News

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The short-term outlook for the euro is uncertain, but Donald Trump's victory in the US presidential election - coupled with a Republican clean sweep of Congress - make a slide against the dollar much more likely in 2025.

After a strong summer, darker nights have seen the euro weaken against the dollar as the US economy continues to pull ahead of European counterparts. The euro had risen to USD 1.12 by the end of September. In October and into early November, it dipped below USD 1.08.

With its summer rally over, what can we expect next for the euro? Analyst Oxford Economics USD forecasts a weakening of the euro to USD 1.05 by the beginning of 2025.

But the near term is more uncertain. Three main risk factors are likely to determine the euro's direction of travel in the coming weeks and months. In the rest of this article we'll discuss what these risks are and the impact they might have.

Interest rate cuts offer support to the euro

Both the European Central Bank (ECB) and US Federal Reserve (Fed) have started on a rate cutting journey, driven by favourable inflation and labour market data. But how far will this loosening go and what impact will it have on exchange rates?

Shifts in expectations around cutting cycles on both sides of the Atlantic are likely to be the chief driver of FX moves in the next few months. As things stand, the trend favours a strengthening euro, at least in the short term.

The market is pricing more cuts, with expectations of a total of 180 basis points (bps) of cuts from the Fed by end of 2025, though some analysts think the figure could be as high as 250bps.

The ECB takes a highly data-dependent, meeting-by-meeting approach to rate cutting which creates considerable volatility in interest rate expectations. At the moment, concerns about wage growth and services inflation remain.

Nevertheless, many analysts expect back-to-back rate cuts from now until at least March 2025, and a total cutting cycle of around 150bps by the end of 2025.

If top end expectations play out, and the Fed cuts rates at a slightly faster rate than the ECB, this would point to the euro strengthening against the dollar. However, much uncertainty remains. A Trump presidency - of which more below - could create inflationary pressures that keep US interest rates higher for longer through 2025 and beyond.

The impact of Trump 2.0

The outcome of the US presidential election was always going to have a significant impact on the global economy and global financial conditions. With the outcome now known, we can focus on what a second Trump presidency might mean for inflation, interest rates and the euro-dollar exchange rate.

During the campaign, Trump floated plans for blanket 10% - 20% tariffs on all imports, and 60% tariffs or more on goods from China. In one outburst, Trump said he would slap a 200% tariff on John Deere's imports if the agricultural machinery giant moved production to Mexico.

Trump now has the power to turn promises into policy. Not only has he won the presidency, the Republican party has a majority in both houses of Congress, giving him a much freer hand.

"The US election results mean that President Trump will be largely unconstrained in terms of economic policy when he takes power in January," says Atradius economist Theo Smid. "That could spell trouble for the euro".

> Tariffs and tax cuts could see the dollar rallying sharply and the euro losing ground
>
> Theo Smid

Goldman Sachs economists have calculated that Trump's win could cause the euro to tumble by 8% to 10%, assuming he follows through on campaign rhetoric. The combination of tariffs and tax cuts are likely to push up US growth and inflation, with the Fed likely to keep interest rates higher for longer in response. That would boost the dollar's appeal. If Trump only imposed tariffs on China, that could still see the euro fall by around 3%, according to Goldman Sachs.

The euro last traded at below parity with the dollar in November 2022, but Trump's sweeping win means a repeat of that scenario now looks likely.

Regional conflicts weigh on euro

The war in Ukraine continues to weigh on eurozone economies, but with the

conflict approaching its third year , the economic impacts are to some extent priced in.

A more pressing geopolitical factor at the moment is the potential for escalation in the Middle East, where Israel and Iran are engaged in tit-for-tat military strikes. In this tinderbox environment there is a very real risk of all-out regional conflict, which would threaten the oil trade and significantly weaken the currencies of net oil importers.

Such a scenario would weigh far more heavily on Europe than the US, undermining eurozone growth. The dollar could also surge as a safe haven asset.

Alternatively, the conflict could gradually peter out, with the global oil trade remaining largely unaffected. This is perhaps the more likely outcome at present, with economic and domestic pressures blunting Iran's appetite for an all-out war. In this scenario, the risk of full-scale conflict would be priced out, supporting the euro against the dollar.

Trade war presents a risk

Taken together, these risk factors paint an uncertain picture.

"On one hand, current interest rate trends and more optimistic predictions for de-escalation in the Middle East support a strengthening euro," says Theo Smid. "On the other hand, an unrestrained Trump presidency looks likely to rally the dollar with inflationary tariffs and tax cuts, and a wider Middle Eastern conflict would also favour the US currency."

The Atradius baseline scenario anticipates targeted US tariffs on China and to a lesser extent on the European Union, Mexico, and Canada. However, if Trump adheres to his campaign promises, such as imposing a 60% tariff on Chinese imports and 10% tariffs on other major trading partners, the situation could change significantly.

This could trigger a trade war, leading to increased costs and price pressures, which would negatively affect productivity and likely result in a further weakening euro in 2025 and beyond.