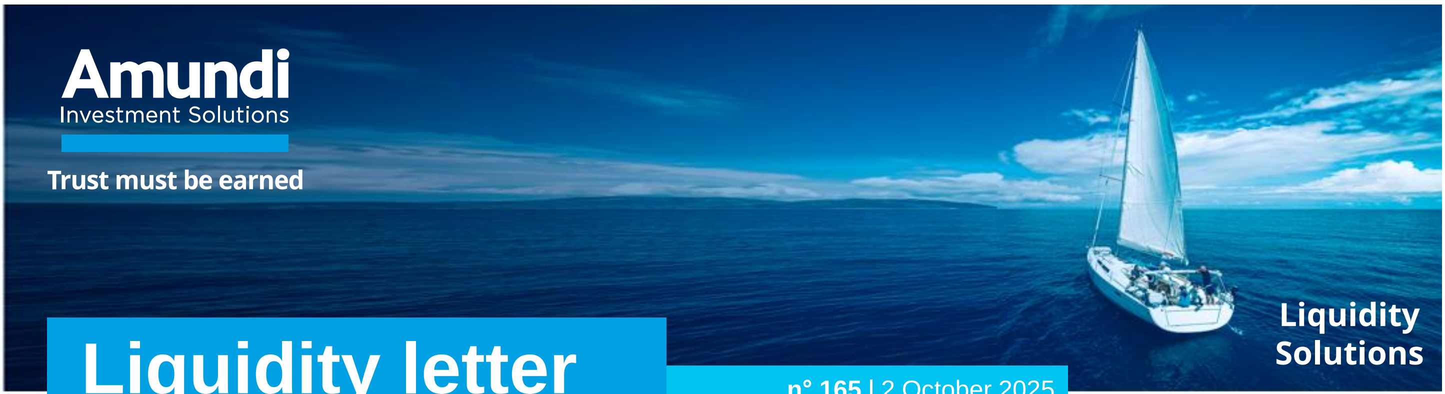


Liquidity letter

n° 165 I 2 October 2025

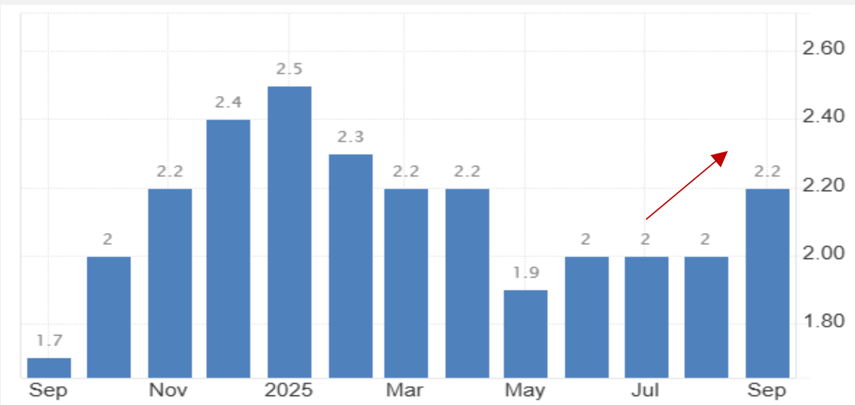
Persistent inflation in the Eurozone

Consumer prices rise to 2.2% at the end of September

According to Christine Lagarde, inflation is at the desired level.

- **Inflation** in the Eurozone reached 2.2% in September 2025, slightly above the ECB's 2% target. Core inflation, excluding energy, food, alcohol and tobacco, remains stable at 2.3%, its highest level since January 2022.
- **The ECB** is keeping its key rates unchanged, with a deposit rate at 2%, and forecasts average inflation to remain stable at around 2% until 2027. Economic growth is revised upwards for 2025, to 1.2%, with a flexible data-driven approach.
- **Martin Kazaks** said rates will remain at 2% in the absence of a new economic shock, with significant uncertainty about future developments. The ECB retains "freedom of action" to adjust rates if necessary.
- **In the UK,** inflation remains high, peaking at 4% in September 2025, making it difficult for the Bank of England to reduce inflation without causing a recession. The monetary committee is deeply divided on interest rate policy**.**

Inflation trends in the euro area



Source: EUROSTAT: 01/10/2025

Eurozone consumer price inflation reached 2.2% in September 2025, up from 2.0% in the previous three months, slightly above the ECB's 2.0% target, according to preliminary data. Services inflation edged up from 3.1% to 3.2%.
Meanwhile, core inflation, which excludes energy, food, alcohol and tobacco, remained stable at 2.3%, remaining at its lowest level since January 2022.

Figure of the week

2,2%

This is the inflation rate in the Eurozone at the end of September

Christine Lagarde

The eurozone economy is holding up better than expected to the US tariffs, leaving inflation risks "quite limited", ECB President **Christine Lagarde** said on Tuesday.

Frankfurt has kept interest rates unchanged since June and has indicated that it is in no hurry to adjust monetary policy further, given that the economy is doing well and inflation is now around its 2% target.

"As expected, inflation risks appear to be fairly limited on both fronts. With benchmark interest rates at 2%, we are in an optimal position to respond if inflation risks change or if new shocks threaten our target."

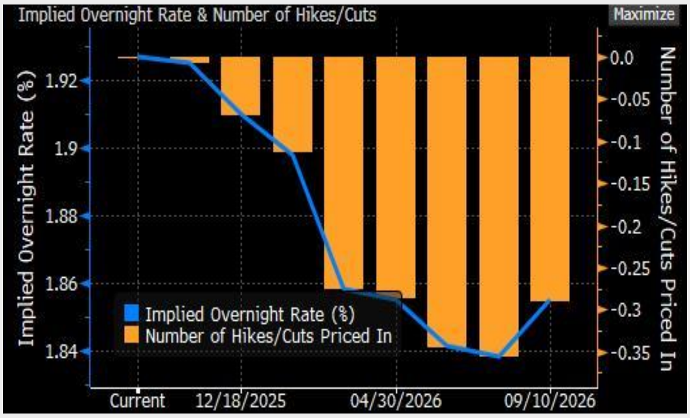
Lagarde said trade shocks were not creating new inflationary pressures and that the ECB was therefore not facing the classic trade-off of managing a period of slowing growth and rising prices.

Kazaks (ECB): rates will remain at 2% in the absence of a new shock

According to **Martins Kazaks**, a member of the Governing Council of the European Central Bank, the European Central Bank can keep its interest rates unchanged unless the economy suffers a new shock.
If nothing significant happens, rates can stay at their current level, but of course there is a lot of uncertainty," Kazaks said in an interview on Thursday.
"From the current perspective, the ECB's 2% rate is entirely appropriate.
" The comments bolster the view that the ECB will maintain the current level of borrowing costs after cutting them in half in the space of a year as inflation eased and the economy faced trade-related headwinds. Commenting on the price outlook, Kazaks said that "right now, I would say there are risks in both directions."
The ECB "keeps its eyes open" at every meeting and has "complete freedom of action" if rates need to rise or fall, he said.

> *Inflation is where we want it to be*
>
> *Christine Lagarde, 30 September 2025*

ECB



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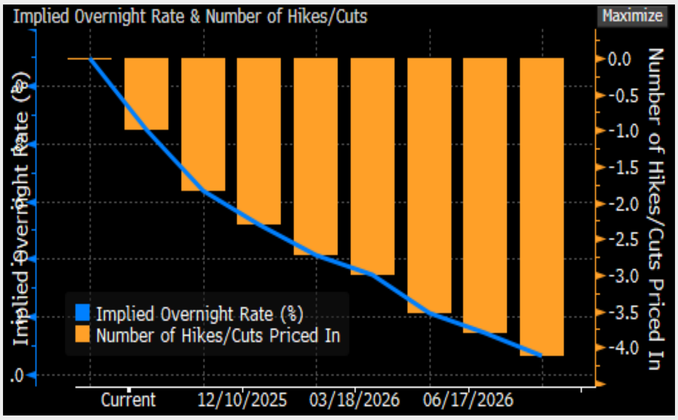

Source: Bloomberg 02/10/25

Market expectations for the evolution of interest rates in the euro area estimate that the ECB has completed its monetary easing cycle, after cutting the deposit facility rate by 2%, from 4% to 2%.

Indeed, the probability of a further rate cut is reduced to 35% and is not expected to occur before the second half of 2026.

Moreover, the recent data published on inflation in the euro area, at 2.2%, supports this position of the ECB.

On the American side, the situation is totally different. After cutting rates by 25 basis points two weeks ago, after a nine-month pause, the cycle of cuts seems far from over.

Markets are pricing in at least four more rate cuts by the end of 2026.

Under this scenario, the Federal Reserve's terminal rate could be around 3% in September 2026.


John Williams, Fed New York

WILLIAMS, FED: SUPPORTING THE JOB MARKET

New York Fed President **John Williams** said emerging signs of weakness in the labor market prompted him to support an interest rate cut at the central bank's last meeting.
"It made sense to cut interest rates slightly" and "ease restrictive policy a little" to help ensure a healthy labour market while maintaining some downward pressure on above-target inflation levels.
Williams' comments on Monday were his first public statements since the central bank's FOMC meeting in mid-September, which met market expectations, with officials cutting their overnight rate target range by a quarter of a percentage point, bringing it down to between 4% and 4.25%.
The Fed justified its rate cut by the growing risks to the labor market, even if inflation remains above target.

UK: Hard work for the central bank

Inflation in the UK is too high and the BoE will have to follow a difficult trajectory to bring it down without triggering a painful recession that would affect employment.

BoE deputy governor Sarah Breeden said inflation is expected to peak at 4% in September due to higher food and energy prices, as well as higher payroll taxes and administered prices.

Moreover, according to Catherine Mann, an external member of the BoE's Monetary Policy Committee, households' expectations for future inflation had clearly moved away from the official 2% target.

In this situation, policymakers "have a lot more work to do" to restore price stability and regain credibility.

These comments reflect the Monetary Policy Committee's concern that the UK is becoming a special case among developed economies due to persistently high inflation.

Deeply divided when it decided to cut interest rates in August, in September, the BoE voted by a clear 7-2 vote to keep borrowing costs at 4%, and market participants do not expect any further changes until the end of the year.

Topicality

- **Australia** | The central bank maintains its Stable rates at 3.60%
- **Germany** | Manufacturing PMI declines less than expected at the end of September at 49.5

Agenda

- **8 October** l New Zelande Central Bank decision on interest rate
- **8 October** l Publication of the minutes of the last meeting of the Federal Reserve

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