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MACRO PICTURE

France's Fiscal Challenge Ahead of the 2027 Election

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- France's deficit stood at 5.1% of GDP in 2025, while public debt has climbed towards 120% of GDP from below 100% in 2019
- Public spending has reached 57% of GDP, around 8 percentage points above the European average, while the primary deficit of 2.9% is the euro area's highest
- Weak growth is complicating consolidation, with the 2026 growth forecast cut from 0.9% to 0.7% and the government's 5% deficit target increasingly difficult to achieve
- Debt-servicing costs are rising rapidly, while higher defence, social-security and climate-related spending is further squeezing fiscal space

The 2027 Budget Showdown

- The government is targeting only a modest reduction in the deficit to around 4.9% of GDP in 2027
- A hung parliament makes even limited consolidation difficult, with two previous governments falling during budget confrontations
- Lecornu may seek to freeze inflation-linked increases in some pensions and benefits, but Socialist support will be difficult to secure for significant welfare cuts
- The approaching presidential election further reduces incentives for parties to support unpopular measures, despite warnings that delaying adjustment will make future consolidation more difficult

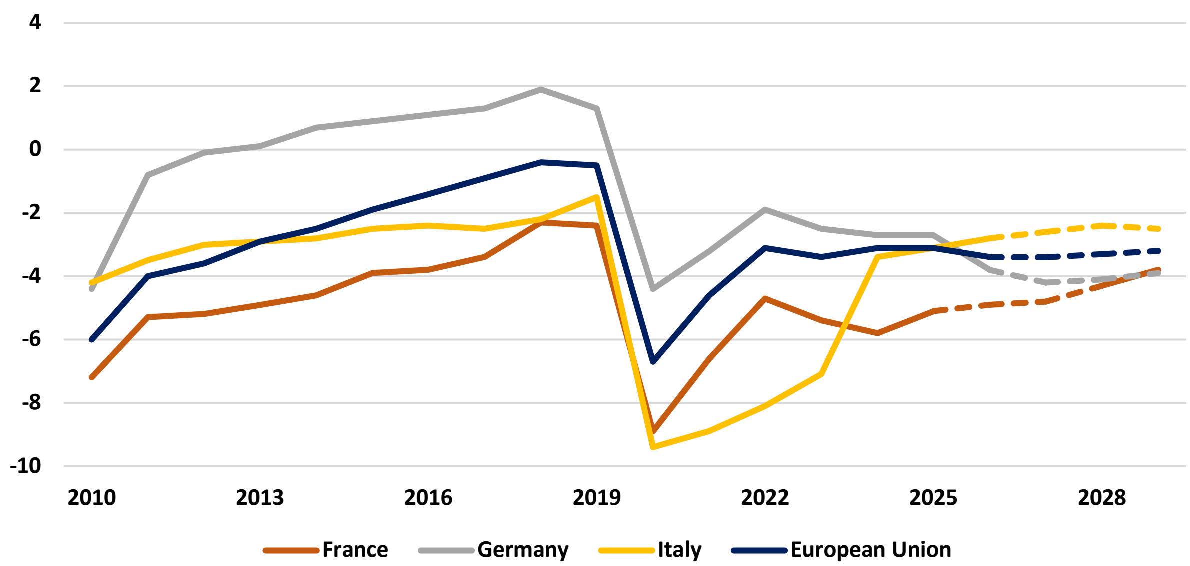
Markets and the Post-Election Fiscal Challenge

- The French-German 10-year yield spread is approaching 90bp, a key level during previous episodes of fiscal stress, while French yields have moved above Italy's
- A sustained break above 90bp could signal a more fundamental reassessment of French debt and revive concerns over fragmentation within the euro area
- Election uncertainty is adding to market concerns, particularly given the contrasting fiscal proposals of Marine Le Pen and Jean-Luc Mélenchon
- Without corrective action, the deficit could approach 7% and debt exceed 130% of GDP by 2030, with an estimated €126bn of cumulative fiscal tightening needed by 2032 to stabilise the debt ratio

France's Worsening Fiscal Position

France's public finances are increasingly strained, raising the risk of a negative cycle of higher borrowing costs, rising debt and weaker growth. The budget deficit stood at 5.1% of GDP in 2025, well above the EU's 3% threshold, while public debt has climbed towards 120% of GDP, from below 100% in 2019 and around 60% in 2000.

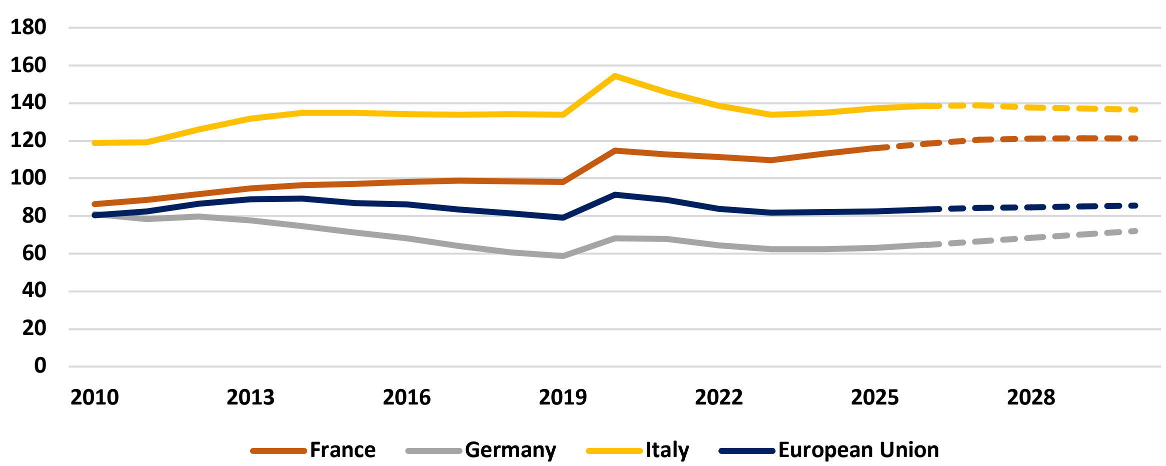
Figure 1: General Government Net Lending/Borrowing (Percent of GDP)



Source: IMF WEO April 2026

The problem is also structural. Public spending has risen to 57% of GDP, around 8 percentage points above the European average, while the number of public-sector employees has increased by around 1 million since 1997. France also runs a primary deficit, excluding interest payments, of 2.9% of GDP, the highest in the euro area. The government had initially aimed to narrow the deficit to 5% this year, but weaker growth and additional spending pressures have put even this modest target at risk. Finance Minister Roland Lescure has acknowledged that reaching 5% will be difficult after the government cut its 2026 growth forecast from 0.9% to 0.7%.

Figure 2: General Government Gross Debt (Percent of GDP)



Source: IMF WEO April 2026

Meanwhile, rising debt-servicing costs are adding to France's fiscal pressures. Interest expenditure reached €34.5bn in the first half of 2026, up 18.8% year-on-year, and is projected to rise from €64.8bn this year to €74.2bn in 2027. Defence spending is also set to increase by another €6.4bn next year.

The deeper structural challenge, however, lies in social spending, particularly healthcare and pensions as the population ages. Pensions, healthcare, unemployment benefits and other transfers account for 58% of public expenditure, while social-security spending is expected to rise by €17bn to €838.3bn in 2027 despite planned savings. With debt servicing, defence and welfare absorbing a growing share of the budget, the government is seeking to keep most other departmental spending growth below inflation.

Climate-related costs are adding to these pressures. Following a summer of extreme heat, drought and wildfires, the government faces additional spending on reconstruction and climate adaptation. Ecological Transition Minister Monique Barbut estimated the immediate economic cost at €10-15bn, or as much as 0.5% of GDP, although the figure remains preliminary. The government has already announced around €100mn in support for fire-affected areas, while longer-term adaptation will require further investment.

The 2027 Budget Showdown

Against this backdrop, Prime Minister Sébastien Lecornu is preparing only a modest fiscal adjustment for 2027, targeting a deficit of around 4.9% of GDP. Yet even limited consolidation will be difficult. The 2024 snap legislative election left France with a hung parliament, turning successive budgets into major political confrontations and contributing to the fall of two of Lecornu's predecessors.

The government is set to submit its 2027 draft budget to the National Assembly within weeks. Among the measures under consideration is a freeze on inflation-linked increases in some pensions and benefits. However, Lecornu lacks a parliamentary majority and will again need support from the Socialists, who are likely to resist significant welfare cuts. Previous attempts to restrain pensions have faced strong opposition, making meaningful consolidation particularly difficult just months before the presidential election.

Budget Minister David Amiel has warned against postponing difficult fiscal decisions until after the election and urged presidential candidates to avoid costly campaign promises. The government argues that reducing the deficit now would give the next president greater room for manoeuvre, but the approaching vote gives political parties little incentive to support unpopular spending cuts.

Markets Price in Political Risk

The uncertainty is increasingly reflected in financial markets. A key level to watch is the spread between French and German 10-year yields, which is approaching 90 basis points. This level has acted as a ceiling during recent episodes of French fiscal stress, with policymakers previously stepping in to reassure markets as spreads approached it. A sustained move above 90bp could therefore signal a broader reassessment of France's debt trajectory rather than another temporary bout of political uncertainty.

French yields have also moved above those of Italy, while French bank shares have come under pressure. Investors see scope for further increases in French borrowing costs, although current tensions are not generally viewed as a threat to broader euro-area financial stability. Such a move could also revive concerns over fragmentation within the euro area, as investors demand higher risk premia from other fiscally vulnerable members. While markets are not currently signalling a debt crisis, further widening would suggest that concerns over France's fiscal outlook are becoming more structural.

The presidential race adds another layer of uncertainty. Markets are particularly sensitive to the prospect of a run-off involving Marine Le Pen and Jean-Luc Mélenchon. Le Pen, currently leading the polls, has pledged to maintain the retirement age at 62, although National Rally is also preparing a €125bn spending-cut package. Mélenchon, meanwhile, has proposed cancelling roughly €600bn of public debt held by the Bank of France.

Figure 3: French and German Yield Spread Is Nearing Critical Levels

Source: [Investing.Com]

Figure 4: The Gap Between Benchmark 10Y Government Bond Yields and Germany's Equivalent

Source: [Reuters]

A Difficult Legacy for Macron's Successor

Whichever president succeeds Emmanuel Macron will inherit a difficult fiscal position. With growth expected at only around 0.7-1% and borrowing costs near 4%, France faces an adverse debt dynamic in which persistently large deficits and rising interest costs leave increasingly limited room for fiscal manoeuvre.

Without corrective measures, the outlook could deteriorate sharply. An independent report commissioned by the finance ministry projects the deficit rising from 5% of GDP in 2026 to nearly 7% by 2030, while public debt would climb from 118% to more than 130% of GDP. Debt-servicing costs would further compound the problem as borrowing issued during years of ultra-low interest rates is gradually refinanced at higher rates.

Putting debt on a sustainable path would therefore require substantial and sustained consolidation. The government-commissioned report estimates that cumulative fiscal tightening of around €126bn will be needed by 2032 to stabilise the debt ratio during the next presidential term. Separately, estimates suggest that reducing the primary deficit from 2.9% of GDP to a stabilising level of around 0.1% would require an adjustment equivalent to roughly 3% of GDP over several years.

The timing of that adjustment will also matter. The report warns that postponing consolidation until after the 2027 election would require larger measures later and could further undermine investor confidence. The next president will therefore face a difficult balance between restoring fiscal credibility and implementing politically contentious reforms at a time of weak growth and mounting spending pressures.

France enters the 2027 budget and presidential election cycle caught between the growing urgency of fiscal consolidation and the political difficulty of delivering it.