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TRUMP 2.0 & IMPLICATIONS FOR PROPERTY

NOVEMBER 2024

Establishing Perspective

Former President Donald Trump won the 2024 presidential election and will become the 47th President of the United States on Inauguration Day, January 20, 2025. The Republican party will take control of the White House and Congress, a full sweep which implies that policy has the potential to change more than it would have under either a Harris presidency and/or a divided Congress.

The policies poised for change encompass a wide range of macroeconomic influences, including regulatory conditions, fiscal (spending and tax) policy, trade policy, and immigration policy. Some of these will have a more immediate impact (for example on the financial markets or trade), but others have a more lagged impact on the economy and financial markets and are therefore more likely to influence leasing fundamentals and the capital markets down the road.

Apart from the natural lag of policy influence, the fact remains that many of the changes to policy have the potential to exert offsetting forces on macroeconomic growth and inflation, which means that there is no easy, or clear-cut diagnosis for what the outcome of this election means for property performance. Moreover, the magnitude, timing, scope and details to policy changes ahead are unknown.

As a result, we feel it is most important to establish a strong framework for contextualizing and interpreting the implications of policy changes, as opposed to making rushed, premature and/or abrupt changes to our economic and commercial real estate (CRE) outlook. Accordingly, we have outlined a synthesized view of “positives” and “negatives” that are unfolding in the wake of the election.

Market Positives

Positive factors that immediately reduce near-term volatility/uncertainty:

- **Eliminating a social unrest scenario:** A contested, protracted election could have created social unrest, violent protests, riots and prolonged uncertainty. In this scenario, the U.S. might have been perceived as a country in chaos, potentially leading to financial market volatility. Fortunately, this grim outcome was avoided.
- **Debt ceiling risk is mitigated:** The U.S. is on track to hit its debt ceiling in January 2025. Under a Harris and/or divided Congress scenario, the markets faced elevated risk that policymakers might not raise the debt ceiling limit, which would have introduced elevated near-term uncertainty and financial market volatility. With a Republican-controlled Congress, this risk has been greatly mitigated.

Positive factors that influence medium-term growth and positively influence near-term market sentiment:

- **Fiscal stimulus means household finances and corporate profits get a boost:** President-elect Trump floated several tax policy ideas on the campaign trail, including extending the expiring Tax Cuts and Jobs Act (TCJA) for individuals, restoring the deduction for state and local taxes (SALT), and reducing the corporate tax rate from 21% to as low as 15%. Extension of the TCJA appears most likely at this point, and with Republicans in control of Congress, additional tax cuts may also be forthcoming. However, it is unclear to what degree Congress will weigh deficit impacts as they craft the extension.

- **Fiscal stimulus means corporate growth prospects build as corporate bond and equity markets gain momentum:** Lowering the corporate tax rate, by definition, will translate into higher after-tax corporate profits, assuming all other factors remain constant. Stronger corporate profits also correlate with an increased demand for real estate space, as businesses enjoy enhanced cash flow enabling them to make strategic investments. This includes hiring more employees and investing in their owned and leased real estate portfolios. As equity markets grow, the wealth effect continues to take shape, leading consumers to feel better about their finances. This newfound confidence promotes increased consumer spending, which in turn fuels further economic growth.

- **Corporate credit spreads have tightened:** Since President-elect Trump's victory, credit spreads (i.e., the difference between corporate bond yields and Treasuries) have narrowed by 16 basis points (bps) since October 30 and by 40 bps since the peak in July 2024. Currently, Baa corporate bond spreads are at their tightest level since just prior to the Great Financial Crisis (GFC). This tightening has occurred, at least in part, because investors have renewed confidence in the prospects for corporate earnings, which are expected to improve on the back of lower taxes and fiscal stimulus to consumers. Improving corporate earnings prospects may also increase investor conviction and interest in corresponding corporate bonds, thereby lowering the required risk premium to hold corporates over risk-free Treasuries. From a property perspective, it's important to note that investment grade corporate bond yields are an important proxy for CRE debt spreads and the required yields in the CRE equity market. Investment grade corporate bonds are ultimately viewed as risk adjacent to CRE, and their relative spreads to Treasuries and overall yields can impact CRE credit spreads and CRE portfolio fund flows. Financial markets have, thus far, taken the election in relative stride. Risk spreads widened just ahead of the election but have since tightened after the markets recognized that election conditions were at least broadly settled.

- **A wave of financial deregulation is anticipated to roll back Biden-era policy:** President-elect Trump and the Republican Congress are expected to reverse a significant amount of Biden-era regulations, affecting a wide range of sectors, including financial services, energy, technology and housing. This wave of anticipated deregulation has already sparked a significant comeback for bank stocks, which have soared post-election. Pressure to further water down Basel III is highly likely.

- **Many real estate and housing-related policies will be protected as regulatory momentum working against real estate and housing will pause and likely reverse:** President-elect Trump has shown clear intention of rolling back regulations on both the financial services (which includes hedge funds and private equity investors) and housing sectors, while also reducing corporate taxes. His administration is likely to preserve existing policies that support the CRE investment industry. This includes: 1) potentially reducing capital gains taxes, 2) supporting existing 1031 exchange benefits, and 3) supporting tax provisions that allow carried interest to be taxed as capital gains as opposed to ordinary income. He also advocates for free-market rents, contrasting with the Biden administration's policy that supported the removal of accelerated depreciation if landlords raise rents by more than 5%, which could have significantly deterred/altered multifamily investment. Trump has also alluded to a housing plan featuring several policies that could spur the supply-side. As part of this plan, he floated the possibility of opening federal lands for housing, while also suggesting he would reduce regulatory barriers that impact homebuilders. This approach aims to improve supply and alleviate housing shortages and costs. A more supportive orientation of the federal government to CRE will likely drive more capital to the sector at large, especially by comparison to a Harris administration that planned to keep many of the Biden-era policies in place.

- **Early rumors of a return-to-office (RTO) mandate for federal workers would be a jolt for office utilization nationwide (if it were to occur):** Rumblings on the street have percolated suggesting that President-elect Trump might utilize his executive powers (via executive order) to require all federal employees to return to the office. Although this remains largely speculative, his efforts on this front would align with previously championed initiatives like the USE IT Act and the SHOW UP Act focused on return-to-office policies for federal agencies. Should these intentions be pursued, a rise in office occupancy rates would follow as federal employees return. Such legislation would also have a ripple effect on related sectors such as lobbyists, contractors, and consultants, likely boosting their in-person presence to stay close to decision-making hubs. In addition to positively impacting the structural-use case for office properties in markets with significant exposure to federal employment, like Washington, DC, such mandates could also have influence on other non-federal (state- and local-level) government jobs that span across all major markets throughout the country. Furthermore, the private sector, already trending toward more in-office attendance, will likely continue this trend given the new tone set in Washington, DC.

Market Negatives[1]

Factors that negatively impact medium-term growth (and inflation), as well as dampen near-term market sentiment, include:

- **Tariffs could contribute to a one-time shock to inflation:** President-elect Trump has suggested that he will impose 10% across-the-board tariffs on all trading partners, with a 60% tariff imposed on China. While it's still difficult to discern what was merely rhetoric during the campaign and what might have served as negotiation tactics with trade partners, it is worth noting that Trump had promised 35% tariffs on Mexico and 45% tariffs on China during the 2016 campaign—commitments that ultimately never materialized. At that time, Trump demonstrated a willingness to shift his policy stance in response to market reactions, anticipating the potential fallout on investor sentiment. Accordingly, he took a much more surgical approach on tariffs during his first term; average effective tariffs went from 1% to just 2% (of total federal revenues). Despite tariffs, CPI inflation remained near 2% throughout Trump's first term. It remains uncertain whether he will adopt a surgical approach to tariffs during his second term, or if he will impose tariffs at the suggested high levels. The timing for implementing such tariffs is also unclear. Whereas immigration policies and fiscal stimulus could eventually be more inflationary, Powell described tariffs as being a one-off level shift rather than a more stubborn inflationary force. Higher tariffs could exacerbate the inflationary dynamics that arise from fiscal stimulus, as they have an offsetting effect on inflation by curtailing labor force growth and curbing economic growth. As a result, the cumulative, collective impact of some of these policies on the economy and on inflation will be somewhat mitigated. This could be further complicated by any retaliation, as many of his touted policies would violate the World Trade Organization's 'most favored nation' status protocols.

- **A potentially more patient Fed:** Inflation is likely to experience upward pressure given Trump's various policy positions. However, it is still early days, and we should not jump to conclusions prematurely given that we do not know the degree or timing with which the new Administration may adopt policy positions mentioned on the campaign trail. While Powell didn't directly acknowledge the election during his post-Federal Open Market Committee (FOMC) press conference in November, it is evident that the path of Fed easing has been tempered. Regardless of the election results, Powell reiterated that the Fed plans to proceed with caution and deliberation, considering the ongoing recalibration and balancing of their policy mandate on both fronts. The futures market has caught on—as of November 13, it was predicting one fewer 25-bps cut next year compared to the Fed's most recent Summary of Economic Projections (dubbed the 'Dot Plot'). The markets

1 Negatives are, of course, mentioned with the context of influence on the macroeconomy and CRE performance. We remain sensitive to the fact that some of these policies lead to positive outcomes elsewhere.

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are still placing a 70% probability of another 25-bps cut at the December meeting. Whether or not the Fed cuts in December, they will likely utilize the meeting to provide markets with additional forward guidance and reassurance of their intention to remain independent. The December 2024 FOMC meeting will also provide a fresh Dot Plot update, which provides a valuable, real-time lens into FOMC officials' views of the path ahead for inflation, economic growth and monetary policy. By providing such forward guidance, the Fed will have ample time to prepare the markets, thereby helping to reduce any potential bond market volatility that would come from near-term monetary policy.

- **Fed independence becomes a topic of conversation rather than a given:** President-elect Trump has expressed his belief that Presidents should have a say in decisions made by the FOMC. It's unclear what "having a say" means in practice and seems unlikely the Fed will not maintain its independence. Economists widely agree that independent central banks are critically important for maintaining price stability, which is proven out in empirical research. In addition to undermining the Fed's influence in maintaining price stability, any further rhetoric around the Fed's lack of complete independence stands to add to market concern, volatility and uncertainty. As has been the resounding case over the last two years, the Fed emphasized its patience during the post-November FOMC meeting. Powell again reiterated that the focus will remain on balancing both sides of the policy mandate as opposed to making premature assumptions about the path of fiscal and trade policy ahead.

- **Upward pressure on neutral policy rates:** If anything, potential changes to immigration and other fiscal policies are likely to influence the Fed's forward-looking view of the neutral policy rate as opposed to influencing near-term, immediate policy response. Indeed, the Fed's median view of neutral rates has been rising over the course of the year, from 2.5% to 2.9% as of September. If inflation or inflation expectations accelerate, the Fed will likely pause cuts in the back half of 2025. So far, inflation expectations remain grounded, but it's an indicator the Fed will be carefully watching.

- **Interest rate volatility will remain, along with upward pressure on the 10-year Treasury:** The Fed's 75 bps of cumulative cuts were already priced into the bond markets. Apart from some of the volatility from the election, the 10-year Treasury yield (US10Y) had been trending between the high 3% range and the low 4% range. More recently, the presidential election added volatility, with the US10Y trending up 60 bps from where it stood at the end of October to 4.4% as of Friday, November 15. Looking ahead, the long end of the yield curve is likely to remain sticky, above 4%, given the implications of protectionism, higher deficit spending and immigration policy on inflation. Rising government debt could also require more Treasury issuance at higher yields to attract investors. The US10Y, however, is influenced by many factors, including monetary policy, relative demand for U.S. bonds, growth and inflation expectations, and the strength of the U.S. dollar, to name a few. We are still assuming the US10Y will hover in the 4% to 4.5% range, but there is now upside risk here.

Factors that adversely affect longer-term growth (and inflation), while also dampening near-term market sentiment, include:

- **More restrictive immigration policies that curb immigrant inflows would stem the economy's potential growth:** President-elect Trump is expected to impose more restrictive immigration policies that will ultimately reduce the inflow of immigrants. Yet, certain macroeconomic jargon is essential to properly frame this discussion: immigration has been an important source of labor force growth over the last few years, a period that has witnessed the strongest growth in nearly 20 years. Labor force growth is viewed as a key determinant toward an economy's ability to reach its full potential, so strong immigration (that leads to labor force growth) is generally viewed as a net positive for economic growth by most economists. That said, it's important to recognize that the implications of tighter immigration policy will influence the labor market gradually over time, rather than causing sudden changes.

- **Deportations could add to social unrest and disrupt specific industries, while adding upward pressure on labor costs:** President-elect Trump indicated his intention to deport undocumented immigrants; however, the scope of this plan remain unclear, including how it would be enforced and funded. Larger scale deportations would reduce the labor force and exert further upward pressure on labor costs, particularly in sectors like construction where immigrants comprise an outsized share.

- **The New Department of Government Efficiency (DOGE) could translate to isolated agency-related cuts, but the impact on markets with a strong federal presence is unclear:** President-elect Trump has recently appointed Elon Musk and Vivek Ramaswamy to head up a new department focused on the efficiency of government spending. Though this could result in the downsizing of the federal workforce, the outcome largely depends on the focus of the new program in identifying inefficiencies and the appetite of Congress to enact proposed changes. For example, if DOGE primarily targets superfluous and duplicative programs, the impact on Washington, DC may not be that significant. If history is any guide, Washington, DC's office sector often gets a boost under unified government as policy momentum builds and organizations seek proximity to the legislative process. Moreover, the return of federal workers to the office, along with government contractors, may yield a net positive impact on the fundamentals of Washington, DC's office sector, even if some shrinkage to the federal workforce were to occur.

Bringing it all Together: Implications for CRE Performance

The economy faces undeniable uncertainty heading into the first half of President-elect Trump's upcoming term, and we don't expect interest rate volatility to dissipate. The degree to which the economy, inflation and the financial markets are impacted depends entirely on the scope of policies adopted, their timing, magnitude and detail. We know that Trump and his advisors intend on making sweeping changes to certain policies. However, history has shown that Trump has shown a willingness to shift his stance based on the reactions of investors and financial markets, as evidenced by his approach to tariffs during his first administration. The willingness to adapt to protect financial market sentiment and the economy suggests that policies may be moderated from their campaign-trail proposals.

Ultimately, the economy is entering this next chapter with remarkable underlying strength and resilience, underpinned by a historically strong foundation. New policies are likely to shift the pace and inner workings of economic growth rather than undermine or threaten it entirely. As we've laid out above, it's important to recognize that no single governmental policy will take effect in a proverbial macroeconomic vacuum. Many of these policies will create both *positive* and *negative* pressures on the economy, financial markets, and CRE sector. The underlying strength of the economy against these forces helps to provide the contours of a still-resilient economic outlook ahead.

While it is premature to shift our house view forecasts just yet, the most prudent course of action is one of reflection. We will continue to carefully hone our outlook as President-elect Trump and his advisors provide more post-election and post-inauguration guidance to the markets and as policy changes take shape. In the meantime, we can emphasize a few key pillars that will shape our perspectives and the outlook ahead:

- **History as a guide:** Historic trends have proven that CRE can perform well under various political scenarios (see the chart on the next page which features annual CRE transaction volumes, distinguished by White House and Congressional controlling party).

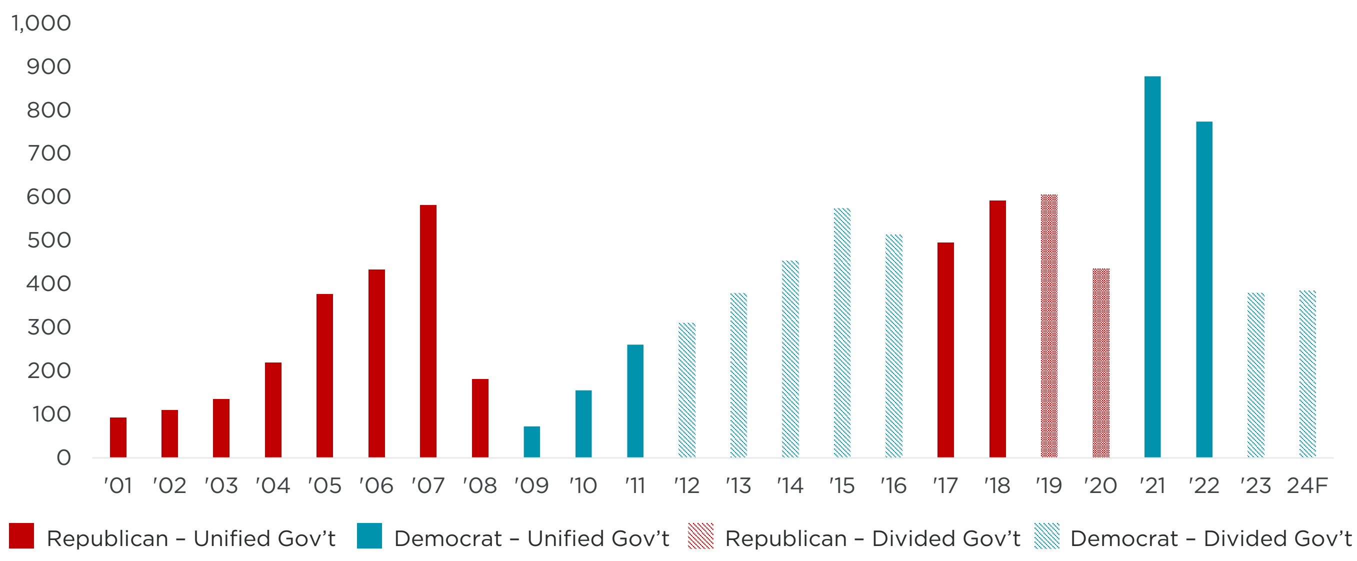
- **30,000-foot level:** The state of economy, interest rates, supply/demand dynamics, return on capital relative to other asset classes, and many other factors are all important in gauging how property will perform in any given quarter, year and into the future. We tend to focus more on the macroeconomic environment, financial market and the fundamentals backdrop to explain CRE performance because it can take upwards of one to two years for fiscal policies to form following an election, let along filter thought into real economic and CRE dynamics.

- **Keeping the long view:** Given the lagged impact of elections on macroeconomic conditions, it is typically imprudent to fundamentally change one's real estate strategy in the wake of elections. Investment managers and property managers are trusted by institutional capital sources to remain fiduciaries of capital and property, which implies that they are expected to keep focus on the medium- and long-term and not isolated periods, election or otherwise.

- **Momentum is still building:** Regardless of the volatility and uncertainty arising from the election, it is important to maintain a balanced perspective along with a solid understanding of the foundation upon which we stand. The Fed's two initial rate cuts have still infused much-needed optimism throughout the marketplace, helping to usher in the next phase of the capital markets recovery. Above and beyond the symbolic influence on sentiment, a less restrictive monetary policy loosens broader financial market conditions. This shift fosters improved and more fluid conditions for both CRE leasing and capital markets. Prospects for a soft landing are also still coming into focus, which implies a stronger outlook for NOI growth and improved conviction for businesses, investors and lenders.

- **Yield curve normalization implications for CRE:** While the pace of easing may be slowing, the reality remains that the Fed is still in an easing mode. As the yield curve continues to flatten and eventually uninverts, capital will naturally and gradually start to shift out of the short end of the curve and into longer-dated instruments in pursuit of better yields. *This natural and logical rotation out of the short-end of the curve into the longer-end will help to ignite more demand for longer-term investments like CRE from both debt and equity providers.* This underscores our view that the CRE capital markets will continue to gain traction, driven not only by improved rate visibility and the loosening of financial markets and debt conditions, but also by the flattening and uninverting of the

U.S. Elections: Weak Correlation to Property
Sales volume, $bils.



Source: MSCI Real Capital Analytics, Cushman & Wakefield Research

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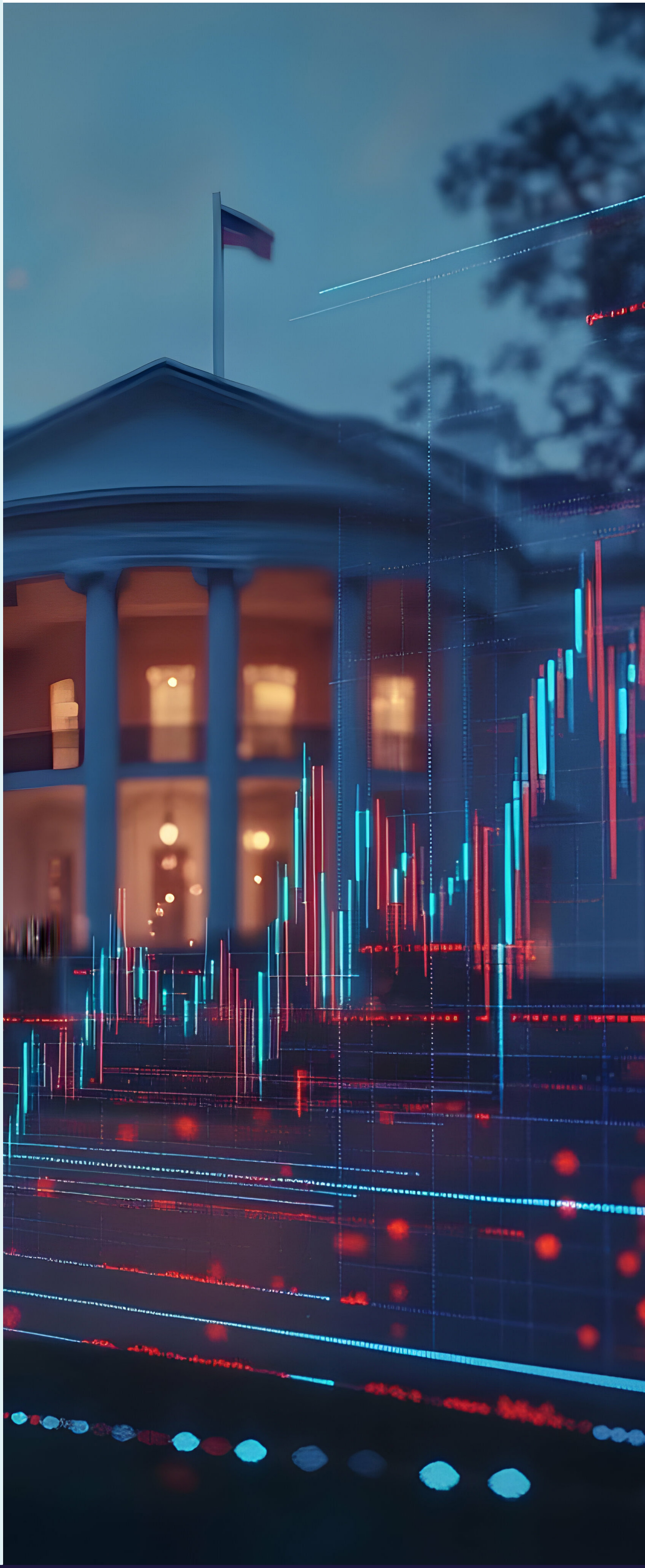

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