nyrej

Is the trade war with China starting to affect the real estate market? - by Ralph Perna

November 05, 2019 - Long Island

Ralph Perna,
Newmark Knight Frank

The trade war with China, which officially began in July 2018 when the U.S. implemented its China-specific tariff, collecting a 25% tariff on 818 imported Chinese products, is starting to show its effects with local companies. During previous administrations, I don't remember any of the Presidents challenging the booming Chinese economy. Over the past 15 to 18 years, the Chinese economy has exploded with an over 6% compounded annual growth rate (CAGR). As a result, rural areas in China have turned into booming towns, huge factories have been built, and unemployment has been substantially reduced. Most of this is thanks to the U.S. economy. However, it was not with significant impacts. Patents have been infringed upon, technology has been compromised and infringed upon. With that said, Trump decided to show who the boss is. Tariffs were imposed and have continued to increase with total U.S. tariffs applied exclusively to Chinese goods now estimated at $550 billion. Without question, this has created new uncertainties not only for U.S. companies and consumers, but also the Chinese economy which now finds itself in a precarious position.

For the first time in a generation, and as a result of the U.S. tariffs, the Chinese economy is starting to show the strain. U.S. companies are looking at shifting production to other Southeast Asian markets. From reliable sources in China, factories are closing, unemployment is rising and, based on several news reports, the Chinese banking system is not in the best of health.

So what is the effect on us? In my opinion, there are two areas which companies are now dealing with: the actual effect and the perception.

The factual aspects relate to the direct financial costs to a company. Who pays the tariff? Does the company absorb a 25-30% increase? Can the cost be passed on to the customer? And, what are short- and long-term effects on consumers? The unfortunate part is the uncertainty as to a defined direction on where the tariffs will finally land. Companies nationwide are filing for appeals on individual products, but the appeals to be granted have a long list of "but for's."

What will the cost be and how long is this going to take? The unknowns are of concern as to how they will affect future growth and expansion plans. Company relocations, expansions and equipment upgrades are all being placed on hold.

The second avenue is the perception factor. This can stop plans cold which I am starting to see. This is where business executives do not know nor understand the tariff issues and how it really affects them, if at all. So they do nothing. When you couple the unknown, and a limited inventory of industrial buildings for sale, we see a reduced interest with companies looking to expand and invest in real estate. This is too bad as most companies would like to relocate and purchase a new building to support their businesses' growth. This is particularly true when interest rates are at all time low. A recent discussion I had with a mortgage broker revealed that there are insurance companies that will provide fixed rate mortgages at 3-1/2% fixed for 20 years. The U.S. has been on a growth engine in high gear for almost a decade as reflected in low unemployment, record low interest rates and a roaring stock market. The tariff issue can be the tipping point.

Currently, the hottest trend in the market is e-commerce warehousing. Major landlords are building new and buying existing hi-bay buildings. Long Island has attracted several high profile companies who are placing big bets, that e-commerce warehousing is the "next new thing." This could be another sector the tariffs affect.

However, there is a shining light in that there has been a beneficiary of the tariffs – food banks. Millions of pounds of soy beans, groceries, wheat and fruits that U.S. farmers had been selling to China are now sitting on the docks. President Trump signed a $12 billion dollar bail out for the farmers for distribution of their products to food banks throughout the country, including Long Island's own Long Island Cares.

So what has to be done? The U.S. has to form an agreement with China. Once in place, companies can understand their position and adjust their businesses accordingly. As soon as companies adjust, then we will see the outcome on real estate values and availability. The worst case is that values remain status quo. Until then, keep your seat belts on.

Stay tuned!

Ralph Perna is an executive managing director at Newmark Knight Frank, Melville, N.Y.