

## Overview

---

**The French financial system continues to display resilience in the face of a series of shocks since 2020, and now faces the consequences of the war in Iran.** The outbreak of the Middle East conflict on 28 February triggered a negative supply shock in commodity markets, notably following the closure of the Strait of Hormuz, a critical transit route for around 20% of global hydrocarbon consumption.

**However, this shock is taking place in a very different context from 2022. Hydrocarbon inventories are much higher than at the time,** which explains why crude oil prices have risen relatively moderately. Sharp reductions in demand since the start of the conflict, particularly in East Asia, have also helped to limit price pressures, while the shock to liquefied natural gas (LNG) has been much milder than after Russia's invasion of Ukraine. Reductions in European demand since 2022 and an expansion of global liquefaction capacity have also contributed to price moderation.

**Nevertheless, price pressures are also affecting other commodities, not just hydrocarbons, leading to upward revisions to inflation forecasts.** In the baseline scenario for its June macroeconomic projections, the Banque de France raised its forecast for 2026 inflation to 2.5%, after 0.9% in 2025 (+0.8 percentage point compared with the March interim projections). Market participants now expect the Eurosystem to tighten its monetary policy going forward; as of 12 June 2026, they were pricing in between one and two additional 25-basis-point rate hikes by the end of the year, on top of the increase decided by the ECB Governing Council on 11 June.

### **The rise in long-term interest rates in G7 countries has increased vulnerabilities related to government finances**

**Expectations of further hikes in key euro rates have driven up sovereign yields, although without increasing significantly the risk premium on French debt.** The yield on French ten-year government bonds reached 3.75% on 12 June, representing a 40-basis-point rise since the start of the war. However, over the same period, the spread between the ten-year OAT and the German Bund only widened by 8 basis points only. The stability of France's risk premium reflects persistently strong demand for the country's debt, both historically and compared with other European countries. However, this demand will need to absorb the government's growing financing needs.

**If France fails to lower its budget deficit to at least 5% of GDP, the factors supporting its sovereign debt could be eroded further,** raising the risk of further downgrades by rating agencies. Such a scenario could lead to higher volatility and reduced liquidity in the market for French sovereign debt, which could potentially be amplified by investors pursuing short-term and procyclical strategies – notably hedge funds. The latter are particularly active in repo markets where they deploy highly leveraged arbitrage strategies involving OATs.

**The thematic chapter in this report analyses the functioning of the repo market and the emergence of vulnerabilities linked to the growing presence of hedge funds.** The trend is heightening the risk of sudden price fluctuations and creating channels of contagion to the broader financial system in the event of a liquidity shock. These vulnerabilities are being exacerbated by the concentration of transactions among a small number of market participants, the predominance of very short maturities and the use of risk management tools (haircuts and margin calls) that are sometimes insufficient and can prove procyclical in the event of a shock.

**A significant deterioration in sovereign financing conditions could spill over to French banks and corporates.** Given that sovereign debt issuance is expected to remain high in the euro area in 2026, particularly in France and Germany, it is essential to ensure a sustainable debt trajectory to maintain sound financing conditions for all economic actors.

**In June, the inflationary environment was already weighing on French government finances.** Various spending items are indexed to inflation, including pensions and family benefits. Moreover, around a tenth of France's debt takes the form of indexed bonds, meaning that part of the debt burden is directly tied to inflation. On the revenue side, any slowdown in consumption tends to reduce government tax receipts – both directly, as in the case of fuel duties which depend on the volumes sold, and more broadly via a decline in activity. Although financial aid for households and businesses remained targeted at the start of June and has only pushed up government expenditure very moderately, the war in Iran will have a non-negligible impact on the budget deficit in 2026.

### **Risky asset markets, especially US equity markets, remain vulnerable to a sudden reversal in investor sentiment**

**The war in Iran triggered only a moderate and temporary correction in equity prices, and markets quickly recouped their losses.** After falling markedly in the first four weeks of the conflict, equity markets subsequently recovered, with US technology stocks seeing particularly strong gains. Since equity markets – especially US indices – are still largely being driven by a small number of technology stocks, valuation ratios and market concentrations remain historically high. This means markets are particularly vulnerable to a sudden reversal in investor sentiment. A downward revision to the earnings outlook for technology stocks could trigger a disorderly correction, with potential spillovers to other markets.

**Investor appetite for US – and, to a lesser extent, European – corporate bonds also remains high.** The fact that corporate credit spreads remain narrow, despite the geopolitical context and macroeconomic risks, could indicate that investors are underestimating the credit risk for certain borrowers. The European corporate debt market has absorbed a wave of large-scale fund-raising by the US technology sector. Between October 2025 and March 2026, nearly two-thirds of net euro-denominated corporate bond issuance was by companies domiciled in the United States.

**The private credit market has expanded sharply over the past decade but experienced turbulence in early 2026.** Concerns emerged in the first quarter about the quality of loans originated in the sector and funds' high exposures to software firms. As a result, several large semi-liquid funds managed by US asset managers received significant redemption requests from retail investors. The sector's growing exposure to the AI sector also makes it particularly vulnerable to downward revisions to expected revenues. AI therefore poses two types of risk: first, the potential negative impact if increasingly indebted AI firms underperform expectations; second, the risk of losses for private credit funds exposed to the software sector in the event of strong competition from AI. The relative opacity of private credit, and its growing concentration among a few large, international asset management firms, further heighten its vulnerability and underscore the need for greater transparency.

**European and French financial institutions have limited direct exposure to private credit, but they could be affected if a shock was propagated to other asset classes.** These exposures can take the form of bank loans, often secured by fund assets, while insurers may be exposed directly as investors in private credit funds. In Europe, under a narrow definition of private credit, these exposures account for only a small share of total assets for banks and insurers.

### **The deterioration in the international environment could pose a risk for small and medium-sized enterprises and low-income households**

**The negative supply shock caused by the geopolitical crisis is dragging on French growth.** In its June 2026 macroeconomic projections, the Banque de France lowered its 2026 growth forecast from 0.9% to around 0.5%, citing a disappointing first quarter, a deterioration in the global environment and a

resurgence of inflationary pressures. It presented several scenarios in its projections that are consistent with those published by the European Central Bank (ECB) for the Eurosystem on 11 June. In its “adverse” and “severe” scenarios, the path of oil and gas prices is based, respectively, on the 75<sup>th</sup> and 95<sup>th</sup> percentiles of the implied price distribution derived from options on energy futures. Both scenarios reflect a more protracted conflict, with stronger pressures on global oil and gas supplies that can no longer be mitigated by available reserves. The “favourable” scenario corresponds to a faster and steeper decline in energy prices compared with the assumptions in the baseline scenario. In the adverse scenario, France avoids slipping into recession over the full year 2026, with weak but positive growth of 0.3%. In the severe scenario, gross domestic product (GDP) remains flat in 2026 and then contracts slightly by 0.1% in 2027, while inflation rises significantly, reaching 4% in 2026 and 3.9% in 2027. Lastly, under the favourable scenario, the slightly faster fall in energy prices has positive effects on both activity and inflation.

**French firms have demonstrated resilience to the successive shocks since 2020, but their high aggregate debt levels leave them particularly vulnerable to potential revenue shocks.** Their debt-service-to-EBITDA (earnings before income tax, depreciation and amortisation) ratio increased in 2025 and remains higher than in the other main euro area countries. This gap reflects a higher consolidated-debt-to-GDP ratio for non-financial corporations (NFCs), and the fact that the rise in interest rates compared with 2021 has already been passed through to corporate balance sheets.

**Since early 2025, business failures have been mounting steadily and can no longer be attributed solely to a post-pandemic catch-up effect.** Additional factors need to be considered, including higher energy prices and the trade war. The rise in failures is mainly concentrated among intermediate-sized enterprises and small and medium-sized enterprises (SMEs), while business creations remain largely driven by small enterprises, particularly micro-enterprises.

**The French commercial real estate market showed signs of stabilising in 2025 but lost momentum again in early 2026.** The sector is particularly sensitive to financing conditions, which affect economic agents’ investment capacity, and to economic activity, which influences rental demand. However, credit risk remains contained in the commercial real estate sector, due to a low default rate and the very limited share of these exposures in banks and insurers’ asset holdings. Moreover, liquidity pressures in real estate investment funds appear to be easing gradually.

**Heightened macroeconomic uncertainty is weighing on the recovery in the residential real estate market.** Household investment slowed in the first quarter of 2026, and rising household borrowing rates could continue to dampen demand for housing loans. The pick-up in French residential real estate prices is also less marked than in the rest of the euro area. This is in part linked to the prevalence of fixed-rate lending for house purchases in France, which creates a certain amount of inertia in the market that slowed the price falls when interest rates rose in 2022. Defaults on housing loans are continuing to rise at a moderate pace, reflecting the gradual increase in the unemployment rate since 2023 to its highest level since 2021.

### **Banks and insurers remain resilient in an uncertain environment**

**French banks benefit from diversified business models and limited exposure to those sectors most sensitive to fossil fuel prices.** In the first quarter of 2026, they also appeared to have very limited exposure to counterparties in countries linked to the conflict in Iran. Household and corporate credit risk is rising, but French banks continue to report robust earnings growth and maintain strong solvency and liquidity positions. Their exposure to private credit also remains limited.

**The insurance sector's solvency position has improved and is well above regulatory requirements.**

Life insurance revaluation rates have been supported by higher investment returns and the mobilisation of profit-sharing reserves accumulated in previous years. These revaluations have made life insurance policies more attractive to savers, resulting in higher gross inflows and lower redemptions, pushing net inflows up to record highs. After deteriorating following the inflationary shock in 2022, underwriting profitability in the non-life segment improved in 2024 and 2025, returning towards levels last seen before the high inflation episode. Insurers remain only marginally exposed to private credit, mainly through their diversified general account holdings.

**The materialisation of geopolitical risks is increasing structural risks, particularly cyber risk and energy dependency**

**Cyber risk is being intensified by the Middle East conflict and the growing threat of hybrid warfare.**

The *Autorité de contrôle prudentiel et de résolution* (ACPR – Prudential Supervision and Resolution Authority) and the Banque de France have not observed an increase in the number of cyberattacks targeting the financial sector as a direct result of current geopolitical tensions. Nevertheless, the geopolitical component of cyber risk remains elevated, even though it has only materialised to a limited extent in France to date. The emergence of advanced AI models (or “frontier AI”), which are capable of quickly identifying critical vulnerabilities and can be used for malicious purposes, represents a structural shift that calls for adaptation by financial institutions.

**Finally, the initial consequences of the war in Iran are a reminder that Europe's dependence on imported fossil fuels creates inflationary pressures and financial instability risks.** Over the past decade, France has taken significant steps to decarbonise its economy; however, it remains reliant both on fossil fuels and on the countries that export them. These dependencies expose it to geopolitical uncertainties that can generate substantial economic and financial risks. To reduce these dependencies and limit the risks, France is pursuing efforts to diversify its energy supplies and decarbonise its economy.

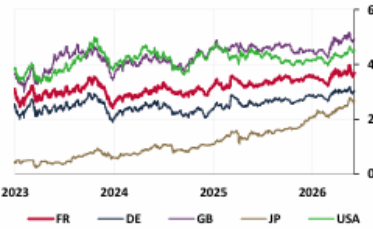


# ASSESSMENT OF THE FRENCH FINANCIAL SYSTEM RISKS | JUNE 2026

CYCLICAL RISKS

## Geopolitical crisis and supply shock

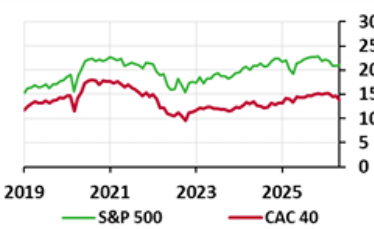
### Sovereign debt risks



Evolution of 10-year sovereign yields

- High public debt and rising interest burden
- Reduced investor demand on the long end of the curve
- Leverage positions on US Treasury securities
- Liquidity of French primary and secondary markets

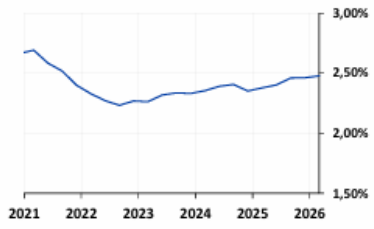
### Risk of disorderly market correction



Evolution of forward price-to-earnings ratios for France and the US

- High concentration of valuations
- Low risk premia
- Highly leveraged positions of certain funds
- Exposures of European non-bank financial intermediaries to US assets
- Resilient market infrastructures
- Diversified investors

### Risk of supply shock propagation



Share of non-performing bank loans (stage 3) out of total bank loans in France

- Downward-revised growth outlook and inflationary pressures
- High indebtedness of certain NFCs
- Vulnerabilities related to the development of private credit
- Decarbonized electricity production
- Low levels of non-performing loans
- Strong solvency of banks and insurance companies

STRUCTURAL RISKS

### Cyber risks

- Frontier AI models: exploitation of vulnerabilities facilitated by artificial intelligence
- Geopolitical tensions
- Crisis exercises
- Investments in cybersecurity
- Implementation of DORA

### Tokenization risks

- Rise of crypto-assets, particularly non-bank stablecoins
- Development of DeFi
- Preparations for a central bank digital currency (wholesale and retail)

### Climate-related risks

- Exposure to physical and transition risks
- Delays in implementing transition policies
- Progress in climate risks supervision



Risk outlook



Materialized risk



Very high risk



High risk



Moderate risk

Vulnerabilities in blue

Resilience factors in green

## Measures taken by authorities

In line with its commitment to stabilise inflation at its 2% target over the medium term, the Eurosystem Governing Council decided on 11 June 2026 to raise the three key ECB interest rates by 25 basis points. With its 11 June decision, the Governing Council is well-positioned to address the uncertainty caused by the war. It will continue to closely monitor the situation and follow a data-dependent and meeting-by-meeting approach to determining the appropriate monetary policy stance.

In France, the *Haut Conseil de stabilité financière* (HCSF – High Council for Financial Stability) is continuing to pursue a macroprudential policy aimed at preserving the resilience of the financial system. At its meeting of 9 June 2026,<sup>1</sup> it highlighted the solidity of French financial institutions in global environment that remains fraught with uncertainties and vulnerabilities. In view of the economic and financial environment, and in the absence of signs of a tightening of credit supply, the countercyclical capital buffer (CCyB) rate was maintained at 1%. With regard to loans for house purchase, the standard governing the granting of loans<sup>2</sup> remained in force. Use of the flexibility margin available to banks under this measure stood at 17.5% in the first quarter of 2026, which was still below the 20% ceiling.

At the European level, the European Commission continued to implement its strategy for the Savings and Investments Union (SIU). In December 2025, the Commission proposed a set of legislative proposals to improve the integration and supervision of financial markets (the “Market Integration Package”).<sup>3</sup> The package proposes transferring direct supervisory power to the European Securities and Markets Authority (ESMA) for significant market infrastructure entities and crypto-asset service providers. It also recommends converting directives into regulations to limit national discrepancies and further harmonise the regulatory framework. In April 2026, the ECB published an opinion<sup>4</sup> supporting this initiative. The legislative proposals are currently being examined by the European Parliament and the Council of the European Union. From 11 February to 19 April 2026, the Commission also held a consultation on the competitiveness of the European Union (EU) banking sector,<sup>5</sup> to gather input on the factors influencing EU banks’ ability to finance investment, innovation and economic growth. The Eurosystem,<sup>6</sup> the European Systemic Risk Board (ESRB)<sup>7</sup> and French authorities (the Treasury, the *Autorité de contrôle prudentiel et de résolution* (ACPR – Prudential Supervision and Resolution Authority) and the Banque de France) all submitted responses, and these will inform the Commission’s report on banking sector competitiveness, which is due to be published in mid-July 2026. On 18 March 2026, the Commission also presented its proposal for “EU Inc.”,<sup>8</sup> a new single set of rules for European companies that is part of the EU’s 28<sup>th</sup> regime. The aim is to simplify and digitalise registration procedures to make it easier for businesses to set up and operate across the EU, while also making investment more attractive. Lastly, the European Single Access Point (ESAP), created under the EU regulation of 13 December 2023<sup>9</sup> as part of the SIU, was transposed into French law by Order 2026-31

---

<sup>1</sup> [HCSF \(2026\) – press release following the second-quarter meeting.](#)

<sup>2</sup> This standard imposes a maximum debt-service-to-income ratio of 35% and a repayment period limited to 25 years (or 27 years in certain specific cases).

<sup>3</sup> European Commission (2025), “[Market integration and supervision package](#)”, 4 December.

<sup>4</sup> “[Opinion of the European Central Bank of 9 April 2026 on proposals as regards the further development of capital market integration and supervision within the Union](#)”, 28 May.

<sup>5</sup> European Commission (2026), “[Targeted consultation on the competitiveness of the EU banking sector 2026 - Finance](#)”, 28 May.

<sup>6</sup> ECB (2026), [Eurosystem response to the EU Commission’s targeted consultation on the competitiveness of the EU banking sector](#), April.

<sup>7</sup> ESRB (2026), [ESRB Response to the European Commission consultation on competitiveness of the EU Banking](#), 17 April.

<sup>8</sup> European Commission (2026), “[Commission presents proposal for EU Inc.](#)”, 18 March.

<sup>9</sup> [Regulation \(EU\) 2023/2859.](#)

of 28 January 2026.<sup>10</sup> ESAP is an EU-wide digital platform that will centralise all public information relating to financial services, capital markets, sustainability and diversity. It will be phased in gradually as of July 2026 and will be fully accessible by 10 July 2027.

**The Eurosystem has developed a set of proposals to strengthen the macroprudential lens in the regulation and supervision of non-bank financial institutions (NBFI).** It notably recommends expanding the macroprudential toolkit to include an instrument for the ex-ante mitigation of liquidity mismatch risk in open-ended funds. To enhance supervision, the Eurosystem recommends introducing system-wide stress testing in Europe, and improving data access and sharing across the region while also maintaining national data collection. Lastly, it proposes strengthening the macroprudential governance framework by introducing a reciprocation mechanism, and giving the European Securities and Markets Authority (ESMA) “top-up” powers, in close collaboration with the ESRB. The Banque de France, the ACPR and the *Autorité des marchés financiers* (AMF – Financial Markets Authority) are continuing to conduct the first French system-wide stress test.<sup>11</sup> An interim report on the exercise has been published.<sup>12</sup> Moreover, the objectives for the NBFI sector are being addressed by the French Presidency of the G7.<sup>13</sup> A report prepared by the Banque de France and the Bank of England on good practices in system-wide stress testing has been submitted to the G7.<sup>14</sup>

**At the international level, the 2026 work programme of the Financial Stability Board (FSB)<sup>15</sup> focuses on identifying systemic vulnerabilities and enhancing the financial system’s resilience.** Since the start of the year,<sup>16</sup> it has highlighted several vulnerabilities, including in short-term and repo financing, and in the expansion of private credit. In a letter to G20 finance ministers and central bank governors, published in April 2026, the FSB Chair stressed that the global financial environment was “uncertain and unpredictable”, notably as a result of geopolitical tensions. He also said that the rapid expansion of AI could pose new risks to financial stability and that the FSB intended to conduct work on this issue.

**The overall banking sector remains resilient, supported by the prudential reforms introduced during the finalisation of the implementation of Basel III.** At the end of September 2025, the vast majority of Basel Committee members published or enacted the final Basel III rules.<sup>17</sup> The EU and other jurisdictions are committed to implementing Basel III, which remains the common standard. In the United States, the recent proposal, reissued on 19 March 2026, for the implementation of Basel III (see Box 1) aims to align more restrictive US requirements with international standards, and includes options for significant deviations to take account of the specificities of the US financial system and the way its economy is financed. These differences in approach mean close attention must be paid to the comparability of the prudential frameworks and the overall consistency of the system. In an environment fraught with risks, particularly geopolitical threats, the solidity of the banking sector is crucial to financial stability.

---

<sup>10</sup> [Order No. 2026-31 of 28 January 2026 on the European single access point providing centralised access to public information that is useful for financial services, capital markets and sustainability - Légifrance.](#)

<sup>11</sup> Banque de France (2025), [The Banque de France, the ACPR and the AMF launch a first system-wide stress test on interconnections within the financial system](#), 2 October.

<sup>12</sup> Banque de France and ACPR (2026) – [press release on the publication of a methodological report on the first system-wide stress test](#), 17 June.

<sup>13</sup> [G7 Finance Ministers' and Central Bank Governors' communiqué, 16 May 2026.](#)

<sup>14</sup> [Report to the G7 prepared by staff from Banque de France and the Bank of England, “System-wide stress testing: takeaways and good practices to date”](#), May 2026.

<sup>15</sup> FSB (2026), [FSB Work Programme for 2026](#), 3 February.

<sup>16</sup> [FSB publications.](#)

<sup>17</sup> Bank for International Settlements (2025), [“RCAP on timeliness: Basel III implementation dashboard”](#), 3 October.

**Regarding climate-related risks, the French G7 Presidency has launched work on the economic impact of extreme climate events and insurability against natural disasters.**<sup>18</sup> Building on the work of previous G7 and G20 presidencies, it will seek to (i) improve understanding of the economic and financial importance of risks linked to extreme weather phenomena and their channels of transmission;<sup>19</sup> and (ii) find courses of action to level up insurability against natural disasters throughout the world, by pooling risks and developing private sector capabilities.

**The Central Banks and Supervisors Network for Greening the Financial System (NGFS) provided significant input for these discussions,** with the publication in May 2026 of a technical note on the impact of extreme weather events. This is based on 31 case studies of recent natural disasters, covering all continents and a wide range of climate events, including flooding, forest fires and heatwaves. In parallel, the NGFS continued to expand its work on monetary policy<sup>20</sup> and nature-related risks.<sup>21</sup> Supervisors' requirements under the European prudential framework have become much stricter since January 2026, with the implementation of new operational rules for climate risk (publication of robust transition plans, need for financial institutions to incorporate climate change into their and governance).

**Box 1 : The Basel III “endgame” in the United States**

On 19 March 2026, US federal agencies issued a request for comments on a new proposal for implementing the final Basel III agreement (“Endgame”), which is due to come into force in 2028. The text, which replaces the draft presented in July 2023, marks a clear shift in approach and reflects the lessons learnt from the 2023 banking turmoil as well as a desire to preserve the US banking sector’s competitiveness.

The proposal includes a review of US rules that are more stringent than international standards, notably those relating to leverage ratios and the calculation of capital buffers for globally systemically important banks. It also introduces a set of national options that depart significantly from Basel standards. If adopted, these adjustments would significantly lower capital requirements for certain activities, particularly those generating non-interest income, such as trading. In addition, the proposed prudential treatment of certain asset classes – including equity financing, derivatives transactions with commercial companies, and certain securitisations, including intermediate tranches – could facilitate the expansion of these activities by US banks. The changes are intended to support corporate financing and the recovery in the US real estate market.

If adopted, the overall impact of the final Basel III reforms on US banks’ capital requirements would be limited to an average increase of just 1.4%. beyond the adjustments to Basel III itself, the proposal also contains significant adjustments to the national prudential framework, including a reduction in supervisors’ discretionary requirements through a lowering of the stress capital buffer. Taken together, these measures would reduce large US banks’ capital requirements by an estimated 6%.

The proposal also provides for additional reductions for medium-sized banks. The main more restrictive change concerns the recognition of unrealised capital losses. The proposed measure reflects the lessons of the collapse of Silicon Valley Bank (SVB) in 2023 and is intended to take better account of the effects of interest rate shocks on this segment of the banking sector.

<sup>18</sup> [Summary of the G7 workshop on the economic impacts of extreme weather events and natural hazards.](#)

<sup>19</sup> The Basel Committee is preparing to launch similar work.

<sup>20</sup> NGFS (2026), [Greening Monetary Policy Operations: Exploring Additional Options](#), January.

<sup>21</sup> NGFS (2026), [NGFS 2026 Nature Package](#), April.

