

CRE AND MULTIFAMILY FINANCE

IN THE SPOTLIGHT

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Private Credit – US and Europe

Private credit growth adds liquidity but heightens risk in CRE market



Summary

Although private credit has long financed commercial real estate (CRE), continued high interest rates and recent property value declines will drive more CRE borrowers to these nonbank lenders in the coming years. Private credit's growth – via both partnerships and in competition with traditional CRE lenders – has added to market liquidity by both (1) extending credit directly to borrowers and (2) absorbing higher-leverage loans from traditional lenders. However, private credit's involvement also heightens and adds new risks to the overall market.

- **Private credit is increasingly funding CRE.** US and European private credit investment funds – from real estate investment trusts (REITs), asset managers and other nondepository institutions – have raised approximately \$500 billion in investor capital for CRE debt investments over the past 13 years, including \$27 billion already this year.¹ Private credit funds also employ asset- and fund-level leverage, which further enhances their investment firepower. Of the current \$9 trillion of CRE mortgages outstanding in Europe and the US, we expect \$1 trillion will shift to private credit in the next three-to five years as traditional lenders deleverage.
- **Private credit plays a role in all phases of CRE lending, transferring and raising risks.** Private credit is involved in nearly every facet of the CRE market, crossing paths with traditional CRE lenders, investors and funding instruments. Each intersection heightens or creates new risks, but private credit's involvement in CRE also has its benefits, for both borrowers and traditional CRE lenders. Despite this ongoing shift in risk, traditional lenders and other entities we rate will remain exposed to some of the riskier CRE assets via warehouse lines (banks), joint ventures (banks and insurance companies), and feeder funds (insurance companies).

¹ As of June 25, 2025.

Private credit is increasingly funding CRE

As property prices in many CRE sectors declined and interest rates rose in the wake of the pandemic, private credit has increasingly stepped in to fund borrowers that no longer meet traditional lenders' standards.

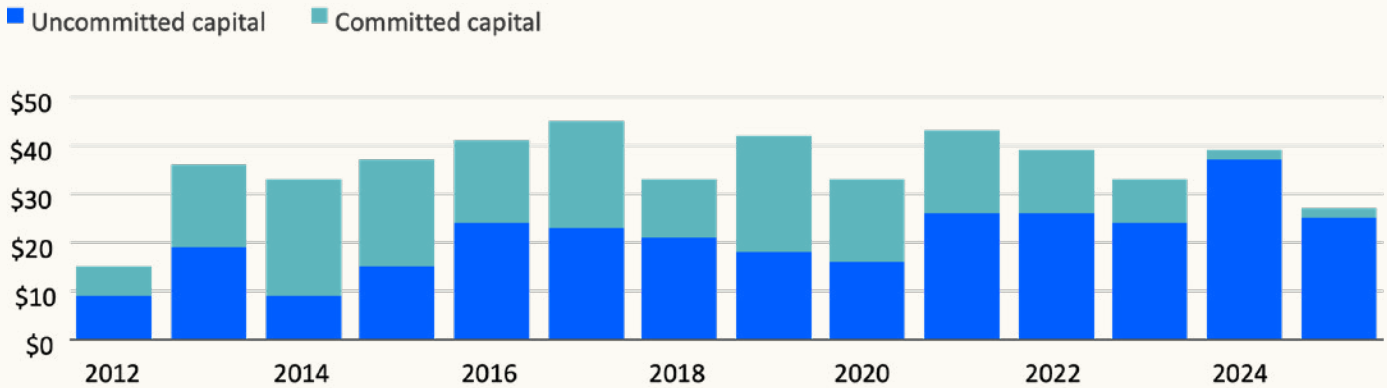
Since 2012, private credit funds – excluding insurance companies – have raised \$498 billion for CRE debt funds, including more than \$30 billion annually since 2013.

This pace has accelerated in 2025, with \$27 billion raised through 25 June (Exhibit 1). Private credit firms invest these funds in a number of ways, including (1) by directly originating, refinancing and buying loans, (2) via joint loan origination ventures, (3) investing in commercial mortgage-backed securities (CMBS) or residential mortgage-backed securities (RMBS), and (4) contractually through significant/credit risk transfer (SRT/CRT).

EXHIBIT 1

Private credit CRE fundraising at record pace in 2025

Private credit firms' CRE fundraising, by committed and uncommitted capital, in billions*



* Over five years, PERE reports the 50 largest US private credit funds raised \$174 billion as of year end 2024. The 2025 data bar is YTD as of 25 June. Excludes insurance companies.

PERE defines "committed capital" as the total amount pledged during the fund life, and "uncommitted capital" as the amount that has not been utilized by the fund.

Source: PERE Credit

Insurance companies have always been a major long-term private credit funding source for CRE borrowers because insurers use mortgage assets to match their longer-term liabilities. But in recent years, other types of private credit investment funds – mortgage REITs, asset managers and other nondepository institutions – have expanded their CRE involvement with a focus on higher-yield loans. This participation was assisted by the dislocation wrought by the 2008

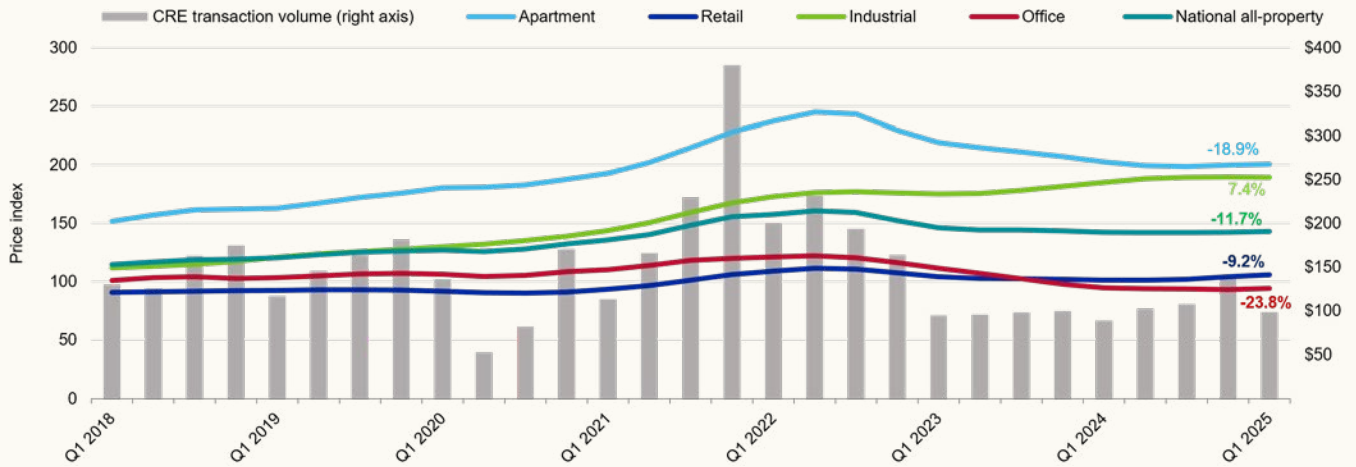
financial crisis and the 2020 pandemic, as those events provided openings for them to grow and lend on more-stable CRE properties. Exhibits 2 and 3 show the extent to which US and European CRE prices have fluctuated across major property types, which has left many mortgaged properties leveraged beyond traditional CRE lenders' debt service coverage ratio (DSCR) and loan-to-value (LTV) standards.

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EXHIBIT 2

Office and multifamily properties have registered the largest US CRE value declines

US CRE transaction volume and price changes, by property type*

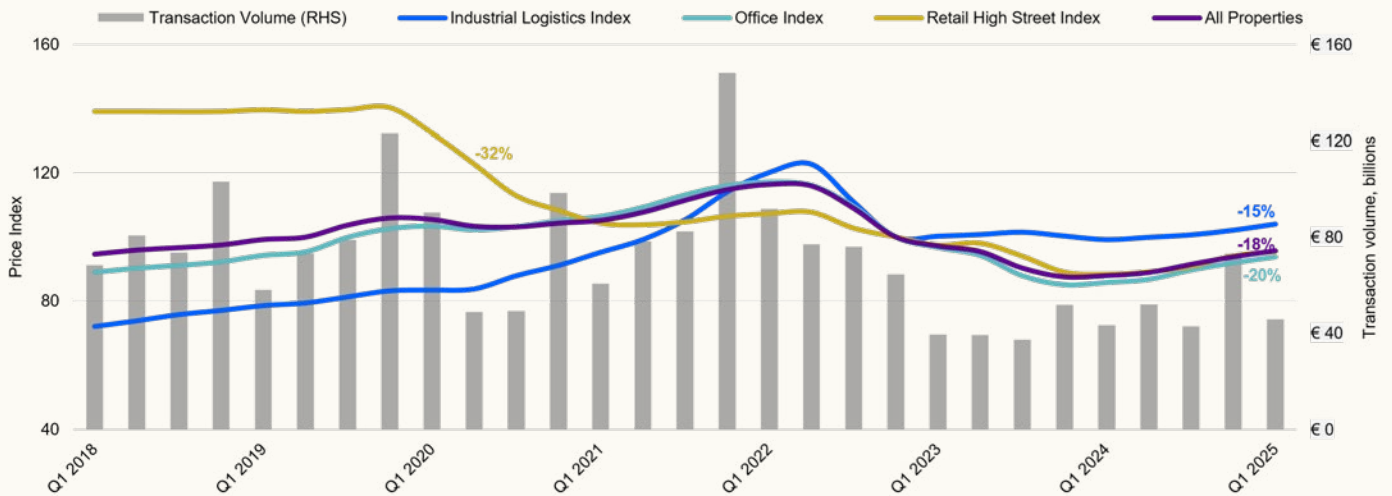


* Percent change is from peak value to most recent index level. The positive industrial figure is from mid-2022 as industrial values have continued to increase.
Source: Real Capital Analytics, Moody's Ratings

EXHIBIT 3

Retail and office properties have registered the largest European CRE value declines

European CRE transaction volume and price changes, by property type*



* Percent change is from the peak value to the most recent index level.
Source: Real Capital Analytics, Moody's Ratings

This heightened leverage was apparent in our 2024 regional bank loan survey where we marked to market the values of the 100 largest CRE loans at 41 regional banks. We estimated the property value decreases pushed property LTVs to an average of 74%, considerably higher than the 55% LTV provided in banks' submissions based on their original or recent appraisals. Since rates increased in 2022, many CRE lenders have extended maturing loans that borrowers could not refinance, while some banks have sold CRE loan portfolios at discounts based upon their old, lower coupons. Among conduit/fusion CMBS we rate, this refinancing challenge is demonstrated by a lower repayment rate, with only 64% of loans successfully paying off at maturity in Q1 2025, down from more than 80% before 2022.

So far, private credit participation has been only a small portion of the greater CRE mortgage market, which totals \$6.1 trillion in the US and \$2.8 trillion in Europe. Exhibit 4 shows the mortgage balances held by various CRE lender types, along with our estimates of how much of today's current loan balances could shift to private credit funds if those loans deleverage in order to restore traditional lenders' portfolios to their original LTV and DSCR levels to conform with lenders' risk appetites and regulatory constraints. Any actual deleveraging would vary based upon lenders' individual LTV or DSCR targets, but if leverage standards require loans to shrink by 6% to 12%, then private credit funds' CRE investments could reach \$2.7 trillion. We expect this shift will take several years and that lender's actual nominal lending volume changes will be subject to market growth and private credit funds' risk appetite.

EXHIBIT 4

An estimated \$1 trillion of today's CRE debt could shift to private credit funds

US and European CRE mortgage holdings by lender type, with potential 12% shift to private credit lenders

Commercial mortgages	Non private CRE lenders Initial holdings: \$7,778 billion				Private credit lending sources Initial holdings: \$1,833 billion			
	Banks	Covered bonds	GSEs	CMBS	Insurance	US CRE CLOs	Mortgage REITs	Private credit funds
US	\$3,174B		\$1,064B	\$548B	\$790B	\$138B	\$220B	\$450B
Europe	\$2,624B	\$334		\$34B	\$98B			\$137B
Shift to private credit	\$711B	+ \$20B	+ \$128B	+ \$70B	\$95B	+ \$17B	+ \$26B	
Percentage shift	12%	6%	12%	12%	11%	12%	12%	
Private credit fund increase	-\$929B				-\$138B			= \$1,066B
Potential total CRE credit \$2,762B or ~\$2.7T								

* Estimated shift to private credit funds selected after considering a variety of rate, value and bank regulation/risk appetite changes. The actual shift to private credit could range from 0% to 20% of outstanding mortgages depending upon how properties have performed, various institutions' current targeted LTV and DSCR standards, changes in regulation, bank funding costs, etc.

** Within securitized products, we assume private credit funds hold non-investment-grade bonds that are roughly 9% of CMBS and 19% of CRE CLOs.

*** To convert European currency to US dollars, we used a 1.14 exchange rate as of 29 May 2025.

**** US and European "other and pension holdings" totaling \$22 billion are not shown in the illustration, but contribute \$2.6 billion to private credit deleveraging.

Source: Moody's Ratings, Federal Reserve, CREFC and ECB reports

To grow their CRE lending business, private credit funds have increasingly partnered with banks and insurance companies to originate relatively high-risk loans in search of higher yields. While a significant portion of private credit CRE lending is in the form of mortgages, it is also often provided via subordinate secured financing that is not recorded as a mortgage. Private credit funds also contractually assume risk via SRT/CRT transactions. These transactions are not recorded as mortgages and can be difficult to monitor. Within CMBS alone, we calculate that subordinate, nonmortgage financing provided \$28 billion (7.8%) of additional leverage as of mid-2024. Many banks and other lenders do not permit borrowers to use mezzanine financing. Nonetheless, unsecured debt involving these lenders is likely currently adding 2%-5% of additional leverage. But to further deleverage their existing CRE loan portfolios, insurance companies and banks will likely loosen restrictions they currently have on secondary debt and SRT/CRT transactions.

For several years now, private credit funds have been targeting not just the transitional, riskier loans, but also longer-term, first mortgages for stabilized properties, which are typically the purview of banks and insurance companies.

To facilitate these lower-yielding loans, private credit funds have raised funding from pension funds and even the insurers and banks they may compete with to originate such loans. Traditional lenders have borrower relationships and other advantages in originating loans for these stabilized properties. But traditional lenders also have incentive to partner with private credit firms because it is an additional avenue to grow their CRE lending business.

Private credit fund CRE holdings are likely larger than the estimates in Exhibit 4, as they can hold a range of investment- and noninvestment-grade CRE bonds – from CMBS and CRE CLOs – that can also be leveraged beyond the funds reported by PERE as being available.

The deleveraging of traditional lenders would likely shift CRE debt holdings away from bank, insurance and securitized lenders and to private credit funds. As that happens, the CRE loan market may continue to grow, allowing traditional lenders to diversify further into lower-leverage CRE mortgages. Insurers will also likely add CRE-related private credit products based upon optimizing return for capital invested.

Private credit plays a role in all phases of CRE lending, transferring and raising risks

As noted above, the private credit and CRE markets intersect in numerous ways. Private credit firms both originate loans directly and purchase them off bank balance sheets, via whole loans, subordinate notes and in synthetic form. And while each intersection may heighten or create new risks, private








credit's involvement in CRE debt also has its benefits, for both borrowers and traditional CRE lenders.

Exhibit 5 shows key CRE parties and funding instruments we rate, along with the risks and benefits of private credit's involvement.

EXHIBIT 5

Private credit intersects with CRE in numerous ways*

Types of CRE lenders and transactions we rate

	CRE connection to private credit	Credit risks	Credit benefits/mitigants
 <p>Banks</p>	<p>Provide leverage via repurchase facilities</p> <p>Offload CRE loan risk to private credit via loan sales or risk-transfer transactions</p>	<p>Risk layering through exposures to borrowers elsewhere in the CRE and private credit ecosystem</p> <p>Existing exposure to CRE through direct on-balance-sheet lending</p>	<p>Advance rates with cross collateralization</p> <p>Partial recourse to borrower</p>
 <p>Life insurers</p>	<p>Originate loans both directly and through joint ventures with other private credit firms</p>	<p>Higher asset leverage, but first losses held by private credit</p>	<p>Creates low-leverage and stable-return CRE pools</p> <p>Good fit for longer-dated liabilities</p> <p>Broadens origination channels/diversifies portfolio</p>
 <p>CMBS</p>	<p>Private credit originates and contributes loans to pools</p> <p>Private credit buys non-investment grade and sometimes senior classes</p>	<p>Post-securitization risk is based upon subordination</p>	<p>Provides matched-term funding</p> <p>Diversifies a range of credit exposures</p> <p>Private credit holds risk-retention classes</p>
 <p>Covered bonds</p>	<p>Private credit retains junior positions on senior loans that collateralize covered bonds</p>	<p>Increased leverage for new loans provided by less-regulated entity</p>	<p>Junior debt provided by private credit reduces default risk of covered bond issuers</p>
 <p>CRE CLOs</p>	<p>Financing vehicle for private direct lenders</p>	<p>Relatively high-risk loans</p>	<p>Creates a leveraged yield</p> <p>Provides matched-term funding</p>
 <p>Equity REITs</p>	<p>Borrow from a range of lenders, including private credit</p> <p>Most likely to tap private credit for niche or under-construction properties</p>	<p>Loan terms favor lenders</p> <p>Conditions/Covenants restrict landlord flexibility</p>	<p>Improves access to capital for complex assets and under-construction projects</p> <p>Enhances market liquidity</p>
 <p>Nonbank direct lenders</p>	<p>First mortgages, subordinate lending and bond investments</p>	<p>Relatively high-risk loans</p>	<p>Enhances market liquidity</p>

* Insurance companies and CRE CLOs are private credit lenders themselves, so for those categories we describe how private credit funds interact with those sectors.

Source: Moody's Ratings

Bank lenders

Beyond traditional direct lending to CRE borrowers, banks are increasingly financing private credit firms' CRE activities through mechanisms such as warehouse lines (as with CRE CLOs, noted above) and repurchase agreements. Private credit firms also acquire nonperforming loans or seasoned mortgages that have become too leveraged to satisfy bank lending criteria, occasionally utilizing bank warehouse financing for these purchases as well. Private credit may also co-originate first mortgage or junior subordinate debt to facilitate refinancing of an overleveraged bank loan. In addition, these firms participate in SRT/CRT transactions with banks, allowing banks to offload the credit risk of specific loans in exchange for a portion of the loan coupon. This strategy boosts bank capital ratios by reducing risk-weighted assets, optimizing their balance sheets and regulatory standing.

Risks:

- Lack of transparency makes it difficult to evaluate private credit ecosystems and can lead to risk layering.
- Existing direct CRE lending, when combined with additional private credit activities, can lead to asset price bubbles and further expose banks' balance sheets to CRE.
- Limited partners' commitments to invest in CRE may not always materialize.
- Banks provide back-leverage to private credit funds on unlevered direct originations through either repo or warehouse lines. In the US, this lending is a portion of the roughly \$1.2 trillion in lending currently reported for all loans to nonbank financial institutions. In the UK, the volume is lower but rising fast with estimates that back-leverage provided by banks to debt funds accounts for about 30% of recent loan origination volumes.
- SRT capital relief is of low quality because SRT can be exposed to counterparty risk (i.e. private credit as SRT credit protection provider, or SRT not being fully collateralized) and high investor concentration (in Europe, the three largest SRT investors account for 50% of all SRT protection by volume).
- Increased competition from private credit could lead banks to weaken underwriting standards to gain/maintain CRE market share.

Benefits:

- Credit risk reduction provides capital that banks can use to diversify their CRE mortgage exposure or more broadly diversify their loan portfolios.
- Selling asset pools and the financing of asset pools allows for cross-collateralization while reducing overall net leverage.
- Banks have recourse to fund assets or seek commitments from limited partners, providing additional financial security.
- SRT/CRT effectively moves risk off bank balance sheets.

Life insurance companies

We consider life insurers an original participant in private credit, as they have had a presence in the origination of CRE assets for decades. However, new partnerships with alternative asset managers are broadening the scope of target assets. As borrowers have sought more leverage than insurance companies typically provide, insurers have set up joint ventures in which insurers hold a senior credit position while the private credit firm takes on the higher-risk/higher-yield position. In those arrangements, insurance companies maintain tight underwriting guidelines and are selective of the assets included in general accounts. In recent years, despite valuation challenges, insurers' loans have average LTVs of around 50% in the US, representing relatively low leverage for all property types. Similarly, in Europe, insurers directly originate high-quality loans with LTVs lower than 60%. However, they increasingly are making lower-quality/higher-yielding investments through private credit partnerships.

US insurers also participate with private credit funds through rated note feeders. Rated note feeders are a capital-efficient way to invest in funds, especially given that most of these instruments are expected to qualify for bond capital treatment under new National Association of Insurance Commissioners principles-based definitions. Such structures are not prevalent in Europe where fund investments receive capital charges aligned with the underlying investment, which typically are not onerous, on a look-through basis.

Risks:

- The lack of transparency and disclosures around these investments can make it hard to make timely valuations or to predict their performance in a downside scenario.
- These investments tend to be illiquid, which could make them riskier in a tail scenario if life insurers were forced to liquidate assets in a short period.
- For companies with higher risk tolerances, with participation in more-junior tranches, asset leverage could be higher, increasing the probability of default.

Benefits:

- Increased access to a larger pool of assets, leveraging expertise from firms that can originate specialized assets.
- Life insurers participate in the underwriting and asset selection process, adhering to tight credit investment guidelines.
- Participation in the higher end of the capital structure leads to better recoveries on defaults.
- US feeder funds' low LTVs and over-collateralization protect insurers from potential shifts in valuation.

CMBS

Private credit firms generally buy and hold non-investment-grade CMBS bonds, often serving as the designated risk-retention party. Private credit firms also frequently buy investment-grade CMBS bonds, usually based upon their analysis of specific collateral. In addition, although not classified as private credit, there are private credit firms that originate CMBS loans and, when they do, usually retain the related junior CMBS bond classes.

Beyond holding subordinate CMBS bond classes, private credit is also a buyer of B-notes and unsecured mezzanine loans that are subordinate to CMBS loans. These B-notes and mezzanine loan purchases decrease the underlying leverage of the CMBS pool but increase overall property leverage.

Risks:

- Loan originators have credit and market exposure while the loans are warehoused pre-securitization. If an originating bank retains the risk-retention classes it is usually via a vertical slice of the transaction, creating a spectrum of credit risk.
- When private credit firms fulfill the risk-retention function, they hold the junior non-investment-grade bond classes and the associated first-loss risk of the collateral within the CMBS transaction.
- Private credit firms review each loan and price the risk based upon the medium-to-long-term credit risk of the junior noninvestment-grade classes.

Benefits:

- Issuer/private credit locks in funding that matches the term of the loans, with private credit keeping the resulting leveraged first-loss risk, usually from Ba- and lower-rated bonds.
- Creates a variety of bonds with different credit profiles, either as long-term fixed or short-term floating-rate classes.

Covered bonds

Private credit is complementary to and competes with covered bonds as a bank funding source. We expect that nominal CRE loan dollar amounts backing covered bonds will continue to grow over the next few years, and that the shift from covered bonds to private credit lenders will be lower than the overall expected potential shift to private credit funds. On the one hand, private credit provides junior loans that rank behind the senior loans that secure covered bonds. On the other hand, private credit encroachment on traditional bank lending means they increasingly compete with banks for whole loans.

Given covered bonds' dependence on their bank issuers' credit quality, the risks and benefits to banks are also risks and benefits to covered bonds (see above). However, there are other covered bond-specific risks and benefits of private credit involvement.

Risks:

- Competition from private credit squeezes margins and reduces the volume of loans available for cover pools.
- Private credit providing large volumes of junior loans creates a clash of incentives between senior and junior loan providers. This could lengthen loan workout procedures and reduce recoveries. For example, covenant-lite lending could weaken the ability of senior lenders to minimize losses if loans underperform.
- A sudden decline of private credit loan volume, for example because of changes to regulatory frameworks, could weaken CRE asset prices.

Benefits:

- Lower default risk for maturing loans that no longer meet banks' underwriting standard where private credit is willing to provide these loans.
- Lower refinancing risk on European CRE loans as private credit offers longer-term financing than traditional lenders.
- Private credit provides an alternative source of funding that may prove more reliable than traditional financing. Given the reliance of banks on short-term funding, they may be more capital-constrained during a CRE downturn than private credit, which is funded with long-term capital.

CRE CLOs

Many US nonbank (private credit) lenders issue CRE CLOs to fund the CRE mortgages they originate. A CRE CLO is a securitization backed by a pool of short-term floating-rate loans on properties whose cash flows and values will likely grow in the future (transitional properties). CRE CLO bonds match funding throughout the referenced loans' terms, while retention of the junior classes (typically 17% to 22% of the collateral balance) creates a higher-levered return for the lender on the loan pool. Unlike CMBS, which are static, CRE CLOs are actively managed by the loan originator, allowing them to monitor and service the loans and provide future takeout refinancing.

Banks provide warehouse financing for CRE CLO transaction sponsors.

Banks, insurers and other asset managers frequently buy senior CRE CLO bonds, which are mostly Aaa (sf) rated, but also include lower investment-grade classes.

Risks:

- Poor property performance can create pool losses. Thus to maintain financing, the manager (also typically the loan originator and servicer) must replace distressed loans and then work to maximize recoveries. In an industry downturn this replacement takeout may not happen, resulting in the loans being worked out within the CRE CLO.
- Collateral are typically floating-rate loans that are sensitive to interest rate changes, potentially increasing upfront costs, but interest rate caps increase funds available for ongoing debt service payments.

Benefits:

- Structural over-collateralization and interest coverage tests protect noteholders from potential shifts in valuation.
- Active management allows for adjustments to the loan portfolio to mitigate risks.
- Collateral are usually first mortgages with a claim on an underlying property.
- Relatively short duration of CRE CLO collateral limits exposure to long-term interest rate risk.
- Pool diversification and revolving nature reduces the risk associated with any single property or borrower.
- Provides natural matched-term leverage to the loan originator.

Equity REITs

Equity REITs access various debt capital sources, such as secured and unsecured loans, bonds, revolving credit facilities, and property level, nonrecourse mortgage debt. Equity REITs also invest in unconsolidated joint ventures that are majority-owned by investors and funded by property-level nonrecourse mortgage debt or other secured debt issuance. Private credit lenders participate in all of these channels. However, we expect the share of private credit funding is higher for assets and portfolios with unusual characteristics, that are under construction or in lease-up.

Risks:

- The customized loan terms typically favor the interests of private credit lenders.
- The conditions of the private credit loans sometimes restrict the landlord's operational flexibility if operating metrics deteriorate or cash flow declines.

Benefits:

- Provides capital access for complex and transitional assets that may not conform to bank underwriting or CMBS investment criteria.
- Enhances market liquidity because it finances buyers who are not able to access traditional CRE financing.

Nonbank direct lenders (private credit funds)

Asset managers, closed-end funds, mortgage REITs, pension funds and other nondepository institutions are among the private credit firms involved in CRE. These lenders grant mortgages directly to CRE borrowers, invest in various forms of CRE derivatives such as CMBS, offer insurance/synthetic credit protection to banks, and have created lending partnerships with insurance companies (which we also consider private credit) and banks. The liquidity private credit provides largely benefits CRE market players. However, several characteristics – such as their light regulation combined with their affinity for high-leverage loans – while not large risk avenues now, could become more of a concern in an economic downturn.

Risks:

- Lightly regulated with short track records, as many funds were not tested by the 2008 financial crisis.
- Frequently originate loans at higher leverage than traditional lenders, which comes with higher default and loss risks.
- Focus on CRE makes them highly vulnerable to industry downturns.
- Reliance on secured bank financing presents liquidity risk should bank credit tighten and lending portfolios come under pressure. The nonbank financial institutions' CRE loan exposure is a portion of the \$1.2 trillion reported by US banks, which currently does not likely create a systemic risk.
- Mortgage REITs must distribute 90% of earnings as dividends, limiting their ability to build capital.

Benefits:

- Facilitate projects that might not otherwise secure financing.
- Potential to provide long-term CRE financing given their own funding is long-term.
- Shifts risk from traditional lenders, diversifying financial exposure and potentially reducing systemic risk.
- Tend to have solid capitalization and reserves, as well as high-quality sponsors.
- Provide both first-lien and subordinate financing, creating a comprehensive capital structure that can handle various risk profiles.
- Use of securitization to fund direct lending spreads their risk across investors, boosting capacity to withstand shocks and maintain stability.