

Overly Indebted Euro Area Sovereigns: More at Risk Than International Peers?

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INTRODUCTION

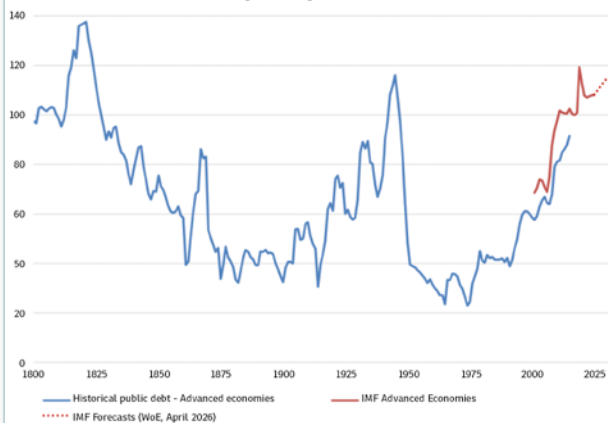
The sovereign debt debate needs to be reframed

Public debt has become a defining feature of advanced economies. It rose from an average of around 40% of GDP in the 1980s to over 120% by 2025 (see Chart 1). Yet the assessment of sovereign debt sustainability continues to focus predominantly on debt-to-GDP ratios. This paper argues that such an approach has become increasingly insufficient. While several advanced economies now carry historically high debt burdens, sovereign vulnerabilities are far from evenly distributed. Our analysis suggests that some highly indebted Euro area Member States are structurally more exposed to a deterioration in financing conditions than other advanced economies carrying comparable – or even substantially higher – levels of public debt, including the United States and Japan.

This apparent paradox reflects differences not simply in fiscal positions, but in monetary sovereignty, economic growth, institutional architecture, financing structures and market resilience. In the current macro-financial environment, these structural characteristics increasingly determine whether high public debt remains manageable or becomes a source of financial vulnerability.

CHART 1.

Advanced economies, gross government debt, % of GDP



A fundamentally different macro-financial environment

The pre-pandemic period, characterised by exceptionally low interest rates, quantitative easing and abundant central bank liquidity, has ended. Higher interest rates, quantitative tightening, demographic pressures, defence spending and weaker productivity growth have fundamentally altered sovereign debt dynamics. As central banks

CHART 2.

Net supply of government bond issuance to private investors

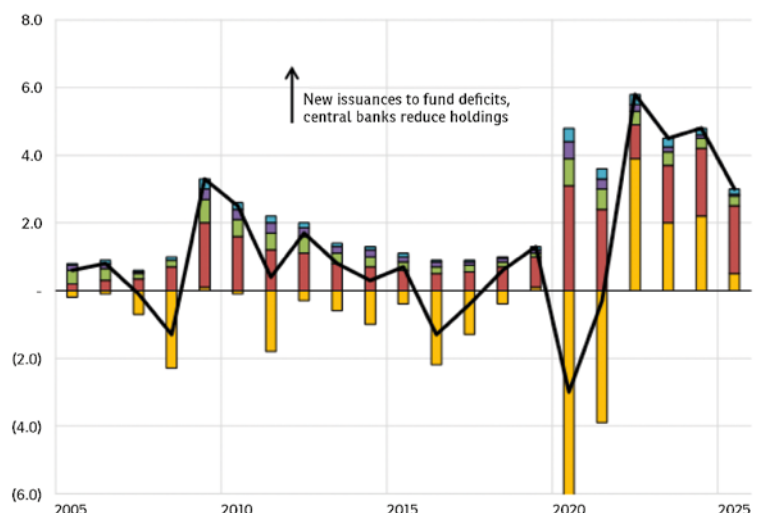
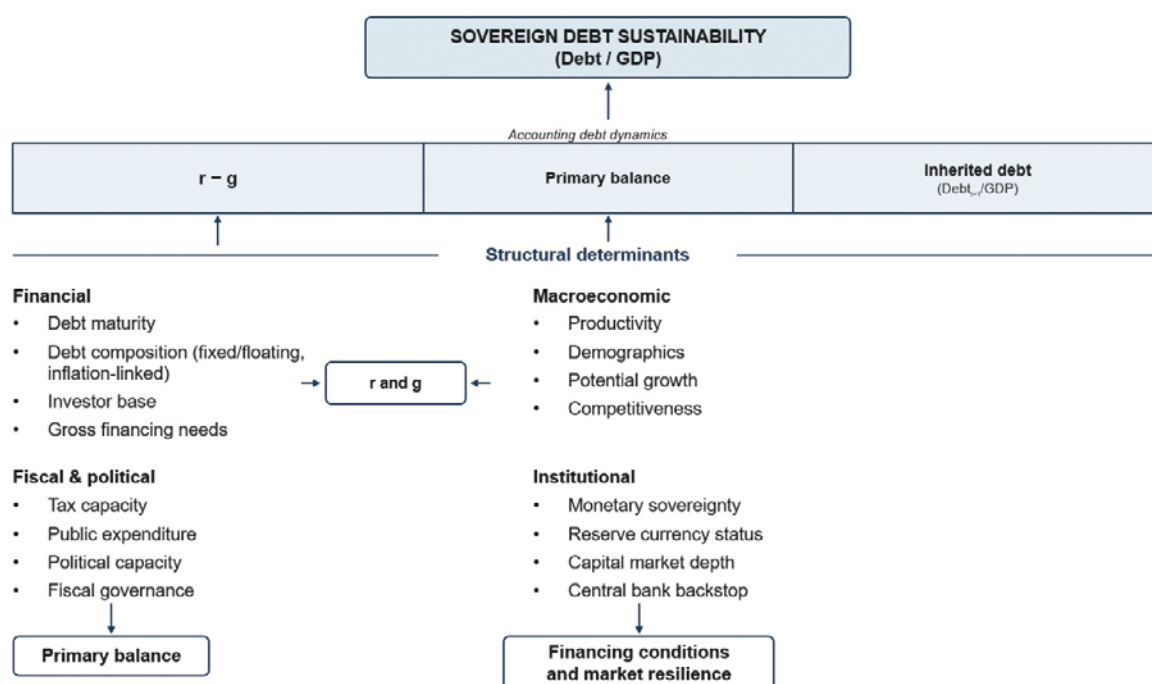


CHART 3.

A multidimensional framework for assessing sovereign resilience



Macroeconomic: $r-g$, potential growth, productivity, demographics, competitiveness.

Fiscal: debt-stabilising primary balance, fiscal capacity, taxation, expenditure quality.

Financial: gross financing needs, maturity, creditor base, external balances, private debt.

Institutional: monetary sovereignty, political capacity, reserve currency status, capital market depth.

gradually withdraw from sovereign bond markets, record gross financing needs must now be absorbed by increasingly price-sensitive private investors – a structural shift that raises both the cost and the volatility of sovereign borrowing (see Chart 2).

The consequences are unlikely to be uniform. Sovereigns combining credible fiscal trajectories, stronger growth, deeper domestic capital markets and greater monetary autonomy are likely to prove significantly more resilient than countries lacking these characteristics.

Why debt-to-GDP ratios no longer discriminate sufficiently between sovereign risks

Ten advanced economies had public debt above 90% of GDP in 2025, five of which were in the Euro area. However, they do not face equivalent risks. Countries displaying similar debt ratios may differ substantially in their ability to absorb future shocks because resilience depends on the interaction between macroeconomic performance, fiscal dynamics, financial structure and institutional arrangements. This observation is particularly relevant when comparing France, Italy and Belgium with the United States and Japan. Although the latter display higher debt ratios, their monetary sovereignty, market depth and investor base provide important stabilising mechanisms unavailable to Euro area sovereigns.

A multidimensional framework for assessing sovereign resilience

Existing analytical frameworks developed by the IMF, the European Commission, the BIS and the OECD have considerably improved sovereign debt surveillance. This paper builds on these approaches rather than challenging them. Its contribution lies in integrating their principal determinants into a single comparative framework centred on sovereign resilience.

None of these indicators alone determines debt sustainability. Their interaction explains why countries with similar debt ratios may exhibit markedly different levels of vulnerability.

The dynamics of public debt is, at its core, an accounting phenomenon: the change in the debt-to-GDP ratio from one period to another is governed by the interaction of three fundamental determinants – the interest rate-growth differential ($r-g$), the inherited debt stock, and the primary budget balance. Any deviation of the primary balance from its debt-stabilising level mechanically translates into a change in the debt ratio, upward or downward.

Yet these three proximate determinants are themselves endogenous to a broader set of structural and institutional forces. The debt service burden is shaped not only by prevailing market interest rates but by the composition of the debt

stock itself – notably its average maturity profile, the share of inflation-indexed or floating-rate instruments, and the structure of the investor base, in particular the relative weight of foreign versus domestic holders and of private versus official creditors, each carrying distinct implications for rollover risk and market sensitivity.

Potential growth, in turn, reflects long-run supply-side fundamentals – above all total factor productivity dynamics and demographic trajectories whose deterioration in most advanced economies structurally compresses the denominator effect that historically helped contain debt ratios.

The primary balance is conditioned by the prevailing degree of political stability, which governs both the capacity to sustain fiscal adjustment over time and the willingness to enforce the expenditure restraint and revenue mobilisation that consolidation requires.

A comprehensive assessment of debt sustainability must further account for private-sector leverage. Countries combining elevated public and private debt are disproportionately exposed to a higher-for-longer interest rate environment, as the simultaneous deleveraging pressures on both balance sheets can amplify contractionary dynamics, erode the tax base, and ultimately impair the sovereign's capacity to generate the primary surpluses on which long-run sustainability rests.

Purpose of the paper

While the macro-financial environment is deteriorating for indebted economies more broadly, exposure to debt sustainability risk – understood as the capacity to generate sufficient resources to

service public debt – is far from uniform. Two countries carrying comparable debt levels can face radically different sustainability trajectories depending on their primary balance, growth outlook, debt structure, institutional framework and political capacity for adjustment, making it difficult to identify a single threshold beyond which debt becomes unsafe.

Rather than asking whether a sovereign debt crisis is imminent, the objective is to understand why apparently similar debt ratios may conceal fundamentally different degrees of resilience, and which indicators deserve the closest attention from policymakers and financial markets in the years ahead.

This note assesses vulnerability along several dimensions: debt arithmetic, debt structure, private sector leverage, and supply-side fundamentals. The arithmetic alone already points to divergent – in some cases unsustainable – trajectories for the United States, France and Belgium, while fiscal effort puts several southern European countries on a more credible path.

Main findings

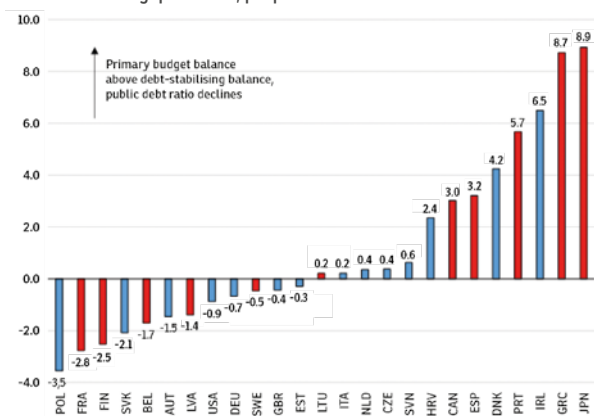
Applying the multidimensional framework developed above to the most highly indebted advanced economies leads to five main findings.

First, debt arithmetic already points to markedly different debt trajectories despite similar debt ratios. While fiscal adjustment is gradually stabilising debt dynamics in countries such as Italy, Portugal and Greece, persistent primary deficits leave the United States, France and Belgium on increasingly difficult-to-stabilise debt paths.

CHART 4.

Fiscal gap and public debt prospects

Chart 4a : Fiscal gap* in 2025, pts points

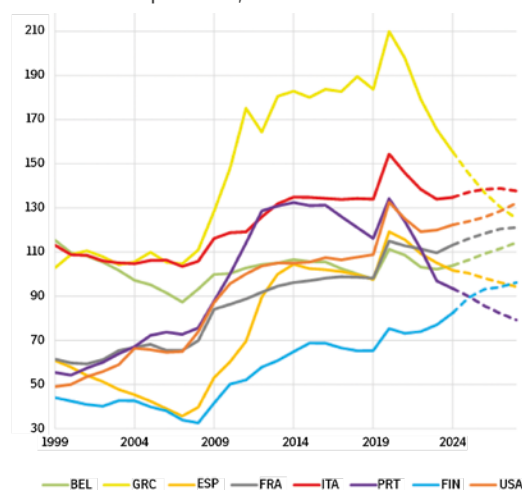


Source: Economics, based on data from the IMF (WoE, April 2026)

Notes: *Gap between the primary balance and the debt-stabilising primary balance.

A negative gap indicates that the primary balance falls short of the level required to stabilize the debt ratio, implying an increase in the public debt-to-GDP ratio relative to the previous year. Red bars are countries with debt to GDP close or above 90% of GDP in 2025

Chart 4b : Gross public debt, % of GDP



Source: Economics, based on data from the IMF (WoE, April 2026)

TABLE 1.

Heatmap of debt sustainability risk – Key indicators across the most heavily indebted advanced economies, 2025

Variable group	Variable	Unit, year	France	Belgium	Italy	Spain	Portugal	Greece	Finland	United States	United Kingdom	Japan	Canada
Arithmetics of public debt	Public debt	% of GDP, 2025	116,0	106,3	137,1	100,4	89,9	145,7	89,3	123,9	102,3	206,5	113,5
	Primary Balance	% of GDP, 2025	-3,1	-3,5	0,5	-0,4	2,1	4,4	-3,5	-3,2	-2,8	-0,9	-2,1
	Stabilizing Primary Balance	% of GDP, 2025	-0,4	-1,8	0,3	-3,6	-3,5	-4,3	-1,0	-2,3	-2,3	-9,8	-5,1
	Fiscal gap	% of GDP, 2025	-2,8	-1,7	0,2	3,2	5,7	8,7	-2,5	-0,9	-0,4	8,9	3,0
Debt structure	Projected Public debt	% of GDP, 2031	120,7	122,3	136,1	90,4	74,4	110,9	100,8	142,1	102,6	192,8	103,5
	Non-resident holders	% of public debt, 2025	54,3	63,4	34,3	48,9	47,2	76,4	61,1	36,0	33,4	11,8	41,0
	Central Banks holdings	% of public debt, 2025	19,2	18,6	18,1	24,4	27,1	10,1	22,4	14,6	18,5	46,3	17,0
	Average weighted Maturity	Years, 2025	8,4	9,9	6,8	7,7	7,6	9,6	7,7	5,8	13,4	9,3	6,7
Supply-Side structure	Variable, Inflation-indexed debt and T-Bill	% of public debt, 2025	19,0	8,0	21,0	11,0	6,0	10,0	10,0	30,0	26,0	12,0	23,0
	Long-term Real GDP growth	%, 2031	1,1	1,3	0,7	1,7	1,6	1,8	1,2	1,8	1,4	0,8	1,8
	Dependency Ratio	2024	40,2	35,7	42,0	34,9	42,5	41,6	42,8	30,8	34,0	54,9	33,2
	Public pensions expenditures	% of GDP, 2025	14,2	13,1	16,1	13,7	12,8	13,2	13,2	5,3	6,2	9,1	7,2
Private debt	Level	% of GDP, 2025	215,4	174,7	94,3	119,3	128,1	97,4	177,4	140,3	132,6	175,1	218,9
	Change 2013-25	pts	32,6	-29,5	-28,7	-88,7	-91,2	-37,4	0,2	-11	-33,8	18,6	29
Government Spending and taxation	Gov. Expenditures	% of GDP, 2025	57,5	38,9	51,1	44,7	43,7	49,7	57,6	37,7	43,6	36,9	44,0
	Interest payment	% of tax burden, 2025	4,8	5,0	8,9	6,3	4,9	7,6	3,7	17,5	9,1	3,6	12,2
	Tax burden	% of GDP, 2025	46,3	44,3	43,2	38,2	37,3	41,6	42,7	26,6	37,3	33,2	14,7

Source: Economics, based on data from the IMF, World Economic Outlook (April 2026); European Commission/ECB; OECD; national authorities

Note: The fiscal gap measures the distance between the observed primary balance and the debt-stabilising primary balance (i.e. the primary balance that would, given the prevailing interest rate-growth differential, hold the debt-to-GDP ratio constant). A negative fiscal gap indicates that the observed primary balance exceeds the stabilising threshold, putting the ratio on a declining path; a positive fiscal gap indicates an insufficient primary balance, consistent with a rising debt ratio. Colour coding follows a traffic-light scale (green: comparatively favourable; red: comparatively unfavourable) applied independently to each across the sample

Second, these accounting dynamics are themselves shaped by deeper structural factors. Italy and the United States remain exposed to refinancing risk because of relatively short debt maturities, whereas France and Belgium are more vulnerable to shifts in investor sentiment owing to their heavy reliance on non-resident investors. High private-sector indebtedness adds a further layer of vulnerability in Belgium, Japan and France, although only France continues to experience rising private leverage. Demographic ageing and weak productivity further aggravate debt dynamics in Italy, are only partly offset by automation in Japan, weigh increasingly on France and Belgium, and remain considerably more favourable in the United States.

Third, several highly indebted Euro area Member States appear structurally more vulnerable than the United States despite carrying comparable – or even lower – public debt ratios. The United States benefits from reserve-currency status, monetary sovereignty, deep and integrated capital markets, stronger long-term growth, energy self-sufficiency and a lower tax burden. By contrast, Euro area sovereigns borrow in a currency they do not individually control, operate within fragmented capital markets and cannot rely on an unconditional central bank backstop. Debt sustainability in the Euro area must therefore be assessed primarily at the level of individual Member States rather than through aggregate Euro area indicators.

Fourth, France emerges as one of the most exposed large Euro area sovereigns. Although its debt ratio remains below Italy's, several forward-looking indicators point to greater vulnerability: a much larger share of debt held by non-residents, the

absence of a primary surplus since 2002, a persistent external deficit, substantially higher private-sector indebtedness and weaker productivity performance. By contrast, Italy has returned to primary surpluses and is pursuing sustained fiscal consolidation despite its much higher inherited debt stock.

Finally, France's fiscal trajectory raises a broader question about the resilience of the Euro area's institutional framework. An economy growing by around 1% cannot indefinitely sustain interest payments approaching 3% of GDP while continuing to run large primary deficits. Rising sovereign yields, increasing market concerns and persistent political difficulties in delivering durable fiscal consolidation suggest that, absent credible adjustment, France's fiscal position could progressively undermine market confidence and generate wider implications for financial stability within the monetary union

1. Debt Arithmetic Suggests Increasingly Difficult to Stabilise Debt Dynamics in the United States, France and Belgium, While Fiscal Efforts Are Putting Some Southern European Countries on a Credible Fiscal Path

Public debt dynamics is an accounting phenomenon. Its variation over time reflects the interaction of three key inputs: the interest rate-growth differential ($r-g$), the inherited level of public debt, and the primary budget balance. The first

CHART 5.**Gross public debt dynamics and drivers across the most indebted countries**

Chart 5a : Change in gross public debt between 2022 and 2025

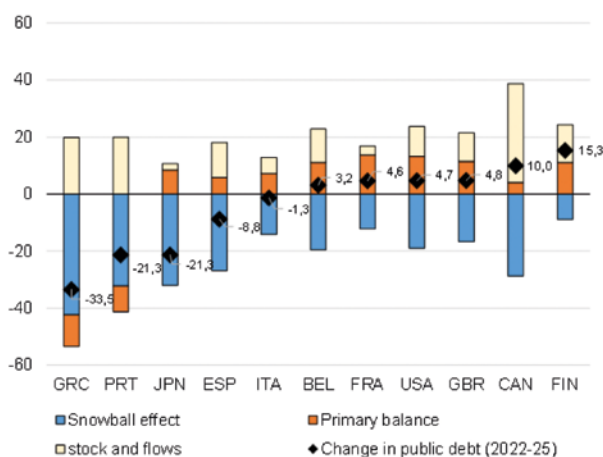
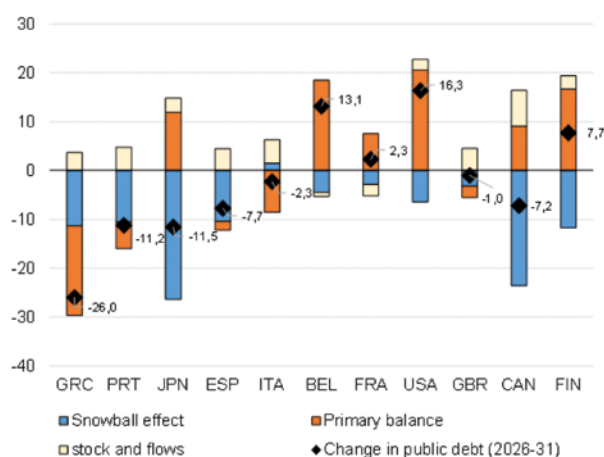


Chart 5b : Projected change in gross public debt between 2026 and 2031



Source: Economics, based on data from the IMF

of these, commonly referred to as the **snowball effect**, captures the mechanical tendency of a debt ratio to rise when the GDP growth rate falls below the interests paid on government debt. From this snowball effect, a debt-stabilising primary balance can be derived analytically – the level of the primary balance that would exactly offset the snowball effect and hold the debt ratio constant. Any primary balance below this stabilising threshold is associated with a rising debt ratio; and where r exceeds g , that threshold is set higher still, since both the inherited stock and the unfavourable differential push the ratio upward.

The sign of the $r-g$ differential determines the level of the primary balance required to stabilise the debt ratio.

- A **negative** $r-g$ differential ($r < g$) implies a deficit-stabilising balance: public debt can be reduced despite a primary deficit, provided that the primary deficit is lower than the stabilising deficit.
- Conversely, a **positive** $r-g$ differential ($r > g$) implies a surplus stabilising balance. To reduce public debt, the primary balance must therefore be in surplus and greater than the stabilising balance.

While the $r-g$ differential has been negative and is projected to remain so in most heavily indebted economies – albeit on a narrowing path – several of them are running primary deficits well above

the debt-stabilising level, such that their debt ratio continues to rise. Chart 5 decomposes the cumulative change in the gross debt-to-GDP ratio of the eleven most indebted advanced economies into its three proximate drivers – the snowball effect, the primary balance contribution, and a residual stock-flow adjustment¹ – over the realised period 2022–25 and the projected period 2026–31. The exercise reveals a striking degree of heterogeneity, which can be organised into five broad archetypes:

1. **Persistent deficits incompatible with debt stabilisation: Belgium, France, the United States, and Finland.** In all four cases, the rise in the debt ratio is overwhelmingly attributable to primary deficits that remain incompatible with stabilisation even where the snowball effect is only mildly favourable: France (+4.6 points of GDP over 2022–25), the United States (+4.7 points), Belgium (+3.2 points) and Finland (+15.3 points – the largest increase in the sample). Projections suggest this pattern is set not merely to persist but to intensify: the United States is projected to accumulate a further +16.3 points and Belgium +13.1 points over 2026–31, with France (+2.3 points) and Finland (+7.7 points) continuing to deteriorate more moderately.
2. **Italy illustrates a contrasting archetype: fiscal consolidation undermined by weak growth and rising debt-servicing costs.** Having

1. The stock-flow adjustment (SFA) captures the difference between the change in the gross debt-to-GDP ratio and the sum of the snowball effect and the primary balance contribution. It reflects transactions that affect the debt level without passing through the deficit – notably financial transactions (acquisitions of financial assets, loan disbursements), valuation effects (exchange rate movements on foreign-currency-denominated debt), and statistical reclassifications. Source: European Commission/Eurostat, AMECO methodology.

returned to a primary surplus in 2024, Italy's primary balance reached 0.8% of GDP in 2025, and is projected to keep rising, to around 1.3% of GDP by 2027. Yet this strengthening fiscal effort has so far delivered only a near-stabilisation of the debt ratio over 2022-25 (-1.3 pts of GDP): with potential growth structurally weak and the cost of debt servicing still rising as the stock of low-yielding debt issued before 2022 is progressively refinanced at higher rates, the snowball effect is projected to roughly neutralize the additional fiscal effort over the near term, leaving debt on a slightly declining path of -2.3 pts over 2026-31 before the consolidation gains take fuller hold. This is consistent with the projected approach of Italian public debt towards 140% of GDP by 2027, overtaking Greece as the most indebted sovereign in the Euro area.

Italy nevertheless remains exposed to the combination of a very high inherited debt stock, weak potential growth and one of the highest interest burdens in Europe. As a result, sustained primary surpluses will need to be maintained over many years before public debt can be placed on a clearly declining trajectory.

3. **Strong nominal growth cushions persistent primary deficits: Japan.** Despite a chronically negative primary balance, its debt ratio fell by -21.3 pts of GDP over 2022-25 and is projected to fall by a further -11.5 pts over 2026-31, as a highly favourable r-g differential – reflecting the post-pandemic resurgence of inflation against a still-contained cost of debt service – performs the consolidation work that the primary balance does not. This lay out illustrates the risk that a benign snowball effect can mask, rather than resolve, an underlying structural deficit problem, leaving debt dynamics vulnerable to any normalisation of the interest rate-growth differential.
4. **Fiscal adjustment compounded by strong growth, on a clearly downward path: Portugal and Greece.** Portugal (-21.3 pts over 2022-25; a further -11.2 pts projected for 2026-31) and Greece (-33.5 pts; -26.0 pts projected) post by far the largest declines in the sample. In both cases, sustained primary surpluses combine with above-average nominal growth to durably outweigh any residual drag from the snowball effect, placing these two countries – paradoxically among the most heavily indebted in the Euro area at the start of the period – on the most credible deleveraging path within the group.
5. **Spain** (-8.8 pts over 2022-25, with a further -7.7 pts projected), the **United Kingdom** (+4.8 pts, reversing to -1.0 pt projected), and

Canada (+10.0 pts, reversing to -7.2 pts projected) **occupy intermediate positions**, combining elements of fiscal effort, supportive growth, and – for the United Kingdom and Canada in particular – an anticipated easing of the snowball effect expected to arrest the recent deterioration in their debt ratios.

Taken together, this decomposition confirms that the level of public debt alone is a poor predictor of sustainability risk. Countries with comparable, or even lower, debt ratios – France and Belgium chief among them – face a markedly less favourable trajectory than some of the currently most indebted economies, owing to the combined effect of high primary deficits and an adverse interest rate-growth differential.

2. Institutional, Financial and Supply-Side Structures Amplify Vulnerability for Italy, France and Belgium – But Provide Japan, Portugal and Greece with a Structural Buffer

The three proximate determinants of public debt dynamics – the r-g differential, the debt stock, and the primary balance – are shaped by a broader set of structural forces that influence how quickly a shock is transmitted to borrowing costs, and how much fiscal capacity a sovereign retains to absorb it. The four categories of factors that matter are: the composition of the debt stock, which determines how quickly a rate shock is passed on to servicing costs; private-sector leverage, which creates contingent fiscal liabilities that materialise precisely when public balance sheets are under the most strain; supply-side fundamentals, such as productivity and demographics, which reduce both potential growth and revenue capacity; and institutional architecture, which determines the conditions under which debt is financed and how resilient market access is under stress. Examining these factors together reveals a markedly different distribution of vulnerability to that suggested by the headline debt ratio alone.

2.1 Debt structure, private-sector leverage and supply-side fundamentals shape the degree of financial vulnerability across highly indebted sovereigns

As specified earlier, public debt sustainability cannot be assessed from the headline debt-to-GDP ratio alone. The dynamics governing debt accumulation – captured analytically by the

CHART 6.**Debt structure and interest payment across selected indebted economies**

Chart 6a: Interest payments, % of GDP

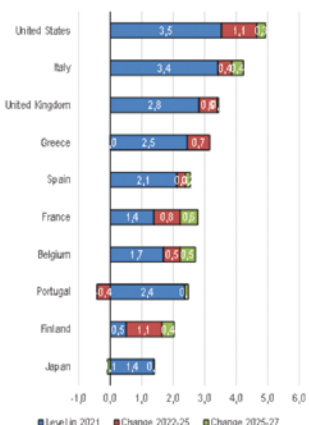


Chart 6b: Average weighted maturity of sovereign in 2025

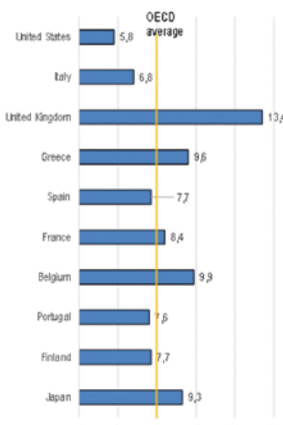


Chart 6c: Instrument composition of the outstanding debt by country in 2025

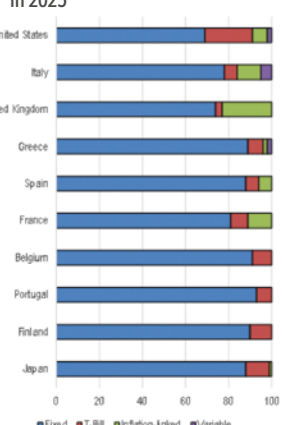
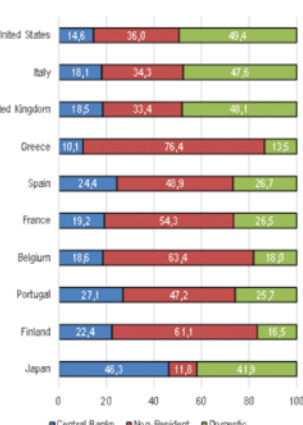


Chart 6d: Holder of government debt in 2025, %



Source: OECD, IMF, ECB, Federal Reserve

interest-growth ($r-g$) differential and the primary balance – are themselves shaped by a wide set of underlying macroeconomic, financial and institutional factors. The BIS Annual Economic Report (BIS AER2026)² frames this multi-dimensionality precisely: “whether fiscal pressures will prove manageable depends on how borrowing costs evolve, which is determined by two factors – the structural demand for government bonds, itself shaped by demographic trends, productivity growth and household saving behaviour; and the capacity of the financial system to intermediate that demand, which can shift rapidly in response to shocks and compress fiscal space well before any limit implied by long-run fundamentals is reached.”

2.1.1 Italy and the United States are rendered vulnerable by their debt maturity, France and Belgium by their debt holders

The structure of public debt – defined by the residency and institutional nature of its holders, the maturity profile of outstanding securities, and the share issued at variable or inflation-linked rates – conditions how quickly and how forcefully a given interest-rate shock passes through to the cost of debt service.

Three channels operate jointly. (I) The maturity structure determines the pace of rollover: a high share of short-term debt forces a government to refinance a larger fraction of its stock at prevailing market rates each year. (II) Floating-rate and inflation-linked instruments remove the buffer that fixed-rate, long-maturity debt normally provides, repricing automatically with policy rates or inflation outturns. (III) And the composition of the investor

base shapes the stability of demand: while a large non-resident holder base signals market access and reduces the adverse feedback loop between sovereign and domestic-bank balance sheets, non-resident holders – particularly non-bank asset managers – are typically more sensitive to global liquidity conditions, making the holder base more prone to sudden stops in periods of stress.

The BIS AER2026 adds a further dimension to this last channel: “the same deterioration in fundamentals can compress fiscal space far more severely” when the financial system’s intermediation capacity is constrained – a risk that has grown as NBFIs, with their “highly leveraged and funding-dependent strategies”, have replaced central banks as the marginal holder of sovereign debt.

Against this framework, the most heavily indebted advanced economies display markedly different vulnerability profiles.

Italy, the United States and the United Kingdom stand out for the level and continued rise of their interest burden, even though they reach it through different channels. Italy’s interest payments rose from 3.4% of GDP in 2021 to a projected 4.2% by 2027, driven by a short average maturity (6.8 years) and a meaningful inflation-linked component. The US shows an even sharper increase (3.5% to close to 4.9%), reflecting the shortest maturity in the group (5.8 years) and an instrument mix tilted toward T-bills, which forces continuous rollover at prevailing rates. The UK reaches a comparably elevated burden (2.8% → roughly 3.4%) through the opposite channel: its maturity is the longest in the sample (13.4 years), but its 24–25% inflation-linked share drives the increase.

2. BIS, Annual Economic Report, June 2026.

France and Belgium sit at the other end of the maturity spectrum (8.4 and 9.9 years) with a far smaller indexed component, which has so far kept their interest burden lower and its increase more contained (1.4% → 2.8% for France; 1.7% → 2.7% for Belgium). Their vulnerability lies elsewhere: both rely heavily on non-resident holders (54.3% and 63.4% of public debt respectively), well above the OECD norm, leaving debt service exposed to shifts in foreign investor sentiment. In the BIS AR2026's framing, this matters beyond the yield level itself: "fiscal risk repricing can tighten financial conditions quickly and weigh on demand, especially if amplified by NBFI deleveraging" – precisely the channel to which France and Belgium are most exposed given the dominance of price-sensitive foreign holders, especially hedge funds, in their creditor bases.

Greece, Japan and Spain show comparatively favourable headline structural metrics, but for reasons that are partly mechanical rather than durable. Greece combines the highest non-resident share in the sample (70.8%) with the longest average maturity (~18 years); however, much of that foreign holding is concessional official-sector lending rather than price-sensitive market debt, keeping its interest bill on a declining trajectory (3.5% in 2019 → 3.3% projected by 2027). Japan's long maturity (9.5 years) and very low non-resident share (14%) delay rate pass-through despite a debt ratio above 200% of GDP, but the BIS AR2026 characterises this cushion as temporary rather than structural, flagging that "debt maturity influences the balance between channels: shorter maturities speed up the pass-through to fiscal

costs" – a mechanism that will reassert itself as Japan's legacy low-yielding debt progressively rolls over.

Across nearly all these economies, one common factor partially offsets country-specific pressures: **central banks retain a meaningful footprint in sovereign debt markets despite quantitative tightening.** Eurosystem PSPP/PEPP holdings still cover a comparable order of magnitude across France, Belgium and Italy (17–19% of general government debt), and notably higher shares in Spain (24%), Finland (22%) and Portugal (27%). This residual footprint continues to provide a common, if diminishing, cushion against the upward pressure on long-term yields that would otherwise compound each of the channels described above.

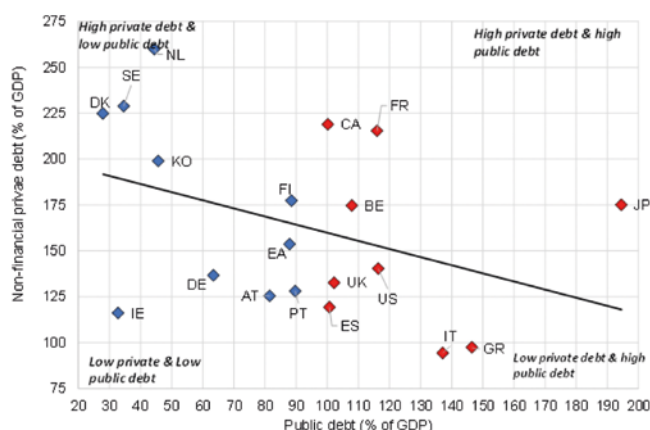
2.1.2 Belgium, Japan and France combine public and private leverage above prudential thresholds – but only France's is still rising

Excessive private debt poses risks to public debt sustainability through several channels. When private debt becomes unsustainable, the state typically absorbs the shock through bank recapitalisation and automatic stabilisers, effectively converting private liabilities into public ones; a high pre-crisis public debt level leaves far less fiscal space to play this lender-of-last-resort role (Jordà, Schularick and Taylor, 2016)³. Even absent an acute crisis, rapid household and corporate debt buildup tends to predict slower growth three to four years later as deleveraging compresses consumption (Mian, Sufi and Verner,

CHART 7.

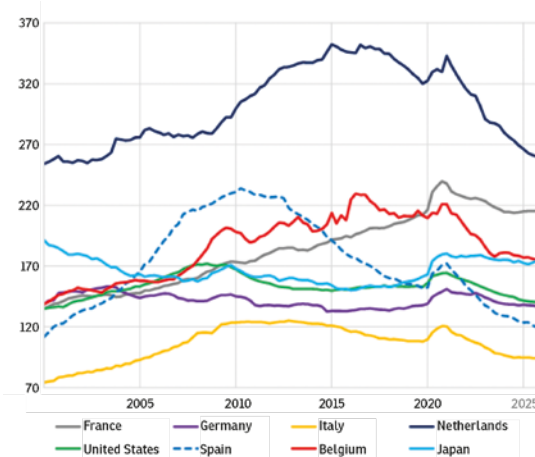
Private and public debt across indebted economies

Chart 7a : Private debt v. public debt across advanced, as of Q4-2025



Source: Economics, based on data from the Bank for International Settlements

Chart 7b : Non-Financial Private sector debt, % of GDP



3. Jordà, Ò., Schularick, M., & Taylor, A. M. (2016). Sovereigns versus banks: credit, crises, and consequences. *Journal of the European Economic Association*, 14(1), 45-79.

2017), mechanically eroding the denominator of the debt ratio⁴. The BIS AER2026 formalises this link explicitly, noting that "public debt may increase due to the fiscal costs of future financial crises, which tend to be linked to the scale of private non-financial sector debt" – and while private debt has fallen slightly since the GFC across advanced economies as a whole, it "remains historically high in several AEs."

This vulnerability maps unevenly across the sample and can be organised into three groups defined by the level of private debt.

A first group – Spain, Italy, Portugal and Greece – carries private debt below 130% of GDP and has seen sustained deleveraging since 2013: Spain's ratio fell by roughly 88 points to 119.3% of GDP by end-2025, Italy's by 29 points to 94.3%, Portugal's by 91 points to 128.1%, and Greece's by 37 points to 97.4% – all four now within or below the Euro area average of 153.6%, despite public debt ratios of 81-147% of GDP.

A second group – the United States and the United Kingdom – carries private debt in the 130-150% range, also on a declining trajectory: US private debt fell by roughly 11 points between 2013 and 2025 to 140.3% of GDP, and the UK's by 34 points to 132.6%. Both combine this moderate and receding private leverage with elevated but comparably contained public debt (116% and 102% of GDP respectively), limiting the scope for private-sector stress to compound their sovereign burden – though the US remains exposed through the sheer scale of its refinancing needs and the structural rather than cyclical nature of its deficit.

A third, more acute risk category comprises France, Belgium, Finland and Japan, all carrying private debt above 170% of GDP. Their recent trajectories diverge, however. Belgium's private debt fell by roughly 30 points from 204.2% in 2013 to 174.7% by end-2025, and Finland's remained broadly flat at 177.4% (up only 0.2 points). France and Japan stand apart: France's private debt rose by approximately 26 points to 215.4%, and Japan's by 16 points to 175.1%. France's trajectory is particularly notable – at 215.4% of GDP, it now converges toward the Netherlands (260%), one of the advanced economies with the highest private debt in the world, whose own ratio nonetheless fell by 77 points over the same period. Unlike the Netherlands, however, France combines this still-rising private leverage with a public debt ratio of 116% and weak potential growth, placing it in the most exposed quadrant of the public-private debt matrix.

2.1.3 Demographics and productivity worsen the debt arithmetic in Italy, are partly mitigated by automation in Japan, represent an unresolved structural challenge in France and Belgium, and still favour the United States

Population ageing and weak productivity growth have implications for public debt sustainability. On the growth side, a declining working-age share mechanically reduces labour input and potential output, widening any positive $r-g$ gap and raising the primary surplus required merely to stabilise the debt ratio; productivity weakness compounds this by lowering g independently of demographics. The BIS AER2026 identifies both as structural forces reshaping long-run borrowing costs: "as populations age and shift from saving to dissaving,

CHART 8.

Demographics, pensions costs and potential growth's long-term prospects among indebted economies

Chart 8a: Average annual potential growth, %

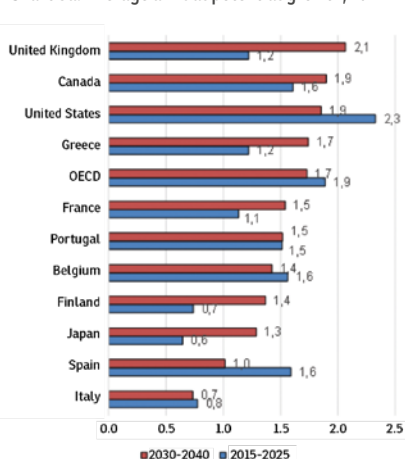


Chart 8b: Old-age dependency ratio (65+ / 20-65)

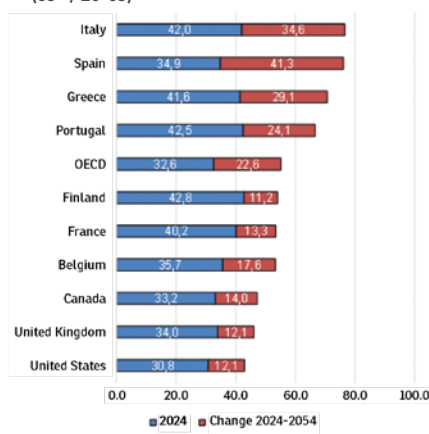
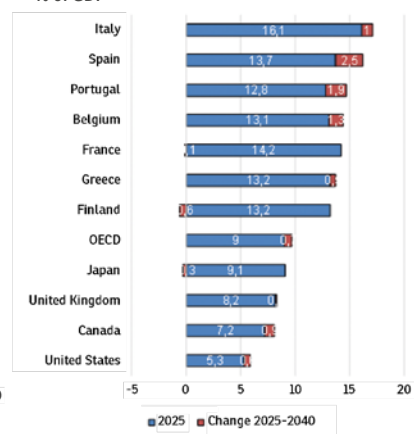


Chart 8c: Public pensions expenditures, % of GDP



Source: OECD extracted from "Pensions at Glance", 2025 and OECD global long-run economic scenarios: 2025 update

4. Mian, A., Sufi, A., & Verner, E. (2017). Household debt and business cycles worldwide. The Quarterly Journal of Economics, 132(4), 1755-1817.

while also demanding more health and social services, aggregate saving may fall, putting upward pressure on real interest rates" – a dynamic whose "timing and scale are highly uncertain" but whose direction is not. On the primary balance side, higher dependency ratios raise age-related expenditure – pensions, healthcare and long-term care – and the BIS projects these to "continue to exert upward pressure on pension and healthcare expenditures in many countries", with demands for higher public investment in infrastructure, defense and renewable energy "intensifying" simultaneously. OECD-wide projections point to an average increase in fiscal pressure of close to 6¼ points of GDP by 2060, of which ageing accounts for more than 40%, absent corrective action⁵.

Exposure across the sample is markedly uneven. **Japan and Italy stand out as the most demographically advanced, both having experienced a roughly fivefold increase in their old-age dependency ratio since 1960 to around 55%, but their growth responses diverge sharply.** Italy's potential growth has remained the lowest in the OECD (0.7–0.8%), compounding a dependency trajectory set to push the ratio from 39 to as much as 70 per 100 working-age people by 2050. Japan, despite comparable demographic compression, has used sustained investment in automation to lift potential growth from 0.6% to a projected 1.3% – a partial offset whose durability the BIS itself questions, given the exposure of Japan's debt dynamics to any normalisation of the r–g differential.

Spain, Greece and Portugal form a second cluster, also characterised by dependency ratios above the OECD average in 2024 (around 42–43% for Italy-comparable for Greece and Portugal, and a lower starting point but the steepest projected increase for Spain, which is set to overtake Italy by 2054 at roughly 76%). Unlike Italy, however, all three show meaningful, if uneven, improvement in potential growth: Greece and Spain are projected to see potential growth rise from around 1.0–1.2% to 1.6–1.7%, while Portugal remains flat at a moderate 1.5%. This relative growth resilience only partially mitigates the fiscal channel, since ageing-related expenditure remains on a steep path regardless of the growth outlook: Spain's public pension spending is projected to rise by 2.5 points of GDP by 2040 to around 16%, among the highest in the EU, while Portugal's is set to climb from 12.8% of GDP in 2025 to 15.1% by 2045, the third-highest ratio in the EU. For this group, the primary-balance channel via ageing costs therefore dominates the growth channel as the principal sustainability risk, even where productivity prospects are improving.

France, Belgium, Finland, the United Kingdom and Canada hold an intermediate position, differentiated chiefly by the trajectory of ageing-related costs. France's pension spending, already as high as 14.6% of GDP across 42 distinct regimes, faces renewed pressure following the suspension of the 2023 pension reform until January 2028. Belgium faces a comparable challenge: pre-reform projections pointed to a 4.7 point rise in total age-related expenditure by 2070, well above the 1.3 point EU average, though a March 2026 draft reform is expected to reduce the projected increase by 1.3 points. Finland, by contrast, benefits from strong innovation fundamentals and favourable AI-complementary employment, consistent with potential growth more than doubling from 0.7% to 1.4%.

The United States anchors the opposite end of the spectrum – with the lowest dependency ratio in the sample (31% in 2024, projected to rise to only 43% by 2054) and potential growth supported by technology investment – but two caveats temper this structural advantage: potential growth is expected to decelerate from 2.3% to 1.9% as the investment impulse normalises, and public healthcare spending (8.5% of GDP federally, close to 10% with state and local outlays) constitutes a structural primary-balance risk not captured by the dependency ratio alone.

2.2 Fragmented markets, weak productivity, faster ageing and the absence of a unified fiscal authority leave indebted Euro area Member States more exposed to adverse financing conditions than the United States

One might argue that concerns over European public debt are exaggerated: after all, the United States carries a debt burden exceeding 120% of GDP, set to rise to 143% by 2035, and is widely regarded as the world's anchor sovereign. Such comparisons, however, risk conflating fundamentally different economic realities – and European leaders who invoke them to reassure markets and citizens risk underestimating the structural divergence between the two sides of the Atlantic. The United States therefore illustrates that reserve-currency status considerably increases fiscal space but does not remove the need for long-term fiscal adjustment when structural primary deficits remain exceptionally large.

The United States combines elevated public indebtedness with robust growth dynamics, sustained productivity gains and unparalleled innovative capacity. Since the pandemic, the US

5. OECD (2025), *Pensions at a Glance 2025: OECD and G20 Indicators*, OECD Publishing, Paris, <https://doi.org/10.1787/e40274c1-en>

economy has grown materially faster than the Euro area, driven by leadership in high-value sectors – digital technologies, artificial intelligence and advanced services. Its deep and unified capital markets, reserve currency status, full monetary sovereignty and fiscal unity further distinguish its structural position. Crucially, the US tax burden remains in the 25-27% of GDP range, significantly below the 40%-plus levels typical across the European Union and above 45% in France – a lower ratio that reflects not only political choices and differing welfare-state models, but also a structurally different incentive environment for growth and private investment. And unlike most European economies, the United States has in recent years re-attracted large-scale industrial investment: industrial investment surged by 32% over 2025 to reach USD1,800 billion⁶, pointing to a productive-base expansion that materially underpins its debt trajectory.

Several European economies, by contrast, face high and rising debt in a context of weaker productivity growth, fragmented capital markets, heavy compulsory levies and limited technological dynamism. To equate the two situations is therefore misleading: debt sustainability cannot be assessed in isolation from growth potential, institutional architecture, fiscal structure and innovation capacity. Aggregate Euro area indicators, to which European leaders often refer, obscure deep structural divergences between Member States – and the Euro area itself does not rest upon a fully unified fiscal authority, a deeply integrated capital market or a single political executive accountable for macroeconomic stabilisation.

The contrast in institutional architecture is, in this respect, the most consequential distinction. The United States issues the world's reserve currency, borrows in a deep and unified sovereign bond market, retains full monetary sovereignty and benefits from an implicit central bank backstop unconstrained by supra-national governance. Euro area Member States enjoy none of these advantages: they borrow in a currency they do not individually control, rely in several cases heavily on non-resident and price-sensitive investors, and operate within a bank-sovereign nexus that can amplify shocks rapidly – as the 2011–2012 sovereign debt crisis demonstrated.

The ECB can act as a backstop through the TPI and OMT mechanisms, but its support is conditional, bounded by its mandate, subject to Governing

Council decisions and eligibility requirements: it cannot be viewed as an unconditional liquidity guarantee of the kind implicitly available to the US Treasury. This institutional fragility is compounded by the economic fragmentation of the union itself – a context that fosters divergence rather than coordination and sustains a climate of mutual distrust that makes collective responses to fiscal stress both slower and less credible⁷.

2.3 France's fiscal trajectory is more concerning than Italy's – and could jeopardise the long-term viability of the monetary union

France carries a lower headline debt ratio than Italy, yet its fiscal position appears more vulnerable on several forward-looking sustainability indicators. France appears to have lost control of its public finances" – a judgment supported by four structural divergences that distinguish the French situation from that of its Italian peer.

1. **The primary balance.** France has not recorded a primary budget surplus since 2002 – more than two decades of uninterrupted primary deficits, regardless of the economic cycle. Italy, despite a far higher headline debt ratio, returned to primary surplus in 2024 (+0.4% of GDP against a deficit of 3.6% the previous year) and is projected to maintain and deepen that surplus to around 1.1% of GDP by 2026. The contrast is stark: Italy's consolidation is driven partly by necessity – rated BBB by S&P, one notch above non-investment grade, a downgrade would trigger forced selling by institutional investors bound by investment-grade mandates – while France's still high-grade rating (AA- from S&P, six notches above the speculative threshold) has removed the market-imposed urgency that typically compels adjustment. The consequence is visible: France's primary deficit widened in 2024 relative to 2023, moving in the opposite direction to every other major indebted Euro area sovereign.
2. **The trade performance.** France runs a structural trade deficit – averaging around €23 billion per year since 2007, when it last recorded a surplus – while Italy has posted a trade surplus averaging over 2% of GDP annually since 2012. This divergence reflects fundamentally different productive structures: the share of industry in value added fell from 16% to 10% in France between 1999 and 2024,

6. Guichard Guillaume, "Les Etats-Unis de Trump continuent d'attirer un déluge d'annonces d'investissements industriels", Les Echos, 23 February 2026.

7. Diverging fiscal interests have repeatedly prevented meaningful agreements, with the euro becoming a permanent source of issues to negotiate and "regularly a source and a manifestation of some discord among Member States. When mutual trust in adherence to common fiscal rules weakens, the architecture becomes more fragile still – and for the most indebted and fiscally exposed Member States, that fragility cannot be offset by pointing to the aggregate debt ratio of the bloc. Debt sustainability in the Euro area is ultimately a Member State-level phenomenon; and it is at that level – not the aggregate – that the risks identified in this note must be assessed.

CHART 9.

Fiscal and external performances of France and Italy

Chart 9a: Current account balance, % of GDP

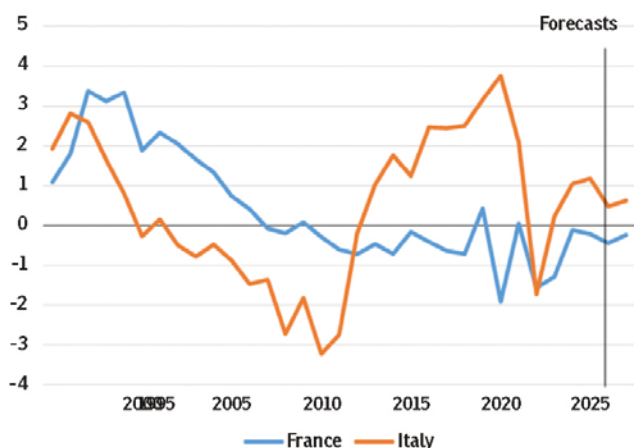
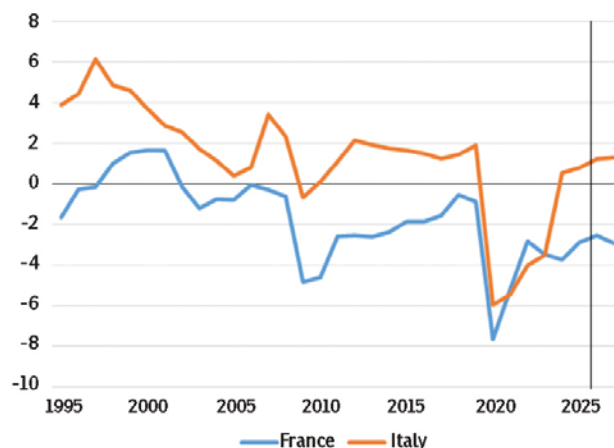


Chart 9b: Primary budget balance, % of GDP



Source: Economics, based on data European Commission (Spring Forecasts of May 2026)

while remaining stable at around 20% in Germany and recovering in Italy. France's de-industrialisation, compounded by one of the highest tax burdens in Europe, has shifted the economy toward services with structurally lower productivity – and it is productivity, ultimately, that generates the tax revenues a state needs to service its debt.

3. **Private sector leverage.** Private non-financial sector debt in France reached 215.4% of GDP by end-2025 – more than double Italy's 94.3% and well above the Euro area average of 153.6%. As discussed in Section 2.2.2, this dual exposure of both the public and private balance sheets is the configuration that leaves the state least equipped to absorb a private-sector shock, since it would be called upon to recapitalise banks and support the economy at the very moment its own fiscal space is most constrained.
4. **The creditor base.** More than half of France's public debt is held by non-residents, compared with around 30% in Italy. Whilst the presence of foreign investors traditionally signals trust and creditworthiness from the market, too heavy a reliance on non-domestic private investors may constitute a structural vulnerability, as identified in Section 2.2.1. Most foreign investors are private and price-sensitive. For instance, the *Banque de France*⁸ noted a stark increase in transactions operated by hedge funds on the secondary European sovereign markets including France, doubling between 2019 and 2023. This heavy reliance on price-sensitive foreign investors exposes the sovereign risks in a rush for exits, herd

behaviour, and sudden stops in funding during crises – precisely the moment when domestic fiscal pressures are most acute.

Assembling these four factors, the arithmetic of France's fiscal trajectory is revealing. France's primary deficit in 2026 is projected at 2.7% of GDP, against a debt-stabilising balance of only 0.3% – a gap of more than 2 points that places the debt ratio on an unambiguously rising path. As a result, public debt is set to rise from 116% of GDP in 2025 to approximately 118.4% in 2026 and 120-122% by 2027-2031 depending on the source.

The underlying debt arithmetic raises a fundamental sustainability question: How can a country sustain interest payments equivalent to 3% of GDP when its economy is growing by only 1%?

Interest payments, which rose from €36.9 billion in 2019 to €66.6 billion in 2025, are projected to reach €88.2 billion by 2027 (close to 2.9% of GDP) according to the EU Commission forecasts dating from May 2026, surpassing education spending and becoming the single largest item in the national budget. As of mid-August 2026, France's 10-year yield was already surpassing 4% against a potential growth rate barely exceeding 0.7-0.8% in 2026-2027, a configuration that makes the *r-g* differential structurally debt-increasing absent a decisive primary balance adjustment. Between 2019 and 2024, total factor productivity in France declined by 2.6%, against an increase of 18.5% in Germany over 1999-2024 and only 0.1% in Italy over the more recent period – a structural competitiveness gap that directly erodes the government's capacity to generate the revenues necessary to service a rapidly rising debt.

8. Banque de France, Financial Stability Report, June 2026.

The market is beginning to price this divergence. Since June 2024, the French 10-year government bond yield has successively risen above those of Portugal, then Spain from October 2024, and Greece from June 2025. By mid-August 2026, it stood some 40 to 50 basis points above the yields of all three countries. More recently, the French yield has also edged above Italy's by a few basis points, making France the country with the widest spread over Germany among the economies that were at the epicentre of the 2011–12 sovereign debt crisis – a clear signal of growing investor unease.

France is replacing Italy at the focal point for market concerns about debt sustainability in Europe. As J. de Larosière states in his article for the *Eurofi Magazine* (September 2026), some bond market investors appear to consider that French public finances will somehow benefit from largesse via a bail-out from the European Central Bank. Otherwise, it is difficult to understand why yields on French 10-year bonds are trading at only 0.8 percentage points over German government bonds. This 'spread' is up from a range largely below 0.5 points in the decade to mid-2024. But it compares favourably with a yield spread of 1.8 points for the UK, whose public finances, although far from healthy, are in a less poor state than France's.

An effort is needed to reduce the primary French deficit from 2,9% of GDP to a stabilising level of around +0,1% and could be achieved over several years. The problem cannot be resolved in its fundamental aspects by a mere support by the ECB. If the ECB were to indulge in buying the public debt that cannot be absorbed by markets anymore, this would not change the basic structural weaknesses that lie at the heart of France's adjustment problems. The worse of all scenarios would be to see the ECB throwing unconditional money at problems that require reforms more than financing. Such a scenario would lead to more inflation and less growth.

As D. Cahen (2025) warns⁹, the structural factors contributing to France's deteriorating fiscal position "are already in place, though their effects are unfolding gradually."

Beyond a certain threshold, the gradual drift in sovereign spreads could accelerate sharply; a sharp rise would trigger contagion to other highly indebted, low-growth economies within the Euro area. The end-state of a failure to adjust, D. Cahen (2025) concludes, is not merely a French fiscal crisis: it is a scenario that "could have significant implications for financial stability within the Euro area and test the resilience of the institutional

framework established since the sovereign debt crisis."

Conclusion

The analysis confirms that sovereign debt sustainability cannot be inferred from the public debt ratio alone. The transition from exceptionally low interest rates and large-scale central bank purchases to higher financing costs, quantitative tightening and record sovereign issuance has increased the importance of fiscal flows, growth capacity, debt structure, investor composition and institutional credibility. The relevant distinction is therefore not simply between countries with high and low debt, but between sovereigns whose economic and institutional frameworks can absorb adverse shocks and those whose vulnerabilities may reinforce one another.

The comparative assessment also points to an important asymmetry. The United States and Japan face substantial and, in several respects, rising fiscal risks; reserve-currency status, monetary sovereignty or a stable domestic investor base do not eliminate the need for adjustment. Nevertheless, in the current macro-financial environment, several highly indebted Euro area Member States appear structurally more exposed to adverse financing conditions than some advanced economies carrying even higher debt ratios. This reflects the interaction of weaker potential growth, persistent primary deficits, more fragmented capital markets, greater dependence on non-resident investors and the absence of full national monetary sovereignty.

Italy illustrates a different configuration: despite credible fiscal adjustment, its exceptionally high inherited debt stock and weak potential growth imply that maintaining debt on a firmly declining path will require sustained primary surpluses over an extended period.

These findings should not be interpreted as a prediction of an imminent sovereign crisis or as a mechanical ranking of countries. They identify relative vulnerabilities that may evolve with policy choices, growth outcomes and market conditions. The policy implication is that fiscal consolidation alone, while necessary in the most exposed countries, will not be sufficient: strengthening sovereign resilience also requires productivity-enhancing reforms, deeper and more integrated capital markets, credible medium-term fiscal frameworks and an institutional architecture capable of containing destabilising feedback loops.

9. D. Cahen, *The Euro Is in Danger*, Odile Jacob, 2025.