Real Estate Research

November 2026

Europe Real Estate Debt Strategic Outlook

November 2026

IN A NUTSHELL

- Real estate debt market remains open and functional, but declining liquidity, geopolitical uncertainty and higher rates drive greater bifurcation across assets and borrowers.
- Bank lenders remain selective, with tighter underwriting, longer approval processes and higher equity requirements.
- We do not expect a wall of distress, but higher-for-longer rates should create more forced sales, restructuring, recapitalisation and discounted CRE loan opportunities.
- New lending remains potentially attractive, supported by higher base rates, stable margins and disciplined underwriting.
- Rising bank funding costs could narrow the pricing gap between banks and debt funds as leverage and complexity requirements increase.
- At the sector level, we favour selected opportunities in logistics, healthcare and hotels, while becoming more positive on food-anchored retail and well-located offices with leasing upside.

Current Market Conditions

Debt capital remains available, but no longer on uniform terms

European debt markets remain functional, particularly for high-quality assets with stable cash flows and conservative leverage. However, financing conditions have become increasingly differentiated as geopolitical uncertainty and higher interest rates have reinforced lender selectivity. Banks, debt funds and insurance lenders continue to provide financing across most sectors, but underwriting has become more conservative, approval processes more demanding and execution less predictable. Refinancing continues to account for a large share of lending activity, while acquisition financing is gradually returning for high-quality assets

Capital availability increasingly depends on asset quality, leverage and the underlying business plan. Liquidity remains comparatively strong for prime and well-capitalised transactions, while more complex or weaker assets face a narrower lender universe and more restrictive financing terms. Banks in particular are placing greater emphasis on risk mitigation and existing borrower relationships, contributing to growing demand for alternative and mezzanine capital where conventional senior leverage is more constrained.

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Higher Rates, Rather Than Margins, Drive Borrowing Costs

Higher long-term government bond yields and swap rates remain the key pressure on financing costs. Lending margins have generally remained comparatively stable, with competitive pressure even supporting margin compression in selected segments. As a result, higher underlying interest rates, rather than a broad deterioration in credit pricing, are currently the main driver of elevated all-in borrowing costs. Higher debt costs continue to challenge debt accretion, reinforcing the importance of assets with resilient cash flows, rental growth potential and strong operational fundamentals.

Real Estate Fundamentals Remain Supportive

Despite more challenging capital-market conditions, the underlying real estate picture remains comparatively resilient. Transaction activity in Europe dropped by 24% in the first three quarters YOY, but occupier fundamentals remain broadly supportive and limited development pipelines constrain new supply.[1] Capital continues to favour sectors and assets with visible income growth and strong operating fundamentals, while weaker occupational performance, higher capital expenditure requirements and limited liquidity can increasingly translate into more challenging financing conditions. This divergence between broadly available debt capital and increasing asset-level selectivity sets the backdrop for a more differentiated European lending market.

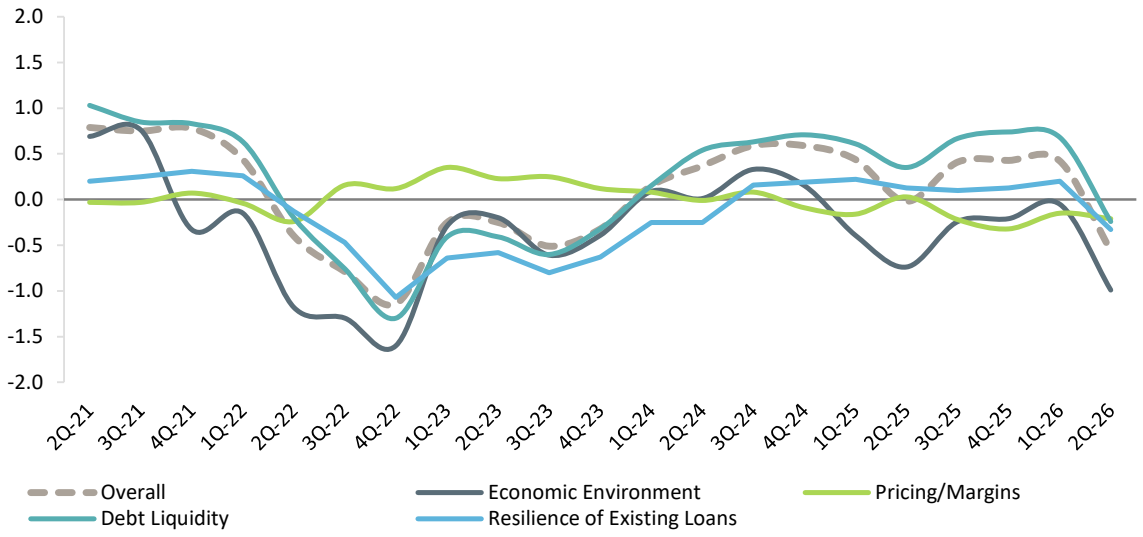
Market Sentiment

Lender Sentiment Weakens, Capital Availability Endures

European real estate debt markets have entered a more cautious phase as geopolitical uncertainty, renewed inflation concerns and a less supportive interest-rate outlook weigh on lender sentiment. The CREFC Europe Sentiment Survey shows a sharp deterioration across most indicators in Q2 2026.[2] Overall sentiment fell from 0.42 in Q1 to -0.56, while views on the economic environment declined more markedly from -0.05 to -0.99. Debt liquidity also moved into negative territory, although the deterioration primarily reflects weaker expectations and greater uncertainty rather than an absence of financing capacity.

European Commercial Real Estate Debt Market Sentiment

Selected Sentiment Indicators



Source: PEI, PERE, CREFC, June 2026

[1] MSCI RCA, Capital Trends Europe, Q3 2026
[2] PEI, PERE, CREFC, June 2026

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Despite weaker sentiment, lending markets remain broadly supportive. Capital continues to be available across banks, debt funds and alternative lenders, while competition remains strong for high-quality, low-leverage transactions. The key constraint is therefore increasingly where lenders are willing to deploy capital rather than the overall availability of debt. Refinancing risk remains more pronounced for lower-quality and more capital-intensive assets, reinforcing the increasing differentiation by asset quality, leverage and business plan.

Germany illustrates this divergence between cautious sentiment and improving financing conditions. The German real estate financing index (DIFI) remained negative at -8.0 in Q2 2026, but its forward-looking component improved to -0.3.[3] At the same time, LTVs increased across major asset classes and financing margins for Value-Add transactions compressed, pointing to renewed lender appetite and competition for selected opportunities even against a still-challenging market backdrop.

Weaker sentiment has not translated into a broad shortage of debt capital. Instead, lenders are becoming increasingly selective, with pricing, leverage, asset quality and borrower strength playing a greater role in determining access to financing.

Credit Conditions

Loan Pricing Increasingly Reflects Leverage and Risk

European CRE lending margins have remained relatively stable overall, but headline averages mask significant differences across leverage levels and markets. Competition remains particularly strong for prime, low-leverage financing, where abundant liquidity has supported further margin compression. In parts of continental Europe, however, pricing becomes increasingly differentiated as leverage rises, with higher-LTV financing commanding a more pronounced premium.

The UK provides a notable contrast. Strong lender competition and improving liquidity have driven margin compression across the leverage spectrum, including at higher LTVs. Debt funds became the largest source of residential and commercial development finance in H1 2026, with around 32% of debt fund lending directed towards development projects.[4] Strong competition for deployment has compressed margins particularly in residential development, where pricing fell from 479 bps to 447 bps, while commercial pre-let development margins declined by 19 bps to 364 bps. The UK therefore illustrates that higher leverage does not necessarily translate into wider margins where lender appetite and capital availability remain strong.

In continental Europe, this differentiation is also supported by structural differences in bank funding and capital economics. A less supportive funding environment and rising liquidity costs can constrain further margin compression at higher leverage, creating a potentially more durable opportunity for private credit.

Access to capital for assets and structures outside the prime, low-leverage, “plain-vanilla” segment has therefore become generally more constrained, costly and complex. We believe this reflects more than a cyclical adjustment. Funding costs, regulatory requirements and bank capital economics can increasingly influence competitiveness as leverage and complexity rise, creating a potentially durable opportunity for alternative lenders.

[3] JLL & HWWI, DIFI Report Q2 2026
[4] Bayes Business School, Market Survey, October 2026

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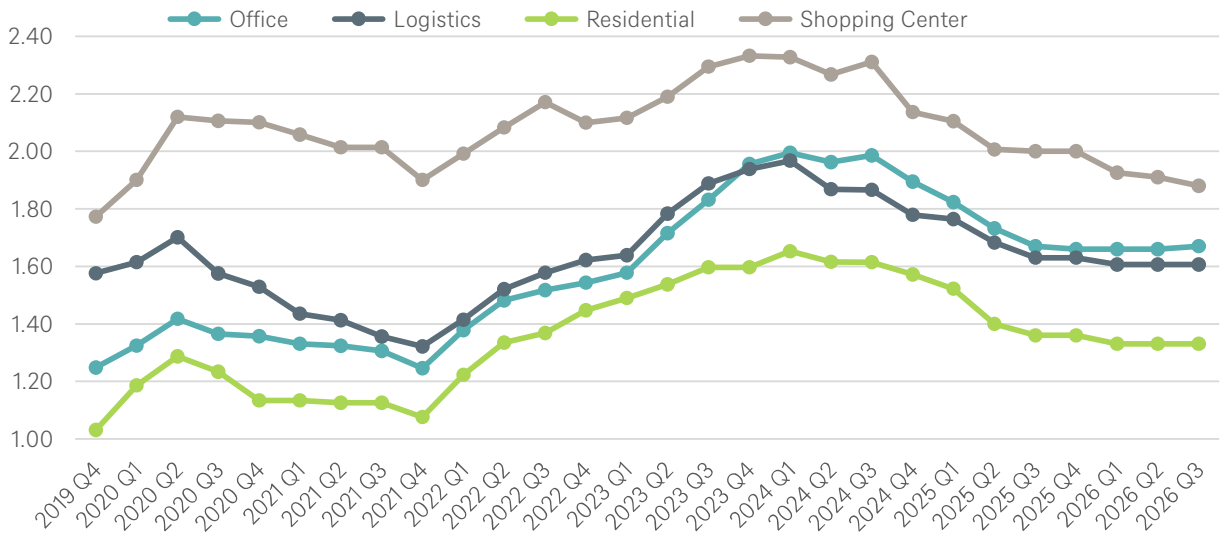
Weighted Average European Prime Senior Lending Margins All Properties (%)



Source: DWS, November 2026

Structural Constraints Create Opportunities for Alternative Lenders

The Bank Funding Advantage Narrows as Leverage and Complexity Rise

The growing bifurcation in European CRE loan pricing reflects not only differences in risk appetite, but also the funding and regulatory constraints facing traditional bank lenders. Germany's Pfandbrief market provides a useful illustration. Banks retain a significant funding advantage in prime, low-leverage lending, but structurally higher sovereign yields and higher refinancing costs have reduced some of the support provided by the exceptionally low-cost funding environment of the previous cycle. This pressure has recently become more visible in covered-bond markets, with Pfandbrief spreads for maturities of around two years widening sharply to approximately 42–49 bps over German government bonds in early October 2026. A sustained increase in Pfandbrief funding costs could limit further compression in bank CRE lending margins and narrow the relative pricing gap with private credit.

These economics become more pronounced as leverage increases. Under the German Pfandbrief framework, covered-bond funding is subject to conservative mortgage lending value requirements, with only the portion of a mortgage loan within 60% of the mortgage lending value eligible for inclusion in the cover pool. As leverage extends beyond the portion that can be efficiently funded through the Pfandbrief market, banks increasingly need to rely on other funding sources and capital, potentially making higher-leverage lending less economically attractive. This contributes to the pronounced differentiation in loan pricing across the LTV spectrum: traditional banks remain highly competitive for prime, low-leverage financing, while private lenders can become increasingly competitive further up the risk curve.

This creates a structural opportunity for alternative lenders, particularly where transactions require higher leverage, greater complexity or more flexible execution. core-plus, value-add and development strategies can require financing structures that sit outside standardised bank lending parameters. Here, borrowers may place greater value on certainty and speed of execution, tailored structures and the ability to accommodate more complex capital requirements. As a result, competition between banks and private lenders increasingly extends beyond headline pricing to the broader financing proposition.

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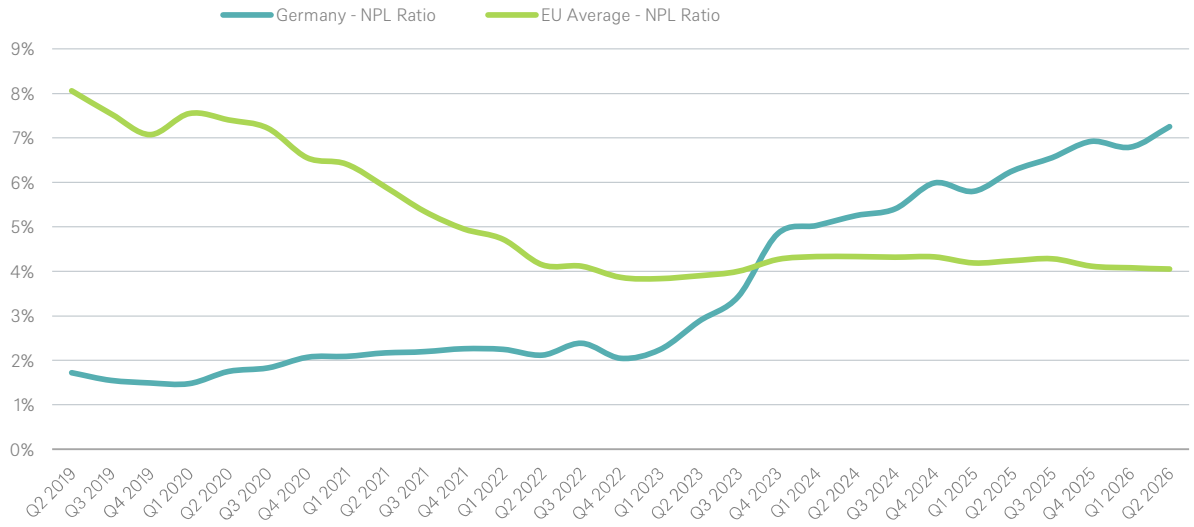
Commercial Real Estate NPL ratio



Source: BKS, EBA Risk Dashboard, October 2026

For real estate debt investors, this can create potentially attractive lender economics. Capital scarcity in more complex segments can support not only margins, but also stronger documentation, greater structural protection and increased selectivity over assets and borrowers. Private credit therefore complements rather than replaces traditional bank lending: banks remain difficult to compete with at the safest end of the market, while alternative lenders can occupy an increasingly important role as leverage, complexity and execution requirements increase.

Existing Loan Books Remain Under Pressure

While the European banking sector has largely worked through the NPL legacy of previous crises, credit stress is re-emerging in commercial real estate. The overall EU NPL ratio remained low at 1.8% in Q2 2026, while CRE presented a more challenging picture: approximately €58 billion of European CRE loans were classified as non-performing, equivalent to a CRE NPL ratio of around 4.0%.[5] Germany has emerged as a particular hotspot. The country's CRE NPL ratio increased from 2.2% in Q1 2022 to 7.2% in Q2 2026, well above the 4.0% European average. German banks now hold around €17 billion of non-performing CRE loans, accounting for almost one-third of the European total.

Several factors help explain Germany's divergence. German banks, particularly Pfandbrief banks, Landesbanken and specialist property lenders, have historically maintained sizeable international real estate exposures, including to the US and UK. As a result, deterioration in overseas commercial real estate markets has also fed into sector-specific NPL ratios reported by German lenders. At the same time, the sharp increase in financing costs since 2022 coincided with a significant repricing of German commercial real estate, where previously low property yields amplified the impact of higher interest rates on valuations. The office sector has been particularly exposed, as higher refinancing costs, softer occupier fundamentals in some markets and more conservative valuations have put additional pressure on loans originated against substantially higher property values.

[5] EBA Risk Dashbord Q2 2026, October 2026

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Legacy Loans Are Creating Refinancing Gaps

Much of today's credit stress reflects the delayed transmission of the interest-rate and property-price correction into existing loan books. Loans originated during the low-interest-rate environment are increasingly approaching maturity in a very different financing and valuation landscape. Lower collateral values increase effective LTVs, while higher refinancing costs weaken debt-service metrics. As a result, some borrowers face refinancing or equity gaps where the original debt quantum can no longer be refinanced on comparable terms.

The challenge is particularly pronounced for secondary and transitional assets, older offices and properties requiring significant capital expenditure, where weaker fundamentals can compound refinancing pressure. There are also indications that some credit deterioration has yet to translate into outright defaults. At the broader loan-book level, Germany's Stage 2 ratio reached 15.3% in Q2 2026, compared with 8.9% across the EU. Germany's elevated Stage 2 ratio signals a broad deterioration in credit quality, but not an equivalent volume of imminent defaults. Stage 2 exposures remain performing and may return to Stage 1 if credit conditions improve. Nevertheless, the ratio indicates a sizeable pipeline of loans requiring closer monitoring, additional borrower equity or restructuring as maturities approach.

Resolution Is Likely to Remain Gradual

The rise in Stage 2 and non-performing exposures points to a growing pipeline of stressed loans, but not necessarily to a simultaneous wave of forced sales. Loan maturities are staggered, many assets continue to generate income and banks generally have incentives to pursue extensions, restructurings or additional equity contributions before enforcing collateral. At the same time, regulatory provisioning requirements and the capital cost of carrying weak exposures limit the scope for indefinite extensions. We therefore expect a prolonged workout phase characterised by a gradually increasing flow of recapitalisations, restructurings and selective loan or asset sales, rather than a single systemic distress event.

A Growing but Highly Selective Opportunity for Private Capital

For real estate debt investors, this creates a potentially attractive but highly selective opportunity set. Refinancing gaps and the gradual resolution of legacy exposures should increase demand for private credit, mezzanine capital and restructuring solutions, particularly where borrowers cannot provide additional equity or existing debt requires a write-down. Germany stands out because the adjustment has been particularly pronounced, but opportunities are likely to emerge asset by asset rather than through a broad distressed cycle. This should favour lenders with the ability to underwrite complex situations, establish strong control rights and provide flexible capital through the workout process.

Investment Strategy

Selective Opportunities Across New Lending and Legacy Loans

In this environment, sector selection alone is not sufficient. We believe the most attractive lending opportunities combine sustainable entry values, resilient in-place cash flows, credible business plans and meaningful borrower equity. Structural protections, covenant packages and conservative attachment points remain particularly important where asset performance depends on leasing, repositioning or capital expenditure.

We see attractive opportunities across both new origination and the gradual refinancing of legacy loan books. In primary markets, higher base rates, conservative underwriting, lower entry valuations and increased borrower equity contributions can support attractive risk-adjusted lending economics. In secondary and restructuring situations, refinancing and recapitalisation gaps should create selective opportunities to provide flexible capital without requiring a broad distressed cycle.

We continue to favour whole-loan strategies and first-ranking transitional loans backed by well-located assets where leasing, repositioning or capital investment can support cash-flow growth. These strategies can combine attractive all-in spreads with downside protection through disciplined attachment points and structuring rather than additional leverage.

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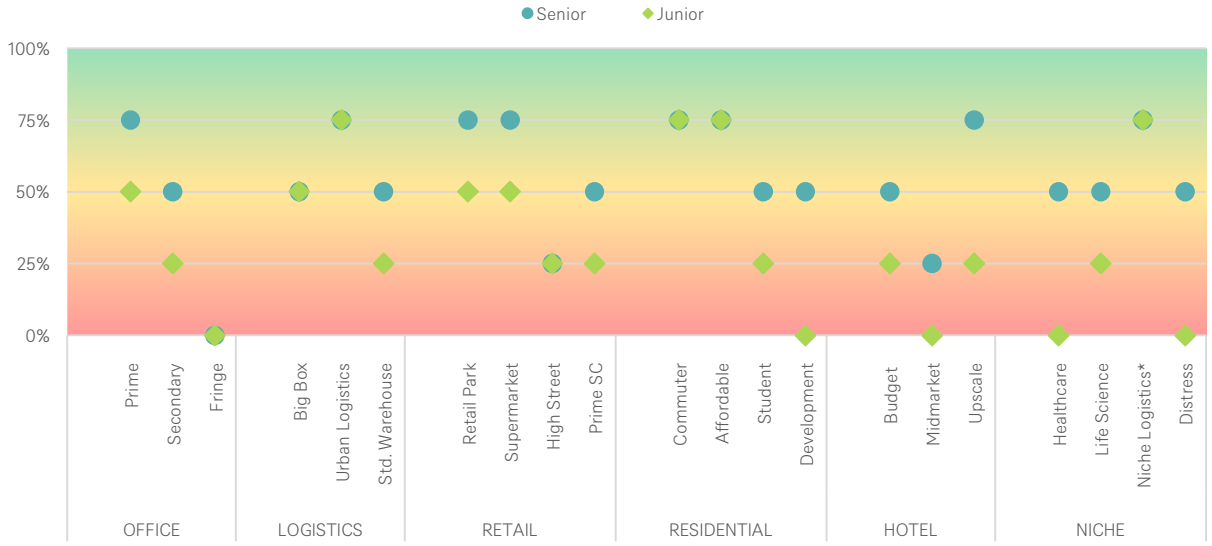
Private Debt Strategies by Subsector (Level of Conviction, %)



*Cold Storage, Self-Storage, Airport Logistics

Source: DWS, November 2026

Key changes to our research view

New themes: Healthcare added as structural growth sector, alongside selective distressed opportunities.

Upgrades: Upscale hotels, retail parks and supermarkets. Downgrades: High-street retail due to rate sensitivity.

Offices: Strong polarisation creates selective lending opportunities. Focus on well-located offices with vacancy or under-rented space, where asset management can drive income and value growth. Increasing polarisation by location and quality continues to support prime rental growth, potentially reinforced by AI-driven demand and competition for best-in-class space in key growth cities. In contrast, we remain cautious on secondary assets and non-CBD locations, where weaker occupier demand and refinancing risks offer less downside protection for lenders.

Logistics: Increasingly attractive as fundamentals strengthen. We remain positive on European logistics, which is among our preferred sectors for rental growth. Improving economic momentum, a recovery in manufacturing activity and continued e-commerce demand are supporting occupier fundamentals, while declining construction starts and low vacancy in key markets provide a favourable supply backdrop. From a debt perspective, we particularly favour assets in defensive, supply-constrained locations, where resilient demand and limited new development provide stronger downside protection.

Hotel: Travel demand remains robust and limited new supply supports fundamentals, with RevPAR growth expected to modestly outpace inflation. However, larger pipelines in selected markets and rising labour and energy costs pose downside risks. We favour upscale hotels for their stronger pricing power and are increasingly positive on upscale resorts, supported by structural leisure demand, scalability and a growing pool of creditworthy operators.

We are more cautious on selected budget and midmarket hotels given greater customer price sensitivity and more limited pricing power. From a debt perspective, however, budget hotels can offer defensive characteristics through simpler operating models, lower replacement costs and greater flexibility to switch operators, potentially reducing execution risk and supporting profitability at lower revenue levels.

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Retail: The sector has experienced one of the sharpest valuation corrections, while rental fundamentals appear to be stabilising. From a debt perspective, this creates more attractive lending opportunities where entry valuations are sustainable and covenant protection is strong. We favour food-anchored retail parks, supported by resilient cash flows, while prime shopping centres are back on the agenda where valuations adequately reflect structural risks. We remain cautious on high-street retail, where low initial yields, asset-specific reletting risk and potentially significant capital expenditure can leave valuations particularly sensitive to higher interest rates.

Residential: Attractive, but increasingly selective. Residential remains supported by structural demand and constrained supply, but affordability pressures, tight pricing and the greater interest-rate sensitivity of low-yielding assets require a more selective approach. Increasing regulation in markets such as Berlin and Madrid adds further complexity. We continue to favour affordable housing and commuter locations, alongside micro-apartments and operational residential, where structural demand and income growth potentially may provide greater resilience.

Niche sectors: We have a particularly positive view on healthcare, supported by structural demand from ageing populations, rising healthcare utilisation and evolving models of care delivery. Opportunities span elderly care as well as healthcare-related real estate such as medical offices, outpatient facilities and clinics. From a debt perspective, operator covenant strength, lease coverage, indexation and the availability of replacement operators are critical. We therefore favour assets combining structural demand with sustainable rent coverage and sufficient alternative-use or re-letting potential.

Distressed opportunities: Distressed opportunities are likely to emerge gradually rather than through a broad wave of forced sales. Higher refinancing costs, lower collateral values and growing capital expenditure requirements should create a sustained pipeline of recapitalisations, restructurings and selective loan or asset sales, particularly among legacy office exposures and transitional assets. We favour situations where the underlying real estate remains viable, the path to stabilisation is clearly identifiable and sufficient equity protection can be established. Success will depend on disciplined entry values, strong control rights and the ability to provide flexible capital through complex workout processes.

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