Fed Watch: In No Hurry

Published June 18, 2025

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Key Takeaways

- Despite holding rates steady for a fourth consecutive meeting, the Fed has already implemented significant easing, with the Fed Funds Rate now 100 basis points below last year's peak.
- Heightened tariff-related uncertainty continues to cloud the Fed's outlook on inflation and employment, prompting a cautious, data-dependent stance through the summer.
- Recent data suggests the U.S. economy may sidestep a textbook recession, with resilient job growth and disinflation trends supporting the possibility of one to two rate cuts later this year.

For the fourth meeting in a row, the Federal Open Market Committee (FOMC) decided to keep rates unchanged, leaving the Fed Funds trading range at 4.25%–4.50%. While it may seem as if the policy maker has not done any easing in this cycle, remember that the level for overnight money is 100 bps below last year's peak reading. Once again, the decision to keep Fed Funds at its current level came as little surprise, as the Fed continues to be sitting back and waiting to see how the economic and inflation landscape unfolds given the uncertainties that have arisen from tariff-related developments. Needless to say, it is not just the Fed but also the markets that are in wait-and-see mode.

For those keeping track, we are now at the halfway point when it comes to the number of FOMC meetings in a calendar year. Interestingly, prior to the just-completed June convocation, various Fed officials had been stating that the voting members may not have enough data to make a future policy decision, aka a potential rate cut, until September.

Powell & Co. have consistently expressed their opinion that the uncertainties surrounding tariffs had placed a cloud of sorts over the macro outlook going forward. In other words, the policy maker sees heightened risks going forward for both aspects of its dual mandate: employment and inflation. The increased risks for both higher unemployment and higher inflation place the Fed in a challenging environment, and as we sit here in the present time, it does not appear as if this cloud will be removed any time in the near future, where a clear-cut rate decision would emerge during the summer months.

So, that leaves us with the question of how the underlying economic and inflation backdrops look post-Liberation Day. Indeed, the Fed, as well as the money and bond markets, now essentially has two months' worth of data to analyze since April 2. Broadly speaking, in my opinion, the macro backdrop still has not changed or altered the monetary policy outlook, for now. Overall, it looks like the U.S. economy will

avoid a “textbook” recession. After posting a modest negative reading of -0.2% for Q1 real GDP, projections for the current quarter are soundly in the plus column.

That brings us back to the Fed’s dual mandate. There’s no question that recent inflation data has revealed a “disinflationary” trend, where the early stages of tariffs that are in effect have not been passed through to either the wholesale or retail level. However, as Chairman Greenspan once said, CPI is like looking in the rearview mirror, so future inflation reports will be integral for Fed decision-making. As far as the employment situation, the May jobs report showed a continued resilient labor market setting. However, signs could be emerging that some slowing is entering the equation, a development to watch for sure.

The Bottom Line

Fed guidance continues to emphasize that the macro setting allows the voting members to take a deliberate approach to monetary policy. In other words, the song remains the same, i.e., the Fed is data-dependent and can let the data “come to them.” Against this backdrop, a reasonable-case scenario still involves potentially one to two rate cuts this year