

# The Fed's strategic pause: the calm before the cuts

*In its June meeting, the U.S. Federal Reserve maintained current interest rates, pointing to ongoing tariff-related uncertainties. Nevertheless, the Fed indicated that two rate reductions remain probable before year-end.*

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## KEY TAKEAWAYS

- The Fed left policy unchanged, with the target policy rate range holding at 4.25%-4.50%.
- Updated economic projections reflect the expected impact of tariffs, showing slower growth and higher inflation than previously noted.
- The median Fed official still expects two 25 basis points (bps) rate cuts this year. That matches our outlook, and we expect a few more cuts in 2026.
- Chair Powell emphasized that growth remains solid, but uncertainty is high. He suggested that the Fed will remain patient, but the base case is still for two rate cuts this year.
- We see attractive investment opportunities in sectors that are somewhat defensive, insulated from tariffs and attractively valued.
- Asset classes to consider include private credit, global infrastructure, preferred securities and municipal bonds.

## WHAT HAPPENED?

The Federal Reserve kept rates unchanged today, with the target fed funds rate range holding at 4.25%-4.50%. The policy statement contained few substantive changes. Language saying that “uncertainty about the economic outlook has increased further” was removed in favor of a more moderate comment that uncertainty “has diminished but remains elevated.”

The Fed also published updated economic projections for the first time since March. As expected, it revised down this year's growth forecast to 1.4% and marked up the core inflation forecast to 3.1%. Those changes reflect the expected impact of large tariffs, which will likely weigh on growth while pushing up prices. The median forecast for the year-end policy rate remained unchanged, implying two 25 bps rate cuts, though the 2026 forecast showed just one rate cut next year, rather than two previously.

In his press conference, Chair Powell emphasized that conditions remain “highly uncertain” and that “the appropriate thing to do is hold where we are.” He said the FOMC expects higher inflation over the course of the summer as tariff effects hit, but that the economy overall is “solid.”

We anticipate two 25 bps rate cuts this year, followed by a few more cuts in 2026. These forecasts are based on our macroeconomic outlook and a probability-weighted view on the outlook for tariffs. But if tariffs end up higher than our models suggest, the Fed could loosen policy more aggressively (and vice versa).

## UNCERTAINTY CONTINUES TO CLOUD THE ECONOMIC OUTLOOK

The level of overall economic uncertainty remains elevated, although it has eased since the last FOMC meeting in early May. The broadest tariffs announced earlier this year – the “reciprocal” measures from 02 April – remain paused until next month.

Multiple scenarios are possible: The pause could expire, leading to increased tariffs; the pause might continue for another 90 days; the pause could become permanent; bilateral deals could be struck, creating varying tariff levels among trading partners.

Tariff uncertainty is compounded by broader fiscal uncertainty. Congress is negotiating a large tax and spending bill, which will likely substantially widen deficits over the near- and medium-term versus the policy baseline. Depending on the results of these negotiations, we expect U.S. federal budget deficits to widen to more than 7% of GDP over the next few years and possibly to 8% by the early 2030s if expiring tax cut provisions are renewed.

On the economic front, recent data are mixed. On the positive side, unemployment has remained low, and consumer spending has picked up slightly. Conversely, business and consumer sentiment remain poor, and job growth has slowed. Overall, data are consistent with a slow but steady deceleration in growth, in line with our expectations.

This high level of policy uncertainty and mixed economic data widens the set of possible economic outcomes. We continue to forecast a real U.S. GDP growth rate of around 1% this year, with core

inflation rising to 3% as tariff impacts hit later this summer. However, we lowered our confidence level in our base case, from 65% to 55%, with the odds of a downside growth scenario rising slightly.

## WHAT DOES THIS MEAN FOR INVESTORS?

Given the high level of uncertainty and likelihood that growth slows later this year, we see attractive opportunities for investors in sectors that are: a) somewhat defensive, b) insulated from tariffs, and c) attractively valued.

One area of opportunity is **private credit**. Because the asset class is often countercyclical, macroeconomic headwinds may be tailwinds for private credit. Service sectors currently provide some cushion amid trade and supply chain challenges, with their all-weather resilience translating to higher purchase price multiples and investor-friendly loan-to-value ratios of around 35%.

It's true that most private credit portfolios haven't been tested by a prolonged recession. By one estimate, only 5% of today's private credit managers existed before 2009. But our base case economic outlook doesn't call for a recession within the next 12 months. Moreover, during the past 16 years, all asset classes have faced the same obstacles, including budget standoffs, a global pandemic, supply chain disruptions and geopolitical conflicts, among others. Private credit has navigated these conditions well relative to other major credit sectors, and we believe it is well-positioned in the current environment.

**Global infrastructure** is another attractive asset class. Investors can gain exposure to the broad, secular theme of AI growth without the risk associated with highly valued equities and limiting sector concentration risks. Infrastructure has long been known for its defensive characteristics, such as its ability to potentially outperform broader equities during periods of negative returns. It is also uniquely positioned to benefit from the AI boom and the continued electrification of the global economy. In addition to data centers, areas of infrastructure

such as midstream pipelines, gas and electric utilities, and electricity transmission are critical to generating and sustaining the energy necessary to power rapidly evolving technologies and to meet the needs of communities where these systems and facilities are located.

In public fixed income, two areas stand out as attractively valued: preferred securities and municipal bonds. **Preferreds** were among the top-performing credit sectors during the rally in May. Total returns for the month were led by our favored segment, \$1000 par preferreds (+1.87%), followed closely by contingent capital securities (CoCos, +1.85%), with \$25 par preferreds lagging (-0.05%). Despite the rally, preferred spreads remain above historical lows. This, combined with continued robust fundamentals and a supportive technical backdrop, could make preferreds an attractive choice for diversifying portfolios in an unsettled macro environment.

**Municipal bonds** have struggled this year, as yields rose in tandem with other fixed income sectors following April's tariff shock, but they now look more relatively attractive. Notably, the upswing in yields has been unrelated to credit concerns. Tax-exempt bonds remain on solid financial footing, with state and local governments recording rainy day funds at 15% of 2025 spending levels, a dramatic increase over the 8% registered in 2019.

Current yields are elevated for investment grade and high yield munis, with income comfortably above or in line with long-term averages. Overall, yields are in the 96<sup>th</sup> percentile compared to payouts over the past 10 years ended 17 May 2025. Since higher yields translate to lower prices, municipal bonds may be poised to deliver not only income, but also the potential for capital gains.

**For more information, please visit us at [nuveen.com](https://nuveen.com).**

Endnotes

Sources

Federal Reserve Statement, June 2025.

Bloomberg, L.P.

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Concentration in infrastructure-related securities involves sector risk and concentration risk, particularly greater exposure to adverse economic, regulatory, political, legal, liquidity, and tax risks associated with MLPs and REITs.

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