

Cheap money is fuelling a divided property market



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Following a historically low transaction volume in June, a number of large deals took place in July and August. This has kept the rolling 12-month transaction volume at around SEK 125 billion (the long-term average is approximately SEK 120 billion), which is still a significant step down from the peak levels of nearly SEK 180 billion in the spring of 2017.

During the summer, a number of large commercial transactions have taken place. The largest deal this summer was Hemfosa/Nyfosa's acquisition of a large commercial property portfolio from Starwood for SEK 3.6 billion, followed by Regio's acquisition of a centrally located office and retail portfolio in Jönköping for SEK 2.1 billion and Allianz's acquisition of Skandia's head office on Kungsholmen in Stockholm from AMF for SEK 1.8 billion.

One of the most important changes in market dynamics over the past six to nine months is that Swedish pension funds have gone from being net buyers to net sellers. In particular, these pension funds have divested office buildings in Stockholm and retail properties. In addition, international investors (especially funds) have increased their spending and become net buyers in Sweden in 2018 (during 2009–2017 these investors were net sellers).

Nevertheless, Swedish buyers make up 80 per cent of the transaction volume, and listed Swedish property companies have dominated the market.

During the summer, the global economy has exhibited clear signs of weakness and the growth of global trade has decreased significantly. Although there is a siege fire between Europe and the US, the trade war between the US and China has intensified. This coincides with a slowdown in the investment-driven and heavily leveraged Chinese economy. The US economy exhibits continued growth, but there are signs of diminishing growth due to a lack of capacity. The Federal Reserve's gradual tightening of their monetary policy (by raising interest rates and shrinking its bond portfolio) has decreased the liquidity of the US dollar and caused serious problems for emerging markets with large debts in US dollars and trade deficits (such as Turkey and Argentina). Moreover, the Eurozone is also beginning to see decreased growth (despite strong consumption growth in Germany) and investors are worried about Italy's fiscal policy and European banks' exposure to Turkey.

The Swedish currency grew weaker during the summer with the poorest exchange rate against the euro since 1999, which was directly after the financial crises in 2008–2009. It appears that the currency market is expecting a slowdown in the Swedish economy and that the Swedish Riksbank will continue to pursue a more expansive monetary policy than the

ECB. In addition, the Swedish long-term interest rate has fallen and is currently around 0.5 per cent. This is problematic, as a weaker currency causes higher inflation and has a negative impact on the Riksbank's ability to pursue a more expansive monetary policy than the ECB. Housing prices will likely continue to fall during the autumn, as the supply of newly constructed housing is considerably higher than what the market can absorb (particularly in Stockholm and a number of regional cities). Reduced new construction of housing combined with gradually decreasing growth in household consumption is expected to cause a fall in GDP growth in the second half of 2018 and in 2019. The development of the housing market combined with Sweden's dependence on exports and the fact that Sweden is likely to have a historically weak government after the election are not factors that favour the Swedish economy.

The property market is currently driven by the availability of affordable financing for large property companies, funds and institutions. During the past year, property companies listed on Nasdaq Stockholm Main Market have issued corporate bonds for more than SEK 40 billion, with a net increase of the issued volume of slightly more than SEK 30 billion. Furthermore, the average credit margin has decreased from around 250 basis points to below 150 basis points. This is in accordance with the credit market improvements seen in the Catella Real Estate Debt Indicator ►

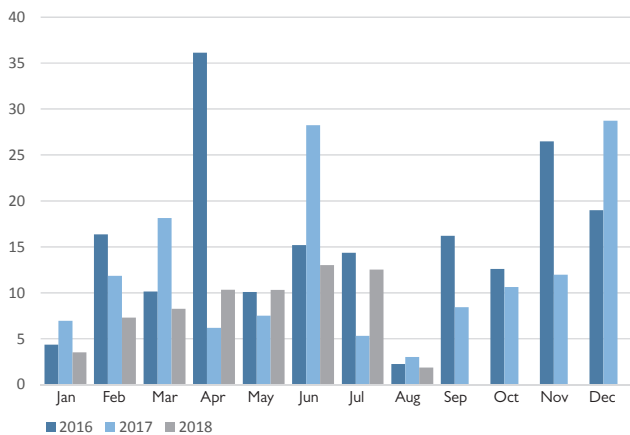


(CREDI) for the second quarter of 2018. Cheap money is a key factor that pushes investors to pursue risk. However, the market is anticipating a gradually less expansive monetary policy. The ECB is expected to decrease or end its purchasing of government and corporate bonds this autumn, while the Riksbank is currently only reinvesting redemptions in its bond portfolio. At the same time, central banks are preparing for the first interest rate hike. For property investors, this entails slightly higher underlying

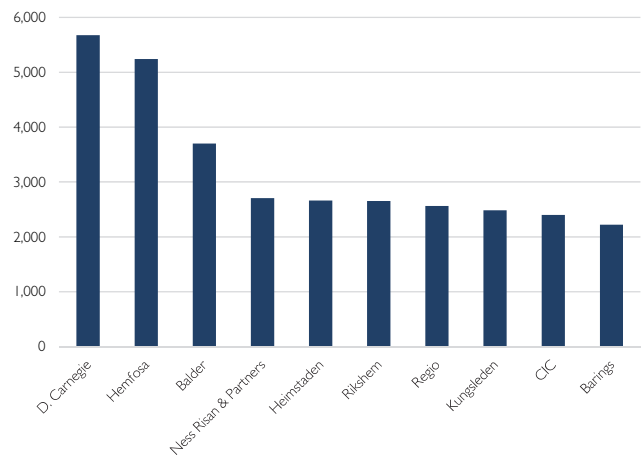
interest rates, but also a higher differences in credit margins between companies with different credit ratings (as bond investors are able to charge more for risk). Although average property yields have fallen in the past year, there are significant gaps between different segments and locations. The supply of newly constructed residential properties and of shopping centres and big box properties is currently high, which has caused property yields to increase throughout the market (except for the

best locations, where property yields remain stable). Most large investors choose to focus on office and retail properties in good locations in the large cities, well-located residential properties and public properties with stable tenants and long leases. These property types have seen a noticeable drop in property yields. Investors have become increasingly selective, and this trend is likely to continue as growth decreases and money gradually becomes more expensive. ■

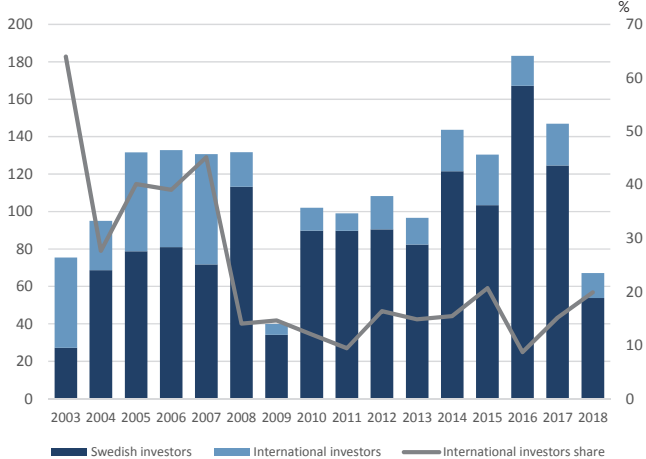
TRANSACTION VOLUME PER MONTH, BSEK



TOP 10 INVESTORS ROLLING 12-MONTHS VOLUMES, MSEK



TOTAL SWEDISH TRANSACTION VOLUME, BSEK



INVESTOR TYPE AND REGION

