

France isn't the new Greece, but the warning signs are familiar

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France's political and fiscal challenges have sparked comparisons with the eurozone debt crisis. But while some warning signs look familiar, key differences mean today's France is not Greece in 2010 and fears of a new euro crisis are overblown

History hardly ever repeats. It rhymes. More than 16 years after the eurozone sovereign debt crisis, France's political and fiscal troubles have revived memories of that period. However, as is so often the case with memories, particularly those of experts and market participants who weren't even around at that time, they tend to be blurry and oversimplified. Luckily, yours truly and other members of ING's Research team were around at that time and can call themselves true euro crisis veterans.

Let me take you on a trip down memory lane. The euro crisis began with a revision, not a recession. In October 2009, the newly elected PASOK government of George Papandreou announced that the 2009 budget deficit would be around 12.7% of GDP, roughly double what Athens had previously reported. Eurostat later put the final figure at 15.4%. Overnight, the problem was no longer the size of the hole; it was that nobody had known how deep it was. Suspicion that Greece had fought its way into eurozone membership with creative accounting accompanied the entire euro crisis.

After the statistical revelation, the numbers were brutal: public debt was close to 130% of GDP and heading for 150%. The current account deficit had hit around 15% of GDP in 2008: Greece was borrowing abroad not only to fund its state but its entire economy. Unit labour costs in Greece had risen much faster than in Germany since euro entry. Interestingly, markets did not panic at once. When the revision came out, the 10-year Greek spread over Bunds was around 130bp, about where France trades now. It took six months of failed promises, rating downgrades and EU dithering to turn that into a funding crisis.

Shortly before Greece finally received a European bailout, and the infamous troika of the European Commission, the ECB and IMF basically took over policymaking in Greece, the spread between Greek and German debt was above 900bp. And actually it was above 3000bp two years later, at the time of the second bailout and haircuts on Greek debt.

It didn't take long before the debt crisis spread from Greece to other European capitals. Not at once but over two years, with spreads vis-à-vis Germany reaching around 1500bp in the case of Portugal, 1100bp in the case of Ireland and around 600bp for Spain and Italy. The transmission channels of contagion differed. While the bailout of its banks blew up the Irish budget deficit to 32% of GDP, Spain saw its real estate market imploding with regional banks going bust, Portugal suffered from an enormous current account deficit and high private debt and, last but not least, Italy got into trouble due to high government debt, low growth and a lack of political credibility. What these countries had in common was a lack of market confidence in the existence of a credible lender of last resort and the unresolved doom loop between banks and sovereigns.

It took Mario Draghi's 'whatever it takes', a multi-layered firewall of new European (rescue) institutions,

as well as the political will in European capitals to implement austerity measures and structural reforms, to stop the crisis.

We receive many questions about whether France is the new Greece and whether we are stumbling into the next euro debt crisis. And, indeed, at least at first glance, some numbers are worrying: France's debt ratio is now similar to that of Italy in 2011 and Greece in 2009. The French fiscal deficit is wider than Italy's was then. The primary deficit – the gap before interest – is close to 3% of GDP. Closing it requires a political consensus that France has not produced since the 1970s. Most worrying is the French track record of missing its own and European targets for years, if not decades. Greece's credibility was destroyed by false statistics; France's is being eroded by false promises and the inability or unwillingness to start fiscal and structural reforms.

While these elements are clearly frightening, there are also significant differences between France now and Greece back then. While Greece had a substantial current account deficit, France's current account is basically in balance, the household savings rate is at around 18% and the effective interest rate France pays on its whole debt stock is still below nominal GDP growth. Greece in 2010 paid around 5% on its debt stock while the economy was shrinking. France has a fiscal problem but not a funding problem. What's more, the eurozone now has a firewall that it didn't have 16 years ago. Admittedly, the firewall has been constructed for smaller eurozone countries, not for France or Italy.

All of this means that fears about a new euro debt crisis are overdone. Fears about the political ability and willingness to bring national economies and the entire EU on course for reforms and sustainable public finances, unfortunately, are not.

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