ISSUER COMMENT
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France, Government of

No-confidence vote deepens fiscal challenges

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On 4 December, a majority of France's (Aa2 negative) National Assembly backed a vote of no-confidence (331 in favour, well above the majority threshold) in the government led by Prime Minister Michel Barnier, forcing him and his cabinet to resign. The vote reflects the country's fractured political environment, being only the second successful no-confidence vote since the creation of the Fifth Republic in 1958[1]. This event is credit negative as it deepens the country's political stalemate, reduces the probability of a consolidation of public finances and contributes to wider risk premia and a higher cost of debt.

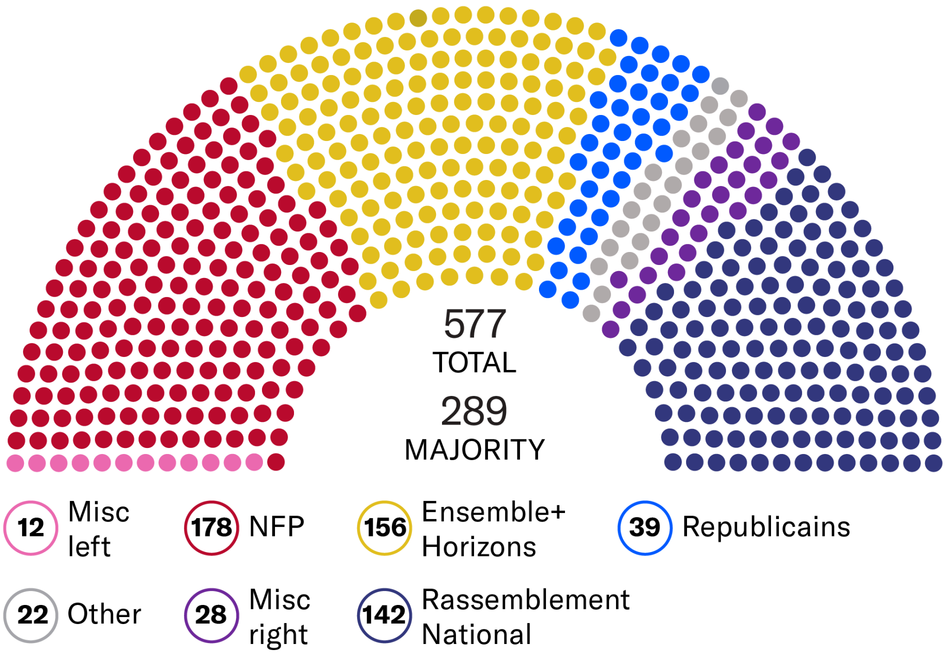
MPs called a confidence vote after PM Barnier decided to push through the government's cost-cutting social security budget (Projet de loi de financement de la sécurité sociale, PLFSS) this week without a parliamentary vote, as permitted under the Constitution's article 49.3.

This budget, together with the state budget (Projet de loi de finances, PLF), which is scheduled for a parliamentary vote later this month, was designed to reduce the country's deficit by €60 billion with spending cuts and tax increases.

The government's budget defeat further complicates policymaking in France. President Emmanuel Macron will need to appoint a new PM without a parliamentary majority since new elections cannot be called before July 2025, a year after the previous dissolution. A new PM is likely to face the same difficulties Michel Barnier encountered over his short tenure, potentially ushering in new political crises.

The heated parliamentary debates over the draft budgets have revealed deep divisions between France's political parties. During these debates, ad hoc majorities were formed to raise several taxes and undo some of the government's spending cuts. A number of contradictory draft bills were subsequently rejected by most MPs, giving the government a new opportunity to return to the original bill.[2] However, the compromise reached by senators and deputies on the final draft social security bill was overturned by the no confidence vote.

Exhibit 1
No single party has a clear majority in parliament



Sources: Moody's Ratings, Ministère de l'Intérieur

Alongside the budget debates, left wing Unbowed France (La France Insoumise) put forward an initiative to reverse a recent pension reform that improves France's long-term fiscal sustainability. This bill proposes lowering the legal retirement age back to 62 from 64, and reducing the contributory period to 42 years from 43 years. While the bill was not adopted because of time constraints, the initiative underscores significant risks to France's fiscal outlook.

We currently expect that the country's annual deficit will reach 6.3% of GDP in 2024, 5.3% in 2025 and 4.7% in 2026, well above the EU's limit of 3%. In the draft budget bills, the outgoing government targeted €60 billion (around 2% of GDP) in spending cuts and tax increases to narrow the deficit to 5.1% of GDP in 2025 from 7.0% of GDP in a no-policy change scenario. Against this backdrop, we forecast France's debt-to-GDP ratio will rise to 115.5% in 2025 and 116.6% in 2026, from 113.3% in 2024 and 98.1% in 2019. We believe that risks to this scenario are now clearly higher, because the emergency bill parliament could adopt before the year-end is not likely to include consolidation measures. We also project deteriorating debt affordability, a key feature of France's credit profile given the country's reserve currency status. We expect its interest payments to revenue ratio will reach 4.6% in 2025 and 5.2% in 2026, up from 4.4% in 2024[3]. A durable increase in financing costs would further weaken debt affordability despite the country's relatively long average maturity of 8.5 years. This would result from the negative feedback loop between higher deficits, a higher debt load and higher financing costs, with significant annual borrowing needs.

Endnotes

1 The first successful no confidence vote was in 1962.

2 There are generally two readings for each bill in France's two chambers, the National Assembly (Lower house) and the Senate (Upper house).

3 The 10-year bond yield would reach on average 3.3% in 2025, 3.6% in 2026 and 3.7% in 2027. That said, the increase in spread against the German Bund has been accompanied by a reduction in rates below the assumption of the draft budget law for 2024.

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