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European elections and country Implications

Key messages

- The EU election results have proven more consequential than expected.
- The bigger surprise and source of uncertainty came from the announcement of snap elections in France.
- The weakness of the euro and the upward pressure on Eurozone government bond yields could persists over the coming months. Equity markets to continue benefitting from a positive global economic outlook and the expectation for lower interest rates

European elections – Facts and projections

The results have proven more consequential than expected. When it comes to winners and losers, they were however not markedly different from what had been signaled by polls in advance, with the centre-right and far-right parties advancing, at the expense of centre-left and left-wing parties. Preliminary results suggest that the super-grand coalition of the EPP, Progressive Alliance of Socialists and Democrats and Renew Europe are projected to retain their majority in the European Parliament. That should make Ursula von der Leyen's reappointment as European Commission President likely but not certain. Using current available information, the EPP, S&D and RE are projected to obtain 401 out of 720 seats (56%), compared with 417 out of 705 (59%) currently held.

Snap elections in France:

The far-right Rassemblement National (RN) won the largest share of the vote (around 32%), around two times the size of the support for Macron's party (around15%), amidst the highest participation rate in some thirty years (of 52.5%).

While a strong performance of the RN in France was not a surprise, given earlier polls, the fact that this led to French President Emmanuel Macron calling snap parliamentary elections - which will take place on 30 June and 7 July – showed that the EU elections have impacted French national politics much more then expected. With only three weeks to go until the first round, a significant change in the voting landscape is not guaranteed. Also to note that, the last historical precedent of a snap vote in 1997 led to a loss of majority for President Chirac.

The main impact of the snap election is to increase policy uncertainty, and this could weigh on business sentiment. Indeed, a far-right government could have implications on the direction of fiscal policy (less fiscal discipline), the implementation of recent structural reforms (for example the pension reform which raised the retirement age to 64 from 62 was opposed by the far-right party) and possible effects on EU relations.

There are also several ways in which the change in the political landscape in France could have implications for the EU:

First, a cohabitation of President Macron with a government of a different colour could affect the negotiations on the formation of the new European Commission, although the President holds the prerogative on foreign affairs. A win of the RN in the coming French vote could hinder the confirmation of the current EU leadership and therefore affect policy priorities.

Guy Ertz, PhD.

Chief Investment Advisor – Deputy Global CIO
BNP Paribas Wealth Management

Second, a change in the French government could affect the likelihood of country level agreements on several matters. Multiple EU programmes and frameworks, including the NGEU and the EU fiscal rules, were born thanks to a significant contribution from the European Commission but ultimately depended on an agreement among member states.

Third, a change in the economic outlook for France can have implications at the EU level. France's weight in eurozone GDP is around 20% and at face value only major shifts in economic projections would have the potential to affect EU dynamics. However, heightened business uncertainty might compound the impact. While we do not think this would be enough to derail the current eurozone recovery, it nonetheless presents a new source of downside risk.

The next important steps:

Over the next few weeks, the focus will be on the French elections with the two steps on June 30th and July 7th. Regarding the European Parliamentary elections, the formation of the political groupings must be decided ahead of the first plenary session (16-19 July). The final composition of these groups will be an important consideration and may have implications for policymaking. preliminary results suggest that the super-grand coalition of the EPP, Progressive Alliance of Socialists and Democrats and Renew Europe are projected to retain their majority in the European Parliament, in turn making Ursula von der Leyen's reappointment as European Commission President likely, albeit still uncertain.

Consequence for financial markets:

The obvious consequence of the recent events is to increase uncertainty and volatility of specific asset prices. Political events generally have a limited impact on markets medium-term if they do not have a systemic impact. We do not expect the outcomes of the votes to materially change the global outlook for economic growth and inflation over the coming years. Whether it could reduce somewhat the potential for growth for the eurozone remains conditional on the major investment programs such as the green deal. Investors should expect short-term weakness in the euro to persist over the coming months. Our 3-month target for the EURUSD (value of one euro) takes that into account with a level of 1.06. On a 12-month horizon we expect 1.12. The spreads on European government bonds could move higher, especially for France. This could offer interesting investment opportunities once the dust settles. Equity markets should continue to benefit from a positive global economic outlook for 2025-26 and the expectation for lower interest rates and bond yields.

THE INVESTMENT STRATEGY TEAM

FRANCE

Edmund SHING
Global Chief Investment Officer

Jean-Roland DESSARD
Chief Investment Advisor

Isabelle ENOS
Investment Advisor

ITALY

Luca IANDIMARINO
Chief Investment Advisor

BELGIUM

Philippe GIJSELS
Chief Investment Advisor

Alain GERARD
Senior Investment Advisor, Equities

Xavier TIMMERMANS
Senior Investment Strategist, PRB

GERMANY

Stephan KEMPER
Chief Investment Strategist

Stefan MALY

LUXEMBOURG

Guy ERTZ
Chief Investment Advisor – Deputy Global CIO

Edouard DESBONNETS
Senior Investment Advisor, Fixed Income

ASIA

Prashant BHAYANI
Chief Investment Officer, Asia

Grace TAM
Chief Investment Advisor, Asia

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