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Central Bank Monetary Policy Space: Q4-2025

Policy Space For G10 and Emerging Market Central Bank Rate Cuts Is Shrinking

Summary

Central bank monetary policy remains top of mind for most market participants, especially now that the Federal Reserve has restarted its easing cycle. But do Fed rate cuts generate policy space for international central banks to continue respective easing cycles? In select cases, tentatively, yes. In others, decisively, no.

With Q4 now underway, we have updated our emerging market central bank monetary policy space framework to assess which EM central banks can continue cutting rates through the end of this year. Our framework reveals that select institutions can deepen rate cutting cycles now that the Fed is lowering rates, but thematically, room to ease is shrinking. We also introduce a new framework designed to gauge monetary policy space for G10 central banks. Exceptions exist, but similar to emerging market central banks, policymakers in advanced economies may also be nearing, or already at, the end of their respective easing cycles.

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G10 Central Banks

G10 Central Bank Monetary Policy Space: Q4-2025 Takeaways

- G10 central banks are approaching the end of their respective easing cycles
    1. Real interest rates and broader monetary policy settings are mixed, but on balance, have moved closer toward neutral
    2. Further disinflation, thematically, will be difficult to achieve and should limit policymakers bias toward additional rate cuts
    3. Economic momentum is sluggish, which could be a source of near-term rate cuts; however, medium-term growth prospects are not far from potential and a need for significantly more easing may not be needed
- According to our framework:
    1. Only two institutions have "Adequate Monetary Policy Space." Sluggish economic momentum and medium-term growth prospects are the driving force of policy space
    2. Central banks with "Limited Monetary Policy Space" have room for interest rate cuts due to subdued near and medium-term growth prospects, but in-range inflation and neutral monetary policy settings restrain capacity for cuts
    3. Most G10 central banks have no policy space for rate cuts. These central banks are associated with resilient economies, neutral monetary policy settings and inflation within target ranges
- Financial market pricing may be misaligned with underlying fundamentals in:
    1. New Zealand. Reserve Bank of New Zealand (RBNZ) may ease more than our framework suggests, and more than markets are priced for, over the next two meetings as the economy is in contraction
    2. Canada. Subdued inflation shifts policymakers' focus to growth. Sluggish activity and a rising jobless rate is a combination that tilts the balance of risk toward more Bank of Canada easing than we forecast, and more than markets are pricing
    3. Eurozone. We believe European Central Bank policymakers can deliver one last 25 bps rate cut this year; however, our framework signals that the easing cycle is over. Markets are split pricing 10 bps of cuts.
    4. Japan. Elevated inflation pressures and strong growth should now prompt a 25 bps Bank of Japan rate hike by YE-25

G10 Central Bank Monetary Policy Space: Framework Output

Our framework suggests the Reserve Bank of New Zealand (RBNZ) and the Bank of Canada (BoC) are the only two G10 central banks with adequate policy space for rate cuts in Q4-2025. Additional easing may be delivered from select institutions, but thematically, our framework reveals G10 easing cycles are mature and nearing an end

	Central Bank Policy Rate	Wells Fargo YE-25 Forecast (bps change)	Perceived Policy Rate Cuts (bps)	Market Implied Rate Change (bps)	Q4-2025 Monetary Policy Space [1] [2]	Real Interest Rate (%)	Inflation From CB Target (%)	Economic Momentum	Output Gap (% of Potential Growth)
New Zealand	3.00%	(75)	(25-50)	(62)					
Canada	2.50%	(25)	(25-50)	(18)					
Australia	3.60%	(25)	(0-25)	(14)					
Switzerland	0.00%	0	(0-25)	(6)					
United Kingdom	4.00%	0	(0-25)	(10)					
Norway	4.00%	0	0	(5)					
Sweden	1.75%	0	0	13					
Eurozone	2.00%	(25)	0	(9)					
Japan	0.50%	25	0	18					

[1] Green indicates "Adequate Monetary Policy Space", Orange indicates "Limited Monetary Policy Space", Red indicates "No Monetary Policy Space"

[2] Adequate Monetary Policy Space represents scope for 25-50 bps of rate cuts, Limited Monetary Policy Space represents scope for 0-25 bps of rate cuts, No Monetary Policy Space represents scope for 0 rate cuts

G10 Central Bank Monetary Policy Space: Overview & Methodology

- Monetary policy space analyzes G10 central banks' capacity to lower interest rates in the current calendar year
- Monetary policy space assesses capacity for interest rate cuts arising from:
    I. Current monetary policy settings: measured by real interest rate
    II. Inflation expectations: measured by a forward-looking assessment of inflation relative to central bank CPI targets
    III. Economic momentum: measured by proxy indicators for GDP growth
    IV. Output gap: measured by Wells Fargo GDP forecast vs. Potential GDP
- Our framework aggregates indicators to determine overall space for central bank interest rate cuts (Adequate, Limited or No Space)
- Our framework also assigns a basis point adjustment (50 bps, between 0-25 bps, or 0 bps) that each central bank can pursue based on overall monetary policy space
- The framework is designed to act as a starting point for the direction and magnitude of policy rate changes, but is not necessarily a forecast or an expression of directional bias. Actual G10 policy rate forecasts may differ from the framework's output
- Should the combination of our framework and empirical judgment suggest a greater or lesser degree of easing relative to financial market pricing, opportunities in rates as well as FX may be present
- For our framework to be most effective, monetary policy space relies on:
    I. Independent and credible central bank (i.e., no real or perceived political influence)
    II. Orthodox monetary policy theory (i.e., higher policy rates leads to lower inflation)
    III. Coordinated fiscal and monetary policy (i.e., no overwhelming fiscal dominance)
    IV. No major economic distortions (i.e., geopolitical conflict)

Emerging Market Central Banks

Emerging Market Central Bank Monetary Policy Space: Q4-2025 Takeaways

- Thematically, emerging market central banks may not adjust policy rates all that significantly in the coming months

  I. Fed cuts have created marginal room for central banks to ease further; however, real rates are a fading source of policy space

  II. Most emerging market central bank easing cycles are restrained by above-target inflation expectations

  III. Economic momentum is resilient and limits capacity for more easing, although growth prospects vary across economies

  IV. FX strength is the most consistent source of policy space despite select currencies weakening off recent highs

- According to our framework:

  I. Only two institutions have “Adequate Monetary Policy Space”, down from seven at the beginning of Q3. These central banks have positive real rate differentials with the Fed, contained inflation and FX stability in common

  II. Central banks with “Limited Monetary Policy Space” are mostly restrained by above-target inflation and resilient economic momentum. Real rate differentials and FX strength, however, offer room for these institutions to cut rates

  III. The Chilean Central Bank joins the Central Bank of Argentina as the only institutions with “No Monetary Policy Space”

- Financial market pricing may be most acutely misaligned with underlying fundamentals related to:

  I. Indonesia (BI). Fundamentals align with up to 25 bps of Bank Indonesia cuts in Q4. However, the administration prefers stronger growth, which requires lower policy rates, a dynamic our framework and market pricing may not be capturing

  II. Mexico. Fed rate cuts generate room for Banxico to extend its easing cycle, but with the Banxico-Fed rate gap historically narrow and core inflation elevated, policymakers may end rate cuts sooner than markets expect in line with our framework

  III. South Africa. Proposed revisions to the CPI target mean SARB may be on hold for an extended period of time

  IV. Poland. Thin real rate differentials, above-target inflation and positive economic momentum limits additional National Bank of Poland easing. Perhaps another 25 bps cut is delivered, but markets are priced for closer to 50 bps of easing by YE

Emerging Market Central Bank Monetary Policy Space: Framework Output

Policy space for easing across the emerging markets is shrinking. Fed rate cuts generate room for rate cuts; however, fundamentals suggests easing should be limited over the next few months

	Central Bank Policy Rate	Perceived Policy Rate Cuts (bps)	Market Implied Rate Change (bps)	Q4-2025 Monetary Policy Space [1,2]	Real Int. Rate Diff. With Fed (%)	Inflation From CB Target (%)	Economic Growth Momentum	FX Performance vs. USD (Last 3 months)
China [3]	1.40%	(25-50)	1					
Philippines	5.00%	(25-50)	(15)					
Indonesia	4.75%	(0-25)	(31)					
Peru	4.25%	(0-25)	(10)					
Israel	4.50%	(0-25)	(14)					
South Africa	7.00%	(0-25)	(29)					
South Korea	2.50%	(0-25)	(3)					
Russia	17.00%	(0-25)	(160)					
Brazil	15.00%	(0-25)	0					
Colombia	9.25%	(0-25)	(8)					
India	5.50%	(0-25)	(5)					
Mexico	7.50%	(0-25)	(59)					
Hungary	6.50%	(0-25)	(25)					
Thailand	1.50%	(0-25)	(32)					
Turkey	40.50%	(0-25)	(309)					
Poland	4.75%	(0-25)	(42)					
Chile	4.75%	0	(14)					
Argentina	29.00%	0	(300)					

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[2] Adequate Monetary Policy Space represents scope for 25-50 bps of rate cuts, Limited Monetary Policy Space represents scope for 0-25 bps of rate cuts, No Monetary Policy Space represents scope for 0 rate cuts

[3] People's Bank of China 7 Day Reverse Repurchase Rate

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- Monetary policy space assesses capacity for interest rate cuts arising from:
    - I. Relative monetary policy settings: measured by real interest rate differential with the Federal Reserve
    - II. Inflation expectations: measured by a forward-looking assessment of inflation relative to central bank CPI targets
    - III. Economic activity: measured by proxy indicators for GDP growth
    - IV. Financial stability & imported inflation risk: measured by FX performance vs. U.S. dollar
- Our framework aggregates indicators to determine overall space for central bank interest rate cuts (Adequate, Limited or No Space)
- Our framework also assigns a basis point adjustment (25-50 bps, between 0-25 bps, or 0 bps) that each central bank can pursue based on overall monetary policy space
- The framework is designed to act as a starting point for the direction and magnitude of policy rate changes, but is not necessarily a forecast or an expression of our directional bias for monetary policy
- Should the combination of our framework and empirical judgment suggest a greater or lesser degree of easing relative to financial market pricing, opportunities in rates as well as FX may be present
- For our framework to be most effective, monetary policy space relies on:
    - I. Independent and credible central bank (i.e., no real or perceived political influence)
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    - IV. No major economic distortions (i.e., geopolitical conflict)

Wells Fargo G10 and Emerging Market Central Bank Policy Rate Forecasts

Wells Fargo International Interest Rate Forecast

(End of Quarter Rates)

	Central Bank Key Policy Rate						
	2025		2026				2027
	Current	Q4	Q1	Q2	Q3	Q4	Q1
United States	4.25%	3.75%	3.50%	3.25%	3.25%	3.25%	3.25%
Eurozone[1]	2.00%	1.75%	1.75%	1.75%	1.75%	1.75%	1.75%
United Kingdom	4.00%	4.00%	3.75%	3.50%	3.25%	3.25%	3.25%
Japan	0.50%	0.75%	0.75%	0.75%	0.75%	0.75%	0.75%
Canada	2.50%	2.25%	2.25%	2.25%	2.25%	2.25%	2.25%
Switzerland	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Australia	3.60%	3.35%	3.10%	3.10%	3.10%	3.10%	3.10%
New Zealand	3.00%	2.25%	2.25%	2.25%	2.25%	2.25%	2.25%
Sweden	1.75%	1.75%	1.75%	1.75%	1.75%	1.75%	1.75%
Norway	4.00%	4.00%	4.00%	3.75%	3.50%	3.50%	3.50%
China[3]	9.00%	8.50%	8.50%	8.00%	8.00%	7.50%	7.50%
India	5.50%	5.25%	5.25%	5.25%	5.25%	5.25%	5.25%
Mexico	7.50%	7.25%	7.25%	7.25%	7.25%	7.25%	7.25%
Brazil	15.00%	15.00%	14.50%	14.00%	13.50%	13.00%	12.50%
Chile	4.75%	4.25%	4.25%	4.25%	4.25%	4.25%	4.50%
Colombia	9.25%	9.25%	9.00%	8.50%	8.50%	8.50%	8.50%
Russia	17.00%	15.00%	13.00%	11.00%	10.00%	9.00%	8.50%

Forecast as of: October 1, 2025

[1] ECB Deposit Rate [2] German Government Bond Yield [3] Reserve Requirement Ratio Major Banks

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