Principal Asset Management℠

Principal Real Estate

U.S. CRE Cycle Monitor: 2Q26 – Resilient Recovery

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Executive Summary

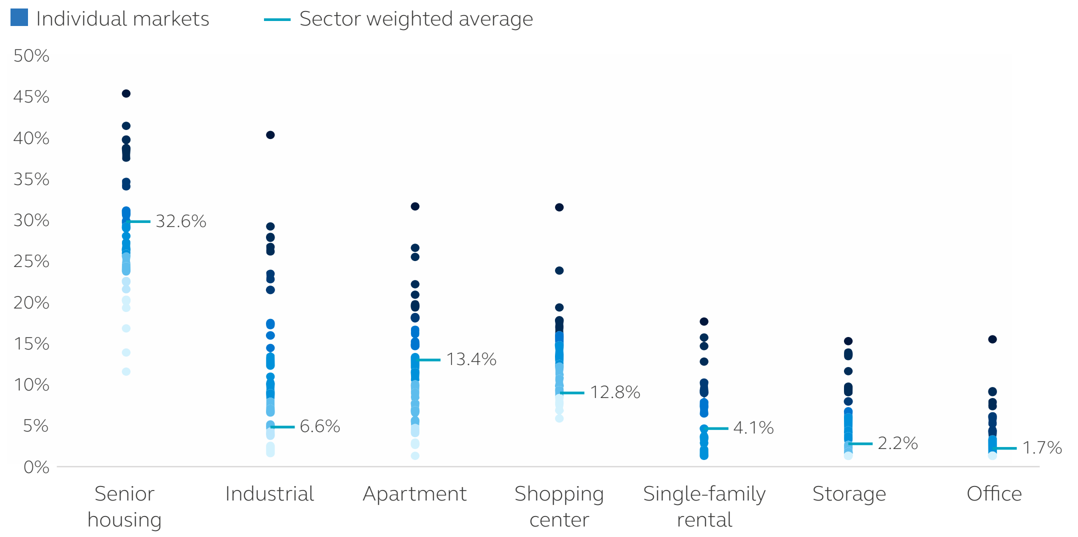
In our mid-year 2026 Global CRE Outlook, we argued that the CRE cycle remains intact despite geopolitical volatility and shifting macro crosscurrents. Our five-signal marketer barometer, that we introduced in May 2026, suggests that the conditions for a sustained momentum remain in place in 2Q26. No single signal is sufficient on its own, but their alignment and sequencing make a compelling case for the direction of commercial real estate.

1. U.S. listed REITs, our leading indicator, rose +10.7% and remain in expansion.
2. The NCREIF NPI and ODCE index have the highest returns since 2Q22.
3. Banks loosening lending standards across all loan types for the first time since early 2022.
4. Transaction volumes rose +14% YoY in 2Q26.
5. Distress, a lagging indicator, continues to rise, but delinquency rates are stabilizing.
6. Sentiment indicators continue to show more deliberation, but not loss of conviction.

3Q26 will undeniable present new challenges as interest rates have risen in July (see [What a 5% 10-year Treasury means for commercial real estate] for further details), but we believe the significant dispersion in returns across property types, markets and even fund vehicles is the key to navigating this backdrop. That said, there continues to be significant dispersion in returns across property types, markets and even fund vehicles. This unevenness isn't a flaw in the cycle - it is the cycle and, in our view, presents a significant alpha opportunity.

EXHIBIT 1: Trough to current recovery in U.S. prices across property types

Top 50 markets



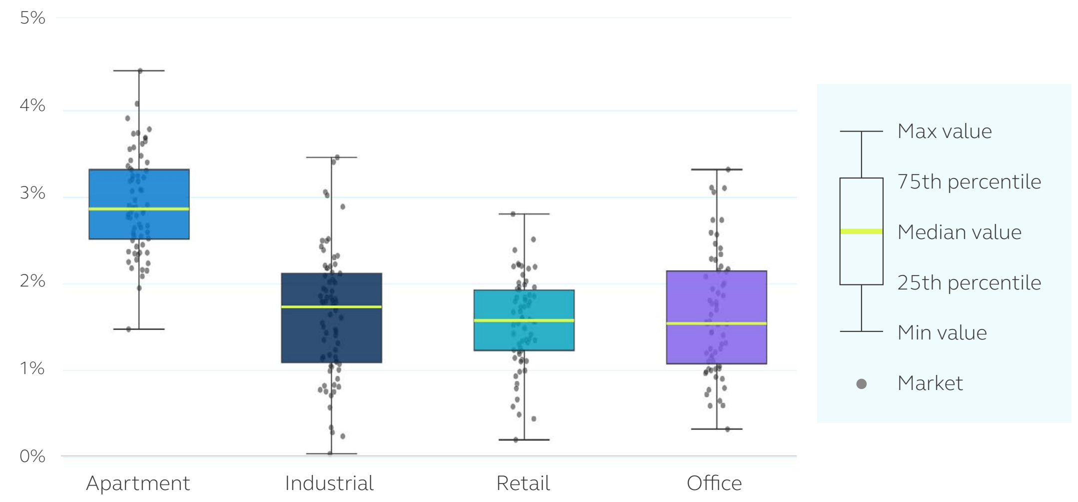
Source: Green Street, Principal Real Estate, as of Q2 2026.

Consensus calls this a K-shaped recovery, but we believe that misses an important nuance. Dispersion has always existed and always will - the market simply hasn't focused on it in a long time. When even relative underperformers produce positive returns in a broad-based expansion, and relative outperformers produce negative returns in a broad-based downturn, the market pays little attention. And the last recovery was V-shaped post-GFC, which felt much different than today. So, it's been more than 30-years, following the S&L crisis, since the market saw dispersion like today. And it feels like a shock to the system where avoiding the losers that blow up track records may just as important than picking the winners. Alpha is earned and not given.

We believe NOI growth will be the key driver of total returns over the next cycle, especially given higher interest rates: it powers both income and capital returns in a market where cap rate compression is unlikely to do much of the work. Investors may have forgotten how much income returns matter. They contributed just 43% of total returns over the prior cycle, as cap rate compression did the heavy lifting against historically low interest rates. Over a full cycle, income typically drives ~85% of total returns.

Maximizing NOI growth still requires the right sector calls. Seniors housing, data centers, and open-air shopping centers lead 5-year growth expectations; office and storage lag. The real alpha, however, comes from picking the right property types in the right markets. Indeed, 10-year annualized rent growth projections from CBRE show significant dispersion within every sector.

EXHIBIT 2: 2026-2035 Rent growth CAGR by property type



Source: CBRE, Principal Real Estate, as of January 2026.

U.S. listed REITs, which are leading indicators, are having a banner year

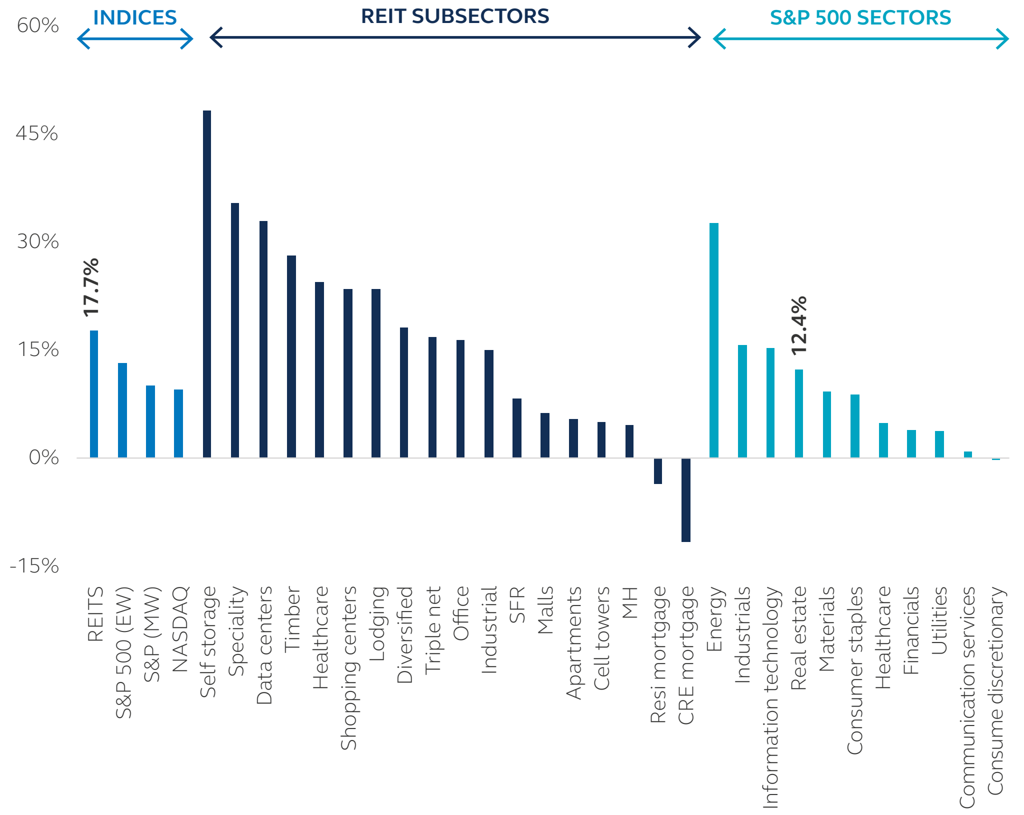
The sector (as measured by the FTSE NAREIT All-Equity Total Return index) generated total returns of +10.7% in 2Q26 with returns of +9% in April, +0.1% in May and +1.5% in June. Real estate is the 4th best of the eleven S&P 500 sectors signaling the public markets are once again prioritizing predictable earnings and income driven total returns.

Importantly, valuations remained +3% above prior cycle highs at the end of quarter. This is important because new market highs are often mistaken for late-cycle signals, but history suggests they more often mark the end of the beginning, not the beginning of the end. Indeed, the U.S. listed REIT market has only recently transitioned from recovery into expansion, which history suggests last 12-13 years and are long, durable periods supported not only by price appreciation but also by underappreciated income growth. In other words, the cycle remains early by historical standards.

And it's worth noting that the strength has continued into 3Q26 with total returns now standing at more than +17.5% YTD as of the end of July 2026, valuations are 5.5% above their prior cycle highs and real estate remains the 4th best sector of the S&P 500. This has occurred despite interest rates rising over the course of the month.

EXHIBIT 3: U.S. listed REITs are sending signals of resiliency for CRE

Year-to-date total returns as of 31 July 2026



Source: Bloomberg, Principal Real Estate, 31 July 2026. U.S. listed REITs represented by FTSE NAREIT All Equity Index. Indices are unmanaged and do not take into account fees, expenses, and transaction costs and it is not possible to invest in an index.

Private CRE valuations continue through the recovery.

The NCREIF Property Index, which measured unlevered total returns, rose +1.3% in 2Q26 – the 8th consecutive quarter of increases and the NCREIF ODCE index, which tracks 25 open ended funds that own U.S. core commercial real estate, also rose +1.5% on a gross basis. The increase in the NPI and the ODCE index were both the greatest since 2Q22.

Green Street showed prices increased by +1.4% and total returns rose +2.8% while the Real Capital Analytics CPPI shows prices rose +0.7%. However, the Costar index showed prices declined -1.5% during the quarter, but it's historically a more volatile index.

Bottom line, while the indices have different methodologies, they collectively point towards valuations rising in 2Q26 and a sustained recovery from the trough.

EXHIBIT 4: Private CRE indices signal sustained valuation recovery

	Total Return		Price	
Index	**2Q26**	**vs Trough**	**2Q26**	**vs Trough**
NCREIF				
ODCE Index (Gross)	1.5%	8.1%	0.5%	0.6%
Unlevered property index	1.3%	9.5%	0.1%	0.4%
Green street	2.8%	25.4%	0.4%	9.5%
RCA	–	–	0.7%	1.9%
Costar	–	–	-1.5%	5.5%

Source: NCREIF, RCA, Green Street, Costar. As of 2Q26.

Debt markets are open & liquid

First, the Mortgage Bankers Association's 2Q26 Commercial / Multifamily Mortgage Bankers Origination Index showed that originations were 16% higher in the second quarter of 2026 compared to a year earlier, and 12% percent from the first quarter of 2026. We focus on YTD metrics that show 2026 YTD volumes are 31% higher compared to the same period last year. Among lender types, Life Co's are the only lender that is down YTD compared to the same period last year and, among property types, every property type is higher YTD.

Second, the Federal Reserve's Senior Loan Officer Opinion Survey (SLOOS) for July 2026 showed that banks generally reported easier standards and roughly unchanged demand for commercial real estate (CRE) loans:

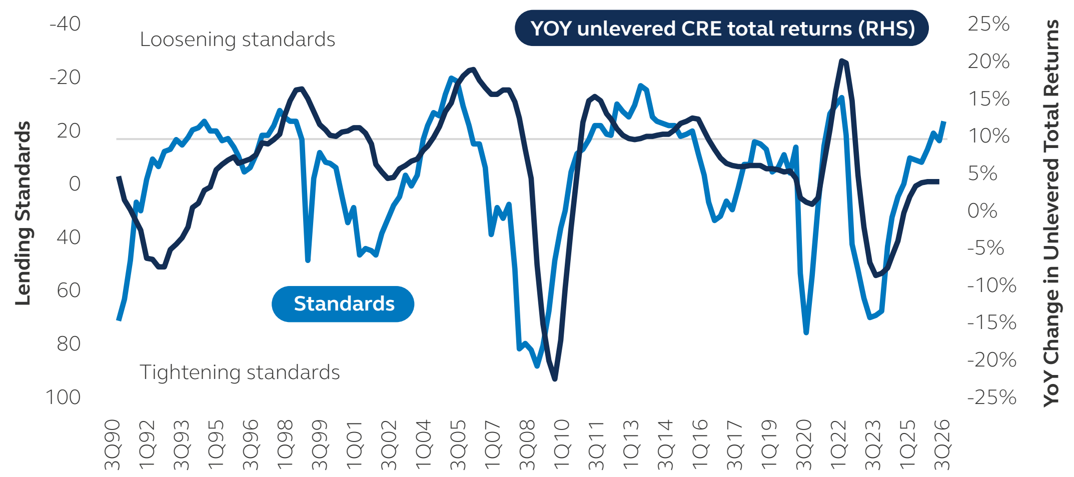
- **Construction:** 3.7% of net respondents reported loosening standards; 11.1% reported weaker demand.
- **Core commercial:** 11.3% of net respondents reported loosening standards; 1.9% reported greater demand.
- **Multifamily:** 5.7% of net respondents reported loosening standards; 3.8% reported weaker demand.

This is the first time since early 2022 that net easing in lending standards has occurred across all CRE loan types. The easing was driven by a larger proportion of small and regional banks re-entering CRE lending, which should be a continued tailwind over the near to medium term.

The survey also included special questions on where current lending standards sit relative to the midpoint of their historical range since 2005. For CRE, a significant net share of banks reported standards for construction loans at the tighter end of that range, while moderate net shares reported similarly tight standards for core commercial and multifamily loans. That said, these tighter-end readings are less pronounced than in the July 2025 survey. C&I loans remain the only category where standards are generally easier than their historical midpoint.

Taken together, we believe the recent quarterly SLOOS supports continued increases in unlevered total returns for private real estate. That said, headline quarterly returns have recently stalled near 5%, which we believe reflects growing dispersion across property types and markets - with robust top-quartile returns being offset by weaker performance at the bottom.

EXHIBIT 5: Senior Loan Office Opinion Survey

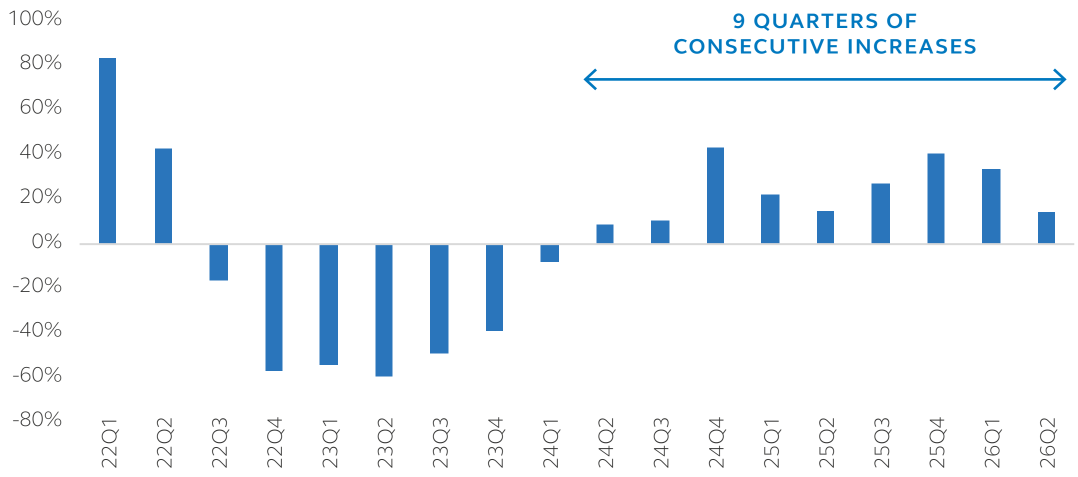


Source: Federal Reserve, Principal Real Estate. As of 2Q26.

Transaction volumes rose broadly.

Real Capital Analytics' latest data show U.S. commercial real estate transaction volumes rose +14% YoY to $136.6bn in 2Q26 - the ninth straight quarter of YoY growth - helping to allay slowdown concerns. Momentum built through the quarter, with June up +15% and May revised sharply higher to +30% (from +15%), while April's decline narrowed to -3% from an original -33%. Sector performance was broadly positive: data centers surged (+1,806% to $7.7bn), followed by senior housing (+51%), industrial (+27%), hotel (+27%), retail (+13%), and apartment (+1%); office was the sole decliner (-9%), and volumes were still +9% ex-data centers. Portfolio and entity-level deals continued to drive liquidity, but individual asset sales returned to positive territory (+4% YoY) after declining in April and May - a sign that, despite increased selectivity amid meaningful return dispersion, investor conviction remains intact. On balance, 1H26 volumes are +23% ahead of 1H25, though tougher comps in 2H26 could make quarterly growth rates more volatile even if underlying activity stays constructive.

EXHIBIT 6: YoY change in U.S. transaction volumes



Source: Real Capital Analytics, Principal Real Estate, as of June 30, 2026.

Distress continues to rise

Real Capital Analytics recently released its 2Q26 Distress Update, showing cumulative distress*[1] of approximately $140.5 billion. This reversal from the first quarter's net decrease in distress was largely due to a decrease in workouts, rather than a significant increase in the quarterly addition to distress. This is roughly in line with levels last seen in 2Q12 in absolute terms, although much lower as a % of total transaction volumes (+3.3% today vs +11% in 3Q12 and a peak of nearly 20% post the GFC).

We've long argued that distress is a lagging indicator, representing the final stage of the adjustment process: acceptance. Borrowers are reluctant to "return the keys to the lender" until the recognize the past isn't coming and they must confront the new realty of the future. As a result, delinquency rates have historically peaked 12–24 months after private CRE valuations trough.

Indeed, CMBS private label (conduit and SASB) +30 day delinquency rates is showing signs of peaking – it stood at 6.9% in June compared to 7.2% in March, 7.0% in April and 7.2%. This inflection came seven quarters after private unlevered capital returns troughed and nine quarters after unlevered total returns troughed.

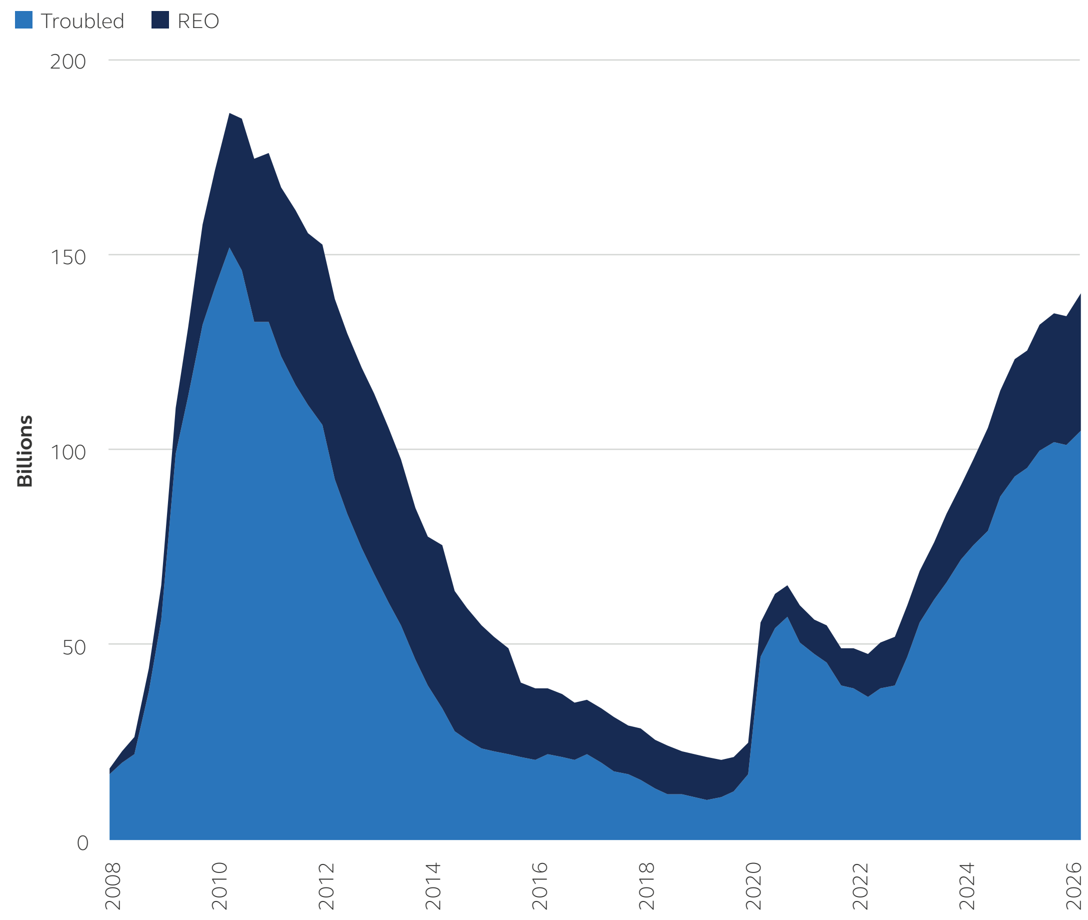
This coincides with the Mortgage Bankers Association's Commercial Real Estate Finance (CREF) Loan Performance Survey for 2Q26, which shows delinquency rates declined versus the prior quarter, although remain elevated compared to the year prior. Overall, the outlook for commercial real estate remains positive during the second half of 2026.

This sequencing continues to reinforce our view that this cycle is playing out in largely textbook fashion, with private CRE now entering the recovery phase of the cycle.

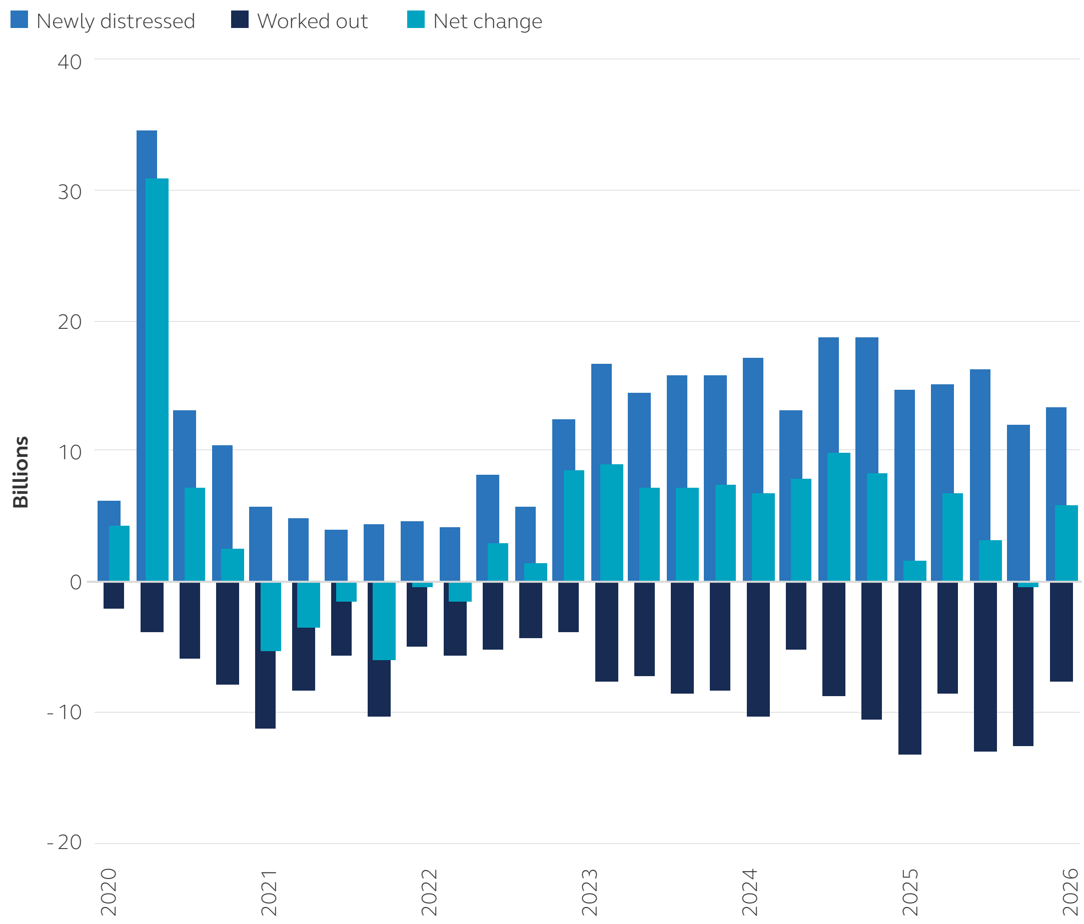
EXHIBIT 7: Distress stands at +$131.6bn, similar levels to 3Q12

It declined in 1Q26 for the first time in 15 quarters

Historical cumulative distress



Additions and reductions to distress



Source: RCA, Principal Real Estate. As of June 30, 2026.

What are sentiment surveys telling us?

We like to point to the latest Real Estate Roundtable and CREFC sentiment surveys that paints a picture of a market that has become more deliberate in 1Q26, but not one that is losing conviction.

The Roundtable, based on responses from senior industry executives, indicates that 62% believe the market is better than a year ago and 64% expect it to be better one year from now. Bottom line, this is a market caught in stalemate, where capital is abundant, debt is open, and fundamentals are holding, yet individual property transactions remain stuck behind a wide bid-ask spread. Sellers are refinancing rather than listing, geopolitical shocks have delayed an otherwise visible recovery, and a K-shaped dynamic is widening the gap between well-capitalized players and those running short on equity. The Real Estate Roundtable describes the mood as "patient, not pessimistic: a 'decaffeinated' recovery that participants believe will accelerate once pricing clarity returns."

The CREFC Sentiment Index, published by the trade association for the commercial real estate finance industry, showed stabilization in the index. It rose 0.9% QoQ to 101 from 1001.1 in 1Q26, holding near the 4Q17 baseline of 100 after the prior quarter's 20% decline. Five of nine core questions improved - led by the economic outlook – while four softened, led by borrower and investor demand. However, context matters as 61% of respondents said they expected improving transaction activity in 1Q26 and 71% said they expected greater financing demand. By comparison, 89% expect similar (47%) or higher (42%) investor demand and 87% expect similar (42%) or higher (45%) borrower demand. Bottom line, the stabilization in 2Q26 suggests a cautious optimism in the market, with demand for financing still net positive despite recent geopolitical shocks. Liquidity remains steady, offering a crucial buffer against ongoing interest rate uncertainties.

*[1] Distress indicates direct knowledge of property-level distress. Known through announcements of bankruptcy, default and court administration as well as significant publicly reported issues — such as significant tenant distress or liquidation — that would exemplify property-level distress. This also includes CMBS loans transferred to a special servicer.

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