

SPOTLIGHT ON: EUROPEAN CORE PROPERTY

EUROPEAN CORE PROPERTY - A GROWTH DRIVEN RECOVERY

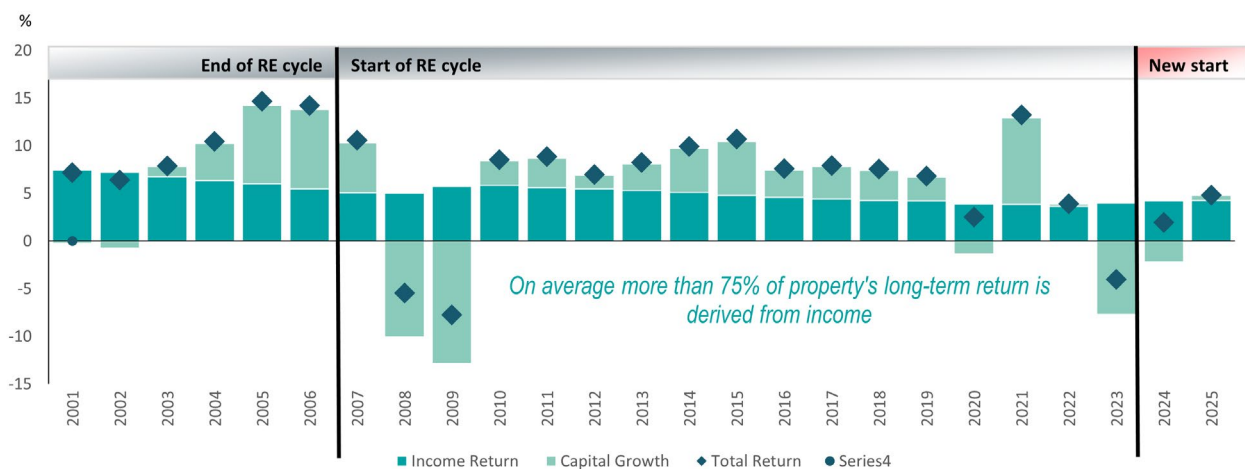
By **Justin Curlow**, Global Head of Research & Strategy

The ongoing Middle East conflict has increased global macroeconomic uncertainty, primarily through higher energy prices, elevated inflation risks and rising government borrowing costs. Renewed inflationary pressures, driven by oil price volatility linked to disruption risks in the Strait of Hormuz, have shifted expectations around monetary policy, with markets now anticipating a prolonged period of higher interest rates.

While the duration and severity of the disruption will likely dictate the short-term rate trajectory the more pressing topic for European property investment centres on the growth opportunity as Europe reshapes itself to become more autonomous. Europe is making significant investments in both defence and energy infrastructure to improve its sovereignty and this will generate additional space needs in property markets (see our recent [Spotlight on: Defence articles](#)).

Real estate market fundamentals across all major property sectors in Europe remain robust with very low vacancy rates – particularly for well located, highly amenitised and accredited space which occupiers are increasingly demanding. In order to cater to this rise in demand we will need to see additional space being constructed but as the inflationary impacts of higher oil prices filter their way through various input components, higher rent levels will be required to justify the increased replacement cost. This should further enhance the market rent growth and indexation opportunities for standing core assets in Europe as the region’s growth story combined with strong occupier markets allow it to lead global property markets into the next stage of recovery, which is expected to be driven by NOI growth rather than yield compression.

All property global Total Returns



Source: MSCI Global Annual Property Index, BNPP AM Alts, data as at April 2026



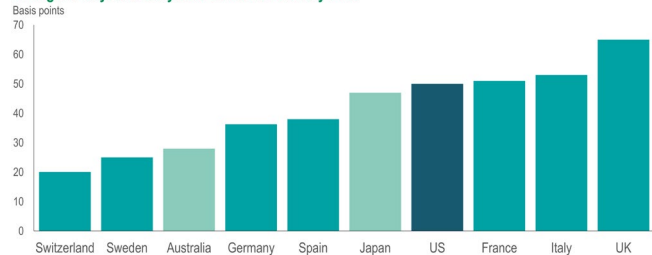
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Renewed bouts of inflation on the back of the Middle East conflict shift the rate trajectory

Renewed bouts of inflation, triggered by the escalation of Middle East tensions and the spike in oil prices following disruption in the Strait of Hormuz, have materially shifted the macroeconomic outlook. Rather than transitioning towards a more accommodative monetary policy environment, markets now anticipate a prolonged period of elevated interest rates.

This has introduced renewed uncertainty around the trajectory of monetary policy and delayed the expected recovery in real estate capital values. Market pricing clearly reflects expectations of higher-for-longer rates — a sharp reversal from the easing cycle anticipated prior to the conflict. Within Europe, those economies with pre-existing concerns around fiscal positions, namely Italy, the UK and France, have seen the largest increases in government borrowing costs, further complicating their fiscal outlook. This shift in rate trajectories comes with important implications for real estate investors, particularly from an equity perspective where higher financing costs delay a value recovery, in contrast to debt strategies which continue to benefit from higher base rates and strong income generation.

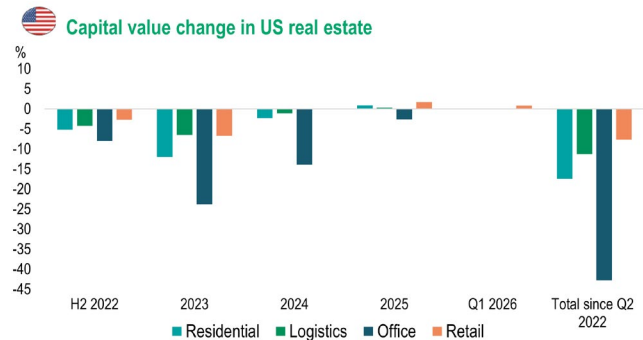
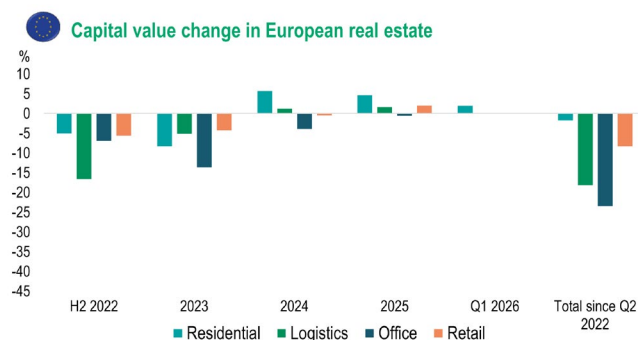
Change in 10 year bond yields since 28 February 2026



Source: Macrobond, BNPP AM Alts 2026, data as at 4 June 2026

Real estate values have stabilised with the strongest sectors and markets starting to experience capital value gains

European real estate is entering the next phase of the cycle, characterised by stabilising capital values and a gradual recovery in performance — albeit within a more volatile macro backdrop. Momentum had begun to build through late 2025, supported by improving sentiment, strengthening occupier fundamentals and early signs of capital market recovery. However, recent geopolitical developments have disrupted this trajectory, reinforcing inflationary pressures and tempering investor confidence. European capital values were quicker to reprice this cycle compared to the US which continues to experience valuation declines and a notable discount in the secondary market for fund interests. Within the property segment, the resilience of the wider living sector is continuing to support valuations alongside the logistics segment while the recovery in retail and office occupier markets in Europe is also driving evidence that these sectors had also started to join the early phase of the valuation recovery. However, these valuation gains have been driven more by capitalising growing NOIs and market rent growth rather than yield compression and given the reverse in rate trajectory and very limited scope for yield compression in the short-term, the recovery is now expected to be predominantly income driven. The critical consideration for equity investors is therefore the extent to which current yield levels provide sufficient buffer against higher financing costs. While, modest rate increases can be absorbed through rental growth, a more material repricing of borrowing costs would likely reintroduce downward pressure on capital values. Consequently, the pace and consistency of recovery remain closely tied to inflation dynamics and central bank responses.



Source: INREV Asset Level quarterly Index, NCREIF ODCE Index, BNPP AM Alts, data as at 10 June 2026

Continental European real estate compares favourably from a relative value perspective

From a value perspective, real estate in Continental Europe continues to compare favourably on a relative basis, particularly when assessed against government bond yields. Despite the upward shift in risk-free rates, the Eurozone still offers a compelling yield premium, with prime property transaction yields in the region remaining meaningfully above sovereign bond levels — for example, cross-sector prime yields of around 5% continue to provide an attractive spread over long-term government borrowing costs. This spread has nevertheless compressed relative to long-term historical averages, reflecting both the legacy of the ultra-low yield environment prior to 2022 and the recent repricing in financial markets. However, in a global context, Continental European spreads — particularly in sectors such as logistics and retail — remain relatively attractive compared to other developed markets. The normalisation of spreads following the rate shock has resulted in a more balanced risk-return profile, with real estate continuing to offer a meaningful risk premium over bonds. As such, while absolute spreads may appear tighter than historic norms, the relative value proposition of European real estate remains intact, supported by higher entry yields, resilient income profiles and a more advanced repricing cycle compared to other regions. Ultimately, the European property market looks well placed to lead the global property markets in the next phase of this cycle’s recovery.

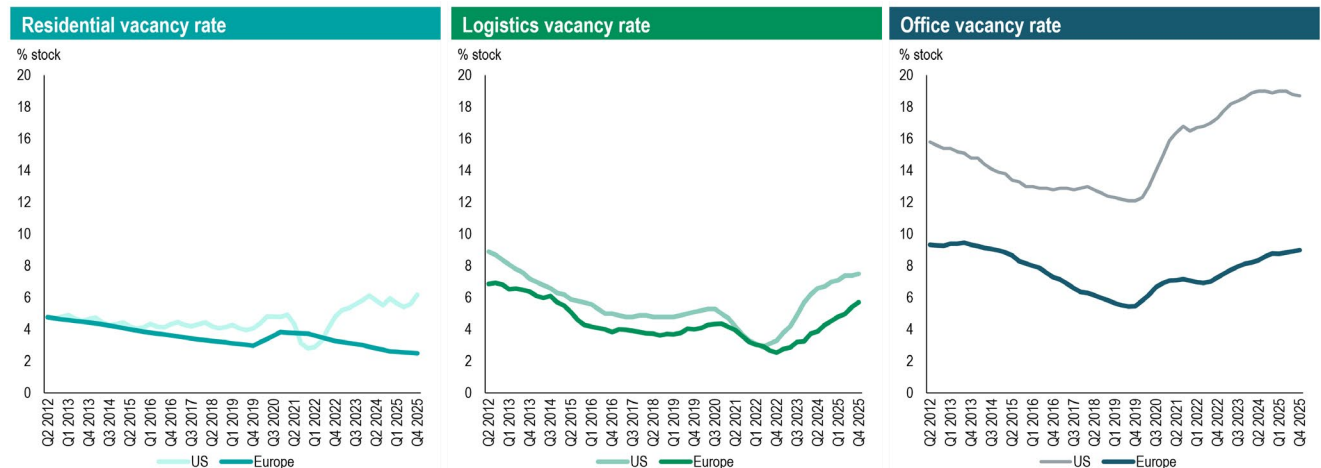
Global property pricing



Source: Macrobond, MSCI Real Capital Analytics, BNPP AM Alts, data as at 8 June 2026

Sector fundamentals in Europe are proving more resilient than the US due to a more muted supply cycle

Occupier market fundamentals across Europe remain notably robust, underpinned by a structurally constrained supply pipeline. This contrasts with the US, where the new supply pipeline was well underway in the run up to the pandemic, and while it has slowed recently, the wave of development completions which did come online in the past five years has disrupted the supply-demand balance and slowed rent growth. By contrast Europe continues to suffer from its age of stock issues and tight fundamentals at the prime end of the occupier market. Development pipelines have been constrained in recent years, limiting new supply and supporting a recovery in occupier markets. When combined with the strong focus on location and building quality prime rental value growth continues to eclipse inflation with most European markets now boasting record nominal rental levels. Strong demand, combined with occupiers’ increasing focus on quality, is reinforcing pricing power for best-in-class assets. In these top performing markets, we are starting to see signs of occupiers widen their locational focus beyond key city centres and into well-established fringe locations to take advantage of the widening price gap that has emerged. However, there remains a key focus on building quality where no compromise is being made, and property valuations are increasingly showing evidence of this tiering by asset quality.

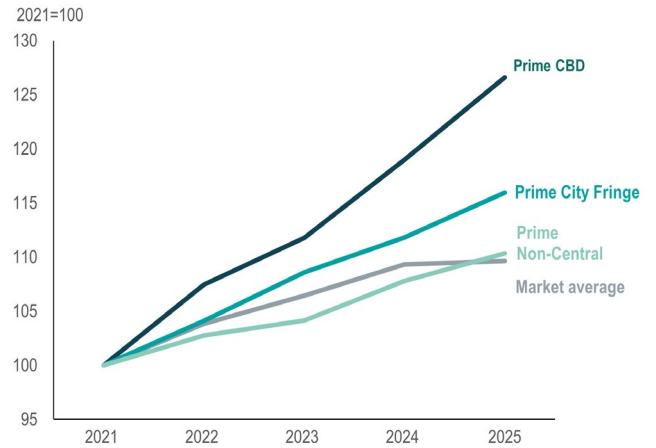


Source: CBRE EA, JLL, Green Street, BNPP AM Alts, data as at Q4 2025

Continued macro and geopolitical uncertainty make a strong case for diversification

The evolving rate outlook is expected to create short-term headwinds, placing upward pressure on property yields which means income growth prospects will therefore likely remain the key driver of outperformance for the foreseeable future. There has been a notable shift within sector performance whereby the ‘beds and sheds’ focus has widened to include retail, office and hotels as their occupier fundamentals have dramatically improved. Demand is strengthening across a broader range of sectors, enabling rental growth to re-emerge as the primary driver of returns. This shift is particularly evident in sectors that have undergone structural transformation. The retail sector provides a useful illustration of this dynamic. Having absorbed a prolonged period of disruption driven by e-commerce and changing consumer behaviour, the sector has undergone significant operational and strategic adaptation. Retailers have increasingly embraced omnichannel models, integrating physical and digital platforms to enhance the customer experience. As a result, occupancy rates are recovering, rental growth is returning, and prime assets are experiencing renewed tenant demand. In certain markets, particularly in Southern Europe, high-quality shopping centres are now seeing tangible supply constraints, with key tenants expanding their footprints. However, within each segment there is a growing divergence and tiering of performance driven by underlying asset quality as both occupiers and investors are focusing on top quality assets. Beyond traditional sector or market calls, we think active asset management initiatives and a focus on the top tier of assets within a diversified sector allocation will likely have a stronger impact on portfolio performance during the next recovery phase. Considering this dynamic alongside heightened macro and policy uncertainty, it is reasonable to make the case that wider diversification will likely provide a certain degree of vintage insurance should adverse scenarios take hold.

Office rental value trends by quality and location in Europe

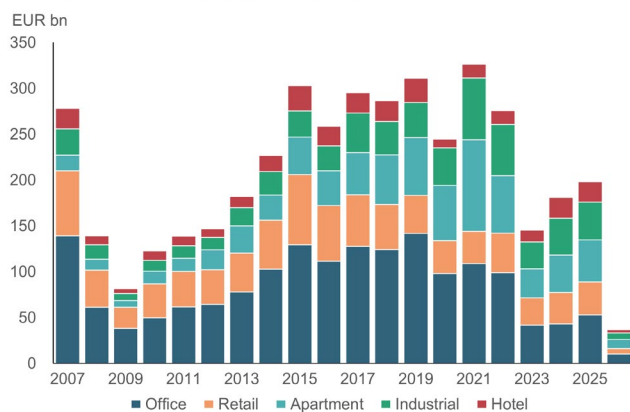


Source: CBRE, BNPP AM Alts, data as at June 2026

Wind out of the sail for transaction activity momentum

We were starting to see signs of a rebound in transaction activity as we progressed through 2025; however, the recent Middle East conflict has had a notable impact on investor sentiment – as evidenced in the recent INREV investor consensus indicator. That said, the pan-European core funds which contribute to INREVs ODCE index have experienced the second quarter of strong net inflows with Q1 2026 reporting €540bn of net inflows. In volume terms, activity remains most active in the residential and logistics segments but there is a notable return of interest for high quality office and retail buildings which are starting to see a bit of a resurgence in activity. This growth and widening in transactional activity is being supported by a more diverse base of investors beyond the high net worth and private buyers to now include the listed players, sovereign wealth funds and some insurance/pension funds. Also notable is the narrowing in pricing and heightened trading levels in the secondary market for private fund investments with European funds trading at a much lower discount to NAV than their US counterparts.

Europe transaction volumes by sector



Source: MSCI Real Capital Analytics, BNPP AM Alts, data as at 8 June 2026

INREV consensus indicator



Source: INREV, BNPP AM Alts, data as at June 2026

European core real estate is entering the next phase of the cycle, marked by stable capital values, strengthening occupier fundamentals and a gradual recovery in investment activity, albeit within an environment of elevated geopolitical and macroeconomic uncertainty. Recent developments in the Middle East have reinforced inflationary pressures and contributed to higher government bond yields, tempering investor confidence and recalibrating expectations for the trajectory of interest rates. In this context, the scope for near-term yield compression remains limited after European markets have undergone a relatively swift repricing and are beginning to show early signs of recovery. Capital value gains are now being supported by income growth rather than further yield movement, underpinned by structural supply constraints and resilient occupier demand across key sectors. At the same time, performance dispersion is becoming more pronounced within sectors, with asset quality, location and sustainability characteristics increasingly determining outcomes. This dynamic is reinforcing the importance of selective capital deployment and active asset management. Looking ahead, a focus on portfolio diversification and income resilience is likely to remain central, with European core real estate well positioned to deliver stable, income-led performance as market conditions continue to normalise.



By **Justin Curlow**, Global Head of Research & Strategy, Alts



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