



Middle East war – all good now?

Signs of an impending peace agreement between Iran and the U.S. are mounting, even though setbacks like last night's exchange of fire are always possible. We analyze what a peace agreement would mean for the economy, inflation, the ECB, and the financial markets.

Dr. Jörg Krämer^{AC}

Hope, but a bumpy road to peace

The U.S. news website [Axios](#) reported on Wednesday that the U.S. and Iran are on the verge of a peace agreement. There is reportedly a document outlining Iran's gradual reopening of the Strait of Hormuz, the end of the U.S. blockade of Iranian ports, and Iran's commitment to refrain from building nuclear weapons, with the U.S. in return lifting sanctions against the country and releasing billions of dollars in frozen funds. The details would need to be negotiated based on this document. Financial markets reacted euphorically to the prospect of peace; at times, the price of Brent crude fell below \$100, and stock prices soared.

So far, there has been no official confirmation of an imminent peace agreement. In recent months, there have been repeated setbacks, such as following the alleged opening of the Strait of Hormuz in mid-April. After all, the positions of the two protagonists are far apart, and mistrust runs deep. We continue to expect a bumpy road to peace. Nevertheless, it is possible that a breakthrough will be achieved soon. We take this as an opportunity to analyze what a peace agreement would mean economically.

Growth: The damage has already been done, but there is no recession

Even if a peace agreement were reached quickly now, the Strait of Hormuz would have been blocked for nearly three months. During that time, the price of Brent crude oil remained well above \$100 for the most part. That represents an increase of more than 50%. The increase is even steeper for natural gas.

Even with a swift peace agreement, energy prices are unlikely to return to their pre-war lows. According to the International Energy Agency, repairing the energy infrastructure and returning to the pre-war production levels will take up to two years, so the supply of oil and natural gas is likely to remain lower than before the war for some time. Added to this is the risk that the conflict could flare up again, which points to higher risk premiums for energy prices.

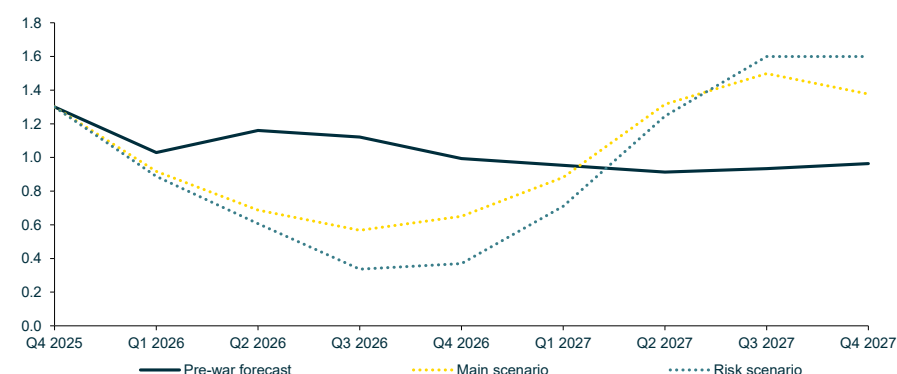
This development largely aligns with our long-standing baseline scenario. For this scenario, our model simulation suggested that the rise in energy prices would dampen economic growth this year by 0.4 percentage points for both Germany and the eurozone (chart 1). Consequently, we lowered our growth forecasts for both regions to 0.6% six weeks ago.

The data released so far supports this forecast. For instance, the composite Purchasing Managers' Index (PMI) for the eurozone has fallen to a level at which recessions have been observed in the past. The Ifo Business Climate Index has also plummeted for two consecutive months. Furthermore, rising oil prices and uncertainty have also dampened consumer sentiment – the GfK consumer climate fell significantly in April.

All in all, we would not raise our growth forecast for Germany and the eurozone even if the conflict were to be resolved soon. However, a permanent reopening of the Strait of Hormuz would prevent a dangerous risk scenario – and thus a recession.

Chart 1 - Euro area: Iran war lowers growth rate by 0.4 percentage points

Real GDP, year-over-year change in percent; main scenario: 3-month oil price of \$110, gas price of €50; risk scenario: 9-month oil price of \$120, gas price of €60





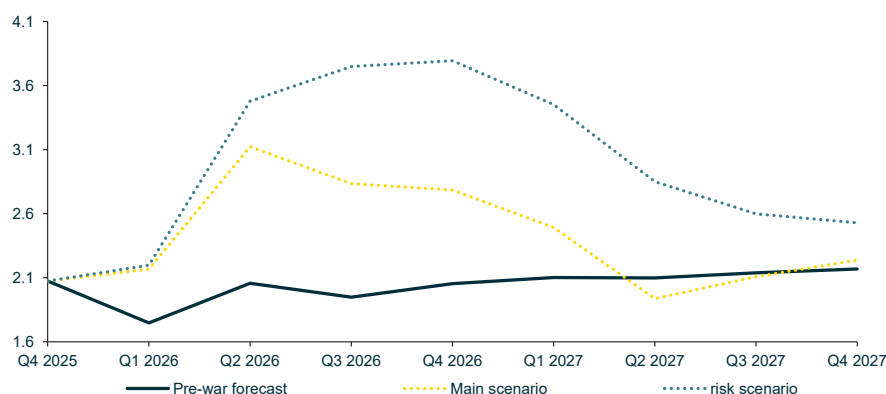
Inflation: Peak to Be Reached Soon

The sharp rise in energy prices pushed inflation in the eurozone up to 3.0% in April. Surveys of purchasing managers suggest that companies will respond quickly to the surge in costs and raise their selling prices. Inflation excluding energy and food is also likely to pick up in the coming months.

According to our model simulation, even if the U.S. and Iran reach a quick agreement and energy prices subsequently fall significantly, the inflation rate in the eurozone would rise to 3¼% by early summer and then gradually decline back toward the 2% mark (chart 2). This means there is no reason to change our inflation forecast published six weeks ago (2026: 2.7%).

Chart 2 - Eurozone - Inflation peak will be soon reached

Harmonized Consumer Price Index, year-over-year change in percent; for Commerzbank's assumptions regarding oil and natural gas prices, see Chart 1



Source: Bloomberg, Commerzbank Research

ECB: No Three Rate Hikes

At its meeting last week, the ECB signaled that it might raise interest rates at its next meeting in June. The ECB will likely go ahead with this decision to address the increased risks of inflation, although such a move would be less certain if tensions in the Persian Gulf ease rapidly.

Otherwise, we continue to believe that the ECB will not raise its key interest rates further in the months leading up to the end of the year. Even at the height of the Iran crisis, we did not believe in the up to three rate hikes that the futures markets had temporarily priced in. Ultimately, the ECB Governing Council is dominated by proponents of a fundamentally loose monetary policy (doves), especially since policymakers want interest rates as low as possible due to very high government debt.

The Implications for Financial Markets

Stock markets had consistently anticipated a relatively swift peace agreement and – following initial significant price declines – have reached new highs, particularly in the U.S. If the Strait of Hormuz were to remain open permanently, the remaining risks of recession would be averted and corporate profits would continue to rise – especially in the U.S. This points to favorable conditions for stocks, especially since an end to the war would make a case for U.S. interest rate cuts toward the end of the year more than ever.

The dollar had initially gained significantly due to the war but had already given up those gains by early April; EUR-USD subsequently rose. In the coming quarters, EUR-USD is likely to further trend upward primarily because the Federal Reserve, under the new Fed Chair Kevin Warsh, is likely to eventually yield to political pressure for lower interest rates, thereby compromising its independence.

Ten-year German government bonds are likely to benefit from a peace agreement, as inflation risks would decline in that scenario and markets would likely scale back their expectations for ECB rate hikes. In the medium term, however, bond yields are likely to rise – due to excessive budget deficits in most Western countries and the erosion of central bank independence.



Analysts

^{AC}
Dr. Jörg Krämer
Chief Economist
+49 69 136 23650
joerg.kraemer@commerzbank.com

^{AC}
Bernd Weidensteiner
Senior Economist
+49 69 9353 45625
bernd.weidensteiner@commerzbank.com

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Frankfurt

Commerzbank AG
DLZ - Gebäude 2, Händlerhaus
Mainzer Landstraße 153
60327 Frankfurt
Tel: + 49 69 136 21200

London

Commerzbank AG
PO BOX 52715
30 Gresham Street
London, EC2P 2XY
Tel: + 44 207 623 8000

New York

Commerz Markets LLC
225 Liberty Street, 32nd floor,
New York,
NY 10281-1050
Tel: + 1 212 703 4000

Singapore

Commerzbank AG
128 Beach Road
#17-01 Guoco Midtown
Singapore 189773
Tel: +65 631 10000