Yields Higher on Hot Inflation Report

It was a market-moving morning as a hot October inflation report sent stocks lower and bond yields higher across the curve. The headline CPI increased 0.4% month-over-month in October, above expectations of 0.3%, although that was down from September's big 0.6% increase. Stripping out food and energy, core CPI was also hotter than expected, rising 0.3% versus a 0.2% projection. This marks the third straight month that core has been up 0.3% on the month, which is not what the Fed wants to see.

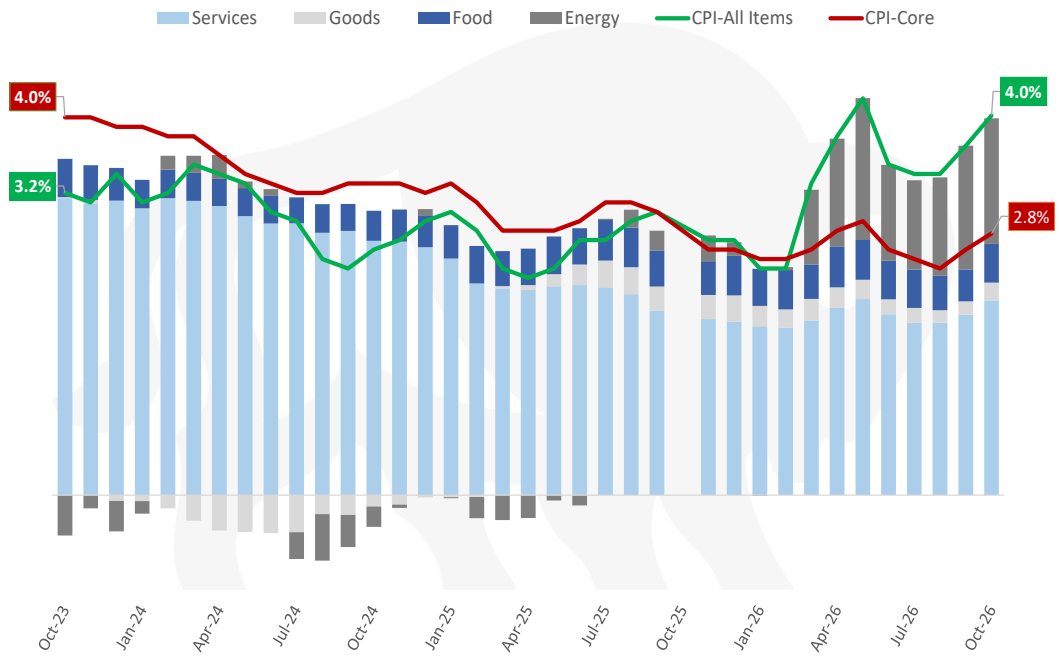
Yields moved higher after the report, especially on the front end, as the 2-year U.S. Treasury yield jumped almost 20 basis points to around 4.76%, while the 10-year moved 11 basis points higher to 5.00%.

Because October 2025 CPI data was not collected, the Bureau of Labor Statistics did not publish year-over-year readings. Using the surrounding months as proxies shows headline inflation is now running around 4%, while core inflation is 2.8%.

Looking at the details, price pressures came from the usual suspects, including medical care, auto insurance, household furnishings and education. Used vehicle prices fell 1.2%, while new vehicles edged up slightly. Shelter continues to be the largest contributor, rising 0.3% in the month and accounting for more than 30% of the overall increase.

What's also concerning for the Fed is that "super core" inflation rose 0.5% in October. This measure looks at services inflation but strips out shelter and is considered a useful measure of underlying inflation pressure. Transportation services were up 0.8%, and recreation services were up 0.9%.

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



Source: Bureau of Labor Statistics

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Please see disclosure starting on page 2.

Looking at the headline numbers, food prices moved 0.5% higher on the month, and energy increased 0.7% after jumping 5.2% in September. Beef prices increased 0.9% and are getting a lot of attention amid the shrinking U.S. cattle herd. Lettuce jumped nearly 8% on the month, and baby food and formula rose 5.1%, the largest monthly increase in the BLS tracking history. On the bright side, coffee prices fell 3.6%.

Adding to the news were comments earlier this morning from Fed Governor Chris Waller before the CPI report was released. He said a 50-basis-point hike should be considered in December if inflation readings came in higher than expected, which they did. Lisa Cook and Beth Hammack had already dissented at the October meeting in favor of raising rates, so there is clearly a hawkish tilt within the Committee.

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Markets have now fully priced a 25-basis point rate hike into the December meeting, with a 17% chance of a jumbo 50bps hike. Assuming December brings a 25bps hike, a second hike is now fully priced by March, with the probability of a third hike by September of next year at 66%.

Looking forward, there might be some relief for energy prices. Brent crude is now trading below $90, and WTI is around $85. National gasoline prices have also fallen below $4 a gallon. This was the last CPI report before the December Fed meeting, but policymakers will get another look at inflation with PPI on Friday, followed by October retail sales next Tuesday. There are also several Fed speakers scheduled before the blackout period begins later this month. With headline inflation now estimated at double the Fed's 2% target, the possibility of more aggressive tightening is in focus.

Market Indications as of 9:44 A.M. Central Time

DOW	Down -315 to 52,075 (HIGH: 54,349)
NASDAQ	Down -180 to 25,073 (HIGH: 27,600)
S&P 500	Down -38 to 7,512 (HIGH: 7,819)
1-Yr T-bill	current yield 4.53%; opening yield 4.35%
2-Yr T-note	current yield 4.73%; opening yield 4.56%
3-Yr T-note	current yield 4.78%; opening yield 4.62%
5-Yr T-note	current yield 4.82%; opening yield 4.67%
10-Yr T-note	current yield 4.99%; opening yield 4.88%
30-Yr T-bond	current yield 5.35%; opening yield 5.27%

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