

ING Monthly: Two anniversaries, one uncomfortable mirror

May 2026 marks one year since Friedrich Merz became Germany's chancellor and Christine Lagarde declared Europe's 'global euro moment'. Twelve months on, the promised momentum has failed to translate into strong outcomes

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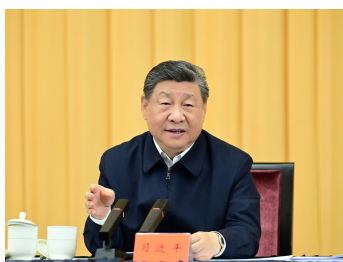
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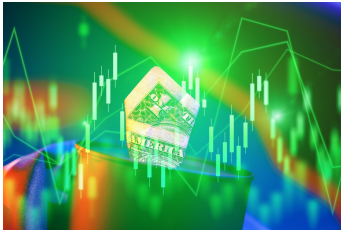


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ING Monthly: Two anniversaries, one uncomfortable mirror

Europe's 'global euro moment' is still waiting to be earned

By Carsten Brzeski

Article | 15 May 2026

Two anniversaries, one uncomfortable mirror

May 2026 marks two milestones: Friedrich Merz becoming Germany's chancellor and ECB President Christine Lagarde announcing Europe's 'global euro moment'. Let's be honest, 12 months on and the optics aren't good



May 2026 comes with two anniversaries, and neither looks particularly flattering in the rear-view mirror. One year ago, Friedrich Merz became Germany's chancellor, confirmed by parliament on the second attempt. An inauspicious start that in hindsight foreshadowed much of what followed. And one year ago, ECB President Christine Lagarde stood in Berlin and declared that the fracturing global order had created Europe's "global euro moment": a rare chance to step up, earn influence, and reshape the international monetary system in Europe's favour. Twelve months on, let's be honest: the optics are not good.

The global backdrop has deteriorated. The war in the Middle East has escalated, the Strait of Hormuz has remained closed for far longer than we and most others anticipated when the conflict began, and energy prices are surging in ways that featured in few base cases a year ago. US tariffs remain a threat to European exports, and global trade flows are being rewired around geopolitical fault lines rather than comparative advantage. Our new base case has brought another downward revision to eurozone growth, and not only there. On inflation, we maintain our view that the current wave will prove largely transitory with only a marginal impact on core inflation across

regions. But any more substantial supply chain disruption would risk more persistent knock-on effects, and we are not yet out of those woods.

Delivering on the promises made a year ago was always going to be harder in a turbulent world. But the gap between ambition and tangible results has opened a second layer of discomfort. Populist parties now lead polls simultaneously in Europe's three largest economies, Germany, France and Italy. In Germany, the party Merz explicitly set out to shrink has overtaken him in the polls. Many of these parties hold foreign policy instincts that sit awkwardly with deeper European integration, more joint borrowing, and a stronger strategic role for the EU on the world stage. The political conditions for Europe's great leap forward have rarely been less favourable.

And yet – to borrow from Monty Python's *Life of Brian* – what has Europe ever done for us? Well, over the last 12 months: the Savings and Investment Union, launched in March 2025. A securitisation reform. A market integration and supervision package. Updated payment services rules. A Savings and Investment Accounts recommendation. EIB defence investment tripled. EU defence spending is up 36% since 2022. A joint letter from Europe's six largest economies demanding capital markets agreement by the summer. A European Council calling for acceleration.

Quite a lot, as it turns out. The problem is that doing things and changing things are not the same. Lagarde's central diagnosis remains unanswered: €8 trillion in European household savings sit in low-yield bank deposits, unproductive and under-deployed. Capital markets remain fragmented. The home bias is structural. Progress is real, but the gap between the legislative pipeline and lived economic reality remains wide.

Europe's "global euro moment" is still waiting to be earned. The more useful question, perhaps, is not what the Romans have done for us but what we are still willing to do for them. The window is open. What happens next is a choice.

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In charts: Three scenarios for energy, macro and markets

How the Middle East conflict could play out across oil and gas markets, plus inflation, central banks and FX

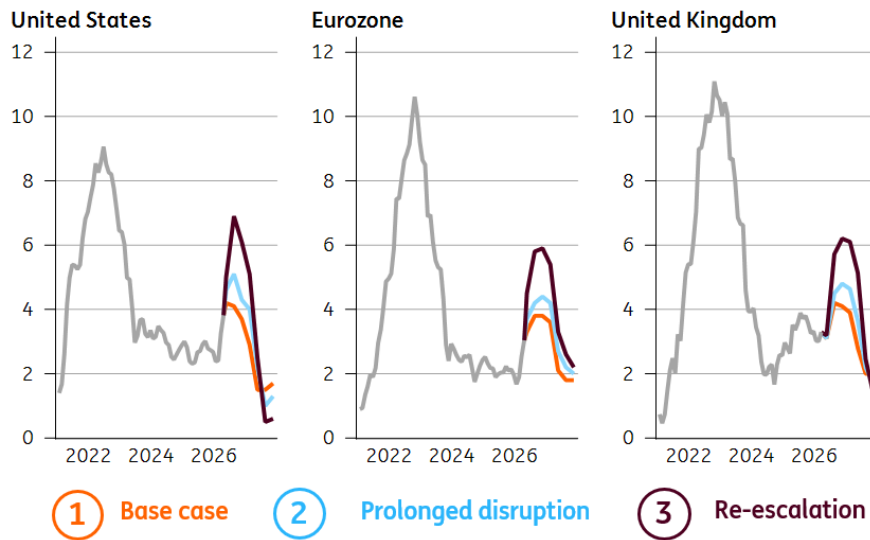


Three scenarios for energy prices

	Scale of disruption (% disruption to pre-war Persian Gulf oil flows)						Oil supply lost (m barrels)	Brent forecast (USD/bbl)			Gas supply lost (bcm)	TTF forecast (EUR/MWh)		
	Mar	Apr	May	Jun	Jul	Aug		Q2	Q3	Q4		Q2	Q3	Q4
ING base 1	70	70	50	35	7	7	1625	104	99	92	31	55	45	45
Prolonged disruption 2	70	70	70	35	14	14	2013	116	112	105	44	74	60	60
Re-escalation 3	70	70	94	94	47	47	3311	135	150	120	58	90	75	80

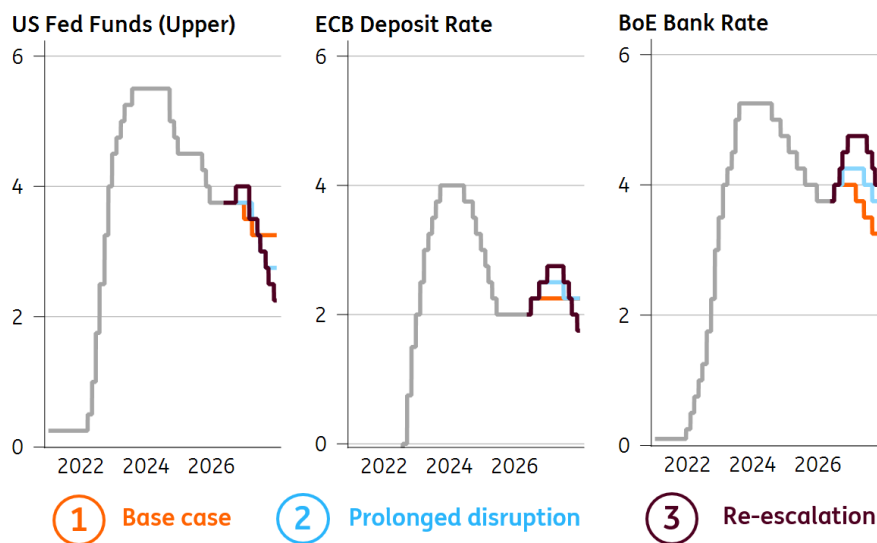
Source: ING

Three scenarios for inflation



Source: ING

Three scenarios for central banks



Source: ING

Three scenarios for markets

	14 May	① Base case			② Prolonged disruption			③ Re-escalation		
		Q2	Q3	Q4	Q2	Q3	Q4	Q2	Q3	Q4
Brent Crude (USD/bbl)	105	104	99	92	116	112	105	135	150	120
Dutch TTF gas (EUR/MWh)	48	55	45	45	74	60	60	90	75	80
US Inflation (YoY%)	3.8	4.2	4.1	3.7	4.6	5.1	4.3	5.0	6.9	6.1
Eurozone Inflation (YoY%)	3.0	3.3	3.8	3.8	3.7	4.2	4.4	4.5	5.8	5.9
ECB Deposit Rate (%)	2.00	2.25	2.25	2.25	2.25	2.50	2.50	2.25	2.50	2.75
Fed Funds Rate (%)	3.75	3.75	3.75	3.50	3.75	3.75	3.75	3.75	4.00	4.00
2Y EUR swap rate (%)	2.85	2.75	2.65	2.55	3.00	3.00	2.70	3.20	3.20	2.80
10Y EUR swap rate (%)	3.08	3.10	3.00	3.00	3.15	3.05	3.00	3.35	3.20	2.90
2Y USD swap rate (%)	3.82	3.65	3.40	3.30	4.00	3.60	3.40	4.00	4.10	3.70
10Y USD swap rate (%)	4.03	4.05	3.85	3.80	4.10	3.95	3.90	4.15	4.00	3.75
EUR/USD	1.17	1.17	1.18	1.20	1.15	1.16	1.17	1.12	1.10	1.12

Source: ING

Chart updated on 18 May to fix typographical errors with some of the swap rate numbers in scenarios 2 and 3.

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Sitting, waiting, wishing... for energy flows to resume

Energy markets remain extremely sensitive to developments in the Middle East, showing the significance of the supply disruptions we are witnessing. However, there have been several factors that have helped to take some pressure off prices



With no imminent peace deal in sight, stalled Hormuz flows continue to hold Brent above \$100/bbl

Falling Chinese imports and rising US exports offer relief to oil markets

It has been another volatile month in energy markets, with oil prices being whipsawed by Iran-related headlines. Cold water has been thrown over optimism for an imminent peace deal, after President Trump rejected Iran's counterproposal peace plan. And as a result, any hopes for a quick resumption in energy flows through the Strait of Hormuz have also faded, which has seen Brent trade convincingly back above \$100/bbl.

However, with the oil market facing a supply disruption of around 13m b/d, one may be surprised that we are not seeing much higher prices. There is an element of the market still clinging to some optimism that energy flows may start picking up. However, there are some fundamental factors

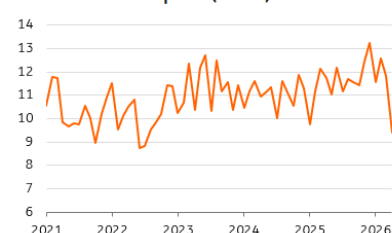
that have also helped. Chinese oil imports have fallen significantly, while US oil exports hit record levels consistently in April, which has helped to take some of the upward pressure off the market. But these are temporary solutions. China will be relying on inventory as imports fall, while similarly the growth in US exports is fed by inventory rather than supply growth.

Another element which has contained the market is that we have already started to see demand destruction in the oil market. Crude oil prices have not had to go as high as many would imagine to drive this decline in demand. This can be largely attributed to the relative strength seen in refined product prices (gasoline, diesel, jet fuel), reflected by the widening in refined product margins. The significant strength in refined product prices has meant that crude oil prices have not had to go as high to ensure demand destruction.

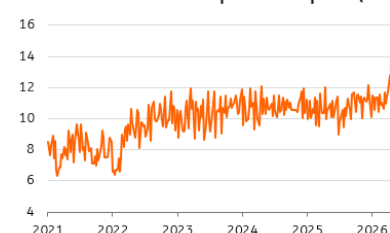
While there is still plenty of uncertainty over how the situation plays out, we are assuming some recovery in oil flows in the remainder of the second quarter, allowing for nearer to normal flows in the third quarter. Under this scenario, Brent averages \$104/bbl in 2Q26 and US\$92/bbl in 4Q26. Clearly, though, every day that goes by without a resolution pushes the market towards a much more aggressive scenario.

Chinese oil imports fall while US oil exports surge amid Persian Gulf supply disruptions

China crude oil imports (m b/d)



US crude oil and refined product exports (m b/d)



Source: China Customs, EIA, ING Research

Demand destruction keeps the gas market in check... for now

While European gas prices are trading above pre-Iran war levels, they have come off significantly from their peak following the start of the war. We believe that gas markets are underpricing the scale of the supply disruption. The gas market has less of a buffer to weather supply shocks, while there is little in the way of alternative routes for Persian Gulf LNG to move to its destination, other than going through the Strait of Hormuz. While ship tracking data shows that Qatar has shipped its first two LNG cargoes since the start of the war, this falls far short of normal flows.

There is not enough slack in the LNG market to offset these supply losses, so the market will have to rely on inventory and demand destruction to try to balance, which is what we have been seeing. In Asia, gas-to-coal switching is occurring within the power sector, while industrial demand is also coming under pressure. Meanwhile, relying on inventories means that buyers will have to come back to the market at a later stage to restock. The big upside risk for the market is if this restocking has to happen before energy flows through the Strait of Hormuz resume.

If we see Asian buyers coming into the spot LNG market to refill inventory/offset disrupted

contracted volumes, this will increase competition between Europe and Asia for cargoes, which would push prices higher.

Gas storage in the EU is relatively tight, at 35% full compared to a five-year average of 48%. This will make the job of refilling storage tougher, especially as the TTF forward curve – currently in backwardation – does not incentivise storage. More flexibility in EU storage targets helps to take some pressure off the market heading into the 2026/27 winter. However, going into the winter with 75% full storage (which is the minimum allowed under extreme conditions) would leave the European market more vulnerable through the winter and risk higher prices.

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Our latest views on the major central banks

Our take on what could be next for the Federal Reserve, the European Central Bank, the Bank of England and the Bank of Japan over the coming months



These are difficult times for global central banks

Federal Reserve

Kevin Warsh is taking over a Federal Reserve that is increasingly divided after three members “did not support the inclusion of an easing bias” in the April FOMC statement, while Stephen Miran again voted for a 25bp interest rate cut. Jerome Powell’s decision to remain on the Board of the FOMC, given his term as governor doesn’t expire until January 2028, adds an extra element of intrigue and means that Stephen Miran will need to step down from his interim position to make way for Warsh.

The prospect of headline inflation above 4% this summer and the recent improvement in jobs numbers suggest an extended pause from the Federal Reserve. We don’t expect to see broad and persistent inflation though, given the lack of demand impetus and the weakness in wage growth. We see a period of prolonged elevated fuel costs as being demand destructive, which will result in a return to cooler job numbers later in the year. Lower fuel costs in 2027 create the potential for sub 2% inflation next year.

We still see the potential for the Fed to move the policy rates down towards neutral, but three months later than we previously forecast. We are now forecasting 25bp policy rate cuts at the

December 2006 and March 2027 meetings.

European Central Bank

Signals after the ECB's April meeting have been very clear: a rate hike in June is clearly in the making. In fact, it would probably need another sharp deterioration of economic sentiment for the ECB not to hike. Even if the war in the Middle East ends tomorrow, the damage to inflation has already been done. Inflation has started and will continue to hit the eurozone economy. The key question is whether this will remain a 'transitory' shock, or whether supply chain disruptions could lead to wider knock-on effects beyond transportation and food inflation.

At the same time, the big unknown for inflation and the ECB is fiscal stimulus. Having been relatively muted in the eurozone so far, a significant stepping up of government efforts to cap energy prices or to offset purchasing power losses would not only fuel the inflationary pressures, but also put more pressure on the ECB.

For now, we only see one insurance rate hike in June, to demonstrate the central bank's willingness and determination to keep inflationary expectations anchored. More rate hikes are not our base case, as it's still hard to see that the ECB would really want to fight an exogenous supply shock at the cost of worsening an economic downturn.

Bank of England

We're leaning towards a one-and-done rate hike in June, but it remains a close call. The BoE seems less sold on the need to tighten policy, given that, before the war in Iran, it was poised to cut rates at least twice this year. In what the Bank is characterising as an "active hold", it has argued that simply not cutting amounts to de facto tightening.

Still, it feels to us that if the crisis hasn't shown much sign of improvement by the June meeting, then a hike is likely. But we're not convinced the three rate hikes priced by financial markets will be delivered this year. Politics is a risk, though not one that we think will affect the BoE outlook before the fourth quarter, if at all. The jobs market is weak. And the risk of second-round effects is considerably reduced compared to four years ago.

Bank of Japan

The Bank of Japan's hesitation over rate hikes is unlikely to persist. We expect a 25bp hike in June as the board acknowledged that inflationary pressures may intensify, resulting from the supply disruption and current loose monetary conditions, if the BoJ doesn't respond appropriately. The Middle East situation continues to pose risks to our call. But the April meeting summary indicates a more hawkish stance than in March and shows discussions among board members centred on the timing of hikes.

There were already three dissenting votes in April while some members believed a rate hike is needed soon to avoid economic harm and further inflation. We believe that the recent weakness in Japanese government bonds and the Japanese yen reflects concerns that the BoJ may be lagging behind current economic developments. With steady wage growth, we expect inflation pressure to broaden and firm up more in the second half of the year. Thus, the BoJ is likely to deliver another

hike in the fourth quarter.

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Rising inflation signals June rate hike in the eurozone

The eurozone economy is rapidly losing momentum, while headline inflation is climbing towards 4%. With inflationary expectations now also picking up, the European Central Bank is likely to raise interest rates in June



ECB President Christine Lagarde

Subdued growth in the first quarter...

According to provisional data, the eurozone grew by a disappointing 0.1% in the first quarter, though the erratic Irish GDP data shaved off nearly 0.1pp from the growth rate. Meanwhile, the first hard data for March shows that the quarter ended on a weak note, hardly surprising given the events in the Middle East.

Retail sales fell 0.1% in March, after a 0.3% decline in February. In the ECB's bank lending survey, banks reported a slight net decrease in loan demand for firms in the first quarter of 2026, mainly driven by a decrease in demand for fixed investment.

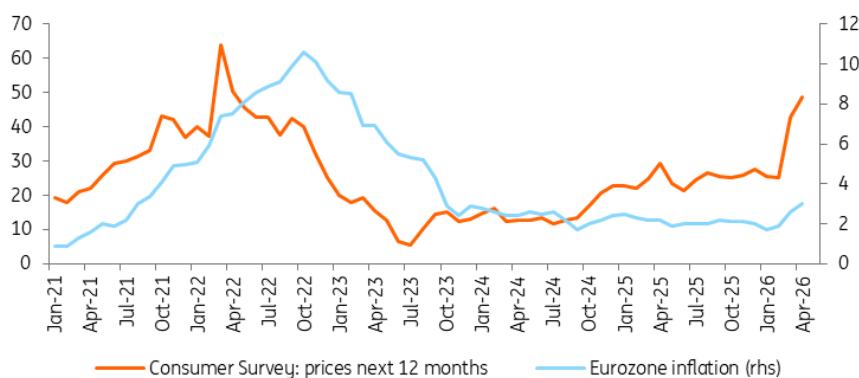
...and the second started on a weak footing

Survey indicators for April show a further loss of momentum, with the PMI below the neutral threshold of 50, indicating a contraction in private-sector activity. This weakness was primarily driven by services, while manufacturing remained somewhat more resilient, albeit partly supported by inventory-building rather than underlying demand.

The fear of supply chain disruption has pushed industrial companies to increase their stock of crucial inputs, which has generated more activity in the intermediate goods-producing sectors. But this is likely to bring only temporary growth support.

We continue to expect eurozone GDP to come close to a standstill in the second quarter and only begin to recover gradually after the summer. We have therefore kept our growth forecast unchanged at 0.7% for 2026 and 1.3% for 2027.

Inflation expectations are rising



Source: LSEG Datastream

Inflation hits 3%

The flash estimate for April showed headline HICP inflation rising to 3.0% year-on-year, up from 2.6% in March. This increase was largely driven by a sharp acceleration in energy prices. Core inflation eased marginally to 2.2%, though the timing of the Easter holidays might have distorted the figure.

Selling price expectations have surged both in the PMI and the European Commission's business surveys. That said, with final demand weaker than in 2022, we don't see these higher selling price expectations fully materialising in reality. We still expect inflation to increase to close to 4% in the coming months, yielding an average inflation rate of 3.3% for the year. With energy prices likely to be lower again in 2027, headline inflation should fall back to 2.3% next year.

Rate hike in June

Even though ECB President Christine Lagarde doesn't like the word, the eurozone is facing a stagflation-like environment, albeit still mild at this stage. Inflation expectations are picking up: the

three-year-ahead consumer inflation expectation climbed to 3% in March from 2.5% in February.

In the April press conference, Lagarde stated that in June there would be enough data to make an informed decision. She also said that the fact that in the baseline scenario the market anticipated two rate hikes means that the ECB's reaction function is well understood.

The bottom line is that a rate hike in June is very likely and that a second one in September cannot be ruled out. That said, three rate hikes this year still seems a bridge too far to us.

Author

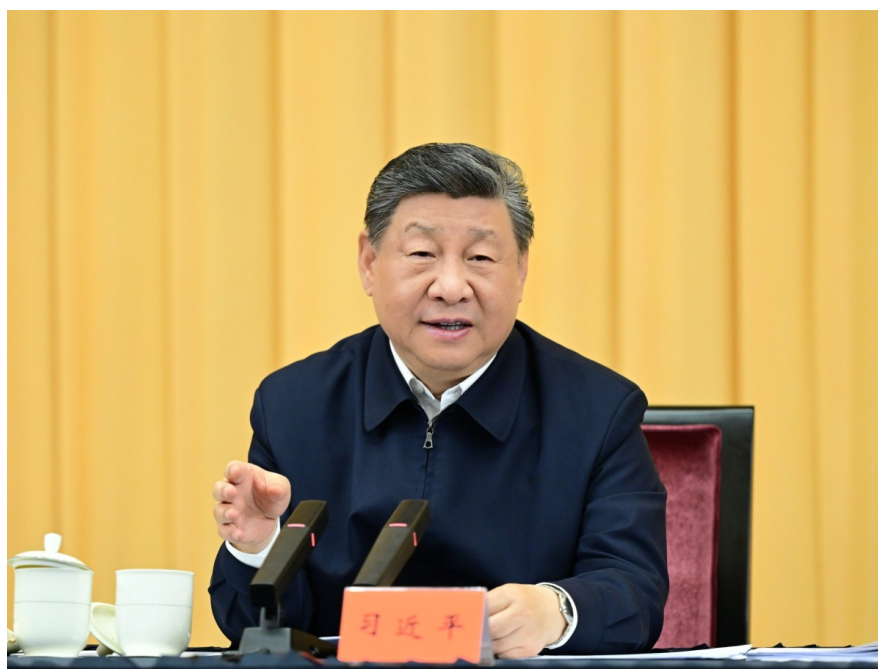
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Stronger growth and reflation ease pressure for stimulus in China

China is faring relatively well despite the Iran war, as the reflation trend gains momentum. We probably haven't yet seen the full impact of higher energy prices. This combination of higher-than-expected growth and inflation will limit policymakers' urgency for new stimulus



Chinese President Xi Jinping ahead of this week's high-stakes summit with US President Trump

'Constructive strategic stability' to guide US-China ties after Trump's first Beijing trip since 2017

President Trump's long-awaited trip to Beijing largely played out as expected, with some positive developments on the economic side but no real breakthrough on geopolitical issues. A Chinese foreign ministry readout noted that Presidents Xi and Trump agreed to establish "China-US constructive strategic stability" to guide the next three years of relations. It holds the potential to expand cooperation on the economy and trade, health, agriculture, tourism, culture, and law enforcement. Earlier announced measures included China agreeing to renew beef import licences and resume Boeing aeroplane imports. We expect there to be additional announcements unveiled

moving forward. But even without any groundbreaking deals, China's trade with the US is expected to show signs of recovery in the months ahead. We saw in the April trade data that China's exports to the US bounced back to 11.3% year-on-year, after falling by 16.4% in the first quarter.

The media and market focus was on the geopolitics side leading up to the summit, especially watching for any potential developments on Iran and Taiwan. No major breakthroughs were expected given the positions of both sides were well known heading into the meetings. China reiterated Taiwan as its core issue, while the US focus was on developments in Iran. We're unlikely to see any major formal announcements of progress on these issues. But actions speak louder than words. If we see any signs of progress in Iran negotiations or the planned Taiwan arms sales in the days ahead, it would likely suggest these discussions bore fruit.

Reflation trend is gaining steam

China's April inflation data surprised on the upside, indicating strengthening reflation momentum. Both PPI and non-food inflation hit 45-month highs in April. We suspect the impact of higher energy prices is yet to fully materialise. As input costs rise, we expect at least part of this to be passed on to consumers.

Reflation will be a mixed bag. In the near term, rising prices should be a drag on activity, as they could translate into slower consumption and thinner corporate margins. Meanwhile, a higher GDP deflator will reduce this year's growth figures. It's important for China to firmly exit the deflationary mindset that had set in over the previous years. This could actually improve the outlook over the medium term and encourage investment and consumption rather than further saving.

Limited signs of urgency for new stimulus

China's April Politburo meeting ended without major policy announcements, with policymakers acknowledging a good start to the year but a need to consolidate the economic recovery.

On the fiscal side, the focus appears to be on accelerating the rollout of existing policy announcements rather than pushing out new measures for now.

The monetary policy tone suggests that rate cuts are conditional. With liquidity still ample, it looks increasingly likely that any potential easing won't take place until the second half of the year.

Without new stimulus, we could return to last year's trajectory, where a solid start is followed by slower momentum as the months progress. This could be particularly true this year, as the economic impact of the Iran war begins to manifest in the data.

We slightly revised our 2026 full-year GDP forecast up to 4.7% YoY last month after the stronger-than-expected 1Q26 GDP read, with risks broadly balanced at this juncture.

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Bank of England unlikely to deliver on market expectations

Political turmoil is driving up UK borrowing costs as investors start to price even higher interest rates, on expectations of looser fiscal policy. Yet the case for rate rises is far from clear-cut. We expect a one-and-done hike in June



Prime Minister Keir Starmer under pressure as ministerial resignations spark Labour leadership crisis

Political drama is once again driving up UK borrowing costs

Financial markets have responded to renewed UK political turmoil by ramping up bets on Bank of England tightening. We warned that what ultimately became disastrous local elections for the ruling Labour Party left markets exposed to a sell-off amid renewed leadership speculation.

Almost three rate hikes are priced before year-end, almost identical to what's expected from the European Central Bank.

We remain unconvinced. We're now forecasting one rate hike from the BoE in June, but only narrowly. At April's meeting, officials made clear that simply not cutting rates – something the

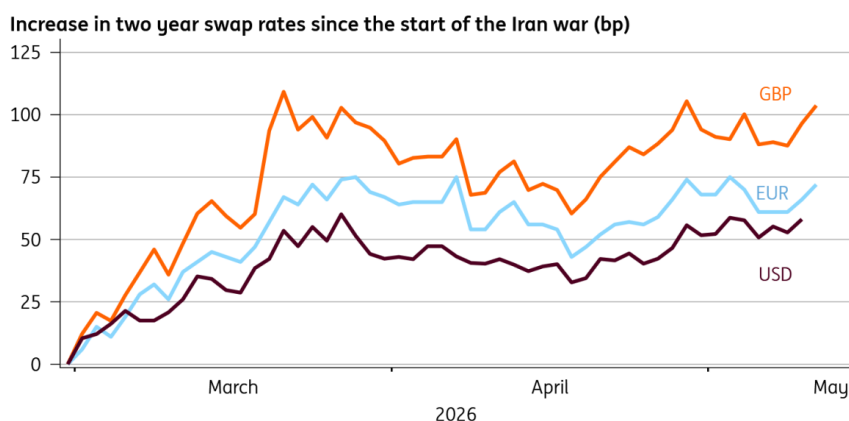
Bank would likely have done at least twice this year absent the Iran war – already amounted to de facto tightening. With energy prices not far from today’s levels, the prevailing view inside the Bank felt somewhere between a prolonged hold and a one-and-done rate hike.

We’re nudging towards the latter, largely because our own energy assumptions are more aggressive than the low and central scenarios officials were considering late last month. Even so, the case for a multi-hike cycle looks thin.

Though Prime Minister Keir Starmer is fighting on, investors are increasingly pricing a leadership contest that leaves Labour shifting left, loosening fiscal rules and increasing borrowing. In theory, that could argue for higher interest rates. In practice, memories of the 2022 mini-budget crisis remain raw, and any leadership hopeful will be under intense pressure to rule out dramatic fiscal changes.

Even if they don’t, meaningful policy shifts are unlikely before the Autumn Budget, probably in November. The Bank of England cannot respond to fiscal changes that have not been formally announced, meaning leadership speculation is unlikely to matter for monetary policy before the fourth quarter – if at all.

UK interest rate expectations have risen further than elsewhere



Source: Macrobond, ING

The UK isn't more exposed than the eurozone on inflation

The wider macro case for higher interest rates is also far from clear-cut – and certainly less so than in the eurozone. UK policy rates are at more restrictive levels already. The jobs market is comparatively weaker, looking at vacancies, and the energy spike is likely to add extra pressure on unemployment. And don’t be fooled by a [spike in first-quarter GDP](#), which we think was overwhelmingly driven by problems with seasonal adjustment. Taken together, the risk of second-round inflation effects shouldn’t be overstated.

Finally, claims that the UK is uniquely exposed to energy shocks are only half right. Britain is highly reliant on natural gas – around 32% of total energy consumption, versus 20% in Germany and 15% in France. But this is not, yet, a gas crisis. On net energy imports, the UK compares favourably with much of Europe.

That is why our UK inflation outlook remains remarkably similar to the eurozone's. We expect CPI to peak a touch above 4% in the second half of the year.

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Upside inflation risks in Asia outweigh downside growth risks

Growth in Asia has proven relatively resilient, but inflation risks are building as elevated energy prices and food supply risks persist. With upside inflation pressures dominating, regional monetary policy is likely to shift further towards tightening



Myeong-dong, Seoul, South Korea. Resilient growth has led us to upgrade our 2026 GDP forecast for Korea

Better-than-expected growth despite energy headwinds

Growth across developed Asia continued to outperform in the first quarter and is expected to remain resilient in the second quarter, driven by factors extending beyond the technology export cycle. This resilience was helped by releasing strategic oil reserves to ease supply shortages, alongside government subsidies that took some pressure off households and businesses facing higher inflation. These factors have helped sustain activity despite elevated energy and geopolitical risks. Against this backdrop, we have upgraded our 2026 GDP growth forecasts for Taiwan and Korea.

At the same time, economies with high dependence on energy imports – most notably India and Singapore – are faring better than expected. In India's case, diversification of crude purchases and increased reliance on multiple supply sources have reduced vulnerability to energy supply

shortages. Gas and fertiliser supplies have been secured, limiting spillovers into food inflation and agricultural output. Singapore has similarly benefited from stable energy access and effective policy management, supporting growth outcomes despite elevated import prices.

Inflation spillovers are starting to show up more clearly

The Philippines stands out as a notable outlier, having experienced a significant slowdown in GDP growth. This divergence highlights differences in domestic demand conditions and policy buffers across the region. The Philippines also experienced a sharp rise in CPI inflation, reaching a three-year high of 7.2%. While the increase in transport inflation was largely anticipated amid higher oil prices, the magnitude of the upside surprise was driven by a pronounced acceleration in food inflation. This was compounded by second-round effects stemming from the continued pass-through of elevated global oil prices into electricity, gas, and restaurant prices.

Looking ahead, inflation pressures are likely to pick up. Even if oil supply disruptions ease significantly by June as per our base case, global oil prices are expected to stay high into the third quarter, leaving countries with thinner fiscal buffers. At the same time, rising El Niño risks could keep upward pressure on food prices for longer.

Economies, such as India, which have thus far kept retail gasoline prices unchanged, limiting the impact of oil price hikes, are also likely to see headline inflation edge above the central bank's target by year-end as fuel subsidies ease, particularly if food price pressures also materialise. In Korea, we expect inflation to rise further despite government measures, reaching around 3% as early as June, while steady wage gains are strengthening the case for a Bank of Japan rate hike in June.

Higher rates for most of Asia

Even as GDP growth across developed Asia slows in the second half of the year from a strong first half, upside risks to inflation are likely to dominate. The upward inflation trajectory across most Asian economies – as elevated energy prices persist for longer due to the war – should outweigh the growth drag over at least the next two quarters.

Accordingly, in addition to the rate hikes for Korea and Japan already incorporated into our profile, we are now adding hikes for the Philippines (75bp), Indonesia (25bp), and Taiwan, and pushing out our rate cut in China to the final few months of the year.

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Energy shock reshapes growth and policy outlook in CEE

Poland remains relatively resilient, while the Czech Republic and Hungary face mounting pressure as the energy shock deepens. Growth is set to slow, inflation risks persist, and central banks remain cautious



The Warsaw skyline. Poland continues to outperform the rest of the CEE region

Poland: Resilient to the energy shock, with rate hikes a remote scenario

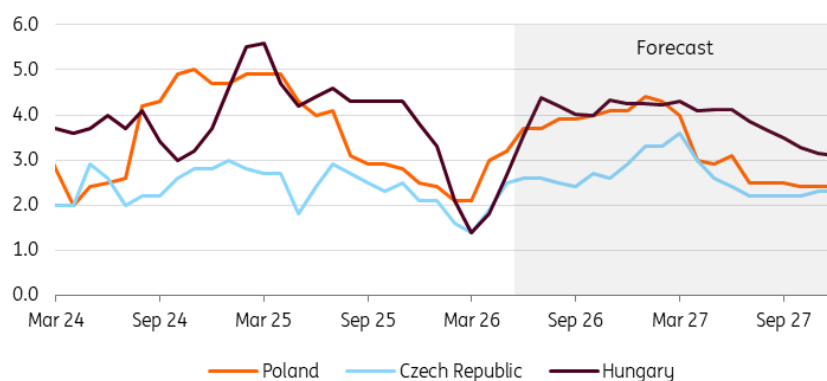
The Polish economy continues to outperform the rest of the CEE region and the EU average, despite a weak manufacturing sector, with growth driven by services. Economic growth was subdued in the first two months of the year but rebounded strongly in March, due to companies and households stockpiling ahead of potential supply chain problems or price spikes. On an annual basis, GDP growth in the first quarter was only slightly below the 4.1% year-on-year rate recorded in the fourth quarter of 2025. We expect the negative impact of the Middle East conflict on activity to become more visible in the second quarter, but for the year as a whole, we still expect 3.4%, only marginally below our pre-war expectations of 3,7% YoY.

The National Bank of Poland left policy rates unchanged in May, maintaining a wait-and-see

approach, but the bias has become more hawkish and President Adam Glapiński stated that monetary policy could be tightened if inflation rises above the upper bound of acceptable deviations from the target (3.5%) and if projections point to inflation remaining above this threshold over the medium term. This makes the July NBP staff projection an important milestone for future monetary policy decisions. We expect inflation to rise above 4% in the second half of this year, but to decline markedly in the second quarter of 2027. Accordingly, our baseline scenario assumes no change in interest rates this year.

The S&P held the rating outlook flat, despite previous downgrades by Moody's and Fitch, as the GDP outperformance, the balanced current account (only 0.9% of GDP deficit) and low private debt offset rising public debt. That, together with the approaching inflow of the Recovery and Resilience Facility (RRF), which is nearly PLN100bn in grants and loans, and SAFE loans, is helping to stabilise the PLN exchange rate against the euro. At the same time, FI investors continue to price in possible monetary tightening ahead, reflecting inflation risks.

Headline inflation forecast (%)



Source: Macrobond, ING estimates

Czech Republic: Keeping cool as the supply shock starts to bite

We are lowering our economic growth outlook to below 2% this year on the back of a soft 1Q26 GDP reading and the extension of the Middle Eastern conflict. Our base case scenario assumes that Brent crude prices will hover above US\$100/bbl until the summer ends and then recede to reasonable levels just above \$80/bbl only at the start of 2027. With no end in sight to both the blockade of Hormuz and the war in Ukraine, the elevated uncertainty will alter investment plans and ultimately weigh on the propensity to spend as energy bills are expected to rise. We take the position that negative effects on economic activity will emerge sooner or later, though it is hard to say when exactly things start to give in and crumble.

The Czech economy entered the negative external supply shock at a rather convenient point, and under our base case scenario, we do not expect headline inflation to move significantly higher for long, despite the impact of elevated energy prices and second-round effects.

We see inflation peaking early next year, violating the 3% upper bound threshold just for a couple of months before receding to the target. Deeming this price level surge as transitory and keeping in mind the risks to economic activity, which can be hard to assess ex ante, the appropriate reaction

of monetary policy is to keep rates unchanged for as long as possible. This way, you can gauge how the negative effects ripple through the economy, you avoid the risk of pushing it over the cliff, and you don't rush into a monetary policy mistake through premature rate hikes.

Hungary: A new chapter but the same challenges

About a month ago, Hungarian voters decided to open a new chapter in Hungary's history book. The dust has settled somewhat since then, but the optimism remains. However, it seems that it is not just pure hope. We have seen a lot of positive data lately. GDP growth in the first quarter was relatively sound, especially compared to the stagnation seen in the past three years. While we are still waiting for the details, we suspect that consumption is behind the strong performance. Although the figure was in line with our expectations, we have revised our forecast GDP growth downward to 1.5% in 2026 due to higher energy prices. However, in all fairness, the toughest part of the energy and supply shock for the economy is yet to come.

Hungary's inflation continued to accelerate in April. However, the latest figures are a clear positive surprise, given that we have now entered a third month of energy price shocks. Despite all the unknowns, we still anticipate an average inflation rate of around 3.0-3.5% this year. With price pressure peaking at around 5% at the end of this year and in the early part of next year, we can't see a clear path towards an interest rate cut by the National Bank of Hungary. Even if the strong investor appetite towards Hungarian assets remains in place, we struggle to see how the forint can emerge unscathed if the European Central Bank hikes rates and markets turn more hawkish on the Federal Reserve.

Nevertheless, the forint should continue to appreciate and yields should keep grinding lower if positive headlines about EU funds, institutional changes, fiscal policy or foreign policy emerge from time to time.

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CIS FX buoyed by inflows while CPI risks hit the rates outlook

Higher commodities prices and strong portfolio inflows are lifting exporters' external buffers and reinforcing currencies in the region. Meanwhile, mounting inflation pressures are leading to tighter monetary policy outlooks. However, that is unlikely to materially affect economic activity in the region



Clockwise from top left: Armenia, Azerbaijan, Uzbekistan, Kazakhstan

External buffers improve

The escalation in the Middle East, including persistent tensions and risks around the Strait of Hormuz, has reinforced a higher commodity-price backdrop (see [here](#)). Compared with our [previous](#) monthly note, the oil price outlook for FY26 has edged up by \$4 to \$93/bbl. Based on the [macro sensitivities](#), Azerbaijan and Kazakhstan remain the main beneficiaries, while Uzbekistan and Armenia present a more balanced picture.

- In **Azerbaijan**, under the new oil scenario, the current account is heading towards a 9-10% GDP this year, while the consolidated budget surplus may reach 4% of GDP.
- **Kazakhstan** is also seeing stronger exports and fiscal revenues, helping to reduce its current account deficit to 2-3% of GDP and balance its consolidated budget.
- **Uzbekistan** faces higher import costs from rising oil prices, while gold exports, on hold since 4Q25, should restart later in the year and help contain the current account deficit at around

4% of GDP.

- **Armenia**, as a net energy importer, remains exposed to global price moves and remains in a twin-deficit pattern, but continues to benefit from remittances of 6%+ of GDP, supported by increased tourism amid regional tensions.

Strong portfolio inflows – the key positive surprise and a supportive factor to CIS-4 FX

Contrary to our [initial concerns](#), global and regional risk appetite has remained resilient despite Middle East tensions. Country-specific developments suggest the CIS-4 is using the current environment to attract capital inflows.

- **Kazakhstan is progressing towards Euroclear inclusion** while preparing sovereign and quasi-sovereign debt issuance. The tenge's 7% appreciation vs. the USD since the outbreak of the Iran War (and the 18% strengthening since the end of 3Q25) reflects stronger capital inflows, as the effect of higher oil prices should be largely offset by dividend outflows and higher imports.
- **Uzbekistan** is advancing its privatisation programme, with [UzNIF IPO](#) and a broader pipeline aimed at foreign investors. We believe stronger capital inflows are currently the primary factor behind the soum's stability in recent months despite the halt in gold exports.
- **Armenia** is also seeing stronger portfolio inflows, reflecting ongoing normalisation with Azerbaijan and supporting FX resilience: the dram continued its strengthening trend, gaining 2% since late February despite a material spike in oil prices and the likely widening of the current account deficit to 8-9% of GDP this year.

Compared with the previous month, we have a more favourable near to medium-term outlook for CIS-4 floating currencies, while maintaining a cautious longer-term view until a proven track record in structural transformation is established. Higher reliance on portfolio flows could be a mixed blessing, as financial market investors, unlike corporate FDI partners, can be easily spooked.

Inflation risks confirmed, policy stance should tighten

The worsening CPI outlook is materialising in line with our expectations. Alongside imported inflation – through exposure to the EU, China, and other trade partners experiencing direct effects of higher commodity prices – domestic factors are amplifying pressures in most economies, with Azerbaijan an exception.

- **Kazakhstan**: fiscal and quasi-fiscal stimulus, together with possible utility tariff increases, complicate a return to single-digit CPI despite the recent slowdown to 10.6% year-on-year in April.
- **Uzbekistan** faces demand-driven pressures from stronger activity, with the recent slowdown in CPI to 7.1% YoY largely driven by base effects, as noted by the central bank.
- **Armenia**, already sensitive to external costs, has seen CPI rise to 5.3% YoY in April, well above its 3% target. [Strong domestic demand](#) (GDP growth of 7.1% YoY in 1Q26) is also highlighted as a risk by the Central Bank of Armenia, while we also see persistent fiscal deficits of around 3.5% of GDP as pro-inflationary.
- **Azerbaijan** (CPI 5.6% YoY as of March), while exposed to imported inflation risks reflected in [the central bank's higher FY26-27 outlook](#), shows weaker domestic pressures given soft

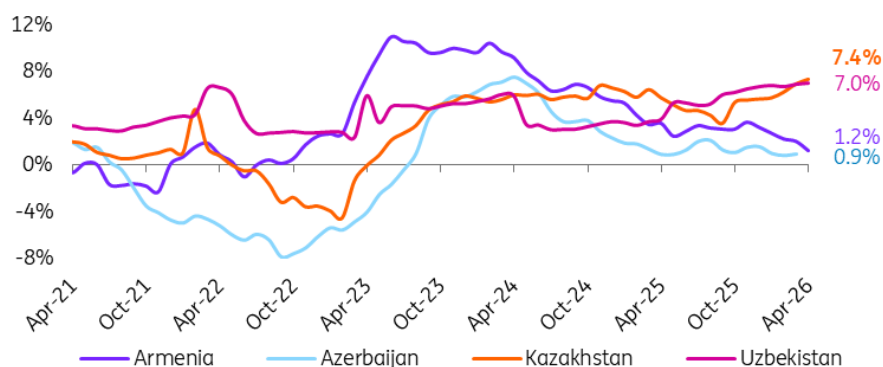
growth. GDP contracted by 0.3% YoY in 1Q26, with overall expected full-year growth in low single digits.

We therefore stand by an upward revision to the CPI trajectory for 2026-27, implying a less steep slowdown in Kazakhstan and Uzbekistan, stabilisation in Azerbaijan, and some acceleration in Armenia. The supply-side nature of these revisions does not require immediate rate hikes but reduces the scope for cuts versus previous expectations.

Meanwhile, despite the more moderate nature of the current global inflationary shock compared to 2022, the balance of risks to global inflation forecasts is still tilted upward, and the second-round effects could trigger more drastic monetary policy action, should our global base case scenario prove too optimistic.

On the positive side, a tighter monetary stance should remain broadly neutral for activity, which remains robust in Kazakhstan, Uzbekistan, and Armenia, and less rate-sensitive in Azerbaijan. Cautious monetary policy should reinforce the CIS-4's competitiveness from the perspective of global investors, and nominal FX rate strength should serve as a disinflationary factor. The current real rate context (see the chart below) suggests that the balance of risks to our policy rate views is tilted upward for Armenia and Azerbaijan, and downward for Kazakhstan and Uzbekistan.

Real policy rates in CIS-4 (%), based on CPI over the past 12 months



Source: National sources, CEIC, Refinitiv, ING

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High rates and commodity exposure preferred in FX

As the global energy shock continues to unfold, it seems investors are preferring exposure to those currencies with high interest rates and sitting on the right side of the energy import ledger. The euro does not tick either of those boxes, but EUR/USD could be lifted by the rising tide of a weaker dollar



Energy exposure and higher yields are driving continued strength in the Norwegian krone

FX volatility has been subdued

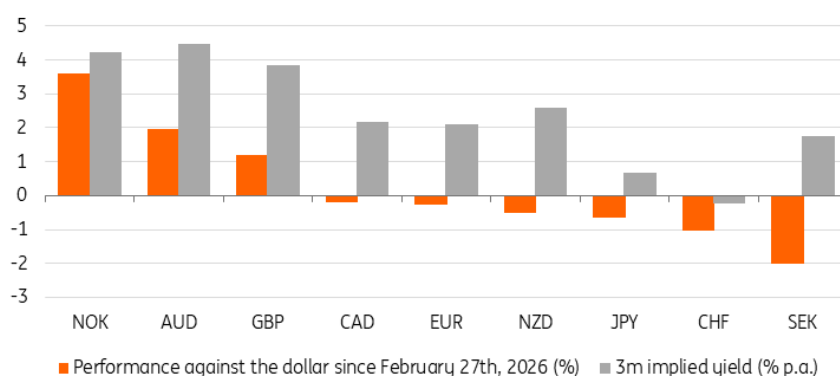
Looking across asset classes, it is fair to say that just like equities and credit, FX markets have traded with a 'glass half full' mindset. After a brief spike through March, FX traded volatility has sunk back to the lower end of the range seen over the last three years. As always, lower volatility encourages the search for yield and, across both developed and emerging currencies, high yielders are in demand.

In the developed space, it has seen both the Norwegian krone and the Australian dollar outperform. Not only do both these currencies offer implied yields in excess of 4%, but also net positive exposure to the energy story. Both countries have seen their terms of trade improve

markedly over the last eight weeks. And both central banks have already hiked during the crisis and are holding open the door for more tightening. We expect continued strength in these currencies.

At the other end of the spectrum are the low yielders and those threatened with a larger energy import bill. The yen stands out here – especially with the Bank of Japan dragging its feet with rate hikes and leaving real interest rates in deeply negative territory. So far, it looks like the Bank of Japan has sold around \$70bn to defend the critical 160 level in USD/JPY. Intervention looks less fundamentally justified than in 2024 (when the Fed was preparing to ease). We suspect this is just the start of a long campaign of the BoJ battling the market at 160.

G10 FX performance against the dollar



Source: Refinitiv, ING

What about the dollar?

Somewhat surprisingly, the dollar sits in the middle of the G10 FX pack when it comes to performance over the last eight weeks. In theory, the dollar should have done better given US energy independence and a challenging environment for risk assets. Holding the dollar back has probably been the global equity rally, where correlations between equity gains and dollar weakness are strengthening. That is certainly the case in emerging markets, where investors have held onto the long positions built between last summer and February this year.

We remain bearish on the dollar over a multi-quarter horizon as the Fed will eventually have the opportunity to cut rates back to neutral. We also note very little risk premia priced into the dollar currently – which could change in the run-up to the US Mid-term elections this November. Yet events in Iran will have a big say in the timing of the dollar sell-off. The longer energy prices stay high, the greater chance the Fed will have to sound hawkish in order to ride out the inflation surge. This could help the dollar and hurt risk assets.

For EUR/USD, this warns of further trading near the 1.16-1.18 range through the second quarter. However, the ECB has to hike in June and sound hawkish to keep real interest rates high during this period of elevated inflation. Later in the year, EUR/USD levels above 1.20 remain entirely possible, assuming the global economy can get back on track and the core investment theme of diversifying US risk resumes.

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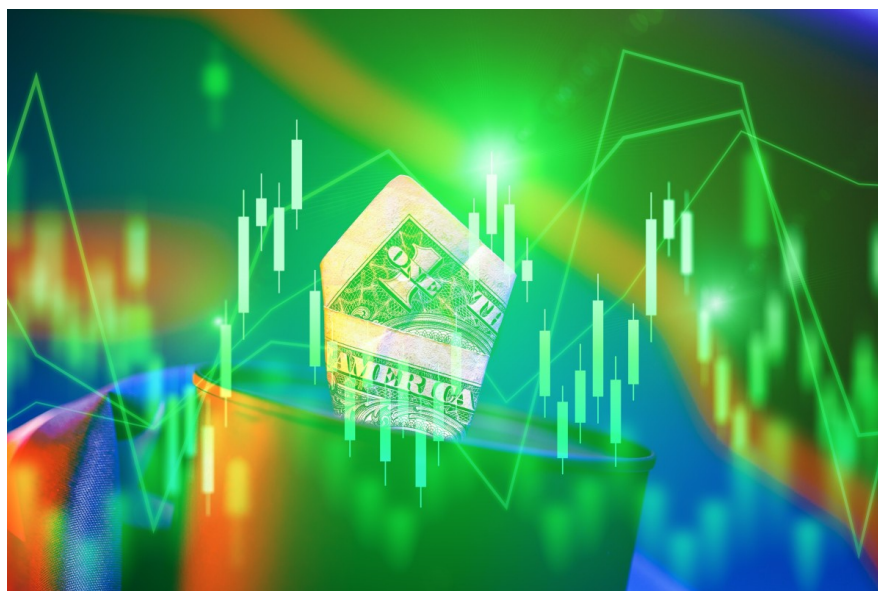
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Rates face risk of instability

Market rates have risen because of the Iran war, but have been controlled (apart from UK gilts). An extrapolation of the shutdown of the Strait points to higher market rates still. We expect the US 10yr yield to land at around 4.5% by mid-year, but it risks overshooting in the next few weeks



Bond yields have risen but remain orderly. We don't expect it, but conditions could deteriorate quickly

US Treasuries showing measured reaction to grind higher in the price of oil. That can change

Where to start. The stand-off between the US and Iran is as good a place as any. The basic market assumption is that the Strait of Hormuz will remain stuck until we know more. And while it's stuck, inflation expectations continue to ratchet higher. If that's true, it's tough to imagine any other route for Treasury yields apart from up, at least in the coming few weeks. US headline inflation has already hit 3.8% (we've just had the April reading). It was 2.4% before the war. We'll very likely hit 4% for May. A continuation of the war, and we risk adding to that.

We have 4.5% as a target for the 10yr Treasury yield for mid-year, but between now and then it risks trading up to the 4.5% to 4.75% area. It's exposed to a snap higher in yield at any point, should Treasury bond investors decide to *really* sell. The flow data since the war began shows

some selling, but also buying, and in fact, in net terms, no *marked* selling. Instead, there has been a re-marking higher in yields in tandem with the slow elevation in inflation expectations. These, in fact, remain relatively tame; the 10yr break-even inflation rate is 2.5%. Good, as it's not particularly high. Bad, as it has plenty of room to move higher.

The eurozone, UK and Japan are trucking along with varying impulses

Eurozone yields are feeling the same pressures, albeit more focused on shorter maturities, as a series of European Central Bank hikes are now discounted (at least 75bp). Upward pressure on market rates is set to be sustained in the weeks ahead, and for at least as long as the stalemate in the Strait persists. The 10yr rate is liable to remain comfortably above 3%. After all, eurozone inflation is now running at 3% and is also on the rise. The 1yr European inflation breakeven is just short of 4%, highlighting the inflation concern the ECB risks reacting to with rate hikes. This protects longer tenors, but does not shield them.

There are also idiosyncratic pressures elsewhere. Both the UK and Japan have had their issues in the past few quarters. Of late, the UK, in particular, has been hit. In fact, since the Iran war began, the UK 10yr gilt yield is up some 90bp. A large chunk of that has nothing to do with the war. Political wobbles and underlying fiscal deficit concerns have been drivers. In Japan, rates have been too low for too long, and this has manifested in material depreciation pressure on the yen. Japanese rates are up in tandem with US rates since the war broke out, but can keep on rising in relative terms when the war ends, as rates adjust higher into the medium term.

The war remains the driving force for direction. We look up for yields ahead first

In the end, direction continues to come from the path of the war. If the past couple of weeks are anything to go by, then the path ahead is clear and yields continue to test higher. It gets more complex beyond that. Whatever happens, we are being left with an echo of higher inflation. So, even if we were to see an earlier-than-expected end to this conflict, yields won't lurch lower dramatically.

If they do, they'll find fairer value at higher-than-normal levels. For the US, that means the 4.25% area as a downside level. And for the eurozone, the 3% area is set to prove a sticky floor. For now, though, we're looking up for yields, not down.

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Report | 15 May 2026

ING Monthly: Two anniversaries, one uncomfortable mirror

May 2026 comes with two anniversaries, and neither looks particularly flattering in the rear-view mirror



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