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MONDAY MACRO UPDATE: FRENCH, ITALIAN AND GERMAN POLITICS

Berenberg Macro Flash

FRANCE: NO LEFT-WING ALLIANCE (YET)

President Marine Le Pen? The only chance for the anti-EU right-winger to win the French election would be if she would face an equally unelectable candidate in the run-off round on 7 May. Fortunately, this remains unlikely. Over the weekend, hardline Socialist candidate Benoit Hamon and the communist-backed candidate Jean-Luc Melenchon did not edge closer to a deal that could give Hamon a chance to make it into the run-off vote. Instead, Melenchon mused that he does not want to “hang on to the hearse” of the Socialist Party whereas Hamon complained about “fairly brutal” statements by Melenchon. However, Hamon did not close the door to further discussions with Melenchon.

Opinion polls for the first round of the presidential election on 24 April project that Le Pen will come first with some 26%, ahead of the centrist reformer Emmanuel Macron (20%) and the centre-right reformer Francois Fillon (19%) followed by Hamon (15%), Melenchon (11%) and Green candidate Yannick Jadot (2% on average for the last 3 polls). In the last few polls, Macron seems to have slipped marginally whereas Fillon has stabilized. If Melenchon withdraws and all his supporters back Hamon on 24 April, the candidate of the united left could get 26% (or 28% if Jadot also withdraws). That would put Hamon ahead of Macron and Fillon. If voters faced a choice between Hamon, who seems to believe that the 35 hour workweek was a mistake and has argued for a 32 hour workweek instead, and ultra-right Le Pen, the outcome of the vote on 7 May could become hard to predict. Hamon would probably have a narrow edge over Le Pen in such a contest.

The weekend news suggest that forming a left-left alliance remains very difficult. Although Hamon’s separate talks with the Green candidate Jadot are reportedly progressing well, support from the Greens for Hamon would not make a decisive difference. And even if Hamon could eventually persuade Melenchon to withdraw in his favour, Hamon would still have to overcome serious obstacles to make it into the run-off round on 7 May.

1. Hamon and Melenchon disagree on major aspects of policy. While Melenchon rails against many aspects of the EU in the French hard-left tradition that views the EU as an Anglo-Saxon conspiracy against French workers, Hamon merely wants some reforms of the EU. Finding common ground won’t be easy.
2. Some mainstream Socialist voters may not follow Hamon into a hypothetical alliance, defecting to Macron instead.
3. A left-left alliance would put pressure on the old liberal stalwart Bayrou to refrain from running. That could add a couple of percentage points to support for Macron and Fillon.
4. In case of a left-left alliance, more centre-right politicians may ask scandal-stricken Fillon to withdraw ahead of the 17 March deadline for nominating candidates. A fresh face for the centre-right Republicans would have a better chance to prevail against a leftist candidate in the first round and make it into the final run-off.



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But what if the unlikely worst-case scenario materialises and Hamon picks up enough support from a potential left-left alliance to throw Macron and Fillon out of the race, only to lose against Le Pen on 7 May? At the subsequent parliamentary elections on 11 and 18 June, a hypothetical president Le Pen would almost certainly fail to win a majority of seats for her Front National. As president, she would still have significant discretion over foreign policy. However, she would have to appoint a prime minister who could win a majority in parliament and would have little room to push her anti-euro and anti-EU agenda. The likely result would be a protracted political stalemate and a serious dent to growth amid heightened uncertainty but not a “Frexit”. We’ll discuss this hypothetical “what if” scenario in more detail in a separate report.

ITALY: RENZI RESIGNS AGAIN

The ongoing power struggle in the centre-left Democratic Party seems to be reducing the risk of early elections. Having lost his constitutional referendum and his position as prime minister last December, Matteo Renzi also resigned as leader of the centre-left Democratic Party on Sunday. The 42-year old reformer wants to use the resulting leadership contest to re-affirm his hold over the party and possibly lead the party into new elections thereafter. If he would win both votes, he could be prime minister again.

Chances are that Renzi can still prevail against his party’s left wing. While the risk that he may then push for early general elections remains significant, it has probably receded somewhat in the last few weeks. A date for a party congress and subsequent primaries has not yet been set. It may even take until September before the leadership struggle has been settled. Also, the likelihood that Renzi would lose the left-wing of his party would rise further if he pushes too hard for early elections. In turn, that would make it more difficult for Renzi to win snap general elections. More likely, the current centre-left government will soldier on until regular elections early next year. That would give the Democratic Party more time to sort itself out – and the economy some extra time to recover before voters have to decide whether they would prefer to be governed by the radical and somewhat dysfunctional “Five Stars” instead.

GERMANY: SCHULZ BOUNCE CONTINUES

Support for the centre-left SPD remains on the rise. Two of the last six opinion polls now give a narrow lead for the SPD over chancellor Merkel’s CDU/CSU. Before the SPD had selected the ex-president of the European Parliament, Martin Schulz, as its new leader three weeks ago, the SPD had been 15 points behind. About one third of the “Schulz bounce” has come directly at the expense of the CDU/CSU, the remainder at the expense of the ultra-left Left Party, the right-wing AfD and the Greens. In a way, the Schulz factor is strengthening the German mainstream against the fringes. Many voters seem delighted that they are now offered a genuine mainstream “safe pair of hands” alternative to Merkel.

I still expect Merkel to prevail and win a fourth term on 24 September, with a 25% chance that Schulz could become chancellor instead. Once the novelty factor of Schulz wears off, the discussion will likely return to key policy concerns such as domestic security and how to send fake asylum seekers home again. These issues are not among the strong points of the centre-left. Still, the German election campaign has become genuinely competitive, with a solidly pro-EU, pro-euro and pro-NATO Merkel up against a centre-left challenger who would likely pursue very similar



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policies except for raising government spending a little faster, reversing some labour reforms and being slightly more open to the idea of Eurobonds and a joint deposit insurance for the eurozone.

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