Empira Study "Real Estate Debt 2023"

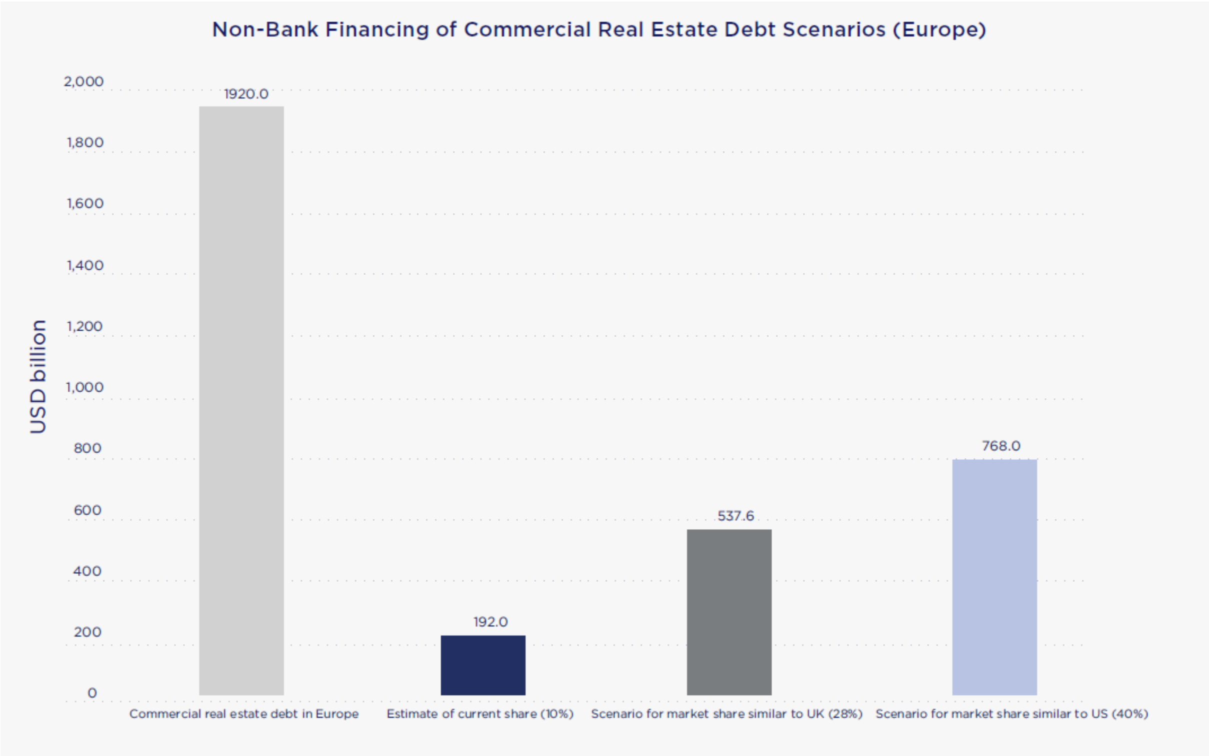
Strong Catch-up Potential for Alternative Debt in Europe

- **Interest rate hikes and bank regulations increase demand for financing instruments outside of conventional bank loans**
- **At a private debt share of 10 percent, continental Europe lags significantly behind the U.S. market at 40 percent**
- **Private debt calls for professional management in specialised funds**

Zug (Switzerland), 25 January 2023 – In its latest study, conducted in January 2023, the Empira Group, a leading investment manager for institutional real estate investments, undertook a thorough analysis of the debt financing market for real estate. The findings clearly demonstrate the presence of considerable potential for loan-based financing beyond conventional bank loans for institutional investors, particularly in continental Europe. In an environment of rising interest rates and limited bank financing, alternative sources of debt financing are taking on a greater role in the commercial real estate market. The market for non-bank financial institutions, including providers like funds, pension funds, insurances, and investment foundations from outside of the banking sector, will expand significantly worldwide.

"Generally speaking, it is safe to assume that non-bank real estate financing will grow and become more significant. For regulatory reasons, this growth will occur almost exclusively in the B2B segment, while lending to consumers in the area of residential financing will remain reserved for banks," comments Prof. Dr. Steffen Metzner, Head of Research at Empira and author of the study. "Since banks tie up their capital in that area, and commercial real estate financing arrangements are often individual and sophisticated in nature, shares of private debt will grow within the commercial real estate debt market."

While current estimates show that lenders from the financial sector beyond conventional banks are already providing 40 percent of debt for financing commercial real estate in the U.S., the share is considerably lower in continental Europe. "Even a scenario assuming 10.0 percent of the European commercial real estate debt market would correspond to a capital amount in the non-bank sector of around EUR 190 billion," explains Prof. Dr. Steffen Metzner. "Increases to the level of Great Britain, where 28 percent is attributable to private debt, or the U.S. would still result in even much larger sub-markets in the private debt sector."



Source: Barings Bank, PGIM RE, Bayes Business School London; own calculation and presentation

Private Debt Calls for Professional Management in Specialised Funds

"Germany's market for real estate financing is likely to see a liquidity bottleneck in the years to come. Therefore, the need is growing for forging new paths and developing innovative instruments for debt and equity financing. Whether and at what rate these become established in the market throughout Germany will be a decisive factor in how the real estate location performs, whether the housing situation in metropolitan areas eases, and to what extent external capital can trigger new growth stimuli," explains Lahcen Knapp, Chairman of the Empira Group Board of Directors.

While the financial demands of institutional investors had been mainly served through conventional bank loans in the past, there are doubts that this source of funding will still manage to provide adequate liquidity for commercial real estate projects going forward – in light of rising interest rates, higher risk provisioning, and reluctance to issue loans. A widening gap is revealed when comparing the growing demand for financing in the real estate and construction industry, on the one hand, and the banking sector's limited financing resources, on the other hand. The relevant banks are seeing virtually no increase in total assets; those increases remain significantly lower than the growth rates of asset prices on the real estate market. This is driving a growing need for alternative sources of financing.

The trend towards loans from alternative, entrepreneurially oriented financing partners will therefore continue to strengthen in years to come.

“The high financing volumes in this country and the individual customizing of arrangements require professional management and controlling. Therefore, high-performance real estate private debt funds will support this expected market growth for the most part. From the institutional investor’s perspective, they also offer the possibility of scaling investments in the real estate debt market,” concludes Knapp.

The complete study can be accessed here.

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The Empira Group at a glance

The Empira Group offers institutional investors a vertically integrated platform for real estate investments in Europe and the United States. With investments under management totaling approximately EUR 7.1 billion, Empira is a leader in the German-speaking region in developing novel, profitable investment approaches using both equity and debt financing. The company drives innovation as a first mover in debt products. The Empira Group’s real estate and capital market experts offer one-stop shopping for services covering the entire residential and office property value chain. The company is headquartered in Zug, Switzerland, and has locations in Luxembourg, Germany, the U.S., Great Britain, and Austria.

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