



Macro - ECB and Fed meeting – July 2025

Despite very different economic contexts on either side of the Atlantic, the European Central Bank (ECB) and the US Federal Reserve (Fed) appear to be moving at the same pace for the time being.

Two different economies, one common outlook (for now)

Both central banks are expected to keep rates unchanged in July, and market expectations point to an almost identical probability of a cut in September. The message is clear: monetary authorities are waiting for greater visibility. This cautious stance is explained by two sources of uncertainty: global trade dynamics and fiscal support measures. These two factors are key determinants of inflation, growth, and exchange rate trajectories.

ECB: no urgency, but vigilance

Over the past 12 months, the ECB has cut its key rates by 200 basis points, bringing them back into a range that many consider neutral, between 1.75% and 2.25%. The monetary framework now appears to be in balance in the eurozone: neither too accommodative nor too restrictive.

However, this stability could be short-lived. Two major uncertainties are keeping the ECB on alert.

First, the potential imposition of tariffs between the United States and the European Union, the details of which are to be revealed on August 1, calls for caution. Second, while the fiscal stimulus measures expected in Germany (with formal approval in September) are cause for some optimism, the willingness to act may be hampered by the ability to implement them. These two uncertainties raise questions about how long inflation will remain below the 2% target.

Given the recent inconclusive data on growth and inflation, and in the absence of immediate negative catalysts, a preventive rate cut in July seems unlikely. The status quo appears to be the order of the day.

For September, the markets estimate a 50% probability of a cut. However, weak growth, the limited impact of a stronger euro on inflation, slower wage growth and the risk of inflation remaining below target due to an increase in cheap Chinese imports diverted from the US to Europe could cause the ECB to shift its stance. With inflation close to target and leading indicators pointing to economic normalization, we believe that the probability of a rate cut in September is higher than the consensus expectation.

The ECB could in the near future therefore bring its key rate back to 1.5%, especially if the tariff risk materializes or if inflation remains persistently below target.



Fed: between economic strength and political pressure

From a macroeconomic perspective, the US economy remains robust. Employment is strong, particularly due to labor supply constraints resulting from new immigration policies. Consumption remains buoyant. And fiscal policy remains expansionary, providing further stimulus to an economy that has been growing above its potential for more than four years.

Politically, however, the situation is more tense. The US president has openly criticized Jerome Powell, casting doubt on the Fed's independence.

Between a rock and a hard place

The Fed does not expect inflation to return to 2% before 2027, which is six years after it last returned to its target. The latest price data is not reassuring. There are already signs that import costs are being passed on to consumer prices, particularly for manufactured goods. The FIFO (first-in-first-out) model, which is predominant in US distribution, suggests that the impact of higher tariffs is only just beginning to be felt.

Jerome Powell is under growing political pressure, but any speculation about his immediate replacement seems unlikely. President Trump has little interest in changing the Fed's leadership six months before the end of his term. Such a move would undermine the central bank's credibility, damaging the stability of the dollar, inflation expectations and long-term interest rates. However, it is precisely the Fed's credibility that has kept long-term inflation expectations anchored since the price surge in 2022. Any drift toward fiscal dominance or premature monetary easing would jeopardize this hard-won stability.

Our central scenario is therefore that the Fed will keep its key rates unchanged at its September meeting, provided that the labor market holds up relatively well in the meantime.

Impact on portfolios

Although the short-term expectations for the two central banks appear to be aligned, market expectations reflect very different outlooks:

ECB: the markets see a 30% probability of key rates at 2% or higher at the end of the year. This if tariffs do not (unlikely) dent economic growth.

Fed: The markets see a 30% probability that the Fed will cut rates to 3.5%. This is if inflation does not show resilience or even rise, due to various factors. (imported inflation et al.)



In this context, we are maintaining our position in favor of short euro rates, as the risks are that the ECB will cut its monetary policy rates further.

We are taking a more cautious approach to US short-term rates, as we believe the markets are too optimistic about the prospect of easing over the summer.

We remain negative on the long end of the yield curve, anticipating a steepening in the context of increased fiscal expansion, particularly if fiscal largesse is combined with rate cuts.

We favor inflation-linked bonds to hedge against the risk of a resurgence of inflationary pressures, even though inflation expectations remain relatively subdued for now.

Finally, we are taking a short position on the dollar, which has been weakened by the erosion of the credibility of US institutions, relentless criticism of the Fed, rising political uncertainty linked to the trade war and the increased risk of domestic inflation fueled by profligate fiscal policy.

The ECB, meanwhile, is operating in a very different environment. Paradoxically, European pluralism, with its 27 members with divergent interests, makes interference more complicated and ultimately strengthens the institution's credibility. This environment leads us to favor euro-denominated bonds and currencies.

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