Economics
Chart of the Week

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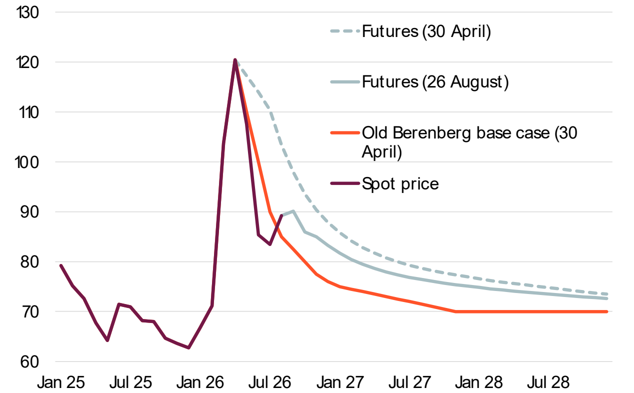
28 August 2026

Forecast change: extended Iran shock = more pain and higher rates

Higher for longer: oil price per barrel Brent crude, in $



Spot and futures prices per barrel Brent crude, in $. Our new base case is close to the 26 August 2026 futures. Sources: Bloomberg, Berenberg.

- **Pain in the pipeline:** Since late April, we had based our economic forecasts on the assumption that the price of Brent crude would decline to $75 by the end of this year. This forecast assumed traffic through the Strait of Hormuz would gradually recover from the near-closure after the start of the Iran war. Until mid-July, oil prices normalised even a bit faster than we had anticipated. At the margin, this may have contributed to the upside surprise in Eurozone and UK growth in Q2. But that luck seems to have run out. While active hostilities with heavy mutual bombardment may be over for now, the Strait of Hormuz remains virtually closed with no apparent resolution in sight. Current oil prices and futures are now higher than we had assumed in April – see chart. We adjust our forecasts accordingly, pushing back the call for the oil price to return to $75 from end-2026 to summer 2027. Our new assumptions are roughly in line with the futures curve.
- **Consumers pay the price:** In addition to more elevated oil prices, more expensive natural gas (now c45% above its late April level) will hurt consumers this winter. Likely food supply constraints due to the European summer drought and the almost complete interruption of Russian and Ukrainian grain exports amid persistent mutual strikes will exacerbate the pain for consumers. We thus raise our near-term forecasts for Eurozone inflation by up to 0.3 percentage points, bringing the call for Q1 2027 from 2.4% to 2.7% yoy. For 2027 as a whole, we now project 2.2% instead of 1.9%. As higher energy and food prices curtail the gains in real disposable incomes, we lower our call for Eurozone growth (ex Ireland) from 1.4% to 1.3% for 2027 after 1.1% in 2026. With gradually receding energy prices and the unfolding German fiscal stimulus, growth could then accelerate to an above-trend 1.6% in 2028 (unchanged).
- **Another ECB mistake in the making:** Central banks cannot do anything about adverse supply shocks. They should not react with rates to the direct effects of such disruptions, which raise prices but hurt growth at the same time. Like the European Central Bank (ECB), we have not yet seen any evidence of major second-round effects such as an acceleration in wage pressures or in non-energy related components of core inflation. As we had argued in June already, we thus see no reason for higher rates. Unfortunately, the ECB seems to be leaning towards repeating its June mistake by raising rates again by 25bp on 10 September. For example, ECB Executive Board member Isabel Schnabel has argued that the ECB needs to tighten policy ahead of potential second-round effects even if they have not materialised (yet). We thus now join the market consensus in predicting a 25bp rate hike on 10 September. Thereafter, we project a long ECB pause until above-trend growth in 2028 could pave the way for two final hikes in late 2028 and early 2029 to a 3% deposit rate – see our Forecasts at a Glance for the full set of our calls.
- **UK outlook:** More resilient aggregate demand than we expected and higher natural gas prices than we assumed cause us to raise our forecast for UK inflation from 2.7% to 2.9% yoy for Q1 and from 1.9% to 2.2% for Q2 2027. Elevated energy and – possibly – food prices will likely delay the return of inflation to the central bank's 2% target from Q2 to the second half of 2027. As a result, we drop our call for a 25bp rate cut in December. The Bank of England (BoE) can afford to wait longer to ease policy as modest growth reduces the risk of a sharp deterioration in the labour market, while higher energy bills keep the hawks on edge.
- **BoE cuts to come – but later:** We still expect the BoE to resume rate cuts eventually, albeit a few months later than we previously forecast. Resilient growth in 1H 2026 has not fed through to an increase in labour demand. As a result, disinflation in wage growth and underlying price pressures remains on track. We now project two instead of three 25bp cuts, one each in Q1 and Q2 next year, to take the policy rate from the current 3.75% to 3.25% by mid-2027.

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