Fed Delivers 3.75%-4.00% Hike, Confirms Aggressive Path for the Rest of the Year

Economic Review
Sep-26 FOMC Meeting



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Economic Review

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- Recent data points to solid US economic activity, with Fed Chair Kevin Warsh highlighting at the Sep-26 press conference that the economy has strengthened further in recent months. This is consistent with the FOMC's assessment that economic activity continues to expand at a solid pace, supported by stronger consumer spending and increased business investment
- The latest Summary of Economic Projections (SEP), reflecting the views of 18 Fed policymakers, also points to a firmer US economic outlook. The median forecast for real GDP growth in 2026 was raised to +2.3%, from +2.2% in June, while the unemployment rate is projected at around 4.1%.
- We foresee a relatively more hawkish policy outlook with the possibility of one rate hike by the Fed later this year. This additional policy tightening may be considered to contain elevated price pressures.

Fed hike by +25bps to keep inflation in check

The Federal Open Market Committee (FOMC) raised the federal funds rate target range by +25bps to 3.75–4.00% at its Sep-26 meeting, marking the first rate hike since 2023. The decision was broadly in line with market and our expectations, as the Fed sought to contain persistent inflationary pressures amid resilient economic activity. The decision was unanimous, reflecting continued concerns over elevated inflation, which remains above the Fed's +2% longer-run target.

Solid economic activity, with stable job market

Recent data points to solid US economic activity, with Fed Chair Kevin Warsh highlighting at the Sep-26 press conference that the economy has strengthened further in recent months. This is consistent with the FOMC's assessment that economic activity continues to expand at a solid pace, supported by stronger consumer spending and increased business investment. At the same time, the labour market remains relatively stable, with job gains broadly keeping pace with labour-force growth and the unemployment rate showing little change. The combination of strengthening economic momentum and a still-resilient job market suggests that the economy remains sufficiently firm to withstand tighter monetary policy, allowing the Fed to place greater emphasis on containing persistent inflationary pressures.

Inflation remained elevated, driven by higher energy prices

The Fed reiterated that inflation remains elevated above its +2% longer-run target, with recent price pressures partly reflecting supply-side and energy shocks. US headline CPI inflation remained high at +3.4%yoy in Aug-26, unchanged from Jul-26, as energy inflation accelerated further to +16.3%yoy (Jul-26: +14.7%yoy), including a +27.4%yoy rise in gasoline prices. In contrast, underlying inflation showed some moderation, with core CPI easing to +2.4%yoy in Aug-26 (Jul-26: +2.5%yoy). Nevertheless, headline inflation remains well above the Fed's objective, while the renewed rise in energy costs continues to pose upside risks to the inflation outlook.

Fed upgrades growth outlook, signals another hike

The latest Summary of Economic Projections (SEP), reflecting the views of 18 Fed policymakers, also points to a firmer US economic outlook. The median forecast for real GDP growth in 2026 was raised to +2.3%, from +2.2% in Jun-26, while the unemployment rate is projected at around 4.1%, lower than the Fed's previous expectation of 4.3%, indicating greater confidence in the resilience of the labour market. However, inflation remains the key concern, with headline PCE inflation projected at +3.7% in 2026, slightly higher than the +3.6% projected in Jun-26, while core PCE inflation is expected at around +3.4%. Policymakers now expect inflation to return to the +2% objective only gradually, reinforcing the case for maintaining a restrictive policy stance.

On monetary policy, the updated projections indicate that the Sep-26 hike is unlikely to be a one-off adjustment. Sixteen of the 18 policymakers envisage at least one further rate increase this year, with the median projection implying another +25bps hike before end-2026. Rates are then expected to remain broadly unchanged through 2027 before gradually declining from 2028 onwards as inflation moves closer to target. Nevertheless, Chair Warsh stressed that future decisions will remain dependent on incoming economic and inflation data rather than follow a predetermined policy path.

Higher yields reflect stronger economy, capital demand and geopolitical risk

In response to a question at the post-meeting press conference, Fed Chair Kevin Warsh attributed the recent rise in long-term Treasury yields to three broader forces rather than solely to expectations of tighter monetary policy. First, the strengthening US economy has supported higher real yields as investors price in firmer growth and a reduced need for accommodative financial conditions. Second, greater competition for capital, particularly from large-scale investment by technology and AI-related firms, has increased financing demand and may require higher yields to attract available savings. Third, heightened geopolitical risks have added a risk premium to longer-term bonds, particularly amid uncertainty surrounding energy markets, global trade and fiscal conditions. Taken together, these factors suggest that long-term yields could remain elevated even if expectations for the fed funds rate eventually stabilise.

Possible additional rate hike if inflation remains elevated

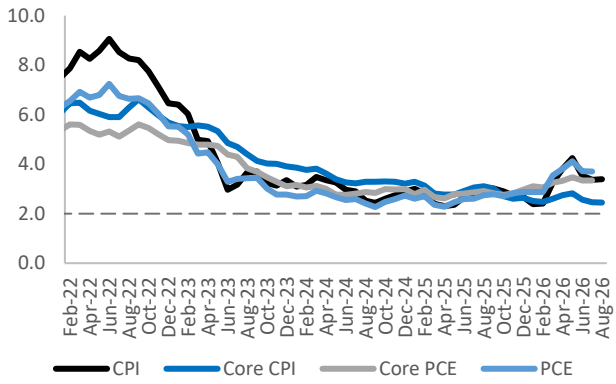
We foresee a relatively more hawkish Fed policy outlook, with scope for one additional rate hike later this year should inflationary pressures remain elevated. The latest FOMC projections reinforce this view, with the median policy-rate projection indicating another +25bps increase by end-2026. Based on the CME FedWatch, investors are pricing in around 50% probability for another rate hike at the upcoming FOMC meeting in Oct-26. Looking ahead, persistent supply disruptions, elevated energy prices and rising raw material costs could sustain inflationary pressures and warrant a tighter monetary policy stance. Conversely, a de-escalation of geopolitical tensions in the Middle East, particularly if accompanied by lower global oil prices, could ease energy-related cost pressures and reduce the need for further tightening.

Table 1: Central Bank Policy Rate for Selected Economies (%)

	Jan-26	Feb-26	Mar-26	Apr-26	May-26	Jun-26	Jul-26	Aug-26	Sep-26
Malaysia	2.75	2.75	2.75	2.75	2.75	2.75	2.75	2.75	2.75
Indonesia	4.75	4.75	4.75	4.75	5.25	5.75	5.75	5.75	5.75
Philippines	4.50	4.25	4.25	4.50	4.50	4.75	4.75	5.00	5.00
Thailand	1.25	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Vietnam	4.50	4.50	4.50	4.50	4.50	4.50	4.50	4.50	4.50
South Korea	2.50	2.50	2.50	2.50	2.50	2.50	2.75	3.00	3.00
India	5.25	5.25	5.25	5.25	5.25	5.25	5.25	5.25	5.25
Japan	0.75	0.75	0.75	0.75	0.75	1.00	1.00	1.00	1.00
UK	3.75	3.75	3.75	3.75	3.75	3.75	3.75	3.75	3.75
Euro area	2.15	2.15	2.15	2.15	2.15	2.40	2.40	2.40	2.65
USA	3.50-3.75	3.50-3.75	3.50-3.75	3.50-3.75	3.50-3.75	3.50-3.75	3.50-3.75	3.50-3.75	3.75-4.00

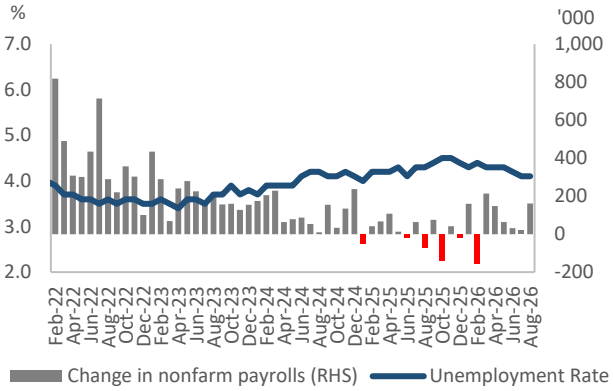
Source: Macrobond, MBSBR

Chart 1: US CPI vs Core PCE Inflation (YoY%)



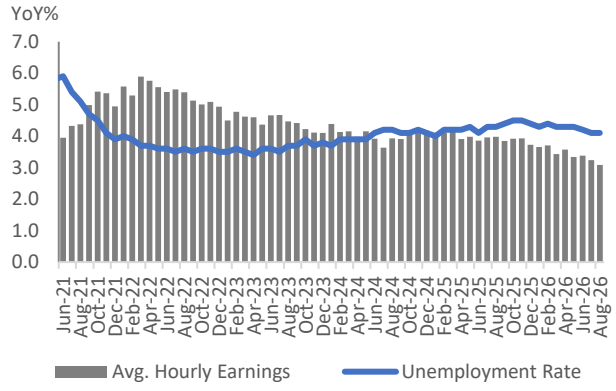
Source: Macrobond, MBSBR

Chart 2: US Unemployment Rate (%) vs Change in Non-Farm Payrolls ('000)



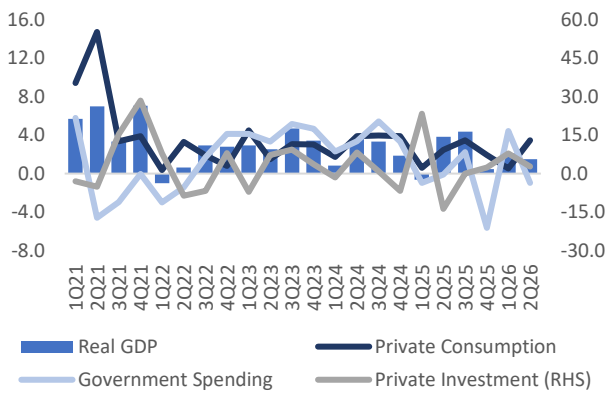
Source: Macrobond, MBSBR

Chart 3: Wage growth (YoY%) vs Unempl. Rate (%)



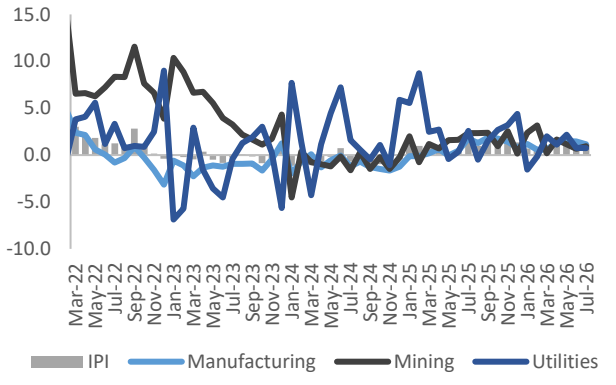
Source: Macrobond, MBSBR

Chart 4: US GDP Growth (Annualised QoQ%)



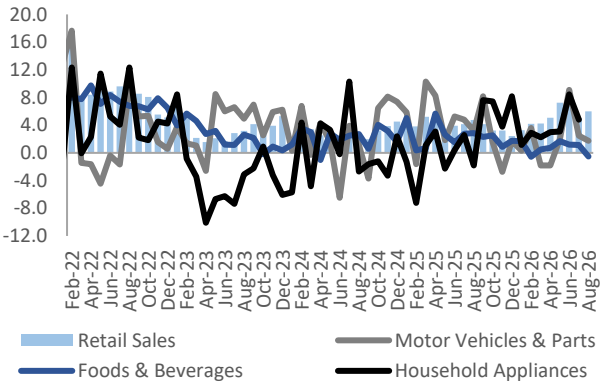
Source: Macrobond, MBSBR

Chart 5: US IPI Performances (YoY%)



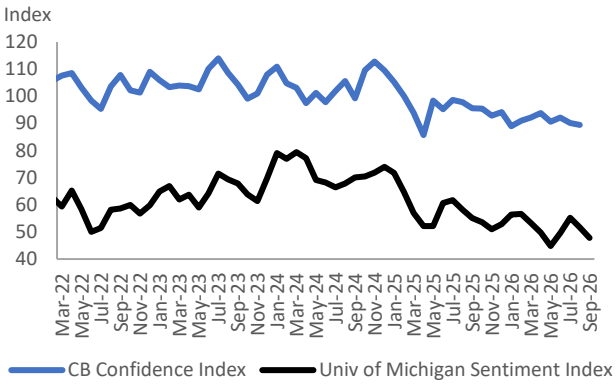
Source: DOSM, MBSBR

Chart 6: US Retail Sales (YoY%)



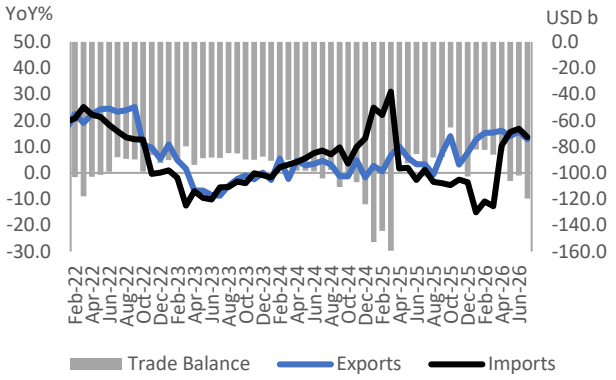
Source: DOSM, MBSBR

Chart 7: US Consumer Sentiment and Confidence (Index)



Source: Macrobond, MBSBR

Chart 8: US External Trade Performance (YoY%)



Source: Macrobond, MBSBR

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