Flash Economics

N° 127
October 16, 2025

Can the dollar collapse and the euro rise sharply?

Most forecasters believe that the dollar will further depreciate significantly versus the euro towards a 1.20-1.25 dollar per euro range by the end of 2026 (compared with 1.16 today). But could there be a collapse in the dollar's exchange rate against the euro?

There are a number of arguments in favour of a sharp depreciation of the dollar against the euro:

- The introduction of a much more expansionary monetary policy in the United States;
- The Federal Reserve's loss of credibility;
- The decline, mainly for political reasons, in foreign exchange reserves held in dollars;
- Weak growth in the United States.

But there are other arguments in favour of a weaker euro against the dollar:

- The dominant and stable role of the dollar in all international currency functions;
- The great weakness of the European economy;
- Europe's technological lag.

All in all, a scenario in which the euro/dollar exchange rate remains roughly stable at current levels seems reasonable.

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Further depreciation of the dollar is expected

Most forecasts for the **dollar's exchange rate against the euro** point to a further depreciation of the dollar (towards an exchange rate against the euro of between 1.20 and 1.25), compared with 1.16 today (**Chart 1**).

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



However, the risk for the European economy would be for the dollar to depreciate significantly, which would further weaken the European Union, and is not necessary to bring down inflation given its current level.

There are a number of arguments in favour of a sharp depreciation of the dollar against the euro

These are:

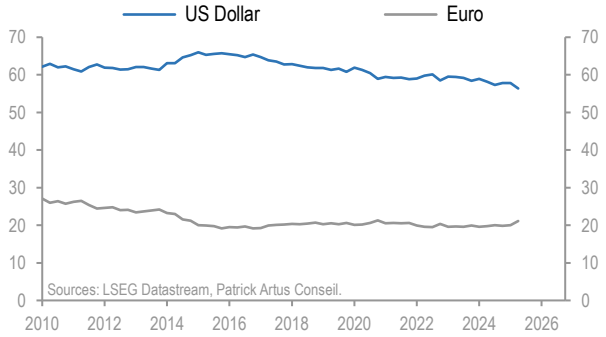
- The introduction of **a much more expansionary monetary policy in the United States**, particularly after the departure of Jerome Powell from the Federal Reserve, which is gradually being anticipated (**Chart 2**);

Chart 2
United States: Eurodollar contracts (3-month)



- **The loss of credibility of the Federal Reserve**, given Donald Trump's desire to control the FOMC, with the intervention of politicians in the decisions of the Central Bank; also given the fact that the US Treasury is essentially being financed in the short term, which casts doubt on the possibility of raising interest rates in the future considering the immediate effect of this increase on interest payments on public debt;
- **The decline in foreign exchange reserves held in dollars** (**Chart 3**), with many countries (Brazil, Russia, China, India, etc.) rejecting the dollar as the dominant reserve currency;

Chart 3
Currency shares in global foreign exchange reserves (as %)



- The weakness of the US economy since the start of 2025 (Charts 4a/4b).

Chart 4A
United States: Real GDP growth (Q/Q annualized, %)

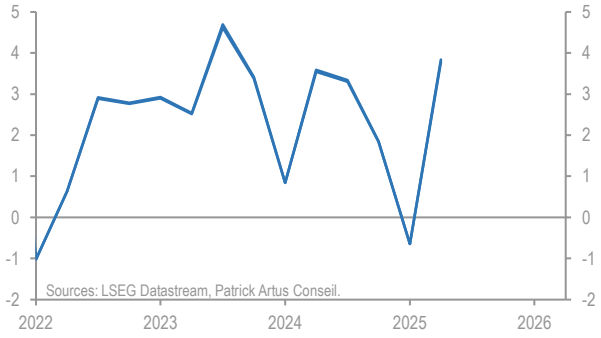
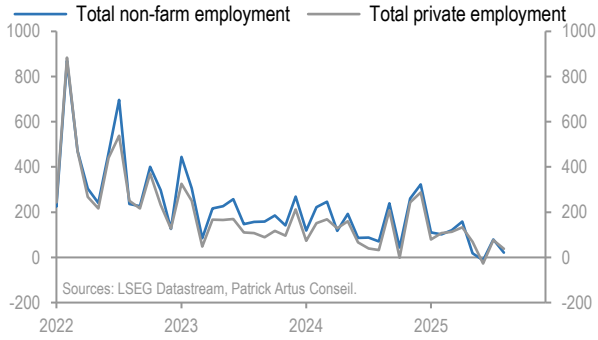


Chart 4B
United States: Change in payroll employment (M/M, thousands of person)



But there are other arguments in favour of a weaker euro against the dollar

1- The dollar's dominant international role

The dollar's share of world foreign exchange reserves has fallen (from 72% in 2001 to 58% today), but the euro's share has also declined (from 31% in 2008 to 20% today), Chart 3.

When considering the other uses of an international currency, we observe that the role of the dollar has increased and become more important, while the weight of the euro has generally decreased:

- In export invoicing, outside America and Europe (Table 1);

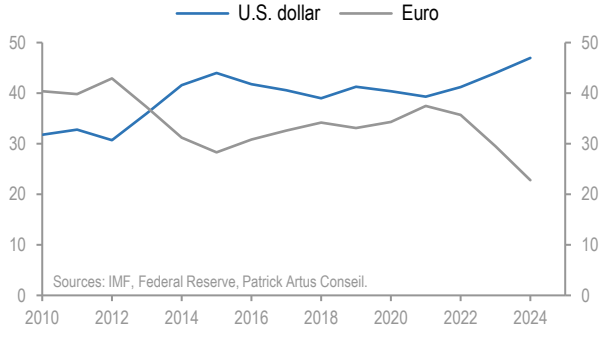
Table 1: Share of export invoicing in US dollar and euro (Annual average from 1999 to 2019, in %)

Currency	Americas	Asia-Pacific	Europe	Rest of World
U.S. dollar	96.3	74	23.1	79.4
Euro	1.6	5	66.1	14

Sources: Federal Reserve, IMF

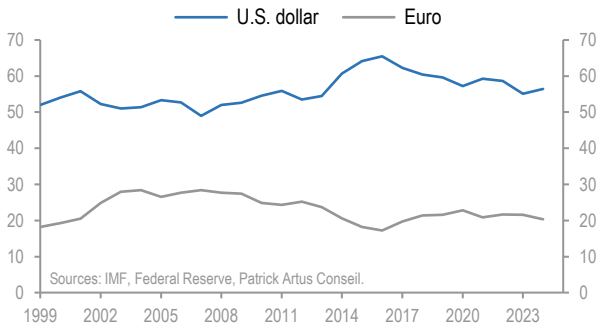
- In international payments (chart 5);

Chart 5
Share of the US dollar and the euro in international payments (in %)



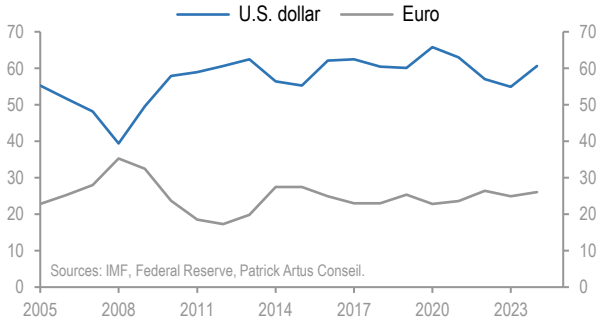
- In banks' international assets in foreign currencies (Chart 6);

Chart 6
Share of international and foreign currency banking claims in US dollar and euro (in %)



- In international debt issuance in foreign currencies (Chart 7) ;

Chart 7
Share of foreign currency debt issuance in US dollar and euro (in %)



- In OTC transactions on the foreign exchange market (Table 2).

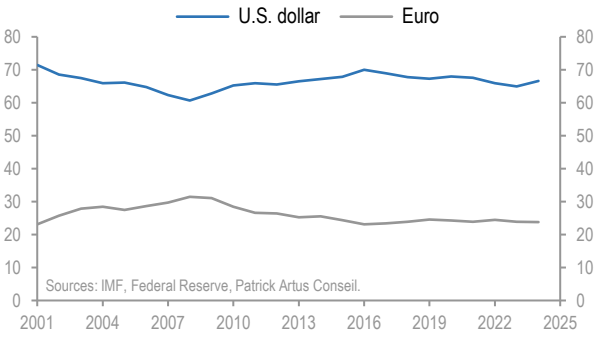
Table 2. Share of over-the-counter foreign exchange transactions in US dollar and euro* (in %)

Year	U.S. dollar	Euro
2001	90	38
2004	88	37
2007	86	37
2010	85	39
2013	87	33
2016	88	31
2019	88	32
2022	88	31
2025	89	29

* Percentages sum to 200 percent because every FX transaction includes two currencies.
Source: BIS Triennial Central Bank Survey of FX and OTC Derivatives Markets

The IMF and the BIS calculate an index of the international use of currencies, which includes all uses (foreign exchange reserves, trade invoicing, international payments, bank claims, international debt issues, foreign exchange market transactions, Chart 8).

Chart 8
Index of international currency usage of US dollar and euro



We can see that 0f0rom 2001 to 2008, the use of the dollar fell and the use of the euro rose, but that since 2008 the opposite has been true, with **a significant decline in the use of the euro and a recovery in the weight of the dollar**.

2- Weakness of the European economy

The second argument against an appreciation of the euro versus the dollar is **the weakness of the European economy** (**Chart 9a**), which is essentially due to the weakness of productivity gains in the euro zone **(Chart 9B**).

Chart 9A
Real GDP (100 = 2002.Q1)

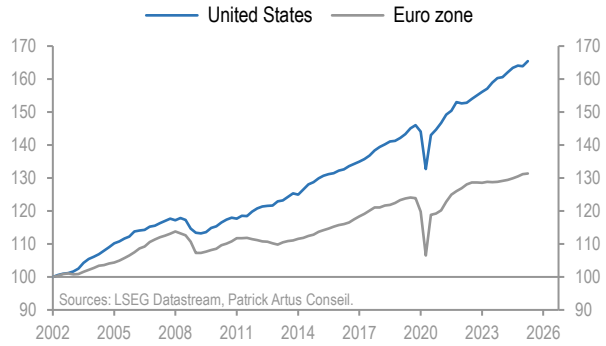
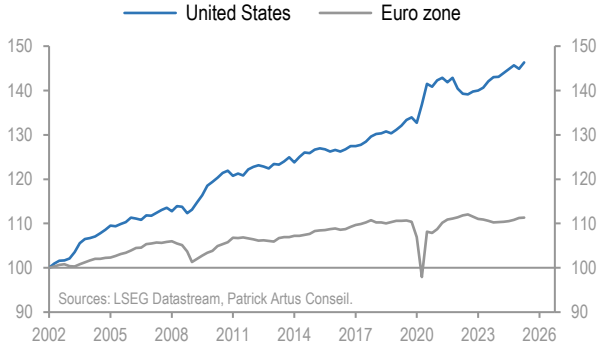


Chart 9B
Productivity per head (2002.Q1 = 100)



This economic weakness makes Europe an unattractive place for capital, which should in principle weaken the euro.

3- Europe's technological lag

A comparison of the level of **R&D spending** (**Chart 10A**) and **the level of investment in new technologies** (**Chart 10B**) clearly shows the extent of Europe's technological lag, which discourages investment flows from the rest of the world to Europe and weakens the euro.

Chart 10A
Total R&D spending (as % of nominal GDP)

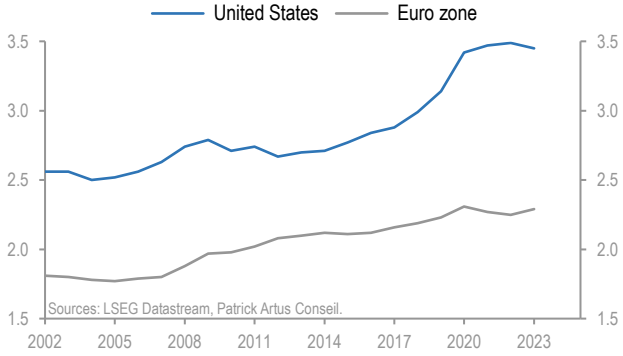
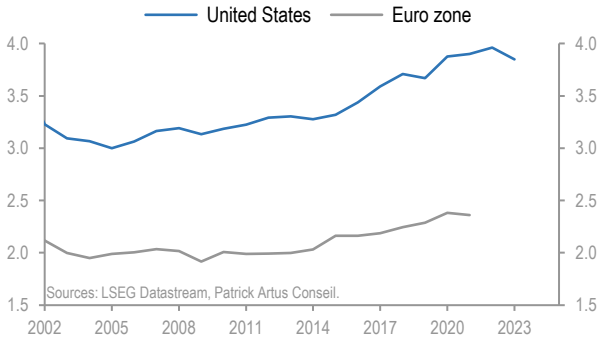


Chart 10B
ICT investment including software (in value terms, as % of nominal GDP)



Summary: The dollar-euro exchange rate is likely to remain fairly stable around the current level

We observe:

- Factors driving the dollar's depreciation against the euro (more expansionary monetary policy in the United States in the future, possible loss of credibility by the Federal Reserve, decline in the dollar's weight in foreign exchange reserves, weaker growth in the United States);
- And factors driving the euro's depreciation against the dollar (dominant and stable role for all uses of an international currency, while the euro's role has been declining since 2008, weakness in the European economy, Europe's technological lag).

Since these factors in opposing directions may offset each other, the most likely scenario is for the euro/dollar exchange rate to remain stable around its current level (1.16).

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