

PREVIEW: ECB Policy Announcement due Thursday, 19th March at 13:15GMT/09:15EDT

- Expected to maintain the Deposit Rate at 2.00%. However, the recent energy shock means the 'good place' assessment is unlikely to hold.
- However, it is too soon to fully assess the inflation/growth impacts of the conflict, and as such the ECB will likely keep optionality open and retain a readiness to act.
- Aside from verbal language, the accompanying projections will likely see a near/medium term lift to inflation and cut to growth. Additionally, an alternative or adverse set of forecasts may be provided.

OVERVIEW: The ECB is expected to maintain the Deposit Rate at 2.00%, however, the recent Middle East driven energy shock means the ECB is unlikely to assess that policy is still in a 'good place'. The main focus for the statement and forecasts will be any signs that the ECB is making a hawkish-tilt to address/acknowledge the inflationary ramifications of the situation; however, the growth impact may negate/supersede this. As a reminder, December 2023 the ECB published a forecast scenario exploring a Middle East escalation, forecasts that saw higher inflation expectations and lower growth forecasts vs the baseline assessment. Thereafter, we look to President Lagarde for further details on the above. A presser that is likely to stress the ECB has optionality and retains a readiness to act, but that in the very near term the approach is to wait and see and gather more information. The press conference commences from 13:45GMT/09:45EDT.

PREVIOUS MEETING: In February, rates were maintained with the Deposit Rate held at 2.00%, as expected. The statement largely stuck to the script, offering little by way of near-term policy signal, sticking to a data-dependent and meeting-by-meeting approach. Overall, the statement stuck to the narrative that the ECB is in a good place for policy. The press conference with President Lagarde offered little else, the main points of note from her revolved around the Euro. As Lagarde outlined that a stronger EUR could weigh on inflation, and while they are keeping an eye on the currency there is no FX target.

MIDDLE EAST SHOCK: The US and Israel action against Iran and the subsequent impact to energy production and supply globally has sparked a marked increase in energy benchmarks, with both WTI and Brent above the USD 100/bbl mark and Dutch TTF eclipsing EUR 60/MWh. Points that have sparked a significant hawkish repricing by the market for 2026. For the ECB, at most, two 25bps hikes were fully priced. As it stands, around 30bps of tightening is implied by end-2026, though a move is not priced until September. Near term, pricing implies around 0bps of activity in March and April, then increasing sharply to 12bps in June.

In brief, the situation currently does not merit tighter policy as the ECB needs further clarity on how long the energy shock lasts, how strong the pass through to inflation is, and what the growth impact of the shock turns out to be. Points that will be the main focus point of the statement, introductory statement and presser from Lagarde; additionally, the updated forecasts, particularly if alternative scenarios are provided, may provide insight on this. Schnabel previewed that the March projections will "partly" reflect the Iran shock while Villeroy outlined that energy costs are only a "minor" part of consumer spending.

Recent ECB speak on the subject has largely seen officials highlight elevated uncertainty given the above, the most pertinent commentary stemmed from Kazimir, who outlined that a hike could be closer than thought, but he stressed that there is no reason to act in March.

DATA: Data releases in recent days and weeks are yet to account for the Middle East situation. Inflation came in at 1.9% Y/Y in February, while Services ticked higher to 3.4% (prev. 3.2%). A series that sparked an incremental hawkish move at the time. Elsewhere, February's PMIs added to the hawkish narrative, with the series showing service sector costs increasing; pertinently, energy factored into the upside even before the Middle East shock.

FORECASTS: In December, the macroeconomic projections were revised up for growth and HICP, the latter primarily due to staff expected services inflation to moderate at a slower pace. On the topic of a potential adverse/alternate scenario set of forecasts, the expectation would be similar to that seen in December 2023 when the ECB published a scenario exploring a Middle East escalation; forecasts that saw higher inflation expectations and lower growth forecasts vs the baseline.

- HICP: 2025 2.1% (Sep. 2.1%), 2026 1.9% (Sep. 1.7%), 2027 1.8% (Sep. 1.9%), 2028 2.0%
- Core-HICP: 2025 2.4% (Sep. 2.4%), 2026 2.2% (Sep. 1.9%), 2027 1.9% (Sep. 1.8%), 2028 2.0%
- Growth: 2025: 1.5% (Sep. 1.2%), 2026 1.2% (Sep. 1.0%), 2027 1.4% (Sep. 1.3%), 2028 1.4%

DESK CALLS:

- Morgan Stanley believes the ECB will now maintain rates through 2026, vs their previous call for 25bps cuts in June and September.
- Goldman Sachs expects rates to be unchanged in 2026. Unless, the world is pushed into a 'very adverse scenario', under which they expect three sequential hikes beginning in June.
- ING expects the ECB to sound more hawkish in its statement, and as such do not expect the "good place" assessment to feature.
- SEB believes the main message is "want and see", maintaining their forecast for unchanged rates across 2026 and 2027.

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