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Fed cuts rates by 25 bps, signals more to come

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The question now is whether today's cut kicks off a string of rate cuts or if the path toward neutral will unfold more gradually

The FOMC delivered a widely expected 25bp rate cut to 4.00-4.25%, with only one dissent from newly appointed Governor Miran, who unsurprisingly favored a 50bp cut. The statement said the move was made "in light of the shift in the balance of risks." While the Fed noted for the first time this year that "inflation has moved up," it also acknowledged that "downside risks to employment have increased." The Committee removed its prior description of "solid" labor market conditions and emphasized that "job gains have slowed" and the "unemployment rate has edged up." Notably, the statement dropped the reference to the "extent and timing" of further moves, now simply indicating that the Committee will consider "additional adjustments" to the target range. This subtle change suggests that more cuts are coming.

The Summary of Economic Projections (SEP) showed growth forecasts edged up for this year and next, while those for inflation and unemployment were largely unchanged. Real GDP growth was revised up by 0.2 pp in both 2025 and 2026, to 1.6% and 1.8%, respectively. The median unemployment rate projection remained at 4.5% for 2025, and was revised down slightly (by 0.1 pp) to 4.4% and 4.3% for 2026 and 2027 (Table 1), suggesting that most participants continue to expect immigration-related labor supply constraints to prevent a more troubling rise in joblessness from subdued labor demand. Core PCE inflation was left unchanged at 3.1% for 2025, but revised up by 0.2 pp to 2.6% for 2026, indicating that most participants still see tariff effects feeding into prices, albeit more slowly than previously expected.

The dot plot continued to show a split within the FOMC, with a majority now indicating that two more cuts this year in October and December are likely. The median participant now anticipates three 25bp cuts this year (i.e., two additional), compared to just two in total projected in June. Out of 19 participants, nine penciled in two additional rate cuts, two projected one more cut, six anticipated no further cuts, and two stood out as outliers—one preferring not to cut even today, and another favoring three consecutive 50 bp reductions, presumably Miran. The dot plot still projects only one 25bp cut in 2026 and another in 2027, but now to 3.50% and 3.25%, respectively (Figure 1). This implies that the dot plot continues to signal less policy easing than both market expectations and our baseline scenario, which projects the rate at 3.00% by end-2026.

Powell's press conference reinforced the statement's dovish shift, offering no major surprises, but carefully leaving the door open to a pause next month. He described the labor market as showing a "curious balance," driven "much more [by] the change in immigration," but also noted that "demand [is] coming down a little more sharply because we now see the unemployment rate edging up." He said there was no widespread support for a 50bp cut, which would be appropriate only when "policy is out of place and [the Fed] needs to move quickly to a new place." When asked if we should view today's cut as the FOMC taking some insurance against the possibility of a downturn, he described today's move as "a risk-management cut," with rising downside risks to the employment mandate making it appropriate to resume "moving in the direction of neutral." On inflation, he noted that the FOMC continues to "expect [tariff effects] to continue to build over the course of the rest of the year and into next year," but also said that "the risks of higher and more persistent inflation have probably become a little less" intense.

This week's cut is unlikely to be the last, as the Fed begins stepping away from a restrictive stance. While Powell reiterated a "meeting-by-meeting" approach, leaving the door open to either a pause or another cut in October, he also emphasized that policy focus has shifted towards a more balanced one, noting that the risks to the two goals "have moved meaningfully towards equality and that means [the Fed] should move in the direction to neutral" —a clear signal of further cuts ahead. A significant short-term upside inflation surprise, which cannot be ruled out, could warrant pausing rate cuts next month, but this seems unlikely as a single CPI print before the next meeting in late October will not be enough to conclude tariff-related price pressures have materially intensified. A sudden rebound in the labor market could also justify such a decision, but we think this is even more unlikely. Risks could even be slightly tilted toward a more significant deterioration in the labor market. While that does not appear to be the Fed's base case, Powell suggested that a sharper response—with stronger forward guidance toward further easing—could be triggered if we "start to see layoffs," as that "could very quickly flow into higher unemployment." Taken together, these factors raise the probability of a second cut in a row in October and tilt our baseline scenario toward two additional cuts this year.

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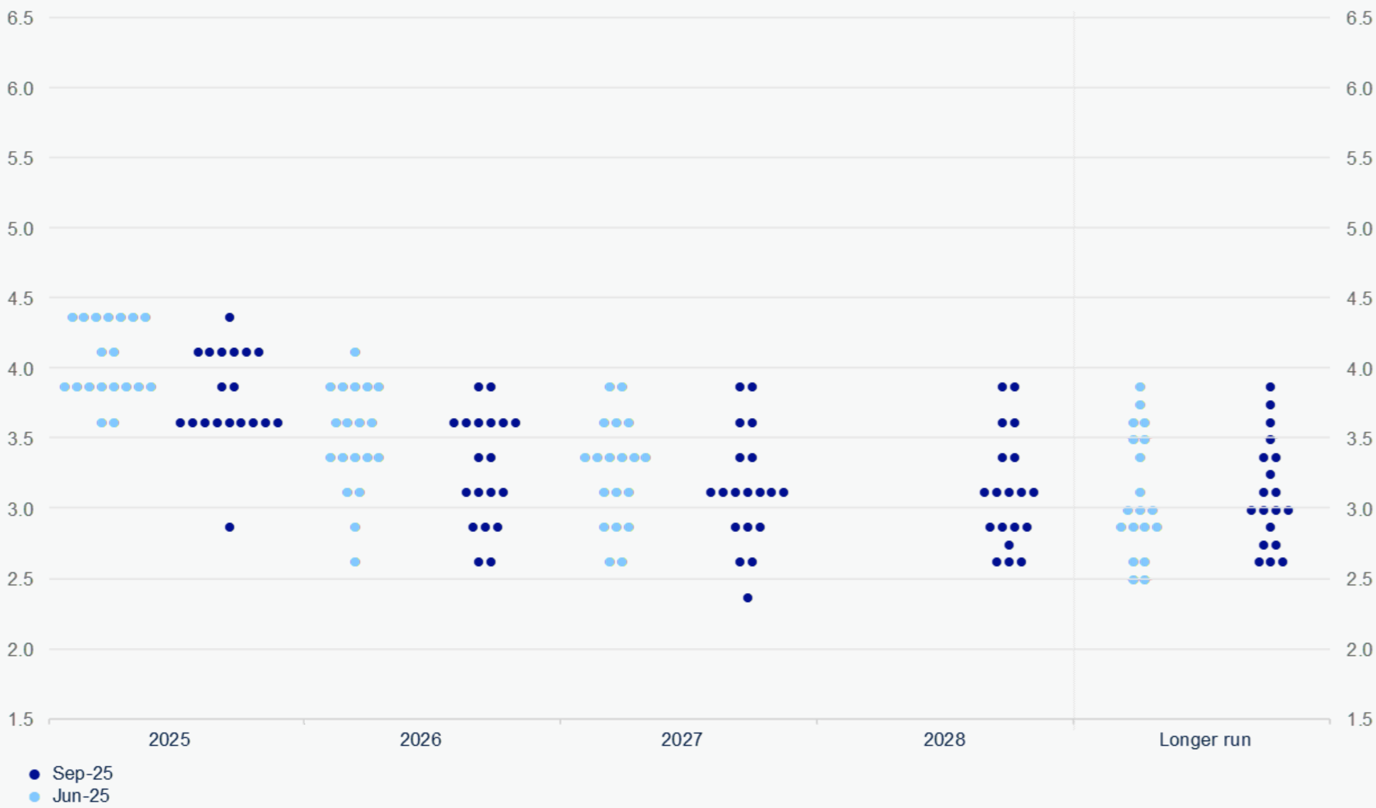
Growth, unemployment and inflation forecasts were little changed, but the dot plot points to 50bp worth of additional rate cuts this year

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

Variable	Median					Central tendency					Range				
	2025	2026	2027	2028	LR	2025	2026	2027	2028	LR	2025	2026	2027	2028	LR
Change in real GDP	1.6	1.8	1.9	1.8	1.8	1.4-1.7	1.7-2.1	1.8-2.0	1.7-2.0	1.7-2.0	1.3-2.0	1.5-2.6	1.7-2.7	1.6-2.6	1.7-2.5
Jun-25	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
Unemployment rate	4.5	4.4	4.3	4.2	4.2	4.4-4.5	4.4-4.5	4.2-4.4	4.0-4.3	4.0-4.3	4.2-4.6	4.0-4.6	4.0-4.5	4.0-4.5	3.8-4.5
Jun-25	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
PCE inflation	3.0	2.6	2.1	2.0	2.0	2.9-3.0	2.4-2.7	2.0-2.2	2.0	2.0	2.5-3.2	2.2-2.8	2.0-2.4	2.0-2.0	2.0
Jun-25	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
Core PCE inflation	3.1	2.6	2.1	2.0		3.0-3.2	2.5-2.7	2.0-2.2	2.0		2.7-3.4	2.2-2.9	2.0-2.4	2.0-2.2	
Jun-25	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		
Federal funds rate	3.6	3.4	3.1	3.1	3.0	3.6-4.1	2.9-3.6	2.9-3.6	2.8-3.6	2.8-3.5	2.9-4.4	2.6-3.9	2.4-3.9	2.6-3.9	2.6-3.9
Jun-25	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

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



Source: BBVA Research / Fed

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