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FLASH REPORT
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ECB Holds With No More Cuts in Sight

- **As widely expected, the ECB kept all its policy settings unchanged in today's decision, leaving the key deposit facility rate at 2.00% for a second consecutive meeting in a unanimous decision.**
- **ECB President Lagarde had a hawkish press conference that saw markets scale back their expectations for additional easing from the ECB, particularly as she said that the "disinflationary process is now over for the euro area."**
- **After today's decision, we are changing our forecast to no more ECB rate cuts over the forecast horizon, from previously projecting one final reduction in late-2025.**
- **The ECB lifted its 2025 GDP growth forecast to 1.2% from 0.9%, with a small negative revision to 2026 at 1% and unchanged at 1.3% for 2027. Small upward revisions to 2025 and 2026 inflation forecasts were offset by a slightly lower 1.9% call for 2027.**

As widely expected, the European Central Bank (ECB) kept all its policy settings unchanged in today's decision, leaving the key deposit facility rate at 2.00% for a second consecutive meeting in a unanimous decision. With the Eurozone economy faring better than expected so far in 2025 together with ongoing stickiness in core inflation, the ECB remains in a wait-and-see stance that suggests another rate cut will likely not be under consideration until late-2025 or early-2026—if at all.

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The ECB's statement struck a relatively neutral tone in line with the July announcement when it halted rate cuts after a six-meeting run of reductions, with cumulative easing of 200bps since June 2024. The decision text mainly differs from the prior meeting's due to a discussion of its quarterly forecast update that include mixed revisions to growth and inflation views (more later) that on balance suggest the ECB is comfortable with its current policy stance.

The decision text spoke to the ECB's new forecasts where GDP growth is now seen growing at 1.2% in 2025, up from 0.9% in the June round, but 2026's expansion is now projected at a smaller 1.0% (from 1.1%), rising to an unchanged 1.3% for 2027. The 2025 revision reflects a better economic performance than expected for the current year, as growth of 0.6% and 0.1% q/q in each of 1Q and 2Q (accompanied by positive revisions to 4Q24) exceeded, on average, the 0.3% and 0.2% expansions for 1Q and 2Q that the ECB's staff had penciled in last quarter.

International trade developments remain the main risk for Eurozone growth in the quarters ahead, as the negotiated 15% U.S. tariff rate on E.U. goods tees up export weakness in the months ahead; ongoing French political uncertainty is an adjacent, albeit smaller, headwind for the bloc's economy. With high tariffs in place (the ECB had previously assumed a 10% level), the net trade drag on GDP growth should become more evident in data over the remainder of 2025 and over 2026, with the added risk of higher tariffs on pharmaceuticals.

However, the ECB cites reduced trade uncertainty as an offsetting factor to the higher-than-expected tariff level, while expecting that growth will strengthen later on thanks to rising real wages and employment, and the tailwind of fiscal outlays (namely in Germany). We believe that the hit from 15% tariffs becoming clearer over late-2025/early-2026 may sow some uncertainty regarding an on-hold stance at the ECB but ultimately fail to push the bank in the direction of additional easing.

Markets initially had a dovish interpretation of the decision, with small declines in European yields and the EUR, due to the ECB's new inflation outlook that implied a lengthier period of slightly undershooting the 2% target. Headline inflation forecasts for 2025 and 2026 were marginally revised higher to 2.1% and 1.7% from 2.0% and 1.6%, respectively, although the bank's staff lowered their projection for 2027 from 2.0% to 1.9%.

The quarterly projection path shows inflation below 2.0% from 1Q26 to 2Q27, compared to 3Q25 to 4Q26 previously, while also having a shallower nadir of 1.6% in 3Q26 versus the 1.4% low for 1Q26 in the June forecast round. The core inflation path was left practically unchanged, with only a small change to 1.8% for 2027 from 1.9%, where stronger assumptions for the EUR just marginally tilted the balance.

ECB President Lagarde had a hawkish press conference that saw markets scale back their expectations for additional easing from the ECB, particularly as she said that the "disinflationary process is now over for the euro area." She also highlighted that a small deviation from the 2% inflation target (as the updated forecasts reflect) in either direction won't always prompt ECB action, suggesting that it would take much larger shifts in expectations for the bank to resume cuts, and she also called out to "more balanced" growth.

Lagarde's hawkishness lifted Eurozone yields across the board, resisting during the presser the pull of U.S. yields which fell on higher than expected jobless claims data, to leave German 2yr yields one or two basis points above pre-statement levels, while markets are at a maximum pricing in toss-up odds of an ECB rate cut at some point next summer (down from ~15bps). Market action has left German 10s unchanged on the day, weighed by a 5bps drop in U.S. 10s. The EUR is outperforming among the major currencies, albeit with a small 0.3–4% rise on the day.