

MARKETING MATERIAL

# ECB PREVIEW

## Rates on hold, increased inflation risk

**The ECB is expected to keep rates unchanged on 19 March, with recent data broadly consistent with its baseline. However, rising energy prices have increased upside risks to inflation, likely prompting a more vigilant communication tone. Against this backdrop, the ECB is also likely to point to scenario analysis in its updated assessment to capture the heightened uncertainty.**

### **Unchanged policy rate, greater vigilance and scenario analysis to capture uncertainty**

The ECB is widely expected to leave policy rates unchanged at its 19 March meeting, with the deposit rate remaining at 2.00%. The decision will be announced on 19 March at 14:15 CET, followed by the press conference at 14:45 CET. In our view, an unchanged decision reflects an economic and inflation backdrop that has evolved broadly in line with the ECB's December projections, although the recent surge in energy prices has increased upside risks to inflation.

Updated staff macroeconomic forecasts will be released at the meeting, but these projections were likely finalised before the latest rise in energy prices and are therefore unlikely to fully reflect the renewed inflationary pressure. However, the ECB may complement its baseline projections with alternative scenarios to better capture the heightened uncertainty.

We expect the ECB to reiterate its familiar message that policy decisions remain data-dependent and will continue to be taken on a meeting-by-meeting basis, without any pre-commitment on the future rate path. At the same time, the Governing Council is likely to adopt a somewhat more vigilant tone, with President Lagarde expected to emphasise that the ECB is closely monitoring developments in the Middle East given their potential implications for energy prices and the inflation outlook.

### **Recent data broadly in line with ECB's December forecasts**

Recent data have provided little reason for the ECB to materially reassess its baseline. Headline inflation stood at 1.9% in February, while core inflation rose to 2.4% and services inflation reached 3.4%, all broadly consistent with the ECB's December expectations. Although services inflation remains elevated, softer-than-expected wage growth should provide some reassurance that underlying domestic inflation pressures are not strengthening materially. Meanwhile, GDP growth of 0.2% Q/Q was also in line with expectations, supporting the view that euro area activity remains relatively weak but stable.

### **Lagarde and other ECB policymakers emphasise uncertainty and volatility**

Recent ECB communication has also pointed to a cautious but somewhat firmer tone in response to geopolitical developments. In an interview with France 2 on Tuesday, 10 March, President Lagarde said that "we will do all that is necessary to ensure that inflation is under control and that the French and Europeans don't suffer the same inflation increases like those we saw in 2022 and 2023". She also stressed that "we won't rush into a decision because there is too much uncertainty, too much volatility". Moreover, she indicated that the ECB is likely to incorporate alternative scenarios into its analysis to better capture the unusually high degree of uncertainty.

Other ECB policymakers have struck a similar tone. Chief Economist Philip Lane noted that a jump in energy prices would put upward pressure on inflation, particularly in the near term, while also weighing on economic activity. He added that the ECB would closely monitor

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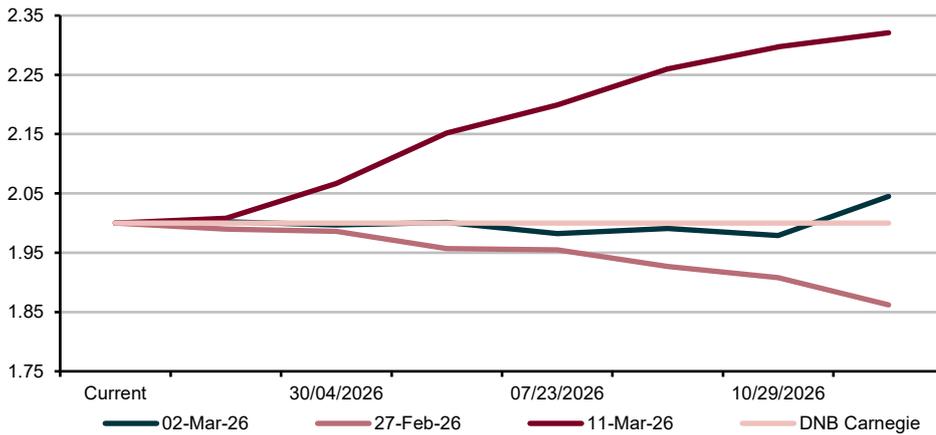
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developments and that the medium-term implications would depend on the breadth and duration of the conflict. Bundesbank President Joachim Nagel struck a somewhat more hawkish note, arguing that the inflationary impact currently appears more pronounced than the effect on growth. By contrast, Finland's Olli Rehn emphasised the importance of keeping a cool head and avoiding overly hasty monetary policy conclusions based solely on immediate market moves.

**ECB deposit rate %, market pricing and DNB Carnegies' forecast**



Source: Bloomberg, DNB Carnegie

Taken together, these comments suggest that while the ECB is not yet ready to alter its policy stance, the Governing Council is becoming increasingly attentive to upside inflation risks.

**Markets now price hikes by year-end, while we still forecast two hikes in early 2027**

Market pricing of the ECB deposit rate has shifted materially since the outbreak of the war in Iran. On 27 February, markets were pricing around 14bp of cumulative cuts by December 2026; they are now pricing around 32bp of hikes. At this meeting, however, markets price virtually no change, indicating that investors also view it as too early for the ECB to move.

Overall, we expect the ECB to keep rates unchanged while acknowledging that inflation risks have become more skewed to the upside due to higher energy prices. Our baseline remains that the next policy move will be a rate hike, with two hikes still pencilled in for the first half of 2027. However, we now see a greater risk that the tightening cycle could begin earlier than previously expected.

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