Flash Economics

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Donald Trump's election could lead to a financial crisis in the eurozone

The election of Donald Trump as President of the United States will lead to a surge in inflation in the United States from 2025 onwards given the tariffs that Donald Trump wants to levy on all US imports and the halt to immigration, which will bring back a strong tension on the labour market[1].

Even if the Federal Reserve does not react to this rise in inflation, it will push up long-term interest rates in the United States and, by contagion, in the eurozone (our estimate of the effect of a 100-basis point rise in the US 10-year interest rate is of a 38-basis point rise in the eurozone 10-year interest rate). A rise of 200-basis points in US long-term interest rates is likely in a scenario where Donald Trump is elected, leading to a rise of 76-basis points in European long-term interest rates, which would push the 10-year interest rate in France and Spain to 3.80%, in Germany to 3% and in Italy to 4.30%, levels that could trigger a public debt crisis in Italy and France.

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(1) The Peterson Institute for International Economics estimates the increase in inflation attributable to such policies at between 4.1 and 7.4 percentage points.

Donald Trump's election is very likely to cause inflation in the United States to rise sharply

Donald Trump's economic programme includes:

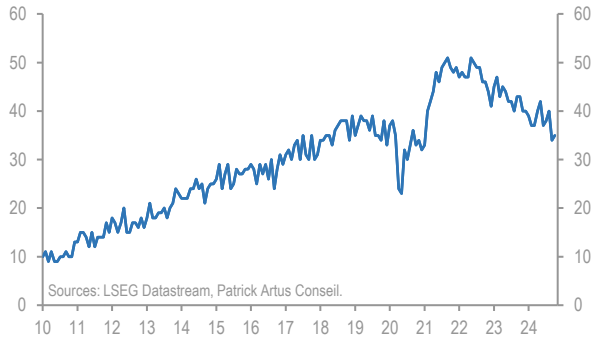
- **a sharp rise in tariffs** not only on products imported from China (with tariffs of 60% on Chinese products and of 100% on Mexican products) but on all US imports (with tariffs of 20% on products imported from countries other than China and Mexico);

- **a halt to immigration**, and even a 'deportation' of immigrants, which would lead to a significant decline in the working-age population **(Chart 1** shows the very high level of immigration to the United States in 2022 and more so in 2023) and **the return of major recruitment difficulties (Chart 2).**

Chart 1
United States: foreign-born population (as % of the total population)



Chart 2
United States: Proportion of companies experiencing recruitment difficulties (as %)

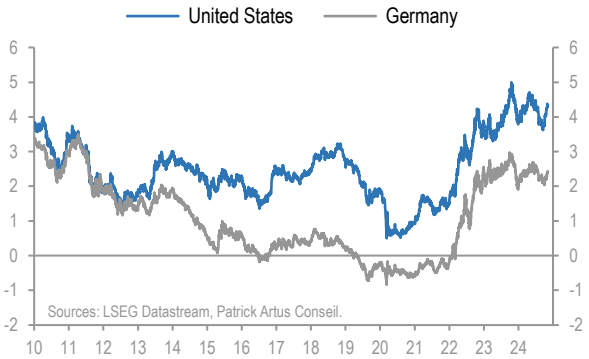


The implementation of these trade and migration policies will lead to a **sharp rise in inflation** (which some estimate at between 4 and 7 percentage points of additional inflation), taking inflation to 7 or 9% over one year.

Effect on interest rates

Assuming that the Federal Reserve does not react to this sharp rise in inflation, it will lead to a **sharp rise in long-term interest rates in the United States and the eurozone (Chart3).**

Chart 3
Interest rate on 10-year government bonds (as %)



One can assume a 200-basis point rise in the 10-year interest rate in the United States, which leads, according to our estimates, to a 76-basis point rise in interest rates in the eurozone, bringing the German 10-year interest rate to 3%, those of France and Spain to 3.80% and that of Italy to 4.3%.

Summary: A public debt crisis, particularly in France and Italy, is a threat to be taken seriously

The election of Donald Trump as US president is very likely to cause inflation and long-term interest rates in the United States to rise sharply, and long-term interest rates in the eurozone to rise sharply too. The level of long-term interest rates in France and Italy is set to rise well above the level of long-term growth, which is likely to trigger a public debt crisis.

The eurozone is therefore threatened by a financial crisis as a result of the US presidential election.

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