

ECB remains content and very much on hold

The October meeting of the ECB's Governing Council saw the central bank leave interest rates on hold. This was the third successive meeting that the central bank left its official rates unaltered. The deposit and refi rates were maintained at 2.00% and 2.15%, respectively. The 'unchanged rates' outcome was very much in line with market expectations. The last time the ECB eased policy was at its June meeting when it cut rates by 25bps. In total, the central bank has cut rates by 200bps since it started its easing cycle in June 2024. Today's decision to keep policy on hold had "absolute unanimity".

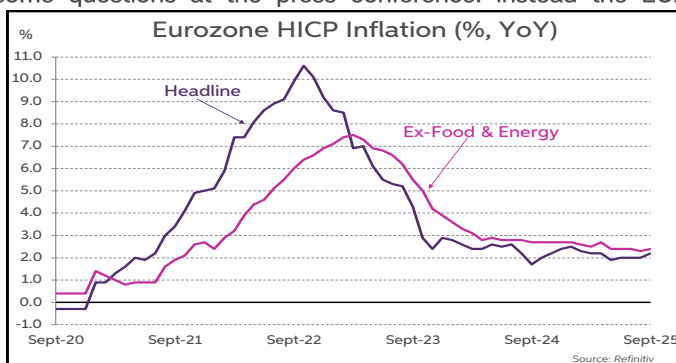
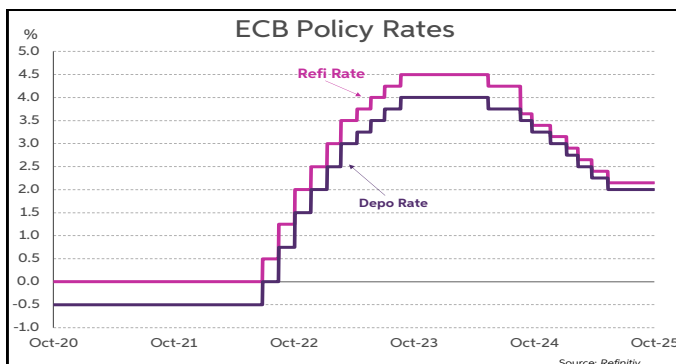
The October meeting statement was similar to its September version. It remained short, and continued to offer little in the way of new guidance. The decision to keep policy on hold was against the backdrop of inflation remaining "close to our 2% medium term target" and the ECB's assessment of the inflation outlook being "broadly unchanged". The ECB also noted that the "economy has continued to grow despite the challenging global environment", while at the same time acknowledging that the outlook remains "uncertain".

The most recent detailed assessment on the economic outlook from the ECB was provided at its September meeting. These forecasts showed no major changes in the ECB's outlook from the June edition. The September update did indicate that the ECB was more optimistic on the near-term growth prospects. It is forecasting Eurozone GDP growth of 1.2% (was 0.9% in June) for this year. It sees GDP averaging 1.0% in 2026 (was 1.1%) and continues to anticipate growth of 1.3% in 2027. These GDP projections continue to embody a subdued growth outlook for the Eurozone economy. Unlike at the September meeting, the ECB did not state that the risks to growth have become more balanced. This generated some questions at the press conference. Instead the ECB highlighted that some of the previous downside risks (EU/US trade tensions, conflict in Middle East and US/China trade tensions) have abated.

In terms of its inflation outlook, the ECB expects headline HICP to average 2.1% (was 2.0%) this year and 1.7% (was 1.6%) in 2026. For 2027, it sees inflation averaging 1.9% (was 2.0%). These projections suggest that the ECB maintains a benign outlook for inflation. In today's statement it commented that the outlook for inflation "continues to be more uncertain than usual on account of the still volatile global trade policy environment".

President Lagarde's press conference remarks suggest that while the ECB retains a willingness to ease policy again, if required, it is satisfied that its current interest rate settings remain appropriate. As a result, it is not contemplating any near term policy changes. She repeated the ECB's mantra that it will follow a "meeting-by-meeting approach" and remains "data-dependent" in determining its interest rate stance. More explicitly, she once again emphasised the ECB's view that "we are still in a good place" and the ECB will do "whatever is needed to make sure we stay in a good place".

Market expectations saw no significant repricing in the aftermath of today's ECB meeting, which is not surprising given the lack of any major new insight from the ECB. At the margin, there has been a modest firming (2-3bps) in futures contracts. The market is now attaching around a 45% probability (was nearer to 50% prior to the meeting) to a 25bps rate cut by mid-2026. Our view since the start of the year has been that the deposit rate will settle at 2%. Today's ECB meeting outcome/tone reinforces our assessment that 2% will represent the trough for the Depo rate.



ECB Macroeconomic Forecasts for the Euro Area

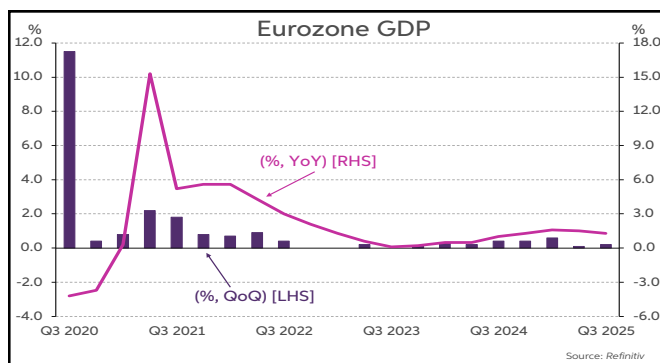
(%)	2024	2025	2026	2027
HICP	2.4	2.1	1.7	1.9
Real GDP	0.8	1.2	1.0	1.3

Forecasts are mid-point of a range and based on the assumption that Brent crude oil prices will average \$69.7 in 2025, \$65.1 in 2026, and \$65.1 in 2027.

Source ECB, September 2025

Moderate growth expected in the Eurozone

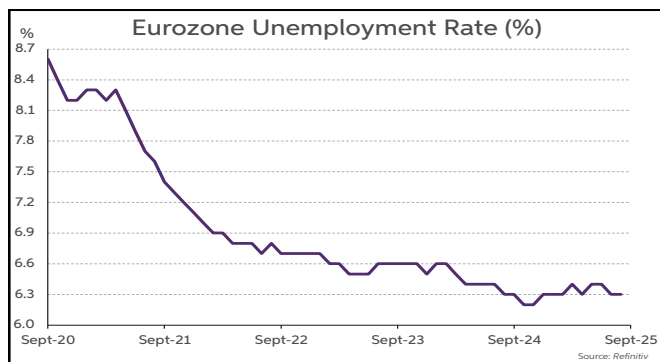
The Eurozone economy gathered some momentum at the start of the year, with GDP rising by 0.6% q/q in Q1, which was the fastest pace of growth since Q2 2022. However, growth slowed sharply to just 0.1% q/q in Q2 of this year, as tariff related front-running unwound. Furthermore, the flash estimate of GDP indicates that the economy expanded by 0.2% q/q in the third quarter. Overall, this would mean that growth in the Eurozone was up by 1.5% y/y in the first three quarters of 2025. The flash estimate of GDP does not contain an expenditure breakdown, but looking at some of the large national economies, Germany and Italy continued to perform poorly (both stagnated in Q3). In contrast, Spain and somewhat surprisingly France, registered robust growth in the quarter, with output rising by 0.6% and 0.5% q/q, respectively.



Meantime, the very limited data available for the fourth quarter suggest that the economy may have gathered some steam. The flash estimates of the manufacturing and services PMIs printed above the consensus in October. The former edged up to the 50.0 no change mark, having registered a slight deterioration (49.8) in September. At the same time, the services PMI jumped to 52.6 in October, its highest level since August 2024. Similarly, the EC economic sentiment indicators improved in October. The improvement was broad based, with the consumer, services and industrial sector indices all rising in the month.

Regarding the labour market, conditions remain solid. Employment expanded for a seventeenth successive quarter in Q2, up by 0.1% q/q and by 0.6% y/y. It means that the number of people at work has risen by 8.4m or 5.1% since the end of Q4 2019. At the same time, the unemployment rate has printed at 6.3% in August and September, just a touch above the all-time low of 6.2% recorded last winter and most recently in July. Despite tight conditions though, wage growth has cooled somewhat. Wages in the Eurozone rose by 3.7% y/y in Q2, up from 3.5% y/y in Q1, but down from 4.7% y/y a year earlier. Furthermore, the Indeed wage tracker - a more frequent measure of wage pressures - indicates that wages have risen more slowly in recent months. It shows that wages rose by 2.8% y/y on average in Q3, down from 3.7% y/y during the same period in 2024.

On the inflation front, a gradual downtrend has emerged this year. The headline rate stood at 2.5% in January, but it declined in the first half of the year, falling to a low of 1.9% in May before edging higher to 2.0% between June and August. More recently, it rose to 2.2% in September, owing to base effects. The month-on-month change in price has remained low, between -0.1% to +0.2% per month since February. Meantime, underlying inflation, which had been quite sticky, stuck between 2.6-2.9% since April '24, has printed at either 2.3% or 2.4% between May-September. This is partly due to a drop in services inflation this year, which stood at 3.1% in September. Looking ahead, the ECB expects inflation to average 2.1% this year, 1.7% in 2026, and 1.9% in 2027. Core inflation is forecast to be 2.4% this year, and 1.9% in 2026-27.



In summary, the Eurozone economy registered an uptick in growth at the start of 2025, albeit growth has moderated in Q2 and Q3. However, the available data suggest activity levels may have gathered steam at the start of Q4. Significant downside risks, such as the political turmoil in France and the changing tariff regime with the US appear to have subsided for now also. At the same time, the labour market remains in good shape. Meanwhile, disinflation and rate cuts in the first half of the year should support real incomes and consumer spending. Higher fiscal spending in Germany, as well as higher defence spending at the EU level could support growth in the medium-term. Proposed changes to the EU budget, may also support economic development in the medium to long-term, although the budget won't come into effect until 2028. For now though, moderate rates of growth are expected to remain the norm in the Eurozone. The IMF sees GDP expanding by 1.2% this year and by 1.1% in 2026.

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