EDITORIAL

WHAT'S ON CENTRAL BANKERS MINDS HEADING INTO THE SUMMER?

Each year, summer is bookended by two landmark central banking conferences where central bankers, academics and a few members of the private financial sector congregate to discuss new research of interest for monetary policy and compare notes on the outlook: in late June, the ECB Forum held in the windy coastal town of Sintra, Portugal; and in late August in the scenic Rocky Mountains valley of Jackson Hole, Wyoming. This year, the Sintra winds were blustery and relentless, but the discussions as calm, focused and insightful as ever, an apt metaphor for central bankers' condition these days. Some key takeaways.

NO HINT OF TRIUMPHALISM DESPITE SOFT LANDINGS BASICALLY ACHIEVED

The leading central banks are reaching or closing in on their inflation targets[1] with labour markets in robust health. All saw themselves "*in a good position*", but none was ready to declare mission accomplished. They are concerned about hazards lurking down the runway.

For the US Federal Reserve (Fed), the key one is the risk of a flare-up in domestic prices because of the tariffs imposed by the White House on all US trade partners. In Sintra, Fed Chair Powell acknowledged the FOMC would likely have cut interest rates already were it not for that risk. So far, there has hardly been any sign of passthrough from tariffs to prices, but firms had non-tariffed inventories to run through and could afford to wait for clarity on the final level of tariffs. This is likely to change over the next few months. How large will the passthrough be and to what extent will it lead to generalized increases in prices and wages are the key questions, with the answer depending in large part on GDP growth. Hence a very non-committal Powell on the next steps, seeing "*multiple paths from here*". We foresee no cut before the autumn or even later.

Like the Fed, the Bank of England (BoE) has yet to fully bring inflation back to 2% and hence is keeping monetary policy restrictive, having eased very gradually thus far; but, unlike the Fed, it is facing the prospect of a rapidly deteriorating employment outlook that made Governor Bailey confident to state that the direction of travel for rates is clearly down. We expect a cut in August.

For the European Central Bank (ECB) and the Bank of Japan (BoJ), on the other hand, the predominant concern is persistently too low inflation. This may seem paradoxical: headline inflation has been running at basically 2% for 2 months in the Eurozone, and well above this target for 3 years running in Japan. But both are concerned about the outcome of tariff negotiations with the US and its impact on domestic and global growth. Japan, in addition, is facing near term political uncertainty, while the ECB has to contend with a fast appreciation of the euro against the dollar (by 14% year-to-date). All these create disinflationary risks, as does a resumption of the downward trend for energy prices.

As such, the ECB saw it as appropriate to hold in a neutral stance for now, and the BOJ in an accommodative one. We expect another 25 bps cut from the ECB in September, while it may take longer for the BoJ to feel confident enough that underlying inflation will settle at 2% to take another step toward normalization (i.e., a rate hike).

STRATEGY REVIEWS TO COPE WITH A MORE UNCERTAIN WORLD

The BoE, ECB, and Fed all embarked last year on a review of their strategy and operational framework. The ECB's concluded first[2], on the eve of the Sintra Forum. Its diagnostic is likely to be echoed by its peers: in a world with greater geopolitical instability, global warming and trade fragmentation, inflation is likely to be more volatile; it will also be more uncertain to forecast owing to the complex and competing effects of artificial intelligence, ageing populations and the climate transition. The key innovation coming out of the ECB's review is its intent to publish scenarios alongside its monetary policy decisions to help explain its policy reaction function. The BoE has been experimenting with these for some time and recently formalized their use too. The Fed and BoJ leaders expressed caution in Sintra when asked about emulating this practice. Beyond this, the ECB confirmed the symmetry of its 2% target (i.e., equal concern for deviations from above and below), and re-underwrote the entire toolkit it has had in the books. It also committed to being "agile", including, if need be, by creating new policy instruments. The closest thing to a "mea culpa" in the review came in the form a reference to the need for "proportionality" in the use and design of non-conventional policies. This, along with reference to using "*appropriately forceful* ***or*** *persistent policy responses to large, sustained deviations*" (emphasis added), suggests a mildly hawkish bias in policy intent, at least compared to past practice.

HOW TO BOOST EUROPE'S PRODUCTIVITY?

Consistent with the perception that inflation outcomes in future will depend importantly on the supply side of the economy, much attention was paid in the program of the ECB Forum[3] to EU-US comparisons and the large productivity gap between them. While differences in labour market dynamism might provide part of the explanation, the lack of financial integration in Europe was seen as a key obstacle to

1 See our June 2025 Inflation tracker for details.
2 See Our 2025 monetary policy strategy assessment
3 See ECB Forum on Central Banking 2025

unleashing Europe's growth potential. While much emphasis has been placed recently on the need for greater integration of capital markets in Europe, the presentations showed that in fact banking markets are even far less integrated, leading to far more heterogeneity of credit pricing across countries (and hence of monetary policy transmission). A discussion of non-bank financial institutions (NBFIs) also made clear there remains significant ambivalence toward these institutions despite their being the core of any capital markets union.

CATCHING UP WITH STABLECOINS

"*If we are to have stablecoins, they ought to be regulated*" said Fed chair Powell, summarizing the general sentiment. Stablecoins —digital assets backed 1:1 by high quality liquid assets like T-bills- were not on the formal agenda of the ECB Forum; however, they featured in many panels and side conversations, having been a key focus of the Annual Meeting of the Bank for International Settlements[4] (BIS) just days before, and becoming a hot topic in Korea. They have been growing very rapidly and are expected to gain further momentum following passage by the US Senate of the Guiding and Establishing National Innovation for US Stablecoins Act (aka, GENIUS Act), which should soon become law. For the US government, the attraction of creating a new source of captive demand for US T-bills is obvious. For all others, it creates pressure to either encourage a local currency equivalent to develop or allow widespread use of US-issued stablecoins in US dollar. The fears relate to implications for financial stability but also, should their use gain ground outside the US, to national authorities' ability to enforce capital controls and even run effective monetary policy. There is also the prospect of the US dollar's global dominance becoming even further entrenched. At a time when Europe is struggling to reach escape velocity on its Savings and Investment Union journey, this is a new challenge that requires urgent attention. Who knows, it might even turn into a helpful catalyst.

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4 The next-generation monetary and financial system