Flash Economics

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Europe faces Chinese overproduction and US tariffs

One can be rather pessimistic about the outlook for European manufacturing, despite the recovery seen at the start of 2025, which was due to anticipation of the tariffs imposed by the Trump administration.

On the one hand, China has excess production capacity in its manufacturing sector and, facing greater difficulty in exporting to the United States, will try to offload its output in Europe.

On the other hand, the United States will tax European exports for the majority of goods at 15%, and Europe is in a weak position in negotiations with the United States because of its dependence on American technology companies.

We must therefore, unfortunately, expect on the one hand a fall in Europe's exports to the United States and a relocation of production from Europe to the United States (exacerbated by the gap in energy prices); and, on the other hand, a rise in Europe's imports from China, resulting overall in a decline in European industrial production.

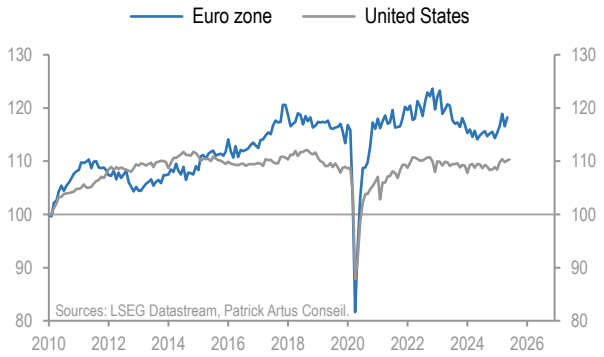
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A recovery in Europe's manufacturing output is very unlikely in the medium term

Europe's manufacturing output rose slightly in the first half of 2025 (Chart 1).

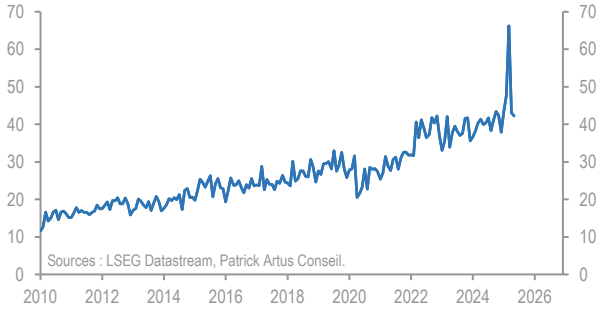
Chart 1
Manufacturing production (2010.M1 = 100)



But this recovery is mainly linked to stockpiling of manufactured goods in anticipation of the increase in US tariffs.

When looking at Europe's exports of goods to the United States, one sees (Chart 2) a peak in the first quarter of 2025 associated with the anticipation of tariffs, but this peak is subsequently corrected.

Chart 2
Euro zone: Exports of goods to the United States
(monthly data, in EUR bn)



In reality, the outlook for European manufacturing is unfavourable due to the economic context:

- The low utilisation of production capacity in China;
- The tariffs imposed by the United States on imports of European goods, in addition to the fact that energy prices are significantly higher in Europe than in the United States.

Underutilisation of capacity in China

China suffers from chronic underutilisation of its industrial production capacity (Chart 3), which leads to falling prices (Chart 4) and a strong ability to export output produced on this excess capacity.

Chart 3
China: Capacity utilization for manufacturing (as %)

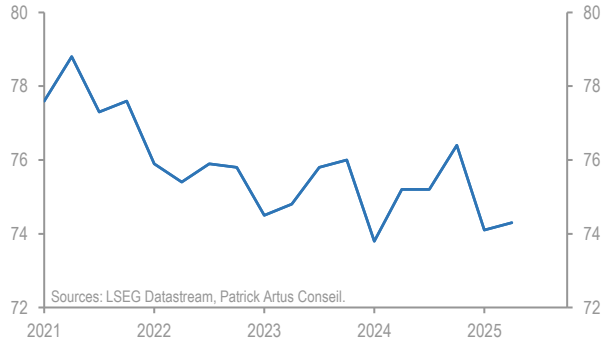
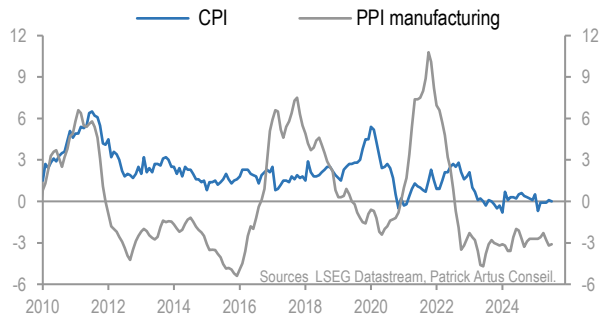


Chart 4
China: Consumer price index and producer price index for manufacturing (Y/Y as %)



We will therefore see strong **growth in China's exports to Europe** (**Chart 5**), with Chinese products replacing European production (for example in steel, electric batteries, electric cars, semiconductors, and so on).

Chart 5
Euro zone: Imports from China (monthly data, in EUR bn)



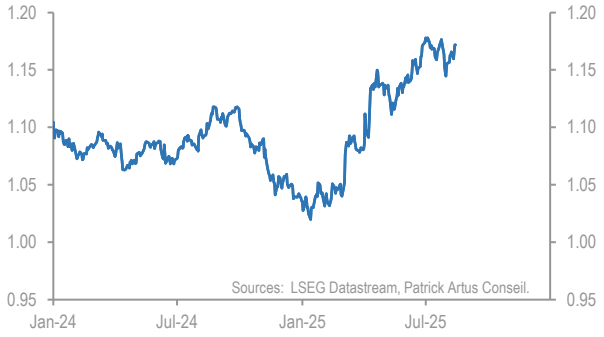
Taxation of Europe's exports to the United States

The European Union's exports to the United States will be taxed at 15% for the majority of goods. Europe's negotiating power is limited:

- It is unrealistic to expect Europe to change its regulation of digital services, its environmental or health rules, or to abolish VAT;
- Europe is highly dependent on the United States for all technological services;
- Europe runs a trade surplus with the United States;
- In reality, Europe has only one lever, which is to increase its imports of LNG (liquefied natural gas) from the United States.

The final tariffs are 15%, which will result in a **cost-competitiveness loss for Europe of nearly 25% compared with the United States, taking into account the depreciation of the dollar against the euro** (**Chart 6**).

Chart 6
Euro/dollar exchange rate (EUR 1 = USD...)



As a result, **Europe's exports to the United States** (Chart 7) **will weaken**, all the more so as energy-intensive industries are encouraged to locate their production in the United States, given the much lower energy prices there compared with Europe (**Chart 8**).

Chart 7
Euro zone: Exports of goods to the United States
(monthly data, in EUR bn)

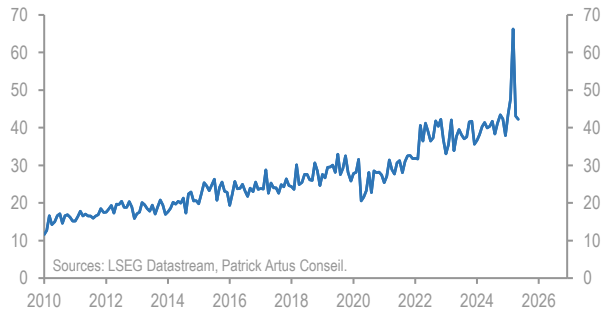
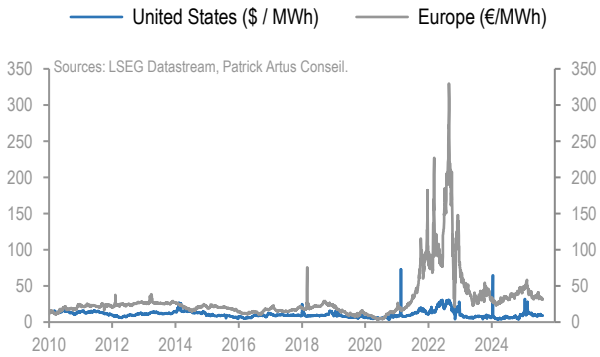


Chart 8
Natural gas price



Summary: Europe's manufacturing output is at risk of weakening

European manufacturing is currently facing several challenges:

- The existence of excess production capacity in China, giving it a strong ability to export to Europe the output produced on this spare capacity;
- High energy prices;
- The tariffs imposed by the Trump administration;
- The depreciation of the dollar.

All these developments point in the same direction: a slowdown in manufacturing activity in Europe.

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