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THE FRENCH ECONOMY.

SUMMARY

1. THE FRENCH ECONOMY STILL BUOYANT, HAVING WEATHERED RECENT ELECTORAL UNCERTAINTY WITHOUT DIFFICULTY. GDP GROWING AT ANNUAL RATE OF AROUND 2.5 PER CENT, WITH GROWTH BETTER BALANCED. BUT INFLATION SLIGHTLY UP, AND UNEMPLOYMENT A CONTINUING WORRY. BALANCE OF TRADE ERRATIC BUT NOT TOO DISQUIETING. THE FRANC STABLE AND THE STOCK MARKET STRONG. THE ELECTED CHAIRMAN AND THE CHIEF EXECUTIVE OF THE BOURSE RESIGN AFTER REVELATIONS OF LARGE LOSSES AT THE END OF LAST YEAR IN THE BOURSE'S RESERVE FUNDS.

DETAIL

2. GOVERNMENT POLICY.
HAVING TAKEN THE RE-ELECTION OF PRESIDENT MITTERRAND AND THE APPOINTMENT OF A CENTRE LEFT GOVERNMENT IN THEIR STRIDE, THE FINANCIAL MARKETS HAVE REMAINED UNPERTURBED BY RECENT POLITICAL UNCERTAINTY. THE BETTING IS ON BEREGOVOY REMAINING FINANCE MINISTER IN A SECOND ROCARD GOVERNMENT WHICH IS LIKELY TO BE ESTABLISHED IN TWO WEEKS TIME, AND EVEN IF HE GOES, THE MARKETS JUDGE THAT THE PRAGMATIC AND MARKET ORIENTED POLICIES OF HIS FIRST MONTH IN OFFICE WOULD BE CONFIRMED BY ANY SUCCESSOR, THEREFORE ENSURING BROAD CONTINUITY FROM THE CHIRAC AND BALLADUR PERIOD.

3. THERE IS LITTLE DOUBT THAT THE BUSINESS AND FINANCIAL COMMUNITY WOULD PREFER BEREGOVOY TO STAY. HE WON RESPECT FOR HIS PRAGMATIC POLICIES AS FINANCE MINISTER FROM 1984-86. HE HAS COMMITTED HIMSELF TO FIGHT INFLATION, AND HAS REAFFIRMED BALLADUR'S COMMITMENT TO REDUCE THE 1988 BUDGET DEFICIT TO F115 BILLION: ADDITIONAL 1988 SPENDING OF F4.4 BILLION, MAINLY ON EDUCATION, EMPLOYMENT, RESEARCH AND OVERSEAS AID, WILL BE FINANCED BY HIGHER THAN EXPECTED REVENUES AND ECONOMIES FROM OTHER BUDGETS. HELPED BY A STABLE INTERNATIONAL ECONOMIC BACKGROUND AND A STRONG FRANC, HE HAS PUSHED INTEREST RATES DOWN SLIGHTLY. HE HAS ABOLISHED SOME OF FRANCE'S FEW REMAINING EXCHANGE CONTROLS.

4. AS EXPECTED, BEREGOVOY HAS SAID THAT THERE WILL BE NO RENATIONALISATIONS, OR FURTHER PRIVATISATIONS AT LEAST ON THE BALLADUR MODEL. BUT HE HAS SAID THAT HE WOULD ACCEPT INJECTIONS OF PRIVATE CAPITAL INTO EXISTING STATE ENTERPRISES, UP TO A MAXIMUM OF 49 PER CENT, WITH THE GOVERNMENT RETAINING OVERALL CONTROL. THE MOST LIKELY MECHANISM FOR THIS WOULD BE THE ISSUE OF CERTIFICATES OF DEPOSITS (IE NON-VOTING SHARES).

5. THE GOVERNMENT HAVE SAID THEY INTEND TO REINTRODUCE A WEALTH TAX, IN LINE WITH MITTERRAND'S ELECTION COMMITMENT, IN THE 1989 BUDGET TO COME BEFORE PARLIAMENT THIS AUTUMN. THE EXACT FORM IT WILL TAKE REMAINS UNCLEAR: ROCARD FAVOURS A WIDE BASE AND LOW RATE, BEREGOVOY THE SIMPLER AND QUICKER APPROACH OF RESURRECTING THE NARROWER BASED, HIGHER RATE TAX ABOLISHED BY THE RIGHT IN 1986.

6. THE ECONOMY.
THE ECONOMY REMAINS BUOYANT. GDP GROWTH FOR THE FIRST QUARTER OF 1988 WAS BETTER THAN PREDICTED AT 1.2 PER CENT, AND OFFICIALS TALK PRIVATELY OF A 1988 GROWTH RATE OF 2.5 PER CENT OR A LITTLE MORE. INDUSTRIAL PRODUCTION IN THE FIRST QUARTER WAS UP BY A STRONG 2.8 PER CENT. GROWTH ALSO LOOKS BETTER BALANCED: CONSUMER DEMAND IS WEAKENING, AND INVESTMENT AND EXPORTS STRONGER.

7. ON THE DOWN SIDE, INFLATION ROSE SHARPLY IN APRIL, (THOUGH THIS MAY HAVE BEEN DUE TO SPECIAL FACTORS) AND THE ANNUAL RATE HAS EDGED UP TO AROUND 2.5. PER CENT OR A LITTLE MORE. CAPACITY MAY HAVE BEEN REACHED IN CERTAIN SECTORS.

8. ALSO WORRYING FOR THE GOVERNMENT IS THAT WITH GDP GROWTH BUOYANT AND INFLATION EDGING UP, THE UNEMPLOYMENT PROSPECTS CONTINUE TO LOOK POOR. UNEMPLOYMENT (AT 10.3 PER CENT) ROSE SLIGHTLY IN APRIL, WITH A FURTHER SIGNIFICANT RISE LIKELY OVER THE SUMMER AS CURRENT SPECIAL PROGRAMMES LAUNCHED IN THE SPRING COME TO AN END. (THE LABOUR MINISTER, DELABARRE, HAS PROMISED A COHERENT PACKAGE OF TRAINING AND EMPLOYMENT MEASURES FOR THE AUTUMN.) OFFICIALS RECKON THAT GDP GROWTH OF BETWEEN 2.5 PER CENT AND 3 PER CENT IS NEEDED TO ABSORB THE ANNUAL 0.7 - 0.8 PER CENT GROWTH IN THE ACTIVE LABOUR FORCE: THE UNDERLYING UNMEMPLOYMENT TREND THEREFORE LOOKS AT BEST STABLE.

9. THERE WAS AN APRIL TRADE DEFICIT OF F2.1 BILLION, BRINGING THE 1988 DEFICIT SO FAR TO F6.4 BILLION. RECENT MONTHLY FIGURES HAVE BEEN ERRATIC, BUT THE ESTIMATE IS FOR A 1988 TRADE DEFICIT OF AROUND F20 BILLION, DOWN ON THE 1987 FIGURE OF F31.4 BILLION.

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10. THE FINANCIAL MARKETS.
THE BOURSE HAS HAD A GOOD FEW WEEKS, GAINING AROUND 10 PER CENT SINCE MID MAY. THE CAC INDEX REACHED A 1988 HIGH ON 9 JUNE. THE REPUTATION OF THE PARIS BOURSE WILL, HOWEVER, HAVE TAKEN A KNOCK WITH THIS WEEK'S RESIGNATION OF DUPONT, THE ELECTED HEAD OF THE NEW STOCK EXCHANGE COUNCIL AND COSSERAT, ITS DIRECTOR GENERAL. BOTH RESIGNED AFTER THE REVELATION THAT THE STOCK EXCHANGE RESERVE FUND ADMINISTERED BY THE STOCK EXCHANGE ITSELF HAD SUFFERED LARGE LOSSES AT THE END OF LAST YEAR THROUGH INJUDICIOUS TRADING ON THE MATIF (FINANCIAL FUTURES MARKET). CRITICISM HAS CENTRED ON THE FAILURE TO REVEAL THE LOSSES SOONER AS WELL AS ON THE LOSSES THEMSELVES.

11. PLEASE ADVANCE PS/CHANCELLOR, LITTLER, MATHEWS (TSY), LOEHNIS (B/E), BRAITHWAITE, RICHARDSON (FCO).

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