

Inflation Heats Up, Rate Hike Odds Rise

Bond yields had generally been trending lower over the past two weeks with the expectation that the Fed would hold steady at the next FOMC meeting in two weeks, but this morning's hotter-than-expected consumer inflation report pushed yields higher and put an October hike back in play. The +0.6% jump in September CPI equaled the median forecast, but the +0.3% increase in the core was a tenth higher. On a year-over-year basis, headline CPI climbed from +3.4% to +3.7%, slightly above forecast, while core CPI rose from +2.4% to +2.6%.

Energy was the primary driver with a +9.1% surge in September gasoline prices accounting for half of the headline advance. Food prices continued a disinflationary string with an *unchanged* reading. Within the general food category, grocery prices were actually down -0.1% for the month. Unfortunately, this was one of just a few cool spots in the report. Airfares, used cars and trucks, hospital services and apparel all heated up last month.

Less evident, but perhaps more concerning, was a +0.4% rise in shelter costs. For several years, housing inflation had been retreating from lofty pandemic highs. The gradual easing of shelter costs had exerted consistent downward pressure and served to counterbalance much of the tariff and energy-related upward pressure. With housing contributing roughly 35% to the overall index and 45% of the core, even a relatively small monthly increase can have a significant impact.

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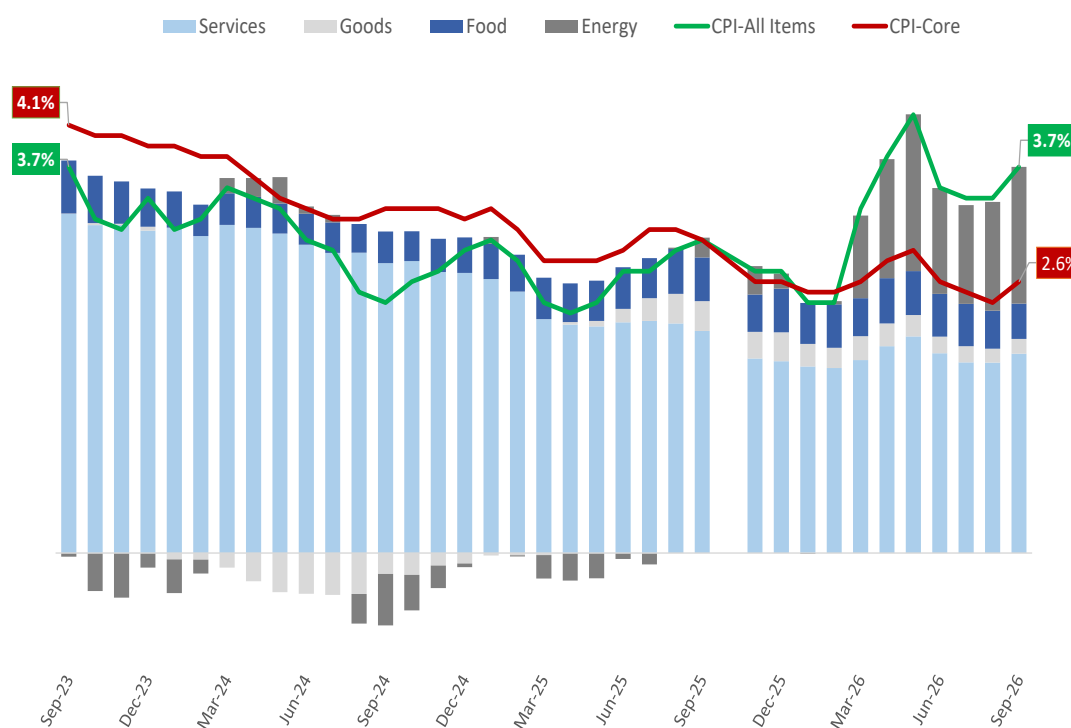
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Consumer Price Index (Year-over-Year Percent Change)



Source: Bureau of Labor Statistics

That being said, available inventory of homes has returned to pre-pandemic levels which should dampen the owners equivalent rent contribution in the coming months. Unfortunately, apartment rents are on the rise as fewer new units are being added. This mixed outlook suggests shelter costs will likely be less of a downward drag on future inflation. *All-in-all, it was a discouraging report.*

Adding to this morning's sell-off and suggesting headline inflation could move even higher in the October report, is a sharp rise in oil prices. Brent crude, the global benchmark, touched \$107 early today while domestic WTI approached \$96 after a series of attacks in the Persian Gulf region and failure of a reported "energy truce" between Russia and Ukraine. The price of diesel fuel rose to \$6.30 today according to AAA, up from \$6.23 a month earlier, but below the record high of \$6.52 from three weeks ago.

Bond yields are higher in early trading while stocks are mostly down as the futures market signals a 44% probability of a quarter point rate hike on October 28, up from 23% yesterday.

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Market Indications as of 9:29 A.M. Central Time

DOW	Up 2 to 51,673 (HIGH: 54,349)
NASDAQ	Down -238 to 26,967 (HIGH: 27,600)
S&P 500	Down -52 to 7,753 (HIGH: 7,819)
1-Yr T-bill	current yield 4.54%; opening yield 4.46%
2-Yr T-note	current yield 4.88%; opening yield 4.79%
3-Yr T-note	current yield 4.99%; opening yield 4.92%
5-Yr T-note	current yield 5.08%; opening yield 5.01%
10-Yr T-note	current yield 5.26%; opening yield 5.22%
30-Yr T-bond	current yield 5.58%; opening yield 5.56%

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