

Central Banks Front and Centre

22nd September 2025

- Fed cuts rates as expected, but the backdrop remains mired in politics and evolving economic landscape.
- The US economic data is particularly difficult to interpret, and patience is needed.
- Risk of Fed policy error is high.
- Bank of England appears in no rush to cut.
- Bank of Japan has set the scene for a rate increase.
- Yen appears stronger, sterling is trading sideways, and dollar is still under some pressure.



As the market had been expecting, the Fed cut interest rates by 25bps last week, but rarely have we seen so many theories put forth about what the Fed is doing. The FOMC meetings are turning into pure theatre. Political brinkmanship and constantly evolving economic theory now dominate the talk.

The politics are poisonous. The chairman is being hunted down before his term ends in April next year. One member is under fire for alleged mortgage fraud. Another has been parachuted in for his fawning “disruptive” analytics. If it were not for the Federal Reserve Act of 1913, the whole Fed might have been shown the door, just as we saw at the CDC with respect to the Advisory Committee on Immunization Practices.

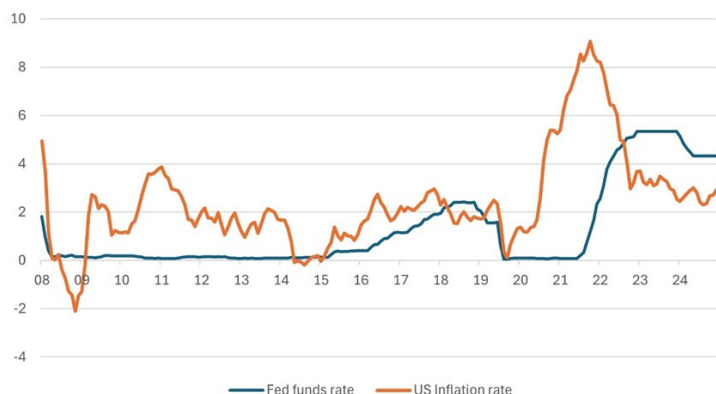
The data the Fed relies on to make decisions has been no better. The quality of economic data has deteriorated badly in recent months. Thanks to DOGE, fewer people are now collecting price data, for example. As a result, 35% of the inflation report is now imputed. That number was 10% at the start of the year. We are in a dangerous blind spot.

The labour market is adding to the confusion. It has become a testing ground for competing theories. There are also similar data collection challenges. Migration, ageing, lack of skilled labour, technology - forces that used to be background noise are now front and centre. The moving parts are swaying harder and faster than in past cycles (see special section later for more detail)

All this put together raises the risk of a monetary policy error sharply. We must remember that economic cycles are defined by policy errors. At this juncture, the question is whether the President will accept that interest rates alone cannot steer the US economy. The Trump government appears to have forgotten its pledges to cut ‘red tape’ and ease business. Immigration and tariff policies continue to complicate corporate life.

For markets the message is clear: when politics, poor data, and structural labour shortages combine, the odds of a Fed misstep rise. That misstep will not be academic this time, it will be the spark that sets the next turn in the cycle, and investors should be ready.

Chart 1: US Fed funds and Inflation - the Future will Likely be Different to the Past
(%)



Source: Bloomberg

The Central Banks in Japan and the UK have their challenges, but they are a little more conventional

The Bank of England kept the bank rate unchanged at 4.0% in a 7–2 vote, with a few voices pushing for a modest cut. The more notable shift came in the form of quantitative tightening: the Bank announced that it will slow the pace of gilt sales to £70 billion over the next year from around £100 billion previously, with fewer long-dated bonds being released. The decision reflects the central bank’s desire to strike a delicate balance. Inflation remains at 3.8%, well above target, with wage pressures and services inflation still uncomfortably high. Yet, growth is stalling, labour-market slack is emerging, and gilt markets have shown fragility. The Bank’s caution highlights the risk of destabilising financial conditions while trying to normalise policy. However, the markets will also have to navigate what may be brutal budget as the UK Chancellor. The UK heads into November’s Budget with public borrowing already overshooting forecasts and productivity downgrades looming. With the Bank of England holding back on rate cuts amid stubborn inflation, the Chancellor faces an ugly mix of higher debt costs, limited fiscal headroom, and the unenviable choice between tax rises and spending restraint.

For investors, the message is that the BoE is in no rush to cut. As we understand, any easing will be gradual and contingent on firmer progress in disinflation. That stance provides some short-term support for sterling, as hopes of aggressive rate cuts diminish. **However, Sterling is unlikely to make decisive gains against the dollar, where the Fed still holds the hawkish advantage. However, it may hold its ground against the euro if the ECB strikes a softer tone.**

Chart 2: UK Sterling Likely Biased Lower against the Dollar
GBP/USD



Source: Bloomberg

The Bank of Japan kept its policy rate at 0.5%, but the move signalled a gradual shift away from extraordinary monetary stimulus. It announced plans to start selling some of its holdings of ETFs and REITs (equivalent to 7% of the equity market), unsettling markets that had grown comfortable with the BoJ as a steady buyer of risk assets. However analysts stress that despite scale of the BoJ’s holding, the unwind is extremely slow. At current pace, it would take over 100 years to sell off the entire ETF/REIT portfolio.

Core inflation remains at 2.7%, above the 2% target, yet most of the board preferred to wait, citing weak domestic demand and global uncertainty. Highlighting growing divisions on policy decisions within the BoJ, two members dissented, pressing for an immediate hike to 0.75%.

Markets interpreted the combination of dissenting voices and the announcement of asset sales as a hawkish posturing. The yen strengthened, while Japanese equities slipped on concerns of reduced central bank support. Investors are not ruling out a rate hike as soon as October, if inflation stays firm. Political uncertainty, with a change in party leadership on the horizon, adds another layer of complexity to the current dynamic. The overall message is that the BoJ is still cautious, but the era of unquestioned accommodation is drawing to a close. Most technical analysts see the yen trading in a range, with firm support around ¥145–146 and resistance near ¥149–150, leaving the dollar-yen pair choppy until one of those levels gives way.

Chart 3: Yen Range Bound Against the Dollar



Source: Bloomberg

Just some Background Reading on the US Labour Market

We must not rush to read the softer payroll numbers as a harbinger of economic malaise – that risks missing the deeper story. America's problem is not simply weak demand; it is that the supply of workers has structurally thinned. The prime-age participation rate sits near a record 83.7%, so there is little hidden slack left to draw on. Older cohorts continue to retire, and with over 10,000 Americans turning 65 every day, the demographic drag is relentless. Immigration, once a reliable shock absorber, has slowed sharply: net inflows in 2025 are tracking closer to 1–1.5 million, less than half the peaks of 2022–23. The result is a labour market that looks sluggish on the surface but is in fact running into a wall of scarcity.

This labour scarcity has knock-on effects. Employers report more than 8 million job openings nationwide, yet the Beveridge curve has shifted outward, more vacancies exist at any given unemployment rate, indicating a mismatch in skills. Healthcare and construction firms are raising wages aggressively to attract scarce talent, while in advanced manufacturing, positions remain unfilled despite solid demand. In short, what once would have been read as cyclical weakness is a structural constraint.

We are at one of those inflection points, where old correlations break down, where thirty years of statistical relationships no longer map neatly in today's reality. Anchoring analysis – or investment decisions – on what 1990s or 2000s were like, when labour supply grew 1% per year – will not help when today's trend is closer to just 0.3%. To interpret current data with the tools of the past is to misread the present; the dynamics of the US economy are shifting, and we must recalibrate our thinking accordingly.

For markets, the policy implication is stark. If the Fed or investors chase payroll growth back to levels no longer commensurate with the demographic and migration realities, they risk cutting rates too far, mistaking scarcity for slack. That would inject unnecessary stimulus into an economy already constrained on the supply side, fuel for higher wage inflation and sticky prices. The challenge now is not to rescue growth at all costs, but to recognise that the capacity of the US economy has changed, and policy must adjust with it.



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Falco Model Performance (as of 31 August)

Falco Models	1 Month	2025 YTD	2024	2023	2022	2021	2020	2019	IRR Since Inc
FPW Cautious	+0.03%	+4.16%	+6.89%	+6.86%	-10.14%	+3.44%	+10.80%	+12.30%	+4.90%
FPW Balanced	+0.13%	+5.76%	+9.56%	+6.51%	-9.75%	+5.10%	+11.10%	+14.90%	+6.21%
FPW Speculative	+0.48%	+8.59%	+11.72%	+7.88%	-10.06%	+9.42%	+13.60%	+18.50%	+8.60%
FPW 100% Equity	+0.91%	+8.27%	+15.74%	+15.82%	-7.19%	+18.05%	+9.36%	+21.34%	+11.85%

Low-Coupon Gilt Summary (as of 22 September)

Holding	Coupon	Maturity Date	Price	Yield to Maturity
0.125% Treasury Gilt 2026 (T26)	0.125%	30/01/2026	£98.89	3.31%
0.375% Treasury Gilt 2026 (T26A)	0.375%	22/10/2026	£96.42	3.78%
0.125% Treasury Gilt 2028 (TN28)	0.125%	31/01/2028	£91.87	3.76%
0.50% Treasury Gilt 2029 (TG29)	0.50%	31/01/2029	£89.40	3.87%
0.375% Treasury Gilt 2030 (TG30)	0.375%	22/10/2030	£83.44	4.01%
0.25% Treasury Gilt 2031 (TG31)	0.25%	31/07/2031	£80.07	4.11%
0.50% Treasury Gilt 2061 (TG61)	0.50%	22/10/2061	£24.25	5.13%

Example Cash Deposits (as of 22 September)

Holding	Interest Rate	Max Deposit	FSCS Protection
Instant Access Deposit	4.03%	£1,000,000	Yes
95 Day Notice Account	3.82%	£2,000,000	Yes
1 Year Fixed Term Deposit	4.40%	£3,000,000	Yes
2 Year Fixed Term Deposit	4.15%	£2,000,000	Yes
5 Year Term Deposit	4.25%	£2,000,000	Yes

Yield Enhancement Examples (as of 18 September)

Holding	Structure	Liquidity	Average Maturity	Yield to Maturity
GBP Liquidity Fund	UK OEIC	Daily	48 days	3.94%
USD Liquidity Fund	Lux SICAV	Daily	52 days	4.12%
Example Short Duration Investment Grade ETF	ETF	Intra-day	2.4 years	4.13%
Example Short Duration High Yield ETF	ETF	Intra-day	2.4 years	5.69%
Example Fixed Income ETF Portfolio	ETF	Intra-day	6 years	5.60%
Asset-Backed Mortgage Bond (GBP and USD)	Bond	Daily	2 years	10.5%

Past performance is not a reliable indicator of future performance. The value of investments can go down as well as up, and you may get back less than you invested. Investment returns are not guaranteed, and all investments carry a degree of risk.