

French elections - a noisy non-event

No clear winner. The worst might have been averted from a (European) perspective, while from a French perspective some uncertainty will persist until a government emerges.

IN A NUTSHELL

- Having failed to produce a clear winner has positive and negative implications. Positive: markets will appreciate that no alliance with more extreme positions gained a majority. Negative: having no clear winner means incertitude will persist as French parliamentarians have little experience in being governed by formal or informal coalitions.
 - On Sunday, Macron's Ensemble was stronger and Rassemblement National weaker than expected and within the left wing alliance Nouveau Front Populaire we saw a shift towards more centrist legislators. This means that there is no clear opposition to Macron's pro-European course.
 - Markets will find it hard to immediately make something out of these results as at first, no radical shift from current politics is to be expected. It remains to be seen whether Macron acknowledges that voters haven't voted for him, but against le RN.
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Evolution, not revolution

Assessing the outcome of the second round of the French general election from a market perspective probably depends on two things: 1: your chosen point of reference: France 2 years ago, France 2 months ago, France after the European election, France after Emmanuel Macron's surprising call for snap elections, France after the first round of elections on June 30 or France according to pollsters last Saturday. 2: your investment horizon. Concerning the first point: without doubt, the peak of incertitude was the day Macron called for snap elections, and the speed at which a left alliance has been built and the results of Rassemblement National (RN) didn't really help soothe the fears. So, judged by what some market participants believed could have happened, the results of yesterday's election could be described as: the worst has been avoided. One could even make the case that the electorate has shown a renewed preference for the political middle ground. Medium term, however, French politics now has become slightly less predictable as it seems that without a clear majority of any single party or alliance, the Assemblée Nationale will try to find new ways of governing itself – and the country. And the RN is unlikely to feel less emboldened to further pursue national political powers.

Digging deeper into the results we find that far from winning an absolute majority of 289 or more seats in the AN, Marine Le Pen's RN has come in third (143 seats), roughly half of what that some of Ms. Le Pen's more enthusiastic supporters hoped for and market participants had feared (though a significant, and unprecedented advance compared to the far right's performance in previous elections). Instead, the winning block turned out to be the Nouveau Front Populaire (NFP), on track towards securing about 182 seats, i.e. also more than 100 seats short of a majority. Emmanuel Macron's Ensemble looks set

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to finish between the two, at 168 seats. Finally, other, mostly center-right candidates who refused to ally themselves with the RN appear on track to win about 65 seats, leaving aside other independent and minor party candidates hard to categorize.¹

Superficially, such a fragmented political landscape might make France appear ungovernable, in particular given the NFP program to introduce such leftwing measures as re-introducing automatic indexation of wages to inflation, restoring wealth taxes and reducing the pension age back to 60 years, after it has just been raised to 64. It is worth keeping in mind, however, that the only reason Ensemble finished as well as it did was that plenty of left-wing voters supported it tactically to avoid RN victories in the second round. Conversely, some, if not quite as many centrist voters appear to have voted tactically for NFP candidates, especially where more moderate ones stood. Partly as a result, the NFP parliamentary bloc will be dominated by moderate forces from the Socialist Party and the Greens, rather than far-left firebrand Jean-Luc Mélenchon.

Finding compromises in the AN is likely to require looking beyond Paris and paying closer attention to La France profonde (the French heartland of provincial towns and villages), while largely keeping intact while selectively improving upon the Macron reforms of recent years should be possible, even if they take a bit of time to materialize. In any case, following the resignation of Gabriel Attal, President Macron is free to nominate whomever he wants as prime minister², who will be in office (and have the full powers of a PM under the constitution) until 2027 and as long as there is no majority against him or her in the AN. For market participants and European allies still worried about the RN ahead of presidential elections in 2027 (which also feature two rounds), it may also be reassuring that for now at least, French voters were willing to turn out in unusually large numbers to prevent just such a far right take over in 2024.

Little to chew on for markets

While markets don't like uncertainty, they normally have no major problem with a developed country having split power, as this regularly curtails big spending programs. At the same time, France is set to produce a budget deficit of more than 5% this year and the European Commission has initiated an Excessive Deficit Procedure (EDP) against France on June 19. S&P had downgraded its rating for France already in May. With the debt to GDP expected to rise further despite optimistic growth forecasts, markets will certainly pay closer attention to how any new government will interact with the European Commission on the EDP issue.

On Monday morning we have seen some relief on markets, as the CAC40 almost moved in line with other European stock markets (slightly up) and French government bond spreads versus German Bunds slightly declining, although still trading above the levels seen before the snap elections were called.

¹ All figures taken from lemonade.fr. The results of the 2024 legislative elections as of 7/8/24; 11:00am

² The fact that Macron asked Gabriel Attal to "stay on for the moment" does not mean he won't elect a different PM any time soon.

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Glossary

A **budget deficit** is created whenever the spending in a public budget exceeds the income within a given time period

Bunds is a commonly used term for bonds issued by the German federal government with a maturity of 10 years.

The **CAC 40** is a French stock-market index, representing the 40 most significant values among the 100 companies with the highest market cap on the Euronext Paris.

The **European Commission (EU Commission)** is the executive body of the European Union (EU) which represents the interests of the EU.

The **gross domestic product (GDP)** is the monetary value of all the finished goods and services produced within a country's borders in a specific time period.

Inflation is the rate at which the general level of prices for goods and services is rising and, subsequently, purchasing power is falling.

S&P 500 is an index that includes 500 leading U.S. companies capturing approximately 80% coverage of available U.S. market capitalization.

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