Election impact

March 2017

Economic and market implications of a Trump presidency

Companies across most industry sectors are eagerly anticipating pro-business reforms, including a reduction of the corporate tax rate, deregulation and a repeal of sequestration.

- Plans to cut taxes and ease regulations may spur growth across a variety of private-sector industries.
- Proposed spending increases to defense and infrastructure projects should boost the government contracting segment.
- Fiscal austerity throughout other branches of government, uncertainty over foreign trade and a pullback in immigration pose potential risks.

In the first 100 days since Donald Trump was elected 45th President of the United States, major stock market indexes have soared to all-time highs and business and consumer confidence have surged to their highest levels in over a decade. Companies across most industry sectors are eagerly anticipating pro-business reforms, including a reduction of the corporate tax rate, deregulation and a repeal of sequestration. The stock market is generally considered the most forward-looking economic indicator and a strong predictor of future company earnings, hiring growth and leasing demand, thus recent activity is likely to have a lasting impact on real estate markets.

The return of single-party alignment between the Executive and Legislative branches promises a period of swift action on Capitol Hill. Under gridlocked government over the past six years, legislative progress has fallen by 43%, with the number of bills signed into law reaching an all-time low. Over this span, a government shutdown and fiscal uncertainty created headwinds across both the public and private sectors.

Political alignment under the 115th Congress may bode well for the U.S. office market. Broad support for defense and infrastructure spending and a repeal of sequestration for programs related to defense and public safety are likely to fuel growth in federal procurement spending, including a proposed increase of $54 billion to the defense budget. Recognizing the growth opportunities in the marketplace, the U.S. aerospace and defense sector has seen its market cap increase by 16.7% in the initial 100 days following the election.

Market reaction

In addition to the surging equity markets, the bond market has seen significant movement since the election. Yields on the U.S. 10-Year Treasury Bond have increased over 50 basis points since November 8, 2016, when rates stood at just 1.86%. Given real estate pricing dynamics and interest-rate sensitivities, the impact of this volatility on property markets may be substantial. Although the bump in interest rates has in some cases slowed investment sales velocity and forced some transactions that were under contract to be repriced, investor optimism remains strong. Commercial real estate spreads are likely to compress given increased confidence in the financial markets, but rent growth will be necessary to offset any prolonged rise in interest rates.

Policy and economic implications

In his first two months in office, President Trump has issued 25 Executive Orders and Presidential Memoranda. These documents provide a broad blueprint of the new administration's policy priorities. Generally speaking, the directives being put forth by the administration represent the first step in delivering upon three core campaign promises: protecting national security; reducing the size of government; and stimulating private-sector job growth.

Spending - Although a full budget isn't expected to be issued until May 2017, President Trump has called for a 10% increase in the defense budget and proportionate reductions to other federal agency budgets. Cuts to agencies including the Department of State and the Environmental Protection Agency appear highly likely. Moreover, the incoming Director of the Office of Management and Budget, Mick Mulvaney, has a well-established record of being a "deficit hawk."

Taxes - President Trump campaigned on the promise of tax cuts, including fewer personal income tax brackets, lowering of corporate tax rates to 15% and a tax holiday for the repatriation of overseas profits. His ability to enact these policies in light of his concurrent position to retain current levels of entitlement spending may be challenged by fiscally moderate legislators.

Regulation - The regulatory environment is expected to be loosened across the board under President Trump. Case in point, three of President Trump's first eight Executive Orders were focused on expediting environmental reviews and speeding the approval of infrastructure projects.

Trade - The President holds strong unilateral power over trade agreements, which presents some level of geopolitical uncertainty. It is likely that some trade deals such as the North American Free Trade Agreement (NAFTA) will be restructured. Discussions of border adjustments and criticism over currency manipulation will likely intensify. China and Mexico will likely face particularly strong criticism.

Global impact - Concerns over the rise of populism and protectionism seem to be receding given the U.S. economy's favorable post-election conditions. The economic upswing seems to be expanding to Europe, Japan and China, where business surveys and financial markets have turned markedly optimistic.

Monetary policy - The initial expectation was that a Trump victory would create more volatility and take expected rate hikes by the Fed off the table. However, the overwhelmingly positive reaction within the equity markets supported a 25-basis-point increase by the Fed on December 14, 2016 and Fed Chair Janet Yellen signaled three additional hikes in the overnight lending rate would be likely in 2017. Trump's fiscal plan seems to point to a rise in both economic growth projections and the size of the federal budget deficit, which could lead to higher inflation and interest rate expectations.

Real estate implications

With financial industry regulation likely to loosen, or at minimum no longer tighten, capital flows may improve and create a short-to-medium term net positive for investment activity and performance. While cap rates are low, spreads remain historically healthy and the fundamentals are sound broadly across real estate sectors. Fiscal and trade policies that could lead to higher inflation and interest rates could impact pricing if not offset by faster growth. Overall on the demand side, some U.S. companies are likely to adopt a wait-and-see approach until fiscal policies and the terms of renegotiated trade deals are finalized.

Deregulation and tax cuts would on their own be pro-growth for real estate demand, but the timing, mix, and other offsetting policies or compromises are still unknown. Until the policy details are further defined and implemented, we expect activity to continue at a moderate pace, with underlying real estate markets holding steady.

Sector impact

Defense - The upside potential for defense contractors is substantial given President Trump's policy positions and a Republican-aligned Congress. A repeal of sequestration would be a major catalyst for contractors, which have seen U.S. federal procurement spending levels cut by 13.5% since 2010. The cyber-security industry is poised for growth, which is likely to benefit Northern California and Metro DC, and industrial markets throughout the Midwest and Sun Belt are likely to experience a boost in manufacturing.

Federal government – Expect the GSA's Reduce the Footprint initiative to remain in effect and for cutbacks to be accelerated within agencies that are not well-aligned with the new administration's strategic objectives. The Department of Education, Department of Labor and Environmental Protection Agency are likely to see programs and funding get cut, while Veterans Affairs, Customs & Border Protection and Defense are likely to grow.

Legal - Republicans will likely seek to overturn Dodd-Frank, reduce consumer protection safeguards and implement tort reform. This may present a missed opportunity for the legal services sector, which would have likely thrived under Democratic leadership.

Finance - The financial sector is likely to receive a boost from deregulation and the steepening yield curve, which will make lending more profitable for banks. Reduced compliance costs should also benefit the industry. Hedge funds and private real estate investors may see a negative impact from a repeal of the carried interest provision, which was a component of Trump's tax reform plan during the campaign.

Energy - Oil prices are up 20% since the election, when WTI crude was trading at just $45 per barrel. With loosened drilling and environmental protection regulations on the horizon, new pipelines will likely move forward. Given improved access to domestic energy, OPEC's impact is likely to recede and future production should be determined by general supply and demand fundamentals. A potential pullback in federal subsidies for clean energy may limit the rate of growth in that segment.

Health care - In a move uncharacteristic of a Republican, President Trump has lashed out at pharmaceutical companies and has taken aim at the price of prescription drugs. Trump has also called for a repeal of the Affordable Care Act, without establishing a clear vision for its replacement, which leaves the health care industry and insurers facing substantial uncertainty ahead.

Technology - The tech sector should experience mixed results. Trump's anti-immigration stance is likely to limit the H-1B talent pool, potentially increasing domestic wages for American workers and raising labor costs for tech companies. On the flip side, the tax holiday for repatriation of overseas profits would be particularly beneficial for multinational tech companies. Continued growth of this sector and spillover demand to secondary markets given the high cost of labor in primary tech hubs appears likely in 2017.

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