Brexit Breakdown:

What does the vote mean for CRE?

BY BRANDI SMITH

Late in June, residents in the United Kingdom voted for Britain to exit the European Union, a decision nicknamed Brexit. The results of the vote shocked the world, especially since most experts believed the country would choose to stay.

"I did not anticipate that they would vote to withdraw from the European Union so it was a bit of a surprise," said Steve Everbach, Colliers' Central Region president. "I knew it was a possibility, but it was still a bit of a surprise."

"Personally, I think it's great and a step in the right direction away from this idea that there should be a global government that's very far away from the population," said Patrick Duffy, Colliers' Houston president. "But professionally, I probably had the same reaction the stock market had, which was 'uh oh.'"

The decision caused ripples throughout the world markets. The value of the pound dropped to a 30-year low and here in the United States, the Dow closed down more than 600 points the day after the vote.

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"The reaction in the financial markets was predictably swift and severe, as currency and equity traders were collectively caught so wrong-footed," said Andrew Nelson, chief economist for Colliers USA.

"[Brexit] brings up some questions as to the stability of the euro as currency and the overall stability of the EU," said Duffy.

In the days that followed, the reaction simmered down as many questions, such as those posed by Duffy, arose about what Brexit meant for the UK, the EU and the rest of the world.

"The result is uncertainty and uncertainty is never good for markets - whether they're equity markets, real estate markets, so on and so forth," Everbach said.

Now, just as the UK and EU start to explore the idea of how this decision will play out in the months and years to come, so too are U.S. analysts examining its impact within our borders.

Some results were immediate; American banks are looking to shore up their losses by pulling thousands of employees out of the U.K., per Fortune. Citigroup, for example, will relocate 2,000 employees out of London, while Bank of America will do the same with 1,365 employees.

"No one knows exactly how long it's going to be, but I suspect it's going to be multiple years as they work through all the exit situations with trade," said Everbach.

As negative as the market reaction was the day after the vote, it's possible America may reap some benefits. Instability in Europe means investors could pull their capital out of U.K. countries and reallocate their money in more stable regions, such as the U.S.

"I'm not saying this will be a flood of capital coming from the U.K. into the U.S., specifically into Texas, but I do think it will cause companies to ascertain their investment portfolios and potentially redeploy capital from the U.K. and Texas will show up on their radar when they consider the U.S.," Everbach said.

The American market is already seen as a kind of safe haven for foreign investment, according to Real Capital Analytics (RCA). The New York City-based research firm reports that in 2016, foreign investors pooled $16.3 billion into the U.S. multifamily sector; $2 billion of that total came from the U.K. That trend could see more traction as uncertainty about the EU builds.

"I think there will be flight capital looking for yield, and commercial real estate still has a very good yield," Duffy said.

"All in all, Texas is positioned very well to receive some of that capital that may be redeployed," Everbach said. "Texas is viewed from a real estate investment standpoint as a stable and growing economy right now. Even with the energy sector challenges in Houston, the Texas economy is well-diversified. From a real estate investment standpoint, Dallas, Austin and Houston are attractive markets."

When it comes to U.S. investors, there's a huge question about how the Brexit vote will affect interest rates. Most experts seem to agree that a 'yes' on Brexit means a 'no' on a summer rate hike, which was speculated to happen before the Britons voted out.

The Federal Reserve has previously referenced U.K.'s potential exit from the E.U. as a risk factor, which means the Fed will likely postpone any decision about an increase until this fall at the earliest.

"The likelihood of a hike this fall will depend on evidence of financial market contagion related to Brexit and the strength of U.S. labor markets and inflation," Nelson said. "I think at least one more hike this year is still likely, absent major economic shifts."

The potential combination of a flood of capital along with maintained low interest rates could trigger price increases in many markets, especially the hubs foreign investors historically prefer.

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Though most assuredly a momentous point in history, the full scope and impact of Brexit will not be known for several years. However, it's likely that the United States will benefit from a boost in domestic commercial real estate, whether it's a temporary influx or a long-term investment. As uncertain as the coming weeks and months may be, commercial real estate may offer shelter from the storm.

Patrick Duffy
President | Houston
Colliers International

Steve Everbach
President | Central Region
Colliers International

Colliers INTERNATIONAL