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# Central banks: Fed & SNB update


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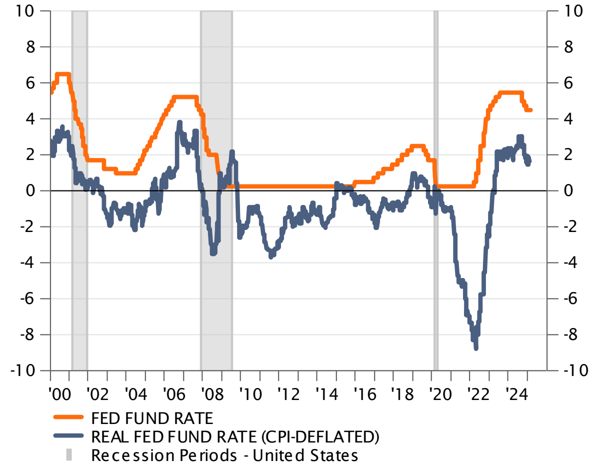
PRIVATE BANKING

## US Federal Reserve – Wait-and-see as the range of potential outcomes for the US economy is unusually wide

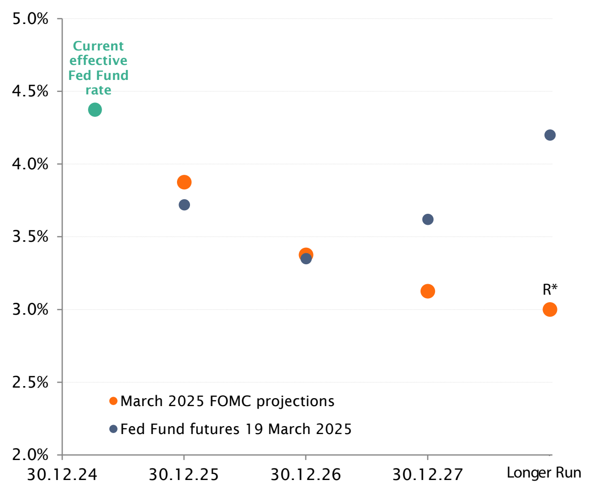
The US Federal Reserve held its target range for the Fed Funds rate unchanged yesterday, as widely expected.

***The Fed Fund rate was maintained at 4.5%, a level that is moderately restrictive with real rates (excluding inflation) around 1.5%.***




- For a second consecutive meeting, the FOMC adopted a wait-and-see stance, faced with significant uncertainties caused by the new administration's economic policies.
- After having lowered the Fed Funds rate by 100bp in the later part of 2024, the central bank is maintaining a moderately restrictive stance to its monetary policy, as the real short-term rate (short-term rate minus inflation) is still positive, around 1.5%.
- In parallel, the Fed announced a slowdown in the runoff of its balance sheet (slowdown in Quantitative Tightening), that will have a positive impact on market liquidity in the weeks ahead.
- Members of the Fed's committee continue to expect on average a resuming of the easing cycle later this year, with two 25bp rate cuts by the end of 2025, and a continuation of this trend next year with two additional 25bp rate cuts.
- Such scenario is also the one currently priced in by financial markets, even if those expectations have proven to be quite volatile in the recent weeks.

***Two 25bp rate cuts in 2025 and in 2026 remain the base case for Fed members and for markets, but uncertainty is rising, and future markets expect higher rates in the long run.***




*Source: Federal Reserve, Bloomberg*

Interestingly, a clear divergence between Fed members and financial markets appears on the long-term rate outlook:

- Based on yesterday's update, Fed members expect a gradual normalisation in economic conditions in the years to come, that will allow the Fed Fund rate to be lowered down toward 3%. This would be the estimated neutral level for an economy growing at slightly-below 2% rate in real terms, combined with a 2% inflation rate.
- Financial markets appear to hold a more sanguine view on long-term growth and inflation prospects for the US economy, with a Fed Fund rate that would increase from 2026, toward 4% or above. Such scenario is closer to the one aimed at by the new US Treasury Secretary Scott Bessent, who intends to raise US real GDP growth toward 3% (with inflation kept around the 2% level targeted by the Fed). Higher expectations for medium-term rates may also reflect investors' concerns around the US inflationary outlook.

Back to short-term prospects, the update of Fed's economic projections confirmed a trend that had started to worry investors in the recent weeks: the odds of a stagflationary scenario for the US economy are rising, even if they are not yet the most likely outcome for the months ahead.

- The recent slowdown in consumption dynamics and the deterioration in sentiment indicators are likely behind the downward revision to GDP growth projections for this year (to +1.7% down from +2.1% projected in December). Growth estimate for the next two years have also been slightly revised lower to 1.8%, the estimated long term growth rate of the economy (vs +2.0% and +1.9% previously projected).
- In the meantime, the Fed has revised its inflation forecasts up, acknowledging recent firmer inflation data and some impact of tariffs on imports. "Core" inflation is now projected to rise to +2.8% in 2025 (+2.5% previously expected), still clearly above the Fed's 2% target, before gradually slowing down toward 2% in the following years. Indeed, Fed's Chair Jerome Powell signalled that he viewed the impact of tariffs on inflation as likely "transitory", suggesting that the Fed would not overreact to a tariff-led acceleration in inflation in the coming months.

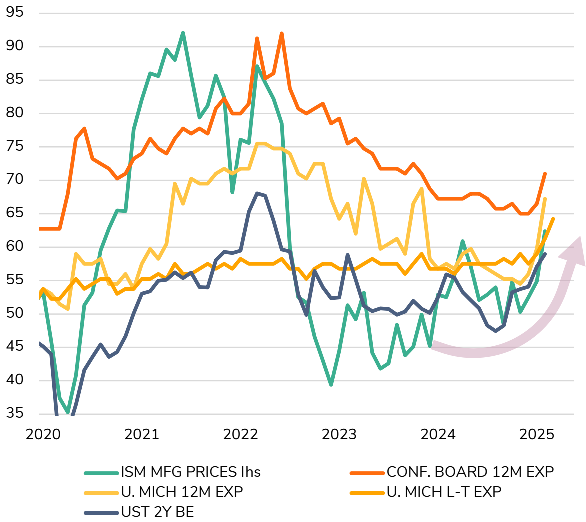
These adjustments in the Fed's economic projections should not be excessively worrying as they overall continue to point toward:

- a resilient economic expansion, around trend growth for the years ahead
- a robust labour market, with the unemployment rate essentially stable just above 4%
- a continuation of the disinflationary trend once the tariff impact on consumer prices dissipates

However, beside the usual pinch of scepticism that should always prevail when looking at economic projections, this update is surrounded by an unusual level of uncertainties related to economic policies and to the recent deterioration in consumer sentiment.

Indeed, household confidence has clearly declined since the beginning of the year, while inflation expectations have been rising. The prospect of tariffs pushing inflation higher and eating into consumers' purchasing power has not fully materialised into actual consumption data yet but risks of a slowdown in the US economy's main growth driver have clearly risen. Conversely, revived inflationary pressures could be amplified and sustained if US economic growth proves to be resilient to the President Trump-driven uncertainties in the coming months.

*Inflation expectations have been rising lately with prospects of tariffs on imports.*




In that context, the decision yesterday to leave the Fed Funds rate unchanged is a true "wait-and-see" stance. There were some episodes in the past when "wait-and-see" meant taking the time to assess when to make the next move in a direction that was already known. This time, the current environment creates a much wider range of possible outcomes:

- Should economic activity and inflation evolve exactly in line the Fed's economic projections, i.e. a mild growth slowdown and a temporary uptick in inflation, then the Fed will be able to follow the set path of a gradual easing in its still restrictive monetary policy stance.
- Should the recent deterioration in consumer sentiment extend and translate in a significant economic growth slowdown, the Fed will then face growing pressures to cut its rate at a faster pace to support economic activity. President Trump would certainly be the loudest advocate of significant rate cuts in such scenario.
- Should economic growth prove to be resilient in the coming months, with the support of tax cuts for businesses and households to be announced during the spring, the Fed could find itself in a situation where rate cuts no longer appear warranted. The question of rate hikes might even arise in this scenario if inflation dynamics become entrenched in business and consumers' expectations.

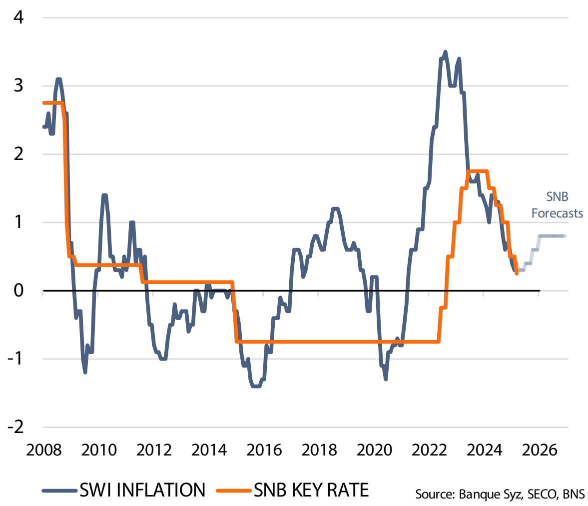
The worst case for the Fed would be a pronounced slowdown in economic activity combined with an acceleration in inflation. The likelihood of this stagflationary scenario remains remote for the time being but would certainly have significant repercussions for financial markets. It would also put the Fed between a rock and a hard place, torn between the two sides of its mandate, contain inflationary pressures and support economic activity. Faced with such unpleasant possibility and with an unusual number of uncertainties around the outlook, the best approach may indeed to wait for hints of things moving in one or the other direction before taking any decision. This is what the Fed and Jerome Powell did yesterday.

## SNB – One last cut, and likely done in a highly uncertain environment

The Swiss National Bank lowered its key policy rate by 25bp to 0.25% today, as it was widely expected.

- This rate cut follows the slowdown in inflation observed in the recent months, down to +0.3% in February.
- Low ongoing inflationary pressures, and the fact that inflation is now at the very bottom of the 0-to-2% target range of the SNB, warranted this additional decline in short-term interest rates.
- Indeed, with the SNB key rate at 0.25%, short-term real rates are brought down a marginally negative level that will help alleviate deflationary pressures and upward pressures on the Swiss franc.
- As such, monetary policy can be described as moderately accommodative, a stance appropriate to the combination of low inflationary pressures and moderate economic growth in Switzerland.
- Looking ahead, expected developments on inflation and economic activity suggest that the rate cut cycle initiated a year ago is now completed.
- The 150bp decline in CHF short term-rates over 12 months, in parallel of the decline in inflation, has helped supporting economic activity and stabilising the level of the Swiss franc.
- Inflation is now expected to stabilise in the coming months and even slightly pickup at the end of the year (toward +0.6%) and in 2026 (+0.8%). In the meantime, economic activity is projected to gradually improve, supported by higher real income for households due to the low level of inflation, and by more accommodative financing conditions.
- The stabilisation and even slight pullback of the Swiss franc also removes a headwind for Swiss exporters.

*The adjustment of the SNB policy rate to falling inflation has been completed.*




*Source: Banque Syz, SECO, BNS*

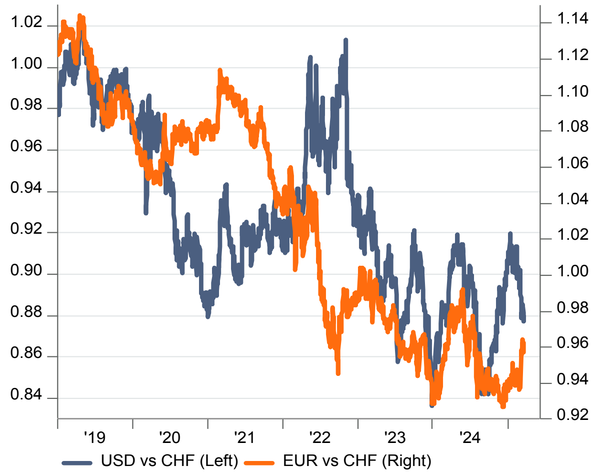
However, the outlook is currently extremely uncertain for Switzerland and for the global economy:

- Potential tariffs on US imports from Switzerland and other European countries could significantly impact economic activity and confidence. They could also possibly revive upward pressures on the Swiss franc. Such scenario would eventually lead the SNB to further lower its key rate down to zero.

- The possibility of a return to negative interest rates cannot be ruled out in case of pronounced downward pressures on growth, along with upward pressures on the currency. However, such possibility would, in our view, require a significant deterioration in the economic environment. Moreover, the SNB is more likely to resort to interventions on the Forex market as a first option in case of unwarranted upward pressures on the CHF.

Conversely, ongoing developments in the neighbouring Eurozone—particularly the prospect of a large fiscal stimulus in Germany—could significantly benefit Switzerland. Stronger demand from its main trading partner, reduced structural concerns about Eurozone growth, and a rebound in the euro would all be positive factors for the Swiss economy, supporting economic growth. Such scenario would also fuel firmer inflationary pressures via a higher activity level and a lower Swiss franc, possibly paving the way for the SNB to adjust its key rate upward in consequence in 2026.

***The Euro and the US dollar have broadly stabilised versus the Swiss franc since last year, helped by the adjustment in the SNB monetary policy.***




*Source: Banque Syz, SECO, BNS*

As a conclusion, today's rate cut is likely to be the last of this monetary policy easing cycle.

Financial conditions are now appropriate for the expected economic environment of 2025.

Downside risks to the growth and inflation outlook prevail in the short run, mostly related to ongoing trade tensions and the potential imposition of tariffs. In such scenario, the SNB might have to intervene on the Forex market and to lower rates further, possibly into negative territory in case of a sharp deterioration.

Over the medium run, some upside risks around the growth and inflation outlook have appeared recently with the shift in Germany's fiscal stance. But those potential developments will more likely be visible in the later part of 2025 or in 2026.

## For further information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