Article | 6 March 2025

ECB cuts rates but the door to further cuts is closing quickly

After today's 25bp rate cut, we expect the ECB to pause at the next meeting and to cut only one more time before the summer

ECB President Christine Lagarde at today's press conference following the Governing Council meeting

The reasons for today's rate cut decision were clear: at 2.75%, the deposit rate was still too restrictive for a eurozone economy showing signs of bottoming out but not yet recovering. And with looming US tariffs on European goods and high geopolitical uncertainty, as well as falling headline inflation, the decision to cut interest rates again was a no-brainer.

The big story for today, however, was not whether or not to cut but rather what will be next for the ECB. Here, the ECB delivered the expected change in its official communication, no longer labelling the current monetary policy stance 'restrictive' but instead 'meaningfully less restrictive'. A clear signal that the ECB considers the new level of interest rates approaching neutral territory but doesn't want to close the door to further cuts.

During the press conference, President Christine Lagarde didn't tire of emphasising the high level of uncertainty but also didn't say that the ECB's path to bringing rates to neutral was over. Lagarde also stated that today's decision was taken by consensus as one ECB member abstained. Surprisingly, Lagarde singled out this one Governing Council member: the Austrian Robert

Holzmann.

The direction of travel no longer that clear

An important basis for today's policy decision was already outdated when the ECB's Governing Council discussed it: the latest staff projections. Due to their cut-off date two weeks ago, these staff projections have not taken into account the events of the last few days. Neither the discussion to increase defence spending nor the announcement in Germany of a €500bn infrastructure fund, in addition to planned changes to the debt brake, will have been covered in the projections. But for the sake of completeness, ECB staff expect GDP growth to come in at 0.9% for 2025, 1.2% for 2026 and 1.3% for 2027, with downward revisions for 2025 and 2026. At the same time, it sees inflation coming in at 2.3% in 2025, 1.9% in 2026 and 2.0%.

However, looking ahead, it will be exactly this German investment boost as well as Europe's efforts to increase defence spending, not forgetting US tariffs, that will affect the ECB's way forward. Lagarde suggested that the current rate cut cycle was not over but became a bit more uncertain over the course of the press conference as she didn't want to confirm her earlier statement that 'the direction of travel was clear'.

What a difference a few days can make

Lagarde's wiggling around simply shows that the developments of the last few days will have triggered an even more heated debate between doves and hawks on whether or not more rate cuts are needed. If eurozone governments do indeed take over the baton and big fiscal stimulus is coming, the ECB will no longer need to do the heavy work to support eurozone growth. Instead, a more optimistic growth outlook on the back of German infrastructure and European defence spending will allow the ECB to stop the current rate cut cycle earlier than we anticipated. At the same time, however, let's not forget that rising bond yields are also more restrictive, increasing costs for private sector investments - a typical example of crowding out.

With the increased uncertainty and the prospects of large fiscal stimulus, the ECB's direction of travel after today's rate cut is no longer as clear as it was a few weeks ago. A pause at the next meeting to come to terms with the new macro reality now looks realistic. At the same time, if most of the fiscal stimulus is delivered, there will no longer be the need for the ECB to bring rates into slightly accommodative territory. Instead, we see the ECB pausing at the April meeting and cutting the deposit rate one more time to 2.25% in the summer, our new terminal rate. Of course, this is assuming there are no political setbacks in Germany. However, even if the need for further rate cuts fades, the ECB won't be off the hook. Rising bond yields on the back of higher government debt could bring another theme to the eurozone soon: yield curve control.

Another week of historical events in Europe is not over, yet, but it looks as if the ECB also needs some time to come to terms with everything that has happened. A lot seems to have changed for Europe, and the ECB, in just a few days.

Author

Carsten Brzeski
Global Head of Macro
carsten.brzeski@ing.de

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("**ING**") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies).* The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Additional information is available on request. For more information about ING Group, please visit www.ing.com.