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Economic Research

Economic Briefing

Fed raises rates

16 September 2026

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In a unanimous decision today, the Fed raised key interest rates by 25 basis points to accelerate progress toward its inflation target. The main factor behind the rate hike was likely the tight conditions in the bond market, which would likely have made maintaining the status quo too risky. We are adjusting our Fed forecast and expect another rate hike in December.

Fed delivers the expected rate hike ...

The Fed raised its key interest rates by 25 basis points today. The fed funds target range was thus raised to 3.75%–4.00%. Today's "policy action will support a timelier return to the Committee's 2 percent goal", according to the Fed's **statement**. The Federal Reserve thus met the expectations—which would be better described as demands—of market participants. The Fed sent a clear signal today that its promise to reach the inflation target is not just talk, but is backed by action. The decision was unanimous, which also sends a strong signal.

... and the dot plot hints at another hike

Following the meeting, the Fed members' updated projections were also released. Once again, Fed Chairman Warsh did not provide his own projection of the policy rate path, meaning the dot plot is once again missing his dot. Sixteen of the remaining 19 meeting participants anticipate at least one more rate hike this year, with two meetings still to come. However, a rate hike at the October meeting is unlikely, as it takes place just a few days before the midterm congressional elections. Therefore, a hike in December is more likely.

Warsh delivers a clear message

Kevin Warsh made it very clear in the post-meeting press conference that price stability is currently the Fed's primary focus. Today's decision is based on the assessment that the U.S. economy has regained strength in recent months (the Atlanta Fed's tracker currently shows GDP growth of over 5% for the third quarter, a significant acceleration compared to the growth rates in the first half of the year). Second, it would depend on inflation trends. And he sees no evidence that these have improved. Finally, the geopolitical situation is having an impact. Warsh's clear focus and the unanimous decision send a strong signal that the Fed is serious about fighting inflation.

Ultimately, the Fed had little choice but to raise key interest rates today. Had Warsh disappointed expectations in this situation and failed to raise rates, there would have been a risk of a severe negative reaction in the bond market. After all, doubts would then have solidified as to whether the Fed would actually do what is necessary to bring inflation back down to the 2% target. President Trump is unlikely to welcome the rate hike. However, there have been signals from the administration that it will accept the decision.

We are revising our Fed forecast

This single step will likely not be enough. After all, Warsh acknowledged that monetary policy was merely made slightly less accommodative today. We therefore expect another rate hike at the December meeting. We have pushed back the first rate cut to the fourth quarter of 2027. The policy rate path we now expect is thus 100 basis points higher at the end of 2027 than in our previous forecast (table).

Table 1 - Fed's rate path pushed up
Upper bound of fed funds target range in %, end of quarter, forecast changes in bold

	2026				2027			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
new forecast	3.75	3.75	**4.00**	**4.25**	**4.25**	**4.25**	**4.25**	**4.00**
previous forecast	3.75	3.75	3.75	3.75	3.75	3.50	3.25	3.00

Source: Fed, Commerzbank Research

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This report was completed 16/9/2026 21:41 CEST and disseminated 16/9/2026 21:41 CEST.

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