Economic Update

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MONTH DAY, 2023

1. FED MEETING MINUTES

- Minutes from the FOMC's May 2-3 policy meeting showed that central bank policymakers were split on the decision to continue raising interest rates or pause increases during its most recent vote.
- Ultimately, the decision to raise rates by 25 basis points in May was unanimous. However, the minutes signal that officials are taking an increasingly balanced approach to fighting inflation as their tightening efforts gradually show their impact on the US economy.
- While some officials have signaled openness to a pause, most have also reiterated that the committee is not "done" in its fight against inflation, and their decisions remain data dependent. Other officials remain aggressive in stamping out recent price pressures, believing that rate hikes should continue to anchor future inflation expectations.
- According to the Chicago Mercantile Exchange's Fed Watch Tool, there is a 66% chance that the Fed will pause rate hikes at its June policy meeting.

2. DEBT CEILING NEGOTIATIONS

- President Biden and House Republicans appear to be inching closer to a bipartisan deal to avert a looming debt-ceiling limit, according to senior aides from the White House and Speaker Kevin McCarthy.
- Talks have intensified in recent days as a projected early-June fiscal cliff approaches, and a deal that satisfies both sides of the aisle remains elusive.
- The Treasury Department estimates that the US could run out of money as soon as June 1st, which economists warn could potentially upend the global financial system and send the economy into recession.
- On May 24th, Fitch, a rating agency, placed the US Government's "AAA" credit rating on negative watch, signaling that partisan disputes have threatened the standing of US creditworthiness.
- House Republicans are seeking significant cuts to discretionary spending before agreeing to raise the debt limit. The White House and Congressional Democrats initially looked to pass a clean increase without cuts but recently agreed to freeze spending at current levels for the following year.
- It is expected that both sides will need to compromise to pass legislation through the Republican-controlled House and Democrat-controlled Senate.

3. HOW A US DEFAULT COULD IMPACT CRE

- If no deal is reached in Washington and the US defaults on its debt, the result will have far-reaching effects on parts of the global economy, with commercial real estate among them.
- US Treasury values would fall, creating upward pressure on mortgage yields and other market interest rates. According to the Mortgage Bankers Association, this process has already begun to play out simply

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based on the growing possibility of default. In recent days, default fears appear to have pushed mortgage rates up and resulted in a decline in purchase applications.
- The recent banking crisis would also likely intensify, as recent distress was mainly due to an oversaturation of treasuries on the bank's balance sheet that was not hedged for the risk of rising interest rates. If a default were to cause even further upward pressure on rates, banks that have avoided issues during the Fed's rate hikes might get thrust into distressed positions. This could significantly dry up financing for CRE projects.
- A debt ceiling crisis would immediately delay deals, and prices would initially fall in the wake of a default. However, opportunistic buyers may swoop in during this time, as seen during the early days of the pandemic, and create some market demand.

4. BANK SHARE OF CRE DEBT

- As small and mid-sized banks face new challenges, there have been increased concerns around their foothold in commercial real estate debt markets. However, a study by Moody's Analytics suggests that while smaller banks have grown in market-share recently, they are far below the "65-70%" number thrown around by some recent doomsday-like analysis.
- According to Moody's estimates, banks account for 38.6% of CRE lending, while mid-sized regional banks, of which there are 135 nationwide, account for just 13.8% of CRE debt.
- The nation's top-25 largest banks hold 12.1% of CRE debt, while the 829 community banks hold 9.6% of CRE Debt.
- As noted in the Fed's most recent Senior Loan Officer Opinion Survey (SLOOS), most lenders tightened credit standards during the first quarter of 2023, which could reduce some financing options for the CRE market. However, Moody's notes the CRE debt market is large and diverse, and several non-bank lenders such as insurance companies, mortgage REITs, and others could step in to fill the gap.

5. Q1 GDP SECOND ESTIMATE

- The Q1 US GDP estimate was revised from a 1.1% annualized rate to 1.3%, according to the latest data from the Bureau of Economic Analysis.
- The upward revision reflected a smaller decrease in private inventory investment than previously estimated, while consumer spending accelerated more than expected (3.8% compared to the previous estimate of 3.7%). The upward revision in spending is notable given rising financing costs and inflation that, while cooling, remains high by historical standards.
- Non-residential fixed investment was also revised upward to 1.4% annualized versus a previously estimated 0.7%, while government spending was revised up to 5.2% annualized compared to the 4.7% previously

estimated. Residential fixed investment shrank more than previously estimated.
- Despite the upward revision, Q1 2023 remains the slowest quarter for growth since Q2 2022, though a US recession appears to have so far been avoided.

6. NEW AND EXISTING HOME SALES

- Sales of new single-family houses rose to a seasonally adjusted annual rate of 683,000 in April, according to the Census Bureau, 4.1% above March's pace and 11.8% above the April 2022 level. For sale inventory currently has 7.6 months of supply.
- The median sales price for a new home sold in April was $402,800.
- Meanwhile, according to the National Association of Realtors (NAR), existing-home sales declined by 3.4% in April to a seasonally adjusted annual rate of 4.28 million. Sales were down 23.2% from one year ago.
- The median existing-home sales price fell 1.7% in April to $388,800.

7. EMERGING TRENDS IN DINING

- At the recent ICSC conference in Las Vegas, dining experts convened for a session to discuss emerging trends in the food and beverage industry, including the evolution of consumer behavior and its impact on retail real estate.
- Speaking about plans to expand their "Dave's Hot Chicken" brand, SVP of Real Estate Dannon Shiff explained that the ideal space for his brand includes daily necessities, possesses high visibility, has ample parking facilities, and presents a significant signage opportunity.
- Patrick Chamberlain of Hart House spoke about the need for location relative to local trade areas, where travel guests or employees seek lunch and dinner options. Their brand is eyeing both urban and suburban locations for expansion, noting that the remote work shift has led to reevaluations of local trade hot spots.

8. CONSUMER SENTIMENT

- US consumer sentiment fell to a six-month low of 57.7 in May 2023, down from a reading of 63.5 in April, according to data from the University of Michigan.
- Survey forecasters had projected a reading of 63 in May, but a recent deterioration in expectations about the economy's future trajectory led to steeper declines.
- The expectations sub-index fell to 53.4 in May from 60.5 during the month prior. The current economic conditions index fell from 68.2 to 64.5.
- Year-ahead inflation expectations fell slightly to 4.5% from 4.6% in April.
- According to survey director Joanne Hsu, recent negative news stories, including the debt ceiling standoff

and banking crisis, may have led to the fall in sentiment in recent weeks.

9. PENDING HOME SALES

- Pending home sales, meanwhile, remain steady. According to the NAR, pending home sales remained unchanged from March at an index reading of 78.9 in April.
- Pending transactions remain down by 20.3% year-over-year. According to NAR Chief Economist Lawrence Yun, limited inventory has prevented some buying interests from being met, while affordability challenges "continue to hold back singings."
- The highest activity level occurred in the South and Midwest regions, respectively. The northeast region saw the lowest activity levels, followed by the West region.

10. HOUSING PERMITS AND STARTS

- Building permits fell 1.5% from March to April, registering a seasonally adjusted annual rate of 1.41 million homes in April, down from 1.43 in March, according to the Census Bureau. Permits are down 21.1% year-over-year.
- Housing starts rose 2.2% month-over-month in April to 1.40 million— up from 1.37 million. However, starts remain 22.3% below their April 2022 level of 1.80 million.
- Housing completions fell 10.4% in April to 1.37 million, down from 1.53 million. However, completions are 1.1% above their April 2022 level of 1.36 million.

SUMMARY OF SOURCES

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