

19th October 2026

The European Union itself, using the European Financial Stabilisation Mechanism, would be the source of a bailout of France

Introduction

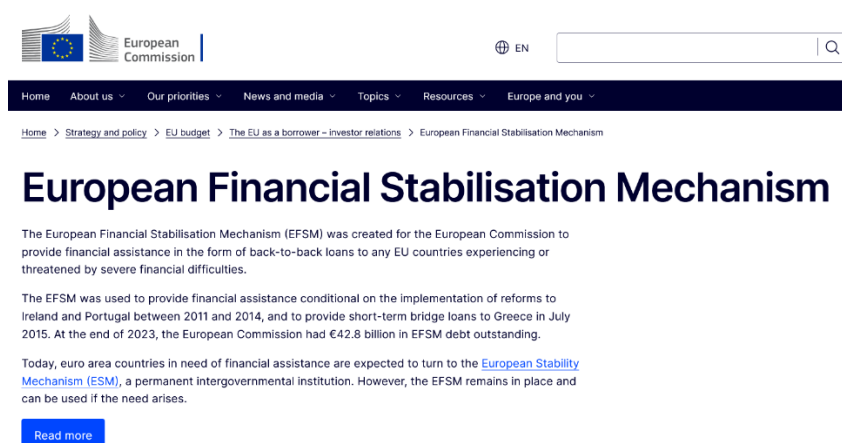
This paper puts the case that it will be the European Financial Stabilisation Mechanism (the EFSM) that will be the platform for mounting a bailout of France, if one is needed.¹

The EFSM is an existing bailout scheme that runs through the European Union (the EU), just like the Coronavirus Recovery Fund (now re-named as Next Generation EU).

Because it runs through the EU and its budget, all EU member states automatically stand behind it, which gives it major debt-raising capacity: €485 billion had been raised via Next Generation EU by mid-2026 out of the EU's total bonds in issue of €793 billion, with plans in place for the EU's borrowings to have risen nearer to €1 trillion by the end of 2026 when Next Generation EU closes.²

Despite not being used for the bailouts of Greece and Cyprus, the EFSM 'remains in place and can be used if the need arises'.

The other options - the European Financial Stability Facility, the European Stability Mechanism, and the European Central Bank's Transmission Protection Mechanism - are either closed, or lack the necessary firepower, or do not qualify for usage as a bailout mechanism.



¹ https://commission.europa.eu/strategy-and-policy/eu-budget/eu-borrower-investor-relations/european-financial-stabilisation-mechanism_en accessed on 10 October 2026

² EU Investor Presentation dated 23 June 2026 slide 26

Size of a bailout of France

The bailout package – if one is required - needs to be at least €2 trillion, given the size of France's public sector debt (17% higher than its General Government Gross Debt as a percentage of GDP) and its annual need for funding (5% of GDP).

We recently made this estimate of the total financial liabilities of the French public sector:

Description of liability	€ billions
General Government Gross Debt	4,100
Net debt position of the Banque de France in TARGET2 payment system ³	181
European Investment Bank loans to French borrowers in the public sector ⁴	63
InvestEU loans to French borrowers in the state-directed sector ⁵	248
Other debts of French public sector borrowers ⁶	325
Sub-total of debts	4,917
Responsibility for the EU's debts and guarantees ⁷	880
Responsibility for subscribed-but-not-called capital of the European Investment Bank ⁸	43
Responsibility for subscribed-but-not-called capital of the European Stability Mechanism ⁹	42
Guarantee of the liabilities of the European Financial Stability Facility ¹⁰	83
Market risk on the Eurosystem's portfolio of bonds ¹¹	150
Credit risk on the Eurosystem's portfolio of bonds ¹²	150
Sub-total of contingent liabilities	1,348
Total of debts and contingent liabilities	6,265

Not all of these liabilities are debts, but even taking the sub-total of debts of €4.9 trillion, and assuming that these debts have an average life of 7 years, there is annual need to refinance existing debt of €702 billion, it being assumed that France will not be in a position to reduce debt during the bailout period.

During the same bailout period, France would need to finance its annual fiscal deficit of 5% of its GDP: 5% of €3.7 trillion adds another €185 billion per annum to the requirement.

France thus needs a facility of €887 billion for every year of the duration of the bailout period. The bailout period is until it can access global capital markets itself on acceptable terms.

A €2 trillion facility would cover France for 27 months.

'Safe assets' and the operation of the EU financial system

The EU financial system has the euro and the Eurozone at its centre. However, two different types of member state coalesce within it.

One is members who have their own currency, of which they are the sole user, and over which they control the levers of monetary policy: money supply, interest rates, and exchange rate. These member states are 'sovereign', and the bonds issued by their governments count as 'sovereign risk', or 'risk-free'.

By contrast the members of the Eurozone share usage of the currency, and have surrendered control over the levers of monetary policy to the European Central Bank (the ECB). They have become 'sub-sovereigns', as was explained in the book we co-authored with Barnabas Reynolds and Professor David Blake entitled 'Managing Euro Risk', and published by Politeia in 2020.

The Eurozone contains no sovereign borrower: neither any of the member states nor any of the EU-level institutions are sovereigns towards the euro. This is unlike the government of the UK towards the pound, and the government of the USA towards the dollar.

In place of 'sovereign assets' or 'risk-free assets', the EU has pioneered the term 'safe assets'. This is what its financial system runs on, like a fuel, when the US and UK financial systems run on risk-free US and UK government bonds respectively: US Treasuries and UK gilt-edged securities.

Because the EU cannot use basic principles to drive the definition of 'safe assets', it uses public credit ratings instead. The applicable ones are issued from the five EU-approved credit rating agencies: S&P Global, Moody's, Fitch, DBRS Morningstar, and Scope. Each has its own rating system, with the one of S&P Global being the most familiar.

A 'safe asset' is one that ranks within 'Credit quality step 1' of the Eurosystem Credit Assessment Framework (ECAF).³ For that, a bond must enjoy a long-term credit rating of AA- or better from S&P Global, or the equivalent rating from Moody's, Fitch, DBRS Morningstar, or Scope.

One such rating is enough, even if the bond is rated by other agencies at a level outside 'Credit quality step 1', or is only rated by one agency. Asset-backed bonds need to have qualifying ratings from two agencies to determine their 'Credit quality step'.

EU member states have public credit ratings ranging from AAA to BBB-.

EU-level institutions enjoy different configurations of backing from the member states. The nature of the configuration drives the institution's credit rating.

The bonds of EU-level institutions are, at present, all rated as 'safe assets', because the amount of their bonds in issue, the nature of their backing from member states, and the credit ratings of enough of these backing member states, ensure at least one AA- rating from one agency.

EU-level institutions are in a position to bail out an individual member state - if there are sufficient member states whose bonds rank as 'safe assets' themselves to back a bailout mechanism of sufficient size, to borrow the necessary money for the bailout, and if those borrowings are made via bonds that themselves rank as 'safe assets'.

These conditions could be fulfilled up until now, for bailing out Ireland, Portugal, Greece, and Cyprus. France, though, poses two challenges: its size, and the fact that in the past this system of EU-level institutions backed by member states required France to act as one of the creditworthy backers of the bailout mechanisms and not as the member state requiring the bailout.

Against that background we can now look at the options for where the money for bailing France out could come from.

The European Financial Stability Facility (EFSF)⁴

The EFSF was the second bailout mechanism and the first one that had its own legal personality. Unlike the EFSM, its backing comes only from the Eurozone member states at the time, not from all of the EU member states. It funded itself by issuing bonds to international investors. It on-lent the proceeds to the Eurozone member states in bailout.

The bonds are guaranteed by the Eurozone member states up to fixed amounts each. The aggregate amount of the guarantees is the theoretical ceiling, or firepower, of the EFSF.

³ <https://www.ecb.europa.eu/mopo/coll/risk/ecaf/html/index.en.html> accessed on 13 October 2026

⁴ <https://www.esm.europa.eu/about-us/governance/efsf> accessed on 12 October 2026

However, the guarantees of the member states in bailout have to be deducted from the theoretical ceiling, because only qualifying guarantees can be counted on. The aggregate amount of qualifying guarantees determines the EFSF's actual lending capacity, or firepower.

'Qualifying' means that the bonds of the member state issuing the guarantee rank as 'safe assets' themselves. As long as the bonds issued by the EFSF are backed by guarantees from member states whose own bonds are 'safe assets', the EFSF's bonds will be rated as 'safe assets'.

The EFSF contains an 'over-guarantee', whereby the actual borrowing-and-lending capacity of the EFSF is some way below its theoretical ceiling. The difference between the two allows the deduction back of any ineligible guarantees: the guarantees from member states who borrow from the EFSF, and the guarantees from member states whose own bonds are not 'safe assets'.

This is explained on pp. 41-43 of our book 'The shadow liabilities of EU Member States, and the threat they pose to global financial stability', published by The Bruges Group in 2023.⁵

The structure is entirely circular: a virtuous circle where an EU institution can raise money on the strength of member state backing, and member states' credit ratings are improved by the existence of an EU institution that can back the member states' debts should the need arise.

For the EFSF, the circle began to rotate in the opposite direction, and became a vicious one. The EFSF found itself in the position of having made loans approaching the aggregate amount of guarantees from member states whose own bonds ranked as 'safe assets'. It could not borrow-and-lend more itself without placing reliance on the guarantees of lower-rated member states, in which case all of the EFSF's own bonds would cease to be 'safe assets'. It therefore closed itself to new business. This was at a time when France was rated AA.

The issue is that there are currently only six Eurozone member states in addition to Germany and France whose own bonds rank as 'safe assets'. These six are all of small or medium size: Netherlands, Luxembourg, Austria, Finland, Belgium, Ireland, and Slovenia.

The EFSF template works if there are several large member states whose own bonds both rank as 'safe assets', and who are not in danger of losing that status i.e. they are rated AAA, AA+, or AA, or, at worst, AA- with Positive or Stable Outlook.

The template has gone into reverse. France has two 'safe asset' ratings but its AA from DBRS carries 'Negative Outlook', as does its Aa3 from Moody's. Fitch, Scope and S&P Global rate France at A+ with Stable Outlook, outside the perimeter of 'safe assets'.⁶

In consequence the EFSF has had its ratings cut to the same level as France, because it is reliant on France's guarantee of its bonds.

The risk is now that Moody's converts its rating of Aa3 with Negative Outlook to A1, which is the highest Moody's rating level within 'Credit quality step 2'. That would leave only one agency – DBRS – rating France as a 'safe asset'.

⁵ ISBN 978-1-8380658-9-8

⁶ <https://www.aft.gouv.fr/en/frances-credit-ratings> accessed on 17 October 2026

DBRS rates France as AA with Negative Outlook.⁷ This rating was made as recently as 16th September 2026. A conversion of the Negative Outlook into a downgrade would take France down to AAL (meaning AA Low) in the DBRS system, which is still within 'Credit quality step 1'. The next step down from there is AH (meaning A High). If Moody's had taken France down to A1, and DBRS to AH, then France's bonds are no longer a 'safe asset', and nor, in consequence, would the EFSF's bonds.

That would be a profoundly serious occurrence, for an EU-level institution's bonds no longer to rank as a 'safe asset' within its own monetary system. The bonds of EU institutions – the EU itself, the EFSF, the ESM, and the European Investment Bank – must remain as 'safe assets'. It is a systemic risk for the EU financial system that they might cease to be. It is also a systemic risk for global financial system. That is the essence of my book, that the total debts that EU member states must answer to are already far higher than the figures for General Government Gross Debt which Eurostat issues.

These EU-level institutions are creatures of the member states for creating borrowings under their responsibility without the borrowings impacting their own General Government Gross Debt or debt-to-GDP ratios.

That has worked well up to now, but will come out into the open with unforeseeable consequences if France's bonds cease to rank as 'safe assets', and cause the bonds of EU-level institutions to cease to rank as 'safe assets' as well.

Quite a lot hangs on the opinion of Moody's, but an awful lot now hangs on the opinion of DBRS. If they downgrade France to outside 'Credit quality step 1', the ratings of all the EU-level institutions could follow.

At any rate, these restrictions mean that the EFSF could not be reopened to help bail out France.

The European Stability Mechanism (ESM)⁸

The ESM was the third Eurozone bailout mechanism, and again one with its own legal personality and backing only from Eurozone member states. It also borrows from international investors and under the same template as the EFSF.

However, instead of having member state guarantees, the mechanism of obtaining backing from member states is that the member states have subscribed to shares in an extremely high amount, of which only 10% is paid in.

The difference between the subscribed amount and the paid-in amount is the subscribed-but-not-called capital: an irrevocable and unconditional undertaking from each member state to pay in at the behest of the ESM, in whole or in part, up to their individual ceiling.

That amounts to a guarantee fund.

We can safely term the subscribers of this uncalled capital as guarantors.

⁷ <https://dbrs.morningstar.com/research/489364/morningstar-dbrs-changes-trends-on-the-republic-of-france-to-negative-confirms-credit-ratings-at-aa> accessed on 18 October 2026

⁸ <https://www.lyddonconsulting.com/full-callable-capital-of-the-european-stability-mechanism-by-credit-rating-level/> accessed on 13 October 2026

The credit ratings of the guarantors, as with the EFSF, define how much of the ESM's theoretical maximum lending capacity could be borrowed and used for a bailout, before the ESM's own credit rating is impacted.

Once again, the bonds of the ESM must rank as 'safe assets', and this is achieved by the ESM being able to call upon new capital of a larger amount than the bonds they have issued, and from member states whose own bonds rank as 'safe assets'.

Currently the bonds the ESM has issued are fully covered by its ability to call in the subscribed-but-not-called capital from member states whose ratings are AAA. The ESM's bonds are thus rated AAA.

Germany's subscribed-but-not-called capital is sufficient to cover all of the bonds that the ESM currently has in issue.

However, and as our blog from 2024 demonstrates, there is only a small capacity for new borrowing and lending before it is France's subscribed-but-not-called capital that is being relied upon.

This is because the amounts that can be called in from Netherlands, Luxembourg, Austria, Finland, Belgium, Ireland, and Slovenia are modest:

ESM callable capital by member state and credit rating level

Member state	S&P rating	Subscribed	Called	Callable	Callable AAA	Callable AA+	Callable AA	Callable AA-	Callable A+	Callable A	Callable A-	Callable BBB+	Callable BBB	Callable BBB-
Germany	AAA	€189.5 bn	€21.6 bn	€167.9 bn	€167.9 bn	€167.9 bn	€167.9 bn	€167.9 bn	€167.9 bn	€167.9 bn	€167.9 bn	€167.9 bn	€167.9 bn	€167.9 bn
Luxembourg	AAA	€1.7 bn	€0.2 bn	€1.5 bn	€1.5 bn	€1.5 bn	€1.5 bn	€1.5 bn	€1.5 bn	€1.5 bn	€1.5 bn	€1.5 bn	€1.5 bn	€1.5 bn
Netherlands	AAA	€39.9 bn	€4.6 bn	€35.3 bn	€35.3 bn	€35.3 bn	€35.3 bn	€35.3 bn	€35.3 bn	€35.3 bn	€35.3 bn	€35.3 bn	€35.3 bn	€35.3 bn
Austria	AA+	€19.4 bn	€2.2 bn	€17.2 bn		€17.2 bn	€17.2 bn	€17.2 bn	€17.2 bn	€17.2 bn	€17.2 bn	€17.2 bn	€17.2 bn	€17.2 bn
Finland	AA+	€12.5 bn	€1.4 bn	€11.1 bn		€11.1 bn	€11.1 bn	€11.1 bn	€11.1 bn	€11.1 bn	€11.1 bn	€11.1 bn	€11.1 bn	€11.1 bn
Belgium	AA	€24.3 bn	€2.8 bn	€21.5 bn		€21.5 bn	€21.5 bn	€21.5 bn	€21.5 bn	€21.5 bn	€21.5 bn	€21.5 bn	€21.5 bn	€21.5 bn
Ireland	AA	€11.1 bn	€1.3 bn	€9.8 bn		€9.8 bn	€9.8 bn	€9.8 bn	€9.8 bn	€9.8 bn	€9.8 bn	€9.8 bn	€9.8 bn	€9.8 bn
France	AA-	€142.3 bn	€16.2 bn	€126.1 bn			€126.1 bn	€126.1 bn	€126.1 bn	€126.1 bn	€126.1 bn	€126.1 bn	€126.1 bn	€126.1 bn
Slovenia	AA-	€3.3 bn	€0.4 bn	€2.9 bn			€2.9 bn	€2.9 bn	€2.9 bn	€2.9 bn	€2.9 bn	€2.9 bn	€2.9 bn	€2.9 bn
Slovakia	A+	€6.9 bn	€0.8 bn	€6.1 bn				€6.1 bn	€6.1 bn	€6.1 bn	€6.1 bn	€6.1 bn	€6.1 bn	€6.1 bn
Estonia	A+	€1.8 bn	€0.2 bn	€1.6 bn				€1.6 bn	€1.6 bn	€1.6 bn	€1.6 bn	€1.6 bn	€1.6 bn	€1.6 bn
Lithuania	A	€2.9 bn	€0.3 bn	€2.6 bn					€2.6 bn	€2.6 bn	€2.6 bn	€2.6 bn	€2.6 bn	€2.6 bn
Latvia	A	€1.9 bn	€0.2 bn	€1.7 bn					€1.7 bn	€1.7 bn	€1.7 bn	€1.7 bn	€1.7 bn	€1.7 bn
Spain	A	€83.1 bn	€9.5 bn	€73.6 bn					€73.6 bn	€73.6 bn	€73.6 bn	€73.6 bn	€73.6 bn	€73.6 bn
Malta	A-	€0.6 bn	€0.1 bn	€0.5 bn						€0.5 bn	€0.5 bn	€0.5 bn	€0.5 bn	€0.5 bn
Portugal	A-	€17.5 bn	€2.0 bn	€15.5 bn						€15.5 bn	€15.5 bn	€15.5 bn	€15.5 bn	€15.5 bn
Croatia	BBB+	€3.7 bn	€0.1 bn	€3.6 bn							€3.6 bn	€3.6 bn	€3.6 bn	€3.6 bn
Cyprus	BBB+	€1.4 bn	€0.2 bn	€1.2 bn							€1.2 bn	€1.2 bn	€1.2 bn	€1.2 bn
Italy	BBB	€125.0 bn	€14.3 bn	€110.7 bn								€110.7 bn	€110.7 bn	€110.7 bn
Greece	BBB-	€19.7 bn	€2.2 bn	€17.5 bn									€17.5 bn	€17.5 bn
Totals	--	€708.5 bn	€80.6 bn	€627.9 bn	€204.7 bn	€233.0 bn	€264.3 bn	€393.3 bn	€401.0 bn	€478.9 bn	€494.9 bn	€499.7 bn	€610.4 bn	€627.9 bn
ESM loan book now					€82.6 bn	€82.6 bn	€82.6 bn	€82.6 bn	€82.6 bn	€82.6 bn	€82.6 bn	€82.6 bn	€82.6 bn	€82.6 bn
Callable capital at this rating level less loan book					€122.1 bn	€150.4 bn	€181.7 bn	€310.7 bn	€318.4 bn	€396.3 bn	€412.3 bn	€417.1 bn	€527.8 bn	€545.3 bn
ESM 'firepower' if it wishes to retain the respective rating					€122.1 bn	€150.4 bn	€181.7 bn	€310.7 bn	€318.4 bn	€396.3 bn	€412.3 bn	€417.1 bn	€417.4 bn	€417.4 bn

'Firepower' means the ESM's capacity to make new loans if the loans are in the exact amount of new bonds issued. The ESM's maximum firepower of €417 billion is only available if the ESM's rating is allowed to fall to BBB+, which permits the callable capital of Spain to be taken into account. There is minimal incremental benefit in allowing the rating to go to BBB.

There are options for increasing the lending without issuing new bonds:

1. divert the €9.2 billion of the €91.8 billion of bonds-in-issue which is currently held in cash and securities: no obligation is broken by doing this;
2. reduce the amount of the paid-in capital of €80.6 billion which is held as cash and securities: the ESM could negotiate a reduction with rating agencies that would not damage its credit rating. As a strawman one could imagine €40.8 billion being released under this heading, and cash and securities of €38.8 billion remaining.

It is conceivable that a global amount of €50.0 billion could be diverted from cash and securities into new lending from these two sources.

If a bailout operation were to be mounted by the ESM and for a different member state than France, reliance would come to be placed on France's subscribed-but-not-called capital. The ESM's credit rating would fall to AA with negative Outlook (the DBRS rating of France currently and the best of France's ratings), which is also AA in the S&P Global system. If France had been downgraded to AH and its equivalents from the other agencies, the rating of the ESM's bonds would fall to AH (or A+ from S&P Global) and they would no longer rate as 'safe assets'.

If France itself was the borrower from the ESM, its subscribed-but-not-called capital would have to be discounted from the calculation. One is then immediately relying on member states with credit ratings of A+ or below, given the size of borrowing that France would need. The ESM's rating would be reduced to that of the lowest-rated member state being relied upon.

According to our 2024 calculation, the ESM had €417 billion of firepower, but only if it allowed its own rating to fall to BBB+. However, with France in bailout and the amount of qualifying backing diminished by €126 billion, there might be as little as €290 billion available and then only if the ESM allowed its rating to fall to well outside the bounds of its bonds ranking as 'safe assets'.

France itself would probably have been downgraded to BBB- (the lowest rung of 'investment grade') if it had gone into bailout, or possibly even worse.

The ESM lacks the firepower to mount a new bailout other than one of a small Eurozone member state. This discounts the ESM as a platform for a bailout of France.

The Transmission Protection Instrument (TPI) of the European Central Bank (ECB)

Ambrose Evans-Pritchard analysed the TPI in an article in the Daily Telegraph published on 6th October 2026 entitled 'The ECB cannot rescue France until its debt crisis is absolutely dire'.⁹

He correctly characterises the TPI as an 'anti-spread shield'. This means that its aim is to control the divergence between the yields on bonds in euro issued by different Eurozone member states.

It has become an article of faith that the yields on German bonds (called Bundesanleihe or Bunds for short) should be the lowest of any Eurozone member state, because Germany has a AAA credit rating, it is large, its debt-to-GDP ratio is below 60% (or was until Friedrich Merz loosened the debt brake and allowed extra borrowings), and it is considered to be the anchor and backstop for the entire Eurozone.

Thus the phrase 'Bund spread' emerged: this is the number of basis points by which the yields on bonds in euro of other Eurozone member states exceed the yield on Bunds.¹⁰

It is the monetary policy of the ECB that the Bund spread should remain within a range. If it verges towards the edge of that range, the TPI can be used to buy up bonds of a particular Eurozone member state, thereby bringing their yields down to within the ECB's acceptable range (which is unstated).

It does not seem to be a possibility that the TPI could be used to push the yields on Bunds up, by short-selling them, thereby narrowing the Bund spread by increasing Bund yields until they come within the accepted range of the bonds of the other Eurozone member states.

The accepted wisdom is that the ECB should mobilise the TPI if the yield on a given Eurozone member state's bonds increased to the perimeter of the acceptable range, a parallel to the Exchange Rate Mechanism (ERM) whereby an EU member state whose currency is a member of the ERM must take certain actions if the exchange rate of its currency against the euro nears the perimeter of its acceptable range, on either the high or the low side.

In the case of the TPI it is the Eurosystem, not the member state itself, that arranges the support.¹¹

⁹ <https://www.telegraph.co.uk/business/2026/10/06/ecb-cannot-rescue-france-until-debt-crisis-absolutely-dire/> accessed on 14 October 2026

¹⁰ A basis point is one hundredth of one percent, written as 0.01%. 253 basis points is 2.53%

¹¹ Eurosystem means the ECB and all the national central banks of Eurozone member states

To be eligible for support under the TPI a member state must fulfil several criteria, and France, as Ambrose points out, fails all of them:

- The member state must pursue ‘sound fiscal and macroeconomic policies’;
- The member state is not ‘subject to an excessive debt procedure’ - France is;
- The member state’s ‘trajectory of public debt is sustainable’; and
- The stress currently applying to the member state’s bonds is ‘not warranted by country-specific fundamentals’.

Taken to a higher level, a bailout of France can scarcely be termed as a ‘monetary policy operation’ at all, meaning a technocratic intervention to iron out anomalous behaviours in the bond market. An intervention by the ECB to buy two or three years’ worth of newly-issued bonds of French public entities, because the market will not buy them at all, does not fall within its mandate and legal powers.

The trigger for a bailout is when the market will not buy the bonds of the issuer in the quantity of money that the issuer needs to be borrow either at all or only at a penal rate of interest. It is not a trigger for a bailout that the market will take up the bonds at an arbitrary yield premium to what it requires to buy German bonds.

The second case is what the TPI is designed to address; the first case is not. The TPI, like the EFSF and the ESM, falls away as a platform for a bailout of France.

Interim summary

None of the EFSF, ESM or TPI is fitted to the task in hand: to raise €2 trillion to on-lend to France.

Given that France is one of the bulwarks of the EU and that its collapse would be a life-threatening event for both the EU and the euro (and therefore for the EU’s main purpose of Economic and Monetary Union), the focus must fall onto the European Union itself as the platform for the bailout.

There is precedent for this: Covid-19 was deemed to be a life-threatening event for the EU, and the EU responded with the Coronavirus Recovery Fund, now re-named NextGeneration EU. As stated above, the EU had borrowed €485 billion by mid-2026 under this programme.

The debts of the EU are a joint-and-several liability of the all EU member states – Eurozone and non-Eurozone - through the mechanism of the EU budget, or Multiannual Financial Framework.

The workings of the joint-and-several liability are explained on pp. 7-8 of our recent paper ‘The UK’s Shadow Liabilities from EU membership, were the UK to rejoin for the start of the 2028-34 Multiannual Financial Framework’.¹²

There is both a legal and mechanical precedent for mobilising an EU fund, and there is a pre-existing platform – the European Financial Stabilisation Mechanism – albeit that its current ceiling is too low.

We now focus on that platform and how it could be mobilised for the task-in-hand.

¹² <http://www.lyddonconsulting.com/wp-content/uploads/2026/09/UK-Shadow-Liabilities-on-Rejoining-EU-for-2028-34-MFF-19sep26.pdf> accessed on 14 October 2026

The European Financial Stabilisation Mechanism (EFSM)¹³

The EFSM was the first euro bailout mechanism, and it is a fund of the European Union. It has been used for only two bailout programmes – for Ireland¹⁴ and for Portugal¹⁵.

€22.5 billion was lent to Ireland. Its bailout programme lasted from 2011 to 2013. €10.8 billion remains to be repaid as of September 2026, according to the maturity dates stated on the referenced webpage.

€24.3 billion was lent to Portugal. Its bailout programme lasted from 2011 to mid-2014. €8.9 billion remains to be repaid as of September 2026, according to the maturity dates stated on the referenced webpage.

The durations of the bailouts of Ireland and Portugal bear out our contention that a package for France would have to meet its needs for at least two years.

As outstandings under the EFSM total €19.7 billion, there is €40.3 billion of headroom available against the current ceiling of €60 billion.

That €40.3 billion remains available, as the European Commission's webpage makes clear: 'the EFSM remains in place and can be used if the need arises'.

While the European Commission states that 'euro area countries in need of financial assistance are expected to turn to the European Stability Mechanism', the EFSM avenue remains open.

Mobilising a bailout for France through an expanded EFSM is the 'path of least resistance', given that the EFSF and ESM are closed or lack the necessary firepower, and the legal obstacles standing in the way of using the TPI as a platform are greater than those standing in the way of using the EFSM.

The expansion of the ESM requires only that the European Commission make a proposal to the European Council of Ministers, and that 15 of the member state ministers sitting in a valid meeting of the Council of Ministers approve it.

These ministers must be ones speaking for member states containing over 65% of the EU's population. The first test – assembling the 15 approving ministers – is far more onerous than the one related to population.

The European Parliament has no role to play.

¹³ https://economy-finance.ec.europa.eu/eu-financial-assistance/euro-area-countries/european-financial-stabilisation-mechanism-efsm_en accessed on 15 October 2026

¹⁴ https://economy-finance.ec.europa.eu/eu-financial-assistance/euro-area-countries/financial-assistance-ireland_en accessed on 15 October 2026

¹⁵ https://economy-finance.ec.europa.eu/eu-financial-assistance/euro-area-countries/financial-assistance-portugal_en accessed on 16 October 2026

Legal coverage for the bailout of France under the EFSM

The legal coverage would be the 'Emergency powers' Article 122.2 in the Treaty on the Functioning of the European Union of 2016:

'Where a Member State is in difficulties or is seriously threatened with severe difficulties caused by natural disasters or exceptional occurrences beyond its control, the Council, on a proposal from the Commission, may grant, under certain conditions, Union financial assistance to the Member State concerned. The President of the Council shall inform the European Parliament of the decision taken'.

Financial markets failing to buy French government bonds on acceptable terms would, within the framework of the EU and Eurozone, be construable as 'exceptional occurrences' and ones beyond France's control. The workings of financial markets are no longer under French control: they are controlled by the ECB, and the European Securities and Markets Association, as well as by a network of financial market infrastructures.

It is not a given that France's own fiscal policies should be construed as the direct cause of the 'exceptional circumstances'. The European Commission can argue that they may have been a contributory factor, but that they have now combined, unexpectedly, with other 'exceptional circumstances' beyond France's control to now constitute an existential threat to the EU and the euro deriving from a French financial collapse.

It seems to us unarguable that such a collapse would be attributable in large part to the architecture of the euro, and to the surrender by France of its monetary policy levers to the ECB.

France is not in sole control of these matters, although it has participated in the surrender of control which has precipitated these 'exceptional circumstances', as it did for Ireland, Portugal, Greece, and Cyprus before.

At any rate it is our view that the European Commission will be able to put together a proposal on terms that attribute France's problems to causes far wider than its own fiscal policies. The European Commission will be able to make this proposal stand up legally against the TFEU and any number of supporting documents about Economic and Monetary Union.

Such a proposal containing its opinion that the issue affects the survival of the EU and the euro will have the support of the European Court of Justice, should any party bring a case to challenge the support package, because the European Court of Justice regards the European Commission as the valid arbiter of what is in the interests of the European Union.

That is the built-in advantage for the authorities in European law.

Process of approval

The approval needed is to raise the ceiling of the EFSM by €2 trillion.

The proposal for this to happen would come from the European Commission. It has to be discounted as a possibility that the proposal could arise in any other way.

The proposal is presented to the Council of Ministers.

This invokes the 'standard' Qualified Majority Voting (QMV) system set out in Art 238.3.a of the Treaty on the Functioning of the European Union (TFEU). The measure must be supported by 'at least 55 % of the members of the Council representing the participating Member States, comprising at least 65 % of the population of these States.' That is 15 out of 25 member states, but still containing 65% of the EU's population.

It does not call for the 'reinforced' QMV system, set out in TFEU Art 238.2, where a measure needs to be supported by 'at least 72 % of the members of the Council, representing Member States comprising at least 65 % of the population of the Union'. That means at least 20 out of 27 member states, and the 20 must contain 65% of the EU's population.

TFEU 238.a also lays down a condition on a blocking minority: it 'must include at least the minimum number of Council members representing more than 35 % of the population of the participating Member States, plus one member'. This gives the larger member states a better chance of blocking a measure, but it is not a veto.

There is no requirement for France's representative in the Council of Ministers to recuse themselves from the voting. The size of France's population gets thrown into the scales towards reaching the 65% threshold, as well as the vote of its minister.

This analysis by Lyddon Consulting shows (i) the smallest number of member states that could speak for 65% of the EU's population; (ii) a possible group of 15 members states speaking for 65% of the EU population; (iii) a possible group of 20 members states speaking for 65% of the EU population:

EU – 27 countries	Population	% of EU	Smallest number to reach 65%	15 to support France	20 to support France
Belgium	11,955.3	2.65%		2.65%	2.65%
Bulgaria	6,423.2	1.42%			1.42%
Czech Rep	10,915.8	2.42%			
Denmark	6,025.6	1.33%			
Germany	83,467.1	18.47%	18.47%	18.47%	18.47%
Estonia	1,360.7	0.30%		0.30%	0.30%
Ireland	5,510.6	1.22%		1.22%	1.22%
Greece	10,366.6	2.29%		2.29%	2.29%
Spain	49,590.1	10.97%	10.97%	10.97%	10.97%
France	69,112.3	15.29%	15.29%	15.29%	15.29%
Croatia	3,876.0	0.86%		0.86%	0.86%
Italy	58,942.8	13.04%	13.04%	13.04%	13.04%
Cyprus	996.6	0.22%		0.22%	0.22%
Latvia	1,845.1	0.41%		0.41%	0.41%
Lithuania	2,887.6	0.64%		0.64%	0.64%
Luxembourg	691.0	0.15%		0.15%	0.15%
Hungary	9,488.4	2.10%			
Malta	588.3	0.13%		0.13%	0.13%
Netherlands	18,130.2	4.01%			
Austria	9,216.0	2.04%			2.04%
Poland	36,332.8	8.04%	8.04%		
Portugal	11,424.0	2.53%			2.53%
Romania	19,041.3	4.21%			
Slovenia	2,135.1	0.47%		0.47%	0.47%
Slovakia	5,409.4	1.20%			1.20%
Finland	5,652.9	1.25%			1.25%
Sweden	10,605.5	2.35%			
	451,990.3	100.00%	65.81%	67.11%	75.54%

Passing the hurdle of 15 member states is perfectly plausible, given the leverage that can be exercised. In effect it is the four largest member states exercising the leverage, and eleven small member states having leverage exercised upon them.

Medium-sized member states are left out of the picture, and are not capable of forming a blocking minority of member states speaking for 35% of the EU population.

The hurdle of 20 member states is far harder to pass than 15. In our analysis it was possible to get to 19, with all the smaller member states, member states that had themselves received a bailout, and the quadrumvirate of Germany, Spain, Italy, and France itself. Getting the last vote meant recruiting one 'hawkish' member state of medium size, and that is Austria in our illustration.

A route to approval via 'standard' QMV is perfectly plausible: 'reinforced' QMV would be far more difficult.

Role of the International Monetary Fund (IMF)

The IMF can play no role in the package. The conditions they impose would not be acceptable to the French government, because their imposition could precipitate civil unrest. The other EU member states are going to have to accept that the support package does not come with arduous conditions attached requiring France to put its house in order as Greece, Cyprus, Portugal, and Ireland had to.

Involvement of the United Kingdom

An interesting complication is that the United Kingdom is a guarantor of the bonds issued by the EFSM to fund its participation in the bailouts of Ireland and Portugal. This ongoing liability is a feature of the 'bar bill' that Jean-Claude Juncker stated that the UK had to pay before leaving the EU.

Impact on the credit ratings of the EU institutions

Even if this support package could be mobilised through the EFSM, there is a high chance that the credit ratings of the EU institutions will be cut anyway, leaving the bonds of some of them no longer qualifying as 'safe assets'.

If France's ratings were cut to BBB- by S&P Global and to its equivalents by the other agencies, the rating of the EFSF would for sure fall out of 'Credit quality step 1' in the ECAF.

The ESM would have miniscule firepower before its bonds dropped from AAA to right out of 'Credit quality step 1': France is currently the only sizeable member state with a credit rating between AA+ and AA- (thanks to its ratings from DBRS and Moody's). The ESM would have to close to new business, as the EFSF has done.

The EIB has multiple rating strengths: the supposed quality of its loan portfolio being mainly to EU public sector borrowers, its subscribed-but-not-called capital due from the EU member states, and the guarantees it enjoys from the EU for several of its programmes (like InvestEU and its loans to borrowers outside the EU).

The problem with these rating strengths is that they all come back to reliance on member states and borrowers in the public sector of member states. Its business model is circular, as are the business models of both the EFSF and ESM.

The threat or reality of the ratings of the EU-level institutions falling to outside of 'safe asset' status would call for a decisive response. That response should be to collapse the separate legal personalities of the EFSF, ESM, and EIB, and to novate their debts onto the EU. The separate legal personalities of these institutions have fulfilled a purpose up to now, but new circumstances demand new solutions. The virtuous circle that enabled them has now begun to change to a vicious circle.

The EFSF has debts of €187 billion.¹⁶ The ESM has debts of €88 billion.¹⁷ The EIB has debts of €433 billion.¹⁸ The total of debts to be novated onto the EU would be €708 billion.

The major disaster would be if the EU lost its AAA rating, a rating that depends largely on its debts being backed in their entirety by Germany, which has a AAA rating.¹⁹ If the EU's debts rose from €1 trillion to €3 trillion on the back of a bailout of France through the EFSM (or even to €3.7 trillion if the debts of the EFSF, ESM, and EIB were novated onto it as well), and at the same time as Chancellor Merz has released Germany's debt brake to allow its own debt-to-GDP ratio to rise sharply, the rating agencies might start to ask themselves whether Germany is good both for its own increasing debts, and for all the debts in EU institutions that investors believe track back onto it.

Interplay of Germany's credit rating with those of the EU-level institutions

Financial markets and credit rating agencies have comfortably assumed that 'it all tracks back onto Germany', without calculating what aggregate amount tracks back onto Germany, or considering what happens when Germany boosts its own borrowings above 60% of its GDP, this baseline being €2.8 trillion of borrowings on a GDP of €4.7 trillion.²⁰

If Germany has a plan to raise its debts to 85% of its GDP before the next parliamentary elections in 2030, and assuming German GDP rises by 1% per annum compounded to reach €4.9 trillion by the same date, Germany's debt would by then be €4.2 trillion.

If, on top of that, it had at least €3.7 trillion of EU debt to answer to as at the end of 2026, and by 2030 the sharply increasing amount of EU debt described in the EU Investor Presentation of June 2026, it would be harder for financial markets and credit rating agencies to continue to assess Germany's credit risk based only on its own debts, rather than adding in the amount that 'tracked back' onto it. These headings would total €6.5 trillion at the end of 2026 rising beyond €8 trillion by the end of 2030.

Almost all the debts that comprise the €6.5 trillion exist now: the EU's debts, the debts of the EU-level institutions, Germany's own debt, and France's borrowing needs over the next two years.

¹⁶ EFSF 2025 annual report p. 19 accessed on 18 October 2026

¹⁷ ESM 2025 annual report p. 79 accessed on 18 October 2026

¹⁸ EIB 2025 annual financial report p. 49 accessed on 18 October 2026

¹⁹ The EU has AAA ratings from four of the five approved agencies, and a AA+ rating from S&P Global - EU Investor Presentation dated 23 June 2026 slide 9

²⁰ <https://data.worldbank.org/indicator/NY.GDP.MKTP.CD?locations=DE> accessed on 16 October 2026

The escalation to €8 trillion by the end of 2030 would be attributable to increases in borrowing by both Germany itself and the EU.

What appears to be missing from the picture being considered by rating agencies and financial markets is the accumulation of debts onto the accounts of just one or two borrowers, rather than their being distributed across the published accounts of six or seven.

Summary and Conclusions

The EU itself is the only possible platform for a bailout of France. The path of least resistance would be to raise the ceiling of the EFSM.

That could be done using the cover of the 'Emergency powers' clause in the TFEU, a proposal from the European Commission to the Council of Ministers, and an approval in the Council of Ministers using its 'standard' Qualified Majority Voting procedure.

Then all of the debts for France's bailout would be the joint-and-several liability of all the EU member states, Eurozone and non-Eurozone.

It could well prove necessary to collapse the separate legal personalities of the EU institutions – EFSF, ESM, and EIB – and novate all their debts onto the EU. The system of setting up these separate vehicles, each with its own backing mechanism, and each reliant on member states maintaining their own credit ratings, has run out of road.

The bonds issued by these EU institutions would then remain as 'safe assets', as long as all the bonds of the EU itself continued to rank as 'safe assets'.

That is the real question, though: whether the EU's bonds would retain their 'safe asset' status once the full scale of the EU's current debts and debt trajectory had been realised, the bailout of France added in to them, and the debts of the other EU-level institutions novated to that entity as well.

That accumulation the debts of the other EU-level institutions onto the EU seems to us to be an inevitable consequence of any bailout of France, because these institutions will not retain their 'safe asset' status once France disappears from the equation as one of their backers.

The edifice has survived and prospered in part because of all these debt piles being separated onto the books of six or seven entities when their source of credit strength is the backing of the same member states.

The accumulation of debts onto the EU and Germany's own rising debt – rising at a time when the EU is becoming more reliant on Germany's unused debt capacity – will force a realisation upon rating agencies or financial markets that neither Germany nor the EU are good for their AAA ratings.

If that results in all member states losing their 'safe asset' status, it would cost the EU its 'safe asset' status under its own system, and pull the EU financial system into disaster.