RESEARCH BRIEF

Marcus & Millichap

FINANCIAL MARKETS

JULY 2023

Fed Resumes Rate Increases, Citing Core Inflation and Job Market Strength

Hiatus short-lived as Fed re-commences rate hikes. On July 26, the Federal Open Market Committee announced the first fed funds rate increase in nearly three months, raising the metric by 25 basis points to a lower bound of 5.25 percent. This follows a pause in June during which the target rate remained flat, as the FOMC chose to observe the impact of previous rate hikes in order to calibrate policy moving forward. The Fed called attention to the resiliency of labor markets during this span, with the U.S. adding a robust 209,000 jobs during the month of June as unemployment remained tight at 3.6 percent. The Fed acknowledged that while wage growth was not initially a major contributory factor to this inflationary cycle, some labor market softening would be necessary to bring annual price increases to 2.0 percent. Tight conditions also allow the FOMC maneuverability in regards to further rate increases; though if adopted, hikes are likely to proceed at a tempered pace.

Core, headline inflation notably decelerate in June. Last month the Consumer Price Index increased by 3.0 percent annually, the lowest gain since early 2021. This was largely driven by decreasing energy prices, which have been normalizing after sharply rising last year in response to geopolitical uncertainty. Core CPI — which does not take food and energy into account, and is the measure more closely watched by the Fed — remains somewhat higher. However, at 4.8 percent, June's increase was 50 basis points below the prior month's gain and 20 basis points lower than consensus forecasts. Although the latter metric is more of a determinant in Fed policy, the FOMC cited the important influence of the headline figure on inflationary expectations.

Fed re-affirms institution's data-dependent stance. As of late July, the Fed has increased interest rates 100 basis points since the start of the year. This is a notable deceleration from the 425-basis-point increase throughout the 2022 calendar year, and Chairman Jerome Powell stated the margin of rate hikes would lessen as the annual pace of inflation returned to the target level. Still, the FOMC did not give numerical guidance regarding policy decisions to be undertaken at September's meeting, indicating future rate hikes will depend on the cumulative macroeconomic conditions witnessed over the next two months.

Commercial Real Estate Implications

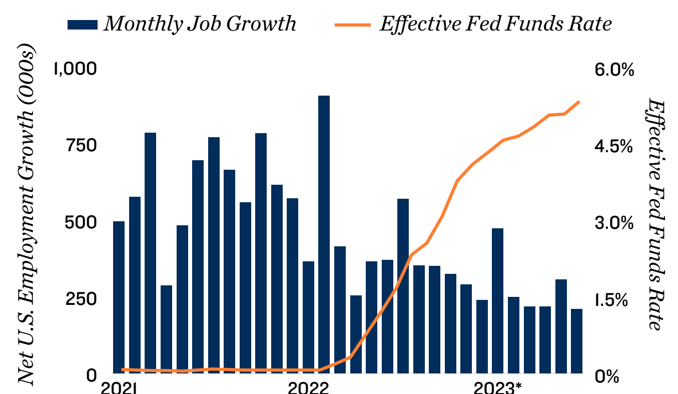
Labor agreements contribute to supply chain normalization. The Pacific Maritime Association and International Longshoremen and Dockworkers Union finalized contract negotiations in June, ending an 11-month long dispute that prompted intermittent work stoppages at West Coast ports. Logistics snarls were a notable inflationary factor in the wake of the health crisis, and the resolution of sector-specific labor disputes should help smooth supply chains moving forward. Similarly, United Parcel Services and Teamsters reached an agreement ahead of a July 31 contract deadline, averting a strike that would have dealt a blow to the economy and prompted inflationary effects.

Retail activity pulls back, despite robust labor market. Consumer spending increased just 1.6 percent in the second quarter, a marked deceleration from the 4.2 percent gain seen in the first three months of 2023. Headwinds may mount further in the year as the effects of recent rate increases become apparent. Slowing discretionary spending could also weigh on wage growth in the retail and hospitality sectors.

4.8% *June Core CPI Inflation*

4.4% *Year-over-Year Growth in Avg. Hourly Earnings*

Job Gains Robust, Despite Deceleration



** Through July 27, employment data through June*
Sources: Marcus & Millichap Research Services; Bureau of Labor Statistics; CoStar Group, Inc.; Federal Reserve; Moody's Analytics; Real Capital Analytics

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