Paris, 19 June 2025

EcoFlash

FOMC: Waiting and Divided

While the Federal Reserve (Fed) estimates that uncertainty has eased, its conviction that a tariff-related rise in inflation is looming has hardened. The Committee (FOMC) nevertheless appears to be greatly divided on the balance of risks. We maintain our forecast that there will be no rate cuts in 2025 in light of renewed inflationary pressures combined with insufficiently slowing growth.

Inflation: The Past Matters Less Than the Future

The latest positive inflation readings (CPI at +2.4%, *Core CPI* at +2.8% y/y) were not enough to resume the easing cycle. **The anticipated rise in inflation linked to the implementation of tariffs underpins the stability of the policy rate target.** We note early signs of this expected rebound, particularly in ISM surveys, with prices paid at their highest since 2022 (Chart 1), whose inflationary impact could add to the rise in the price of imported finished goods alone. **The anticipated rise in inflation linked to the implementation of tariffs underpins the stability of the policy rate.** We note early signs of this expected rebound, particularly in ISM surveys, with prices paid at their highest since 2022 (Chart 1), whose inflationary impact could add to the rise in the price of imported finished goods alone. In addition, plummeting imports and extended delivery times point to potential supply difficulties. **The FOMC seems to have gained conviction that inflation will pick up.** This was reflected in the revisions to the Summary of Economic Projections (SEP) for the PCE and Core PCE (+0.3 pp for 2025 compared with March).

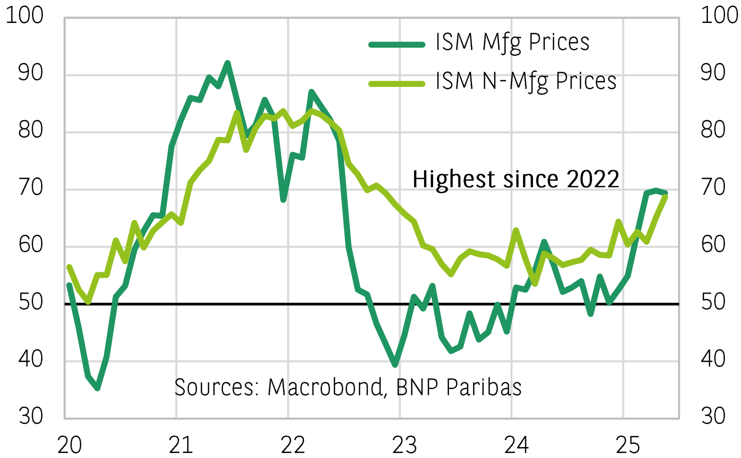

Chart 1

A Divided FOMC

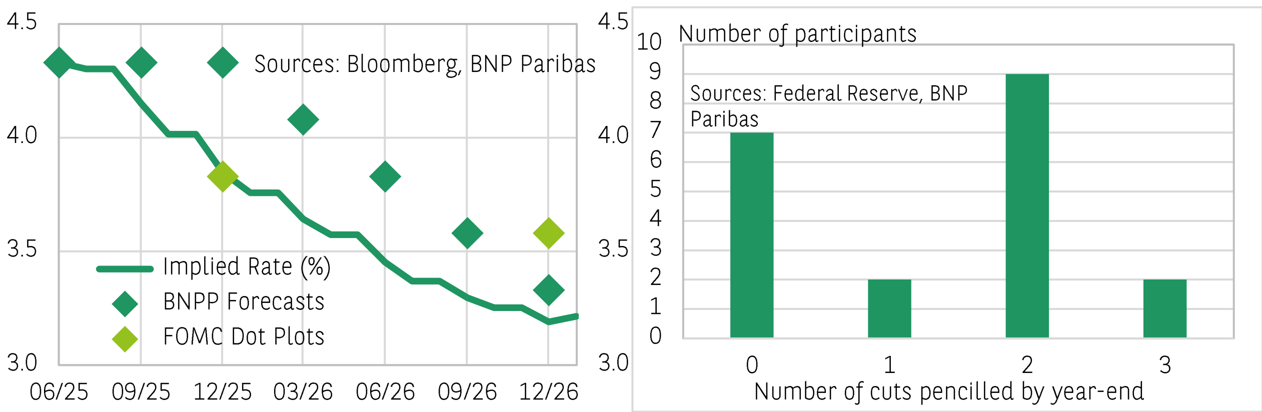

Chart 2 and Chart 3

Q2 SEP retained the median forecast of two rate cuts in 2025, which is in line with the market expectations (Chart 2). However**, this figure conceals strong and surprising dissent within the Committee** (Chart 3), with nine members penciling two cuts, compared with seven anticipating the 'no cut' scenario. **J. Powell called for caution regarding dot plots**, citing the uncertainty surrounding them and the data-dependent approach to future rate decisions, thereby confirming the division.

The projections also reported downward revisions to GDP growth compared with the March SEP, to +1.4% y/y (-0.3pp) in Q4 2025 (+1.2% for BNP Paribas). This **dual risk** – that of an economic slowdown, calling for monetary easing, and that of accelerating inflation, suggesting tightening – explains both the FOMC's **unanimous wait-and-see stance** and the **division among its members on the way forward**. Data released over the summer should tip the balance, with J. Powell likely to benefit from the influence of his position. **We are maintaining our scenario of no rate cut in 2025, with inflation rebounding and an economic slowdown insufficient to prompt easing**.

A Matter of Anchoring

A key challenge for the Fed is to **ensure that the expected rise in prices does not turn into sustained inflation**, which would also threaten the full employment component of the dual mandate. As such, **maximum attention is being paid to keeping inflation expectations anchored**. Announcements on tariffs caused household expectations to soar, reaching their highest levels in over 30 or even 40 years. However, while the labour market remains robust, or 'solid' according to the Fed, it has cooled substantially since the post-pandemic reopening (Chart 5), limiting the potential second-round effects via the wage channel.

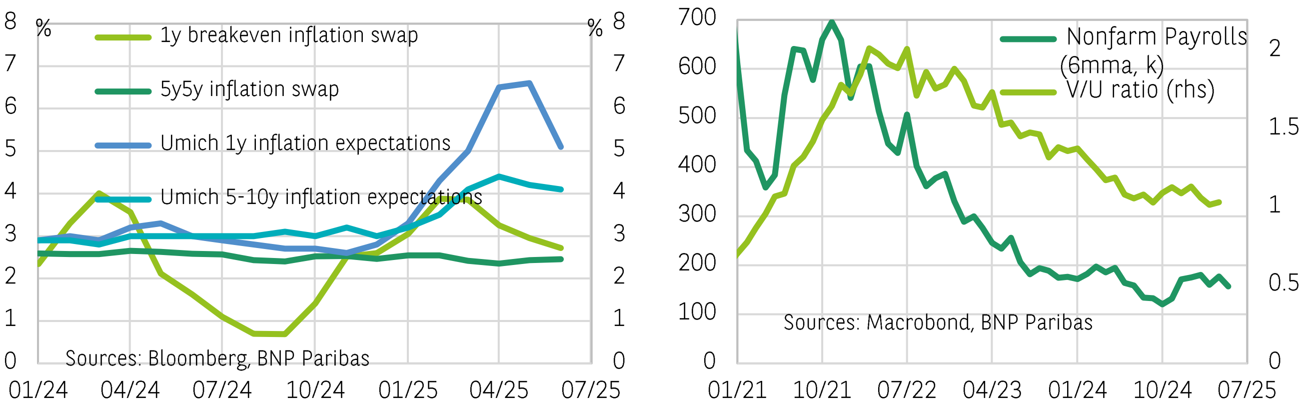

Chart 4 and Chart 5

Developments in market inflation expectations have been more reassuring for the Fed. The side-by-side analysis of the 1-year breakeven inflation swap and the 5y5y inflation swap is consistent with the idea of a temporary rise in inflation (Chart 2). The **robustness of medium-term anchoring** reflects market confidence in the FOMC's actions. **The risks associated with a de-anchoring of expectations are significant**: persistent inflation, a loss of monetary policy effectiveness or higher bond yields. These risks are sufficiently significant to prevent the Fed from deviating from its current stance in the absence of a significant downturn in employment and activity.

Anis Bensaidani
Economist, United Stated and Japan
anis.bensaidani@bnpparibas.com

Article completed on June 19