

France after Lecornu: What's next?



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"Prolonged political uncertainty is weighing on household confidence and domestic demand, highlighting the economic risks ahead."

- **Prime Minister Lecornu's resignation** amid opposition from both the left and right has ushered in a new phase of political uncertainty. President Macron faces the choice of appointing a new Prime Minister or dissolving the National Assembly to call snap elections. Either way, France will have a budget for 2026: its Constitution provides procedures to avoid a US-style shutdown.
- **Despite political fragility and mildly widening government bond spreads, demand for French debt remains robust.** France benefits from a large, liquid bond market, a historically low average cost of debt, extended debt maturities, and a strong tax collection capacity. The European Central Bank (ECB) holds a significant share of French debt, and recent rating downgrades have had a limited impact on investor appetite, reflecting confidence in France's financial stability.
- **The political uncertainty has weighed on the French equity market**, particularly in domestic stocks, while the impact on European equity indices has been limited. **The French market already prices in political risk and, with around 80% of its capitalisation export-oriented, it is expected to remain relatively resilient** despite ongoing uncertainty. However, prolonged political instability could weigh on household confidence and domestic demand, as evidenced by rising savings rates, further impacting the most domestically oriented segments of the market.

Policy uncertainty is back, following Prime Minister Lecornu's resignation

PM Lecornu's resignation follows opposition from both left and right parties regarding the composition of his government, which was announced on Sunday evening. As was the case when the Bayrou government fell, President Macron now has two options: he can

- 1) Either appoint a new PM or
- 2) Dissolve the National Assembly and call snap elections.

Some voices (La France Insoumise (LFI) and Rassemblement National (RN)) are calling for the President's resignation. However, this last option is highly unlikely, as President Macron has repeatedly stated his intention to respect the institutional calendar (presidential elections are scheduled for April/May 2027, at the end of his second term). Recent polls suggest that, in the event of snap elections, the far right could maintain its lead with 32% of the vote, while the centre-right bloc would lose seats. Initially, therefore, the president will likely be tempted to appoint another PM (technocratic government or a PM from the Republican / Socialist party or even from RN). However, given the successive failures of his predecessors, the chances of success for a new PM are fairly slim. Against this backdrop, **the likelihood of snap elections seems high; the question is when they will be held.** Elections must be held at least 20 days and no more than 40 days after dissolution (Article 12 of the Constitution). In 2024, for example, the dissolution of the National Assembly was announced on 9 June, with elections held 3 weeks later on 30 June and 7 July.

In any case, there will not be enough time to adopt the 2026 budget before the end of the year, as required by the Constitution. However, last year's events (following the fall of the Barnier government) showed that the Constitution provides procedures to avoid a shutdown, as happens in the US (see box). Conversely, there is a risk of a prolonged period of political inertia at a time when clear decisions are needed.

The precedent of 2025: how an institutional crisis was avoided last year

On 10 December, the Council of State issued an opinion on the interpretation of Article 45 of the 'organic law on finance laws' (LOLF). This article allows the government to propose a special bill to ensure the continuity of national life and the regular functioning of public services in 2025. This is in the event that Parliament does not adopt the Finance Act for the year before 31 December, and it is not possible to enact a Finance Bill before this date.

The Bill was presented to the Council of Ministers on 11 December and adopted by the National Assembly on Monday 16 December (481 votes in favour, 0 against). On 18 December, the Bill was adopted by the Senate (345 votes in favour, 0 against). The special law was promulgated by the President of the Republic on 20 December 2024.

This law does not replace the budget and was intended to manage a temporary situation until the Finance Law was adopted in 2025. Its scope being strictly limited, it authorised the collection of necessary taxes and public resources to finance essential public expenditure.

From an economic standpoint, it is clear that a prolonged period of uncertainty would weigh on household confidence and business climate. Indeed, in Q2 2025, the household savings rate reached its highest level since 2021, a trend not observed elsewhere in the Eurozone. This shows how much political uncertainty is affecting domestic demand.

Investment implications

Fixed Income: there is a political crisis but no financial crisis

Lecornu's resignation opens a new phase of political crisis. Volatility on spreads is expected.

The resignation of the appointed Prime Minister Lecornu sparked some volatility in the bond market, with the 10-year OAT-Bund spread reaching 86 basis points. The French budgetary situation is perceived by the markets as a manageable risk, but one that is more enduring. The French 10-year yield is close to 3.5%, marking its highest level since 2011. These levels can be seen as the new norm. It illustrates an immediate political fragility, due to the difficulty in forming a new government, and a structural budgetary drift driven by high public spending and sluggish economic growth.

France continues to raise debt easily.

Demand for French debt remains strong. Political uncertainty is forcing France to pay more to place its debt, yet it continues to be able to raise debt without difficulty.

Who buys French debt? A quarter of the debt is held by domestic actors, a quarter by the Bank of France, a quarter by Eurozone residents, and a quarter by residents outside the Eurozone.

According to the latest data from the Bank of France, in the first quarter of 2025, 54.7% of the state's negotiable debt is held abroad by "non-residents", including in Eurozone countries other than France. This proportion has even increased over the past four years, as debt held by foreign investors was 48.5% at the beginning of 2022.

Positive points of French government bonds:

- The impact of rising rates on the state's debt burden will materialise gradually.
- France, like all Eurozone countries, has benefited from very low and even negative interest rates to finance itself throughout the 2013-2021 period, which have enabled it to improve its financial profile: manifested by (1) a decrease in the average cost of its debt. The average cost of debt is around 2% after reaching a low of 1% in 2021. Before 2010, the average rate was between 3% and 5%; and (2) an extension of the average maturity of its debt from 6 years to 8.6 years. As a result, the debt burden as a proportion of GDP is around 2.1% in 2023, significantly lower than levels observed in 2010.
- It is one of the most liquid and deepest markets in the Eurozone, thus part of the preferred markets for foreign investors.
- Strong capacity of France to collect taxes. Solvent households with solid balance sheets.
- The ECB: A quarter of French debt is held by the ECB.

The bond market did not react to a recent rating downgrade, which only had a limited impact on the demand for bonds from banks and insurance companies.

Equity market: Some volatility is back

The initial intraday reaction of the CAC40 Index has been negative but not brutal, with a slightly sharper correction for the CAC Small Index. Domestic stocks, such as banks, are subject to some profit-taking. The reaction has been limited to the French market, with other European indices showing little movement. At this stage, the event is implicitly interpreted as being domestic rather than systemic; political and not financial.

Some caution is warranted in the short term, but the French market already factors in a risk premium linked to political uncertainty; so far this year, it has failed to break through its 2024 highs, unlike most other European indices, notably the Eurostoxx50, the Dax, the Ibex and the FTSE/MIB. At 15x 12-month forward earnings, it is trading in line with its 12-year median, as is the MSCI Europe. Moreover, around 80% of the flagship Index's market capitalisation is export-oriented, which should limit the negative impact.

"A new phase of political crisis is leading French government bond spreads higher. Yet, French debt continues to attract investors thanks to its size, liquidity and resilience due to its relatively low cost of debt."

"With political uncertainty priced in and a largely export-driven market, the French equity market is expected to remain resilient."

Amundi Investment Institute

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Definitions

- **Volatility:** A statistical measure of the dispersion of returns for a given security or market index. Usually, the higher the volatility, the riskier the security/market.

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