Flash Economics

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Where will the lack of control over France's public debt ratio lead?

France's public debt ratio is not under control: stabilising it would require turning a primary deficit (excluding interest payments) of close to 3% of GDP into a primary surplus of more than 3% of GDP.

Where could this continuous rise in the public debt ratio lead? Four scenarios can be envisaged:

- a stabilisation of the interest rate spread between France and the other euro zone countries at a high level, but one not high enough for the ECB to intervene. This stabilisation would result from investors returning to French sovereign debt, given its high yield. There would be no abrupt financing crisis for the general government sector, but the economy would be stifled, with increased underinvestment and structurally very weak growth, making it impossible to eliminate public deficits;

- a continuous widening of the interest rate spread between France and the other European countries, without an abrupt debt crisis. At some point, as the spread widens, France would have to call on the ECB for help in financing its public deficits at a lower interest rate. The ECB normally attaches conditions to the use of the Transmission Protection Instrument (TPI). However, given France's economic weight, it is not certain that these conditions would be very strict. That said, they would still require an initial correction of the primary deficit;

- an abrupt financing crisis, with the Treasury no longer able to raise the funds needed to finance the deficits. This crisis would force an equally abrupt shift to fiscal austerity, with adverse consequences in the short term (higher unemployment, a decline in activity) and favourable ones in the long term (lower interest rates, a return to growth);

- an attempt to stimulate demand, either by supporting the incomes of low- and middle-income households or by supporting investment. The problem with such a policy is that, given weak investment and limited production capacity, much of the stimulus would leak into imports; moreover, if it were aimed at boosting consumption, it would weaken investment further.

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France's public debt ratio is not under control

France's fiscal position is characterised by:

- **a high primary deficit** (excluding interest payments on public debt): 2.9% of GDP in 2025 (**Chart 1**);
- **a long-term interest rate well above nominal GDP growth** (**Charts 2A and 2B**), so that, given current interest rates and growth, **stabilising the public debt ratio would require a primary surplus of 3.2% of GDP**.

Chart 1
France: General government primary deficit
(as % of GDP)

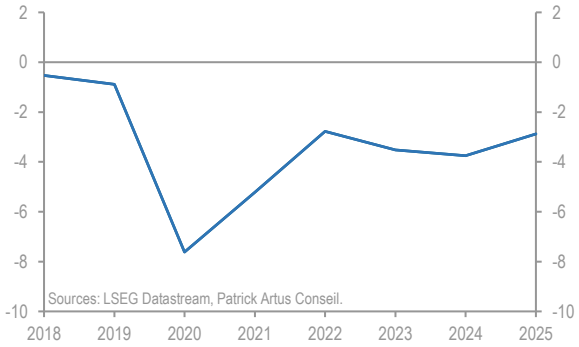


Chart 2A
France: 10-year interest rate on government bonds
(as %)

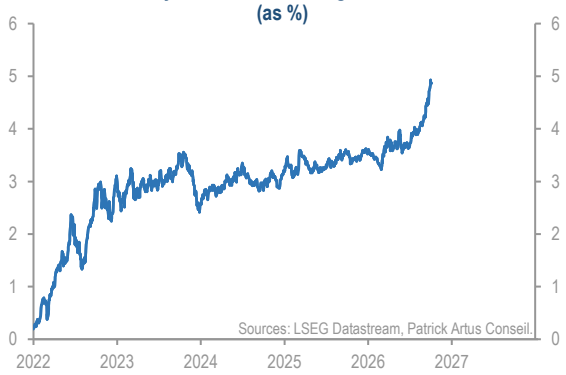
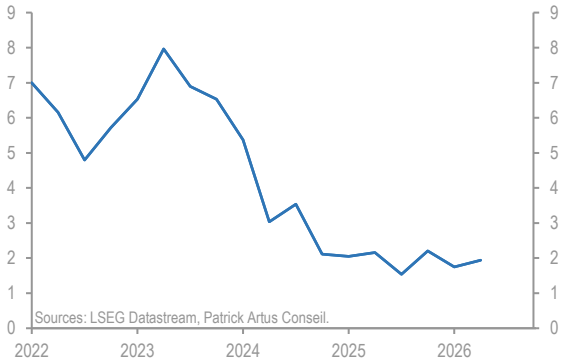


Chart 2B
France: Nominal GDP (Y/Y, %)



It follows that, **with fiscal policy, growth and interest rates unchanged, the public debt-to-GDP ratio would rise by around 6 percentage points a year**. France's public debt ratio is therefore not under control. Where could this upward drift lead?

What is the outlook for interest rates and fiscal policy?

First scenario: stabilisation of the long-term interest rate at a high level

In this scenario:

- **the long-term interest rate and its spread over Germany** (**Chart 3**) **stabilise at a high level**, as investors are attracted to French public debt by its high yield;
- the level at which the interest rate and the spread stabilise is not high enough to trigger ECB intervention;
- the high level of interest rates would therefore **stifle the economy**, with weakened investment (**Chart 4**) and low potential growth, making it **impossible to reduce the primary deficit**.

Chart 3
France: 10-year government bond yield spread relative to Germany (percentage points)

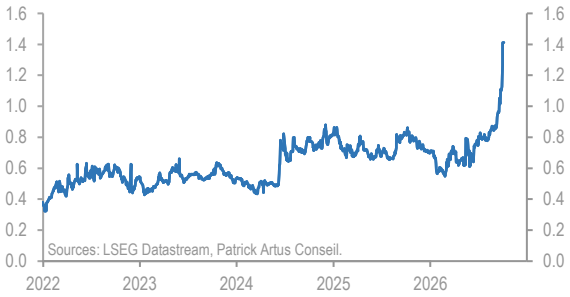
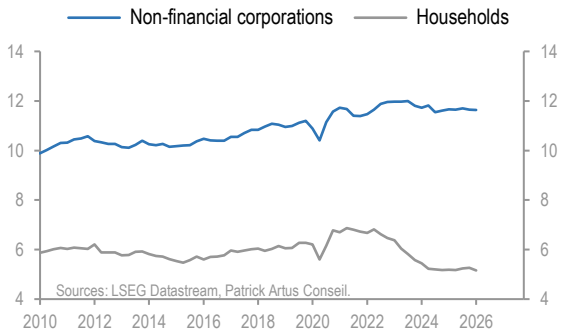


Chart 4
France: Investment by non-financial corporations and households (as % of GDP)



Second scenario: ECB intervention

In this scenario, the interest rates faced by France rise so sharply that **the ECB has to activate the Transmission Protection Instrument** (TPI), which allows targeted purchases of the government bonds of a country whose financing difficulties are becoming severe. The rationale behind the TPI is to prevent the interest rates faced by a country from becoming so high that monetary policy impulses are no longer felt there.

In principle, activation of the TPI presupposes that **the country concerned is pursuing policies to correct its public deficits** (use of the TPI is normally conditional on such measures being implemented). However, since France carries great economic weight, and therefore considerable bargaining power, and could wield the threat of a default, it is likely that **the conditions set by the ECB for activating the TPI in France's favour would not be very restrictive**.

There would nonetheless be **an initial correction of the public deficit**, through a slowdown in public spending growth and higher taxes and social contributions.

Third scenario: abrupt financing crisis

In this scenario, the French Treasury eventually faces **a collapse in demand for government securities** as a result of a deteriorating financial or political situation. This would entail **a rapid shift to fiscal austerity**, with the consequences observed in southern European countries, illustrated here by the case of Spain:

- **a rapid reduction in the public deficit** from 2010 onwards (**Chart 5**);
- **a prolonged downturn, followed by a strong pick-up in growth** (**Chart 6**), driven by improved competitiveness (public spending cuts that made room for lower business taxes, and wage restraint).

Austerity is very costly in the short term in terms of output and jobs (**Chart 7**), but it enables a recovery in the long term once public finances have been restored.

Chart 5
Spain: General government balance (as % of GDP)

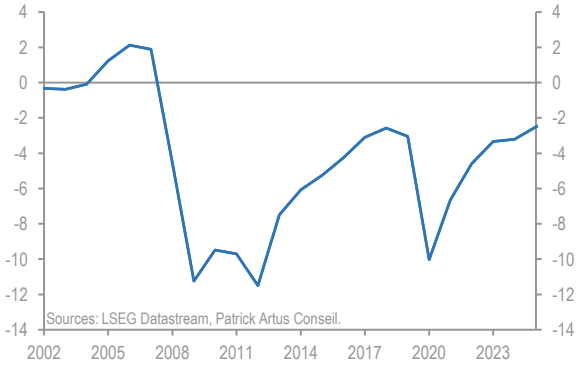


Chart 6
Spain: Real GDP (Y/Y, %)



Chart 7
Spain: Unemployment rate (as %)



Fourth scenario: demand stimulus policy

A future government, **faced with weak growth in France** (**Chart 8**) and, as a result, with difficulty in reducing public deficits, could decide to pursue **a demand stimulus policy**: higher wages and social benefits, job creation in the public sector, increased public investment in the energy transition, and support for industry. The aim would be to boost growth and, in turn, tax revenue. The danger of such a policy, however, is that in a heavily deindustrialised country (**Chart 9**) with high production costs (**Table 1**), **a demand stimulus would mainly result in higher imports and a deterioration in the trade balance** (**Chart 10**).

Chart 8
France: Real GDP

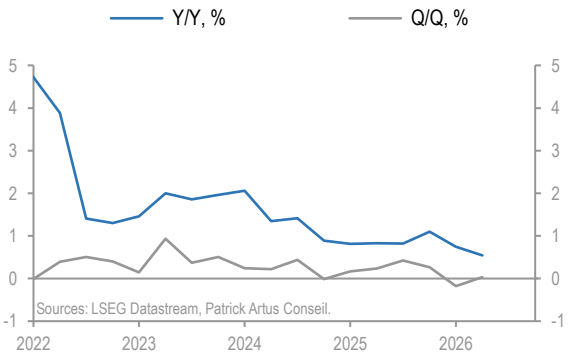


Chart 9
Manufacturing value added
(as % of GDP, in volume terms)

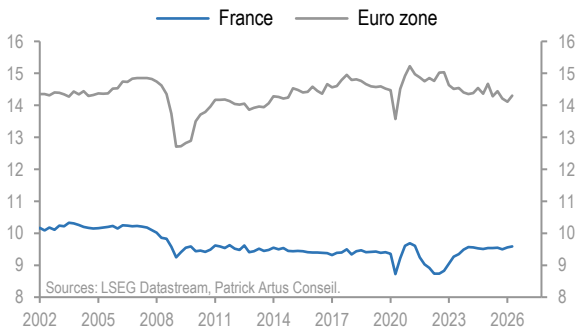
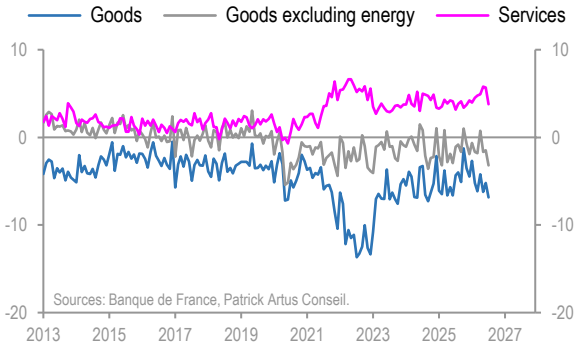


Table 1: Mean nominal hourly labour cost per employee in the manufactring sector (2025, EUR)

Country	Mean nominal hourly labour cost (EUR)
Germany	49.5
France	47.1
Italy	32.8
Slovenia	29.8
Spain	28.2
Czechia	20.2
Slovakia	19.3
Croatia	19.2
Poland	17.1
Portugal	16.5
Hungary	15.6
Romania	12.0
Bulgaria	10.2

Source: Eurostat

Chart 10
France: Goods and services balances
(in EUR bn, monthly data)



Conclusion: which scenario is the most likely?

All four scenarios (stabilisation of long-term interest rates at a high level; interest rates rising so high that the ECB has to intervene; a Treasury financing crisis and fiscal austerity in response to it; a demand stimulus policy) have a non-zero probability of materialising.

Which of these four scenarios materialises will depend on:

- investors' reaction: will they be drawn back to French debt once interest rates exceed a certain threshold?
- the extent of the ECB's willingness to avert the risk of a French default;
- the authorities' ability to persuade the French public to accept moderate fiscal restraint in order to avoid an abrupt financing crisis;
- the political context (the election of a far-left, left-wing, centrist, right-wing or far-right president).

The most optimistic scenario is one in which a "centrist" president is elected, investors are willing to hold French sovereign debt at an interest rate that is not excessively high, the ECB makes it clear that it will not tolerate a French default and the French public accepts a degree of fiscal restraint. But this is only one of several possible scenarios.

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