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### Normalizing Rent Growth Points to Future Cooling in Core Inflation

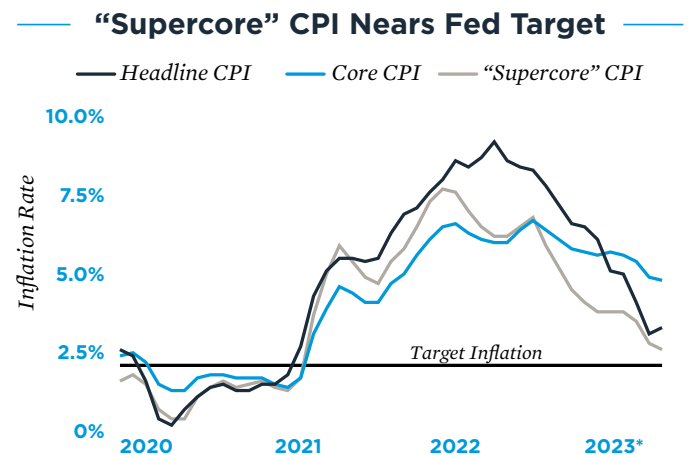
**“Supercore” CPI at favorable level.** The headline consumer price index increased by 3.2 percent year-over-year in July, trending up slightly from June’s 3.0 percent reading. Accelerated cost increases for food and some forms of energy ticked up the headline statistic for the first time since June 2022. While this could signal a bumpier inflation path ahead, market expectations for a continued CPI slowdown are anchored by a cooling job market and easing price pressures for most goods and services. Core CPI, which omits food and energy costs, slowed to 4.7 percent year-over-year in June, its lowest rate since October 2021. Further removing shelter from the measure, “supercore” CPI only lifted by 2.5 percent year-over-year. The housing component of inflation tends to be a lagging indicator that is expected to materially subside, reducing inflationary pressure.

**Housing data foretells lessening pricing pressures.** The shelter index, which tracks various housing costs, rose by 7.7 percent year-over-year in June and drove over 90 percent of last month’s CPI increase. The index tends to lag market conditions, however, with most residential leases only renewing on an annual basis. As a result, the shelter category could be echoing rent gains baked into current leases, inflating last month’s CPI metric. More recent data indicates rent growth for apartments is meaningfully slowing. Nationally, the average effective multifamily rent advanced by only 4.0 percent over the year ended in June, less than one-fourth of the 16.9 percent pace recorded at the same time in 2022. This downshift foretells a drawback in the index for shelter, which may help bring core CPI closer to the Federal Reserve’s target. While the Fed references core PCE inflation and not core CPI, both measures often move in close relation to one another.

**Relative affordability underscores long-term Class A prospects.** While slowing multifamily rent growth may suggest softer rental demand, the trend has been heavily influenced by record volumes of inventory that came online over the first six months of 2023. By the end of this year, supply-side pressures are anticipated to bring rent growth to nearly a decade-low. However, on a positive note, this cooling is emphasizing the relative cost benefit of renting an apartment as opposed to owning a single-family home. In June, the difference between the mean monthly Class A rent and the typical payment on a median priced home widened to \$663 per month, nearing a record high.

**Fed likely pauses in September.** Headline inflation has held under 4.0 percent for two months, and as pricing pressures have begun to normalize, consumer confidence and sentiment have broadly improved. The shift is an indicator of household formation, which was previously hindered by steep price jumps. Potential interest rate stability may also aid formations. Cooler inflation, paired with slower job growth, bolster market expectations that the Fed will hold the overnight lending rate flat in September. The likely benefit to household formation bodes well for multifamily properties, given persistent ownership challenges. Already in the first half of 2023, over 127,000 units were absorbed nationally on net, offsetting relinquishments from 2022.

**Steady lending rate will benefit retail sector.** A pause in September from the Fed would ease consumers’ borrowing costs, after the mean interest rate on credit cards rose to an all-time high in May. This could better enable shoppers to finance spending going into the holiday season, sustaining positive momentum in the retail sector. Core retail sales were up by 3.9 percent year-over-year in June, helping keep nationwide growth in asking rents at an above-average 3.0 percent.



\* Through July

Sources: IPA Research Services; Bureau of Labor Statistics; CME Group; Federal Reserve; RealPage, Inc.; The Conference Board; Moody’s Analytics



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