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FOMC Holds Rates Steady as Retail and Industrial Landscape Shifts

Fed maintains wait-and-see approach. The Federal Open Market Committee opted to not adjust the overnight lending rate at its June meeting, marking six months at a 4.25 percent lower bound. This decision indicates that the FOMC has a favorable view of both the current state of the labor market and inflation. The U.S. unemployment rate has held under 4.5 percent — around the level of full employment — for almost four years, while the total job count expanded 7 percent. Meanwhile, the year-over-year pace of headline CPI inflation has stayed in the mid-2 percent zone since March. Consumer activity, as measured by receipts at retailers, is also still climbing. Until these metrics show signs of worsening, the Federal Reserve is unlikely to adjust rates.

Sales metrics pose implications for retail properties. The pace of growth in consumer spending at physical stores has been slowing since March — up 2.9 percent year over year in May. Among retail categories, vendors of personal and health products have captured the most growth, with sales up 7.7 percent in that same span. This may bode well for unanchored strip centers, where many such establishments reside, including drug, beauty supply and eyeglass stores. Vacancy at such properties was at 4.8 percent in March, below where the rate was for most of the past two decades. Still, the overall retail sector got off to a slow start in 2025, recording the first quarter of negative net absorption since 2020. New space demand may lag later into the year; so far, retailers have announced more store closings than openings for 2025. Years of underdevelopment, however, have placed added emphasis on well-located floorplans, highlighting backfill potential.

Digital shopping tailwinds benefit industrial properties. Spending has risen at both physical and digital storefronts, but online sales have increased the most — up 8.8 percent year over year in May. E-commerce comprised 22.1 percent of total core retail receipts in April, which is 70 basis points below 2020's lockdown peak. Additional direct-to-consumer shopping underscores the need for distribution space. Although the overall industrial vacancy rate is rising this year after years of elevated development, it is advancing by the smallest margin since 2022, as total net absorption will pass 100 million square feet in 2025.

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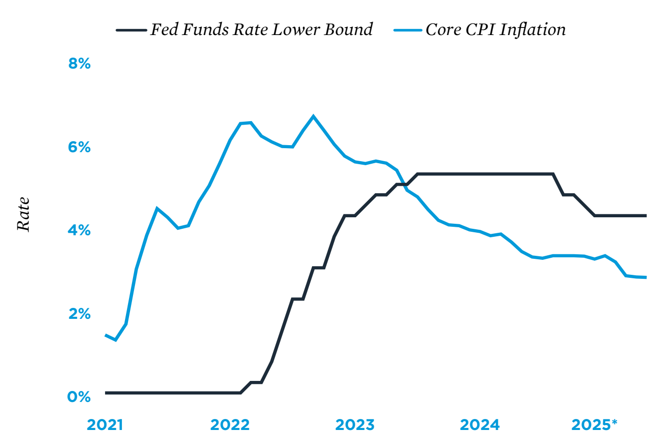
Results of tariffs yet to fully manifest. While U.S. trade policy is still evolving, a 0.3 percent year-over-year shift in Core Goods CPI in May suggests the end effect on prices has yet to be felt in domestic markets. An estimated effective tariff rate over 15 percent as of June will, however, have an impact on prices. Although the Trump administration is open to negotiation, few final resolutions have come to pass so far. As the upcoming June 23rd extension of the 50 percent steel and aluminum tariffs on derivatives such as household appliances illustrates, import taxes could also still climb higher.

Escalating conflict in the Middle East a further inflation risk. Iran exports about 1.5 million barrels per day of crude oil — capacity that could theoretically be replaced by OPEC. Even so, roughly 20 million barrels pass through the adjacent Strait of Hormuz daily. If relations erode to the point of interfering with that trade, it could have a profound effect on the global energy market. Yet a deescalation from here would result in only a modest, temporary price impact in the U.S.

4.25%
Federal Funds Rate Lower Bound

2.8%
Y-O-Y Change in Core CPI in May

Inflation Continuing to Slow



** Through June*

Sources: IPA Research Services; CoStar Group, Inc.; Federal Reserve; Moody's Analytics; U.S. Bureau of Labor Statistics; U.S. Census Bureau; Yale Budget Lab