Pills

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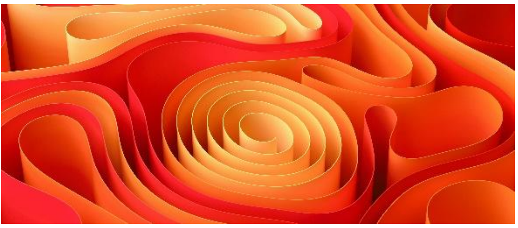

TOPICS:

Banking System

SOURCE

Financial Stability Board

FSB Examines Vulnerabilities in Non-bank Commercial Real Estate (CRE) Investors

- This FSB's report examines **the growing risks posed by non-bank institutions involved in Commercial Real Estate (CRE) markets.** These institutions - primarily Real Estate Investment Trusts (REITs), property funds, and non-bank mortgage lenders - have expanded in significance, particularly as banks reduce their risk appetite.
- **The CRE market has faced substantial pressure in recent years**, especially in office and retail segments, due to post-pandemic structural changes and rising interest rates. While banks remain the dominant lenders, **non-bank entities - especially in regions like the EU, UK, US, and Asia-Pacific - play a growing role**.
- The FSB identifies **four core vulnerabilities** among non-bank CRE investors: 1) **Liquidity mismatches** – Open-ended property funds often offer frequent redemptions despite holding illiquid underlying assets. This exposes them to run risk during market stress; 2) **High financial leverage** – REITs and property funds exhibit significant leverage, sometimes exceeding three times their equity. This increases the risk of breaches in loan covenants during property value declines, potentially triggering forced asset sales and broader market disruptions; 3) **Valuation uncertainty** – The illiquid nature of CRE assets and limited transaction data create opacity around valuations. Delayed recognition of losses - exacerbated by "extend and pretend" lending practices - could result in abrupt value corrections under stress; 4) **Interconnectedness with banks** – Non-bank CRE investors rely on banks for financing and often hold common exposures. Shocks in the CRE market may transmit to the banking system, underlining the need for integrated monitoring frameworks.
- The FSB calls for **enhanced data collection, harmonised definitions, and implementation of macroprudential tools to mitigate systemic risk** from the non-bank CRE sector.