Can't Trump this: How commercial property fares in a China/US trade war

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It's getting predictable isn't it? The Donald tweets, the rest of the world reacts and equity markets shudder. Blame the 24-hour news cycle, event driven macro traders, fake news or almost anyone with an opinion (in my opinion).

The latest episode of Global Hysteria is a Trump trade war with China. The narrative runs like this: Trump imposes trade tariffs on China, retaliation ensues and global GDP plummets. The closing scene is the Federal Reserve slashing interest rates to prop up an ailing US economy.

This seems unlikely. The reason why we hear so much about Trump-induced panics is because reporters get paid to write about them. As for the 'experts' on Bloomberg TV, they have a dog in the fight. Usually US hedge funds shorting the Yuan, they profit from jawboning markets.

Running a Fund focused on real estate investment trusts in Asia (REIT), we often get asked our view on how a trade war will affect Asian commercial real estate. The short answer is "not much".

Real estate is a local game. The primary determinant of rents, whether it be a new shopping centre, office building or industrial warehouse, is supply.

This is what makes commercial real estate cyclical. Whilst demand is dynamic, supply, at least in the short term, is static. A new office building can take upwards of three years to complete. In the meantime, if other buildings are being released to market, landlords typically respond to an increase in supply by reducing rents.

As for demand, it is very much linked to GDP growth. Falling exports can inhibit economic growth, and with it rental growth. Given this theoretical background it's tempting to draw an adverse conclusion about the impact of a US/China trade war on commercial property in the Asian region.

The reality, however, is more nuanced. Japan, Singapore and Hong Kong - the developed Asian markets in which APN's Asian REIT Fund invests - all run current account surpluses, meaning their economic growth is export-led. Potentially, this could make them vulnerable in a Trump-led trade war.

Either Trump targets each country directly by imposing trade tariffs, or he keeps his focus on China, with the reverberations felt across the Asian region, causing an indirect impact.

This is where nuance is required. Here are the top five exports to the US from the three countries which are the focus of the Asian REIT Fund:

Singapore		Hong Kong		Japan	
1 Intergrated Circuits	11.00%	1 Telephones	8.40%	1 Cars	28.00%
2 Gas Turbines	7.90%	2 Computers	6.30%	2 Vehicle Parts	6.00%
3 Packaged Medicaments	3.90%	3 Broadcasting Equipment	5.20%	3 Aircraft Parts	2.90%
4 Aircraft Parts	3.40%	4 Jewellery	4.30%	4 Large Construction Vehicles	2.00%
5 Computers	3.10%	5 Diamonds	4.10%	5 Custom Industrial Machinery	1.90%
% of Exports to USA	7.20%	% of Exports to USA	8.3%	% of Exports to USA	22.0%

Source: OEC 2018

Whilst steel and aluminium tariffs have got much of the media attention, the list reveals that tech and precision machinery are driving exports from Singapore, Hong Kong and Japan.

Thus far, Trump's strategy has been to try and revitalise the country's manufacturing base by raising the cost of imported raw materials, which are easily substituted. The same cannot be said of aircraft parts, gas turbines and broadcasting equipment. Raising tariffs on high spec machinery that the US cannot produce itself could have serious adverse impacts on the US.

The one outlier is Japan, with its emphasis on vehicle exports. With a well-established auto industry it's possible that Trump could impose tariffs to give the country's ailing industry a leg up.

Even here though, there's less reason for concern. Our Japanese logistics investments do not cater to the Japanese auto industry. Auto manufacturers produce vehicles and send them directly to ports, where they are stored before being loaded onto ships for export, bypassing the traditional warehouse facilities in which we prefer to invest .

This is not to say common sense will prevail. In April, US trade officials produced a 1,300-strong list of Chinese goods that could be targeted by tariffs. Aircraft parts, industrial robots and antibiotics featured on the list. At this stage, whilst the bluster is manifold, actual policy is sparse. My guess is that it stays that way, US businesses are too reliant on these goods in their supply chains to stomach much of a price increase.

Of course, we'll continue to see bumps in the stock market as the Trump Trade narrative gets rehashed for the umpteenth time. What we can confidently say is that the commercial property market isn't buying into the short-termism.

Right now, commercial rents are on an upswing in Singapore, the Hong Kong office market continues to break transaction records and Tokyo recorded a low commercial vacancy rate of 2.65% in April.

We've long argued that investing in Asian commercial property offers exposure to Asian growth without much market volatility. Recent events support that thesis.

We're more than happy to leave Trump as fodder for the late-night talk show hosts and focus on the long term bigger picture, which happens to be far more attractive than most commentators would have you believe.

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