Unexpectedly Hot PPI Data Lowers Possibility of Larger Cut Next Month

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Treasury Secretary Scott Bessent, speaking with Larry Kudlow on Fox Business on Tuesday touted what he considered a "fantastic" July consumer inflation report, and reiterated that if Fed officials had seen the since-revised May/June payroll numbers, they would have already begun cutting rates. As a result, Bessent suggested a 50 basis point cut might be appropriate for September.

He also told Kudlow that upcoming Fed appointments are likely to alter the monetary policy narrative, giving Trump supporters a majority in the seven-member Board of Governors. Bessent failed to mention that the four governors certain to favor more aggressive future cuts will still have to persuade a couple of the regional Fed presidents to join the dove team in order to reroute policy. This morning, the Treasury Secretary indicated the Fed might begin with a smaller, 25 basis point cut before accelerating.

Earlier this week, Trump threatened to allow a lawsuit over the Fed's $3.1 billion building renovation project to move forward, furthering the case to remove Chairman Powell for cause. This scenario introduces the idea that if persuasion isn't effective, less cooperative committee members might also be investigated and ultimately replaced.

This morning, Bessent's characterization of a fantastic July CPI report was challenged by an unexpectedly hot PPI report as headline producer prices jumped +0.9% in July, well above both the unchanged June measure and the +0.2% median forecast. This surge in wholesale prices sent the year-over-year pace up from +2.3% to +3.3%, the highest final demand PPI reading since February. Core PPI was a similar story, up +0.6% in July, well above both the previous month's unchanged reading as well as the +0.2% forecast. On a year-over-year basis, core PPI jumped from +2.6% to +3.7%.

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So far this morning, the financial markets have taken the news of surprisingly hot pipeline prices reasonably well. Apparently, producers have been willing to absorb most increases without passing them along to consumers. Over time, this strategy is likely to erode profit margins.

Bond yields are slightly higher in early trading, generally dismissing the notion that rising producer prices will ultimately bleed into consumer prices. A quarter point reduction in the overnight funds target next month remains a near certainty along with at least one more cut before the year ends.

Market Indications as of 10:03 A.M. Central Time

DOW	Down -91 to 44,831 (HIGH: 45,014)
NASDAQ	Up 7 to 21,721 (NEW HIGH)
S&P 500	Up 6 to 6,473 (NEW HIGH)
1-Yr T-bill	current yield 3.90%; opening yield 3.84%
2-Yr T-note	current yield 3.73%; opening yield 3.68%
3-Yr T-note	current yield 3.69%; opening yield 3.64%
5-Yr T-note	current yield 3.81%; opening yield 3.76%
10-Yr T-note	current yield 4.27%; opening yield 4.24%
30-Yr T-bond	current yield 4.86%; opening yield 4.83%