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Economic Situation and Strategy

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Where are Interest Rates Headed? Part I: The Fed's decision

Yesterday, the US Federal Reserve raised its policy rates by 25 basis points to a target range of 3.75% to 4.00%. Although market data had suggested that this move was almost 100% certain, the reality behind the scenes may have been somewhat different. From our perspective, it was not entirely out of the question that, under the leadership of Kevin Warsh, the Fed might have decided against raising rates, especially given the enormous pressure coming from the White House. At the same time, some capital markets experts were quietly expecting a surprise in the opposite direction: a 50-basis-point increase, combined with a signal that rates would not be raised again for the foreseeable future.

Instead, the Fed chose not only the path of least resistance, but also the economically wiser course. Given the current economic data, it is difficult to justify leaving interest rates unchanged. A 50-basis-point increase, however, would have caused considerable concern in the markets. It is also worth noting that the decision was unanimous. This has no longer been a given at the Fed. Against the backdrop of strong labor market data, a PCE inflation rate of 3.7%, and the Fed's expectation that this figure will not fall below 2% even in 2028, the decision is easy to justify from a monetary-policy perspective. The fact that 16 of the 18 Fed members expect another rate increase by the end of the year also fits the overall picture and is unlikely to have surprised anyone. After all, the war involving Iran shows no sign of easing. On the contrary: the destruction of a pipeline by Houthi rebels and their control of the Bab al-Mandab Strait, known as the "Gate of Tears", are making the situation even more difficult, particularly as global crude oil inventories have fallen significantly.

Trump is Both a Burden and a Relief for the Fed

At the same time, Donald Trump had created an almost unprecedented level of pressure ahead of the rate decision. On social media, the US president argued that interest rates in the United States should be set at 1%, since the country's creditworthiness supposedly justified such a level. He called on the Fed to cut interest rates sharply. In the same breath, he threatened to halt trade with countries with which the United States runs a trade deficit.

This naturally raised concerns that such pressure from the US president could undermine the independence of the Federal Reserve. However, the opposite may have happened. Trump's statements have become so surreal that even normally loyal allies can only shake their heads. In such an environment, it becomes much easier for the Fed to distance itself from the president's demands, since they are expressed without any real intellectual authority. Anyone who openly follows such demands risks making themselves look ridiculous. Trump may therefore be achieving the exact opposite of what he intends. Put simply: every additional bizarre demand from Trump makes it a little easier for the Fed to defend its independence. We can therefore assume that, in line with the projections in the dot plot, the Fed will raise interest rates once more by the end of the year.

What happens afterwards will be much more difficult to predict. The current inflation rates are largely driven by high energy prices. So far, second-round effects have remained limited. Yet higher interest rates cannot directly reduce energy prices. The rate increase delivered yesterday, as well as the increase likely to follow at the end of the year, should therefore be viewed primarily as precautionary measures. In anticipation of possible second-round effects, the Fed is administering the appropriate medicine in advance. This is somewhat like taking antibiotics before going to Oktoberfest because experience suggests that one might later contract a bacterial infection. This form of monetary policy is well established, and its effects have been tested many times. The challenge for a central bank, however, is always to avoid overdosing the medicine. In the worst-case scenario, excessive tightening could weaken the economy or even derail a capital-market rally, without bringing about the desired reduction in inflation to its full extent.

Against The United States faces an additional problem. Two-year US Treasury bonds currently offer a yield of 4.7%, while five-year bonds yield 4.8%. The ten-year Treasury, which often serves as a benchmark for the capital markets, offers a yield of just under 5%. In fact, there are not many countries in the world that offer an even higher yield while also providing acceptable credit quality and liquidity. In other words, financial conditions are already highly restrictive. From today's perspective, there is therefore no compelling reason for the Fed to continue raising interest rates aggressively next year.

In our view, there is much to suggest that, after one further rate hike, the Fed will enter an extended pause. During this phase, it will carefully monitor whether higher energy prices are feeding through into wages, services and inflation expectations. If second-round effects remain limited, the rate-hiking cycle could reach its peak quite soon. If price pressures become entrenched, however, the Fed would have to tighten policy further despite the risks to economic growth. The decisive factor will be less the development of headline inflation, which is heavily influenced by energy prices in the short term, than the dynamics of core inflation. Monthly labor-market reports are also likely to become increasingly important. As long as employment and wages continue to grow strongly, the Fed will have the necessary room to maintain its restrictive monetary policy. If, by contrast, clear signs of weakness begin to emerge in the labor market, the willingness to raise rates further will quickly diminish.

The Impact on Bonds and Equities

For the US bond market, this means that investors should not expect yields at the short end of the curve to fall. They are unlikely to start pricing in rate cuts until either inflation declines much more sharply than expected or the economy clearly loses momentum. At the long end of the curve, inflation is only one of the relevant factors. Expansionary fiscal policy and the government's persistently high funding requirements also play a decisive role. The combination of large budget deficits and a correspondingly high supply of newly issued government bonds limits the potential for long-term yields to decline.

For the equity market, this is not an ideal starting point when viewed in isolation. Higher bond yields increase the discount rate applied to future corporate earnings and, at the same time, create a more attractive investment alternative. However, it should not be overlooked that high interest rates do not necessarily lead to falling equity prices. The resilience of the US stock market so far can also be interpreted as a sign of underlying strength. As long as the US economy remains robust and corporate earnings continue to grow, the current capital-market rally does not necessarily have to come to an end. The key question is whether the Fed can accomplish the difficult task of engineering a soft landing: inflation must decline without seriously damaging the labor market or the wider economy.

The longer energy prices remain high, however, the narrower the monetary-policy tightrope becomes. Our base-case scenario is therefore as follows: one more rate hike, followed by an extended pause, with the Fed paying less attention to calls from the White House and more attention to incoming economic and inflation data. This may not be spectacular, and it is certainly not politically convenient. But that is probably precisely why it is the right monetary policy.

Dr. Christian Jasperneite

Market data

Stock markets (in local currency)	As of 18.09.2026 11:55	Change versus 11.09.2026 -1 week	17.08.2026 -1 month	17.06.2026 -3 months	17.09.2025 -1 year	31.12.2025 YTD
S&P 500	7717	0,8%	-0,4%	4,0%	16,9%	12,7%
Nasdaq	26418	0,3%	-0,9%	1,5%	18,7%	13,7%
DAX	25571	0,0%	-2,9%	2,6%	9,5%	4,4%
MDAX	31479	-0,6%	-2,7%	-4,2%	4,2%	2,8%
TecDAX	3990	0,2%	-2,5%	1,1%	11,6%	10,2%
EuroStoxx 50	6288	-0,6%	-3,7%	-0,2%	17,1%	8,6%
Stoxx 50	5340	0,1%	-2,9%	-0,3%	17,7%	8,6%
SMI (Swiss Market Index)	13921	1,1%	-2,7%	0,8%	16,0%	4,9%
Nikkei 225	65019	1,6%	-6,1%	-7,0%	45,2%	29,2%
Brasilien BOVESPA	185992	-0,6%	11,5%	10,4%	27,7%	15,4%
Indien BSE 30	74586	-0,3%	-4,0%	-3,3%	-9,8%	-12,5%
China CSI 300	4507	-0,1%	-4,9%	-8,6%	-1,0%	-2,6%
MSCI Welt	4922	-0,3%	-1,7%	2,4%	15,4%	11,1%
MSCI Emerging Markets	1688	-2,0%	-1,3%	-5,3%	25,2%	20,2%
Bond markets						
Bund-Future	120,80	32	-341	-583	-811	-677
Bobl-Future	112,12	-21	-178	-292	-582	-404
Schatz-Future	104,53	-12	-98	-132	-249	-227
3 Monats Euribor	2,63	-1	13	22	61	61
3M Euribor Future, Dec 2026	3,01	0	26	36	101	91
3 Monats $ Libor	4,12	5	25	29	10	45
10 year US Treasuries	4,96	-1	24	46	91	82
10 year Bunds	3,51	3	32	58	88	69
10 year JGB	2,98	3	8	40	139	94
10 year Swiss Government	0,54	-2	14	22	34	22
US Treas 10Y Performance	622,45	0,4%	-1,2%	-2,1%	-2,1%	-2,7%
Bund 10Y Performance	544,72	0,2%	-1,8%	-3,4%	-3,1%	-2,4%
REX Performance Index	450,94	-0,3%	-1,5%	-2,3%	-1,6%	-1,7%
IBOXX AA, €	4,15	-1	35	60	106	82
IBOXX BBB, €	4,44	1	44	68	104	87
Commodities						
MG Base Metal Index	586,25	0,8%	0,3%	1,4%	33,4%	13,6%
Crude oil Brent	103,58	-1,1%	14,0%	30,0%	52,3%	70,2%
Gold	4377,25	0,3%	-1,0%	0,7%	18,8%	1,2%
Silver	65,22	1,1%	-0,9%	-4,1%	56,5%	-8,5%
Aluminium	3321,53	1,4%	1,9%	-2,6%	23,7%	11,9%
Copper	14491,35	1,8%	-0,7%	5,3%	46,0%	16,4%
Iron ore	97,42	-0,6%	2,6%	-3,8%	-7,5%	-9,1%
Freight rates SPCI	3688	0,7%	9,9%	23,5%	163,8%	122,7%
Currencies						
EUR/ USD	1,1486	-0,9%	-0,9%	-0,9%	-3,0%	-2,2%
EUR/ GBP	0,8586	0,0%	0,4%	-0,8%	-1,0%	-1,7%
EUR/ JPY	181,38	1,6%	-1,7%	-2,4%	4,7%	-1,5%
EUR/ CHF	0,9467	0,2%	0,8%	3,0%	1,6%	1,6%
USD/ CNY	6,6976	-0,2%	-0,7%	-0,9%	-5,7%	-4,2%
USD/ JPY	155,98	1,6%	-2,2%	-2,9%	6,1%	-0,4%
USD/ GBP	0,75	1,2%	1,4%	0,2%	2,2%	0,6%

Source: LSEG Datastream

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