Central banks to step up the pace of rate cuts later this year

The Federal Reserve is poised to cut rates at every meeting this year and larger 50 basis point moves look plausible. The ECB and Bank of England are moving more slowly for now, but by the start of 2025 we think both will have stepped up the pace of easing

Federal Reserve

At the recent Jackson Hole conference, Fed chair Jerome Powell made it clear that the Federal Reserve would cut interest rates on 18 September, stating that "the time has come for policy to adjust. The direction of travel is clear". Our previous forecast update round coincided with the market volatility at the beginning of August and we changed our three 25bp rate cut call for this year to one whereby the Fed could cut by 50bp in September before reverting to 25bp moves in November and December with the policy rate reaching 3.5% by summer 2025.

A 25bp move on 18 September is slightly favoured by markets right now, but if we get a sub-100k on payrolls and the unemployment rate ticks up to 4.4%, or even 4.5%, then 50bp looks likely given Powell's comment that "we don't seek or welcome further cooling in labour market conditions". Even if they move by 25bp, there is still the possibility of a 50bp cut at some point with softening business surveys and hiring indicators suggesting the Fed will manoeuvre policy to a more neutral level relatively swiftly, in line with a cooling economy where inflation is on the path to 2%.

European Central Bank

With the latest inflation data out of the eurozone, a rate cut at the ECB's September meeting has almost become a done deal. As current headline inflation is closing in on 2% and longer-term inflation forecasts remain stable at around 2%, the ECB will see enough reason to reduce the level of monetary policy restrictiveness further. However, still high wage growth and too high selling price expectations suggest that the fight against inflation is not entirely over yet. This will make further rate cut decisions beyond the September meeting initially more complicated and controversial than currently priced in by financial markets.

Still, we expect the ECB to eventually show a stronger reaction to the weakening economic prospects of the eurozone, stepping up rate cut efforts in 2025. As a result, we see the ECB cutting rates by 25bp in September and December and another 100bp in the first half of next year.

Bank of England

The BoE cut rates for the first time at the August meeting but made it abundantly clear that it didn't want investors to run away with the idea that this will be an aggressive easing cycle. Policymakers are divided, but there's a general sense that services inflation is too high and wage growth has been consistently higher than expected. That's led some of the more hawkish members of the committee to conclude that it could still be more difficult to get inflation consistently back to target.

That means a September rate cut looks unlikely. But by November, we think the committee will have become more relaxed about the inflation backdrop and cracks in the jobs market may have started to show more clearly too. We therefore expect a cut in November and think a December move is more likely than not. We anticipate that rates will fall to 3.25% by next summer, which is a steeper move than markets expect.

Bank of Japan

The BoJ is set for a pause in September after a 15bp hike in July. Another hike in the fourth quarter remains likely, although the timing Is uncertain. Following market jitters in early August, the BoJ's policy stance is likely to have become more risk-adverse. Governor Kazuo Ueda signalled that the BoJ would not be in a hurry to take further policy action, as it examines the impact of financial market moves on inflation.

The sharp depreciation of the JPY should ease the BoJ's concerns about rising import prices. The policy uncertainty caused by the recent announcement of Prime Minister Fumio Kishida's resignation also won't be welcomed by the BoJ. Meanwhile, household spending and wage growth should improve, showing that the economy is moving in line with the BoJ's projection. Core inflation is likely to ease due to the re-starting of the utility subsidies for the summer months. We therefore see a slightly higher chance of a December hike than an October move for now.

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