FROM THE DESK OF

New York Life Investment Management
Global Market Strategy team

September FOMC: tightening resumes, more to come

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Investment Management

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September FOMC: tightening resumes, more to come

As of 4:30pm ET, 16 September 2026

- The FOMC unanimously raised the federal funds rate by 25bp to 3.75-4.0%. The Committee reinforced its inflation focus, noting that today's action is intended to support a "timelier return" to its 2% inflation target.
- Importantly, the Fed signaled that today's hike is unlikely to be a one-off. The updated dot plot shows an overwhelming majority of FOMC participants expect at least one additional hike this year. While we continue to see room for the Fed to remain on hold, the Fed has made clear that the balance of risks has shifted in response to inflation pressures. We have therefore updated our outlook to include one additional rate hike before year-end.
- In the press conference, Chair Warsh characterized the hike as removing "a dose of accommodation," while emphasizing that the U.S. economy appears to be strengthening. The combination suggests that the Fed sees room to tighten further to address inflation without necessarily containing economic activity.
- Markets took the decision as hawkish. The rally in Treasuries ahead of the announcement partially reversed, with the policy-sensitive 2-year yield moving higher as investors digest the hike and prospect of further tightening. The dollar appreciated following the decision, consistent with a higher expected path for U.S. policy rates.

Inflation risks push the Fed toward higher rates

As we noted following last week's CPI report, it was not simply the latest inflation print that drove the sharp repricing of Fed expectations. The more important concern was what the data suggested about the path ahead. With crude oil and gasoline prices running well above August levels, the Fed faced the prospect that already-elevated inflation could accelerate further in the coming months.

At the same time, the broader economic data arguably gave the Fed room to remain on hold, consistent with our view going into the meeting. The labor market is broadly balanced, wage growth has moderated, and inflation expectations remain well anchored. Moreover, monetary policy remains a blunt tool for addressing supply-driven inflation, particularly an increase in energy prices. Energy shocks can also be self-limiting, weighing on consumer demand, economic growth, and corporate margins, while the effects of monetary policy operate with long and variable lags.

The Fed ultimately placed greater weight on the upside risks to inflation. Chair Warsh characterized the economy as strengthening. The Fed appears to see greater scope to tighten policy to prevent higher energy prices from feeding into broader and more persistent inflation. The updated dot plot reinforces that message, with most FOMC members expecting at least one additional rate hike this year. The decision and projections suggest the Fed is increasingly willing to accept the risk of additional tightening to prevent those second- and third-order effects from elevated oil prices.

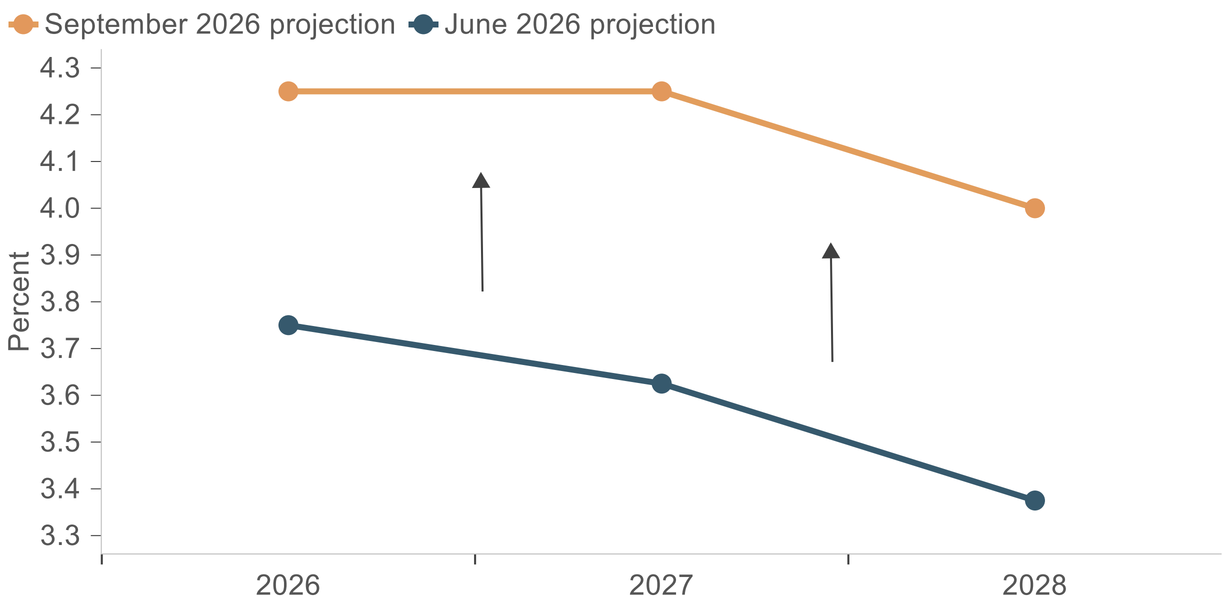
The dots may matter more than the hike itself

The more consequential signal may come from the updated Summary of Economic Projections (SEP). Twelve of the 16 participants expect at least one more hike this year. Beyond year-end, there is much less agreement. The 2027 dots are widely dispersed, with the median implying no change. Still, with roughly half the Committee expecting one more hike in 2027, a hawkish bias is likely to persist unless inflation pressures moderate.

On inflation, the SEP shows that participants view inflation as a greater risk than they did in June. The 2026 PCE projections increased from 3.6% in June to 3.7%, with PCE cooling gradually through 2027 and 2028. FOMC participants are also optimistic about growth and the labor market, with real GDP projections increasing for both 2026 and 2027, while they expect unemployment to remain unchanged.

The Fed's rate path shifts higher

FOMC median rate projections



Sources: New York Life Investment Management, Global Market Strategy, Federal Reserve, Macrobond, September 2026.

Investment implications

The key portfolio question has shifted from whether the Fed will hike to how much additional tightening follows. We have updated our base case to include one more rate hike this year, consistent with the updated dot plot. Beyond that, the path is less certain and will depend on how quickly inflation moderates. For portfolios, this keeps the focus on the effects of higher rates today.

In equities, we believe expectations for higher policy rates and the recent rise in yields are pressuring valuations lower. However, a more sustained hiking cycle could increase downside risks to growth and earnings, strengthening the case for quality and defensive exposure.

Further Fed hikes may narrow the divergence between the U.S. and other developed-market policy paths. With the ECB already raising rates and markets pricing further tightening in Europe, a more hawkish Fed will help close that gap. This could provide some support for the dollar, which we saw move higher following the FOMC statement, and temper the case for rotation away from U.S. assets.

In fixed income, higher policy rates increase the income available at the front end of the curve, adding to the appeal of short-maturity credit. At the long-end, a hawkish Fed may help contain some of the recent rise in long-rates, tempering inflation expectations and uncertainty around the path of policy. We continue to see opportunity to extend duration with the 10-year Treasury yield above 4.7%. A sustained move above 5% could signal a more fundamental shift in how investors demand compensation for U.S. fiscal and policy risk, but this is not our base case.