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COMMERCIAL REAL ESTATE SERVICES

Q3 2023 ECONOMIC REPORTS

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GDP GROWTH
EMPLOYMENT
MONETARY POLICY
GLOBAL ECONOMY

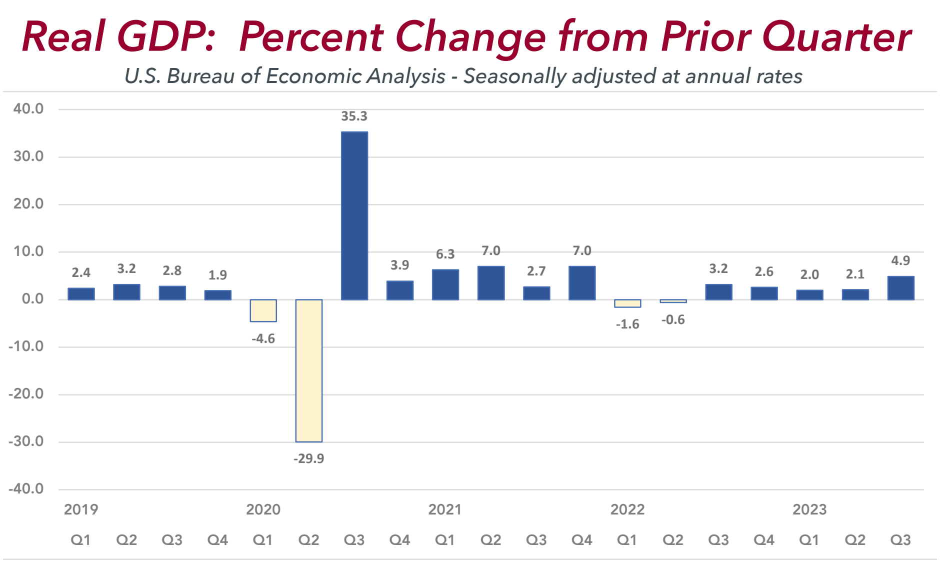
GDP GROWTH: TRENDING IN Q3 2023

The U.S. economy grew faster than expected in the third quarter and the most in nearly two years, fueled by strong consumer spending in spite of higher interest rates, inflation pressures and other domestic and global headwinds.

Gross domestic product, a measure of all goods and services produced in the U.S., rose at a 4.9% annualized pace from July through September, more than double the 2.1% pace of the second quarter, the Commerce Department said.

The economy accelerated despite the Federal Reserve's commitment to slow growth and inflation by raising its benchmark short-term interest rate to about 5.4%, its highest level in 22 years.

Meanwhile, core inflation has eased sharply from its recent peak in June 2022. The Commerce Department said prices – excluding volatile food and energy categories – rose an annualized 2.4% in the third quarter, only modestly above the Fed's 2% target. But there are warning signs underlying the surprising Q3 numbers. Americans saved less and their incomes, adjusted for inflation, fell over the summer. That could mean the pace of spending will ease in coming months. Business investment also stalled.



Consumer spending gained 4% for the quarter after increasing just 0.8% in Q2.

The summer's strong performance showcased the economy's stamina. Growth could slow in the fourth quarter because of the United Auto Workers strikes, the resumption of student loan repayments by millions of Americans, the lagging effects of the rate hikes and rising geopolitical tensions. Long-term interest rates, wars in Ukraine and Middle East, and possibility of a partial government shutdown also could cause cracks to emerge. The sharp increase in GDP came due to contributions from consumer spending, increased inventories, exports, residential investment and government spending. Economists had been expecting a 4.7% increase. The GDP increase marked the biggest gain since the fourth quarter of 2021.

A buildup in inventories also supported the third quarter's economic expansion, contributing more than one percentage point to growth. Government expenditures, meanwhile, rose 4.6% over the summer. Consumer spending gained 4% for the quarter after increasing just 0.8% in Q2. Gross private domestic investment surged 8.4% and government spending and investment increased 4.6%. Spending at the consumer level split fairly evenly between goods and services, with the two measures up 4.8% and 3.6%, respectively.Residential investment defied the trend and rebounded in the third quarter after contracting for nine straight quarters.

According to a report from the Fed, Americans, as a whole, began the year on healthy financial footing. The net worth of a typical household jumped 37% from 2019 through 2022. Home prices soared, and the stock market rose in the biggest surge on record dating back more than 30 years. At the same time families benefited from the unusually low interest rates from the pandemic recession of 2020 until late last year. The typical household – defined by the Fed as midway between the richest and poorest – paid 13.4% of its income to cover interest on debts, the lowest rate on record.

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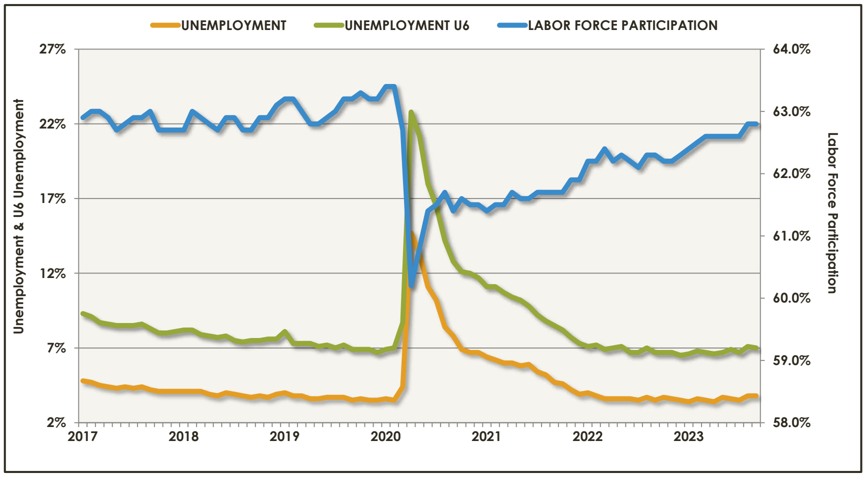
EMPLOYMENT: TRENDING IN Q3 2023

The U.S. job market demonstrated its resilience in the third quarter even as the Federal Reserve continued to pump the brakes on the economy. September nonfarm payrolls grew by 336,000, the most in eight months and exceeding expectations. Job growth data for July and August were revised upward. More jobs were added in the third quarter compared to the second. The unemployment rate was unchanged and near its 50-year low.

Employment has been a focus of the Federal Reserve. In its efforts to reduce inflation, the central bank has been raising interest rates to slow economic and wage growth. A recession was widely expected in 2023, but hiring remains strong and third-quarter GDP was 4.9%, the most in nearly two years. Meanwhile, the rate of core inflation fell to 4.1% at the end of Q3 from a post-Covid peak of 6.6% a year ago. The Fed's target rate is 2%. "Like most reports, the Fed will find things to like and dislike here. Inflation data will weigh heavily" ahead of the Fed's next meeting, said Andrew Patterson, Vanguard senior economist.

September's gain, the 33rd consecutive monthly increase, is the largest monthly jump since January. It is significantly more than August's net increase of 227,000 jobs, which was revised up by 40,000 from initial estimates. Job growth at the height of summer was stronger than initially thought. In addition to August's revisions, July's gains were revised up by 79,000 to 236,000.

United States Unemployment



'Like most reports, the Fed will find things to like and dislike here' – Andrew Patterson, Vanguard senior economist.

The job growth occurred across all major sectors. Leisure and hospitality helped drive job growth higher with 96,000 jobs added. That exceeds the pace of 61,000 jobs a month the sector posted during the past 12 months, according to the BLS report. Government jobs also saw a hefty boost in September, rising by 73,000.

Healthcare added 41,000 jobs in September, compared with the average gain of 53,000 over the prior 12 months. September employment continued to trend up in ambulatory health care services with 24,000 positions, hospitals 8,000, and nursing and residential care facilities 8,000.

Social assistance added 25,000 jobs in September, about the same as the average monthly gain of 23,000 over the prior year. Employment in transportation and warehousing changed little at 9,000. Truck transportation added 9,000 jobs, following a decline of 25,000 in August largely due to the sudden bankruptcy of trucking company Yellow Corp. Air transportation added 5,000 jobs in September.

Employment in professional, scientific, and technical services increased by 29,000 in September, in line with the average of 27,000 over the prior 12 months. Wage growth cooled. September's increase is the lowest since February 2022, showing that the Fed's tightening is having an effect. In September, average hourly earnings for all employees on private nonfarm payrolls rose by 7 cents, or 0.2 percent, to $33.88. Average hourly earnings rose by 0.2% in September, bringing the annual gain to 4.2%, according to the Bureau of Labor Statistics. That lands below projections from many analysts for a monthly uptick of 0.3% and annual increase of 4.3%.

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MONETARY POLICY: TRENDING IN Q3 2023

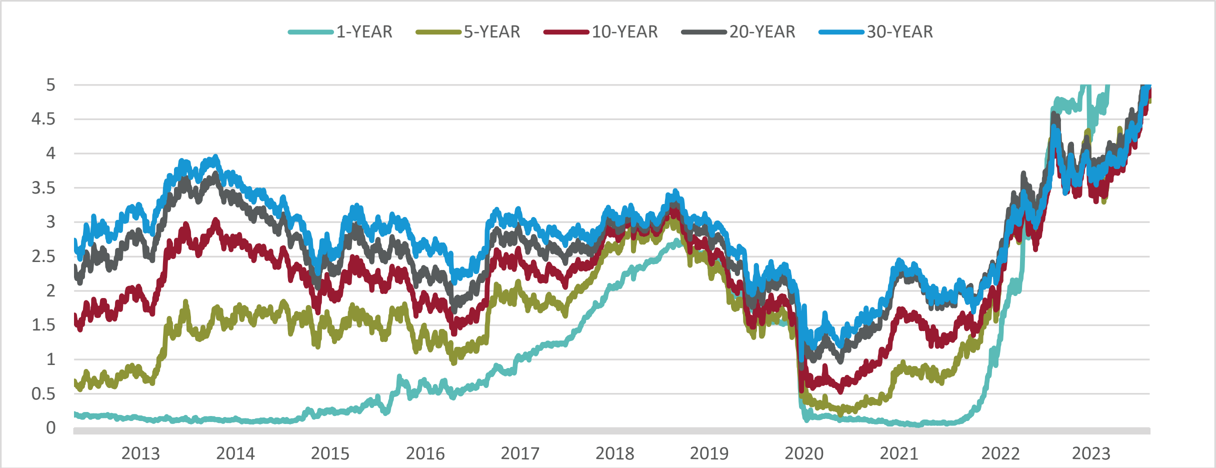
The Federal Reserve declined to raise interest rates at its regularly scheduled September meeting but Federal Reserve Chairman Jerome Powell held out the possibility of another rate hike by the end of the year. To reduce inflation, the Fed has raised rates 11times since early 2022. There is a growing sense at the central bank that the economic slowing it has sought could produce a "soft landing" or, at the worst, a garden-variety recession.

The federal funds rate today is set at a range of 5.25% to 5.5%, its highest level since early 2001. The Federal Open Market Committee will make interest rate decisions in early November and again in mid-December. It's unclear when the central bank will begin cutting rates.

The Fed's current rate policy is a dramatic shift from its easy money stance dating back to the financial crisis of 2008. Over much of that period, including 2020 and 2021, the federal funds rate was set to a range of 0.00% to 0.25%. In March 2022, as inflation surged, the Fed shifted course and rapidly raised rates throughout the remainder of 2022 and into this year.

The Fed also retained its commitment to reversing its Covid-era policy that involved purchases of Treasurys and mortgage-backed securities to ensure ample liquidity to meet the demands of capital

Daily Treasury Yield Curve Rates (Decade Trend)



markets. The Fed has trimmed its balance sheet of those assets from a peak of nearly $9 trillion in April 2022. This tightening combined with higher interest rates was aimed at tempering inflation by slowing economic growth through higher borrowing costs. Since early 2022, the Fed's balance sheet declined to roughly $8.1 trillion, down 9.6% from its peak, but still sizable by historical standards.

The main challenge the Fed seeks to correct is the sudden, rapid rise in the cost of living. Headline inflation, as measured by the Consumer Price Index, peaked at 9.1% for the 12-month period ending in June 2022 before dropping steadily over the course of a year. The CPI stood at 3.7% for the 12-month period ending in August 2023. Inflation still exceeds the Fed's target long-term rate of 2%.

The job market has been a key measure the Fed uses to help it make determinations on monetary policy. Unemployment remains below 4% and the number of available jobs, while in decline, still greatly outpaces the number of unemployed workers.

Recent reports show that compensation for workers rose 4.3% for the 12 months ending in August 2023, little changed from recent trends. Fed officials are aiming to slow wage growth further because higher wages feed into higher demand for goods and services, contributing to higher prices.

"Without price stability, the economy does not work for anyone," Powell said following the September meeting at which the central bank reaffirmed its commitment to fighting inflation. He added that core inflation – a key measure of living costs that excludes the volatile food and energy sectors – remains well above the headline CPI number of 3%.

GLOBAL ECONOMY: TRENDING IN Q3 2023

Elements of the global economy have improved this year but the conflict between Israel and Hamas appears certain to inject renewed volatility into the markets reminiscent of the commodity chaos that followed Russia's invasion of Ukraine early last year.

"Geopolitical tensions are the real economic risks now and we are all aware of that," said French Finance Minister Bruno Le Maire, at a meeting hosted by the International Monetary Fund in Morocco immediately after Hamas' attack. "Any escalation in the region would, of course, have a significant impact on global growth."

Total global trade is set to grow only 0.9% this year as the IMF expects a sharp drop from 5.1% growth last year. The IMF is concerned that slowing global trade could usher in an era of deglobalization with national security driving economic policy of nations rather than growth. Geopolitical conflicts such as Russia's invasion of Ukraine – and friction between the U.S. and China – have already upended supply chains. Supply disruptions not only slow growth but also have prompted investors to factor in more future risks from potential geopolitical shocks, helping drive up interest rates.

Persistent inflation continues to vex global central banks and investors. The IMF boosted its inflation

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European Union GDP Annual Growth Rate

The IMF is concerned that slowing global trade could usher in an era of deglobalization.

forecast for next year to 5.8%, up from its previous forecast of 5.2%. For most nations, the IMF doesn't expect price growth to return to targets set by central banks before 2025.

Strong U.S. economic data, including September's strong hiring report, helped send Treasury yields to 16-year highs while many investors bet the Federal Reserve would keep interest rates elevated. The IMF this week boosted its growth projections for the U.S. economy, now forecasting 2.1% growth this year and 1.5% next year, a sign of "a softer landing than earlier expected."

Global officials fear rising interest rates and a stronger dollar could usher in a new wave of debt distress across the developing world. The strength of the dollar is already making it more expensive for emerging-market countries to service dollar-denominated debts. The rise in interest rates makes it harder for them to issue new debt to fund themselves and refinance bonds coming due.

"It's a burden on very-low-income countries with a lot of debt without a lot of fiscal space," Treasury Secretary Janet Yellen said in an interview. "These countries are already hurt by higher food prices, higher energy prices—spillovers from Russia's war against Ukraine." There are warnings that rising debt costs are threatening vulnerable countries' ability to spend on climate-change projects. According to the IMF, nearly 60% of low-income countries are in, or at risk of, debt distress, a classification that signifies a country can't meet its debt obligations

"Many of these countries have already lost access to market financing and so their ability to finance even the most basic public spending needs is limited," said Vitor Gaspar, director of the IMF's fiscal affairs department.

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