Fed Stays on Hold While Uncertainty Persists

With ongoing tariff uncertainty and U.S. employment still strong, the Fed kept its key interest rate at 4.25–4.50%.

Authors	Date	Topic
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Key takeaways

- In our view, the next likely window for the Fed to lower rates will be September.
- While inflation has been trending down, a tight labor market and the potential for increased tariffs could bring short-term higher inflation.
- Although uncertainty has prevailed in recent months, we think this environment offers potential opportunities for investors in areas of the equity and fixed income markets.

The Fed today—and our outlook

Today, the Federal Open Market Committee announced another pause in its key interest rate, the federal funds rate, keeping it at 4.25–4.50%. With the ongoing uncertainty around tariffs and a still-robust U.S. labor market, the Federal Reserve (Fed) is taking a widely expected **"wait and see" approach** on rates. From our perspective, the next likely window for the Fed to lower rates will be September. We expect the Fed to potentially cut interest rates twice this year should inflation continue to drop toward its 2.0% target.

Inflation

U.S. inflation continued trending downward over the past month as the Fed's preferred consumption-based core inflation measure, the Personal Consumption Expenditures Index, dropped to 2.5% year over year. Consumer and corporate price expectations have both remained elevated, though, as tariff uncertainty persists. Underlying price trends for core inflation—including stickier, slower-moving items like rents—have been positive although a tight labor market and the potential for increased tariffs could lead to short-term higher inflation.

Growth

U.S. labor market data remained fairly robust in May, and real wages continue to support the U.S. consumer. However, elevated interest rates and a slowing U.S. economy have led to some spending fatigue. Despite some recovery in consumer sentiment, personal spending and retail sales trended lower in May. On the corporate side, the Institute for Supply Management® Services Purchasing Managers' Index indicated weakening below the level of 50, which reflects a reduction in activity, and new orders continued to fall. The services sector had generally been the bright spot of the U.S. economy while the manufacturing sector had struggled. With ongoing tariff uncertainty and declining trade flows between the U.S. and China, further slowing in the U.S. economy can't be ruled out.

Rates

The interest rate market currently expects the Fed will **cut rates to around 3.8%** by the end of 2025. A lot will depend on how the inflation-versus-growth trade-off develops. In our view, growth will likely continue weakening and the Fed would ideally want to cut rates to support growth—over the shorter term, though, higher prices could make that tricky.

Market outlook

We expect **equity market performance to remain volatile** and continue to favor cheaper parts of the U.S. equity market, international equities, and emerging market equities given better valuations, more fiscal and monetary stimulus likely to come, and higher valuations of a number of U.S. large-cap equities. Our outlook for **higher-quality bonds remains favorable** given still-attractive overall yields.

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