Economic Update

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1. GDP

- Real GDP, which measures inflation-adjusted economic growth, increased at an annualized rate of 6.9% in Q4 2021, according to the advanced estimate released by the Bureau of Economic Analysis on January 27th. Q4's reading is 4.6% above the Q3 2021 estimate.
- According to the bureau, the increase in growth during Q4 is largely contributed to increases in private investment, exports, and consumption. Government spending decreased during the quarter, while imports, which have a negative effect on GDP numbers, increased.
- Retail and wholesale trade industries led private inventory investment, with motor vehicle retailers leading the pack. Both goods exports and service exports increased over the quarter. Within goods exports, consumer goods, industrial supplies, and materials, as well as food and beverage, led the increase. Service exports were led by increases in foreign travel expenditures.
- Healthcare, recreation, and transportation services led an increase in consumption, a notable trend given the relative growth of goods-consumption over service-consumption throughout much of the pandemic.
- Non-residential fixed investment also increased in Q4, led by an increase in intellectual property products.

2. FED HOLDS INTEREST RATES

- Federal Reserve officials held the Federal Funds rate unchanged during their most recent policy meeting on January 26th. Still, they indicated a willingness to conduct their first rate hike in March, citing a tight labor market and persistent inflationary pressures.
- In arguably his most hawkish signals to date since the COVID-19 pandemic began, Fed Chair Jerome Powell stated that officials no longer felt that monetary support was needed to sustain the rapidly recovering economy. Powell noted that "the committee is of a mind to raise the federal funds rate," assuming that conditions hold during the FOMC's March meeting.
- While Powell stopped short of suggesting how many rate hikes could come in 2022, he noted that the pandemic recovery and expansion have been very different from past recoveries— most notably the high inflation levels and stronger growth rate. He stated that markets should expect upcoming policy decisions to reflect this reality.

3. STOCK MARKET VOLATILITY

- The stock market has recently experienced increased volatility as markets pay close attention to the timing and scope of the Federal Reserve's anticipated rate increase. On January 24th, the S&P500 fell as much as 4% during trading before bouncing back into positive territory. Markets experienced similar

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swings throughout the week as investors digested statements from Fed policymakers indicating a more hawkish stance on monetary policy.

- Tech stocks have suffered some of the steepest losses through the week, with the tech-heavy Nasdaq 100 underperforming all major indices on January 26th.
- According to a tally by Bloomberg, more than $5 trillion has been wiped out from stock values this year. While markets have generally anticipated a monetary tightening cycle beginning this year, most projections were in the range of two-to-four rate hikes by year's end. However, since Chair Powell's statement earlier in the week signaled his belief that the Central Bank should no longer need to support the economic recovery with accommodative rates, market forecasts have risen to an average of five rate hikes in 2022.

4. MORTGAGE RATES

- The Mortgage Bankers Association reported that the average rate on a 30-year mortgage jumped for the fourth consecutive week to 3.64% during the week ending January 14th. This is the highest rate on the 30-year mortgage since March 2020.
- In recent weeks borrowing costs have climbed as bond markets react to the likelihood of monetary tightening by the Federal Reserve in the coming months.
- On the one hand, the rise in costs has come with a refinancing drop-off. However, as prospective homeowners look to lock in lower rates in anticipation of higher rates on the horizon, lenders have noticed an increase in home-purchase loan applications. According to MBA, home-purchase applications rose 7.9% during the week ending January 14th. Refinancing applications dropped by 3.1%— its lowest mark in over two years.

5. EVOLVING DEMOGRAPHICS OF THE APARTMENT MARKET

- A recent study by MetLife Investment Management analyzed the evolving demographics that are likely to shape the future of apartment demand in the US. In their report, researchers indicated an anticipated 11 million new households will be formed in the US between now and 2030.
- Separate from the cyclical factors observed during the pandemic, the analysis predicts several longer-term structural factors that have and may continue to exert upward pressure on residential prices and rents in the coming years. An immediate standout is the low rate of new construction experienced over the past decade. According to the report, the US housing stock ticked up just 0.3% each year from 2010 to 2020 compared to a 1.4% average annual increase between 1980 and 2010.
- Demographically, aging Baby Boomers and family-forming Millennials stand out as the cohorts likely to fuel apartment rents over the coming decade. Baby Boomers are increasingly less likely to live their

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senior years in retirement communities than previous generations, which is already impacting available housing supply but may also contribute to rent inflation as homeowning responsibilities become burdensome for aging households. Aging Millennials who also face increased financial constraints in student debt and low savings are also likely to contribute to rent pressures, particularly in single-family rentals.

- Further, remote workers will also increase rent costs as they migrate away from the urban centers and sort into communities that more fit their living preferences.

6. OFFICE DEMAND

- The VTS national Office Demand Index (VODI) finished the year at 58 in December, representing a decline of 33% since August and the fifth straight month of deterioration. The metric represents current Office demand as a percentage of a 2018-2019 benchmark to help quantify the effects of COVID-19 on the sector.
- VTS notes that declines were due to some leveling off after pent-up demand led to a surge in the index in 2021, culminating in a reading of 87 in August 2021. The decline in the year's closing months could also be related to pandemic-driven economic and health concerns. The December drop in demand was less than expected before the pandemic. Demand fell 2-to-3 times more in December 2018 and 2019 than it did in 2021.
- Each metro that VTS produces data for has seen office demand decline from its 2021 peaks. In 2021, peak-to-current declines ranged from 30.8% in Seattle to 50.5% in Washington DC. This translates into the December metro-level VODIs showing demand as low as 33 in Boston and as high as 72 in Seattle.

7. INDEPENDENT LANDLORD RENTAL PERFORMANCE

- Research by Chandan Economics suggests that the on-time collection rate for independently operated residential properties was 80.7% in January, up slightly from December's rate of 80.1%. The improvement puts the on-time collection rate about one percentage point below the 81.7% seen in March 2020 – the last full month before the start of the pandemic. On-time collection rates have improved for three consecutive months.
- On-time collection rates in the Sun Belt region have underperformed the rest of the market of late. The first estimate for January 2022 shows on-time collection rates average 79.3% in the Sun Belt compared to 80.6% outside of it. Due to rapid migration and strong economic fundamentals, local property markets are generally strong in the Sun Belt. Still, rising rents could also be pressuring existing tenants to adjust to a new equilibrium.
- On-time collection rates in single-family rentals averaged higher than other property types in recent

months but dipped by 93 basis points (bps) month-over-month to 79.4% in January's first estimate. Notably, other property types' on-time collection rates are trending up. On-time collection rates have improved for five straight months in small multifamily properties and three months in a row for 2-4 unit properties. In January's first estimate, both property types had on-time collection rates averaging just under 81%.

8. UNEMPLOYMENT CLAIMS

- For the first time in four weeks, initial jobless claims fell from the week prior, an early signal of the Omicron variant's fading effect on labor markets.
- During the week ending on January 22nd, seasonally adjusted initial claims were 260k, 30k less than the previous week. However, the 4-week moving average for initial claims rose by 15k, settling at 247k.
- Continuing unemployment claims, which measures all non-first-time applications, rose by 51k to 1.64 million during the week ending January 15th, the latest week of data availability.
- While the federal government and most states have sunset extended unemployment benefits that were available during the pandemic, New Jersey and New Mexico still have supplemental benefits available.
- Notably, in December, first-time unemployment claims fell to their lowest level in over 50 years, indicative of a tight labor market where employers who typically make job cuts following the holiday rush are retaining workers amid a persistent labor shortage.

9. NEW RESIDENTIAL CONSTRUCTION

- According to the Census Bureau's latest report, building permits for privately-owned housing units rose by 9.1% month-over-month in December to a seasonally adjusted annual rate (SAAR) of 1.87 million. This is 6.5% above the December 2020 rate.
- Notably, real estate tax changes enacted in Philadelphia, PA, for residential projects permitted after December 31st had the effect of pushing up averages in the Northeast region. Permits issued in the region rose by 112% from November to December.
- From November, housing starts rose 1.4% to a SAAR of 1.7 million in December. This is 2.5% above the December 2020 rate of 1.66 million housing starts.
- Completions fell 8.7% from November to December to an estimated SAAR of 1.3 million. This is 3.9% below the December 2020 rate of 1.38 million completions.
- Overall, roughly 1.33 million housing units were completed in 2021, 4.0% above the 2020 figure of 1.29 million.

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10. INCREASED SOFR ACTIVITY

- According to recent reporting by Bloomberg and documented activity at the Chicago Mercantile Exchange, futures activity surrounding the Secured Overnight Financing Rate (SOFR), the industry's replacement for the historically used LIBOR rate, has increased in recent weeks as speculation increases over the Federal Reserve's policy plans.
- According to the CME Group, SOFR open rates have climbed to a record 2.27 million contracts, roughly 20% of total Eurodollar volume. Daily, SOFR versus Eurodollar activity has risen from 10% in October to above 30% at the beginning of January.
- SOFR, like LIBOR, is meant to serve as a benchmark interest rate for dollar-denominated loans. The transition to SOFR is expected to increase long-term liquidity but also result in substantial short-term trading volatility in derivatives markets.

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SUMMARY OF SOURCES

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