Economic Update

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JULY 15, 2022

1. JOBS REPORT

- Despite rising capital costs and renewed recession fears, the US economy added 372k jobs in June, according to the latest employment numbers from the Bureau of Labor Statistics.
- Business Services led the way with 74k new payrolls in June. Management roles had the largest increase within the industry, with 12k jobs added in the month.
- Leisure and hospitality had a strong month with 67k new jobs added in June. Food services and drinking places continued to grow, adding 41k of all Leisure and Hospitality job gains. According to the Federal Reserve's most recent beige book release, most of the nation is reporting an increase in travel and recreational activity. Still, employment in Leisure and Hospitality remains down by 1.3 million or 7.8% since February 2020.
- The unemployment rate remained unchanged at 3.6%, where it has sat for the past four months. The number of unemployment persons was also unchanged at 5.9 million.
- The Labor Force participation was little changed at 62.2% and remains below the 63.4% registered at the labor market's pre-pandemic peak in February 2020.

2. INFLATION AND INFLATION EXPECTATIONS

- The Consumer Price Index (CPI) rose 9.1% year-over-year through June according to the Bureau of Labor Statistics, another four-decade-plus high for the popular inflation gauge.
- Core-CPI inflation, which excludes food and energy prices and is more consequential for policymakers, appears to have peaked at 6.5% in March and has nicked down in each successive month since. Nonetheless, the continued pressure on food and energy prices continues to be a significant concern for policymakers and forecasters.
- The energy sub-index of CPI rose 7.5% in just the past month and accounted for almost half of overall price increases in June.
- Inflation-adjusted or "real" incomes reduced by 1% in June and are down 3.6% from one year ago, according to data from both the CPI and Jobs reports.

3. BEIGE BOOK

- Several of the twelve Federal Reserve districts reported growing signs of slowing demand, with at least five districts concerned about an increased risk of a recession, according to Fed's July 13th Beige Book release.
- Overall economic activity has been expansive since mid-May, but most districts reported a moderation in consumer spending as higher food and gasoline prices soaked up households' discretionary income.

- Auto sales remained sluggish, largely due to low inventory rather than slowing demand. Meanwhile, manufacturing activity was mixed, with several districts reporting that supply chain and labor issues continued to slow down production.
- Hospitality and tourism activity remains strong, with several districts reporting an uptick in group travel.
- Housing demand continues to noticeably weaken. Growing concerns about affordability is believed to have contributed to non-seasonal declines in sales, causing inventory to climb and prices to moderate.
- Commercial Real Estate conditions also slowed, while overall loan demand was mixed across most districts. Demand for consumer credit lines has grown while residential loan demand has weakened in the face of higher interest rates.

4. NMHC CONSTRUCTION SURVEY

- Developers reported continued permit delays, materials price increases, and labor market tightness, according to the latest Quarterly Construction Survey conducted by NMHC in early June.
- 97% of respondents reported permitting delays—though the backlog has been consistent through the pandemic and is evident of similar labor and resource shortages being felt by state and local governments.
- 83% of respondents report that they have had to re-price deals over the past three months. Repricing has improved since March—the average project in June was repriced up by 11% compared to 25% three months ago.
- Developers reported a 5% decline in lumber prices over the past three months, a reversal from the previous quarterly survey.
- Labor shortages are impacting over half of apartment developers. 53% report increased labor costs over expected levels within the last three months. 50% report that labor availability has remained the same compared to three months ago, while 40% report that availability has worsened.

5. CMBS DELINQUENCIES

- The CMBS delinquency rate posted a small but unexpected uptick in June, climbing 6 bps and landing at 3.2%, according to data by Trepp. The uptick was only the second over the past two years, with the last increase occurring in late 2021.
- Each of the major property sectors saw a slight increase in delinquencies last month, with 0.18% of all loans now in the 30 days delinquent bucket— up five bps from May. The percentage of loans with special services fell to 4.91, a decline of 21 bps from May.
- By sector, Industrial remained on the most solid footing (0.23%) but saw delinquencies climb by 11 bps month-over-month in June. Multifamily (1.04%) is up 2 bps from May. Office (1.28%) rose 5 bps. Lodging (5.08%) is up 6 bps from May while Retail (5.69%) is up 14 bps.

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6. GAS PRICES

- Wholesale gasoline futures are falling, with unfinished gas, commonly referred to as "RBOB" down roughly 20% since its June 9th high. Prices at the pump often follow RBOB prices.
- The average price per gallon at the pump stood at $4.63, down 15 cents from the week prior and down 38% over four weeks, according to AAA. Gasoline prices have now declined for 28 days straight.
- According to an analysis by the NY Times, energy analysts say that Americans are spending in total $140 million less per day at the pump than they were one month ago.
- Despite a massive, 11.2% month-over-month increase for the all-gasoline sub-index of CPI in June, fuel oil posted a -1.2% month-over-month decline over the same period.

7. OFFICE DEMAND

- New Office demand ticked up in May, according to the VTS Office Demand Index (VODI).
- Office demand has essentially plateaued since March, falling into what appears to be a new post-pandemic equilibrium. However, VODI is up 21.8% quarter-over-quarter as the office market has shaken off the temporary headwinds induced by the omicron wave. VODI is down 14.1% year-over-year.
- On a metro-level, many metros showed slight recoveries in May but remain below their post-vaccine peak. New York City saw a notable increase of 12.7% month-over-month in May and 31.1% quarter-over-quarter. However, the Big Apple remains 16.7% below its post-vaccine peak in Fall 2021.
- Other metros that saw Office demand climb were San Francisco (+2%), Boston (+3%), and Seattle (+9%). Declines were seen in Chicago (-14%), Washington D.C. (-2%), and Los Angeles (-1%).

8. GDPNOW PREDICTS RECESSION

- A growing number of analysts, institutions, and key indicators are increasingly signaling signs of a recession, and the Atlanta Federal Reserve's GDPNow index just became the latest metric to flash a warning sign.
- According to the latest GDPNow update (July 8th), seasonally adjusted real GDP growth is expected to register an annualized -1.2% decline in Q2 2022.
- While the GDPNow forecast finished the week stronger than it had started, the predictions add to the grey cloud hovering above markets. Following Friday's jobs data and wholesale trade reports from the BLS and Census Bureau, respectively, GDPNow revised up real personal consumption expenditures from 1.3% to 1.9% annualized and private investment was revised up from -14.9% to -13.7%, annualized.

9. THE HOT MARKET FOR COLD STORAGE

- Cold Storage, which saw an influx of interest during the pandemic as increased demand for food delivery, groceries, and vaccine distribution poured money into those assets, faces an uncertain future as we move into the post-pandemic phase.
- Overall, high demand remains, with the average vacancy rate standing at 3.5% for Cold Storage properties according to an analysis by Wealth Management.com. Cold Storage is seeing lower vacancy rates than overall traditional warehouse space.
- High population, a large volume of agricultural imports, proximity to large ports, and limited space for cold storage are thought to be the key factors aiding asset pricing. Jacksonville, Detroit, and South New Jersey stand out as examples of where this is taking place, according to the analysis.
- Historically, Cold Storage has been dominated by handful of specialized REITs, but in recent years, the sector has attracted interest from private equity and institutional capital.

10. APARTMENT DEVELOPMENT RISKS

- While apartment demand remains strong in the face of growing economic uncertainty, the industry should remain on the lookout for oversupply risks, according to analysis by Apartments.com and CoStar.
- Multifamily construction stands at its highest level in 40 years with over 842k units currently in development. Recent trends largely reflect an attempt to catch supply up to soaring apartment demand, which has been responsible for some of the fastest residential rent growth on record.
- However, the analysis looked at metros that fall into three categories: Markets with the greatest rise in apartment vacancies over the past year; markets that have experienced the steepest rent growth declines over the past year; and current supply levels compared to the previous three-year average.
- The analysis found that Phoenix, Tampa, and Austin could be candidates for potential overbuilding using the three metrics, as both Phoenix and Tampa fall in the top 10 for all three categories, while Austin does for two categories and registers at #11 in a third. Raleigh and Las Vegas, while considered as high-risk as the previous three, came in close behind.

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SUMMARY OF SOURCES

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