Flash Economics

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The trap is closing in on Europe

Europe is in a very difficult situation:

- With a lack of productivity gains and an ageing population, and therefore structurally weak growth ;
- With its technological underdevelopment, which is encouraging savers to invest in the rest of the world: the investments needed to correct weak growth are not being made;
- With the tariffs introduced by the Trump administration and the postponement of China's exports to Europe and Europe's traditional markets, resulting in weak exports and industrial production.

As we can see, Europe's economy cannot be driven by either domestic demand or exports.

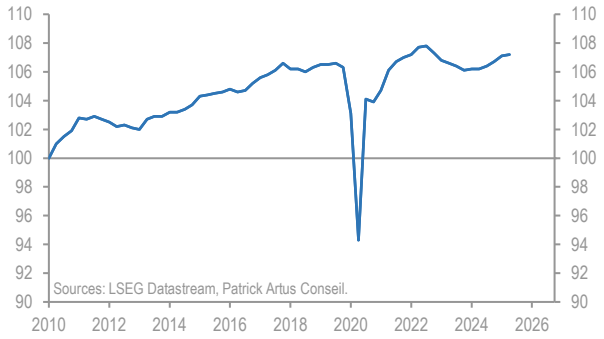
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Europe's first problem: lack of productivity gains and demographic ageing

Let's take a look at the data for the euro zone.
The euro zone has been suffering from **stagnating labour productivity** since 2017 (**Chart 1**).

Chart 1
Euro zone: Productivity per head (2010.Q1 = 100)



It is also suffering from **demographic ageing**, which means that the working-age population is shrinking (**Chart 2**), a trend that is set to accelerate with the increasingly low fertility rate (**Chart 3**).

Chart 2
Euro zone: population aged 15 to 64 (annual growth rate, in %)

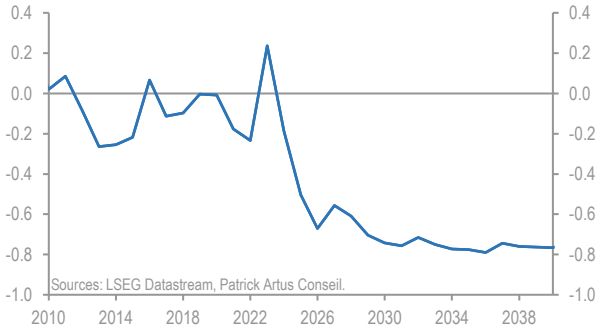
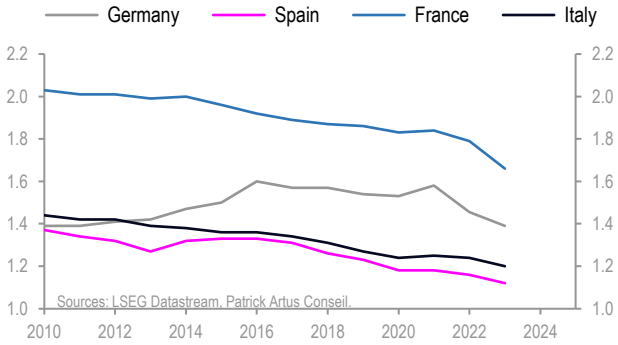


Chart 3
Fertility rate (births per woman)

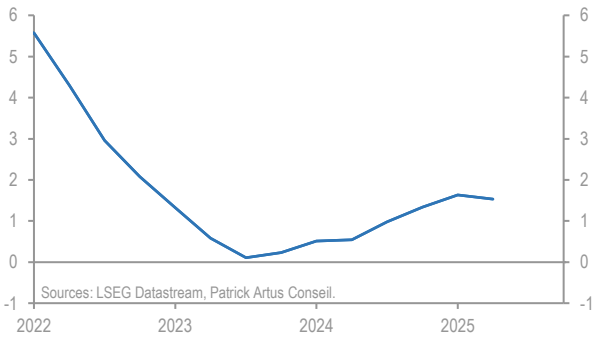


These trends imply that **growth is structurally weak** (**Charts 4A/B**), which is due solely to the rise in the employment rate.

Chart 4A
Euro zone: Real GDP growth (Y/Y as %)



Chart 4B
Euro zone: Real GDP growth (Y/Y as %)

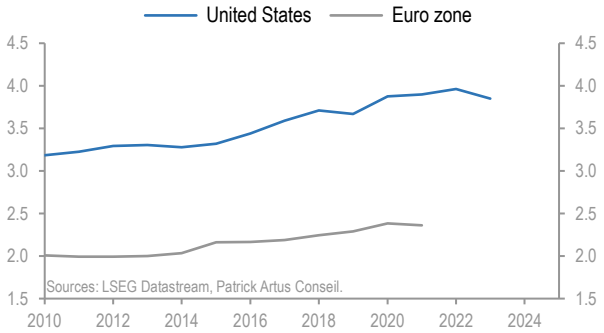


Europe's second problem: technological underdevelopment

When we compare the euro zone with the United States, one can see:

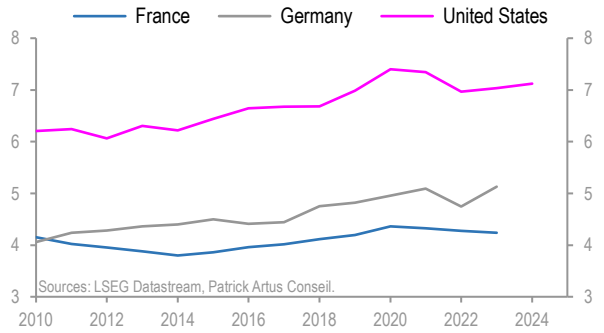
- The low level of investment in new technologies in the euro zone (Chart 5);

Chart 5
ICT investment including software
(in value terms, as % of nominal GDP)



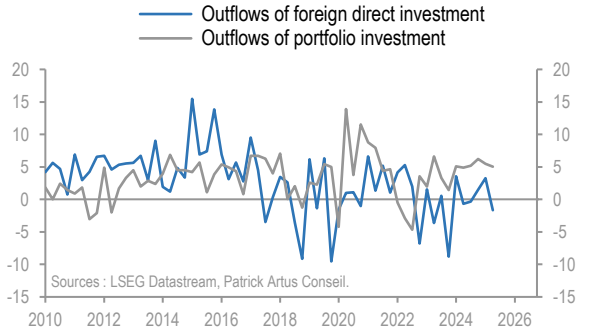
- The small size of the new technology industry (Chart 6).

Chart 6
Gross value added of the ICT sector
(as % of nominal GDP)



This encourages Europeans to invest in the rest of the world (Chart 7), leading to the emergence of a vicious circle: weak technological investment, leading to weak growth and a weak technology sector, leading to an incentive to invest abroad, leading to even weaker technological investment.

Chart 7
Euro zone: Outflows of foreign direct investment and
portfolio investment* (as % of nominal GDP)



(*) Outflows of foreign direct investment and portfolio investment are capital outflows leading to an increase in assets (in this case for the euro zone), and are therefore given a positive sign

Europe's third problem: Tariffs in the United States and the transfer of China's exports to the European market

The imposition of **substantial tariffs in the United States on European products** (15% for all products, except steel and aluminium, for which the tariff is 50%) has led to **a fall in the value of exports of goods from the euro zone to the United States since the start of the 2nd quarter of 2025** (**Chart 8**).

Chart 8
Euro zone: Exports of goods to the United States
(monthly data, in EUR bn)



Furthermore, the existence of overcapacity in China (**Chart 9**) implies **a net increase in exports from China to the euro zone** (**Chart 10**), an increase that is amplified by the fall in prices in China and by the depreciation of the RMB.

Chart 9
China: Capacity utilization for manufacturing (as %)

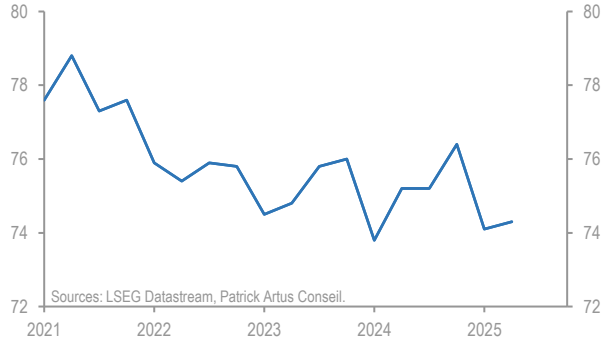
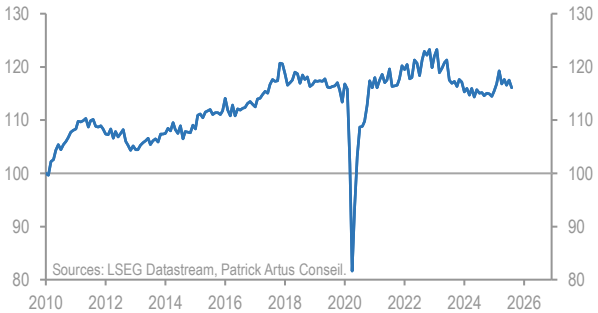


Chart 10
Euro zone: Imports of goods from China
(monthly data, in EUR bn)



These two trends (falling exports to the United States, rising imports from China) will contribute to weak **manufacturing production in the euro zone** (**Chart 11**).

Chart 11
Euro zone : Manufacturing production (2010.M1 = 100)



Summary: growth in the euro zone stimulated neither by domestic demand nor by foreign trade

Growth in Europe:

- Is no longer stimulated by domestic demand (with stagnating productivity, an ageing population and under-investment) ;
- Is no longer stimulated by foreign trade (with tariffs in the United States and competition from China).

As one can see, there is nothing to boost growth in Europe.

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