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Economist's Weekly Market View

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Central banks kick to touch amid uncertainty

Last week's Fed and Bank of England meetings left monetary policy unchanged, as expected, with both central banks playing for time over the summer months, amid heightened uncertainty.

For the Fed, the decision to leave rates on hold at 4.25-4.50% was unanimous, leaving it on hold since December 2024. More instructive was its latest set of economic projections, including the much-watched interest rate 'dot plot'. This showed the median projection of FOMC members was for a 50bps cut by year-end, identical to the March 2025 forecast. However, the dots also showed a growing minority of members expect no rate cuts in 2025, while the overall median projection for 2026 and 2027 shows a more gradual trajectory to a terminal rate of 3% in the long term.

While Chair Powell largely kicked to touch on tariff-related questions in his press conference, it is clear some members are now factoring higher inflation into their outlook and adjusting their rate expectations accordingly. Powell himself placed something of a deadline on his thinking, stating "we're going to learn a great deal more over the summer on tariffs". This brings the annual Jackson Hole gathering of central bankers in late-August into play as the next potential juncture where Powell might elaborate further on the impact of President Trump's tariffs on the Fed's policy outlook.

For his part, the President continued to criticize the "stupid" Powell, stating "it would be nice to be 2½ points lower". So far, the Fed Chair has asserted its independence, but his departure date is fast approaching in May 2026, with attention now turning to potential successors. While there are fears of a 'patsy pick' by President Trump, the next Chair will be just one of 12 voters on the FOMC, with the others insulated from political pressure by terms mostly running into the 2030s for the seven Board of Governors members, and the decentralized nature of the Federal Reserve system from which the remaining five voting Presidents are drawn.

For the Bank of England, the decision to hold rates at 4.25% remained a disputed decision, with three members of its MPC favoring a 25bps cut. Despite persistently weak GDP growth, the BoE is still grappling with domestic inflationary pressures, with inflation running at an annual rate of 3.5%. For now, most members retain a bias to "squeeze out" these lingering price pressure, as Governor Bailey described it.

Meanwhile, the escalation in the conflict in the Middle East had little dent on financial markets at the beginning of the trading week, including interest rate expectations; but the conflict adds a further layer of uncertainty for global central banks as they seek to navigate through the current policy fog.

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