INSIGHTS FROM THE BDO REAL ESTATE & CONSTRUCTION PRACTICE

INDUSTRIAL REITS CAUTIOUS AMID TARIFFS, TRADE TURBULENCE

By Stuart Eisenberg

Ignited by President Trump's announcement of tariffs on foreign steel and aluminum, trade tensions have dominated news headlines since March 2018.

The impact was immediate: U.S. tariffs and retaliatory measures by other countries slowed the flow of global trade in 2018. The Wall Street Journal reports that, according to the CPB Netherlands Bureau for Economic Policy Analysis, the total volume of goods moving across borders increased just 3.3 percent in 2018 compared to the 4.7 percent rise in 2017.

The U.S.-China trade relationship has been the most contentious, resulting in multiple rounds of retaliatory tariffs amid U.S. allegations of Chinese business malpractice and industrial espionage. To date, nearly half of all Chinese goods brought into the U.S. have been subject to additional tariffs, many at a rate of 25 percent, and the remaining at a rate of 10 percent. The Trump Administration is also weighing implementing additional tariffs on autos and auto components, targeting major U.S. trading partners, including: the European Union, Japan and South Korea.

Protectionist trade policies and retaliatory measures have slowed the flow of goods in and out of warehouses and distribution facilities, impacting demand and pricing for industrial real estate after years of sustained growth.

IMPACT TO INDUSTRIALS' INVESTMENTS

Trade tensions slowed new investments by industrial REITs in 2018, a trend likely to continue until the uncertainties surrounding trade are alleviated. New industrial buildings under construction declined significantly between 2017 and 2018, according to analysis by BDO's 2019 Real Estate & Construction Compass. Disruptions to global trade have made industrial REITs and other owners and operators cautious about making new investments in the near-term, as no one is sure how long the disruptions and uncertainty will continue.

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WHAT TO EXPECT IN THE LONG-TERM

We anticipate that industrial REITs will wait out the short-term trade turbulence, but the long-term outlook for the sector remains sunny. Industrial real estate performed well in the last decade—catalyzed by the rise of e-commerce and increased demand for omnichannel and last-mile delivery.

Consumer demand for rapid delivery and e-commerce is projected to continue growing and will increase the demand for distribution and warehouse spaces, especially in urban areas. To compete in crowded, primary markets, warehouses and distributors will need to invest in technology. Drones, AI, robotics and other technologies can lower system costs and improve efficiencies for warehouses or distribution centers.

For industrial REITs seeking new opportunities, they'll need to assess demand for industrial and warehouse space based on existing market conditions as well as potential shifts due to technology and changes to distribution channels from major infrastructure projects.

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