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Toasted OATs? What it might mean for SSAs

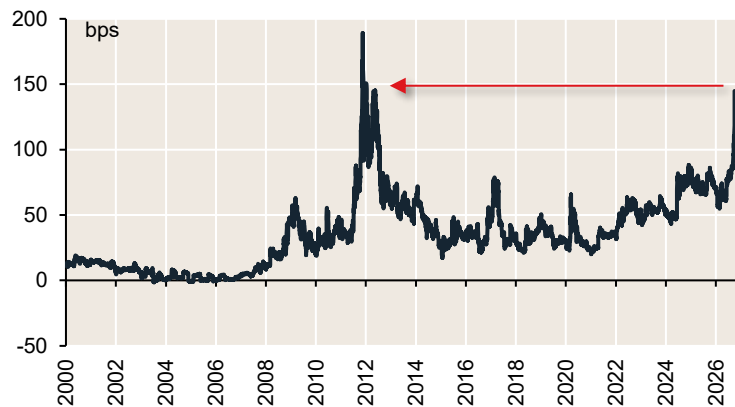
By Taylor Schleich & Ethan Currie

Years of political instability and loose fiscal policy in France have come to a head in recent weeks as French bond investors have gotten a case of the jitters. The closely watched OAT-Bund spread widened to its most extreme level since 2011 (peaking at 152 bps in 10s before settling at 141 bps). The absolute and relative moves in OATs are jarring but still nothing like the weakness seen in peripheral sovereigns in the Euro debt crisis. Nor is the move as extreme as Italy's 2018 political crisis, when BTP-Bund spreads widened over 150 bps (to nearly 300 bps) in a few weeks.

Still, there are legitimate concerns about France's fiscal outlook. The government is poised to run a deficit of 5.4% of GDP in 2026. Even with material budget cuts and "optimistic" economic assumptions, this is set to ease only modestly in 2027, to 5.0%. PM Lecornu still believes the deficit can reach 3% of GDP by 2029, but investors need more convincing given France's exceptional political volatility. For France, it's not a revenue problem as general government revenue exceeds 50% of GDP—far more than most economies. The greater challenge is restraining spending without crushing growth or provoking more political turmoil.

Chart 1: France sovereign risk sharply reassessed

10-year OAT-Bund (France-Germany) yield spread

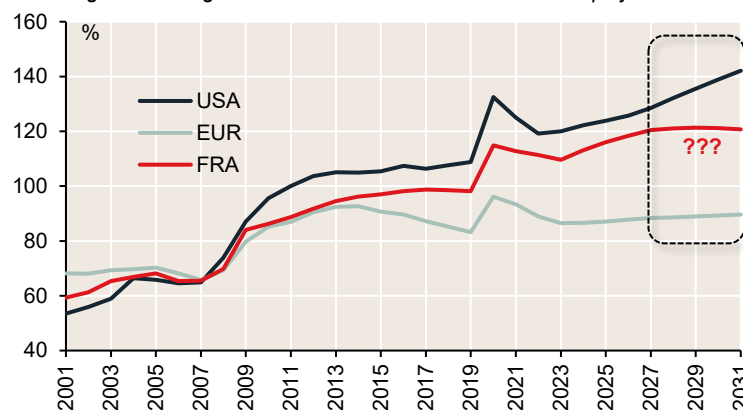


Source: NBC, Bloomberg

The OAT-Bund spread was gradually widening since COVID but this move accelerated in recent months and surged even faster in recent weeks. At nearly 150 bps, the spread in 10s is rivaling Euro debt crisis levels. Still, France's repricing pales in comparison to that of some PIIGS nations in the early 2010s. The relative sell-off is also significantly less sharp than Italy's 2018 episode.

Chart 3: France's debt burden has tracked in line with U.S...

General government gross debt as a share of GDP: Actual and projected



Source: NBC, IMF, Bloomberg

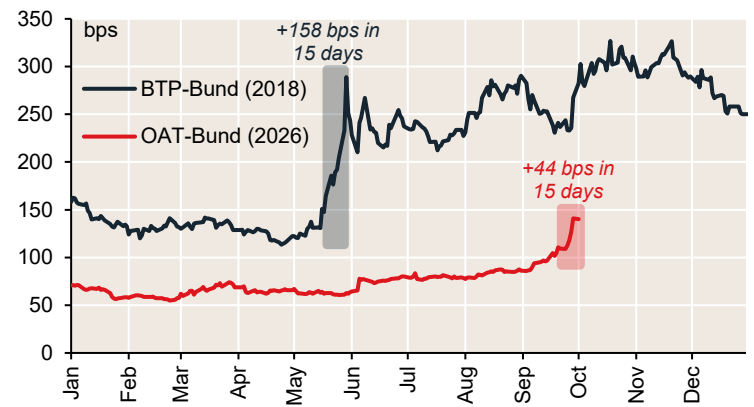
The French debt burden may be below the U.S.'s but (1) their fiscal 'advantage' is small, (2) it's grown at the same pace as the U.S. since the GFC and (3) it's well above the Eurozone aggregate. IMF projections technically see stabilization ahead, but investors will need to see it to believe. A new French budget still sees a 5% of GDP deficit in 2027—and that's with material budget cuts.

Notably, France-related anxiety isn't confined to sovereign debt. Cracks are even forming in the ultra-safe SSA market with European supras underperforming. While the move is understandable, the intrinsic credit quality of these names remains rock solid. And while France is a large shareholder/capital contributor to many of these institutions—including the EIB, ESM, CEB and EBRD—its share of subscribed capital is sub-20% in each case. Moreover, the amount of paid-in capital is much smaller than the institution's total subscribed or callable capital.

Even if one were to entertain doomsday scenarios where France's fiscal problems weakened its support for European institutions, the U.K.'s departure from the EIB provides a useful precedent. Despite the U.K. accounting for 16% of the EIB's capital, its withdrawal was orderly. Paid-in capital is being returned over 12 years, and the callable capital was redistributed among the remaining shareholders. There was no material disruption to the EIB's operations or market access. That may be comfort for investors worried about a material credit impairment to European supranationals even if spreads remain vulnerable to sentiment for now.

Chart 2: Relative OAT repricing smaller than Italy's in 2018

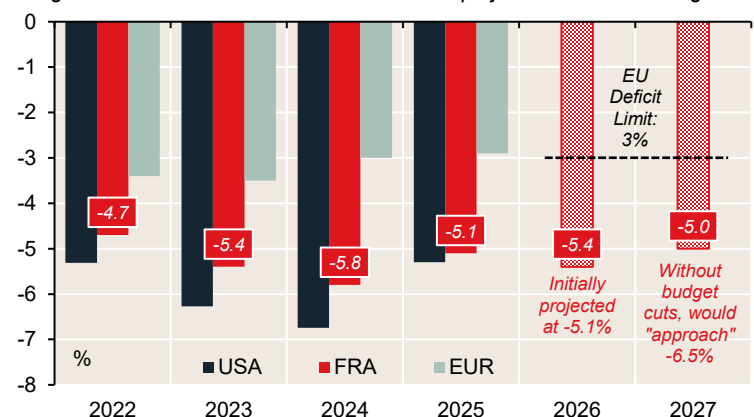
10-year BTP-Bund spread (2018) and 10-year OAT-Bund spread (2026)



Source: NBC, Bloomberg

Chart 4: ...due to comparable federal budgetary shortfalls

Budget balance as a share of GDP: Actual and projected from FRA Budget '27



Source: NBC, Bloomberg, France | Note: Patterned bars denote FRA '27 Budget proposal

**Chart 5: In France, there's no shortage of revenue...**

General government revenue as a share of GDP: 2026

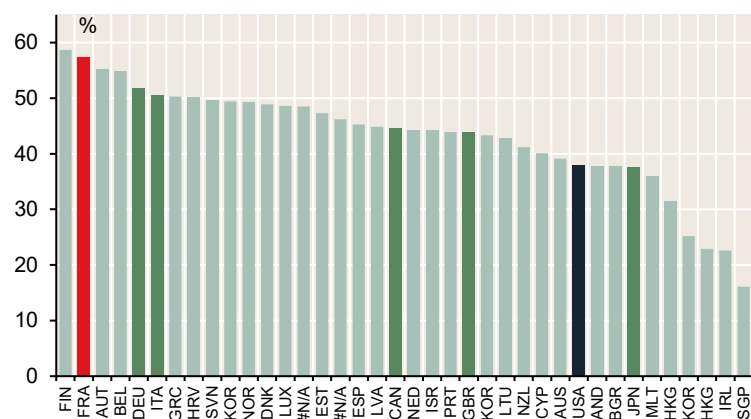


Source: NBC, IMF, Bloomberg | Note: Darker bars denote G7 nations

France does not have a revenue problem. As a share of GDP, general government revenues are greater than all G7 nations and the vast majority of advanced economies (only Norway and Finland collect more). But its spending is nearly the highest in the developed world. Notionally, there's room to cut back then. But doing so is a politically sensitive endeavor that's been easier said than done.

Chart 6: ...but spending is the bigger source of fiscal angst

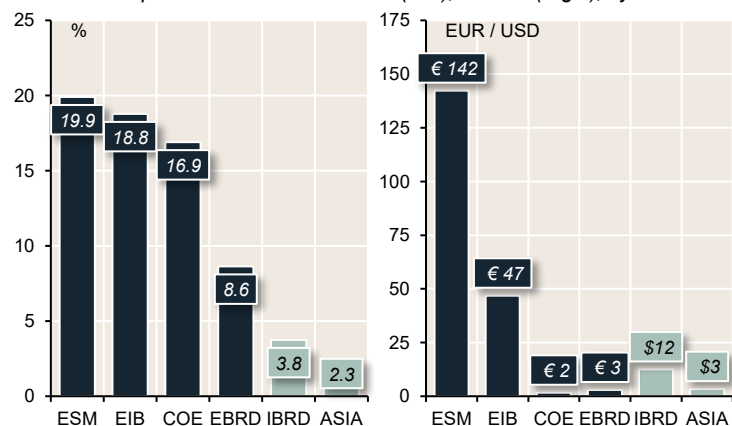
General government expenditure as a share of GDP: 2026



Source: NBC, IMF, Bloomberg | Note: Darker bars denote G7 nations

Chart 7-8: Visualizing SSA exposure to France sponsorship

Subscribed capital from France: % of total (Left), amount (Right), by select SSA

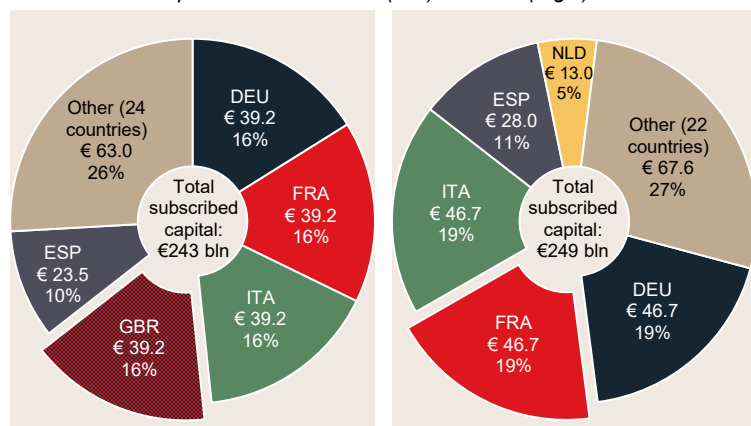


Source: NBC, Issuers | Note: Lighter bars denote USD-based SSAs, for added context

Diversified government sponsorship is a longstanding strength of MDBs. We highlight above issuers with greater exposure to French subscribed capital. While a French withdrawal is not our base case, we recognize the uncertain climate. Even if support was threatened/disrupted, European SSAs have shown balance sheet and credit resilience, as demonstrated by the U.K.'s EIB exit.

Chart 9-10: A case study of the UK's departure from EIB

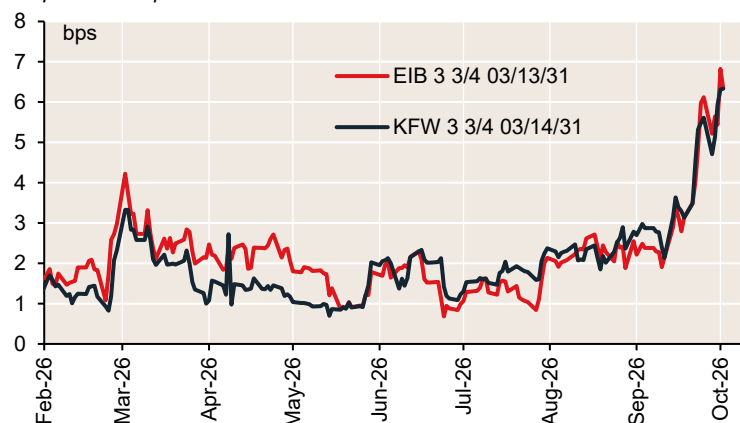
EIB subscribed capital breakdown: 2019 (Left) vs. latest (Right)



Source: NBC, EIB | Note: In each case, top 5 shareholders shown

Chart 11: SSA valuations were softer in September...

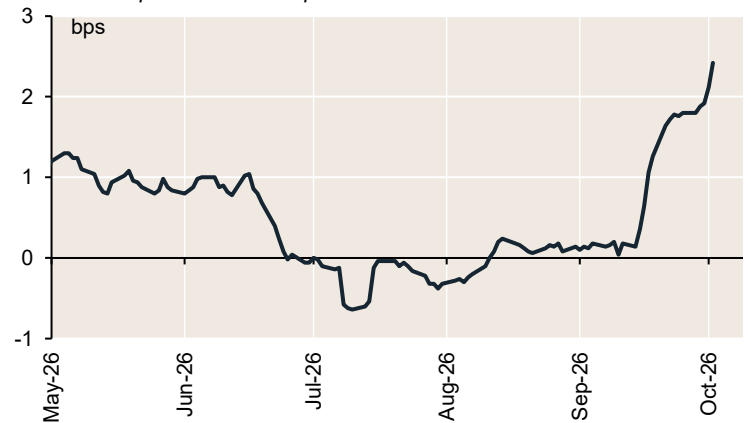
G-spreads of representative 5Y USD benchmark issues from EIB and KfW



Source: NBC, Bloomberg | Note: Yield spread (mid) is 5D moving average

Chart 12: ...with EUR basis wider for French-exposed names

EIB-KfW G-spread basis on representative 5Y EUR benchmark issue



Source: NBC, Bloomberg | Note: G-spread (mid) basis is 5D moving average

SSA spreads have widened in recent weeks. In our view, this reflects a healthy back-up in broader risk tone, with softness also evident across IG markets. Names with greater French exposure have underperformed, though that weakness has been confined to EUR issues. USD benchmarks from European supras continue to trade broadly in line with other core names.



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