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This Sunday's second round of the French presidential elections has the capacity to create major waves. General expectations are for Emmanuel Macron to win his second mandate, albeit with a narrower margin than five years ago. But far-right populist and Eurosceptic Marine Le Pen also has a fighting chance, especially if abstention rates are high among voters on the left who would be unhappy with either outcome. This time, unlike five years ago, French banks appear less vulnerable to a nationalist-populist presidency.

A Le Pen victory would be an intensely disruptive event at any time but particularly now, when European unity and resolve are needed more than ever to support Ukraine against Russia's aggression. Thanks to France's central position on the continent (currently enhanced by its temporary EU presidency), a far-right victory would, on a geopolitical Richter scale, be on a par with Brexit and the advent of the Trump presidency, and arguably more disruptive than the Italian populists' electoral victory in 2018.

To nobody's surprise, a Macron electoral victory would leave French banks on their existing trajectory. But, unlike the presidential contest five years ago, this time around a Le Pen win, while an undesirable outcome for them, would not be a game changer either.

First, because the French banking sector has, on balance, displayed reassuring strength, common sense and stability in recent years. I have followed French banks for nearly 35 years, since before the great deregulation of the early 1990s, and I don't recall seeing the sector in the good financial, prudential and business shape it currently displays. Profitability is not stellar, but it hasn't ever really been, largely due to stubbornly high cost-income ratios that are worse than European averages.

Scope's bank rating team recently put out a report on French banks (French banks: a turbulent period but credit strength reassuring), which covers some of the sector's current strengths and caveats.

Second, the regulatory environment for banks, although in place for nearly a decade, is viewed with more confidence and appreciation now than it was five years ago. The Single Supervisory Mechanism has proved its mettle over several years. Its bank supervisors have not been found wanting, at least not as far as French banks are concerned. And an initially feared degree of dysfunctionality between the ECB and the French national competent authorities has not surfaced and is no longer a material worry.

Third, French banks shed their negative image during the pandemic, an image that had dogged them after the Global Financial Crisis. Not only have they restored and preserved solid prudential and financial fundamentals – including asset quality – they have also played an active and constructive role in providing finance to households and individuals during the pandemic, often in conjunction with financial support and guarantees from public-sector actors.

And, with Société Générale's recently announced exit from Russia through the sale of its local subsidiary to a local oligarch, a remaining blot on the bank and the sector's image will soon fade. Yet it would be reckless to gloss over the negative implications of a Le Pen presidency on France's banks and financial markets. It may not be game-changing but it may not be inconsequential either. I highlight some of the implications.

A far-right presidency could mainly affect French banks' international presence

Unlike her presidential campaign five years ago, Marine Le Pen is not advocating potential exit from the Euro Area this time around. Given the entrenchment of the euro in France, such a platform would have been a certain vote loser. Her insistence on more sovereignty vis-à-vis the EU, even if not couched in terms of directly fighting financial globalisation, can upset markets and foreign investors if Le Pen's Rassemblement National (RN) party gets into power.

The far-right campaign's focus is on limiting immigration, plugging France out of NATO's military structure, equidistance between the US and Russia, primacy of French laws vs. EU laws, climate-change scepticism, as well as some demagogic solutions to address French voters' main current fears – inflation and the cost of living. Banks and their policies and profits are not being directly attacked, as they were in the past by the far right (although to a lesser degree than by Jean-Luc Mélenchon's hard left).

Nevertheless, I believe that, given their universal-bank profile and substantial European footprint, the large French groups will not be happiest under a Le Pen presidency. Especially BNP Paribas, Société Générale and, to a lesser extent, Crédit Agricole, which have a more widespread European presence. As a reminder, all three of them as well as BPCE (mainly domestically oriented), were included in the FSB's list of the 30 global systemically important banks (G-SIBs) in 2021[1]. No other European banking sector has as many G-SIBs as France.

French banks are far more independent of French government policy than they have been in previous decades. Nevertheless, they were able to benefit from, and in turn supported, both France's lead role in an expanding and increasingly relevant EU (especially in the aftermath of the GFC), and its clout as the world's sixth-largest economy, highly integrated in Europe and globally.

In fact, the large French banks have been key actors in pushing for the globalisation of the French economy, accompanying the large French corporates in their international activities.

A far-right presidency should not affect the banks' domestic activities – lending to households and businesses – unless the country enters economic stagnation or recession (less likely). But it could raise red flags with respect to France's commitment to Europe and to globalisation in general – areas in which the large French banks have traditionally excelled. Being labelled as global does not earn praise from any populist government – left or right.

Domestic impact should be less relevant, but…

More ominously, if a Le Pen presidency follows an aggressive populist agenda (if that is what brought it to power), political hurdles could complicate efforts by the French banks to shrink their physical branch and back-office structures, which will entail substantial staff reductions. But, in an increasingly digitalised world, faling to reduce excess legacy capacity is not an option for banks, especially in France where the large groups have been lagging European peers in digital migration.

[1] https://bit.ly/3rARYkU

That being said, for more substantial steps to be successful, especially in domestic policies, a president needs legislative support, short of which political effectiveness would be blunted. Should Le Pen win the presidency, it is highly doubtful her extreme-right RN party would muster sufficient parliamentary power in the legislative elections in June.

Negative effect on Paris as a key EU financial centre

Not directly related to the banking sector but highly consequential nonetheless, a far-right nationalist-populist presidency could undermine existing efforts to build Paris as a top financial marketplace following Brexit. The Macron administration has been relatively successful in increasing the attractiveness of Paris as key EU financial centre alongside Frankfurt and Amsterdam.

One notable achievement has been the post-Brexit relocation of the European Banking Authority from London to Paris, where the European Securities and Markets Authority has been headquartered since its inception more than a decade ago. It is unlikely that an RN administration, in and of itself, would motivate the European Commission and Parliament to consider relocating these agencies elsewhere in the EU. But the risk is less negligible than in the case of a second Macron mandate.

Beyond the location of European public institutions, hard nationalism and populism may dampen the enthusiasm of international investors or financial institutions considering relocation to Paris. Especially if labour reforms promised and partially implemented by the Macron administration, aiming for more labour flexibility and less rigidity, are postponed or abandoned.

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