

# Vasakronan AB

## Q2 18: Keen on green

Strong market fundamentals in the commercial property space continued to be the main theme as Vasakronan posted a solid Q2 report. Rental income rose 3% y/y to SEK1,690m for the period. On a like-for-like basis, rental growth was 6% y/y, driven by net letting and renegotiation of lease contracts. Increased cash flow from its properties coupled with lower yield requirements led to SEK4bn in unrealised valuation gains on the property portfolio. Net LTV and secured LTV remained fairly unchanged sequentially at 45% and 11%, respectively. We note positively that Vasakronan strengthened its green profile further in the quarter as the share of certified buildings rose to 85% as of end-June from 84% in Q1 18. In terms of pricing, we view Vasakronan's SEK bonds as fairly valued versus the 'A-' curve and therefore maintain our Marketweight recommendation.

### Strong market fundamentals

The commercial property market in Sweden, especially in Stockholm, remains in good shape with low vacancies and rent increases. During the period, Vasakronan posted a like-for-like development in rental income of 6% y/y. Furthermore, the economic occupancy rate improved q/q to 93% as of end-Q2. As a result of increased cash flow on its properties coupled with lowered yield requirements, Vasakronan's result was boosted by SEK4bn in unrealised valuation gains. The valuation changes were mitigated, however, by SEK4bn in dividends and SEK924m in capital expenditure for the quarter, leaving net LTV and secured LTV unchanged compared to last quarter at 45% and 11%, respectively.

Vasakronan was a net seller of properties during the quarter with SEK170m of asset disposal. Instead, to capitalise on the current market momentum, Vasakronan is focusing on project development. While project development could be viewed as opportunistic, the exposure is fairly modest in our view, with a pipeline of c.6-7% of total assets. Moreover, we believe current development projects will increase asset quality.

### Key figures

SEKm	Q2 17	Q1 18	Q2 18	y/y	q/q
Rental income	1,629	1,643	1,690	3.74%	2.86%
EBITDA (rep.)	1,156	1,132	1,213	4.93%	7.16%
Net income	3,936	2,027	5,248	33.33%	158.90%
Investment properties	121,403	128,339	133,518	9.98%	4.04%
Total debt	58,956	58,903	62,397	5.84%	5.93%
Ratios	Q2 17	Q1 18	Q2 18	y/y	q/q
Gross LTV	48.6%	45.9%	46.7%	-1.8pp	0.8pp
LTM NOI margin	72.8%	70.4%	73.4%	0.6pp	3.0pp
LTM EBITDA interest coverage (x)	3.8	4.0	4.1	0.3pp	0.2pp
Net debt/LTM EBITDA (x)	12.5	12.3	13.1	0.6pp	0.7pp
Total debt/total capital	55.4%	52.4%	53.3%	-2.1pp	0.9pp

Source: Company data, Danske Bank DCM Research

## Marketweight

Sector: Real estate

Corporate ticker: FASTIG

Equity ticker 1276Z SS

### Ratings:

S&P: NR / NR

Moody's: A3 / S

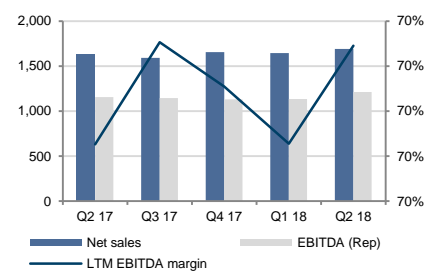
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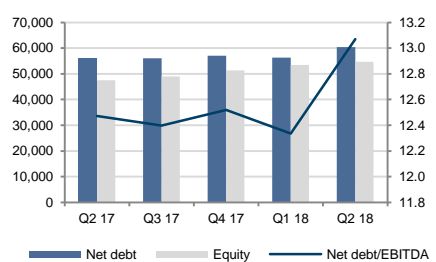
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### Profitability (SEKm)



Source: Company data, Danske Bank DCM Research

### Financial metrics (SEKm)



Source: Company data, Danske Bank DCM Research

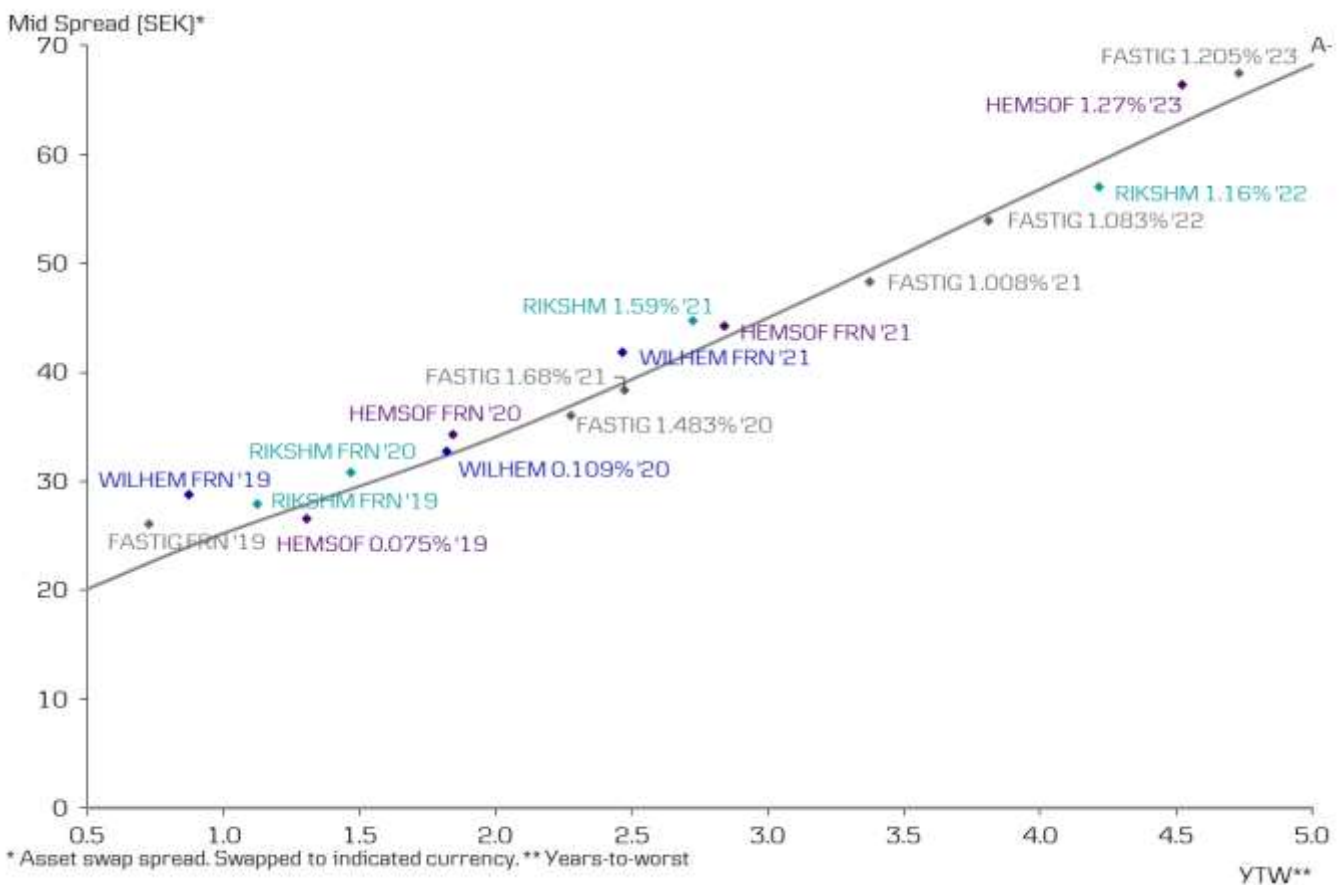
## Ownership support

In 2014, Vasakronan announced that it had entered into an agreement with its owners AP1, AP2, AP3 and AP4 related to a funding commitment from the owners. The agreement stipulates that the owners, on Vasakronan's request, commit to purchase commercial paper issued by the company up to a maximum volume of SEK18bn. The agreement also stipulates a notice period of 24 months. If the agreement is not terminated, the maturity would be extended automatically, with a notice period of 24 months. At end-Q2 18, Vasakronan's outstanding commercial paper amounted to SEK6.2bn.

## Recommendation

Vasakronan showcased a satisfactory operational performance in Q2 18. Considering its solid fundamentals and strong ownership profile, we see Vasakronan's SEK bonds as fairly valued compared with 'A-' rated publicly owned real estate companies such as Hemsö, Rikshem and Willhem, and we maintain our Marketweight recommendation. We note positively the company's ambitious green bond framework, which has received a dark green shading from Cicero.

Chart 1. SEK Large Real Estate Relative Value



Source: Bloomberg, Danske Bank DCM Research

## Company summary

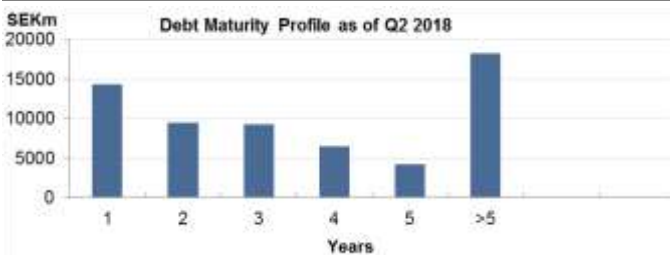
### Company description

Vasakronan is the largest property company in Sweden. The portfolio is concentrated to Sweden's largest cities and in terms of property type, offices and retail make up for the large majority of the total. The current structure of the company was formed after AP Fastigheter (controlled by the state-owned AP funds) bought all the shares of Vasakronan from the Swedish government on 3 July 2008. The merged corporation changed its name to Vasakronan. It is the company's strategy to focus on growth markets in Sweden and own properties that provide a stable return over time.

### Key credit strengths

- High-quality urban property portfolio with low vacancy rates
- Strong ownership from government pension funds
- Diversified client base with large proportion of public sector
- Proven access to capital and bank markets

### Debt maturity profile



### Selected outstanding bonds

Isin	Coupon	Currency	Maturity/Call	Seniority	Rating*
SE0008730774	FRN	SEK	12/12/2018	Sr Unsecured	NR/NR
SE0009241425	FRN	SEK	24/04/2019	Sr Unsecured	NR/NR
SE0006732087	FRN	SEK	22/01/2020	Sr Unsecured	NR/NR
SE0004357192	4%	SEK	01/12/2020	Sr Unsecured	NR/NR
SE0007953930	1.68%	SEK	20/01/2021	Sr Unsecured	NR/NR

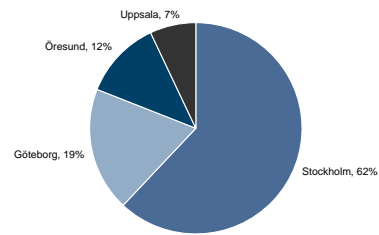
\*Moody's/S&P

### Rating migration



Source: Company data, Bloomberg, Danske Bank DCM Research [all charts and tables]

### Sales breakdown, segments



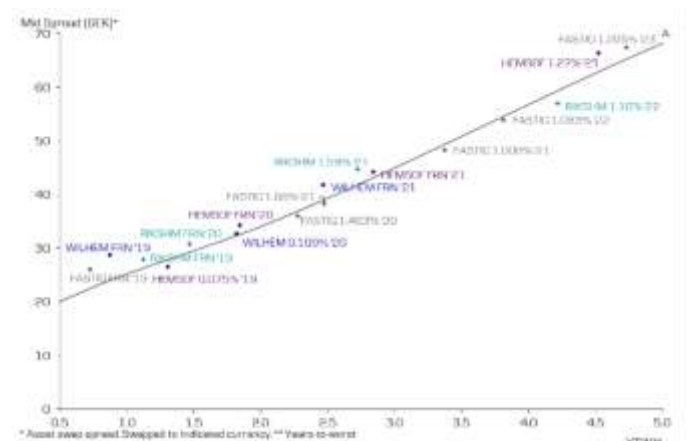
### Key credit challenges

- Earnings are exposed to swings in economic cycles
- Some, albeit manageable, exposure to project development
- Some sensitivity to interest rate movements, although mitigated by strong balance sheet

### Main shareholders

Name	Votes (%)	Capital (%)
AP1	25.0%	25.0%
AP2	25.0%	25.0%
AP3	25.0%	25.0%
AP4	25.0%	25.0%

### Relative valuation



## Summary tables

<b>Income statement (SEKm)</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>	<b>2018E</b>
Rental income	5,899	6,009	6,269	6,490	6,642
Other operating income	0	0	0	0	0
Total revenue	5,899	6,009	6,269	6,490	6,642
Total property related costs	1,675	1,735	1,792	1,812	1,838
Net operating income (NOI)	4,224	4,274	4,477	4,678	4,804
EBITDA	4,109	4,114	4,371	4,553	4,644
Net interest expenses	1,256	1,121	1,052	1,165	1,076
Profit from property management	2,875	3,065	3,338	3,416	3,568
Change in property values	3,519	10,212	12,056	7,973	7,292
Change in financial derivatives	-2,956	598	-764	468	8
Other	-22	-72	-19	-28	0
Pre-tax profit	3,416	13,803	14,611	11,829	10,832
Current tax	-112	-45	0	-95	-791
Deferred tax	-529	-2,814	-3,019	-2,464	-224
Net income	2,775	10,944	11,592	9,270	9,817
<b>Balance sheet (SEKm)</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>	<b>2018E</b>
Market value properties	91,889	103,894	115,922	126,875	137,018
Other fixed assets	51	58	54	46	48
Intangible assets	2,259	2,188	2,171	2,145	0
Deferred tax assets	0	0	0	0	0
Investments in associated companies					
Cash and cash equivalents	1,757	2,301	2,147	1,423	2,008
Total assets	97,184	109,786	122,056	131,970	141,514
Equity	35,094	41,245	46,117	51,377	57,194
Shareholder loans	0	0	0	0	0
Deferred taxes	8,532	11,356	14,362	16,824	17,047
Total debt	47,764	50,750	55,240	58,421	62,638
Other liabilities	5,794	6,435	6,337	5,661	4,635
Total equity and liabilities	97,184	109,786	122,056	132,283	141,514
<b>Cash flow statement (SEKm)</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>	<b>2018E</b>
FFO (adjusted)	2,789	2,855	3,137	3,383	3,518
Cash flow from operations (FFO)	2,902	3,210	3,439	3,111	3,873
Investment (properties)	1,017	470	1,563	440	-1,249
Disposals (properties)	1,574	1,387	2,120	612	1,135
Investments other (net)	-13	-22	0	-5	-6
Capex	-1,021	-1,386	-1,626	-1,489	-2,737
Free operating cash flow	4,472	3,681	5,496	2,674	1,022
Dividends and share repurchased	-4,000	-4,924	-7,933	-4,000	-4,000
Debt financing (net)	1,558	4,033	5,930	3,150	3,452
Change in cash	2,000	2,768	1,980	1,819	586

Source: Company data, Danske Bank DCM Research estimates

## Summary tables

<b>Adjusted ratios (SEKm)</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>	<b>2018E</b>
Sales growth	-2.2%	1.9%	4.3%	3.5%	2.3%
EBITDA margin	69.7%	68.5%	69.7%	70.2%	69.9%
NOI margin	71.6%	71.1%	71.4%	72.1%	72.3%
EBITDA interest coverage (x)	3.3	3.7	4.2	3.9	4.3
FFO/interest coverage (x)	3.2	3.5	4.0	3.9	4.3
FFO/debt (x)	5.8%	5.6%	5.7%	5.8%	5.6%
Net debt/EBITDA (x)	11.2	11.8	12.1	12.5	13.1
Gross LTV	52.0%	48.8%	47.7%	46.0%	45.7%
Net LTV	50.1%	46.6%	45.8%	44.9%	44.3%
Equity ratio	36.1%	37.6%	37.8%	38.9%	40.4%
Total debt/total capital	57.6%	55.2%	54.5%	53.2%	52.3%
<b>Quarterly overview (SEKm)</b>	<b>Q2 17</b>	<b>Q3 17</b>	<b>Q4 17</b>	<b>Q1 18</b>	<b>Q2 18</b>
Rental income	1,629	1,590	1,654	1,643	1,690
EBITDA	1,156	1,145	1,130	1,132	1,213
Net interest expenses	296	295	291	271	265
Net income	3,936	1,512	2,436	2,027	5,248
CFO	646	899	862	953	1,161
Investment properties	121,403	122,999	126,875	128,339	133,518
Total debt	58,956	59,058	58,421	58,903	62,397
Net debt	56,232	56,095	56,998	56,285	60,389
Equity	47,438	48,950	51,377	53,404	54,652
<b>Ratios</b>					
LTM NOI margin	72.8%	73.5%	71.3%	70.4%	73.4%
LTM EBITDA margin	70.0%	70.3%	70.2%	70.0%	70.2%
Direct yield	3.8%	3.8%	3.7%	3.7%	3.6%
Gross LTV	48.6%	48.0%	46.0%	45.9%	46.7%
LTM EBITDA interest coverage (x)	3.8	3.9	3.9	4.0	4.1
Net debt/LTM EBITDA (x)	12.5	12.4	12.5	12.3	13.1
Total debt/total capital	55.4%	54.7%	53.2%	52.4%	53.3%
FFO/debt	1.6%	1.4%	1.4%	1.3%	1.6%

Source: Company data, Danske Bank DCM Research estimates

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Underweight	Underperformance relative to peer group	6 months	8%	15%

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