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Bond, French bond: licence to widen?

French bond spreads have nearly doubled since early September. Large deficits, political gridlock, and rising interest costs, are self-reinforcing. A Le Pen presidency with a hung Parliament next year is our base case, but structural challenges, not concerns about Le Pen per se, are the driver of market worries. If spreads widen further, ECB intervention may then come into view.

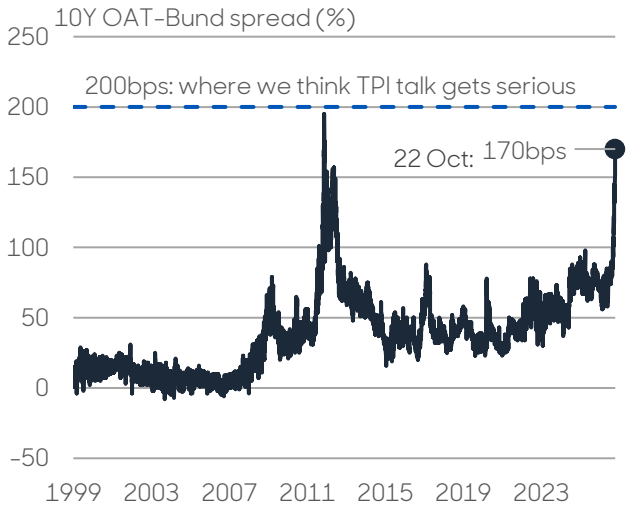
Key Takeaways

- Our long-held view that France is 'periphery', not 'core', is playing out. Last week, 10-year French OAT yields rose above 5%, the highest since 2002. The spread over Bunds doubled from early September to above 170bps, the widest since 2011, although they are at 155bps at the time of writing, as Moody's didn't downgrade France's debt rating.
- Until mid-October, spreads tracked prediction market odds of a Marine le Pen win in May 2027's election. But spreads continued to widen in recent weeks even as Le Pen's odds levelled off.
- Instead, a self-reinforcing 'ratchet' has been at work, with large deficits, political gridlock, and rising interest costs feeding off each other.
- Our base case is a Le Pen presidency and a hung National Assembly. The risks to that are the *cordon sanitaire* locking out Le Pen, or alternatively National Rally (RN) winning in Parliament too.
- Gridlock would limit the scope for a populist fiscal expansion. But it also makes consolidation unlikely.
- While there may be scope for more pressure on spreads, we think the ECB's Transmission Protection Instrument (TPI) comes into play at spreads of 200–250bps.

OAT of control?

Ten-year French government bond (OAT) yields have risen to 4.9%, and were briefly above 5% last week, from 4.2% in early September. This is the highest since 2002. The spread over German bunds is around 155bps, and peaked above 170bps, up from 86bps in early September. That is not that far off the euro-crisis peak of 187bps (see Figure 1). Between the 2024 snap election and this summer, the spread had mostly traded in a 55–85bps range.

Figure 1: France's 10-year spread over Germany is closing in on its euro-crisis peak



Source: Haver, Aberdeen, October 2026

The selloff has outgrown its original trigger

Until this month, the widening in French spreads looked like a bet on the presidential race, reflecting investor concerns that a populist National Rally (RN) government could worsen debt and deficit dynamics.

Between July and early October, the spread and the Polymarket-implied probability of an RN presidential victory moved closely (see Figure 2). But that relationship has now broken down. Le Pen's odds have been level around 47% since 15 October, while the spread widened a further 33bps to 22 October. It has since narrowed 17bps on Moody's decision not to downgrade France's debt rating.

Figure 2: Spreads tracked Le Pen's odds until mid-October… then broke away



RN win probability is the sum of the Polymarket contracts on Marine Le Pen and Jordan Bardella.
Source: Polymarket, Bloomberg, Haver, Aberdeen, October 2026

Mélenchon, protests, energy, and default risk are exacerbating the selloff

Several factors explain this divergence. First, Le Pen's recent commitment to fiscal consolidation, and the polling strength of far-left presidential candidate Jean-Luc Mélenchon mean her candidacy no longer represents the most adverse outcome for markets.

Second, recent protests triggered by proposed budget cuts in the 2027 French budget have underlined the political barriers to fiscal consolidation.

Third, and most concerningly, wider spreads may now be self-reinforcing. Volatility deters buyers, and as higher debt-service costs are built into projections, the fiscal arithmetic worsens in a way that seems to justify the move. Higher gas prices add to the pressure by pushing the European Central Bank (ECB) towards the further rate hikes we expect in December and March.

French debt interest payments already amount to 2.6% of GDP. Because France will run a significant deficit over coming years, the rise in yields means an increasing proportion of its debt pile will be written at high rates of interest, putting further pressure on the debt service bill.

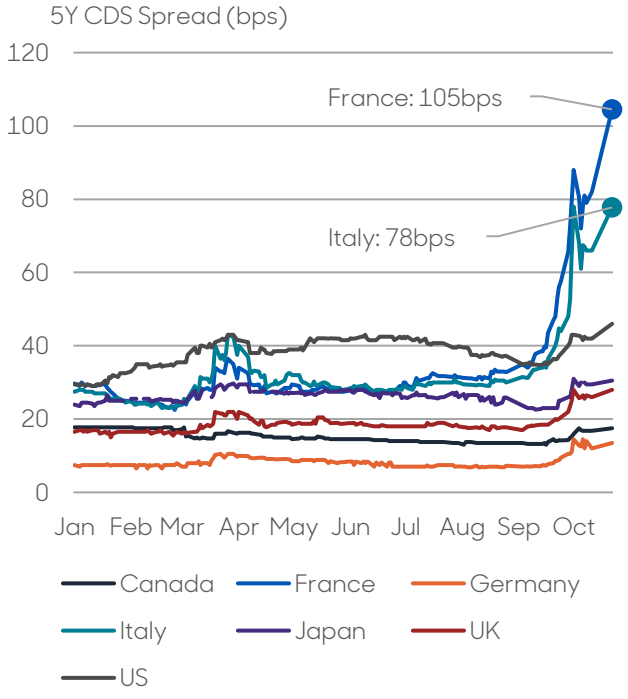
This 'rachet' effect is a game changer for French fiscal stability because it could plausibly push OAT yields dangerously high even without a clear trigger.

It also matters for the institutional foundation of the Eurozone. In most developed countries, depreciation of the currencies of highly indebted countries acts as an endogenous release valve that makes debt service more affordable. And, *in extremis*, a national central bank can monetise the debt. Such a scenario still results in high yields but keeps the risk of default low.

But in France's case, dangerously high yields can result only in radical austerity, a bailout from its partners in the Eurozone, or debt restructuring.

Markets are increasingly paying attention to the latter scenario. The cost of insurance against a French default has risen sharply – a development that has emerged concomitantly with the decoupling of Le Pen's odds and OAT spreads (see Figure 3).

Figure 3: Default risk is taking over from political risk

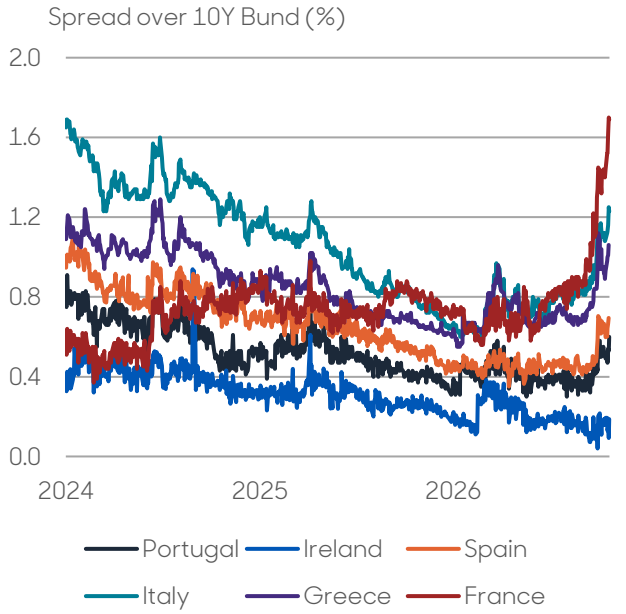


Source: Aberdeen, Bloomberg, October 2026

Memories of the euro crisis continue to loom

Another sign of this can be seen in the broadening of the selloff from France to other Eurozone peripheries. Very little news about the Italian or Greek fiscal outlooks has come to light in recent weeks – yet spreads have widened between 25 and 30bps (see Figure 4).

Figure 4: Early signs of contagion from French widening



Source: Aberdeen, Haver, October 2026

The conditions for a broader euro debt crisis redux scenario are not in place at this point. But we are alert to the possibility of the ECB intervention being needed to ward it off, especially if Eurosceptic political movements continue to gather momentum.

Our electoral base case: a Le Pen presidency

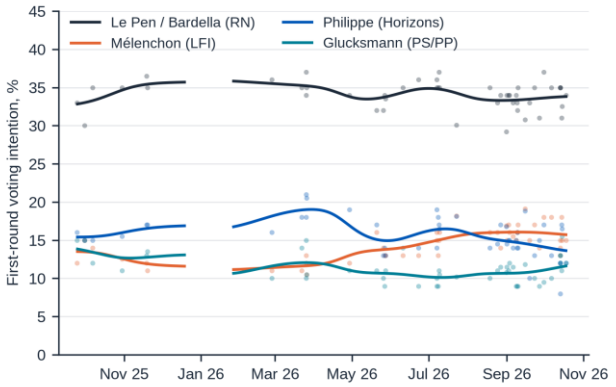
Our base case is that Marine Le Pen wins the presidency in May 2027.

Le Pen leads every first-round poll, averaging around 35% (see Figure 5). Since 1958, no presidential candidate with such a clear first-round polling lead at this stage of the cycle has lost. Though we expect the centrist field to consolidate over coming months, hypothetical smaller fields show little change in first-round voting intentions.

Our base case assumes a centrist, most likely Édouard Philippe, reaches the run-off. But Mélenchon has a meaningful chance of doing so instead in a crowded field. This would in turn make a Le Pen victory more likely.

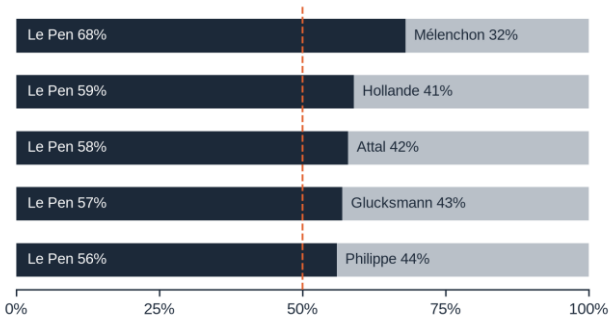
France's two-round system leaves scope for polling surprises as voting patterns shift between rounds. The recent Brazilian election outcome is but the latest warning about over-extrapolating polls. Still, second-round polling shows Le Pen winning every possible run-off (see Figure 6). She beats Philippe 56-44, and Mélenchon 68-32.

Figure 5: Le Pen leads every first-round poll...



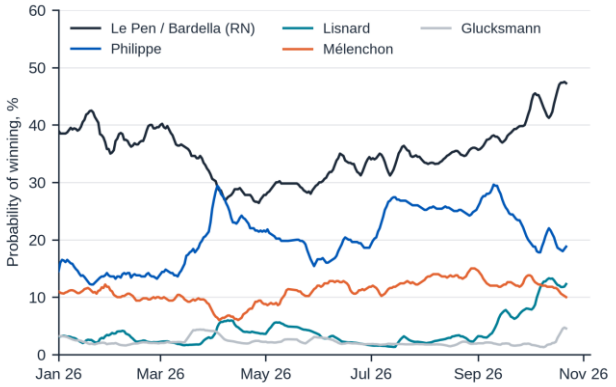
Source: Cluster17, Elabe, Harris Interactive, Ifop, Ipsos BVA, Odoxa, OpinionWay, Verian, YouGov, sondage-presidentielle.fr, Aberdeen, October 2026

Figure 6: ...and she would win every run-off



Source: Ifop-Fiducial for LCI, Le Figaro and Sud Radio (fieldwork 17-19 October 2026), Aberdeen, October 2026

Figure 7: Prediction markets also make the RN the favourite



Five-day moving averages. RN is the sum of the contracts on Marine Le Pen and Jordan Bardella.
Source: Polymarket, Bloomberg, Aberdeen, October 2026

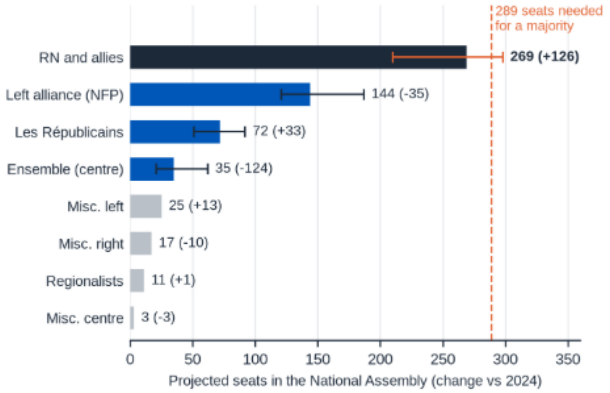
Prediction markets also show Le Pen as the clear favourite, putting the chances of an RN presidency at around 47%, well ahead of Philippe at 19% (see Figure 7).

But any president likely faces a hung Parliament

The 2024 snap election has ended the modern cadence of French parliamentary elections being automatically held shortly after presidential elections. However, given the instability of the current Parliament, we expect a snap election to restore the previous French political calendar as likely. But any president, including Le Pen, would struggle to win a majority.

Legislative outcomes remain highly uncertain given two-round voting and inter-party electoral pacts. One projection puts the RN and its allies on around 269 seats, short of the 289 needed for a majority, although the top of its likely range clears that bar (see Figure 8). If anti-RN tactical voting weakens, the RN could win outright.

Figure 8: Projections leave the RN short of a majority, but within reach



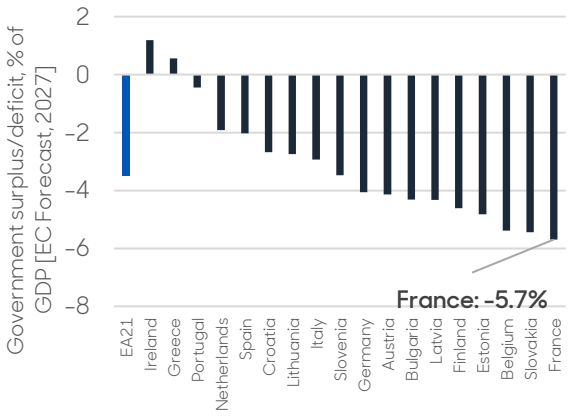
Central projections; lines show the likely range (90% of simulations). Changes are versus the 2024 election. Ranges are approximate.
Source: Poliwave (forecast of 13 August 2026), Aberdeen, October 2026

We still lean towards a hung Parliament given the fractured state of the French electorate. But Le Pen is the presidential candidate best placed to secure a parliamentary majority.

Gridlock, not populism, is the fiscal problem

The 2027 budget targets a deficit of 5.0% of GDP, from 5.4% this year, against a no-policy-change path closer to 6%. France has a history of slippage, and the protests against a modest package show how hard larger adjustments will be. European Commission forecasts see France running a large deficit next year compared to other Eurozone economies (see Figure 9).

Figure 9: France to run the Eurozone's largest deficit in 2027



Forecasts assume no change in policy, so exclude measures in France's draft 2027 budget. This chart excludes small states
Source: European Commission (Spring 2026 forecast), Aberdeen, October 2026

In a hung Parliament, a Le Pen government, with Jordan Bardella as her stated choice of prime minister, would face the same dynamics as recent French governments: compromise bills; budgets forced through via Article 49.3; and the constant threat of censure motions, a taboo that has now been broken.

That cuts both ways. It limits the scope for the most populist parts of her platform. But it also makes meaningful consolidation unlikely. Le Pen now proposes a referendum on binding fiscal rules and €140bn of net savings by 2032, but her plans lack detail and lean on contested savings such as lower EU contributions. Hemmed in at home, she may spend more political capital confronting Brussels.

How bad could it get? The ECB is the circuit breaker

We have previously argued that the ECB is a long way from deploying its Transmission Protection Instrument (TPI) to contain French bond spreads. France is (technically) ineligible while subject to an excessive deficit procedure, and widening that tracks fiscal and political news is hard to call 'unwarranted and disorderly'. But, though we remain far from the thresholds for intervention, our thinking is evolving. If conditions deteriorate sharply, we suspect the ECB would find a way around the eligibility block.

But TPI intervention would have considerable political implications. It would effectively mutualise French fiscal risk across the Eurozone, meaning all members could stand to lose out in the event of restructuring or mark-to-market losses. That could be profoundly unpopular with other Eurozone countries, especially Germany.

So, we think 200bps is the minimum spread for intervention to become plausible, with the ECB most likely to act somewhere between 200bps and 250bps. Wide spreads are not in themselves a sign of disfunction in euro sovereign debt markets and so will not be enough. The ECB will want evidence that markets are undermining the euro system itself rather than responding to French fundamentals (see Figure 10).

Figure 10: What would bring the ECB in: TPI signposts

Signpost	Now	Danger zone
OAT-Bund ten-year spread	c.155bp	200-250bp, moving disorderly
French government five-year CDS	100bps	150bps
Periphery spreads	Italy c.115bp in early October (59bp in January); Spain c.65bp	Contagion to peripherals with relatively solid fundamentals such as Ireland and Portugal. Italian and Greek selloffs deepen
EUR/USD	1.12, from 1.16 in early September	Disorderly fall through parity
French banks	French banks are out of favour, yet the consensus view remains that the French banking system much better capitalised than in 2012. MSCI France Banks -26.5% since 1 Aug CDS spreads between 35-50bps	The narrative shifts: concerns over the French banking system's exposure to OATs prompts comparisons to the mutually reinforcing collapse of sovereign debt markets and the banking sector that precipitated the Euro crisis. MSCI France Banks falls another 15%+ CDS spreads spike to 100bps
Market functioning	Auctions still covered	Auctions of long-dated debt slated for November and December are weak, with wide bid-ask spreads, and generate broader uncertainty
ECB messaging	Lagarde: "France must resolve its debt problems on its own"	Officials link the selloff to "non-fundamental" factors, and push back against market pricing

Source: LSEG, ECB, Aberdeen, October 2026

TPI could work even for a market as large as France's: being on the wrong side of an intervention day would be painful enough to deter speculators even before the ECB had to buy in size.

But this cuts both ways. If the TPI were to be less successful than we expect, it could be taken by markets as a signal that the ECB lacks the firepower to stem the selloff. That would see selling resume after a brief reprieve, and challenge the ECB to make a more powerful intervention.

What we think now

France's political fragmentation and rising borrowing costs risk becoming self-reinforcing. Our base case of a Le Pen presidency with a hung Parliament contains the worst populist risks, but offers little prospect of fiscal consolidation.

For two years we have argued that France belongs with the periphery rather than the core. That has played out. France now finds itself at the epicentre of a selloff that bears more than a passing resemblance to the early stages the periphery debt crisis. Should it spiral out of control, the ECB will be forced to respond to it as such.

So, we now believe TPI intervention to be a serious, though still low probability, possibility.

What is certain is that the structural challenge will persist.

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