CUSHMAN & WAKEFIELD

TRUMP: IMPACT ON THE U.S. ECONOMY & THE PROPERTY MARKETS

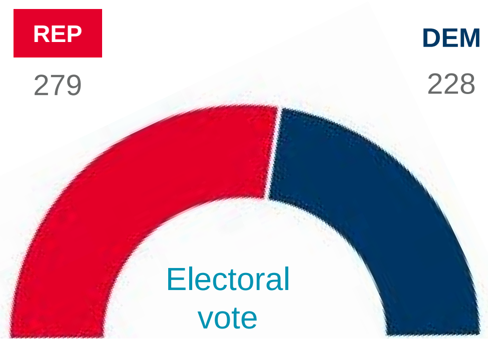
How will the new president impact the economy and commercial real estate?

November 2016

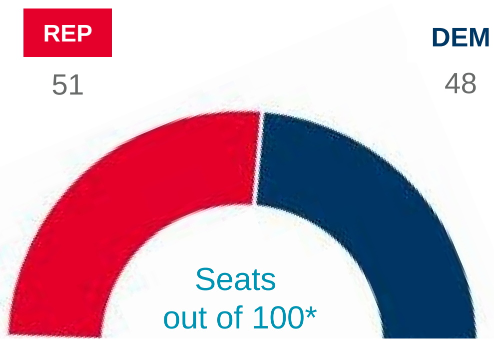
U.S. Makes Hard Turn to the Right

Summary of the election results

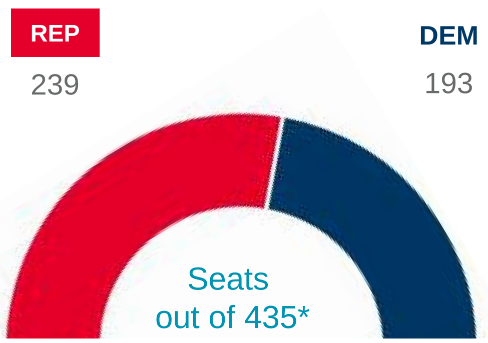
President



Senate



House



*Runoff for the seat in Louisiana will be held in December

Republican candidate Donald Trump was elected the 45th president of the United States. The Republicans also maintained control of both chambers of Congress and control the governor's office in 33 states.

Elections and Commercial Real Estate

It's the economy stu…

The Election

- The election of Donald Trump as president of the United States surprised most observers.
- He is backed by Republican majorities in both the House and Senate.
- Will his agenda have an impact on commercial real estate?
- **Yes and No**
- Over the next few months, the change in the White House is unlikely to have a significant impact on property market conditions. It will take many months before the Trump Administration can enact legislation and implement policy.
- In the longer term, the policies that are enacted will have an impact on the U.S. economy and commercial real estate. Positive impact next two years, unclear further out.

History

- Elections that have resulted in a president of a different party taking the White House (1992, 2000, 2008) have generally not led to any immediate changes in property market fundamentals.
- In 1992 the commercial real estate sector was in the midst of a major correction that began in 1990 and lasted until 1995. The election did not change market trends.
- In 2000 commercial real estate markets did become materially weaker not long after the new administration was sworn in, but this was caused by the bursting of the dot-com bubble, not by any policies implemented by the new president.
- In 2008 commercial real estate markets were declining from a peak reached in early 2008 and continued to do so as the "great recession" unfolded.

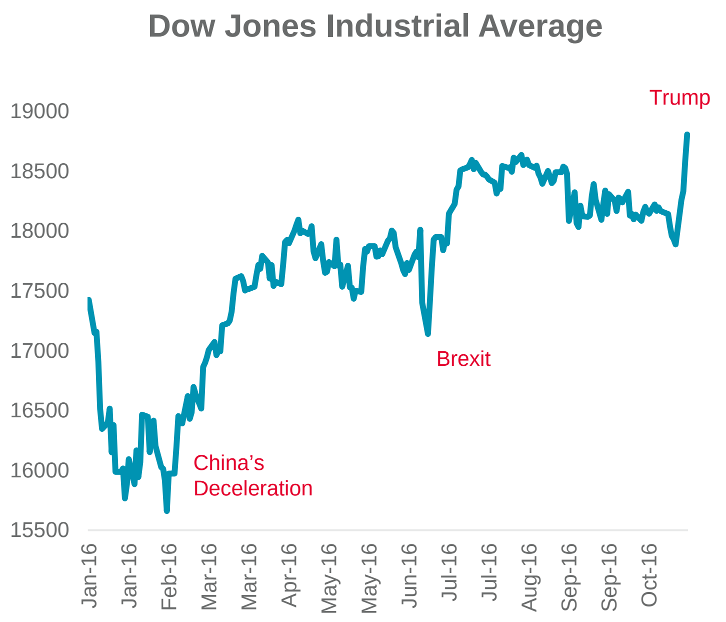
It's the Economy……

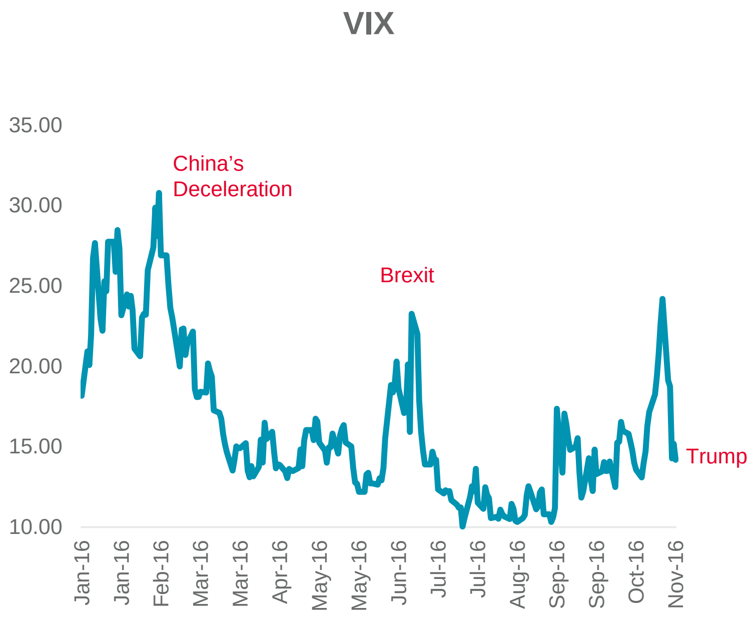
- Economic conditions are a far more important driver of commercial real estate markets. The condition of the economy can be impacted by policies enacted in Washington, and that will eventually work its way into commercial real estate markets.
- But it's important to remember that, with very few exceptions, the way an administration affects commercial real estate is through the impact of its policies on the economy.

The consensus is that Trump policies, if enacted, will likely support stronger economic growth and improving property market fundamentals in the near term.

The Market's Initial Reaction

Not what was expected

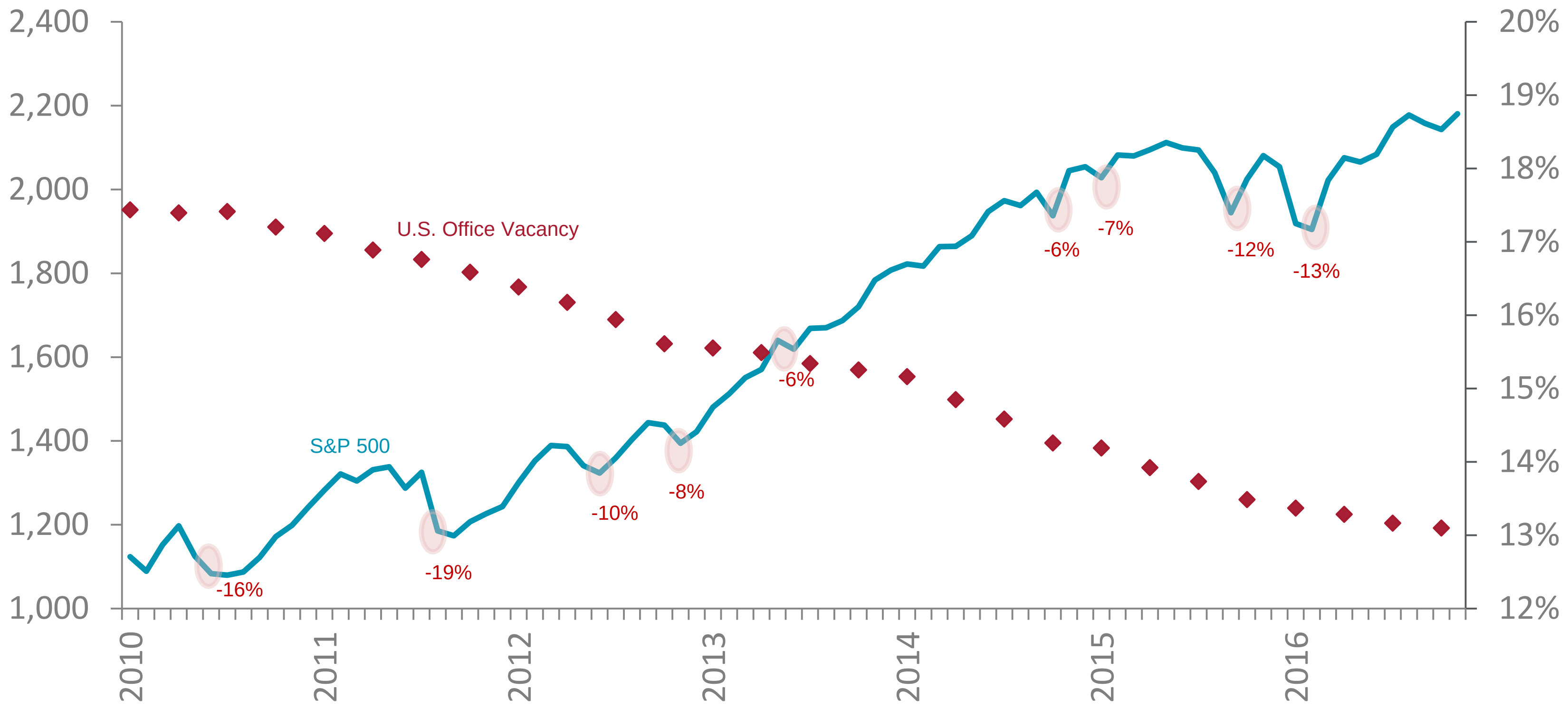




Financial markets have reacted in a manner almost opposite to what had been expected. Of most importance to commercial real estate will be the behavior of the bond market going forward.

CRE Is Not the Stock Market

S&P 500 movements vs. U.S. vacancy rates



The property market fundamentals are rarely influenced by daily movements in the equity markets. There have been nine stock market corrections in the current cycle and demand for real estate space has remained healthy and has not deviated from pre-correction trends.

Source: S&P Dow Jones Indices

HOW MIGHT POLICY CHANGE?

Tax Policy

"Greatly simplify the code"

TAX REFORM PROPOSALS

- Reduce corporate income tax from 35% to 15%
- Top income tax brackets reduced from 39.6% to 33%, number of brackets from 7 to 3
- Repeal the estate tax and eliminate the alternative minimum tax
- Advocate for a one-off 10% tax rate on repatriated corporate earnings

Assessment

- Would constitute a major near-term fiscal stimulus, likely boosting GDP and business profits
- Most estimates suggest tax cuts would reduce government revenue by $5 trillion over the next decade

Impact on commercial real estate

- A stronger economy supports a stronger commercial real estate market. Job growth is likely to remain healthy, continuing to fuel demand for office space.
- Faster income growth is also likely to boost retail and industrial demand.
- Capital gains tax stability takes away the threat of a major increase and may lead to more property sales in 2017.

Changes in tax policy are likely to be favorable for commercial real estate. However, implementation of these changes will take time as Congress and the administration work out the issues.

Regulation

"Bureaucratic red tape and Washington mandates are not the answer"

REGULATION POLICIES

- Dismantle Dodd-Frank law
- Repeal and replace Obamacare
- American energy dominance declared strategic priority

Assessment

- Dodd-Frank – unlikely to be repealed in total, but likely a win for the financial sector and the banks
- Obamacare – still unclear, but likely to create uncertainty for health insurance industry; could increase demand for pharma due to decreased regulations
- Energy policy changes – likely a win for the oil and gas industry

Impact on commercial real estate

- After lagging for years, the financial sector is likely to go into stronger growth mode
- Demand for medical office could slow, but demand from pharma and biotech companies will likely pick up
- Energy producing markets should benefit from loosened policies but oil supply glut and stronger U.S. dollar will remain headwinds

A change in the regulatory environment will likely be a net positive for the commercial real estate markets in the near-term as the proposals are more focused on loosening lending conditions and fostering stronger economic growth.

Government Spending

PROPOSALS

- Spend $1 trillion on infrastructure over 10 years, much of it privately funded
- Eliminate the sequester on defense spending (boost troop levels, number of ships, aircrafts, and bolster missile defense system)
- Eliminate government waste and budget gimmicks

Assessment

- Spending increases to improve highways, bridges, tunnels, airports, schools, hospitals
- Eliminating sequester would amount to $500 billion of increased defense spending over 10 years
- Unclear how the increase in government spending will be paid for and could result in increased budget deficits

Impact on commercial real estate

- Most U.S. property markets will benefit from improvements in local infrastructure
- After years of fiscal austerity, defense agencies and contractors will enter growth mode
- If spending increases are not matched by revenue gains, expect higher deficits and upward pressure on interest rates

Trump's spending plan amounts to fiscal stimulus in the near-term. Many cities will benefit from increases in infrastructure spending as will the manufacturing sector through improved intermodal network. Cities with strong defense spending component (DC, Northern VA/MD, Baltimore, Sacramento, San Diego) will also benefit.

Trade & Globalization

"Negotiate fair trade deals that create American jobs"

PROPOSALS

- Halt new trade deals like the Trans-Pacific Partnership
- Enforce existing trade treaties more strictly
- Potentially renegotiate existing treaties like NAFTA
- Strengthen U.S. stance against currency manipulation

Assessment

- This is one policy area where the impact is generally seen as a negative in the near-term
- If enacted in full, U.S. trade is likely to decline both imports and exports
- Likely to slow job outsourcing but also likely to increase inflationary pressures

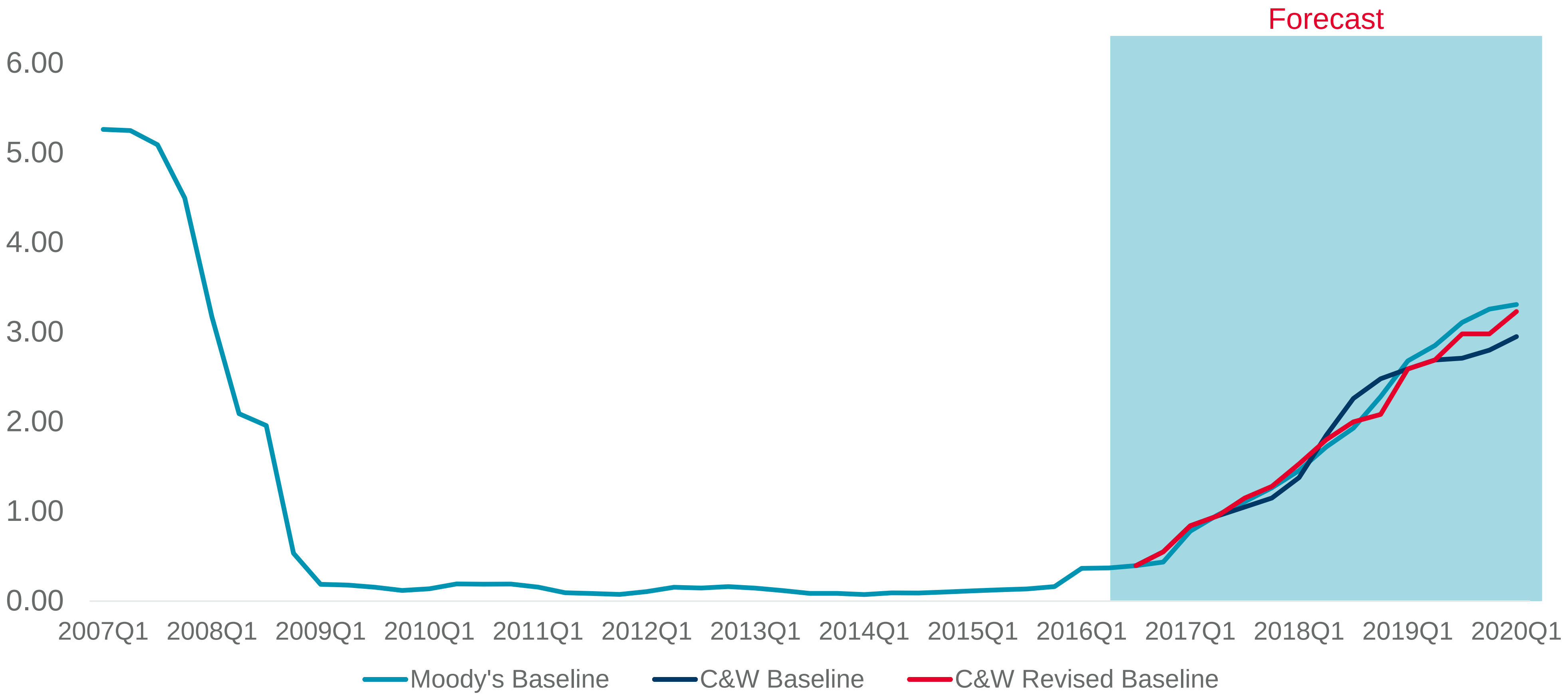
Impact on commercial real estate

- Generally, way too early to say. But if enacted…
  - Industrial port cities could be most negatively impacted in the near term by reduced trade flows
  - Protectionist policy could trigger trade wars which would hit U.S. exports and potentially drag down global growth
  - Benefits of globalization would be decreased – likely resulting in higher inflation and interest rates

Restricting trade has historically had a negative impact on economic growth. Industrial port cities and trade hubs would likely be the most negatively impacted. Certain U.S. manufacturing businesses could benefit from decreased global competition, but Trump's trade policies, if enacted, are likely a net negative for the U.S. property markets overall.

Trump's Impact on Monetary Policy

Fed funds rate



As of November 15, Fed futures implied a 94% probability of a December rate hike. Given Trump's stronger fiscal stimulus policies along with unemployment and inflation near the targets, the Fed may decide to raise rates at a quicker pace. Core pricing could come under pressure, but debts markets will welcome the upward move in rates bringing in a stronger leveraged buyer.

Possible Winners

Defense – Significant spending increases for defense programs; sequester eliminated; after several years of fiscal austerity government defense contractors go into growth mode

Retail – Tax cuts put more money in consumer's pockets which boosts spending across the board, eCommerce and Bricks and Mortar all benefit

Energy – Prices are set globally, but less regulation helps energy-producing regions; Keystone XL reinstated; regions impacted: Gulf Coast, shale regions in upper Midwest, Western PA

Manufacturing – More demand for products comes from stronger economy; import competition may be reduced, but supply chains don't change overnight; keep your eye on the U.S. dollar.

Financial services – Deregulation boosts opportunity; higher rates boost margins; look for more employment in this sector

Construction – Infrastructure, infrastructure, infrastructure; also, stronger U.S. economy boosts spending on commercial development

Technology – Stronger economy = stronger consumer demand for new technology; internet of things; sharing economy; Cloud; data analytics; repatriation of overseas profits also likely to benefit tech companies

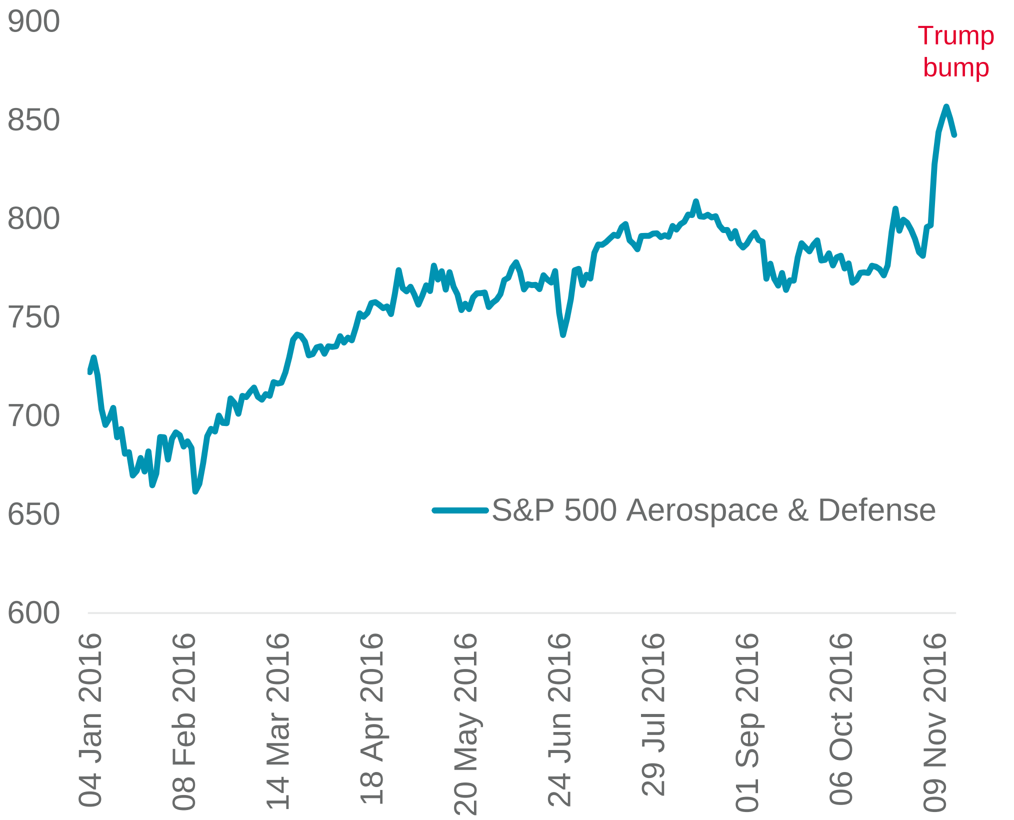
Pharmaceutical – Affordable Care Act (ACA) revisions, less scrutiny of prices and costs; this industry was headed for price regulation, that is now off the table

Social Media – The Twitter presidency; alternative media outlets become more mainstream

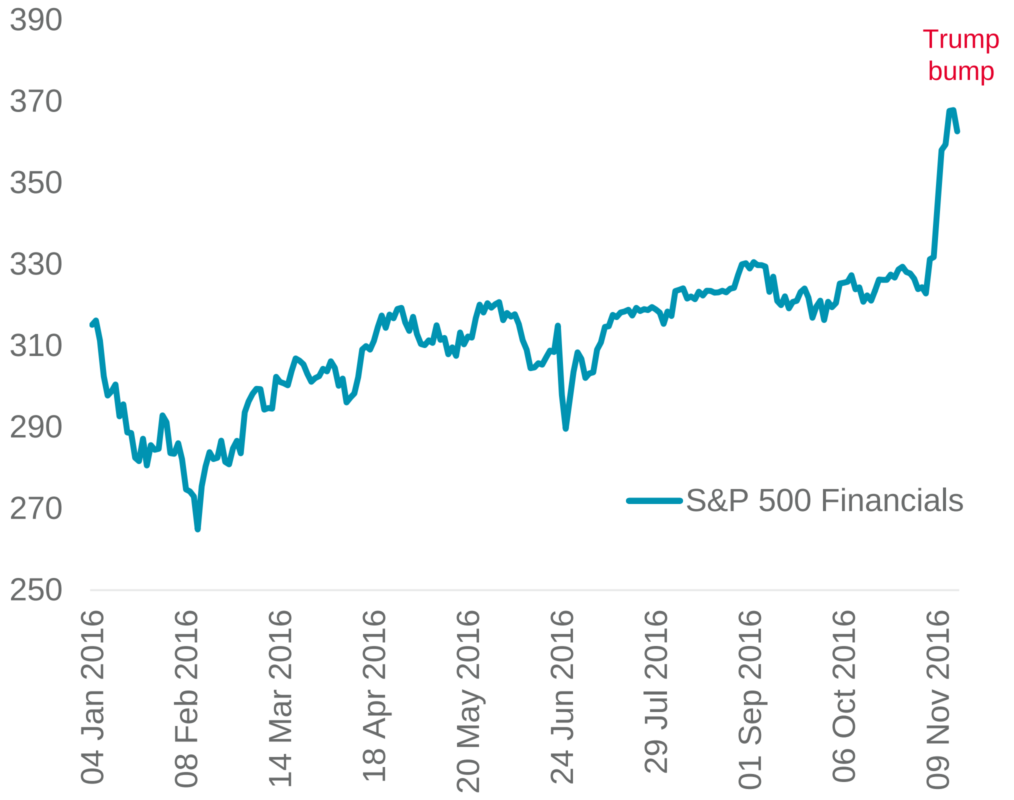
Biggest Winners

The market signaling these sectors will grow under Trump

Aerospace & Defense



Financial Sector



Possible Losers

Non-defense agencies – To fund defense and infrastructure spending increases, non-defensive agencies will likely come under increased budgetary pressure

Utilities – Higher interest rates make utility yields less attractive (this is more a valuation play than a comment on the industry outlook)

Healthcare – Having just totally changed its delivery and pricing model to adapt to ACA, now the industry faces the possibility of more changes, resulting in lack of stability

Housing sector (mixed) – Rising mortgage rates slow demand, but less regulation could lead to greater availability of credit; aging Millennials and increased household formation also likely to drive stronger demand for homes

Auto sector – After two very strong years a pull back is likely; rising interest rates trigger slowdown but stronger consumer keeps sector healthy

Alternative Energy – Fewer subsidies and incentives; push to revive coal production

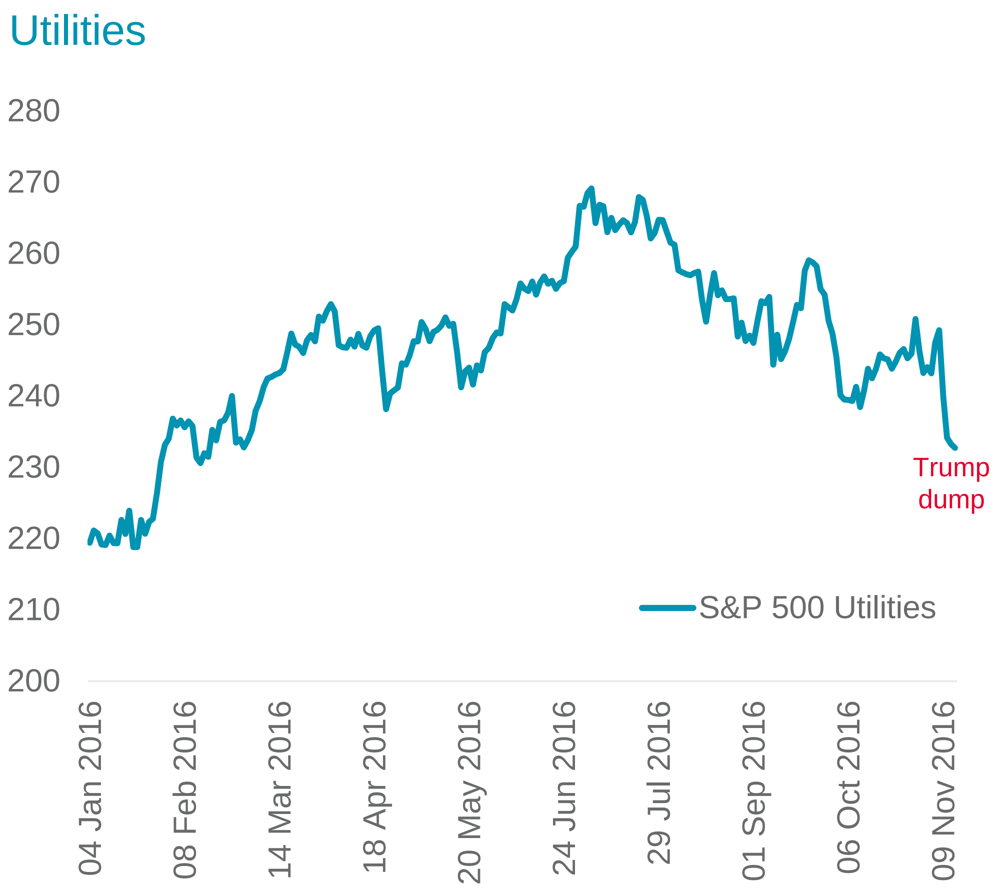
Port Cities – Trade policy threatens to reduce imports and exports; won’t happen overnight

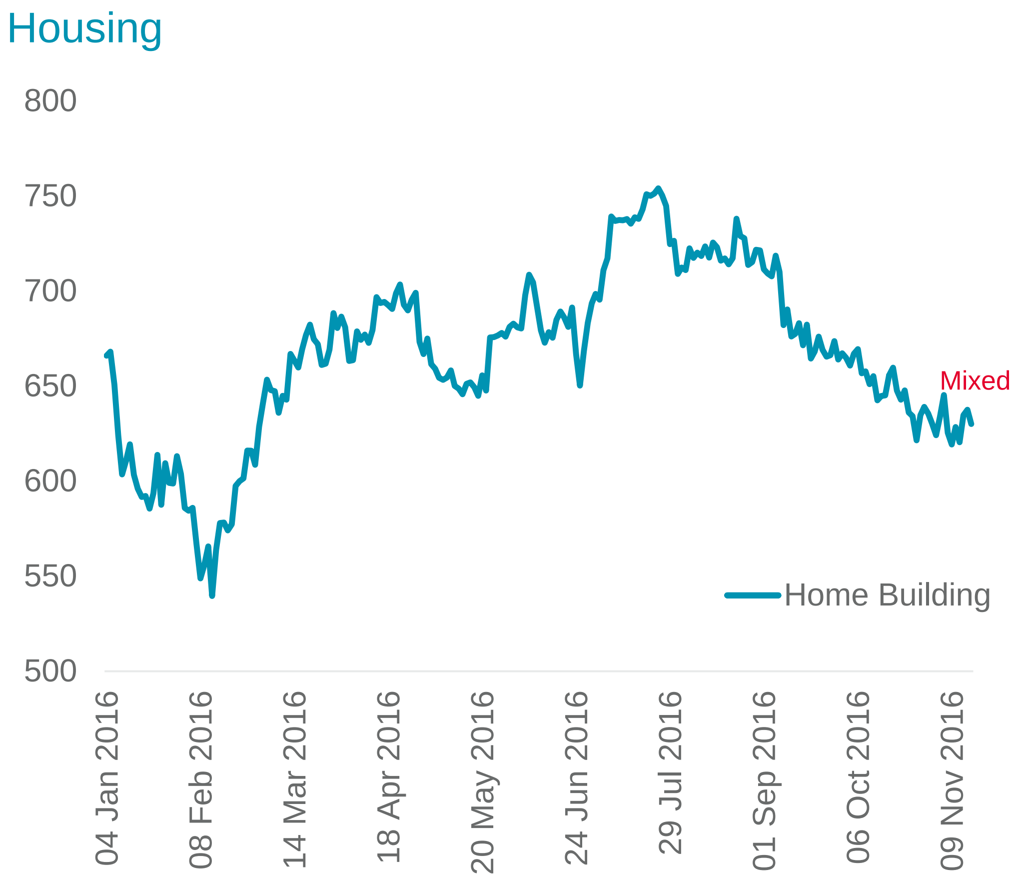
Border Cities – Any location that relies on transient migrant workers could experience labor shortages depending on immigration policy

Mainstream Media – This president is less dependent on mainstream media; more competition than ever from web-based streaming content and social media

Biggest Losers

The market signaling these sectors will shrink under Trump





Early Market Signals for Various Sectors

Signals from the market that these sectors will grow/shrink under Trump

S&P 500 Sectors	Before Trump	After Trump				
	07 Nov 2016	08 Nov 2016	09 Nov 2016	10 Nov 2016	11 Nov 2016	14 Nov 2016
Utilities	248	249	240	234	233	233
Information Technology	796	800	798	785	789	775
Energy	511	510	518	520	511	513
Transportation	546	550	559	568	570	579
Pharmaceuticals	721	721	761	771	757	754
Homebuilding	496	487	487	496	494	503
Financials	367	367	382	396	399	408
Industrials	530	533	547	559	561	565
Consumer Discretionary	579	581	584	586	591	592
Consumer Staples	568	571	563	548	547	546
Health Care	819	820	847	857	845	843
Telecommunication Services	155	156	158	154	154	153
Aerospace & Defense	835	836	870	888	896	903
Building Products	492	507	512	524	520	522
Airlines	325	328	333	337	340	349

Better after Trump | Similar | Worse after Trump

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