Shift in investor sentiments in September propel logistics and residential prices close to bubble territory

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The transaction activity fell back quite a lot in September. In total, transactions amounting to SEK 7.5 billion took place during the month, compared to SEK 12.4 billion and approximately SEK 19.9 billion during the same two-month-periods in 2018 and 2019.

There were only 17 transactions exceeding SEK 80 million during the months, which can be compared to 24 and 25 transactions during the same months in 2018 and 2019. The rolling 12-months transaction volume was around SEK 132 billion and the rolling 12-month number of deals remains just above 300 deals. This is well below the long-term average of 370 deals, and below the interval of 330–400 deals that the market has normally fluctuated within during the last 15 years. Blackstone has taken a big leap forward on the market and made both of the two largest deals during September. The largest transaction was their acquisition of a logistics portfolio from Nyfosa for SEK 2.1 billion. The second largest deal was Blackstone's purchase of a mixed office, logistics and industrial portfolio located in Malmö harbour, Bulltofta and Arlöv from Wihlborgs for around SEK 1.4 billion.

The longer-term economic outlook has improved lately due to the massive monetary and fiscal stimuli as well as the likely arrival of a vaccine for the Covid-19 during mid-2021. The economic growth throughout the developed world is, however, increasingly dependent on fiscal stimulus as monetary policy has become less effective (the central banks are increasingly taking a supporting role while governments/fiscal policies are taking the lead). In addition, declining competitiveness compared to the emerging markets continues to be a major problem in the USA and Europe (as well as for the other major developed economies). The developed countries continue to counter their declining competitiveness by increasing debt levels (government, private and corporate debt). The focus for these countries should instead be on structural reforms (including increasing the training/education of the workforces and spending on R&D and infrastructure). This is, however, politically very hard as few countries have strong governments with clear political majority for these reforms.

The Republicans and the Democrats have not been able to agree on a new fiscal stimulus package (the last one expired during the summer). However, the administration has come up with a USD 1,500 billion proposal, which would propel growth during the first half of 2021. However, the political climate has deteriorated significantly during the recent week due to Trump's nomination of a new judge to the Supreme Court, Trump's ongoing corona infection and last week's chaotic presidential debate. In Sweden, the economic slump has been relatively mild so far. Although exports have fallen significantly, the domestic economy has performed rather stable. Swedish retail sales recovered significantly during the summer and grew by 3.0 per cent year-on-year in August. The Swedish government coalition has also presented a stimulus package for 2021 amounting to around 2 per cent of GDP (focusing on tax cuts and benefits for low- and middle-income households). Leading indicators are pointing at a Swedish GDP drop of around 2.5–3 per cent in 2020.

However, the economic recovery will likely be weak in 2021 due to a combination of factors. Brexit seems to turn out bad. It is almost certain that an all-encompassing trade agreement is no longer possible (the most likely outcome is a no-deal Brexit or limited agreements covering differed areas). Tensions between the USA and China will most likely continue to rise steadily (regardless of the outcome of the US election), but this is already to a large extent expected by the financial markets.

We are now in the first phase of a second wave of the corona virus and new partial lock-down measures may cause more economic damage in UK, Continental Europe and the USA during the autumn and winter. Although a vaccine may be available relatively soon, it will only be 50–70 per cent effective and will only be broadly distributed among the population by mid-2021 according to RCA Research. In addition, more than one-third of the global population may hold off being vaccinated for the time being (due to lack of trust in the vaccines). Finally, the upcoming US election will likely have a negative impact on the global economy. A narrow victory for one of the parties is the most likely scenario. This could trigger uncertainty and equity market turbulence if it leads to the other party challenging the result (Trump has indicated that he will refuse to peacefully transfer power if he loses). The potential upcoming political turbulence could also delay coming US fiscal stimulus packages.

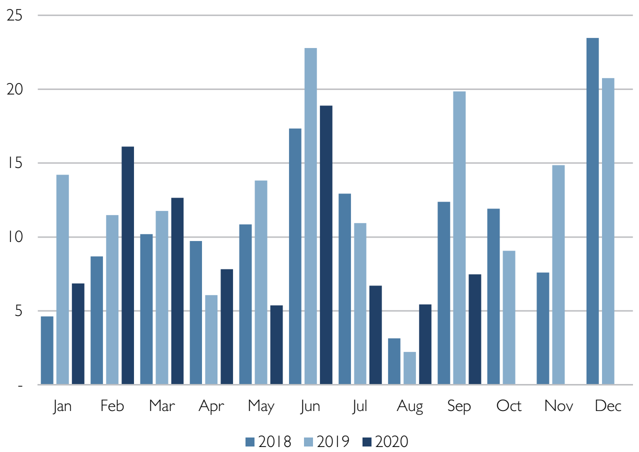
Fiscal and monetary stimuli throughout the developed world are pushing the economy in the right direction though and are heavily benefitting most asset prices. The consensus macro view among investors is low economic growth, low inflation and low interest rates for decades (even if more and more investors are starting to anticipate inflation ahead). Investors are again focusing on building volume and there are portfolio premiums on the Swedish property market. Residential rental properties, public properties and logistics/mix industrial properties in reasonably good locations with stable cash ▶

flows are now the main targets. Investors are increasingly concerned that Covid-19 may be a starting point of a structural shift on the office market. High quality offices in Stockholm are still considered trophy assets though, and there are still plenty of investors as long as there are not too much vacancies and projects. The massive central bank response to the corona crisis has pushed down credit spreads (we saw a massive improvement in Catella's credit market survey, CREDI, last week) and the banks' lending to the property sector will likely hold up relatively well during the autumn 2020 and in 2021. However, companies with high risk in their business models will meet higher credit costs going forward. This will especially be the case if there are further setbacks on the financial market during the coming 12–18 months (which is not unlikely).

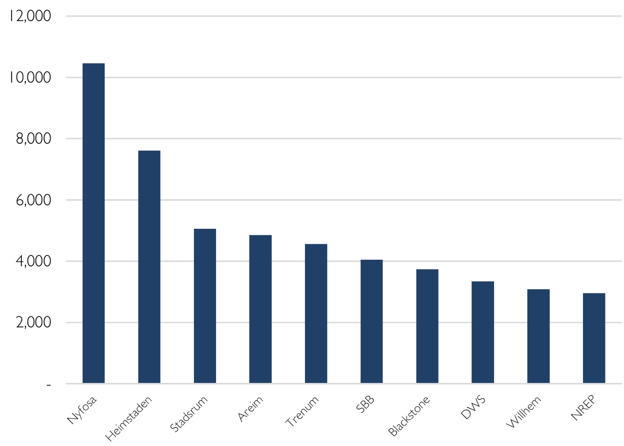
There was a clear shift in investor sentiments concerning the listed property companies during the first half of September, and the real estate sector as a whole performed extremely strong. The average share price for ten of the largest companies* increased by over 20 per cent (the performance during the second half of September has been more sideways though). Investors have obviously seen good value in the discounted companies with large office (and retail) exposure. However, the equity market development has been even stronger for companies with a focus on residential and logistics/industrial properties. The equity market pricing of these property segments now seems to be close to bubble territory. The current pricing will have problems to withstand any major setbacks, either in the NOIs (for instance trough increasing vacancies) or a macroeconomic development with stagflation and gradually increasing interest rates. Negative real interest rates and lots of central bank liquidity will, however, likely benefit companies with portfolios allocated to stable segments like residential properties, public properties and mix commercial properties for another 18–24 months. Property portfolios with higher yield levels also tend to sustain higher market interest rates better than their low-yielding counterparts. The equity prices for several of the listed property companies are, however, likely close to a structural peak and the trend will go sideways or decline during coming years for many of the companies, especially for companies with large shares of their portfolios including commercial properties (offices/retail) in the major cities.

* Atrium Ljungberg, Castellum, Diös, Fabege, Fastpartner, Hufvudstaden, Klövern, Kungsleden, Wallenstam and Wihlborgs.

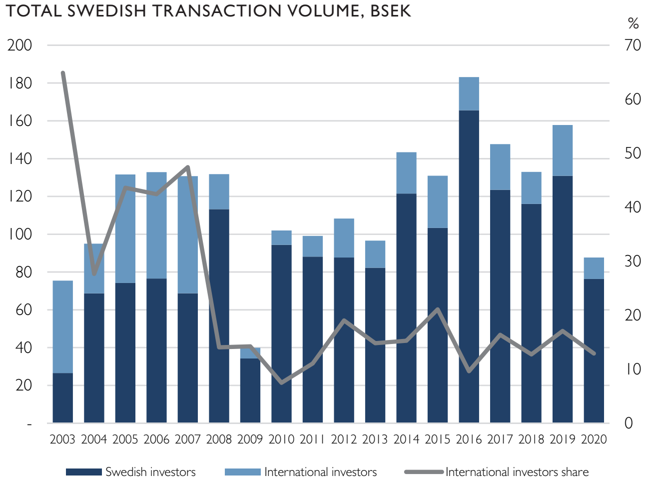
TRANSACTION VOLUME PER MONTH, BSEK



TOP 10 INVESTORS ROLLING 12-MONTHS VOLUMES, MSEK



TOTAL SWEDISH TRANSACTION VOLUME, BSEK



INVESTOR TYPE AND REGION