French political uncertainty weighs

2 December 2024

Overview

- A motion of no-confidence could be triggered
- French budget & government may be voted down
- French consumer & business sentiments to be hit
- French-German yield spreads may widen further
- We are cautious of French risk assets
- German bunds could outperform equities
- Prefer risk assets in other regions to the Euro Area
- Within EU, look to sectors riding on secular trends
- EUR to weaken through 1H 2025, stabilise in 2H 2025

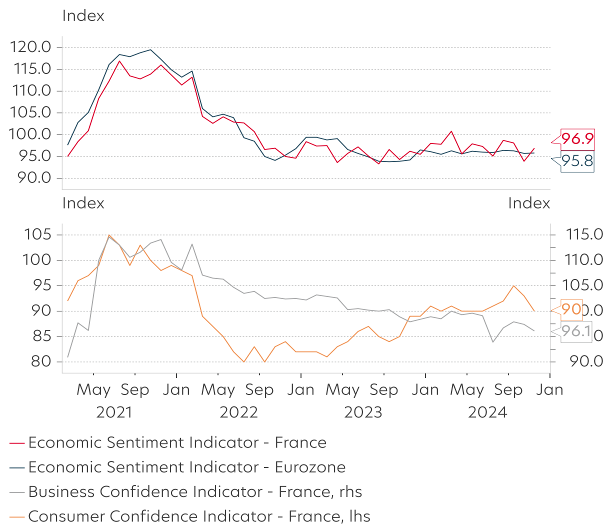
Quick take: French political uncertainty weighs

For context, the coming weeks will be key for France's 2025 budget and the government led by Prime Minister Michel Barnier. The budget bill is discussed at the house. The process involves the lower and upper house, with the former having the last word.

The French government has weak support in the lower house and thus, is likely to bypass it by using article 49.3 of the constitution. In this case, the budget bill would become law unless the members of Parliament (MPs) trigger a motion of no confidence. If a majority of MPs vote in favour of it, the budget bill would be rejected, and government shutdown occurs.

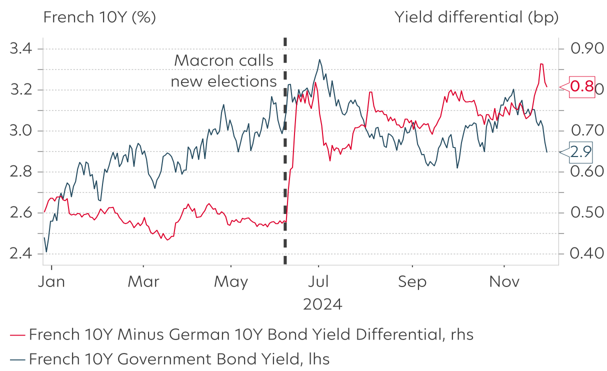
As at writing, according to a Bloomberg article, Marine Le Pen of the far-right party, National Rallies (RN), has provided strong indications that she is prepared to topple the French government as soon as this week, given that "the government has expressed its wish" not to modify the social security bill as proposed by the far-right leader. French Finance Minister Antoine Armand said the government does not take ultimatums, and will not accept artificial budget deadlines from Marine Le Pen.

Figure 1: Languishing French sentiments



Source: Bloomberg, UOB Private Bank

Figure 2: French 10Y yield & spread over Germany



Source: Bloomberg, UOB Private Bank

French budget and government to be voted down?

There is a significant risk for the budget and the government to be voted down together. Having no budget before 2024 ends would be manageable as the 2024 budget would be carried forward. However, this scenario brings forth heightened political uncertainty as well as fiscal slippage. This would broadly impact already lacklustre business and consumer sentiments **(Fig. 1)**, as well as lead to further sovereign bond spread widening **(Fig. 2)**. Market participants are focused on whether the budget can pass or if the government will fall; the results are linked through whether a no-confidence vote will go through. Looking ahead, rising political uncertainty points to downside risks for growth next year.

French political uncertainty weighs

2 December 2024

What it means for markets

France

Political challenges will remain at the forefront going into 2025. The odds of a government shutdown are rising, while new lower house elections may only be triggered next summer (as Macron must wait a year a call a new election). Meanwhile, clarity on US tariff actions will likely take time to materialise.

While improved financial conditions could support growth next year, significant fiscal consolidation would likely leave France's GDP growth weak. Household savings rate stands at 18%, which is above the regional aggregate. However, weak sentiments point to muted household spending, especially in a highly uncertain political environment. On the upside risk, the fiscal budget may eventually prove to be less restrictive than expected, while the sentiments and growth may be boosted once the political uncertainty fades. We are cautious of French risk assets.

Euro Area

We expect some negative spillovers in terms of investor sentiments, which suggests higher market volatility in the near term. Companies with material sales exposure in France may be impacted. The French to German 10Y yield differential could stay elevated until the French political uncertainty is lifted.

Germany

The economy is squeezed by a lingering energy crunch, weak Chinese demand but intense competition, as well as fiscal austerity. German bunds could outperform equities. Overall, we prefer risk assets in other regions to those in the Euro Area. Within the Euro Area, we continue to prefer peripheral regions including Spain, as well as sectors riding on structural themes or trends (e.g., aerospace defence).

Currencies - EUR

Our house forecast is for EUR/USD to weaken to 1.02 in 1Q 2025, and 0.99 in 2Q 2025, before a recovery to 1.03 by the end of 4Q 2025 (as at 28 November 2024). This reflects the domestic pressures, as well as external headwinds faced by the Euro Area. Economic risks are tilted to the downside, with France and Germany unlikely to be able to support Eurozone growth amid the political quagmire. The European central bank (ECB) is projected to cut rates by 25bp each quarter for 2025, following a 25bp interest rate cut when policymakers convene on 12 December for the final time this year (as at 28 November 2024).

Disclaimer

General
This document contains material based on publicly-available information. Although every reasonable care has been taken to ensure the accuracy and objectivity of the information contained in this document, United Overseas Bank Limited ("**UOB**") makes no representation or warranty as to, neither has it independently verified, the accuracy or completeness of such information (including any valuations mentioned). UOB neither represents nor warrants that this document is sufficient, complete or appropriate for any particular purpose. Any opinions or predictions reflect the writer's views as at the date of this document and may be subject to change without notice.

The information contained in this document, including any data, projections and underlying assumptions, are based on certain assumptions, management forecasts and analysis of known information and reflects prevailing conditions as of the date of publication, all of which are subject to change at any time without notice. Past performance figures are not indicative of future results.

Not an offer or solicitation to any particular person
This document should not be regarded as an offer or solicitation to any particular person to transact in any product mentioned. Before deciding to invest in any product mentioned, please seek advice from your financial, legal, tax or other appropriate advisers on the suitability of the product for you, taking into account your specific investment objectives, financial situation or particular needs (to which this document has no regard). If you do not wish to seek such advice, please consider carefully whether any product mentioned is suitable for you.

Risks
An investment in any product mentioned in this document may carry different risks of varying degrees, including credit, market, liquidity, legal, cross-jurisdictional, foreign exchange and other risks (including the risks of electronic trading and trading in leveraged products). Nothing in this publication constitutes personalised accounting, legal, regulatory, tax, financial or other advice that regards the personal circumstances of a particular recipient. Please speak to your financial, legal or other appropriate adviser to understand the risks involved and whether it is appropriate for you to assume such risks before investing in any product.

Any description of investment products is qualified in its entirety by the terms and conditions of the investment product and if applicable, the prospectus or constituting document of the investment product.

Valuation
Product valuations in this document are only indicative and do not represent the terms on which new products may be entered into, or existing products may be liquidated or unwound, which could be less favourable than the valuations indicated herein. These valuations may vary significantly from those available from other sources as different parties may use different assumptions, risks and methods.

No liability
To the fullest extent permitted under applicable laws and regulations, UOB and its affiliates shall not be liable for any loss or damage howsoever arising as a result of any person acting or refraining from acting in reliance on any information, opinion, prediction or valuation contained herein.

UOB and its affiliates involved in the issuance of this document may have an interest in the products mentioned in this document including but not limited to, marketing, dealing, holding, acting as market-makers, performing financial or advisory services, acting as a manager or co-manager of a public offering, of persons mentioned in this document. UOB and its affiliates may also have alliances, contractual agreements, or broking, investment banking or any other relationships for the provision of financial services, with any product provider mentioned in this document. UOB and its affiliates may have issued other reports, publications or documents expressing views which are different from those stated in this document and all views expressed in all reports, publications and documents are subject to change without notice.

Others
Unless you are notified otherwise by UOB, UOB deals as a principal in any transaction which UOB has been instructed to effect, other than transactions relating to securities traded on an exchange, unit trusts and funds on your behalf where UOB acts as your agent.

Singapore. This document and its contents are intended for Accredited Investors (as defined in Section 4A of the Singapore Securities and Futures Act (Chapter 289)).

Hong Kong. This document and its contents are intended for "professional investors" (as defined in the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong) (the "SFO") and its subsidiarity legislation) ("Professional Investors"). Shares or debentures in a company may not be offered or sold in Hong Kong, by means of any document, other than (i) to Professional Investors; or (ii) in other circumstances which do not result in the document being a "prospectus" within the meaning of the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Chapter 32 of the Laws of Hong Kong)(the "CWUMPO") or which do not constitute an offer to the public within the meaning of the CWUMPO. Unless permitted to do so under the laws of Hong Kong, no person may issue or have in his/her possession for the purpose of issue, or will issue, or have in his/her possession for the purposes of issue, any advertisement, invitation or document relating to the securities, structured products or interests in collective investment schemes whether in Hong Kong or elsewhere, which is directed at, or the contents of which are likely to be accessed or read by, the public of Hong Kong, other than with respect to the securities, structured products or interests in collective investment schemes that are or are intended to be disposed of only to persons outside Hong Kong, or only to Professional Investors.

WARNING: The contents of this document have not been reviewed by any regulatory authority in Hong Kong. You are advised to exercise caution in relation to this document. If you are in any doubt about any of the contents of this document, you should obtain independent professional advice.

This document may only be distributed in countries where its distribution is legally permitted. This document is not directed to any person in any jurisdiction where (by reason of that person's nationality, residence or otherwise) such publications are prohibited This document may contain proprietary information of UOB (or its product providers) and may not be reproduced or disseminated in whole or in part without UOB's prior consent.

If there is any inconsistency, or any difference in meaning between the English version and any translation of this document, the English version shall apply and prevail.

United Overseas Bank Limited. Co. Reg. No. 193500026Z
United Overseas Bank Limited is a licensed bank in Hong Kong and is a registered institution in respect of Types 1 (Dealing in Securities) and 4 (Advising on Securities) regulated activities under the SFO.

Right By You