SITUATION ANALYSIS

October 28, 2026

Fed holds rates steady after hiking last meeting, with investors expecting more increases to come

Key takeaways

- The U.S. Federal Reserve (Fed) held its policy interest rate in a range of 3.75%-4.00% after hiking rates in September for the first time in three years.
- Two members dissented in favor of a hike, while new Fed Chair Kevin Warsh reiterated his commitment to return inflation to the Fed's 2% target.
- Market prices reflect expectations for another rate hike in December and two more next year amid lingering inflation.

The Federal Reserve held its target federal funds interest rate in a range of 3.75%-4.00% at its October meeting, in line with investor expectations. The decision followed a rate hike at the Fed's last meeting in September, the first in three years as a response to above-target inflation. Two voting members dissented, favoring a rate increase. Rising energy costs and lingering inflation this year drove rate hike expectations higher, in turn pushing both short- and long-term bond yields up. Investors anticipate three additional rate hikes in the next 12 months, including an expected hike in December 2026.

Kevin Warsh has taken a strong stance against inflation in his comments since assuming the chairmanship role at the Fed earlier this year. He has noted the Fed's 2% inflation target as foundational to Fed credibility and expressed skepticism of forward guidance due to risks it can anchor policymakers' decisions despite changes in data. He also established task forces to reevaluate Fed conduct relating to data, communication and balance sheet policy.

Warsh reiterated these themes during his press conference on October 28, particularly the importance of returning inflation to 2%. The Fed's official policy statement remained concise and largely unchanged since the last meeting but upgraded the assessment of economic activity from "solid" to "strong" and emphasized the importance of accumulating more information for future decisions. Warsh reasoned that the recent rate hike's economic impact, combined with upcoming data, justified a pause in rate increases, leaving the option available to raise rates again later this year. The Fed plans to provide an updated Summary of Economic Projections at its next meeting in December. Warsh also noted that next year, one of the Fed's eight scheduled meetings will emphasize discussions of broader strategic policy issues without holding a vote on policy rates.

Fed interest rate increases from 2022 to 2023 helped mitigate post-COVID inflation pressure, but higher oil costs in 2026 contributed to elevated near-term prices. The Fed's preferred inflation measure, the Personal Consumption Expenditures (PCE) Price Index, accelerated from as low as 2.7% year-over-year in January to as high as 3.8% in May, with August moderating to 3.4%. The Fed also closely watches Core PCE, which strips out more volatile food and energy prices. This measure has fluctuated less this year, with the most recent reading indicating 3.0% year-over-year gains. West Texas Intermediate crude oil front-month futures prices rose from nearly $57 per barrel at the beginning of the year to a peak of $113 in April. Prices currently stand above $100. Higher energy prices have acted as the primary driver of rising rate hike expectations, in turn driving Treasury bond yields higher. Longer-term inflation expectations remain well anchored, with investors anticipating that rate hikes will eventually bring inflation under control.

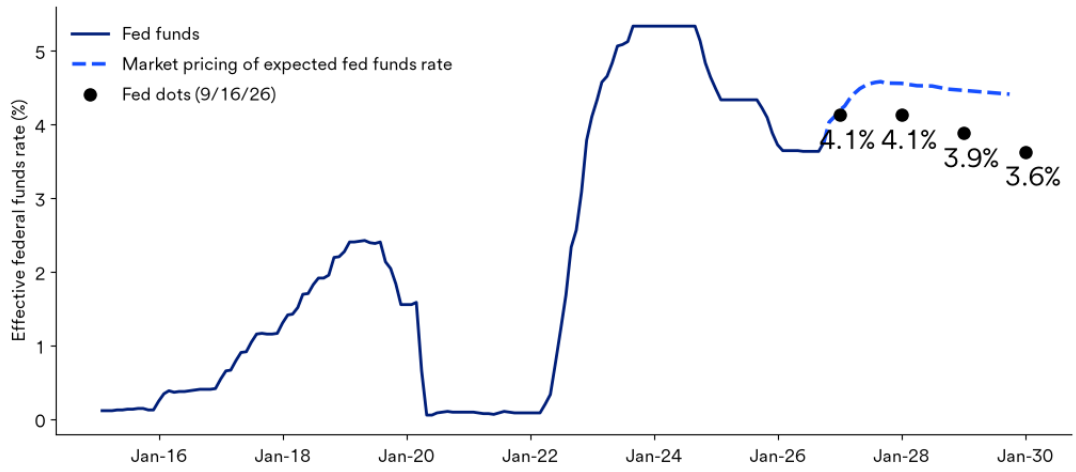
Federal Reserve balance sheet and market liquidity

The Fed stopped shrinking its bond holdings and began buying short-term Treasury bills in December 2025 to ensure ample banking system reserves and to keep short-term interest rates near its policy rate. The Fed's bond holdings of $6.6 trillion today peaked near $9 trillion in 2022. The Fed reduced its regular purchases this year, and holdings have grown at a modest

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pace since Warsh became chair. Expanding the balance sheet by purchasing Treasury bills can result in improved market liquidity by absorbing a portion of incremental supply. Liquidity, the money readily available to purchase goods, services and financial assets, can also cushion markets against unforeseen financial market shocks, and liquidity measures remain constructive. Warsh has expressed reservations about its long-run efficacy and questioned its appropriateness as a policy tool, forming a task force to explore the topic.

Market pricing of the expected path of the federal funds rate

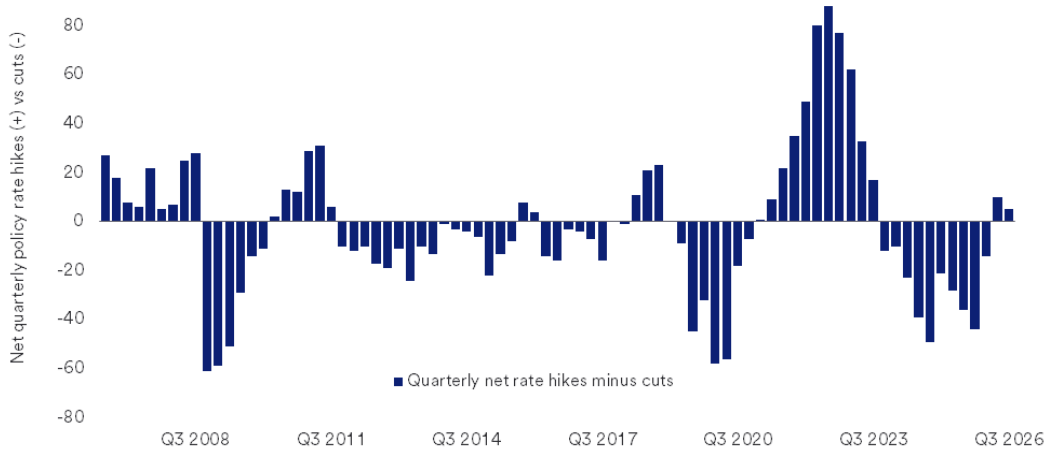


Sources: U.S. Bank Asset Management Group Research, Federal Reserve, Bloomberg, 1/1/2015-10/28/2026.

Two-year Treasury yields fell 0.04% to 4.70% today, while 10-year yields rose 0.03% to 5.02% versus the prior day's close. Large stocks, represented by the S&P 500, and small stocks, represented by the Russell 2000, rose 0.3% and 0.4%, respectively.

Central banks across the globe eased policy in 2024 and 2025 but many began increasing rates this year in response to rising energy prices. The European Central Bank, Bank of Japan and Bank of Canada increased rates in 2026 with more expected, while investors also anticipate a hike from the Bank of England this year.

Global net central bank rate hikes (net hikes minus cuts), quarterly



Sources: U.S. Bank Asset Management Group Research, FactSet, 4/1/2006-10/28/2026.

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