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Rates Spark: Hawkish ECB not helping French government bonds

French government bond (OAT) spreads face more widening pressure as political uncertainty adds to the precarious fiscal situation. But spillovers to other markets remain limited. Elsewhere, for thoughts on Friday s Jackson Hole Symposium and the US Treasury buyback story see here and here

France is moving into focus given its precarious fiscal position and added layer of political uncertainty

EUR rates face a hawkish ECB and scrutiny of France

European rates have backed up again over the past few sessions, with the 10y Bund yield back at 3.25%. The backdrop is one where the relief in energy markets has proved only fleeting, especially as natural gas prices in Europe have once again come closer to recent peaks. The European Central Bank itself was quick to signal that it stands by its hawkish intentions, and Isabel Schnabel is more likely to reiterate that stance at the Jackson Hole Symposium today.

France is increasingly moving into the focus of markets given its precarious fiscal situation and the added layer of political uncertainty. Last night saw the first presidential debate of the main contenders that included Le Pen and Melenchon. Polling has given rise to prospects of the latter advancing to the second round run-off in the elections amid a more fragmented political centre. Markets see Melenchon as potentially more disruptive.

10y French government bond spreads over their German peers have widened beyond 85bp in the past weeks; thus closing in on the peak of 2024. Spreads are also 3bp above their Italian peers, which suggests that a high uncertainty premium is already baked into the spread. Italy remains lower rated, still shows higher debt levels and is potentially also more exposed to ongoing geopolitical turmoil. But for now the market is more concerned about the worsening trajectory of France and headline risks are bound to increase.

That said, after Friday's market close, Fitch has scheduled a review of its A+/Stable rating for France. We doubt that the agency will update its assessment ahead of the budget with limited new information thus far to justify changes.

Friday's events and market views

The highlight will be Fed Chair Warsh speaking in the European afternoon at Jackson Hole. Even though we don't expect much to work with, all words will be weighed carefully by markets. In terms of data, we have US payroll revisions which could give a feel for the accuracy of payroll figures in 2026. We also get some interesting data from the eurozone, including French and Spanish CPI figures for August. Headline numbers are expected to nudge slightly higher. We also have confidence numbers for the eurozone aggregate, which consensus sees improve slightly versus the previous month.

Italy will auction 5y BTP, New 10y BTP, 8y CCTeu and 9y CCTeu for a total of €8.5bn.

Author

Benjamin Schroeder
Senior Rates Strategist
benjamin.schroder@ing.com

Michiel Tukker
Senior UK & Eurozone Rates Strategist
michiel.tukker@ing.com

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