

SAVING TELEGRAM

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FRAME ECONOMIC

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TO FCO

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FRANCE : ECONOMIC REPORT FOR SEPTEMBER 1985

SUMMARY

1. Industrial production is increasing, industrial investment appears to be rising. Demand for manufactured goods is at a high level, and the annual rate of inflation is down to its lowest level for many years. There has been a surplus on trade in two recent months. Predictably, unemployment continues to rise slowly.
2. Industrial production has been increasing since June and is expected to continue to increase during the rest of the year. The monthly rate of bankruptcies in industry dipped in July and August but is expected to rise again. The annual rate of inflation fell to 5.6% at the end of August, a decrease of almost 1 percentage point over 2 months.
3. There was a very small surplus on the balance of trade in August, the second surplus in three months.
4. Thanks to a large differential in real interest rates, the franc remained firm against the deutschmark and other EMS currencies, despite the fall in the dollar.
5. At a time when other continental exchanges were reaching new peaks, the Paris Bourse was on a downward path, with investors discouraged by several factors: prospective capital issues, the anticipated effect of the opposition's privatisation plans, and a general pre-electoral political uncertainty.

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DETAIL

Foreign Trade and the Balance of Payments

6. In August there was a foreign trade surplus of F0.004 billion FOB/FOB seasonally adjusted and of F0.177 billion unadjusted. This follows a deficit of F3.837 billion seasonally adjusted in July. The improvement was due to a decrease in imports of F3.221 billion, to F74.919 billion. Exports increased by only F0.62 billion to F74.923 billion. For the first 8 months of 1985 there is a deficit of F18.232 seasonally adjusted.

7. This is only the second monthly surplus since the beginning of 1985. (There was a surplus of F1.995 billion in June.) In July INSEE commented that the balance of trade would improve during the summer because of a temporary drop in energy imports, but would deteriorate towards the end of 1985. Average monthly energy imports for June to August of F15.5 billion, were F4.6 billion down on the monthly average for January to May. INSEE forecast a trade deficit of F20.0 billion for the whole of 1985 but this was based on an average exchange rate of F9.40 to the dollar. At the beginning of October the exchange rate was F8.15 to the dollar.

8. A new monthly series of volume and constant price trade figures published by INSEE in September includes arms sales, ship building and oil rig construction, which were excluded from the previous series. These figures show that a substantial drop in arms sales has had a significantly adverse effect on the balance of trade. Over the first half of 1985 compared with the average level of 1984 in volume total exports increased by only 1.3% while imports increased by 2.7%. If arms sales are excluded exports increased by 2.1%. Arms exports fell by 16.9% in volume during the first half of 1985 compared with the average for 1984. This reflects the low value of arms contracts concluded abroad in 1983: F29.1 billion. The financial press estimates that the full effect of the record F61.8 billion of arms export contracts signed in 1984 will be seen in the balance of trade in 1986.

9. Another exceptional grain harvest may boost exports during the last few months of 1985 but the international market is more difficult than in 1984 when a record grain harvest made an exceptional contribution to exports.

10. An increase of 5.7% in the volume of capital goods imported over the first half of 1985 compared with the average level of 1984 suggests that investment may be increasing.

Industrial Production

11. INSEE industrial production index for July has not been published yet.

/12.

12. Industrialists replying to an INSEE survey completed in September report that the production is increasing in all sectors except in the car industry where it is stable and that demand has reached a level not attained for several years. The increase in production costs continues to be moderate. Industrialists are optimistic about prospects.

13. According to industrialists the rise in the production of capital goods begun six months ago continues, but at a slower rate. Stocks continue to decrease and demand both in France and for exports is growing. Industrialists forecast that there will be a further slow increase in production during the fourth quarter.

14. The increase in the production of consumer goods begun 3 months ago continues, with the exception of domestic equipment and publishing. Stocks have continued to fall and are now below normal levels. Demand, both in France and for export, is stable at a high level, following an increase during the second quarter. Industrialists forecast that production will continue to increase during the coming months.

15. Car production is stable following the drop in production recorded in the previous survey. Demand in France has fallen, but export demand is increasing. Stocks have decreased slightly and industrialists forecast that production will remain stable during the coming months.

16. The increase in the production of semi-finished goods which started at the beginning of the second quarter continues except in the paper and non-ferrous metals sectors. Stocks are still below normal levels. Demand both in France and for exports is increasing. Industrialists forecast that production will increase during the fourth quarter.

17. In August the cost of raw materials imported by industry was 20.2% lower in francs than at the end of 1984 and 12.3% lower in foreign currency.

Industrial Sectors : Textiles and Clothing  
include

18. The MER will henceforth/a brief report on the state of one or two industrial sectors, the first being textiles and clothing.

19. The French industry now employs some 450 - 460,000 people (2.2% of the active labour force) compared with 700,000 10 years ago, and 540,000 in 1980. The reduction in jobs continues but at a slower rate of some 10 - 15,000 annually in the last two or three years. Taking 1970 as a base (= 100), the production index for the industry is now 91, compared with 117 in 1973 and 107 in 1979 (the overall industrial production index stands at 132). The industry's share of total GDP in 1983, the last year for which reliable statistics are available, was 1.4%. In the same year its share of total French exports was 4.1%, while imported goods in the sector accounted for 4.6%

/of French

of French imports. Some 31% of the French market is taken by imports, while the overall ratio of exports to imports is 85%. The sectoral deficit in 1984 was some F8 billion.

20. After the steep decline of the 1970s and early 1980s, the industry is now in a relatively stable period. It was helped from 1982 - 84 by government aids (reduction of social charges, soft loans) which pushed up investment - F3.8 billion or 4% of turnover in 1984 - and slowed down job losses. Modern production methods and equipment are beginning to penetrate the industry. However, its health remains fragile. Domestic demand has been in decline for the last two years, because of the drop in household purchasing power, but this has so far been compensated for by higher demand from other recovering OECD economies, notably the US (exports up some 60% in 1984). Clothing has suffered in all areas from the fall in domestic demand and more recently from unseasonal weather but this has been at least partly compensated for by exports.

21. Profit levels are generally recovering after several lean years, although the picture remains patchy. Most of the bigger names, with the notable exception of Boussac St Frères (still restructuring but beginning to look healthier) and Rhone Poulenc Textile/Fibre, are now doing reasonably well.

22. Future prospects are not encouraging. A lower dollar is likely to affect exports directly and also increase import pressures because of diversion of cheap Far Eastern goods from the US market. This may be partly matched by an increase in domestic demand if the wider economy recovers significantly. But a continuing slow decline is likely unless efficiency and competitiveness improve markedly. Against this background, the industry's main concerns are potential threats from the forthcoming renegotiation of the Multi-Fibre Arrangement, where they are opposed to any significant liberalisation, and from mounting protectionist pressures in the US. They are also continuing to press the government for a new textile aids scheme, despite the known Brussels complications, and (an old claim) for a lasting reduction in the heavy social charges to which they are subject in France as a labour-intensive industry.

#### Demand

23. Signs of increased demand have been visible in the retail trade since July. Spending by households has increased in anticipation of the reduction in income tax levels effective in the autumn. An INSEE survey completed in September shows that in the non-food trade, following a drop in sales in May and June, sales rose sharply in July-August to well above the level for January to April. Stocks are low and retailers are increasingly optimistic about prospects. Sales in the food trade which had been stable from January to June decreased in July and August. (Sales in the food trade also decreased in July and August 1984, but by a larger amount.)

/Prices and Wages

## Prices and Wages

24. The annual rate of inflation (over 12 months) decreased to 5.6% at the end of August from 6.1% at the end of July. The annual rate has fallen by almost 1 percentage point since the end of June, when it was 6.4%, following six months during which the rate remained almost stable. The government's target for inflation at the end of 1985 is 4.5% to 5.0%. In August the retail price index rose by only 0.1%.

## Unemployment and Industrial Relations

25. The number of unemployed increased in August by 10,700 to 2,424,900 seasonally adjusted and by 50,700 unadjusted to 2,309,000.

26. The effect of the government's special measures for young people is reflected in the unemployment statistics. Since August 1984 the number of unemployed under 25 years old has decreased, seasonally adjusted from 984,700, 41.7% of the total unemployed to 918,600, 37.9% of the total unemployed. Over this period unemployment in all other age groups has increased except in the over 50s group where it has remained stable.

27. In the five months to August 1985 new vacancies, seasonally adjusted, averaged 31,260 per month compared with 33,140 during the same period in 1984. In the five months to August 1985 deletions from the unemployment registers, seasonally adjusted, averaged 382,000 per month, 67,000 more per month than over the same period in 1984.

28. In a television appearance on 4 September, the Prime Minister estimated that 200,000 - 400,000 new jobs a year would have to be created to solve the unemployment problem over 15 years, and emphasised the need to promote economic growth and productivity by means of more flexible working patterns. A Parliamentary report (le rapport Taddei) published on 26 September recommended a number of measures based on this approach to promote a better utilisation of capital equipment. One of its main recommendations was implemented immediately: with effect from 1 October certain state aids to companies for training and employment, soft loans for investment, and loans for industrial modernisation are to be available on condition that negotiations on flexible working patterns are undertaken.

29. A draft law to increase fiscal disincentives for retirement pensioners (aged over 60) who take paid employment has been put to Parliament. Commentators are sceptical about likely effects on job vacancies and tax revenues.

30. The TUC scheme (work of community benefit by young people) continued to grow: 146,000 young people were taking part at the end of August, 4,600 more than at end-July. Employers and unions agreed to relaunch training for young people by companies ('formation en alternance'). They aim to provide

/300,000

300,000 places by April 1986.

31. A survey published by the research institute ADIA found that in 1983 French companies spent some 2.11% of payroll on training, compared with 2.04% in 1979.

32. Government spokesmen played down the problems of the Social Security system, taking the line that the general fund (pensions, health, family allowances) would be in surplus at the end of 1985, and that it is too early to take a view on 1986. But commentators on the draft 1986 budget noted that proposed savings in state expenditure in this field would increase the deficit expected in the social security funds at the end of 1986.

33. The Employment Minister agreed to suspension of repayment of the unemployment benefit fund's capital debt until March 1986, provided the employers and unions define a plan for financial stability, and to consider rescheduling the debt with effect from April 1986 provided that a new long-term agreement is reached on the financing of unemployment benefit. However, negotiations were broken off on 1 October when the Communist-dominated CGT gave the press a tape-recording of the employers' proposals.

34. Basic unemployment benefit was increased by 2.5% with effect from 1 October to a daily minimum of 104,55 francs.

35. The number of days lost in localised industrial action rose to 39,840 in June, involving 80,680 people in 25,582 establishments. In July 36,450 days were lost by 39,631 people in 14,383 establishments. In addition, 10,365 days were lost in June and 1,809 in July in strikes affecting more than one region. There were a number of strikes in September: two by air traffic controllers on 4 and 18/19 September grounded most internal and European flights. An official railstrike on 27/29 September disrupted traffic, but was overshadowed by a wildcat strike by drivers which spread throughout France on 1 October, bringing railways to a virtual standstill. A return to work was achieved only after management withdrew their decision that drivers' knowledge of safety procedures should be tested: a meeting to discuss all aspects on safety on railways is to be held on 18 October. The CGT continued to encourage strikes and stoppages, and called for a general day of action on 24 October.

36. Barge-owners blocked the Seine and took violent action in a number of other areas of France during the first three weeks of September, protesting against unfair competition from other freight carriers.

#### The Situation of Companies

37. In July 2,253 company bankruptcies seasonally adjusted were recorded and in August 2,166. Although these figures are below the monthly average of 2,310 for the first six months of 1985 INSEE estimates that there is an underlying trend towards a gradual increase in the number of bankruptcies.

38. There has been a total of 18,279 company bankruptcies, seasonally adjusted recorded during the first 8 months of 1985, 990 more than during the same period in 1984. Bankruptcies in the services are around 20% higher, but bankruptcies in industry are almost 7% lower.

39. In a report published in September INSEE remarks that although company results have improved on average over the last three years, the general situation of companies is still far from good. Company finances have benefitted from moderate wage increases and a rise in the level of exports, but investment is increasing only in industry, and by a far greater amount in the nationalised industries than in privately owned firms. INSEE comments that a combination of weak demand and high real long term interest rates (5 - 6%) is discouraging investment by companies which would have to borrow to invest, and encouraging companies with funds to put them in the money markets rather than into new plant or equipment.

#### Denationalisations

40. RPR Banque, an RPR study group, has published a document refuting claims in some quarters of the financial press that the Paris financial markets would not have the capacity to finance the denationalisation of state enterprises. The study group has however omitted from its calculation several large companies such as Air France, Renault, Framatome, SNECMA, SNIAS and Machines Bull, on the basis that these companies' losses in 1983 and 1984 make it difficult to calculate their likely capitalisation. The group estimates at F145 billion francs the stock market capitalisation of the remaining state enterprises in the opposition's denationalisation programme. This is equivalent to just over 9% of the total French stock market capitalisation of F1,600 billion. The group suggests that the French financial markets could finance the opposition's denationalisation programme without difficulty if it were spread over three years.

#### 1986 Draft Central Government Budget

41. The 1986 draft central government budget was approved by the Council of Members in September and some of its details published. Planned government expenditure excluding debt servicing will increase by only 2.8% in 1986 compared with a government forecast for an average annual rate of inflation of 3.4%. For probably the first time since the Second World War, there will be a real decrease in public spending other than for debt service. If debt service, which has grown rapidly since 1981, is included planned expenditure will increase by 3.6% to F1,030 billion. Only the Ministries of Defence, Research, Education, Interior and Culture will enjoy real increases. The biggest cut has been made in the Ministry of Industry's vote.

42. The planned deficit of F145.3 billion would be equivalent to the 3% of the GDP ceiling set for budget deficits by President Mitterrand, but opposition spokesmen have pointed out that F12 billion of expenditure has been debudgetised. F11 billion of the debudgetisation takes for the form of a reduction in social security transfers.



43. Several newspapers have pointed out that if the opposition win the Legislative elections due in March 1986 they will find it extremely difficult to make radical amendments to the budget without making unpopular cuts in public spending in, for example, education or defence, or increasing government borrowing.

44. The budget is based on the following forecasts for the economy in 1985 and 1986.

/INTERNATIONAL ENVIRONMENT

INTERNATIONAL ENVIRONMENT	1984	1985	1986
franc/dollar exchange rate	F8.73	F9.10	F8.50
GDP growth of France's principal trading partners (weighted according to importance of French exports) %	2.7	2.4	2.2
Official oil price (dollars per barrel)	28.5	26.3	25.0
Inflation (average of France's 8 principal trading partners) %	5.5	4.6	4.0
<b>FRENCH ECONOMY</b>	<b>%</b>	<b>%</b>	<b>%</b>
GDP (marketed)	1.5	1.3	2.1
Consumption	0.5	1.3	1.6
Investment by companies	-2.9	1.8	4.0
Exports	6.3	3.0	3.4
Imports	1.6	2.7	3.7
Retail price rise (over 12 months)	6.7	4.5-5.0	2.9
Purchasing power of disposable income	-0.7	1.1	1.3
Total number of employed	-1.4	-0.8	-0.4
Balance of trade (billions of francs)	-25.0	-12/15	5
Balance of payments (billions of francs)	-6.6	0 to 5	10 to 15

45. This is a slightly more optimistic forecast for the French economy in 1986 than that published by the government in June (paragraph 49 of the MER for June) perhaps partly because it is based on a more favourable forecast for the international environment: a greater depreciation of the dollar against the franc, lower oil prices and lower average inflation in France's main trading partners.

46. The principal changes in the forecast are for 1985 consumption growth (1.3% instead of 0.8%, export growth 3.0% instead of 4.1%) and for investment by companies in 1986 (4.0% increase instead of 1.8%) and for a balance of trade surplus of 5 billion instead of 2. The government has also added a forecast of a balance of payment surplus in 1986 of F10 to F15 billion.

#### The Stock Exchange

47. Dealing on the Stock Exchange is becoming subdued with the approach of the Legislative elections due in March 1986, and prices are on a downward trend. Calls for fresh capital, a large programme of government borrowing, the growing popularity of short-term money market funds, general pre-electoral uncertainty, and questions over the effect on French companies of the dollar's decline are all factors in this situation. In addition, dealers are anticipating a substantial increase in the volume of shares on the market if the opposition parties win the elections and put their denationalisation programme into effect.

48. The CAC index of French shares which rose by 30% during the first five months of 1985, following rises of 16% in 1984 and 57% in 1983, has fallen by 9% since the beginning of June. A recovery in the CAC index in August was short lived and was followed by a 5% fall in September. At the beginning of October the volume of share offers continues to exceed demand and Le Monde's stock exchange correspondent has reported steady selling of shares from abroad. The trend of the Paris Bourse is in sharp contrast to other Continental exchanges such as Frankfurt, Milan and Brussels.

49. A F15 billion government bond issue on 16 September has been received with circumspection. Investors have calculated that interest rates will rise if there is pressure on the franc with the approach of the Legislative elections. Some leading members of opposition parties have spoken of the need to devalue the franc after the elections.

#### Monetary Policy

50. No figures for the money supply have been published since July when the March figures were announced. In June the Bank of France announced that preliminary figures for the first five months of 1985 showed that M2R, the main French money supply measure was growing at an annual rate of 8%, well above the government's target range of 4% to 6% and that corrective measures were being taken.

51. The Director of the Tresor, Monsieur Lebègue, said in a speech on 17 September that the changes taking place in the world's financial markets would inevitably lead to a change in the methods used to control the money supply, particularly in France. The setting of quantative ceilings would have to give way progressively to control by interest rates and open market dealing by central banks.

#### The Exchange Rate

52. For the first three weeks of September the rate of exchange of the franc against the dollar varied between F8.70 and F9.00, then, following the G-5 meeting in New York on 22 September, the franc together with the other main currencies, strengthened rapidly against the dollar. By 3 October, the exchange rate had fallen to F8.07, the lowest rate for 18 months and substantially below the record F10.61 attained on 26 February 1985.

53. The franc has remained strong within the exchange rate mechanism of the E.M.S. It rose slowly from near its ceiling rate at the beginning of September to reach the ceiling rate at the end of September, and has remained there during the first few days of October.

54. The franc, supported by relatively high interest rates, has remained firm against the deutschmark, despite the sharp depreciation of the dollar.

55. At the end of September rumours that the pound was to join the exchange rate mechanism of the EMS caused it to depreciate against the franc. Over two days the rate fell from FF11.81 on 25 September to around F11.40 where it has remained over the first few days of October.

#### Interest Rates

56. The Bank Base Rate remained unchanged at 10.85% during September.

FRETWELL

FRANC ECONOMIC  
(C D C I)

FRANC VALUES IN PARIS IN SEPTEMBER 1985

(weekly closing prices)

US\$	8.96	8.86	8.73	8.18
100 SF	370.86	369.16	371.59	372.60
100 DM	305.28	304.68	305.28	305.26
£	11.88	11.87	11.90	11.50

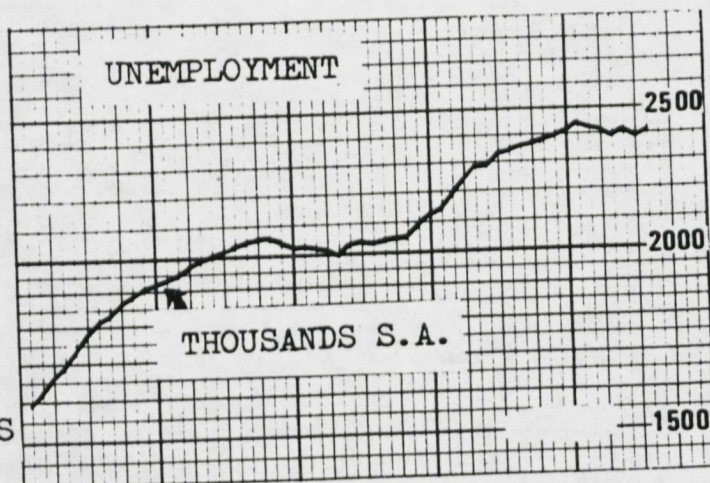
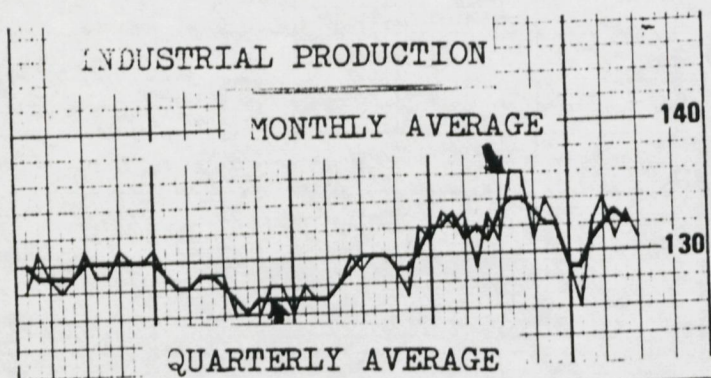
FRENCH ECONOMIC INDICATORS

(Seasonally adjusted, except as noted)

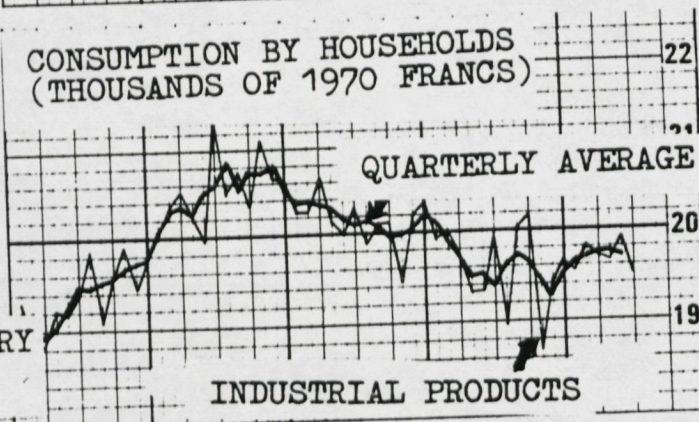
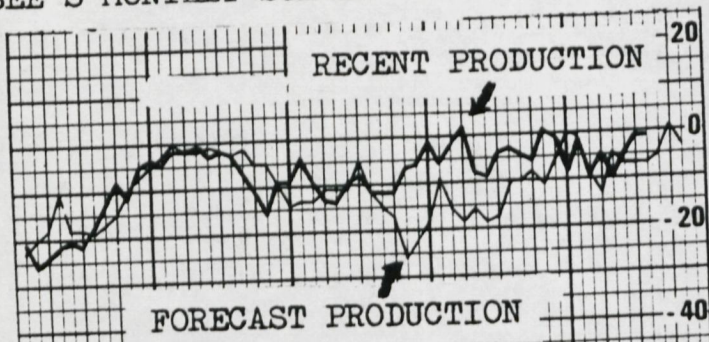
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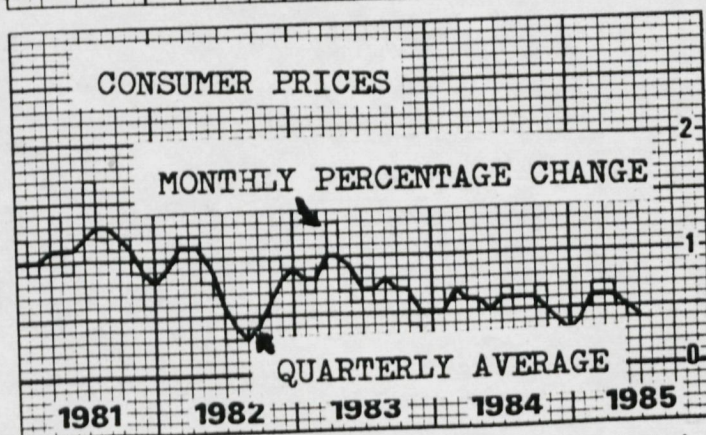
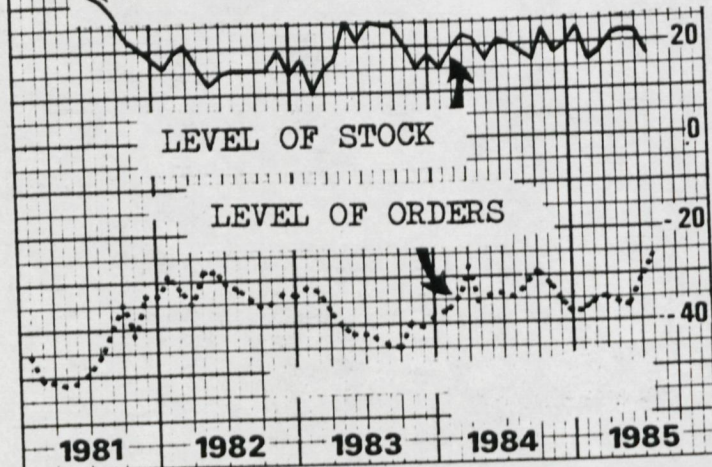
1. GDP, annual growth	1.5	1.5 (govt forecast)
2. Industrial production index Base 100: 1970	130 (June)	131 (June)
3. Total unemployed	2,360,000 (August)	2,424,900 (August)
4. Exports	F76.5 billion (August)	F74.923 billion (August)
5. Imports	F73.0 billion (August)	F74.919 billion (August)
6. Trade balance	+F 3.5 billion (August)	+F 0.004 billion
7. Balance on Current Account	-F12.6 billion (Jan-June)	-F 2.7 (Jan-June)
8. Exchange rate against US\$ (last working day of the month)	F 9.28 (September)	F 8.15 (September)
9. Official reserves	F405.41 billion (27 September)	F424.627 billion (26 September)
10. Growth in money supply (M2R)	1.1% (March)	1.2% (March)
11. Rise in retail prices	0.5% (August) 7.4% change over 12 months)	0.1% (August) 5.6% change over 12 months)
12. Rise in hourly wage rates of manual workers	1.5% (Q1) 9.1% (change over 12 months)	1.4% (Q1) 6.3% (change over 12 months)
13. Industrial disputes Working days lost Firms affected (Cumulative totals to end July )	870,000   2,216	297,300   1,209
14. French exports to UK FOB French imports from UK (Jan - June) CIF	F30.61 billion F36.35 billion	F35.72 billion F43.14 billion (revised)

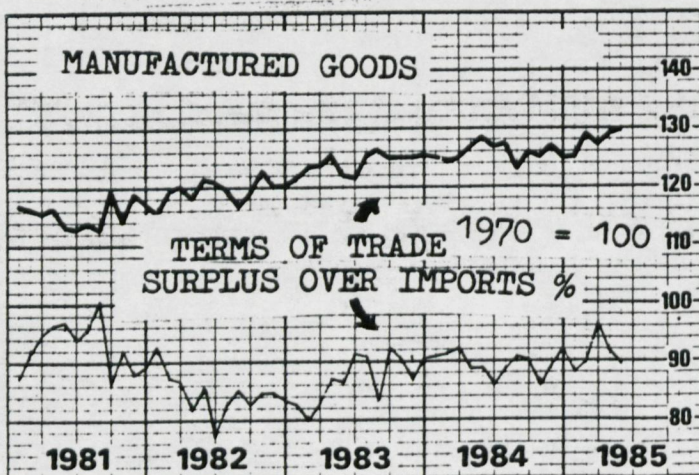
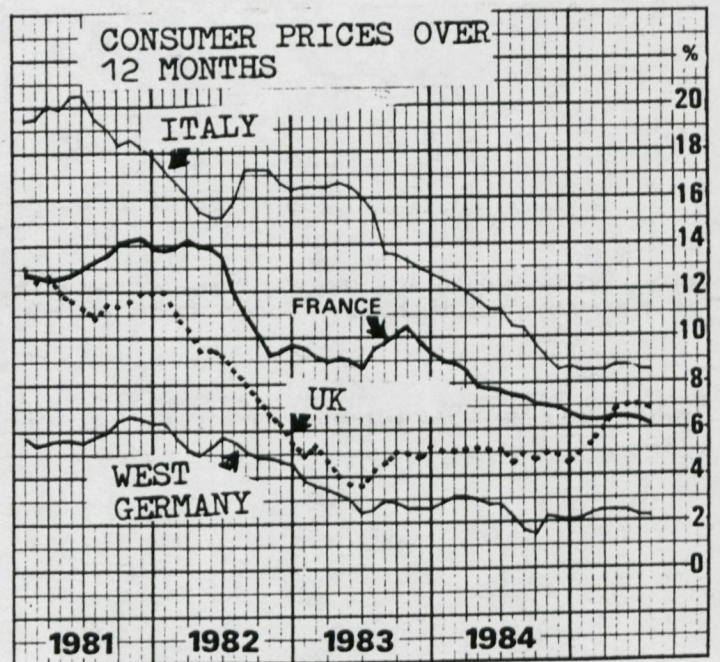
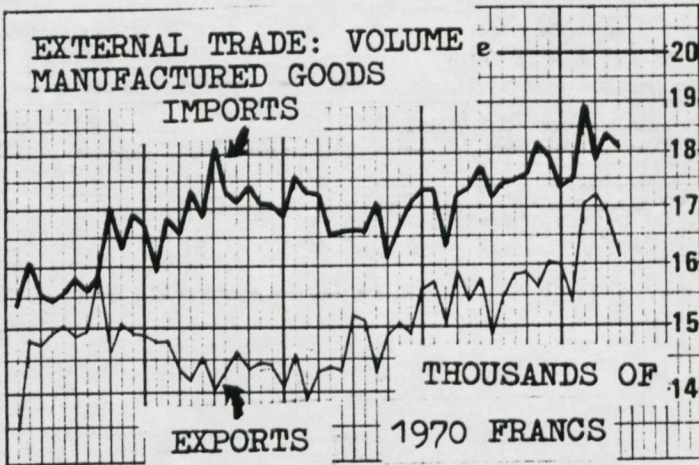
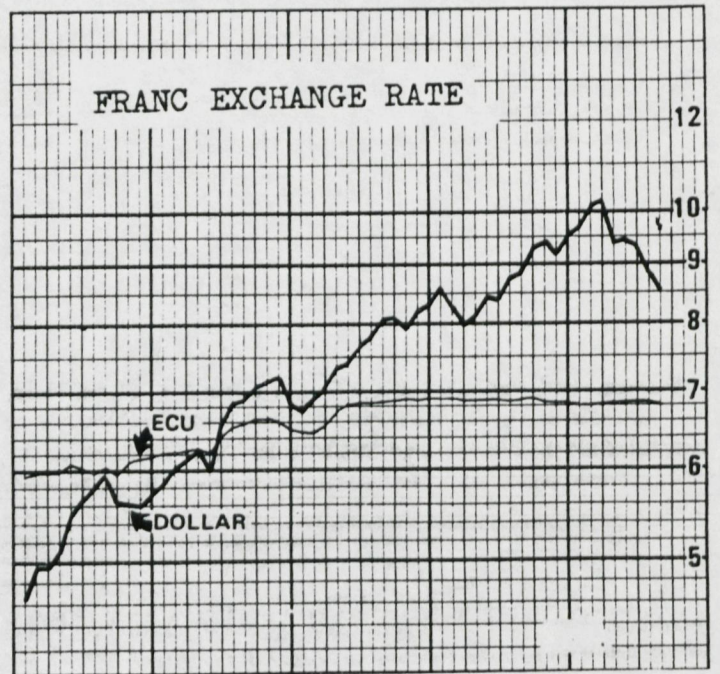
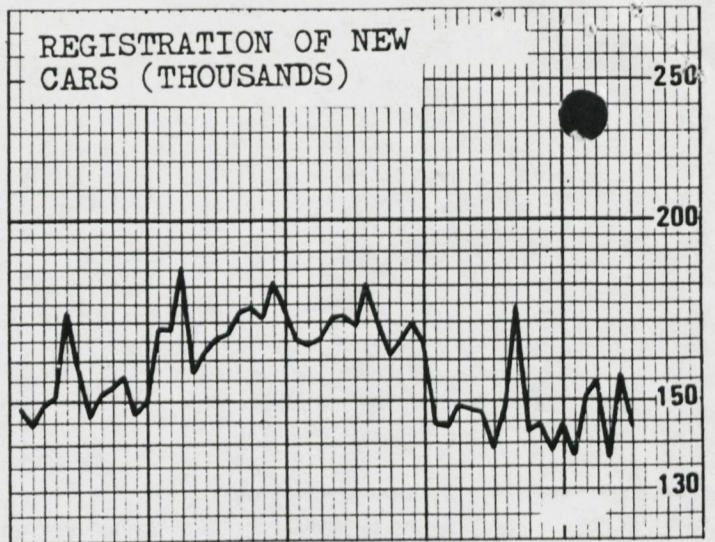
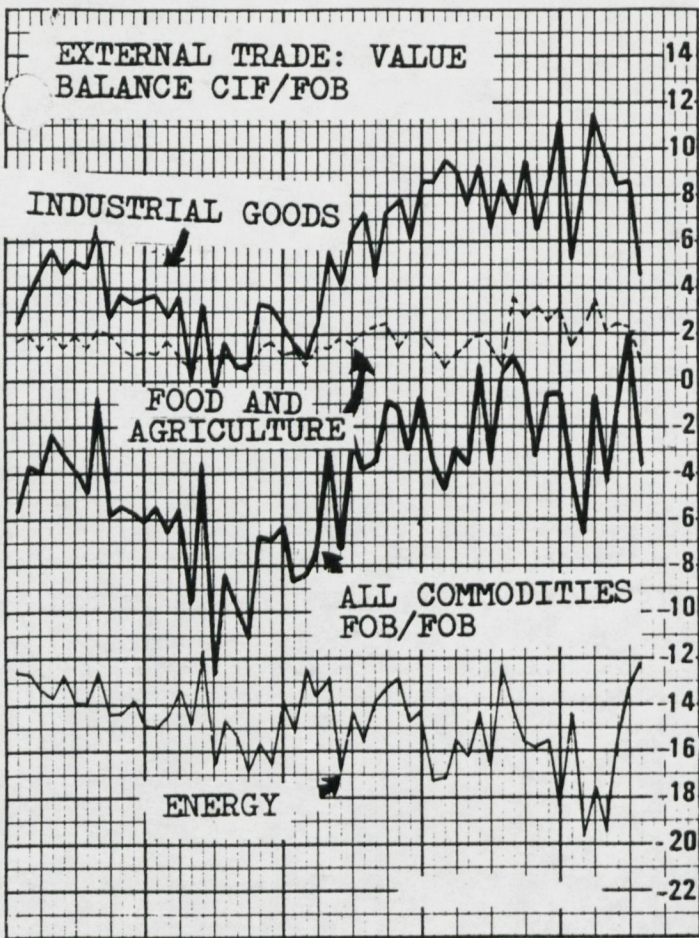


INSEE'S MONTHLY SURVEY OF INDUSTRIALISTS



INSEE'S MONTHLY SURVEY OF INDUSTRY (SEASONALLY ADJUSTED)





\* Le solde CAF-FAB est calculé avec les importations CAF (coût, assurances, fret) relevées directement par les Douanes. Le solde FAB-FAB s'obtient en prenant les importations FAB (franco à bord) qui sont calculées en appliquant un coefficient de 95,7 pour 1984 aux importations CAF. La "fabisation" des importations vise à les rendre homogènes avec les exportations qui sont, elles, toujours FAB. Ce calcul n'est valide que pour les importations globales. En chiffres bruts pour 1984 le solde CAF-FAB est de - 58,7 milliards de francs et le solde FAB-FAB de - 19,8 milliards de francs.