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The equity market is still indicating a pressure downwards on property yields during the coming 6–12 months despite the recent month's market correction

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Transactions amounting to SEK 48 billion took place during September, compared to SEK 19.9 billion and SEK 8.9 billion during the same month in 2019 and 2020. The rolling 12-month transaction volume has been in an uptrend since mid-2018 and soared to SEK 222.9 billion in September (from SEK 184.8 billion in August).

The number of deals exceeding SEK 80 million ended up at 34 in September, more than the 27 and 23 deals respectively that took place during the same month in 2019 and 2020. The rolling 12-month number of transactions increased to 404 deals (well above the long-term average). The by far largest deal in September (in fact the largest direct property deal since AP Fastigheter's acquisition of Vasakronan in 2008) was Heimstaden's acquisition of a residential portfolio including properties in Sweden, Denmark and Germany from Akelius. The Swedish part of the portfolio amounts to around SEK 36.7 billion. The second largest deal was Oscar Property's acquisition of a mix commercial portfolio from Castellum including 16 properties in the Stockholm and Malmö regions, as well as in Norrköping and Västerås, for around SEK 1.7 billion. The third largest deal was a forward sale deal where Platzer acquired a 32,000 sq.m. office project in central Mölndal from NCC for around SEK 1.5 billion.

The institutions were the single largest net-investors on the Swedish property market for around 10 months up to January 2021. After that, they started to reduce their investments and rolling 12-months net-acquisitions halved from SEK 31.8 billion in January to 15.7 billion in August. Heimstaden's acquisition from Akelius in September changed that entirely as the institutions net-acquisitions soared to SEK 52.8 billion for the 12 months to September. Adjusted for the Akelius deal, however, the volume stand firm at SEK 16.1 billion, well in line with the August figure. In other words, it is too early to say that we now see a trend with higher institutional net-acquisitions going forward (although several Swedish institutions are working to increase their property allocation). The listed property companies have also increased their acquisitions massively during recent months, a deal flow that has been much more board based than that of the institutions. The listed companies' rolling 12-months net-acquisitions now stand at SEK 31.4 billion, up from SEK 27.8 billion the month before. Funds were (along the institutions) among the largest net-buyers on the market during the spring 2021, and their rolling 12-months net-acquisitions peaked at SEK 21.9 billion in April. The funds have, however, slowed down their investment activity during the summer and their net-acquisitions now stand at SEK 14.2 billion. Also, foreign funds have reduced their rolling 12-months net-acquisitions lately to SEK 17.4 billion in September from to 21.4 in August.

The transaction market has become increasingly concentrated during recent years. The share of the total market of deals that are larger than 1 per cent of the total volume has gone from around 20–30 per cent in 2016–2017, to over 50 per cent to so far in 2021. The concentration has been most pronounced within the office, retail and residential segments. In many sub-segments and geographies, the share of the total market of deals that are larger than 5 per cent of the total volume is now in the range 80–100 per cent. The increased market concentration indicates that although volumes are at historically high levels, market liquidity has actually deteriorated on the Swedish property market over the last five-year period. Cross-ownership (when physical persons, institutions and/or asset managers own stakes in companies that are on the opposite side of the same transactions) has also become more common. Cross-ownership has become rather common within the office and the logistics/industrial segments, while it is unusual in the residential and retail property sectors.

The Swedish listed property companies had an extremely strong development between early April and mid-August. The average equity price for 37 of the largest listed property companies was up 45.7 per cent (compared to 7.2 per cent for OMX Stockholm 30). The melt-up peaked on August 20 and the listed companies have now entered a correction-phase. They are down 11.4 per cent in average from the August peak (this can be compared to a decline of 4.5 per cent for the Stockholm OMX 30). The correction is due to factors like the increasing global inflation, the looming energy crisis and investors starting to question how fast and when the major central banks (and especially the Fed) will wind down their monetary stimuli. The worst hit sub-sectors are the companies that are focusing on logistics/industrial and ▶

office/retail properties, down 13.4 and 13.9 per cent respectively since August 20. Despite this setback, however, the equity prices are still up 31.3 per cent in average for the property companies so far in 2021 (compared to 20.3 per cent for Stockholm OMX 30). The average premium to all capital employed for 14 of the largest property companies is currently 8.5 per cent. There are major premiums on companies that focus on mix industrial properties, well located logistics, residential rental properties and/or public properties. There are, however, equity market discounts for some companies with a focus on retail and/or office properties. As a result, the equity market is still indicating a pressure downwards on property yields during the coming 6–12 months, where the largest pressure downwards is for logistics/industrial properties, offices in secondary locations in the Stockholm region and residential properties in more or less all geographies (except for the absolute smallest municipals with weak growth potential). There is also a significant pressure downwards for property yields within the public property sector, basically all over the line.

Prices of a broad range of commodities have increased significantly over the last 12 months, and especially energy prices have been soaring (we may be heading towards an energy crisis this winter). This has also driven up food prices. Crude oil is up 16 per cent since just before the pandemic in early January 2020. Iron ore is up 31 per cent, soybeans is up 32 per cent, corn is up 35 per cent and oats is up 77 per cent during this 19-months period. In addition, European gas contracts for delivery in November has increased to EUR 117.5 per megawatt hour from just EUR 18 six months ago (an increase by 553 per cent). Inflation is starting to be an issue in the developed world, but it is already a major problem in several emerging economies (like Turkey and South Africa) where food and energy constitute relatively larger parts of the consumer basket than in the developed world. Central banks have already raised rates in countries like Russia, Brazil, and Mexico. In addition, Norway became the first major western central bank to raise the policy rate (since the eruption of the pandemic) in September. Although several commodity prices have increased markedly over the last 12–18 months, prices for several of them have actually started to fall back since the summer. For instance, oats are down 45 per cent since late June, iron ore is down 44 per cent, palladium is down 32 per cent, corn is down 18 per cent and soybeans is down 15 per cent. As a result, Catella's CPI Macro Index (a leading index for inflation including 10 leading macro indicators/commodities) is indicating a short-term peak in inflation during the autumn at around 2.75 per cent year-on-year and then a decline to slightly below the 2-per-cent level in early 2022. However, the model does not include indicators that mirrors the current supply chain bottlenecks (because this factor has not been instrumental for inflation during the last decades, and the model is based on historical correlations).

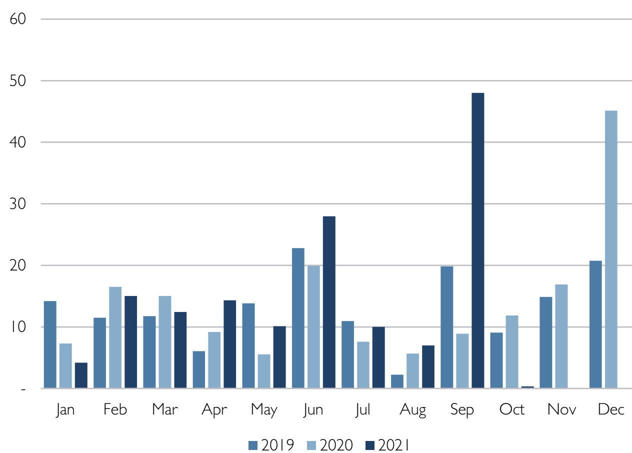
Investors are overall very concerned right now about the combination of gradually declining global economic growth and sticky inflation. The global economy is currently facing a few negative developments including the Delta virus, less fiscal stimuli, government measures that are currently slowing down the Chinese economy (most urgently the development on the property market), central bank tapering/rate rises and deglobalisation. Although the global economy has slowed down somewhat, economic growth is still considerable. The growth rate in world trade volume has declined from a peak of almost 25 per cent year-on-year in April to 9.9 per cent in July. Sweden is an export dependent country, and our economic growth is very dependent on the trajectory of world trade. Swedish Manufacturing PMI has recovered to 64.5 in September (from 60.1 in August) but is still well below the historic peak level from April. The Swedish exports growth has slowed down to 10.7 per cent in August from 30.8 per cent year-on-year in May. The Swedish real GDP growth came out at extremely strong 9.7 per cent year-on-year during the second quarter. The exceptionally strong performance was expected and can largely be explained by base effects (the drop in GDP was extreme during the same quarter last year due to the coronavirus). Catella's GDP Macro Index (which is a mix of six leading indicators for the Swedish GDP growth) is indicating that we are currently on a cyclical peak with a real GDP growth rate of around 4.8 per cent year-on-year in October (this is a little bit above the actual quarter-on-quarter growth rate during the second quarter of 0.9 per cent). Further on, Catella's GDP Macro Index is indicating that economic growth will slow down to around 4.0–4.2 per cent year-on-year in November/December. Four of the six underlying macro indicators are then pointing at a continuous slowdown in growth during the spring of 2022.

There are major uncertainties regarding how the major central banks will respond to the current growth/inflation mix. If the spread of coronavirus will be curbed relatively soon, then wage increases, and inflation will automatically slow down due to a recovering supply side (as the bottlenecks are being sorted out). In this scenario, the central banks can gradually/slowly wind down their stimuli during coming years with one eye on the asset market (the equity and bond markets are extremely sensitive to all signs of tapering and rate increases). If productivity improves in line with this, economic growth will remain healthy and the record-high global debt levels (private, corporate and government debt) will gradually decline as a share of GDP to manageable levels. Long-term real interest rates may gradually increase and the TINA situation (there is no alternative to risky assets) will gradually diminish as risk free bonds will start to provide positive return. This would gradually put an upward pressure on property yields. All in all, this is a rather bright scenario for the overall economy, but a less good sce- ▶

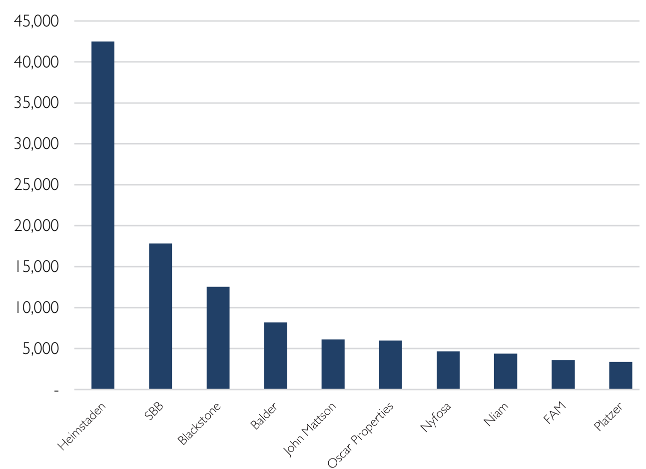
nario for the property market (at least in the short term). It is an especially bleak scenario for property segments with rental markets that have tight connections to the CPI inflation (like residentials, logistics/industrials and public properties). After all, a well-functioning, productive economy can combine healthy growth with low inflation – and healthy growth also means higher/positive real interest rates. In this scenario, the transaction markets will likely slow down to a virtual standstill and market concentration will increase further (it will likely take a very long time for property yields to shift upwards). However, prime offices, and to some extent retail properties, tend to manage higher real interest rates better as long as it is driven by healthy economic growth (as their rental markets have a tighter connection to GDP growth). In addition, the yield developments have been relatively stable in these segments over the last 12–18 months, leaving a major yield gap to risk-free real interest rates.

However, this is not the most likely scenario for the coming years. It seems like the coronavirus has not yet been defeated. In this case, governments and central banks will continue to stimulate the demand side to a considerable extent. In addition, the authorities are unable to efficiently boost the supply side of the economy, which means that the stimuli will keep driving up wage increases and inflation. The US is ahead of Europe in this aspect due to their larger spare capacity. Asset prices and debt levels are now so high that the economy cannot sustain much higher real interest rates than we have right now in an environment with low potential growth. Investors are freaking out as soon as the central banks are starting to speak about tapering or rate hikes (as we see now). Central banks will therefore keep monetary policy as loose as possible for as long as possible. This should ensure that asset prices do not decline significantly. This means that they will do too little too late to curb inflation. Real interest rates remain negative in this scenario, although growth and inflation remain rather high. As a result, nominal interest rates increase, slowly to start with but then faster and faster. As inflation expectations increase, investors may rush out of financial assets/fiat currencies into real assets (like property). This may further increase the flow of capital to property in general, and the residential, logistics/industrial and public property segments in particular (as rents in these segments move in line with inflation). ■

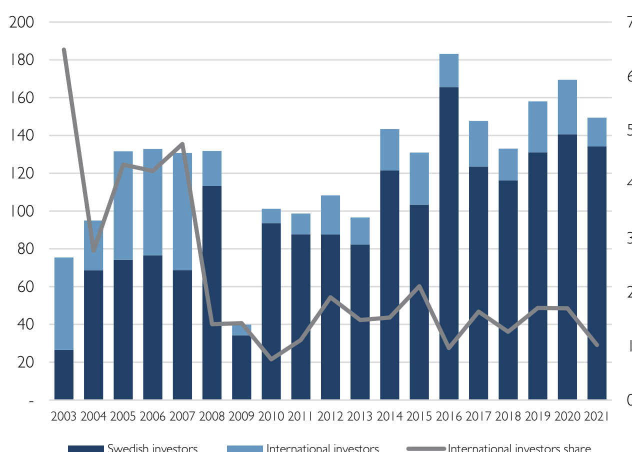
TRANSACTION VOLUME PER MONTH, BSEK



TOP 10 INVESTORS ROLLING 12-MONTH VOLUMES, MSEK



TOTAL SWEDISH TRANSACTION VOLUME, BSEK



INVESTOR TYPE AND REGION