

## PREVIEW: French no-confidence vote looms, what next?

- On Wednesday, 4th December at 15:00GMT/10:00EST a no-confidence motion in PM Barnier's gov't will be held, a motion Barnier is expected to lose.
- Thereafter, the next step goes to President Macron who could call a Presidential election (has said he won't) or attempt to find another PM to form a majority around to deliver fiscal reform.
- Candidates for the role haven't been forthcoming as they know they are unlikely to be able to form a working gov't and pass the necessary fiscal reform. As such, we look for signs of a compromise between Macron's centrists and left-/right-wings of parliament.

### Monday

- PM Barnier put forward the social security element of the 2025 budget to parliament, knowing this wouldn't pass despite making concessions to Le Pen's RN on two of their three main sticking points, Barnier did this via Article 49.3.
- Usage of this means the measures passes without vote, but opens the gov't up to a confidence motion being called within 48hrs. As expected, LFI (part of NFP) on the left and RN on the right both put forward a motion almost immediately.
- The session saw the CAC 40 close at the unchanged mark after underperforming in the first half of the session. The OAT-Bund 10yr yield spread peaked at 87.8bps while EUR/USD hit a 1.0459 trough, pressure also a function of strong US data.

### Tuesday

- The National Assembly has decided to hold the confidence motion on Wednesday, December 4th at 15:00GMT/10:00EST. A motion which Barnier is all but certain to lose given that the left-wing coalition (192 seats) and RN (140 seats) are both expected to vote against the PM, which gets them to 332 seats and far in excess of the 289 absolute majority mark and Barnier's own Ensemble coalition (164 seats).
- As a side note, the French parliament has agreed on a version of the end-of-management bill which provides a final budget figure for 2024 and allows the current calendar year to conclude without fiscal issue.
- As it stands, the CAC 40 is firmer on the session with gains of 0.4% but does lag broader benchmarks slightly i.e. Euro Stoxx 50 +0.7%. OAT-Bund 10yr yield spread peaked at 87.9bps but has since tightened significantly to as low as 83.4bps while EUR/USD is back above 1.05 (USD is broadly softer vs. peers).

### Wednesday

- At 15:00GMT/10:00EST France's parliament will begin to vote on the confidence motion.
- In the unlikely scenario that Barnier wins then the social security element of the budget, with two of the three requested RN concessions included, will be implemented and will work to resolve the fiscal crisis in France and bring the debt-GDP ratio back towards the Commission's 3% mandate. Such a result would be seen as a near-term market positive, likely tightening the spread and bolstering assets that have been pressured as the French turmoil heightened. However, Jefferies notes that in this scenario they would use the bond recovery to add to its short position given supply concerns next year.
- If Barnier loses then the next step goes to President Macron who will need to appoint a replacement.
- French-assets and the EUR have been under pressure in recent sessions as the prospect of a confidence vote heightened. While Barnier is expected to lose, the confirmation of this outcome could well spark renewed pressure and a further widening of the OAT-Bund 10y yield spread (90bps last week's 12yr peak), CAC 40 pressure and downside in the EUR.

### Market Reaction

- Reaction centers on heightened political uncertainty/instability and the prospect that France will not make progress towards reducing its budget deficit as required by the Excessive Deficit Procedures the EU Commission put it under earlier in the year. Procedures enacted based on a 5.5% debt-to-GDP ratio in 2023 A ratio which is expected at around 6.1% in 2024 according to the Bloomberg forecast and then falling to 5.0% in 2025; significantly above the 3% level the Commission demands.
- As above, Jefferies has retained a structural short position on OATs due to supply concerns and political uncertainty and would use any rally on the survival of Barnier as an opportunity to add to the short position. Jefferies' Kumar writes "Our worry remains in the first quarter when increased net supply hits the markets and Asian investors are not willing buyers of French bonds."
- Citi takes the view that it is difficult to see the spread tightening, highlighting Thursday's upcoming auction as an additional challenge; France to sell EUR 3-5bln 4.0% 2038, 0.5% 2040, 1.5% 2050 0.5% 2072 OATs. Citi writes that while the pace of widening may slow down after Monday's events, it looks unlikely to reverse in the coming months.
- Much of the concern around France has been that it could spillover into a broader EZ crisis, of the like sparked by the periphery over a decade ago. Thus far, peripheral spreads to Germany haven't widened in-tandem with the OAT-Bund moves and in fact the French 10yr yield remains very close to its Greek counterpart after eclipsing it last week and on Monday. Within a John Authers article on the subject, BCA Research is quoted as saying "The good news is that the periphery is not infected", however, Tigress Financial's Ergas cautions that the problem "is yet more chipping away at the euro zone, its credibility, and the role of the euro as a reserve currency."
- For the Euro, ING has an end-2024 EUR/USD target at 1.05 but with risks skewed to the 1.02/03 region.
- In terms of assessing any medium-term reaction, it is worth considering the tense political backdrop in Germany ahead of their own early-2025 election and also the bleak growth outlook for the bloc as a whole with ECB pricing currently implying 160bps of easing before the cycle concludes.

### Rating Agencies

- We haven't heard from agencies since last Friday when S&P affirmed France at AA-, outlook stable. Likely as they are awaiting a resolution of the confidence motion before commenting. In the wake of recent price action, ING writes "French 10y spreads over swaps are more in line with an "A-" rating rather than its current "AA-" – three notches lower.". Note, if France was cut into single-A territory then it could have significant ramification, highlighted by Rabobank who wrote that they spoke to a large multilateral in recent weeks who stated they would be forced to liquidate their exposure to France in such a scenario.

### Wednesday Onwards

- Macron is unlikely to be able to immediately appoint a successor, not least because he is out of the country until late-

Wednesday/early-Thursday, as such Barnier may well be asked to remain as caretaker. During this period, Barnier could enact special legislation to rollover the 2024 budget for a period of time (wouldn't solve the fiscal crisis) or could use a gov't order to force the legislation through.

- In the latter scenario as caretaker Barnier wouldn't be able to deliver the budget so Macron would have the unenviable task of finding a PM accepted by a majority and one who is willing to deliver the tabled budget. Even if this was attained, passing the budget by majority in its existing form is highly unlikely.
- As such, Macron will have to try and find a PM candidate who a majority can be formed around. It remains to be seen if they will give in to the right-wing's final red line, and if RN would be receptive at this point. Or, if Macron will attempt to draw support from NFP on the left. As a reminder, NFP came out on top but shy of a majority in June's election and pledged to call a confidence motion against Barnier as revenge to Macron not appointing a NFP candidate as PM.
- From the NFP, Socialist Party leader Olivier Faure has said he does not want/wish for Macron to resign, but looks for him to appoint a left-wing PM.
- As a reminder, the next election cannot occur until July 2025 under the French constitution.
- In terms of potential candidates to be the next PM, French press is quite light on suggestions with key members of the Assembly not wishing to come forward as they know that they are very unlikely to be able to form a working government and pass the required fiscal measures. As such, compromise is likely required; it just remains to be seen if that will be to the left, as the likes of Faure have called for, or to the right as Barnier attempted but failed to manage successfully.

### Macron's Position

- Given rhetoric from Le Pen after the confidence motion was called, it appears as if her intention has been to put pressure on Macron to call for Presidential elections earlier than the current 2027 schedule. Note, Le Pen is currently under investigation in France over alleged embezzlement of EU funds, a verdict on this is expected on March 31st 2025. If found guilty Le Pen could be banned from running for public office (incl. Presidency) for a five-year period. Overall, it appears Le Pen is trying to push Macron into an early Presidential election in order to be in power before the verdict is delivered.
- As it stands, there is no indication that Macron will call an early Presidential election. He has been clear in commentary in recent weeks that he has no intention of doing so and while he hasn't spoken on the matter this week, there is nothing to believe this narrative has changed. As a reminder, Macron cannot partake in the next Presidential election as he cannot run for a third consecutive term.

### Presidential Election

- If a Presidential election was called, then Le Pen would almost certainly be the right wing candidate (dependent on the timing and above legal proceedings) and, according to polls for the 2027 election, would win the first round with 35-40% of the vote. Note, under the French system if a candidate gets an absolute majority (i.e. >50%) in the first round then the election ends and they are appointed President.
- If not, then the process moves onto a second round which would be between the top two candidates from the first round. Polling currently indicates that this would be between Le Pen and Edouard Philippe, who was the PM under Macron during 2017-20. A runoff Le Pen would likely win.
- However, the prospect of this being the second round is more a function of the left-wing NFP alliance not standing behind one candidate with numerous names theoretically contenders. Polling on a concerted left-wing contender vs Le Pen is unfortunately sparse.

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