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Research Euro Area

A costly winter is coming

Europe's gas market is again in focus as the winter approaches, with prices sharply higher and inventories at record lows. The key question is how this will affect the economy and the ECB.

Europe enters the winter with record-high gas prices and record-low inventories. The EU benchmark gas price is around EUR 80/MWh, 150% higher than a year ago and its highest since January 2023. Inventories are 68% full, 12 percentage points below last year and the lowest on record. On the other hand, EU gas consumption is about 18% below pre-war levels, while higher US LNG supply provides some cushion. Even so, current inventories cover only around 31% of last winter's consumption—the lowest share since 2021 (see chart 2).

To estimate the economic impact, we calculated the additional gas cost for the coming heating season using current futures. **EU gas expenditure this winter is set to be EUR 117bn, or 0.6% of GDP, higher than last winter** (see chart 3)**.** This estimate assumes demand matches last winter and gas averages EUR 80/MWh, in line with futures. The extra cost will weigh on growth and push up prices for businesses and consumers.

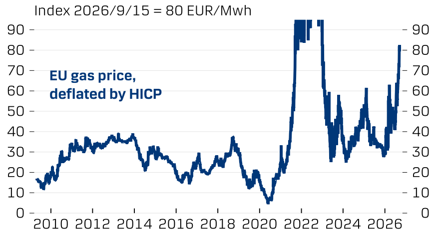
Extra gas costs of 0.6% of GDP could reduce winter growth by around 0.3 p.p., mainly in Q1 2027. The bulk of the effect should be on private consumption, as higher energy bills reduce real disposable income and thereby spending. So far, however, the euro area economy has been resilient: real private consumption grew 0.4% q/q in Q2 2026 despite higher energy costs. Consumers may initially have cut spending less because they expected the energy price increase to be temporary, but that now looks less likely. Our latest economic forecast from September 3 assumed winter gas prices of around EUR 70/MWh, so most of the impact is already included in our 2027 GDP growth forecast of 1.4%.

Yet, given the recent weeks' rise in broad energy products and our new ECB call of two additional hikes, we expect GDP growth next year closer to 1.1% y/y, although energy prices and thereby the degree of ECB tightening could move the forecast in either direction.

Euro area headline inflation to rise to 4% y/y during winter

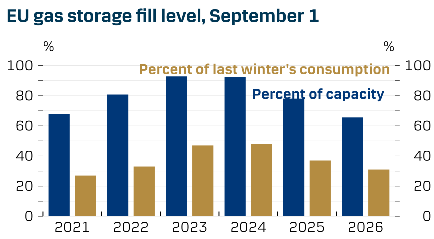
Higher energy costs will push inflation further above target in the coming months. Market pricing points to headline inflation of around 4% y/y from October to February, broadly matching the ECB staff's adverse scenario, which most closely reflects current energy futures (see chart 4).

Chart 1. Gas price more than twice as high as last year



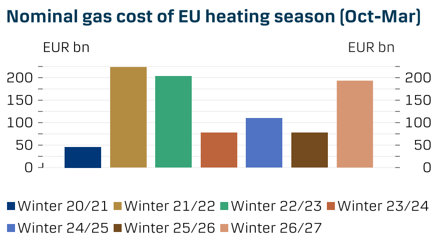
Source: Bloomberg, Eurostat, Macrobond, Danske Bank

Chart 2: EU gas inventories at record lows, even after adjusting for lower demand



Note: Fill level on September 1. Winter = Oct. to Mar.
Source: GIE, Eurostat, Macrobond, Danske Bank

Chart 3: EU to pay EUR 117 bn extra for gas this winter



Note: The Winter 26/27 estimate assumes gas demand as last winter and a price of EUR 80/MWh
Source: GIE, Eurostat, Macrobond, Danske Bank

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Transport fuels will drive most of the increase because the category has the largest HICP weight at 4% and costs pass quickly from wholesale to retail prices. Gas and electricity have smaller weights of 1.6% and 2.9% and a slower passthrough, as 59% of EU households have regulated or fixed-price contracts. In Germany, the share is 99% leading to an even slower passthrough.

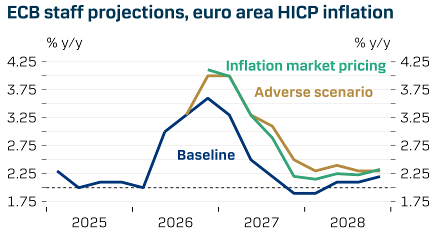
The main question is when indirect effects will appear in non-energy inflation; so far, they have not. We expect an impact on goods prices from higher production costs due to the global nature of the energy shock. We are more sceptical about effects on services inflation - outside of transportation costs - because labour demand and wage growth are weakening. Low consumer confidence may also make it harder for companies, especially food retailers, to pass higher costs on to consumers. We therefore see inflation market pricing and the ECB's adverse scenario forecast beyond the near-term prints as too high.

ECB to hike the deposit rate to 3.00% during winter

Higher gas prices are likely to prompt further ECB rate hikes. The September meeting revealed that the ECB is more focused on headline inflation and energy costs than on underlying inflation. Several Governing Council members have said that *"markets understand our reaction function well"*, and market pricing is closely correlated with energy prices (chart 5). Given the current energy outlook, we expect two additional 25bp hikes, taking the deposit rate to 3.00% by December, with risks tilted towards the hike at the October meeting being skipped or pushed to March.

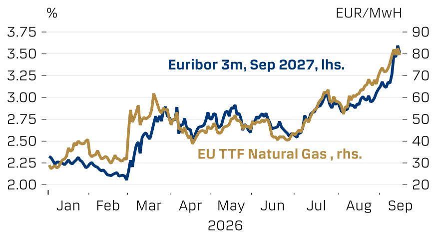
Risks to the energy and ECB outlook run in both directions. A milder winter or the reopening of the Strait of Hormuz could limit the ECB to one additional rate hike, which we would expect in December. A cold winter or further escalation in the Middle East could trigger a third hike in March. Beyond March, further hikes would be less likely in our view even in this severe scenario because even more demand destruction would weaken the labour market and wage growth, making the decision to hike further into supply shocks harder.

Chart 4: Inflation to hover around 4% during the winter



Source: ECB, Macrobond, Danske Bank

Chart 5: ECB pricing highly correlated with gas futures



Source: Bloomberg, Danske Bank

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This research report has been prepared by Danske Bank A/S ('Danske Bank'). The author of this research report is Rune Thyge Johansen, Senior Analyst.

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