Economic Update

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1. CPI INFLATION

- The Consumer Price Index rose 3.7% year-over-year and 0.6% month-over-month in August, its largest monthly increase this year, according to Wednesday's release by the Bureau of Labor Statistics.
- Energy was responsible for much of the increase in headline inflation, rising 5.6% on the month, including a 10.6% increase in gasoline offset by other key energy metrics.
- Core-CPI, which excludes food and energy prices from the calculation, rose 0.3% from July and 4.3% year-over-year, hotter than many economists expected. Shelter continued to be a pivotal contributor to core CPI, while prices for other core items, such as used vehicles and airfare, continued to decline.
- Just one week after the CPI release, FOMC officials are set to meet to conduct their newest policy decision, where they are largely expected to hold rates steady.

2. INTEREST RATE OUTLOOK

- According to the Chicago Mercantile Exchange's Fed Watch Tool, an overwhelming majority of futures markets (97.0%) expect the FOMC to hold the benchmark Fed Funds rate unchanged at 5.25-5.50%.
- Despite a hotter-than-expected core-CPI inflation reading in August, officials prefer the Bureau of Economic Analysis' PCE core inflation, which, while currently hovering slightly above the CPI measure, has shown a steadier decline over the past year.
- Fed policymakers have recently positioned themselves with a more balanced outlook on inflation, viewing underlying price pressures as fading but cautious about taking their foot off of the break too prematurely. Presently, futures markets do not predict a rate cut from current levels until June 2024.

3. CONSUMER INFLATION EXPECTATIONS

- US consumer inflation expectations for the year ahead rose to 3.6% in August, up from 3.5% in July, according to the New York Fed's monthly survey.
- This month marked the first time since March that consumer inflation expectations increased. One-year-ahead inflation expectations for rent ticked up 20 basis points to 9.2%, gas up 40 basis points to 4.9%, and food up 10 basis points to 5.3%.

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- Median home-price expectations for one year ahead climbed 30 basis points to 3.1%, its highest mark since July of last year.
- Despite the broader rise in inflation expectations, they remain well below where they were one year ago. August's marginal increase is unlikely to move the Fed away from its likely decision to hold rates firm in September.

4. AUGUST JOBS REPORT

- The US economy added 187,000 jobs during August, continuing a positive but annualized downtrend as job openings continue to fall from their March 2022 peak. The unemployment rate jumped to 3.8%, its highest level since February 2022.
- Health care experienced the largest gain by sector (+71,000), followed by leisure and hospitality (+40,000), social assistance (+26,000) and construction (+26,000).
- Transportation and Warehousing was the biggest loser (-40,000), likely impacted by a recent major bankruptcy in the trucking industry.
- Partially explaining the rise in the unemployment rate is an expansion of the labor force, which increases the number of people looking for jobs relative to job openings, distorting the unemployment rate. The labor force participation rate rose to 62.8% in August, the highest since February 2020, shortly before the COVID-19 pandemic in the US.
- Average hourly earnings increased 0.2% month-over-month and 4.3% over the past 12 months, a slowdown from previous months. The slowdown in wage inflation is a crucial signal that underlying inflation pressures are easing in the United States.

5. SMALL BUSINESS OPTIMISM

- The Small Business Index, produced by the National Federation of Independent Business (NFIB), declined slightly in August from the previous month, the first monthly decline since April.
- Small Business optimism rose steadily throughout the spring and early summer months, indicative of fading recession fears and re-anchored inflation expectations. However, the recent downtick may signal a

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reversal in sentiment as experts warn that US recession risks remain. At the same time, Fed policymakers indicate a willingness to keep rates restrictive in the medium term.

- 23% of small business owners indicated that inflation was their single most important problem, up two percentage points from July.
- The share of owners expecting better business conditions over the next six months declined, discouraged by lower future sales growth prospects.

6. LOGISTICS MANAGERS' INDEX

- The Logistics Managers' Index (LMI), a diffusion index that measures activity in Inventory, Warehousing, and Transportation, rose in August at its fastest pace since February.
- The increase arrives after five consecutive months of declines, each registering all-time lows for the index. Sector activity is a key barometer for the underlying fundamentals impacting Industrial Real Estate.
- August's expansion was driven by increased activity across all eight LMI sub-metrics. While inventories remain in contraction, the rate of decrease has slowed, while inventory costs and warehouse pricing have risen.
- Transportation utilization has also moved from contraction territory to neutral, while transit pricing continues to fall, but at a slower rate than in previous months.
- While it is unclear if LMI's trend toward expansion is a one-off or here to stay-, concurrent trends in wages and consumer spending levels, alongside anecdotal evidence from industry participants, support the latter.

7. WHOLESALE INVENTORIES

- Wholesale inventories in the US fell by 0.2% between June and July, according to the latest data available from the US Census Bureau. On an annual basis, inventories remain up by 0.5%.
- Inventory levels performed worse than market forecasts but slightly recovered from a steeper 0.7% drop between May and June. Levels have now declined for five consecutive months.
- The most significant declines were in furniture (-2.9%), hardware (-0.8%), electrical equipment (-0.8%),

and durable goods (-0.3%).

- On the flip side, inventories of petroleum rose (4.9%), as well as farm products (3.4%, and non-durable goods (0.1%).

8. DATA CENTER TRENDS

- Power availability appears to be the primary driver of data center development in the US, according to a recent analysis penned in Globe St.
- Rental rates appear to increase faster in areas where data centers already exist. While these agglomerations aren't completely surprising, it questions why newer markets with cheaper available aren't emerging more quickly and normalizing nationwide rents.
- As the article notes, one key reason for this is the power requirements for such real estate ventures. These requirements have forced developers to prioritize space with existing power infrastructure suitable for their needs, keeping rents high and skyrocketing construction activity in the sector.

9. REDBOOK RETAIL INDEX

- The Redbook Index, a sales-weighted index of year-over-year same-store sales growth in the US, has quietly rebounded from two-year lows that snowballed earlier this summer, according to the latest data from Redbook Research, Inc.
- Just seven weeks ago, the index had fallen into negative territory, falling by an average of 0.3% year-over-year during July. In August, year-over-year retail sales accelerated and have climbed back to an annual growth rate of 4.6% as of the week ending on September 9th.
- The Redbook serves as a leading indicator for the retail industry, showing near-real-time sales data for retailers. At the same time, the more popular Census Bureau measure reports on a one-month lag. The latest Redbook data may signal a continued positive trajectory for the Census Bureau's sales data, which during July, experienced its biggest annual increase in five months.

10. SPECIAL SERVICING RISES

- Special servicing rates, a helpful test for the health of commercial property cash flows and their ability to cover debt service, rose for the seventh consecutive month in August, according to the latest data from Trepp.

- Office properties continued to lead increases in special servicing, up 39 basis points during the month. Most other property levels had negligible changes, with multifamily experiencing the second largest increase, rising 32 basis points, while the retail rate fell by 80 basis points.
- In total, $1.21 billion in loans were transferred to the special servicer in August. Noteworthy, a single multifamily property in San Francisco that was transferred accounted for 21% of the overall monthly increase. A separate Midtown Manhattan office property that was transferred accounted for 15% of the overall increase.
- Special servicing rates for lodging and industrial properties were little changed during August.

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SUMMARY OF SOURCES

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