Principal Asset Management℠

**PRINCIPAL REAL ESTATE**

# Commercial real estate lending standards stable amid volatility

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The Federal Reserve recently published the **Senior Loan Officer Opinion Survey on Bank Lending Practices** for 1Q 2025. The survey captures responses collected between March 31st to April 11th, a period of pronounced market volatility given the announcement of Tariffs. Commercial real estate (CRE) lending standards were largely unchanged even as banks tightened standards for corporate and consumer loans. Large banks loosened standards while small banks tightened. A greater percentage of large banks reported that they were originating loans at the same or at tighter spreads (90%), higher Loan-to-Values (LTVs) (85%), and lower Debt Service Coverage Ratio (DSCR) (85%) compared to last year.

## OUR TAKE

We aren't surprised that lending standards are unchanged and view it as a positive development:

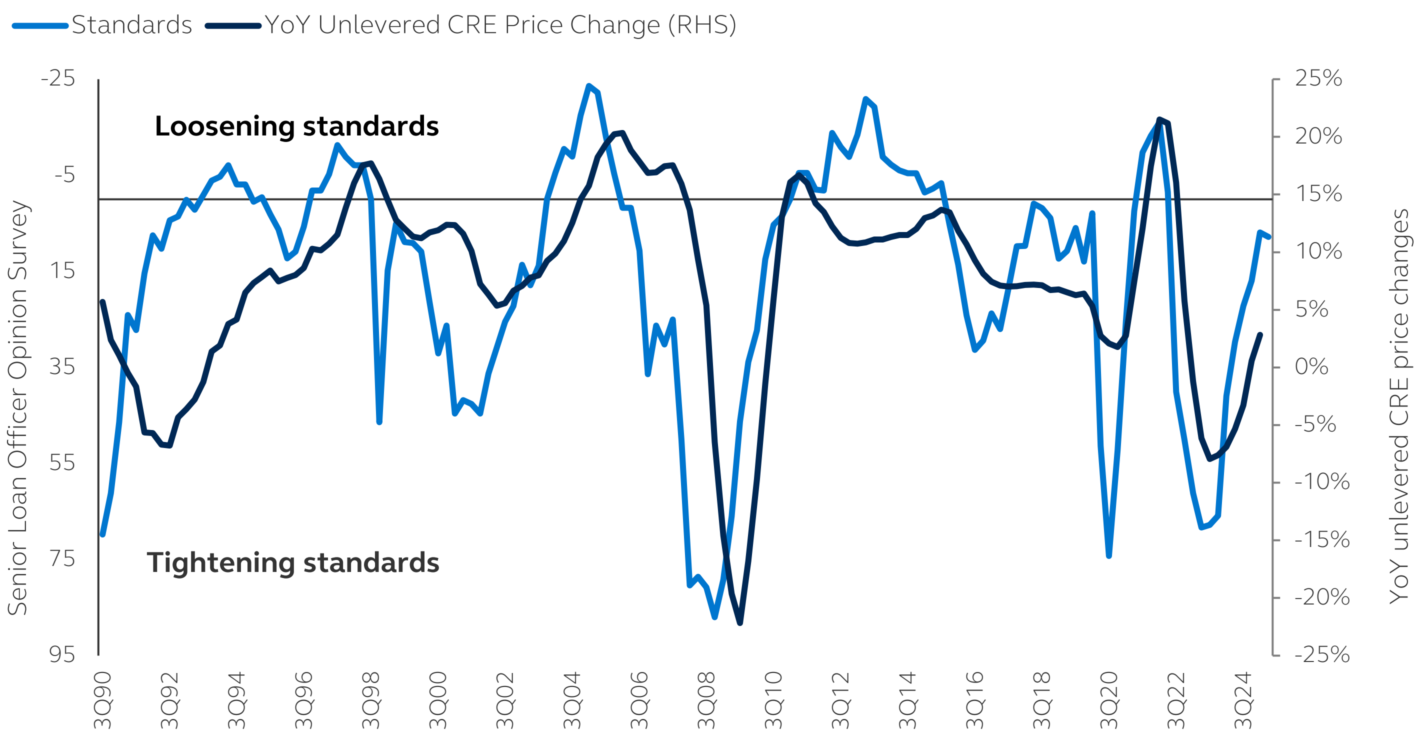
1. The CBRE Lending Momentum index surged in 1Q24 to 259, well exceeding the 5-year pre-pandemic average of 229. Some mean reversion was likely in the coming quarters.
2. The Commercial Real Estate Finance Council Sentiment Index declined 30.5% to 87.9 from 126.6 in 4Q24. It's now in-line with year-over-year changes in CRE valuations of ~5%.

We believe this reinforces our view that real estate is a relative winner in the current market environment. Indeed, listed REITs, which are a leading indicator in both downturns and recoveries, are outperforming the broader markets in 2025. In our opinion, CRE total returns can "muddle along" in 2025 as income returns mitigate potential headwinds to capital returns, but history shows that 7% to 8% annual returns over the longer term are reasonable.

## What happened?

A nearly unchanged percentage of banks (7.9% vs 6.9% previously) reported tighter CRE lending standards in 1Q25. This is the first time since 3Q23 that lending hasn't shown sequential improvement, but it's still substantially better than 29.7% reading a year ago and a peak of +68%. Meanwhile, loan demand continued to improve to -3.2% vs -4.8% previously—in other words, loan demand is on the cusp of turning positive. This represents the 8th consecutive quarter of sequential improvement.

### **EXHIBIT 1: Senior Loan Officer Opinion Survey**




Source: RCA, NCREIF, Principal Real Estate, as of 31 March 2025. (RHS – right hand side axis)

## The devil is in the details

**Lending standards** tightened for **construction & land development** (11.1% vs 9.5% previously), as well as **core commercial** (10.9% vs 8.1% previously), while **multifamily loans** were less tight (1.6% vs 3.2% previously). Among large banks, significant and moderate net shares reported having eased standards for **multifamily** and **construction & land development loans**, respectively, while leaving standards for core commercial unchanged. In contrast, significant or moderate net shares of other banks reported having tightened standards for all CRE loan categories. Lastly, modest net shares of foreign banks reported having tightened standards for CRE loans.

**Loan demand** for **construction & land development** was unchanged at -6.3%, while demand improved for **core commercial** (-1.6% vs -3.2% previously), and **multifamily loans** (-1.6% vs -4.8% previously). A significant or moderate net shares of **large banks reported stronger demand**, while moderate net shares of other banks reported weaker demand for all CRE loan categories over the first quarter. In addition, a significant net share of foreign banks reported stronger demand for CRE loans.

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