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EUROPEAN CENTRAL BANK

Europe’s Mixed Economic Fortunes Complicate Path for Stimulus

Sharp slowdowns in growth in France and the U.K. pose challenge to policy makers at ECB and BOE

Robots assemble Renault and Nissan vehicles at a factory near Paris. PHOTO: BENOIT TESSIER/REUTERS

By William Horobin and Paul Hannon
Updated April 27, 2018 10:41 a.m. ET

PARIS—Europe’s economies displayed mixed fortunes in the first three months of the year, injecting a fresh source of uncertainty as central banks consider further steps to withdraw crisis-era stimulus.

Figures released Friday on gross domestic product—the broadest measure of the goods and services produced in an economy—recorded sharp slowdowns in France and the U.K. But Spain produced steadily strong growth, while Austria and Belgium slowed only slightly.

At the same time, a European Commission survey showed business confidence stabilized in April, suggesting the slowdown in the early part of the year was caused by temporary factors such as poor weather and strikes. Indeed, economic forecasters surveyed by the European Central Bank have raised their growth forecasts for the year as a whole.

The mixed bag complicates deliberations at the ECB and the Bank of England, where policy makers are seeking clearer signals as to the underlying trend before deciding to proceed with reducing stimulus.

"The very first thing we have to do is understand exactly...whether it's temporary or permanent," ECB President Mario Draghi told a news conference Thursday. "Whether it's something that is...the beginning of a more significant decline or it's simply normalization after a prolonged period of very strong growth."

France's Insee statistics agency Friday said GDP increased at less than half the pace recorded for the final three months of last year.

But the Spanish economy didn't appear to encounter similar obstacles, with growth continuing at the rapid rate recorded at the end of last year. And Austria's economy also sustained a strong expansion. Because the French economy accounts for a fifth of all activity in the eurozone, that points to a slowdown in growth across the currency area as a whole.

The U.K. economy barely grew at all as it recorded its slowest expansion in more than five years. The pound fell in response to the weak growth figures as investors considered it less likely that the BOE would raise its key interest rate next month. As elsewhere in Europe, a cold-weather system known locally as "the Beast from the East" had a role in the sharp slowdown as construction slumped, but policy makers will also be alert for any signs of a more durable loss of momentum.

"The chance of a May rate hike is now close to zero," said Samuel Tombs, an economist at Pantheon Macroeconomics.

In France growth in business investment slowed sharply while consumer spending—the traditional motor of France's economy—grew at an unchanged, but modest pace. And there were signs the headwinds to growth won't be removed quickly.

French businesses say President Emmanuel Macron's election on an overtly pro-business platform and his speedy action to decree changes to labor laws awakened so-called animal spirits. That, combined with the cuts to payroll taxes by the previous government, set the conditions for businesses to catch up on years of delayed investment and hiring.

But many French companies now warn they are struggling to keep pace with demand as they lack capacity and skilled workers. Capacity utilization rates are at decade-highs over 85% and 42% of employers in manufacturing are reporting difficulties recruiting, recent statistics show.

At machine component manufacturer Redex, 60 miles south of Paris, chief executive Bruno Grandjean extended deadlines for many orders to 14 weeks from eight weeks previously and put his 250 staff to work overtime and Saturdays to try to match strong foreign demand. But that system has reached a limit as it becomes too difficult to manage recuperation days and there are legal limits on overtime. It takes time, Mr. Grandjean says, to hire and train new staff.

Redex also urgently needs new machinery. Instead of buying a new machine, Mr. Grandjean hopes to get a second hand-machine sooner, but even then it may not arrive until September.

“French industry is a bit like a burned forest. To replant an industry and grow our businesses we need time,” Mr. Grandjean said.

Bottlenecks are also appearing in services as employers lack workers with top qualifications. As French employers scramble to recruit, they are increasingly turning to recruitment firms. Revenues at OpenSourcing, a firm in the Paris region, are up 40% in the first quarter after a 30% increase last year, says Chief Executive Sebastien Canard. In some sectors, like business development, the shortage of skilled workers is pushing up starting salaries by as much as 20% compared with 2016 in some areas. That makes it difficult for some companies to adjust.

“We have to explain to companies that recruiting in 2018 is nothing like in 2015 and 2016,” Mr. Canard said.

—David Hodari in London and Tom Fairless in Frankfurt contributed to this article

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Corrections & Amplifications
OpenSourcing Chief Executive Sebastien Canard said: “We have to explain to companies that recruiting in 2018 is nothing like in 2015 and 2016.” An earlier version of this article incorrectly attributed the quote to Redex CEO Bruno Grandjean. (April, 27)