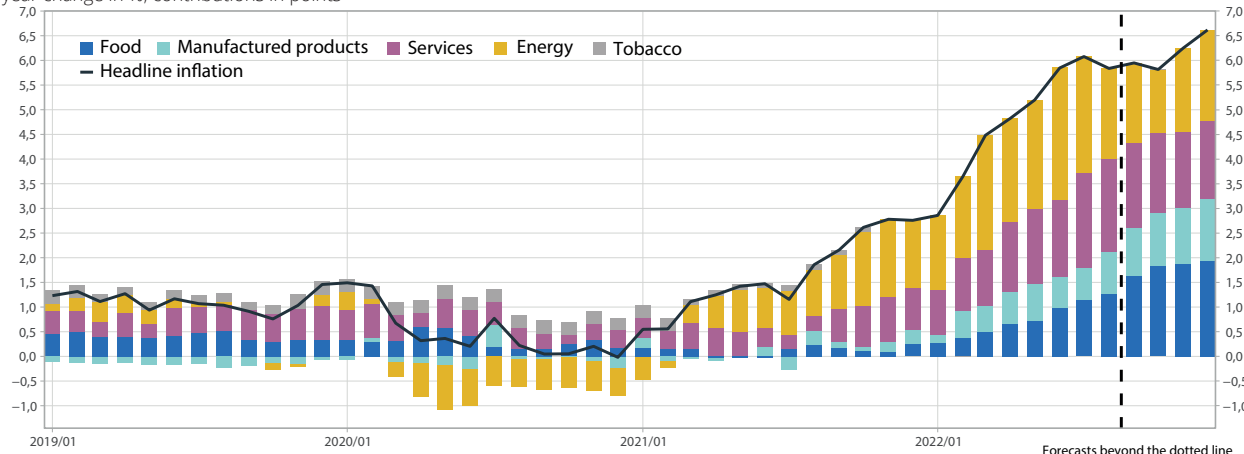
Forecast

How to read it: in August 2022, the consumer price index increase by 5.8%, according to the provisional estimate. It increased by 5.9% year-on-year in September.

Source: INSEE

► 6. Headline inflation and contributions by item

year-on-year change in %, contributions in points



How to read it: in August 2022, consumer prices rose by 5.8% year-on-year, according to the provisional estimate. They are expected to increase by 5.9% year-on-year in September 2022.

Source: INSEE

successor to the extraordinary purchasing power bonus. Incomes should also be boosted by the 4% increase in many social benefits on 1st July and the one-off back-to-school bonus. In Q4, household GDI is expected to benefit from a reduction in taxes and social contributions (abolition of the television and radio licence fee and the continuing reform of the housing tax for the households concerned).

In this context of significant variations in purchasing power from quarter to quarter, it is likely that changes in household consumption will reflect not only smoothing behaviours regarding purchasing decisions but also catch-up effects in those services most affected by the Covid-19 epidemic. In addition, household confidence remains weakened, despite an improvement in August after 7 consecutive months of decline.

Consumption thus recovered moderately in Q2 (+0.3%), after a very distinct downturn at the start of the year (-1.2%). Services drove the majority of this rebound, particularly accommodation-catering, while consumption of goods declined again, linked with the continuing rise in inflation. Consumption is expected to continue to increase in Q3 at the same pace as in the previous quarter but is likely to slow at the end of the year as the catch-up effects recede. The savings ratio is expected to rise sharply in H2 given the expected rebound in purchasing power.

More generally, demand signals appear mixed. For example, business managers in industry interviewed for the business tendency surveys, were less concerned about demand than about supply, but the balance of opinion on order book levels has tended to decline over that last two months. Finally, the darkening international environment could have repercussions for world demand for French products.

Economic activity in France is expected to continue its progress into Q3, but at a slower pace, before eventually coming to a standstill at year's end in an international environment over which dark clouds are gathering

Growth looks set to be slightly positive in Q3, but activity is expected to slow (+0.2% forecast, after +0.5% in Q2, ► **Figure 7**). It will probably continue to be driven mainly by catch-up effects in services, a phenomenon that was already noted in the spring (► **Figure 8**). Meanwhile, manufacturing output is expected to be in decline over the quarter, in a context of strong constraints over supply and high levels of finished goods inventory (except in agri-food) according to the different surveys.

The forecast for Q4 appears more uncertain, against a backdrop of monetary tightening, especially in the United States, and concerns over energy supply chains in Europe. The usual models based on business climates (► **Figure 9**) certainly suggest a return to slightly positive quarterly growth; however, the risk of an energy crisis has increased since companies' responses to the business tendency

surveys were collected during August. A contraction in GDP in the last quarter cannot be ruled out in the event of a worsening of energy supply chain difficulties in Europe.

Our main scenario is therefore one of activity at a standstill overall in the last quarter (0.0% forecast). This scenario can be interpreted both as the one most likely to come about, even without a major shock, given the friction likely to arise as a result of the latest developments, and as the midpoint between a relatively optimistic forecast based on the surveys and a significantly worse scenario that could include restrictive measures.

All in all in 2022, GDP growth as an annual average is expected to reach 2.6%. The growth overhang for 2023 (i.e. annual growth that year if quarterly GDP stayed at the level reached at the end of 2022, in each quarter) is likely to be relatively modest, at around +0.2%.

There are of course significant uncertainties that could affect this forecast, whether related to geopolitics, energy or even health (with the risk of an eighth wave of Covid-19), climate (with the consequences of the drought) or more directly to economics (with the consequences of the tightening of monetary policies). ●

► 7. Past and projected economic activity (GDP)

in %

	2021				2022				2021	2022	2023 ovhg
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
Gross domestic product	0.0	1.0	3.4	0.5	-0.2	0.5	0.2	0.0	6.8	2.6	0.2

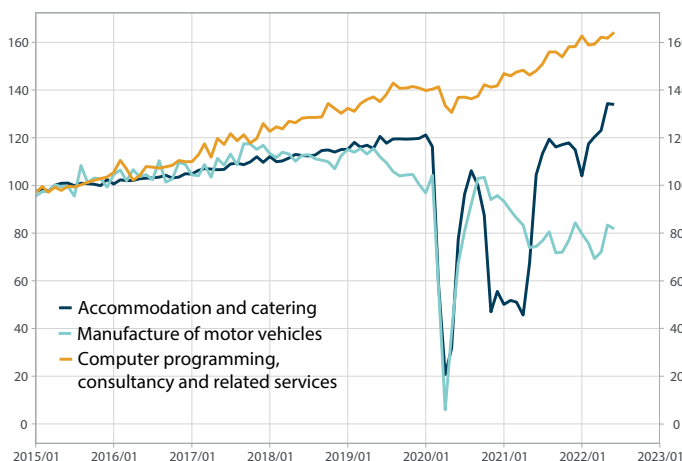
■ Forecast

How to read it: in Q2 2022, GDP increased by 0.5%. It is expected to rise by 0.2% in Q3 then remain stable in Q4 2022. Year-on-year growth is likely to be +2.6% in 2022, after +6.8% in 2021.

Source: INSEE

► 8. Monthly production indices in some service and industrial branches

CVS-CJO data, base 100 in 2015

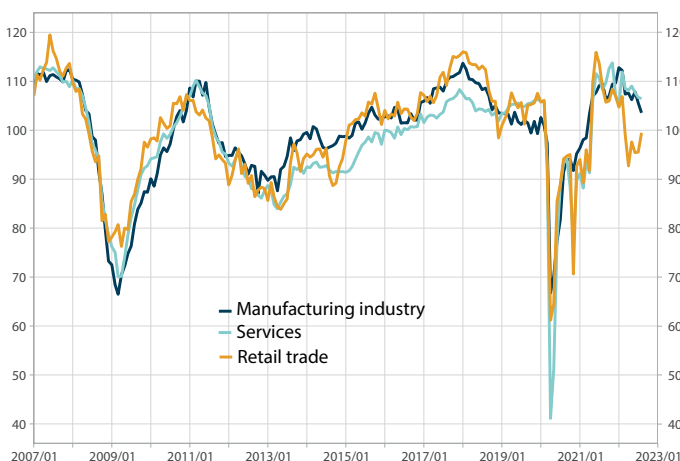


Last point: June 2022

Source: INSEE

► 9. Business climates

standardised indicator: average = 100 and standard deviation = 10



Last point: August 2022

Source: INSEE, business surveys

