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France Takes Market Pulse at Bond Sale as AAA Decision Looms (1)
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(Updates with today's yields in third, sixth paragraphs.
For more on the region's debt crisis EXT4.)

By Mark Deen and Paul Dobson

Jan. 5 (Bloomberg) -- France plans to sell as much as 8 billion euros ($10.3 billion) of debt today in the country's first test this year of investor appetite for its bonds as credit companies threaten to cut the nation's AAA rating.

"It's going to be a tough one," said Michael Leister, a fixed-income strategist at DZ Bank AG in Frankfurt. "The rating is an evergreen topic. France has been suffering since the second half of December against its AAA peers. But given the importance of the signal from this first auction, I guess it will go alright."

The extra yield investors demand to hold French bonds instead of benchmark German bunds rose to 204 basis points on Nov. 17, the most since 1990, as concern deepened the region's debt crisis was spreading. While the gap was 140 basis points at
8:17 a.m. London time today, it compares with a premium of 47 basis points for AAA rated Finland and 38 basis points for the Netherlands.

The French sale comes a day after Germany sold 4.1 billion euros of bonds, getting more bids than its maximum target of 5 billion euros. The German sale kicked off a rush for funding that may determine whether euro-area leaders can save the 13- year-old single currency. Italy and Spain are among countries that in the coming weeks will sell debt that may reach 262 billion euros in the first quarter, according to Deutsche Bank AG forecasts.

Longer Maturity

France plans to sell securities maturing in October 2021, October 2023, April 2035 and April 2041 today. It sold 4.3 billion euros of debt on Dec. 1, with its benchmark 10-year bonds yielding 3.18 percent. French 10-year bonds fell for a seventh-straight day today, with the yield climbing as high as 3.37 percent yesterday, the most since Dec. 9, and widening the spread with bunds.

The 10-year yield rose 3 basis points to 3.34 percent today. It climbed to a high last year of 3.82 percent on Nov. 17 and fell to a low of 2.44 percent on Sept. 12.

The longer maturity of the bonds being put up for sale may make it a riskier auction, although it will probably go "fairly well" because of French debt's recent underperformance relative to bunds, said Norbert Aul, a fixed-income strategist at RBC Capital Markets in London.

"We do not expect nasty surprises," he said. The offer from the French debt-management body, Agence France Tresor, of long-term bonds is considered "a sign of actual investor demand in this maturity segment," he said.

Sarkozy Efforts

The success of the sale of longer maturing debt will be an indication of investors' faith in the government's ability to manage its debt load, said DZ Bank's Leister.

"France needs to sell longer-term debt because that's what investors and ratings agencies are watching in terms of a signal of confidence," he said. "The market is wary of the financing agency going for the easy option."

The sale comes as President Nicolas Sarkozy -- who faces re-election in about four months -- seeks to protect France's creditworthiness with tax increases and spending cuts.

France has also shrunk its 2012 bond-sale plan, with the debt-management body saying last month it will need 177.9 billion euros in financing this year, down from the 182 billion euros estimated on Sept. 28.

To be sure, the average financing costs of medium and long- term French debt remains low. Last year, it was 2.8 percent, the second-lowest since the creation of the euro, after the 2.53 percent in 2010, according to AFT. The bid-to-cover ratio, or the number of bids received for each unit of debt sold, at auctions last year was 2.4, up from 2.1 in 2010.

Ratings Cloud

Still, concern remains as ratings companies review the sovereign credit grade of Europe's second-largest economy.

Moody's Investors Service said Dec. 12 it will review the ratings of all EU countries after a summit on Dec. 9 in Brussels failed to produce "decisive policy measures" to end the region's debt turmoil.

Standard & Poor's placed the ratings of 15 euro nations, including AAA rated Germany and France, on review for possible downgrades on Dec. 5. Fitch Ratings cut France's credit outlook on Dec. 16 on the "heightened risk of contingent liabilities"
from the euro-region crisis.

Euro-area leaders are struggling to solve the region's sovereign debt crisis that is now in its third year. The push continues with a Jan. 9 meeting between Sarkozy and German Chancellor Angela Merkel in Berlin. Euro area finance chiefs convene in Brussels on Jan. 23, with government leaders gathering a week later.

Slowing Growth

France's woes, like those of other euro-area countries, are compounded by an economy that's edging toward recession as budget cuts to contain the fiscal crisis bite.

The French economy is probably already in a recession that will last through March, national statistics office Insee said last month. The European Commission reduced the region's 2012 growth forecast by more than half to 0.5 percent in November.

The euro has for the first time in a decade recorded two consecutive annual losses against the dollar.

France has the biggest debt burden of the six top-rated euro nations, at 85 percent of gross domestic product. After Italy, it has the most amount of debt coming due this year in Europe at $367 billion, followed by Germany at $285 billion, according to data compiled by Bloomberg.

Governments of the world's leading economies have more than
$7.6 trillion of debt maturing this year, with most facing a rise in borrowing costs.

Governments Borrowing

Led by Japan's $3 trillion and the U.S.'s $2.8 trillion, the amount coming due for the Group of Seven nations and Brazil, Russia, India and China is up from $7.4 trillion at this time last year, according to the data.

France's financial institutions also have the largest debt holdings in the five crisis-hit countries -- Greece, Portugal, Ireland, Italy and Spain -- at $681 billion as of June, according to data from the Bank for International Settlements in Basel, Switzerland.

European banks have about $665 billion of debt coming due in the first six months, according to Citigroup Inc., based on Dealogic data.

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