

# 1031 Exchange Trends & Info for 2023



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2023 is underway! Below are key trends, issues and points regarding 1031 Exchanges and Commercial Real Estate.

## 1031 Exchange Market Update for 2023

The recurring question is, after a robust 2022 for Commercial Real Estate and 1031 Exchange transactions, what's in store for 2023?

With a new business cycle notably marked by higher interest rates, inflation, and slower growth, the Commercial Real Estate industry has a more pessimistic outlook which will also impact the number of 1031 Exchanges that may occur. It will be a year of challenges and of opportunities.

The pace of Commercial Real Estate transaction volume has continued to trend down with the interest rate hikes.

The pandemic spurred structural shifts in how certain property types are used. This is expected to continue. With more employees continuing to work remote or hybrid, the need for office space will continue to shift as needs are re-evaluated. The weakening of demand will cause more office buildings to be turned into retail or residential, and retail buildings will become office or industrial or residential or mixed use, while other properties will be scrapped for developable land.

The housing market will continue to be negatively impacted by rising interest rates and housing market activity is likely to stay low. Higher mortgage rates and near record price levels make ownership, especially for first time homebuyers, less attainable. However this will support continuing growth in the rental house market spurring opportunity for single family home and multifamily investment.

Multifamily and industrial are predicted to remain popular asset classes, and retail with repurposed class usage, and hospitality, particularly with the growth of Airbnb and VRBO rental investment, will continue. These asset classes generally structure their transactions as 1031 Exchanges.

On the Washington DC front, as a result of a very active multiyear effort to educate Representatives and Senators of the importance of 1031 Tax Deferred Exchanges to the US economy - which was supported by updated economic studies, Section 1031 remained unchanged in 2022. As we enter 2023, it will be necessary to continue those efforts as well as proactively educate new members of Congress of the legitimate, economically important benefits of Section 1031. We also will be watching for the Administration to issue its proposed budget within the coming months and remain prepared to respond to any threats to IRC Section 1031. As always, IPX1031 will continue to issue periodic legislative updates.

With the anticipated market challenges, 1031 Tax Deferred Exchange transactional activity should be slower than the unprecedented pandemic era volume. However, 1031 activity will remain resilient. There will continue to be many opportunities for educated investors and commercial property owners to utilize the strength of 1031 tax deferral.

## 1031 Exchange Trends for 2023

- Prices of properties will continue to decrease.
- Properties are on the market longer due to high interest rates
- More investors will be using Adjustable Rate Mortgages (ARMs). These interest rates are typically lower than a traditional 30-year fixed, but adjust to market rate when the ARM matures in 5, 7 or 10 years. As one banker recently commented, "Customers will realize that they are dating the rate, but marrying the property." Meaning that they can be serious about buying the piece of real estate that they want but don't have to stay with the interest rate long-term. Once rates decline owners will refinance to a fixed rate mortgage product.
- As interest rates continue to rise and property values begin to decline, more "all-cash" investors will utilize 1031 Exchanges.
- As the market has softened, more investors will patiently wait to sell, or convert all or part of their primary residence to qualifying investment property as they expect prices to rebound.
- Market uncertainty may not affect 1031 Exchange transactional activity for commercial, industrial and multifamily apartments. These sectors will outpace office, and single family rental activity.
- Continued increase of [qualifying vacation home rental property purchases in warmer climates or other vacation or remote-working locations with high short-term rental income.](#)

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