

French Bonds: Not likely a Banking Crisis

26 October 2026

Key Takeaways:

- France's fiscal and political challenges are real, and volatility may remain elevated. However, the rise in French sovereign yields does not automatically imply a deterioration of similar magnitude in the credit fundamentals of large French banks.
- For French banks, the recent weakness in their bonds means yields are reaching attractive levels. We think the large banks are generally healthy with strong capital ratios, and do not think the banks will face a systemic crisis like Silicon Valley bank or Credit Suisse.
- There have been mark-to-market concerns on French bank bonds, but we do not think the credit quality of the French banks is impaired.
- **We remain comfortable with bonds that are senior in the capital structure. Within junior subordinated bonds or AT1s, we think that investors should focus on quality issuers and strong structural features (i.e. wider backend reset spreads).**

Do you hear the people sing?

Bond markets interpreted this as evidence that France's fiscal position is unlikely to improve and could deteriorate over the medium term. Consequently, the 10-year OAT yield rose sharply to 5.07%, while its spread over German Bunds approached 160 basis points, well above its five-year average of around 60 basis points.

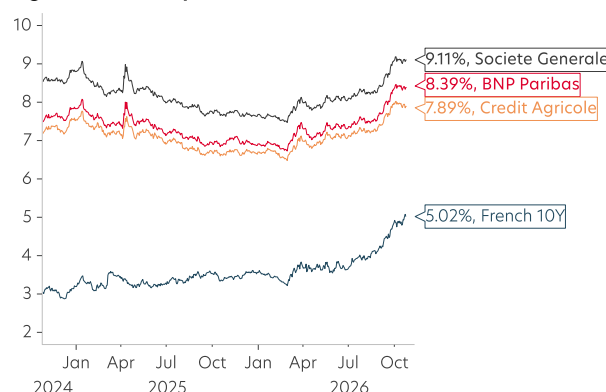
The deterioration in France's fiscal and political outlook is material and may keep market volatility elevated. However, investors should distinguish between sovereign risk, mark-to-market pressure and the underlying solvency of France's leading banks. Current evidence points to higher global base rates and greater French sovereign risk, rather than the onset of a domestic banking crisis.

We assess the large French banks as fundamentally resilient, supported by sound capital, solid deposit funding and diversified earnings. We remain constructive on senior and selected Tier 2 bonds. Current spreads reflect sovereign and political uncertainty more than an immediate deterioration in bank fundamentals. Investors may selectively accumulate where yields exceed long-term averages and issuer fundamentals remain stable.

For junior subordinated bonds and Additional Tier 1 securities, investors should favour quality issuers and remain selective on coupon-reset structures. Within

an issuer's AT1 curve, wider-resetting tranches offer a better buffer against non-call risk if credit spreads widen. We recommend holding existing positions and adding when yields appear to have peaked, rather than making a wholesale reduction in French bank exposure.

Figure 1: Example of French AT1 YTM



Source: Bloomberg, UOB Private Bank.

France fiscal health unlikely to improve in near term

France is expected to record a fiscal deficit of approximately 5.4% of GDP in 2026, while public debt is likely to reach 122% of GDP by 2027. The government aims to reduce the deficit to 5% in 2027, but political divisions and resistance to spending cuts could make this difficult. French government bonds have sold off as investors demand greater compensation for the country's fiscal and political

French Bonds: Not likely a Banking Crisis

26 October 2026

uncertainty. The 10-year French government bond yield reached 5% on 21 October 2026, its highest level since 2002. Its yield premium over 10-year German government bonds also widened to almost 170 basis points.

Figure 2: OATs vs Bunds spread near Euro debt crisis peak



Source: Bloomberg, UOB Private Bank.

Nevertheless, this is not solely a French event. Global bond yields have also risen because of inflation concerns, higher oil prices and changing monetary policy expectations. Since 1 September 2026, French bank AT1s had negative returns of 3.0%, compared with negative 2.7% for a broader group of European bank AT1s. French AT1s therefore underperformed by around 30 basis points. While this difference reflects greater concern about France, most of the absolute decline appears to have been caused by higher interest rates and near term spread widening, rather than a sharp deterioration in French bank fundamentals.

Are French banks in difficulty? We do not think so

Higher sovereign yields can affect banks by raising funding costs, leading to higher cost of capital for companies and weakening the domestic economy. If these conditions persist, slower growth could eventually result in higher credit losses. French bank spreads may also widen because investors often apply a higher country-risk premium to banks whose home sovereign is under pressure.

However, France's leading banks entered this period with sound capital, liquidity and deposit positions. Their diversified businesses and international operations also reduce their dependence on the French economy alone. They also fund a significant portion of their activities through customer deposits, reducing their dependence on short-term wholesale markets.

For example, BNP Paribas reported a CET1 ratio of 13.0% at the end of June 2026, while Société Générale reported a Common Equity Tier 1 capital ratio of 13.2%, higher than the regulatory requirement of 10%. For BNP, its global operations across commercial banking, insurance, asset management, securities services and corporate and investment banking provide multiple sources of earnings and reduce its reliance on France alone.

Current market conditions therefore represent primarily a valuation and funding-cost shock, rather than an immediate solvency shock. Lower bond prices do not, by themselves, indicate that the banks are approaching capital triggers, coupon restrictions or resolution. The longer term risk is that French fiscal stress becomes prolonged and spreads in the form of higher funding cost and weakening asset quality.

What does this mean for bondholders?

For senior bonds, we remain constructive. Senior debt offers the greatest protection within the bank capital structure and is mainly affected by interest rates, credit spreads and the bank's overall financial strength. For investors able to tolerate short-term volatility, the higher yields available from leading French banks offer a more attractive entry point.

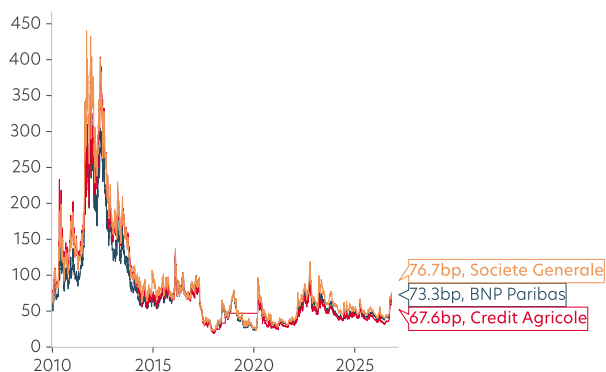
We also remain comfortable with selected Tier 2 bonds. Tier 2 debt carries greater risk than senior debt because it absorbs losses under severe stress. However, it normally has a defined maturity and does not carry the same coupon-cancellation and perpetual-extension risks as AT1s.

French Bonds: Not likely a Banking Crisis

26 October 2026

AT1s require greater selectivity. These securities are perpetual, their coupons may be cancelled, and their principal may absorb losses under specified conditions. Their prices can also fall sharply when investors become less confident that they will be called. Hence, within the AT1 space we prefer quality issuers and remain very selective on coupon reset structure, preferring the wider resetting tranches within an issuer's AT1 curve to buffer against non-call risks should credit spreads widen.

Figure 3: French banks' CDS spreads remain muted relative to recent history



Source: Bloomberg, UOB Private Bank

Source: Bloomberg, UOB Private Bank.

Conclusion: Vive la France, low risk of near-term default

French fiscal and political uncertainty are likely to keep sovereign and bank bonds volatile. However, the current situation does not point to an immediate crisis among the leading French banks. Their capital, liquidity, deposit funding and earnings remain supportive.

We remain comfortable with senior and selected Tier 2 bonds and would consider adding gradually on weakness. For AT1s, we think investors should favour strong issuers with strong structural features (i.e. wider backend reset spreads).

The main downside risk is a prolonged loss of French fiscal credibility that keeps sovereign and bank spreads significantly wider, weakens the economy and restricts access to refinancing markets. Current conditions require close monitoring and careful bond selection, but not indiscriminate selling of fundamentally sound French bank bonds.

Disclaimer:

General

This document contains material based on publicly available information. Although every reasonable care has been taken to ensure the accuracy and objectivity of the information contained in this document, United Overseas Bank Limited ("UOB") makes no representation or warranty as to, neither has it independently verified, the accuracy or completeness of such information (including any valuations mentioned). UOB neither represents nor warrants that this document is sufficient, complete or appropriate for any particular purpose. Any opinions or predictions reflect the writer's views as at the date of this document and may be subject to change without notice.

The information contained in this document, including any data, projections and underlying assumptions, are based on certain assumptions, management forecasts and analysis of known information and reflects prevailing conditions as of the date of publication, all of which are subject to change at any time without notice. Past performance figures are not indicative of future results.

Not an offer or solicitation to any particular person

This document should not be regarded as an offer or solicitation to any particular person to transact in any product mentioned. Before deciding to invest in any product mentioned, please seek advice from your financial, legal, tax or other appropriate advisers on the suitability of the product for you, taking into account your specific investment objectives, financial situation or particular needs (to which this document has no regard). If you do not wish to seek such advice, please consider carefully whether any product mentioned is suitable for you.

Risks

An investment in any product mentioned in this document may carry different risks of varying degrees, including credit, market, liquidity, legal, cross-jurisdictional, foreign exchange and other risks (including the risks of electronic trading and trading in leveraged products). Nothing in this publication constitutes personalized accounting, legal, regulatory, tax, financial or other advice that regards the personal circumstances of a particular recipient. Please speak to your financial, legal or other appropriate adviser to understand the risks involved and whether it is appropriate for you to assume such risks before investing in any product.

Any description of investment products is qualified in its entirety by the terms and conditions of the investment product and if applicable, the prospectus or constituting document of the investment product.

Valuation

Product valuations in this document are only indicative and do not represent the terms on which new products may be entered into, or existing products may be liquidated or unwound, which could be less favourable than the valuations indicated herein. These valuations may vary significantly from those available from other sources as different parties may use different assumptions, risks and methods.

No liability

To the fullest extent permitted under applicable laws and regulations, UOB and its affiliates shall not be liable for any loss or damage howsoever arising as a result of any person acting or refraining from acting in reliance on any information, opinion, prediction or valuation contained herein.

UOB and its affiliates involved in the issuance of this document may have an interest in the products mentioned in this document including but not limited to, marketing, dealing, holding, acting as market-makers, performing financial or advisory services, acting as a manager or co-manager of a public offering, of persons mentioned in this document. UOB and its affiliates may also have alliances, contractual agreements, or broking, investment banking or any other relationships for the provision of financial services, with any product provider mentioned in this document. UOB and its affiliates may have issued other reports, publications or documents expressing views which are different from those stated in this document and all views expressed in all reports, publications and documents are subject to change without notice.

Others

Unless you are notified otherwise by UOB, UOB deals as a principal in any transaction which UOB has been instructed to effect, other than transactions relating to securities traded on an exchange, unit trusts and funds on your behalf where UOB acts as your agent.

Singapore. This document and its contents are intended for Accredited Investors (as defined in Section 4A of the Singapore Securities and Futures Act (Chapter 289)).

Hong Kong. This document and its contents are intended for "professional investors" (as defined in the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong) (the "SFO") and its subsidiary legislation) ("**Professional Investors**"). Shares

or debentures in a company may not be offered or sold in Hong Kong, by means of any document, other than (i) to Professional Investors; or (ii) in other circumstances which do not result in the document being a "prospectus" within the meaning of the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Chapter 32 of the Laws of Hong Kong)(the "**CWUMPO**") or which do not constitute an offer to the public within the meaning of the CWUMPO. Unless permitted to do so under the laws of Hong Kong, no person may issue or have in his/her possession for the purpose of issue, or will issue, or have in his/her possession for the purposes of issue, any advertisement, invitation or document relating to the securities, structured products or interests in collective investment schemes whether in Hong Kong or elsewhere, which is directed at, or the contents of which are likely to be accessed or read by, the public of Hong Kong, other than with respect to the securities, structured products or interests in collective investment schemes that are or are intended to be disposed of only to persons outside Hong Kong, or only to Professional Investors.

WARNING: The contents of this document have not been reviewed by any regulatory authority in Hong Kong. You are advised to exercise caution in relation to this document. If you are in any doubt about any of the contents of this document, you should obtain independent professional advice.

This document may only be distributed in countries where its distribution is legally permitted. This document is not directed to any person in any jurisdiction where (by reason of that person's nationality, residence or otherwise) such publications are prohibited. This document may contain proprietary information of UOB (or its product providers) and may not be reproduced or disseminated in whole or in part without UOB's prior consent.

If there is any inconsistency, or any difference in meaning between the English version and any translation of this document, the English version shall apply and prevail.

United Overseas Bank Limited. Co. Reg. No. 193500026Z

United Overseas Bank Limited is a licensed bank in Hong Kong and is a registered institution in respect of Types 1 (Dealing in Securities) and 4 (Advising on Securities) regulated activities under the SFO.