

Economy

Focus France

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Birth and death of French companies

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If we judge the French economy by the demographics of its businesses then the verdict is irrefutable: the present situation is one of the best experienced in a very long time. Business start-ups are soaring, bankruptcies are falling, a phenomenon typical of an expanding economy. Whilst these developments are not a leading indicator of future growth, they do allay recurring concerns related to social disruption (rejection of reforms) and political uncertainty (unpopularity of Macron). In any case, it is little short of astonishing that business creation is so strong in a country with such a high tax burden.

The fortnight's focus

According to INSEE, the number of new companies created exceeded 800,000 in 2019, a record (+18% compared to 2018). Stripping out self-contractors (*autoentrepreneurs*), who make up 47% of this total, this implies an increase of 430,000 "standard" companies, again a record. For the past three years, this has mainly concerned corporate consulting and trade and warehousing, a sideline to the development of the digital economy; last year, there was also a marked upturn in construction. All told, the uptrend, initiated in 2015, is gaining momentum (chart lhs). According to the Banque de France, the number of business failures was close to 51,000 in 2019 (-5%), the lowest level since 2008 (chart rhs). This concerns most sectors. Loan outstandings of bankrupt companies account for around 0.4% of the total, down from the peaks of 2009 and 2014, two periods when the economy was emerging from recession.

Has France become a paradise for entrepreneurs? Far from it. The tax burden remains heavy. In the budget trade-offs at the time of the "Yellow Vests" crisis, the government chose to postpone the cut in the corporate rate tax¹. The weight of taxes on production remains prohibitive, not to mention the complexity of their calculation. According to the government's economic think tank², they represent 3.6% of companies' value-added compared with less than 0.5% in Germany. This hampers competitiveness. The government accepts the principle of reducing these taxes, but this means foregoing tax revenues. A conundrum for the finance ministry? The president of the jury for the 2019 entrance exam to ENA, the school that trains France's top public servants, recently deplored the fact that a large proportion of candidates saw companies only "as a source of financing for the State's action"! Since 2015, under then president François Hollande, with Emmanuel Macron Minister of the Economy at the time, efforts have been made to recreate a more favourable climate for companies (tax credit, lower social security contributions, flexibility). This project is still far from being completed.

1. In 2020, the corporate tax rate is 31% for large companies, 28% for all others. The goal is to align the rates at 25% in 2022. 2. See Martin & Trannoy (2019), "Taxes on Production: The Good, the Bad and the Ugly", CAE

France: business creation



Sources: INSEE, Banque de France, ODDO BHF Securities

France: business bankruptcies



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Economic news over the last fortnight

- According to the initial estimate for the quarterly national accounts, real GDP was down 0.1% q-o-q in **Q4 2019**. This is a particularly surprising result given that the usual proxies were pointing towards a gain of +0.1% and +0.3%. INSEE and the Bank of France had forecast an increase of +0.2%. According to INSEE, the decline is entirely due to changes in inventories which shaved 0.4 points off growth¹. Q4 was marked by social unrest, including the transport strike that started on 5 December and which ran until mid-January. The impact is visible in two main areas: ① on the supply side, the sharp decline in manufacturing production (-1.6% q-o-q); ② on the demand side, the marked decrease in spending on transport services (-2.0% q-o-q). In spite of this shock, domestic end-demand was actually up by 0.3% q-o-q, due to modest gains in consumption spending (private + public) and investment (household + business). All told, in 2019 the increase in end-demand *accelerated* to 1.8% vs 1.3% in 2018. Conversely, the pace of real GDP growth *slowed* from 1.7% to 1.2%. Since inventory corrections are temporary by nature, end demand provides a clearer picture, in our view, of the situation of the French economy.

(q/q% or y/y%)	2019				2016	2017	2018	2019
	Q1	Q2	Q3	Q4				
Real GDP	0.3	0.4	0.3	-0.1	1.0	2.4	1.7	1.2
- o/w Household consumption	0.3	0.3	0.4	0.2	1.6	1.6	0.9	1.2
- o/w Household investment	0.2	1.7	0.9	0.5	2.8	6.6	2.0	2.2
- o/w Business investment	0.6	1.1	1.6	0.3	2.7	5.0	3.9	4.2
Inventories (contribution, %pt)	0.3	-0.2	-0.1	-0.4	-0.4	0.2	-0.2	-0.4
Private employment	0.5	0.2	0.2	0.2	0.9	1.4	1.2	1.1

- The **January** surveys were encouraging. Household confidence rebounded, almost wiping out the correction observed in December at the height of the transport strike (+2 after -3). The INSEE index came in at 104, i.e. 4% above its long-term average vs 100 in 2019 and 97 in 2018. The unemployment expectations index was very low and, symmetrically, the spending intentions index was very high. For companies, the business climate is in an expansionary zone (see table on page 3). The synthetic INSEE index stood at 105 points, stable vs Q4, whilst retail trade continued to count the cost of disruption linked to the strikes. This was also visible in the PMI-Services index which was down to 51.1 points (-0.9 points m-o-m). The Bank of France survey for service activities was on a slightly more positive trend last month.

Forthcoming events

- The draft pension reform was supposed to be examined by the relevant committee of the National Assembly but this was made impossible due to the high number of amendments presented by the opposition (22,000 amendments). The reform's text will now be discussed in the plenary session from **17 February** with the vote on the first reading to be held by **3 March**. This will be a test of unity for the LREM majority on a controversial bill. As a last resort, the government can invoke article 49.3 so that the law could be passed without a vote, but this would be a political failure.
- The first round of the local elections will be held on **15 March** and the second on **22 March**. Normally, political parties with a strong long-standing base do well in this vote. At first glance, it is therefore unfavourable for new political parties, such as Emmanuel Macron's LREM, or those with an uneven presence throughout the country, such as Marine Le Pen's RN. The LREM's poor preparation for this election (internal divisions) is a complicating factor for the president, as is his unpopularity. **Early February**, President Macron's approval ratings continued to erode, reaching an average of 32% for the different surveys available. They have been on a continuous decline since their recent high of 36% in September 2019, with the period marked by the muddled presentation of the pension reform and the vigorous opposition that was the result. Their low point of 24% was hit in December 2018 when the "yellow-vest" crisis was at its peak.
- The impact of the coronavirus epidemic is unknown and the repercussions on the rest of the world even more so. The first indicator will be the business climate surveys in **February**. In France, they are due out on **21 February** for the PMIs and **25 February** for the INSEE indices. The French economy's sensitivity to China seems moderate with exports to China accounting for 0.9% of GDP, but certain sectors (tourism and luxury) have much higher exposure. According to the Directorate-General for Enterprise, China accounts for 2.5% of tourists in France (having doubled in ten years) and Asia around 7% of the total.

¹ The "inventories" category includes everything that cannot be attributed to the other aggregates; there might therefore be errors and omissions.



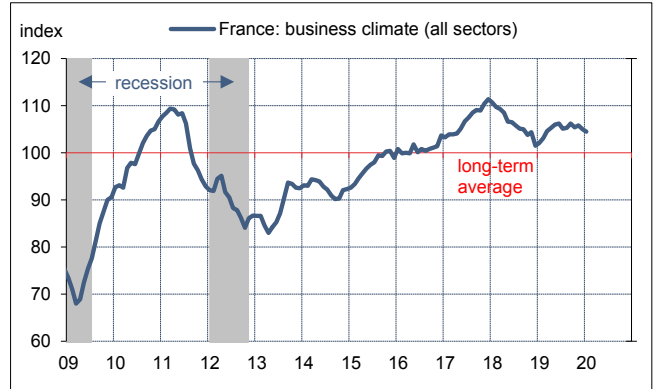
Appendix chart: business climate, confidence, households

Confidence indicators

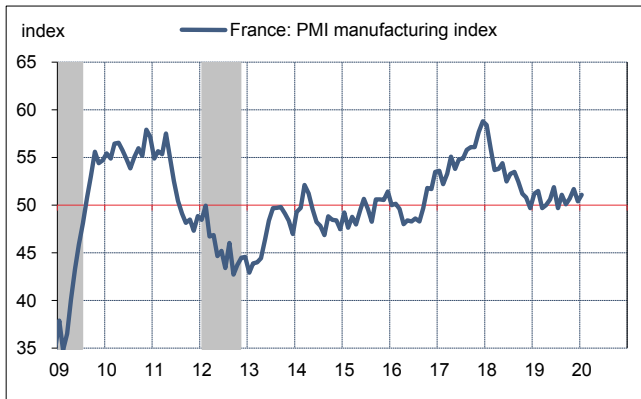
Index	Current			Expansion	Recession*	
	Jan	Dec	Nov		2008-09	1992-93
PMI manufacturing	51.1	50.4	51.7	52.0	42.6	-
PMI services (output)	51.0	52.4	52.2	55.2	46.8	-
PMI composite (output)	51.1	52.0	52.1	54.5	44.9	-
INSEE manufacturing	100	98	102	102	84	81
INSEE services	107	107	106	101	84	84
INSEE construction	111	111	111	103	102	85
INSEE retail sector	104	108	106	101	86	85
INSEE wholesale sector	104	105	106	101	85	87
INSEE consumer conf.	104	102	105	101	84	101
BdF manufacturing	96	96	97	103	79	86
BdF services	98	97	99	101	91	83

*from Q2 2008 to Q2 2009; and from Q2 1992 to Q2 1993

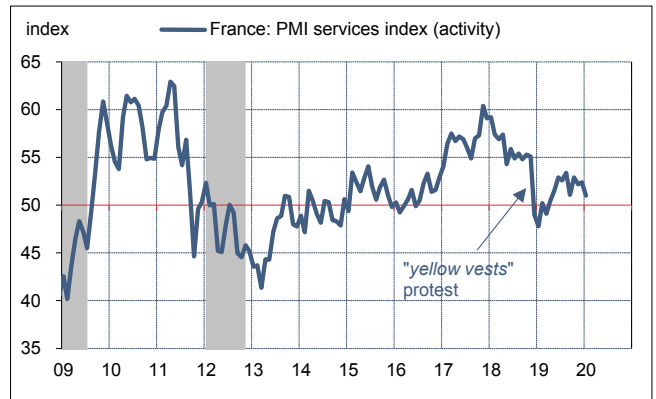
Business climate



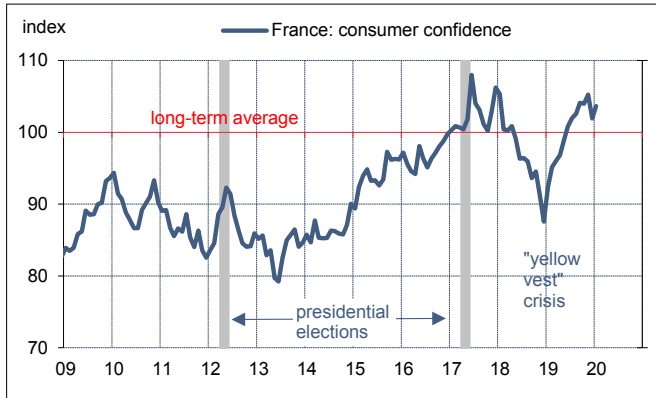
PMI-manufacturing survey



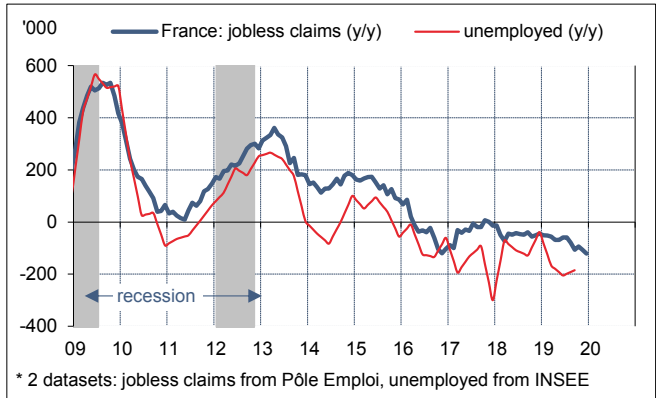
PMI services survey



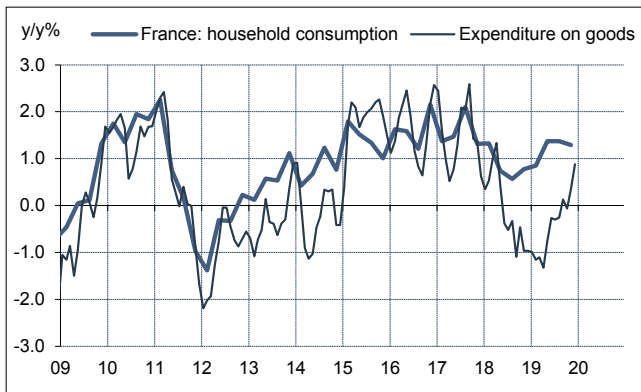
Consumer confidence



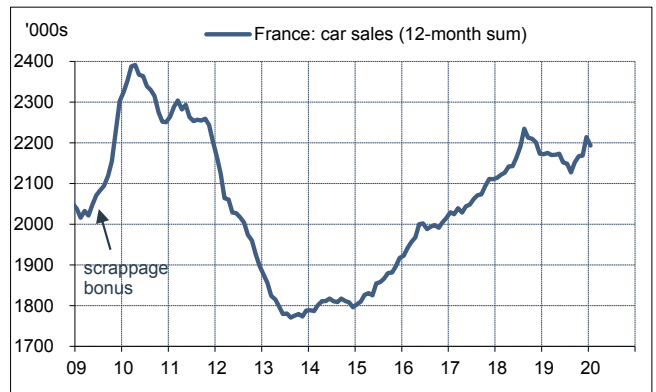
Jobless claims



Household spending



Vehicle sales

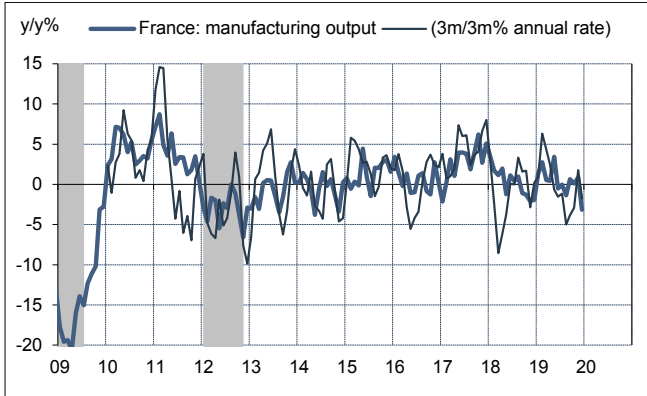


Sources : Thomson Reuters, Markit, ODDO BHF Securities

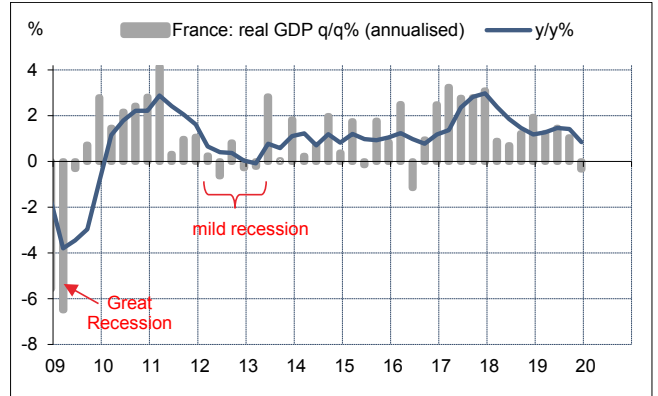


Appendix chart: activity, inflation, credit, finances

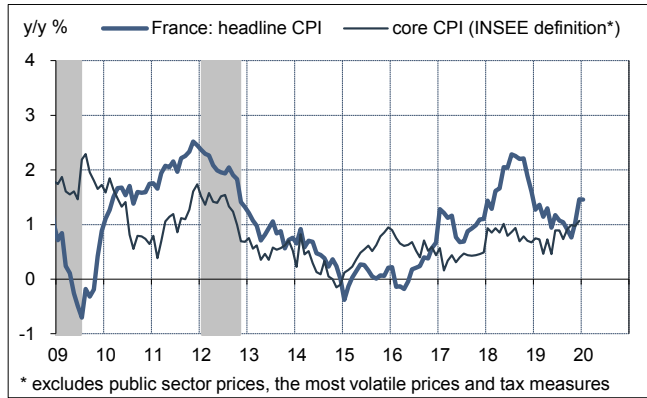
Industrial output



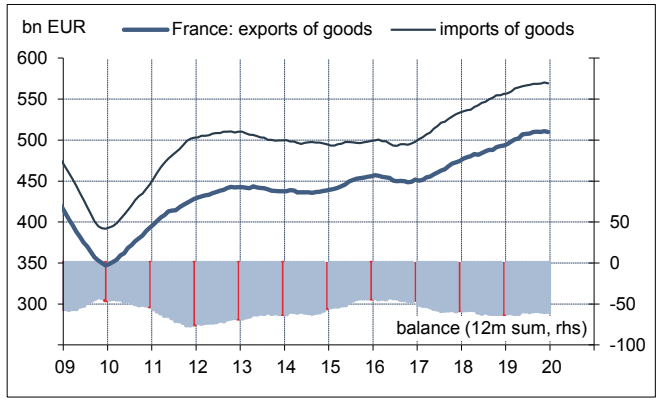
Real GDP



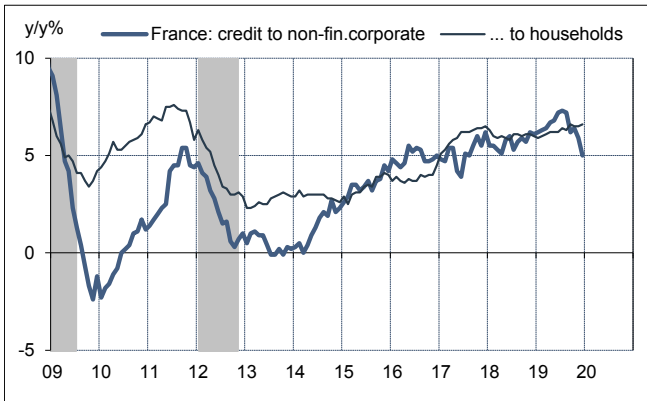
Headline and core inflation



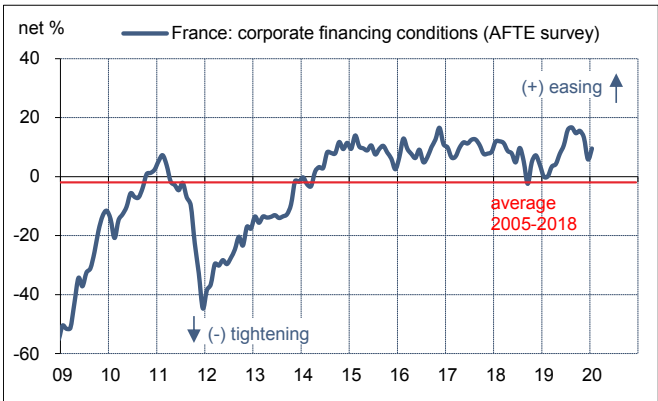
Trades of goods



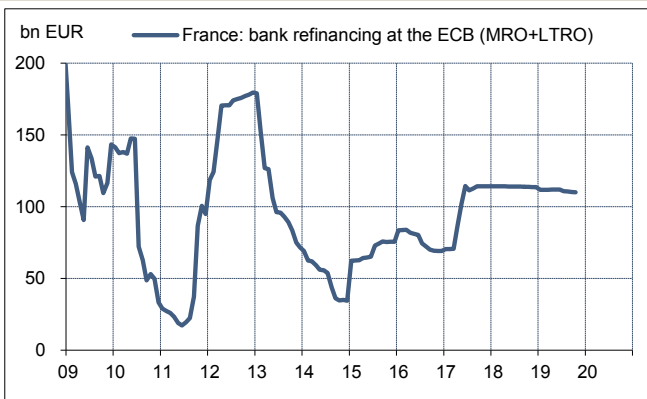
Private sector credit



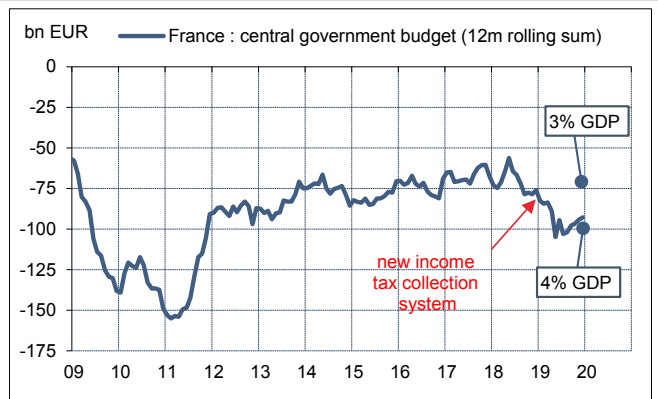
Credit conditions for businesses



Bank refinancing at the ECB



Government budget



Sources : Thomson Reuters, AFTE, ODDO BHF Securities



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