



Economic Update France

3 May 2011

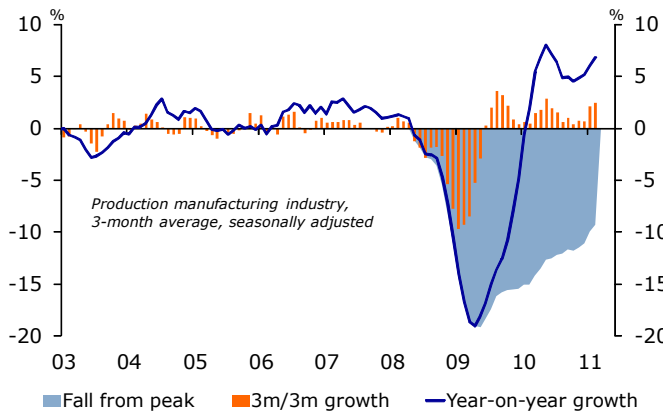
Producers take the lead

year-on-year change (%)	'10	'11	'12
Gross Domestic Product	1.5	1½	1½
Private consumption	1.7	1¼	1¼
Government consumption	1.4	1	1¼
Private investment	-1.7	2¼	2¼
Exports	10.1	7¼	4
Imports	7.8	5½	5½
Inflation	1.7	2	1½
Unemployment (%)	9.7	9½	9¼
Government balance (% GDP)	-7.0	-6	-5¼
Government debt (% GDP)	81.7	86¼	89¾

The economic recovery remains on track, based on a very strong momentum in the industrial sector. Producer confidence is currently at a record high and may lead to a pickup in investment. Production seems to be robust amid increased foreign demand. The inventory cycle is also helpful. Private consumption is expected to contribute less to growth this year, although the slowdown in 11Q1 was not as bad as feared. Later this year the austerity measures and rising inflation will surely take their toll. That said, the extent to which president Sarkozy is willing to announce further austerity measures will play an important role in the ongoing economic recovery.

Source: Reuters EcoWin, Rabobank

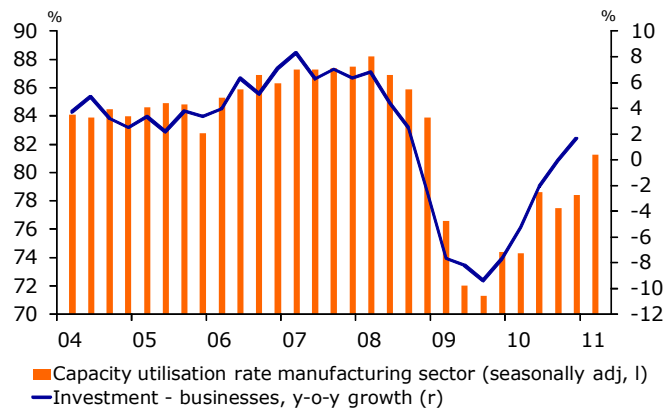
Industrial production has very strong momentum...



The production in the manufacturing industry had a robust start of the year and grew strongly in both January and February (by respectively 1.5% and 0.7% m-o-m). While the growth of domestic demand is slowing down, foreign orders are still encouraging. Moreover, business managers perceive their current stock levels as relatively low, which means production has further room to rise (albeit temporarily). Producer confidence (INSEE) in April is at its 40-month high and the sentiment among purchasing managers is particularly good as well (PMI is 56.9). Therefore, despite rising inflation, the outlook for 11H1 remains strong.

Source: Reuters EcoWin

...which might lead to investment growth



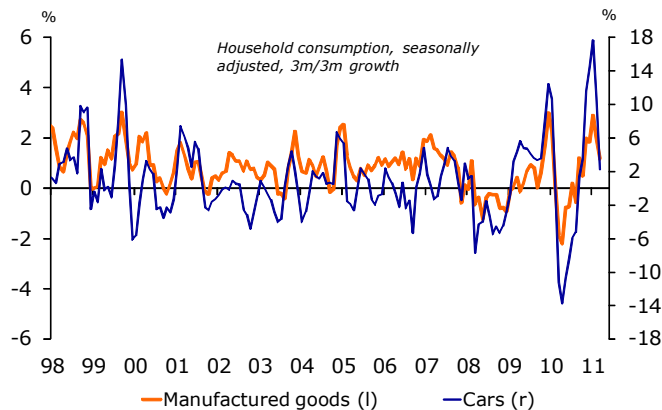
Despite the economic recovery, business investments decreased last year by 1.5% y-o-y. An important reason was that the capacity utilisation rate (CUR) in the manufacturing sector was far below its long term average (84%). The current CUR (81.3%) is still below that level, but the improvement compared to last year is significant. As a consequence of the recent production growth more producers are likely to invest with the aim of expanding their production capacity. However, we do not expect exuberant investment growth as the strong increase in producer prices (6.3% y-o-y in April) is putting downward pressure on profit margins.

Source: Reuters EcoWin

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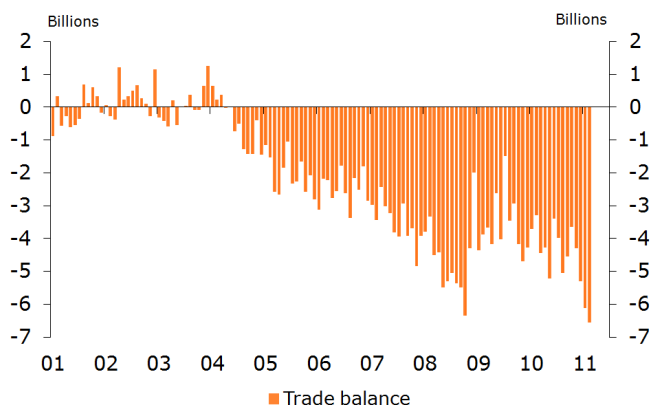
Consumption slowdown limited for now



Source: Reuters EcoWin

The anticipated slowdown of private consumption after a strong 10Q4 turns out better than expected. The consumption of manufactured goods had a bumpy start of the year but still showed 1.2% q-o-q growth in March. An important reason is that the fall in car sales following the expiration of the car scrappage scheme in January becomes only slowly visible in the sales data. That said, we expect a moderate growth of private consumption in 2011 due to the upcoming austerity measures, the rise in inflation and the muted nominal wage growth. Despite improving employment expectations (EC) in both the services and the industrial sector, consumer confidence (INSEE) remains on a low level.

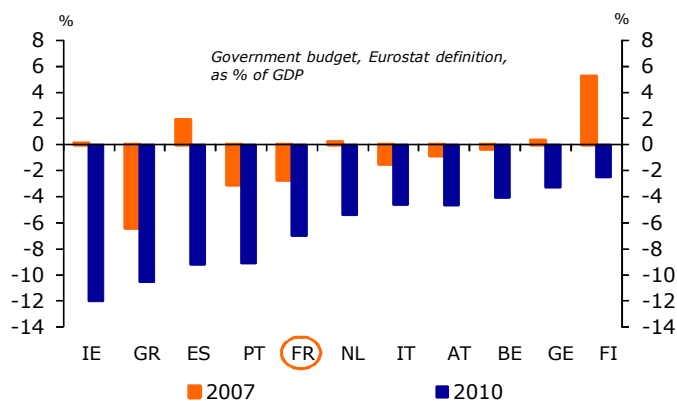
Trade balance shows record deficit



Source: Reuters EcoWin

The French trade deficit rose in February for four months in a row and is currently, despite a robust exports recovery (+13.9% y-o-y), on its highest level ever. This can be explained by high commodity and food prices, but also by relatively strong domestic demand in recent months. Private consumption, investments and inventory building have all contributed to high imports. Furthermore, the deterioration of the trade balance also reflects the ongoing weakness in France's competitiveness in the international marketplace. To remain able to take advantage of growing world trade in the future, wage moderation together with a boost in innovation is of crucial importance.

Public finances remain precarious



Source: Reuters EcoWin

The French budget deficit in 2010 has recently been revised downwards from 7.7%-GDP to 7.0%. This is good news for the French government, but does not reduce the necessity of austerity measures. The deficit is high from a European perspective and the unambitious budget target for 2011 (deficit of 6%-GDP) does not improve the situation. Besides that, for the period after 2011 only a few measures have been announced in concrete terms. As the election of May 2012 draws closer, Sarkozy's government is ignoring the precarious state of the public finances to prevent further loss of approval. In the long term the austerity measures will surely put a drag on growth.

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