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1031 exchange outlook for 2008: Huge part of economy

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These days it is fashionable to speak negatively about the real estate market where, until recently, pundits were still talking about only a cooling period. And while the sub-prime mess will account for a definite weakness in the residential markets for 2008 (and possibly for longer than that); there is still enough steam in the commercial markets to prevent the free-fall in property values that is occurring in the residential market. Accordingly, I am still bullish about investment real estate and 1031 exchanges for 2008.

One overriding factor, which will continue to add strength to the real estate market, is the historically low interest rates. The combination of "cheap money" in the form of low interest loans, and the down turn in the market, will generate activity among the bargain hunters and investors who have a war chest for occasions such as these. An overwhelming majority of these transactions will be in commercial and industrial properties or multifamily.

The segment of the real estate investment community which will be totally absent in 2008 will be the "mom and pop" investors dealing in one and two family homes. Currently, lending institutions are skittish enough about lending money to people trying to buy a primary residence. Investors seeking loans for rental properties, second homes, or vacation homes are finding that lending requirements have been tightened so significantly that even the strongest credit scores may not be enough. The absence of these transactions will be felt in the 1031 community as there were a significant number of mom and pop investors in the past seven to eight years who were gravitating from their smaller residential properties into larger investments such as apartment buildings, small strip malls, and triple net leased properties. These types of transactions have all but evaporated.

It remains to be seen if lenders and financial institutions, eager to regroup from their losses, will return to their old ways and begin lending again as rates continue to plummet. Low interest rates got us into this mess, and as of the writing of this article, the Federal Reserve seems to believe that low interest rates will get us back out. The health and recovery of the real estate market will be dependent upon lenders going back to the fundamentals of underwriting and staying away from the quick buck.

The last factor which will buoy the real estate market is the continuing flood of foreign investors attracted by the cheap dollar. The real estate market in the U.S. has looked attractive to overseas investors for a while now, and with the recent dip in values, real estate looks extremely cheap to them. These investors, along with the bargain hunters, will be entering the market at a different price point and even a small uptick will mean a profit.

Accordingly, although the market continues to slow the number of 1031 exchanges will most likely increase as investors continue to become aware of the benefits of an exchange. There are still plenty of attorneys, accountants, and realtors, who, in addition to their clients, are not fully aware of the benefits of an IRC 1031 tax deferred exchange. The qualified intermediary community continues to do its part to educate tax, legal and real estate advisors by holding continuing education classes. In addition, the main stream media has picked up on 1031 exchanges and there continues to be numerous articles in real estate sections across the country.

In conclusion, 1031 exchanges continue to be a huge part of the economy and the trend will continue in 2008. The volume of IRC §1031 exchanges will continue to grow until all real estate investors and their advisors are aware of the benefits of exchanging instead of selling.

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