

### Inflation Remains Services-Driven as Essential Spending Guides Real Estate Demand

**Tariff pass-through absent for now, but services remain sticky.** May's CPI report reflected a modest increase in prices. Headline inflation rose 0.1 percent month over month, bringing the annual rate to 2.4 percent. The data suggests price pressures from tariffs have yet to pass through to consumers; Core Goods CPI stayed flat in May and the year-over-year rate held at just 0.3 percent. Apparel and vehicle prices continued to decline slightly month over month, indicating prior inventory buildup has, for now, allowed businesses to absorb cost increases without raising prices. Meanwhile, services inflation remained the primary driver of headline CPI, rising 0.3 percent month over month and 3.6 percent year over year. Categories such as insurance and medical care are still posting modest increases, stressing the persistence of structural cost pressures within the broader economy.

**Regional inflation trends reinforce shifts in multifamily demand.** Inflation continued to diverge geographically in May, with coastal markets experiencing more persistent price pressures. Annual CPI reached 2.8 percent in the Northeast and 2.7 percent in the Pacific region, compared with 2.4 percent in the Midwest, 2.0 percent in the South and 1.7 percent in the Mountain West. This disparity may further reinforce out-migration from high-cost coastal cities to more affordable Sun Belt and Midwestern metros. While tight supply should support rent growth in coastal areas, mounting consumer strain could begin to limit pricing power. Improving migration trends may aid rent performance in the Southeast and Mountain West. The Midwest is well-positioned for continued strength, as limited development activity is helping sustain 4.1 percent annual rent growth as of March.

**Travel price declines pressure budget hotels.** Airline fares and hotel rates continued to decline in May, pointing to softer global travel demand and weakening discretionary spending. Airfares fell 7.2 percent year over year, while the hotels and motels category declined 1.7 percent. This trend has weighed most heavily on limited-service hotels, where growth in average daily rates and occupancy remain muted amid mounting financial pressure on lower-income households. In contrast, the full-service segment has posted steadier performance, supported by business travelers and more affluent guests.

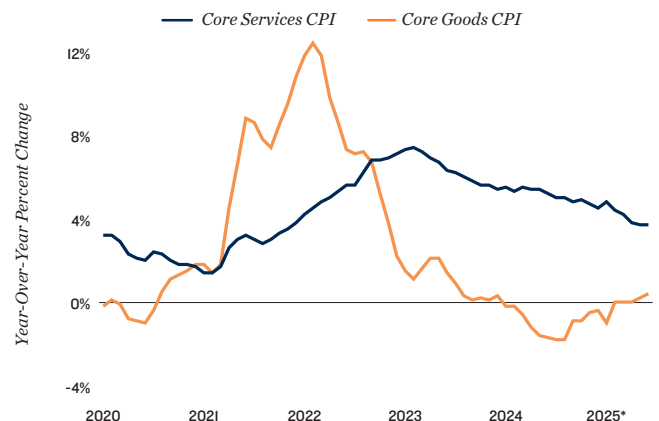
**Health care demand supports medical space uptake.** Medical care inflation remained elevated in May. Prices for medical equipment and supplies rose 0.9 percent month over month, while costs for hospital and nursing home services also continued to increase. Given the relatively inelastic demand for health care services, providers may encounter less resistance when passing along higher costs to patients. This pricing power may help uphold leasing activity across health care-related real estate. In the first quarter of 2025, both the medical office and senior housing sectors recorded their highest quarterly gross absorption totals since mid-2022.

**Pet and day care tenants fuel growth in service retail.** Retail spending in the personal care category rose 8.5 percent year over year in April, outpacing subcategories like pet service and day care, which saw a 4.9 percent and 5.6 percent increase in prices, respectively, in May's CPI data. This steady demand growth underscores sustained interest in increasingly essential services, assisting leasing at neighborhood and service-oriented retail centers. Tenants such as Wag N' Wash — planning 25 new locations in 2025 — and expanding private school operators like Montessori programs are driving demand for space.

**2.4%** Increase in Headline CPI Year Over Year

**2.8%** Increase in Core CPI Year Over Year

#### Core Services Elevated, Goods Remain Tepid



\* Through May

Sources: Marcus & Millichap Research Services; Bureau of Labor Statistics; CME Group; CoStar Group, Inc.; Federal Reserve; RealPage, Inc.



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