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**Preview: ECB To Take A Pause in July, While
Keeping The Door Open to Further Easing**

By

Brunello Rosa and Nato Balavadze



22 July 2025

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Executive Summary

- ✦ **Expected Decision:** *We expect the ECB to remain on hold in July.* In line with consensus, at the July Governing Council (GC) meeting, we expect the European Central Bank (ECB) to keep its main policy rates i.e. its *i)* interest rate on the ‘main refinancing operations’ at 2.15%; *ii)* interest rate on the ‘marginal lending facility’ at 2.40%; and the key *iii)* ‘deposit facility’ at 2.00%.

The ECB is expected to maintain its data-dependent, meeting-by-meeting approach, reaffirming its three-pronged reaction function. While a September cut remains possible, the ECB is unlikely to pre-commit, while waiting for more clarity on US tariffs and legal outcomes.

- ✦ **Policy Discussion:** *Trump’s threat to raise EU import tariffs to 30% by August 1 has renewed uncertainty over transatlantic trade, leading the ECB to pause its rate-cutting cycle and wait for clearer signals.* Since June 2024, the ECB has cut rates eight times, bringing the deposit rate to 2% as inflation eased to target in June.

The ECB is expected to hold rates steady at its July meeting. Despite Trump’s threats, eurozone data has improved: factory output has risen for four straight months, manufacturing PMI hit a near two-year high, and Q1 growth exceeded expectations. However, further tariffs and a stronger euro—driven in part by Trump’s rhetoric—could weigh on exports and inflation, complicating the ECB’s path.

Officials are closely watching upcoming data, including Thursday’s PMI and Friday’s Ifo index, ahead of the Q2 GDP release on July 30, to gauge whether their June projections remain valid. While Lagarde has indicated the easing cycle is nearing its end, risks such as sticky services inflation, oil price volatility, and U.S. trade tensions remain. Some GC members, like Isabel Schnabel, see the economy as resilient and the bar for more cuts as high, though others warn of stagnation in Q2 and Q3 as early momentum fades. A rate cut remains possible in September, depending on how conditions evolve.

Key Picture: European Central Bank Key Forecasts – 2024-2027

	Latest reading	2025 ^f		2026 ^f		2027 ^f	
		June Projections	March Projections	June Projections	March Projections	June Projections	March Projections
GDP (<i>real growth, y-o-y</i>)	1.5	0.9	0.9	1.1	1.2	1.3	1.3
Inflation (% <i>y-o-y</i>)	2.0	2.0	2.3	1.6	1.9	2.0	2.0
Core-inflation (% <i>y-o-y</i>)	2.3	2.4	2.2	1.9	2.0	1.9	1.9
Unemployment (% <i>y-o-y</i>)	6.3	6.3	6.3	6.3	6.3	6.0	6.2

Source: ECB ‘Macroeconomic projections’ [June](#) and [March](#) 2025 Note: Latest readings: 1. GDP for Q1 2025; 2. Unemployment for May 2025; 3. Inflation for June 2025. *Inflation = Harmonized Index of Consumer Prices (HICP).

Analysis

- ✦ **EXPECTED DECISION:** *We expect, in line with consensus, the ECB to remain on hold in July.* At the Governing Council (GC) meeting on July 24th, we expect the European Central Bank (ECB) to keep its main policy rates i.e. its *i)* interest rate on the ‘main refinancing operations’ at 2.15%; *ii)* interest rate on the ‘marginal lending facility’ at 2.40%; and the key *iii)* ‘deposit facility’ at 2.00%.

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In terms of *forward guidance*, the ECB will stress that it remains data-dependent and the decisions will be still taken meeting-by-meeting, with its usual three-pronged approach about its reaction function confirmed. Looking ahead, the ECB is expected adopt a cautious, data-dependent approach. While a further cut in September remains possible, the Governing Council is likely to wait for more clarity on US tariff developments and related court rulings before committing.

In terms of *Balance Sheet policies*, the GC has decided to move forward with the normalization of the balance sheet. GC confirmed that it will reduce the Eurosystem’s holdings of securities under the PEPP. As of December 2024, the ECB has stopped re-investing the PEPP proceedings. The process for reducing PEPP holdings will generally follow the same approach as the APP.

- ✦ **POLICY DISCUSSION:** *Trump’s threat to raise EU import tariffs to 30% by August 1 has cast fresh uncertainty over transatlantic trade, prompting the ECB to pause rate cuts and await clarity.* Since June 2024, the ECB has cut rates eight times, bringing the benchmark to 2% as inflation cooled from 2022 highs and hit the 2% target in June. Traders continue to expect one more ECB rate cut, with market participants are split between September and December.

The ECB is expected hold rates steady at its upcoming meeting. Despite Trump’s threats, eurozone indicators have improved, factory output has grown for four consecutive months and manufacturing PMI hit a near two-year high. The economy also expanded more than expected. However, further tariffs could reverse recent gains. A stronger euro, partly driven by Trump’s Fed attacks and trade rhetoric, complicates the ECB’s path by risking lower inflation and weaker exports. The euro has gained about 15% against the dollar this year and 2% since the June meeting alone, raising concerns about undershooting the target. Though the ECB typically avoids commenting on exchange rates, recent remarks, including Vice President de Guindos calling levels above 1.20 “tricky”, signal growing unease.

ECB officials say future rate cuts remain likely but depend on developments, making a “wait-and-see” stance the most probable outcome for now, with the next potential move in September. Thus, ECB officials are closely watching upcoming data for signs of how the eurozone is weathering Trump’s tariff threats and broader geopolitical risks. Key indicators, such as Thursday’s PMI survey and Friday’s Ifo index, will offer insight ahead of the official Q2 GDP release on July 30, shedding light on the impact of Trump’s trade threats and whether the ECB’s June projections still hold. While Q1 growth surprised on the upside, ECB Vice President de Guindos expects growth to be nearly flat in Q2 and Q3 as early gains fade.

ECB President Lagarde has signaled the easing cycle is nearing its end, though signs of economic weakness could keep further cuts on the table. External risks—such as stubborn services inflation, volatile oil prices from Middle East tensions, and possible U.S. tariffs—could disrupt the disinflation trend. The ECB estimates a 20% tariff war with EU retaliation could keep inflation below target through 2027. Cheap Chinese exports may add to disinflation, though the effect is less clear if EU countermeasures hit services. Meanwhile, Germany’s large fiscal stimulus could push inflation up. However, policymakers remain divided: Italy’s Panetta urges continued easing if trade tensions drag on prices, while Germany’s Schnabel, who sees the economy as resilient, says another cut would require a “very high” bar.

- ✦ **ECONOMIC ANALYSIS:** *The Eurozone economy grew by 0.6% in Q1 2025 that is double the initial estimate and the strongest pace since Q3 2022.* The reading was boosted by Ireland's 9.7% surge and an upward revision in Germany's performance. Although Ireland accounts for just 4% of eurozone GDP, it contributed roughly half of Q1's 0.6% growth, largely due to strong pharma output and inflated figures from tax-driven accounting by foreign multinationals. Licensing revenues tied to intellectual property are booked in Ireland, boosting its GDP artificially, even though the income is often shifted abroad and doesn't reflect real domestic activity.

Among major economies, Spain grew 0.6%, Germany 0.4%, Italy 0.3%, while France and the Netherlands saw modest 0.1% gains. Fixed investment rose sharply by 1.8% (up from 0.7%), household consumption edged up 0.2% (down from 0.5%), and government spending was flat. Net trade added 0.1 percentage points to GDP, while inventories subtracted 0.1.

Real GDP growth is forecast at 0.9% in 2025. 2025 outlook combines a strong Q1 with weaker expected growth ahead. While trade uncertainty may dampen investment and exports in the near term, increased public investment, rising real incomes, and strong labor markets are set to support medium-term growth and resilience. Recent heatwaves could cut Europe's 2025 GDP by up to 0.5 points, with losses ranging from 0.1 points in Germany to 1.4 in Spain. Regarding Trump's recent threats to impose 30% tariffs on EU imports from August 1, it could trim Eurozone GDP growth by up to 0.3 percentage points annually over the next two years. The impact varies by assumptions around key sectors like pharma and autos, and hinges on how much tariffs dent confidence and investment. The EU is expected to respond with limited countermeasures; its delay in retaliation signals hope for a deal before the August 1 deadline.

Eurozone inflation edged up to 2% in June, matching the ECB's target, according to Eurostat flash data. Core inflation held steady at 2.3%, while services inflation rose to 3.3% up from May's three-year low of 3.2%. National data showed mixed trends: Germany's inflation eased, France and Spain saw slight increases, and Italy remained flat—pointing to a stable euro area average. The figures reinforced expectations that the ECB will hold rates steady in July, with a likely 25-basis-point cut in September. The euro rose 0.3% against the dollar following the release. ECB Chief Economist Philip Lane said the current phase of inflation-fighting policy is likely complete.

- ✦ **MARKET IMPLICATIONS:** *The pause is widely expected, so little market reaction should we expected about that.* All the attention of market participants will be focused on the press conference, to understand if Ms Lagarde will provide signals regarding the ECB's intentions in September. Any indication about a likely cut in September would prompt a "dovish" market reaction, with lower short- and long-term yields, weaker EUR and higher equity prices.

To put things into context, *In the bond market*, German curve steepened as investors focused on fiscal spending. Since the last meeting on June 5 and as of July 21 the yields on a: i) 10y German bund increased by 3 bps to around 2.62% (+125bps y-t-d); and ii) 2y German bund edged down by 5 bps to 1.82% (-26 bps y-t-d). In the periphery of the Eurozone, the 10y Italian bonds decreased by 16 bps and trades around 3.49% since the last meeting. The gap between Germany and Italy's 10Y yields fell to 87 bps. *In the currency space*, since last meeting in June and as of July 21, EUR/USD rose by 1.9% to around 1.17 (+5.6% y-t-d). The euro has strengthened notably against the dollar, driven in part by uncertainty over President Trump's tariff policies. However, this trend should be viewed within the broader context of a weakening U.S. dollar. *In the equity space*, European stocks show mixed performance, as investors awaited developments in U.S.-EU trade talks. The Eurostoxx 500 fell by 1.4% since the last meeting in June to 5333,95 as of July 21 (+8.5% y-t-d).

✦ **MACROECONOMIC ANALYSIS (APPENDIX):** *The Eurozone GDP growth grew in Q1, marking the strongest expansion since Q3-2022.* In Q1-2025, the eurozone GDP expanded by 0.6% q-o-q (c: 0.4%; p: 0.3%). On an annual basis, GDP advanced by 1.5% (c: 1.2%; p: 1.2%). Among the largest economies in the bloc, German economy advanced by 0.4% q-o-q (p: -0.2%). France's GDP advanced marginally by 0.1% q-o-q (p: -0.1%). Italian economy also expanded by 0.3% q-o-q (p: 0.2%).

Private sector activity marked the strongest expansion in three months. In June, the HCOB Eurozone Composite PMI rose to 50.6 (c: 50.7). Services PMI also decreased to 50.5 (c: 50.0; p: 49.7). Manufacturing PMI increased to 49.5 (c: 49.4; p: 49.4).

Eurozone unemployment ticks up modestly. In May, unemployment rate edged up to 6.3% (c: 6.2%; p: 6.2%). The number of unemployed increased by 54K to 10.83mn. Amongst the largest Euro Area economies: i) the unemployment in Italy increased to 6.5% (p: 6.1%) in March; ii) the unemployment rate edged up to 7.4% (p: 7.2%) in Q1 in France; and iii) in Germany the seasonally adjusted jobless rate held steady at 6.3% (p: 6.3%) in June. The 'youth unemployment rate' – measuring job-seekers under 25 years old – increased to 14.4% (c: 14.3%) in May. Wages and salaries in the EZ rose by 3.4% y-o-y (p: 4.1%) in Q1-2025.

Eurozone inflation rise to ECB's target. In June, final estimates showed that: i) headline inflation rose to 2.0% y-o-y (c: 2.0%; p: 1.9%); and ii) core inflation – which excludes food and energy prices – stood at 2.3% y-o-y (c: 2.3%; p: 2.3%). In Germany, annual CPI inflation eased off to 2.0% y-o-y (c: 2.1%). In France, the inflation rate rose to 1.0% y-o-y (c: 0.9%; p: 0.7%). In Italy prices inflation rose to 1.7% (c: 1.7%; p: 1.6%).



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