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Fed holds the policy rate steady amid vast uncertainty

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Unconvinced recent disinflation will persist amid looming tariff effects, policymakers support holding a “well positioned” stance

The FOMC left the federal funds rate unchanged at 4.25-4.50%, reaffirming its cautious stance amid still-elevated, though recently “diminished,” uncertainty. The policy statement introduced two minor changes. First, it updated its labor market assessment, stating that the unemployment rate “remains low,” replacing previous language that it had “stabilized at a low level.” Second, it dropped the earlier assertion that “the risks of higher unemployment and higher inflation [had] risen,” instead stating that uncertainty “has diminished but remains elevated.” Both revisions might appear dovish at first glance, though Powell later clarified they were not intended to signal any fundamental shift in the Committee’s risk assessment. Whether a significant part of the discussion focused on emerging downside risks to activity and employment will become clearer when the minutes are released in three weeks. The updated Summary of Economic Projections (SEP) for 2025 shows higher inflation—core PCE now at 3.1% (up from 2.8%)—weaker growth (1.4%, down from 1.7%), and a slightly higher unemployment rate (4.5%, up from 4.4%) (Table 1). While directionally consistent with our expectations (see), these adjustments were not sufficient to alter the median fed funds rate projection for end-2025, which remains at 3.9%, implying two 25bp cuts. For 2026 and 2027, participants now expect the policy rate to be 3.6% and 3.4%, respectively—above the 3.4% and 3.1% projected in March. In contrast to the statement’s tweaks, this suggests a more hawkish stance than recently signaled by FOMC members. However, Powell explained that the changes instead reflect a catching-up process, noting that the March SEP was compiled before the larger-than-expected “Liberation Day” tariffs were incorporated into baseline projections.

Powell reaffirmed the Fed’s strong preference to remain on hold amid lingering uncertainty over the inflationary impact of tariffs. His introductory comments highlighted the diversity of views within the Committee regarding the persistence of these effects, ranging from “short-lived, reflecting a one-time shift in the price level,” to “more persistent.” However, he emphasized that all members support the current policy stance as “well positioned,” allowing them “to wait to learn [...] a great deal more over the summer on tariffs.” Powell clarified that the apparent shift in the statement—from “increased risks” to “diminished uncertainty”—should not be interpreted as a dovish pivot. Rather, it reflects a decline in peak uncertainty since “Liberation Day,” not a reduction in the Fed’s concern over the complexity of the outlook. Consistent with this, he noted that while there are signs of labor market softening, the FOMC sees only “a very, very slow continued cooling but nothing that's troubling at this time,”

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suggesting no immediate concern about the most recent employment trends (e.g., the downward revisions to non-farm payroll figures for March and April and/or the recent increase in continuing claims for unemployment insurance). Rejecting the idea of easing based on recent soft inflation prints, Powell repeatedly stressed that monetary policy must remain forward-looking. He argued that it is more likely than not that inflation will rise in the coming months because “ultimately the cost of the tariffs has to be paid” by someone. At the same time, he made clear that no participant holds their rate path with high conviction on the magnitude and duration of such inflationary pressures, and that the current uncertainty justifies the Fed’s cautious stance. Altogether, Powell’s tone reinforced the Fed’s long-held strategy of remaining on pause while awaiting further clarity on the inflation path.

Today’s decision and SEP revisions are consistent with our view of no rate changes until December, when we anticipate a single 25bp cut. While the new projections for higher core inflation and weaker growth in 2025 were not enough to shift the median dot (which remains at 3.9%), they coincided with a notable realignment within the Committee. Instead of growing dispersion, the dot plot now reveals two almost evenly sized camps—those expecting two cuts and those expecting none—likely reflecting a divide between participants confident in continued economic resilience and those anticipating a material slowdown this year (Figure 1). But Powell’s message was clear: uncertainty remains high, and although recent inflation prints have been benign, this does not justify preemptive easing. His repeated emphasis on a forward-looking policy stance, coupled with the still-solid overall position of the economy, supports our view that the Fed will take more time before initiating rate cuts. The risk remains that, as the labor market continues to gradually cool and tariffs weigh more heavily on real activity, the Fed could place increasing emphasis on growth and employment dynamics, even as inflation edges higher in the coming months. For now, we remain confident that December is the most likely timing for the start of the easing cycle.

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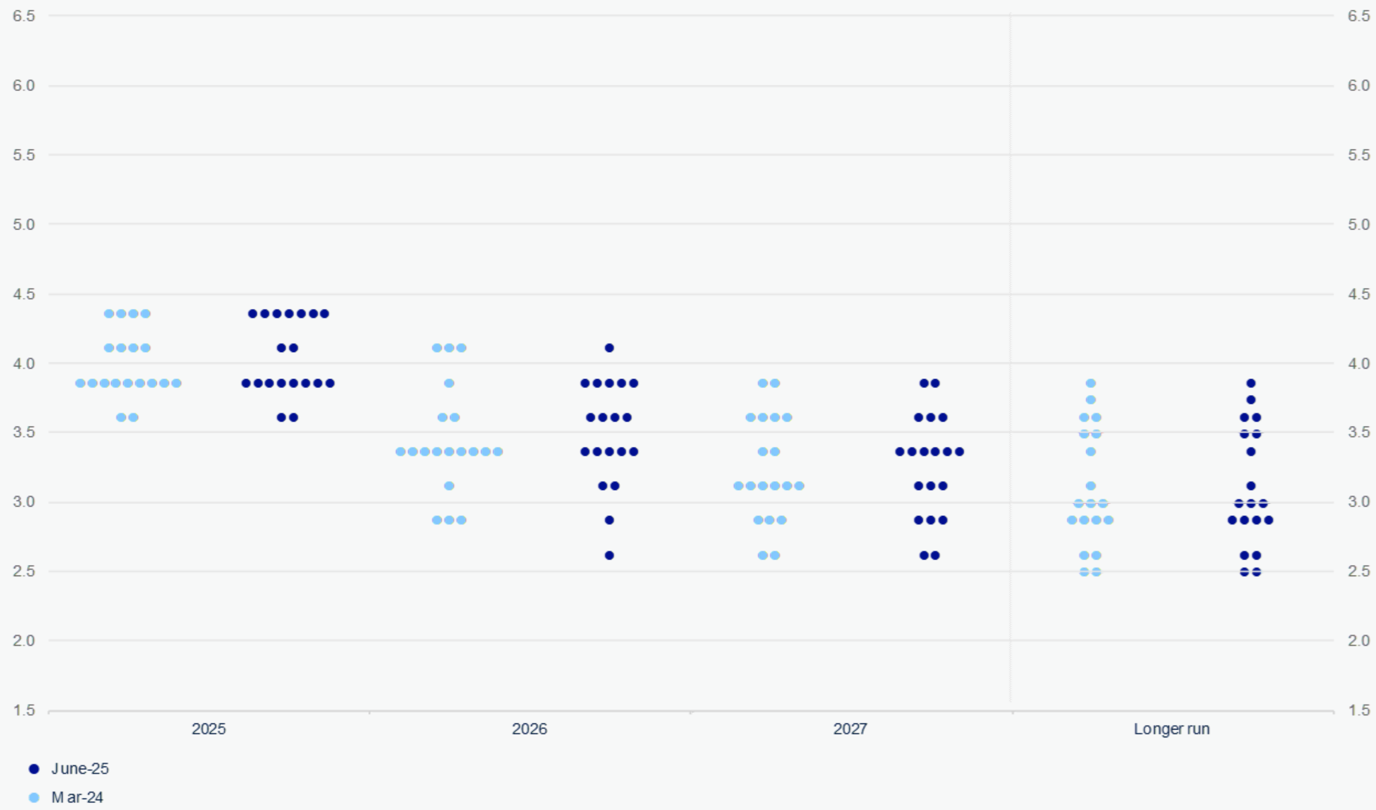
TABLE 1. FOMC PARTICIPANTS' SUMMARY OF ECONOMIC PROJECTIONS (JUNE 2025, %)

Variable	Median				Central tendency				Range			
	2025	2026	2027	LR	2025	2026	2027	LR	2025	2026	2027	LR
Change in real GDP	1.4	1.6	1.8	1.8	1.2-1.5	1.5-1.8	1.7-2.0	1.7-2.0	1.1-2.1	0.6-2.5	0.6-2.5	1.5-2.5
Mar-25	1.7	1.8	1.8	1.8	1.5-1.9	1.6-1.9	1.6-2.0	1.7-2.0	1.0-2.4	0.6-2.5	0.6-2.5	1.5-2.5
Unemployment rate	4.5	4.5	4.4	4.2	4.4-4.5	4.3-4.6	4.2-4.6	4.0-4.3	4.3-4.6	4.3-4.7	4.0-4.7	3.5-4.5
Mar-25	4.4	4.3	4.3	4.2	4.3-4.4	4.2-4.5	4.1-4.4	3.9-4.3	4.1-4.6	4.1-4.7	3.9-4.7	3.5-4.5
PCE inflation	3.0	2.4	2.1	2.0	2.8-3.2	2.3-2.6	2.0-2.2	2.0	2.5-3.3	2.1-3.1	2.0-2.8	2.0
Mar-25	2.7	2.2	2.0	2.0	2.6-2.9	2.1-2.3	2.0-2.1	2.0	2.5-3.4	2.0-3.1	1.9-2.8	2.0
Core PCE inflation	3.1	2.4	2.1		2.9-3.4	2.3-2.7	2.0-2.2		2.5-3.5	2.1-3.2	2.0-2.9	
Mar-25	2.8	2.2	2.0		2.7-3.0	2.1-2.4	2.0-2.1		2.5-3.5	2.1-3.2	2.0-2.9	
Federal funds rate	3.9	3.6	3.4	3.0	3.9-4.4	3.1-3.9	2.9-3.6	2.6-3.6	3.6-4.4	2.6-4.1	2.6-3.9	2.5-3.9
Mar-25	3.9	3.4	3.1	3.0	3.9-4.4	3.1-3.9	2.9-3.6	2.6-3.6	3.6-4.4	2.9-4.1	2.6-3.9	2.5-3.9

FIGURE 1. FOMC PARTICIPANTS' PROJECTED APPROPRIATE FEDERAL FUNDS RATE (%)



Source: BBVA Research / Fed

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