Cruising along

- **The euro area economy has grown faster than expected despite geopolitical uncertainty, and the labour market remains resilient. We expect moderate growth to continue in both 2026 and 2027 driven by rising real incomes and investments. We see risks to the outlook as balanced.**
- **Inflation has fallen below the 2% target and is expected to remain close to 2% in both 2026 and 2027. The recent rise in energy prices due to the war in Iran is expected to drive inflation above target in the near-term but declining wage growth will drive core inflation lower during the forecasting period. We consider the risks to the inflation outlook as tilted to the upside due to energy prices.**
- **We expect the ECB to leave the policy rate unchanged at 2.00% in both 2026 and 2027, and thereby look through a temporary rise in inflation due to higher energy prices from the war in Iran as medium-term inflation expectations remain anchored. We view the risks to the outlook as balanced.**

	2025	Forecast 2026	2027
GDP Growth	1.5%	1.3% (1.2%)	1.4% (1.4%)
Inflation	2.1%	2.1% (1.8%)	1.8% (1.9%)
Unemployment	6.4%	6.2% (6.4%)	6.0% (6.2%)
Policy rate*	2.00%	2.00% (2.00%)	2.00% (2.00%)

Parentheses are the old projections (From December 2025)
**End of period*
Source: Danske Bank, Eurostat, ECB

Economic activity in the euro area has continued to beat expectations on the back of decent growth in the service sector and a manufacturing sector that is no longer a drag on activity. In February, the manufacturing PMI rose to its highest level since the ECB began raising rates in 2022. At the same time, the labour market remains resilient with low unemployment and a continued rise in employment although several indicators do suggest a gradual cooling in labour demand. We expect a continued rise in employment driven by Southern Europe, which should cause a further decline in the unemployment rate.

Moderate growth is also expected to continue in the coming years, and we forecast GDP growth at 1.3% y/y in 2026 and 1.4% y/y in 2027. The strong labour market combined with rising real incomes should support private consumption in both years. Weak consumer confidence has caused a significant rise in the household savings rate, which provides excess savings to be

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Important disclosures and certifications are contained from page 3 of this report.

"In February, the manufacturing PMI rose to its highest level since the ECB began raising rates in 2022"

Rune Thyge Johansen, Analyst

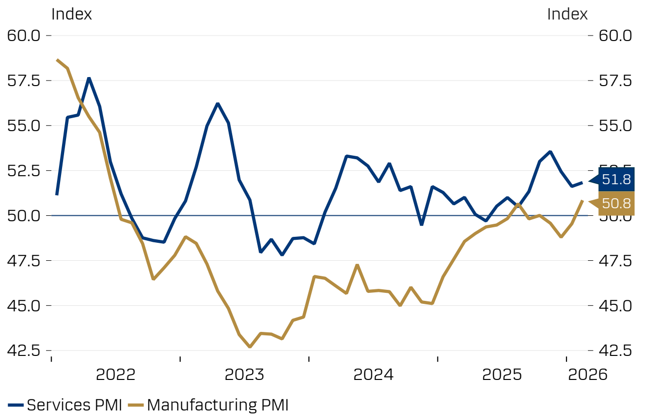
spend as confidence should gradually normalise over the forecast horizon. We expect investments to rise driven by the German fiscal package although a fading credit impulse in the euro area is suggesting only a gradual improvement. Funding from the German fiscal package started to fuel growth in the final quarter of 2025 and we therefore expect a rebound in activity to finally happen in 2026.

We still expect the southern European economies to be the fastest growing countries despite a German rebound as the strong rise in employment is fuelling private consumption and domestic demand, which again causes rising employment in a virtuous circle. Higher tax incomes also means that fiscal policy is tightened, which leaves the aggregate euro area fiscal stance neutral in 2026 and 2027 despite German easing and rising defence spending. We expect net export growth in 2026 to be negative due to the strengthened euro before turning neutral in 2027. Even with higher tariffs in the US, euro area exports to the US rose in 2025 and the trade balance was exactly the same as in 2024. We view the risks to the growth outlook as balanced since a stronger-than-expected boost to domestic production from rising defence spending could increase growth more than expected while a continued high household savings rate could result in lower than expected growth.

Inflation has returned below the ECB's 2% target due to lower energy prices and weaker momentum in underlying inflation. Core inflation is still slightly above target, but we expect it to fall below 2% next year due to easing wage growth and thereby services inflation. Goods inflation is set to remain low in 2026 due to the stronger euro but rising input prices from metals, energy prices, and a rebound in the manufacturing sector should give some upward pressures in 2027. The recent rise in energy prices due to the war in Iran is expected to drive inflation temporarily above target in the second and third quarter of 2026. Yet, commodity futures show only a temporary increase in prices so energy inflation is expected to decline again in the summer. At the same time declining wage growth will drive core inflation lower during the forecasting period. We thereby forecast headline inflation to average 2.1% y/y in 2026 and 1.8% y/y in 2027. We view the risks to the inflation outlook as tilted to the upside this year as energy prices could be higher than expected.

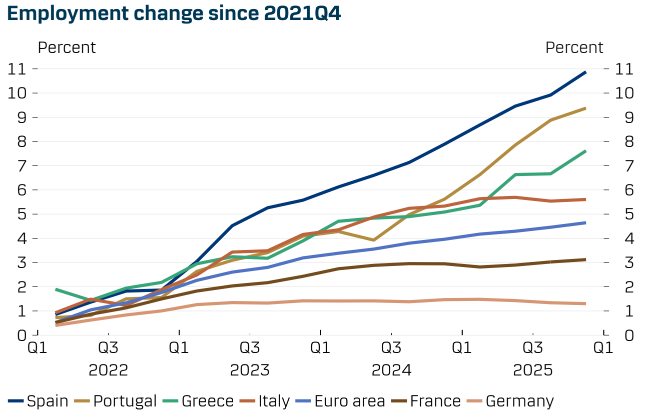
We expect the ECB to keep the policy rate unchanged at 2.00% in both 2026 and 2027. Although inflation is expected to temporarily overshoot the 2% target this year due to higher energy prices caused by the war in Iran, we view this as a temporary effect. We expect the ECB to look through it, given that growth is also hurt and as medium-term inflation expectations remain anchored. We view the risks to the ECB outlook as balanced since higher than expected energy prices that spills over to core inflation could force the ECB to hike while lower than expected activity and a quick decline in energy prices could warrant a cut.

Rebounding manufacturing activity



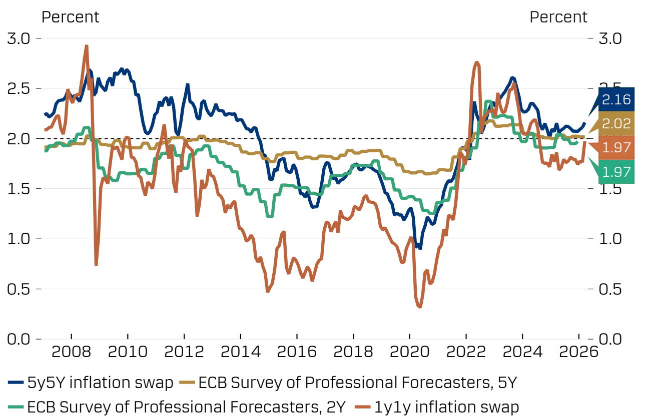
Source: S&P Global, Macrobond

Rising employment in Southern Europe creates virtuous circle



Source: Eurostat, Macrobond

Inflation expectations are anchored despite current undershooting



Source: ECB, Bloomberg, Macrobond

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