



FRANCE IN A NEW ECONOMIC REFORM INFIGHT

“The suggestions about economic and labour market reforms in France are so far fairly unnoticed but the demonstrations are growing across France.”

My best guess is that more than 99 pct. of all economic analyses from the end of 2015 predicted a higher GDP growth in France this year. I myself have since long been sceptical about the economic growth prospects for the Eurozone, including France. The French government now plans to present reforms of the labour market to give the economy more momentum - maybe I therefore must reform my own assessment of France and its growth prospects.

Graphic one shows the French budget deficit as pct. of the GDP during the last 20 years. Throughout the period, the country had a budget deficit, and even quite large deficits in most years. The few times that the deficit has been reduced on a relative scale, it was partially due to pure mathematics. Because the deficit is shown as a percentage of the country's total GDP the deficit as a share of GDP declined during years with high GDP growth. This effect occurred in 1998-2000 just before the dot.com bubble busted. A similar effect was visible in the years ahead of the financial crisis that also ended with a recession. In reality, it quite well describes the French economy, namely surfing the global economic waves spiced with ongoing domestic economic stimulus. The economic stimulus is the annual budget deficit that compensates for unresolved issues such as

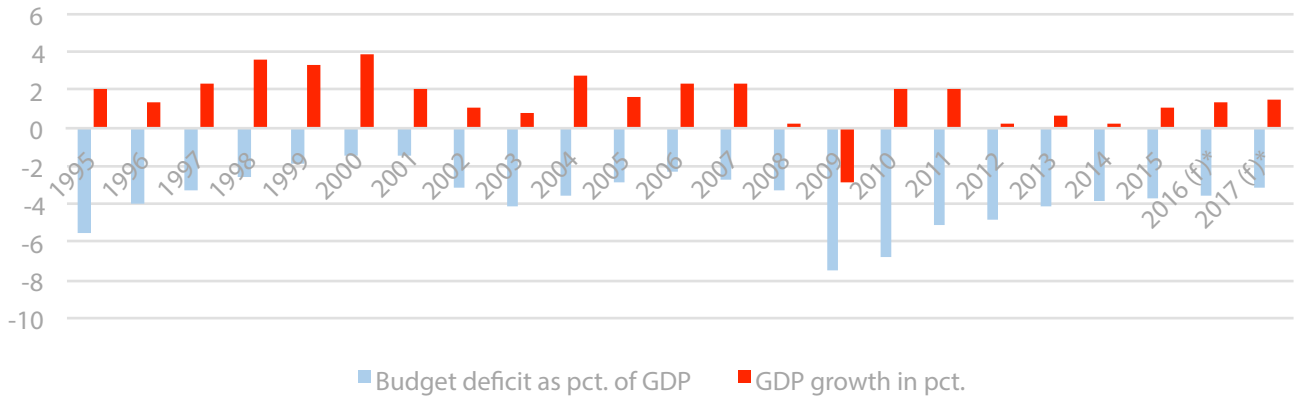
poor competitiveness compared to other countries. The very persistent and large annual budget deficit in France increasingly is a concern in the financial markets. As mentioned, I argue that France's GDP growth is almost a function of the global GDP growth without its own strong progress. My concern for France's growth prospect increases during a time when the global trade declines and global growth is under pressure as is the case right now.

France's GDP growth was 1.1 pct. last year but the “jump” in growth comes after several years with very low and partially negative economic growth. In an optimistic moment last fall, the International Monetary Fund (IMF) estimated that France's GDP growth would reach 1.5 pct. this year. The forecast was hurriedly corrected down to 1.3 pct. The only institution to maintain an expectation of 1.5 pct. GDP growth this year is the French finance ministry.

In January, what was brewed in the French government with the French Economy Minister Emmanuel Macron in front suddenly seemed quite interesting. The centrepiece of his ideas, and the eternal in the French reform discussions, is the labour market. Economy Minister Macron pointed out at the time that the reforms would be radical. Since then other government members also made proposals. One main pillar in the reforms is to make it easier for companies to lay-off employees. Moreover, there will be an attempt to end the 35-hour working week as companies should be allowed to negotiate longer work schedules for the employees. Some proposals include working weeks of up to 48 hours and working days of 12 hours.

Some of the labour market reform proposals would mean a dramatic deregulation relative to the rest of Europe. It does not seem likely that such a significant deregulation will be adopted.

FRENCH BUDGET DEFICIT AND GDP-GROWTH



Source: Eurostat / *(f) is an average of market expectations

What makes the political signals unclear are caused by internal political reasons as several politicians try to come in the limelight with reform suggestions.

The next presidential election in France will take place in 2017, though the current president Hollande plus the government is unpopular. Therefore, there is emerging turmoil in the government where several of the socialist politicians that are most featured in the Medias with reform proposal also tries to be considered as the Socialist Party presidential candidate. It makes it difficult precisely to assess how strong the real desire for reform changes is.

Certainly a reform of the labour market would be positive for France in the long run - if the reforms become reality. So far, other parts of the ruling Socialist Party opposed the proposals. The unions are protesting and there have been many demonstrations during the past weeks with close to 400,000 people demonstrating on 31st March.

I argue that the belief that reforms would lead to higher GDP growth this year is overly optimistic. According to medias, The Governor of the French central bank, Francois Villeroy de Galhau was particularly sharp in his criticism of the French government two weeks ago. His criticism was that the government recently had once again delayed reforms of the labour market.

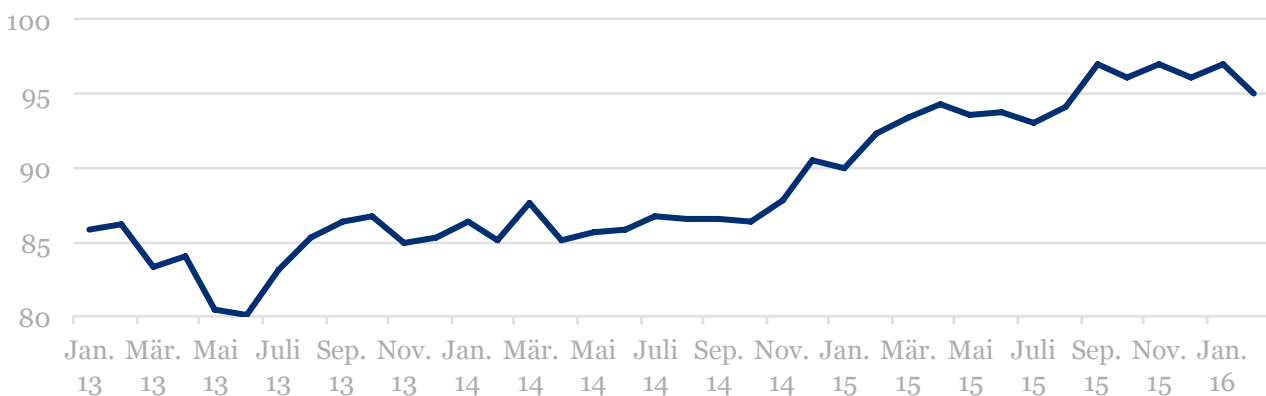
However, the Governor argued that the path to growth is through higher business investments. I regard this as less realistic in a world with overcapacity in the industrial production sector. My observation is further that countries with robust GDP growth currently are the countries with strong domestic private consumption.

On the first glance graphic two could indicate that France is among the countries with a robust private consumption as the consumer confidence is high despite the decline last month. But „neutral“ is 100 against the current standing at 95 meaning the country still has not even reached a neutral consumer confidence. The recent decline in confidence is interestingly partly due to households' assessment of their own financial situation plus a growing concern about unemployment.

I am not convinced that the labour market reforms will be impressive at all. But should it happen, then a short-term negative impact on private consumption is likely to take place. In any case, I am convinced that the current uncertainty about possible changes in the labour market will cause the consumer confidence to fall further.

I keep my view from last year, that the most likely scenario is a lower growth in 2016. So far, I see no reason to change this view unless the French government presents some unique economic reforms.

CONSUMER CONFIDENCE IN FRANCE



Source: INSEE, France

