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Shifting Dynamics in the CRE Lending Market

Ongoing structural changes and shifts in market share among providers of capital are creating a fluid opportunity set across the commercial real estate (CRE) credit market. Managers with an opportunistic bent could be well suited for the current dynamic market environment, operating with agility in areas where traditional financial sources of capital are less adaptable, either due to complexity, speed or limitations in structuring flexibility. In this report, we explain the dynamics of the CRE market and discuss what we consider differentiated opportunities within real estate credit.

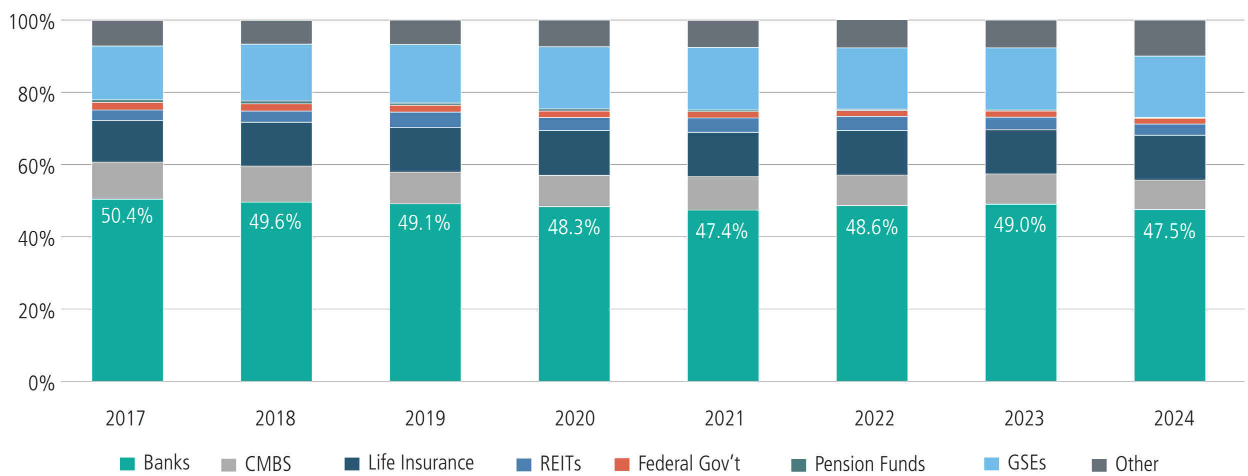
The $6 trillion commercial real estate (CRE) lending market[1] has seen banks steadily cede market share over time, though they still represent roughly half the market. Even small shifts in market share are significant, with every 1% change equating to $60 billion—making it critical, in our view, for investors to understand and anticipate these trends. While commercial mortgage-backed securities (CMBS) have also contributed to share losses, the primary beneficiaries have been non-banks, life insurance companies and government-sponsored entities (GSEs), particularly in the multifamily sector. Life insurers have maintained consistent participation, while non-banks have expanded their footprint, especially in floating rate loans.

We believe that the ongoing structural changes and the resulting shifts in market share among providers of capital will continue to create a fluid opportunity set across various segments of the real estate credit market. In our view, managers with an opportunistic bent are well suited for the current dynamic market environment and can operate with agility in areas where traditional financial sources of capital are less adaptable, either due to complexity, speed or limitations in structuring flexibility.

In this report, we explain the dynamics of the CRE market and discuss what we consider differentiated opportunities within real estate credit.

Key Trends

CRE DEBT MARKET SHARE



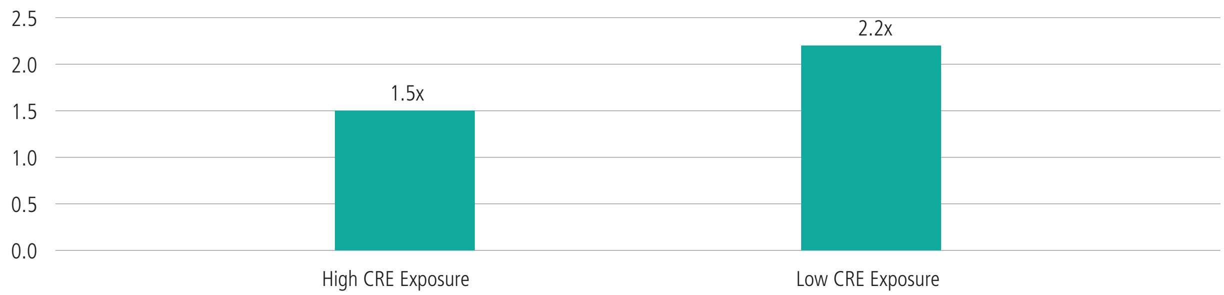
Source: KBW Research, as of December 31, 2024. For illustrative purposes only. Historical trends do not imply, forecast or guarantee future results. Due to a variety of factors, actual events or market behavior may differ significantly from any views expressed. **Past performance is not indicative of future results.**

As discussed above, for reasons including the adaptability required in today's market and valuation considerations at banks, borrowers are increasingly turning to non-bank solutions. In our opinion, private lenders are well positioned to continue filling the funding gap, offering tailored and flexible solutions to meet the evolving demands of the CRE market.

[1] Source: KBW, as of December 31, 2024.

CRE EXPOSURE WEIGHS ON BANK PRICE/TANGIBLE BOOK VALUE MULTIPLES

Ratios for Banks With High and Low Exposures

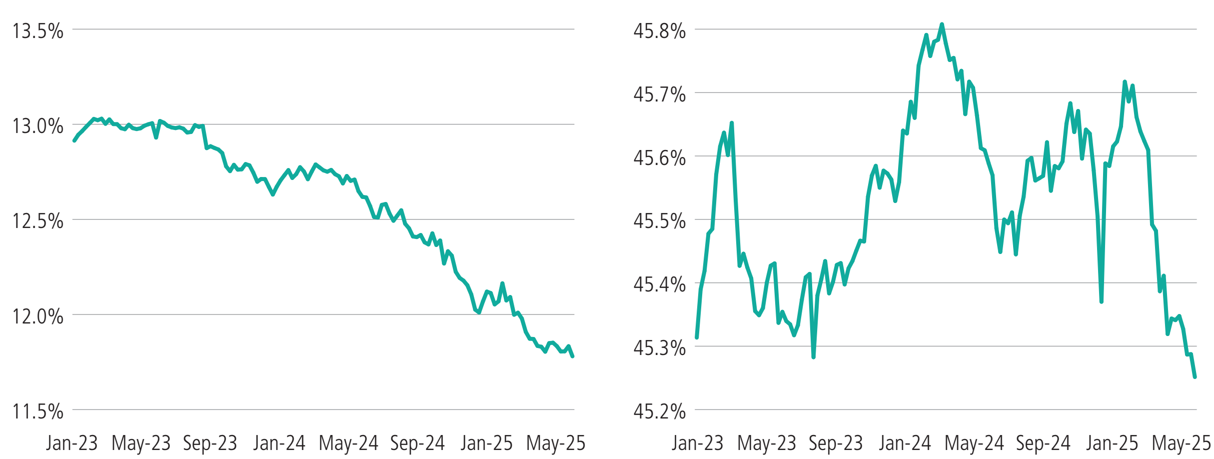


Source: FactSet and KBW Research for CRE/Total RBC %. "High CRE Exposure" and "Low CRE Exposure" categorize banks into the highest and lowest quintiles by CRE/Total RBC % based on regulatory data as of December 31, 2024. Analysis includes the top 100 banks by market cap as of June 30, 2025, excluding GS, MS, STT, BK and NTRS.

BANKS HAVE BEEN DE-EMPHASIZING THEIR DIRECT CRE EXPOSURE…

Large Banks: CRE % Total Loans

Small Banks: CRE % Total Loans

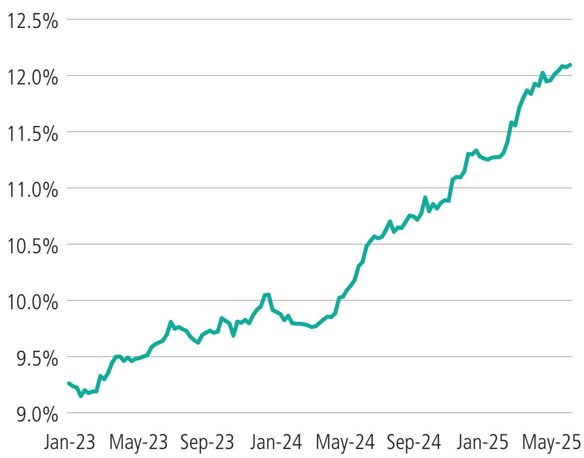


Source: Federal Reserve. Data as of June 18, 2025. For illustrative purposes only. Historical trends do not imply, forecast or guarantee future results. Due to a variety of factors, actual events or market behavior may differ significantly from any views expressed. **Past performance is not indicative of future results.**

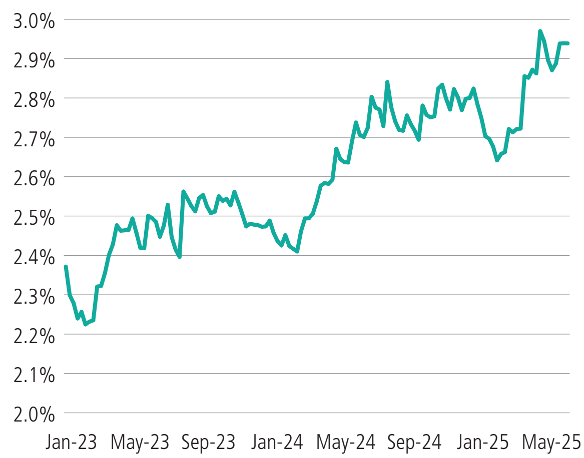
Notably, we have observed that banks, particularly the largest banks in the U.S., are increasingly shifting their focus in real estate by providing financing to private market players. This trend is reflected in the weekly Federal Reserve data, which shows material growth in lending to non-depository financial institutions, highlighting banks' preference for indirect exposure to various sectors, including real estate.

… ON THE FLIP SIDE, BANKS ARE INCREASING THEIR EXPOSURE TO NON-BANK FINANCIAL INSTITUTIONS

Large Banks: Loans to NBFIs % Total Loans



Small Banks: Loans to NBFIs % Total Loans

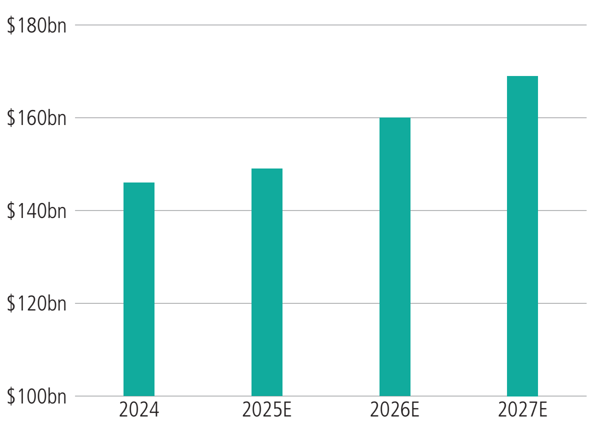


Source: Federal Reserve. Data as of June 18, 2025. For illustrative purposes only. Historical trends do not imply, forecast or guarantee future results. Due to a variety of factors, actual events or market behavior may differ significantly from any views expressed. **Past performance is not indicative of future results.**

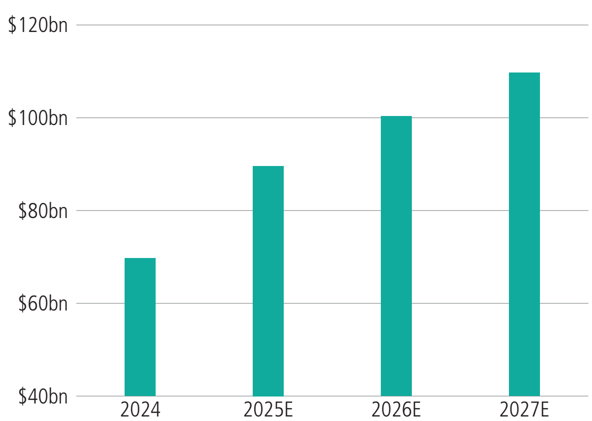
We acknowledge that an improving regulatory environment is beneficial for banks, and it may enable them to recoup some of the market share they have ceded in recent years. However, we do not anticipate a dramatic reversal, as the relationship between banks and private market lenders has become increasingly symbiotic rather than adversarial. Notably, the largest U.S. banks (many of which have transformed their business models over the years) are generating record earnings, with a significant portion of excess capital being allocated to share buybacks as opposed to organic or inorganic opportunities. Indeed, from a public market perspective, the current state of play at the banks is by and large viewed favorably by equity investors, and bank stocks have meaningfully outperformed the broad market over the past 12 months.

RECORD EARNINGS AND ROBUST CAPITAL RETURNS AMONG U.S. GSIBs

U.S. GSIBs: Total Annual Earnings



U.S. GSIBs: Total Annual Buybacks



Source: Company filings, FactSet, VisibleAlpha. Data as of June 30, 2025. Figures for 2025 – 2027 are consensus estimates. U.S. Global Systemically Important Banks (GSIBs) = BAC, BK, C, GS, JPM, MS, STT and WFC. U.S. GSIB Total Annual Earnings in 2024 excludes $6 billion one-time Visa gain at JPM. For illustrative purposes only. Historical trends do not imply, forecast or guarantee future results. Due to a variety of factors, actual events or market behavior may differ significantly from any views expressed. **Past performance is not indicative of future results.**

BANK STOCKS HAVE MEANINGFULLY OUTPERFORMED BROAD EQUITY BENCHMARKS

Total Return, Past 12 Months

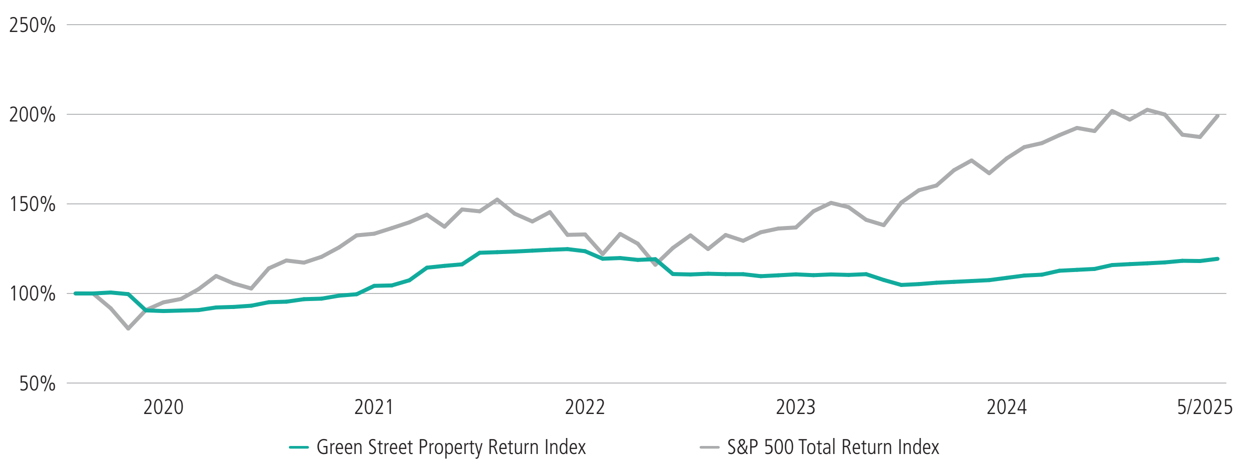
Source: FactSet. Data as of June 30, 2025. **Past performance is not indicative of future results.**

The Case for Real Estate

As highlighted by our colleagues in their recent paper, *Real Estate: Uncovering Value Amid Uncertainty*, real estate currently stands out as a particularly attractive asset class for several reasons. First, it begins from a more reasonable relative value position than many other asset classes, with a large portion of the sector's challenged assets already addressed, creating a stronger foundation for future lending and investment. Additionally, rising tariffs, material costs and persistent labor shortages are constraining new development, particularly in North America and Europe, which reinforces the scarcity value of existing assets. This combination of relative value and supply constraints presents lenders and investors with unique opportunities to deploy capital in a "less stretched" sector.

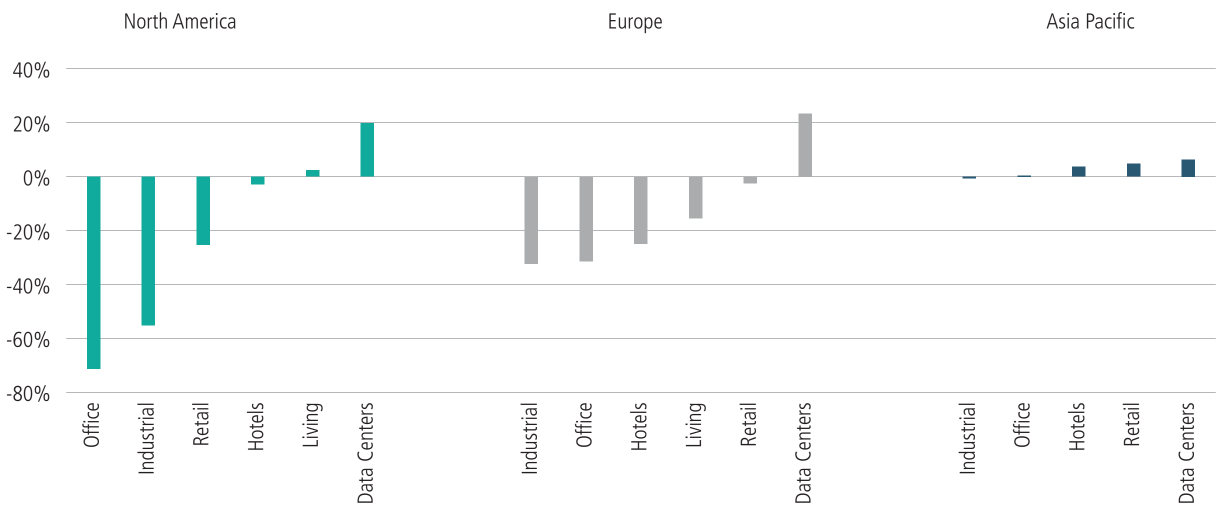
COMMERCIAL PROPERTY HAS MEANINGFULLY UNDERPERFORMED PUBLIC MARKETS

Indexed to 100 at Year-End 2019



Source: Bloomberg, Green Street. Data as of May 30, 2025. For illustrative purposes only. Historical trends do not imply, forecast or guarantee future results. Due to a variety of factors, actual events or market behavior may differ significantly from any views expressed. **Past performance is not indicative of future results.**

2025 FORECAST COMPLETIONS VS. 2021 – 2024 PEAK (%)



Source: JLL, *Global Real Estate Outlook 2025*. For illustrative purposes only. Historical trends do not imply, forecast or guarantee future results. Due to a variety of factors, actual events or market behavior may differ significantly from any views expressed. **Past performance is not indicative of future results.**

The Case for Real Estate Debt

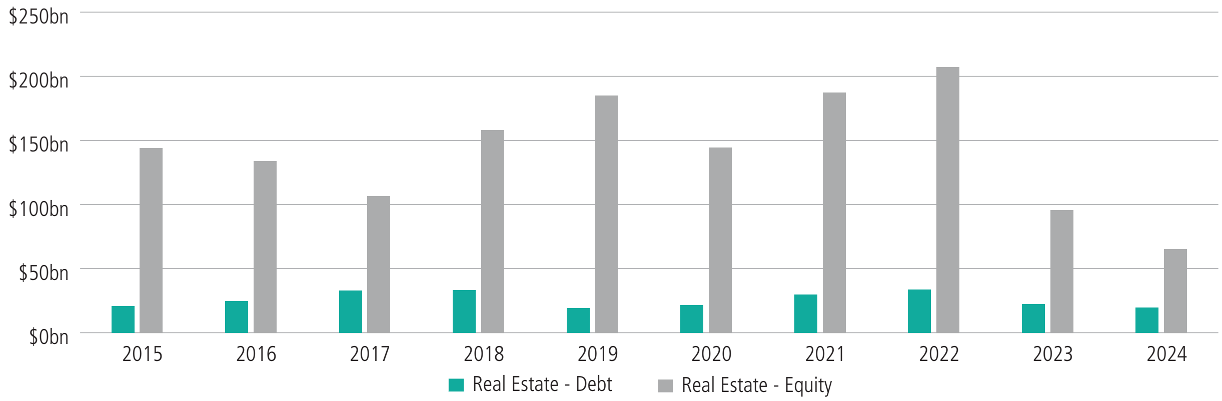
Real estate debt offers several characteristics that we believe make it appealing to institutional investors. First-lien loans, which often represent the core of the real estate debt capital stack, typically feature conservative loan-to-value (LTV) ratios of around 65% and floating rates, providing meaningful downside protection against declines in property values. Beyond first-lien loans, customized financing solutions are increasingly being used to address the entire capital stack. These structures are designed to meet more complex borrower needs while offering investors opportunities to achieve attractive risk-adjusted returns. This diversity of financing structures allows investors to tailor their strategies to specific market conditions and borrower profiles.

While real estate debt has historically played a complementary role to equity in institutional portfolios, its risk-return characteristics and emphasis on downside protection distinguish it from equity-focused strategies, which often aim to capture value through property appreciation and active asset management.

Fundraising trends reflect this distinction, with real estate debt historically representing about 20% of the capital raised for real estate equity.[2] This balance underscores the broader appeal of equity investments for those seeking higher potential returns, while highlighting the stability and diversification benefits that debt can provide, particularly during periods of market dislocation.

[2] Source: PitchBook. Data as of December 31, 2024.

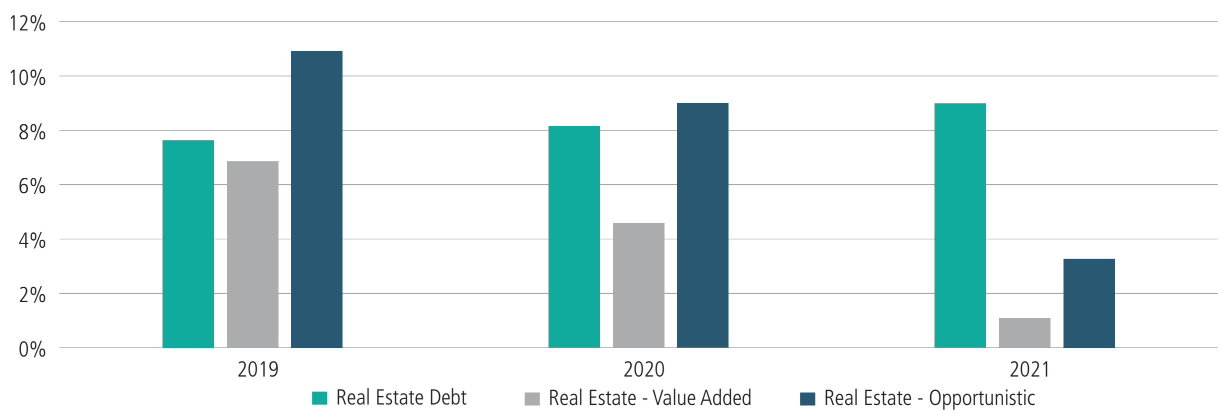
REAL ESTATE FUNDRAISING ACTIVITY



Source: PitchBook. Data as of December 31, 2024. For illustrative purposes only. Historical trends do not imply, forecast or guarantee future results. Due to a variety of factors, actual events or market behavior may differ significantly from any views expressed. **Past performance is not indicative of future results.**

Performance data further illustrates the resilience of real estate debt. In general, real estate debt-focused funds delivered more consistent returns and, during the 2019 – 2021 vintage, in some cases outperformed real estate equity-focused funds. However, equity investments continue to play a critical role for investors seeking long-term growth and direct exposure to property appreciation.

INTERNAL RATE OF RETURN BY VINTAGE



Source: PitchBook. Data as of September 30, 2024. Return metrics are median and net of fees and carry. For illustrative purposes only. Historical trends do not imply, forecast or guarantee future results. Due to a variety of factors, actual events or market behavior may differ significantly from any views expressed. **Past performance is not indicative of future results.**

Opportunity Set and Themes

As mentioned, we believe the combination of ongoing shifts in the provisioning of capital, along with a significantly improved transaction outlook and more attractive valuations, is creating a rich and evolving opportunity set across different segments of the real estate credit market. While the availability of capital may vary by sector, type and loan-to-value (LTV) ratio, we find that the most compelling opportunities reside in the "in-between" space: segments of the market not typically served by traditional forms of lending. Two such opportunities are **transitional financing** and **NAV loans.**

Transitional financing. We believe this is one of the most appealing categories within real estate credit, and is the direct result of the shift of supply/demand dynamics among credit providers. In particular, for assets that are not yet fully stabilized, banks and other traditional senior lenders are often willing to finance only a portion of the total loan amount, typically at lower loan-to-value ratios. Private credit managers can then provide additional financing to complete the capital stack. Many of these opportunities are underwritten at lower LTVs than would have historically been the case and at higher spreads, resulting in equity-like return potential with credit-like risk features, in the form of subordination, strong collateral package and covenants.

NAV loans. While traditionally NAV loans have been a more common feature for private equity portfolios (see *Navigating Private Credit's Next Act*), we have found very compelling opportunities in real estate-related net asset value (NAV) loans. The opportunity is underpinned by a combination of limited liquidity events and low distributions to limited partners, as well as constrained financing at the underlying asset level. With very conservative LTVs, often ranging in the 20 – 30% range, investors with a flexible investment mandate and underlying asset know-how are able to seek what we believe to be compelling excess return potential for the risk undertaken. Yields range from the low to mid-teens, often featuring a payment-in-kind element to provide flexibility to the general partner/real estate owner. Just like NAV loans structured on private equity portfolios or other underlying assets, we believe that the opportunity set is likely to shift with the market cycle, and the pressing need to return capital to investors may lessen when exit activity reverts to its historical mean.

Conclusion

In our view, the market dynamics noted above are creating some of the most compelling opportunity sets across CRE credit in years. We believe CRE credit should be an integral part of investors' portfolios, potentially delivering significant diversification benefits, downside protection and yield enhancement without relying on a directional view on valuation given conservative LTVs. While investors can access the asset class by focusing on a single sector, or single strategy, we believe that a flexible multi-sector approach is particularly suited to respond to shifts in market conditions and sector dynamics, allowing investors to approach the asset class within an all-weather mindset.

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