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Is the Fed About to Raise Rates?

MARKETS |

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A couple of months ago, the answer was no— but next week might tell a different story

For all the hubbub surrounding them, Fed meetings had become pretty predictable. Not any more. Next week's rate decision is "live," as they say. Back in May, traders in the futures market were acting as if the chance of a quarter point hike were close to zero. Peace had broken out in the Middle East, and oil prices were having their weakest quarter in years, easing inflationary pressure.

That implied probability has risen to about one-third. The outcome hasn't been so uncertain for years, and it's no accident. New Fed Chairman Kevin Warsh has abandoned his predecessors' hints, called "forward guidance," pledging to let the data talk instead.

Note

So the creeping suspicion that the Fed will hike for the first time in more than three years isn't crazy. At the June meeting, Warsh's first as chair, nine of 18 participants (only 12 of them vote) foresaw at least one hike this year, up from zero at the previous meeting.

Now, oil prices are up by a third just this month, reigniting inflation fears. And Warsh told Congress just 10 days ago that he'd have "no tolerance" for inflation, which has now been above the Fed's target for more than five years.

Even so, it's a good bet the Fed will stand pat for now.

The European Central Bank made a unanimous decision to lift rates last month, but the economic arguments for hiking in the face of commodity-driven inflation are weak. Central banks can't unblock the Strait of Hormuz or make more oil come out of the ground.

And, even though the Fed denies watching the S&P 500, it certainly seems to. Recent market turbulence, especially among the most interest-rate sensitive stocks, could nudge inflation "hawks" to hold fire.

Note

A decision to stand pat has been made easier by the bond market. It's effectively tapping the economic brakes all by itself. On Thursday, the 2-year Treasury yield touched its highest in more than a year. So did mortgage rates.

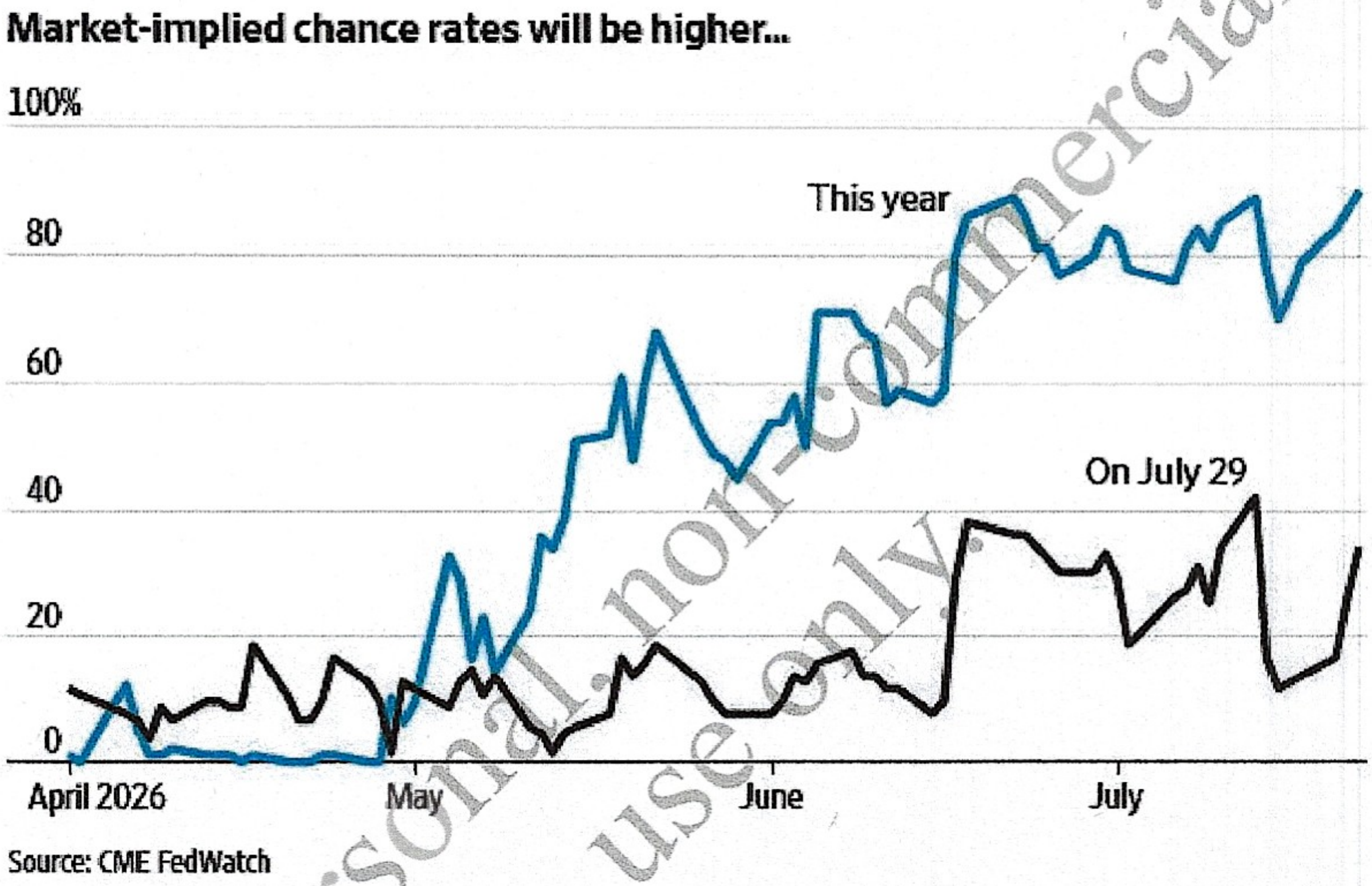
Then there's politics. Unprecedented pressure on former Chair Jerome Powell to lower rates, and President Trump's so-far unsuccessful efforts to fire him and Governor Lisa Cook, put Warsh in a tough spot to prove the Fed's independence.

He can't be fired either. But pushing for a rate hike three months before midterm elections would enrage the White House for little benefit.

Warsh's tough inflation talk has already established his bona fides.

Will he walk the walk later this year if job growth stays strong and price pressures worsen? On Thursday, the chance of any rate hike in 2026 rose above 90%. Count on Warsh to explain his thinking next week, but not to telegraph future decisions.

Investors need to get used to the strong, silent type.


Market-implied chance rates will be higher...
100%
80
60
40
20
0
This year
On July 29
April 2026
May
June
July
Source: CME FedWatch