

France

INSEE survey adds to sense of gloom in second quarter

- **INSEE survey signals business climate still running at lowest level since 2009, despite small rise in May**
- **Survey adds to PMI signal of Q2 downturn**
- **Economy hit by weak demand, lack of export competitiveness and downbeat consumers**

Business confidence remained firmly in the doldrums in May, according to INSEE. The survey data correspond with the flash PMI from Markit, which showed an ongoing marked deterioration in business conditions during the month.

Both surveys suggest the underlying health of the economy is worse than official data have indicated so far this year, representing a puzzle as to why official and survey data have diverged.

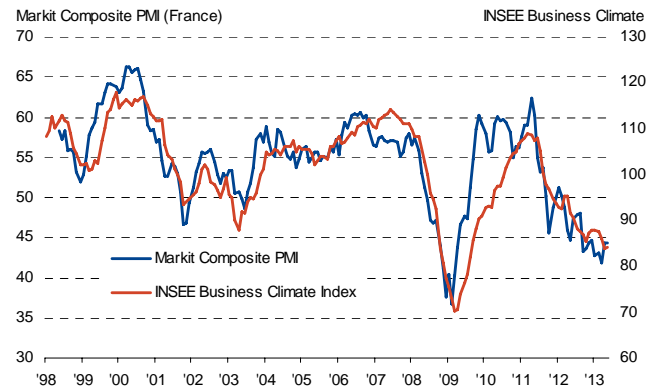
The INSEE survey's main Business Climate index rose only modestly to 84.2 in May, having slumped to 83.8 in April, its lowest since August 2009. The survey therefore suggests that the French economy is contracting at a steep rate in the second quarter. Historical comparisons suggest the average reading so far in the second quarter is consistent with GDP contracting at a quarterly rate of approximately 0.6%.

The PMI survey also points to a strong rate of contraction of GDP, consistent with a quarterly rate of decline of 0.6% in April and May.

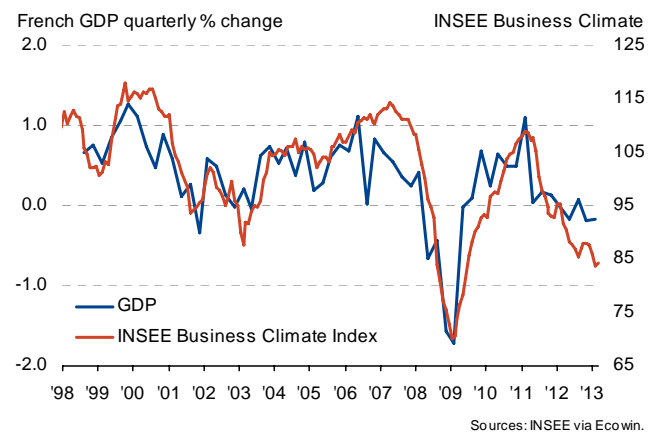
Both surveys therefore suggest that the French economy fared considerably worse in the second quarter than the 0.2% declines in GDP seen in the fourth quarter of 2012 and the first quarter of 2013. France's double-dip recession therefore looks set to have run into a third consecutive quarter. However, both surveys have signalled stronger rates of decline than the GDP numbers over these periods, making interpretation of the survey data for the second quarter difficult.

The PMI survey in particular has had a very close correlation with official GDP data prior to the middle of last year, making the current divergence unusual. However, the fact that both PMI and INSEE surveys

French business surveys

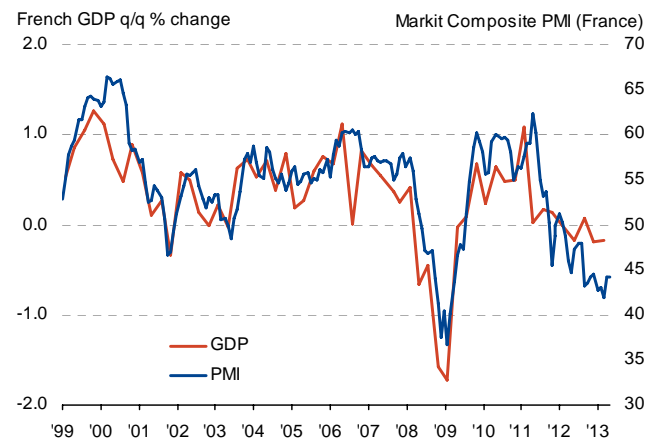


INSEE survey v GDP



Sources: INSEE via Ecwin.

PMI survey v GDP



continue to correlate closely suggest there is a possibility that the recent GDP data may be revised lower at some point in the future.

Export and consumer downturns

In April, the manufacturing PMI for France was the weakest of all countries surveyed by Markit, displacing Greece at the foot of the PMI rankings. Much of this can be linked to disappointing foreign sales. With the exception of two months of modest growth in early 2012, the PMI shows that French goods exports have fallen continually since mid-2011.

This poor performance is attributable to a number of factors. Clearly many of France's traditional export markets such as Italy and Spain remain entrenched in deep downturns themselves. However, the manufacturing sector is suffering from poor competitiveness. For example, while Spain saw unit labour costs fall in every quarter of last year, costs continued to rise throughout the year in France. Spain's unit labour costs have now fallen 5% below those of Germany, while France's remain almost 6% higher.

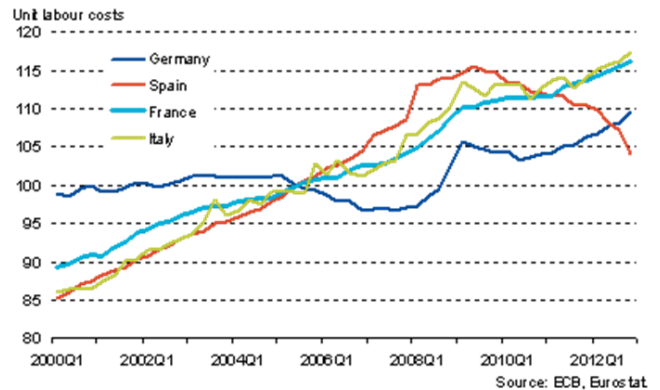
It is not just exporters that are struggling. A gloomy mood persists among consumers, where confidence has failed to show any significant sustained improvement on the lows seen at the height of the financial crisis five years ago.

The downbeat mood in the household sector largely reflects job worries. The unemployment rate rose to 10.2% at the end of last year, its highest since mid-1999, and job insecurity – measured by people's expectations of how they think unemployment will change over the next 12 months – has risen this year to the highest since the peak of the financial crisis.

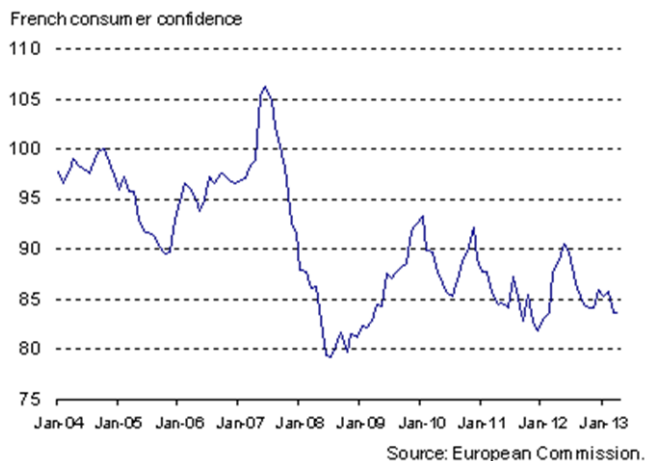
These job worries naturally relate to concerns about the ongoing downbeat flow of economic indicators, but also highlight growing discontent with the French government's handling of the economy and the lack of policy tools to reinvigorate growth.

The IMF sees the French economy contracting 0.1% this year but reviving to grow 0.9% next year. Given the recent flow of disappointing economic data, those forecasts are starting to look too optimistic.

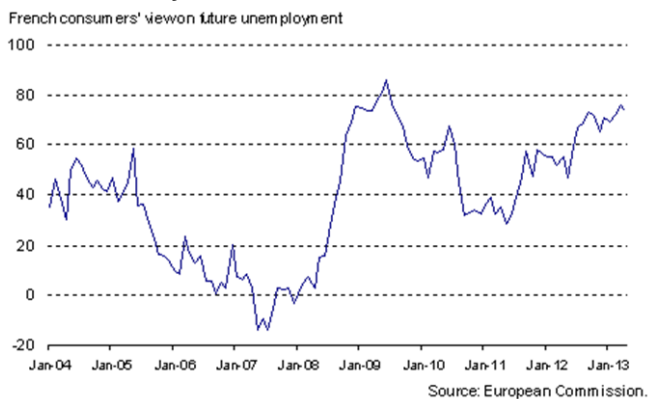
Unit labour cost comparisons



Consumer confidence



Job insecurity



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