Market Insight

REAL ESTATE LENDING

EXPLORING THE IMPACT OF THE ECONOMIC ENVIRONMENT ON REAL ESTATE DEBT



In November 2026, ASK hosted a roundtable for real estate lenders to discuss the UK lending landscape.

Paul Dales, Chief UK Economist at Capital Economics, opened the roundtable with his assessment of the UK economy, highlighting near-term inflationary pressures and a more positive medium-term outlook for interest rates and growth.

The discussion explored how changing market conditions, competitive pressures and evolving risk appetites are shaping lending decisions and capital deployment.

ECONOMIC OUTLOOK

A temporary slowdown

Capital Economics expects inflation to rise in the near term, weighing on household spending and slowing UK GDP growth. However, a significant recession is not anticipated, with AI-related business investment providing some resilience in an increasingly two-speed economy.

The UK could outperform the eurozone over the next decade

Interest rates and fiscal pressures

Capital Economics expects Bank Rate to peak at around 4.25%, against market expectations of 5%, before potentially falling to 3.5% in 2028. Gilt yields are also forecast to decline, although fiscal pressures could lead to further tax increases, particularly affecting property and higher-income individuals.

Longer-term growth prospects

Beyond the immediate slowdown, the UK's services-led economy, flexible labour market and lighter regulation mean that potential productivity gains from AI could support stronger growth than the eurozone over the next five to ten years.

THE EVOLVING LENDING LANDSCAPE

Plenty of debt, but where are the transactions?

With activity largely concentrated on refinancing and distressed situations, abundant debt capital is competing for relatively few new transactions. This is putting pressure on margins and leverage, which raises concerns over whether lender economics are commensurate with the levels of risk being taken.

A short-term problem or a longer-term correction?

Views diverged sharply on property values, particularly in the living sectors. Some considered current development economics unsustainable, while others anticipated a recovery in capital values, with schemes delivered into a supply-constrained market in 2028–29 potentially performing well. The immediate challenge is underwriting responsibly today without relying on that recovery. Even those anticipating a recovery stressed the importance of conservative underwriting, assessing transactions against current rents and allowing for extended repayment periods.

Income versus valuation

While some lenders remain constrained by LTV requirements and credit committees, others argued that interest cover and sustainable cash flow provide a more meaningful measure of debt affordability particularly where limited transaction evidence makes valuations harder to establish. The cost of interest-rate hedging was also highlighted as a constraint, affecting borrowers' financing decisions, interest cover and the prices leveraged buyers can afford to pay.

Has delaying the recognition of losses prevented the market from finding its clearing price?

Has the market been waiting for a correction that never came?

Some questioned whether lenders had prolonged the downturn by extending loans rather than crystallising losses. Earlier asset sales might have established realistic prices and enabled fresh investment. Others argued that forced sales would achieve little where development land has negligible or negative residual value.

Will today's development slowdown create tomorrow's shortage of prime assets?

UK ECONOMIC OUTLOOK — SELECTED FORECASTS

4.3%
CPI inflation
Forecast peak, early 2027

1.0%
GDP growth
2027 forecast

3.5%
Bank Rate
Potential level in 2028

4.5%
10-year gilt yield
End-2027 forecast

2.0%
UK GDP growth
Annual average in the 2030s

1.0%
Eurozone growth
Estimated longer-term rate

Source: Capital Economics forecasts presented by Paul Dales

REFINANCING AND THE CHANGING DEBT MARKET

The missing equity

Despite plentiful debt, equity investors remain reluctant to commit capital against uncertain valuations. Some questioned whether increasingly stretched debt structures were bridging genuine funding gaps or merely transferring equity risk to lenders. Without fresh equity and greater transaction activity, refinancing remains challenging and uncertainty over valuations persists. However, some argued that slow restructuring reflects the complexity of negotiations and uncertainty over underlying values, rather than simply an unwillingness to recognise losses.

Lending volumes and development finance

According to Bayes Business School, new UK commercial real estate lending rose 29% year-on-year to £28.7 billion in H1 2026, driven largely by refinancing. Debt funds became the leading source of development finance, allocating 32% of their lending to residential and commercial projects. However, participants differed on the scale of potentially distressed development debt with some anticipating significant losses and others arguing that longer-term housing shortages could support underlying values.

Source: Bayes Business School, UK Commercial Real Estate Lending Report, H1 2026

WHERE NEXT FOR REAL ESTATE DEBT?

An increasingly divided market

Participants anticipated greater differentiation between best-in-class assets, opportunities at attractive entry prices and an increasingly difficult middle market. Prime offices and high-quality residential schemes may benefit from constrained future supply, while mid-market PBSA, build-to-rent and undifferentiated offices face greater uncertainty over demand and values. While ground-up development was considered challenging, selected office acquisitions and refurbishment strategies were seen as viable where entry pricing, rental demand and business plans were sufficiently robust.

New areas of opportunity

Interest extended to data centres backed by hyperscale demand, healthcare and care-related operating assets. These sectors offer potential structural growth, but require specialist knowledge and careful assessment of operating fundamentals.

Why invest in the UK?

The UK's international appeal prompted contrasting views. Brexit, political instability, taxation and regulation were seen as damaging investor confidence. Others highlighted the UK's established institutions and enduring attraction to global capital, although even the strength and predictability of its legal and regulatory framework was contested. Investment in energy infrastructure was also identified as an opportunity to strengthen the UK's self-sufficiency and competitiveness.

Looking ahead

The discussion highlighted a market in which debt remains plentiful, but a shortage of viable transactions, refinancing pressures and uncertainty over asset values continue to constrain deployment. While views differed on the timing and extent of any recovery, the discussion reinforced the importance of disciplined underwriting, sustainable income, strong sponsors and assets capable of performing through the cycle.

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