FOMC Hikes as Expected, as Dot Plot Points to Additional Rate Hikes

Headlines

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- **The FOMC, as widely expected, increased the fed funds rate by 25 basis points.**
- **The FOMC statement bluntly said that "the Committee will deliver price stability."**
- **The median dot points to one more rate hike this year, followed by no change in rates in 2027. PNC expects one additional hike in early 2027, leaving its forecast slightly above the median dot.**

Details

As widely expected, the Federal Open Market Committee raised the federal funds rate this afternoon by 25 basis points, to a range of 3.75% to 4.00%. After cutting the fed funds rate in fits and starts from late 2024 to late 2025, and then holding it steady throughout 2026, this was the first rate hike since mid-2023. The vote was unanimous.

In their post-meeting statement, the FOMC cited inflation that is above the Committee's 2% objective as the reason for the rate hike: "Inflation remains elevated. Today's policy action will support a timelier return to the Committee's 2% goal. The Committee will deliver price stability."

The statement also said that the economy is expanding "at a solid pace," although it also noted elevated uncertainty due to geopolitical factors. The statement cited resilient domestic spending, strong productivity growth, and robust business investment. The statement also noted job growth consistent with an expanding labor force and a little-changed unemployment rate.

This release also included the Summary of Economic Projections, or "dot plot," that shows FOMC participants' projections for the economy and the fed funds rate over the next few years. New Fed Chair Warsh has declined to provide his projections for the dot plot.

The dot plot released today shows that most participants (12 of 18) expect one more 25 basis point fed funds rate increase this year, with the rate in a range between 4.00% and 4.25% by the end of 2026. The median participant has the rate in that same range at the end of 2027, with small rate cuts projected for 2028 and 2029. The median value for the long-range fed funds rate is 3.2%, up from 3.1% from the last dot plot in June.

The median projection for GDP growth (Q4 to Q4 basis) is 2.3% in 2026 and 2.4% in 2027, both up slightly from the last dot plot. The unemployment rate is expected to remain at its current 4.1% level over the next few years, marked down slightly from June as the unemployment rate has declined since the spring.

Participants expect PCE inflation, both overall and core, to gradually ease over the next few years but not return to the 2% objective until 2029. Inflation projections are slightly higher in the current dot plot compared to the previous one, reflecting a pickup in inflation in recent months.

With inflation above the central bank's objective since early 2021 and moving higher over the past year, the Federal Open Market Committee needed to reassure the public and financial markets that it is committed to pushing it back to 2%. Today's rate hike was the first concrete step in that process, but it will likely take further rate hikes to push inflation lower and convince markets of the Fed's resolve. Most notable in today's statement was the blunt declaration that "the Committee will deliver price stability." Warsh reiterated the FOMC's commitment to 2% inflation in his post-meeting press conference.

PNC's fed funds rate forecast is consistent with the median dot through the end of 2026 but is somewhat more hawkish for 2027. PNC expects no change at the FOMC's next meeting on October 28, a week before the midterm elections, but a 25 basis point increase at the year's final meeting in mid-December. PNC also expects an additional rate hike in the early spring of 2027, which would take the rate to a range of 4.25% to 4.50%. In contrast, the median dot shows the target range remaining at 4.00% to 4.25% through the end of 2027.

Risks to the outlook are balanced. The FOMC expects inflation to ease gradually over the next few years. If inflation remains sticky, however, the FOMC could hike more aggressively, with a faster pace of hikes and/or more rate increases. Alternatively, if high gasoline prices lead to a slowing in economic growth and a deteriorating labor market, the FOMC could decide to hold off on additional monetary tightening, even if inflation temporarily accelerates.

The overall financial market reaction suggests that today's statement and dot plot were slightly more hawkish than expected. The S&P 500 is down slightly following the FOMC's announcement, with yields up slightly on longer-term Treasurys. The dollar strengthened against a basket of currencies and the price of gold fell. The price of a barrel of West Texas Intermediate crude oil is down by about 3% today to slightly below $103.

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