Swedish investor universe is dominated by pension funds

> Real estate forms 12.8% of the overall portfolio, higher than the European norm
> Maintaining strategic control is a key motivation for Swedish real estate investors
> Sustainability has risen up the agenda to help reduce risks as well as for ethical reasons

The Investor Universe Sweden Study examines real estate's role in Swedish institutional investment, describing the overall investment landscape and investigating investors' motivations for holding real estate and the ways these are being implemented in practice.

The Swedish real estate investor landscape is dominated by the pensions industry. The universe of second-pillar pension related institutions comprised €376 billion in AUM during the fourth quarter of 2018, according to official figures by Svensk Försäkring. Adding this to figures for first-pillar institutions, the total amount managed in the first and second pillars totaled €541 billion.

'The main purpose of the real estate portfolio is diversification. We are selling fixed income in favour of real estate investments, as there is a desire to increase real estate and other specialist investment allocations.'

A pension fund

Swedish pension capital is relatively concentrated and professionally managed, and the organisations involved tend to be highly self-sufficient in the management of their portfolios. All decisions, including asset allocation, currency strategy and inflation hedging, are made internally.

Swedish institutions' allocation to real estate has been steadily increasing over the past nine years, to now stand at 12.8% on average, compared to 11.2% for investors across Europe. The rising allocation is due to strong past performance, an attractive return outlook in relation to other asset classes and a high cash yield compared to fixed income.

The main reason for holding real estate is to diversify risk in the overall portfolio, but income return and other return considerations are also significant. Inflation hedging is less important, but more so for those Government Institutions that are not fully funded.

The Swedish institutions covered by this study are all active investors in real estate, which is integrated into their asset allocation processes. All rely on quantitative tools for their allocation decisions. The majority use an

'We use an asset optimisation approach for asset allocation. The analysis is done by a separate group, and uses a combination of models and tools over multiple time periods. The liability side is not included due to the fund's nature as a buffer fund.'

A government institution

Asset Liability Matching (ALM) model to set their allocations, although the process is not purely quantitative.

Real estate is included with other illiquid investments in the ALM analysis. The framework for analysing real estate allocations tends to be relatively long-term, and can look up to 30 years into the future. All the Swedish respondents indicated a relatively long horizon for real estate investment of more than 10 years. However, they tend to review their strategies quite frequently compared to other European investors, the majority at least every three years.

‘Sustainability is a very important area, and is led by a team of five individuals across all asset classes…For real estate, certification is not a requirement (at the time of investment). Rather, a strategy can include making assets more sustainable (through our investment)’

A pension fund

Sustainability has become increasingly important for Swedish institutions, even if they may define it in different ways, All the institutions responded that sustainability was either ‘important’ or ‘very important’. When asked why, the most common response was that it is a requirement in today’s real estate market. Apart from being an ethical responsibility, sustainability is also seen as making sense from a number of investment perspectives.

Diversity is also deemed as important to Swedish investors. At present, the focus of diversity policies is mainly on establishing equal opportunities for both sexes. An important area of diversity policy for these investors is in determining the composition of boards for joint ventures and club deals.

For further details contact research@inrev.org. The full report is available to members at inrev.org/research.

Swedish institutions expect to invest €2.22 billion in real estate through 2019. Three-quarters intend to increase their real estate portfolio allocation, a share that is broadly consistent with their European peers (78.8%). The remaining 25.0% plan to leave their real estate allocation unchanged. The intention to invest in real estate may well have moderated due to the poor showing of equities towards the end of 2018, which resulted in an increase in the year-end real estate exposure.

Swedish institutional investors, like their European peers, see the biggest risk coming from the macro-economic environment. All those interviewed agree that pricing is keen and are somewhat apprehensive about achieving expected returns. At the same time, they do not identify an unambiguous source of this risk, other than the level of interest rates.

Figure 1: Importance of sustainability