
March 20, 2026

Commentary

Weekly Economic Perspectives

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Contact

Simona Mocuta
Chief Economist
simona_mocuta@statestreet.com

Amy Le
Macro-Investment Strategist
amy_le@statestreet.com

Krishna Bhimavarapu
Economist
VenkataVamseaKrishna_Bhimavarapu@statestreet.com

Weekly Highlights

Central banks get inflation jitters amid Iran war, but reactions may be overdone.

US: Fed Funds Rate
(Upper)

3.75%

More hawkish tone.

US: Philly Fed Index
(Mar)

18.1

Six-month high.

EZ: ECB Main
Refinancing Rate

2.15%

On hold.

BoC: Policy Rate

2.25%

No real surprises.

BoE: Policy Rate

3.75%

On hold with hawkish tone.

UK: Average Weekly
Earnings (Jan, 3m y/y)

3.9%

In line with expectations.

JP: BOJ Policy Rate
(Mar)

0.75%

(When) Will it get to 1.0%?

AU: Unemployment Rate
(Feb)

4.3%

Even higher than our estimate!

AU: Full-Time
Employment (Feb)

-30,500

Payback from January.

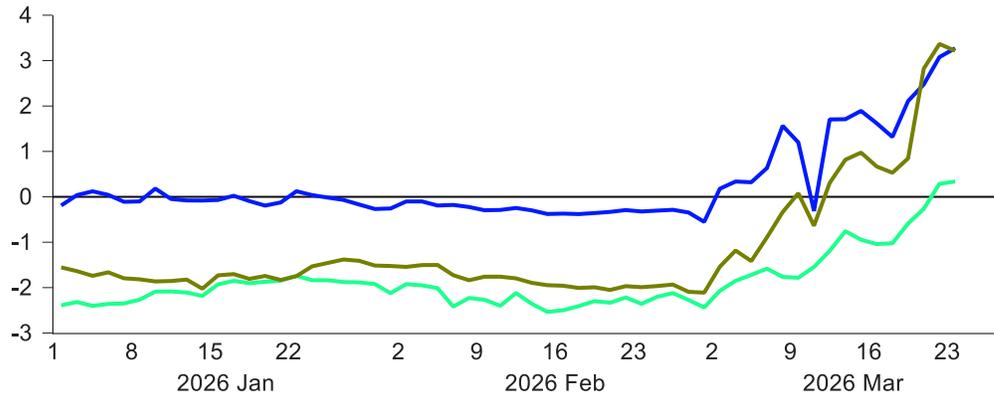
US: We Just Don't Know

This was a central bank “tour de force” kind of week, with considerable divergence in reactions to the Iran war from the various monetary policy makers around the world. We would characterize the Fed as slightly hawkish in its assessment of impact from the Iran war...but anything else would have been truly surprising. The median dot still indicates one rate cut this year, but seven FOMC participants see none (three see three or more). Notably, none currently sees reasons to hike. We see none, either. In fact, we side with the minority as we are reluctant to let go of our three-rate cut forecast for the year—even as the market has moved violently in the other direction, pricing a slight probability of a hike.

To entirely forgo additional rate cuts this year seems very premature. The rationale evidently is the inflationary effect of the Iran conflict. But a prolonged conflict would present not merely an inflationary shock but also a material growth shock. With the labor market already leaning towards softness and with the potential for AI-labor disruption likely to intensify over the course of the year, we still see soft labor demand as the bigger concern. Higher interest rates would do nothing to stem inflation triggered by an energy supply shock, but could further dent labor demand and push unemployment higher. There is no doubt that headline inflation will jump in March, but we have no way of knowing how soon and how fully that rise will be retraced. If the Iran conflict winds down with only moderate damage to energy production capacity within the next 5 weeks, there is plenty of time for normalization

in activity. We are, after all, only in March. The lessons of Liberation Day should be remembered, namely, that worst case scenarios need not become reality, and that there is perhaps more resilience in the global economic system than we might dare to believe.

Figure 1: Extreme Hawkish Turn in Dec 2026 Rate Expectations



— WIRP Est Number of Moves Priced in for the UK - Tenor-Based OIS Model
 — WIRP Est Number of Moves Priced in for the US - Futures Model
 — WIRP Est Number of Moves Priced in for Euro Zone - Tenor-Based OIS Model

Source: Macrobond, State Street Investment Management, Bloomberg

BoE: Open To Options

The BoE’s meeting on Thursday prompted considerable market volatility, resulting in notable adjustments to short-term interest rate expectations. However, we feel this response overexaggerated, as the BoE simply maintained flexibility in light of prevailing uncertainty. Our view is that an extended pause remains the most likely scenario.

Consistent with forecasts, the bank held its policy rate steady and communicated a more hawkish stance. The decision was unanimous, marking a shift away from its prior inclination toward easing. The BoE signaled that inflation would remain elevated in the near term. According to data from March 16, the Bank expected CPI inflation to reach a high of 3.5% in the third quarter. Yet, with energy prices rising further since then, total inflation could surpass last year’s peak of 3.8%.

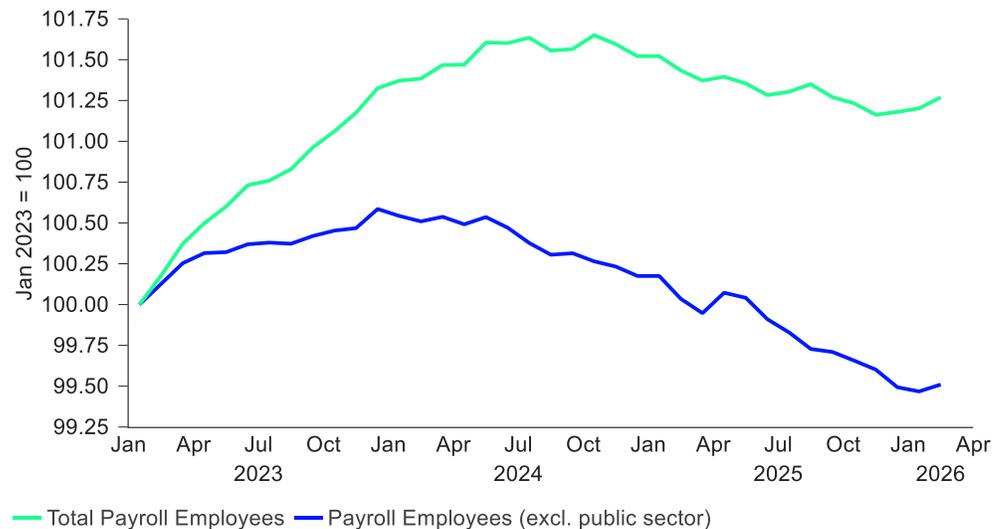
As inflationary pressures intensify, policymakers reaffirmed their commitment to closely monitor risks linked to structural shifts in wage and price determination. The MPC underscored the importance of remaining alert to increased domestic inflation risks from second-round effects, especially in the context of sustained high energy prices.

The unexpected unanimous 9-0 vote showed rare unity among MPC members, contrasting with the expected 7-2 split. Dhingra warned of possible rate hikes if oil and gas supply issues persist, despite economic weaknesses. Mann shared these concerns, while Bailey, Ramsden, and others confirmed their preparedness to act. Following the announcement, Governor Bailey advised caution in drawing

definitive conclusions, noting a range of possible outcomes. Elevated energy prices may contribute to sustained inflation in the UK. However, given significant uncertainty, the Bank of England is expected to maintain its current policy stance while continuing to monitor price developments.

Despite high energy prices and ongoing uncertainty, we think immediate rate hikes seem unlikely. Tight monetary policy and the energy price cap will shield consumers until July, with policymakers considering possible fiscal interventions. The Chancellor has indicated that targeted measures could curb inflation from energy costs. As risks exist with early policy changes, authorities will likely wait for clear signals like sustained wage growth before acting. Therefore, the chance for significant changes at the April meeting appear limited.

Figure 2: UK Labor Market Easing Continues



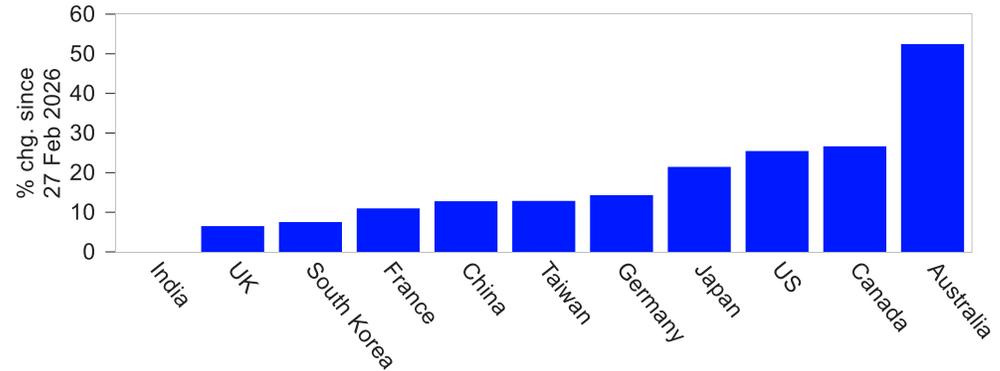
Source: Macrobond, State Street Investment Management, U.K. Office for National Statistics (ONS)

Japan: Keeping Options Open for Now

The Bank of Japan (BoJ) held its policy rate at 0.75%, in line with expectations. Board member Hajime Takata dissented, voting to raise the rate to 1.0%, but the decision to hold was supported by a majority. Governor Ueda’s press conference was carefully balanced, hawkish enough to keep the possibility of an April hike alive, yet sufficiently cautious to avoid commitment.

Governor Ueda referred to the Middle East conflict on two occasions, highlighting both downside and upside risks to inflation. He noted that the conflict could worsen Japan’s terms of trade, placing downward pressure on economic activity and potentially on underlying prices once temporary factors are excluded. At the same time, he cautioned that it could lift medium- to long-term inflation expectations among households and businesses, thereby pushing underlying inflation higher. However, it is important to recognize that retail pump prices in Japan have risen range bound compared to the peers (figure 3).

Figure 3: Change In Fuel Prices At Pump Since The Iran War Started*



Source: State Street Investment Management, Macrobond, Australian Institute of Petroleum, Energy Information Administration (EIA), U.K. Department for Business, Energy & Industrial Strategy, Kalibrate Canada, Inc., Indian Ministry of Petroleum & Natural Gas (MOPNG), China National Bureau of Statistics (NBS), European Commission (DG ENERGY), Japanese Ministry of Economy, Trade & Industry, Korea National Oil Corporation, Chinese Petroleum Corporation (CPC)
Updated as of 3/22/2020

*AU-Avg. national terminal gate; US-Avg. gasoline; UK-ULSP pump; CA-Volume wtd. avg. gasoline; IN-Gasoline in Mumbai; CN-Gasoline (97# or 95#); GE & FR-Gasoline Super 95; JP-Regular gasoline; SK-Ordinary gasoline; TW-92 Unleaded gasoline

For now, the BoJ has the right policy stance, but the Bank may have to intervene in the bond market and think about supporting the yen if the Middle East conflict drags on. More importantly, we think the BoJ would not hesitate to make a firmer dovish pivot in such a case as the success of policy normalization hinges on staying the course and not on rigid timeline. Next week, we see CPI easing to 1.4% y/y in February but all eyes will be on the release of the first round of the *shunto* results; we see it coming slightly below last year's 3.84%.

Australia: Standing Vigilant, Fearing Demand-Destruction

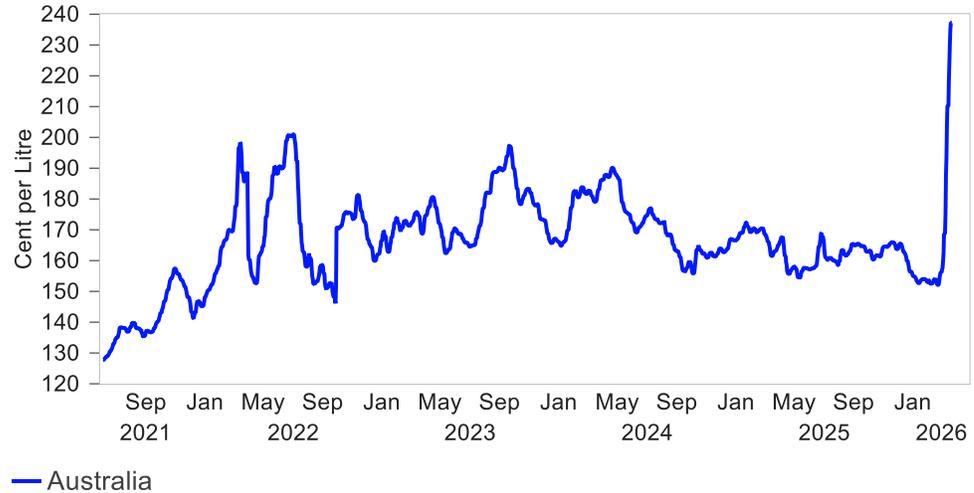
We warned that the Reserve Bank of Australia (RBA) could hike rates this month soon after the Q4 GDP release on March 4. Our concern was that the Bank would focus on stronger-than-expected consumption even as the war with Iran had just begun, at a time when markets were pricing less than a 20% probability of a hike. Market pricing shifted only after Deputy Governor Hauser's hawkish podcast, delivered just ahead of the Bank's mandatory blackout period, and consensus expectations moved rapidly thereafter.

The decision ultimately came as a narrow 5–4 vote. Importantly, the hike should not be read as dovish. Governor Bullock made it clear that the internal disagreement was over timing, not over the direction of monetary policy. More telling were three comments from the press conference that offer insight into where policy is headed. She stressed the need for aggregate demand, particularly consumer spending, to slow; noted that a stronger Australian dollar would help contain inflation; and warned that failure to rein in excess demand would allow businesses to embed higher costs into prices. While the Governor maintained that she was not providing forward guidance, these remarks underscore how attuned the Bank is to rising inflation risks stemming from the Middle East conflict. Even though we see a rising probability of the war becoming more prolonged at the margin, our base case remains that it ends relatively soon.

Australia is already feeling the impact through energy prices. Retail petrol prices have risen by more than 30% since the conflict began, among the sharpest increases globally. This raises the risk of demand destruction, particularly as some of Australia’s key refined fuel suppliers, including Malaysia and South Korea, have reportedly considered restricting exports to prioritize domestic needs. As a result, fuel prices in Australia have climbed well above those of its peers, as shown in Figure 4.

We are also optimistic that the economy has positive externalities as one of the largest natural gas exporters of the world, however such news have yet to emerge.

Figure 4: Australia's Petrol Prices Jump To Record High



Source: Macrobond, State Street Investment Management, Australian Institute of Petroleum

At the same time, the labor market is showing signs of strain. The unemployment rate rose two tenths to 4.3% in February, one tenth above our forecast and two tenths above consensus. Full-time employment fell by 30.5k, although a strong rise in part-time jobs meant total employment still increased by 48.9k. The rise in unemployment was accompanied by a 22 bp jump in the participation rate to 66.9%, highlighting ongoing volatility in labor market dynamics.

The most consequential development, however, comes from the Treasury’s scenario analysis. In the first scenario, global crude prices rise above \$100 before returning to pre-war levels of around \$70 by December. In that case, inflation would rise by 0.75 percentage points, while GDP growth would slow by 0.2 percentage points. In the more adverse scenario, crude reaches \$120 per barrel in the first half of the year and takes three years to return to pre-war levels. Inflation would then rise by 1.25 percentage points, with growth lower by 0.6 percentage points. This aligns with our concern that demand destruction could emerge relatively quickly in Australia given capacity constraints and low stockpiles. That said, if the conflict ends sooner, the outcome is likely to fall

somewhere between these two scenarios and a shallow hiking cycle from the RBA could help keep inflation contained.

Week in Review

A summary of macro data releases from the past week.

Country	Release (Date, format)	Consensus	Actual	Last	Comments
Monday, Mar 16					
US	Empire Manufacturing (Mar)	3.9	-0.2	7.1	Soft.
US	Industrial Production (Feb, m/m)	0.1%	0.2%	0.7%	Modest.
CA	Housing Starts (Feb, thous)	255	250.9	240.1	Weaker than expected.
CA	CPI (Feb, y/y)	1.9%	1.8%	2.3%	OK.
Tuesday, Mar 17					
US	Pending Home Sales (Feb, m/m)	-0.6%	1.8%	-1.0% (↓)	Positive surprise in brief rate drop.
GE	ZEW Survey Expectations (Mar)	39.2	-0.5	58.3	Collapse on energy price spike.
JN	Tertiary Industry Index (Jan, m/m)	0.9%	1.7%	-0.8% (↓)	Good.
AU	RBA Cash Rate Target	4.10%	4.10%	3.85%	A rate hike hat-trick is in play.
AU	Westpac Leading Index (Feb, m/m)	-n/a	-0.09%	0.01% (↑)	March data is more critical.
Wednesday, Mar 18					
US	PPI Final Demand (Feb, m/m)	0.3%	0.7%	0.5%	Stronger than expected.
US	Factory Orders (Jan)	0.1%	0.1%	-0.4% (↑)	Improving trend.
US	Durable Goods Orders (Jan, final)	0.0%	0.0%	0.0%	Improving trend.
US	FOMC Rate Decision (Upper Bound)	3.75%	3.75%	3.75%	Mildly hawkish.
CA	Bank of Canada Rate Decision	2.25%	2.25%	2.25%	No surprises.
JN	Core Machine Orders (Jan, m/m)	-9.6%	-5.5%	16.1% (↓)	Payback from strong December.
Thursday, Mar 19					
US	Initial Jobless Claims (Mar 14, thous)	215	205	213	Surprisingly low.
US	Continuing Claims (Mar 7, thous)	1,852	1,857	1,847	Moderate.
US	Philadelphia Fed Business Outlook (Mar)	8	18.1	16.3	Six-month high.
US	New Home Sales (Jan, thous)	722	587	712(↓)	Has been quite volatile lately.
UK	Average Weekly Earnings (Jan, 3m y/y)	3.9%	3.9%	4.2%	Weakening.
UK	Bank of England Bank Rate	3.75%	3.75%	3.75%	Hawkish tone.
JN	BOJ Target Rate	0.75%	0.75%	0.75%	Mildly hawkish hold.
JN	Industrial Production (Jan, m/m, final)	--	4.3%	2.2%	Good data.
AU	Unemployment Rate (Feb)	4.1%	4.3%	4.1%	More than our above-the-consensus forecast.
Friday, Mar 20					
CA	Retail Sales (Jan, m/m)	1.5%	1.1%	-0.4%	Weaker than expected.

Source: data, Bloomberg®; for commentary, SSGA Economics.

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