The Impact of Elections on European Financial Indices: Do Political Events in Europe Influence Market Returns?

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Diplôme : Master en sciences de gestion, à finalité spécialisée en Banking and Asset Management
Année académique : 2024-2025
URI/URL : http://hdl.handle.net/2268.2/25010

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THE IMPACT OF ELECTIONS ON EUROPEAN FINANCIAL INDICES: DO POLITICAL EVENTS IN EUROPE INFLUENCE MARKET RETURNS?

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Master thesis presented by
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To obtain the degree of
MASTER IN MANAGEMENT
with a specialization in
Banking and Asset Management
Academic year 2024/2025

Ecole de Gestion de l'Université de Liège

Acknowledgments

First and foremost, I would like to express my deepest appreciation to my supervisor, Professor Georges Hübner, for his availability, attentive guidance, and advice throughout the writing of this thesis. His rigorous and encouraging supervision was crucial in the successful completion of this work.

I also wish to thank Mr. Vincent Colot for taking the time to read and assess my thesis.

My heartfelt gratitude goes to my parents, whose constant support, encouragement, and presence have been invaluable throughout this academic journey.

Lastly, I extend my warmest thanks to my fellow students from the double degree program in Rome. Sharing the experience of writing our theses together has been a tremendous source of strength and motivation.

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List of Abbreviations

EPU	Economic Policy Uncertainty
MLR	Multiple Linear Regression
OLS	Ordinary Least Squares
VIF	Variance Inflation Factor
ADF	Augmented Dickey-Fuller
IFES	International Foundation for Electoral Systems

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1 Introduction

1.1 Background and Context

The relationship between political events and financial markets is a topic of particular interest in financial economics. Markets are inherently forward-looking, reacting to economic fundamentals, political uncertainty and institutional change. Among political events, elections represent a key moment of potential disruption or continuity, during which market participants reassess expectations regarding fiscal policy, regulation, taxation, and international relations. The impact of elections on stock markets has been studied in contexts such as the United States (Santa-Clara & Valkanov, 2003), emerging economies (Dinç, 2005) and is increasingly studied in European countries as political landscapes have grown more volatile.

In the European context, the influence of elections on stock market returns is especially relevant. The European Union represents a complex political and economic union where decisions made at both national and EU levels can have widespread consequences. Political shifts in major EU economies like France and Germany tend to generate heightened investor attention due to the weight these countries carry within the Eurozone. Research by Białkowski, Gottschalk, and Wisniewski (2008) found that national elections in OECD countries can lead to significant increases in stock market volatility. This finding is confirmed in later studies focused by Pastor and Veronesi, 2013. More recently, Ghirelli, Pérez, and Urtasun (2021) showed that political uncertainty in the Euro Area, focusing on Spain, significantly affects stock returns and risk premia.

France and Germany are of particular interest due to their contrasting political systems and market dynamics. France's semi-presidential system and history of political shifts create different anticipatory reactions compared to Germany's more consensus-driven, federal parliamentary system. For instance, elections in France often introduce substantial policy uncertainty depending on the ideological distance between candidates. In contrast, Germany's coalition-based politics may lead to more moderate market reactions.

From an investor's perspective, understanding the timing and nature of these political events is critical for managing risk and exploiting opportunities. Elections can coincide with abnormal returns, either due to policy surprises or shifts in investor risk perception. Portfolio managers, institutional investors, and policy analysts are increasingly interested in quantifying the extent to which political cycles influence market behavior, especially in environments marked by populist movements, geopolitical instability, and fiscal uncertainty. This research, focusing on the legislative elections in France and Germany, is particularly pertinent given the rise of Euroscepticism and the polarization of electorates, which can alter market expectations around EU integration, monetary policy, and regulation.

Exploring the impact of European elections on financial markets offers valuable insights into the political sensitivity of financial markets, as well as into the broader mechanisms through which investor sentiment and macroeconomic expectations are shaped in the European context.

1.2 Research Problem

This thesis seeks to address a central question: What is the impact of political elections in Europe on the performance of major European financial markets, as measured by national stock indices such as the CAC 40 (France) and the DAX (Germany)? While the literature acknowledges the influence of political events on market behavior, empirical evidence specific to European elections remains fairly limited.

By combining macroeconomic, financial, and political variables in a structured regression model, this thesis aims to quantify the effect of elections on stock returns. It also explores how these effects may vary depending on market conditions and political contexts. The findings are intended to help investors better understand and anticipate market reactions to political events, thereby contributing to more informed decision-making and risk management strategies, allowing investors to better prepare their reaction to political events.

1.3 Research Objectives

The main objective of this thesis is to empirically assess the effect of legislative elections on the returns of major European stock indices, with a specific focus on France and Germany. To achieve this goal, the thesis pursues the following specific objectives:

- To identify and quantify the impact of national election periods on the monthly returns of the CAC 40 (France) and DAX (Germany).
- To evaluate whether this impact is moderated by macroeconomic factors such as inflation and GDP growth, and financial market trends such as the MSCI Europe Index performance.
- To analyze how political factors, including the ideological orientation of the elected government, influence post-election market behavior.
- To incorporate interaction effects in the econometric model to better understand how the effect of elections is shaped by underlying economic and policy uncertainty.
- To provide actionable insights for investors, portfolio managers, and financial analysts seeking to better anticipate market responses to political events in the European context.

By meeting these objectives, this research contributes to a more nuanced understanding of the relationship between democratic processes and financial markets.

2 Literature Review

2.1 Politics and Financial Markets

2.1.1 Impact of Political Events on Stock Markets

Elections represent pivotal moments of uncertainty and potential policy transformation, which can significantly affect investor sentiment and asset pricing. Political uncertainty during electoral periods is especially impactful, as markets attempt to anticipate the implications of possible shifts in government leadership and economic direction.

Empirical research has often demonstrated that elections tend to trigger fluctuations in stock prices, often attributed to the reassessment of future policy risks and opportunities. For instance, Pantzalis, Stangeland, and Turtle (2000) investigated the effects of national elections across various countries and found that abnormal stock returns were prevalent in the pre-election period, especially in cases where opposition parties were expected to win. Their findings support the Uncertain Information Hypothesis (UIH) by Brown et al (1988), which suggests that markets initially react negatively to political uncertainty but recover once that uncertainty is resolved, leading to the repricing of assets.

This framework is particularly relevant in the context of fragmented or polarized political systems as the European Union, where the outcome of legislative elections can create ambiguity over future fiscal policies, regulatory directions, or even the stability of governing coalitions. The Legislative power, held by the different Parliaments of the countries, plays a crucial role in shaping financial regulation and trade agreements, thus increasing the stakes for investors during election periods.

Further expanding on this relationship, Faccio (2006) analyzed the performance of politically connected firms during periods of political transition. The findings revealed that firms with direct political ties, such as board members who previously held public office, tend to experience less negative price adjustments during uncertain political episodes. This phenomenon underscores the perceived resilience of politically connected firms.

Goodell and Vähämaa (2013) focused on U.S. presidential elections and their effect on implied market volatility, concluding that periods of political uncertainty led to significant spikes in volatility, especially as elections draw near. While the institutional setting of U.S. elections differs from European legislative contests, their findings are transferable in terms of mechanism: as uncertainty rises, so does the cost of risk, often reflected in heightened volatility indices and shifts in capital allocation. A similar pattern can be expected in European markets, particularly when elections involve significant ideological realignments, such as surges in populist or Eurosceptic parties.

The theoretical underpinning for these observations is further developed by Pastor and Veronesi (2013), who constructed a model showing that political uncertainty imposes a risk premium on financial markets. Investors, facing ambiguity over future policies on taxation, regulation, and public spending, require higher expected returns to bear this risk. In the EU context, where policy changes can cascade from European-level decisions to national economies, this premium becomes particularly relevant. For example, legislative issues in Brussels or a shift in the European Parliament's ideological majority could delay or alter regulatory frameworks affecting multiple sectors across member states. The same logic can be applied to the different Parliaments of the EU countries. Although many studies have focused on the U.S. or broad international samples, the mechanisms they highlight (uncertainty, political connections, and risk pricing) are interesting also within the European context.

2.1.2 Stock Market Volatility and Elections

A study by Bialkowski, Gottschalk, and Wisniewski (2008) revealed that stock market volatility rises significantly in the days surrounding national elections. Their analysis demonstrated that volatility increased during an event window centered around election dates. While their focus was global, their findings are particularly pertinent for the USA, where shifts of power can be significantly important. Furthermore, their study can be an interesting start of thought for the analysis regarding the EU elections impact, since important shifts can occur in economic direction, such as changes in EU-wide regulation, monetary coordination, or fiscal policy alignment. These findings are especially relevant to countries such as France, Germany and Italy whose political shifts often ripple through broader European financial markets due to their economic weight within the EU.

In a complementary analysis, Lobo, B. J. (1999) examined how market participants react to external political shocks, finding that political uncertainty correlates positively with stock market volatility. Investors, in anticipation of potential regulatory or macroeconomic upheaval, become more risk-averse and demand greater compensation for holding risky assets. This insight is highly relevant to the EU setting, where political fragmentation or extreme parties gains during elections may provoke uncertainty about policy continuity and institutional stability, factors that are quickly priced into market movements.

Although much of the existing literature centers on the U.S. political environment, comparative insights remain valuable. For example, Santa-Clara and Valkanov (2003) found that stock market returns in the U.S. varied systematically depending on which political party held the presidency, with higher average returns during Republican administrations. While such partisan dynamics are less straightforward in Europe due to multiparty systems and coalition governance (historically depending on the EU country studied), the underlying premise (that investor expectations and market behavior adjust in response to political orientation), remains applicable.

Additional research by Bechtel and Füss (2008) strengthens the link between political risk and market volatility in Europe. They find that markets respond more strongly to elections where the expected policy outcome is uncertain, where the government is divided and where institutional constraints are weak. This finding suggests that volatility is not only driven by elections by itself, but by the degree of unpredictability regarding post-election policy implementation.

2.1.3 Studies on National Elections in Europe and Financial Markets

While much of the foundational literature on political events and stock markets has traditionally centered on presidential systems across the world, a growing body of research has turned its attention to elections in Europe. These national legislative contests, though distinct across countries in terms of institutional design and electoral rules, are increasingly recognized as influential moments for financial markets due to the policy uncertainty they generate. Given the integrated nature of the European economy and the interdependence of its capital markets, elections in major EU member states can have significant effects, influencing domestic assets and broader European stock indices.

In terms of market response to political orientation, Belke and Potrafke (2012) investigated how changes in government ideology, particularly shifts between left and right coalitions, influence monetary policy in OECD countries and therefore, investor expectations and market returns. Their findings suggest that the election of market-friendly or fiscally conservative parties tends to produce positive stock market reactions, especially in export-driven economies. Conversely, increased electoral support for populist or anti-establishment parties tends to increase volatility and decrease investor confidence, as such outcomes often bring with them uncertainty over fiscal discipline, EU cooperation, or regulatory policies.

Additional insights are provided by Goodell, McGee, and McGroarty (2020), who employed prediction market data to assess the interplay between election uncertainty and financial market expectations. Their findings underline that financial markets respond to electoral outcomes and to shifts in the perceived probabilities of those outcomes, which evolve dynamically during campaign periods and media coverage. This highlights the forward-looking nature of markets and the role of political expectations, even before actual votes are cast.

2.1.4 Heterogeneity in Market Reactions to European and U.S. National Elections

One of the key insights emerging from the literature is that financial market responses to political events are not uniform across various countries. While some mechanisms, such as policy uncertainty and investor risk aversion, are common, their effects are mediated by national institutional contexts, electoral systems, and the structure of government. This heterogeneity supports the logic for a comparative analysis of European countries, as undertaken in this thesis.

There are notable differences between European and American political systems, which help explain the varying magnitude and direction of market reactions. In the United States, where the presidential system concentrates power and party alternation tends to result in abrupt policy shifts, markets often respond more dramatically to electoral outcomes. In contrast, many European countries employ proportional representation systems, leading to coalition governments that moderate political swings and slow down legislative change.

For example, Döpke and Pierdzioch (2006) analyzed the relationship between political orientation and stock market performance in Germany. They found no evidence supporting the idea that market returns are different depending on the political orientation of the administration, a finding that stands in contrast to U.S. patterns. These findings will be compared to those of this thesis and the effect could be attributed to Germany's political structure. The institutional features reduce the probability of drastic policy changes, thereby softening the market's response to electoral outcomes.

Looking at the United States and the United Kingdom, Mukherjee and Leblang (2007) examined stock market behavior around general elections and found that volatility tends to rise when right-wing parties (Conservatives) are expected to win, reflecting heightened uncertainty about fiscal and regulatory policy. Interestingly, their analysis also shows that volatility often remains after the party takes office, indicating a market adjustment once policy direction becomes clearer. This underscores the distinction between pre-electoral uncertainty and post-electoral clarity and reinforces the idea that market volatility is most pronounced during the anticipation phase of political change.

2.2 Different Political Models in Europe

2.2.1 Political Systems and Electoral Models in Europe: The Cases of France and Germany

To understand the heterogeneous impact of legislative elections on financial markets in Europe, it is essential to first examine the institutional and electoral frameworks of major European economies. The structure of political regimes, the process of government formation, and the role of key political offices vary significantly from one country to another, influencing both the degree of policy uncertainty during elections and the responsiveness of financial markets. This section focuses on two core economies of the Eurozone: France and Germany, which embody distinct political traditions and institutional architectures.

France operates under a semi-presidential system established by the 1958 Constitution of the Fifth Republic. The country is characterized by a dual executive, composed of a President of the Republic, elected by direct universal suffrage for a five-year term, and a Prime Minister, appointed by the President but typically drawn from the majority party or group in the National Assembly. We can note that France has not historically used the coalition framework.

The legislative branch, the “Assemblée nationale”, is composed of deputies elected via a two-round majority voting system, which tends to produce single-party or stable majorities. As a result, when the president's party wins a legislative majority, the executive wields considerable power and policy implementation tends to be swift and coherent. Conversely, when opposing parties control the presidency and the legislature, cohabitation occurs, creating a duality of power that can increase political uncertainty.

Germany, in contrast, is a parliamentary democracy with a federal structure. The executive power is vested in the Federal Chancellor (Bundeskanzler), who is elected by the “Bundestag” (Federal Parliament) following legislative elections. The President of the Republic, elected by a federal convention, has in fact less executive power than in France and holds a largely ceremonial role. The electoral system is mixed-member proportional representation system, which combines direct constituency elections with proportional party lists.

Due to this system, it is rare for a single party to obtain an absolute majority. As a result, coalition governments are the norm, and coalition negotiations are required to form a government after elections. This negotiated power-sharing arrangement introduces an extended period of political uncertainty after elections but also tends to dilute the impact of extreme policy shifts, creating an environment of institutional continuity that markets can interpret as stable and predictable.

Moreover, the “Bundesrat”, Germany’s upper house, which represents the “Länder” (states), must approve significant legislation, further moderating policymaking. The necessity for cooperation across federal levels and between coalition partners leads to gradualist reforms rather than abrupt policy reversals.

2.3 Variables in the Empirical Analysis

Throughout this thesis, several variables will be used in the analysis to assess the impact of politics on the return of European indices. The pertinence of these variables is discussed below, and their computation is further explained in the Methodology section.

2.3.1 « Election months » variable

The inclusion of a time-sensitive political variable such as “Election Months” is central to the empirical investigation of how political uncertainty influences financial markets. This variable captures the temporal proximity to national legislative elections, including the election month itself and the months immediately preceding and following, which are considered as periods of heightened market sensitivity. The logic for this construction is rooted in both theoretical and empirical findings that suggest investors begin adjusting their expectations on election day, but also often weeks or months before, as polls, debates, and policy signals shape the anticipated direction of government.

Market reactions are not confined to the election day itself. Herold, Kanz and Muck (2021) highlight that pre-election periods in the 2016 US presidential election exhibit heightened volatility and abnormal returns as investors react to polls and campaign developments, some findings that can be applied to the European context. Similarly, Goodell, McGee, and McGroarty (2020), using prediction market data, show that expectations about possible outcomes fluctuate significantly in the months preceding elections, impacting market behavior in real time. These findings support the decision to include the election month and the surrounding months as critical windows of political influence.

For example, Bernhard and Leblang (2006) and Mukherjee (2008) argue that investors anticipate policy shifts and reallocate assets in the run-up to elections. Their analysis of exchange rate and bond market data across developed democracies reveals anticipatory patterns driven by electoral dynamics. Jayachandran (2006) finds that campaign announcements and expected outcomes influence the stock prices of politically sensitive firms even before any official result is declared. Moreover, Bialkowski and al. (2008) found that stock market volatility was systematically elevated on election day, and on the weeks around the election day.

Post-election months are also critical. Santa-Clara and Valkanov (2003) found that stock returns are systematically affected by the partisan composition of the incoming government, with markets reacting to the anticipated policy trajectory of the new administration. However, this adjustment process often takes time, especially in Europe, where new governments may only be formed weeks after the election. Policy uncertainty may remain elevated even after elections, particularly when new political actors enter office or when coalition governments are unstable.

2.3.2 « Return MSCI EU » variable

In empirical finance, macro-level stock indices are frequently used to control for regional or global market influences that might otherwise confound the estimated effect of country-specific events, such as national elections. In the context of this thesis, the inclusion of the MSCI Europe Index return as a control variable is essential to isolate effects from broader European market movements.

The MSCI Europe Index, created and maintained by MSCI Inc., is a free-float-adjusted market capitalization weighted index that tracks large and mid-cap stocks across 15 developed European countries. It includes over 400 European companies from countries such as France, Germany and Italy. The index represents approximately 85% of the free float-adjusted market capitalization in each country (MSCI, 2025).

Because it aggregates firms from various sectors and regions across Europe, the MSCI Europe Index serves as a proxy for overall European market sentiment and performance. In this way, it captures macroeconomic shocks, pan-European investor sentiment, monetary policy decisions from the European Central Bank, and systemic risk, which may affect all national markets simultaneously.

In studies that aim to isolate event-specific or policy-specific effects, such as elections, it is standard econometric practice to include a broad market return variable to account for systematic factors unrelated to the event in question. As emphasized by Fama (1970) in his foundational work on market efficiency, asset returns are influenced by both firm-specific (or event-specific) information and systematic factors. Controlling for the latter is essential to avoid biased or inflated estimates of the effect of interest.

Several studies have implemented this approach using global or regional indices such as the MSCI World, MSCI Emerging Markets, or MSCI Europe. For example, Hoe and Nippani (2017) include the MSCI World return as a control in their study of political connections and stock performance in their study on U.S. elections and stock markets in China. Similarly, Brogaard and Detzel (2015) use global equity indices to account for time-varying risk premia and economic uncertainty. These findings show that using an index for broader European market dynamics improves the accuracy and explanatory power of models estimating the effect of political uncertainty, within the European context.

Although global indices like the MSCI World or the S&P 500 are commonly used in international finance, the choice of the MSCI Europe Index is more targeted and appropriate in the context of this thesis. The MSCI Europe reflects only developed European markets, which are subject to similar macroeconomic environments, regulatory frameworks, and monetary policies. This improves the comparability with national indices like the CAC 40 or DAX, which are heavily influenced by European Central Bank decisions, EU-wide economic policy, and regional investor sentiment. Furthermore, global indices like the MSCI World are heavily weighted toward U.S. stocks, which can introduce external noise unrelated to the European political context. By using the MSCI Europe index, the model filters out non-European drivers and concentrates on specific and pertinent factors.

2.3.3 « GDP Growth » variable

GDP growth is a fundamental macroeconomic indicator that reflects a country's overall economic health and is directly tied to corporate earnings expectations and investor sentiment. Since stock indices as the CAC 40 and DAX represent large domestic firms, their performance is closely linked to national growth trends (Chen, Roll, & Ross, 1986). Including GDP growth in the model helps distinguish the impact of elections from broader economic conditions. Markets may rise during election months not because of political factors, but due to strong underlying economic performance.

In political finance, GDP growth also influences investor expectations about election outcomes. When the economy performs well, markets may anticipate political continuity and policy stability, decreasing volatility (Lewis-Beck and Stegmaier, 2000). Conversely, weak GDP growth can signal higher electoral risk and increase uncertainty premiums.

2.3.4 « Inflation Rate » variable

Similarly to the GDP Growth, inflation is a critical macroeconomic indicator that directly affects investor behavior, asset pricing, and monetary policy expectations. In financial markets, rising inflation is often associated with higher interest rate expectations, reduced real returns, and increased market volatility. As such, including the inflation rate as a control variable in the model is coherent to distinguish political shocks from macroeconomic pressures. This makes it an important variable, markets may react to the election itself, but also to the inflation context in which it occurs.

2.3.5 « Global Economic Policy Uncertainty » variable

The Global Economic Policy Uncertainty (EPU) Index, developed by Baker, Bloom, and Davis (2016), measures the level of uncertainty regarding global economic policy based on newspaper coverage frequency, tax code expirations, and economic forecasts. This variable captures broad, time-varying uncertainty that can influence financial markets across countries, regardless of domestic political cycles.

Using the Global EPU Index in the model serves to control for exogenous, uncertainty that could affect national stock indices like the CAC 40 and DAX. During periods of elevated global policy uncertainty, such as geopolitical tensions, international trade conflicts, or global health crises, investor sentiment tends to become more cautious, often resulting in declines in risk appetite and increased volatility, even in the absence of political events.

As emphasized by Baker, Bloom, and Davis (2016), economic policy uncertainty leads to greater market volatility, reduced investment, and lower employment growth. Including this index helps avoid attributing these global effects to national elections. Recent extensions of the EPU framework show that spillover effects from the U.S. or China, for example, can significantly affect European financial markets.

Furthermore, studies such as Brogaard and Detzel (2015) find that elevated policy uncertainty is associated with higher equity risk premia and lower asset valuations, especially in open, globally integrated economies, typical of the Eurozone.

2.3.6 « European News-Based Index » variable

The European News-Based Economic Policy Uncertainty (EPU) Index provides a measure of economic policy-related uncertainty specific to the European context, constructed using the frequency of terms related to “economy”, “uncertainty”, and “policy” in leading European newspapers. This indicator is part of the broader EPU framework developed by Baker, Bloom, and Davis (2016), and is publicly available via the Economic Policy Uncertainty portal.

Incorporating this index in the model allows the control for Europe-specific uncertainty, as opposed to global factors captured by the Global EPU. While elections are country-level events, cross-border spillovers, such as EU fiscal negotiations, ECB decisions, or common regulatory changes, often generate continent-wide uncertainty that can affect national markets like France (CAC 40) and Germany (DAX). The European EPU Index aggregates uncertainty signals from press outlets in countries such as Germany, France and Italy using a methodology aligned with the original U.S. index (Baker, Bloom, and Davis (2016). Furthermore, the index has specific variations allowing to focus on the particular cases of France and Germany.

2.3.7 Interaction variables

In empirical research on political uncertainty and financial markets, interaction terms are often used to explore how the effect of an explanatory variable varies under specific conditions, such as during election periods. In the context of this thesis, interaction variables constructed by combining “Election Months” with macroeconomic or financial indicators (inflation x election, GDP growth x election, etc.) allow for the identification of conditional effects, whether these variables influence market behavior differently during politically sensitive periods.

From a theoretical standpoint, elections often act as shock amplifiers, altering the way markets interpret traditional macroeconomic signals. For instance, an inflation spike might have a stronger negative impact on investor sentiment during election periods, when policy responses are uncertain or politically constrained. Interaction terms allow the model to explicitly test these conditional relationships (Brambor, Clark and Golder, 2006). This modeling strategy aligns with the logic of contextual moderation, where the main effect of a variable (for example, inflation) is hypothesized to vary depending on political context (for example, election month). As such, it avoids misleading conclusions based on average effects and captures the election-specific sensitivities of financial markets. Interaction terms have been used in the political economy of markets such as the study of Julio and Yook (2012), which shows that corporate investment drops more significantly when economic uncertainty coincides with volatile policy environments. Similarly, Goodell and Vähämaa (2013) examine how U.S. elections interact with volatility indices to measure the election-specific responsiveness of investor sentiment.

Including interaction terms improves the econometric precision and interpretability of the model. It enables the detection of conditional heterogeneity, whether variables like GDP growth or inflation, for example, only significantly affect stock returns under electoral uncertainty. Moreover, interaction terms are essential to test specific hypotheses, such as: “Does inflation increase volatility only during election months?” or “Is the impact of regional uncertainty stronger in politically sensitive periods?” Without these terms, such effects would remain hidden or diluted in average estimates.

These interaction terms allow for the modeling of conditional effects, enhancing the explanatory power of the regression and revealing dynamics that are only relevant during electoral periods. Their use is consistent with best practices in political finance and econometrics.

2.4 Gap in the Literature

While studies have examined the relationship between political events and financial markets, much of this literature has concentrated on elections in the United States (Santa-Clara & Valkanov, 2003 and Pastor & Veronesi, 2013), often using major indices like the S&P 500 as benchmarks. In contrast, studies on the impact of national legislative elections in Europe remain relatively limited, particularly when it comes to multi-country analyses and legislative elections, adopting a comparative approach.

This thesis addresses a gap by investigating the effects of legislative elections in European countries on the returns of major national stock indices over a period spanning from August 2004 to January 2025. By adopting a time frame that extends to the very recent past, the study captures a wide range of political contexts which are underexplored in existing election-related financial literature.

Beyond the temporal and geographical scope, this thesis offers several methodological choices. First, it introduces a dedicated "Election Months" variable, whose valuation will be further discussed in the following sections, allowing a clear distinction between electoral and non-electoral periods. This variable is studied in isolation and used to build interaction terms with other key variables, such as the "Election and European News-Based Economic Policy Uncertainty" and the "Election and Inflation rate", to test whether the influence of uncertainty or macroeconomic factors is intensified during election periods.

Moreover, most previous research tends to focus on global indices (MSCI World) or U.S. centered indices (S&P 500), while studies focusing specifically on key European indices such as the CAC 40 and DAX remain rare. This thesis helps fill that gap by providing detailed insights into how these major European markets respond to national political events.

The study tests clearly formulated hypotheses, grounded in theory and literature, which are empirically evaluated using an econometric model. This combination of specificity, scope, and methodological robustness positions the thesis as a contribution to the intersection between political economy and empirical finance in the European context.

3 Methodology

3.1 Introduction

This section outlines the methodology employed in the empirical analysis of this thesis. The primary objective of the research is to provide insights into the following question: “What is the impact of political elections in Europe on European financial markets, represented by the main European stock indices?” To address this question, the thesis formulates a set of hypotheses grounded in a relevant theoretical framework. The empirical analysis is designed to test these hypotheses using carefully selected and justified data. The methodological approach adopted to conduct this analysis is detailed in the following sections.

3.2 Research Design

The empirical analysis of this thesis is conducted through a multiple linear regression model estimated using the Ordinary Least Squares (OLS) method. This approach is commonly employed in financial and economic research due to its feasibility, interpretability, and effectiveness in estimating relationships between variables. The main objective is to identify which independent variables has a statistically significant influence on the variation of the dependent variable.

The independent variables selected for this analysis include macroeconomic indicators (such as inflation rates), financial variables (such as market indices), political variables (such as the occurrence of national elections), and interaction terms that capture the combined effects of these factors. These variables will be described in detail in a subsequent section of the methodology.

The dependent variables are the monthly returns of major national stock indices, such as the CAC 40 (France) and the DAX (Germany), which are used as proxies for the performance of European financial markets.

The analysis covers the period from August 2004 to January 2025. The use of a monthly frequency (one observation per month) allows for a balance between data availability and the ability to capture medium-term market reactions. Monthly data are also less prone to noise and volatility than daily data, making them particularly suitable for capturing the effects of political events such as elections.

All statistical analyses, including the regression estimations and preliminary diagnostic tests such as multicollinearity (through Variance Inflation Factor tests) and stationarity (using Augmented Dickey-Fuller tests), are conducted using the R programming language via R Studio, a widely used open-source environment for statistical computing.

3.3 Data collection

For the purposes of this study, all data were collected from academically recognized sources, as well as official reputable sources.

Financial data related to the indices under analysis, namely the CAC 40, DAX, and MSCI Europe, were retrieved primarily from the official Capital IQ platform, accessed through the institutional license provided by the University of Liège. Complementary data were also obtained from Investing.com, a widely recognized open-access financial data platform. The specific financial metric used is the monthly return based on the "Adjusted Close" price of each index.

Macroeconomic variables, including GDP growth and inflation rates, were sourced from a variety of reliable databases. These include Statista (accessed through the University of Liège), the official statistical websites of the countries under study, and the World Bank Data portal, which offers consistent and internationally comparable macroeconomic indicators.

Political data, which are central to constructing variables such as "Election Months", "Right Wing Wins", "Left Wing Wins", and "Center Wins", were gathered from the official governmental websites of the respective countries. Additional political event data were obtained from the Election Guide website, an internationally recognized source of election information compiled by the International Foundation for Electoral Systems (IFES).

3.4 Data analysis

3.4.1 Multiple Linear Regression (MLR)

As previously mentioned, the empirical analysis is based on a multiple linear regression model using the Ordinary Least Squares (OLS) method, implemented through the R programming environment via R Studio. This statistical technique is widely used in financial and econometric research due to its ability to estimate the relationship between a dependent variable and multiple independent variables in a clear and interpretable manner.

The OLS regression allows for the identification of significant determinants of stock market returns, including macroeconomic, financial, and political variables. The model is applied individually to each country's main stock index to capture country-specific effects of electoral events on financial markets.

Prior to the regression analysis, preliminary integration tests are performed to ensure the validity of the model assumptions. These include multicollinearity tests, such as the Variance Inflation Factor (VIF), to detect potential redundancies among independent variables and stationarity tests, such as the Augmented Dickey-Fuller (ADF) test, to ensure that the time series data used in the regressions are stable over time and suitable for analysis. The results of the tests are shown in the Appendices section.

3.4.2 MLR in the context of the thesis

MLR allows for the estimation of the marginal effect of each explanatory variable (elections, inflation, GDP growth, policy uncertainty, etc.) on the dependent variable (stock index return). From a methodological standpoint, MLR is particularly suitable when the goal is to isolate the individual contribution of multiple factors to an outcome that is influenced by a complex economic and political environment. This is essential in a setting such as financial markets, where returns are rarely driven by a single cause but instead by a confluence of macroeconomic indicators, institutional variables, and political events. This modeling strategy also aligns with existing literature in political economy and empirical asset pricing. For example, Bialkowski and al. (2008) rely on regression-based frameworks to quantify the influence of political or economic shocks on market returns.

3.4.3 Used Variables

For clarity and conciseness, abbreviations and simplified names are employed for the variables throughout the analysis. This section provides a detailed overview of all variables used in the empirical model, including their definitions and the methods used for their calculation or valuation.

3.4.3.1 Dependent variables:

The "Return CAC 40" and the "Return DAX" variables ($R_{CAC40,t}$ and $R_{DAX,t}$ in the formulas) represent the monthly return, based on the "Adjusted Close" price, of the CAC 40 and DAX index. The CAC 40 serves as a key benchmark for the French equity market. Similarly, the DAX serves as the primary benchmark for the German equity market.

3.4.3.2 Independent variables:

The "Election Months" variable ($Election_t$ in the formulas) captures the temporal proximity of political elections. It is constructed as follows: a value of 3 is assigned to the month in which a national election takes place; a value of 2 is assigned to the month immediately preceding and following the election (one month before and after); a value of 1 is assigned to the second month before and after the election; and a value of 0 otherwise. After multiple tests, allowing more value to months closer to the election turns out to be the most efficient manner to assess the election effect on financial returns.

The "Return MSCI EU" variable ($MSCI_t$ in the formulas) represents the monthly return, based on the "Adjusted Close" price, of the MSCI Europe Index. The index includes approximately 400 large and mid-cap companies across 15 developed European markets, covering around 85% of the total market capitalization in the included countries. It serves as a broad benchmark for the performance of European equities.

The "GDP Growth" variable (GDP_t in the formulas) represents the annual GDP growth rate of the country under study, assigned to each corresponding month to align with the monthly frequency of the dataset. Although GDP growth is typically reported on an annual basis, it is incorporated here as a constant monthly value for each year to maintain consistency across the panel.

The "VAR Inflation Rate" variable ($Infl_t$ in the formulas) measures the annual change in the inflation rate for the country under study. Although the underlying inflation data are annual, the variation is applied uniformly across all months of the corresponding year to maintain consistency with the monthly structure of the dataset.

The "VAR Global Economic Policy Uncertainty" variable ($Uncert_t$ in the formulas) captures the monthly variation in the Global Economic Policy Uncertainty (GEPU) Index, developed by Baker, Bloom, and Davis (2016). The GEPU Index measures uncertainty related to economic policy on a global scale and is constructed from a weighted average of national EPU indices based on the GDP levels of participating countries. The monthly variation allows for the analysis of short-term shifts in global policy-related uncertainty and their potential impact on financial markets.

The "VAR European News-Based Index (France)" and "VAR European News-Based Index (Germany)" variables ($NewsFR_t$ and $NewsGER_t$ in the formulas) represent the monthly variation in the European News-Based Economic Policy Uncertainty Index specific to France and Germany, respectively, developed by Baker, Bloom, and Davis (2016). The index quantifies economic policy uncertainty based on the frequency of related terms in leading national newspapers. Monthly changes in this index are used to capture fluctuations in policy-related uncertainty within the media landscape and assess their influence on financial market dynamics.

Interaction Variables

The "Election and MSCI EU" variable is an interaction variable constructed by multiplying the "Election Months" variable with the "Return MSCI EU" variable. To ensure consistency and interpretability of results, "Election Months" is transformed into a binary variable for the purposes of this interaction: it takes the value 1 if its original value is greater than 0 and 0 otherwise. This interaction term is designed to capture the differential effect of European market movements on national indices during politically sensitive periods.

The "Election and GDP Growth" and "Election and Inflation rate" interaction variables are computed similarly. The "Election and Uncertainty" and "Election and European News-Based" interaction variables are computed using respectively the "VAR Global Economic Policy Uncertainty" and "VAR European News-Based Index" variables.

Political Orientation variables

The "Left wing wins", "Center wins" and "Right wing wins" binary variables ($Left_t$, $Center_t$ and $Right_t$ in the formulas) take the value 1 if the political party that came to power (specifically, the party of the elected Prime Minister in the country under study) is classified as left-wing, centrist or right-wing, respectively. The value of 1 is assigned for the twelve months following the election in which the party took power; it is 0 otherwise. This variable is intended to capture the medium-term market response to the political orientation of the governing party.

3.4.3.3 Further use of the variables

The variables described above constitute the core of the empirical framework employed in this thesis. Special attention has been given to the construction and transformation of variables to ensure consistency in temporal alignment and interpretability of results. The combination of these variables enables a nuanced analysis of the effects of electoral events on national stock indices. In the following sections, these variables will be used to estimate multiple regression models, to test the validity of the research hypotheses, which are detailed hereafter, and draw empirically grounded conclusions.

3.5 Hypotheses

3.5.1 Election Months Hypotheses

Elections are periods of heightened political uncertainty, which directly influences investor behavior, leading to volatility, risk repricing, and shifts in equity valuations (Pastor & Veronesi, 2013). The variable "Election Months" captures this period of uncertainty by flagging the month of a national election and its surrounding months, when policy expectations are actively formed or revised by market participants.

Given that the timing of elections is known beforehand, and that political risk materializes gradually through campaigns, polling dynamics, and negotiations, using an election-focused variable like "Election Months" allows the model to capture deviations in return behavior attributable to electoral events. This is consistent with the findings of Brogaard and Detzel (2015), who link policy uncertainty to lower asset valuations and higher risk premia. Consequently, the hypotheses, which will be tested for both France and Germany, are the following:

H0 (Null Hypothesis): The Election Months variable does not impact the return of the European Indices

H1 (Alternative Hypothesis): The Election months variable has an impact on the return of the European Indices

3.5.2 Interactions Hypotheses: Election Months and Economic and Political Uncertainty (EPU)

This hypothesis tests whether the effect of political uncertainty on stock returns is amplified during election periods, using an interaction term between the "Election Months" variable and an index of political uncertainty, such as the Economic Policy Uncertainty Index (EPU). This approach is supported by both theoretical and empirical literature in political economy and financial markets.

The Economic Policy Uncertainty (EPU) Index, developed by Baker, Bloom, and Davis (2016), is a widely used measure of policy-related uncertainty. It captures investors and policymakers' perceptions of ambiguity surrounding future economic direction. European versions of the index are available for major economies, providing a quantifiable measure of political uncertainty.

By using an interaction term between Election Months and EPU, the model allows for a conditional effect, testing whether the influence of political uncertainty on stock returns intensifies during elections. Consequently, the hypotheses, which will be tested for both France and Germany, are the following:

H0 (Null Hypothesis): Being on Election Months does not increase the impact of the Political uncertainty on the return of the European Indices

H1 (Alternative Hypothesis): Being on Election Months increases the impact of the Political uncertainty on the return of the European Indices

This hypothesis will be divided into two sub-sections: the Global Economic Policy Uncertainty and the European News-Based Political Uncertainty.

3.5.3 Interactions Hypotheses: Election Months and Macro-Economic variables

This hypothesis tests whether the influence of macroeconomic fundamentals, such as GDP growth and inflation, on stock returns is amplified during national election periods. The inclusion of interaction terms between “Election Months” and macroeconomic variables allows the model to capture whether investor sensitivity to economic signals changes under electoral uncertainty. From a theoretical perspective, election periods are marked by increased uncertainty over future policy direction, which can lead investors to overreact or respond more strongly to macroeconomic indicators.

By including interaction terms (such as Election Months x GDP Growth or Election Months x Inflation rate), the model allows for the possibility that the same macroeconomic indicator can have a different effect depending on the political context. This approach follows the methodological recommendations of Brambor, Clark, and Golder (2006), who argue that interaction terms are essential for testing hypotheses where the effect of one variable is conditional on the presence of another. Consequently, the hypotheses, which will be tested for both France and Germany, are the following:

H0 (Null Hypothesis): Being on Election Months does not increase the impact of the Macro-economic variables on the return of the European Indices

H1 (Alternative Hypothesis): Being on Election Months increase the impact of the Macro-economic variables on the return of the European Indices

This hypothesis will be divided into two sub-sections: the GDP Growth and the inflation rate.

3.5.4 Political Orientation Hypotheses

This hypothesis tests whether the ideological orientation of the ruling party (left-wing, center, or right-wing) following national legislative elections affects the performance of stock markets. The theoretical premise is that different political ideologies imply different policy priorities, especially in terms of fiscal policy, regulation, taxation, and labor market interventions, all of which can affect corporate earnings, investor expectations, and asset valuations.

Financial markets often adjust to election outcomes not only based on who wins, but on what that victory implies for future economic governance. As Santa-Clara and Valkanov (2003) show in the U.S. context, equity markets tend to perform differently under Republican versus Democratic administrations. Although Europe's multiparty parliamentary systems differ from the U.S. majoritarian model, similar mechanisms apply; markets react to the anticipated policies of the winning parti or coalition. Consequently, the hypotheses, which will be tested for both France and Germany, are the following:

H0 (Null Hypothesis): The political orientation of the parti that is in power after the election does not impact the return of the European Indices

H1 (Alternative Hypothesis): The political orientation of the parti that is in power after the election impacts the return of the European Indices

3.6 Formulas used for the Multiple Linear Regression (MLR)

3.6.1 General Model

France

$$R_{CAC40,t} = \beta_0 + \beta_1 \cdot Election_t + \beta_2 \cdot MSCI_t + \beta_3 \cdot GDP_t + \beta_4 \cdot Infl_t + \beta_5 \cdot Uncert_t + \beta_6 \cdot NewsFR_t + \beta_7 \cdot (Election_t \times MSCI_t) + \beta_8 \cdot (Election_t \times GDP_t) + \beta_9 \cdot (Election_t \times Infl_t) + \beta_{10} \cdot (Election_t \times Uncert_t) + \beta_{11} \cdot (Election_t \times NewsFR_t) + \varepsilon_t$$

Germany

$$R_{DAX,t} = \beta_0 + \beta_1 \cdot Election_t + \beta_2 \cdot MSCI_t + \beta_3 \cdot GDP_t + \beta_4 \cdot Infl_t + \beta_5 \cdot Uncert_t + \beta_6 \cdot NewsGER_t + \beta_7 \cdot (Election_t \times MSCI_t) + \beta_8 \cdot (Election_t \times GDP_t) + \beta_9 \cdot (Election_t \times Infl_t) + \beta_{10} \cdot (Election_t \times Uncert_t) + \beta_{11} \cdot (Election_t \times NewsGER_t) + \varepsilon_t$$

3.6.2 Specific Model

France

$$R_{CAC40,t} = \beta_0 + \beta_1 \cdot Election_t + \beta_2 \cdot MSCI_t + \beta_3 \cdot GDP_t + \beta_4 \cdot (Election_t \times GDP_t) + \beta_5 \cdot (Election_t \times Uncert_t) + \beta_6 \cdot (Election_t \times NewsFR_t) + \varepsilon_t$$

Germany

$$R_{DAX,t} = \beta_0 + \beta_1 \cdot MSCI_t + \varepsilon_t$$

3.6.3 General Model with Political Orientation

France

$$R_{CAC40,t} = \beta_0 + \beta_1 \cdot Election_t + \beta_2 \cdot MSCI_t + \beta_3 \cdot GDP_t + \beta_4 \cdot Infl_t + \beta_5 \cdot Uncert_t + \beta_6 \cdot NewsFR_t + \beta_7 \cdot (Election_t \times MSCI_t) + \beta_8 \cdot (Election_t \times GDP_t) + \beta_9 \cdot (Election_t \times Infl_t) + \beta_{10} \cdot (Election_t \times Uncert_t) + \beta_{11} \cdot (Election_t \times NewsFR_t) + \beta_{12} \cdot Left_t + \beta_{13} \cdot Center_t + \beta_{14} \cdot Right_t + \varepsilon_t$$

Germany

$$R_{DAX,t} = \beta_0 + \beta_1 \cdot Election_t + \beta_2 \cdot MSCI_t + \beta_3 \cdot GDP_t + \beta_4 \cdot Infl_t + \beta_5 \cdot Uncert_t + \beta_6 \cdot NewsGER_t + \beta_7 \cdot (Election_t \times MSCI_t) + \beta_8 \cdot (Election_t \times GDP_t) + \beta_9 \cdot (Election_t \times Infl_t) + \beta_{10} \cdot (Election_t \times Uncert_t) + \beta_{11} \cdot (Election_t \times NewsGER_t) + \beta_{12} \cdot Left_t + \beta_{13} \cdot Center_t + \beta_{14} \cdot Right_t + \varepsilon_t$$

3.6.4 Specific Model with political orientation

France

$$R_{CAC40,t} = \beta_0 + \beta_1 \cdot Election_t + \beta_2 \cdot MSCI_t + \beta_3 \cdot Infl_t + \beta_4 \cdot (Election_t \times GDP_t) + \beta_5 \cdot (Election_t \times Uncert_t) + \beta_6 \cdot (Election_t \times NewsFR_t) + \beta_7 \cdot Left_t + \varepsilon_t$$

Germany

$$R_{DAX,t} = \beta_0 + \beta_1 \cdot MSCI_t + \varepsilon_t$$

3.6.5 Model with the macro-economic and financial variables only

France

$$R_{CAC40,t} = \beta^0 + \beta_1 \cdot MSCI_t + \beta_2 \cdot GDP_t + \beta_3 \cdot Infl_t + \varepsilon_t$$

Germany

$$R_{DAX,t} = \beta_0 + \beta_1 \cdot MSCI_t + \beta_2 \cdot GDP_t + \beta_3 \cdot Infl_t + \varepsilon_t$$

3.6.6 Model with the political variables only

France

$$R_{CAC40,t} = \beta_0 + \beta_1 \cdot Election_t + \beta_2 \cdot Uncert_t + \beta_3 \cdot NewsFR_t + \beta_4 \cdot (Election_t \times Uncert_t) + \beta_5 \cdot (Election_t \times NewsFR_t) + \beta_6 \cdot Left_t + \beta_7 \cdot Center_t + \beta_8 \cdot Right_t + \varepsilon_t$$

Germany

$$R_{DAX,t} = \beta_0 + \beta_1 \cdot Election_t + \beta_2 \cdot Uncert_t + \beta_3 \cdot NewsGER_t + \beta_4 \cdot (Election_t \times Uncert_t) + \beta_5 \cdot (Election_t \times NewsGER_t) + \beta_6 \cdot Left_t + \beta_7 \cdot Center_t + \beta_8 \cdot Right_t + \varepsilon_t$$

4 Results

4.1 Introduction

This section presents the results obtained from the econometric analysis, which will be further interpreted in the next section (Discussion). The analysis is based on multiple linear regressions using the Ordinary Least Squares (OLS) method, conducted in R Studio. The results are structured around several regression models, each designed to isolate the effects of different sets of explanatory variables. These models are presented and described in detail in the following subsections. These models focus on France and Germany, with the returns of the CAC 40 and DAX respectively serving as the dependent variables and the selected economic and political factors as independent variables.

4.2 Results for France

4.2.1 General Model

Table 4.1: Results of the General Model (on R Studio)

	Estimate	Std. Error	P-value	
(Intercept)	0,000	0,001	0,991	
`Election months`	-0,005	0,003	0,104	
`Return MSCI EU`	1,058	0,022	0,000	***
`GDP growth`	0,036	0,037	0,325	
`VAR Inflation rate`	0,076	0,076	0,319	
`VAR Global Economic Policy Uncertainty`	0,001	0,006	0,876	
`VAR European News-Based Index (FRANCE)`	0,001	0,003	0,832	
`Election and MSCI EU`	0,036	0,077	0,638	
`Election and GDP Growth`	0,315	0,290	0,279	
`Election and Inflation rate`	0,177	0,173	0,308	
`Election and Uncertainty`	0,036	0,026	0,177	
`Election and European news-based`	-0,015	0,009	0,093	*

Adjusted R-squared = 92,25%

Source: The author's analysis

This model represents the general analysis, meaning it includes all the variables studied. The variable "Election months", as described in the methodology section, appears just above the 10% significance threshold. Although not strictly significant, we can note its proximity to the threshold. The variable "Return MSCI EU" is highly statistically significant, as denoted by three asterisks (***)[1] in the regression output. The variable "Election and European news-based" shows a p-value of 0,093, placing it within the 10% significance level. It is therefore considered weakly significant, and this is indicated by a single (*) in the output. The model achieves an Adjusted R-squared of 92,25%.

[1] Different levels of statistical significance: $p \leq 0,1$ (*) – $p \leq 0,05$ (**) – $p \leq 0,01$(***).

4.2.2 Specific Model

Table 4.2: Results of the Specific Model (on R Studio)

	Estimate	Std. Error	P-value	
(Intercept)	0,000	0,001	0,857	
`Election months`	-0,006	0,003	0,040	**
`Return MSCI EU`	1,054	0,020	0,000	***
`GDP growth`	0,055	0,032	0,092	*
`Election and GDP Growth`	0,470	0,267	0,079	*
`Election and Uncertainty`	0,036	0,026	0,161	
`Election and European news-based`	-0,016	0,008	0,048	**

Adjusted R-squared = 92,28%

Source: The author's analysis

This model represents the specific analysis, meaning it includes only a subset of the variables initially studied. These variables were selected based on statistical testing aimed at identifying the most relevant and significant model. The variable "Election months" is statistically significant at the 5% level, with a p-value of 0,040 (**), indicating a notable effect during election periods. The variable "Return MSCI EU" is highly statistically significant, with three asterisks (***) and a p-value of 0,000 returns. The macroeconomic variable "GDP Growth" shows a p-value of 0,092, making it significant at the 10% level (*), suggesting a weak but potentially meaningful influence on the index. The interaction term "Election and GDP Growth" also reaches the 10% significance level, with a p-value of 0,079 (*). Additionally, the variable "Election and European news-based" is statistically significant at the 5% level, with a p-value of 0,048 (**), indicating that periods of heightened European political news may influence market returns. The model achieves an Adjusted R-squared of 92,28%.

4.2.3 General Model including Left-wing, Center and Right-wing variables

Table 4.3: Results of the General Model including Left-wing, Center and Right-wing variables (on R Studio)

	Estimate	Std. Error	P-value	
(Intercept)	-0,001	0,001	0,552	
`Election months`	-0,006	0,003	0,027	**
`Left wing wins`	-0,007	0,004	0,069	*
`Center wins`	0,002	0,003	0,397	
`Right wing wins`	0,000	0,003	0,984	
`Return MSCI EU`	1,060	0,022	0,000	***
`GDP growth`	0,037	0,037	0,319	
`VAR Inflation rate`	0,081	0,076	0,284	
`VAR Global Economic Policy Uncertainty`	0,002	0,006	0,747	
`VAR European News-Based Index (FRANCE)`	0,000	0,003	0,927	
`Election and MSCI EU`	0,002	0,077	0,977	
`Election and GDP Growth`	0,523	0,280	0,063	*
`Election and Inflation rate`	0,183	0,224	0,415	
`Election and Uncertainty`	0,039	0,027	0,142	
`Election and European news-based`	-0,015	0,009	0,076	*

Adjusted R-squared = 92,27%

Source: The author's analysis

This model represents the general analysis with political orientation, meaning it includes all previously studied variables along with those related to the political orientation of the party that came to power following the elections. The variable "Election months", as described in the methodology, is statistically significant at the 5% level, with a p-value of 0,027 (**). The variable "Left-wing wins" is weakly significant, with a p-value of 0,069 (*). The variable "Return MSCI EU" is highly statistically significant, with a p-value of 0,000 and marked with three asterisks (***). The interaction variable "Election and GDP Growth" has a p-value of 0,063 and is considered weakly significant (*). Similarly, the variable "Election and European news-based" is weakly significant, with a p-value of 0,076 (*). The model achieves an Adjusted R-squared of 92,27%.

4.2.4 Specific Model including Left-wing, Center and Right-wing variables

Table 4.4: Results of the Specific Model including Left-wing, Center and Right-wing variables (on R Studio)

	Estimate	Std. Error	P-value	
(Intercept)	0,000	0,001	0,935	
`Election months`	-0,007	0,003	0,019	**
`Left wing wins`	-0,007	0,004	0,061	*
`Return MSCI EU`	1,061	0,020	0,000	***
`VAR Inflation rate`	0,143	0,061	0,019	**
`Election and GDP Growth`	0,539	0,274	0,051	*
`Election and Uncertainty`	0,041	0,026	0,107	
`Election and European news-based`	-0,015	0,008	0,053	*

Adjusted R-squared = 92,43%

Source: The author's analysis

This model represents the specific analysis with political orientation, meaning it includes a selected subset of the studied variables, including those related to the political orientation of the party elected to power. Variable selection was based on statistical testing aimed at identifying the most relevant and statistically significant model. The variable "Election months", as defined in the methodology, is statistically significant at the 5% level, with a p-value of 0,019 (**). The variable "Left-wing wins" is weakly significant, with a p-value of 0,061 (*). The variable "Return MSCI EU" is highly significant, with a p-value of 0,000 and marked with three asterisks (***). The macroeconomic variable "VAR Inflation rate" is significant at the 5% level, with a p-value of 0,019 (**). The interaction term "Election and GDP Growth" shows a p-value of 0,051, making it weakly significant (*). Finally, the variable "Election and European news-based" is also weakly significant, with a p-value of 0,053 (*). The model achieves an Adjusted R-squared of 92,43%.

4.2.5 Model using only macro-economic and financial variables

Table 4.5: Results of the Model using only macro-economic and financial variables (on R Studio)

	Estimate	Std. Error	P-value	
(Intercept)	0,000	0,001	0,896	
`Return MSCI EU`	1,061	0,020	0,000	***
`GDP growth`	0,025	0,036	0,488	
`VAR Inflation rate`	0,125	0,067	0,062	*

Adjusted R-squared = 92,26%

Source: The author's analysis

This model includes only macroeconomic variables (Inflation rate and GDP Growth) and the market variable "Return MSCI EU". The purpose of this model is to analyze the isolated impact of macroeconomic and market-related factors, excluding political influences. The variable "Return MSCI EU" is highly statistically significant, with a p-value of 0,000 and marked by three asterisks (***). The macroeconomic variable "VAR Inflation rate" is weakly significant, with a p-value of 0,062 (*). The model has an Adjusted R-squared of 92,26%.

4.2.6 Model using only political variables

Table 4.6: Results of the Model using only political variables (on R Studio)

	Estimate	Std. Error	P-value	
(Intercept)	0,007	0,003	0,045	**
`Election months`	-0,006	0,005	0,240	
`Left wing wins`	-0,013	0,013	0,333	
`Center wins`	0,006	0,010	0,504	
`Right wing wins`	-0,021	0,012	0,070	*
`VAR Global Economic Policy Uncertainty`	-0,073	0,019	0,000	***
`VAR European News-Based Index (FRANCE)`	0,009	0,011	0,447	
`Election and Uncertainty`	0,095	0,086	0,272	
`Election and European news-based`	-0,009	0,029	0,755	

Adjusted R-squared = 6,73%

Source: The author's analysis

This model includes only political variables, specifically those related to the political orientation of the party that came to power following elections. It does not include macroeconomic or market-related variables. The variable "Right-wing wins" is weakly significant, with a p-value of 0,070 (*). The variable "VAR Global Economic Policy Uncertainty" is highly statistically significant, with a p-value of 0,000 and marked with three asterisks (***). The model yields an Adjusted R-squared of 6,73%.

4.3 Results for Germany

4.3.1 General Model

Table 4.7: Results of the General Model (on R Studio)

	Estimate	Std. Error	P-value	
(Intercept)	0,004	0,001	0,007	**
`Election months`	-0,001	0,002	0,701	
`Return MSCI EU`	1,089	0,030	0,000	***
`GDP growth`	0,047	0,060	0,434	
`VAR Inflation rate`	-0,050	0,074	0,505	
`VAR Global Economic Policy Uncertainty`	0,005	0,008	0,534	
`VAR European News-Based Index (Germany)`	-0,005	0,004	0,215	
`Election and MSCI EU`	0,032	0,123	0,794	
`Election and Uncertainty`	0,003	0,034	0,925	
`Election and European news-based`	-0,003	0,011	0,797	

Adjusted R-squared = 86,85%

Source: The author's analysis

This model represents the general analysis, including all variables under study. The variable "Return MSCI EU" is highly statistically significant, with a p-value of 0,000 and marked with three asterisks (***), indicating a strong and positive relationship with the DAX returns. All other variables included in the model do not exhibit statistical significance, as their p-values exceed conventional thresholds. The model produces an Adjusted R-squared of 86,85%.

4.3.2 Specific Model

Table 4.8: Results of the Specific Model (on R Studio)

	Estimate	Std. Error	P-value	
(Intercept)	0,004	0,001	0,001	***
`Return MSCI EU`	1,095	0,027	0,000	***

Source: The author's analysis

This model represents the specific analysis, meaning it includes only a subset of the studied variables. The variables were selected based on statistical testing aimed at identifying the most relevant and significant model. The variable "Return MSCI EU" is highly statistically significant, with a p-value of 0,000 and denoted by three asterisks (***), indicating a strong and positive relationship with the DAX returns. The model achieves an Adjusted R-squared of 87,10%.

4.3.3 General Model including Left-wing, Center and Right-wing variables

Table 4.9: Results of the General Model including Left-wing, Center and Right-wing variables (on R Studio)

	Estimate	Std. Error	P-value	
(Intercept)	0,005	0,002	0,005	***
`Election months`	0,000	0,002	0,942	
`Left wing wins`	-0,002	0,007	0,761	
`Center wins`	-0,003	0,003	0,269	
`Return MSCI EU`	1,090	0,030	0,000	***
`GDP growth`	0,057	0,064	0,374	
`VAR Inflation rate`	-0,046	0,096	0,632	
`VAR Global Economic Policy Uncertainty`	0,005	0,008	0,520	
`VAR European News-Based Index (Germany)`	-0,005	0,004	0,205	
`Election and MSCI EU`	0,027	0,124	0,830	
`Election and Uncertainty`	0,001	0,034	0,981	
`Election and European news-based`	-0,002	0,011	0,876	

Adjusted R-squared = 86,81%

Source: The author's analysis

This model represents the general analysis including political orientation, meaning it includes all variables under study as well as those related to the political orientation of the party elected following elections. The variable "Return MSCI EU" is highly statistically significant, with a p-value of 0,000 and denoted by three asterisks (***). None of the other variables included in the model reach statistical significance. The model reports an Adjusted R-squared of 86,81%.

4.3.4 Specific Model including Left-wing, Center and Right-wing variables

Table 4.10: Results of the Specific Model including Left-wing, Center and Right-wing variables (on R Studio)

	Estimate	Std. Error	P-value	
(Intercept)	0,004	0,001	0,001	***
`Return MSCI EU`	1,095	0,027	0,000	***

Source: The author's analysis

This model represents the specific analysis including political orientation, meaning it includes a selected subset of the variables studied, including those related to the political orientation of the party that came to power following elections. The variables were chosen based on statistical testing to determine the most relevant and significant specification. This model gives the exact same results as the Specific Model.

4.3.5 Model using only macro-economic and financial variables

Table 4.11: Results of the Model using only macro-economic and financial variables (on R Studio)

	Estimate	Std. Error	P-value	
(Intercept)	0,004	0,001	0,009	***
`Return MSCI EU`	1,094	0,027	0,000	***
`GDP growth`	0,046	0,058	0,434	
`VAR Inflation rate`	-0,053	0,073	0,474	

Adjusted R-squared = 87,03%

Source: The author's analysis

This model includes only macroeconomic variables (Inflation rate and GDP Growth) as well as the market-related variable "Return MSCI EU". The objective of this model is to assess the isolated impact of macroeconomic and market-related factors, excluding political variables. The variable "Return MSCI EU" is highly statistically significant, with a p-value of 0,000 and denoted by three asterisks (***). The model yields an Adjusted R-squared of 87,03%.

4.3.6 Model using only political variables

Table 4.12: Results of the Model using only political variables (on R Studio)

	Estimate	Std. Error	P-value	
(Intercept)	0,012	0,004	0,002	***
`Election months`	0,006	0,006	0,291	
`Left wing wins`	-0,030	0,014	0,034	**
`Center wins`	-0,002	0,008	0,810	
`VAR Global Economic Policy Uncertainty`	-0,047	0,022	0,029	**
`VAR European News-Based Index (Germany)`	-0,019	0,010	0,063	*
`Election and Uncertainty`	0,078	0,090	0,387	
`Election and European news-based`	0,017	0,030	0,568	

Adjusted R-squared = 8,31%

Source: The author's analysis

This model includes only political variables, particularly those related to the political orientation of the party elected following national elections. Macroeconomic and market-related variables are excluded. The variable "Left-wing wins" is statistically significant at the 5% level, with a p-value of 0,034 (**), indicating a measurable effect on DAX returns when a left-wing party comes to power. The variable "VAR Global Economic Policy Uncertainty" is also statistically significant at the 5% level, with a p-value of 0,029 (**). The variable "VAR European News-Based Index (Germany)" is weakly significant, with a p-value of 0,063 (*). The model produces an Adjusted R-squared of 8,31%.

5 Discussion

5.1 Introduction

This section of the thesis addresses the hypotheses formulated in the Methodology chapter, using the empirical results presented in the Results section. Each hypothesis is examined considering the statistical evidence obtained through the regression analyses. The discussion is structured by country and by the type of variable studied, following the same framework established in the Methodology to ensure consistency and clarity.

5.2 Answering Hypotheses regarding France

The following sections will discuss the hypotheses regarding the CAC 40.

5.2.1 Election months

H0 (Null Hypothesis): The Election Months variable does not impact the return of the European Indices

H1 (Alternative Hypothesis): The Election months variable has an impact on the return of the European Indices

The empirical results from the multiple linear regression models provide significant support for the alternative hypothesis. In these models, the variable “Election months” is statistically significant at the 5% level (**) several times. These findings allow us to reject the null hypothesis and support the alternative hypothesis that election periods do have a significant effect on the returns of the CAC 40 index. This suggests that French financial markets are sensitive to the political cycle, especially during the months surrounding national elections.

This sensitivity can be explained by several structural and historical characteristics of the French political and institutional environment. France has a semi-presidential system where presidential and legislative elections can bring about significant policy shifts. The Fifth Republic, established in 1958, grants considerable power to the executive branch which means that elections can substantially alter the political and economic outlook.

French elections are highly mediatized and politically charged. Electoral debates often involve strong ideological contrasts, particularly between left-wing and right-wing parties. This polarization contributes to elevated political uncertainty, which has been shown to affect investor behavior and increase market volatility (Pastor & Veronesi, 2013). France's historical experience with alternating political regimes and instances of cohabitation (when the president and prime minister come from opposing political camps) adds another layer of uncertainty during elections, which could explain the heightened market reactions.

The statistical significance of the “Election months” variable reflects the importance of electoral cycles in shaping investor sentiment and market behavior in France. This supports the idea that political events, especially elections, are not neutral for financial markets, and must be considered when analyzing the dynamics of stock returns.

The regression results indicate that the variable Election Months has a negative estimate for the CAC 40, suggesting that stock returns tend to decrease during French legislative election periods. This implies that investors may respond cautiously to electoral uncertainty, likely anticipating shifts in economic policy following a change in government. Such periods may raise concerns about regulatory changes, fiscal adjustments, or redistribution policies that could adversely affect certain sectors. This is consistent with the literature on policy uncertainty, which finds that elections can lead to temporary declines in market performance due to increased perceived risk (Pastor & Veronesi, 2013).

5.2.2 Interactions Hypotheses: Election Months and Economic and Political Uncertainty (EPU)

H0 (Null Hypothesis): Being on Election Months does not increase the impact of the Political uncertainty on the return of the European Indices

H1 (Alternative Hypothesis): Being on Election Months increases the impact of the Political uncertainty on the return of the European Indices

The first sub-section of this hypothesis regards the variable assessing the variation in the Global Political Uncertainty Index, by Baker, Bloom, and Davis (2016).

This hypothesis is tested using multiple linear regression models. In all these models, the interaction term “Election Months and Uncertainty” fails to reach statistical significance. This variable was constructed by interacting the “Election Months” variable (capturing domestic political events) with the variation of the Global Political Uncertainty Index, which reflects fluctuations in global political instability, by Baker, Bloom, and Davis (2016).

Given the lack of significance, we fail to reject the null hypothesis, which states that being in an election month does not amplify the effect of Global political uncertainty on the returns of European indices, in this case, the CAC 40. This suggests that, during election months in France, the influence of global political uncertainty on French stock market performance does not intensify.

There are several plausible explanations for this finding. First, it is possible that the domestic electoral effects are already priced, and that their influence dominates any marginal amplification from global uncertainty. Elections in France are highly anticipated, scheduled events with significant media coverage and public discourse, which means that investors may already adjust their portfolios in advance, reducing the marginal effect of global uncertainty.

Secondly, and perhaps more compellingly, the Global Political Uncertainty Index may not be an adequate proxy for the kind of uncertainty that affects French markets during national elections. This index, by construction, captures broad global events, such as geopolitical tensions, U.S. elections, Brexit, or wars, and may not reflect country-specific factors such as French fiscal, labor, or regulatory uncertainty. In other words, the French financial market may be more sensitive to local political developments than to generalized global uncertainty.

The empirical results do not support the idea that global political uncertainty interacts with election periods to affect the CAC 40. This suggests that French stock market responses to political events are primarily driven by domestic political context, rather than an intensification of global uncertainty during national elections.

The second sub-section of this hypothesis regards the variable assessing the variation in the European News-Based Political Uncertainty by Baker, Bloom, and Davis (2016).

This alternative version of the hypothesis, tested with a different proxy for political uncertainty, finds empirical support in four regression models considered. In these models, the interaction term "Election Months and European News-Based Index" is statistically significant at the 5% level (**) and weakly significant at the 10% level (*). This interaction term captures the joint effect of election timing and the European News-Based Political Uncertainty Index (France), which reflects media-based measures of political instability specifically related to France and, more broadly, the European context.

The statistical significance of this variable allows us to reject the null hypothesis and accept the alternative: being in an election month increases the impact of domestic political uncertainty on French stock market returns.

This result is both intuitive and economically meaningful. Elections in France, particularly presidential and legislative elections, are major political events with the potential to reshape economic policy, regulatory frameworks, and fiscal priorities. During these periods, investors face a higher degree of uncertainty regarding the future political orientation of the government, which may influence market-sensitive sectors such as energy, defense, banking, or public infrastructure.

The European News-Based Political Uncertainty Index, by focusing on news coverage of political instability in France and Europe, offers a much more granular and country-relevant signal than global indices. It captures episodes of national political tension (strikes, reform debates, etc.) that are highly correlated with investor sentiment during politically sensitive periods. When such uncertainty coincides with the electoral calendar, the perceived risk by investors intensifies, leading to greater volatility or significant shifts in asset allocation (Kelly, Pástor & Veronesi, 2016).

This amplification effect can be interpreted as a "contextual sensitivity": the same political uncertainty signal has a stronger market impact when the institutional context is already volatile, such as during an election. In line with this, empirical literature suggests that political news has a stronger effect on financial markets when uncertainty is elevated, particularly in countries with centralized decision-making power like France (Julio & Yook, 2012).

The interaction between domestic political uncertainty and election periods appears to magnify the influence of politics on the CAC 40, underlining the importance of context-sensitive uncertainty indices when analyzing election-related effects on financial markets.

The estimate associated with the interaction term "Election Months and Economic and Political Uncertainty (EPU)" is negative, indicating that the combination of electoral periods and rising political uncertainty is associated with lower returns on the CAC 40. In other words, when elections occur amid heightened uncertainty, investor confidence appears to deteriorate, leading to downward pressure on stock prices. This can be attributed to anticipations of political transition, which may raise doubts about future fiscal or regulatory directions. These findings are in line with studies showing that the conjunction of policy uncertainty and political events amplifies market volatility and suppresses returns (Kelly, Pástor, & Veronesi, 2016).

5.2.3 Interactions Hypotheses: Election Months and Macro-Economic variables

H0 (Null Hypothesis): Being on Election Months does not increase the impact of the Macro-economic variables on the return of the European Indices

H1 (Alternative Hypothesis): Being on Election Months increases the impact of the Macro-economic variables on the return of the European Indices

The first sub-section of this hypothesis regards the variable assessing the GDP growth.

This hypothesis is explored through interaction terms in multiple linear regression models. Among the interaction variables, the term "Election Months and GDP Growth" emerges as marginally significant at the 10% level (*), indicating a weak but noteworthy relationship. This variable captures the interaction between monthly electoral periods and annual GDP growth in France, serving as a proxy for the domestic macroeconomic environment.

Based on these empirical results, we reject the null hypothesis and consider that there is some support for the alternative hypothesis: being in an election month increases the impact of GDP growth on the performance of the CAC 40.

This finding aligns with the idea that political cycles and macroeconomic expectations are interdependent, especially in countries like France, where electoral outcomes can lead to substantial shifts in economic policy. In times of elections, macroeconomic indicators such as GDP growth are likely to be scrutinized more closely by investors, as they are viewed both as reflections of current economic health and as benchmarks for campaign promises and future fiscal policy. Moreover, during electoral periods, GDP growth figures may carry additional signaling power. Political candidates and parties often frame their campaigns around economic performance, either highlighting it as a success or criticizing it as a failure, therefore elevating the occurrence of GDP data in public discourse and financial markets.

Another possible explanation is that elections may create expectations of economic intervention or reform, especially when GDP growth is either particularly strong or weak. In such cases, markets may anticipate that a newly elected government will enact fiscal stimulus, adjust taxation, or implement structural reforms, all of which are highly relevant for future earnings expectations and stock valuations.

The estimate for the interaction term "Election Months and GDP Growth" is positive, suggesting that higher GDP growth during electoral periods is associated with higher returns on the CAC 40. This indicates that in times of political transition, strong macroeconomic fundamentals, such as robust economic growth, may reinforce investor confidence. In such contexts, markets may interpret positive GDP figures as evidence of effective economic management by the incumbent government, thereby reducing perceived risk and boosting returns. This finding supports that strong economic performance can mitigate the uncertainty typically associated with elections, particularly when it signals political and policy stability.

The second sub-section of this hypothesis regards the variable assessing the variation in inflation rate, focusing on the interaction between election periods and inflation rate variations in France.

The interaction variable "Election Months and Inflation Rate" was tested across different models. In all specifications, this variable fails to achieve statistical significance. According to the information given by the result, we do not reject the null hypothesis: being in an election month does not increase the impact of changes in the inflation rate on the return of the CAC 40. This suggests that, unlike GDP growth, variations in inflation do not exert a stronger influence on financial markets during election periods in France.

Inflation in advanced economies like France is often influenced more by external global dynamics, such as commodity prices, energy shocks, and supply chain disruptions, than by immediate domestic political events. As such, market participants may not associate short-term inflation changes with electoral cycles, especially when monetary policy is delegated to an independent central bank, such as the European Central Bank (ECB).

France, as a Eurozone member, does not conduct national monetary policy, which substantially limits the direct influence of election outcomes on inflation expectations. Unlike countries with monetary sovereignty, where markets may expect inflationary fiscal policies post-election, France's inflation trajectory is primarily shaped by the ECB's euro-wide policy, insulating it from national political fluctuations (Olson and Wohar, 2016). Furthermore, from a market perspective, inflation data, especially when expressed as monthly or annual variation, is often seen as a "backward-looking" indicator, reflecting past conditions rather than immediate political risk. Investors may prioritize forward-looking indicators such as fiscal policy plans or macroeconomic forecasts when assessing election risk.

This result also underscores that not all macroeconomic variables interact equally with political cycles.

5.2.4 Political Orientation Hypotheses

H0 (Null Hypothesis): The political orientation of the parti that is in power after the election does not impact the return of the European Indices

H1 (Alternative Hypothesis): The political orientation of the parti that is in power after the election impacts the return of the European Indices

This hypothesis was tested using regression models that included variables reflecting the political orientation of the elected government, categorized as "Left wing wins", "Center wins", and "Right wing wins".

Across these models, some evidence of weak statistical significance emerges. The variable "Left wing wins" is weakly significant at the 10% level (*) in two out of three models, while "Right wing wins" also reaches the 10% threshold in one model. Center wins, however, is consistently insignificant. The adjusted R-squared of the political model remains relatively low at 6,73%, suggesting that the explanatory power of political orientation alone is limited, but non-negligible. Given this pattern, we can reject the null hypothesis and state that the results conclude that the political orientation of the ruling party impact the returns of the CAC 40.

Importantly, the estimated coefficients for both "Left wing wins" and "Right wing wins" are negative, indicating that the CAC 40 tends to exhibit lower returns following the election of either left or right-leaning governments, relative to a baseline (likely centrist or coalition governance).

This symmetric negative effect may reflect market aversion to ideologically driven policy agendas, whether from the left or the right. In the French context, left-wing governments are often associated with redistributive policies, higher public spending, and more stringent labor market regulations, all of which can create concerns among investors about corporate profitability and tax burdens. Conversely, right-wing governments may raise uncertainty about deregulation, social tensions, or austerity policies, particularly if they are perceived as politically polarizing or aggressive.

The markets may therefore interpret both outcomes, left or right, as increasing policy uncertainty, particularly when compared to more centrist or technocratic leadership. This aligns with the argument by Pastor and Veronesi (2013), who show that policy uncertainty increases when ideological shifts are expected, because such shifts introduce ambiguity about the future regulatory, fiscal, or institutional environment.

An alternative interpretation is that the act of deviating from political moderation, rather than the specific ideology, is what creates volatility. Investors may prefer continuity, coalition governance, or centrist stability, particularly in a country like France, where past transitions have sometimes been marked by sharp policy reversals or contentious reforms.

5.3 Answering Hypotheses regarding Germany

The following sections will discuss the hypotheses regarding the DAX.

5.3.1 Election months

H0 (Null Hypothesis): The Election Months variable does not impact the return of the European Indices

H1 (Alternative Hypothesis): The Election months variable has an impact on the return of the European Indices

This hypothesis was tested using multiple linear regression models. In all specifications, the variable "Election Months", which accounts for the proximity to election dates through a weighted intensity scale, fails to reach statistical significance. Based on this outcome, we do not reject the null hypothesis: the election months variable does not significantly affect the return of the DAX index.

This result can be interpreted considering Germany's unique political structure, which is known for its institutional stability and coalition-based governance. Unlike in countries with a majoritarian electoral system, German federal elections rarely result in a single party gaining an outright majority in the Bundestag. Consequently, coalition governments are the norm rather than the exception (Budge and McDonald, 2007). These coalitions typically require extensive negotiations and lead to consensual, moderate policymaking, which may reduce the perceived political risk for investors.

Furthermore, the German political system places a strong emphasis on continuity and institutional checks, which historically limit abrupt policy shifts, even when governments change (Manow, 2009). This likely explains why the markets do not react strongly to the electoral calendar: investors may not expect significant policy deviation, regardless of which party or coalition takes power.

The empirical findings in this case reflect that German elections do not represent a major source of uncertainty for investors and therefore do not have a statistically observable impact on the DAX. The electoral process does not appear to trigger returns during the months surrounding national elections.

5.3.2 Interactions Hypotheses: Election Months and Economic and Political Uncertainty (EPU)

H0 (Null Hypothesis): Being on Election Months does not increase the impact of the Political uncertainty on the return of the European Indices

H1 (Alternative Hypothesis): Being on Election Months increases the impact of the Political uncertainty on the return of the European Indices

The first sub-section of this hypothesis regards the variable assessing the variation in the Global Political Uncertainty Index, by Baker, Bloom, and Davis (2016).

This hypothesis was evaluated using multiple linear regression models. In all these specifications, the interaction term "Election Months and Global Political Uncertainty" does not attain statistical significance. This variable was constructed by interacting the weighted election calendar with the variations of the Global Political Uncertainty Index by Baker, Bloom, and Davis (2016), which captures variations in perceived political risk across the world.

Given the lack of statistical significance, we do not reject the null hypothesis: being in an election month does not amplify the effect of global political uncertainty on the return of the DAX index. This result may be interpreted through both methodological and structural lenses. First, the Global Political Uncertainty Index, while comprehensive, aggregates a wide range of geopolitical and national events, including U.S. policy decisions, Chinese regulatory shifts, conflicts, and large-scale economic shocks (Baker, Bloom, & Davis, 2016). As such, it may fail to capture the specific political risk that German markets respond to, especially during domestic electoral cycles. Second, the German political context plays a mediating role. As previously discussed, Germany is characterized by high institutional predictability and policy continuity, which makes the domestic impact of elections relatively muted (Manow, 2009). Even when global political uncertainty rises, investors may differentiate between international and local risk, particularly when elections in Germany are unlikely to produce sudden changes in economic direction.

Moreover, previous studies such as Brogaard and Detzel (2015) emphasize that political uncertainty is more likely to affect stock returns when it is specific and context relevant. This reinforces the idea that a global index may be too broad to meaningfully interact with domestic electoral timing in Germany. This contrasts with more sensitive contexts, where elections coincide with broader populist shifts, institutional instability, or highly polarized political competition, conditions less typical of modern German politics.

The second sub-section of this hypothesis regards the variable assessing the variation in the European News-Based Political Uncertainty by Baker, Bloom, and Davis (2016).

This hypothesis was tested using four multiple linear regression models. In all cases, the interaction term “Election Months and European News-Based Index (Germany)” failed to reach statistical significance. This variable captures the interaction between the electoral calendar and domestic media political uncertainty, centered specifically on German political developments.

Based on these findings, we do not reject the null hypothesis: being in an election month does not increase the impact of national political uncertainty on the return of the DAX. This result is consistent with Germany's broader political and institutional context. As previously discussed, the German political system is characterized by stability, coalition governance, and policy moderation. This makes the expected policy trajectory relatively stable, even following elections (Anderson, 2000).

The European News-Based Uncertainty Index (Germany) may not deliver sufficient new information to market participants during election months. If German investors already anticipate low volatility in policy direction due to predictable coalition outcomes, then even elevated domestic political uncertainty, when timed with elections, may have limited additional impact on market returns.

This finding reflects earlier literature showing that financial markets are less reactive to political uncertainty in countries with high institutional trust and policy stability (Bialkowski et al., 2008).

5.3.3 Interactions Hypotheses: Election Months and Macro-Economic variables

H0 (Null Hypothesis): Being on Election Months does not increase the impact of the Macro-economic variables on the return of the European Indices

H1 (Alternative Hypothesis): Being on Election Months increases the impact of the Macro-economic variables on the return of the European Indices

In the case of the DAX, this hypothesis could not be tested empirically due to high multicollinearity in the interaction variables. Specifically, the variables "Election Months and GDP Growth" and "Election Months and Inflation Rate" were removed from the regression models because their Variance Inflation Factor (VIF) values exceeded 10, commonly considered the threshold at which multicollinearity becomes problematic (Tsagris and Pandis, 2021). The different integration tests computed, such as the VIF, are in the Appendices section of the thesis.

Multicollinearity occurs when two or more explanatory variables in a regression model are highly correlated, making it difficult to isolate their individual effects. In this case, the interaction terms between election timing and macroeconomic indicators likely capture overlapping variance with either the base variables or with each other, leading to unstable coefficient estimates and inflated standard errors.

The decision to remove these variables is supported by methodological best practices. As noted in the econometric literature, a VIF value greater than 10 is often used as a rule of thumb for identifying multicollinearity that may bias regression results (Tsagris and Pandis, 2021). Including such variables could have compromised the reliability of the whole model, leading to misleading interpretations.

This limitation does not necessarily imply that no relationship exists between macroeconomic conditions and electoral timing in Germany. Future research could explore this relationship using alternative model specifications.

5.3.4 Political Orientation Hypotheses

H0 (Null Hypothesis): The political orientation of the parti that is in power after the election does not impact the return of the European Indices

H1 (Alternative Hypothesis): The political orientation of the parti that is in power after the election impacts the return of the European Indices

This hypothesis was tested using multiple regression models incorporating political orientation variables: the General Model with Left-Center-Right classification, the Specific Model with political alignment, and the model limited to political factors. The results indicate limited statistical significance overall regarding the hypothesis, except for the "Left wing wins" variable, which is statistically significant at the 5% level (**) in the model containing only political variables. The adjusted R-squared of this model is modest, at 8,31%, suggesting limited but non-negligible explanatory power.

"Center wins" and "Right wing" wins are consistently insignificant across all model specifications, implying that electoral outcomes involving centrist or conservative parties do not generate a significant market reaction. However, the significance and negative estimate of "Left wing wins" suggest that the DAX tends to perform worse when a left-leaning party assumes power in Germany.

This negative reaction can be attributed to several factors. Historically, left-leaning parties in Germany, such as the SPD or Die Linke, have advocated for higher public spending, labor market protections, and more progressive taxation, which can be perceived by markets as less favorable to business profitability and investor returns. While Germany's coalition-based governance often tempers radical policy shifts, the election of a dominant left-leaning party may still signal potential regulatory changes or fiscal expansion, which may raise concerns about corporate taxation and economic efficiency.

Moreover, investors may interpret a left-wing electoral victory as a signal of redistributive or interventionist policies. This interpretation is consistent with the broader literature on partisan effects in financial markets, which finds that markets tend to react negatively to the prospect of left-wing economic platforms, particularly in contexts where such outcomes are unexpected or coincide with weak macroeconomic fundamentals (Anderson et al., 2008).

At the same time, the absence of significance for center and right-wing victories could reflect market expectations of policy continuity or moderation, especially given Germany’s strong institutional stability and tradition of coalition governments. Investors may discount the impact of right-leaning leadership due to its historical alignment with market-friendly reforms and fiscal discipline.

This reinforces the idea that political ideology can shape market expectations, particularly when the policy direction departs from status quo norms.

5.4 Comparative Discussion

The results of this thesis show a clear divergence in how political events affect financial markets in France and Germany. While the CAC 40 demonstrates significant sensitivity to electoral variables, including election months, political orientation, and interactions with uncertainty and macroeconomic indicators, the DAX appears largely less affected. This divergence can be explained by profound institutional and political differences between the two countries.

Political Concentration and Market Sensitivity in France

France's semi-presidential system has historically fostered a high degree of political concentration following elections. The political landscape has traditionally been polarized, with clear ideological blocks on the left and right, and more recently, a centrist force gaining prominence. This polarization is structurally reinforced by the two-round presidential election system, which tends to produce decisive outcomes, historically resulting with dominant position in the political landscape, as strong executive power is attributed to the president.

Following the presidential elections, legislative elections are held within a few months, historically resulting in a parliamentary majority for the newly elected president's party. This synchronization of executive and legislative powers enables the ruling party to implement its policy agenda with limited opposition, as the president appoints a prime minister from within his political camp, and the National Assembly historically supports the government's proposals.

This institutional arrangement has significant implications for financial markets. The capacity of a single political force to alter economic, fiscal, and regulatory policy increases the market salience of elections, since investors anticipate concrete policy changes. As a result, markets often respond more strongly to electoral outcomes in France than in countries with more fragmented political systems. This observation is consistent with Pastor and Veronesi (2013), who argue that policy uncertainty, and by extension, market volatility, intensifies when a government has the institutional capacity to implement sweeping reforms.

Empirical evidence supports this link between political alignment and market impact in France. For example, in 2017, following the election of Emmanuel Macron, his newly formed party La République En Marche! secured an absolute majority in the National Assembly. This alignment allowed the swift introduction of labor reforms and tax incentives favoring businesses, contributing to a temporary boost in investor confidence. However, in 2022, despite Macron's re-election, his party only narrowly avoided a political deadlock in the legislative elections, and by 2024, after his decision to organize early legislative elections, no party held an outright majority. This departure from the traditional majoritarian pattern introduced political fragmentation and policy uncertainty, which likely increased market volatility during that period.

In contrast, Germany's system of coalition governments structurally prevents this kind of unilateral policymaking. The French political model, centered on concentrated executive power and ideological polarization, contributes to the amplified effect of elections on the CAC 40, relative to the more muted reactions observed in the German DAX.

Coalition Governance and Market Stability in Germany

Germany's political system contrasts sharply with France's, particularly in the way governments are formed and policies implemented. The German Bundestag is elected through a mixed-member proportional representation system, which almost never results in a single party gaining an absolute majority. Consequently, the formation of government always requires multi-party coalitions, often involving ideologically diverse partners from the center-right (CDU/CSU), center-left (SPD), Greens, and liberal or social democratic parties.

This coalition-based model inherently encourages moderation and compromise, as policy platforms must be negotiated among partners with different priorities. This results in incremental, consensus-driven policymaking, is typically viewed as more predictable and stable by financial markets. Accordingly, elections in Germany do not generate sharp changes in economic policy direction, unlike in more majoritarian systems such as France.

This structural feature likely explains why the empirical analysis shows little to no significant relationship between political events and DAX returns. Investors in German financial markets appear to interpret elections as procedural rather than disruptive events, given that the eventual policy trajectory will likely be the result of a carefully negotiated coalition agreement.

The literature supports this view. Bialkowski, Gottschalk, and Wisniewski (2008) show that stock market volatility around elections is significantly lower in consensus democracies, such as Germany, compared to countries with highly polarized or unstable political environments. Similarly, Pastor and Veronesi (2013) emphasize that policy uncertainty has a greater impact on markets when the probability of policy change is high, an unlikely outcome in a coalition-bound system.

Moreover, Germany's reputation for fiscal prudence, institutional resilience, and export-led economic strength adds an additional layer of stability. The market perceives German institutions as relatively immune to short-term political shocks, reinforcing the idea that the DAX is structurally less sensitive to electoral cycles.

Institutional Fracturing and Emerging Uncertainty in France

While France has historically exhibited a majoritarian and centralized model of governance, recent political developments suggest a departure from this paradigm. As previously mentioned, the 2024 legislative elections, which followed a presidential dissolution of the National Assembly, failed to produce an absolute majority for any party or bloc. This political fragmentation has introduced a level of institutional instability rarely seen under the Fifth Republic.

President Emmanuel Macron, re-elected in 2022 under the Renaissance (formerly La République En Marche!) banner, faced legislative defeats in both 2022 and 2024. His party failed to secure a governing majority, compelling negotiations with opposition forces to form an unstable and informal coalition. Following a vote of no-confidence against the initial government led by Michel Barnier (from the Right wing parti, Les Républicains), the president appointed Bayrou (from the centrist parti, MoDem) as prime minister under a new configuration, incorporating members of the presidential majority. Yet, this arrangement remained fragile, reflecting deep institutional tension and limited capacity for coherent policy implementation.

This evolution weakens one of the key features of the French model, executive-legislative alignment, which has historically enabled fast policymaking. As a result, markets may perceive higher political risk and reduced policy clarity, thus potentially increasing financial market sensitivity to political events, even without changes in ideological leadership, suggesting that uncertainty rises when governments are unable to credibly implement their platforms, regardless of political orientation.

These developments have led some analysts and political actors to question the relevance of the Fifth Republic's institutional architecture, with growing calls for a Sixth Republic featuring greater parliamentary empowerment and a more proportionally representative electoral system. The current two-round majority voting system, designed to produce stable majorities, now appears misaligned with the fragmentation of the modern French electorate. Analysts argue that this misalignment complicates governance and amplifies the market's reaction to political divergence.

In this context, France may be converging, de facto, towards a more coalition-based system, similar to Germany's. If France actually changes its electoral system and policy regime, as a result and on a long-term basis, the French financial markets may become more immune to political risk, adopting a coalition-based political regime.

Historical Example: The Mitterrand Shock of 1981

A landmark historical case illustrating the sensitivity of French financial markets to political change is the 1981 election of François Mitterrand, the first socialist president of the Fifth Republic. His victory marked a radical ideological shift after two decades of center-right leadership and was accompanied by the formation of a left-wing government including members of the French Communist Party, a highly symbolic political realignment at the height of the Cold War.

The policy program announced by Mitterrand included a series of left-leaning economic reforms, such as mass nationalizations of banks and industrial groups, the creation of hundreds of thousands of public sector jobs, a reduction in working hours, and tax increases on wealth and capital. These proposals triggered widespread investor concern about the future of private enterprise and the direction of economic governance.

The market response was immediate and pronounced. The Paris stock exchange dropped sharply in the days following the election. At the same time, capital flight intensified, with investors moving assets abroad in anticipation of restrictive policies and potential capital controls. According to historical financial press and economic analyses, the franc came under significant pressure, leading the government to eventually devalue the currency and introduce emergency capital controls in the early 1980s.

This episode serves as a powerful example of how, in the French institutional context, an electoral victory that grants full governing power to a single ideological bloc can trigger dramatic market reactions, especially when policy platforms diverge sharply from the status quo. The "Mitterrand shock" illustrates the argument advanced by Pastor and Veronesi (2013): the greater the expected policy change, the stronger the market response to electoral outcomes.

Although France has evolved since the 1980s, particularly in its relationship to the EU and the euro, the Mitterrand case remains a historical benchmark for understanding how centralization of power and ideological polarization can make French elections impactful for financial markets.

The Rise of Political Extremes and Market Exposure: France vs. Germany

Since the early 2000s, both France and Germany have experienced a notable rise in support for political extremes, on both the left and the right. This trend has introduced new sources of uncertainty for financial markets, particularly in countries where institutional structures allow these movements to convert electoral gains into actual governing power.

In France, the majoritarian two-round electoral system, combined with a historically low barrier to parliamentary representation, has created an environment where radically positioned parties can access power more easily. For instance, the far-right Rassemblement National (formerly Front National) has steadily increased its presence in national politics, reaching the second round of the presidential election in both 2017 and 2022, with its candidate Marine Le Pen. On the left, the rise of La France Insoumise, led by Jean-Luc Mélenchon and his close-by reach of the second tour in 2022, has introduced another pole of anti-establishment sentiment. While neither has held power directly, the possibility of a decisive electoral breakthrough remains tangible under the current system, particularly in the event of low turnout or fragmentation among moderate forces. The 2024 French legislative elections also marked a historic moment in the country's political landscape, with the rise of both far-right and far-left forces to unprecedented levels of parliamentary representation. The Rassemblement National (RN), secured 143 seats in the National Assembly, its highest number to date, despite coordinated efforts by parties to block its advance through tactical voting and alliances. On the left, La France Insoumise (LFI) formed an electoral alliance with traditional left-wing parties, such as the Socialist Party and the Greens, under the banner of the New Popular Front (Nouveau Front Populaire, NFP). This coalition won 192 seats, making it the largest political group in the Assembly, although still lacking an absolute majority. As a result, no single party or group emerged with the ability to govern independently, reinforcing the perception of political fragmentation.

This dual rise, of both the radical right and a broad left alliance, has contributed to heightened investor uncertainty and increased stock market volatility, particularly on indices such as the CAC 40. Markets reacted to the elevated risk of ideological polarization, potential institutional instability, and the ambiguity surrounding future economic policy direction. This reaction is consistent with recent empirical findings by Stancea, Ciocîrlan, and Despina (2024), who demonstrate that market volatility tends to rise sharply when ideologically extreme parties gain influence in European elections, especially when such outcomes create governance uncertainty. The fear among investors is rooted in possible policy reversals, but also in institutional paralysis.

The surge of the RN raised concerns over potential protectionist measures, anti-EU rhetoric, and restrictive immigration policies, while the rise of the NFP was associated with increased public spending, labor market regulation, and fiscal redistribution, all of which may affect sectors such as finance, energy, and large multinationals represented on the CAC 40.

By contrast, Germany’s coalition-based parliamentary system acts as a buffer against extremist outcomes. Even with the electoral gains of the far-right Alternative für Deutschland (AfD) or the more radical left elements within Die Linke, the likelihood of these parties joining a governing coalition remains very low. Coalition negotiations typically exclude such parties and prioritize moderation and policy compatibility, ensuring that government agendas remain predictable.

Political Extremes and Institutional Insulation in Germany

In Germany, the rise of Alternative für Deutschland (AfD) has represented the most significant challenge to the post-war political consensus. The party entered the Bundestag for the first time in 2017, securing 94 seats and becoming the third-largest parliamentary group. In the subsequent 2021 federal elections, the AfD maintained a strong presence with over 80 seats, solidifying its role as a major opposition force. Although outside of this thesis study period, the 2025 German elections resulted in a new increase of seats for AfD, with 152 seats, making it the second largest parti in the Bundestag.

Despite these electoral advances, the AfD has remained systematically excluded from all coalition negotiations at the federal level. Both major center-right and center-left parties, Christlich Demokratische Union (CDU), Sozialdemokratische Partei Deutschlands (SPD), as well as the Greens and Free Democratic Party (FDP), have repeatedly ruled out any collaboration with the AfD, citing its nationalist, anti-EU, and anti-immigration rhetoric.

This broad political consensus has resulted in the formation of centrist and ideologically diverse coalitions, such as the "traffic light" coalition (SPD-Greens-FDP) that took power after the 2021 elections. These coalitions tend to pursue moderate, negotiated policy agendas, and their formation signals a high degree of institutional stability and commitment to the European democratic framework.

Consequently, financial markets have exhibited limited reaction to AfD's electoral performance. The exclusion of the party from executive power reduces the probability of radical policy implementation, and the coalition model ensures continuity and predictability in economic and fiscal policymaking. This aligns with the findings of Döpke and Pierdzioch (2006), who argue that in Germany, stock market responses to political shifts are generally muted, due in part to coalition constraints and institutional safeguards.

While the rise of political extremes is not absent in Germany, the institutional architecture of coalition governance effectively buffers markets from policy shocks, contributing to the lower volatility of the DAX index in response to elections, as observed in this thesis.

Italy as an Intermediate Case: Electoral Sensitivity and Political Uncertainty

To nuance the comparative findings of this thesis, the case of Italy offers a compelling example. In addition to France and Germany, Italy was included in the analysis as a representative of a third major European market. The results concerning Italy, available in the Appendices section, indicate that the FTSE Italy index occupies a middle ground between the French and German models in terms of market sensitivity to political variables.

The primary electoral variable ("Election months") was not statistically significant for Italy, suggesting that the mere occurrence of elections does not systematically impact stock returns. However, several interaction variables did reach statistical significance, notably "Election Months and MSCI EU" and "Election Months and European News-Based". These findings reveal that Italian financial markets are particularly sensitive to political and economic uncertainty during electoral periods, especially when that uncertainty is reflected in broader European trends or domestic news-based indicators.

Importantly, the estimates for these interaction variables are negative, suggesting that when political uncertainty rises during election periods, stock returns on the FTSE Italy tend to decrease. This aligns with the interpretation that markets view Italian elections as risk-enhancing events, particularly in the presence of broader uncertainty or regional instability.

This dynamic can be linked to the institutional characteristics of the Italian political system, which is a parliamentary democracy with a proportional representation electoral system. While this system, like Germany's, often produces coalition governments, Italian politics has historically been marked by frequent government turnover, short-lived coalitions, and limited policy continuity. This instability has contributed to a reputation for political volatility, which remains a key risk factor for investors.

Furthermore, the recent rise of the far right in Italy, exemplified by the 2022 general election victory of Giorgia Meloni and her party, Fratelli d'Italia, has likely contributed to elevated perceptions of political uncertainty. Meloni's ascent marked a historic moment, as it brought a post-fascist party to power for the first time since World War II. While her government has maintained EU alignment and fiscal discipline so far, the election itself introduced heightened short-term uncertainty, especially given her previous Eurosceptic positions and nationalist rhetoric. This partially explains why Italian markets exhibit some degree of electoral sensitivity, but not to the same extent as France. In contrast to the institutional rigidity and centralization of power observed in France, Italy's political fragmentation and coalition constraints limit the scope for radical policy change. However, unlike Germany, Italian coalitions are often unstable, and investors remain concerned about governance continuity, particularly during elections.

The Italian case illustrates that the interaction between political uncertainty and electoral timing matters more than elections alone. While not as reactive as the French market, the Italian financial system demonstrates a moderate level of sensitivity to political uncertainty, shaped by a mix of structural volatility and institutional limits on executive power.

6 Limitations and Further Research

The methodological approach adopted in this thesis proved to be an appropriate tool for answering the research question. However, some limitations must be acknowledged. First, the model assumes linearity and independence between variables, which may not fully capture the complexity of market reactions to political events. While the analysis included controls such as MSCI indices and inflation or GDP growth, there may be non-linear dynamics that a linear model cannot identify. Additionally, issues of multicollinearity led to the exclusion of certain interaction terms in the German case, which reduced the comparability of some results across countries. Another limitation is the reliance on monthly data, which may obscure short-term shocks or rapid market corrections that often occur in the days immediately following elections. A more granular analysis using weekly data could offer different insights.

While this thesis provides insights into the relationship between legislative elections and stock market performance in Europe, several avenues remain open for future research, both in terms of scope and methodological refinement.

One promising direction concerns the impact of political extremism on financial markets, particularly in the case of France and Germany. While the present study focused on election timing and government orientation, it did not explore in detail the composition of the legislature, nor the rise of far-left and far-right parties. Future models could examine whether the number of parliamentary seats obtained by extreme parties, even if they do not enter government, affects investor sentiment and market performance. Given the increased prominence of parties such as “La France Insoumise” or “Rassemblement National” in France, it is plausible that markets respond negatively to the strengthening of radical political forces, due to fears of policy disruption or institutional instability. Such a study would help investors better anticipate election-driven shifts in perceived political risk.

Second, future research could broaden the geographical scope of analysis. This thesis included additional countries in the Appendices section, such as Italy, Spain, the United Kingdom, Belgium, and the Netherlands. Some of these showed preliminary patterns of interest and would merit full empirical inclusion in future comparative studies. A broader panel would allow researchers to test the generality of the mechanisms identified in France and Germany, and to explore regional political dynamics, especially within the eurozone.

Another highly relevant extension would be to study the impact of European Parliament elections. While supranational in nature, these elections may increasingly influence national markets, particularly when they result in shifts in EU policy direction, the strengthening of populist blocs, or market-sensitive outcomes such as debates on fiscal rules, environmental regulation, or integration policy.

Another valuable area of exploration would be the development of “cross-country spillover models”, which examine whether political events in one country influence financial indices in others. For instance, one could analyze whether a legislative shock in France affects investor behavior in Germany, or whether Italian election uncertainty spills over into broader European indices such as the MSCI Europe. This would capture the interconnected nature of European financial markets, where local political instability may have contagion effects, especially in periods of heightened integration or systemic stress.

Future research could continue to examine how political events inherently are key moments of financial and geopolitical significance.

7 Conclusion

This thesis aims to answer a central question: do legislative elections in European countries impact the performance of national stock indices, and if so, to what extent does this impact differ across political systems? To answer this question, a comparative empirical analysis was conducted using multiple linear regression models, focusing on two representative European economies: France and Germany. The thesis also mentions an analysis of Italy, to provide a more nuanced and comparative study. Therefore, their respective stock indices are analyzed: the CAC 40, DAX, and FTSE Italy.

The main conclusion drawn from the analysis is that legislative elections do affect financial markets, but the intensity, direction, and nature of this effect are strongly context dependent. The relationship is not uniform across Europe; instead, it is mediated by institutional characteristics, political traditions, and market expectations.

In France, the results clearly show a significant and consistent market reaction during election periods. The Election Months variable and several interaction terms (with uncertainty and macroeconomic indicators) were statistically significant, often with a negative estimate, indicating increased volatility and reduced investor confidence. This can be attributed to the semi-presidential political system, which tends to centralize power and allows a newly elected majority to enact rapid policy changes. Historically, French voters have reinforced presidential authority through legislative support, creating conditions for strong, ideologically driven policy shifts. Markets react to this concentration of power because it increases both policy uncertainty and potential for abrupt economic reforms, particularly when ideological extremes gain influence.

In contrast, the case of Germany revealed no significant impact of elections on stock market returns. Neither the occurrence of elections nor the orientation of the winning party significantly affected the DAX index. This can be explained by Germany's federal, parliamentary system, which nearly always results in coalition governments, often composed of centrist parties. These coalitions reduce ideological polarization and increase predictability, dampening the market's reaction to political cycles. The German political environment is perceived by investors as institutionally robust and resistant to radical change, a perception confirmed by the empirical findings.

The results for Italy fall somewhere between the French and German cases. While the main election-related variables were not significant, some interaction effects, such as "Election Months and Political Uncertainty", were both significant and negatively signed. This suggests that Italian markets react to elections primarily when they coincide with periods of heightened uncertainty, reflecting concerns about governance instability and policy fragmentation. Italy's frequent government turnover, complex coalition arrangements, and a growing presence of populist parties contribute to a perception of fragility, even if direct electoral effects remain less visible than in France.

Taken together, these findings support the conclusion that legislative elections can influence stock market returns. This influence depends critically on the institutional and political context of each country. Centralized systems with majoritarian outcomes, like France, tend to provoke stronger market responses, while consensual and coalition-based systems, like Germany's, act as a buffer. Italy demonstrates that institutional weakness and uncertainty, rather than elections per se, can also trigger market reactions.

This thesis contributes to the growing literature at the intersection of political science and financial economics by offering a comparative analysis of the impact of legislative elections on national stock markets in Europe. While previous studies have often focused on single-country cases or presidential elections, this research provides a national perspective, drawing on the contrasting political systems of France, Germany, and Italy to highlight the institutional determinants of market reactions to electoral events.

The key contribution lies in demonstrating that elections do not affect markets in a uniform way across democratic contexts. Instead, the effect depends strongly on the structure of the political system, the potential for abrupt policy change, and the degree of political uncertainty surrounding the electoral cycle. By incorporating interaction terms with macroeconomic and political uncertainty indicators, this thesis also shows that markets react most strongly to elections that occur under conditions of elevated uncertainty.

The study offers a framework for investors and policymakers to better assess political risk, particularly in countries where institutional structures amplify the consequences of electoral outcomes. This research underscores the importance of contextualizing political risk, showing that the structure of governance matters just as much as electoral results. It invites investors to consider the institutional architecture that transforms elections into economic signals.

Ultimately, this thesis demonstrates that understanding the financial consequences of political elections in Europe requires more than tracking electoral calendars, it demands a deeper analysis of institutional structures, political dynamics, and market psychology. The findings contribute to a more nuanced perspective on how democracy shapes markets in Europe. As the continent faces rising political polarization and growing electoral uncertainty, understanding how democratic processes influence financial markets is more important than ever.

8 Appendices

8.1 Integration Tests for the MLR

8.1.1 Stationarity Tests (on R Studio)

France

Table 8.1: Results of the Stationarity tests of the variables for the CAC 40 models

Augmented Dickey-Fuller Test	Coefficient	p-value	<0,05
`Return CAC 40`	-5,70	0,01	stationary
`Election months`	-4,15	0,01	stationary
`Left wing wins`	-3,64	0,03	stationary
`Center wins`	-4,20	0,01	stationary
`Right wing wins`	-3,49	0,04	stationary
`Return MSCI EU`	-5,53	0,01	stationary
`GDP growth`	-4,56	0,01	stationary
`VAR Inflation rate`	-3,98	0,01	stationary
`VAR Global Economic Policy Uncertainty`	-6,76	0,01	stationary
`VAR European News-Based Index (FRANCE)`	-6,91	0,01	stationary

Source: The author's analysis

Germany

Table 8.2: Results of the Stationarity tests of the variables for the DAX models

Augmented Dickey-Fuller Test	Coefficient	p-value	<0,05
`Return DAX`	-5,91	0,01	stationary
`Election months`	-4,40	0,01	stationary
`Left wing wins`	-3,83	0,02	stationary
`Center wins`	-4,43	0,01	stationary
`Return MSCI EU`	-5,53	0,01	stationary
`GDP growth`	-4,13	0,01	stationary
`VAR Inflation rate`	-3,49	0,01	stationary
`VAR Global Economic Policy Uncertainty`	-6,76	0,01	stationary
`VAR European News-Based Index (Germany)`	-7,35	0,01	stationary

Source: The author's analysis

To verify the stationarity of the time series variables used in the regressions, the Augmented Dickey-Fuller (ADF) test was applied using R Studio. Testing for stationarity is a crucial step in time series econometrics, as the presence of a unit root can lead to spurious regression results (Newbold & Granger, 1974; Damjanovic et al., 2015). The ADF test evaluates the null hypothesis that a unit root is present in the series. A variable is considered stationary if the null hypothesis is rejected at conventional significance levels.

According to standard econometric literature, a p-value below 0.05 is generally used as the threshold for rejecting the null hypothesis of non-stationarity. In this study, all variables used in the models for both France and Germany yielded p-values below 0.05 in the ADF test, indicating that the time series are stationary and suitable for regression analysis without the risk of non-stationarity bias.

8.1.2 Multicollinearity Tests (on R Studio)

8.1.2.1 France

Table 8.3: Results of the Multicollinearity tests of the variables for the CAC 40 models

General Model

Variable	`Election months`	`Return MSCI EU`	`GDP growth`	`VAR Inflation rate`
Coefficient	3,75	1,24	1,32	1,67
Variable	`VAR Global Economic Policy Uncertainty`	`VAR European News-Based Index (FRANCE)`	`Election and MSCI EU`	`Election and GDP Growth`
Coefficient	1,80	1,99	1,16	4,47
Variable	`Election and Inflation rate`	`Election and Uncertainty`	`Election and European news-based`	
Coefficient	1,64	2,80	3,15	

Specific Model

Variable	`Election months`	`Return MSCI EU`	`GDP growth`	`Election and GDP Growth`
Coefficient	3,54	1,01	1,02	3,78
Variable	`Election and Uncertainty`	`Election and European news-based`		
Coefficient	2,64	2,61		

General Model with Political Orientation

Variable	`Election months`	`Left wing wins`	`Center wins`	`Right wing wins`
Coefficient	3,91	1,15	1,14	1,16
Variable	`VAR Global Economic Policy Uncertainty`	`Return MSCI EU`	`GDP growth`	`VAR Inflation rate`
Coefficient	1,82	1,27	1,34	1,67
Variable	`VAR European News-Based Index (FRANCE)`	`Election and MSCI EU`	`Election and GDP Growth`	`Election and Inflation rate`
Coefficient	1,99	1,16	4,16	1,28
Variable	`Election and Uncertainty`	`Election and European news-based`		
Coefficient	2,85	3,11		

Specific Model with political orientation

Variable	`Election months`	`Left wing wins`	`Return MSCI EU`	`VAR Inflation rate`
Coefficient	3,84	1,10	1,04	1,09
Variable	`Election and GDP Growth`	`Election and Uncertainty`	`Election and European news-based`	
Coefficient	4,08	2,67	2,62	

Model with the macro-economic and financial variables only

Variable	`Return MSCI EU`	`GDP growth`	`VAR Inflation rate`
Coefficient	1,05	1,26	1,30

Model with the political variables only

Variable	`Election months`	`Left wing wins`	`Center wins`	`Right wing wins`
Coefficient	1,13	1,04	1,06	1,11
Variable	`VAR Global Economic Policy Uncertainty`	`VAR European News-Based Index (FRANCE)`	`Election and Uncertainty`	`Election and European news-based`
Coefficient	1,68	1,97	2,47	2,79

Source: The author's analysis

8.1.2.2 Germany

Table 8.4: Results of the Multicollinearity tests of the variables for the DAX models

General Model

Variable	`Election months`	`Return MSCI EU`	`GDP growth`	`VAR Inflation rate`
Coefficient	1,27	1,19	1,43	1,41
Variable	`VAR Global Economic Policy Uncertainty`	`VAR European News-Based Index (Germany)`	`Election and MSCI EU`	`Election and Uncertainty`
Coefficient	1,88	2,03	1,35	2,49
Variable	`Election and European news-based`			
Coefficient	2,82			

Specific Model

N/A

General Model with Political Orientation

Variable	`Election months`	`Left wing wins`	`Center wins`	`Return MSCI EU`
Coefficient	1,37	1,73	1,15	1,20
Variable	`GDP growth`	`VAR Inflation rate`	`VAR Global Economic Policy Uncertainty`	`VAR European News-Based Index (Germany)`
Coefficient	1,65	2,32	1,88	2,03
Variable	`Election and MSCI EU`	`Election and Uncertainty`	`Election and European news-based`	
Coefficient	1,36	2,51	2,86	

Specific Model with political orientation

N/A

Model with the macro-economic and financial variables only

Variable	`Return MSCI EU`	`GDP growth`	`VAR Inflation rate`
Coefficient	1,01	1,38	1,40

Model with the political variables only

Variable	`Election months`	`Left wing wins`	`Center wins`	`VAR Global Economic Policy Uncertainty`
Coefficient	1,16	1,04	1,10	1,82
Variable	`VAR European News-Based Index (FRANCE)`	`Election and Uncertainty`	`Election and European news-based`	
Coefficient	2,01	2,49	2,82	

Source: The author's analysis

To assess potential multicollinearity issues in the regression models, the Variance Inflation Factor (VIF) test was performed using R Studio. According to standard econometric literature, a VIF value below 5 is generally considered acceptable, although some authors accept values up to 10 (Tsagris and Pandis, 2021). In this study, all retained explanatory variables across models exhibit VIF values below 5, indicating no serious multicollinearity concerns.

For the General Model of Germany, two interaction terms, "Election months and GDP Growth" and "Election months and Inflation rate", were removed from the model due to high multicollinearity. Their VIF values exceeded the threshold of 10, indicating a strong linear dependency with other explanatory variables. Once excluded, the remaining variables showed acceptable VIF levels, all below 5.

In the Specific Model and the Specific Model with political orientation for Germany, multicollinearity was not an issue, as each model includes only one independent variable alongside the dependent variable. Therefore, no VIF test interpretation was necessary in those cases.

For the General Model with political orientation of Germany, multicollinearity was again observed. The variable "Right-wing wins" and the interaction terms "Election months and GDP Growth" and "Election months and Inflation rate" were excluded due to VIF values exceeding 10. After removing these variables, the remaining predictors passed the VIF test, with all values under 5.

8.2 Results of the MLR analysis for FTSE Italy

8.2.1 General Model

Table 8.5: Results of the General Model for the MLR analysis of the FTSE Italy

FTSE Italy	Estimate	Std. Error	P-value	
(Intercept)	-0,002	0,002	0,307	
`Election months`	-0,002	0,003	0,604	
`Return MSCI EU`	1,182	0,044	0,000	***
`GDP growth`	0,023	0,053	0,667	
`VAR Inflation rate`	-0,006	0,091	0,946	
`VAR Global Economic Policy Uncertainty`	-0,005	0,010	0,642	
`VAR European News-Based Index (Italy)`	0,000	0,005	0,986	
`Election and MSCI EU`	-0,217	0,127	0,089	*
`Election and GDP Growth`	-0,264	0,381	0,489	
`Election and Inflation rate`	0,409	0,331	0,217	
`Election and Uncertainty`	0,030	0,040	0,450	
`Election and European news-based`	-0,049	0,020	0,014	**

Adjusted R-squared = 78,43%

Source: The author's analysis

8.2.2 Specific Model

Table 8.6: Results of the Specific Model for the MLR analysis of the FTSE Italy

FTSE Italy	Estimate	Std. Error	P-value	
(Intercept)	-0,002	0,002	0,269	
`Return MSCI EU`	1,188	0,041	0,000	***
`Election and MSCI EU`	-0,209	0,124	0,093	*
`Election and European news-based`	-0,045	0,016	0,006	***

Adjusted R-squared = 78,90%

Source: The author's analysis

8.3 Results of the MLR analysis of the other indices

Table 8.7: Results of the General Model for the MLR analysis of the AEX (Netherlands)

AEX	Estimate	Std. Error	P-value	
(Intercept)	0,002	0,001	0,239	
`Election months`	-0,002	0,003	0,349	
`Return MSCI EU`	1,005	0,028	0,000	***
`GDP growth`	0,004	0,060	0,941	
`VAR Inflation rate`	-0,006	0,049	0,895	
`VAR Global Economic Policy Uncertainty`	-0,009	0,010	0,339	
`VAR European News-Based Index (EU)`	0,008	0,008	0,328	
`Election and MSCI EU`	-0,037	0,123	0,765	
`Election and GDP Growth`	0,040	0,176	0,821	
`Election and Inflation rate`	-0,101	0,185	0,587	
`Election and Uncertainty`	-0,046	0,031	0,142	
`Election and European news-based`	0,033	0,027	0,220	

Adjusted R-squared = 85,82%

Source: The author's analysis

Table 8.8: Results of the Specific Model for the MLR analysis of the AEX (Netherlands)

AEX	Estimate	Std. Error	P-value	
(Intercept)	0,001	0,001	0,225	
`Return MSCI EU`	1,000	0,026	0,000	***
`Election and Uncertainty`	-0,053	0,029	0,072	*
`Election and European news-based`	0,040	0,026	0,116	

Adjusted R-squared = 86,10%

Source: The author's analysis

Table 8.9: Results of the General Model for the MLR analysis of the FTSE UK

FTSE UK	Estimate	Std. Error	P-value	
(Intercept)	0,003	0,002	0,212	
`Election months`	0,000	0,003	0,959	
`Return MSCI EU`	0,994	0,028	0,000	***
`GDP growth`	-0,003	0,034	0,936	
`Inflation rate`	-0,038	0,052	0,464	
`VAR Global Economic Policy Uncertainty`	-0,007	0,007	0,340	
`VAR European News-Based Index (UK)`	0,005	0,004	0,264	
`Election and MSCI EU`	0,040	0,128	0,756	
`Election and GDP Growth`	0,084	0,125	0,503	
`Election and Inflation rate`	0,016	0,236	0,946	
`Election and Uncertainty`	-0,020	0,031	0,524	
`Election and European news-based`	-0,024	0,013	0,066	*

Adjusted R-squared = 85,80%

Source: The author's analysis

Table 8.10: Results of the General Model for the MLR analysis of the IBEX 35 (Spain)

IBEX 35	Estimate	Std. Error	P-value	
(Intercept)	-0,003	0,003	0,396	
`Election months`	-0,006	0,004	0,160	
`Return MSCI EU`	1,055	0,051	0,000	***
`GDP growth`	0,030	0,064	0,640	
`Inflation rate`	0,128	0,115	0,266	
`VAR Global Economic Policy Uncertainty`	-0,003	0,012	0,796	
`VAR European News-Based Index (Spain)`	-0,006	0,005	0,184	
`Election and MSCI EU`	-0,218	0,156	0,165	
`Election and GDP Growth`	0,200	0,218	0,360	
`Election and Inflation rate`	0,152	0,279	0,587	
`Election and Uncertainty`	-0,020	0,035	0,571	
`Election and European news-based`	-0,006	0,016	0,693	

Adjusted R-squared = 68,83%

Source: The author's analysis

Table 8.11: Results of the Specific Model for the MLR analysis of the IBEX 35 (Spain)

IBEX 35	Estimate	Std. Error	P-value	
(Intercept)	-0,004	0,003	0,147	
`Return MSCI EU`	1,038	0,046	0,000	***
`Inflation rate`	0,182	0,091	0,046	**
`VAR European News-Based Index (Spain)`	-0,008	0,004	0,070	*

Adjusted R-squared = 69,14%

Source: The author's analysis

Table 8.12: Results of the General Model for the MLR analysis of the BEL 20 (Belgium)

BEL 20	Estimate	Std. Error	P-value	
(Intercept)	-0,001	0,002	0,429	
`Election months`	-0,001	0,005	0,799	
`Return MSCI EU`	0,943	0,035	0,000	***
`GDP growth`	0,089	0,070	0,204	
`VAR Inflation rate`	-0,050	0,067	0,453	
`VAR Global Economic Policy Uncertainty`	0,006	0,012	0,601	
`VAR European News-Based Index (EU)`	-0,009	0,010	0,357	
`Election and MSCI EU`	-0,064	0,160	0,689	
`Election and GDP Growth`	-0,073	0,385	0,850	
`Election and Inflation rate`	-0,434	0,272	0,111	
`Election and Uncertainty`	-0,032	0,035	0,363	
`Election and European news-based`	0,050	0,027	0,067	*

Adjusted R-squared = 78,75%

Source: The author's analysis

Table 8.13: Results of the Specific Model for the MLR analysis of the BEL 20 (Belgium)

BEL 20	Estimate	Std. Error	P-value	
(Intercept)	-0,001	0,001	0,616	
`Return MSCI EU`	0,954	0,031	0,000	***
`Election and Inflation rate`	-0,396	0,234	0,091	*
`Election and European news-based`	0,027	0,017	0,115	

Adjusted R-squared = 79,13%

Source: The author's analysis

Although not directly analyzed or interpreted within the core scope of this thesis, the regression results presented in the appendices for several other European countries (Italy, Spain, the Netherlands, the United Kingdom, and Belgium) provide valuable insights and could serve as a foundation for further research. These findings have the potential to contribute meaningfully to the growing body of literature examining the impact of political events on financial markets across Europe.

This thesis focuses primarily on France and Germany, with references to Italy to enrich the discussion and introduce comparative nuance. However, extending the analysis to include additional countries such as Spain, the Netherlands, the UK, and Belgium would be a highly relevant direction for future studies, especially considering some of the preliminary patterns observed in these datasets.

It should be noted, however, that the results for these additional countries were generated using a simplified approach and have not been subjected to the same level of in-depth econometric scrutiny as those for France and Germany.

8.4 Codes used for the MLR on R Studio

The R script presented in this section is a representative example of the code used to perform one of the MLR models developed in this study. While the specific code varies depending on the structure and variables of each individual model, only one example is provided here for clarity and conciseness.

8.4.1 Code for the MLR

```
modele_complet_General <- lm(`Return CAC 40` ~ `Election months` +
                       `Left wing wins` +
                       `Center wins` +
                       `Right wing wins` +
                       `Return MSCI EU` +
                       `GDP growth` +
                       `VAR Inflation rate` +
                       `VAR Global Economic Policy Uncertainty` +
                       `VAR European News-Based Index (FRANCE)` +
                       `Election and MSCI EU` + `Election and GDP Growth` +
                       `Election and Inflation rate` +
                       `Election and Uncertainty` +
                       `Election and European news-based`,
                     data = donnees)

summary(modele_complet_General)

modele_step <- step(modele_complet, direction = "both")

summary(modele_step)
```

8.4.2 Code for the VIF Tests (Multicollinearity)

```
library(car)

vif(modele_complet_General)
```

8.4.3 Code for the Augmented Dickey-Fuller Tests (Stationarity)

```
library(tseries)

adf.test(donnees$`Return CAC 40`, alternative = "stationary")
adf.test(donnees$`Election months`, alternative = "stationary")
adf.test(donnees$`Left wing wins`, alternative = "stationary")
adf.test(donnees$`Center wins`, alternative = "stationary")
adf.test(donnees$`Right wing wins`, alternative = "stationary")
adf.test(donnees$`Return MSCI EU`, alternative = "stationary")
adf.test(donnees$`GDP growth`, alternative = "stationary")
adf.test(donnees$`VAR Inflation rate`, alternative = "stationary")
adf.test(donnees$`VAR Global Economic Policy Uncertainty`, alternative = "stationary")
adf.test(donnees$`VAR European News-Based Index (FRANCE)`, alternative = "stationary")
```

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Statement on the Use of Artificial Intelligence

In accordance with the ULiège Charter for the use of generative Artificial Intelligence in academic work, I declare that AI tools were used exclusively as linguistic assistants and information search assistants during the preparation of this thesis. Their role was to improve the formulation, clarity, and syntax of texts that I personally wrote. I take full responsibility for the intellectual content of this thesis.

EXECUTIVE SUMMARY

This thesis investigates whether legislative elections in European countries have a measurable impact on national stock market returns, with a comparative analysis of France and Germany. While the link between political uncertainty and market volatility is well-documented, this research focuses specifically on the electoral context and how different political systems condition market reactions.

The study uses multiple linear regression models applied to monthly data from 2004 to 2025, incorporating variables such as election periods, political uncertainty indices, macroeconomic indicators, and political orientation. Each country's main stock index (CAC 40 and DAX) is analyzed in relation to its institutional and electoral framework.

The results reveal significant differences between countries. In France, legislative elections consistently impact market returns, often negatively, due to the centralized nature of its semi-presidential system and the possibility of abrupt policy shifts. Germany shows no significant electoral effect, reflecting the stability and predictability provided by its coalition-based parliamentary model. The analysis also finds that the political orientation of governing parties may influence market outcomes, particularly in France, where left and right-wing victories tend to have negative effects.

These findings highlight the importance of institutional context in mediating how markets react to democratic events. Elections do matter, but their effects depend on how power is structured and exercised. The thesis also suggests that the political orientation of the parti in power influences domestic financial markets.

Further research is encouraged to examine other European countries and to explore cross-border electoral effects. By linking political structures to financial behavior, this study offers valuable insights for investors in understanding the evolving relationship between politics and financial markets in Europe.

KEYWORDS: Legislative Elections, Financial Market Returns, Political Uncertainty, Comparative Economy, European Indices, Institutional Context, Econometric analysis, Political Orientation, Market Volatility.

WORD COUNT: 17 574

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