

Comparing Commercial and Residential Real Estate Investment Opportunities and Risks in Modern Economic Times

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Abstract

The researcher combines his personal case study with a literature review to present his real estate investment model, exploring commercial and residential real estate investment opportunities and risks in the current market economy. The main premise of the model is that using financial acumen and systems models as the approach to investing in real estate provides the opportunity for high rates of return due to a variety of innate factors. The model explores the risks and opportunities of investing by: a) The use of leverage in property acquisitions; b) Accessing significant IRS tax advantages for investors, including the use of depreciation schedules, cost segregation models, 1031 tax-deferred exchanges, and tax-free cash-out refinancing. Risks in residential and commercial real estate can result from internal factors within the owner's control or be caused by external factors beyond the investor's control. AI, machine learning, and dynamic factor models for real estate investment are explored.

Keywords

Property Management, Real Estate Investment, Positive Cash Flow, Cost Segregation, Leverage, Real Estate Passive Income, Real Estate Tax Advantages, Cost of Capital, Return on Investment (ROI), Capitalized Rate of Return (CAP Rate), Loan to Value (LTV), Debt Service Cover Ratio (DSCR), 1031 Tax Deferred Exchange

1. Introduction

Real estate remains one of the leading investment asset classes in the United States, helping ordinary people achieve financial independence. Real estate is a physical, tangible, reliable commodity that has existed for hundreds of years as a vital part

of our societal landscape and human existence. Most people understand what real estate is and what it entails, even if they are not aware of how to invest in it or the benefits of doing so.

As an asset, real estate is also subject to different risk factors on the local, state, and federal levels. For example, changes in the US economy can impact the job market, resulting in lower monthly rental rates and increased property vacancies. State and local regulatory changes can also impact the real estate market and its associated risk factors. Federal Reserve interest rate increases increase the cost of capital, and changes in IRS regulations affect tax-advantaged real estate, which are other external factors that contribute to real estate investment risks.

A common adage in the real estate investment business is that one must be willing to take big risks to achieve big results. Therefore, no risk means no reward! The good news is that real estate, as a tangible asset, offers stability and consistency, potentially reducing unknown risks and providing investors with a higher degree of predictability regarding their future returns. However, taking these risks means educating oneself on financial instruments and how to leverage the various regulations.

2. Background of the Problem

As an investment vehicle, real estate falls into two main categories: residential and commercial. Residential real estate covers houses, condos, apartments, and multifamily properties of two to four units. Commercial real estate facilitates the space needed for businesses to lease, occupy, and residential properties of five or more units. Both real estate classifications are subject to financial and sector-specific risks and opportunities. Real estate, as a commodity, is an essential component that contributes to every community. Key economic variables, including interest rates, inflation, tax policies, and income levels, all impact real estate markets and investor behavior. Investing in real estate offers several advantages, including capital leverage, tax incentives, depreciation benefits, and consistent cash flow. In contrast, the disadvantages include internal issues, such as weak property management, as well as external problems, including regulatory uncertainty and economic instability.

Both residential and commercial real estate are crucial to economic growth and stability. [The Real Estate Roundtable \(2024\)](#) reports that the total value of America's commercial real estate reached \$22.5 billion in the fourth quarter of 2023. This value was spread across various sectors, including multifamily housing, specialty, sports, and other venues, office and retail space, industrial, healthcare, and hospitality. These commercial sectors contributed approximately \$0.25 trillion to the US gross domestic product (GDP) in 2022, representing 10% of the total GDP.

In the residential real estate segment, the [National Association of Home Builders \(2024\)](#) has determined that residential real estate contributes approximately 15% - 18% to GDP annually. This sector includes single and multifamily homes, renters, builders, property managers, and service providers. The National Associ-

ation of Home Builders also recognizes the “ripple effect” of homeownership on residential real estate, which stimulates additional services such as furniture, appliances, home improvements, and moving services.

3. Purpose of the Research

Research on financial literacy in the United States reveals that nearly 50% of adults lack a basic understanding of their own finances (Meineke, 2024). Thus, the risk factors and benefits of investing in the current United States residential and commercial real estate markets are not fully understood by most investors, despite the fact that real estate affects approximately 20 percent or more of the US economy (Real Estate Roundtable, 2024). Thus, the purpose of the research is to review the current information needed by potential real estate investors considering investments in the residential and commercial real estate segments.

4. Theoretical Framework

As a professional real estate investor, the author approaches his investment portfolio as a business. Within this framework, two of the largest obstacles facing investors are the lack of financial literacy and acumen, as well as a limited understanding of leveraging investments through the use of systems theory. Financial literacy theory refers to an individual’s ability to understand financial instruments, manage their finances effectively, and make informed financial decisions. (Beal & Delpachitra, 2003; Noctor et al. 1992). Financial literacy involves the application of knowledge and comprehension skills coupled with desirable attitudes, behaviors, and external enabling factors that are necessary for an individual to invest in both residential and commercial real estate properties. Concerning systems theory, Von Bertalanffy (1968), a biologist, first introduced the concept and discovered evidence that components within systems interact in a complex yet cohesive and organized manner, utilizing inputs, processes, adjustments, and outputs. As real estate exists within a complex system subject to environmental fluctuations, systems theory is a relevant model for understanding the risks and opportunities associated with real estate investing.

5. Methodology and Research Design

This study employs a mixed-methods approach to review and analyze the literature on commercial and residential real estate opportunities and risks. The research design employs a case study (Baxter & Jack, 2008) and a comprehensive literature review to examine the variables influencing the risk and reward of commercial and residential real estate investing. The data represented a combination of this general real estate research literature and the author’s personal case study. Articles were obtained using the search terms “commercial + residential real estate opportunities” and “commercial + residential real estate risks”. These key search terms were applied in the following databases: Academia.edu, American Real Estate Society (AREAS) journals open access, Google Scholar, ResearchGate.net, and

Scientific Research Publishing (SCIRP) open access articles. This approach combines academic sources and real-world insights to provide a well-rounded perspective on collecting and analyzing current opportunities and risks in real estate investment.

5.1. Case Study

A case study is a qualitative approach to studying a bounded concept of a phenomenon in its context (Baxter & Jack, 2008). According to Yin (2013), a case study design is appropriate when the focus of the study is to answer “how” and “why” questions, or when you cannot manipulate the behavior of those involved in the study. A significant component of the design is the author’s personal experience as a real estate investor, developer, property owner, and licensed real estate broker across the states of Florida (FL), Georgia (GA), and Alabama (AL). With over three decades of direct involvement in the real estate industry, the researcher has navigated a variety of market conditions and economic climates, including surviving the 2008-2009 real estate market crash. Jones & Trevillion (2022) highlight that the author’s personal experience, particularly the near collapse of his real estate investment management company in 2008-2009, has offered valuable, real-world insights into real estate investment strategies, risk management, and the ability to adjust to shifting market conditions. The lessons learned from failures and successes enabled the author to develop a methodology that combines both the theoretical aspects of real estate investment and the practical, real-world experience of navigating market volatility.

The researcher draws on case studies from their portfolio of real estate investments to illustrate key points. Real-life examples are used to demonstrate the application of specific investment strategies, such as purchasing undervalued properties, undertaking renovations to increase rents and net operating income (NOI), and utilizing the 1031 tax-deferred exchange to defer capital gains. These examples help ground the theoretical concepts discussed in the literature review and bring clarity to the real-world application of real estate investment principles. By combining academic insights with hands-on knowledge and case studies, the study provides a nuanced understanding of the complex and dynamic nature of real estate investment. The methodology emphasizes the importance of adapting to market changes, making informed decisions based on data, and effectively managing risks to achieve financial success.

5.2. Literature Research

The study employed a general literature review to collect data. The researcher conducted extensive online research to gather data from reputable sources, including federal and local government agencies, academic databases like Google Scholar, and current academic real estate journals, as well as economic and real estate market reports. The literature review compiled articles using both quantitative and qualitative methodologies to establish a foundational understanding of the industry’s current landscape and identify relevant trends, emerging technologies (such

as AI and machine learning), and global economic factors influencing the real estate sector.

By leveraging academic research, real estate organizational and government reports, the study gained insights into various economic conditions, taxation policies, risk management strategies, and investment models in both residential and commercial real estate. Key sources from journals and authoritative books on real estate finance, investment strategies, and market dynamics were also consulted to gain insight into past and ongoing market changes.

5.3. Analytical Approach

The study employs a qualitative descriptive design approach (Sandelowski, 2000) to analyze the various factors influencing real estate investment. A qualitative descriptive design is referred to as “basic or fundamental qualitative description” (Sandelowski, 2000: p. 355), which uses the facts of the research to develop a low-inference analysis. The basic description enables the researcher to base the findings on facts derived from the data.

The risks associated with different market conditions are examined, including internal factors (such as debt management, property management practices, and investor decision-making) and external factors (such as changes in government policy, economic conditions, and interest rates). These factors are explored through both the research results and personal anecdotes, offering a comprehensive examination of the complexities of real estate investing. The study also incorporates relevant real estate models, tax strategies, and methods of leveraging investments, offering a balanced view of opportunities and risks.

6. Assumptions and Limitations

While this methodology provides a comprehensive analysis, it is worth noting that real estate investment is a highly dynamic field. Several assumptions and limitations are associated with this dynamism. Both assumptions and limitations may not be under the control of the researcher.

6.1. Assumptions

It is assumed that investors have undertaken the process to become qualified as professional real estate investors. This recognized designation of the Internal Revenue Service (IRS) allows real estate investors to take advantage of specific tax codes and accounting treatments. According to Turner & Leavins (2017) and section 469(c)(7)(C) of the IRS code¹, property investors must satisfy two basic requirements to qualify for the professional real estate investor designation:

The investor was active, providing real estate services to clients or participating in a real estate-related business for more than 750 hours during the tax year. Such services could include, but are not limited to, property selling, leasing, and man-

¹Internal Revenue Service Code Section 469(c) (7) (year). Professional Real Estate Investor. Designation.

agement. For instance, a good example of someone who could qualify is a commercial real estate broker, a residential real estate agent, a property manager specializing in vacation rentals, or a real estate broker managing a brokerage. During the tax year, investors must have spent more than 50% of their time materially involved in working in real estate-related businesses and activities. A few good examples of these real estate activities include renting homes, condominiums, or commercial buildings; property acquisitions; renovations; and development.

6.2. Limitations

There are three main limitations to this study. First, as a commercial enterprise, investing in real estate is a local and location-focused business. Therefore, the research is limited by changing market conditions that can vary significantly across different geographic locations and investment types. Future market and political changes may introduce new risks and opportunities not captured in this study.

Second, the researcher has drawn on a single case study of personal experience and selected examples. As such, these examples may not generalize to or reflect the experiences of all investors. Due to the local nature of real estate valuation and location, opportunities and risks in different locales could be comprised of different variables. As such, conducting due diligence on any property is a common approach to understanding the particular needs and differences that any property may represent for a potential investor. Third, the methodology is limited by its reliance on secondary research. While every effort has been made to use reputable sources, the real estate landscape continues to evolve rapidly, particularly with the increasing role of technology, economic shifts, and regulatory changes. Therefore, the study's conclusions are based on the available data at the time of writing and may require updates as the industry progresses.

7. Literature Review

The literature review examines studies that investigate both risk factors and opportunities available in the United States' real estate market. Some investment and risk factors are under the investor's control, while some issues are not. Investment opportunities appear through tax-advantaged benefits, specifically the IRS section 1031 tax-deferred exchange. Real estate risks fall into two primary categories: (a) factors that impact risk within the investor's control, and (b) external conditions beyond the investor's control.

7.1. Real Estate Investment Model of Opportunity and Benefits

In general, as an investment, both residential and commercial sectors of real estate present numerous opportunities to achieve financial independence. The structure of this business model may explain why real estate investors can potentially earn such extraordinary total annual returns. A traditional real estate investment model is likely to include key characteristics such as:

- 1) Buyers commonly use leverage to purchase investment real estate using a

blend of lender debt and owner equity. Especially in commercial real estate, this leverage is based on understanding two concepts related to the operating income potential. The first concept is the cap rate, or the amount of capital that a property produces (net operating income or NOI) compared to its asset or market value (Smith, 2024). The second concept is the debt service coverage ratio (DSCR), which measures the ability of the property and the investor to service the ongoing debt costs of the property, minus taxes and interest payments (Fernando, 2025).

2) The model postulates that real estate should be bought at a discount below market price, often because of death, divorce, or financial distress.

3) The property would typically have significant add-value upside. This added value can be achieved if the property is dated, in poor repair, or if the mechanical systems require replacement.

4) Renovations drive up rents, increase the net operating income (NOI), and force the “after-repair” appraised value higher.

5) The link between real estate hold times and inflation rates impacts long-term appreciation and the overall return on investment (ROI).

6) Historically, property values increase as rental income rises over time.

7) As the loan balance diminishes, the gap between the lower principal balance and the higher real estate value increases the amount of equity in the property.

8) Depreciation on real estate, which will be discussed later in the article, is the greatest mechanism ever to reduce or eliminate real estate investor income taxes.

7.1.1. Residential Real Estate Investment Opportunities

For those beginning their careers as professional real estate investors, residential real estate offers an entry point into the process of investing, upgrading, and developing services, such as property management. Extreme housing shortages, increased homelessness, and the unaffordability of housing have prompted changes in current state laws, as seen in the recent legislation signed into law by California (California Department of Housing and Community Development, 2025). States such as Washington, Oregon, Montana, and Texas have also moved to redefine zoning laws, especially concerning the number of multifamily housing units allowed on lots formerly zoned for single-family housing (Wamsley, 2024). These changes should increase opportunities for those willing to work their way into residential real estate investment.

7.1.2. The Tax-Advantaged Benefits of Real Estate Investing

The IRS designation of “Professional Real Estate Investor” (Section 469[c] [7]) provides individual investors with significant tax advantages. When you meet the guidelines, your property investing activities and rental income will be considered “nonpassive”. IRS rules legally enable investors to depreciate their investment property structure and mechanical components, excluding land. Depreciation is a process by which an investor can take an annual tax deduction against a portion of their property investment cost to account for the wear and tear on the property. Depreciation on investment properties falls into two categories, each with its own

depreciation schedule, as follows: a) residential real estate depreciation is scheduled over 27.5 years, and b) commercial real estate depreciation is scheduled over 39 years. Many real estate investors break even or incur tax losses year after year, utilizing the depreciation model. Depreciation is among the most favorable tax strategies in real estate, which is why many people become professional real estate investors. Losses that are not absorbed in one tax year can be carried over to the next year. An accelerated depreciation model, known as cost segregation, also exists, which fast-tracks the depreciation timeline to write off more taxes in the early years.

This depreciation-tax strategy enables real estate investors to save substantial amounts of federal taxes on income earned from sources such as a W-2 job, stock market earnings, or other business income. The most remarkable aspect of the strategy is that real estate investors can apply their yearly carryover losses from real estate investing to their IRS Form 1040 income and may never pay any taxes, legally. Individual investor tax circumstances may vary. This segment of the article is not an attempt to provide real estate investor tax or accounting advice. Readers should consult a professional tax advisor if needed.

7.1.3. IRS Section 1031 Tax-Deferred Exchange

The most impactful tax-saving gift the IRS provides to real estate investors is more widely known as a 1031 exchange. This exchange is available to both residential and commercial investors, as long as the property remains an investment vehicle. The best way to describe a 1031 exchange is that it allows real estate investors who have owned an investment rental property for at least one year to sell their rental property and defer any capital gains. Investors can conduct a 1031 exchange by purchasing a “like-kind exchange” property in exchange for the one they sold.

According to IRS rules, investment property held for less than one year is classified as a short-term investment and is subject to the ordinary income tax rate. Real estate held for more than one year is treated as a long-term investment, and if sold without doing a 1031 exchange, it would be subject to capital gains tax, not the ordinary income tax rate. The exchange of property to defer capital gains must follow specific IRS 1031 exchange rules. The money received by the closing attorney for the sale of the original property must be wired to an approved 1031 tax exchange intermediary service. IRS rules prohibit the seller from getting access to the proceeds of the sale unless the seller is willing to pay the capital gains on the portion received. The timelines that must be met, such as the 45-day rule and the 180-day rule, are crucial. These deadlines arrive quickly. Therefore, the seller should be prepared for any last-minute hurdles that may arise in identifying a replacement property. The guidelines for a successful 1031 tax-deferred exchange include the following:

- 1) A like-kind exchange must replace the property sold. This exchange requires that the property to be purchased for the exchange must be an investment property with a rental or income-producing component. For instance, if a leased shopping center were sold, the seller could exchange it for another shopping center, an apartment complex, an industrial warehouse park, or a self-storage facility.

2) The (45) Day Rule. The 45-day identification period for the replacement property starts on the original closing date. Three properties can be identified, but only one can be selected.

3) The (180) Day Rule. The closing of the property identified for the exchange must occur 180 days from the original closing date.

4) The loan amount for the replacement property must exceed the amount received for the property sold in the exchange. Suppose the loan for the property being purchased is less than that of the property sold. In that case, the investor will have to pay capital gains on the difference between the loan amounts.

5) The 1031 exchange model allows a real estate investor to utilize the government's tax dollars to purchase a replacement investment property while deferring capital gains for years, potentially indefinitely. The 1031 exchange model is a prime example of the benefits of real estate investing, enabling more ordinary people to become millionaires.

7.2. Risk Factors Within Investors' Control

Both risk and opportunity factors can drive market volatility. However, real estate investors need to differentiate between the risks that they can and cannot control. Supply and demand economics, as well as interest rates and weather conditions, may not be within the investors' control. Those factors related to debt, general liability, and property management can be analyzed in advance.

7.2.1. Debt Ratio, Leverage, and Financial Decision-Making

Debt is a standard part of real estate investing. Managing debt is within the investor's control. The percentage ratio of debt to value, or contract price, is known as the loan-to-value (LTV) ratio. In real estate, the debt-to-value ratio set by lenders typically falls within the 65% to 95% range, depending on the borrower's qualifications and the type of real estate, whether residential or commercial. Generally, the investor uses cash or savings as a down payment for the 5% to 35% equity portion required by the lender and uses leverage to obtain a bank or private lender loan. Occasionally, lenders may collaborate to provide the borrower with the combined amount of debt needed to make the purchase, up to a certain loan-to-value (LTV) percentage. In certain cases, the bank makes the primary loan and holds a first lien position against the property, while the seller may hold a second mortgage in a secondary lien position behind the bank. Seller second mortgages must be lender-approved.

In a seller second mortgage scenario, the bank and private lender could have a combined loan-to-value (CLTV) ratio of up to 90% of the appraised price. In that situation, the borrower would put down only 10% as equity. As a real estate investor, broker, and developer, I believe that property investors are the stewards of the debts they accrue and the financial risks they take. I recognize that: a) More debt means a larger debt repayment commitment, a higher monthly mortgage payment, a higher risk of loan default, or foreclosure; b) Debt can be an investor's greatest friend to grow wealth or worst enemy in going bankrupt depending how

the investor manages the money; c) Debt should be utilized for long-term financial growth and profit; d) Borrow what you need for your real estate investment to succeed; avoid the pitfalls of unnecessary borrowing, and frivolous spending; e) The investor has control over how much they borrow and how responsibly they manage and repay the debt.

7.2.2. General Liability and Fire Insurance Coverage

The ongoing challenge for many real estate investors today is how to mitigate the risk of loss and damage to investment property, satisfy lender insurance requirements, and keep the cost of liability, fire, and wind insurance to a minimum. Managing general liability, fire damage risks, and related insurance costs are within the scope of the real estate owner-investor (Taylor, 2020). Currently, insurance rates are extremely expensive, especially in Florida, where property investors are vulnerable to annual hurricanes from July to October. Traditional banks and a few private lenders insist upon strict insurance coverage requirements to protect their loan collateral. Fire and general liability coverage are standard to protect against damage or losses from hurricanes. However, investors who have zero debt on commercial properties or have a seller-financed loan often opt to self-insure. Self-insurance is a cost-management concept in which the investor does not purchase standard liability, fire, or wind insurance. Instead, the owner-investor creates an insurance fund or reserve within the company to cover any expenses in the event of (hurricane) property losses or damages. Property self-insurance is a way to manage risk while managing the high cost of fire and general liability insurance.

Many older commercial buildings in Florida are like bunkers; they were built with cavity blocks from the 1950s to 1980s and have a strong resistance to hurricanes and high-speed winds. However, most banks still require general liability, fire damage insurance, and insist on wind coverage, which is about 5 times the cost of standard fire and general liability insurance. A few action steps real estate investors could take to keep insurance costs down and limit risk of loss and damage to their commercial property include: a) Shopping rates with multiple carrier to get cheaper quotes; b) Avoid the higher cost of “captive” insurance companies who sell only their proprietary insurance products; c) Investors seeking to pay less for insurance, can raise the deductible to the maximum the lender will allow.

7.2.3. Elements of Property Management that Impact Risk

Every investment property must be managed. The owner-investor has the decision-making authority to determine how the property should be managed and, therefore, has control over factors that impact risk. Property management elements that can impact risk include, but are not limited to, the following: a) How timely and thorough property maintenance and repairs are handled. Deferred maintenance neglected for long periods can result in tenant defaults, higher vacancy, loss of rent, and property value decline; b) Financial losses due to management’s failure to collect rents on time, failure to retain tenants and maintain high occupancy, poor management of accounting, financial record-keeping, and the

misuse of working capital. For example, purchasing unnecessary products or services, failing to negotiate with multiple contractors for lower renovation prices, and overpaying for routine mechanical services, such as plumbing diagnostics, repairs, or installation, A/C unit replacement, or electrical panel upgrades.

Many of the risk elements associated with real estate investing can be monitored, measured, and controlled by the property manager, thereby enhancing the effectiveness of property operations. For example, most real estate investors with smaller portfolios up to \$10 million in assets generally manage these properties themselves. However, large real estate corporations, syndicated partnerships, real estate investment trusts (REITs), and private equity groups with real estate assets between \$10 million and \$10 billion hire outside property management companies. Self-managed properties are usually less vulnerable to risk because the owner is hands-on, personally oversees the financial obligations, and handles most of the work, including leasing, accounting, rent collection, maintenance, and repairs. On the other hand, the property investment groups, who hire third party real estate management companies to manage their property portfolios, may unintentionally have greater exposure and higher risk than the smaller, self-managed, owner-operator for a variety of reasons: a) The property management company has nothing invested, no financial risk, and little to lose, other than a management contract; b) Good management companies are hard to hire; the high turnover and frequent replacement of real estate management companies by investment groups is relatively common; c) How the property performs under management is in proportion to the management company's use of advanced technology, the training, knowledge, and experience of the management company's employees and managers.

8. External Conditions beyond the Real Estate Investor's Control

When investing in real estate, external conditions beyond the investor's control may lead to higher costs, unforeseen risks, and potential losses in the real estate industry. Two examples are the 2009 real estate crash, which caused havoc and financial devastation for many. In the Spring and Summer of 2020, COVID-19 was rampant around the world. The flu-like illness led to a government moratorium on residential property evictions, resulting in job losses and creating financial hardships for many. External conditions beyond one's control include factors such as changes in the economy, shifts in government policies, fluctuations in interest rates, alterations in tax laws, and acts of nature, such as hurricanes and terrorist attacks on the homeland.

8.1. Residential Real Estate Investment Risks

In particular, one major risk associated with residential real estate is the lack of financial leverage for smaller properties. The controls on the definition of residential real estate, which define properties as one to three units, mean that a single

unit in need of repair or with tenants is a loss of income that can impact the project's financing. These situations are usually not within the investor's control. As an example of a passive investment system, this means that the system is not fully leveraged to continue operating at full capacity. This break in the system's functioning means the investor will lose passive income while using funds to repair and replace broken systems in the property.

8.2. Economy

Major cyclical events in the US economy over the next few years are expected to have a significant impact on property rental rates, the cost of capital, and potential decreases in property values (Garriga et al., 2023). Any such changes could impact the wealth of residential, multifamily, and commercial real estate investors. Currently, the US economy is in a transitional phase due to the change in administrations from President Biden to President Trump. Historically, the state of the economy has determined the prosperity of the people and their exposure to risk (Bonomo, 2023). However, the United States is currently \$36 trillion in debt (Pozan, 2016). The Trump administration's "Big Beautiful Bill" has focused on tax breaks and tariffs, rather than actual debt reduction (Horsley, 2025). If the debt is not reduced, the country could fall into recession (Grisales & Sprunt, 2025).

8.3. Government Policy

Any government policy changes affecting real estate investing could create a risk environment in the property investment sector (Lifflander, 2010). For example, while Trump has maintained the IRS Tax codes that apply: a) To the Professional Real Estate Investor status; b) Retained favorable terms for the 1031 tax deferred exchange; c) Has maintained the rules that govern real estate depreciation and cost segregation studies, Trump has introduced tariffs on goods imported and exported between the US and foreign trading partners.

While Trump believes that tariffs will level the playing field for excise taxes between the US and other foreign countries, tariffs will affect many additional costs involved in home and office construction, such as tools, steel, lumber, and the like (National Association of Home Builders, 2024). Additionally, the immigration policies of the Trump administration have focused on deporting workers, including those in construction. The lack of workers will delay timely construction schedules and raise labor costs overall (González-Hermoso et al., 2025).

8.4. Hurricanes, Acts of God, or Terrorist Attacks

Real estate investors cannot control hurricanes, Acts of God, or Terrorist attacks. True, these disaster events cause property damage, create havoc, result in loss of life, and lead to financial losses, but property owners and investors may be wiser to plan and be prepared (Fisher & Rutledge, 2021). For example, Florida residents are aware that between August and October every year, there is a high probability of one or more hurricanes occurring in the state. Therefore, Florida's real estate

investors can be prepared in advance for the hurricane's high winds, torrential rains, and flooding. In preparation for a hurricane, property investors in Florida routinely stock up on food supplies, monitor weather reports, heed warnings prior to the hurricane, and board up their properties. The same is true for forest fires in California, which a few months ago burned 1000's of acres and destroyed a significant number of homes throughout LA County. Forest fires have long been a part of California's landscape. The most that California investors can do to manage their risk against fires is to be as prepared as possible for the fires when they break out.

Property investors are aware that the United States has a long history of tornadoes, hurricanes, avalanches, and snowstorms. Over time, city mayors, state governors, and federal agencies, such as the Federal Emergency Management Agency (FEMA), have pre-planned, prepared, and developed the knowledge to handle Acts of God involving Mother Nature. However, the greatest risks by far for the real estate investment sector may be: a) the unpredictability of another terrorist attack on the homeland or b) a cyber-attack on some major part of our national infrastructure, which could throw our economy into chaos. Though the government continually monitors radical groups inside and outside the United States, who pose significant threats to property, our society, and way of life, the threats of such a catastrophe always exist. Property investors lack a viable way to prepare for the unpredictability of a foreign terrorist attack or cyberattack. Therefore, real estate investors always remain vulnerable and on guard against such risks.

8.5. Interest Rate Variables

Money is what drives the real estate market. Therefore, access to capital is the most vital component of investing in real estate. When investors borrow to buy, build, renovate, or develop real estate, a concept known as the cost of capital is involved. The cost of capital is the amount of interest the borrower must pay the lender, along with the principal, for the use of the money over a specified period.

The Federal Reserve oversees the United States' monetary policy. It sets interest rates for banks, which in turn influence the rates that banks charge consumers, businesses, and property investors. Interest rates for real estate can vary across a broad range of channels, depending on whether the source of money is from a traditional bank or a private money lender. For example, residential rental properties and small apartment buildings with up to 4 units qualify for residential investor rates under various FHA programs. Private lenders, also known as "hard money" lenders, offer quick-turnaround loans, set their own interest rates (usually 10% to 16% plus 2% to 4% points), and have fewer restrictions. Private lenders act as a viable source of funding at higher rates for investors who cannot meet bank requirements or qualify for traditional bank loans.

Though real estate investors can shop with different lenders for the best rates, borrowers have no control over the variations in market interest rates, which are

monitored and determined by the Federal Reserve. This lack of control over rate changes, particularly rate increases, can contribute to a greater risk for real estate investors (Chen et al., 2022). For example, higher interest rates increase the cost of borrowing and the monthly mortgage payment, resulting in a decrease in net operating income (NOI) and a lower property value. Five years ago, during the COVID-19 pandemic, real estate investors were able to borrow at an average interest rate of 4% to 5%. In March 2025, now 5 years later, a lot has changed in lending. Many commercial real estate loans made in 2020 are coming due in 2025 and will need to be refinanced and paid off. The challenge for real estate investors now is that interest rates for commercial property loans are much higher than they were in 2020, with the current range from 6.75% to 9.95%. Consequently, mortgage payments could increase by up to 50% or more. The risks for investors are as follows: a) many borrowers may not be able to afford today's higher interest rates or payments on the buildings they bought 5 - 7 years ago b) investors may be forced into default and foreclosure c) owners might have to sell the properties at discounted prices below market to pay off the lenders d) the borrower might have to get a temporary bridge loan at a higher rate to avoid default and prevent losing the investment property. As stated earlier in the article, there are many positive advantages to investing in real estate. However, the greatest risks for real estate investors beyond their control are those associated with lending, particularly interest rate increases (Chen et al., 2022).

8.6. The Impact of Inflation on Investor Real Estate

Historically, inflation causes investment property rents to increase. In turn, as rents increase, so too does the building's cash flow and net operating income (NOI). Any increase in net income forces the property's value to rise, thereby building investor wealth over time. Many commercial and residential property owners have built in an automatic annual rent escalation of 3% to 4%. This escalation serves as a hedge against future rising costs throughout the lease term and facilitates property appreciation.

Furthermore, real estate investors should consider today's purchasing power of a dollar and the future value of money, as shifts in inflation can impact real estate values over a 5- to 25-year period. For example, the average price of a gallon of gas in the United States in 1975 was \$0.53. In March 2025, the average price of gasoline in America was around \$3.10 per gallon. That is a 585% increase in 50 years.

9. Modifications to the Investment Model

Technology has been rapidly adopted in both the residential and commercial real estate markets. Online 360-degree virtual and augmented reality video tours were innovations quickly adopted by the global real estate companies during the COVID-19 Pandemic (Naeem et al., 2023). Drones, sensors, and new housing construction using 3D and 4D printers are being used to reduce development and

emission costs associated with construction (Elmousalami et al., 2025). Artificial intelligence (AI) is being used to create property assessments, improve property management processes, and analyze historical data (Deppner et al., 2023; Veluru, 2023). Machine learning (ML) and dynamic factor modeling are being developed using extensive databases generated from multiple listings, property ownership data, tenant research (Bytautè, 2024), and sales data (Mottaghi et al., 2024; Veluru, 2023). Machine learning is also being used to evaluate and create credit assessments for potential buyers and sellers (Anchoe, 2025).

In particular, dynamic factor modeling, developed by researchers van de Minne et al. (2020), uses 80 granular, nonoverlapping commercial property price indices in time series to project property prices and market index returns. These emerging tools rely on access to data repositories, thereby increasing the ability to analyze and understand the benefits and risk factors associated with a changing real estate investment market.

10. Opportunities: Case Studies of Cashout Refinance-Investor Tax Benefits

Many real estate investors grow their wealth by refinancing the equity they have built up in their properties. Earlier, I discussed buying investment property at a discount, making renovations on the property, increasing the rents, and driving up the original purchase price to an entirely new, much higher, appraised value. The method involves trading new debt for the increased equity in the higher-value renovated property.

For instance, an investor who owns a \$5 million shopping center and owes a balance of \$1 million could leverage that property to a 70% Loan-to-Value (LTV) ratio by doing a Cash-Out Refinance. The investor would obtain a new loan of \$3.5 million and, after paying off the original \$1 million loan balance, would receive a \$2.5 million cash-out at closing. The IRS would consider the \$2.5 million from the refinance as a “loan” and would not immediately be subject to capital gains or income tax. Perhaps in 10 or 20 years, the investor may have to pay capital gains on the cash-out proceeds if they sell that shopping center and a) put the money into savings bonds or the stock market, or b) do not reinvest the money in another property using a 1031 exchange. In the meantime, the investor has the use of the money (tax-free) to buy other investment real estate and continue the same wealth-building cycle over and over for many years.

Another example is a real estate investor friend who purchased a neighborhood strip center in Manatee County, Florida, in June 2020 for \$1.1 million. After making approximately \$400,000 in improvements, increasing the rents, and leasing up the property to 100% occupancy, the property was appraised in the Fall of 2024 for \$4,000,000. That is a \$2.5 m –167% gain in 4 years. Another investor I know purchased an office building in Florida in 1995 for \$175,000 and sold it in 2024 for \$887,000 (Manatee County Property Tax, 2025). That was a 407% gain! This increase is how real estate millionaires are made in America!

11. Finding and Conclusion

In conclusion, real estate investment remains a prominent and valuable avenue for building wealth, offering both substantial opportunities and significant risks. While the market presents various advantages for real estate investors to achieve financial success, such as leveraging debt for property acquisitions, utilizing tax benefits, and benefiting from long-term appreciation, it also requires careful consideration of internal and external risks. Effective management, including prudent debt management, property oversight, and adaptation to market conditions, plays a crucial role in mitigating risks. Additionally, factors beyond an investor's control, such as economic shifts, interest rate fluctuations, and natural disasters, can significantly impact property values and returns. The integration of emerging technologies, such as artificial intelligence and machine learning, in real estate valuation offers new potential for informed decision-making; however, challenges remain in their adoption. Ultimately, real estate investment success relies on a blend of strategic planning, informed risk-taking, and the ability to navigate both market fluctuations and evolving technological advancements. Investors must approach real estate with a clear understanding of both the rewards and the risks, ensuring that their strategies are adaptable to the changing dynamics of the global economy.

Conflicts of Interest

The author declares no conflicts of interest regarding the publication of this paper.

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