US inflation

Kevin Warsh under mounting pressure to raise rates as US inflation persists

Inflation remained stubbornly elevated at 3.4% in August at the end of a week of surging oil prices

Myles McCormick in Washington and **Kate Duguid** in New York

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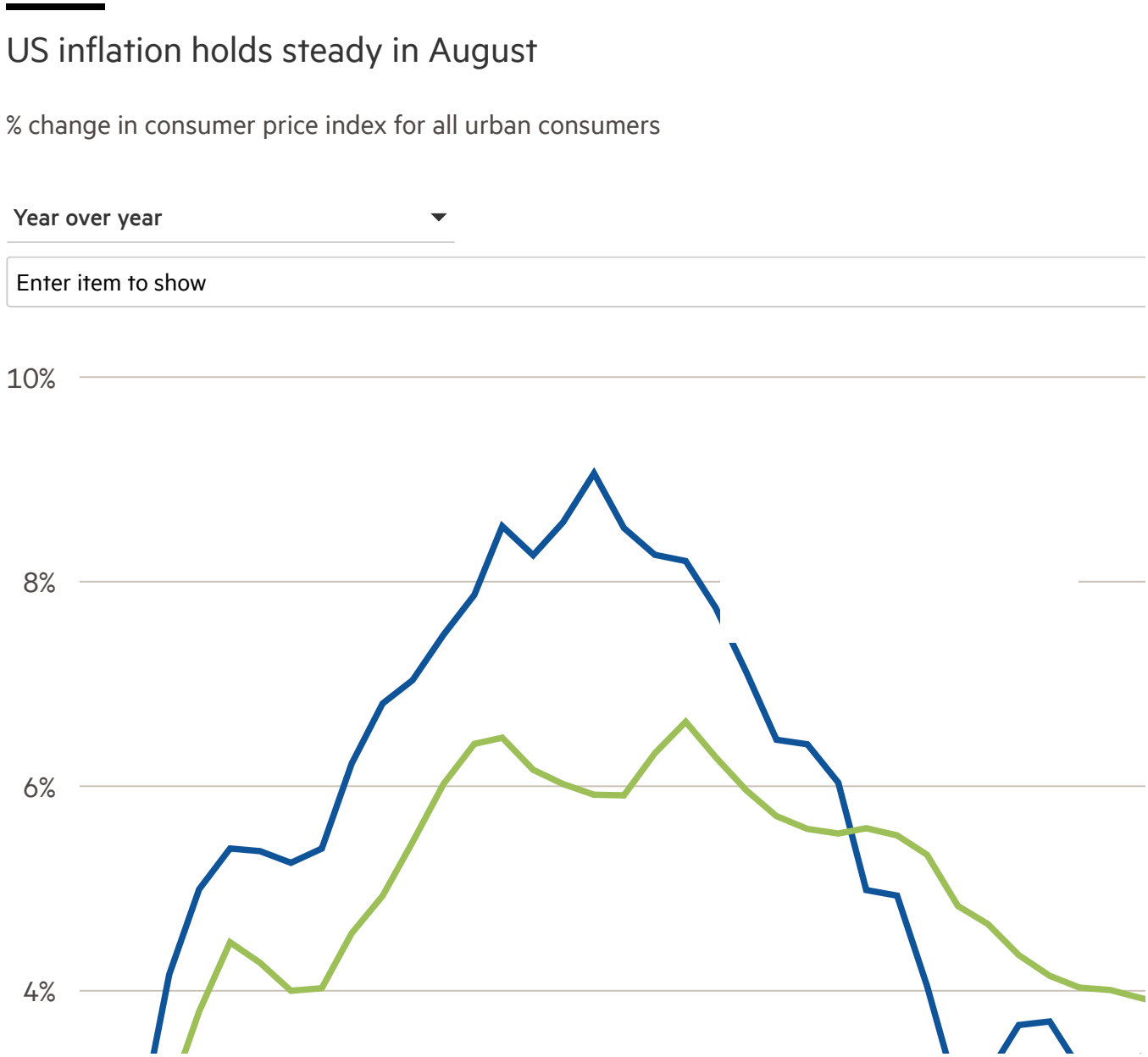
Federal Reserve chair Kevin Warsh is under mounting pressure to c | Remove highlight interest rates next week after US inflation remained stubbornly elevated at the end of a week of surging oil prices.

Expectations in financial markets of a rate increase next week jumped to almost 85 per cent after the Bureau of Labor Statistics reported on Friday that its annual consumer price index figure was unchanged in August from July's 3.4 per cent.

Core inflation, which strips out volatile food and energy prices, was 2.4 per cent, down only slightly from a 2.5 per cent rate in July.

Economists said persistent inflation made it increasingly likely that the Fed would raise borrowing costs when it meets next week, putting Warsh on a collision course with the president, who has repeatedly demanded lower rates.

"This inflation print, in tandem with recent jobs data, sharpens the conflict between the Fed's price stability mandate and the keep-Trump-happy dictate," said Eswar Prasad, economics professor at Cornell University.



Friday's report comes amid a fresh surge in oil prices driven by the conflict in the Middle East. Brent crude surpassed $100 a barrel this week for the first time since July, sparking a global bond sell-off that pushed US long-term borrowing costs to their highest level in years.

Following the inflation data, traders added to bets that the Fed will have to raise interest rates. An increase at the central bank's September meeting was viewed as a coin toss by traders a week ago.

"A Fed rate hike next week now looks like a go," said Krishna Guha at Evercore ISI. But he added that any move was "still subject to some residual uncertainties", including over Warsh's ability to convince fellow policymakers and the possibility that the oil surge could reverse.

This week's rise in energy prices comes amid the latest flare-up of the conflict in the Middle East, in which the Iran-backed Houthi rebels captured a key Red Sea port, threatening to disrupt shipping in the Bab al-Mandeb Strait at a time when the Strait of Hormuz remains all but closed.

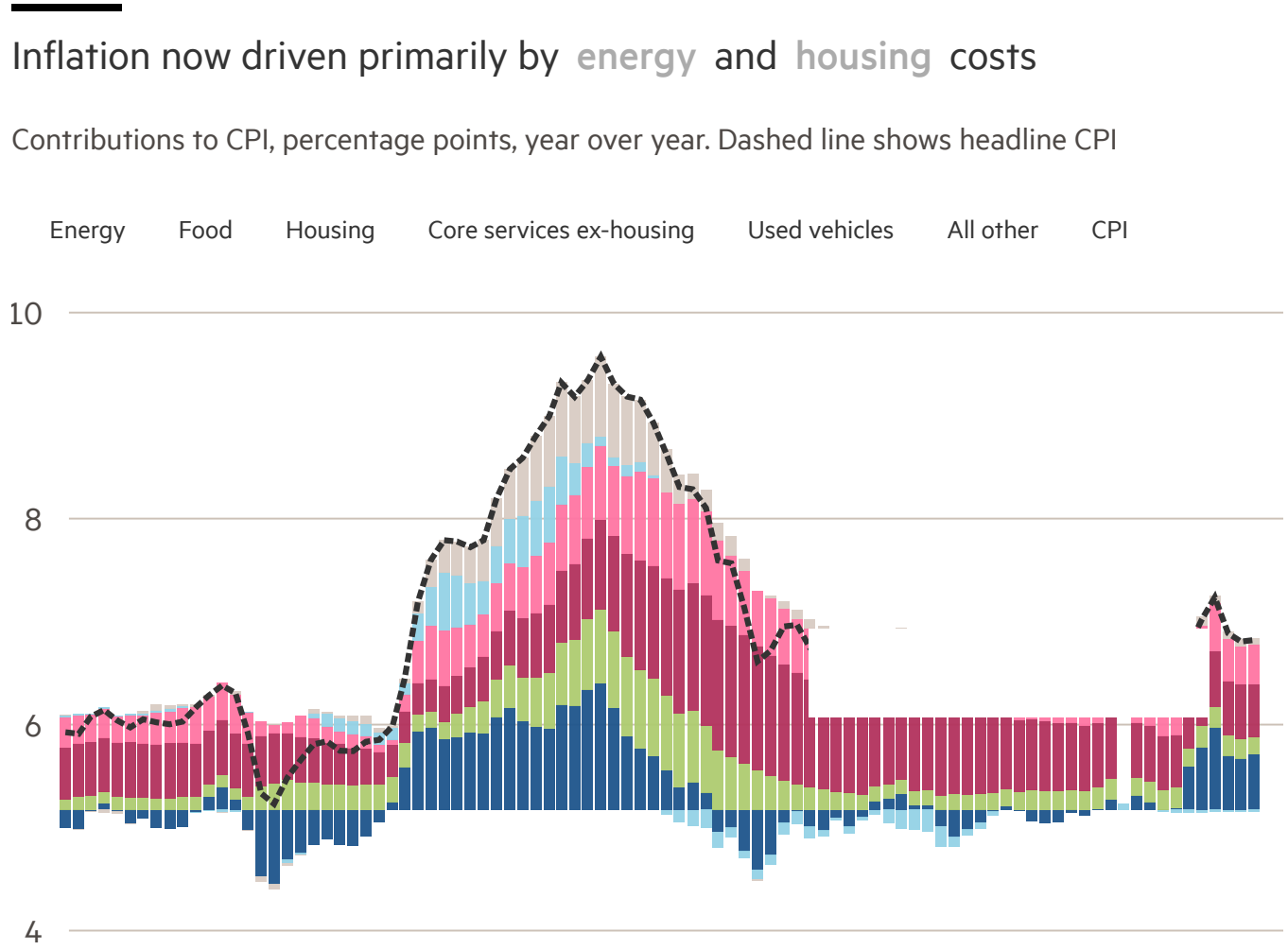
Against the backdrop of global borrowing costs soaring to their highest levels in years, US Treasury secretary Scott Bessent's effort to tame long-term Treasury yields with a bond buyback received a frosty reception in markets.

However, on Friday, 10-year Treasury yields steadied close to three-year highs as the prospect of a prompt increase in interest rates bolstered investor confidence that inflation will not be allowed to run out of control and oil fell back from its recent high.

At the last meeting of the Federal Open Market Committee in July, officials opted to keep borrowing costs on hold in a range of 3.5 to 3.75 per cent.

Three of the 12 voters broke with the majority to vote for a quarter-point rise, however. Analysts said Friday's sticky inflation data was likely to push others on the committee to join them in backing an increase.

"The August inflation data is heading in the wrong direction for the Fed," said Mike Reid at RBC Capital Markets. "Those folks that were in the hold camp are going to look at this and go: 'We have to get this under control.'"



Market bets on a rate rise had already risen sharply after Warsh gave a hawkish speech at Jackson Hole late last month, indicating that unless there was swift progress in containing prices, the central bank would have “work to do”.

The central bank’s preferred personal consumption expenditures measure of inflation sat at 3.7 per cent in July, the last month for which data is available, and has exceeded its 2 per cent goal for more than five years.

“We’re going to a hike now,” said Kurt Lewis at Piper Sandler. “This was a case where everybody was, like, one more bad thing has to happen, and then we’re ready to go. And I think this is enough of that.”

Still, some economists cautioned that despite the growing expectations of a rate increase, it was not guaranteed that the Fed would act.

“Some in the market believed a lower CPI reading was necessary for the Fed to remain on pause and have now shifted their expectations toward a hike,” said Atsi Sheth, chief credit officer at Moody’s Ratings.

“However, because inflation came in largely as expected rather than accelerating, the possibility of a continued pause remains on the table,” she added.

Elevated fuel prices remained the biggest driver of inflation in August, with petrol accounting for more than a third of the monthly rise of 0.4 per cent.

Kroger, the largest US supermarket chain, on Friday cut sales guida
executive Greg Foran said that higher fuel prices had contributed to “tighter” conditions where “customers are buying more on need”.

“What we’re seeing is the consumer continues to be disciplined. They’re not absent. They’re turning up to the stores, but they’re pretty disciplined about what they buy,” Foran said.

Additional reporting by Gregory Meyer in New York

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