2025 Rate Cut Outlook: What's Keeping the Fed on Hold?

Services
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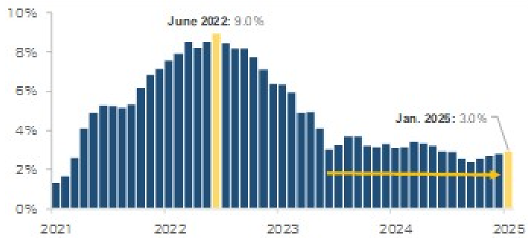
In recent years, the Federal Reserve (Fed) carried out one of the fastest rate-hiking campaigns in history to bring inflation down from a multi-decade high. After holding rates high for over 12 months, the central bank started its current rate-cutting cycle in late 2024, lowering rates by a total of -1% between September and the end of December. Where do things stand now? The central bank has two main objectives: (1) price stability, meaning low and stable inflation, and (2) full employment, which refers to conditions that create new jobs and keep unemployment low. The charts below show that the balance between those two goals has shifted in early 2025.

The chart on the left graphs the year-over-year change in the Consumer Price Index (CPI), which measures the change in price for a basket of goods and services. It shows that inflation progress has slowed. In January 2025, CPI rose by +0.5% from the previous month, the largest increase since August 2023. This caused the annual inflation rate to rise to +3.0% compared to December's +2.9%. While inflation has fallen significantly from its mid-2022 peak of around 9%, progress has stalled, with CPI hovering around 3% since late 2023. This recent data has added to concerns that inflation could remain above the Fed's 2% target for an extended period.

The chart on the right graphs the U.S. unemployment rate, revealing a labor market that remains strong by historical standards. In January, unemployment fell by -0.1% to 4.0%, the lowest since May 2024. Monthly job growth totaled +143,000, a slowdown from the post-pandemic hiring boom but indicative of steady labor demand. Additionally, job revisions for November and December 2024 were positive, with the U.S. adding +100,000 more jobs than initially reported. While the Fed cited rising unemployment as a reason to start cutting in 2024, recent data suggests the labor market isn't weakening as much as previously thought.

The latest CPI and unemployment reports underscore the complex economic landscape facing the Fed and the market. The central bank began cutting rates in 2024 as its focus shifted from reducing inflation to supporting the labor market. However, with inflation progress stalling and the labor market holding firm, many believe the Fed will pause its rate-cutting cycle until there is more clarity on both fronts. Reflecting this shift, the Fed held interest rates steady at its January 2025 meeting after three consecutive cuts from September to December 2024. Fed Chair Jerome Powell has also signaled a more patient approach, stating, "We don't need to be in a hurry" to adjust rates given current economic conditions. Market expectations have adjusted accordingly, with the next rate cut now anticipated in June 2025.

FIGURE 1 – Consumer Price Index (CPI % Year-over-Year Change)



Source: Bureau of Labor Statistics (seasonally adjusted). January 2021 to January 2025.

FIGURE 2 – U.S. Unemployment Rate

Source: Department of Labor (seasonally adjusted). January 2021 to January 2025.

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