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The strong equity market performance for the listed property companies in Q2 is indicating continuously high activity on the transaction market during the autumn

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Transactions amounting to SEK 23.9 billion took place in June, compared to SEK 22.8 billion and SEK 19.9 billion during the same month in 2019 and 2020. The rolling 12-month transaction volume has been in an uptrend since mid-2018 and increased somewhat to SEK 175 billion (from SEK 171 billion in May).

The number of deals exceeding SEK 80 million ended up at 39 in June, less than the 48 and 53 deals that took place during the same month in 2019 and 2020. As a result, the rolling 12-month number of transactions fell back somewhat to 368 deals (in line with the long-term average). The by far largest deal of the month was SBB's acquisition of 70 per cent of the residential owner/developer Riksbyggen's daughter company Unobo. Unobo currently owns 5,368 apartments. The second largest deal was Platzer's acquisition of three Life-Science properties in Gothenburg from the municipal company Higab for around SEK 1.9 billion. The third largest deal was ALM Equity's purchase of the Stockholm based residential developing company Järntorget for SEK 1.7 billion. Apart from that, Axfast acquired a 16,000-sq.m. office property on Kungsholmen in Stockholm from Blackstone and Areim.

Institutions and funds are the two largest net-investors with rolling 12-month net-acquisitions of around SEK 20 billion respectively. Foreign funds have been active on the market since mid-2020 (especially Blackstone), but some of the Swedish funds have made large acquisitions recently too (like Niam, NREP and Estea). Some of the listed property companies have been large sellers, while others have been major buyers during recent years. As a result, their net-acquisitions have been hovering around the zero-mark since early-2020. However, the listed companies have picked up their rolling 12-month net-investments lately and it now stand at around SEK 5.5 billion.

High quality offices in Stockholm are still considered trophy assets, and there are still investors at good price levels both in Stockholm and the other major cities. However, investors' concern about an upcoming structural shift within the office sector (due to more WFH and increasing area efficiency) has increased further during the spring. Both the supply of assets on the market and investor demand of office properties has declined significantly since the corona pandemic erupted in early 2020. This has led to a massive fall in transaction volume within the office sector. The rolling 12-month transaction volume has declined from around SEK 40 billion in 2019 to SEK 13.2 billion now.

The rolling 12-month number of deals initially held up relatively well but has fallen back significantly since March 2021. The drop in number of deals and transaction volumes have been especially large on the Stockholm market. Investors continue to focus on residential rental properties, public properties and logistics/mix industrial properties, where the yield compression has been powerful since the spring 2020.

The fiscal stimuli have been massive in all large economies since the corona pandemic erupted. Simultaneously, the central banks have flushed the market with liquidity, buying a wide range of assets. Six major central banks (the Fed, ECB, BoJ, BoE, PBoC and the Riksbank) have increased their compared balance sheet by USD 10.3 trillion since February 2020. This is in line with the total USD 10.6 trillion that they increased their balance sheet with during the entire decade from February 2010 to February 2020. The stimuli have had a substantial effect on economic growth. OECD recently upgraded their forecast for the global GDP growth in 2021 to 5.8 per cent growth (from 4.2 per cent in its December forecast). Combined with a global GDP growth rate of 4.4 per cent in 2022, this would bring most of the world back to pre-corona levels by then according to the organisation. The Fed has updated its GDP growth forecast to 7 per cent in 2021 and 3.3 per cent in 2022. The stronger economic growth means that the financial conditions are easing further (as banks are lending more). The price index of S&P 500 has been moving tightly in line with the total assets of the six major central banks over the last decade. Also, average yield levels on the Swedish logistics/industrial property transactions are tightly correlated to assets of the six central banks, where the central bank assets are a leading indicator 12 months ahead.

Growth expectations are now about as high as they can get in this cycle. Economic sentiments remain at historic peaks in most Western economies (especially within the manufacturing sectors) and the Chinese economy engines on at a high speed. World trade volumes increased by over 25 per cent year-on-year in April. Although the strong growth rate was due to base ▶

effects from the sharp drop in trade after the pandemic erupted last spring, the average month-on-moth growth rate has been impressively strong at 1.3 per cent since trade volumes started to stabilise from August 2020 and onwards. This can be compared to an average monthly growth rate of zero during 2018–2019. Sweden is an export dependent country, and our economic growth is very dependent on the trajectory of world trade. Swedish Manufacturing PMI is at an historic peak level and our exports growth was up 30 per cent year-on-year in May. However, the massive fiscal stimuli that have been applied in especially the USA are now gradually being wind down. It is becoming increasingly clear that Biden will not succeed in getting all his stimulus proposals passed by Congress (a USD 1 trillion infrastructure package is currently on the table, a significantly smaller figure than just a few weeks/months ago). Fiscal stimuli in the USA represented 10.5 and 11 per cent of GDP respectively in 2020 and 2021. In 2022, this figure is expected to fall back to just 2.3 per cent. However, it is likely that employment growth and wage growth will compensate for the reducing fiscal stimuli (this is very much depending on the trajectory of the corona pandemic though).

The Swedish listed property companies have had an extremely strong development over the last quarter and the average equity price for 39 of the largest listed property companies has recovered all ground they lost against the OMX Stockholm 30 during the first quarter (the equity prices are up around 20 per cent in average in Q2). This development peaked in mid-June when the Fed announced a slightly more hawkish stance than expected by the markets, and equity prices have dropped somewhat since that. However, prices seem to have bottomed-out in the short-term and have been overall flat over the last week. One reason behind the strong performance of the listed property companies during recent months is that the real interest rate has been in a downtrend since late March. Based on the strong equity price development of the companies focusing on residential/public properties (up around 30 per cent in Q2), as well as the logistics/industrial and mix commercial properties (up 18–25 per cent in Q2), there will continue to be a major inflow of capital into these property sectors at the property market for at least six months ahead or so. After all, the approximately 30-per-cent-increase that has taken place for the residential/logistics companies in less than three months represents 15–20 per cent up in the underlying asset values. As a point of reference, the average equity price for companies that focus on office/retail properties has only increased by around 8.5 per cent in 2021 (the equity prices for this group of companies have, however, been in a relatively flat up-trend since March).

The equity market premiums (to all capital employed) soared during Q2 and now stand at 18.2 per cent in average for 32 listed property companies. There are major premiums on companies that focus on mix industrial properties, well located logistics, residential rental properties (especially companies with strategies that include new production or project development) and/or public properties. There are, however, still equity market discounts for some companies with a focus on retail and/or office properties.

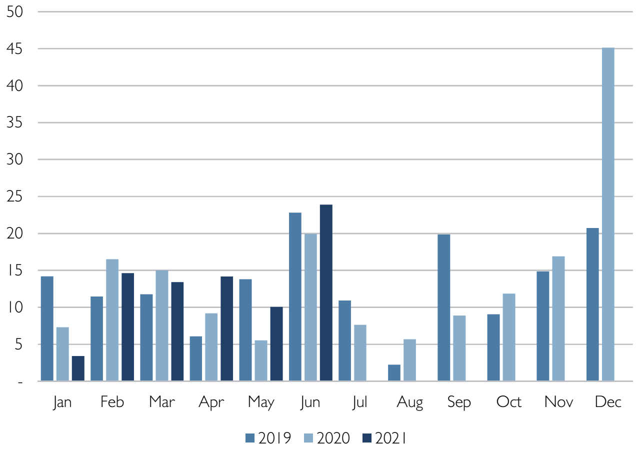
The major central banks have reassured markets at multiple occasions since the spring 2020 that they will keep on stimulating the economy a good way into the recovery, even if inflation overshoots the targets for a good while. However, financial markets panicked somewhat after the Fed in mid-June indicated that it expects to start increasing interest rate in 2023. This was earlier than expected as most Fed officials previously predicted that current rates would be maintained until at least 2024. The FT and the University of Chicago recently made a survey polling 52 leading academic economics on the likelihood that the Fed policy rate will be raised by 50 basis points by the end of 2023 (as indicated by the Fed dot plot). A majority of the respondents said the likelihood of a move of that size was more than 75 per cent, and a large minority put it as high as 90 per cent. The survey respondents see inflation as the biggest driver of Fed's officials changing thinking regarding the timing and speed of future rate rises. Inflation has surged even beyond the loftiest estimates in most large Western economies during the spring. In the USA, the CPI inflation rose by 5.0 per cent year-on-year in May. Core PCE, the inflation measure targeted by the Fed, was up 3.4 per cent in May, the highest level for 29 years. In Sweden, CPI inflation hit 2.2 per cent in April and fell back to 1.8 per cent in May. Base effects are a major driver behind the higher consumer prices. However, other main contributing factors to the higher consumer prices are supply chain problems, soaring commodity/energy prices and lack of labour which generates wage increases (especially in the USA). When/if the large central banks start to taper their asset purchases and raise rates, this will reduce the volume of capital that is heading for the property market and push up property yields (because this drives up real interest rates).

There is, however, a large risk that central banks are overestimating their ability to depress inflation that has risen to excessively high levels. Asset prices and debt levels are now so high that the economy cannot sustain much higher real interest rates than we have right now. Debt levels (private, corporate and government debt) were at historically record levels even before Covid-19 and are now at absolute historic highs. If central banks remain supportive during the coming 12–18 months (which is very likely), real interest rates can be zero or negative although growth and nominal interest rates are increasing. However, it will be very hard for them to stop stimulating the economy.

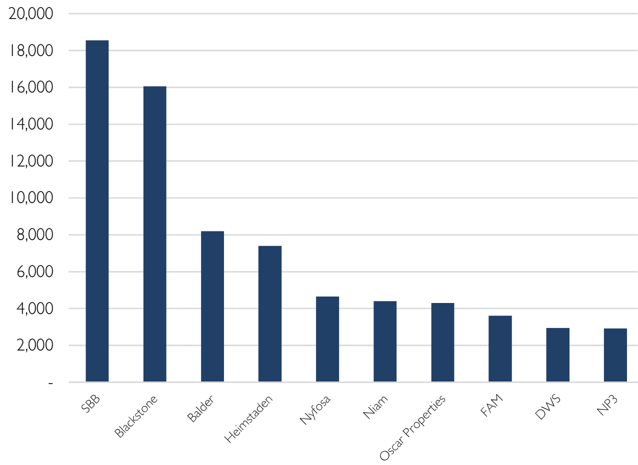
We have probably now entered a new phase in the global economy with ▶

higher political tensions, trade barriers, competitive devaluations, continuously high commodity prices (we may be at the early stages of a new commodity super-cycle), central banks that are aiming at inflation over target (the Fed still wants inflation to be above 2 per cent for a period of time before raising rates), and continuous fiscal deficits directly/indirectly financed by the central banks. According to Catella's main scenario, inflation and interest rates will follow a gradual uptrend from 2022 until the next recession. Real interest rates will likely remain low and not increase until a later stage when investors apply a risk premium on bond yields. At that point, asset prices will enter a long period of macro-economic headwind. As inflation picks up, the global economy will end up in a period of 1970-style stagflation (a combination of increasing inflation and continuously low economic growth). It is not unlikely that higher real and nominal interest rates will result in a major financial crisis and another global recession during the coming five-year-period.

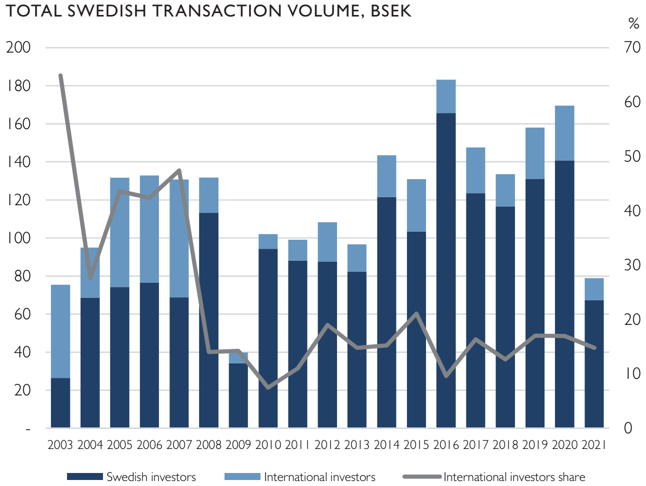
TRANSACTION VOLUME PER MONTH, BSEK



TOP 10 INVESTORS ROLLING 12-MONTH VOLUMES, MSEK



TOTAL SWEDISH TRANSACTION VOLUME, BSEK



INVESTOR TYPE AND REGION