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Economist's Weekly Market View

Monday, 14th July 2025

Eurozone outlook clouded by uncertainty

As the Eurozone economy makes the turn for the second half of 2025, the background remains challenging, especially amid the heightened trade tensions between the EU and US. Looking back over the last few years, the Eurozone economy has struggled to generate any sustained growth momentum in the aftermath of the Covid pandemic.

The Russian invasion of Ukraine and the resulting energy price and supply shock were significant drags on the performance of its main economies, especially Germany and Italy. The series of rate hikes from the ECB over the period July'22-Sept'23 to get inflation back down towards its 2% target also acted as a hindrance to growth for the region overall.

In short, the economic recovery in the Eurozone has been muted, with the currency bloc rebounding by less than half the rate of the US economy (the Eurozone is around 5% larger than in Q4 2019, whereas the US is over 12% bigger). Over the two-year horizon 2023-2024, GDP growth for the Eurozone averaged just 0.6%.

It is useful to examine the contribution from the region's 'Big 4' economies as these account for nearly 75% of overall Eurozone GDP. Over this 2-year period, the German economy averaged a minus 0.2% growth rate, France grew on average by around 1%, Italy averaged growth of 0.7%, while the Spanish economy registered a more robust performance, posting a 2-year average growth rate of 3%.

Looking ahead, the outlook for the Eurozone economy remains clouded by the aforementioned trade tensions between the EU and US and elevated global uncertainty. The OECD in its recent Economic Outlook, published in June, noted that "substantial increases in trade barriers, tighter financial conditions, weakened business and consumer confidence and elevated policy uncertainty all pose significant risks" to global growth. This backdrop hampers the growth prospects for the Euro area.

It is not surprising therefore that the consensus is for on-going muted growth for the Eurozone economy. On a positive note, the labour market remains strong, employment is rising with unemployment near its all-time low. These jobs market fundamentals combined with a resumption of the disinflationary trend and less restrictive monetary policy should help to underpin growth in real wages which in-turn will be supportive of the domestic economy.

New government spending initiatives, particularly in relation to Germany should strengthen Eurozone GDP from 2026 onwards also. Clarity on new trading relations or progress towards a new trade framework with the US could see a rebound in external demand, although recent euro strength is an unhelpful development in this regard.

The ECB sees Eurozone GDP at 0.9% this year, a modest improvement from the 0.7% rate recorded in 2024. Thereafter, the central bank is forecasting growth picking up to 1.1% in 2026 and to 1.3% in 2027. Both the OECD and IMF envisage a broadly similar trajectory for the Euro Area. In summary, on-going improvement is anticipated for the Eurozone economy, but the pace of growth is set to remain sluggish.

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