

Global monetary policy: From chorus line to solo acts

- ▶ **US-Iran war has added fresh uncertainty to an outlook already clouded by tariff pressures.**
- ▶ **As various central banks navigate this, we see divergence in their monetary policy actions.**
- ▶ **We still see Fed cutting 50bp in 2026 and now see the Bank of England staying on hold.**
- ▶ **ECB is likely to do hesitant hiking (25-50bp); BoJ will do 25bp cautious front-loaded hike.**

The global monetary policy easing cycle has clearly lost momentum. Over the past three months, the pace of easing has slowed to a standstill, with 0% of developed market central banks cutting policy rates on a GDP weighted basis and only around 20% of emerging market central banks doing so. The next phase is likely to be defined not by synchronized easing, but by widening divergence: the Fed remains cautious, while the ECB is signaling rate hikes as Eurozone inflation shows upward bias. This creates a more complex policy landscape, where uncertainty is elevated and the risk grows that some central banks move ahead of others, potentially amplifying currency volatility, capital flow pressures, and cross market spill overs. The era of coordinated easing is over; what lies ahead is a fragmented monetary policy cycle with asymmetric risks. This is also likely to result in more split monetary policy committees across the central banks. In this note, following the central bank bonanza week (ending May 01, 2026), we take stock of meeting outcomes, and revisit of our policy rate expectations for the four key central banks – Fed, ECB, BoE, and BoJ.

Federal Reserve (FOMC)

Meeting outcome: The latest FOMC meeting delivered another steady policy decision, with the federal funds target range held at 3.50-3.75%. The Committee's internal dynamics, however, were more nuanced than the unchanged headline suggests. A group of policymakers pushed back against the continued use of language that markets interpret as an "easing bias," arguing that the statement should no longer imply that the next move is more likely to be a cut than a hike. This dissent did not translate into votes for a rate increase, but it did signal discomfort with the current communication framework. Chair Powell emphasized that policy remains well-positioned to "wait and see," even as he prepares to hand over leadership to Kevin Warsh in June. Markets absorbed the meeting calmly: front-end yields rose modestly on the hawkish tilt, the USD firmed, and risk assets continued to trade on earnings momentum rather than monetary policy.

Policy outlook: The Fed's forward path remains highly dependent on the evolution of inflation, particularly core PCE. Policymakers appear to want core PCE to fall below 3% – and ideally closer to 2.5% – before they are comfortable signaling a return to rate cuts. At the same time, the Fed expects tariff-related inflation pressures to fade over the next two quarters, which could help bring measured inflation lower without a deterioration in underlying demand. While the Committee's baseline remains a prolonged hold, the center of gravity is shifting toward a more neutral stance, and the leadership transition introduces an additional layer of uncertainty. If inflation moderates faster than expected and geopolitical volatility recedes, the Fed could still cut later this year. The hurdle is high, but not insurmountable, and the balance of risks is more symmetric than the recent dissent might imply. We continue to expect two rate cuts from the US Fed in 2026 – in September and December. Admittedly, our conviction on our call has weakened over the past couple of weeks.

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Bank of England (BoE)

Meeting outcome: The Bank of England opted for what it termed an “active hold,” keeping Bank Rate at 3.75% with an 8–1 vote. The decision reflected a deliberate balancing act rather than a passive pause. The MPC refrained from publishing a single central forecast, instead presenting three scenarios that differ primarily in their assumptions about energy prices and second-round inflation dynamics. All three scenarios imply some degree of upward pressure on rates, but the Committee was careful to avoid signaling inevitability. Governor Bailey noted that tighter market-based financial conditions may already be doing part of the Bank’s job, while several members – some historically dovish – indicated they would consider a hike if energy prices remained elevated. The tone of the meeting suggested a delicately balanced Committee, with the possibility of a rate rise at the next meeting but no firm commitment.

Policy outlook: The BoE faces one of the most challenging growth-inflation trade-offs among major central banks. The labor market is softening, real incomes remain under pressure, and the energy shock continues to cloud the near-term outlook. While the Bank’s scenarios show inflation falling back toward target in the more benign cases, the risk of second round effects remains a central concern. Market pricing reflects a meaningful probability of a hike in the coming months, but the Bank’s communication leaves open the possibility of staying on hold if energy prices stabilize or if demand weakens further. Importantly, the BoE retains flexibility within its mandate to take longer to return inflation to target if doing so avoids unnecessary volatility in activity. Against this backdrop, we think cuts later this year remain plausible, particularly if the more optimistic scenario materializes and the real-income squeeze intensifies. However, now our base case points to a hold from the BoE for the remainder of the year. Given the perceived reaction function of the BoE, the risks are tilted hawkishly – especially if energy prices were to stay elevated for the remainder of the year.

European Central Bank (ECB)

Meeting outcome: The ECB kept the deposit rate unchanged at 2.00% in a unanimous decision, but the Governing Council’s discussion revealed a more complex internal debate. President Lagarde acknowledged that both upside risks to inflation and downside risks to growth have intensified, and that the economy is drifting away from the baseline scenario published earlier in the year. The Council discussed the possibility of a rate hike “at length,” but concluded that it could afford to wait for more information. Lagarde emphasized the absence of clear second-round effects and pointed to early signs of labor-market softening as reasons not to move immediately. Markets interpreted the press conference as hawkish, with pricing for June tightening rising modestly, but the ECB avoided any explicit pre-commitment.

Policy outlook: Lagarde signaled that June will be a highly consequential meeting, noting that the ECB’s published scenarios are conditioned on two rate hikes. However, she also stressed that the policy path depends heavily on the duration of the Middle East conflict and the behavior of energy prices. If the Strait of Hormuz remains closed and oil stays above USD100/bbl., the ECB could move toward its adverse scenario, making a hike more likely. But the Governing Council’s emphasis on data-dependence, combined with the softening growth backdrop, means conviction on further tightening remains low. Second-round effects take time to materialize, and June may not provide definitive clarity. We think a hike or two is possible but far from assured, and the ECB may avoid additional tightening if energy pressures ease or if growth weakens further. Equally, any interest rate hikes in the near-term should be followed by more interest rate cuts in the medium-term (into 2027) especially if energy prices fall from the current levels sharply.

Bank of Japan (BoJ)

Meeting outcome: The BoJ held its policy rate at 0.75%, but the 6-3 vote revealed the widest split under Governor Ueda, with three members favoring an immediate 25bp hike. The updated Outlook Report strengthened the case for tightening, with inflation forecasts revised higher and growth expectations trimmed. Policymakers highlighted intensifying cost-push inflation from energy and reaffirmed their confidence in Japan's wage-price cycle, supported by structural labor shortages. The statement introduced more explicit language about considering the "timing and pace" of future adjustments while monitoring Middle East developments – an incremental but meaningful shift toward a more hawkish stance. Governor Ueda reiterated that the BoJ intends to continue normalizing policy but avoided giving any guidance on timing.

Policy outlook: The BoJ's challenge is navigating a stagflationary mix: rising inflation risks alongside slowing growth. The base case remains a single 25bp hike this year, in July, but the risk of a June move has increased, particularly given yen weakness and the potential for imported inflation. Fiscal dynamics – especially the sustainability of fuel-subsidy funding – add another layer of complexity. Governor Ueda emphasized that if the energy shock proves temporary, patience is warranted, but if second-round effects take hold, tightening will be necessary. The BoJ appears committed to continuing its cautious normalization path, with a bias to hike but a preference to avoid abrupt moves. We expect the Bank to proceed gradually, balancing the need to anchor inflation expectations with the desire to avoid destabilizing the recovery. Accordingly, we see one front-loaded rate hike followed by cautious well-balanced guidance from the BoJ in 2026.

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