

POLITICAL PULSE

## A French Election Correction

Monday, April 23, 2012

**Lorcan Roche Kelly**

### Whether with Hollande or Sarkozy, France will support European integration and reform.

Market reaction to the results of the first round of the French presidential election has been negative, with the CAC40 -- the main French stock index -- off over 3%. The sell-off is not unique to France, with [the collapse of the Dutch government](#) and disappointing [PMI data from Germany](#) adding to selling pressure. But to the extent that this market action is about the French election, we think it's an over-reaction: no matter who wins the second round on May 6, France will continue to play its role in the integration and reform of Europe. In the grand scheme of Europe's crisis, all else is details -- but it is also the stuff of headlines.

- The [results of the first round](#) of the French presidential election gave the expected outcome at the topline -- socialist candidate Francois Hollande and incumbent Nicolas Sarkozy are through to the second round.
- The strong performance of the far-right Front National leader Marine Le Pen and the worse than expected turnout for communist Jean-Luc Mélenchon (please see the table below) means that the second round is still very much in play.

Candidate	Result	Poll	Surprise
<b>Hollande</b> -- Socialists (center left)	28.6%	29.0%	-0.4%
<b>Sarkozy</b> -- UMP (center right)	27.2	25.5	+1.7
<b>Le Pen</b> -- National Front (far right)	17.9	16.0	+1.9
<b>Mélenchon</b> -- Left Front (communist)	11.1	14.0	-2.9
<b>Bayrou</b> -- Modern Democracy (center)	9.1	10.0	-0.7
<b>Others</b>	6.1	5.5	+0.6

Source: [Ipsos](#) and TrendMacro calculations

- The general expectation would be that Le Pen's votes would cross over to Sarkozy and that Mélenchon's votes would cross over to Hollande, with Bayrou's votes split. *If this were to happen, then Nicolas Sarkozy would win the second round.*
- So all the noise between now and the second round will be dominated by Sarkozy trying to get crossovers from Le Pen's base.

#### Update to strategic view

##### EUROPE MACRO:

Francoise Hollande will likely be the next French president, but we think it is premature to write off Nicolas Sarkozy's chances, given Marin Le Pen's surprising results. Whichever wins, it will matter less than the market seems to think. Hollande has the luxury of being able to get elected on banker-bashing rhetoric -- but he is a committed pro-European integrationist, and his internal policies will ultimately be driven by the logic of a fiscal adjustment that simply has to take place.

[\[Strategy Dashboard home\]](#)

([click here to use an interactive calculator](#) that shows how critical Le Pen's crossovers are going to be).

- According to the [first poll of voter intentions](#) after the first round, only 60% of Le Pen voters will cross over to Sarkozy, with 18% voting for Hollande and 22% undecided.
- That 18% of voters for far right Le Pen will now support socialist Hollande in the second round seems schizophrenic -- it means Le Pen's stronger than expected result was a generalized protest vote, not a lurch to the isolationist right. Nevertheless, as we warned (see "[The French Election Connection](#)" February 7, 2012), the strong performance of Le Pen is catching much of [the headlines this morning](#). But, from a strategic standpoint, we can eliminate the worst case outcome of a far right big-government French president for the next five years.
- Mélenchon's votes will cross over almost entirely to Hollande, with the poll showing a three way split for Bayrou's votes between Hollande, Sarkozy and "undecided."

So prepare yourself for two weeks of alarming rhetoric. But most of what will be said over the coming weeks will be nothing more than electioneering. Sarkozy will pander to the right, already saying the first round results shows the importance of [controlling immigration](#). And Hollande will pander to the left. He already proposes [a 75% tax on millionaires](#), and said in a [speech in January](#) (which for some reason is making the rounds today as though it were news), "My true adversary...has no name, no face...He will not be elected, yet he governs. My enemy is the world of finance."

What is missing from the debate is either candidate facing up to the fiscal challenges that France will have to overcome. Standard and Poor's [downgraded France](#) in January, and there have been [persistent market rumors](#) of another downgrade in the coming weeks.

- Sarkozy does not wish to talk about the problem, as any discussion would center on it being his fault as the incumbent. Instead, he [repeats his 2007 campaign](#) call to get the [ECB to do more to support growth with monetary policy](#).
- Hollande's policies do little to address the fiscal problems. Hollande is open to attack on his populist policies, but his lack of experience -- he has never even reached the rank of minister in government -- is another key weakness that Sarkozy [is already trying to exploit](#).

From a macro viewpoint, it actually [matters surprisingly little](#) whether Sarkozy or Hollande wins on May 6. Sarkozy would be better from a continuity standpoint, and his close relationship with German leader Angela Merkel means that the Franco-German axis would remain undisturbed.

- But when it comes to policies, either leader would be tied by France's need to address its [fiscal challenges](#). It is unlikely that Hollande would be able to force through his more draconian anti-

## Contact TrendMacro

On the web at  
[trendmacro.com](http://trendmacro.com)

Follow us on Twitter at  
[twitter.com/TweetMacro](https://twitter.com/TweetMacro)

Donald Luskin  
Menlo Park CA  
650 429 2112  
[don@trendmacro.com](mailto:don@trendmacro.com)

Thomas Demas  
Charlotte NC  
704 552 3625  
[tdemas@trendmacro.com](mailto:tdemas@trendmacro.com)

Lorcan Roche Kelly  
Sixmilebridge Ireland  
212 537 9067  
[lorcan@trendmacro.com](mailto:lorcan@trendmacro.com)

John Clinton  
Charlotte NC  
704 552 3629  
[jclinton@trendmacro.com](mailto:jclinton@trendmacro.com)

[\[About us\]](#)

finance measures and still maintain market access at the favorable rates France has enjoyed throughout the crisis.

- From a euro-area integration view, it is even possible that Hollande would be the better president (again, see "[The French Election Connection](#)"), as he is -- like most socialists in Europe -- very pro-European integration.

We expect lots of headline grabbing by both sides over the coming weeks, which will continue to roil markets. But we do not expect either leader to pose a significant risk to the progress made towards reform and integration at a European level.

---

### **Bottom line**

Francoise Hollande will likely be the next French president, but we think it is premature to write off Nicolas Sarkozy's chances, given Marin Le Pen's surprising results. Whichever wins, it will matter less than the market seems to think. Hollande has the luxury of being able to get elected on banker-bashing rhetoric -- but he is a committed pro-European integrationist, and his internal policies will ultimately be driven by the logic of a fiscal adjustment that simply has to take place. ▶