



Higher Rates Test Stocks, But Growth Endures

9/21/2026

The Federal Reserve delivered the 25-basis-point increase the markets had largely anticipated, but the overall message was somewhat more hawkish than expected. The decision was unanimous, and the new dot plot points to another rate increase this year. Four participants apparently see the possibility of raising rates at each remaining meeting, so there is clearly a meaningful hawkish contingent on the FOMC. Chairman Warsh said relatively little at the press conference, but his message was clear: economic growth remains very strong, inflation has not made sufficient progress, and the Fed is prepared to lean against both.

The strength of the economy is increasingly difficult to ignore. The latest retail sales report was particularly strong, with the control group pushing third-quarter GDP estimates higher. The Fed raised its growth forecast and lowered its year-end unemployment projection to 4.1% from 4.3%. That combination of stronger growth and persistent inflation explains why Warsh was willing to tighten policy. Now the most interesting question is whether October or December brings the next increase. My expectation is December. Raising rates just before the midterm election invites unnecessary political controversy, and the Fed has no need to do that unless the data become considerably hotter.

The long end of the bond is even more important for equities than the fed funds rate. Stocks are long-duration assets, and the 10-year Treasury yield around 5% and the 10-year TIPS yield near 2.6%, provide real competition for equities. A 20-times earnings multiple represents roughly a 5% real earnings yield, leaving an equity premium of about 2.4 percentage points over TIPS. That premium is certainly narrower than investors became accustomed to when real bond yields were negative, but it is hardly unprecedented. Real yields exceeded 4% around 2000 when equity valuations were considerably more demanding than they are today.

If yields stabilize below 5%, equities can continue to grind higher. If long-term yields decisively move above 5%, it becomes much more difficult for stocks to advance, particularly after the strong gains we have already seen this year. I do not see a major upside catalyst for equities over the immediate term unless bond yields retreat or the geopolitical pressure on energy prices begins to ease.

Warsh attributed the rise in long-term yields primarily to strong economic growth, enormous AI-related investment and borrowing, and geopolitical inflation pressures. One notable omission was the federal budget deficit. Most economists discussing why the 10-year Treasury is near 5% would include the deficit and growing federal interest expense among the important factors pushing yields higher. Whether Warsh's omission was intentional or not, it was striking.

There is also an important distinction between the impact of higher rates on the broader economy and their impact on the AI boom. Roughly \$15 trillion of dollar-denominated loans are tied directly or indirectly to short-term rates. But I am less convinced that these rate hikes will materially derail AI infrastructure investment. In fact, AI itself is creating an unusual inflationary impulse. Memory and semiconductor prices are rising in areas where technological progress historically produced relentless price declines. Demand for computing power is simply overwhelming supply in parts of the technology complex.

The longer-term effect should be precisely the opposite. AI should eventually generate productivity gains that lower costs and increase real output. Yet we have not yet seen those gains clearly in the productivity statistics. This reminds me of Robert Solow's famous observation in the 1980s during the computer revolution that computers could be seen everywhere except in the productivity statistics. Shortly thereafter, productivity accelerated sharply.

Finally, I will be watching money and credit growth very closely. Deposit growth and money supply growth have been running hot, and Warsh has indicated that monetary aggregates matter to him. Higher short-term rates should reduce the willingness of households and businesses to borrow and eventually slow credit and money growth. That is one of the clearest tests of whether this tightening is working.

Please see the [WisdomTree Glossary](#) for definitions of terms and indexes.

Past performance is not indicative of future results. You cannot invest in an index.

Professor Jeremy Siegel is Senior Economist to WisdomTree. This material contains the current research and opinions of Professor Siegel, which are subject to change, and should not be considered or interpreted as a recommendation to participate in any particular trading strategy, or deemed to be an offer or sale of any investment product and it should not be relied on as such. The user of this information assumes the entire risk of any use made of the information provided herein. Unless expressly stated otherwise the opinions, interpretations or findings expressed herein do not necessarily represent the views of WisdomTree or any of its affiliates.