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Inflation rises, though consumers see some relief in grocery prices

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WASHINGTON · U.S. inflation accelerated last month as the prices of gasoline and many other goods and services rose, though grocery prices dipped, providing consumers some relief.

The consumer price index rose 3.7% in September compared with a year ago, the Labor Department said Wednesday, up from 3.4% in August. On a monthly basis, costs jumped 0.6% from August to September, the biggest gain in five months, up from a 0.4% increase the previous month.

The government said Wednesday that Social Security recipients will receive a 3.6% cost-of-living increase, based on the inflation figures.

Amid the rise in inflation, consumers saw some relief in grocery prices, which actually declined 0.1% last month and are up just 1.8% from a year ago. Ground beef prices fell 0.8% in September, though they are still up 5.4% from last year.

In the last four decades, the steepest increase in year-over-year inflation occurred under then-President Joe Biden in June 2022, when the rate hit 9.1%. The average hourly earnings dropped by 3.6%, seasonally adjusted, from June 2021 to June 2022.

By comparison, the Labor Department said Wednesday that the average hourly paychecks, when adjusted for inflation, shrank by 0.7 percent.

The latest figures underscore the lingering impact of the Iran war on gas prices and the stubborn persistence of inflation, which has ticked higher since the war began in late February.

The rise isn't all linked to oil and gas, as surging investment in data centers and AI has also pushed up prices for computer chips and the consumer electronics that use them.

Wednesday's figures are the last major inflation data to be released before the upcoming midterm elections.

Elevated inflation is a challenge for the Federal Reserve, which is required by Congress to seek stable prices.

Excluding the volatile food and energy categories, core prices rose 2.6% in September from a year ago, up from 2.4% the previous month and higher than economists had expected. And they climbed 0.3% from August to September, an elevated pace that, if it continued for a year, would run well above the Fed's 2% target.

Higher inflation will likely put more pressure on the Fed to lift its key interest rate at its next meeting Oct. 27-28.

Economists noted that the report showed price increases were spread more broadly across the economy than in recent months.

"The report was worse than expected," Bill Adams, chief U.S. economist at Fifth Third Bank, said in a note to clients. "Price increases were widespread. ... Consumer demand seems to be holding up better than the downbeat consumer surveys would suggest, helping businesses maintain pricing power."

Gas prices jumped 9.1% just from August to September, the government's consumer price index report said. Rising gas costs are a highly visible sign of inflation and often drive down measures of consumer sentiment about the economy.

With fuel much more expensive, airfares rose 1.2% last month and have soared 22% compared with a year ago. Hotel prices rose 2% from August to September and are up 4.4% compared with a year earlier. Consumers saw some relief in grocery prices, which actually declined 0.1% last month and are up just 1.8% from a year ago. Ground beef prices fell 0.8% in September, though they are still up 5.4% from last year.

The cost of toys, new and used cars, sporting goods and shoes all rose at a rapid clip last month, the government said.

The Middle East and Russia-Ukraine conflicts have sharply inflated the cost of diesel fuel, which is used by longhaul trucks. Higher diesel prices will increase shipping expenses, which in turn could push up prices for a range of goods.

Federal Reserve officials are watching inflation data closely to determine whether they need to raise their shortterm interest rate further, and by how much.

Fed Chairman Kevin Warsh said last month that inflation isn't moving quickly enough back to the central bank's target, causing the Fed to hike rates for the first time in three years, to about 3.9%.

Yet some key Fed officials have suggested the central bank can wait before increasing rates again. Fed officials have penciled in just one more rate hike this year.

Still, Wednesday's report has led many Wall Street investors to project that the Fed will now act in two weeks.

Stock prices fell slightly after the report, while greater expectations for rate hikes pushed up bond yields.

By raising borrowing costs, the Fed hopes to slow spending and growth and cool price increases. Much of the current inflation comes from supply shocks, such as the Iran war's disruption to oil and gas supplies and higher interest rates can't address those bottlenecks.

Warsh has said his goal is to keep the gas price spike from seeping into more areas of the economy. It's already pushed up the price of airfares about 22% from a year ago.

Those costs raise shipping and other expenses for many large and small businesses, some of which are forced to pass the cost to consumers. Last week, PepsiCo said that it will raise prices for its snack foods, including Doritos, Ruffles, Sun Chips and some sodas to offset higher costs for fuel, aluminum and food ingredients.

The artificial intelligence buildout has also sharply elevated the cost of semiconductors, computer equipment and electrical components, which have been passed on to consumers in the form of more expensive electronics, such as gaming devices, laptops and smartphones.

Goldman Sachs estimated in a report Tuesday that the AI buildout has added about a half-percentage point to the annual inflation rate, according to the Fed's preferred inflation gauge.

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High retail prices in October suggest pain at the pump will continue.

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Energy costs drove inflation in September, and there were signs that they are spreading to other parts of the economy. ZAK BENNETT/ BLOOMBERG NEWS

Inflation Jumped to 3.7% in September

Gasoline drove good part of the month's climb, stepping up pressure for rate rise

BY KONRAD PUTZIER

U.S. inflation accelerated to 3.7% in September as energy costs soared, making the Federal Reserve's interest-rate decision later this month a closer call ahead of the midterm elections in November.

Consumer prices last month were hotter than August's gain of 3.4%, the Labor Department said on Wednesday, and above the 3.6% rise expected by economists surveyed by The Wall Street Journal. There were signs that high energy prices were starting to seep into other parts of the economy.

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The latest inflation report raises pressure on the central bank. Fed officials must now decide whether they can afford to wait until December to increase rates again after signaling recently that they didn't anticipate a rate rise at their Oct. 27-28 meeting.

Wall Street traders dialed up their bets that the Fed might indeed raise rates when officials meet in two weeks. Probabilities in futures markets of an October rate increase jumped to about 50% after the report was released, though that eased back to about 33% later in the day. But that is up from 22% before the report was released.

The bigger question, though, is how high rates ultimately need to go. That depends on whether pressures from higher energy prices and the artificial-intelligence investment boom are spreading into the broader economy.

Prices excluding food and energy—the so-called core prices, which economists watch to gauge underlying trends—rose 2.6% last month, above forecasts for a 2.5% increase. Month over month, core prices rose by 0.3%, surprising economists who expected a 0.2% increase.

“At this point we're at dangerously elevated levels of inflation,” said Lindsey Piegza, chief economist at Stifel.

High prices have been a political flashpoint for Americans, who have grown fed up with more than five years of inflation. Prices rose much faster in September than average hourly earnings, which increased 3% from a year earlier, marking

the sixth month in a row of inflation outpacing wages. That means many people are seeing their real incomes fall.

That dynamic could be costly to Republicans as voters cast their ballots. President Trump's critics said his policies contributed to inflation: war with Iran on energy, tariffs on goods, and the AI buildout, of which Trump has been an enthusiastic backer, on computer equipment.

Trump's advisers said rising prices reflect years of cumulative growth and that the White House's deregulation push will lower prices. The U.S. economy, by many measures, remains resilient.

Stocks fell broadly on Wednesday, with the Nasdaq 1.9% lower, and the Dow Jones Industrial Average trading off 0.1%. The S&P 500 was off 1.1%.

Bond yields were whipsawed as the hotter-than-expected inflation report gave way to a tech selloff that had investors fleeing for more defensive assets. Treasury yields rose sharply in the morning after the report, but the 10-year yield later fell from its Wednesday peak above 5.32% to 5.189%.

Energy costs drove inflation in September, and high retail prices in October suggest pain at the pump will continue. Prices have soared since the Iran conflict started at the end of February. Gasoline prices last month rose 9.1% from the prior month—a faster pace than August's 3.9% rise—and are up 34% over the past year. Fuel-oil prices are up 74% since last September.

Food prices were flat from the prior month after rising 0.1% in August but are up 2.5% over the past year. Economists are paying attention to signs that higher transportation costs are trickling through to prices of goods like meat and dairy.

Airfare, which is highly sensitive to fuel costs, was up 22% from a year earlier.

Used car and truck prices rose by 0.7% month over month, up from 0.4% in August, but were down from last year. Prices of goods like apparel and toys, which are often made from petrochemicals, ticked up.

While oil was the main driver of inflation, price growth picked up in categories that are less energy sensitive. “This points to broad-based inflation pressure,” said Samuel Tombs, chief U.S. economist at Pantheon Macroeconomics.

The cost of recreation services like streaming rose, reflecting “buoyancy in consumer demand,” Tombs said. Prices of hospital services also ticked up.

Some economists see the September report as a worrying sign that the Iran war wasn't just a one-off price shock and that higher inflation is here to stay unless the Fed acts. “It's already becoming a prolonged issue” seven months into the war, said Stifel's Piegza.

One particular concern: Surveys show consumers expect higher inflation in the years to come, which can become a self-fulfilling prophecy if they rush into purchases to get ahead of price increases. Respondents in the University of Michigan's latest

consumer survey said they expect inflation of 4.7% over the next year, up from 4.6% in last month's survey. Five-year inflation expectations rose to 3.5% from 3.4%.

Other economists are more sanguine, pointing to falling real wages as a sign that inflation is likely to come down. "Right now the labor market looks weak," Tombs said.

A key reason inflation is stuck above the Fed's target is the strength of U.S. consumers. Buoyed by low unemployment and rising stock prices, households continue to spend despite rising prices. Executives at the country's biggest banks said this week that higher rates so far haven't dented consumer or business appetite to borrow and spend.

That has all made it easier for businesses to pass on cost increases to their customers.

As for whether Fed officials will raise rates at their next meeting, some analysts argue that there is little reason for the Fed to wait if officials expect to raise rates anyway. Officials, though, haven't given any sign that one report would lead them to reconsider.

The inflation report raised the stakes for Federal Reserve Chairman Kevin Warsh's coming appearance at the International Monetary Fund's meetings in Bangkok, the last scheduled remarks by a Fed official before policymakers go quiet ahead of the October meeting, which is less than a week before the midterm elections.

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