

# 2026 Outlook: Energy price shock is weighing on Euro area growth

27 May 2026

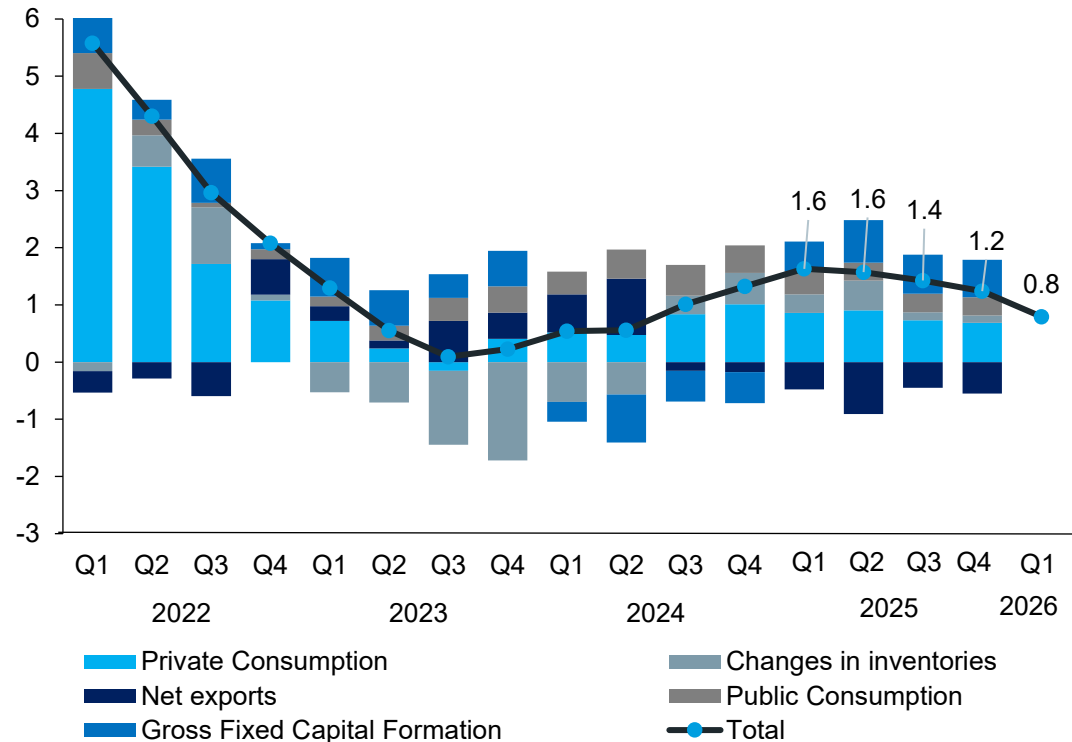
*Europe 360°: Strengthening the economy, shaping the future*

*Federation of German Industries (BDI)*

*Frederik Lange, Economics*

## 2 Euro area growth softens further – subdued start to 2026

### Contributions to GDP growth, Euro area (20)



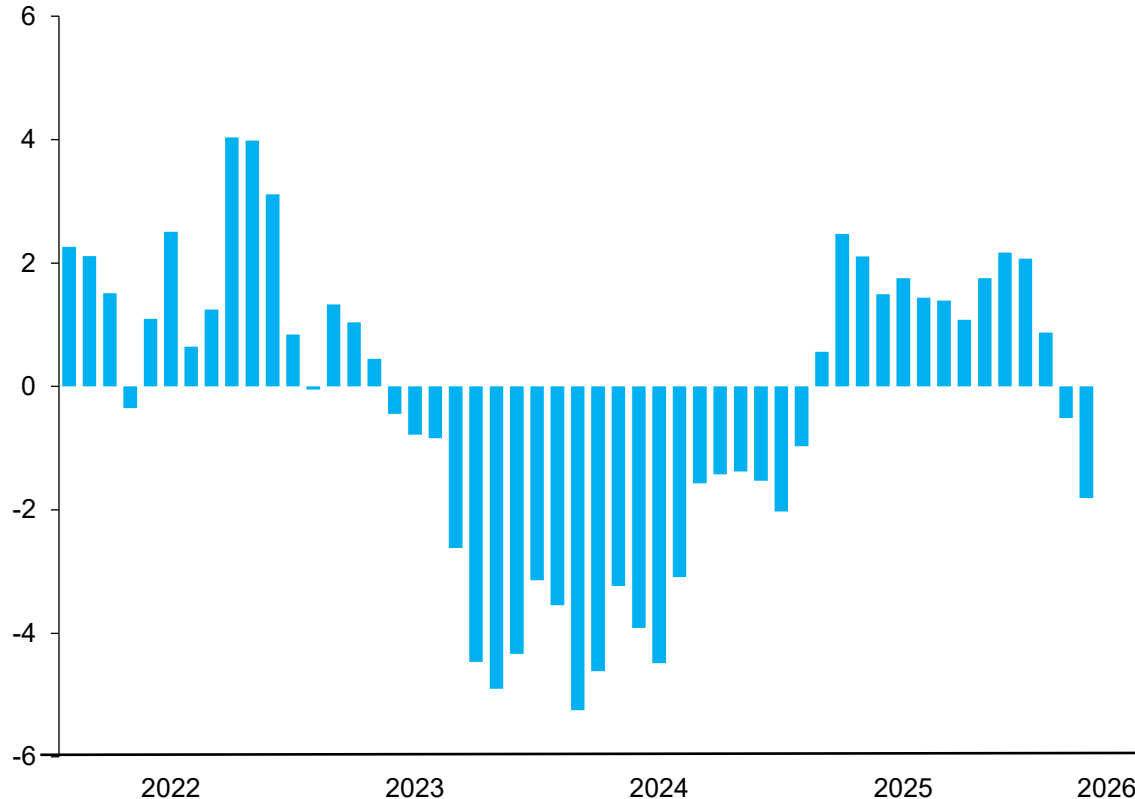
\*change over previous year, calendar and seasonally

Sources: Macrobond, ECB

- **Growth continues to decrease:** GDP rose by 0.8% year-on-year in Q1 2026 (down from 1.3% in Q4 2025), while quarter-on-quarter growth remained marginal at 0.1%
- **Geopolitical impact yet to fully feed through:** Despite already slowing growth, the effects of the recent Middle East conflict are not yet fully reflected, with higher energy prices and potential supply disruptions likely to intensify headwinds in coming quarters
- **Domestic demand remains the main driver:** Private consumption continued to underpin growth, while investment made a modest positive contribution; net exports weighed on activity amid rising trade tensions

### 3 Industrial momentum weakens again – recovery remains fragile

#### Industrial production, Euro area



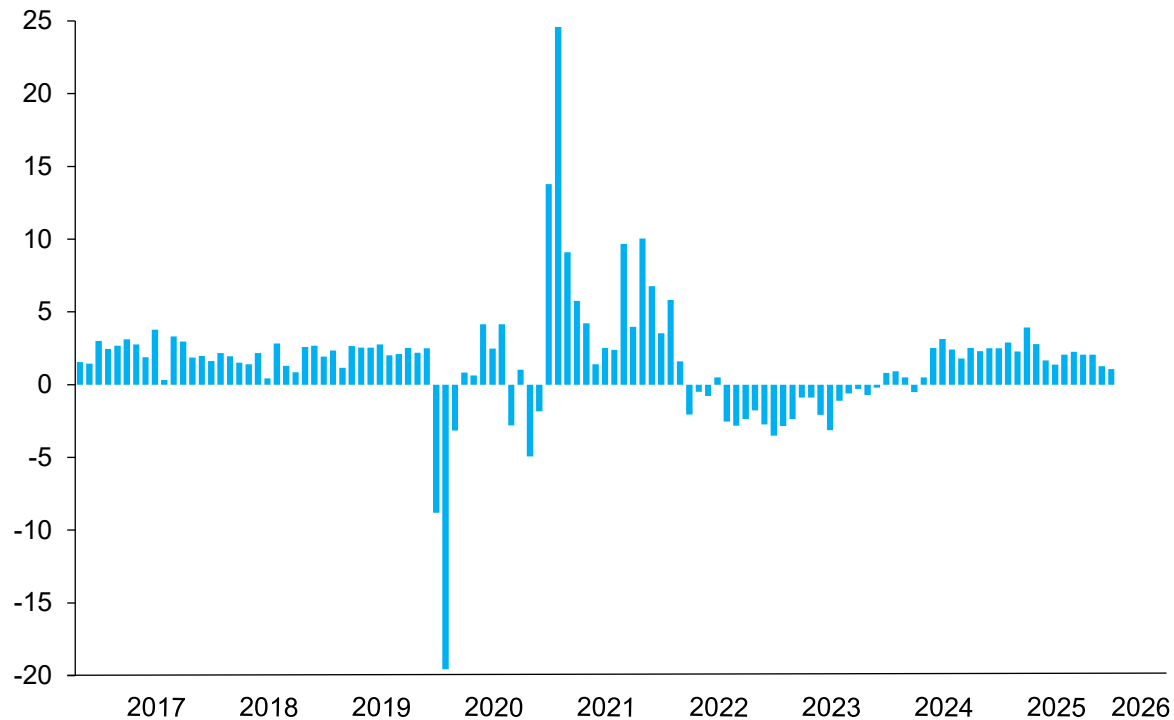
\*Volume index, 2-month-average, seasonally adjusted

Sources: Macrobond, Eurostat

- **Partial recovery followed by renewed weakening:** After a prolonged decline (mid-2023 to early-2025), industrial production recovered through 2025 (1.6% average growth), but has declined again since February 2026
- **Capacity utilisation remains subdued:** Utilisation edged up to 78.5% at the start of Q2 2026, but remains below the 10-year average (80.3%), pointing to continued slack in the industrial sector
- **Recovery still lacks strength:** The combination of renewed production declines and below-average utilisation suggests that the industrial upswing has not yet become firmly established

## 4 Retail sales growth moderates after a recovery phase

### Euro area (20) retail trade (excl. motor vehicles)



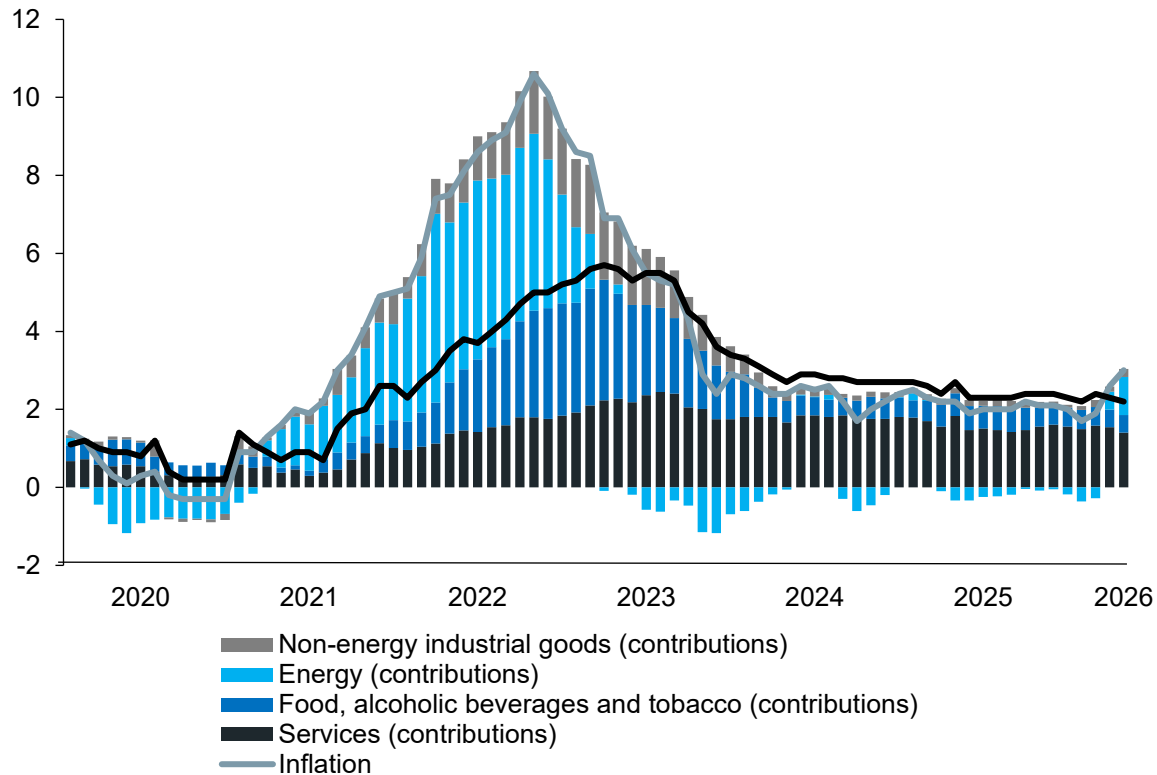
\*change over previous year, calendar and seasonally adjusted

Sources: Macrobond, Eurostat

- **Strong expansion before the slowdown:** Retail sales grew steadily from March 2024, with particularly strong momentum of around 2.6% between August 2024 and July 2025
- **Momentum has weakened since mid-2025:** Growth has gradually slowed, declining from around 1.7% to 1.1% by March 2026
- **Growth remains positive but subdued:** Retail activity continues to expand, but at a clearly reduced pace compared to the previous peak phase

## 5 Inflation rises again – energy prices drive renewed pressures

### Inflation Contributions\*, Euro area



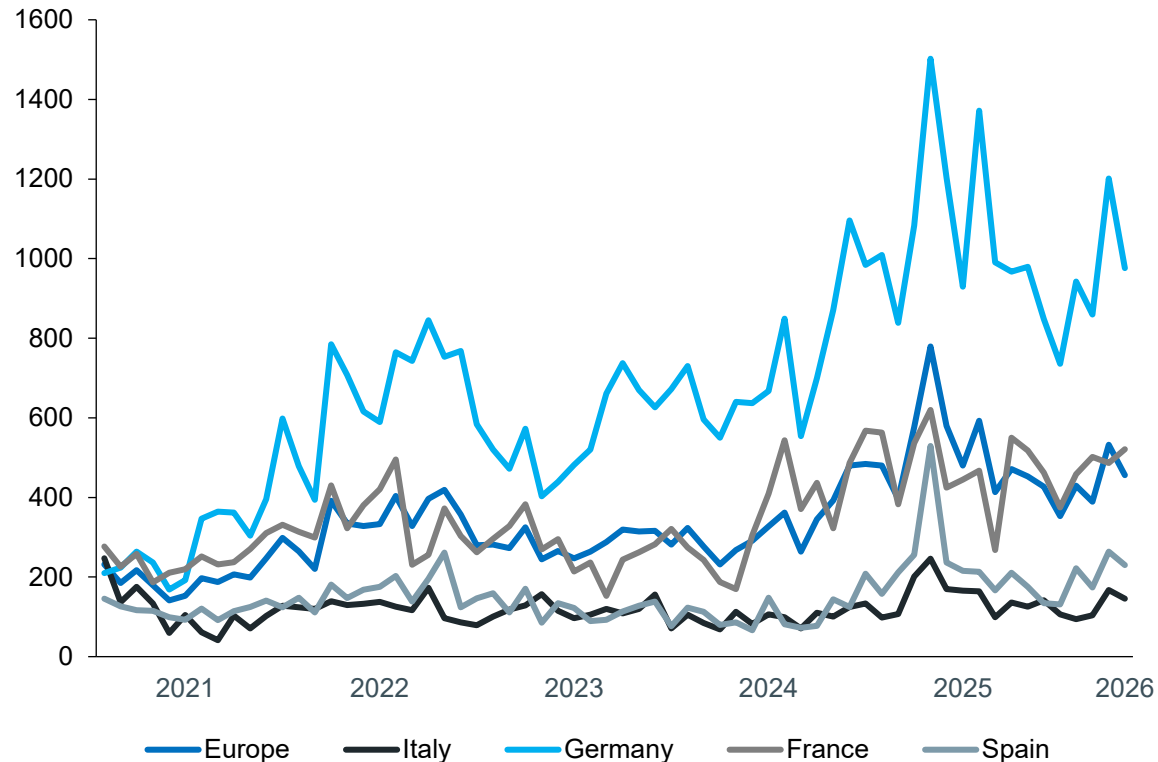
\*Change over previous year

Sources: Macrobond, European Central Bank

- **Headline inflation picks up:** Inflation increased to 3.0% in April 2026 (from 2.6% in March), after having been below target at the start of the year
- **Energy prices as the key driver:** The rise is mainly due to a sharp surge in energy inflation (10.8% in April), linked to the recent geopolitical shock
- **Underlying inflation remains contained:** Core inflation declined to 2.2%, with services, goods and food prices showing only moderate dynamics
- **Mixed picture across countries:** Inflation rates vary significantly across member states, reflecting differences in energy exposure and national price dynamics

## 6 Uncertainty rises as forward-looking indicators weaken

### Economic policy uncertainty index\*



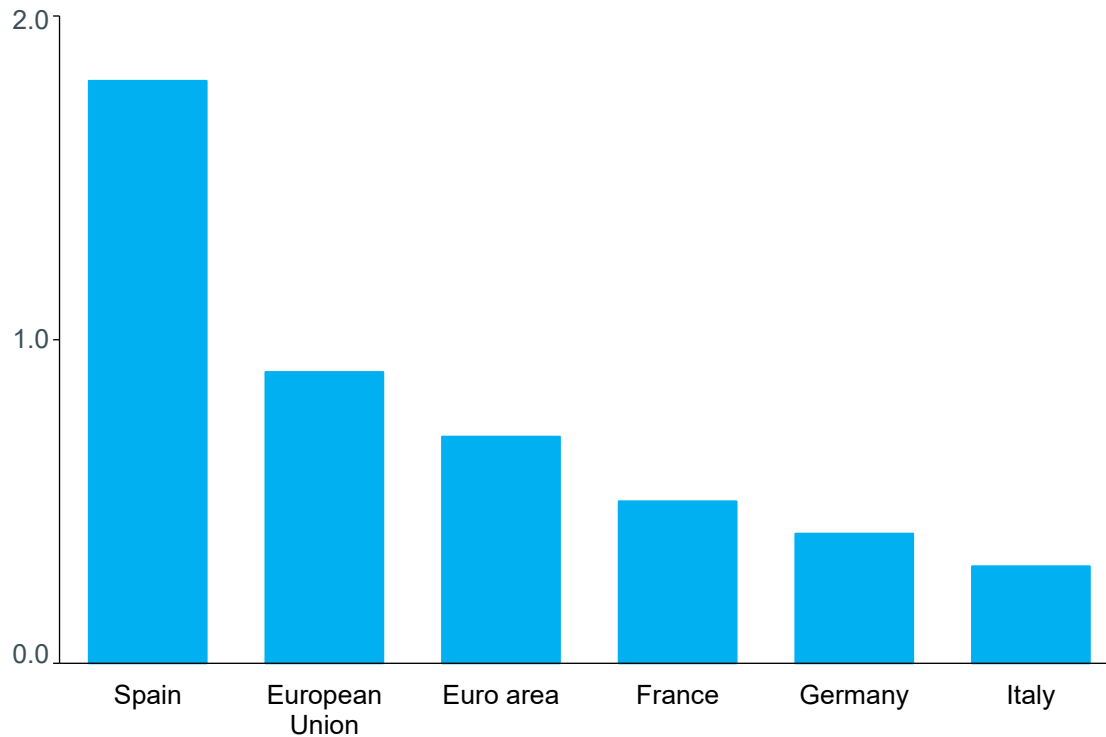
\*news-based indices

Sources: Macrobond, Economic Policy Uncertainty

- **PMI signals contraction:** The Composite Eurozone PMI fell to 47.5 in May, remaining below the expansion threshold for the second consecutive month
- **Weakness in both sectors:** Both manufacturing and services declined, with a more pronounced drop in services
- **Costs are elevated as activity weakens:** Input prices increased sharply, outpacing selling prices and putting pressure on margins – pointing to stagflationary tendencies
- **Uncertainty increases:** Economic policy uncertainty has picked up again recently and remains elevated, reflecting ongoing geopolitical and trade tensions

## 7 Euro area growth expected to slow markedly in 2026

### Growth forecast for 2026: EU, Euro area and Big-4

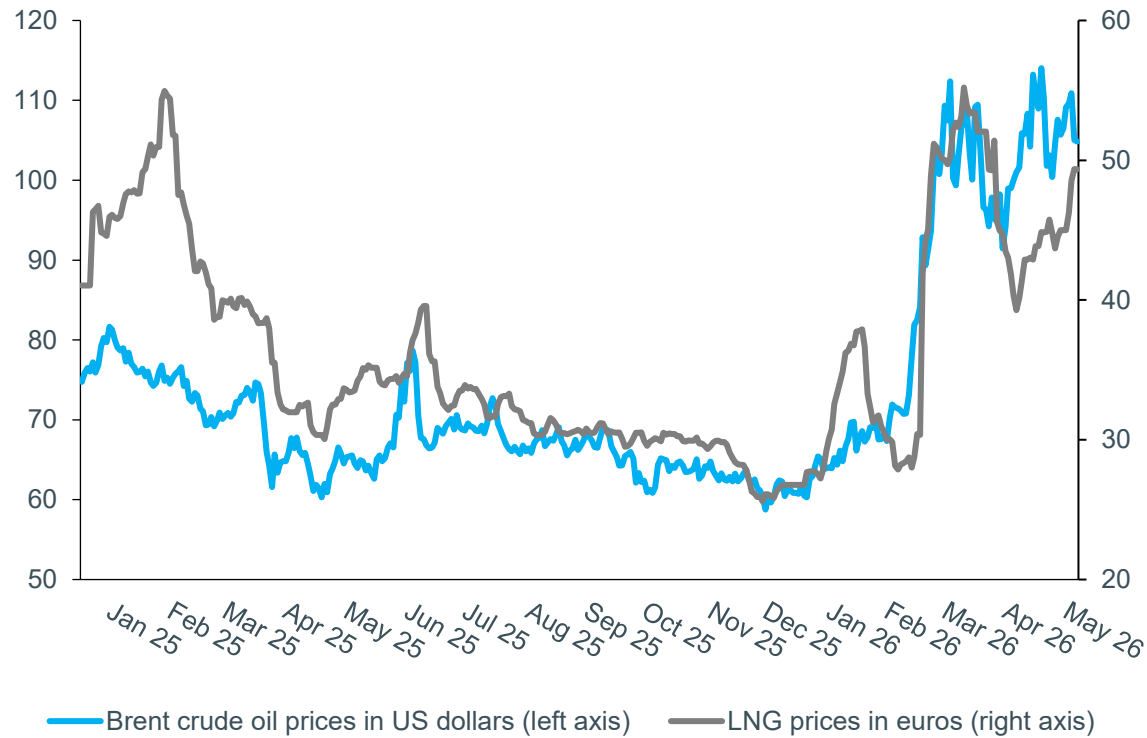


Source: BDI

- **Baseline:** Growth is expected to slow to 0.7% in 2026 (from 1.4% in 2025), remaining below potential and weaker than in most international forecasts
- **Drivers:** Domestic demand remains subdued, with weak consumption and investment, while net exports act as a drag
- **Policy mix provides limited support:** Neutral to slightly restrictive monetary policy and only slightly expansive fiscal stance (support in some countries, consolidation in others)
- **Risks remain tilted to the downside:** primarily driven by geopolitical developments and energy market uncertainty

## 8 Iran conflict remains the key risk for the 2026 outlook

### Price developments for oil and gas (Brent & LNG) (1 January 2025 – 21 May 2026)



Source: Macrobond

- **Transmission channels:** Higher energy prices, elevated uncertainty, tighter financing conditions, and global spillovers via trade and supply chains
- **Key uncertainty:** Level and persistence of the energy shock
- **Recent developments:** Oil (50-55%) and LNG gas (~30%) above 2025 levels in Q2 (average to 21 May), with no clear sign of rapid normalisation
- **Market pricing may be too optimistic:** Energy futures imply declining prices, but likely underestimate persistence given low liquidity and high uncertainty

## 9 Our scenarios for the Euro area in 2026

Scenario	Conflict dynamics	Channels	Macro impact
<b>Upside</b>	Rapid de-escalation, stabilisation of supply routes (incl. Hormuz)	Energy prices decline quickly (oil <100 USD), uncertainty falls, financing conditions ease	Growth 0.8-1.0%; consumption and investment recover slightly
<b>Baseline</b>	Gradual stabilisation, no major new disruptions but sustained tensions	Energy prices ease only gradually and remain elevated through 2026, uncertainty and financing conditions remain somewhat restrictive	Growth 0.7%; subdued domestic demand, below potential
<b>Downside</b>	Prolonged or renewed escalation, persistent disruptions to energy supply and transport	Energy prices remain high or increase further through 2026 (especially gas), with persistently high uncertainty and tighter financing conditions	Growth 0.2-0.4%, with risk of stagnation as consumption and investment weaken

→ ***Risks are clearly skewed to the downside, with limited upside and a tangible risk of stagnation in adverse scenario***

# Global macroeconomic environment – key assumptions

## 10 underpinning our outlook

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- **Strong momentum before the shock:**
  - Global growth remained robust into early 2026, supported by private demand and strong investment (incl. technology/AI)
  - Without the energy shock, growth in 2026 would likely have been revised upwards (~+0.3pp)
- **Energy shock weakens outlook:**
  - Higher energy prices reduce real incomes and increase production costs, while rising uncertainty and tighter financial conditions weigh on consumption and investment
- **Moderation in global growth:**
  - Growth is expected to slow to 2.9-3.1% in 2026 (from 3.3-3.4% in 2025), with the energy shock acting as the main drag
- **Global trading environment weakens:**
  - Tariffs, geopolitical uncertainty and structural competition (notably from China) weigh on trade; after strong growth in 2025, global trade is expected to slow markedly in 2026

# 11 Fiscal policy: Moderate support, constrained by limited fiscal space

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- **Slight fiscal impulse:**
  - Euro area fiscal stance remains slightly expansionary (0.3% of GDP in 2026, ECB), primarily driven by public investment (incl. defence, infrastructure) and ongoing EU programmes
- **Uneven contribution across countries:**
  - Stronger expansion in Germany, while several large economies (e.g. France, Italy) face consolidation needs
- **Limited and largely broad-based energy measures:**
  - Fiscal response to the energy shock remains small (0.1-0.3% of GDP) and mainly broad-based, supporting incomes but with limited targeting
- **Worsening public finances:**
  - Deficits rise to around 3.4% of GDP, while debt reaches ~88% (ECB; Commission somewhat higher), mainly due to higher interest payments and structural pressures
- **Constrained policy space:**
  - Fiscal rules allow flexibility (e.g., targeted use of escape clauses), but application remains selective and politically constrained, limiting scope for additional support

# 12 Monetary policy: Balancing elevated inflation pressures and weakening growth

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- **Energy shock creates policy trade-off:**
  - As a supply-driven shock, higher energy prices raise inflation in the short term while weakening activity; this creates a trade-off between looking through temporary inflation pressures and preventing potentially more persistent inflation dynamics
- **Transmission of the shock remains uncertain:**
  - Inflation is still driven primarily by direct energy effects, while indirect effects are emerging; second-round effects are not yet evident, but remain a key risk
- **Data-dependent, meeting-by-meeting approach:**
  - The ECB has kept rates unchanged so far (2.0% deposit rate) and continues to assess incoming data without pre-commitment to a rate path
- **Non-linear rate outlook:**
  - A (stronger) transmission into underlying inflation could require (further) tightening, while a severe growth slowdown could ultimately lead to easing despite temporarily higher inflation
- **Financing conditions have tightened:**
  - Higher risk premia, rising market rates and tighter credit standards are already restricting financing, partly substituting for additional policy tightening

## 13 Summary and policy recommendations

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- **Euro Area Growth Outlook:**

- **Fragile macro environment:** Growth remains weak and highly uncertain, shaped by the energy shock, tighter financing conditions and external headwinds, while structural weaknesses limit medium-term growth prospects
- **Risks clearly skewed to the downside:** The outlook depends critically on energy markets; persistent disruptions could lead to stagnation or even recession, while upside remains limited
- **Policy support remains constrained:** Monetary policy faces a trade-off from a supply shock, while fiscal space is limited, implying only partial stabilisation of the shock

- **Policy Recommendations:**

- **Deepen the Single Market:** Strengthen integration in services, energy and digital markets and reduce regulatory frictions
- **Accelerate structural reforms:** Simplify regulation, reduce administrative burdens and modernise labour and product markets
- **Mobilise investment and close the investment gap:** Improve conditions for private capital and better align public and EU funding with strategic priorities
- **Strengthen resilience in trade and energy:** Advance trade diversification and market access, address global distortions and overcapacity, and ensure secure, competitive and resilient energy supply

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