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MACRO UPDATE: FRENCH POLITICS, MERKEL, ECB

Berenberg Macro Flash

FRANCE: THE RACE IS ON

With a late surge in support for ex-prime minister Francois Fillon, the first round of the centre-right presidential primary this Sunday has turned into a three-way race. Besides Fillon, his former boss, ex-president Nicolas Sarkozy, and another ex-prime minister, Alain Juppé, could advance into the run-off on 27 November. The victorious centre-right candidate will be the top favourite to win the presidential election on 7 May 2017. If opinion polls are any guide, either of the three would likely beat Marine Le Pen from the ultra-right Front National in the run-off presidential vote, with Juppe doing so more decisively than the other two. The outcome of the Republican primaries on 20 and 27 November can depend very much on voter turnout. If mostly core Republican supporters cast their vote, Sarkozy would benefit. The more centrist or centre-left voters show up, the better for centrist Juppe. Despite some recent slippage, Juppe tends to do better in overall opinion polls rather than in those restricted to the core Republican base. Of course, if more Front National rather than centrist voters take part in the Republican primaries, the impact could be different. The most recent momentum is a bit on Fillon's side.

All three leading centre-right candidates propose serious economic reforms, with Fillon sounding most radical - almost Thatcherite - and Sarkozy least convincing. Of the three, Juppe is the most strongly pro-EU and Fillon the least so. Fillon and, to a lesser extent, Sarkozy come across as soft versus Putin whereas Juppe is most in line with the EU position that serious sanctions against Russia must be maintained until Russia stops misbehaving in Ukraine.

Of the three main contenders in the Republican primaries, Juppe seems to have the broadest appeal beyond the centre-right. His chances of enlisting significant centre-left support in the final round of the presidential vote to beat Marine Le Pen would thus be even better than those of Sarkozy and Fillon. Remarkably, the widespread anti-establishment sentiment in France is not just bolstering ratings for the Front National's Marine Le Pen, who scores around 30% in opinion polls. It also strengthens the more reformist politicians in both the centre-right (Fillon, Juppe) and the centre-left (Macron, Valls). With luck, French politics in 2017 could be more an opportunity - namely a wave of pro-growth reforms mirroring earlier reforms in Germany (2004), Spain (2013-2014) and Italy (2015) - than a risk (Le Pen as president).

We often get asked why we see only a low probability that Le Pen will win in May 2017. Well, the tail risk does exist. It would be the biggest potential threat to the EU and the euro. We need to watch it very closely. An opinion poll suggesting that she clearly won't make it can be wrong. However, Le Pen has been around for a long time. Unlike the Brexit vote and the Trump campaign, she is not a novelty that pollsters can't get a grip on. As discussed in our [Chart of the week - After Trump: could France be next?](#), French opinion polls did not systematically underestimate her support in French elections in the last four years. Of course, shifting voter turnout patterns can introduce an extra element of uncertainty. See also our [Update on European political risks](#)

GERMANY: WILL SHE, WON'T SHE?

German chancellor Angela Merkel is widely expected to seek - and win - a fourth term as German chancellor at the national election in September 2017. But she has not said so yet, which leaves a nagging tail risk. This Sunday, she may finally take a big step towards clarifying the issue. Some observers in Berlin expect her to announce at a leadership conference of her party whether she wants to stand for re-election as CDU



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chairwoman at the upcoming CDU party congress on 6-7 December. If so, that would be taken as a clear hint that she will also run for office as chancellor again, announcing that decision either just before or at that CDU congress in early December or – at the very latest – after agreeing with the CDU’s Bavarian partner CSU on a joint campaign approach in early January.

As discussed before, we expect support for Merkel’s CDU/CSU to rebound modestly from the current level of 33% to at least 35% as the election approaches, leaving behind some of the recent mid-term blues. Under realistic assumptions about the potential strength of other parties, a share of the popular of 35% or more would probably mean that no realistic coalition could be built against her CDU/CSU next autumn. See [Up-date on European political risks](#).

ECB MERSCH: PREMATURE TO REDUCE ECB STIMULUS

No surprise. Even according to ECB board member Yves Mersch, who is usually counted among the ECB hawks, it would be premature to talk about reducing the ECB stimulus. Noting that the US Fed was “very careful in normalising policy” and pointing at the “fragility of the European growth path”, Mersch emphasised on Thursday according to a Reuters report that “I’m not off the mark if I say that the ECB will also do the same, acting with the necessary caution”.

Pundits including us expect the ECB to prolong its current €80 billion monthly asset purchases by at least three and more likely six months beyond March 2017 before finally starting to taper, announcing that decision to extend purchases at its 8 December meeting. In addition, the ECB will likely make some technical changes to its programme to broaden the scope of eligible (German) paper without changing the capital key distribution of purchases or breaking new ground by venturing into purchases of major new asset classes such as bank bonds or equities.

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