

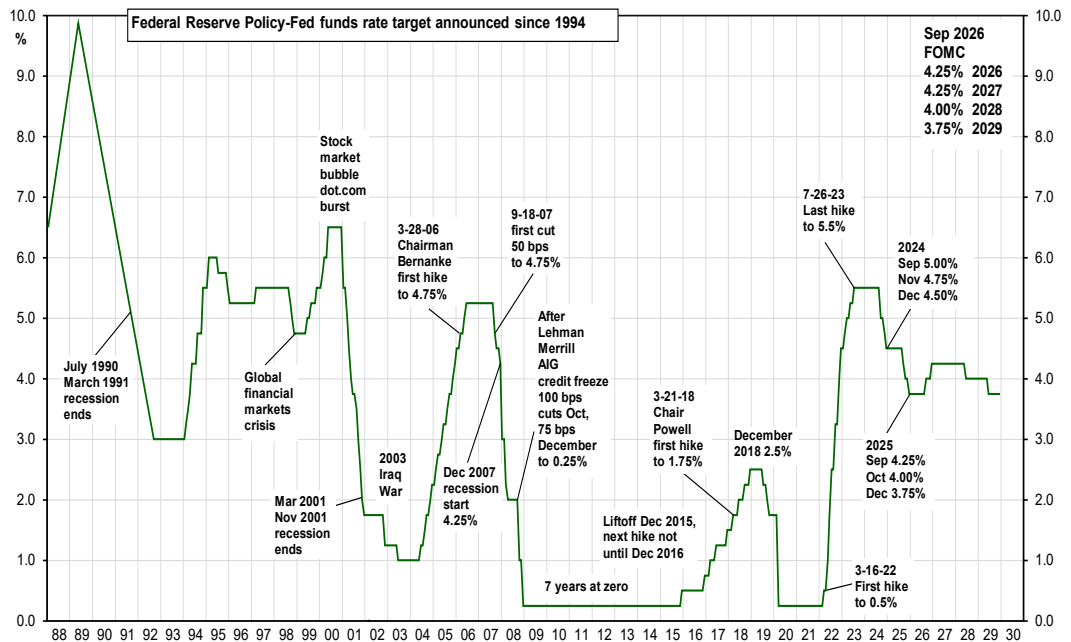
Financial Markets This Week

18 SEPTEMBER 2026

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2 FED HIKES 2026

Two Fed hikes in 2026. We think. The biggest surprise at Wednesday's Fed meeting was the nearly unanimous, 16 out of 18 votes for a 4.25% Fed funds rate at the end of the year (minus Warsh not-voting). Two rate hikes in 2026 not just one and done. It is a good thing the dot plot interest rate forecasts were still here

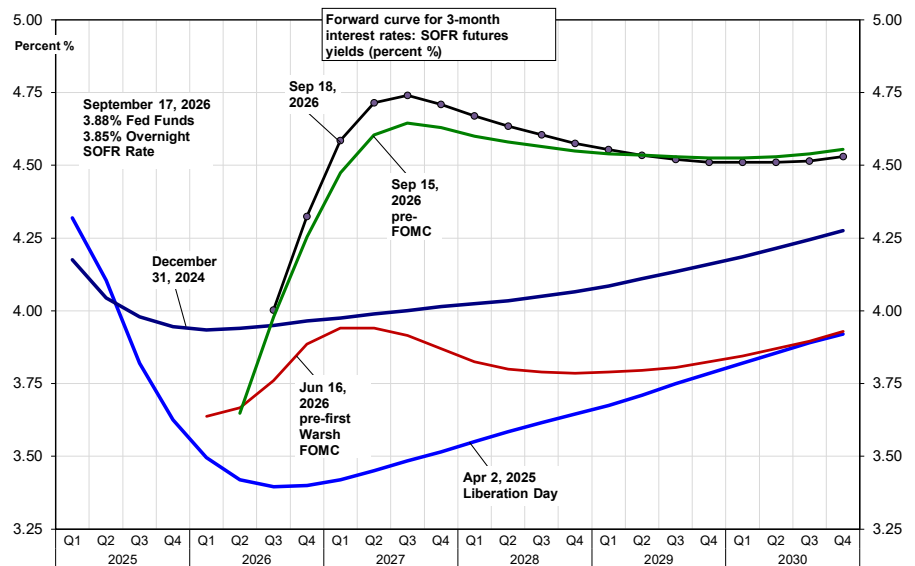


to let us know. We thought Warsh wanted to get rid of them to tell you the truth, and maybe he still does and is just waiting for his communications task force (two old former central bankers among his old G30 friends, and the guy who eliminated the long bond after 9/11) to recommend the elimination of the "Dot Plot" to the FOMC. So two rate hikes this year were unexpected FOMC meeting news, but the rates forecast does not look like much in the grand scheme of things. 50 bps removal of accommodation perhaps this year, keep rates at 4.25% next year, then drop rates slowly back to square one with 25 bps in 2028 and another lone 25 bps rate cut in 2029 back to 3.75%. It is not really explained or explainable how a 4.25% Fed funds rate is going to return inflation to the 2.0% target faster than 3.75% would. Maybe it need not be explained given the inflation illusion posed by the strange situation where core CPI inflation year-over-year is at 2.4% in August and the official Fed target of core PCE inflation is at 3.3% year-year, and could be 2.9% on September 30 for all we know. Inflation illusion is a measurement problem for policymakers and economists even though the public sees no such illusion as prices continue to move up in their real-world shopping experience. The Fed forecasts themselves, one myopic participant did not give a rates forecast way out in 2028-29, peak at 4.25% this year and all through 2027. The Powell inflation battle Fed rate peak was 5.5%

Fed Individual Forecasts					
Fed funds rate at year-end					Longer
Votes	2026 End	2027 End	2028 End	2029 End	run
1	3.875	3.125	3.125	2.875	2.875
2	3.875	3.625	3.125	3.125	3.000
3	4.125	3.625	3.125	3.125	3.000
4	4.125	3.625	3.125	3.125	3.000
5	4.125	4.125	3.375	3.125	3.000
6	4.125	4.125	3.625	3.375	3.000
7	4.125	4.125	3.625	3.375	3.000
8	4.125	4.125	3.625	3.625	3.125
9	4.125	4.125	3.875	3.625	3.250
10	4.125	4.125	3.875	3.625	3.250
11	4.125	4.375	3.875	3.625	3.375
12	4.125	4.375	3.875	3.625	3.500
13	4.125	4.375	3.875	3.625	3.500
14	4.125	4.375	4.125	3.625	3.625
15	4.375	4.375	4.125	3.875	3.625
16	4.375	4.375	4.125	3.875	3.750
17	4.375	4.375	4.125	3.875	3.875
18	4.375	4.375			3.875
19					
Median	4.125	4.125	3.875	3.625	3.250
Meeting	Sep 26	Sep 26	Sep 26	Sep 26	Sep 26

in July 2023. The FOMC neutral rate forecast is up to 3.25% now from 3.063% in June. Again, neutral was 4.25% in the first Fed rate forecasts ever made at the start of 2012. Eliminating this information for markets would be a mistake, however flawed, thinking about the press conference where Warsh implied a 25 bps hike to 4.0% was taking away some accommodation, which means what, that the neutral rate is much higher than the 3.25% forecast? Warsh did not answer as he thinks the neutral rate is interesting and there can be a discussion to help them think about policy but it has no “operational effect on decisions we make.”

The press conference keeps shrinking, and Wednesday’s was about thirty minutes. The transcript was 15 pages, where Powell’s December 2025 press conference with a rate change was 27 pages. The stock market did seem to sink as Warsh began speaking at 230pm ET. Warsh did answer why a rate hike today and not at the July 27-28 meeting, assuming this reflected his thinking and not just an off-the-cuff response as he is a good talker. One thing that changed was that a wide-ranging set of data including the labor markets say the economy has strengthened. Second was the inflation trend this summer was not going the right way, and little information since then has led him to believe otherwise. The third thing was the geopolitical situation as changed, and all three things led to the unanimous decision to hike rates today. Okay.

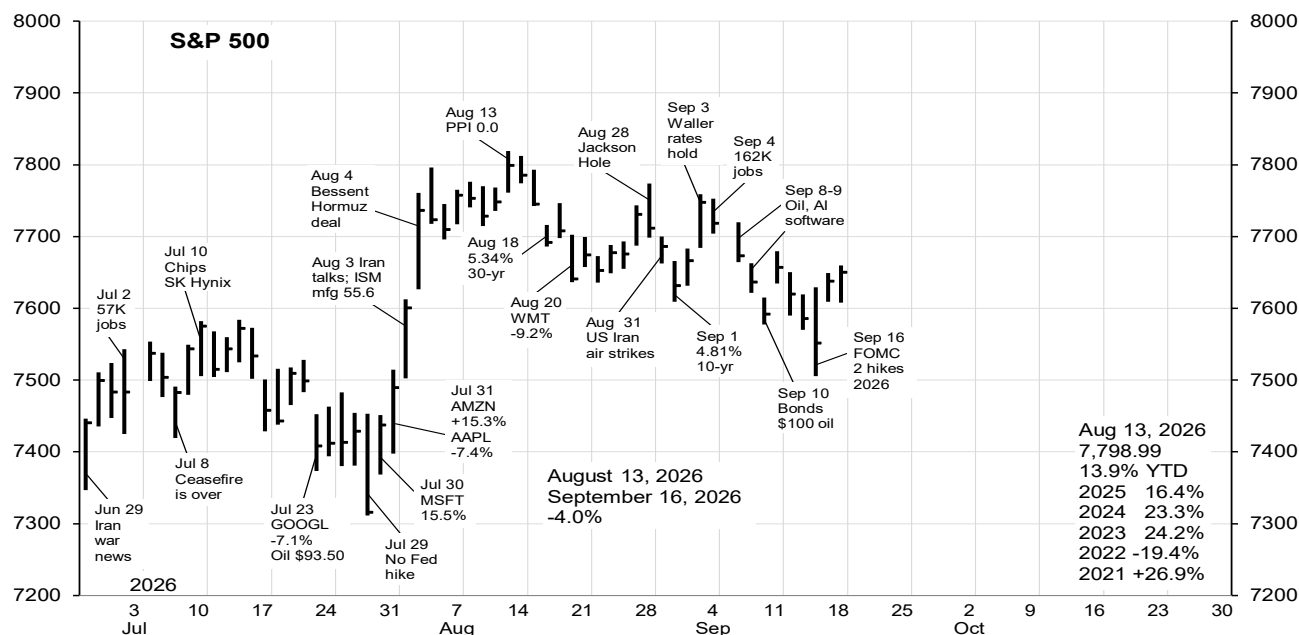


Review and Outlook: Two rate hikes this year, one is done, but it is unsettling that Warsh won’t talk about this future path of interest rates based on some sort of long-held principle. This suggests he needs some new data between now and the future that shows inflation is not returning to target as quickly as he would like. There is an interplay between himself as Chairman and the rest of the Committee as well to consider, the other participants that come down to Washington to make policy, have a voice and a vote on where to set interest rates. It is nice to have the dots forecasts, but we still wonder if the days for these are numbered, and essentially investors will have to go from meeting to meeting and guess if the economic situation has changed enough for the Fed to hike rates again. Doesn’t sound like a way to run a business. The night before the Fed meeting, October Fed funds futures closed at an adjusted yield of 3.995%, the rate hike 98% discounted. This will have to be the guiding light for Fed watchers for now. If futures say green light, then the Committee moves or at least is reluctant to disappoint. The odds are slightly over 50% that the Fed hikes rates on the next October 28 decision date.

Fed Policy-key variables					Long Term
	2026	2027	2028	2029	
Fed funds	4.1	4.1	3.9	3.6	3.2
PCE inflation	3.7	2.3	2.1	2.0	2.0
Core inflation	3.4	2.5	2.2	2.0	
Unemployed	4.1	4.1	4.1	4.1	4.2
GDP	2.3	2.4	2.2	2.1	2.0
September 2026 median Fed forecasts					

Fed funds futures call Fed policy	
Current target: Sep 18 -- 4.00%	
Rate+0.12 Contract	Fed decision dates
4.140 Nov 2026	Oct 28
4.345 Jan 2027	Adds Dec 9*
4.440 Feb 2027	Adds Jan 27
4.610 Apr 2027	Adds Mar 17*
*Jan 2027 could be 4 days at a new rate	
*Apr 2027 could be 2 days at a new rate	

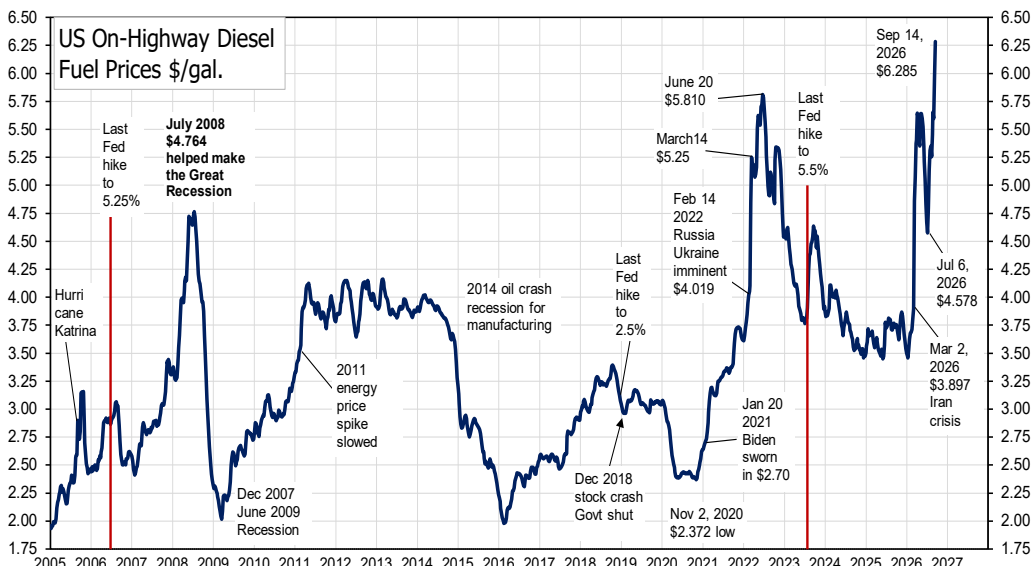
INTEREST RATES



Crude oil drives bonds, higher oil prices, then higher bond yields, higher bond yields mean a lower stock market. [AAA gasoline prices](#) are 17 cents higher this week at \$4.46. [Diesel at \\$6.44](#) is at a record and nearly 50 cents higher for the Friday week. The Fed raised rates to fight inflation as it says economic growth is solid for now. We used to think higher energy prices could lead to a recession at least before the 2022 energy shock came and went. Crude oil on Friday was still supportive of a 5% 10-yr yield. The more time that yields stay at this benchmark psychological level, the greater the risk it pushes higher to 5.25%. 10-yr yields did close at 5.02% on Wednesday Fed Day, but this did not lead to hedge sales by mortgage-backed securities portfolios. We are interested in August core PCE inflation on September 30 due to new methodological changes bringing it down from 3.3% in July.

Diesel prices set records and threaten the Fed's solid economic activity

The [Fed meeting press statement](#) said the economy was expanding at a solid pace, and that domestic spending has been resilient despite the uncertainty from geopolitical developments. For how long is the question, as many companies are experiencing life-threatening, higher costs from spiraling diesel fuel prices. The historical graph here is the Energy Information Agency (EIA) U.S. No 2 Diesel Retail Prices for the week ending Monday, and AAA diesel prices are daily. Weekly Diesel prices came down briefly to \$4.578 on July 6 when the Iran War was over and now are setting records.



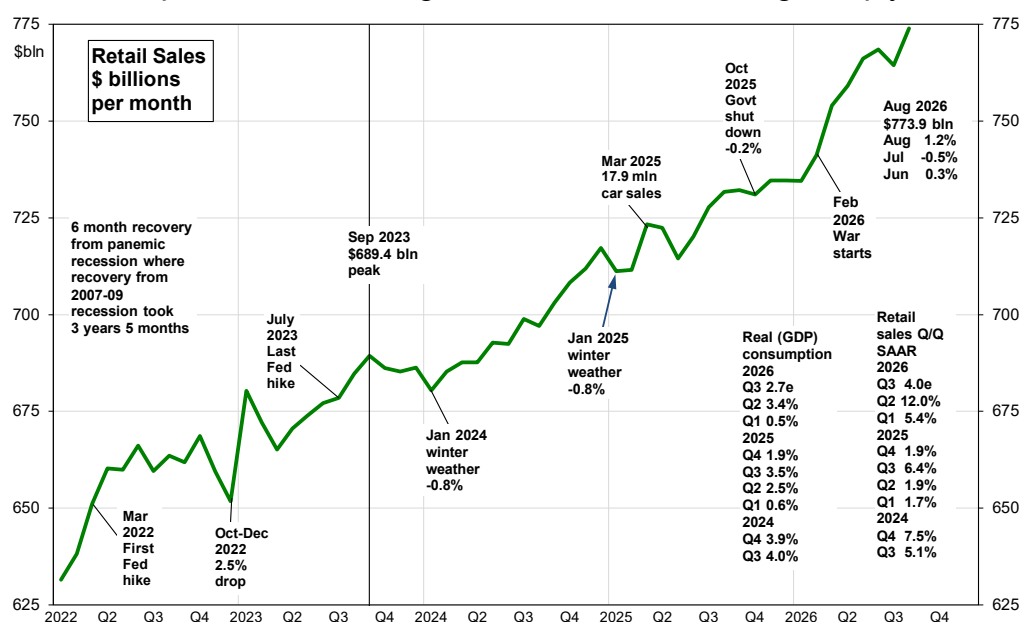
OTHER ECONOMIC NEWS

Retail sales are hot in August at least (Wednesday)

Breaking economy news. Retail sales bounced back from July's 0.5% decline, by climbing 1.2% in August. We are guessing a 4.0% retail sales increase for Q3 which means a 2.7% increase in real consumption expenditures. The Atlanta Fed GDPNow sees a higher 4.1% consumer spending figure which supports their latest 5.1% Q3 2026 real GDP forecast due on Thursday, October 29. For GDP growth it is the consumer and business investment in equipment leading the charge.

Net, net, Americans returned to the shops and malls in August with sales rebounding sharply from the downturn in July.

Consumer spending will be supportive of strong real GDP this quarter. Gasoline prices increased 3.1% with the return of the Iran war growth in the third quarter, but consumers had money to burn and retail sales minus gasoline stations rebounded 1.1% in August after falling 0.6% in July. Fed officials wanting to sit this meeting out will find nothing in the



retail sales report to support that hold-tight view as sales were strong in August. Services spending has been the standout as they are less affected by tariff costs as sales at restaurants and bars jumped 1.2% in August following on July's 0.5% gain. The cost of living crisis for Americans won't be seeing any relief from imported goods either as the nonfuel import prices jumped 0.8% in August. Stay tuned. The economy has not gone off the rails yet due to the uncertainty of the Middle East conflict and higher energy prices. The sun is shining on the economy in August, but September is likely to be a different story as energy prices have soared the last month taking a toll on consumer confidence. Two reports today call for a rate hike as do the financial markets.

Retail spending, actual dollars, each month

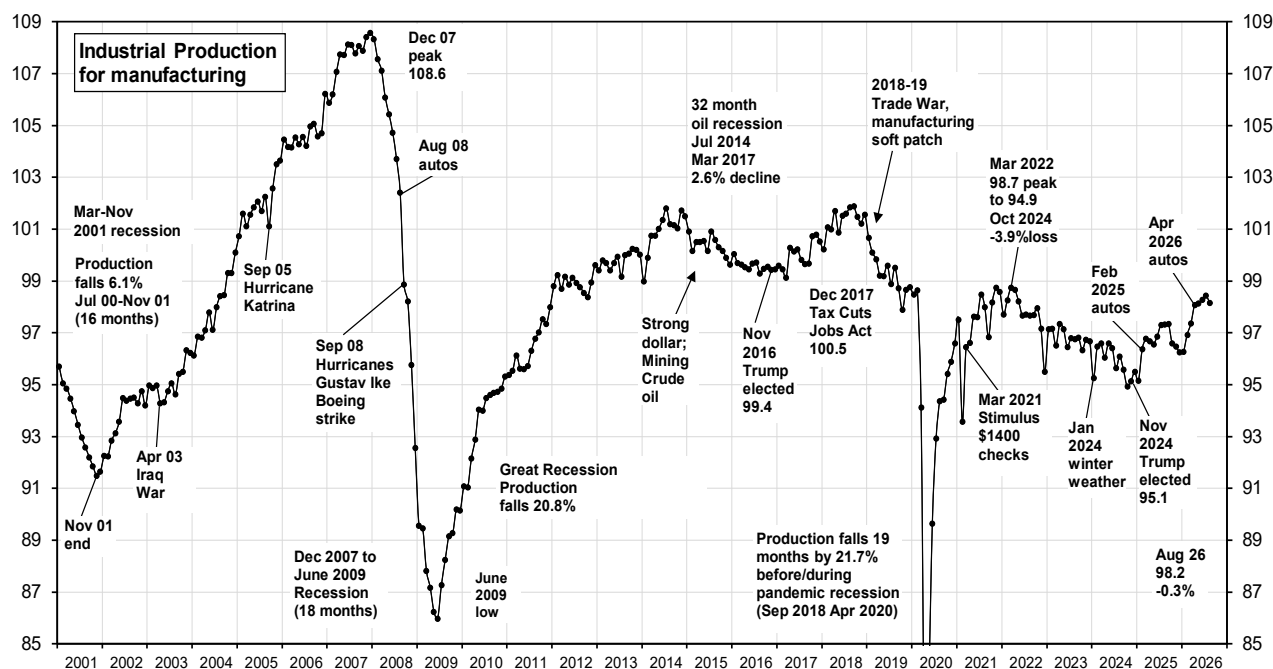
	\$million	% to	Percent Changes %		
	Aug	Total	Aug	Jul	Year/year
Total Retail Sales	773,947	100.0	1.2	-0.5	6.0
Motor vehicles/parts	142,379	18.4	0.6	-1.8	2.1
Furniture/furnishings	11,398	1.5	0.9	-0.2	1.9
Electronics/appliances	8,307	1.1	1.6	-0.1	7.8
Building materials/garden	42,227	5.5	-0.2	-0.1	5.1
Food & beverage	85,580	11.1	0.4	-0.2	0.5
Health/personal care	40,721	5.3	0.9	0.3	1.9
Gasoline stations	62,303	8.1	3.1	-0.2	21.0
Clothing/accessories	28,353	3.7	0.7	1.3	4.3
Sporting goods, books	9,061	1.2	1.2	0.2	10.7
General merchandise	80,388	10.4	0.7	0.5	4.5
Department stores	3,297	0.4	-0.8	0.0	1.9
Miscellaneous retailers	16,821	2.2	1.9	-0.6	14.0
Nonstore retailers (internet)	141,339	18.3	2.6	-1.7	9.9
Eating & drinking places	105,070	13.6	1.2	0.5	5.8
[Total ex-autos/gas]	564,437	72.9	1.2	-0.3	5.6

Industrial production flat (Friday)

Breaking economy news. Industrial production was flat in August and 1.4% higher than a year ago. Manufacturing industrial production fell 0.3% in August and is 0.9% higher than a year ago. The transit category was down in August, chiefly motor vehicles and parts production; it had added a lot to the index especially in April this year. Transit is part of business equipment, and business equipment has risen 7.1% from a year ago, and has a 9.3% weight in the overall industrial production index. For the August total index 1.4% year-year change, a big driver besides business equipment is energy production both for the consumer and especially industry.

Percent changes			Industrial Production	
Jun	Jul	Aug	Aug 2026	
0.2	0.2	0.0	YOY	Weight
0.1	0.2	-0.3	1.4 Total Index	100.0
0.4	0.1	0.1	0.9 Manufacturing	75.9
0.3	0.5	1.8	0.3 Mining	11.7
			6.2 Utilities	12.4
			Manufacturing payroll jobs	
			12.6 million +23K YOY	
			9.3% of Private Payroll Jobs	

Net, net, factory production fell back in August as manufacturing output retreated even if industrial production overall managed to be unchanged due to the warmer than seasonal summer temps that pushed up utility output. Fed Chairman Warsh said this week the economy was solid and the greater threat was from inflation, but factory output shows the first signs of a slowdown which could worsen if the geopolitical headwinds intensify and diesel fuel prices do not come back down. Soaring energy prices are costly for industry and higher diesel prices may start to chip away at the manufacturing renaissance picture painted by White House economic officials. Manufacturing output is up 0.9% in August from a year ago which counts as just a modest increase for factories and the result was less than anticipated by economists. Stay tuned. Import tariffs have not brought as many factories back to the US as the administration had expected yet.



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