Nordic Property Breakfast: Stable region still offering diverse long-term values

PIE's Nordic Property Breakfast on May 12 brought four experts together to discuss the theme: Given large local capital pools, can foreign investors find true value in the Nordics? Held at the London offices of law firm DLA Piper, PIE welcomed (left to right): Simon de Chateau, chief investment officer at Alma Property Partners, based in Stockholm; Jonas Grander, founder and managing partner of Nordika Fastigheter, based in Stockholm; Andrew Smith, partner and managing director at Catella Corporate Finance, based in London and Stockholm; and Petr Zemcik, director of economic research at Moody's Analytics, based in London.

Nordics property values still evident

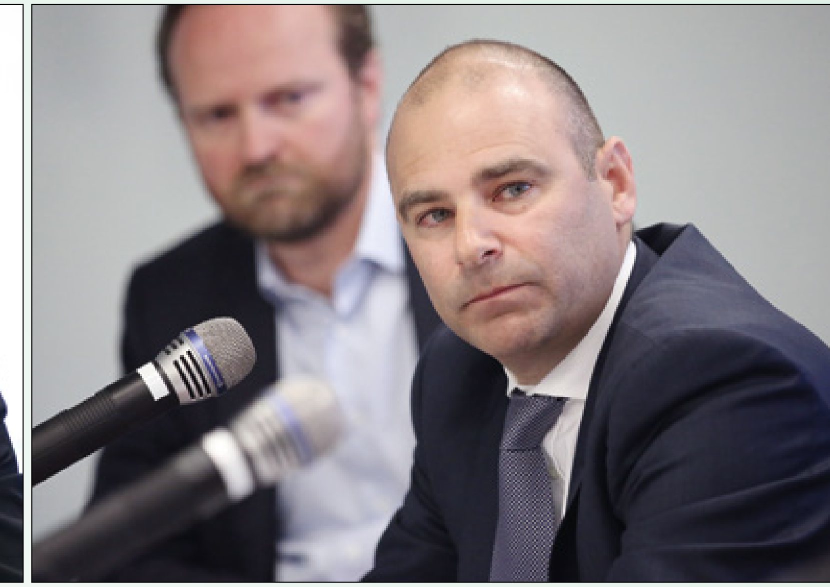
International investors seeking property in the Nordic region face fierce competition from well-capitalised domestic institutions but can still find interesting acquisitions in sectors such as industrial and residential, PIE's Nordic Property breakfast heard on Tuesday.

Nordic investments slipped down the agenda for many international groups over the last few years as buyers focused on core deals in UK, Germany and France, as well as opportunistic deals in deeply distressed locations like Spain. However, the underlying strength of many of the Nordic economies is drawing people back to the region. "Yields came back very strongly in places like Spain. People in this room are starting to think about the Nordics because there is a strong base," said Smith. However those returning institutions face very stiff competition from large, well-financed domestic buyers, particularly large listed Swedish companies. "With the cost of capital as low as it is, the Swedish real estate groups have been rolling up their sleeves and getting invested in transactions. And that has locked out international buyers," he said.

Grander agreed the domestic appetite is wide-spread and includes pension funds as well as wealthy individuals. "Swedish, Danish and Norwegian institutions want to step up exposure to real estate and they are happy to do it in their local markets," he said. In contrast, Finnish investment groups are divesting assets in their local markets to redirect their capital abroad, as the Finnish economy – the only Nordic state in the Eurozone – continues to contract.

Zemcik said Nordic countries share similarities but have their own very specific economic and political characteristics. "It looks like a homogenous region but they are very different countries," he said. He sees moderate growth across the region with the exception of Finland, suffering from closeness to Russia and also the decline of major revenue earning firms such as Nokia, taken over by Microsoft.

Understanding the economies' differences can give investors an advantage. "One of the attractions of the Nordic region is that the markets move slightly differently; they have different cycles," said de Chateau. "For large institutional investors, Nordic markets are pretty competitive." That competition is obvious from yields that - for core office - can touch 4.25% in Stockholm, 4.5% in Copenhagen, and 4.75% in Helsinki, the panel said. However, more secondary locations in the major cities can offer yields of between 5.5%-7%, de Chateau added. Zemcik sees residential investment in Copenhagen yielding 5%, while Smith sees logistics and industrial deals offering 6% of more, even with the sector proving a hot target. "There are always objectives to be found in the local markets, and you will not be left behind with all the dogs," Grander added. ■ pie



Sweden dominates a diverse region

The Nordic real estate market presents investors not only with four different currencies but four very different economies, not to mention different cultures, the Breakfast heard. Sweden is by far the largest and most active market.

"The biggest mistake is to see the four markets as one market," Grander told the Breakfast. While Sweden – the largest of the four with a population of about 9.5m – is an industrial nation based on manufacturing, Denmark is more of a trading nation. Norway, the wealthiest of the group, is tied to its massive offshore oil industry. "We tend to view Norway as a derivative of the oil price, and we tend to stay away," Grander said. Finland, meanwhile offers the highest potential yields, de Chateau added, though is the least liquid of the four.

However, it is Sweden and its capital Stockholm that dominate the investment scene in the region. Some €20bn of property transactions are carried out in Sweden in a typical year, compared with €4bn in Finland, Smith said. "Stockholm takes the cake in terms of volume and liquidity. But I would also say there is just a lack of stock, so it's quite difficult to actually trade on that."

Sweden has other attractions, including low unemployment, a number of large global corporations, and high levels of innovation. "Malmö and Stockholm are two of the markets with the highest number of patents per person in Europe," Zemcik said. Since 2003, there are five companies that have started up in Stockholm and now are worth over €1bn, he added. ■ pie

Industrial on rise as e-commerce surges

The strong manufacturing heritage of Sweden, with firms including toolmaker Husqvarna, truck manufacturer Scania and white goods group Electrolux, combined with a solid economy and surging requirement from e-commerce are causing industrial property to heat up.

Zemcik noted that analysis of income and spending trends by Moody's Analytics across the region also marks clear winners and losers. The disposable income of people in most of Sweden's metropolitan areas grew by over 30% between 2009 and 2014, while retail sales rose more than 25% in the same period – equating to roughly 5% a year. Norway has a high level of income and retail sales, though slower growth. Further east, Finland has had double-digit

Catella's Andrew Smith (top left) told the Breakfast that Nordic stability is a major attraction to insitutions. Nordika founder Jonas Grander (top right) added that a major mistake is to see the four markets as one; Finland is markedly weaker at present. Moody's Analytics Petr Zemcik (above) said an analysis of income and spending by Moody's Analytics marks out the clear winners and losers

Antti Niemi, one of the Nordics leading M&A lawyers (top), stands in intensive discussion in a packed PIE Nordic Breakfast last month. Alma Property Partners' Simon de Chateau (centre) told the panel that strong demographics mean housing and care homes also hold strong future value across the region. Audience members (above) found good networking opportunities.

retail growth over the period – despite its ongoing recession – and some income growth, he added. But Denmark has had the worst experience, with retail sales down everywhere except Copenhagen where they are just 1% higher than five years ago. "Sweden has been the star performer of the Nordic countries. From an economic perspective, the growth is there," Zemcik said.

Smith commented: "Industrials seems to be the darling asset class at the moment." He also drew attention to the countries' AAA ratings - excluding Finland - and a "fantastic logistics set-up". He highlighted the upcoming trade of a huge packet of industrial properties - finally announced a few days later by private group Nordic Real Estate Partners. "This will be the largest logistics transaction that has ever taken place in the Nordics and the largest in Europe since the crisis," Smith said. However core yields of 6% are still some way above new lows being tested in the UK, citing a Standard Life purchase in Britain at 4.2% yield.

Grander commented: "Logistics in good locations is performing very well. On the other hand, yields are coming down quite rapidly. That's a consideration to bear in mind." The rising popularity of logistics contrasts with concerns about some large retail sites, however. "Over time, that may take a severe hit due to ecommerce picking up," he added.

Changing consumption patterns are also shaking up the retail offering, de Chateau told the Breakfast. People increasingly want to head to city centre locations where they can shop, eat out and meet friends, rather than large out-of-town malls. The trend has already taken hold in Stockholm will move outwards. "We believe this is going to spread to regional cities. There are a lot of under-invested assets in those cities sitting with passive investors who don't really have it as their business plan to upgrade and be part of that transition," de Chateau added. ■ **pie**

Housing, state-backed care also with value

High employment compared with other parts of Europe, and a strong urbanisation trend is making Nordic residential investment appealing for large institutions, the PIE Breakfast heard. But care homes of various kinds also have value.

"Population growth in cities like Stockholm is among the highest in Europe," de Chateau told the Breakfast. "At the same time, you have a shortage of housing. There is simply not enough new development to meet that population growth." Home prices are rising across the region as a result.

"Residential is a really good sector to be focusing on in the Nordics," agreed Smith. Catella recently worked on the sale of a residential block in Copenhagen which had been built with funding from a Danish pension fund. The deal allowed the buyer to acquire the whole development and sell apartments individually. "That's financially rewarding," he said. The firm sold a similar portfolio in Sweden, playing into the growing trend among Swedes to buy rather than rent.

Professional purchase of residential property to rent out also has potential, but is not without risks. Residential in Copenhagen can yield 5%, Zemcik said. Even if investors should not rule out the risk of rent controls, underlying trends are good; unemployment rose only slightly during the financial crisis, in contrast with much of the rest of Europe where joblessness rose more sharply. "The labour market in general in the Nordics is more flexible and there is a higher participation rate of women," Zemcik said. "From the perspective for longer-term growth this could be place to go. The demographic situation seems to be good."

Grander said the attractions are also obvious in associated sectors such as assisted living for the disabled disabilities and care homes for the elderly - assets which in the Nordics are usually backed by municipal governments and have indexed rents. Nordika recently bid on a care home asset in Stockholm, supported by a 20-year lease, yielding 5.5%. "We think that's expensive but you can get higher leverage on that," Grander said. "And also in relative terms to other markets it's a very solid investment with long-term stable cash flow. You get to a good return on equity which is far superior to what you can achieve in more risky areas." ■ **pie**