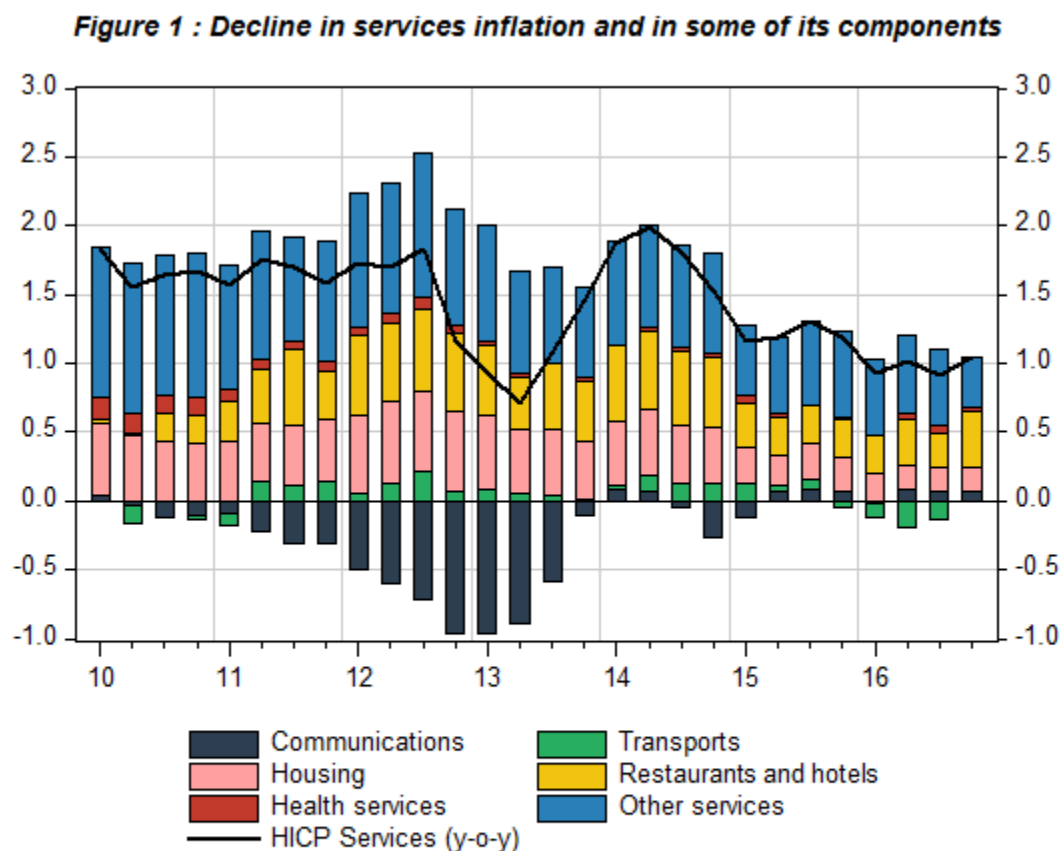


Services prices in France and oil prices

By Louis de Charsonville and [Caroline Jardet](#)

Services price inflation in France stood at 1.0% in 2016, well below its average from 1999 to 2015 (around 2%). This paper looks at the mechanisms through which the fall in oil prices and lower headline inflation have contributed to slowing services prices since mid-2014. An analysis of these interactions suggests that services price inflation will begin to recover as of 2017, to around 2%.



Contributions to the year-on-year trend in the quarterly average of the "services" component of the Harmonised Index of Consumer Prices.

Sources: Insee, authors' calculations

The “services” component of the Harmonised Index of Consumer Prices (HICP)¹ represents 44% of the total index. It includes all services for consumers, covering a variety of services including transport, communications, housing, healthcare, restaurants, etc.

As an annual average, services price inflation was 1.0% in 2016, after 1.2% in 2015. In February 2017, it stood at just 1.1% year on year. This growth rate is well below the average of around 2% recorded between 1999 and 2015.

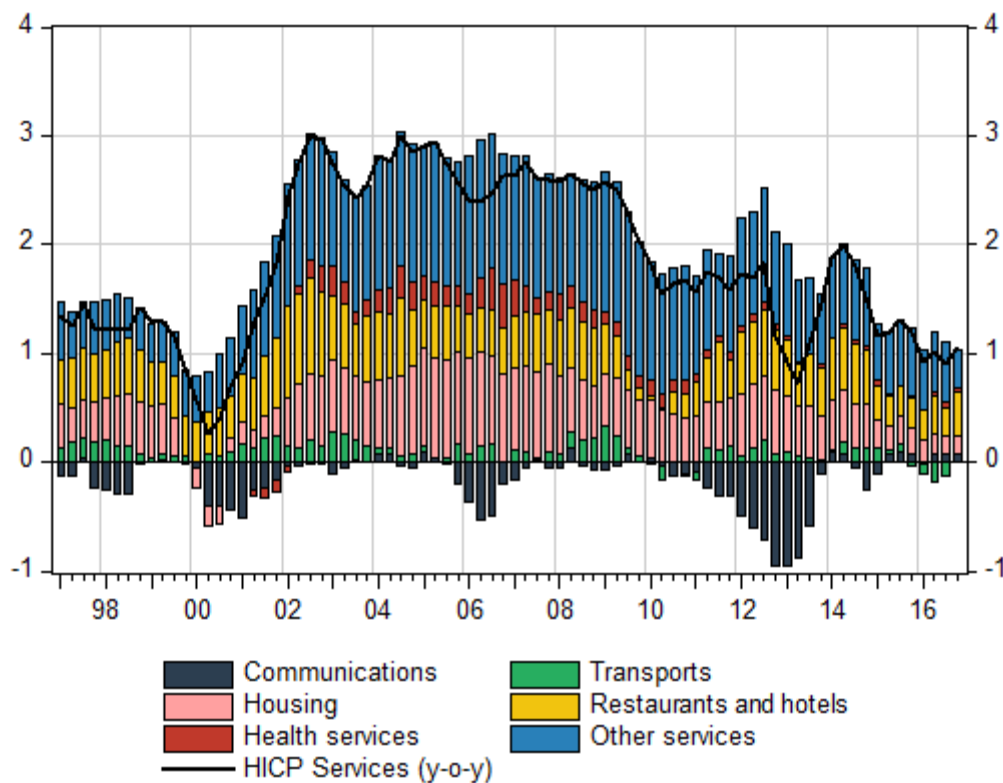
The slowdown concerns most of the components of services prices

Two periods of very low services price inflation have been recorded in the past twenty years: (i) in 2000, services inflation dropped to 0.6% (after 1.2% in 1999); (ii) in 2013, it dropped to 1.0%, mainly due to lower communications prices linked to the arrival in the market of new mobile telephone operators in 2012.

The present situation differs from that of 2013 as there has been a generalised slowdown in prices in several sub-components of the “services” HICP and it is not solely the result of lower communications prices. Figure 2 shows the contributions to the HICP of the six services sub-components. A comparison of the trends in 2012 with those of 2016, to avoid using 2014, which was marked by a rise in VAT rates, and 2013, which featured the fall in communications prices, shows a strong slowdown in prices in three of the six categories: “housing”; “transport” and “other services”, which includes repairs, cleaning services, hairdressers, etc. Between Q1 2012 and Q4 2016, services inflation slowed by 0.7 percentage point (pp). The decline in inflation in these three categories contributed -1.1 pp to this decrease.

Figure 2: Decline in services price inflation and in several of its components

¹ For HICP, see [Insee definition](#)



Contributions to the year-on-year trend in the quarterly average of the "services" component of the Harmonised Index of Consumer Prices.

Source: INSEE, authors' calculations

How is this linked to the fall in oil prices?

The price of crude oil per barrel has halved since mid-2014. Despite rising slightly since the beginning of 2016, oil prices are still low. Through which mechanisms do these oil shocks feed through to services prices?

- *A direct impact on transport prices:*

This direct impact on the "transport" sub-component can be seen in Figure 1, where its contribution to services inflation turns negative as of the end of 2015. The "transport" sector includes air transport (40% of this sub-component and 2% of the entire services sector) whose prices are linked to oil prices, with a time lag of a little over one year.

- *An indirect impact through the fall in headline inflation:*

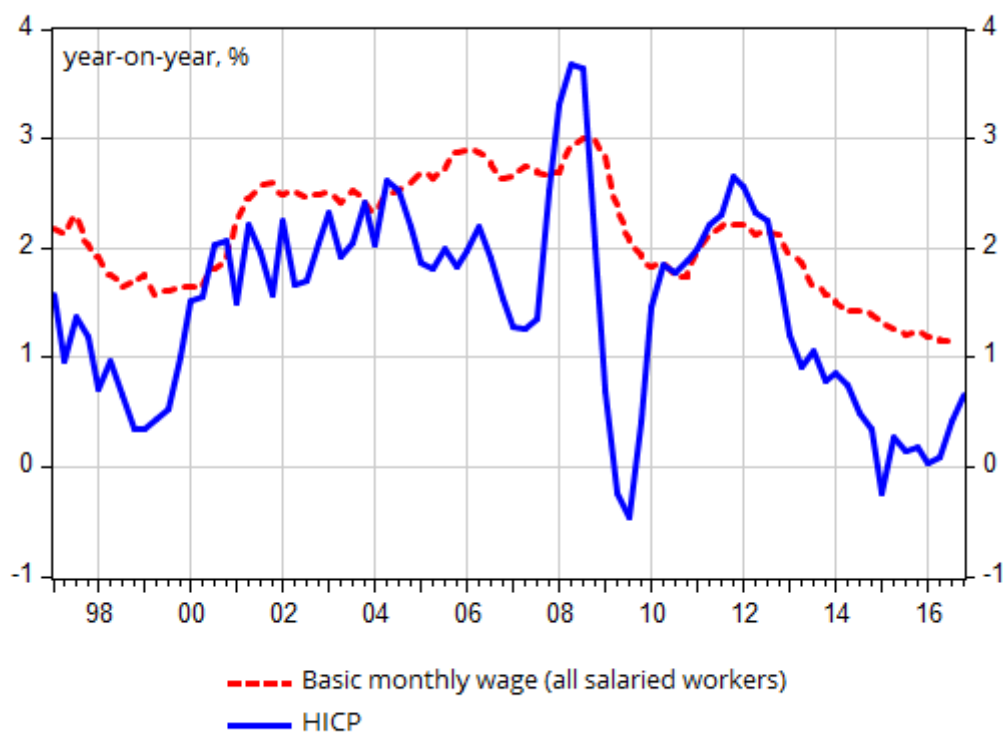
The slowdown and subsequent fall in oil prices has contributed to the fall in headline inflation ([Box 3, economic projections, June 2016](#)). Moreover, the deceleration and then decline in the price of imports excluding energy has also favoured disinflation, in particular

by dragging on the prices of manufactured goods. Headline inflation was 0.1% in 2015 and 0.3% in 2016.

The fall in headline inflation affects services prices through two channels:

- On the one hand, disinflation has repercussions on rent prices through the Rent Reference Index (Indice de Référence des Loyers - IRL). The IRL sets the ceiling for annual rent reviews by property owners. As the IRL is indexed to the previous year's headline inflation (excluding tobacco and rent), the fall in inflation of the past few years has resulted in lower rent inflation.
- Also, in a context of high unemployment, lower inflation has favoured a slowdown in wage growth. There are close links between inflation and wage costs, known as the wage-price spiral (see Figure 3). The decline in wage inflation more particularly affects labour-intensive segments, such as "restaurants and hotels" and "other services".

Figure 3: Headline inflation and wage inflation



Source: INSEE/DARES, authors' calculations

Apart from the fall in headline inflation since 2014, two other measures have undoubtedly contributed to slowing labour costs. The Tax Credit for Competitiveness and Employment or CICE, paid as from the beginning of 2014, may have resulted in a reduction in labour costs through the impact of production subsidies. The same can be said for the reduced employer social security contributions introduced by the Responsibility and Solidarity Pact (PRS) as of

the beginning of 2015. The reduction in labour costs could have apparently led to moderation of services prices.

Services inflation should pick up by 2019

According to [Banque de France's revised economic projections](#), services inflation should recover by 2019.

Assuming a recovery in oil prices, these will cease to have a negative impact on headline inflation and in particular on transport price inflation. A rise in labour-intensive services prices will be boosted by a gradual recovery in wage growth and improved macroeconomic conditions. Lastly, in conditions of stronger inflation, rents should once again begin to accelerate.

Under these conditions, services price inflation is likely to remain low in 2017, but should rise to 1.8% in 2018 and 2.0% in 2019.