



April 27, 2017

French Elections, the Eurozone, and the EU's Fate After the First Round¹

FIRST ELECTORAL STEP COMPLETE

Pro-EU reformer wins first round. Last Sunday, Emmanuel Macron, an advocate of European Union (EU) integration, domestic tax reform, and regulatory relief, [won a plurality in the first round of the French presidential election](#) with 24 percent of the vote. Marine Le Pen, who wants to bring back the French franc and call a referendum on leaving the EU, finished second with 21.3 percent. The runoff election will take place on May 7th.

Positive market reaction. Various market indicators—among them a rise in the euro's international exchange value, a rise in European stock indices, and a drop in the risk premium on French bond yields relative to German bunds—signaled relief at Macron's plurality win, and opinion polls show a wide lead for Macron over Le Pen in the next round.

Mainstream parties closer to Macron. Voters supporting mainstream parties, Les Republicans and the Socialist Party, whose candidates finished third (19.9 percent) and fifth (6.4 percent), respectively, are more likely to support Macron than Le Pen. The fourth-place finisher, Mr. Mélenchon (19.5 percent), while also an EU critic, is a far-left socialist whose supporters are considered unlikely to vote for Le Pen. However, Mélenchon's refusal to endorse Macron—as the other candidates have—could cause his supporters to stay home in the second round, [which could benefit Le Pen](#).² Her statist economic platform also may hold some attraction.

CHALLENGES AHEAD

Economic policy conundrum. High unemployment rates, large migrant populations, and terrorist attacks have unsettled French voters. [France has 10 percent unemployment and a large share of temporary workers](#), but staunch opposition to reforming labor laws persists.³ While most French voters do not necessarily favor leaving the Eurozone, many are resistant to policies they

Key Points:

- *Market reaction to the first round vote was positive as risks associated with "Frexit" receded.*
- *Many French voters oppose labor market reforms; blame Eurozone for domestic difficulties.*
- *Political mandate for pro-growth reform still in question.*

¹ Also see Joint Economic Committee report, "The French Election, the Eurozone, and the Fate of the EU," April 21, 2017; <https://www.jec.senate.gov/public/index.cfm/republicans/2017/4/french-elections>

² "How Marine Le Pen can steer a narrow path to victory in France," *Financial Times*, April 24, 2017; <https://www.ft.com/content/186f7f50-28f6-11e7-bc4b-5528796fe35c>

³ "Round Two Will Challenge Ideas on Nation's Workers," by Greg Ip, *The Wall Street Journal*, April 24, 2017 (print edition). In 2015, 60 percent of young workers were on temporary employment contracts. <https://www.wsj.com/articles/french-election-will-signal-nations-commitment-to-economic-reform-1492964748> (link to earlier version).

view as shrinking the benefits of the social welfare state and look toward outside forces as the cause of their difficulties.

Incumbent President Francois Hollande and Emmanuel Macron, who was his economics minister at the time, managed to implement only modest changes to French employment law. Still, this contributed to an erosion of public support for Hollande, which fell to a record low of 4 percent in late 2016. More than 40 percent first round voters chose one of the two Eurosceptic party candidates.

Leaving the Eurozone, however, will not accelerate real economic growth in France. Positive market reactions after the first round of voting likely relate to those mentioned in last week's Joint Economic Committee report, "[The French Election, the Eurozone, and the Fate of the EU](#),"⁴ on the exchange rate risk of France reverting to its own currency; the loss of transactional efficiencies the Eurozone affords; and the possibility that national monetary policy would lead to expansion of domestic social benefits.

Uncertain political mandate. A new parliament will be elected on June 11 and 18 and choose the next prime minister. Emmanuel Macron's party, En Marche, is new and does not hold any seats in the National Assembly while Le Pen's party, the National Front, holds only two seats out of 577. Absent a huge gain by the party of the winner in the presidential runoff election that at least approaches a parliamentary majority, a different party may choose the future prime minister.

If the president and the prime minister are from different parties (the French call this "cohabitation"), and if the next prime minister is reliant on a shaky parliamentary coalition, implementing substantial domestic economic reforms may not be feasible.

⁴ "The French Election, the Eurozone, and the Fate of the EU," April 21, 2017;
<https://www.jec.senate.gov/public/index.cfm/republicans/2017/4/french-elections>