A Global Balancing Act

Rate cuts, currency divergence, and geoeconomic realignments

→ The ECB continues its easing trajectory while the Fed points to conditional openness to policy shifts, creating growing transatlantic monetary divergence.

→ Inflation and economic growth remain asymmetrical, complicating central bank mandates globally.

As the first half of 2025 concludes, the financial and geopolitical landscape remains fraught with tension. While the post-April 2nd tariff negotiation period in the U.S. has technically entered its final days, consensus remains elusive. U.S. trade representatives have signalled openness to bilateral exemptions, yet China, Brazil, and India have hinted at retaliatory frameworks tied to digital services and critical minerals.

The result is a fragile situation layered over persistent economic uncertainty. Financial markets have shown heightened sensitivity to central bank decisions, fiscal imbalances, and real-time geopolitical developments.

U.S.: Monetary patience in a highly politicized climate

The Federal Reserve continues its wait-and-see approach, holding rates steady at 4.25% -4.50%. However, new messaging in June's FOMC minutes hints at a possible shift. Chairman Powell, while reiterating the need for "convincing evidence" of inflation moderation, acknowledged that "a window may be opening for limited recalibration."

The Fed continues its wait and-see approach, holding rates steady at 4.25%–4.50%; however, June's FOMC minutes hint at a possible shift

The White House intensified its rhetorical push for rate cuts, citing wage stagnation and softening in non-residential investment. Nevertheless, the Fed remains cautious. While headline inflation dipped to 2.4% in May, core inflation has proven sticky at 2.8%, with housing and services components still at high levels.

Bond markets have reacted with cautious optimism: the yield on 2-year Treasuries declined by 18 basis points in June, and volatility–while still elevated–has retreated slightly from April peaks. However, the inversion of the yield curve continues to reflect deep investor unease.

Europe: Rate cuts deepen but structural headwinds persist

The ECB announced its eighth consecutive rate cut in mid-June, lowering the deposit facility rate to 2.00%. Policymakers remain committed to easing

The ECB cut rates for the 8th time in a row in mid-June, bringing the deposit facility rate to 2.0%

despite some lingering inflation pressures, particularly in some southern economies where food and energy prices have not fully normalized.

Tariff turmoil and global economic uncertainty seem to be having a greater negative impact on prospects for the U.S. economy and the dollar than the widening U.S.-Eurozone rate gap, such that dollar-denominated assets are taking a hit

The ECB's easing has widened the U.S. Eurozone rate gap. However, the euro keeps appreciating against the U.S. dollar (well above 1.18 dollar/euro). Tariff turmoil and global economic uncertainty seem to be affecting more negatively the prospects for the U.S. economy and the dollar, such that dollar-denominated assets are taking a hit.

Investor positioning: Treading the tightrope

In fixed income, investors are increasingly barbell-structuring their portfolios, balancing short-duration inflation-protected assets with selective long-duration bets on easing cycles. The divergence between U.S. and European monetary paths has created fertile ground for currency-hedged carry trades and relative value strategies.

Equities remain range-bound, with investor enthusiasm tempered by geopolitical uncertainty. The tech sector, driven by AI and semiconductor dynamics, continues to outperform, but signs of sector fatigue keep emerging. Energy and industrials have become more attractive as hedges against geopolitical supply shocks, particularly in natural gas and critical materials.

Alternative assets–particularly infrastructure and renewables–have seen renewed interest, driven by both inflation protection features, and policy tailwinds related to energy sovereignty.

On 12 July, President Trump announced he would increase tariffs on all EU goods to 30% if the two sides do not reach a deal by 1 August

The next quarter will be decisive. On 12 July, President Trump announced he would increase tariffs on all EU goods to 30% if the two sides do not reach a deal by 1 August. He also threatened to raise tariffs even higher if the EU retaliates. Funcas plans to assess the implications of the announcement in the months ahead. The Federal Reserve's Jackson Hole Symposium in late August may mark a turning point in forward guidance, while the ECB will face pressure to justify further easing as inflation shows signs of persistence.

Investors will need to remain agile, monitoring not only interest rate decisions but also geopolitical developments

Investors will need to remain agile, monitoring not only interest rate decisions but also geopolitical developments. In a world where policy is reactive and crosscurrents are increasingly non-linear, staying ahead will require global awareness, tactical accuracy, and a large tolerance for unclear trends and ambiguity.