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**Preview: ECB To Keep Rates Unchanged in April,
While Awaiting More Data on the War's Economic Impact**

By

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24 April 2026

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Executive Summary

➤ **Expected Decision:** *We expect the ECB to remain on hold in April.* In line with consensus, at the April 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.

Financial markets expect at least 50bps of ECB tightening this year, taking rates to around 2.5%, but policymakers remain uncertain about the scale and persistence of inflation pressures. The base case is a hold at the upcoming meeting, with a potential "insurance" hike in June, if data were to confirm the risk of a de-anchoring of inflation expectations. The ECB expects an initial, energy-driven inflation wave, starting with fuel and feeding into transport, food, and industrial prices, but if it remains temporary, it would not warrant immediate tightening.

➤ **Policy Discussion:** *Christine Lagarde signalled that the European Central Bank is not ready to draw firm policy conclusions, stressing the need for more data as the impact of the Iran war remains uncertain and second-round inflation effects have yet to materialise.* As a result, an April rate hike looks unlikely, with markets instead leaning toward a move in June, while policymakers deliberately keep all options open. More broadly, ECB officials at the IMF Spring Meetings converged on two messages: no urgency to hike now, but full optionality going forward—ranging from potential cuts if growth weakens to further tightening if inflation proves persistent. The Bank has shifted back to a reactive, data-dependent, meeting-by-meeting approach, focusing on inflation, expectations, and wages against a backdrop of slowing growth.

The policy trade-off is increasingly complex. Higher energy prices risk lifting inflation, but are simultaneously squeezing incomes and dampening demand, limiting pass-through. Unlike 2022, inflation pressures may be more contained due to weaker consumption, while growth risks are more pronounced. At the same time, the ECB starts from a stronger position, with rates already at neutral and liquidity tightening.

Martins Kazaks, Latvia's Central Bank Governor, captures the current environment as a "layer cake" of shocks—overlapping crises that can interact in non-linear ways. For now, core inflation remains stable, but policymakers are watching closely for spillovers and stand ready to act if second-round effects emerge.

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

| | Latest reading | 2025f | | 2026f | | 2027f | | 2028f | |
|----------------------------|----------------|-------------------|----------------------|-------------------|----------------------|-------------------|----------------------|-------------------|----------------------|
| | | March Projections | December Projections | March Projections | December Projections | March Projections | December Projections | March Projections | December Projections |
| GDP (real growth, y-o-y) | 1.2 | 1.5 | 1.4 | 0.9 | 1.2 | 1.3 | 1.4 | 1.4 | 1.4 |
| Inflation (% , y-o-y) | 2.6 | 2.1 | 2.1 | 2.6 | 1.9 | 2.0 | 1.8 | 2.1 | 2.0 |
| Core-inflation (% , y-o-y) | 2.3 | 2.4 | 2.4 | 2.3 | 2.4 | 2.2 | 1.9 | 2.1 | 2.0 |
| Unemployment (% , y-o-y) | 6.2 | 6.3 | 6.3 | 6.3 | 6.2 | 6.3 | 6.1 | 6.2 | 5.9 |

Source: ECB 'Macroeconomic projections' December and September 2025 Note: Latest readings: 1. GDP for Q4 2025; 2. Unemployment for February 2026; 3. Inflation for March 2026. *Inflation = Harmonized Index of Consumer Prices (HICP).

Analysis

- ✦ **EXPECTED DECISION:** *We expect, in line with consensus, the ECB to remain on hold in April.* At the Governing Council (GC) meeting on April 30th, 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%.

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.

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.

Financial markets expect at least 50bps of ECB tightening this year, taking rates to around 2.5%, but policymakers remain uncertain about the scale and persistence of inflation pressures. Markets are pricing a pause in April followed by a likely hike in June.

- ✦ **POLICY DISCUSSION:** *Lagarde signalled that the ECB is not ready to draw firm policy conclusions, stressing the need for more data as the impact of the Iran war remains uncertain.* The ECB now faces a delicate balance: memories of the 2022 inflation shock could accelerate wage and price-setting, but higher energy costs are also squeezing incomes and dampening demand. Markets expect a pause in April, followed by hikes starting in June, but officials are deliberately keeping all options open.

At the IMF Spring Meetings, ECB officials broadly converged on two points: there is no case for an April rate hike, and policy optionality is back, ranging from potential cuts if the economy weakens to the possibility that further hikes could still be justified. With the Middle East war driving energy prices higher, the ECB has shifted back into a more reactive, “data-dependent” mode, focusing on inflation, expectations, and wages against a backdrop of slowing growth. However, limited new data ahead of the next meeting makes a near-term policy shift unlikely.

While energy prices have surged, policymakers see no clear evidence yet of second-round inflation effects, key for justifying a rate hike, making an April move unlikely. Lagarde noted that the shock has not yet reached the ECB’s adverse scenario, with mixed energy dynamics (higher oil, softer gas) and limited supply chain disruption so far.

While memories of 2022, when the ECB reacted too slowly to inflation, linger, today’s context is different. Inflation pressures from energy are likely to be more muted due to weaker consumer demand, while growth risks are more pronounced. Crucially, unlike 2022, policy is no longer highly accommodative: rates are already at neutral and liquidity is tightening, giving the ECB a stronger starting position.

Martins Kazaks, governor of central bank of Latvia, described the current environment as a “layer cake” of shocks, where overlapping crises can interact in unpredictable ways and trigger broader inflation dynamics. He stressed that the European Central Bank is proceeding meeting-by-meeting, watching closely for signs that price pressures are spilling over, though core inflation has remained stable so far.

- ✦ **ECONOMIC ANALYSIS:** *Christine Lagarde warned that the Middle East war has made the outlook more uncertain, raising the risk that inflation could exceed current projections while dragging on eurozone growth.* She noted that higher energy prices are likely to feed into inflation in the near term, compounding pressures already in place. Despite this, the ECB is not rushing into action. Policymakers remain cautious, sticking to a data-dependent approach and avoiding any firm signals on the rate path. Markets,

meanwhile, have largely ruled out a move in April but still expect a rate hike around mid-year, with another potentially following by the end of the year.

Eurozone growth ended 2025 on a softer note, with GDP rising just 0.2% in Q4, revised down from 0.3% and slightly weaker than the previous quarter, pointing to only modest momentum despite easing inflation and lower interest rates. The economy has remained resilient, but still faces headwinds, including US tariffs on EU imports. Household consumption provided some support, accelerating to 0.4% from 0.2% in Q3. However, other components lost pace: fixed investment slowed sharply to 0.6% (from 1.3%), and public spending eased to 0.5% (from 0.7%). Both inventories and net trade weighed on growth, each subtracting 0.1 pp.

Eurozone business activity unexpectedly contracted in April as the Middle East conflict drove up costs and weakened demand, according to PMI data. The composite index fell to 48.6 from 50.7, slipping into contraction territory, with a sharp drop in services offsetting a modest improvement in manufacturing. Rising fuel prices pushed input costs to their highest levels since 2022, intensifying inflation pressures and complicating the policy outlook. The data point to a growing trade-off for the ECB: whether to tighten policy to contain inflation or support an economy increasingly at risk of slowdown.

✦ **MARKET IMPLICATIONS:** *If on hold, the market reaction should be muted.* All market action should be driven by the press conference, depending how decisive Lagarde will sound on the direction to take in June. But the reality is that Lagarde will likely keep all options open for June, as a longer ceasefire, let alone a full-fledged peace deal in the Middle East, would allow the ECB to look through this past shock, however severe, and however persistent may be the damages to the energy facilities in the Middle East.

To put things into context, *In the bond market*, German bund yields increase on renewed inflation fears. Since the last meeting on March 19 and as of April 23 the yields on a: *i*) 10y German bund rose by 8 bps to around 3.03% (+17 bps y-t-d); and *ii*) 2y German bund increased by 1 bps to 2.57% (+45 bps y-t-d). In the periphery of the Eurozone, the 10y Italian bonds rose by 4 bps to 3.83% since the last meeting. The gap between Germany and Italy's 10Y yields is at around 80 bps. *In the currency space*, the euro risers on Middle East ceasefire optimistic. Since last meeting in March and as of April 23, EUR/USD increased by 1.0% to around 1.17 (-0.4% y-t-d). *In the equity space*, European stocks fell for a third straight session as Middle East tensions continued to weigh on sentiment, with a fragile US-Iran truce and disruptions in the Strait of Hormuz keeping oil prices elevated. The STOXX 600 slipped 0.4%, alongside declines in major indices such as Germany's DAX and France's CAC 40, while rising energy costs also pushed bond yields higher and dampened growth expectations. The Eurostoxx 50 rose by 4.4% since the last meeting in March to around 5861 as of March 19 (+0.2% y-t-d).

✦ **MACROECONOMIC ANALYSIS (APPENDIX):** *The eurozone closed 2025 with solid growth despite weak exports and escalating U.S. trade tensions.* Q4-2025, the eurozone GDP advanced by 0.2% q-o-q (c: 0.3%; p: 0.3%). Spain led growth with its strongest quarter in a year (0.8%), expanding faster than expected on strong household consumption and investment. The Netherlands grew 0.5% on export strength, while Germany and Italy each posted 0.3%, both beating forecasts. France grew 0.2% as expected, its weakest quarterly pace since Q1 2025. Eurozone GDP rose 1.3% y-o-y (c: 1.2%; p: 1.4%, above the 1.2% forecast). For 2025, growth reached 1.4%, just below earlier estimates of 1.5%, but accelerating from 0.9% in 2024.

Leading indicators point to the sharpest contraction in private sector since November 2024. In April, the HCOB Eurozone Composite PMI fell to 48.6 (c: 50.2; p: 50.7). Services PMI decreased to 47.4 (p: 50.2). Manufacturing PMI rose to 52.2 (c: 50.8; p: 51.6).

Eurozone unemployment rises slightly. In February, unemployment rate edged up to 6.2% (c: 6.1%; p: 6.1%). The number of unemployed increased by 93K to 10.92mn. Amongst the largest Euro Area economies: *i)* the unemployment declined to 5.2% in February in Italy; *ii)* the unemployment rate rose to 7.9% (c: 7.7%) in Q4 in France; and *iii)* in Germany the seasonally adjusted jobless rate held steady at 6.3% (p: 6.3%) in March. The 'youth unemployment rate' – measuring job-seekers under 25 years old – was at 14.9% in February (p: 14.9%). Wages and salaries in the EZ eased to by 3.0% y-o-y (p: 3.2%) in Q4-2025.

Inflation rises to the highest level since July 2024. In March: *i)* headline inflation rose to 2.6% y-o-y (c: 2.5%; p: 1.9%); and *ii)* core inflation – which excludes food and energy prices – cooled to 2.3% y-o-y (c: 2.3%; p: 2.4%). In Germany, annual CPI inflation increased to 2.7% y-o-y (c: 2.7%; p: 1.9%). In France, the inflation rate rose to 1.7% y-o-y (c: 1.7%; p: 0.9%). In Italy prices inflation increased to 1.7% y-o-y (p: 1.5%).



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