

Macro Note

Eurozone: ECB stays the course; rate hikes conditional on prolonged energy shock

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- The European Central Bank (ECB) kept all key interest rates unchanged on 19 Mar, extending its pause to a sixth meeting, while reaffirming a neutral, data-dependent stance allowing flexibility amid heightened geopolitical uncertainty.
- The ECB revised inflation forecasts higher—reflecting a temporary energy price shock that is assumed to fade over time—while cutting medium-term growth projections as higher energy costs, second-round inflation effects, and weaker confidence weigh on activity.
- Alternative scenarios show that only a prolonged and severe energy shock would push inflation high enough to warrant a rate hike. While upside inflation risks — especially from energy prices and potential second-round effects — have increased, our base case remains that policy rates stay on hold for now, with hikes contingent on energy prices staying significantly elevated for an extended period.

The ECB decided to keep interest rates unchanged on 19 Mar, marking the sixth meeting that the central bank has kept interest rates on hold. Accordingly, the interest rates on the deposit facility, the main refinancing operations and the marginal lending facility will remain unchanged at 2.00%, 2.15% and 2.40% respectively.

In the accompanying [press release](#), the ECB noted that the conflict in the Middle East has substantially increased uncertainty around the outlook, posing upward risks to inflation and downward risks to growth. It added that the medium-term impact would hinge on how severe and prolonged the conflict becomes, as well as the extent to which energy costs feed through to prices and broader economic activity. Remaining firmly data-dependent, the ECB reiterated its neutral stance, emphasizing that this approach would enable it to calibrate policy appropriately.

At the subsequent [press conference](#), ECB President Christine Lagarde echoed this neutral message, stating that the ECB is “well positioned” to navigate the heightened uncertainty, while underscoring that current conditions differ from the 2022 inflation spike driven by supply chain disruptions and the forceful post-pandemic rebound.

In updated macroeconomic projections, the ECB partly factored in the recent surge in oil and natural gas prices. The new staff forecasts put average inflation at 2.6% this year and 2.0% next year, revised up from 1.9% and 1.8% in the Dec projections. Notably, the inflation profile shows only a modest 0.2 percentage point upward revision to the 2027 forecast, implying an assumption that energy prices will normalize over time. Since late Feb, the Dutch TTF natural gas benchmark has

jumped by roughly 75% to around €61/MWh (at the time of writing), still well below the €200/MWh-plus levels seen at the peak in summer 2022.

Core inflation is now projected at 2.3% in 2026 and 2.2% in 2027, compared with 2.2% and 1.9% previously, reflecting pass-through from higher energy and food prices, with the larger upward revision at the longer horizon likely capturing delayed and potentially stronger second-round effects via wages. On growth, the ECB lowered its growth projections for 2026 and 2027 to 0.9% and 1.3%, respectively, from 1.2% and 1.4%, citing the drag from higher electricity and fuel costs on industrial activity and discretionary consumer spending, alongside weaker consumer and business confidence stemming from the conflict. The ECB noted, however, that these headwinds should be mitigated by low unemployment, resilient private-sector balance sheets, and continued fiscal spending on defence and infrastructure.

Beyond its baseline outlook, the ECB also presented alternative scenarios for the euro area economy based on the duration of the conflict and the persistence of elevated energy prices. These scenarios deliberately exclude any fiscal or monetary policy responses that could mitigate the economic or inflationary effects.

- In an adverse case, the ECB assumes a 40% reduction in oil and gas flows through the Strait of Hormuz during the second quarter – already effectively materializing – with volumes and prices returning to normal from the fourth quarter of 2026. Under the adverse scenario, headline and core inflation are projected to average 3.5% and 2.4% in 2026, and 2.1% and 2.7% in 2027. GDP is expected to expand by just 0.6% in 2026 and 1.2% in 2027.
- In a more severe scenario, shipments are assumed to fall by 60%, with normalisation only beginning in the first quarter of 2027, alongside damage to energy infrastructure. In this scenario, inflation is seen at 4.4% and 2.6% in 2026, rising further to 4.8% and 3.9% in 2027, a setting in which a rate hike would likely be considered. GDP is seen at just 0.4% in 2026, and 0.9% in 2027 under this scenario.

For now, we maintain our view that policy rates will remain on hold. A tightening move would likely only come into play if energy prices remain significantly elevated for a prolonged period, consistent with the ECB's adverse or severe scenario assumptions discussed above. While the ECB continues to emphasise its data-dependent, meeting-by-meeting approach, upside risks to inflation – particularly from energy prices and potential second-round effects – have increased. As a result, the balance of risks has tilted more towards a rate hike than a cut, even though growth risks remain skewed to the downside.

Our Forecast					
%	As of 25 Mar	1Q26	2Q26	3Q26	4Q26
EUR Main Refinancing Rate	2.15	2.15	2.15	2.15	2.15
EUR Marginal Lending Facility Rate	2.40	2.40	2.40	2.40	2.40
EUR Deposit Facility Rate	2.00	2.00	2.00	2.00	2.00
Source: Global Economics & Markets Research					

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